

Bond Market Insight

Steep peak in yields continues

Comment on government bond placement

Tuesday's auction, which was two days before the NBU key policy rate revision and a few days after November's reported inflation rate, saw large demand and provided the state budget with a lower cost of financing.

Demand was, as usual, concentrated in the longer maturities, the 2.6-year and four-year. Together, these notes received UAH13.4bn or 96% of total demand for the auction. The longer, the four-year note, received UAH11.4bn of demand or 81% of total demand. Certainly, it had a significant impact on the decline in interest rates.

Table 1. Details of domestic government bonds placed at the auction (UAHbn)

ISIN	Coupon rate (%)	Payment freq ¹	Maturity	Qty of bonds sold	Price (UAH)	Proceeds ² (UAHm)	Volume ² (UAHm)	YTM ³ (%)	Outstanding (m) ⁴
UA4000202469	17.25	SA	30-Sep-20	212,940	1,064.15	226.60	212.94	13.46	5,940.99
UA4000204572	16.06	SA	3-Aug-22	1,000,000	1,144.79	1,144.79	1,000.00	12.41	6,695.97
UA4000206460	11.67	SA	22-Nov-23	3,000,000	1,004.40	3,013.19	3,000.00	12.04	3,000.00
Total UAH				4,212,940	4,384.58	4,212.94			15,636.96

Note: [1] payment frequency abbreviations: M - monthly, Qtly - quarterly, SA - semi-annually, @Mty - at maturity date; [2] proceeds and volumes for the USD-denominated bonds are calculated based on the previous day's exchange rate 23.93/USD, 29.6/EUR; [3] yields on coupon-bearing bonds are effective yields to maturity. Sources: Ministry of Finance of Ukraine, Bloomberg, ICU.

Demand for five-month bills was low and was rejected due to quite high interest rates. But for 10-month bills, the MoF likely accepted one competitive bid and all non-competitive bids, receiving just UAH226m of proceeds. Cut-off and weighted-average rates were decreased by 75bp and 74bp respectively, compared with the auction a month ago.

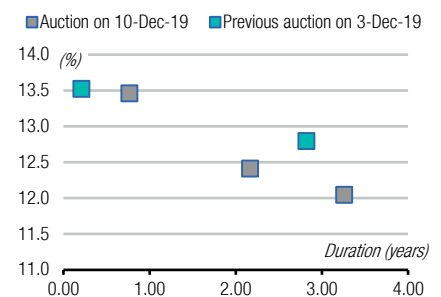
For paper with a 2.6-year maturity, half of demand was accepted, and compared with the three-year notes sold in November, the cut-off rate was down 107bp to 12.05% and weighted-average rate by 106bp to 12.01%.

Rates for the four-year note were also slightly reduced. Compared with last week's 3.5-year notes, the cut-off rate was reduced by 80bp, and compared with the four-year note placement two weeks ago by 94bp. The weighted-average rate was decreased by 71bp compared with last week's auction. Of note, yesterday was the first time in the last four years that interest rates for local-currency paper declined below 12%.

Large demand and low caps caused the significant decline in interest rates, which is

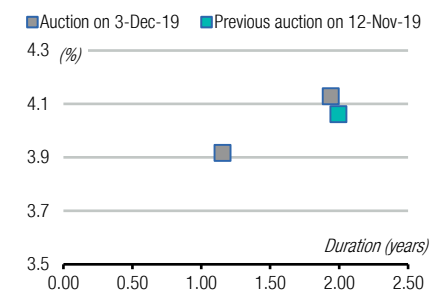
THURSDAY, 12 DECEMBER 2019

UAH-denominated domestic gov't bonds: yield curve in past two auctions



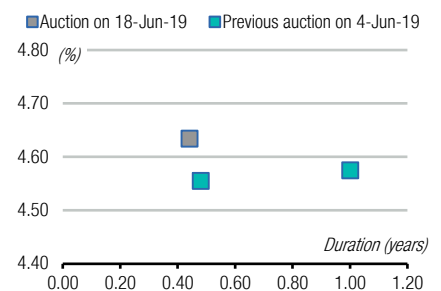
Source: Ministry of Finance of Ukraine, ICU.

USD-denominated domestic gov't bonds: yield curve in past two auctions



Source: Ministry of Finance of Ukraine, ICU.

EUR-denominated domestic gov't bonds: yield curve in past two auctions



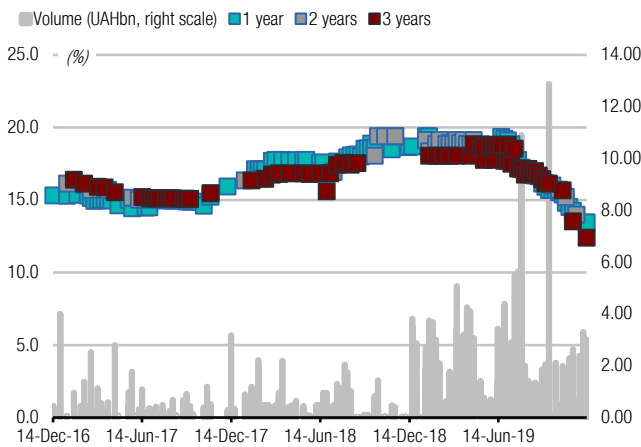
Source: Ministry of Finance of Ukraine, ICU.

faster than NBU key policy rate decline. Currently, with inflation low at 5.1% and significant expectations of a sharp decline in the NBU key policy rate, demand at low rates was justified, but may subsequently lead to increased risks in attracting necessary budget financing.

Appendix: Yields-to-maturity, repayments

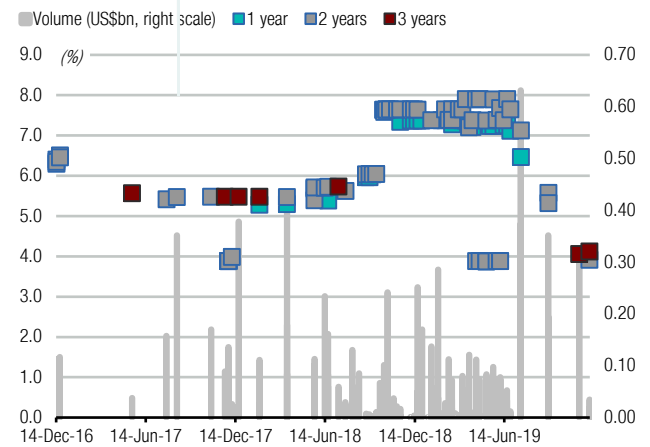
Chart 1. Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

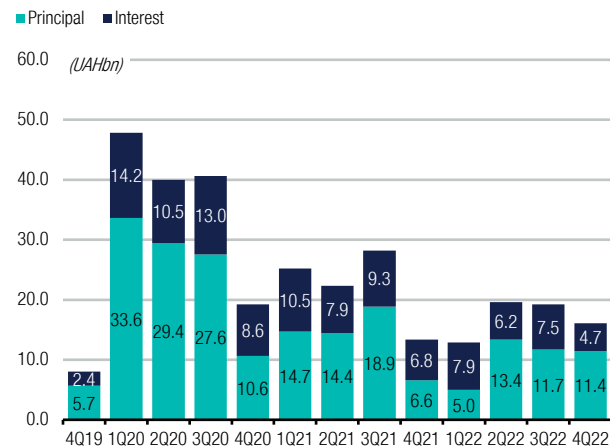
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

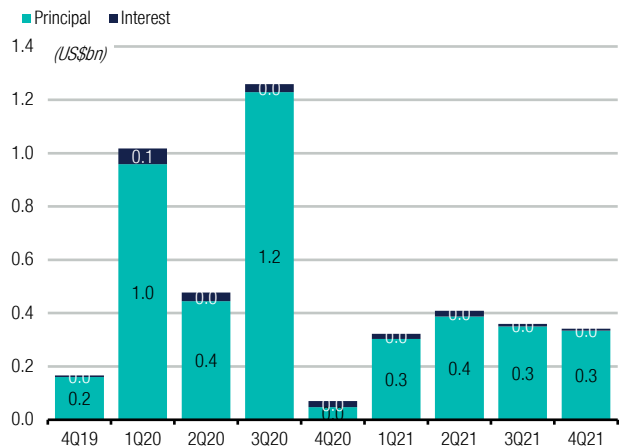
Chart 2. Future repayments on domestic government bonds (in billions of currency)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

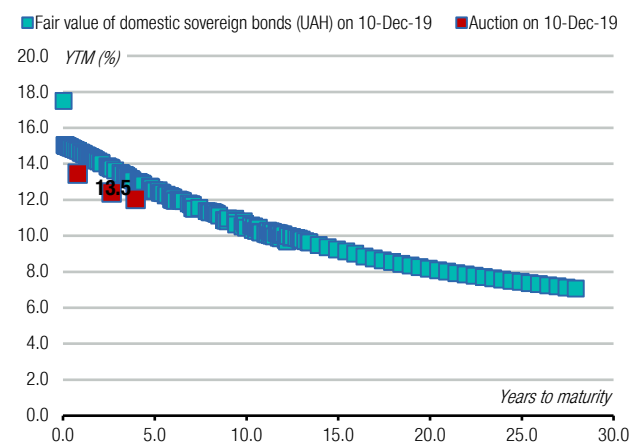
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

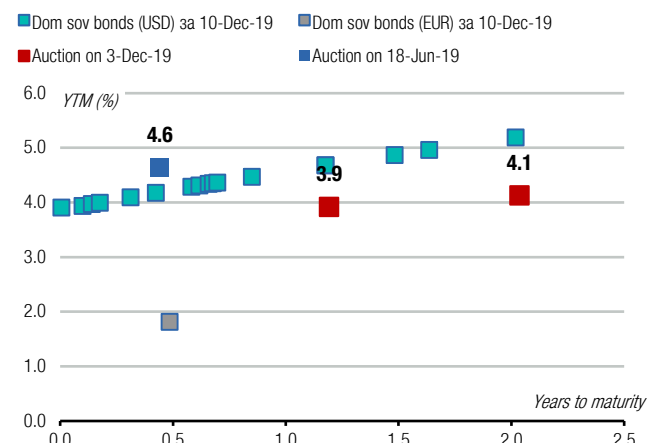
Chart 3. Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions

UAH-denominated domestic government bonds



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

USD- and EUR-denominated domestic government bonds



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

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

WEB www.icu.ua



RESEARCH

Alexander Martynenko

Head of corporate research
alexander.martynenko@icu.ua

Mykhaylo Demkiv

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

Taras Kotovych

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

Dmitriy Dyachenko

Junior financial analyst
dmitriy.dyachenko@icu.ua

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