



Focus  
**Ukraine**

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

Research team  
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Taras Kotovych**

# Weekly Insight

## Inflation keeps accelerating

### Key messages of the today's comments

MONDAY, 16 MAY 2022

### Ukrainian bond market

#### Foreigners reduce UAH bond portfolios

Foreign investors cut their portfolios of local-currency bonds after last Wednesday's redemption for the first time since Russia's full-scale invasion of Ukraine.

#### Eurobond prices rise slightly

The price of Ukrainian Eurobonds rose during most of the last week, but declined moderately at the end of the week, still keeping some of the gains.

### Foreign exchange market

#### NBU allows repatriation of UAH bond proceeds

Last week, the NBU amended its FX regulations such that foreign investors would be able to repatriate their investments without any limitations into local UAH-denominated bonds that mature after 1 April 2023.

### Economics

#### Inflation keeps accelerating in April

Annual inflation increased further significantly to 16.4% YoY in April from 13.7% in March.

### Banks' reserves market (13 May 2022)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) <sup>1</sup>	10.00	+0bp	+250bp
ON rate (%)	9.76	+0bp	+303bp
Reserves (UAHm) <sup>2</sup>	62,507	+30.86	+1.14
CDs (UAHm) <sup>3</sup>	189,560	+6.92	+23.19

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) (13 May 2022)

	Last	Weekly chg (%)	YoY chg (%)
NBU	420,106	+13.15	+34.00
Banks	535,743	-1.96	+1.97
Residents	73,153	-1.36	+64.24
Individuals	26,982	+1.30	+64.99
Foreigners <sup>1</sup>	72,353	-2.75	-25.88
<b>Total</b>	<b>1,128,337</b>	<b>+3.33</b>	<b>+13.27</b>

Source: NBU, ICU.

### FX market indicators (13 May 2022)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	29.4926	-2.54	+6.78
EUR/USD	1.0412	-1.32	-13.82
DXY	104.563	+0.87	+15.22
UAH TWI <sup>1</sup>	138.257	+3.55	+13.95

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

### Market gov't bond quotes<sup>1</sup> (16 May 2022)

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

Source: ICU.

# Ukrainian bond market

## Foreigners reduce UAH bond portfolios

Foreign investors cut their portfolios of local-currency bonds after last Wednesday's redemption for the first time since russia's full-scale invasion of Ukraine.

Last week, almost UAH18bn (US\$0.6bn) of local-currency bonds were redeemed, and as a result, foreigners' portfolios of UAH-denominated bills declined for the first time since 24 February. Total local-currency bonds outstanding decreased by UAH13bn (US\$0.4bn), of which UAH2bn (US\$68m) is a decline in foreign investors' portfolios.

The offering of new 1.5-year paper attracted very limited interest last Tuesday. According to the primary auction result, UAH4.7bn (US\$159m) was raised for the budget of which just UAH87m (US\$3m) was via new paper. More details in the [auction review](#).

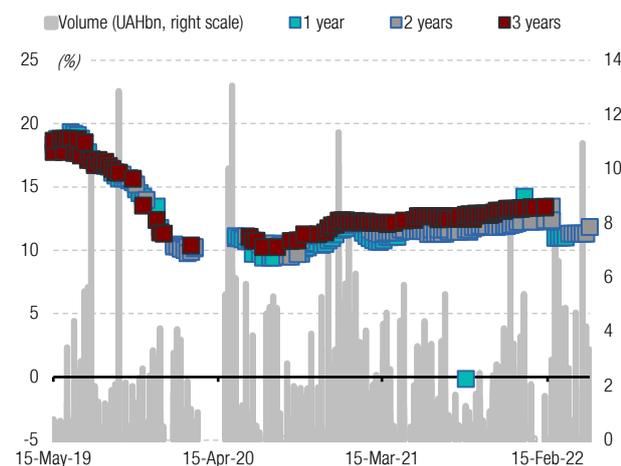
**ICU view: The NBU has only allowed the use of funds from principal and interest repayments of local-currency bonds for hard currency purchases beginning in April of next year (see comment below). Thus, foreigners are likely to gradually convert last week's debt repayments into new bills. We expect they will only have interest in securities maturing in early 2Q23 and will be reluctant to invest in debt with longer tenor.**

**Total investment of foreigners into Ukrainian domestic bonds stood at UAH72.4bn (equivalent of almost US\$2.5bn) as of 13 May 2022, about UAH2.4bn (US\$83m) down from 24 February when russia's invasion of Ukraine started.**

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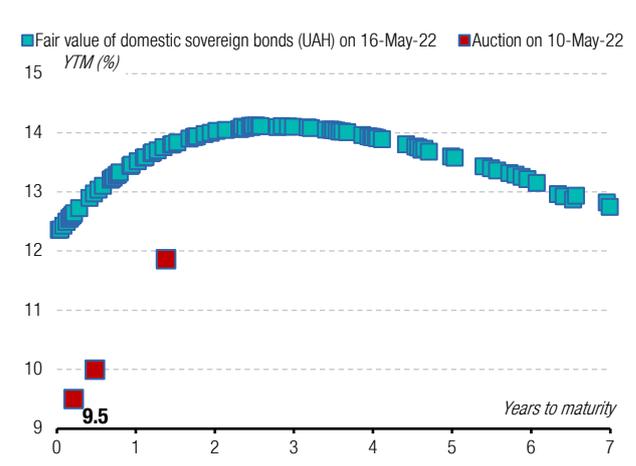
**Chart 1. Local-currency bonds**

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.

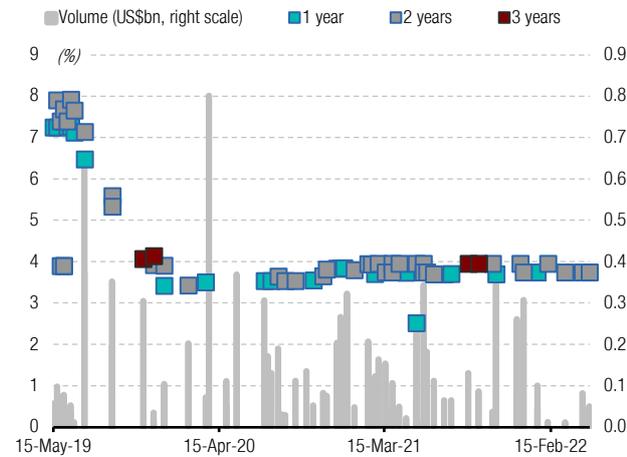
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



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

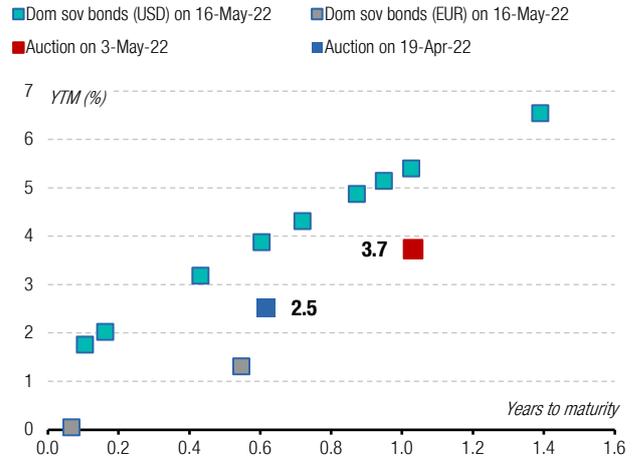
**Chart 2. FX-denominated bonds**

*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 prices rise slightly**

The price of Ukrainian Eurobonds rose during most of the last week, but declined moderately at the end of the week, still keeping some of the gains.

For most of last week, prices on Eurobonds were rising and gains reached as much as 10% for some of them. However, by the end of the week, the trend reversed, and WoW gains are 4-9%.

The price of securities with maturity this September increased the most, adding 5 cents per dollar to reach almost 64 cents. Other Eurobonds rose mostly by two cents to 35-44 cents per dollar. Along with Eurobonds, the price of VRIs rose by almost two cents to almost 33 cents per dollar.

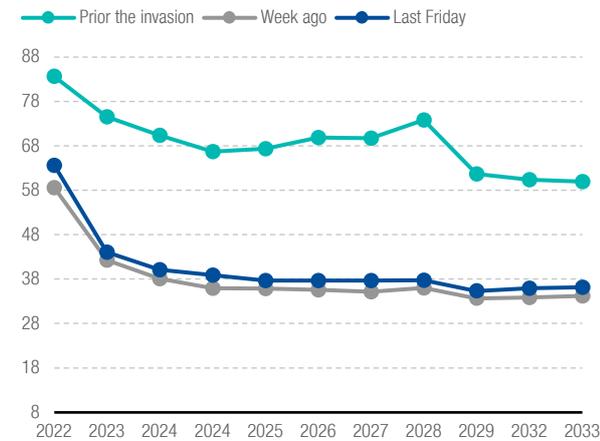
Last week, the US House of Representatives passed a bill to seek immediate bilateral, multilateral, and commercial debt-service payment relief for Ukraine. The draft is to be voted on by the Senate. The bill consists of three parts. One concerns instructing the US representatives in international financial institutions to take steps to immediately suspend all debt service payments owed to the institutions by Ukraine. The second proposes steps to ease debt payments on all multilateral and commercial debt so that it may be applied to Ukrainian Eurobonds. The third includes an increase of concessional financial assistance for Ukraine.

**ICU view: Although the bill passed by the US House of Representatives is highly beneficial for Ukraine, it has worried investors. They fear that international financial institutions will not only take steps to soften Ukraine's debt burden, but will, along with the US, encourage private creditors to do the same. Therefore, in the future, investors in Eurobonds will closely monitor messages from international financial institutions and Western governments on the approach they use to ease Ukraine's debt burden.**

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**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.

## Foreign exchange market

### NBU allows repatriation of UAH bond proceeds

Last week, the NBU amended its FX regulations such that foreign investors would be able to repatriate their investments without any limitations into local UAH-denominated bonds that mature after 1 April 2023.

The NBU imposed severe FX capital controls since Russia invaded Ukraine on 24 February, including a ban to buy hard currency with proceeds from local UAH bond redemptions and related coupons. The earlier version of the document did not provide any indication about when this ban would be lifted.

**ICU view:** *The news is positive as it provides more clarity about how the NBU intends to gradually liberalize the FX market and lift its tough FX restrictions. With new information in, non-residents who already have UAH bonds in their portfolios or keep cash in Ukrainian banks can now adjust their investment approaches. The NBU's decision may also encourage new inflows of non-resident money into local bonds in the future when the macro picture becomes more favourable.*

**We believe the indicated timeline for lifting the FX restrictions on UAH bonds is fully credible. Ukraine is in a good position to properly address its major economic challenges over the one-year horizon thanks to generous financial support from its allies.**

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## Economics

### Inflation keeps accelerating in April

Annual inflation increased further significantly to 16.4% YoY in April from 13.7% in March.

Food prices rose 4.2% MoM and 23.1% YoY and remain the key contributor to the high consumer inflation. Transportation was the second fastest-growing component of the CPI basket in terms of prices (+18.2%) on the back of surging fuel costs. Prices for clothes remain 6% lower than in last year's April.

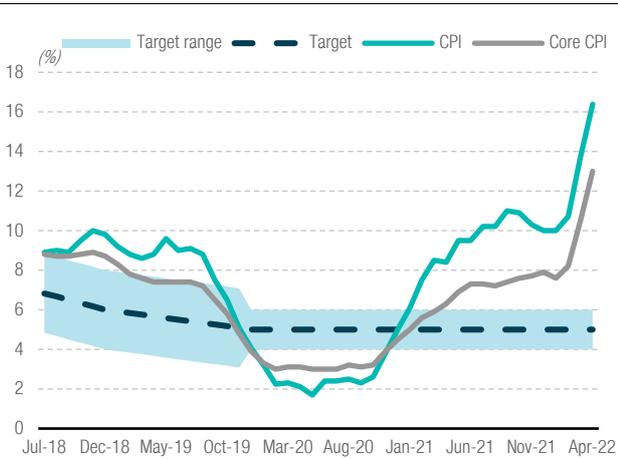
Core CPI, an index that better captures fundamental inflationary pressures, also accelerated considerably to 13.0% YoY from 10.5% YoY in March.

**ICU view: Ukraine’s inflation remains to be shaped by substantial supply-side constraints and surging transportation costs. An additional pro-inflationary factor in play is the growing costs of imports despite the fact that official UAH/USD exchange rate has remained unchanged since the beginning of the war. We expect inflationary pressures to stay high over the next 12-18 months and maintain our projection of CPI reaching 25-30% range in autumn.**

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**Chart 5. CPI, core CPI and target, YoY, %**

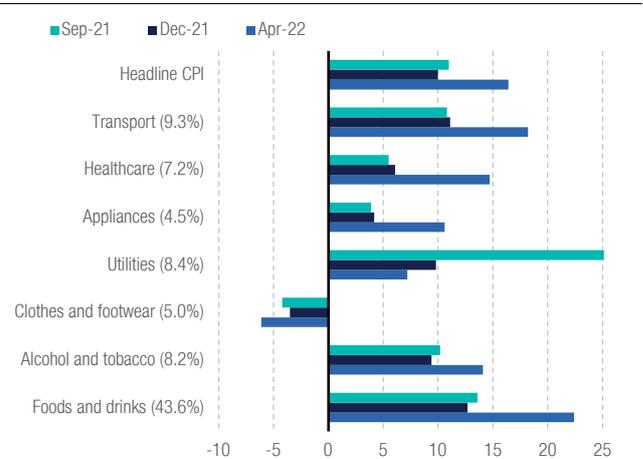
*Inflation keeps accelerating*



Source: Ukrstat, NBU, ICU.

**Chart 6. CPI and its main components, YoY, %**

*Food prices expectedly remain the key inflation driver*



Source: Ukrstat, ICU.

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