

# Weekly Insight

## IMF completes first review of Stand-by Programme

### Key messages of the today's comments

#### Domestic liquidity and bonds market

##### Borrowing becoming more expensive

Last week, the Ministry of Finance again raised interest rates on UAH-denominated bonds, which attracted non-bank investors, but has not yet attracted foreigners. Demand may increase this week due to reinvestment of redemptions, but domestic investors are likely to prevail again.

#### Foreign exchange market

##### The hryvnia continues to weaken

Demand for hard currency remains high, and even increased compared with previous weeks, but the supply of hard currency is not enough to satisfy such increased demand. Therefore, the hryvnia continued to weaken last week and may weaken further this week, gradually finding a balance in the range of UAH27–27.5 UAH/US\$.

#### Economics

##### IMF completes first review of Stand-by Programme after a delay of more than a year

The IMF Board of Directors approved the first review of Ukraine's Stand-by Programme last week. The review comes after a delay of more than one year relative to the initial schedule. The IMF also agreed to extend the Stand-by Programme that was scheduled to end this year by another six months until June 2022.

MONDAY, 29 NOVEMBER 2021

#### Banks' reserves market (26 November 2021)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) <sup>1</sup>	8.50	+0bp	+250bp
ON rate (%)	7.85	-4bp	+223bp
ON \$ swap (%)	N/A	...	...
Reserves (UAHm) <sup>2</sup>	49,610	-5.04	-11.35
CDs (UAHm) <sup>3</sup>	151,454	-6.01	+43.57

Notes: [1] NBU's key policy rate; [2] stock of banks' reserves held at NBU; [3] stock of NBU's certificates of deposit.

Source: NBU, Bloomberg, ICU.

#### Breakdown of gov't bond holders (UAHm) (26 November 2021)

	Last	Weekly chg (%)	YoY chg (%)
NBU	312,606	+0.00	-3.69
Banks	503,149	+0.67	+10.63
Residents	59,594	+9.25	+75.93
Individuals	24,017	+2.64	+174.18
Foreigners <sup>1</sup>	92,146	-2.73	+22.28
<b>Total</b>	<b>991,512</b>	<b>+0.65</b>	<b>+10.49</b>

Notes: [1] non-residents

Source: NBU, ICU.

#### FX market indicators (26 November 2021)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	27.1376	+2.13	-4.70
EUR/USD	1.1317	+0.24	-5.00
DXY	96.089	+0.06	+4.45
UAH TWI <sup>1</sup>	130.458	-1.01	+10.01

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

#### Gov't bond quotes<sup>1</sup> (29 November 2021)

Maturity	Bid	Ask
6m	11.00	10.00
12m	12.50	11.50
2y	13.00	12.00
3y	13.50	12.50
12m (\$)	4.50	3.00
2y (\$)	5.00	3.25

Notes: [1] Actual quotes you can see at [www.icu.ua](http://www.icu.ua).

Source: ICU.

# Domestic liquidity and bonds market

## Borrowing becoming more expensive

Last week, the Ministry of Finance again raised interest rates on UAH-denominated bonds, which attracted non-bank investors, but has not yet attracted foreigners. Demand may increase this week due to reinvestment of redemptions, but domestic investors are likely to prevail again.

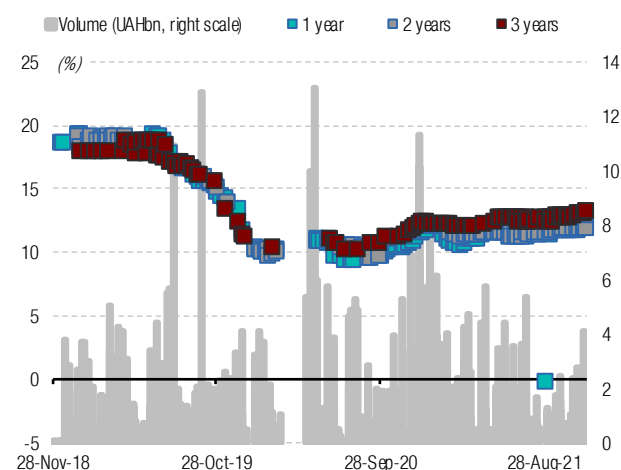
The Ministry of Finance had to raise interest rates on UAH-denominated bills even to attract small amounts of money. For three-month securities, the rate was increased by 50bp to 10%, while borrowings amounted to only UAH150mn. See more details in the [auction review](#). In total, borrowings at the auction amounted to only UAH4.4bn, and most borrowings were for a period of 203 days, most likely bought by non-bank investors whose portfolios by the end of Wednesday - the day of settlement - increased by UAH3.4bn, a volume that is almost identical to the placement of semi-annual bills.

**ICU view:** *This week, there is a redemption of bills sold by MoF last year, which were bought mainly by domestic investors. Therefore, we do not expect that this redemption will accelerate foreigners' fund withdrawals, although we do not expect large new investments from them at the moment due to the difficult security situation in the country. The Ministry of Finance plans to place six-year notes, which are attractive mainly to foreigners. But domestic investors can become more active and reinvest funds at even higher rates.*

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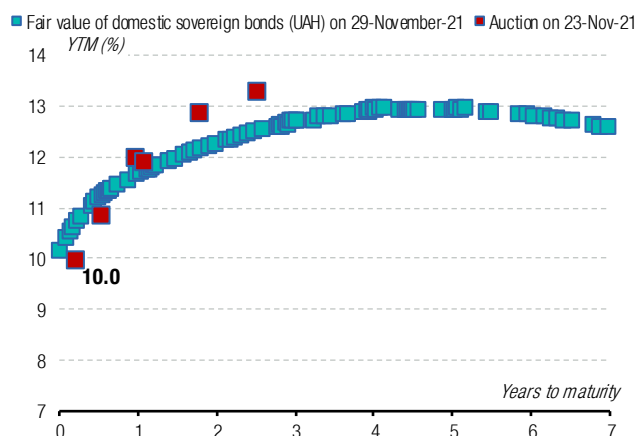
**Chart 1. Local-currency bonds**

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.

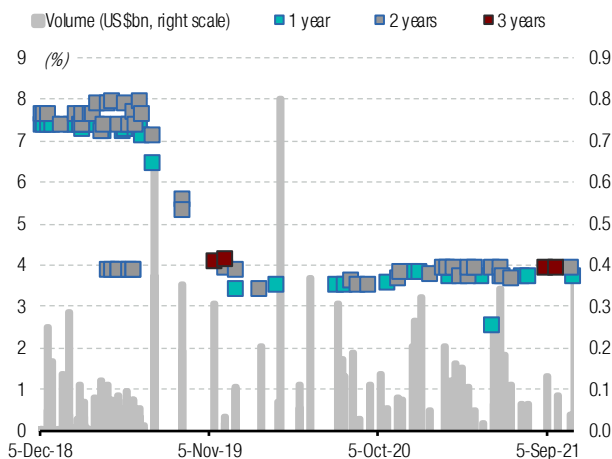
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



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

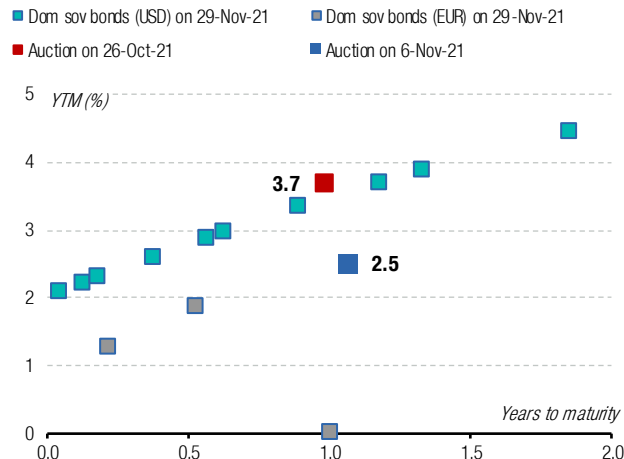
**Chart 2. FX-denominated bonds**

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.

## Foreign exchange market

### The hryvnia continues to weaken

Demand for hard currency remains high, and even increased compared with previous weeks, but the supply of hard currency is not enough to satisfy such increased demand. Therefore, the hryvnia continued to weaken last week and may weaken further this week, gradually finding a balance in the range of UAH27–27.5 UAH/US\$.

The difficult security situation at the country's borders has led to an increase in demand for hard currency from both foreigners and residents. And such demand was not matched by adequate supply, because despite the payment of quarterly and monthly taxes, residents reduced the sale of hard currency, in anticipation of better conditions. In addition, UAH11.7bn of VAT refunds were paid from the budget in a week, including UAH7.6bn on Friday.

On Tuesday and Wednesday, the balance of banks' clients' transactions was on the demand side, as they bought more than they sold by US\$140-160mn per day, forcing the NBU to intervene in the market and satisfy excessive demand. About US\$300mn was sold in the first three days of last week, and another US\$330mn on Friday. This is the largest intervention since the COVID-19 pandemic started in March, 2020.

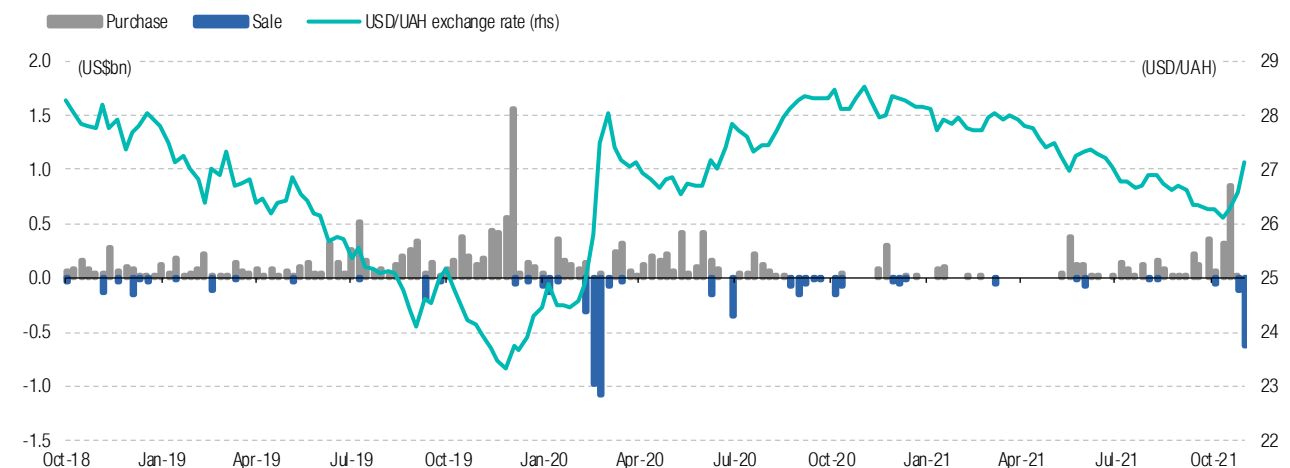
Due to this, the hryvnia exchange rate has been gradually weakening since mid-November, and at the end of last week, it crossed the level of UAH27/US\$, ending the week at UAH27.14/US\$, for a loss of 2.13%.

**ICU view:** We expect that the unstable situation in the FX market will continue, but thanks to the NBU's interventions and the gradual resumption of hard currency sales by exporters, the market should be balanced this week in the range of UAH27–27.5/US\$. Offering a six-year note should help to stabilize the market, as they may attract foreigners due to the weaker hryvnia and higher interest rates than before. We can see a gradual depletion of excess demand, although imports, especially energy, may need even more hard currency.

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**Chart 3. FX market indicators, 3-year history**

*Ukraine hryvnia UAH exchange rate per US dollar at the interbank market and NBU interventions (weekly data)*



Source: NBU, Bloomberg, ICU.

## Economics

### IMF completes first review of Stand-by Programme after a delay of more than a year

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Ukraine received around US\$700mn following the review and is scheduled to receive a similar amount following a review in March and another US\$1.5bn upon review in June 2022. Ukraine committed to undertake a number of ambitious reforms in several areas:

- **Fiscal policy:** Approval of the 2022 state budget deficit within 3.5% of GDP, limiting state guarantees to 3% of state budget revenues, improving tax revenue administration, keeping the tax system broadly unchanged, improving efficiency of social programmes, including energy-related subsidies.
- **Monetary and FX policy:** Continued commitment to inflation targeting and proper monetary policy response to bring inflation within the NBU's inflation target band, refrain from long-term refinancing operations.
- **Financial sector:** Strengthening bank capital requirements, reducing NPLs, implementation of reform of state-owned banks, addressing the Deposit Guarantee Fund insolvency issue, and strengthening regulatory framework for the non-bank financial sector.
- **Structural policies:** Enhancing institutional capacity of NABU and Anticorruption Prosecutor's Office, advancing judicial system reform.
- **Energy sector:** Preventing accumulation of a quasi-fiscal deficit, removing caps on gas prices for households since May, appointing Naftogaz supervisory board member via a transparent competition, enhancing competition in wholesale and retail gas market.
- **Corporate governance and privatization:** Enhancing corporate governance standards of state-owned enterprises, continued privatization.

***ICU view: We expect a relatively smooth second review of the IMF programme in March – the authorities have already made it clear to the international community that they plan to deliver on their promises. However, the June review may become problematic as several critical commitments are at risk to be met on time or in full, in particular the removal of a cap on gas prices for households. The IMF agreed that government can use the full amount of loans under the existing Stand-By programme for its purposes. If Ukraine stays firmly on its path of cooperation with the IMF, the government is unlikely to face any significant challenges in financing of the state budget deficit and rolling over its existing debt.***

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