

Weekly Insight

NBU pauses hryvnia devaluation

Key messages of the today's comments

Ukrainian bond market

Investors focus on longer maturities

Last week, investors' interest in UAH bonds with longer maturities sharply increased as they tried to lock in current YTM's for longer. Taking advantage of high demand, the Ministry of Finance continued to lower interest rates on UAH instruments.

Eurobond prices down in absence of restructuring news

Last week was broadly news-neutral as there was no important new information about the planned debt restructuring. Ukrainian Eurobond prices declined, contrary to the global trend of the EM bond market.

Foreign exchange market

NBU pauses hryvnia devaluation

After almost five months of moderate devaluation when the hryvnia exchange rate dropped from UAH36.7/US\$ to UAH39.8/US\$, the NBU seems to have taken a break and has kept the exchange rate in the tight range of UAH39.3–39.7/US\$ for four weeks.

TUESDAY, 21 MAY 2024

Banks' reserves market (20 May 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	13.50	+0bp	-1,150bp
ON rate (%)	13.50	+0bp	-650bp
Reserves (UAHm) ²	217,620	-16.0	+9.9
CDs (UAHm) ³	548,810	+2.3	+0.0

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) (20 May 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU	677,990	+0.0	-2.4
Banks	690,396	+0.1	+25.8
Residents	162,859	-0.4	+39.6
Individuals	61,957	-0.5	+55.2
Foreigners	39,898	-2.9	-28.9
Total	1,634,595	-0.1	+12.0

Source: NBU, ICU.

FX market indicators (20 May 2024)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	39.6125	-0.1	+7.2
EUR/USD	1.0857	+0.4	+0.5
DXY	104.565	-0.4	+1.3

Source: Bloomberg, ICU.

Market gov't bond quotes (21 May 2024)

Maturity	Bid (%)	Ask (%)
6 months	16.00	14.00
12 months	16.50	15.00
2 years	17.25	16.25
3 years	19.00	17.25
12 months (\$)	5.00	4.50
2 years (\$)	N/A	N/A

Source: ICU.

Ukrainian bond market

Investors focus on longer maturities

Last week, investors' interest in UAH bonds with longer maturities sharply increased as they tried to lock in current YTM for longer. Taking advantage of high demand, the Ministry of Finance continued to lower interest rates on UAH instruments.

In the primary bond market, the MoF offered the usual maturities of UAH bonds (one-, two- and three-year securities) and a 12-month EUR-denominated paper. Demand for one-year bills was below the supply cap, while demand for three-year bills was four times larger than the cap. Such oversubscription allowed the MoF to lower rates on three-year notes by 30bp to 17.2%. See details in the [auction review](#).

Since the beginning of the spring cycle of monetary policy easing, the Ministry has reduced rates on one-year bills by 165bp, on two-year paper by 140bp, and three-year notes by 130bp.

In the secondary bond market, the most traded bills were those maturing in January 2025 (17% of all UAH bond trades), but more than a half of all trades was with longer maturities, including 13% with bills due in October next year, 11% with paper maturing in June 2025 and 10% of trades were with notes due in July 2027. The total volume of trades decreased by 14% to UAH6.8bn last week.

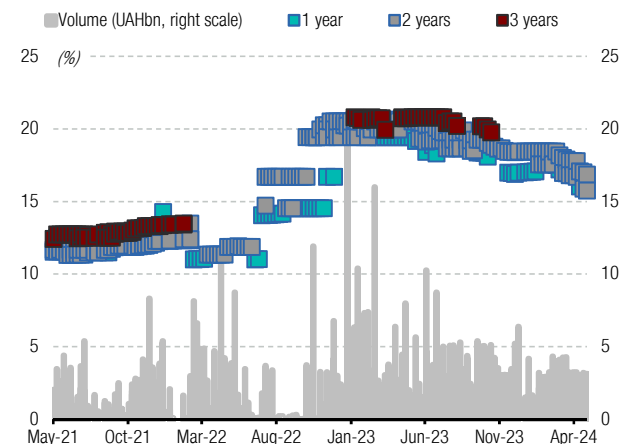
Portfolios of all investor groups declined last week. This was mainly the result of the redemption of EUR-denominated bills last Thursday. Only foreign investors reduced their portfolios by selling UAH bonds. This week, the MoF will redeem UAH22bn of bonds, and after that the Ministry will have a break in redemptions until June.

ICU view: The low inflation rate in April reinforced market expectations that the NBU will cut rates more aggressively than its current macroeconomic forecast predicts. Therefore, the focus of demand in both the primary and secondary markets shifted to longer maturities. Investors seek to lock in current levels of YTM for several years. Additional demand and competitive bids allow the MoF to lower rates in the primary bond market in small steps. We expect rates to decline further in the coming weeks. We recommend that investors who intend to increase their portfolios of UAH bonds not delay their investment decisions.

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

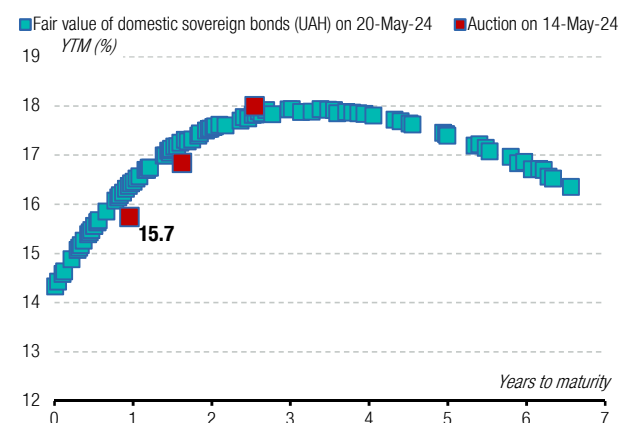
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

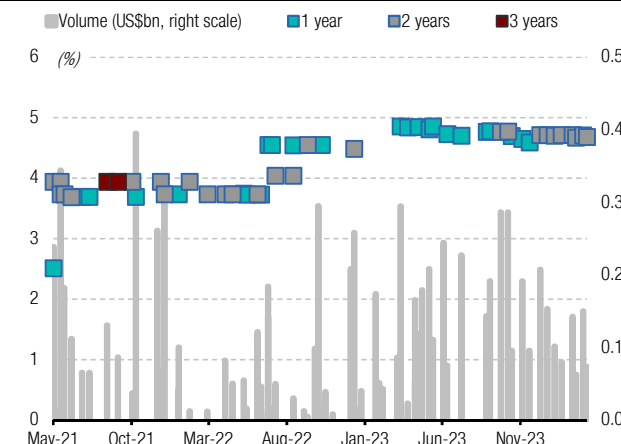
YTM of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

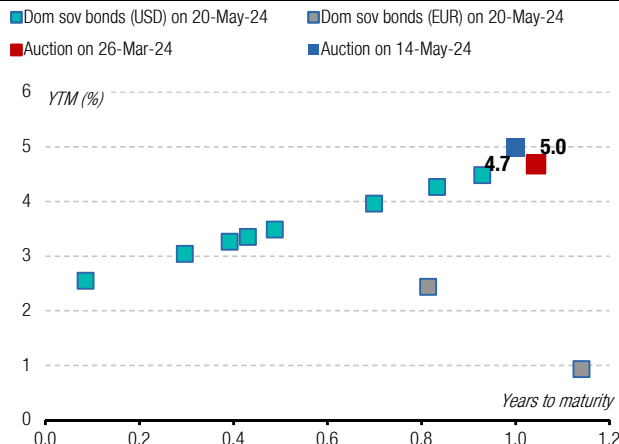
Chart 2. FX-denominated bonds

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



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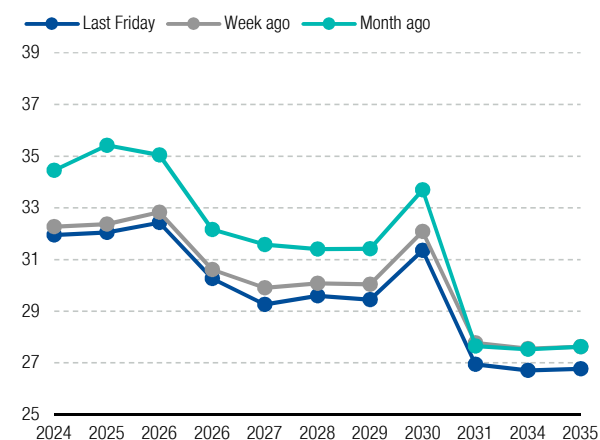
Ukrainian Eurobond prices slid by an average of 2% to 26.7–32.4, with the price range for instruments with different maturities widening to 9.7%. The price of VRIs declined by almost 3% to 52.2 cents per dollar of notional value. The EMBI index rose by 0.9% last week.

ICU view: Consultations between Ukrainian advisers and the creditors' committee continued last week, but no new public information was released. Therefore, the market was relying on guesses and assumptions about possible restructuring terms and what could happen if restructuring terms are not quickly approved by investors.

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

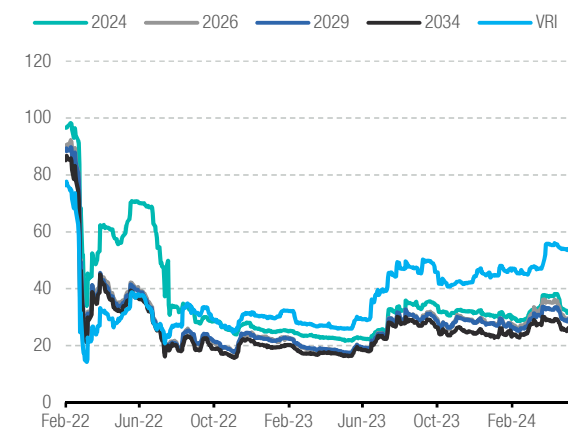
Chart 3. Ukrainian Eurobonds and VRI prices

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

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In the interbank market, FX trading increased noticeably. Foreign currency purchases by bank clients (legal entities) amounted to almost US\$1.3bn (13% more than in the previous week), and sales increased by 21% to US\$1.2bn. Therefore, net purchases fell by 32% to US\$120m.

In the retail market last week, FX purchases increased by 11% while sales increased by 14%. Net purchases of foreign currency rose by 7% to US\$217mn.

Overall, the foreign currency deficit in the FX market decreased by approximately 11% to US\$337m, but NBU interventions decreased by only 8% to US\$491m, strengthening the hryvnia.

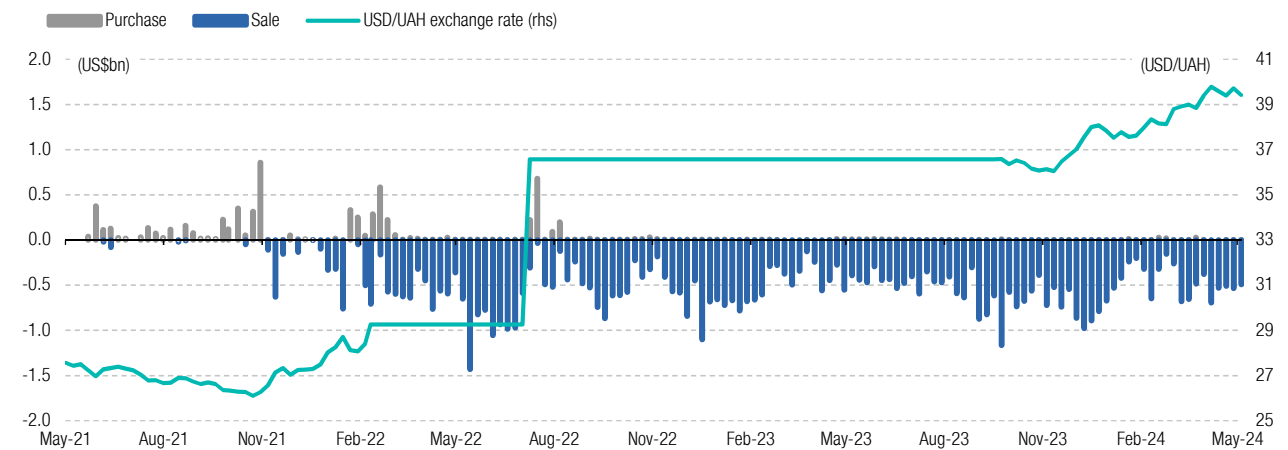
As of last week, the official exchange rate strengthened by 0.7% to UAH39.43/US\$, and the cash rate in systemically important banks strengthened by less than 0.2% to UAH39.3–39.9/US\$.

ICU view: The NBU paused hryvnia devaluation for the past four weeks and has allowed only small fluctuations of the exchange rate in a narrow range, keeping interventions at a high level. The average weekly intervention in the last four weeks is US\$516m, above the average weekly interventions YTD (US\$476m) and especially above US\$300m of average weekly interventions in February and March, when hryvnia lost more than 4%. These facts may indicate that the NBU is determined to assess the effects of devaluation and choose the best period to resume the gradual weakening of the hryvnia exchange rate. We maintain our forecast of a gradual weakening of the hryvnia until the end of the year to UAH42.3/US\$.

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.

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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

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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