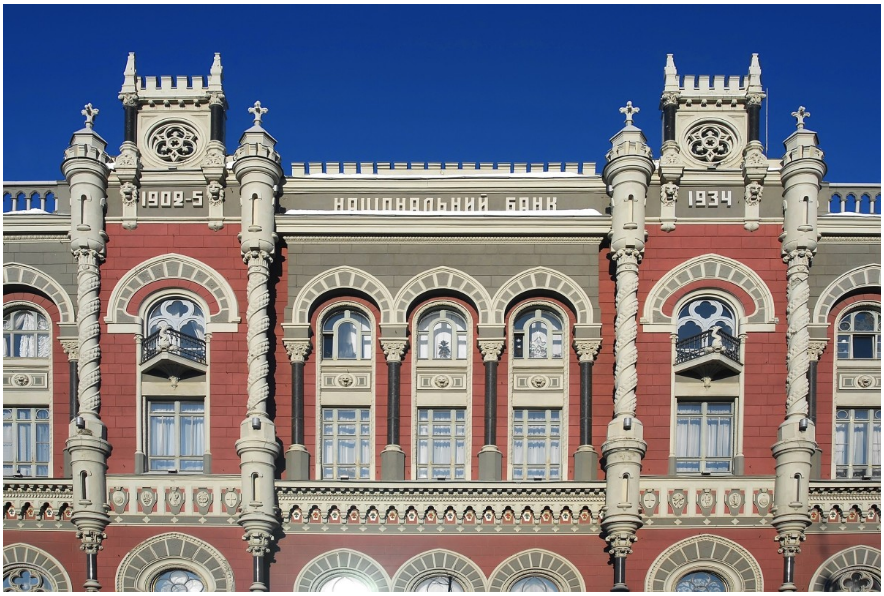
Ukraine: NBU minutes – profiting from the window of opportunity

After surprising the markets with a 200bp cut to 8.00%, the Monetary Policy Committee hints that there is room for more this year. We are revising our year-end key rate forecast to 6.50%



As we have been anticipating – though at a less cautious pace than expected – the National Bank of Ukraine is turning growth supportive. While we still believe that the monetary policy will remain – or turn immediately when needed – FX-centered, the calm waters on the FX front provides a window of opportunity to slash the interest rate. And the NBU is fully taking advantage of it.

Inflation is seen as closing the year within the 5% ± 1 percentage point target range both in 2020 and 2021. The NBU's inflation forecast remains below what the market expects right now. We share the same view and expect inflation to surprise to the downside this year, as plunging domestic demand and energy prices will far offset the weaker hryvnia and some one-off price increases caused by circumstantial stronger demand for essential goods.

On the FX topic, we have entered a period of relative calm, with the seasonal appreciation pattern still at work, largely balanced by the bond redemptions which are partly exchanged into dollars by investors wanting to exit. We maintain our already established view for the hrynia to stay in the 27-28 range this year.

Last but definitely not least, is the long-awaited IMF agreement. As things seem to be unfreezing in the Parliament, we still believe that the IMF Board will approve a deal by the end of May 2020, although it could be June as well. It is worth mentioning that this agreement is likely priced-in to a large extent by the markets and probably by the NBU as well.

Given the background of a more benign inflation outlook and the prospects of a medium-term FX-stabilising IMF agreement, we believe that the NBU will take the opportunity and further slash the key rate beyond its initially indicated 7.00% level by the end of 2020. We are now expecting the key rate to reach 6.50% this year and believe that there is scope for an even lower rate should the FX conditions turn more favourable than we currently expect.

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