



Focus  
Ukraine

Markets  
Domestic liquidity,  
government bonds, FX  
market, and macro

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# Weekly Insight

## Parliament approves 2022 state budget

### Key messages of the today's comments

#### Domestic liquidity and bonds market

##### Sentiment toward Ukrainian debt improves

Over the past week, the sentiment of investors toward Ukrainian government bonds has improved slightly, but it is too early to talk about a return to stability.

#### Foreign exchange market

##### The hryvnia exchange rate is stabilizing

Last week, the hryvnia exchange rate fluctuated in the range of UAH27–27.5/US\$ and is likely to remain in this range this week too.

#### Economics

##### Parliament approves 2022 state budget

Ukraine's parliament approved the state budget for 2022 with a target deficit of UAH189bn (US\$6.9bn based on current ER). This is the equivalent of 3.5% of 2022F GDP according to government estimates.

### MONDAY, 6 DECEMBER 2021

#### Banks' reserves market (3 December 2021)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) <sup>1</sup>	8.50	+0bp	+250bp
ON rate (%)	7.73	-1bp	+305bp
ON \$ swap (%)	N/A	...	...
Reserves (UAHm) <sup>2</sup>	43,407	-12.50	-15.86
CDs (UAHm) <sup>3</sup>	148,339	-2.06	+27.17

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 govt bond holders (UAHm) (3 December 2021)

	Last	Weekly chg (%)	YoY chg (%)
NBU	312,606	+0.00	-3.69
Banks	507,623	+0.83	+9.76
Residents	77,415	+30.08	+121.62
Individuals	24,255	+0.99	+171.98
Foreigners <sup>1</sup>	91,283	-0.84	+21.41
<b>Total</b>	<b>1,013,183</b>	<b>+2.18</b>	<b>+11.83</b>

Notes: [1] non-residents

Source: NBU, ICU.

#### FX market indicators (3 December 2021)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	27.3275	+0.70	-3.37
EUR/USD	1.1315	-0.02	-6.83
DXY	96.117	+0.03	+5.96
UAH TWI <sup>1</sup>	129.215	-0.95	+9.51

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

#### Gov't bond quotes<sup>1</sup> (6 December 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

## Sentiment toward Ukrainian debt improves

Over the past week, the sentiment of investors toward Ukrainian government bonds has improved slightly, but it is too early to talk about a return to stability.

The exit of foreign investors from Ukrainian UAH-denominated debt continues, but its pace is gradually slowing. Thus, if in the previous two weeks portfolios decreased by UAH2.5bn and UA1.6bn, last week the decline was only UAH0.8bn. The slowing could be partially caused by the placement of the six-year note, but more important, likely it was due to hryvnia weakening and an increase in bonds yields, which made the sale of UAH-denominated paper less interesting.

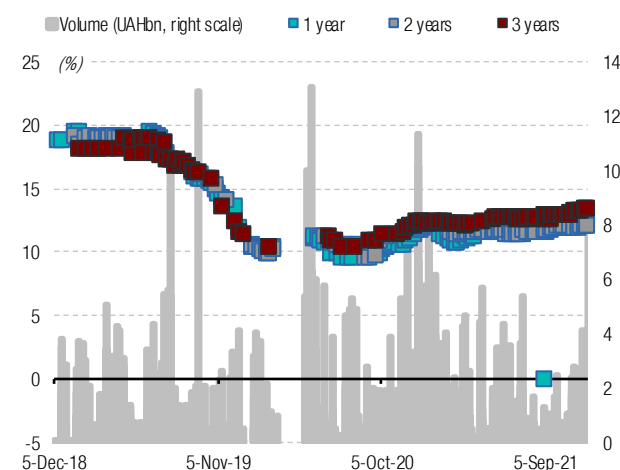
Nonetheless, it appears that the general sentiment of investors toward Ukraine is gradually improving. It seems that they are gradually calming down and assessing the risk of Russian invasion at a slightly lower level. As a result, in addition to a smaller exit from local-currency debt, demand for Eurobonds and VRIs has increased. VRIs rose in price to almost 95 after slumping to 88 a week earlier. Eurobond yields decreased by 30–55bp, to 6.24–7.85%, both due to lower benchmark yields and tightening spreads. Because of this, prices rose to 95–110 from 93–107 a week earlier.

**ICU view: The security situation at the border remains difficult, but investors seem to be paying less attention to it due to various statements and assessments of the situation regarding the possibility of invasion and when it may occur. Therefore, the prices of external debt are gradually returning to the levels of a month ago, although this will take some time. But in the domestic market, the likelihood of foreign investors returning has increased due to higher yields and a weaker hryvnia.**

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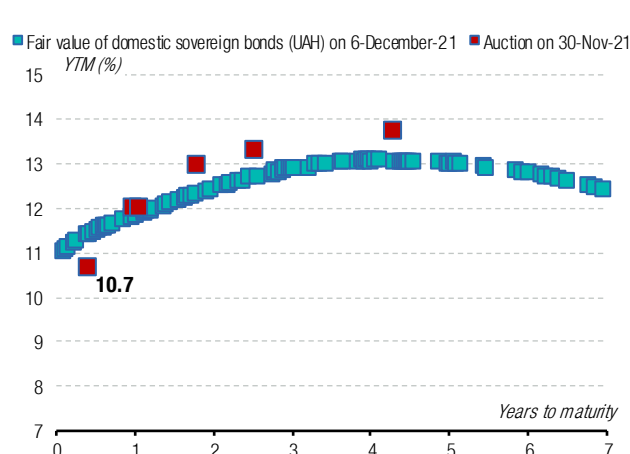
**Chart 1. Local-currency bonds**

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.

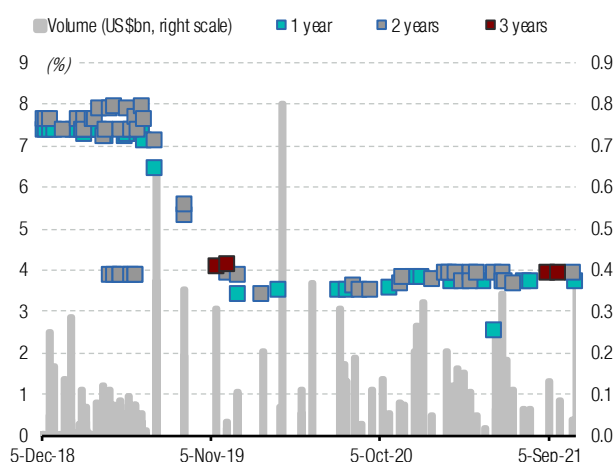
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



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

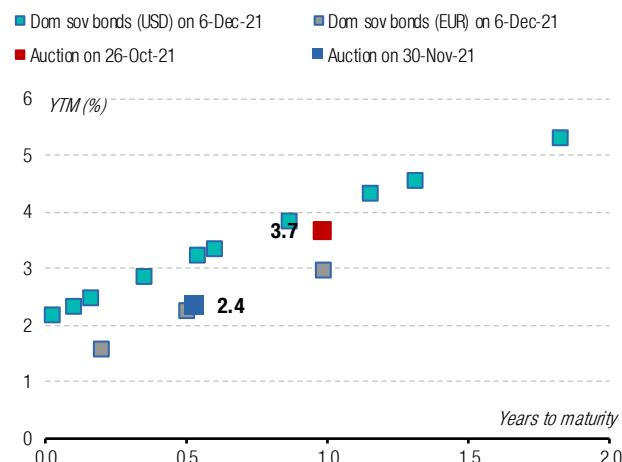
## Chart 2. FX-denominated bonds

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 exchange rate is stabilizing

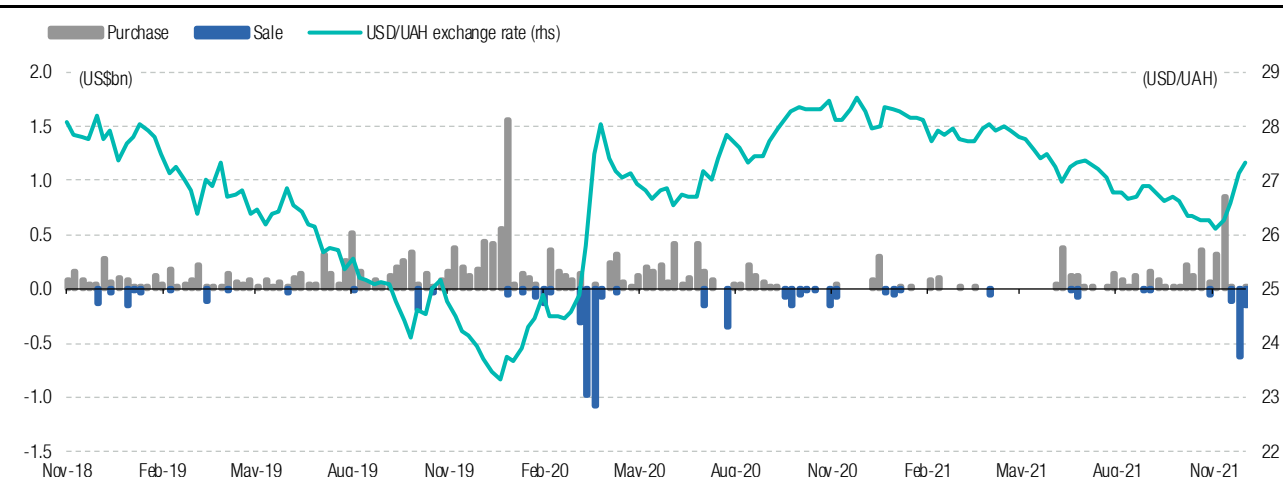
Last week, the hryvnia exchange rate fluctuated in the range of UAH27–27.5/US\$ and is likely to remain in this range this week too.

The situation in the FX market is gradually stabilizing, as despite the continued dominance of demand, the NBU is intervening less in the market. It seems that the hryvnia exchange rate has found a level of relative stability.

So, last week, the NBU sold considerably less hard currency from reserves than the week before, only US\$155mn vs US\$630mn. Sales took place on Monday and Wednesday, and on Thursday, the NBU even bought the usual US\$5mn. Most of the hard currency—almost US\$100mn—was sold on Wednesday, when there were redemptions of UAH-denominated bills and the new regulation of banks' open positions came into force. Accordingly, on this day, the purchase of hard currency by bank customers was US\$175mn more than the sale, and market turnover increased by more than US\$100mn.

**ICU view:** At the end of the week, the market was mostly self-balanced with minimal NBU intervention, which may indicate that a new balanced level has been found, and exchange rate volatility is not expected. Most likely, this week the exchange rate will fluctuate within the same range of UAH27–27.5/US\$ and further movement will depend on foreigners' activity and exporters' supply, who have probably already spent the funds received through VAT refunds.

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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

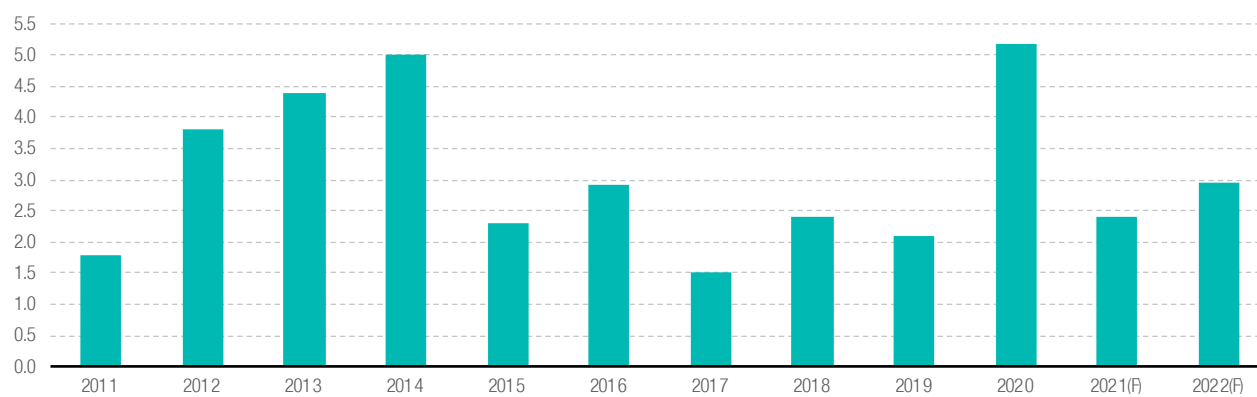
### Parliament approves 2022 state budget

Ukraine's parliament approved the state budget for 2022 with a target deficit of UAH189bn (US\$6.9bn based on current ER). This is the equivalent of 3.5% of 2022F GDP according to government estimates.

Budget revenues and expenditures are projected to grow significantly slower than nominal GDP. There is also a quasi-fiscal component in the budget plan. Government is given the right to issue state guarantees of up to c. UAH35bn (3% of planned revenues) and also to capitalize the State Housing Corporation (Ukrfinzhytlo) to the tune of UAH30bn for thermo-modernization of housing. The budget deficit is expected to be covered with net domestic borrowings of UAH99bn, net external borrowings of UAH79bn, and privatization proceeds of UAH8bn. On a separate note, the Minister of Finance indicated that the 2021 state budget deficit will increase to 3.0–3.5% of GDP for full 2021 from 1% of GDP in 11M21.

**ICU view:** *The target state budget deficit of 3.5% of GDP and the cap on state guarantees in 2022 are both fully in line with Ukraine's commitment within the IMF Stand-by Programme. The central government's financial plan for 2022 looks reasonably conservative. Even so, we expect that raising the full amount of the planned borrowings may be a challenge given jitters in global debt markets. Ukraine will thus critically depend on concessional funding from IFIs to close its budget shortfall. Staying on track of the IMF Stand-by Programme, which offers another US\$2.2bn in budget support in 2022, is of utmost importance. Overall, we expect the actual 2022 fiscal balance will be slightly below the targeted level, likely less than 3% of GDP.*

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**Chart 4. State budget deficit, % of GDP***Ukraine's fiscal deficit remains reasonable in relation to GDP*

Source: MoF, Ukrstat, ICU.

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