

Ukrainian Banking sector

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Ukrainian Banking Sector – Significant work done

- Banking sector has one of the best track record of reforms in Ukraine. Bank issues comprise a significant part of each Memorandum with the IMF.
- Recapitalization program in on track with all large and medium banks.
- Bank cleaning is de-facto over with the nationalization of Privatbank.
- Improvement of the regulatory function.
- Transparency in bank ownership structure.
- Fair and square rules regarding the disbursement NBU funding are set.
- Introduction of term deposits for household (no early repayment) helped to mediate recent turbulences.

In other areas:

- Macroeconomic stability reached; tough FX controls are constantly relaxed, although the pace of relaxation is far from investors' expectations.
- NBU key rate declined from 30% in March 2015 to 12.5% in June 2017 followed by the decrease of deposit rates.

Ukrainian Banking Sector – Current situation

- Domination of state-owned banks: 55% of total assets, 2/3 of infrastructure (cards, branches, ATMs). Government revise its strategy in the banking sector. Sale of Ukgazbank is expected within next few years, while Oschadbank and Privatbank might get strategic minority shareholders. Ukreximbank is cutting retail and is likely to concentrate on its mission as a 100%-state bank.
- High hryvnia liquidity and satisfactory FX liquidity among most of the large and medium-size banks.
- Deposit Guarantee Fund concentrated app. \$4.3bn of assets of insolvent banks under its management (by fair value). Less than US\$0.5bn of this amount have sold or repaid so far.

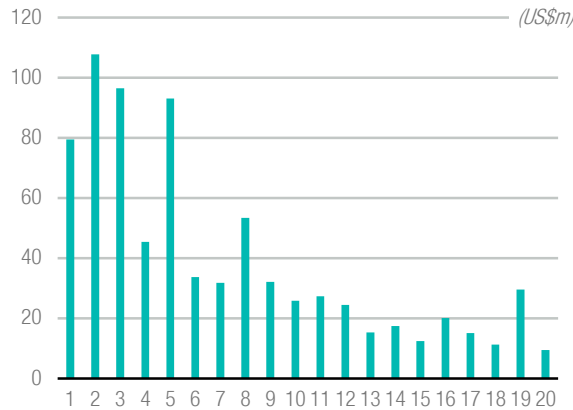
Problems:

- Weak lending.
- One-offs like Privatbank deteriorate the market.
- Slow deposit growth – it's current accounts that increase the funding base.
- Creditors right protection has little support in the Parliament

Very good liquidity but weak lending

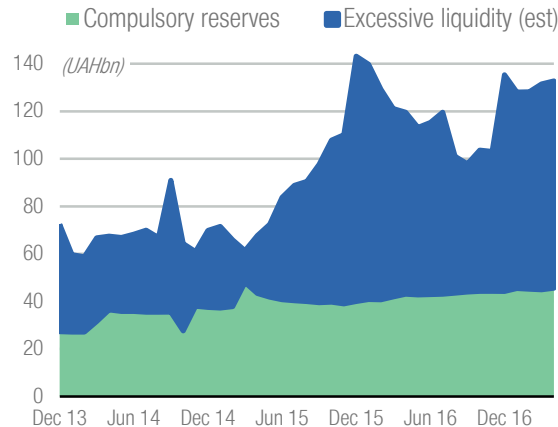
- Excessive UAH liquidity amounts to UAH80-90bn (US\$3-3.5bn).
- Total FX liquidity amounts to US\$4bn.
- Due to regulatory requirements (exposure is limited by 25% of the regulatory capital per borrower), top-banks cannot lend more than US\$20-100m in one hands.
- Shortage of good borrowers;
- Very high corporate loans-to-GDP ratio (40%) and very low retail debt-to-GDP ratio (<10%).
- Significantly weaker regulations in non-banking lending sector.
- Further decline of interest rates + economic growth should boost lending activity.

Exposure to borrower allowed (Top-20)



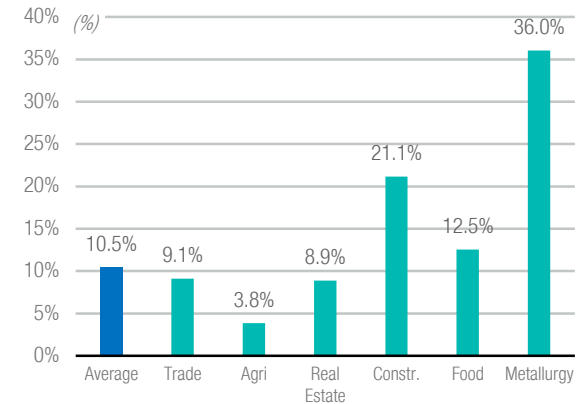
Source: ICU estimation

UAH liquidity of Ukrainian banks



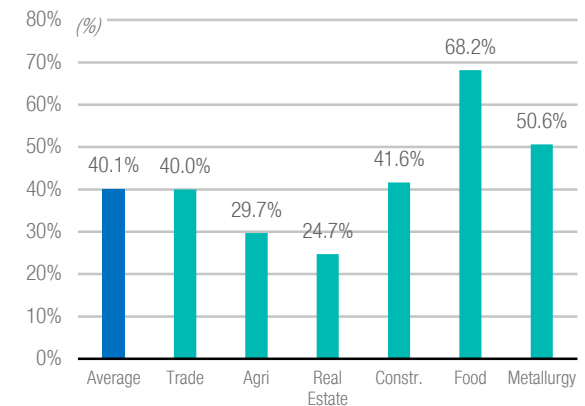
Sources: NBU, ICU estimation

Overdue loans (UAH) by industry



Sources: NBU, ICU estimation

Overdue loans (USD) by industry



Sources: NBU, ICU estimation

Decline of interest rates

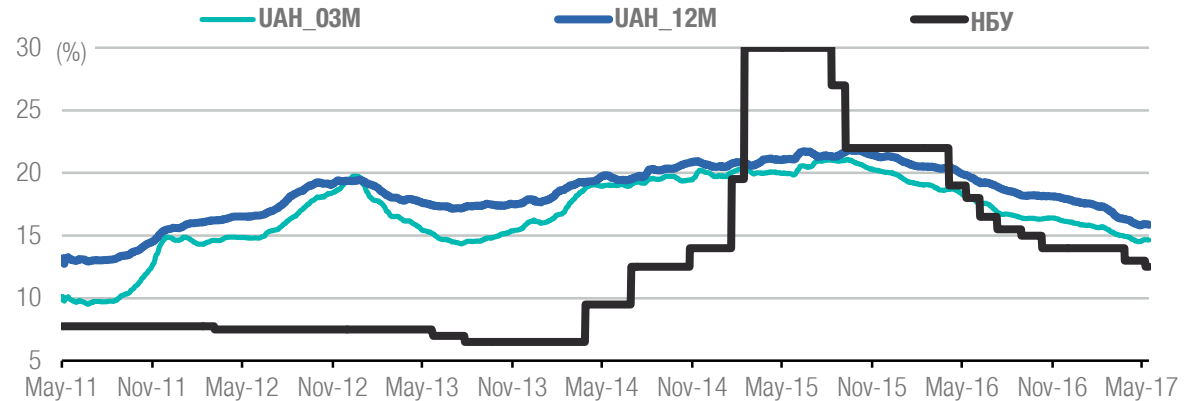
Reasons for interest decline:

- Sector cleaning. Banks that used to operate as Ponzi scheme went into liquidation;
- Weak lending;
- Government that controls >50% of the market benefits from declining rate of borrowing;
- No new FX loans to retail sector; Very cautious FX lending to corporates;

How much lower?

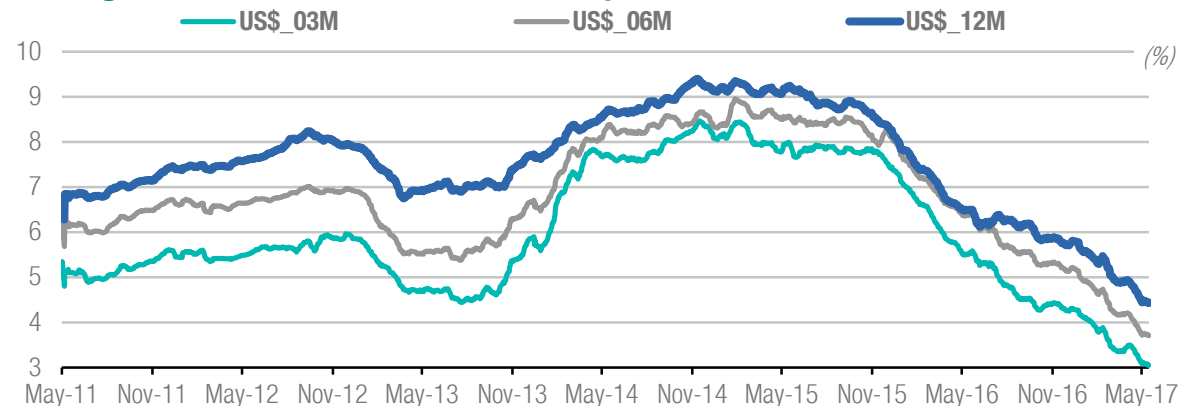
- NBU is targeting a single digit inflation by the end of the year;
- Without major negative shock, Key rate should drop below 10 in 1H18.
- No much room for further USD interest rate decline;
- Desire to substitute Eurobonds with local funding can have upward pressure for the interest rates;

Average retail interest rates on UAH deposits



Sources: NBU, ICU estimation

Average retail interest rates on USD deposits



Sources: NBU, ICU estimation

Eurobonds buyback by banks

Low interest rates on local deposits and inactive FX lending give initiative for banks to seek early redemption of Eurobonds or seek maturity extension;

NBU has specifically permitted early redemption of Eurobonds in one of its recent round of FX control relaxations;

FUIB has announced partial redemption at minimum price of 101.5%;

Oschadbank and Ukreximbank have considerably larger amount of outstanding bonds but current amount of FX liquidity does not allow full redemption;

Contacts

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