

# Bond Market Insight

## Cautious increase in rates

### Comment on government bond placement

WEDNESDAY, 26 JANUARY 2022

The first reaction of market participants to NBU's increase in the key policy rate last week was to try to induce the Ministry of Finance to increase interest rates on local-currency bills by at least 50bp. But for most issues offered yesterday, this didn't happen.

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

ISIN	Coupon rate (%)	Payment freq <sup>1</sup>	Maturity	Qty of bonds sold	Price (UAH)	Proceeds <sup>2</sup> (UAHm)	Volume <sup>2</sup> (UAHm)	YTM <sup>3</sup> (%)	Out-standing (m) <sup>4</sup>
UA4000221436	0.00	@Mty	27-Apr-22	2,923,026	972.13	2,841.56	2,923.03	11.50	17,803.82
UA4000200885	15.97	SA	19-Apr-23	3,830	1,087.78	4.17	3.83	12.29	12,531.68
<b>Total UAH</b>				<b>2,926,856</b>	<b>2,845.73</b>	<b>2,926.86</b>			<b>30,335.50</b>

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 28.31/USD, 30.69/EUR; [3] yields on coupon-bearing bonds are effective yields to maturity. Sources: Ministry of Finance of Ukraine, Bloomberg, ICU.

In fact, interest rates were raised only for three-month bills, where demand at face value was just slightly below UAH3bn in 10 bids with a unanimous rate of 11.5%. This is 55bp more than two weeks ago with almost five times larger demand. Therefore, there was not much for the MoF to decide and all demand was met.

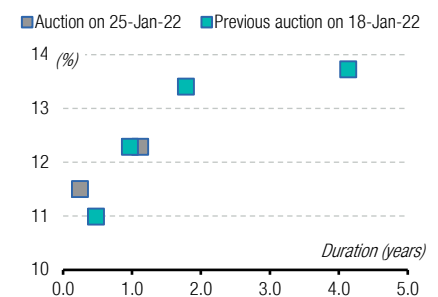
But for 15-month securities, demand was only in non-competitive bids, so there was nothing to choose from. Using the right to accept the non-competitive demand at the weighted average rate of the previous similar placement (also two weeks ago), the Ministry accepted this demand at a rate of 11.9%.

The MoF cancelled the offering of both the 12-month and two-year bills, rejecting all received demand. It is possible that if the volume of demand was higher, not UAH12m and UAH120m, respectively, at face value, part of the demand could have been satisfied. But two factors together — high interest rates for relatively small amounts — impacted the MoF's decision.

There were six bids for the 12-month bills, of which all competitive bids were at a single rate of 12.4%. However, all demand was less than UAH12m. Although the volume was ten times higher for two-year paper, almost UAH120m, rates were too high. Competitive bids ranged from 13.45% to 15%.

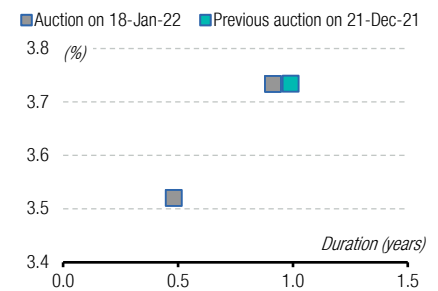
Of course, the Ministry could have raised rates by 50bp, half of the increase in the key policy rate, which was what the bidders were looking for. The Ministry didn't, probably because of the small amounts in these bids.

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



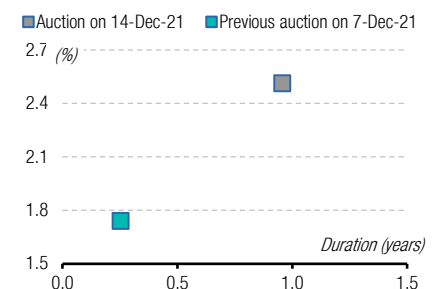
Source: Ministry of Finance of Ukraine, ICU.

### 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



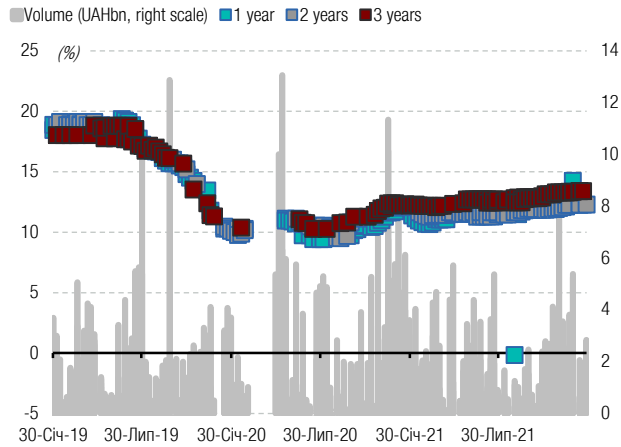
Source: Ministry of Finance of Ukraine, ICU.

It is very likely that next week market participants will want at least the same level of interest rates as yesterday, but may be ready to submit bids with larger amounts. Demand should be much higher, as next week there will be redemptions of UAH10bn of bills sold last year. According to the schedule, next week, UAH-denominated bonds with a maturity of six months to four years should be offered.

# Appendix: Yields-to-maturity, repayments

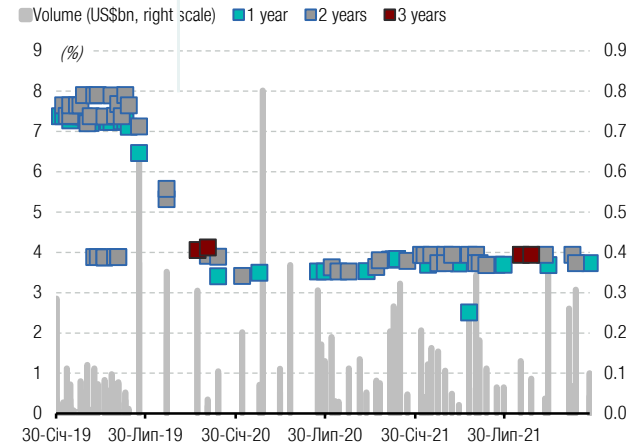
**Chart 1. Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)**

*UAH-denominated domestic government bonds*



Source: Ministry of Finance of Ukraine, ICU.

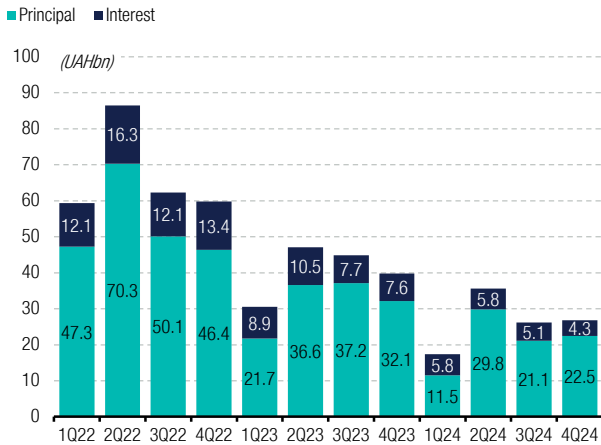
*USD-denominated domestic government bonds*



Source: Ministry of Finance of Ukraine, ICU.

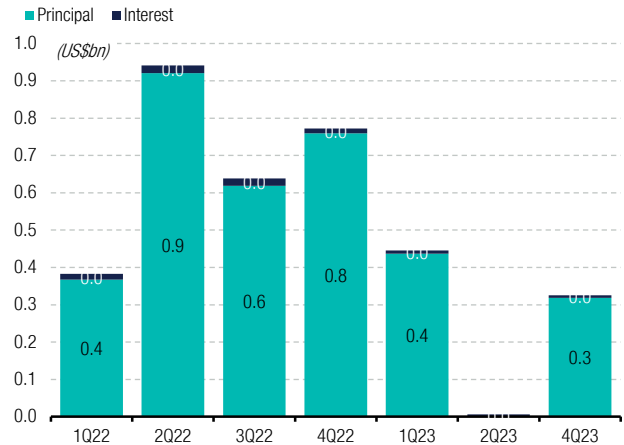
**Chart 2. Future repayments on domestic government bonds (in billions of currency)**

*UAH-denominated domestic government bonds*



Source: Ministry of Finance of Ukraine, ICU.

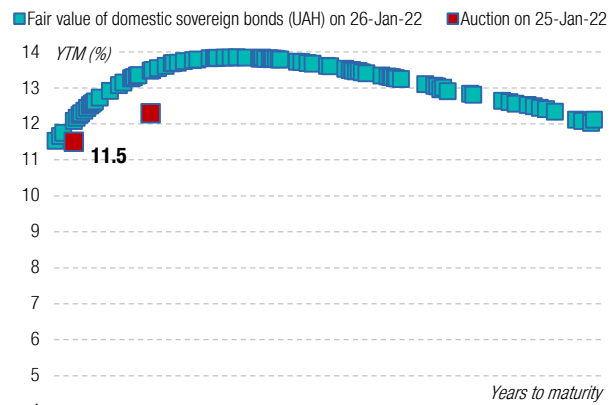
*USD-denominated domestic government bonds*



Source: Ministry of Finance of Ukraine, ICU.

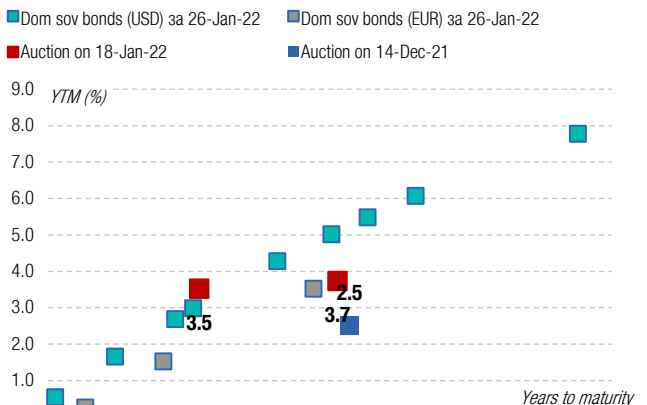
**Chart 3. Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions**

*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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