Focus
Ukraine

Markets
Government bonds, FX market, and macro

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Weekly Insight

Another key rate cut

Key messages of the today's comments

Ukrainian bond market

Investors diversify bond maturities

Last week, interest in UAH war bonds was primarily in instruments maturing in 2026, that are currently available only in the secondary market.

Concern about delay of Ukraine's financial aid lingers

Ukrainian Eurobond prices declined last week because there was no positive news about financial aid.

Foreign exchange market

Hryvnia weakens on higher trading

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Economics

Another key rate cut

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DUE TO HOLIDAY SEASON WE PLAN TO SEND THE NEXT WEEKLY ON JANUARY 8, 2024.

MONDAY, 18 DECEMBER 2023

Banks' reserves market (15 December 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%)[1]	15.00	-100bp	-1,000bp
ON rate (%)	15.00	-100bp	-800bp
Reserves (UAHm)[2]	184,450	-9.0	+134.7
CDs (UAHm)[3]	555,570	+6.4	+45.3

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) (15 December 2023)

	Last	Weekly chg (%)	YoY chg (%)
NBU	689,990	+0.0	+0.1
Banks	635,623	+0.9	+30.9
Residents	134,802	+0.6	+73.8
Individuals	52,358	+1.8	+72.0
Foreigners	44,553	+0.1	-22.6
Total	**1,559,351**	**+0.5**	**+16.2**

Source: NBU, ICU.

FX market indicators (15 December 2023)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	37.0472	+0.8	+0.4
EUR/USD	1.0895	+1.2	+2.5
DXY	102.550	-1.4	-1.9

Market gov't bond quotes (18 December 2023)

Maturity	Bid (%)	Ask(%)
6 months	17.50	15.00
12 months	18.50	17.00
2 years	19.50	18.00
3 years	20.00	18.75
12 months ($)	5.00	4.50
2 years ($)	N/A	N/A

Source: ICU.

Ukrainian bond market

Investors diversify bond maturities

Last week, interest in UAH war bonds was primarily in instruments maturing in 2026, that are currently available only in the secondary market.

Last week, the Ministry of Finance raised only UAH5.2bn at the primary auction. Investors were more interested in one-year bills than in two- and three-year securities. Demand for one-year paper was more than double supply, and the MoF sold its planned volume of bills with a minimal decline in interest rates of 2–4bp. See details in the auction review.

The total volume of UAH bond trading in the secondary market more than doubled WoW to UAH9bn. The most traded securities were paper due in 2026 (57% of all UAH bond trades) and in December 2024 (14%). At the same time, the share of one-year bills that entered the market last week was only 3% of all UAH bond trades. Trades in FX-denominated bills fell 2x compared with the previous week, to UAH1.1bn, the smallest volume since early February.

As a result, the portfolios of all investor groups grew for the third week in a row. Individuals' portfolios increased the most, by 1.5%.

ICU view: In the absence of debt redemptions over three consecutive weeks, investors are gradually increasing holdings of government bonds. The next repayment is scheduled at the end of the year. Investors purchase both new issues at the primary auction and also instruments available only in the secondary market, thus diversifying investments by maturity.

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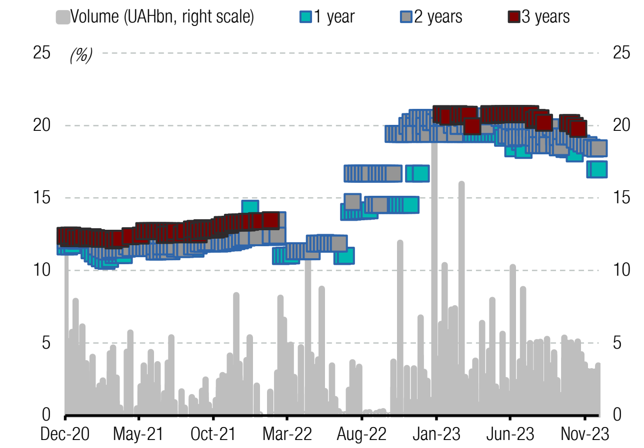
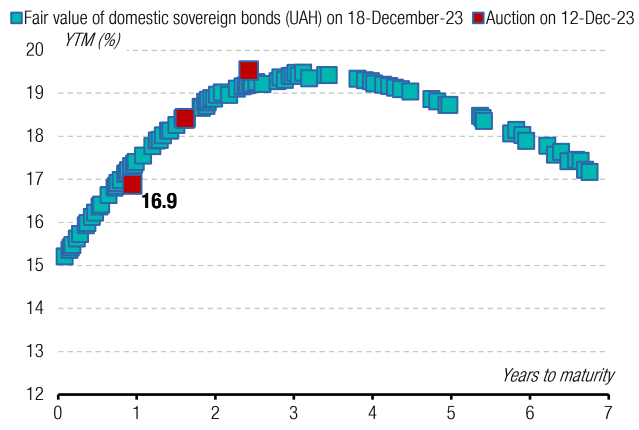
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

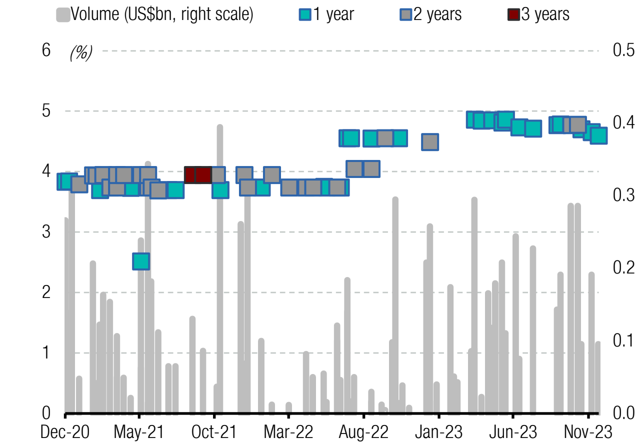
YTMs of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

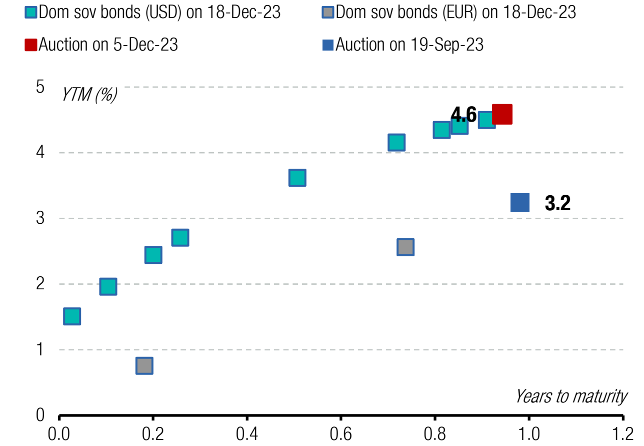
Chart 2. FX-denominated bonds

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



Source: MFU, ICU.

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



Source: NBU, MFU, ICU.

Concern about delay of Ukraine's financial aid lingers

Ukrainian Eurobond prices declined last week because there was no positive news about financial aid.

Due to Hungary's veto, the EU could not agree on a four-year aid package for Ukraine and will again attempt to take a decision in early January. There also remains significant uncertainty about the prospects for approval of the aid package for Ukraine by the US Congress. At the same time, the newly published IMF Memorandum does not provide new information about the prospects and conditions for Ukraine's sovereign Eurobond restructuring.

Ukrainian Eurobonds lost an average of 2.5% over the past week, declining to 24–31 cents per dollar. The price range for Ukrainian Eurobonds with different maturities narrowed to 12.3%. The price of VRIs slid by 3% to 45 cents per dollar of notional value. The EMBI index increased by another 2.2% over the past week.

ICU view: The new Memorandum with the IMF confirms that the government will restructure sovereign Eurobonds in 2024. So, the likelihood of a scenario where the government will prefer to maintain the status quo (suspension of all coupon and principal payments) and postpone full-scale restructuring is currently low. In the absence of new significant information about the possible terms of restructuring in the Memorandum, investors will focus on the progress of approval of Ukraine's financial assistance by key allies.

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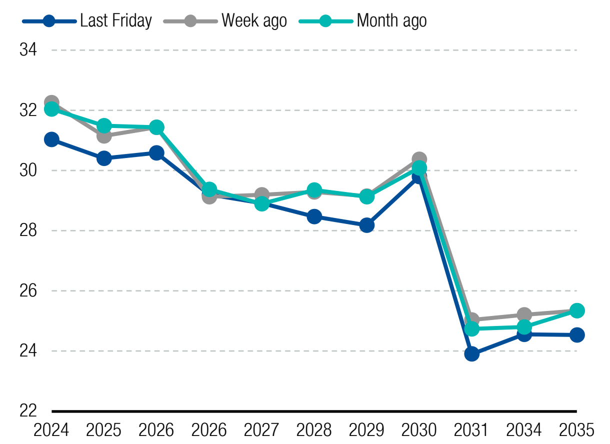
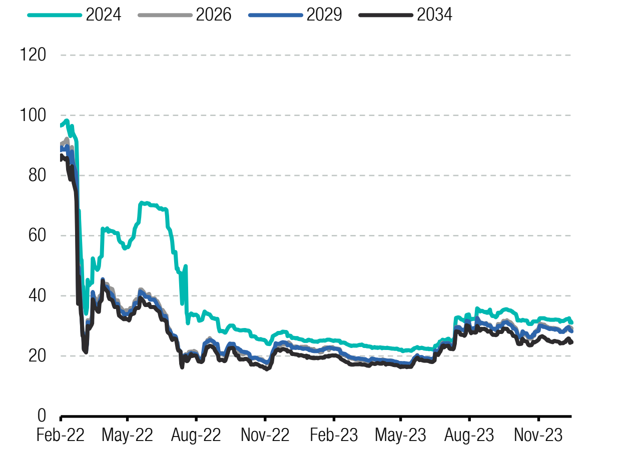
Chart 3. Ukrainian Eurobonds prices

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

Hryvnia weakens on higher trading

Over the past week, the hryvnia exchange rate weakened on the interbank and cash markets at equivalent rates.

Bank clients (legal entities) reduced the volume of hard currency sales in the interbank market in the four business days of last week by approximately 13% while buying 16% more hard currency than in the same period of the previous week. The higher imbalance led the NBU to increase interventions to US$863m, the largest volume of interventions in two months. The official exchange rate weakened by 0.8% to UAH37.02/US$ in a week.

In the retail market, the hryvnia exchange rate in systemically important banks weakened by 0.8% to UAH37.0–37.7/US$.

ICU view: The interbank market saw increased client trading, likely due to purchases of hard currency by government entities for import contracts. The NBU increased its interventions, seeking to satisfy this excess demand and restrain the weakening of the hryvnia exchange rate, but still allowed the official exchange rate to slip below UAH37/US$. The retail market followed the interbank market and the official exchange rate, indicating all exchange rates are moving in sync, which is probably the first such episode since russia's full-fledged invasion.

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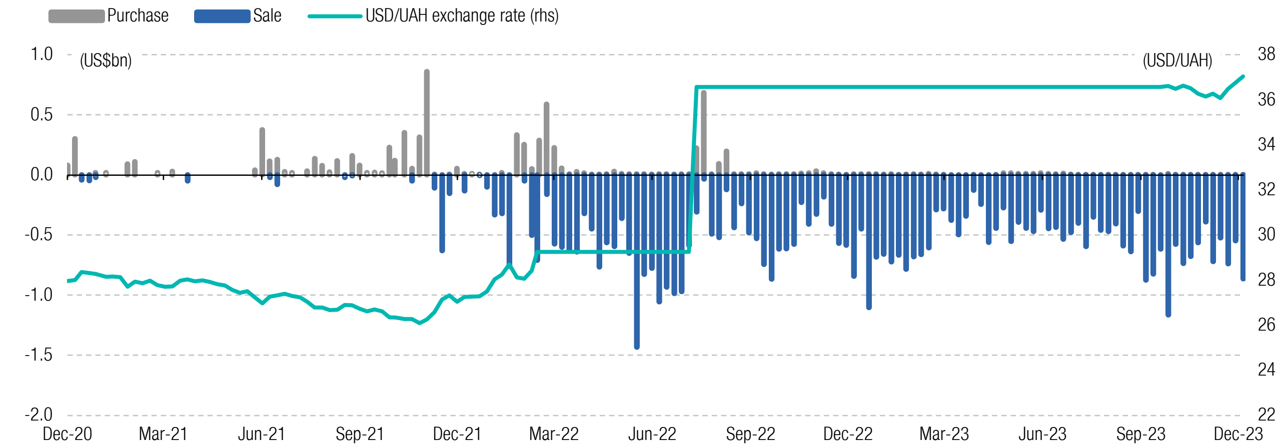
Chart 4. FX market indicators, 3-year history

Ukraine hryvnia UAH exchange rate per US dollar at the interbank market and NBU interventions (weekly data)



Source: NBU, Bloomberg, ICU.

Economics

Another key rate cut

The NBU has decreased the key rate by 100bp to 15%, in line with the expectations and October's forecast.

No changes in monetary policy design this time, and the regulator simultaneously lowered the rates on deposit certificates and refinancing loans by 100bp.

ICU view: NBU's macro forecast expects no more changes in the key rate next year. However, we believe that should the situation with external financing improve substantially, the regulator would lower the rate by as much as 200bp in 2024.

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