MARKET REVIEW: UKRAINE

A NATION UNBOWED

In 2023, Ukraine's economy began to recover from the full-scale war's initial impact as the country found ways to adapt where possible, including a metals and mining industry that was adjusting to operate amid the prevailing constraints.

A NASCENT ECONOMIC RECOVERY

In 2023, Ukraine's economy delivered a significant rebound in GDP amid the ongoing full-scale war. The front lines remained relatively static during the year, with fighting concentrated in the southern and eastern regions of the country. Importantly, in the second half of the year, the country managed to achieve strategic successes, including establishing a navigation corridor for broader exports and imports through the Black Sea and the continued support of Ukraine's allies for its defence efforts. These developments, along with stabilised international reserves and a substantial reduction in inflation, highlighted an economy adapting to wartime conditions, albeit with the understanding that circumstances could change quickly.

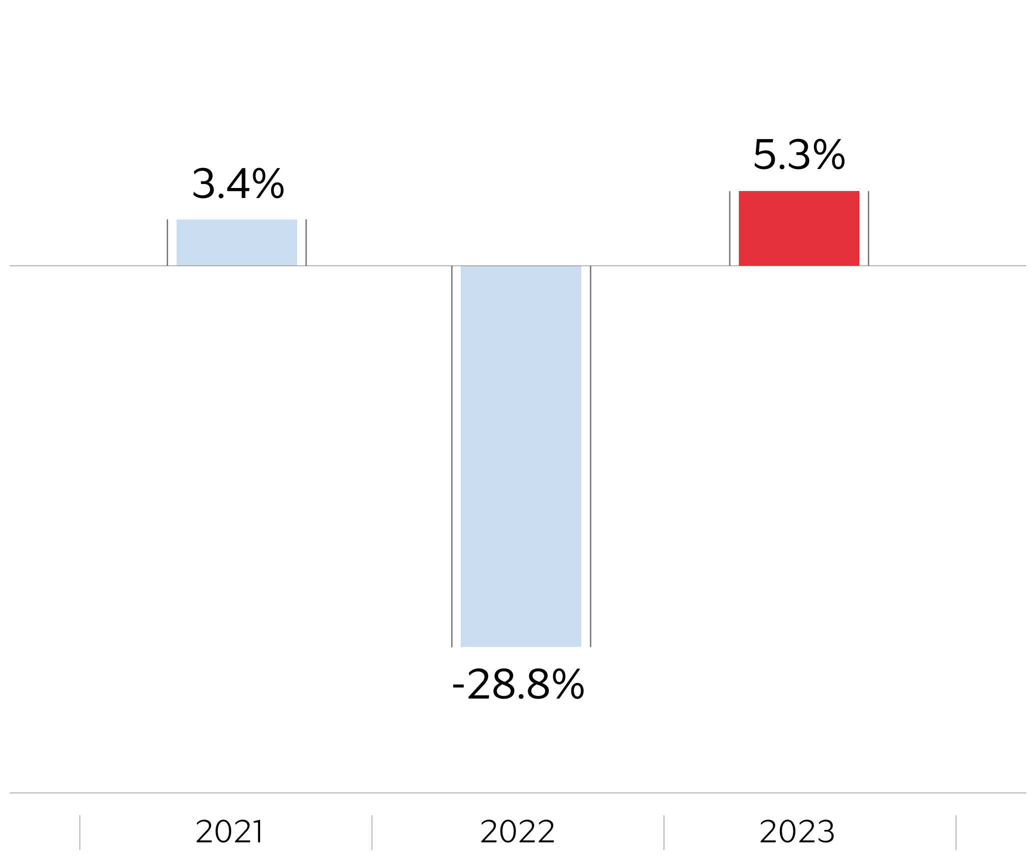
None of these achievements should obscure the challenges facing the country's economy. Millions of Ukrainians remained unable to return to their homes because of the war's impact. As of the year-end, an estimated 3.7 million people[1] continued to be internally displaced, while more than 6.5 million were still recorded as refugees in other countries[2].

Following Russia's withdrawal from the Grain Deal in July 2023, Ukraine's defence forces were able to push the aggressor's navy far enough away to establish a maritime corridor, opening the possibility for exports and imports without being restricted to grains. Despite the reopening of Ukraine's Black Sea navigation, its exports of goods fell further in 2023 because of a high base for comparison due to pre-war exports in 2022, drops in export product prices and logistical bottlenecks at the land border with Poland.

Overall, in 2023, real GDP rose by 5.3% year-on-year from the low base of 2022, when it fell by 28.8%. Nominal GDP rebounded to US$179 billion[3], up from US$162 billion[3] in 2022.

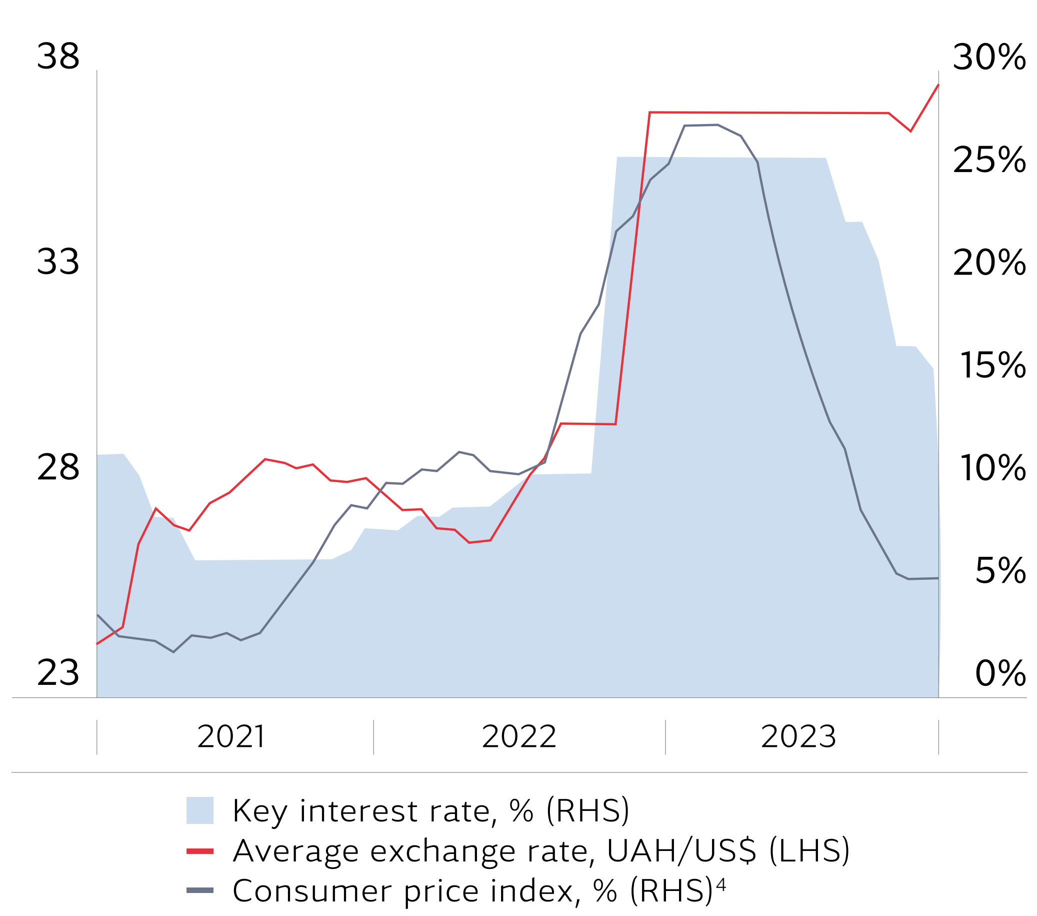
The expenditure components of GDP increased year-on-year for gross fixed investments by 52.9%[3], for government consumption by 9.0%[3], and for household consumption by 6.3%[3], while exports decreased by 5.4%[3] and imports increased by 8.5%[3].

REAL GDP DYNAMICS



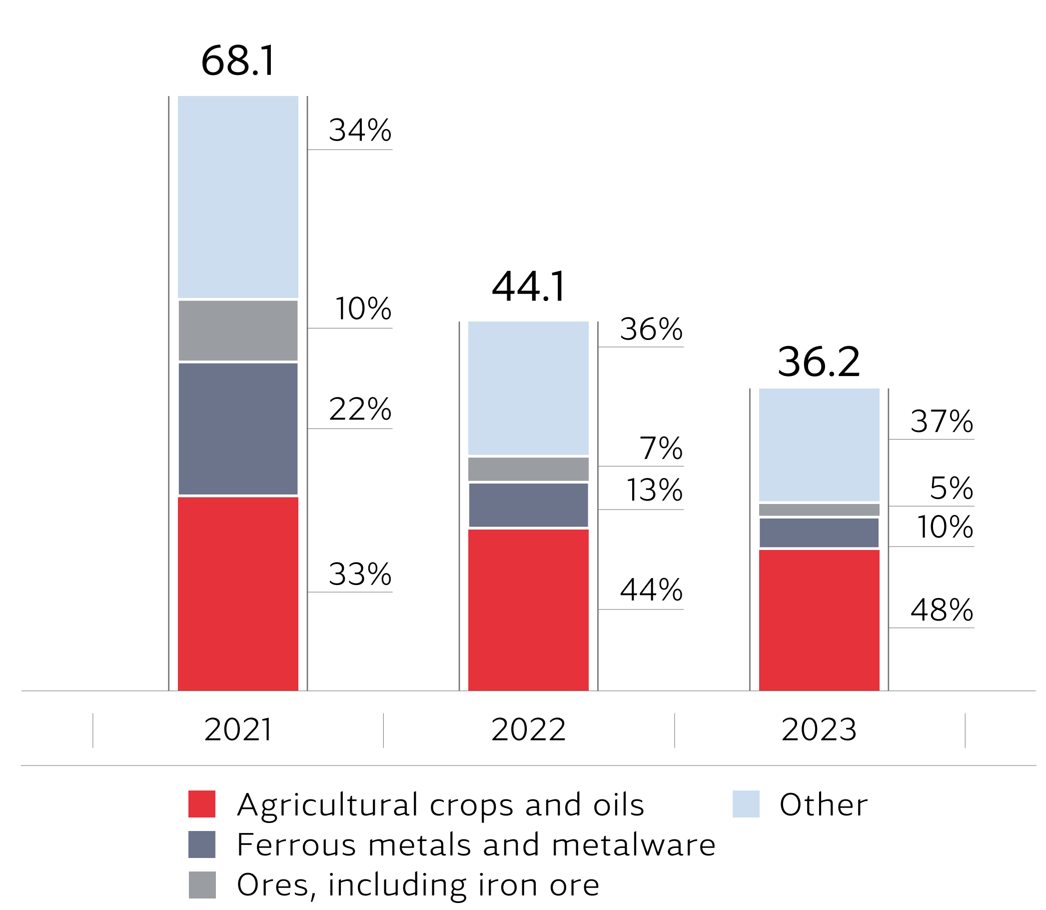
Source: State Statistics Service of Ukraine

MONETARY POLICY



Source: NBU, State Statistics Service of Ukraine

EXPORTS OF GOODS STRUCTURE, US$ BN



Source: State Statistics Service of Ukraine

[1] The UN International Organisation for Migration.
[2] The UN High Commissioner for Refugees.
[3] State Statistics Service of Ukraine.
[4] For CPI, the year-on-year change is for the individual monthly periods.

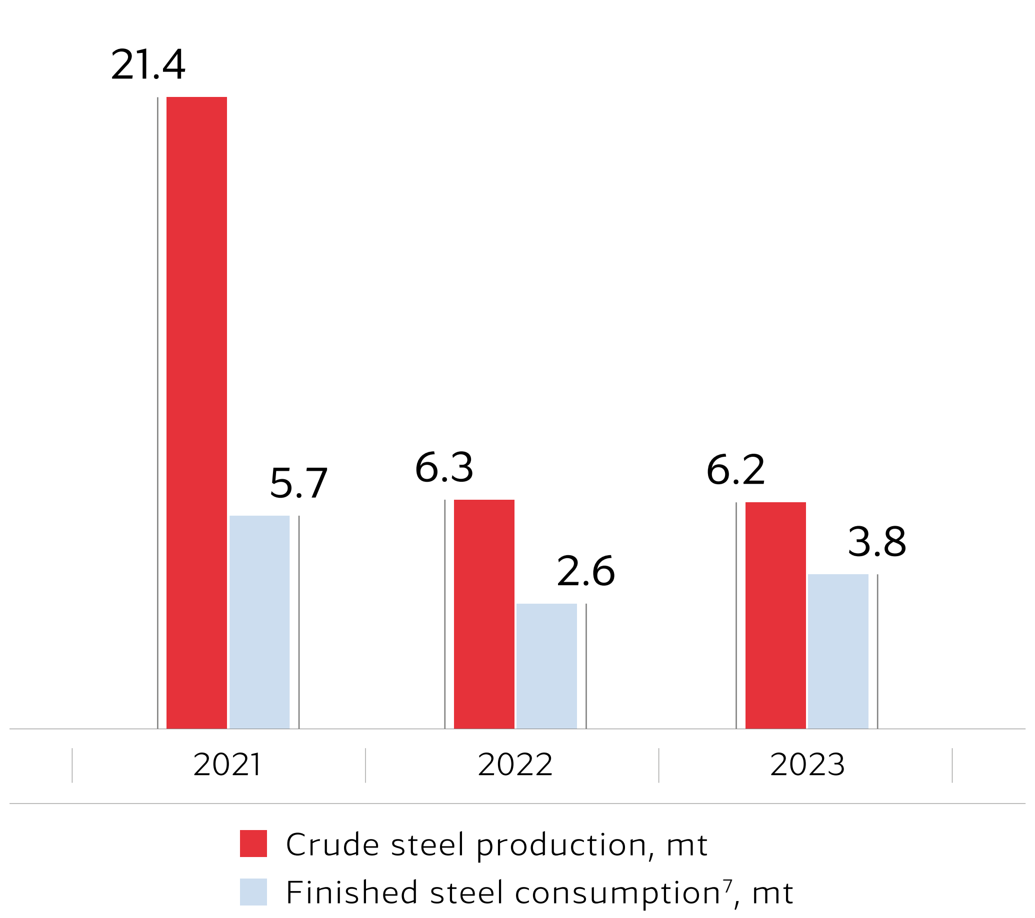
The increase in the production components of GDP was led by public administration (5.8%[3]), manufacturing (13.8%[3]), wholesale and retail trade (6.6%[3]) and agriculture (7.6%[3]).

Ukraine's industrial production rose by 6.8%[3] year-on-year in 2023, whereas the output of iron, steel and ferroalloys edged down by 0.6%. Larger year-on-year declines were reported for 2023 in coal mining (3.0%) and metal ore mining (10.2%), as well as in coke production (13.5%). However, oil and natural gas extraction was unchanged year-on-year in the reporting period.

Economic stabilisation was also seen in the year's inflation trends. The annual CPI fell from 20.2%[3] year-on-year in 2022 to 12.9%[3] in 2023, while the end-of-period CPI shrank from 26.6% in December 2022 to just 5.1% in December 2023. The National Bank of Ukraine (NBU) also began to ease its monetary policy through several rounds of key policy rate reductions from a nearly seven-year high of 25% at the end of 2022, to 15% at the end of 2023.

As Ukraine's economy started to adapt to the realities of war, certain of the associated regulatory changes were relaxed, including some of the NBU's currency controls.

STEEL INDUSTRY



Source: WSA, Metal Expert

In October 2023, the NBU introduced managed flexibility of the official exchange rate of the Ukrainian hryvnia. This represented a significant change in policy, narrowing the gap between the official and cash market rates. While the official rate had been pegged against the US dollar at 36.57 since July 2022, it stood at 37.98 as of the end of 2023. In 2023, the hryvnia's average official exchange rate to the US dollar was 36.57, a 12% weakening, compared with a 16% decline in 2022.

Ukraine remains highly dependent on external financing to cover government expenditures and the substantial cost of funding the national defence effort, while defence and security spending equalled roughly 67% of total budget expenditures in 2023[5]. The state budget deficit reached a record high for the second consecutive year, up from US$28.3 billion[5] in 2022 to US$36.4 billion[5] in 2023. Ukraine's international partners provided an unprecedented level of monetary support during the year, helping to cover the cost of running and defending the country. In 2023, Ukraine received a total of US$42.5 billion in financial assistance, including US$19.5 billion from the EU, US$11.0 billion from the US, US$4.5 billion from the IMF and US$1.8 billion from Canada[5].

International aid remained the primary source of capital inflows and helped to boost the NBU's international reserves at the end of 2023 by 42.2% year-on-year to US$40.5 billion, US$11.4 billion above the pre-war level. At the end of 2023, Ukraine's public debt totalled US$145 billion, compared with US$111 billion at the end of 2022. As a result of the significant rise in debt, the ratio of public debt to GDP increased further from 78% in 2022 to 84% in 2023.

During the reporting period, S&P and Moody's made downward adjustments to their sovereign credit ratings for Ukraine. As of 31 December 2023, S&P had a rating of 'CCC', the outlook 'negative'; Moody's rating was 'Ca', the outlook 'stable'; and Fitch's assessment stood at 'CC'.

TOUGHENED THROUGH HARDSHIP

While Ukraine's steel industry faced significant challenges going into the year amid continued blackouts, the stabilisation of power supplies in the first quarter of 2023 partially enabled an increase in production. As the industry started to adapt to operating under wartime conditions, the capacity utilisation of steelmaking plants in operation located in territory under Ukrainian government control recovered to around 40% by the year-end from around 20% a year earlier[6].

Throughout most of the year, the blockade of Ukraine's ports on the Black Sea left rail logistics as the key bottleneck constraining steel output. In autumn 2023, the Ukrainian military restored a corridor for maritime navigation, enabling the resumption of seaborne trade. However, this came too late in the year to have a material impact in the reporting period.

Overall, domestic steelmakers produced 6.2 million tonnes of crude steel in 2023, down 0.6% year-on-year. Metinvest's crude steel output decreased by 30.6% year-on-year to 2.0 million tonnes as a consequence of the temporary occupation of Mariupol and suspension of production at its steelmakers in that city. Increased production at Kamet Steel partly compensated for this loss in capacity. Ukraine's apparent steel consumption (excluding pipes) jumped by 45.8% year-on-year to 3.8 million tonnes.

During the reporting period, logistical and infrastructural constraints continued to limit iron ore production. Ukraine's merchant iron ore product output totalled 28.8 million tonnes in 2023, down 3.7% year-on-year, according to the Group's estimates based on Ukrainian Industry Expertise (UEX) data. Meanwhile, Metinvest's total iron ore concentrate output grew by 3.5% year-on-year to 11.1 million tonnes.

In 2023, Ukrainian mining companies exported 19.0 million tonnes of iron ore, down 9.6% year-on-year, with European countries being the main importers. Following the restoration of Black Sea navigation, China reemerged as a key destination for Ukrainian iron ore by the end of the year.

DEVELOPMENTS AFTER THE REPORTING PERIOD

In 2024, the Russian military maintained its offensives. Its aerial strikes have persistently targeted Ukraine's energy and civilian infrastructure beyond the front lines. Ukraine lost significant amounts of its thermoelectric and hydroelectric generating capacities because of the renewal of targeted attacks.

Amid these challenges, the US approved a new support package for Ukraine in April 2024. It offers critical relief and bolsters the capacity of the country's defence forces to counteract the enemy's offensives more effectively. US Congressional approval of this aid was a critical demonstration of international support for Ukraine. Regarding Ukraine's budget, the NBU estimates[8] that Ukraine can count on US$38 billion in external support in 2024.

After Ukraine secured US support and had received US$10.6 billion of support in March-April from the EU, Canada, Japan, the UK and the IMF, the NBU eased some of its FOREX restrictions in early May 2024. Among other steps, the central bank allowed for repatriation of dividends earned from the beginning of 2024 (capped at EUR1 million per month).

The domestic steel industry has demonstrated resilience. In the first quarter of 2024, crude steel production in Ukraine totalled 1.7 million tonnes, up 37% year-on-year and 3% more quarter-on-quarter, according to WSA. Steel consumption in Ukraine amounted to 0.9 million tonnes in the first quarter of 2024, 25% more year-on-year, although it was down 11% quarter-on-quarter, according to Metal Expert. The reopening of Ukraine's Black Sea corridor for effectively unlimited commercial navigation boosted Ukraine's iron ore industry: in the first quarter of 2024, iron ore production rose 92% year-on-year to 11.8 million tonnes while exports increased 138% to 9.7 million tonnes, according to the Group's estimates based on UEX data.

[5] Ministry of Finance of Ukraine.
[6] WSA, Metal Expert, Ukrmetalurgprom, Metinvest estimates
[7] Consumption in Ukraine includes flat, long and certain semi-finished products, but excludes pipes.
[8] NBU's Inflation Report, April 2024.