

Weekly Insight

Ukraine to tap the EUR debt market

Key messages of the today's comments

TUESDAY, 11 JUNE 2019

Domestic liquidity and bonds market

Ukraine to tap the EUR debt market

Ukraine began a roadshow yesterday for the placement of a seven-year euro-denominated Eurobond. We expect the rate for this issue at about 6.5%. Pricing will come at the end of this week after investors' meetings.

Foreign investment in local-currency debt increases

Last week, foreign investors purchased an additional UAH1.6bn of local-currency government bills, increasing portfolios outstanding to UAH43.9bn. This week, we expect a further increase in investment portfolios to slightly below UAH50bn.

NBU supported liquidity

New investments in local-currency debt prompted the NBU to buy FX on the market and to support liquidity, which declined significantly. This week, liquidity will continue to fluctuate within the range of UAH95-100bn.

Foreign exchange market

Hryvnia appreciated

Last week, the hryvnia started at the historical minimum for June – 27.15/US\$, but became stronger by the end of the week to below UAH27/US\$. This week, we anticipate further appreciation, which will be restrained by the NBU.

Economics

NBU kept rate unchanged

The Regulator decided to abstain from further cuts, and kept the key rate at 17.5%. The NBU is likely to abstain from further cuts during the next meeting in July.

Banks' reserves market (10 June 2019)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	17.50	+0bp	+50bp
ON rate (%)	16.31	+28bp	+51bp
ON \$ swap (%)	14.52	+10bp	-114bp
Reserves (UAHm) ²	53,790	+17.30	+37.78
DepCerts (UAHm) ³	47,053	-9.10	+0.00

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) (10 June 2019)

	Last	Weekly chg (%)	YoY chg (%)
NBU	337,088	+0.00	-3.78
Banks	360,865	-0.99	+2.04
Residents	25,761	-1.32	+7.54
Individuals	9,523	-0.16	+221.98
Non-res ⁴	43,875	+5.66	+329.97
Total	777,113	-0.21	+4.94

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

FX market indicators (10 June 2019)

	Last	Weekly chg (%)	YTD chg (%)
USD/UAH	26.3150	-3.08	+0.67
EUR/USD	1.1312	+0.53	-3.88
DX ²	96.761	-0.32	+3.45
UAH TWI ³	123.853	+2.78	+4.40

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

Gov't bond quotes¹ (11 June 2019)

Maturity	Bid	Ask
6m	19.00	18.00
12m	19.25	18.00
2y	19.25	18.00
3y	19.00	17.00
12m (\$)	7.50	5.50
2y (\$)	7.50	5.75

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

Domestic liquidity and bonds market

Ukraine to tap the EUR debt market

Ukraine began a roadshow yesterday for the placement of a seven-year euro-denominated Eurobond. We expect the rate for this issue at about 6.5%. Pricing will come at the end of this week after investors' meetings.

The government has awarded BNP Paribas and Goldman Sachs the mandate for joint lead management and joint bookrunners. We expect the pricing will be set close to 6.5%, given the current 8% yield of USD-denominated UKRAIN'26, 200bp spread between USD and EUR rates, and a 50bps premium for liquidity and a new issue.

ICU view: This EUR-denominated placement looks like a good idea, as it will widen the investor base. Currently, EUR accounts for just 9.2% of the total debt portfolio of Ukraine, versus 42.4% of USD-denominated debt.

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Foreign investment in local-currency debt increases

Last week, foreign investors purchased an additional UAH1.6bn of local-currency government bills, increasing portfolios outstanding to UAH43.9bn. This week, we expect a further increase in investment portfolios to slightly below UAH50bn.

Foreign investors made new investments in UAH-denominated bills, and not only at primary auctions. The hryvnia weakening to around UAH27/US\$ added some additional attractiveness to investments over what was possible in May. However, the amount of new bills purchased was still restrained. Market participants are focusing on negative news and political instability.

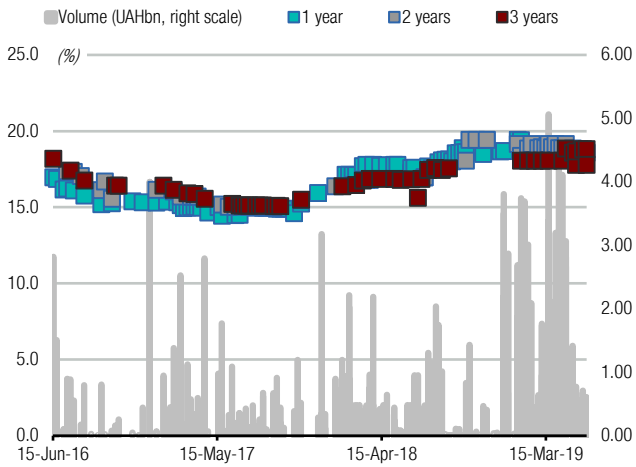
Debt repayments of close to UAH6bn are scheduled this week, most of which were borrowed in February and March. During these auctions, foreign investors were not active, and did not increase their portfolios significantly, although they may have bought these bills later in the secondary market. We do not exclude the possibility that part of the repayments will be made to foreigners.

ICU view: Although foreign investors may receive repayments this week, they may still increase in their portfolios because of the link to Clearstream, making new investments larger than repayments. We expect the rate of increase in portfolios will be similar to last week, with the ending balance remaining slightly below UAH50bn.

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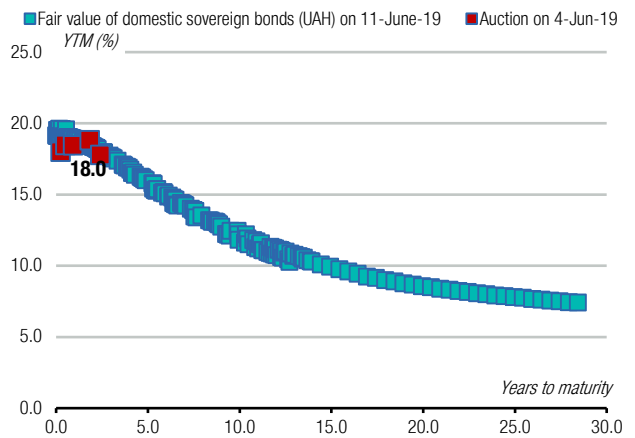
Chart 1. Local-currency bonds

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.

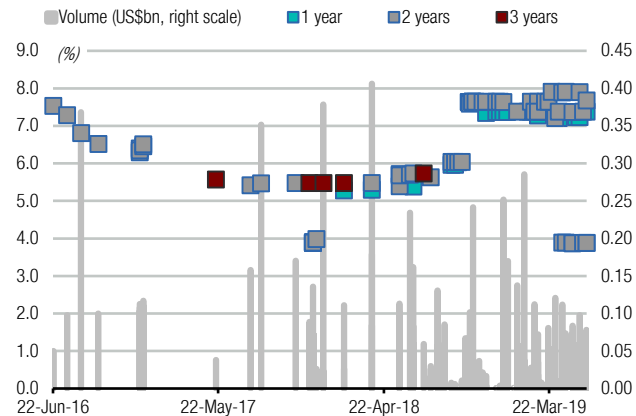
Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions



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

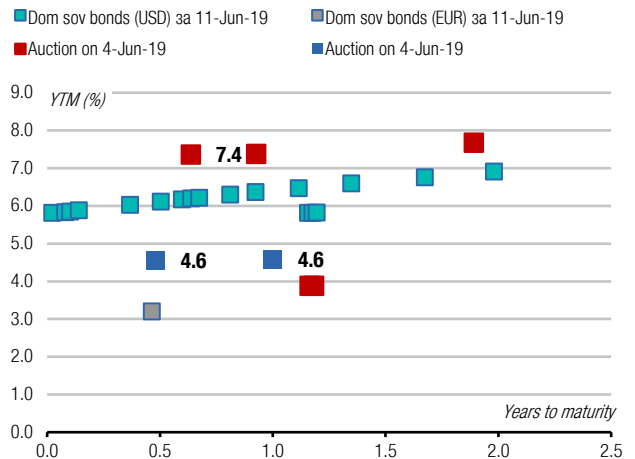
Chart 2. FX-denominated bonds

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.

NBU supported liquidity

New investments in local-currency debt prompted the NBU to buy FX on the market and to support liquidity, which declined significantly. This week, liquidity will continue to fluctuate within the range of UAH95-100bn.

Traditionally, at the beginning of the month, banks increased exchange of reserves into cash, reducing the total amount of liquidity by more than 5.4 billion UAH.

The most important support for liquidity was received from the NBU, which returned to the market with the purchase of FX, reducing the impact of extra FX supply from foreign investors. In total, US\$102m were purchased last week, injecting UAH2.8bn in banking-sector liquidity.

ICU view: Taking all transactions in account, last week, liquidity was around UAH97bn. This week, it is unlikely to move significantly, remaining in the range of UAH95-100bn with a possible deviation on some days.

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

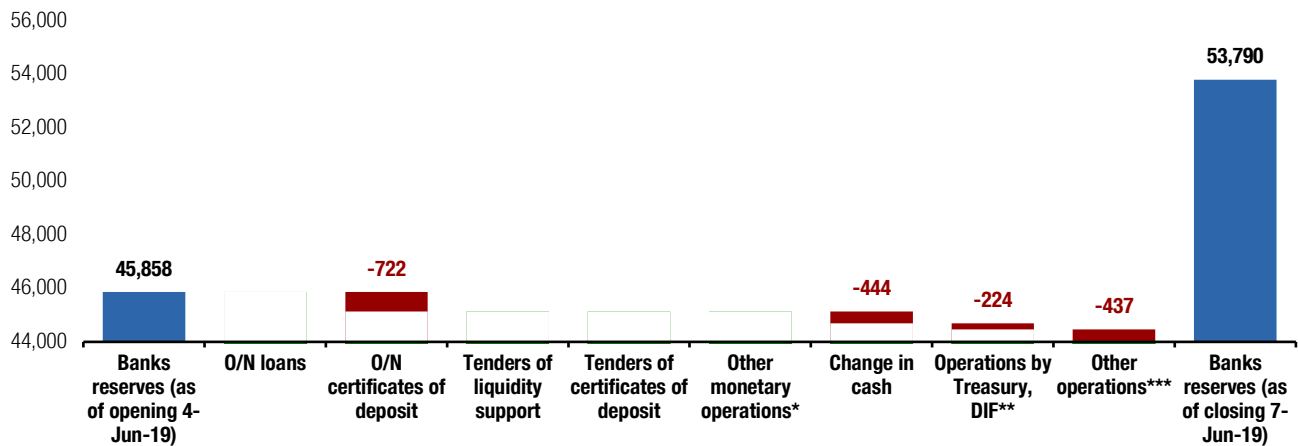
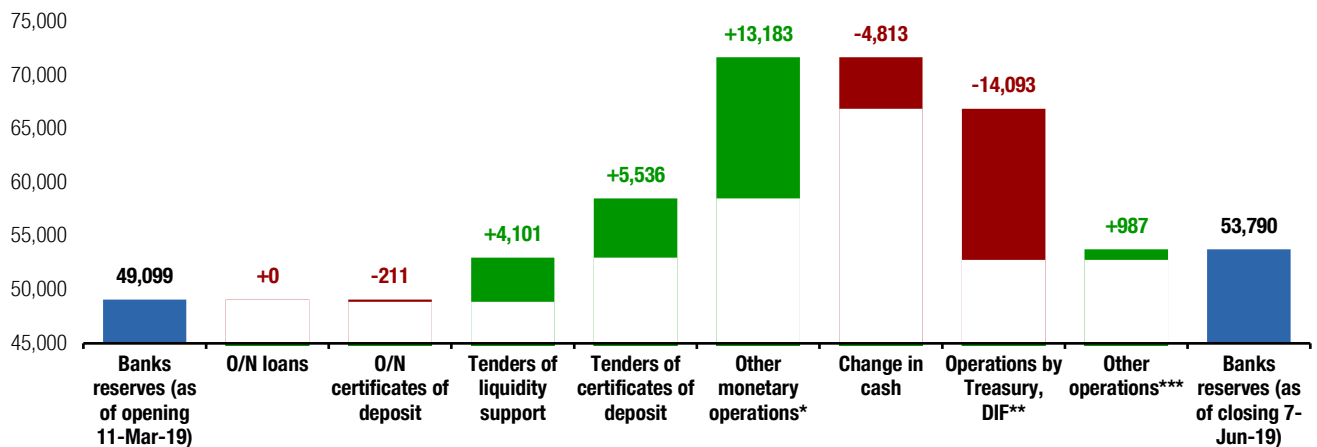


Chart 4. Banks reserves usages over last 90-day period (UAHm)



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

* 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 appreciated

Last week, the hryvnia started at the historical minimum for June – 27.15/US\$, but became stronger by the end of the week to below UAH27/US\$. This week, we anticipate further appreciation, which will be restrained by the NBU.

The week started with demand for USD significantly exceeding supply. Reacting to negative news, international companies actively purchased FX to pay dividends abroad, while USD supply was low. This caused the hryvnia to weaken to UAH27.15/US\$ on Tuesday. This could be an additional reason for the increase in activity of foreign investments in UAH-denominated debt. These new investments reversed movements of the UAH exchange rate and forced the NBU to purchase FX on the market in large amounts. From Wednesday to Friday, as much as US\$102m was purchased, but it restrained appreciation of hryvnia, which appreciated last Friday to UAH26.54/US\$ or by 1.2% during the week.

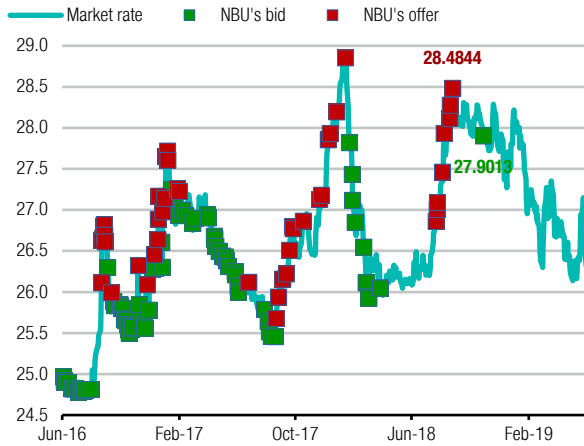
ICU view: This week, we expect stability of the exchange rate with possible slight appreciation. The market will depend on activity of foreign investors making new investments in government bills, and on their decision about possible debt

repayments received — whether to convert them into FX or to invest them into new bonds.

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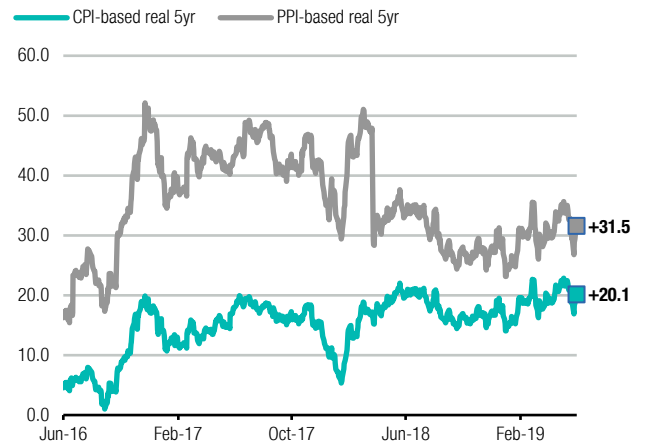
Chart 5. FX market indicators, 3-year history

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 misalignment¹ from fundamental level² (%)



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

Economics

NBU kept rate unchanged

The Regulator decided to abstain from further cuts, and kept the key rate at 17.5%. The NBU is likely to abstain from further cuts during the next meeting in July.

After commencing the new cycle of interest rate cuts immediately after the presidential elections in April, the regulator has hesitated given the uncertainties that have arisen since then. A dubious court ruling challenging the nationalization of PrivatBank, and speculations about the artificial default increased concerns over what the economic policy of new administration will be. The IMF programme is de facto on hold until the new parliamentary election and new government is in place.

ICU view: There is a good chance the NBU will abstain from further cuts during the next meeting in July, as most of the risks are unlikely to be resolved by then.

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