



National Bank
of Ukraine

Ukrainian banking: refreshed and efficient, but vulnerable to political risks

Dmytro Sologub

Deputy Governor

Berlin, June 2019



Where we are

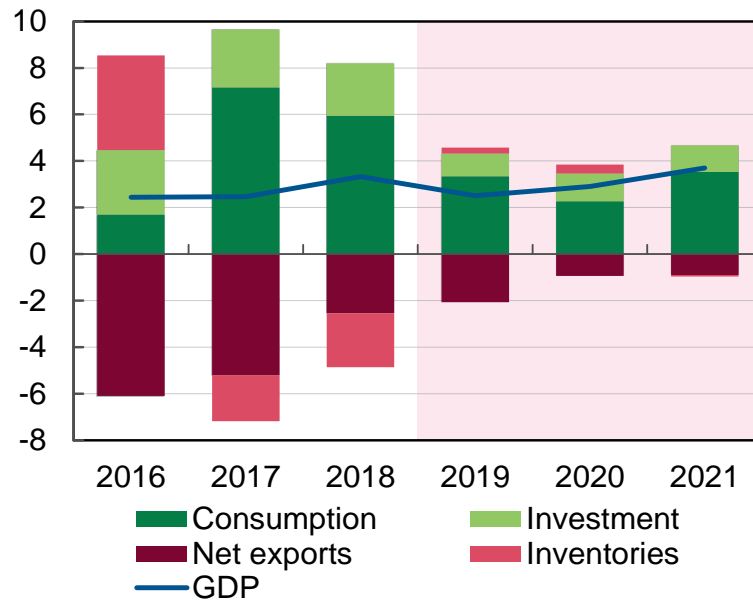
- The next IMF tranche has been postponed until the parliamentary elections and formation of a new government.
- Macroeconomic policy remains sound.
- No disruptive issues with banking system.
- Mild deterioration of FX and business expectations.
- **A key assumption of the macroeconomic and financial sector forecast is that Ukraine will continue to cooperate with the IMF**, which will allow to attract other official financing, improve access to the international capital markets and support interest of nonresidents in UAH-denominated bonds.

Key risks

- More uncertainty due to early parliament election
- External risks (global recession, decline in commodity prices)
- Uncertainty over the volume of gas transit through Ukraine in 2020
- Escalation of the military conflict and new trade restrictions by RF
- Risks to Ukraine's financial stability and the NBU's independence

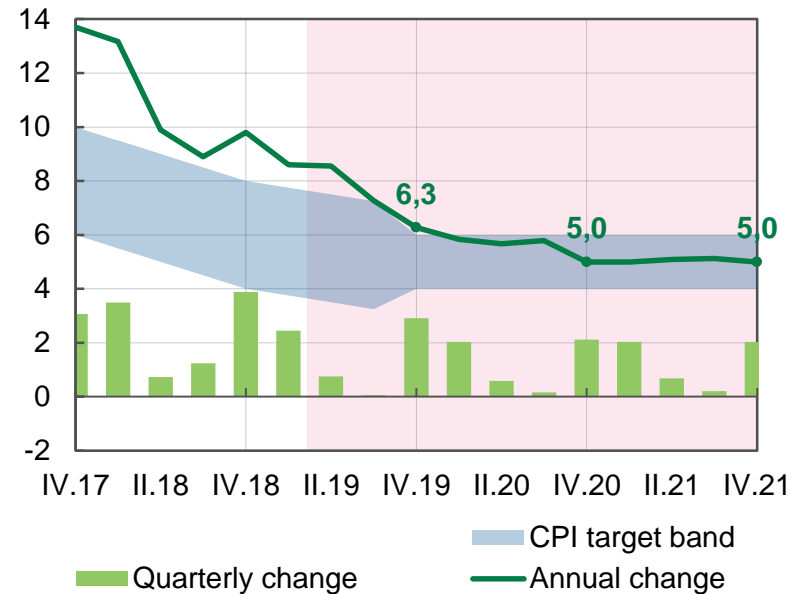
Macroeconomic recovery is underway

Contributions to Real GDP Growth, pp



Source: SSSU, NBU staff estimates.

Headline CPI, %

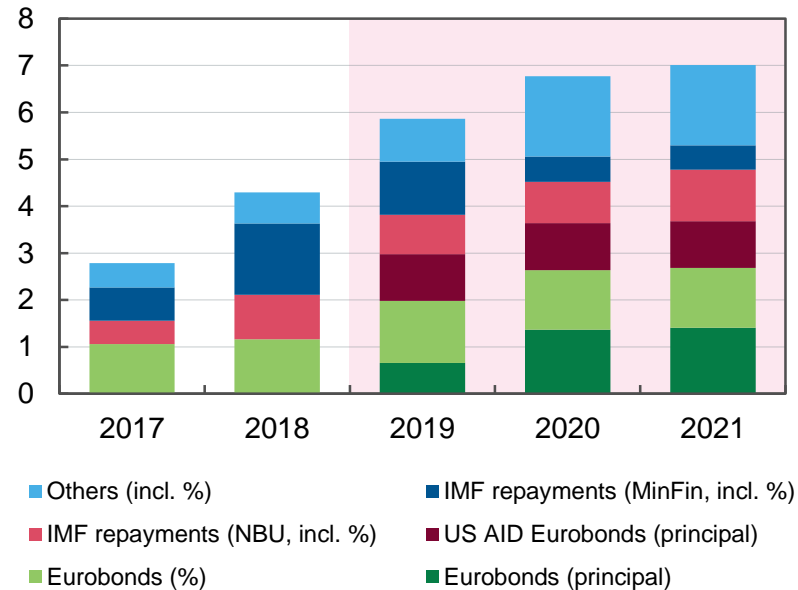


Source: SSSU, NBU staff estimates.

- Macroeconomic stability has been entrenched amid steady growth recovery and decelerating inflation
- GDP growth slows down to 2.5% in 2019 but will accelerate in the coming years.
- Inflation will go down to 6.3% this year and will hit the target in 2020.

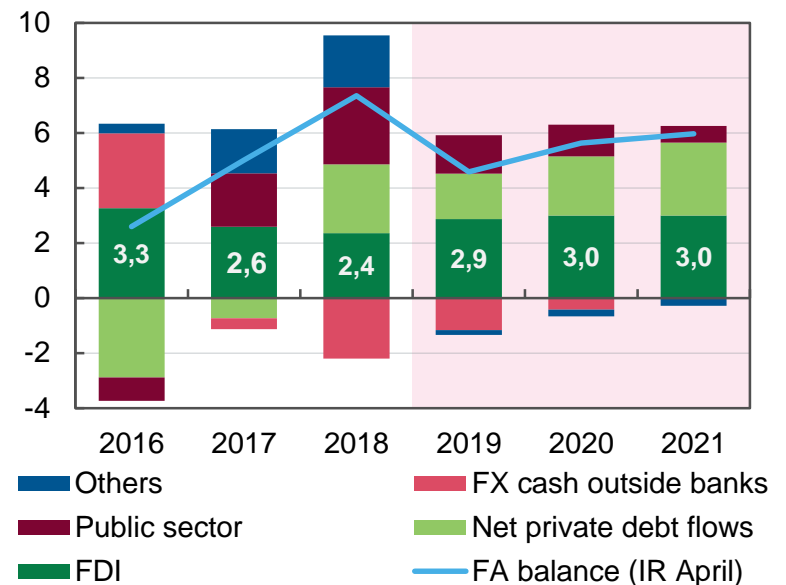
We don't expect capital outflows, though planned public external debt repayments are challenging

Public External Debt Repayments*, USD bn



* As of April 16, 2019
Source: IMF, C-bonds, NBU, Inflation Report April 2019

Financial Account (FA): Net Inflows, USD bn



Source: NBU, Inflation Report April 2019.

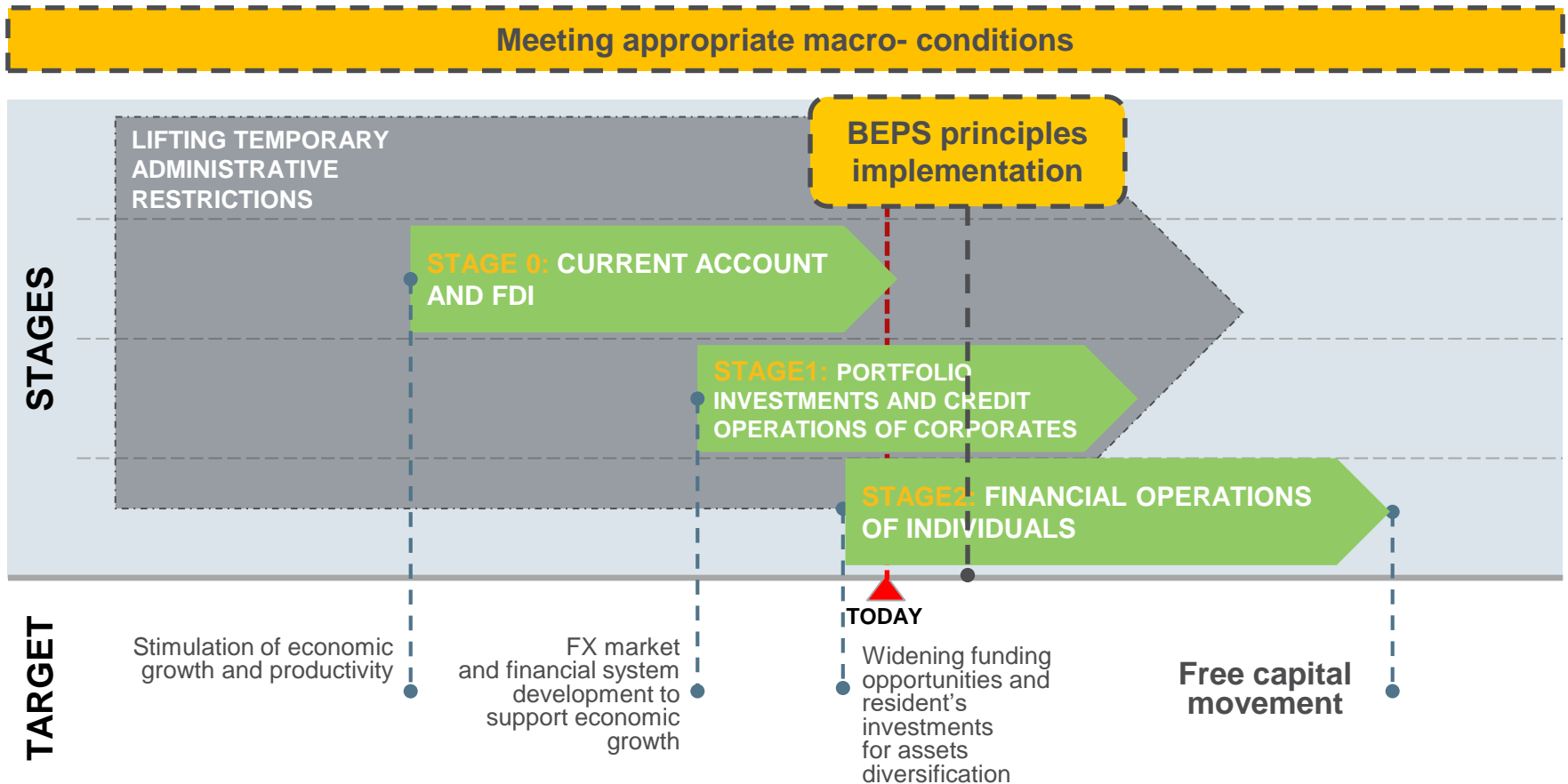
- Stable macroeconomic situation allows NBU to ease FX regulations without negative consequences for capital flows. Connection to ClearStream system launched in 2019.
- In 2019-2021 due repayments on sovereign debt should exceed to USD 20 bn USD.
- Cooperation with IMF and other IFI's is vital to assure smooth fulfillment of government obligations. Our baseline scenario implies that cooperation continues.

Key macroeconomic indicators

	2018	2019	2020	2021
Real GDP, change, %	3.3	2.5	2.9	3.7
Nominal GDP, UAH bn	3 559	3 970	4 342	4 750
CPI, y-o-y, %	9.8	6.3	5.0	5.0
Core CPI, y-o-y, %	8.7	5.0	3.7	3.7
Current account balance, USD bn	-4.5	-4.9	-5.8	-6.7
<i>% GDP</i>	-3.4	-3.3	-3.6	-4.0
BOP (overall), USD bn	2.9	-0.3	-0.1	-0.7
Gross reserves, USD bn	20.8	21.2	21.9	21.8

Source: Inflation Report, April 2019

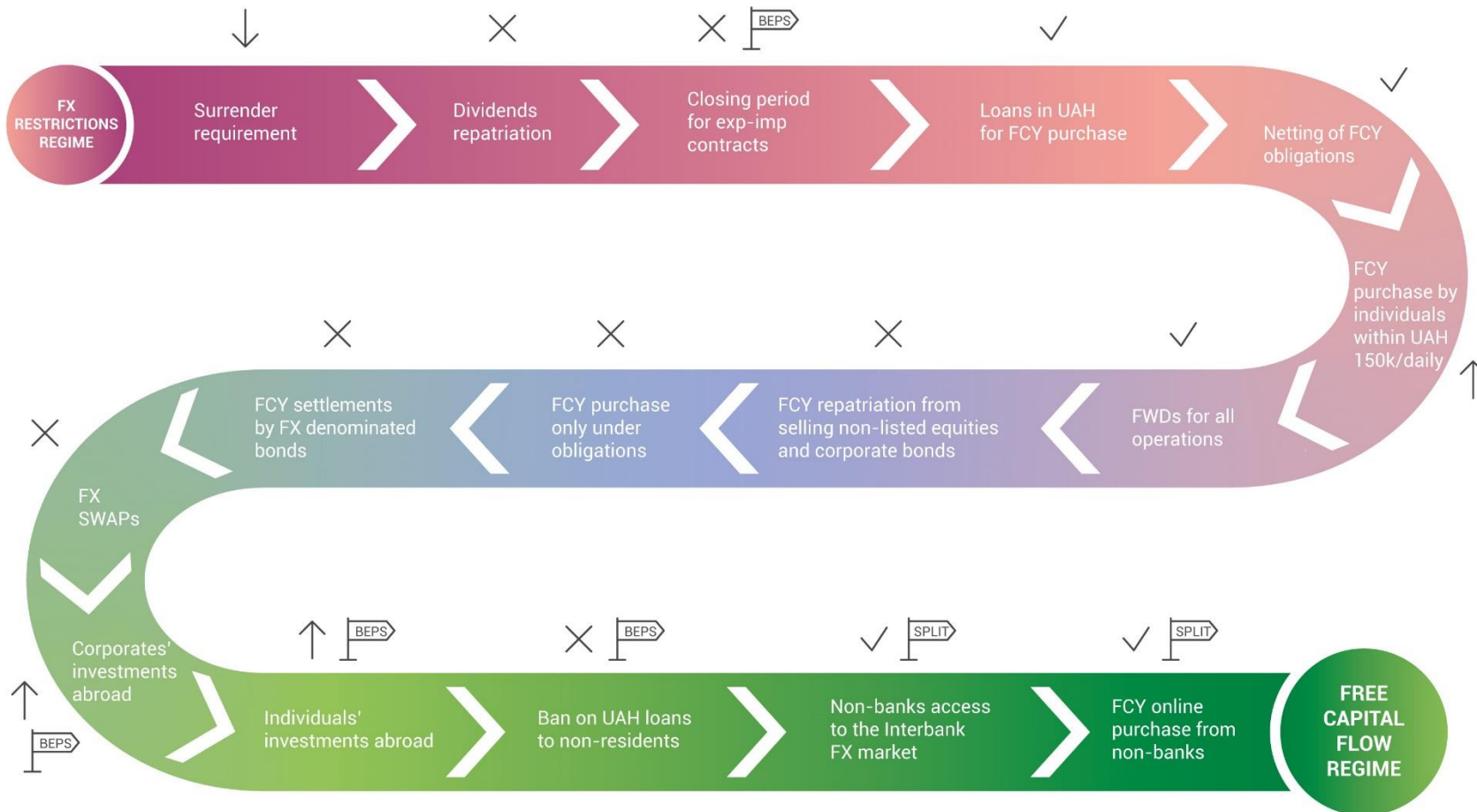
The NBU is moving towards a currency liberalization



- Transition to the next stage of currency liberalization can be done in case of implementation of OECD recommendations to BEPS resistance and unified standard of automatic exchange of financial information

The road map for cancelling FX restrictions

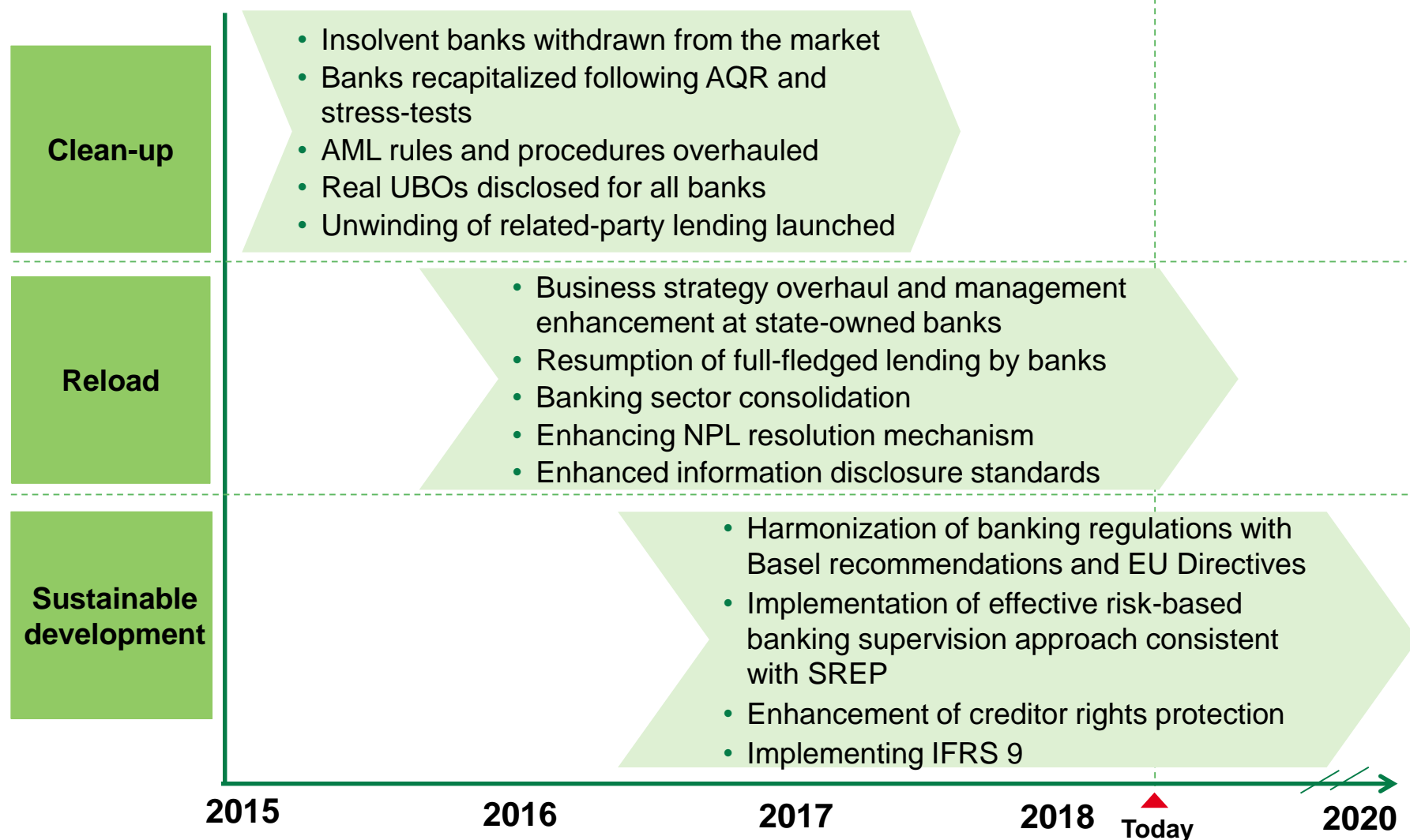
(According to the dynamics of macroeconomic preconditions improvement)



Legend:

- From top priority to low-priority steps
- Limit's increase and its cancellation
- Limit's decrease and its cancellation
- All restrictions cancellation
- Allowed
- Not before BEPS implementation
- Not before SPLIT implementation

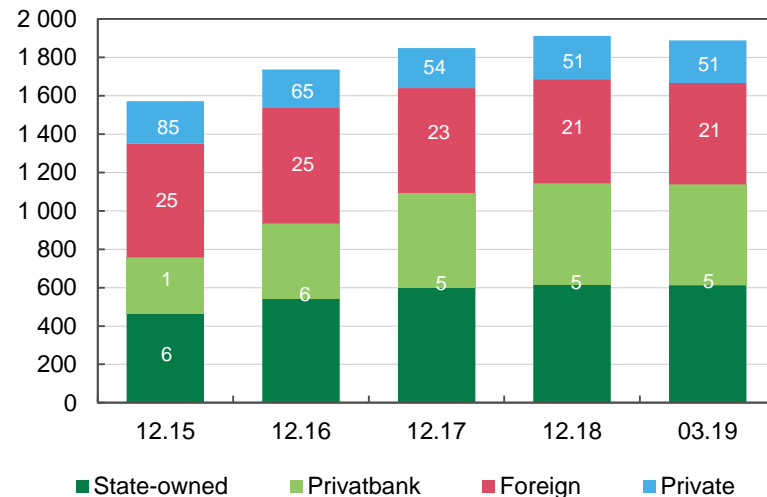
Facing the perfect storm, the National Bank of Ukraine launched a comprehensive reform of the local banking industry



- In addition to the overhaul of the banking system, the NBU simultaneously launched a radical internal transformation

Run on banks ends off, the banking system is stable though still dominated by state-owned banks

Banks' total assets by groups, UAH billion



Source: NBU.

Solvent banks were grouped under the relevant classification for the given years. Figures - number of banks in each group.

Number of banks

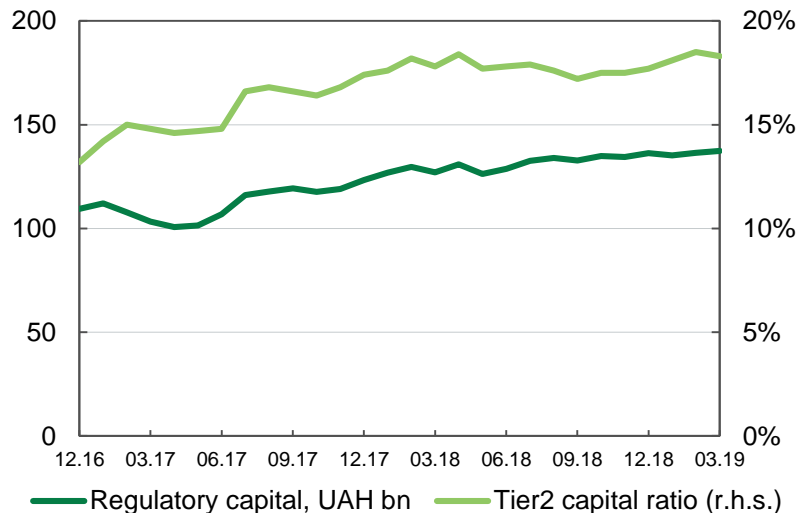
	2015	2016	2017	2018	May-19
Solvent	117	96	82	77	76
- change	-30	-21	-14	-4	0
State-owned	7	6	5	5	5
- change	0	-1	-1	0	0
Foreign	25	25	23	21	21
- change	0	0	-2	-2	0
Private	85	65	54	51	51
- change	-30	-20	-11	-2	0
Insolvent	3	4	2	1	1
- change	-13	1	-2	0	0

Source: NBU.

- 76 banks operate in the market as of the beginning of June.
- No new bank bankruptcies over last 1.5 years – a smaller number of banks results from M&A and banks' reorganizations into financial companies.
- At present, state-owned banks dominate the market – the issue which Ukraine started to resolve in 2018. Government has adopted *The Strategy for SOBs*, which aims at privatization of state-owned banks. New supervisory boards with independent Directors were appointed, which will lead to corporate governance improvement.

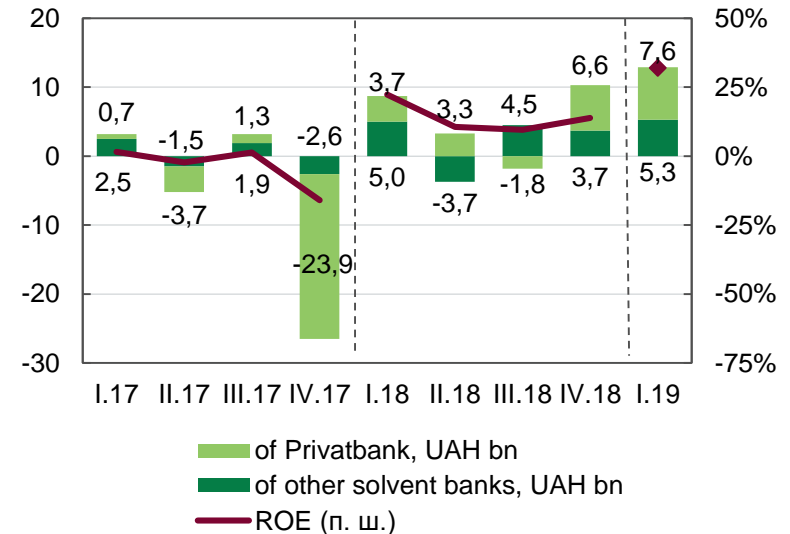
The banking system is solvent and profitable

Regulatory capital and regulatory capital adequacy



Source: NBU.

Banking system net profit, UAH billion

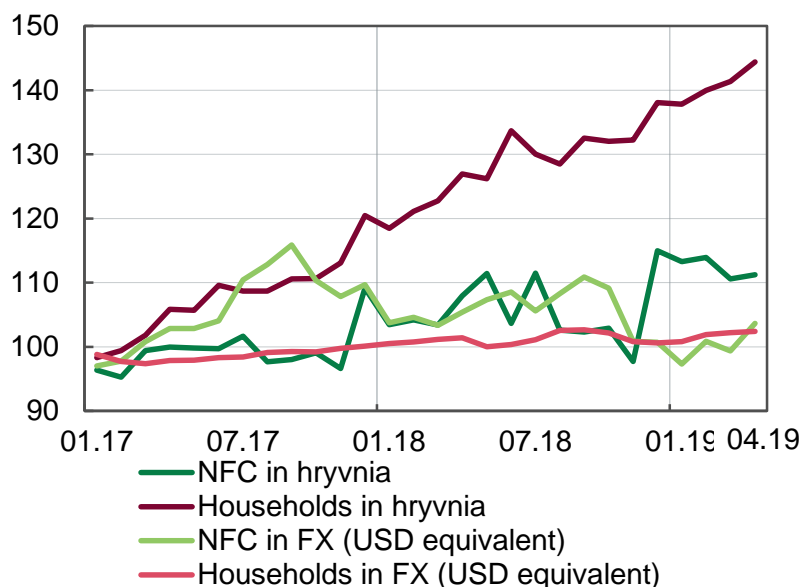


Source: NBU.

- Capital adequacy ratios are well above the minimum required level (10% for T1).
- Banking system returned to profitability in 2018, driven mostly by state-owned PrivatBank, while almost all large and medium-sized banks also reported solid financials (only 13 out of 76 banks reported net losses in 2018).
- In 2019, the trend continues, net profit for the banking system grew up 1.5x yoy, driven by both interest and commission income growth, LLPs rates are record low (cost of risk less than 2%).

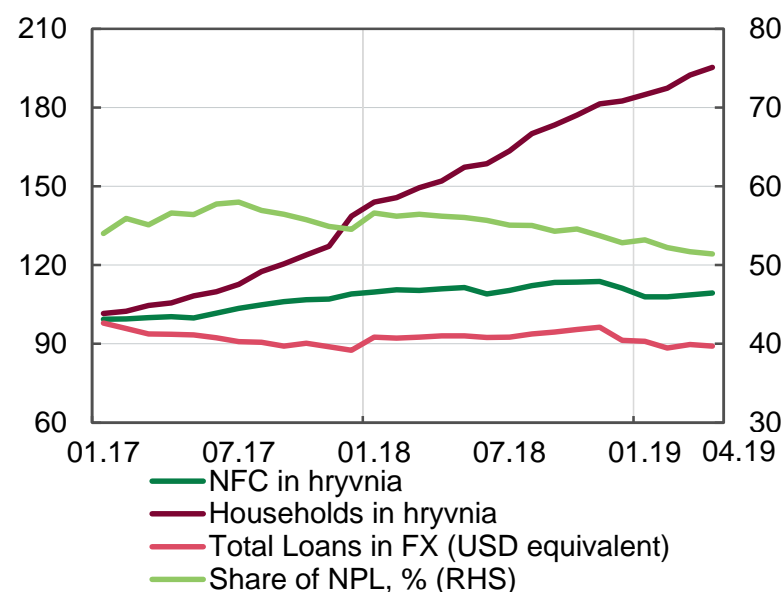
Both loans and deposits are growing, mostly UAH-denominated

Deposit Developments, 12.2016=100



Source: NBU.

Loan Developments, 12.2016=100

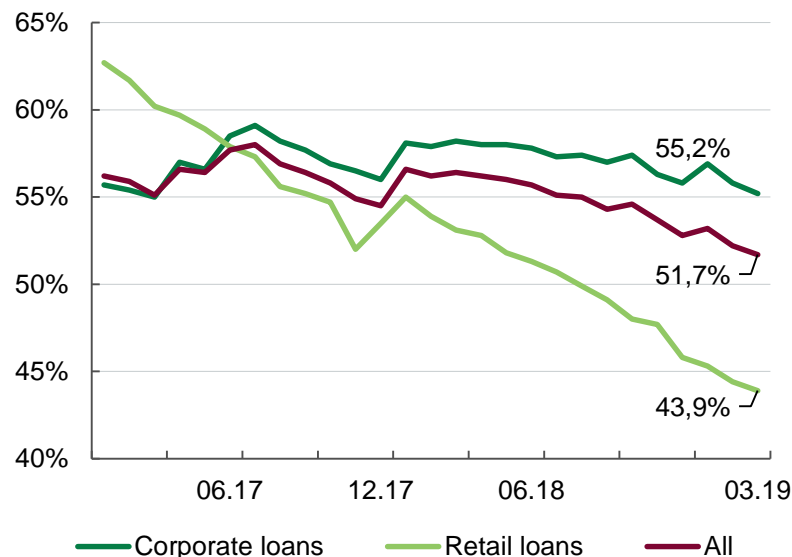


Source: NBU.

- Strong increase in nominal wages, high interest rates on the back of hryvnia appreciation and improved inflation expectations contributed to the inflow of households' UAH deposits.
- Consumer loans have been growing fast. Loans to high-quality borrowers with no record of loan default in 2014–2018 continued to grow by more than 25% yoy in 2018. However, high share of NPLs still restrains corporate loans growth.

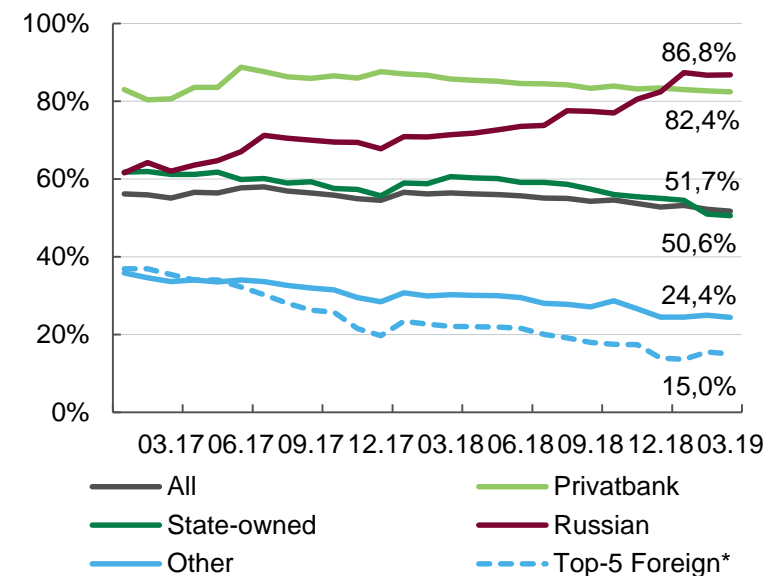
The NPL ratio is still high, but shows a solid downward trend

NPL portfolio ratio



Source: NBU

NPL portfolio depending on the ownership of the banks



Source: NBU

- The big share of NPLs is mainly caused by PrivatBank legacy portfolio – the companies related to its former shareholders, which stopped to serve their loans shortly after the bank was nationalized in late-2016.
- The rest of SOBs actively used restructuring tools in 2018. Hope, in 2019 this will be reflected in their statement and results.
- For private and foreign-owned banks NPL level is moderate and tends to decrease.

Key domestic challenges for the banking system



Dominance of state-owned banks



Still high volumes of NPLs



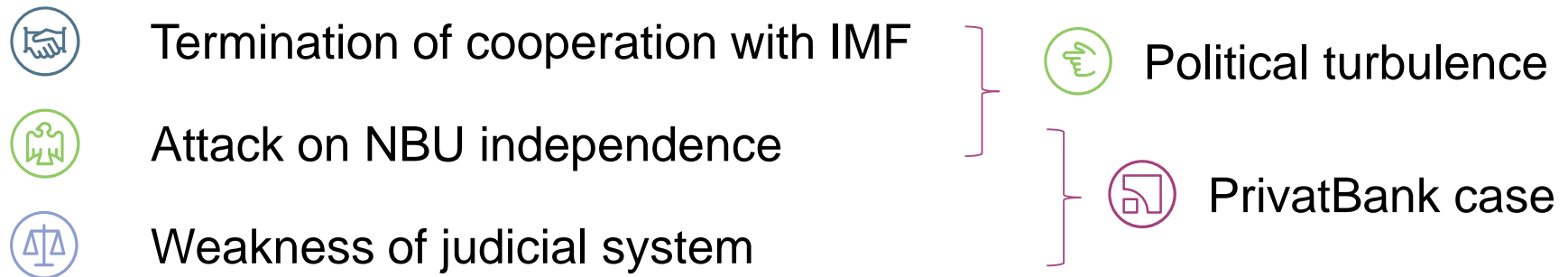
Maturity mismatches between funding and lending – prevalence of short-term funding



High share of FX-denominated loans and deposits

National bank of Ukraine has full capability and competence to properly address these challenges.

Key external threats are political uncertainty and politicians' attempts to interfere with the NBU's activities



- Political uncertainty has already resulted in postponement of the next IMF tranche until parliamentary elections and formation of a new government.
- Cooperation with the IMF is crucial for successful repayment of external public debt – the recent postponement increases the risk of potential fiscal dominance.
- Some recent decisions of Ukrainian courts bear risks to NBU independence and Ukraine's macroeconomic stability.
- Ukraine's key partners, including G-7 and leading IFIs have already confirmed they support the NBU's actions and see the NBU's independence as a key factor for financial and macroeconomic stability.
- **The turbulence rises. Safeguarding Ukrainian financial reforms is a duty of all stakeholders. We have to stand together to assure continuation of this path.**



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