



National Bank
of Ukraine

National Bank of Ukraine Strategy

Action Plan 2019



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Introduction

2018 was proof that a consistent and independent policy by the central bank is supportive of macrofinancial stability. Last year, the National Bank of Ukraine (NBU) focused on delivering price and financial stability and implementing long-awaited financial sector reforms.

As a direct result of that focus, Ukraine achieved many new highs and records, including: the fastest pace of economic growth in the past seven years, the lowest level of inflation in the past five years, and the highest level of international reserves in the past five years. The banking system is not only resilient, capitalized, and transparent, but also profitable – for the first time in five years. Ukrainians are becoming more and more used to cashless payments: four out of every ten hryvnia spent via payment cards are cashless.

Ukraine has embarked on a new cooperation program with the International Monetary Fund (IMF), laying the groundwork for a further strengthening of macrofinancial stability. Not only will the IMF program allow Ukraine to navigate several debt-heavy years, but it also sets benchmarks for state policy and reduces uncertainty for businesses and financial market players in an election year.

The central bank's priorities that made those results possible have been outlined in the Strategy of the National Bank of Ukraine. Approved and

made public in spring 2018, the NBU's medium-term strategy is the first document that outlines the central bank's goals for the coming years. This document is a step forward in the NBU's development as a modern, open, independent, and effective state institution; the strategy serves as a guiding beacon for the NBU's operations. At the same time, the strategy reduces uncertainty in the economy by providing a clear and understandable view on the NBU's policies to all stakeholders.

The strategy identifies seven goals for the NBU. Six of the seven are external, aimed at meeting the needs of financial system participants. To achieve those six goals, the NBU's institutional capacity must be robust, and that requirement informs the seventh, internal goal of the list:

1. Low and stable inflation.
2. Stable, transparent, and effective banking system.
3. Resumption of lending.
4. Effective regulation of the financial sector.
5. Free flow of capital.
6. Financial inclusion.
7. Modern, open, independent, and effective central bank.

The NBU's work towards those strategic goals allowed Ukraine to achieve the strong results and records in 2018. Below are the main steps the NBU took towards each of the goals.

Strategic Goals of the National Bank of Ukraine: Top Accomplishments in 2018

1. Low and Stable Inflation

Key accomplishments

- Inflation decreased to a five-year low of 9.8%, down from 13.7% in 2017.
- For the first time, the NBU's inflation target was set as an objective in the program of cooperation between Ukraine and the IMF.
- The NBU also updated its approach to interventions in the interbank foreign exchange (FX) market.
- The regulator committed to a more transparent monetary policy by publishing summaries of Monetary Policy Committee discussions.

In 2018, inflation returned to single digits and decreased to a five-year low. However, as expected, price growth exceeded the NBU's year-end target of $6\% \pm 2$ pp that was identified in the Monetary Policy Guidelines for 2018 and the Medium Term. The turnaround of the inflation trend and the weaker inflationary pressure was primarily driven by tight monetary policy. An increase in food supply and lower global food prices also contributed to the slowdown in inflation. At the same time, factors that are not impacted by monetary policy held back inflation from slowing at an even faster pace. These factors include higher administered prices, the wage-driven increase in production costs, the global oil prices that rose for most of the year, and a weather-driven decrease in the supply of vegetables used to make borshch.

2018 marked the five-year minimum of inflation. Ukraine's tight monetary policy conditions were predicated by a series of key policy rate hikes. The environment will ensure a continued slowdown in inflation in the coming years. As such, the NBU is gradually getting closer to its strategic goal of bringing inflation down to $5\% \pm 1$ pp in the medium term.

It is important that the medium-term monetary policy strategy that was adopted by the NBU Council established the immutability of the inflation target and the inflation-targeting principles of the implementation of monetary policy. This forms an institutional foundation for a stable monetary regime and improves the predictability and consistency of monetary policy, which stabilizes inflation expectations.

International partners are supporting the NBU in these efforts. In December 2018, the IMF approved

a new Stand-By Arrangement for Ukraine. For the first time in Ukraine's history, the NBU's inflation target ($5\% \pm 1$ pp) has been included as an objective of the IMF program. This is a sign that low and stable inflation is a prerequisite for sustainable economic growth and that the inflation-targeting regime chosen by the NBU is the most effective way to achieve that goal. In addition, the IMF's support proves that the NBU is realistic in its intentions to lower inflation to the target level over the medium term and subsequently maintain it in the range of $5\% \pm 1$ pp. That is an important signal for all stakeholders of the NBU, especially for households, businesses, and financial market participants.

In 2018, as part of efforts to further develop monetary policy, the NBU updated its approach to interbank FX transactions.

In the spring, to strengthen the market approach and transparency of the formation of the hryvnia exchange rate, the NBU changed its approach to prioritizing interventions in the FX market. As set out in the NBU's Foreign Exchange Market Intervention Strategy for 2016–2020, the NBU can make four types of FX market interventions: FX auctions, single rate interventions, request for quotations (best rate intervention), and targeted interventions. Until last year, FX auctions were the priority method of intervention. Since then, however, the NBU has not prioritized any individual type of intervention. Instead, the use of each intervention will be determined by prevailing conditions in the interbank FX market.

However, considering the need to minimize the impact of the central bank on the exchange rate

trend during FX interventions to accumulate reserves, the NBU will continue to favor those interventions in which the NBU accepts the price offered by FX traders.

In April, the NBU switched to FX interventions via Matching, a new platform for concluding contracts through trade information systems (Bloomberg, Thomson Reuters, etc.). The main advantages of the Matching platform include anonymity, an unlimited number of participants, and promptness. This innovation will drive increased competitiveness, transparency, and accuracy of the formation of the hryvnia exchange rate in the interbank FX market.

In 2018, following the practice of leading central banks that use inflation targeting, the NBU began

publishing *the Summary of the Discussion on the Key Policy Rate in the Monetary Policy Committee*. The summary provides details of the discussion between members of the Monetary Policy Committee (MPC) ahead of each key policy rate decision by the NBU Board. That has increased the transparency and predictability of the NBU's monetary policy. Businesses have started to better understand the logic behind monetary decisions, which has helped enhance the impact of the key policy rate on the level of interest rates in the economy and bring inflation expectations closer to the NBU's goals. As a result, the increased transparency of the monetary decisions has broadened the NBU's influence on the growth rate of consumer prices.

2. Stable, Transparent, and Effective Banking System

Key accomplishments

The NBU

- initiated the transition to Basel III international regulatory standards for banks
- implemented the risk-oriented supervisory review and evaluation process (SREP)
- introduced an annual assessment of the resilience of banks
- improved transparency and increased information disclosure standards for banks
- laid the strategic groundwork for macroprudential policy
- resolved the issue of information security and cybersecurity of banks
- improved the approach to structuring corporate governance at Ukrainian banks
- conducted a top-to-bottom review of bank licensing processes, and
- Introduced new standards for implementing risk management systems at Ukrainian banks and banking groups.

As part of the transition to Basel III international regulatory standards for banks, the NBU introduced its first macroprudential instrument last year – the Liquidity Coverage Ratio (LCR), a mandatory liquidity ratio. The LCR sets the minimum liquidity level required to cover a bank's net expected outflow of funds within 30 days in a stress scenario. It is more effective than current standards at reflecting the level of a bank's resilience to short-term liquidity shocks that are typical for crisis periods when significant outflows of client funds occur. The LCR meets generally accepted global approaches to liquidity assessment and is understood by international investors. The LCR was developed by the Basel Committee on Banking Supervision in response to the 2007–2008 global financial crisis.

Also in 2018, the NBU successfully introduced new supervisory tools based on the assessment of

risks and risk management quality at banks (risk-based approach). As such, the SREP has become a continuous process and one that is conducted simultaneously for all banks by assessing the size of risks and the quality of their management and by analyzing existing trends in bank activities, including by comparing a bank's key performance indicators with those of peer banks. The results of the assessment inform supervisory strategy for that bank. The strategy is based on the bank's viability over the subsequent 12 months, the sustainability of the strategy over a 3-year period, the adequacy of capital and liquidity to cover risks, and the state of corporate governance at the bank.

The NBU also introduced the annual assessment of bank resilience, which consists of an assessment of asset quality, as well as stress tests of the largest banks. The stress test models an unlikely

but realistic adverse macroeconomic scenario. Assessing asset quality and stress-testing banks are established practices at leading regulators around the world. They prevent an excessive accumulation of systemic risks and prepare banks for future crises. That approach contributes to the stability of the banking system and overall financial stability in Ukraine.

The NBU is constantly expanding the list of information that banks are required to disclose to stakeholders. Clients, lenders, analysts, and other financial market participants now have more ability to assess the financial standing of banks. At the end of 2018, Ukrainian banks for the first time ever disclosed the results of the assessment of asset quality and stress tests.

All of these actions were reflected in the Macroprudential Policy Strategy approved by the NBU last year. The document identifies the NBU's future actions that will ensure the financial stability that is necessary for sustainable economic growth. The strategy lays the groundwork for the introduction in Ukraine of a systemic macroprudential policy that is aimed at preventing the accumulation and materialization of systemic risks in the financial sector. Furthermore, the implementation of macroprudential policy by the NBU will enhance confidence in banks and support further macroeconomic stabilization. In the long run, it will facilitate sustainable economic growth, more resistant to negative shocks and crises.

In addition, in response to technological challenges last year, the NBU for the first time addressed the issue of information security and cyber defense of the banking system and defined mandatory information security requirements. Banks implemented basic information security measures in March 2018. This helped increase the stability and safety of banks, prevent and mitigate the consequences of possible malicious acts, and protect the interests of depositors and bank lenders from modern cyber threats.

In late 2018, the NBU approved the Recommendations on Corporate Governance at Ukrainian Banks, which are in-line with the recommendations on corporate governance put forth by the Basel Committee on Banking Supervision. The document contains recommendations on corporate governance issues, in particular regarding the responsibilities, functions, composition, and operating procedure of a bank's board, its collective suitability, the formation, composition, powers, and work procedures of committees of the bank's council, the role of the bank's council in ensuring the effective functioning of the internal control system at the bank, the introduction of an effective remuneration policy that will encourage employees to act in the interests of the bank and not resort to excessive risks, and disclosure by the bank of information about corporate governance.

Also, at the end of 2018, the NBU adopted a new regulation on bank licensing. This is a new document aimed at transitioning from a formal to a risk-based approach to licensing banks and providing regulators with tools for substantive analysis during the approval process.

Also important was the introduction of new standards for risk management systems. The NBU introduced the standards by approving the Regulation *On the Establishment of a Risk Management System in Ukrainian Banks and Banking Groups*. The document provides for greater involvement of a bank council's supervisory function in creating a powerful risk management culture, monitoring compliance with risk profiles, monitoring compliance with general risk management principles, and more. The regulation identifies the list of key risks (credit risk, liquidity risk, interest rate risk, market risk, operating risk, and compliance risk) that banks must identify, measure, monitor, control, and report. In addition, the bank should manage other significant risks it encounters during operations.

3. Resumption of Lending

Key accomplishments

- The protection of creditor rights has been enhanced.
- The NBU launched the NBU Credit Register.

In the past year, Ukraine adopted a law that the banking community had been expecting for more than two years and that reinforces the protection of the rights of creditors and investors: the Law of Ukraine *On Amendments to Certain Laws of Ukraine on a Resumption of Lending*. For a long time, significant legal risks had remained one of the main obstacles to the resumption of lending, first and foremost corporate lending. Developed with the support of the NBU, approved by the Verkhovna Rada, and signed by the president, the law eliminates most legislative loopholes that borrowers used to avoid repaying debt or to dodge their responsibility for a failure to repay.

Thanks to the law, banks have greater confidence in the legal protection of their rights and thus can ease requirements for potential borrowers. This will increase the volume of lending, reduce the cost of credit, and facilitate access for businesses and households to banking products.

Those improvements will also be helped by the newly granted access for banks to the NBU Credit

Register, which launched in 2018. On 1 September, the NBU allowed banks to obtain from the Credit Register information on borrowers, loan terms, fulfillment of loan obligations, and borrower classes. This information will help banks assess credit risks in a timely and thorough manner. Using the Credit Register, banks can gain access to information about a client's loans from other banks and a borrower's loan burden. This, in turn, helps create the conditions to reduce the level of credit risk and interest rates, which are directly dependent on the assessment of credit risk.

As a result, the NBU Credit Register will help reduce the proportion of distressed assets and the formation of a competitive market environment in which honest borrowers have advantages over unscrupulous borrowers. Ultimately, this will contribute to the resumption of lending and strengthen the financial stability of the banking sector.

4. Efficient Regulation of Financial Sector

Key accomplishments

- A draft version of the regulatory framework for the non-bank financial sector was prepared.

As a potential regulator of a part of the non-bank financial market after the functions of the National Financial Services Commission were divided last year, the NBU initiated discussions with market participants regarding the draft white paper titled *The Future of Regulating the Non-Bank Financial Sector*, in which it presented its vision for the regulation of the non-bank financial market. The document outlines the NBU's approach to market segmentation, licensing, prudential supervision, reporting, inspections, corporate governance, and the protection of consumer rights. The new regulation is intended to cover insurance companies, credit unions, pawnshops, leasing and factoring companies, and other financial

companies that exchange currency and transfer money, lend, provide guarantees, etc.

The regulatory model has two main objectives: identifying new growth areas for each segment of the non-bank financial market and ensuring maximum protection for financial service consumers. The project takes into consideration the high segmentation and heterogeneity of players in these markets, both by type of product and by type of service. It offers the most flexible approach to licensing non-bank financial institutions and to reporting and supervision.

The main innovation for market participants will be the risk-based approach that the NBU has been

successfully implementing in the banking market for the third consecutive year. The new approach will make it possible to predict problems at companies and enact preventive measures, rather than react once a company has become insolvent. In addition, the NBU is focusing on introducing corporate governance standards that will improve

company performance and protect consumer rights. The new model of regulation of non-bank financial institutions is intended to achieve market efficiency and transparency as well as to bring the non-bank financial services received by Ukrainian consumers closer to European best practices.

5. Free Flow of Capital

Key accomplishments

- In 2018, Ukraine adopted the *Law On Currency and Currency Operations* – legislation that ensures the free flow of capital.
- A series of temporary currency restrictions for businesses and banks were eased.

In the summer of 2018, the Verkhovna Rada adopted the *Law On Currency and Currency Operations*, which was developed by the NBU. The law enables Ukraine to move from a repressive, obsolete, and complicated 25-year-old system of currency regulation to a new, liberal, transparent, and modern model. All existing restrictions will be gradually removed, and eventually currency transactions in Ukraine will be conducted on the principle that “everything that is not forbidden by law is allowed”. Businesses and households will finally be able to decide when and how to conduct currency transactions, without restrictions and without getting permission from the NBU. The liberalized approach to currency markets will become the basis for easing the conduct of business, improving Ukraine’s investment climate and the inflow of foreign capital, and promoting sustainable economic growth.

To enforce the law, the NBU also developed a simple, understandable, and accessible currency regulatory framework. The framework consists of only seven resolutions, replacing an intricate regulatory system made up of dozens of regulations. The NBU developed a draft version of each resolution in conjunction with businesses and the banking community. The resulting regulatory framework was thus created with market participants and for market participants, rather than against their interests.

At the same time, the NBU continued to liberalize currency markets throughout the year without

waiting for that law to enter into force. A key decision, and one that was unanimously supported by business, was the permission to repatriate dividends for all past years and to increase the monthly limit from USD 5 million to USD 7 million. In addition, the NBU expanded opportunities for early repayment of foreign currency loans to non-residents and liberalized the terms for foreign currency transactions.

The NBU also introduced a series of concessions for banking institutions. First and foremost, the NBU expanded the opportunities for banks to perform their own currency transactions in the interbank market. The cancellation of the requirement for the authorized balance of the purchase and sale of foreign currency and investment metals by banks within one working day allowed banks to actively trade currency in the interbank market and thereby more effectively manage currency liquidity. This allowed the market to find an equilibrium independently and efficiently. In addition, the NBU unified the limits for the general long and short open currency positions of banks to deepen the FX market, increase its liquidity, and improve the efficiency of currency risk management by banks.

These and other concessions helped improve Ukraine’s business and investment climate and contributed to the development of financial markets.

6. Financial Inclusion

Key accomplishments

- The NBU introduced the ability to remotely open bank accounts using the BankID system.
- The NBU created the conditions for banks to transition to paperless customer service operations (without bringing present physically and without the need for a physical signature or for the use of any paper).
- The PROSTIR National Payment System (PROSTIR NPS) made a substantial leap forward in its development.
- The usage area for PROSTIR cards expanded.

Since last year, Ukrainians have been able to open accounts and access banking services online with the use of electronic documents without having to wait in line. The NBU's BankID system, which provides remote identification in Ukraine, was key in unlocking online banking. Using this system, Ukrainian citizens can remotely access state, administrative, banking, and other services. This greatly increases the availability of financial services for Ukrainians and helps boost the involvement of Ukrainians in the financial system.

The Paperless Project was another of the NBU's successes in 2018. Aimed at incentivizing banks to abandon the use of paper documents in client services, this project is as an important step towards expanding the accessibility of financial services for Ukrainians. It affords Ukrainians new opportunities to bank without being physically present, without the use of paper documents, and without the need to physically sign documents.

The paperless changes have affected the processes of identifying and verifying clients, cash operations, servicing foreign trade, trade finance transactions, and building client credit histories. Clients can now remotely communicate with their bank, including through electronic and digital signatures.

Over the past year, the NBU made significant progress in developing the PROSTIR NPS, including

the following achievements:

- the ability to make payments using PROSTIR payment cards at 95% of all POS terminals
- the ability to make card-to-card transfers between banks (P2P transfers)
- implemented two-factor authentication to ensure secure online payments
- expanded the system's product line
- implemented a joint project with Kyivstar PrJSC to introduce cashless payments using PROSTIR electronic money and mobile phone balances.

In addition, the NBU substantially expanded the usage area of PROSTIR cards last year by signing an agreement with UnionPay International, the world's largest international payment system by the number of issued payment cards. Under the agreement, co-badged cards of PROSTIR NPS and UnionPay International will be issued.

Thanks to UnionPay's global card acceptance network, users of the PROSTIR/UnionPay co-badged cards will be able to pay for goods and services and withdraw funds at ATMs in Ukraine and practically anywhere in the world. The development will also promote competition in Ukraine's payment market.

7. Modern, Open, Independent and Effective Central Bank

Key accomplishments

- The NBU's medium-term strategy has been approved.
- The NBU and the banking system have converted to IFRS 9.

The strategy of the NBU for the medium-term was approved and presented to the public in spring 2018.

The strategy is the greatest achievement on the NBU's path to becoming a modern institution. First, it

promotes transparency. The NBU Strategy is a clear reference for all stakeholders of the central bank that allows for the full understanding of key policy areas and prevents surprises or inconsistencies. Second, it will contribute to efficiency. The strategy defines clear goals, the actions required to achieve those goals, criteria and deadlines, key activities, and measurable outcomes.

In addition to the strategy, the NBU presented its updated brand – a logical embodiment of its new philosophy and the ongoing changes and transformations. According to the new brand vision of an architect of the financial sector, the central bank is not only a regulator but also a partner for market participants, a center of expert opinion on the economy, a hub for gifted professionals, and an innovator open to new ideas and projects.

Last year, the NBU and Ukraine's banking system converted to the new IFRS 9 standard, as did the global financial community. Developed in response to the need to fill gaps in the classification of financial assets and the assessment of credit risks that were revealed by the global financial crisis, IFRS 9 introduces a new model for assessing credit losses – not incurred losses, as was the case prior to IFRS 9, but risk-based expected losses.

The NBU was one of the first banks in the world to start the conversion to IFRS 9 as it is an important element of economic development and the

development of financial markets and contributes to the establishment of a transparent information infrastructure. It is also important because the NBU's activities directly influence Ukraine's public finances. The NBU has effectively converted to IFRS 9 and, thus, was able to share its experience with other central banks and ensure the smooth conversion of the Ukrainian banking system to the new standard.

The banking sector has converted to IFRS 9 gradually: at the beginning of 2018, the NBU offered banks a three-month transition period, during which no enforcement measure was applied for non-compliance with requirements and reporting rules due to changes in the assessment of financial instruments under IFRS 9. That period was then extended to the end of June to enable a smooth transition to interim reports for banks. The conversion to the new standard did not have a significant impact on the banking sector's operating performance. Despite concerns about the need to increase capital because of the new standard, the conversion to IFRS 9 did not impact the capital adequacy of banks.

Overall, the conversion to IFRS 9 is a positive development that will encourage banks to be more responsible and more aware of the risks they take on. Moreover, financial reporting under IFRS increases the trust of stakeholders in the financial reporting of the Ukrainian banking system.

NBU Action Plan for 2019

Risks to Achieving Goals

Before planning its action plan for 2019, the NBU assessed the risks posed by the environment in which it exercises its mandate. The likelihood of those risks, capabilities for their management, and the extent to which they can cause the NBU to deviate from the goals of the NBU Strategy constitute the basis for the action plan.

The risks the NBU faces can be divided into external risks (those that emerge outside Ukraine's economy) and internal risks (those caused by factors within Ukraine).

External risks:

- External military aggression. Attempts by Russia and its military to interfere in Ukraine's affairs are still possible. Lately, Russia's aggression has taken on a new form, and the situation around the Sea of Azov will remain tense.
- Trade wars and a slowdown in the global economy. The threat of disorderly Brexit persists, as does the risk of an escalation in the trade wars between the US and China and other countries. Through negotiations, the US and China have agreed to postpone, but not cancel, increases to customs tariffs. Any escalation of trade wars between the world's largest economies may slow the growth in global trade and cause problems for the global economy. That type of conflict could cause an excess supply of raw commodities in certain regions and depress prices. In such a case, or if access

to certain markets were restricted, Ukraine's foreign currency proceeds from exports would decline, which would pressure the hryvnia exchange rate and drive up inflation.

- Weakened interest in emerging markets and the resulting capital outflows from those markets. A rapid tightening of monetary policy by leading central banks prompts capital outflows from emerging markets like Ukraine. Experts are becoming increasingly concerned with the prospect of a global recession.

Domestic risks:

- A deterioration of inflation expectations as the new election cycle unfolds. As the new election cycle starts, so grows the amount and intensity of populist statements aimed at winning over voters ahead of the next election.
- Labor migration of Ukrainians. Ukraine's continued integration into European structures, including the start of visa-free relations with Schengen states, has already increased the volume of workers moving from Ukraine to countries with higher wages. The outflow of workers is exacerbating the disparity between supply and demand on the domestic labor market, leading to higher wages and shortages of qualified staff, which hinders the economy's potential growth and puts pressure on prices. The announced easing of employment rules for foreign citizens in the Czech Republic and Germany enhances this risk for Ukraine.

The Nbu's Actions and Key Activities in 2019

The goals set out in the NBU's Strategy can be achieved by combining two types of measures. The first type comprises **actions** or direct changes that are clearly achievable and, thus, can be planned within a concrete timeframe. The other comprises **key activities**, or the long-term continuous process of the use of measures that result in gradual changes with the goal of achieving a desired effect.

When planning the activities of the National Bank of Ukraine for 2019, we took into account the need to apply both types of measures and described our plans accordingly.

The Strategy of the National Bank states that the value created by the regulator can multiply and create conditions for the creation of new value by other clients from the list of clients of the National Bank.

At the same time, the final direct or indirect recipient of the value created by the NBU, as well as the values created by other clients of the NBU, is the last group of clients — citizens of Ukraine.

Within the framework of the Strategy for Creating End Value for Citizens of Ukraine, the National Bank has a non-uniform chain of mandate implementation: the achievement of some goals of the National Bank is impossible without the active

involvement and support of other participants in the financial ecosystem.

At the same time, the National Bank is an equal participant in the system and is not able to authoritatively involve other stakeholders in fulfilling their goals. However, the National Bank is convinced that its objectives are not only aimed at fulfilling the statutory mandate of the regulator, but are a prerequisite for the economic well-being of all participants in the Ukrainian economy. That is why achieving these goals is mutually beneficial and necessary in historical perspective for the country. Thus, the National Bank believes that the only possible way to achieve the objectives of the NBU Strategy is to come to an understanding with stakeholders, and at the same time is convinced that achieving such an understanding is possible and timely.

When planning the achievement of goals, there will be identified those stakeholders (from among the clients of the National Bank) interaction with which is necessary to achieve the expected results.

- [N] – The National Bank of Ukraine
- [X] – The expert community
- [P] – The government as a policymaker
- [F] – The financial sector
- [B] – Business entities
- [S] – The government as a service provider
- [H] – Households

Low and Stable Inflation

Actions		
Introduce a new operational framework for monetary policy: improve procedures for monetary operations to enable a more flexible response to changes in liquidity in the banking system	Q1	
Develop and introduce an automated processing system for Big Data	Q4	

Key actions	
Coordinate efforts with other authorities that are mandated to ensure price stability	[P][S]
Foster the development of financial markets and thus strengthen the impact of monetary instruments on inflation and economic growth	[P][F]
Improve the toolkit for macroeconomic forecasting: expand the range of tools and upgrade current models	
Communicate to the public, businesses, and participants of financial markets the motives and consequences of monetary policy decisions, including by publishing the Summary of the Discussion on the Key Policy Rate in the Monetary Policy Committee and researching the possibility of publishing a key policy rate forecast, as well as holding meetings with the media, experts, money market participants, and the academic community and students in Kyiv and other regions.	

Expected effect
<ul style="list-style-type: none"> ▪ A decrease of inflation to 5% in the mid-term, which will create the basis for improved investment attractiveness and sustainable economic growth in Ukraine ▪ A narrowing of the inflation expectations of economic agents to the NBU's inflation targets and the elimination of ambiguity on future inflation, which is required to decrease loan rates ▪ The operational goal of monetary policy is to keep hryvnia interbank rates close to the NBU's key policy rate

Stable, Transparent, and Effective Banking System

Actions		
Establish independent supervisory boards at state-owned banks	Q1	[S]
Develop the calculation method and introduce the Net Stable Funding Ratio (NSFR) for the new structure of regulatory capital	Q4	
Introduce revised requirements for internal control systems at banks	Q3	
Improve and automate the NBU's procedures for performing supervisory functions	Q4	
Improve internal financial monitoring systems at banks	Q4	[F]

Key actions		
Further harmonize prudential requirements on banks with EU laws and the recommendations of the Basel Committee on Banking Supervision		
Promote the risk-based approach for banking supervision and bank licensing procedures		
Regular stress-tests and SREP of banks		
Examine banks' plans on resolving non-performing loans		
Support legislation for corporate governance requirements at banks		[P]

Expected effect	
<ul style="list-style-type: none"> ▪ banking system that is resilient to macroeconomic shocks and systemic risks ▪ the banking system's liquidity ratios complying with Basel III standards and CRD IV/CRR; the share of high-quality liquid assets in the banking system being sufficient to comply with the LCR at 100% ▪ more transparent prudential requirements on banks, improved supervisory processes, and instruments harmonized with the best practices of the ECB and the EBA ▪ Improved standards for establishing risk management systems at banks will enhance the quality of bank loan portfolios and increase the banking system's profitability ▪ corporate governance in banks, including state-owned banks, that adhere to international standards and best practices ▪ Introduction of requirements on the collective suitability of the supervisory and management boards, updated requirements on business reputation and the individual suitability of bank managers ▪ higher quality information disclosed by banks ▪ a reduction of the de-risking effect (refusal of foreign financial institutions to prolong correspondent relationships with Ukrainian banks) 	

Resumption of Lending

Actions		
Introduce requirements on the management of non-performing exposures at banks in-line with recommendations from the ECB	Q3	

Key actions		
Support regulation that develops the secondary market for non-performing exposures and legislation that strengthens the rights of creditors and investors on the primary real estate market		[P]
Enable banks to access state registers for customer data		
Encourage banks to resort to out-of-court settlements for non-performing exposures, including through financial restructuring		[F]

Expected effect		
<ul style="list-style-type: none">▪ A gradual reduction of the non-performing loan portfolio (including due to the development of the secondary market for non-performing exposures)▪ Growth in bank loan portfolios equal to or above the rate of nominal GDP growth▪ Increased share of long-term corporate and retail loans▪ Reduced credit risks at banks		

Efficient Regulation of Financial Sector

Actions		
Improve the target-based consolidated regulatory and supervisory model of the financial sector by adopting relevant draft legislation	Q1	[P]
Open a global depository account with the NBU Depository	Q1	
Streamline licensing rules for non-bank financial institutions	Q2	
Centralize the depository function in Ukraine: Align with the NSSMC and the National Depository of Ukraine on the conditions for transferring depository record-keeping functions for domestic government bond operations from the NBU Depository to the National Depository of Ukraine	Q3	[P]

Key actions		
Foster the development of new capital market infrastructure that meets international standards (EMIR, PFMI IOSCO)		[P]

Expected effect		
<ul style="list-style-type: none"> ▪ Expanded and diversified capital markets in Ukraine ▪ Greater access for economic agents to financial resources ▪ Simplified requirements for non-residents to enter the securities market, including the domestic government bond ▪ Improving the quality of regulation of the non-bank financial market ▪ Increased trust in banks and other financial services participants 		

Free Flow of Capital

Actions		
Revise the NBU's legal framework on foreign currency regulation in accordance with the Law of Ukraine <i>On Currency and Currency Operations</i>	Q1	
Implement recommendations from the OECD on counteracting base erosion and profit-shifting (following the adoption of legislation on the implementation of the BEPS Action Plan)		[P]
Join the international system for the automatic exchange of information (approval followed by the introduction of draft laws on the implementation of the FATCA and accession to the Multilateral Competent Authority Agreement on the Automatic Exchange of Financial Account Information according to OECD standards)		[P]

Key actions	
Gradually liberalize/eliminate restrictions on foreign currency transactions according to actions identified in the road map, provided there is no threat of financial instability	

Expected effect
<ul style="list-style-type: none"> ▪ Expanded options for economic agents to execute foreign currency transactions ▪ Greater integration for Ukraine into international capital markets ▪ Increased foreign investment in the Ukrainian economy ▪ Improved financial and tax transparency of businesses and households

Financial Inclusion

Actions		
Introduce the international bank account number standard (IBAN)	Q2	[F]
Develop a strategy to improve financial literacy in Ukraine	Q2	[P]
Develop a national strategy for financial inclusion in Ukraine	Q4	[P]
Introduce requirements for disclosing information on financial services to consumers	Q2	[H][P] [F]
Regulatory support of the use of the BankID System for individuals remote identification	Q2	[F]
Implement standards for making payments via QR codes for market participants	Q2	
Present proposals on legal amendments for the implementation of PSD2 (draft law <i>On Payment Services</i>)	Q4	
Create the NBU Expert Council on Communicating with Innovative Companies and Projects	Q1	
Issue co-badged PROSTIR–UnionPay cards by Ukrainian banks	Q4	

Key actions	
Promote financial inclusion in Ukraine	[F]
Enhance the protection of the rights of financial services consumers	[P][F]
Stimulate the development of innovative financial services and strengthen cooperation between financial services market participants	[F]
Promote paperless technologies at the NBU and the banking system by simplifying regulations and encouraging the use of digital/electronic signatures	[F]
Host economic awareness days in Ukraine's oblast centers to improve economic and financial awareness	
Improve the public's awareness of the possibilities and benefits of remote identification for using financial and other services	[P][F]

Expected effect
<ul style="list-style-type: none"> ▪ enhanced protection of the rights and interests of financial services consumers ▪ expanded financial opportunities for economic agents and greater access to financial services/infrastructure ▪ development of banking and financial products that can be provided to customers remotely ▪ use of IBAN account numbers for domestic and cross-border settlements ▪ improved settlement speed ▪ improved public financial literacy ▪ greater electronic workflow and communication with market participants ▪ improved performance and competitiveness of Ukraine's banking system ▪ development of innovative solutions/services on the financial services markets

Modern, Open, Independent and Effective Central Bank

Actions		
Develop the NBU Strategy and the regulator's brand plan	Q4	
Establish the NBU Strategy and development plan for international cooperation	Q1	
Establish the NBU Expert Platform	Q1	
Introduce a mid-term financial plan that meets the NBU's strategic priorities	Q2	
Launch the NBU's new website	Q2	
Introduce the concept of process management as an instrument for the implementation of the NBU Strategy	Q2	

Key actions		
Improve the effectiveness of the communication of the NBU's mandate, goals, approach, thinking, consequences, and plans for its policy and operating activity, and provide access for customers of the NBU to the information required to make informed decisions		
Build a brand as a top employer and develop the NBU's human capital		
Improve transparency during project discussions with stakeholders and the adoption of regulatory decisions		
Rebuild internal processes that meet the value-added principle for internal and external clients		
Automate and digitalize NBU processes		

Expected effect		
<ul style="list-style-type: none"> ▪ improved trust of stakeholders to the NBU as to an open, independent, competent, and effective regulator ▪ improved cooperation of the NBU with professional market participants ▪ development of the NBU's analytical and research capabilities and the further establishment of the NBU as a center of excellence in Ukraine and abroad ▪ improved communication of information to clients of the NBU ▪ improved quality of preparation for and approval of decisions at the NBU ▪ modern information infrastructure and automated processes ▪ improved allocation of resources and reduced administrative expenses 		

Conclusions

By making this document public, the NBU as a modern, open, independent, and effective central bank, is committing to delivering low and stable inflation; ensuring a stable, transparent, and effective banking system; reviving lending; and promoting the effective regulation of the financial sector, free movement of capital, and financial inclusion.

In 2019, the NBU will focus on achieving these strategic objectives by implementing the actions outlined to create a favorable environment for financial system participants – from banks to businesses, and from current consumers of banking services to those who currently have no access to these services.

At the same time, the NBU itself is also a participant in the financial system, meaning its ability to meet strategic goals often directly depends on the

actions of other participants. The NBU is open to constructive cooperation with all stakeholders and encourages all those stakeholders to join in the efforts to develop the Ukrainian economy and the financial system.

The NBU's ability to successfully achieve its strategic goals is predicated on an absence of substantial shocks in the internal and external environments. If risks materialize, they could threaten the NBU's ability to enact the key activities that are required to achieve its strategic goals. In particular, the ability to curb inflation and to ensure the free movement of capital is contingent on the health of the global economy, regardless of the presence of protectionist sentiments, movements in commodity prices, and investor interest in emerging markets. Finally, any escalation of military aggression could threaten not only future achievements but also past accomplishments.

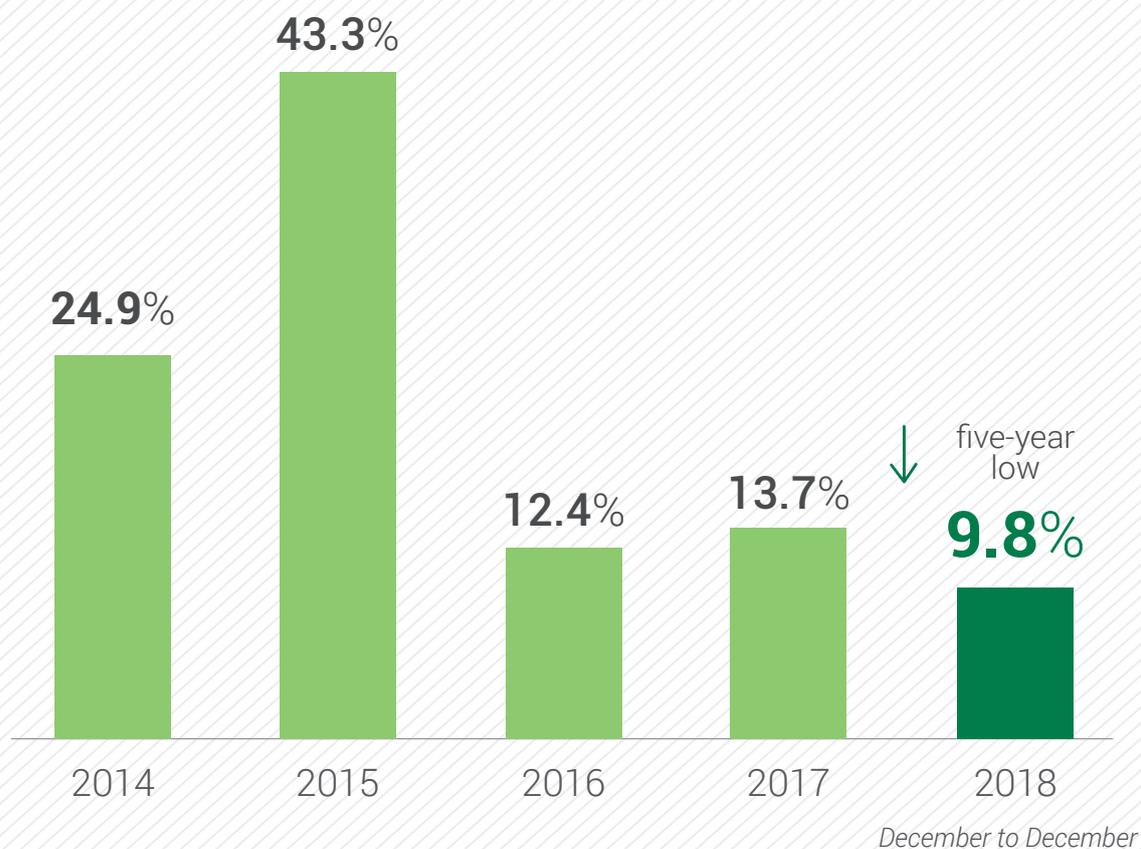


Annexes

2018 Accomplishments

<p>The NBU laid the groundwork for its macroprudential policy</p> 	<p>Inflation declined</p> <p>to 9,8% from 13,7%</p> 	<p>Remote account opening capability</p> <p>BankID</p>
 <p>The Law On Currency and Currency Operations</p>	<p>Analysis of banks' business models as part of SREP</p> 	<p>Enhancing creditor rights protection</p> 
 <p>Transition to Basel III ratios for banks</p>	<p>Strategy</p>  <p>of the NBU</p>	 <p>Annual assessment of banks' resilience</p>
<p>NBU Credit Register</p> 	<p>Transparency in monetary policy: Summary of discussion by members of the MPC</p> 	 <p>The NBU mitigated currency restrictions for businesses and banks</p>
<p>The NBU prepared a draft of future regulation of the non-bank financial sector</p> 	 <p>The NBU identified information security requirements for banks</p>	<p>Transition to IFRS 9</p> 

Consumer price inflation decreased to 9.8%, a **five-year low**



What restrained price growth:

-  The NBU raised its key policy rate
-  FX market conditions were favorable
-  Domestic supply of food increased as global food prices fell

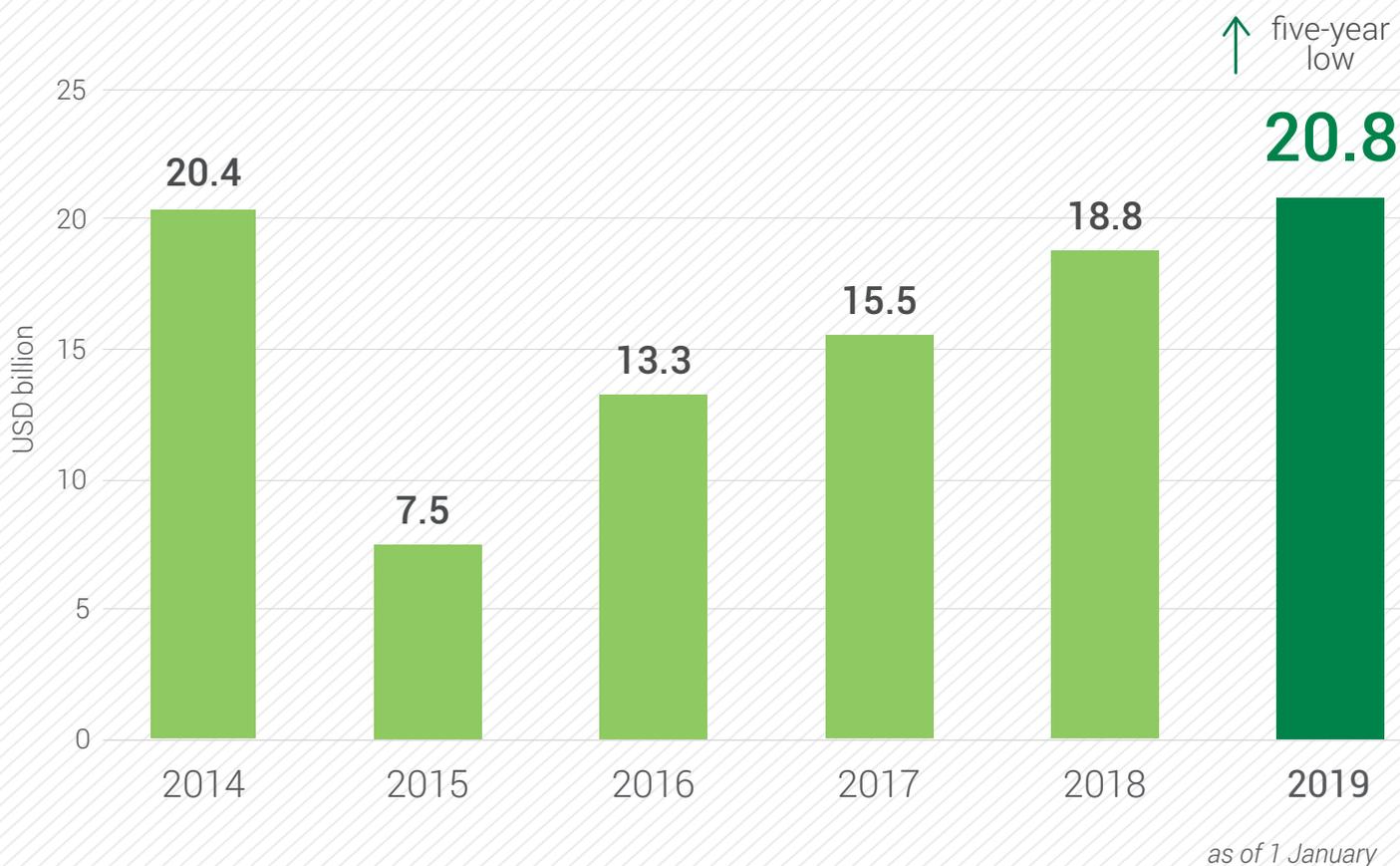
What stimulated price growth:

-  Administered prices (billing rates for gas, passenger transportation, etc.) increased
-  Consumer demand and production costs grew rapidly, driven by higher wages
-  Unfavorable weather resulted in the cost of borsch vegetables increasing significantly



Inflation overshot the NBU target in 2018 (6% ± 2 pp) due to factors that were only partially influenced by monetary policy. In 2019–2020, inflation will continue to decrease until it reaches 5%, the NBU predicts.

Ukraine's international reserves increased to USD 20.8 billion – a five-year high



What facilitated the growth in reserves:



The NBU purchased the excess currency in the interbank FX market



The IMF, World Bank, and EU provided financing



The government placed bonds in the domestic and external markets

The Law On Currency and Currency Operations is...



“Visa-free travel for capital”: freedom for businesses and the public to independently decide when and how to conduct currency transactions without limits or permission from the regulator



Easy, transparent, and consistent currency regulation as a step toward improving the investment climate



Proof of Ukraine's ability to be part of Europe. Under the EU-Ukraine Association Agreement, Ukraine takes responsibility to ensure free movement of capital



An **opportunity to speed up currency liberalization:** a raft of painful restrictions will be cancelled when the law has gone into effect



Guarantee of financial stability: the NBU will lift the rest of the restrictions gradually and carefully under favorable macrofinancial conditions



The NBU's capability to forestall and overcome all types of financial crises and create conditions for sustainable economic growth for years to come

Currency liberalization measures that businesses and households will enjoy after 7 February 2019



Canceled

- **currency supervision of export/import transactions** worth up to UAH 150,000
- **individual licenses** to conduct currency transactions
- **sanctions** that suspend international economic activity
- the **limit** on early repayment of external obligations
- **registration** of external borrowings
- **double checking** of transactions when the customs declaration is received by another bank



Allowed:

- **free opening of accounts** for legal entities abroad
- **settlements in foreign currency** under foreign-currency-denominated government bonds
- **currency swaps** between banks, on the one hand, and residents and nonresidents, on the other hand
- **nondeliverable forward contracts** and forward contracts to hedge debt operations
- **import/export** of foreign currency cash and investment metals by legal entities
- **foreign-currency payments** for life insurance purposes
- **accumulation of currency** in accounts of legal entities to repay external obligations
- **unlimited investment by banks** in investment-grade securities
- **investment and lending** to residents from hryvnia-denominated loro accounts of nonresident banks
- **investments** in Ukraine in currencies belonging to group two of the currency classifier



Increased:

- the **settlement period** for export/import transactions is extended to 365 days
- the **limit on sending remittances abroad** without opening a bank account for individuals is increased tenfold, to UAH 150,000 a year
- the **limit on the purchase of investment metals** by individuals and legal entities is raised from 3.21 troy ounces a week (100 g) to an equivalent of UAH 150,000 a day, with no limitations on specialized legal entities

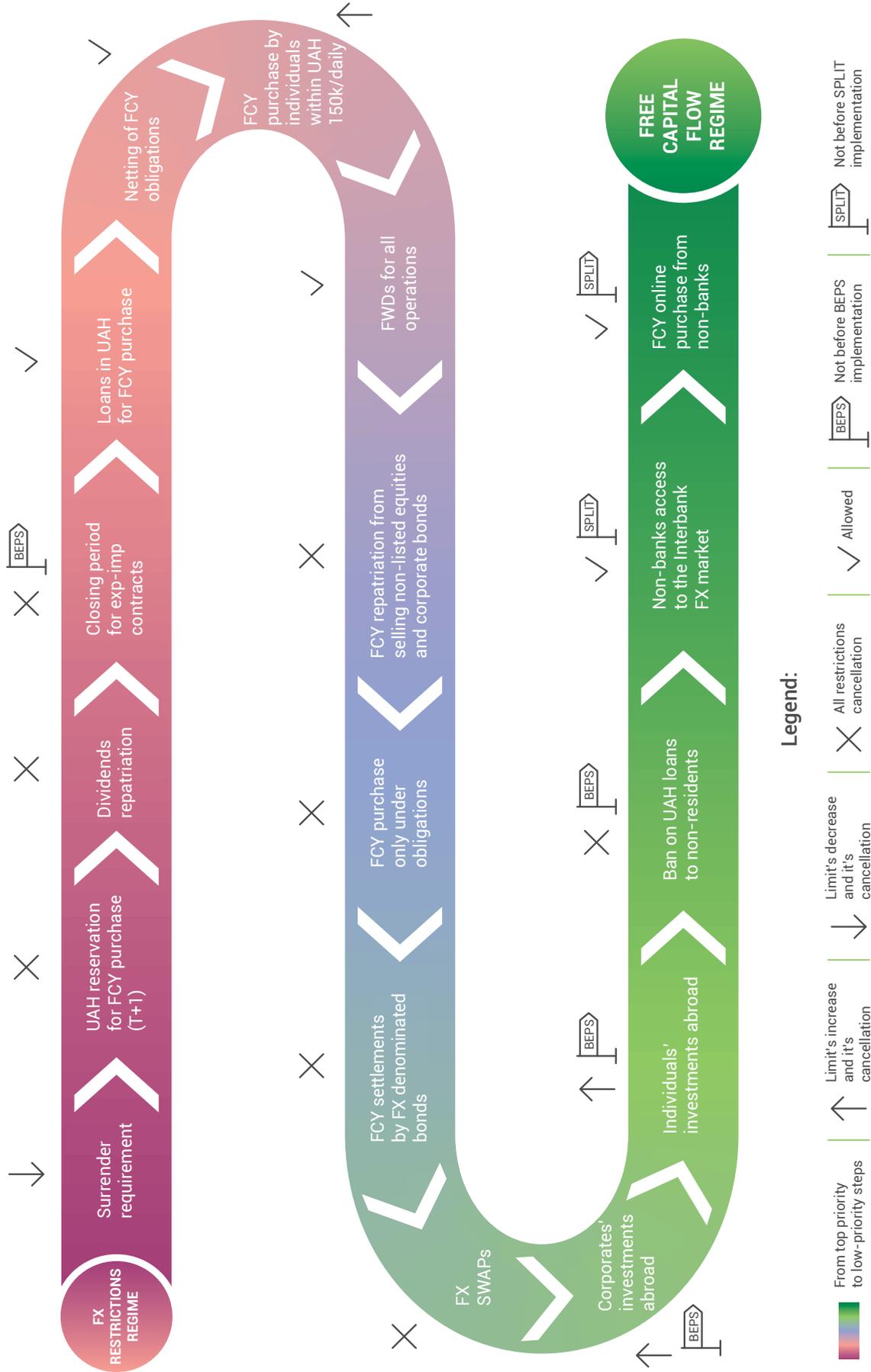


Eased:

- **transactions** involving accounts of nonresident legal entities in Ukrainian banks
- cross-border **movement of currency valuables**: there is now a unified procedure for the obligatory customs declaration of all valuables worth at least EUR 10,000

The more than 20 currency liberalization measures will ease the conduct of business and improve Ukraine's investment appeal

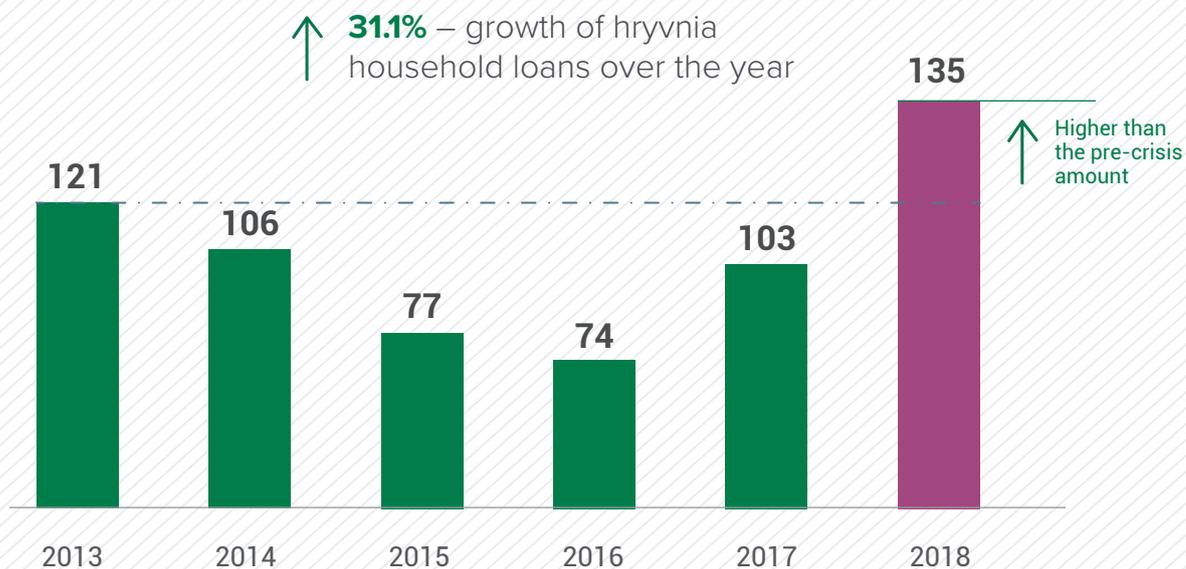
The road map for cancelling FX restrictions



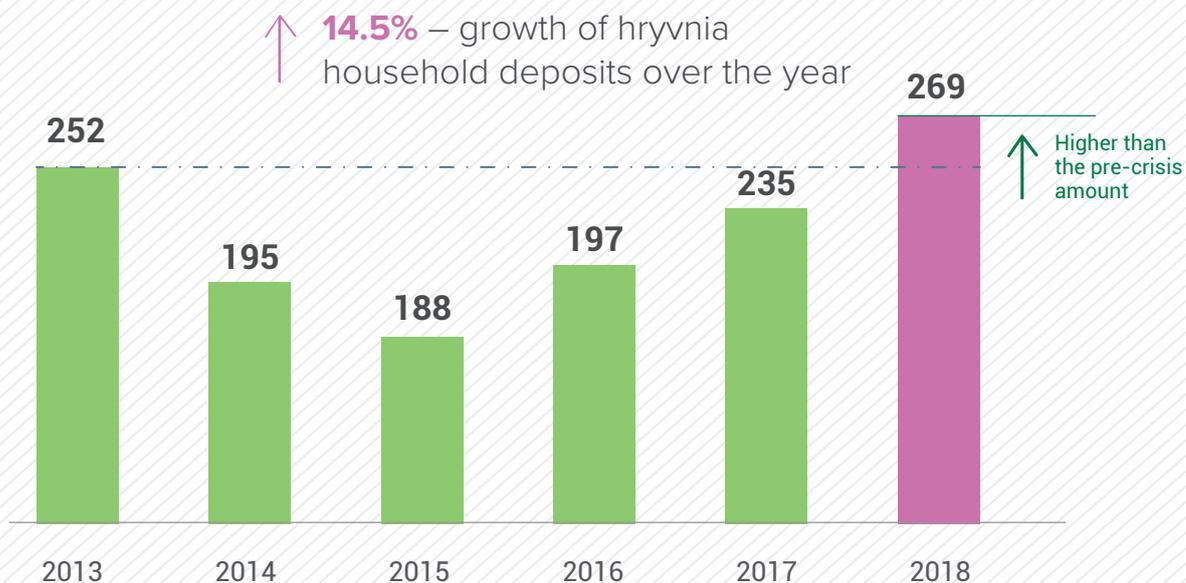
In 2018, banks stepped up efforts to engage the public



Portfolio of Hryvnia Household Loans (UAH billion)



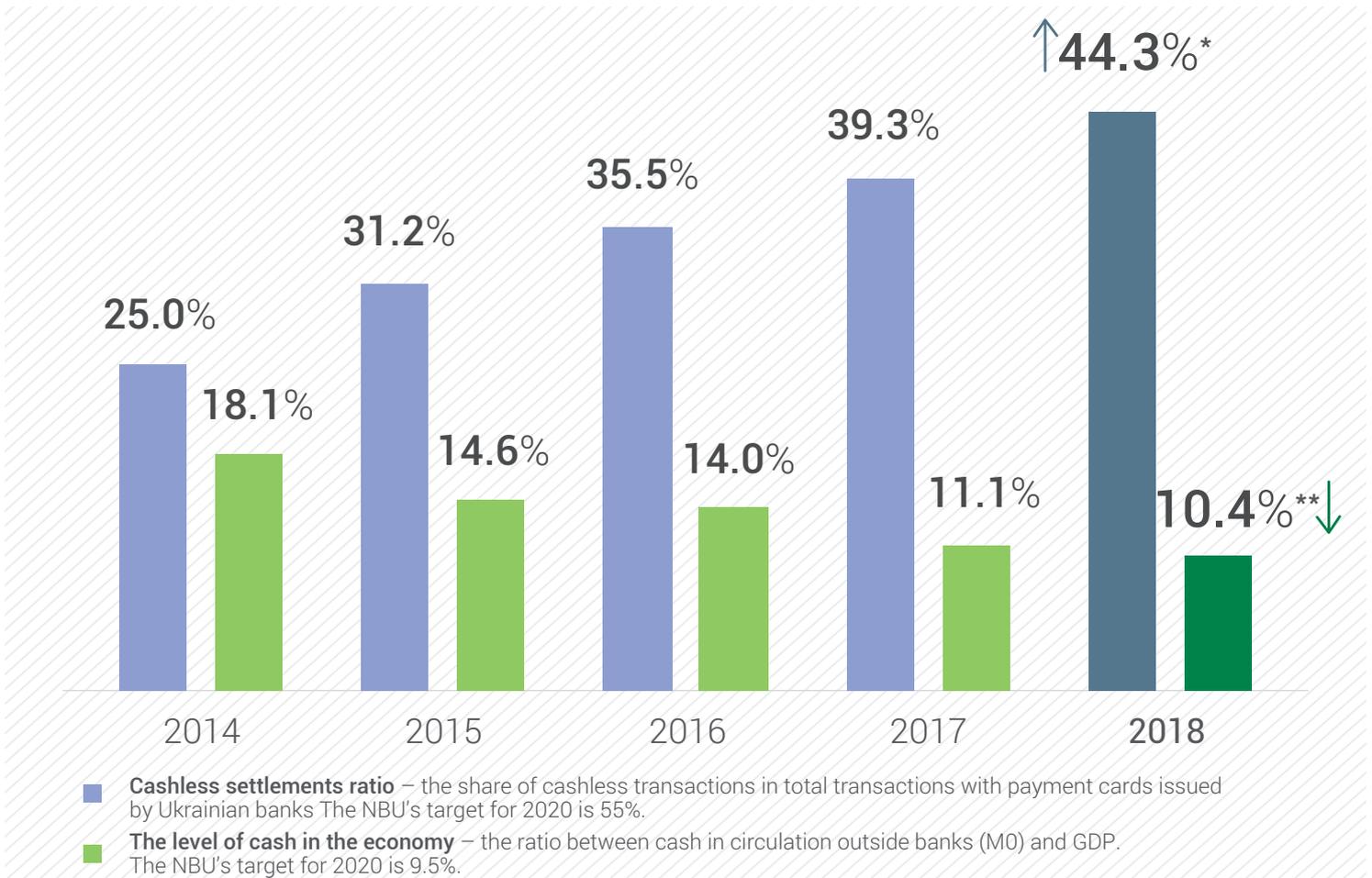
Portfolio of Hryvnia Household Deposits (UAH billion)



2018: the year the NBU spent working to increase public confidence in the banking system

The public does not include sole proprietors.
According to the NBU's monetary statistics. All of the data are as of the end of the period.
Data for 2018: the preliminary refined data will be published on the NBU's website in late January 2019.

Ukrainians are increasingly more inclined to use convenient and secure cashless payments



What Drove the Development of Cashless:



Ukrainians changed their preferences:

more than half (51.7%) of cashless transactions using payment cards take place in the POS terminal network*



the POS terminal network expanded:

Ukraine's POS terminal network has grown 13.6% since the year started*



new technologies and Fintech products arrived:

every 10th payment card in active use and 78.7%*** of POS terminals are contactless

**in the first 9 months of 2018*
***by preliminary estimates*
****as of 1 October 2018*



Adopted Laws:



Establishment and maintenance of the Credit Register



Code of Insolvency Proceedings



Currency and currency transactions



Protection of creditors' and investors' rights



Improvement of the operation of Ukraine's financial sector



Facilitating the inflow of foreign investment



Registered Draft Laws:



Refinement of certain provisions regarding banking supervision, No. 9067



Prevention of and counteraction to legalization (laundering) of proceeds from crime and terrorist financing, No. 9417

Laws necessary to reform the financial sector in 2019



Draft Laws Adopted in the First Reading:



Protection of the rights of financial service consumers, No. 2456-D



The split, No. 2413A



Liberalization of cash settlements, No. 4117



Registered Draft Laws:



Specifics of the conduct of the bank liquidation procedure, No. 6608



Improving the effectiveness of withdrawal of banks from the market, No 6273



Payment systems and the transfer of funds in Ukraine, No. 7270



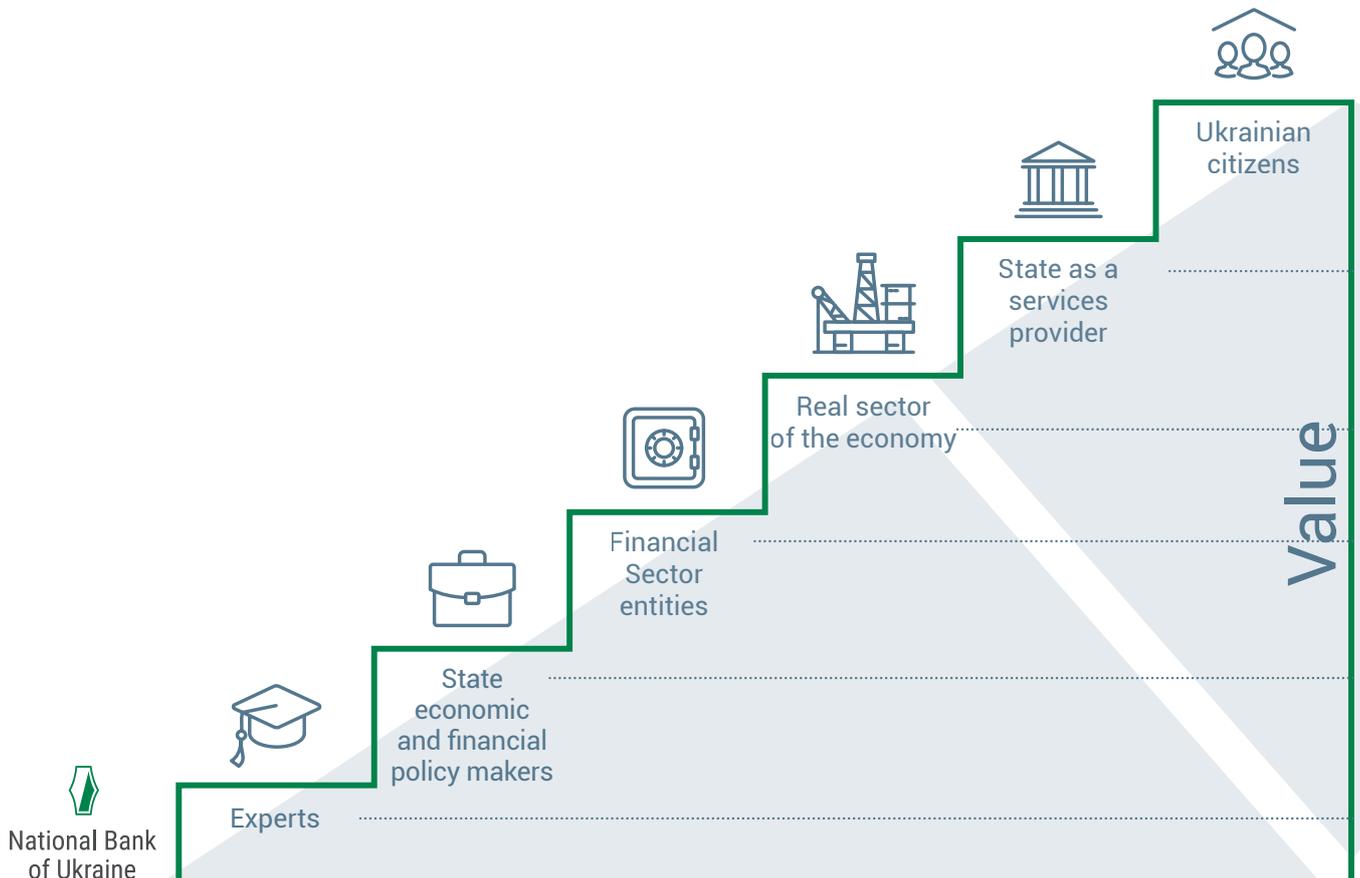
Refinement of certain provisions regarding banking supervision, No. 9067



Prevention of and counteraction to legalization (laundering) of proceeds from crime and terrorist financing, No. 9417

NBU clients

Value can be accumulated and serve as a foundation for creating value for other clients. Citizens of Ukraine receive the maximum value



Experts

make decisions concerning consumption and savings to maximize their welfare



State economic and financial policy makers

ensure the well-being of the country and the free access to public services essential for viable and effective economic activity



Financial sector entities

producing goods and providing services – the driving force of economic development



Real sector of the economy

ensure access to financial services and resources, risk management, safe investment and savings



State as a services provider

creates a robust legal framework for all participants of the financial market



Ukrainian citizens

lay the groundwork for developing adequate regulations