

Daily Insight

Hryvnia strengthens

Key messages of the today's comments

TUESDAY, 17 OCTOBER 2017

Domestic liquidity **2**

Liquidity continues to decline 2

Last Thursday, liquidity (excluding govt bonds) declined yet again following autonomous non-monetary operations of negative UAH1.81bn. An exchange of reserves into cash, of net UAH1.95bn to cash, was the maximum of this month and just UAH0.36bn less than the largest outflow seen in June. Other non-monetary operations were also negative, with UAH0.03bn in the Treasury, offset only by UAH0.18bn in funds. **2**

MoF will offer 5-year bonds today 2

Today, the MoF will hold its debut auction this month, after over one year, of offering 5-year bonds. The Ministry also will offer 11-month bonds with semi-annual coupon payments. **2**

Foreign exchange markets **3**

Hryvnia strengthens 3

At the end of the week, the hryvnia strengthened 0.4% against the greenback to 26.5380 USD/UAH. The weak US dollar and decreasing banking sector liquidity (see comment on liquidity) fed into the hryvnia's strength. At the same time, upcoming month-end tax payments should increase demand for the hryvnia. On Friday, in the Ukrainian cash market, it sold for 26.63 USD/UAH versus 26.81 to buy. Its CPI-based real trade-weighted index rose 0.04% to 105.13; in year-on-year terms, it is up 1.89% from 103.18 last year. **3**

Appendix #1: Domestic liquidity **4**

Ukraine's hryvnia exchange rate per US dollar (three months through 13 October 2017)



Source: Bloomberg.

Selected indicators of the financial markets (three months through 13 October 2017)

| | Last | Daily chg (%) | YTD chg (%) |
|---|----------|---------------|-------------|
| DOMESTIC LIQUIDITY | | | |
| NBU key policy rate (%) | 12.50 | +0bp | -150bp |
| Overnight rate (interbank) | 11.60 | +10bp | +100bp |
| Banks reserves (UAHm) | 48,648 | -1.73 | -2.18 |
| Deposit certificates* (UAHm) | 25,577 | -3.58 | -58.91 |
| FOREIGN EXCHANGE MARKET | | | |
| UAH per US dollar | 26.5200 | -0.28 | -2.14 |
| Total trade volume (US\$m) | N/A | | |
| UAH index CPI-based | 105.132 | +0.04 | -2.66 |
| UAH index PPI-based | 162.033 | +0.04 | -3.77 |
| UKRAINE SOVEREIGN EUROBOND MARKET | | | |
| CDS 5yr | 454bp | +4bp | -199bp |
| GLOBAL FINANCIAL MARKET INDICATORS | | | |
| S&P 500 | 2,557.64 | +0.18 | +14.24 |
| MSCI EM | 1,125.91 | +0.38 | +30.58 |
| US dollar index (DXY) | 93.091 | +0.04 | -8.92 |
| EUR / USD | 1.1820 | -0.08 | +12.39 |
| Crude oil WTI (US\$/bbl) | 51.45 | +1.68 | -4.23 |
| Crude oil BRENT (US\$/bbl) | 57.17 | +1.64 | +0.62 |
| CRB, commodities index | 184.83 | +0.85 | -3.99 |
| Gold (US\$/ounce) | 1,304.57 | +0.84 | +13.22 |

Notes: * NBU's short-term bonds.

Source: Bloomberg, ICU.

Domestic liquidity

Liquidity continues to decline

Last Thursday, liquidity (excluding govt bonds) declined yet again following autonomous non-monetary operations of negative UAH1.81bn. An exchange of reserves into cash, of net UAH1.95bn to cash, was the maximum of this month and just UAH0.36bn less than the largest outflow seen in June. Other non-monetary operations were also negative, with UAH0.03bn in the Treasury, offset only by UAH0.18bn in funds.

Fund outflows were divided between reserves and CDs, as some banks used CD redemptions to offset outflows from reserves. Banks' correspondent accounts balance with the NBU declined UAH0.86bn while total CDs outstanding fell UAH0.95bn.

ICU view: The Treasury is keeping its operational balance close to zero these days, which under current conditions support the decline in liquidity. This week, liquidity should recover prior to month-end tax payments, but it could fall below UAH70bn.

MoF will offer 5-year bonds today

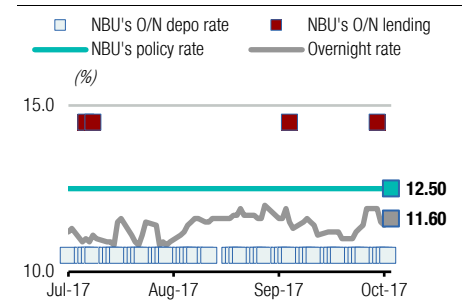
Today, the MoF will hold its debut auction this month, after over one year, of offering 5-year bonds. The Ministry also will offer 11-month bonds with semi-annual coupon payments.

The 11-month bond was last offered in September at a 14.35% cut-off rate and YTM of 14.91%. 5-year bonds were sold last September at interest rates above 16%; however, this year the NBU decreased its key monetary rate several times and yields for govt bonds also declined.

ICU view: After a long break from offering 5-year bonds, there could be significant demand for them today, mostly from primary dealers' clients rather than from banks, as insurance companies and pension funds could be quite interested in these bonds. Most important will be the interest rates in bids and the MoF's view on the cut-off level. As 3-year bonds last time were issued at 14.50%, demand for 5-year bonds could be concentrated at above 15%.

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Interest rates in the banks' reserves market (three months through 13 October 2017)



Source: Bloomberg, ICU.

Key indicators (as of 13 October 2017)

| | Last | Daily | Weekly | Monthly | YTD |
|---|----------------|--------------|--------------|--------------|---------------|
| | chg (%) | chg (%) | chg (%) | chg (%) | chg (%) |
| BANKS' RESERVES MARKET (%) | | | | | |
| NBU rate ¹ | 12.50 | +0bp | +0bp | +0bp | -150bp |
| ON rate | 11.60 | +10bp | -30bp | -30bp | +100bp |
| ON \$ swap | N/A | N/A | N/A | N/A | N/A |
| DOMESTIC LIQUIDITY (UAH MILLION) | | | | | |
| Reserves ² | 48,648 | -1.73 | +10.31 | +3.65 | -2.18 |
| DepCerts ³ | 25,577 | -3.58 | -20.05 | -14.15 | -58.91 |
| Total | 74,225 | -2.38 | -2.45 | -3.26 | -33.71 |
| BREAKDOWN OF GOVT BOND HOLDERS (UAH MILLION) | | | | | |
| NBU | 360,573 | +0.00 | +0.00 | -0.80 | +1.24 |
| Banks | 308,491 | +0.04 | -0.28 | +0.78 | +79.00 |
| Residents | 23,484 | +0.03 | +0.26 | +0.46 | +49.78 |
| Non-res ⁴ | 3,042 | +8.29 | +8.66 | +65.89 | -52.10 |
| Total | 695,590 | +0.05 | -0.08 | +0.12 | +26.35 |
| IMPLIED YIELDS OF THE UAH NDF MARKET (%) | | | | | |
| 1 month | 11.84 | -38bp | -3bp | +35bp | -10ppt |
| 3 months | 12.49 | +33bp | +0bp | +47bp | -957bp |
| 6 months | 12.16 | +1bp | +3bp | +8bp | -588bp |
| 1 year | 11.74 | +9bp | +8bp | +9bp | -425bp |
| UKRAINE SOVEREIGN EUROBOND MARKET | | | | | |
| CDS 5yr | 454 | +4bp | -3bp | +9bp | -199bp |

Notes: [1] NBU's key policy rate; [2] stock of banks' reserves held at NBU; [3] stock of NBU's short-term bonds; [4] non-residents.

Source: Bloomberg, ICU.

Foreign exchange markets

Hryvnia strengthens

At the end of the week, the hryvnia strengthened 0.4% against the greenback to 26.5380 USD/UAH. The weak US dollar and decreasing banking sector liquidity (see comment on liquidity) fed into the hryvnia's strength. At the same time, upcoming month-end tax payments should increase demand for the hryvnia. On Friday, in the Ukrainian cash market, it sold for 26.63 USD/UAH versus 26.81 to buy. Its CPI-based real trade-weighted index rose 0.04% to 105.13; in year-on-year terms, it is up 1.89% from 103.18 last year.

The USD weakened on Friday after US consumer prices rose less than expected in September. However, thanks to solid macroeconomic data, the US dollar traded slightly higher against other major currencies on Monday. The Empire State Manufacturing Index surged in October more than expected to 30.20, the best reading in three years. At the same time, the president of the Boston Fed stated that the Federal Reserve should hike the Fed funds rate in December. The DXY index rose 0.2% to 93.312 on Monday.

The euro remains under influence of the Spanish constitutional crisis as the Catalan leader did not clarify his position regarding independence as requested by Spanish Prime. On the other hand, the Eurozone current account surplus fell EUR1.4bn year-on-year in August to EUR16.1bn, putting additional pressure on the euro. On Monday, it weakened 0.2% to 1.1796 EUR/USD.

On the back of the USD's strength, the Chinese renminbi weakened 0.15% to 6.5898 USD/CNY. It remained stronger than the 6.6 USD/CNY seen last week, as investors anticipate the start of the Chinese communist party congress scheduled for 18 October. The Russian ruble was under the influence of two opposing factors -- rising oil prices, which traditionally support the Russian currency, and the stronger US dollar. Having strengthened in the first half of Monday, the ruble trimmed gains by the end of the trading session as the impact of the stronger USD outweighed rising oil prices. It closed up 0.1% to 57.2693 USD/RUB.

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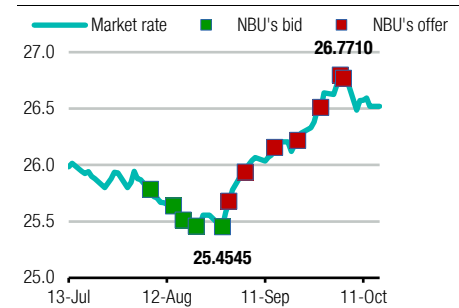
Readers may follow the ICU trade-weighted indices of the local-currency, the hryvnia (UAH), on the ICU [website](#).

Key indicators (as of 13 October 2017)

| | Last | Daily | Weekly | Monthly | YTD |
|---|----------|---------|---------|---------|---------|
| | chg (%) | chg (%) | chg (%) | chg (%) | chg (%) |
| EXCHANGE RATES (PER US DOLLAR, EXCEPT EURO, POUND) | | | | | |
| UAH | 26.5200 | -0.28 | -0.90 | +1.65 | -2.14 |
| USD ¹ | 93.091 | +0.04 | -0.76 | +0.62 | -8.92 |
| EUR | 1.1820 | -0.08 | +0.77 | -0.55 | +12.39 |
| JPY | 111.8200 | -0.41 | -0.74 | +1.20 | -4.39 |
| GBP ² | 1.3285 | +0.17 | +1.68 | +0.56 | +7.66 |
| CNY | 6.5796 | -0.12 | -1.10 | +0.58 | -5.26 |
| RUB | 57.3410 | -0.65 | -1.38 | -1.03 | -6.82 |

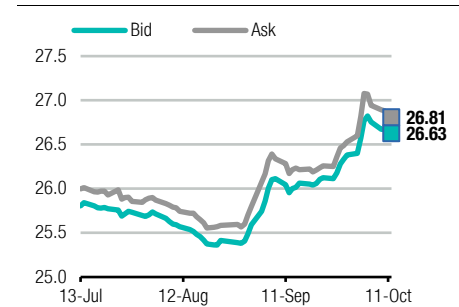
Notes: [1] DXY, US dollar index; [2] British pound.
Source: Bloomberg, ICU.

Ukraine hryvnia UAH exchange rate per US dollar at the interbank market (three months through 13 October 2017)



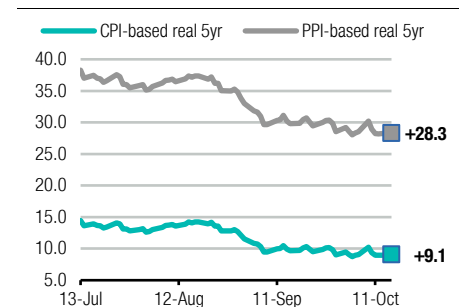
Notes: the chart provides labels for the average exchange rate at last two NBU auctions (one on buying FX from the market and one on selling it). Source: NBU, Bloomberg, ICU.

Ukraine hryvnia UAH exchange rate per US dollar at the cash market (three months through 13 October 2017)



Source: NBU.

UAH exchange rate misalignment¹ from fundamental level² (%) (three months through 13 October 2017)



Notes: [1] "+" overvalued, "-" undervalued; [2] based on the UAH's CPI- and PPI-based real TWIs. Source: ICU.

Appendix #1: Domestic liquidity

Chart 1. Banks reserves usages over last reporting date (UAHm)

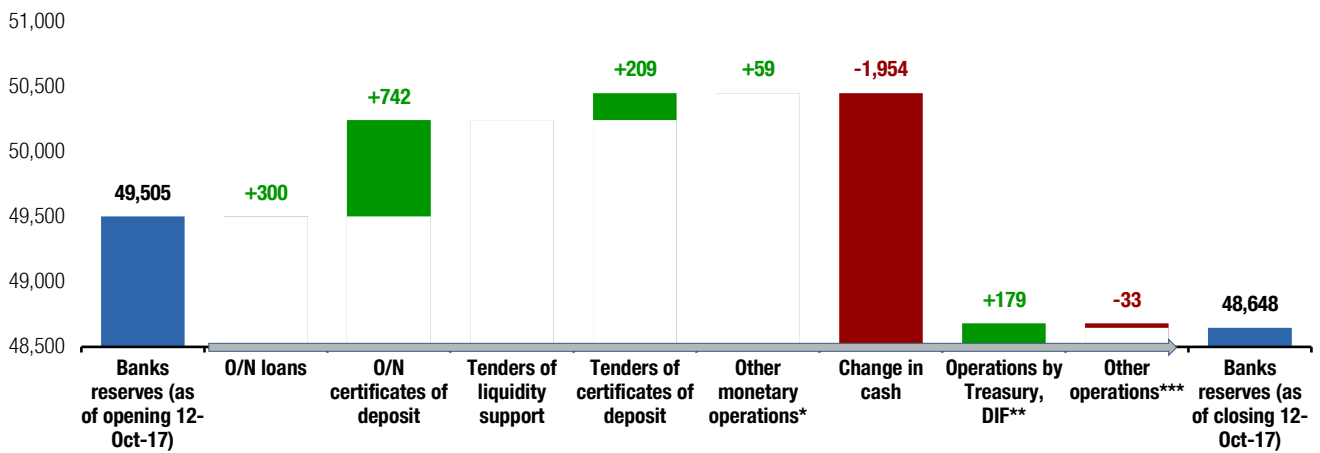
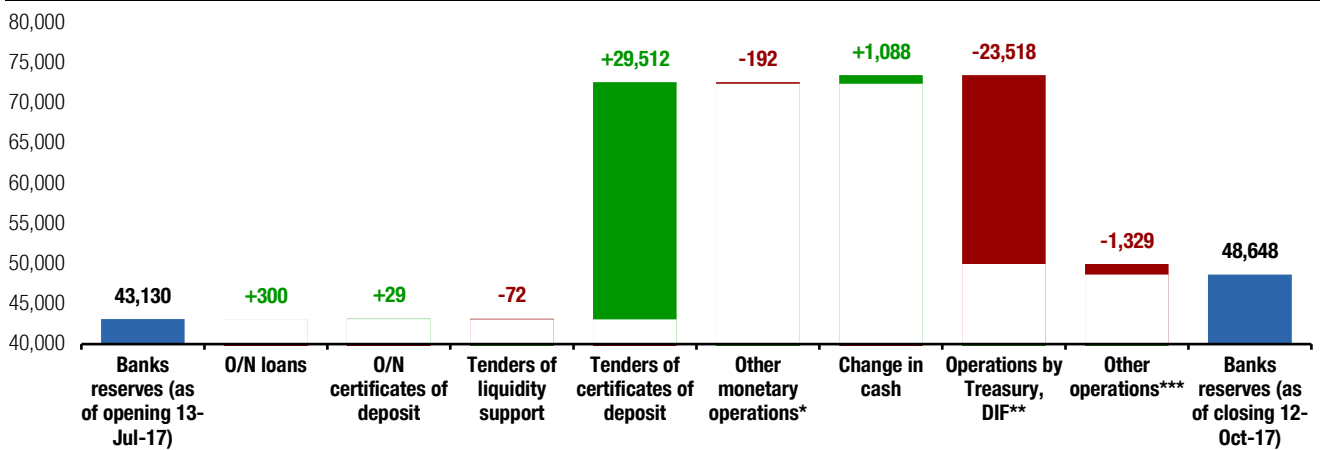
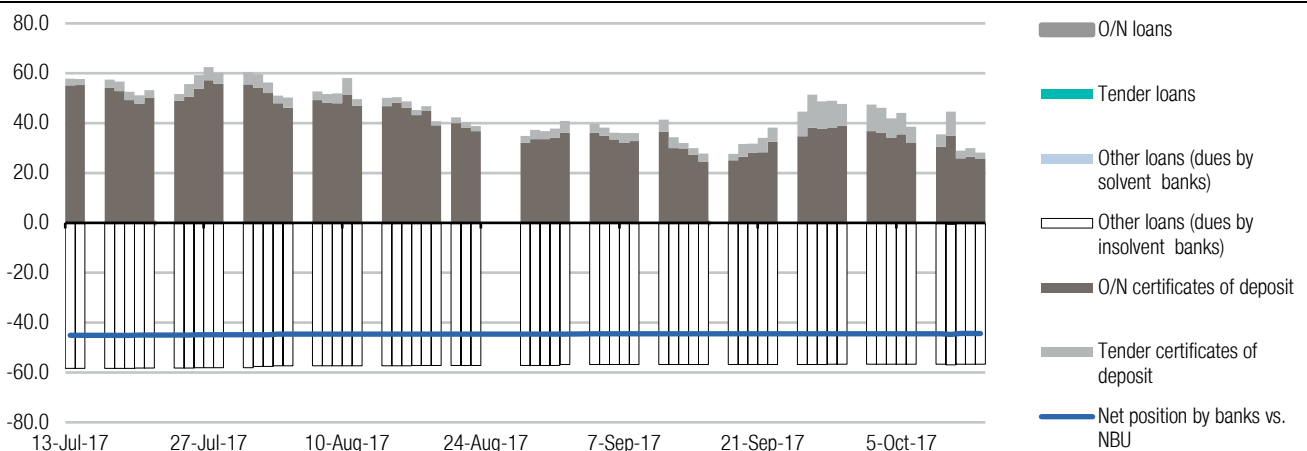


Chart 2. Banks reserves usages over last 90-day period (UAHm)



Notes: [1] data from the NBU's daily reporting https://bank.gov.ua/control/uk/publish/article?art_id=38643651&cat_id=40807142 ;
 * operations repo, purchase and sale of government bonds, FX market interventions, stabilisation loans, FX swap agreements; ** DIF – deposit insurance fund;
 *** interest payments on NBU's loans and on NBU's certificates of deposit, other operations. Source: NBU, ICU.

Chart 3. Stocks of NBU's monetary instruments and net position by banks versus NBU (UAHbn)



Source: NBU, ICU.

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