



Focus
Ukraine

Markets
Government bonds,
FX market, and macro

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Weekly Insight

NBU surprises with a rate cut

Key messages of the today's comments

Ukrainian bond market

Investors' interest shifts to longer maturities

Demand in the primary bond market partially shifted to longer maturities last week. In the secondary bond market, investors mainly purchased instruments maturing in January 2025, and beyond.

Eurobond rally ends

Ukrainian Eurobond prices declined after a two-week rally, and the price range for papers with different maturities widened.

Foreign exchange market

Hryvnia weakens due to worse market balance

FX market turnover declined last week while market balance worsened in the final days of the week. Therefore, the NBU increased interventions and the hryvnia weakened.

Economics

NBU surprises with a rate cut

The key monetary policy rate was lowered by 50 bps to 14.5%. This surprised the market since the latest macro forecast from the regulator indicated an unchanged rate until July. NBU stated that weakening inflation reached 4.3% YoY in February, FX market stabilized and inflows of foreign financial aid improved.

MONDAY, 18 MARCH 2024

Banks' reserves market (15 March 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	14.50	-50bp	-1,050bp
ON rate (%)	14.50	-50bp	-850bp
Reserves (UAHm) ²	167,530	-23.2	-15.7
CDs (UAHm) ³	582,591	+9.2	+73.8

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 gov't bond holders (UAHm) (15 March 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU	682,490	+0.0	-2.1
Banks	667,731	+0.0	+25.8
Residents	149,080	-0.3	+34.3
Individuals	58,215	-0.2	+71.5
Foreigners	39,716	-8.7	-28.6
Total	1,598,986	-0.3	+11.7

Source: NBU, ICU.

FX market indicators (15 March 2024)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	38.8250	+1.5	+5.2
EUR/USD	1.0889	-0.5	+2.9
DXY	103.432	+0.7	-1.2

Source: Bloomberg, ICU.

Market gov't bond quotes (18 March 2024)

Maturity	Bid (%)	Ask(%)
6 months	17.00	15.00
12 months	17.50	16.50
2 years	19.00	17.50
3 years	19.75	18.50
12 months (\$)	5.00	4.50
2 years (\$)	N/A	N/A

Source: ICU.

Ukrainian bond market

Investors' interest shifts to longer maturities

Demand in the primary bond market partially shifted to longer maturities last week. In the secondary bond market, investors mainly purchased instruments maturing in January 2025, and beyond.

In the primary bond market, demand was up approximately by a third compared with previous weeks. Expectedly, demand was the largest for a 12-month paper. Bids for two-year bills rose six-fold and four-fold for three-year notes, and they provided the state budget with more than half of last week's proceeds. See details in the [auction review](#).

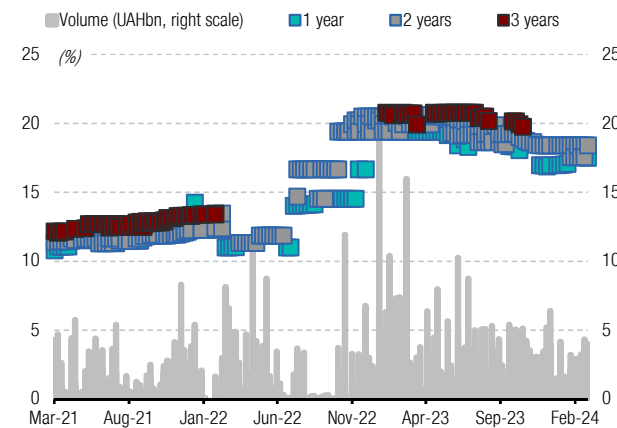
In the secondary bond market, the most traded UAH paper was the one due in July 2027, with a 25% share in total UAH bond deals, while just 22% of deals were with bills due this year. Among FX-denominated bills, most trades were in paper due this September.

ICU view: While reinvesting last week's proceeds from debt redemptions, investors preferred longer maturities, especially notes due in 2027, to lock in current YTM for the longest possible term. NBU's decision to cut the key policy rate and rates for three-month CDs (see [comment below](#)) will likely impact deposit rates and YTM of UAH bonds within the next month or two. The bond market will probably react to this NBU decision faster than banks. Therefore, the market will likely see high demand for longer bonds, similar to last week.

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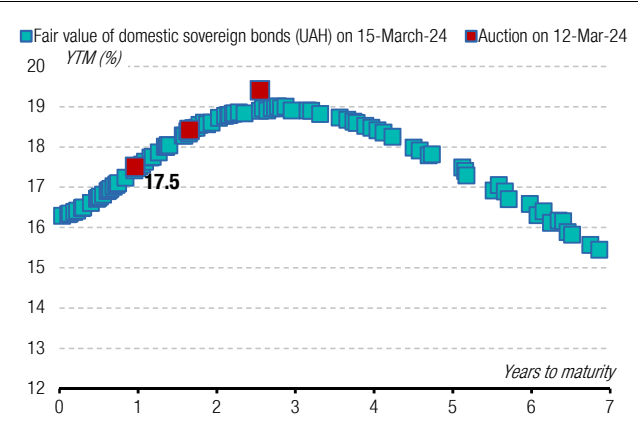
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

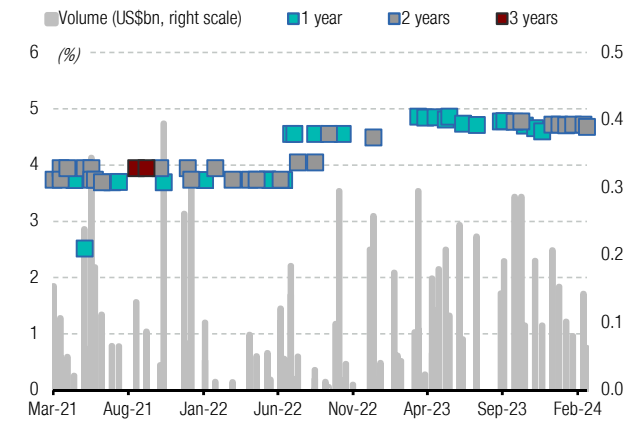
YTM of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

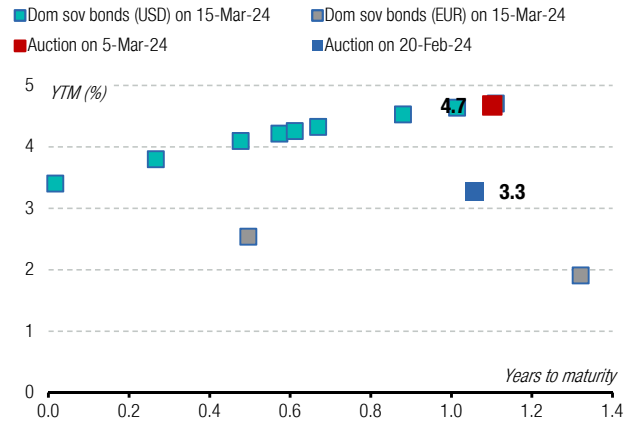
Chart 2. FX-denominated bonds

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



Source: MFU, ICU.

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



Source: NBU, MFU, ICU.

Eurobond rally ends

Ukrainian Eurobond prices declined after a two-week rally, and the price range for papers with different maturities widened.

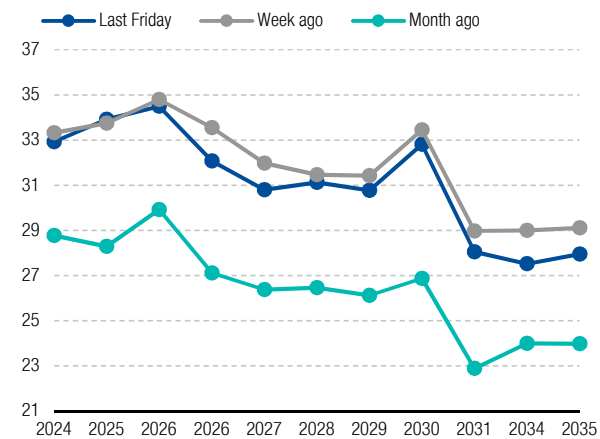
Eurobond prices declined by an average of 2.5% to 27–34 cents, with the price range widening to 11.2%. The price of VRIs slid by 1.8% to 47 cents of the notional value. The EMBI index declined by 0.8%.

ICU view: A week ago, S&P cut the Ukrainian foreign-currency rating to CC with a negative outlook on expected debt restructuring. At the same time, Ukraine signed a memorandum with the EU last week and will receive EUR6bn in March and April according to a new four-year program called the Ukraine Facility. This combination of news stabilized Eurobond prices and some investors locked in gains from the previous weeks. Investors’ mood remains largely positive, as they expect restructuring talks to start soon, probably next month. Further moves in Eurobond prices in the nearest weeks will primarily depend on the progress with the passage of the Ukrainian aid package in the US House of Representatives.

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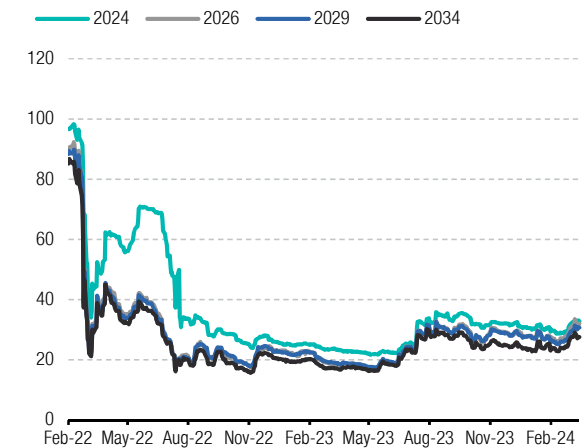
Chart 3. Ukrainian Eurobonds prices

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 weakens due to worse market balance

FX market turnover declined last week while market balance worsened in the final days of the week. Therefore, the NBU increased interventions and the hryvnia weakened.

In the interbank FX market legal entities sold US\$932m and purchased US\$902m (in four business days). Total turnover in the interbank market declined by nearly 20%. Last Thursday (and probably last Friday) demand exceeded supply in the interbank FX market segment.

In the retail FX market, turnover declined by approximately 10%, and net purchases fell to US\$84m, the smallest amount since last September.

Net hard currency purchases doubled to US\$53m compared to previous week. Balance shifted to demand side last Thursday and probably the deficit of hard currency even increased last Friday, as the NBU had to increase interventions. Finally, the NBU sold US\$263m, increasing weekly interventions by 68%.

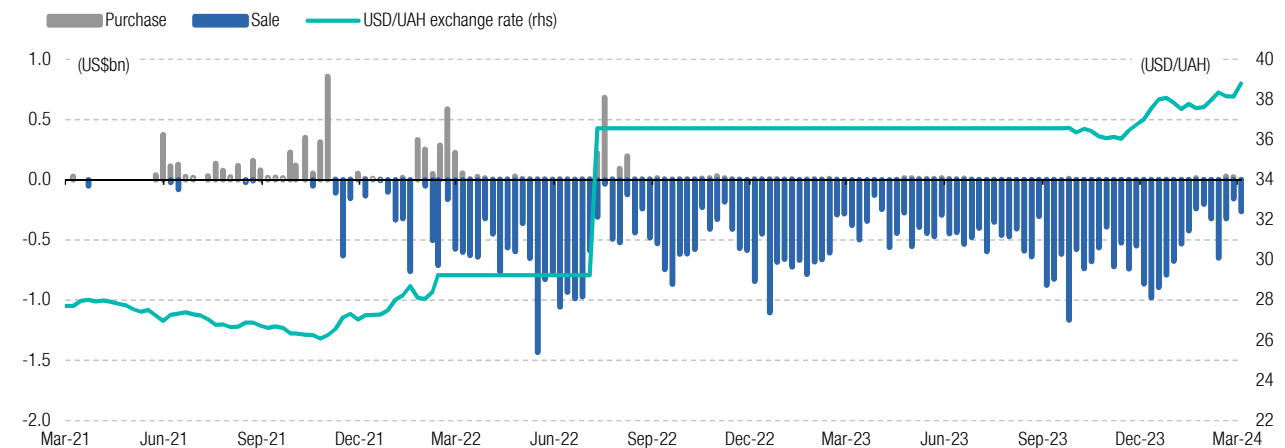
The hryvnia exchange rate weakened last week. The official exchange rate weakened by 1.7% to UAH38.8/US\$, and the cash rate in systemically important banks weakened by 1.1% to UAH38.4–39.0/US\$.

ICU view: Although the total amount of hard currency trades declined last week, the market balance still worsened. Imbalances were likely caused by FX purchases of government institutions for import contracts. Occasionally, on several days, the NBU had to sell more hard currency, which resulted in larger FX interventions for the week and also a weaker hryvnia exchange rate.

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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 surprises with a rate cut

The key monetary policy rate was lowered by 50 bps to 14.5%. This surprised the market since the latest macro forecast from the regulator indicated an unchanged rate until July. NBU stated that weakening inflation reached 4.3% YoY in February, FX market stabilized and inflows of foreign financial aid improved.

The interest rate on the 3-month certificates of deposits (CDs) and the rate on refinancing loans were lowered by 150bps to 17.5%. NBU will amend the rules that determine the amount of liquidity banks can invest in 3-month CDs to stimulate longer maturities of retail deposits.

ICU view: NBU can extend the current cycle with one or two cautious cuts in 1H24. Regulator will continue doing so in 2H24 in case of lower inflation risks, particularly crop related.

We expect smaller banks with above-average interest rates on retail deposits to cut rates after the NBU's move. Overall, the earlier-than-expected rate cut will spur a quicker decline in deposits interest rates and YTM's of UAH bonds this year.

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