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## Winds of Change

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### EXECUTIVE SUMMARY

With Yulia Tymoshenko narrowly elected prime minister and her first premier Alexander Turchynov in place, the first half of December saw several key political advances.

Tymoshenko's early challenges will be to keep her Orange coalition together, while restraining her populist tendencies and advancing approval of the 2008 budget. Despite government promises, we think the budget is unlikely to be approved this year.

Though the growth is slowing, its 7.2% annualized rise over the first 11 months of the year is still running well above official expectations. Traditionally market services and manufacturing supported real sector growth.

But inflation continued to speed up, with CPI running 14.2% by the end of November, driven by expensive food and rising tariffs.

In an effort to slow prices rises, the Central Bank tightened monetary policy by increasing rates and mobilizing transactions. But the effect of these measures was muted by the de facto fixed exchange rate policy: in November the Bank bought additional \$479 million in currency, increasing gross reserves to \$32.8 billion, or 5.6 months of imports.

Tymoshenko revived revaluation expectations; although the head of the Central Bank already announced an intent to strengthen the currency, Tymoshenko followed this by stating that the hryvnia would move to 4.9 to the U.S. dollar, from its longtime 5.05.

Evrast Group, Russia's second-largest steelmaker, agreed to acquire six metallurgy companies of Ukrainian industrial group Privat. Evrast paid \$3.8 billion: \$1 billion in cash, plus 10.6% of its shares.

Ukraine's prospects for WTO entry were delayed, after the EU made additional demands. A further meeting of the Ukraine working group is now expected in the second half of January.

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