

# Weekly Insight

## NBU's mood becoming more positive

### Key messages of the today's comments

#### Domestic liquidity and bonds market

##### T-notes in foreigners' portfolios above UAH110bn

After last week's auction, T-notes in foreigners' portfolios rose above UAH110bn (US\$4.7bn) and will continue to increase after yesterday's auction by about UAH5bn (US\$200m).

##### Budget expenditures increased liquidity

Last week, the total amount of banking sector liquidity rose to UAH162.5bn, setting a new record high. This week, liquidity will continue to rise on support from the NBU and budget expenditures.

#### Foreign exchange market

##### Hryvnia still appreciating

Last week, the hryvnia appreciated to UAH23.49/US\$, slightly weaker than at the beginning of 2016. Despite the increase in liquidity and large budget expenditures, the hryvnia continues to appreciate, and this week it should get closer to UAH23/US\$.

#### Economics

##### NBU's mood becoming more positive

Lower-than-expected inflation in November enabled the regulator to make a larger rate cut, from 15.5% to 13.5%. We expect a faster decrease of real rates in 1H20.

WEDNESDAY, 18 DECEMBER 2019

#### Banks' reserves market (17 December 2019)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) <sup>1</sup>	13.50	-200bp	-450bp
ON rate (%)	12.08	-176bp	-523bp
ON \$ swap (%)	10.51	-192bp	-618bp
Reserves (UAHm) <sup>2</sup>	70,930	+17.86	+10.73
DepCerts (UAHm) <sup>3</sup>	93,180	-1.07	+174.74

Notes: [1] NBU's key policy rate; [2] stock of banks' reserves held at NBU; [3] stock of NBU's short-term bonds.  
Source: NBU, Bloomberg, ICU.

#### Breakdown of gov't bond holders (UAHm) (17 December 2019)

	Last	Weekly chg (%)	YoY chg (%)
NBU	337,065	+0.00	-3.17
Banks	323,318	-1.06	-8.34
Residents	25,659	-2.07	+35.95
Individuals	9,445	-2.64	+59.81
Non-res <sup>4</sup>	110,119	+3.82	+1,657.99
<b>Total</b>	<b>805,605</b>	<b>-0.02</b>	<b>+10.08</b>

Notes: [1] non-residents  
Source: NBU, ICU.

#### FX market indicators (17 December 2019)

	Last	Weekly chg (%)	YTD chg (%)
USD/UAH	23.4650	-0.55	-15.75
EUR/USD	1.1150	+0.18	-1.74
DX <sup>2</sup>	97.222	-0.20	+0.13
UAH TWI <sup>3</sup>	139.421	+0.14	+18.77

Notes: [1] UAH trade-weighted index.  
Source: Bloomberg, ICU.

#### Gov't bond quotes<sup>1</sup> (18 December 2019)

Maturity	Bid	Ask
6m	14.25	12.25
12m	14.25	12.00
2y	14.00	11.75
3y	14.00	11.50
12m (\$)	5.00	3.75
2y (\$)	5.00	4.00

Notes: [1] Actual quotes you can see at [www.icu.ua](http://www.icu.ua).  
Source: ICU.

# Domestic liquidity and bonds market

## T-notes in foreigners' portfolios above UAH110bn

After last week's auction, T-notes in foreigners' portfolios rose above UAH110bn (US\$4.7bn) and will continue to increase after yesterday's auction by about UAH5bn (US\$200m).

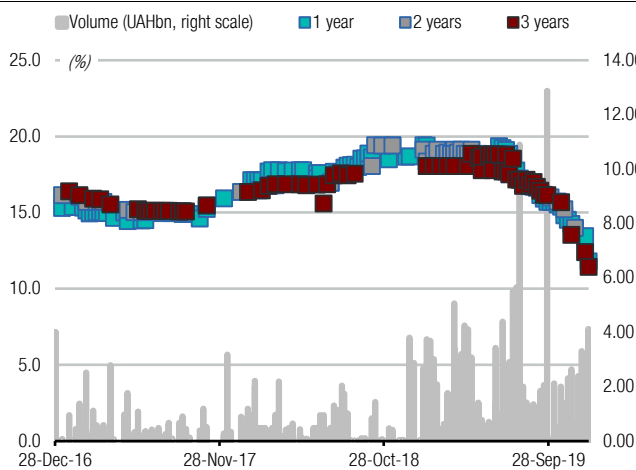
Taking into account that last week about UAH1bn (US\$40m) and UAH3bn (US\$120m), of 2.6- and four-year notes, respectively, were sold, most of these notes were purchased by foreigners. We see this from the increase in their portfolios by the same UAH4bn (US\$160m) to UAH110.1bn (US\$4.7bn).

**ICU view: As the result of yesterday's primary auction, most bonds could have been purchased by foreigners, as they are main bidders with low rates that are attractive and acceptable to the MoF. Therefore, we expect an increase in foreigners' portfolios by about UAH5bn (US\$200m) to UAH115bn (US\$4.9bn).**

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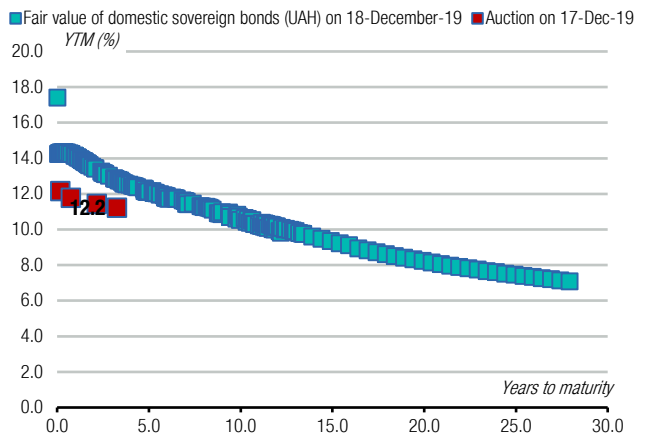
**Chart 1. Local-currency bonds**

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



Source: Ministry of Finance of Ukraine, ICU.

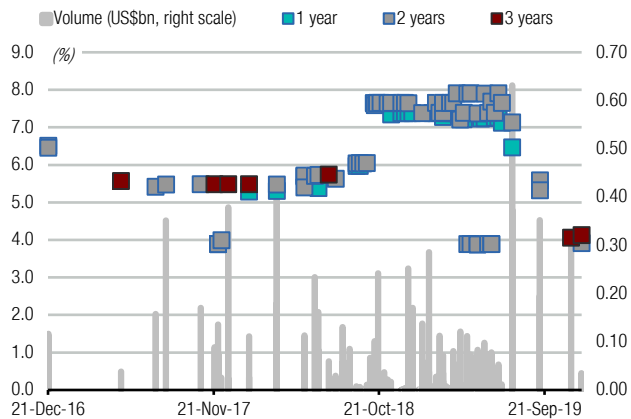
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: National Bank of Ukraine, Ministry of Finance of Ukraine, ICU.

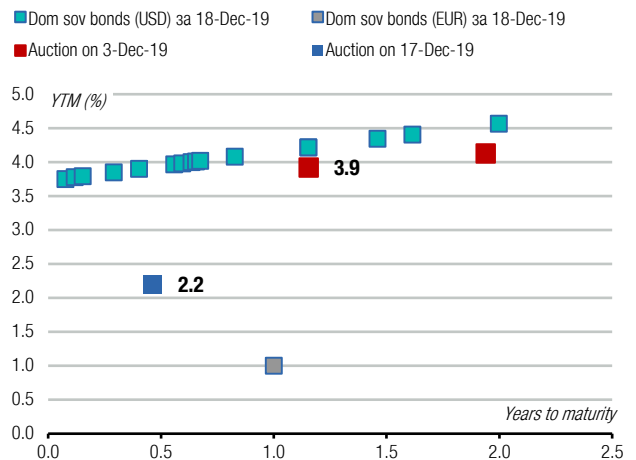
**Chart 2. FX-denominated bonds**

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



Source: Ministry of Finance of Ukraine, ICU.

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



Source: National Bank of Ukraine, Ministry of Finance of Ukraine, ICU.

**Budget expenditures increased liquidity**

Last week, the total amount of banking sector liquidity rose to UAH162.5bn, setting a new record high. This week, liquidity will continue to rise on support from the NBU and budget expenditures.

Totally banking sector liquidity rose by UAH15bn to UAH162.5bn on significant inflows via NBU monetary operations and Treasury operations. NBU purchased hard currency in the amount of UAH10bn and an additional UAH5bn were obtained by non-monetary operations. The Treasury injected UAH12.9bn and other non-monetary operations provided UAH0.4bn. Outflows via reserves exchange in cash were UAH8.4bn.

**ICU view:** This week, we do not expect significant liquidity outflows due to a positive balance of Treasury operations and a slight decrease in reserves exchange in cash. Month-end tax payments, which could start this Friday, will not have a large impact on liquidity, as we see an increase in budget expenditures, including the unusually large VAT refunds with more than UAH4.5bn paid so far, which is more than in most months of this year.

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**Chart 3. Banks reserves usages over last week(UAHm)**

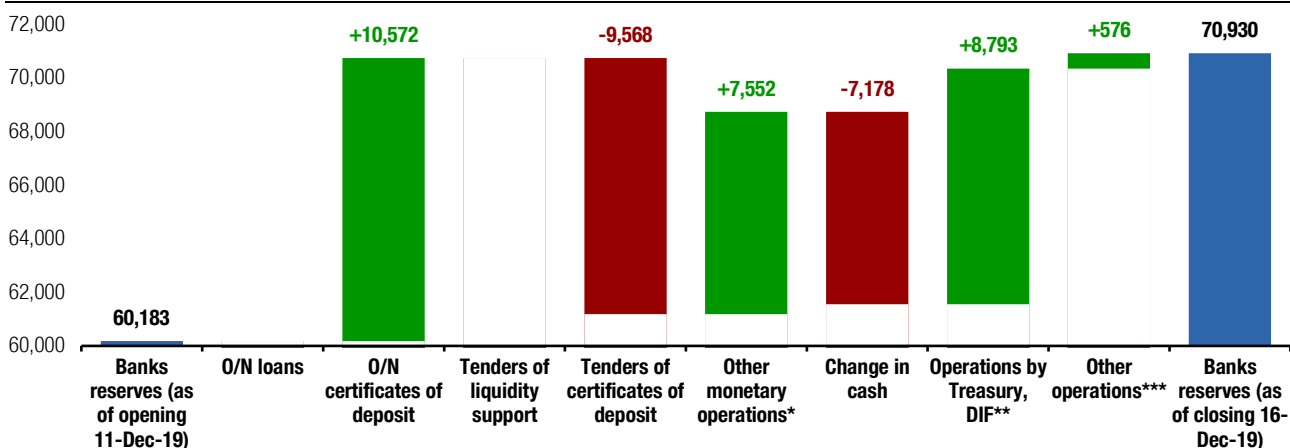
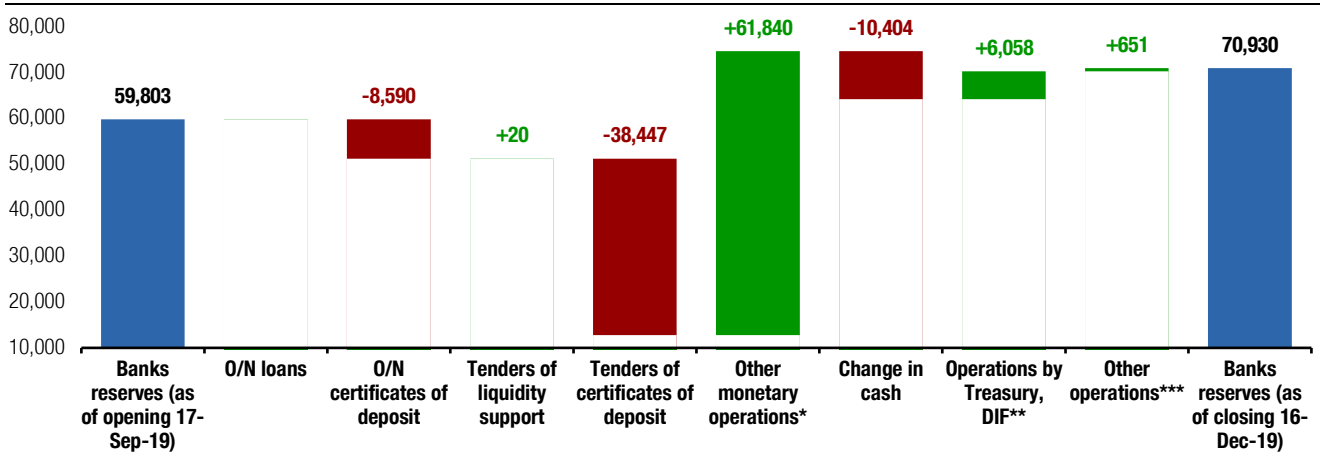


Chart 4. Banks reserves usages over last 90-day period (UAHm)



Notes: [1] data from the NBU's daily reporting [https://bank.gov.ua/control/uk/publish/article?art\\_id=38643651&cat\\_id=40807142](https://bank.gov.ua/control/uk/publish/article?art_id=38643651&cat_id=40807142) ;

\* operations repo, purchase and sale of government bonds, FX market interventions, stabilisation loans, FX swap agreements; \*\* DIF – deposit insurance fund;

\*\*\* interest payments on NBU's loans and on NBU's certificates of deposit, other operations. Source: NBU, ICU.

## Foreign exchange market

### Hryvnia still appreciating

Last week, the hryvnia appreciated to UAH23.49/US\$, slightly weaker than at the beginning of 2016. Despite the increase in liquidity and large budget expenditures, the hryvnia continues to appreciate, and this week it should get closer to UAH23/US\$.

Last week, the hryvnia appreciated by 1%, the same as the prior week. This was an increase of UAH0.23, bringing total appreciation over the last 12 months to 15.35%. NBU restrained appreciation for the second consecutive week by purchasing more than US\$400m per week, or US\$424.1m last week, US\$12.5m less than the week before.

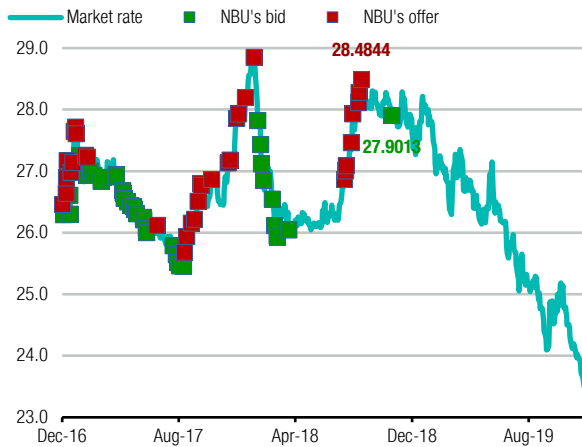
The hryvnia's CPI-based real trade-weighted index (which includes currencies of 27 countries that are trade partners of Ukraine) rose 0.4% to 139.5, while in YoY terms, it was up 18.7%.

**ICU view: This week, the MoF increased the offering of local-currency T-notes, which can cause an increase in FX supply, which continues support for the hryvnia exchange rate. We expect that the hryvnia will continue to appreciate this week, moving towards UAH23/US\$.**

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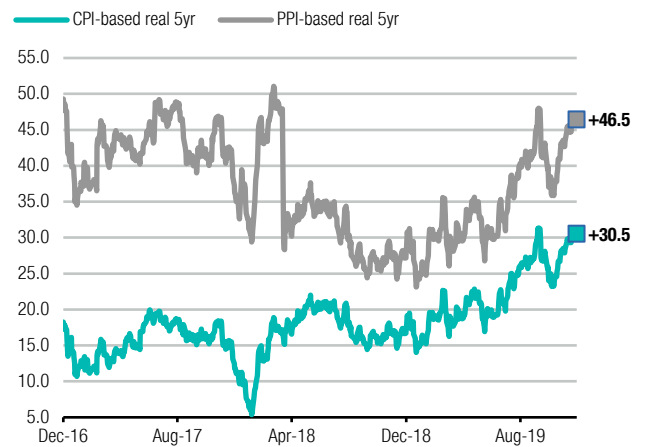
**Chart 5. FX market indicators, 3-year history**

*Ukraine hryvnia UAH exchange rate per US dollar at the interbank market*



Notes: the chart provides labels for the average exchange rate at last two NBU auctions (one on buying FX from the market and one on selling it). Source: NBU, Bloomberg, ICU.

*UAH exchange rate misalignment<sup>1</sup> from fundamental level<sup>2</sup> (%)*



Notes: [1] "+" overvalued, "-" undervalued; [2] based on the UAH's CPI- and PPI-based real TWIs. Source: ICU.

## Economics

### NBU's mood becoming more positive

Lower-than-expected inflation in November enabled the regulator to make a larger rate cut, from 15.5% to 13.5%. We expect a faster decrease of real rates in 1H20.

NBU just made the largest interest rate cut since early 2016, decreasing the key rate more than previously expected by both the market and the regulator's own forecast. It has also increased the daily amount of FX interventions from US\$30m to US\$50m and relaxed requirements for compulsory reserves in UAH.

**ICU view: Despite the significant rate cut, the NBU remains cautious. According to NBU's previous forecast, the year-end real interest rate was 7.7% vs the current 8.0% (based on November inflation). We expect a faster decrease of real rates in 1H20.**

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