



Focus
Ukraine

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

Research team
Vitaliy Vavryshchuk
Alexander Martynenko
Taras Kotovych
Mykhaylo Demkiv

Weekly Insight

NBU may cut rate earlier

Key messages of the today's comments

Ukrainian bond market

Foreigners have renewed interest in primary auctions

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New Eurobonds rally

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Foreign exchange market

NBU's first FX liberalization moves are modest

The NBU allowed resident borrowers to transfer funds abroad to meet their liabilities, but only for a very narrow category of external loans.

Economics

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MONDAY, 19 JUNE 2023

Banks' reserves market (16 June 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	25.00	+0bp	+0bp
ON rate (%)	9.76	+0bp	+0bp
Reserves (UAHm) ²	200,347	-0.34	+235.65
CDs (UAHm) ³	449,933	+3.45	+159.68

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) (16 June 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU	694,346	+0.00	+39.26
Banks	543,859	-0.88	+2.65
Residents	117,848	+0.84	+67.85
Individuals	41,546	+0.01	+44.69
Foreigners ¹	51,401	+1.64	-27.69
Total	1,452,610	-0.18	+21.20

Source: NBU, ICU.

FX market indicators (16 June 2023)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	36.9313	+0.00	+24.82
EUR/USD	1.0937	+1.75	+3.68
DXU	102.243	-1.27	-1.34
UAH TWI ¹	111.531	-0.57	-19.17

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

Market gov't bond quotes (19 June 2023)

Maturity	Bid	Ask
6m	18.00	16.00
12m	21.00	18.00
2y	23.00	20.00
3y	23.50	20.50
12m (\$)	6.00	4.50
2y (\$)	N/A	N/A

Source: ICU.

Ukrainian bond market

Foreigners have renewed interest in primary auctions

Last week, the Ministry of Finance attracted one of the lowest amount of funds in local currency to the budget YTD, a part of which was from foreign investors.

At last Tuesday's primary auction, the MoF sold UAH-denominated bills for UAH2.5bn (US\$69m), mainly with 1-year and 1.5-year maturities. See details in the [auction review](#).

Last week, trading in the secondary market was more evenly distributed between different bond issues than in previous weeks. Bonds maturing in 2027 were the most actively traded (23% of all trades in UAH bonds). Bills with the nearest coupon payment in September and November followed with a 13% and 10% share respectively. The share of "reserve" bonds due in April 2025 and with the nearest coupon in October was 12%.

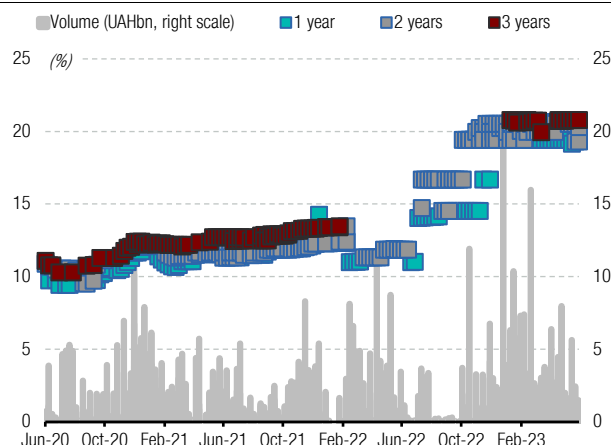
The foreign investors' portfolios of UAH government bonds grew the most — by UAH1bn (US\$29m) in a week — exceeding UAH50bn (US\$1.4bn), the largest amount since the sharp drop at the end of May.

ICU view: Auction results and data on trading in the secondary market indicate that foreigners could have bought a significant part of the auctioned government bonds. They may also be changing the term structure of their portfolios so as to optimize the volume of funds eligible for repatriation this autumn.

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

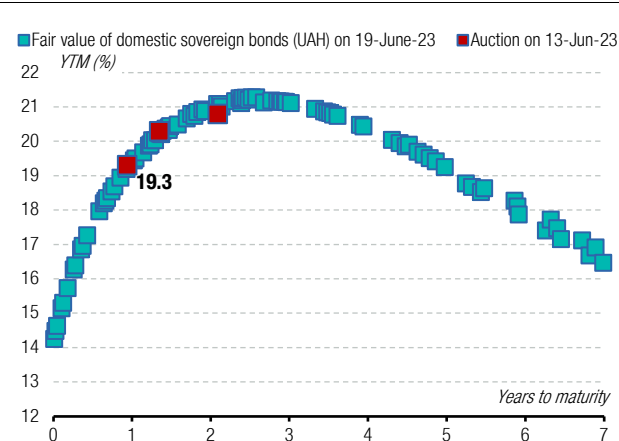
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

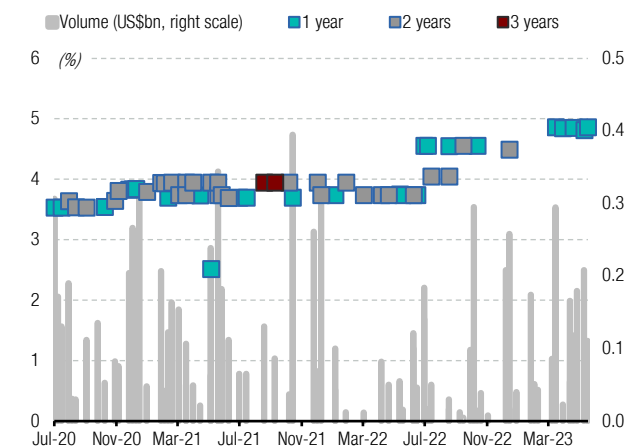
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

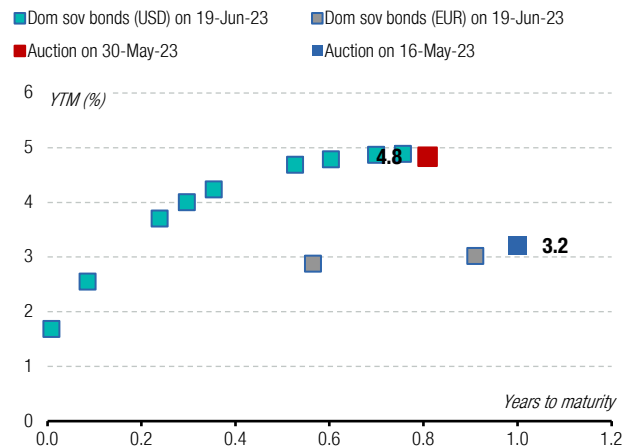
Chart 2. FX-denominated bonds

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.

New Eurobonds rally

Ukrainian Eurobonds ended last week with a sharp rise in prices and a narrowing of the price range across different maturities.

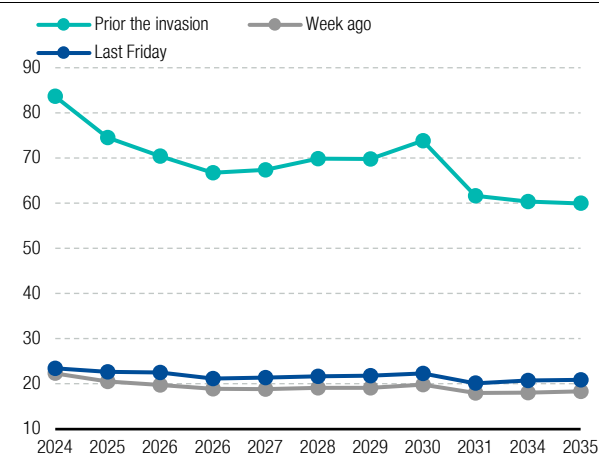
For most of the last week, Eurobonds were quoted in a range close to those of the previous weeks: 18–22 cents. But on Thursday, prices were up approximately 2%, and on Friday, up further by another 4–12%. All in, Ukrainian Eurobonds ended the week with a price increase of 5–14%. The price range shifted to 20–23 cents, with a narrowing to 7.5%. VRIs also rose in price last week by almost 25% to 36 cents per dollar of notional value.

ICU view: At the end of last week, Ukrainian sovereigns saw a new wave of demand, likely supported by a combination of positive news. Against the background of the launch of the Ukrainian counteroffensive, another Ramstein-format meeting was held in Brussels, where a new package of military support for Ukraine was announced. Also, the first Ukraine-NATO meeting since 2016 took place in Brussels, and representatives of NATO countries spoke positively about Ukraine having good chances of joining the alliance after the war. In addition, the Financial Times published information that US senators introduced a bipartisan bill that would allow the seizure and transfer of Russian sovereign assets to Ukraine.

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

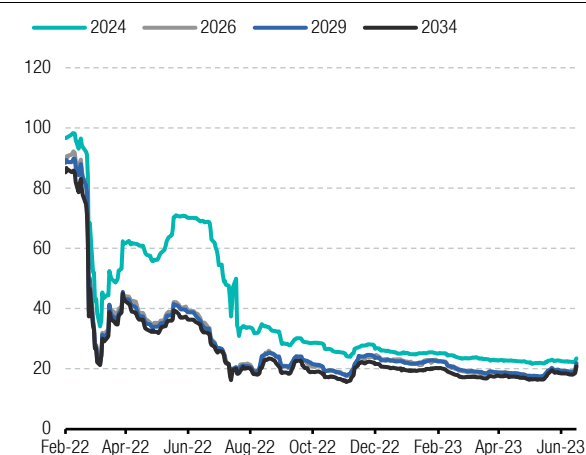
Chart 3. Ukrainian Eurobonds prices

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

NBU's first FX liberalization moves are modest

The NBU allowed resident borrowers to transfer funds abroad to meet their liabilities, but only for a very narrow category of external loans.

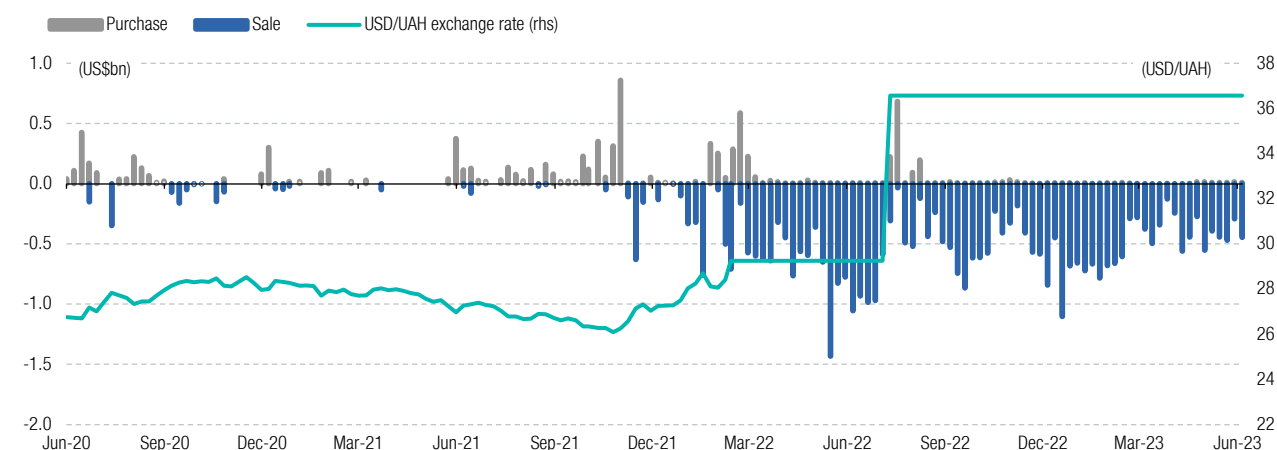
Last week, the NBU allowed residents to transfer funds abroad to fulfill obligations under external loans secured by a guarantee or surety of an international financial organization or those involving a foreign export credit agency or a foreign state.

The cash FX market remained stable at the beginning of last week, but in the last days of the week, the hryvnia exchange rate in systemically important banks strengthened slightly by 0.1% to UAH36.75–37.36/US\$.

In the interbank FX market, the volume of hard currency purchases by bank clients (legal entities) increased by 19% in four business days. Their sale of hard currency in the same period decreased by 3%. Therefore, the imbalance between supply and demand increased fivefold to US\$220m and led to a 53% increase in NBU FX sale interventions to US\$447m.

ICU view: The NBU's first steps towards FX market liberalization were extremely modest, probably a sign that the NBU is not ready to make bold moves in this direction in the coming months or quarters. However, it is still worth waiting for the publication of the FX liberalization roadmap. The NBU's decision last week is unlikely to affect demand for hard currency on the interbank market or the volume of NBU interventions.

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

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

NBU may cut rate earlier

The key rate was kept unchanged at 25%, in line with expectations, but falling inflation may urge the regulator to cut the rate in 3Q23.

During the previous decision on the key monetary policy rate, the NBU has significantly improved its forecast eyeing for a rate cut in 4Q23 rather than 2Q24. While no update for its macro forecast was due at this time, NBU announced it may cut the rate earlier.

ICU view: *There are two rate reviews in the next quarter scheduled for July 27 and September 14. We expect the latter to be a more likely date for the first rate cut since NBU imposed a 25% key rate a year ago. We expect NBU to cut the rate by 500bp by the end of the year.*

Mykhaylo Demkiv, Kyiv, (044) 377-7040 ext.723

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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

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