

Weekly Insight

Inflation at 12.9% in January

Key messages of the today's comments

MONDAY, 17 FEBRUARY 2025

Ukrainian bond market

MoF halts yields increase; borrowings at record low

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Bondholders maintain optimism

Ukrainian Eurobond prices continued to rise last week in anticipation that ceasefire negotiations will continue and bear fruit.

Foreign exchange market

NBU interventions up to average volume

The NBU allowed the hryvnia to weaken only by 0.4% last week, increasing interventions by half to slightly above the weekly average during the war.

Economics

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Consumer inflation picked up further to 12.9% in January, up from 12.0% in December. It will keep accelerating through May due to the low base effect, but is expected to reverse sharply in June.

Banks' reserves market (14 February 2025)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	14.50	+0bp	-50bp
ON rate (%)	14.50	+0bp	-50bp
Reserves (UAHm) ²	257,229	+26.6	+11.6
CDs (UAHm) ³	482,901	-8.5	-9.3

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) (14 February 2025)

	Last	Weekly chg (%)	YoY chg (%)
NBU	677,606	+0.0	-1.1
Banks	878,554	-0.4	+32.2
Residents	205,468	+1.7	+35.7
Individuals	83,145	+3.3	+38.6
Foreigners	22,294	-0.7	-49.5
Total	1,867,480	+0.1	+16.2

Source: NBU, ICU.

FX market indicators (14 February 2025)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	41.5943	+0.2	+9.3
EUR/USD	1.0492	+1.6	-2.2
DXY	106.710	-1.2	+1.9

Source: Bloomberg, ICU.

Market gov't bond quotes (17 February 2025)

Maturity	Bid (%)	Ask (%)
6 months	15.50	14.25
12 months	16.50	15.25
2 years	18.00	16.50
3 years	18.50	17.00
12 months (\$)	5.00	4.50
2 years (\$)	N/A	N/A

Source: ICU.

Ukrainian bond market

MoF halts yields increase; borrowings at record low

Last week, the MoF opted not to raise rates further on military bonds. Yet, it set rates on a new two-year paper slightly above the yield curve.

The MoF decided not to raise interest rates on military bonds last week. Therefore, the cut-off rates for 17-month and 2.4-year bonds remained unchanged, although the weighted average rates were up by 7-10bp. At the same time, for a new two-year ordinary UAH bill, the MoF set the cut-off rate at 16.65%, which is 80bp above the yield for 17-month paper but only 30bp lower than that for 2.4-year securities, while it should be close 16.5% to be on a yield curve. Last week's borrowings stood at just UAH1bn, the smallest amount since December 2022. See details in the [auction review](#).

The secondary bond market is very gradually adjusting to the recent MoF decisions to raise cut-off rates in the primary auctions. Last week, weighted-average YTM of deals rose by about 10-20bp, but for selected instruments only. Total turnover in the secondary bond market declined by 28% WoW to UAH7.2bn, and was concentrated in military bonds (68% in total turnover). The share of FX-denominated bonds rose to 33%.

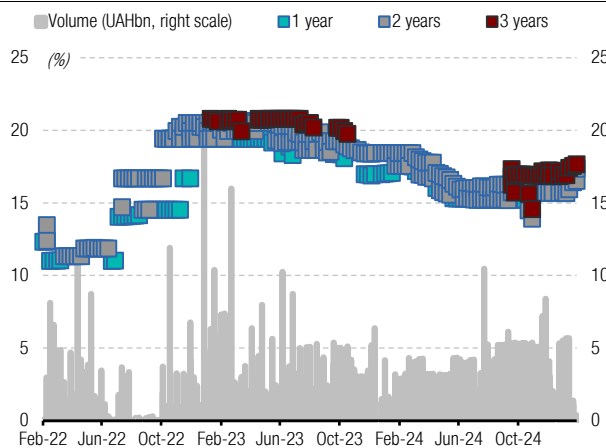
Portfolios of retail investors rose by almost 3% to above UAH83bn last week, a new record high, with the share of UAH bonds slightly over 50%. Non-bank investors purchased bonds from banks and also increased their portfolios.

ICU view: The MoF halted the increase in yields in the primary bond market after it increased them by just half of the size of the cumulative increase in the NBU key policy rate from December. We think further increases in interest rates in the primary bond market are unlikely, even though demand remains low. It is unlikely that interest rates are currently the obstacle that most limits investors' interest in government bonds.

The next local debt redemption is scheduled for next week and will be the largest ever at UAH41bn. However, we do not expect the MoF will attempt to borrow the full amount of funds in advance. We anticipate that a significant part of redemption proceeds will be reinvested in the following weeks.

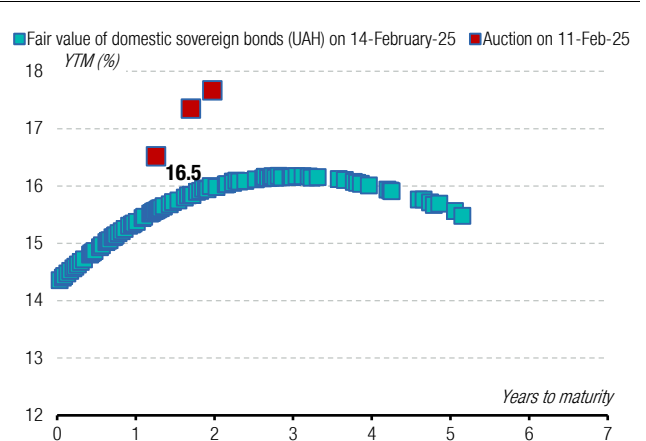
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

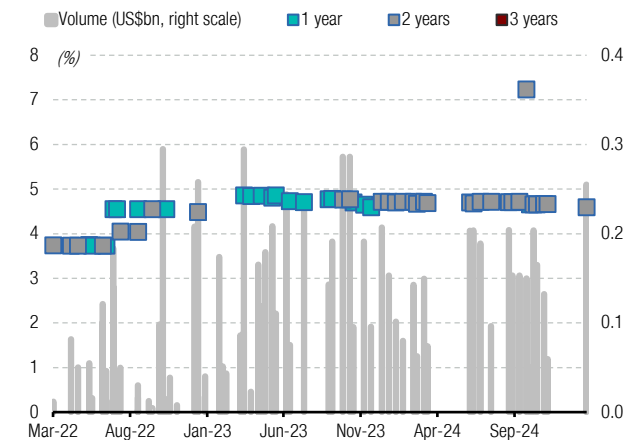
YTM of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

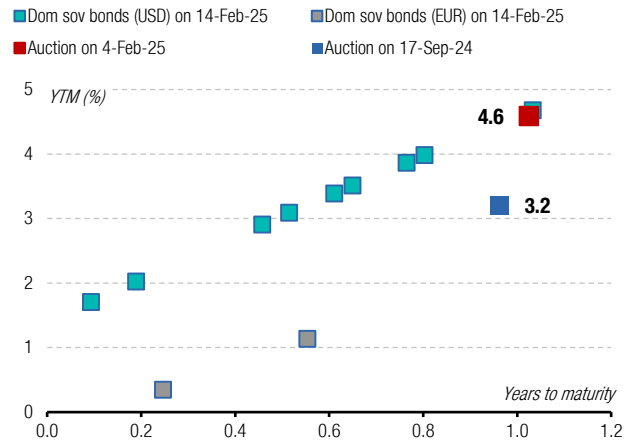
Chart 2. FX-denominated bonds

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



Source: MFU, ICU.

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



Source: NBU, MFU, ICU.

Bondholders maintain optimism

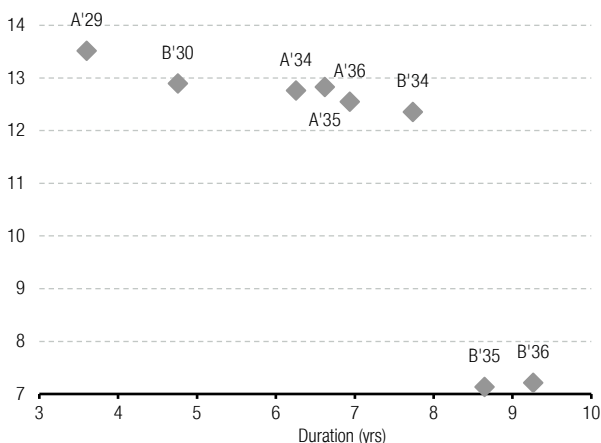
Ukrainian Eurobond prices continued to rise last week in anticipation that ceasefire negotiations will continue and bear fruit.

Eurobond prices rose by 2% to new historical highs last Thursday. Prices of UKRAIN'B'35 and UKRAIB'B'36 rose the most, by 4%, as their holders may get extra bonds in 2030 if Ukrainian GDP reaches a threshold in 2028. Ukrainian VRI prices slid by 1.5% to below 86 cents per dollar of notional value. The EMBI index rose by 0.1% last week.

ICU view: The Munich Security Conference was last week's key event, but eventually it failed to generate any specifics about the negotiation plan and possible formula for ending the war. Also, last Friday, it became crystal clear that representatives of the US, Europe, and Ukraine have different views on their role in the peace process. This caused investor enthusiasm to weaken somewhat and a minor price correction was observed last Friday. Despite this, general investor sentiment remains positive in anticipation of more details that are set to be discussed at the meetings of US and Russian leaders in Saudi Arabia in late February.

Chart 3. Ukrainian Eurobond YTM's and prices

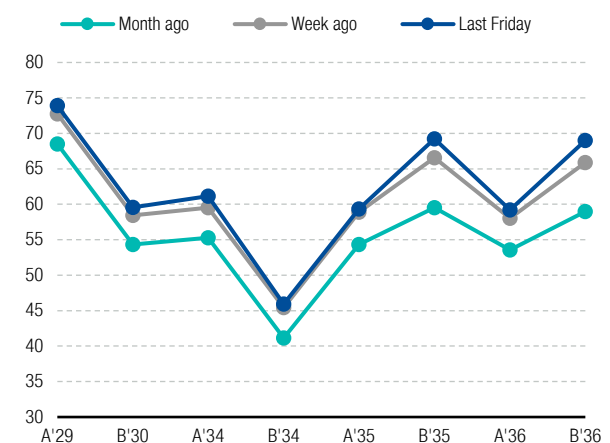
Eurobonds yield map



Note: The nominal value of Series B bonds due in 2035 and 2036 may increase in 2030

Source: Bloomberg, ICU.

Prices of Eurobonds as of last Friday, a week and a month ago



Source: Bloomberg, ICU.

Foreign exchange market

NBU interventions up to average volume

The NBU allowed the hryvnia to weaken only by 0.4% last week, increasing interventions by half to slightly above the weekly average during the war.

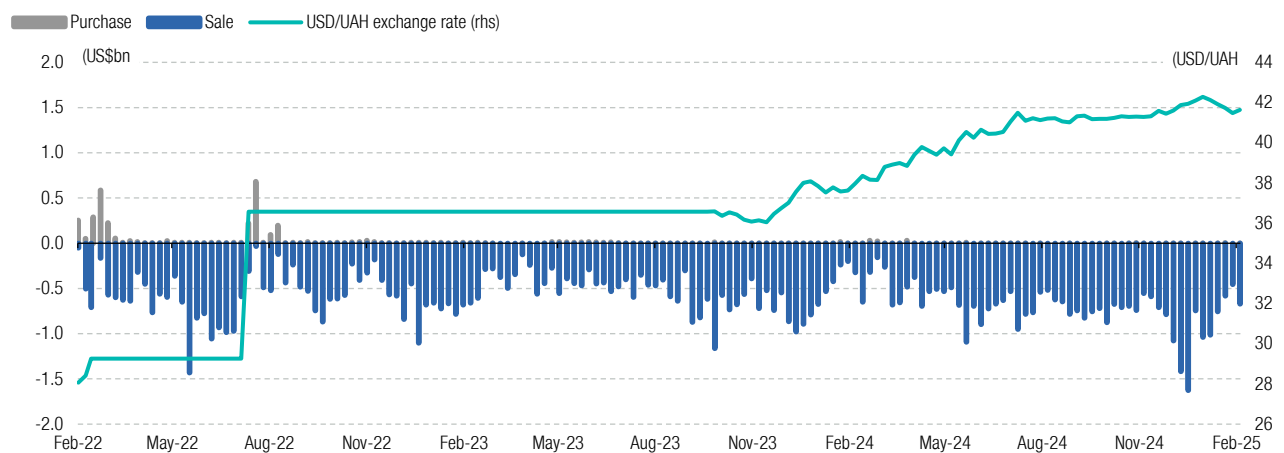
The deficit of foreign currency in the interbank FX market almost tripled last week, from US\$94m to US\$250m. At the same time, net hard-currency purchases in the retail segment fell by 28% WoW to US\$178m. Therefore, the total hard-currency deficit rose by 25% WoW to US\$428m, causing the NBU's interventions to rise by 47% to US\$670m.

The official hryvnia exchange rate weakened by 0.4% to UAH41.63/US\$, the same level as in mid-December.

ICU view: The NBU significantly increased interventions WoW, which corresponded to their weekly average for the last three years since the full-scale war began (US\$605m) and for an average for the period since the NBU switched to a managed flexible FX regime (US\$683m). If the FX market shortage does not increase in the coming week, the NBU may choose to keep the hryvnia official exchange rate close to UAH42/US\$.

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

Inflation at 12.9% in January will accelerate through May

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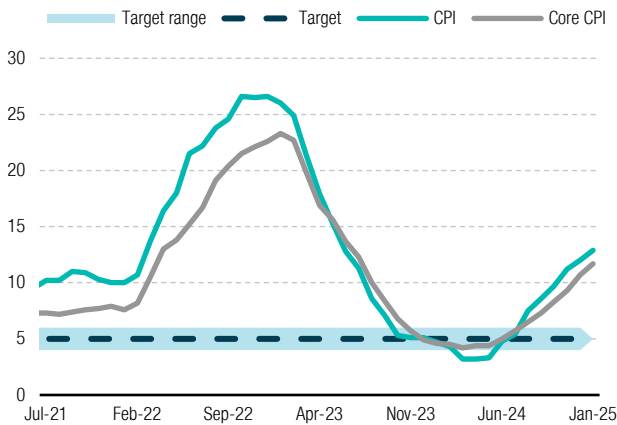
Notably, monthly inflation decelerated to 1.2% in January from 1.4% in December and was at the lowest level since August 2024. In YoY terms, the prices for transportation (a January hike in motor fuel excise tax is to blame), healthcare, alcohol, and tobacco continued to accelerate. Yet, the growth in food prices, the key driver of consumer inflation in 2H24, has remained broadly stable over the past three months. Price growth remained little changed for clothes and footwear, utilities, and appliances.

ICU view: By our estimates, a hike in motor third-party liability insurance fees and an upsurge in the mobile communication fee contributed about 0.4pp to monthly inflation last month. The increase in the price of these two components was to a large extent

driven by regulatory decisions rather than a reflection of regular yearly price revisions by the service providers. Net of these effects, the monthly increase in consumer prices was close to 0.8% and that is a clear signal the inflationary pressures are starting to ease. Another important observation is that the growth rate for food prices seems to be peaking, as it has remained little changed from November. This implies that effects of a summer draught that undercut the harvest in Ukraine last year are also fading away. Despite weakening price pressures, we expect that annual inflation will continue to accelerate till May due to the base effect as inflation was abnormally low in 5M24 (consumer prices were up by only 2.0%, well below the pace consistent with the NBU inflation target of 5% YoY). We maintain our projection of end-2025 CPI of 7.0% if weather doesn't surprise to the downside again and the harvest recovers from last year's low levels. We expect the NBU will deliver another 50 bp increase in key policy rate in March in line with its guidance.

Chart 5. CPI, core CPI and target, YoY, %

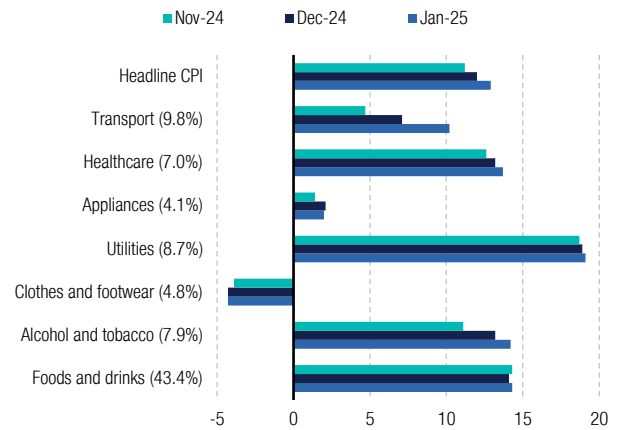
Annual inflation is likely nearing its peak



Source: Ukrstat, NBU, ICU.

Chart 6. CPI and its main components, YoY, %

Growth in food prices leveled off



* numbers in brackets indicate the share of the component in consumer basket

Source: Ukrstat, ICU.

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