National Bank of Ukraine

Financial Stability Report

June 2025

The Financial Stability Report (FSR) is a key publication of the National Bank of Ukraine (NBU). It aims to provide information about existing and potential risks that might undermine the stability of Ukraine's financial system. The report focuses on the risks that Ukraine's financial sector and economy face amid the protracted full-scale war. The FSR also provides authorities and financial institutions with recommendations for mitigating wartime risks and enhancing financial system's resilience against these risks.

The report is primarily aimed at financial market participants, and all those interested in financial stability issues. The publication of the report promotes the transparency and predictability of macroprudential policy, helps to boost public confidence in this policy, and thus facilitates the NBU's management of systemic risks.

The Financial Stability Committee of the NBU approved this report on 12 June 2025.

Content

Summary

Economic conditions remained favorable for the banks in H1 2025. Key indicators of the banking system's resilience – capital adequacy, liquidity, profitability, and loan quality – were high by historical standards. As a result, bank lending to businesses and households has been growing: competition for prime borrowers is high, making loans more affordable for the economy. The continuation of the war remains the key risk to the financial sector and restrains economic recovery.

Economic growth continues to be driven primarily by robust consumer demand. However, the recovery is constrained by a shortage of labor, as the unemployment rate has almost returned to "pre-war" levels, and the labor force is recovering very slowly. The production capacity limitations are having an increasing effect, as expansion of the facilities is constrained by high security risks. Investments are primarily being made to strengthen Ukraine's defense capabilities and energy efficiency – the banks are taking an active part in their financing.

The ongoing hostilities are limiting the room for fiscal consolidation and reduction of the external-accounts deficit. Therefore, financial support from international partners is one of the key prerequisites for macroeconomic and financial stability. External support maintains international reserves at all-time highs, enabling the NBU to ensure the proper functioning of the FX market. This year, the inflow of grants and loans remains at an acceptable level, in particular thanks to the ERA mechanism, which was launched at the end of last year. The timeliness of financing depends on the full and timely fulfillment of commitments to partners, primarily under the IMF program and the Ukraine Facility. Ukraine will still need significant injections of additional financial resources to support defense and post-war reconstruction, and the confiscation of immobilized russian assets may be a source of such resources.

Despite depressed production volumes, businesses' revenues grew on the back of higher prices. Businesses have maintained solid financial performance and creditworthiness and thus remained sought-after clients for the banks. The growth in real household income is slowing, but consumer demand remains strong, supporting demand for banking products. However, lending continues to play only a moderate role in household consumption.

In April, the annual growth rates in the net portfolio of hryvnia loans to households and businesses reached 34% and 29%, respectively, so loan penetration relative to GDP is rising. The banks of all groups are building up their portfolios. Financial institutions are actively competing for clients by improving the quality of their services and maintaining interest rates at moderate levels. Lending has been revived by the measures taken under *the Lending Development Strategy*. At the end of the year, the government implemented the program to finance defense companies that was envisaged by the strategy. A number of strategy measures have been taken to revive lending to the energy sector, and the banks have signed a memorandum to that effect. Construction of about 700 MW of power generation capacities was financed over the year. In addition, the banks are ready to offer syndicated loans – such products are not yet widespread, but their average size is significant. By preserving prudent lending standards, the banks are ensuring that the quality of the new loan portfolio is high.

The role of state support in corporate lending is declining: subsidized loans account for less than a third of outstanding hryvnia loans. Further narrowing of the areas of state support will increase its effectiveness. On the other hand, state-supported mortgages account for over 95%. Ukrfinzhytlo's ability to increase the volume of subsidized mortgage loans under the *eOselia* program solely with its own liquidity is limited. Scaling up mortgage programs requires greater reliance on the liquidity currently available to the banks. The development of mortgages also requires a number of infrastructure changes, such as better regulation of developers, greater transparency in the housing market, and improved market statistics. The NBU, together with other institutions, is finalizing the *Mortgage Lending Development Strategy*, which will set the timelines for such changes.

Increased inflationary pressures and accelerating consumer price growth prompted the NBU to launch a cycle of key policy rate hikes at the end of last year. Additionally, the NBU adjusted the operational design of its monetary policy, increasing the premium for bank investments in

3-month certificates of deposit – access to which is determined by how actively banks attract term deposits. Market rates increased in response to these changes: quicker for corporate deposits, and somewhat more slowly for retail deposits and loans. As a result, the banks' asset yields remained almost unchanged, while funding became more expensive. These changes slightly reduced the banks' net interest margin. As inflationary pressures ease, market rates are expected to move down, which will increase pressure on net interest margin due to lower asset yields. The banks should take these risks into account when planning their asset structure and rely more on instruments with more stable yields, such as loans.

The banks' losses from operational risk remain high, although they have decreased compared to the losses they incurred in the first years of the full-scale invasion. The three-and-a-half years of full-scale war have shown how much the banks can lose from operational risk events under severe adverse scenarios. Taking into account the information received, the NBU may adjust the calculation of the capital requirement for covering operational risk, harmonizing it with the EU approach. This will free up some of the banks' capital.

The operational efficiency of the banking system is consistently high. The banks continue to use their net profits to replenish capital. The capital cushion is currently contributing to the growth in lending. However, the repeated retroactive application of the windfall tax rate creates great uncertainty in the banks' capital planning and may reduce their appetite for credit and market risks going forward.

The NBU has started the scheduled annual banks' resilience assessment. The asset quality review – the first stage of the resilience assessment – has been already completed, confirming that the banks' overall assessments of their credit risks are correct. The next stage is now underway – stress testing to assess the banks' resilience to hypothetical external shocks. Based on the results of the resilience assessment, the NBU may set higher capital requirements for certain banks. These financial institutions will be required to draw up capitalization or restructuring programs and fulfill them by the end of the year. The resilience assessment will also make it possible to determine an optimal schedule for implementing capital buffers. The size of two of the buffers – capital conservation and systemic importance buffers – is clearly set out in the EU regulatory requirements and will be replicated for Ukrainian banks. Another buffer – the countercyclical buffer – requires regular updates and justification of its level after its introduction. To regularly assess the target size of the countercyclical capital buffer, the NBU is starting to calculate the financial cycle index. Its current values indicate that a macroprudential response is not needed at this phase of the financial cycle.

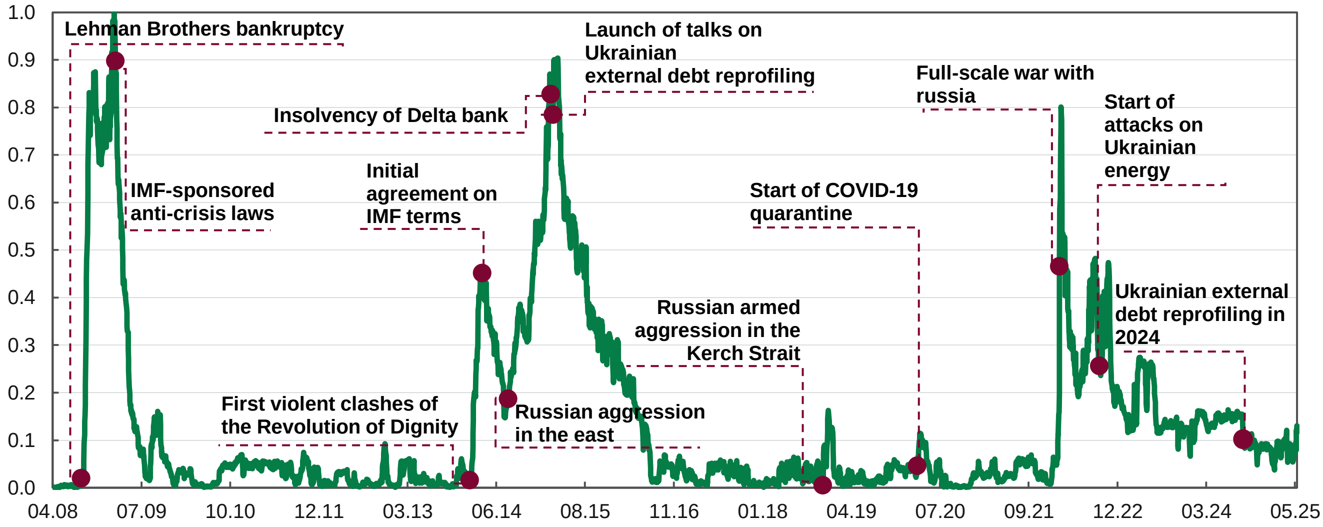
The NBU continues to harmonize its regulatory framework and supervisory practices for the banks and non-bank institutions with EU standards. The next steps in banking regulation include the introduction of the leverage ratio and updating the requirements for covering credit risk with capital, as well as the introduction of settlement and credit valuation adjustment risk components. Another parallel goal for the NBU is to obtain the status of the equivalent third country in terms of the banking regulatory and supervisory framework from the European Commission. This status will facilitate more active lending by Ukrainian subsidiaries of European banks. The NBU expects to move closer to commencing the formal equivalence assessment process within a year.

Financial Stress Index

In H1, the Financial Stress Index (FSI) was at its lowest level since the onset of the full-scale invasion, although it was volatile. The FX sub-index remained the largest contributor to the FSI, although declining slightly compared to the start of the year – primarily due to a decrease in FX interventions. The main source of volatility in the FSI was the government debt sub-index, which fluctuated due to sharp changes in sovereign Eurobond spreads. It has increased slightly compared to the start of the year. The value of the household behavior sub-index was little changed, primarily due to deposit rates remaining relatively high. The corporate sub-index rose temporarily due to fluctuations in the share prices of Ukrainian companies, driven by changes in expectations about the success of peace talks. However, it returned to its minimum values in early summer. The banking sub-index remained low despite a slight decline in liquidity in the spring.

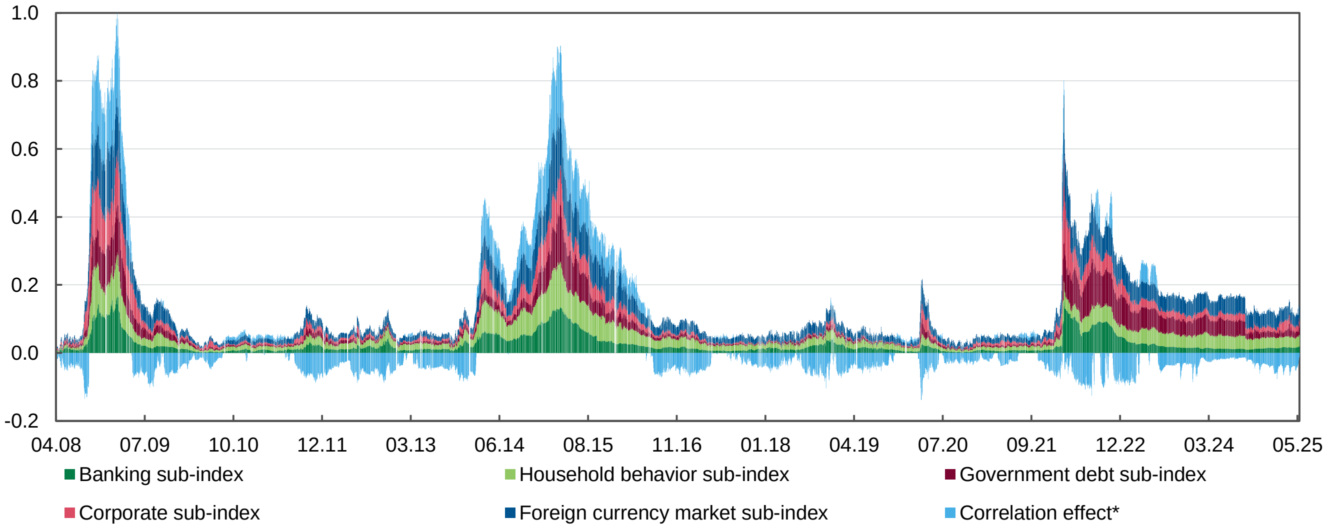
The FSI reflects only the current condition of the financial sector and does not signal future risks that may arise over the short or long term.

Figure FSI1. **Financial Stress Index**



Source: NBU.

Figure FSI2. **Financial Stress Index decomposition**



* The correlation effect is the contribution of the current correlation between sub-indexes compared to the average over the entire observation period.

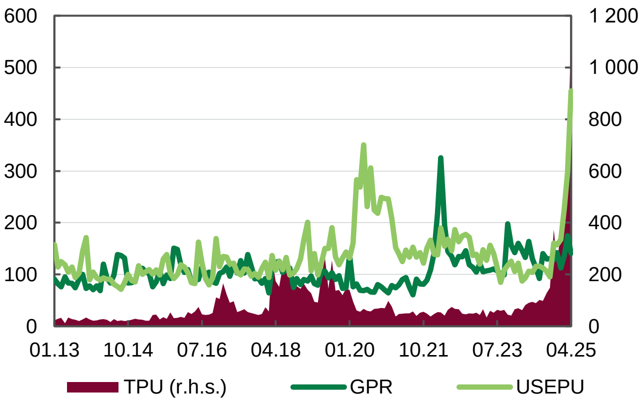
Source: NBU.

Part 1. External Conditions and Risks

1.1. External Developments

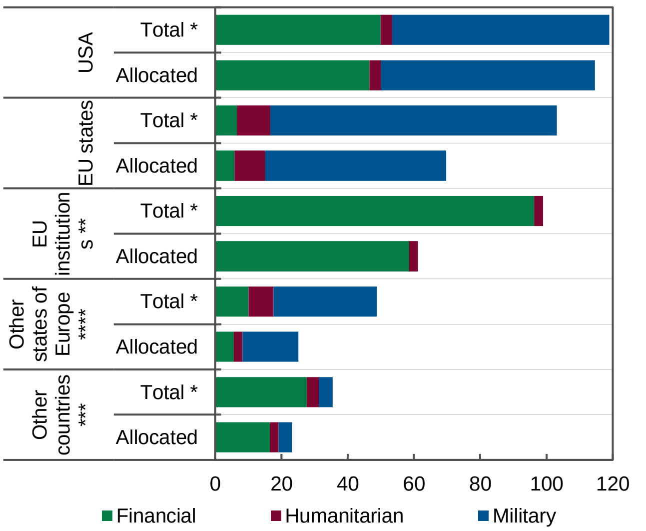
International efforts to establish peace have not yet yielded the results Ukraine wants. International financial support for Ukraine will be sufficient this year if it is disbursed as planned. Europe's role in financial and military assistance is increasing. Ukraine continues to move toward European integration. The change in the U.S. foreign policy stance has sharply increased uncertainty and protectionism in international trade. This makes the further course of international economic relations unpredictable. As a result, the economies of partner countries are growing more slowly than expected. This may divert partners' resources from supporting Ukraine. However, the direct impact of international trade confrontations on Ukrainian exports will be limited, as will the restoration of EU customs quotas, primarily on agricultural products. The terms of trade will remain favorable.

Figure 1.1.1. Indices of Geopolitical Risk Index (GPR), U.S. economic policy uncertainty (USEPU), and global trade policy uncertainty (TPU)



Source: Dario Caldara and Matteo Iacoviello https://www.matteoiacoviello.com/gpr.htm; Scott Baker, Nicholas Bloom and Steven J. Davis www.PolicyUncertainty.com.

Figure 1.1.2. Committed official assistance for Ukraine from January 2022 through April 2025, EUR billions



* All commitments, including disbursed ones. ** European Commission, EU Council, and European Investment Bank. ***Australia, Canada, New Zealand, South Korea, Taibei, Turkiye, and Japan. **** United Kingdom, Iceland, Norway, and Switzerland.

Source: Kiel Institute for World Economy.

Attempts to achieve peace continue

In May, negotiations started on ensuring peace in Ukraine. International partners are continuing to support Ukraine in achieving peace. So far, the success of these efforts has been limited, primarily because of the enemy's reluctance to end the war. In addition, there is a lack of unanimity on the part of the free world countries over ways to force the aggressor to make peace. The outlines of future security guarantees for Ukraine are also unclear. At present, there is clarity only about the terms of a range of bilateral security agreements that have already been concluded.

Despite the attempts to negotiate, the enemy is not easing up on ground attacks and continues its aerial terror. The frontline is now relatively stable thanks to the efforts of the defense forces, but the situation remains difficult. At the same time, military innovations and the development of the national defense complex are yielding noticeable results. A number of successful operations by the defense forces are helping to weaken the military potential and deter the enemy.

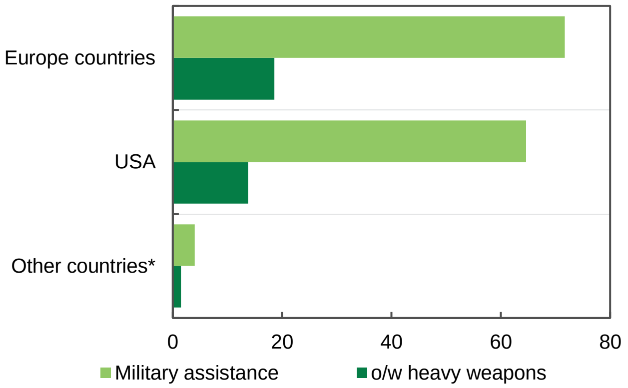
Global geopolitical tensions are also growing. The economic – and sometimes military – confrontation between traditional adversaries has intensified since the start of the year. As a result of trade wars, new lines of economic division have emerged between states and groups of states that had been allies for many years. The U.S. tariff policy and changes in its foreign policy make further international economic relations unpredictable. This undermines the system of international agreements and may also divert the resources of partner countries from supporting Ukraine.

The EU, together with the UK, has launched an important program to rearm Europe (SAFE) and is creating a trust fund worth EUR 150 billion. The fund will, among other things, allow for the purchase of weapons for Ukraine or the financing of their production directly in the country. High-level officials of the European Commission expect that the production of weapons directly in Ukraine will allow Europe to reduce the cost of such assistance and compensate for the reduction in U.S. aid. In total, the EU and the U.S. have annually provided Ukraine with military assistance worth about EUR 40 billion.

The role of European financial assistance is growing

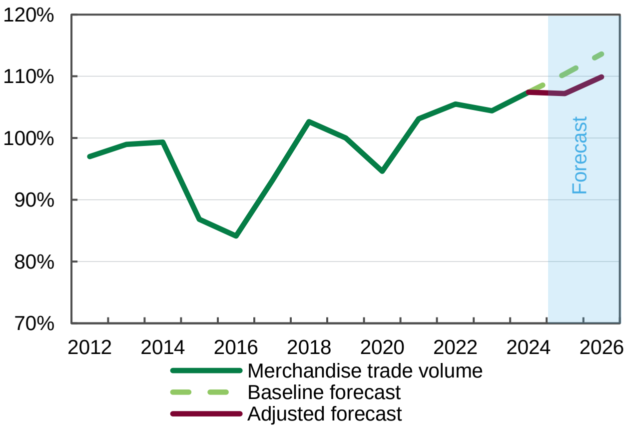
International financial support for Ukraine slated for this year allows the country to count on the proper execution of the state budget. To ensure timely inflows of funds, part of the

Figure 1.1.3. Military assistance to Ukraine from January 2022 through April 2025, EUR billions



Military assistance includes financing tied to military purposes. Heavy weapons are estimates that do not include ammunition of any kind, smaller arms or equipment.
* Canada, Australia, Turkiye, Japan, New Zealand, and South Korea.
Source: Kiel Institute for World Economy.

Figure 1.1.4. Global merchandise trade*, 2019 = 100%



* Export and import average. Baseline WTO forecast of early 2025, adjusted forecast - WTO forecast of early April 2025 adjusted for announced tariffs and increased uncertainty around global trade.
Source: WTO.

assistance envisaged for next year was also allocated this year. This year's largest donor is the EU, with an expected contribution to the budget of more than EUR 30 billion – EUR 18 billion under the ERA program (Extraordinary Revenue Acceleration based on income from immobilized russian assets), and EUR 12.5 billion under the Ukraine Facility. Cooperation with the IMF remains the benchmark for Ukraine's reform implementation. As a result of the eighth review of the current program, a staff level agreement was reached with the IMF. The program is to run until the end of March 2027. Its successful implementation is a key part of an international assistance package amounting to almost USD 149 billion. Overall, since the onset of the full-scale war, the budget has already received more than USD 133 billion in international financing. Ukraine will continue to need the support of the IMF and other partners. The most effective step would be a decision to confiscate russian assets in favor of Ukraine. The G7 statement that russia's assets will remain immobilized until russia ends its aggression and pays compensation to Ukraine is a positive signal.

The European integration progress is rapid

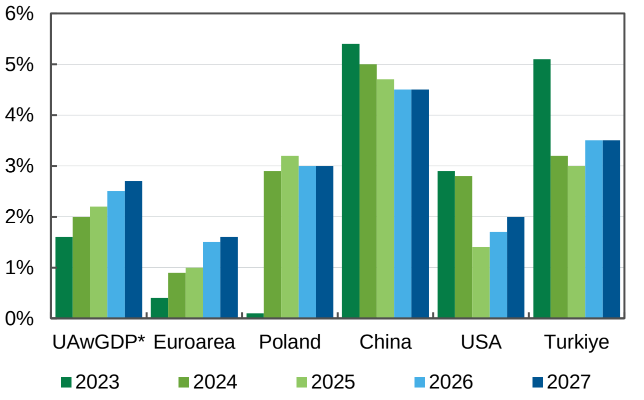
To date, Ukraine has already completed the screening of legislation in four of the six clusters (1 – Fundamentals, 2 – Internal Market, 3 – Competitiveness and Inclusive Growth, and 6 – External Relations). The screening is expected to be completed this year. In order to open negotiations on the screened clusters, it is necessary to overcome blocking by one of the EU countries. The list and schedule of implementation of EU regulations by Ukraine will be agreed upon at the start of the negotiations. However, Ukraine is continuing to implement previously planned legislative and regulatory reforms based on EU acquis.

Growth in partner countries will continue despite higher uncertainty

The intensification of trade tensions has slowed the global economy and increased risks to its development. According to the NBU's baseline forecast, the growth rates of the economies of a number of partner countries will be comparable to 2024, but will be lower than expected at the start of the year. The Euroarea's real GDP will increase by 1%, compared to +0.9% last year, although the January forecast was +1.4%. U.S. growth may slow compared to 2024 as a result of the trade confrontation. Its impact will also affect China's economy. Trade and geopolitical confrontation significantly increase risks in the medium term.

According to the World Trade Organization, the global merchandise trade will decline by 0.2% this year, as opposed to the previously expected growth of 2.7%. The full implementation of tariffs by the United States and the announced reciprocal measures will deepen the decline in global trade. The level of global trade uncertainty has thus reached record levels over the period when the indicator was measured. At the same time, U.S. tariffs will have a limited impact on Ukraine's trade due to the small share of the United States in its volumes and the partial reorientation of exports to other markets.

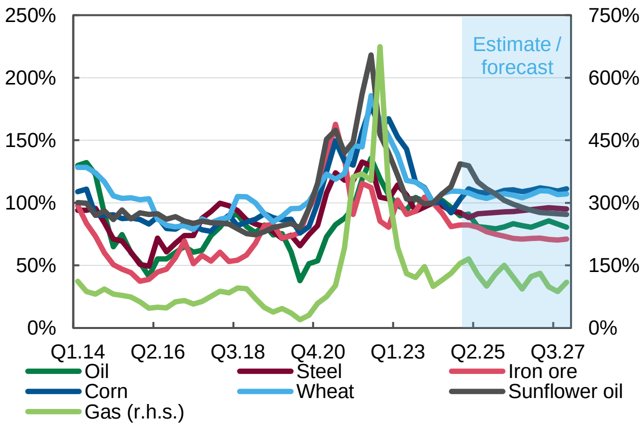
Figure 1.1.5. Change in real GDP of Ukraine's main trading partners, % yoy



2026, 2027 – forecast.
* Weighed average indicator of economic growth of Ukraine's main trading partners.

Source: NBU Inflation Report, April 2025.

Figure 1.1.6. Global commodity prices, Q1 2024 = 100%



Brent crude oil; natural gas at Netherlands Title Transfer Facility (TTF); steel billet Exp FOB Ukraine; China import Iron Ore Fines 62% FE spot; European wheat prices; average global quarterly prices for sunflower oil and corn.

Source: NBU Inflation Report, April 2025.

Barriers to international trade are increasing inflationary pressures in many advanced economies. This could lead to a more cautious stance by some leading central banks and a halt to interest rate cuts in financial markets. This will not have a direct impact on Ukraine but will make it more difficult for emerging markets to raise funds.

Sanctions are holding back russia's economy, but the prospects for their tightening are uncertain

New European sanctions against the aggressor country primarily target banking and energy sectors and limit opportunities for bypassing previous oil trade restrictions. According to the IMF's baseline forecast, russia's economic growth will slow sharply due to a decline in private investment and consumption; fiscal imbalances continue to accumulate. However, intensive military spending enables the aggressor state to avoid a recession, and it is managing to circumvent restrictions by using loopholes in sanctions policy. Therefore, sanctions and monitoring of their compliance should be further tightened. However, given the peculiarities of U.S. foreign policy, the prospects for introducing new sanctions and maintaining existing ones remain uncertain.

Prices for most Ukrainian exports will change only slightly

Prices for Ukrainian exports will largely remain historically high. Due to strong global demand, prices for corn and wheat will stay at their current levels, despite the expectedly high supply. At the same time, sunflower oil will gradually become cheaper due to the expected bumper harvests of sunflower and other oilseeds, including soybeans in Brazil. Iron ore prices may decline slightly as production increases, particularly in Brazil, Australia, and some other regions. Steel prices in Europe will also remain close to current levels, supported by demand from the defense sector and infrastructure. The successful functioning of the sea corridor will help to take advantage of generally favorable terms of trade.

In early June, autonomous trade measures for Ukraine, the so-called "visa-free regime for trade" introduced by the EU in 2022, expired. At the same time, in May, the European Commission adopted a set of transitional measures. These measures and a potential reorientation of trade may ease the negative impact on Ukraine's exports.

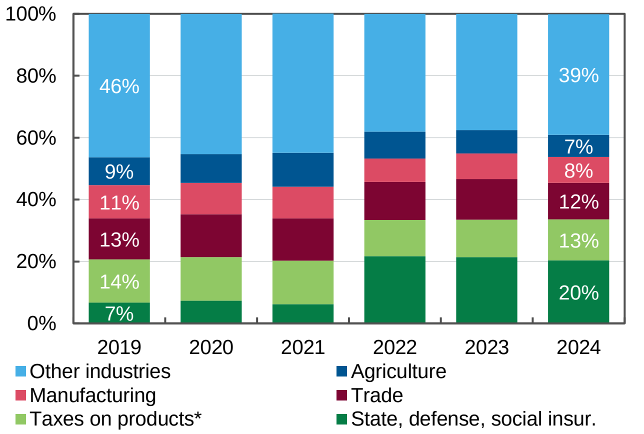
Crude oil prices will decline due to lower demand as a result of the trade confrontation, the announced increase in production by OPEC+ countries, and the simultaneous expansion of supply by countries outside the organization. Natural gas prices, on the other hand, will be volatile: in addition to traditional seasonal factors and the replenishment of gas storage facilities, the prices will be affected by a decrease in supplies from russia and Norway, an increase in liquefied natural gas imports, and the economic expectations. However, escalation of conflicts, primarily in the Middle East, may cause hikes of energy prices.

Part 2. Domestic Conditions and Risks

2.1. Macroeconomic and Fiscal Risks

This year, the pace of economic recovery will remain restrained due to the effects of the war – significant destruction and a shortage of skilled staff. Private consumer demand remains the main driver of growth. Larger inflows of assistance from partners will boost international reserves to new record highs and generate a sizeable stock of foreign currency to finance budget expenditures in 2026. The foreign trade deficit will widen, but it will not yet pose a threat due to the sufficiently high level of international support. The NBU will continue to ensure the stable operation of the FX market and offset the structural deficit in the private sector through FX interventions. In summer, inflation will start to decline. The passage of the price peak and a subsequent decline in inflationary risks will allow the central bank to move to a cycle of monetary policy easing.

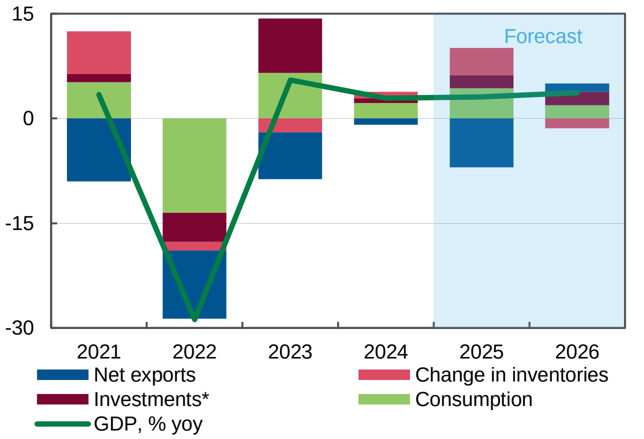
Figure 2.1.1. GDP components by production approach, in current prices



* Including subsidies on products.

Source: SSSU, NBU estimates.

Figure 2.1.2. Contributions to real GDP growth by demand components, pp



* Gross fixed capital formation.

Source: SSSU, NBU estimates.

Economic growth is moderate

According to the NBU's current forecast, real GDP will grow by 3.1% in 2025, slightly more slowly than expected at the start of the year. The economy is held back primarily by uncertainty and the protracted war. There is a significant shortage of skilled labor. Production capacity is increasingly constrained, particularly due to destruction from the war, while businesses are cautious about making capital investments to expand production. In addition, economic activity was negatively affected by the destruction of natural gas infrastructure as a result of russia's air attacks, which led to a significant decrease in production and an increase in imports of natural gas. The end of EU trade preferences and the consequences of global trade confrontations are new risks to Ukrainian exports.

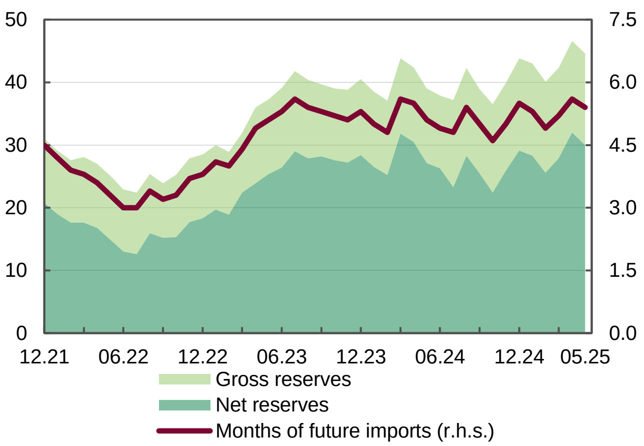
The economy remains driven by consumer demand, supported by an increase in real wages. Another factor is the continued high budgetary spending on defense, much of which is used to purchase products from domestic companies. Investment sentiment remained subdued, but the private sector continued to invest in reconstruction and energy supply during the year. The business outlook index indicates a further improvement in the forecasts for sales, investment, and the financial standing of enterprises in general. Improved business sentiment is fueling demand for loans, including for necessary investments.

Given the ongoing active hostilities, Ukraine remains critically dependent on international assistance. The potential decline in the volume of aid starting in 2026 will require substantial fiscal consolidation, which will lead to a reduction in the contribution of public consumption to GDP. To sustain economic growth, this contribution must be offset by an increase in private consumer and investment demand.

The more rapid receipt of international aid will help accumulate a record-high reserves of foreign currency

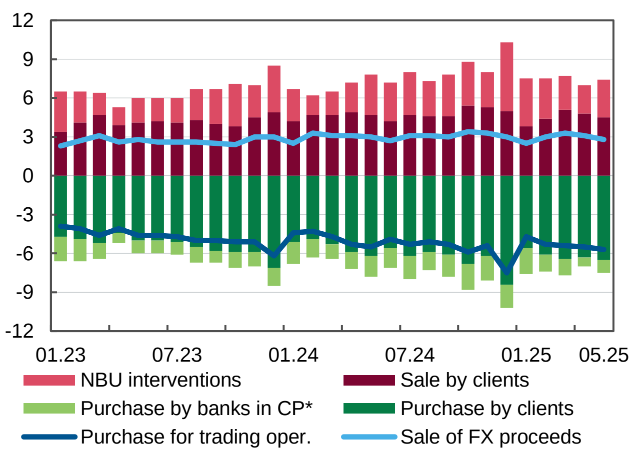
In the first five months of 2025, Ukraine received almost USD 18 billion in foreign assistance in the form of soft loans and grants. By the end of the year, this amount may increase to USD 55 billion. This will happen primarily due to the accelerated disbursement of tranches under the ERA mechanism, as well as the receipt of planned support from the EU under the Ukraine Facility program. This requires the timely and full fulfillment of commitments to partners, primarily under the IMF program and the Ukraine Facility. In

Figure 2.1.3. Gross and net international reserves, USD billions



Source: NBU.

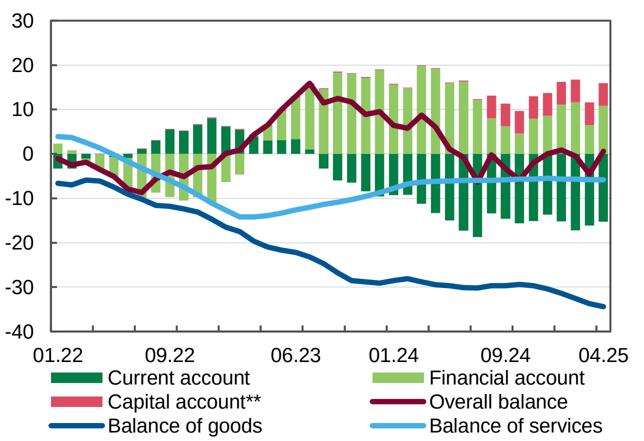
Figure 2.1.4. Demand and supply for non-cash foreign currency, USD billions equivalent



* Buying in a currency position.

Source: NBU.

Figure 2.1.5. Balance of payments*, USD billions



* Analytical presentation, trailing twelve months. ** The increase in the capital account in August 2024 was mainly due to the write-off of USD 5.2 billion of debt on Eurobonds as a result of a restructuring.

Source: NBU.

June, Ukraine is due to receive a tranche based on the results of the eighth review of the IMF program.

The more rapid receipt of funds from partners allows Ukraine to increase its international reserves. At the start of June, they amounted to USD 44.5 billion, and the NBU's forecast for the end of the year is about USD 58 billion. Both indicators significantly exceed the required level according to the IMF composite criterion. At the same time, the level of reserves accumulated this year is expected to decrease going forward. It will allow the NBU to meet the needs of the FX market in the coming years, when the volume of assistance might decline.

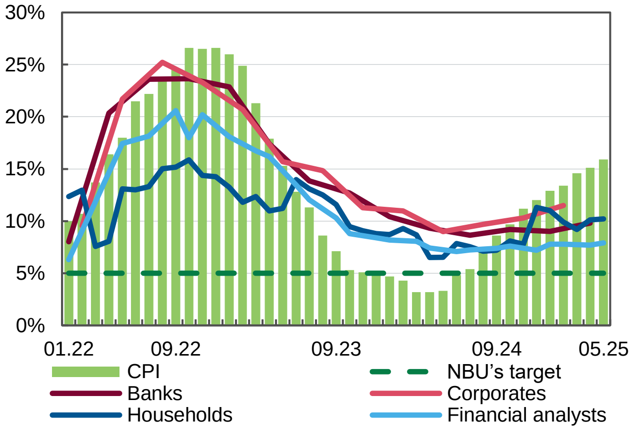
In the first half of the year, the NBU continued to compensate for the structural shortage of foreign currency in the market. Net demand for foreign currency in the first five months of the year increased compared to a year ago. It is fueled by the needs of the defense sector and natural gas imports. Demand for foreign currency from the households increased sporadically, but the pressure from this factor has recently eased. Net purchases of foreign currency by individuals in April–May 2025 were at their lowest levels since August 2023. The NBU stays ready to ensure the proper functioning of the FX market.

The trade deficit will deepen

Growth in commodity exports will slow in 2025 due to last year's low harvests and weaker external demand. An additional negative impact will come from the abolition of trade preferences by the EU in June and the return of the terms of trade that were in effect until February 2022 for most product groups. The uninterrupted operation of the sea corridor will allow Ukraine to redirect a significant portion of its food exports to other markets. The imposition of duties by the United States will not have a significant impact on Ukrainian exports to this country due to their low volumes and moderate rates. On the other hand, the growth of imports is accelerating due to defense needs and large purchases of natural gas and coking coal. The balance of trade in services remains relatively stable: the suspension of natural gas transit is offset by a decline in Ukrainians' spending abroad. The NBU expects the trade deficit to grow by 13% yoy, to USD 40.5 billion in 2025. The balance of primary income is close to zero: interest and dividend payments to non-residents are offset by remittances from Ukrainians' earnings abroad.

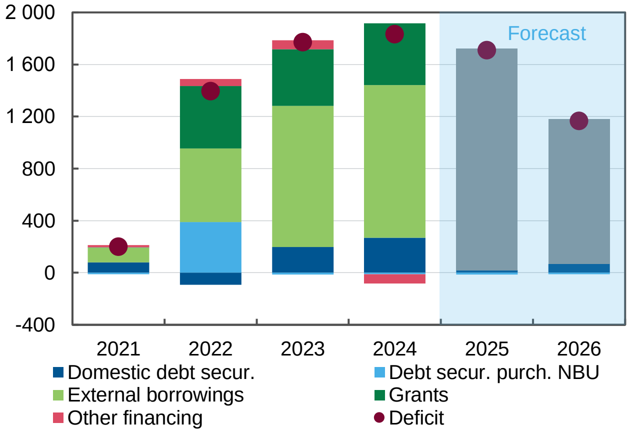
The financial account also shows a net outflow of funds, external financial assistance not taken into account. The main factor behind the outflows is the growth of FX cash outside banks, but its impact has weakened this year. Significant volumes of international assistance fully cover the trade deficit and balance international accounts in general. Funds received under the ERA mechanism are classified as loans, so they are recorded in the financial account and increase public debt. All of the debt under the ERA mechanism will be repaid using the proceeds from immobilized russian assets and will not be taken into account in the assessment of public debt sustainability.

Figure 2.1.6. Annual CPI and inflation expectations for the next 12 months



Source: SSSU, NBU, Info Sapiens.

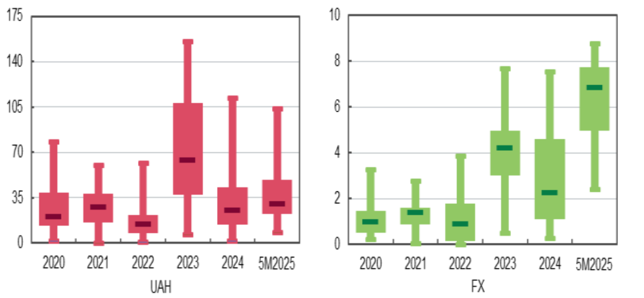
Figure 2.1.7. Financing* of the state budget deficit (excluding grants in revenues), UAH billions



* Net borrowing. Deficit in 2025–2026 is the NBU forecast. External borrowing, grant funds, and other financing in the forecasted periods are marked in grey.

Source: STSU, NBU estimates.

Figure 2.1.8. Daily balances of the Treasury's accounts in hryvnia and foreign currencies (USD equiv.), billion units*



Upper and lower edges of the rectangles represent the distribution's first and third quartiles. The dashes inside the rectangle show the median. Upper and lower dashes outside the rectangles show the minimum and maximum.

Source: NBU estimates.

Inflation will start to slow in summer

In May, annual inflation reached 15.9%. However, the impetus driving the acceleration of inflation has been exhausted. With the arrival of the new harvest, food inflation will begin to decline, even despite the effects of the spring frosts. This will drive a general slowdown in price growth. Additional disinflationary factors will include an improvement in the energy sector and the current unchanged natural gas and heating tariffs for households.

One of the prerequisites for reducing inflationary pressures is to maintain a tight monetary policy. The tightening of monetary conditions since the end of last year has contributed to an increase in interest rates on savings and supported investments by households and businesses in hryvnia term instruments. An easing of interest rate policy will become possible after the price peak is passed and the risks of persistently high inflation decrease.

Gradual fiscal consolidation continues

The state budget deficit, excluding grants in revenues, has been declining as a percentage of GDP since 2023, but its monetary value has remained almost unchanged. Although revenues in Q1 grew by 44% yoy, expenditures also grew rapidly, by 38%. Revenue growth was driven by better administration, improved financial performance of certain industries, and increases in certain tax rates, in particular for the banks. The growth in spending was driven by defense and reconstruction needs.

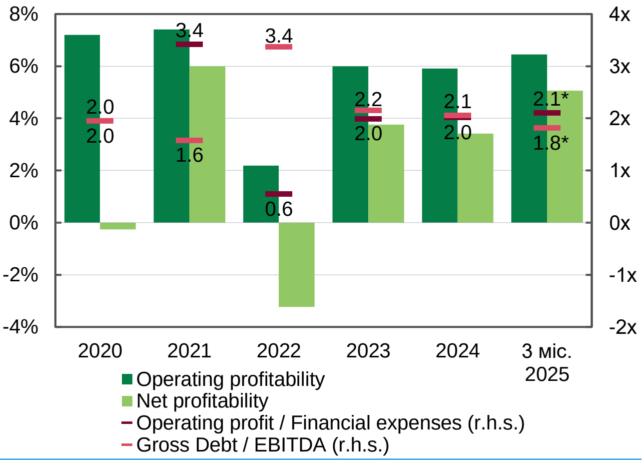
High defense needs may require increasing the current year's budget deficit beyond the planned targets. The government will be able to partially raise additional funds on the domestic debt market to finance the deficit. The potential for growth in borrowing through the placement of domestic government debt securities remains high. This is facilitated by both the significant liquidity of the banking system and the attractive market conditions for borrowing. Additional measures introduced earlier to boost the domestic debt market – in particular, the inclusion of benchmark government debt securities in the required reserves – will continue to be in effect. Moreover, additional funds may be raised from the non-bank sector. Since the start of the year, businesses' and households' portfolios of government debt securities have increased by UAH 12 billion and UAH 16 billion, respectively, and their demand for these securities is growing.

The more rapid receipt of funds from international partners will allow the government to accumulate a substantial reserve of funds by the end of the year to finance the 2026 budget expenditures. Next year's budget needs are currently difficult to estimate due to the ongoing military operations, persistently high security risks, and the need to finance the defense forces. This may make it harder to achieve the previously planned targets for reducing the state budget deficit. Therefore, Ukraine might need additional resources from donors. This once again highlights the need for decisive action by Ukraine's partners to confiscate and transfer immobilized russian assets to Ukraine.

2.2. Real Sector and Related Risks

Businesses' revenues continue to grow, driven by rising prices, while production is being held back by shortages of skilled labor and limited capacity. Businesses are moderately optimistic about their prospects, but the protracted war is hurting their propensity to invest. Growth in revenue and maintaining acceptable operating and net profitability means businesses remain attractive for bank lending. SMEs offer the best prospects for the banks in terms of building up loan portfolios.

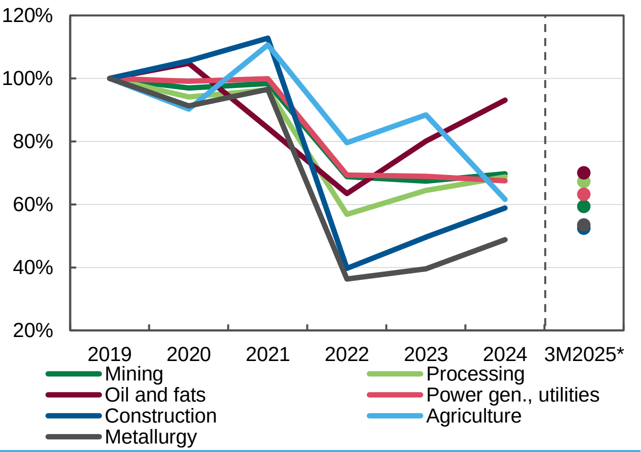
Figure 2.2.1. Profitability and debt burden



* Calculated for the 12 months ending March 2025.

Source: Open data portal, NBU estimates.

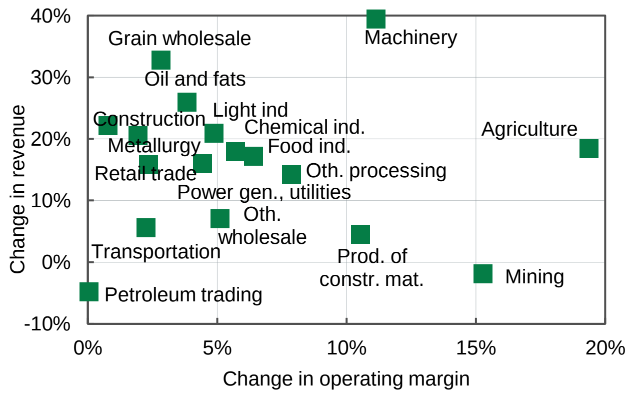
Figure 2.2.2. Production index by sectors, 2019 = 100%



* Q1 2019 = 100%.

Source: SSSU, NBU estimates.

Figure 2.2.3. Change in revenue and operating margin over the 12 months ending March 2025



Source: Open data portal, NBU estimates.

Prices are driving businesses' revenue growth

For the 12 months ending in March, corporate revenues grew by more than 13% yoy. This was primarily a result of rising prices. Production volumes, however, were depressed. Last year's moderate gains in manufacturing were followed by a slump in Q1 2025. Production decreased in a number of key sectors: energy, food processing, and mining. Despite all the challenges, companies maintained satisfactory operating and net profit margins. By retaining sound financial positions, businesses promote further lending and curb credit risks for the banks.

Export-oriented sectors are benefiting from global prices, while the rest are being fueled by stable domestic consumption

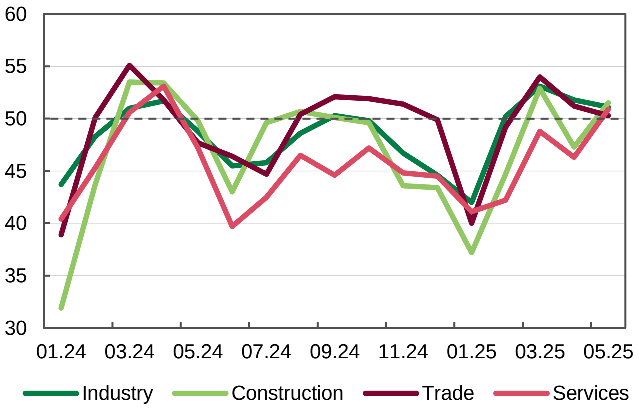
Current market conditions are favorable for export-oriented industries. Through the recovery of sustainable logistical routes, physical export volumes have increased significantly over the past year – by more than one-third. Stabilized freight rates have also contributed to larger deliveries. However, the main contribution to the increase in export volumes came from active exports in H1 2025 of crops left over from previous seasons. The termination in June of the duty-free trade regime with the EU will slightly worsen export performance, especially for grains. However, historically favorable global prices for a number of crops will bolster farmers' financial performance. Over the 12 months ending in March 2025, the sector's business revenue increased by more than 18% year-on-year, and profitability remains the highest across all sectors. This means the sector will remain attractive to the banks.

Metals-and-mining companies have been operating with uninterrupted access to port infrastructure for over a year now. Sustained consumer demand for metallurgy products has stimulated exports, which have risen by about a quarter over the year. The production of metals is also being driven by the growth in domestic orders. Meanwhile, the high volatility of prices and uncertainty over trade will restrain iron-ore exports and extraction.

Manufacturing in some industries that are focused on the domestic market is being fueled by government consumption. This is primarily happening in machinery, including the production of military goods. The industry needs to borrow funds to finance its re-equipment and working-capital replenishment. The revenues of companies that build engineering structures have risen significantly over the year. However, anticipated cuts to government spending going forward pose challenges to sector growth.

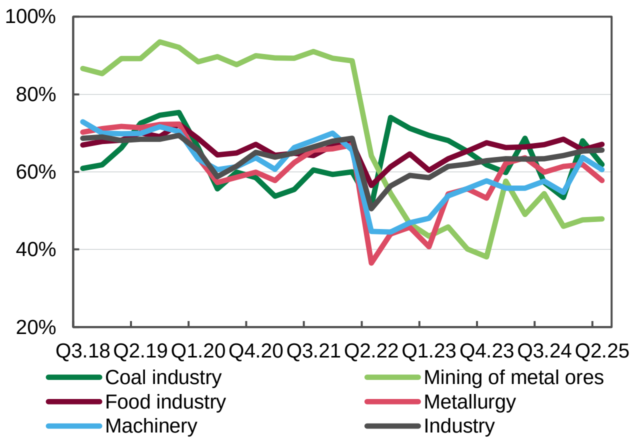
The revenues of trade and food sector enterprises are growing, underpinned by robust consumer demand. But

Figure 2.2.4. Business Activity Expectations Index by sectors



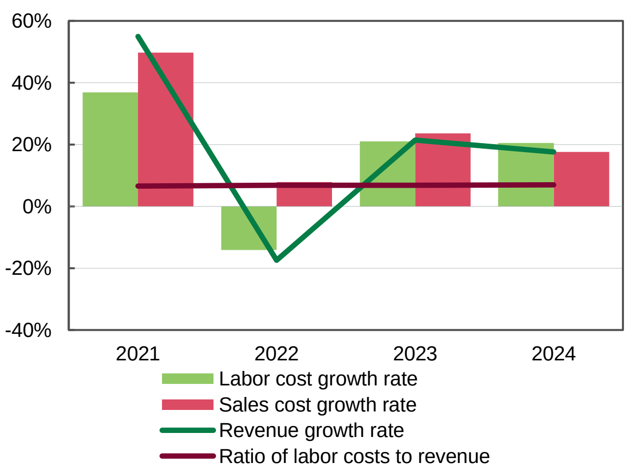
The dashed line denotes the neutral level.
Source: NBU survey.

Figure 2.2.5. Production capacity utilization by industrial enterprises (as of the start of the quarter)



Source: NBU survey.

Figure 2.2.6. Changes in revenue, sales costs, and labor costs of businesses*



* Data from large and medium-sized enterprises. Adjusted for outliers.
Source: Open data portal.

companies are still in need of working-capital financing from the banks. Revenue growth in these segments has nonetheless decelerated from previous periods.

Businesses have more optimism but are suffering from worker shortages

Businesses are cautiously optimistic. In May, the Business Activity Expectations Index exceeded the neutral level in all sectors of the economy for the first time in a year (see the Monthly Business Outlook Survey). Businesses expect a revival of capital investment, although their appetite for it remains subdued by war risks (see the Business Outlook Survey). Up until now, enterprises' investments have primarily focused on restoring and supporting current production, including the development of their own energy generation, most notably in trade and the food industry. The expansion of non-core power generation has helped businesses adapt to power outages. A number of energy independence projects are being implemented by businesses, with the support of the banks. At the same time, the wear and tear and destruction of capacities will continue to hinder business development. A number of sectors are already operating close to "pre-war" capacity utilization levels. To scale up their activities, they need capital investment.

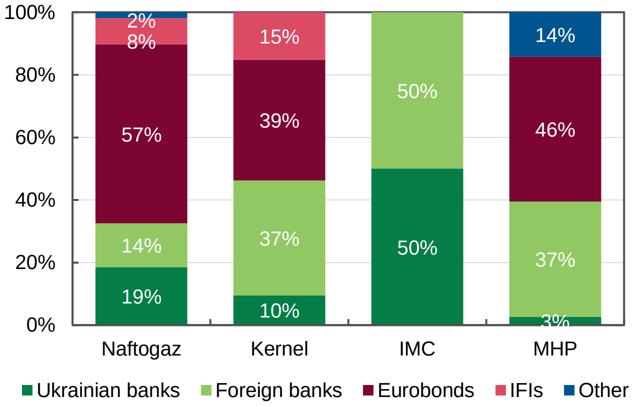
Companies believe the protracted war is a major obstacle to doing business. For twelve straight months, the deficit of qualified personnel has ranked second among adverse factors. In Q1 2025, this factor was quoted by about half of the companies polled in the Business Outlook Survey. This share has more than doubled compared to 2023. Enterprises have so far been attracting and retaining workers by significantly raising their wages and salaries. This has had a moderate impact on companies' operating profitability at a time of rapid revenue growth. Going forward, however, it will be much more difficult for enterprises to keep raising wages and salaries at such a pace. For low-margin industries like construction, problems with finding people to hire are already significantly hindering operations. Moreover, the unemployment rate is approaching its "pre-war" level, meaning it will be more difficult to come across qualified workers. The issue of labor shortages will therefore continue to impede business development for a long time.

Businesses' debt burden is moderate

Companies' debt burden is not excessive. In the 12 months to March 2025, the ratio of operating profit to financial expenses was 2.1x, while that of gross outstanding debt to EBITDA was 1.8x. Rising revenues and maintaining sufficient operating profit margins ensure acceptable solvency indicators for bank clients. The respondents polled in Bank Lending Surveys also cited the moderate debt burden of enterprises.

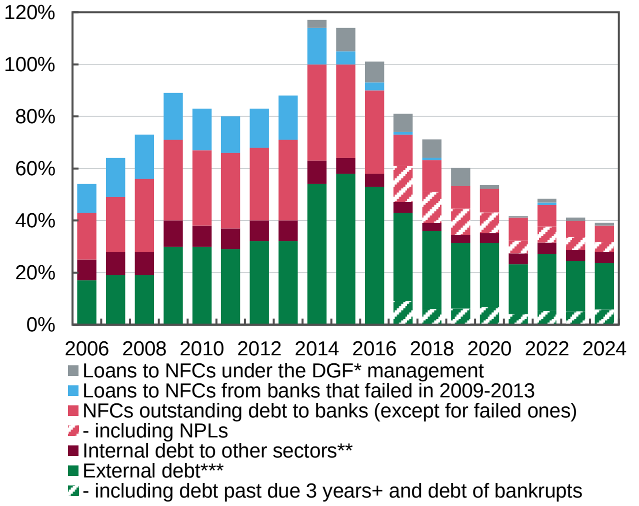
However, not all segments of business rely equally on Ukrainian banks to finance their needs. Historically, large enterprises have primarily used Eurobonds to raise funds or borrowed from foreign banks or IFIs. The share of Ukrainian banks' loans in large companies' debt has never exceeded

Figure 2.2.7. Debt composition of selected public companies as of 1 January 2025



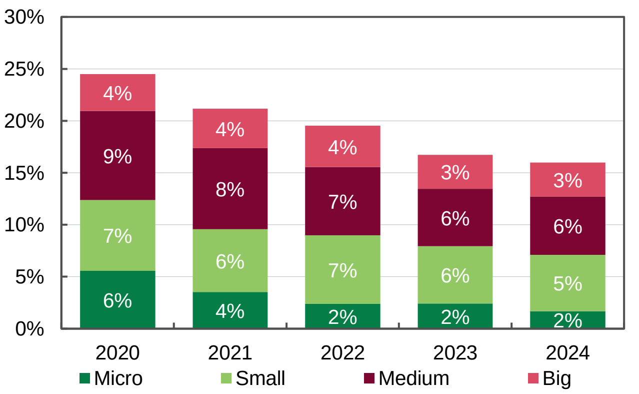
MHP – Myronivsky Hliboproduct, IMC – Industrial Milk Company.
Source: company data.

Figure 2.2.8. Debt of nonfinancial corporations (NFCs), % GDP



* Book value of loans at the time the bank was declared insolvent. ** Non-bank financial institutions, for debt securities. *** For Eurobonds and loans to non-residents, incl. direct investment enterprises. No trade credit.
Source: NBU, Open data portal, National Commission on Securities and Stock Market, STSU.

Figure 2.2.9. Bank loans-to-assets ratio by company size



The size of companies is determined in accordance with the Law of Ukraine No 4196-IX based on the revenue criterion in the relevant year. Bank loans are loans over UAH 2 million issued by Ukrainian banks.
Source: NBU, Open data portal.

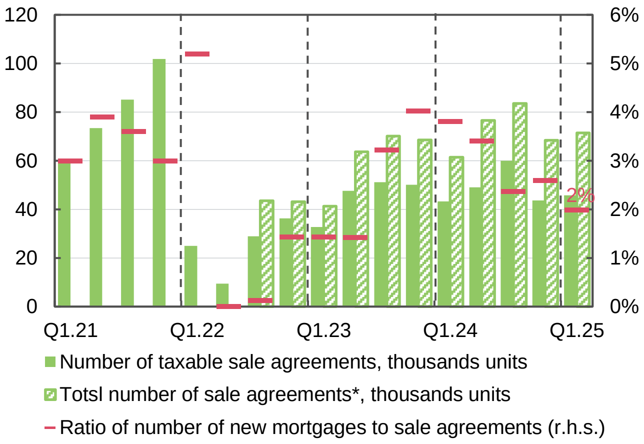
25%, which is one-third to one-half less than for SMEs. The debt these companies owe to banks has only slightly decreased from pre-full-scale-war levels. But conventional bank lending cannot meet their needs. The highest loan amount a medium-sized Ukrainian bank can provide, under the concentration restrictions in place, is a relatively small, up to UAH 3 billion at most. The average debt of large capital-intensive industrial enterprises, primarily in metallurgy, mining, oil refining, and the chemical industry, is substantially higher. Some large companies take out loans from multiple Ukrainian banks at once. However, differences in approaches to lending and incoherent actions by creditors make it difficult to obtain loans and to resolve such debts later if needed. The development of consortium lending will improve the financing conditions for large businesses. Going forward, particularly as war risks abate, large companies will most likely have to seek out non-bank sources of financing for their investments.

Meanwhile, before the full-scale invasion, small, medium, and micro-enterprises relied most heavily on loans from Ukrainian banks compared to all other sources of debt. However, the percentage of bank loans in the SME and microenterprise debt has at least halved since then. The share of these firms in the sector's revenues is not as significant, while their debt burden is somewhat higher than that of large companies. However, considering the rapid growth in their assets and operations, this segment is the most promising in terms of bank lending expansion.

2.3. Real Estate Market and Mortgage Lending

The growth in the number of house-purchase transactions has decelerated. There is a lack of incentives for demand to revive, although prices are attractive compared to historical levels, and the effect of war-induced migration is fading. Buildings at existing construction sites are slowly being completed, but new construction is hardly starting. Mortgage lending has slowed due to restrictions on properties eligible for financing under the *eOselia* mortgage program, and a lack of liquid funds to implement the program. However, it is by changing the model of state support for mortgages and by conducting a number of infrastructure reforms to regulate the construction market and increase its transparency that the market can be given a boost.

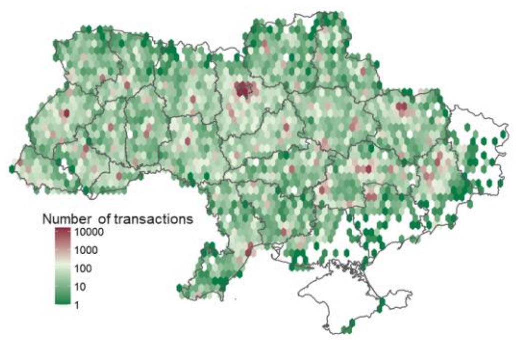
Figure 2.3.1. Housing market activity



* According to the state register of property rights, which includes tax-free transactions.

Source: Ministry of Justice of Ukraine, State Property Fund of Ukraine, National Information Systems, banks' data.

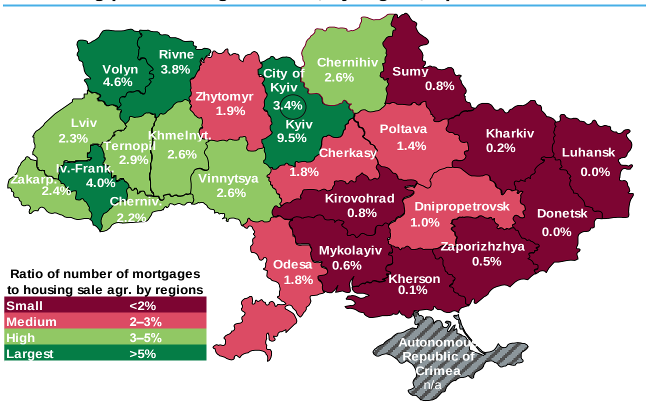
Figure 2.3.2. Number of housing purchase agreements in April 2024 – March 2025



The area is divided into equal hexagons.

Source: National Information Systems.

Figure 2.3.3. Ratio of the number of new mortgages to the number of housing purchase agreements, by region, April 2024–March 2025



Source: National Information Systems, banks' data.

Demand for housing is subdued

The growth in the number of home purchases has been slowing recently. In Q4 2024 through Q1 2025, only 8% more house purchases were made than in the same period a year ago. At the end of 2024, a cyberattack disrupted the work of some of the state registers for a while, making it hard to sign agreements. But the reopening of the registers early this year did not lead to a tangible increase in market activity.

The volume of tax-free housing sales has grown faster since the full-scale invasion. Those are first-time-in-a-year sales of housing that has been owned for at least three years. Such sales usually occur due to the change of permanent residence, including migration. Deals closed in regions near the battle zone make up the largest share of all tax-free sales.

Almost two-thirds of the deals are made outside oblast centers, but the share of the deals concluded in large cities has edged higher over the year. The average area of a purchased apartment remains close to 48 sq. m, and that of a house, up to 70 sq. m. As before, buyers are more often interested in older housing sold on the secondary market: in three out of four cases, they buy a home built more than 15 years ago. "Newly built"[1] housing is being purchased less and less often, even in large cities where construction is more active.

Despite generally good consumer sentiment and steady income growth, the recovery of demand in the real-estate market is extremely slow. War risks and general uncertainty continue to deter home purchases. Active internal migration's ad-hoc stimulating effect on the market has faded significantly. Without improving security expectations or providing insurance mechanisms against war risks for mortgage agreements, demand is unlikely to rise tangibly.

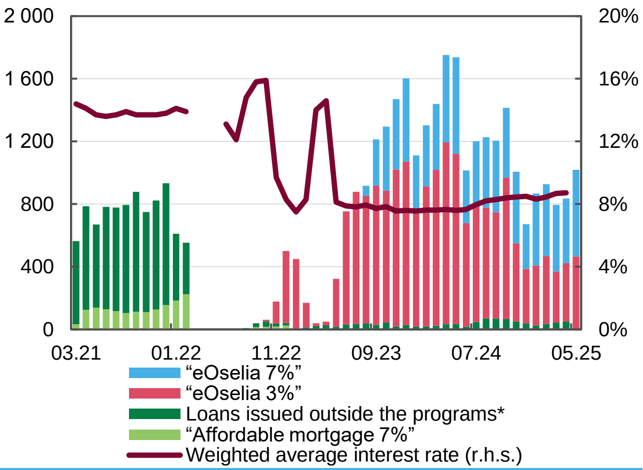
The outlook for mortgage lending will be shaped by the overhaul of the state support mechanism

Mortgages are still not a driver of demand in the real estate market. The share of mortgage-financed home purchase transactions continues to fluctuate within 2%–3%, which is lower than the level of 2021. However, this percentage is quite uneven across regions: in Kyiv oblast, it has been much higher over the past year, at 10%. Overall, more housing is purchased through mortgages in the country's west and capital.

Almost every mortgage is provided under the *eOselia* program. New mortgages have decreased significantly. The December cyberattack complicated the registration of

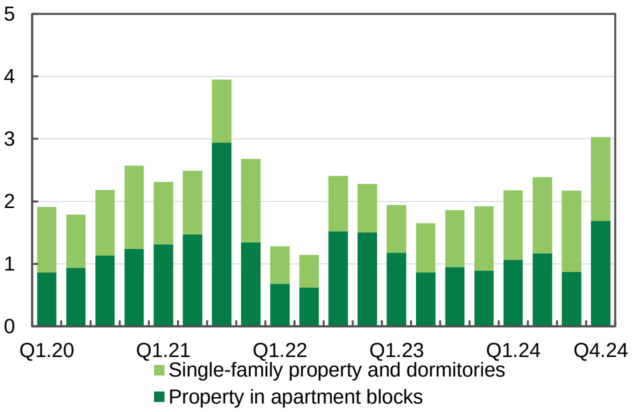
[1] LUN classifies buildings constructed after 2010 as "newly built".

Figure 2.3.4. New mortgage lending, UAH millions



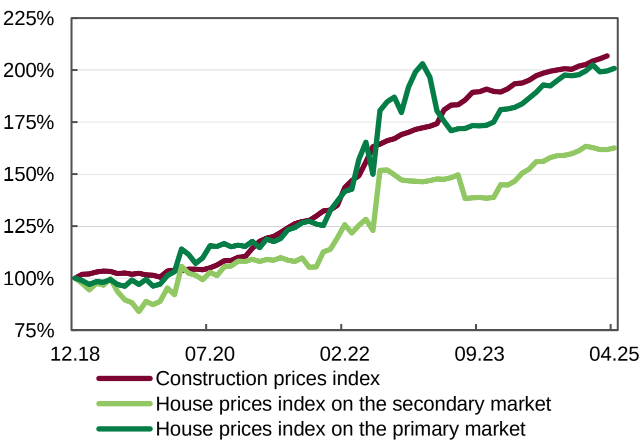
The *eOselia* 7% program covers loans to wide categories of households.
* No data available for May 2025.
Source: banks' data, BDF, UFHC.

Figure 2.3.5. Commissioned residential property in Ukraine, millions sq. m



In 2023, the area is divided proportionally to the structure by the number of comissioned apartments. In Q1 and Q2 2024, the structure is reflected according to the data of the H1 of 2024.
Source: SSSU.

Figure 2.3.6. Construction and housing price index in hryvnia, December 2018 = 100%



Source: SSSU, real estate agencies, NBU estimates.

housing ownership. Lending resumed at the end of January. But despite pent-up demand, the average monthly volume of new mortgages in H1 2025 is down by a quarter from H2 2024. Last year's age-related restriction on housing financed under *eOselia* narrowed the range of eligible properties. So, the primary market's share of mortgages rose as there is less lending for purchases of older housing. The breakdown of mortgage approvals has also changed: the share of universally available mortgages to improve housing conditions (carrying 7% interest) leapt from 25% to almost 40% of new approvals. In addition, the amount of Ukrfinzhytlo's liquidity prevents there being a more rapid buildup of the portfolio. The state support strategy is being revised to scale it up and stimulate market demand (see Box 1. Vision of the Mortgage Lending Development Strategy).

Supply of new housing replenished slowly

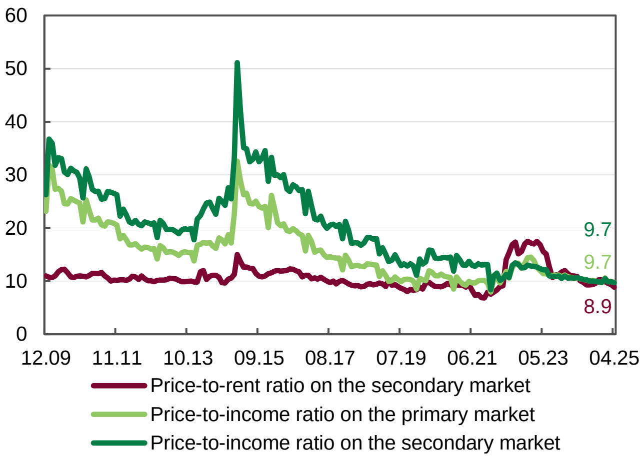
In 2024, the area of commissioned housing rose by one-third. For the most part, this was driven by the completion of projects launched before the full-scale war. Construction on the other sites has been progressing at a snail's pace for about four years. And the area commissioned in 2024 is still down 15% from the pre-full-scale-war year of 2021. Construction doesn't actually increase the housing supply in the primary market, as the number of residential complexes starting sales is almost equal to those where sales have concluded. In Q1 2025, properties in Ukraine's capital and western oblasts were put up for sale most actively. New housing starts are also primarily happening in the west.

With demand being sluggish, there is currently a sufficient supply of housing. Most ads feature relatively spacious and expensive housing, but the majority of apartments that end up being sold are relatively cheap and small. Weak demand, especially for new housing, is holding back construction. Even after demand revives, the housing stock will take rather long to replenish, because of protracted construction times. More effectively regulating the activities of developers and improving urban planning can attract investment in housing even at the initial stages of construction.

Home purchase prices plateaued, while rents accelerated

Although prices in home sales ads have increased since the beginning of the year, actual transactions do not confirm such an uptrend. Prices paid in housing purchase transactions on the secondary market have almost held steady since the start of the year. There are currently no underlying price pressures, and construction costs that used to drive up the price of a square meter have grown much more slowly over the past year. With real-estate prices being traditionally denominated in the U.S. dollar, the strengthening of the hryvnia exchange rate against this currency has also restrained the growth in housing prices. So, the per-square-meter price of apartments has mostly remained unchanged, and has actually decreased in some places, such as Kyiv and Lviv. In the primary market, prices have also stalled, even in regions with the highest demand for new housing.

Figure 2.3.7. Price-to-rent and price-to-income ratios in Kyiv



Since February 2022, income has been calculated using average salary increases in Kyiv, based on data from work.ua and robota.ua, and salary increases in Ukraine, according to the SSSU, relative to January 2022.

Sources: SSSU, websites of real estate agencies, websites of job aggregators, and NBU estimates.

In contrast to the sluggish growth in housing prices, rental prices have risen quite rapidly, especially in Kyiv. The need for comfortable housing is not always backed by the ability and willingness to purchase it, but this need fuels the demand for rental housing, which pushes rents up. Buying a home thus remains more profitable compared to renting: the ratio of purchase prices to rents in Kyiv has fallen slightly below the long-term average and significantly below the pre-full-scale-war level, sometimes to as low as 9x. The ratio of the price of a standard apartment to household income remains at historical bottoms, also indicating the relative affordability of housing. However, uncertainty over the security situation continues to erode market incentives and restrain demand for housing.

The market for commercial real estate is brisk, although office tenants are still hard to find

All activity indicators in the commercial real estate segment are improving. Consumer activity is increasing, as is shopping mall attendance. Landlords' incomes, determined as a percentage of sales, are also increasing as turnover rises. In addition, landlords are also raising the fixed component of rent in response to strong demand for retail space. According to CBRE, the vacancy rate in Kyiv's prime shopping malls is gradually declining, down 3 pp, to 14%, in Q1 2025. Along with large international brands, Ukrainian manufacturers are also opening offline stores. However, not all shopping centers are faring the same way. In Kyiv, a number of them have high vacancy rates, but this is not due to the sector's condition, but because of deficiencies in their business models. Although the market is brisk, developers have almost no plans to build and open new shopping malls.

The office real estate market is dull. The vacancy rate remains high, although it is somewhat lower than a year ago, primarily in high-end office centers. Due to rents being low, tenants often relocate to higher-class, renovated offices, while the remainder of the landlords look for clients that will pay just enough rent to cover utility bills. Nobody is starting to build new office centers. The few that neared completion in early 2022 were only commissioned last year.

Demand for warehouse and logistics infrastructure rentals is high, particularly in e-commerce. The vacancy rate among warehouses is therefore low. However, rents in this segment have stabilized after a period of growth.

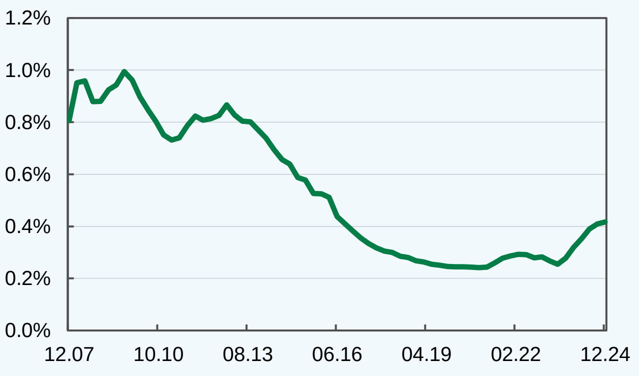
Box 1. Vision of the Mortgage Lending Development Strategy

Institutions are finalizing the draft *Mortgage Lending Development Strategy*, after which it will be submitted to the Financial Stability Council for approval. This document seeks to remove obstacles to more active mortgage lending by the banks and to make mortgages accessible to the general public.

The war put the mortgage market's recovery on hold

In Ukraine, mortgages were a mass product only up until the financial crisis of 2007–2008. Due to significant demand for housing and the entry of foreign banks into the market, mortgage lending surged. Foreign financial institutions had experience issuing mortgages and access to FX funding. However, due to regulatory flaws, the banks underestimated the risks and made FX loans without first vetting borrowers' financial standing, thus fueling real-estate prices. The accumulated imbalances led to a crisis on the market: real-estate prices collapsed, borrowers stopped servicing mortgages en masse, and so most mortgages turned non-performing. To alleviate social pressures, the state imposed a legal moratorium on foreclosure of mortgaged property. Significant losses deterred both the banks and households from engaging in mortgages. At the end of 2021, the mortgage-to-GDP ratio was as low as 0.3%.

Figure B.1.1. **Gross hryvnia mortgages to GDP**



Source: banks' data, SSSU.

Since then, the real estate market has received almost no support from mortgages. It was mainly the funds of developers and buyers that revitalized this market. However, the sector lacked a proper regulatory framework and safeguards to protect the rights of investors in construction. Violations of building codes and delays in commissioning housing have become constant companions in the sector. The sector was rattled by multiple high-profile developer bankruptcies. These risks discouraged the banks from renewing mortgages. State support programs were unsustainable in the long term.

Positive changes only began in the early 2020s: the moratorium was lifted, and the protection of creditors' and consumers' rights was strengthened. The State Architecture and Construction Inspection of Ukraine (SACIU) was reformed, leaving the market's regulation somewhat improved. To reduce risks to construction completion, a guaranteed construction share and the state registration of construction site ownership were introduced. Meanwhile, better economic conditions led to lower market rates, making mortgages more affordable. In 2021, almost UAH 9 billion in mortgages were granted.

The full-scale war broke this uptrend. In the first months since the invasion, the real estate market went completely quiet, and later remained inert. In late 2022, the government launched the *eOselia* program to promote preferential mortgages. The program is primarily designed to provide housing for military personnel, teachers, and doctors. However, other household categories wishing to improve their housing conditions are also entitled to access the program. Since then, market-based banking products have been unable to compete with the program, which has been dominating the market, providing over 96% of new mortgages.

However, the state's capacity to subsidize mortgages in the current setup is limited. Without market products, the program will not be able to meet the demand for housing during the war and the reconstruction period. Moreover, the current program design is unsustainable in the long run, which is crucial for mortgage support. The *Mortgage Lending Development Strategy*, currently being finalized by the NBU in cooperation with other state authorities and international partners, will give the necessary momentum.

Mortgage development requires infrastructure changes

The *Mortgage Lending Development Strategy*'s main proposals are:

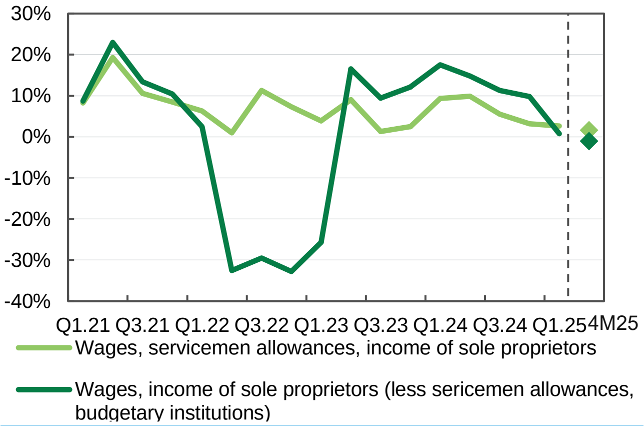
- Implement the provisions of Directive 2014/17/EU on mortgages: rules for calculating the rate, disclosure of mortgage terms in contracts and advertising, and procedures to resolve non-performing mortgages.
- Ensure the availability of mortgage insurance against war risks. Draft law No. 12372 provides for involving a wider range of insurers and establishing a multi-level model for loss coverage. Insurance will make mortgages more interesting to the banks and more affordable for customers.
- Introduce EU property valuation standards and improve the exchange of valuation information, including through creating an open database of real-estate prices.
- Improve the controllability of construction financing, in particular through the unification of financing conditions and the use of funds only for the purposes of construction, and conditional on its progress.
- Improve the terms of state support for mortgages. The main tool should be compensation for part of the interest that borrowers pay to the banks. This will encourage the banks to offer their products, properly assess risks, and increase competition among lenders.
- Determine the terms of covered-bond issuance and securitization to promote risk sharing and stable funding.

The implementation of these measures will take place in parallel, but legislative reforms will require considerable time. Going forward, the Strategy should become an element of a broader *Housing Strategy*.

2.4. Households and Related Risks

Nominal household incomes are growing primarily due to further wage increases in the private sector and lower unemployment, but in real terms aggregate incomes are slowing down. Despite this, improved consumer sentiment is boosting demand for loans. The total debt burden of households remains low. Households continue to show high interest in term deposits, and investments in hryvnia domestic government debt securities are becoming increasingly popular.

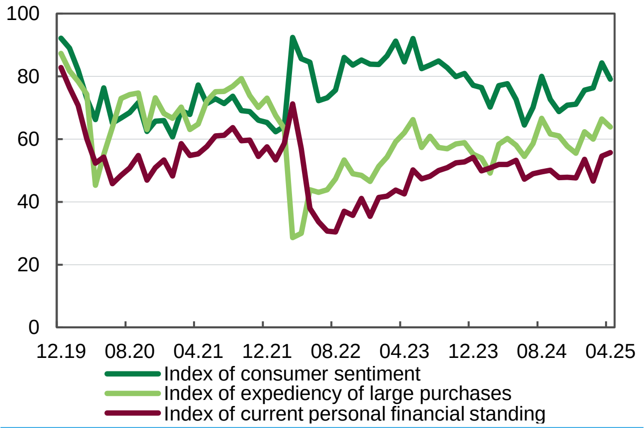
Figure 2.4.1. Estimated of real household incomes*, change yoy



* Data on the amounts of official wages and incomes of sole proprietors come from bank reports. PrivatBank's data was adjusted to include only wage payments.

Source: Pension Fund of Ukraine, STSU, banks' data, NBU estimates.

Figure 2.4.2. Households' consumer confidence*, points



* The index readings below 100 means that society considers the situation to be mostly negative.

Source: Info Sapiens, monthly surveys of households (respondents aged 16+).

Figure 2.4.3. Ratio of annual change in consumer loans from banks and NBFIs to annual income, annual consumer spending

* Data on the amounts of official wages and incomes of sole proprietors come from bank reports, those on pensions from Pension Fund of Ukraine data.

Source: Pension Fund of Ukraine, SSSU, banks' data, NBU estimates.

Wages are continuing to rise in the private sector

The nominal incomes of private sector employees are continuing to grow rapidly. In Q1 2025, the average monthly wage increased by 24% yoy. Unemployment continued to decline, reaching 11% according to NBU estimates — the lowest level since the start of the war. However, wages in budgetary institutions are growing much more slowly than in the private sector, suppressing overall wage growth. Real wage growth was significantly constrained by inflation accelerating to double digits.

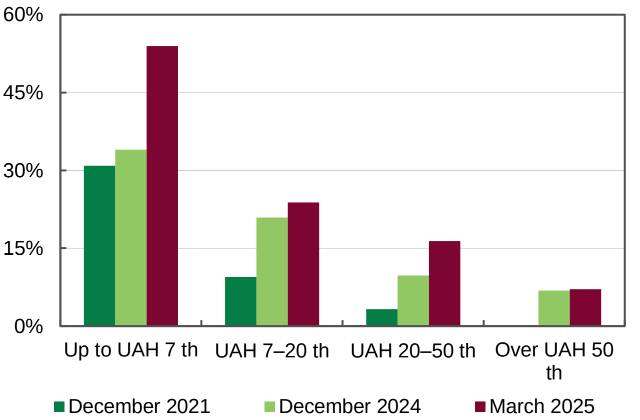
The main drivers of household income growth remain in place. The economy continues to grow, as does business activity. Competition for employees remains fierce, prompting businesses to raise wages. However, it is becoming increasingly difficult for companies to maintain high wage growth rates. In addition, unemployment is approaching its "pre-war" levels, and the workforce is not yet recovering as migrants are not returning. Therefore, the impact of employment growth on incomes is gradually coming to an end. This will be offset by the expected slowdown in inflation, which will support real income growth.

Lending is being fueled by consumer optimism

The slowdown in real incomes did not affect consumer behavior. The spring of this year saw a rise in the consumer sentiment and propensity to spend indices measured by Info Sapiens. As a result, demand for loans grew and, consequently, so did retail loan portfolios. Households actively use bank loans to finance current expenses. The average loan amount is moderate, and the terms for using bank loans are short. Even the free use of funds by customers during the so-termed grace period has advantages for banks – card issuers will receive additional fees and commissions, measured as a percentage of card turnover – as a share of interchange fees from payment systems. Therefore, the banks are actively encouraging their clients to use their products.

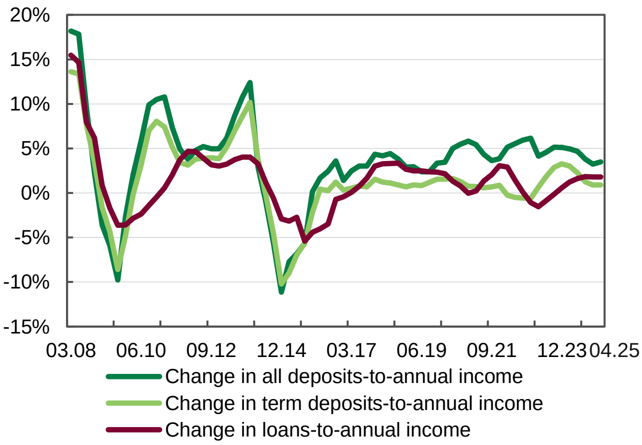
In contrast, trends in non-bank lending are not constant, and their dynamics depend more on the supply of financial institutions than on demand. Over the past six months, new loans have declined. This is a consequence of the exit from the market of a number of lenders that violated consumer protection and AML/CFT requirements. Work is under way to prevent predatory lending by non-banks, which causes excessive debt burdens due to opaque terms and fraudulent practices. At the same time, outstanding loans have been rising due to increasingly longer loan terms. Non-bank lenders continue to account for less than one-tenth of the total retail portfolio of financial institutions, and the ratio of these loans to household income is less than 2%.

Figure 2.4.4. Debt-to-income ratio of household borrowers by monthly income



Source: NBU, Info Sapiens, quarterly surveys of households (respondents aged 16+), NBU estimates.

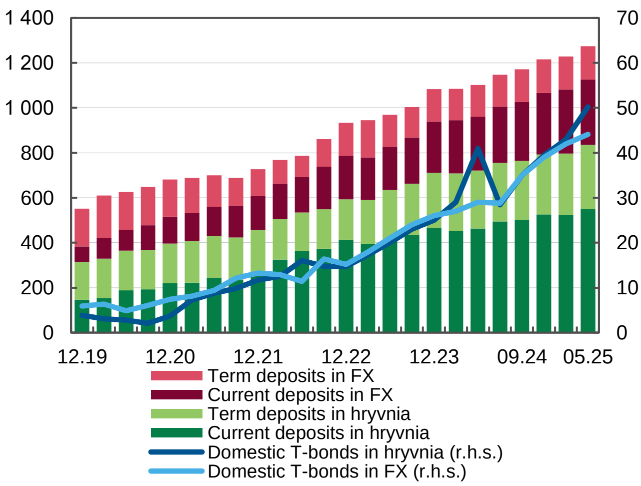
Figure 2.4.5. Ratios of annual changes in hryvnia deposits and retail loans at banks to annual income*



* Data on the amounts of official wages and incomes of sole proprietors come from bank reports, and those on pensions from Pension Fund data.

Source: Pension Fund of Ukraine, banks' data, NBU estimates.

Figure 2.4.6. Main instruments of households' financial savings, UAH billions



Source: NBU estimates.

The ratio of growth in consumer loans from banks and non-bank financial institutions to household consumption remains tiny, at 1%. Therefore, the impact of lending on consumption is still not decisive.

The debt burden of households is little changed

Given the growth in nominal incomes, brisk lending is not changing the overall debt burden of households. At the beginning of April 2025, the ratio of all loans from banks and non-banks to household income remained at 10%. According to a study by Info Sapiens, only a quarter of households had loans in Q1.

However, the debt burden varies greatly depending on the income of borrowers. Over the year, the debt burden has increased significantly for clients with the lowest incomes. Their low solvency limits their access to bank loans, so they rely more on more expensive loans from the non-banks or from relatives and acquaintances. On the other hand, overall income growth reduces the share of this category in the total population. The debt burden of higher-income clients has remained virtually unchanged.

Propensity to save in banks has declined somewhat

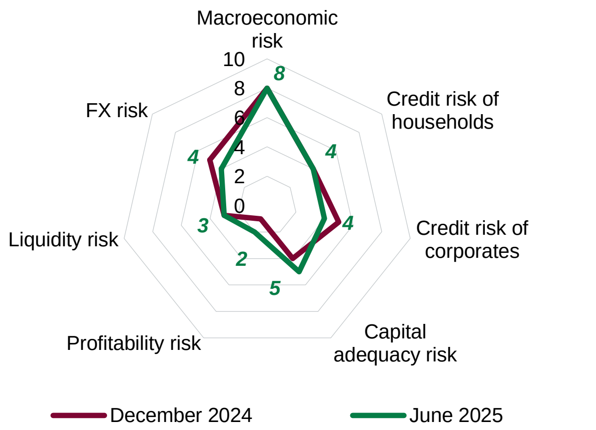
Over the last six months, the ratio of growth in bank deposits to household income has declined slightly. That ratio stands at around 3%, which corresponds to the average for EU countries. However, in most of these countries, households mainly keep their savings in other instruments. In Ukraine, however, the bulk of households' funds continue to be accumulated in hryvnia bank accounts.

The inflow of term hryvnia deposits into banks continues. Their share in total client deposits has stabilized at around 34%. Households have significantly increased their investments in government securities, which, in the absence of taxation, offer more attractive returns than other available instruments. In the first five months of the year, investments in hryvnia domestic government debt securities have grown by UAH 11 billion, which is more than half of the increase in hryvnia term deposits. Therefore, investments in government securities are becoming increasingly popular, although their volumes are still insignificant compared to other savings. Households' demand for FX as a savings instrument also persists.

Part 3. Banking Sector Conditions and Risks

3.1. Financial Sector Risk Map

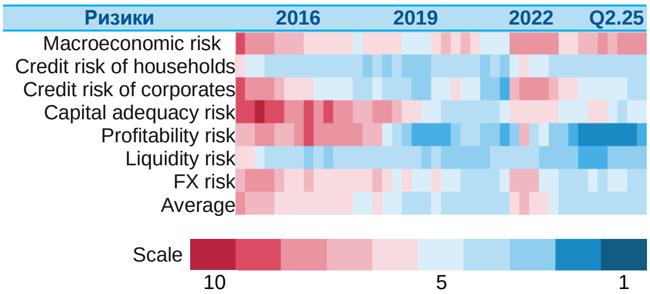
Figure 3.1.1. Financial sector risk map



The NBU assesses risks on a scale from 1 to 10, with 1 being the lowest level of risk and 10 the highest. The assessment reflects the outlook for the next 12 months. The methodology for building the risk map has been adjusted given data availability.

Source: NBU estimates.

Figure 3.1.2. Financial sector risk heatmap



Source: NBU estimates.

Description:

- Macroeconomic risk indicates the level of threats arising in the real economy, the external sector, and the fiscal area.
- The credit risks of households and corporates reflect expected changes in the share of non-performing loans in bank loan portfolios and the need for extra provisions for those loans.
- Capital adequacy risk measures the ability of banks to maintain an adequate level of capital.
- Profitability risk measures the ability of banks to generate net profit.
- Liquidity risk is a measure of the ability of banks to meet their liabilities to depositors and creditors in full and on time.
- FX risk is the risk that foreign exchange market trends will affect the resilience of banks.

Macroeconomic risk: unchanged

The economy continues to grow, albeit at a slower pace than previously forecast. Growth is constrained by the protracted war. The current account deficit of the balance of payments remains significant. The budget deficit, along with the public and gross external debt relative to GDP remain high. At the same time, substantial international assistance largely offsets these challenges.

Credit risk of households: unchanged

The quality of the retail portfolio somewhat improved, with the share of loans overdue by more than 30 days continuing to decline. The economic expectations of households also improved slightly. However, these changes were still not enough to improve the overall estimate.

Credit risk of corporates: decreased

The level of corporate defaults continued to decline. As a result, banks' expectations of the future corporate portfolio quality have improved. The financial performance of companies is acceptable. Businesses' assessments of future business activity are positive, although subdued.

Capital adequacy risk: increased

Capital risk increased to medium. Capital adequacy declined slightly, primarily due to higher income taxation and an increase in the amount of operational risk to be covered by capital. However, the sector's capital cushion remains significant.

Profitability risk: increased

Profitability risk remains low, but the risk assessment has deteriorated somewhat due to a decline in return on equity. The sector's profitability continues to be driven by rising interest income and the high operating efficiency of the banks.

Liquidity risk: unchanged

The liquidity risk is moderate. The banks continue to increase customer deposits. Despite a slight decline, the LCR ratio in all currencies continues to significantly exceed regulatory requirements. The stock of high-quality liquid assets remains significant. Financial institutions' expectations of future liquidity risk have improved.

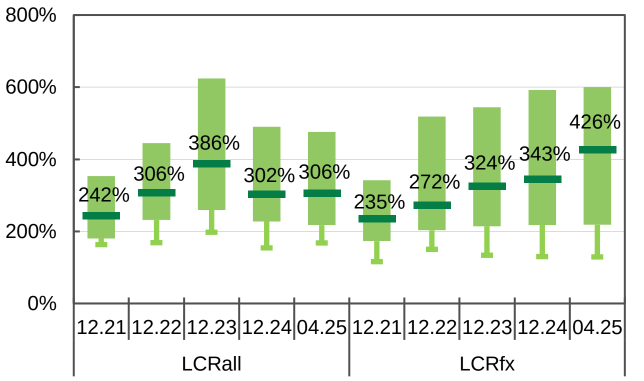
FX risk: decreased

FX risk has decreased to moderate. The UAH/USD exchange rate has recently been fluctuating within a narrow range. Significant financial assistance from partner countries has allowed the NBU to build up international reserves. The banks' FX risk assessments and households' depreciation expectations have also improved. In addition, banks maintain a balanced net open foreign exchange position.

3.2. Liquidity and Funding Risk

Deposit flows into the banking system have slowed somewhat, with growth rates converging among different groups of banks. This indicates stronger competition among banks for funding. The existing stock of high-quality liquid assets minimizes liquidity risks and provides the banks with room for comfortable further increasing their loan portfolios and investments in domestic government debt securities.

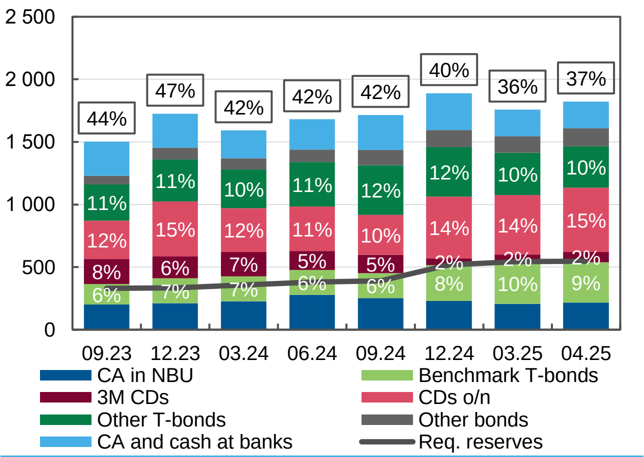
Figure 3.2.1. Liquidity coverage ratios in all currencies (LCRall) and FX (LCRfx)



The upper and lower edges of the rectangles show the first and the third quartiles of the distribution. The dashes inside the rectangles indicate the median. Lower dashes outside the rectangle show the minimum. The required ratio is 100%.

Source: NBU.

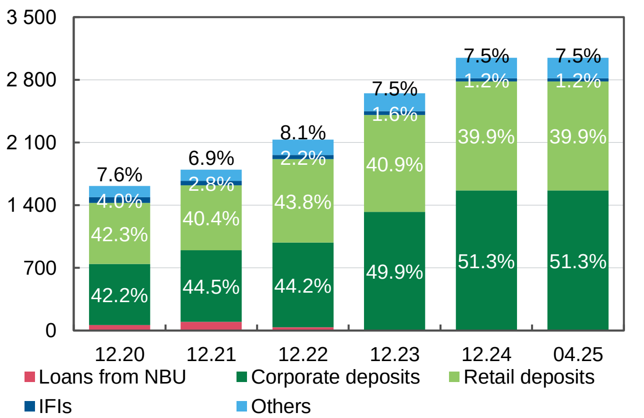
Figure 3.2.2. High-quality liquid assets in all currencies, UAH billions, and their share in net assets



The percentage indicates the share in net assets. CA – current accounts. Data on benchmark T-bonds indicate nominal value.

Source: NBU.

Figure 3.2.3. Banks' liabilities, UAH billions



Source: NBU.

The banks have substantial liquidity buffers

In H1 2025, the banks paid significant amounts of income tax at the windfall tax rate, and the state-owned banks also paid out dividends. So, the banks' high-quality liquid assets (HQLA) have decreased slightly compared to the beginning of the year. However, their share in assets remains more than comfortable, at 37%. The banks continue to comply with the liquidity coverage ratio (LCR) in all currencies and in foreign currency with a margin to spare. Medium-term liquidity ratios remain normal – the median NSFR value across the system is almost twice the minimum requirement. None of the banks is in breach of the aforementioned ratios. According to a survey of banks, liquidity risk has even subsided recently.

The share of benchmark domestic government debt securities continued to grow in hryvnia HQLAs, allowing the banks to partially cover reserve requirements, which were raised last year, and earn interest income from them. At the same time, the share and volume of investments in other domestic government debt securities shrank. The banks' investments in NBU certificates of deposit remained significant.

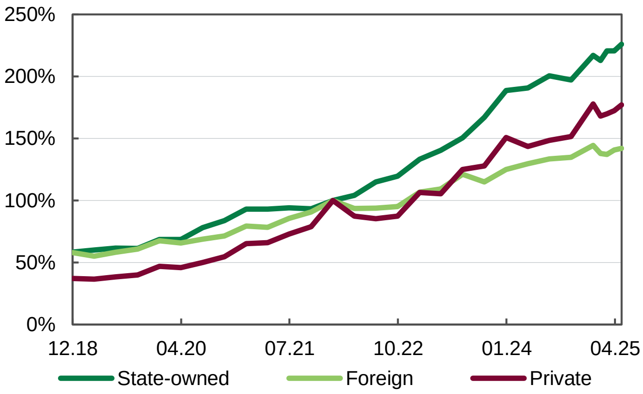
The share of investment-grade funds in the banks' FX HQLAs has dropped to a third. This is due to a regulatory restriction on their inclusion in the LCR, while the volumes of these funds haven't decreased themselves. At the same time, the banks moderately increased their holdings of investment-grade securities, which now account for about half of their total HQLAs. Correspondent accounts in foreign investment grade banks and investments in securities cover approximately 26% of the banks' FX liabilities.

Inflows of customer funds continued to support bank funding

Annual growth in hryvnia corporate and retail deposits at the end of April was 17% and 14% respectively, which was significantly less than last year. This was due to the outflow of retail and corporate deposits at the beginning of the year caused by more active consumption and the payment of taxes and dividends abroad. Overall, after a brisk recovery in business and household incomes in previous years, this process is now slowing down. This slowdown in deposit inflows into the banking system is in line with economic dynamics and does not pose a threat to further growth in bank lending. The amount of FX deposits remained virtually unchanged, while their hryvnia equivalent decreased slightly due to the strengthening of the exchange rate.

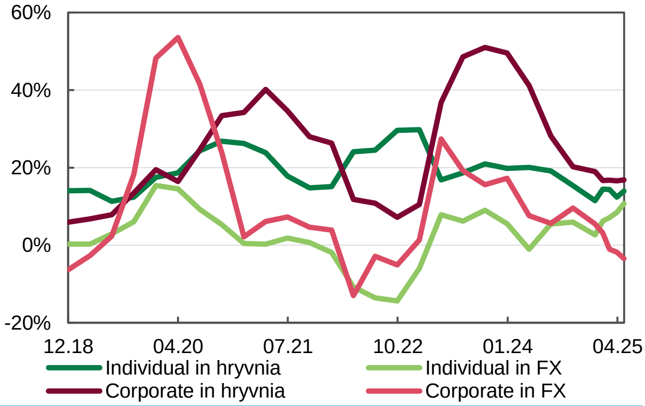
At the same time, competition for depositors is intensifying in the market. This manifests in the converging growth rates of hryvnia deposits among different groups of banks. The growth of corporate and retail deposits at private banks even exceeded the rate of inflows to state-owned banks. This latter

Figure 3.2.4. Hryvnia deposits from business and households by groups of banks, 31 December 2021 = 100%



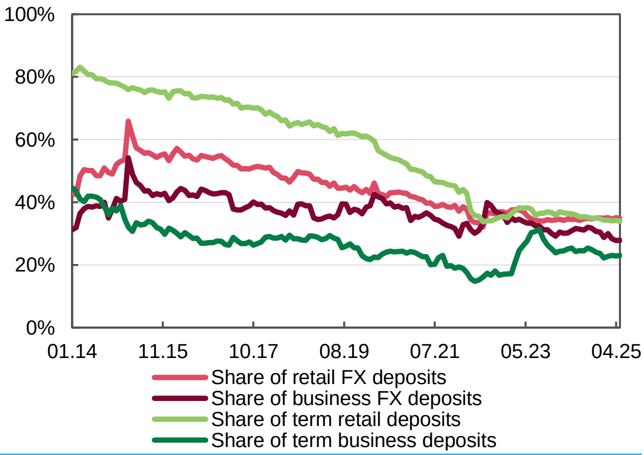
Source: NBU.

Figure 3.2.5. Annual rate of change of corporate and retail deposits



Source: NBU.

Figure 3.2.6. Dollarization rate and the share of term deposits in retail and corporate deposits



Source: NBU.

rate was significantly higher after the full-scale invasion, partly because clients saw state-owned banks as a safe haven, and partly because of the increased role of direct state payments as a source of funds inflows to household accounts. The smooth and effective operation of the banking sector over the past three years has confirmed the reliability of banks across all groups. So now the NBU observes a more even redistribution of deposits between the client accounts at different banks.

Client deposits remained the basis of bank funding – they account for 92% of liabilities, with a slight predominance of corporate deposits. Given stable funding and excess liquidity, the financial institutions still do not require any funding other than client deposits. Although some financial institutions attract funds from IFIs to implement individual projects, their volume remains virtually unchanged, and the share of external funding has remained at historically lowest levels since 2004.

The term and currency structure of deposits remained unchanged in the past six months

Due to noticeably higher average amounts of corporate deposits compared to retail ones, business clients typically have greater leverage over financial institutions. Large corporate depositors impose pricing terms for their accounts based on the NBU's key policy rate. As a result, interest rates on corporate deposits are more sensitive to changes in the key policy rate. In order to retain deposits and client loyalty, the banks were forced to raise interest rates even on current accounts. At the same time, deposit yields do not affect the term structure of corporate deposits. As before, two-thirds of funds remain in current accounts due to the need for access to them for operational activities.

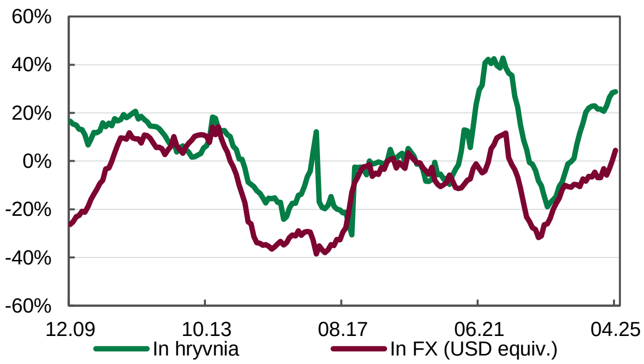
However, even a moderate increase in retail deposit rates revived inflows into term deposits. Accordingly, the share of term hryvnia retail deposits stabilized at around 34%.

The dollarization rate of the banks' liabilities has declined slightly since the beginning of the year, but overall remains close to one-third. Inflows of FX deposits remain lower than those of hryvnia deposits. Dollar-denominated liabilities continue to dominate FX liabilities, accounting for about two-thirds of them. At the same time, the share of the euro is constantly growing – from 26% in December 2020 to 31% in April 2025. In general, the banks continue to expect a further decline in the share of FX deposits, as the options for using these funds remain very limited, and increased reserve requirements restrict the profitability of such deposits for the banks.

3.3. Corporate Lending Risk

Hryvnia lending has reached a pace last seen before the full-scale invasion. Banks of all groups are actively expanding their portfolios, increasingly cooperating with borrowers in industries that are new for them, using a wider range of instruments, including consortium and specialized lending, and providing longer-term loans. Reliance on government support for loans for working capital replenishment is decreasing, while the share of loans for investment purposes in the government's *5-7-9%* program is slowly growing. The implementation of the *Lending Development Strategy* has yielded results. The quality of the new portfolio is high.

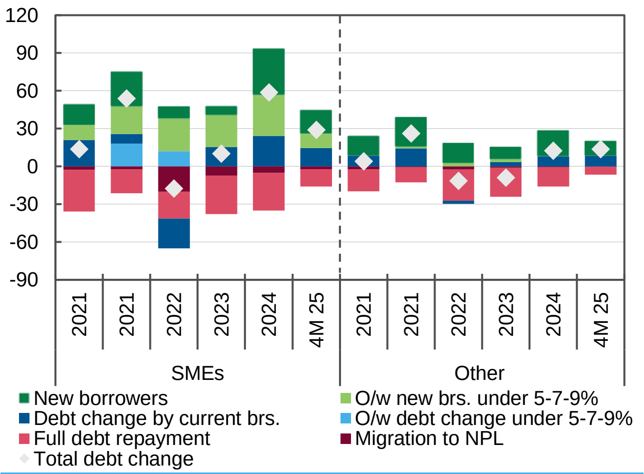
Figure 3.3.1. Annual change in net corporate loans



At banks that were solvent at each reporting date.

Source: NBU.

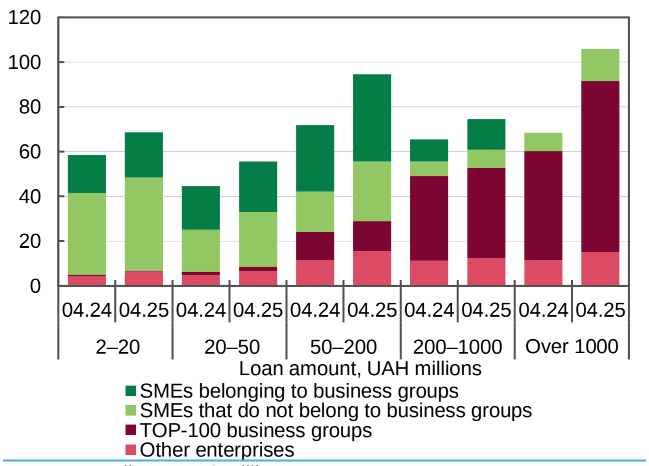
Figure 3.3.2. Change in performing hryvnia corporate loans, UAH billions



Loans exceeding UAH 2 million.

Source: NBU, BDF.

Figure 3.3.3. Net hryvnia loans to businesses by borrower group and loan size, UAH billions



Loans exceeding UAH 2 million.

Source: NBU.

Corporate loans continue to grow rapidly

The growth in the portfolio of hryvnia corporate loans is accelerating, with the annual pace of growth reaching almost 29% in April. Bank surveys indicate that businesses' demand for loans has continued to increase. It is being fueled by both the working capital needs of businesses and the increasingly pronounced demand for capital investment financing. Loans with a maturity of more than a year have grown much faster than shorter-term loans. However, a significant share of enterprises continue to finance their needs without taking out bank loans. In surveys, businesses point to a certain increase in the need for loans, although it remains moderate overall. The growth in the portfolio is driven more by the attraction of new clients rather than an increase in existing clients' debt.

The SME segment remains the driver of loan portfolio growth. SME loans grew by 31% yoy and continue to dominate the portfolio. The dynamics of lending to large businesses have also improved somewhat. Businesses that have been financing their operations primarily from their own resources since 2022 are slowly returning to the use of bank funds.

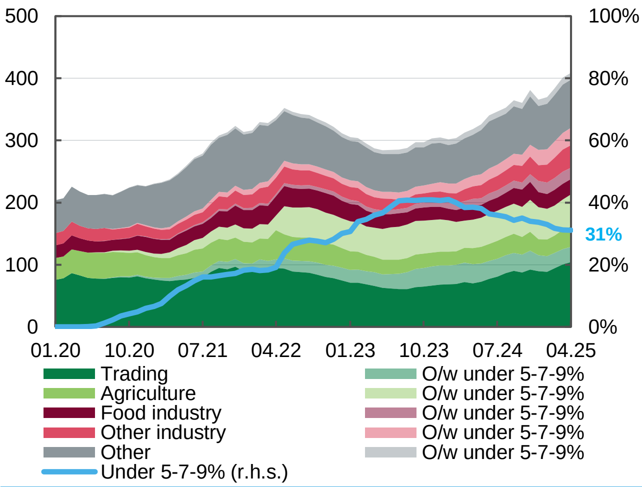
FX lending is still sluggish. The portfolio only recently stopped declining in annual terms. However, this trend is not new – the FX loan portfolio has not grown since 2014. Even before that, growth had been very moderate, and a significant share of the loans granted in foreign currency at that time later became non-performing. The banks are now more realistic in their assessment of clients' prospects for using borrowed funds, and about lending risks. That is why financial institutions lend in foreign currency only if borrowers have income in FX.

Competition between the banks limits lending rates

Banks of all groups are active in lending to businesses. In recent months, portfolio growth has been faster at foreign banks, but the performance of state-owned and private banks lags only slightly behind. Overall, competition in the segment is quite strong. The banks cite competitive pressure as the driver behind the easing of lending conditions over the past year-and-a-half, when portfolio has been growing. Moreover, financial institutions note competition both in the SME segment and in lending to larger companies.

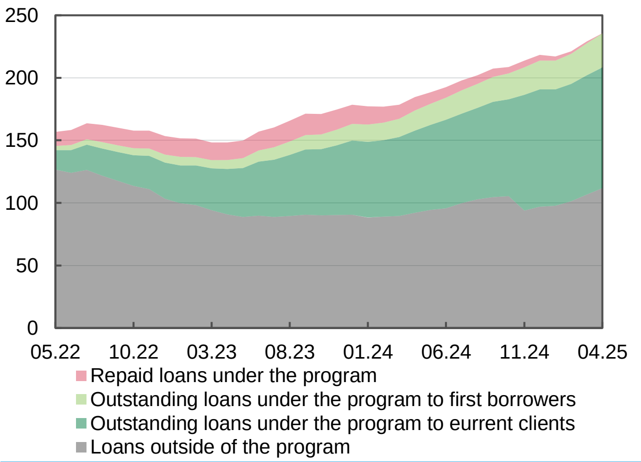
The moderate response of lending rates to changes in the NBU's key policy rate in the last six months is a clear indication of competition. Although the key policy rate increased by 2.5 pp, average lending rates rose by only 1.2 pp, to 15.6% in April. This level allows the banks to further actively attract clients. Although a certain negative impact of rate changes on loan approvals was noted by the banks in

Figure 3.3.4. **Net hryvnia corporate loans, UAH billions**



Source: NBU, BDF.

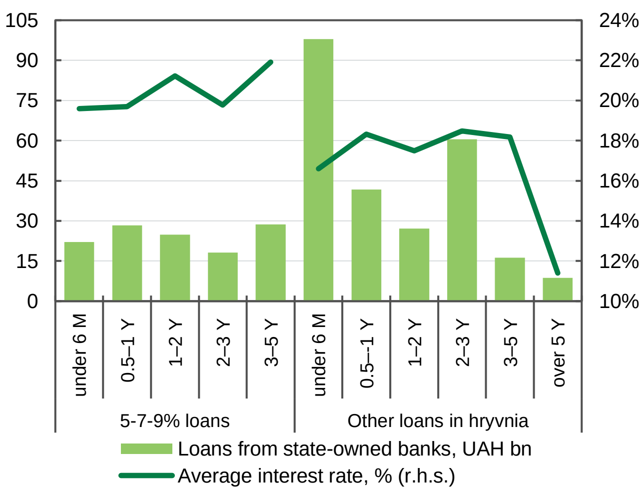
Figure 3.3.5. **Gross loans to 5-7-9% clients, UAH billions**



Loans exceeding UAH 2 million.

Source: NBU, BDF.

Figure 3.3.6. **Performing hryvnia loans to businesses by maturity and effective interest rate**



Loans exceeding UAH 2 million. The effective interest rate is a calculated rate that reflects a constant level of profit (loss) by evenly distributing income and expenses over all periods during the term of the loan.

Source: NBU.

the lending survey, lending conditions did not change overall due to the revision of non-price terms.

The role of state support has weakened significantly

As the banks strive to resume market lending, reliance on state support programs is declining. The share of loans granted under the program *Affordable loans 5-7-9%* has decreased by 7 pp over a year, reaching 31% of net hryvnia portfolio in April. Clients with loans under the program often have other unsubsidized loans with banks. Volumes of subsidized loans for replenishing working capital are decreasing. This is facilitated by previous decisions to refine the program's design: raising the compensation rate for working capital loans and reducing the maximum loan amount. Lending to farmers under the program slowed significantly after the introduction of requirements for the banks to comply with environmental and social standards when issuing a loan. As a result, the share of investment loans increased to a quarter, which is more in line with the essence of the program itself and better targets businesses that need support. In addition, the problem of debts on compensation payments to the banks is still unresolved. Although delays in payments from the government are shorter, the amount of debt is still substantial and is unlikely to decline by the end of this year.

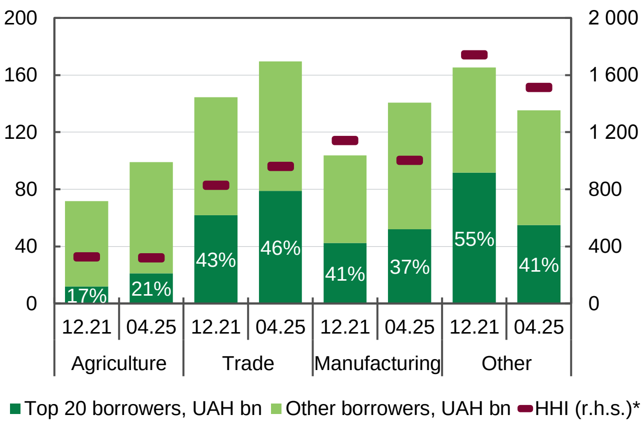
Despite positive developments, the program needs further transformation (read more in Affordable Loans 5-7-9% Program Is Changing Slowly, FSR, December 2024). This primarily relates to eliminating opportunities for the banks to set excessively high loan rates and reducing the margin over deposit rates allowed under the program. Currently, outside the program, interest rates are on average 3–4 pp lower for businesses of all sizes and for loans of all maturities, as the banks adjust loan rates to compete for clients. Another promising area for changes in the program is to further limit working capital lending to companies in industries that are less in need of support.

***Lending Development Strategy* is yielding results**

Agricultural companies and traders remain the banks' main borrowers. These industries have repeatedly demonstrated the highest resilience to crises: they are less affected by shocks and recover faster. At the same time, the banks are increasingly cooperating with clients in less leveraged industries, whose development is now being fueled by structural changes in the economy: the food industry and machinery industry, including defense companies. Loan growth here is more rapid than the average for the portfolio. The banks continue to support state-owned companies, but the share of these loans in the portfolio is moderate, at 15% (10% at the end of 2021). The portfolio concentration by largest clients remains moderate, with concentration being the highest at state-owned banks. At those financial institutions that are growing their portfolios faster, concentration is declining more rapidly. Currently, 20 top private company groups account for 17% of net corporate bank loans. This share has declined by 1 pp since 2021.

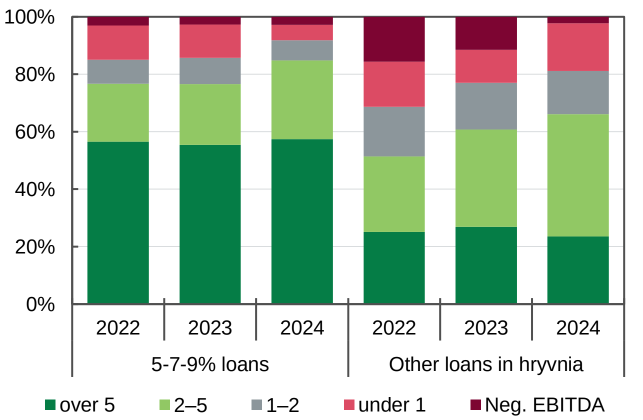
The increase in the loan portfolio in several areas is, among other things, the result of the implementation of the *Lending*

Figure 3.3.7. Net hryvnia business loans by concentration



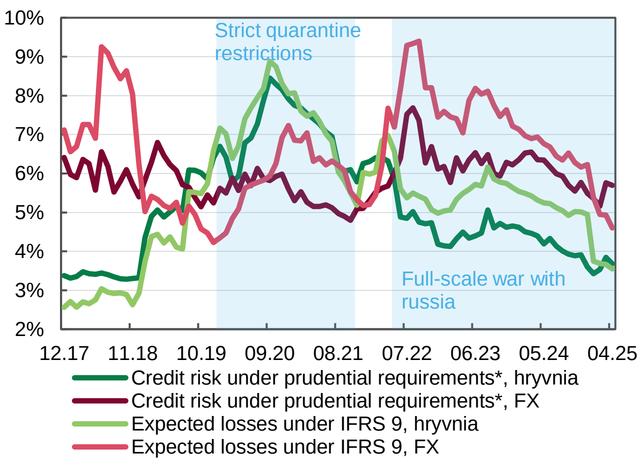
A borrower or a group of related counterparties in individual banks for loans exceeding UAH 2 million.
The Herfindahl-Hirschman Index (HHI) is an indicator of banking sector concentration by industry and by number of debtors. The index ranges from 0 to 10,000, with values below 1,000 indicating low market concentration.
Source: NBU.

Figure 3.3.8. Breakdown of the performing corporate portfolio by EBITDA interest coverage ratio



Loans exceeding UAH 2 million.
Source: NBU, Open Data Portal, BDF.

Figure 3.3.9. Provision coverage of performing corporate loans



* Credit risk according to Resolution No. 351.
Source: NBU.

Development Strategy. The reform roadmap approved a year ago is being successfully implemented. As envisaged by the Strategy, a program to finance defense industry projects was launched at the end of 2024, with a number of private and state-owned banks joining in. Contracts worth about UAH 1 billion have already been signed under the program.

The implementation of the *Lending Development Strategy* facilitated lending to energy projects co-financed by the banks that are signatories to the relevant Memorandum. Over the year since June 2024, the banks have issued UAH 18 billion in loans. The development of energy generating capacities of about 700 MW is already being financed. In this volume, a little less than half are gas-piston cogeneration units and over a third is for the construction of solar power plants.

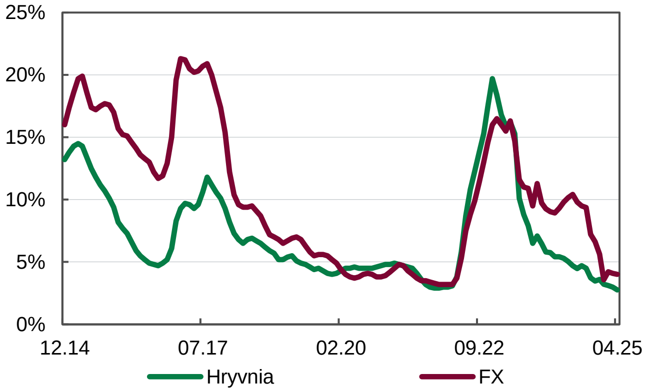
For the first time in a long time, the banks have become more active in financing specialized projects, and consortium loans have also emerged. Such business financing instruments are more difficult to launch, but they often better meet businesses' needs and help with the implementation of large investment projects. It is important that the initiative in this area comes from private Ukrainian banks.

Credit risk is not growing, provisions are being reduced

The banks are managing to increase their portfolio while maintaining its high quality. The debt metrics of debtors with performing loans are good. The weighted average ratio of operating profit to financial expenses for 2024 improved to 3.6x. The average net debt to EBITDA ratio decreased to 4.2x. The business loan default rate has fallen to around 3% over the past 12 months. The coverage of the performing portfolio with IFRS financial and prudential provisions has been declining gradually. For the first time since the full-scale invasion, these two indicators have converged, indicating that the "crisis" period is over and that the banks' expectations are improving. After all, financial provisions reflect expectations for the near future, whereas prudential provisions are neutral to the phase of the economic cycle. In general, the banks are continuing to maintain proper lending standards, which will ensure that risks in the segment are under control as they grow their portfolios.

The update of the NPL definition in accordance with EU standards (read more in Box 3 Changes in Regulatory Requirements for Defining Non-Performing Assets, FSR, June 2024) had an expectedly moderate impact on the indicator, adding about 1 pp to it. However, this did not change the trend: the share of corporate NPLs continued to decline, to 37% – or to 20% excluding legacy NPLs. Almost 90% of the NPLs are covered with provisions. The NPL ratio decreased across all groups of banks, mainly due to portfolio growth and active efforts by the banks to write off and sell non-performing assets.

Figure 3.3.10. Default rate of large borrowers* over 12 months by number, smoothed data



Loans exceeding UAH 2 million.
* According to Resolution No. 351.

Source: NBU.

Table 1. The corporate loan portfolio as of 1 May 2025

No	Sector	Gross performing loans			Loan migration* to NPLs over 12 months		NPL ratio**	Leverage ratio (net debt / EBITDA)*		Interest coverage ratio (EBITA / financial costs)		Structure of loans, 5-7-9% (a total of UAH 123 billion)
		total, UAH billion	o/w SMEs, UAH billion	credit risk coverage	by number	by debt amount		2023	2024	2023	2024	
1	Agriculture	105	88	3.3%	1.8%	1.7%	13%	3.9	2.5	3.8	5.1	39.8%
2	Wholesale trade in grain	25	9	4.5%	6.4%	5.4%	37%	5.5	4.8	2.3	2.9	1.6%
3	Trade in petroleum products	28	19	6.4%	9.3%	4.1%	4%	6.9	3.4	1.3	4.5	1.9%
4	Other wholesale trade	79	59	4.0%	2.9%	2.3%	12%	4.1	4.1	3.4	3.2	15.0%
5	Retail trade	23	6	4.5%	0.5%	0.0%	17%	2.6	2.6	3.9	3.9	1.2%
6	Food industry	46	24	4.1%	1.8%	1.6%	13%	4.0	4.1	4.2	3.9	10.9%
7	Production of vegetable oil and animal fats	24	10	2.0%	0.0%	0.0%	6%	5.0	2.6	3.0	3.8	1.3%
8	Mining	5	1	5.0%	14.3%	10.0%	29%	3.6	2.8	3.5	3.1	0.1%
9	Metals industry	10	7	3.8%	2.3%	8.8%	45%	3.3	3.6	3.8	3.8	3.2%
10	Machinery industry	15	7	2.4%	2.5%	0.7%	15%	6.9	4.7	4.2	4.2	3.3%
11	Chemical industry	12	9	2.7%	1.7%	0.9%	4%	2.7	3.4	5.0	4.5	4.5%
12	Production of construction materials	6	3	3.7%	3.3%	3.3%	15%	5.4	4.4	4.3	4.1	1.6%
13	Light industry	3	3	4.0%	5.0%	8.5%	14%	4.2	6.3	4.9	3.7	1.2%
14	Other manufacturing sectors	12	10	2.3%	1.6%	0.5%	11%	3.0	3.2	5.7	5.7	4.0%
15	Electricity supply and public utilities	11	7	6.4%	5.4%	0.9%	32%	5.8	3.3	3.9	4.4	1.2%
16	Green energy	9	5	5.7%	7.2%	10.2%	65%	6.2	2.4	2.7	5.2	0.5%
17	Real estate transactions	14	9	6.2%	2.4%	2.8%	44%	7.8	7.3	1.9	2.0	0.2%
18	Commercial real estate	8	7	5.3%	2.1%	0.3%	84%	5.3	5.6	2.5	2.5	0.3%
19	Transportation	16	11	3.2%	3.7%	3.5%	18%	2.6	3.6	4.1	3.8	3.7%
20	Construction	7	4	4.1%	3.3%	7.1%	53%	5.9	2.8	4.1	5.1	2.1%
21	Financial services	20	19	0.6%	6.5%	0.2%	24%	2.8	7.4	0.7	1.5	0.1%
22	Other	25	10	6.6%	4.4%	3.2%	43%	3.5	3.8	3.6	3.7	2.2%
23	State-owned companies	76	13	2.4%	0.0%	0.0%	8%	6.1	5.7	1.9	2.5	0.0%
	Total	578	345	3.8%	2.7%	2.0%	25%	4.6	4.2	3.2	3.6	100%

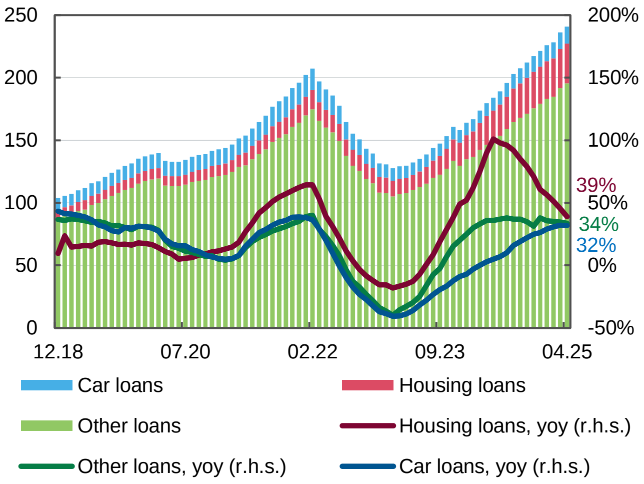
* Share of the total number or amount of debt of borrowers that defaulted within 12 months, as required by Regulation No. 351.
** Excluding non-performing loans of PrivatBank related to former shareholders and their affiliates.

Source: Open Data Portal, NBU.

3.4. Retail Lending Risk

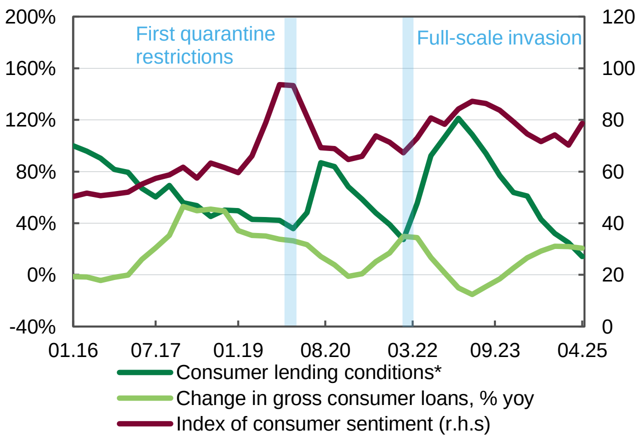
The retail loan portfolio continues to grow steadily, driven by sustained consumer demand from households and the banks' willingness to lend amid improving macroeconomic conditions. Mortgage lending continues to depend on the terms of the *eOselia* program. A revision of these terms should give a new boost to the development of market products. Households' debt burden is moderate and portfolio quality indicators are acceptable. The banks continue to take a prudent approach to provisioning.

Figure 3.4.1. Net hryvnia loans to households, UAH billions



Source: NBU.

Figure 3.4.2. Lending conditions and growth rates of consumer loans



* The line reflects the cumulative change in the balances of responses to the quarterly Bank Lending Survey question about how the criteria for approving household loan applications have changed during the current quarter. An increase in the indicator points to a tightening in lending standards.

Source: NBU, Info Sapiens, monthly surveys of households (respondents aged 16+).

Banks are quickly building up retail loans

The net retail loan portfolio has been growing at a consistently high rate for the second straight year, and is up 34% yoy. The portfolio volume has doubled from the low of 2022. All the portfolio's components have been growing at almost the same rate. Consumer loans clearly dominate the portfolio structure. The volume of this segment is growing due to both an increase in the number of clients and a rise in the average loan size. The mortgage portfolio is growing somewhat faster than the unsecured portfolio, but this increase has decelerated because of a higher comparison base and a slowdown in the *eOselia* program. The growth in car loans has been the slowest so far, but it is picking up.

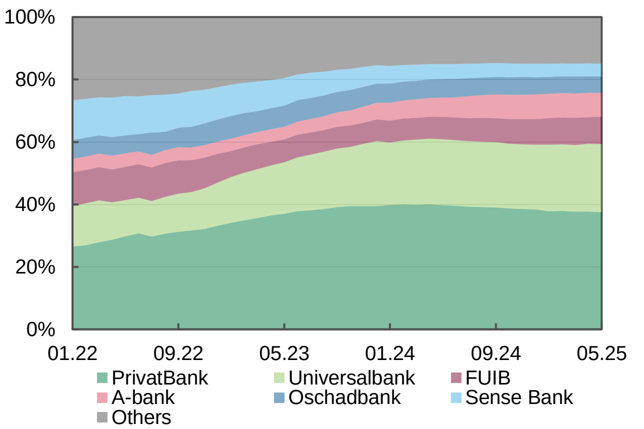
The main driver of demand for consumer loans is further growth in consumption thanks to higher incomes and the maintenance of high consumer sentiment. As households have already become accustomed to using credit funds both to meet current needs and to make more expensive purchases, demand for consumer loans will persist. The banks are expecting that demand for loans will rise, the Bank Lending Survey shows. The banks' willingness to meet this demand is shaped by their assessments of the economic outlook. Lending plunges when economic shocks hit, such as the COVID-19 crisis or the full-scale invasion. As expectations improve, the banks' appetite for lending revives, and they simplify access to their loans. The banks view the current market situation as favorable, a perception reflected in the portfolio's rapid growth. Loan penetration is currently low, leaving significant room for further growth.

Mortgage portfolio developments are more inert than the rest of the retail portfolio. Having sustained significant shocks, the banks need more time before they can resume lending. Although real-estate market conditions have improved since the shock of the full-scale invasion, market-based mortgage lending is recovering extremely slowly. The main reason is its low competitiveness compared to *eOselia* products. An overhaul of the state support program should give the segment a boost by launching a mechanism that reimburses the difference between *eOselia* mortgage rates and market rates. This will allow the banks to set lending rates that can compete with market conditions, while making it possible for clients to enjoy cheaper loans. A number of other steps necessary to improve mortgage conditions are outlined in the draft *Mortgage Lending Development Strategy* (see Box 1. Vision of the Mortgage Lending Development Strategy). The strategy's adoption and implementation will help the mortgage portfolio grow.

Banks compete intensely in retail lending

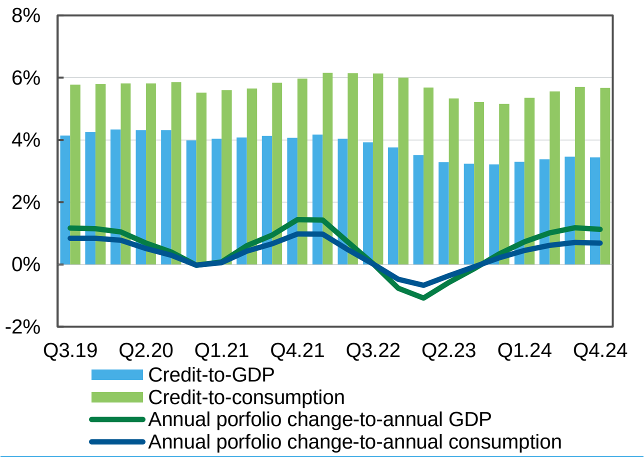
The retail portfolio's concentration surged because of the portfolio's reduction in 2022. Concentration remains relatively

Figure 3.4.3. Breakdown of net unsecured retail portfolio by bank



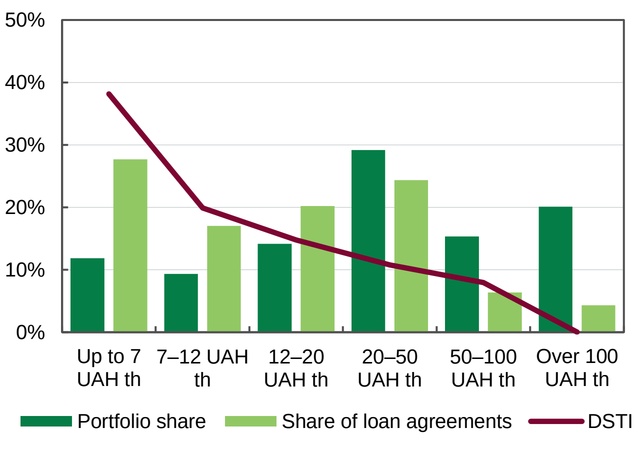
Source: NBU.

Figure 3.4.4. Gross retail credit to annual GDP and consumption ratios



Source: NBU, SSSU.

Figure 3.4.5. Portfolio composition and DSTI by income group of borrowers as of 1 April 2025



Only borrowers with verified incomes are included.

Source: NBU.

high but is gradually declining. The majority of large banks, universal ones in particular, have plans to actively scale up unsecured lending. Under favorable macro conditions, this portfolio significantly improves the banks' profitability due to yields being consistently high and credit losses low. An additional motivation to expand this high-yield portfolio is the anticipated decrease in market rates within other segments, following a slowdown in inflation and a loosening of monetary policy. Consequently, competition in the segment is gathering strength. To at least maintain their market share, banks are investing in improving mobile applications, actively advertising their products, and offering better conditions to active users: lower rates, higher limits, additional cashback, and so on.

State-owned banks issue two-thirds of loans in the mortgage segment. The same institutions dominate the *eOselia* program. Due to the fixed low margin for banks, the program remains more of a social project. Although a dozen financial institutions are registered with the program, most of them seldom grant any mortgages. A number of large private banks that used to be active players in this market before the full-scale war have yet to resume their mortgage programs. Without an incentive to develop market products that would be partially subsidized, competition in the segment is unlikely to revive.

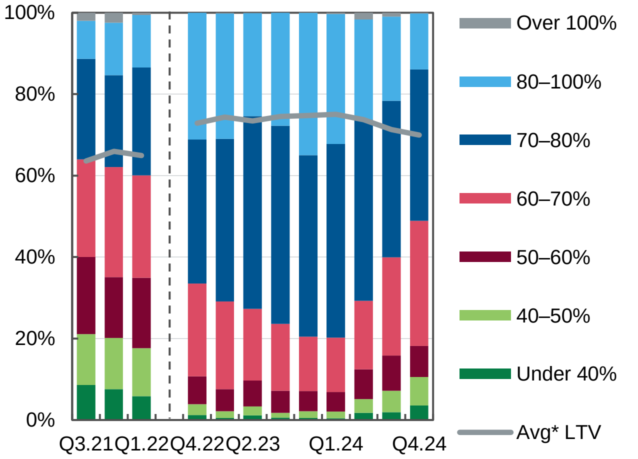
Car loans are made in a way that relies on direct sales through dealerships, the reason the portfolio continues invariably to be formed by four banks. Two of these are state-owned. The rest of the banks are not even launching relevant programs.

Client debt burden is acceptable

The ratio between bank and non-bank gross retail loans and households' income has edged higher, but is only 10%, and 8% for unsecured loans. Such a low debt burden of households is generally attributable to their moderate exposure to credit products (mainly mortgages), and the small size of unsecured loans. The debt burden of bank borrowers is higher. Truth be told, the banks primarily look at the debt-to-income ratio when granting mortgages. In the unsecured segment, the banks rarely focus on debt metrics. To assess future payment discipline, the banks look instead at customers' behavior, including their loan-servicing record, frequency and location of purchases, average receipt size, and more. According to financial institutions, they have reliable data on client income for only 40% of the performing portfolio. This indicator varies greatly across banks: one of the largest lenders does not have any confirmed data on borrower income at all, while other banks know everything about almost all of their clients' incomes. Low attention to borrower income increases the risk of excessive debt burden being carried by some of the clients.

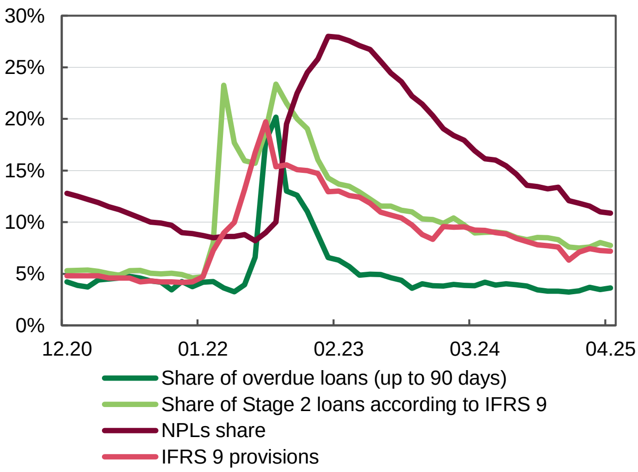
The average Debt Service to Income (DSTI) ratio of clients whose incomes have been confirmed by the banks is close to 20%, which is a good level. Mortgagees have a higher DSTI of about 40%. The average loan size rises with income. The debt burden is higher for low-income clients, but their share in the portfolio is marginal. Among clients whose

Figure 3.4.6. New mortgage distribution by LTV at origination



* Average, weighted by the number of loans issued.
Source: NBU.

Figure 3.4.7. Selected metrics of the retail loan portfolio quality



Provisioning equals the ratio of provisions to gross loans.
Source: NBU.

income is known to the banks, two-thirds are individuals with incomes over UAH 20,000 per month. Overall, the debt burden indicators of bank clients have not changed significantly from their pre-COVID-19 levels (see Households and Related Risks, FSR, June 2020). So, despite a certain easing of lending standards that the banks mentioned in the bank lending survey, the retail portfolio's metrics remain satisfactory.

Down payments for mortgages are rising

The volume of secondary-market mortgages has declined since a limit was imposed on the age of housing eligible for *eOselia* mortgages. On average, the cost of new housing is significantly higher than the maximum loan amounts under the program. This is driving a rise in down payments. The banks are increasingly granting mortgages with down payments over 30%. As a result, the average loan-to-value (LTV) ratio shrank to about 70% from around 80% a year ago. Reducing the LTV ratio while keeping the average mortgage size and customer debt burden unchanged mitigates portfolio risks.

Retail portfolio quality is consistently acceptable

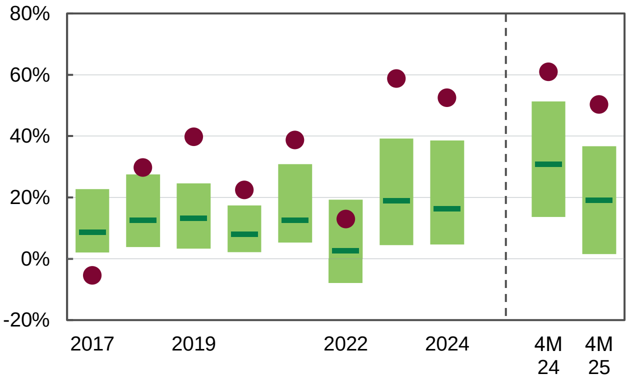
Despite the rapid growth in the portfolio, its quality remains unchanged. The share of loans overdue by less than 90 days is sustainably low, at 4%. The segment's NPL ratio therefore decreased as well. Financial institutions are still expecting the quality of retail loans to deteriorate slightly within one year, the bank lending survey showed. The banks therefore continue to take a conservative approach, maintaining their provisioning levels at 7% of the performing portfolio.

Under EU standards, when assessing capital adequacy, retail loans may be assigned reduced risk weights. However, taking into account historical data on consumer portfolio losses, primarily those on unsecured loans, and to maintain the banks' resilience to risks in the segment, the NBU decided to keep risk weights for unsecured consumer loans at 100%, while reducing them to 45% for mortgages. The updated requirements for credit risk weights will take effect in 2026. To some extent, such a decision ensures that the macroprudential goal – limiting excessive portfolio growth without having an adequate capital buffer in place – is achieved.

3.5. Profitability Risk

The banks are continuing to make profits, although their returns are more moderate than in the previous two years. High net interest margins underlie the profitability. The rebalancing of portfolios in favor of loans and domestic government debt securities in previous periods ensured stable returns on operations. Pressure on margins mostly comes from higher interest rates on corporate deposits. The share of fee and commission and trading incomes in the banks' revenues remains unchanged. The banks are forced to increase their operating expenses, which worsens the operational efficiency of some institutions. Despite this, the sector's overall operational efficiency indicators remain high.

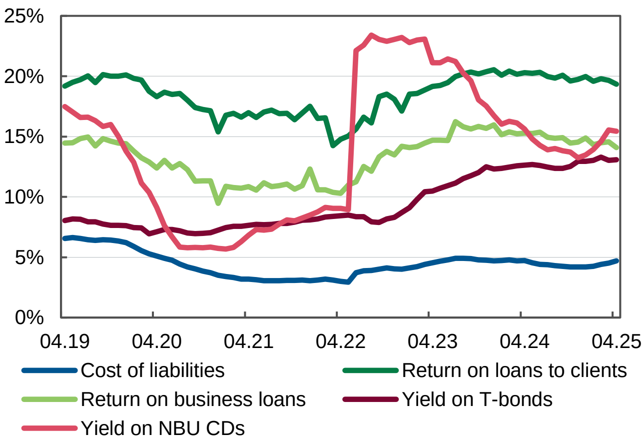
Figure 3.5.1. Return on equity based on profit before taxes



The upper and lower edges of the rectangles correspond to the distribution's first and third quartiles. The dashes inside the rectangles show the median. The dot is the mean. At banks solvent as of 1 May 2025.

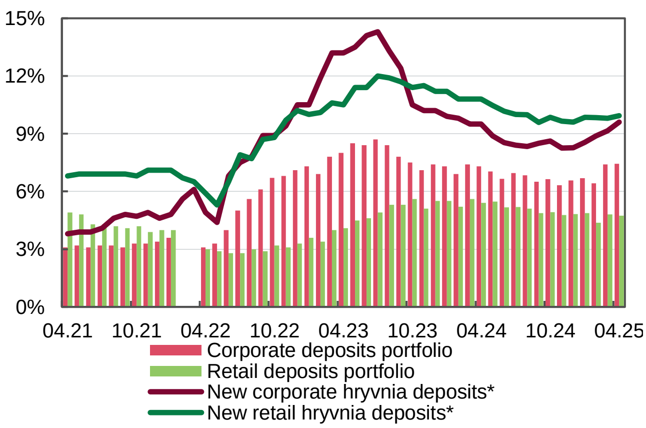
Source: NBU.

Figure 3.5.2. Yield on assets and cost of liabilities



Source: NBU.

Figure 3.5.3. Cost of corporate and retail funding in hryvnia, % per annum



Interest rate on deposit portfolio and liabilities data for February–March 2022 were not submitted. * No loan rescheduling or any other amendments to contractual terms.

Source: NBU.

The banks' profitability is declining moderately

Bank profitability is exceeding historical averages thanks to sustained high interest margins and operational efficiency. However, their profitability is slowly declining if we evaluate the dynamics based on pre-tax profit to exclude the effect of tax rate changes. In Q1 2025, the average return on equity before tax was about 50%, and was 10.7 pp lower than in the same period last year.

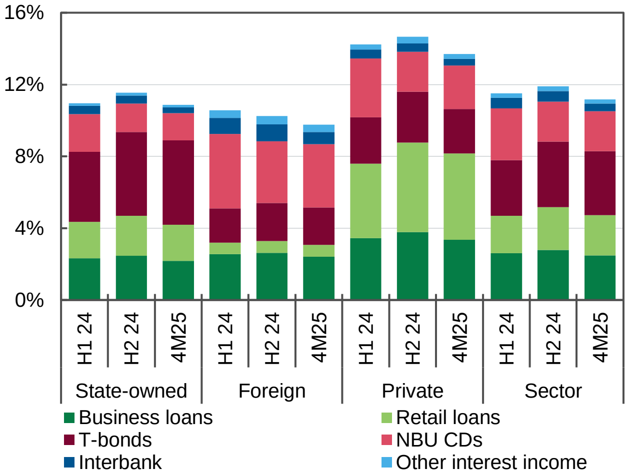
However, after the windfall income tax at the rate of 50% for 2024 was counted in, the sector's profitability was 25%, which is lower than in the "pre-war" year of 2021. The practice of retroactive taxation at an increased rate remains a significant challenge, worsening the business climate. It increases uncertainty for the banks, complicates capital planning, and restrains their investment plans and capacity for further lending growth.

The return on banks' assets barely increased due to the higher cost of liabilities

In December last year, the NBU began raising its key policy rate and subsequently revised the operational design of its monetary policy, increasing the spread between the interest rate on three-month certificates of deposit and overnight instruments. In response to these changes, hryvnia retail deposit rates rose in the spring. Given the average maturity of deposits, the increase in interest rates will affect the cost of hryvnia funding from households with a lag of up to six months. At the same time, the banks continue to use households' current deposits mainly free of charge. Therefore, interest rates on retail hryvnia deposits have hardly increased. On the other hand, interest rates on new corporate deposits have risen significantly. Businesses took advantage of the strong competition among banks for funding to obtain better deposit terms. This increased the cost of corporate funding for banks to 7% per annum and put the major pressure on interest margins.

Yields on certificates of deposit have increased since December last year, as the NBU tightened monetary policy in response to inflationary risks. However, on average, the share of these instruments in assets in the first five months of this year was lower than last year. Therefore, the contribution of investments in certificates of deposit to the return on bank assets did not change. Yields on domestic government debt securities have risen: interest rates on newly placed securities grew, and older redeemed securities were replaced with new ones offering higher yields. In particular, low-yield domestic government debt securities held in the capital of state-owned banks were redeemed. The share of domestic government debt securities in assets also

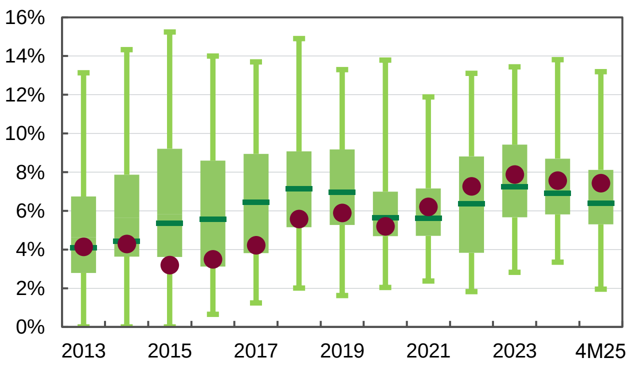
Figure 3.5.4. Interest income of banks, in % of net assets



Annualized data.

Source: NBU.

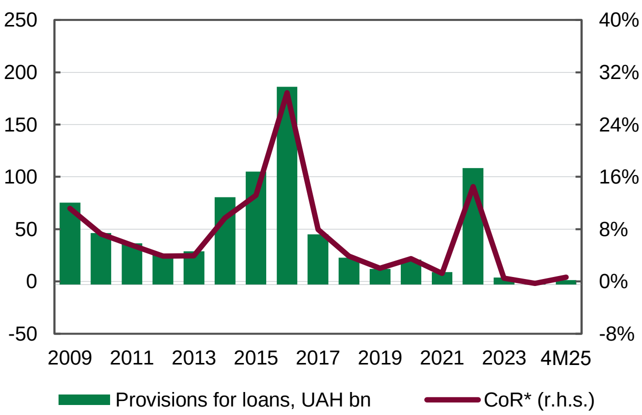
Figure 3.5.5. Net interest margin of banks



The upper and lower edges of the rectangles correspond to the distribution's first and third quartiles. The dots indicate the mean. The upper and lower dashes outside the rectangle indicate the 5th and the 95th percentiles.

Source: NBU.

Figure 3.5.6. Cost-of-Risk (CoR)



* Ratio of loan loss provisions in the respective period to the net loan portfolio.

Source: NBU.

grew. Thus, overall, the contribution of domestic government debt securities to the return on bank assets increased.

Interest income from lending to clients makes the most stable contribution to the overall profitability of banking operations. In recent months, despite changes in monetary conditions, the banks have only moderately raised loan rates to maintain the competitiveness of their products. Compared to last year's averages, loan rates have, on the contrary, decreased, primarily interest rates on corporate loans. The increase in lending volumes offset the decline in interest rates. In general, the overall return on assets was almost unchanged. The growing role of lending and investments in domestic government debt securities compared to certificates of deposit makes the banks' profitability more resistant to changes in monetary policy.

The banks' net interest margins have narrowed

The almost unchanged yield on assets, combined with a rise in funding costs slightly decreased the net interest margin, from 7.6% last year to 7.4% in the first four months of 2025. Large financial institutions are somewhat better at adapting to changes in market rates, maintaining margins at a comfortable level for themselves. In particular, the net interest margins of the three largest state-owned banks increased slightly.

The lagged effects of the key policy rate hike may have only a moderate impact on bank margins. A possible transition to key policy rate cuts by the end of the year will change the risk factors for bank margins. The main threat will be the rapid response of yields on risk-free instruments to changes in monetary conditions. The banks will be able to maintain their profitability under these conditions by actively expanding their loan and government securities portfolios.

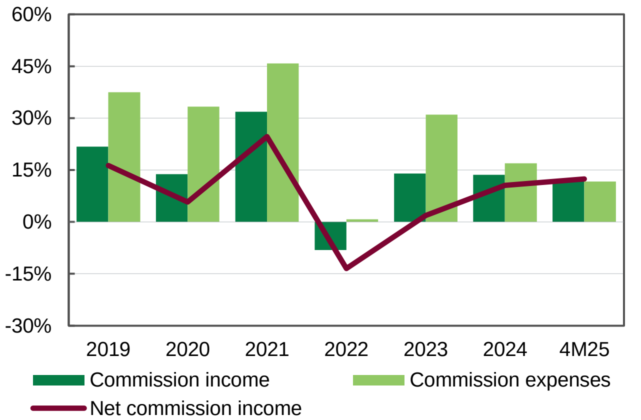
The banks' credit losses are moderate

A stable macroeconomic environment and appropriate credit risk assessment standards are helping the banks maintain high credit quality. The banks do not have to worsen the parameters for calculating loan loss provisions. At the same time, the effect of conservative provisioning in previous years has already worn off: there is almost no room left for releasing provisions for the existing portfolio. Therefore, looking ahead, provisions will change mainly due to the growth of loans. The cost-of-risk (CoR) for loans rose this year to 0.6% yoy. Due to the stability of volume of investments in domestic government debt securities, the banks spent almost nothing on additional provisioning for these securities, so provisioning expenses are almost entirely driven by expected credit losses. The banks' interest margins allow them to painlessly cover total provisioning.

Fee and commission and trading incomes account for over a quarter of the banks' total revenues

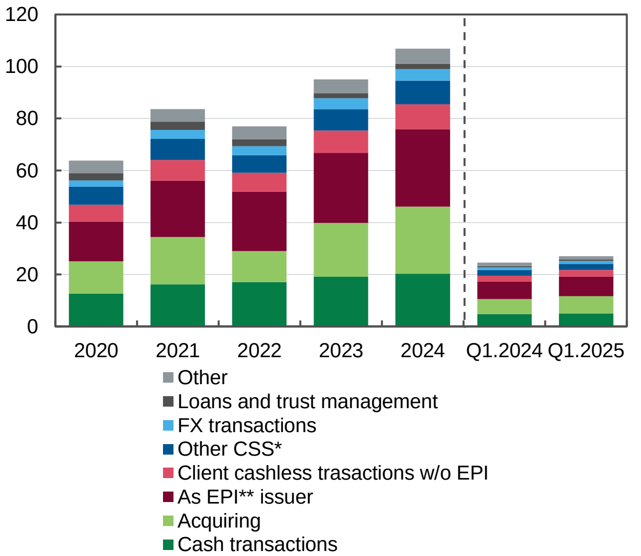
The growth rate of net fee and commission income is close to 12% for the first four months of 2025 year-on-year. This is close to last year's figures. The share of fee and commission income in operating income is also stable, at just over 17%. The growth in fee and commission income has stabilized, and its volume has already exceeded pre-full-scale invasion

Figure 3.5.7. Annual change in fee and commission income and expenses



Source: NBU.

Figure 3.5.8 Components of the fee and commission income of top-20 market participants, UAH millions



Data from a survey on fee and commission income and expenses of the top-20 banks in terms of net fee and commission income. * CSS – cash and settlement services. ** EPI – electronic payment instruments.

Source: NBU.

levels. This is despite the fact that some banks lost their fee and commission income due to the halting of some operations and the tightening of AML/CFT control. The growth is primarily driven by an increase in client transactions, while tariffs have not been significantly revised. Fee and commission expenses are growing in proportion to income, albeit less evenly. The contribution to the banks' income from trading operations (primarily the revaluation of securities) and FX purchase and sale remains stable. Going forward, the decrease in interchange rates to levels close to those seen in the EU countries by the end of 2027 will have a moderate impact on the banks' fee and commission income.

Maintaining high margins allows for covering necessary operating expenses

The banks are incurring higher operating costs – in the first four months of this year, these costs rose by 22% compared to the same period last year. First and foremost, labor costs are rising in order to retain skilled workers in the face of staff shortages. The maintenance, restoration, and upgrading of fixed assets, along with the development of payment infrastructure, also require additional expenses. The growth in operations and the maintenance of high interest margins enable most banks to incur the necessary expenses without jeopardizing their operating efficiency. The cost-to-income ratio (CIR) in the sector remains at an average of up to 40%.

Although the vast majority of financial institutions, especially large ones, maintain good CIR indicators, the number of loss-making banks has increased to eleven. These are small banks, five of which were making operating losses at the beginning of 2022. These banks' operating losses arise from long-standing problems with inefficient business models. The normalization of market conditions and stronger competition are exposing these flaws. However, due to their small size, these banks are not affecting the stability and performance of the sector.

Box 2. Wartime Recovery Plans of Most Banks are Acceptable

In 2024, for the first time since the start of the full-scale invasion, Ukrainian banks submitted recovery plans. The banks updated the documents to reflect wartime realities, including revising the list of indicators for risk monitoring, making stress scenarios more detailed, and expanding the list of recovery measures. However, the recovery plans of many banks had shortcomings: an incomplete system of indicators, financial indicators that are not sensitive to external shocks, and proposed recovery measures that could not always be implemented to achieve the declared effects in a crisis. The NBU provided the banks with recommendations to improve their recovery plans in the future.

Most banks prepared acceptable recovery plans at the first attempt

An effective response by the banks to the unfolding crisis is always the result of systemic preparations, including the drawing up of recovery plans. Each of these documents contains an assessment of the impact of hypothetical crises on a bank's financial condition, a system of indicators to trigger an early response to such crises, and a list of measures to improve the financial institutions' soundness. Adverse hypothetical scenarios that underlie recovery plans complement regulatory stress tests and have important special features:

- they must necessarily cause a breach of regulatory capital and liquidity requirements by banks – reverse stress testing may be used as a basis.
- they should take into account the bank's business model and include specific risks, particularly those related to key counterparties and bank functions. This kind of modeling better reflects the risk profile of a specific financial institution.

The drawing up of recovery plans has been an integral part of Ukrainian banks' risk management systems since 2020. After the full-scale invasion, the NBU did not require the banks to update these plans annually. During the deep crisis caused by the war, the banks' efforts were aimed at restoring their financial health, including the implementation of previously developed recovery plans (see How Banks Prepared for Working under Emergency Conditions, FSR, June 2022).

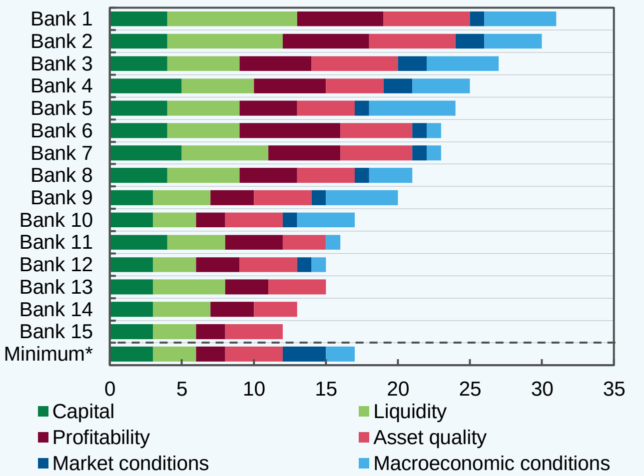
In 2024, the NBU once again required the banks to update their recovery plans in view of the stabilization of the economy. However, the banks were to apply only one market-wide stress scenario (as opposed to three or four under the standard requirements). The NBU recognized the recovery plans of 35 banks as acceptable. These financial institutions took into account the regulator's previous recommendations in their recovery plans: they refined the list of indicators for risk monitoring, developed more detailed scenarios, and expanded the list of recovery measures. The plans of the remaining 25 banks had significant shortcomings that the financial institutions were to eliminate by June.

The system of indicators does not fully take into account the specifics of the banks

To monitor the financial health in their recovery plans, the banks use a system of indicators based on the traffic-light principle: the values of the indicators can fall into the "green zone", "yellow zone" or "red zone". Under normal conditions, the values of the indicators are in the "green zone". The falling of an indicator into the "yellow zone" is a signal that certain plan measures need to be taken. An indicator falling into the "red zone" means there is a stress event that requires the immediate implementation of a recovery plan.

The banks include indicators of macroeconomic and market conditions, capitalization, liquidity, profitability, and asset quality into the traffic-light system. For all banks, the system of indicators includes a minimum required list, including capital and liquidity ratios. This year, some systemically important banks supplemented the system with deposit outflows and other liquidity metrics, cost-to-income ratios (CIR), and losses from operational risk. However, the banks failed to pay proper attention to macroeconomic factors that have a direct impact on their operations. Ignoring indicators that are important to the banks limits the ability of financial institutions to effectively monitor their activities.

Figure B.2.1. Number of "traffic light" indicators in systemically important banks

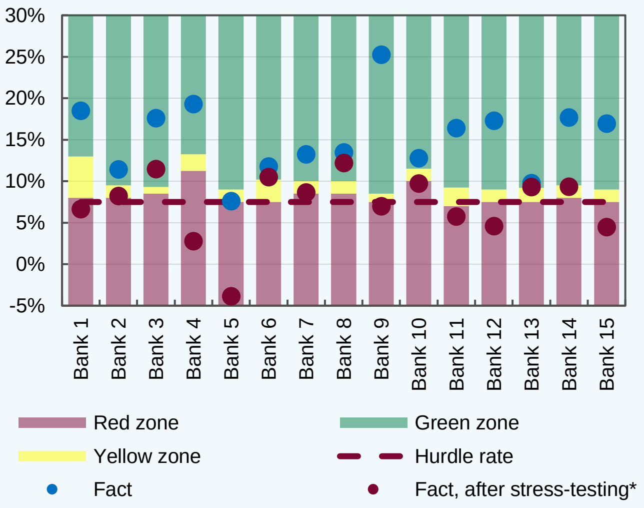


* Minimum required list of indicators in line with Regulation on recovery plans of Ukrainian banks and banking groups (Regulation No. 95).

Source: banks' data.

Also of note is that the banks often set the "yellow zone" and "red zone" thresholds for capital and liquidity ratios close to the minimum prudential requirements. If the thresholds are too low, it makes it unlikely that the banks will respond to their deteriorating financial health in a timely manner.

Figure B.2.2. Tier 1 capital adequacy ratio (broken down by banks)



* If there is more than one scenario in a bank's recovery plan, the most conservative one is indicated.

Source: banks' data.

The banks' stress scenarios are quite conservative, but the banks' sensitivity to shocks is underestimated

In their recovery plans, the banks have focused on scenarios in which there is a significant deterioration in security risks. Given their high capitalization and liquidity, the banks often have to assume a very deep crisis before they breach the minimum requirements. For systemically important banks, the median decline in real GDP is 11%, for that in inflation it is 20%, and for that in the annual depreciation of the hryvnia vs the US dollar it is 24%. This is significantly worse than the adverse scenario assumed in this year's NBU stress test.

The materialization of stress scenarios decreases the banks' Tier 1 capital adequacy ratio by 8.5 pp on average in the recovery plans. This is significantly more than the 2 pp reduction in the adverse scenario under the normative perspective in the ICAAP, but is comparable to the results of the NBU's 2019 and 2021 resilience assessments, which had much softer macroeconomic assumptions.

Table 2. Parameters of stress test scenarios, % change

Indicator	2024	2025 resilience assessment	Stress scenarios included in recovery plans*		
			Min	Median	Max.
Real GDP	2.9	(-3.1)	(-50.0)	(-11.4)	0.0
CPI	12.0	17.9	16.0	20.0	105.0
Exchange rate**	(-9.6)	(-11.9)	(-57.5)	(-24.0)	(-9.1)

* If there is more than one scenario in a bank's recovery plan, the most conservative one is indicated. ** UAH/USD exchange rate.

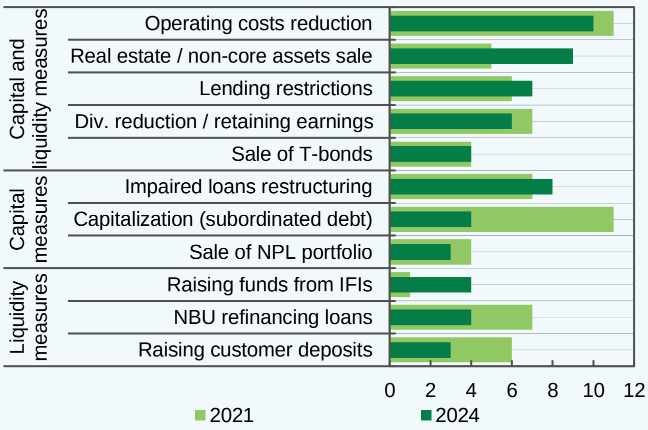
Source: NBU estimates.

The conservatism of macroeconomic assumptions is often the result of the banks underestimating the sensitivity of their financial performance to external shocks. For example, some banks did not anticipate the materialization of interest rate risk during a crisis, did not revaluate their financial instruments, and did not take into account the effects of maturity mismatches in assets and liabilities. In adverse scenarios, the banks' net interest margins decline by only 2 pp on average, which is comparable to the baseline scenario of the 2023 resilience assessment. Another shortcoming was that the banks only rarely assumed failures of critical counterparties. Not all financial institutions have consistently integrated assumptions about deposit outflows into their macroeconomic scenarios.

A number of bank recovery measures will take time, and their effects are uncertain

In their recovery plans, systemically important banks on average selected five measures that sometimes simultaneously improve both capital and liquidity. The most popular measures included cutting operating expenses, selling real estate and non-core assets, and restructuring NPLs. Such measures are sometimes difficult to implement in a short time frame, and their effectiveness is lower under stressed conditions. In particular, in a crisis, real estate or other assets can only be sold at a significant discount, cost cutting may adversely affect the bank's operational resilience, and restoring the quality of non-performing loans even after restructuring takes a long time, especially under stressed conditions. At the same time, the banks do not pay enough attention to analyzing and testing options for restoring capital and liquidity, such as additional capitalization by a shareholder or taking refinancing loans from the NBU.

Figure B.2.3. Recovery measures, by number of banks



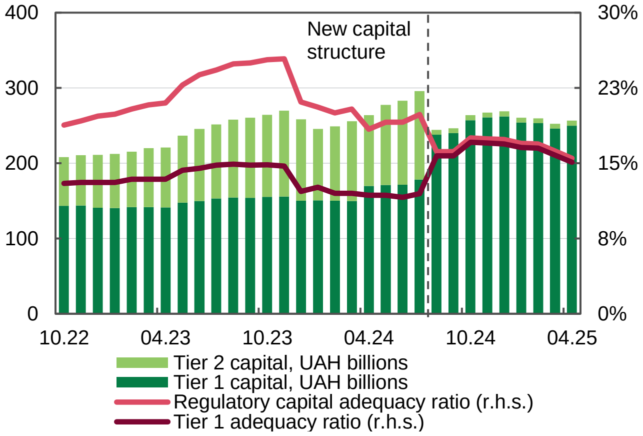
Source: banks' data.

The NBU has once again provided the banks with recommendations to improve their recovery plans and boost their resilience in the future. First of all, the banks should supplement their systems of indicators with metrics that take into account the specifics and scale of the financial institutions' operations and calibrate the thresholds of indicators on the basis of their current values and business plans. Stress scenarios should contain assumptions about all risk factors relevant to a bank, and crisis modeling should take into account the actual sensitivity of the bank's indicators to them. The list of options for bank recovery should be expanded, taking into account the limited ability to implement certain measures in a severe crisis. Starting in 2025, the banks will have to expand the list of stress scenarios in their recovery plans. Looking ahead, systemically important banks and banks that are responsible entities of banking groups will be required to update their recovery plans annually, while other financial institutions will have to do it every two years.

3.6. Capital Adequacy Risk

The banks have maintained sufficient capital cushion to ensure resilience and continue lending. However, the second retroactive increase in the corporate income tax for the banks slightly reduced their capital adequacy compared to the start of the year. Several updates to capital requirements are planned for this year and next year, primarily updates of credit risk weights and the introduction of a leverage ratio. These changes will harmonize Ukraine's prudential requirements with EU standards without putting additional pressure on the banks' capital, and will in some cases even ease the pressure, facilitating lending. The results of this year's resilience assessment will help determine the schedule for the introduction of capital buffers.

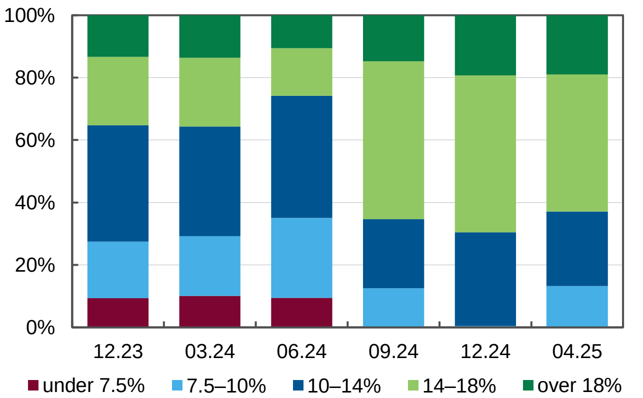
Figure 3.6.1. Components of regulatory capital and regulatory capital adequacy ratio



Before August 2024, the figure shows core and additional capital instead of Tier 1 and Tier 2 capital, respectively. Instead of Tier 1 and regulatory capital ratios, it shows core and former regulatory capital adequacy ratios as the closest proxies.

Source: NBU.

Figure 3.6.2. Distribution of Tier 1 capital adequacy ratios (core capital before August 2024) by the shares of banks' total assets



Source: NBU.

The banks' capital cushion remains large

The banks' capital adequacy continues to significantly exceed the minimum requirements. However, the dynamics of this indicator have been trending down in recent months. The repeated retrospective increase in the tax on bank profits last year led to a decrease in the banks' regulatory capital in Q1 2025. Overall, the banks paid almost UAH 96 billion in income tax to the budget for 2024. In addition, in H1 2025, state-owned banks will also pay about UAH 35 billion in dividends to the budget – these funds are not included in the regulatory capital under the new rules. The decline in capital adequacy was also affected by the annual revaluation of capital to cover operational risk, which increased by 19% over the year.

After the transition to a three-tier structure, the capital structure is dominated by common equity tier 1 instruments. This is the highest quality capital available to absorb losses immediately, and without restrictions. Such capital composition enhances the system's resilience. Given the large stock of Tier 1 capital, the banks hardly need to raise additional Tier 1 or Tier 2 capital. Each weighted average capital adequacy ratio is close to 15%, well above the minimum requirements. Currently, only one small bank occasionally violates the minimum capital requirements, and three other small banks have less than the minimum required regulatory capital. However, these banks account for only 0.1% of the system's assets, so this does not pose a risk to the sector.

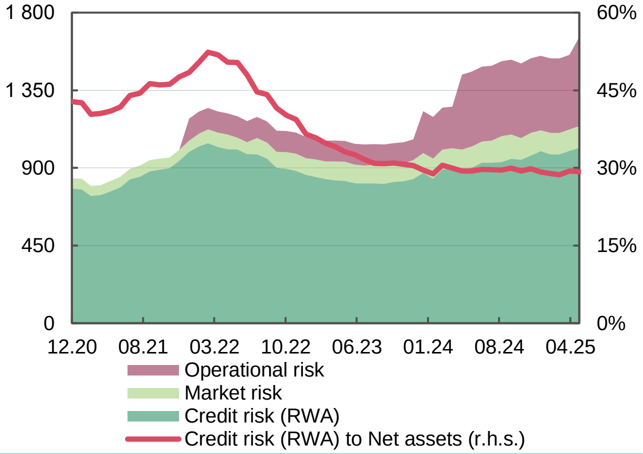
The banks' current capital cushion is sufficient to maintain their resilience and continue lending. In addition, capital is being replenished thanks to profitable operations. However, given the updated requirements, the inclusion of profit into regulatory capital will only be based on the results of an annual or interim audit. Therefore, when increasing assets during the year, the banks will mainly rely on the accumulated capital cushion, which requires careful planning. At the same time, the recurring practice of retrospective income taxation creates uncertainty and significantly limits the banks' lending potential.

Further harmonization of capital requirements with EU standards will not require an increase in capital

Last year's changes to capital requirements – updating the structure and fully incorporating market and operational risks – did not complete the cycle of planned regulatory novelties. The next steps to bring banking regulation closer to EU standards include:

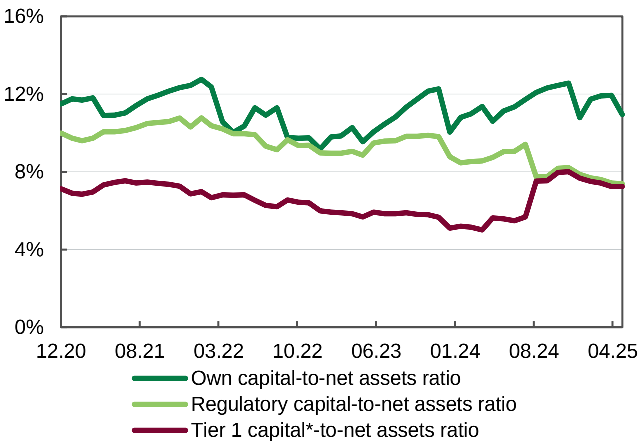
- updating the approach to calculating the credit risk to be covered by capital. From now on, the credit risk weight will

Figure 3.6.3. **Banks' risk-weighted assets, equivalent, UAH billions**



Source: NBU.

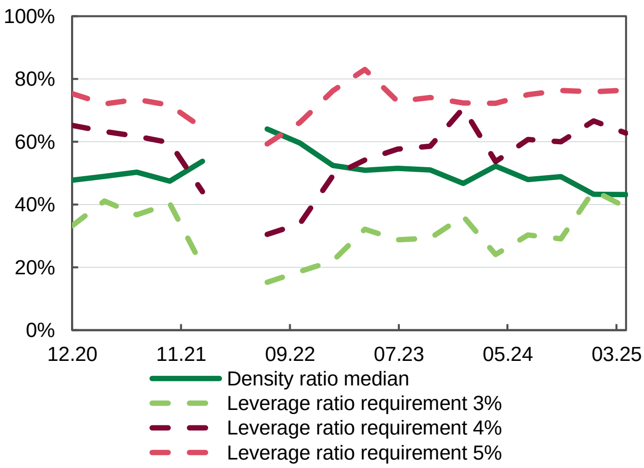
Figure 3.6.4. **Banks' capital-to-net-assets ratio**



* Core capital before August 2024.

Source: NBU.

Figure 3.6.5. **Density ratio* and percentage of banks with binding leverage ratio**



* Ratio of risk-weighted assets to off-balance assets and liabilities.

Source: NBU estimates.

be assessed not only on the basis of the type of instrument, but also on the counterparty risk itself. The risk assessment is based on the use of international credit ratings. If a borrower does not have a rating, the loan will be assigned a higher risk weight, which will equal to the current level of 100% for most exposures. At the same time, reduced risk weights are being introduced for well-diversified portfolios of performing SME loans and mortgages – 75% and 45%, respectively. Such risk weights will be set subject to a number of criteria, including the maximum size of SME loans and the condition that the exposure does not exceed 80% of the value of the property – and only for performing loans. The list of instruments to mitigate credit risk will also be expanded – primarily the list of eligible guarantees. The updated requirements will come into effect in August 2026, and test calculations will begin next March

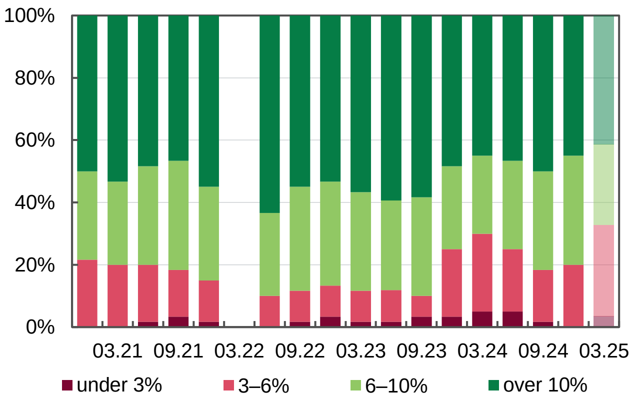
- capital coverage of settlement risk. This reflects the likelihood of losses or shortfall in income if counterparties fail to settle transactions for the purchase, sale, and exchange of securities, commodities, and foreign currency. This risk will affect capital adequacy from March 2026, and test calculations will begin as soon as this November
- coverage of credit value adjustment (CVA) risk. This risk arises from changes in the value of over-the-counter derivatives due to a deterioration in the counterparty's solvency. It will also be included in the capital adequacy calculation from 1 March 2026.

According to preliminary estimates, the need to cover settlement and CVA risks will not have a significant impact on capital adequacy due to their insignificant amounts. The updated requirements for calculating credit-risk-weighted assets may spur lending, as risk weights will be lowered for a number of assets and counterparties. This primarily concerns exposures to SMEs and mortgages. Therefore, the above novelties will not deter the banks from increasing their lending.

Introduction of the leverage ratio

Starting in September, the capital requirements for the banks will be supplemented by a new standard – the leverage ratio (LR). The introduction of the LR globally began after the global financial crisis, one of the reasons for which was the underestimation of risks from certain instruments. The advantage of the new standard is its simplicity and transparency. The LR determines the level of capital coverage of risks from exposures, disregarding their risk weights. The LR is calculated as the ratio of Tier 1 capital to total assets and off-balance-sheet liabilities (taking into account the probability of their conversion to on-balance-sheet liabilities). The NBU approved the approaches to calculating the LR last summer, and its test calculations started in April. The Basel Committee on Banking Supervision and the CRR provisions set the minimum leverage ratio at 3%. The test data made it possible to verify the applicability of this minimum requirement in the Ukrainian context.

Figure 3.6.6. Change in leverage ratio by number of banks



The banks' test calculations are shown as of 1 April 2025; before that, the data are NBU staff estimates.

Source: NBU estimates.

Table 3. Prioritization of uses for the banks' accumulated profits

Order of priorities:	
1	Coverage of unexpected losses from risks materializing during the war
2	Fulfillment of postponed requirements to cover risks with capital: ▪ operational risk in full (implemented) ▪ market risk (implemented) ▪ 100% risk weights for FX domestic government debt securities (currently, the risk weight is 50% including adjusting coefficients).
3	Compliance with new requirements to be introduced in 2025–2026, in particular for: ▪ the updated regulatory capital structure (implemented) ▪ updated credit risk weights for certain assets (the adopted regulation will apply from 2026) ▪ settlement risk (the adopted regulation will apply from 2026) ▪ the leverage ratio (the adopted regulation will apply from autumn 2025) ▪ credit valuation adjustment risk
4	Building the capital conservation buffer and the systemic importance buffer
5	Distribution of dividends

Source: NBU.

The LR will have a binding effect on a portion of banks, as it additionally prevents an excessive growth of their balance sheets. The binding effect is determined by the ratio of risk-weighted assets to total assets and off-balance-sheet liabilities of a bank, the denominator of the LR, that is the total assets and off-balance-sheet liabilities. This ratio is called the density ratio. The density ratio should be compared to the ratio of minimum Tier 1 capital adequacy ratio and LR. If the density ratio is lower than this ratio, then by increasing operations a bank is more likely to violate the LR, while the capital adequacy will stay above the minimum requirement. For both capital requirements, the LR and the capital adequacy requirements, to be effective, there should be roughly the same number of banks on the market that are constrained by each requirement. If the minimum LR is set at 3%, the leverage ratio will be binding for more than 40% of Ukrainian banks. If a higher minimum value of the ratio is assumed, the share of the banks with a binding LR will increase disproportionately.

The LR introduction essentially provides for an additional coverage of the risks of increasing off-balance-sheet liabilities, government securities, and NBU instruments. According to test calculations, most banks will be able to meet the new requirement without any problems and continue to expand their operations, primarily investment into domestic government debt securities. Moreover, the share of the government securities in the assets remains at "pre-war" levels.

The deadlines for establishing capital buffers will be determined this year

The banking system's resilience assessment has been underway since January. The first stage of the assessment – the asset quality review – has now been completed. The results confirm that the banks have generally correctly determined the amount of credit risk (prudential provisions) and that there are no hidden risks in their balance sheets. The next step is to stress test the 21 largest banks under baseline and adverse scenarios. The results of the resilience assessment will be known in late summer, and in the autumn, if necessary, the banks will develop and implement capitalization or restructuring programs.

The results of this year's resilience assessment will be the basis for determining the NBU's steps to introduce capital buffers. The capital conservation and systemic importance buffers must be maintained by the banks at all times, and their levels are unchanged: 2.5% and 1%–2%, depending on the level of systemic importance. The NBU will set the implementation schedule for these buffers. The NBU will also introduce a procedure for quarterly assessing and setting the size of the countercyclical capital buffer (read more in Box 5. NBU to Regularly Assess Financial Cycle Index for Ukraine). The decision will be announced one year before the buffer is activated. The introduction of the capital buffers is the last step before the restriction on dividend payments by the banks is lifted.

Box 3. Banks' Losses from Operational Risk Decreasing

The banks continue to incur losses from war-related operational risk events. Nevertheless, their volumes in 2024 were significantly lower than in 2022. Considering the accumulated information on operational risk losses, the NBU can more accurately assess the banks' capital needs to cover operational risk and abandon excessive conservatism in its calculation.

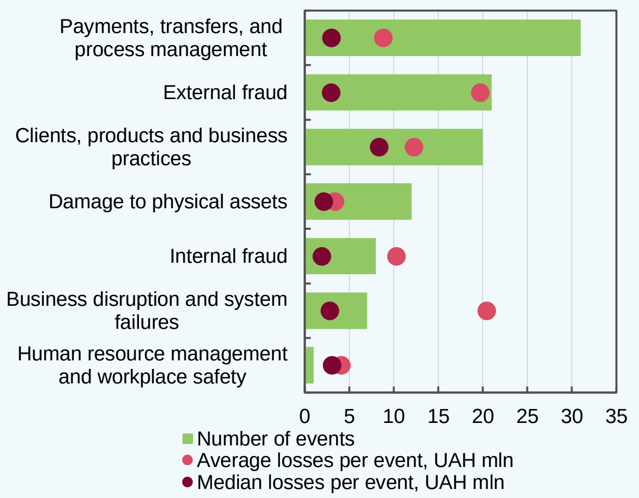
The banks' losses from operational risk decreased

In 2024, the banks' reported total losses from operational risk (OR) events amounted to UAH 1.6 billion. This was four times less than their OR losses in the year when the full-scale invasion started (both figures do not include the shortfall of income), indicating that OR has eased. However, the number of recorded OR events varies significantly, even among banks with similar risk profiles. This indicates that financial institutions have different approaches to accounting for OR events and may underestimate losses.

The NBU has analyzed the 100 largest OR events of banks in terms of losses. They accounted for about three quarters of last year's OR losses. Most of the OR episodes were related to process management. Most events of this type were the result of materialized compliance and legal risks. The second type by number of events was external fraud. These events generated the highest average losses, primarily due to several significant events in one bank. Losses from system failures were comparable in volume and concentration, although few in number. Only half of the banks reported partial recovery of losses from OR events, averaging around a fifth of the gross losses.

A quarter of the losses in 2024 were related to past OR events. Such lingering effects are typical of major shocks, such as the war. However, more and more banks are trying to register the full materialization of losses and finalize past events, including those related to the war, in their databases.

Figure B.3.1. **Types of the major* OR events of banks in 2024**



* 100 largest operational risk events by the amount of gross losses.

Source: Banks' data, NBU estimates.

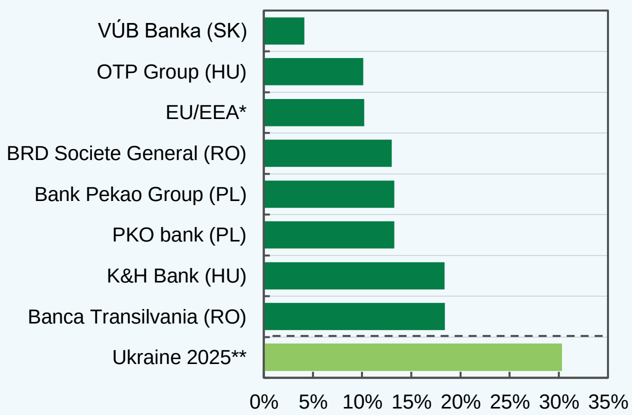
The banks attributed more than 40% of all last year's OR losses to the war. This share nearly halved compared to 2022. Such events fall into different types. About two-thirds of war-related losses came from one bank's loss of cash and precious metals in the temporarily occupied territories, which the bank classified as external fraud. In addition, this includes losses from damage and loss of property.

Maintaining complete and reliable statistics on losses from OR events allows the banks to better manage risks, including assessing more accurately capital needs under the ICAAP and making more realistic business continuity plans (BCP) and recovery plans. This information is also useful for the regulator, primarily for calibrating the amount of capital required to cover OR.

OR capital requirements for the banks should be brought closer to European standards

Capital requirements for covering OR in Ukraine are somewhat more conservative than in the EU. When introducing them in 2019, the NBU chose this approach due to the lack of data on OR events at the time. The amount of OR losses recorded in 2024 was only 4% of the capital for the OR at the start of the year. In 2022, this ratio was close to 25%. In other words, the available capital is more than sufficient to cover even the OR losses experienced in 2022, which can genuinely be described as extreme. Therefore, there are reasons to abandon the excessive conservatism and move to common EU approaches to assessing OR capital when determining the marginal coefficient (α). This coefficient determines the capital requirement as a percentage of the bank's operations (measured by a business indicator). Currently, it is fixed at 15%, while in Europe it varies from 12% to 18% depending on the size of the bank's business indicator. This change will maintain sufficient system resilience to OR and align domestic approaches more closely with European standards.

Figure B.3.2. **Average share of OR-weighted assets in total risk-weighted assets of banks in 2024**



* Overall in European Economic Area, according to EBA as of 1 July 2024.

** The median for Ukrainian banking system as of 1 May 2025.

Source: NBU, EBA, banks' data.

Box 4. Ukraine Makes Progress on EU Banking Regulatory Equivalence

On its course toward EU accession, Ukraine will continue to align its legislation with that of the European Union. The Association Agreement initiated these changes in financial sector regulation, and significant progress has already been made under it. Although it may take long to fully harmonize all provisions with the EU's, the interim goal is to achieve banking regulation equivalence. Such a status will simplify the operation of European banks in the Ukrainian market and galvanize the financing of the economy. Within a year, the NBU plans to move closer to launching an equivalence assessment.

European approaches to regulating the financial sector have been a guide for improving the domestic regulatory field since the Association Agreement was concluded. The first noticeable steps in implementing European standards were taken during the banking reform that started in 2015. Since then, Ukraine has come through the difficult times of the COVID-19 pandemic, and is now enduring the challenges of full-scale war. This has objectively slowed the implementation of requirements that are fundamentally new to the banks. However, significant progress has been made in modernizing banking regulations in the decade since the reform started. In line with European approaches, requirements have been set for the structure of regulatory capital, the risks it has to cover, the liquidity and leverage ratios, and standards in corporate governance and risk management.

Those provisions with the most significant impact on the sector's resilience were the first to be introduced into domestic legislation. The NBU considered the unique characteristics of the Ukrainian banking system: it didn't introduce approaches that would be disproportionately complex for the simple financial instruments Ukrainian banks work with.

To fulfill its intention of joining the EU, Ukraine will need to completely align its domestic requirements with EU acquis over time. A final action plan will be approved following accession negotiations on relevant chapters with the European Commission. Considering the prior experience and practices of other countries, full alignment of legislation is a complex process that may continue even after accession to the EU.

But before banking legislation is fully harmonized with EU standards, the NBU has the interim goal of ensuring the equivalence of domestic regulation and supervisory practices with EU rules. This should in turn eliminate a number of barriers to European banks operating in the local market. One important expected outcome of equivalence is the possibility for EU banks to treat their subsidiaries' holdings of host-country securities as zero-risk investments. When assessing capital adequacy, EU parent banks in their consolidated reporting currently assign the highest credit risk weights to some of the investments made by their Ukrainian-based subsidiaries into domestic government debt securities. Reducing these weights will free up capital that the banks could use to lend more actively to businesses or the state.

EU regulatory equivalence means that the quality of banking regulation and supervision in a jurisdiction is generally comparable to that achieved in Europe. The equivalence assessment is carried out by the European Banking Authority (EBA) and approved by the European Commission. More than 20 countries, including a number of Europe's non-EU states, have already received confirmation that their regulations are equivalent to EU requirements. The process of obtaining such status is based on the self-assessment of regulators who have applied for it. A country is eligible to start a regulatory equivalence assessment if the legislation that is being assessed provides for equivalence in the field of professional secrecy. To implement the relevant standards, including with regard to the non-disclosure of information received from the regulators of other countries, the NBU is currently finalizing amendments to Ukrainian laws. This process is to be completed by the end of the year. An assessment of regulatory equivalence can commence immediately after these amendments are implemented.

The equivalence assessment is carried out for more than a dozen components, including the regulatory capital structure, required capital for each risk, liquidity and leverage ratios, reporting, market discipline and disclosure, securitization, macroprudential requirements, and the supervisory approach. The NBU conducted its first self-assessment of equivalence in 2022 with the EBRD's assistance. The results showed that approximately half of the key provisions required for equivalence were in place. Since then, the self-assessment has been revised on a regular basis. Currently, the level of implementation of requirements and practices necessary to achieve equivalence exceeds 75%.

The biggest gaps right now are due to a lack of these components:

- securitization legislation
- requirements for banks to hold capital instruments for resolution (e.g. TLAC/MREL)
- tighter requirements for global systemically important banks
- requirements for maintaining capital buffers
- risk disclosure requirements under Pillar III.

Given the deadlines for developing the necessary changes to Ukraine's banking regulations and legislation, there is an opportunity to eliminate the gaps noted above and bring closer the start of the equivalence assessment next year already. This is precisely the plan enshrined in the *Strategy of Ukrainian Financial Sector Development*.

Box 5. NBU to Regularly Assess Financial Cycle Index for Ukraine

To prevent the accumulation of systemic risks, it is necessary to monitor financial cycles. For this purpose, the NBU has developed the Financial Cycle Index. The index will be used as one of the benchmarks for calibrating macroprudential policy instruments, primarily the countercyclical capital buffer.

Financial systems evolve in cycles, with periods of growth followed by phases of decline. In the upward phase of the financial cycle, market participants' optimism promotes intensive lending, higher economic activity, and thus, asset price growth. Under such conditions, financial institutions often underestimate risks, which leads to the accumulation of imbalances and systemic threats to financial stability. In general, the risks materialize during the downturn phase of the financial cycle, and could lead to serious economic shocks. Macroprudential policy aims to prevent the buildup of systemic risks. Therefore, timely identification of the phase of the financial cycle is essential for effective macroprudential policy. The Basel standards stipulate the use of indicators to track the phase of the financial cycle.

To assess the phases of the financial cycle in Ukraine, the NBU has developed its own indicator – the Financial Cycle Index[2] (FCI). The FCI consists of four sub-indices that reflect the key factors of the financial cycle: the private sector debt burden (businesses and households), credit conditions and demand, the state of the housing market, and macroeconomic conditions.

Each sub-index includes from two to six indicators. The selected indicators are those that best reflect the financial sector's approach to a certain phase of the cycle. Quarterly data were used to calculate the index. For some indicators, data have been available since 2001, and the FCI has been calculated since then. However, since the data for all indicators have only been available since the end of 2011, the contributions of each sub-index have been calculated starting from that period.

The input data were pre-processed. A number of indicators were smoothed using the moving average method to reduce their short-term volatility and reveal fundamental changes in dynamics. All indicators were calculated in such a way that higher values reflect an upswing in the financial cycle.

Loan volumes for some indicators were adjusted for changes in the exchange rate in proportion to the dollarization rate of the loan portfolio. Real estate prices, often quoted in U.S. dollars, were also adjusted for the exchange rate. Such adjustments help avoid false signals from changes in indicators due to depreciation.

Most indicators are included in the FCI in in terms of gaps, i.e. as deviations of the actual values of the indicator from its long-term equilibrium level. All indicator gaps, except for the output gap[3], are calculated using a two-sided Hodrick–Prescott filter, a time-series smoothing method to extract long-term trends. Thus, the indicators point to an upward phase of the financial cycle when the values are above the long-term trend, and to a downward phase when the values are below the trend.

Table 4. Financial Cycle Index composition

Subindex	Indicator
Debt burden of private sector	Credit to private sector / corporations / households to GDP gap
	Debt service ratio gap for households
	Gap in the ratio of new loans to non-financial corporations/households to GDP
Credit conditions and demand	Interest rate on new loans to corporations / households gap
	Average of past and expected change in credit standards / credit demand for corporations and households
	Google search queries for credit*
Housing market**	Real house price gap
	House price to income gap
	House price to rent gap
Macroeconomic conditions	Output gap
	Current account balance to GDP

* Frequency of the 'credit' term searched for on Google over a quarter.
** Sub-index indicators for the primary market of Kyiv.

Source: NBU.

Subsequently, all indicators were brought to the same dimension – normalized by dividing the difference between the current and average values of the indicator by its standard deviation. As a result, the historical normalized values of all indicators are mostly in the range between -2 and +2, with a mean of zero. The values of the FCI also remain within these bounds.

The FCI sub-indices are simple averages of normalized indicators. The FCI is calculated as a simple average of the four sub-indices. Taking into account the residual volatility of the constructed quarterly FCI over the year, the index is additionally smoothed using a Hodrick–Prescott filter using a smoothing parameter corresponding to the annual data frequency. The FCI values may be slightly adjusted retrospectively with each data update due to the statistical properties of the two-sided Hodrick–Prescott filter. However, given the historical dynamics of the FCI, such adjustments do not distort the overall assessment of the cycle phase. The final FCI fluctuates within a narrower range than individual indicators, as the index combines financial cycle components, some of which may indicate a downturn, while others suggest an upturn.

The FCI reached its highest value in 2007, just before the global financial crisis. For several years before the crisis, the index had been gradually rising, signaling the accumulation of procyclical risks, primarily due to credit expansion and a real estate market bubble. After the financial crisis, the FCI

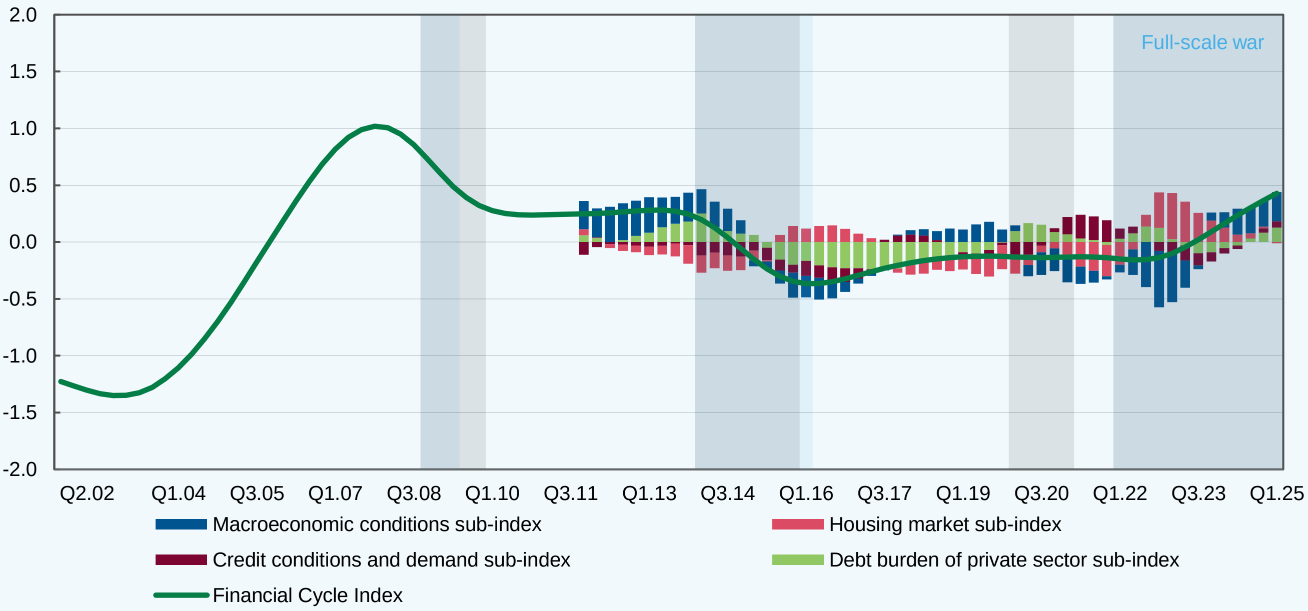
[2] For a full description of the methodology, see Geršl, A., Dadashova, P., Bazhenova, Y., Hlazunov, A., Krasovytskyi, D. (2025). The Financial Cycle Index of Ukraine. NBU Working Papers, 1/2025. Kyiv: National Bank of Ukraine.
[3] The methodology for calculating output gap is described in detail in the October 2021 NBU Inflation Report.

primarily reflected macroeconomic imbalances, which were eventually accompanied by an increase in the debt burden of businesses and households. After 2016, the FCI was at a neutral level, so the economic shocks that Ukraine experienced in 2020 and 2022 did not trigger financial crises. Over the past year, the FCI has shown an upward trend, driven mainly by macroeconomic factors. However, the existing macroeconomic imbalances are caused by the prolonged impact of the war and are offset by substantial international assistance, so the increase in the index should be interpreted taking into account the war-related features of the economy.

The FCI will complement the system of indicators used by the NBU for macroprudential analysis. Unlike the high-frequency FSI, which reflects the level of stress in the sector at a particular point in time, the FCI has predictive power and captures medium-term cyclical fluctuations of the financial sector. The FCI also supplements the risk map, which focuses on forecasting the level of risks in the sector, by providing information on imbalances that cause these risks to increase.

The calculated value of the FCI is one of the benchmarks for making decisions on the introduction of macroprudential instruments, primarily the countercyclical capital buffer. This approach is fully in line with the provisions of EU directives and the recommendations of the European Systemic Risk Board, which emphasize the importance of developing and utilizing credit cycle indicators when determining the level of this buffer. A significant increase in the FCI would signal the need for a higher buffer. However, when deciding on the size of the countercyclical capital buffer, the NBU will consider a wide range of indicators characterizing the credit risks of banks, the dynamics of capital adequacy ratios, the results of stress tests of the banks, and the causes and possible consequences of the cycle factors identified by the FCI. The NBU's decisions on setting a certain level of the countercyclical capital buffer will be made on a quarterly basis and will be accompanied by analytical materials, including the estimated value of the FCI. The NBU will decide on the introduction of a countercyclical capital buffer together with its decision on the levels of other buffers based on the results of this year's assessment of the resilience of the banks and the banking system.

Figure B.5.1. Financial Cycle Index



The blue shading indicates periods of financial crises, while the gray shading marks periods of economic crises. The crisis periods are defined according to Filatov (2021).

Source: NBU estimates.

Box 6. ESG Risk Management at Ukrainian Banks Is Improving

Ukrainian banks are integrating environmental, social, and governance (ESG) risk management into their business processes. An NBU survey has shown a significant progress in this area.

Ukraine is moving toward a sustainable development model

The processes of developing sustainable finance and managing environmental, social and, governance (ESG) risks[4] have picked up pace noticeably in Ukraine over the past year. At the state level, priority measures for the development of sustainable finance have already been outlined. Among them, it is worth highlighting, the introduction of:

- green taxonomy and relevant terminology based on European documents. The taxonomy will establish clear technical criteria for activities that can be considered environmentally sustainable in various sectors of the economy
- sustainability reporting for companies, including financial institutions, based on the EU's CSRD and the European Sustainability Reporting Standards (ESRS)
- classification and attributes of products, primarily financial instruments, that contribute to sustainable development
- requirements for ESG risk management.

Given the wide range of areas covered by the planned transformation, many state institutions are involved in it: the government, the National Securities and Stock Market Commission, and the NBU. In 2024, the Green Transition Office was established under the auspices of the Ministry of Economy to coordinate the institutions' efforts.

NBU presented vision of ESG risk management model for the financial sector

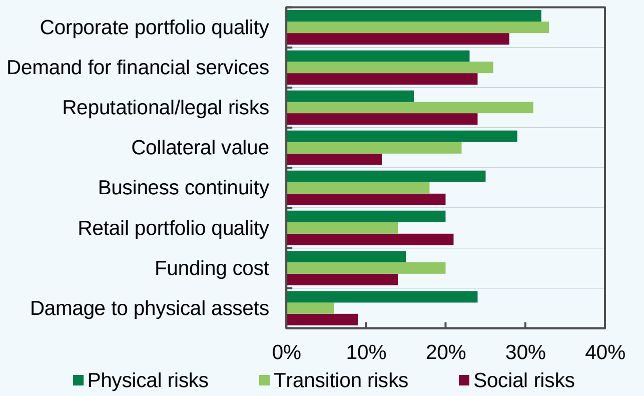
The impact of ESG risks on NBU-supervised financial institutions is twofold: these risks affect their business activities directly and through the activities of the clients they finance. Therefore, financial institutions make a significant contribution to the speed of the transition to a sustainable economy. To this end, in April, the NBU developed a White Paper that outlines the envisioned state of ESG risk management in the financial sector and contains an action plan to achieve it. It applies to all banks and other financial institutions important for the public, or those that have a significant impact on sustainable development and higher exposure to ESG risks. According to this vision, in the medium term, these institutions will:

- have strategic documents on ESG risk management. Such documents will reflect the dual impact of ESG risks on the institution and contain quantitative and qualitative ESG commitments, as well as exclusion lists – activities that the institution does not finance
- manage ESG risks within the framework of the established corporate governance system
- properly identify these risks, including in their assessments of liquidity and capital
- collect and process information from clients about their ESG risks and communicate with them to mitigate relevant threats
- disclose information about their ESG risks and the ESG profile of their loans and other investments.

The banks are aware of the impact of ESG risks

Last year, the NBU for the first time surveyed the largest banks about climate risks as one of the key components of ESG risks (read more in the June 2024 Financial Stability Report). In April, the NBU held a repeated survey of 58 banks on the management of all components of ESG risks. The results confirmed that the banks are already experiencing the impact of these risks on their operations, as indicated by about three-quarters of the banks surveyed. Most banks expect that ESG risks will affect the solvency of their corporate clients and the demand for financial services. Climate transition risks[5] and social risks will affect the reputation of financial institutions, primarily due to the need to meet increasingly stringent requirements. About a quarter of the banks expect physical climate risks to affect the value of collateral, business continuity, and asset integrity.

Figure B.6.1. Percentage of banks citing the impact of risks on various indicators



Source: bank survey.

The banks believe that the likelihood of ESG risks materializing is the highest in the medium term. At the same time, the financial institutions more often see new opportunities in managing ESG risks than threats to their business.

Participation in state support programs encourages the banks to better manage ESG risks

More than half of the banks have already developed environmental and social management systems. Building a

[4] According to the EU Capital Requirement Regulation (CRR), ESG risks mean risks of any negative financial impact on an institution stemming from the current or prospective impact of environmental, social or governance (ESG) factors on that institution's counterparties or invested assets.
[5] Transition risks refer to the risk of any negative financial impact on an institution as a result of the current or prospective effect of the transition to sustainable economy on its counterparties or its assets. Physical risks mean the risks of any negative financial consequences for an institution due to current or prospective physical impact of the environment on its counterparties or its assets.

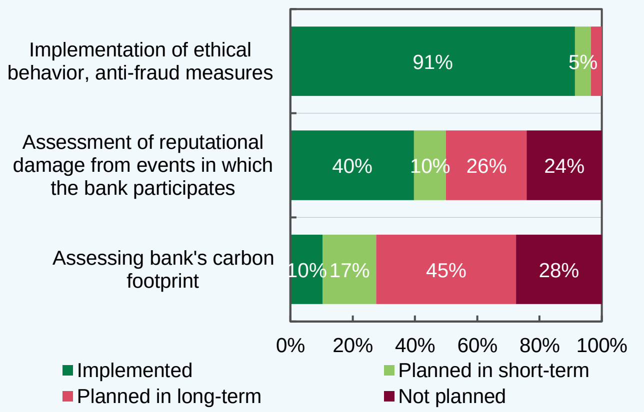
system involves developing a strategic document – a policy or a strategy – for managing environmental and social risks, as well as implementing processes and procedures, and recruiting qualified personnel to carry them out. However, only ten banks have clear, measurable goals for risk mitigation. Only 40% of the banks have staff with experience in ESG risk assessment.

The implementation of an environmental and social management system is one of the requirements for participation in the lending support programs of the Business Development Fund and the Partial Credit Guarantee Fund in Agriculture. For now, these requirements apply only to lending to farmers, but they will be extended to all programs of the respective funds starting in November. Access to state support has motivated financial institutions to accelerate the development of relevant systems.

The banks have made more progress in integrating social and governance components into their operations than environmental ones. Almost all financial institutions have implemented standards of ethical conduct and are taking anti-fraud and anti-corruption measures. At the same time, there are still many unimplemented elements of environmental components. For example, almost half of the banks are going to assess their carbon footprint only in the long term, and a quarter do not plan to do so at all.

As sustainability reporting is still not mandatory in Ukraine, only about ten banks prepare such reports voluntarily and in an arbitrary format.

Figure B.6.2. Implementation of certain ESG processes in banks



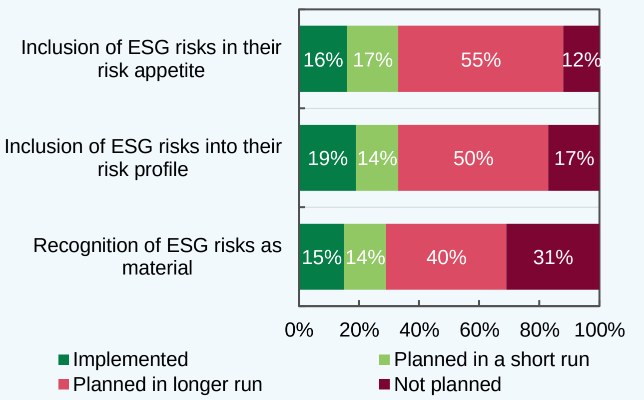
Source: bank survey.

ESG risk management is not yet fully integrated into the risk management system

ESG risk management has not yet fully integrated into the banks' overall risk management system. According to the banks, less than half of them have integrated ESG risks into all three lines of defense. However, only a third of the banks have implicitly assigned ESG risk management responsibilities to their risk management unit. In a few financial institutions, compliance with ESG risk assessment procedures is checked by the audit function. Sixteen banks have appointed persons responsible for this area in the management board, and four banks have persons in charge in their supervisory boards. None of the banks indicated that the remuneration of supervisory board or management board members is tied to the achievement of ESG goals.

Currently, the banks mostly define ESG risks as triggers of traditional types of risks for financial institutions, primarily credit and operational risks, and do not categorize them separately. Nevertheless, nine banks recognized ESG risks as material (compared to four banks last year). One third of the banks do not see any prospects for recognizing ESG risks as material even in the long term.

Figure B.6.3. Incorporating ESG risks into risk assessments at the bank level



Source: bank survey.

Interaction with clients in the ESG area is unsystematic

ESG risk assessment is integrated into the lending process at the decision-making stage and during the annual credit review. However, the results of this assessment rarely affect the pricing of loans. Covenants in loan agreements are often the requirements to obtain environmental permits. The assessment of clients' ESG profiles is hampered by borrowers' unawareness, the banks' deficit of in-depth expertise, and a lack of understanding of how to use the information collected in risk assessment. Only a quarter of the banks collect data on their clients' resource efficiency, and about a tenth collect data on their carbon intensity. At the same time, state programs provide for mandatory assessment of a client's environmental and social profile.

Table 5. Share of banks indicating that ESG risks are taken into account in the lending process

Process	Corporate	Retail
Loan approval	66% (+27 pp)	22% (+19 pp)
Annual credit review	40% (+25 pp)	5% (+5 pp)
Collateral examination	21% (+15 pp)	12% (+9 pp)
Collateral eligibility evaluation	19% (+10 pp)	12% (+9 pp)
Setting the interest rate	10% (+6 pp)	–
LGD assessment	5% (+5 pp)	–
PD assessment	3% (+3 pp)	–

The change in percentage points of positive responses compared to 2024 is indicated in parentheses.

Source: bank survey.

As in the previous year, only a few banks offer "sustainable" loan products – 16 types for businesses and 9 for households. Most of the products are implemented in cooperation with IFIs and are financed by them. These loans are mostly long term, up to 10 years. The banks' interpretations of product sustainability vary widely. In the absence of clear criteria, it is impossible to verify whether products meet the sustainability criteria.

Recommendations

Ensuring financial stability in wartime requires concerted efforts and coordinated actions by all financial market participants: the banks, NBFIs, the NBU and other market regulators, as well as the effective interaction of state institutions. The NBU makes recommendations to government authorities and financial institutions, and communicates its near-term priorities.

For state authorities

Going forward, ensure timely implementation of reforms agreed with partners
In May, the Financial Stability Council approved the updated *Strategy of Ukrainian Financial Sector Development* and *Lending Development Strategy*. The Council revised the deadlines and expanded the list of measures necessary for the further development of the financial sector's infrastructure and the more active financing of the economy. The implementation of the envisaged reforms is also reflected in Ukraine's commitments under IMF-supported financing program, the Ukraine Facility, and the ERA mechanism. Therefore, implementing the reforms remains a prerequisite for receiving international financial assistance and ensuring macrofinancial stability in wartime. The current pace of reform has made it possible to successfully pass the eighth review of the IMF program. However, delays in taking certain steps must be eliminated in order for funds to be disbursed on time.

Key legislative changes outlined in the *Strategy of Ukrainian Financial Sector Development*, necessary to maintain financial stability and fulfill agreements with international partners, are contained in the following draft laws:

- on the war risk insurance system (No. 12372), which introduces a system of mandatory insurance of a number of objects, primarily new buildings and mortgages, with standardized terms
- on the adoption of laws and regulations necessary for Ukraine's accession to the Single Euro Payments Area (SEPA) (No. 13233), including in the field of AML/CFT.

Another step in the pursuit of the strategies will be the implementation of the Law *On Factoring*, which was passed in June. It clearly defines the rights and obligations of parties to a factoring agreement, will help prevent fraud, and will ultimately expand access to financing for SMEs. The factoring legislation also paves the way to the development of the NPL resolution market by allowing the assignment of business loans to a wider range of companies. It is also necessary to finish drafting and adopt amendments to the law on property valuation and appraisal activities. The amendments will bring the regulation of this area closer to European standards and improve the quality and reliability of property valuation.

Adopt and begin to implement the *Mortgage Lending Development Strategy*
The preparation of the *Mortgage Lending Development Strategy* is being completed. Its concept has been agreed upon by the relevant institutions and international partners. The document contains a list of necessary reforms to reduce the risks of mortgage lending and make it cheaper and more accessible to households. One element of the strategy concerns reforming state support for mortgage lending. In the future, the *Mortgage Lending Development Strategy* should become an element of the broader *Housing Strategy*, which is being prepared by the Ministry for Development of Communities and Territories of Ukraine, and which outlines the necessary steps for the development of the real-estate market as a whole.

Complete the optimization of state lending support programs
The government has drafted another package of amendments to the terms of the state program *Affordable Loans 5-7-9%*. In June, the base interest rates at which the banks lend funds were cut by 1–2 pp, and the cap on the size of loans to finance working capital was lowered to UAH 5 million. However, the outstanding amount of interest compensation to the banks remains considerable, making it necessary to focus the program further on areas that require support. An additional challenge is the introduction in November of requirements for the banks' environmental and social management systems in all areas. The banks and the Business Development Fund therefore need to coordinate the procedure for the banks' interactions with clients, primarily the versions of questionnaires on the environmental and social profile of businesses, in order to maintain access to the program for clients who need

support. In addition, the *eOselia* program's updated design is being finalized to introduce an interest rate compensation mechanism for clients. The program update should contribute to the scaling of mortgages and ensure the development of market demand for residential real estate.

Recommendations for financial institutions

Banks must adjust to new regulatory requirements
As the NBU continues to update its regulatory requirements to bring them into line with EU rules, the banks need to:

- comply with the leverage ratio that goes into effect in September this year
- perform test calculations and prepare to include into the capital adequacy ratio the settlement risk, the credit valuation adjustment risk, and the updated approach to weighting assets by credit risk.

Moreover, banks will have to develop and implement capitalization or restructuring programs by the end of the year if higher required capital adequacy ratios are set for them on the basis of the resilience assessment.

Banks must develop expertise in environmental and social governance
Banks that continue to participate in the programs of the Business Development Fund and the Partial Credit Guarantee Fund in Agriculture must develop their own environmental and social management systems. Specifically, such banks need to develop procedures for assessing and mitigating social and environmental risks of their clients. Going forward, the measures outlined in the NBU's White Book on ESG Risk Management will serve as guidelines for financial institutions to develop their ESG risk management systems.

Providers of non-bank financial services must meet the legal requirements, including by taking the following steps:

- comply with consumer protection and AML/CFT requirements and improve the management of relevant risks
- (for insurers and finance companies) comply with capital ratios and eliminate violations in a timely manner and (for credit unions) meet the updated requirements for solvency and corporate governance
- ensure high-quality, timely reporting and automate internal accounting systems. Credit unions have been submitting all their reports on a monthly basis since the start of the year. Finance companies and pawnshops have had to submit data on regulatory balance sheets and off-balance sheet liabilities on a monthly basis since 1 April, and must submit all other reports once a month from 1 July.

NBU Priorities

Complete the banks' resilience assessment and publish its results
In June, the NBU launched the stress testing of the 21 largest banks under baseline and adverse scenarios as part of its resilience assessment of the banks and the banking sector. Based on the resilience assessment results, required capital adequacy ratios will be assigned to some of the banks, which they will have to achieve by the end of this year.

Continue to implement EU regulatory standards
The NBU will work to ensure the greater compliance of the Ukrainian regulatory environment with European standards. This year, the NBU will enhance the requirements for the framework of third-party risk management at the banks. Based on the resilience assessment results, the NBU will also set the schedule for the implementation of capital buffers. Disclosure requirements for banks under Pillar III are being developed, and procedures for establishing higher requirements under Pillar II are being finalized. The NBU strives to prepare for a formal launch of the assessment of equivalence to EU regulations by the end of the year.

Gradually introduce ESG risk management requirements for financial institutions
The NBU will implement the measures outlined in its White Paper on ESG Risk Management in the Financial Sector, which has been discussed with stakeholders. The requirements will be imposed gradually and will take into account the systemic importance of institutions.

Abbreviations and Terms

This FSR, unless otherwise stated, shows data for the banks that were solvent for 1 May 2025, in chapters 3.2, 3.4, 3.5, and 3.6 – for the banks that were solvent at each reporting date.

War, invasion	Full-scale russian invasion to Ukraine since 24 February 2022
"Pre-war"	Before the full-scale invasion
5-7-9%, 5-7-9% program	State program *Affordable Loans 5-7-9%*
AML/CFT	Anti-money laundering / countering financing of terrorism
BDF	Business Development Fund
CD	Certificate of deposit
CIR	Cost-to-income ratio
CoR	Cost of risk
COVID, COVID-19	Coronavirus disease 2019
CPI	Consumer price index
CRR	Capital Requirement Regulation
DGF	Deposit Guarantee Fund
DSTI	Debt service-to-income ratio
EBA	European Banking Authority
EBITDA	Earnings before interest, taxes, depreciation and amortization
EBRD	European Bank for Reconstruction and Development
ECB	European Central Bank
eOselia	State program of affordable housing lending
ESG	Environmental, Social, and Governance
ERA	Extraordinary Revenue Acceleration mechanism
EU	European Union
FSR	Financial Stability Report
FX	Foreign currency/exchange
G7	Group of Seven
GDP	Gross Domestic Product
HQLA	High quality liquid assets
ICAAP	Internal Capital Adequacy Assessment Process
IFI	International Financial Institutions
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
LCR	Liquidity coverage ratio
LGD	Loss given default
LTV	Loan-to-value
MREL	Minimum requirement for own funds and eligible liabilities
NBFI	Non-bank financial institution
NBU	National Bank of Ukraine
NFC	Non-financial corporations
NPE/NPL	Non-performing exposure / loan
NSFR	Net stable funding ratio
o/n	Overnight
OPEC	Organization of the Petroleum Exporting Countries
o/w	Of which
PD	Probability of default
Regulation No. 351	Regulation of the NBU of 30 June 2016 No. 351 approving Regulation on credit risk calculation by Ukrainian banks
ROE	Return on equity
RWA	Risk-weighted assets
SMEs	Small and medium-sized enterprises
SSSU	State Statistics Service of Ukraine
STSU	State Treasury Service of Ukraine
T-bonds	Domestic government debt securities
TLAC	Total loss-absorbing capacity
UFHC, Ukfinzhytlo	Ukrainian Financial Housing Company
UIRD	Ukrainian Index of Retail Deposit Rates
UK	United Kingdom of Great Britain and Northern Ireland
U.S., USA	United States of America
WTO	World Trade Organization
w/o	without

th	thousand
bn	billion
mln	million
MW	Megawatt
sq. m	square meters
EUR	euro
UAH	Ukrainian hryvnia
USD	US dollar
USD equiv.	US dollar equivalent
pp	percentage points
yoy	year-on-year
x	Number of times
r.h.s.	right hand scale
Y	year
H	half of a year
Q	quarter
M	month