



National Bank
of Ukraine

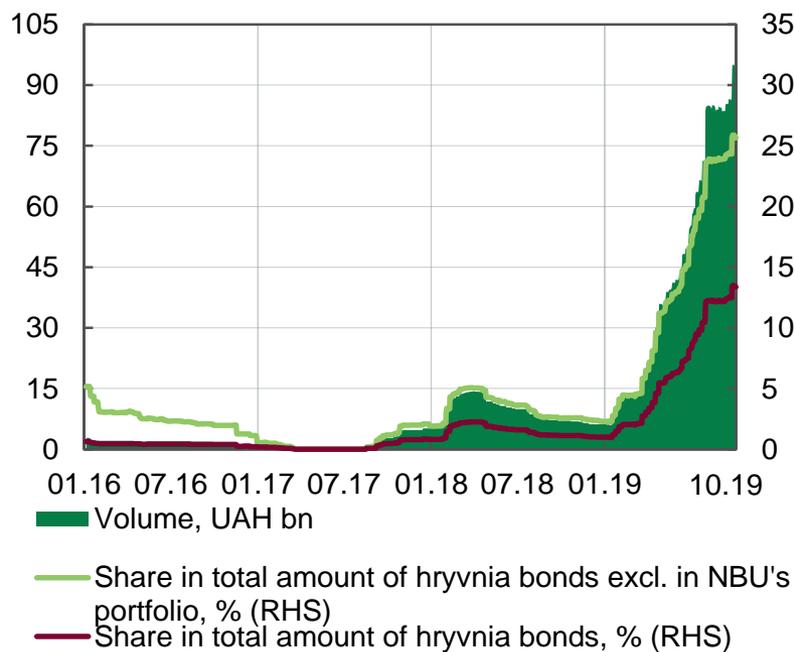
UAH appreciation: reasons and policy options

Dmytro Sologub
Deputy Governor
Kyiv, 09 October 2019



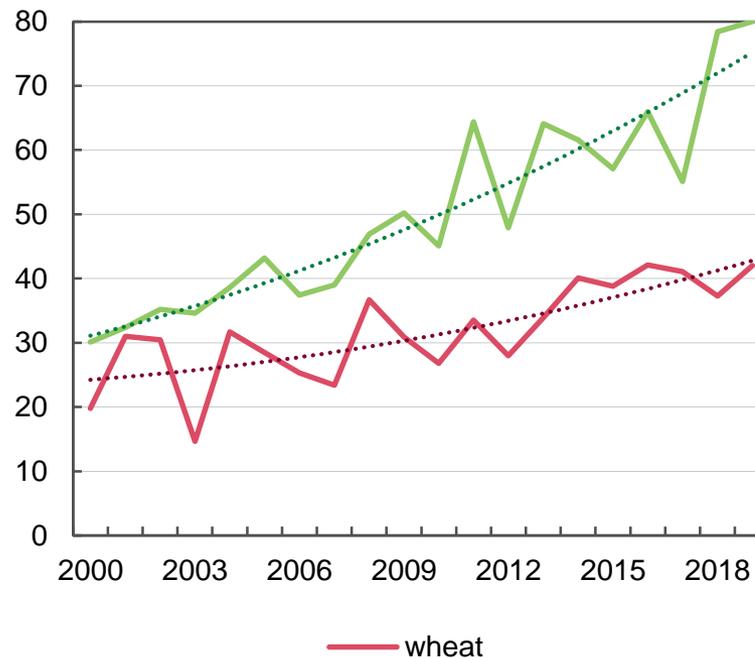
The reasons for UAH appreciation

Hryvnia Domestic Government Bonds Held by Non-Residents



Source: NBU.

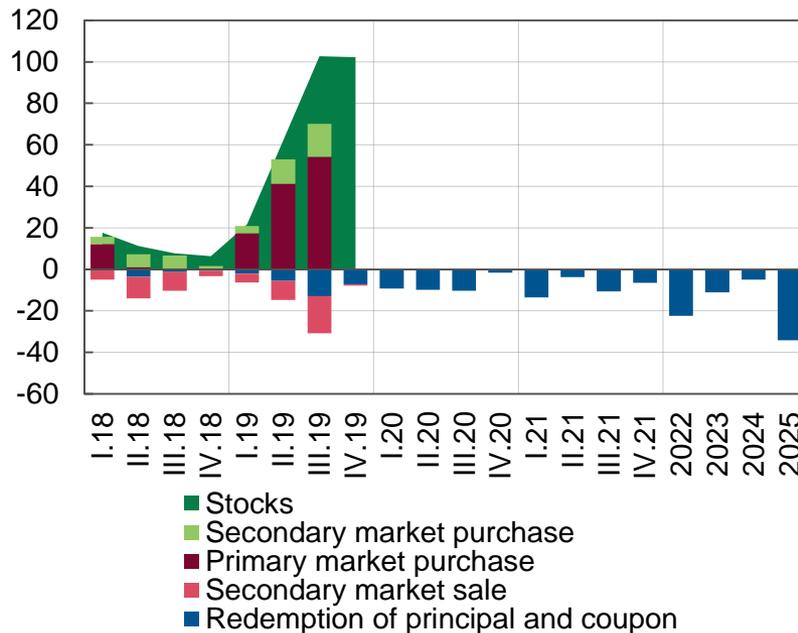
Wheat and corn yields in Ukraine, centers/ha



Data for 2019 – NBU estimate.
Source: SSSU.

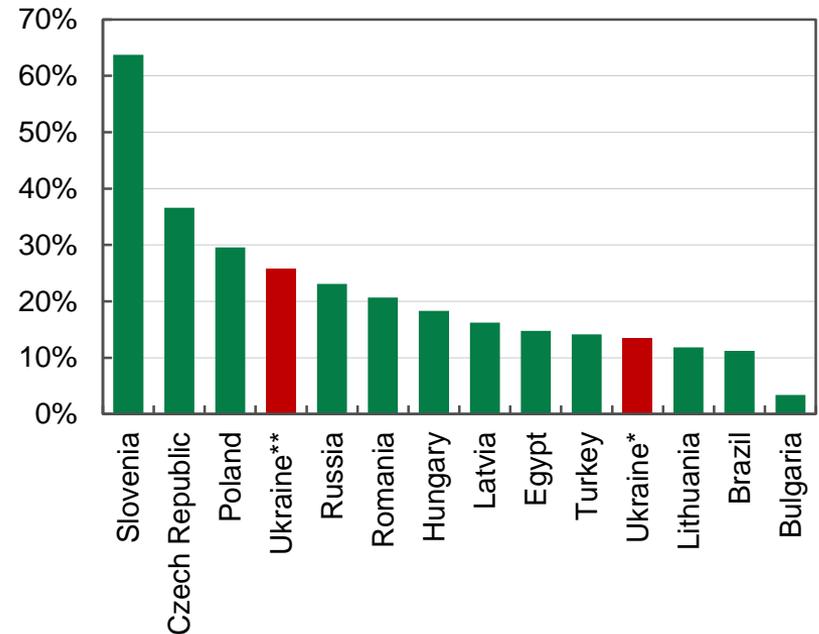
(?) UAH appreciation is unsustainable because of ... short term nature of capital inflows

Non-resident Operations with Domestic Government Bonds and its Scheduled Redemption*, bn UAH



*As of 04.10.2019.
Source: NBU.

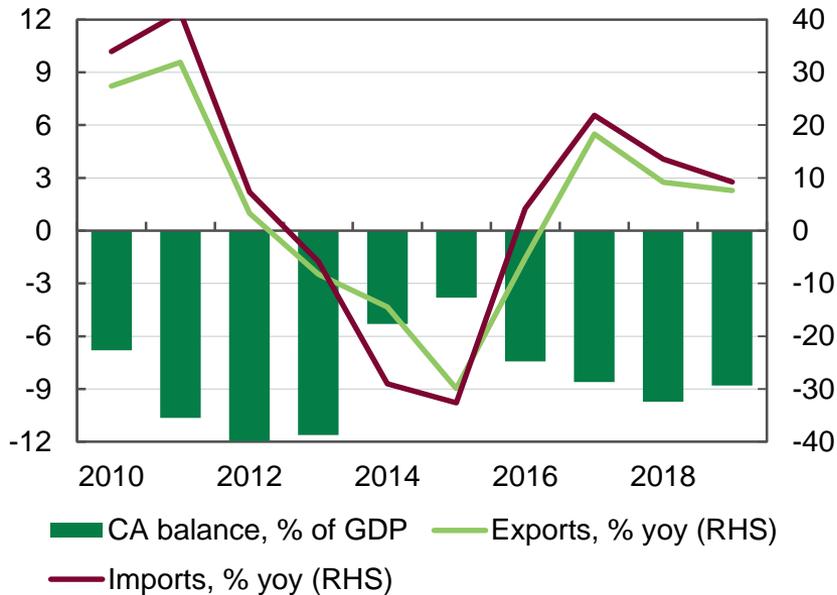
Non-residents share in Government Bonds in Local Currency in 2018, % eop



* Jan-Sep 2019; ** excluding NBU holdings of government bonds
Source: NBU, IMF.

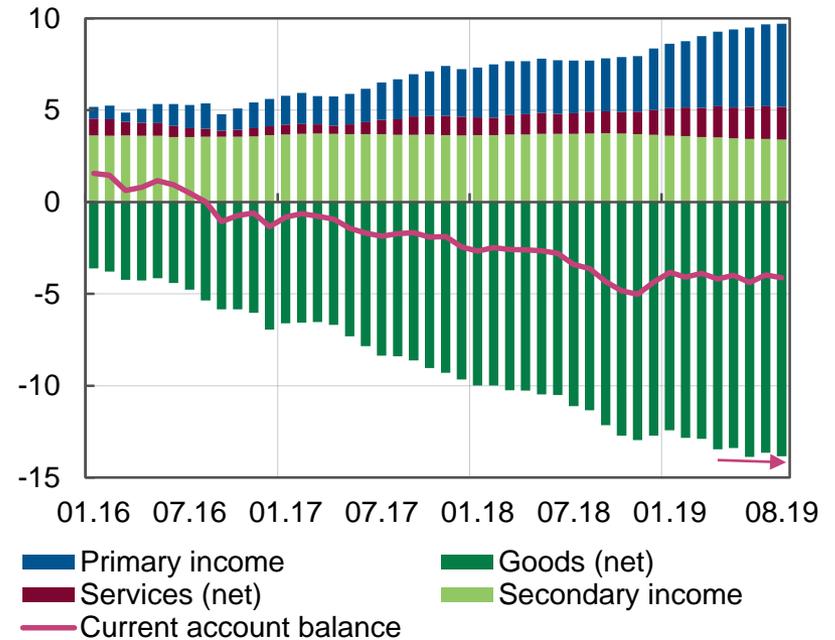
(?) UAH appreciation is unsustainable because of ... external position deterioration (1)

Merchandise trade balance indicators



Source: NBU, SSSU.

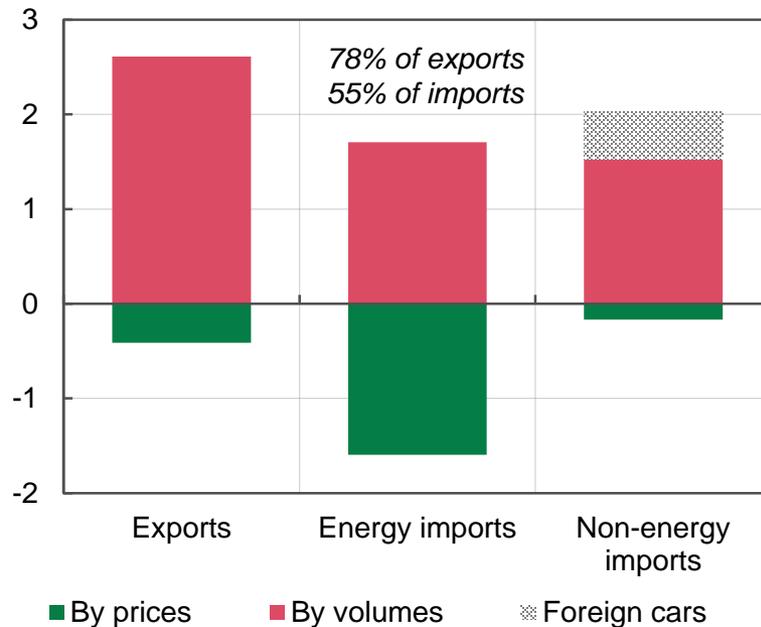
Current account, USD bn, 12-month rolling



Source: NBU.

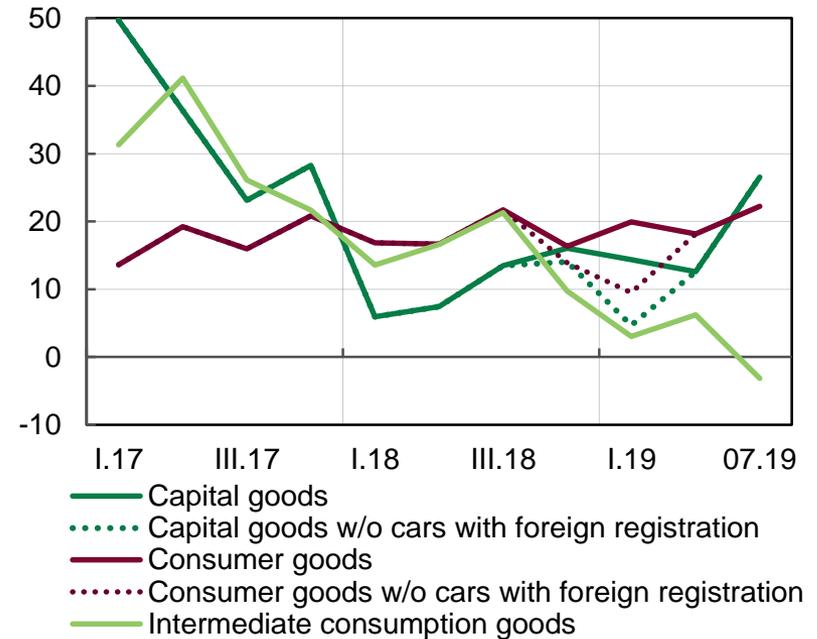
(?) UAH appreciation is unsustainable because of ... external position deterioration (2)

Absolute annual change of selected trade indicators, Jan-Aug 2019, USD bn



Source: NBU, SSSU.

Imports by BEC, % yoy



Source: Ukrautoprom, NBU calculations.

Capital inflows into government bonds: concerns

Risks associated with hot capital inflows

- Vulnerability to capital sudden stops
 - accumulation of international reserves and de-dollarization of government debt minimize the risks
- Overvaluation of exchange rate and widening current account deficit
 - however CAB is close to the norm, floating ER prevents large misalignments
- Overheating demand and inflation
 - capital flows into public sector
- Fiscal expansion
 - unlikely as government financing sources are constrained

Capital inflows into government bonds: possible policy options

Pros	Cons
Increase purchases of FX and prevent further UAH appreciation	
<ul style="list-style-type: none">• increase reserves buffer	<ul style="list-style-type: none">• inconsistent with IT: one-sided ER fluctuations (allowing only devaluation) will harm credibility and de-anchor expectations• could stimulate even more capital and attack on peg• inflationary pressure
Emergency key rate cut despite concerns over inflation	
<ul style="list-style-type: none">• could prevent further inflows and reduce costs for MinFin	<ul style="list-style-type: none">• inconsistent with IT and undermines NBU`s credibility• might provoke outflows
Capital controls	
? not applicable as capital flows into government debt	

Capital inflows into government bonds: policy reaction consistent with proclaimed strategy

NBU Monetary policy strategy

“ ...the NBU shall consider achievement and maintenance of price stability in the country to be its priority...

...

The NBU will remain committed to the floating exchange rate regime, meaning that it will not use monetary policy to achieve a certain level or the band of exchange rate.”

In current circumstances that mean \Rightarrow continue balanced mix of UAH appreciation and FX accumulation

Results: enhanced credibility to inflation target

- ✓ de-anchoring inflation expectations and exchange rate
- ✓ de-dollarization
- ✓ extension of debt maturities and lower yields
- ✓ increase of salaries in USD terms – tamed labor migration