Oesterreichische Nationalbank

78th East Jour Fixe

The current IMF program: Key aspects and implementation

Jerome Vacher
IMF Resident Representative in Ukraine

Vienna, February 26, 2016

Background: Years of unsustainable macroeconomic policies

A largely inadequate policy mix in previous years:

- Lack of structural reforms
- Large fiscal and quasi fiscal deficit
  - ➢ Absent any adjustment and based on budget adopted in Jan. 2014, combined deficit > 12 percent of GDP
- Fixed exchange rate
- Large current account deficit
- Low level of reserves

Strong commitment to new policies but impact of the conflict

Impact of the conflict and its intensification in the summer of 2014:

- Direct impact:
  - Real sector (industrial production, export, import)
  - Fiscal (revenues, expenditures)
  - Financial sector and demand for Fx
- Most important: impact on confidence (domestic, external)

A new IMF supported program

Moving from a Stand By Arrangement to an Extended Fund Facility:

- 4 year arrangement (instead of 2 years)
- Longer repayment period
- Focus on structural reforms
- Frontloaded:
  - 1st tranche: 5 bn USD (of which 2.7 bn USD in budget support)
  - 2nd tranche: 1.7bn USD

5 key areas

1. Exchange rate and monetary policies
2. Financial sector stabilization and reform
3. Fiscal adjustment
4. Energy sector reform
5. Structural reforms

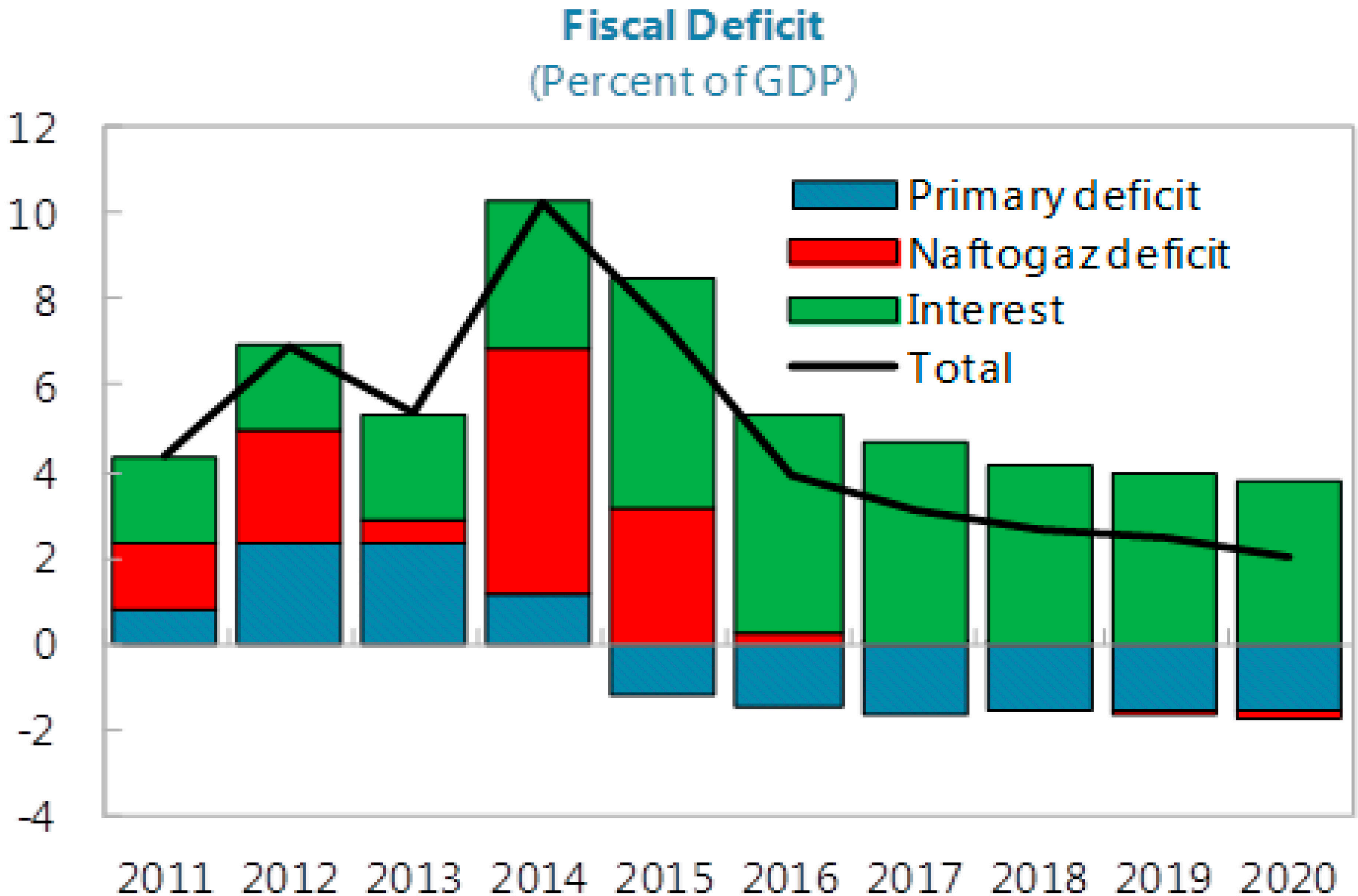
Fx and monetary policies

1. Maintain a flexible exchange rate to restore competitiveness and foster accumulation of reserves
2. Focus monetary policy on domestic price stability
3. Prepare to move to inflation targeting

Fiscal adjustment

- Enhanced revenues and collections
  - Higher excises, Social Security Contribution reform
  - Closing of tax loopholes, including in agriculture
  - Revenue administration reform
- Contained expenditure growth
  - Pension reform
- Reallocation of expenditures

Fiscal adjustment



Sources: Ukrainian authorities and staff calculations.

An important milestone in debt operation has been reached

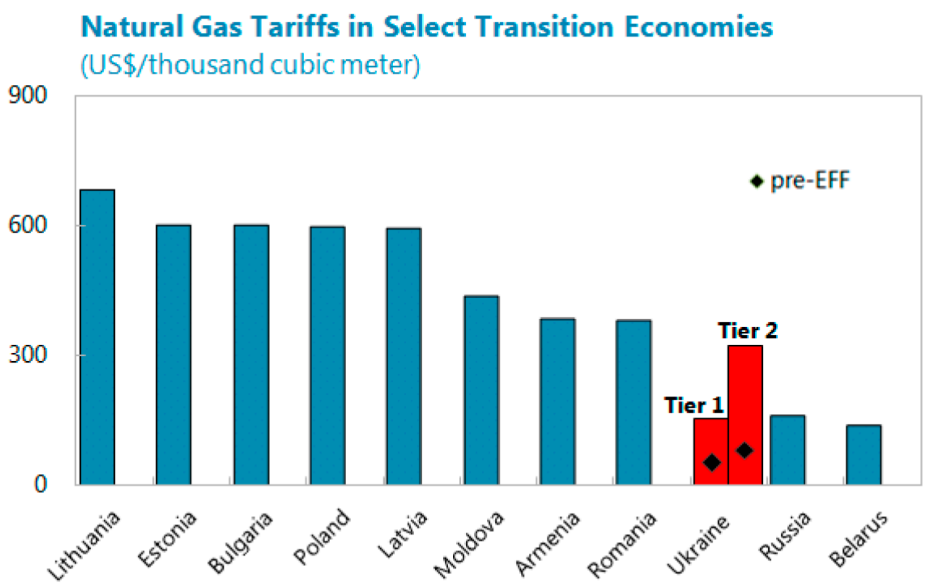
The agreement with the committee of creditors satisfies the three objectives for the debt operation set by the IMF for the debt operation:

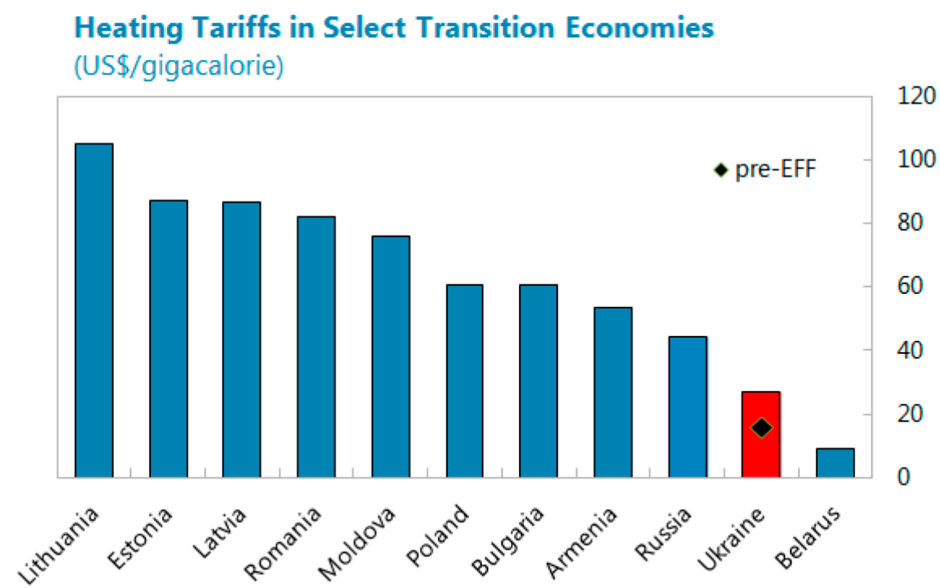
- Reduce annual post-program gross financing needs
- Place public debt on a downward path
- Provide targeted external debt service relief

Energy sector reform

1. Increased gas and heating tariffs over time towards cost recovery
2. Accompanied by enhanced sustainable social assistance measures to mitigate the impact on the poorest (means-tested subsidies)
3. Improvements in governance and transparency
4. Strengthening of payment discipline

Energy tariff increase





Source: Ukrainian authorities; Eurostat; WB and IMF staff estimates; www.energy.eu; www.euroheat.org.

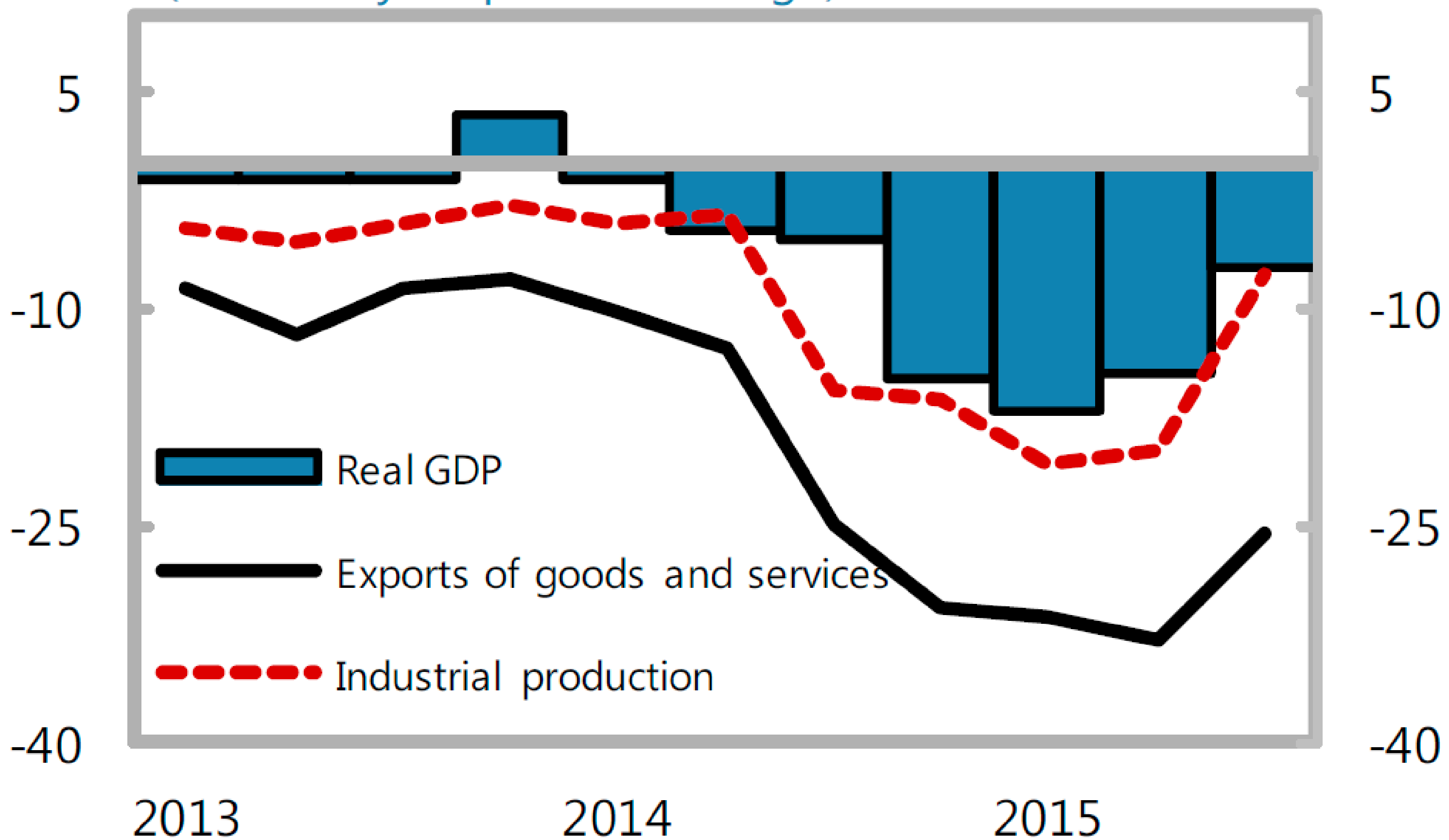
Improvements in governance are critical

- National Anti Corruption Bureau
- AML and asset disclosure
- Improvement of the business climate and deregulation
- Effectiveness of the judiciary
- Reform of state owned enterprises, governance and privatization

Real sector indicators

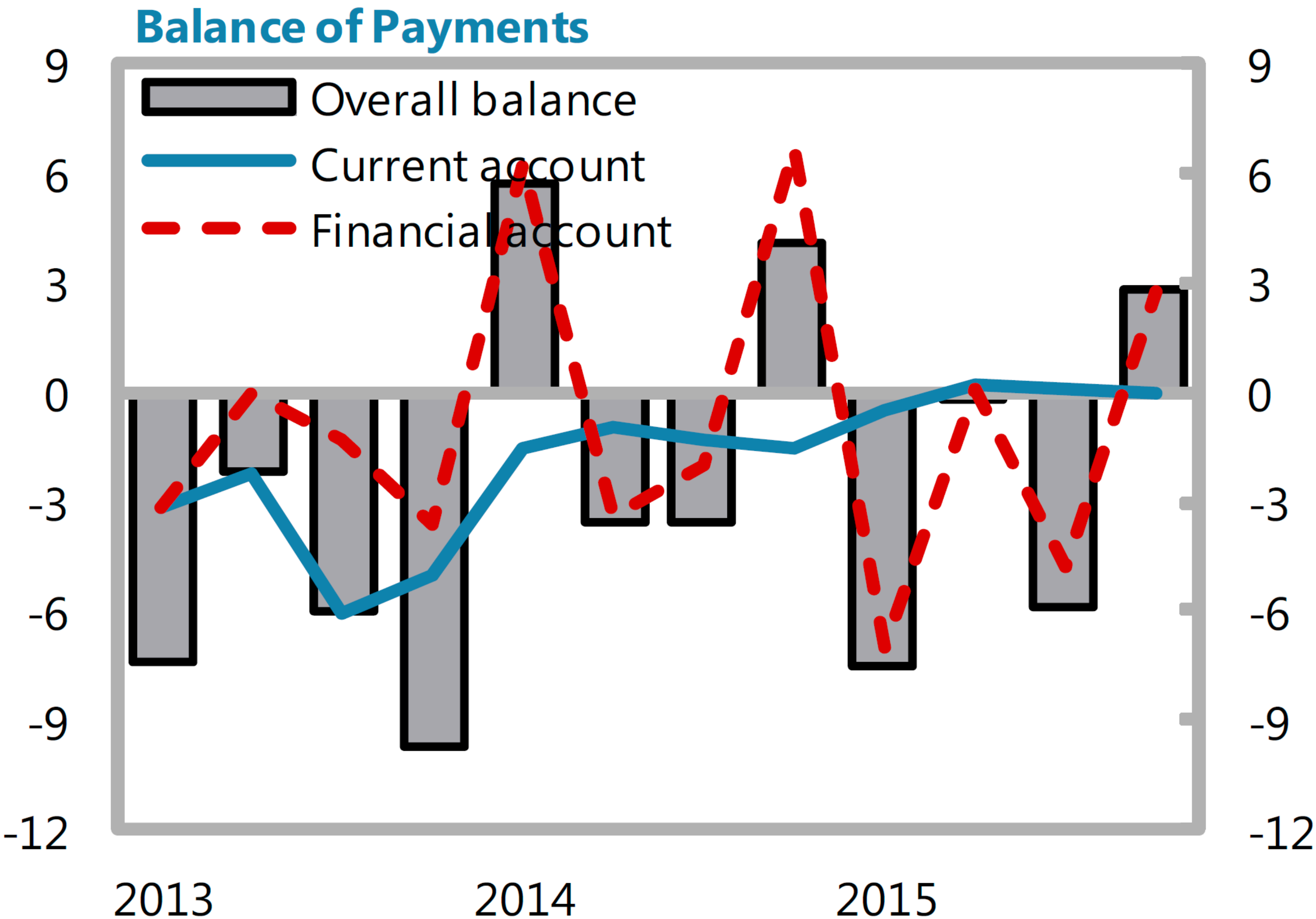
The recovery is gradual and fragile:

Real GDP, Exports, and Industrial Production
(Year-on-year percent change)



External sector developments

The external imbalances have narrowed:



However, risks remain on the downside

1. Program ownership, domestic politics and policy slippages
2. Global environment
3. Extension or worsening in geopolitical and trade tensions
   - Tensions in the East and relations with Russia
4. Financial sector risks
5. Financing

Conclusions

- A critical and challenging reform program for Ukraine: rebuilding confidence and institutions
- Commitment, program ownership and maintaining the reform momentum will continue to be key
- Stepping up anti-corruption efforts is critical
- Vested interests should not have the control of economic policies

Conclusions

- Support of reforms by the international community also fundamental
- Crisis should be used as a unique opportunity to reform
- Return to growth might be slow, important to show short term decisive gains (e.g. anti-corruption) and medium term path to the population

More information at

The IMF Resident Representative Office in Ukraine Website

http://www.imf.org/external/country/UKR/rr/index.htm

Thank you!