

Bond Market Insight

Rates fall

Comment on government bond placement

To restore successful bond auctions after a month's break, the MoF had to increase interest rates and shorten maturities. However, this increase was replaced by decrease in rates yesterday, and an extension of maturities to 12 months. In total, yesterday, the MoF borrowed UAH21bn, including proceeds from FX-denominated bills and with limited offerings for some issues.

Yesterday, the MoF offered three-month and six-month bills with limits, just UAH1bn for each maturity. Demand exceeded the offer by a few times, but the Ministry did not cancel limits due to August's large debt burden and large repayments scheduled for July. It is better for the Ministry to sell longer maturities, preferably into next year, and finance the budget deficit.

Table 1. Details of domestic government bonds placed at the auction (UAHbn)

ISIN	Coupon rate (%)	Payment freq ¹	Maturity	Qty of bonds sold	Price (UAH)	Proceeds ² (UAHm)	Volume ² (UAHm)	YTM ³ (%)	Out-standing (m) ⁴
UA4000198873	14.50	SA	19-Aug-20	1,000,000	1,045.41	1,045.41	1,000.00	10.80	6,430.73
UA4000209225	0.00	@Mty	25-Nov-20	1,000,000	947.15	947.15	1,000.00	10.78	7,705.84
UA4000209373	0.00	@Mty	24-Feb-21	6,480,484	922.18	5,976.18	6,480.48	11.00	6,480.48
UA4000209381	0.00	@Mty	19-May-21	3,809,560	901.39	3,433.90	3,809.56	10.97	3,809.56
Total UAH				12,290,044	11,402.63	12,290.04			24,426.61
UA4000209399	0.00	@Mty	10-Dec-20	375,767	981.48	9,788.18	9,972.86	3.38	9,972.86
Total USD				375,767	9,788.18	9,972.86			9,972.86

Note: [1] payment frequency abbreviations: M - monthly, Qtly - quarterly, SA - semi-annually, @Mty - at maturity date; [2] proceeds and volumes for the USD-denominated bonds are calculated based on the previous day's exchange rate 26.54/USD, 30.44/EUR; [3] yields on coupon-bearing bonds are effective yields to maturity. Sources: Ministry of Finance of Ukraine, Bloomberg, ICU.

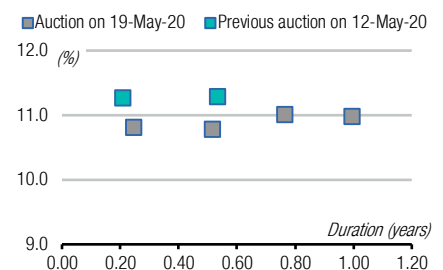
By using limits, the MoF was able to decrease interest rates for short maturities. For three-month bills, as demand was four times larger than offering, both the cut-off and weighted-average rates decreased to 10.5% or 80bp and 76bp, respectively. The Ministry accepted only 11 out of 21 bids for this paper, probably some of them partially.

The decline in interest rates for the six-month instrument was less material. Demand was two times larger than the offering. Out of 15 bids received, the MoF rejected only four. As a result, the cut-off rate was down 28bp to 11% and the weighted-average rate declined 50bp to 10.78%.

Most of the proceeds in local currency were received from bills with maturities in February and May of next year, UAH6bn and UAH3.4bn, respectively. The MoF sold

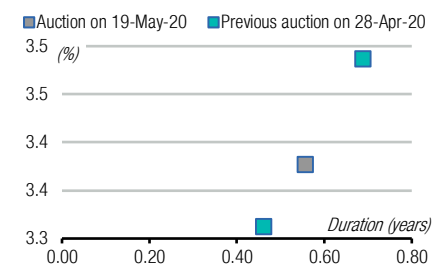
WEDNESDAY, 20 MAY 2020

UAH-denominated domestic gov't bonds: yield curve in past two auctions



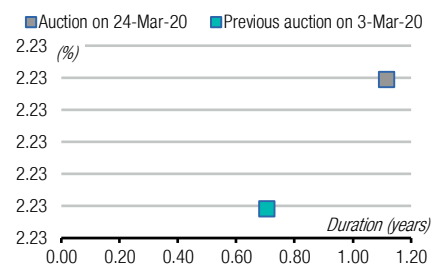
Source: Ministry of Finance of Ukraine, ICU.

USD-denominated domestic gov't bonds: yield curve in past two auctions



Source: Ministry of Finance of Ukraine, ICU.

EUR-denominated domestic gov't bonds: yield curve in past two auctions



Source: Ministry of Finance of Ukraine, ICU.

similar maturities last year, but under different demand and tight monetary policy conditions. But compared with December, rates declined a bit. For nine-month bills, the cut-off rate was set at 11%, while for the 12-month issue, it was set at 10.97%.

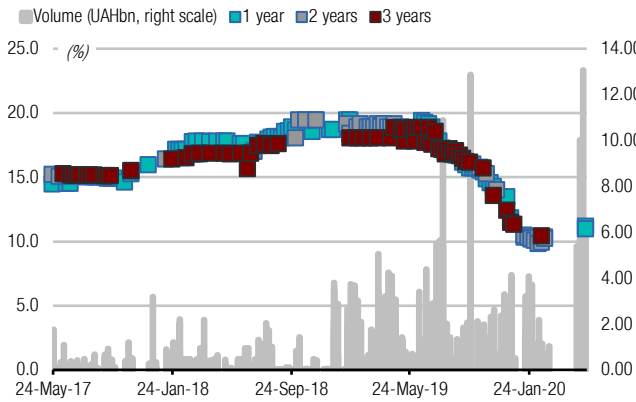
For USD-denominated bills, the decline in rates was less material. The cut-off rate decreased by 10bp to 3.4%, while the weighted-average rate slid 11bp to 3.39%.

The current market situation has become more positive for the government. Demand is for different maturities within one year. Sure, the ability to receive loans from the NBU is very important, but in recent weeks, banks took out loans in significantly lower amounts than what they bought in new government paper. Banks are not in a hurry to take loans, instead, they will use their own funds for bills' purchases. This week, we again expect low demand for loans. Later, however, we expect to see offerings of longer maturities at the auction, and likely a further decline in interest rates brought about by limited offered amounts.

Appendix: Yields-to-maturity, repayments

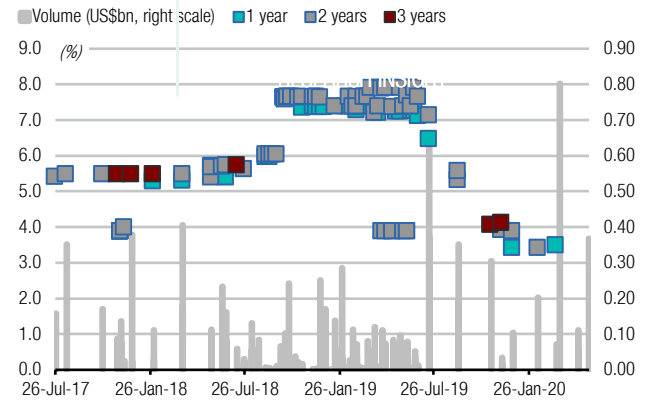
Chart 1. Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

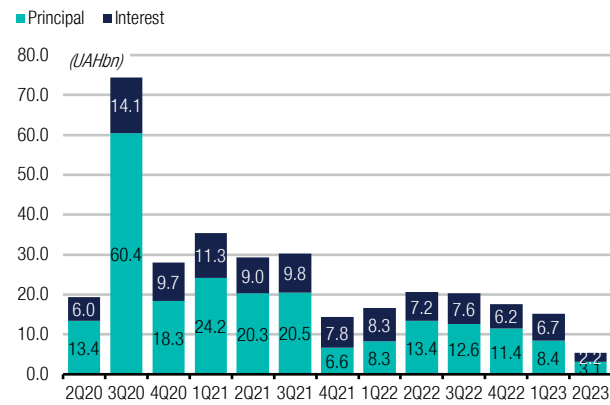
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

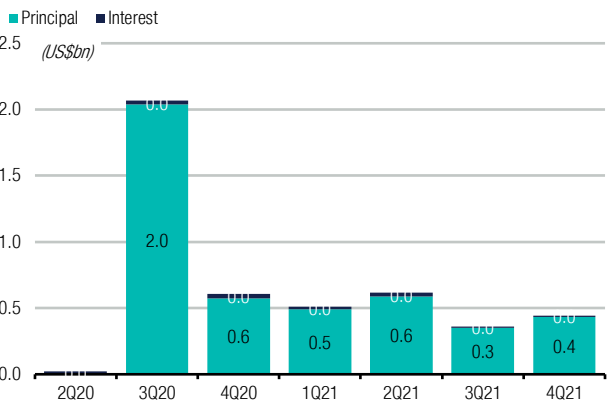
Chart 2. Future repayments on domestic government bonds (in billions of currency)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

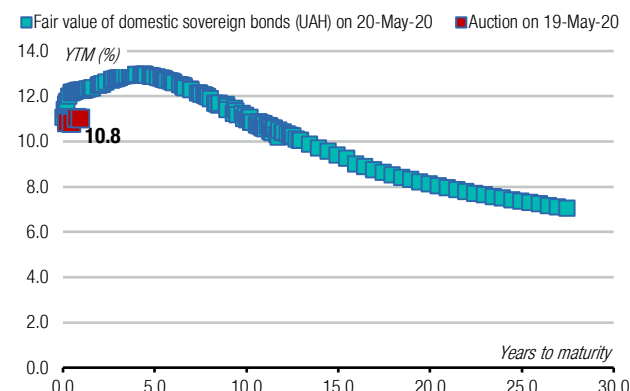
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

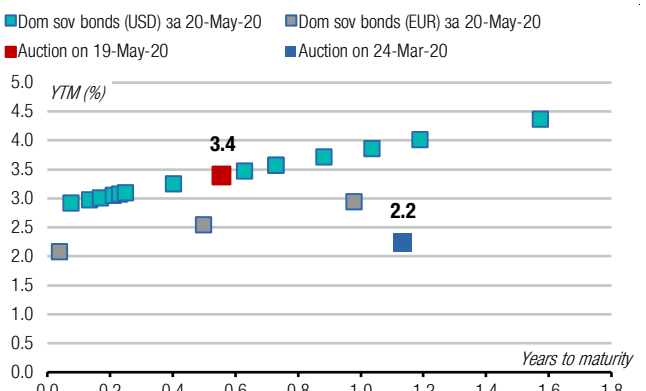
Chart 3. Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions

UAH-denominated domestic government bonds



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

USD- and EUR-denominated domestic government bonds



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

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