



Focus
Ukraine

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

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Weekly Insight

FX market jitters persist

Key messages of the today's comments

MONDAY, 21 FEBRUARY 2022

Ukrainian bond market

Activity in domestic bond market remains low

The total volume of deals in the domestic secondary bond market last week increased only insignificantly, and borrowings in the primary market have been minimal, the lowest since 2018.

Eurobond market is feverish again

Investors in Ukrainian Eurobonds are still very nervous about the news about a possible escalation of Russia's aggression against Ukraine and, when possible, they are reducing investments in Ukrainian assets.

Foreign exchange market

FX market jitters persist

The hryvnia exchange rate weakened further last week, although it did not set new negative records.

Banks' reserves market (18 February 2022)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	10.00	+0bp	+400bp
ON rate (%)	9.43	+12bp	+424bp
Reserves (UAHm) ²	54,126	-15.15	-9.38
CDs (UAHm) ³	129,090	-9.98	-3.15

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) (18 February 2022)

	Last	Weekly chg (%)	YoY chg (%)
NBU	310,106	+0.00	-3.72
Banks	534,557	-1.21	+2.59
Residents	80,251	-0.60	+31.28
Individuals	25,145	-0.04	+96.32
Foreigners ¹	76,639	-3.27	-25.21
Total	1,026,877	-0.93	+0.69

Source: NBU, ICU.

FX market indicators (18 February 2022)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	28.4130	+1.24	+2.05
EUR/USD	1.1322	-0.25	-6.37
DXY	96.043	-0.04	+6.02
UAH TWI ¹	124.869	-1.17	+4.73

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

Market gov't bond quotes¹ (21 February 2022)

Maturity	Bid	Ask
6m	14.00	12.00
12m	15.00	12.25
2y	15.50	13.00
3y	16.00	13.50
12m (\$)	4.00	3.00
2y (\$)	4.50	3.25

Source: ICU.

Ukrainian bond market

Activity in domestic bond market remains low

The total volume of deals in the domestic secondary bond market last week increased only insignificantly, and borrowings in the primary market have been minimal, the lowest since 2018.

Foreign investors continue to reduce their UAH-denominated bond portfolios, which fell by more than UAH2.4bn to UAH75.4bn last week. Repayment of FX-denominated bills last Thursday led to a reduction in the portfolios of all groups of investors. They were in no hurry to buy new bonds, neither in the primary auction nor on the secondary market.

Last week, the Ministry of Finance offered only two bills with a maturity of up to one year, effectively abolishing the placement of longer maturities. Only one bid for UAH5m was rejected, and just UAH66m was borrowed (more details in the [auction review](#)). This is the lowest amount since the end of November 2018, when only UAH48m was raised for the budget.

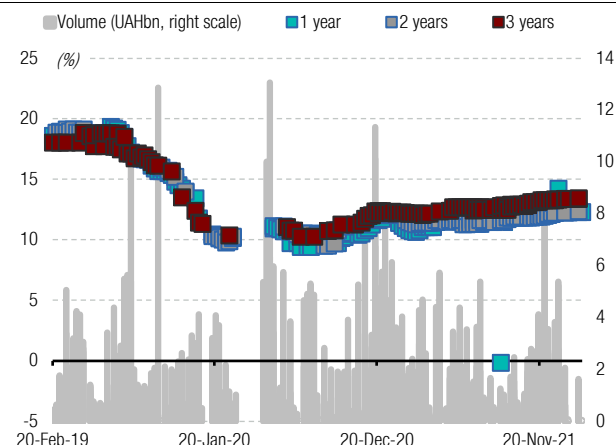
In the secondary market, the activity of UAH-denominated bonds trading rose insignificantly compared with previous week. The volume of deals increased by only UAH1.5bn to UAH7.8bn. But trading of FX-denominated bills, partially due to the redemption of a large issue last Thursday, was low as the total amount of deals fell by UAH0.5bn to UAH1.7bn. However, it is quite important that trading of the three-year note decreased to UAH0.7bn from UAH1.2bn from the previous week or UAH2.7bn a week before. This paper will be included in the JP Morgan GBI EM index despite the threat of war.

ICU view: Because the risk of a Russian invasion persists and the hryvnia exchange rate remains relatively weak compared with the beginning of the year (see [comment below](#)), demand for new bills is very low among domestic investors, and almost non-existent from foreigners. This week, the redemption of UAH18bn may increase interest in new bills among residents, especially Ukrainian banks, which have been the largest investors in this paper. But no significant improvement in budget funding is expected in the coming weeks.

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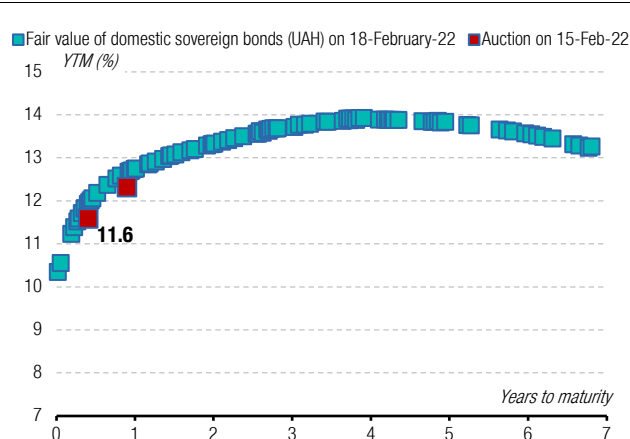
Chart 1. Local-currency bonds

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.

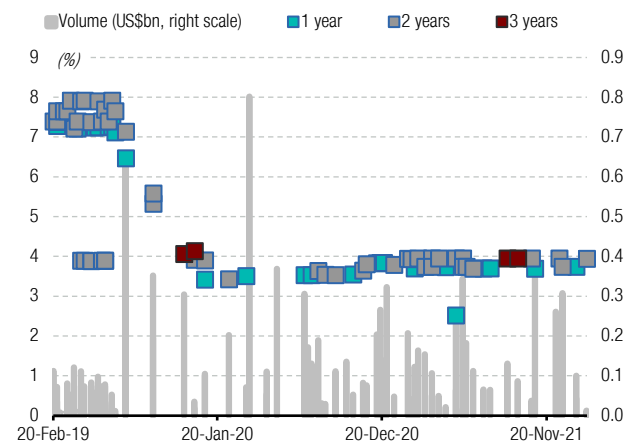
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



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

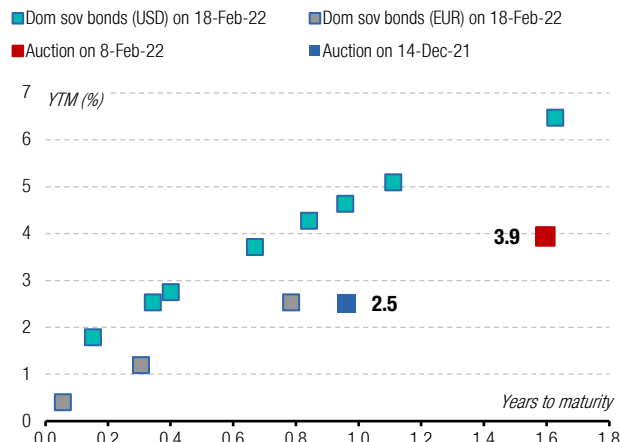
Chart 2. FX-denominated bonds

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.

Eurobond market is feverish again

Investors in Ukrainian Eurobonds are still very nervous about the news about a possible escalation of Russia's aggression against Ukraine and, when possible, they are reducing investments in Ukrainian assets.

Geopolitical tensions continued to be decisive for yields, and they remained under pressure of negative news about Russia's escalation of hostilities. There were several sharp fluctuations during the week, including in response to provocative Russian shelling of civilian sites last Thursday. They were presented by the Russian media as an attack by the Ukrainian side, which could be used by Russia as a pretext for invasion. The reliable facts presented by Ukraine reassured investors, but did not contribute to a significant decline in YTM's, especially on Eurobonds maturing in September this year.

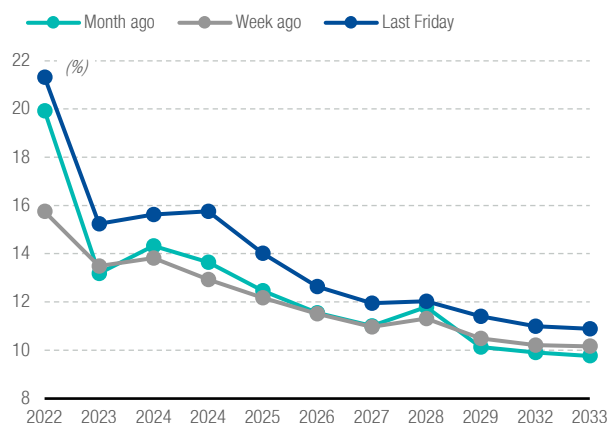
The general sentiment remains negative despite the US's announcement to provide guarantees for Ukraine's debt of US\$1bn, EU steps to complete procedures to provide Ukraine with the first tranche of macro-financial assistance for EUR600m, and information about financial support for Ukraine by a number of countries.

ICU view: We expect more clarity this week about Russia's intentions to withdraw troops from the Ukrainian border. According to preliminary statements, the military exercises were to end on Sunday, but according to the Belarusian Ministry of Defense, they will be extended. Therefore, investors' sentiment will remain very cautious. Geopolitical tensions will continue to be a key factor in the pricing of Ukrainian Eurobonds, as de-escalation is not to be expected in the near future.

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Chart 3. Ukrainian Eurobonds yield curves

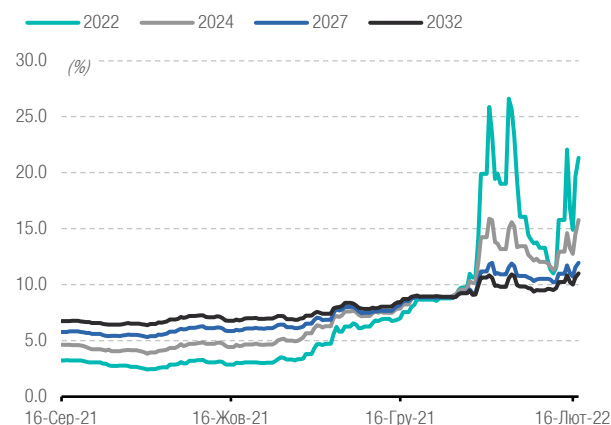
Yield curves of USD-denominated Eurobonds as of last Friday, a week and a month earlier



Source: Bloomberg, ICU.

Chart 4. YTM of selected Ukrainian Eurobonds

Last six-month historical data



Source: Bloomberg, ICU.

Foreign exchange market

FX market jitters persist

The hryvnia exchange rate weakened further last week, although it did not set new negative records.

Last Monday, hard currency sales fell sharply, with bank customers selling hard currency for US\$305m less than they bought, although total market turnover rose to almost US\$1.1bn that day. The excessive demand was covered by the NBU's interventions, selling about US\$377m on Monday. In general, during the week, sale interventions prevailed, a total of US\$503m was sold, but when the market was calmer, the NBU even bought back US\$50m in reserves.

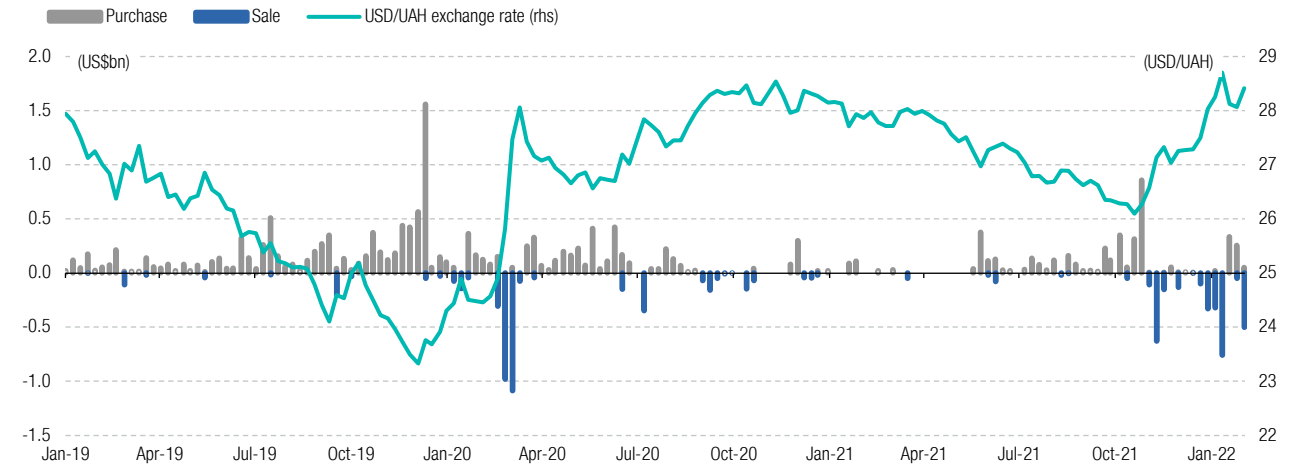
By the end of the week, the FX market became somewhat calmer, and sales of hard currency by bank customers could increase due to the deadlines for payment of a number of taxes for 4Q21. Therefore, the hryvnia exchange rate stabilized at around UAH28.4/US\$ on Friday. In general, during the week, the hryvnia exchange rate weakened by 1.2% to UAH28.41/US\$, and since the beginning of the year, the weakening of the national currency has been 4.1%.

ICU view: Tax payments today may add supply to the FX market, but negative expectations of an escalation of Russia's hostilities will increase nervousness, which will not help the hryvnia. Demand for hard currency to finance imports of natural gas and other goods may increase, as importers can increase purchases by taking advantage of temporary exchange rate stabilization.

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Chart 5. 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.

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