Focus
Ukraine

Markets
Government bonds, FX market, and macro

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Weekly Insight

Eurobond restructuring complete

Key messages of the today's comments

Ukrainian bond market

Domestic bond market still in summer lull

Banks maintain their interest primarily in reserve bonds, while non-banking investors prefer paper with short maturities.

Eurobond restructuring complete

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Foreign exchange market

NBU keeps hryvnia in narrow corridor

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Economics

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MONDAY, 2 SEPTEMBER 2024

Banks' reserves market (30 August 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%)[1]	13.00	+0bp	-900bp
ON rate (%)	13.00	+0bp	-500bp
Reserves (UAHm)[2]	240,295	+4.3	+36.0
CDs (UAHm)[3]	506,208	-4.2	-4.1

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) (30 August 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU	677,606	+0.0	-1.9
Banks	733,491	+0.5	+32.5
Residents	172,506	+0.0	+41.9
Individuals	67,458	+1.2	+41.2
Foreigners	27,135	-1.4	-43.9
Total	**1,678,920**	**+0.2**	**+14.7**

Source: NBU, ICU.

FX market indicators (30 August 2024)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	41.0450	-0.8	+11.1
EUR/USD	1.1048	-1.3	+1.1
DXY	101.698	+1.0	-1.4

Source: Bloomberg, ICU.

Market gov't bond quotes (2 September 2024)

Maturity	Bid (%)	Ask(%)
6 months		
12 months		
2 years		
3 years		
12 months ($)		
2 years ($)		

Source: ICU.

Ukrainian bond market

Domestic bond market still in summer lull

Banks maintain their interest primarily in reserve bonds, while non-banking investors prefer paper with short maturities.

Last week, demand in the primary bond market was concentrated in new three-year notes, which the MoF issued to replace reserve bonds that had been redeemed at the beginning of August. Banks gradually reinvested funds in the new paper, but they also bought older reserve instruments.

Total trading in the secondary market increased thanks to banks' demand for reserve bonds, which accounted for about one-third of total volume traded.

Last month, the MoF borrowed UAH27.2bn while redeeming UAH20bn. There were no redemptions or borrowings in foreign currencies. Therefore, the rollover of UAH debt was 136% in August and 158% in 8M24. Rollover in hard currencies remained unchanged at 132% for USD and 81% for euros. Total rollover in 8M24 was 141%, the same as in 7M24. Total net borrowings of the government in the domestic market reached UAH88.3bn in 8M24.

This month, small redemptions in hryvnia totalling UAH4.1 bn are scheduled, while in hard currency, the planned repayments are US$350m and EUR77m.

ICU view: The MoF's offering of a new reserve paper helped keep the primary bond market reasonably active, but demand for other issues of bills declined compared with July. The secondary bond market also remains concentrated in reserve securities, i.e. paper that banks can use to cover part of mandatory reserves. We don't expect any significant pickup in new placements and trading in the coming weeks. Given prevailing expectations that interest rates will remain little changed in the near future, investors are broadly reluctant to increase bond portfolios. This autumn, the MoF is faced with large redemptions in hard currency, and it, thus, plans to offer FX-denominated bills almost every week.

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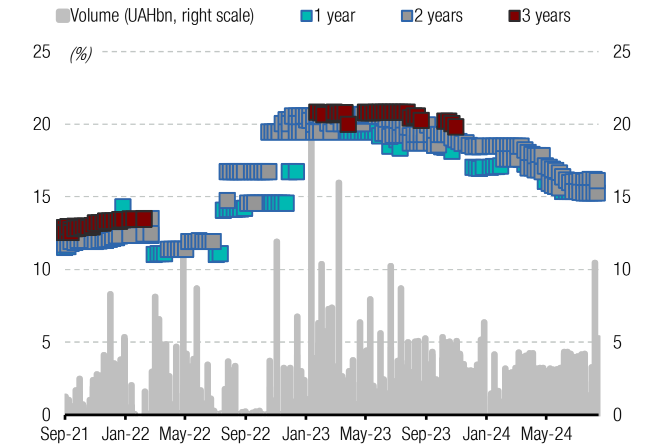
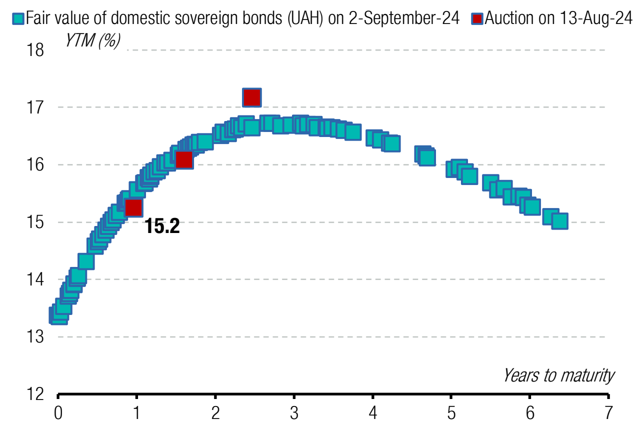
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

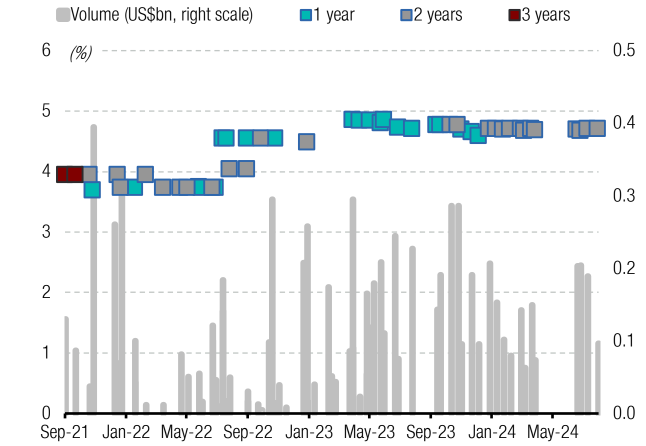
YTMs of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

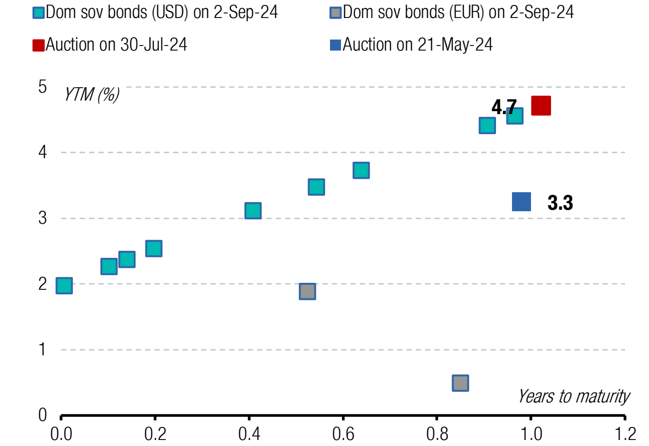
Chart 2. FX-denominated bonds

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 restructuring complete

Last Friday, Ukraine completed the restructuring of Eurobonds and received record-high support from investors.

After the start of the restructuring, the MoF decided to extend the early consent period, which allowed investors to receive a consent fee, as some Eurobond holders were facing technical issues in delivering their participation instructions through their custodians and clearing systems. Other deadlines remained unchanged. In the end, the MoF received votes representing 97.4% of the principal amount of the outstanding notes. Thirteen sovereign Eurobonds and the Ukravtodor paper were exchanged for eight new issues of sovereign Eurobonds.

The quote for new instruments was close to 40 cents per dollar, except for Series A bonds due in 2029, which were quoted at 60 cents per dollar. This bond is the shortest of all new papers and the only one that already bears a coupon.

YTMs were mostly above 16%, except for Series B bonds due on 2035-36, which were quoted with YTMs slightly below 13%. Holders of these bonds are eligible to receive extra bonds in 2030, if the size of the Ukrainian economy in 2028 exceeds the IMF forecast.

ICU view: The market expected a swift formal approval of the exchange offer after the largest institutional investors indicated their consent to restructuring terms. Vote participation far exceeded the 75% level reached in 2022, when investors gave their approval for payment deferral. Ukraine is now in a position to write off 37% of the face value of Eurobonds and accrued interest (just above US$8.5bn or nearly 6% of sovereign debt at the end of July). However, 12% of the debt written off can potentially be recovered by investors in 2030.

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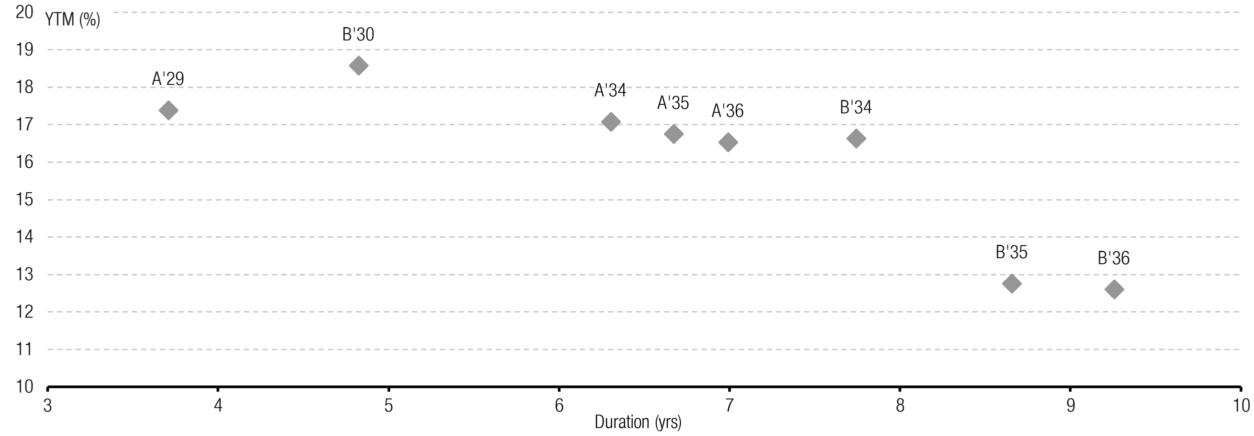
Chart 3. Banks reserves usages over last 90-day period (UAHm)



Notes: A-Step Up A Bonds, B – Step Up B Bonds

Source: NBU, ICU.

Foreign exchange market

NBU keeps hryvnia in narrow corridor

The hryvnia slightly appreciated last week while the NBU's interventions edged up.

The hard-currency deficit was up by 16% to US$355. NBU interventions rose to US$646m, thus remaining above the weekly average YTD.

Net FX purchases of foreign currency by legal entities rose by 13% to US$256m in the four days of the week. In the retail segment, net purchases rose to US$99m, staying below the weekly average YTD.

Over the week, the official hryvnia exchange rate strengthened by 0.4% to UAH41.06/US$, and the cash hryvnia in systemically important banks appreciated by 0.3% to UAH4.9-41.4/US$.

ICU view: The NBU continues to limit exchange rate fluctuations while keeping it slightly above UAH41/US$. This came at a cost, as the NBU has been increasing interventions for two weeks in a row, and they again exceed the average weekly interventions YTD. Decisive NBU steps to limit exchange rate volatility over the past couple of weeks weakened the anxiety of businesses and households after the market went through a period of turbulence in mid-July. We expect the NBU to resume a managed and gradual weakening of the hryvnia in September. The pace of devaluation is likely to be slower than in 1H24. We expect the exchange rate to be UAH42.6/US$ at the end of the year.

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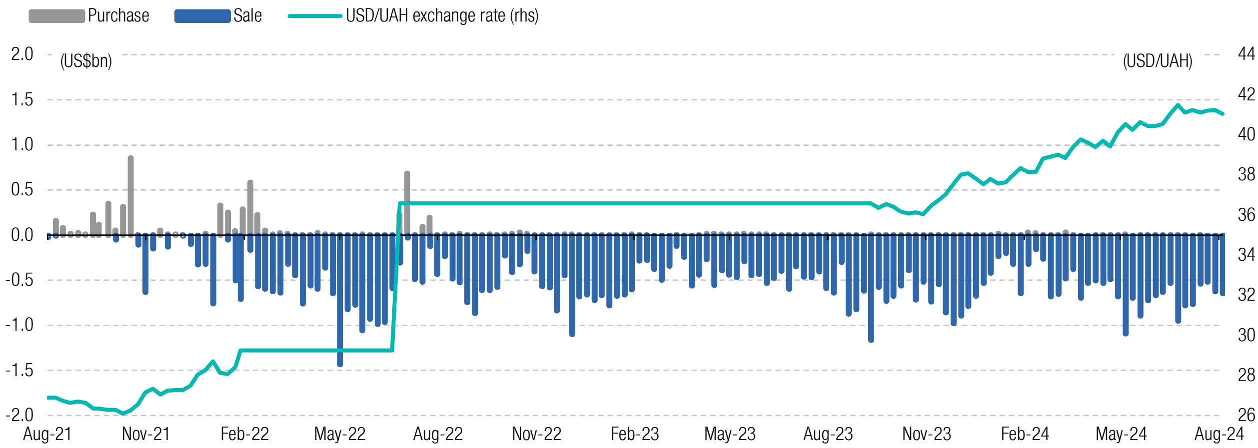
Chart 4. FX market indicators, 3-year history

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



Source: NBU, Bloomberg, ICU.

Economics

Current account worsens in July, set to improve by year-end

The monthly current account (C/A) worsened in July taking the 7M24 deficit to US$10.9bn, but it is set to improve dramatically by year-end.

The C/A gap widened to US$2.2bn in July, the second largest monthly shortfall since the start of russia's full-scale invasion of Ukraine. The monthly deficit of trade in goods was just above US$3.0bn, the largest monthly number since the invasion. The deterioration in the trade balance and current account came on the back of an upsurge in imports, up 14% YoY in July, as consumer demand remained strong and Ukraine also bolstered imports of energy-generating equipment to deal with electricity shortages. Exports also surged in July, up 29% YoY, as agro producers were quick to deliver the new grain and rapeseed harvest abroad. There were no major noticeable changes in other BoP components. Migrant remittances and transfers to the private and the official sector fell short of the foreign trade deficit. Ukraine did not receive any meaningful budgetary grants in July.

The financial account (F/A) balance was also negative in July as outflows of private capital remained substantial while government did not receive significant loans in July. A bigger part of the combined (C/A+F/A) deficit was offset with an IMF loan of US$2.2bn (recorded below the line in BoP statistics). Also, the NBU spent net US$0.7bn (1.7%) of its reserves to cover the remaining gap.

ICU view: The downward trend of Ukraine's current account is set to reverse by the year-end as the economy is scheduled to receive up to US$11bn in grants (secondary income component of BoP) in 2H24 from the US and the EU. These grants will most likely be nearly sufficient to offset other negative BoP components. We thus expect that the C/A gap for the full year will remain close to the 7M24 level of around US$11bn. This implies the C/A for the full year of 2024 will deteriorate only marginally to 5.6% of GDP from 5.4% of GDP in 2023. The financial account will be in surplus in the four remaining months of the year. This implies the NBU might see an increase in reserves to above US$43bn by the end of 2024. This will offer a thick cushion against a possible imbalance in the FX market.

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Chart 5. Key balance of payment components, $m

Current account deficit widens further in July

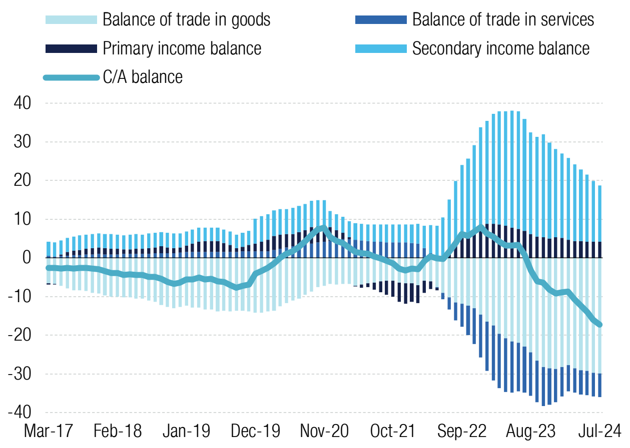
	Jul.24	Jun.24	Jul.23
Current account	**-2,241**	**-2,150**	**-933**
Trade in goods	-3,031	-2,776	-2,940
Trade in services	-585	-478	-600
Primary income	422	349	368
incl. migrant income	704	667	893
Secondary income	953	755	2,239
incl. transfers to gov't	119	104	1,506
Financial account*	**732**	**-1,203**	**-3,499**
Change in trade credits	-647	-590	-454
Change in cash out of banks	1,441	1,285	554
Net loans to government	52	-1,951	-3,145
Other	-114	53	-454

* negative numbers in financial account indicate increase in liabilities (cash inflow)

Source: MoF, ICU.

Chart 6. Current account, 12-month trailing, $bn

12-month current account balance keeps deteriorating



Source: NBU, ICU.

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