

Weekly Insight

Economy healthier but too slow

Key messages of the today's comments

TUESDAY, 28 DECEMBER 2021

Domestic liquidity and bonds market

Ministry of Finance more active borrowing through T-bills

Last week, the Ministry of Finance held the most active auction of the year, and this week's auction may further improve budget deficit financing.

Foreign exchange market

Hryvnia keeps FX market in balance

The FX market was mostly self-balanced, with small fluctuations in the hryvnia exchange rate. But this week, volatility may increase due to VAT refunds and importer's need for hard currency.

Economics

Ukrainian Economy: Healthier but Too Slow

Ukraine will enter 2022 with a solid safety cushion thanks to sound fiscal and monetary policies, strong external commodity markets, and a resilient banking sector. However, sluggish economic growth and high inflation will be a grain of salt. Russia's aggression toward Ukraine will be the key non-economic factor to closely monitor next year and beyond. Repetitive maneuvers of Russia's troops along Ukraine's borders will continue to disturb business and damage investor sentiment toward Ukraine.

Due to the Christmas and New Year holidays next weekly is scheduled for 10th January, 2022

Banks' reserves market (24 December 2021)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	9.00	+0bp	+300bp
ON rate (%)	8.31	+9bp	+281bp
ON \$ swap (%)	N/A
Reserves (UAHm) ²	51,612	-25.34	-1.00
CDs (UAHm) ³	133,299	-0.93	+35.51

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) (24 December 2021)

	Last	Weekly chg (%)	YoY chg (%)
NBU	312,606	+0.00	-3.69
Banks	534,131	+3.64	+5.18
Residents	81,326	+2.31	+87.54
Individuals	24,895	+4.56	+133.70
Foreigners ¹	92,497	-0.89	+9.63
Total	1,045,532	+2.04	+7.68

Notes: [1] non-residents

Source: NBU, ICU.

FX market indicators (24 December 2021)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	27.2688	+0.06	-3.86
EUR/USD	1.1319	+0.70	-7.12
DXY	N/A
UAH TWI ¹	127.880	-2.56	+9.10

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

Gov't bond quotes¹ (28 December 2021)

Maturity	Bid	Ask
6m	11.75	10.50
12m	12.50	11.50
2y	13.25	12.25
3y	13.50	12.75
12m (\$)	4.00	3.00
2y (\$)	4.50	3.25

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

Source: ICU.

Domestic liquidity and bonds market

Ministry of Finance more active borrowing through T-bills

Last week, the Ministry of Finance held the most active auction of the year, and this week's auction may further improve budget deficit financing.

Until the last week, the largest auction was in June, when the Ministry of Finance was able to borrow more than UAH19bn with a weighted average maturity of two years, which included large participation from foreign investors. Last week, a new record amount of funds was borrowed at UAH20.5bn, but with a weighted average maturity of just slightly above one year. Just offering of the UAH-denominated bills with maturities of up to one year, allowed to set a new record high. These bills provided the budget with UAH8.2bn, while 12-month USD-denominated securities provided additional UAH8.4bn for the budget. In addition, a further UAH4bn was raised from bills and notes with maturity of more than one year.

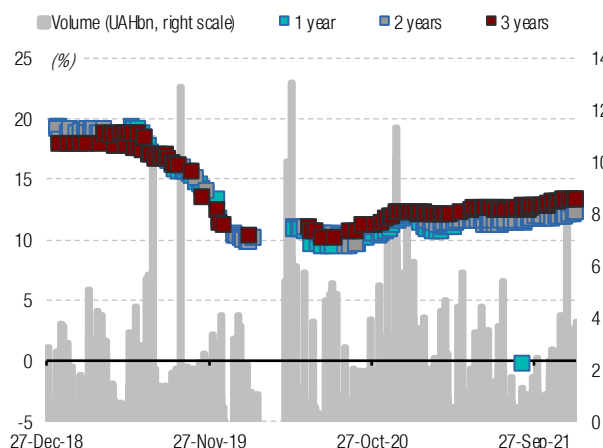
According to NBU statistics, the main investors last week were Ukrainian banks, which bought the vast majority of bonds. In addition, activity in the secondary market intensified, and trading volumes increased to almost UAH11bn, where UAH6.3bn was traded in UAH-denominated bonds, including not only bills sold at last week's auction. Foreigners reduced their portfolios again, probably by selling bonds maturing in 2026, of which UAH1.5bn traded last week.

ICU view: We expect the auction to be active again today, but we do not think it will set a new record. Most likely, foreign investors will again ignore the primary market, and investors will not be in a hurry to buy large amounts of new bonds. It is possible that the vast majority of bonds will be purchased by banks, including state-owned banks, which will prefer short-term bills.

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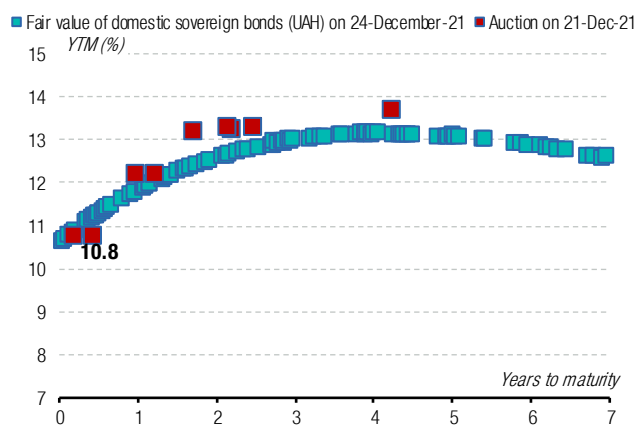
Chart 1. Local-currency bonds

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.

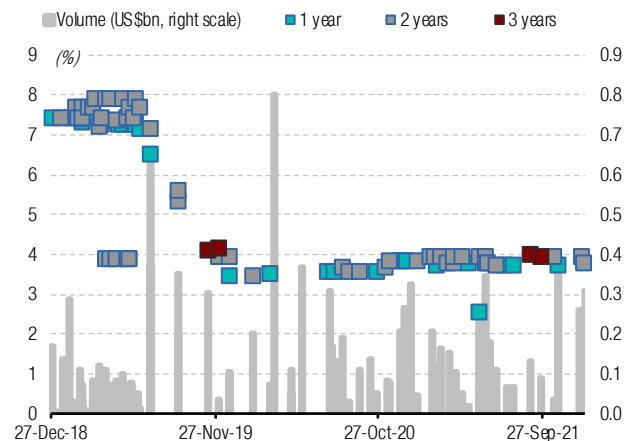
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



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

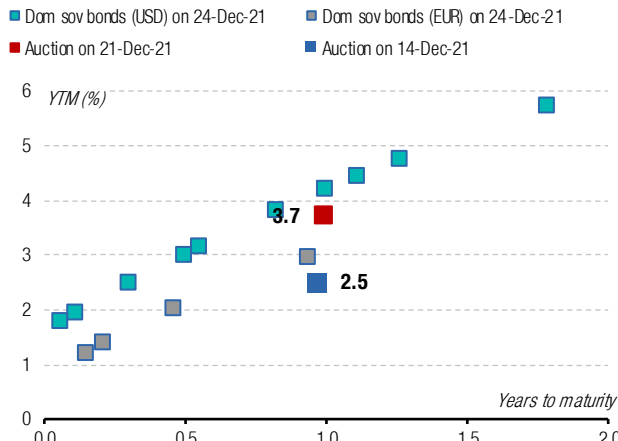
Chart 2. FX-denominated bonds

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

Hryvnia keeps FX market in balance

The FX market was mostly self-balanced, with small fluctuations in the hryvnia exchange rate. But this week, volatility may increase due to VAT refunds and importer's need for hard currency.

In general, the imbalance among bank customers persisted, requiring more hard currency than sellers offered, and this need was covered by banks. In general, market turnover changed insignificantly, but the NBU refrained from selling interventions and instead, bought US\$10mn in reserves in two days.

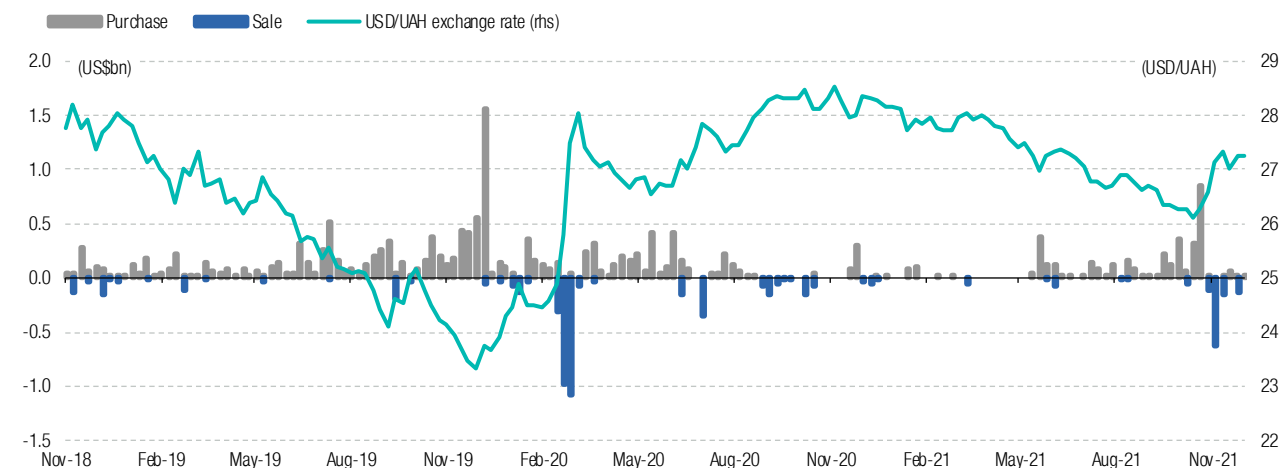
As a result, the hryvnia exchange rate remained in the expected range of UAH27–27.5/US\$ and weakened by 0.1% to UAH27.27/US\$ by the end of the week, which was stronger than at the beginning of the year.

ICU view: This week, the hryvnia will be under pressure from lower currency supply from exporters due to VAT refunds that can reach UAH10bn and due to the Christmas and New Year holidays with low business activity. Therefore, demand will prevail again, but the NBU can meet excess demand using reserves, balancing the market in the same range of UAH27–27.5/US\$ by the end of the year. However, in the first few weeks of 2022, the exchange rate may weaken a little more, approximately to UAH28/US\$, although such a movement will be short-lived and caused by the same low business activity due to holidays.

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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

Ukrainian Economy: Healthier but Too Slow

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Completion of the first review of the IMF-Ukraine Stand-by Programme came after a significant delay of more than one year, but, still, it was a significant milestone. Ukraine reconfirmed its commitment to reforms, which was received as a much-awaited positive signal to the international community. However, risks are still high that some commitments, like removing the cap on gas prices for households, may be difficult to deliver. Smooth rollover of external debt and the state deficit financing in 2022 critically depend on Ukraine being able to stay firmly on track with the IMF cooperation programme.

[Read full Macroeconomic Review \(dated Dec. 21, 2021\)](#)

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