

Weekly Insight

Inflation remains low at end-2023

Key messages of the today's comments

MONDAY, 15 JANUARY 2024

Ukrainian bond market

Investors focus on FX-denominated bills

Last week, investors' interest was primarily in FX-denominated instruments.

Ukrainian Eurobond prices situationally up

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Foreign exchange market

Six-week hryvnia weakening streak ends

Last Tuesday, the official hryvnia exchange rate reached a new all-time low, but by the end of last week, it strengthened again as imbalances in the interbank FX market narrowed.

Economics

Inflation remains low at end-2023

Ukraine's annual inflation stayed at 5.1% YoY at end-2023, same as November, reflecting a mix of favourable preconditions that will keep CPI relatively low at least until next summer.

Banks' reserves market (12 January 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU rate (%) ¹	15.00	+0bp	-1,000bp
ON rate (%)	15.00	+0bp	-800bp
Reserves (UAHm) ²	227,544	+22.9	+73.8
CDs (UAHm) ³	565,947	-11.4	+50.4

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 gov't bond holders (UAHm) (12 January 2024)

	Last	Weekly chg (%)	YoY chg (%)
NBU	689,990	+0.0	-2.1
Banks	658,572	+0.5	+32.0
Residents	142,422	+0.8	+32.0
Individuals	55,002	+2.5	+78.7
Foreigners	43,696	+0.0	-24.4
Total	1,591,714	+0.4	+13.5

Source: NBU, ICU.

FX market indicators (12 January 2024)

	Last	Weekly chg (%)	YoY chg (%)
USD/UAH	37.9090	-0.5	+2.9
EUR/USD	1.0951	+0.1	+0.9
DXY	102.404	+0.0	+0.2

Source: Bloomberg, ICU.

Market gov't bond quotes (15 January 2024)

Maturity	Bid (%)	Ask(%)
6 months	17.50	15.00
12 months	18.00	16.50
2 years	19.50	18.00
3 years	20.00	18.75
12 months (\$)	5.00	4.50
2 years (\$)	N/A	N/A

Source: ICU.

Ukrainian bond market

Investors focus on FX-denominated bills

Last week, investors' interest was primarily in FX-denominated instruments.

At last week's primary auction, the Ministry of Finance raised the equivalent of almost UAH16.8bn (US\$439m), including UAH13.8bn (US\$361m) or 82% from FX-denominated bills. The demand for UAH bonds was relatively small, and only UAH2.9bn (US\$231m) of proceeds was raised in that form. At the same time, the demand for USD-denominated bills exceeded the supply cap, so the MoF rejected some bids, and some bids were satisfied only partially within the cap. EUR-denominated bills were offered without limits and with a put option. MinFin thus raised US\$153m and EUR190m. The MoF sold all bonds without changes in the cut-off rates. See details in the [auction review](#).

In the secondary market, the total volume of trades was the equivalent of UAH11.2bn (US\$295m), including UAH4.5bn (US\$122m) in FX-denominated bond. New EUR-denominated bills were not traded. Among USD-denominated bonds, the most traded was the paper maturing at the end of next month (52% of all FX-denominated bills trades) and new paper sold at last week's auction (22% of trades). In the UAH segment, the most traded was "reserve" paper due in February 2026 (43% of all trades in UAH bonds).

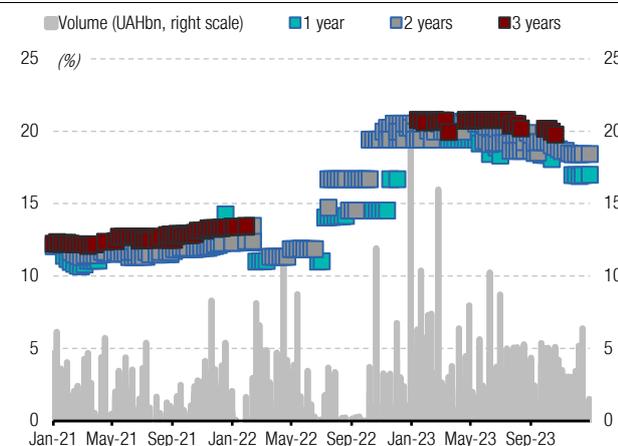
Of all investors, individuals increased their portfolios most significantly, by 2.2%, mainly due to the purchase of FX-denominated bills.

ICU view: Investors preferred USD-denominated bills last week, which probably reflects their desire to hedge FX risks against the backdrop of hryvnia weakening in December and early January. In addition, significant demand results from the MoF's limited supply of FX-denominated bonds in recent months. Due to delay in international financial assistance, the Ministry will likely seek to increase domestic borrowings in the coming weeks.

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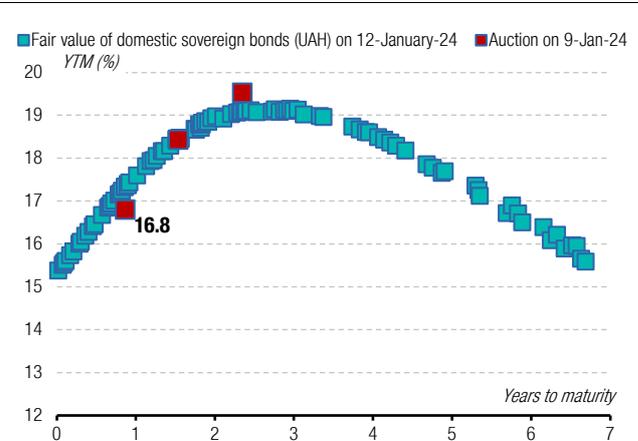
Chart 1. Local-currency bonds

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



Source: MFU, ICU.

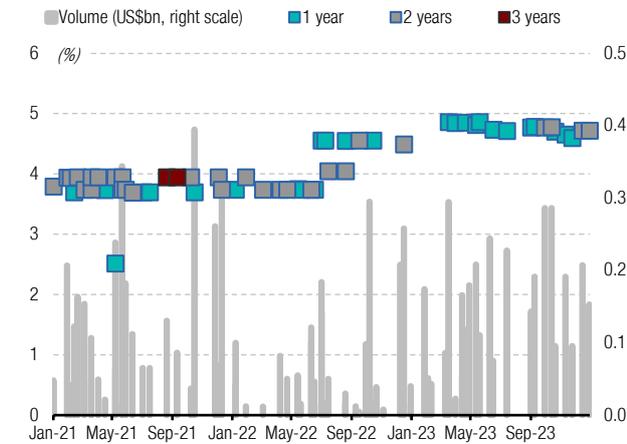
YTM's of domestic government bonds as calculated by NBU versus placements via primary market auctions



Source: NBU, MFU, ICU.

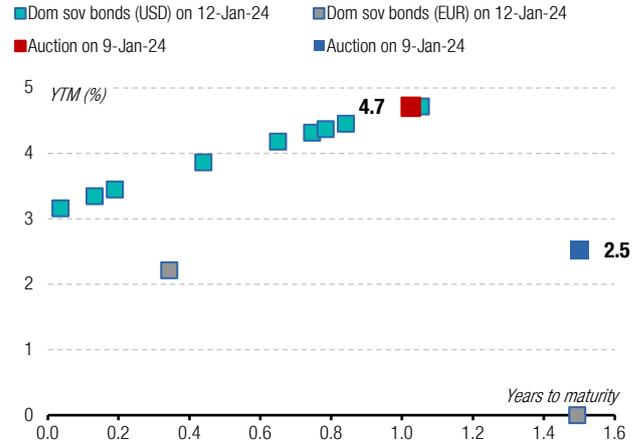
Chart 2. FX-denominated bonds

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.

Ukrainian Eurobond prices situationally up

Ukrainian sovereign Eurobonds prices rose sharply at the end of last week, approaching levels last seen at the beginning of November.

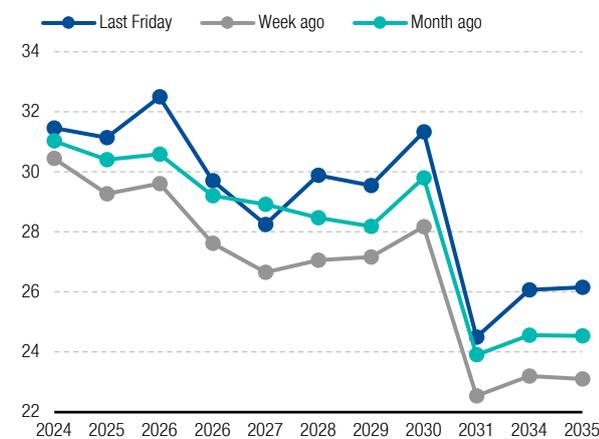
Over the past week, Ukrainian Eurobond prices rose by an average of 9%, shifting to the range of 24–32 cents per dollar, with the price range for Eurobonds with different maturities narrowing to 13.5%. The VRIs price rose by about 8% to 48 cents per dollar of notional value, more than on the eve of a full-scale russian invasion in 2022. The EMBI index increased by 1.1% during last week.

ICU view: *The US Congress resumed its work last week, and it initially looked like the likelihood of passing the US budget in January was high and also the Congress was one step closer to stamping the aid package for Ukraine. Therefore, interest from some optimistic investors could have caused a situational rally last Thursday. However, price gains may reverse, as Congress is now likely to adopt the new stopgap spending bill for another month, and the discussions of US immigration policy saw little progress. The uncertainty about the prospects for the approval of the aid package for Ukraine will remain decisive for Ukrainian Eurobonds in the coming weeks.*

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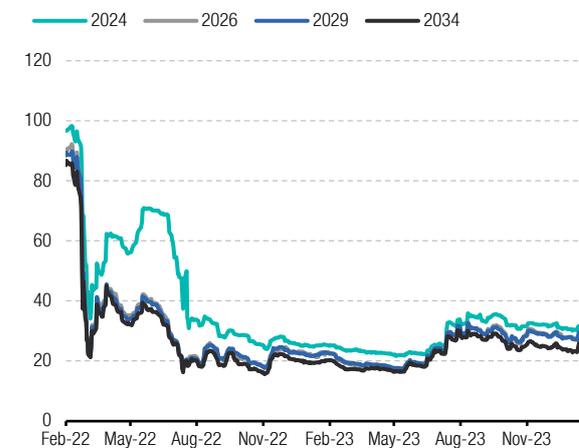
Chart 3. Ukrainian Eurobonds prices

Prices of USD-denominated Eurobonds as of last Friday, two weeks and a month ago



Source: Bloomberg, ICU.

Historical data since February, 2022



Source: Bloomberg, ICU.

Foreign exchange market

Six-week hryvnia weakening streak ends

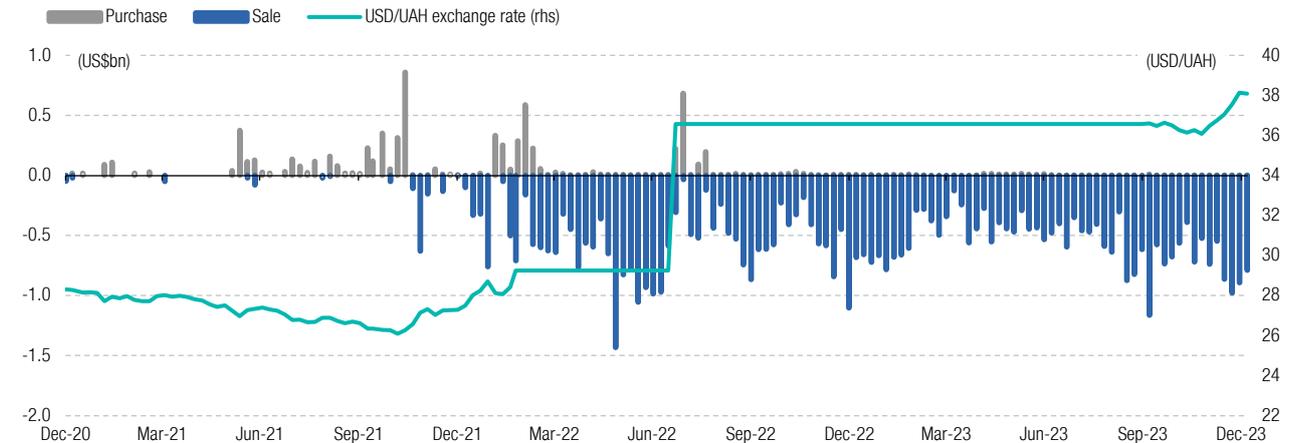
Last Tuesday, the official hryvnia exchange rate reached a new all-time low, but by the end of last week, it strengthened again as imbalances in the interbank FX market narrowed.

Bank clients (legal entities) increased the sale of hard currency by 59% compared with the first week of the year, while the volume of hard currency purchases rose by only 13% (during four business days). In general, last week, the difference between the purchase and sale of hard currency was below US\$85m on all days, while at the end of December it occasionally exceeded US\$200m per day. Lower imbalances allowed the NBU to reduce the volume of interventions by 15% to US\$674m, the smallest volume since the beginning of last December. So, today's official exchange rate is UAH37.84/US\$, implying a 1% appreciation after weakening to a historical low of UAH38.22/US\$ last Tuesday.

In the retail market, FX trading rose by approximately 30% in four business days compared with the same period of the previous week. On average, the hryvnia cash rate in systemically important banks strengthened by 0.5% to UAH38.0–38.8/US\$ over the week.

ICU view: The end of the holiday season increased business activity, which narrowed imbalances in the FX market. This favoured a moderate strengthening in the hryvnia exchange rate. The NBU will maintain an active presence in the market, allowing fluctuations in both directions and, likely, for now, supporting a gradual strengthening of the hryvnia exchange rate. The retail market continues to respond to changes in the interbank market, moving exchange rate in tandem.

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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

Inflation remains low at end-2023

Ukraine's annual inflation stayed at 5.1% YoY at end-2023, same as November, reflecting a mix of favourable preconditions that will keep CPI relatively low at least until next summer.

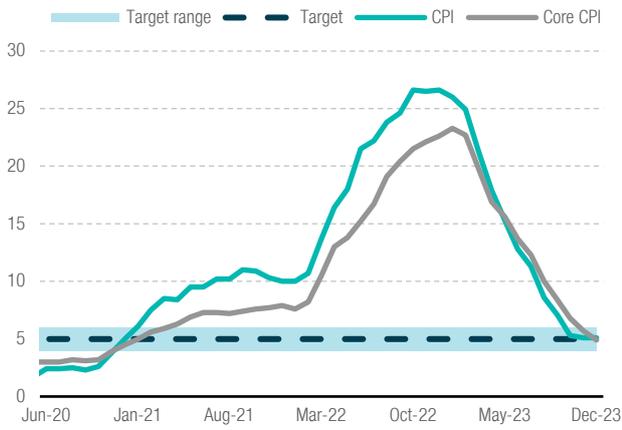
Consumer prices decelerated across the board in 2023, while prices for clothes and footwear even fell in YoY terms. The prices for the largest CPI components—food and transportation—increased by 4% or less over 2023.

ICU view: *The slowdown in consumer inflation came on the back of abundant agricultural harvest, stable exchange rate, and only moderate revision of administratively regulated utility tariffs. Consumer demand had been strengthening over 2023, but had only a moderate negative impact on the general price level. We expect annual CPI will remain below 7% till summer, but it is likely to accelerate further in 2H24 on normalization of the agriculture harvest and gradual weakening of hryvnia. We project end-2024 CPI at 10.1%.*

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

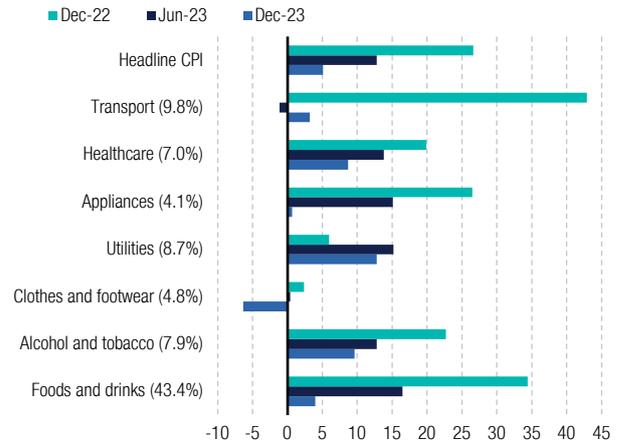
Inflation falls to 5.1% at end-2023



Source: Ukrstat, NBU, ICU.

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

Prices for all consumer-basket components slowed substantially



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

Source: Ukrstat, ICU.

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