Focus
Ukraine

Markets
Government bonds, FX market, and macro

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Weekly Insight

NBU signals rate cuts in 2H24

Key messages of the today's comments

MONDAY, 29 JANUARY 2024

Ukrainian bond market

MoF borrows for future redemptions

The MoF has already refinanced all debt redemptions made in January, so new borrowings replenish government accounts before upcoming February redemptions.

Eurobond prices up amid lingering uncertainty about US aid

Prices of Ukrainian Eurobonds rose last week in response to the near approval of the EU aid package for Ukraine while aid from the US is still uncertain.

Foreign exchange market

Hryvnia weakening again

Despite narrower imbalances in the FX market, the hryvnia exchange rate started to weaken last week.

Economics

NBU signals rate cuts in 2H24

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Banks' reserves market (26 January 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%)[1]	15.00	+0bp	-1,000bp
ON rate (%)	15.02	+0bp	-798bp
Reserves (UAHm)[2]	241,453	+14.1	+91.6
CDs (UAHm)[3]	553,280	-3.3	+40.9

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) (26 January 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU	687,490	+0.0	-2.1
Banks	662,325	+0.1	+30.7
Residents	145,430	+0.3	+30.4
Individuals	57,208	+2.9	+76.7
Foreigners	44,016	-0.3	-30.4
Total	**1,598,506**	**+0.2**	**+12.7**

Source: NBU, ICU.

FX market indicators (26 January 2024)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	37.8312	+0.5	+2.5
EUR/USD	1.0853	-0.4	-0.4
DXY	103.433	+0.1	+1.6

Source: Bloomberg, ICU.

Market gov't bond quotes (29 January 2024)

Maturity	Bid (%)	Ask(%)
6 months	17.50	15.00
12 months	18.00	16.50
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

MoF borrows for future redemptions

The MoF has already refinanced all debt redemptions made in January, so new borrowings replenish government accounts before upcoming February redemptions.

Last week, the MoF borrowed UAH6bn (US$160m), including US$101.6m in hard currency, implying it fully refinanced last week's redemption of USD-denominated bills. Most of the bonds were sold at usual interest rates, except the three-year "reserve" note, for which the MoF decreased interest rates by 10bp to 18.5%. See details in the auctions review.

In the secondary bond market, the volume of trades declined by 12% to UAH11.5bn (US$304m). The most traded were UAH bonds due in February 2026 (21.5% of all bond trades) and USD-denominated bills due at the end of February 2024 (21.7% of all trades).

Last week, the MoF redeemed US$80m of bonds, the last redemption this month, while the next redemption of UAH2.5bn is scheduled for February 7. The largest redemptions in February will be UAH10bn in the middle of the month and EUR297m and US$453m in the last two weeks.

ICU view: The MoF borrowed two times more than what it needed for debt redemptions (in all currencies) in January. By currency, the refinancing of EUR-denominated bonds slightly fell short of 100%. As there will not be large debt redemptions this week or next, the MoF will accumulate funds for deficit financing and/or debt redemptions in February.

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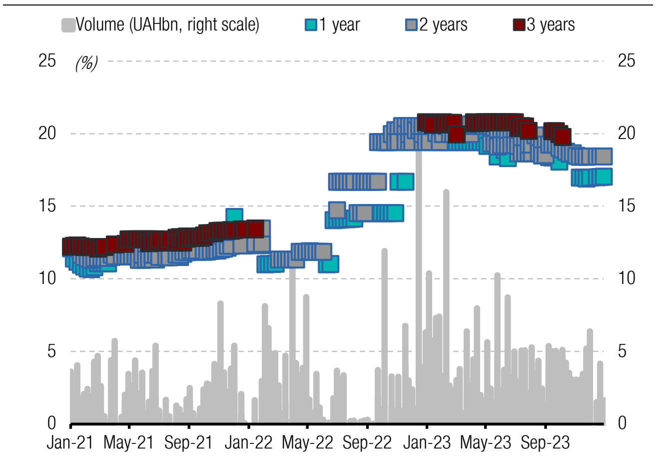
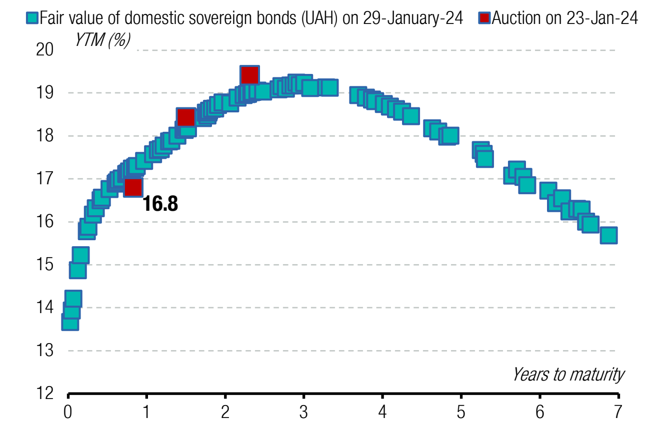
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

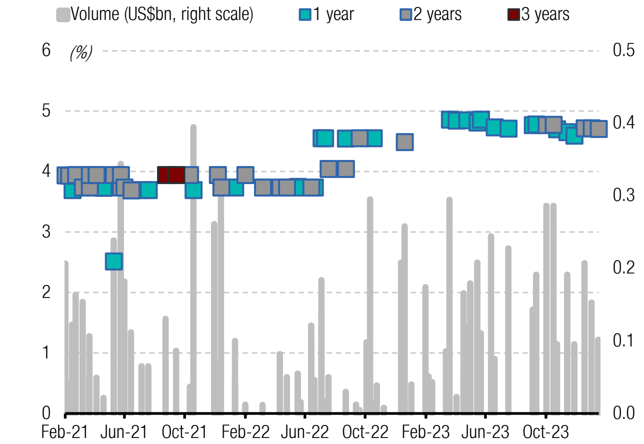
YTMs of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

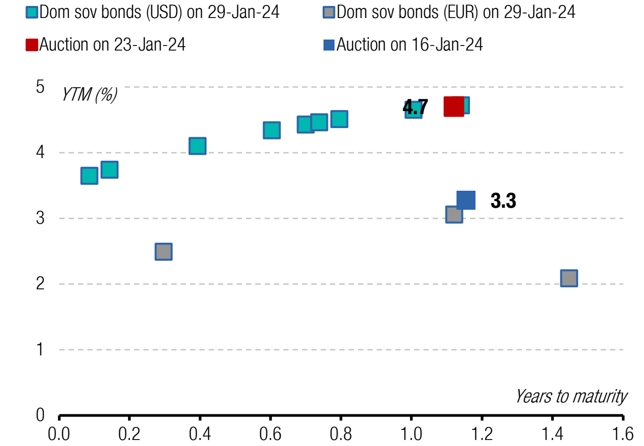
Chart 2. FX-denominated bonds

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.

Eurobond prices up amid lingering uncertainty about US aid

Prices of Ukrainian Eurobonds rose last week in response to the near approval of the EU aid package for Ukraine while aid from the US is still uncertain.

Last Tuesday ended a nearly two-week-long downward trend for Ukrainian Eurobonds; their prices rose by 3% on average to 23–31. The price range for Eurobonds with different maturities tightened to 12.6%. The price of VRIs was up by 0.5%, staying below 47 cents per dollar of notional value. The EMBI index slid by 0.2% last week.

ICU view: Last week's Eurobond prices recovered some of the losses of the past two weeks. The chances are high that a financial aid package from the EU will be approved this week. This may support Eurobond prices. Meanwhile, bondholders keep a close watch on the progress with the US assistance. The US aid package is of utmost importance as it includes not only financial but critical military support for Ukraine. The IMF mission will start in February to review the EFF program, and may approve the restructuring terms for the Ukrainian paper. All these factors together will be decisive for Eurobond prices in the coming weeks.

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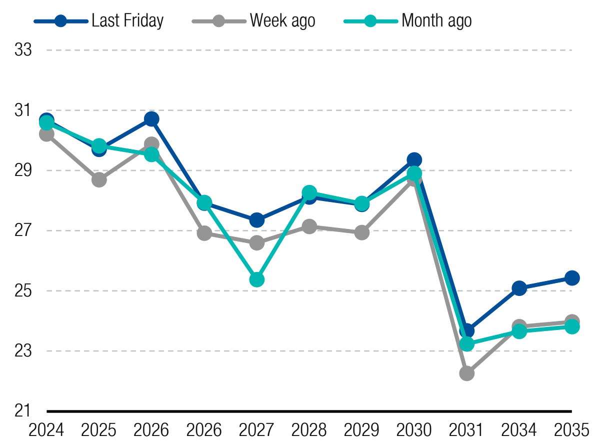
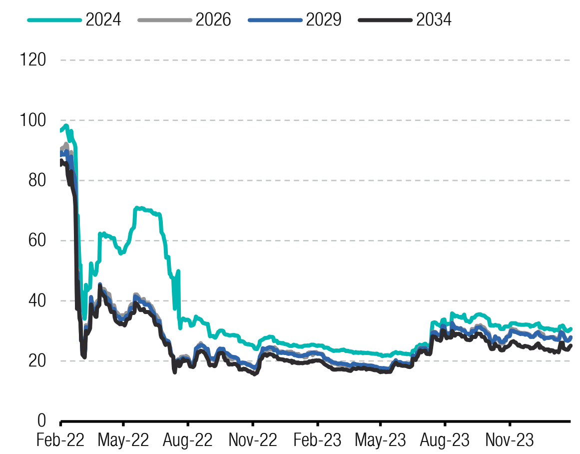
Chart 3. Ukrainian Eurobonds prices

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



Source: Bloomberg, ICU.

Historical data since February, 2022



Source: Bloomberg, ICU.

Foreign exchange market

Hryvnia weakening again

Despite narrower imbalances in the FX market, the hryvnia exchange rate started to weaken last week.

In the interbank market, balance improved on Monday and Tuesday and FX supply from legal entities exceeded demand. But on Wednesday, the pattern was back to normal. Overall, in four business days last week, clients decreased purchases and increased sales by 9% and 20% respectively, sold US$27m more than purchased, the first time since April 2023. At the same time, in the retail market, hard currency purchases rose by 27% to US$405m.

All these factor led to a decline in NBU interventions 21% to US$421m, the lowest amount in almost three months.

However, higher demand for hard currency in the second half of the week caused hryvnia weakening: the official exchange rate weakened by 0.7% to UAH37.78/US$ and the cash exchange rate in systemically important banks by 0.2% to UAH37.6–38.3/US$.

ICU view: A probable explanation for narrowed imbalances in the FX market is that exporters sold more hard currency to make tax payments. At the same time, households used short-lived appreciation to increase FX purchases of cash hard currency. The NBU does not prevent the movement of the hryvnia exchange rate in both directions, decreasing range and duration of fluctuations.

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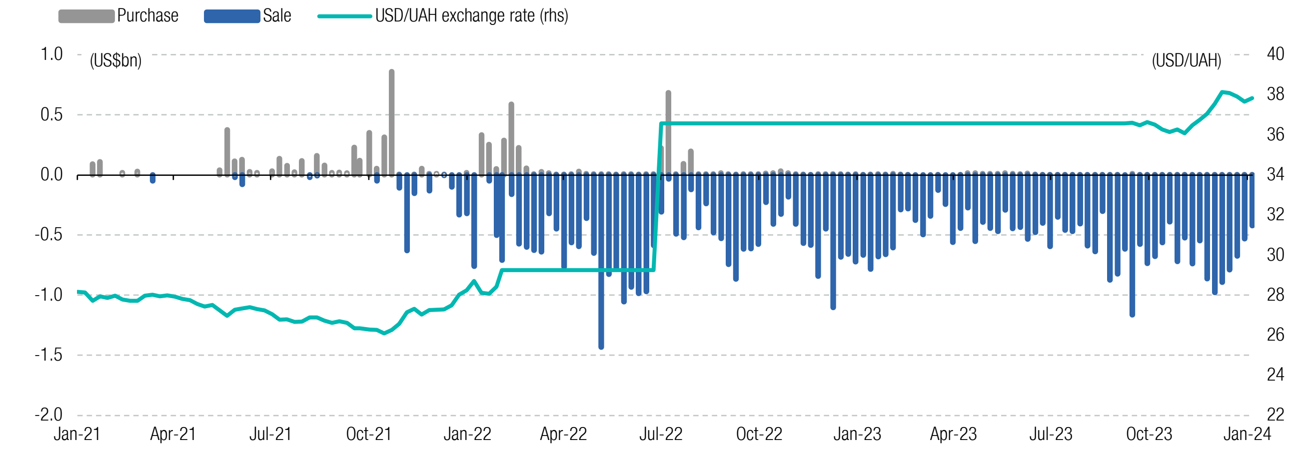
Chart 4. FX market indicators, 3-year history

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



Source: NBU, Bloomberg, ICU.

Economics

NBU signals rate cuts in 2H24

The key monetary policy rate has been maintained at 15%, in line with expectations.

The revised macroeconomic forecast points to a 50bps reduction in both 3Q24 and 4Q24, bringing the key rate down to 14% by year-end. This marks an optimistic shift compared with the October forecast, which did not anticipate any cuts throughout 2024.

Additionally, the NBU revised its CPI forecast for 2024, adjusting it from 9.8% YoY to 8.6% YoY. This adjustment is attributed to the NBU's commitment of ensuring exchange rate stability.

ICU view: We expect the key rate to remain at 15% during 1H24. Should the situation with Western financial aid significantly improve and inflation risks remains under control, the NBU can cut the rate even further, to 13% by the end of the year.

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