

Bond Market Insight

Competition for short-term bills

Comment on government bond placement

In an effort to repeat its success with 1.5-year bills last week, yesterday, the MoF offered two-year and three-year bills. However, this week, demand was concentrated in the short-term maturities with redemptions this year. Out of UAH4.6bn of demand, only UAH1bn was for longer maturities; almost UAH3.6bn was for short-term bills.

Since the two shortest issues had limited offerings, bidders had to submit low rates to win in the auction. The highest rate for three-month bills declined by 125bp to 8.5% while the lowest was down 150bp to 7.5%. The Ministry accepted only the lowest rates until the limit of bills was exhausted, likely only partially satisfying seven out of 21 bids, where 30% of the bids were non-competitive. Very similar results came from the placement of six-month bills, where, in full, only bids with the lowest rate of 7.99% were accepted, while rest of the bills were distributed between non-competitive bids and bids at 8%.

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

ISIN	Coupon rate (%)	Payment frequency	Maturity	Qty of bonds sold	Price (UAH)	Proceeds ² (UAHm)	Volume ² (UAHm)	YTM ³ (%)	Outstanding (m) ⁴
UA4000202469	17.25	SA	30-Sep-20	500,000	1,063.42	531.71	500.00	7.66	6,940.99
UA4000209225	0.00	@Mty	25-Nov-20	500,000	965.92	482.96	500.00	8.00	9,414.82
UA4000209886	10.57	SA	23-Feb-22	706,365	1,032.23	729.13	706.37	10.88	706.37
UA4000207682	9.84	SA	15-Feb-23	213,430	1,011.07	215.79	213.43	11.08	1,148.56
Total UAH				1,919,795	1,959.59	1,919.80			18,210.74

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 26.73/USD, 30.23/EUR; [3] yields on coupon-bearing bonds are effective yields to maturity. Sources: Ministry of Finance of Ukraine, Bloomberg, ICU.

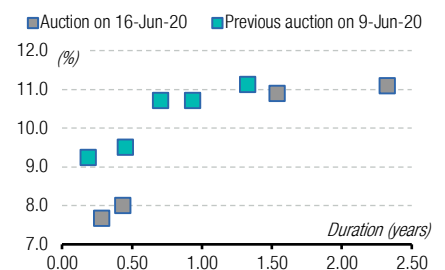
However, for longer bills, the Ministry accepted most of demand, despite having to increase rates compared with similar auctions in February, prior to the lockdown. Only one bid for two-year bills at UAH100m with a 10.8% rate was rejected. The cut-off rate for this paper was set at 10.7% with the weighted-average at 10.57%, or 70bp and 57bp above the pre-lockdown level.

For the three-year issue, the MoF accepted all bids, and also increased interest rates. The cut-off rate was set 66bp above the pre-lockdown level, and the weighted-average rate was increased 1bp less, by 65bp.

Consequently, banks are more interested in short-term bills, which provide them a 150-200bp premium to NBU's key policy rate and seven-day NBU CDs. Potentially,

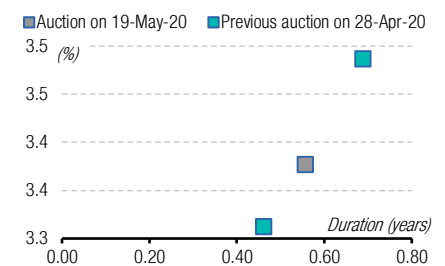
WEDNESDAY, 17 JUNE 2020

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



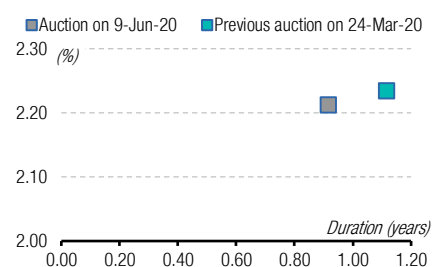
Source: Ministry of Finance of Ukraine, ICU.

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.

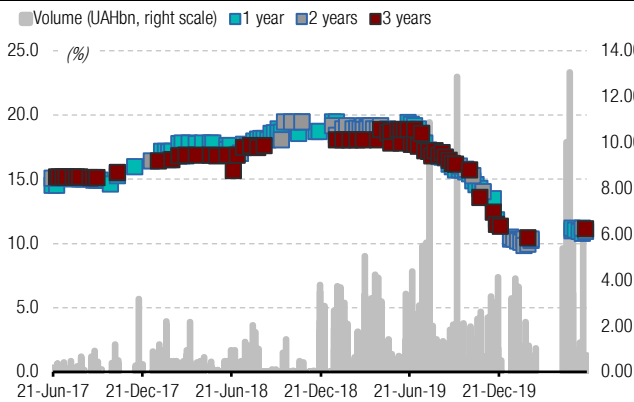
short-term bills will be mostly purchased using funds from CDs or funds that could be invested in CDs at the next tender. Therefore, short-term paper received large demand at low rates compared with other maturities.

However, longer bills likely were purchased by other investors and not only by banks. However, without debt redemptions, demand is quite moderate. It could stay low until the beginning of July, when there will be another local-currency debt redemption.

Appendix: Yields-to-maturity, repayments

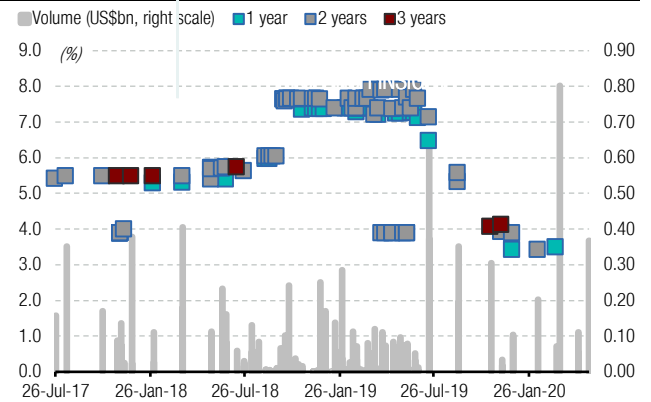
Chart 1. Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

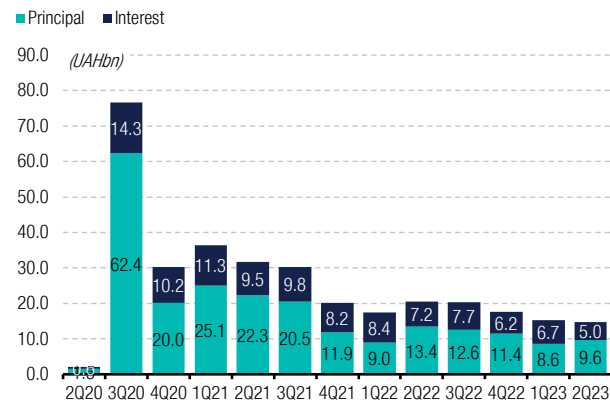
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

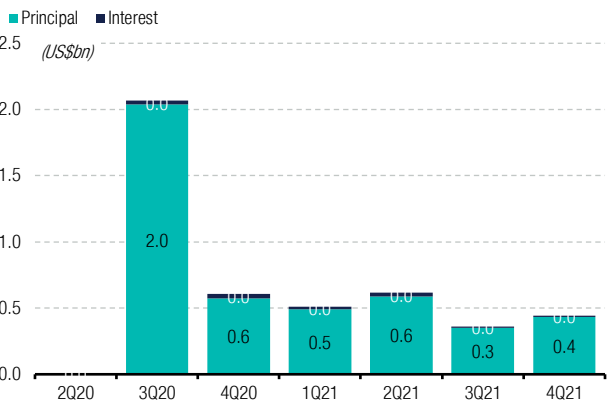
Chart 2. Future repayments on domestic government bonds (in billions of currency)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

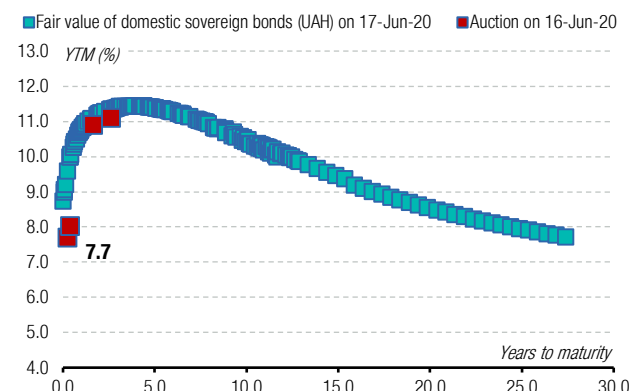
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

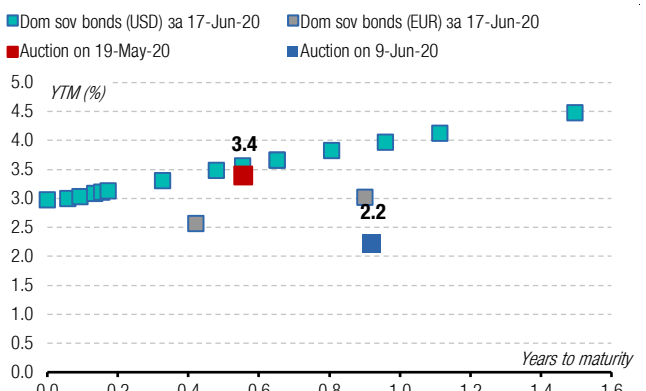
Chart 3. Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions

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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11th floor, LEONARDO Business Centre
19-21 Bogdan Khmelnytsky Street
Kyiv, 01030 Ukraine
Phone/Fax +38 044 3777040

WEB www.icu.ua



RESEARCH

Sergiy Nikolaychuk

Head of macro research
sergiy.nikolaychuk@icu.ua

Taras Kotovych

Senior financial analyst (Sovereign debt)
taras.kotovych@icu.ua

Dmitriy Dyachenko

Junior financial analyst
dmitriy.dyachenko@icu.ua

Alexander Martynenko

Head of corporate research
alexander.martynenko@icu.ua

Mykhaylo Demkiv

Financial analyst (Banks)
mykhaylo.demkiv@icu.ua

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