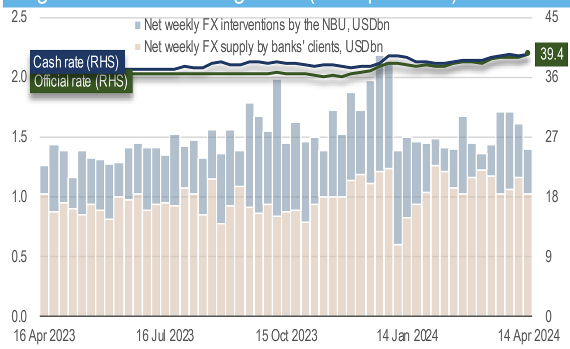
ECONOMICS | INTEREST RATES | FX MARKETS

18 April 2024

UKRAINIAN CAPITAL MARKETS REVIEW

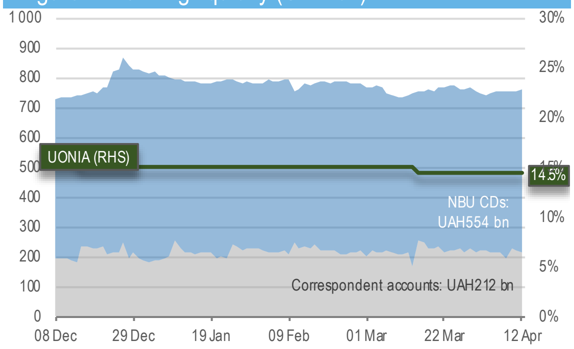
	Rating	Outlook	Last update
Fitch	CC	-	08.12.2023
S&P	CC	NEGATIVE	08.03.2024
Moody's	Ca	NEGATIVE	10.02.2023
R&I	CCC	NEGATIVE	23.01.2024

Figure 1. UAH exchange rate (UAH per USD)



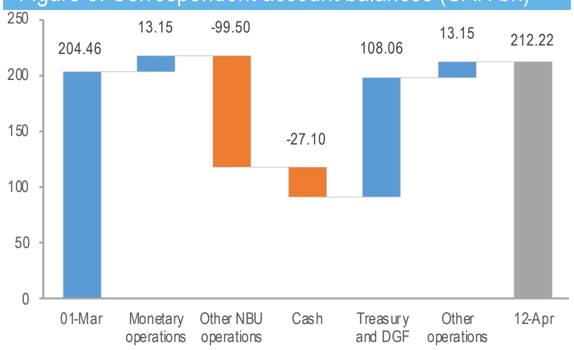
Sources: NBU, MinFin (media)

Figure 2. Banking liquidity (UAH bn)



Source: NBU

Figure 3. Correspondent account balances (UAH bn)



Source: NBU

This week in focus: Growth in a shadow of airstrikes

Ukraine's GDP growth is poised to moderate in 2024, reflecting lingering consequences of the protracted approval of the US aid package. And uncertainties surrounding the timing of the approval of the US support exacerbate concerns, dampening both business and consumer confidence.

FX and interest rates: UAH struggles to regain ground

The USDUAH rate broke the record high twice in April. On Tuesday (16 April), the interbank rate stabilized at the mark of 39.57. However, the UAH continues to struggle in regaining ground amidst unsettling news flow, coupled with the ongoing USD strengthening in global markets.

The trend emerged in the second half of March when weekly demand for FX soared to USD1.7bn, up 17% compared to the weekly average since the beginning of the year. Although the uptick followed shortly after the NBU's key rate cut, we see little evidence of the monetary decision serving as a catalyst. FX supply by bank clients remained unchanged, holding slightly above USD1bn per week. Additionally, the abrupt rise in the USDUAH rate disincentivized some market participants from purchasing FX at apparently unfavourable levels.

After some stabilization in the first decade of April, the rate resumed its upward march following the news of massive damage to Ukrainian civil and energy infrastructure caused by Russian missile strikes on 11 April. Simultaneously, USD strengthening on the global market added to the hryvnia weakening.

While we maintain our forecast of a 15%-hryvnia depreciation against the US dollar by the end of the year, **we see little reasons for the current rate upsurge to develop further**. We adhere to the view that most of the risks to the hryvnia are concentrated in 2H24. Worth pointing out, however, that the extent of central bank's interventions remains pivotal in shaping FX market dynamics.

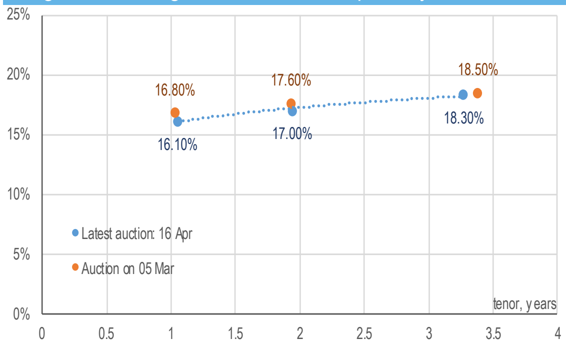
Banking liquidity has stabilized around the level of UAH750bn.

While state treasury transactions remain the major source of liquidity, the inflow continues to weaken, reflecting the delays in foreign support disbursements that Ukraine has faced this year. The corresponding funds are effectively absorbed through FX interventions conducted by the NBU.

Demand for paper money continues to rise, with total cash hryvnia withdrawals in March exceeding UAH19bn. The relatively stable demand for cash FX in banks suggests that the corresponding hryvnia does flow into the cash FX market. However, if sustained over several months, these withdrawals may signal excessive easing in the central bank's monetary policy.

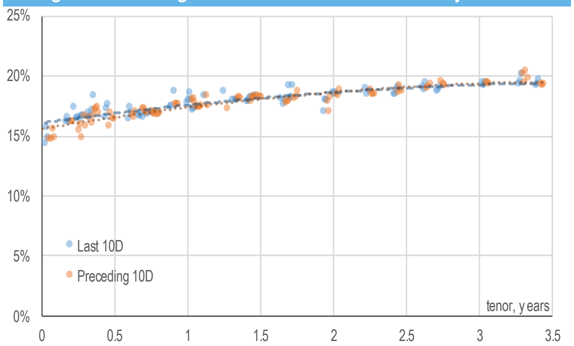
As of end of last week (12 April), balance of correspondent accounts amounted to UAH212bn, banks' position in NBU's CDs was UAH554bn.

Figure 4. UAH government bonds primary market



Source: FinMin

Figure 5. UAH government bonds secondary market



Source: NBU

Government bond market

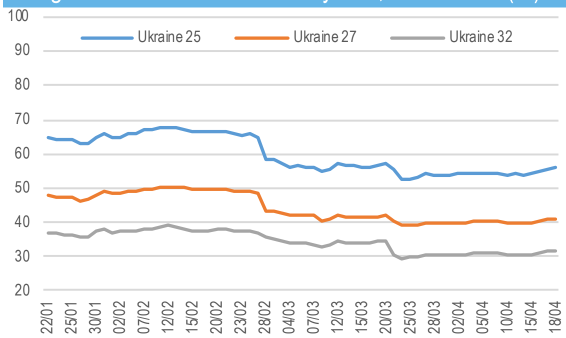
In March, the Ministry of Finance raised over UAH45bn (in UAH equivalent), marking a 9% increase compared to the preceding month.

The set of securities auctioned last month remained unchanged, featuring 1-year, 2-year, and 3-year bonds. Most of the demand was concentrated in the short end of the curve.

Initially, the resumed monetary easing, accompanied by signals from the central bank indicating further rate cuts ahead this year, bolstered demand for long-term UAH bonds. However, this interest waned as concerns arose due to escalating Russian attacks and missile strikes, raising fears of a potential new offensive campaign.

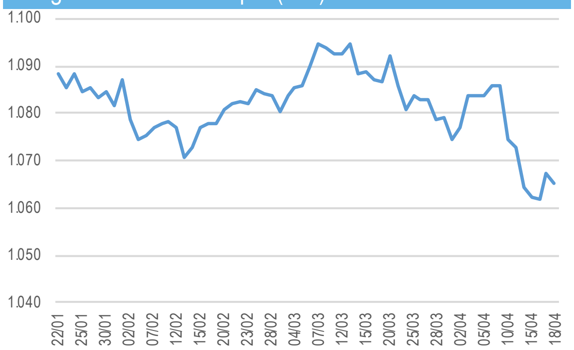
It is worth noting that the **Ministry of Finance continued to cap the volume of bonds on offer**, for both short and long maturities, attracting amounts needed for debt repayment and servicing only. Such an approach may indicate the ministry's confidence in the sustainability of demand for public debt, allowing for a wait-and-see approach for new rate cuts. Following the 50bp key rate cut in March, primary market yields for UAH bonds decreased by 70bp on the short end and 20bp on the long end, while secondary market yields lowered by about 40-45bp across the curve.

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



Source: Bloomberg

Figure 7. EUR USD spot (mid)



Source: Bloomberg

EURUSD revisits 1.0600 area on dovish ECB

The Euro has plunged to fresh five-month lows near the 1.0600 mark, as the Fed and ECB diverge further in their monetary policy stance.

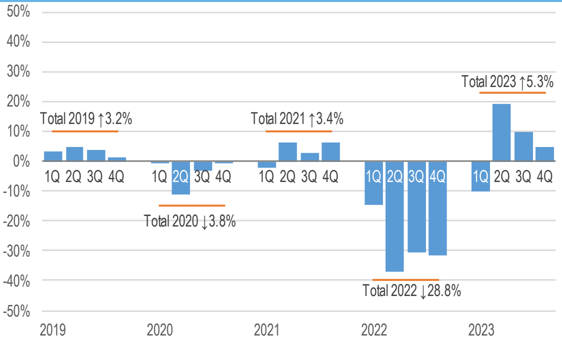
Despite indications from the Fed at the March monetary policy meeting of holding plans for multiple cuts this year, economic data suggests a different narrative. The resilient performance of the US economy and persistent inflationary pressures suggest that the Fed may refrain from swift interest rate cuts. The maintenance of comparatively higher interest rates is buoying the USD, attracting increased foreign capital inflows.

Fed Chairman's remarks on 16 April, emphasizing that recent economic data have clearly not given the Fed enough confidence for policy easing, have reinforced market expectations for fewer rate cuts than initially anticipated this year.

Meanwhile, although the ECB maintained rates at the 4% level following the monetary policy meeting on 11 April, some committee members leaned towards a rate cut. This, coupled with the dovish tone of the monetary statement, has heightened expectations of impending monetary easing from the ECB.

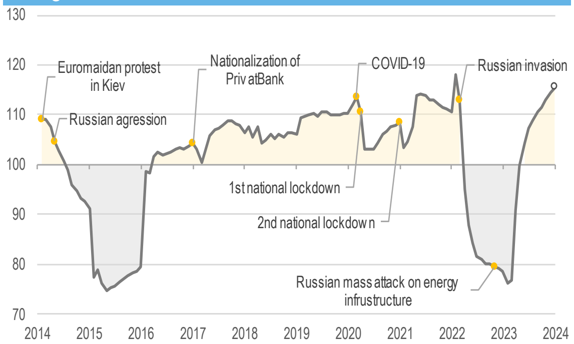
This week the euro has exhibited some correction after the substantial decline over the past week. But upside attempts appear remain constrained.

Figure 8. Annual GDP growth



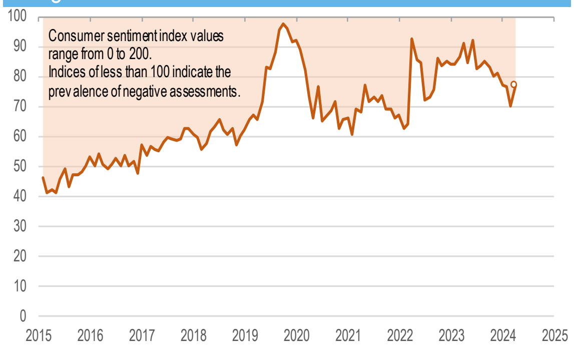
Source: Ukrstat

Figure 9. Retail trade turnover index



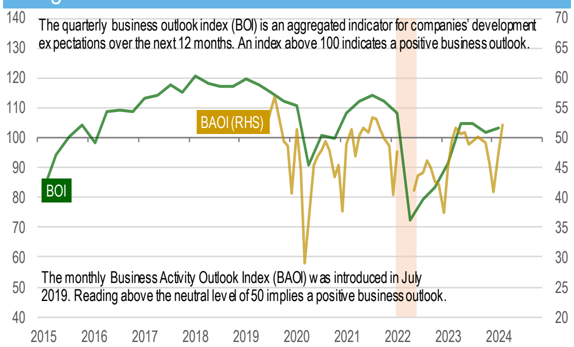
Source: Ukrstat

Figure 10. Consumer sentiment index



Source: Info Sapiens

Figure 11. Business sentiment indices



Source: NBU

Growth in a shadow of airstrikes

Ukraine's GDP growth is poised to moderate in 2024, reflecting lingering consequences of the protracted approval of the US aid package. While increased support from other countries has alleviated some strain on government finances, the depletion of munitions has become increasingly critical. This depletion has already manifested in accelerated Russian advances on the battlefield and intensified missile attacks, heavily damaging Ukraine's civil infrastructure. And uncertainties surrounding the timing of the approval of the US support exacerbate concerns, dampening both business and consumer confidence.

The annual GDP surged by 5.3% in 2023, primarily fueled by foreign financial aid injected into the economy through government expenditures. With military spending driving the surge, the government's share in nominal GDP exceeded 40%, twice as high as the five-year average preceding the Russian invasion.

The backbone of the economy, however, remains private consumption. Sustained consumer expenditures are also buoyed by foreign funds, cascading down to consumers through salaries.

Looking forward, **we anticipate real GDP growth to decelerate to 2% this year**, primarily due to delays in foreign support inflow Ukraine has encountered this year.

While the approval of the EUR50bn four-year financing program by the EU, featuring a EUR6bn upfront payment, and increased direct financial support from multiple countries have partially alleviated financial strain, **the US aid package, an particularly its military component, remains crucial**.

The depletion of munitions has already manifested in reaccelerated Russian progress on the battlefield and intensified Russian missile and drone strikes on energy and civil infrastructure across Ukraine. The recent airstrikes are deemed to be the strongest since beginning of the war. Destruction/heavy damaging of power infrastructure in Kharkiv, Odessa and several other regions in the aftermath has already resulted in regular electricity shutdowns and correspondingly business activity decline there. And the loss of Trypillia Thermal Power Plant - one of the biggest in Ukraine - will impact power supply not only in Kyiv but also in adjacent regions.

Furthermore, continuous airstrikes pose risks to further development of the sea corridor, with seaports already unable to operate at full capacity because of heavy damages to a nearby logistic and energy infrastructure.

Despite these challenges, we still see potential for a positive GDP growth this year. Lengthy negotiations notwithstanding, we expect the US support package to ultimately be approved. Moreover, the strained financial situation has spurred Ukraine's progress along reform agenda, enhancing the country's prospects to attract support from other countries.

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	5.3	2.0
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	6 538	7 869
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	5.8
CPI (end of year %YoY)	13.7	9.8	4.1	5.0	10.0	26.6	5.1	8.9
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	37.0
Imports coverage (months of imports of goods)	3.6	3.5	3.9	4.8	4.1	3.7	5.4	4.8
Interest and exchange rates								
NBU discount rate (% end of year)	14.5	18.0	13.5	6.0	9.0	25.0	15.0	13.0
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

FOUR WEEKS AHEAD

Mon	Tue	Wed	Thu	Fri	Sat	Sun
15.04.2024	16.04.2024	17.04.2024	18.04.2024	19.04.2024	20.04.2024	21.04.2024
		LGB % UAH 927.6mn				
22.04.2024	23.04.2024	24.04.2024	25.04.2024	26.04.2024	27.04.2024	28.04.2024
			NBU: MPC			
29.04.2024	30.04.2024	01.05.2024	02.05.2024	03.05.2024	04.05.2024	05.05.2024
	IMF SDR 0.0mn NBU: BoP	IMF SDR 165.2mn LGB % UAH 1 312.9mn LGB P UAH 21 864.0mn Fed: FOMC				
06.05.2024	07.05.2024	08.05.2024	09.05.2024	10.05.2024	11.05.2024	12.05.2024
NBU: Minutes	NBU: FX Reserves (deadline - 7th day)	LGB % UAH 1 980.9mn LGB % UAH 1 872.2mn		Ukrstat: Price indices		

MOST COMMON TERMS AND ABBREVIATIONS

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

bp	basis point
pp	percentage point
y/y	in annual terms; year-on-year change
m/m	in monthly terms; month-on-month change
TTM	trailing twelve months
RHS	right-hand scale

Contacts

Investment Business Group

Viktoriia Nebeska
Market Making Government Bonds
(+38044) 298-83-36
viktoriia.nebeska@ukrsibbank.com

Olha Koval
Fixed Income Dealer
(+38044) 298-83-35
olha.koval@ukrsibbank.com

Mykhailo Kharchuk
Market Analysis
mykhailo.kharchuk@ukrsibbank.com

FX Business

Kostiantyn Rupchev
Head of FX Sales
(+38044) 298-83-34
kostiantyn.rupchev@ukrsibbank.com

Corporate Business

Vitaliia Yukhnovska
Head of MNC team
(+38095) 701-42-10
vitaliia.yukhnovska@ukrsibbank.com

Distribution:
macro@ukrsibbank.com