

Weekly Insight

Inflation slows to 9% YoY in June

Key messages of the today's comments

Domestic liquidity and bonds market

Foreigners increased market share to 8.5%

Foreign investors increased their share in government bonds outstanding to 8.5%, extending portfolios to above UAH65bn (US\$2.5bn). This week, we anticipate a further increase in holdings, but at a bit slower pace.

Liquidity stays above UAH100bn

Thanks to NBU's purchase of FX and an increase in budget expenditures, liquidity remained above UAH100bn. We do not expect it to decline below this level this week.

Foreign exchange market

Jitters for the hryvnia leading up to elections

Last week, the hryvnia beat the record of previous week, but due to coming Parliamentary elections this Sunday, it slightly weakened, losing 0.3%. This week, we expect weakening to continue. We could see the hryvnia moving above UAH26/US\$.

Economics

Inflation slows to 9% YoY in June

Tight monetary and a restrictive fiscal policy, as well as lower world energy prices will contribute to the further slowdown of inflation.

MONDAY, 15 JULY 2019

Banks' reserves market (12 July 2019)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	17.50	+0bp	+0bp
ON rate (%)	16.13	-60bp	+23bp
ON \$ swap (%)	14.07	+51bp	-106bp
Reserves (UAHm) ²	63,189	+68.05	+13.87
DepCerts (UAHm) ³	44,316	-27.43	-21.66

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

Source: NBU, Bloomberg, ICU.

Breakdown of govt bond holders (UAHm) (12 July 2019)

	Last	Weekly chg (%)	YoY chg (%)
NBU	337,088	+0.00	-3.78
Banks	329,258	-4.38	-6.98
Residents	23,055	-0.84	+6.81
Individuals	8,817	-1.63	+157.50
Non-res ⁴	65,162	+8.31	+552.17
Total	763,380	-1.35	+3.25

Notes: [1] non-residents

Source: NBU, ICU.

FX market indicators (12 July 2019)

	Last	Weekly chg (%)	YTD chg (%)
USD/UAH	25.7600	+0.32	-1.75
EUR/USD	1.1270	+0.40	-3.44
DXY ²	96.810	-0.49	+2.09
UAH TWI ³	125.740	-0.64	+4.83

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

Gov't bond quotes¹ (15 July 2019)

Maturity	Bid	Ask
6m	19.00	18.25
12m	19.25	18.15
2y	19.25	18.00
3y	19.00	17.00
12m (\$)	7.50	6.00
2y (\$)	7.90	6.50

Notes: [1] Actual quotes you can see at www.icu.ua.

Source: ICU.

Domestic liquidity and bonds market

Foreigners increased market share to 8.5%

Foreign investors increased their share in government bonds outstanding to 8.5%, extending portfolios to above UAH65bn (US\$2.5bn). This week, we anticipate a further increase in holdings, but at a bit slower pace.

Last week, foreign investors added UAH3.5bn (US\$136m) to their portfolios. Portfolios grew due to offerings at last week’s auction including the three-year and six-year notes, which are the most attractive for foreigners. The share of local-currency bills in this portfolio rose to 97.7%, as USD-denominated bills were redeemed last week, and this category of investors received UAH0.4bn (US\$15m) of redemptions.

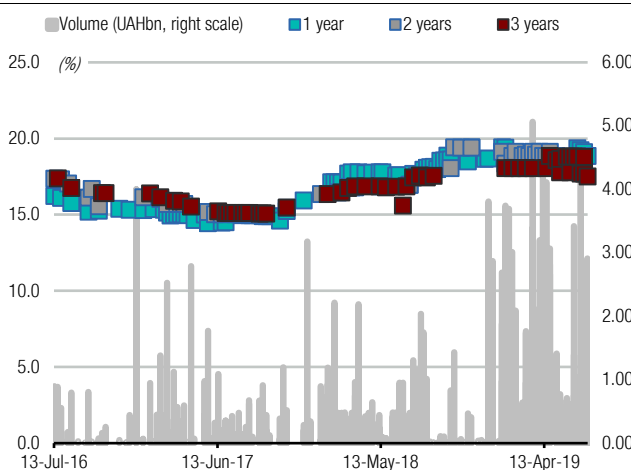
After last week’s redemption of FX-denominated bills, banks’ portfolios declined to UAH329bn (US\$12.8bn), with their share in total bonds outstanding declining to 43.1%. This made the NBU once again the largest bondholder with 44.2% in total outstanding.

ICU view: As the MoF is scheduled to offer bills with maturities of up to two years, foreign investor’s participation in this week’s auction is likely to be lower than last week. We expect a decline in demand for UAH-denominated bills, with demand moving to USD-denominated paper, which will be offered for the first time this month. As a result, we expect foreigners’ portfolios will continue to rise, but less significantly compared with the two previous weeks.

Taras Kotovych, Kyiv, (044) 377-7040 ext.724

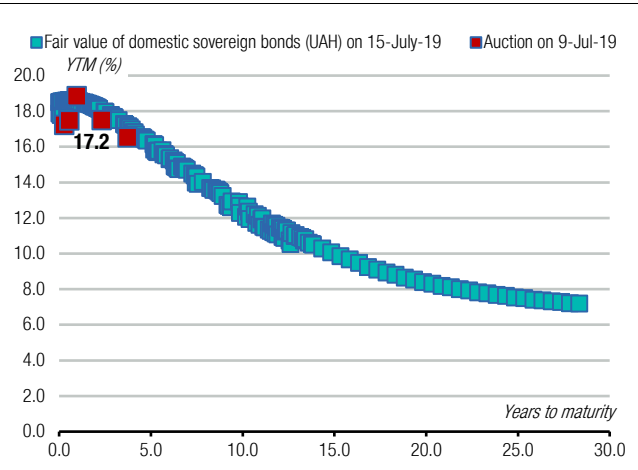
Chart 1. Local-currency bonds

Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)



Source: Ministry of Finance of Ukraine, ICU.

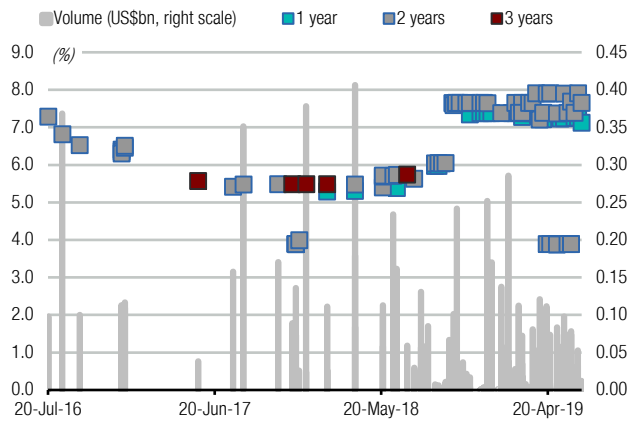
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: National Bank of Ukraine, Ministry of Finance of Ukraine, ICU.

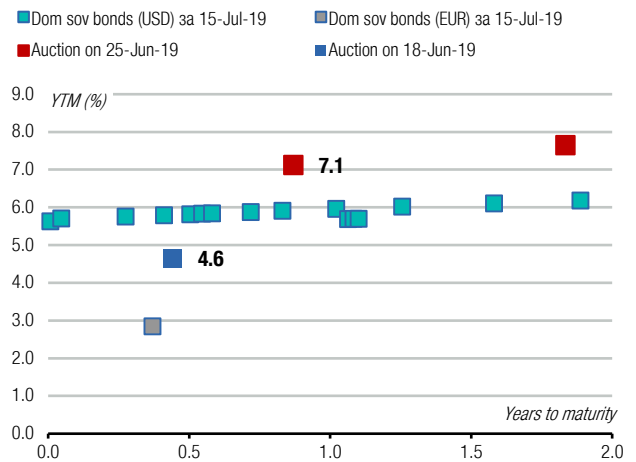
Chart 2. FX-denominated bonds

Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)



Source: Ministry of Finance of Ukraine, ICU.

Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: National Bank of Ukraine, Ministry of Finance of Ukraine, ICU.

Liquidity stays above UAH100bn

Thanks to NBU's purchase of FX and an increase in budget expenditures, liquidity remained above UAH100bn. We do not expect it to decline below this level this week.

Last week, the NBU was quite active in the FX market, but purchasing lower amounts than a week before. With these transactions, the NBU provided banks with UAH3.5bn. Through non-monetary operations, liquidity received UAH3bn, including inflows from the Treasury via budget expenditures of UAH6.5bn, which fully compensated outflows via reserves exchange in cash, which amounted to UAH4.3bn.

ICU view: We do not expect significant volatility in liquidity this week. Most likely, it will be above UAH100bn at the end of the week. The NBU will support liquidity slightly, while the main impact will come from the Treasury's budget operations.

Taras Kotovych, Kyiv, (044) 377-7040 ext.724

Chart 3. Banks reserves usages over last week(UAHm)

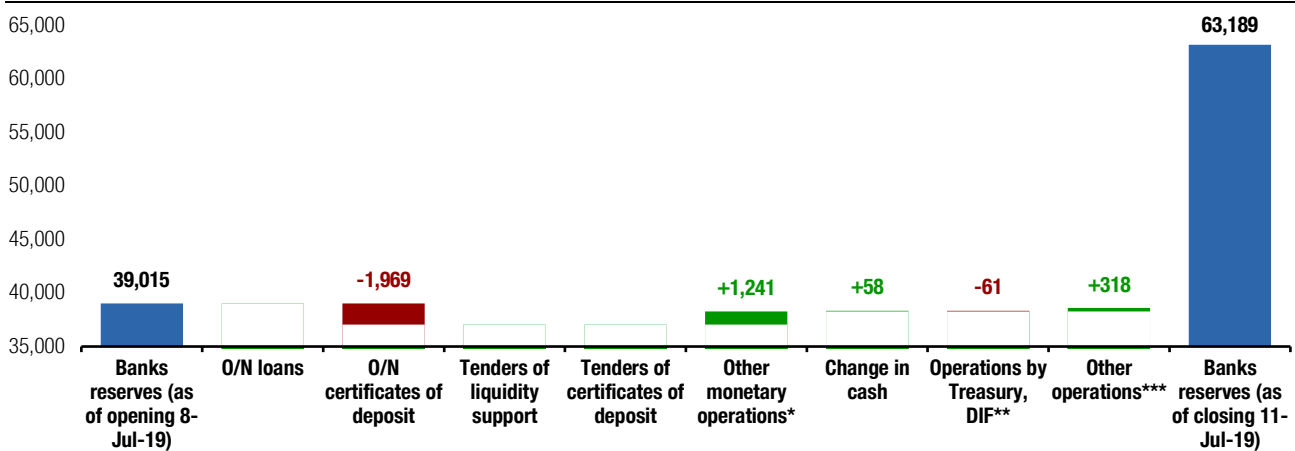
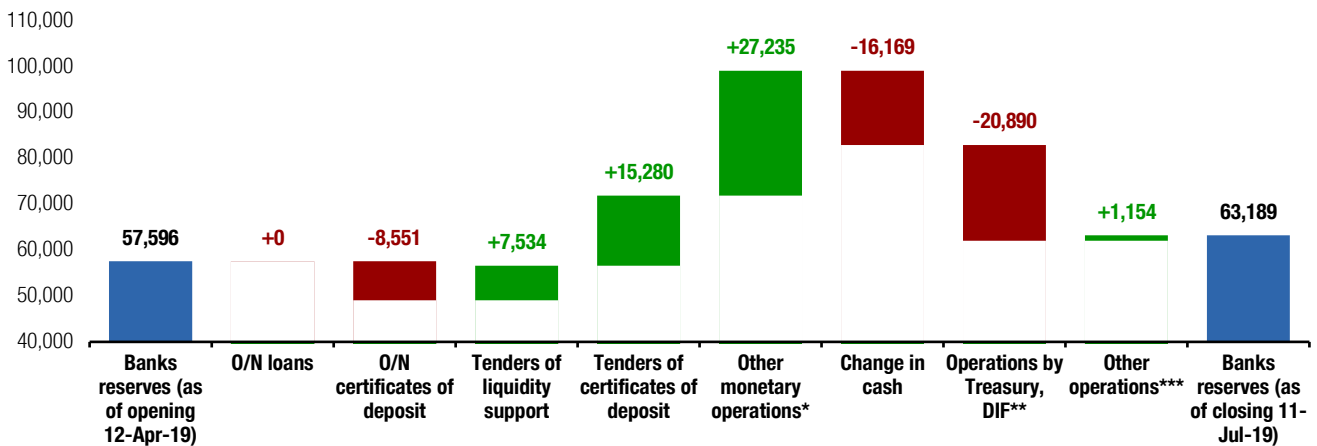


Chart 4. Banks reserves usages over last 90-day period (UAHm)


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.

Foreign exchange market

Jitters for the hryvnia leading up to elections

Last week, the hryvnia beat the record of previous week, but due to coming Parliamentary elections this Sunday, it slightly weakened, losing 0.3%. This week, we expect weakening to continue. We could see the hryvnia moving above UAH26/US\$.

Inflows of FX two weeks to prior elections have been lower, and the NBU decreased amounts of FX purchases to US\$138m from US\$321m a week before. As a result, the hryvnia set a new record for the last two years reaching UAH25.59/US\$, but later weakened to UAH25.76/US\$ at the end of last week.

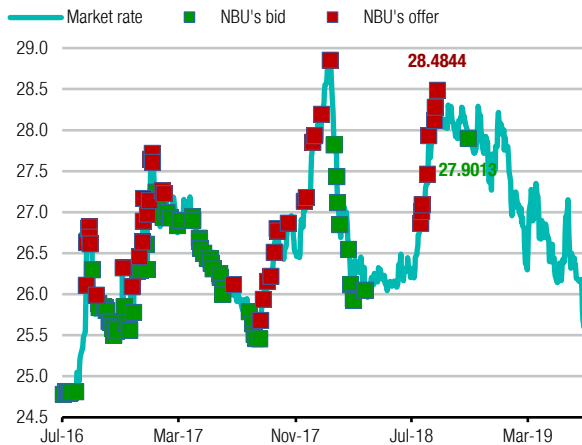
Foreign investors' participation in the bond market was less active and a lower supply of FX from these investors was not compensated by domestic sources. With only a week to elections, domestic players are likely to keep FX, in order to decrease devaluation risks.

ICU view: This week, foreign investors will purchase fewer new bills, so the supply of FX will be lower. This will have negative impact on the demand side. As a result, we expect further weakening of the hryvnia to or above UAH26/US\$.

Taras Kotovych, Kyiv, (044) 377-7040 ext.724

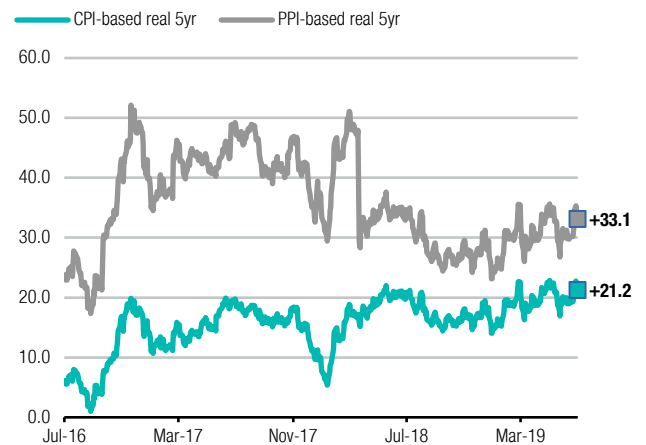
Chart 5. FX market indicators, 3-year history

Ukraine hryvnia UAH exchange rate per US dollar at the interbank market



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.

UAH exchange rate misalignment¹ from fundamental level² (%)



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

Economics

Inflation slows to 9% YoY in June

Tight monetary and a restrictive fiscal policy, as well as lower world energy prices will contribute to the further slowdown of inflation.

In June, headline inflation slowed to 9% YoY, down from 9.6% YoY seen in May, while in MoM terms, prices fell 0.5%. The greatest contribution to the inflation slowdown came from food products (+8.5% YoY), which account for 45% of the consumer basket. Most of the other categories posted a decline in price growth rates except for healthcare, and recreation and culture. Core inflation holds steady at 7.4% YoY for the third consecutive month. The NBU forecasts headline CPI at 6.3% YoY by the end of 2019, but may update its forecasts in new its inflation report on 25 July.

ICU view: Solid consumer demand, the shifting of some costs onto final customers due to further growth of wages, and higher cost of sowing this year will continue inflationary pressure. However, given lower-than-expected world energy prices as well as still tight monetary and a restrictive fiscal policy, we improve our inflation forecast to 8% by YE2019 vs. previously expected 8.5%.

Dmytro Dyachenko, Kyiv, (044) 377-7040 ext.738

This page is intentionally left blank



11th floor, LEONARDO Business Centre
19-21 Bogdan Khmelnytsky Street
Kyiv, 01030 Ukraine
Phone/Fax +38 044 3777040

WEB www.icu.ua



INVESTMENT ADVISORY

Makar Paseniuk, CFA, Managing Partner
makar.paseniuk@icu.ua

Ivan Shvydanenko, Director
ivan.shvydanenko@icu.ua

Roman Nikitov, ACCA Director
roman.nikitov@icu.ua


Yuriy Kamarytskyi, Vice President
yuriy.kamarytskyi@icu.ua

Ruslan Kilmukhametov, Director
ruslan.kilmukhametov@icu.ua


Ruslan Patlavsky, Director
ruslan.patlavsky@icu.ua

ASSET MANAGEMENT

Grigoriy Ovcharenko, Director
Head of Local Asset Management
grigoriy.ovcharenko@icu.ua

Liliya Kubytovych 
Head of Marketing and Sales
liliya.kubytovych@icu.ua


TRADE OPERATIONS

Konstantin Stetsenko 
Managing Partner
konstantin.stetsenko@icu.ua

Vlad Sinani, Director
Strategy and Business Development
vlad.sinani@icu.ua


Sergiy Byelyayev
Head of Fixed-Income Trading
sergiy.byelyayev@icu.ua

Yevgeniya Gryshchenko
Head of Brokerage Services Department
yevgeniya.gryshchenko@icu.ua

Vitaliy Sivach 
Trader, Fixed-Income & Forex
vitaliy.sivach@icu.ua


Bogdan Vorotilin 
bogdan.vorotilin@icu.ua

RESEARCH

Alexander Martynenko 
Head of corporate research
alexander.martynenko@icu.ua

Dmitriy Dyachenko
Junior financial analyst
dmitriy.dyachenko@icu.ua

Taras Kotovych 
Senior financial analyst (Sovereign debt)
taras.kotovych@icu.ua

Mykhaylo Demkiv 
Financial analyst (Banks)
mykhaylo.demkiv@icu.ua

Investment Capital Ukraine LLC is regulated by Securities and Stock Market State Commission of Ukraine (license numbers: dealer activity AE 263019, broker activity AE 263018, underwriting activity AE 263020 dated 11 April 2013).

DISCLAIMER

This research publication has been prepared by Investment Capital Ukraine LLC solely for information purposes for its clients. It does not constitute an investment advice or an offer or solicitation for the purchase or sale of any financial instrument. While reasonable care has been taken to ensure that the information contained herein is not untrue or misleading at the time of publication, Investment Capital Ukraine makes no representation that it is accurate or complete. The information contained herein is subject to change without notice. Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of Investment Capital Ukraine LLC. All rights are reserved. Any investments referred to herein may involve significant risk, are not necessarily available in all jurisdictions, may be illiquid and may not be suitable for all investors. The value of, or income from, any investments referred to herein may fluctuate and/or be affected by changes in exchange rates. Past performance is not indicative of future results. Investors should make their own investigations and investment decisions without relying on this report. Only investors with sufficient knowledge and experience in financial matters to evaluate the merits and risks should consider an investment in any issuer or market discussed herein and other persons should not take any action on the basis of this report.

Additional information is available upon request.

