

State enterprise

“FINANCING OF INFRASTRUCTURAL PROJECTS”

(incorporated as a state enterprise under the laws of Ukraine)

U.S.\$568,000,000

8.375 per cent. Guaranteed Notes due 2017

guaranteed by

**The Cabinet of Ministers of Ukraine (acting on behalf of Ukraine)
represented by the Minister of Finance of Ukraine**

The reoffer price to investors of the U.S.\$568,000,000 8.375 per cent. Guaranteed Notes due 2017 (the “Notes”) of the State enterprise “FINANCING OF INFRASTRUCTURAL PROJECTS” (the “Issuer”) is 101.448 per cent. of their principal amount. Unless previously purchased, redeemed or cancelled, the Notes will be redeemed at their principal amount on 3 November 2017.

The Notes will bear interest from 3 November 2010 at the rate of 8.375 per cent. per annum payable semi-annually in arrear on 3 May and 3 November each year commencing on 3 May 2011. Payments on the Notes will be made in U.S. dollars without deduction for or on account of taxes imposed or levied by Ukraine to the extent described under “*Terms and Conditions of the Notes—Taxation*”. The Cabinet of Ministers of Ukraine (acting on behalf of Ukraine) represented by the Minister of Finance of Ukraine (the “Guarantor”) will unconditionally and irrevocably guarantee the payment of all amounts at any time becoming due and payable in respect of the Notes.

SEE “RISK FACTORS” FOR A DISCUSSION OF CERTAIN FACTORS TO BE CONSIDERED IN CONNECTION WITH AN INVESTMENT IN THE NOTES ON PAGES 8 to 23.

The Notes and the Guarantee have not been and will not be registered under the United States Securities Act of 1933, as amended (the “Securities Act”), or with any securities regulatory authority of any State or other jurisdiction of the United States, and may not be offered or sold within the United States or to, or for the account or benefit of, any U.S. person except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act.

The Notes and the Guarantee will be offered and sold (i) outside the United States to persons that are not U.S. persons in reliance on Regulation S and (ii) within the United States in reliance on Rule 144A under the Securities Act (“**Rule 144A**”) only to persons who are both (a) “qualified institutional buyers” (each a “**QIB**”) within the meaning of Rule 144A and (b) “qualified purchasers” (each a “**QP**”) within the meaning of Section 2(a)(51)(A) of the United States Investment Company Act of 1940, as amended (the “**Investment Company Act**”), and the rules and regulations thereunder, in each case acting for their own account or for the account of one or more QIBs who are also QPs. Each purchaser of the Notes in making its purchase will be deemed to have made certain acknowledgements, representations and agreements. Prospective purchasers are hereby notified that the sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A. For a summary of certain restrictions on resale, see “*Subscription and Sale*” and “*Forms of Notes and Transfer Restrictions*”.

The Notes will be offered and sold in registered form in denominations of U.S.\$100,000 and integral multiples of U.S.\$1,000 in excess hereof. Notes which are offered and sold in reliance on Regulation S (collectively, the “**Unrestricted Notes**”) will each be represented by beneficial interests in a global Note (each, an “**Unrestricted Global Note**”) in registered form without interest coupons attached, which will be registered in the name of The Bank of New York Depository (Nominees) Limited, as nominee for, and shall be deposited on or about 3 November 2010 (the “**Closing Date**”) with, The Bank of New York Mellon, as common depository (the “**Common Depository**”) for, and in respect of interests held through, Euroclear Bank S.A./N.V. (“**Euroclear**”) and Clearstream Banking, société anonyme, Luxembourg (“**Clearstream, Luxembourg**”). Notes that are offered and sold in reliance on Rule 144A (collectively, the “**Restricted Notes**”) will each be represented by beneficial interests in a global Note (each, a “**Restricted Global Note**”) and, together with the Unrestricted Global Notes, the “**Global Notes**”) in registered form without interest coupons attached, which will be deposited on or about the Closing Date with a custodian (the “**Custodian**”) for, and registered in the name of Cede & Co. as nominee for, The Depository Trust Company (“**DTC**”). Interests in the Restricted Global Notes will be subject to certain restrictions on transfer. Beneficial interests in the Global Notes will be shown on, and transfers thereof will be effected only through, records maintained by DTC, Euroclear and Clearstream, Luxembourg and their participants. Except as described herein, certificates will not be issued in exchange for beneficial interests in the Global Notes.

The Prospectus has been approved by the Central Bank of Ireland (the “**Central Bank**”), as competent authority under Directive 2003/71/EC (the “**Prospectus Directive**”). The Central Bank only approves this Prospectus as meeting the requirements imposed under Irish and EU law pursuant to the Prospectus Directive. This Prospectus constitutes a “Prospectus” for the purposes of the Prospectus Directive. Application has been made to the Irish Stock Exchange for the Notes to be admitted to the official list (the “**Official List**”) and trading on its regulated market (the “**Market**”). The Market is a regulated market for the purposes of Directive 2004/39/EC (the “**Markets in Financial Instruments Directive**”).

Lead Manager

MORGAN STANLEY

1 November 2010

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CERTAIN IMPORTANT INFORMATION

Except for the Guarantor Information (as defined below), the Issuer accepts responsibility for the information contained in this Prospectus. To the best of the knowledge of the Issuer (having made all reasonable enquiries and having taken all reasonable care to ensure that such is the case) the information contained in this Prospectus, aside from the Guarantor Information (as defined below), is in accordance with the facts and does not omit anything likely to affect the import of such information.

The Guarantor accepts responsibility for the information with respect to it and Ukraine, including but not limited to the information in the sections entitled “Risk Factors Relating to the Guarantor”, “Description of the Guarantor”, “Political Framework”, “Economy of Ukraine”, “The Labour Market”, “External Sector”, “Public Finance and Fiscal Policy”, “Public Debt”, “The Monetary System”, and “The Banking System and Securities and Financial Services Markets in Ukraine” (the “**Guarantor Information**”) contained in this Prospectus. To the best of the knowledge of the Guarantor (having made all reasonable enquiries and having taken all reasonable care to ensure that such is the case) the Guarantor Information contained in this Prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information.

Neither the Issuer nor the Guarantor has authorised the making or provision of any representation or information regarding the Issuer, the Guarantor or the Notes other than as contained in this Prospectus or as approved for such purpose by the Issuer or the Guarantor, as the case may be. Any such representation or information should not be relied upon as having been authorised by the Issuer or the Guarantor. The delivery of this Prospectus shall not, under any circumstances, constitute a representation or create any implication that there has been no change in the affairs of the Issuer or the Guarantor since the date hereof. This Prospectus may only be used for the purpose for which it has been published.

The Issuer has confirmed to the Lead Manager named under “*Subscription and Sale*” below (the “**Lead Manager**”) that this Prospectus contains all information regarding the Issuer and the Notes which is (in the context of the issue of the Notes) material; such information is true and accurate in all material respects and is not misleading in any material respect; any opinions, predictions or intentions expressed in this Prospectus on the part of the Issuer are honestly held or made and are not misleading in any material respect; this Prospectus does not omit to state any material fact necessary to make such information, opinions, predictions or intentions (in such context) not misleading in any material respect; and all proper enquiries have been made to ascertain and to verify the foregoing.

The Guarantor has confirmed to the Lead Manager that this Prospectus contains all information regarding the Guarantor and the Guarantee which is (in the context of the giving of the Guarantee) material; such information is true and accurate in all material respects and is not misleading in any material respect; any opinions, predictions or intentions expressed in this Prospectus on the part of the Guarantor are honestly held or made and are not misleading in any material respect; this Prospectus does not omit to state any material fact necessary to make such information, opinions, predictions or intentions of the Guarantor (in such context) not misleading in any material respect; and all proper enquiries have been made to ascertain and to verify the foregoing.

No representation, warranty or undertaking, express or implied, is made, and no responsibility or liability is accepted by the Lead Manager nor any of its respective affiliates as to the accuracy or completeness of the information contained in this Prospectus or any other information provided by the Issuer and the Guarantor in connection with the Notes or their distribution. Neither the delivery of this Prospectus nor the offering, sale or delivery of any Note shall in any circumstances create any implication that there has been no adverse change, or any event reasonably likely to involve any adverse change, in the condition (financial or otherwise) of the Issuer or the Guarantor since the date of this Prospectus. The contents of this Prospectus are not to be construed as and should not be relied on as legal, business or tax advice. Each prospective investor should consult its own advisors for legal, business, tax and related advice regarding an investment in the Notes.

The distribution of this Prospectus and the offering, sale and delivery of Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Issuer, the

Guarantor and the Lead Manager to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers, sales and deliveries of Notes and on distribution of this Prospectus and other offering material relating to the Notes, see “*Subscription and Sale*” and “*Forms of Notes and Transfer Restrictions*”. Each recipient of this Prospectus shall be taken to have made its own investigation and appraisal of the condition (financial or otherwise) and status of the Issuer.

The Notes and the Guarantee have not been approved or disapproved by the U.S. Securities and Exchange Commission, any State securities commission in the United States or any other U.S. regulatory authority, nor have any of the foregoing authorities passed upon or endorsed the merits of the offering of the Notes or the accuracy or adequacy of this Prospectus. Any representation to the contrary is a criminal offence in the United States.

In this Prospectus, unless otherwise specified, references to a “**Member State**” are references to a Member State of the European Economic Area, references to the “**State**” are to the government of Ukraine, references to “**U.S. \$**”, “**U.S. dollars**” or “**dollars**” are to United States dollars and references to “**Hryvnia**”, “**UAH**” are to Ukrainian Hryvnia. References to “**billions**” are to thousands of millions.

Certain figures included in this Prospectus have been subject to rounding adjustments; accordingly, figures shown for the same category presented in different tables may vary slightly and figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

NOTICE TO NEW HAMPSHIRE RESIDENTS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENCE HAS BEEN FILED UNDER CHAPTER 421 B OF THE NEW HAMPSHIRE REVISED STATUTES (“RSA 421-B”) WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

FORWARD LOOKING STATEMENTS

Some of the statements contained in this Prospectus, as well as written and oral statements that the Issuer and the Guarantor and their respective representatives make from time to time in reports, filings, news releases, conferences, teleconferences, web postings or otherwise, are or may be deemed to be forward looking statements. Statements that are not historical facts, including, without limitation, statements about the Issuer’s and the Guarantor’s beliefs and expectations, are forward looking statements. These statements are based on current plans, objectives, assumptions, estimates and projections. Therefore, undue reliance should not be placed on them. Forward looking statements speak only as of the date on which they are made and neither the Issuer nor the Guarantor undertakes any obligation to update publicly any of them in light of new information or future events. Forward looking statements involve inherent risks and uncertainties. The Issuer and the Guarantor caution that a number of important factors could cause actual results to differ materially from those contained in any forward looking statement. Forward looking statements include, but are not limited to: (i) plans with respect to the implementation of economic policy, including privatisations, and the pace of economic and legal reforms; (ii) expectations about the behaviour of the economy if certain economic policies are implemented; (iii) the outlook for inflation, exchange rates, interest rates, foreign investment, trade and fiscal accounts; and (iv) estimates of external debt repayment and debt service.

In addition to the factors described in this Prospectus, including, but not limited to, those discussed under “*Risk Factors*”, the following factors, among others, could cause future results to differ materially from those expressed in any forward looking statements made herein: (i) decisions of international organisations, such as the IMF, regarding the terms of their financial assistance to Ukraine and accordingly the net cashflow to or from such international organisations over the life of the Notes; (ii) adverse external factors, such as higher international interest rates, low commodity prices or recession or low growth in Ukraine’s trading partners or increases in world oil and gas prices, which could each decrease Ukraine’s fiscal and foreign exchange revenues and could negatively affect the current account, balance of payments and international reserves and cause or contribute to recession or low growth in Ukraine; (iii) adverse domestic factors, such as recession, declines in foreign direct investment (“**FDI**”) and portfolio investment, high domestic inflation, high domestic interest rates, exchange rate volatility, a reduction in gas supplies, difficulties in borrowing in the domestic and foreign markets, trade and political disputes between Ukraine and its trading partners, including Russia, political uncertainty or lack of political consensus, which could each lead to lower growth in Ukraine and lower international currency reserves; (iv) decisions of Ukraine’s official creditors, including the European Union (“**EU**”), Germany, the United States and Japan, regarding the provision of new loans following the implementation of the Paris Club debt rescheduling agreed in July 2001; (v) decisions of international financial institutions such as the IMF, the World Bank, the European Bank for Reconstruction and Development (the “**EBRD**”) and the European Investment Bank (the “**EIB**”) regarding the funding of new or existing projects over the life of the Notes; and (vi) political factors in Ukraine, which affect the timing and structure of economic reforms, the climate for FDI and the pace, scale and timing of privatisations.

OVERVIEW

This following general description of the Notes must be read as an introduction to the more detailed information appearing elsewhere in this Prospectus and any decision to invest in the Notes should be based on a consideration of the Prospectus as a whole and not solely on this summarised information. Words and expressions defined in the “Terms and Conditions of the Notes” below or elsewhere in this Prospectus have the same meanings in this summary.

Issuer:	State enterprise “FINANCING OF INFRASTRUCTURAL PROJECTS”.
Guarantor:	The Cabinet of Ministers of Ukraine (acting on behalf of Ukraine) represented by the Minister of Finance of Ukraine.
Risk Factors:	Investing in the Notes involves certain risks. The principal risk factors that may affect the abilities of the Issuer and the Guarantor to fulfil their respective obligations under the Notes are discussed under “ <i>Risk Factors</i> ” below.
Manager:	Morgan Stanley & Co. International plc.
Principal Paying Agent:	The Bank of New York Mellon.
Paying Agent:	The Bank of New York Mellon (Luxembourg) S.A.
Transfer Agent:	The Bank of New York Mellon. The Bank of New York Mellon (Luxembourg) S.A.
Trustee:	BNY Corporate Trustee Services Limited.
European Registrar:	The Bank of New York Mellon (Luxembourg) S.A.
New York Registrar:	The Bank of New York Mellon, New York Branch.
Irish Listing Agent:	Arthur Cox Listing Services Limited.
The Notes:	U.S.\$568,000,000 8.375 per cent. Notes due 2017.
Reoffer Price:	101.448 per cent. of the principal amount of the Notes.
Issue Date:	3 November 2010.
Use of Proceeds:	The proceeds from the issuance of the Notes will be used for the performance of tasks and actions provided by the “State Purpose Programme for the Preparation and Holding in Ukraine of the European Football Championship Finals in 2012” approved by the Resolution of the Cabinet of Ministers of Ukraine as of 14 April 2010 No. 357, specifically to finance the construction of stadia. Please refer to “Use of Proceeds”.
Interest:	The Notes will bear interest from (and including) 3 November 2010 at a rate of 8.375 per cent. payable semi-annually in arrear on 3 May and 3 November in each year commencing on 3 May 2011.
Listing and Trading:	Application has been made to the Irish Stock Exchange for the Notes to be admitted to the Official List and trading on its regulated market. The listing of the Notes and admission to

trading is expected to be effective on or about 3 November 2010.

Clearing Systems:	Euroclear Bank S.A./N.V., Clearstream Banking, <i>société anonyme</i> and/or The Depository Trust Company.
Form of Notes:	The Notes will be issued in registered form in the denomination of USD100,000 and integral multiples of USD1,000 in excess thereof.
Status of the Notes:	The Notes constitute direct, general and unconditional obligations of the Issuer which will at all times rank <i>pari passu</i> among themselves and at least <i>pari passu</i> with all other present and future unsecured obligations of the Issuer.
Status of the Guarantee:	The Guarantee constitutes direct, general and unconditional obligations of the Guarantor which will at all times rank at least <i>pari passu</i> with all other present and future unsecured and unsubordinated obligations of the Guarantor.
Final Redemption:	3 November 2017.
Redemption at the option of the Issuer (Issuer Call):	The Notes will be redeemable at the option of the Issuer on or after 3 November 2015 in whole, but not in part, at a redemption price per Note equal to the greater of (i) 102 per cent. of its principal amount plus accrued and unpaid interest, if any, to but excluding the date of redemption or (ii) as determined by an independent investment banker, the sum of the present values of its principal amount and the remaining scheduled interest payments thereon, in each case discounted to the date of redemption on a semi-annual basis at the Treasury Rate plus 0.50 per cent., plus accrued and unpaid interest, if any, to but excluding the date of redemption and any additional amounts payable in respect of the Notes. See Condition 5(d) (<i>Issuer Call</i>).
Negative Pledge:	The Notes will have the benefit of a negative pledge as described in Condition 3 (<i>Negative Pledge</i>).
Cross Default:	The Notes will have the benefit of a cross default as described in Condition 8 (<i>Events of Default</i>).
Taxation:	All payments in respect of the Notes will be made free and clear of withholding taxes of Ukraine, unless the withholding is required by law. For a description of taxes levied on the interest and other gains received by Noteholders in connection with the Notes see " <i>Taxation</i> " below.
Governing Law:	English law.
Selling Restrictions:	<p>For a description of certain restrictions on offers, sales and deliveries of Notes and on the distribution of offering material in the United States of America, the United Kingdom and Ukraine see "<i>Subscription and Sale</i>" below.</p> <p>The Issuer may compel any beneficial owner of an interest in the Restricted Notes to sell its interest in such Notes, or may sell such interest on behalf of such holder, if such holder is a U.S. person (as defined in Regulation S) that is not a QIB and a QP.</p>

RISK FACTORS

Prospective investors should read the entire Prospectus. Words and expressions defined in the “Terms and Conditions of the Notes” below or elsewhere in this Prospectus have the same meanings in this section. Investing in the Notes involves certain risks. Prospective investors should consider, among other things, the following:

Risk Factors Relating to the Issuer

The Issuer is a State Enterprise with no income of its own

The Issuer is a state enterprise, founded by the National Agency on Preparation and Holding in Ukraine of the UEFA Euro 2012. According to the Charter of the Issuer, the purpose of the activity of the Issuer is the procurement of additional (non-budget) funds of financing to facilitate the preparation and holding in Ukraine of the European Football Championship Finals in 2012 pursuant to the State Purpose Programme for the Preparation and Holding in Ukraine of the European Football Championship Finals in 2012, approved by the Resolution of the Cabinet of Ministers of Ukraine as of 14 April 2010 No. 357.

All funds raised by the Issuer are to be on-lent to NSC Olympic, Lviv Directorate (as these terms are defined below) and, possibly, other ultimate operating companies which are directly responsible for the implementation of the State Purpose Programme for the Preparation and Holding in Ukraine of the European Football Championship Finals in 2012. Repayment by the Issuer of principal, interest and/or additional amounts (if any) under the Notes is dependent on the Issuer actually receiving the funds from the State Budget or from the ultimate operating companies to which the funds raised by the Issuer were on-lent in the amounts equivalent to the sums of principal, interest and/or additional amounts (if any). Consequently, if the ultimate operating companies fail to meet their obligations to the Issuer in respect of the funds on-lent, or if the Issuer does not receive respective amounts of State Budget funds, the Noteholders could receive less than the full amount of principal, interest and/or additional amounts (if any) on the relevant due date from the Issuer and would have recourse under the Guarantee for the balance.

Further the State is the sole owner of the Issuer and thus exerts influence over the Issuer as an owner, and there can be no assurance that the State will not change its policies in respect of the Issuer or the conduct of its business (including replacing the Issuer’s management) in a manner which could negatively affect the Notes.

Risk Factors Relating to the Notes and the Guarantee

The Issuer and the Guarantor may be unable to repay the Notes at maturity

At maturity, the Issuer may not have the funds to fulfil its obligations under the Notes and the Guarantor may not have the funds to fulfil its obligations under the Guarantee and may not be able to arrange for additional financing.

Payments under the Notes could be made out of funds allocated from the State Budget pursuant to the procedure envisaged by the Budget Code of Ukraine and other laws of Ukraine. Such allocations require the approval of various State organs and there is a procedure in place on how these payments should be processed. Accordingly, the payments under the Notes due from the Issuer or the Guarantor (as a case may be) out of funds allocated from the State Budget, would be subject to such approvals (which remain at discretion of relevant organs) and compliance with the procedure.

The claims of Noteholders may be limited in the event that the Issuer is declared bankrupt

In the event of bankruptcy, Ukrainian bankruptcy law may materially affect the ability of the Issuer to make payments to the Noteholders or the Trustee.

In the event of bankruptcy of the Issuer, its obligations to the Noteholders would be subordinated, inter alia, to the following obligations:

- obligations secured by pledges/mortgages of the assets of the Issuer;
- expenditures associated with the conduct of bankruptcy proceedings, including severance pay;
- obligations arising as a result of inflicting harm to the life or health of individuals;
- payment of wages to the employees of the Issuer due as of the commencement of the bankruptcy procedure; and
- tax and mandatory payment obligations of the Issuer, etc.

In addition, the Issuer by being a state enterprise is subject to a temporary moratorium on enforcement against its fixed assets, which are necessary for its production activities, introduced by the Law of Ukraine “On Introducing of Moratorium for Forced Sale of Property”. By virtue of the moratorium, enforcement against the fixed assets of the Issuer arising in connection with, inter alia, (a) court judgments and arbitration awards or (b) bankruptcy proceedings, is currently prohibited. As a result, creditors of the Issuer who seek to satisfy a judgment, award or a court approved settlements against the fixed assets of the Issuer may not be able to do so.

Ukrainian currency control regulations could impact the ability of the Issuer to make payments to the Noteholders

The National Bank of Ukraine (“NBU”) is empowered to define policies for, and regulate currency operations in Ukraine, and has the power to establish restrictions on currency operations, cross-border payments and procedure, for the repatriation of profits. Purchase of foreign currency and foreign currency payments outside of Ukraine are possible only in cases provided by applicable laws of Ukraine and subject to the submission of documents required under currency control regulations. As a general rule, unless special exceptions apply, foreign currency payments made to recipients outside of Ukraine are possible only on the basis of a licence issued by the NBU or a loan registration certificate issued by the NBU, as the case may be. Although the NBU has adopted a resolution exempting the Issuer from the loan registration requirements and has issued a letter which (while not a normative act under Ukrainian law) confirms that a licence is not required by the Issuer for making payments under the Trust Deed and the Agency Agreement it is possible that at some later date, the NBU will require that the Issuer obtain a licence before making payments under the Notes, the Agency Agreement and the Trust Deed. If the NBU determines that a licence is required for payments by the Issuer, the Issuer will need to apply for a licence. The Issuer cannot assure investors that it would receive such a licence. If the Issuer does not receive such a licence or an exemption from the licence requirement, no assurance can be given that it will be able to make payments under the Notes. Current NBU regulations do not require that a licence be obtained by the Guarantor in relation to any payments under the Guarantee, and the Guarantor will not be restricted by the respective NBU rules in its ability to perform under the Guarantee in the event that the Issuer is required to obtain a licence but fails to do so.

Ukrainian courts may not enforce the gross-up obligations of the Issuer

The Profits Tax Law generally prohibits contractual provisions requiring a resident entity paying income from sources in Ukraine to a non-resident entity to pay Ukraine’s income tax for such non-resident. The letter of the State Tax Administration of Ukraine No. 14086/5/22-5016 dated 18 November 2009 (the “**Restrictive Letter**”) states that payment of any additional amount to a non-resident of Ukraine to compensate tax deducted amounts contradicts the Law of Ukraine “On Taxation of Company Income”. However, by a further letter of the State Tax Administration of Ukraine No. 13039/5/15-0516 dated 13 October 2010 (“**Notes Specific Clarification**”), which was provided specifically in the context of the Notes, the State Tax Administration of Ukraine has clarified that the provisions of the Restrictive Letter shall not be applicable to external borrowings (agreements on placement of notes outside of Ukraine) made by state enterprises by means of issuance of notes secured by state guarantees if repayment of principal and interest payments thereunder are made out of the State Budget funds. Although it is expected that repayment of principal and interest payments under the Notes will generally be made out of the State Budget funds, it may not be excluded that such payments could also be made out of the funds generated by NSC Olympic, Lviv Directorate or other operating companies or otherwise out of the funds which are not the State Budget funds.

Therefore, should the position of the Tax Administration of Ukraine pursuant to the Restrictive Letter be supported, or should tax gross-up obligations be otherwise interpreted as prohibited under Ukrainian law in any proceedings before Ukrainian courts, the Issuer's gross-up obligations would be voidable and unenforceable under Ukrainian law. Currently, the Profits Tax Law does not prohibit the Guarantor to make payments of any such additional amount to a non-resident of Ukraine.

Judgments relating to assets in Ukraine and Ukrainian assets in other jurisdictions may be difficult to enforce

Ukraine is a sovereign state. There is a risk that, notwithstanding the waiver of sovereign immunity by Ukraine, a claimant will not be able to enforce a court judgment against certain assets of the Guarantor in certain jurisdictions (including the imposition of any arrest order or attachment or seizure of such assets and their subsequent sale) without the Guarantor having specifically consented to such enforcement at the time when the enforcement is sought. Furthermore, the Guarantor reserves the right to plead sovereign immunity under the U.S. Foreign Sovereign Immunities Act of 1976 with respect to actions brought against it under any United States federal or State securities law.

It may not be possible to effect service of process against the Guarantor in courts outside Ukraine or in a jurisdiction to which the Guarantor has not explicitly submitted. Moreover, it may not be possible in the courts of Ukraine to enforce foreign court judgments against the Guarantor that are predicated upon the laws of foreign jurisdictions without a re-examination of the merits of such judgment in the Ukrainian courts. Furthermore, if a foreign judgment were to provide for an enforcement procedure contravening Ukrainian law requirements, a Ukrainian court would likely refuse to recognise and enforce the judgment. Courts in Ukraine will not recognise and/or enforce a judgment obtained in a court established in a country other than Ukraine unless such recognition and/or enforcement is provided for by an international treaty ratified by Ukraine, and then only in accordance with the terms of such treaty. Such treaties are in existence with certain CIS countries and other countries including, amongst others, Cyprus, Turkey, Hungary, Bulgaria and China. However, there is no such treaty or arrangement in effect between Ukraine and Ireland, the United Kingdom or the United States.

In the absence of such treaty, the courts of Ukraine may only recognise or enforce a foreign court judgement on the basis of the principle of reciprocity. Under Article 390 of the Civil Procedure Code, unless proven otherwise, the reciprocity is deemed to exist in relations between Ukraine and the country where the judgement was rendered. The Civil Procedure Code does not provide for any clear rules on the application of the principle of reciprocity and there is no official interpretation or court practice of these provisions of the Civil Procedure Code. Accordingly, there can be no assurance that the courts of Ukraine will recognise or enforce a judgement rendered by the courts of Ireland, the United Kingdom or the United States on the basis of the principle of reciprocity. Furthermore, the courts of Ukraine might refuse to recognise or enforce a foreign court judgement on the basis of the principle of reciprocity on the grounds provided in the Civil Procedure Code.

The foreign exchange reserves of Ukraine are controlled and administered by the NBU, which is an independent central bank legally distinct from the Government of Ukraine. Accordingly, such reserves would not be available to satisfy any claim or judgment in respect of the Guarantee.

Risk Factors Relating to the Guarantor

Ukraine's economy is vulnerable to fluctuations in the global economy.

When the global economic and financial situation began to deteriorate in 2008, the effect on Ukraine's economy was particularly severe.

In particular, because Ukraine is a major producer and exporter of metal and agricultural products, the Ukrainian economy is especially vulnerable to declines in demand for exports, declines or fluctuations in world commodity prices and the imposition of import tariffs by the United States, the EU or by other major export markets. For instance, Ukraine's industrial output decreased dramatically starting in the 4th quarter of 2008: the full-year decline in industrial output in 2008 amounted to 5.2 per cent., compared to a growth of

7.6 per cent. in 2007. Industrial output further declined in 2009 by 21.9 per cent., as a result of which industrial output returned to the levels recorded in 2003-2004, or approximately 80 per cent. of the level recorded in 1990. In particular, Ukraine's relatively strong reliance on exports of ferrous and non-ferrous metals and their products (32.3 per cent. and 36.3 per cent. of total goods exports value in 2009 and the six months ended 30 June 2010, respectively) makes the country's export revenues and, by extension, its broader macroeconomic performance, vulnerable to declines or fluctuations in global metal demand or prices. In line with a decline in industrial output, real gross domestic product ("GDP") declined by 15.1 per cent. in 2009. However, in 2010, industrial production started to recover and in the seven months ended 31 July 2010, industrial production increased by 11.1 per cent. compared to the same period in 2009. In addition, during the first quarter of 2010, Ukraine's real GDP increased by 4.9 per cent. as compared to a 20.2 per cent. decline for the first quarter of 2009, and, according to preliminary data, in the second quarter of 2010 the real GDP increased by 5.9 per cent., as compared to 17.8 per cent. decline for the second quarter of 2009.

The economic crisis has also contributed to an increase in Ukraine's State Budget deficit as a percentage of its GDP. Although this percentage remains relatively low in absolute terms, it has increased significantly from 1.3 per cent. at year-end 2008 to 3.9 per cent. at year-end 2009. The 2010 State Budget Law initially contemplated a State Budget deficit of 5.3 per cent. of GDP for 2010. On 8 July 2010, Parliament passed an amendment to the 2010 State Budget Law (the "State Budget Amendment") providing for a decrease of the 2010 State Budget deficit to 4.99 per cent. of GDP. The Budget Declaration for 2011 provides for a budget deficit of not more than 4.5 per cent. of GDP as a target of 2011 budgetary policy. See "*Public Finance and Fiscal Policy – The Central-Local Fiscal Relationship*" and "*Public Finance and Fiscal Policy – Budget Process*".

Consumer price inflation was 9.3 per cent. for the seven months ended 31 July 2010, as compared to the corresponding period of 2009. Consumer price inflation in Ukraine was 15.9 per cent. in 2009, 25.2 per cent. in 2008 and 12.8 per cent. in 2007, in each case as compared to the corresponding period of the previous year. Wholesale prices are also vulnerable to the increases in world prices for metal products and grain, as well as natural gas and oil. Wholesale price inflation, or WPI, has a direct bearing on consumer price inflation and both have been high in recent years, threatening macroeconomic stability and performance. WPI was 35.5 per cent. in 2008 and 6.5 per cent. in 2009, in each case as compared to the corresponding period of the previous year. WPI was 21.6 per cent. for the seven months ended 31 July 2010, as compared to the corresponding period of 2009, while in the seven months ended 31 July 2009, WPI was 7.2 per cent. compared to the corresponding period of 2008. See "*Economy of Ukraine—Inflation*".

Further, Ukraine's economy has been significantly affected by the global credit crunch that began in 2007, as a result of which international capital markets ceased to be available for Ukrainian borrowers. Prior to the global credit crunch, relatively easy access to liquidity, both from within Ukraine and internationally, was a significant factor facilitating growth in Ukraine's GDP. Reduced external financing available for Ukrainian companies contributed to a decline in industrial production and cutting down of investment projects and capital expenditures generally. Any further deterioration of global or regional economic conditions, including a so-called "double dip" recession, may stall any current recovery or lead to worsening of the economic and financial crisis in Ukraine. Any such developments, including continued unavailability of external funding and increases in world prices for goods imported to Ukraine or decreases in world prices for goods exported from Ukraine, may have or continue to have a material adverse effect on the economy and thus on the ability of Ukraine to perform its obligations under the Guarantee.

Investments in emerging market countries such as Ukraine carry risks not typically associated with risks in more mature markets.

An investment in a country such as Ukraine, which achieved independence less than 20 years ago and whose economy is in transition, is subject to substantially greater risks than an investment in a country with a more developed economy and more mature political and legal systems. Although some progress has been made since independence in 1991 in reforming Ukraine's economy and political and judicial systems, to a large extent Ukraine still lacks the necessary legal infrastructure and regulatory framework that are essential to support market institutions, the effective transition to a market economy and broad-based social and economic reforms. In addition, Ukraine may become subject to heightened volatility due to regional

economic, political or military conflicts. As a consequence, an investment in Ukraine carries risks that are not typically associated with investing in more mature markets.

These risks may be compounded by incomplete, unreliable or unavailable economic and statistical data on Ukraine, including elements of the information provided in this Prospectus. See “– *Official economic data and third-party information may not be reliable*”.

Accordingly, investors should exercise particular care in evaluating the risks involved and must decide for themselves whether, in light of those risks, their investment is appropriate. Generally, investments in emerging markets, such as Ukraine, are only suitable for sophisticated investors who fully appreciate the significance of the risks involved and investors are urged to consult their own legal and financial advisers before making an investment in the Notes and the Guarantee.

Ukraine’s Government may be unable to sustain political consensus, which may result in political instability.

Historically, a lack of political consensus in the Verkhovna Rada, or Parliament, of Ukraine has made it difficult for the Government to sustain a stable coalition of parliamentarians to secure the necessary support to implement a variety of policies intended to foster liberalisation, privatisation and financial stability.

The 2010 presidential elections were the subject of a number of controversies between the Parliament, the Government and the President. Eighteen candidates, including the then incumbent President and Prime Minister and Speaker of Parliament, participated in the first round of elections on 17 January 2010. The two candidates who received the largest number of votes in the first round, Viktor Yanukovich and Yuliya Tymoshenko, participated in a run-off that took place on 7 February 2010. On 14 February 2010, Mr. Yanukovich was declared the official winner of the run-off, having received 48.95 per cent. of votes, compared to 45.47 per cent. received by Ms Tymoshenko. Although Ms Tymoshenko initially challenged the results of the run-off, she subsequently withdrew her challenge, and Mr. Yanukovich was inaugurated as President on 25 February 2010.

On 11 March 2010, the Parliament appointed Mykola Azarov, a member of Party of Regions, as the new Prime Minister and endorsed the coalition Government.

In July 2010, 252 members of Parliament had requested the Constitutional Court to opine on the constitutionality of the 2004 law that was the basis of a constitutional reform implemented in 2006. On 30 September 2010, the Constitutional Court issued a ruling against the constitutionality of the 2004 law (the “**CCU Ruling**”). Pursuant to the CCU Ruling, starting from 30 September 2010, Ukraine is governed by the Constitution that was in effect before the amendments were introduced by the 2004 law. Following the CCU Ruling, certain legislation may contradict the Constitution of Ukraine and require amendment. This may result in the uncertainty in distribution of powers among state authorities and may lead to further political uncertainty in Ukraine. Accordingly, whilst the long term consequences of the CCU Ruling are not yet clear, it may result in continued or heightened political instability in Ukraine. See “*Description of the Guarantor – Political Developments*” and “*Political Framework – The Constitution and the President*”.

As at the date of this Prospectus, relations between the President, the Government and Parliament, as well as the procedures and rules governing the political process in Ukraine, remain in a state of uncertainty and may be subject to change through the normal process of political alliance-building or, if the required action is taken, through constitutional amendments and decisions of the Constitutional Court. Recent political developments have also highlighted potential inconsistencies between the Constitution of Ukraine and various laws and presidential decrees. Furthermore, such developments have raised questions regarding the judicial system’s independence from economic and political influences. See “*Description of the Guarantor – Political Developments*”.

A number of additional factors could adversely affect political stability in Ukraine, including:

- lack of agreement within the factions and amongst individual deputies;
- disputes between factions that form a majority and opposition factions on major policy issues, including Ukraine’s foreign and energy policy;

- court action taken by opposition parliamentarians against decrees and other actions of the President or Government or the majority factions; or
- court action by the President against Parliamentary or Governmental resolutions or actions.

If political instability continues or heightens, it may have negative effects on the Ukrainian economy including access to international capital markets and borrowing from multilateral organisations, and, as a result, a material adverse effect on Ukraine’s capacity to perform its obligations under the Guarantee.

Political instability may affect economic indicators and result in a negative effect on the economy of Ukraine.

In recent years, Ukraine has undergone substantial political transformation from a constituent republic in a federal socialist state to an independent sovereign democracy. In parallel with this transformation, Ukraine is transitioning from a centrally planned economy to a market economy. However, this process of economic transition is not complete.

Although Ukraine made significant progress in 2007 and 2008 in increasing its GDP, increasing real wages and improving its trade balance, political instability compounded the negative effects that the global economic downturn had on key economic indicators in 2009. See “*Economy of Ukraine*” and “*External Sector*”. If political instability continues or heightens, it may have further negative effects on the Ukrainian economy and, as a result, a material adverse effect on Ukraine’s capacity to perform its obligations under the Guarantee.

Positive developments in the economy may not be achieved if certain important economic and financial structural reforms are not made.

The negative impact of the global economic and financial downturn has been compounded by weaknesses in the Ukrainian economy, which is sensitive to external and internal events. In particular, although the Government has generally been committed to economic reform, the implementation of reform has been impeded by lack of political consensus, controversies over privatisation (including privatisation of land in the agricultural sector and privatisation of large industrial enterprises), restructuring of the energy sector, and removal of exemptions and privileges for certain state owned enterprises or for certain industry sectors.

The negative trends in the Ukrainian economy may continue if commodity prices on the external market are low and access to foreign credit is limited, unless Ukraine undertakes certain important economic and financial structural reforms. The most critical structural reforms that need to be implemented or continued include: (i) comprehensive reforms of Ukrainian tax legislation with a view to broadening the tax base by bringing a substantial portion of the shadow economy into the reporting economy; (ii) reform of the energy sector through the introduction of uniform market-based energy prices and improvement in collection rates (and, consequently, the elimination of the persistent deficits in that sector); and (iii) reform of social benefits and pensions.

Failure to achieve the political consensus necessary to support and implement such reforms could adversely affect the country’s macro-economic indices and economic growth. Furthermore, future political instability in the executive or legislative branches could hamper efforts to implement necessary reforms. There can be no assurance that the political initiatives necessary to achieve these or any other reforms described elsewhere in this Prospectus will continue, will not be reversed or will achieve their intended aims. Rejection or reversal of reform policies favouring privatisation, industrial restructuring and administrative reform may have negative effects on the economy and, as a result, a material adverse effect on Ukraine’s capacity to perform its obligations under the Guarantee.

The Ukrainian banking system may be vulnerable to stress due to fragmentation, undercapitalization and a potential increase in non-performing loans, all of which could have a material adverse effect on the real economy.

The recent global financial crisis has led to the collapse or bailout of some Ukrainian banks and to significant liquidity constraints for others. The crisis has prompted the government to inject substantial funds into the banking system amid reports of difficulties among Ukrainian banks and other financial institutions. See “*The Banking System and Securities and Financial Services Markets in Ukraine — Recent Developments in the Banking Sector*”. The Government’s policy has been to intervene in support only of banks whose size is such that their failure would create systemic risk for the Ukrainian economy.

Despite progress with the restructuring and recapitalisation of Ukrainian banks, problems with asset quality and indebtedness persist. Asset quality was affected significantly by the devaluation in the hryvnia in 2008 (52.5 per cent. against the dollar and 46.3 per cent. against the euro) and further exacerbated by the 15.1 per cent. contraction of the economy in 2009. Despite government and NBU intervention and progress in stabilising the foreign exchange market by the end of 2009 and during the first half of 2010, the high dollarisation in the Ukrainian financial system increased exchange rate risks and could contribute to a worsening of banks’ asset quality. Doubtful and bad loans are another factor affecting the asset quality of Ukrainian banks. The proportion of loans represented by doubtful and bad loans was 3.8 per cent. and 13.1 per cent. as at 31 December 2008 and 2009, respectively, and 14.6 per cent. as at 31 July 2010. Although the rate of growth of the share of doubtful and bad loans in banks’ credit portfolios has slowed, a future increase in this rate could place additional strain on the banking system. Furthermore, in addition to the loans that the NBU categorises as doubtful and bad, a significant proportion of Ukrainian banks’ loan portfolios could be described as substandard. The IMF, in connection with approving in July 2010 a new stand-by agreement with Ukraine, which is described in greater detail below, provided two estimates for loans which could be categorised as non-performing. Under a broad definition of non-performing loans that includes loans classified as substandard, doubtful and loss, the IMF estimated that 41.6 per cent. of loans held by Ukrainian banks were non-performing as at 31 March 2010. Under a narrower definition that does not count as non-performing those substandard loans that are serviced in a timely manner, the IMF estimated that 15 per cent. of loans were non-performing as at 31 March 2010.

The continuation or worsening of the financial crisis, further insolvencies of Ukrainian banks, growth in the share of doubtful and bad loans, the need for the Ukrainian government to inject more capital into the banking system and the failure to adopt and implement a system of banking regulation that achieves an increased degree of soundness and stability in the nation’s banks could all have a material adverse effect on the Ukrainian economy and the ability of Ukraine to perform its obligations under the Guarantee.

The Ukrainian currency is subject to volatility and depreciation.

In view of the high dollarisation of the Ukrainian economy and increased activity of Ukrainian borrowers on external markets in 2005-2007, Ukraine has become increasingly exposed to the risk of hryvnia exchange rate fluctuations. Since September 2008, the interbank U.S. dollar/hryvnia exchange rate has fluctuated significantly. See “*The Monetary System — Exchange Rates*”.

The official U.S. dollar/hryvnia exchange rate increased from UAH 4.85 = U.S.\$1.00 as at 24 September 2008 to UAH 7.87 = U.S.\$1.00 as at 19 December 2008. In total, in 2008, the hryvnia depreciated against the dollar by 52.5 per cent. and against the euro by 46.3 per cent. as compared to year-end 2007, and further depreciated against these currencies in 2009 by 3.7 per cent. and 5.5 per cent., respectively.

The National Bank of Ukraine, or NBU, sought to address the hryvnia instability by taking administrative measures (including certain foreign exchange market restrictions), and used approximately U.S.\$13.4 billion and U.S.\$10.4 billion of its foreign exchange reserves to support the Ukrainian currency in 2008 and 2009, respectively. In the eight months ended 31 August 2010, due to increased supply, and resulting surplus, of foreign currency in the market, the hryvnia appreciated against the U.S. dollar by 1.24 per cent. and against the euro by 12.52 per cent. The official exchange rate was UAH 7.91 to U.S.\$1.00 as at 14 October 2010.

The depreciation in the U.S. dollar/hryvnia exchange rate in 2008-2009 negatively affected the ability of Ukrainian borrowers to repay their indebtedness to Ukrainian banks (as at 31 July 2010, approximately 50 per cent. of the domestic loans are denominated in foreign currency) as well as to external lenders. Gradual exchange rate liberalisation is one of the key elements in the IMF program. The liberalisation process could result in a period of greater currency volatility.

Any further currency fluctuations may negatively affect the Ukrainian economy in general and, as a result, have a material adverse effect on Ukraine's capacity to perform its obligations under the Guarantee.

Inability to obtain financing from external sources could affect Ukraine's ability to meet financing expectations in its budget.

Ukraine's internal debt market remains illiquid and underdeveloped as compared with markets in most western countries. See "*Public Debt — Internal Debt*". In the wake of the emerging market crisis in the autumn of 1998 and until the second half of 2002, loans from multinational organisations such as the EBRD, the World Bank, the European Union (the "EU") and the IMF comprised Ukraine's only significant sources of external financing.

From 2003 until 2008, the international capital markets were Ukraine's main source of external financing but they ceased to be available from mid-2008 due to the global economic and financial crisis. As a result, Ukraine sought IMF financing. In November 2008, the IMF approved a two-year Stand-By Arrangement ("SBA") with Ukraine for approximately U.S.\$16.4 billion to assist the Ukrainian Government in restoring financial and economic stability. In 2008 and 2009, total disbursements under the SBA amounted to approximately U.S.\$10.6 billion. The drawdowns of IMF financing were contingent upon Ukraine's satisfaction of requirements including:

- reducing the budget deficit by imposing additional taxes and taking other non-tax measures,
- introducing a comprehensive approach to budget and fiscal sector management,
- strengthening the independence of the NBU as the principal regulator in the banking sector and developing and implementing a comprehensive bank refinancing and restructuring programme, and
- bringing domestic natural gas prices in line with international market prices.

In November 2009, a third tranche of IMF financing under the SBA in an expected amount of approximately U.S.\$3.9 billion was suspended due to failure to reach agreement with respect to the results of the third review of Ukraine's compliance with the terms of the SBA.

In March-July 2010, after the new President took office, IMF missions visited Ukraine to review the macroeconomic situation and budget, fiscal and monetary policy of the Government and the NBU and to consider possible resumption of IMF support. On 28 July 2010, the IMF Executive Board noted the cancellation of the SBA approved in November 2008. On the same date, the IMF Executive Board approved a new U.S.\$15.15 billion stand-by arrangement for Ukraine to be extended in ten tranches in 2010-2012, with two tranches expected to be extended in 2010, and four tranches expected to be extended in each of 2011 and 2012, subject, in each case, to Ukraine's compliance with the stand-by arrangement terms. On 2 August 2010, Ukraine received the first tranche in the amount of approximately U.S.\$1.89 billion, approximately U.S.\$1.0 billion of which was earmarked for the financing of the State Budget deficit.

The goal of the Ukrainian economic programme supported by the new IMF financing arrangement is to entrench fiscal and financial stability, advance structural reforms, and put Ukraine on a path of sustainable and balanced growth. To achieve these aims, the stand-by arrangement focuses on three key areas: (i) fiscal policy; (ii) monetary and exchange rate policy, and (iii) financial sector policy. In particular, fiscal policy as envisaged by the arrangement contemplates restoration of confidence and fiscal sustainability by reducing the general government deficit to 5.5 per cent. of GDP in 2010, 3.5 per cent of GDP in 2011, and 2.5 per cent. of GDP in 2012; reducing the deficit of Naftogas to 1.0 per cent. of GDP in 2010 and eliminating it thereafter; setting public and publicly guaranteed debt-to-GDP ratio firmly on a downward path with the objective of stabilising it below 35 per cent. by 2015; and relying proportionally more on expenditure-saving

measures to gradually reduce the tax burden on the economy. The monetary and exchange rate policy contemplated under the arrangement provides for maintaining core CPI inflation in single digits in 2010 and bringing overall CPI to no more than 5 per cent. over the medium term; strengthening the independence and accountability of the NBU; and improving the functioning of the foreign exchange market. The third element of the arrangement, financial sector policy, centers on completing the resolution and recapitalisation of systemic banks, strengthening state-owned banks, and enacting key legislation and regulations, including, among other things, through creating a framework that properly recognises and facilitates the resolution of impaired loans and implementing consolidated supervision. In addition, the stand-by arrangement provides for the quantitative and continuous performance criteria that are to be met by Ukraine as of each of 30 September and 31 December 2010. Such criteria include, among other things, a ceiling on the cash deficit of the general government, a floor on net international reserves of the NBU, a ceiling on the net domestic assets and a ceiling on the state-guaranteed debt. The first review of Ukraine's compliance with the stand-by arrangement terms is expected to take place in November 2010 and the second tranche is expected to be extended in December 2010 subject to the satisfactory results of the first review, while the second review is proposed for March 2011 based on year-end 2010 targets. See "*Public Debt – International Organisations – IMF*".

The IMF's methodology for calculating the target consolidated general government deficit as percentage of GDP differs from Ukraine's methodology for calculating the projected State Budget deficit as percentage of GDP in the 2010 State Budget. Therefore, were Ukraine to calculate its consolidated general government deficit using the IMF methodology, that number would differ from the State Budget deficit figure contemplated in the 2010 State Budget.

On 8 July 2010, in order to comply with the new arrangements reached with the IMF, Parliament passed the State Budget Amendment. The State Budget Amendment provides for a decrease in revenues to the 2010 State Budget of approximately UAH 13.4 billion, a decrease in expenditures from the 2010 State Budget of approximately UAH 17.1 billion, a decrease in the 2010 State Budget deficit of approximately UAH 3.6 billion (to 4.99 per cent. of GDP) and a decrease in target privatisation proceeds of approximately UAH 3.65 billion. The UAH 13.4 billion decrease in revenues includes a decrease in revenues from VAT collection of approximately UAH 10 billion. The UAH 17.1 billion decrease in expenditures includes an approximately UAH 8.75 billion decrease in expenditures from the Stabilisation Fund and an approximately UAH 3.0 billion decrease in transfers to cover the deficit in the Pension Fund.

If, despite the new IMF financing arrangement and attendant economic reforms, the international capital markets or syndicated loan markets are unavailable to Ukraine, the Government would have to further rely to a significant extent on official or multilateral borrowings, such as borrowings from the IMF or the World Bank, to finance part of the budget deficit, fund its payment obligations under domestic and international borrowings and support foreign exchange reserves. Unavailability of external financing may place additional pressure on Ukraine's ability to meet its payment obligations.

More generally, external borrowings from multilateral organisations such as the IMF, the EBRD, the World Bank or the EU may be conditioned on Ukraine's satisfaction of various requirements. These requirements may include:

- implementation of strategic, institutional and structural reforms;
- limits on the consolidated budget deficit;
- reduction of overdue tax arrears;
- absence of increase of budgetary arrears;
- improvement of sovereign debt credit ratings; and
- reduction of overdue indebtedness for electricity and gas.

If Ukraine is unable to meet these requirements, multilateral organisations may withhold or suspend funding, as occurred with respect to the third tranche of IMF financing under the SBA. If Ukraine is unable to resort to the international capital markets or syndicated loan markets, a failure by official creditors and of

multilateral organisations to grant adequate financing could put pressure on Ukraine's budget and foreign exchange reserves and have a material adverse effect on its ability to perform its obligations under the Guarantee.

Adverse changes in global or Ukrainian economic conditions have resulted in several restructurings of Ukrainian commercial debt and a significant liquidity risk.

In 2007 and 2008, Ukraine's total debt as a percentage of GDP, including both State debt (direct debt) and State-guaranteed debt (contingent liabilities), was at a relatively moderate level, amounting to 12.3 per cent. at the end of 2007 and 20.0 per cent. at the end of 2008. In 2009, total debt of Ukraine as a percentage of GDP increased to 34.6 per cent. at the end of 2009. The Government expects that the total debt of Ukraine, including both State debt (direct debt) and State-guaranteed debt (contingent liabilities), as a percentage of GDP will increase to 39.1 per cent. by the end of 2010 and then decrease to 36.1 per cent. by the end of 2011.

Ukraine's debt owed to private creditors has undergone a number of restructurings. In the last quarter of 1998 and in July 1999, Ukraine entered into voluntary agreements with the holders of various hedged domestic and foreign currency-denominated obligations. These restructurings, conducted in consultation with the IMF, allowed Ukraine to postpone repayment of a substantial portion of the maturing principal of such obligations to 2000 and 2001, and also involved the conversion of some domestic debt into U.S. dollar-denominated eurobonds. These measures were aimed at alleviating the liquidity problems then facing the Government.

In 2000, Ukraine faced a severe liquidity crisis. This crisis stemmed largely from Ukraine's inability to make payments on external debt falling due in 2000 and 2001 due to low levels of foreign exchange reserves, the deteriorating state of Ukraine's economy and the inaccessibility of the international capital markets. In response, Ukraine comprehensively restructured its commercial debt through a series of exchange offers in which this debt was amended or exchanged for new notes. These new notes matured and were repaid in March 2007. Following the 2000 exchange offer, in order to treat its creditors equally, Ukraine also restructured official debt falling due in 2000 and 2001 to its official creditors within the framework of the Paris Club. In February 2003, Ukraine agreed with Turkmenistan to reschedule U.S.\$281 million of debt, which represented the amount Ukraine owed in arrears for gas deliveries by Turkmenistan in the 1990s and was repaid in April 2007. See "*Public Debt – External Debt – Official Creditors*".

The ratio of State external debt service (including principal, interest and fees but excluding debt owed to the IMF by the NBU) to GDP was approximately 0.9 per cent. in 2007, approximately 0.5 per cent. in 2008, approximately 1.9 per cent. at the end of 2009, and, as at 31 July 2010, it is estimated that it will be approximately 2.6 per cent. by year-end 2010 and 1.1 per cent. by year-end 2011. Total State external debt service (excluding payments to the IMF by the NBU) was approximately U.S.\$1,231.8 million in 2007, approximately U.S.\$897.0 million in 2008 and approximately U.S.\$2,168.0 million in 2009. The increase in 2009 resulted from the repayment of U.S.\$500 million in floating rate notes in August 2009 and from the exercise of a bondholder put on CHF 768 million in 3.5 per cent. bonds initially due in 2018, which then became due in September 2009. See "*Public Debt – Commercial Creditors*". As at 1 August 2010, the Government expects total State external debt service (excluding payments to the IMF by the NBU) to be approximately U.S.\$3,459.8 million and U.S.\$ 1,560.3 million in 2010 and 2011, respectively. Total IMF debt service and repayment was approximately U.S.\$465.8 million in 2007, approximately U.S.\$385.2 million in 2008 and approximately U.S.\$285.0 million in 2009 and is expected by the Government to be approximately U.S.\$205.4 million in 2010. As at 1 August 2010, the amount of State external debt service payments (including principal and interest payments but excluding debt owed to the IMF by the NBU) is expected to increase significantly in 2013 to U.S.\$4,555.1 million, largely due to scheduled repayment in 2013 of debt owed to the IMF by the Government in the amount of U.S.\$2,755.1 million and redemption of U.S.\$1,000.0 million 7.65 per cent. Notes due 2013. This expected increase does not include any additional debt issuance or guarantee of debt by Ukraine. Although current authorisations permit guarantees of debt up to an aggregate of UAH 45 billion in 2010, the government currently intends to remain within the IMF's recommended limit of UAH 15 billion for 2010.

The substantial payment obligations of Ukraine and many state-owned companies falling due in 2009 and 2010 (including debt repayments, payments for natural gas supplied for domestic consumption to Ukraine)

has exerted additional pressure on Ukraine's liquidity. In particular, during 2009, National Joint-Stock Company "Naftogas of Ukraine" ("Naftogas") began negotiations with its lenders to restructure its debts to foreign banks aiming to extend payment terms and to amend other substantial terms of its loan undertakings. On 5 November 2009, Naftogas completed the restructuring of its term loan facilities from foreign banks of approximately U.S.\$1.6 billion. Further, the State Railway Administration of Ukraine (Ukrzaliznytsya) began negotiations with its lenders to reschedule certain of its debts to foreign banks amounting to approximately U.S.\$440 million aiming to extend payment terms of its loan undertakings.

This pressure on Ukraine's liquidity may intensify if the State does not meet its budget revenue targets in 2010. In 2009, revenues of the Consolidated Budget were UAH 273.0 billion or below the budgeted target by UAH 51.7 billion largely due to the effect of financial and economic downturn globally and in Ukraine. Of that amount, UAH 609.4 million, UAH 13,046.3 million and UAH 9,917.9 million reflects decreased collection of import duties, VAT and corporate income tax, respectively. If the trends recorded in 2009 continue in 2010, actual revenues of the Consolidated Budget may fall short of the amended revenue budget for 2010 in the amount of UAH 320.1 billion. See "*Public Finance and Fiscal Policy*". If these factors occur or persist, Ukraine may experience a lack of liquidity in 2010.

Continued adverse changes in global or domestic political and economic conditions or in the international capital markets may place renewed pressure on Ukraine's foreign exchange reserves and increase its liquidity risk, which could in turn adversely affect its ability to comply with its payment obligations under the Guarantee. See also "*- Inability to obtain financing from external sources to provide financing could affect Ukraine's ability to meet financing expectations in its budget*".

In addition, it should be noted that many enterprises in the Ukrainian private sector have significant levels of indebtedness, and as a result of the ongoing financial crisis may experience difficulty accessing new financing. Although private-sector debt, unlike state debt, does not have a direct negative effect on the State's foreign currency reserves or liquidity, high levels of indebtedness of, and limited availability of new credit to, the private sector may complicate economic recovery and pose a significant risk in an already challenging economic environment.

Ukraine's economy depends heavily on its trade flows with Russia and certain of the CIS and any major change in relations with Russia could have adverse effects on the economy.

Ukraine's economy depends heavily on its trade flows with Russia and the rest of the Commonwealth of Independent States (the "CIS"), largely because Ukraine imports a large proportion of its energy requirements, especially from Russia (or from countries that transport energy-related exports through Russia). In addition, a large share of Ukraine's services receipts comprise transit charges for oil, gas and ammonia from Russia.

Ukraine therefore considers its relations with Russia to be of strategic importance. However, until recently, relations between Ukraine and Russia were strained to a certain extent due to factors including:

- disagreements over the prices and methods of payment for gas delivered by the Russian gas supplier OJSC Gazprom ("Gazprom") to, or for transportation through, Ukraine;
- issues relating to the temporary stationing of the Russian Black Sea Fleet (*Chernomorskyi Flot*) in the territory of Ukraine; and
- a Russian ban on imports of meat and milk products from Ukraine and anti-dumping investigations conducted by Russian authorities in relation to certain Ukrainian goods.

However, relations with Russia have strengthened since the election of President Yanukovich in 2010. In particular, on 21 April 2010, Ukraine and Russia signed a new agreement on issues of the stationing of Russia's Black Sea Fleet on Ukrainian territory, under which the term of the stationing of Russia's Black Sea Fleet in Sevastopol was extended for a further 25-year period with an additional 5-year extension option. See "*The Political Framework of Ukraine – International Relations – Foreign Countries – Russia*".

If bilateral trade relations were to deteriorate or if Russia were to stop transiting a large portion of its oil and gas through Ukraine or if Russia halted supplies of natural gas to Ukraine, Ukraine's balance of payments and foreign currency reserves could be materially and adversely affected.

Russia has, recently and in the past, threatened to cut off the supply of oil and gas to Ukraine in order to apply pressure on Ukraine to settle outstanding gas debts and maintain the low transit fees for Russian oil and gas through Ukrainian pipelines to European consumers. In line with its threats, Gazprom substantially decreased natural gas supplies to Ukraine in early January 2009, reportedly, due to failure by Naftogas to timely repay all outstanding debts owed to Gazprom for natural gas supplied to Ukraine for domestic consumption in 2008. Following negotiations between the governments of Russia and Ukraine and the signing of agreements between Naftogas and Gazprom setting out the terms of further natural gas supplies and transit through the territory of Ukraine, Gazprom on 20 January 2009 resumed natural gas supplies to Ukraine and Western Europe.

Prices for natural gas supplied by Gazprom for domestic consumption in Ukraine increased in each of 2006, 2007 and 2008 from U.S.\$50 per 1,000 cubic metres as of 1 January 2005 to U.S.\$179.5 per 1,000 cubic metres as of 1 January 2008. Pursuant to the agreements signed between Naftogas and Gazprom on 19 January 2009 for natural gas supplies and transit in 2009 through 2019, a price for natural gas supplied to Ukraine for domestic consumption and a tariff for transit of natural gas through the territory of Ukraine is to be determined pursuant to formulae set out in the agreements. In 2009, the average weighted price for natural gas was approximately U.S.\$233.0 per 1,000 cubic metres. On 21 April 2010, amendments to the Gas Supply Contract and the Gas Transit Contract were signed, under which Gazprom has agreed to give Naftogas certain discounts from the otherwise applicable price for natural gas supplied for domestic consumption to Ukraine. The Government estimates that the average weighted annual price for natural gas supplied for domestic consumption in Ukraine in 2010 will be approximately U.S.\$266.5 per 1,000 cubic metres. See *"Economy of Ukraine – Principal Sectors of the Economy – Oil and Gas"*.

In addition, Naftogas and its subsidiaries contributed approximately 18.8 per cent. (or UAH 39.4 billion) and 10.2 per cent. (or UAH 24.5 billion) of revenues to Ukraine's State Budget for the years ended 31 December 2009 and 2008, respectively. However, the State Budget revenues received from Naftogas and its subsidiaries have been in part offset by direct subsidies from the State Budget to cover differences between the purchase price of imported gas and the price charged to municipal heating enterprises. For instance, in 2009 and 2008, UAH 4.1 and UAH 7.4 billion (including UAH 4.0 billion of compensation due for 2008 and UAH 3.4 billion of compensation due for 2006 and 2007) were extended from the State Budget to Naftogas to cover this difference. The 2010 State Budget provides for UAH 3.4 billion to be extended to Naftogas to cover this difference and as at 18 August 2010, the State Budget had allocated approximately UAH 2.9 billion of this amount to Naftogas for the same purpose. In addition to these direct subsidies, the Government may use other measures to support Naftogas, including but not limited to deferral of taxes and increasing the statutory capital of Naftogas through the issuance of additional shares and their exchange for T-bills.

Further Russian increases in gas supply prices, decreases in the volumes of gas transportation or other developments could adversely affect Naftogas' future results of operations, reducing the revenue the State Budget receives from Naftogas or increasing Naftogas's need for support. Reduced revenue from Naftogas, or an increased need for support, could put pressure on the State Budget and have a material adverse effect on Ukraine's ability to perform its obligations under the Guarantee.

Currently, approximately 30 per cent. of Ukrainian exports of goods go to Russia, while much of Russia's exports of energy resources are delivered to the EU via Ukraine. Russia's increases in the price for natural gas have adversely affected the pace of economic growth of Ukraine due to the considerable dependence of the Ukrainian economy on Russian exports of energy resources. Furthermore, although the gas price increases have increased pressure for reforms in the energy sector and modernisation of major energy-consuming industries of Ukraine through the implementation of energy-efficient technologies and the modernisation of production facilities, there can be no assurance that these reforms will be implemented successfully.

Any further adverse changes in Ukraine's relations with Russia, in particular any such changes adversely affecting supplies of energy resources from Russia to Ukraine or Ukraine's revenues derived from transit charges for Russian oil and gas, may have negative effects on the Ukrainian economy.

Relations with Russia and other CIS states may also affect Ukraine's economy indirectly, through the actions of companies directly or indirectly owned or otherwise controlled by these states or their subdivisions and agencies. For example, in May 2008, the Russian company Tatneft filed a request for arbitration against Ukraine. According to its published financial reports, Tatneft is subject to significant influence by the government of Tatarstan, an autonomous republic within Russia. See "*Judicial or arbitral proceedings may result in significant foreign currency awards against Ukraine*" and "*Political Framework – Legal Proceedings*". There can be no assurance that actions of companies owned or controlled by foreign states would not have negative effects on the Ukrainian economy; such actions could have political as well as economic motives.

Failure to fulfil privatisation plans will adversely affect achievement of financing levels anticipated in the State Budget.

The State Budget is dependent to a significant extent on receipts from privatisations. For 2008, target privatisation receipts were initially set at approximately UAH 8.9 billion; this target was reduced to UAH 607.1 million in December 2008. Actual privatisation receipts in 2008 were UAH 482.7 million, or 79.4 per cent. of the revised annual target. For 2009, target privatisation receipts were set at approximately UAH 8.5 billion and actual privatisation receipts were only UAH 814.9 million, or 9.6 per cent. of the annual target. A significant shortfall in actual privatisation receipts in 2008 and 2009 as compared to the respective targets was principally due to the failure to privatise OJSC "Ukrtelecom", JSC "Odessa Port Plant", OJSC "Turboatom" and a number of regional energy distribution companies. Certain of such privatisations were either cancelled or significantly delayed in 2008 and 2009 due to decrees of the President of Ukraine prohibiting or suspending these privatisations. See "*Economy of Ukraine – Privatisation*".

For 2010, target privatisation receipts were initially set at UAH 10.0 billion, but were subsequently decreased in July 2010 to UAH 6.35 billion. In the seven months ended 31 July 2010, actual privatisation receipts were only UAH 410.8 million, or 6.5 per cent. of the annual target (as compared to actual privatisation receipts of UAH 566.0 million, or 6.7 per cent. of the annual target, for the seven months ended 31 July 2009). Meeting budgeted privatisation targets for 2010 depends on the successful sale of major assets, most of which were due for privatisation in 2008 and 2009. In particular, the State Property Fund of Ukraine ("SPF") is preparing to sell in 2010 a 92.79 per cent. shareholding in OJSC "Ukrtelecom" with a nominal value of approximately UAH 4.3 billion and the starting price of UAH 10.5 billion. On 12 October 2010, the terms of this sale were approved by the Cabinet of Ministers of Ukraine and on 13 October 2010 the SPF announced that the bidding for this shareholding would take place on 28 December 2010.

Another sale that was scheduled by the SPF for 2010 is that of a 76 per cent. stake in JSC HC Luganskteplovov, the initial privatisation of which took place in 2007. This privatisation was declared invalid by a Ukrainian court and the transferred shares were re-transferred to the SPF. The SPF conducted a reprivatisation auction on 15 June 2010, at which Bryanskiy Machine-Building Plant, the initial purchaser of the shares, was again declared the winner with a bid price of UAH 410 million. As the buyer failed to make the payment for the shareholding as required under the terms of the relevant sale and purchase agreement, on 7 October 2010, the SPF filed a claim with the Kyiv Commercial Court requesting the court to terminate the sale and purchase agreement and to require the buyer to pay penalties and a fine. On 22 October 2010, the Kyiv Commercial Court ruled to terminate the sale and purchase agreement and to require the buyer to pay penalties and a fine in the amount of UAH 84.2 million. In addition, on 30 July 2010, the Kyiv commercial court opened proceedings on the claim filed by Mantara Holdings Limited against the SPF and Bryanskiy Machine-Building Plant. The plaintiff, which was not admitted by the SPF for participation in the auction, seeks to challenge the results of the auction and invalidate the sale and purchase agreement relating to the shareholding in JSC HC Luganskteplovov. On 21 September 2010, the Kyiv commercial court decided to invalidate the sale and purchase agreement relating to the shareholding in JSC HC Luganskteplovov, the judgment of the Kyiv commercial court having been appealed by the SPF and the buyer. As at 29 October 2010, it is unlikely that privatisation of HC Luganskteplovov will be completed in 2010.

Privatisation of a number of state-owned companies remains restricted by decrees approved by the President of Ukraine in 2008. The SPF has submitted its proposals to the Government with respect to lifting the relevant restrictions. If the Government and the President uphold the SPF proposal, these additional assets, including, among others, JSC “Turboatom” and four energy generating companies, may be offered for sale in 2010.

In light of the privatisations in 2007-2009 and the low level of 2010 privatisation receipts realised through the date of this Prospectus, no assurance can be made that budgeted privatisation receipts will be met in 2010. A significant shortfall in actual privatisation receipts compared to budgeted privatisation receipts may have negative effects on the performance of the State Budget and adversely affect the ability of Ukraine to perform its obligations under the Guarantee. See “*Economy of Ukraine – Privatisation*”.

Successful future privatisations will depend on the implementation of structural and other reforms. Meeting future privatisation receipt targets may also require the Government (with approval from the Parliament of Ukraine) to release for privatisation additional state-owned enterprises that are currently excluded from privatisation (as was the case with OJSC “Ukrtelecom”), as these enterprises may prove more attractive to investors than certain of the non-excluded businesses. In 2008, the SPF prepared the draft privatisation programme for 2008-2012 which was approved by Parliament in a second reading in February 2009, but rejected in May 2009. In July 2010, the SPF prepared its draft 2010-2014 privatisation programme. In the absence of a clear privatisation programme, not all of the privatisation receipts budgeted as forecasted may be realised, which may create or contribute to future budget deficits. Litigation and related court orders may also delay specific privatisations, as has occurred in the past, or prevent them altogether. See “*Economy of Ukraine — Privatisation*”. In addition, the failure to privatise key state-owned assets may reduce the willingness of multilateral organisations to provide financial support to Ukraine. See “– *Inability to obtain financing from external sources could affect Ukraine’s ability to meet financing expectations in its budget*”.

Ukraine’s developing legal system creates risks and uncertainties for investors in Ukraine and for participants in the Ukrainian economy.

Since independence in 1991, as Ukraine has been developing from a planned to a market-based economy, the Ukrainian legal system has also been developing to support this market-based economy. Ukraine’s legal system is, however, in transition and is, therefore, subject to greater risks and uncertainties than a more mature legal system. In particular, risks associated with the Ukrainian legal system include:

- inconsistencies between and among the Constitution of Ukraine and various laws, presidential decrees, governmental, ministerial and local orders, decisions, resolutions and other acts;
- provisions in the laws and regulations that are ambiguously worded or lack specificity and thereby raise difficulties when implemented or interpreted;
- it is not unusual in Ukraine for laws to be enacted with retroactive effect or to be published some time after their enactment;
- authority or guidance for interpreting provisions of Ukrainian legislation remains rare, particularly as regards the imperative or facultative character of many norms in the absence of an express indication established by law;
- difficulty in predicting the outcome of judicial application of Ukrainian legislation due to, amongst other factors, a general inconsistency in the judicial interpretation of such legislation in the same or similar cases; and
- the fact that not all Ukrainian resolutions, orders, decrees, decisions and similar governmental, regulatory and judicial acts are readily available to the public or available in comprehensibly organised form.

These and other factors that have an impact on Ukraine’s legal system make an investment in the Notes and the Guarantee subject to greater risks and uncertainties than an investment in a country with a more mature legal system.

Official economic data and third-party information may not be reliable.

Although a range of government ministries, along with the NBU and the State Statistics Committee of Ukraine, produce statistics on Ukraine and its economy, there can be no assurance that these statistics are as substantially complete or reliable as those compiled in many more developed countries. Prospective investors in the Notes and the Guarantee should be aware that figures relating to Ukraine's GDP and many other aggregate figures cited in this Prospectus may be subject to some degree of uncertainty and may not be fully in accordance with international standards.

Furthermore, standards of accuracy of statistical data may vary from ministry to ministry or from period to period due to the application of different methodologies. In this Prospectus, data are presented as provided by the relevant ministry to which the data is attributed, and no attempt has been made to reconcile such data to the data compiled by other ministries or by other organisations, such as the IMF. Since the first quarter of 2003, Ukraine has produced data in accordance with the IMF's Special Data Dissemination Standard.

There can be no assurance, however, that this IMF standard has been fully implemented or correctly applied. The existence of a sizeable unofficial or shadow economy may also affect the accuracy and reliability of statistical information. In addition, Ukraine has experienced variable rates of inflation, including periods of hyperinflation. Unless otherwise indicated, the information and figures presented in this Prospectus have not been restated to reflect such inflation and, as a result, period to period comparisons may not be meaningful. Prospective investors should be aware that none of these statistics have been independently verified.

Ukraine has also provided information on certain matters pertaining to documentation that belongs to independent third parties. In certain of these circumstances, Ukraine has relied on reported information in presenting such matters but is unable to independently verify such information.

Changes in relationships with western governments and institutions may affect competitiveness of Ukrainian manufacturers in export markets.

With effect from 16 May 2008, Ukraine became a member of the World Trade Organisation (the "WTO"). Ukraine continues to pursue the objective of achieving a closer relationship with the EU and developing practical cooperation with the North Atlantic Treaty Organisation ("NATO"). With effect from 30 December 2005, Ukraine was given market economy status by the EU, though without any immediate prospect of EU membership for Ukraine. See "*Political Framework – International Relations*".

Any major changes in Ukraine's relations with Western governments and institutions, in particular any such changes adversely affecting the ability of Ukrainian manufacturers to access or to fully compete in world export markets, may have negative effects on the economy and thus on the ability of Ukraine to perform its obligations under the Guarantee.

Ukraine has been identified by the media and analysts as having corruption and money laundering issues.

Independent analysts and media reports have identified corruption and money laundering as problems in Ukraine. Until February 2006, Ukraine was subject to monitoring by the Financial Action Task Force on Money Laundering and, until February 2004, was in its list of Non-Co-operative Countries and Territories. See "*Political Framework – The Judicial System and Legal Framework*". Any future allegations of corruption in Ukraine or evidence of money laundering could have a negative effect on the ability of Ukraine to attract foreign investment and, more generally, on the economy of Ukraine and thus on Ukraine's ability to perform its obligations under the Guarantee.

Uncertainties relating to the judicial system may hamper development of the economy.

The independence of the judicial system and its immunity from economic and political influences in Ukraine remain questionable. Although the Constitutional Court of Ukraine is the only body authorised to exercise constitutional jurisdiction and is generally viewed as impartial, the system of constitutional jurisdiction itself remains complicated and, accordingly, it is difficult to ensure smooth and effective removal of discrepancies between the Constitution and applicable Ukrainian legislation on the one hand and among various laws of Ukraine on the other hand.

The court system is understaffed and underfunded. Because Ukraine is a civil law jurisdiction, judicial decisions under Ukrainian law generally have no precedential effect. For the same reason, courts themselves are generally not bound by earlier decisions taken under the same or similar circumstances, which can result in the inconsistent application of Ukrainian legislation to resolve the same or similar disputes.

Not all Ukrainian legislation is readily available to the public or organised in a manner that facilitates understanding. Furthermore, to date only a relatively small number of judicial decisions have been publicly available and, therefore, the role of judicial decisions as guidelines in interpreting applicable Ukrainian legislation to the public at large is generally limited.

The Ukrainian judicial system has become more complicated and hierarchical as a result of the recent judicial reforms. The generally perceived result of these reforms is that the Ukrainian judicial system is now even slower than before.

All of these factors make judicial decisions in Ukraine difficult to predict and effective redress uncertain and court orders are not always enforced or followed by law enforcement institutions. The uncertainties of the Ukrainian judicial system could have a negative effect on the economy and thus on the ability of Ukraine to perform its obligations under the Guarantee.

Judicial or arbitral proceedings may result in significant foreign currency awards against Ukraine.

From time to time, Ukraine, its state agencies and its political subdivisions become involved in disputes with various parties. These disputes most often involve issues of trade or inward investment, and are typically brought before arbitral panels, although court proceedings also occur. In proceedings in which claims are asserted against Ukraine, an adverse decision could result in the award of substantial damages or other remedies.

In particular, Ukraine is currently involved in arbitration against the Russian company OJSC “Tatneft” (“Tatneft”). See *“The Political Framework of Ukraine – Legal Proceedings — Tatneft arbitration”*. The arbitration concerns disputes over the shareholder structure and management of CJSC “Ukratnafta”, a Ukrainian company. Tatneft has named Ukraine as party to the arbitration on the basis of allegations that Ukraine violated an agreement between the Ukrainian and Russian governments on mutual protection of investments. Tatneft is currently seeking awards in the amount of U.S.\$2.4 billion. Following oral hearings on jurisdictional matters held in March 2010, the arbitration tribunal is expected to render by the end of 2010 a decision whether it has jurisdiction to decide this case. If the tribunal accepts jurisdiction and returns an award adverse to Ukraine, Ukraine may become liable to pay significant damages denominated in a foreign currency.

In addition, on 24 February 2010, Mr Semenyi, a Russian citizen, filed a claim with the Moscow Arbitration Court against the Government of the Russian Federation and the Government of Ukraine. See *“The Political Framework of Ukraine – Legal Proceedings – Semenyi litigation”*. The claim alleges that Ukraine breached the national legislation rules and the Agreement between the Government of the Russian Federation and the Government of Ukraine on Avoidance of Double Taxation of Income and Property and Prevention of Tax Evasion dated 8 February 1995. In particular, the claim alleges that actions and failures to act of Ukrainian state authorities, including law enforcement authorities, resulted in the expropriation of the claimant’s income, property and proprietary and intangible rights owned by the claimant in OJSC “Vatra”. The amount of the claim is approximately 716 billion Russian roubles, equivalent to approximately U.S.\$23.6 billion. On 5 July 2010 the Moscow Arbitration Court ruled that the matter was not subject to consideration by an arbitration court and closed the proceedings. On 26 July 2010, the plaintiff filed with the Ninth Arbitration Appeal Court an appeal against the Moscow Arbitration Court ruling. On 23 August 2010, the Ninth Arbitration Appeal Court issued a ruling rejecting the plaintiff’s appeal and upholding the ruling of the Moscow Arbitration Court. The plaintiff can, however, further appeal against this ruling within two months from 23 August 2010.

An adverse decision in the Tatneft arbitration or the Semenyi litigation, or in other proceedings resulting in awards of substantial damages or other monetary remedies denominated in currency other than the hryvnia, could strain Ukraine’s foreign currency reserves and have a negative effect on its ability to perform its obligations under the Guarantee.

TERMS AND CONDITIONS OF THE NOTES

The following is the text of the terms and conditions of the Notes, which upon issue and subject to completion and amendment, will be endorsed on each Note Certificate (as defined below) and will be attached and (subject to the provisions thereof) apply to each Global Note.

The U.S.\$568,000,000 8.375 per cent. Guaranteed Notes due 2017 (the “**Notes**”, which expression includes any further notes issued pursuant to Condition 14 (*Further Issues*) and forming a single series therewith) of the State enterprise “FINANCING OF INFRASTRUCTURAL PROJECTS” (the “**Issuer**”) (i) are constituted by, are subject to, and have the benefit of, a trust deed dated 3 November 2010 (as amended or supplemented from time to time, the “**Trust Deed**”) between the Issuer, the Cabinet of Ministers of Ukraine (acting on behalf of Ukraine) represented by the Minister of Finance of Ukraine (the “**Guarantor**”) and BNY Corporate Trustee Services Limited as trustee (the “**Trustee**”, which expression includes all persons for the time being trustee or trustees appointed under the Trust Deed), (ii) have the benefit of a deed of guarantee dated 3 November 2010 (the “**Deed of Guarantee**”) executed and delivered by the Guarantor under which the Guarantor has guaranteed payment of all amounts payable by the Issuer under the Trust Deed, and the benefit of the Guarantee is held by the Trustee on trust for itself and for the Noteholders (as defined below) from time to time pursuant to the terms of the Trust Deed, and (iii) and are the subject of an agency agreement dated 3 November 2010 (as amended or supplemented from time to time, the “**Agency Agreement**”) between the Issuer, the Guarantor, The Bank of New York Mellon, New York Branch as New York Registrar (the “**New York Registrar**”), The Bank of New York Mellon (Luxembourg) S.A. as European Registrar (the “**European Registrar**”, and together with the New York registrar, the “**Registrars**”, which expression includes any successor registrar appointed from time to time in connection with the Notes), The Bank of New York Mellon as principal paying agent (the “**Principal Paying Agent**”, which expression includes any successor principal paying agent appointed from time to time in connection with the Notes), the transfer agent named therein (the “**Transfer Agent**”, which expression includes any successor or additional transfer agents appointed from time to time in connection with the Notes), the paying agents named therein (together with the Principal Paying Agent, the “**Paying Agents**”, which expression includes any successor or additional paying agents appointed from time to time in connection with the Notes) and the Trustee. References herein to the “**Agents**” are to the Registrars, the Principal Paying Agent, the Transfer Agent and the Paying Agents and any reference to an “**Agent**” is to any one of them. Certain provisions of these Conditions are summaries of the Trust Deed and the Agency Agreement and are subject to their detailed provisions. The Noteholders (as defined below) are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and the Agency Agreement applicable to them. Copies of the Trust Deed and the Agency Agreement are available for inspection by Noteholders during normal business hours at the registered office for the time being of the Trustee, being at the date hereof One Canada Square, London, E14 5AL, England and at the specified offices (as defined in the Agency Agreement) of each of the Agents, the initial specified offices of which are set out below.

1. Form, Denomination, Status and Guarantee

- (a) *Form and denomination:* The Notes are in registered form in the denominations of U.S.\$100,000 and integral multiples of U.S.\$1,000 in excess thereof (each, an “**Authorised Denomination**”).
- (b) *Status of the Notes:* The Notes constitute direct, general and unconditional obligations of the Issuer which will at all times rank *pari passu* among themselves and at least *pari passu* with all other present and future unsecured obligations of the Issuer save for such obligations as may be preferred by provisions of law that are both mandatory and of general application.
- (c) *Guarantee of the Notes:* The Guarantor has in the Deed of Guarantee unconditionally and irrevocably guaranteed the due and punctual payment of all sums from time to time payable by the Issuer in respect of the Notes. This guarantee (the “**Guarantee of the Notes**”) constitutes direct, general and unconditional obligations of the Guarantor which will at all times rank at least *pari passu* with all other present and future unsecured and unsubordinated obligations of the Guarantor except for obligations preferred by mandatory operation of law.

2. Register, Title and Transfers

- (a) *Register*: Title to the Notes will pass by transfer and registration as described in this Condition 2. The European Registrar and New York Registrar will each maintain a register (each, a “**Register**”) in respect of the Notes in accordance with the provisions of the Agency Agreement. In these Conditions, the “**Holder**” of a Note means the person in whose name such Note is for the time being registered in the Register (or, in the case of a joint holding, the first named thereof) and “**Noteholder**” shall be construed accordingly. A certificate (each, a “**Note Certificate**”) will be issued to each Noteholder in respect of its registered holding. Each Note Certificate will be numbered serially with an identifying number which will be recorded in the Register.
- (b) *Title*: The Holder of each Note shall (except as otherwise required by law) be treated as the absolute owner of such Note for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any other interest therein, any writing on the Note Certificate relating thereto (other than the endorsed form of transfer) or any notice of any previous loss or theft of such Note Certificate) and no person shall be liable for so treating such Holder. No person shall have any right to enforce any term or condition of the Notes or the Trust Deed under the Contracts (Rights of Third Parties) Act 1999.
- (c) *Transfers*: Subject to paragraphs (f) (*Closed periods*) and (g) (*Regulations concerning transfers and registration*) below, a Note may be transferred upon surrender of the relevant Note Certificate, with the endorsed form of transfer duly completed, at the Specified Office of the relevant Registrar or any Transfer Agent, together with such evidence as the relevant Registrar or (as the case may be) such Transfer Agent may reasonably require to prove the title of the transferor and the authority of the individuals who have executed the form of transfer; *provided, however, that* a Note may not be transferred unless the principal amount of Notes transferred and (where not all of the Notes held by a Holder are being transferred) the principal amount of the balance of Notes not transferred are Authorised Denominations. Where not all the Notes represented by the surrendered Note Certificate are the subject of the transfer, a new Note Certificate in respect of the balance of the Notes will be issued to the transferor.
- (d) *Registration and delivery of Note Certificates*: Within five business days of the surrender of a Note Certificate in accordance with paragraph (c) (*Transfers*) above, the relevant Registrar will register the transfer in question and deliver a new Note Certificate of the same principal amount to the Notes transferred to each relevant Holder at its Specified Office or (as the case may be) the Specified Office of any Transfer Agent or (at the request and risk of any such relevant Holder) by uninsured first class mail (airmail if overseas) to the address specified for the purpose by such relevant Holder. In this paragraph, “**business day**” means a day on which commercial banks are open for general business (including dealings in foreign currencies) in the city where the relevant Registrar or (as the case may be) the relevant Transfer Agent has its Specified Office.
- (e) *No charge*: The registration or transfer of a Note will be effected without charge by or on behalf of the Issuer, any Registrar or any Transfer Agent but against such indemnity as the Registrar or (as the case may be) such Transfer Agent may require in respect of any tax or other duty of whatsoever nature which may be levied or imposed in connection with such registration or transfer.
- (f) *Closed periods*: Noteholders may not require transfers to be registered during the period of 15 calendar days ending on the due date for any payment of principal or interest in respect of the Notes.
- (g) *Regulations concerning transfers and registration*: All transfers of Notes and entries on the Register are subject to the detailed regulations concerning the transfer of Notes scheduled to the Agency Agreement. The regulations may be changed by the Issuer with the prior written approval of the Trustee and the relevant Registrar. A copy of the current regulations will be mailed (free of charge) by the relevant Registrar to any Noteholder who requests in writing a copy of such regulations.

- (h) *Compulsory sale*: The Issuer may compel any beneficial owner of an interest of the Restricted Notes to sell its interest in such Notes, or may sell such interest on behalf of such holder, if such holder is a U.S. person (as defined in Regulation S) that is not a QIB and a QP. For these purposes:

QIB means a “qualified institutional buyer” within the meaning of Rule 144A;

QP means a “qualified purchaser” within the meaning of Section 2(a)(51)(A) of the U.S. Investment Company Act of 1940, as amended, and the rules and regulations thereunder;

Regulation S means Regulation S under the Securities Act;

Restricted Notes means the Notes which are offered and sold within the United States in reliance on Rule 144A under the Securities Act (“**Rule 144A**”) only to persons that are QIBs that are also QPs, acting for their own account or the account of one or more QIBs that are also QPs; and

Securities Act means the U.S. Securities Act of 1933, as amended.

3. Negative Pledge

So long as any Note remains outstanding (as defined in the Trust Deed), neither the Issuer nor the Guarantor shall grant or permit to be outstanding, and shall procure that there is not granted or permitted to be outstanding, any Lien (other than a Permitted Lien) over any of its present or future assets or revenues or any part thereof, to secure any External Indebtedness or Relevant Indebtedness, as the case may be, unless either the Issuer or the Guarantor, as relevant, shall (i) before or at the same time procure that the Notes and the Trust Deed are secured equally and rateably therewith to the satisfaction of the Trustee or (ii) promptly thereafter ensure that the Notes and the Trust Deed have the benefit of such other Lien as the Trustee deems not materially less beneficial to the interests of the Noteholders or as is approved by an Extraordinary Resolution (as defined in the Trust Deed) of the Noteholders.

In these Conditions:

“**External Indebtedness**” means any Indebtedness of the Issuer which is payable in or by reference to a currency which is not the lawful currency for the time being of Ukraine or to a Person resident outside Ukraine;

“**Indebtedness**” means any indebtedness of any Person for money borrowed or raised including (without limitation) any indebtedness for or in respect of:

- (a) amounts raised by acceptance under any acceptance credit facility;
- (b) amounts raised under any note purchase facility;
- (c) the amount of any liability in respect of leases or hire purchase contracts which would, in accordance with applicable laws and generally accepted accounting principles, be treated as finance or capital leases;
- (d) the amount of any liability in respect of any purchase price for assets or services the payment of which is deferred for a period in excess of 60 days; and
- (e) amounts raised under any other transaction (including, without limitation, any forward sale or purchase agreement) having the commercial effect of a borrowing;

“**Lien**” means any mortgage, charge, pledge, lien or other security interest (but excluding any Lien arising by operation of law or pursuant to the judgment of any court in respect of the Old Notes and/or the Old Loans);

“**Old Notes**” means any and all of the outstanding Deutsche Mark denominated 16 per cent. Notes due 2001 issued on a fiduciary basis by Chase Manhattan Bank Luxembourg S.A. (the “**DM Notes**”) as may be amended from time to time;

“**Old Loan**” means any and all of the outstanding Deutsche Mark denominated loan made to Ukraine by Chase Manhattan Bank Luxembourg S.A. in furtherance of the DM Notes;

“**Permitted Liens**” means:

- (a) any Lien arising by operation of law which has not been foreclosed or otherwise enforced against the assets to which it applies; or
- (b) any Lien existing on any property at the time of its acquisition; or
- (c) any Lien upon any property to secure indebtedness incurred for the purpose of financing the acquisition of such property (or property which forms part of a class of assets of a similar nature where the Lien is by reference to the constituents of such class from time to time); or
- (d) any Lien securing or providing for the payment of indebtedness incurred in connection with any Project Financing provided that such Lien applies solely to (x) any property which is, or forms part of, the subject of such Project Financing or (y) revenues or claims which arise from the operation, failure to meet specifications, exploitation, sale or loss, or failure to complete or damage to, any such property; or
- (e) any renewal or extension of any Lien described in sub-paragraphs (b) to (d) above, provided that the principal amount of the indebtedness secured thereby is not increased;

“**Person**” means any individual, company, corporation, firm, partnership, joint venture, association, unincorporated organisation, trust or any other entity, including, without limitation, state, state authority or agency of a state or other entity, whether or not having separate legal personality;

“**Project Financing**” means any arrangement for the provision of funds which are to be used solely to finance a project for the acquisition, construction, development or exploitation of any property pursuant to which the Persons providing such funds agree that the principal source of repayment of such funds will be the project and the revenues (including insurance proceeds) generated by such project;

“**Relevant Indebtedness**” means any indebtedness (whether being any principal, premium, interest or other amounts constituting such indebtedness), present or future, of the Guarantor in the form of or represented by notes, bonds or other similar instruments whether or not:

- (a) incurred by means of a loan, the making of which has been directly funded by the issue by a fiduciary (or other person whose liability is conditional upon the payments due in respect of the loan) of notes, bonds or other similar instruments; or
- (b) issued directly by the Guarantor,

where, in any such case, such notes, bonds or other similar instruments are:

- (i) capable of being traded on any stock exchange or other securities market; and
- (ii) denominated in a currency other than the legal currency of Ukraine.

4. Interest

The Notes bear interest from and including 3 November 2010 (the “**Issue Date**”) at the rate of 8.375 per cent. per annum, (the “**Rate of Interest**”) payable semi-annually in arrear on 3 May and 3 November in each year (each, an “**Interest Payment Date**”), commencing on 3 May 2011, subject as provided in Condition 6 (*Payments*).

Each Note will cease to bear interest from the due date for redemption unless on any portion of outstanding amount, payment of principal is improperly withheld or refused, in which case it will continue to bear interest at such rate (both before and after judgment) until whichever is the earlier of (a) the day on which all sums due in respect of such Note up to that day are received by or on behalf of the relevant Noteholder

and (b) the day which is seven calendar days after the Principal Paying Agent or the Trustee has notified the Noteholders that it has received all sums due in respect of the Notes up to such seventh calendar day (except to the extent that there is any subsequent default in payment).

The amount of interest payable on each Interest Payment Date shall be U.S.\$4,187.50 in respect of each Note of U.S.\$100,000 denomination and a proportionately higher amount in respect of each Note of a higher denomination. If interest is required to be paid in respect of a Note on any other date, it shall be calculated by applying the Rate of Interest to the Calculation Amount, multiplying the product by the relevant Day Count Fraction, rounding the resulting figure to the nearest cent (half a cent being rounded upwards) and multiplying such rounded figure by a fraction equal to the Authorised Denomination of such Note divided by the Calculation Amount, where “**Calculation Amount**” means U.S.\$1,000 and “**Day Count Fraction**” means, in respect of any period, the number of calendar days in the relevant period divided by 360 (the number of calendar days to be calculated on the basis of a year of 360 days with 12 30-day months).

5. Redemption and Purchase

- (a) *Scheduled redemption*: Unless previously redeemed, or purchased and cancelled, the Notes will be redeemed at their principal amount on 3 November 2017 (the “**Maturity Date**”), subject as provided in Condition 6 (*Payments*).
- (b) *Purchase*: The Issuer, the Guarantor or any agency, body or entity (incorporated or otherwise) of, or owned or controlled by, the Guarantor (a “**Guarantor Subsidiary**”) may at any time purchase Notes in the open market or otherwise and at any price. Any Notes so purchased may be cancelled or held and resold. Any Notes so purchased, while held by or on behalf of the Issuer, the Guarantor or any Guarantor Subsidiary shall not entitle the holder to vote at any meeting of holders of Notes and shall not be deemed to be outstanding for the purposes of, among other things, calculating quorums and meetings of holders of Notes.
- (c) *Cancellation*: All Notes so redeemed or purchased by or on behalf of the Issuer, the Guarantor or any Guarantor Subsidiary may be cancelled or reissued and resold by the Issuer and all Notes redeemed by the Issuer shall be cancelled.
- (d) *Issuer Call*: The Issuer may, on or after 3 November 2015, having given:
 - (i.) not less than 60 nor more than 75 days’ notice to the Holders in accordance with Condition 15 (*Notices*); and
 - (ii.) not less than 15 days before the giving of the notice referred to in (i), notice to the Principal Paying Agent, the Registrar and the Trustee,

which notices shall be irrevocable and shall specify the date fixed for redemption, redeem all but not some only of the Notes then outstanding on such date at a redemption price per Note equal to the greater of (i) 102 per cent. of the principal amount of the Note plus accrued and unpaid interest thereon, if any, to but excluding the date of redemption of the Notes or (ii) as determined by an Independent Investment Banker, the sum of the present values of the principal amount of such Note and each scheduled interest payment thereon up to and including the Maturity Date, in each case discounted to the date of actual redemption of the Notes on a semi-annual basis (using the same interest rate convention as that used in computing interest on the Notes) at the Treasury Rate plus 0.50 per cent., plus any accrued and unpaid interest on such Note and any other additional amounts payable in respect of such Note.

In this Condition 5(d):

“**H.15 (519)**” means the weekly statistical release designated as such, or any successor publication, published by the Board of Governors of the United States’ Federal Reserve System;

“**Independent Investment Banker**” means an independent investment banking institution of international standing in the U.S. dollar denominated bond markets appointed by the Issuer and the Guarantor; and

“**Treasury Rate**” means the annual rate equal to the semi-annual yield to maturity for United States Treasury securities maturing on the Maturity Date and trading in the public securities markets in the United States either:

- (i) as determined by interpolation between the most recent weekly average yield to maturity for two series of United States Treasury securities trading in the public securities markets in the United States, with one series maturing as close as possible to, but earlier than, the Maturity Date, and the other series maturing as close as possible to, but later than, the Maturity Date, in each case as published in the most recent H.15 (519); or
- (ii) if the weekly average yield to maturity for United States Treasury securities maturing on the Maturity Date is reported in the most recent H.15 (519), this weekly average yield to maturity as published in such H.15 (519).

6. **Payments**

- (a) *Payments in respect of the Notes:* Payments of principal and interest shall be made by transfer to a U.S. dollar account maintained by the payee with a bank in New York City and (in the case of redemption or interest payable on redemption, as applicable) upon surrender (or, in the case of part payment only, endorsement) of the relevant Note Certificates at the specified office of any Paying Agent.
- (b) *Payments subject to fiscal laws:* All payments in respect of the Notes are subject in all cases to any applicable fiscal or other laws and regulations, but without prejudice to the provisions of Condition 7 (*Taxation*). No commissions or expenses shall be charged to the Noteholders in respect of such payments.
- (c) *Payments on business days:* Payment instructions (for value the due date, or, if the due date is not a business day, for value the next succeeding business day) will be initiated (i) (in the case of payments of principal and interest payable on redemption) on the later of the due date for payment and the day on which the relevant Note Certificate is surrendered (or, in the case of part payment only, endorsed) at the Specified Office of a Paying Agent and (ii) (in the case of payments of interest payable other than on redemption) on the due date for payment. A Holder of a Note shall not be entitled to any interest or other payment in respect of any delay in payment resulting from the due date for a payment not being a business day. In this paragraph, “**business day**” means any day on which banks are open for general business (including dealings in foreign currencies) in New York City and, in the case of surrender (or, in the case of part payment only, endorsement) of a Note Certificate, in the place in which the Note Certificate is surrendered (or, as the case may be, endorsed).
- (d) *Partial payments:* If a Paying Agent makes a partial payment in respect of any Note, the Issuer shall procure that the amount and date of such payment are noted on the Register and, in the case of partial payment upon presentation of a Note Certificate, that a statement indicating the amount and the date of such payment is endorsed on the relevant Note Certificate.
- (e) *Record date:* Each payment in respect of a Note will be made to the person shown as the Holder in the Register at the opening of business in the place of the relevant Registrar’s Specified Office on the fifteenth day before the due date for such payment (the “**Record Date**”).

7. **Taxation**

All payments of principal and interest in respect of the Notes by or on behalf of the Issuer or the Guarantor shall be made free and clear of, and without withholding or deduction for or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or on behalf of Ukraine or any political subdivision thereof or any authority therein

or thereof having power to tax, unless the withholding or deduction of such taxes, duties, assessments or governmental charges is required by law. In that event, the Issuer or (as the case may be) the Guarantor shall pay such additional amounts as will result in receipt by the Noteholders of such amounts after such withholding or deduction as would have been received by them had no such withholding or deduction been required, except that no such additional amounts shall be payable in respect of any Note:

- (a) held by a Holder which is liable to such taxes, duties, assessments or governmental charges in respect of such Note by reason of its having some connection with the jurisdiction by which such taxes, duties, assessments or charges have been imposed, levied, collected, withheld or assessed other than the mere holding of the Note; or
- (b) to a Holder, or to a third party on behalf of a Holder, who would not be liable or subject to the withholding or deduction of Taxes by making a declaration of non residence or other similar claim for exemption to the relevant tax authority; or
- (c) held by a Holder who would have been able to avoid such withholding or deduction by arranging to receive the relevant payment through another Paying Agent in a member state of the European Union; or
- (d) where (in the case of a payment of principal or interest on redemption) the relevant Note Certificate is surrendered for payment more than 30 calendar days after the Relevant Date except to the extent that the relevant Holder would have been entitled to such additional amounts if it had surrendered the relevant Note Certificate on the last day of such period of 30 calendar days; or
- (e) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC on taxation of savings income or any law implementing or complying with, or introduced in order to conform to, this Directive.

In these Conditions, “**Relevant Date**” means whichever is the later of (1) the date on which the payment in question first becomes due and (2) if the full amount payable has not been received in New York City by the Principal Paying Agent or the Trustee on or prior to such due date, the date on which (the full amount having been so received) notice to that effect has been given to the Noteholders.

Any reference in these Conditions to principal or interest shall be deemed to include any additional amounts in respect of principal or interest (as the case may be) which may be payable under this Condition 7 (*Taxation*) or any undertaking given in addition to or in substitution of this Condition 7 (*Taxation*) pursuant to the Trust Deed.

8. Events of Default

If any of the following events occurs and is continuing, then the Trustee at its discretion may and, if so requested in writing by Holders of at least one quarter of the aggregate principal amount of the outstanding Notes or if so directed by an Extraordinary Resolution, shall (subject, in the case of the happening of any of the events mentioned in paragraphs (k) (*Unlawfulness*) to (l) (*Invalidity*) below in so far as it relates to an obligation other than a payment obligation, to the Trustee having certified in writing that the happening of such event is in its opinion materially prejudicial to the interests of the Noteholders and, in all cases, to the Trustee having been indemnified and/or pre-funded and/or provided with security to its satisfaction) give written notice to the Issuer declaring the Notes to be immediately due and payable, whereupon they shall become immediately due and payable at their principal amount together with accrued interest without further action or formality:

- (a) *Non-payment by the Issuer*: the Issuer fails to pay any amount of principal, premium or interest in respect of the Notes on the due date for payment thereof and default continues for a period of 10 days; or
- (b) *Breach of Guarantor’s obligations*: the Guarantor defaults in the performance or observance of any of its obligations under or in respect of the Notes, the Trust Deed or the Deed of Guarantee (except that such default shall not include any default that would constitute an Event of Default under (k)

- (Unlawfulness) or (l) (Invalidity) below) and such default (i) is, in the opinion of the Trustee, incapable of remedy or (ii) being a default which is, in the opinion of the Trustee, capable of remedy, remains unremedied for 30 calendar days after the Trustee has given written notice thereof to the Guarantor; or
- (c) *Indebtedness*: if any Relevant Indebtedness shall become due and payable prior to the stated maturity thereof following a default or any security therefor becomes enforceable or the Guarantor fails to make any payment of any Relevant Indebtedness on the due date for payment thereof or, if applicable, at the expiration of any grace period originally applicable thereto or any guarantee of, or indemnity in respect of, any Relevant Indebtedness of any other Person given by the Guarantor shall not be honoured when due and called upon; *provided that* the aggregate amount of such Relevant Indebtedness is in excess of euro 25,000,000 (or its equivalent in any currency or currencies) and provided further that the acceleration of the maturity of or any payment default in respect of any Old Notes or the Old Loan will not constitute an Event of Default; or
 - (d) *Authorisation*: if any authorisation, consent of, or filing or registration with, any governmental authority necessary for the performance of any payment obligation of the Guarantor under the Deed of Guarantee or Trust Deed when due, ceases to be in full force and effect or remain valid and subsisting; or
 - (e) *Moratorium*: if the Guarantor shall suspend payment of, or admit its inability to pay, Relevant Indebtedness or any part thereof, or declare a general moratorium on or in respect of Relevant Indebtedness or any part thereof or anything analogous to the foregoing shall occur in each case other than with respect to Old Notes or the Old Loan; or
 - (f) *Unsatisfied judgment*: one or more judgment(s) or order(s) for the payment of an amount in excess of U.S.\$100,000 (or its equivalent in any other currency or currencies, whether individually or in aggregate) is rendered against the Issuer, or any of the Issuer's subsidiaries and continue(s) unsatisfied and unstayed for a period of 30 days after the date(s) thereof or, if later, the date therein specified for payment; or
 - (g) *Security enforced*: a secured party takes possession, or a receiver, manager or other similar officer is appointed, of the whole or a substantial (in the opinion of the Trustee) part of the undertaking, assets and revenues of the Issuer, or any of its respective subsidiaries; or
 - (h) *Insolvency, etc.*: (i) the Issuer, or any of its respective subsidiaries becomes insolvent or is unable to pay its debts as they fall due, (ii) an administrator or liquidator of the Issuer, or any of its respective subsidiaries or the whole or a substantial (in the opinion of the Trustee) part of the undertaking, assets and revenues of the Issuer, or any of its respective subsidiaries is appointed (or application for any such appointment is made), (iii) the Issuer, or any of its respective subsidiaries takes any action for a readjustment or deferment of any of its obligations or makes a general assignment or an arrangement or composition with or for the benefit of its creditors or declares a moratorium in respect of any of its External Indebtedness or any guarantee of any External Indebtedness given by it or (iv) the Issuer, or any of its respective Subsidiaries ceases or threatens to cease to carry on all or any substantial part of its business); or
 - (i) *Winding up, etc.*: an order is made or an effective resolution is passed for the winding up, liquidation or dissolution of the Issuer, or any of its subsidiaries; or
 - (j) *Analogous event*: any event occurs in respect of the Issuer or any of its subsidiaries which under the laws of Ukraine has an analogous effect to any of the events referred to in paragraphs (g) (*Security enforced*) to (i) (*Winding up, etc.*) above; or
 - (k) *Unlawfulness*: it is or will become unlawful for the Guarantor to perform or comply with any of its obligations under the Deed of Guarantee or Trust Deed; or
 - (l) *Invalidity*: any one or more of the Guarantor's obligations under the Deed of Guarantee becomes unenforceable or invalid, or the Guarantor contests the validity of the obligation in question.

9. Prescription

Claims for payment of principal and interest in respect of the Note Certificates shall become void unless made within periods of ten years (in case of principal) and five years (in case of interest) after the appropriate Relevant Date.

10. Replacement of Note Certificates

If any Note Certificate is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the Specified Office of the relevant Registrar and the Transfer Agent, subject to all applicable laws and stock exchange requirements, upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer may reasonably require. Mutilated or defaced Note Certificates must be surrendered before replacements will be issued.

11. Trustee and Agents

Under the Trust Deed, the Trustee is entitled to be indemnified and relieved from responsibility in certain circumstances and to be paid its costs and expenses in priority to the claims of the Noteholders. In addition, the Trustee is entitled to enter into business transactions with the Issuer, the Guarantor and any entity relating to the Issuer or the Guarantor without accounting for any profit.

In connection with the exercise by it of any of its trusts, powers, authorities and discretions (including, without limitation, any modification, waiver, authorisation, determination or substitution), the Trustee shall have regard to the general interest of the Noteholders as a class but shall not have regard to any interests arising from circumstances particular to individual Noteholders (whatever their number) and, in particular but without limitation, shall not have regard to the consequences of any such exercise for individual Noteholders (whatever their number) resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory or any political sub division thereof and the Trustee shall not be entitled to require, nor shall any Noteholder be entitled to claim, from the Issuer, the Trustee or any other person any indemnification or payment in respect of any tax consequence of any such exercise upon individual Noteholders except to the extent already provided for in Condition 7 (*Taxation*) and/or any undertaking given in addition to, or in substitution for, Condition 7 (*Taxation*) pursuant to the Trust Deed.

In acting under the Agency Agreement and in connection with the Notes, the Agents act solely as agents of the Issuer, the Guarantor and (to the extent provided therein) the Trustee and do not assume any obligations towards or relationship of agency or trust for or with any of the Noteholders.

The initial Agents and their initial Specified Offices are listed below. The Issuer and the Guarantor reserve the right (with the prior approval of the Trustee) at any time to vary or terminate the appointment of any Agent and to appoint a successor registrar, principal paying agent, agent bank and additional or successor paying agents and transfer agents; *provided, however, that* the Issuer and the Guarantor shall at all times maintain (a) a principal paying agent and a registrar and (b) a paying agent in an EU member state that will not be obliged to withhold or deduct tax pursuant to any law implementing European Council Directive 2003/48/EC.

Notice of any change in any of the Agents or in their Specified Offices shall promptly be given to the Noteholders.

12. Meetings of Noteholders; Modification and Waiver; Substitution

- (a) *Meetings of Noteholders*: The Trust Deed contains provisions for convening meetings of Noteholders to consider matters relating to the Notes, including the modification of any provision of these Conditions, the Trust Deed or the Deed of Guarantee. Any such modification may be made if sanctioned by an Extraordinary Resolution. Such a meeting may be convened by the Issuer and the Guarantor (acting together) or by the Trustee and shall be convened by the Trustee subject to the Trustee being indemnified and/or pre-funded and/or secured to its satisfaction against all Liabilities

thereby occasioned upon the request in writing of Noteholders holding not less than one-tenth of the aggregate principal amount of the outstanding Notes. The quorum at any meeting convened to vote on an Extraordinary Resolution will be two or more persons holding or representing one more than half of the aggregate principal amount of the outstanding Notes or, at any adjourned meeting, two or more persons being or representing Noteholders whatever the principal amount of the Notes held or represented; *provided, however, that* certain proposals (including any proposal to change any date fixed for payment of principal or interest in respect of the Notes, to reduce the amount of principal or interest payable on any date in respect of the Notes, to alter the method of calculating the amount of any payment in respect of the Notes or the date for any such payment, to change the currency of payments under the Notes, to amend the terms of the Guarantee of the Notes or to change the quorum requirements relating to meetings or the majority required to pass an Extraordinary Resolution (each, a “**Reserved Matter**”)) may only be sanctioned by an Extraordinary Resolution passed at a meeting of Noteholders at which one or more persons holding or representing not less than two-thirds or, at any adjourned meeting, one third of the aggregate principal amount of the outstanding Notes form a quorum. Any Extraordinary Resolution duly passed at any such meeting shall be binding on all the Noteholders, whether present or not.

In addition, a resolution in writing signed by or on behalf of all Noteholders who for the time being are entitled to receive notice of a meeting of Noteholders under the Trust Deed will take effect as if it were an Extraordinary Resolution. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Noteholders.

- (b) *Modification and waiver:* The Trustee may, without the consent of the Noteholders, agree to any modification of these Conditions or the Trust Deed or the Deed of Guarantee (other than in respect of a Reserved Matter) which is, in the opinion of the Trustee, proper to make if, in the opinion of the Trustee, such modification will not be materially prejudicial to the interests of Noteholders and to any modification of the Notes or the Trust Deed which is of a formal, minor or technical nature or is to correct a manifest error.

In addition, the Trustee may, without the consent of the Noteholders, authorise or waive any proposed breach or breach by the Issuer or the Guarantor of the Notes, the Trust Deed (other than a proposed breach or breach relating to the subject of a Reserved Matter) or Deed of Guarantee, if in the opinion of the Trustee, the interests of the Noteholders will not be materially prejudiced thereby.

Unless the Trustee agrees otherwise, any such authorisation, waiver or modification shall be notified to the Noteholders as soon as practicable thereafter.

- (c) *Substitution:* the Trust Deed contains provisions under which the Trustee may, without the consent of the Noteholders, agree that the Guarantor or any other company may assume the obligations of the Issuer as principal debtor under the Trust Deed and the Notes *provided that* certain conditions specified in the Trust Deed are fulfilled, including, in the case of a substitution of the Issuer by a company other than the Guarantor, a requirement that the Guarantee of the Notes is fully effective in relation to the obligations of the new principal debtor under the Trust Deed and the Notes.

No Noteholder shall, in connection with any substitution, be entitled to claim any indemnification or payment in respect of any tax consequence thereof for such Noteholder, except to the extent provided for in Condition 7 (*Taxation*) (or any undertaking given in addition to or substitution for it pursuant to the provisions of the Trust Deed).

13. Enforcement

The Trustee may at any time, at its discretion and without notice, institute such proceedings as it thinks fit to enforce its rights under the Trust Deed and the Deed of Guarantee in respect of the Notes, *provided, however, that:*

- (a) the Deed of Guarantee provides that if the Guarantor fails to pay any amount of principal, premium or interest in respect of the Notes in accordance with Clauses 2.1 or 2.2 of the Deed of Guarantee (a

“**Non-Payment**”), the Trustee shall not be entitled to call for payment or take any other action to enforce its rights under the Deed of Guarantee in respect of such Non-Payment unless a Default Event occurs (where “**Default Event**” means an Non-Payment which continues for a period of 10 days or more); and

- (b) in all circumstances the Trustee shall not be bound to do so unless:
 - (i) it has been so requested in writing by the Holders of at least one quarter of the aggregate principal amount of the outstanding Notes or has been so directed by an Extraordinary Resolution; and
 - (ii) it has been indemnified and/or pre-funded and/or provided with security to its satisfaction.

No Noteholder may proceed directly against the Issuer or the Guarantor unless the Trustee, having become bound to do so, fails to do so within a reasonable time and such failure is continuing.

14. Further Issues

The Issuer may from time to time, without the consent of the Noteholders and in accordance with the Trust Deed, create and issue further notes having the same terms and conditions as the Notes in all respects (or in all respects except for the first payment of interest) so as to form a single series with the Notes, even if further Notes have original issue discount (“**OID**”) for U.S. federal income tax purposes and even if doing so may adversely affect the value of the original Notes. The Issuer may from time to time, with the consent of the Trustee, create and issue other series of notes having the benefit of the Trust Deed.

15. Notices

Notices to the Noteholders will be sent to them by first class mail (or its equivalent) or (if posted to an overseas address) by airmail at their respective addresses on the relevant Register. Any such notice shall be deemed to have been given on the fourth day after the date of mailing provided that for so long as the Notes are listed on the Irish Stock Exchange, notice will also be provided either via the Companies Announcement Office of the Irish Stock Exchange or in the Irish Times. Any such notice shall be deemed to have been given on the date of such publication.

16. Currency Indemnity

The Issuer agrees that if a judgment, order or award given or made by any court or arbitral tribunal for the payment of any amount in respect of any Note is expressed in a currency (the “**judgment currency**”) other than U.S. dollars (the “**denomination currency**”), the Issuer will pay any deficiency arising or resulting from any variation in rates of exchange between the date as of which the amount in the denomination currency is notionally converted into the amount in the judgment currency for the purposes of such judgment, order or award and the date of actual payment thereof. This obligation will constitute a separate and independent obligation from the other obligations under the Notes, will give rise to a separate and independent cause of action, will apply irrespective of any waiver or extension granted from time to time and will continue in full force and effect notwithstanding any judgment, order or award for a liquidated sum or sums in respect of amounts due in respect of the relevant Note or under any such judgment, order or award for a liquidated sum or sums in respect of amounts due in respect of the relevant Note or under any such judgment, order or award.

17. Governing Law and Jurisdiction

- (a) *Governing law:* The Notes and the Trust Deed and any non-contractual obligations arising out of or in connection with the Notes and the Trust Deed are governed by English law.
- (b) *English Courts:* Subject to Condition 17(c) (*Arbitration*), the Courts of England shall have jurisdiction to settle any dispute arising out of or in connection the Notes or the Trust Deed (including a dispute regarding the existence, validity or termination of the Notes or the Trust Deed or the consequences of

their nullity) (a “**Dispute**”). The Issuer, the Guarantor and the Trustee agree that, subject to Condition 17(c) (*Arbitration*), the Courts of England are the most appropriate and convenient courts to settle any Dispute and accordingly no party will argue to the contrary. This Condition 17(b) (*English Courts*) is for the benefit of the Trustee only. As a result the Trustee may take proceedings relating to a Dispute (the “**Proceedings**”) in any other courts with jurisdiction. To the extent allowed by law, the Trustee may take concurrent Proceedings in any number of jurisdictions.

- (c) *Arbitration*: At the option of any of the Issuer, Guarantor or the Trustee, a Dispute shall be settled by arbitration in accordance with the Rules of the London Court of International Arbitration as at present in force, with the exception of Article 6 which shall not apply, (the “**Rules**”) by a tribunal of three arbitrators (or a sole arbitrator if the parties to the Dispute so agree) appointed in accordance with the Rules. If any Party elects for arbitration, the parties shall take the steps necessary to terminate any court proceedings relating to the Dispute. The seat of any arbitration shall be London, England. The language of any arbitral proceedings shall be English. For the purposes of arbitration pursuant to this Condition, the parties waive any right of application to determine a preliminary point of law or appeal on a point of law under sections 45 and 69 of the Arbitration Act 1996.
- (d) *Process agent*: Each of the Issuer and the Guarantor irrevocably appoint the Ambassador of Ukraine to the United Kingdom of Great Britain and Northern Ireland at the Embassy of Ukraine in London, to act as their respective authorised agents for service of process in England and agree that failure by the relevant process agent to notify the Issuer or the Guarantor of the process will not invalidate the proceedings concerned. Nothing in these Terms and Conditions shall affect the right of the Trustee to serve process in any other manner permitted by law. The Issuer and the Guarantor irrevocably agree not to contest or otherwise object to the validity of service of process in accordance with this Condition 17 (d) on the ground of any immunity or inviolability of its Ambassador or any other member of its diplomatic or consular staff or of the premises of its diplomatic mission or consular post in the United Kingdom.
- (e) *Waiver of immunity*: To the extent that each of the Issuer and the Guarantor may in any jurisdiction claim for itself or its assets or revenues any immunity from suit, from measures to secure the recognition and/or enforcement of a judgment or an arbitral award, from attachment in aid of execution of judgment, from execution of a judgment or arbitral award, from enforcement of an arbitral award or from any other legal or judicial process or remedy (other than pre-judgment attachment which is expressly not waived), and to the extent that in any such jurisdiction there shall be attributed such an immunity, each of the Issuer and the Guarantor irrevocably waives such immunity under Ukrainian law and waives such immunity to the fullest extent permitted by the laws of any other jurisdiction. Such waiver of immunity constitutes only a limited and specific waiver by each of the Issuer and the Guarantor for the purposes of the Notes or any related judgment or award and under no circumstances shall it be construed as a general waiver by the Issuer or the Guarantor or a waiver with respect to proceedings unrelated to the Notes. Each of the Issuer and the Guarantor reserves the right to plead sovereign immunity under the United States Foreign Sovereign Immunities Act of 1976 with respect to such actions brought against it under United States federal or state securities law. The Guarantor does not waive any immunity and/or inviolability in respect of (a) property used by a diplomatic or consular mission of Ukraine (except as may be necessary to effect service of process), (b) property of a military character and under the control of a military authority or defence agency or (c) property located in Ukraine and dedicated to a public or governmental use (as distinct to property dedicated to a commercial use).

USE OF PROCEEDS

In April 2007, the Executive Committee of the Union of European Football Associations (“**UEFA**”), the controlling body for European football, announced that a joint bid by Poland and Ukraine to host the 2012 UEFA European Football Championship (“**Euro 2012**”) had been successful and that accordingly Euro 2012 would be held partly in Poland and partly in Ukraine.

The proceeds from the issuance of the Notes will be used to finance the performance of tasks and actions provided by the “State Purpose Programme for the Preparation and Holding in Ukraine of the European Football Championship Finals in 2012” approved by the Resolution of the Cabinet of Ministers of Ukraine “On Approval of the State Purpose Programme for Preparation and Holding in Ukraine of the European Football Championship Finals in 2012” dated of 14 April 2010 No. 357 (the “**Programme**”) which use of proceeds corresponds with the aim of the Issuer, as established by its constitutional documents, specifically to finance the reconstruction of the Olimpiysky Stadium in the city of Kyiv, the construction of a stadium with approximately 33,400 seats in the city of Lviv, the expansion of the Donetsk International Airport, the expansion of Lviv International Airport, the renovation of Kyiv Sports Palace in order for it to be used as a mass media centre and the establishment of the infrastructure necessary to host a successful Euro 2012 championship in Ukraine.

DESCRIPTION OF THE ISSUER

Establishment and Legal Ownership

State enterprise “FINANCING OF INFRASTRUCTURAL PROJECTS” (the “**Issuer**”) was established as a state enterprise by the Order of the National Agency on Preparation and Holding in Ukraine of the UEFA Euro 2012 On Establishment of State Enterprise “FINANCING OF INFRASTRUCTURAL PROJECTS” dated 7 September 2010, No. 115. By virtue of its charter, the Issuer has the status of a legal entity under Ukrainian law and its registration number is 37264503. The Issuer is supervised by the Agency (as defined below) but is wholly-owned by the State. The principal offices of the Issuer are located at 1, Sportyvna Ploscha, the City of Kyiv, Ukraine and its telephone number is +380 44 281 9998.

Objectives

The functions of the Issuer are set out in its charter. The primary task of the Issuer is to provide financing for the implementation of the tasks and events in pursuance of the Programme by raising capital on the domestic and international finance markets.

No year-end financial statements have been produced by the Issuer as at the date of this Prospectus.

Management and Employees

The Agency, as the founder of the Issuer, acts as the asset management body with respect to the Issuer. The day-to-day management of the Issuer is performed by its director, who is appointed by the Agency. The director of the Issuer is authorised to act on behalf of the Issuer without proxy, open bank accounts for the Issuer, sign contracts on behalf of the Issuer (although the execution of contracts the value of which exceeds UAH 50,000.00 require prior approval and authorisation from the Agency) and perform certain other functions listed in the constitutional documents of the Issuer. Currently, Oksana Serdiuk acts as director of the Issuer.

The distribution of management rights with respect to the Issuer between the Issuer’s director and the Agency, which manages the Issuer on behalf of the state of Ukraine, is defined in the Issuer’s charter. In accordance with the Issuer’s charter the operational (day-to-day) management of the Issuer is performed by its director. The management rights of the Agency are limited to such rights as, inter alia, making decisions on any reorganisation of the Issuer, the approval of amendments to the Issuer’s charter, the preliminary approval of certain contracts of the Issuer and execution of contracts with the Issuer’s director. Management rights of the Issuer’s director include such rights as, inter alia, the disposal of the Issuer’s assets, the signing of agreements on behalf of the Issuer and the opening and closing of bank accounts.

Pursuant to the Commercial Code of Ukraine, the organs of the State power of Ukraine, such as the Agency, may not arbitrarily interfere in the operational management of the Issuer.

The business address of the acting director is 1, Sportyvna Ploscha, the City of Kyiv, Ukraine.

There are no potential conflicts of interest between the duties to the Issuer of the person listed above and her private interests or other duties.

DESCRIPTION OF THE AGENCY

Establishment and Legal Ownership

The National Agency on Preparation and Holding in Ukraine of the UEFA Euro 2012 (the “**Agency**”) was established by the Resolution of the Cabinet of Ministers of Ukraine “On Arrangements to Improve the Management System for Preparation and Holding in Ukraine of the European Football Championship Finals in 2012” dated 7 April 2010, No. 298, as a central organ of executive power with the status of a legal entity under Ukrainian law and whose activities are directed and coordinated by the Cabinet of Ministers of Ukraine. The Cabinet of Ministers of Ukraine is capable of changing, without further explanation, the status or capacity of the Agency. The offices of the Agency are located at 2 Mechnikova str., Kyiv, Ukraine.

An agency with the same name as the Agency was previously created by the government of Ukraine in 2007, tasked with the same principal objective as the Agency. However, this agency was liquidated at the end of 2008 as it was deemed to have insufficient capacity to achieve its principal objective effectively. The Agency is independent of this previous agency and has not assumed any liabilities of the previous agency.

Objectives

In accordance with the “Regulation on National Agency on Preparation and Holding in Ukraine of UEFA 2012” (the “**Agency Regulation**”) approved by the Resolution of the Cabinet of Ministers of Ukraine “On Arrangements to Improve the Management System for Preparation and Holding in Ukraine of the European Football Championship Finals in 2012” dated 7 April 2010, No. 298, the main objective of the Agency is to implement the effective organisation and holding of Euro 2012. In pursuance of its main objective, the Agency administers and supervises the implementation of the Programme. The Programme sets out twenty-two tasks which must be implemented before 2012 by the Agency, the Ministry of Transport and Communications and various municipal authorities and other entities in order to deliver the commitments given to UEFA in relation to Euro 2012.

In administering and supervising the implementation of the Programme, the Agency coordinates and directs the efforts of other governmental and municipal authorities as well as private and state owned companies that are responsible for the performance of the tasks and events relating to the Programme. The Agency also has the authority to establish, manage and supervise state enterprises in respect of which it acts as an asset management entity (the “**State Enterprises**”) including the National Sports Complex “Olympic” in Kyiv (“**NSC Olympic**”) and State Enterprise “Directorate for Construction of Objects for Euro 2012 in the City of Lviv” (the “**Lviv Directorate**”). It is also responsible for supervising certain projects related to the infrastructure which will support Euro 2012, for example, the reconstruction of Donetsk International Airport, the reconstruction of Lviv International Airport, the transformation of Kyiv Sports Palace into a mass media centre and other projects related to safety and security, power supply and transport.

Relationship with State Enterprises and Sub-Contractors

The Agency has authority to grant prior approval to any contract which the State Enterprises enter into with third party sub-contractors where the amount of that contract exceeds the limits provided by the constitutional documents of the respective State Enterprises. Thus, any contract entered into by NSC Olympic for an amount equal to or exceeding UAH 1,000,000 is subject to prior approval by the Agency. With respect to Lviv Directorate there are two thresholds for which the Agency’s prior approval is required.

These are reached if Lviv Directorate enters into any contract for an amount exceeding UAH 500,000 or disposes of fixed assets with a value equal to or exceeding UAH 100,000. The Agency plays an active role in reviewing these contracts and approving the appointment of sub-contractors. Failure of a State Enterprise to obtain the Agency’s approval of a contract in circumstances where such approval is required could be a ground for the invalidation of the contract.

Material Contracts

The Agency has entered into a number of contracts which are essential for its day to day operations, such as leasing office premises and utility supplies, none of which is material in the context of the issue and offering of the Notes.

Funding

As at the date of this Prospectus, the Agency obtains its funding from the State Budget. In the period from the date of establishment of the Agency until 1 September 2010, the Agency received UAH 4,634,000 from the State Budget to cover its operational costs. The total allocation of funds from the State Budget in 2010 is UAH 11,244,000. The Agency expects that it will require a further UAH 13,959,000 to cover its operational costs in the next financial year.

The Agency also acts as a chief administrator of the State Budget funds allocated for the implementation of the Programme. In the period from the date of its establishment until 1 September 2010 the Agency received and disposed of UAH 4,941,230,000 of State Budget funds for the implementation of the Programme. The Agency expects that it will receive UAH 6,081,920,000 of State Budget funds and will require a further UAH 15,000,000,000 to finance the implementation of the Programme in the next financial year.

Financial Reporting

The Agency provides monthly, quarterly and annual reports to respective divisions of the State Treasury of Ukraine and Accounting Chamber of Ukraine (*Rakhunkova Palata Ukrainy*). Various reports which must be prepared by the Agency include a Balance Sheet, a Report on Receipts and Use of Allocations from the Special Fund, a Report on In-kind Assets and a Report on Indebtedness under Budget Funds. The Agency also submits quarterly reports to the Ukrainian fiscal authorities (reports on taxes withheld from revenues paid to other parties and reports on the use of funds by non-profit institutions) and statistics bodies (a report on employment). The Agency is subject to annual audits by the Main Control and Revision Service of Ukraine (the “MCRS”). Such audits are performed in accordance with the schedule prepared by MCRS. The Agency’s financial systems and controls are approved by the Ministry of Finance. The Agency’s financial year-end is 31 December and no year-end financial statements have been produced by the Agency as at the date of this Prospectus.

Management and Employees

According to the Agency Regulation, the Agency is run by the head of the agency (the “**Head of the Agency**”). The Head of the Agency must be appointed pursuant to a resolution of the Cabinet of Ministers of Ukraine, upon a submission by the Prime Minister of Ukraine. The Head of the Agency performs general management functions of the Agency, directs the Agency’s activities and performs other functions assigned to him or her under Ukrainian legislation. The current Head of the Agency, Mr. Volodymyr Kovalevskiy, was appointed by the Cabinet of Ministers of Ukraine, by its Resolution dated 12 April 2010 No. 828-p. The Cabinet of Ministers of Ukraine may, by resolution, appoint deputy heads, including one first deputy head. The deputy heads are Messieurs Oleksandr Birsan (First Deputy Head), Valeriy Zhaldak (Deputy Head – Chairman of the Operational Department), Mykola Shubin (Deputy Head – Chairman of the Department for Budget Programs and Financing), Dmytro Kotlubey (Deputy Head) and Oleksandr Krasnoshtan (Deputy). Prior to being hired, the Head of the Agency and deputy heads are subject to background checks.

In accordance with the Resolution of the Cabinet of Ministers of Ukraine “On Arrangements to Improve the Management System for Preparation and Holding in Ukraine of the European Football Championship Finals in 2012” dated 7 April 2010, No. 298, the Agency may employ up to 70 people. The employees of the Agency effectively have the status of employees of the State. The Agency believes it has good relations with its employees.

Other Opportunities Before and Beyond 2012

Following the adoption of the Further Resolution Regulating the Agency (as defined below), the Agency expects to have further opportunities both before and beyond 2012. In particular, the Agency will be responsible for the implementation of infrastructural projects connected with other international sports events. Such opportunities could arise if, for example, the Agency were responsible for the preparation and implementation of infrastructural projects connected with the hosting of the 2011 International Ice Hockey Federation World Championship Division I, which will be held in Kyiv Sports Palace from 17 to 23 April 2011, or if Ukraine were to submit a bid to host the 2022 Winter Olympics.

Further Changes of the Agency's Name, Objectives and Agency Regulations

On 15 September 2010 the Cabinet of Ministers of Ukraine passed Resolution No. 871 "On Change of the Name of the National Agency on Preparation and Holding in Ukraine of UEFA Euro 2012" (the "**Further Resolution Regulating the Agency**"). The Further Resolution Regulating the Agency was published on 30 September 2010 and will become effective 60 days after its publication. The Further Resolution Regulating the Agency changes the name of the Agency, broadens the objectives of the Agency and approves a new version of the regulations governing the Agency. Thus the Agency's name will be changed to the "National Agency on Preparation and Holding in Ukraine of UEFA Euro 2012 and Implementation of Infrastructural Projects". The objectives of the Agency will be broadened to cover the preparation and implementation of infrastructural projects connected with UEFA Euro 2012 and other international sports events.

Key Legislation

The Agency is constituted, and its activities are governed, by specific legislation. The principal elements of this legislation are:

The Budget Code of Ukraine.

Law of Ukraine "On State Budget for Year 2010".

Resolution of the Cabinet of Ministers of Ukraine "On Procedure of Providing Guarantees under Obligations of the National Agency on Preparation and Holding in Ukraine of the UEFA Euro 2012", dated 18 August 2010, No.766.

Law of Ukraine "On Management of Objects of State Property".

Resolution of the Cabinet of Ministers of Ukraine "On Arrangements to Improve the Management System for Preparation and Holding in Ukraine of European Football Championship Finals in 2012" dated 7 April 2010, No. 298.

"Regulation on National Agency on Preparation and Holding in Ukraine of European Football Championship Finals in 2012", approved by the Resolution of the Cabinet of Ministers of Ukraine "On Arrangements to Improve the Management System for Preparation and Holding in Ukraine of the UEFA Euro 2012" dated 7 April 2010, No. 298.

Resolution of the Cabinet of Ministers of Ukraine "On Change of the Name of the National Agency on Preparation and Holding in Ukraine of UEFA Euro 2012" dated 15 September 2010, No. 871 which Resolution will become effective from 60 days after its publication on 30 September 2010.

"State Purpose Programme for Preparation and Holding in Ukraine of the European Football Championship Finals in 2012", approved by the Resolution of the Cabinet of Ministers of Ukraine as of 14 April 2010 No. 357.

DESCRIPTION OF NSC OLYMPIC

Establishment and Legal Ownership

The National Sports Complex “Olympic” (“**NSC Olympic**”) was established as a State Enterprise in accordance with the Edict of the President of Ukraine “On the National Sports Complex “Olympic” dated 12 May 1996, No. N 331/96. By virtue of its charter, which was approved by the Agency on 25 May 2010, NSC Olympic has the status of a legal entity under Ukrainian law. Since 21 April 2010, NSC Olympic has been supervised by the Agency in accordance with the Resolution of the Cabinet of Ukraine “On the Transfer of the State Enterprise “National Sports Complex “Olympic” into the Management by the National Agency on Preparation and Holding in Ukraine of the UEFA Euro 2012” dated 21 April 2010, No. 956- whereby the Agency took over the management of NSC Olympic from the Ministry of Ukraine for Family, Youth and Sports. NSC Olympic is wholly-owned by the State. The principal offices of NSC Olympic are located at 55, Chervonoarmijska str., the City of Kyiv, 03150, Ukraine.

Objectives

The functions of NSC Olympic are set out in its charter. The primary task of NSC Olympic is to organise and hold sports and entertainment events and provide sports and rehabilitation services. In pursuance of this task NSC Olympic is authorised, alongside others, to plan and organise various construction and reconstruction projects. In particular, NSC Olympic is supervising the reconstruction of the Olympiysky National Sports Complex in Kyiv to provide, amongst other things, a stadium with approximately 69,000 seats (the “**Olympiysky Stadium**”) as part of the commitment of Ukraine to UEFA to co-host Euro 2012. Following the reconstruction and commissioning of the Olympiysky Stadium, NSC Olympic will be responsible for the operation of the Olympiysky Stadium.

General Contractor

On 28 November 2008, pursuant to a decision of its tender committee, NSC Olympic entered into a general contract agreement (the “**NSC Olympic General Contract**”) with JSC “HC Kyivmiskbud”, a joint stock company incorporated in Ukraine (the “**NSC Olympic General Contractor**”). The NSC Olympic General Contractor was selected pursuant to a “single source procurement procedure” which was performed based on the Resolution of the Cabinet of Ministers of Ukraine “On Procurement of Construction and Assembly Works for the Reconstruction of the National Sports Complex “Olympic” dated 9 November 2008, No. 1020. The NSC Olympic General Contractor was chosen after the consultation meeting held by the Ministry of Ukraine for Family, Youth and Sports on 25 November 2008, in which the representatives of the major Ukrainian construction companies participated. Based on the result of that consultation meeting, and the market research conducted by the tender committee of NSC Olympic, the tender committee came to the conclusion that the NSC Olympic General Contractor was the only construction company capable of completing all requisite reconstruction works within the necessary timeframes.

The function of the NSC Olympic General Contractor is to manage and implement the project of the reconstruction of the Olympiysky Stadium both by its own efforts and by the appointment of sub-contractors. Since reconstruction works began in July 2008 the Olympiysky Stadium has not been used and will not be capable of being used again until the reconstruction work is complete.

The NSC Olympic General Contract establishes certain criteria which determine whether or not NSC Olympic’s approval is required for the appointment of any particular sub-contractor. NSC Olympic plays an active role in approving the appointment of all sub-contractors and reviewing the contracts between the NSC Olympic General Contractor and its sub-contractors. Failure of the NSC Olympic General Contractor to obtain NSC Olympic’s approval of a contract in circumstances where such approval is required could be a ground for the invalidation of the contract. The NSC Olympic General Contractor is directly responsible to NSC Olympic for all its decisions and actions.

Sub-contractors

As at the date of this Prospectus, various contractors have been appointed by NSC Olympic. These include the NSC Olympic General Contractor, the NSC Olympic Roofing Contractor (as defined below) and the NSC Olympic Engineering Contractor (as defined below). Each has engaged a number of sub-contractors.

The NSC Olympic General Contractor has appointed 41 sub-contractors to carry out different types of work. The most important sub-contractors are those responsible for the performance of concrete-related work such as LLC “Solstroy”, OJSC “Domobudivniy Kombinat No. 3”, OJSC “Domobudivniy Kombinat No. 4” and JSC “Reinforced Concrete Construction Plant No. 1”.

The NSC Olympic Engineering Contractor has appointed 27 sub-contractors to carry out different types of work relating to the engineering infrastructure of Olimpiysky Stadium. Sub-contractors of the NSC Olympic Engineering Contractor include, amongst others, such companies as LLC “Budtechnoservice”, LCC “Hydrobudmontazh”, LLC “Energomontazhventilation”, LCC “Master-Group-Construction” and LLC “Agromat”.

The NSC Olympic Roofing Contractor has appointed 34 sub-contractors to carry out different types of work. Sub-contractors of the NSC Olympic Roofing Contractor include, amongst others, such companies as OJSC JSC “V.Shimanovsky UkrRDIsteelconstruction”, the E.O.Paton Electric Welding Institute, CJSC SRIE “Kryvorihstalconstruksia”, LLC “Megabud-Holdings” and LLC “Stalkanat market”.

All current sub-contractors of the NSC Olympic General Contractor and the NSC Olympic Engineering Contractor have been approved by NSC Olympic. The NSC Olympic Roofing Contractor does not require the NSC Olympic Roofing Contractor to have all its sub-contractors approved by NSC Olympic, however the NSC Olympic Roofing Contractor does notify NSC Olympic of all appointed sub-contractors.

Other Material Contracts

On 6 August 2008, following the tender organised by the Ministry of Ukraine for Family, Youth and Sports of Ukraine, NSC Olympic entered into an agreement with GMP Generalplanungsgesellschaft mbH (the “**NSC Olympic Design Contractor**”) for the performance of design works in relation to the Olimpiysky Stadium (the “**NSC Olympic Design Contract**”). GMP Generalplanungsgesellschaft mbH won the tender in competition with 18 other design proposals. The winning design was assessed cumulatively on factors such as cost efficiency, ability to meet deadlines, fitting in with surrounding architecture and compliance with UEFA requirements.

On 16 October 2009, the NSC Olympic General Contractor entered into a contract for roof assembly works (the “**NSC Olympic Roofing Contract**”) with LLC “Plant Master-Profi-Ukraine” (the “**NSC Olympic Roofing Contractor**”), a limited liability company incorporated in Ukraine, as a result of a tender organised by the NSC Olympic General Contractor. The NSC Olympic Roofing Contractor won the tender in competition with five other parties based on such factors as cost efficiency and ability to meet deadlines. On 17 June 2010 the NSC Olympic General Contractor transferred its rights and obligations under the NSC Olympic Roofing Contract to NSC Olympic.

On 22 June 2010, NSC Olympic entered into a contract for the performance of engineering works (such as water supply and sewage systems, electricity) (the “**NSC Olympic Engineering Contract**”) with LCC “AK Engineering” (the “**NSC Olympic Engineering Contractor**”), a limited liability company incorporated in Ukraine. The NSC Olympic Engineering Contract was entered into without a tender based on a legislative exemption from tender procedures for procurements performed in connection with the preparation and holding in Ukraine of the European Football Championship Finals in 2012.

Funding

Currently, NSC Olympic obtains all of its funding from the State Budget. However, NSC Olympic is able to obtain funding from other sources to the fullest extent permitted by law. In the period from 1 January 2010 until 1 September 2010, NSC Olympic received UAH 1,231,200,000 from the State Budget. The total allocation of funds from the State Budget in 2010 is UAH 1,923,640,210. NSC Olympic expects that it will

receive a further UAH 217,260 of funding from the State Budget to cover its operational costs in the next financial year.

Financial Reporting

NSC Olympic provides monthly, quarterly and annual financial reports to Ukrainian fiscal authorities and statistics bodies. Reports submitted by NSC Olympic to Ukrainian fiscal authorities include a declaration on corporate profit tax, a declaration on value added tax and other tax related reports. Reports submitted by NSC Olympic to the Ukrainian statistics bodies include a Balance Sheet, a Report on Financial Results, a Report on Cash Flows and a Report on Own Capital. In addition, NSC Olympic also files, on a monthly, quarterly and annual basis, a Report on the Receipts and Use of Allocations from the Special Fund with the State Treasury. NSC Olympic is also required to submit its annual report to the Agency and is subject to annual audits by MCRS. NSC Olympic's financial year-end is 31 December.

The audited financial statements for the financial year ending 31 December 2009 show a loss of UAH 1,528,000. This loss was attributable to the maintenance of a building for the Ministry of Ukraine for Family, Youth and Sports which belonged to and was maintained by NSC Olympic until the building was transferred to the Ministry of Ukraine for Family, Youth and Sports in April 2010. NSC Olympic is no longer responsible for the maintenance of this building and now focuses solely on the reconstruction of the Olympiysky Stadium.

Management and Employees

According to the Resolution of the Cabinet of Ministers of Ukraine dated 21 April 2010 No. 956-P, the Agency is responsible for the management of NSC Olympic. Day-to-day management of NSC Olympic is performed by its director general, who is appointed by the Agency. The director general of NSC Olympic is authorised to act on behalf of NSC Olympic without proxy, open bank accounts for NSC Olympic, sign contracts on behalf of NSC Olympic (execution of contracts the value of which equals or exceeds UAH 1,000,000 require prior approval and authorisation from the Agency), and perform certain other functions listed in the constitutional documents of NSC Olympic. The position of director general of NSC Olympic was until recently held by Mr Jitese Arquissandas, who resigned on 21 October 2010 following completion of his mandate to bring the works of the Olympiysky stadium back on schedule. Mr Arquissandas' role is currently being filled by Mr Volodymyr Barkovskyy, who is the acting director general of NSC Olympic. As the acting director general, Mr Volodymyr Barkovskyy has the same authorities as a director general, as described above.

As at 1 September 2010, NSC Olympic had 120 full-time employees. Prior to being hired, each prospective employee is subject to background checks. NSC Olympic believes it has good relations with its employees.

Key Legislation

NSC Olympic is constituted, and its activities are governed, by specific legislation. The principal elements of this legislation are:

The Commercial Code of Ukraine.

Law of Ukraine "On Management of Objects of State Property".

Edict of the President of Ukraine "On the National Sports Complex "Olympic" dated 12 May 1996, No. N 331/96.

Resolution of the Cabinet of Ministers of Ukraine "On the Transfer of the State Enterprise "National Sports Complex" "Olympic" into the Management by the National Agency on Preparation and Holding in Ukraine of the UEFA Euro 2012" dated 21 April 2010, No. 956-p.

Resolution of the Cabinet of Ministers of Ukraine "On Procurement of Construction and Assembly Works for the Reconstruction of the National Sports Complex "Olympic" dated 9 November 2008, No. 1020.

DESCRIPTION OF THE LVIV DIRECTORATE

Establishment and Legal Ownership

The State Enterprise “Directorate for Construction of Objects for Euro 2012 in the City of Lviv” (“**Lviv Directorate**”) was established as a State Enterprise by the Agency’s Order “On Establishment of State Enterprise “Directorate for Construction of Objects for Euro 2012 in the City of Lviv” dated 20 May 2010, No. 5. By virtue of its charter, which was approved by the Agency on 22 June 2010, Lviv Directorate has the status of a legal entity under Ukrainian law. Lviv Directorate is supervised by the Agency but is wholly-owned by the State. The principal offices of Lviv Directorate are located at 43, Sakharova str., Lviv, Ukraine.

Objectives

The functions of Lviv Directorate are set out in its charter. The primary objectives of Lviv Directorate are to supervise the construction, commissioning and operation of a stadium with approximately 33,400 seats in the city of Lviv located at Stryiska-Kiltseva Street (the “**Lviv Stadium**”) as well as the reconstruction of Lviv International Airport and other construction projects relating to utility and engineering networks adjacent to the Lviv Stadium, as part of the commitment of Ukraine to UEFA to co-host Euro 2012. Ownership of the integral property complex of Lviv Stadium was transferred from the ownership of the territorial community of the City of Lviv to the State on 7 April 2010 pursuant to the Resolution of the Cabinet of Ministers of Ukraine “On the Transfer of the Integral Property Complex of Lviv Municipal Enterprise “Directorate for Construction of Stadium in the City of Lviv” into State Ownership” dated 7 April 2010, No. 823. A further Resolution of the Cabinet of Ministers of Ukraine “On the Transfer of the Integral Property Complex of Lviv Municipal Enterprise “Directorate for Construction of Stadium in the City of Lviv” into State Ownership” dated 21 April 2010, No. 971-p, reconfirmed the transfer of the integral property complex of Lviv Municipal Enterprise “Directorate for Construction of Stadium in the City of Lviv” into state ownership under the management of the Agency.

General Contractor

On 28 March 2010, Lviv Municipal Enterprise “Directorate for Construction of Stadium in the City of Lviv” (the “**Lviv ME**”) entered into a general contract agreement (the “**Lviv General Contract**”) with LLC “Altcomkyivbud”, a limited liability company incorporated in Ukraine (the “**Lviv General Contractor**”). The Lviv General Contractor was selected on the basis of its ability to deliver an appropriate stadium and following extensive market research commissioned by the Ministry of Economy of Ukraine. Following the establishment of Lviv Directorate and the transfer of the integral property complex of Lviv ME to Lviv Directorate, the Lviv General Contract was also transferred from Lviv ME to Lviv Directorate on 24 June 2010.

The function of the Lviv General Contractor is to project manage the construction of the Lviv Stadium both by its own efforts and by the appointment of sub-contractors. The Lviv General Contract establishes certain criteria which determine whether or not Lviv Directorate’s approval is required for the appointment of any particular sub-contractor. Lviv Directorate plays an active role in approving the appointment of sub-contractors and reviewing the contracts between the Lviv General Contractor and its sub-contractors. Failure of the Lviv General Contractor to obtain Lviv Directorate’s approval of a contract in circumstances where such approval is required could be a ground for the invalidation of such contract. The Lviv General Contractor is directly responsible to Lviv Directorate for all its decisions and actions.

Sub-contractors

As at the date of this Prospectus, work in connection with the construction of the Lviv Stadium and the surrounding infrastructure is being carried out by the Lviv General Contractor and six sub-contractors. Sub-contractors are engaged mainly to carry out preparatory work for the construction of the Lviv Stadium and the surrounding infrastructure network.

The following are the sub-contractors which are currently engaged:

1. LCC “Ukrinvestbud” to construct the gas supply system for the construction period;
2. LLC “Electro-technical Union” to create the outside electricity supply network;
3. LLC “Altcom-Roads” to construct new roads near the Lviv Stadium;
4. “Road-Building Altcom” Ltd. to construct the new road junction near the Lviv Stadium; and
5. JSC “Naftogazbud” and LCC “Ukrinvestbud” to construct different parts of the water supply and sewage systems.

Other Material Contracts

On 19 April 2010, Lviv ME entered into an agreement for the performance of design works with LLC “Arnika” (the “**Lviv Design Contract**”), a limited liability company incorporated in Ukraine. Following the establishment of Lviv Directorate and the transfer of the integral property complex of Lviv ME to Lviv Directorate the Lviv Design Contract was also transferred from Lviv ME to Lviv Directorate on 24 June 2010. The Lviv Design Contract was made without a tender (pursuant to an exemption in the Resolution of the Cabinet of Ministers of Ukraine dated 17 October 2008, No. 921).

On 30 June 2010, Lviv Directorate entered into a consultancy contract with arenaCom GmbH (the “**Lviv Consultancy Contract**”) for the provision of consultancy services connected with UEFA requirements in relation to the construction of stadia. The Lviv Consultancy Contract was made without a tender (pursuant to an exemption in the Resolution of the Cabinet of Ministers of Ukraine dated 17 October 2008, No. 921).

Funding

Currently Lviv Directorate obtains all of its funding from the State Budget. However, Lviv Directorate is able to obtain funding from other sources to the fullest extent permitted by law. In the period from the date of its incorporation to 1 September 2010, Lviv Directorate received UAH 470,200,000 from the State Budget to finance the construction of Lviv Stadium. The total allocation of funds from the State Budget in 2010 is UAH 2,361,570,000. Lviv Directorate expects that it will receive a further UAH 1,309,400,000 funding from the State Budget to cover its operational costs in the next financial year.

Financial Reporting

Lviv Directorate provides monthly, quarterly and annual financial reports to Ukrainian fiscal authorities and statistics bodies. Reports submitted by Lviv Directorate to Ukrainian fiscal authorities include a declaration on corporate profit tax, a declaration on value added tax and other tax related reports. Reports submitted by Lviv Directorate to Ukrainian statistics bodies include a Balance Sheet, a Report on Financial Results, a Report on Cash Flows and a Report on Own Capital. In addition, Lviv Directorate also files, on a monthly, quarterly and annual basis, a Report on the Receipts and Use of Allocations from the Special Fund with the State Treasury (this report is filed separately with respect to Lviv Stadium and Lviv International Airport). Lviv Directorate is also required to submit its annual report to the Agency and is subject to annual audits by MCRC. Lviv Directorate’s financial year-end is 31 December and no year-end financial statements have been produced by Lviv Directorate as at the date of this Prospectus.

Management and Employees

The Agency, as the founder of Lviv Directorate, acts as the asset management body with respect to Lviv Directorate. The day-to-day management of Lviv Directorate is performed by its chief executive officer (*kerivnyk*), who is appointed by the Agency. In accordance with the internal list of members of staff of Lviv Directorate, the title for the chief executive officer of Lviv Directorate is “Director General”. The Director General of Lviv Directorate is authorised to act on behalf of Lviv Directorate without proxy, open bank accounts for Lviv Directorate, sign contracts on behalf of Lviv Directorate (although the execution of contracts for the alienation of any fixed assets of Lviv Directorate the value of which equals or exceeds UAH 100,000 and the execution of any other contract the value of which exceeds UAH 500,000 require prior

approval and authorisation from the Agency) and perform certain other functions listed in the constitutional documents of Lviv Directorate. Currently, Mr. Volodymyr Shadrin acts as Director General of Lviv Directorate.

As at 1 September 2010, Lviv Directorate had 131 full-time employees. Prior to being hired, each prospective employee is subject to background checks. Lviv Directorate believes it has good relations with its employees.

Key Legislation

Lviv Directorate is constituted, and its activities are governed, by specific legislation. The principal elements of this legislation are:

The Commercial Code of Ukraine.

Law of Ukraine “On Management of Objects of State Property”.

Resolution of the Cabinet of Ministers of Ukraine “On the Transfer of the Integral Property Complex of Lviv Municipal Enterprise “Directorate for Construction of Stadium in the City of Lviv” into State Ownership” dated 7 April 2010, No. 823.

Resolution of the Cabinet of Ministers of Ukraine “On the Transfer of the Integral Property Complex of Lviv Municipal Enterprise “Directorate for Construction of Stadium in the City of Lviv” into State Ownership” dated 21 April 2010, No. 971-p.

DESCRIPTION OF THE GUARANTOR

Area and Population

Ukraine is a republic occupying a land area of 603,548 square kilometres, which makes it the second largest country in Europe after Russia. It is bordered by Russia to the east, Belarus to the north, Poland, Slovakia, Hungary, Romania and Moldova to the west and the Black Sea to the south.

Ukraine is subdivided into 24 oblasts (or regions). Two Ukrainian cities — Kyiv, the capital of Ukraine, and Sevastopol, currently the site of a major naval base of the Russian Federation — are granted special status under the Ukrainian Constitution in respect of certain administrative, budgetary and other matters. The Autonomous Republic of Crimea, an autonomous region within Ukraine, is located on the Crimean Peninsula on the country's Black Sea and Azov Sea coast.

Based on figures from the Ukrainian State Committee of Statistics, the population of Ukraine totalled approximately 45.9 million at 1 July 2010. According to the all-Ukrainian census of 2001, about 78 per cent. of the country's population were ethnic Ukrainians and 17 per cent. ethnic Russians. Other groups, including Belarusians, Moldavians, Bulgarians, Crimean Tatars, Hungarians, Romanians, Greeks and Poles, accounted for about 5 per cent. of the population. The official language is Ukrainian, although approximately 80 per cent. of the population is bilingual, speaking both Ukrainian and Russian fluently. The literacy rate is approximately 98 per cent.

Between 1980 and 1990, the population grew by 0.4 per cent. annually, but this trend has reversed since 1991, reflecting the worsening economic and social conditions associated with the significant post-independence recession. As a result, the population of Ukraine has declined by approximately 6.3 million people since 1993. The Government estimates that the population is currently decreasing at a rate of 0.7 per cent. per year.

History

Ukraine was settled by Slavic tribes in the first millennium AD, but from the thirteenth century through to the seventeenth century, control of the present territory passed under several powers, including the principality of Kyiv Rus, the Kingdom of Poland/Grand Principality of Lithuania and the Mongol Golden Horde.

Slavic tribes occupied central and eastern Ukraine in the sixth century AD and played an important role in the establishment of Kyiv. Situated on lucrative trade routes, Kyiv quickly prospered as the centre of the powerful state of Kyiv Rus. In the eleventh century, Kyiv Rus was, geographically, the largest state in Europe. Kyiv was razed by Mongol raiders in the thirteenth century, leaving Kyiv Rus rendering tribute to the Mongol Golden Horde.

In 1654, the leader of the Ukrainian (Zaporozhian) Cossacks accepted the protection of the Russian Tsar under the Treaty of Pereyaslav, and most of what is present-day Ukraine remained under Russian administration from that time until World War I. The end of the Russian and Hapsburg Empires brought about by World War I allowed Ukraine briefly to assert its independence. In 1917 and 1918, three separate Ukrainian republics declared independence. However, by 1921, the western part of the traditional territory had been incorporated into Poland and the larger, central and eastern, part became part of the Soviet Union. As a consequence of the imposition of farm collectivisation by Stalin, around seven million Ukrainians are estimated to have died in the 1930s.

After World War II, the western Ukrainian regions were incorporated into the Soviet Union. Many Ukrainians and people of other nationalities living in Ukraine (including almost the entire population of Crimean Tatars) were deported by Stalin, adding to the millions of victims of the war itself. From the end of the war, Ukrainian patriotic feelings were strongly suppressed, but surfaced from time to time in resistance to the "Russification" policies pursued by Moscow.

The greater openness (glasnost) which followed the accession to power of Mikhail Gorbachev allowed the formation in the mid-1980s of the Ukrainian patriotic movement Rukh, which won 27 per cent. of the vote in elections in 1990. In a referendum in early 1991, 60 per cent. of voters favoured Ukraine's participation in a new Union of Sovereign States. Ukraine became an independent state on 24 August 1991 following the dissolution of the Soviet Union. Ukraine's Parliament officially adopted the Act Declaring the Independence of Ukraine, a decision ratified by 90.3 per cent. of the votes cast in a subsequent referendum on 1 December 1991. After its declaration of independence, Ukraine experienced separatist activities in the Crimean Peninsula, although such activities ceased after Ukraine's acceptance of the Crimean Peninsula's status as an autonomous region. Crimea is an autonomous republic within Ukraine, with its own constitution, parliament and government, but its government remains subordinate to the central Government of Ukraine as provided in the Constitution of Ukraine and other applicable legislation.

Political Developments

Ukraine experienced significant political instability during the 2004 Presidential election. The results of the first run-off of the election, between Mr Yushchenko and Mr Yanukovich on 21 November 2004, in which Mr Yanukovich was declared the winner, were disputed on the basis of allegations of corruption, voter intimidation and direct electoral fraud, as reported by numerous domestic and foreign observers. The Supreme Court of Ukraine invalidated the results of the election and ordered a second run-off, which was held on 26 December 2004. Mr Yushchenko was declared the official winner of the second run-off and was inaugurated as President on 23 January 2005.

On 25 May 2006, when the Parliament elected in March 2006 gathered for its first session, the constitutional reform limiting the powers of the President and transferring certain powers from the President to Parliament and the Prime Minister became effective (with certain provisions already in effect since 1 January 2006). As a result of this constitutional reform, Ukraine became a parliamentary-presidential republic, as the President was no longer empowered to exercise direct executive powers over decisions and actions of the Government. In particular, until the CCU Ruling, Parliament was empowered to appoint, upon the President's nomination, the Prime Minister, Minister of Defence and Minister of Foreign Affairs and, upon the nomination of the Prime Minister, the remaining members of the Government. Parliament was also empowered to dismiss these officials. The President was no longer empowered to appoint members of the Government.

According to other provisions of the constitutional reform, parliamentarians were required to form a majority coalition, which was entitled to propose a candidate for the position of Prime Minister to the President, who made a further nomination to Parliament. The majority coalition was further entitled to propose candidates for positions of members of the Government (subject to certain exceptions) to the Prime Minister, who made further nominations to Parliament. The President received new powers for early termination of Parliament. In particular, the President could dissolve Parliament if (i) it failed to form a majority coalition within a month of the commencement of its first session or the dissolution of the previously existing coalition; (ii) it failed to appoint the Government within 60 days following the previous Government's dismissal or resignation; or (iii) it failed to convene for 30 days in a continuous period.

On 2 April 2007, President Yushchenko signed a decree dissolving Parliament. The President's decree stated that the process of forming a majority coalition in Parliament during recent months had breached the procedure set forth in the then effective Constitution of Ukraine. Pursuant to this decree, new parliamentary elections were scheduled for 27 May 2007. On 26 April 2007, by a subsequent decree, the President rescheduled the parliamentary election for 24 June 2007. Notwithstanding the President's decrees, Parliament continued to function, claiming that the President did not have sufficient grounds under the Constitution of Ukraine for the early termination of the powers of Parliament.

Following negotiations held by the working group comprising representatives of the President, the parliamentary coalition and the opposition, President Yushchenko, Speaker of Parliament Moroz and Prime Minister Yanukovich reached agreement on 27 May 2007 to hold early parliamentary elections on 30 September 2007.

More than 160 deputies from the Our Ukraine Bloc and Yuliya Tymoshenko's Bloc applied to withdraw from their parliamentary factions in order to implement the compromise reached to hold early parliamentary

elections on 30 September 2007. In June 2007, the governing bodies of Our Ukraine Bloc and Yuliya Tymoshenko's Bloc approved the decision on the termination of powers of their respective deputies and excluded from their electoral lists all candidates who had not obtained seats in Parliament; without this cancellation, these candidates would have automatically replaced the deputies whose powers were terminated. The termination of powers of the deputies from these two blocs led to Parliament lacking a sufficient number of deputies to form the constitutional quorum required for further action.

On 5 June 2007, the President signed a decree (further amended on 31 July 2007) scheduling the parliamentary elections for 30 September 2007 on the grounds of absence of a constitutional quorum in Parliament as a result of the termination of powers of Our Ukraine Bloc's and Yuliya Tymoshenko's Bloc's deputies. In 2007, the decree was subject to unsuccessful challenges in the Constitutional Court.

On 30 September 2007, early elections to Parliament were held as a result of which, out of 20 political parties and election blocs participating in the elections, only five political parties and election blocs managed to collect the 3 per cent. or more of the national vote required to gain seats in Parliament. Of these, Partiya Regioniv (the Party of Regions), led by Viktor Yanukovich, established the largest faction, with 175 seats out of 450 total seats; Yuliya Tymoshenko's Bloc established a faction with 156 seats; Bloc Nasha Ukrayina — Narodna Samooborona (Our Ukraine — People's Self-Defense Bloc), associated with President Yushchenko, established a faction with 72 seats; and the Communist Party of Ukraine and Lytvyn's Bloc (led by the Speaker of Parliament) established factions with 27 and 20 seats, respectively. On 23 November 2007, the newly elected Parliament held its first session.

The table below shows a breakdown of the number of seats in Parliament for each faction/bloc:

	Total seats as a result of elections⁽¹⁾	Current number of seats⁽²⁾	Percentage of seats in Parliament
Party of Regions	175	172	38.2
Yuliya Tymoshenko's Bloc	156	124	27.6
Our Ukraine — People's Self-Defense Bloc	72	72	16.0
Communist Party of Ukraine	27	27	6.0
Lytvyn's Bloc	20	20	4.4
Out-of-Faction Deputies ⁽³⁾	–	35	7.8
Total	450	450	100.0

Notes:

(1) As a result of the September 2007 Parliamentary elections.

(2) As at 30 September 2010.

(3) Two deputies left the faction of Party of Regions on 23 June 2009; one deputy left the faction of Yuliya Tymoshenko's Bloc on 8 October 2009; one deputy left the faction of Party of Regions on 9 October 2009; three deputies left the faction of Yuliya Tymoshenko's Bloc on 8 September 2010 and twenty-eight deputies left the faction of Yuliya Tymoshenko's Bloc on 21 September 2010.

Source: Central Election Commission, Parliament of Ukraine

The initial majority coalition in Parliament elected in September 2007 was established on 29 November 2007 and was composed of the parliamentary factions of Yuliya Tymoshenko's Bloc and Our Ukraine — People's Self Defense Bloc. On 4 December 2007, Parliament elected Arseniy Yatsenyuk as the new Speaker of Parliament. On 18 December 2007, Parliament appointed Yuliya Tymoshenko as Prime Minister of Ukraine and endorsed the coalition Government.

However, it has been reported that one deputy of Our Ukraine — People's Self-Defense Bloc did not sign the coalition agreement in November 2007. It has also been reported that, on 6 June 2008, two deputies (one from Our Ukraine — People's Self-Defense Bloc and one from Yuliya Tymoshenko's Bloc) submitted applications for their withdrawal from the majority coalition, which de facto left the coalition with less than a majority in Parliament. In the absence of clear rules governing the coalition dissolution, this could have been viewed as a ground for formal dissolution of the coalition. However, the coalition was not officially

dissolved, which led to a constitutional challenge brought by representatives of the opposition parties. Further, on 3 September 2008, Our Ukraine — People's Self Defense Bloc announced its decision to withdraw from the majority coalition. Such decision was reportedly caused by the joint vote by their coalition partner (Yuliya Tymoshenko's Bloc) and the opposition Party of Regions in relation to the Russia-Georgia conflict and in favour of a number of laws reducing the powers of the President of Ukraine, which draft laws were subsequently vetoed by the President and further rejected by Parliament.

In connection with the withdrawal of Our Ukraine — People's Self Defense Bloc from the majority coalition, on 16 September 2008, Speaker of Parliament Arseniy Yatsenyuk officially announced the dissolution of the majority coalition. Pursuant to the then effective Constitution of Ukraine, a new majority coalition would need to have been formed within one month from the date of dissolution of the previous coalition. On 9 October 2008, the President issued a decree dissolving Parliament on the basis of a failure by the parliamentary factions to timely form a new coalition, and determined 7 December 2008 as the date for new parliamentary elections. However, the Decree was challenged in court by the representatives of Yuliya Tymoshenko's Bloc and was subsequently cancelled by the President on 20 October 2008.

On 9 December 2008, Parliament elected Volodymyr Lytvyn as its new Speaker. The majority coalition was formed pursuant to the coalition agreement signed on 17 December 2008 comprising three parliamentary factions: Our Ukraine — People's Self Defense Bloc, Yuliya Tymoshenko's Bloc and Lytvyn's Bloc. Pursuant to the coalition agreement, Yuliya Tymoshenko retained the position of the Prime Minister of Ukraine.

On 1 April 2009, Parliament approved 25 October 2009 as the date for new presidential elections. On 12 May 2009, upon the President's submission, the Constitutional Court of Ukraine resolved that the Parliament's decision of 1 April 2009 was not constitutional. Subsequently, members of Parliament and the President reached an agreement and on 23 June 2009, Parliament determined 17 January 2010 as the date of the 2010 presidential elections.

On 21 August 2009, Parliament approved a law amending the legislation governing presidential elections. The law introduces a number of changes to the procedures of election campaigns, formation and operation of election commissions and other matters related to the electoral process. On 10 September 2009, the law was officially promulgated and became effective, but the President shortly requested the Constitutional Court of Ukraine to opine on the constitutionality of certain provisions of the new law. On 19 October 2009, the Constitutional Court of Ukraine ruled that certain of the challenged provisions of the new law were unconstitutional.

The presidential elections campaign commenced on 19 October 2009. Eighteen candidates participated in the first round of the elections held on 17 January 2010. The two candidates who received the largest number of votes in the first round, Viktor Yanukovich (35.32 per cent.) and Yuliya Tymoshenko (25.05 per cent.), participated in a run-off that took place on 7 February 2010. On 14 February 2010, Viktor Yanukovich was declared the official winner of the run-off, having received 48.95 per cent. of the votes, compared to 45.47 per cent. received by Yuliya Tymoshenko. The inauguration of new President was scheduled for 25 February 2010.

Following the declaration of the official results of the run-off, Yuliya Tymoshenko filed an appeal with the Higher Administrative Court of Ukraine challenging the results of the run-off and alleging electoral fraud. On 17 February 2010, the Higher Administrative Court of Ukraine suspended the ruling of the Central Election Commission that declared Viktor Yanukovich as a winner of the election, but did not postpone or cancel the President's inauguration. Subsequently, Yuliya Tymoshenko withdrew her appeal on 20 February 2010 as the Higher Administrative Court in Kiev rejected some of her petitions, and the inauguration of Viktor Yanukovich as the new President was held on 25 February 2010.

On 2 March 2010, the Speaker of Parliament announced the termination of the majority coalition of Our Ukraine – People's Self-Defense Bloc, Yuliya Tymoshenko's Bloc and Lytvyn's Bloc.

On 11 March 2010, the parliamentary factions of Party of Regions, Communist Party of Ukraine, Lytvyn's Bloc and a number of deputies from Our Ukraine-People's Self-Defense Bloc and from Yuliya Tymoshenko's

Bloc established the majority coalition “Stability and Reform”, which, as at 30 September 2010, consisted of 264 deputies. On the same date, the Parliament appointed Mykola Azarov, a member of Party of Regions, as the new Prime Minister and endorsed the coalition Government.

In July 2010, 252 members of Parliament had requested the Constitutional Court to opine on the constitutionality of the 2004 law that was the basis of a constitutional reform implemented in 2006. On 30 September 2010, the Constitutional Court issued the CCU Ruling. Pursuant to the CCU Ruling, starting from 30 September 2010, Ukraine is governed by the Constitution that was in effect before the amendments were introduced by the 2004 law. As a result of the CCU Ruling, Ukraine has become a presidential-parliamentary republic, as the President is now empowered to exercise direct executive powers over decisions and actions of the Government and certain powers transferred from the President to Parliament and the Prime Minister as a result of the constitutional reform implemented in 2006 have been transferred back to the President. See *“Risk Factors – Risk Factors Relating to the Guarantor – Ukraine’s Government may be unable to sustain political consensus, which may result in political instability”* and *“Political Framework – The Constitution and the President”*.

There can be no assurance that Ukraine will not experience continued or heightened political instability in the future. See *“Risk Factors — Risk Factors relating to the Guarantor — Ukraine’s Government may be unable to sustain political consensus and any resulting political instability may have negative effects on the economy of Ukraine.”*

POLITICAL FRAMEWORK

The Constitution and the President

The Constitution (the Fundamental Law of Ukraine) was adopted by Parliament on 28 June 1996. It defines Ukraine as a sovereign, independent, democratic, social, legal and unitary state. The Constitution guarantees, among other things, the principles of political, economic and ideological diversity; human and civil rights and freedoms; freedom of information; the inviolability of private property and the right to conduct entrepreneurial activity. The State ensures the protection of competition and business activity.

The Constitution also stipulates the responsibilities of Parliament, the President and the Government and outlines the system for the administration of justice and the functions of the judiciary of Ukraine. Under the Constitution, both the President and Parliament are directly elected by universal suffrage. As a result of amendments to the Constitution passed on 8 December 2004 which were declared unconstitutional and lost their effect starting from 30 September 2010 pursuant to the CCU Ruling, Ukraine became a parliamentary presidential republic as the President was not empowered to exercise direct executive powers over decisions and actions of the Government.

In July 2010, 252 members of Parliament had requested the Constitutional Court to opine on the constitutionality of the 2004 law that was the basis of a constitutional reform implemented in 2006. On 30 September 2010, the Constitutional Court issued the CCU Ruling against the constitutionality of the 2004 law. As a result of the CCU Ruling, Ukraine has become a presidential-parliamentary republic, as the President is now empowered to exercise direct executive powers over decisions and actions of the Government and certain powers transferred from the President to Parliament and the Prime Minister as a result of the constitutional reform implemented in 2006 have been transferred back to the President. See *“Risk Factors – Risk Factors Relating to the Guarantor – Ukraine’s Government may be unable to sustain political consensus, which may result in political instability”* and *“Description of the Guarantor – Political Developments”*.

The Constitution provides that the President is the head of the sovereign state of Ukraine and is authorised to act on behalf of Ukraine. The President is elected for a term of five years.

Following the CCU Ruling, the President has the authority to appoint the Prime Minister, subject to parliamentary approval, to terminate the powers of the Prime Minister and to accept his resignation. In addition, the President has the authority to appoint members of the Cabinet of Ministers upon nomination of the Prime Minister as well as to appoint heads of other central executive bodies and local state administrations and to terminate their powers. Furthermore, the President has the authority to appoint, subject to parliamentary approval, the Chairman of the Antimonopoly Committee, the Prosecutor General, the Chairman of the SPF and the Chairman of the State Committee on TV and Radio Broadcasting. The President has the right to initiate legislation, the power to veto parliamentary bills and the right to cancel acts of the Cabinet of Ministers. The President may also issue his own decrees and directives.

The President is also the head of the National Security and Defence Council (the “NSDC”) and is authorised to appoint its members. The NSDC was created in 1992 to develop national security policy on domestic and international matters and to advise the President. Ex officio members of the NSDC include the Prime Minister, the Minister of Defence, the Head of the Security Service, the Minister of the Interior and the Minister for Foreign Affairs.

The Executive

The powers of the Government of Ukraine are vested in the Cabinet of Ministers of Ukraine, which is the highest body of executive power in Ukraine and includes the Prime Minister, First Vice Prime Minister, Vice Prime Ministers and Ministers. The Cabinet of Ministers is accountable to the President and Parliament and reports to Parliament within the limits set forth by the Constitution of Ukraine. Following the CCU Ruling, the President has the authority to appoint the Cabinet of Ministers upon nomination of the Prime Minister. The powers of an existing Cabinet of Ministers are terminated if a new President is elected, the Prime Minister resigns or is dismissed by the President or a vote of no-confidence in the Cabinet of Ministers is

passed in Parliament. If any of these events occurs, the President is required to nominate a new candidate who must be affirmed by the majority of the Parliament to act as Prime Minister and to form a government. If the candidate does not obtain the required parliamentary approval, a different candidate must be nominated by the President and this process continues until a candidate has obtained parliamentary approval. The powers of the Cabinet of Ministers include implementation of financial, pricing, investment, labour, social, education, science, environment and tax policies, management of state-owned assets and elaboration and performance of the State Budget Law for each relevant year.

Following the CCU Ruling, on 7 October 2010, Parliament approved a new law defining the principal objectives of the Cabinet of Ministers, its organisation and other related issues. The new law introduces, among other things, certain changes to the relations between the Cabinet of Ministers and other executive authorities and local self-government authorities.

As of 1 September 2010, 20 ministries and 46 other central executive authorities have been established in Ukraine. Following the CCU Ruling, the power to establish, reorganise and disband ministries and other central governmental agencies is vested in the President of Ukraine upon nomination of the Prime Minister.

The Legislature

Legislative power in Ukraine is vested in the Verkhovna Rada, or Parliament. Parliament adopts laws, which have the highest authority in the hierarchy of normative acts in Ukraine after the Constitution itself. Parliament is a unicameral body with 450 seats and is elected for four years. Since the March 2006 parliamentary elections, all seats are chosen according to a system of proportional representation from lists of candidates proposed by political parties and electoral blocs that accumulate at least 3 per cent. of the total vote.

In addition to its legislative function, Parliament nominates the Governor of the NBU and confirms the President's appointment of the Prime Minister, the Chairman of the Antimonopoly Committee, the Prosecutor General, the Chairman of the SPF and the Chairman of the State Committee on TV and Radio Broadcasting. Parliament also appoints judges with life tenure to all courts other than the Constitutional Court, and one third of the judges of the Constitutional Court.

Parliament also decides on items such as approval of the general Government agenda, nationwide programmes of economic, scientific, social, cultural and environmental development, the general outlines of domestic and foreign policy, the State Budget and the list of state-owned assets barred from privatisation; the granting of loans to foreign countries and international organisations, and receiving of loans from foreign countries, banks and international financial organisations that are not otherwise envisaged in the State Budget in any given year; and the general structure and functions of the Ukrainian armed forces and the Security Service of Ukraine.

The President may dismiss Parliament only if it fails to convene for 30 days during a non-recess period.

The Judicial System and Legal Framework

In general, the Constitutional Court of Ukraine has exclusive jurisdiction over the interpretation of the Constitution and laws of Ukraine and acts as final arbiter on constitutional issues. The Court consists of 18 judges, six appointed by the President, six appointed by Parliament and six appointed by the Congress of Judges. Judges of the Constitutional Court were chosen for the first time in 1996, as the late adoption of the Constitution hampered development of the judicial system before June 1996.

The judicial system reform that commenced in 2002 envisaged the creation of new judicial institutions as well as a system of specialised courts. However, until 2007 the creation of specialised courts had been postponed because of insufficient funds in the State Budget. In 2005, the Higher Administrative Court of Ukraine and the Administrative Chamber of the Supreme Court of Ukraine were constituted, but the process of formation of local and appellate administrative courts took several years more. As at 1 September 2010, all local and appellate administrative courts have been constituted. On 30 July 2010, the Law of Ukraine "On the Judicial System and the Status of Judges" came into force, replacing existing Laws of Ukraine "On the Judicial System of Ukraine" and "On the Status of Judges". The new law aims to improve the legislative

framework governing the judicial system, the judicial process and the status of judges and provides for, among other things, the establishment of new, Higher Specialised Court of Ukraine for Civil and Criminal Matters.

The Law of Ukraine “On Arbitration Courts”, enacted in 2004, provides for the establishment of independent permanent arbitration courts and ad hoc arbitration tribunals (tribunals formed for the purpose of resolving a particular dispute). Permanent arbitration courts are subject to state registration by the Ministry of Justice of Ukraine or its regional departments.

Historically, only a small number of judicial decisions taken in Ukraine have been publicly available; accordingly, their utility to the public in interpreting Ukrainian legislation is limited. However, in accordance with the law “On Access to Court Decisions”, which became effective on 1 June 2006, decisions of courts of general jurisdiction in civil, economic, administrative and criminal matters issued from 1 June 2006 (and, in the case of local courts of general jurisdiction, from 1 January 2007) onward, are required to be made available to the public. The Unified State Register of Court Decisions has been established pursuant to this law and is accessible on the official website of the judiciary, which makes current court decisions available through the Register, primarily on a going-forward basis.

As a result of its relatively recent transition towards a market economy, Ukraine does not yet have a mature legal system comparable to the legal systems of most major European countries. Although new laws have been introduced and amendments have been made to company, property, bankruptcy, securities, taxation, banking and foreign investment laws, this legislation is undeveloped and contains many gaps, thereby failing to provide an adequate underpinning for complex transactions. In order to facilitate implementation and enforcement of important legislation, such as tax legislation, Parliament has gradually been taking steps to adopt new legislation that consolidates the laws into unified codes. See *“Risk Factors – Risk Factors Relating to the Guarantor – Ukraine’s developing legal system creates risks and uncertainties for investors in Ukraine and for participants in the Ukrainian economy.”*

In 2001, Parliament enacted a new Land Code and a new Criminal Code. The Land Code, which became effective as of 1 January 2002, applies to all types of land in Ukraine and governs the ownership, use and disposition of land in Ukraine. Under the Land Code, agricultural land may not be sold or otherwise disposed of (subject to certain exceptions) until the enactment of laws on the state land register and the land market (dates for hearings on which are not yet scheduled), but in any event not before 1 January 2012. In addition, the Land Code generally prohibits natural persons and legal entities from owning more than 100 hectares of agricultural land per person until 1 January 2015. The Land Code does not contain any similar restrictions with respect to non-agricultural land. Foreign individuals, legal entities and foreign states are permitted to own, use and dispose of certain non-agricultural land in Ukraine but are explicitly prohibited from owning agricultural land.

On 1 January 2004, a number of new legislative acts came into force, the key acts comprising new versions of the Civil Code, the Commercial Code, the Customs Code, the Family Code and the Criminal Enforcement Code.

The new Civil Code replaced the former Civil Code adopted in 1963. The new Civil Code provides new regulations in the areas of company law, property law and inheritance law as well as intellectual property laws that take into account Ukraine’s transition to a market economy and brings Ukrainian laws and regulations closer to those that exist in more developed civil law countries.

The new Commercial Code codifies existing legislation and provides legal guidelines for economic activities and relationships by regulating the use of natural resources, intellectual property rights and the market for equity and debt securities, as well as by defining corporate rights, the procedures for executing economic contracts, the status of free economic zones, insurance procedures, banking procedures and auditing procedures. Application of the inconsistent and often conflicting rules of the new Commercial Code and the new Civil Code has resulted in conflicting judicial and administrative decisions, in particular in the context of the regulation of securities and legal entities. A law aimed at reducing inconsistencies between the Civil Code of Ukraine and the outdated Law of Ukraine “On Commercial Entities”, as well as certain other

legislative acts, came into effect on 20 June 2007. The law strives to create a consistent and comprehensive legal framework for the regulation of civil relations in compliance with the Civil Code of Ukraine.

On 6 July 2005, the Code of Administrative Procedure of Ukraine was enacted by Parliament. The Code establishes the powers of administrative courts in relation to administrative matters, the procedure of appeal in administrative courts and the procedure for the enforcement of administrative court decisions. In accordance with the Code, any decisions, actions or inaction of governmental or local self-government authorities and their officials, other than cases in relation to which another procedure is established by the Constitution or laws, can be appealed in administrative courts. Under the Code, which came into force on 1 September 2005, as amended, the Higher Administrative Court of Ukraine, as a court of first and last instance, is responsible for deciding cases related to the Central Electoral Commission's decisions, actions or failures to act in connection with the election results determined by the Central Electoral Commission or results of Ukrainian referendums, early termination of powers of a member of Parliament, as well as cases related to challenging of decisions, actions or failures to act of Parliament, the President of Ukraine, the Higher Council of Justice and the Higher Qualification Commission of Judges of Ukraine.

From 1 September 2005, the new Code of Civil Procedure, adopted on 18 March 2004, and the new Code of Administrative Procedure together replaced the previous Code of Civil Procedure by introducing different procedural rules for proceedings in courts of general jurisdiction and administrative courts. In December 2006, the Code of Civil Procedure and the Code of Commercial Procedure were amended to provide that disputes involving individual shareholders in Ukrainian companies and disputes relating to the privatisation of state property would, with certain exceptions, be heard before commercial courts rather than courts of general jurisdiction.

On 20 May 2008, Parliament approved a draft Labour Code of Ukraine in a first reading. The new code is intended to replace the existing Labour Code of Ukraine approved in 1971, which, although revised several times, is generally perceived as failing adequately to regulate labour relations arising within the market economy. The Code is also intended to replace certain other laws of Ukraine governing labour relations. The draft Code is intended to bring the labour legislation of Ukraine in line with provisions of the European Social Charter and other international standards in the sphere of labour. To become effective, the draft Labour Code must be passed by Parliament in the second and, as the case may be, third reading, signed by the President and officially promulgated.

Currently, Parliament is also considering a draft Electoral Code that aims to create a unified legal basis for preparing and holding elections for the office of President, Parliament, council members in the Autonomous Republic of Crimea, villages, cities, rayons and oblasts, as well as village and city mayors. The Electoral Code, once enacted, is expected to set forth clear rules governing the election process, including creation of election commissions, maintenance of the State Register of Voters, and other elements of nationwide and local elections.

In 2000, a new comprehensive tax code was proposed in Parliament and approved in the second reading, but rejected in its third reading in 2001. Since then, Parliament adopted several separate tax laws throughout 2002 and 2003 instead of implementing the proposed new tax code. For instance, the corporate profit tax rate was reduced from 30 per cent. to 25 per cent. effective from 1 January 2004. Also effective from 1 January 2004, the personal income tax was reformed by introducing a flat tax of 13 per cent. on substantially all levels of income until 31 December 2006 and 15 per cent. starting from 1 January 2007. Before the introduction of these changes, individuals were subject to personal income tax at rates ranging from 10 per cent. to 40 per cent. Furthermore, a new tax on interest accrued on private deposits and current accounts held by individuals in Ukrainian commercial banks was introduced, which tax will be withheld starting from 1 January 2013.

As of 1 January 2007, a number of changes were introduced into Ukrainian tax laws in accordance with WTO requirements, including changes in taxation of dividends distributable through holding companies and changes in the rates of excise and customs duties on certain goods and licence charges for various activities. The changes also introduced a number of tax incentives for investment activities in special economic zones and priority development territories, including investment tax loans and import duty exemptions for certain equipment.

The 2010 election programme of the President contemplated introduction of a 5-year tax break for small businesses and a decrease of the value added tax rate to 17 per cent. and the corporate income tax rate to 19 per cent. starting in 2011, to be followed by a gradual decrease of the corporate income tax rate to 16 per cent. The 2010 President's election programme also contemplated adoption of the Tax Code of Ukraine.

On 17 June 2010, Parliament approved in a first reading a draft Tax Code of Ukraine proposed by the Government. On 7 September 2010, Parliament cancelled its approval of the draft Tax Code in a first reading and instructed the Government to submit to Parliament a revised draft Tax Code taking into account comments received during the nationwide public discussions on the draft. On 7 October 2010, the draft Tax Code was approved by the Parliament in the first reading. The draft Tax Code remains to be approved by Parliament in a second, and, as the case may be, third reading, signed by the President and officially promulgated to become effective. See "*Public Finance – Revenues*".

On 8 July 2010, Parliament approved the restatement of the Budget Code of Ukraine. The restatement aims to, among other things, further develop medium-term budget planning; introduce modern forms and methods of management of budget funds and State and local debt management; improve the system for State control over budget performance; tighten responsibility of budget process participants; and strengthen financial independence of local budgets. See "*Public Finance – The Budget Process*".

A bill against money laundering came into force in 2003, establishing two levels of financial monitoring. At the primary level, financial institutions involved in transferring money and certain other entities or individuals are required to monitor financial transactions, while State financial monitoring is conducted by the NBU, the State Financial Monitoring Committee, which is a specially authorised executive agency for financial monitoring, and other central agencies. In February 2004, Ukraine was removed from the list of Non-Cooperative Countries and Territories of the Financial Action Task Force on Money Laundering, or FATF, the international organisation combating money laundering, and in January 2006, the FATF ended formal monitoring of Ukraine.

In May 2010, Parliament enacted a law, which came into force on 21 August 2010, significantly amending the Ukrainian anti-money laundering legislation in order to implement 40 revised recommendations and nine special recommendations of the FATF, as well as the directive of the European Parliament on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. The law extends a list of entities that are required to monitor financial transactions at the primary level by adding to the list such companies and individuals as antique and arts dealers, realtors, precious metal and stone dealers, notaries, attorneys, auditors, accountants and certain other entities. The law also extends the list of state agencies authorised to conduct State financial monitoring over financial transactions involving these entities. In addition, the law provides that a financial transaction is subject to monitoring if its aggregate value equals or exceeds UAH 150,000 (or its equivalent in foreign currency) (previously UAH 80,000), subject to exceptions that reduce or increase the general threshold amount for certain specific transactions including, for instance, transactions with real estate or gaming. Furthermore, the law broadens the list of grounds on the basis of which a financial transaction may be viewed as a suspicious operation and requires the entities that monitor financial transactions to use certain additional precautionary measures in respect of clients whose activities present a higher level of potential money-laundering concern, including, among others, certain foreign officials and financial institutions.

On 1 January 2004, the Laws of Ukraine "On Mortgage" and "On Mortgage Lending, Transactions with Consolidated Mortgage Debt and Mortgage-Backed Certificates" came into force. These laws were amended in December 2005 in order to eliminate certain inconsistencies and gaps and were further supplemented by the Law of Ukraine "On Mortgage Bonds" with effect from 24 January 2006. These laws have permitted, among other things, mortgage-backed financial instruments and their trading on the securities market. The laws have also introduced a procedure for state registration of mortgages and established new rules for the determination of priority of claims over collateral. The Law of Ukraine "On Securing Claims of Creditors and Registration of Encumbrances", adopted in November 2003, further regulates the granting of security over movable property by providing a broad definition of an encumbrance, setting up a comprehensive regime of registration and introducing a requirement for advance notice of enforcement.

In July 2004, the Law of Ukraine “On State Registration of Property Rights to Immovable Property and Their Restrictions” was passed and, in March 2010, the revised version of this Law came into force. The revised version of this Law establishes legal, economic and organisational measures to create a unified system of registration of property rights to land plots and other real property by submitting a single notification to a respective registration authority. According to the revised Law, the Ministry of Justice of Ukraine and its regional divisions will perform the registration of any rights and encumbrances on immovable property and the Register of Property Rights to Immovable Property will be in effect starting 1 January 2012. However, as of the date of this Prospectus, such unified system has not yet been created and property rights to land plots are registered in a register that is separate from the register in which property rights to buildings located on such land plots are registered.

On 1 July 2004, the Law of Ukraine “On State Registration of Legal Entities and Individuals-Entrepreneurs” came into force. This law simplifies the procedure for state registration of natural persons and legal entities undertaking business activities, providing for registration with state statistical bodies, tax authorities and social security funds by submitting a single notification to a state registrar. In June 2005, the Cabinet of Ministers further simplified the procedure for state registration of persons and entities undertaking business activities. Currently, the system of state registration of legal entities and individual entrepreneurs through submission of a single notification to a state registrar is fully operative in all regions of Ukraine.

In June 2005, Ukraine adopted the Law of Ukraine “On Organisation of Formation and Circulation of Credit Histories” permitting the establishment of credit bureaus that collect information on borrowers (both individuals and legal entities) and compile credit histories of each borrower. The information gathered by such credit bureaus is intended to assist Ukrainian banks in evaluating and managing the credit risk of prospective borrowers. Several credit bureaus established in Ukraine are operating in the field of the collection, processing, storage and use of credit information.

On 1 September 2005, the Law of Ukraine “On International Private Law” came into force. This law supplements the Civil Code of Ukraine and governs private legal relationships involving foreign elements (parties, subject matter or legal facts). This law covers such issues as the determination of governing law, the legal capacity of foreigners, submission to the jurisdiction of Ukrainian courts, service of process, and recognition and enforcement in Ukraine of foreign judgments. In January 2006, Ukraine also acceded to the UNIDROIT Convention on International Financial Leasing and the UNIDROIT Convention on International Factoring.

For a number of years, Ukraine has been working on the harmonisation of its legislation with EU legislation. The “All-Nation Programme of Harmonisation of the Legislation of Ukraine to EU Legislation” was adopted by Parliament in 2004. As a result, certain draft laws and regulations are subject to obligatory examination by the Ministry of Justice as to compliance with EU law. In addition, new draft laws are developed by applying a comparative analysis of comparable regulations in the EU. In February 2006, Ukraine enacted the Law of Ukraine “On the Enforcement of Judgments of the European Court of Human Rights (“ECHR”) and the Application of its Case Law”. The law is Ukraine’s first on the enforcement of ECHR judgments, introducing the mechanisms for enforcing ECHR judgments in Ukraine and the legal framework for the application of ECHR case law. One of the provisions of the law is the requirement that monetary remedies awarded in a judgment be paid by Ukraine within three months of the judgment becoming final. The law also provides for the enforcement of non-monetary remedies ordered by the ECHR, such as *restitutio in integrum* (i.e., restoration to the original position). It also identifies the responsible state bodies, expands on the mechanism for their collaboration and sets deadlines within which they must comply.

Between 2005 and 2007, in preparation for Ukraine’s 2008 accession to the WTO, numerous laws were enacted governing such areas as customs, standards and compliance assessments, foreign currency settlements, insurance, banking, licensing, intellectual property protection and taxation of agricultural producers. One of these was the law pursuant to the requirements of the WTO Agreement on Trade Aspects of Intellectual Property. Certain laws enacted to comply with WTO requirements were further amended and additional work is underway on further amendments to Ukrainian legislation in line with the WTO agreements and Ukraine’s commitments undertaken within the accession process.

A new edition of the Law of Ukraine “On Securities and the Stock Market” was enacted by Parliament on 23 February 2006 and, subject to certain exceptions, came into force on 12 May 2006. The revised law has updated the Ukrainian legal and regulatory framework governing the issuance and circulation of securities and codified in one document various stock market rules. In March 2006, Ukraine also enacted a new law “On Holding Companies in Ukraine” governing the creation, operation (including decision-making processes, mandatory information disclosure and liability) and liquidation of holding companies in Ukraine. In September 2006, Parliament enacted a new law “On the Management of State-Owned Assets” setting out the legal framework for the management of various state-owned assets, including state property transferred to state enterprises and state-owned shares in joint stock and limited liability companies.

On 17 September 2008, Parliament passed a new law “On Joint Stock Companies”, which is aimed at eliminating gaps in corporate law, detailing procedures for the creation, activities and termination of joint stock companies and strengthening protection of shareholders’ interests. The law also clarifies the legal status of joint stock companies, which are to be incorporated in the form of public or private joint stock companies, and the rights and obligations of their shareholders. The law became effective on 30 April 2009 and existing joint stock companies have until 30 April 2011 to change their form into a public or private joint stock company and otherwise bring their charters and internal governance into compliance with the new law.

In addition, in 2008 and 2009, the legislative and regulatory framework governing recapitalisation of Ukrainian banks by the State was enacted. In particular, pursuant to a law passed on 31 October 2008, the State may purchase shares in Ukrainian banks either for cash or against contributions of T-bills and the share capital increases in such instances are carried out pursuant to simplified procedures. See “*The Banking and Securities and Financial Services Markets in Ukraine – Recent Developments in the Banking Sector*”.

Despite the developments in post-independence legislation, many laws continue to be unclear, internally inconsistent and in conflict with other legislation, and may be subject to varying interpretations and unpredictable implementation by Ukrainian courts, state agencies and authorities. Finally, enforcement of such laws is relatively untested. See “*Risk Factors – Risk Factors Relating to the Guarantor – Ukraine’s developing legal system creates risks and uncertainties for investors in Ukraine and for participants in the Ukrainian economy.*”

Legal Proceedings

From time to time, Ukraine, its state agencies and its political subdivisions become involved in disputes with various parties. These disputes most often involve issues of trade or inward investment, and are typically brought before arbitral panels, although court proceedings also occur.

The following section describes the active material disputes in which Ukraine is currently involved. This section does not describe legal proceedings against State-owned companies except to the extent that Ukraine is also a party. For a description of an arbitration proceeding between RosUkrEnergo AG and Naftogas see section “*Economy of Ukraine – Oil and Gas - Russia*”.

In addition, from time to time Ukrainian authorities may receive information to the effect that various parties may be contemplating legal or arbitral proceedings against the state or its agencies. Unless and until formal action is taken to commence such proceedings, it is not possible to form a view as to the likelihood such proceedings may commence, the nature and magnitude of any award that might be sought or the merits, if any, of any such claim.

An adverse decision in proceedings involving Ukraine and resulting in awards of substantial damages or other monetary remedies denominated in currency other than the hryvnia, could strain Ukraine’s foreign currency reserves and have a negative effect on its ability to perform its obligations under the Guarantor.

Tatneft arbitration

On 21 May 2008, the Russian company OJSC “Tatneft” (“Tatneft”) filed a notice of arbitration and statement of claim against Ukraine pursuant to UNCITRAL Arbitration Rules, proposing Paris, France as site of the arbitration.

Tatneft is a shareholder in CISC “Ukratnafta” (“Ukratnafta”), incorporated in Ukraine pursuant to the Decree of the President of Ukraine “On Creation of Transnational Financial-Industrial Oil Company “Ukratnafta” dated 29 November 1994 and the Agreement between the Government of Ukraine and the Government of the Tatarstan Republic (Russia) dated 4 July 1995. The initial shareholders in Ukratnafta included Tatneft (20.01 per cent.), the State Committee of the Tatarstan Republic on State Property Management (29.73 per cent.), the SPF (49.99 per cent.) and seven minority shareholders (0.27 per cent.).

In April 1998, due to a failure of certain shareholders to pay for their shareholdings, a decision was made at the general meeting of shareholders of Ukratnafta to sell a number of shares to other foreign investors, as a result of which Tatneft’s shareholding was reduced to 8.61 per cent., while new shareholders Amruz Trading AG and Seagroup International Inc. acquired 8.34 per cent. and 9.96 per cent. shareholdings, respectively. Thereafter, the shareholding of the State Committee of the Tatarstan Republic on State Property Management was reduced to 28.78 per cent., while the SPF shareholding decreased to 43.05 per cent. On 27 June 2009, shares owned by Amruz Trading AG and Seagroup International Inc. in the total amount of 18.3 per cent. were sold to another minority shareholder LLC “Korsan”, as a result of which its share in Ukratnafta increased to 19.4 per cent. In addition, both before and after initiation of the arbitration proceeding, proceedings in Ukrainian courts were ongoing with respect to challenging of sales of shareholdings in Ukratnafta to Amruz Trading AG, Seagroup International Inc. and the State Committee of the Tatarstan Republic on State Property Management.

In its notice of arbitration and statement of claim Tatneft claims that Ukraine has allegedly violated the Agreement between the Cabinet of Ministers of Ukraine and the Government of the Russian Federation on Facilitation and Mutual Protection of Investments because Tatneft and other foreign shareholders were deprived of the right to effective control over their investments. Tatneft initially sought reinstatement of what it alleged was the lawful management at Ukratnafta, reimbursement of arrears for oil supplies in the amount of U.S.\$520.0 million and payment of compensation for the loss of control over its shareholding in Ukratnafta in the amount of U.S.\$610.0 million.

On 29 June 2009, Tatneft increased the amount of its claim to U.S.\$2.4 billion. The increase in the amount, which includes the previously-asserted claims in the amounts of U.S.\$520.0 million and U.S.\$610.0 million, relates to alleged losses in the amount of approximately U.S.\$1.3 billion incurred by Tatneft in connection with the sale of an 18.3 per cent. shareholding by Amruz Trading AG and Seagroup International Inc. to LLC “Korsan”, such sale allegedly being a forced expropriation of shares held by Amruz Trading AG and Seagroup International Inc in Ukratnafta.

On 16 January 2009, the arbitration tribunal was constituted, and on 29-31 March 2010, oral hearings on jurisdictional matters were held. On 28 September 2010, the arbitral tribunal rejected Ukraine’s objections to the jurisdiction of the arbitration tribunal. The parties must agree a further schedule of submissions and hearings on the matter by 29 November 2010.

Semeniy litigation

On 24 February 2010, Mr Semeniy, a Russian citizen, filed a claim with the Moscow Arbitration Court against the Government of the Russian Federation and the Government of Ukraine. The claim alleges that Ukraine breached the national legislation rules and the Agreement between the Government of the Russian Federation and the Government of Ukraine on Avoidance of Double Taxation of Income and Property and Prevention of Tax Evasion dated 8 February 1995. In particular, the claim alleges that actions and failures to act of Ukrainian state authorities, including law enforcement authorities, resulted in the expropriation of the claimant’s income, property and proprietary and intangible rights owned by the claimant in OJSC “Vatra”. The amount of the claim is approximately 716 billion Russian roubles, equivalent to approximately U.S.\$23.6 billion. On 5 July 2010, the Moscow Arbitration Court ruled that the matter was not subject to consideration by an arbitration court and closed the proceedings. On 26 July 2010, the plaintiff filed an appeal with the Ninth Arbitration Appeals Court against the Moscow Arbitration Court ruling. On 23 August 2010, the Ninth Arbitration Appeals Court issued a ruling rejecting the plaintiff’s appeal and upholding the ruling of the Moscow Arbitration Court. The plaintiff can, however, further appeal against this ruling within two months from 23 August 2010. As at 29 October 2010, the Ministry of Justice of Ukraine did not have information as to whether such further appeal was filed by the plaintiff.

Vanco arbitration

On 16 July 2008, Vanco Prykerchenska Limited (“Vanco”) filed a request for arbitration against Ukraine in accordance with the Rules of the Arbitration Institute of the Stockholm Chamber of Commerce. The ground for the request was the termination by the Cabinet of Ministers of Ukraine of the Hydrocarbons Sharing Agreement (the “Agreement”) entered into on 19 October 2007 between the Cabinet of Ministers of Ukraine and Vanco International Limited for hydrocarbons to be extracted within the Prykerchenska subsoil block of the Black Sea continental shelf.

On 19 October 2007, Vanco became an assignee of Vanco International Limited under the Agreement. The main elements of relief that Vanco seeks are: a declaration that the Agreement is valid and binding for the parties; a declaration that Ukraine breached the Agreement; specific performance of the Agreement by Ukraine; and reimbursement by Ukraine of damages alleged to have been incurred as a result of Ukraine’s failure to perform the Agreement as well as of expenses incurred in connection with the arbitration proceedings. In its request for arbitration, Vanco specified the amount of the claim as not less than U.S.\$100.0 million. In its statement of claim submitted on 17 April 2009, Vanco did not specify the amount of the claim but requested specific performance of the Agreement and issuance of a decision holding the unilateral termination of the Agreement by Ukraine to be unlawful.

On 7 August 2009, the State of Ukraine filed its statement of defence and on 13 November 2009, Vanco submitted its statement of reply. On 27 December 2009, the Arbitration Tribunal divided the arbitration proceedings into two stages, the first stage being the consideration of the matter on its merits and issuance of a decision on the validity of the Agreement, and the second stage being the determination of the damages borne by the parties and issuance of a decision on reimbursement of such damages. On 29 January 2010, Ukraine filed its statement of rejoinder. On 15-17 March 2010, oral hearings on this matter were held, and on 17 May 2010 the parties filed post-hearing briefs. Subsequently, for the purposes of entering into negotiations for a peaceful settlement, the parties applied to the Arbitration Tribunal requesting it to suspend the issuance of the award on the merits of the case. On 7 July 2010, the Arbitration Tribunal agreed to suspend the issuance of the award until 30 September 2010 and on 23 September 2010, the Arbitration Tribunal extended this deadline until 31 December 2010. As at 1 October 2010, the parties were discussing a draft of a peaceful settlement agreement. Should the parties fail to reach an agreement by peaceful settlement by 31 December 2010, arbitration proceedings may recommence.

Lemire arbitration

In December 2006, Joseph Lemire, a U.S. citizen, filed a request for arbitration against Ukraine at the ICSID. This request for arbitration alleges failure to perform the Settlement Agreement dated 20 March 2000 between the Cabinet of Ministers of Ukraine and Joseph Lemire, violations of the Agreement between Ukraine and the United States on Promotion and Mutual Protection of Investment, dated 4 March 1994 and unfair treatment of Joseph Lemire and the radio station owned by him operating in Ukraine, in respect of granting licences for radio frequencies (which, according to the claimant, were unfairly granted to other stations).

The Settlement Agreement was intended to settle a lawsuit during the 1990s, under which Mr. Lemire sought damages of approximately U.S.\$15.0 million. In 2007-2008, the parties exchanged written memorandums and written testimonies of parties’ witnesses, and hearings on the merits were held in December 2008.

On 14 January 2010, the Arbitration Tribunal issued an award on jurisdiction and liability finding Ukraine liable for the failure to perform Article II(3) of the Agreement between Ukraine and the United States on Promotion and Mutual Protection of Investment but rejecting all claims against Ukraine in respect of the alleged failure of Ukraine to perform under the Settlement Agreement. The Arbitration Tribunal also decided that the determination of damages payable by Ukraine to the claimant would be considered at the second stage of the arbitration during 2010. On 16 April 2010, the claimant filed its memorandum on the issue of the amount of compensation, according to which the amount of damages payable to the claimant ranges from approximately U.S.\$30.5 million to U.S.\$46.7 million. In addition, the claimant demands reimbursement of moral damages in the amount of U.S.\$3.0 million and expenses incurred in connection with the arbitration proceedings in the amount of U.S.\$1.6 million. Ukraine filed its counter-memorandum to the claimant’s

memorandum on 21 June 2010. Hearings on these issues were held on 12 July 2010, following which the arbitration tribunal is expected to render a decision. On 27 October 2010, the arbitration tribunal notified the parties about the closure of the proceeding. Pursuant to ICSID Arbitration Rules, an arbitral award shall be drawn up within 120 days after closure of the proceeding, i.e. 27 October 2010 subject to a possible extension of up to additional 60 days.

GEA arbitration

On 30 October 2008, ICSID received a request for arbitration from GEA Group Aktiengesellschaft, a German company (“GEA”), against the State of Ukraine. The request alleges that Ukraine has failed to comply with the Agreement between Ukraine and Germany on Facilitation and Mutual Protection of Investments dated 15 February 1993.

The ground for the dispute is an alleged failure by state enterprise OJSC “Oriana” (“Oriana”) to comply with its undertakings under a contract for the conversion of fuel into petrochemical products dated 13 December 1995 and related contracts. In the request for arbitration GEA seeks an award for damages of U.S.\$40.0 million plus 3 per cent. interest per annum, accruable from 28 December 2000, and reimbursement of expenses incurred in connection with the arbitration proceedings.

On 21 November 2008, the request for arbitration was registered by ICSID and on 12 May 2009, the Arbitration Tribunal held its first session, at which the procedural schedule for written submissions was determined. Ukraine provided its submission on the merits of the case and jurisdictional issues on 11 January 2010, followed by the claimant response submitted by GEA on 15 April 2010. Ukraine provided its respondent’s rejoinder on 15 June 2010. Oral hearings on this matter occurred on 5-9 July 2010. An arbitration award in this matter is expected not earlier than the end of 2010.

Globex/Global arbitration

On 21 May 2009, ICSID received a request for arbitration from U.S. companies Globex International, Inc (“Globex”) and Global Trading Resource Corp. (“Global”) against Ukraine. On 11 June 2009, ICSID registered the request.

In their request for arbitration, Globex and Global allege that Ukraine failed to comply with the Agreement between Ukraine and the United States on Facilitation and Mutual Protection of Investments dated 4 March 1994 because of the breach by the Ukrainian party of certain contracts on purchase of poultry products entered into with the claimants. Global’s claim is in the amount of U.S.\$28.0 million and Globex’s claim is for U.S.\$6.8 million.

On 9 December 2009, the arbitration tribunal was formed and on 5 January 2010 Ukraine submitted its objections to the jurisdiction of the arbitration tribunal followed by the claimants’ response on 15 March 2010. On 26 March and 9 April 2010, the parties submitted the respondent reply and the claimants’ rejoinder, respectively. Oral hearings on jurisdictional matters and the first session of the arbitration tribunal on procedural issues were held on 7 July 2010. As at 29 October 2010, the arbitration tribunal has not yet ruled on Ukraine’s objections to the jurisdiction of the arbitration tribunal.

Torno/Beta arbitration

On 22 September 2009, the International Chamber of Commerce (Paris) received a request for arbitration from Italian companies Torno Global Contracting S.P.A. (previously known as Torno Internazionale S.p.a.) (“Torno”) and Beta Funding S.R.L. (“Beta”) against the Ministry of Transport of Ukraine and the State Road Service of Ukraine (“Ukravtodor”).

In their request for arbitration, Torno and Beta allege that the Ministry of Transport of Ukraine and Ukravtodor breached the terms of the General Agreement on Cooperation in the Reconstruction and Operation of the Kiev-Odessa Highway dated 8 October 2003 entered into between the Ministry of Transport and Communications of Ukraine, Ukravtodor and Torno. The claimants indicated in the request for arbitration that the amount of their claims is not less than €45.0 million.

On 15 December 2009, Ukravtodor and the Ministry of Transport of Ukraine submitted to the International Arbitration Court at the International Chamber of Commerce their reply to the request for arbitration and the counterclaim. As at the date of this Prospectus, the arbitration tribunal has been constituted and the parties have agreed a schedule of submissions and hearings on the matter. According to the schedule, a number of submissions will need to be made by the parties throughout 2010, 2011 and 2012 and the oral hearings are currently scheduled for March 2012.

Naftac Limited arbitration

On 25 November 2009, the Permanent Chamber of the Arbitration Court (the Hague) received a request for arbitration from Naftac Limited (Cyprus) (“Naftac”) against the National Environmental Investment Agency of Ukraine (the “Agency”) in connection with the performance of the Collateral Custody Agreement entered into on 19 December 2008 by the Agency, Fortis Intertrust (Netherlands) B.V. and Naftac. According to its claim, Naftac demands compensation in connection with the alleged violation of its rights as an investor, with the amount of its claims being not less than U.S.\$185 million that includes compensation of losses incurred by Naftac, including expenses, liabilities, claims and loss of profit; reimbursement of expenses incurred in connection with the arbitration proceedings; and payment of interest accrued both before and after judgement at the interest rate to be determined. On 8 April 2010, the arbitration tribunal was formed. On 7 May 2010, Naftac requested the tribunal to grant interim (provisional) measures. On 11 June 2010, the Agency submitted its respondent’s response to claimant’s application for interim measures and on 16 July 2010 oral hearings on these issues were held. On 27 July 2010, the tribunal issued a ruling refusing to grant interim (provisional) measures requested by the plaintiff. The Agency submitted its rebuttal to the claim on 10 September 2010, while the plaintiff is to submit its rejoinder by 11 November 2010.

Transportation Investment Limited claims

On 2 July 2010, the Ministry of Justice of Ukraine received a notice from Transportation Investment Limited (“TIL”) (United Kingdom) on the pre-trial settlement of the dispute between Ukraine and TIL pursuant to Article 8(1) of the Treaty between the Government of Ukraine and the Government of the United Kingdom of Great Britain and Northern Ireland on promotion and mutual protection of investments dated 10 February 1993 (the “Treaty”), such settlement to be carried out within 3 months from the date of the notice.

In its notice, TIL alleges that it is incurring significant losses in connection with its investments made in Ukraine through its subsidiary, PE “Ukrtranscontainer” (“Ukrtranscontainer”). TIL alleges that its losses and damages have arisen in connection with the construction by Ukrtranscontainer of a container terminal in Illichivsk port. The terminal was being constructed pursuant to a joint activities agreement entered into by Ukrtranscontainer and State Enterprise “Illichivsk Marine Trade Port” (the “JAA”), which was terminated through court proceedings in Ukraine. TIL currently estimates its losses to be in the amount of over U.S.\$1 billion, including lost profit under the JAA. On 14 September 2010, the parties agreed to extend the period for the pre-trial settlement of the dispute until 16 October 2010. Ukraine rejected the terms of the settlement of the dispute proposed by TIL. Accordingly, TIL is entitled to submit the dispute to trial pursuant to Article 8(2) of the Treaty.

Regional Administration

Executive power in each of Ukraine’s 24 oblasts, special-status cities (Kyiv and Sevastopol) and rayons (or subdivisions thereof) is vested in the respective region’s state administration. Each state administration is headed by a governor who is appointed by the President upon nomination of the Cabinet of Ministers. In addition, municipal government is administered by a local Council, a body made up of representatives elected by the population of the region; such councils are elected in villages, cities, rayons and oblasts. In certain regions, local councils may, in addition to local state administrations, establish executive bodies; otherwise, either a local state administration or a mayor who is subject to direct election by the population acts as such executive body. Crimea is an autonomous republic within Ukraine, with its own parliament, government and constitution (passed by the parliament of the Autonomous Republic of Crimea and approved by the Parliament of Ukraine), but remains subject to the Constitution, laws and regulations of Ukraine.

On 30 July 2010, the law governing elections of local Councils' members came into effect. Among the new law's provisions are a modification of the system for electing members of oblast, city, and rayon Councils as well as the parliament of the Autonomous Republic of Crimea. The law replaces a pure proportional system previously used for the election of members of such bodies with a mixed system, under which half the seats will be elected by majority voting and the other half under a proportional representation system. In addition, all members of village councils will be elected on the basis of majority vote.

International Relations

Ukraine has established diplomatic relations with 167 countries, is a member of over 100 international organisations and attaches significant importance to developing relations with international organisations. Ukraine is a member of the United Nations ("UN"), is a member of several UN bodies and specialised agencies and participates in the organisation's activities in the areas of security, human rights, economic co-operation and environmental protection. Ukraine has signed and ratified the Non-Proliferation Treaty and certain other conventions banning weapons of mass destruction. Ukraine is a member of the IMF, the World Bank, the WTO and a number of other international organisations, and it co-operates closely with the Organisation for Economic Co-operation and Development ("OECD").

As at 30 September 2010, Ukraine was party to over 900 multilateral treaties and approximately 4,000 bilateral treaties, including treaties on promotion and mutual protection of investments entered into with 72 foreign states. International treaties ratified by Parliament are an integral part of Ukraine's domestic legislation and will prevail over such domestic laws and regulations whose provisions are inconsistent with international treaties.

Ukraine is a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (with a reservation to the effect that, in respect of the awards made in a state that is not a party to the New York Convention, Ukraine will only apply the New York Convention on a reciprocal basis) and the Convention on the Settlement of Investment Disputes between States and Nationals of Other States. Ukraine has entered into treaties on the recognition and enforcement of judgments with certain CIS countries and other countries including Cyprus, Turkey, Hungary, Bulgaria and China. However, Ukraine has not entered into such treaties with Ireland, the United States or the United Kingdom.

In June 2010, the Committee for Economic Reform chaired by the President of Ukraine (the "Reform Committee") presented for public comment the Programme of Economic Reforms in 2010-2014 "Prosperous Society, Competitive Economy, Efficient State" (the "Economic Reform Programme") (see "*Economy of Ukraine – Action Programmes*"), which provides for the following targets of Ukraine's foreign policy for 2010-2014:

- at the first stage that should take place by the end of 2010, Ukraine should implement comprehensive reforms required for introduction of a free trade area (the "FTA") with the EU and development of association relations between Ukraine and the EU in line with the Ukraine-EU association agenda (the "Association Agenda"). In addition, Ukraine should, among other things, execute a road map for visa-free regime with the EU and create a regulatory framework for its implementation as well as develop a national road map that would provide for intensified cooperation with the OECD and certain international financial organisations;
- at the second stage that should be completed by the end of 2012, Ukraine should, among other things, complete negotiations on the introduction of the Ukraine-EU FTA, such FTA to become a part of the Association Agreement between Ukraine and the EU. Ukraine should also enter into and implement a FTA agreement with other CIS Member States in line with the WTO requirements, and develop and perform the Programme for Long-Term Trade and Economic Cooperation with the Russian Federation; and
- at the third stage that should be completed by the end of 2014, Ukraine should, among other things, continue developing a regulatory framework and customs procedures required for the operation of the FTA with the EU, working on creation of FTAs with other main trade partners of Ukraine and implementing measures aimed at Ukraine's accession to the OECD.

Supranational Organisations

WTO

In 2008, after an accession process lasting almost 15 years, Ukraine joined the World Trade Organisation. On 5 February of that year, the WTO's General Council approved the accession package and the President of Ukraine and the Director General of the WTO signed the Protocol of Ukraine's Accession. The law ratifying the Protocol was passed in Parliament on 10 April 2008 and signed by the President on 16 April 2008. On 16 May 2008, upon completion of internal WTO procedures, Ukraine became the 152nd member state of the WTO.

As part of the accession process, Ukraine held bilateral negotiations with more than 50 WTO members. In addition, a number of laws were enacted by Parliament to address inconsistencies between Ukrainian legislation and the WTO agreements and requirements. See "*Political Framework of Ukraine — The Judicial System and Legal Framework*".

The Government expects to continue amending certain laws and regulations of Ukraine to comply with the WTO agreements and with Ukraine's specific commitments made during the accession process. Expected amendments include changes to laws governing, among other things, standardisation and certification, consumer rights protection and implementation of an additional import duty that could be used as a temporary mechanism in the event of a significant deterioration in the country's balance of payments. Other important tasks in the context of the Ukraine's membership in the WTO include Ukraine's participation in the multilateral negotiations of the Doha Development Round and bilateral negotiations on other countries' accession to the WTO, implementation of efficient mechanisms for the state support of national producers and promotion of investments in Ukrainian industrial and agricultural enterprises. In addition, Ukraine has applied for accession to the WTO Agreement on Government Procurement. Following Ukraine's accession to the WTO, Ukraine has also commenced negotiations on creation of free trade areas with the EU (see – "EU"), Canada, Singapore and Turkey and is currently considering commencement of negotiations on free trade areas with a number of other countries. On 24 June 2010, a free trade agreement was signed between Ukraine and the European Free Trade Association (whose members are Iceland, Lichtenstein, Norway and Switzerland).

EU

Accession to the EU is a long-term strategic goal of the Government. The first and most important step towards European integration was the signing of the Partnership and Co-operation Agreement with the EU in June 1994, which came into force in March 1998 ("PCA"). On 5 March 2007, Ukraine and the EU launched negotiations for execution of a new agreement with the EU, known as an Association Agreement between Ukraine and the EU. By its terms, the PCA is extended automatically on an annual basis until execution of the Association Agreement.

At the meeting of the Council for Cooperation between Ukraine and the EU held on 16 June 2009, the Association Agenda was signed, which replaced the EU-Ukraine Action Plan and became an important step towards Ukraine's integration into the EU. The main purpose of the Association Agenda is to allow for a deepening of co-operation between Ukraine and the EU, as the Association Agenda requires mutual actions by Ukraine and the EU, in contrast to the earlier Ukraine-EU Action Plan, which largely contained requirements to be met by Ukraine.

The Association Agreement is viewed by Ukraine as one of the stages of implementation of Ukraine's strategic goal of accession into the EU. Ukraine and the EU have agreed that the grounds for the new agreement should be both political association and economic integration of Ukraine and the EU. In terms of economic integration, Ukraine intends to satisfy the prerequisites for its participation in the EU domestic market through the concurrent gradual implementation of free movement of goods, services and capital, and partially free movement of the labour force, based on the principles of freedom of competition and economy. Currently, negotiations on the Association Agreement are being held by four joint EU-Ukrainian working groups: Political Dialogue for Foreign and Security Policy; Justice, Freedom and Security; Economic, Sectoral and Human Potential Issues; and Creation of Free Trade Area Issues. Furthermore, a draft

Association Agreement that is being negotiated provides for strengthening of cooperation in the regulatory sphere and continuation of Ukraine's work on the adaptation of Ukrainian laws to the EU legislation in such spheres as, among others, trade in goods, technical barriers in trade, trade protection instruments, sanitary and phytosanitary measures, trade relations in the energy sphere, company incorporation, capital movements and current payments, intellectual property, anti-monopoly policy, state support and public procurement; provided that any work on the enactment of necessary new laws or amendments to existing laws should be carried out concurrently with the creation of efficient mechanisms for implementation of such laws.

Ukraine's accession to the WTO created the necessary preconditions for the launch of formal negotiations for introduction of an FTA with the EU. In twelve rounds of negotiations on the FTA held between Ukraine and the EU from 2008 to August 2010, the parties discussed a broad spectrum of issues in such spheres as tariffs; trade in goods, including technical barriers in trade, trade protection instruments, sanitary and phytosanitary measures; cooperation on the customs issues; trade relations in the energy sphere; services; investments, capital movements and current transfers; intellectual property protection; dispute resolution; competition issues; transparency; sustainable development and trade, and public procurement.

In April 2004, Ukraine executed the Protocol on Accession of 10 New Member States of the EU to the Partnership and Co-operation Agreement. All free trade agreements Ukraine had with certain of the 10 new EU member states were terminated upon such states' accession to the EU. In March 2007, Ukraine executed the Protocol on Accession of Bulgaria and Romania to the Partnership and Co-operation Agreement, which was ratified by Parliament in March 2008.

In 2005 and 2007, Ukraine signed agreements with the EU relating to trade in certain steel products, which established quotas for Ukrainian steel product exports to the EU. In connection with Ukraine's accession to the WTO, with effect from 28 May 2008, the EU cancelled quotas for Ukrainian steel exports and terminated the related licensing regime. Upon the cancellation of quotas, Ukraine became subject to the EU import surveillance system, which remained in effect until 31 December 2009. A bilateral agreement on trade in textile products signed with the EU in May 1993 (and extended several times thereafter) terminated automatically upon Ukraine's accession to the WTO. See "*External Sector – International Trade*".

With effect from 30 December 2005, Ukraine was given market economy status by the EU. The most significant benefit of the new status is that Ukraine is now better protected against charges of illegally dumping goods on the EU market. Any EU member state that takes anti-dumping measures against Ukraine must prove its case, whereas formerly the burden of proof was on the relevant Ukrainian exporter. In 2009, against the background of the global economic downturn, the EU remained the largest external trade partner of Ukraine, with exports of goods and services from Ukraine amounting in 2009 to U.S.\$12.5 billion (25.4 per cent. of total exports of goods and services), and imports of goods and services to Ukraine amounting to U.S.\$18.4 billion (36.3 per cent. of total imports of goods and services), or a 43.7 per cent. and 43.8 per cent. decrease compared to 2008, respectively. In the six months ended 30 June 2010, the EU remained the largest external trade partner of Ukraine with exports of goods and services from Ukraine amounting to U.S.\$7.1 billion (24.9 per cent. of total exports of goods and services), or a 31.6 per cent. increase compared to the same period of 2009, and imports of goods and services to Ukraine amounting to U.S.\$9.4 billion (33.5 per cent. of total imports of goods and services), or a 16.3 per cent. increase compared to the same period of 2009.

In June 2007, Ukraine and the EU signed agreements on re-admission and visa facilitation. The agreements entered into force in February 2008 and aim to combat illegal migration. In October 2008, Ukraine and the EU began discussions with the goal of permitting Ukrainian citizens to travel visa-free to the EU. In the course of these discussions, the parties intend to prepare a framework document (road map) setting forth the requirements that Ukraine must comply with in order to establish a visa-free travel regime for short-term trips of Ukrainian citizens to the EU.

The EU provides substantial financial and technical assistance to Ukraine in various spheres such as legal reform, the strengthening of border infrastructure, the improvement of its anti-money laundering system and the counteraction of illegal human and drug trafficking. Currently, the EU is the largest donor to Ukraine. Since 1991, total financial and humanitarian assistance provided by the EU to Ukraine as well as assistance provided within the framework of the Technical Aid for the Commonwealth of Independent States (TACIS)

programme amounted to more than €1.0 billion. Ukraine expects that financial co-operation with the EU aimed at implementation of infrastructure projects in Ukraine will continue in the future, including within the Framework Agreement entered into between Ukraine and the European Investment Bank in 2005. See “*Public Debt – International Financial Organisations*”.

In recent years, the EU has intensified co-operation with Ukraine on energy matters, including nuclear energy, space exploration and environment. The EU has increased political and financial support in reforming the Ukrainian energy sector, including modernisation of the Ukrainian gas transport system and mining industry, improvement of the quality of oil refining products, preparation of a feasibility study on extension of the Odessa-Brody oil pipeline and development of alternative energy sources, as well as mitigation of the consequences of the Chernobyl disaster.

In 2005, Ukraine and the EU signed the Memorandum of Mutual Understanding on Co-operation in the Energy Sector, which covers five areas of expanded bilateral co-operation, including nuclear safety, integration of gas and electricity markets, improvement of safety of energy supplies and transit, structural reforms in the mining sector and efficiency of energy resources management.

In 2007, Ukraine and the EU launched the implementation of a programme aimed at supporting the energy sector of Ukraine. The total budget of the programme amounts to €82.0 million to be disbursed in several instalments for funding such projects as development of the Ukrainian oil and natural gas transportation infrastructure, integration of the Ukrainian energy system into the European system and an increase in the energy efficiency of the energy infrastructure objects, including efficiency of the natural gas transit through Ukrainian trunk pipelines. As at 1 September 2010, €40.0 million has been disbursed under the programme. Ukraine and the EU are currently negotiating implementation of similar support programmes for other sectors of the Ukrainian economy, including transportation and environment.

Further to the Joint Declaration signed on 23 March 2009 upon the results of the Joint EU-Ukraine International Investment Conference on the Modernisation of Ukraine’s Gas Transit System, Ukraine held several rounds of discussions on possible investment mechanisms with experts from the European Commission, the World Bank, the European Investment Bank and the EBRD. Within the framework of the Joint Declaration implementation, Ukraine prepared feasibility studies for the priority gas transit system modernisation projects. In 2010, the European Commission agreed to extend Euro 2.5 million to finance preparation of the combined feasibility study for the project of modernisation of the Ukrainian gas transit corridors and underground storage facilities.

In addition, in November 2006, Ukraine became an observer to the Energy Community and on 24 September 2010 the Protocol on Ukraine’s accession to the Energy Community was signed. The main tasks of the Energy Community are to extend the EU internal energy market to southeastern Europe on the basis of a legally binding framework, and to create legal and economic prerequisites for a unified grid and energy market in southeastern Europe.

In addition, in June 2010, Naftogas became an associated member of the European Union of the Natural Gas Industry (“Eurogas”). The Government expects that Naftogas’ associated membership in Eurogas will contribute to ensuring safety of natural gas supplies to the European countries and facilitate Ukraine’s participation in discussion and resolution of major issues of European energy policy.

Ukraine is a member of the Eastern Partnership initiative aimed at strengthening relations between the EU and its Eastern neighbours. Other members of the initiative include Azerbaijan, Belarus, Armenia, Georgia and Moldova. It is expected that the Eastern Partnership will focus on such measures as replacing partnership and cooperation agreements entered into between the EU and members of the initiative by new comprehensive agreements, creating enhanced FTAs, liberalising the visa regime between the EU and members of the initiative and cooperating on energy safety issues.

NATO

Relations of a distinctive partnership with NATO continue to be an important element of Ukraine's security policy. Ukraine was the first CIS country to join the "Partnership for Peace" programme in 1994 and is also an active member of the Euro-Atlantic Partnership Council.

On 9 July 1997, the "Charter on a Distinctive Partnership" between NATO and Ukraine was signed in Madrid, the supplement to the Charter having been signed on 21 August 2009. In addition, as at 1 September 2010, approximately 30 agreements have been signed between NATO and Ukraine governing their cooperation on various practical issues.

From 2003 to 2008, Ukraine developed its relations with NATO and carried out domestic reforms through the implementation of annual target plans based on the Ukraine-NATO Action Plan approved in 2002. At the meeting of the North Atlantic Council in December 2008, it was decided that Ukraine, in co-operation with NATO within the framework of the Ukraine-NATO Commission, would develop annual national programmes ("NAP") for implementing necessary reforms. The 2009 NAP was approved by the President of Ukraine on 7 August 2009 and the 2010 NAP was approved on 3 February 2010. Ukraine's priorities in the development of its relations with NATO at the current stage include the maintenance of positive political dialogue and practical cooperation as well as the furtherance of the reforms within the framework of the NAP using expert assistance and funding of NATO.

Under the Law "On Principles of Internal and External Policy", which became effective on 20 July 2010, Ukraine is to refrain from becoming a member state of military-political alliances such as NATO. However, the law calls for Ukraine to continue its cooperation with NATO and other military-political alliances in various matters of mutual interest, while preventing Ukraine from becoming dependent on any state, group of states or international organisation.

Ukraine has sent troops to, and is otherwise actively involved in, a number of NATO-led peacekeeping operations, including operations in Afghanistan, Kosovo, Iraq, and the Mediterranean. Ukraine and NATO also cooperate in such areas as counter-terrorism, counter-piracy, counter-trafficking in people, anti-money laundering, fighting cyber crimes and corruption, utilisation of excessive ammunition supplies, reforms in security and defence sectors, and air traffic. In addition, Ukraine is interested in the cooperation in non-military spheres, including NATO science programmes, environmental protection, rehabilitation and social adaptation of retired military personnel, and counteracting consequences of emergencies and disasters.

CIS and BSEC

Ukraine is, together with Russia and Belarus, one of the founding members of the CIS. Although Ukraine considers economic co-operation a priority of its membership in the CIS, it intends to remain responsible for its own affairs at an international level. Ukraine is also one of the 12 member states of the Organisation of Black Sea Economic Co-operation ("BSEC"), which also includes the Russian Federation, Georgia and the Republic of Turkey, and has chaired BSEC several times. BSEC was formed with the goal of extending economic co-operation by facilitating contracts between businesses and eliminating barriers to trade among its member states. Organised by BSEC, the Black Sea Trade and Development Bank finances and implements joint regional projects.

Foreign Countries

United States

Since independence, Ukraine has considered its relationship with the United States a strategic priority. The United States has been one of the most important contributors of FDI to Ukraine, accounting for 4.8 per cent. in 2007, 4.1 per cent. in 2008 and 3.5 per cent. in 2009. Although FDI from the United States has increased in absolute terms in recent years, its share in overall FDI has been decreasing. In 2008 and 2009, the United States was the 7th and 8th largest contributor of FDI to Ukraine, respectively. Pursuant to the U.S. Freedom Support Act enacted in 1992, Ukraine, along with other former Soviet Union countries, has received financial aid from the United States.

In previous years, relations between the two countries were strained at times due to anti-dumping allegations by the United States (in particular in relation to steel exports), intellectual property rights disputes, a perceived lack of progress in relation to Ukrainian anti-money laundering regulations and other trade-related issues, as well as suspicions about radar sales to Iraq. As a result of an alleged sale of Kolchuga military radar equipment to Iraq in defiance of UN embargoes, the United States temporarily suspended approximately U.S.\$54 million of aid to Ukraine, pending results of an investigation. However, Ukraine's active support for the U.S.-led coalition in Iraq and its participation in the coalition forces stationed in Iraq, as well as reforms of the anti-money laundering legislation, maintained good relations with the United States even prior to President Yushchenko's election in 2005.

Relations with the United States have strengthened since the election of President Yushchenko in 2005. In 2006, the Generalised System of Preferences was reinstated for Ukraine and in 2008, the Office of the U.S. Trade Representative added Ukraine to its Watch List of 30 countries with an improved level of intellectual property protection. Moreover, with effect from 1 February 2006, the United States granted Ukraine market economy status and, on 23 March 2006, the Jackson-Vanik amendment that had restricted Ukrainian exports was repealed by the United States.

In April 2008, Ukraine and the United States signed a "road map" of U.S.-Ukraine relations that outlines the priorities of bilateral co-operation. The priorities of U.S.-Ukraine bilateral co-operation envisaged by the "road map" include, among other things, assistance with Ukrainian legal system reform and law enforcement, support in the fight against corruption, co-operation in the energy sphere, intensification of activities in the sphere of disarmament and arms control and further Ukrainian military reforms. Also in April 2008, Ukraine and the United States signed a Trade and Investment Cooperation Agreement providing for, among other things, establishment of the Ukrainian-American Council on Trade and Investments. The Trade and Investment Cooperation Agreement is supplemented by cooperation agreements in other spheres, such as, for instance, science and technology, space exploration for peaceful purposes and health protection. In total, as at 1 August 2010, more than 100 international agreements have been concluded between Ukraine and the United States.

In line with signing of the Ukraine-U.S. Charter on Strategic Partnership in December 2008, new mechanisms of the bilateral intergovernmental cooperation have been launched during the recent years, with the Ukraine – United States Commission on Strategic Partnership coordinating their activities. Priority directions for the activities of the Commission on Strategic Partnership, which was inaugurated in December 2009, include foreign policy, security and non-proliferation of mass destruction weapons; energy sector; economic development; democracy and supremacy of law. In addition to the Ukrainian-American Council on Trade and Investments, bilateral bodies that have been launched include a Working Group on Energy Security established in 2009 and the Non-Proliferation and Export Control Group and the Consultations on Defense-related Issues, sessions of which are being held on a regular basis.

During the visit to the United States of the newly elected President Yanukovich in April 2010, the Ukrainian and U.S. Presidents agreed on cooperating in such spheres as renewal of the IMF programme for Ukraine, minimisation of adverse consequences of the financial and economic downturn, implementation of systematic reforms, including in the energy sector, deepening of the bilateral cooperation on the basis of the Charter on Strategic Partnership and enhancement of the activities of the bilateral mechanisms. Furthermore, during the visit, the President of Ukraine confirmed an important decision taken by Ukraine to remove its stocks of highly enriched uranium by 2012, with a substantial share of the stock to be removed by the end of 2010. President Yanukovich also announced a decision to convert Ukraine's civil nuclear research facilities to operate with low enriched uranium fuel and President Obama declared that the United States was ready to provide Ukraine with technical and financial support for such conversion. The two Presidents agreed to enhance the countries' cooperation in the sphere of use of nuclear energy for peaceful purposes, including Ukraine's efforts to diversify nuclear fuel supplies.

During the second sitting of the Commission on Strategic Partnership held in July 2010, Ukraine and the United States agreed to establish three new working groups, including a working group on peaceful nuclear energy; a working group on political dialogue and law supremacy; and a working group on science and

technologies. The third sitting of the Commission on Strategic Partnership is expected to be held by the end of 2010.

In addition, in December 2009, Ukraine completed the implementation of the “Threshold Programme” aimed at fighting corruption in Ukraine. Under the “Threshold Programme”, started in 2006, the Millennium Challenge Corporation, a U.S. government agency created to reduce poverty through sustainable economic growth, allocated U.S.\$45.0 million to Ukraine to finance the implementation of the independent external testing for prospective university students, the development of a number of anti-corruption laws and other measures. It is expected that, in late 2010, the Board of Directors of the Millennium Challenge Corporation will consider Ukraine’s participation in “Threshold Programme-2”.

Russia

Relations with Russia are considered to be of strategic importance. A number of differences between Ukraine and Russia were addressed in the context of the Friendship and Co-operation Agreement signed in May 1997. Ukrainian territorial integrity, including that of the Crimea (the population of which is two-thirds ethnic Russian), was confirmed. In addition, Ukraine agreed to the stationing of the Russia’s Black Sea Fleet in Sevastopol until 2017, in exchange for Russia’s agreement to offset Ukraine’s energy debts accumulated prior to 1993. However, certain differences between Ukraine and the Russian Federation regarding the performance of the Friendship and Co-operation Agreement and the stationing of the Black Sea Fleet still exist, including the return of certain navigational facilities to Ukraine, violation by Russia’s Black Sea Fleet of Ukraine’s environmental laws and failure to properly formalise relations on the leasing of facilities in the city of Sevastopol, as well as Russia’s violation of the jurisdiction of Ukraine in legal issues relating to Russia’s Black Sea Fleet operating in the territory of Ukraine.

Relations with Russia have strengthened since the election of President Yanukovich in 2010. A broad spectrum of political and economic issues was discussed during several visits of the Ukrainian President, Prime Minister and Minister for Foreign Affairs to Russia and visits of the Russian President, Prime Minister and Minister for Foreign Affairs to Ukraine that took place in March-May 2010. In particular, on 21 April 2010, Ukraine and Russia signed a new agreement on the stationing of Russia’s Black Sea Fleet in Ukrainian territory, under which the term of the stationing of the Russia’s Black Sea Fleet in Sevastopol was extended for a further 25-year period with an additional 5-year extension option and the amount of the lease charges payable for the Fleet stationing was increased. This new agreement also provides that a portion of the lease charges payable for the Fleet stationing will be set off against certain discounts to the price of natural gas supplied by Gazprom for domestic consumption in Ukraine. On 27 April 2010, this agreement was ratified by the Ukrainian and Russian Parliaments. In addition, a number of bilateral documents were signed during the third meeting of the Ukrainian-Russian Interstate Commission that was held in May 2010, including an agreement on the demarcation of the Ukraine-Russia land border.

Issues regarding maritime border delineation remain outstanding. On 24 December 2003, Ukraine and the Russian Federation signed the Agreement on Co-operation in Usage of the Azov Sea and the Kerch Strait (the “Azov Agreement”) which established general preconditions facilitating the process of negotiations with regard to maritime delineation and resolved a dispute between the two nations that arose after Russia began building a causeway from its mainland to an island on the Kerch Strait. The land border agreement and the Azov Agreement acknowledge that the Azov Sea (including the Kerch Strait) has historically been part of the internal waters of both Ukraine and the Russian Federation, and provide that the Azov Sea shall be divided by a state border between the two countries. Further, Ukraine and the Russian Federation agreed pursuant to the Azov Agreement to resolve all matters relating to the waters of the Kerch Strait by mutual consent. The Azov Agreement was ratified by both parties in April 2004. Since 2004, Ukraine and Russia have been negotiating the issues relating to the delineation of their respective borders in the waters of the Azov Sea and the Kerch Strait.

International relations between Russia and Ukraine have been significantly influenced by the relations between the two countries in the oil and gas sphere. Russia has in the past threatened to cut off the supply of oil and gas to Ukraine in order to apply pressure on Ukraine to settle outstanding gas debts and reduce transit fees for Russian oil and gas through Ukrainian pipelines to European consumers. Furthermore, prices

for Russian natural gas supplied to Ukraine for domestic consumption were increased by Gazprom in each of 2006, 2007 and 2008, from U.S.\$50 to U.S.\$179.5 per 1,000 cubic metres as of 1 January 2005 and 2008, respectively. On 12 March 2008, Naftogas and Gazprom signed an agreement on the development of relations in the gas sphere providing for an action plan for a transfer to direct Naftogas-Gazprom gas supply deals.

In early January 2009, Gazprom substantially decreased natural gas supplies to Ukraine, reportedly due to failure by Naftogas to timely repay all outstanding debts owed to Gazprom for natural gas supplied for Ukraine's domestic consumption in 2008. On 19 January 2009, Naftogas and Gazprom signed an agreement setting out the terms of natural gas supplies to Ukraine from 2009 through 2019 (the "Gas Supply Contract") and an agreement on volumes and conditions of the natural gas transit through the territory of Ukraine (the "Gas Transit Contract"). According to the Gas Supply Contract, the price for natural gas supplied for domestic consumption to Ukraine depends on a formula linked to changes in oil price. On 21 April 2010, further to the new Russia-Ukraine agreement with respect to the stationing of Russia's Black Sea Fleet in Ukrainian territory, amendments to the Gas Supply Contract and the Gas Transit Contract were signed, under which Gazprom has agreed to give Naftogas certain discounts from the otherwise applicable price for natural gas supplied for domestic consumption to Ukraine. In addition, Ukraine and Russia have launched negotiations in relation to two new agreements with respect to cooperation in the gas sphere and cooperation in the sphere of oil transportation to Ukrainian oil refinery plants and oil transit through the Ukrainian territory. See "*Economy of Ukraine – Principal Sectors of the Economy – Oil and Gas*".

In 2002, Ukraine and Russia entered into a framework agreement pursuant to which they agreed to establish a consortium to ensure the transit of Russian natural gas through the territory of Ukraine for the next 30 years and to provide for the construction, modernisation and operation of gas pipelines. In 2004, the participants in the consortium entered into agreement on co-operation in construction and management of the first section of the gas pipeline between Bohorodchany and Uzhgorod. However, as of 20 August 2010, a decision on the commencement of the Bogorodchany-Uzhgorod gas pipeline construction has not yet been taken by the consortium participants. See "*Economy of Ukraine – Principal Sectors of the Economy – Oil and Gas*".

Russia has on several prior occasions increased the tariffs on the export of oil, thus effectively curtailing the volume of crude oil that is processed at Ukrainian facilities and dramatically decreasing revenues at Ukrainian refineries. Since 2005, Russia significantly increased its oil export duty, which resulted in the temporary establishment of minimum retail prices for fuel by the Government of Ukraine. For example, Russian oil export duty rose from U.S.\$101.00 per tonne as at 1 December 2004 to U.S.\$237.60 per tonne as at 1 October 2006. After that, Russian oil export duty fluctuated between U.S.\$156.40 per tonne as of 1 April 2007 to a historical maximum of U.S.\$495.9 per tonne as of 1 October 2008. The export duty subsequently decreased substantially due to the decrease in global crude oil prices. As at 1 August 2010, the Russian oil export duty was U.S.\$263.8 per tonne. Any future increases could adversely affect the Ukrainian economy.

In February 1998, Ukraine and Russia signed a programme on economic co-operation for 1998 to 2007 and, in June 2007, a programme on economic co-operation for 2008 to 2010. These programmes remain the basis for trade relations between the two states. Between 1999 and 2004, Ukraine's exports of certain products, such as steel, pipes and confectionery items, have been adversely affected by measures taken by the Russian government to limit the export of such products to Russia, including the imposition of antidumping duties and quotas. Although some of these measures have been cancelled, Ukrainian exporters still experience certain difficulties in promoting their goods on the Russian market.

As of 21 August 2010, one anti-dumping investigation (relating to Ukrainian steel rollers) and three special investigations (relating to Ukrainian mechanical fixtures, hard boiling confectionery and absorbent carbon) were underway in Russia. As of that date, Russia has been applying restrictive measures in relation to exports from Ukraine as a result of three anti-dumping investigations (on small- and medium-diameter pipes, polyamide technical fibre and mechanical fixtures) and two special investigations (non-corrosive pipes and glass grid). In addition, at the beginning of 2006, Russia banned imports of meat and milk products from Ukraine due to alleged non-compliance with Russian sanitary standards. Russia lifted this ban with effect from 1 July 2010. However, only Ukrainian companies that have been certified by the relevant Russian

authorities may export meat and dairy products to Russia. Against the global economic background as well as developments in Russia-Ukraine political and trade relations, exports to Russia increased by 46.4 per cent. in 2007, and by 24.2 per cent. (from U.S.\$12.7 billion to U.S.\$15.7 billion) in 2008 but decreased by 46.1 per cent. in 2009 (from U.S.\$15.7 billion to U.S.\$8.5 billion). The volume of exports was U.S.\$5.7 billion in the six months ended 30 June 2010, an increase by 65.4 per cent. as compared to the corresponding period of 2009.

On 9 May 2005, the Presidents of Ukraine and Russia signed a declaration creating a Ukrainian-Russian Interstate Commission, with a committee on economic co-operation headed by the two Prime Ministers, subcommittees for defence, international co-operation and humanitarian co-operation, and a subcommission for issues of Russia's Black Sea Fleet stationing in Ukraine. More generally, high level discussions between Ukraine and Russia continue on an ongoing basis, including periodic meetings between the presidents and prime ministers of the two nations, the frequency of which intensified starting from March 2010. A broad spectrum of economic issues was discussed during recent meetings of the Ukrainian-Russian Interstate Commission, the committee on economic co-operation and other top level meetings, including issues related to the implementation of projects in such key spheres of cooperation as fuel and energy, the aircraft and space industries, shipbuilding and machinery manufacturing industry, transport, nuclear energy, advanced technologies and agriculture. A number of bilateral documents were signed during the third meeting of the Ukrainian-Russian Interstate Commission that was held in May 2010, including, amongst others, agreements on cooperation in the use and development of a global navigation satellite system and scientific and educational cooperation. In addition, six meetings of the committee on economic co-operation were held since its creation, the last one taking place in April 2010. The Government believes that the results of the last meeting of the committee on economic co-operation evidence the transition to a new stage in Ukrainian-Russian cooperation based on the comprehensive modernisation of trade and economic relations, deepening of integration processes and implementation of the innovation and investment grounds of the bilateral cooperation in the economic sphere.

Romania

On 2 June 1997, Ukraine concluded a friendship and co-operation treaty with Romania in which both sides agreed to recognise their existing borders. On 17 June 2003, Ukraine and Romania signed a treaty in relation to co-operation and mutual assistance in border matters, which came into effect on 28 May 2004. The treaty confirmed the official state border between Ukraine and Romania. Also in 2004, the agreement between the Cabinet of Ministries of Ukraine and the Government of Romania on cross-border movement of persons became effective. The agreement liberalised visa procedures for residents of Ukraine and Romania and abolished visa requirements for certain visitors.

The two countries were involved in a dispute over the continental shelf surrounding Zmiyinyi Island in the Black Sea, which is thought to hold sizeable crude oil and natural gas reserves. In September 2004, Romania asked the UN International Court of Justice ("ICJ") to delineate its Black Sea maritime border with Ukraine, including the continental shelf and exclusive economic zones. The decision of the ICJ, which is final and binding upon the states, was issued on 3 February 2009. The approach used by the ICJ for establishing the maritime boundary delineating the continental shelf and exclusive economic zones of Romania and Ukraine was not based on the grounds submitted by either of the two states. The delimitation sector with its area of 75,200 square km was divided with the ratio of 2.1 to 1 in favour of Ukraine, which left Ukraine with all explored oil fields and the majority of the explored gas fields located in the delimitation sector. The ICJ decision has settled one of the most complex issues on the Ukraine-Romania agenda and is expected to have a positive effect on relations between Romania and Ukraine and contribute to the promotion of investments in Black Sea oil and gas exploration and production ventures.

Relations between the two nations have also been strained by a dispute over Ukraine's restoration of the Danube-Black Sea deep-water vessel passage. From 1990s, this passage, in the Ukrainian sector of the Danube delta, had become silted up and was no longer navigable. In 2004, Romania requested that the Secretariat of the Convention on Environmental Impact Assessment in a Transboundary Context, or Espoo Convention, establish an inquiry commission to consider the project's cross-border environmental impact, which in 2006 concluded that the project would likely have a significant environmental impact. Ukraine

carried out dredging operations to make safe navigation of its Danube-Black Sea passage possible once more, and navigation recommenced in April 2007. In May 2008, the parties to the Espoo Convention approved the inquiry commission's conclusions and urged Ukraine to suspend its December 2007 final decision on implementation of the project and to refrain from carrying out the second phase of the project unless in full compliance with the Convention's provisions. In 2008, Ukraine withdrew its decision on implementation of the second stage of the project pending full compliance with provisions of the Espoo Convention. In January 2010, Ukraine completed performance of the Espoo Convention procedures, reapproved the decision on implementation of the second stage of the project and sent such decision to Romania and the Espoo Convention Implementation Committee. It is expected that in 2011 the parties to the Espoo Convention will perform a final assessment of Ukraine's compliance with the provisions of the Espoo Convention.

In addition, in March 2009, Ukraine addressed the Espoo Convention Implementation Committee with a request to consider possible adverse environmental impact of Romania's business activity in the Danube delta. In February 2010, the Committee concluded that Romania did not violate the Espoo Convention and did not carry out activities that would result in the degradation of the Ukrainian part of the Danube Delta. It is expected that the Committee's conclusion will be considered and finalised at the next meeting of the parties to the Espoo Convention in 2011.

Moldova

On 3 June 1997, Ukraine and Romania signed a trilateral agreement with Moldova to settle long-standing border disputes. The three countries also agreed to co-operate on legislation in accordance with EU norms and to act to promote trade by approving the creation of a free economic zone spanning the three states. Ukraine has worked consistently for settlement of the Transdnister dispute. In April 2005, then President Yushchenko proposed a plan for strengthening democracy in the Transdnister. This plan was supported by the parties to the dispute and by Russia and the OSCE Mission, which together with Ukraine are co-mediators in the negotiation process. In 2007, Ukraine as a co-mediator took part in several rounds of consultations, which resulted in settlement of a number of disputed issues between Moldova and Transdnister.

In addition, the leadership of the EU established the EU Border Assistance Mission to Moldova and Ukraine at the joint request of the Presidents of Ukraine and Moldova. The Border Assistance Mission aims to assist the two states in creating a system of border and customs controls and border surveillance that meets European standards. On 20 May 2009, the Cabinet of Ministers of Ukraine resolved to extend the mandate of the mission for another two years. Work on the demarcation of the Ukraine-Moldova border is in progress.

Due to the large number of Ukrainians living in Moldova, Ukraine views bilateral relations with Moldova as important. Although a number of unresolved ownership, demarcation, energy and environmental issues in bilateral relations between Ukraine and Moldova were identified in the Schedule for the Settlement of Top Priority Issues of Ukrainian-Moldovan Relations signed on 1 February 2008, such Schedule had not been fully implemented in 2008 and 2009.

In 2006-2008, interstate and inter-governmental ties between Ukraine and Moldova intensified. Ukraine became Moldova's main trading partner with a trade of goods turnover of U.S.\$1.34 billion in 2008, a U.S.\$262.1 million increase compared to 2007, and U.S.\$745.6 million in 2009, a decrease of U.S.\$596.0 million as compared to 2008 against the background of the global economic downturn. In the six months ended 30 June 2010, the trade of goods turnover between Ukraine and Moldova amounted to U.S.\$355.2 million, an increase of U.S.\$26.7 million compared to the corresponding period of 2009.

ECONOMY OF UKRAINE

Unless otherwise stated, the statistical information presented in this section has been derived from reports published by, or information obtained from, the Ministry of Finance of Ukraine.

Background

Prior to commencing the transition to a market economy, Ukraine had a centrally planned economy that was geared towards Russia and the other countries in the CIS. Although considerable progress has been achieved in the transition to a market economy in the realm of economic liberalisation, privatisation and financial stabilisation policies, the process remains incomplete in many substantial respects.

The Ukrainian economy grew at an annual average of approximately 7 per cent. in real GDP terms from 2000 until 2008, driven mainly by a rapid increase in foreign demand, rising commodity prices on external markets and the availability of foreign financing. Although these factors have positively affected the pace of Ukrainian economic growth in recent years, they have also increased the economy's vulnerability to external shocks. As a result, when the global economic and financial situation began to deteriorate, Ukraine's economy was one of the most severely affected. In 2009, Ukraine's real GDP decreased by 15.1 per cent. The real GDP growth started to recover in 2010 reaching, according to preliminary estimates, 4.9 per cent. in the first quarter of 2010 and 5.9 per cent. in the second quarter of 2010, respectively. The negative influence of external factors has been compounded by weaknesses in the Ukrainian economy. In particular, although various Governments have generally been committed to economic reform, lack of political consensus and controversies surrounding such issues as privatisation, subsidies to state-owned enterprises and co-operation with international financial institutions have impeded reform. Delays in implementing reforms, together with deteriorating conditions in the social sphere associated with substantial declines in income and high unemployment, have exerted considerable pressure on limited state resources. The structural weaknesses in the economy that have not yet been corrected are likely to restrain economic growth and continue to impose substantial fiscal pressures on the Government over the coming years.

Action Programmes

In May 2010, the Parliament approved the Law of Ukraine "On the State Programme for Economic and Social Development of Ukraine for 2010" (the "2010 Programme"). The 2010 Programme priorities include restoring economic growth and laying out an investment foundation for stable growth of the economy and improvement of the population welfare. The priorities set forth by the 2010 Programme also include, among other things, the following:

- macro-economic stabilisation, encouragement of entrepreneurship development;
- minimisation of negative social consequences of the financial crisis and creating conditions for post-crisis development, including rehabilitation of the public finance system and banking system;
- enhancement of efficiency of governmental agencies' activities;
- mitigation of regional imbalances;
- implementation of reforms targeted at the European and Euro-Atlantic integration of Ukraine;
- technological development and competitive growth of the domestic manufacturing sector, implementation of energy-saving measures;
- ensuring energy security of Ukraine;
- optimisation of the fiscal burden on the economy; and
- development of a highly efficient agro-industrial complex.

Furthermore, in June 2010, the Reform Committee presented for public comment the Economic Reform Programme. The Economic Reform Programme provides for a wide range of reforms in all sectors of national economy, while focusing on the following five main directions:

- creation of preconditions for the economic growth through maintaining low level of inflation, stabilisation of public finance system and creation of a stable financial system;
- establishment of the most favourable treatment regime for business through reducing the role of the State in the economy, lowering administrative barriers for business development, modernising the tax system and strengthening Ukraine's international economic integration;
- modernisation of infrastructure and main sectors of economy through eliminating structural problems in power generation, coal, oil and gas sectors, housing and communal services, transport and land market;
- preservation and development of social and human capital through increase of efficiency and stability of social protection, improvement of quality and availability of education and medical service; and
- increased efficiency of public management through reform of civil service and executive authorities system.

The Economic Reform Programme establishes three stages for the implementation of reforms: the first stage should be completed by the end of 2010, the second stage should be completed by the end of 2012, while the third stage should be completed by the end of 2014. For instance, to achieve the targets of business climate improvement and increase of investment inflows, the Economic Reform Programme provides for, among other things, a narrowing down, by 30 per cent., of the list of activities that are subject to licensing, and a significant reduction in the number of activities that require obtaining various approvals or certification, such steps to be taken by the end of 2010; it also provides that by the end of 2014 the EU technical standards must be implemented, customs procedures should be simplified and certain inspection authorities should be liquidated. For discussion of reforms in other sectors, as contemplated by the Economic Reform Programme, see *“Political Framework – International Relations”*, *“– Mining”*, *“– Oil and Gas”*, *“– Electricity Generation and Nuclear Power”*, *“– Agriculture”*, *“– Transport and Communications”*, *“– Privatisation”*, *“Labour Market – Pension, Unemployment Benefits and Social Insurance”*, *“Public Finance – Revenues”*, *“Public Finance – Central-Local Fiscal Relationship”* and *“Banking System and Securities and Financial Services Markets in Ukraine – Recent Developments in the Banking Sector”*.

Gross Domestic Product

According to official statistics, real GDP fell by an aggregate of 50.4 per cent. from 1992 to 1999. The main reasons for this decline were the breakdown of intra-CIS trade coupled with slow progress in finding new markets, the impact of energy prices that more closely reflected world levels (compared to the previous level of approximately one-third of world prices), the slow emergence of market structures, failure to impose tight budgetary constraints, a significant fall in domestic demand and, since 1995, high real interest rates. Economic growth began in 2000 and from 2000 to 2008, real GDP grew by an aggregate of 81.8 per cent., which was followed by a 15.1 per cent. decline in GDP recorded in 2009.

In 2007, Ukraine's real GDP increased by 7.9 per cent., industrial production increased by 7.6 per cent. and agricultural output declined by 6.5 per cent. Decline in agricultural production in 2007 resulted from a 9.5 per cent. decline in crop production due to unfavourable weather conditions between April and June 2007, including a severe drought in the central, eastern and southern regions of Ukraine. The real GDP growth in 2007 was a result of increases in gross added value in almost all sectors of economic activity, with the exception of agriculture, where gross added value declined by 6.0 per cent. In 2007, in the service industries, such as wholesale and retail trade and the transport and communications sector, gross added value increased by 15.8 per cent. and 9.3 per cent., respectively, as compared to 2006. Gross added value in the extractive industries, construction and manufacturing increased by 2.0 per cent., 14.1 per cent. and 10.1 per cent., respectively, in 2007 as compared to 2006; the 10.1 per cent. growth in gross added value in the manufacturing industry was mainly a result of the growth in machinery manufacturing, metallurgy and metal processing. The

real growth rates in 2007 reflect improvement in the external conditions affecting Ukraine's exports (in particular, metallurgy, chemical and machinery exports), high growth rates in real income of the population resulting in rapid growth of the consumer demand, as well as high growth rates in capital investments.

In 2008, Ukraine's real GDP increased by 2.3 per cent., industrial production decreased by 5.2 per cent. and agricultural output increased by 17.1 per cent. The decline in industrial production in 2008 and the more modest rate of real GDP growth for the full year 2008 as compared to the 5.8 per cent. growth recorded in the first quarter of 2008 are largely attributable to a 26.3 per cent. decline in industrial production in the fourth quarter of 2008 resulting from external shocks. In particular, starting from the end of the third quarter of 2008, a decrease in production was recorded in export-oriented industries and industries that are dependent on borrowings due to the global economic downturn and reduced external demand. At the same time, positive growth dynamics were recorded in industries oriented on the domestic market. In particular, in 2008, in the service industries, such as wholesale and retail trade and the transport and communications sector, gross added value increased by 2.4 per cent. and 9.6 per cent., respectively, as compared to 2007. In 2008, compared to 2007, gross added value in agriculture, hunting and forestry increased by 16.6 per cent., while gross added value in construction, education, and health and social protection decreased by 29.1 per cent., 0.5 per cent., and 1.0 per cent., respectively.

In 2009, Ukraine's real GDP decreased by 15.1 per cent., industrial production decreased by 21.9 per cent. and agricultural output decreased by 1.8 per cent. The decline in GDP in 2009 was a result of unfavourable external conditions, including both reduced external demand and low export prices, decreased domestic demand and limited volumes of available financing due to the global financial downturn. However, Ukraine's economy was gradually adjusting to external shocks caused by the global economic and financial downturn. As a result, in 2009, cumulative rates of decline in GDP decelerated throughout the year. In particular, in the second quarter of 2009, the rate of decline in real GDP compared to the second quarter of 2008 (17.8 per cent.) decelerated as compared to the decline recorded in the first quarter of 2009 compared to the first quarter of 2008 (20.2 per cent.). In the third quarter of 2009, the rate of decline in real GDP compared to the third quarter of 2008 was 16.0 per cent., and the rate of decline in real GDP further decelerated in the fourth quarter of 2009 compared to the fourth quarter of 2008 (6.8 per cent.). The largest declines in gross added value were recorded in machinery manufacturing (44.9 per cent.), production of other non-metallic mineral products (38.5 per cent.), metallurgy (26.7 per cent.) and construction (48.2 per cent.). In addition, in 2009, gross added value in agriculture, trade and transport and the communications sector declined by 0.3 per cent., 15.7 per cent. and 9.1 per cent., respectively.

According to the preliminary data, during the first quarter of 2010, Ukraine's real GDP increased by 4.9 per cent. compared to a 20.2 per cent. decline in the first quarter of 2009, and during the second quarter of 2010, real GDP increased by 5.9 per cent. compared to 17.8 per cent. decline in the second quarter of 2009. The Government expects that for the full year 2010 Ukraine's real GDP will increase by 3.7 per cent. and that for 2011 Ukraine's real GDP will increase by 4.5 per cent.

The following table sets forth certain information about Ukraine's GDP for the periods indicated:

	Year ended 31 December			31 March	
	2007	2008	2009	2009	2010
GDP					
Nominal GDP (UAH millions)	720,731.0	948,056.0	914,720.0	188,037.0	218,125.0
Nominal GDP (U.S.\$ millions) ⁽¹⁾	142,719.0	179,896.8	117,422.3	24,420.4	27,299.7
Real GDP (% change) ⁽²⁾	7.9	2.3	(15.1)	(20.2)	4.9
Nominal per capita GDP (U.S.\$) ⁽¹⁾	3,071.5	3,889.0	2,549.7	N/A ⁽³⁾	N/A ⁽³⁾

Notes:

- (1) Hryvnia amounts have been converted to dollar amounts using the average exchange rate specified under the heading "The Monetary System – Exchange Rates".
- (2) The State Committee of Statistics calculates real GDP for a particular period by dividing nominal GDP (UAH millions) for such period by the relevant consumer price index.
- (3) As full-year nominal GDP is not yet available, this figure does not offer a meaningful comparison with nominal per capita GDP for prior years.

Source: State Committee of Statistics

GDP by Source

Before its independence in 1991, Ukraine's economy was highly integrated into the economic system of the former Soviet Union. Ukraine imported oil and gas from Russia, Azerbaijan and Turkmenistan, and exported steel, machinery, chemical, agricultural and other products to other Republics within the former Soviet Union. Since independence, the composition of GDP has undergone a period of restructuring and adjustment.

The following tables set forth the composition of GDP by source for the periods indicated:

	Year ended 31 December						1st quarter	
	2007		2008		2009		2010	
	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)
GDP ⁽¹⁾	720,731.0	100.0	948,056.0	100.0	914,720.0	100.0	218,125.0	100.0
Industry ⁽²⁾	198,368.0	27.6	247,872.0	26.1	211,992.0	23.2	56,057.0	25.7
Agriculture, hunting and forestry	47,417.0	6.6	65,148.0	6.9	65,517.0	7.2	6,253.0	2.9
Construction	30,456.0	4.2	29,185.0	3.1	22,110.0	2.4	4,461.0	2.0
Transport and communication	70,063.0	9.7	87,078.0	9.2	103,527.0	11.3	28,095.0	12.9
Trade and services	95,220.0	13.3	131,261.0	13.9	123,115.0	13.5	29,056.0	13.3
Other economic activity ⁽³⁾	215,368.0	29.8	300,170.0	31.7	321,591.0	35.1	75,681.0	34.7
Services of financial agents	(22,098.0)	(3.1)	(36,538.0)	(3.9)	(50,849.0)	(5.6)	(10,987.0)	(5.0)
Taxes other than product subsidies ..	85,937.0	11.9	123,880.0	13.0	117,717.0	12.9	29,509.0	13.5

Notes:

- (1) Totals may not add up to GDP figures in the table above because of statistical discrepancies.
- (2) Consists of extractive industries (such as mining), manufacturing and energy, gas and water production and distribution.
- (3) Includes education, health protection and other segments of the economy.

Source: State Committee of Statistics

2009

	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter	
	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)
GDP ⁽¹⁾	188,037.0	100.0	213,690.0	100.0	251,263.0	100.0	261,730.0	100.0
Industry ⁽²⁾	46,061.0	24.5	52,250.0	24.4	54,627.0	21.7	59,054.0	22.6
Agriculture, hunting and forestry	5,084.0	2.7	8,998.0	4.2	35,719.0	14.2	15,716.0	6.0
Construction	4,019.0	2.1	5,564.0	2.6	5,852.0	2.3	6,675.0	2.6
Transport and communication	22,475.0	12.0	24,117.0	11.3	26,506.0	10.5	30,429.0	11.6
Trade and services	27,012.0	14.4	29,216.0	13.7	32,459.0	12.9	34,428.0	13.2
Other economic activity ⁽³⁾	68,468.0	36.4	80,673.0	37.8	83,860.0	33.5	88,590.0	33.8
Services of financial agents.....	(13,845.0)	(7.4)	(12,401.0)	(5.8)	(12,891.0)	(5.1)	(11,712.0)	(4.5)
Taxes other than product subsidies ..	28,763.0	15.3	25,273.0	11.8	25,131.0	10.0	38,550.0	14.7

Notes:

- (1) Totals may not add up to GDP figures in the table above because of statistical discrepancies.
(2) Consists of extractive industries (such as mining), manufacturing and energy, gas and water production and distribution.
(3) Includes education, health protection and other segments of the economy.

Source: State Committee of Statistics

GDP by Use

The following tables set forth the composition of GDP by use for the periods indicated:

	Year ended 31 December						1st quarter	
	2007		2008		2009		2010	
	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)
GDP ⁽¹⁾	720,731.0	100.0	948,056.0	100.0	914,720.0	100.0	218,125.0	100.0
Consumption	558,581.0	77.5	758,902.0	80.1	774,075.0	84.6	194,049.0	89.0
Private Sector.....	423,174.0	58.7	582,482.0	61.4	590,196.0	64.5	148,068.0	67.9
Non-profit organisations	6,445.0	0.9	7,257.0	0.8	8,502.0	0.9	2,206.0	1.0
Government	128,962.0	17.9	169,163.0	17.9	175,377.0	19.2	43,775.0	20.1
Gross fixed investment	198,348.0	27.5	250,158.0	26.4	164,522.0	18.0	33,631.0	15.4
Change in stock	4,685.0	0.7	14,379.0	1.5	(8,491.0)	(0.9)	(5,744.0)	(2.6)
Net acquisition of valuables	285.0	0.0	346.0	0.0	449.0	0.0	103.0	0.0
Resource balance (net export GNFS) ⁽²⁾	(41,168.0)	(5.7)	(75,729.0)	(8.0)	(15,835.0)	(1.7)	(3,914.0)	(1.8)
Export of goods and NFS ⁽³⁾	323,205.0	44.8	444,859.0	46.9	423,565.0	46.3	110,236.0	50.5
Import of goods and NFS ⁽³⁾	364,373.0	50.5	520,588.0	54.9	439,400.0	48.0	114,150.0	52.3

Notes:

- (1) Totals may not add up to GDP figures in the table above because of statistical discrepancies.
(2) GNFS means "goods and non-factor services".
(3) NFS means "non-factor services".

Source: State Committee of Statistics

Inflation

The following table sets forth certain consumer price index and wholesale price index information, as percentage change rates as at the end of the period, as compared to end of the previous year:

	Year ended 31 December					Seven months ended 31 July	
	2005	2006	2007	2008 ⁽¹⁾	2009 ⁽¹⁾	2009 ⁽¹⁾	2010 ⁽¹⁾
	<i>(Increase (decrease) against end of previous year in %)</i>						
Consumer Price Index (CPI)	10.3	11.6	16.6	22.3	12.3	8.5	3.1
Food	10.7	3.5	22.9	24.5	10.9	7.6	4.4
Non-Food	4.0	2.5	6.0	N/A	N/A	N/A	N/A
Paid Services	15.8	49.4	12.0	N/A	N/A	N/A	N/A
Wholesale Price Index (WPI)	9.5	14.1	23.3	23.0	14.3	4.9	14.1

Notes:

(1) Beginning in 2008, the State Committee of Statistics uses international COICOP classification and does not calculate non-food and paid services indices. Also beginning in 2008, food index does not include alcoholic beverages and tobacco.

Source: State Committee of Statistics

At year-end 2007, against year-end 2006, Ukraine had 16.6 per cent. inflation, measured by CPI. In the summer of that year, inflation accelerated significantly due to unfavourable weather conditions resulting in a low harvest, political uncertainties resulting in increased consumer inflation expectations, continued global inflation, an increase of consumer purchasing capacity and an increase in the monetary base and money held outside banks. While the main reason for CPI inflation in 2006 was the growth in prices for services, in 2007, an increase in food prices accounted for approximately 80 per cent. of CPI growth. At the same time, factors mitigating the inflation pressure included a growth of retail deposit volumes, exchange rate stability and various measures taken by the Government and the NBU to restrain inflation rates. The CPI inflation in the fourth quarter of 2007 was the highest among quarterly indices from 2000. In 2007, consumer price inflation was 12.8 per cent. as compared to 2006. At year-end 2007, against year-end 2006, Ukraine had 23.3 per cent. inflation as measured by WPI, which was mainly the result of an increase in natural gas prices for industrial consumers, domestic wholesale agricultural product prices and world prices for metal products, grain and oil, as well as a result of increased wages and an intensification of the industrial modernisation.

At year-end 2008, against year-end 2007, Ukraine had 22.3 per cent. inflation as measured by CPI. At 14.6 per cent., CPI growth rates (against year-end 2007) were higher in the five months ended 31 May 2008 than in the subsequent seven months of that year. The reasons for the acceleration of CPI inflation in the five months ended 31 May 2008 included the continuing effects of the high inflation rate during the last quarter of 2007 during the first five months of 2008, increasing prices for agricultural production resulting from the agricultural output decline in 2007 as well as from increasing prices for such products in external markets, and an increase in natural gas and oil prices. In June-August 2008, however, the inflation rate decelerated, and in July-August deflation was recorded, for the first time since April 2006. In September-December 2008, the rate of inflation increased again, largely due to increased non-food prices and prices for municipal services against the background of the global financial downturn. In this period, increased prices for non-food products were largely caused by a significant devaluation of hryvnia against foreign currencies. For the full year, the highest levels of inflation were recorded in food products (24.5 per cent.), which included 34.0 per cent., 27.8 per cent., and 37.8 per cent. growth in prices for meat and meat products, bread and bakery products, and fruits, respectively. In 2008, consumer price inflation was 25.2 per cent. as compared to 2007. At year-end 2008, against year-end 2007, Ukraine had 23.0 per cent. inflation as measured by WPI, which was mainly the result of an increase in natural gas prices for industrial consumers, domestic wholesale agricultural product prices and world prices for metal products, grain and oil, as well as a result of increased wages and intensification of industrial modernisation.

In response to the high inflation levels recorded in the fourth quarter of 2007 and first quarter of 2008, the Government, together with the NBU, developed the Plan of Anti-Inflationary Measures (the “Plan”) that called for joint and coordinated activities aimed at the prevention of the growth of the inflationary pressure on the economy. In January 2009, the Plan was extended to 2009 as well. In accordance with the Plan, during 2008 and 2009, anti-inflationary measures focused on four areas:

- reducing the level of demand inflation by means of monetary and fiscal measures;
- preventing unreasonable price increases for certain goods and services, unfair competition and abuses of monopoly positions;
- increasing the efficiency of accumulation and investment of idle funds, including the development of the stock market and the financial markets; and
- reducing energy consumption and the dependency of the Ukrainian economy on external energy prices.

In accordance with the Plan, in 2008, a number of memoranda (most of which imposed price controls) were entered into with agricultural producers and wholesale traders in order to prevent unjustified increases in wholesale and retail prices for products of social importance, for example, sugar and meat. The NBU was also pursuing tighter monetary policy aimed at reducing inflationary pressure on the economy. See “*Monetary System*”.

At year-end 2009, against year-end 2008, Ukraine had 12.3 per cent. inflation as measured by CPI. In 2009, consumer price inflation was 15.9 per cent. as compared to 2008. After acceleration of CPI inflation in 2008, inflation growth decelerated in 2009 due to good harvest recorded in 2008-2009, reduced wholesale prices for agricultural products, renewal of retail deposits growth, reduced consumer lending, reduced volumes of cash in circulation and money supply and continued implementation of anti-inflation measures by the Government and the NBU. The reasons for deceleration of CPI inflation in this period also include increased unemployment, reduced wages and restrictions on deposit withdrawals introduced by the NBU in the end of 2008. Factors adversely affecting CPI inflation in 2009 included rising fuel prices, which increased by 46.0 per cent. against year-end 2008, against the background of global oil price growth, a significant increase of oil export duty by Russia and an increase in the consolidated budget deficit. Factors adversely affecting CPI inflation in 2009 also included hryvnia devaluation against U.S. dollar, high inflation expectations in the population, rising prices for tobacco, alcohol and sugar and prices (tariffs) for certain other goods that remain subject to national price regulation, as well as growing processed food manufacturers prices. The 12.3 per cent. inflation in 2009, against year-end 2008, included 10.9 per cent. inflation in food products, 8.2 per cent. inflation in prices for housing, water, electricity and fuel for housing and 19.2 per cent. inflation in transport. The rate of consumer price inflation is particularly influenced by the prices of grain, milk and meat, as food products accounted for approximately 53.3 per cent. of the consumer basket in 2009; however, the share of non-food products and paid services in the consumer basket has been increasing over the years as a result of the growth in household income.

In 2009 against year-end 2008, WPI inflation was 14.3 per cent. as compared to 23.0 per cent. in 2008 against year-end 2007. 14.3 per cent. WPI inflation in 2009 included 17.2 per cent., 42.9 per cent. and 20.3 per cent. WPI inflation in metallurgy industry, coke and oil-refining industry and food, drinks and tobacco production, respectively. WPI inflation was 6.5 per cent. in 2009 compared to 2008, and was 35.5 per cent. in 2008 compared to 2007. The deceleration in the rate of growth of wholesale prices in 2009 was mainly due to a decrease in world prices for primary export products, the low level of economic activity in the domestic market and deceleration in the growth rate of wages in this period. Factors adversely affecting WPI inflation in 2009 included increased threshold prices for natural gas for industrial consumers, hryvnia devaluation against U.S. dollar and increased global oil prices.

For the seven months ended 31 July 2010 against year-end 2009, the CPI inflation rate was 3.1 per cent. compared to a rate of 8.5 per cent. during the corresponding period of 2009 against year-end 2008. The CPI rate was 9.3 per cent. in the seven months ended 31 July 2010 compared to the corresponding period in 2009, while in the seven months ended 31 July 2009, CPI inflation was 17.3 per cent. compared to the

corresponding period of 2008. The reasons for deceleration of CPI inflation in the seven months ended 31 July 2010 as compared to the same period in 2009 include relative stabilisation of the hryvnia exchange rate, a good harvest recorded in 2008-2009, increased supply of agricultural production and a moderate increase in the purchasing power of the population, due to continued reductions in consumer lending against the background of the growth in real wages, and renewal of retail deposits growth. Factors adversely affecting CPI inflation in the seven months ended 31 July 2010 include rising global and/or domestic prices on certain food products, in particular, sugar, vegetables and fruits and rising domestic fuel prices due to high oil prices at the global market. The 3.1 per cent. inflation in the seven months ended 31 July 2010 against year-end 2009 included 4.4 per cent. inflation in food products, 2.4 per cent. inflation in prices for housing, water, electricity and fuel for housing and 4.3 per cent. inflation in transport.

During the seven months ended 31 July 2010 against year-end 2009, WPI inflation was 14.1 per cent. as compared to 4.9 per cent. in the corresponding period of 2009 against year-end 2008. WPI inflation was 21.6 per cent. in the seven months ended 31 July 2010 compared to the corresponding period in 2009, and was 7.2 per cent. in the seven months ended 31 July 2009 compared to the corresponding period in 2008. The WPI inflation rate accelerated in the seven months ended 31 July 2010 as compared to the corresponding period of 2009 due to a significant increase in global metal and fuel prices and an increased external demand for such products during the period starting from January to the first half of April 2010, as well as an increase in prices (tariffs) in energy, gas and water production and distribution (by 21.1 per cent. in the seven months ended 31 July 2010). Factors positively affecting WPI inflation in the seven months ended 31 July 2010 include maintenance in January-April 2010 of threshold prices for natural gas for industrial consumers at the 2009 level and their minor decrease in May-July 2010, and hryvnia revaluation against U.S. dollar.

In 2010, the Government expects the CPI inflation rate to be 12.0 per cent. against year-end 2009. Consumer price dynamics in the second half of 2010 are expected to be largely influenced by non-monetary factors, such as an increase in natural gas prices for population and municipal heating enterprises by 50.0 per cent. effective 1 August 2010, an increase in housing prices (tariffs) and levelling of supply and demand in commodity markets. The factors positively influencing consumer price dynamics in 2010 include renewal of retail deposits growth, stabilisation of foreign exchange rates and reduced inflation expectations of the population. In 2010, the Government expects the WPI inflation rate to be 18.5 per cent. against year-end 2009. The wholesale price dynamics in 2010 is expected to be largely influenced by growing external prices for main export products, rising oil prices and increased expenditures on transportation and wages.

The Government and the NBU will continue to pursue a policy aimed at restraining inflation growth by way of hryvnia exchange rate stabilisation, mitigation of commodity markets imbalances and control over the growth of the monetary aggregates. In addition, the Government will continue to pursue a policy aimed at development of the domestic stock market and financial instruments necessary for the efficient distribution of temporarily idle funds for investment activities and the economy modernisation, prevention of economically unsubstantiated increases in prices and abuses of the monopoly position at certain markets, as well as a policy aimed at improvement in the energy efficiency and reduced dependence of the Ukrainian economy on the conditions at the external energy markets. In 2010, the Government developed a plan of measures aimed at stabilisation of prices at the consumer markets for 2010, which contemplates, among other things, an improvement of the legislative framework on pricing and price control issues, creation of independent authorities to regulate pricing in the housing and transport spheres, introduction of market pricing mechanisms for fuel and energy products and related services, mitigation of food markets imbalances and improvement of the mechanisms of the state support for agricultural producers.

Further inflationary pressure in 2010 may be caused by, among other things, an increase in the consolidated budget deficit, an increase in global prices for fuel and raw materials, grain and certain other food products, as well as an increase in tariffs for municipal services up to economically reasonable levels. For the purposes of municipal services, electricity charges, gas supplied by Naftogas and similar functions, Ukraine deems an economically reasonable price to be one that covers the cost of inputs as well as certain financing and other costs of the provider.

Price Liberalisation

From 1991 to date, Ukraine has taken steps towards liberalising prices to ameliorate misallocation of resources. Starting in 1993, state-determined prices for energy, agricultural products and communal services were gradually raised towards full cost recovery and global market prices. The majority of price-distorting practices were eliminated in October 1994.

Currently, the only goods that remain subject to national price regulation are gas, electricity, certain telecommunications, postal and transportation services and such housing and communal services as central heating, water, sewage and housing maintenance services, and certain agricultural products. Gas and electricity prices are regulated by an independent body, the National Commission on Electric Power Industry Regulation, while local authorities set tariffs on housing maintenance services and certain transportation services. In addition, local authorities may regulate prices of bread, crops, sugar, oil, meat, eggs and dairy products. Pursuant to a law that came into effect on 22 July 2010, powers to set tariffs for heating, water and sewage services were transferred to the National Commission for Regulation of Communal Services Market in Ukraine. The new Commission is to be established by 1 January 2011 and until its establishment, relevant tariffs are being set by the National Commission on Electric Power Industry Regulation.

In recent years, rates for municipal services, such as central heating, water, sewage and housing maintenance services, increased steadily, with such an increase being, depending on the type of services, in the range of 15 to 23 per cent. in 2007, 30 to 45 per cent. in 2008, 6 to 40 per cent. in 2009 and 3 to 5 per cent. for the seven months ended 31 July 2010. These increases reflect the general policy of gradually bringing such prices to economically reasonable levels. Household electricity tariffs were increased in nominal terms by 26.9 per cent. in 2000 (as a condition to the disbursement of IMF funds) and remained unchanged from that time until May 2006, when household electricity tariffs were increased by 25 per cent.; a further 25 per cent. increase followed in September 2006. From September 2006 to the present, household electricity tariffs have remained stable. See “— *Electricity and Natural Gas Tariffs*”.

Tariffs for public telecommunications services and access to the telecommunications networks of the operator with a dominant market position as well as for universal postal services are regulated by the National Commission for the Regulation of Communications. Tariffs for certain transportation services, including railway transportations services and specialised services of ports and airports, are regulated by the Ministry of Transport and Communications of Ukraine subject to the approval of the Ministry of Economy of Ukraine.

Principal Sectors of the Economy

Industry

Ukraine inherited a large heavy industrial sector from the Soviet era, especially in iron and steel, aerospace and transport aircraft and other military equipment. However, these sectors have been impeded historically by the lack of structural reform, increased energy costs and market downturns.

The table below shows percentage changes in the rates of industrial production for the years ended 31 December 2007 to 2009 and for the seven months ended 31 July 2009 and 2010 compared to the comparable period in the previous year:

	Year ended 31 December			Seven months ended 31 July	
	2007	2008	2009	2009	2010
	<i>(Increase (decrease) over comparable period of previous year, in %)</i>				
Total industry	7.6	(5.2)	(21.9)	(30.3)	11.1
<i>of which:</i>					
Extractive industry	2.6	(4.3)	(10.6)	(17.4)	5.1
Manufacturing (processing).....	9.9	(6.0)	(26.5)	(35.6)	13.0
<i>of which:</i>					
Food, drinks and tobacco industry	7.5	(2.1)	(6.0)	(6.2)	1.4
Light industry	(2.6)	(10.6)	(25.8)	(31.2)	5.9
Woodworking industry (other than furniture)	12.4	(2.4)	(24.6)	(35.3)	12.3
Pulp, paper and publishing industry ..	11.6	0.1	(18.7)	(22.3)	1.6
Coke and oil-refining industry.....	2.1	(13.4)	(3.4)	(13.6)	2.4
Chemical and petrochemical industry	8.4	(8.6)	(23.0)	(33.0)	20.8
Non-metallic industry	11.9	(2.8)	(38.5)	(46.3)	5.4
Metallurgy and metal products	7.0	(12.3)	(26.7)	(41.2)	14.8
Machinery manufacturing	19.0	0.3	(44.9)	(52.2)	31.3
Energy, gas and water production and distribution	2.3	(1.8)	(11.1)	(17.3)	11.3

Note:

The State Committee of Statistics calculates the index of industrial production on the basis of monthly production volumes through comparing two subsequent months (the indices of industrial production for the respective period are calculated on the basis of monthly indices during this period).

Source: State Committee of Statistics

Industrial production increased by 7.6 per cent. in 2007, but decreased by 5.2 per cent. in 2008 and by 21.9 per cent. in 2009. In 2009, industrial production decreased in all sectors, while the main industries contributing to the decline in 2009 were metallurgy, machinery manufacturing and the chemical industry, largely due to a reduced demand for these industries' products in external markets.

In the seven months ended 31 July 2010, industrial production increased by 11.1 per cent. compared to the same period in 2009. During this period, industrial production increased in all sectors of economic activities, including a 5.1 per cent., 13.0 per cent. and 11.3 per cent. growth in the extractive, manufacturing (processing) and energy, gas and water production and distribution industries, respectively. In particular, in the seven months ended 31 July 2010, industrial production increased in all sectors of the manufacturing (processing) industry; the growth in the industrial production was recorded both in the export-oriented industries such as metallurgy and the chemical industry and in the industries oriented at the domestic market such as light, food and woodworking industries. The main industries contributing to the growth in the seven months ended 31 July 2010 were machinery manufacturing, metallurgy and the chemical industry. Reasons for the Ukrainian economy's transition from the recession recorded in 2008 and 2009 to the growth in the seven months ended 31 July 2010 include both improved external conditions and a gradual improvement in the domestic market.

Production in the light industry sector decreased by 25.8 per cent. in 2009, including a 28.0 per cent. decline in the production of textiles, garments, fur and related products and a 15.9 per cent. decline in leather and footwear production. A decline in the production of garments, fur and related products as well as leather and footwear was due to oversaturation of the market with imported products, including those smuggled into the

country as, according to the data of the Ministry of Economy of Ukraine, approximately 90 per cent. of imported light industry products are imported into Ukraine at the understated customs value or are smuggled resulting in an unfair competition at the domestic market. In the seven months ended 31 July 2010, as compared to the same period in 2009, production in the light industry sector increased by 5.9 per cent. including a 6.6 per cent. increase in the production of textiles, garments, fur and related products and a 3.2 per cent. increase in the production of leather and related products.

In 2009, production in the woodworking industry decreased by 24.6 per cent. as compared to 2008. However, in the seven months ended 31 July 2010, the woodworking industry increased production by 12.3 per cent. In 2009, the pulp, paper and publishing industries experienced a decrease in production of 18.7 per cent. and in the seven months ended 31 July 2010, production in the pulp, paper and publishing industry increased by 1.6 per cent. In 2009, production in the non-metallic industry decreased by 38.5 per cent., and in the seven months ended 31 July 2010 it increased by 5.4 per cent., largely as a result of an increase in output of construction-related products, including concrete, plaster and cement products, glass and ceramic tiles.

The chemical and petrochemical industry decreased production by 23.0 per cent. in 2009, largely due to unfavourable conditions on external markets and a reduction in prices of mineral fertilisers. The 23.0 per cent. decline in 2009 included 22.7 per cent. and 23.7 per cent. declines in chemical production and rubber and plastic production, respectively. During 2009, a number of chemical enterprises (ammonia and nitrogen producers in particular) either stopped production completely or curtailed it significantly. These enterprises were loss-making in this period due to increased natural gas prices and their products failing to compete against cheaper imports from Russia and other CIS countries. However, in the seven months ended 31 July 2010 as compared to the same period in 2009, production in the chemical and petrochemical industry increased by 20.8 per cent. primarily due to an increased external demand and export prices, increased domestic demand for fertilisers, maintenance of threshold natural gas prices at the optimal level and a continued moratorium on increases in prices for services and tariffs of natural monopolies such as railways and electricity generation companies. Factors adversely affecting growth in the industry in this period include high level of the VAT refund arrears of the State Budget to chemical enterprises, low competitiveness of Ukrainian nitrogen fertilisers compared to Russian and Belorussian similar products as the natural gas prices for producers in these countries are lower, and low competitiveness of Ukrainian phosphate and composite fertilisers as Ukraine does not have its own deposits of raw materials needed to produce such fertilisers. The 20.8 per cent. growth in the seven months ended 31 July 2010 included growth in rubber and plastic production and chemical production by 9.5 per cent. and 24.4 per cent., respectively.

The metallurgy industry decreased production by 26.7 per cent. in 2009 against the background of unfavourable conditions on external markets, which included both reduced external demand and low export prices for such products, and a reduced domestic demand from the domestic machinery manufacturing and construction industries. The decline in 2009 included decreases of 31.6 per cent., 17.1 per cent. and 32.6 per cent. in the production of pipes, cast iron and steel, respectively. In the seven months ended 31 July 2010, the metallurgy industry increased production by 14.8 per cent. as compared to the same period in 2009, primarily due to an increased external demand and export prices, maintenance of threshold natural gas prices at the level of 2009 and a continued moratorium on increases in prices for services and tariffs of natural monopolies such as railways and electricity generation companies. The 14.8 per cent. growth in the seven months ended 31 July 2010 included 13.9 per cent. growth in cast iron, steel and ferroalloy production as well as 9.3 per cent. and 20.0 per cent. growth in pipe and finished metal products production, respectively.

The coke and oil refining industry decreased production by 3.4 per cent. in 2009. In the seven months ended 31 July 2010 as compared to the same period in 2009, the coke and oil refining industry increased production by 2.4 per cent. due primarily to a 8.8 per cent. growth in coke production.

The food industry decreased production by 6.0 per cent. in 2009. The decline in 2009 was a result of reduced domestic demand due to, among other things, reduced purchasing power of the population. The decline in 2009 was also a result of price growth, including fuel and energy price increases, reduction in the investment volumes and the available working capital, increased excise duties for tobacco and alcoholic beverages and increased imports. In particular, production of meat products, dairy products, tobacco and bread and bakery products decreased by 12.2 per cent., 9.2 per cent., 12.6 per cent. and 9.3 per cent., respectively. In the seven

months ended 31 July 2010, production in the food industry increased by 1.4 per cent. as compared to the same period in 2009. The 1.4 per cent. increase in the seven months ended 31 July 2010 as compared to the same period in 2009 included 10.3 per cent., 5.3 per cent., and 5.0 per cent. increases in oil and fat, confectionary and meat production, respectively. Such increases were offset to a certain extent by a decline in vegetables and fruit processing by 7.3 per cent., and tobacco, dairy products and drinks production by 5.5 per cent., 3.6 per cent. and 0.8 per cent., respectively.

In 2009, production in the machinery manufacturing industry decreased by 44.9 per cent., largely as a result of the reduced demand at the external and domestic markets, including due to the reduced consumer lending, and lack of available financing for domestic machinery manufacturing enterprises. In 2009, production of electric, electronic and optical equipment decreased by 28.2 per cent., machinery and equipment production decreased by 37.6 per cent. and transport vehicles and related equipment production decreased by 57.9 per cent. In the seven months ended 31 July 2010, production in the machinery manufacturing industry increased by 31.3 per cent. as compared to the same period in 2009. In the seven months ended 31 July 2010, production of electric, electronic and optical equipment increased by 12.4 per cent., machinery and equipment production increased by 19.4 per cent. and transport vehicles and related equipment production increased by 61.7 per cent. (including cargo vehicle and bus production growth by 2.2 times and 2.4 times), respectively, as compared to the same period in 2009.

In 2009, production in the extractive industry decreased by 10.6 per cent., but in the seven months ended 31 July 2010 production in this industry increased by 5.1 per cent. The 5.1 per cent. growth in the seven months ended 31 July 2010 was primarily a result of a growth in the extraction of sintered and non-sintered iron ores, which increased by 16.3 per cent. and 31.2 per cent., respectively. In 2009, energy, gas and water production and distribution decreased production by 11.1 per cent., but in the seven months ended 31 July 2010 production in this industry grew by 11.3 per cent. as compared to the same period in 2009.

The Government expects that for the full year 2010 industrial production will increase by at least 5.3 per cent. The positive dynamics of the industrial production will be primarily influenced by the growth in the production in the machinery manufacturing industry and metallurgy by 10 per cent. and 7 per cent., respectively, such growth due both to improved external conditions and an increased demand from domestic construction and other industries. In addition, a 2.5 per cent. increase in the food industry production for the full year 2010 is expected largely due to an increased domestic consumer demand as a result of an expected increase in household income as well as a growing external demand.

The table below summarises the volume of realised industrial production (goods and services sold) in each sector for 2007, 2008, 2009 and the seven months ended 31 July 2009 and 2010.

	Year ended 31 December						Seven months ended 31 July			
	2007		2008		2009 ⁽²⁾		2009 ⁽³⁾		2010 ⁽³⁾	
	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)	(UAH millions)	(%)
Total industry⁽¹⁾	717,076.7	100.0	917,035.5	100.0	806,345.8	100.0	353,290.1	100.0	476,203.7	100.0
<i>of which:</i>										
Extractive industry	56,348.6	7.9	85,755.4	9.3	67,284.2	8.4	32,076.0	9.1	54,079.4	11.3
Manufacturing (processing)	530,162.7	73.9	668,466.4	72.9	558,208.2	69.2	249,229.4	70.5	336,601.9	70.7
<i>of which:</i>										
Food, drinks and tobacco industry	109,959.9	15.3	139,892.4	15.2	159,506.5	19.8	68,281.8	19.3	78,509.6	16.5
Light industry	7,034.1	1.0	8,201.5	0.9	7,320.7	0.9	3,008.2	0.9	3,338.2	0.7
Woodworking industry (other than furniture) ..	5,796.4	0.8	6,786.6	0.7	6,236.4	0.8	2,502.7	0.7	2,989.4	0.6
Pulp, paper and publishing industry	16,788.0	2.4	20,539.3	2.2	21,486.7	2.6	8,373.6	2.4	9,841.8	2.1
Coke and oil-refining industry	52,527.7	7.3	66,135.2	7.2	53,931.1	6.7	25,578.8	7.2	40,334.7	8.5
Chemical and petro chemical industry	43,911.4	6.1	55,576.4	6.1	48,227.5	6.0	23,033.5	6.5	29,452.7	6.2
Non-metallic industry	27,464.5	3.8	34,314.6	3.8	24,176.4	3.0	11,739.8	3.3	12,877.4	2.7
Metallurgy and metal products	157,450.5	22.0	202,034.6	22.0	141,526.3	17.5	67,053.1	19.0	103,557.9	21.7
Machinery manufacturing	98,339.9	13.7	121,780.4	13.3	85,386.4	10.6	36,503.5	10.3	50,671.0	10.6
Energy, gas and water production and distribution.....	130,565.4	18.2	162,813.7	17.8	180,853.4	22.4	71,984.7	20.4	85,522.4	18.0

Notes:

- (1) Data includes small enterprises and takes into account sales volumes of enterprises' customers, i.e., figures include both volumes produced by manufacturing enterprises as well as sales volumes of manufactured products by customers that purchased the products from the initial manufacturers.
- (2) Data is based on uniform products which, using the classification of economic activities, relate to the relevant type of economic activities; data does not include changes by enterprises of their main type of economic activities.
- (3) Data does not include small enterprises and does not take into account sales volume of enterprises' customers, i.e., figures include only volumes produced by manufacturing enterprises and do not include sales volumes of manufactured products by customers that purchased the products from the initial manufacturers.

Source: State Committee of Statistics

State Aid and Industrial Development

To stimulate industrial growth, Parliament and the Government of Ukraine have enacted a number of legislative initiatives aimed at developing certain industrial sectors, including car production, ship-building, ammunition manufacturing, mining and processing of iron ore, airline manufacturing, the defence industry and alternative energy sources.

On 24 June 2004, the Law of Ukraine "On State Support of the Agriculture of Ukraine" was adopted, setting state policy in the budget, credit, pricing, insurance, regulatory and other spheres of Government in order to stimulate domestic agricultural production and develop the agricultural market. State support envisaged by the law includes state loans to certain types of agricultural producers, as well as insurance, credit and cattle breeding subsidies. Amendments to this law as well as the Law "On Milk and Dairy Products" enacted in November 2006 were intended to bring state support policy in line with WTO and EU requirements, including in relation to export and import operations with products whose prices are subject to state regulation.

State aid is expected to be influenced by WTO agreements that govern provision of government subsidies affecting trade. Application of WTO rules governing subsidies and compensatory measures is expected to result in structural reforms of the mechanisms, forms and volumes of state support of certain Ukrainian industries, including the coal sector, the agricultural sector, agricultural machine manufacture and the aircraft industry. See also “*Agriculture*”.

Mining

Ukraine possesses a large mineral reserve base, with approximately 8,000 deposits of 80 different minerals. It has more than 70 per cent. of the CIS countries’ reserves of manganese ores, 60 per cent. of kaolins, approximately 30 per cent. of iron ore deposits, 25 per cent. of cooking salt and 15 per cent. of coal deposits. Ukraine is the world’s fifth largest producer of iron ore and has the second largest reserve of manganese after South Africa. It also produces chrome, nickel, titanium and aluminium. Ukraine exported approximately U.S.\$1.6 billion, U.S.\$2.9 billion, U.S.\$1.8 billion and U.S.\$1.2 billion of non-metallic minerals and approximately U.S.\$1.1 billion, U.S.\$1.1 billion, U.S.\$617.3 million and U.S.\$369.6 million of nonferrous metals in 2007, 2008, 2009 and the six months ended 30 June 2010, respectively.

In 2009, 73.9 million tonnes of coal were produced, a 7.1 per cent. decrease compared to 2008. In the seven months ended 31 July 2010, 43.8 million tonnes of coal were produced, a 2.2 per cent. increase compared to the same period in 2009. Exports of coal in 2008, 2009 and the six months ended 30 June 2010, were 4.8 million, 5.3 million and 2.8 million tonnes, respectively. In 2008 and 2009, the total value of exports of coal was U.S.\$554.3 million and U.S.\$346.4 million, respectively. During the six months ended 30 June 2010, the value of coal exports was U.S.\$237.1 million.

The aggregate volume of coal deposits is estimated at approximately 117.5 billion tonnes. This volume represents 94.5 per cent. of the energy reserves of Ukraine and includes industrial reserves located at active mines of approximately 6.5 billion tonnes. The remaining 2 per cent. and 2.6 per cent. accounted for by oil and natural gas, respectively. As of 1 August 2010, 111 coal mining enterprises were in liquidation.

As of the date of this Prospectus, a significant number of coal producing enterprises are loss-making. However, due to a lack of financing for physical shut-down of coal-producing enterprises, as well as for environmental measures, redundancy payments and coal supplies for local heating requirements, progress on the closure of coal producing enterprises has been delayed. The Government continues to view coal as an important source of energy for Ukraine. In addition, many coal mines are seen as “social assets”, as they are the only or largest source of employment in certain cities or towns.

In 2009, state financing of the coal industry equalled UAH 10,494.0 million (UAH 5,057.2 million out of the State Budget general fund and UAH 5,436.8 million out of the special fund); this amount included expenditures for additional pension provisions for retired miners in the amount of UAH 3,997.5 million. In the six months ended 30 June 2010, state financing of the coal industry equalled UAH 2,761.6 million (UAH 24.4 million out of the State Budget general fund and UAH 2,737.2 million out of the special fund). State Budget expenditures to support the coal industry in 2010 are expected to total UAH 7.9 billion.

Priority tasks of the coal sector reform determined by the Concept for the Coal System Reform include raising private investments into the coal sector and reconstruction and modernisation of fixed assets of mining enterprises. In addition, as part of legislative changes required as a result of Ukraine’s accession to the WTO, a draft law on state support (subsidies) to the coal industry is being developed. Such law, once enacted, is expected to contribute to the promotion of the fair market competition amongst mining enterprises and improvement of their profitability.

Furthermore, the Economic Reform Programme (see “– *Action Programmes*”) provides for implementation of the following main measures aimed at reforming the Ukraine’s mining sector:

- at the first stage that should be completed by the end of 2010, Ukraine should, among other things, prepare for privatisation of coal mining companies and develop relevant privatisation programmes;
- at the second stage that should be completed by the end of 2012, Ukraine should, among other things, bring prices for coal produced by state-owned coal mines in line with market prices; develop auction

system for coal trade; liberalise coal imports; complete a transition to a system of direct and transparent subsidies for loss-making coal mines; privatise profitable coal mines; liquidate coal mines that either are at the closure or conservation stage, or have depleted their reserves; and ensure provision of state support to employees of liquidated coal mines; and

- at the third stage that should be completed by the end of 2014, Ukraine should, among other things, gradually reduce the amount of subsidies for state-owned coal mines.

Oil and Gas

Ukraine imports a significant portion of its primary energy needs, mainly in the form of crude oil and natural gas. Total domestic consumption of gas in Ukraine in 2008 and 2009 was 66.3 billion cubic metres (5.2 per cent. less than in 2007) and 51.9 billion cubic metres (21.7 per cent. less than in 2008), respectively. A decrease in domestic gas consumption in 2009 was caused by reduced demand from industrial producers, largely attributable to the significant decrease in industrial production in this period as well as to increased natural gas prices. In the seven months ended 31 July 2010, total domestic consumption of gas in Ukraine was 34.0 billion cubic metres, an increase of 14.6 per cent. compared to the same period of 2009. It is expected that for the full year 2010 total domestic consumption of gas will amount to 55.7 billion cubic meters.

In 2008, domestic production of gas increased by 1.7 per cent. compared to 2007 and reached 21.0 billion cubic metres. In 2009, domestic production of gas increased by 1.4 per cent. compared to 2008 and reached 21.3 billion cubic metres. The main reason for the low growth of domestic gas production is that Ukrainian gas reserves are difficult to extract, requiring special technologies and significant investments for exploitation. In the seven months ended 31 July 2010, domestic production of gas was 12.0 billion cubic metres, a decrease of 4.6 per cent. as compared to the same period in 2009. It is expected that for the full year 2010 total domestic production of gas will amount to 20.5 billion cubic meters.

Total domestic demand for oil has been approximately 23 million tonnes annually, which is substantially less than the consumption of similar sized countries in Western Europe. Domestic oil and gas condensate production was 4.0 million tonnes in 2009, a decrease of 6.8 per cent. as compared to 2008. In the seven months ended 31 July 2010, domestic production of oil and gas condensate was 2.1 million tonnes, a decrease of 11.5 per cent. as compared to the same period in 2009 caused by a depletion of reserves at the main deposit fields and reduction in the volumes of the exploitation drilling. Recently discovered oil fields in western Ukraine and the Black Sea may potentially increase the output of the sector. However, available resources in these regions are moderate and costs of exploration high due to great depths.

Ukraine has pipelines to transport gas and oil from the CIS to western Europe. Ukraine's gas transit system consists of approximately 39.8 thousand km of gas pipelines, 74 compressor stations and 13 underground gas storage facilities (with the capacity to store 32.0 billion cubic metres of gas), with a total transit capacity of approximately 178 billion cubic metres of gas per year, including 142 billion cubic metres of gas per year to central and western Europe. Approximately 21 per cent. of the pipelines have been in operation for more than 33 years and an additional 30 per cent. of the pipelines have been in operation for about 15 to 25 years. Ukraine's oil transit system consists of approximately 4,766.1 km of oil pipelines with a total capacity of 114.0 million tonnes per year, 28 pumping stations and tank fields with a capacity of more than one million tonnes. In June 2001, OJSC Ukrtransnafta ("Ukrtransnafta"), a state-owned oil company and 100 per cent. subsidiary of Naftogas, was established to manage and operate the transportation of oil by pipelines through Ukraine. This pipeline infrastructure is a major source of revenue with significant effects on Ukraine's balance of payments. See "*External Sector – Balance of Payments*".

In 2007, 115.2 billion cubic metres of gas were transited from one foreign country to another via Ukraine and not for use in Ukraine, a decrease by 10.3 per cent. as compared to 2006. In 2007, 39.8 million tonnes of oil were transported through Ukraine, an increase of 19.7 per cent. as compared to 2006. In 2008, 119.6 billion cubic metres of gas were transited from one foreign country to another via Ukraine (rather than for use in Ukraine), an increase of 3.8 per cent. compared to 2007. In 2008, 32.8 million tonnes of oil were transported through Ukraine, a decrease of 17.0 per cent. as compared to 2007.

In 2009, 95.8 billion cubic metres of gas were transited from one foreign country to another via Ukraine (rather than for use in Ukraine), a decrease of 19.9 per cent. compared to 2008. A decrease in gas transit volume in 2009 was largely attributable to European countries, which generally reduced consumption in response to the global economic downturn. In addition, transit volumes in 2009 were adversely affected by the temporary suspension of transit by Gazprom in January 2009. See “— *Oil and Gas — Russia*”. In the seven months ended 31 July 2010, 57.6 billion cubic metres of gas were transited from one foreign country to another via Ukraine, an increase of 20.5 per cent. compared to the same period of 2009. An increase in gas transit volume in the seven months ended 31 July 2010 as compared to the same period of 2009 is largely attributable to a low comparative base of the same period of 2009 caused by the temporary suspension of transit by Gazprom in January 2009.

In 2009, 29.1 million tonnes of oil were transported through Ukraine, a decrease of 11.4 per cent. as compared to 2008. In the seven months ended 31 July 2010, 11.9 million tonnes of oil were transported through Ukraine, a decrease of 33.2 per cent. as compared to the same period in 2009 largely as a result of the termination of the transit through Ukraine of Kazakh oil that is currently transported through Belarus. Pumping of oil for domestic use increased by 16.0 per cent. to 9.4 million tonnes in 2009, compared to 8.1 million tonnes in 2008 and increased by 9.4 per cent. to 5.4 million tonnes in the seven months ended 31 July 2010, compared to the same period in 2009.

Several pipelines bypassing Ukraine, including Nord Stream (together with internal European distribution pipelines), South Stream and Nabucco are presently projected by international consortia. When and if completed, such pipelines may be used to divert some of the gas currently transported through Ukraine. Ukraine will seek to minimise any potential influence, including through assurances on transportation volumes.

While Ukraine reports untapped internal energy sources of natural gas and oil, most of Ukraine’s external liabilities are generated through purchases of oil and gas. Ukraine imports oil almost exclusively from Russia, which has substantially raised its prices to close to world levels. Before 2009, Ukraine was one of the largest importers of natural gas in the world, with imports covering approximately 70 per cent. of its total domestic demand for gas. Ukraine imported 50.1 billion, 52.6 billion, 26.8 billion and 17.7 billion cubic metres of natural gas in 2007, 2008, 2009 and the seven months ended 31 July 2010, respectively. The decrease in imports in 2009 was largely attributable to the global economic downturn and increased natural gas prices. Ukraine imported 9.8 million tonnes, 6.6 million tonnes, 7.1 million tonnes and 4.3 million tonnes of oil in 2007, 2008, 2009 and the seven months ended 31 July 2010, respectively. Fuel and energy sources such as natural gas, oil and coal accounted for 18.8 per cent. of total imports in 2008 and 25.9 per cent. of total imports in 2009, with imports of natural gas alone accounting for 11.0 per cent. and 17.6 per cent., respectively. Fuel and energy sources such as natural gas, oil and coal accounted for 26.1 per cent. of total imports in the six months ended 30 June 2010 as compared to 27.9 per cent. in the six months ended 30 June 2009, with imports of natural gas alone accounting for 15.4 per cent. as compared to 21.0 per cent., respectively.

As at 31 December 2008, arrears to the State Budget of oil and gas sector enterprises amounted to UAH 1.6 billion and, by 1 August 2010, these arrears had decreased to UAH 1.0 billion.

The Economic Reform Programme (see “— *Action Programmes*”) provides for implementation of the followings main measures aimed at reforming the Ukraine’s oil and gas sector:

- at the first stage that should be completed by the end of 2010, Ukraine should, among other things, abolish natural gas price preferences established for certain industry sectors and develop a programme for modernisation of the domestic and transit gas pipeline systems as well as a programme for a restructuring of Naftogas (including, among other things, contemplated transfer of pipeline network and gas storage facilities to a separate state-owned legal entity);
- at the second stage that should be completed by the end of 2012, Ukraine should, among other things, gradually bring natural gas prices for consumers up to economically reasonable levels; and

- at the third stage that should be completed by the end of 2014, Ukraine should, among other things, complete Naftogas restructuring, implement a new model for use of natural gas distribution networks, and proceed with implementation of a modernisation programme for oil and natural gas transit systems, as well as implementation of the EU quality standards for oil products and modernisation of Ukraine's oil refinery capacities.

Russia

Based on the inter-governmental agreement dated 4 October 2001, Naftogas and Gazprom finalised long-term contracts on the transit and storage of Russian gas. Maintenance of the annual level of Russian gas transit through Ukraine to Western Europe at the level of at least 110 billion cubic metres per year until 2013 has been agreed. On the same date, Ukraine and Russia agreed to restructure U.S.\$1.4 billion of payment arrears accumulated for natural gas deliveries by Gazprom. Ukraine and Russia agreed that Naftogas would issue eurobonds to Gazprom in the aggregate principal amount of approximately U.S.\$1.4 billion, the amount of the arrears, with maturities between 2004-2013. As Gazprom had repeatedly refused to accept the delivery of the bonds, Naftogas and Gazprom reached an agreement on the new mechanism for the settlement of Naftogas' debt in August 2004. As a result of the 2004 settlement, Naftogas accepted a prepayment of transit fees from Gazprom in the amount of U.S.\$1.25 billion (equal to U.S.\$250.0 million per annum) for certain transit services between 2005 and 2009 (inclusive) and used received funds to settle its debt to Gazprom.

On 23 January 2003, an international consortium related to the management and development of the gas transit system was registered in Kyiv with Naftogas and Gazprom as the two founders. On 26 August 2003, Russia and Ukraine approved a project to build a 1,500 km gas pipeline in Ukraine for exports to Western Europe, with a capacity of 28 to 30 billion cubic metres annually. In December 2003, the consortium participants agreed to commence a feasibility study for the construction of a section of this gas pipeline between Novopskov and Uzhgorod in Ukraine. In 2004, Naftogas and Gazprom signed a co-operation agreement for the construction and management of the initial section of the Bogorodchany Uzhgorod gas pipeline and establishing the conditions for transportation of gas. If this project goes forward as planned, gas volumes transported through Ukraine may increase, according to Naftogas, by 19 billion cubic metres per year. In 2008-2010, Ukraine and Russia inter-governmental consultations on this issue were underway.

On 29 July 2004, Naftogas, Gazprom and certain other parties entered into a series of agreements for the provision of natural gas to, and development of gas transportation infrastructure in, Ukraine from 2005 to 2028. Further to these agreements, a new company, RosUkrEnergo AG, was established as an indirect subsidiary of the Joint-stock Bank of the Gas Industry Gazprombank (Closed Joint-stock Company) ("Gazprombank") and Raiffeisenbank, a member of the Austrian Raiffeisen Banking Group. RosUkrEnergo AG was managed by a coordination committee consisting of representatives of Gazprom, Gazprombank, Naftogas and Raiffeisenbank. RosUkrEnergo AG purchased gas for the Ukrainian market and oversaw the transit of the purchased gas shipments to and through Ukraine.

In late 2005, Gazprom began negotiations with Naftogas with a view to increasing prices for natural gas supplied by Gazprom to Ukraine to levels at which Gazprom sold natural gas to its customers in Western Europe. On 1 January 2006, Gazprom temporarily stopped selling natural gas to Naftogas in connection with a dispute over an increase in prices. On 4 January 2006, Gazprom, RosUkrEnergo AG and Naftogas entered into a series of agreements for the supply of natural gas by RosUkrEnergo AG and supplies resumed. Further to these agreements, on 2 February 2006 Naftogas and RosUkrEnergo AG established a joint venture, Ukrgaz Energo, which on the same date entered into a five-year contract (subsequently extended to 2028) with RosUkrEnergo AG for the supply of natural gas at a price to be fixed on a year-by-year basis. That agreement provided for the purchase by RosUkrEnergo AG of natural gas of Turkmen, Uzbek, Kazakh and Russian origin. The base price for the natural gas of Russian origin (used in calculations of the final price) was established at U.S.\$230.00 per 1,000 cubic metres. The parties agreed on a price of U.S.\$95.00 per 1,000 cubic metres of gas for the first six months of 2006 (which price remained in effect until 31 December 2006) as compared to the previous price of U.S.\$50.00 per 1,000 cubic metres, and for a transit fee for natural gas through the territories of Ukraine and the Russian Federation of U.S.\$1.60 per 1,000 cubic metres of gas for each 100 km until 1 January 2011. The parties further agreed that the transit fee and the price for natural gas

established by the agreement may be changed only by the parties' mutual consent. In 2006 and 2007, Ukgaz Energo was also selling natural gas to industrial customers in Ukraine. In October 2006, RosUkrEnergo AG and Ukgaz-Energo agreed to increase the price for natural gas which was supplied for domestic consumption in Ukraine in 2007 to U.S.\$130 per 1,000 cubic metres.

On 1 October 2007, immediately following the early elections to Parliament in Ukraine, Russia threatened to cut off the supply of gas to Ukraine in order to apply pressure on Naftogas and Ukgaz-Energo to settle outstanding debts owed by Naftogas to Ukgaz-Energo, which amounted to approximately U.S.\$700 million, as well as outstanding debts owed by Ukgaz-Energo to RosUkrEnergo AG. On 9 October 2007, Naftogas, Ukgaz-Energo, RosUkrEnergo AG and Gazprom reached a settlement agreement on the outstanding debts for the natural gas providing for the agreement of the parties to complete repayment of relevant debts by 1 November 2007. Naftogas used a prepayment of transit fees for services provided by Naftogas from October to December 2007, from Gazprom and RosUkrEnergo AG, as well as payments from other sources, to settle its debt to Ukgaz-Energo and Ukgaz-Energo intended to use the funds received from Naftogas to settle its debt to RosUkrEnergo AG. By 1 November 2007, the U.S.\$700 million owed by Naftogas to Ukgaz-Energo had been repaid in full. In December 2007, RosUkrEnergo AG and Ukgaz-Energo agreed to increase the price for natural gas which was supplied for domestic consumption in Ukraine in 2008 to U.S.\$179.5 per 1,000 cubic metres.

On 12 March 2008, Naftogas and Gazprom signed an agreement on the development of relations in the gas sector setting out an action plan to switch to direct Naftogas-Gazprom gas supply deals. In addition, in March 2008 Naftogas and RosUkrEnergo AG entered into a contract to supply 49.8 billion cubic metres of imported natural gas in 2008 at the price of U.S.\$179.5 per 1,000 cubic metres at the Russia/Ukraine border. A transit fee for transit of natural gas through the territories of Ukraine was set at U.S.\$1.70 per 1,000 cubic metres of gas for each 100 km for 2008. Further to the 12 March 2008 agreement, Gazprom established a subsidiary in Ukraine, LLC "Gazpromzbut Ukraina", that purchased 3.2 billion cubic metres and approximately 2.2 billion cubic metres of natural gas from Naftogas in 2008 and 2009, respectively, and is required to purchase not less than 2.8 billion cubic metres in 2010 for sale to Ukrainian consumers.

In 2008, Naftogas and Gazprom failed to reach agreement on the terms of natural gas supplies to Ukraine for 2009. On 1 January 2009, Gazprom significantly reduced gas supplies to Ukraine, both for domestic consumption and for transit to European countries. On 7 January 2009, Gazprom suspended natural gas supplies to Ukraine. In order to avoid large-scale interruptions, Naftogas put the gas transportation system into reverse functioning mode, with gas being transported not from east to west, as during normal functioning, but from Western Ukraine to Eastern Ukraine, which consumes more gas. The dispute between Ukraine and Russia over gas supplies was elevated to the European level, and experts from European states were granted access to the Ukrainian gas transportation system for monitoring purposes. On 17-19 January 2009, delegations from the Ukrainian and Russian governments, Naftogas and Gazprom conducted negotiations in Moscow to resolve outstanding issues and agree the terms of natural gas supplies. On 19 January 2009, contracts for natural gas supplies and transit in 2009-2019 were signed between Gazprom and Naftogas. The current contracts provide for a European-type formula for calculating the price of natural gas supplied for domestic consumption in Ukraine. According to this formula, the natural gas price depends upon the price of oil and oil products in the international markets and is determined on a quarterly basis subject to adjustments depending on gas quality. The average weighted price for natural gas in 2009 was approximately U.S.\$233.0 per 1,000 cubic metres, such price reflecting a 20 per cent. discount granted by Gazprom in 2009 to the price originally established for the following years. The tariff for natural gas transit through Ukrainian territory was fixed at a level of U.S.\$1.7 per 1,000 cubic metres for 2009. Starting from 2010, the tariff for natural gas transit through Ukrainian territory is calculated using a formula subject to adjustments depending on the natural gas price.

On 21 April 2010, amendments to the contracts for natural gas supplies and transit in 2009-2019 were signed, under which Gazprom has agreed to give Naftogas certain discounts from the otherwise applicable price for natural gas supplied for domestic consumption to Ukraine. Such discount shall be U.S.\$100.0 if the price for natural gas is equal to or greater than U.S.\$333.0 per 1,000 cubic metres, or 30 per cent. of the price if the price is below U.S.\$333.0 per 1,000 cubic metres. The discount shall account towards a partial payment of the rental price for the stationing of the Russian Black Sea Fleet the territory of Ukraine. In the seven months

ended 31 July 2010, the average weighted price for natural gas was approximately U.S.\$262.1 per 1,000 cubic metres. In 2010, the expected average weighted price for natural gas is currently estimated at U.S.\$266.5 per 1,000 cubic metres. The average tariff for natural gas transit through Ukrainian territory in 2010 is currently expected to be at U.S.\$2.65 per 1,000 cubic metres. In addition, pursuant to these amendments, the volume of natural gas transit via Ukraine in 2010 is expected to be up to 98.2 billion cubic metres, including up to 94.9 billion cubic metres to be transited to the European countries; the volume of natural gas to be supplied to Ukraine in 2010 for domestic consumption was increased from up to 33.7 billion cubic metres to up to 36.5 billion cubic metres. In addition, Ukraine and Russia have launched negotiations in relation to two new agreements with respect to cooperation in the gas sphere and cooperation in the sphere of oil transportation to Ukrainian oil refinery plants and oil transit through the Ukrainian territory.

In April 2008, RosUkrEnergo AG initiated an arbitration proceeding against Naftogas. During 2008 and 2009, Naftogas filed counterclaims against RosUkrEnergo AG, while RosUkrEnergo AG raised further claims against Naftogas, the aggregate amount of claims of each party being material. Subsequently, all such claims and counterclaims were consolidated into one dispute. According to reports, in June 2010, the arbitration tribunal issued an award in favour of RosUkrEnergo AG obliging Naftogas to return 11 billion cubic meters of natural gas to RosUkrEnergo AG, transfer to RosUkrEnergo AG an additional 1.1 billion cubic meters of natural gas as reimbursement of damages and pay approximately U.S.\$200.0 million as penalties and fines.

On 16 November 2004, Ukrtransnafta, the Russian company OJSC Transneft and the Russian-British joint venture TNK-BP signed an agreement for co-operation in the transportation of oil through Ukraine and Russia. The agreement provided for the annual supply of seven to nine million tonnes of Russian oil over a period of three years in the direction of Samara-Mozyr-Brody-Odessa; in 2006, the agreement was extended until 31 December 2009 and in December 2009 the agreement was further extended to 31 December 2010. In 2007 and 2008, approximately 9.1 million tonnes and 7.7 million tonnes of oil, respectively, were transported over this route. In 2009 and the seven months ended 31 July 2010, 8.2 million tonnes and 2.3 million tonnes of oil were transported over this route.

Turkmenistan

In May 2001, Ukraine and Turkmenistan signed a framework agreement under which Ukraine had the option to buy a total of 250 billion cubic metres of natural gas during the period 2002-2006, with annual volumes set out in separate protocols. This agreement was not extended beyond 2006. In each of 2003 and 2004, 31.5 billion cubic metres of gas were supplied to Ukraine at a rate of U.S.\$44 per 1,000 cubic metres, for which half of the purchase price was to be paid in dollars and half in goods and services. On 3 January 2005, Ukraine and Turkmenistan signed a further agreement that provided for the supply of 31.5 billion cubic metres of gas in 2005 at a rate of U.S.\$58 per 1,000 cubic metres, for which half of the purchase price was to be paid in dollars and half in goods and services. Pursuant to this agreement, Naftogas received 16.7 billion cubic metres of gas in the six months ended 30 June 2005. On 24 June 2005, Naftogas and Turkmenistan signed a new agreement setting conditions of sale of Turkmen gas to Ukraine in the second half of 2005. The price of gas was set at U.S.\$44 per 1,000 cubic metres compared to the previous U.S.\$58 per 1,000 cubic metres. From 1 July 2005, all payments for Turkmen gas were made in cash. Under a separate agreement, Ukraine received five billion cubic metres of gas in 2005 (0.5 billion more than previously agreed). As of 26 August 2010, all cash payments for natural gas supplied by Turkmenistan to Ukraine in 2003-2005 have been made in full, but Ukraine is to settle outstanding in-kind debts in the amount of approximately U.S.\$0.8 million.

In 2006-2009, no Turkmen gas was supplied to Ukraine under direct contracts with Turkmenistan and the Government does not expect that such supplies will resume in 2010. In the past, Turkmenistan confirmed the availability of resources necessary to ensure supplies of gas to Ukraine. However, Turkmenistan's position was that such supplies were conditional upon agreeing terms and conditions with Russia for the transit of Turkmen gas to be supplied to Ukraine.

A draft agreement on future long-term co-operation in the oil and gas sphere between Ukraine and Turkmenistan was prepared by Ukraine and submitted to Turkmenistan for consideration in 2005. The draft

agreement provides for the supply of annual volumes of 40-60 billion cubic metres of natural gas from Turkmenistan during the period of 2007-2031. As of 26 August 2010, this draft agreement had not yet been concluded.

Poland and the Euro-Asian oil transport corridor (EAOTC Project)

From 2005 to 1 August 2010, Naftogas exported minor volumes of natural gas to Poland, totalling approximately 24.2 million cubic metres of gas.

On 14 January 2004, the Cabinet of Ministers approved an agreement with the Government of Poland on the use of the Odessa-Brody pipeline. On 16 January 2004, an agreement was signed by Ukrtransnafta and the Polish oil transportation company Przyjazn PERN to establish a joint venture extending the Odessa-Brody pipeline to Plotsk in Poland, as well as to attract investment for the project. In 2004, the Sarmatia joint venture was created with the participation of Ukrtransnafta and Przyjazn PERN.

In February 2007, Poland proposed to change the bilateral form of this project to a five-party joint venture between Ukraine, Lithuania, Poland, Georgia and Azerbaijan. At the Energy Summit held in May 2007, these five nations agreed to create an inter-governmental working group to formulate criteria for the establishment and function of the joint venture. The purpose of this joint venture is to develop joint energy projects, particularly relating to the Odessa-Brody-Plotsk-Gdansk oil pipeline and the transportation of Caspian oil to European consumers. In June 2007, the inter-governmental working group decided to prepare a feasibility study for this project and to include Lithuania, Georgia and Azerbaijan as new shareholders of Sarmatia; these new shareholders joined in January 2008. At the Energy Summit held in October 2007, an Agreement on Cooperation in the Energy Sector was signed by relevant ministries of Ukraine, Lithuania, Poland, Georgia and Azerbaijan, providing for the creation of a comprehensive legal framework for the implementation of the Odessa-Brody-Plotsk-Gdansk project. At the International Energy Summit held in May 2008, participants reviewed a draft feasibility study for the Odessa-Brody pipeline, as well as a Ukraine-Azerbaijan agreement to fill this pipeline with Caspian oil. Also at the summit, the Presidents of Azerbaijan, Georgia, Lithuania, Poland and Ukraine signed a Joint Declaration concerning the Euro-Asian oil transport corridor.

In 2009, construction of an oil pipeline that would connect Ukrainian and Polish oil transport infrastructure as part of the EAOTC Project was included in the list of priority projects to be implemented within the framework of the Infrastructure and Environment Operational Programme approved by the European Commission (the “EU Programme”). At the Energy Conference held in Batumi, Georgia, in January 2010, a feasibility study of the EAOTC Project was presented to the conference participants, which included representatives of the EU Commission, and the Joint Statement of Batumi Energy Conference was adopted supporting the EAOTC Project countries’ intention to develop an Action Plan setting out measures for the timely and efficient implementation of the project. In addition, in January 2010, the shareholders of Sarmatia decided on a capital increase of Sarmatia to comply with the eligibility criteria set by the European Commission in order to obtain financing within the EU Programme.

Electricity Generation and Nuclear Power

As of 1 January 2010, the total electricity generating capacity of Ukraine was estimated at approximately 53.0 gigawatts. Production in 2007, 2008, 2009 and the seven months ended 31 July 2010 was recorded at 195.1 billion kwh, 191.7 billion kwh, 172.9 billion kwh and 107.6 billion kwh (an increase of 10.1 billion kwh or 10.4 per cent. compared to the seven months ended 31 July 2009), respectively, of which 92.5 billion kwh, 89.8 billion kwh, 82.9 billion kwh and 50.8 billion kwh, respectively, was provided by nuclear energy.

In 2009, 48.0 per cent. of the energy generated by United Energy System of Ukraine (a group of Ukrainian power industry entities having a common production regime and a centralised management) was provided by nuclear power stations, 41.1 per cent. was provided by thermal power stations, 6.8 per cent. was provided by hydropower stations and 4.1 per cent. was provided by low-capacity thermal-fired block stations owned and operated by enterprises and thermal power stations operated by local authorities. In 2009, thermal power stations and nuclear power stations decreased production by 11.3 billion kwh and 6.9 billion kwh, respectively, as compared to 2008, while hydropower stations increased production by 0.4 billion kwh. In

2009, 4,108.3 million kwh were exported from Ukraine, a decrease of 3,729.5 million kwh, or 47.6 per cent., compared to 2008. A decrease in electricity export volume in 2009 was largely attributable to European countries, which generally reduced consumption in response to the global economic downturn, and repair works undertaken at the thermal power stations in Western Ukraine that are main producers of the electricity exported to Hungary, Slovakia and Romania.

In the seven months ended 31 July 2010, 47.2 per cent. of the energy generated by United Energy System of Ukraine was provided by nuclear power stations, 40.0 per cent. was provided by thermal power stations, 8.6 per cent. was provided by hydropower stations and 4.2 per cent. was provided by low-capacity thermal-fired block stations owned and operated by enterprises and thermal power stations operated by local authorities. In the seven months ended 31 July 2010, thermal power stations, nuclear power stations and hydropower stations increased production by 4.6 billion kwh, 3.3 billion kwh and 1.9 billion kwh, respectively, each as compared to the same period of 2009. Should demand in Ukraine increase, additional electricity generation is likely to be achieved primarily by increasing output from thermal and nuclear power stations. In the seven months ended 31 July 2010, 2,323.4 million kwh were exported from Ukraine, an increase of 507.2 million kwh, or 27.9 per cent., compared to the same period in 2009. Ukraine currently exports electricity to Hungary, Slovakia, Romania, Moldova and Belarus.

Ukraine currently operates 15 nuclear energy reactors located at four nuclear power stations (“NPSs”): Zaporizhzhya NPS, with six reactors with a production capacity of 1,000 megawatts each; Rivne NPS, with four reactors with a production capacity of 415 megawatts, 420 megawatts and 1,000 megawatts (two reactors), respectively; Khmelnytsky NPS, with two reactors of 1,000 megawatts each; and Pivdenoukrainska NPS, with three reactors with a production capacity of 1,000 megawatts each. These four power stations have a total production capacity of 13,835 megawatts, or 26.1 per cent. of total electricity production capacity in Ukraine. Most of the nuclear reactors in Ukraine were put into operation during the 1980s and 1990s and two nuclear reactors were put into operation during 2006 and 2007. The Government expects the initially contemplated lifetime of 13 of the 15 currently active nuclear reactors to expire between 2010 and 2025. However, the Government is implementing a refurbishment programme for certain of these reactors which will, if successful, extend their useful life by an additional period to be determined for each such reactor separately.

In 2009, Ukrainian nuclear power stations produced 82.9 billion kwh of electrical energy (as compared to 89.8 billion kwh in 2008), amounting to 48.0 per cent. of total electrical energy produced in Ukraine. The NPS capacity use ratio was 68.4 per cent. (compared to 73.9 per cent. in 2008). In the seven months ended 31 July 2010, Ukrainian nuclear power stations produced 50.9 billion kwh of electrical energy (compared to 47.5 billion kwh in the seven months ended 31 July 2009), equal to 47.1 per cent. of total electrical energy produced in Ukraine. The NPS capacity use ratio amounted to 72.1 per cent. in the seven months ended 31 July 2010 (compared to 67.5 per cent. in the seven months ended 31 July 2009).

To date, Russia is the only supplier of nuclear fuel for the needs of Ukrainian NPSs. In general, countries with a developed nuclear energy industry have at least two suppliers of nuclear fuel. Ukraine is taking measures to increase the number of alternative suppliers of nuclear fuel. In order to eliminate the Russian monopoly and diversify nuclear fuel supplies, Ukraine is currently implementing a U.S.-Ukrainian Nuclear Fuel Qualification Project for 2005-2010. In 2005, within the first stage of the project, Ukraine began operating its first six research units of U.S. produced fuel and from April 2010 Ukraine has been operating 42 heat-generating units of U.S. produced fuel. After completion of the qualification, Ukraine will be able to purchase nuclear fuel from suppliers other than Russia. In addition, Ukraine is considering establishing a company to produce nuclear fuel domestically.

Following the incident at the Chernobyl NPS in 1986, in accordance with requirements of international treaties and the Memorandum of Understanding (the “MOU”) with the G-7 states signed in December 1995, the Government has implemented certain measures for the improvement of operating safety at functioning nuclear reactors.

In accordance with the terms of the MOU, on 15 December 2000, Ukraine permanently stopped operation of the energy reactors at the Chernobyl NPS. To compensate for the loss of production capacity, Ukraine has constructed and put into operation two new nuclear reactors without raising funds from external sources: N 4

at the Rivne NPS and N 2 at the Khmelnytsky NPS, with total production capacities of 1,000 megawatts each. In August 2004, the new N 2 nuclear reactor at the Khmelnytsky NPS was connected to the electrical grid, followed by the connection of the new N 4 nuclear reactor at the Rivne NPS in October 2004. During 2006-2007, reactor N 2 of the Khmelnytsky NPS and reactor N 4 of the Rivne NPS were put into operation.

In 2004, Energoatom, Ukraine's nuclear energy company, entered into loan agreements with the EBRD and the European Atomic Energy Community (Euratom) for the purpose of modernising and upgrading the safety features of Ukrainian NPSs. These loans are guaranteed by the State. The total amount of these agreements is U.S.\$125.0 million, consisting of a loan from the EBRD of U.S.\$42.0 million and a loan from Euratom of U.S.\$83.0 million. In addition, in February and October 2008, a €150.0 million loan agreement with the EBRD and a €150.0 million loan agreement with the EIB under a joint EBRD-EIB-Ukraine "Construction of the 750 kV Rivne NPP — Kyiv Overhead Transmission Line" Project were signed. The Government expects that €150 million for this project will be funded by the EIB, with another €150.0 million to be funded by the EBRD. As at 1 August 2010, €1.52 million in EBRD funds had been disbursed for this project. The project aims to eliminate capacity limitations at the Rivne NPS and Khmelnytsky NPS and to improve the reliability of energy supply to the consumers in Central Ukraine. The EBRD and Ukraine are also considering the implementation of a project for energy savings in the railway transport sector, Ukrhydroenergo Rehabilitation Project, under which Ukraine expects to borrow €200 million from the EIB, with an additional €200 million proposed to be funded by the EBRD, and two projects for the construction of electrical transmission lines, under which Ukraine expects to borrow €225 million from the EIB, with an additional €225 million proposed to be funded by the EBRD. See "*Public Debt – International Organisations*".

Ukraine has developed a programme for electricity grid development through 2011, which provides, among other things, for the creation by 2011 of a system for the transfer of electricity from regions with excess capacity (Western Ukraine) to regions experiencing electricity deficits (Central and Eastern Ukraine), and for increased reliability of electricity supplies.

The Economic Reform Programme (see "*– Action Programmes*") provides for implementation of the followings main measures aimed at reforming the Ukrainian power generation sector:

- at the first stage that should be completed by the end of 2010, Ukraine should, among other things, abolish electricity price preferences established for certain industry sectors; lift the moratorium on privatisation of state-owned assets in the energy sector (save for certain exceptions, such as state-owned assets in nuclear and hydropower sectors); implement certain measures to improve payment discipline, including introduction of penalties for overdue payments for electricity and housing and communal services; and start gradually bringing the electricity tariffs to economically reasonable levels;
- at the second stage that should be completed by the end of 2012, Ukraine should, among other things, abolish the single tariff system, complete bringing the tariffs to economically reasonable levels, privatise energy-distribution companies and launch privatisation of thermal energy-generating companies; and
- at the third stage that should be completed by the end of 2014, Ukraine should, among other things, complete privatisation of thermal energy-generating companies.

Electricity and Natural Gas Tariffs

In order to eliminate the practice of cross-subsidisation and minimise price distortions between electricity market consumers, the Government adopted a resolution at the end of 2005 to bring tariffs for energy carriers to economically reasonable levels for all categories of consumers. During 2007, the average wholesale market price for electrical energy was UAH 0.2392 per kwh. In 2008, 2009 and the seven months ended 31 July 2010, the wholesale market price for electrical energy increased to UAH 0.3330 per kwh, UAH 0.4077 per kwh and UAH 0.4630 per kwh, respectively.

In 2006, prices for electricity supplied to the population were increased in two stages: by 25 per cent. in May and by 25 per cent. in September. Starting from September 2006, therefore, the population purchased electrical energy at an average price of UAH 0.1933 kwh, which as at September 2010 constituted approximately 26 per cent. of the economically reasonable price. During 2007, 2008, 2009 and the eight months ended 31 August 2010, there were no increases in prices for electricity supplied to the population.

In August 2005, the Cabinet of Ministers adopted a resolution recommending that the National Commission for Electrical Power Industry Regulation adopt effective from 1 September 2005, a single tariff for all consumers with the exception of electricity supplied to the population, cities, towns and villages, or to exterior lighting. Monthly increases in the unified tariff should not exceed 5 per cent. of the tariff for the previous month. During the period from November 2008 to October 2009, the single tariffs for the first and second voltage classes remained unchanged at UAH 0.4359 kwh and UAH 0.5846 kwh, respectively. The National Commission for Electrical Power Industry Regulation has been gradually increasing the single tariffs, starting in November 2009. As of 31 August 2010, the single tariffs for the first and second voltage classes were UAH 0.5527 kwh and UAH 0.6860 kwh, respectively. From October 2008 to April 2010, the single tariffs for mining, metallurgical and chemical enterprises within the first and second voltage classes remained at UAH 0.4221 kwh and UAH 0.5624 kwh, respectively. In April-June 2010, the single tariff was established for mining, metallurgical and chemical enterprises within the first and second voltage classes at UAH 0.4572 kwh and UAH 0.6068 kwh, respectively. Starting July 2010, mining, metallurgical and chemical enterprises do not enjoy preferential tariffs.

In response to substantial changes in the natural gas market and the review by the Russian Federation of contracts for gas supply to Ukraine, the threshold level of natural gas prices was increased several times during 2006 and 2007. Starting from 1 January 2008, the threshold price level was UAH 934.7 per 1,000 cubic metres (excluding VAT, transportation, underground gas storage and supply tariffs, Naftogas sales related expenses and special purpose charge) for state-financed consumers, industrial consumers and other commercial entities. In October 2008, in line with the significant devaluation of the hryvnia against the U.S. dollar, the Government increased threshold price levels for these categories of consumers. In particular, from 15 November 2008 the threshold price was UAH 1,152.0 per 1,000 cubic metres (excluding VAT, transportation, distribution and supply tariffs, Naftogas sales-related expenses and special-purpose charges) for state-financed consumers, industrial consumers and other commercial entities. In addition, the Government permitted this price to be subject to indexing based on the ratio of the average monthly hryvnia U.S. dollar exchange rate and the official hryvnia exchange rate to the U.S. dollar. Furthermore, beginning 1 May 2008, the Government permitted Naftogas to include the amount of its sales-related expenses in the gas sale price for state-financed consumers, industrial consumers and other commercial entities. These expenses amounted to UAH 87.43, UAH 86.95 and UAH 121.0 per 1,000 cubic metres as of 1 May, 1 August and 1 November 2008, respectively.

In 2009 and the four months ended 30 April 2010, the threshold price was UAH 2,020.25 per 1,000 cubic metres (excluding VAT, transportation, distribution and supply tariffs, and special purpose charge) for state-financed consumers, industrial consumers and other commercial entities, subject to indexing based on the ratio of the average monthly hryvnia exchange rate to the U.S. dollar and the official hryvnia exchange rate to the U.S. dollar. Starting 1 May 2010, the threshold price reduced to UAH 1,992.8 per 1,000 cubic metres (excluding VAT, transportation, distribution and supply tariffs, and special purpose charge) for state-financed consumers, industrial consumers and other commercial entities. In addition, from 1 January 2009 to 1 April 2010, a reduced threshold price of UAH 1,899.25 per 1,000 cubic metres (excluding VAT, transportation, distribution and supply tariffs, and special purpose charge) applied to mining, metallurgical and chemical enterprises; and starting 1 January 2009 to 1 July 2010, a reduced threshold price applied to enterprises producing nitrogen fertilisers, such threshold price being UAH 1,633.3 per 1,000 cubic metres (excluding VAT, transportation, distribution and supply tariffs, and special purpose charge) from 1 April 2010 to 1 July 2010. Starting from 1 August 2010, the threshold price is UAH 2,187.2 per 1,000 cubic metres (excluding VAT, transportation, distribution and supply tariffs, and special purpose charge) for all categories of industrial consumers and state-financed consumers.

Beginning 1 June 2008, the threshold price was UAH 710.0 per 1,000 cubic metres (including VAT, transportation, underground gas storage and supply tariffs, Naftogas sales-related expenses and special

purpose charge) for municipal heating enterprises. This price increased by 3.5 per cent. monthly in the course of 2008 up to UAH 872.8 per 1,000 cubic metres from 1 December 2008, representing an increase of approximately 27 per cent. as compared to May 2008. In 2009 and the seven months ended 31 July 2010, the threshold price for municipal heating enterprises remained UAH 872.8 per 1,000 cubic metres (including VAT, transportation, distribution and supply tariffs, storage expenses and special purpose charges). In September 2009, the National Commission for Electrical Power Industry Regulation decided to increase the threshold price for municipal heating enterprises by 20 per cent. from 1 October 2009. However, because the Kyiv District Administrative Court prohibited implementation of this increase, no actual increase took place on 1 October 2009. In order to comply with the arrangements reached between Ukraine and the IMF, on 13 July 2010, the National Commission for Electrical Power Industry Regulation approved an increase of threshold prices for natural gas charged to municipal heating enterprises. In particular, starting from 1 August 2010, the threshold price for municipal heating enterprises was increased by 50.0 per cent. to UAH 1,309.2 per 1,000 cubic metres (including VAT, transportation and distribution tariffs, and special purpose charges). As at August 2010, such threshold price for municipal heating enterprises constitutes 44.0 per cent. of economically reasonable price level.

In addition, from 1 January 2007, the Government changed its approach to establishing natural gas prices for households. Threshold levels of wholesale prices were replaced with differentiated threshold retail prices for households depending on the volumes of consumption. As of 1 January 2007, prices for households ranged from UAH 315.0 to UAH 1,290.0 per 1,000 cubic metres and increased to a range of UAH 358.2 to UAH 1,458.6 per 1,000 cubic metres from 1 September 2008, followed by a further increase to a range of UAH 483.6 to 1,968.6 per 1,000 cubic metres from 1 December 2008. In July 2009, the National Commission for Electrical Power Industry Regulation decided to increase the threshold price for households by 20 per cent. from 1 September 2009. However, the National Forum of Trade Unions of Ukraine challenged this decision before the Kyiv District Administrative Court, which ruled the decision unlawful on 31 August 2009. As a result, the increase was not implemented from 1 September 2009 as planned. In order to comply with the arrangements reached between Ukraine and the IMF, on 13 July 2010, the National Commission for Electrical Power Industry Regulation approved an increase of threshold prices for natural gas charged to households. In particular, with effect from 1 August 2010, threshold retail prices for were increased by 50.0 per cent. to a range of UAH 725.4 to UAH 2,954.1 per 1,000 cubic meters.

The threshold prices charged to households, to state-financed consumers and to municipal heating enterprises have been subsidised from the State Budget. In particular, in 2009, UAH 4.1 billion were extended from the State Budget to Naftogas as a compensation for the difference between the purchase price of imported gas by Naftogas and the sales price of such gas to municipal heating enterprises. The 2010 State Budget provides for UAH 3.4 billion to be extended to Naftogas to cover this difference and as at 18 August 2010, the State Budget allocated approximately UAH 2.9 billion to Naftogas for the same purpose. These and a number of other measures are aimed at an improvement of the financial standing of Naftogas. The Government intends to gradually increase the threshold prices charged to households and to municipal heating enterprises to economically reasonable levels. In particular, pursuant to the Memorandum on Economic and Financial Policy entered into within the framework of the 2010 IMF stand-by arrangement, another 50 per cent. increase in natural gas prices for households and municipal heating companies is to be effected in April 2011. Thereafter, semi-annual increases of gas prices for these categories of consumers are expected to continue until domestic price levels reach import parity.

In May 2010, the Parliament of Ukraine adopted amendments to the Law of Ukraine “On Value Added Tax”, which exempts from VAT natural gas imports to Ukraine. The exemption shall apply starting from the first tax reporting period after 16 June 2010.

Due to increased efforts by the Government, domestic consumer payment discipline has improved in comparison to earlier periods. The average cash collection rate for electricity consumption was 97.8 per cent. in 2009, 100.7 per cent. in 2008 and 98.9 per cent. in 2007. Collection rates in excess of 100 per cent. reflect payment of overdue indebtedness from earlier periods. In the seven months ended 31 July 2010, the rate of collection for electricity consumption was 97.3 per cent. compared to 98.1 per cent. in the same period of 2009. The rate of cash collection for gas consumption reached 86.4 per cent. in 2009, 93.9 per cent. in 2008

and 86.7 per cent. in 2007. The rate of cash collection for gas consumption was 84.9 per cent. in the seven months ended 31 July 2010 compared to 83.1 per cent. in the same period in 2009.

Agriculture

Ukraine was traditionally viewed as the “bread basket” of the Soviet Union. Thus, although Ukraine accounted for only 15 per cent. of arable land in the former USSR and 4.6 per cent. of total agricultural land area in 1988, it produced 26 per cent. of the former USSR’s total grain output, 53.5 per cent. of its sugar beet output, 26.7 per cent. of its potato output and 20 per cent. of its total livestock production.

The Ukrainian agro-food industries were highly integrated into the Soviet food supply system. Since independence, this sector has been hit by protectionist policies adopted by some of Ukraine’s trade partners. Russia, for instance, in order to reduce its dependence on imported grain and sugar, has imposed high tariffs and indirect taxes on these commodities that remain in effect. Significant reduction in demand, and slow progress in privatisation of land and the agricultural sector in general, has led to a decline in agricultural output. Nonetheless, between 1992 and 1995, the sector performed relatively better than the rest of the economy. With the liberalisation of foreign trade in 1995-1996, food exports began to recover, reaching 21 per cent. of total merchandise exports of Ukraine in 1996. Between 1996 and 1999, due principally to a lack of structural reform and increasing inefficiencies in the sector, production declined continuously. In 2000, the Government initiated reforms of the agricultural sector, pursuant to which members of collective farms could take their share of land or lease their land plots. The food-production sector began to recover and agricultural production increased in 2000, 2001 and 2002 followed by 11.0 per cent. decrease in 2003 as a result of frosty weather destroying winter crops at the beginning of 2003.

In 2004, agricultural production increased by 19.7 per cent. compared to 2003 because of a grain harvest of 41.8 million tonnes, more than double that of 2003. In 2005, agricultural production remained substantially at 2004 levels. In 2006, agricultural production increased by 2.5 per cent. as compared to 2005, which included a 9.9 per cent. decrease in crop production and a 3.6 per cent. growth in livestock production.

In 2007, agricultural production decreased by 6.5 per cent. compared to 2006, reflecting a decrease of 4.2 per cent. in the production of agricultural enterprises (both state-owned and private) and a decrease of 7.9 per cent. in the agricultural production of household plots (land not registered as an enterprise). Decline in the agricultural production in 2007 resulted from a 14.5 per cent. decline in crop production due to unfavourable weather conditions between April and June 2007, including a severe drought in the central, eastern and southern regions of Ukraine. This decrease in crop production included a decrease of 11.1 per cent. in the production by agricultural enterprises (both state-owned and private) and a decrease in the production by household plots of 24.7 per cent. Declines in crop production have resulted in an increase in crop prices; in particular, wholesale grain prices increased by 61.8 per cent. in 2007. In 2007, livestock production declined by 2.3 per cent. compared to 2006. This overall decline reflected an increase by 7.1 per cent. in the production of agricultural enterprises (both state-owned and private) and a decrease in production by household plots of 7.3 per cent.

In 2008, agricultural production increased by 17.1 per cent. compared to 2007, reflecting an increase of 35.1 per cent. in the production of agricultural enterprises (both state-owned and private) and an increase of 5.2 per cent. in the agricultural production of household plots (land not registered as an enterprise). The increase in agricultural production in 2008 resulted from a 30.5 per cent. growth in crop production, especially grain and sunflower, due to favourable weather conditions. This growth in crop production included an increase of 55.6 per cent. in the production by agricultural enterprises (both state-owned and private) and an increase in the production by household plots of 12.7 per cent. In 2008, livestock production increased by 0.1 per cent. compared to 2007. This minor increase reflected an increase by 6.4 per cent. in the production of agricultural enterprises (both state-owned and private) and a decrease in production by household plots of 3.8 per cent.

In 2009, agricultural production decreased by 1.8 per cent. compared to 2008, reflecting an increase of 0.4 per cent. in the agricultural production of household plots and a decrease of 4.4 per cent. in the production of agricultural enterprises (both state-owned and private). The decrease in agricultural production in 2009 included a 5.2 per cent. decrease in crop production partially offset by a 3.8 per cent. increase in

livestock production. The 3.8 per cent. increase in livestock production reflected an increase of 9.9 per cent. in the production of agricultural enterprises (both state-owned and private) and minor decline in production by household plots of 0.4 per cent., while a 5.2 per cent. decline in crop production included a decrease of 11.3 per cent. in the production of agricultural enterprises (both state-owned and private) and minor growth in production by household plots of 0.9 per cent.

In the seven months ended 31 July 2010, agricultural production decreased by 0.6 per cent. compared to the same period in 2009. This decrease reflects a decrease of 4.7 per cent. in the production of agricultural enterprises (both state-owned and private) and an increase of 3.6 per cent. in the agricultural production of household plots. The decrease in agricultural production in the seven months ended 31 July 2010 was due to a decrease in crop production by 5.7 per cent., including a decrease in crop production by agricultural enterprises (both state-owned and private) by 16.7 per cent. and an increase in crop production by household plots by 12.5 per cent. In the seven months ended 31 July 2010, the decline in crop production was offset by the increase in livestock production by 3.3 per cent., including the increase in livestock production by agricultural enterprises (both state-owned and private) by 9.0 per cent. and the decrease in livestock production by household plots by 0.8 per cent. The Government expects that for the full year 2010 agricultural production will decrease by 1.4 per cent.

Beginning in 2005, agricultural producers enjoyed certain tax privileges, including a right to retain the 20 per cent. VAT collected from customers instead of remitting such VAT to the State. The law extending the VAT privileges, including zero-rate VAT for certain kinds of meat and dairy producers, applied from 1 January 2005 until 1 January 2009. Pursuant to a law passed in May 2007 as part of the process of WTO accession, from 1 January 2009, zero rate VAT was expected to be abolished. Instead, starting from 1 January 2009, agricultural, forestry and fishery producers were to apply for a special VAT regime providing a 9 per cent. VAT rate for agricultural products and 6 per cent. VAT rate for forestry and fishery products. However, pursuant to a law passed in October 2008 as part of measures aiming to minimise the impact of the financial downturn, from 1 January 2009 agricultural producers apply a new regime. Under this regime, agricultural producers are not required to remit to the State 20 per cent. VAT received from the customers and may use such VAT to compensate the 20 per cent. VAT payable by them to suppliers of agricultural products as well as to finance other business needs. In addition, meat and milk producers receive subsidies from the State Budget at the expense of VAT paid to the State Budget by processing enterprises.

The Government believes that one of the priority tasks of the agro-industrial complex for the near future is the reform of the forms, mechanisms and volumes of state support to the agricultural sector in accordance with the WTO principles. Agreements reached during the negotiations on Ukraine's accession to the WTO permit Ukraine to effectively subsidise the agro-industrial complex within the specific programmes aimed at the support of livestock and crop production and partially reimburse to agricultural producers their expenditures on borrowings, as well as indirectly support agricultural producers through VAT retention and VAT subsidy mechanisms. At the same time, Ukraine has undertaken not to exceed the maximum permitted cumulative amount of support at the level of UAH 3.4 billion, such amount not including amounts that could be spent on so called "green" programmes, which have zero or minimal impact on trade, and which are not restricted by the WTO arrangements.

The Economic Reform Programme (see "*Action Programmes*") provides for a wide range of measures to increase efficiency and competitiveness of Ukraine's agricultural sector, including the following measures:

- at the first stage that should be completed by the end of 2010, Ukraine should ensure that the State does not inadequately intervene into the regulation of prices for agricultural products or establish export restrictions. Ukraine should also agree with the WTO and implement certain technical regulations for imports in order to reduce low-quality imports into Ukraine, as well as improve the subsidy system in line with the WTO rules; and
- at the second stage that should be completed by the end of 2012, Ukraine should, among other things, create a transparent market for agricultural land plots based on the single land cadastre system, and harmonise with the WTO rules the system of standards and technical regulations for agricultural products.

Approximately one-third of Ukraine's total population lives in rural areas, and approximately 7 per cent. of the country's employed labour was employed in agriculture in 2009.

Construction

The construction sector experienced a large output decline in the period 1992 to 1997. In 2000 to 2001, the construction sector began to recover. In 2003 and 2004, construction increased by 26.5 per cent. and 17.2 per cent., respectively, as a result of several large public projects, including the building of two nuclear power plants and the reconstruction of a segment of the Kyiv-Odessa highway. In 2005, however, construction declined by 6.6 per cent., as several of the projects undertaken in the previous two years were completed and no new large projects were built, the 2005 decline being followed by a 9.9 per cent. increase in construction in 2006. In 2007, construction increased by 15.6 per cent., which included 16.5 per cent. growth in the construction of residential and non-residential buildings, 38.9 per cent. growth in the construction and repairs of highways and 15.0 per cent. in the construction of bridges and underground. In 2008, construction decreased by 15.8 per cent., which included a 13.2 per cent. decline in the construction of residential and non-residential buildings, a 36.3 per cent. decline in the construction and repairs of highways and a 6.9 per cent. decline in the construction of bridges and underground. In 2009, construction decreased by 48.2 per cent., which included a 54.5 per cent. decline in the construction of residential and non-residential buildings, a 37.5 per cent. decline in the construction and repairs of highways and a 50.6 per cent. decline in the construction of bridges and underground.

In the seven months ended 31 July 2010, as compared to the same period in 2009, construction declined by 16.7 per cent., which included an 18.3 per cent. decline in construction of residential and non-residential buildings, a 40.1 per cent. decline in construction of bridges and underground, a 15.9 per cent. decline in construction and repairs of highways, a 11.9 per cent. decline in construction of trunk pipelines and energy supply lines and a 23.6 per cent. decline in construction of local pipelines and energy supply lines. The decline under major types of construction works in the seven months ended 31 July 2010 is attributable to the reduced volumes of mortgage lending to the population as well as of lending to construction companies by Ukrainian banks and an increase in the cost of construction works as compared to the planned figures.

Transport and Communications

The transport and communication infrastructure of Ukraine is fairly well developed, with a wide network of roads and railroads and a moderately developed telecommunications network. As in many other CIS countries, the transportation and communication systems are in need of modernisation. Like other sectors of Ukraine's economy, the transportation and communication sector was adversely affected by the decline in domestic investment and the economic crisis of the 1990s as well as a more recent financial and economic downturn in 2009. In 2007 and 2008, output in the transportation and communication sectors increased by 11.7 per cent. and 7.5 per cent., respectively, which was followed by a decrease of 9.3 per cent. in 2009.

The growth in transport recorded in 2007 and 2008 was principally caused by higher actual income of the population and an increasing volume of intercity and international traffic as a result of an increase in the volume of trade and exports. In 2009, against the background of the global economic downturn, the growth trend was reversed and transport enterprises transported 696.2 million tonnes of cargo, a decrease of 21.9 per cent. as compared to 2008, and 7.3 billion passengers, a decrease of 12.7 per cent. as compared to 2008. The decline in transportation in 2009 was largely attributable to the reduction in production in the mining, construction and chemical industries and reduction in foreign trade turnover volumes, as well as to a decline in household income. In the seven months ended 31 July 2010, transport enterprises transported 421.1 million tonnes of cargo and 3.95 billion passengers, representing 12.5 per cent. increase and 7.7 per cent. decline as compared to the seven months ended 31 July 2009, respectively. The growth in cargo transportation in the seven months ended 31 July 2010 is attributable to the increase in production by mining, machinery manufacturing, metallurgy and chemical industries, the increase in the gas transportation volumes and the increase in foreign trade turnover volumes.

Increasing demand for services in mobile and international telephone connections led to a growth in communications; in 2009, mobile communication services accounted for approximately 61.6 per cent. of all

communication services, with intercity and international telephone, local telephone and internet services accounting for approximately 10.1 per cent., 9.0 per cent. and 6.2 per cent., respectively. In the seven months ended 31 July 2010, mobile communication services accounted for 60.6 per cent. of all communication services, with intercity and international telephone, local telephone and internet services accounting for 9.0 per cent., 9.0 per cent. and 7.7 per cent., respectively.

The largest international airport in Ukraine is Boryspil International State Airport in Kyiv. In March 2005, the Japanese Bank of International Co-operation extended a ¥19.092 billion (U.S.\$178 million at the then current exchange rate) loan to construct a new passenger terminal at Boryspil to international standards and to convert the airport into a regional hub, capable of handling increasing volumes of air traffic between Russia and the Near East. As at 1 August 2010, U.S.\$71.9 million of loan proceeds have been spent on this project. For water-borne transportation, Ukraine has four warm-water commercial ports, the largest of which is Feodosiya, and 2,175.7 km of inland river waterways.

Between 2004 and 2006, the EBRD agreed to lend Ukraine U.S.\$120 million to finance high-speed trains and €300 million for the reconstruction of the Kyiv-Chop highway. In August 2004, the EBRD and Ukraine's main passenger and freight carrier, Ukrzaliznytsia (the State Railway Transport Administration of Ukraine), signed an agreement for a U.S.\$120 million loan to finance the development of high-speed trains. In January 2009, Ukraine and the EBRD signed a U.S.\$62.5 million facility agreement for the railway car purchase project for Ukrainian railways; the project is for an aggregate amount of U.S.\$125.0 million.

In February 2005, the EBRD and Ukraine signed an agreement for extension of a second €100 million credit to repair part of the 824-kilometre long Kyiv-Chop highway, which connects Kyiv with Western Europe (a first agreement with the EBRD for the extension of €75 million loan on this project was signed in 2000). In December 2006, Ukraine and the EBRD entered into agreement extending a further €200 million loan for reconstruction of the Kyiv-Chop highway. In July 2007, Ukraine and the EIB entered into an agreement providing for a €200 million loan to finance reconstruction of the Kyiv-Chop highway jointly with the EBRD; in July 2009 this agreement came into force. As of 1 August 2010, 497 kilometres of the Kyiv-Chop highway have been repaired and put into operation. As at 1 August 2010, approximately €521.9 million has been spent on the project, including approximately €365.8 million in proceeds from the EBRD loans and approximately €156.1 million from the State Budget. The M06 highway is a part of TransEuropean corridors III and V, which connect central Ukraine with the EU member countries; its development is a priority for Ukraine.

In April 2009, Ukraine and the World Bank signed a U.S.\$400 million facility agreement for the Roads and Safety Improvement Project. Ukraine and the World Bank are also currently preparing to launch the Railway Modernisation Project involving a loan of U.S.\$500 million. In addition, in November 2007, Ukraine and the EBRD signed an agreement for extension of €26 million loan for the development of the Illichivsk sea trade port. See *“Public Debt-International Organisations”*.

On 2 July 2004, the Cabinet of Ministers issued a guarantee to Deutsche Bank AG as lender under a seven year, U.S.\$480 million credit facility, dated 29 June 2004, granted to Ukravtodor as borrower, for the purpose of financing the reconstruction of a segment of the Kyiv-Odessa highway. On 12 August 2005, the Cabinet of Ministers issued a guarantee to Deutsche Bank AG as lender under a 10-year, U.S.\$100 million credit facility, dated 17 August 2005, granted to Ukravtodor as borrower, to complete construction of the Kyiv-Odessa highway. On 7 July 2006, the Cabinet of Ministers issued a guarantee to Citibank N.A. London as lender under a 10-year, €279,886,635 credit facility extended to Ukravtodor to finance the construction, reconstruction and capital repair of roads in general use. On 30 August and 28 September 2007, the Cabinet of Ministers issued guarantees to Morgan Stanley International Bank Limited as lender under two 10-year credit facilities in the aggregate amount of U.S.\$930 million, which were extended to Ukravtodor for the purpose of financing the construction, reconstruction and capital repair of a number of roads. On 28 January 2009, the Cabinet of Ministers issued a guarantee to Credit Suisse International as lender under a credit facility in the aggregate amount of U.S.\$465 million extended to Ukravtodor. In addition, in November and December 2009, the Cabinet of Ministers availed (guaranteed) certain bills of exchange due 2012 in an aggregate amount of approximately UAH 1.6 billion issued by regional state road services as payment for supplied goods, works or services in connection with modernisation of roads in view of holding the Euro-

2012 Championship in Ukraine, liquidation of the consequences of certain natural disasters and other road construction, reconstruction and capital repair projects.

On 18 October 2004, the Cabinet of Ministers issued a guarantee to Deutsche Bank AG as lender under a seven-year, U.S.\$700 million credit facility, dated 19 October 2004, granted to the State Railway Transport Administration of Ukraine (Ukrzaliznytsya) as borrower, intended to finance the planning and construction of a railway and automobile bridge across the Dnipro river in the city of Kyiv.

The Government expects to direct significant capital investments into transport and road sector modernisation and development in view of holding the Euro-2012 Championship in Ukraine. The State Purpose Programme for the Preparation and Holding of the European Football Championship 2012 (the "Programme"), approved by the Government in February 2008 and revised in 2009 and 2010, sets forth a list of sport, transport, tourism and social infrastructure elements to be constructed or reconstructed in line with UEFA requirements. The aggregate amount of financing required for the purposes of the Programme implementation is UAH 142.8 billion, including UAH 35.3 billion to be financed out of the State Budget, UAH 30.2 billion to be financed through state support programmes, UAH 6.0 billion to be financed out of the local budgets and UAH 71.3 billion to be financed out of other sources. In particular, the aggregate amount of financing required under the Programme for the transport and road sector development (not including amounts of financing required for development of transport within cities (towns) and municipal roads) is UAH 77.1 billion, including UAH 29.0 billion to be financed out of the State Budget, UAH 19.2 billion to be financed through state support programmes, UAH 0.3 billion to be financed out of the local budgets and UAH 28.5 billion to be financed out of other sources.

Within the framework of preparations for the Euro-2012 Championship, the Government plans to develop Ukraine's road network and related transport by constructing and maintaining roads connecting the main cities of Ukraine involved in the Euro-2012 Championship and Ukrainian border checkpoints, as well as to implement a programme for comprehensive development of airports and railways. In 2008, as part of the implementation of the Programme as revised in 2010, UAH 5.5 billion were spent on transportation infrastructure projects, including UAH 1.2 billion on the reconstruction of a number of Ukrainian airports, UAH 2.5 billion on the reconstruction of Ukrainian railways and UAH 1.8 billion (including UAH 1.3 billion of State Budget funds) on the construction and maintenance of roads. In 2009, as part of the implementation of the Programme as revised in 2010, UAH 5.7 billion was spent on transportation infrastructure projects, including UAH 1.1 billion on the reconstruction of a number of Ukrainian airports, UAH 2.2 billion on the reconstruction of Ukrainian railways and UAH 2.4 billion (including UAH 1.4 billion of State Budget funds) on the construction and maintenance of roads.

Taking into account preparations for the Euro-2012 Championship, the Programme provides for approximately UAH 9.2 billion to be spent out of the State Budget for the development of the road and transport sector in 2010, while the aggregate amount of financing required under the Programme for such purposes for 2010 is approximately UAH 24.2 billion (not including amounts of financing required for development of transport within cities (towns) and municipal roads). As at 28 August 2010, the actual amount of financing under the Programme for the transport infrastructure projects was approximately UAH 5,973.5 million out of the State Budget, of which UAH 2,339.7 million was spent on the reconstruction of Ukrainian airports, UAH 500.0 million on the development of Ukrainian railways, UAH 3,053.8 million on the construction and maintenance of roads and UAH 80.0 million on the development of subways.

The Economic Reform Programme (see "*Action Programmes*") provides for implementation in 2010-2014 of a number of reforms in the transportation sector, including, among other things, abolishment of preferential cargo transportation tariffs for certain industries; gradual increase of transportation tariffs to economically reasonable level; restructuring of railway companies; privatisation of certain state-owned assets in the transportation sector; implementation of nationwide infrastructural projects financed both out of the State Budget and by the World Bank, EBRD and private investors; and increase of the State Budget financing for modernisation and development of transport infrastructure by 10 per cent. each year.

Privatisation

Ukraine began implementing a privatisation programme in 1992 with the objectives of increasing the private sector's share of the economy, generating foreign direct investment and contributing funds to the State Budget. From 1992 to 31 July 2010, Ukraine collected more than UAH 42 billion in privatisation receipts, with approximately UAH 36 billion collected during the course of 2003-2007. From 1992 to 31 July 2010, more than 124,600 objects were privatised, including approximately 28,500 objects initially in state ownership and approximately 96,100 objects initially in communal (municipal) ownership. In the seven months ended 31 July 2010, 124 objects initially owned by the State and 1,459 objects initially in communal (municipal) ownership were privatised.

Initially, the privatisation programme focused on the auction of small-scale enterprises (defined before 2000 as enterprises with a book value of fixed assets worth not more than UAH 170 million; after 2000, enterprises with up to 100 employees). According to figures provided by the SPF, approximately 105,200 small scale entities were privatised by 31 July 2010. As of the date of this Prospectus, small-scale privatisation has been nearly completed. In addition, Ukraine has been implementing a privatisation programme for medium to large scale enterprises. Between 1993 and 31 July 2010, approximately 11,200 entities were converted into joint-stock companies, and as of 31 July 2010 approximately 700 companies remain at least partially owned by the State.

The SPF administers the privatisation programme in Ukraine. In consultation with various ministries, the SPF identifies enterprises to be privatised each year. Once the Cabinet of Ministers approves the list of companies to be privatised, the SPF proceeds with the conversion of the enterprises into joint-stock companies and the sale to investors. Foreign and Ukrainian investors have equal rights in the privatisation processes, subject to certain exceptions, such as prohibitions on land sales and restrictions on companies located in off-shore zones (such as British Virgin Islands, Liberia and others) from participating in the privatisation of certain large assets.

Several bills governing the activities of the SPF were approved by Parliament throughout 2007-2009, but were vetoed by the President. At present, the activities of the SPF are governed by temporary regulations approved in 1992.

In September 2006, Parliament enacted a new law "On the Management of State-Owned Assets". The new law sets out the legal framework for the management of various state-owned assets, including state property transferred to state enterprises and state-owned shares in joint-stock and limited liability companies. The law also defines the powers of various state authorities, including the SPF, which is responsible for maintaining the Unified Register of State-Owned Assets. As of 31 July 2010, the Unified Register of State-Owned Assets included approximately 25,100 state-owned legal entities, 700 companies in the statutory funds of which the State has corporate rights, 591,600 real estate assets of state enterprises and organisations, and 444,400 state owned assets on the balance sheets of previously privatised or corporatised companies.

Certain laws prohibit the privatisation of particular enterprises in strategic sectors, including power generation, the military and mining, without the consent of the Cabinet of Ministers and, if privatisation of such enterprises involves foreign investments, the approval of Parliament. Furthermore, the State has the right to retain an ownership interest in such enterprises, enabling the State to block certain management decisions.

For 2007, target privatisation receipts were set at approximately UAH 10.6 billion, and actual privatisation receipts were only UAH 2,446.8 million (UAH 2,458.3 million was transferred to the general fund of the State Budget), 23.2 per cent. of the annual target. The largest privatisations that took place in 2007 include the sale of a 25.1 per cent. stake in OJSC "National Joint Stock Insurance Company "Oranta" for UAH 500.8 million and a 96.67 per cent. stake in the OJSC "Nikopol Pivdennotrubny Plant" for UAH 352.6 million. A significant shortfall in actual privatisation receipts as compared to the targets was due to the failure to privatise OJSC "Ukrtelecom", JSC "Odessa Port Plant" and six regional energy distribution companies.

The sale of the 99.52 per cent. shareholding in JSC "Odessa Port Plant" (with a nominal value of UAH 0.8 billion) was expected to take place in September 2007 with an initial sale price of UAH 2.5 billion. Sales

of shareholdings in six regional energy distribution companies were expected to take place in 2007 following the approval of the Concept for Privatisation of Objects of Power Industry. However, in September 2007, the President suspended the effectiveness of the resolutions of the Cabinet of Ministers of Ukraine permitting the sales of shareholdings in JSC “Odessa Port Plant” and the six regional energy distribution companies, and asked the Constitutional Court of Ukraine to opine on the constitutionality of these resolutions; the sales were cancelled in October 2007 and the Constitutional Court of Ukraine terminated review of the President’s applications in January 2008.

Privatisation of OJSC “Ukrtelecom” was initially planned to be divided into two stages. In the first stage, the SPF planned to sell five 1 per cent. shareholdings in OJSC “Ukrtelecom” during 2007. The total nominal value of these five 1 per cent. shareholdings was UAH 234.1 million and the estimated sale price was approximately UAH 1 billion. Several offerings of 1 per cent. stakes in OJSC “Ukrtelecom” made by the SPF on Ukrainian stock exchanges in the course of 2007 failed due to an absence of interest or due to court injunctions. As a result, as at 1 January 2008, only a 0.072 per cent. stake in OJSC “Ukrtelecom” was sold for UAH 15.5 million. In the second stage of the privatisation, the SPF initially expected the 37.86 per cent. shareholding in OJSC “Ukrtelecom” (with UAH 1.7 billion nominal value) to be offered for sale on international stock markets, with estimated sale price of approximately U.S.\$1 billion. However, the terms of this sale were not approved by the Cabinet of Ministers in 2007.

For 2008, target privatisation receipts were initially set at approximately UAH 8.9 billion. This target was reduced to UAH 607.1 million in December 2008. Actual privatisation receipts in 2008 were UAH 482.7 million, 79.4 per cent. of the revised annual target. A significant shortfall in actual privatisation receipts compared to the original targets was due to the failure to privatise OJSC “Ukrtelecom”, JSC “Odessa Port Plant” and six regional energy distribution companies.

The decision of the NSDC dated 15 February 2008, which was enacted by the Decree of the President dated 6 March 2008, instructed the Government not to permit the privatisation of companies in the fuel and energy, defence, transport, housing and other strategic sectors of the economy pending an approval of privatisation programmes governing privatisation of state-owned assets in such sectors. This decision also instructed the Government not to permit, pending an approval of the State Privatisation Programme, the privatisation of enterprises having strategic importance for the economy and safety of the state if this would result in the monopolisation of the respective markets.

The SPF initially contemplated to sell shareholdings in the six regional energy distribution companies at stock exchanges by 30 June 2008, however, in May 2008, pursuant to the decision of the NSDC dated 15 February 2008, the SPF cancelled the respective sales. In addition, in pursuance of the decision of the NSDC dated 15 February 2008, the SPF suspended the inclusion of five other large companies on the list of companies subject to sale in 2008. The sale of the 99.52 per cent. shareholding in JSC “Odessa Port Plant” (with a nominal value of UAH 0.8 billion) was expected to take place in May 2008 with an initial sale price of UAH 3.0 billion. However, in April 2008, pursuant to the decision of the NSDC dated 15 February 2008, the President suspended the effectiveness of the resolution of the Cabinet of Ministers of Ukraine approving the terms of the sale of the shareholding in JSC “Odessa Port Plant”, and asked the Constitutional Court of Ukraine to opine on the constitutionality of this resolution. The Constitutional Court of Ukraine terminated review of the President’s applications in November 2008. The terms of sale in 2008 of 67.79 per cent. shareholding in OJSC “Ukrtelecom” with a nominal value of approximately UAH 5.2 billion were not approved by the Government in 2008.

For 2009, target privatisation receipts were set at approximately UAH 8.5 billion and actual privatisation receipts were only UAH 814.9 million, or 9.6 per cent. of the annual target. A significant shortfall in actual privatisation receipts compared to the budgeted target was due to the failure to privatise a number of major assets planned for privatisation in 2009, including OJSC “Ukrtelecom”, JSC “Odessa Port Plant”, OJSC “Turboatom” and certain regional energy distribution and generating companies. Certain of such privatisations were either cancelled or significantly delayed in 2009 due to decrees of the President of Ukraine prohibiting or suspending these privatisations.

In 2009, the SPF resumed sales of the six regional energy distribution companies on Ukrainian stock exchanges, and in May 2009, shareholdings in two of these companies were sold for the aggregate amount

of UAH 421.3 million. Shareholdings in four other regional energy distribution companies with an aggregate nominal value of UAH 44.4 million were not sold in 2009. Shareholdings in an additional 14 regional energy distribution companies were also included in the list of planned privatisations for 2009. In order to sell the shares of these 14 companies, the shares should have been formally transferred to the management of the SPF; however, such transfers were not effected in 2009.

In accordance with the terms of sale of JSC “Odessa Port Plant” announced in July 2009, the sale of the 99.57 per cent. shareholding in the company was scheduled to take place during 2009 with an initial sale price of UAH 4.0 billion. On 17 September 2009, the President issued a decree suspending the Cabinet of Ministers’ authorisation of the sale of JSC “Odessa Port Plant” during 2009 and requested the Constitutional Court of Ukraine to opine on its constitutionality. On 14 October 2009, however, the Constitutional Court of Ukraine declined to open proceedings on the constitutionality of the authorisation. In addition, according to press reports, one or more Ukrainian courts have enjoined any actions aimed at privatising the company. Despite the President’s decree and the reported court actions, the privatisation auction took place on 29 September 2009. Three bidders submitted bids for the auction, with the highest bid being UAH 5.0 billion. However, the auction committee did not declare a winner of the auction and this sale was not consummated in 2009.

The terms of the sale of a 67.79 per cent. shareholding in OJSC “Ukrtelecom” with a nominal value of approximately UAH 5.2 billion were not approved by the Government in 2009.

For 2010, target privatisation receipts were initially set at UAH 10.0 billion, but were subsequently decreased in July 2010 to UAH 6.35 billion. In the seven months ended 31 July 2010, actual privatisation receipts were only UAH 410.8 million, or 6.5 per cent. of the annual target (as compared to actual privatisation receipts of UAH 566.0 million, or 6.7 per cent. of the annual target, for the seven months ended 31 July 2009). To ensure that UAH 6.35 billion target privatisation receipts are met in 2010, the SPF plans to offer for sale a number of objects, which should be attractive for investors and which do not require lengthy sale preparations, as well as to focus on the simplified sale of those shareholdings that were previously unsuccessfully offered for sale.

The largest privatisation planned by SPF for 2010 is OJSC “Ukrtelecom”. The SPF is preparing for sale in 2010 a 92.79 per cent. shareholding in OJSC “Ukrtelecom” with a nominal value of approximately UAH 4.3 billion and the starting price of UAH 10.5 billion. On 12 October 2010, the terms of this sale were approved by the Cabinet of Ministers of Ukraine and on 13 October 2010, the SPF announced that the bidding for this shareholding would take place on 28 December 2010.

Another sale that the SPF has scheduled for 2010 is a 76 per cent. shareholding in JSC HC Luganskteplovoy, the initial privatisation of which took place in 2007. The sale price of UAH 292.5 million realised for this shareholding in 2007 was below its originally estimated value, primarily because the court orders in litigation involving JSC HC Luganskteplovoy reduced its value. In November 2007, the privatisation of JSC HC Luganskteplovoy was declared invalid by a Ukrainian court, and on 29 September 2009, pursuant to a court order, the 76 per cent. shareholding in JSC HC Luganskteplovoy was transferred to the SPF. In March 2010, the SPF announced an auction for the reprivatisation of a 76 per cent. shareholding in JSC HC Luganskteplovoy with an initial sale price of UAH 400 million. The auction took place on 15 June 2010 and Bryanskiy Machine-Building Plant (Russia) was declared the winner with a bid price of UAH 410 million. Bryanskiy Machine-Building Plant is the same entity that purchased a 76 per cent. shareholding in JSC HC Luganskteplovoy in 2007, which purchase was subsequently rendered invalid. On 29 June 2010, Ukraine and Bryanskiy Machine-Building Plant signed a sale and purchase agreement relating to this shareholding, pursuant to which the buyer was to transfer the purchase price by 28 August 2010. As the buyer failed to make the relevant payment, on 7 October 2010, the SPF filed a claim with the Kyiv Commercial Court requesting the court to terminate the sale and purchase agreement and to require the buyer to pay penalties and a fine. On 22 October 2010, the Kyiv Commercial Court ruled to terminate the sale and purchase agreement and to require the buyer to pay penalties and a fine in the amount of UAH 84.2 million. In addition, on 30 July 2010, the Kyiv commercial court opened proceedings on the claim filed by Mantara Holdings Limited against the SPF and Bryanskiy Machine-Building Plant. The plaintiff, which was not admitted by the SPF for participation in the auction, seeks to challenge the results of the auction and

invalidate the sale and purchase agreement relating to the shareholding in JSC HC Luganskteplovoy. On 21 September 2010, the Kyiv commercial court decided to invalidate the sale and purchase agreement relating to the shareholding in JSC HC Luganskteplovoy, the judgment of the Kyiv commercial court having been appealed by the SPF and the buyer. As at 29 October 2010, it is unlikely that privatisation of HC Luganskteplovoy will be completed in 2010.

The SPF is also preparing for sale in 2010 shareholdings in four regional energy distribution companies with an aggregate nominal value of UAH 0.04 billion and potential sale price of UAH 0.5 billion. In June and July 2010, the SPF announced an auction for privatization of three regional energy distribution companies. As at 1 September 2010, the SPF had sold an 8.76 per cent. shareholding and 25.0 per cent. shareholding in two of these companies, with the aggregate sale proceeds of approximately UAH 145.0 million. The SPF plans to offer for sale by the end of 2010 a 25.0 per cent. shareholding in a third regional energy distribution company as well as another 16.24 per cent. shareholding in the company, 8.76 per cent. shareholding in which was sold earlier this year.

Privatisation of a number of state-owned companies remains restricted by decrees approved by the President of Ukraine in 2008. The SPF has submitted proposals to the Government with respect to lifting relevant restrictions. If the Government and the President uphold the SPF proposal, these additional assets, including, among others, JSC “Turboatom” and four energy generating companies, may be offered for sale in 2010.

In addition, in January 2005, a Law of Ukraine “On the Suspension of the Privatisation of Oil Refining Enterprises in Ukraine” entered into force suspending privatisation of the relevant enterprises until the adoption of the State Privatisation Programme and the Law of Ukraine on particular features of the privatisation of the oil-refining industry.

The SPF has prepared a draft law on the privatisation programme for 2007-2009, which was approved by Parliament in June 2007. However, it was not signed by the President and did not become effective. In 2008, the SPF prepared a draft privatisation programme for 2008-2012, which was approved by Parliament in a second reading on 18 February 2009, but rejected on 19 May 2009.

The Economic Reform Programme (see “– *Action Programmes*”) provides for implementation of the followings main measures in the area of privatisation and state-owned property management:

- at the first stage that should be completed by the end of 2010, Ukraine should, among other things, approve a law governing the activities of the SPF and programmes for the reform and development of certain strategic sectors of economy, which should outline the terms for privatisation of state-owned assets in such sectors. Ukraine should also permit privatisation of a number of state-owned assets, privatisation of which is currently prohibited;
- at the second stage that should be completed by the end of 2012, Ukraine should continue privatisation of companies in the strategic sectors of economy (including privatisation of banks recapitalised by the Government); and
- at the third stage that should be completed by the end of 2014, Ukraine should largely complete privatisation process, and change the focus of the SPF activities from privatisation to accounting and management of state-owned assets. Ukraine should also focus on attraction of private investment into assets that remain controlled by the State.

In July 2010, in furtherance of the Economic Reform Programme, the SPF prepared a draft law on the privatisation programme for 2010-2014 as well as proposed amendments to privatisation legislation aimed at supporting implementation of the privatisation programme and increasing the efficiency of privatisation process.

State bodies have examined a number of privatisations that took place in previous years under irregular conditions and without full transparency. A Special Parliamentary Control Commission on Privatisation supervises compliance with privatisation laws. If the Commission determines that such laws have been breached, it may request that the authorised privatisation bodies, including the SPF, annul illegal orders or unwind illegal actions. If these sales are found to have taken place on illegally favourable terms, the

Government may decide to petition the appropriate courts to annul the sales of the companies concerned and to refund the original purchase price to the owners. As at 15 July 2010, 125 privatisations had been challenged in court by the SPF, though the large majority of these challenges have been for noncompliance with the terms of the relevant purchase and sale agreements rather than for illegally favourable terms. As of 15 July 2010, 292 items had been returned to State ownership, and 153 had been resold, for total proceeds of UAH 97.5 million. As at 1 September 2010, the largest privatisation being challenged was the privatisation of a stake in SJSHC Black Sea Shipbuilding Plant with a nominal amount of UAH 116.6 million.

Inter-enterprise Arrears

The level of inter-enterprise arrears (debt which is due but unpaid between businesses) is significant and has been increasing for several years. Inter-enterprise payments in arrears (not part of the Budget) are estimated to be much larger than wage arrears. Inter-enterprise net debt (current debts payable minus current debts receivable) increased from UAH 78.0 billion as at 31 December 2006 to UAH 94.2 billion as at 31 December 2007, followed by a decrease to UAH 92.8 billion as at 31 December 2008 and an increase to UAH 110.9 billion as at 30 September 2009. Overdue inter-enterprise net debt (overdue current debts payable minus overdue current debts receivable) increased from approximately UAH 12.3 billion as at 31 December 2006 to UAH 20.6 billion as at 31 December 2007 and to UAH 21.6 billion as at 31 December 2008 and decreased to UAH 19.4 billion as at 30 September 2009. These inter-enterprise arrears threaten the solvency of many Ukrainian companies, reduce potential budgetary revenues and represent an impediment to economic growth.

On 29 November 2001, a temporary moratorium was introduced on the forced sale of property of State enterprises and enterprises owned more than 25 per cent. by the State pending settlement of related legal issues. In February 2004, the bankruptcy law was amended by introducing a moratorium on the bankruptcy of mining enterprises in which the State holds an interest greater than 25 per cent. These amendments provided that bankruptcy proceedings of such enterprises could be initiated not earlier than one year after the beginning of the privatisation of such enterprises. In January 2007, the moratorium was extended to 1 January 2010 and in December 2009, the moratorium was prolonged to 1 January 2013. In June 2005, a Law of Ukraine “On Measures Aimed at Ensuring Stable Operation of Fuel and Energy Sector Enterprises” was enacted providing for various indebtedness repayment procedures (including indebtedness restructurings and write-offs). The law also provides for a register to be established of fuel and energy enterprises that participate in indebtedness repayment procedures and provides that a court may refuse to initiate bankruptcy proceedings and suspend relevant judicial and enforcement proceedings against companies so registered. In December 2008, the moratorium was extended to 1 January 2011.

Environment

To a large extent, the significant environmental problems facing Ukraine stem from the period when it was a part of the Soviet Union. Historically, major problems have included waste accumulation (including toxic waste), water and atmosphere pollution, contamination from the Chernobyl incident, and the closure of mines. Despite the general economic decline witnessed in the 1990s, levels of air and water pollution still remain high largely as a result of significant depreciation of equipment and development of resource consuming and polluting sectors of the economy. For example, according to data of the State Statistics Committee of Ukraine, in 2008 and 2009, approximately 7.2 and 6.4 million tonnes, respectively, of harmful substances were released into the atmosphere by stationary and mobile sources of pollution. These figures represent a 2.3 per cent. decrease in 2008 compared to 2007 and 10.6 per cent. decrease in 2009 compared to 2008. Out of approximately 6.4 million tonnes of harmful substances estimated to have been released into the atmosphere in 2009, approximately 3.9 million tonnes were released by enterprises and approximately 2.5 million tonnes were released by mobile sources, such as cars, railways and river and aviation transport. In the six months ended 30 June 2010, approximately 2.0 million tonnes of harmful substances were released into the atmosphere by stationary sources of pollution, representing a 5.7 per cent. increase compared to the six months ended 30 June 2009. During 2009, approximately 1.8 billion cubic metres of polluted run-off water drained into Ukrainian waters, as compared to approximately 2.7 billion tonnes in 2008. In addition, the total volume of accumulated waste is estimated at the level of approximately 35 billion tonnes, including two billion tonnes of hazardous waste.

While the closure of the last working reactor at Chernobyl in December 2000 helped to address safety concerns of the international community, concerns regarding radiation and contamination in the surrounding territory continue to remain high. In addition, the closure eliminated approximately 5 per cent. of Ukraine's energy generating capacity, thus creating electricity shortages in certain regions that had to be compensated for with additional power from fossil fuel plants. In 2007, 2008 and 2009, the amount of the State Budget expenditures on eliminating the consequences of the Chernobyl incident was UAH 528.0 million, UAH 586.6 million and UAH 512.9 million, respectively. In the seven months ended 31 July 2010, the amount of the State Budget expenditures on eliminating the consequences of the Chernobyl incident was UAH 349.0 million, while the amount budgeted for the full year 2010 is UAH 776.9 million. In general, pursuant to official estimates, the economic losses of Ukraine associated with this incident alone will amount to U.S.\$130 billion.

Although Ukraine has established a legal framework for environmental protection that is generally consistent with standards accepted by EU member states and set forth in various international treaties, it does not have sufficient resources to fully comply with these standards. Environmental protection is financed by the State Budget, local budgets, funds of enterprises and organisations, voluntary contributions and other funds. In total, UAH 11.1 billion were spent on environmental protection in 2009, including current expenditures on the operation and maintenance of environmental facilities and measures in the amount of UAH 8.0 billion, investments into fixed assets in the amount of UAH 2.5 billion and expenditures on capital repairs in the amount of UAH 0.6 billion. Out of these amounts, 20.5 per cent. of capital investments and 4.1 per cent. of current expenditures were financed out of the State Budget and local budgets, while 76.5 per cent. of capital investments and 95.8 per cent. of current expenditures were financed by enterprises and organisations.

To fund more effective measures to protect the environment in Ukraine, environmental protection funds have been allocated each year within the State Budget, the budget of the Crimea Autonomous Republic, oblast budgets, the Kyiv and Sevastopol city budgets and local (village, township and city) budgets for the purpose of remedying environmental pollution and damage caused by violations of environmental protection legislation as a result of economic or other activities. In 2007 and 2008, receipts to these funds were UAH 1,107.4 million and UAH 1,182.0 million, respectively, including receipts to the State Fund for Environmental Protection in the amount of UAH 719.8 million and UAH 768.3 million, respectively. In 2009 and the seven months ended 31 July 2010, receipts to these funds were UAH 1,150.4 million and UAH 731.1 million, of which receipts to the State Fund for Environmental Protection amounted to UAH 345.1 million and UAH 219.3 million, respectively. The Ministry of Environment intends to streamline the organisation of these funds and to utilise resources from other sources (including grants and loans from foreign sources).

To increase financial resources for the implementation of environmental protection measures, Ukraine is reviewing alternative sources of funding, including introducing market-oriented instruments (for example, reduction of prices for loans from commercial banks for remedial environmental actions through reimbursement of interest paid) and reforming the system of environmental protection funds.

Ukraine enacted the law "On Environmental Protection" in 1991 and, thereafter, promulgated a number of regulations and guidelines with respect to environmental matters. Furthermore, as of 1 June 2010, Ukraine is a party to 22 international conventions, 15 protocols, and 152 bilateral agreements regarding the environment. On 4 February 2004, Ukraine ratified the Kyoto Protocol to the UN Framework Convention on Climate Change. The aggregate assigned amount units, or AAUs, available for sale by Ukraine for the period of effectiveness of the Kyoto undertakings amount to approximately one billion tonnes of carbon dioxide equivalent. In 2009 and 2010, Ukraine sold AAUs to Japan and Spain. The State received €320.0 million from these sales, and another €150.0 million are expected to be received from Japan in 2010, subject to Ukraine's use of funds for the specified purpose. In addition, Ukraine expects to sell AAUs to other countries in the future, including a possible sale to Italy and further sales to Spain.

In 2009 — 2010, Ukraine has continued financing a number of measures to implement the Kyoto Protocol, and has started a number of new projects including development of the National Plan on allocation of permits on greenhouse gas emissions. In April 2007, the Government established a new central executive authority, the National Ecological Investments Agency. The principal tasks of this Agency include implementation of

the mechanisms of the UN Framework Convention on Climate Change and the Kyoto Protocol, including the implementation of environmental protection projects.

On 24 June 2004, the Law of Ukraine “On Environmental Audit” was enacted, providing a framework for environmental auditors to audit enterprises and to provide their suggestions with regard to the elimination of breaches of environmental legislation and taking relevant remedial environmental measures. The Law “On Environmental Audit” provides for both voluntary and mandatory audits. Mandatory environmental audits must be performed in such cases as, among others, bankruptcy or privatisation of state-owned companies, establishment of joint ventures on the basis of state-owned assets and long-term leases of state-owned assets. In 2007, Regulations on Maintaining the Register of Environmental Auditors and Legal Entities Authorised to Perform Environmental Audit, as well as Regulations on Certification of Environmental Auditors, approved by the order of the Ministry of Environment of Ukraine, were enacted to implement the environmental audit system. In addition, the Ministry of Environment created a special Scientific Expert Group and Commission for Environmental Auditors Certification, which is tasked with review and analysis of draft regulatory acts developed further to the Law of Ukraine “On Environmental Audit”, as well as holding qualification exams and issuing environmental auditor certificates. Currently, 102 environmental auditors are certified in Ukraine and 55 legal entities are entered in the register of legal entities authorised to carry out environmental audits.

In October 2007, the Government approved the Concept of National Environmental Policy of Ukraine through 2020. Among the goals of this Concept is tightening environmental liability for users and polluters of natural resources, as well as rationalising the use of natural resources. One of the underlying principles of the Concept is that prevention of damage to the environment should be a priority task and that comprehensive environmental implications should be taken into account while making any governmental decisions. The Concept also provides for the implementation of an efficient system of public information on environmental protection and sustainable development issues.

State control is exercised over management and protection of land, environmental and radiation safety, protection and management of territories and objects of natural reserve funds, management and disposal of waste products (other than radioactive waste products), hazardous chemical substances, pesticides and agrochemicals, the management, protection and use of the ecological network, as well as over compliance with environmental security standards. In addition, the State exercises geological and geodesic monitoring and control. However, the damages paid for the breach of the environmental legislation tend to be low, which reduces their deterrent value and is inadequate compared to the sums required to remedy the consequences of the breach of environmental legislation. Beginning on 1 January 2007, damages paid for breaches of environmental legislation (pollution of the environment) are to be automatically indexed to the consumer price inflation index for the preceding year. As a result of indexing to the CPI, these damages are expected to increase in line with the inflation rate.

THE LABOUR MARKET

Wages

The average monthly wage has steadily increased over the last several years. For example, between 2005 and 2009, the average monthly nominal wage increased by approximately 135 per cent. In 2007, the average monthly wage increased by 29.7 per cent. compared to the level in 2006 to UAH 1,351.1 and, in 2008, it further increased by 33.7 per cent. compared to the level in 2007 to UAH 1,806.3. In 2009, the average monthly wage as calculated by the State Statistics Committee of Ukraine was UAH 1,905.9, an increase of 5.5 per cent. compared to the level in 2008. In the six months ended 30 June 2010, the average monthly wage was UAH 2,110.0, an increase of approximately 18.7 per cent. compared to the same period in 2009. The Government expects that for the full year 2010 the average monthly nominal wage will increase by 17.8 per cent. primarily due to renewed economic growth. According to the index of real wages, the average monthly real wage increased by 6.3 per cent. in 2008 compared to 2007 and decreased by 9.2 per cent. in 2009 compared to 2008. However, the average monthly real wage increased by 8.6 per cent. in the six months ended 30 June 2010 compared to the same period in 2009.

The minimum wage in Ukraine is determined by Parliament on the basis of the Government's recommendation. The Government bases its recommendation on a number of factors, including the forecasts of key macro-economic indices for the relevant period as well as the then current average wage and employment level. The 2009 State Budget Law initially provided for an increase of the minimum monthly wage to UAH 625, UAH 630, UAH 650 and UAH 669 from 1 April, 1 July, 1 October and 1 December 2009, respectively. On 20 October 2009, Parliament adopted a new law which provided for an increase of the minimum monthly wage and monthly subsistence level for people capable of working to UAH 744 from 1 November 2009 and to UAH 869 from 1 January 2010, respectively, to be followed by a number of further increases up to UAH 922 from 1 December 2010.

In addition, the 2010 State Budget Law provides for a minimum hourly wage in the amount of UAH 5.20, UAH 5.29, UAH 5.32, UAH 5.43 and UAH 5.52 from 1 January, 1 April, 1 July, 1 October and 1 December 2010, respectively.

The 2008 State Budget Law, as amended, provided for an increase of expenditures on the payment of salaries to employees of budgetary institutions by UAH 23.8 billion as compared to 2007. In particular, salaries of highly-qualified employees of budgetary institutions (teachers, doctors and certain others) increased on average by 30 per cent. in 2008 as compared to 2007. The 2009 State Budget Law provided for an increase of expenditures on the payment of salaries to employees of budgetary institutions by UAH 7.9 billion as compared to 2008. The 2010 State Budget Law provides for expenditures on the payment of salaries to employees of budgetary institutions in the amount of UAH 116.9 billion, an increase of UAH 21.7 billion as compared to the plan for 2009.

In 2009, the average monthly wage in the private sector was UAH 972.0, while the average monthly wage in the public sector was UAH 2,314.0. Average wages in the private sector are only slightly higher than the minimum wage. This average is depressed, however, by very low wages in the agricultural sector and, most likely, by the failure to report private sector wages earned in the "shadow economy".

Historically, it was common for Ukrainian businesses and certain governmental authorities to fail to pay salaries and pensions on time. In August 1999, wage arrears reached UAH 7.2 billion. As a result of the promulgation of a Presidential decree on the acceleration of wage arrears repayments, between May 2001 and December 2006, wage arrears to employees of all enterprises, institutions and organisations (both operating and bankrupt) were reduced to UAH 806.4 million. During 2007, such wage arrears further decreased by UAH 137.7 million, or 17.1 per cent., and on 31 December 2007 wage arrears of all enterprises (including operating, non-operating and bankrupt enterprises) amounted to UAH 668.7 million. However, during 2008, such wage arrears increased by UAH 520.0 million, or 77.8 per cent., and on 31 December 2008 wage arrears of all enterprises (including operating, non-operating and bankrupt enterprises) amounted to UAH 1,188.7 million. During 2009, such wage arrears further increased by UAH 284.7 million, or 23.9 per cent., and on 31 December 2009 wage arrears of all enterprises (including operating, non-operating and bankrupt enterprises) amounted to UAH 1,473.3 million.

As of 1 August 2010, wage arrears of all enterprises (including operating, non-operating and bankrupt enterprises) amounted to UAH 1,550.1 million, or an increase by UAH 76.7 million or 5.2 per cent. compared to the wage arrears recorded at 1 January 2010. As of 1 August 2010, out of the total amount of wage arrears, UAH 529.9 million or 34.2 per cent. are arrears of enterprises, which are subject to bankruptcy or readjustment proceedings, UAH 67.6 million or 4.4 per cent. are arrears of non-operating enterprises and UAH 952.6 million or 61.4 per cent. are arrears of operating enterprises. The reasons for the increase in wage arrears during 2009 and the seven months ended 31 July 2010 include significant decline in industrial production, reduced profitability of companies, significant amounts of overdue accounts payable and accounts receivable, inefficiency of state property management and inefficient implementation of restructuring, readjustment and bankruptcy procedures.

As at 1 August 2010, wage arrears of operating enterprises in the public sector (i.e., both arrears due from State and local budgets and those due from State-owned and municipal enterprises) were UAH 289.1 million. Of the public sector wage arrears as at 1 August 2010, wages of state-owned operating enterprises were UAH 156.2 million, an increase of UAH 54.2 million, or 53.2 per cent., since 31 December 2009. Of the public sector wage arrears as at 1 August 2010, wages of municipally-owned operating enterprises were UAH 132.9 million, an increase of UAH 25.1 million, or approximately 23.3 per cent., since 31 December 2009. Of the public sector wage arrears as at 1 August 2010, wages of operating enterprises payable out of the State Budget were UAH 12.0 million, a decrease of UAH 4.7 million, or approximately 28.1 per cent., since 31 December 2009. As at 1 August 2010, wage arrears of operating enterprises in the private sector were UAH 663.5 million. The failure to pay full salaries on a regular basis and the failure of salaries and benefits generally to keep up with the rapidly increasing cost of living have led in the past, and could lead in the future, to labour and social unrest. In addition, companies unable to pay their wage arrears may be subject to sanctions or liquidation.

Before the economic crises, steady increases in wages have improved household income. In particular, in 2008, nominal household income increased by 37.4 per cent., available household income increased by 37.2 per cent. and real available household income (adjusted by the CPI) increased by 9.6 per cent., each as compared to 2007. In 2009, as a result of the economic downturn, nominal household income increased by only 6.2 per cent. and available household income increased by 6.0 per cent., while real available household income (adjusted by the CPI) decreased by 8.5 per cent., each as compared to 2008.

Unemployment

The State Statistics Committee calculates unemployment monthly on the basis of all persons between the ages of 15 and 70 capable of working, using the International Labour Organisation's (the "ILO") internationally accepted methodology of household surveys. According to the ILO methodology, the average unemployment level in Ukraine was 6.4 per cent. in 2007, 6.4 per cent. in 2008, 8.8 per cent. in 2009 and 9.0 per cent. in the three months ended 31 March 2010.

In 2007, the employed population in Ukraine was 20.9 million persons and, during 2008, it increased by 0.3 per cent. to 21.0 million persons as compared to 2007. However, in 2009, the employed population in Ukraine decreased by 3.7 per cent. to 20.2 million persons, which was followed by a further decrease to 20.1 million persons in the three months ended 31 March 2010. The Government expects that for the full year 2010 the employed population in Ukraine will increase to 20.4 million persons. For 2007 there was a decrease in the unemployed population to 1.42 million persons, which was followed by an increase up to 1.43 million in 2008, 1.96 million persons in 2009 and 1.98 million persons in the three months ended 31 March 2010.

In 2009, the average unemployment rate, as determined by the ILO methodology, was 8.8 per cent. overall, with 7.2 per cent. in rural areas and 9.6 per cent. in urban areas, in each case as determined by the ILO methodology. In the three months ended 31 March 2010, the average unemployment rate, as determined by the ILO methodology, was 9.0 per cent. overall. According to the State Programme for Economic and Social Development of Ukraine for 2010, approved by Parliament on 20 May 2010, the Government expects that the average unemployment rate in Ukraine will decrease to 8.1 per cent. in 2010.

In July 2006, the Government approved the National Employment Programme until 2009, which provided for the annual creation of one million new jobs, enrichment of the professional and educational potential of the population as well as “de-shadowing”, that is, bringing jobs that currently form part of the shadow economy into the legitimate labour market. Recently, the Ministry of Labour has prepared a draft of the Principles of the State Employment Policy for 2010-2011, which is expected to be approved by the Government. The policy will focus on such measures as, among other things, minimisation of the adverse impact of the financial and economic downturn on the Ukrainian labour market; promotion of new jobs creation at the level of 600 thousand new jobs in each of 2010 and 2011; promotion of individual entrepreneurship and self-employment, in particular, for young people and disabled; de-shadowing and regulation of labour migration.

During 2009, 2.4 million people joined the workforce (i.e., the number of persons working or seeking work) and 3.0 million left the workforce, a decrease of approximately 824 thousand joining and a decrease of approximately 681 thousand leaving the workforce, as compared to 2008. During the six months ended 30 June 2010, approximately 1,255.0 thousand people joined the workforce, an increase of approximately 88 thousand, as compared to the same period in 2009, and approximately 1,316.0 thousand people left the workforce, a decrease of approximately 205.0 thousand as compared to the same period in 2009. During 2009, approximately 748 thousand new jobs were created, which fell below the annual target set by the Government by 25.2 per cent. In the six months ended 30 June 2010, approximately 434 thousand new jobs were created. Approximately three quarters and 80 per cent. of newly-created jobs in 2009 and the six months ended 30 June 2010, respectively, were created by individual entrepreneurs and self-employed persons. In 2009 and the six months ended 30 June 2010, de-shadowing accounted for approximately 40 per cent. and 45 per cent. of newly-created jobs, respectively.

In 2009 and the seven months ended 31 July 2010, respectively, 2.1 million and 1.2 million Ukrainian citizens took advantage of job placement and other services offered by the National Employment Service. Of this number, in 2009 and the seven months ended 31 July 2010, respectively, 157 thousand and 122 thousand persons were engaged in skills training, 241 thousand and 194 thousand took part in public works and 703 thousand and 450 thousand obtained employment with the assistance of the National Employment Service. The level of employment obtained with the assistance of the National Employment Service decreased to 32.8 per cent. in 2009 as compared to 43.3 per cent. in 2008. In the seven months ended 31 July 2010, the level of employment obtained with the assistance of the National Employment Service amounted to 37.3 per cent. as compared to 27.8 per cent. in the seven months ended 31 July 2009.

The global financial and economic downturn in recent years has adversely affected the Ukrainian labour market. In particular, since October 2008, the number of persons unemployed, employed part-time or on involuntary unpaid leave has increased significantly, especially in such sectors as the metallurgical industry, construction and the chemical industry as well as hotels, restaurants, trade and repair services. In response, Parliament enacted an anti-crisis law aimed at preventing the improper dismissal of employees and providing social support to employees made redundant. These measures contributed to a reduction in the number of dismissals as well as the number of persons employed part-time or on involuntary unpaid leave. In particular, in the six months ended 30 June 2010, 41 thousand employees were dismissed from their positions as compared to 107 thousand dismissed in the same period of 2009. Moreover, in July 2010, the number of persons employed part-time and on involuntary unpaid leave was 571 thousand and 52 thousand persons, respectively, a significant decrease compared to 1,096 thousand and 348 thousand persons in July 2009, respectively. In addition, as at 1 August 2010, approximately five citizens registered with the National Employment Service competed to fill each vacant position offered by the Service, as compared to nine citizens per vacant position as at 1 August 2009.

The Government believes that measures to prevent deterioration in the labour market should be its priority policy. These measures include continued efforts to create new jobs and improve the services offered by the National Employment Service. The Government also expects that a restatement of the Labour Code of Ukraine, passed by Parliament in a first reading on 20 May 2008, will be enacted and will provide for more adequate regulation of labour relations at various levels. The Labour Code has not yet been passed by Parliament in a second reading.

Pensions, Unemployment Benefits and Social Insurance

The Ukrainian social insurance system consists of pensions, unemployment benefits and other social benefits, including those related to temporary incapacity, work related injury, illness and pregnancy, childbirth and child-care benefits and funeral payment assistance. As a part of Ukraine's ongoing transition, the Government is currently working with the World Bank and the IMF in connection with the restructuring of the social insurance system. Such restructuring includes the introduction of a new system of collecting and accounting for a single social contribution under a mandatory state social insurance scheme as well as the further development of the Ukrainian pension system. Priority goals in developing the pension system include the introduction of a defined-contribution system of state pension insurance and development of non-state pension provisions. Despite success in the development of non-state provisions, a defined contribution system has not yet been implemented.

The Economic Reform Programme (see "*Economy of Ukraine – Action Programmes*") provides for implementation of the followings main measures to reform Ukrainian labour market and social insurance system:

- at the first stage, which should be completed by the end of 2010, Ukraine should, among other things, limit a maximum amount of pension; prepare for an introduction of the defined contribution system of state pension insurance; and establish a 5-year moratorium on introduction of new types of social benefits and extension of the list of persons entitled to existing types of social benefits;
- at the second stage, which should be completed by the end of 2012, Ukraine should create incentives for later retirement; cancel certain benefits for early retirees; gradually bring retirement age for men and women to the same level; and introduce a single social contribution, a defined contribution system for state pension insurance, and mandatory corporate pension schemes for funding certain types of pensions; and
- at the third stage, which should be completed by the end of 2014, Ukraine should continue diversification of non-state pension insurance schemes, implementation of joint investment programmes and monitoring and audit of social support programmes.

In addition, on 8 July 2010, Parliament approved a law that introduces, with effect from 1 January 2011, a single social contribution to replace the various social duties that are currently levied. It is expected that the Pension Fund will be an agency charged with accounting and collecting this single social contribution.

Ukraine has established a Uniform State Automated Register of Persons Entitled to Benefits. This Register records information on military and labour-service veterans, certain categories of pensioners, persons harmed by the Chernobyl disaster and other categories of individuals entitled to benefits. Social security authorities use the Register to verify information received from entities that render services to entitled persons and to make payments for such services. As of 1 August 2010, this Register contained information on approximately 13.3 million persons.

In 2007, social insurance and pension expenditures amounted to UAH 113.5 billion, or 15.9 per cent. of GDP, with pension expenditures amounting to UAH 98.6 billion, and in 2008, social insurance and pension expenditures amounted to UAH 165.9 billion, or 17.5 per cent. of GDP, of which pension expenditures amounted to UAH 150.3 billion. In 2009, social insurance and pension expenditures amounted to UAH 183.4 billion, or 20.0 per cent. of GDP, of which pension expenditures amounted to UAH 165.7 billion. In the seven months ended 31 July 2010, social insurance and pension expenditures amounted to UAH 118.8 billion of which pension expenditures represent UAH 108.5 billion. For the full year 2010, social insurance and pension expenditures are budgeted at UAH 211.1 billion, of which pension expenditures represent UAH 192.3 billion.

Pensions

In Ukraine, a basic pension is available to individuals who are retired and have made contributions to the pension fund for at least five years. The current retirement age in Ukraine is 55 for women and 60 for men. The average pension stood at UAH 751.38 per month, UAH 898.36 per month, UAH 999.02 and UAH

1,103.6 per month on 1 January 2008, 2009, 2010 and 1 July 2010, respectively. The minimum retirement pension was increased in several stages from UAH 544.0 as of 1 July 2008 to UAH 604.4 as of 1 November 2009. According to the 2010 State Budget Law, from 1 January 2010, the minimum retirement pension for retired persons amounted to UAH 695 and from 1 April and 1 July 2010 it increased to UAH 706 and UAH 709, respectively. It is expected that the minimum retirement pension for retired persons will be increased from 1 October 2010 and 1 December 2010 to UAH 723 and UAH 734, respectively.

The pension payment increases during 2005-2008 are attributable to an increase in the subsistence level, which is the basis for calculating the minimum pension. In 2007 and 2008, the Pension Fund did not have a deficit, which was partially due to allocation of certain funds that were formerly part of the Temporary Disability Social Insurance Fund for pension purposes in 2008, but also evidenced growth in the pension fund revenues. However, in December 2008, the Ministry of Finance extended a UAH 4.7 billion loan to the Pension Fund to finance an advance payment of pensions in January 2009 and other temporary cash gaps. In accordance with the Law on the State Budget for 2009, the Pension Fund was budgeted to have a UAH 13.7 billion deficit in 2009 that was expected to be covered out of the State Budget. In addition, during 2009, the Ministry of Finance extended a UAH 17.4 billion loan to the Pension Fund to finance temporary cash gaps. In accordance with the Law on the State Budget for 2010, the Pension Fund is budgeted to have a UAH 26.6 billion deficit in 2010 that is expected to be covered out of the State Budget. In the seven months ended 31 July 2010, the Ministry of Finance extended loans in the amount of UAH 20.8 billion to the Pension Fund to finance temporary cash gaps. During this period, approximately UAH 23.0 billion in loans previously extended to the Pension Fund were repaid.

The Government expects that large numbers of people born in the years of population increase following World War II will be retiring in coming years. In order to mitigate the effects of a substantial increase of pension expenditures on the State Budget, the Government intends to change the pay-as-you-go system of mandatory state pension insurance and to introduce a defined contribution system of state pension insurance, as discussed above.

On 1 January 2004, the Laws of Ukraine “On Mandatory State Pension Insurance” and “On Non-State Pension Provision” came into force providing for the creation of a three-tier system of pension insurance in Ukraine. The first level is a pay-as-you-go system of mandatory state pension insurance; the second level is a defined contribution system of state pension insurance; and the third level is non-state pension provisions. The “pay-as-you-go” system of mandatory state pension insurance provides that pensions paid out of the Pension Fund to current retirees are funded by contributions of current employers and employees. Therefore, the viability of such a system depends largely on demographic factors, especially on the ratio of the employed to total population in the country. In 2010, the pay-as-you-go system is funded by employer contributions set at 33.2 per cent. of an employee’s salary, with exceptions for certain categories of employees (disabled employees, aviation crew and others), and by a special 2 per cent. tax paid by the employee. The defined contribution system envisages the creation of a special accumulation fund composed of individual pension accounts to which employees may transfer up to 7 per cent. of their salaries. Contributions accumulated in such a fund would be invested and paid out together with the investment income to the employees upon retirement, in addition to pensions paid out of the Pension Fund.

In addition, these laws allow differentiation among pension amounts in an attempt to improve pension provision for citizens, such differentiation being based on the duration of the employment period, during which the person was making contributions to the Pension Fund, and the amount of the previous wages (income). Citizens who already receive a pension are entitled to its recalculation pursuant to the provisions of the law enacted in January 2004. On average, the recalculation has resulted in pension increases by more than five times to date as compared to 2004. Periods of labour prior to the enactment of the law are credited towards seniority in determining the pension amounts to be paid under the laws enacted in January 2004.

Since 1 January 2004, approximately 12.5 million pensioners have had their pensions recalculated based on the principles of pension payment established in 2004. Although the introduction of the pension reform has resulted in the increase of the ratio of average pension to average wages from 20 per cent. to 54 per cent., a sufficient level of pension provision will only be attainable through the efficient operation of the pension insurance system at all levels. The first and third levels of pension insurance have been operating from 1 January 2004, while the second level, a defined contribution system of state pension insurance remains to be

developed. The establishment of a successful system of non-state pension provision is viewed as a “testing stage” before development of the defined contribution system and hence a prerequisite for implementation of the second level of pension reform.

As of 1 January 2010, the State Commission on the Regulation of Financial Services Markets had information on 108 non-state pension funds. As at 31 December 2008 and 31 December 2009, non-state pension funds held total assets of UAH 612.2 million and UAH 857.9 million, respectively, and had approximately 483 thousand and 497 thousand individual participants, respectively. As at 31 March 2010, non-state pension funds held total assets of UAH 939 million and had approximately 499 thousand individual participants. The number of individual non-state pension fund participants and the amount of non-state pension fund assets has been increasing. See “*The Banking System and Securities and Financial Services Markets in Ukraine — The Financial Services Market in Ukraine*”.

Unemployment Benefits

Mandatory unemployment insurance was introduced on 1 January 2001 and is currently funded through a 1.6 per cent. payroll tax paid by the employer to the Employment Fund and a 0.6 per cent. tax paid by the employee. It is expected that starting from 1 January 2011 such payroll tax will be replaced by a single social contribution. Self employed individuals and individual entrepreneurs may participate in the unemployment insurance scheme on a voluntary basis. Both insured and uninsured persons are entitled to benefits and social services, provided that they are registered as unemployed with the State Employment Service. Benefits are currently payable out of the Unemployment Fund. Insured unemployed persons’ benefits depend on their past wages, insurance period and the reasons for dismissal from the last workplace. Uninsured persons have the right to unemployment benefits in the minimum amount.

During 2009 and through 31 May 2010, the minimum unemployment benefit was UAH 360 for uninsured unemployed persons and for insured long-term unemployed persons. During this period, for insured unemployed persons the minimum unemployment benefit was UAH 500. The minimum unemployment benefit for uninsured unemployed persons and for insured long-term unemployed persons was increased to UAH 400, UAH 430 and UAH 480 from 1 June, 1 July and 1 September 2010, respectively, and is expected to be further increased to UAH 490 and UAH 500 from 1 October and 1 December 2010. The minimum unemployment benefit for insured unemployed persons was increased to UAH 550, UAH 600 and UAH 665 from 1 June, 1 July and 1 September 2010, respectively, and is expected to be further increased to UAH 680 and UAH 700 from 1 October and 1 December 2010, however, it is capped at the level of an average monthly wage in a relevant region for the previous month.

In December 2009, the average unemployment benefit was UAH 655.6 per month, an increase of 14.8 per cent. as compared to December 2008. In July 2010, the average unemployment benefit was UAH 735.5 per month, an increase of 16.4 per cent. compared to July 2009.

In accordance with Ukrainian employment laws, any unemployed person who worked for at least 26 weeks within the 12 months preceding unemployment is entitled to benefits, depending on such person’s past employment period. In particular, one is entitled to benefits equivalent to 70 per cent. of one’s average monthly salary if the employment period was more than ten years, 60 per cent. if it was between six and 10 years, 55 per cent. if it was between two and six years and 50 per cent. if it was less than two years. An unemployed person is entitled to 100 per cent. of such benefits for the first 90 calendar days, 80 per cent. for the subsequent 90 calendar days and 70 per cent. for the following months.

The major categories of social services rendered to the unemployed include professional training or re-training, assistance in finding employment, including through subsidies to the employers for creation of additional workplaces and financing of public works, as well as informational and consulting services related to employment.

Social Insurance and Benefits

In addition to pensions and unemployment benefits, social insurance consists of public support for persons who are temporarily incapable of working or have suffered labour-related injury or illness, as well as pregnancy, childbirth and child-care benefits. Furthermore, social benefits include subsidies to low income

families, cash subsidies for the purchase of fuel and gas, subsidies for the payment of housing and communal services, as well as assistance for funeral and health improvement (rehabilitation).

In 2009, the average monthly insurance payment to employees injured at work as a result of accidents and professional illnesses was UAH 782.0, an increase of 4.5 per cent. as compared to 2008. In the six months ended 30 June 2010, the average monthly insurance payment to employees injured at work as a result of accidents and professional illnesses was UAH 841.7, an increase of 5.0 per cent. as compared to the same period in 2009. From 1 March 2008 and 1 March 2009, the amount of monthly insurance payments to employees injured at work as a result of accidents and professional illnesses was increased by 12.5 per cent. and 6.3 per cent., respectively; however, no increase of such insurance payments took place in March 2010.

Since 2007, childbirth benefits and child care benefits to insured persons are funded out of the State Budget rather than out of the Temporary Disability Social Insurance Fund. In 2008, 2009 and 2010, the childbirth benefit is UAH 12,240 for the first child in a family (currently equivalent to 16 times the monthly subsistence level for a child up to six years old), UAH 25,000 for a second child and UAH 50,000 for each additional child. A portion of these benefits is payable at birth, with the remainder payable in instalments over the period ranging from 12 to 36 months thereafter. The aggregate amount of childbirth benefits was UAH 8,444.8 million and UAH 5,725.3 million in 2009 and the seven months ended 31 July 2010, respectively. The total amount of childbirth benefit budgeted in the State Budget for 2010 is UAH 11,111.0 million. Child-care benefits are available until a child is three years old. Certain additional benefits are available to children under guardianship and to single mothers. The minimum child care benefit is currently UAH 130.0 per month. In 2009 and the seven months ended 31 July 2010, the average amount of monthly child care benefit was UAH 170.9 and UAH 283.2, respectively. At each of 1 January 2010 and 1 August 2010, approximately 1.3 million persons were recipients of such benefits. The aggregate amount of these benefits was approximately UAH 2,506.2 million and UAH 2,504.0 million in 2009 and the seven months ended 31 July 2010, respectively.

In 2009 and during the seven months ended 31 July 2010, the average amount of monthly subsidies to low income families was UAH 551.5 and UAH 847.8, respectively. As of 1 January 2010 and 1 August 2010, approximately 81 thousand and 77 thousand families, respectively, were recipients of such subsidies, which totalled approximately UAH 705.4 million and UAH 480.1 million in 2009 and the seven months ended 31 July 2010, respectively.

In 2009 and during the seven months ended 31 July 2010, the average amount of cash subsidy for the purchase of fuel and gas was UAH 372.3 and UAH 333.8, respectively. In 2009 and the seven months ended 31 July 2010, approximately 256 thousand and 78 thousand families, respectively, were recipients of such subsidies. In 2009 and during the seven months ended 31 July 2010, the average amount of subsidy for the payment of housing and communal services was UAH 156.5 and UAH 91.3, respectively. As at 1 January 2010 and 1 August 2010, approximately 869 thousand and 230 thousand families, respectively, were recipients of such subsidies.

As of 1 August 2010, social benefit arrears for subsidies to families with children and low income subsidies had been completely eliminated. As of 1 August 2010, total arrears for cash subsidies for the purchase of fuel and gas amounted to UAH 9.5 million.

EXTERNAL SECTOR

Balance of Payments

Ukraine had a current account surplus from 1999 until 2005. In 2006, the current account balance had a deficit of U.S.\$1.6 billion and the overall current account deficit represented 1.5 per cent. of GDP. In 2007, due to significant increase in volumes of imports, the current account deficit increased to 3.7 per cent. of GDP or U.S.\$5.3 billion.

In 2008, the current account deficit increased to U.S.\$12.8 billion or 7.0 per cent. of GDP, mainly due to the increase of the external goods trade deficit to U.S.\$16.1 billion and the increase of the revenue deficit to U.S.\$1.5 billion. Notwithstanding the consequences of the global financial downturn, which significantly affected Ukraine's economy in the fourth quarter of 2008, the positive economic dynamics of the first three quarters resulted in high rates of growth of almost all current account items for the full year 2008.

In 2009, reductions in external demand and world market prices due to the global financial and economic downturn resulted in a significant decrease of revenues from the exports of goods and services by 36.6 per cent. At the same time, reduction in domestic demand, lack of external financing as well as a significant devaluation of hryvnia in late 2008 resulted in a 43.7 per cent. decline in imports. Consequently, in 2009, the current account deficit significantly decreased to U.S.\$1.8 billion (or 1.5 per cent. of GDP) as compared to U.S.\$12.8 billion (or 7.0 per cent. of GDP) in 2008.

In 2008, the financial account surplus amounted to U.S.\$9.7 billion, a decrease of 35.0 per cent. as compared to U.S.\$14.7 billion recorded in 2007. The reduction in the financial account surplus resulted from a capital outflow of U.S.\$5.8 billion during the fourth quarter of 2008. This was the first time such a capital outflow occurred since early 2006 and was caused by the global financial downturn. The net capital outflow resulted from the decrease in the long-term funding inflow recorded concurrently with high rates of short term loan and foreign currency physical cash outflow from the banking system.

In 2009, the financial account deficit amounted to U.S.\$11.9 billion as compared to the financial account surplus of U.S.\$9.7 billion in 2008. The financial account deficit in 2009 was largely due to limited global liquidity, instability of global and domestic capital markets and significant volumes of debt that had been accumulated by the private sector during previous years and matured in 2009. In particular, the financial account balance was affected by net repayment in 2009 of U.S.\$9.1 billion of external debt accumulated by private and public sectors before the global financial downturn as well as by a significant decrease in inflows of foreign direct investments in 2009.

According to the preliminary data published by the NBU, for the seven months ended 31 July 2010, the current account surplus was U.S.\$24.0 million (as compared to a current account deficit of U.S.\$1.1 billion for the same period in 2009). The current account surplus for the seven months ended 31 July 2010 was largely due to the increase in surplus of trade in services (by more than two times to U.S.\$2.4 billion, as compared to a surplus of trade in services of U.S.\$1.1 billion for the seven months ended 31 July 2009) and the reduction in the revenues deficit (by 26 per cent. to U.S.\$1.0 billion as compared to a deficit of U.S.\$1.4 billion for the seven months ended 31 July 2009).

For the seven months ended 31 July 2010, Ukraine had a financial account surplus of U.S.\$5.1 billion (as compared to a U.S.\$7.1 billion deficit for the seven months ended 31 July 2009). The financial account surplus was largely attributable to the reduction in net repayments by the private sector under the external borrowings, the Government's borrowing under the U.S.\$2.0 billion facility entered into in June 2010, and a gradual increase in confidence in hryvnia and the banking system resulting in the deceleration of accumulation of cash outside banks. At the same time, the net inflow of foreign direct investments remained at a relatively low level.

The NBU expects that in the second half of 2010 the recovery of Ukrainian economy will continue against the background of a global economic recovery and gradual revival of commodity and capital markets. As at 31 July 2010, the NBU expected the financial account balance to be positive in 2010, with the surplus amounting to U.S.\$1.6 billion (as compared to a U.S.\$11.9 billion deficit in 2009). The current account

deficit was expected to decrease in 2010 as compared to 2009 (to U.S.\$0.9 billion) due to intensified renewal of external demand and gradual expansion of domestic demand. The overall surplus of the balance of payments in 2010 is expected to be in the amount of approximately U.S.\$700.0 million.

The following table sets out Ukraine's balance of payments for the periods shown:

	Year ended 31 December			Seven months ended 31 July	
	2007	2008	2009	2009	2010 ⁽¹⁾
	<i>(in U.S.\$ millions)</i>				
Current account	(5,272)	(12,763)	(1,801)	(1,102)	24
Goods and services (balance)	(8,152)	(14,350)	(2,022)	(1,228)	(580)
Export of goods and services	64,001	85,612	54,253	28,449	36,552
Import of goods and services	(72,153)	(99,962)	(56,275)	(29,677)	(37,132)
Goods (balance)	(10,572)	(16,091)	(4,655)	(2,309)	(3,016)
Services (balance)	2,420	1,741	2,633	1,081	2,436
Income (balance)	(659)	(1,540)	(2,440)	(1,401)	(1,036)
Current transfers (balance)	3,539(2)	3,127	2,661	1,527	1,640
Capital and financial account	14,693	9,700	(11,925)	(7,111)	5,146
Capital account	3	5	595	520	194
Direct investment (balance)	9,218	9,903	4,654	2,478	2,547
Portfolio investment (stock capital)	715	398	(63)	26	(11)
Loans and bonds	23,077	12,412	(9,139)	(5,338)	1,234
Medium- and long-term loans	18,210	13,443	(4,665)	(2,328)	771
Short-term loans	4,867	(1,031)	(1,031)	(3,036)	463
Other capital	(18,320)	(13,018)	(7,972)	(4,797)	1,182
including foreign currency cash					
outside banks	(13,518)	(12,897)	(9,713)	(5,478)	(1,498)
Overall balance	9,421	(3,063)	(13,726)	(8,213)	5,170
Financing	(9,421)	3,063	13,726	8,213	(5,170)
Reserves assets ⁽³⁾	(8,980)	(1,080)	5,654	2,169	(5,170)
Loans from IMF (net)	(441)	4,143	1,228	1,246	–
IMF loan to Government of Ukraine....	–	–	4,798	–	–
SDR	–	–	2,046	–	–

Notes:

- (1) According to preliminary estimates of the NBU.
- (2) Includes payments from Germany and Austria as compensation for World War II victims in the aggregate amount of U.S.\$5 million in 2007.
- (3) Numbers in parentheses represent an increase in reserves.

Source: NBU

International Trade

Prior to independence, commerce was centrally controlled from Moscow, and the integrated trade system of the USSR meant that the majority of Ukraine's cross-border trade was with other Soviet republics. Figures are difficult to obtain, but by 1989 Ukraine tended to import energy and raw materials while exporting machinery, metals and chemicals. About 80 per cent. of both imports and exports are estimated to have been with non-Ukrainian Soviet markets.

Following independence, the large increases in the price of Ukraine's energy imports were offset by decreases in import volumes, with the result that nominal import flows remained broadly the same. The price of energy, in particular of oil (delivered by Russia) and of gas (delivered by Russia and, in certain periods, Turkmenistan), increased from intra-Soviet to world market levels. The immediate impact on the economy was less severe than it might have been because part of the price was credited to Ukraine by its suppliers, especially Russia's Gazprom.

During the period from 1992 through 2009, Ukrainian exports of goods and services increased from 24.0 per cent. to 34.3 per cent. of GDP, and imports increased from 22.0 per cent. to 38.5 per cent. of GDP. The increasing proportion of exports and imports between 1992 and 2009 as a percentage of GDP reflects, among other factors, the gradual integration of Ukraine into the world economy.

In 2007, goods and services export volumes increased by 27.4 per cent., while goods and services import volumes increased by 35.4 per cent., each as compared to 2006. In 2007, the external trade turnover increased by 31.5 per cent. as compared to 2006 and was U.S.\$136.2 billion and the external trade deficit was U.S.\$8.2 billion (as compared to U.S.\$3.1 billion deficit in 2006). As a percentage of GDP, in 2007, Ukrainian exports of goods and services decreased to 45.3 per cent. of GDP and imports increased to 50.6 per cent. of GDP. The growth of goods export volumes in 2007 was primarily attributable to stable demand and favourable price conditions in external markets for metal, chemical products and certain agricultural products as well as to growth in demand for machinery products. The growth of goods imports volumes in 2007 was largely attributable to intensification of investment demand, the growth of real household incomes and consumer lending and sharp increases in energy prices.

In 2008, goods and services import volumes grew by 38.5 per cent. as compared to the 33.8 per cent. growth of goods and services export volumes. As a result, the external trade deficit increased to U.S.\$14.4 billion in 2008 compared to U.S.\$8.2 billion in 2007, with the main increase in the deficit occurring in the first half of 2008 and being largely attributable to increased household income, stimulated by significant social expenditures made by the Government, dynamic development of consumer lending and the strengthening of the hryvnia exchange rate against the U.S. dollar in this period. High prices for traditional export products, such as ferrous metallurgical products, positively affected the external trade balance in the middle of 2008.

Despite the economic downturn at the end of 2008, goods export volumes grew by 35.9 per cent. in that year as compared to 2007 and amounted to U.S.\$67.7 billion, or 37.6 per cent. of GDP in 2008. The growth of export volumes in goods in 2008 was primarily attributable to increases in that year in the value of exports of metallurgical products by 32.9 per cent. (accounting for a 38.3 per cent. share of the total goods export volume growth), agricultural products by 73.4 per cent. (accounting for 25.7 per cent. of goods export growth) and machinery products by 28.6 per cent. (accounting for 13.6 per cent. of goods export growth), respectively.

In 2008, volumes of imported goods increased by 38.7 per cent. to U.S.\$83.8 billion (46.6 per cent. of GDP). This growth was primarily attributable to an increase in domestic demand, as well as to increased world prices for energy, raw materials and other materials recorded in the first half of 2008. The growth of imported goods volumes in 2008 was primarily attributable to the increase in value of imports of mineral products by 50.1 per cent. (accounting for a 32.7 per cent. share of total goods import volume growth), machinery by 34.8 per cent. (29.4 per cent. of the goods import volume growth) and chemical industry products by 32.4 per cent. (12.5 per cent. of the goods import volume growth), respectively.

In 2009, volumes of exported goods and services were U.S.\$54.3 billion (or 46.1 per cent. of GDP), a decrease of 36.6 per cent., or U.S.\$31.4 billion, compared to 2008. Volumes of imported goods and services in 2009 were U.S.\$56.3 billion (or 48.1 per cent. of GDP), a decrease by 43.7 per cent. (or by U.S.\$43.7 billion) as compared to 2008. As a result, the external trade deficit decreased to U.S.\$2.0 billion in 2009 compared to U.S.\$14.4 billion in 2008.

In 2009, the goods trade deficit decreased to U.S.\$4.7 billion (U.S.\$16.1 billion in 2008). Though in aggregate in 2009 the commodities turnover was 43.6 per cent. less than in 2008, it kept increasing during the year (after a significant decrease in the first quarter of 2009) and in the fourth quarter it was by only 14.2 per cent. less than in the respective period of 2008. While the rate of recovery for exports of goods was faster than that for the imports of goods, the balance of trade in goods remained negative in 2009 largely due to the significant increase of prices for imported gas.

Exports of goods, in aggregate 40.3 per cent. lower in 2009 than in 2008, kept increasing during 2009. This improvement was due to a gradual renewal of external demand and a stabilisation of prices for Ukrainian exports after their sharp decline in the last quarter of 2008 and first quarter of 2009. In 2009, the largest decline was recorded in exports of ferrous metal products (by 55.4 per cent.), chemical industry products (by 48.6 per cent.) and mineral products (by 44.6 per cent.).

In 2009, the aggregate volumes of imported goods amounted to U.S.\$45.0 billion, a decrease by 46.2 per cent. as compared to 2008. A sharp decline in imports was recorded in the first quarter of 2009. Starting in the second quarter of 2009, imports increased by an average of 14.3 per cent. per quarter due to a gradual recovery of Ukrainian economy and a relative stabilisation of the hryvnia exchange rate. In 2009, the largest declines in value of imports were recorded for machinery and metallurgical products, at 66.0 per cent. and 58.1 per cent., respectively. Imports of mineral products decreased by 35.5 per cent. largely due to reductions in value volumes of oil and oil refinery products of 33.8 per cent. and 54.8 per cent., respectively. Imports of chemical products and agricultural products decreased by 28.0 per cent. and 23.5 per cent., respectively.

For the seven months ended 31 July 2010, volumes of exported goods and services amounted to U.S.\$36.6 billion, an increase of 32.6 per cent. (or U.S.\$8.1 billion) compared to the corresponding period in 2009. The increase was largely attributable to an increase in physical export volumes and export prices due to a gradual recovery of the global economy and stabilisation of conditions in global commodity markets, as compared to 2009. The increases in the value of exports of ferrous metals by 1.5 times, machinery by 39.8 per cent. and fuel and energy products by 2 times (including an increase in the value of exports of oil products by 3.1 times) were the main contributors to the total goods exports volume growth in the seven months ended 31 July 2010 (as compared to the same period in 2009).

For the seven months ended 31 July 2010, volumes of imported goods and services amounted to U.S.\$37.1 billion, an increase of 32.4 per cent. (or U.S.\$7.5 billion) as compared to the corresponding period in 2009. This increase was largely attributable to an increase in the imports value volumes of energy resources by 37.5 per cent. caused by the oil price growth. The value of imports of chemical industry products, machinery and ferrous metals increased by approximately 30.2 per cent., 33.3 per cent. and 45.2 per cent., respectively, for the seven months ended 31 July 2010, as compared to the same period in 2009.

The NBU expects that, for the full year 2010, volumes of goods exports and imports will increase by approximately 23.9 per cent. and 23.7 per cent., respectively, as a result of renewed external and domestic demand and positive price dynamics. The export of goods is expected to increase to up to U.S.\$50.0 billion due to GDP growth in Ukraine's major trade partners and price advantages caused by hryvnia devaluation in 2009. Import of goods is expected by the NBU to increase to up to U.S.\$55.7 billion as a result of the gradual recovery of the Ukrainian economy and further increases in prices for imported natural gas and oil. In 2010, the goods trade deficit is expected by the NBU to increase to U.S.\$5.7 billion (as compared to U.S.\$4.7 billion in 2009) and the services trade surplus is expected to increase to U.S.\$4.1 billion (as compared to U.S.\$2.6 billion in 2009) largely due to an increase of natural gas transit charges.

An open trade regime is being codified in a number of trade agreements. Ukraine applied to join the WTO in 1993. Within the framework of the WTO accession process, between 2005 and 2007, 49 laws were enacted (including, for example, laws relating to customs and excise, standards and compliance assessment, foreign currency settlements, insurance, intellectual property protection and the taxation of agricultural producers) with the intention of significantly reducing or eliminating the differentiation among rates of import duties on agricultural, industrial and consumer goods. On 5 February 2008, Ukraine's accession package was considered and approved by the WTO General Council and on the same day the President of Ukraine and the Director General of the WTO signed the Protocol of Ukraine's Accession to the WTO. The law of Ukraine ratifying the Protocol was passed by Parliament on 10 April 2008 and signed by the President on 16 April 2008. On 16 May 2008, upon completion of internal WTO procedures, Ukraine became the 152nd member state of the World Trade Organization. WTO membership is expected to provide better access for Ukraine's exports to western and other markets.

On 1 February 1996, an Interim Trade Agreement with the EU was signed. The Partnership and Co-operation Agreement, which was signed with the EU in 1994, came into force in 1998 and remains in place to date. In previous years, Ukraine and the EU entered into agreements relating to trade in steel products and trade in textile products providing for special quotas, licensing and other restrictions, which automatically terminated upon Ukraine's accession to the WTO. Upon the cancellation of the quotas, Ukraine became subject to the EU import surveillance system for steel products, which remained in effect until 31 December 2009.

As at 21 August 2010, various countries were conducting a total of five anti-dumping investigations and seven special investigations against Ukrainian products. The investigations were primarily conducted in

relation to Ukrainian metallurgical products (including rolled metal and rollers), confectionary, mechanical fixtures, absorbent carbon, beer and other goods. Out of the total of twelve investigations conducted against Ukrainian goods worldwide, Russia is conducting one anti-dumping investigation in relation to steel roller and three special investigations in relation to Ukrainian mechanical fixtures, hard boiling confectionery and absorbent carbon. Of the remaining investigations, Pakistan, Moldova, Indonesia and Persian Gulf countries are conducting one each, while Kazakhstan and Belarus are conducting two investigations each. As at 21 August 2010, as a result of previous investigations, there were 30 anti-dumping restrictive measures and three special restrictive measures applied worldwide against Ukrainian products (mainly chemical and metallurgical products), including, among others, seven anti-dumping measures imposed by the United States, six anti-dumping measures imposed by the EU and four anti-dumping measures imposed by Mexico. The Russian Federation imposed two special restrictive measures against Ukrainian non-corrosive pipes and glass grid, and three anti-dumping restrictive measures against Ukrainian pipes, polyamide technical fibre and mechanical fixtures. In addition, as at 21 August 2010, three reviews of previously imposed anti-dumping measures were in progress (the Russian Federation, Thailand and Mexico). See also “*Political Framework — International Relations — Foreign Countries*”.

As at 21 August 2010, Ukraine was conducting six investigations, including two anti-dumping investigations against poultry imported from the United States and Brazil and pneumatic tyres imported from Belarus; and four special investigations against flat glass, mineral fertilisers, ferroalloys and refrigerating equipment imported from any country. As at 21 August 2010, as a result of previous investigations, Ukraine applied 16 restrictive measures against imports of various products (including 14 anti-dumping measures and 2 special measures).

Tariffs

Tariffs in Ukraine are imposed based on both value and quantity. Ukraine adopted a revised law on tariffs on 5 April 2001, which provides that any changes to import duties or introductions of new import duties may only be enacted by Parliament. On 1 January 2004, a new Customs Code relating to customs procedures in the areas of air, rail and sea transportation came into effect. The Government aims, in the long run, to harmonise its tariffs with those of the EU countries.

In recent years, the customs and tariff policy of Ukraine has been pursued in light of the negotiation process on Ukraine’s accession to the WTO. As a result of these negotiations, the Consolidated Tariff Offer set the aggregate level of tariff protection at 6.28 per cent. (the final binding level agreed in connection with accession to the WTO), while the current level of tariff protection in Ukraine amounts to 5.4 per cent.

Parliament enacted a number of laws providing for improvement of intellectual property protection during goods transfer over Ukraine’s customs border and changes in the laws governing foreign economic activities including setting forth a list of goods, exports and imports of which could be prohibited, and a list of measures which Ukraine may undertake in response to discriminatory or non-amicable actions of other states, customs or economic unions against Ukraine. Such laws also provide for the establishment of a tariff quota on imports of raw cane sugar, reduction of the export duties on live cattle, leather and ferrous, alloy and non ferrous metal scrap and semi-finished products thereof. The majority of these laws became effective upon Ukraine’s accession to the WTO. Thus, Ukraine’s accession to the WTO has resulted in a reduction of tariff rates. However, to offset adverse consequences of this reduction, transition periods have been established for certain sensitive products, including fish and alcoholic beverages. It is expected by the Government that by 2013 Ukraine will complete the process of bringing its tariff rates in line with the WTO requirements.

Composition of Trade

Since independence, Ukraine’s trade has been gradually re-oriented towards raw materials. This reorientation reflects in part the quality and quantity of Ukraine’s natural resources, which include large reserves of coal, high-grade iron ore, manganese, titanium and magnesium. These resources have formed the basis for the growth of heavy industry since the late nineteenth century.

In 2007, 2008, 2009 and the six months ended 30 June 2010, ferrous and non-ferrous metals and their products accounted for approximately 42.1 per cent., 41.2 per cent., 32.3 per cent. and 36.3 per cent., respectively, of export value, and the combined trade surplus on these items was U.S.\$16.0 billion, U.S.\$21.2 billion, U.S.\$10.1 billion and U.S.\$6.7 billion, respectively. Chemicals accounted for a further 10.2 per cent., 9.0 per cent., 7.7 per cent. and 7.6 per cent. of exports in 2007, 2008, 2009 and the six months ended 30 June 2010, respectively. In 2007 and 2008, an increase in the export value of ferrous and nonferrous metals, as well as of chemical products, was due to an improvement of external market conditions in comparison with the beginning of the year, including an increase in world prices for ferrous metals and chemical products, respectively. The decrease in the export value of ferrous and nonferrous metals, as well as of chemical products in 2009 was due to a deterioration in the market conditions generally and decreased world prices for such products. In the six months ended 30 June 2010, such prices increased as compared to the same period in 2009.

Agricultural products accounted for a further 12.8 per cent., 16.2 per cent., 24.0 per cent. and 18.3 per cent. of exports in 2007, 2008, 2009 and the six months ended 30 June 2010, respectively. The increased exports of agricultural and food processing products in 2007 and 2008 were due to a productive harvest of the traditionally exported agricultural products and increased demand for such products in their respective markets. The decrease in the exports of agricultural and food processing products in 2009 was due to a decrease in global demand for such products. In the six months ended 30 June 2010, demand for agricultural products returned which resulted in an increase of their exports.

In addition, machinery and equipment accounted for a further 10.1 per cent., 9.5 per cent., 12.6 per cent. and 11.2 per cent. of exports in 2007, 2008, 2009 and the six months ended 30 June 2010, respectively. In 2007, the volume of machinery exports increased by 49.5 per cent. as compared to 2006, contributing to a recovery in the economy in that year. In 2008, the volume of machinery exports increased by 27.4 per cent. as compared to 2007. In 2009, the volume of machinery exports decreased by 20.9 per cent. as compared to 2008 due to reduced liquidity, demand and production in external markets, as well as due to a decrease in global prices for machinery. In the six months ended 30 June 2010, the volume of machinery exports increased by 24.7 per cent. as compared to the same period in 2009 due to intensification of investment activities and increased demand in external markets, as well as due to last year's low comparative basis. Fuel and energy product exports have also decreased as suspension of operation of several oil refinery plants in 2007, 2008 and 2009 resulted in a decrease in oil-refinery volumes and reduction in export volumes of oil-refinery products. Since July 2005, there have been practically no export supplies of natural gas.

Strong concentration was also evident on the import side, where the largest item in 2007, 2008, 2009 and the six months ended 30 June 2010 were fuel and energy products (representing 26.3 per cent., 26.7 per cent., 32.2 per cent. and 32.2 per cent. of imports, respectively). Machinery and equipment also account for a significant share of Ukrainian imports (representing 17.5 per cent., 15.6 per cent., 13.8 per cent. and 12.8 per cent. of imports, respectively). The figures relating to imports of fuel and energy products reflect the energy intensity of the Ukrainian economy, resulting in a deficit in energy trade of approximately U.S.\$13.3 billion in 2007, U.S.\$18.7 billion in 2008, U.S.\$12.5 billion in 2009 and U.S.\$6.7 billion in the six months ended 30 June 2010. Increased import volumes of gas and coal and increased gas and oil prices produced higher total imports in 2007 and 2008. The significant changes in the terms of energy resources trade in early 2008 and early 2009 were the main reason for the deficit in trade of goods and services in 2008 and 2009. Notwithstanding an increase in prices for energy resources in 2010 as compared to 2009, the surplus in trade in goods and services amounted to U.S.\$400.5 million in the six months ended 30 June 2010.

Energy-intensive production was encouraged in the Soviet economy by the artificially low price of energy resources and by an incentive system that encouraged the wasteful use of economic inputs. Depletion of domestic energy resources (especially coal) and the orientation of much of industry towards the use of natural gas (another legacy from the Soviet period) have made Ukraine increasingly dependent on imported energy, although some products are imported for the purpose of re-export. The Government is trying to mitigate this situation by re-orienting Ukraine's energy needs towards locally available sources and away from costly imported gas.

The following table sets out exports from Ukraine by major commodity group and as a percentage of total exports for the periods shown:

	Year ended 31 December					Six months ended 30 June				
	2007		2008		2009	2009		2010		
	<i>(in U.S.\$ millions and %)⁽¹⁾</i>									
Fuel and Energy Products	2,630.2	5.3	4,109.2	6.1	2,130.8	5.4	737.7	4.3	1,587.0	6.9
Machinery and Equipment	4,977.1	10.1	6,341.1	9.5	5,013.5	12.6	2,074.6	12.0	2,587.2	11.2
Wood and Paper Products	1,595.2	3.3	1,675.6	2.5	1,471.9	3.7	655.2	3.8	815.1	3.6
Chemical Related Products	5,047.5	10.2	6,043.0	9.0	3,078.4	7.7	1,377.5	8.0	1,768.3	7.6
Agriculture Products	6,287.0	12.8	10,837.6	16.2	9,514.9	24.0	4,156.2	24.0	4,246.7	18.3
Ferrous Metals and their Products	19,645.6	39.9	26,487.7	39.6	12,198.4	30.7	5,577.1	32.2	8,019.2	34.7
Non-Ferrous Metals and their Products	1,131.0	2.2	1,106.4	1.6	617.3	1.6	264.1	1.6	369.6	1.6
Mineral Products	1,645.1	3.3	2,936.8	4.4	1,769.3	4.5	715.2	4.1	1,231.5	5.4
Textiles and shoes	1,393.4	2.3	1,162.7	1.8	857.5	2.2	395.7	2.3	416.7	1.8
Other	4,944.0	10.6	6,267.1	9.3	3,043.7	7.6	1,346.6	7.7	2,056.9	8.9
Total	49,296.1	100.0	66,967.3	100.0	39,695.7	100.0	17,299.9	100.0	23,098.2	100.0

Note:

(1) Percentages may not add up to 100.0 because of rounding.

Source: State Committee of Statistics; International Trade Bulletin

The following table sets out imports to Ukraine by major commodity group and as a percentage of total imports for the periods shown:

	Year ended 31 December					Six months ended 30 June				
	2007		2008		2009	2009		2010		
	<i>(in U.S.\$ millions and %)⁽¹⁾</i>									
Fuel and Energy Products	15,923.0	26.3	22,832.0	26.7	14,638.7	32.2	6,540.7	33.1	8,238.6	32.2
Machinery and Equipment	10,578.6	17.5	13,379.8	15.6	6,254.6	13.8	2,501.3	12.7	3,267.2	12.8
Wood and Paper Products	1,897.5	3.1	2,381.0	2.7	1,654.6	3.6	688.1	3.5	870.6	3.4
Chemical Related Products	8,730.0	14.4	11,435.7	13.3	7,983.1	17.6	3,349.5	17.0	4,360.4	17.0
Agriculture Products	4,111.5	6.7	6,456.6	7.5	4,936.0	10.9	2,279.4	11.5	2,674.6	10.4
Ferrous Metals and their Products	3,257.3	5.4	4,732.4	5.6	1,737.3	3.9	735.5	3.7	1,138.3	4.4
Non-Ferrous Metals and their Products	1,485.8	2.4	1,657.7	1.9	939.2	2.0	401.0	2.0	530.1	2.1
Mineral Products	1,296.2	2.1	2,609.3	3.0	1,056.4	2.3	435.7	2.2	831.0	3.2
Textiles and shoes	1,704.9	2.9	2,630.3	3.1	1,703.4	3.7	792.0	4.1	991.1	3.9
Other	11,633.2	19.2	17,420.5	20.6	4,529.8	10.0	2,043.1	10.2	2,711.2	10.6
Total	60,618.0	100.0	85,535.3	100.0	45,433.1	100.0	19,766.3	100.0	25,613.1	100.0

Note:

(1) Percentages may not add up to 100.0 because of rounding.

Source: State Committee of Statistics; International Trade Bulletin

Direction of Trade

The structure of Ukraine's trade with the CIS is determined by its need to import a large proportion of its energy requirements, especially from Russia (with which Ukraine runs large trade deficits) or from countries that transport energy exports through Russia. The need to import large quantities of energy products explains the fact that the CIS countries remain the main suppliers of Ukraine's imports, accounting for 42.0 per cent. of total goods imports in 2007, 39.0 per cent. in 2008, 43.3 per cent. in 2009 and 43.9 per cent. in the six months ended 30 June 2010. Of this amount, imports from Russia alone accounted for 27.8 per cent. in 2007, 22.7 per cent. in 2008, 29.1 per cent. in 2009 and 36.7 per cent. in the six months ended 30 June 2010.

The CIS countries also remain Ukraine's main export destinations, accounting for 36.7 per cent. of Ukraine's exports in 2007, 34.6 per cent. in 2008, 33.9 per cent. in 2009 and 35.0 per cent. for the six months ended 30 June 2010, of which exports to Russia accounted for 25.7 per cent. of total exports of goods in 2007, 23.5 per cent. in 2008, 21.4 per cent. in 2009 and 24.8 per cent. for the six months ended 30 June 2010. A large share of Ukraine's receipts for services exports comprises transit charges for oil, gas, ammonia and electricity from Russia, which made up approximately 22.1 per cent. of total services exports in 2007, 18.5 per cent. in 2008, 21.5 per cent. in 2009 and 32.8 per cent. in the six months ended 30 June 2010. Exports of goods to Russia increased by 46.4 per cent. in 2007 and by 24.2 per cent. in 2008, but decreased by 46.1 per cent. in 2009, followed by an increase of 65.4 per cent. in the six months ended 30 June 2010 as compared to the corresponding period in 2009. The significant decrease of goods exports to Russia in 2009 was primarily caused by reductions in exports of machinery by 2.1 times, metallurgical products by 2.3 times and agricultural and food products by 1.4 times, respectively, each as compared to 2008. Increase of goods exports to Russia in the six months ended 30 June 2010 was largely due to an increase in exports of machinery, metallurgical products, agricultural and food products and oil and oil refinery products by 1.8 times, 1.7 times, 1.4 times and 5.3 times, respectively.

Exports of goods to Asia increased by 27.3 per cent. in 2007 and by 47.1 per cent. in 2008, but decreased by 23.6 per cent. in 2009, followed by an increase by 16.1 per cent. in the six months ended 30 June 2010 as compared to the corresponding period in 2009. Exports of goods to the EU increased by 15.1 per cent. in 2007 and 30.3 per cent. in 2008, decreased by 47.6 per cent. in 2009, and increased by 45.3 per cent. in the six months ended 30 June 2010, respectively. The reduction of exports of goods to the EU in 2009 was primarily attributable to reductions in exports of ferrous metals and their products by 3.0 times, mineral products by 2.3 times and chemical products by 2.1 times, respectively, each as compared to 2008. Increase of exports of goods to the EU in the six months ended 30 June 2010 was largely due to increase in exports of metallurgical products, machinery, wood, light industry products and oil and oil refinery products (other than crude oil) by 2.1 times, 23.2 per cent., 21.4 per cent., 2.8 per cent. and 1.8 times, respectively. Exports of goods to Africa increased by 17.6 per cent. in 2007 and by 39.8 per cent. in 2008, decreased by 32.7 per cent. in 2009 and increased by 22.3 per cent. in the six months ended 30 June 2010 as compared to the same period in 2009.

In 2006, the EU became Ukraine's largest trading partner, a trend that continued in 2007, 2008 and 2009. In 2009, exports of goods and services from Ukraine to the EU amounted to U.S.\$12.5 billion, and imports of goods and services to Ukraine from the EU amounted to U.S.\$18.4 billion, or a 43.6 per cent. and 43.6 per cent. decrease compared to 2008, respectively. The significant decrease of exports to the EU in 2009 was primarily caused by the global financial downturn and reduced demand. In the six months ended 30 June 2010, the EU remained one of the major external trade partners of Ukraine accounting for a 29.2 per cent. share in Ukraine's external trade turnover, with exports of goods and services from Ukraine amounting to U.S.\$7.1 billion, or a 31.6 per cent. increase compared to the same period for 2009, and imports of goods and services to Ukraine amounting to U.S.\$9.4 billion, or a 16.3 per cent. increase compared to the same period for 2009. In the six months ended 30 June 2010, the bilateral trade in goods and services with the EU had a U.S.\$2.3 billion deficit. Trade between Ukraine and the EU consists largely of exports of Ukrainian raw materials, semi-finished products and agricultural products and imports by Ukraine of machinery and vehicles from the EU. The main trading partners of Ukraine within the EU are Germany, Italy and Poland.

In 2007 and 2008, the consolidated trade deficit for goods increased to U.S.\$11.3 billion and U.S.\$18.6 billion, respectively, and in 2009, the consolidated trade deficit for goods decreased to U.S.\$5.7 billion. The deterioration of the consolidated balance of trade in goods during 2007 and 2008 was due to an excess of the import growth rates over export growth rates caused by the deterioration of trade conditions and a decrease in world demand. The reduction in deficit of the consolidated trade balance for goods in 2009 was primarily due to a decline in volumes of imported goods resulting from reduced domestic demand. In the six months ended 30 June 2010, the consolidated trade balance for goods had a deficit totalling U.S.\$2.5 billion and remaining almost at the same level as in the respective period in 2009 due to almost equal growth of imports and exports. See "*External sector — International Trade*".

In 2007, 2008 and 2009, the consolidated balance of trade in goods and services had a deficit totalling U.S.\$7.3 billion, U.S.\$13.3 billion and U.S.\$1.3 billion, respectively. The deterioration of the consolidated

balance of trade in goods and services during 2007 and 2008 was a result of several factors, including the substantial share of energy imports in total imports and significant energy price increases as well as the low pace of production re-equipment and an increased need to implement energy-saving technologies in the machinery manufacturing, metallurgy and chemical industries, requiring growth of inward investment. These factors also included increased demand for imported consumer goods, reduction of customs tariffs and liberalisation of access of goods to Ukraine's domestic market, aimed at the reduction of smuggling. The reduction in deficit of the consolidated trade balance for goods and services in 2009 was largely due to a decline in volumes of imported goods resulting from reduced domestic demand as well a related decrease in services imports. In the six months ended 30 June 2010, the consolidated surplus of trade in goods and services amounted to U.S.\$400.5 million as compared to the deficit of U.S.\$479.1 million for the same period in 2009. The surplus recorded in the six months ended 30 June 2010 resulted from the goods and services exports growing at a rate higher than the imports growth rate during this period. See "External sector — International Trade".

The following table sets out exports of goods by country of destination for the periods shown:

	Year ended 31 December			Six months ended 30 June						
	2007	2008		2009		2009	2010			
	<i>(in U.S.\$ millions and %)⁽¹⁾</i>									
China.....	431.7	0.9	547.5	0.8	1,434.4	3.6	812.0	4.7	495.6	2.1
Germany	1,644.5	3.3	1,837.1	2.7	1,248.1	3.1	507.0	2.9	711.3	3.1
Turkey	3,645.3	7.4	4,633.3	6.9	2,126.5	5.4	955.4	5.5	1,491.5	6.5
United States.....	1,058.1	2.2	1,949.1	2.9	250.4	0.6	74.7	0.4	400.3	1.7
Italy	2,675.1	5.4	2,911.7	4.3	1,227.6	3.1	526.8	3.0	1,144.4	5.0
Poland	1,636.9	3.3	2,338.3	3.5	1,208.0	3.0	459.6	2.7	740.1	3.2
Hungary	1,235.1	2.5	1,367.1	2.0	730.2	1.8	296.7	1.7	341.6	1.5
Thailand	104.6	0.2	270.2	0.4	269.2	0.7	123.2	0.7	227.7	1.0
Slovak Republic	645.2	1.3	910.2	1.4	433.7	1.1	228.9	1.3	255.9	1.1
Syria	846.9	1.7	1,037.3	1.5	753.3	1.9	373.9	2.2	300.9	1.3
Lebanon	136.2	0.3	339.9	0.5	694.1	1.7	301.5	1.7	471.3	2.0
Czech Republic.....	429.0	0.9	670.8	1.0	340.7	0.9	126.3	0.7	293.3	1.3
Netherlands	765.7	1.6	1,117.9	1.7	594.9	1.5	207.6	1.2	242.3	1.0
Greece	221.0	0.5	339.4	0.5	100.3	0.3	46.8	0.3	78.4	0.3
Spain	557.4	1.1	870.0	1.3	570.4	1.4	302.3	1.7	196.8	0.9
Lithuania.....	363.3	0.7	432.3	0.6	193.5	0.5	72.8	0.4	99.6	0.4
Latvia	258.6	0.5	280.5	0.4	178.0	0.4	77.9	0.5	87.0	0.4
CIS	18,087.0	36.7	23,166.3	34.6	13,472.9	33.9	5,833.1	33.7	8,083.7	35.0
Russian Federation	12,668.5	25.7	15,748.5	23.5	8,494.9	21.4	3,466.9	20.0	5,734.5	24.8
Moldova	911.3	1.8	1,172.0	1.8	693.5	1.7	304.5	1.8	320.3	1.4
Kazakhstan	1,433.5	2.9	1,832.6	2.7	1,418.4	3.6	785.5	4.5	586.4	2.5
Belarus	1,561.5	3.2	2,105.6	3.1	1,258.9	3.2	546.6	3.2	802.3	3.5
Turkmenistan	196.6	0.4	376.9	0.6	325.2	0.8	155.2	0.9	97.0	0.4
Azerbaijan.....	631.1	1.3	910.5	1.4	546.0	1.4	250.0	1.4	295.6	1.3
Uzbekistan	346.9	0.7	595.3	0.9	406.2	1.0	203.3	1.2	98.6	0.4
Other CIS states	337.6	0.7	424.9	0.6	329.8	0.8	121.1,	0.7	149.0	0.7
Other	14,554.6	29.5	21,948.4	32.8	13,869.5	34.9	5,973.4	34.5	7,436.5	32.2
Total	49,296.1	100.0	66,967.3	100	39,695.7	100.0	17,299.9	100.0	23,098.2	100.0

Note:

(1) Percentages may not add up to 100.0 because of rounding.

Source: State Committee of Statistics; International Trade Bulletin

The following table sets out imports of goods by country of origin for the periods shown:

	Year ended 31 December			Six months ended 30 June						
	2007	2008		2009		2009		2010		
	<i>(in U.S.\$ millions and %)⁽¹⁾</i>									
Germany	5,830.0	9.6	7,165.3	8.4	3,852.1	8.5	1,682.7	8.5	1,879.5	7.3
USA	1,404.5	2.3	2,808.2	3.3	1,286.3	2.8	634.8	3.2	731.8	2.9
Poland	2,920.5	4.8	4,280.3	5.0	2,170.3	4.8	968.1	4.9	1,083.0	4.2
Italy	1,788.7	3.0	2,432.1	2.8	1,139.8	2.5	507.7	2.6	617.2	2.4
France	1,330.0	2.2	1,682.5	2.0	971.5	2.1	426.2	2.2	474.4	1.9
Czech Republic	1,154.6	1.9	1,376.0	1.6	622.2	1.4	223.8	1.1	274.7	1.1
Slovak Republic	523.5	0.9	742.5	0.9	306.0	0.7	131.3	0.7	166.7	0.7
Hungary	1,240.9	2.0	1,282.7	1.5	678.3	1.5	257.7	1.3	436.4	1.7
United Kingdom	886.4	1.5	1,375.8	1.6	651.1	1.4	301.7	1.5	376.7	1.5
Netherlands	881.0	1.5	1,283.7	1.5	677.5	1.5	323.6	1.6	324.1	1.3
Austria	800.4	1.3	1,031.2	1.2	612.2	1.3	276.9	1.4	289.9	1.1
Turkey	972.3	1.6	1,950.1	2.3	952.2	2.1	422.2	2.1	525.9	2.1
Japan	1,406.6	2.3	2,795.8	3.3	519.5	1.1	271.9	1.4	301.1	1.2
Switzerland	429.8	0.7	1,171.6	1.4	438.0	1.0	220.0	1.1	188.6	0.7
China	3,307.5	5.5	5,601.5	6.5	2,734.3	6.0	1,096.2	5.5	1,843.1	7.2
Lithuania	380.4	0.6	723.9	0.8	410.3	0.9	166.0	0.8	268.7	1.0
Latvia	118.6	0.2	113.1	0.1	110.1	0.2	55.6	0.3	38.8	0.2
CIS	25,469.3	42.0	33,377.8	39.0	19,692.6	43.3	8,624.8	43.6	11,232.9	43.9
Russian Federation	16,838.2	27.8	19,414.2	22.7	13,235.8	29.1	4,254.3	21.5	9,412.0	36.7
Turkmenistan	4,707.4	7.8	5,631.7	6.6	718.3	1.6	697.6	3.5	12.1	0.0
Belarus	1,445.4	2.4	2,809.6	3.3	1,692.8	3.7	642.1	3.2	893.5	3.5
Kazakhstan	1,686.6	2.8	3,118.9	3.6	2,033.9	4.5	1,374.0	7.0	327.5	1.3
Uzbekistan	546.0	0.9	2,118.3	2.5	1,640.8	3.6	1,603.8	8.1	36.4	0.1
Moldova	168.2	0.3	169.6	0.2	52.1	0.1	24.0	0.1	34.9	0.1
Other CIS states	77.5	0.1	115.5	0.1	318.9	0.7	29.1	0.1	516.5	2.0
Other	9,773.0	16.1	14,341.2	16.8	7,608.8	16.7	3,175.1	16.1	4,559.6	17.8
Total	60,618.0	100.0	85,535.3	100.0	45,433.1	100.0	19,766.3	100.0	25,613.1	100.0

Note:

(1) Percentages may not add up to 100.0 because of rounding.

Source: State Committee of Statistics; International Trade Bulletin

Foreign Investment

As a result of a significant shortage of internal financial resources, Ukraine has sought to attract foreign investment as an important contributor to economic growth and structural reform. However, the pace and amount of foreign direct investment (“FDI”) in Ukraine has been adversely affected by overly complex and inconsistent legislation and non-transparent procedures, including in the areas of privatisation, Government intervention and taxation, and by perceived corruption. Nevertheless, the amount of cumulative FDI has been increasing in recent years. Cumulative FDI increased by 36.7 per cent. in 2007 as compared to 2006, by 20.6 per cent. in 2008 as compared to 2007, by 12.4 per cent. in 2009 as compared to 2008 and by 1.2 per cent. in the six months ended 30 June 2010 as compared to 1 January 2010. As at 1 January 2007, 1 January 2008, 1 January 2009, 1 January 2010 and 1 July 2010, cumulative FDI (including foreign interests in privatisations) reached U.S.\$21.6 billion, U.S.\$29.5 billion, U.S.\$35.6 billion, U.S.\$40.0 billion and U.S.\$40.4 billion, respectively.

At the same time, the annual amount of FDI decreased from U.S.\$7,935.4 million in 2007 to U.S.\$6,073.7 million in 2008 and further decreased to U.S.\$4,410.4 million in 2009 due to the global financial downturn. The net amount of FDI inflow for the six months ended 30 June 2010 was U.S.\$495.8 million as compared to U.S.\$2,358.6 million in the same period in 2009. The main reasons for the low level of FDI inflow in the six months ended 30 June 2010 include, among other things, increased risks of foreign exchange market instability, limited access to financial resources both in the domestic and external markets, and decrease in profitability of Ukrainian companies. Foreign currency FDI was approximately U.S.\$880.7 per capita as of 1 July 2010.

The following table shows the breakdown of FDI for the periods indicated:

	FDI (cumulative total) at the end of the relevant period⁽¹⁾	Growth of FDI for the relevant period
	<i>(in U.S.\$ millions)</i>	
2007	29,542.7	7,935.4
2008	35,616.4	6,073.7
Six months ended 30 June 2009	37,965.7	2,358.6
2009	40,026.8	4,410.4
Six months ended 30 June 2010	40,402.1	495.8

Note:

(1) FDI (cumulative total) measures the volume of FDI starting from 1991.

Source: State Committee of Statistics

The following table shows the breakdown of cumulative FDI by country of origin for the periods indicated:

	Year ended 31 December				Six months ended 30 June					
	2007		2008		2009		2009		2010	
	<i>(U.S.\$ millions)</i>	<i>Share (% of total)</i>	<i>(U.S.\$ millions)</i>	<i>Share (% of total)</i>	<i>(U.S.\$ millions)</i>	<i>Share (% of total)</i>	<i>(U.S.\$ millions)</i>	<i>Share (% of total)</i>	<i>(U.S.\$ millions)</i>	<i>Share (% of total)</i>
USA	1,430.1	4.8	1,464.6	4.1	1,387.1	3.5	1,369.2	3.6	1,214.6	3.0
Cyprus.....	5,946.4	20.1	7,646.2	21.5	8,593.2	21.5	8,063.7	21.2	9,079.2	22.5
Russian Federation	1,462.4	5.0	1,847.2	5.2	2,674.6	6.7	2,125.7	5.6	2,877.2	7.1
UK.....	1,975.5	6.7	2,249.8	6.3	2,375.9	5.9	2,330.0	6.1	2,228.1	5.5
Netherlands	2,508.8	8.5	3,197.4	9.0	4,002.0	10.0	3,717.1	9.8	3,929.0	9.7
Germany	5,918.3	20.0	6,393.0	17.9	6,613.0	16.5	6,530.9	17.2	6,618.6	16.4
Austria.....	2,067.4	7.0	2,443.8	6.9	2,604.1	6.5	2,490.0	6.6	2,591.1	6.4
Other ⁽¹⁾	8,233.8	27.9	10,374.4	29.1	11,776.9	29.4	11,339.7	29.9	11,864.3	29.4
Total⁽²⁾	29,542.7	100.0	35,616.4	100.0	40,026.8	100.0	37,965.7	100.0	40,402.1	100.0

Notes:

(1) Includes countries whose cumulative FDI contribution did not exceed 5.0 per cent. of the total (other than the U.S. included in a separate line).

(2) Totals may not add up due to rounding.

Source: State Committee of Statistics

In 2007, 2008 and 2009, Cyprus was the largest contributor of FDI to Ukraine. As at 1 July 2010, Cypriot investments into Ukraine amounted to U.S.\$9,079.2 million, constituting 22.5 per cent. of the total volume of investments. Cypriot FDI is believed to consist primarily of “off-shore” investment originating in Russia or other CIS countries that is structured through Cyprus for tax reasons. Germany, Netherlands, Austria, the United Kingdom, the Russian Federation, British Virgin Islands, Sweden and the United States continue to be among the most important sources of FDI.

The principal forms of FDI are monetary contributions (which were U.S.\$5,008.9 million in 2009, and U.S.\$1,618.6 million in the six months ended 30 June 2010) and investments in personal and real property (which were U.S.\$384.8 million in 2009, and U.S.\$149.2 million in the six months ended 30 June 2010). Investments made in Ukraine to date have primarily been in the fields of industry, financial sector, trade and repair of cars and household goods, real estate, rent, engineering and rendering of services for entrepreneurs. In the six months ended 30 June 2010, FDI in the financial and banking sector accounted for the largest share of the growth in investment over the same period.

The following table sets out cumulative FDI by sector for the periods indicated:

	Year ended 31 December				Six months ended 30 June					
	2007		2008		2009		2009		2010 ⁽¹⁾	
	(U.S.\$ millions)	Share (% of total)	(U.S.\$ millions)	Share (% of total)	(U.S.\$ millions)	Share (% of total)	(U.S.\$ millions)	Share (% of total)	(U.S.\$ millions)	Share (% of total)
Food Industry	1,561.2	5.3	1,685.9	4.7	1,837.2	4.6	1,792.1	4.7	1,772.0	4.4
Wholesale Trade	2,610.3	8.8	3,104.5	8.7	3,446.4	8.6	3,176.5	8.4	3,637.1	9.0
Finance/Insurance	4,869.1	16.5	7,154.7	20.1	8,968.4	22.4	8,015.7	21.1	13,010.4	32.2
Machinery manufacturing	1,013.1	3.4	1,016.9	2.9	1,094.1	2.7	1,051.7	2.8	1,096.8	2.7
Fuel Industry	319.6	1.1	330.2	0.9	451.4	1.1	331.8	0.9	454.8	1.1
Transport	1,274.4	4.3	1,411.1	4.0	1,506.3	3.8	1,442.6	3.8	1,623.7	4.0
Chemical and Petrochemical Industry	840.8	2.8	949.9	2.7	1,205.6	3.0	1,150.7	3.0	1,064.9	2.6
Real estate activities	2,669.3	9.0	3,613.8	10.1	4,065.0	10.2	4,068.7	10.7	4,285.9	10.6
Metallurgy	1,596.7	5.4	1,356.5	3.8	1,401.2	3.5	1,406.0	3.7	5,641.1	14.0
Other	12,788.2	43.4	14,992.9	42.1	16,051.2	40.1	15,529.9	40.9	7,815.4	19.4
Total⁽²⁾	29,542.7	100.0	35,616.4	100.0	40,026.8	100.0	37,965.7	100.0	40,402.1	100.0

Note:

- (1) These figures take into account information from the NBU and the SPF regarding the difference between market and nominal value of shares and other property, not reflected in the statistical reporting of certain companies (broken down by economic activity).
- (2) Totals may not add up due to rounding.

Source: State Committee of Statistics

Foreign investors are treated equally with domestic investors and, in most circumstances, are permitted to conduct business on the same terms as domestic business enterprises. In addition, capital assets imported into Ukraine as a contribution to the charter fund of a Ukrainian legal entity by a foreign investor are exempt from customs duties on imports.

Foreigners are permitted to own up to 100 per cent. of a Ukrainian company, subject to foreign ownership restrictions in certain industry sectors such as publishing, television and radio broadcasting and news agency services. The hryvnia is not yet freely exchangeable, and a withholding tax of 15 per cent. may be applied to profit repatriation, subject to the provisions of treaties on the avoidance of double taxation, which can reduce or eliminate this tax.

PUBLIC FINANCE AND FISCAL POLICY

Upon independence, Ukraine was confronted with a number of challenges to its fiscal policy. A new fiscal structure had to be built, the tax system had to be redesigned in a market-oriented manner and the disruptions caused by the split from the Soviet Union led to new demands on the budget. In the early post-independence years expansionary fiscal policies were sometimes regarded as a useful tool to shelter the economy from adjustment shocks. Consequently, Ukraine's fiscal deficits increased rapidly in the first years following independence.

The deficits were financed from 1991 to 1995 predominantly by loans from the NBU and by accumulating arrears on energy imports from Russia and Turkmenistan. Only a relatively small part of the budget deficit was financed by foreign official loans and grants due to disagreements with Western donors over nuclear safety and disarmament. The Government's attempts to protect the economy from the impact of the separation from the Soviet Union through subsidies and social transfer payments meant that the percentage of GDP represented by budget expenditures remained at approximately 53 per cent. from 1992 to 1994 (even according to the official expenditure figures, which are probably understated) and the share of subsidies in budget expenditures rose from 14 per cent. in 1992 to 21 per cent. in 1994.

With the emergence of a domestic treasury bill market in March 1995, the Government continued to finance the deficit in part through the domestic debt markets. However, the domestic treasury bill market was characterised by short maturities and high real interest rates (which were necessary to protect the Ukrainian currency from devaluation). As a result, Ukraine increasingly relied upon external sources of funding to cover budget deficits, including official creditors, multilateral organisations and commercial debt. This resulted in a sharp rise in the aggregate external debt of Ukraine from 1994 to 1998. The lack of substantial progress in implementing needed structural reforms in the economy (including improved revenue collection), combined with the fall-out from the Russian and Asian economic crises of 1998/1999, made it increasingly difficult from mid-1998 for Ukraine to refinance its external obligations except on highly disadvantageous terms. During this period, loans from international organisations such as the IMF and the World Bank and from the EU were the only substantial new source of external financing for Ukraine. See *“Public Debt – External Public Debt”*. See also *“Risk Factors – Risk Factors Relating to the Guarantor – Inability to obtain financing from external sources to provide financing could affect Ukraine's ability to meet financing expectations in its budget”*.

The Government also used various payment arrears as a means of helping finance the budget deficit. The consolidated budget-related arrears amounted to UAH 927 million at year-end 1999, increasing to UAH 1,388 million as at 1 July 2010.

The Budget Process

Pursuant to the Constitution, each year, following review by the Cabinet of Ministers, a proposed State Budget is to be submitted to Parliament by 15 September. The deadline for approval of the State Budget Law by Parliament is 1 December. No penalties apply if this deadline is not met, and the review period resumes. However, if the State Budget Law is not adopted by 1 January, certain borrowing restrictions apply until the adoption of the State Budget Law for a relevant year.

The 2007 State Budget Law initially contemplated revenues of UAH 147.9 billion, expenditures of UAH 161.8 billion, privatisation receipts of UAH 10.6 billion and a budget deficit of UAH 15.7 billion (or 2.6 per cent. of GDP) for 2007. Basic assumptions underlying the 2007 State Budget included a real GDP growth rate of 6.5 per cent., nominal GDP of UAH 594.1 billion (further increased to UAH 636.6 billion), annual consumer price inflation of 7.5 per cent., wholesale price inflation of 14.4 per cent. and an average annual exchange rate of UAH 5.1 = U.S.\$1.00. Pursuant to several rounds of amendments to the 2007 State Budget Law, budgeted revenues were increased to UAH 157.3 billion and budgeted expenditures were increased to UAH 174.6 billion with a budget deficit unchanged at the level of UAH 15.7 billion (or 2.6 per cent. of GDP). Actual revenues and expenditures of the 2007 State Budget amounted to UAH 165.9 billion and UAH 174.3 billion, respectively. The actual deficit of the 2007 State Budget amounted to UAH 9.8 billion (or 1.4 per cent. of GDP). According to the 2007 State Budget Law, the Cabinet of Ministers directed an

additional UAH 3.0 billion from the disposable balance of State Budget funds to finance the general fund of the State Budget in 2007.

In March 2007, the Budget Declaration for 2008 was adopted, setting forth the basic parameters of budget policy for 2008 as well as specific tasks and objectives for further social and economic development. The Declaration provided for the improvement of allocation of inter-budgetary transfers. It also called for the concentration of capital expenditures for implementation of investment projects (for instance, it contemplated allocating at least 10 per cent. of privatisation proceeds to financial support of investment projects of strategic importance). Furthermore, the Declaration expanded the budget powers of the local executive authorities and local self-government bodies. Under the Declaration, the Government planned to further decentralise financial resources by granting subventions from the State Budget to local budgets and increasing the share of the general fund of the local budgets in the general fund of the consolidated budget. For the purposes of implementing budget policy for 2008 a number of important regulations were adopted, including the Concept of Local Budget Reform and the Strategy for Modernisation of the State Finance Management System.

The 2008 State Budget Law initially contemplated revenues of UAH 215.4 billion, expenditures of UAH 232.4 billion, privatisation receipts of UAH 8.9 billion and a budget deficit of UAH 18.8 billion (or 2.1 per cent. of GDP) for 2008. Basic assumptions underlying the 2008 State Budget initially included a real GDP growth rate of 7.2 per cent., nominal GDP of UAH 810.1 billion, annual consumer price inflation of 6.8 per cent., wholesale price inflation of 11.6 per cent. and an average annual exchange rate of UAH 4.95 to 5.25 = U.S.\$1.00. Pursuant to several rounds of amendments to the 2008 State Budget Law, underlying basic assumptions were revised to include a real GDP growth rate of 6.8 per cent., nominal GDP of UAH 959.2 million, consumer price inflation of 15.9 per cent., wholesale price inflation of 31.2 per cent. and an average annual exchange rate of UAH 4.95 to 5.25 = U.S.\$1.00. Budgeted revenues and expenditures were revised several times in 2008, and pursuant to the last amendment to the 2008 State Budget Law enacted on 12 December 2008, budgeted revenues were increased to UAH 231.9 billion, budgeted expenditures were increased to UAH 253.2 billion and privatisation receipts were decreased to UAH 607.1 million, with a budget deficit at the level of UAH 25.0 billion (or 2.6 per cent. of GDP). Actual revenues and expenditures of the 2008 State Budget amounted to UAH 231.7 billion and UAH 241.5 billion respectively. The actual deficit of the 2008 State Budget amounted to UAH 12.5 billion (or 1.3 per cent. of GDP). The 2008 State Budget priorities included wage increases for public sector employees and military personnel, pension, scholarships and other social benefit increases, reimbursement of lost savings to citizens, implementation of measures relating to the preparation and hosting of the Euro-2012 Championship, financial support for Naftogas, as well as development of rural localities, road and transport sector and the aircraft industry.

In March 2008, the Budget Declaration for 2009 was adopted, setting forth the basic parameters of budget policy for 2009, as well as specific tasks and objectives for further social and economic development. The Declaration established that the targets for 2009 would include a ratio of total State debt (including guaranteed debt) to GDP at a level not higher than in 2008; and a budget deficit of not more than 2 per cent. of GDP. The Declaration allowed an increase of borrowings in the amount of up to 1 per cent. of GDP to be used to finance expenditure for the preparation and hosting of the Euro-2012 Championship. The Declaration set forth, among other things, the following priorities of budget policy for 2009: (i) establishing a minimum monthly wage at the subsistence level; (ii) targeting budget capital expenditures at development of information, communication, transport and municipal infrastructure; (iii) gradual decrease of the tax burden; (iv) expansion of the tax base and improvement of the tax administration system; (v) elaboration of the budget based on the harmonisation of the Ukrainian tax legislation with that of the EU; and (vi) strengthening of the local budgets' revenue bases and creating incentives for local authorities for an expansion thereof.

The 2009 State Budget Law initially contemplated revenues of UAH 238.9 billion, expenditures of UAH 267.3 billion, privatisation receipts of UAH 8.5 billion and a budget deficit of UAH 31.1 billion (or 3.0 per cent. of GDP) for 2009. Pursuant to several rounds of amendments to the 2009 State Budget Law, budgeted revenues were increased to UAH 245.3 billion, budgeted expenditures were increased to UAH 274.2 billion and the budget deficit was increased to UAH 31.6 billion (or 3.0 per cent. of GDP). Actual revenues and

expenditures of the 2009 State Budget amounted to UAH 209.7 billion and UAH 242.4 billion respectively. The actual deficit of the 2009 State Budget amounted to UAH 35.5 billion (or 3.9 per cent. of GDP). Basic assumptions underlying the 2009 State Budget included a real GDP growth rate of 0.4 per cent., nominal GDP of UAH 1,046.5 billion, annual consumer price inflation of 9.5 per cent., wholesale price inflation of 12.0 per cent. and an average annual exchange rate of UAH 7.5 = U.S.\$1.00. The 2009 State Budget priorities included wage increases for public sector employees and military personnel, pension, scholarships and other social benefit increases, reimbursement of lost savings to citizens, implementation of measures relating to the preparation and hosting of the Euro-2012 Championship, financial support for Naftogas, as well as development of rural localities, road and transport sector and the aircraft industry.

In February 2009, the Budget Declaration for 2010 was adopted aiming at the implementation of efficient tax and budget policy and development of a balanced budget for 2010. The Declaration sets forth, among other things, the following priorities of budget policy for 2010: (i) ensuring balance and sustainability of the budgetary system in the conditions of the financial and economic downturn; (ii) optimisation of budget expenditures, while meeting all state social standards; (iii) rationalisation of the tax and customs system; and (iv) strengthening of the local budgets' revenue bases and creating incentives for local authorities for an expansion thereof.

Unlike in several previous years when the State Budget Law was adopted before the start of the relevant budget year, the 2010 State Budget Law was adopted by Parliament only on 27 April 2010, largely due to pre-election political controversies. The 2010 State Budget Law initially contemplated revenues of UAH 267.5 billion, expenditures of UAH 324.0 billion, privatisation receipts of UAH 10.0 billion and a budget deficit of UAH 57.7 billion (or 5.3 per cent. of GDP) for 2010. Pursuant to an amendment to the 2010 State Budget Law passed by Parliament in May 2010, budgeted revenues were decreased to UAH 266.1 billion and budgeted expenditures were decreased to UAH 322.7 billion. Basic assumptions underlying the 2010 State Budget include a real GDP growth rate of 3.7 per cent., nominal GDP of UAH 1,083.1 billion, annual consumer price inflation of 13.1 per cent., wholesale price inflation of 14.4 per cent. and an average annual exchange rate of UAH 8.0 = U.S.\$1.00. Priorities of the 2010 State Budget as originally enacted included an increase of the minimum wage and increases of wages for public sector employees and military personnel, pension, scholarships and other social benefit increases, reimbursement of lost savings to citizens, implementation of measures relating to the preparation and hosting of the Euro-2012 Championship, financial support for Naftogas, as well as development of rural localities, the road and transport sector, the aircraft industry and agriculture and mining sectors.

On 8 July 2010, in order to comply with the new arrangements reached with the IMF, Parliament passed the State Budget Amendment. The State Budget Amendment provides for a decrease in revenues to the 2010 State Budget of approximately UAH 13.4 billion, a decrease in expenditures from the 2010 State Budget of approximately UAH 17.1 billion, a decrease in the 2010 State Budget deficit of approximately UAH 3.65 billion (to 4.99 per cent. of GDP) and a decrease in target privatisation proceeds of approximately UAH 3.65 billion. The UAH 13.4 billion decrease in revenues includes a decrease in revenues from VAT collection of approximately UAH 10 billion. The UAH 17.1 billion decrease in expenditures includes an approximately UAH 8.75 billion decrease in expenditures from the Stabilisation Fund and an approximately UAH 3.0 billion decrease in transfers to cover the deficit in the Pension Fund.

The amendments to the 2008 State Budget Law, introduced to counteract adverse effects of the global financial downturn, as well as the 2009 State Budget Law and the 2010 State Budget Law contemplate the creation of a Stabilisation Fund. In 2009, expenditures from the Stabilisation Fund amounted to UAH 9,955.0 million. In 2010, the revenues assigned to the Stabilisation Fund include proceeds from certain placements of T-bills, privatisation receipts, proceeds from the sale of state-owned land plots on which privatisation objects are located, and repayment of borrowings raised from the Stabilisation Fund in 2009. As at 1 January 2010, the balance of the Stabilisation Fund was UAH 1,610.3 million from 2009, and in the seven months ended 31 July 2010, the revenues to the Stabilisation Fund amounted to UAH 10,602 million, which included the UAH 1,610.3 million balance as at the beginning of 2010. The expenditures that may be made out of the Stabilisation Fund in 2010 include, among other things, financing of investment projects and support for certain projects in agriculture, the aviation industry, defence, machine-building, and construction and refurbishment of mining and peat production companies; financing of investment and innovative energy

saving projects in the housing and communal sector; support for social and economic development of regions; extension of loans for the completion of residential real estate construction projects; and implementation of measures relating to the preparation and hosting of the Euro-2012 Championship. In the seven months ended 31 July 2010, UAH 7,434.9 million were spent out of the Stabilisation Fund for these purposes.

In April 2010, the Government adopted the Budget Declaration for 2011 with the aim of overcoming the effects of the financial and economic downturn, implementation of efficient tax and budget policy, transition to an investment and innovative model of economy development, increase of employment, wage increases and facilitation of pricing and exchange rate stability. The Declaration sets forth, among other things, the following priorities of 2011 budget policy: (i) creating favourable conditions for industry development and incentives for sustainable economic and social development; (ii) implementation of well-considered debt policy; (iii) gradual increase of social standards; (iv) reform of inter-budgetary relations to ensure sustainable social and economic development of regions; and (v) focusing budget resources on implementation of priority government programmes. The Declaration also establishes that the budget targets for 2011 include a ratio of State debt to GDP at a level not higher than 40 per cent. and a budget deficit of not more than 4.5 per cent. of GDP.

In furtherance of the Budget Declaration for 2011, the Ministry of Finance is currently preparing a draft 2011 State Budget, basic assumptions underlying which include a real GDP growth rate of 4.5 per cent., nominal GDP of UAH 1,253.0 billion, annual consumer price inflation of 8.9 per cent., wholesale price inflation of 11.3 per cent. and an average annual exchange rate of UAH 7.95 = U.S.\$1.00.

On 8 July 2010, Parliament approved the restatement of the Budget Code of Ukraine. The restatement aims to, among other things, further develop medium-term budget planning; introduce modern forms and methods of management of budget funds and State and local debt management; improve the system for State control over budget performance; tighten responsibility of budget process participants; and strengthen financial independence of local budgets. The restatement of the Budget Code introduces a number of changes to existing budgetary legislation to achieve these goals, including, among other things, changes in the procedure for consideration and approval of State Budget laws and other legislation affecting budgetary indices. The restatement also provides for the introduction of a new local tax on real estate (other than land plots) and envisages a transfer to local budgets of certain additional revenues, such as revenues from licensing and certification and, partly, revenues from charges for use of natural resources and state registration. It is expected that certain provisions of the restatement will enter into force from 1 January 2011, with others to become effective from 1 January 2013.

The Consolidated Budget

The main figures of the Consolidated Budget (consisting of the State Budget plus local budgets) and actual Consolidated Budget performance for 2007 and 2008 are set out in the table below:

	2007		2008	
	Budget as amended	Actual	Budget as amended	Actual
	<i>(in UAH millions)</i>			
Revenues				
Tax revenue	158,770.8	161,264.2	232,475.2	227,164.8
<i>of which:</i>				
Personal income tax	33,365.6	34,782.1	47,724.3	45,895.8
Enterprise income tax	29,006.6	34,407.2	42,717.5	47,856.8
VAT	65,122.5	59,382.8	99,292.7	92,082.6
Excise duty on domestic goods	9,073.3	9,072.2	11,228.2	10,230.1
Excise duty on imported goods	1,329.1	1,495.5	2,573.1	2,553.0
Non-tax revenue	48,325.3	48,553.2	57,235.8	60,543.6
Capital revenue	6,899.1	6,373.4	12,321.3	6,702.4
Official transfers	97.6	104.5	95.3	135.2
Special funds ⁽¹⁾	3,494.6	3,641.2	4,145.0	3,347.0
Total revenues	217,587.4	219,936.5	306,272.7	297,893.0
Expenditures				
State function	26,637.7	24,270.9	39,357.1	30,829.2
<i>of which:</i>				
Public and local administration, financial and foreign economic activity	15,368.1	14,900.1	21,430.2	20,551.5
Public debt service ⁽²⁾	4,993.1	3,678.9	4,485.5	4,264.8
Fundamental research	1,788.2	1,733.4	2,300.5	2,230.1
National defence	10,604.7	9,416.5	12,226.1	11,733.0
Law enforcing activity and State security and court power	18,781.4	18,445.7	27,908.2	27,080.9
Economic activity	45,860.1	40,523.4	59,396.4	51,322.4
<i>of which:</i>				
General economic, trade and labour activity	826.1	807.2	1,107.2	973.4
Agriculture, forestry, fishery and hunting	8,374.8	8,037.7	11,273.4	9,630.5
Fuel and energy complex	9,160.4	7,350.4	16,328.1	15,484.0
Transport	15,162.6	14,563.0	16,324.5	14,002.5
Communication, telecommunication and informatics	150.1	142.0	239.9	168.4
Education	45,075.3	44,333.6	62,492.9	60,959.4
Health	26,522.6	26,717.6	34,283.9	33,559.9
Social protection and insurance	51,376.3	48,517.3	77,154.7	74,069.7
Housing and communal services	6,520.4	5,900.3	10,333.2	8,968.5
Intellectual and physical development	5,681.4	5,687.7	8,243.2	7,916.1
<i>of which:</i>				
Culture and art	3,275.3	3,268.3	5,006.9	4,808.9
Mass media	874.2	849.8	1,073.1	1,005.1
Physical culture and sport	1,496.4	1,537.2	2,123.2	2,064.2
Protection of environment	2,553.8	2,241.3	3,129.7	2,764.7
Total expenditures	239,613.6	226,054.4	334,525.4	309,203.7
Domestic lending	1,978.2	1,583.9	4,084.9	2,813.8
External lending	(10.1)	–	–	–
Total lending	1,968.1	1,583.9	4,084.9	2,813.8
Balance (surplus/deficit)	(23,994.3)	(7,701.7)	(32,401.7)	(14,124.5)
Balance (% of GDP) ⁽³⁾	(3.3)	(1.1)	(3.4)	(1.5)
Domestic financing ⁽⁴⁾	–	3,244.6	5,994.4	11,021.7
<i>of which:</i> Receipts from privatisation of State property	10,587.7	2,458.8	607.1	482.3
External financing ⁽⁵⁾	–	4,457.1	6,092.4	3,102.9
Total financing⁽⁶⁾	23,994.3	7,701.7	32,401.7	14,124.5

Notes:

- (1) "Special funds" includes amounts received into the fund for Social Insurance of Disabled Persons, a fund for the remediation of environmental pollution and special funds established by the parliament of the Autonomous Republic of Crimea and other local governance bodies and authorities in Ukraine.
- (2) Does not include repayments of principal.
- (3) Actual figures have been provided for this item.
- (4) "Domestic financing" includes domestic issues, domestic repayments, changes in cash volumes and receipts from privatisation of State property. "Domestic financing" is presented net of repayments (i.e. net of domestic issues and domestic repayments).
- (5) "External financing" is presented net of repayments (i.e. net of external issues and external repayments).
- (6) "Total financing" and components of this line reflect financing of both State and local budgets. State property privatisation receipts are included in the State Budget only.

The 2007 Consolidated Budget, as amended, contemplated revenues of UAH 217.6 billion, expenditures of UAH 239.6 billion and a budget deficit of UAH 24.0 billion, or 3.4 per cent. of GDP. Basic assumptions underlying the 2007 Consolidated Budget, as amended, included a real GDP growth rate of 6.5 per cent., nominal GDP of UAH 594.1 billion, consumer price inflation of 7.5 per cent. and an average annual exchange rate of UAH 5.1 = U.S.\$1.00. The actual revenues and expenditures of the 2007 Consolidated Budget amounted to UAH 219.9 billion and UAH 226.1 billion, and actual budget deficit amounted to UAH 7.7 billion, or 1.1 per cent. of GDP in 2007.

The 2008 Consolidated Budget, as amended, contemplated revenues of UAH 306.3 billion, expenditures of UAH 334.5 billion and a budget deficit of UAH 32.4 billion, or 3.3 per cent. of GDP. Basic assumptions underlying the 2008 Consolidated Budget, as amended, included a real GDP growth rate of 6.8 per cent., nominal GDP of UAH 959.2 billion, consumer price inflation of 15.9 per cent. and an average annual exchange rate of UAH 4.95 to 5.25 = U.S.\$1.00. The actual revenues and expenditures of the 2008 Consolidated Budget amounted to UAH 297.9 billion and UAH 309.2 billion, respectively, and actual budget deficit amounted to UAH 14.1 billion, or 1.5 per cent. of GDP in 2008.

The main figures of the Consolidated Budget in 2009 and 2010 and actual Consolidated Budget performance in 2009 and the seven months ended 31 July 2009 and 2010 are set out in the table below:

	2009		2010		
	Budget as amended	Actual (seven months ended 31 July 2009)	Actual	Budget ⁽¹⁾	Actual (seven months ended 31 July 2010)
<i>(in UAH millions)</i>					
Revenues					
Tax revenue.....	240,648.9	111,658.6	208,073.2	254,771.4	133,241.6
<i>of which:</i>					
Personal income tax.....	46,091.9	25,008.8	44,485.3	50,532.8	27,528.1
Enterprise income tax	42,966.0	16,270.9	33,048.0	40,602.6	18,867.6
VAT	97,643.0	46,463.8	84,596.7	104,735.2	56,083.3
Excise duty on domestic goods	19,566.4	8,538.0	17,934.5	25,992.0	13,079.9
Excise duty on imported goods	4,387.4	1,944.6	3,690.0	4,374.0	2,502.5
Non-tax revenue	72,709.8	3,480.8	58,435.8	60,590.1	39,176.2
Capital revenue	7,429.4	1,745.6	3,653.1	1,948.6	1,868.4
Official transfers	838.0	91.7	645.3	680.5	104.5
Special funds ⁽²⁾	3,070.4	1,170.9	2,159.5	2,069.3	1,486.8
Total revenues	324,696.5	151,147.6	272,967.0	320,059.8	175,877.4
Expenditures					
State function	47,587.7	16,662.0	33,156.0	49,194.1	21,552.4
<i>of which:</i>					
Public and local administration, financial and foreign economic activity	19,502.4	10,463.0	18,675.4	15,821.7	10,370.1
Public debt service ⁽³⁾	13,063.4	3,857.3	9,783.8	14,428.8	7,777.8
Fundamental research	2,258.4	1,147.9	2,188.3	2,357.6	1,248.1
National defence.....	12,991.3	4,928.6	9,663.3	12,012.9	5,513.7
Law enforcing activity and State security and court power	25,465.8	13,146.6	24,346.1	26,231.2	14,274.1
Economic activity	61,763.9	23,009.6	39,753.0	27,394.8	19,586.7
<i>of which:</i>					
General economic, trade and labour activity ..	1,052.6	362.7	806.8	679.2	459.8
Agriculture, forestry, fishery and hunting	7,165.3	3,275.3	6,285.6	5,303.9	2,706.1
Fuel and energy complex.....	14,240.8	7,665.5	11,965.3	6,481.1	6,496.5
Transport	19,057.4	8,757.5	13,711.2	9,344.0	7,535.2
Communication, telecommunication and informatics	249.9	76.8	191.7	91.5	84.5
Education	69,646.4	38,342.5	66,773.6	76,308.9	44,143.9
Health	37,001.6	19,082.1	36,564.9	41,029.4	22,275.7
Social protection and insurance	83,038.7	44,154.6	78,775.4	106,535.2	65,931.3
Housing and communal services	8,444.5	3,584.6	7,498.1	6,296.4	2,103.7
Intellectual and physical development	8,794.5	3,972.3	8,330.2	10,744.0	5,728.3
<i>of which:</i>					
Culture and art	4,959.6	2,489.6	4,766.1	7,344.2	3,005.4
Mass media	923.9	430.9	848.2	1,164.7	507.3
Physical culture and sport	2,882.0	1,036.8	2,687.8	2,202.6	2,199.7
Protection of environment	3,157.5	971.2	2,538.8	2,798.6	978.7
Total expenditures	357,891.9	167,854.2	307,399.4	372,974.3	202,088.4

	2009		2010		Actual (seven months ended 31 July 2010)
	Budget as amended	Actual (seven months ended 31 July 2009)	Actual	Budget ⁽¹⁾	
	<i>(in UAH millions)</i>				
Domestic lending	3,884.8	1,130.6	2,825.8	1,180.9	(938.0)
External lending	–	0.01	–	–	–
Total lending	3,884.8	1,130.6	2,825.8	1,180.9	(938.0)
Balance (surplus/deficit).....	(37,174.3)	(17,837.1)	(37,258.1)	(54,095.4)	(25,273.0)
Balance (% of GDP) ⁽⁴⁾	(4.1)	–	(4.1)	(4.99)	–
Domestic financing ⁽⁵⁾	55,675.8	17,374.3	(7,541.7)	49,128.3	11,554.6
of which: Receipts from privatisation of State property	8,501.2	565.4	807.8	6,350.0	314.4
External financing ⁽⁶⁾	5,878.2	35,211.5	44,799.9	27,333.9	13,718.4
Total financing ⁽⁷⁾	37,174.3	17,837.1	37,258.1	54,095.4	25,273.0

Notes:

- (1) As per preliminary calculations of the Ministry of Finance.
- (2) "Special funds" includes amounts received into the fund for Social Insurance of Disabled Persons, a fund for the remediation of environmental pollution and special funds established by the parliament of the Autonomous Republic of Crimea and other local governance bodies and authorities in Ukraine.
- (3) Does not include repayments of principal.
- (4) Actual figures have been provided for this item.
- (5) "Domestic financing" includes domestic issues, domestic repayments, changes in cash volumes and receipts from privatisation of State property. "Domestic financing" is presented net of repayments (i.e. net of domestic issues and domestic repayments).
- (6) "External financing" is presented net of repayments (i.e. net of external issues and external repayments).
- (7) "Total financing" and components of this line reflect financing of both State and local budgets. State property privatisation receipts are included in the State Budget only.

The 2009 Consolidated Budget, as amended, contemplated revenues of UAH 324.7 billion, expenditures of UAH 357.9 billion and a budget deficit of UAH 37.2 billion, or 4.1 per cent. of GDP. Basic assumptions underlying the 2009 Consolidated Budget, as amended, included a real GDP growth rate of 0.4 per cent., nominal GDP of UAH 1,046.5 billion, consumer price inflation of 9.5 per cent. and an average annual exchange rate of UAH 7.5 = U.S.\$1.00. The actual revenues and expenditures of the 2009 Consolidated Budget amounted to approximately UAH 273.0 billion and UAH 307.4 billion, respectively, and actual budget deficit amounted to UAH 37.3 billion, or 4.1 per cent. of GDP in 2009. In 2009, revenues of the Consolidated Budget were below the budgeted target by UAH 51,728.5 million largely due to the effect of financial and economic downturn globally and in Ukraine. Of that amount, UAH 609.4 million, UAH 13,046.3 million and UAH 9,917.9 million reflects decreased collection of import duties, VAT and corporate income tax, respectively.

The 2010 Consolidated Budget initially contemplated revenues of UAH 334.8 billion, expenditures of UAH 391.4 billion and a budget deficit of UAH 57.7 billion (or 5.3 per cent. of GDP). Basic assumptions underlying the 2010 Consolidated Budget include a real GDP growth rate of 3.7 per cent., nominal GDP of UAH 1,083.1 billion, consumer price inflation of 13.1 per cent. and an average annual exchange rate of UAH 8.0 = U.S.\$1.00. On 8 July 2010, in order to comply with the new arrangements reached with the IMF, Parliament passed the State Budget Amendment providing for a decrease in revenues, expenditures and the deficit of the State Budget. The State Budget Amendment has resulted in a decrease of planned revenues, expenditures and the deficit of the Consolidated Budget to UAH 320.1 billion, UAH 373.0 billion and UAH 54.1 billion (or 4.99 per cent of GDP), respectively.

Expenditures

The 2007 Consolidated Budget, as amended, contemplated social expenditure of 53.7 per cent. of the Consolidated Budget. Of this amount, the State Budget Law for 2007, as amended, contemplated social

expenditure of 39.5 per cent. of the State Budget, which included wage increases for public sector employees and social benefit increases. The “protected” expenditure, including external debt service, wages for public employees and certain social benefit payments, totalled approximately UAH 113.4 billion, or 67.3 per cent. of the State Budget.

The 2008 Consolidated Budget, as amended, contemplated social expenditure of 54.5 per cent. of the Consolidated Budget. Of this amount, the State Budget Law for 2008, as amended, contemplated social expenditure of 43.2 per cent. of the State Budget, which included wage increases for public sector employees and social benefit increases. The “protected” expenditure, including external debt service, wages for public employees and certain social benefit payments, totalled UAH 163.1 billion, or 61.9 per cent. of the State Budget.

The 2009 Consolidated Budget, as amended, contemplated social expenditure of 54.4 per cent. of the Consolidated Budget. Of this amount, the State Budget Law for 2009, as amended, contemplated social expenditure of 40.3 per cent. of the State Budget, which included wage increases for public sector employees and social benefit increases. The “protected” expenditure, including external debt service, wages for public employees and certain social benefit payments and payments for the implementation of measures relating to the preparation and hosting of the Euro-2012 Championship, totalled UAH 180.6 billion, or 65.9 per cent. of the State Budget.

As per preliminary calculations of the Ministry of Finance, the 2010 Consolidated Budget contemplates social expenditure of 61.8 per cent. of the Consolidated Budget. Of this amount, the State Budget Law for 2010 contemplates social expenditure of 45.8 per cent. of the State Budget, which includes wage increases for public sector employees and social benefit increases. The “protected” expenditure, including external debt service, wages for public employees and certain social benefit payments and payments for the implementation of measures relating to the preparation and hosting of the Euro-2012 Championship, total UAH 236.7 billion, or 77.5 per cent. of the State Budget.

The 2010 State Budget Law provides for expenditure of UAH 250.0 million for cash payouts to citizens compensating for lost savings deposited with the USSR State Savings Bank or invested in USSR state securities (as compared to UAH 650.0 million, UAH 6,400.0 million and UAH 250.0 million envisaged for this purpose by the 2007, 2008 and 2009 State Budget Laws, respectively). In 2009, actual expenditures for such purpose amounted to UAH 19.7 million (as compared to UAH 506.0 million and UAH 6,079.1 million directed for this purpose in 2007 and 2008, respectively). In 2009, a maximum of UAH 500 per depositor was reimbursed. In total, from 1997 through 2009, UAH 10,646.8 million were reimbursed. In the seven months ended 31 July 2010, no expenditures for this purpose were made from the State Budget.

Revenues

The following table sets forth sources of revenues of the Consolidated Budget for the years 2007 to 2009 and the seven months ended 31 July 2009 and 2010:

	Year ended 31 December			Seven months ended 31 July	
	2007	2008	2009	2009	2010
	<i>(in UAH millions)</i>				
Tax revenues	161,264.2	227,164.8	208,073.2	111,658.6	133,241.6
Direct taxes	76,025.8	106,457.4	92,068.6	49,236.1	55,470.5
<i>of which:</i>					
Personal income tax.....	34,782.1	45,895.8	44,485.3	25,008.8	27,528.1
Corporate income tax	34,407.2	47,856.8	33,048.0	16,270.9	18,867.6
Land tax	3,889.3	6,681.4	8,362.7	4,682.5	5,367.1
Property tax (motor vehicle tax)	1,354.6	1,558.4	1,538.3	848.3	1,132.6
Uniform tax for small business	1,592.6	1,854.4	1,766.3	999.5	1,045.9
Indirect taxes	79,830.8	118,190.2	114,008.5	61,241.6	76,650.0
<i>of which:</i>					
VAT	59,382.8	92,082.6	84,596.7	46,463.8	56,083.3
Excise tax on domestic goods	9,072.2	10,230.1	17,934.5	8,538.0	13,079.9
Excise tax on imported goods	1,495.5	2,553.0	3,690.0	1,944.6	2,502.5
Import duty	9,588.9	11,932.8	6,328.8	3,444.3	4,243.4
Export duty	291.4	197.4	382.7	231.3	187.6
Other taxes	2,820.0	2,517.2	1,996.2	1,180.9	1,121.1
Non-tax revenues	48,553.2	60,543.6	58,435.8	36,480.8	39,176.2
<i>of which:</i>					
Entrepreneurial and property income ..	13,214.0	22,468.7	17,062.6	11,858.5	18,407.1
Administrative fees and charges, non commercial sale income	2,963.5	3,037.0	2,719.0	1,568.6	1,469.6
Other non-tax revenue ⁽¹⁾	11,387.7	14,668.7	12,539.2	8,056.7	7,203.2
Capital revenue	6,373.4	6,702.4	3,653.1	1,745.6	1,868.4
Official transfers	104.5	135.2	645.3	91.7	104.5
Special funds	3,641.2	3,347.0	2,159.5	1,170.9	1,486.8
Payments to Fund of Social Insurance of Disabled of Ukraine	223.2	254.4	227.0	208.1	168.5
Collection for pollution of the environment	1,088.1	1,182.0	1,211.8	573.6	1,029.3
Special funds established by parliament of Autonomous Republic of Crimea and local self- governmental bodies and authorities	2,329.9	1,910.5	720.7	389.2	289.0
Total revenues	<u>219,936.5</u>	<u>297,893.0</u>	<u>272,967.0</u>	<u>151,147.6</u>	<u>175,877.4</u>

Note:

(1) Includes own source revenues of budgetary institutions and organisations and certain other items.

Source: Ministry of Finance

In 2008, tax revenues of the State Budget amounted to UAH 167.9 billion, or 97.8 per cent. of the target for 2008, an increase of 43.9 per cent., or UAH 51.2 billion, compared to 2007. In 2009, tax revenues of the State Budget amounted to UAH 148.9 billion, or 83.3 per cent. of the target for 2009, a decrease of 11.3 per cent., or UAH 19.0 billion, compared to 2008. In the seven months ended 31 July 2010, tax revenues of the State Budget amounted to UAH 96.5 billion, an increase by 22.9 per cent. as compared to the corresponding period in 2009. The increase in tax revenues in the seven months ended 31 July 2010 was largely due to an

increase of revenues from corporate income tax and excise tax by 16.5 per cent. and 46.5 per cent., respectively.

The high taxation of enterprises is one reason for the continuing importance of the shadow economy, which has impeded revenue collection. The overall State Budget tax arrears for 2009 increased by UAH 2.3 billion to UAH 10.9 billion at 31 December 2009, as compared to UAH 8.6 billion at 31 December 2008 and UAH 6.2 billion at 31 December 2007. State Budget tax arrears for the seven months ended 31 July 2010 decreased by UAH 0.4 billion as compared to 31 December 2009 to UAH 10.5 billion as at 31 July 2010.

As of 1 January 2004, the general corporate tax rate was reduced from 30 per cent. to 25 per cent. Enterprises in agriculture, space industry, publishing and certain other sectors enjoy preferential tax regimes. Starting from 2010, tax preferences were also introduced for producers and consumers of alternative energy and fuel sources; such preferences will remain effective for ten years. In addition to corporate taxes, firms have to pay additional contributions in an aggregate amount between 36.8 per cent. and 49.7 per cent. (depending on the risk level of the particular industry) of gross wages (of which 33.2 per cent. accounts for contributions to the pension fund with the remainder for the temporary disability social insurance fund, the unemployment insurance fund and the industrial accident social insurance fund). In addition, firms are required to withhold and remit 2.0 per cent. of the amount of gross taxable income of each employee to the pension fund, 0.5 to 1.0 per cent. of each employee's gross salary to the temporary disability social insurance fund and 0.6 per cent. to the unemployment insurance fund. The amount of annual wages used to calculate these mandatory contributions is capped. This cap is established by legislation and is subject to annual revision by Parliament. The cap is currently UAH 13,320 per employee and will be UAH 13,605 and UAH 13,830 per employee starting from 1 October and 1 December 2010, respectively. Pension fund duties are also levied on certain types of transactions such as the purchase and sale of fine jewellery (5 per cent.) or cars (3 per cent.).

Until 2004, individuals in Ukraine were subject to personal income tax at rates ranging from 10 per cent. to 40 per cent. Effective 1 January 2004, a flat tax of 13 per cent. was introduced for all levels of income. After 31 December 2006, this flat rate increased to 15 per cent. This resulted in an increase of the personal income tax revenues of the local budgets from UAH 22.8 billion in 2006 to UAH 34.8 billion in 2007 and UAH 45.9 billion in 2008. In 2009, personal income tax revenues of the local budgets decreased to UAH 44.5 billion. In the seven months ended 31 July 2010, personal income tax revenues of the local budgets amounted to UAH 27.5 billion.

VAT is currently assessed in Ukraine at a rate of 20 per cent. Because VAT serves an important macro-economic stabilisation role, the Government believes that collection of VAT should be assigned to the central Government. In accordance with this principle, VAT collection was shifted entirely to the central Government under the 1997 budget, and constituted approximately 40.3 per cent. of total revenues and 56.8 per cent. of total tax revenues of the 2009 State Budget and 41.2 per cent. of total revenues and 58.1 per cent. of total tax revenues for the seven months ended 31 July 2010.

Credits for VAT paid are available for exports. In the past, significant arrears owed to exporters for VAT refunds were addressed by the issuance of T-bills to exporters in 2004; no T-bills to securitise accumulated VAT refund arrears were issued in 2005-2009. The amount of VAT arrears to exporters for VAT refunds increased from UAH 11.7 billion as at 1 January 2009 to UAH 24.2 billion as at 1 January 2010 and to UAH 31.9 billion as at 1 August 2010. The 2010 State Budget Law provides for issuance in 2010 of T-bills to securitise accumulated VAT refund arrears. On 12 May 2010, the Government approved the procedure and the terms of issuance of such T-bills, which provide, among other things, that T-bills to exporters shall be issued with a five year maturity and a 5.5 per cent. interest rate. In the seven months ended 31 July 2010, no such T-bills were issued by the Ministry of Finance; however, in August 2010, the Ministry of Finance issued four tranches of T-bills to securitize VAT refund arrears in the aggregate amount of approximately UAH 16.4 billion.

In 2008 and 2009, a number of changes were introduced into Ukrainian tax laws in accordance with WTO requirements, including changes in taxation of dividends distributable through holding companies, abolition of customs duties, reductions in import duties for more than 2,500 goods and changes in the rates of licence charges for various activities. In addition, a number of tax incentives were introduced, including import duty exemptions for energy saving equipment and materials and equipment operating on non-traditional and

alternative energy sources. On 20 May 2010, Parliament passed a law increasing excise tax and import duties for a number of products, improving tax administration system and eliminating certain loopholes in tax legislation. Certain provisions of the new law came into effect on 16 June 2010, with others to become effective on various dates through 1 January 2011. The Government expects that implementation of the new law should allow increasing tax revenues of the State Budget.

The 2010 election programme of the President contemplated introduction of 5-year tax break for small business and decrease of the value added tax rate to 17 per cent. and the corporate income tax rate to 19 per cent. starting 2011, to be followed by a gradual decrease of the corporate income tax rate to 16 per cent. The 2010 President's election programme also contemplated adoption of the Tax Code of Ukraine.

In addition, pursuant to the Economic Reform Programme (see "*Economy of Ukraine – Action Programmes*"), the following main measures are proposed to be implemented within the framework of the tax system reform in 2010-2014:

- at the first stage which should be completed by the end of 2010, Ukraine should, among other things, develop and approve the Tax Code of Ukraine, securitise VAT refund arrears through an issuance of T-bills and ensure timely refund of VAT starting from 1 August 2010;
- at the second stage which should be completed by the end of 2012, Ukraine should further reduce the number of inefficient taxes and duties, introduce a single social contribution, real estate tax and new types of environmental taxes, and reform the system of the tax and duties administration;
- at the third stage which should be completed by the end of 2014, Ukraine should, among other things, gradually reduce the corporate income tax rate.

Further to the Economic Reform Programme, on 17 June 2010, Parliament approved in a first reading the draft Tax Code of Ukraine proposed by the Government. On 7 September 2010, Parliament cancelled its approval of the draft Tax Code in a first reading and instructed the Government to submit to Parliament a revised draft Tax Code taking into account comments received during the nationwide public discussions on the draft. On 7 October 2010, the draft Tax Code was approved by the Parliament in the first reading. The draft Tax Code remains to be approved by Parliament in a second, and, as the case may be, third reading, signed by the President and officially promulgated to become effective. The draft Tax Code aims to create a comprehensive legal framework for tax reform and provides for a wide range of changes in the existing tax system to improve tax collection and administration. Among other things, the draft Tax Code provides for a decrease of the corporate income tax rate from 25 per cent. to 19 per cent. from 1 January 2011, to be followed by a decrease to 18 per cent. from 1 January 2013, to 17 per cent. from 1 January 2015 and to 16 per cent. from 1 January 2016. The draft also provides for decreases of the general VAT rate to 17 per cent. from 1 January 2014. Furthermore, the draft envisages abolishment of a number of local taxes and duties, along with the introduction of certain new taxes at local level.

In addition, on 8 July 2010, Parliament approved a law that introduces, with effect from 1 January 2011, a single social contribution to replace the various social duties that are currently levied. This law aims to simplify the operation of the State social insurance system and provide for collection of insurance contributions by a single authority, the Pension Fund of Ukraine.

The Central-Local Fiscal Relationship

The following table sets forth the actual revenues, expenditures, deficit/surplus, and deficit/surplus as a percentage of GDP for the consolidated budget and the State Budget for 2007-2009 and data for the seven months ended 31 July 2009 and 2010:

	Year ended 31 December			Seven months ended 31 July	
	2007	2008	2009	2009	2010
	<i>(in UAH millions unless otherwise specified)</i>				
GDP	712,945	949,864	914,720	–	–
Consolidated Budget					
Revenues	219,936.5	297,893.0	272,967.0	151,147.6	175,877.4
Expenditures	226,054.4	309,203.7	307,399.4	167,854.2	202,088.4
Lending	1,583.9	2,813.8	2,825.8	1,130.6	938.0
Surplus (Deficit)	(7,701.7)	(14,124.5)	(37,258.1)	17,837.1	25,273.0
Surplus (Deficit)(% of GDP).....	(1.1)	(1.5)	(4.1)	–	–
State Budget					
Revenues	165,939.2	231,722.9	209,700.3	115,856.5	136,186.5
Expenditures	174,254.3	241,490.1	242,437.2	130,103.6	164,880.5
Lending	1,527.7	2,734.8	2,780.3	1,105.0	945.5
Surplus (Deficit)	(9,842.9)	(12,502.0)	(35,517.2)	15,352.1	27,748.5
Surplus (Deficit)(% of GDP).....	(1.4)	(1.3)	(3.9)	–	–

Source: Ministry of Finance

The Budget Code, which was initially adopted on 21 June 2001, governs the balance between the central budgets and local budgets and regulates payments from and to donor and recipient regions. According to the Budget Code, local budgets are established for the Autonomous Republic of Crimea and each of Ukraine's oblasts, cities, rayons and other administrative regions, as a result of which there are 691 local budgets to which direct transfers are made out of the State Budget. In addition, there are 11,341 local budgets of lower-level political subdivisions such as small towns, villages and settlements to which no direct transfers are made from the State Budget but which may receive central funds indirectly through transfers from the higher-level subdivisions. The Government is responsible for all expenditures that have a national scope, while local governments in Ukraine manage a significant portion of expenditure in the social sectors (including approximately 60 per cent. of education expenditure). Oblasts are responsible for expenditures whose benefit is regional (such as social protection), and rayons and cities are responsible for providing local goods and services, such as basic health and sanitation.

The 2001 Budget Code was an important step in modernising and improving the efficiency of allocating and administering budgetary funds. The Budget Code introduced a "formula method" that reallocates budget resources among oblasts on the basis of their population count through "interbudgetary transfers". This approach also provides an incentive for local governments to create their own tax bases, giving them the right to keep revenue from a variety of sources, including full entitlement to land tax and enterprise profit tax from communally owned enterprises. Another important revenue base for local budgets is personal income tax, which, together with the land tax, the Government estimates to account for approximately 89.8 per cent. of local revenues. In 2009, interbudgetary transfers from the State Budget to the local budgets amounted to UAH 62.2 billion. The 2010 State Budget Law provides for interbudgetary transfers from the State Budget to local budgets in the amount of UAH 78.1 billion. In the seven months ended 31 July 2010, interbudgetary transfers from the State Budget to the local budgets amounted to UAH 42.0 billion.

In 2007, the Cabinet of Ministers approved a Concept of Local Budget Reform. The Concept aims to strengthen the financial basis of local governments and the investment component of local budgets, to decentralise budget funds management, to improve the system of interbudgetary relations, to increase the efficiency of local budget funds management and to introduce medium-term planning of local budgets. In particular, pursuant to the Concept, an increase of the share of the local budgets in the consolidated budget

as well as optimal distribution of taxes and other revenues between State and local budgets are expected. The Concept also provides for re-allocation of revenues and expenditure among local budgets of different levels.

The Economic Reform Programme (see “*Economy of Ukraine – Action Programmes*”) also provides for implementation in 2010-2014 of a number of measures to improve the efficiency of inter-budgetary relations and increase revenues of the local budgets. These measures include:

- transfer to local budgets of certain additional revenues, such as revenues from charges for use of natural resources, state registration, licensing and certification;
- reform of local taxes and duties (including abolishment of inefficient taxes and improvement of the tax administration);
- introduction of a property tax, which will contribute to local budget revenues;
- simplification of borrowing procedures for local authorities;
- introduction of medium-term planning for local budgets; and
- development of legislation governing external audit of local budgets.

On 8 July 2010, Parliament approved a restatement of the Budget Code of Ukraine, which provides for the implementation of a number of measures set forth in the Economic Reform Programme with respect to inter-budgetary relations. See “*Public Finance – Budget Process*”.

Local authorities are permitted to incur general fund budget deficits up to the amount of any remaining balance of funds in the preceding year. In addition, the Autonomous Republic of Crimea and municipalities are permitted to incur special fund budget deficits, which can be financed by internal borrowings, whilst cities with populations greater than 800,000 are also permitted to incur external debt. Both internal and external borrowings by the Autonomous Republic of Crimea and municipalities may be made only for specific projects. So far, only the city of Kyiv and the city of Odessa have issued external debt. Any borrowings by local authorities are subject to prior review of the Ministry of Finance for compliance with applicable budgetary legislation.

All levels of sub-national government are involved in the social sector, although the level of service differs. Cities and rayons provide communal services, garbage and sanitation, housing and transportation. Sub national governments also manage a number of companies that are in the process of being privatised, such as hotels and restaurants.

PUBLIC DEBT

General

The high fiscal deficits of 1991-1995 were financed predominantly by direct central bank credits to the Government, which increased the money supply and, together with other factors, contributed to the hyperinflation experienced during that period. The deficits were also financed by arrears on energy imports from Russia and Turkmenistan. The emergence of a Treasury bill market in March 1995, and the release of IMF and other official Western funds, as well as bond issues in the international capital markets, made it possible to finance the deficit increasingly by non-inflationary means. While in 1995 72.7 per cent. of the budget deficit (amounting to 6.6 per cent. of GDP) was financed by the NBU, with the rest coming from the issue of treasury bills, foreign grants and loans, by 1998, the share of NBU financing of the deficit fell to just 0.8 per cent. In 1999, the NBU ceased the practice of providing direct financing of the budget. Currently, budget deficits are funded by a combination of debt financing and privatisation proceeds.

Historically, the State and state-owned enterprises have accumulated significant arrears to employees, including for social benefits. However, when calculating its public debt figures (including for the purposes of this section), Ukraine takes into account only liabilities of the State (Central Government) for which specific bonds or loans have been issued. Furthermore, data relating to borrowings and repayments in this section do not include borrowings disbursed to the special fund of the State Budget in 2010 and previous years and repayments from the special fund of the State Budget. See “– *Special Fund Borrowings*”. However, data relating to outstanding state debt includes the debt raised in such borrowings. In addition, in certain of the tables below, borrowings, outstanding state debt and debt servicing data are presented excluding debt owed to the IMF that is accounted for as a liability of the NBU as opposed to debt owed to the IMF that is accounted for as a direct debt of the Government. See the relevant tables and notes thereto for more information. For the purposes of this Prospectus, ratios of total debt and/or State external debt to GDP were calculated based on nominal GDP converted into U.S.\$ using the period end exchange rates specified under the heading “*The Monetary System – Exchange Rates.*”

As at 1 August 2010, the total outstanding debt obligations of the State were approximately U.S.\$45.9 billion, including approximately U.S.\$33.9 billion in State debt (direct debt) and approximately U.S.\$12.0 billion in State-guaranteed debt (contingent liabilities).

The following table sets forth the total outstanding debt obligations of the State at the end of the periods indicated:

	Year ended 31 December			Seven months ended 31 July
	2007	2008	2009	2010
	<i>(in U.S.\$ billions)</i>			
Total debt	17.57	24.60	39.69	45.87
State debt (direct debt)	14.12	16.97	28.43	33.86
Internal debt (direct debt) ⁽¹⁾	3.53	5.80	11.41	14.35
External debt (direct debt)	10.59	11.17	17.02	19.50
<i>of which: debt to the IMF owed by the Government....</i>	–	–	6.82	7.64
State-guaranteed debt (contingent liabilities)	3.45	7.63	11.26	12.02
Internal debt ⁽¹⁾	0.20	0.26	1.76	1.75
External debt	3.26	7.37	9.50	10.27
<i>of which: debt to the IMF owed by the NBU</i>	0.43	4.71	6.07	6.90

Notes:

(1) Hryvnia amounts have been converted to dollar amounts using the period-end exchange rate specified under the heading “The Monetary System – Exchange Rates”.

Source: Ministry of Finance

The following table sets forth Ukraine's total State debt service and total State borrowings (not including contingent liabilities and debt to the IMF owed by the NBU) for the periods indicated:

	Year ended 31 December			Seven months ended 31 July
	2007	2008	2009	2010
Total State debt service	1,848	1,705	5,014	2,657
Internal State debt service ⁽¹⁾	616	808	2,846	2,204
Principal	469	653	2,254	1,529
Interest.....	147	155	592	675
External State debt service	1,232	897	2,168	454
Principal	716	358	1,609	216
<i>of which: debt to the IMF owed by the Government</i>	—	—	—	—
Interest.....	516	539	559	238
<i>of which: debt to the IMF owed by the Government</i>	—	—	58	51
Total State borrowings	1,907	3,728	14,625	4,591
Internal borrowing ⁽¹⁾	707	2,930	7,473	2,591
External borrowing	1,200	798	7,152	2,000
Securities issued by the State	1,200	—	—	—
Multilateral creditors.....	—	798	7,152	—
<i>of which: IMF loans to the Government</i>	—	—	6,753	—

Notes:

- (1) Hryvnia amounts have been converted to dollar amounts using the official exchange rate set by the NBU as at the date when relevant payment was made.

Estimated State Debt Service for 2010-2013⁽¹⁾

	2010 ⁽²⁾	2011 ⁽³⁾	2012 ⁽³⁾	2013 ⁽³⁾
	<i>(in U.S.\$ billions)</i>			
Principal payments	2,876.9	3,438.5	3,484.7	4,851.6
Internal debt ⁽⁴⁾	2,132.7	2,420.2	1,765.1	856.4
External debt	744.2	1,018.3	1,719.6	3,995.4
Interest payments	1,775.3	2,067.9	1,773.8	1,472.1
Internal debt ⁽⁴⁾	1,270.6	1,525.9	1,208.4	912.3
External debt	504.7	542.0	565.4	559.8
Total payments	4,652.2	5,506.4	5,258.5	6,323.7

Notes:

- (1) Estimates as at 1 August 2010, excluding contingent liabilities and debt to the IMF, which is accounted for as a liability of the NBU.
(2) As approved by the 2010 State Budget Law.
(3) Excluding future borrowings and payments under service agreements.
(4) Hryvnia amounts have been converted to dollar amounts using assumed average UAH/U.S.\$ exchange rate of UAH 8.0 = U.S.\$1.00 for 2010-2011 and assumed average UAH/U.S.\$ exchange rate of UAH 7.5 = U.S.\$1.00 for 2012-2013.

Source: Ministry of Finance

Total debt of Ukraine as a percentage of GDP, including both State debt (direct debt) and State guaranteed debt (contingent liabilities), was 12.3 per cent. at the end of 2007, 20.0 per cent. at the end of 2008 and 34.6 per cent. at the end of 2009. The significant increase in the ratio of total debt to GDP in 2009 was largely attributable to a significant increase in debt raised from the IMF, the need to finance budget deficit of UAH

31.6 billion in 2009, the need to finance the bank and Naftogas recapitalisation programme in the amount of UAH 44.0 billion in 2009, as well as to an increase in contingent liabilities.

The Government expects total debt of Ukraine as a percentage of GDP, including both State debt (direct debt) and State-guaranteed debt (contingent liabilities), to increase to 39.1 per cent. by the end of 2010 and then decrease to 36.1 per cent. by the end of 2011. This expected increase in the ratio of total debt of Ukraine to GDP in 2010 is expected to be largely attributable to the need to finance expected budget deficit of UAH 52.9 billion in 2010, the need to finance the bank recapitalisation programme in the planned amount of UAH 30.0 billion, as well as to an increase in contingent liabilities. Of these amounts, State external debt (direct debt) as a percentage of GDP was 7.4 per cent. at the end of 2007, 9.1 per cent. at the end of 2008, 14.9 per cent. at the end of 2009 and, as at 31 July 2010, is expected by the Government to be approximately 15.6 per cent. at the end of 2010 and 15.3 per cent. by the end of 2011. The ratio of State external debt service (including principal and interest payments but excluding debt owed to the IMF by the NBU) to GDP was approximately 0.9 per cent. at the end of 2007, approximately 0.5 per cent. at the end of 2008, approximately 1.9 per cent. at the end of 2009 and, as at 31 July 2010, is expected by the Government to be approximately 2.6 per cent. at the end of 2010 and approximately 1.1 per cent. at the end of 2011.

The 2008 State Budget Law provided for expected total state debt service payments (including principal and interest payments but excluding debt owed to the IMF by the NBU) to be in an amount of UAH 9,918.7 million in 2008, 50.4 per cent. (or UAH 5,003.1 million) of which were internal debt payments and 49.6 per cent. (or UAH 4,915.6 million) of which were external debt payments (equal to U.S.\$963.8 million at an exchange rate of UAH 5.1 = U.S.\$1.00). State borrowings for 2008 were planned in the amount of approximately UAH 14,134.0 million or UAH 4,307.7 million more than the amended plan for 2007, including external borrowings to the general fund amounting to UAH 6,358.0 million (an increase of UAH 361.4 million from that planned for 2007) and internal borrowings to the general fund amounting to approximately UAH 7,776.0 million (an increase of UAH 3,946.2 million from that planned for 2007). Actual state borrowings in 2008 amounted to UAH 26,612.6 million or 88 per cent. more than the amended plan for 2008, including external borrowings to the general fund amounting to UAH 5,396.5 million (15 per cent. less than was planned for 2008) and internal borrowings to the general fund amounting to approximately UAH 21,216.2 million (173 per cent. more than was planned for 2008). Pursuant to the 2008 State Budget Law, external and internal borrowings were expected to amount to 20 per cent. and 80 per cent. of total borrowings, respectively. Actual external and internal borrowings in 2008 amounted to 20.3 per cent. and 79.7 per cent. of total borrowings, respectively.

The 2009 State Budget Law provided for expected total state debt service payments (including principal and interest payments but excluding debt owed to the IMF by the NBU) to be in an amount of UAH 40,941.9 million in 2009, 56.9 per cent. (or UAH 23,314.1 million) of which were internal debt payments and 43.1 per cent. (or UAH 17,627.7 million) of which were external debt payments (equal to U.S.\$2,350.4 million at an exchange rate of UAH 7.5 = U.S.\$1.00). State borrowings for 2009 were planned in the amount of approximately UAH 80,037.5 million, or UAH 65,903.5 million more than the amended plan for 2008, including external borrowings to the general fund amounting to UAH 14,625.0 million (an increase of UAH 8,267.0 million from that planned for 2008) and internal borrowings to the general fund amounting to approximately UAH 65,412.5 million (an increase of UAH 57,636.5 million from that planned for 2008). Actual state borrowings in 2009 amounted to UAH 113,851.3 million or 42.2 per cent. more than the amended plan for 2009, including external borrowings for the general fund amounting to UAH 55,726.2 million (281 per cent. more than was planned for 2009) and internal borrowings to the general fund amounting to approximately UAH 58,125.1 million (11.1 per cent. less than was planned for 2009). As planned, the actual amount of internal borrowings raised in 2009 for the purpose of the banking system and Naftogas recapitalisation was UAH 44.0 billion. In 2009, it was expected that external and internal borrowings would amount to 18.3 per cent. and 81.7 per cent. of total borrowings, respectively. Actual external and internal borrowings in 2009 amounted to 48.1 per cent. and 51.9 per cent. of total borrowings, respectively.

The 2010 State Budget Law provides for expected total state debt service payments (including principal and interest payments but excluding debt owed to the IMF by the NBU) to be in an amount of UAH 37,218.1 million in 2010, 73.2 per cent. (or UAH 27,226.9 million) of which are internal debt

payments and 26.8 per cent. (or UAH 9,991.2 million) of which are external debt payments (equal to U.S.\$1,248.9 million at an exchange rate of UAH 8.0 = U.S.\$1.00). State borrowings for 2010 were initially planned in the amount of approximately UAH 78,253.3 million, or UAH 1,784.2 million less than the amended plan for 2009, including external borrowings to the general fund amounting to UAH 30,400.0 million (an increase of UAH 15,775.0 million from that planned for 2009) and internal borrowings to the general fund amounting to approximately UAH 47,853.3 million (a decrease of UAH 17,559.2 million from that planned for 2009). The planned amount of internal borrowings included borrowings for the purpose of the banking system recapitalisation amounting to approximately UAH 30.0 billion. Pursuant to the 2010 State Budget Law, external and internal borrowings were initially planned to amount to 38.8 per cent. and 61.2 per cent. of total borrowings, respectively.

On 8 July 2010, Parliament approved the State Budget Amendment providing for an increase in the aggregate amount of internal borrowings to the general fund of the State Budget in 2010 of approximately UAH 5,100.0 million, to UAH 52,953.3 million. At the same time, planned borrowings to the special fund of the 2010 State Budget were decreased by the same amount. See “-*Special Fund Borrowings*”. Pursuant to the State Budget Amendment, aggregate planned State borrowings to the general fund of the 2010 State Budget were increased to approximately UAH 83,353.3 million, or UAH 3,315.8 million more than in the amended plan for 2009, and internal and external borrowings to the general fund 2010 State Budget are planned to amount to 36.5 per cent. and 63.5 per cent. of total borrowings, respectively. On 23 September 2010, Parliament approved an amendment to the 2010 State Budget Law providing for an increase in the ceiling on state debt up to UAH 315,715,906.3 thousand to provide for the planned amount of internal borrowings for the purpose of the Naftogas recapitalization in the amount of UAH 7,400.0 million. As a result, aggregate planned State borrowings to the general fund of the 2010 State Budget were increased to approximately UAH 90,753.3 million.

The Government is continuously taking measures to increase the efficiency of state debt management, including through further development of domestic market for state securities. In 2009, a number of regulations were enacted for this purpose, including the Concept for Development of the Domestic Market for State Securities for 2009-2013 and Regulations on the Implementation of the Primary Dealer Institute in the State Securities Market. The Concept for Development of the Domestic Market for State Securities for 2009-2013 provides for the implementation of the following measures: introduction of market pricing at T-bills placements; broadening the scope of state borrowing instruments; creation of the state securities primary dealer system; enhancing transparency of state borrowings; timely placement of idle State Budget funds; and improvement of state debt risk management. Pursuant to the Concept, starting from 14 May 2009, the market pricing mechanism has been introduced at the primary placements of T-bills. In 2009 and in the eight months ended 31 August 2010, five primary dealer tenders were held and fifteen banks were selected as state securities primary dealers. Since 19 February 2010, T-bills in the primary market have been sold only to such primary dealers. In addition, T-Bills may be sold in the primary market to the NBU acting on instruction and at the expense of its clients.

The draft 2011 State Budget Law that is currently being prepared by the Ministry of Finance provides for expected total state debt service payments (including principal and interest payments but excluding debt owed to the IMF by the NBU) to be in an amount of UAH 69,371.7 million in 2011, 78.5 per cent. (or UAH 54,467.2 million) of which are internal debt payments and 21.5 per cent. (or UAH 14,904.5 million) of which are external debt payments (equal to U.S.\$1,874.8 million at an exchange rate of UAH 7.95 = U.S.\$1.00). According to the draft 2011 State Budget Law, state borrowings to the general fund of the State Budget for 2011 are planned in the amount of approximately UAH 79,401.3 million, or UAH 3,952.0 million less than the amended plan for 2010, including external borrowings to the general fund amounting to UAH 27,825.0 million (a decrease of UAH 2,575.0 million from that planned for 2010) and internal borrowings to the general fund amounting to approximately UAH 51,576.3 million (a decrease of UAH 1,377.0 million from that planned for 2010). Pursuant to the draft 2011 State Budget Law, external and internal borrowings are planned to amount to 37.9 per cent. and 62.1 per cent. of total borrowings, respectively.

Internal Debt

Internal debt of Ukraine comprises three categories: (i) securities issued by the State (T-bills and other obligations); (ii) rescheduled Government debt owed to the NBU; and (iii) State-guaranteed debt (including obligations guaranteed by the State and Government bonds issued during the Soviet period).

The State Budget Law contains a specific line item setting forth the ceiling for State internal debt (direct debt) or, alternatively, a combined State internal and external debt (direct debt) to be issued for each year, although the 2010 State Budget Law permits additional borrowings by the Government (i) if privatisation receipts are below expectations, up to the amount of the shortfall, and (ii) in certain other cases, including, among other things, for the purposes of banks' recapitalisation, financial assistance to banks, increase of statutory capital of the State Mortgage Institution, granting loans to the Fund for the Guaranteeing of Deposits of Individuals (the "Fund") and Agrarian Fund. In addition, the 2010 State Budget Law allows the Government to change borrowing sources (from external to internal or vice versa) provided that the combined limit on State debt is complied with.

The following table sets forth the total outstanding internal debt obligations of the State and the ceiling on internal debt under the budget at the end of the periods indicated:

	Year ended 31 December			Seven months ended 31 July
	2007	2008	2009	2010
	<i>(in UAH thousands)</i>			
State internal debt (direct debt)	17,806,386.3	44,666,547.6	91,070,076.8	113,290,212.8
<i>of which:</i>				
Obligations under T-bills	9,146,565.7	33,521,860.4	87,631,511.0	109,917,773.5
Obligations to the NBU ⁽¹⁾	8,659,820.7	11,144,687.2	3,438,565.8	3,372,439.3
State-guaranteed debt (contingent liabilities)	1,000,966.3	2,000,966.3	14,062,842.6	13,833,409.5
Total internal debt	18,807,352.6	46,667,513.9	105,132,919.4	127,123,622.3
Budget ceiling for State internal debt (direct debt) ⁽²⁾	20,274,714.9	89,138,062.3 ⁽³⁾	193,076,747.3 ⁽⁴⁾	315,715,906.3 ⁽⁵⁾

Notes:

- (1) Including debt owed to the NBU undertaken to finance the budget deficits in 1994-1996, which debt was restructured in April 2000.
- (2) Including hryvnia-denominated and dollar-denominated state internal debt. The dollar-denominated state internal debt is converted to hryvnia at the exchange rate assumed for purposes of the law "On the State Budget of Ukraine" for the relevant year. See "Public Finance and Fiscal Policy — Consolidated Budget".
- (3) In accordance with the 2008 State Budget Law, the ceiling on state debt was set at UAH 89,138,062.3 thousand, not sub-divided into internal and external state debt.
- (4) In accordance with the 2009 State Budget Law, the ceiling on state debt is set at UAH 193,076,747.3 thousand, not sub-divided into internal and external state debt.
- (5) In accordance with the 2010 State Budget Law, the ceiling on state debt is set at UAH 315,715,906.3 thousand, not sub-divided into internal and external state debt.

Source: Ministry of Finance

As at 31 December 2007, 2008, 2009 and 1 August 2010, the ratio of State internal debt (direct debt) to total State internal and external debt (direct debt) was approximately 25.0 per cent., 34.2 per cent., 40.1 per cent. and 42.4 per cent., respectively.

In 2007 and 2008 the Government placed new T-bills in the amount of UAH 3.6 billion and UAH 21.2 billion, respectively. In 2009, the Government placed new T-bills in the amount of UAH 62.8 billion (not including T-bills issued in exchange of debt to the NBU). In the seven months ended 31 July 2010, the Government placed new T-bills in the amount of UAH 25.4 billion. The Government also issued guarantees for the aggregate amount of UAH 3.0 billion debt of the State Mortgage Institution in 2006-2008, and guarantees to several state aviation enterprises under domestic bonds issued in the aggregate amount of UAH 2.5 billion in 2009.

The total amount of State internal debt (direct debt) was UAH 17.8 billion as at 31 December 2007, UAH 44.7 billion as at 31 December 2008, UAH 91.1 billion as at 31 December 2009 and UAH 113.3 billion as at 31 July 2010. The 2009 State Budget Law limited State debt (direct debt) at 31 December 2009 to UAH 193.1 billion without breakdown for internal and external State debt. The 2010 State Budget Law limits State debt (direct debt) at 31 December 2010 to UAH 308.3 billion without breakdown for internal and external State debt.

In April 2000, the debt owed to the NBU undertaken to finance the State Budget deficits in 1994-1996 was recognised as State debt and restructured. The restructuring provided for repayments of maturing principal in the aggregate amount of U.S.\$1.18 billion between 2002 and 2009 and UAH 3.44 billion between 2010 and 2035. In 2004, the NBU and the Government further restructured the U.S.\$1.18 billion of State debt in 2004; the Government paid U.S.\$133 million of this debt to the NBU in 2004, U.S.\$50 million in each of the years from 2005 through 2007 and U.S.\$33.1 million in 2008. At the end of 2009, new T-bills maturing in 2012 and 2014 were issued in exchange for the remaining state debt to the NBU restructured in 2004 in the amount of U.S.\$1,000.8 million. From 2010, the Government also started repayment of UAH 3.44 billion of debt to the NBU. As of 1 August 2010, the outstanding amount of this debt owed to the NBU was UAH 3.37 billion.

The average annual weighted T-bill yield, based on the actual volumes of T-bill proceeds, was 6.7 per cent. in 2007, 11.9 per cent. in 2008 and 12.2 per cent. in 2009. The average annual weighted T-bill yield, based on the actual volumes of T-bill proceeds, was 13.2 per cent. in the seven months ended 31 July 2010 and the average annual weighted T-bill yield, based on the nominal value of the placed T-bills, was 13.3 per cent. in this period. The average annual weighted yield of T-bills that were issued for the purpose of the recapitalisation of banks was 9.5 per cent. in each of 2008 and 2009 and the seven months ended 31 July 2010. The average annual weighted yield, based on the actual volumes of T-bill proceeds, of T-bills that were sold at the primary auctions to market participants was 20.1 per cent. and 14.1 per cent. in 2009 and the seven months ended 31 July 2010, respectively, and their average annual weighted yield, based on the nominal value of the placed T-bills, was 20.2 per cent. and 14.1 per cent. in 2009 and the seven months ended 31 July 2010, respectively.

Currently, the demand for T-bills from non-residents is insignificant. As at 1 August 2010, non-residents held approximately 3.7 per cent. of all outstanding T-bills, in the aggregate amount of approximately UAH 3.9 billion. The Government is aware of the inflationary pressures and instability that non-resident investment in T-bills can create in the money market and such investment is therefore subject to certain restrictions under Ukrainian legislation.

To diversify domestic financing streams, Ukraine issued two tranches of State saving bonds in 2002 in a nominal amount of UAH 50 million each. In 2003, a further UAH 50.0 million of savings bonds were issued, with their placement being completed during 2004. In 2004, a further UAH 47.0 million of savings bonds were issued. These instruments were not issued in 2005-2008. In 2009, however, the Government recommenced the issuance of savings bonds. In particular, the Government launched sales to the public of a first series of savings bonds in an aggregate nominal amount of UAH 200 million beginning 23 September 2009 and UAH 1.6 million of such bonds were sold to the public as at 1 August 2010.

The table below sets forth the total amount of State internal borrowings from T-bills and State savings bonds issued in each of the years 2007 to 2009 and the seven months ended 31 July 2010:

	Year ended 31 December			Seven months ended 31 July
	2007	2008	2009	2010
Security (Maturity)	<i>(in UAH thousands)</i>			
T-bills (twelve-year maturity)	–	–	1,500,000.0	1,500,000.0
T-bills (eleven-year maturity)	–	–	3,850,000.0	3,849,981.0
T-bills (ten-year maturity)	–	–	10,217,189.0	16,607,188.0
T-bills (nine-year maturity)	–	–	18,470,748.0	18,470,748.0
T-bills (eight-year maturity)	–	–	9,316,198.0	9,316,198.0
T-bills (seven-year maturity)	–	17,470,000.0	17,470,000.0	17,470,000.0
T-bills (five-year maturity)	249,000.0	2,887,145.8	8,108,003.0	6,979,003.0
T-bills (four-year maturity)	–	223,788.1	–	–
T-bills (three-year maturity)	2,017,000.0	–	9,427,995.0	15,099,850.0
T-bills (two-year maturity)	–	–	665,800.0	3,355,188.0
T-bills (18-month maturity)	1,307,000.0	–	–	800,000.0
T-bills (12-month maturity)	–	–	4,540,152.0	9,778,841.0
T-bills (9-month maturity)	–	–	130,000.0	2,376,010.0
T-bills (6-month maturity)	–	18,913.4	3,744,865.0	2,895,000.0
T-bills (3-month maturity)	–	616,315.9	189,142.0	1,418,200.0
State savings bonds (1 year maturity)	–	–	1,419.0	1,566.5

Source: Ministry of Finance

External Debt

External debt of Ukraine comprises five categories: (i) securities (Eurobonds) issued by the State, (ii) loans from international financial organisations, (iii) loans from foreign governments, (iv) loans from foreign banks, and (v) State-guaranteed debt (including obligations under external loans guaranteed by the State).

At the end of 2007, Ukraine's external debt was approximately U.S.\$13.9 billion, including State debt (direct debt) of U.S.\$10.6 billion and State-guaranteed debt of U.S.\$3.3 billion. At the end of 2008, Ukraine's external debt was approximately U.S.\$18.6 billion, including State debt (direct debt) of U.S.\$11.2 billion and State-guaranteed debt of U.S.\$7.4 billion. At the end of 2009, Ukraine's external debt was approximately U.S.\$26.5 billion, including State debt (direct debt) of U.S.\$17.0 billion and State-guaranteed debt of U.S.\$9.5 billion. As at 31 July 2010, Ukraine's external debt was approximately U.S.\$29.8 billion, including State debt (direct debt) of U.S.\$19.5 billion and State-guaranteed debt of U.S.\$10.3 billion. The limit for State debt (direct debt) at the end of 2010 has been set by the 2010 State Budget Law at UAH 308.3 billion without breakdown for internal and external State debt.

The tables below set forth Ukraine's (i) public external debt structure as at 31 December 2007, 2008, 2009 and 31 July 2010; (ii) actual and estimated external debt service for the year 2010; (iii) estimated payments of State external debt service for the years 2011 to 2019; and (iv) estimated IMF debt service for 2010-2014:

Public External Debt Structure as at 31 December 2007, 2008, 2009 and 31 July 2010

	As at 31 December			As at
	2007	2008	2009	31 July
	<i>(in U.S.\$ thousands)</i>			
State external debt (direct debt)	10,591,661.8	11,171,831.4	17,022,696.3	19,503,835.2
<i>of which:</i>				
Multilateral borrowings (IFI loans).....	2,483,678.5	3,189,090.4	8,486,433.4	9,223,330.0
<i>of which:</i>				
European Union.....	42,606.8	20,442.1	–	–
EBRD	202,956.9	265,800.2	342,574.2	322,040.4
EIB.....	–	–	97,498.4	88,869.2
debt to the IMF owed by the				
Government	–	4,899,032.9	5,770,358.2	–
World Bank	2,238,114.8	2,902,848.1	3,147,327.9	3,042,062.3
Bilateral borrowings	1,936,412.5	1,724,772.0	1,570,533.2	1,427,899.2
<i>of which:</i>				
Russia	1,290,105.9	1,192,355.9	1,094,605.8	996,885.9
USA	154,359.3	125,937.6	99,699.9	89,779.8
France	18,572.6	14,851.4	12,083.3	9,637.2
Japan	78,874.6	74,029.4	104,395.8	122,294.5
Germany	326,445.3	262,365.4	215,084.1	172,463.9
Italy	68,054.9	55,232.3	44,664.3	36,867.9
SDR allocations received to the				
State Budget.....	–	–	1,925,124.0	1,864,736.8
Loans from foreign banks ⁽¹⁾	75.1	72.1	73.3	2,000,066.8
State External Bonds 2003	1,000,000.0	1,000,000.0	1,000,000.0	1,000,000.0
State External Bonds 2004	1,100,000.0	1,100,000.0	600,000.0	600,000.0
State External Bonds 2005	881,520.0	845,880.0	860,280.0	784,140.0
State External Bonds 2006	1,989,975.7	2,112,016.8	1,380,252.3	1,403,662.5
State External Bonds 2007	1,200,000.0	1,200,000.0	1,200,000.0	1,200,000.0
Limit of state external debt (direct debt)				
under the State Budget Law as of				
31 December each year⁽²⁾	9,890,764.5(3)	17,478,051.0(4)	25,743,566.3(4)	38,539,488.3(4)
State-guaranteed external debt				
(contingent liabilities)	3,257,326.2	7,366,204.0	9,495,987.9	10,265,289.58
<i>of which:</i>				
Multilateral borrowings (IFI loans).....	665,090.4	5,020,310.4	6,441,086.7	7,126,609.4
<i>of which:</i>				
European Atomic Energy Community ..	57,298.8	74,233.1	77,549.7	69,636.59
EBRD.....	124,998.8	158,229.8	173,578.4	162,489.77

	As at 31 December			As at
	2007	2008	2009	31 July
<i>(in U.S.\$ thousands)</i>				
debt to the IMF owed by the NBU	431,252.4	4,709,040.6	6,074,800.9	6,757,393.1
World Bank	51,540.5	78,806.9	115,157.7	137,089.9
Bilateral borrowings ⁽⁵⁾	11,102.1	1,991.3	–	45,944.0
Loans from foreign banks	1,790,300.4	1,686,402.4	650,579.6	613,734.5
Other	790,833.3	657,500.0	2,404,321.7	2,479,001.7
Total external debt	13,848,988.0	18,538,035.4	26,518,684.2	29,769,124.8

Notes:

- (1) Figures include DM 100,000 aggregate principal amount of 16 per cent. Notes due 2001 issued on a fiduciary basis by Chase Manhattan Bank Luxembourg S.A. and supported by a fiduciary loan agreement with Ukraine in the same principal amount, as each of the foregoing may be amended from time to time.
- (2) Hryvnia amounts have been converted to dollar amounts at the exchange rate assumed for purposes of the law "On the State Budget of Ukraine" for the relevant year. See "Public Finance and Fiscal Policy – Consolidated Budget".
- (3) The 2007 Budget Law allowed the Government to exceed the limit of State external direct debt if the privatisation receipts were below expectations or if the limit on State internal debt remained unused.
- (4) The 2008, 2009 and 2010 State Budget Law limit State debt at 31 December 2008, 31 December 2009 and 31 December 2010 to UAH 89,138,062.3 thousand, UAH 193,076,747.3 thousand and UAH 315,715,906.3 thousand, respectively, without explicit breakdown for internal and external State debt.
- (5) Bilateral borrowings are represented by debt owed to the Federal Republic of Germany.

Source: Ministry of Finance

Actual and Estimated External Debt Service for 2010

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.	Total
<i>(in U.S.\$ millions)⁽¹⁾</i>													
State external debt													
(direct debt)	53.4	56.4	32.3	67.0	113.2	86.7	44.2	69.2	32.8	106.9	131.6	2,665.1	3,459.8
Interest	9.4	33.4	22.6	9.0	84.6	71.3	8.0	38.31	22.83	50.0	98.4	257	704.8
debt to the IMF owed by													
the Government	0.0	25.5	0.9	0.0	24.6	0.0	0.0	31.5	0.0	0.0	32.7	0.0	115.2
Principal	44.0	23.0	9.7	58.0	28.6	16.3	36.2	30.9	10.0	56.9	33.3	2,408.1	2,754.9
debt to the IMF owed by													
the Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Payments to IMF													
(debt of the NBU)	0.0	19.0	0.0	0.1	33.2	0.0	0.0	18.7	0.0	0.0	19.2	0.0	90.2

Notes:

- (1) Repayment amounts are actual for January – July and estimated for August – December and in total. Figures do not include any borrowings that have been or will be raised after 31 July 2010. SDR amounts have been converted to dollar amounts as of the maturity date. The assumed average 2010 exchange rate of SDR is 0.67=U.S.\$1.00.

Estimated State External Debt Service for 2011-2019⁽¹⁾

	2011	2012	2013	2014	2015	2016	2017	2018	2019
<i>(in U.S.\$ millions)</i>									
State external debt									
(direct debt) ⁽²⁾	1,560.3	2,285.0	4,555.1	2,846.2	1,883.1	1,593.1	1,535.4	460.8	389.5
Interest	542.0	565.4	559.8	392.6	314.8	255.0	176.9	117.5	105.4
Principal	1,018.3	1,719.6	3,995.3	2,453.6	1,568.3	1,338.1	1,358.5	343.3	284.1

Note

- (1) Estimates as at 1 August 2010, excluding any borrowings that have been or will be raised after 31 July 2010 and payments under service agreements.
- (2) Excluding debt owed to the IMF and accounted for as a liability of the NBU.

Source: Ministry of Finance

As at 31 July 2010, the amount of State external debt service payments (including principal and interest payments but excluding debt owed to the IMF by the NBU) is expected to increase significantly in 2013 to U.S.\$4,555.1 million, largely due to scheduled repayment in 2013 of debt owed to the IMF by the Government in the amount of U.S.\$2,569.2 million and redemption of U.S.\$1,000.0 million 7.65 per cent. notes due 2013.

Estimated IMF Debt Service for 2010-2014⁽¹⁾

	2010 ⁽²⁾	2011 ⁽³⁾	2012 ⁽³⁾	2013 ⁽³⁾	2014 ⁽³⁾
	<i>(in U.S.\$ millions)</i>				
Total debt to IMF	205.4	309.5	3,774.4	5,846.4	2,578.1
Debt of the Government	115.2	145.1	937.8	2,755.1	2,232.3
Interest	115.2	145.1	133.4	185.9	72.6
Principal.....	–		804.4	2,569.2	2,159.7
Debt of the NBU	90.2	164.4	2,836.6	3,091.3	345.9
Interest	90.2	164.4	155.3	68.8	4.6
Principal.....	–		2,681.3	3,022.5	341.3

Notes:

- (1) Excluding future borrowings and payments under service agreements.
- (2) SDR amounts have been converted to dollars using an assumed average full-year 2010 exchange rate of SDR 0.67 – U.S.\$1.00.
- (3) SDR amounts have been converted to dollars using an assumed average 2011-2017 exchange rate of SDR 1.56 – U.S.\$1.00.

Source: Ministry of Finance

Commercial Creditors

In August and October 1997, the Ministry of Finance raised a total of U.S.\$559 million through the issue of bonds in the international capital markets. In addition, UAH 750 million of T-bills were sold to foreign investors in December 1997. In 1998, the Government issued a DM 1.5 billion eurobond that matured in February 2001 and a €500 million eurobond maturing in March 2000. A further U.S.\$503 million issue that matured in September 2000 consisted of restructured T-bills, previously held by foreign investors.

In early 2000, Ukraine found itself in a critical financial position. Ukraine's external debt, which amounted to U.S.\$11.5 billion at the end of 1998, equivalent to approximately 37.9 per cent. of GDP, had grown to U.S.\$12.5 billion as of 31 December 1999, equivalent to approximately 40.1 per cent. of GDP. With foreign exchange reserves of approximately U.S.\$1.04 billion at the end of 1999, Ukraine was scheduled to pay more than U.S.\$3.0 billion in debt servicing in 2000 and a further U.S.\$2.8 billion in 2001. The contribution of scheduled debt service payments falling due in 2000 and 2001, combined with inadequate levels of foreign exchange reserves and its inability to obtain financing from the international capital markets, prompted Ukraine to undertake a comprehensive debt restructuring in which notes representing existing commercial indebtedness of approximately U.S.\$2.7 billion of its existing commercial indebtedness were amended or exchanged for new notes on 14 April 2000, 15 March 2001 and 15 November 2002. On 27 November 2002 and 17 December 2002, Ukraine issued an aggregate principal amount of U.S.\$260 million and U.S.\$139 million, respectively, of bonds maturing in 2007, which were fungible with the U.S. dollar-denominated bonds issued pursuant to the three exchange offers in 2000, 2001 and 2002. All U.S. dollar-denominated and euro-denominated bonds issued in 2000-2002 offerings matured in March 2007. The purpose of these exchange offers was to improve Ukraine's debt servicing profile and balance of payments. Ukraine has also restructured certain aspects of its internal indebtedness; see “— *Internal Debt*”.

On 11 June 2003, Ukraine issued an aggregate amount of U.S.\$800 million bonds due 2013, which bear interest at the rate of 7.65 per cent. per annum; on 3 October 2003, Ukraine issued additional bonds of the same series in the aggregate principal amount of U.S.\$200 million. On 2 March 2004, Ukraine issued an aggregate principal amount of U.S.\$600 million 6.875 per cent. bonds due 2011. On 5 August 2004 Ukraine issued an aggregate principal amount of U.S.\$500 million floating rate notes that were redeemed in full in 2009. On 13 October 2005, Ukraine issued an aggregate principal amount of €600 million 4.95 per cent.

bonds due 2015. On 13 September 2006, Ukraine issued an aggregate principal amount of CHF 384 million 3.5 per cent. bonds due 2018; on 7 December 2006, Ukraine issued additional bonds of the same series in the aggregate principal amount of CHF 384 million. Following the exercise of the scheduled put option by holders of the CHF bonds, all CHF bonds were redeemed in September 2009. On 20 November 2006, Ukraine issued an aggregate principal amount of U.S.\$1,000 million 6.58 per cent. bonds due 2016 and on 19 December 2006 Ukraine issued an aggregate principal amount of JPY 35,100 million 3.2 per cent. notes due 2010. On 26 June 2007, Ukraine issued an aggregate principal amount of U.S.\$500 million 6.385 per cent. bonds due 2012 and on 14 November 2007, Ukraine issued an aggregate principal amount of U.S.\$700 million 6.75 per cent. bonds due 2017.

In addition, in June 2010, Ukraine entered into a credit facility with JSC VTB Bank, which assigned its rights under the facility to VTB Capital plc in August 2010. Under this facility, Ukraine has been extended a loan of U.S.\$2.0 billion at an annual interest rate of 6.7 per cent. The loan is for an initial term of six months, which may be extended up to three times for a maximum maturity of two years, subject to agreement between the parties on a new interest rate for each extension period.

International Organisations

Since Ukraine's independence, credits from international financial organisations have played a significant role in fostering economic and structural reforms. The resources of these organisations provide long-term support for economic growth in an environment of low domestic investment and more expensive (and sometimes unavailable) commercial borrowing options. From 1992 to 1 August 2010, Ukraine obtained loans totalling U.S.\$14.9 billion from the IMF and U.S.\$4.81 billion from the World Bank. As at 1 August 2010, Ukraine and Ukrainian companies raised €5.4 billion from the EBRD under 249 projects (this figure includes loans raised by Ukrainian companies with and without state guarantees). In the wake of the emerging market crisis in the autumn of 1998 and up until the second half of 2002, loans from international organisations such as the IMF, the EBRD and the World Bank and the EU comprised Ukraine's only significant source of external financing. See "*Risk Factors – Risk Factors Relating to the Guarantor – Inability to obtain financing from external sources to provide financing could affect Ukraine's ability to meet financing expectations in its budget.*"

As at 31 December 2007, 2008, 2009 and 31 July 2010, the total amount of debt owed to the IMF stood at U.S.\$0.4 billion, U.S.\$4.7 billion, U.S.\$12.9 billion and U.S.\$14.5 billion, respectively (including debt owed to the IMF by the Government amounting to approximately U.S.\$6.8 million and U.S.\$7.7 billion, as at 31 December 2009 and 31 July 2010, respectively), and the total amount of direct debt owed to other international organisations and the EU stood at U.S.\$2.5 billion, U.S.\$3.2 billion, U.S.\$10.4 billion and U.S.\$11.1 billion, respectively. Repayments of principal and interest in respect of IMF debt for the seven months ended 31 July 2010 were U.S.\$103.2 million. Repayments of principal and interest in respect of IMF debt for full-year 2010 are estimated at U.S.\$205.4 million (including payments by the Government amounting approximately to U.S.\$115.2 million) and for 2011 are estimated at U.S.\$0.3 billion. Repayments of principal and interest in respect of debt owed to the EU and international organisations other than the IMF for the seven months ended 31 July 2010 were U.S.\$193.3 million. Repayments of principal and interest in respect of debt owed to the EU and international organisations other than the IMF for full-year 2010 are estimated at U.S.\$309.6 million and for 2011 are estimated at U.S.\$419.4 million.

IMF

During the first stage of market reforms, the credit resources of the IMF made monetary reform possible, were used to support the exchange rate, and provided funds to increase currency reserves, service external debt and finance balance of payments deficits. During this period, the co-operation with the IMF took place under "stand-by" loan arrangements aimed at stabilising the economy. In the period after 2000, following the establishment of the relevant economic conditions, the co-operation has taken the form of "extended fund facilities", which support economic development.

In 2005-2007, Ukraine did not borrow any funds from the IMF and co-operation between Ukraine and the IMF was focused on technical assistance intended to reduce threats to stability and to address problems

associated with macro-economic, monetary, currency, tax and budgetary policy. Such co-operation also included technical assistance on issues related to debt, the shadow economy and forecasting. During 2005-2006, IMF technical missions made several visits to Ukraine aimed at assisting the Government in various areas, amongst others, related to public debt management, fiscal policy and customs administration. In 2006-2007, an IMF expert was permanently involved in the activities of the Ministry of Finance relating to fiscal analysis and forecasting, strategy of budget planning and control over fiscal stability.

In the fourth quarter of 2008, against the background of the global financial downturn, Ukraine approached the IMF for financing. On 5 November 2008, the IMF approved for Ukraine a two-year stand-by facility in an aggregate amount of U.S.\$16.4 billion. The financing extended under the stand-by arrangement was intended to support Ukraine's long-term economic policy in line with the Memoranda of Economic and Financial Policies issued by Ukraine in October 2008, April 2009 and July 2009.

In particular, the stand-by arrangement aimed to restore economic growth, reduce inflation and bring about financial stabilisation. A priority of the arrangement was to mitigate problems in the financial services sector and encourage lending through a complex restructuring of the banking system. Furthermore, the arrangement aimed to reduce inflationary pressure through changes in macro-economic policy, a flexible exchange rate policy and a tight fiscal policy.

To achieve these aims, the stand-by arrangement focused on three key areas: (i) fiscal policy; (ii) monetary and exchange rate policy, and (iii) financial sector policy. In particular, the fiscal policy as envisaged by the arrangement contemplated following of a prudent fiscal policy and undertaking additional savings measures to help ease the pressure on public finances while providing for the required recession-related social expenditures. The monetary and exchange rate policy contemplated under the arrangement provided for the implementation of a flexible exchange rate regime, a transparent strategy for the NBU interventions and strengthening of the NBU independence and governance structure. The third element of the arrangement, the financial sector policy, envisaged development and implementation of a comprehensive framework for the recapitalisation and restructuring of the banking system in order to restore the financial stability in Ukraine and confidence in the banking sector.

Furthermore, the stand-by arrangement provided for the quantitative and continuous performance criteria that should have been met by Ukraine as of each of 31 December 2008, 31 March 2009, 31 May 2009, 30 September 2009 and 31 December 2009. Such criteria included, among other things, a ceiling on the cash deficit of the general government, a floor on net international reserves of the NBU, and a ceiling on the monetary base, some of such criteria having been revised in 2009 as compared to the initial targets.

In 2008 and 2009, Ukraine received three tranches under the stand-by arrangement in the total amount of U.S.\$10.6 billion, U.S.\$4.8 billion of which were earmarked for the financing of the State Budget deficit, including repayments of external State debt. The first tranche in the amount of U.S.\$4.5 billion was approved by the IMF on 5 November 2008 and received by Ukraine on 7 November 2008. The second tranche in the amount of U.S.\$2.8 billion was approved by the IMF on 8 May 2009 and received by Ukraine on 12 May 2009. The third tranche in the amount of U.S.\$3.3 billion was approved by the IMF on 28 July 2009 and received by Ukraine on 31 July 2009.

The next tranche of IMF financing in the amount of approximately U.S.\$3.9 billion was expected to be disbursed after the third review of Ukraine's compliance with the terms of the stand-by arrangement. However, in November 2009, IMF financing under the stand-by arrangement was suspended due to a failure to reach an agreement with respect to results of the third review.

Starting March to July 2010, after the new President took office, IMF missions visited Ukraine with a view to review the macroeconomic situation and budget, fiscal and monetary policy of the Government and the NBU and to consider a possibility of resumption of IMF support. On 28 July 2010, the IMF Executive Board noted the cancellation of the SBA approved in November 2008. On the same date, the IMF Executive Board approved a new U.S.\$15.15 billion stand-by arrangement for Ukraine to be extended in ten tranches in 2010-2012, with two tranches expected to be extended in 2010, and four tranches expected to be extended in each of 2011 and 2012, subject, in each case, to Ukraine's compliance with the stand-by arrangement terms. On

2 August 2010, Ukraine received the first tranche in the amount of approximately U.S.\$1.89 billion, approximately U.S.\$1.0 billion of which were earmarked for the financing of the State Budget deficit.

The goal of the Ukrainian economic programme supported by the new IMF financing arrangement is to entrench fiscal and financial stability, advance structural reforms, and put Ukraine on a path of sustainable and balanced growth. To achieve these aims, the stand-by arrangement focuses on three key areas: (i) fiscal policy; (ii) monetary and exchange rate policy, and (iii) financial sector policy. In particular, fiscal policy as envisaged by the arrangement contemplates restoration of confidence and fiscal sustainability by reducing the general government deficit to 5.5 per cent. of GDP in 2010, 3.5 per cent of GDP in 2011, and 2.5 per cent. of GDP in 2012; reducing the deficit of Naftogas to 1.0 per cent. of GDP in 2010 and eliminating it thereafter; setting public and publicly guaranteed debt-to-GDP ratio firmly on a downward path with the objective of stabilising it below 35 per cent. by 2015; and relying proportionally more on expenditure-saving measures to gradually reduce the tax burden on the economy. The monetary and exchange rate policy contemplated under the arrangement provides for maintaining core CPI inflation in single digits in 2010 and bringing overall CPI to no more than 5 per cent. over the medium term; strengthening the independence and accountability of the NBU; and improving the functioning of the foreign exchange market. The third element of the arrangement, financial sector policy, centers on completing the resolution and recapitalisation of systemic banks, strengthening state-owned banks, and enacting key legislation and regulations, including, among other things, through creating a framework that properly recognises and facilitates the resolution of impaired loans and implementing consolidated supervision.

In addition, the stand-by arrangement provides for the quantitative and continuous performance criteria that should have been met by Ukraine as of each of 30 September and 31 December 2010. Such criteria include, among other things, a ceiling on the cash deficit of the general government, a floor on net international reserves of the NBU, a ceiling on the net domestic assets and a ceiling on the state-guaranteed debt. The first review of Ukraine's compliance with the stand-by arrangement terms is expected to take place in November 2010 and by the time of this compliance review, Ukraine is required to have met certain criteria as to net domestic assets, net international reserves and cash deficit of the general government sector. In particular, as at 30 September 2010, Ukraine is required to comply with a ceiling on the cash deficit of the general government excluding Naftogas in the amount of UAH 47.0 billion and a ceiling on the cash deficit of the general government including Naftogas in the amount of UAH 56.0 billion. In addition, as at 30 September 2010, Ukraine is required to have net international reserves in the amount of not less than U.S.\$18.3 billion, and to comply with a ceiling on the cumulative change in net domestic assets in the amount of UAH 9.9 billion. The second tranche is expected to be extended in December 2010 subject to the satisfactory results of the first review, while the second review is proposed for March 2011 based on year-end 2010 targets.

On 28 August 2009, the IMF announced that Ukraine would receive 1.017 billion in SDRs (equal to U.S.\$1.6 billion) as part of a distribution of approximately 161.2 billion in SDRs among 186 shareholder states of the IMF. In September 2009, the IMF made an additional allocation to Ukraine in the amount of 292 million in SDRs as part of a special one-time distribution of SDRs to IMF members. As at 1 August 2010, Ukraine utilised 1.2 billion in SDRs of the aggregate amount of such IMF allocations. The amount of SDR allocations received to the State Budget is accounted as state borrowings and, therefore, is included into State debt (direct debt).

World Bank

From 1992 to 1 August 2010, the World Bank approved a total of 39 loans and four Global Environment Facility grants to Ukraine totalling approximately U.S.\$6.59 billion (U.S.\$4.81 billion had been raised under such loans to that date). Loans from the World Bank are directed at supporting the State Budget and reforming the tax, banking, and financial systems, as well as the energy sector and state governance sector. World Bank loans also support social protection and road reconstruction.

The World Bank and Ukraine are parties to a two-part U.S.\$750 million Programmatic Adjustment Loan ("PAL") programme. Ukraine received a loan in the amount of U.S.\$250 million in the first stage of the PAL, in September 2001. The loans in the second stage of the PAL (PAL-II) were provided by the World Bank in

two tranches, the first tranche, in the amount of U.S.\$75 million, in December 2003 and the second tranche, in the amount of U.S.\$175 million, in June 2005. In 2005, Ukraine agreed with the World Bank on the completion of the transactions under the PAL programme and preparation of a new Development Policy Loan (“DPL”) project to replace the PAL.

On 19 July 2005, Ukraine received a DPL of U.S.\$251.26 million from the World Bank. The DPL provides for assistance in supporting priority initiatives in the economic and social spheres of the Government Action Programme. The DPL was intended to support broad improvements in governance, especially political and institutional reforms in the following sectors: investment climate improvement; improvement of public administration and state finance management; and enhancement of social integration.

In February 2008, Ukraine received a second stage DPL (DPL-II) of U.S.\$300 million from the World Bank. In December 2008, Ukraine received a third stage DPL (DPL-III) of U.S.\$500 million from the World Bank. DPL-II and DPL-III were intended to support improvement of investment climate needed for further economic development; creation of a fiscal foundation for economic growth by means of strengthening of the public finance sector; and a reform of the public sector and improvement of the quality of social services. Currently, Ukraine and the World Bank are preparing to launch the Fourth Development Policy Loan expected to amount to U.S.\$500 million.

In June 2006, the loan agreement under the Access to Financial Services Project was signed (ratified by Parliament on 13 December 2006, the World Bank loan amounts to U.S.\$150 million). On 22 October 2009, the Project was terminated and no further disbursements are expected to be made under the loan agreement. As at 1 August 2010, the outstanding amount under this loan was U.S.\$17.4 million. In July 2006, the Board of Directors of the World Bank approved the Second Export Development Project (U.S.\$154.5 million, the guarantee agreement under the Project between Ukraine and the World Bank and the loan agreement between Ukreximbank and the World Bank were ratified on 1 December 2006). As at 1 August 2010, U.S.\$117.0 million had been disbursed under the Second Export Development Project.

In August 2007, the Board of Executive Directors of the World Bank approved the Power Transmission Project, involving a U.S.\$200.0 million loan, and the Urban Infrastructure Development Project, involving a U.S.\$140.0 million loan. The loan agreements under these projects came into effect on 5 December 2008 and 10 November 2008, respectively. As at 1 August 2010, U.S.\$0.3 million and U.S.\$5.4 million has been disbursed under the Power Transmission Project and the Urban Infrastructure Development Project, respectively. The Power Transmission Project is intended to increase the reliability of power transmission. The project seeks to achieve this goal through transmission station rehabilitation and the renewal of Ukraine’s power transmission network. The Urban Infrastructure Development Project aims to support utility companies in providing reliable utility services to the Ukrainian population.

In January 2008, the Board of Executive Directors of the World Bank approved the Public Finance Modernisation Project, involving a U.S.\$50.0 million loan to Ukraine (the loan agreement was signed in March 2008). The loan agreement under this project came into effect on 23 October 2008. As at 1 August 2010, U.S.\$1.0 million has been disbursed under the Public Finance Modernisation Project. The project aims to strengthen the public finance management in Ukraine through improvement of functional efficiency and transparency in the sector, introduction of an integrated system of public finance management and support of major reform programmes of the Ministry of Finance of Ukraine.

In the first quarter of 2009, Ukraine and the World Bank initiated the Programmatic Financial Rehabilitation Loan Project, under which Ukraine expects to borrow U.S.\$750 million in two tranches. The first tranche under this project in the amount of U.S.\$400 million was received by Ukraine in September 2009, and Ukraine is currently preparing a drawdown of the second tranche. The project is intended to assist the Government and the NBU in implementation of the system of the recapitalisation by the State of large problem banks, consolidation of the banking system, strengthening of the system for guaranteeing individual deposits, and increasing the population’s confidence in the banking system.

On 21 April 2009, Ukraine and the World Bank signed the facility agreement under the Roads and Safety Improvement Project involving a loan of U.S.\$400 million. The project is intended to improve the condition of the Boryspil-Lubny section of the M-03 Kyiv-Kharkiv highway, and to repair dangerous sections of roads

of general use. The facility agreement came into effect on 3 September 2009 and, as at 1 August 2010, U.S.\$21.2 million had been disbursed under this project. In addition, Ukraine and the World Bank have launched preparations for the Railway Modernisation Project involving a loan of U.S.\$500 million. The project provides for the construction of a second track, electrification and modernisation of the railway in the Znamyanka-Dolynska Mykolaiv-Kherson-Dzhankoy direction.

In December 2007, the World Bank approved the Strategy for Partnership of the World Bank and the International Finance Corporation with Ukraine for 2008-2011. The Strategy provides for loans supporting the improvement of public finance management, the development of the private sector and social protection. The Strategy is based on principles of selectivity, flexibility and partnership based on which the World Bank intends to extend funding to a small number of key projects. In addition, since October 2007, rates under World Bank loans have been reduced and certain commitment fees have been eliminated.

The activities of other members of the World Bank Group, such as the International Finance Corporation (“IFC”), the Multilateral Investment Guarantee Agency (“MIGA”) and the International Development Association are directed at encouraging foreign private investment in various sectors of the economy. The aim is for this investment to modernise and restructure production, transfer technology and boost exports of goods and services. The improved investment climate from 2000 to 2008 led to growth in the number of IFC investments and loan projects for private sector companies. The Government also believes that MIGA may expand its activities in Ukraine by guaranteeing investments against non commercial risks and providing technical assistance in developing a national system of investment incentives.

European Investment Bank and Nordic Investment Bank

On 22 December 2004, a new mandate of the European Investment Bank, or EIB, was approved authorising lending operations in Russia, Ukraine, Moldova and Belarus up to a ceiling of €500 million. In July 2005, Ukraine signed a co-operation agreement with the EIB, which became effective in April 2006. Work on establishing a viable loan portfolio is ongoing and initial lending operations were started in 2006. The new mandate of the EIB for 2007-2013 for Russia, Ukraine, Moldova, Belarus, Armenia, Azerbaijan and Georgia authorised lending operations in such countries of up to €3.7 billion for projects in the transport, energy, telecommunications and environmental protection spheres. As at the date of this Prospectus, the EIB and Ukraine have initiated dialogue for implementation of joint projects in transport, energy and municipal services. The Government expects that EIB lending operations will focus on the transport sector (including construction, repair and modernisation of highways and railways), telecommunications, energy efficiency, energy infrastructure and environmental protection.

In June 2010, Ukraine and the EIB signed a Host Country Agreement for EIB representation for Ukraine. The parties expect that this agreement will strengthen cooperation between them and improve the EIB’s response to the financing needs of public and private clients in Ukraine. As at 30 August 2010, this agreement remains to be ratified by the parties to become effective.

On 30 July 2007, Ukraine and the EIB signed a Financing Agreement relating to the Kyiv-Chop Road Rehabilitation Project under which Ukraine expects to borrow from the EIB a loan in the amount of €200 million. The EBRD has agreed to provide an additional €200 million in financing; see “— EBRD”. On 28 April 2009, the Financing Agreement with the EIB relating to the Kyiv-Chop Road Rehabilitation Project came into effect. As at 1 August 2010, the EIB disbursed €68.0 million under the Kyiv-Chop Road Rehabilitation Project. Currently, Ukraine and the EIB are preparing a joint project “Improvement of Roads Around Kyiv”, under which Ukraine expects to borrow €450.0 million from the EIB. It is expected that this project will be financed jointly by the EIB and the EBRD, which is expected to provide an additional €450.0 million in financing.

In addition, a €150 million loan agreement was signed with the EIB in October 2008 and came into effect in September 2009 under a joint EBRD EIB-Ukraine project “Construction of the 750 kV Rivne NPP — Kyiv Overhead Transmission Line”. The Government expects that €150 million for this project will be funded by the EIB, with another €150 million to be funded by the EBRD. As at 1 August 2010, €1.52 million of EBRD funds had been disbursed under this project.

On 2 February 2010, Ukraine and the EIB signed a Financing Agreement relating to the Development of the Water Supply and Wastewater System in the City of Mykolayiv. Under this project, Ukraine expects to borrow €15.54 million from the EIB in the form of a loan.

Other projects that are being prepared with the EIB include projects for the construction of electrical transmission lines, under which Ukraine expects to borrow €225 million from the EIB, with an additional €225 million proposed to be funded by the EBRD; Ukrhydroenergo Rehabilitation Project, under which Ukraine expects to borrow €200 million from the EIB, with an additional €200 million proposed to be funded by the EBRD; and a project for financing of small and medium businesses in the telecommunications, transport, energy and environmental protection sectors, under which the EIB is expected to provide a loan in the amount of €775 million.

On 14 December 2006, a framework agreement between Ukraine and the Nordic Investment Bank became effective, providing for financing to Ukraine for the implementation of various infrastructural, energy, banking, telecommunications, environmental and other investment projects. In particular, the Board of Directors of Nordic Investment Bank has made a decision to extend €20 million for a project to reconstruct water supply and heating systems in the City of Odessa. In addition, the Nordic Investment Bank is considering a number of projects involving Ukrainian state-owned and privately-owned banks and metallurgical companies.

EBRD

As at 1 August 2010, the EBRD portfolio in Ukraine included 249 projects with a total financing volume of € 5.4 billion. From the beginning of Ukraine-EBRD relations, significant attention has been paid to funding nuclear safety measures. The EBRD oversees both the Nuclear Safety Account and the Chernobyl Fund “Shelter” established in December 1997 by the G-7 and other contributor countries in connection with the clean-up of the Chernobyl nuclear reactor disaster.

The EBRD has also supported projects in food processing, the oil and gas industries, transport, telecommunications, finance and agricultural services, as well as municipal infrastructure projects relating to water supply and heating. In addition, joint projects between Ukraine and the EBRD have commenced for the introduction of energy-saving technologies in the power consuming sectors of the economy. See “*Economy of Ukraine – Transport and Communication*” and “*Economy of Ukraine – Electricity Generation and Nuclear Power*”.

In August 2005, Ukraine and the EBRD signed a co-operation programme for 2005-2006 that was intended to provide €360 million for the implementation of various projects in Ukraine. The programme covered projects in the energy sphere, updating of rolling stock of Ukrainian railways, seaports modernisation and road construction. An amount of €346 million was extended under the Ukraine-EBRD co-operation programme for 2005-2006, including €300 million to road construction, €26 million to electricity grid construction and €20 million to energy efficiency projects.

In June 2007, Ukraine and the EBRD signed a co-operation programme for 2007-2009 that provided for a significant increase in EBRD investments in the public sector of Ukraine. The total volume of funding of joint Ukraine-EBRD investment projects in the public sector of Ukraine’s economy for the period covered by the Programme was approximately €1 billion. The programme covered projects in such sectors as energy, transport, communications, municipal infrastructure, natural resources and energy efficiency. In addition, one of the key objectives of this programme was the mobilisation of co-financing for Ukrainian projects from other leading international financial institutions, in particular the EIB.

Furthermore, on 18 September 2007, the EBRD’s board of directors approved the 2007-2009 strategy for Ukraine. According to this strategy, priority areas for EBRD activities in Ukraine included domestic capital markets development; increasing the economy’s competitiveness, including through transport and communications infrastructure development; energy sector reform, including use of alternative fuels; and corporate governance and transparency improvement.

In June 2010, representatives of Ukraine and the EBRD met to review the portfolio of EBRD loans to Ukraine. The new EBRD strategy for Ukraine is expected to be approved in the fourth quarter of 2010, following which a new Ukraine-EBRD cooperation programme is expected to be developed.

Within the framework of co-operation with the EBRD in the public sector, on 15 January 2007, the Loan Agreement between the State Railways Administration of Ukraine (“Ukrzaliznytsya”) and the EBRD and the Guarantee Agreement between Ukraine and the EBRD under the joint Ukraine-EBRD Fast Passenger Trains Project became effective. The amount of the loan from the EBRD is U.S.\$120 million, of which U.S.\$80.5 million had been disbursed as at 1 August 2010.

In addition, on 16 August 2007, the Loan Agreement and the Project Agreement under the Third Kyiv – Chop Road Rehabilitation Project came into effect. The agreements relating to this project provide for financing by the EBRD in the amount of €200 million, of which € 124.36 million had been disbursed as at 1 August 2010. This project is financed by the EBRD jointly with the EIB, which has agreed to provide an additional €200 million; see “– *European Investment Bank and Nordic Investment Bank*”.

In November 2007 Ukraine and the EBRD signed an agreement for a €26 million loan for the development of Illichivsk sea trade port, which came into effect on 22 May 2009. As at 1 August 2010, €0.5 million had been received by Ukraine under this agreement. The EBRD has also undertaken to support a “pilot” project offered by Ukravtodor for the development of public-private partnerships and to consider financing a concessionaire to be selected in an open tender.

The EBRD and Ukraine are considering the implementation of a U.S.\$90 million project for energy savings in the railway transport sector. Ukraine and the EBRD are also discussing potential financing for subway construction in Dnipropetrovsk and Donetsk, under which the EBRD may lend to Ukraine €740 million in total. In addition, Ukraine is considering issuance of guarantees under €1,014.2 million financing to be extended by the EBRD and Euroatom to finance the project on implementation of the consolidated programme on enhancement of safety at the Ukrainian NPSs.

See “– *European Investment Bank and Nordic Investment Bank*” for a description of certain projects financed jointly by the EBRD and the EIB”.

BSTDB

Ukraine has also undertaken a number of projects with the Black Sea Trade and Development Bank (“BSTDB”), which provides support to projects in the transport, communications and energy sectors and for environmental protection in the Black Sea area. The aggregate value of loans under BSTDB projects implemented in Ukraine was approximately U.S.\$243.8 million as of 1 August 2010. The BSTDB also promotes business co-operation among the member states of the Organisation of the Black Sea Economic Co-operation. Among the investment projects undertaken by the BSTDB is the reconstruction of a gas pipeline supplying Russian gas through Ukraine to the Balkans and Turkey. It has become common practice for the BSTDB to finance projects jointly with the EBRD and cooperate with commercial banks by providing loan facilities to support trade and small businesses.

Official Creditors

On 13 July 2001, Ukraine reached agreement with Paris Club creditors to reschedule U.S.\$581.7 million of debt arising under agreements concluded or pursuant to guarantees issued before 31 December 1998 and in respect of principal balances falling due prior to 3 September 2002. Pursuant to bilateral agreements with each of Ukraine’s principal official creditors to implement the Paris Club agreement, Ukraine agreed to repay the rescheduled principal balances in 18 equal semi-annual instalments commencing 30 April 2005 and ending 31 October 2013. Ukraine paid Paris Club creditors (other than Russia and Turkmenistan) U.S.\$148.3 million in 2007, U.S.\$145.2 million in 2008, U.S.\$136.4 million in 2009 and U.S.\$59.9 million in the seven months ended 31 July 2010. Outstanding debt to Paris Club creditors as at 31 July 2010 was approximately U.S.\$431.0 million (excluding debt to Russia, which amounted to U.S.\$996.9 million).

Ukraine's largest bilateral creditor is Russia. A framework agreement was entered into in May 1997 with the Russian government pursuant to which, with effect from 1 January 1998, a portion of debt then outstanding was deemed to have been repaid in exchange for a 20-year lease to the Russian Navy of port facilities in Sevastopol in the Crimea. Debt service payments to Russia are netted off against lease payments for the port facilities and both figures appear in future budgets. Under this agreement, Ukraine's state debt to Russia was reduced by approximately U.S.\$97.8 million in each of 2001 through 2009 and the seven months ended 31 July 2010. Approximately U.S.\$1.29 billion, U.S.\$1.19 billion, U.S.\$1.09 billion and U.S.\$1.0 billion was owed to Russia as at 31 December 2007, 2008, 2009 and 31 July 2010, respectively.

Further to a €110 million macro-financial support loan to Ukraine approved by the EU in 2002, the European Parliament approved in May 2010 a 15 year macro-financial support loan for Ukraine in the amount of up to €500 million to finance the deficit of its balance of payments and to meet its budgetary needs. As at 30 August 2010, Ukraine and the EU are negotiating a Memorandum on Understanding and a Loan Agreement for a €610.0 million loan. Extension of such macro-financial support loan is conditioned on, among other things, compliance by Ukraine with its commitments under the new stand-by arrangement with the IMF.

Contingent Liabilities

Historically, Ukraine has issued guarantees in favour of state-owned and other enterprises, including liabilities arising under export credit lines. All payments on guarantees and to Paris Club creditors were suspended after 21 January 2000. After reaching agreement with its Paris Club creditors in July 2001, Ukraine also resumed payments on outstanding guarantees. Ukraine paid U.S.\$4.3 million in 2007, U.S.\$4.6 million in 2008, U.S.\$109.7 million in 2009 and U.S.\$13.8 million in the seven months ended 31 July 2010.

The ceiling recommended by the IMF for the amount of guarantees issued in 2000 was UAH 1.5 billion and the ceiling for 2001, 2002 and 2003 was UAH 2.5 billion. The IMF issued no recommendation regarding a ceiling for the amount of guarantees issued from 2004 through to 2009. The ceiling recommended by the IMF for the amount of guarantees issued in 2010 is UAH 15.0 billion.

The total amount of guarantees issued by the Cabinet of Ministers from 1 January 2004 through 31 August 2010 in respect of various loans was approximately U.S.\$7.9 billion. On 2 July 2004, the Cabinet of Ministers issued a guarantee to Deutsche Bank AG as lender under a seven year, U.S.\$480 million credit facility, dated 29 June 2004, granted to Ukravtodor as borrower, for the purpose of financing the reconstruction of a segment of the Kyiv-Odessa highway. On 18 October 2004, the Cabinet of Ministers issued a guarantee to Deutsche Bank AG as lender under a seven-year U.S.\$700 million credit facility granted to the State Railway Transport Administration of Ukraine (Ukrzaliznytsnya) to finance the planning and construction of a railway and automobile bridge across the Dnipro river in Kyiv. On 18 November 2004, the Cabinet of Ministers of Ukraine issued a guarantee to Credit Suisse First Boston, London branch, as lender under a U.S.\$150 million loan granted to Yangel Yuzhnoye State Design Office for financing of a joint Ukraine-Brazil project for engineering of a missile complex "Cyclone-4". In August 2005, the Cabinet of Ministers issued a guarantee to Deutsche Bank as lender under a 10-year U.S.\$100 million credit facility granted to the State Road Service of Ukraine (Ukravtodor) to finance the completion of reconstruction of the Kyiv-Odessa highway. In July 2006, the Cabinet of Ministers issued a guarantee to Citibank N.A. London as lender under a 10-year €279,886,635 credit facility extended to Ukravtodor to finance the construction, reconstruction and capital repair of roads in general use.

In December 2006, November 2007 and December 2008, the Cabinet of Ministers guaranteed obligations of the State Mortgage Institution under domestic bonds issued in the aggregate amount of UAH 3 billion.

The aggregate amount of sovereign guarantees issued by the Cabinet of Ministers in 2009, including guarantees in respect of obligations of Ukravtodor and Naftogas, was U.S.\$4.1 billion. On 28 January 2009, the Cabinet of Ministers issued a guarantee to Credit Suisse International as lender under a credit facility in the aggregate amount of U.S.\$465 million extended to Ukravtodor. On 5 November 2009, sovereign guarantees were issued in respect of the restructured external debt obligations of Naftogas. The guarantees extend to payment obligations of Naftogas under the new U.S.\$1,595,017,000 9.5 per cent. notes issued by Naftogas on 5 November 2009 as well as one of Naftogas loans from a foreign lender, which has partially

survived the restructuring. In June 2009, the Cabinet of Ministers issued sovereign guarantees under domestic corporate bonds issued by Kharkiv State Aviation Enterprise and Kyiv Aviation Plant “Aviant” in the aggregate amount of UAH 2,478 million. Further, in October 2009, the Cabinet of Ministers issued a sovereign guarantee under a EUR 50 million loan from Aquasafety Invest for implementation of an anti-flood defence project and a sovereign guarantee under a EUR 85 million loan granted by UniCreditBank Austria to State Enterprise “Ukrmedpostach”. In December 2009, the Cabinet of Ministers issued a sovereign guarantee under USD 292.4 million loan granted by Export Development Canada to State Enterprise “Ukrkosmos” for the creation of the National Satellite Communication System.

In addition, in November and December 2009, the Cabinet of Ministers avalised (guaranteed) certain bills of exchange due 2012 in an aggregate amount of approximately UAH 1.6 billion issued by regional state road services as a payment for supplied goods, works or services in connection with modernisation of roads in view of holding the Euro-2012 Championship in Ukraine, liquidation of the consequences of certain natural disasters and other road construction, reconstruction and capital repair projects. See also “*Economy of Ukraine – Industry – Transport and Communications*”.

The 2010 State Budget Law authorises the Cabinet of Ministers to issue a number of state guarantees in 2010 in an amount not exceeding UAH 45.0 billion, including guarantees under obligations of Ukravtodor, State Mortgage Institution, the Agency to implement activities connected with the preparation and holding of the championship, as well as enterprises of the state sector economy to finance investment, innovation, infrastructure and other development projects that have strategic importance and which contribute to the economic development of Ukraine. As at 30 September 2010, no sovereign guarantees have been issued by the Cabinet of Ministers of Ukraine in 2010.

Special Fund Borrowings

In addition to borrowings accounted for in the general fund of the State Budget, which, excluding contingent liabilities and debt owed to the IMF accounted for as a liability of the NBU, amounted to U.S.\$1,907 million, U.S.\$3,728 million, U.S.\$14,625.4 million and U.S.\$4,591.4 million in each of 2007, 2008, 2009 and the seven months ended 31 July 2010, respectively, the Government has made certain borrowings that have been accounted for in the special fund of the State Budget. Such borrowings include, for instance, certain loans from international financial organisations and special issuances of T-bills for replenishment of Stabilisation Fund, including for the purposes of financing the measures connected with holding of the Euro-2012 Championship in Ukraine, although the majority of loans from international financial organisations and T-bill issuances are accounted for in the general fund of the State Budget. An aggregate UAH 22,005.1 million in borrowings to the special fund of the State Budget were initially planned for 2010. On 8 July 2010, Parliament approved the State Budget Amendment providing for a decrease in this amount of approximately UAH 5,100.0 million, to UAH 16,905.1 million.

The following table sets forth the borrowings made to the special fund of the State Budget and repayments of principal from the special fund of the State Budget in the periods indicated (no interest payments from the special fund of the State Budget were made in these periods):

	Year ended 31 December			Seven months ended 31 July
	2007	2008	2009	2010
	<i>(in U.S\$ millions)</i>			
Borrowings accounted for in the special fund	171.9	1,169.5	905.0	993.4
Internal borrowings	–	1,017.4	590.9	903.9
External borrowings	171.9	152.1	314.1	89.5
Repayments from the special fund	97.8	97.8	97.8	97.8
Internal borrowings	–	–	–	–
External borrowings	97.8	97.8	97.8	97.8

Debt Ratings

The outstanding foreign currency long-term debt of Ukraine is rated “B+” (stable) by Standard & Poor’s (“S&P”), “B2” (stable) by Moody’s Investors Service (“Moody’s”), “B” (stable) by Fitch Ratings Ltd. (“Fitch”) and “B+” (stable) by Rating and Investment Information, Inc. The outstanding national currency long-term debt of Ukraine is rated “BB- ” by S&P, “B2” by Moody’s and “B” ” by Fitch. A security rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal by the assigning rating agency.

THE MONETARY SYSTEM

National Bank of Ukraine

The NBU is the central bank of Ukraine. Established in 1991 pursuant to the Law of Ukraine “On Banks and Banking” and governed in accordance with the Law of Ukraine “On the National Bank of Ukraine”, dated 20 May 1999, the NBU is a special state authority with the principal objective of ensuring the external and internal stability of the national currency. To implement such main function, the NBU aims to promote the banking system stability as well as price stability. The principal governing bodies of the NBU are the Council and the Board. The Council, the highest governing body of the NBU, consists of 15 members, seven of whom are appointed by Parliament and seven of whom are appointed by the President and is responsible for the annual approval of the main principles of monetary-lending policy as well as supervision of their performance. The NBU Governor acts ex officio as the fifteenth member of the Council. The NBU Governor is nominated by the President and appointed by Parliament for a five-year term.

The NBU is empowered to develop and conduct monetary policy, organise banking settlements and the foreign exchange system with a view to integrating Ukraine into the international economy, ensure stability of the monetary, financial and banking systems and protect the interests of commercial bank depositors. On 8 July 2010, Parliament approved a law, which entered into force in October 2010, subject to certain provisions coming into effect from 1 January 2012, and has significantly amended the legislative framework that governs the activities of the NBU in order to comply with the arrangements reached by Ukraine with the IMF and the World Bank. The primary purpose of this law is to strengthen the independence of the NBU. For instance, the law provides that, in carrying out its primary function of ensuring the stability of the national currency, the NBU shall aim to:

- promote and maintain price stability as a priority,
- facilitate stability of the banking system to the extent this does not prevent ensuring price stability, and
- facilitate stable economic growth and support the economic policy of the Government, to the extent this does not prevent ensuring price stability and the stability of the banking system.

Among other things, the law provides for changes in the procedures for distribution of profits of the NBU, including with respect to their transfer to the State Budget; tightens qualification requirements for the members of the NBU Council and the Board; and increases the term of office of the NBU Governor from five years to seven years.

Under the principles for monetary lending policy for 2010, the NBU expects that the principal objective of its monetary-lending policy will be ensuring the stability of the hryvnia. To reach this goal, the main priorities of the monetary-lending policy for 2010 include ensuring stability of financial system, pursuing flexible exchange rate policy and increase in the role of monetary base targets as intermediary indicators for the monetary-lending policy.

Monetary Policy

The NBU is charged with implementing monetary policy. In making monetary decisions, the NBU primarily relies on the forecast of the development of the real sector of the economy, balance of payments and financial markets that is based on the analysis of a large spectrum of macro-economic, budgetary and monetary indicators, their interrelation and impact on hryvnia stability. Based on the review of such forecast development estimates, the NBU determines which regulatory measures shall be taken.

In 2009 and the seven months ended 31 July 2010, monetary-lending policy was carried out under challenging macro-economic conditions. As a result of changes in the macroeconomic environment, the development of the monetary and lending market in this period was substantially different from that in previous years. In particular, an economic downturn in the first quarter of 2009 put significant pressure on the monetary and lending market during that period. However, an improvement of macroeconomic indices in subsequent periods contributed to a gradual improvement of the situation in the monetary sphere reflected

in the stabilisation of the foreign exchange market, an increase in the foreign currency supply at the interbank market, the gradual return of retail deposits to the banking system and a decline in interest rates on loans.

In addition, in 2009 and the seven months ended 31 July 2010, the monetary and lending market was materially affected by fiscal factors such as spending of the Government's funds, loan funds provided by the IMF and mandatory repurchases of T-bills by the NBU. Under such circumstances, the NBU conducted its monetary and lending policy with a view to ensuring a prompt adjustment to changes in the economic environment using various monetary instruments and mechanisms. Measures taken by the NBU to stabilise the monetary and lending market were mainly focused on preventing hryvnia devaluation and counteracting inflationary pressures and ensuring that the credit support extended by banks to the economy was not unduly restricted by monetary measures. Furthermore, against the background of instability in the financial markets, the NBU applied flexible approaches to the regulation of banks' liquidity. In particular, in the first quarter of 2009, in order to address the outflow of funds from the banking system, the NBU focused its transactions on supporting the banks' liquidity. Since the second quarter 2009, when banks started to form a liquidity surplus, the NBU shifted its focus from refinancing transactions to mobilisation transactions, including through the placement of NBU deposit certificates in the amount of UAH 155.9 billion during the seven months ended 31 July 2010. Subsequently, starting from May 2010, the NBU has shifted to gradual relaxation of the monetary-lending policy, which has reflected in a decrease in the discount rate and other NBU interest rates and a reduction in the volumes of the mobilisation transactions, including through the narrowing of the maturity range of the NBU deposit certificates.

To prevent excessive liquidity in the banking system caused by, among other things, conversion into hryvnia of proceeds from the external borrowings raised by the Government, in the second half of 2009 and during the seven months ended 31 July 2010, the NBU several times strengthened mandatory reserve requirements and intensified transactions with T-bills on the two-way quotation basis. In particular, in the five months ended 31 May 2010, during such transactions the NBU sold T-bills in the nominal amount of UAH 7.5 billion, and purchased T-Bills in the nominal amount of UAH 2.7 billion; however, in May 2010, the NBU stopped mobilisation transactions by way of T-bills sale/purchase on the two-way quotation basis.

In addition, to ensure stability of hryvnia and a renewal of banks' lending to the economy, the NBU took a number of measures aimed at returning to the banking system funds withdrawn during the second half of 2008 and the first quarter of 2009. Such measures included improvement of the system for guaranteeing retail deposits, facilitation of banks' recapitalisation and support of banks' liquidity, including through prolongation of previously extended refinancing loans, although in the seven months ended 31 July 2010 the NBU sought to minimise the volume of the banks' liquidity support through refinancing mechanisms. As a result of such measures, the trend of outflow of funds from the banking system reversed and, since the second quarter of 2009, an increase in retail deposits has been recorded (with the exception of a minor decline in September 2009). In particular, during the seven months ended 31 July 2010, retail deposits increased by 17.7 per cent. In addition, starting from March 2010, growth has also been recorded in the corporate deposits, which increased by 8.5 per cent. during the seven months ended 31 July 2010. At the same time, recent positive trends in the monetary and lending market, while being reflected in an increase in interbank short-term lending, have not yet resulted an increase in lending to the real sector of the economy. In the absence of sufficient solvent borrowers, Ukrainian banks invest most of their available resources into financial instruments, in particular, T-bills and deposit certificates issued by the NBU.

The main risks for the monetary system and hryvnia stability in 2010 include (i) significant dependence of Ukrainian economy on external market conditions, which keeps Ukraine exposed to possible "second wave" of global financial and economic downturn, (ii) deferred inflation, particularly in the sphere of services, prices for which are subject to the administrative regulation, and (iii) imbalances in public finance sector, including the risk of failure to meet revenue targets set forth by 2010 State Budget Law and the need to improve the financial standing of Naftogas and to balance the budget of the Pension Fund. The NBU expects that in 2010, the main priorities of its monetary and lending policy will continue to include restraining inflation and ensuring stability of the financial system. In line with this, the NBU is committed to taking further measures aimed at overcoming the effect of the global downturn on the Ukrainian economy and renewing economic growth, including measures required to increase the funding potential of the banking system and increase banking lending and investment activities. Pursuant to the principles for monetary-

lending policy for 2010, the NBU expects that in 2010 monetary base indices will remain an important factor for its monetary-lending policy. In particular, regulation of monetary base volumes should allow the NBU to promptly react to inflation and devaluation risks, and, at the same time, to maintain required level of liquidity in the market. Such approaches largely correspond to the policies contemplated by the Memorandum on Economic and Financial Policy entered into within the framework of the 2010 IMF stand-by arrangement. In particular, the 2010 IMF stand-by arrangement envisages that core CPI inflation should be maintained in single digits in 2010, overall CPI should be no more than 5 per cent. over the medium term, and the monetary base should increase by 15.4 per cent. in 2010. In addition, the IMF stand-by arrangement contemplates that the NBU should use its interest rates as the main instrument of the monetary policy and should ensure foreign exchange rate flexibility.

Methods and instruments currently used by the NBU for the implementation of its monetary-lending policy include interest rate policy, mandatory reserve requirements, liquidity requirements and operations for the purpose of regulation of banks' liquidity, and transactions on sale or purchase of T-bills at the open market.

In particular, as part of its interest rate policy, the NBU gradually increased the discount rate from 7.0 per cent. in December 2002 to 9.5 per cent. (effective from 10 August 2005), which was followed by a decrease to 8.5 per cent. effective from 10 June 2006 and to 8 per cent. effective from 1 June 2007. On 1 January 2008, the NBU reversed course with an increase back to 10 per cent., followed by a further increase to 12 per cent. effective from 30 April 2008. With effect from 15 June 2009, the NBU decreased the discount rate to 11 per cent., followed by a further decrease to 10.25 per cent. effective from 12 August 2009, to 9.5 per cent. effective from 8 June 2010, to 8.5 per cent. effective from 8 July 2010 and 7.75 per cent. effective from 10 August 2010.

The NBU performs daily deposit operations with banks through issuances of its deposit certificates (overnight, up to 14 days, and up to 90 days). In addition, the NBU performs operations with banks including repo and refinancing transactions (overnight loans, up to 14 day and up to 90 day refinancing loans) and transactions with notes of internal state borrowings. The NBU also provides stabilising loans to solvent banks for support of their liquidity. Stabilising loans are provided for a term of up to 90 days and could be further extended up to the maximum term of 360 days or 450 days in case of a real threat to stability of a bank's operations. Since 1 March 2004, the NBU has separately determined interest rates on overnight unsecured loans (10.75 per cent. as at 30 August 2010) and overnight loans secured by state securities (8.75 per cent. as at 30 August 2010). Starting from 17 November 2006, the NBU has been setting separate interest rates on a weekly basis for deposit certificates issued by the NBU on various terms.

In 2001, the NBU adopted new regulations permitting it to sanction commercial banks for failure to keep prescribed amounts of mandatory reserves. These sanctions are payable from the banks' profits. Currently, commercial banks must transfer to their reserve fund no less than 5 per cent. of their profits annually until and unless the reserve fund is equal to 25 per cent. of their regulatory capital. The NBU can require additional allocations to be made to the reserve fund.

The NBU has established a mandatory reserve requirement to maintain the liquidity of the banking system and the stability of the Ukrainian hryvnia. Banks are required to maintain certain reserves in current accounts with the NBU; such reserve requirements are computed as a percentage of certain of the bank's liabilities. In particular, since 1 February 2009, reserves are required to be not less than the sum of 4 per cent. of the amount of term deposits of customers in foreign currency, 7 per cent. of demand deposits and current accounts of customers in foreign currency and 2 per cent. of funds borrowed from non-resident banks and financial organisations. Currently, term deposits, demand deposits and current accounts of customers in hryvnia are not subject to such mandatory reserve requirements. Further, with effect from 1 August 2008, Ukrainian banks are generally required to form reserves for funds (e.g., loans and deposits) attracted from non-residents for the term of up to six months in the amount of 20 per cent. of the aggregate amount of such funds. Overnight loans and deposits, as well as loans and deposits guaranteed by the Government or received from international financial organisations, to which Ukraine is a member, are exempt from the above reserve requirements. However, from 13 October 2008 to 1 October 2010, the NBU temporarily suspended the requirement to form such reserves. In addition, with effect from 1 May 2010, a bank is required to maintain

100 per cent. of the amount of the mandatory reserves formed during the previous reporting period at the separate correspondent account with the NBU.

The NBU has also established three separate liquidity requirements for commercial banks. A bank must have an instant liquidity ratio (the ratio of highly liquid assets to current liabilities) of at least 20 per cent., a current liquidity ratio (the ratio of assets with maturities under 31 days to liabilities with maturities under 31 days) of 40 per cent. and a short-term liquidity ratio (the ratio of liquid assets with maturities under one year to liabilities with maturities under one year) of at least 60 per cent. The NBU has determined that, for the purpose of calculating assets and liabilities with maturities under one year, liquid assets include cash funds, bank metals, funds in correspondent accounts opened with the NBU, loans granted to commercial entities, state authorities and individuals, debt securities in the bank's trade portfolio, available-for-sale portfolio and held-to-maturity portfolio, term deposits at the NBU and certain portion of funds in correspondent accounts opened with other banks, deposits placed with other banks and loans granted to other banks. Liabilities with maturities under one year are defined to include budget funds, term loans from the NBU, term deposits of the NBU, funds in the correspondent account opened by the NBU with the relevant bank, loans from international and other financial organisations, debt securities issued by the bank, overdue indebtedness under term deposits of other banks and loans raised from other banks, bank's subordinated debt, liabilities under all types of guarantees, suretyships and avals, customers' funds, accounts payable in respect of purchase of assets, committed credit lines to banks and customers and certain portion of funds in correspondent accounts of other banks, deposits of other banks and loans raised from other banks.

In 2009, in order to mitigate the effects of the financial downturn and ensure stabilisation of the banking system, the NBU refinanced commercial banks through overnight loans, repo and swap transactions, up to 14, up to 90 and up to 365 day refinancing loans, stabilisation loans, as well as loans secured by the pledge of property rights to deposits placed with the NBU. The aggregate volume of refinancing transactions in 2009 was UAH 64,410.0 million, 19.8 per cent. of it as overnight loans, 75.4 per cent. as stabilisation and other loans, 1.9 per cent. as up to 14 day and up to 365 day refinancing loans, 0.7 per cent. as repo transactions, and 2.2 per cent. as swap transactions. The weighted average interest rate under all refinancing instruments in 2009 was 16.7 per cent. per annum. In the seven months ended 31 July 2010, the NBU refinances commercial banks through overnight loans, repo transactions, up to 14 and up to 90 day refinancing loans, and stabilisation loans. In the seven months ended 31 July 2010, the aggregate volume of refinancing transactions was only UAH 3.9 billion (more than UAH 58.0 billion in the corresponding period of 2009). 0.1 per cent. of this volume consisted of overnight loans, 1.3 per cent. of up to 14 day and up to 90 day refinancing loans and the remaining 98.6 per cent. of stabilisation and other loans. The weighted average interest rate under all refinancing instruments in the seven months ended 31 July 2010 was 12.3 per cent. per annum as compared to 17.0 per cent. per annum in the same period of 2009.

Money Supply

The ratio of broad money supply (M3) to GDP was 55.0 per cent. in 2007, 54.3 per cent. in 2008, 53.3 in 2009 and 50.9 per cent. in the seven months ended 31 July 2010. In the period between 2000 and the seven months ended 31 July 2010, the broad money supply (M3) increased by approximately 25 times (including a 13.1 per cent. increase in the seven months ended 31 July 2010, as compared to an 8.5 per cent. decrease in the corresponding period of 2009). As at 1 August 2010, the broad money supply (M3) amounted to UAH 550.9 billion. The 13.1 per cent. increase in the broad money supply (M3) in the seven months ended 31 July 2010 was largely attributable to an increase in hryvnia deposits, including an increase of transferable deposits by 22.8 per cent and other deposits by 21.7 per cent.

The financial and economic downturn materially affected Ukrainian monetary-lending system in 2009. Significant debt pressure in the private sector, along with the limited access to external borrowings, put additional devaluation pressure on hryvnia, even against the background of gradual improvement of conditions in external commodity markets. At the same time, deterioration of borrowers' financial standing affected the financial stability of the banking system. These factors, also strengthened by the low pace of economic reforms and misbalances in the public finance sector, created significant risks for monetary-lending market in 2009. However, due to measures taken by the NBU, the inflation growth rate decreased significantly by the end of 2009, largely due to stabilisation of the hryvnia exchange rate and use of other monetary instruments. Such stabilisation in the foreign exchange market was coupled with a gradual renewal

of confidence in the banking system among the general public. In January-July 2010, a monetary-lending policy was implemented by the NBU against the background of certain improvements in macroeconomic conditions and was aimed at facilitating the renewal of the economy's high growth rates and ensuring the stability of financial system. Measures taken by the NBU during this period further stabilised the foreign exchange market and strengthened the trend toward the return of funds to the banking system which, in turn, contributed to a decrease of interest rates under bank loans and gradual resumption of lending to economy, although banking credit to the economy has not yet increased in cumulative terms.

In 2007, 2008 and 2009, the monetary base increased by 46.0 per cent., 31.6 per cent. and 4.4 per cent., respectively, and, in the seven months ended 31 July 2010, the monetary base increased by 14.8 per cent. (as compared to a 1.4 per cent. increase in the corresponding period of 2009). In the period between 2000 and the seven months ended 31 July 2010, the monetary base increased by 19.1 times and, as at 1 August 2010, amounted to UAH 223.8 billion.

The NBU contributed to economic growth in 2008 and 2009 in part through the satisfaction of a continuous increase in money demand as a result of, amongst other things, active re-monetisation of the Ukrainian economy at a rate of 54.8 per cent. as at 1 January 2010, as compared to 48.1 per cent. as at 1 January 2009 and 45.6 per cent. as at 1 January 2008. The rate of re-monetisation as at 1 August 2010 was 47.9 per cent. The monetisation process was supported by a deceleration of the money turnover rate: the rate of money turnover decreased from 2.19 to 2.08 in 2008 and further decreased to 1.82 in 2009. In the seven months ended 31 July 2010, the money turnover rate increased to 2.09.

According to NBU data, the average weighted interest rate on hryvnia deposits was approximately 8.2 per cent. in 2007, 9.9 per cent. in 2008, 14.0 per cent. in 2009 and 9.8 per cent. in July 2010. The average weighted interest rate on foreign currency deposits decreased from 5.8 per cent. in 2007 to 5.4 per cent. in 2008, but increased to 9.2 per cent. in 2009, and further decreased to 7.6 per cent. in July 2010. The average weighted interest rate on credits in the national currency fluctuated between 13.9 per cent. in 2007, 17.6 per cent. in 2008, 20.5 per cent. in 2009 and 13.5 per cent. in July 2010. The average weighted interest rate on credits in foreign currency increased from 11.3 per cent. in 2007 to 11.6 per cent. in 2008, decreased to 9.9 per cent. in 2009 and increased to 10.5 per cent. in July 2010.

The following table sets forth information concerning Ukraine's money supply as at the end of the periods indicated:

Available Money Supply in Circulation in Ukraine⁽¹⁾

	Year ended 31 December			Seven months ended 31 July 2010
	2007	2008	2009	
	<i>(in UAH millions except as noted)</i>			
Money outside banks (M0)	111,119	154,759	157,029	175,080
Money supply (M1)	181,665	225,127	233,748	269,281
Money supply (M2).....	391,273	512,527	484,772	550,096
Money supply (M3).....	396,156	515,727	487,298	550,941
as % of the previous year	151.7	130.2	94.5	113.1
as % of GDP	55.0	54.3	53.3	50.9(2)
Monetary base	141,901	186,671	194,965	223,819
as % of the previous year	146.0	131.6	104.4	114.8
Deposits in local currency	192,297	201,835	173,091	212,496
Deposits in foreign currency	91,577	157,905	161,862	166,417
Credit extended	426,867	734,022	723,295	711,964

Notes:

- (1) The data include accrued interest
- (2) Based on 2010 GDP forecast in the amount of UAH 1,083.1 billion.

Banking Credit

According to NBU statistics, overall banking credit to the economy increased in real terms by 74.1 per cent. in 2007 and 72.0 per cent. in 2008, but decreased by 1.5 per cent. in 2009 and further decreased by 1.6 per cent. in the seven months ended 31 July 2010 (as compared to a decrease of 2.2 per cent. in the corresponding period of 2009). Long-term (over one year) lending as a percentage of total lending decreased in 2009, reaching 68.1 per cent. of total lending, as compared to 69.8 per cent. in 2008, and further increased in the seven months ended 31 July 2010, reaching 68.6 per cent. of total lending. Foreign currency lending accounted for 59.1 per cent. in 2008, 50.8 per cent. in 2009 and 48.3 per cent. in the seven months ended 31 July 2010.

Treasury Bills

Placements of T-bills sold in the market are conducted through an auction process carried out by the NBU as agent for the Ministry of Finance. Auctions are currently conducted through the NBU's electronic communication network, pursuant to a schedule approved and published in advance. Since 19 February 2010, T-bills in the primary market are only sold to primary dealers selected by the Ministry of Finance. In addition, T-bills in the primary market may be sold to the NBU acting on the instruction and at the expense of its clients. See "*Public Debt – General*". According to the data of the Ministry of Finance, the Government placed in 2009 T-bills with maturities ranging from three months to twelve years in the aggregate amount of approximately UAH 62.8 billion. This amount includes T-bills of approximately UAH 2.7 billion for the increase of the statutory capital of the state-owned banks, T-bills of approximately UAH 17.0 billion for the recapitalisation of the three banks in which the State became a shareholder in July 2009, T-bills of approximately UAH 24.4 billion for the increase of the statutory capital of Naftogas, and T-bills sold in the market in the aggregate amount of approximately UAH 18.8 billion. In addition, in 2009 new T-bills in the amount of approximately UAH 8.0 billion were issued in exchange for certain remaining USD debt of the Government to the NBU. See "*Public Debt – Internal Debt*".

In the seven months ended 31 July 2010, the Government placed T-bills with maturities ranging from three months to ten years in the aggregate amount of approximately UAH 34.1 billion, including T-bills of approximately UAH 6.4 billion for the increase of the statutory capital of the state-owned banks and T-bills sold in the market in the aggregate amount of approximately UAH 27.7 billion.

As of 1 August 2010, non-residents held approximately 3.7 per cent. of Ukrainian T-bills. The share of T-bills held by non-residents decreased significantly in 2008 and 2009 due to foreign capital outflow from the domestic capital market resulting from the global financial downturn and the devaluation of the hryvnia, but further increased in the seven months ended 31 July 2010.

Interest Rates

During the financial markets crisis of late 1997 and 1998, yields of T-bills in the secondary market rose to over 70 per cent. but dropped to about 50 per cent. again in September 1998. In the primary market, average T-bill yields decreased further to 20.5 per cent. in 2000 and 9.8 per cent. in 2003. The average T-bill yields sold in the primary market fluctuated between 6.7 per cent. in 2007, 14.9 per cent. in 2008, 20.1 per cent. in 2009 and 14.1 per cent. in the seven months ended 31 July 2010.

The following table sets out the average refinancing rates and average yields of T-bills for the periods indicated:

	Treasury bill yields			
	Weighted average rates under all refinancing instruments	Including:		
		Average	T-bills sold in the market	T-bills issued for share capital increase
2007	10.1	6.7	6.7	N/A
2008	15.3	11.9	14.9	9.5
2009	16.7	12.2	20.1	9.5
Seven months ended 31 July 2010	12.3	13.2	14.1	9.5

Source: NBU

The NBU plans to increase the importance of its interest rate policy (which includes discount, overnight loan, overnight deposit, refinancing rates and certain other rates) as an instrument of monetary regulation. To this end, the NBU is contemplating important improvements in the regulation of short-term market interest rates through improving the approach to establishing interest rate corridors for asset and liabilities transactions and strengthening the connection between short-term and long-term interest rates through minimising the exposure of interest rates to non-market risks. The NBU believes that the efficiency of its interest rate policy could be strengthened if the Government continues to support further development and institutional improvement of the stock market and non-banking financial services markets.

Exchange Rates

The currency of Ukraine, the hryvnia, was introduced in 1996. In 2007, the hryvnia was stable against the dollar at the level of UAH 5.05 = U.S.\$1.00 and depreciated against the euro by 11.6 per cent. In 2008, drastic fluctuations of foreign currency demand and supply adversely affected hryvnia exchange rate dynamics and the hryvnia depreciated against the dollar by 52.5 per cent. and against the euro by 46.3 per cent. During 2009, the inflow of foreign currency into the economy was continuously declining, thus contributing to the deficit of foreign currency in the domestic foreign exchange market and hryvnia exchange rate fluctuations. In 2009, the hryvnia depreciated against the dollar by 3.7 per cent. and against the euro by 5.5 per cent. In the eight months ended 31 August 2010, due to an increased supply of foreign currency in the market, the hryvnia appreciated against the dollar by 1.24 per cent. and against the euro by 12.52 per cent.

In 2008 and 2009, the balance of intervention by the NBU had a deficit of U.S.\$3.9 billion and U.S.\$10.4 billion, respectively, that contributed to exchange rate stabilisation. In addition, at the end of 2008, the NBU introduced foreign currency auctions for banks as a new form of interventions and, starting from February 2009, the NBU introduced special auctions where foreign currency funds are sold to the population for the purpose of making payments under retail loans in foreign currencies. In 2009, the NBU sold foreign currencies in the amount equivalent to U.S.\$2,248.3 million at foreign currency auctions, including foreign currencies in the amount equivalent to U.S.\$1,413.1 million sold at the auctions for the retail loan repayments. In the eight months ended 31 August 2010, the NBU sold foreign currencies in the amount equivalent to U.S.\$68.2 million at the auctions for the retail loan repayments. The NBU believes that foreign currency auctions are an efficient instrument that contributed to the reduction of pressure in the Ukrainian foreign exchange market.

Improvement of the situation in the foreign exchange market allowed the NBU to resume purchase of foreign currency for replenishment of international reserves starting March 2010. In particular, in the eight months ended 31 August 2010, the balance of intervention by the NBU had a surplus of U.S.\$3,488.2 million.

Under the NBU's monetary lending policy principles for 2008 the official hryvnia/U.S. dollar exchange rate was initially targeted at between UAH 4.95 and 5.25 = U.S.\$1.00. However, on 22 May 2008 the NBU revalued the hryvnia against the U.S. dollar by 4 per cent. in an attempt to reduce inflationary pressure on the Ukrainian economy. The official hryvnia/U.S. dollar exchange rate on 22 May 2008 was UAH 4.85 to the dollar compared with UAH 5.05 to the dollar immediately prior to such revaluation.

However, starting from September 2008, as a result of decreased foreign currency proceeds under export transactions and external borrowings against the background of global financial downturn and reduced external demand, a significant deficit of foreign currencies was recorded at the Ukrainian foreign exchange market. On 7 October 2008, the NBU Council revised the official hryvnia/U.S. dollar exchange rate target at the level of UAH 4.95 = U.S.\$1.00 with possible fluctuations in the range of +/- 8 per cent., and on 27 October 2008 the NBU Council decided to remove the official hryvnia/U.S. dollar exchange rate target from the principles for monetary lending policy for 2008. In 2008, the average official hryvnia/U.S. dollar exchange rate was UAH 5.27 to the dollar while market exchange rates fluctuated at between UAH 4.57 and 8.90 = U.S.\$1.00.

During 2009, a deficit of foreign currencies was recorded on the Ukrainian foreign exchange market. This deficit was the result of negative market expectations, deepening of the global economic downturn, reduced external demand and reduced foreign currency inflows into the country in a form of export revenues and external borrowings. In 2009, the average official hryvnia/U.S. dollar exchange rate was UAH 7.79 to the dollar, while market exchange rates fluctuated at between UAH 7.57 and 8.65 = U.S.\$1.00. Starting from February 2010, supply of foreign currency in the foreign exchange interbank market has been increasing which facilitates strengthening of the hryvnia and a concurrent reduction of the gap between official and market exchange rates. In the eight months ended 31 August 2010, the average official hryvnia/U.S. dollar exchange rate was UAH 7.94 to the dollar, while market exchange rates fluctuated at between UAH 7.89 and 8.06 = U.S.\$1.00. In the eight months ended 31 August 2010, the hryvnia strengthened against the dollar both in the interbank market and in the cash foreign exchange market by 1.32 per cent. and 1.79 per cent., respectively.

The official hryvnia/U.S. dollar exchange rate reported by the NBU on 14 October 2010 was UAH 7.91 = U.S.\$1.00.

The following table sets out the average and period end official hryvnia/U.S. dollar exchange rates reported by the NBU:

	Average	Period end
	_____	_____
2005	5.12	5.05
2006	5.05	5.05
2007	5.05	5.05
2008	5.27	7.70
Three months ended 31 March 2009	7.70	7.70
2009	7.79	7.99
Three months ended 31 March 2010	7.99	7.93
Eight months ended 31 August 2010	7.94	7.89

Source: NBU

In line with the Memorandum on Economic and Financial Policy entered into in 2008-2009 within the framework of the IMF stand-by arrangement, the NBU has completed the transition to a flexible exchange rate by changing the methodology for the calculation of the official hryvnia/U.S. dollar exchange rate. Starting from May 2009, the official hryvnia/U.S. dollar exchange rate is determined based on the average weighted exchange rate at the Ukrainian foreign exchange market as of the preceding business day, with possible fluctuations +/- 2 per cent. The average monthly difference between the official hryvnia/U.S. dollar exchange rate and the average weighted exchange rate in the Ukrainian foreign exchange market was -0.7 per cent., -0.2 per cent., -0.8 per cent. and -2.0 per cent. in each of May, June, July and August 2009. However, in September 2009, the deficit of foreign currencies in the Ukrainian foreign exchange market heightened as

a result of a seasonal increase in payments under import contracts and negative market expectations caused by, among other things, expected increases in minimum wages and pensions. In view of the temporary nature of such factors, the NBU was conducting interventions in the foreign exchange market and resorted to broadening the gap between the official and market exchange rates: in September 2009, the average monthly difference between the official hryvnia/U.S. dollar exchange rate and the average weighted exchange rate in the Ukrainian foreign exchange market was -3.4 per cent. However, from October 2009, the gap between the official and market exchange rates returned to the +/- 2 per cent. range. In particular, in the fourth quarter of 2009 and the seven months ended 31 July 2010, the average monthly difference between the official hryvnia/U.S. dollar exchange rate and the average weighted exchange rate in the Ukrainian foreign exchange market fluctuated between -1.6 per cent. and 0.15 per cent.

In 2010, growth of foreign currency inflows into Ukrainian economy was gradually restoring, along with the slow-down of foreign currency outflow from Ukraine, as a result of which the foreign currency deficit at the interbank market changed into the foreign currency surplus. This trend facilitates strengthening of hryvnia market exchange rates and replenishment of international reserves. Starting from the end of August 2010, a seasonal increase in the foreign currency demand has been recorded at the foreign exchange market, such an increase being aggravated by negative market expectations caused by, among other things, increases in tariffs for municipal services and prices for certain consumer goods. At the same time, the NBU does not expect destabilisation of the foreign exchange market until the end of 2010.

The NBU expects that until the end of 2010 its exchange rate policy will continue to be based on the main principles of the monetary-lending policy for 2010 and the commitments undertaken by Ukraine as set forth in the Memorandum on Economic and Financial Policy entered into within the framework of the IMF stand-by arrangement. In particular, in 2010, the NBU intends to continue pursuing a flexible exchange rate policy, avoid multiple exchange rates and comply with the requirements with respect to the minimum level of net international reserves.

The NBU also has a number of other monetary tools that it can use to support the hryvnia. These include licensing and registration requirements applicable to movements of financial capital and a maximum 180-day period between the prepayment of imported goods and their delivery, as well as reserve requirements and open currency position limits.

Following a number of measures taken by the NBU from 2004 through 2006 to liberalise the foreign exchange market and currency control rules, in 2007, the NBU further liberalised the regulations governing cross-border movement of national currency and also amended the regulations on foreign borrowings by Ukrainian residents, such amendments included, amongst others, an introduction of a simplified loan agreement registration procedure for Ukrainian banks and a clarification of the maximum interest rate restrictions. In addition, in 2007, the NBU broadened the list of transactions permitted for the foreign exchange market participants. In particular, insurance companies are now entitled to purchase and transfer funds in foreign currencies under re-insurance agreements with foreign re-insurers, and banks have the right to purchase coins from foreign mints.

In 2007, the NBU started implementing gradual measures aimed at reducing the level of dollarisation in the economy (calculated as the ratio of the amount of foreign currency deposits to the amount of cash in national currency outside banks, bank deposits and debt securities issued by banks) and increasing the use of the national currency for lending. For example, with effect from April 2007, the NBU introduced increased provisioning requirements for loans in foreign currency and, with effect from 20 November 2007, the NBU has required banks to create provisions for loans raised from foreign banks. See *“The Banking System and Securities and Financial Services Markets in Ukraine – The Banking System of Ukraine”*. These and other measures have contributed to the deceleration in the rate of the dollarisation of the economy: in 2007, the growth rate of the economy dollarisation level fell to 22.8 per cent. However, in 2008, the economy dollarisation level increased to 30.6 per cent., which was followed by a further increase to 31.7 per cent. in 2009 and a decrease to 29.6 per cent. in the seven months ended 31 July 2010. In addition, in July 2007, the NBU established a legal framework within which the EBRD can provide loans in the national currency to residents of Ukraine.

In 2008, the NBU continued implementing measures aimed at further liberalising the foreign exchange market. These measures included permission for individuals to make wire transfers abroad, if such transfers are unrelated to entrepreneurial or investment activities, without any limitation as to amount, as well as authorisation to legal entities to pay accession or membership fees to international organisations without the need to receive an individual licence from the NBU. In addition, State Enterprise “Ukrposhta” (Ukrainian Mail) was authorised to perform foreign exchange operations as well as individual transfers abroad, and certain changes have been made in order to accelerate settlements at the interbank foreign exchange market. Furthermore, from 4 November 2008, pursuant to the amended foreign currency trade rules, Ukrainian banks are required to perform all foreign currency trades only at the time when the NBU deal confirmation system is operative; thus, the NBU is able to receive full real-time information on conditions on the Ukrainian interbank foreign exchange market (market exchange rates and trade volumes) and, based on such information, to adjust its forecasts and actions as appropriate.

In 2008-2009, the NBU implemented a number of measures aimed at improving the foreign investment regime and increasing the investment attractiveness of Ukraine’s economy. These measures included permitting foreign investors to place deposits in hryvnias with Ukrainian banks, removing limitations on a maximum period during which hryvnia funds must be used for a foreign investment and simplifying purchase of foreign currency funds for repatriation of investments made into blue chip companies. Also, in 2008, the NBU liberalised rules governing physical transfers of cash and banking metals out of and into Ukraine. From October 2008, taking into account increased interest rates under borrowings on the international markets, the NBU removed maximum interest rate limitations for all foreign currency loans other than loans with maturities of less than one year; however, the maximum interest rate limitations for loans with maturities of more than one year are reinstated starting 15 November 2009.

From October 2008, the NBU introduced a number of currency control limitations, some of which have since been removed. Restrictions that were introduced beginning in October 2008 but removed by 23 October 2009 included a restriction on purchasing foreign currency for payments to non-residents for imports of products or services that are not transported to or used in the territory of Ukraine and a UAH 75,000 limitation on the maximum amount permitted for transfer abroad by individuals for certain non-trade purposes. As of 30 September 2010, the following restrictions remain in place:

- limitations on operations in hryvnias that may be performed through correspondent accounts of non resident banks opened with Ukrainian banks;
- a five business day maximum period during which a resident company must use foreign currency funds purchased on the foreign exchange market;
- a restriction, with certain exceptions, on exchange of foreign currencies that are not freely convertible into hard currencies and *vice versa*;
- a prohibition on banks acting as both seller and buyer in transactions on sale/purchase of a particular foreign currency for hryvnia at the interbank foreign exchange market; and
- restrictions on opening correspondent accounts in hard currencies in certain foreign banks.

In addition, in April 2009, the NBU introduced a new methodology for calculating open currency position limits of banks.

Within the framework of the regulation of the foreign exchange market, the NBU is currently considering routes for further development in currency risk hedging instruments and improving procedures for the licensing of certain foreign exchange transactions. In addition, the NBU plans to improve the main mechanisms and instruments of the regulation of financial capital import and export. To this end, the NBU expects that a new law on currency control will be enacted contributing to, amongst other things, a reduction of the use of foreign currencies in the territory of Ukraine.

In February 2009, due to the necessity to reduce volumes of speculative transactions at the interbank foreign exchange market, the NBU imposed a temporary prohibition on performance of sales/purchases of foreign currency on “forward” and “spot” terms. Such restrictions for spot operations were removed in September

2009 and restrictions for forward operations were removed in October 2009. Starting from 20 November 2009, Ukrainian banks may sell, within a business day, to one individual cash foreign currencies in an amount not exceeding the equivalent of UAH 80,000. A bank is also prohibited, within a business day, from changing its cash foreign exchange rates as compared to the rates set by the bank at the beginning of the day.

International Reserves

As at 31 December 2007 as compared to 31 December 2006, international reserves increased by U.S.\$10,207.3 million, or 45.9 per cent., to U.S.\$32,463.3 million, equivalent to approximately 4.7 months of import coverage. In 2007, international reserves dynamics were influenced by proceeds from the external borrowings, including placement of the notes of external state borrowing, the NBU intervention surplus and positive exchange difference as a result of the decline in value of the U.S. dollar as compared to other hard currencies.

At 31 December 2008 as compared to 31 December 2007, international reserves decreased by U.S.\$920.1 million, or 2.8 per cent., to U.S.\$31,543.2 million, equivalent to approximately 6.9 months of import coverage. This decrease was principally attributable to large volumes of sales by the NBU of foreign currencies in the fourth quarter of 2008, volumes of state debt repayments as well as positive exchange difference as a result of the strengthening in value of the U.S. dollar as compared to other hard currencies. At the same time, in 2008, the dynamics of the international reserves were positively influenced by the state borrowings from the World Bank, EU and IMF.

As at 31 December 2009 as compared to 31 December 2008, international reserves decreased by U.S.\$5.0 billion or 16.0 per cent. to U.S.\$26,505.1 million, equivalent to approximately 4.9 months of import coverage. The decrease was attributable to the deficit of the balance of the NBU interventions and volumes of state debt repayments, as well as to the transfer by the Government of its foreign currency funds held at the NBU to the Government's accounts at commercial banks. In May and July 2009, international reserves increased as a result of borrowings from the IMF.

In the eight months ended 31 August 2010, international reserves increased by U.S.\$6,187.0 million or 23.3 per cent. to U.S.\$32,692.1 million, equivalent to approximately 5.4 months of import coverage.

Dynamics of international reserves

	As at 31 December			As at 31 August	
	2007	2008	2009	2009	2010
	<i>U.S.\$ millions</i>				
International reserves ⁽¹⁾	32,463.3	31,543.2	26,505.1	28,871.0	32,692.1
including:					
Monetary gold ⁽²⁾	490.1	529.6	680.5	588.3	781.4
Reserves in SDR and reserve position in IMF	2.8	8.6	63.6	1,599.4	12.6
Foreign currency ⁽³⁾	31,970.4	31,005.0	25,761.0	26,683.3	31,898.1
Import coverage (month) ⁽⁴⁾	3.9	6.7	4.9	5.7	5.4

Notes:

(1) International reserves are equal to the sum of foreign currency, SDR and monetary gold.

(2) Cost of gold is calculated on the basis of the price for one ounce of gold in U.S. dollars at the London Precious Metal Exchange.

(3) Including securities issued by non-residents.

(4) Imports of goods and services of the immediately succeeding months are used for these calculations.

Source: NBU

THE BANKING SYSTEM AND SECURITIES AND FINANCIAL SERVICES MARKETS IN UKRAINE

The Banking System in Ukraine

A two-tier banking system exists in Ukraine, comprising the National Bank of Ukraine (NBU), which supervises the commercial banks, and the commercial banks, which operate as multi-purpose or specialised (mortgage, investment, savings or clearing) banks. Following Ukraine's accession to the WTO in May 2008, Ukraine's banking system may include branches of foreign banks established and functioning in the territory of Ukraine. The Law of Ukraine "On Banks and Banking" gave the NBU power and independence to pursue monetary policy and to regulate and supervise the banking sector by, for example, authorising the NBU to revoke a bank's licence to conduct banking activities and to initiate a liquidation of banks whose licences have been revoked.

As of 1 January 2010, 197 banks were registered in Ukraine (of which 182 held licences from the NBU to perform banking transactions with the remaining 15 banks including banks whose license had been revoked or had not yet been granted) with a total registered and paid statutory capital of UAH 119.2 billion, representing a 44.6 per cent. increase in statutory capital in 2009 following a 92.3 per cent. increase during 2008 and a 63.2 per cent. increase during 2007. As of 1 January 2010, the total assets of all banks in Ukraine amounted to UAH 1,001.6 billion (U.S.\$125.4 billion), their credit portfolio amounted to UAH 747.3 billion (U.S.\$93.6 billion), each of their balance-sheet capital (net worth) and deposit capital received from corporate entities amounted to UAH 115.2 billion (U.S.\$14.4 billion), and their deposits from individuals amounted to UAH 210.0 billion (U.S.\$26.3 billion), using the then current official hryvnia/U.S. dollar exchange rate UAH 7.99 = U.S.\$1.00.

As at 1 August 2010, 194 banks were registered in Ukraine (of which 176 banks held licences from the NBU to perform banking transactions with the remaining 18 banks including banks whose license had been revoked or had not yet been granted) with a total registered and paid statutory capital of UAH 134.1 billion representing an increase of 12.5 per cent. in statutory capital in the seven months ended 31 July 2010. As at 1 August 2010, the total assets of all banks in Ukraine amounted to UAH 1,041.2 billion (U.S.\$131.9 billion), their credit portfolio amounted to UAH 725.3 billion (U.S.\$91.9 billion), their balance-sheet capital (net worth) amounted to UAH 128.0 billion (U.S.\$16.2 billion), their deposit capital received from corporate entities amounted to UAH 127.0 billion (U.S.\$16.1 billion), and their deposits from individuals amounted to UAH 247.3 billion (U.S.\$31.3 billion), using the then current official hryvnia/U.S. dollar exchange rate UAH 7.89 = U.S.\$1.00.

For 2010, the commercial banks operating in Ukraine were divided by the NBU into four groups according to the value of their assets as at 1 December 2009. As of 1 December 2009, the first group included 18 major banks with total assets of more than UAH 13,000 million; the second group included 20 banks with total assets ranging from UAH 4,000 million to UAH 13,000 million; the third group included 21 banks with total assets ranging from UAH 1,500 million to 4,000 million; and the fourth group included 122 banks with total assets of less than UAH 1,500 million. Though as at 1 August 2010, certain banks have exceeded or have not reached the thresholds for their respective groups, throughout the year they remained in the groups to which they were allocated by the NBU as at 1 December 2009.

The minimum statutory capital requirements for national, regional and cooperative banks established prior to 4 October 2006 are €5 million, €3 million and €1 million, respectively. From 4 October 2006 through 24 November 2009, the minimum statutory capital requirement for all banks at the time of their registration was €10 million. With effect from 24 November 2009, the minimum statutory capital requirement for all banks at the time of their registration is UAH 75 million. Such requirement applies only to banks which have been registered after 24 November 2009. In addition, from 4 October 2006 until 5 August 2009 banks may have been established only in the form of an open joint stock company or a cooperative bank (i.e., it was not permitted to establish banks in the form of a closed joint stock company or a limited liability company and banks existing in the form of a closed joint stock company or a limited liability company had three years until 4 October 2009 to change their form into an open joint stock company or a cooperative bank).

Furthermore, on 30 April 2009, the Law of Ukraine “On Joint-Stock Companies” entered into force. This law provides that joint stock companies in Ukraine are to be established in the form of a public or private joint stock company. Companies established previously as open joint-stock companies or closed joint-stock companies are required to reorganise into a public or private joint-stock companies by 30 April 2011. Pursuant to the amendments to the Law on Banks and Banking, which became effective on 5 August 2009, banks may be established only in the form of a public joint stock company or a cooperative bank.

In Ukraine, the regulatory capital of a bank (i.e. the sum of principal and additional capital) must not be less than the minimum statutory capital. With effect from October 2008, the NBU revised the minimum regulatory capital requirement for the banks establishing a €10 million minimum amount of regulatory capital for all banks (as opposed to previously-effective differentiated requirements based on the period of a bank’s activity). With effect from 17 July 2010, the NBU revised the minimum regulatory capital requirement for the banks establishing a UAH 120 million minimum amount of regulatory capital for all banks. Banks with the regulatory capital below the minimum required amount have to increase the capital to comply with the newly established requirements by 1 January 2012. Regulatory capital requirements are subject to periodic increases, which may present problems for banks that are insufficiently capitalised.

The minimum regulatory capital adequacy ratio of existing banks is currently 10 per cent. For banks that have been operating for less than 12 months, this ratio is 15 per cent., and for banks that have been operating between 12 and 24 months, this ratio is 12 per cent. The average regulatory capital adequacy ratio of all Ukrainian banks was 20.0 per cent. as of 1 August 2010. The minimum ratio of regulatory capital to total assets reflects the amount of the regulatory capital necessary for the banks to perform active operations and is set by the NBU at 9 per cent. The average ratio of regulatory capital to total assets of all Ukrainian banks was 14.25 per cent. as of 1 August 2010. Starting from December 2007, the NBU Directive on Ukrainian Banking Activity Regulation requires banks to take account of foreign exchange risks in the calculation of the regulatory capital adequacy ratio as well as to maintain sufficient level of regulatory capital to cover risks arising out of mismatches in the assets’ and liabilities’ maturities.

In 2007, the registered and paid statutory capital of Ukrainian banks increased by 63.2 per cent. and amounted to UAH 42.9 billion as at 31 December 2007, their regulatory capital increased by 75.6 per cent. and amounted to UAH 72.3 billion, their total assets increased by 75.3 per cent. and amounted to UAH 619.0 billion whilst balance-sheet capital (net worth) increased by 63.5 per cent. and amounted to UAH 69.6 billion as at 31 December 2007. In 2008, the registered and paid statutory capital of Ukrainian banks increased by 92.3 per cent. during the course of the year and amounted to UAH 82.5 billion at 31 December 2008, their regulatory capital increased by 70.3 per cent. and amounted to UAH 123.1 billion, their total assets increased by 57.2 per cent. and amounted to UAH 973.3 billion and the balance-sheet capital (net worth) of these banks increased by 71.4 per cent. and amounted to UAH 119.3 billion.

In 2009, the registered and paid statutory capital of Ukrainian banks increased by 44.6 per cent. during the course of the year and amounted to UAH 119.2 billion at 31 December 2009; their regulatory capital increased by 10.3 per cent. and amounted to UAH 135.8 billion, and the balance-sheet capital (net worth) of these banks decreased by 3.4 per cent. and amounted to UAH 115.2 billion as at the same date. In the seven months ended 31 July 2010, the regulatory capital of Ukrainian banks increased by 7.8 per cent. (compared with an increase of 3.2 per cent. in the seven months ended 31 July 2009) and amounted to UAH 146.4 billion as at 1 August 2010, and the registered and paid statutory capital increased by 12.5 per cent., amounting to UAH 134.1 billion (compared with increase of 25.2 per cent. in the seven months ended 31 July 2009). In the seven months ended 31 July 2010, balance-sheet capital (net worth) increased by 11.1 per cent. (as compared to a 0.7 per cent. increase in the seven months ended 31 July 2009) and amounted to UAH 128.0 billion as at 1 August 2010. The 7.8 per cent. increase in the regulatory capital of Ukrainian banks recorded in the seven months ended 31 July 2010 was largely attributable to the increase in registered and paid-in statutory capital by UAH 14.9 billion and the increase in subordinated debt by UAH 2.6 billion in this period, respectively.

Two of the largest banks in Ukraine, the State Export-Import Bank of Ukraine (Ukreximbank) and the State Oschadnyi Bank (Savings Bank), are fully state-owned. From 2006 to 31 July 2010, the Cabinet of Ministers approved an increase in the statutory capital of Oschadnyi Bank and Ukreximbank by UAH 13,189.0 million

and 15,649.5 million, respectively. In particular, the statutory capital of Ukreximbank was increased in 2009 and in the seven months ended 31 July 2010, by UAH 6,941.0 million and UAH 6,390.0 million, respectively. The statutory capital of Oschadnyi Bank was not increased during these periods.

As at 1 August 2010, 52 banks in Ukraine had some foreign shareholders, and 20 of these banks were fully foreign-owned. The share of foreign capital in the total registered statutory capital of Ukrainian banks increased from 35.0 per cent. as at 31 December 2007 to 36.7 per cent. as at 31 December 2008, respectively, but fell to 35.8 per cent. as at 31 December 2009 and 35.7 per cent. as at 1 August 2010.

In recent years, certain banks with foreign capital became more active in the Ukrainian market. The Polish PKO Bank Polski S.A. acquired Kredyt Bank, Russian NRB-Ukraine acquired Energobank and SEE International Group acquired Bank Ajio through the Lithuanian Vilniaus Bankas. Significant takeovers in 2005-2009 also include the acquisition by Raiffeisen International Bank-Holding AG (Austria) of Bank Aval, the acquisition by BNP Paribas of 51 per cent. of the shares in UkrSibbank, the acquisition by the Russian Vneshtorgbank of 98 per cent. of the shares in Bank Mriya, the acquisition by Credit Agricole S.A. of 98 per cent. of the shares in Index Bank, the acquisition by the Hungarian OTP Bank of 100 per cent. of the shares in Raiffeisen Bank Ukraina, the acquisition of Prestige Bank by the Austrian Erste Bank, the acquisition of Tas Kommerzbank by Swedbank, the acquisition of UkrSotsbank by Bank Austria Creditanstalt AG, the acquisition of Bank Forum by Commerzbank, the acquisition of Pravex Bank by Intesa Sanpaolo and the acquisition by Vnesheconombank of Prominvestbank.

The NBU expects the Ukrainian banking market to become more competitive as a result of the enactment of laws permitting foreign banks to operate branch offices in Ukraine and Ukraine's accession to the WTO. Starting from 16 May 2008, foreign banks may operate branch offices in Ukraine, subject to certain access criteria established by the Law "On Banks and Banking". One of the pre requisites to be satisfied before general permission is granted to open and operate a branch is that the NBU and a bank supervisory authority of the foreign state where the relevant parent is head-quartered execute an agreement about their co-operation in the bank supervision field and the harmonisation of principles and terms of such supervision. To date, only a few such agreements have been signed by the NBU, including with banking regulators of such countries as Armenia, Belarus, China, Cyprus, Kyrgyzstan, Latvia, Lithuania, Luxembourg, Poland, Russia, Hungary and Turkey.

The banking sector has suffered from a number of significant weaknesses, which have included undercapitalisation, weak corporate governance and management, poor asset quality and excessive political interference in certain banks. Since 1997, Ukraine has been implementing a series of banking sector reforms under the IMF reform programme with the aim of supporting commercial banks that undertake structural reforms and demonstrate long-term stability. Since the beginning of 1998, banks have been required to prepare accounts that are based in many respects on International Accounting Standards and International Financial Reporting Standards.

The 2001 Law of Ukraine "On the Fund for Guaranteeing the Deposits of Individuals" (the "Deposits Securing Law") introduced a system of securing deposits held by individuals with Ukrainian banks that modified the existing system, which was established in 1998 by the Presidential Decree "On Measures for the Protection of Rights of Individuals — Depositors of Commercial Banks of Ukraine" (the "Decree"). Pursuant to the Deposits Securing Law, commercial banks in Ukraine are obliged to remit to the Fund, which was established under the Decree and which operates according to the Deposits Securing Law, an initial duty in the amount of 1 per cent. of their registered statutory capital, payable once after obtaining a banking licence, as well as a regular duty in the amount of 0.25 per cent. of the aggregate amount of deposits, including interest accrued, payable twice a year and a special duty established by the Fund upon the occurrence of certain circumstances. The Fund guarantees deposits with commercial banks, including any interest, up to a maximum of UAH 150,000 (as of 5 November 2008) per depositor with each such bank. Deposits are recognised as unavailable, i.e. eligible for compensation, on the day of appointment of a bank's liquidator. The Deposits Securing Law does not apply to the Oschadnyi Bank, whose retail deposits are guaranteed by the State. Since Ukraine's accession to the WTO, the Deposits Securing Law applies to branch offices of foreign banks operating in Ukraine. As at 1 August 2010, the Fund had 175 member banks and the total accumulated by the Fund was approximately UAH 3,093.0 million. In addition, pursuant to the Law

“On Immediate Measures to Avoid Negative Consequences of the Financial Crisis and Amendments to Certain Legislative Acts of Ukraine” enacted on 31 October 2008, the NBU transferred UAH 1.0 billion to increase funds available for the Fund for pay-outs to depositors of bankrupt banks. Furthermore, the NBU has approved its regulations on extension of loans by the NBU to the Fund in certain circumstances including, among other things, if the aggregate amount of deposits to be reimbursed by the Fund exceeds 80 per cent. of the Fund’s available resources.

The NBU is responsible for the reorganisation or closure and liquidation of insolvent banks to strengthen confidence in the banking sector. In 2001, one of Ukraine’s largest banks, Bank Ukraina, was declared insolvent by the NBU, the representative of which was appointed liquidator of Bank Ukraina. The liquidation of Bank Ukraina was finalised in April 2009. As at 31 December 2009 and 3 August 2010, 14 and 18 banks were in liquidation, respectively. See “– *Recent Developments in the Banking Sector*”.

Banks are required to submit an annual report that contains audited financial statements as well as a general description of their business. Banks are also required to submit to the NBU financial and statistical data on daily, weekly, monthly and other bases that permits permanent review by the NBU of the banks’ performance and financial position. In addition, banks are required to publish in printed mass media quarterly and annual financial statements as well as certain other information required by the NBU, including information on bank’s shareholders directly or indirectly holding 10 per cent. or more of the share capital of the bank.

The NBU oversees the activities of commercial banks using both off-site and on-site inspections and through a system of audits by auditors certified by the NBU and the Audit Chamber of Ukraine. The planned inspection may be carried out not more than once per year. The NBU may also decide to carry out an extra inspection if it has sufficient grounds for such inspection.

If a bank violates banking laws and regulations or engages in risky operations threatening the interests of its depositors or other creditors, the NBU may use one of the various measures provided for in the Law of Ukraine “On Banks and Banking”, depending on the nature and the extent of the violation. Such measures include suspension of dividend payments; increase of provisioning requirements; limitation, termination or suspension of certain high risk transactions; prohibition on extending unsecured loans; the imposition of penalties on the bank and its management; and the appointment of a temporary administrator.

Banks must keep reserves to cover exposures under asset transactions (potential losses from lending and securities transactions and accounts receivable) and review those provisions on a monthly basis. Some loans and securities transactions do not require any provisions. These include “budget loans”, credit transactions between entities within the system of one bank (for banks 100 per cent. owned by foreign entities, credit transactions with the parent company if such company is assigned an investment-grade credit rating), real-estate backed leasing transactions, subordinated loans, uncommitted off balance sheet credit lines (other than commitments extended to banks), funds in foreign currency transferred to the NBU, securities issued by central state executive authorities and the NBU as well as shares in stock exchanges, securities depositaries, payment systems and credit bureaus. The NBU sets forth separate provisioning requirements for loans in national and foreign currency as well as for certain consumer loans.

Loans are classified into five categories, subject to varying provisioning requirements. The following provisioning requirements are set forth for loans in national currency: 1 per cent. for standard loans; 5 per cent. for loans on watch; 20 per cent. for substandard loans; 50 per cent. for doubtful loans; and 100 per cent. for bad loans. Provisioning requirements applicable to loans in foreign currency are higher than for loans in national currency in line with an NBU policy aimed at reducing credit risks, especially under loans in foreign currencies and are as follows: 2 per cent. (50 per cent. for loans to borrowers who have no foreign currency earnings) for standard loans; 7 per cent. (100 per cent. for loans to borrowers who have no foreign currency earnings) for loans on watch; 25 per cent. (100 per cent. for loans to borrowers who have no foreign currency earnings) for substandard loans; 60 per cent. (100 per cent. for loans to borrowers who have no foreign currency earnings) for doubtful loans; and 100 per cent. for bad loans. Provisioning requirements applicable to consumer loans in hryvnia are: 2 per cent. for standard loans; 10 per cent. for loans on watch; 40 per cent. for substandard loans; 80 per cent. for doubtful loans; and 100 per cent. for bad loans. Provisioning requirements applicable to consumer loans in foreign currencies are: 50 per cent. for standard loans and 100 per cent. for loans on watch, substandard loans, doubtful loans and bad loans. Since October 2008, banks

have been prohibited from purchasing foreign currency for the purpose of forming provisions under loans denominated in foreign currency.

On 20 May 2010, Parliament approved a law that instructed the NBU to establish, within one month of the law coming into effect, provisioning requirements not higher than 3 per cent. with respect to foreign currency-denominated standard, substandard loans and loans on watch for borrowers who have no foreign currency earnings. On 16 June 2010, however, the President submitted for consideration by Parliament a draft law that would countermand this instruction to the NBU. As at 30 August 2010, Parliament has not yet held hearings on the President's draft law.

Performance and Balance Sheet of the Banking System

The banking sector's asset and liability structure reflects the history of Ukraine's macro-economic development.

The hyperinflation experienced from 1992 to 1995 and bank defaults on household deposits undermined public confidence in the banking sector. The banking sector continued to derive the bulk of its profit from foreign exchange operations in 1997. In 1998, the NBU restricted foreign exchange transactions to prevent a further destabilisation of the hryvnia. The 1998-1999 recession led to a sharp reduction of loan disbursements to domestic market participants. The poor credit quality of loan portfolios and the lack of institutional infrastructure for debt recovery accounted for a major part of losses on long-term credits. From 2002 until 2008, bank lending to the economy was rapidly increasing and in 2006 and 2007 it increased by 71.0 per cent. and 74.1 per cent., the highest growth rates in recent years. The rapid accumulation of credit resources, improvement of the term structure and reduction in interest rates on credits were the main reasons for the development of lending activity. At the same time, efforts of Ukrainian banks to increase long-term lending against a background of scarcity of long-term resources intensified liquidity and solvency risks of the Ukrainian banking system as a result of mismatches in the term structure of assets and liabilities. For instance, in 2008, long-term loans increased by 73.9 per cent., or UAH 215.8 billion, while long-term deposits grew by only 22.6 per cent., or UAH 29.4 billion. In 2009, long-term loans decreased by 3.8 per cent., or UAH 19.7 billion and long-term deposits decreased by 49.9 per cent., or UAH 79.4 billion. In the seven months ended 31 July 2010, long-term loans decreased by 4.6 per cent., or UAH 20.2 billion, while long-term deposits increased by 26.7 per cent., or UAH 21.3 billion. In 2008, the gap between long-term assets and liabilities increased by UAH 8.4 billion. In 2009, the gap between long-term assets and liabilities decreased by UAH 77.0 billion due to suspension of lending by banks. In the seven months ended 31 July 2010, this gap became negative and amounted to UAH 9.5 billion. See “– *Recent Developments in the Banking Sector*”.

The NBU continues to balance the size and the structure of assets and liabilities of Ukrainian banks and to limit the risks inherent to their activities. One of the measures taken for this purpose is the introduction, starting from December 2007, of a requirement that banks take account of foreign exchange risks in the calculation of the regulatory capital adequacy ratio and maintain a sufficient level of regulatory capital to cover risks arising out of mismatches in the maturities of their assets and liabilities.

Liabilities

In 2009, liabilities of banks decreased by 5.2 per cent. or UAH 41.7 billion and amounted to UAH 765.1 billion as at 1 January 2010, caused mainly by the decrease of:

- interbank credits and deposits by 22.1 per cent., or UAH 55.0 billion;
- deposits of corporate entities by 20.0 per cent. or UAH 28.7 billion; and
- loans from international and other financial organisations by 19.3 per cent. or UAH 10.0 billion.

As at 1 January 2010, the ratio of foreign currency liabilities to total liabilities was 59.7 per cent.

As at 1 August 2010, the aggregate liabilities of Ukrainian banks amounted to UAH 773.8 billion, an increase of 1.1 per cent. during the seven months ended 31 July 2010, caused mainly by the increase in deposits of

individuals and corporate entities by 17.8 per cent. and 10.2 per cent., respectively, which was to a certain extent off-set by the decline in interbank loans and deposits, and funds from the NBU, which decreased during this period by 15.1 per cent. and 8.6 per cent., respectively. As at 1 August 2010, the proportion of foreign currency liabilities to total liabilities was 57.2 per cent.

As of 1 August 2010, Ukrainian banks had the following liability structure:

- funds of economic entities amounted to UAH 127.0 billion (16.4 per cent. of the total sum of bank liabilities);
- retail deposits amounted to UAH 247.3 billion (32.0 per cent.);
- interbank credits and deposits amounted to UAH 164.5 billion (21.3 per cent.);
- budget and non-budget funds amounted to UAH 4.4 billion (0.6 per cent.);
- funds of the NBU amounted to UAH 77.2 billion (10.0 per cent.);
- funds of non-bank financial institutions amounted to UAH 13.1 billion (1.7 per cent.);
- subordinated debt amounted to UAH 30.9 billion (4.0 per cent.);
- own debt securities amounted to UAH 2.1 billion (0.3 per cent.);
- loans from international and other financial institutions amounted to UAH 41.1 billion (5.3 per cent.);
- correspondent accounts of other banks amounted to UAH 10.5 billion (1.4 per cent.); and
- other liabilities amounted to UAH 55.7 billion (7.0 per cent.).

As at 1 August 2010, the liabilities of Ukrainian banks to foreign entities amounted to UAH 248.6 billion or approximately 32.1 per cent. of their total liabilities. Out of this UAH 248.6 billion, liabilities of foreign-owned banks accounted for approximately 76 per cent. of the total due to, among other things, extensive lending to such banks by their parent banks.

Assets

In 2009, net assets (total assets less accumulated reserves on active transactions) decreased by 4.9 per cent. compared to 2008 and reached UAH 880.3 billion. During the same period, total assets increased by 2.9 per cent. and amounted to UAH 1,001.6 billion. These trends were mainly the result of the decrease of banks' credit portfolios by 5.7 per cent. in 2009.

In the seven months ended 31 July 2010, net assets (total assets less accumulated reserves relating to active transactions) increased by 2.4 per cent. to UAH 901.8 billion. During the same period, total assets increased by 3.9 per cent. to UAH 1,041.2 billion. As at 1 August 2010, Ukrainian banks' total assets consisted of the following assets:

- credit portfolio amounted to UAH 725.3 billion (69.7 per cent.);
- investments in securities amounted to UAH 66.5 billion (6.4 per cent.);
- accounts receivable amounted to UAH 34.7 billion (3.3 per cent.);
- fixed assets and intangible assets amounted to UAH 38.9 billion (3.7 per cent.);
- accrued revenues that have not yet been received amounted to UAH 47.5 billion (4.6 per cent.);
- funds of the NBU amounted to UAH 34.1 billion (3.3 per cent.);
- cash and bank metals amounted to UAH 22.5 billion (2.1 per cent.); and
- other assets amounted to UAH 71.7 billion (6.9 per cent.).

The credit portfolio of Ukrainian banks decreased by 3.0 per cent. in the seven months ended 31 July 2010, such decline being mainly a result of decline in retail loans, which decreased during this period by 10.6 per cent. In this period, loans denominated in foreign currencies decreased by 7.1 per cent., while loans in hryvnia increased by 1.7 per cent. The credit portfolio of Ukrainian banks has the following structure as of 1 August 2010:

- credits granted to economic entities amounted to UAH 477.1 billion (65.8 per cent. of the total volume of the credit portfolio);
- credits granted to individuals amounted to UAH 199.0 billion (27.4 per cent.);
- deposits placed with other banks and credits granted to other banks amounted to UAH 42.5 billion (5.9 per cent.);
- credits granted to non-banking financial institutions amounted to UAH 0.1 billion (0.01 per cent.); and
- credits granted to state authorities amounted to UAH 6.6 billion (0.9 per cent.).

In the credit portfolio of Ukrainian banks in 2009, long-term credits decreased by 3.8 per cent. and credits in investment activities increased by 4.6 per cent. In the credit portfolio of Ukrainian banks in the seven months ended 31 July 2010, long-term credits decreased by 4.6 per cent. and credits in investment activities decreased by 1.4 per cent., respectively. The decrease in the amount of long-term loans in 2009 and the seven months ended 31 July 2010 was largely due to outflow of customers' funds from the banking system in the first quarter of 2009, limited access to borrowings in international markets; reduction in the share of long-term funds in the borrowings' structure, increase in the volumes of problem loans and resulting increase in provisions to cover exposures under such loans; deterioration in financial standing of borrowers as a result of unfavourable conditions in external markets and low domestic demand; lack of liquid security under loans and absence of an efficient insurance mechanism; and limited investment opportunities for the use of idle funds.

The share of doubtful and bad credits in the credit portfolio increased from 2.5 per cent. as at 31 December 2007 to 3.8 per cent. as at 31 December 2008, 13.1 per cent. as at 31 December 2009 and 14.6 per cent. as at 31 July 2010. The significant increase in problem credits in 2009 was largely attributable to the deterioration in the financial standing of corporate entities and a decrease in household income against the background of overall economic and political instability. In the seven months ended 31 July 2010, the amount of doubtful and bad loans increased by 7.7 per cent., or UAH 9.0 billion, including an increase of doubtful and bad credits granted to economic entities by 3.1 per cent., or UAH 2.3 billion, and an increase of doubtful and bad retail loans by 15.4 per cent., or UAH 5.1 billion.

The IMF, in connection with approving in July 2010 a new stand-by agreement with Ukraine provided two estimates for loans which could be categorised as nonperforming. Under a broad definition of non-performing loans that includes loans classified as substandard, doubtful and loss, the IMF estimated that 41.6 per cent. of loans held by Ukrainian banks were non-performing as at 31 March 2010. Under a narrower definition that does not count as nonperforming those substandard loans that are serviced in a timely manner, the IMF estimated that 15 per cent. of loans were non-performing as at 31 March 2010.

In comparison to 2008, revenues of banks increased in 2009 by 16.7 per cent. and as of 1 January 2010 amounted to UAH 143.0 billion, which included interest revenues of UAH 121.1 billion (84.7 per cent. of total revenues), commission revenues of UAH 16.2 billion (11.3 per cent.), results from trade operations of UAH 2.9 billion (2.0 per cent.) and other revenues of UAH 2.8 billion (2.0 per cent.).

In comparison to the same period in 2009, in the seven months ended 31 July 2010, revenues of banks decreased by 7.2 per cent. and, as of 1 August 2010, amounted to UAH 78.4 billion, which included interest revenues of UAH 66.7 billion (85.1 per cent. of total revenues), commission revenues of UAH 8.2 billion (10.5 per cent.), results from trade operations of UAH 1.0 billion (1.3 per cent.) and other revenues of UAH 2.5 billion (3.1 per cent.).

Recent Developments in the Banking Sector

In recent years, Ukrainian banks have aggressively expanded their credit portfolios, largely due to improved access to foreign financing. However, the global financial turmoil and the economic downturn in developed economies in the second half of 2008 limited the Ukrainian banking system's access to foreign financing. In addition, political instability has eroded investors' confidence in the country's prospects, which contributed to the withdrawal of foreign capital from Ukraine. These factors, along with negative trends in the real economy, became the main drivers which undermined the period of growing stabilisation in the Ukrainian banking sector. Overall, the financial crisis revealed significant weaknesses in the Ukrainian banking system resulting in massive withdrawals of deposits and lending freezes, such that many Ukrainian banks face problems with liquidity.

In 2008-2009, the NBU, together with experts from international financial organisations, carried out a diagnostic review of all Ukrainian banks in order to identify banks that required additional capital. According to this review, 56 banks initially required additional capital in an aggregate amount of UAH 38.7 billion. The NBU required owners of such banks to increase their banks' share capital based on the results of the diagnostic review. Out of these 56 banks, as of 1 August 2010, 47 banks fully complied with requirements of the NBU with respect to increase of their regulatory capital (including one bank in which the State became a shareholder). As at 1 August 2010, temporary administration has been imposed in six of these banks and three further banks entered liquidation. All banks identified in the diagnostic review are subject to ongoing monitoring by the NBU.

In view of threats to solvency, between October 2008 and August 2010 the NBU imposed temporary administration and a moratorium on the satisfaction of claims of creditors in respect of 26 banks, including five banks that belonged to the group of the largest banks. In March 2009, the temporary administration was removed from one of the largest banks, Prominvestbank, which was acquired by Vnesheconombank. As of 1 August 2010, temporary administration remained in place in 4 banks, and liquidation procedures have been initiated in respect of 14 banks that had previously been subject to temporary administration.

The NBU has taken a number of administrative measures to address the instability in the Ukrainian banking sector, including measures aimed at preventing funds outflow, ensuring due liquidity levels and uninterrupted settlements as well as balancing foreign currency demand and supply. In particular, since late 2008, the NBU has adopted several resolutions widening the range of possible means to receive NBU liquidity support by Ukrainian banks, loosening restrictions on several economic ratios and subordinated debt and establishing certain exchange control restrictions. For instance, the purchase of foreign currency by banks for their own purposes is now limited to amounts within their open currency position and is allowed only at maturity of the relevant payment obligation in the same currency. In addition, the NBU took measures aimed at restricting the early withdrawal of deposits from the Ukrainian banking system, though such restrictions were further removed. See also *"The Monetary System – Exchange Rates"*.

Against the background of the significant withdrawal of funds from the banking system, especially of retail deposits, which has adversely affected the banking system, the NBU, as a lender of last resort, has continued to refinance affected banks to ensure that such banks have sufficient funding to perform their liabilities. The NBU has also approved regulations on credit support of Ukrainian banks in case of a real threat to the stability of their operations, which govern procedures for extension and prolongation of emergency loans to banks that have approved financial rehabilitation programmes. In 2009, the NBU also approved a number of regulations aimed at allowing Ukrainian banks to efficiently restructure problem loans in their loan portfolio or change the currency of such loans.

Further, the NBU has approved special procedures for financial rehabilitation of banks that provide for simplified procedures and reduced deadlines for the share capital increase registration. The NBU has also approved new regulations governing financial rehabilitation of a bank once a temporary administration has been imposed and regulations governing recapitalisation with participation of the State and other investors. In particular, a temporary administrator has been granted powers to carry out a reorganisation of a bank, reduce the share capital of a bank, determine new nominal value and approve share consolidation as well as additional share issuances. In addition, the NBU has introduced a "supervisor" position, being a new special control instrument for banks that are likely to experience problems. A main function of the supervisor

appointed by the NBU is to carry out a detailed evaluation of the bank's financial standing and prospects and to reveal risks inherent in its activities. In late 2009 and in 2010, the NBU approved a number of further regulations aimed at improvement of procedures for reorganisation and liquidation of troubled banks.

On 31 October 2008, Parliament passed the Law of Ukraine "On Immediate Measures to Avoid Negative Consequences of the Financial Crisis and Amendments to Certain Legislative Acts of Ukraine" which, together with the relevant regulation of the Cabinet of Ministers of Ukraine and resolutions of the NBU, establishes the regulatory framework for recapitalisation of Ukrainian banks by the Government through the purchase of shares of such banks. In particular, the Government has to own or control at least 75 per cent. plus one share of a bank's share capital as a result of recapitalisation (or at least 60 per cent. plus one share of a bank's share capital if the State participates in the recapitalisation together with a third-party investor).

The decision on recapitalisation of particular banks is made by the Cabinet of Ministers of Ukraine upon the NBU's proposal. The amount of internal State borrowings (through issuance of T-bills) planned for 2009 for the purpose of the banking system and Naftogas recapitalisation was approximately UAH 44.0 billion. The actual amount of State internal borrowings raised in 2009 (through issuance of T-bills) for the purpose of the banking system recapitalisation was UAH 19.6 billion. The amount of internal State borrowings (through issuance of T-bills) planned for 2010 for the purpose of the banking system recapitalisation is approximately UAH 30.0 billion. The actual amount of internal State borrowings raised (through issuance of T-bills) in the seven months ended 31 July 2010 for the purpose of the banking system recapitalisation (recapitalisation of Ukreximbank) was UAH 6.4 billion.

On 10 June 2009, the Cabinet of Ministers of Ukraine approved resolutions for the recapitalisation of three Ukrainian banks through the purchase of shares in the banks against contributions of T-bills by the Government. In July 2009, the Government contributed T-bills in the approximate principal amounts of UAH 3.1 billion to OJSB "UkrGasBank", UAH 3.6 billion to JSCB "Kyiv", and UAH 2.8 billion to JSC "Rodovid Bank". Further in 2009, the Government contributed additional T-bills in the aggregate principal amount of UAH 1.9 billion to OJSB "UkrGasBank" and UAH 5.6 billion to JSC "Rodovid Bank" (to ensure a repayment of retail deposits transferred from Ukrprombank (see below). The resulting government shareholdings in these banks are 87.7 per cent. in UkrGasBank and over 99 per cent. in each of the other two banks. The NBU is required to purchase, at par, T-bills contributed in exchange for shares in banks recapitalised using this method upon the banks' request. Through 31 July 2010, the NBU purchased T-bills in the aggregate amount of UAH 16.2 billion from the three banks named above.

The method chosen in 2009 by the Government and the NBU for Ukrprombank's recapitalisation was a transfer of retail deposits from Ukrprombank to JSC "Rodovid Bank", together with a certain share of its assets, and provided that the amount of the share capital of JSC "Rodovid Bank" was to be respectively increased. Further to this decision, the relevant parties approved a mechanism for the transfer of retail deposits and assets from Ukrprombank to JSC "Rodovid Bank" and a corresponding transfer agreement was signed. However, only liabilities of Ukrprombank were transferred to JSC "Rodovid Bank", while assets remained on the balance sheet of Ukrprombank. From 23 November 2009, JSC "Rodovid Bank" started repaying to Ukrprombank depositors those deposits which have become due and payable. On 21 January 2010, the NBU terminated banking licence of Ukrprombank and initiated its liquidation. In July 2010, part of the assets and liabilities of Ukrprombank were transferred to Delta Bank.

The Government is currently considering a strategy for further development of recapitalised banks and options for disposing of its shareholdings in such banks. The SPF has developed a proposed procedure for disposing of such State shareholdings in recapitalised banks. As at 1 September 2010, the SPF is seeking agreement to this procedure from the relevant ministries and agencies. Under the proposed procedure, the Government will decide as to disposition of such shareholdings upon the proposal of the Ministry of Finance and with prior approval of the sale plan by the SPF and the NBU. Under this procedure, the Government may sell the State's shareholding to other shareholders of the relevant bank or, if these shareholders are not interested in the purchase, to third party investors through an auction.

In April 2010, the NBU submitted for consideration of the Ministry of Finance a proposal with respect to recapitalisation of Nadra Bank with participation of the State. The Government contemplates that recapitalisation of Nadra Bank will be made with participation of private investor. It is proposed that the

Government will purchase shares in the bank against contributions of T-bills in the amount of approximately UAH 5.0 billion and private investor will purchase the shares in approximately the same amount, with the resulting Government's and investor's shareholdings in the bank to amount to 50 per cent. plus one share and 50 per cent. minus one share, respectively. Private investor will be also expected to transfer a portion of its shareholding into management of the Government to ensure that the Government would control 75 per cent. plus one share in the bank. It is intended that recapitalisation of Nadra Bank on the terms described above will be effected upon satisfaction by the bank of a number of conditions determined by the Expert and Analytical Council on Participation of the State in Banks' Recapitalisation in May 2010. Such conditions include restructuring of external debts of Nadra bank, as well as repayment by the bank of arrears to public sector. As at 30 August 2010, restructuring of external debts of Nadra bank has been completed, while restructuring of its debts to public sector will be completed once a respective settlement agreement between Nadra bank and the State Mortgage Institution is signed. Upon satisfaction by the bank of such conditions, the Government will be taking final decision with respect to its recapitalisation.

Following stress-testing carried out in 2010, the NBU has determined that 61 banks require additional capital in an aggregate amount of approximately UAH 41.0 billion. In particular, the NBU has determined amounts in which each of such 61 banks must increase its regulatory capital by 1 January 2011, including through an increase in the share capital and/or subordinated debt and/or taking measures aimed at minimisation of credit risks. Among banks identified as requiring an increase in regulatory capital are OJSB "UkrGasBank" and JSCB "Kyiv", which regulatory capital increase needs amount to approximately UAH 3.7 billion and UAH 3.0 billion, respectively.

In addition, the NBU will be considering whether proposals should be submitted to the Government with respect to recapitalisation of any other banks. Furthermore, the Government is currently developing a procedure for provision in 2010 of financing from the State Budget to financial institutions that are willing to participate in financial rehabilitation of troubled Ukrainian banks through purchase of assets and liabilities from such banks.

On 23 June 2009, Parliament passed a new law in an effort to address the negative consequences of the financial crisis in Ukraine, such law having been amended by Parliament on 22 October 2009 and 27 April 2010. The law contains, among other things, a number of provisions relating to Ukrainian banks and banking services. In particular, the law introduces a temporary (until 1 January 2011) prohibition on physical cash pay-outs on foreign currency loans and extension of foreign currency loans to individuals other than for certain limited purposes, and establishes new rules for the restructuring by banks of problem loans as well as a prohibition on enforcement against mortgaged residential real estate other than in specified circumstances.

In addition, in accordance with the changes introduced to the Law On Banks and Banking on 24 July 2009, the Government and the NBU are currently contemplating creation of a "bad bank", that is, a special rehabilitation bank to whose balance sheet troubled assets can be transferred from problem banks to protect the problem banks' depositors and other creditors. In 2009, the NBU developed a draft regulation on the procedures for the creation and operation of the "bad bank". Such regulation currently is being revised by the NBU in order to provide for, in addition to "bad bank" creation, a creation of an "intermediary" bank as an instrument to assist in the financial rehabilitation of problem banks.

A number of draft laws have been developed to improve regulation of the banking sector. One of such draft laws provides for significant extension of powers of the Fund and allows the Fund to perform the functions of temporary administrator and liquidator for Ukrainian banks. Another draft law is aimed at improvement of banking supervision and establishes a mechanism for identifying the real owners and persons controlling Ukrainian banks. Other draft laws provide for, among other things, introduction of banking supervision on consolidated basis and implementation of a number of measures to ensure better protection of rights of creditors. As at 30 September 2010, only some of these draft laws have been submitted for consideration by Parliament.

Furthermore, the Economic Reform Programme (see "*Economy of Ukraine – Action Programmes*") provides for implementation in 2010-2014 of the following main measures aimed at increasing the role of the financial sector in the development of the Ukrainian economy:

- at the first stage that should be completed by the end of 2010, Ukraine should, among other things, enhance independence and transparency of the NBU; ensure an additional capitalisation of banks depending on the audit of their credit portfolios; facilitate banks' restructuring of problem assets; recapitalise, reorganise or liquidate banks that became insolvent during the 2008-2009 financial and economic downturn; improve the system for guaranteeing of retail deposits; and tighten disclosure requirements and liability for misuse of insider information at the securities market;
- at the second stage that should be completed by the end of 2012, Ukraine should continue further capitalisation of banks and facilitation of the consolidation in the financial sector; improve prudential supervision over financial institutions (including introduction of supervision on the consolidated basis); complete a transition to the preparation of financial statements by all financial institutions in accordance with the IFRS; privatise banks, which became state-owned following their recapitalisation with participation of the State in 2009; and develop regulatory framework for transactions with derivatives; and
- at the third stage that should be completed by the end of 2014, Ukraine should introduce new market instruments for accumulation and re-allocation of long-term financial resources, including measures to be taken within the framework of introduction of the defined contribution system of state pension insurance.

The Securities Markets in Ukraine

In 2010, exchange-based trading of corporate and municipal securities in Ukraine is currently concentrated on two main exchanges, although the country has 10 stock exchanges in total. The two main exchanges are the First Securities Trading System Stock Exchange with 178 member companies and the Ukrainian Stock Exchange with 156 member companies as at 30 June 2010, respectively.

The cumulative aggregate volume of securities issuances registered by the State Securities and Stock Market Commission of Ukraine increased by UAH 162.7 billion, or 28.2 per cent., during 2009 to UAH 740.1 billion as of 31 December 2009. The cumulative aggregate volume of securities issuances registered by the State Securities and Stock Market Commission of Ukraine further increased by UAH 41.3 billion (as compared to a UAH 73.6 billion increase during the six months ended 30 June 2009), or 5.6 per cent., during the six months ended 30 June 2010 to UAH 781.4 billion as of 30 June 2010.

In 2009, the total trading volume on all organised and over-the-counter securities markets in Ukraine was UAH 1,067.3 billion (UAH 883.4 billion in 2008). Against the background of global financial downturn, trading volume on organised securities markets in 2009 amounted to UAH 36.0 billion as compared to UAH 37.8 billion in 2008. Trading volume on organised securities markets in the six months ended 30 June 2010 amounted to UAH 46.9 billion as compared to UAH 9.6 billion in the six months ended 30 June 2009.

The State Securities and Stock Market Commission of Ukraine, which was established in 1995, has responsibility for regulating the primary and secondary markets, the licensing and regulation of securities traders, registrars and joint investment institutions, as well as stock exchanges and securities custodians and depositaries. As of 30 June 2010, there were 1,812 professional participants in the securities markets, including 741 brokers, three depositaries conducting both depositary and clearing activities, 342 custodians, 355 registrars, 358 asset management companies and 10 stock exchanges.

All companies with more than 150 shareholders are required to have an independent registrar. Entities involved in trading securities are not permitted to manage institutional investors' assets but may engage in custodial and registrar business.

According to the Main Directions of Development of Securities Market of Ukraine for 2006-2010, as approved in March 2006, priorities for stock market development include improving protection of investors' rights; developing new stock market instruments; developing investment infrastructure; introducing prudential supervision over activities of professional securities market participants; increasing the proportion of securities sales on organised stock exchanges and trade information systems; and improving the National Depository System. The priorities for stock market development determined by the State Securities and

Stock Market Commission of Ukraine for 2010 include the creation of strong domestic institutional investors in the stock market, and reform of depositary system.

Throughout 2006 and 2007, the State Securities and Stock Market Commission of Ukraine enacted a number of regulations, including new licence requirements for professional participants in the securities market, new regulations governing procedures for disclosure of information by issuers, new regulations on depositary, registrar and clearing activities, and new regulations governing share, corporate bond and mortgage bond issuances, some of which have been amended during 2008. In addition, in December 2007, the State Securities and Stock Market Commission of Ukraine enacted new regulations on the capital adequacy and investment ratios of security traders. Such regulations are designed to limit the risks arising out of their professional activities and have become effective from 1 November 2008.

In June 2008, a number of changes were introduced to the license requirements for professional participants in the securities markets. Among these changes was the requirement that a participant maintain its own equity capital in an amount not less than the amount of its registered statutory capital.

On 30 April 2009, a law “On Joint Stock Companies” became effective, providing for a two-year transitional period for existing joint stock companies to change their form into that of a public or private joint stock company. The new law is aimed at eliminating gaps in various laws and regulations of Ukraine relating to joint stock companies, including, among other things, corporate governance matters, pre-emptive share purchase rights, mandatory buy-outs, and shareholders’ rights protection, especially for minority shareholders. In addition, the law requires public joint stock companies to be listed on at least one stock exchange. Such requirement is expected to contribute to the development of the organised securities market in Ukraine by increasing its size and improving liquidity.

The global financial and economic downturn in 2008 and 2009 adversely affected the Ukrainian securities market, including aggregate market capitalisation and the structure of assets of professional securities market participants, especially joint investment institutions. In order to address the challenges posed by the global financial crisis and to minimise its adverse effects on the domestic stock market, Parliament introduced changes to the Law of Ukraine “On Joint Investment Institutions (Mutual and Corporate Investment Funds)” effective as of 13 February 2009. These amendments, among other things, allow joint investment institutions to diversify their assets and provide for a wider range of stock market instruments, which can be employed by market participants for investment. In addition, in January 2009, more stringent liability rules for securities market participants were introduced, in particular with regard to insider trading and price manipulation.

Further, in early 2010, a number of changes were introduced to the licensing rules for professional participants in the securities markets. These changes are aimed at establishing increased requirements for such participants, including brokers, custodians, registrars and stock exchanges, to ensure better protection for their clients. Among other things, these changes require stock exchanges that are engaged in settlement of derivative transactions, to maintain, unless relevant transactions are fully secured, a reserve fund in order to reduce non-performance risks. These changes also tighten prior record requirements for directors of professional stock market participants.

In addition, a law providing for more stringent requirements for professional stock market participants became effective on 27 July 2010. In particular, minimum statutory capital requirements for depositaries and minimum own capital requirements for clearing depositaries were established at UAH 15.0 million and UAH 25.0 million, respectively.

The Financial Services Markets in Ukraine

The State Commission for Regulation of Financial Services Markets of Ukraine, which was established in 2003, has responsibility for regulating and supervising the non-bank financial sector. The non-bank financial sector of Ukraine includes insurance companies, insurance and reinsurance brokers, credit unions and other non-bank credit institutions, state entities providing financial services, non-state pension funds and their administrators, pawnshops, financial companies (rendering such services as financial leasing, factoring,

provision of sureties and guarantees) and legal entities that do not have the status of financial institution but are permitted to render specific kinds of financial services.

The following table sets forth information concerning numbers of non-bank financial institutions as at the end of the periods indicated:

	31 December		As at 30 June	
	2007	2008	2009	2010
Credit unions	800	829	755	700
Insurance companies	446	469	450	441
Pawnshops	309	314	373	400
Legal entities which do not have the status of financial institution but are permitted to render specific kinds of financial services				
(financial leasing)	171	208	216	192
Insurance and reinsurance brokers	69	61	61	60
Financial companies	171	193	208	210
Administrators of non-state pension funds	50	51	44	43
Non-state pension funds	96	109	108	107
State entities providing financial services.....	27	29	29	29
Other non-bank credit institutions.....	8	20	32	37

In 2009, the growth in the assets of insurance companies and non-state pension funds decelerated, and the assets of credit unions reduced, as compared to 2008, as a result of the financial and economic downturn in Ukraine and globally, political instability, limited access of the market participants to the borrowed funds, decline in companies' solvency and suspension of investment projects. In particular, in 2009, the assets of insurance companies increased by 0.1 per cent. (as compared to an increase of 30.2 per cent. in 2008) to UAH 42.0 billion, the assets of credit unions decreased by 30.5 per cent. (as compared to an increase of 15.2 per cent. in 2008) to UAH 4.2 billion and the assets of non-state pension funds increased by 40.1 per cent. (as compared to an increase of 117.9 per cent. in 2008) to UAH 857.9 million, respectively. The decline of the assets of credit unions in 2009 was largely attributable to the freeze on new lending in late 2008 and 2009 as well as to a withdrawal of deposits by credit union members and an increase in bad loans in this period. The significant deceleration in the growth rate of the assets of non-state pension funds in 2009 was principally due to the increase in the amount of pension disbursements, as well as to a suspension or significant reduction of pension contributions by certain legal entities and individuals as a result of the financial and economic downturn.

In the six months ended 30 June 2010, the assets of insurance companies increased by 2.8 per cent. (as compared to an increase of 0.2 per cent. in the corresponding period of 2009), while the assets of financial companies increased by 3.5 per cent. (as compared to an increase of 18.8 per cent. in the corresponding period of 2009). The assets of credit unions declined by 29.3 per cent. in the six months ended 30 June 2010, as compared to a decrease by 23.8 per cent. in the corresponding period of 2009, whereas the assets of non-state pension funds increased in the six months ended 30 June 2010 by 14.8 per cent. as compared to an increase by 19.9 per cent. in the corresponding period of 2009. The decline of the assets of credit unions in the six months ended 30 June 2010 was largely attributable to the reduced volumes of new lending as well as to a withdrawal of deposits by credit union members and an increase in bad loans in this period. The growth in the assets of non-state pension funds in the six months ended 30 June 2010 was principally due to the increase in the amount of pension contributions and an increase in profits from investments made by the non-state pension funds.

The following table sets forth information concerning main indicators of activities of non-bank financial institutions as at the end of the periods indicated:

	31 December		30 June	
	2007	2008	2009	2010
Insurance				
Number of executed insurance agreements (thousands)	559,767	675,498	574,972	282,926
Total assets (UAH million)	32,213	41,931	41,970	43,166
Insurance reserves (UAH million)	8,423	10,904	10,141	9,394
Gross insurance premiums (UAH million)	18,008	24,009	20,442	9,636
Gross insurance payments (UAH million)	4,213	7,051	6,737	2,619
Financial companies				
Total assets (UAH million)	3,274	6,012	7,579	7,848
Volume of rendered services (UAH million)	20,898	19,610	21,834	13,069
Credit unions				
Number of members (thousand person)	2,392	2,669	2,190	1,521
Total assets (UAH million)	5,261	6,065	4,218	2,984
Volume of extended loans to members (UAH million) ..	4,512	5,573	3,909	2,743
Volume of raised deposits of members (UAH million) ..	3,451	3,951	2,959	1,662
Pawnshops				
Total assets (UAH million)	368	525	619	787
Volume of loans extended during the period (UAH million)	1,404	2,127	3,505	1,292
Non-state pension funds				
Number of participants under executed pension contracts (thousand person)	279	483	497	500
Total assets (UAH million)	281	612	858	985
Pension contributions (UAH million)	234	583	755	840
Pension disbursements (UAH million)	9	27	90	127

The Government expects the Ukrainian non-bank financial sector, and in particular the insurance sector, to become more competitive as a result of Ukraine's accession to the WTO. Pursuant to the changes to the Law of Ukraine "On Insurance" enacted for the purpose of harmonising Ukrainian legislation with WTO requirements, foreign insurers will be permitted to operate branch offices in Ukraine, and certain limitations on insurance intermediary activities will be eliminated, from 16 May 2013, i.e., upon expiry of five years following Ukraine's accession to the WTO. In addition, starting from 16 May 2008, foreign insurers are permitted, subject to certain access criteria established by the Law "On Insurance", to perform re-insurance activities in any area as well as insurance activities in a limited number of areas, such as insurance of certain risks related to marine transportation, commercial aviation, missile launching and freight (including satellites). However, before a general permission for a foreign insurer to perform any activities in Ukraine is granted, several pre-requisites need to be satisfied, including execution of an agreement between the State Commission for the Regulation of Financial Services Markets of Ukraine and an insurance supervisory authority of the foreign state where the relevant insurer is head-quartered concerning information exchange as well as the existence of a double taxation treaty between Ukraine and the foreign state where the relevant insurer is head-quartered.

During 2007-2009, the State Commission for Regulation of Financial Services Markets of Ukraine enacted a number of regulations aimed at improvement of the regulatory framework for financial services markets. These regulations include rules that govern the activities of non-state pension funds and non-state pension fund administrators and the functioning of self-regulated organisations of such administrators, establish a licensing framework for activities of construction financing and real estate funds, set out detailed requirements for insurance reserves as well as amend regulatory requirements for insurance companies, credit unions and pawnshops.

Furthermore, during 2007-2009, the State Commission for Regulation of Financial Services Markets of Ukraine has developed a number of laws, including a law aimed at improving protection of individual

investors preventing financial abuses in the residential real estate construction, which came into effect on 23 July 2010. Another draft law developed by the State Commission for Regulation of Financial Services Markets of Ukraine in 2008 and aimed at comprehensive regulation of the establishment and activities of pawnshops as well as at protecting the rights of pawnshop clients was approved by Parliament in the first reading in May 2009. As at 30 September 2010, this draft law remained to be approved by Parliament in the second reading, signed by the President and officially promulgated to become effective.

The priorities of the State Commission for Regulation of Financial Services Markets of Ukraine for 2010 include: ensuring transparency and openness of financial services markets and protection of interests of financial services consumers; introduction of prudential supervision over non-banking financial institutions and transition to supervision based on risk evaluation; improvement of temporary administration, stabilisation and financial rehabilitation mechanisms in non-banking financial institutions; introduction of a system for guaranteeing the deposits of credit union members and insurance payments under life insurance agreements; introduction of capital adequacy, asset diversification and asset quality ratios limiting the risks of insurers' operations with financial assets; and taking measures for the transition to the preparation of financial statements in accordance with IFRS.

To achieve these aims, in the second half of 2009 and in the first half of 2010, the State Commission for Regulation of Financial Services Markets of Ukraine developed a number of additional draft laws, including a revised draft law "On Insurance" and a draft law on disclosure of information by financial institutions, including information in respect of beneficial owners, and improvement of corporate governance system.

The Ukrainian non-bank financial sector has been adversely affected by the global financial crisis largely due to a decline in the quality of banking assets, significant devaluation of the hryvnia and negative changes in the structure of Ukraine's balance of payments and exports as well as a decline in foreign borrowings. These factors have resulted in 2009 in reductions in the value of assets of the respective financial market participants. Other factors that had a negative impact on the Ukrainian non-bank financial sector in 2009 include a freeze on deposits held by financial market participants with problem banks and a decline in market value of financial instruments, especially those which were held by insurance companies and non-state pension funds, that adversely affected the profitability of these entities and the levels of reserves they maintain to cover future payments to customers.

The State Commission for Regulation of Financial Services Markets of Ukraine expects that in 2010, the non-bank financial sector will generally continue to be affected by global financial crisis. The main factors that may be adversely affect the non-bank financial sector in 2010 are expected to include outflows of investments from Ukrainian stock market; limited access to external and internal borrowings; a general reduction of confidence in financial institutions; increased risks connected with asset investments; a lack of stability in foreign exchange market; negative inflation expectations among population; and a decrease in assets of non-bank financial institutions due to their revaluation in light of increased foreign exchange, credit and other risks. It is expected that in 2010 the insurance market may face difficulties with retaining new clients and business expansion due to, among other things, expected continued declines in consumer lending and residential construction. Credit unions may be experiencing an increase in the number of non-performing loans, including as a result of borrowers' reduced solvency. The non-state pension insurance sector may also be adversely affected in 2010 due to a lack of low-risk investments and a reduction of non-state pension programs by Ukrainian companies. At the same time, the State Commission for Regulation of Financial Services Markets of Ukraine expects that the non-bank financial sector will gradually stabilise towards the end of 2010.

TAXATION

The following is a general description of certain tax considerations relating to the Notes. It does not purport to be a complete analysis of all tax considerations relating to the Notes. Prospective purchasers of Notes should consult their own tax advisers as to the consequences under the tax laws of the country of which they are resident for tax purposes and the tax laws of Ukraine of acquiring, holding and disposing of Notes and receiving payments of interest, principal and/or other amounts under the Notes. This summary is based upon the law as in effect on the date of this Prospectus and is subject to any change in law that may take effect after such date.

Also investors should note that the appointment by an investor in Notes, or any person through which an investor holds Notes, of a custodian, collection agent or similar person in relation to such Notes in any jurisdiction may have tax implications. Investors should consult their own tax advisers in relation to the tax consequences for them of any such appointment.

UKRAINE

Tax Implications for Non-Residents of Ukraine

Tax on Interest Payments

The Law of Ukraine “On Taxation of Profits of Enterprises”, dated 28 December 1994 (the “Profits Tax Law”) stipulates that the income of entities that are non-tax residents of Ukraine, which is derived from sources in Ukraine in the form of interest payments, is subject to a 15 per cent. withholding tax. At the same time, paragraph 13.2 of Article 13 of the Profits Tax Law provides that the withholding tax rate may be reduced or interest income exempted from taxation by the provisions of an applicable treaty on the avoidance of double taxation. This means that if the Noteholder is a tax resident of a state which has an effective treaty on the avoidance of double taxation with Ukraine (the “Double Tax Treaty”), then provided that certain conditions (as may be stipulated by the Double Tax Treaty and by applicable Ukrainian law) are duly satisfied, the interest payable under the Notes may be exempt from withholding tax in Ukraine or the rate of withholding tax may be reduced.

Applicable Ukrainian legislation allows upfront relief under the Double Tax Treaty if current confirmation of the recipient’s tax residency in the respective state in accordance with the requirements of the Ukrainian law is available. In order to be current, a confirmation of the recipient’s tax residency must be obtained for each tax year. Obtaining this upfront relief does not require the payee or payor to apply for and/or obtain any transaction specific clearance from the Ukrainian tax authorities. Instead, the Ukrainian payor directly applies the rate or exemption under the Double Tax Treaty, provided that the current confirmation of the recipient’s tax residency is available on or prior to the date of payment of the Ukrainian source income.

The reduced tax rate or exemption shall not apply if the non-resident entity, Noteholder, carries on business in Ukraine through a permanent establishment situated therein and interest on the Notes derived by such non-resident is attributable to its permanent establishment in Ukraine. In such a case, interest shall generally be subject to taxation in Ukraine on a net basis by self-assessment at the rate of 25 per cent.

Tax on the Issue of the Notes

No registration tax, stamp duty, state duty, documentary tax or other similar tax is payable in Ukraine in connection with the issuance of the Notes because the Notes will be issued outside Ukraine.

Tax on Redemption of the Notes

The amount received by a non-resident on redemption of the Notes should not be subject to taxation in Ukraine to the extent that the redemption price at maturity does not exceed the original issue price. Although there are no precedents in the past and Ukrainian legislation does not provide clear guidance, Ukrainian tax authorities may seek to impose tax on the amount by which the redemption value of the Notes exceeds the

purchase price paid for the Notes acquired by the holder on a secondary securities market (subject to provisions of any applicable Double Tax Treaty).

Gross-Up Obligations

If payments under the Notes are subject to any withholding tax (as a result of which the Issuer would reduce payments under the Notes in line with such withholding), then, subject to certain exceptions set out in Condition 7 of the Terms and Conditions of the Notes, the Issuer would be obliged to pay such additional amounts as may be necessary so that the net payments received by the Noteholders will not be less than the amount they would have received in the absence of such withholding.

Notwithstanding the foregoing, the Profits Tax Law generally prohibits contractual provisions requiring a resident entity paying income from sources in Ukraine to a non-resident entity to pay Ukraine's income tax for such non-resident. The letter of the State Tax Administration of Ukraine No. 14086/5/22-5016 dated 18 November 2009 (the "**Restrictive Letter**") states that payment of any additional amount to a non-resident of Ukraine to compensate tax deducted amounts contradicts the Law of Ukraine "On Taxation of Company Income". However, by a further letter of the State Tax Administration of Ukraine No. 13039/5/15-0516 dated 13 October 2010 ("**Notes Specific Clarification**"), which was provided specifically in the context of the Notes, the State Tax Administration of Ukraine has clarified that the provisions of the Restrictive Letter shall not be applicable to external borrowings (agreements on placement of notes outside of Ukraine) made by state enterprises by means of issuance of notes secured by state guarantees if repayment of principal and interest payments thereunder are made out of the State Budget funds. Although it is expected that repayment of principal and interest payments under the Notes will generally be made out of the State Budget funds, it may not be excluded that such payments could also be made out of the funds generated by NSC Olympic, Lviv Directorate or other operating companies or otherwise out of the funds which are not the State Budget funds. Therefore, should the position of the Tax Administration of Ukraine pursuant to the Restrictive Letter be supported, or should tax gross-up obligations be otherwise interpreted as prohibited under Ukrainian law in any proceedings before Ukrainian courts, the Issuer's gross-up obligations would be voidable and unenforceable under Ukrainian law.

In addition, pursuant to the draft Tax Code of Ukraine, which was approved by Verkhovna Rada of Ukraine in the first reading on 7 October 2010, profits of non-residents obtained in the form of interest or discount under the state bonds or debt securities secured by state guarantees, which are sold (placed) to non-residents outside of Ukraine through authorised non-resident agents, shall not be subject to taxation in Ukraine. The draft Tax Code remains to be approved by Parliament in a second, and, as the case may be, third reading, signed by the President and officially promulgated to become effective. If adopted in their current form, the relevant provisions of the Tax Code of Ukraine would also apply to the Notes.

Transfer of Notes to Resident Investors

Although there are no precedents in the past and Ukrainian legislation does not provide clear guidance, Ukrainian tax authorities may treat the gains derived from the sale of the Notes as income from a source in Ukraine and impose a 15 per cent. tax, if the respective gain is received by an entity, or a 30 per cent personal income tax if the respective gain is received by an individual, unless there is an exemption under an applicable double tax treaty. Resident entities (buyers of the Notes) may be obliged to collect withholding tax from payments to non-resident sellers of the Notes in respect of any gain derived from a sale of the Notes to such resident buyers unless an exemption is available under an applicable Double Tax Treaty.

If the non-resident entity (seller of the Notes) carries on business in Ukraine through a permanent establishment situated therein, and the gain derived on the sale of the Notes is attributable to such permanent establishment, the gain shall be subject to taxation in Ukraine on a net basis by self-assessment at the rate of 25 per cent.

Tax Implications for Residents of Ukraine

A holder of a Note who is an individual or entity resident in Ukraine for tax purposes is subject to applicable Ukrainian taxes. Income of a non-resident entity attributable to its permanent establishment situated in

Ukraine is subject to taxation in Ukraine on a net basis by self-assessment at the rate of 25 per cent. Interest received by a resident entity from holding debt securities is subject to taxation in Ukraine on a net basis by self-assessment at the rate of 25 per cent. The principal amount of the Notes received by a resident entity at redemption of the Notes is generally not treated as taxable income to the extent such amount does not exceed the original issue price, or, as the case may be, the purchase price of the Notes acquired by the resident entity on a secondary security market. Gains realised by a resident entity on the sale of the Notes are subject to taxation in Ukraine on a net basis by self-assessment at the rate of 25 per cent.

The resident entities (Noteholder) must accrue taxable income or deductible expenses (for corporate profit tax purposes) as a result of calculating foreign exchange differences (gains or losses) in respect of the Notes according to the official exchange rate of the National Bank of Ukraine. The same applies to the permanent establishments situated in the Ukraine of non-resident entities with respect to foreign exchange gains or losses arising from the revaluation of indebtedness under the Notes in a foreign currency attributable to such permanent establishment.

Interest on the Notes received by a resident individual shall be subject to personal income tax in Ukraine at the rate of 15 per cent. The principal amount of the Notes received by a resident individual at redemption of the Notes shall not be treated as income of that resident individual to the extent that such amount does not exceed the original issue price, or, as the case may be, the purchase price of the Notes acquired by the resident individual on a secondary security market. Gains derived by resident individuals from the sale of Notes are subject to 15 per cent. personal income tax in Ukraine.

EU SAVINGS DIRECTIVE

Under EC Council Directive 2003/48/EC on the taxation of savings income, each Member State is required, from 1 July 2005, to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in that other Member State; however, for a transitional period, Austria, Belgium and Luxembourg may instead apply a withholding system in relation to such payments, deducting tax at rates rising over time to 35 per cent. The transitional period is to terminate at the end of the first full fiscal year following agreement by certain non EU countries to the exchange of information relating to such payments. Belgium has replaced this withholding tax with a regime of exchange of information to the Member State of residence as from 1 January 2010.

Also with effect from 1 July 2005, a number of non EU countries, and certain dependent or associated territories of certain Member States, have agreed to adopt similar measures (either provision of information or transitional withholding) in relation to payments made by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in a Member State. In addition, the Member States have entered into reciprocal provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to, or collected by such a person for, an individual resident or certain limited types of entity established in one of those territories.

On 13 November 2008, the European Commission published a proposal for amendments to the Directive, which included a number of suggested changes which, if implemented, would broaden the scope of the requirements described above. The European Parliament approved an amended version of this proposal on 24 April 2009. Investors who are in any doubt as to their position should consult their professional advisers.

UNITED STATES FEDERAL INCOME TAX

TO ENSURE COMPLIANCE WITH TREASURY DEPARTMENT CIRCULAR 230, HOLDERS ARE HEREBY NOTIFIED THAT: (A) ANY DISCUSSION OF FEDERAL TAX ISSUES IN THIS PROSPECTUS IS NOT INTENDED OR WRITTEN TO BE RELIED UPON, AND CANNOT BE RELIED UPON, BY HOLDERS FOR THE PURPOSE OF AVOIDING PENALTIES THAT MAY BE IMPOSED ON HOLDERS UNDER THE INTERNAL REVENUE CODE; (B) SUCH DISCUSSION IS INCLUDED HEREIN BY THE ISSUER IN CONNECTION WITH THE PROMOTION OR MARKETING (WITHIN THE MEANING OF CIRCULAR 230) BY THE ISSUER OF THE TRANSACTIONS OR MATTERS

ADDRESSED HEREIN; AND (C) HOLDERS SHOULD SEEK ADVICE BASED ON THEIR PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISER.

The following is a summary of certain material U.S. federal income tax consequences of the acquisition, ownership and disposition of Notes by a U.S. Holder (as defined below). This summary deals only with initial purchasers of Notes at the Issue Price (as defined below) that are U.S. Holders and that will hold the Notes as capital assets. The discussion does not cover all aspects of U.S. federal income taxation that may be relevant to, or the actual tax effect that any of the matters described herein will have on, the acquisition, ownership or disposition of Notes by particular investors, and does not address state, local, foreign or other tax laws. This summary also does not discuss all of the tax considerations that may be relevant to certain types of investors subject to special treatment under the U.S. federal income tax laws (such as financial institutions, insurance companies, investors liable for the alternative minimum tax, individual retirement accounts and other tax-deferred accounts, tax-exempt organisations, dealers in securities or currencies, investors that will hold the Notes as part of straddles, hedging transactions or conversion transactions for U.S. federal income tax purposes or investors whose functional currency is not the U.S. dollar).

As used herein, the term “U.S. Holder” means a beneficial owner of Notes that is, for U.S. federal income tax purposes, (i) an individual citizen or resident of the United States, (ii) a corporation created or organised under the laws of the United States or any State thereof, (iii) an estate the income of which is subject to U.S. federal income tax without regard to its source or (iv) a trust if a court within the United States is able to exercise primary supervision over the administration of the trust and one or more U.S. persons have the authority to control all substantial decisions of the trust, or the trust has elected to be treated as a domestic trust for U.S. federal income tax purposes.

The U.S. federal income tax treatment of a partner in a partnership that holds Notes will depend on the status of the partner and the activities of the partnership. Prospective purchasers that are partnerships should consult their tax advisers concerning the U.S. federal income tax consequences to their partners of the acquisition, ownership and disposition of Notes by the partnership.

The summary is based on the tax laws of the United States, including the Internal Revenue Code of 1986, as amended, its legislative history, existing and proposed regulations thereunder, published rulings and court decisions, all as of the date hereof and all subject to change at any time, possibly with retroactive effect.

THE SUMMARY OF U.S. FEDERAL INCOME TAX CONSEQUENCES SET OUT BELOW IS FOR GENERAL INFORMATION ONLY. ALL PROSPECTIVE PURCHASERS SHOULD CONSULT THEIR TAX ADVISERS AS TO THE PARTICULAR TAX CONSEQUENCES TO THEM OF OWNING THE NOTES, INCLUDING THE APPLICABILITY AND EFFECT OF STATE, LOCAL, FOREIGN AND OTHER TAX LAWS AND POSSIBLE CHANGES IN TAX LAW.

Payments of Stated Interest

General

Stated interest on a Note will be taxable to a U.S. Holder as ordinary income at the time it is received or accrued, depending on the holder’s method of accounting for tax purposes. Stated interest paid by the Issuer on the Notes constitutes income from sources outside the United States. Prospective purchasers should consult their tax advisers concerning the applicability of the foreign tax credit and source of income rules to income attributable to the Notes.

Original Issue Discount

General

If the Issue Price of a Note is less than its principal amount by more than a de minimis amount, U.S. Holders will be subject to special U.S. federal income tax rules with respect to this “original issue discount” (“OID”). OID will be considered to be de minimis if it is less than 0.25 per cent. of the principal amount multiplied by the number of complete years to maturity. A U.S. Holder must include a portion of the OID in gross income as interest in each taxable year or portion thereof in which the U.S. Holder holds the Notes even if

the U.S. Holder has not received a cash payment in respect of the OID. OID, if any, accrued with respect to the Notes constitutes income from sources outside the United States.

Generally, the Issue Price of a Note will be the first price at which a substantial amount of Notes included in the issue of which the Note is a part is sold to persons other than bond houses, brokers, or similar persons or organisations acting in the capacity of underwriters, placement agents, or wholesalers (the “**Issue Price**”).

U.S. Holders of Notes must include OID in income calculated on a constant-yield method before the receipt of cash attributable to the income, and generally will have to include in income increasingly greater amounts of OID over the life of the Notes. The amount of OID includible in income by a U.S. Holder of a Note is the sum of the daily portions of OID with respect to the Note for each day during the taxable year or portion of the taxable year on which the U.S. Holder holds the Note (“**accrued OID**”). The daily portion is determined by allocating to each day in any “accrual period” a pro rata portion of the OID allocable to that accrual period. Accrual periods with respect to a Note may be of any length selected by the U.S. Holder and may vary in length over the term of the Note as long as (i) no accrual period is longer than one year; and (ii) each scheduled payment of interest or principal on the Note occurs on either the final or first day of an accrual period. The amount of OID allocable to an accrual period equals the excess of (a) the product of the Note’s adjusted issue price at the beginning of the accrual period and the Note’s yield to maturity (determined on the basis of compounding at the close of each accrual period and properly adjusted for the length of the accrual period) over (b) the sum of the payments of interest on the Note allocable to the accrual period. The “adjusted issue price” of a Note at the beginning of any accrual period is the Issue Price of the Note increased by (x) the amount of accrued OID for each prior accrual period and decreased by (y) the amount of payments previously made on the Note that were not interest payments.

Election to Treat All Interest as Original Issue Discount

A U.S. Holder may elect to include in gross income all interest that accrues on a Note and OID, if any, using the constant-yield method described above under “Original Issue Discount—General”, with certain modifications. This election generally applies only to the Note with respect to which it is made and may not be revoked without the consent of the IRS. U.S. Holders should consult their tax advisers concerning the propriety and consequences of this election.

Fungible Issue

The Issuer may, without the consent of the Holders of outstanding Notes, issue additional Notes with identical terms. These additional Notes, even if they are treated for non-tax purposes as part of the same series as the original Notes, in some cases may be treated as a separate series for U.S. federal income tax purposes. In such a case, the additional Notes may be considered to have been issued with OID even if the original Notes had no OID, or the additional Notes may have a greater amount of OID than the original Notes. These differences may affect the market value of the original Notes if the additional Notes are not otherwise distinguishable from the original Notes.

Treatment of Premium

If a U.S. Holder purchases a Note for an amount greater than its principal amount, such U.S. Holder will be considered to have purchased the Note at a premium. A U.S. Holder generally may elect to amortise this premium over the term of the Note. If a U.S. Holder makes this election, the amount of interest income such U.S. Holder must report for U.S. federal income tax purposes with respect to any interest payment date will be reduced by the amount of premium allocated to the period from the previous interest payment date to that interest payment date. The amount of premium allocated to any such period is calculated by taking the difference between (i) the stated interest payable on the interest payment date on which that period ends and (ii) the product of (a) the Note’s overall yield to maturity and (b) your purchase price for the Note (reduced by amounts of premium allocated to previous periods). If a U.S. Holder makes the election to amortise premium, such U.S. Holder must apply it to the Note and to all debt instruments acquired at a premium that the U.S. Holder holds at the beginning of the taxable year in which the election is made and all debt

instruments subsequently purchased at a premium, unless the U.S. Holder obtains the consent of the IRS to a change.

If a U.S. Holder does not make the election to amortise premium on a Note and such U.S. Holder holds the Note to maturity, the U.S. Holder will have a capital loss for U.S. federal income tax purposes, equal to the amount of the premium, when the Note matures. If a U.S. Holder does not make the election to amortise premium and sells or otherwise disposes of the Note before maturity, the premium will be included in the U.S. Holder's tax basis in the Note as defined below, and therefore will decrease the gain, or increase the loss, that the U.S. Holder otherwise would realize on the sale or other disposition of the Note.

Sale and Retirement of the Notes

A U.S. Holder will generally recognise gain or loss on the sale or retirement of a Note equal to the difference between the amount realised on the sale or retirement and the tax basis of the Note. A U.S. Holder's tax basis in a Note will generally be its cost increased by the amount of any OID included in the U.S. Holder's income, and decreased (but not below zero) by any amortised premium (as described above) with respect to the Note. The amount realised does not include the amount attributable to accrued but unpaid interest, which will be taxable as interest income to the extent not previously included in income. Gain or loss recognised by a U.S. Holder on the sale or retirement of a Note will be capital gain or loss and will be long-term capital gain or loss if the Note was held by the U.S. Holder for more than one year. Gain or loss realised by a U.S. Holder on the sale or retirement of a Note generally will be U.S. source.

Backup Withholding and Information Reporting

Payments of principal and, interest on, and accrued OID (if any) on, and the proceeds of sale or other disposition of Notes by a U.S. paying agent or other U.S. intermediary will be reported to the IRS and to the U.S. Holder as may be required under applicable regulations. Backup withholding may apply to these payments if the U.S. Holder fails to provide an accurate taxpayer identification number or certification of exempt status or fails to report all interest and dividends required to be shown on its U.S. federal income tax returns. Certain U.S. Holders are not subject to backup withholding. U.S. Holders should consult their tax advisers as to their qualification for exemption from backup withholding and the procedure for obtaining an exemption.

New Legislation

Recently enacted legislation imposes new reporting requirements on the holding of certain foreign financial assets, including debt of foreign issuers, if the aggregate value of all of these assets exceeds \$50,000. The Notes are expected to constitute foreign financial assets subject to these requirements unless the Notes are held in an account at a domestic financial institution. U.S. Holders should consult their tax advisors regarding the application of this legislation.

FORM OF NOTES AND TRANSFER RESTRICTIONS

The following information relates to the form, transfer and delivery of the Notes. Because of the restrictions set out below, purchasers of Notes offered in the United States in reliance on Rule 144A are advised to consult appropriately qualified legal counsel prior to making any offer, resale, pledge or transfer of Notes. Capitalised terms used but not defined herein have the meanings provided in the section entitled “Terms and Conditions of the Notes”.

1. Form of Notes

All Notes will be in registered form, without interest coupons attached. Notes offered and sold outside the United States in reliance on Regulation S will be represented by interests in an Unrestricted Global Note, in registered form, without interest coupons attached, which will be deposited on or about the Closing Date with The Bank of New York Mellon as common depositary in respect of interests held through Euroclear and Clearstream, Luxembourg.

Notes offered and sold in reliance on Rule 144A will be represented by interests in a Restricted Global Note in registered form without interest coupons attached, which will be deposited on or about the Closing Date with the Custodian for, and registered in the name of Cede & Co. as nominee for, DTC. Each Restricted Global Note (and any Note Certificates issued in exchange therefor) will be subject to certain restrictions on transfer contained in a legend appearing on the face of such Note as set forth under “*Transfer Restrictions*” below.

Each of the Unrestricted Global Note and the Restricted Global Note will have separate ISIN numbers and Common Codes and the Restricted Global Note will also have a CUSIP number.

2. Transfer Restrictions

Transfers of interests in Global Notes within DTC, Euroclear and Clearstream will be in accordance with the usual rules and operating procedures of the relevant system.

Each Restricted Global Note will bear a legend substantially identical to that set out below and neither a Restricted Global Note nor any beneficial interest in a Restricted Global Note may be transferred except in compliance with the transfer restrictions set forth in such legend.

A beneficial interest in a Restricted Global Note may be transferred to a person who wishes to take delivery of such beneficial interest through an Unrestricted Global Note only upon receipt by the Registrar of a written certification from the transferor (in the form scheduled to the Trust Deed) to the effect that such transfer is being made in accordance with Regulation S or Rule 144 (if available) under the Securities Act.

Any beneficial interest in either a Restricted Global Note or an Unrestricted Global Note that is transferred to a person who takes delivery in the form of a beneficial interest in the other relevant Global Note will, upon transfer, cease to be a beneficial interest in such Global Note and become a beneficial interest in the other relevant Global Note and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to a beneficial interest in such other relevant Global Note for so long as such person retains such an interest.

The Notes and the Guarantee are being offered and sold in the United States only to qualified institutional buyers within the meaning of and in reliance on Rule 144A that are also qualified purchasers within the meaning of Section 2(a)(51)(A) of the Investment Company Act and the rules and regulations thereunder, in each case acting for their own account or for the account of one or more qualified institutional buyers each of which is also a qualified purchaser. Because of the following restrictions, purchasers of Notes and the Guarantee offered in the United States in reliance on Rule 144A are advised to consult legal counsel prior to making any offer, resale, pledge or transfer of such Notes.

3. Restricted Notes

Each prospective purchaser of Notes and the Guarantee in reliance on Rule 144A (a “144A Offeree”), by accepting delivery of this Prospectus, will be deemed to have represented, agreed and acknowledged as follows:

- (i) such 144A Offeree acknowledges that this Prospectus is personal to such 144A Offeree and does not constitute an offer to any other person or to the public generally to subscribe for or otherwise acquire Notes. Distribution of this Prospectus, or disclosure of any of its contents to any person other than such 144A Offeree and those persons, if any, retained to advise such 144A Offeree with respect thereto and other persons meeting the requirements of Rule 144A or Regulation S is unauthorised, and any disclosure of any of its contents, without the prior written consent of the Issuer, is prohibited.
- (ii) such 144A Offeree agrees to make no photocopies of this Prospectus or any documents referred to herein.

Each purchaser of Restricted Notes within the United States, by accepting delivery of this Prospectus, will be deemed to have represented, agreed and acknowledged as follows (terms used herein that are defined in Rule 144A or in Regulation S are used herein as defined therein, as applicable):

- (a) the purchaser (i) is a QIB that is also a QP, (ii) was not formed for the purpose of investing in the Notes or the Issuer, (iii) is not a broker dealer which owns and invests on a discretionary basis less than U.S.\$25,000,000 in securities of unaffiliated issuers, (iv) is not a participant-directed employee plan such as a 401(k) plan, (v) is acting for its own account, or the account of one or more QIBs each of which is also a QP, and (vi) is aware, and each beneficial owner of the Notes has been advised, that the sale of the Notes to it is being made in reliance on Rule 144A.
- (b) it will (i) along with each account for which it is purchasing, hold and transfer beneficial interests in the Restricted Notes in a principal amount not less than U.S.\$100,000 and (ii) provide notice of these transfer restrictions to any subsequent transferees. In addition, it understands that the Issuer may receive a list of participants holding positions in the Restricted Notes from one or more book-entry depositaries.
- (c) (i) the Restricted Notes have not been and will not be registered under the Securities Act and may not be offered, sold, pledged or otherwise transferred except (a) in accordance with Rule 144A to a person that it, or any person acting on its behalf, reasonably believes is a QIB that is also a QP purchasing for its own account or for the account of one or more QIBs each of which is also a QP, (b) in an offshore transaction in accordance with Rule 903 or Rule 904 of Regulation S under the Securities Act, (c) pursuant to an exemption from registration under the Securities Act provided by Rule 144 thereunder (if available) or (d) pursuant to an effective registration statement under the Securities Act, in each case in accordance with any applicable securities laws of any State of the United States and (ii) it will, and each subsequent holder of the Restricted Notes is required to, notify any purchaser of the Restricted Notes from it of the resale restrictions on the Restricted Notes.
- (d) it understands that the Issuer has the power to compel any beneficial owner of the Restricted Notes that is a U.S. person and is not a QIB and a QP to sell its interests in the Restricted Notes, or may sell such interest on behalf of such owner. The Issuer has the right to refuse to honour the transfer of an interest in the Restricted Notes to a U.S. person who is not a QIB and a QP. Any purported transfer of the Restricted Notes to a purchaser that does not comply with the requirements of the transfer restrictions herein will be of no force and effect and will be void *ab initio*.
- (e) the Restricted Notes offered hereby will bear a legend to the following effect, unless the Issuer determines otherwise in accordance with applicable law:

“THIS NOTE HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE “**SECURITIES ACT**”), OR WITH ANY SECURITIES REGULATORY AUTHORITY OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES AND MAY NOT BE OFFERED, RESOLD, PLEDGED OR OTHERWISE TRANSFERRED EXCEPT (1) TO THE ISSUER, (2) IN ACCORDANCE WITH RULE 144A UNDER THE SECURITIES ACT (“**RULE 144A**”) TO A PERSON THAT THE HOLDER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER (“**QIB**”) WITHIN THE MEANING OF RULE 144A THAT IS ALSO A QUALIFIED PURCHASER (“**QP**”) WITHIN THE MEANING OF SECTION 2(a)(51)(A) OF THE U.S. INVESTMENT COMPANY ACT OF 1940, AS AMENDED (THE “**INVESTMENT COMPANY ACT**”), AND THE RULES AND REGULATIONS THEREUNDER PURCHASING FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT ONE OR MORE QIBs EACH OF WHICH IS ALSO A QP WHOM THE HOLDER HAS INFORMED, IN EACH CASE, THAT SUCH OFFER, SALE, PLEDGE OR OTHER TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A AND IN AN AMOUNT FOR EACH ACCOUNT OF NOT LESS THAN U.S.\$100,000, (3) IN AN OFFSHORE TRANSACTION IN ACCORDANCE WITH RULE 903 OR RULE 904 OF REGULATION S UNDER THE SECURITIES ACT OR (4) PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT PROVIDED BY RULE 144 THEREUNDER (IF AVAILABLE), IN EACH CASE IN ACCORDANCE WITH ANY APPLICABLE SECURITIES LAW OF ANY STATE OF THE UNITED STATES. THE HOLDER WILL, AND EACH SUBSEQUENT HOLDER IS REQUIRED TO, NOTIFY ANY PURCHASER FROM IT OF THE NOTES IN RESPECT HEREOF OF THE RESALE RESTRICTIONS REFERRED TO ABOVE. ANY TRANSFER IN VIOLATION OF THE FOREGOING WILL BE OF NO FORCE OR EFFECT AND WILL BE VOID AB INITIO. NO REPRESENTATION CAN BE MADE AS TO THE AVAILABILITY OF ANY EXEMPTION UNDER THE SECURITIES ACT FOR REALES OF THIS NOTE.

EACH PERSON WHO PURCHASES OR OTHERWISE ACQUIRES THIS NOTE (OR A BENEFICIAL INTEREST HEREIN) IN A TRANSACTION MEETING THE REQUIREMENTS OF RULE 144A, BY PURCHASING SUCH INTEREST, IS ALSO DEEMED TO REPRESENT, WARRANT, ACKNOWLEDGE AND AGREE FOR THE BENEFIT OF THE ISSUER THAT IT, AND EACH PERSON FOR WHICH IT IS ACTING, (i) IS A QIB THAT IS A QP, (ii) WAS NOT FORMED FOR THE PURPOSE OF INVESTING IN THE ISSUER OR THE NOTES, (iii) IS NOT A BROKERDEALER WHICH OWNS AND INVESTS ON A DISCRETIONARY BASIS NOT LESS THAN U.S.\$25,000,000 IN SECURITIES OF UNAFFILIATED ISSUERS, (iv) IS NOT A PARTICIPANT DIRECTED EMPLOYEE PLAN, SUCH AS A 401(k) PLAN, (v) IS ACTING FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF ONE OR MORE QIBs EACH OF WHICH IS ALSO A QP, (vi) IT, AND EACH ACCOUNT FOR WHICH IT HOLDS THE NOTES, WILL HOLD AND TRANSFER BENEFICIAL INTERESTS IN THE NOTES IN A PRINCIPAL AMOUNT THAT IS NOT LESS THAN U.S.\$100,000, (vii) IT UNDERSTANDS THAT THE ISSUER MAY RECEIVE A LIST OF PARTICIPANTS HOLDING POSITIONS IN THE NOTES FROM ONE OR MORE BOOK-ENTRY DEPOSITARIES AND (viii) IT WILL PROVIDE NOTICE OF THE FOREGOING TRANSFER RESTRICTIONS TO ANY SUBSEQUENT TRANSFEREES.

ANY RESALE OR OTHER TRANSFER OF THIS NOTE (OR BENEFICIAL INTEREST HEREIN) WHICH IS NOT MADE IN COMPLIANCE WITH THE RESTRICTIONS SET FORTH HEREIN WILL BE OF NO FORCE AND EFFECT, WILL BE NULL AND VOID AB INITIO AND WILL NOT OPERATE TO TRANSFER ANY RIGHTS TO THE TRANSFEREE, NOTWITHSTANDING ANY INSTRUCTIONS TO THE CONTRARY TO THE ISSUER OR ANY OF ITS AGENTS. IN ADDITION TO THE FOREGOING, IN THE EVENT OF A TRANSFER OF THIS NOTE (OR BENEFICIAL INTEREST HEREIN) TO A U.S. PERSON WITHIN THE MEANING OF REGULATION S THAT IS NOT A QIB AND

A QP, THE ISSUER MAY (A) COMPEL SUCH TRANSFEREE TO SELL THIS NOTE OR ITS INTEREST HEREIN TO A PERSON WHO (I) IS A U.S. PERSON WHO IS A QIB AND A QP THAT IS, IN EACH CASE OTHERWISE QUALIFIED TO PURCHASE THIS NOTE (OR BENEFICIAL INTEREST HERE) IN A TRANSACTION EXEMPT FROM REGISTRATION UNDER THE SECURITIES ACT OR (II) IS NOT A U.S. PERSON WITHIN THE MEANING OF REGULATION S IN AN OFFSHORE TRANSACTION IN COMPLIANCE WITH REGULATION S OR (B) COMPEL SUCH TRANSFEREE TO SELL THIS NOTE (OR BENEFICIAL INTEREST HEREIN) TO A PERSON DESIGNATED BY OR ACCEPTABLE TO THE ISSUER AT A PRICE EQUAL TO THE LESSER OF (X) THE PURCHASE PRICE THEREFOR PAID BY THE ORIGINAL TRANSFEREE, (Y) 100 PER CENT. OF THE PRINCIPAL AMOUNT THEREOF OR (Z) THE FAIR MARKET VALUE THEREOF. THE ISSUER HAS THE RIGHT TO REFUSE TO HONOUR A TRANSFER OF THIS NOTE (OR BENEFICIAL INTEREST HEREIN) TO A U.S. PERSON WHO IS NOT A QIB AND A QP. EACH TRANSFEROR OF THIS NOTE WILL PROVIDE NOTICE OF THE TRANSFER RESTRICTIONS SET FORTH HEREIN AND IN THE AGENCY AGREEMENT TO ITS TRANSFEREE. THE ISSUER HAS NOT REGISTERED AND DOES NOT INTEND TO REGISTER UNDER THE INVESTMENT COMPANY ACT.

THIS NOTE AND RELATED DOCUMENTATION MAY BE AMENDED OR SUPPLEMENTED FROM TIME TO TIME TO MODIFY THE RESTRICTIONS ON AND PROCEDURES FOR RESALES AND OTHER TRANSFERS OF THIS NOTE TO REFLECT ANY CHANGE IN APPLICABLE LAW OR REGULATION (OR THE INTERPRETATION THEREOF) OR IN PRACTICES RELATING TO THE RESALE OR TRANSFERS OF RESTRICTED SECURITIES GENERALLY. BY THE ACCEPTANCE OF THIS NOTE, THE HOLDER HEREOF SHALL BE DEEMED TO HAVE AGREED TO ANY SUCH AMENDMENT OR SUPPLEMENT.

THE ISSUER MAY COMPEL EACH BENEFICIAL HOLDER HEREOF TO CERTIFY PERIODICALLY THAT SUCH OWNER IS A QIB AND A QP.”

For so long as the Notes of the relevant series are held in global form, Noteholders of such series may not require transfers to be registered during the period beginning on the third business day before the due date for any payment of principal or interest in respect of such Notes.

Prospective purchasers are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A.

4. Unrestricted Notes

Each purchaser of Notes pursuant to Regulation S by accepting delivery of this Prospectus and the Notes, will be deemed to have represented, agreed and acknowledged that:

- (1) it is, or at the time Notes are purchased will be, the beneficial owner of such Notes and (a) it is not a U.S. person and it is located outside the United States (within the meaning of Regulation S) and (b) it is not an affiliate of the Issuer or a person acting on behalf of such an affiliate.
- (2) the Issuer, the Registrar, the Lead Manager and their affiliates, and others will rely upon the truth and accuracy of the foregoing acknowledgments, representations and agreements.
- (3) none of the Issuer, the Lead Manager or any person representing any such entity has made any representation to it with respect to any such entity or the offering or sale of any Notes, other than the information in this Prospectus.

5. Exchange of Interests in Global Notes for Note Certificates

Registration of title to Notes initially represented by a Restricted Global Notes in a name other than DTC or a successor depository or one of their respective nominees will not be permitted in respect of the Notes unless (a) such depository notifies the Issuer that it is no longer willing or able to discharge properly its

responsibilities as depository with respect to the Global Notes or ceases to be a “clearing agency” registered under the United States Securities Exchange Act of 1934 (the “**Exchange Act**”), or is at any time no longer eligible to act as such, and the Issuer is unable to locate a qualified successor within 90 days of receiving notice of such ineligibility on the part of such depository or (b) following a failure to pay principal in respect of the relevant Notes at maturity or upon acceleration of any such Note, and the Trustee has received a request from the registered holder of the relevant Restricted Global Note requesting exchange of such Restricted Global Note for individual note certificates (the “**Restricted Note Certificates**”).

Registration of title to Notes initially represented by an Unrestricted Global Note in a name other than the nominee of the common depository for Euroclear and Clearstream, Luxembourg will not be permitted unless (a) Euroclear or Clearstream, Luxembourg is closed for business for a continuous period of 14 days (other than by reason of holidays, statutory or otherwise) or announces an intention permanently to cease business or does in fact do so and no alternative clearing system satisfactory to the Trustee is available or (b) following a failure to pay principal in respect of any relevant Note at maturity or upon acceleration of any such Note, and the Trustee has received a request from the registered holder of the relevant Unrestricted Global Note requesting exchange of such Unrestricted Global Note for individual note certificates (the “**Unrestricted Note Certificates**”, and together with the Restricted Note Certificates, the “**Note Certificates**”).

In such circumstances, the relevant Global Note shall be exchanged in full for Note Certificates and the Issuer will, at the cost of the Issuer (but against such indemnity as the Registrar or any relevant Transfer Agent may require in respect of any tax or other duty of whatever nature which may be levied or imposed in connection with such exchange), cause sufficient Note Certificates to be executed and delivered to the Registrar for completion, authentication and dispatch to the relevant Noteholders. A person having an interest in a Global Note must provide the Registrar with (a) a written order containing instructions and such other information as the Issuer and the Registrar may require to complete, execute and deliver such Note Certificates and (b) in the case of a Restricted Global Note only, a fully completed, signed certification substantially to the effect that the exchanging holder is not transferring its interest at the time of such exchange or, in the case of simultaneous sale pursuant to Rule 144A or Regulation S, a certification that the transfer is being made in compliance with the provisions of Rule 144A or Regulation S. Note Certificates issued in exchange for a beneficial interest in a Restricted Global Note shall bear the legends applicable to transfers pursuant to Rule 144A, as set out under “*Transfer Restrictions*” above.

The holder of a Note may transfer such Note in accordance with the provisions of Condition 2 of the Terms and Conditions of the Notes. See “*Terms and Conditions of the Notes — Register, Title and Transfers*”. Note Certificates may not be eligible for trading in the DTC, Euroclear and Clearstream, Luxembourg systems.

Upon the transfer, exchange or replacement of a Restricted Note Certificate bearing the legend referred to under “*Transfer Restrictions*”, or upon specific request for removal of the legend on a Restricted Note Certificate, the Issuer will deliver only Restricted Note Certificates that bear such legend, or will refuse to remove such legend, as the case may be, unless there is delivered to the Issuer and the Registrar such satisfactory evidence, which may include an opinion of counsel, as may reasonably be required by the Issuer that neither the legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act.

The Registrar will not register the transfer of or exchange of interests in a Global Note for Note Certificates for a period of 15 calendar days ending on the due date for payment of principal or interest.

6. DTC, Euroclear and Clearstream, Luxembourg Arrangements

So long as DTC or its nominee or Euroclear, Clearstream, Luxembourg or the nominee of their common depository is the registered holder of a Global Note, DTC Euroclear, Clearstream, Luxembourg or such nominee, as the case may be, will be considered the sole owner or holder of the Notes represented by such Global Note for all purposes under the Trust Deeds, Agency Agreements and the Notes. Payments of principal, interest and additional amounts, if any, in respect of the Global Notes will be made to DTC, Euroclear, Clearstream, Luxembourg or such nominee, as the case may be, as the registered holder thereof. None of the Issuer, the Trustee, any Agent or the Lead Manager or any affiliate of any of the above or any person by whom any of the above is controlled for the purposes of the Securities Act will have any

responsibility or liability for any aspect of the records relating to or payments made on account of beneficial ownership interests in the Global Notes or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

Distributions of principal and interest with respect to book entry interests in the Notes held through Euroclear or Clearstream, Luxembourg will be credited, to the extent received by Euroclear or Clearstream, Luxembourg from the Principal Paying Agent, to the cash accounts of Euroclear or Clearstream, Luxembourg customers in accordance with the relevant system's rules and procedures.

Holders of book-entry interests in Notes held through DTC will receive from the Principal Paying Agent through DTC, to the extent received by DTC from the Principal Paying Agent, all distributions of principal and interest made with respect to book-entry interests in such Notes. Distributions in the United States will be subject to relevant U.S. tax laws and regulations.

Each payment in respect of a Global Note Certificate will be made to the person shown as the Holder in the relevant Register at the close of business (in the relevant clearing system) on the Clearing System Business Day before the due date for such payment (the "**Record Date**") where "**Clearing System Business Day**" means a day on which each clearing system for which the Global Note Certificate is being held is open for business. Trading between a Restricted Global Note and the relevant Unrestricted Global Note, as the case may be, will therefore be net of accrued interest from the relevant Record Date to the relevant interest payment date.

The laws of some states of the United States require that certain persons take physical delivery of securities in definitive form. Consequently, the ability to transfer interests in a Global Note to such persons will be limited. Because DTC, Euroclear and Clearstream, Luxembourg can only act on behalf of participants, who in turn act on behalf of indirect participants, the ability of a person having an interest in a Global Note to pledge such interest to persons or entities which do not participate in the relevant clearing system, or otherwise take actions in respect of such interest, may be affected by the lack of a physical certificate in respect of such interest.

The holdings of book entry interests in the Notes through Euroclear, Clearstream, Luxembourg and DTC will be reflected in the book entry accounts of each such institution. As necessary, the Registrar will adjust the amounts of Notes on the Register for the accounts of (i) The Bank of New York Depository (Nominees) Limited and (ii) Cede & Co. to reflect the amounts of Notes held through Euroclear and Clearstream, Luxembourg and DTC, respectively. Beneficial ownership of Notes will be held through financial institutions as direct and indirect participants in Euroclear, Clearstream, Luxembourg and DTC.

Interests in the Unrestricted Global Note and the Restricted Global Note will be in uncertificated book entry form.

7. Secondary Market Trading in Relation to Global Notes

The Issuer has obtained the information in this section concerning DTC, Euroclear and Clearstream, Luxembourg and their book entry systems from sources made publicly available by DTC, Euroclear and Clearstream, Luxembourg, which the Issuer believes to be reliable and which has been accurately extracted and/or summarised from those sources. The Issuer takes no responsibility for the accuracy of this information and only accepts responsibility for accurately extracting the information from those sources.

8. Trading between Euroclear and/or Clearstream, Luxembourg participants

Secondary market sales of book entry interests in the Notes held through Euroclear or Clearstream, Luxembourg to purchasers of book entry interests in the Notes through Euroclear or Clearstream, Luxembourg will be conducted in accordance with the normal rules and operating procedures of Euroclear and Clearstream, Luxembourg and will be settled using the procedures applicable to conventional eurobonds.

9. Trading between DTC Participants

Secondary market sales of book-entry interests in Notes between DTC participants will occur in the ordinary way in accordance with DTC rules and will be settled using the procedures applicable to U.S. corporate debt obligations in DTC's Same Day Funds Settlement System.

10. Trading between DTC Seller and Euroclear/Clearstream Purchaser

When a book-entry interest in Notes is to be transferred from the account of a DTC participant holding a beneficial interest in a Restricted Global Note to the account of a Euroclear or Clearstream accountholder wishing to purchase a beneficial interest in the relevant Unrestricted Global Note (subject to such certification procedures as are provided in the Agency Agreements), the purchaser must send instructions to Euroclear or Clearstream at least one business day prior to the settlement date. Euroclear or Clearstream, as the case may be, will instruct the common depository to receive the beneficial interest and make payment for it. Payment will include interest accrued on the beneficial interest in the Notes from and including the last interest payment date to and excluding the settlement date. On the settlement date, the common depository will make payment to the DTC participant's account against delivery of the beneficial interest. After settlement has been completed, the beneficial interest will be credited to the respective clearing system, and by the clearing system, in accordance with its usual procedures, to the Euroclear or Clearstream accountholder's account. The securities credit will appear the next day, European time. The cash debit will be back-valued to, and interest on the relevant Unrestricted Global Notes will accrue from, the value date, which will be the preceding day when settlement occurs in New York. If settlement is not completed on the intended value date, that is, if the trade fails, the Euroclear or Clearstream cash debit will be valued instead as of the actual settlement date, whenever that may be.

The Euroclear or Clearstream accountholder will need to make available to its clearing system the funds necessary to process same-day funds settlement. The most direct means of doing so is to pre-position funds for settlement, either from cash on hand or existing lines of credit, as it would for any pre-settlement occurring within Euroclear or Clearstream. Under this approach, the purchasing accountholder may take on credit exposure to Euroclear or Clearstream until the beneficial interest in such Unrestricted Global Notes is credited to its account one day later. As an alternative, if Euroclear or Clearstream has extended a line of credit to the purchasing accountholder, it can elect not to pre-position funds and allow that credit line to be drawn upon to finance settlement. Under this procedure, the Euroclear or Clearstream accountholder purchasing the beneficial interest in such Unrestricted Global Notes would incur overdraft charges for one day, assuming it cleared the overdraft when the beneficial interest was credited to its account. However, interest on such Unrestricted Global Notes would accrue from the value date. Therefore, in many cases, the investment income on such Unrestricted Global Notes earned during that one-day period may substantially reduce or offset the amount of such overdraft charges, although this result will depend on each accountholder's particular cost of funds.

Because the settlement is taking place during New York business hours, the DTC participant can use its usual procedures for transferring a beneficial interest in the Global Notes to the common depository for the benefit of the Euroclear or Clearstream accountholder. The sale proceeds will be available to the DTC seller on the settlement date. Thus, to the DTC participant, a cross-market transaction will settle no differently than a trade between two DTC participants.

Day traders that use Clearstream or Euroclear to purchase interests in the Bonds from DTC participants for delivery to Clearstream participants or Euroclear participants should note that these trades will automatically fail on the sale side unless affirmative action is taken. At least three techniques should be readily available to eliminate this potential problem:

- Borrowing through Clearstream or Euroclear for one day, until the purchase side of the day trade is reflected in their Clearstream or Euroclear accounts, in accordance with the clearing system's customary procedures; or

- Borrowing the interests in the United States from a DTC participant no later than one day prior to settlement, which will give the interests sufficient time to be reflected in their Clearstream or Euroclear account in order to settle the sale side of the trade; or
- Staggering the value date for the buy and sell sides of the trade so that the value date for the purchase from the DTC participant is at least one day prior to the value date for the sale to the Clearstream participant or Euroclear participant.

11. Trading between Euroclear/Clearstream Seller and DTC Purchaser

Due to time zone differences in its favour, a Euroclear or Clearstream accountholder may employ customary transfer procedures when transferring a book-entry interest in Unrestricted Global Notes to the account of a DTC participant wishing to purchase a beneficial interest in the relevant Restricted Global Note (subject to such certification procedures as are provided in the Agency Agreements). The seller must send instructions to Euroclear or Clearstream at least one business day prior to the settlement date. Euroclear or Clearstream will instruct the common depositary to credit the beneficial interest in the Global Notes to the DTC participant's account and receive payment. Payment will include interest accrued on the beneficial interest in the Notes from and including the last interest payment date to and excluding the settlement date. Payment will be reflected in the account of the Euroclear or Clearstream accountholder the following day. Receipt of cash proceeds in the Euroclear or Clearstream accountholder's account will be back-valued to the value date, which will be the preceding day, when settlement occurs in New York. If the Euroclear or Clearstream accountholder has a line of credit with its clearing system and elects to draw on such line of credit in anticipation of receipt of sale proceeds in its account, the back-valuation may substantially reduce or offset any overdraft charges incurred over that one-day period. If settlement is not completed on the intended value date, that is, if the trade fails, receipt of the cash proceeds in the Euroclear or Clearstream accountholder's account will instead be valued as of the actual settlement date, whenever that may be.

For a further description of restrictions on the transfer of Notes, see "*Transfer Restrictions*" above.

DTC has advised the Issuer that it will take any action permitted to be taken by a holder of Notes (including, without limitation, the presentation of Global Notes for exchange as described above) only at the direction of one or more participants in whose account with DTC interests in Global Notes are credited and only in respect of such portion of the aggregate principal amount of the relevant Global Notes as to which such participant or participants has or have given such direction. In the circumstances described above, DTC will surrender the Global Notes for exchange for individual Note Certificates, which will, in the case of Restricted Note Certificates, bear the legend applicable to transfers pursuant to Rule 144A.

DTC has advised the Issuer as follows: DTC is a limited-purpose trust company organised under the laws of the State of New York, a member of the United States Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code and a "clearing agency" registered pursuant to the provisions of Section 17A of the Exchange Act. DTC was created to hold securities for its participants and to facilitate the clearance settlement of transactions between its participants through electronic book-entry changes in accounts of its participants, thereby eliminating the need for physical movement of certificates. DTC participants include securities brokers and dealers, banks, trust companies and clearing corporations and may in the future include certain other organisations. Indirect access to the DTC system is also available to banks, brokers, dealers and trust companies that clear through, or maintain a custodial relationship with, a participant, either directly or indirectly. DTC is owned by a number of its direct participants and by the New York Stock Exchange, Inc., the American Stock Exchange, Inc. and the National Association of Securities Dealers.

Euroclear and Clearstream have advised the Issuer as follows: Euroclear and Clearstream hold securities for participating organisations and facilitate the clearance and settlement of securities between their respective accountholders through electronic book-entry changes in accounts of such accountholders. Euroclear and Clearstream provide to their accountholders, among other things, services for safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Euroclear and Clearstream interface with domestic securities markets. Euroclear and Clearstream accountholders are

financial institutions such as underwriters, securities brokers and dealers, banks, trust companies and certain other organisations. Indirect access to Euroclear or Clearstream is also available to others such as banks, brokers, dealers and trust companies that clear through or maintain a custodian relationship with a Euroclear or Clearstream accountholder, either directly or indirectly.

Although the foregoing sets out the procedures of DTC, Euroclear and Clearstream to facilitate transfers of beneficial interests in Global Bonds among participants and accountholders of DTC, Euroclear and Clearstream, none of DTC, Euroclear or Clearstream is under any obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time. Neither the Issuer nor any agent of the Issuer nor any person by whom any of them is controlled for purposes of the Securities Act will have any responsibility for the performance by DTC, Euroclear or Clearstream or their respective direct or indirect participants or accountholders of their respective obligations under the rules and procedures governing their operations or the sufficiency for any purpose of the arrangements described above.

While a Global Note is lodged with DTC or the Custodian, Notes represented by individual Notes Certificates will not be eligible for clearing or settlement through DTC. While a Global Note is lodged with Euroclear or Clearstream or the common depository for Euroclear or Clearstream, Notes represented by individual Note Certificates will not be eligible for clearing or settlement through Euroclear or Clearstream.

12. Notices

So long as Unrestricted Global Notes are held on behalf of Euroclear and Clearstream, Luxembourg or any other clearing system (an “**Alternative Clearing System**”), notices to holders of Notes represented by a beneficial interest in such Unrestricted Global Notes may be given by delivery of the relevant notice to Euroclear or Clearstream, Luxembourg or, as the case may be, the Alternative Clearing System and so long as a Restricted Global Note is held on behalf of DTC or an Alternative Clearing System, notices to holders of Notes represented by a beneficial interest in such Restricted Global Note may be given by delivery of the relevant notice to DTC or the Alternative Clearing System; except that, so long as the notes are listed on the Irish Stock Exchange, notices will also be published either via the Companies Announcement Office of the Irish Stock Exchange or in the Irish Times.

SUBSCRIPTION AND SALE

Morgan Stanley & Co. International plc (the “**Lead Manager**”) has, in a subscription agreement dated 1 November 2010 (the “**Subscription Agreement**”) and made between the Issuer, the Guarantor and the Lead Manager upon the terms and subject to the conditions contained therein, agreed to subscribe for the Notes at their issue price of 99.2302 per cent. of their principal amount. The Issuer (failing which, the Guarantor) has also agreed to reimburse the Lead Manager for certain of its expenses incurred in connection with the management of the issue of the Notes. The Lead Manager is entitled in certain circumstances to be released and discharged from its obligations under the Subscription Agreement prior to the closing of the issue of the Notes.

United Kingdom

The Lead Manager has represented, warranted and undertaken that:

- (a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the Financial Services and Markets Act 2000 (the “**FSMA**”) received by it in connection with the issue or sale of the Notes in circumstances in which Section 21(1) of the FSMA does not apply to the Issuer or the Guarantor; and
- (b) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

United States of America

The Notes and the Guarantee have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, any U.S. person except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. Accordingly, the Lead Manager has agreed to offer the Notes for resale in the United States initially only to persons they reasonably believe to be qualified institutional buyers that is also a qualified purchaser within the meaning of Section 2(a)(51)(A) of the Investment Company Act and the rules and regulations thereunder, in each case acting for their own account or for the account of one or more qualified institutional buyers each of which is also a qualified purchaser in reliance on Rule 144A and outside the United States in offshore transactions in reliance on Regulation S. Terms used in this paragraph have the respective meanings given to them by Regulation S.

The Lead Manager has agreed that, except as permitted by the Subscription Agreement, it will not offer or sell the Notes as part of its distribution at any time, within the United States or to, or for the account or benefit of, U.S. persons. Terms used in this paragraph have the meaning given to them by Regulation S.

The Notes and the Guarantee are being offered and sold outside of the United States to non-U.S. persons in reliance on Regulation S. The Subscription Agreement provides that the Lead Manager may, through its U.S. broker-dealer affiliates, resell a portion of the Notes and the Guarantee within the United States only to qualified institutional buyers that are also qualified purchasers in reliance on Rule 144A.

Ukraine

The Notes have not been and will not be registered in Ukraine and may not be offered or sold in Ukraine without prior registration in Ukraine.

General

The Lead Manager has represented, warranted and agreed that it has complied and will comply with all applicable laws and regulations in each country or jurisdiction in which it purchases, offers, sells or delivers Notes or possesses, distributes or publishes this Prospectus or any other offering material relating to the Notes. Persons into whose hands this Prospectus comes are required by the Issuer, the Guarantor and the

Lead Manager to comply with all applicable laws and regulations in each country or jurisdiction in which they purchase, offer, sell or deliver Notes or possess, distribute or publish this Prospectus or any other offering material relating to the Notes, in all cases at their own expense.

GENERAL INFORMATION

Authorisation

1. The creation and issue of the Notes has been authorised by an order of the Agency dated 19 October 2010. The giving of the Guarantee of the Notes has been duly authorised by Resolution No 936 of the Cabinet of Ministers of Ukraine dated 12 October 2010.

Legal and Arbitration Proceedings

2. Save as disclosed in the Prospectus on pages 58 – 62, there are no governmental, legal or arbitration proceedings, (including any such proceedings which are pending or threatened, of which the Issuer or the Guarantor are aware), which may have, or have had during the 12 months prior to the date of this Prospectus, a significant effect on the financial position or profitability of the Issuer or the financial position of the Guarantor.

Significant/Material Change

3. Since its incorporation there has been no material adverse change in the prospects of the Issuer nor any significant change in the financial or trading position of the Issuer.

Documents on Display

4. Copies of the following documents (together with English translations thereof), in physical form, may be inspected during normal business hours at the offices of the Agency at 2 Mechnikova str., Kyiv, Ukraine from the date of this Prospectus:
 - (a) the constitutive documents of the Issuer;
 - (b) the Agency Agreement and the Trust Deed;
 - (c) the Deed of Guarantee;
 - (d) a copy of the authorisations listed above under “Authorisations”; and
 - (e) the budget for the current fiscal year for Ukraine.

Yield

5. On the basis of the reoffer price of the Notes of 101.448 per cent. of their principal amount, the yield of the Notes is 8.1 per cent. on a semi-annual basis.

ISIN, Common Code and CUSIP

6. The Unrestricted Global Note has been accepted for clearance through Euroclear and Clearstream, Luxembourg and the Restricted Global Note has been accepted for clearance through DTC.

	Unrestricted Global Note	Restricted Global Note
ISIN	XS0556327822	US31771VAA17
Common Code	055632782	055635676
CUSIP	N/A	31771VAA1

Language

7. The language of the Prospectus is English. Certain legislative references and technical terms have been cited in their original language in order that the correct technical meaning may be ascribed to them under applicable law.

Financial Statements

8. The Issuer was established as a state enterprise by the Order of the National Agency on Preparation and Holding in Ukraine of the UEFA Euro 2012 On Establishment of State Enterprise “FINANCING OF INFRASTRUCTURAL PROJECTS” dated 7 September 2010, No. 115. It currently does not produce any financial statements but is expected to in the future.

Listing

9. The expenses in connection with the admission of the Notes to the Official List and to trading on the Market are expected to amount to approximately EUR 4,940.
10. Arthur Cox Listing Services Limited is acting solely in its capacity as listing agent for the Issuer in relation to the Notes and is not itself seeking admission to the Official List or trading on the regulated market of the Irish Stock Exchange for the purpose of the Prospectus Directive.

ANNEX - FORM OF DEED OF GUARANTEE

The following is the text of the Deed of Guarantee save for the signature page.

THIS DEED OF GUARANTEE is dated 3 November 2010 and is issued by:

- (1) The Cabinet of Ministers of Ukraine (acting on behalf of Ukraine) represented by the Minister of Finance of Ukraine (the “**Guarantor**”) in favour of
- (2) **BNY CORPORATE TRUSTEE SERVICES LIMITED** as trustee (the “**Trustee**” which expression shall, wherever the context so admits, include such company and all other persons or companies for the time being trustee or trustees of the Trust Deed and this Guarantee) for itself and on behalf of the Noteholders.

BACKGROUND

- (1) State enterprise “Financing of Infrastructural Projects” (the “**Issuer**”) has authorised the creation and issue of USD 568,000,000 8.375 per cent. Guaranteed Notes due 2017 (the “**Notes**”).
- (2) The Notes will be in registered form and in the denomination of USD 100,000 and integral multiples of USD 1,000 in excess thereof. The Notes will be represented by a global note certificate, which will be exchangeable for individual note certificates in the circumstances specified therein.
- (3) The Notes will be constituted by the Trust Deed (as defined below).
- (4) The Issuer and the Guarantor will, in relation to the Notes, enter into the Agency Agreement (as defined below).
- (5) The Guarantor has agreed to guarantee the payment of all sums expressed to be payable from time to time by the Issuer in respect of the Notes and under the Trust Deed upon the terms of this Guarantee.

1. DEFINITIONS AND CONSTRUCTION

1.1 Definitions

In this Guarantee, unless a contrary indication appears, terms used in the Trust Deed have the same meaning and construction and:

“**Agency Agreement**” means the issue and paying agency agreement dated 3 November 2010 and made between, among others, the Issuer, the Guarantor, the Trustee and The Bank of New York Mellon as principal paying agent.

“**Guarantee**” means this Deed of Guarantee as from time to time amended, supplemented, novated or restated.

“**Party**” means a party to this Guarantee.

“**Trust Deed**” means the trust deed dated 3 November 2010 and made between the Issuer, the Guarantor and the Trustee, as from time to time amended, supplemented, novated, restated or replaced and for the purposes of this Deed shall include any fee letter entered into by the Trustee in connection with its remuneration as Trustee.

1.2 Construction of certain references

Any reference in this Guarantee to:

- (a) a “business day” means a day (other than a Saturday or Sunday) on which banks generally are open for business in London and Kiev; and

- (b) a “person” includes a reference to that person’s legal personal representatives, successors in title, permitted assigns and any further assigns, permitted transferees and any further transferees, and chargees.

1.3 **Third Party Rights**

A person who is not a Party has no right under the Contracts (Rights of Third Parties) Act 1999 to enforce or to enjoy the benefit of any term of this Guarantee.

1.4 **Clauses**

In this Guarantee any reference to a “Clause” is, unless the context otherwise requires, a reference to a Clause to this Guarantee.

1.5 **Headings**

Headings and sub-headings are for ease of reference only and shall not effect the construction of this Guarantee.

1.6 **Languages**

This Guarantee has been executed in both the English language and the Ukrainian language. In the case of any discrepancy between the English and Ukrainian texts of this Guarantee, the English language text shall prevail and questions of interpretation shall be addressed solely in the English language.

2. **GUARANTEE AND INDEMNITY**

2.1 **Guarantee**

The Guarantor unconditionally and irrevocably:

- (a) guarantees to the Trustee the performance by the Issuer of the Issuer’s payment obligations under the Trust Deed and in respect of the Notes, as and when the same shall become due and payable, whether at maturity, upon early redemption, upon acceleration or otherwise, in each case according to the terms of the Trust Deed and the Notes; and
- (b) undertakes with the Trustee that whenever the Issuer does not or will not pay any amount as and when the same shall become due and payable under the Trust Deed and the Notes, the Guarantor shall pay that amount punctually as if it was the principal obligor, as and when the same becomes due and payable, whether at maturity, upon early redemption, upon acceleration or otherwise, as if such payment were made by the Issuer.

2.2 **Indemnity**

The Guarantor unconditionally and irrevocably agrees with the Trustee that if any obligation guaranteed by it is or becomes unenforceable, invalid or illegal, it will, as an independent and primary obligation, pay the Trustee amounts sufficient to indemnify the Trustee and the Noteholders against any cost, loss or liability which the Trustee or the Noteholders incur as a result of the Issuer not paying any amount which would, but for such unenforceability, invalidity or illegality, have been payable by it under the Trust Deed and the Notes on the date when it would have been due. The amount payable by the Guarantor under this Clause 2.2 will not exceed the amount it would have had to pay under Clause 2.1 if the amount claimed had been recoverable on the basis of a guarantee.

2.3 **Guarantor as principal debtor**

Neither the obligations of the Guarantor herein contained nor the rights, powers and remedies conferred upon the Trustee and the Noteholders by this Deed of Guarantee or by law shall be discharged, impaired or otherwise affected by:

- (a) the winding up, dissolution, administration, re organisation or moratorium of the Issuer or any change in its status, function, control or ownership;
- (b) any amendment, novation, supplement, extension, restatement or replacement of the Notes and/or the Trust Deed, in each case, with the prior written consent of the Guarantor;
- (c) the taking, existence or release of any other guarantee;
- (d) the release of the Issuer or any other person under the terms of any composition or arrangement with any creditor of the Issuer;
- (e) any illegality, invalidity or unenforceability of any obligations of any person under the Notes and the Trust Deed;
- (f) the taking, variation, compromise, exchange, renewal or release of, or refusal or neglect to perfect, take up or enforce, any rights against, or security over assets of, the Issuer, the Guarantor or any other person or any non-presentation or non-observance of any formality or other requirement in respect of any instrument or any failure to realise the full value of any security; or
- (g) any other act, event or omission which, but for this sub-clause, might operate to discharge, impair or otherwise affect the obligations expressed to be assumed by the Guarantor herein or any of the rights, powers or remedies conferred upon the Trustee and the Noteholders or any of them by this Deed of Guarantee or by law.

2.4 **Guarantor's obligations continuing**

This Guarantee is a continuing guarantee and will extend to the ultimate balance of sums payable by the Issuer or the Guarantor under the Notes and the Trust Deed, regardless of any intermediate payment or discharge in part.

2.5 **Compliance with Conditions**

The Guarantor covenants in favour of the Trustee that it will duly perform and comply with the obligations expressed to be undertaken by it in the Conditions.

2.6 **Reinstatement**

If any discharge, release or arrangement (whether in respect of the obligations of the Issuer and/or the Guarantor or any security for those obligations or otherwise) is made by the Trustee in whole or in part on the basis of any payment, security or other disposition which is avoided or must be restored in bankruptcy, insolvency, liquidation, dissolution or otherwise, without limitation, then the liability of the Guarantor under this Clause 2 will continue or be reinstated as if the discharge, release or arrangement had not occurred.

2.7 **Additional security**

This Guarantee is in addition to and is not in any way prejudiced by any other guarantee or security now or subsequently held by the Trustee.

2.8 Enforcement

The Guarantor waives any right it may have of first requiring the Trustee (or any trustee or agent on its behalf) to proceed against or enforce any other rights or security or claim payment from any person before claiming from the Guarantor under this Clause 2. This waiver applies irrespective of any law or any provision of the Notes and the Trust Deed to the contrary. However, if the Guarantor fails to pay any amount of principal, premium or interest in respect of the Notes in accordance with Clauses 2.1 or 2.2 (a “**Non-Payment**”), the Trustee shall not be entitled to call for payment or take any other action to enforce its rights under this Deed of Guarantee in respect of such Non-Payment unless a Default Event occurs (where “**Default Event**” means an Non-Payment which continues for a period of 10 days or more).

2.9 Exercise of Guarantor’s rights

- (a) Until all amounts which may be or become payable by the Issuer or the Guarantor under or in connection with the Notes and the Trust Deed have been irrevocably paid in full and unless the Trustee otherwise directs, the Guarantor will not exercise any rights which it may have by reason of performance by it of its obligations under this Guarantee or by reason of any amount being payable, or liability arising, under this Clause 2:
- (i) to be indemnified by the Issuer;
 - (ii) to claim any contribution from any other guarantor of the Issuer’s obligations under the Notes and the Trust Deed;
 - (iii) to take the benefit (in whole or in part and whether by way of subrogation or otherwise) of any rights of the Trustee under the Trust Deed or of any other guarantee or security taken pursuant to, or in connection with, the Notes and the Trust Deed;
 - (iv) to bring legal or other proceedings for an order requiring the Issuer to make any payment, or perform any obligation, in respect of which the Guarantor has given a guarantee, undertaking or indemnity under this Guarantee;
 - (v) to exercise any right of set-off against the Issuer;
 - (vi) to claim or prove as a creditor of the Issuer in competition with the Trustee;
 - (vii) to enforce, or receive any payments arising out of or based upon or prove in any insolvency or winding up of the Issuer in respect of such right of subrogation; and/or
 - (viii) to take any security (which term shall not, for the avoidance of doubt, include the concept of a “penalty” (“*Penya*”) as understood under Ukrainian law) from the Issuer in respect of the Guarantor’s obligations under this Clause 2.
- (b) Any amount received by the Guarantor as a result of any exercise of any such right shall to the extent of amounts still owed to the Trustee be paid to the Trustee for the benefit of the Noteholders in accordance with the terms of the Trust Deed and the Notes.

2.10 Suspense Account

Any amount received or recovered by the Trustee from the Guarantor in respect of any sum payable by the Issuer under the Trust Deed or the Notes may be placed in a suspense account and kept there for so long as the Trustee thinks fit.

3. REPRESENTATIONS

The Guarantor represents and warrants to the Trustee as follows:

3.1 Status

It has the powers and authorities granted to it under the laws of Ukraine.

3.2 Binding obligations

The obligations expressed to be assumed by it in this Guarantee are, subject to any general principles of law limiting its obligations, legal, valid, binding and enforceable obligations.

3.3 Non-conflict

The entry into and performance by it of, and the transactions contemplated by, this Guarantee do not conflict with:

- (a) any law or regulation applicable to it;
- (b) any public policy or public order in Ukraine; and
- (c) any agreement, instrument or treaty binding upon it or any of its assets.

3.4 Powers and authority

It has the power to enter into, perform and deliver, and has taken all necessary action to authorise its entry into, performance and delivery of, this Guarantee and the transactions contemplated by this Guarantee.

3.5 Authorisations

All authorisations, resolutions, consents, licences and approvals of any administrative agency or governmental or other body required to be taken or obtained by it in connection with the entry into, performance, validity and enforceability of, and the transaction contemplated by this Guarantee have been obtained or effected and are in full force and effect.

3.6 Pari passu ranking

This Guarantee constitutes direct, general and unconditional obligations of the Guarantor which will at all times rank at least *pari passu* with all its other present and future unsecured and unsubordinated obligations, except for obligations which are preferred by mandatory operation of law.

3.7 Governing law and enforcement

- (a) The choice of English law as the governing law of this Guarantee, and any non-contractual obligations arising out of in connection with it, will be recognised and enforced under the laws of the Ukraine.
- (b) Any arbitral award obtained in England in relation to this Guarantee will be recognised and enforced under the laws of Ukraine subject to the terms of the applicable international treaties of Ukraine (including the 1958 New York United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards) subject to any applicable limitations set forth therein and applicable procedural laws of Ukraine.

4. TAX

4.1 Definitions

In this Guarantee:

“**Tax Credit**” means a credit against, relief or remission for, or repayment of any Tax.

“**Tax Payment**” means either the increase in a payment made by the Guarantor under Condition 7 (*Taxation*) or a payment under Clause 4.2 (*Tax indemnity*).

4.2 **Tax indemnity**

- (a) To the extent not paid by the Issuer, the Guarantor shall, within 10 calendar days from receipt of a demand in writing from the Trustee, pay to the Trustee an amount equal to the loss, liability or cost which it and/or the relevant Noteholder has suffered for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature in respect of payments under this Guarantee or the Trust Deed (other than the Notes) imposed, levied, collected, withheld or assessed by or on behalf of Ukraine or any political subdivision or any authority therein or thereof having power to tax.
- (b) Nothing in this Clause 4 shall oblige the Guarantor to pay or reimburse the Trustee for any taxes assessed on the Trustee under the law of a jurisdiction in which the Trustee is treated as resident for tax purposes if that tax is imposed on or calculated by reference to the net income received or receivable by the Trustee.

4.3 **Stamp taxes**

The Guarantor shall, within 10 calendar days from receipt of a demand in writing from the Trustee, pay and indemnify the Trustee against any liability it incurs in respect of any stamp, registration and similar tax which is or becomes payable in Ukraine in connection with the entry into, performance or enforcement of this Guarantee.

5. **PAYMENTS**

5.1 **Manner of payments**

- (a) On each date on which any sum is due from the Guarantor it shall make that sum available to the Trustee for value on the due date in same day freely transferable funds in accordance with the Trust Deed and the Agency Agreement.
- (b) Payment shall be made to the Trustee to such account notified by the Trustee from time to time for such purpose.

6. **INDEMNITIES**

6.1 **Currency indemnity**

If any sum due from the Guarantor under this Guarantee (a “**Sum**”), or any order, judgment or award given or made in relation to a Sum, has to be converted from the currency (the “**First Currency**”) in which that Sum is payable into another currency (the “**Second Currency**”) for the purpose of:

- (a) making or filing a claim or proof against the Guarantor;
- (b) obtaining or enforcing an order, judgment or award in relation to any litigation or arbitration proceedings,

the Guarantor shall, as an independent obligation and within thirty business days from receipt of a demand in writing from the Trustee, indemnify the Trustee against any cost, loss or liability arising out of or as a result of the conversion including any discrepancy between (A) the rate of exchange used to convert that Sum from the First Currency into the Second Currency and (B) the rate or rates of exchange available to that person at the time of its receipt of that Sum.

6.2 **Indemnities separate**

Each of the indemnities in this Guarantee constitutes a separate and independent obligation from the other obligations in this Guarantee, shall give rise to a separate and independent cause of action, shall apply irrespective of any time or other indulgence granted or agreed to be granted by the Trustee and shall continue in full force and effect despite any judgment, order, claim or proof for a liquidated amount in respect of any sum due under the Guarantee, Trust Deed and the Notes or any other judgment or order.

7. **SET-OFF**

The Trustee may, to the extent permitted by applicable law, set-off any matured obligation owed to it by the Guarantor under this Guarantee (to the extent beneficially owned by it) against any matured obligation owed by it to the Guarantor regardless of the place of payment, booking branch or currency of either obligation. If the obligations are in different currencies, the Trustee may convert either obligation in accordance with Clause 17(1) of the Trust Deed for the purpose of the set-off.

8. **CHANGES TO THE PARTIES**

8.1 **Changes to the Trustee**

The Trustee may assign its rights and obligations under this Guarantee if it is permitted to do so under, and subject to and in accordance with, the Trust Deed.

8.2 **Changes to the Guarantor**

The Guarantor may not assign any of its rights or transfer any of its rights or obligations under this Guarantee.

9. **REMEDIES AND WAIVERS**

No failure to exercise, nor any delay in exercising, any right or remedy under this Guarantee shall operate as a waiver, nor shall any single or partial exercise of any right or remedy prevent any further or other exercise or the exercise of any other right or remedy. The rights and remedies provided in this Guarantee are cumulative and not exclusive of any rights or remedies provided by law.

10. **NOTICES**

10.1 **Communications in writing**

Any communication to be made under or in connection with this Guarantee shall be made in writing and, unless otherwise stated, may be made by fax or letter.

10.2 **Addresses**

The address and fax number (and the department or officer, if any, for whose attention the communication is to be made) of each Party for any communication or document to be made or delivered under or in connection with this Guarantee is:

(a) in the case of the Guarantor:

The Cabinet of Ministers of Ukraine (acting on behalf of Ukraine) represented by the Minister of Finance of Ukraine
12/2 Grushevsky Street
Kyiv, 01008
Ukraine

Attention: Minister of Finance
Fax No.: +380 44 253 0023

- (b) in the case of the Trustee:
One Canada Square
London E14 5AL

Attention: Trustee Administration Manager
Fax No.: +44 020 7964 2536

or at such other address as shall have been notified (in accordance with this Clause) by the party in question by not less than five business days' notice to the other party hereto for the purposes of this Clause.

10.3 **Delivery**

Any notice sent by post as provided in this Clause shall be deemed to have been given, made or served 24 hours (in the case of inland post) or three days (in the case of overseas post) after despatch and any notice sent by facsimile transmission as provided in this Clause shall be deemed to have been given, made or served at the time of despatch provided that in the case of a notice or demand given by facsimile transmission a confirmation of transmission is received by the sending party and such notice or demand shall forthwith be confirmed by post. The failure of the addressee to receive such confirmation shall not invalidate the relevant notice or demand given by facsimile transmission.

10.4 **English language**

- (a) Any notice given under or in connection with this Guarantee must be in English.
- (b) All other documents provided under or in connection with this Guarantee must be:
- (i) in English; or
 - (ii) if not in English, accompanied by a English translation and, in this case, the English translation will prevail unless the document is a constitutional, statutory or other official document.

11. **PARTIAL INVALIDITY**

If, at any time, any provision in, or obligation under, this Guarantee is or becomes illegal, invalid or unenforceable in any respect under any law of any jurisdiction, neither the legality, validity or enforceability of the remaining provisions nor the legality, validity or enforceability of such provision under the law of any other jurisdiction will in any way be affected or impaired.

12. **COUNTERPARTS**

This Guarantee may be executed in any number of counterparts, and this has the same effect as if the signatures on the counterparts were on a single copy of this Guarantee and each of which shall be deemed an original.

13. **GOVERNING LAW AND JURISDICTION**

13.1 **Governing law**

This Guarantee and any non-contractual obligations arising out of or in connection with it are governed by English law

13.2 **English Courts**

Subject to Clause 13.3, the Courts of England shall have jurisdiction to settle any dispute arising out of or in connection with this Guarantee (including a dispute regarding the existence, validity or termination of this Guarantee or the consequences of its nullity) (a "**Dispute**"). The Parties agree that, subject to Clause 13.3, the Courts of England are the most appropriate and convenient courts to settle any Dispute and accordingly no Party will argue to the contrary. This Clause 13.2 is for the benefit of

the Trustee only. As a result, the Trustee may take proceedings relating to a Dispute in any other courts with jurisdiction. To the extent allowed by law, the Trustee may take concurrent proceedings in any number of jurisdictions.

13.3 **Arbitration**

At the option of any Party, a Dispute shall be settled by arbitration in accordance with the Rules of the London Court of International Arbitration as at present in force, with the exception of Article 6 which shall not apply, (the “**Rules**”) by a tribunal of three arbitrators (or a sole arbitrator if the Parties to the Dispute so agree) appointed in accordance with the Rules. If any Party elects for arbitration, the Parties shall take the steps necessary to terminate any court proceedings relating to the Dispute. The seat of any arbitration shall be London, England. The language of any arbitral proceedings shall be English. For the purposes of arbitration pursuant to this Clause 13.3, the Parties waive any right of application to determine a preliminary point of law or appeal on a point of law under sections 45 and 69 of the Arbitration Act 1996.

13.4 **Process agent**

The Guarantor irrevocably appoints the Ambassador of Ukraine to the United Kingdom of Great Britain and Northern Ireland at the Embassy of Ukraine in London to act as its authorised agent for service of process in England and agrees that failure by a process agent to notify the Guarantor of the process will not invalidate the proceedings concerned. Nothing in this Guarantee shall affect the right of the Trustee to serve process in any other manner permitted by law. The Guarantor irrevocably agrees not to contest or otherwise object to the validity of service of process in accordance with this Clause 13.4 on the ground of any immunity or inviolability of its Ambassador or any other member of its diplomatic or consular staff or of the premises of its diplomatic mission or consular post in the United Kingdom.

13.5 **Waiver of immunity**

To the extent that the Guarantor may in any jurisdiction claim for itself or its assets or revenues any immunity from suit, from measures to secure the recognition and/or enforcement of a judgment or an arbitral award, from attachment in aid of execution of judgment, from execution of a judgment or arbitral award, from enforcement of an arbitral award or from any other legal or judicial process or remedy (other than pre-judgment attachment which is expressly not waived), and to the extent that in any such jurisdiction there shall be attributed such an immunity, the Guarantor irrevocably waives such immunity under Ukrainian law and waives such immunity to the fullest extent permitted by the laws of any other jurisdiction. Such waiver of immunity constitutes only a limited and specific waiver by the Guarantor for the purposes of this Guarantee, the Notes or any related judgment or award and under no circumstances shall it be construed as a general waiver by the Guarantor or a waiver with respect to proceedings unrelated to this Guarantee or the Notes. The Guarantor reserves the right to plead sovereign immunity under the United States Foreign Sovereign Immunities Act of 1976 with respect to such actions brought against it under United States federal or state securities law. The Guarantor does not waive any immunity and/or inviolability in respect of (a) property used by a diplomatic or consular mission of Ukraine (except as may be necessary to effect service of process), (b) property of a military character and under the control of a military authority or defence agency or (c) property located in Ukraine and dedicated to a public or governmental use (as distinct to property dedicated to a commercial use).

This Guarantee has been executed as a deed by the Guarantor and is intended to be delivered on the date stated at the beginning of this Guarantee.

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PRINCIPAL OFFICE OF THE ISSUER

1, Sportyvna Ploscha
Kyiv
Ukraine

OFFICE OF THE GUARANTOR

Ministry of Finance of Ukraine
12/2 Grushevsky Street
Kyiv
Ukraine
Tel: +38 044 277 53 93

LEAD MANAGER

Morgan Stanley
20 Bank Street
Canary Wharf
London E14 4AD
United Kingdom

PRINCIPAL PAYING AGENT

The Bank of New York Mellon
One Canada Square
London E14 5AL
England

NEW YORK REGISTRAR

The Bank of New York Mellon, New York Branch
101 Barclay Street
New York
NY 10286
United States

EUROPEAN REGISTRAR

The Bank of New York Mellon (Luxembourg) S.A.
Vertigo Building
Polaris
2-4 rue Eugène Ruppert
L-2453 Luxembourg

PAYING AGENTS AND TRANSFER AGENTS

The Bank of New York Mellon
One Canada Square
London E14 5AL
England

The Bank of New York Mellon (Luxembourg) S.A.
Vertigo Building
Polaris
2-4 rue Eugène Ruppert
L-2453 Luxembourg

TRUSTEE

BNY Corporate Trustee Services Limited
One Canada Square
London E14 5AL
England

LEGAL ADVISERS

To the Guarantor as to English and U.S. law:

Linklaters LLP
One Silk Street
London EC2Y 8HQ
England

To the Guarantor as to Ukrainian law:

Magisters
38 Volodymyrska St.
Kyiv 01034
Ukraine

*To the Issuer as to
Ukrainian law:*

Andriy Kravets & Partners
38 Volodymyrska Street
Kyiv 01034
Ukraine

*To the Lead Manager and the Trustee as to English
and U.S. law:*

Clifford Chance LLP
10 Upper Bank Street
London
E14 5JJ
United Kingdom

To the Lead Manager as to Ukrainian law:

Salans LLC
49-A Volodymyrska Street
2nd Floor
Kyiv 01034
Ukraine

LISTING AGENT

Arthur Cox Listing Services Limited
Earlsfort Centre
Earlsfort Terrace
Dublin 2
Ireland