



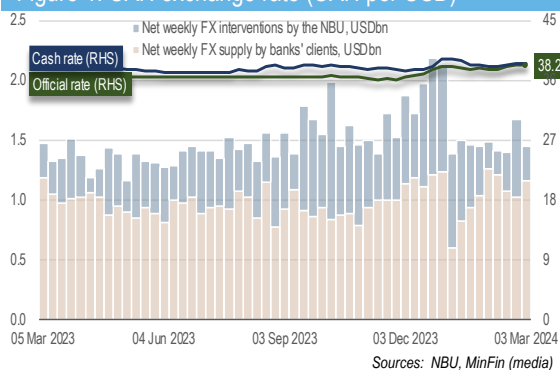
ECONOMICS | INTEREST RATES | FX MARKETS

6 March 2024

UKRAINIAN CAPITAL MARKETS REVIEW

	Rating	Outlook	Last update	This week in focus: Unblocked sea paves the way for FX policy easing
Fitch	CC	-	08.12.2023	Ukraine's achievements on the Black Sea have boosted sea grain exports above the "grain deal" volumes. And now they feed into overseas trade in other commodities. Although the country will likely to remain heavily burdened with import for quite some time, a sustained recovery in export may pave the way for resumed progress in the FX easing strategy latter in the year.
S&P	CCC	NEGATIVE	08.09.2023	
Moody's	Ca	NEGATIVE	10.02.2023	
R&I	CCC	NEGATIVE	23.01.2024	

Figure 1. UAH exchange rate (UAH per USD)



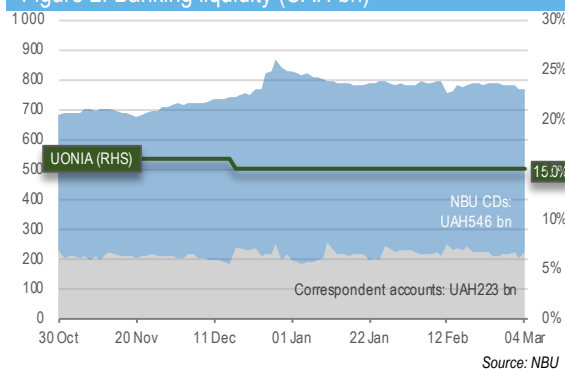
FX and interest rates: Delays in external support inflow add to pressure on UAH

Hryvnia struggles to regain ground against the US dollar, despite marginal rate depreciation. The pair ended last month at the mark of 38.05, registering a 1.2% decline over the period.

At one point, the NBU scaled back its market presence to a 9-months minimum, thanks to the sea corridor, facilitating the recovery of agricultural commodity exports to pre-war levels.

However, **the absence of timely US support is increasingly straining the country's financial sustainability**, a challenge that extends to the situation on the battlefield too. Ukraine has received approximately USD1.2bn in external assistance since the beginning of the year, falling short of the needed of USD3bn per month.

Figure 2. Banking liquidity (UAH bn)

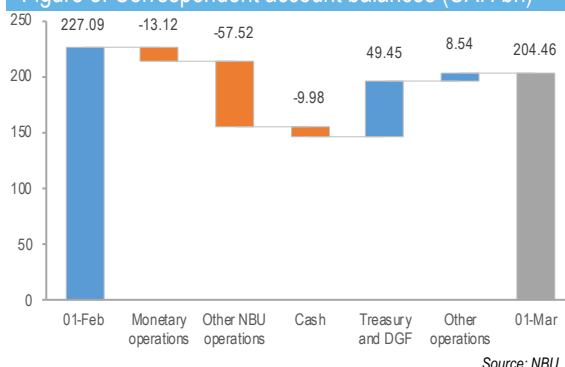


Renewed tension on the country's western borders add to pressure on hryvnia too. Although Ukraine's exports to and through Poland dropped to a minimum since border topic emerged a year ago, the unease remains an important psychological driver, fuelling demand on the cash market.

Despite these challenges, **the NBU consistently reaffirms its commitment of being a key player** in the market, effectively smoothing the pair trend.

We expect market pressure moderate after Ukraine receives the first tranche worth USD4.5bn under the EU-led EUR50bn program this month. But this will barely give a pretext for FX policy easing in 1H24, as long as prospects for US support remain unclear.

Figure 3. Correspondent account balances (UAH bn)



Banking liquidity stabilized below UAH800bn in February, reflecting moderated spending by the government.

Since beginning of the year, net injection by the State treasury amounted to UAH83bn, half of the amount spent a year ago.

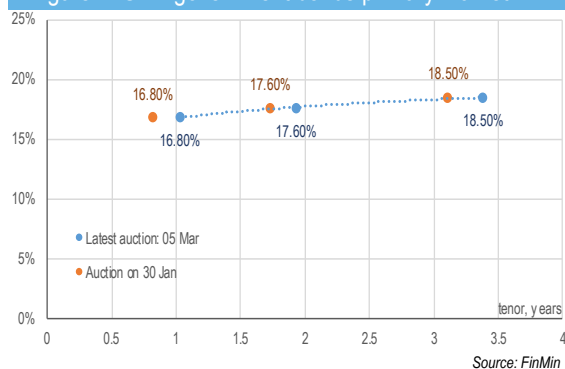
Demand for cash reverted to its usual monthly pattern.

As of the end of February balance of correspondent accounts with the NBU was UAH204.5bn, position in CDs was UAH566.9bn.



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Figure 4. UAH government bonds primary market



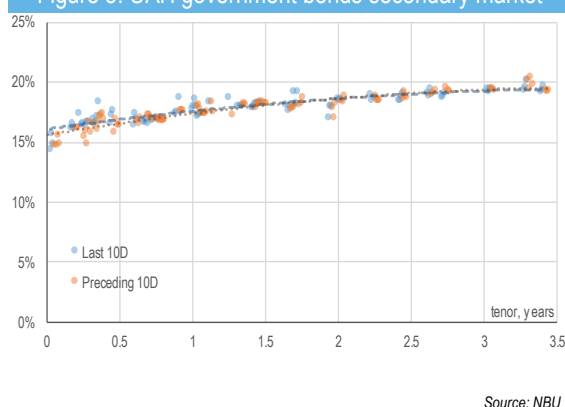
Government bond market

FinMin is closing the gap with new debt placement from the state budget projections. Last month the ministry raised over UAH70bn in hryvnia equivalent, significantly reducing the monthly lag from UAH11.6bn to UAH3.7bn compared to the previous month.

In February FinMin maintained its regular offering of securities, featuring 1-year, 2-year, and 3-year bonds. The yield curve held unchanged, with cut-off rates set at 16.8%, 17.6%, and 18.5%, respectively.

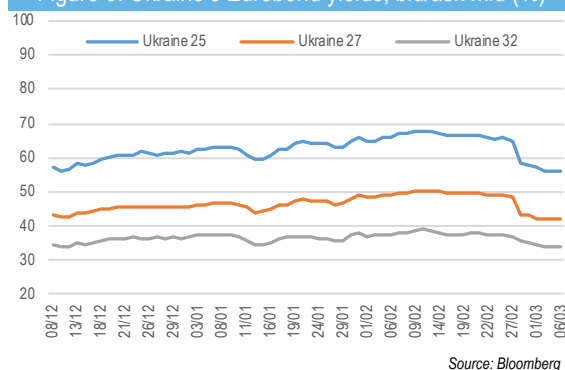
While most of demand was concentrated in 1-year and 2-year securities, there was notable interest in 3-year bonds, particularly sparked by positive inflation statistics for January, fueling speculation over a potential key rate cut.

Figure 5. UAH government bonds secondary market



But the Ministry is still lagging behind the state budget projections. The market remains worried about Ukraine's ability to sustain itself without US support. Recent news about Ukraine's retreat from Avdiivka, partly attributed to delayed US support, coupled with uncertainty around approval timelines for the package, limits the FinMin's capacity not only to lower cut-off rates but also to garner sufficient interest in public debt.

Figure 6. Ukraine's Eurobond yields, bid/ask mid (%)



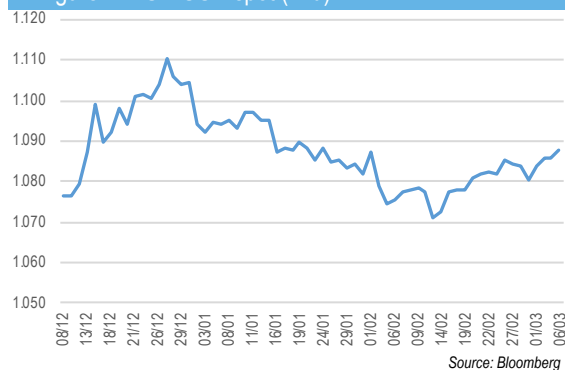
EUR/USD recovers from drop in early-February

The EUR/USD pair embarked on a recovery path in February, overcoming initial setbacks triggered by a robust US inflation report that tempered expectations of Federal Reserve interest rate cuts.

Headline inflation for January came at 3.1% y/y, lower than December's data but above the 2.9% expected. The higher-than-expected US Inflation has shifted market sentiment toward no interest rate adjustment by the Fed in the upcoming March meeting.

Despite facing headwinds, the euro found support from positive statistics, released in the second half of the month. Better-than-expected Economic Sentiment indices in the Eurozone and Germany, were followed by encouraging stats on the EU's current account surplus and inflation.

Figure 7. EUR USD spot (mid)



The EUR/USD pair now aims to consolidate above the 1.085 mark, driven by evolving expectations of a Fed rate cut and upcoming key events, including the Fed's congressional testimony on Wednesday and Thursday (6-7 March) and the ECB monetary policy decision on Thursday (7 March).

Benchmark 10-year Treasury yields experienced a rebound above 4% in February, peaking at 4.327%. The yield now is retreating towards the 4.1% level as investors are looking forward for the Fed's guidance.



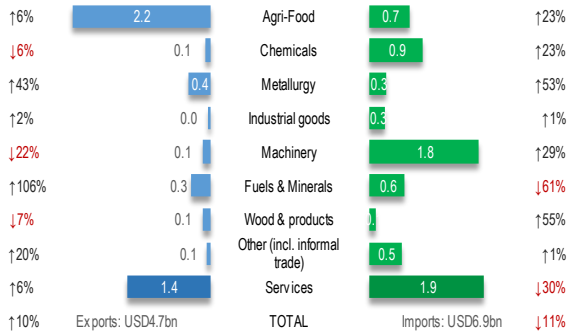
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Figure 8. Breakdown of trade balance in January 2024

Unblocked sea paves the way for FX policy easing

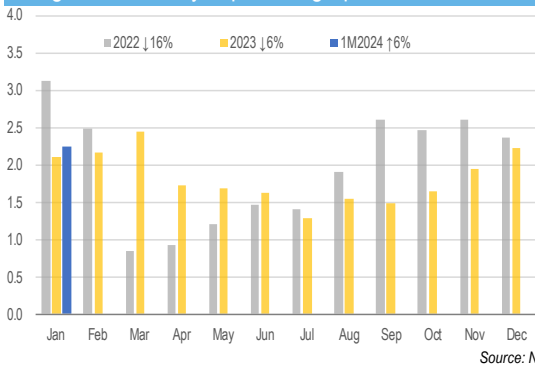


Source: NBU

Ukraine's achievements on the Black Sea have boosted sea grain exports above the "grain deal" volumes. And now they feed into overseas trade in other commodities. Ukraine's trade gap hit record high last year. Although the country will likely to remain heavily burdened with import for quite some time, a sustained recovery in export may pave the way for resumed progress in the FX easing strategy.

The cargo turnover of the ports of Odesa reached 8 million tonnes in February, the highest since Russia's full-scale invasion in February 2022, with exports through the Black Sea ports gradually approaching pre-war levels, according to Deputy Prime Minister Oleksandr Kubrakov.

Figure 9. Monthly export of agri-products, USDbn

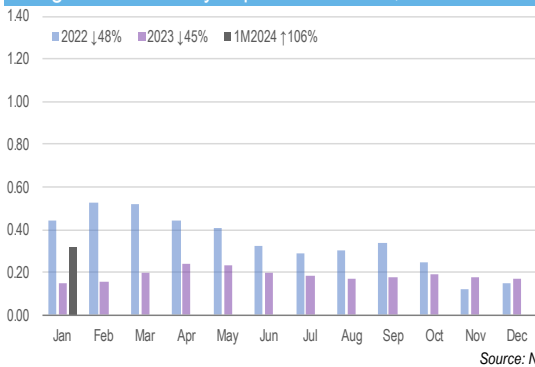


Source: NBU

The corridor has been gradually developed since August 2023 - several weeks after Moscow refused to extend the "grain deal" - by destroying or pushing Russia's navy away from Ukraine's coasts.

The export of agricultural products via the unblocked corridor has already exceeded monthly volumes during the "grain deal". And now a recovery emerged in export of iron ore and metals too. In January Ukraine shipped abroad minerals – an item where iron ore exports is accounted in – for some USD316mn, almost twice as high as monthly average in 2023. Export of metals came in at USD360mn, up by 43% compared to January 2023, and 11% above monthly average in 2023. The correspondent figures are still far below the pre-war levels. If sustain throughout the year, however, they may improve Ukraine's trade balance by some USD6bn of export revenue.

Figure 10. Monthly export of minerals, USDbn



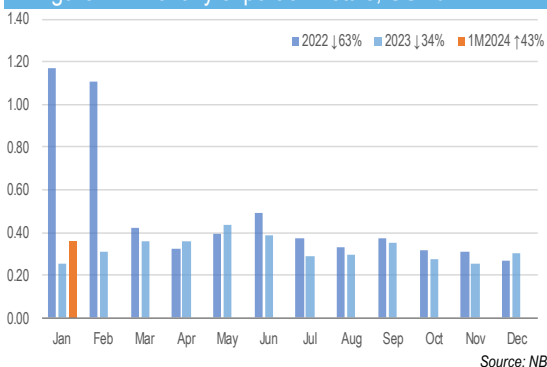
Source: NBU

The country's trade gap reached a historical high of USD37.8bn last year, with visible trade deficit accounting for USD20bn. Imports neared pre-war levels in 2023, while exports remained depressed due to persistent logistic issues, as well as seizure, damage and/or destruction of production facilities.

A substantial burden to the trade balance also remains import of services. Because of mass migration of people abroad, fleeing from Russian invasion, the correspondent import nearly doubled in 2022, exceeding USD27bn. As more people are getting employed abroad, import of services contracted by 7.1% to USD 25.2bn in 2023, and may drop by another 10% this year.

But negative scenarios are also possible. Prolonged delays in foreign support inflow may further deteriorate the trade balance.

Figure 11. Monthly export of metals, USDbn



Source: NBU

In total, the evolving trade dynamics, propelled by Black Sea breakthroughs, offer a glimmer of hope for Ukraine's trade deficit to contract by at least a third this year. Although the trade gap is likely to persist for quite some time, the foregoing improvement may pave the way for FX easing initiatives in the latter part of the year.



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Key Macroeconomic Indicators

	2017	2018	2019	2020	2021	2022	2023	2024E
Real sector								
Real GDP (%YoY)	2.4	3.5	3.2	-3.8	3.4	-28.8	4.5*	3.0
Industrial production (%YoY)	1.1	3.0	-0.5	-4.5	1.9	-36.9	NA	NA
Retail sales (%YoY)	6.5	6.2	10.3	8.4	10.7	-21.4	NA	NA
Unemployment rate end of year (ILO, working age)	9.5	8.8	8.2	9.5	9.8	NA	NA	NA
Nominal GDP (UAH bn)	2 981	3 560	3 977	4 222	5 451	5 191	NA	NA
Nominal GDP (USD bn)	112	131	155	157	200	161	NA	NA
Prices								
CPI (average %YoY)	14.4	10.9	7.9	2.7	9.4	20.2	12.9	8.9
CPI (end of year %YoY)	13.7	9.8	4.1	5.0	10.0	26.6	5.1	10.0
Real average wage growth (%YoY)	19.1	12.5	9.8	7.4	11.9	NA	NA	NA
Fiscal balance (% of GDP)								
State budget deficit (without Naftogaz)	1.6	2.4	1.8	5.2	3.6	17.6	NA	NA
Total public debt (% of GDP)	71.8	61.0	51.6	60.8	48.9	78.4	NA	NA
External balance								
Exports of goods and services (USD bn)	53.9	59.2	63.6	60.7	81.5	57.0	50.9	NA
Imports of goods and services (USD bn)	62.7	70.6	76.1	63.1	84.2	82.7	88.7	NA
Current account balance (USD bn)	-3.5	-6.4	-4.1	5.3	-3.9	7.9	-9.8	NA
Current account balance (% of GDP)	-3.1	-4.9	-2.7	3.4	-1.0	5.2	NA	NA
Net FDI (USD bn)	3.7	4.5	5.2	-0.1	7.5	0.3	4.2	NA
Foreign exchange reserves (end of year)	18.8	20.8	25.3	29.1	30.9	28.5	40.5	30.0
Imports coverage (months of imports of goods)	3.6	3.5	3.9	4.8	4.1	3.7	5.4	3.8
Interest and exchange rates								
NBU discount rate (% end of year)	14.5	18.0	13.5	6.0	9.0	25.0	15.0	15.0
Exchange rate (USD/UAH) end of year	28.1	27.7	23.7	28.3	27.3	36.6	38.0	44.0
Exchange rate (EUR/UAH) end of year	33.5	31.7	26.4	34.7	30.9	39.0	42.0	50.6

*estimates, no official data yet available

NA – data is not available because of continuing military operations



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FOUR WEEKS AHEAD

Mon	Tue	Wed	Thu	Fri	Sat	Sun
04.03.2024	05.03.2024	06.03.2024	07.03.2024	08.03.2024	09.03.2024	10.03.2024
		LGB % UAH 24.0mn	NBU: FX Reserves (deadline - 7th day) ECB: MPC			
11.03.2024	12.03.2024	13.03.2024	14.03.2024	15.03.2024	16.03.2024	17.03.2024
IMF SDR 187.5mn Ukrstat: GDP		IMF SDR 295.5mn LGB % UAH 72.1mn LGB % UAH 1 274.7mn LGB P UAH 15 933.4mn	NBU: MPC	IMF SDR 59.7mn		
18.03.2024	19.03.2024	20.03.2024	21.03.2024	22.03.2024	23.03.2024	24.03.2024
		Fed: FOMC	LGB P USD 262.4mn			
25.03.2024	26.03.2024	27.03.2024	28.03.2024	29.03.2024	30.03.2024	31.03.2024
NBU: Minutes				NBU: BoP		

MOST COMMON TERMS AND ABBREVIATIONS

GDP	Gross domestic product	DGF	Deposit Guarantee Fund
CPI	Consumer price index	Ukrstat	State Statistics Service of Ukraine
FDI	Foreign direct investment	NBU	National Bank of Ukraine
BoP	Balance of Payments	ECB	European Central Bank
CA	Current account	Fed	Federal Reserve System
FA	Financial account	FOMC	The Federal Open Market Committee
IIP	International investment position	MPC	Monetary policy committee meeting
VAT	Value-added tax	Minutes	Summary of MPC meeting
CD	Certificate of deposit	IMF	International Monetary Fund
FX	Foreign exchange, foreign currency	IFI	International financial institutions
UAH	Ukrainian hryvnia	LGB	Local government bonds
USD	U.S. dollar	FGB	Foreign government bonds (Eurobonds)
EUR	Euro	P	Principal due
SDR	Special drawing rights	%	Interests due
UONIA	Ukrainian OverNight Index Average	*	government bonds held by NBU or issued for recapitalization of state-owned banks
WA	Weighted average		
bp	basis point	m/m	in monthly terms; month-on-month change
pp	percentage point	TTM	trailing twelve months
y/y	in annual terms; year-on-year change	RHS	right-hand scale



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