National Bank of Ukraine

Banking Sector Review

May 2021

The gradual economic recovery is spurring demand for banking services. The hryvnia loan portfolio grew in Q1 in both the corporate and retail segments. The growth in household deposits slowed, but remained significant. The financial performance of banks declined due to the revaluation of indexed securities, while net interest and commission income grew by over 15%. The net stable funding ratio (NSFR) became mandatory in early April. Almost all institutions have complied with its initial minimum of 80%. The first stage of a diagnostic examination of the banks – the asset quality review – is coming to an end. The NBU is currently processing the banks' reports and starting stress testing.

Sector Structure

In Q1 2021, the number of operating banks in Ukraine did not change (73). At the same time, the NBU approved a plan to terminate Settlement Center PJSC due to amendments in legislation. The share of private banks in net assets increased by 1 pp, as in the previous two quarters. However, state-owned banks continue to hold more than half of assets and household deposits. At the end of March, the 20 largest banks accounted for more than 90% of the sector's assets.

Assets

The net assets of the banking sector grew by 0.7% qoq in Q1. The most significant increase occurred in the banks' accounts with the NBU, interbank assets, and the customer loan portfolio.

Net hryvnia corporate loans grew by 5.3% qoq and 5.8% yoy. Three-quarters of the nominal increase was due to loans made to a state-owned company. The only type of customers that reduced their demand for loans were subsidiaries of foreign corporations. Private banks did most of the lending. The volume of FX loans decreased in dollar terms by 2.9% qoq and by 7.3% yoy.

After decelerating last year, the growth in net hryvnia retail loans accelerated (by 6.0% qoq and by 8.2% yoy). Private banks led the way here as well, their hryvnia portfolio growth surpassing 10% qoq.

The NPL ratio continued to decline, but at a slower pace than last year. In Q1, this ratio fell by 1.1 pp (to 39.9%). Banks made significantly fewer NPL write-offs in Q1 2021 than in Q4 2020.

Funding

Bank liabilities grew by 0.3% in Q1. This change was mainly driven by increases in budgetary funds and in the NBU's refinancing loans. The share of the latter in the sector's total liabilities increased to 4.3%, its highest since 2016. Meanwhile, external borrowings – loans from IFIs and other institutions – fell significantly (by 18.2% qoq) after state-owned banks made repayments on Eurobonds. Customer deposits, accounting for 84.7% of liabilities, remain the basis of bank funding.

In Q1, hryvnia retail deposits grew by 2.6% qoq (24.2% yoy), most notably in banks with private and foreign capital. As hryvnia time deposits grew faster than demand deposits, the share of the latter fell by 0.6 pp in Q1 (to 54.5%). FX retail deposits did not significantly change in volume.

The volume of hryvnia corporate deposits seasonally declined by 2.3% qoq in Q1 after a surge in Q4 2020. The drop occurred during the first two months of the quarter, and deposit inflows resumed in March. The volume of hryvnia deposits increased only in state-owned banks. At the same time, the volume of FX corporate deposits in Q1 increased in the dollar equivalent by 6.4% qoq. The most significant increase in FX deposits was reported by banks with private capital (30.4%). As a result, the dollarization of customer deposits increased by 0.3 pp in Q1 (to 38.3%).

Interest Rates

To curb inflation, the NBU raised its key policy rate by 0.5 pp (to 6.5% per annum) in Q1, and by another 1 pp in April. This stopped the decline in interest rates on 12-month hryvnia retail deposits, and slowed the decrease in rates on 3-month deposits. Overall, these rates fell by 0.6 pp in Q1 and by another 0.1 pp in April. Interest rates on retail dollar deposits reached new historic lows, falling below a negligible 1%.

Interest rates on new hryvnia corporate loans continued to decline, though at a slower pace than last year: by 0.4 pp in Q1 (to 8.8% per annum). As loan and deposit rates fell simultaneously, the interest rate spread for new transactions with customers was little changed.

Financial Results and Capital

The banks reported profits of UAH 10.9 billion in Q1 2021, down almost one-third from the same period of 2020. Seven institutions remained loss-making, but their total loss was insignificant. Provisioning fell by 58.3% compared to last year and did not play a significant role in reducing financial performance.

The drop in the sector's profits was primarily due to the negative effect from the revaluation of securities, which resulted in a UAH 9.3 billion loss, compared to a UAH 18.2 billion gain last year. This in particular affected the performance of the two largest state-owned banks, which saw their profits fall from Q1 2020. The cost-to-income ratio (CIR) in Q1 2021 was worse than in the same quarter of the previous year: 61.0% compared to 47.4% last year. However, excluding the revaluation of securities, foreign currency, and financial derivatives, operating income was up 16.3% yoy, while the CIR stood at 50.7%.

Net interest income increased by 21.9% yoy, primarily due to a noticeable decline in the interest rate on deposits over the past 12 months. Despite the tightening of quarantine restrictions, which last year had a negative impact on the size of commissions, net commission income grew by 15.1% yoy in Q1, primarily due to an increase in cashless payments.

Prospects and Risks

The fact that interest rates stopped falling will result in a general narrowing of the interest rate spread, thus affecting the banks' interest income. To a lesser extent, this will affect banks that have significant volumes of ultra-short loans, as these banks changed the rates on these loans almost in sync with the NBU's key policy rate hike.

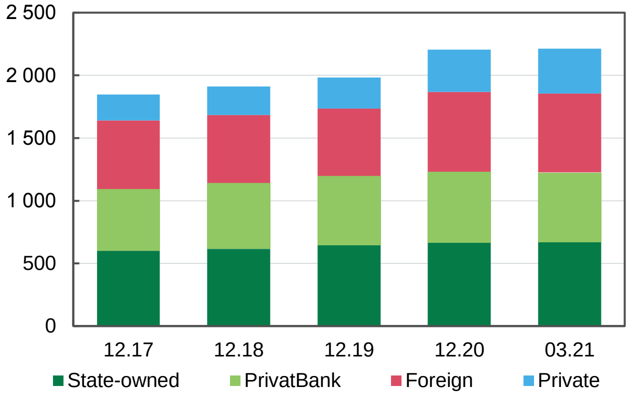
Although the provisions made in Q1 were moderate, credit risk is likely to remain high. To verify that the loan portfolio quality declared by the banks is accurate, the NBU is processing the results of the asset quality review of banks, which they were to have filed by the end of April. Another 30 banks will undergo stress testing, which was canceled last year due to the pandemic. In April, the NBU approved the methodology and macroeconomic scenarios for the stress testing of banks.

The NSFR took effect at the start of April. The NSFR at all of the banks apart from one small one have exceeded the minimum required level of 80%. The value of the NSFR will have been gradually raised to 100% by April 2022. Risk weights for FX securities issued by the Ukrainian government took effect on 1 April. The first stage of raising risk weights for unsecured consumer loans will start on 1 July, with an increase to 125%. Starting in 2022, they will rise to 150%.

Sector Structure

Total sector assets increased by 0.4% (to UAH 2.21 trillion) in Q1 2021. At the end of March, there were 73 solvent banks, the same number as in the previous quarter.

Figure 1. Banks' total assets, UAH billions*



* Solvent banks have been grouped in accordance with their classification in the respective reporting period.

Table 1. Number of banks*

	2017	2018	2019	2020	I.21
Solvent	77	75	73	73	73
Change	-14	-5	-2	-2	0
State-owned**	5	5	5	5	5
Change	-1	0	0	0	0
Foreign	23	21	20	20	20
Change	-2	-2	-1	0	0
Private	54	51	50	48	48
Change	-11	-3	-1	-2	0

* As of end of period.
** Including PrivatBank.

For the third quarter running, banks with private Ukrainian capital increased significantly their share in sector assets, by 1.1 pp in Q1, to 18.3%. As of the end of March, the shares of state-owned banks (including PrivatBank) of net assets and retail deposits were 51.9% and 59.3%, respectively.

Figure 2. Distribution of net assets across groups of banks

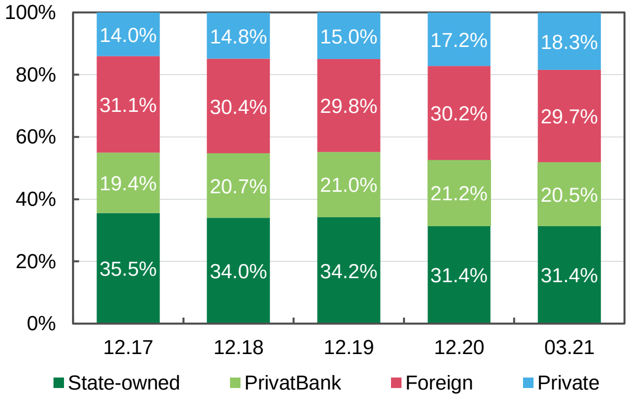
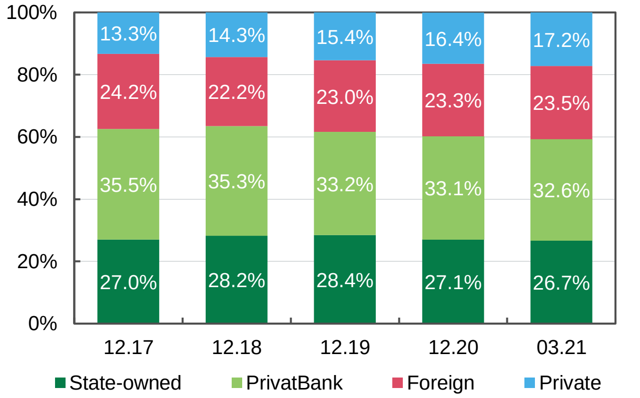


Figure 3. Distribution of retail deposits across groups of banks



As a result of private banks' activity, the share of the largest 20 banks has declined over the past two years. In Q1 2021, it decreased by 0.3 pp, to 91.3%.

Figure 4. The largest banks' share of the sector's net assets

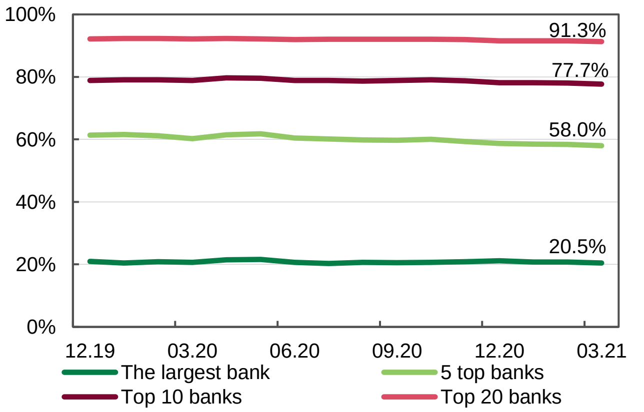
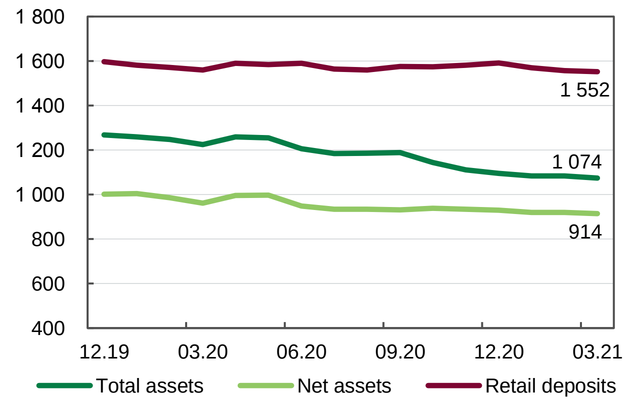


Figure 5. Concentration as defined by the HHI indicator*

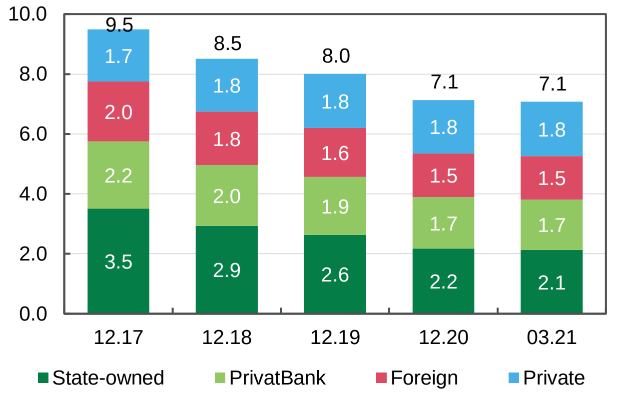


* The Herfindahl-Hirschman Index (HHI) is an indicator of banking sector concentration. It is calculated by summing the squared market shares of individual banks. The index ranges from 0 to 10,000, with values below 1,000 indicating low market concentration. Retail deposits include certificates of deposit.

Banking Infrastructure

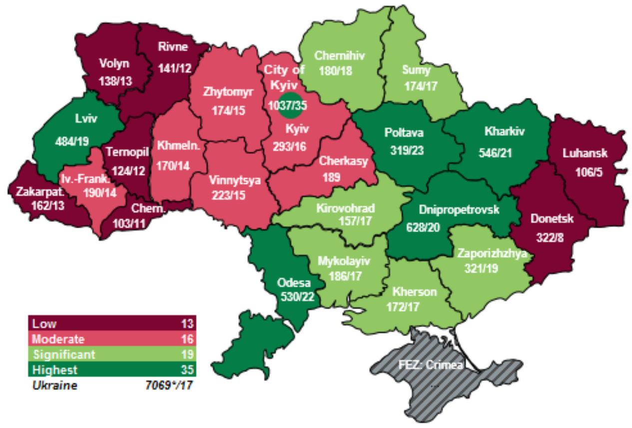
In Q1, the banks scaled down overall their branch network: most branches were closed by state-owned banks (by 81 including those of PrivatBank), and 6 by foreign banks. Only private banks opened new branches (+27). The largest reduction in the number of branches took place in Dnipropetrovsk and Donetsk regions (16 and 13, respectively).

Figure 6. Number of bank structural units*, thousands



* Standalone bank structural units and head offices.

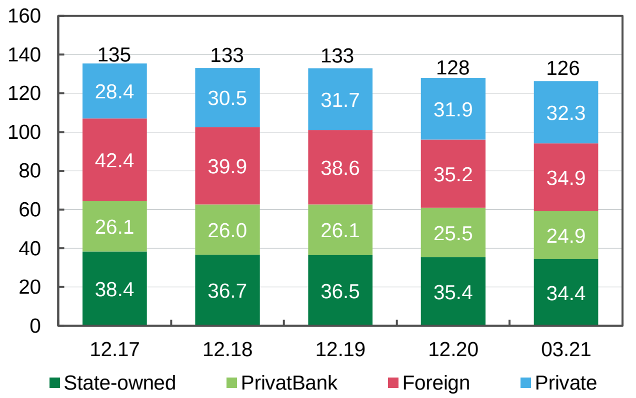
Figure 7. Operating bank structural units in selected regions as of 1 April 2021, structural units per 100,000 individuals



* Excluding four structural units abroad.

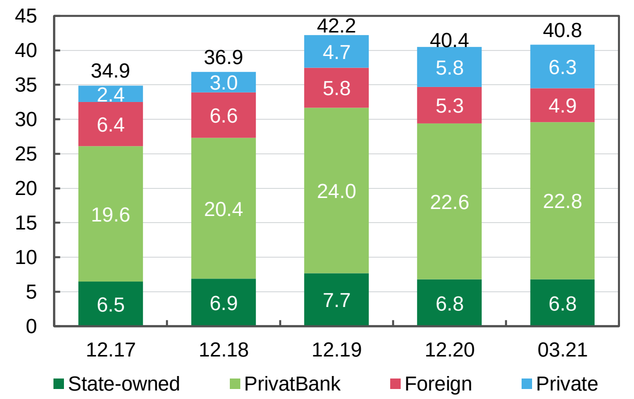
In Q1, state-owned banks (including PrivatBank) and foreign banks continued to lay off employees: 1,639 and 350, respectively. Private banks were hiring (+342 people).

Figure 8. Bank staff headcount, thousands of employees



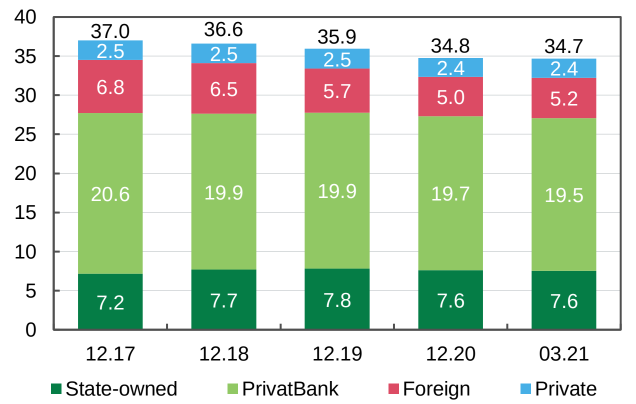
The number of active payment cards increased slightly in Q1. Private banks led this increase, outpacing PrivatBank. The number of active cards of foreign banks decreased.

Figure 9. Number of active payment cards by groups of bank, millions of units



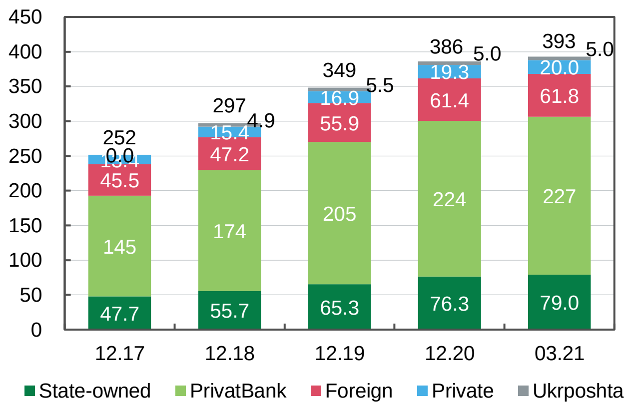
The network of bank POS-terminals expanded in Q1. The highest increases were made by PrivatBank (+3,000 terminals) and other state-owned banks (+2,800). The banks withdrew 66 ATMs from their network in Q1.

Figure 10. Number of ATMs*, thousands of units



* Number of self-service bank machines (ATMs, deposit ATMs, and self-service kiosks).

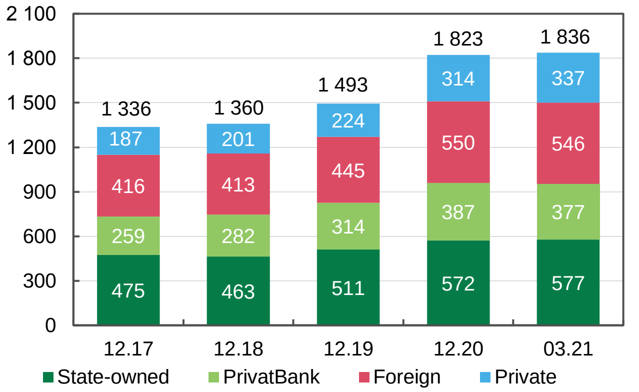
Figure 11. Number of POS terminals, thousands of units



Assets

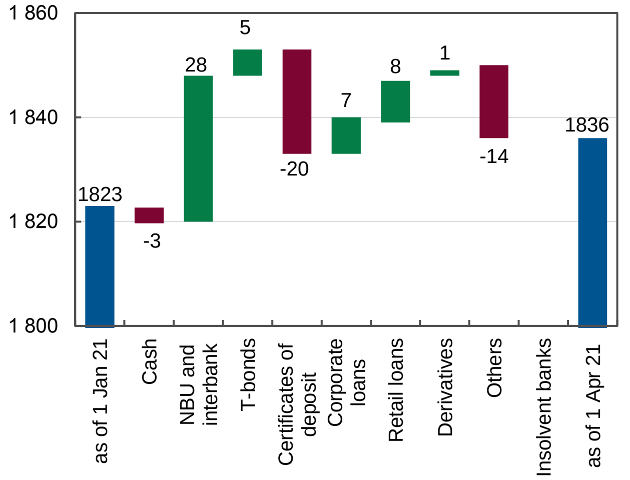
The banking sector's net assets grew by 0.7% in Q1, to UAH 1.84 trillion. The funds held in NBU accounts and customer loans increased the most.

Figure 12. Banks' net assets*, UAH billions



* Adjusted for loan loss provisions of banks.

Figure 13. Change in net assets by component in Q1 2021, UAH billion



The share of retail loans returned to growth in Q1, up 0.4 pp to 8.6%. Corporate loans as a share of net assets remained unchanged at 23.9%. Write-offs of FX NPLs have been more moderate this year than last year.

Figure 14. Sector net assets by component

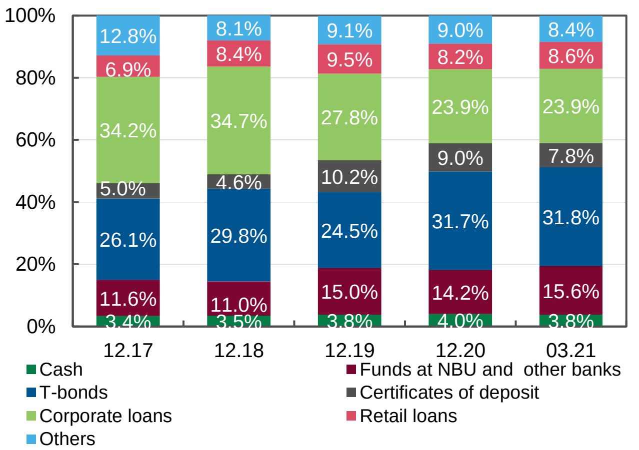
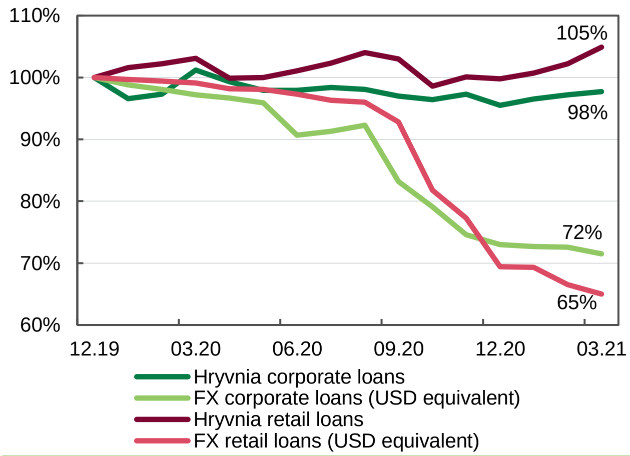


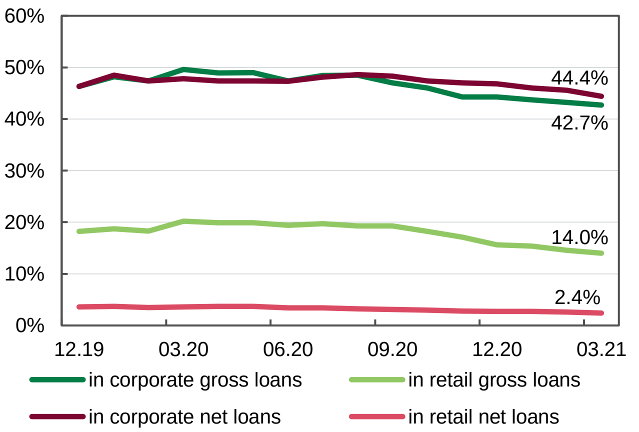
Figure 15. Gross corporate and retail loans, 2019 = 100%



* Issued by banks solvent as of 1 April 2021.

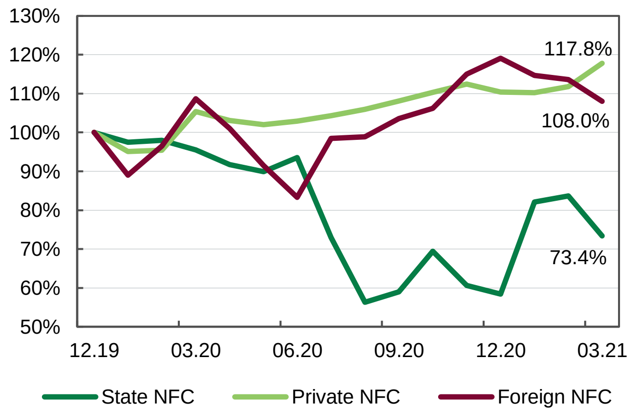
The recovery in hryvnia lending reduced the dollarization of net corporate loans by 2.4 pp in Q1, to 44.4%.

Figure 16. Share of FX loans



Net hryvnia loans to domestic private and state-owned companies grew by 6.7% and 25.6% in Q1, respectively.

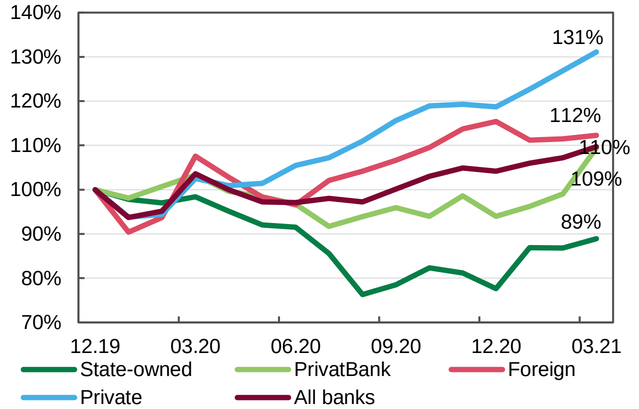
Figure 17. Net loans to nonfinancial corporations (NFCs) in UAH, 2019 = 100%*



* Issued by banks solvent as of 1 April 2021.

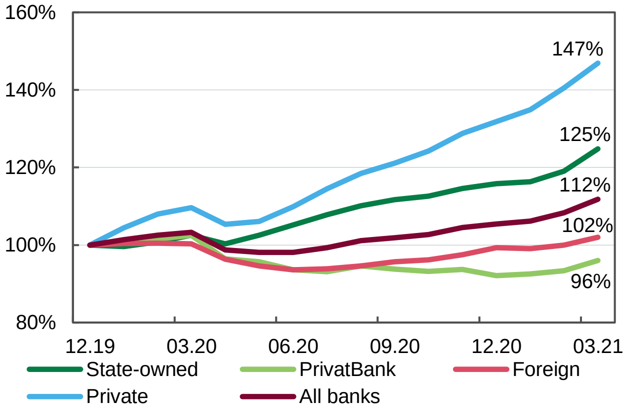
The net hryvnia retail portfolio returned to growth in Q1, gaining 6.0% qoq and 8.2% yoy. Net hryvnia corporate loans also increased, by 5.3% qoq and 5.8% yoy. The fastest increases occurred in private banks.

Figure 18. Net hryvnia corporate loans, 2019 = 100%*



* Issued by banks solvent as of 1 April 2021.

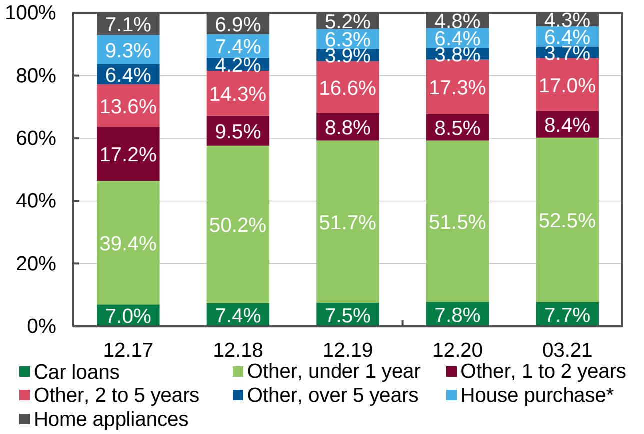
Figure 19. Net hryvnia retail loans, 2019 = 100%*



* Issued by banks solvent as of 1 April 2021.

In the breakdown of the hryvnia retail portfolio, the share of loans granted for up to one year for other consumer purposes increased.

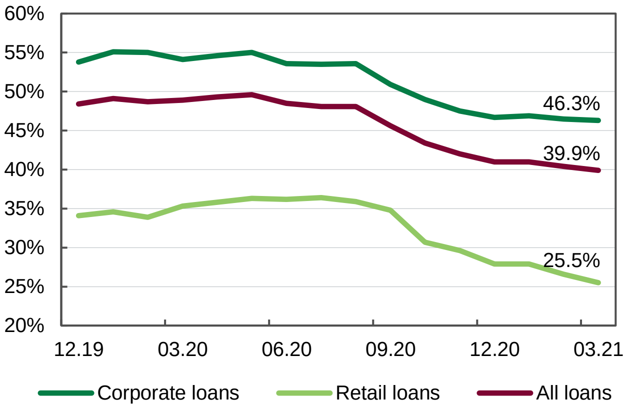
Figure 20. Gross hryvnia retail loans by purpose



* For the purchase, construction, and renovation of real estate (including land plots).

With the revival of retail lending, the NPL ratio for retail loans fell rapidly compared to that for corporate loans.

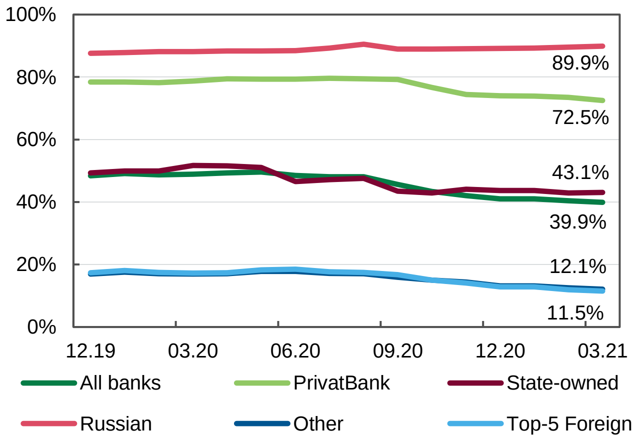
Figure 21. Banks' NPL ratios*



* At all banks, including insolvent ones; excluding off-balance sheet liabilities. Individuals, including sole proprietors.

Write-offs during the quarter were significantly lower than in Q4 2020, slowing the decrease in the NPL ratio. In late March, NPLs made up 39.9% of the banking sector's loan portfolio.

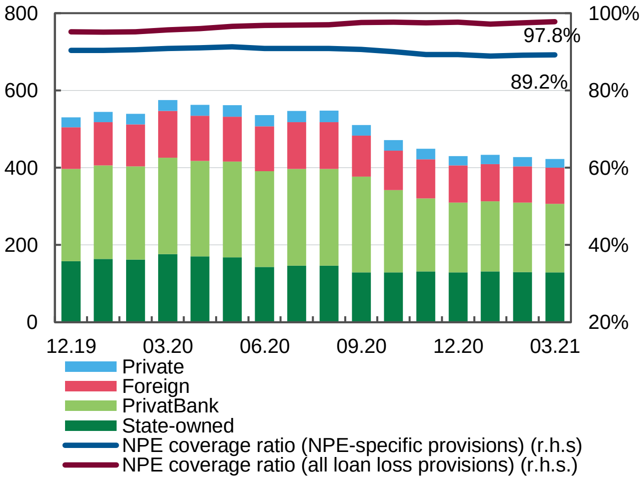
Figure 22. NPL ratio across groups of banks*



* Including interbank loans; at all banks, including insolvent ones; excluding off-balance sheet liabilities.

** Top-5 foreign banks by net assets as of 1 April 2021 (excluding Russian-owned banks).

Figure 23. Non-performing exposures (NPE) and provisions



* At all banks including insolvent ones, excluding off-balance sheet liabilities.

Funding

The banks' liabilities increased by 0.3% in Q1. State budget funds almost doubled, while IFI loans fell by 18.2% due to Eurobond repayments by state-owned banks.

Figure 24. Liabilities by groups of banks, UAH billions

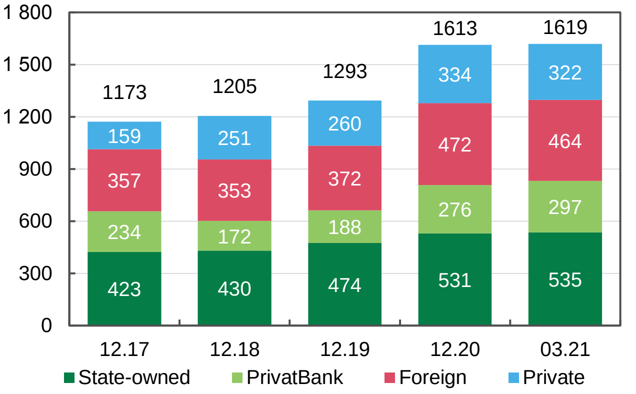
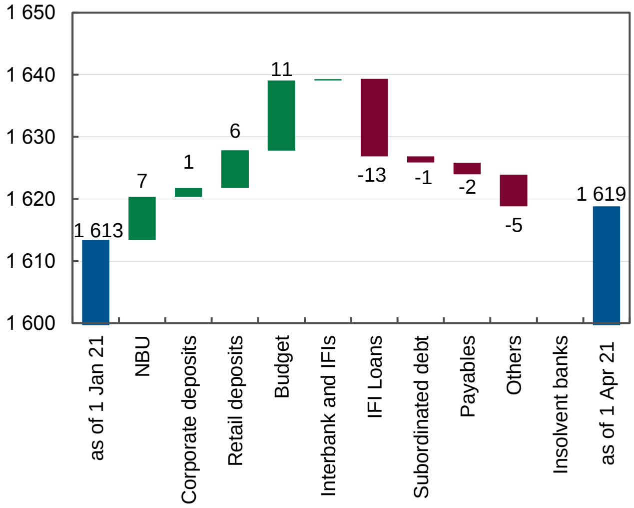
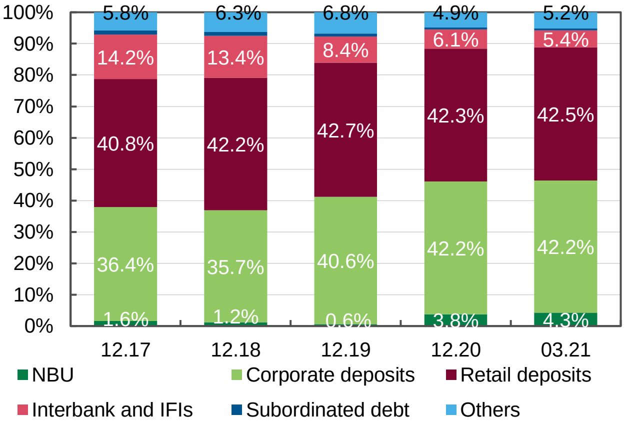


Figure 25. Changes in liabilities in Q1 2021 by factor, UAH billions



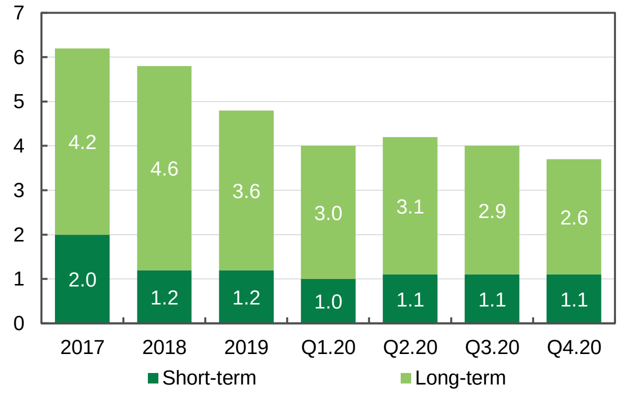
Customer deposits as a share of liabilities increased by 0.2 pp in Q1, to 84.7%. The share of interbank and IFI loans decreased (-0.8 pp)

Figure 26. Breakdown of liabilities



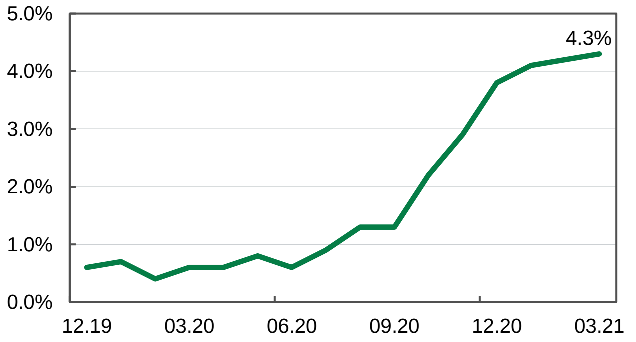
In Q4 2020, the banks' gross external debt fell by 8.8%, primarily due to repayments on long-term Eurobonds.

Figure 27. Banks' gross external debt, USD billions



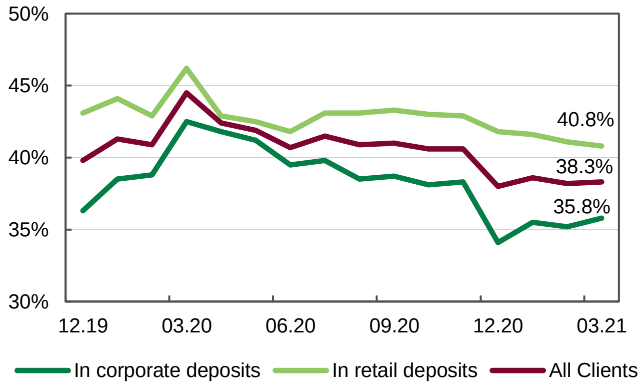
As the banks took out refinancing loans, the share of NBU loans in liabilities increased by 0.4 pp to 4.3%, its highest since 2016.

Figure 28. Share of NBU funds in bank liabilities



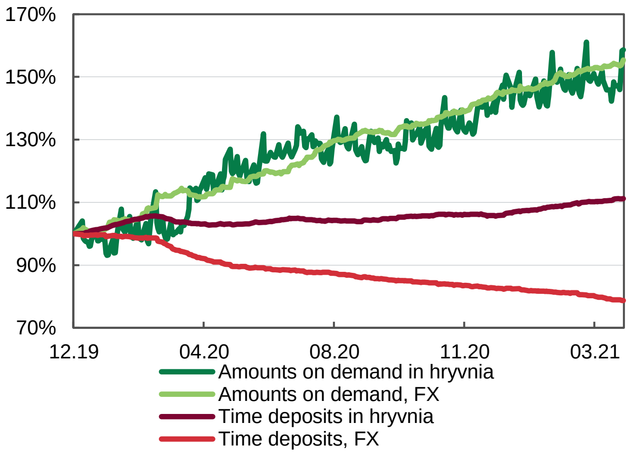
The dollarization of customer deposits in Q1 increased by 0.3 pp (to 38.3%), mainly due to the growth in FX corporate deposits.

Figure 29. Percentage of FX deposits



Hryvnia deposit growth decelerated to 2.6% qoq, down from 7.8% qoq in Q4 2020. The volume of FX deposits remained almost unchanged after inching down by 0.1% qoq.

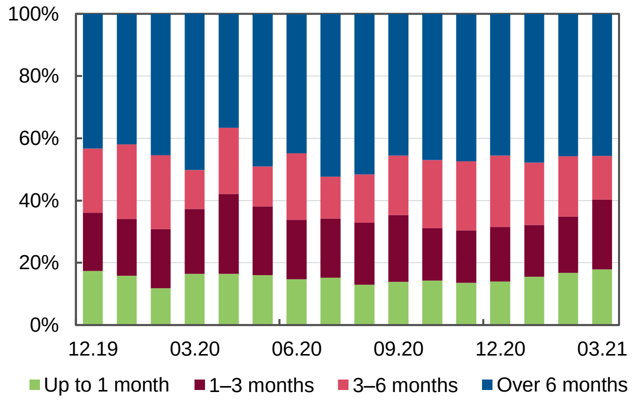
Figure 30. Retail deposits, 2019 = 100%*



* At solvent banks as of 1 April 2021, including certificates of deposit.

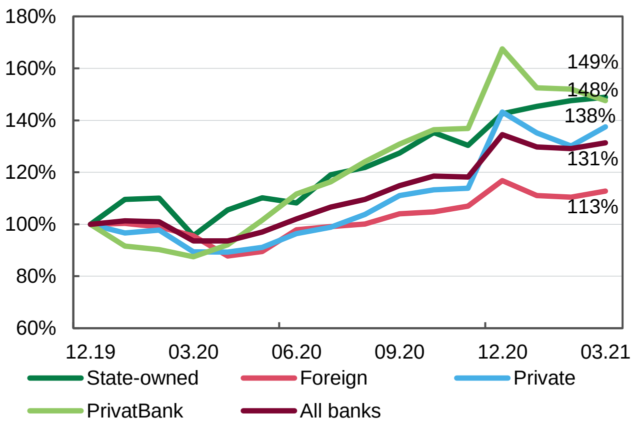
The share of new time deposits with maturities of up to three months increased by 8.8 pp in Q1, to 40.3% at the end of the quarter.

Figure 31. New hryvnia retail deposits by maturity



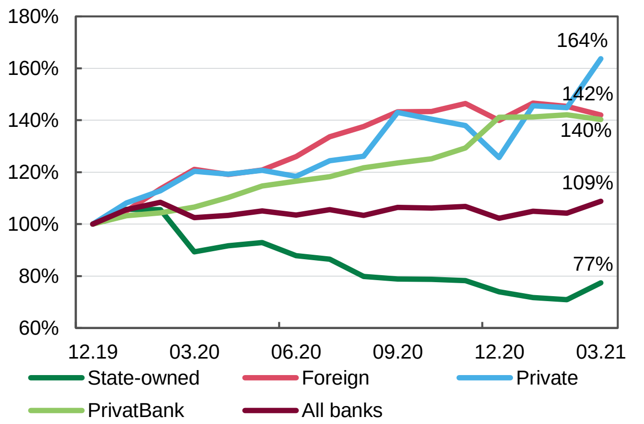
Hryvnia corporate deposits declined by 2.3%. Deposit outflows were seen in all groups, except for banks with state capital (+4.5% qoq). FX corporate deposits grew by 6.4%, most notably in banks with private capital (+30.4%).

Figure 32. Hryvnia corporate deposits by groups of banks, 2019 = 100%*



* Issued by banks solvent as of 1 April 2021.

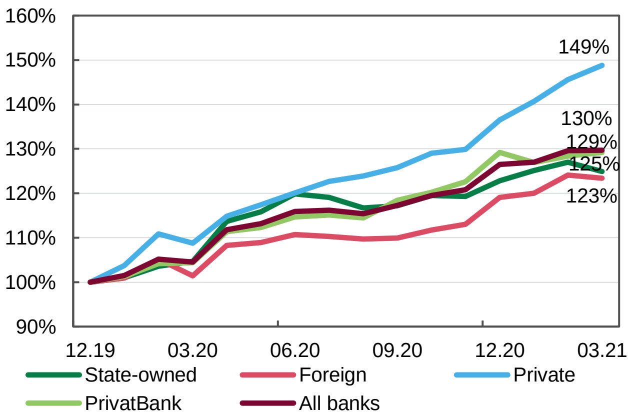
Figure 33. FX corporate deposits (in US dollar equivalent) by groups of banks, 2019 = 100%*



* Issued by banks solvent as of 1 April 2021.

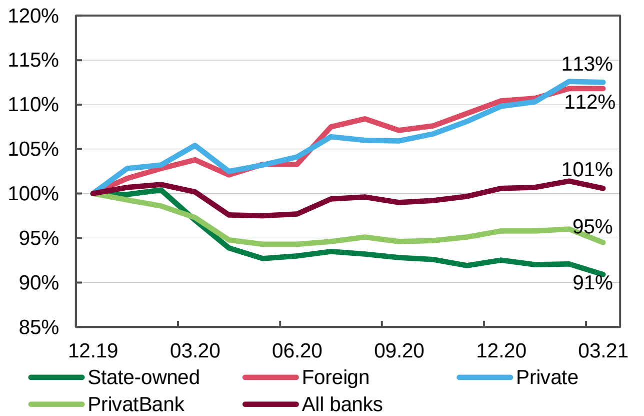
Hryvnia retail deposits grew in all groups of banks. The most significant increase – 8.9% – was reported by banks with private capital. FX deposit outflows were seen in PrivatBank (-1.4%) and other state-owned banks (-1.7%).

Figure 34. Hryvnia retail deposits by groups of banks, 2019 = 100%*



* Issued by banks solvent as of 1 April 2021.

Figure 35. FX retail deposits (in US dollar equivalent) by groups of banks, 2019 = 100%*

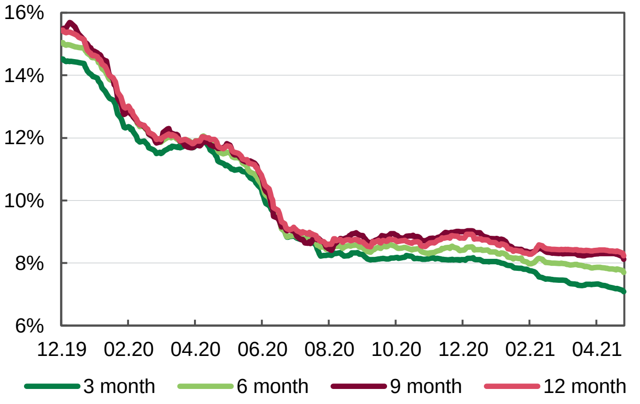


* Issued by banks solvent as of 1 April 2021.

Interest Rates

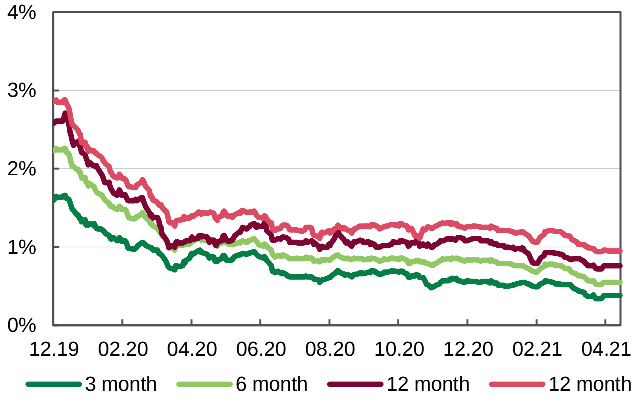
In January 2021, the interest rate on 12-month hryvnia deposits decreased by 0.3 pp (to 8.4% per annum) and hovered around this level until the end of the quarter. The rate on 3-month hryvnia deposits decreased by 0.6 pp in Q1, slightly widening the interest rate spread between these and one-year deposits. Rates on 12-month dollar deposits fell by 0.4 pp (to 1.0% per annum).

Figure 36. Ukrainian Index of Retail Deposit Rates for hryvnia deposits, % per annum*



* Thomson Reuters data, 5-day moving average.

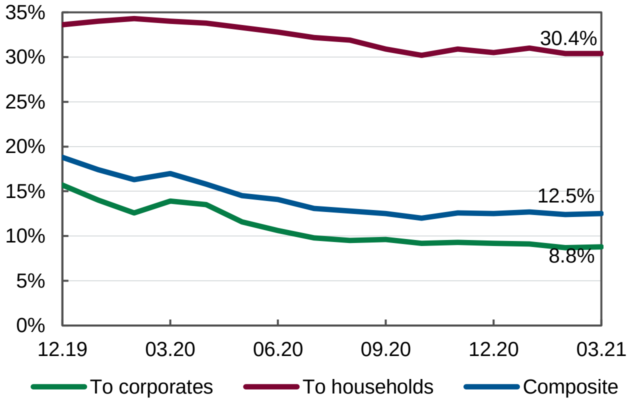
Figure 37. Ukrainian Index of Retail Deposit Rates for US dollar deposits, % per annum*



* Thomson Reuters data, 5-day moving average.

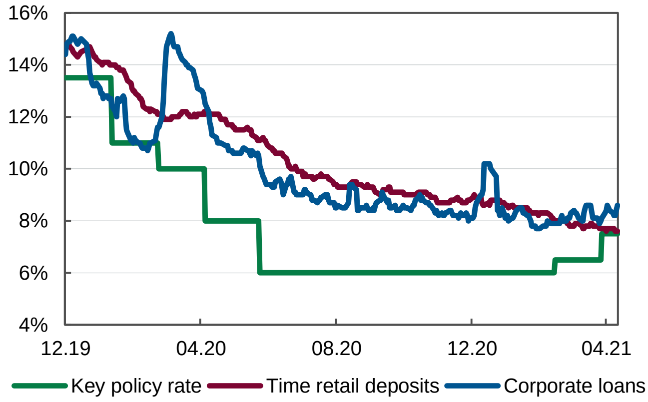
Interest rates on hryvnia corporate loans decreased by 0.4 pp in Q1 (to 8.8% per annum). Retail deposit rates were around 30% per annum.

Figure 38. Interest rates on new hryvnia loans*, % per annum



* No loan rescheduling or any other amendments to lending terms.

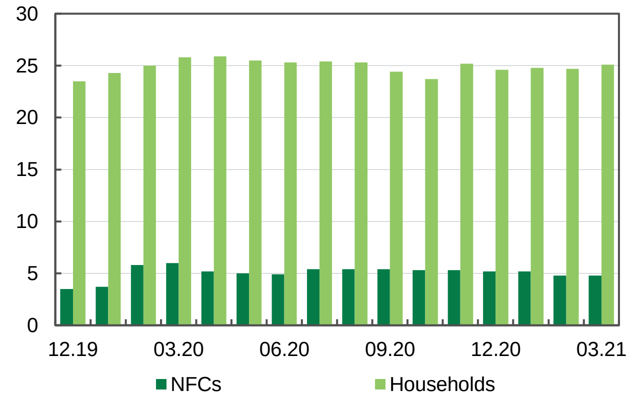
Figure 39. NBU key policy rate and interest rates on new hryvnia deposits and loans*, % per annum



* Daily rates, 5-day moving average.

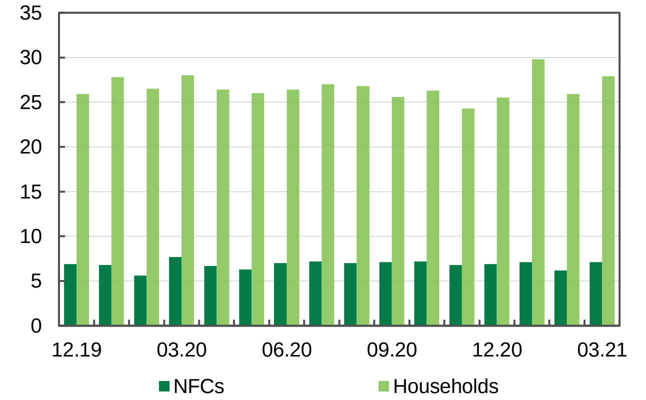
The interest rate spread between new loans and deposits was little changed due to divergent dynamics in the corporate and retail segments. At the same time, the spread between outstanding loans and deposits increased.

Figure 40. Spread between rates on new** loans and deposits, pp*



* Including insolvent banks.
** New loans and deposits include amounts under primary agreements that were entered into during the reporting period, as well as those under addendum agreements that changed either the amount or interest rate.

Figure 41. Spread between rates on outstanding loans and deposits, pp*

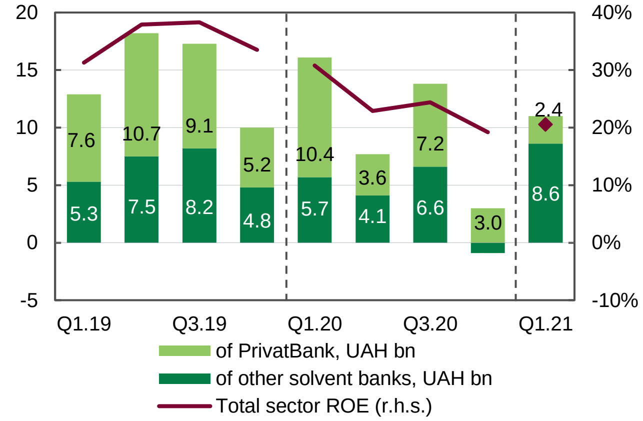


* Including insolvent banks.

Financial Results and Capital

In Q1, the sector's profits fell by 32.2% yoy, primarily due to a decrease in operating income.

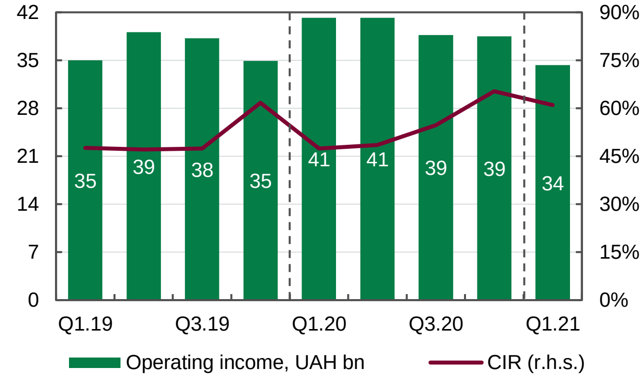
Figure 42. Profit/loss* and return on equity of banks



* Quarterly data, including adjusting entries.

The banks' operating efficiency worsened in Q1: the CIR* stood at 61.0%, up from 47.4% last year.

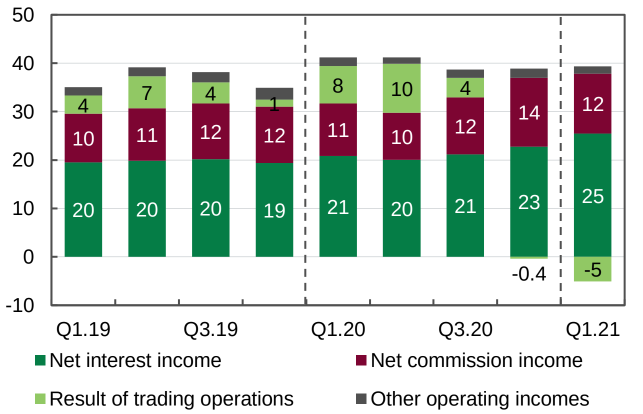
Figure 43. Operating income and operational efficiency of banks



* The CIR (cost-to-income ratio) measures the ratio of operating expenses to operating income.

Operating income fell by 16.8% yoy due to losses from the revaluation of securities, although interest and commission income went up.

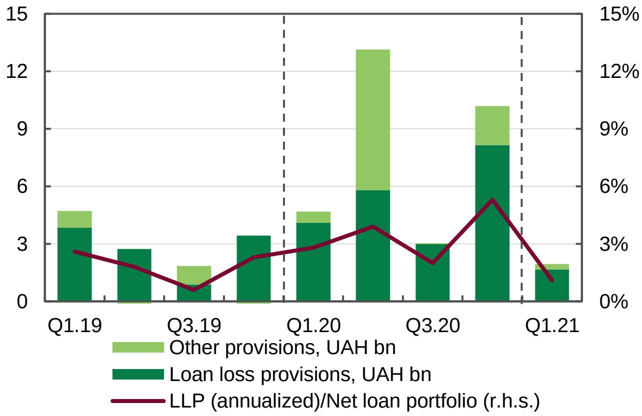
Figure 44. The banks' operating income components for the period*, UAH billions



* Including adjusted entries.

The banks' provisioning decreased by 58.3% yoy.

Figure 45. Loan loss provisions (LLP)*



* Annualized, including adjusted entries.

Since the start of the year, regulatory capital has decreased by 1.9%, in particular in state-owned banks, while authorized capital has remained almost unchanged (+0.02%). The sector's overall capital adequacy remained significantly above the required minimum.

Figure 46. Regulatory capital and the regulatory capital adequacy ratio

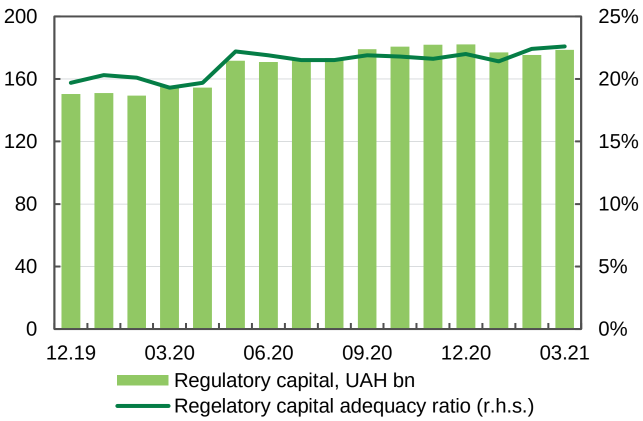
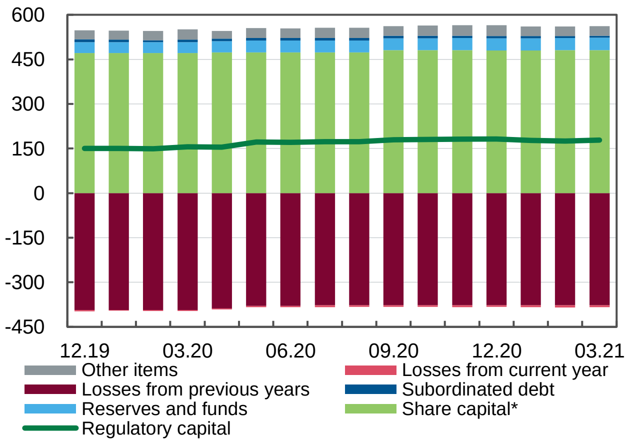


Figure 47. Banks' regulatory capital, UAH billion



* Registered and unregistered authorized capital.

Table 2. **Key banking sector indicators** [1]

	2014	2015	2016	2017	2018	2019	2020	Q1 2021
Number of operating banks	145	117	96	82	77	75	73	73
General balance sheet indicators (UAH billion)[2]								
Total assets	1 477	1 571	1 737	1 840	1 911	1 982	2 206	2 214
of which in foreign currency	667	800	788	755	779	718	746	740
Net assets	1 290	1 254	1 256	1 334	1 360	1 493	1 823	1 836
of which in foreign currency	565	582	519	507	495	492	585	585
Gross corporate loans[3]	820	831	847	864	919	822	749	751
of which in foreign currency	400	492	437	423	460	381	332	320
Net corporate loans[3]	710	614	477	451	472	415	432	439
Gross retail loans	208	176	157	171	197	207	200	206
of which in foreign currency	101	97	83	68	61	38	31	29
Net retail loans	144	96	76	92	114	143	149	157
Corporate deposits[3]	283	349	413	427	430	525	681	683
of which in foreign currency	114	141	177	163	150	191	233	244
Retail deposits[4]	403	402	437	478	508	552	682	688
of which in foreign currency	214	215	239	244	241	238	285	281
Change (yoy, %)								
Total assets	4.8%	6.4%	10.6%	5.9%	3.8%	3.7%	11.3%	5.7%
Net assets	1.0%	-2.8%	0.2%	6.2%	1.9%	9.8%	22.1%	17.3%
Gross corporate loans[3]	12.8%	1.3%	2.0%	2.0%	6.3%	-10.6%	-8.8%	-15.2%
Gross retail loans	10.3%	-15.7%	-10.4%	8.5%	15.3%	5.0%	-3.5%	-5.8%
Corporate deposits[3]	9.5%	23.5%	18.2%	3.4%	0.8%	22.1%	29.7%	25.4%
Retail deposits[4]	-8.9%	-0.3%	8.7%	9.4%	6.3%	8.6%	23.5%	12.7%
Penetration[5] (%)								
Gross corporate loans[3] / GDP	51.7%	41.8%	35.5%	29.0%	25.8%	20.7%	17.9%	17.2%
Net corporate loans[3] / GDP	44.7%	30.9%	20.0%	15.1%	13.3%	10.4%	10.3%	10.0%
Gross retail loans/ GDP	13.1%	8.8%	6.6%	5.7%	5.5%	5.2%	4.8%	4.7%
Net retail loans/ GDP	9.1%	4.8%	3.2%	3.1%	3.2%	3.6%	3.5%	3.6%
Corporate deposits[3] / GDP	17.8%	17.6%	17.3%	14.3%	12.1%	13.2%	16.2%	15.6%
Retail deposits/ GDP	25.4%	20.2%	18.3%	16.0%	14.3%	13.9%	16.3%	15.7%
Profit or Loss[6] (UAH billion)								
Net interest income	52.2	39.1	44.2	53.0	73.0	78.9	84.8	25.4
Net commission income	23.1	22.6	24.2	27.5	37.8	44.0	46.5	12.4
Provisions	84.4	114.5	198.3	49.2	23.8	10.7	31.0	2.0
Net profit/loss	-33.1	-66.6	-159.4	-26.5	22.3	58.4	39.7	10.9
Memo items:								
UAH/USD (period average)	11.89	21.84	25.55	26.60	27.20	25.85	26.96	27.97
UAH/USD (end-of-period)	15.77	24.00	27.19	28.07	27.69	23.69	28.27	27.89
UAH/EUR (period average)	15.72	24.23	28.29	30.00	32.14	28.95	30.79	33.76
UAH/EUR (end-of-period)	19.23	26.22	28.42	33.50	31.71	26.42	34.74	32.72

[1] Data for solvent banks for each reporting date.

[2] Including accrued income/expenses.

[3] Including non-banking financial institutions.

[4] Including certificates of deposits.

[5] GDP is calculated as defined in the 2008 national accounts system methodology. From 2008 through 2013 it includes data for the temporarily occupied Republic of Crimea and City of Sevastopol; from 2014 it excludes data for the temporarily occupied Autonomous Republic of Crimea and City of Sevastopol and a part of the ATO zone.

Data for Q1 2021 – readings for the last 12 month based on NBU forecast as published in Inflation Report.

[6] Taking into consideration adjustment entries, except for the Q4 2020 data.

Remarks:

The source for the data is the National Bank of Ukraine, unless otherwise noted.

The sample of banks consists of the banks that were solvent at each reporting date, unless otherwise stated.

The sample of banks that were solvent as of the last reporting date includes those banks that merged with other banks using a simplified procedure.

Groups of banks for 2017 were formed pursuant to NBU Board Decision No. 76-D, dated 10 February 2017. Data for 2018 and beyond were prepared pursuant to Decision No. 444 by the Committee on Banking Regulation and Supervision, dated 29 December 2017.

State-owned banks are Ukrainian banks with public capital excluding PrivatBank, unless otherwise specified.

Foreign banks are banks where the share of capital owned by at least one foreign investor (including foreign states) is no less than 10 percent.

Private banks are banks whose qualifying holders are exclusively residents of Ukraine.

The data include accrued interest as of the end of the period (month, quarter, year), unless otherwise specified.

Gross loans are loans not adjusted for provisions against asset-side banking transactions.

"Fixed-exchange-rate-based change" refers to the foreign-currency sum of an instrument being calculated using the exchange rate at the beginning of the period.

Data on corporate loans and deposits include data on nonbank financial institutions.

Retail deposits include certificates of deposit, unless otherwise specified.

The sum of individual components and the total may differ due to rounding.

Terms and Abbreviations:

ATM	Automated teller machine / cash dispenser
CIR	Cost-to-Income Ratio
FX	Foreign currency
GDP	Gross domestic product
HHI	Herfindahl-Hirschman Index
IFI	International financial institution
NBU	National Bank of Ukraine
NFC	Non-financial corporation
NPL / NPE	Non-performing loan / non-performing exposures
NSFR	Net stable funding ratio
POS	Point of sale
T-bond	Domestic government debt securities and debt securities refinanced by the NBU, which are carried at (1) fair value through profit or loss, (2) fair value through other comprehensive income, and (3) amortized cost.
PJSC	Public Joint Stock Company
ROE	Return on equity
UIRD	Ukrainian Index of Retail Deposit Rates
pp	Percentage point
EUR	Euro
UAH	Ukrainian Hryvnia
USD, US dollar	United States dollar
M	Month
Q	Quarter
bn	Billion
r.h.s.	right-hand scale
qoq	Quarter-on-quarter
yoy	year-on-year