Focus
Ukraine

Markets
Government bonds, FX market, and macro

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Weekly Insight

NBU amends monetary policy design

Key messages of the today's comments

MONDAY, 23 SEPTEMBER 2024

Ukrainian bond market

Banks' demand for bonds up as new reserve requirements rolled out

Banks keep purchasing large volume of UAH bonds as the NBU is rolling out a new set of regulations to incentivize them to increase portfolios.

Eurobond prices up on positive news

Prices of new Ukrainian Eurobonds increased last week on a number of various positive news.

Foreign exchange market

NBU increases interventions to keep hryvnia steady

Last week, the NBU increased interventions to push the hryvnia exchange rate to UAH41.35/USD after allowing hryvnia to weaken to nearly UAH41.5/USD earlier last week.

Economics

NBU amends monetary policy design

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Banks' reserves market (20 September 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%)[1]	13.00	+0bp	-700bp
ON rate (%)	12.99	+0bp	-301bp
Reserves (UAHm)[2]	268,901	+13.5	+19.9
CDs (UAHm)[3]	470,805	-4.3	+1.4

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 September 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU	677,606	+0.0	-1.9
Banks	764,061	+1.0	+34.9
Residents	174,211	+1.7	+44.4
Individuals	68,834	+2.1	+44.4
Foreigners	25,840	-3.4	-47.7
Total	**1,711,325**	**+0.7**	**+15.9**

Source: NBU, ICU.

FX market indicators (20 September 2024)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	41.3406	-0.1	+11.9
EUR/USD	1.1162	+0.8	+4.7
DXY	100.723	-0.4	-4.4

Source: Bloomberg, ICU.

Market gov't bond quotes (23 September 2024)

Maturity	Bid (%)	Ask(%)
6 months	15.00	14.00
12 months	15.75	15.00
2 years	16.75	15.50
3 years	17.75	16.50
12 months ($)	5.00	4.50
2 years ($)	N/A	N/A

Source: ICU.

Ukrainian bond market

Banks' demand for bonds up as new reserve requirements rolled out

Banks keep purchasing large volume of UAH bonds as the NBU is rolling out a new set of regulations to incentivize them to increase portfolios.

Last week, the MoF borrowed UAH12.8bn and EUR23m. The larger part of new proceeds came from two and three-year bonds, about UAH5bn from each issue. See details in the auction review.

Trading in the secondary market was insignificant for the second week in a row. Total volume rose by 21% to UAH5.7bn, significantly below the weekly average YTD. FX-bonds' share in trading declined to 23%.

The total portfolio of domestic bonds held by the private sector hit a new historic high last week, UAH1.7tn. Banks increased portfolios the most, by UAH8bn to UAH764bn. Household portfolios recovered after having declined earlier this month due to redemptions. It also reached a new historical high, UAH69bn. Non-bank legal entities increased portfolios by UAH3bn to UAH174bn. Only foreign investors decreased portfolios.

ICU view: Last week, the NBU revised the mandatory reserve requirements for banks and increased the share of reserves that banks can cover with designated government bonds. The new norms will take effect on October 11. Banks' activity in the primary bond market in recent weeks was likely driven by these expected changes. Banks purchased certain bonds in advance, anticipating that the NBU would add them to the list of designated bonds. We also expect heightened demand for new bonds at the primary auction tomorrow and going forward. However, cut-off interest rates are unlikely to change, while competition can slightly decrease weighted average rates.

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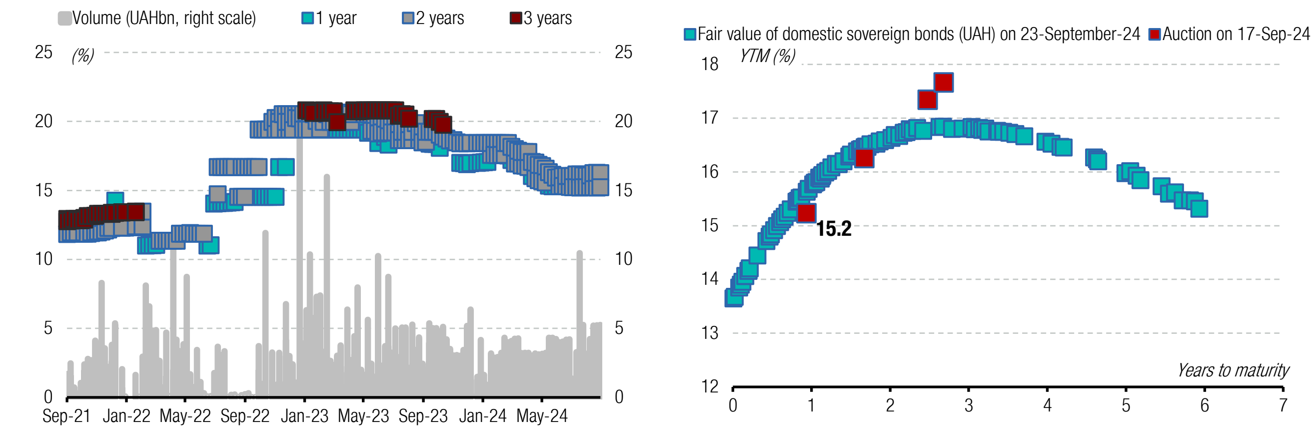
Chart 1. Local-currency bonds

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

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

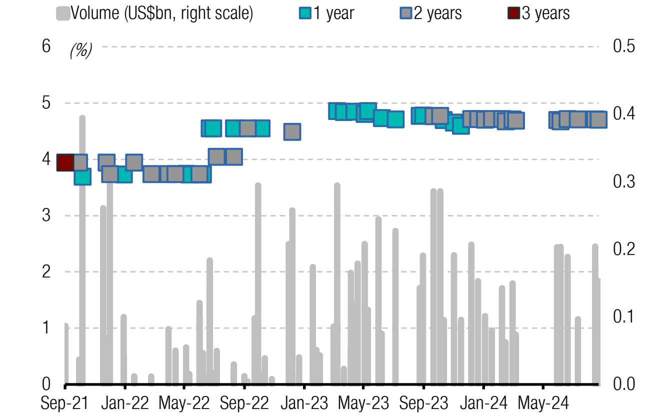


Source: MFU, ICU.

Source: NBU, MFU, ICU.

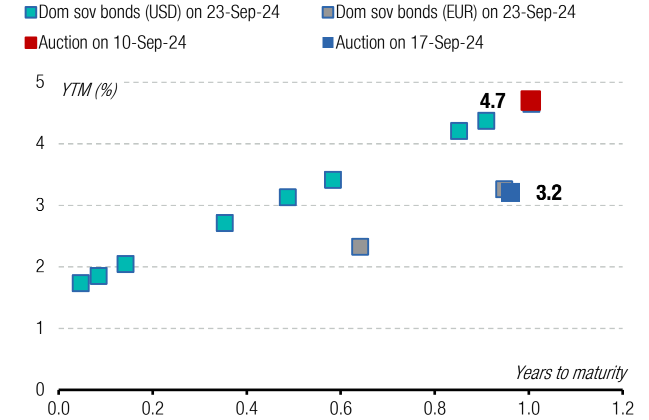
Chart 2. FX-denominated bonds

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 on positive news

Prices of new Ukrainian Eurobonds increased last week on a number of various positive news.

On average, Eurobond prices rose by 2%, but not evenly. Step Up bond B due in 2035-36 added 5% and 6% to their prices, respectively. Prices of Step Up bond A due in 2029 and Step Up bond B due in 2034 rose by 2%, while other bond prices rose insignificantly or declined. The EMBI index rose by 0.7% last week.

ICU view: The recent positive news pushed Eurobond prices up last week. The positive developments include an addition of bonds to the JP Morgan index, assignment of ratings for new bonds, and a successful completion of the IMF mission in Ukraine. The most significant price increase for Step Up bond B due in 2035-36 can be due to the news about a EUR35bn loan for Ukraine from the EU, which will be repaid from russian frozen assets. This loan can support economic growth and increase the likelihood that the principle of these bonds will increase in 2030.

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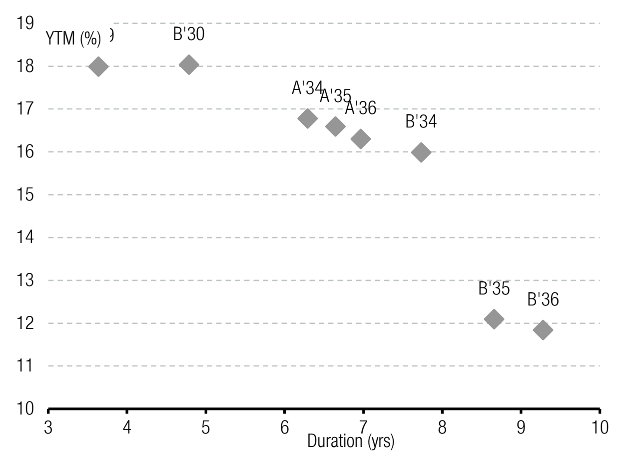
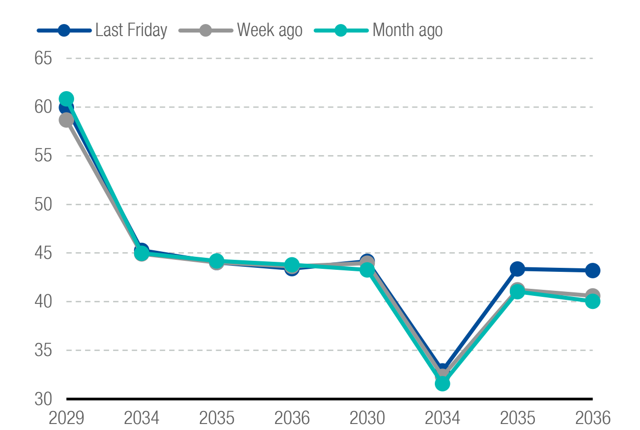
Chart 3. Ukrainian Eurobonds yields and prices

Eurobond yields map



Source: Bloomberg, ICU.

Prices of Eurobonds as of last Friday, two weeks and 2 September, 2024



Source: Bloomberg, ICU.

Foreign exchange market

NBU increases interventions to keep hryvnia steady

Last week, the NBU increased interventions to push the hryvnia exchange rate to UAH41.35/USD after allowing hryvnia to weaken to nearly UAH41.5/USD earlier last week.

The total FX market deficit increased last week (in four business days) by 22% to US$567m. Bank clients (legal entities) increased net hard currency purchases by 30% to US$346m. Households' net purchases rose by 11% to US$221m.

The NBU sold US$826m from international reserves, or 11% more than the week before. Daily interventions were above this year's average.

The official hryvnia exchange rate weakened by 0.1% to 41.35%, while the cash exchange rate weakened by 0.1% to UAH41.1-41.7/US$.

ICU view: The hard currency deficit and NBU interventions remained high for the third consecutive week. By balancing the market and satisfying excessive demand, the NBU kept the exchange rate below UAH41.5/US$ for the tenth week. Legal entities probably decreased hard currency sales last week, anticipating the NBU would allow the hryvnia to weaken gradually. However, the NBU is likely not yet ready for this and will keep the hryvnia exchange rate close to the current level this week.

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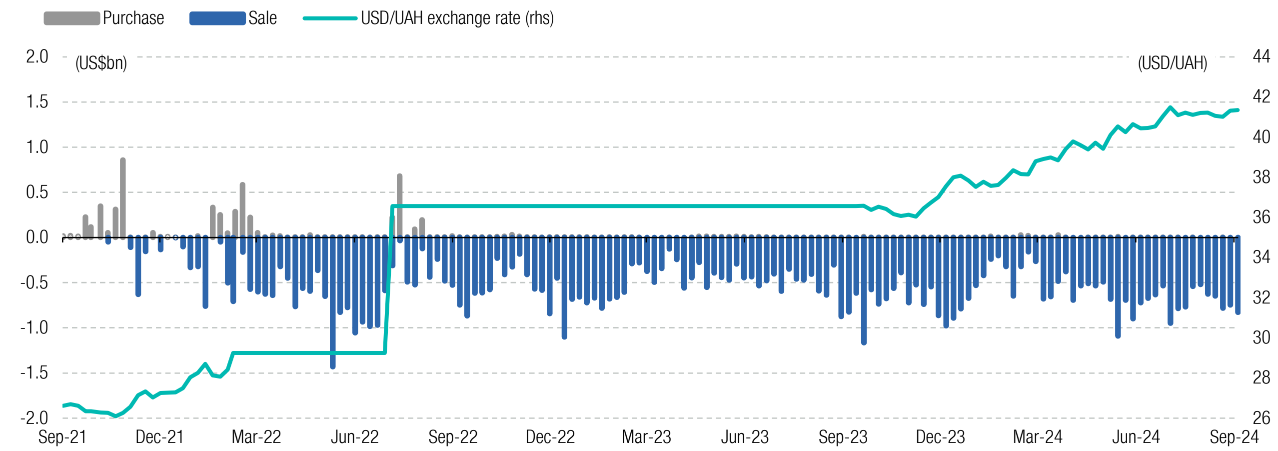
Chart 4. FX market indicators, 3-year history

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



Source: NBU, Bloomberg, ICU.

Economics

NBU amends monetary policy design

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Additionally, banks will face tougher mandatory reserve requirements on all customer accounts except retail term deposits in UAH with a maturity of 93 days or more. For these, the reserve requirement will remain 0%. Banks will be allowed to hold up to 60% of their mandatory reserves in designated government bonds, up from the current 50%.

ICU view: We expect the NBU to stick to its current macroeconomic forecast and abstain from cutting the rate at least during the two remaining revisions in October and December of this year. The probability of reverting to rate hikes is currently low.

The NBU is trying to assist the Ministry of Finance in financing the budget deficit by creating additional incentives for banks to increase their holdings of government bonds. The higher coverage of reserves by bonds is likely to generate an additional UAH20 to 40 billion in demand in October, while the increased reserve requirements will further boost demand.

The zero mandatory reserve requirement for retail deposits in UAH aims to encourage banks to increase such deposits, as opposed to current accounts. This may also weaken household consumption in favor of saving and, subsequently, ease inflationary pressures and pressures on FX market.

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