



Focus
Ukraine

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

Research team
**Vitaliy Vavryshchuk
Alexander Martynenko
Taras Kotovych**

Weekly Insight

BoP data send mixed signals

Key messages of the today's comments

Ukrainian bond market

NBU increases purchases of military bonds

Last Wednesday, the National Bank of Ukraine bought another UAH10bn of military bonds to support the state budget during wartime.

Fall in Eurobond prices slows

After an up to 10% drop in Eurobond prices in previous weeks, prices slid by only 2-4% last week.

Economics

Ukraine's public debt inches down YTD

In March, Ukraine's public debt increased 4% MoM, but still declined 1% YTD to an equivalent of US\$96.8bn.

Balance-of-payments data sent mixed signals in March

NBU reported balance-of-payments data for March, the first full calendar month of war, which sheds much light on how the economy adjusted to significant economic and social disruptions.

MONDAY, 2 MAY 2022

Banks' reserves market (29 April 2022)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	10.00	+0bp	+250bp
ON rate (%)	9.76	+0bp	+295bp
Reserves (UAHm) ²	48,572	-24.65	-14.77
CDs (UAHm) ³	185,238	+11.47	+19.99

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) (29 April 2022)

	Last	Weekly chg (%)	YoY chg (%)
NBU	380,106	+2.70	+18.42
Banks	540,602	-0.92	+3.25
Residents	73,770	-2.88	+67.58
Individuals	25,677	-0.08	+61.73
Foreigners ¹	74,398	+0.01	-23.65
Total	1,094,552	+0.24	+9.22

Source: NBU, ICU.

FX market indicators (29 April 2022)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	30.2617	+0.01	+9.24
EUR/USD	1.0545	-2.27	-13.00
DXY	102.959	+1.72	+13.62
UAH TWI ¹	133.175	+1.37	+9.99

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

Market gov't bond quotes¹ (2 May 2022)

Maturity	Bid	Ask
6m
12m
2y
3y
12m (\$)
2y (\$)

Source: ICU.

Ukrainian bond market

NBU increases purchases of military bonds

Last Wednesday, the National Bank of Ukraine bought another UAH10bn of military bonds to support the state budget during wartime.

Last week, the NBU purchased another UAH10bn (US\$0.3bn) of military bonds, with total purchases reaching UAH50bn (US\$1.7bn) in April and UAH70bn (US\$2.4bn) since the Russian invasion. The National Bank said this was a necessary step given the significant defence, humanitarian, and social needs.

At the same time, the NBU stressed that such support could not be the main source of funding for government expenditures. It also added that the government should increase market borrowing through primary auctions, including borrowing from the banking system.

The Ministry of Finance raised UAH13bn (US\$0.4bn) through the primary auction last week (more details in the auction review) and refinanced a large part of the repayments it made last Wednesday. Since debt rollover last week was not full, and given the high liquidity in the banking system, the NBU believes that banks have the capacity to increase their debt portfolios significantly.

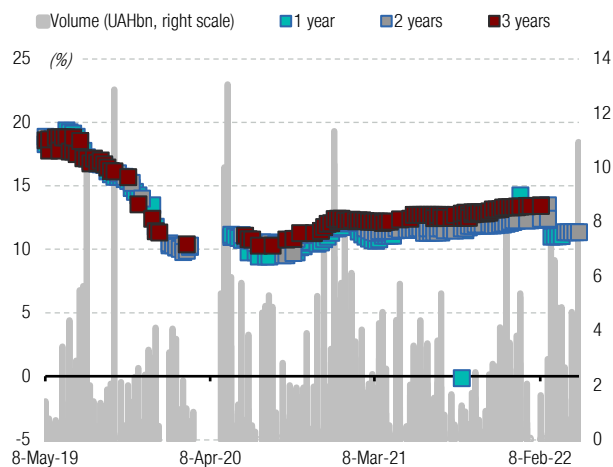
Total banking-system liquidity has long been close to UAH200bn (US\$6.8bn). In late March and early April, it fell to UAH186bn (US\$6.3bn) due to tax payments, but just a few days later, it exceeded UAH200bn (US\$6.8bn) and then UAH230bn (US\$7.8bn) since the end of the third week of April. As of this morning, the total amount of liquidity was UAH223bn (US\$7.6bn), including UAH54.9bn (US\$1.9bn) in the banks' correspondent accounts with the NBU and UAH168.1bn (US\$5.7bn) invested in the NBU's ON CDs.

ICU view: Currently, the banking system has a significant stock of liquidity. Last week, it increased thanks to budget expenditures and less than full rollover of maturing debt. However, banks' ability to lend money to the government is likely limited by the term structure of liquidity. Also, new investments in government bills are likely constrained by limits imposed by parent banking institutions (for banks with foreign capital) or risk management. At the same time, given the stability of the funding base, banks are likely ready to increase investments in military bills in the coming months to ensure full rollover of hryvnia debt in 2022.

Taras Kotovych, Kyiv, (044) 377-7040 ext.724

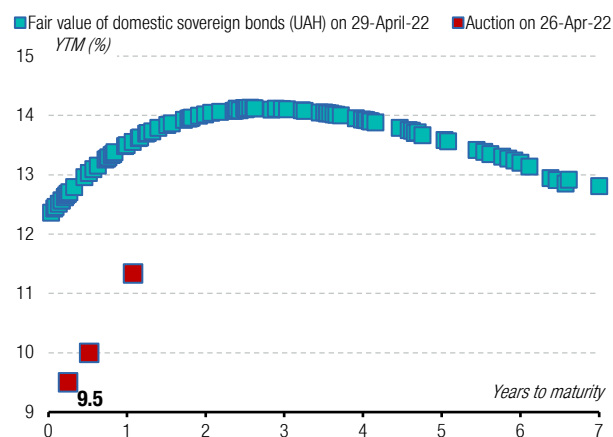
Chart 1. Local-currency bonds

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.

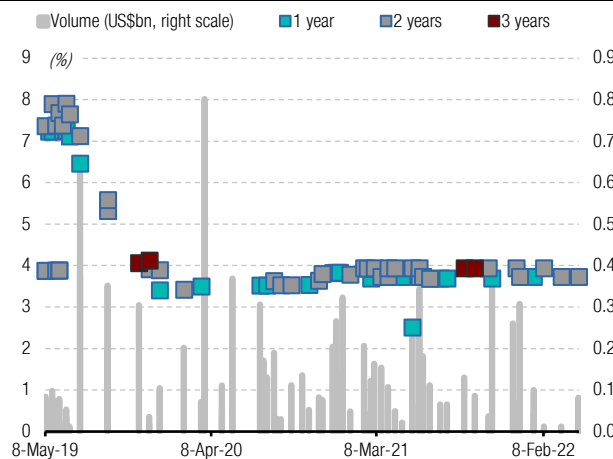
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



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

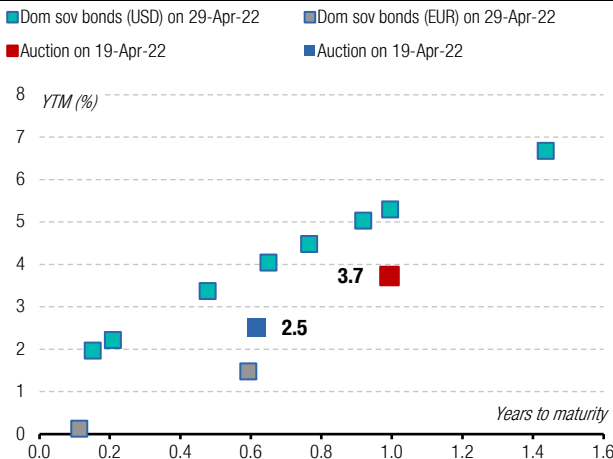
Chart 2. FX-denominated bonds

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.

Fall in Eurobond prices slows

After an up to 10% drop in Eurobond prices in previous weeks, prices slid by only 2-4% last week.

The prices of bonds maturing in 2024 decreased by almost 4%, or by 1.5 cents. For the rest of Eurobonds, prices fell by an average 2.7% or about one cent. In general, prices are still somewhat above the minimums of 21-31 cents that were seen on 7th March, 2022

ICU view: Investors' attention remains focused on news from the battlefields and Ukraine's ongoing negotiations for military and financial support with international partners. The key relevant events last week were a large-scale defence meeting in Ramstein and on Thursday, the adoption of a lend-lease law for Ukraine in the United States. In addition, US President Joe Biden announced plans to increase war-related aid.

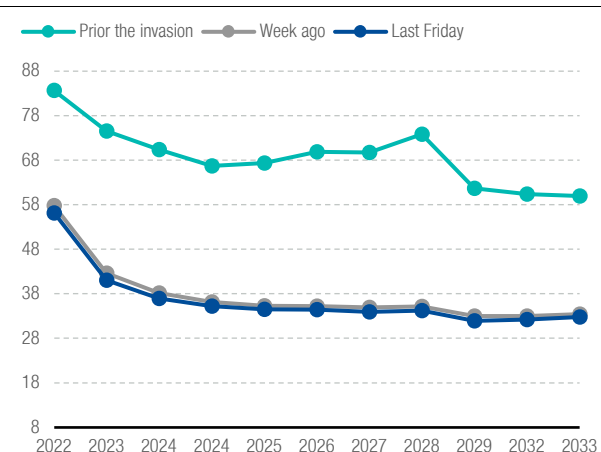
At the same time, it is too early to talk about a fundamental change in the situation at the front. Also, there is still no clear information on the volume, terms, and timing of large-scale financial assistance to Ukraine from Western governments and

international financial organizations. The volume of loans received by Ukraine in April decreased significantly compared with March. Therefore, foreign investors still do not have enough positive signals that would improve their assessment of the fair value of Ukrainian Eurobonds.

Taras Kotovych, Kyiv, (044) 377-7040 ext.724

Chart 3. Ukrainian Eurobonds prices

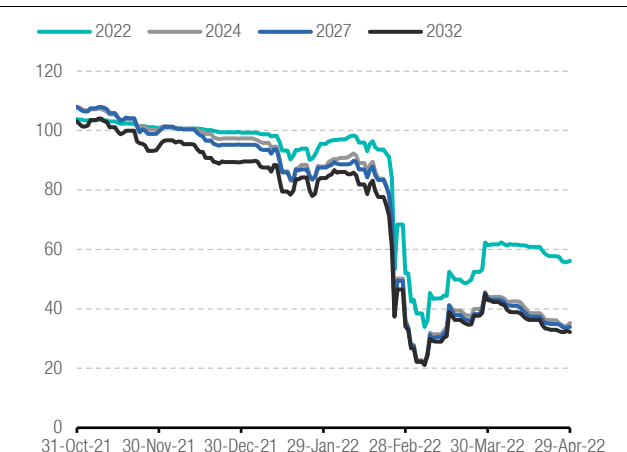
Prices of USD-denominated Eurobonds as of last Friday, a week ago and prior the Russian invasion



Source: Bloomberg, ICU.

Chart 4. Prices of selected Ukrainian Eurobonds

Last six-month historical data



Source: Bloomberg, ICU.

Economics

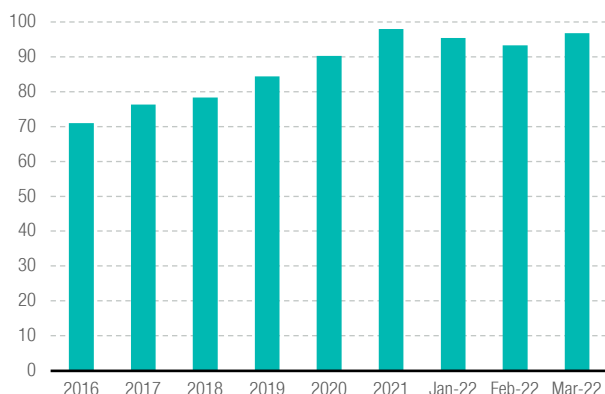
Ukraine’s public debt inches down YTD

In March, Ukraine’s public debt increased 4% MoM, but still declined 1% YTD to an equivalent of US\$96.8bn.

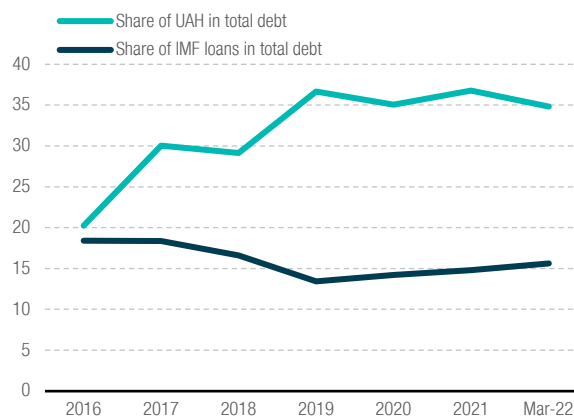
The growth in public debt in March was primarily driven by external borrowings. Government raised more than \$3bn in new loans in March from Western governments and IFIs while facing much smaller redemptions. Domestic debt declined by 7.8% during 1Q to an equivalent of \$35.9bn. The share of UAH-denominated debt was also down in 1Q by 2pp to 34.8%.

ICU view: Ukraine’s public debt was little changed during 1Q in dollar terms, but it is expected to grow substantially in the coming months as Ukraine is upscaling borrowings to cover the huge fiscal shortfall. The end-March debt of \$96.8bn implies debt-to-GDP ratio of 49% based on 2021 GDP. However, the expected significant decline in Ukraine’s nominal GDP combined with heavy new borrowings may push the debt-to-GDP ratio close to 100% by the end of 2022. This ratio can hardly be considered comfortable by Ukraine’s creditors.

Vitaliy Vavryshchuk, Kyiv, (044) 377-7040 ext.721

Chart 5. Ukraine's public debt, \$bn*Public debt inches down YTD*

Source: MoF, ICU.

Chart 6. Share of UAH and IMF loans in total debt, %*The share of hryvnia debt slightly down YTD*

Source: MoF, ICU.

Balance-of-payments data sent mixed signals in March

NBU reported balance-of-payments data for March, the first full calendar month of war, which sheds much light on how the economy adjusted to significant economic and social disruptions.

The most prominent observation was a significant decline in the volume of trade in goods — exports declined 52% YoY in March while the downward adjustment in imports was even more significant at 65%. This implies the trade-in-goods balance turned positive in March at \$0.3bn. Trade-in-services balance, which is usually in hefty surplus, turned negative in March on an upsurge in day-to-day expenditures of Ukrainian refugees abroad. Those were recorded as import of services to Ukraine. Transfers of Ukrainian migrants from abroad (a component of primary income) declined 24% in March to \$0.94bn as many migrants likely preferred to delay transfer of money to Ukraine to better times. Ukraine also saw a significant increase in private sector transfers (an element of secondary income) on an upsurge in humanitarian aid. All in, Ukraine's current account (C/A) turned positive at \$1.35bn in March and \$2.5bn in 1Q22, which is an outstanding good result.

However, the C/A statistics should be interpreted with a great deal of caution. The accuracy of data is significantly lower than in normal times, especially data on trade flows. For example, the official data may understate the volume of import of goods. An abrupt upsurge (\$3.2bn) in trade credit and advance payments in March may indicate that either significant amounts of imports came unnoticed or imports will increase significantly in the coming months.

On the financial account side, outflows stood at \$1.4bn in March (\$2.5bn in 1Q22). While Ukraine saw significant inflows of debt into the state sector at \$1.9bn as its Western partners provided generous support to the state budget, the private sector saw significant outflows. The key components of private sector outflows were 1) an increase in export-related trade credit and advance payments for imports, and 2) withdrawal of FX cash from banks, both from FX deposits and via electronic cards linked to hryvnia accounts.

Overall, while the C/A surplus and F/A deficit nearly offset each other, NBU reserves still increased 2% MoM thanks to net IMF loans of \$0.7bn.

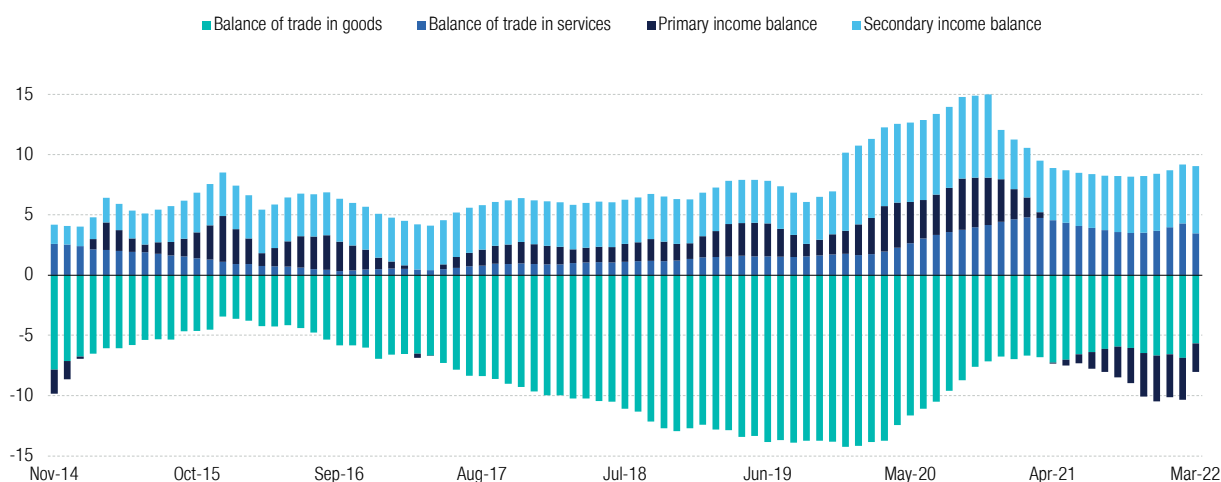
ICU view: March BoP data show dramatic adjustments that happened across all BoP lines within the first month of the war. At the same time, March data are very unlikely to be indicative for the upcoming quarters and full 2022. We expect that the trade-in-goods balance will deteriorate significantly in the coming months as imports recover more strongly than exports following the initial war shock. We, thus, expect the C/A

balance will slip into the negative territory quite soon. Should this happen, the NBU may be forced to reconsider its commitment to a fixed exchange rate it undertook since the start of the war. The C/A gap is still expected to be largely covered by inflows via the financial account as western allies' promises to lend to the Ukrainian government seems credible. We, thus, don't expect a significant decline in NBU reserves through end-2022.

Vitaliy Vavryshchuk, Kyiv, (044) 377-7040 ext.721

Chart 7. Current account, 12-month trailing, \$bn

Balance of trade in goods improved in March



Source: NBU, ICU.

This page is intentionally left blank



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

WEB www.icu.ua



RESEARCH

Vitaliy Vavryshchuk

Head of macro research
vitaliy.vavryshchuk@icu.ua

Taras Kotovych

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

Dmitriy Dyachenko, CFA

Financial analyst
dmitriy.dyachenko@icu.ua

Alexander Martynenko

Head of corporate research
alexander.martynenko@icu.ua

Mykhaylo Demkiv

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

Investment Capital Ukraine LLC is regulated by Securities and Stock Market State Commission of Ukraine (license numbers: dealer activity AE 263019, broker activity AE 263018, underwriting activity AE 263020 dated 11 April 2013).

DISCLAIMER

This research publication has been prepared by Investment Capital Ukraine LLC solely for information purposes for its clients. It does not constitute an investment advice or an offer or solicitation for the purchase or sale of any financial instrument. While reasonable care has been taken to ensure that the information contained herein is not untrue or misleading at the time of publication, Investment Capital Ukraine makes no representation that it is accurate or complete. The information contained herein is subject to change without notice. Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of Investment Capital Ukraine LLC. All rights are reserved. Any investments referred to herein may involve significant risk, are not necessarily available in all jurisdictions, may be illiquid and may not be suitable for all investors. The value of, or income from, any investments referred to herein may fluctuate and/or be affected by changes in exchange rates. Past performance is not indicative of future results. Investors should make their own investigations and investment decisions without relying on this report. Only investors with sufficient knowledge and experience in financial matters to evaluate the merits and risks should consider an investment in any issuer or market discussed herein and other persons should not take any action on the basis of this report.

Additional information is available upon request.

