

Weekly Insight

Ukraine's real GDP declines 29% in 2022

Key messages of the today's comments

MONDAY, 17 APRIL 2023

Ukrainian bond market

Domestic bond market trading declines

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Minor volatility in Eurobonds prices

Ukrainian Eurobonds continued to fluctuate in a narrow range after the MoF announced a restructuring of Eurobonds is imminent.

Foreign exchange market

Activity in FX market low

Hard-currency trading last week was not very active, which led to a slight correction of the cash exchange rate.

Economics

Annual inflation continues to fall

Ukraine's annual inflation decelerated to 21.3% in February, down from 24.9% in February, as the high base effect comes into play.

Ukraine's real GDP declines 29% in 2022

Ukraine's real GDP contracted 29.1% YoY in 2022, according to Ukrstat's detailed statistics. The sharpest decline was reported for 2Q22 at 36.9% YoY when the economy was hit hardest by the Russia's invasion.

Banks' reserves market (14 April 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	25.00	+0bp	+1,500bp
ON rate (%)	9.76	+0bp	+0bp
Reserves (UAHm) ²	204,375	+5.45	+269.05
CDs (UAHm) ³	389,105	+5.00	+137.21

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) (14 April 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU	696,970	+0.00	+99.07
Banks	530,224	+0.13	-3.41
Residents	109,975	+0.36	+37.25
Individuals	37,030	+2.61	+41.08
Foreigners ¹	54,954	+1.11	-26.24
Total	1,432,480	+0.20	+32.64

Source: NBU, ICU.

FX market indicators (14 April 2023)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	36.9496	+0.46	+25.68
EUR/USD	1.0992	+0.80	+1.51
DXY	101.552	-0.53	+1.23
UAH TWI ¹	109.830	-0.85	-18.35

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

Market gov't bond quotes¹ (17 April 2023)

Maturity	Bid	Ask
6m	20.00	17.00
12m	22.00	18.00
2y	25.00	21.00
3y	26.00	22.00
12m (\$)	6.00	4.50
2y (\$)	N/A	N/A

Source: ICU.

Ukrainian bond market

Domestic bond market trading declines

The volume of borrowings for the budget and trading on the secondary market decreased significantly last week.

The Ministry of Finance borrowed only UAH2.4bn at the primary auction, including UAH1.5bn in hryvnia (see details in the [auction review](#)). This is the second lowest weekly volume this year.

Trading on the secondary market also declined. During the week, almost 6,535 deals were concluded, but most of them were small. The total volume of trading of UAH bonds in the secondary market for the week was only UAH3.2bn.

The largest volumes were traded in bonds maturing this week, in May 2024 and February 2025 (UAH1.8bn or 55% of total trades last week), but the number of deals was small. The most frequently traded paper was due in May, June, and October of this year, as well as June 2024. There were 3,914 deals, but the total volume of trading amounted to UAH162m for all four of these instruments.

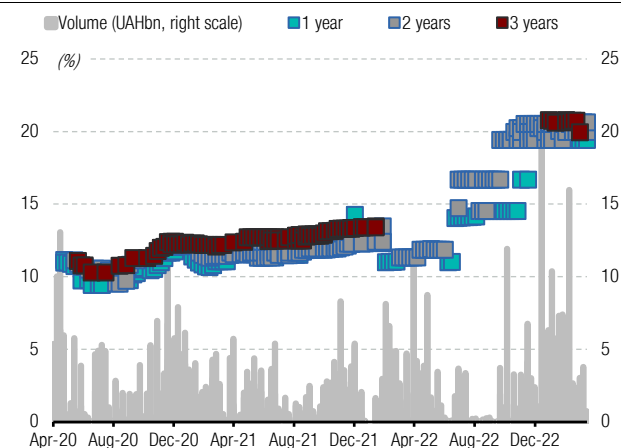
ICU view: Foreign investors were again focused on bonds that had a coupon payment in the coming months. Likely, they participated in the primary auction for the paper with the nearest coupon scheduled for June 2023, while at the same time selling two-year government bonds from their portfolios. Individuals bought short bonds maturing this year and military bills maturing in June 2024, available now through the Diia app and named "Yalta."

As MoF is facing UAH13bn in redemptions this week, they will offer four issues to refinance these repayments: two military bills maturing next year, ordinary bonds maturing in October 2024, and "reserve" paper maturing in April 2025. Therefore, demand may increase, but it is unlikely that this week's redemption will be refinanced in full.

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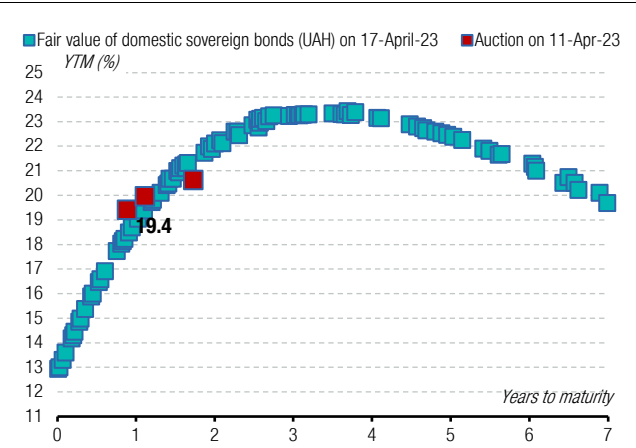
Chart 1. Local-currency bonds

Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)



Source: MFU, ICU.

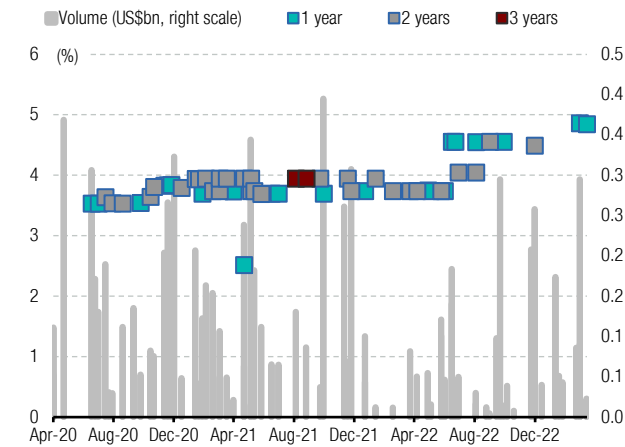
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

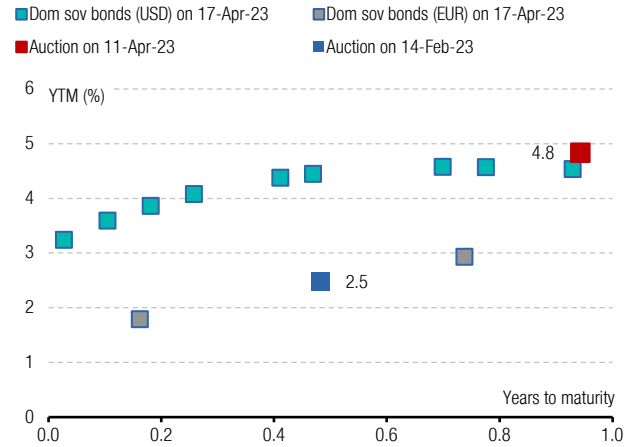
Chart 2. FX-denominated bonds

Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)



Source: MFU, ICU.

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



Source: NBU, MFU, ICU.

Minor volatility in Eurobonds prices

Ukrainian Eurobonds continued to fluctuate in a narrow range after the MoF announced a restructuring of Eurobonds is imminent.

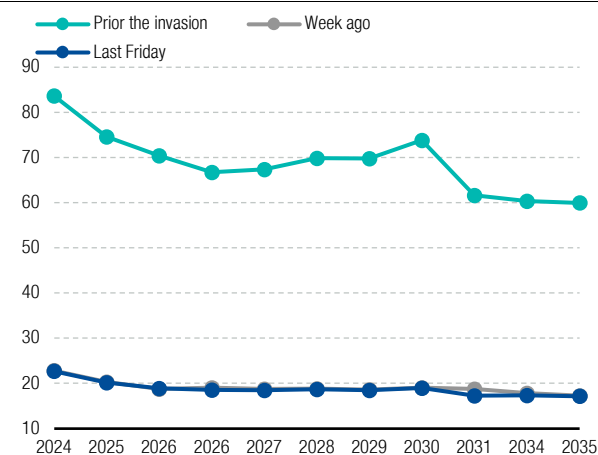
All last week, the quotations of sovereign Eurobonds remained in the usual range of 17–23 cents, and VRIs price fell to less than 27 cents per dollar of notional value.

ICU view: Uncertainty over further developments in the war with russia and the just-announced-for-next-year debt restructuring without any details, lead to minor changes in the prices of Eurobonds. Risk balancing for all bond issues keeps prices in a narrow range.

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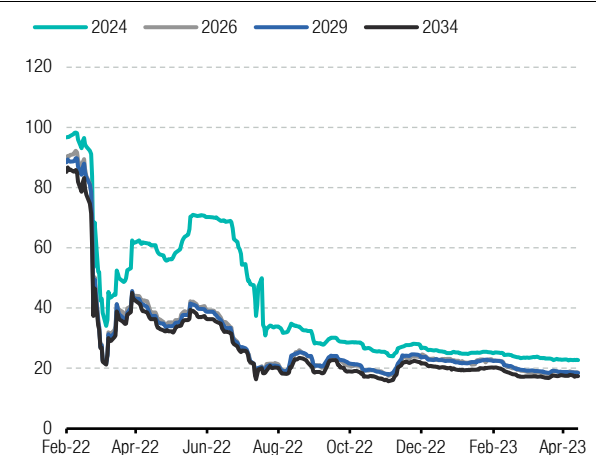
Chart 3. Ukrainian Eurobonds prices

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



Source: Bloomberg, ICU.

Historical data since February, 2022



Source: Bloomberg, ICU.

Foreign exchange market

Activity in FX market low

Hard-currency trading last week was not very active, which led to a slight correction of the cash exchange rate.

Purchases of non-cash hard currency by retail customers further decreased last week. In four days of the last week, the sale of non-cash FX by households exceeded purchases (by US\$1.6m) for the first time since last September. In the cash segment, in four days, households purchased hard currency of US\$39m more than they sold.

During the week, the cash exchange rate in systemically important banks slightly declined by 0.3–0.5% to UAH37.39–38.06/US\$ with a tightening of the spread between the bid-offer rates to UAH0.67.

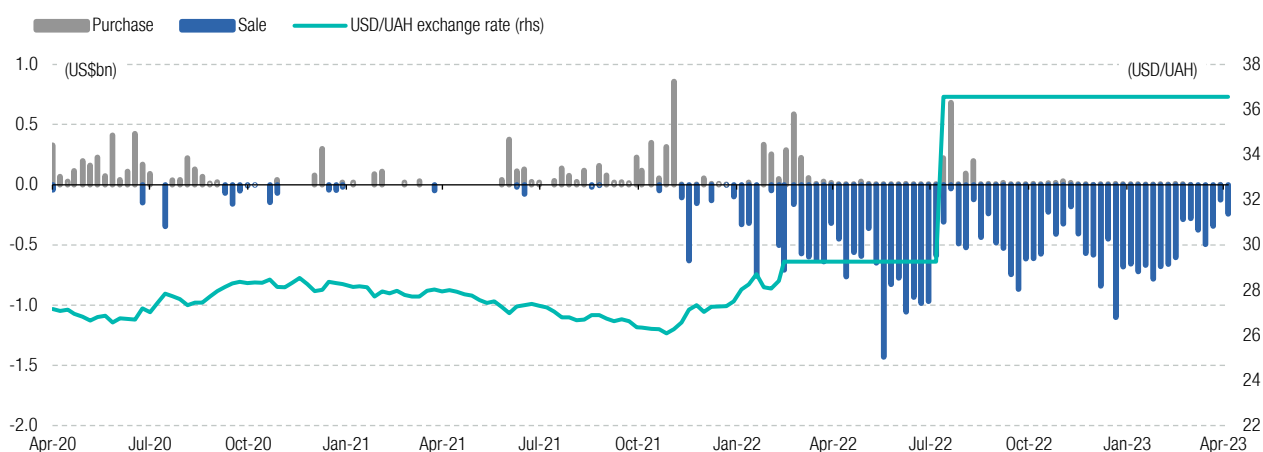
On the interbank market banks reduced hard currency trading volumes for the second week in a row. However, the volume of NBU interventions on the sale of hard currency almost doubled to US\$243m.

ICU view: In the cash market, the demand for hard currency prevails over supply, but this has almost no effect on the cash exchange rate. The activity in the interbank market declined due to Easter weekend in the USA and Europe, which allowed the NBU to keep its sale interventions low.

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Chart 4. 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

Annual inflation continues to fall

Ukraine's annual inflation decelerated to 21.3% in February, down from 24.9% in February, as the high base effect comes into play.

Even though consumer prices increased 1.5% MoM, significantly higher than the 0.7–0.8% increases in November–February, annual inflation decelerated notably. The key contributors to disinflation were prices for food (26.5% YoY in March vs. 31.5% in February) and transportation services (27.1% vs. 33.6%). A deceleration was registered for nearly all

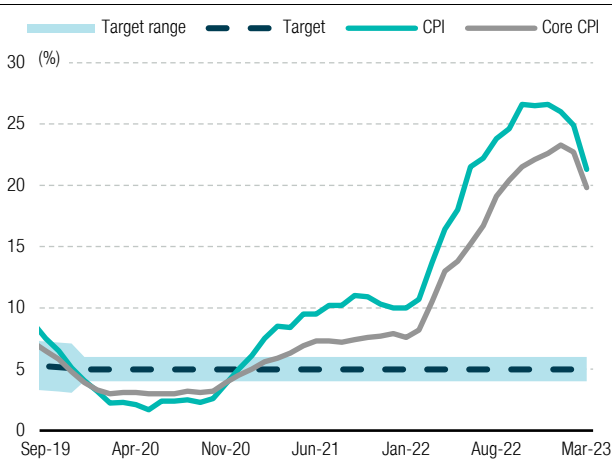
components of the consumer basket, except for two groups that account for an insignificant part of total consumption, i.e., telecommunications and education. The pace of growth in price for these either stayed flat or accelerated marginally.

ICU view: The rate of growth in consumer prices will continue to fall in the coming months as the base effect will play a prominent role. Last year, russia's full-scale invasion disrupted production and logistics forcing producers and retailers to hike prices in the spring months. Absent these effects, monthly inflation declined considerably making annual numbers fall unprecedentedly. Slower inflation in Ukraine is also supported by a stable exchange rate, stable regulated tariffs for utilities, and declining global food prices. We expect consumer inflation will decelerate to the 15–16% range by the end of 2023. This projection implies that NBU will have fewer and fewer reasons to keep its key policy rate at the current high level. We, therefore, project it will be lowered to 20% by the end of 2023.

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

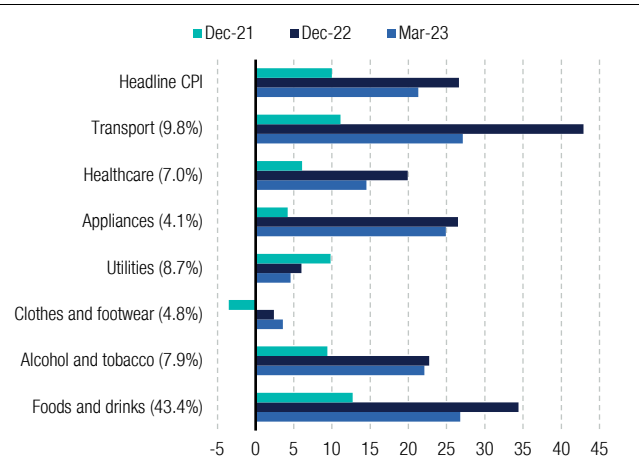
Annual inflation decelerates sharply



Source: Ukrstat, NBU, ICU.

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

Prices for food and transport decelerated the most



* numbers in brackets indicate the share of the component in consumer basket

Source: Ukrstat, ICU.

Ukraine's real GDP declines 29% in 2022

Ukraine's real GDP contracted 29.1% YoY in 2022, according to Ukrstat's detailed statistics. The sharpest decline was reported for 2Q22 at 36.9% YoY when the economy was hit hardest by the russia's invasion.

Nominal GDP is estimated at UAH5,191bn (-5% YoY), exceeding official and our projections due to an extremely high 2022 GDP deflator of 34.3% on the back of surging prices in the defense sector. In FX terms, GDP amounted US\$161bn (-20% YoY) based on the 2022 official average exchange rate.

The performance of the economy was not uniform. Construction, transportation, and manufacturing were hit the hardest due to destruction of production facilities, impaired logistics, and the dry-up of investments. Sectors that depend heavily on budget, like education and healthcare, suffered to a lesser extent thanks to uninterrupted financing. The only notable exception from the broad pattern is the sector of state governance, which includes defense and law enforcement. It grew 35% in real terms on surging outlays to the military sector. Accounting for the change in prices, the share of state governance in total GDP increased by 15pp YoY to a whopping 21.1%.

ICU view: Massive outlays on defense that were facilitated by international financial assistance prevented an even deeper decline in Ukraine's GDP in 2022. However, they are unlikely to have a positive contribution to real GDP in 2023. We expect the economy will expand marginally by about 2% this year on the back of the improved safety situation and logistics. On the demand side, this small recovery will be largely driven by household consumption.

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Table 1. Ukraine's GDP in 2022

The structure of Ukraine's GDP changed considerably due to the war

Sector	Production method			GDP component	Consumption method		
	Share in nominal GDP	Change in share, YoY	Real change YoY		Share in nominal GDP*	Change in share, YoY	Real change YoY
Agriculture	8.2%	-2.7pp	-28%	Household consumption	64%	-3.8pp	-27%
Extraction industry	5.7%	-0.7pp	-32%	Government consumption	38%	20.5pp	18%
Manufacturing	7.6%	-2.7pp	-43%	Net fixed capital formation	12%	-1.6pp	-34%
Power supply	4.5%	1.1pp	-33%	Exports	35%	-5.2pp	-42%
Construction	1.2%	-1.5pp	-68%	Imports	-52%	-10.2pp	-19%
Trade	12.4%	-1.3pp	-31%				
Transportation	3.9%	-1.5pp	-44%				
Telecommunications	4.6%	-0.1pp	-15%				
Financial services	2.9%	-0.1pp	-16%				
Real estate	4.9%	-0.9pp	-35%				
Professional activities and science	1.9%	-1.0pp	-46%				
State governance (incl defense)	21.1%	15.0pp	35%				
Education	4.2%	-0.2pp	-11%				
Health care	2.4%	0.0pp	-18%				
Other	2.9%	-1.1pp	na				
Taxes net of subsidies	11.8%	-2.3pp	na				

* shares do not add up to 100% due to omitted other minor components

Source: Ukrstat, ICU.

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