

Yakiv Smolii: The National Bank of Ukraine's key achievements in 2018 and action plan for 2019

Speech by Mr Yakiv Smolii, Governor of the National Bank of Ukraine, at the opening of the meeting of the National Bank of Ukraine with stakeholders, Kiev, 16 January 2019.

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Dear Colleagues,

I am pleased to welcome you, our partners and clients, those for whom we work, those whom we regulate, and those with whom we cooperate, here in the National Bank of Ukraine.

Our policy is built on dialogue, which lays the foundation of our success as a central bank. Low and stable inflation, reliable, transparent, and sound banking system, developed financial markets, an investment climate that favors economic growth and widens the international horizon – all of these are our objectives. That is why it is important for us not only to be heard, but also to receive feedback from our stakeholders.

Today, we will summarize the economic and financial results of 2018, share the NBU's action plan for 2019, determine the main challenges for the Ukrainian economy, and discuss the development potential of the economy and the financial system.

The year 2018 was marked by a recovery of macrofinancial stability to the level seen before the annexation of Crimea and the Donbas conflict.

Last year was a year of many peaks and records.

In 2018, the economy of Ukraine demonstrated **the most rapid growth in the past seven years**. Real GDP grew 2.8% over three quarters and the full-year economic growth was 3.4% according to the NBU forecast.

Despite having exceeded the NBU target, year-end inflation returned to the downward trend and **has declined to a single-digit value for the first time over five years, coming in at 9.8%**.

As a result, today we see:

- ♦ lower underlying inflationary pressures on the economy of Ukraine
- ♦ a more comfortable business environment and an increase in household savings
- ♦ inflation gradually approaching our medium-term target of 5%.

This is primarily **the result of the NBU's tight monetary policy**.

The gradual increase in the key policy rate began in October 2017 prompted by heightened inflation risks. In 2018, we raised the key policy rate four times, by a total of 3.5 pp to the current level of 18.0% per annum, in order to bring inflation down to the target over the medium term.

This pushed up deposit interest rates, thus making savings more attractive.

Thanks to the tight monetary policy as well as the benign global price environment for Ukrainian exports in the first half of the year, and the record harvest of grain crops in the second half of 2018, **the hryvnia strengthened by 1.4% over the year**.

This is the sign of stabilization in the foreign exchange market of Ukraine. At the same time, Ukrainians now trust the NBU's ability to smooth out excessive market fluctuations. This is proven by the fact that even Russian aggression in the Kerch Strait and the imposition of the

martial law have not caused any major panic on the foreign exchange market. We highlighted developments on the foreign exchange market and continued to be active in the market, thus preventing panic among market participants and households.

The stronger hryvnia allowed the NBU to increase international reserves throughout the year by purchasing foreign currency on the interbank market.

External financing became another source: Ukraine received **a new program of cooperation with the IMF**, which lays the groundwork for further strengthening of macrofinancial stability. As a result, USD 2.4 billion was added to the reserves by international partners (the IMF, the EU and the World Bank).

The resulting amount of **international reserves is the highest in five years**, at USD 20.8 billion. The last time we saw such figures was in the fall of 2013.

The financial sector is showing good performance as well. **The banking system is not only resilient, capitalized, and transparent, but also profitable – for the first time in five years.**

Consumer confidence in the banking system is on the rise. Hryvnia household deposits increased 15% last year.

Banks are finally doing more lending, with hryvnia household loans up 31% last year.

In addition, we can currently talk about a certain recovery in corporate lending.

Our priorities in achieving these results were identified by the NBU's Medium-Term Strategy. Approved and unveiled in the spring of 2018, the Strategy identifies seven key goals of the NBU:

1. Low and stable inflation.
2. Stable, transparent, and effective banking system.
3. Resumption of lending.
4. Effective regulation of the financial sector.
5. Free flow of capital.
6. Financial inclusion.
7. Modern, open, independent, and effective central bank.

The NBU's activities aimed at achieving these goals were what made possible the comforting highs and record-high figures of 2018.

We will continue to work to ensure price and financial stability as a foundation for sustainable economic growth.

We begin the year 2019 with a revolutionary currency liberalization the likes of which Ukraine has never seen. In less than a month, the *Law On Currency and Currency Operations* and our new currency regulation will go into effect, significantly easing currency transactions for households and businesses. The new legislation is going to actually work in practice rather than remaining just words on paper.

But with extended freedom comes extended responsibility. The more liberal the conditions that financial market participants, businesses, and households enjoy, the more attention we at the NBU have to pay to financial stability.

Thus, we should devote the current year to the next important step without which no financial stability is possible within either the banking sector or the entire financial system. And by this I mean the “split,” which is something that stands to shape the future of the nonbank financial sector.

It is not for nothing that the planned adoption of the bill on the “split” by the Rada has become one of the structural milestones in the new program of cooperation between Ukraine and the IMF as a prerequisite for strengthening the financial sector. The new law will bring the nonbank financial market in alignment with European standards, enhance the quality of financial companies’ operation, protect financial service consumers, and encourage the arrival of new international players in this market by creating the right conditions.

In addition, 2019 should become an important year for a further recovery in lending. Despite the progress made over the past two years, banks have yet to become fully operational, especially as regards working with large corporate borrowers and making mortgage loans to households.

A more active recovery in lending is currently impeded by the high level of nonperforming loans. The market is waiting for the Verkhovna Rada to consider and adopt a bill on asset resolution activities that has been prepared by the EBRD. The new law will pave the way for the operation of asset resolution companies and ensure the creation of an adequate competitive environment in Ukraine’s secondary market for loans.

In addition, significant institutional risks are still there, and the reform of the judiciary is still pending implementation. Completion of the reform would ensure the strict observance of laws and protection of creditor rights.

It goes without saying that we cannot, on our own, travel all the way to a sustainable economy and a developed and stable financial system. Doing so requires that **the NBU operate in conjunction with you: banks, businesses, government agencies, the expert community, and the media.**

We can now talk about the challenges that lie ahead and how we can best meet them – in a joint effort.

I wish you an interesting and fruitful discussion!