

# Weekly Insight

## NBU changes monetary policy design

### Key messages of the today's comments

MONDAY, 30 OCTOBER 2023

### Ukrainian bond market

#### MinFin lowers rates on UAH bonds

The MoF took advantage of market expectations of a NBU policy rate cut last Thursday and lowered interest rates on UAH bonds by approximately 20bp.

#### Eurobonds under impact from global sentiment

Prices of Ukrainian Eurobonds remained volatile under the impact from global sentiment on emerging markets.

### Foreign exchange market

#### FX market stabilises

The FX market remains under NBU control as it is adjusting to the new exchange-rate regime.

### Economics

#### Ukraine's public debt broadly unchanged in September

Ukraine's public debt inched down 0.2% in US\$ terms in September to US\$133.6bn.

#### NBU changes monetary policy design

The NBU has cut the key policy rate by 400 bps, to 16% from 20%.

### Banks' reserves market (27 October 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) <sup>1</sup>	16.00	-400bp	-900bp
ON rate (%)	9.76	+0bp	+0bp
Reserves (UAHm) <sup>2</sup>	216,172	+3.07	+249.46
CDs (UAHm) <sup>3</sup>	439,806	-4.29	+51.19

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) (27 October 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU	690,693	+0.00	+8.84
Banks	601,617	+1.38	+20.62
Residents	125,280	-1.37	+89.13
Individuals	47,684	-1.74	+53.87
Foreigners <sup>1</sup>	47,159	-0.05	-22.49
<b>Total</b>	<b>1,513,961</b>	<b>+0.37</b>	<b>+17.14</b>

Source: NBU, ICU.

### FX market indicators (27 October 2023)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	36.5100	-0.32	-0.82
EUR/USD	1.0565	-0.27	+6.03
DXY	106.559	+0.37	-3.64
UAH TWI <sup>1</sup>	116.188	+0.49	+0.27

Notes: [1] UAH trade-weighted index.

Source: Bloomberg, ICU.

### Market gov't bond quotes (30 October 2023)

Maturity	Bid	Ask
6m	18.00	15.00
12m	19.50	17.50
2y	20.00	18.25
3y	20.25	18.75
12m (\$)	5.00	4.50
2y (\$)	N/A	N/A

Source: ICU.

# Ukrainian bond market

## MinFin lowers rates on UAH bonds

The MoF took advantage of market expectations of a NBU policy rate cut last Thursday and lowered interest rates on UAH bonds by approximately 20bp.

Last week's primary auction saw a decline in interest rates for all offered UAH bonds by 18-26bp, which happened for the first time this year. Demand for local-currency instruments was UAH19.5bn (US\$535m) with non-competitive bids making up 30% to 90% of the volume. The range of interest rates in competitive bids was 20–33bp. The MoF accepted only some competitive bids with the lowest rates. The Ministry sold UAH12.2bn (US\$334m) of UAH bonds (par value), receiving UAH12.4bn (US\$340m) for budget needs. In addition, the MoF sold a new issue of USD-denominated bills for US\$300m (par value) at a 4.8% cut-off rate. See details in the [auction review](#).

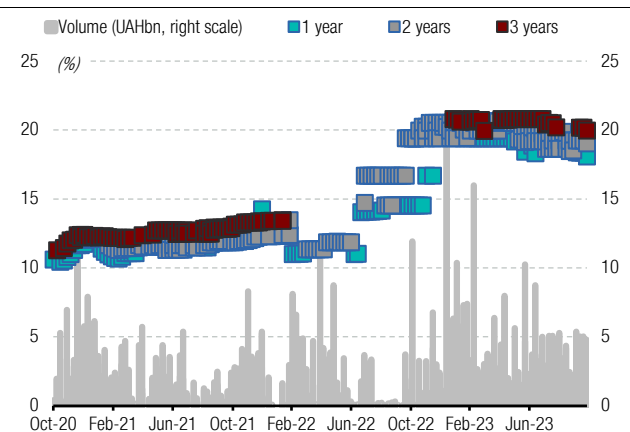
In the secondary bond market, trading amounts rose: by 13% to UAH6.6bn (US\$182m) in local-currency bonds and by 0.7% to UAH9.1bn (US\$250m) in FX-denominated securities. Last week was the third consecutive week when trading in FX-denominated bonds exceeded trading in local-currency securities. The most traded were just three bond issues: UAH "reserve" notes allowed to cover reserves from November 11 (UAH3.5bn), USD-denominated bills due February 2024 (UAH4.4m), and USD-denominated paper issued last week (UAH2.9bn).

**ICU view: Expecting the NBU policy rate cut, investors preferred the primary auction. Much of the demand was non-competitive, allowing investors to buy part of the desired amount at the weighted-average interest rate. The MoF took advantage of oversubscription, rejecting most competitive bids and setting cut-off rates close to the lowest submitted interest rates. The NBU's decision to cut the key policy rate while keeping rates on its operations unchanged may imply rates will remain little changed for a couple of weeks. However, the NBU indicated that it can decrease the key rate and interest rates for NBU CDs in December, leaving room for a decline in bond rates until the end of the year.**

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

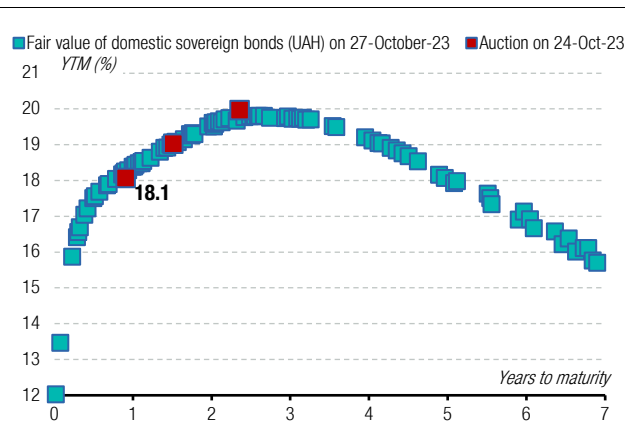
**Chart 1. Local-currency bonds**

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



Source: MFU, ICU.

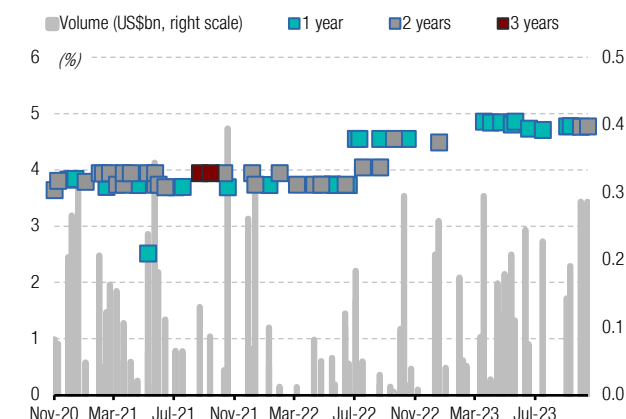
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

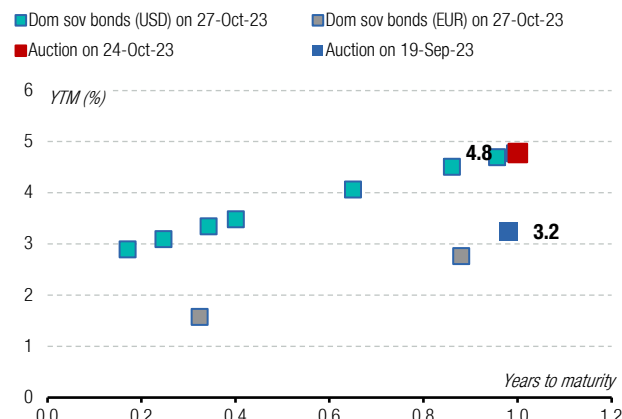
**Chart 2. FX-denominated bonds**

*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.

**Eurobonds under impact from global sentiment**

Prices of Ukrainian Eurobonds remained volatile under the impact from global sentiment on emerging markets.

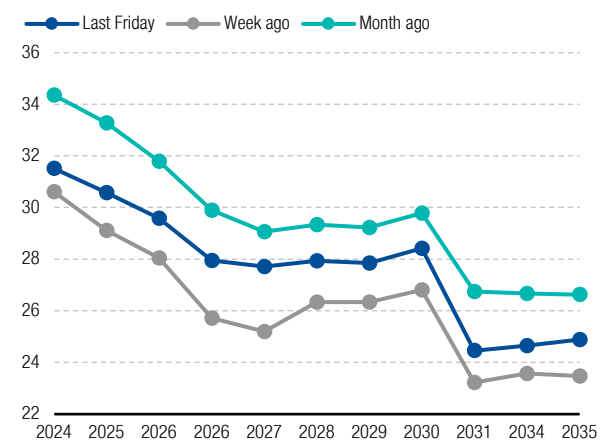
Last week, prices increased by an average of 3% to 24–31 cents. The price range for instruments with different maturities tightened to 12.6%. VRI prices are up by 1%, with quotes at around 41 cents per dollar of notional value. The EMBI index rose by 0.9%

**ICU view:** *Global sentiment toward emerging markets remains the key factor for valuing Ukrainian Eurobonds while low liquidity amplifies the volatility. Uncertainty regarding financial assistance from the US for Ukraine for 2024 remains after the Speaker of the House of Representatives was elected, but investors have likely priced in this risk already. In the next few weeks, investors’ focus will likely be on US Congress discussions of aid to Ukraine. It is very likely that many Republicans voted for the new speaker as they got a promise that, among other things, he will bring the issue of aid to Ukraine for consideration by the House of Representatives. Last week’s news about the EU plans to transfer interest income from Russian assets to Ukraine may help improve investor sentiment.*

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

**Chart 3. Ukrainian Eurobonds prices**

Prices of USD-denominated Eurobonds as of last Friday, a week and a month ago



Source: Bloomberg, ICU.

Historical data since February, 2022



Source: Bloomberg, ICU.

## Foreign exchange market

### FX market stabilises

The FX market remains under NBU control as it is adjusting to the new exchange-rate regime.

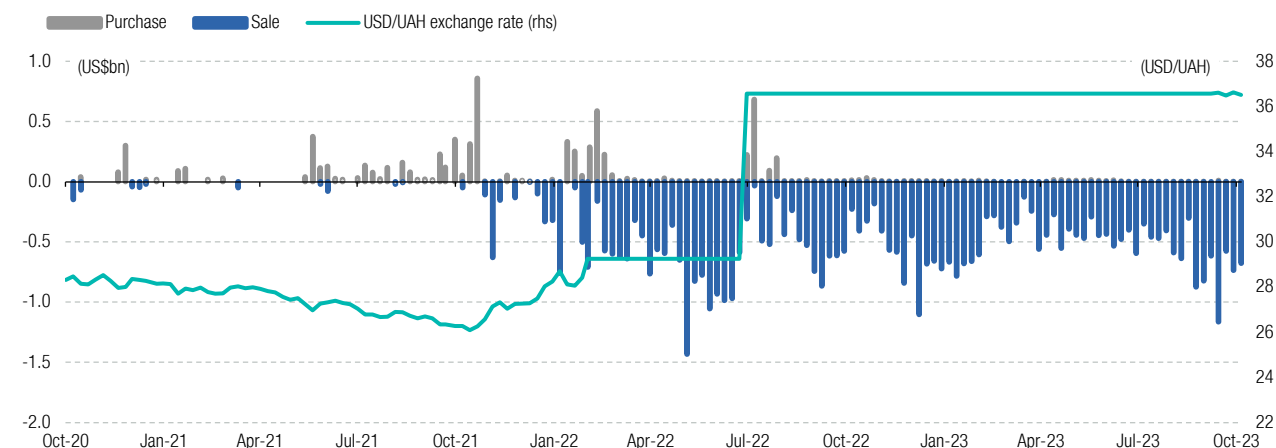
In the interbank FX market, bank clients (legal entities) decreased purchases of hard currency (in four business days) by 6% and selling by 4% compared with the same period of the previous week. The NBU decreased interventions by 8% to US\$676m. The official exchange rate strengthened by 0.3% to UAH36.42/US\$.

**ICU view:** *NBU's weekly interventions remain above YTD averages. However, the rules of NBU interventions caused little volatility and no hryvnia weakening so far. Market imbalances declined somewhat, indicating that businesses and households are no longer worried over managed exchange-rate flexibility. However, we expect that volatility will rise, and the NBU will allow moderate hryvnia devaluation by the end of the year.*

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

### Ukraine’s public debt broadly unchanged in September

Ukraine’s public debt inched down 0.2% in US\$ terms in September to US\$133.6bn.

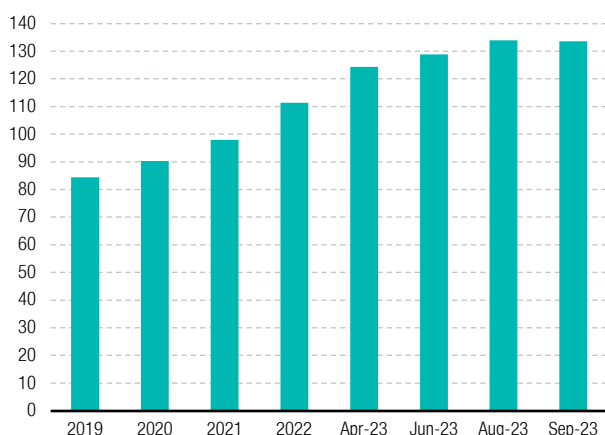
In September, the key drivers of debt were a new EU loan for EUR1.5bn and repayment of loans to IFIs for a total of nearly US\$0.9bn.

**ICU view: We maintain our projection of end-2023 public debt-to-GDP ratio landing in the range of 80–85%. This ratio will continue to grow at least for the next three years as fiscal consolidation is unlikely to be fast. However, there are good chances that at its peak value the ratio will not exceed 100%.**

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

**Chart 5. Ukraine’s public debt, \$bn**

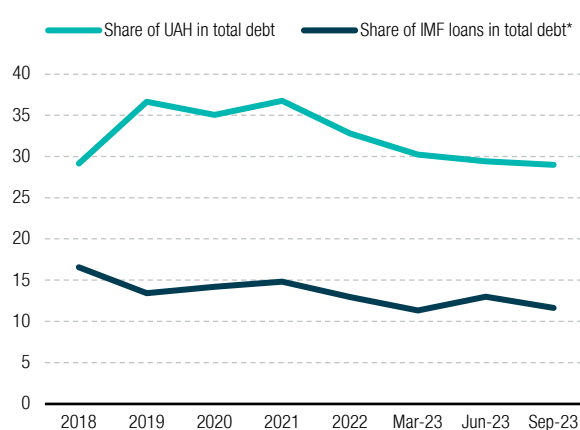
Public debt down 0.2% in September



Source: MoF, ICU.

**Chart 6. Share of UAH and IMF loans\* in total public debt, %**

Share of debt from IMF declined on substantial repayments



\* includes IMF SDR allocation

Source: MoF, ICU.

## NBU changes monetary policy design

The NBU has cut the key policy rate by 400 bps, to 16% from 20%.

At the same time, interest rates on CDs and refinance loans remain unchanged. Prior to this adjustment, the three-month CD rate was equal to the key rate, whereas the overnight CD rate was lower by 400bps. Following these changes, the rate for overnight CDs now matches the key rate. Meanwhile, three-month CD rate carries a premium of 400bps over the key rate.

***ICU view: Despite the seemingly bold move, this cut changes nothing in terms of the interest rates at which commercial banks can borrow or place their liquidity. Meanwhile, The Ministry of Finance will benefit from such changes as a coupon on UAH280bn of military bonds in NBU's portfolio is derived from the key rate. A lower monetary policy rate would imply a lower cost of servicing that debt for the government.***

***The NBU has presented an updated macro forecast and gave an unusually strong forecast of a 100bps rate cut in December 2023. Currently, the regulator does not expect any changes in key rate throughout 2024, as its base-case scenario implies a full 12-month period of intense war with russia. This outlook is likely to slow the fall of the interest rates in UAH deposits, as the NBU is keen to keep UAH assets attractive against the expected surge in inflation and likely weakening of the UAH.***

*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](http://www.icu.ua)



## RESEARCH

### Vitaliy Vavryshchuk

Head of macro research  
[vitaliy.vavryshchuk@icu.ua](mailto:vitaliy.vavryshchuk@icu.ua)

### Taras Kotovych

Senior financial analyst (Sovereign debt)  
[taras.kotovych@icu.ua](mailto:taras.kotovych@icu.ua)

### Dmitriy Dyachenko

Financial analyst  
[dmitriy.dyachenko@icu.ua](mailto:dmitriy.dyachenko@icu.ua)

### Alexander Martynenko

Head of corporate research  
[alexander.martynenko@icu.ua](mailto:alexander.martynenko@icu.ua)

### Mykhaylo Demkiv

Financial analyst (Banks)  
[mykhaylo.demkiv@icu.ua](mailto:mykhaylo.demkiv@icu.ua)

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