

Weekly Insight

NBU reserves decline 8% in May

Key messages of the today's comments

MONDAY, 10 JUNE 2024

Ukrainian bond market

Investors continue to lock in yields

In the primary market, demand for three-year notes was the largest, in line with previous weeks, and this tenor also remains the most actively traded in the secondary market.

Investors wait for details on Eurobonds restructuring terms

Last week, the Minister of Finance said that negotiations on restructuring are already underway and may soon become public.

Foreign exchange market

NBU keeps hryvnia in a new range

Lower demand for hard currency and uniform interventions during the week allowed the NBU to return the hryvnia to below UAH40.5/US\$ and keep it there during the week.

Economics

NBU reserves decline 8% in May on FX interventions

NBU gross international reserves were down 7.9% in May to US\$39.0bn as the inflows of foreign financial aid were insignificant, and the NBU upped its FX sale interventions.

Banks' reserves market (7 June 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	13.50	+0bp	-1,150bp
ON rate (%)	13.50	+0bp	-650bp
Reserves (UAHm) ²	236,505	+6.5	+18.8
CDs (UAHm) ³	542,230	-3.7	+27.1

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) (7 June 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU	677,606	+0.0	-2.4
Banks	690,436	-0.3	+26.3
Residents	161,975	-0.4	+39.3
Individuals	62,169	-2.2	+50.4
Foreigners	36,500	-1.2	-25.6
Total	1,629,700	-0.3	+12.4

Source: NBU, ICU.

FX market indicators (7 June 2024)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	40.2260	-0.8	+8.9
EUR/USD	1.0801	-0.4	+1.0
DXY	104.885	+0.2	+0.8

Source: Bloomberg, ICU.

Market gov't bond quotes (10 June 2024)

Maturity	Bid (%)	Ask (%)
6 months	15.00	13.00
12 months	16.50	15.00
2 years	17.50	16.00
3 years	18.00	16.50
12 months (\$)	5.00	4.50
2 years (\$)	N/A	N/A

Source: ICU.

Ukrainian bond market

Investors continue to lock in yields

In the primary market, demand for three-year notes was the largest, in line with previous weeks, and this tenor also remains the most actively traded in the secondary market.

The Ministry of Finance increased the weekly supply of two-year and three-year UAH bonds at primary auctions to UAH4bn each and continued to lower rates on all issues. Traditionally, the auction offer consisted of three UAH bonds maturing in 2025, 2026, and 2027. Demand focused on the two longer securities, which received almost equal bids: UAH14bn each. At the same time, the 12-month paper collected bids for only UAH5.5bn. Due to the great demand, the Ministry sold the entire planned volume of bonds and reduced the cut-off rates by 9–33bp. See details in the [auction review](#).

In the secondary bond market, trades increased by 15% to UAH13.8bn. Investors mostly traded bonds maturing in 2027. The total volume of deals was 42% of all UAH bond trades last week.

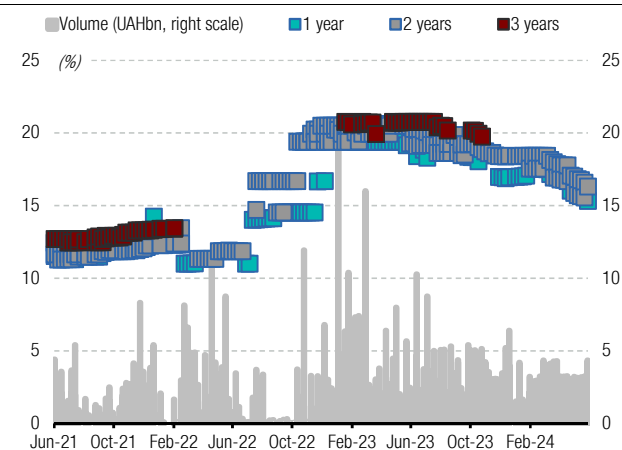
Last week, the Ministry repaid UAH15bn in UAH bond redemptions. The next repayments are scheduled for the next week (US\$303m) and the last week in June (UAH18bn).

ICU view: The Ministry of Finance increased borrowings, but this did not prevent the reduction of interest rates on UAH bonds. Overall, since the beginning of the spring cycle of monetary policy easing, the decline in yields reached almost 200bp for 12-month and two-year bills and 221bp for three-year paper. It clearly signals investors' desire to lock in current YTM. This week's key event will be NBU's decision on the key policy rate. The market's attention will be focused on the size of its immediate reduction and also on the regulator's signals about the future rate trajectory. Currently, the NBU's forecast implies that there is potential to reduce the rate by only 0.5 percentage points for the remainder of the year from the current level of 13.5%. However, persistently low inflation may encourage the NBU to set more ambitious rate-reduction targets.

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

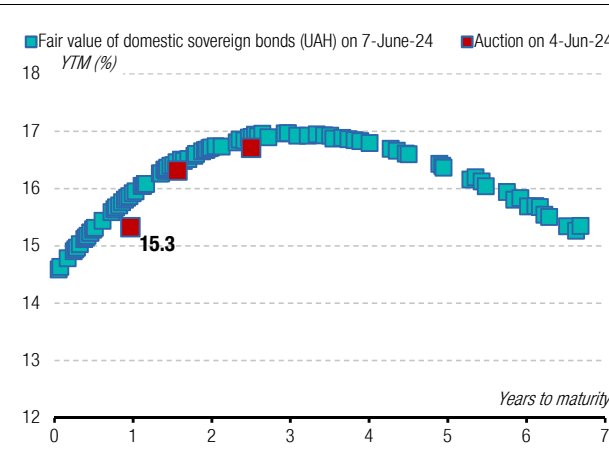
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

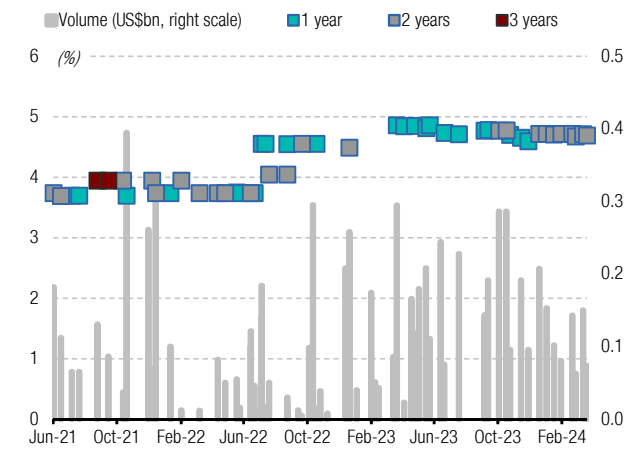
YTM of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

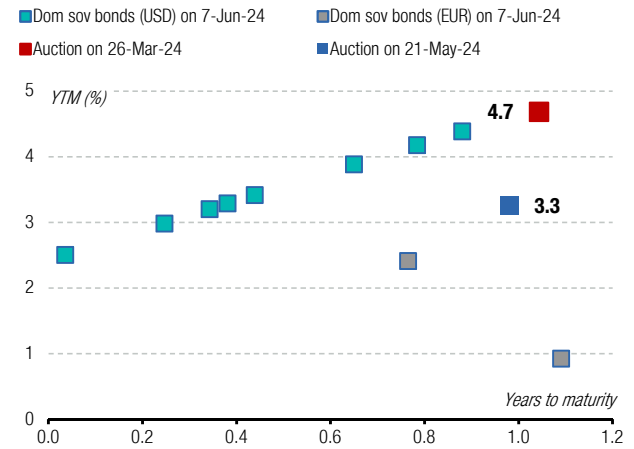
Chart 2. FX-denominated bonds

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



Source: NBU, MFU, ICU.

Investors wait for details on Eurobonds restructuring terms

Last week, the Minister of Finance said that negotiations on restructuring are already underway and may soon become public.

The minister also confirmed that restructuring terms will include a haircut, but he did not specify the size. At the same time, new rumours in the markets emerged that availability of cash flows for coupon payments within the IMF program period may be a contentious issue. Reportedly, the G7 countries insist that there should be no payments to commercial creditors during the IMF program, or these payments should be minimal.

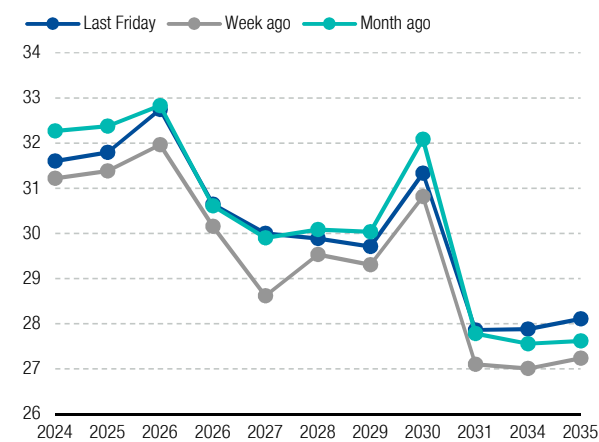
Such news did not have much impact on investor sentiment. Prices rose by an average of 2.3% to 27.9–32.8, with the price range for instruments with different maturities narrowing to 8.1%. The price of VRIs rose by 0.2% to 52.1 cents per dollar of notional value. The EMBI index slightly fluctuated within 0.4% last week and, at the end of the week, returned to the level of the previous Friday.

ICU view: Investors are waiting for detailed information on the restructuring offer from the Ministry of Finance. The release of an updated DSA analysis from the IMF is also likely to provide more input data and hints about whether market expectations about the size of the haircut and availability of coupons in the nearest years are well grounded. The prices will remain volatile until more clarity about the restructuring emerges in the coming weeks.

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

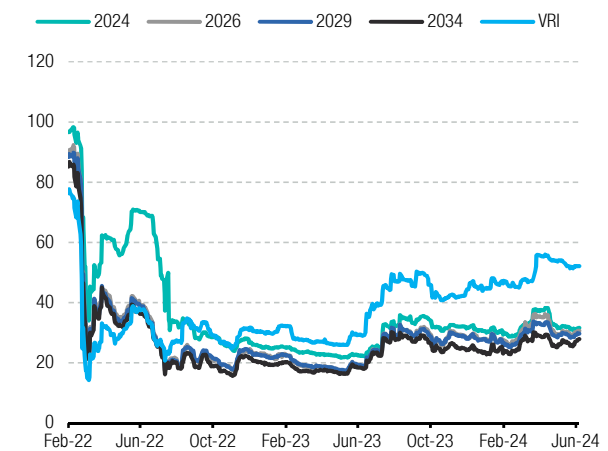
Chart 3. Ukrainian Eurobonds and VRI prices

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

NBU keeps hryvnia in a new range

Lower demand for hard currency and uniform interventions during the week allowed the NBU to return the hryvnia to below UAH40.5/US\$ and keep it there during the week.

Imbalances in the interbank FX market narrowed last week. FX sales by bank clients (legal entities) increased by 4.5% to US\$841m, and purchases decreased by 23% to US\$1.1bn. The net purchase of foreign currency decreased twofold to US\$253m.

At the same time, in the retail market last week (in four business days), the volume of transactions hardly changed. In four days, households bought US\$540m, the same amount of foreign currency as the week before, and sold almost US\$300m, nearly 5% less than in the same period of the previous week. The net purchase of foreign currency did not change and amounted to US\$243m.

In total, in four days, the hard currency deficit amounted to US\$497m, almost halved from the previous week. The NBU's interventions decreased by about a third to \$695 million.

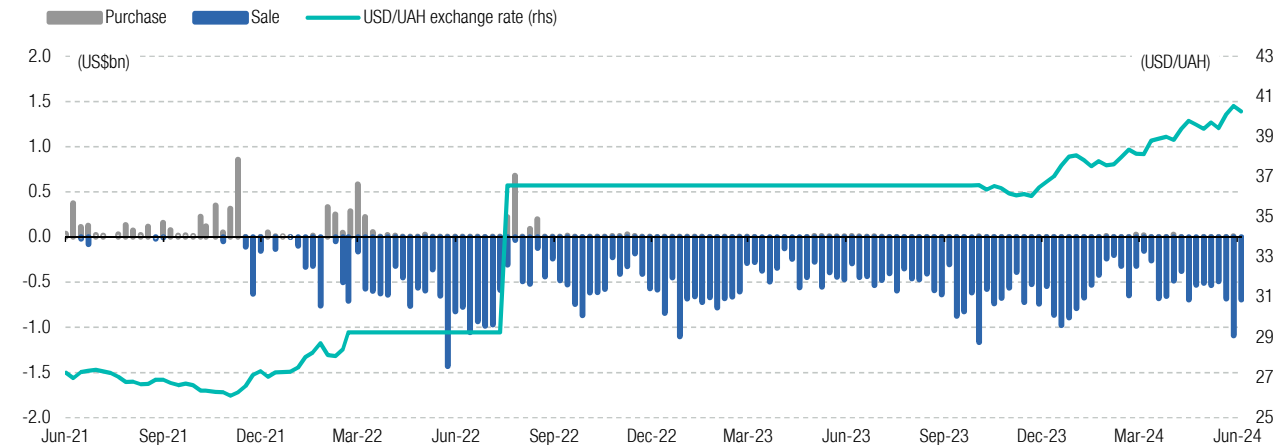
The official hryvnia exchange rate strengthened by 0.7% to UAH40.25/US\$, and in systemically important banks, cash hryvnia appreciated by 0.4% to UAH40.1–40.7/US\$ by the end of the week.

ICU view: With no significant one-off demand from government agencies, the market returned to more usual volumes of FX trading and lower imbalances. This allowed the NBU to stabilize the hryvnia exchange rate at new levels in a new range where it may fluctuate in the coming weeks.

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

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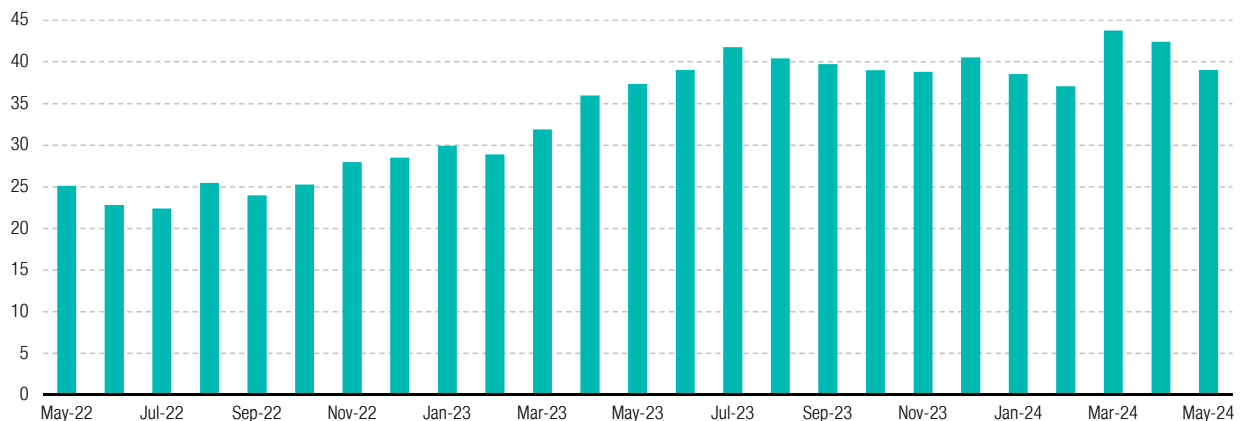
The NBU sold net US\$3.1bn to alleviate imbalances in the FX market in May. Previously, the NBU monthly interventions exceeded the US\$3.0bn level only six times since the start of Russia's full scale invasion. Last month, Ukraine received only US\$20mn in loans from foreign partners while repaying about US\$340mn of debts to IFIs.

ICU view: NBU reserves will recover to above US\$40bn in June as Ukraine is scheduled to receive a US\$2.2bn loan tranche from the IMF following a successful fourth revision under the EFF program. Ukraine also expects to receive an EUR1.9bn loan tranche from the EU within the Ukraine Facility. We expect NBU reserves will be close to US\$45bn at the end of 2024 if all foreign loans and grants are provided as scheduled.

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

Chart 5. NBU gross international reserves, US\$bn

NBU gross reserves down 7.9% in May



Source: NBU, 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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