Medium-Term State Debt Management Strategy for 2024 - 2026

[October 2023]

Introduction

The Medium-term state debt management strategy for 2024 - 2026 (hereafter referred to as the Strategy) is a tool designed by the Ministry of Finance of Ukraine (hereafter referred to as the MinFin) to assess the current status and dynamics of the state debt of Ukraine and define objectives, targets and tasks over the medium term to optimize state debt structure from a cost/risk perspective while bringing the country on the path to a more sustainable debt trajectory.

The Strategy is being implemented in the context of Russia's unprovoked full-scale military invasion of Ukraine started in 2022. Before the war, Ukraine had achieved a significant reduction in its debt burden since 2015 and a strong macro-economic performance. However, despite showcasing strong resilience, the Ukrainian economy and public finances have been strongly impacted by Russia's war of aggression against Ukraine given the unprecedented nature of the shock. In this context, Ukraine's financial position has been and is still strongly supported by international partners through grants and highly concessional funding.

Over the next twelve months, Ukraine's primary objective is to meet its close its financing gap in order to continue to support the war effort and provide the basis for a rapid reconstruction of the country. To reach this objective, and in view of the high uncertainty stemming from the war, a sound and proactive management of current debt is required as well as reinforcing international partnerships to unlock external financing on appropriately concessional terms to ease the strong pressure exercised on the Ukrainian budget by the Russia's aggression against Ukraine. This financing strategy is consistent with our commitments under the IMF Extended Fund Facility (EFF) arrangement with the aim of safeguarding fiscal and debt sustainability.

After the upcoming State external debt treatment expected in the first semester of 2024, we will next publish a medium-term debt Strategy. Ukrainian authorities committed on March 24, 2023[1] to undertake a debt treatment of Ukraine's external commercial external debt in 2024, with the objective of (i) restoring Ukraine's debt sustainability, (ii) preserving liquidity and reducing Ukraine's financing gap during the IMF programme period, and (iii) creating the necessary conditions for commercial sector participation in the post-war reconstruction of Ukraine, being mindful of the objective to restore Ukraine's market access as early as practicable. Debt treatment with the official bilateral sector is expected to follow a two-step approach, since official creditors have agreed to a standstill over the IMF programme period (2023-2027) and committed to provide additional debt treatment before the final review of the programme.

Over the medium term, Ukraine will continue to implement a financing strategy at the lowest possible cost, while containing risks. In this respect, 3 main objectives for state debt management have been identified:

1. *Attract long-term concessional funding and maximize the share of grants in official sector support*
2. *Maintain strong investor relations and pursue the development of local capital markets*
3. *Contain refinancing risk*

[1] https://mof.gov.ua/en/news/ukrainian_authorities_anticipate_a_commercial_debt_treatment_in_2024-3903

1. Ukraine's state debt snapshot

State debt split by holders as of end of period

	2021		2022		June 2023	
	UAHbn	% of total	UAHbn	% of total	UAHbn	% of total
External debt	**1,300**	**55%**	**2,325**	**63%**	**2,922**	**67%**
IFIs, EU	584	25%	1,254	34%	1,782	41%
Bilateral loans	41	2%	183	5%	250	6%
Commercial banks	51	2%	60	2%	59	1%
Eurobonds holders	625	26%	829	22%	831	19%
Domestic debt	**1,063**	**45%**	**1,390**	**37%**	**1,455**	**33%**
NBU	314	13%	703	19%	690	16%
Domestic government bond holders	529	22%	438	12%	515	12%
State banks, SOEs and DGF[1] (recapitalization)	219	9%	249	7%	249	6%
Total state debt	**2,363**	**100%**	**3,715**	**100%**	**4,376**	**100%**
as % of GDP	***43.3%***		***71.6%***		***67.1%***	
State-guaranteed debt	**309**	**12%**	**360**	**9%**	**334**	**7%**
as % of GDP	***5.7%***		***6.9%***		***5.1%***	
Total public debt	**2,672**	**100%**	**4,075**	**100%**	**4,710**	**100%**
as % of GDP	***49.0%***		***78.5%***		***72.2%***	

Note 1 Such domestic government bonds are recorded at nominal value

State debt split by instruments as of end of period

	2021		2022		June 2023	
	UAHbn	% of total	UAHbn	% of total	UAHbn	% of total
Marketable securities[1]	**1,299**	**55%**	**1,691**	**46%**	**1,772**	**40%**
Domestic government bonds	529	22%	438	12%	515	12%
NBU (CPI & key-policy linked)[2]	145	6%	425	11%	425	10%
Eurobonds	625	26%	829	22%	831	19%
NBU and commercial bank loans	**53**	**2%**	**62**	**2%**	**60**	**1%**
Concessional loans[3]	**624**	**26%**	**1,437**	**39%**	**2,032**	**46%**
IFIs, EU	584	25%	1,254	34%	1,782	41%
Bilateral loans	41	2%	183	5%	250	6%
Other securities	**387**	**16%**	**525**	**14%**	**513**	**12%**
State banks, SOEs and DGF[4] (recapitalization)	219	9%	249	7%	249	6%
NBU (incl. recapitalization)	167	7%	276	7%	263	6%
Total state debt	**2,363**	**100%**	**3,715**	**100%**	**4,376**	**100%**
as % of GDP	***43.3%***		***71.6%***		***67.1%***	
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Note 1 Marketable securities are financial assets generally in bond format which can be easily exchanged (either on a stock market or over-the-counter) and/or which bear interest rates aligned with current market conditions
Note 2 NBU securities are not listed but are issued in bond format and thus defined as marketable securities as per Note 1
Note 3 Concessional loans are defined here as loans with a combination of lower-than-market interest rates, grace periods and/or long-term maturities (the definition retained here is broader than the IMF definition, based on a minimum of 35% grant element using a 5% discount rate)
Note 4 Such domestic government bonds are recorded at nominal value

State debt split by currency as of end of period

	2021	2022	June 2023
	% of total	% of total	% of total
UAH	40%	34%	30%
USD	35%	29%	26%
EUR	14%	23%	29%
GBP	0.02%	0.02%	0.02%
XDR[1]	10%	10%	12%
JPY	1%	1%	1%
CAD	0%	1%	3%
Total state debt	**100%**	**100%**	**100%**

Note 1 Debt denominated in XDR (or SDR) pertains solely to debt owed to the IMF. For reference, the IMF SDR is based on a basket of currencies, which currently consists in 43% of USD, 29% of EUR, 12% of CNY, 8% of JPY and 7% of GBP

State debt split by interest rate type as of end of period

	2021	2022	June 2023
	% of total	% of total	% of total
Fixed	74%	66%	68%
Variable	26%	34%	32%
Total state debt	**100%**	**100%**	**100%**

State domestic debt split by remaining maturity as of end of period

	2021	2022	June 2023
	% of total	% of total	% of total
< 3 years	43%	30%	37%
3-5 years	12%	7%	8%
5-7 years	6%	7%	4%
7-10 years	14%	12%	13%
> 10 years	24%	44%	38%
Total domestic debt	**100%**	**100%**	**100%**

State external debt split by remaining maturity as of end of period

	2021	2022	June 2023
	% of total	% of total	% of total
< 3 years	0%	2%	8%
3-5 years	16%	13%	8%
5-7 years	9%	12%	8%
7-10 years	28%	21%	24%
> 10 years	47%	52%	51%
Total external debt	**100%**	**100%**	**100%**

2. Ukraine's state debt benchmarking

As part of the analysis, a set of 65 peers were selected based on the size of their economies, their macroeconomic and financial performances in recent years, as well as their current trading and credit ratings. From this initial list, a sample of 20 countries was selected as relevant peers for Ukraine. These peers regularly publish comparable and up-to-date data on their state debt, enabling a relevant comparison to be made.

This peer sample was divided into three categories, based on the following classification:

- **Regional peers**: geographical proximity to Ukraine divided into two subgroups depending on their membership in the European Union, as we believe this reflects both the current status of Ukraine as an aspiring EU member, and shows the target debt structure to be reached in the medium term;

- **Rating peers**: similar credit rating before Russia's aggression against Ukraine according to international rating agencies. This category has been removed due to current rating evolutions, but a return to a BB target rating is envisaged in the medium-term, in line with previous MTDS rating set of peers although they would be also amended to include the European Union peers;

- **Trading peers**: countries with comparable current trading levels to Ukraine.

List of selected peers for Ukraine (S&P / Moody's / Fitch: CCC / Ca / CC) by sample

Regional EU-linked peers (6)	Regional Non EU-linked peers (6)	Trading peers (8)
Bulgaria (BBB / Baa1 / BBB)	**Albania** (B+ / B1 / NR)	**Argentina** (CCC- / Ca / CC)
Croatia (BBB+ / Baa2 / BBB+)	**Bosnia and Herzegovina** (B+ / B3 / NR)	**Ecuador** (B- / Caa3 / CCC+)
Cyprus (BBB / Ba1 / BBB)	**Georgia** (BB / Ba2 / BB)	**Egypt** (B / B3 / B)
Czech Republic (AA- / Aa3 / AA-)	**Macedonia** (BB- / NR / BB+)	**Ghana** (SD / Ca / RD)
Hungary (BBB- / Baa2 / BBB)	**Montenegro** (B / B1 / NR)	**Nigeria** (B- / Caa1 / B-)
Poland (A- / A2 / A-)	**Serbia** (BB+ / Ba2 / BB+)	**Pakistan** (CCC+ / Caa3 / CCC)
-	-	**Sri Lanka** (SD / Ca / RD)
-	-	**Turkey** (B / B3 / B)

Sources: Rating agencies
Note As of August 23, 2023

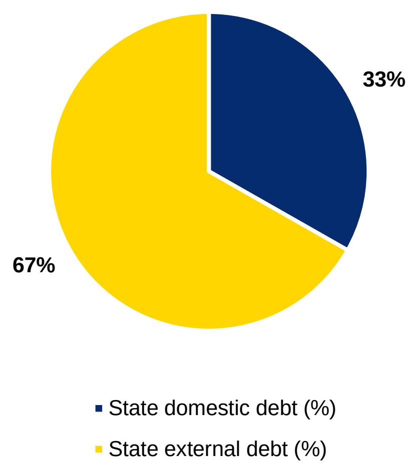
The average indicators for each of the sub-samples were used to benchmark Ukraine's state debt structure within the implemented analysis.

2.1 State debt composition

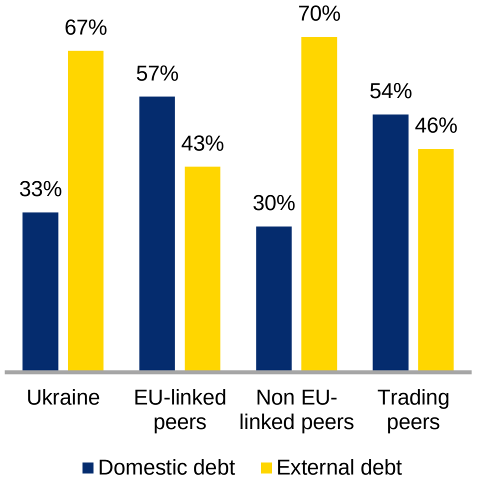
Domestic vs external debt

Ukraine's state debt is characterized by a relatively high share of external debt, accounting for 67% of total state debt.

Ukraine's state debt as of 30/06/2023



Ukraine compared to selected peers (% of total)



Ukraine had been successfully keeping the relatively high share of domestic state debt over the last years having it at the level of 47% as of end-2019, 44% as of end-2020 and 45% as of end-2021. After the beginning of the war (over 2022-2023) Ukraine significantly relied on external concessional financing leading to a decline in the share of domestic debt to 33% as of June 2023.

Nevertheless, Ukraine keeps its focus on the domestic government bond market and further developing it through the expansion of the range of available debt instruments and enhancing state debt management predictability while attraction of foreign investors to the market is currently complicated due to FX regulations but will remain a priority after the liberalization of FX regulations.

A comparison with peer countries illustrates the fact that Ukraine's debt structure targets the aspiration to transition from a debt structure in line with non-EU peers to EU peers. Indeed, non EU-linked peers have a stronger part of external fundings. On the other hand, EU member peers display a more robust domestic debt market. Ukraine will continue to focus on the development of domestic markets and coincide with Ukraine's closer collaboration with the EU.

State debt composition by instruments

As of June 2023, marketable securities constitute 40% of Ukraine's state debt, including 19% of Eurobonds, 12% of domestic government bonds as well as 10% of NBU-owned bonds (CPI & key-policy linked). The share of external marketable securities in total state debt has decreased significantly from 26% as of end-2021 to 19% as of June 2023. "Other" category reflects nonmarket state debt and comprises, in particular, other domestic government bonds issued for the recapitalization of state banks and SOEs. The share of such recapitalization bonds is substantial compared to selected peers, representing one-tenth of Ukraine's total state debt.

The amount due to international financial institutions and foreign countries represents 46% of the total state debt and illustrates their strong support of Ukraine received over the course of the war. The strong and continuous support from IFIs and bilateral partners in the context of the war has decreased the share of marketable debt. This trend goes against our aspiration to increase presence on the markets, while observing a balance with the share of concessional financing obtained from IFIs.

Ukraine's state debt structure as of 30/06/2023

	2021		June 2023	
	UAHbn	% of total	UAHbn	% of total
Marketable securities	**1,154**	**49%**	**1,772**	**40%**
Domestic government bonds	529	22%	515	12%
NBU (CPI & key-policy linked)	145	6%	425	10%
Eurobonds	625	26%	831	19%
NBU and commercial bank loans	**53**	**2%**	**60**	**1%**
Concessional loans	**624**	**26%**	**2,032**	**46%**
IFIs, EU	584	25%	1,782	41%
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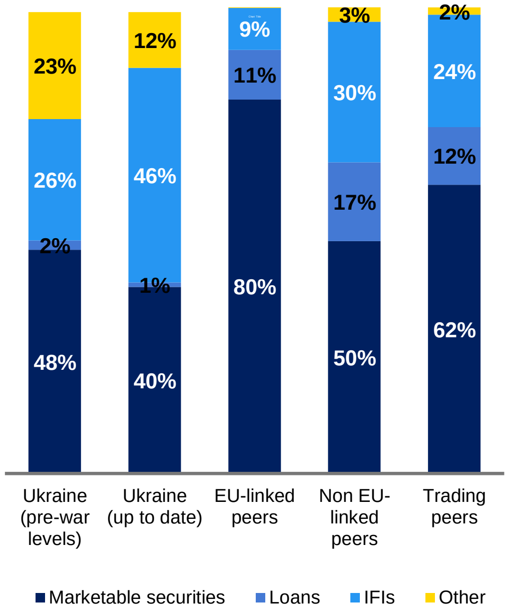
NBU (incl. recapitalization)	167	7%	263	6%
Total state debt	**2,363**	**100%**	**4,376**	**100%**
as % of GDP	***43%***		***67%***	

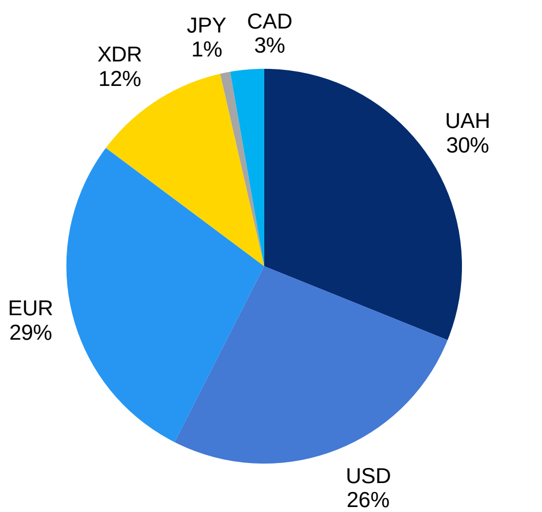
Ukraine compared to selected peers (%)



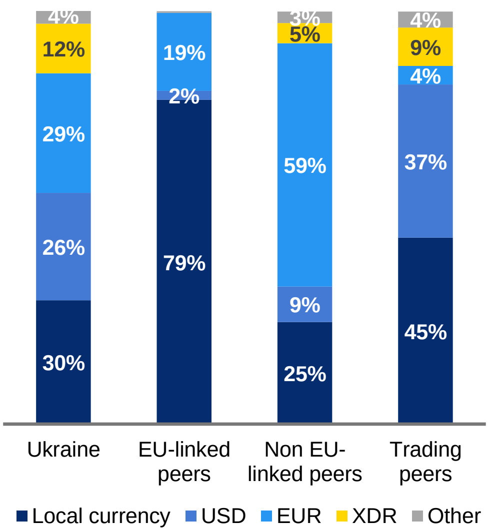
State debt composition by currency

Ukraine's state debt is largely comprised of foreign currency denominated debt accounting for 70% of the state debt as of June 2023. EUR-denominated debt experienced a rapid increase in its share in the state debt from 14% as of end-2021 to 29% as of June-2023 as the result of significant increase of EU's Macro-Financial Assistance (hereafter referred to as the MFA). The second largest category comprises USD-denominated debt mainly composed of USD-denominated Eurobond series. XDR-denominated debt raised as part of financing within the IMF programs represents 12% of Ukraine's state debt as of June 2023. The existence of domestic debt denominated in foreign currency (c.10% of domestic debt and 3% of total state debt) increases the share of total foreign currency denominated debt and, hence, its FX risk.

Ukraine's state debt split by currency as of 30/06/2023



Ukraine compared to selected peers (%)

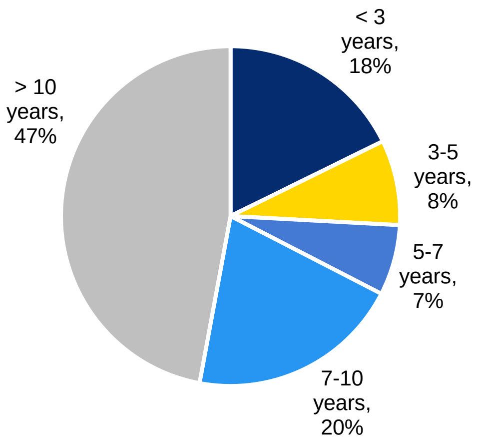


Note: For Eurozone member peers, euro-denominated debt is reported as local currency.

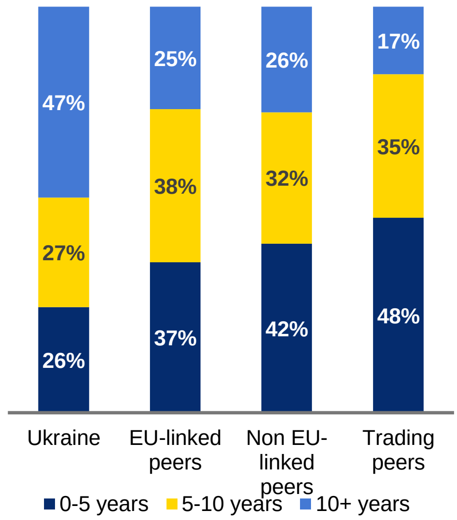
State debt composition by maturity

The largest share is attributed to debt instruments maturing in more than 10 years. As of June 2023, the weighted average term to maturity of Ukraine's domestic debt (including domestic government bonds in the NBU portfolio) amounts to 8.4 years, while state external debt matures on average in 10.1 years (this represents a significant improvement since the end of 2021 when the average maturity of the external debt was 6.3 years). As a consequence, the weighted average time to maturity of Ukraine's total state debt stands at 9.5 years.

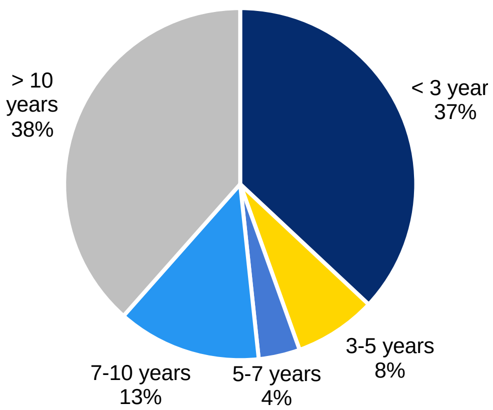
Ukraine's state debt composition by maturity as of 30/06/2023



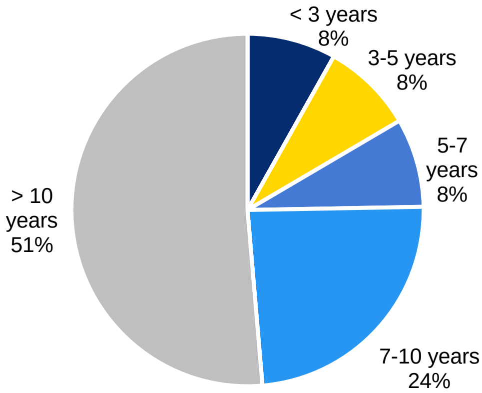
Ukraine compared to selected peers (%)



Ukraine's domestic debt composition by maturity as of 30/06/2023



Ukraine's external debt composition by maturity as of 30/06/2023

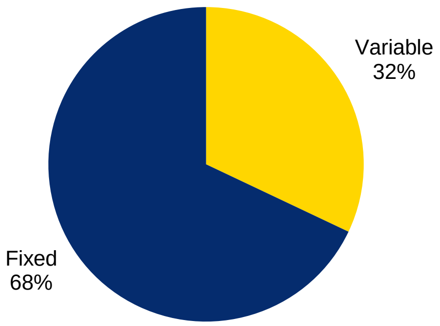


State debt composition by interest rate type

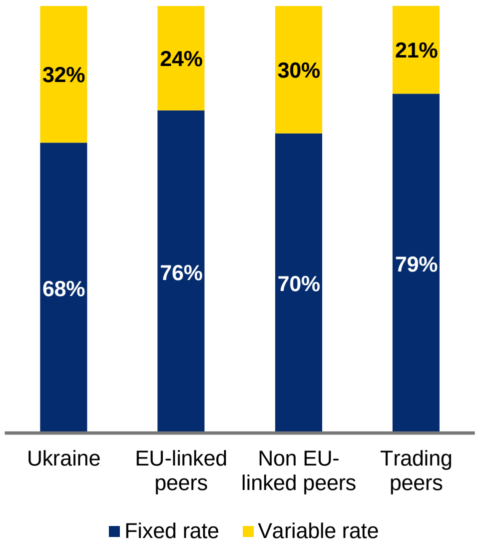
Ukraine's state debt includes a high portion of fixed-rate debt instruments (68%), which keeps its interest rate risk low. Another relevant indicator of exposure to interest-rate risk is the ratio of state debt to be refinanced in one year, leading to interest rates reset, which reaches 44% for total state debt, and 53% for domestic debt

The majority of Ukraine's state debt with variable interest rates is mainly tied to the IMF's Special Drawing Rights (SDR) interest rate, the National Bank of Ukraine's (NBU) key policy rate for domestic bonds held by the NBU, and the Secured Overnight Financing Rate (SOFR), which primarily represents debt owed to the World Bank. Specifically, debt linked to the SDR interest rate makes up 11% of the total state debt, while those tied to the NBU key policy rate and SOFR each constitute 7%. Therefore, such state debt interest payments are sensitive to the increase in interest rates in the Eurozone and the USA**.**

Ukraine's state debt composition by interest rate as of 30/06/2023



Ukraine compared to selected peers (%)



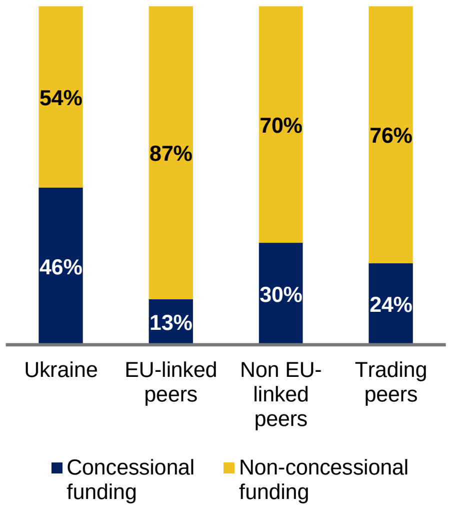
State debt composition by financing terms

The share of concessional instruments in Ukraine's state debt structure accounts for 46%. A significant share of concessional debt in Ukraine's state debt structure reflects a cooperation with the IFIs prior to the war as well as from considerable concessional financing provided on the back of the Russian invasion in 2022. Furthermore, one of the objectives of this Strategy is to increase the amount of financial support by deepening the cooperation with the concessional financing providers such as the EU, the IMF, World Bank, EIB, and EBRD, as well as through the development of new partnerships with foreign countries. Concessional funding represented 25% of total Ukrainian debt before the beginning of the war, while it currently represents 46%.

Ukraine's state debt concessional composition as of 30/06/2023

	June 2023		as % of GDP
	UAHbn	% of total	
Non-concessional funding	**2,345**	**53.6%**	***35.9%***
Concessional funding	**2,032**	**46.4%**	***31.1%***
of which EU (MFA)	824	18.8%	*12.6%*
of which IMF	510	11.6%	*7.8%*
of which World Bank	340	7.8%	*5.2%*
of which bilateral loans	250	5.7%	*3.8%*
of which EIB	100	2.3%	*1.5%*
of which EBRD	8	0.2%	*0.1%*
Total state debt	**4,376**		***67.1%***

Ukraine compared to selected peers (%)

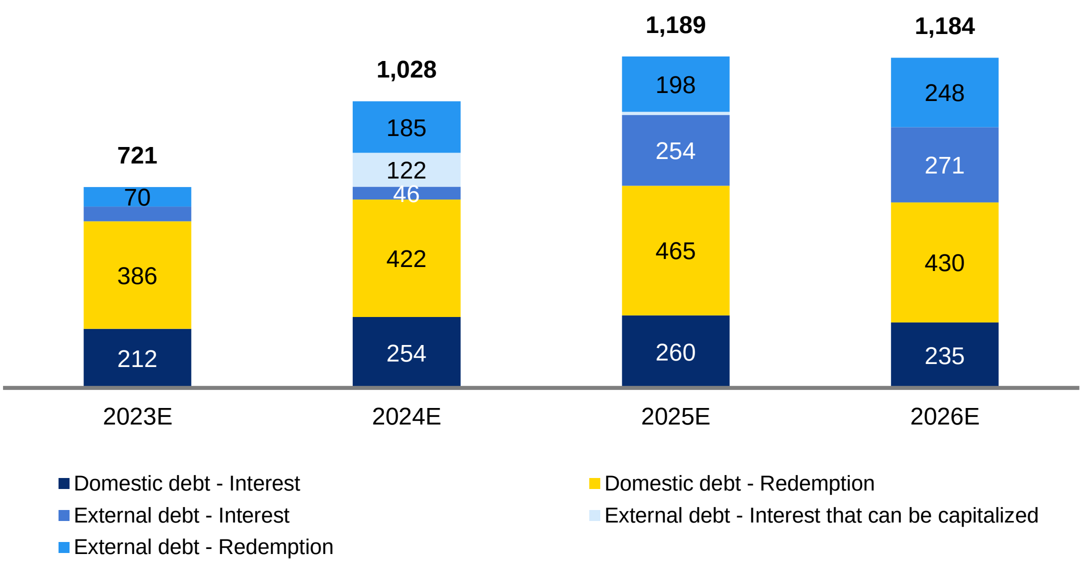


2.2 State debt service

Ukraine's state debt service profile

Ukraine's debt service is frontloaded on the short term with peaks occurring over 2024-26. The result is primarily driven by the significant increase of debt financing needed to finance immense war-caused needs. The average state debt interest and redemption amounts to UAH 1,031bn per annum over 2023 – 2026 (including outstanding and planned debt obligations).

Ukraine's state debt service profile, UAHbn (based on existing debt obligations)[1]



Note: 1. The current debt service profile assumes capitalization as of September 2024 in the principal of coupon amounts deferred as part of the August 2022 debt management transaction. It also reflects the fact that official creditors have agreed to a standstill (i.e. deferral of all principal and interest payments) over the IMF programme period (2023-2027)

Periods of state debt refinancing peaks

State debt interest and redemption in 2023 – 2026 (based on existing debt obligations)

UAH bn	2023	2024	2025	2026
Total	**721**	**1,028**	**1,189**	**1,184**
Average (2023-2026)		**1,031**		
Debt payments / GDP	**11.1%**	**13.4%**	**13.3%**	**11.7%**
Debt payments / State budget revenues	**25.3%**	**32.2%**	**32.4%**	**28.6%**

Sources MinFin, IMF

Smoothing refinancing peaks can be accomplished by (i) attracting concessional loans with long tenors (> 5Y) as well as (ii) performing liability management operations (in addition to the expected upcoming state debt treatment which will enable a reduction in refinancing risk over the short and medium term). Liability management ("LM") operations consist in the proactive refinancing of selected state debt liabilities (domestic or external) prior to their final maturity date, with the objective of smoothening the redemption profile of state debt, reducing refinancing risk, extending its weighted average maturity and/or reducing the average cost of debt.

By way of illustration, Ukraine had conducted such LM operations in 2020 and 2017.

In July 2020, Ukraine executed a switch tender offer targeting its Eurobonds series due 2021 and 2022, and successfully refinanced a notional amount of c.$800m$, financed by the issuance of a new 12-year Eurobond.

In September 2017, Ukraine launched a tender offer on its outstanding Eurobonds series due 2019 and 2020, and refinanced a notional amount of $1.6bn, equivalent to 64% of the 2019 series and 23% of the 2020 series. The operation was financed by a new 15- year Eurobond issuance, thereby significantly reducing refinancing risk. Similar operations will continue to be considered opportunistically by Ukraine going forward.

2.3 State debt cost

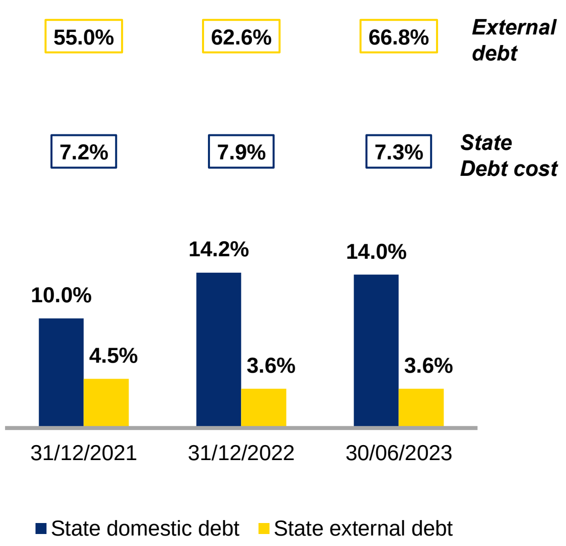
Evolution of Ukraine's state debt interest payments *(based on existing debt obligations)*

	2021	2022	2023
State domestic debt interest payments (in UAH bn equiv.)	**99.5**	**117.9**	**212.0**
USD bn equivalent	3.6	3.6	5.1
% of GDP	1.8%	2.3%	4.1%
% of state budget revenues	7.7%	7.9%	15.2%
State external debt interest payments (in UAH bn equiv.)	**50.6**	**38.6**	**53.3**
USD bn equivalent	1.9	1.2	1.3
% of GDP	0.9%	0.7%	1.0%
% of state budget revenues	3.9%	2.6%	3.8%
Total State budget interest payments (in UAHbn equiv.)	**150.1**	**156.5**	**265.3**
USD bn equivalent	5.5	4.8	6.4
% of GDP	2.7%	3.0%	5.1%
% of state budget revenues	11.6%	10.5%	19.1%

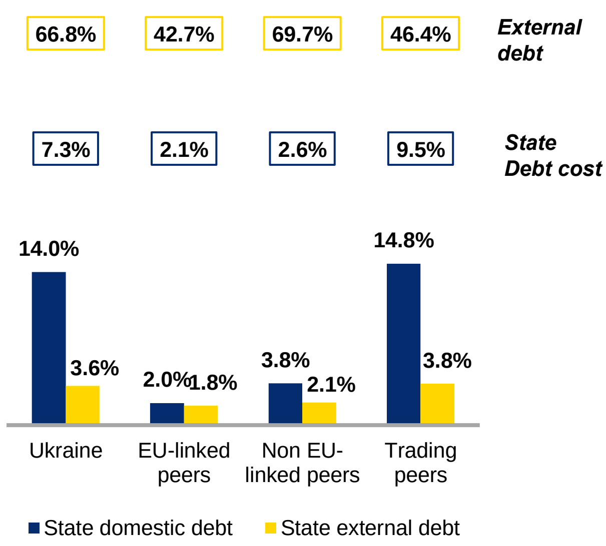
Average state debt cost

Ukraine's weighted average cost of state debt stands at 7.3% as of the end June 2023, which is substantially higher as compared to rating peers (3.6%), but significantly lower than trading peers (9.5%). On the other hand, regional peers demonstrate a meaningfully lower cost of debt – at 2.5% on average. Such cost of debt arises from an average external debt nominal cost of 3.6% and a substantially higher average nominal cost of state domestic debt of 14.0%, which, in turn, results primarily from corresponding inflation levels and NBU's efforts to contain inflation. Despite the ongoing war as well as the increasing inflation pressure worldwide over the recent years, Ukraine's state debt cost increased only by 0.4 p.p. vs pre-war levels. Such dynamics are driven by substantial disbursement of the external concessional loans over 2022-23 with lower-than-market interest rates (c. 2.0% on average), which led to external debt to increase from 55% as of end-2021 to 67% as of June 2023.

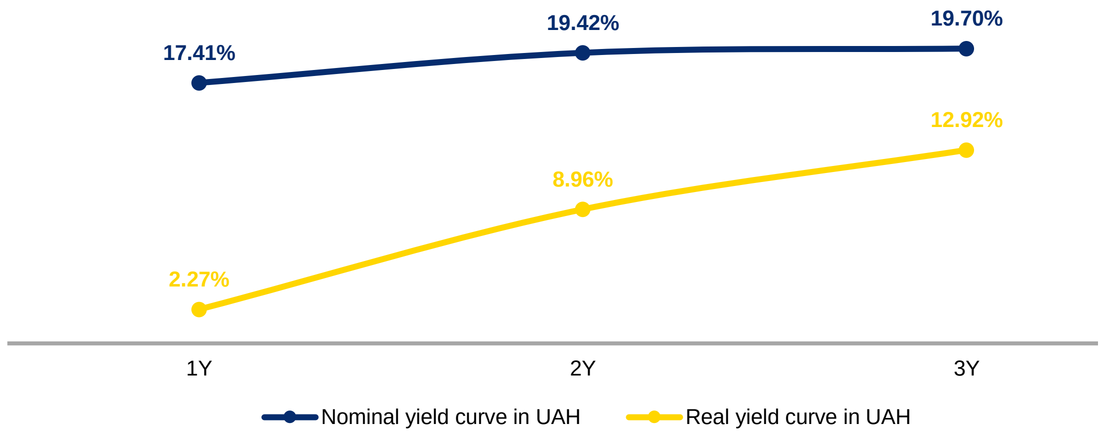
Evolution of Ukraine's weighted average cost of debt (%)



Ukraine's weighted average cost of debt compared to selected peers (%)



Ukraine's UAH-denominated domestic government bonds primary yield curve



Note UAH nominal yield curve is based on the results of primary auctions from July 2022 – to June 2023; real yield curve in UAH is calculated by using NBU CPI forecasts from April 2023 Inflation Report (direct forecasts for the first three years and assumed constant CPI at 5% of the NBU's medium-term target afterwards)

Ukraine's UAH-denominated domestic government bonds real yield curve is upward sloping for the next 3 years, which is among others due to the expected lower inflation in the following years.

2.4 Developments over 2021-2023

Ukraine's credit ratings

Ukraine's current credit ratings

	Standard & Poor's	Fitch	Moody's	Rating and Investment Information (R&I)
Current rating	**CCC / Negative**	**CC / -**	**Ca / Negative**	**CCC / With view to downgrading**
Last rating action	Downgrade to CCC Negative (April 2023)	Rating CC Affirmed (June 2023)	Downgrade to Ca Stable Affirmed (February 2023)	Downgrade to CCC (July 2022)

Note As of 31/07/2023

(1) S&P Global Ratings

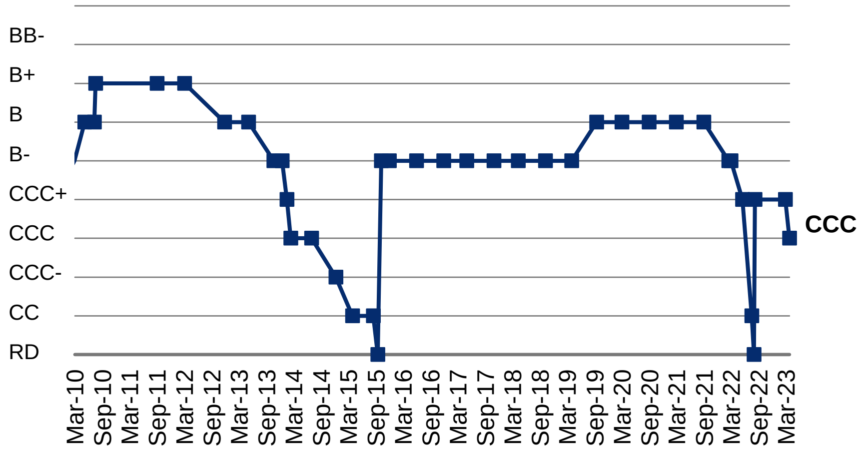
Ukraine's credit rating from S&P is based on the assessment of 5 composing factors, ranked from "1" (highest) to "6" (lowest):

- Institutional assessment with a "5" score
- Economic assessment with a "5" score
- External assessment with a "6" score
- Fiscal assessment with a "6" score
- Monetary assessment with a "6" score

The combination of these factors leads to "B-" indicative long-term foreign currency credit rating. At the same time, S&P assigned "CCC" rating based on "Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings" supported by the following conclusions:

- Medium-term growth prospects remain uncertain and depend on the evolution of military hostilities

- Debt-servicing capacity remains vulnerable and depends on favorable external conditions to meet the financial commitments

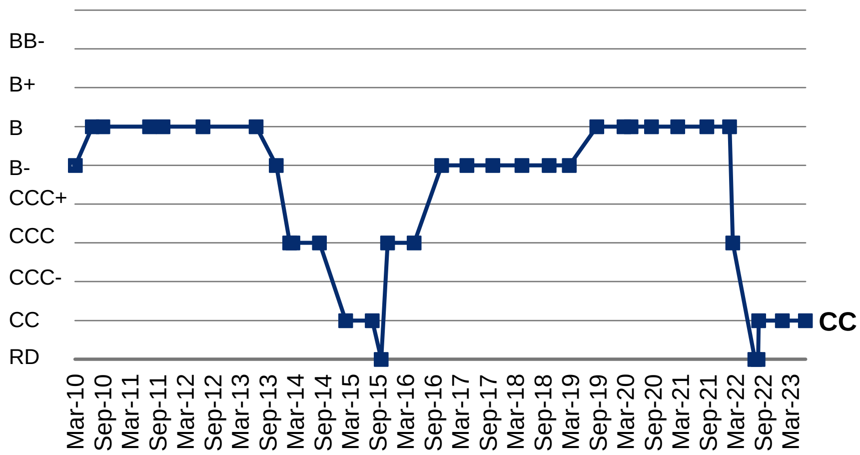


(2) Fitch

Fitch derives Ukraine's credit rating based on the assessment of 18 indicators within the Sovereign Rating Model (SRM) as well as Qualitative Overlays (QO) for each of the category. These indicators are grouped under four categories:

- Structural features
- Macroeconomic performance
- Public finances
- External finances

The SRM output leads to "CCC+" indicative long-term foreign currency credit rating. At the same time, Since March 2022, Fitch did not utilize the SRM and QO to define Ukraine's credit rating because of the ongoing war and the liability management transaction on outstanding Eurobonds in August 2022. "CC" was assigned given the high level of uncertainty surrounding Ukrainian debt.



Cooperation with IFIs and Bilateral partners

Against the backdrop of the Russia's war against Ukraine started in February 2022, concessional funding from international partners has become the key source of Ukraine's budget financing. As of end July 2023, Ukraine has attracted USD 60.2bn in grants and concessional loans / guarantees (incl. USD 32.1bn in 2022).

The provided loans have long tenors (e.g. up to 35Y for the EU's MFA), a grace period of 5 to 10 years as well as concessional interest rates.

As of July 2023, the EU, the USA, the IMF, Canada as well as the World Bank have provided USD 51.8bn (83% of the total). The remaining USD 8.4bn has been covered by EIB, Germany, the UK, Japan as well as 17 other countries.

Canadian Ukraine Sovereignty Bond

In December 2022, Canada agreed to provide a **CAD 500m loan to Ukraine** through a dedicated vehicle. Canada has issued a specific **Ukraine Sovereignty Bond** to raise proceeds to support the general state budget destined to provide essential services to Ukrainians such as pensions, the purchasing of fuel or restoring energy infrastructure. This **5-year vehicle offers a 3.245% rate of return for Canadian investors**.

This bond issuance is entirely guaranteed by the Government of Canada, which will assume the credit risk associated with the loan. Proceeds from the bond issuance were transferred to Ukraine through a specific loan through the IMF Administered Account for Ukraine which aims at coordinating international financial support to Ukraine in a structure reflecting terms of the bond issued by Canada.

Received budget financing since February 2022[2]

US$ m	2022			2023			Total since Feb 2022
	Loans	Grants	Total	Loans	Grants	Total	
EU	7,265	696	7,961	11,428	-	11,428	19,389
USA	-	11,980	11,980	-	8,500	8,500	20,480
IMF	2,693	-	2,693	3,592	-	3,592	6,286
Canada	1,889	-	1,889	1,757	-	1,757	3,645
World Bank	1,385	-	1,385	579	-	579	1,964
EIB	1,720	-	1,720	-	-	-	1,720
Germany	324	1,260	1,584	-	52	52	1,636
UK	949	91	1,040	499	-	499	1,539
Japan	581	-	581	1,496	-	1,496	2,078
France	437	-	437	-	-	-	437
Italy	206	125	330	-	-	-	330
Netherlands	318	-	318	-	-	-	318
Denmark	30	21	51	-	-	-	51
Spain	-	-	-	36	50	86	86
Sweden	49	-	49	-	-	-	49
Lithuania	10	12	22	-	-	-	22
Norway	-	21	21	-	-	-	21
Finland	-	-	-	-	36	36	36
Ireland	-	-	-	-	21	21	21
Latvia	10	5	16	-	-	-	16
Austria	-	11	11	-	-	-	11
Switzerland	-	-	-	-	10	10	10
Belgium	-	5	5	-	3	3	8
Albania	-	1	1	-	-	-	1
Iceland	-	0	0	-	2	2	2
Estonia	-	-	-	-	0.1	0.1	0.1
Total	**17,867**	**14,228**	**32,095**	**19,387**	**8,674**	**28,061**	**60,156**

European Union Macro-Financial Assistance (MFA). Over 2022-2023, the EU disbursed under 3 various MFA programs for Ukraine. The latest and the largest program, MFA+, was signed on January 16, 2023.

It consists of EUR 18bn loan package of highly concessional terms with 35Y tenor (incl. 10Y grace period) and the interest expenses reimbursed by the EU. EUR 3bn have been disbursed immediately after signing while other disbursements are conditioned upon reforms implementation. The disbursement may be possible until March 2024.

Overall, in 2021-2023 more than EUR 16.7bn was disbursed to Ukraine within three MFA programs.

[2] As of 31.07.2023

USA. On April 29, 2022, Ukraine received the first non-repayable USD 0.5bn grant from the USA through the World Bank's Ukraine PEACE Project[3]. To date, overall Ukraine has received USD 20.5bn of grants from the USA, while another USD 3.7bn is yet to be provided in second half of 2023. These funds are used to provide priority social, humanitarian, and healthcare expenses, as well as to support internally displaced persons.

IMF. On March 9, 2022, the IMF approved SDR 1.0bn (c. USD 1.4bn) equivalent to 50% of Ukraine's quota under the Rapid Financing Instrument (RFI). Ukraine canceled the Stand-by Arrangement[4] and expressed intent to work with the IMF to design an appropriate economic program aimed at rehabilitation and growth, when conditions permit. On October 7, 2022, another SDR 1.0bn (c. USD 1.3bn) were disbursed under the RFI Food Shock Window.

On April 8, 2022, the IMF established Multi-Donor Administered Account for Ukraine, aiming to channel donor resources in the form of grants and loans with USD 4.5bn being provided to date.

On November 23, 2022, Ukraine requested a four-month Program Monitoring with Board Involvement (PMB) to anchor macroeconomic policies and prepare to a fully-fledged IMF program. In December 2022, IMF approved the request and in February 2023 completed review of Ukraine under this program.

On March 31, 2023, the IMF approved 48-month Extended Fund Facility (EFF) program of SDR 11.6bn (577% of quota or about USD 15.6bn) and immediately disbursed SDR 2bn (c. USD 2.7bn). On June 29, 2023, following the successful completion of the first review, another SDR 0.7bn (c. USD 0.9bn) has been disbursed.

Canada. Over 2022-2023, Ukraine received USD 3.6bn concessional loans from Canada. USD 3.3bn have been provided in the form of concessional loans with a 10Y tenor and a 4.5Y grace period. The remaining USD 0.4bn has been covered by the Ukraine Sovereignty Bond[5] issuance with 5Y tenor.

World Bank Group: Over 2022-2023, the World Bank disbursed USD 4.6bn for Ukraine under 8 various programs. Against the backdrop of the Russian invasion, the World Bank repurposed funds from programs that were already in place (such as Ukraine Emergency COVID-19 Response and Vaccination Project).

On March 7, 2022, the World Bank approved a supplemental budget support package, called Financing of Recovery from Economic Emergency in Ukraine (FREE Ukraine), providing USD 0.4bn loan and in parallel started developing a dedicated program of supporting Ukraine during wartime.

On June 9, 2022, PEACE[6] program has been signed aiming to support Ukraine's critical budget expenditures (health and social). The World Bank provided USD 1.5bn in 15 different tranches through this program in 10Y and 18Y concessional loans with 4Y grace period.

Moreover, FREE Ukraine, PEACE as well as other programs have become a platform for mobilizing donor support in the form of grants and guarantees. Since February 2022, the World Bank has mobilized more than USD 37.5bn in financial support to Ukraine, of which nearly USD 23bn has been disbursed to date.

European Investment Bank (EIB). Over 2022-2023, EIB provided USD 0.7bn to Ukraine in the form of concessional loans. On March 4, 2022, EIB approved EIB's Ukraine Solidarity Urgent Response EUR 0.7bn package for direct budget support.

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[3] The Public Expenditures for Administrative Capacity Endurance (PEACE) Project helps the Government of Ukraine sustain critical (social, humanitarian, and healthcare) budget expenses. The Project became the platform for accumulating donor funding (grants and guarantees) with c.USD 20bn is being provided as of the end of June 2023.

[4] The Stand-by Arrangement (SBA) provides short-term (12-24 months typically, but not more than 36 month) financial assistance to countries facing balance of payments problems. Ukraine's 14-month SBA was signed in June 2020. In October 2021 it was extended by June 2022.

[5] To offer Canadians an opportunity to directly support Ukraine, the Government of Canada issued a 5Y CAD 500m Ukraine Sovereignty Bond on November 29, 2022. Proceeds from the bond issue were transferred to Ukraine through the IMF Administered Account.

Ukraine major institutional supports

IFI / Bilateral	Amount	Selected program terms
EU	EUR 16.7bn in MFAs (Disbursed in 2020 – 2023)	**<u>Macro-Financial Assistance program + (MFA):</u>** – The agreement signed in January 2023 – Size: EUR 18bn – Total disbursed amount: EUR 9.0bn (5 tranches) – Interest rate: Member States cover the interest costs – Maturity date: till 2053 with 10Y grace period **<u>Exceptional MFA:</u>** – The agreement signed in October 2022 – Size: up to EUR 5bn – Total disbursed amount: EUR 5bn (3 tranches) – Interest rates: 3.375% for the 1st tranche; 3.0% for the 2nd tranche, 2.5% for the 3rd tranche. Member States cover most of the interest costs – Maturity date: till 2042 for the 1st tranche; till 2053 for the 2nd tranche; till 2052 for the 3rd tranche **<u>Exceptional MFA:</u>** – The agreement signed in July 2022 – Size: up to EUR 1bn – Total disbursed amount: EUR 1bn (2 tranches of EUR 500mln) – Interest rate: 1.75% for the 1st tranche; 2.125% for the 2nd tranche. Member States cover most of the interest costs. – Maturity date: till 2034 for the 1st tranche; till 2040 for the 2nd tranche **<u>Emergency MFA:</u>** – The agreement signed in March 2022 – Size: EUR 1.2bn – Total disbursed amount: EUR 1.2bn (2 tranches) – Interest rate: 0.875% for the 1st tranche, 1.0% for the 2nd tranche. – Maturity date: till 2037 for the 1st tranche, till 2032 for the 2nd tranche **<u>Macro-Financial Assistance program (MFA) (Covid-19):</u>** – The agreement signed in July 2020 – Total disbursed amount: EUR 1.2bn (the latest tranche disbursed in October 2021) – Interest rate: 0.125% for the 1st tranche, 0.250% for the 2nd tranche – Maturity date: till 2035 for the 1st tranche; till 2036 for the 2nd tranche
USA	USD 20.5bn (Disbursed in 2022 – 2023)	**<u>Grant budget support:</u>** – Commenced on the backdrop of Russian invasion – Total commitments (2022-23): USD 22.9bn – Provided through the World Bank Trust Fund
IMF	SDR 6.7bn (Disbursed in 2020 – 2023)	**<u>EFF:</u>** – 48-month EFF arrangement approved in March 2023 – Size: SDR 11.6bn – Total disbursed amount: SDR 2.6bn as of June 30th 2023 – Maturity date: till 2037 **<u>RFI:</u>** – Outright purchases under the RFI approved in March and October 2022 – Size: SDR 2.0bn (SDR 1.0 bn each) – Total disbursed amount: SDR 2.0bn – Maturity date: till 2027

		SBA: – 18-month SBA approved in June 2020 (extended to 21 months; cancelled in March 2022) – Total disbursed amount: SDR 2.0bn – Maturity date: till 2026
Canada	USD 3.6bn (disbursed in 2022-2023)	**Concessional loans:** – Total disbursed amount: USD 3.3bn – Interest rate: 1.69% for the 1^{st} and 2^{nd} tranche, 3.245% for the 3^{rd} tranche, 1.5% for the 4^{th} tranche with 4.5Y grace period – Tenor: 10Y with 4.5Y grace period **Ukraine Sovereignty Bond:** – Issued in November 2022 – Total disbursed amount: USD 0.4bn – Interest rate: 3.155% p.a. – Tenor: 5Y
World Bank	USD 4.6bn (disbursed in 2021-2023)	**Public Expenditures for Administrative Capacity Endurance (IDA):** – Total disbursed amount: USD 1.0bn (11 tranches) – Tenor: 10Y with 4Y grace period – Bilateral guarantees **Public Expenditures for Administrative Capacity Endurance (WB):** – Total disbursed amount: USD 0.5bn (4 tranches) – Bilateral guarantees o UK guarantee: USD 450m o Dutch guarantee: USD 21m o Lithuanian guarantee: USD 10m o Latvian guarantee: USD 10m – Tenor: 18Y with 4Y grace period Public Expenditures for Administrative Capacity Endurance (Additional Financings): o Total disbursed amount: USD 1.53 bn o UK guarantee: USD 1.50 bn o Danish guarantee: USD 30m **Emergency in Ukraine – FREE Ukraine:** – Total disbursed amount: USD 0.4bn – WB funds: USD 312m – Bilateral guarantees: o Dutch guarantee: USD 80m o Swedish guarantee: USD 50m **Ukraine Emergency COVID-19 Response and Vaccination Project:** – Total disbursed amount: USD 0.25bn – Tenor: 19Y with 5Y grace period **Other programs:** – Total disbursed amount: USD 0.25bn – Maturity: 2037-2055, grace period by 2024-2026 – Bilateral guarantees: – Spanish guarantee: EUR 43m
EIB	USD 0.7bn (Disbursed in 2022)	**Selected projects:** – Support for SMEs – Support for agriculture sector

Source IFIs, MinFin

2.5 Specific domestic bonds to fund war expenses

To fund the war effort, the Government of Ukraine chose to reinforce its domestic debt market. Ukraine has been issuing wartime bonds regularly since March 2022 in the domestic market in order to ensure the uninterrupted provision of financing for the state's financial needs under martial law. The government is committed to use these proceeds to support military efforts, such as purchasing weapons, ammunition, equipment, food and medicine. For residents, these wartime bonds represent a relevant opportunity to combine support for the defending effort with the search for a profitable investment instrument.

Wartime bonds are essentially denominated in UAH and may be purchased by both residents and non-residents, by both institutional and individual investors. As of the end of June 2023, issuances of wartime bonds attracted UAH 130bn to the state budget.

The latest issuances displayed high yields. In July 2023, Ukraine raised UAH 24.5bn by issuing wartime bonds, out of which UAH 16.2 were local-currency bonds. UAH-bonds yield ranged between 18.0% and 19.2%, depending on the maturity ranging between 10 months and 1.5 years.

2.6 Financing going forward

USA. In August 2023, the White House has asked Congress for an **additional USD 24bn financial aid plan** to reinforce US support to Ukraine, bringing the total aid to USD135bn since the beginning of the war. A such financial support would not be exclusively dedicated to military expenses but also to ease the war's humanitarian impact. This additional aid plan takes place in the context of a long and large-scale conflict which implies a more lasting support.

As of September 2023, USD 24bn of expected aid to Ukraine should be divided into three main categories:

- USD14.1bn will be dedicated to military funding: USD 10.5bn to fund regular governmental operations and USD 3.6bn to strengthen US military production to provide Ukraine with additional Defense capacities.
- USD 6.5bn should be spent on humanitarian aid in order to mitigate war's impact on the Ukrainian population.
- Finally, more than USD 3bn should be engaged to support usual Ukrainian Government's expenses.

If, in this Aid to Ukraine program, not all funds are sent directly to Ukraine, the totality of the USD 24bn are related to the war and aims at supporting country's efforts. Moreover, part of proceeds could be disbursed through international institutions, such as the World Bank and the IMF. Another aid package announcement may be expected by the end of the year.

European Union. The European Commission is going to establish a dedicated instrument to support Ukraine's war and reconstruction efforts and sustain macro-financial stability. This new **Facility to support Ukraine's recovery, reconstruction and modernization** should reach up to **EUR 50bn for the period 2024 to 2027** for both grants and loans. Grants will be mobilized through a new special instrument, proposed in the context of the Multiannual Financial Framework (MFF) mid-term review. The loans will be guaranteed through the headroom[7].

The Facility is based on three pillars, with the detailed breakdown described below:

- <u>Pillar I</u>: The Commission will bring support to the Ukrainian state in the form of grants and loans. This first pillar aims at providing the Ukrainian authorities with a stable and predictable funding, especially in order to sustain the state budget. To benefit from this support, the Government of Ukraine will have to prepare a **Plan for the recovery,**

[7] Difference between the own resources ceiling and the funds that the Commission actually needs to cover the expenses foreseen by the budget.

reconstruction and modernization of the country. This plan should include some structural reforms needed to progress on the path of EU accession.
Totally, through this pillar, the European Union envisages to disburse EUR 6.0bn in grants and EUR 33.0bn in loans, distributed equally each year between 2024 and 2027.

- Pillar II: A specific **Ukraine Investment Framework** will aim at attracting and mobilizing public and private investments in order to support the Plan's implementation.
  This pillar is planned to mobilize EUR 2.0bn in grants each year between 2024 and 2027.
- Pillar III: Technical assistance and other supporting measures will be provided to facilitate the implementation of the Plan, including mobilization of expertise on reforms, support to municipalities, civil society and other forms of bilateral assistance. Traditionally, this type of assistance is only available for pre-accession countries. Interest rate subsidies for the cost of loans will also be covered through this pillar.
  Globally, the European Union envisages to disburse EUR 2.5bn in grants over 2024-2027, of which EUR 0.5bn in administrative support.

3. Ukraine's guidelines for state debt management

3.1 Objective 1. Attract long-term concessional funding and maximize share of grants in official sector support

Ukraine will seek to maintain one of its structural objectives which consists in reducing its average state debt cost. Taking into account the current market conditions, reaching this target implies developing concessional funding, including a high share of grants, to benefit from more favorable financing conditions. Reduction of the weighted average cost of state debt over the medium term will enable Ukraine to improve both fiscal performance and state debt sustainability.

Over the medium-term, the Extended Fund Facility (EFF) program, and the catalytic effect it may entail on other official creditors, will support public finances. It is essential to ensure such multilateral support until the end of the war and during the reconstruction period, especially to mitigate the liquidity risks.

Ukraine benefits from strong support from IFIs and aims **to further expand cooperation with such multilateral institutions and establish bilateral partnerships,** similar to those with Japan, Canada, Germany, and the USA. Much attention will be paid to raising funds from these institutions and from the European Union in order to implement the post-war reconstruction plan. At the end of the current aggression, considerable investment needs will arise, especially to rebuild infrastructure and industrial sectors.

The first pilar of this strategy consists in deepening the cooperation with the IMF, the IBRD, and the EU within structural reforms' implementation in most vulnerable areas of the Ukrainian economy is important both for attracting concessional funding, including from the IBRD and the EU, as well as for strengthening the confidence of foreign investors and a further decrease in the cost of commercial loans.

The second pilar relies on maximizing the share of grants in funding official support. Benefiting from a more important share of grants would be a relevant opportunity to reinforce Ukrainian relationships with multilateral and bilateral stakeholders as the same time as funding post-war reconstruction and investment plan at a limited cost.

3.2 Objective 2. Continue developing strong investor relationships and pursue the deepening of local capital markets

Ensure strong support from international investors

Funding from private commercial investors will remain a key pillar of Ukraine's financing strategy for the reconstruction. In order to ensure sustainable access to international capital markets in the post-war reconstruction, **it is necessary to continue developing systematic and long-term investor relationships**. One of Ukraine's tasks within this Strategy is to expand its investor base in terms of geography and type of investors. As such, the Strategy envisages Ukraine providing investors with regular updates with regard to key macroeconomic and fiscal data.

Ukraine's efforts to develop communication with investors are supported **by regular update and publication of the investor presentation on the MinFin website**, dissemination of monthly outlooks on the essential developments and events in Ukraine, non-deal road shows, as well as by maintaining an official MinFin page on Bloomberg and Reuters terminals.

Ukraine has demonstrated its commitment to maintaining strong relations with the commercial investors community by engaging in active discussions despite the ongoing war. Ukraine will continue to engage in these active discussions in order to (i) provide regular updates on its debt management strategy and macroeconomic developments and (ii) take into account investor feedback with regards to the execution of this debt management strategy.

Interactions with credit rating agencies

Ukraine will actively interact with rating agencies in the following years to further enhance its sovereign credit ratings with an ultimate goal to improve the investment attractiveness of Ukraine's sovereign debt instruments.

Current rating does not reflect the Ukrainian long-term credit quality and we look forward to the restoration of Ukraine's rating in line with the previous MTDS objectives.

Pursue the development of domestic capital markets

As well as reinforcing investor relationships, Ukraine will continue developing its domestic debt market, (i) enhancing relation with resident investors in domestic capital markets, and (ii) by encouraging the return of non-resident investors to domestic bonds market. This will be fostered by continued discussions with international investors regarding their expectations and prerequisites for accessing local capital markets. Increasing the share of debt denominated in local currency debt will allow enhancing Ukrainian financial stability. As such, some other measures may be implemented to reinforce Ukrainian financial stability and thus develop domestic capital markets. Indeed, reforms aiming at increasing banks' reserve requirements on deposits can strengthen domestic financial resources with a focus on local participants. For instance, since January 2023, the NBU has allowed banks to use benchmark domestic government debt securities to meet up to 50% of their total required reserve ratio.

In 2019 Clearstream established a link to the Ukrainian capital market for Ukrainian debt securities, which has greatly facilitated the access of international investors to the local UAH-denominated government bond market. In January 2023, Clearstream announced it was planning to expand its existing link towards additional asset classes, in particular towards reconstruction-related instruments.

Alongside these elements, Ukraine remains committed to addressing the other obstacles that non-resident investors may face when seeking to access domestic capital markets, including with regards to market infrastructure, as well as settlement and clearing procedures.

Rebalancing the composition of the debt in favor of more instruments denominated in local currency would allow containing the exchange rate risk. Indeed, a lower exposure to exchange rate risk allows a reduction the volatility of debt service cost.

3.3 Objective 3. Contain refinancing risk

Manage short-term external debt refinancing risk over 2024-2026

The ongoing Russian war of aggression against Ukraine has put a strong pressure on Ukraine's public finances. Indeed, the damage of several key Ukrainian financial and industrial centers and the flight of several millions people will limit the country's resources for debt servicing. Moreover, the defense effort requires large financial resources.

In this respect, **highly concessional international support is going to be a decisive pillar to manage external public finances over the short-term in order to close the financial gap and limit debt servicing.** This will require continued engagement with the IMF in the context of the Extended Funds Facility (EFF) program over 2023-2027 which has catalyzed over USD 115bn of committed donor support. This will also require negotiating with external commercial creditors in order to achieve debt sustainability as per the IMF DSA's.

Ukraine also has the objective to restore access to capital markets as swiftly as possible, in order to accelerate the recovery of the country.

Ensure continued functioning of the domestic debt market

Developing the domestic debt market is key to reduce Ukrainian financial vulnerability. Despite the Russia's ongoing war against Ukraine, Ukraine has maintained the functioning of the domestic debt market and been able to fully rollover its domestic debt maturities. This has enabled the domestic debt market to play an important role in meeting evolving financing needs through the war while preserving domestic banking sector stability despite the Russia's aggression against Ukraine.

Ensuring functioning of the domestic debt market is all the more key as external financing sources are limited and amid high uncertainty relating to the war. **Building a stronger domestic investors base is a determinant point in this strategy and will coincide with the reconstitution of the productive sector**.

4. Risk factors of Ukraine's state debt

The control over the state debt risks is based on the analysis of refinancing risk, liquidity risk, as well as interest rate, currency, budget and state debt management[8] (contingent liabilities) risks.

4.1 Refinancing risk

State debt maturing in 2023 – 2026

Considering Ukraine's current state debt portfolio, high refinancing peaks are anticipated over the next 4 years. In particular, the state debt payments are frontloaded on a short-term with UAH 1,028bn falling due in 2024 followed by UAH 1,189bn and UAH 1,184bn in 2025 and 2026 respectively. Almost two-thirds of payments are attributable to the domestic government bonds in local and foreign currencies.

This risk can be mitigated owing to the increasing rollover ratio on the domestic government bond market as well as issuing bonds with longer maturities.

- In H1'2023, the rollover ratio of domestic bonds constituted 1.3x (positive net financing of UAH 71.3bn) vs 0.7x over 2022 (negative net financing of UAH 133.2bn).
- Moreover, domestic issuances have shifted towards longer-dated maturities: bonds with 1–3-year maturity constituted 85% of total volume, while in 2022 bonds with up to 1-year maturity prevailed (64% of total volume)

Furthermore, efforts to attract individual retail investors into the government bond market can be continued. For instance, domestic bonds can be conveniently purchased through the Unified State Web Portal of Electronic Services. Such instruments can be available in UAH, USD, and EUR. These bonds offer attractive terms compared with traditional bank deposits, presenting an alternative investment option for individual investors.

Ukraine will remain committed to a proactive debt management strategy which includes the opportunity to consider liability management operations, in particular targeting outstanding Eurobonds.

Average time to maturity of Ukraine's state debt

Weighted average time to maturity of Ukraine's state debt as of 30/06/2023

	years
State debt	**9.5**
State domestic debt	8.4
State external debt	10.1

Ukraine's state debt structure has a balanced average time to maturity. In October 2017, Ukraine has successfully re-profiled its state domestic debt held by the NBU, thus extending the average time to maturity of the domestic debt.

On the external debt market side, Ukraine has continuously lengthened the maturity of its external debt by issuing long-term Eurobonds and attracting concessional funding:

- 10-year EUR 1.25bn Eurobond in January 2020, 12.5-year USD 2.0bn Eurobond in July 2020, and 8-year USD 1.25bn Eurobond in April 2021. In addition, the Ministry of Finance has conducted an active management of its liabilities with a portion of the proceeds from July 2020 issuance used for purchase of Eurobonds due in 2021 and 2022.

[8] According to CMU resolution №815 dated 01/08/2012 state debt management risk includes a risk of an event that can lead to the increase in state (local) budget expenditures related to debt interest and redemption

- Over 2020-2021 Ukraine has signed several programs with the IFIs and the EU. **World Bank**: USD 0.8bn (several programs) with maturity in 2037-2055. **EBRD**: EUR 0.8bn with 15Y tenor. **EU**: EUR 1.2bn COVID MFA with 25Y tenor.

Moreover, the subsequent Russia's war against Ukraine led to increase of average maturity due to the several factors:

- **Domestic market developments.** In 2022, domestic market issuances were successful despite lower volumes[9] and skewed towards short-term instruments (bonds with up to 1 year maturity constituted 64%). From Q4 2022 onwards, the NBU took several steps to increase the attractiveness of domestic bonds by increasing reserve requirements for demand deposits and allowing banks to cover a part of required reserves with benchmark domestic government debt securities. In 2023, the domestic issuances have shifted towards longer-dated maturities, with a notable increase in the 1–3-year maturity period compared to 2022 (85% of total)
- **NBU's financing.** In 2022, NBU has purchased domestic bonds worth UAH 400bn with an average maturity of 16.9 years
- **Long-term concessional loans.** USD 35.6bn of concessional loans provided since February 2022 having long tenor (e.g. up to 35Y for the EU's MFA)

4.2 Liquidity risk

External liquidity indicators

UAH bn	2021	2022	LTM (Jun-23)
International reserves, USDbn	30.9	28.5	39.0
State external debt service, USDbn	5.3	2.6	3.5
Exports, USDbn	81.5	57.0	54.8
Imports, USDbn	84.2	82.7	89.2
International reserves to external debt service	5.8x	10.9x	11.2x
International reserves in months of imports	4.4x	4.1x	5.2x
Exports to external debt service	15.3x	21.8x	15.7x

Sources State Statistics Service of Ukraine, NBU

Following an economic downturn in 2014, Ukraine suffered from a sharp decrease in its international reserves. Owing to the financial support received from the international community as well as the NBU's decision to implement a floating exchange rate regime, the country was able to quickly restore its international reserves, from USD 7.5bn as of the end of 2014 to USD 15.5bn as of the end of 2016 and further boost them up to USD 30.9bn as of end of 2021.

After the Russian invasion in February 2022, the NBU adopted a fixed foreign exchange rate regime to ensure price and financial stability. With a significant decrease in export flows (around 40%) and limited market access due to ongoing war, the NBU had to conduct substantial interventions to uphold the fixed FX rate. To boost international reserves during February-December 2022, the NBU relied on concessional loans and grants from international partners, attracted by the government to cover the financing gap receiving a total of USD 32.1bn.

As of end-June 2023, Ukraine's international reserves amounted to USD 39.0bn, representing 5.2 months of future imports, which indicates considerable progress in rebuilding international reserves from 1.8 months of imports as of end-2014.

[9] UAH 164bn in 2022 vs UAH 288bn in 2021

4.3 Exchange rate risk

UAH correlation with other currencies

The impact of UAH/USD exchange rate fluctuations on the state budget is accentuated by a high degree of correlation with other major currencies in which Ukraine's debt obligations are denominated, thus increasing exchange rate risk of Ukraine's state debt.

Historical correlation between exchange rates of UAH and main currencies of Ukraine's state debt since January 2021

	UAH / USD	UAH / EUR	UAH / XDR	UAH / CAD	UAH / JPY
UAH / USD		*90%*	*98%*	*98%*	*62%*
UAH / EUR	*90%*		*97%*	*91%*	*83%*
UAH / XDR	*98%*	*97%*		*98%*	*74%*
UAH / CAD	*98%*	*91%*	*98%*		*64%*
UAH / JPY	*62%*	*83%*	*74%*	*64%*	

Source NBU

Exchange rate dynamics forecast

On October 2nd 2023, the NBU introduced managed flexibility of the exchange rate to ensure price and financial stability. At the same time, **it aims for the gradual liberalization of administrative restrictions**, which become less effective over time, and **will allow a return to the floating exchange rate as the functioning of the economy normalizes and to support the recovery.**

4.4 Interest rate risk

The average time to re-fix the interest rates for Ukraine's state debt portfolio stands at 5.4 years. Such a figure indicates that a relatively low share of the state debt will be exposed to interest rate risk in the near future. Moreover, the value is higher for the external debt compared to the domestic one due to a larger share of long-term state external debt with fixed rates.

Interest rate risk indicators

	Domestic debt	External debt	Total state debt
Average time to re-fix the interest rates (years)	3.2	8.9	5.4
Debt with interest rates to be refixed in 1 year (% of total)	52.6%	31.6%	44.4%
Service payments with fixed interest rates (% of total)	58.7%	68.6%	62.6%

Note 1 Debt re-fixing in 1 year includes variable-rate debt and fixed-rate debt maturing in 2023

The proportion of Ukraine's state debt with interest rates to be re-fixed in 2023 constitutes 44.4%. In particular, the interest rates are expected to be re-fixed for 52.6% of state domestic debt and 31.6% of state external debt in 2023.

Ukraine aspires to enhance the interest rate structure, i.e. to have a limited share of external debt to be re-fixed in the near-term, thus limiting the interest rate risk. With regard to the domestic market, such figure is in line with the government's expectations on decreasing interest rates as well as with the forecast of decreasing inflation in the medium term.

4.5 Budget risk

In 2020-21 following the government's fiscal consolidation efforts, Ukraine managed to reduce the state budget deficit to GDP ratio from 4.5% in 2020 to 3.5% in 2021.

Against the backdrop of Russia's war against Ukraine in 2022, Ukraine's budget deficit reached 17.9% (vs 27.0% planned initially), supported by higher-than-expected grants from international partners as well as an economic downturn.

In 2023, the budget deficit is expected at 26.4% of GDP driven by higher military expenditures. At the same time, as of June 2023, last-twelve-months budget deficit stood at 15.3% of GDP supported by grants from international partners[10].

At the same time, based on the recently agreed IMF program, the government's key near-term policy measures include the restoration of the pre-war taxation regimes and avoiding measures that would erode the revenue base. Such steps slightly offset the higher-than-expected military expenditures. Shocks to the budget stemming from the ongoing war can present sudden changes to financing needs, and the debt management strategy aims to be sufficiently flexible to meet these needs while preserving fiscal and debt sustainability.

The end of the war will result in an increasing revenue base while also reducing war-related expenditures, leading to a more sustainable budget balance.

4.6 Other risks

Macroeconomic risks and their implications for state debt management strategy

Given the ongoing war, the security situation and the associated uncertainty are the key determinants of Ukraine's macroeconomic risks:

- **Real GDP growth:** the transition of the war into a protracted stage, which will increase (i) human and the economy losses, (ii) destruction of production facilities, and (iii) have negative impact on growth and recovery prospects of Ukraine.
- **Inflation:** the NBU's prudent monetary policy during wartime (key policy rate increase to 25%) already significantly reduced the pace of inflation in Ukraine. However, the risk of rising inflation remains elevated.
- **Balance of payments:** a decrease in the inflow of international financial aid to a level that will not cover the existing BoP deficit will undermine the stability of the foreign exchange market. This may lead to a significant reduction in the FX reserves, hryvnia depreciation and inflationary processes in the economy.

The above-mentioned macroeconomic risks are beyond the control of the MinFin, thus not defining the analysis of Ukraine's state debt management.

State debt management (contingent liabilities) risk

The Ukrainian banking sector is characterized by a relatively large proportion of banks with state participation, representing 55.9% of the sector's total assets as of May 2023. Five banks, partially or wholly owned by the state, constitute contingent liabilities that could materialize in case of banks' failure. PrivatBank, the largest commercial bank in Ukraine, was nationalized on December 19, 2016, following a major capital shortfall, which led to the need for capital injections by issuing domestic government bonds. In addition, contingent liabilities risk also stems from the additional recapitalization of the Deposit Guarantee Fund which may take place in case of commercial banks' bankruptcy.

Additional contingent liabilities risk is stemming from Ukraine's domestic government bonds issued for the recapitalization of state banks and SOEs. These securities are largely FX-linked bonds and represent approximately 7% of Ukraine's total state debt.

Moreover, the state-guaranteed debt contains another risk. As of end-June 2023, state-guaranteed debt stood at USD 9.2bn vs USD 11.3bn as of the end of 2021. The decrease was

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[10] Grants are not accounted in the budget plan and are reflected in the budget performance data only following their disbursement

primarily driven by the repayment of the IMF's loans (USD 2.7bn decrease) by the NBU. At the same time, other categories (such as loans from IFIs and domestic banks) witnessed a USD 0.5bn increase.

State-guaranteed debt (USD bn)

USD bn	Dec-21	Dec-22	Jun-23
Domestic state-guranteed debt	**1.8**	**2.0**	**1.9**
Domestic bonds	0.6	0.3	0.3
Domestic banks or commercial loans	1.2	1.7	1.6
External state-guaranteed debt	**9.5**	**7.9**	**7.3**
IFIs	1.2	1.5	1.7
IMF	5.7	3.8	3.0
Billaterals	0.0	0.0	0.0
Commercial loans	1.1	1.0	1.0
Eurobonds	1.5	1.5	1.5
Total state-guaranteed debt	**11.3**	**9.9**	**9.2**

The general rules for providing state guarantees on the basis of decisions of the Cabinet of Ministers of Ukraine and international treaties are set out in the Budget Code.

Ukraine's state derivatives overview

In accordance with the Ukrainian legislation, state derivatives do not constitute a part of Ukraine's state debt. The IMF and credit rating agencies also do not include state derivatives into state debt, as these instruments do not contribute to current expenses with regards to Ukraine's state debt interest payments.

Ukraine's only state derivatives consist in GDP-Linked warrants, issued in the context of 2015 debt restructuring. These securities have a total nominal amount of USD 3.2bn, but do not have a specific face value at the repayment date. Payouts on these instruments are entirely contingent, and depend on Ukraine's real GDP growth rate from 2019 to 2039 (see below). Payments (if any) are made annually with a lag of two calendar years, namely from 2024 to 2041. Aside from these instruments, Ukraine does not have any other outstanding derivatives.

Payouts under the GDP warrants are computed as follows:

- if real GDP growth is <3% or Ukraine's nominal GDP is less than USD 125.4bn: payment is not made;
- if real GDP growth ranges between 3% and 4%: 15% of the real GDP growth from 3% to 4%;
- if real GDP growth is > 4%: 40% of the real GDP growth exceeding 4%, in addition to the amount for GDP growth from 3 to 4%;
- from 2021 to 2024 payments are limited at 1% of GDP,2025 payment is limited at 0.5% of GDP

In August 2022, Ukraine successfully reprofiled the GDP-linked warrants in the context of broader liability management operation amending the following terms:

- The 2023 payment, linked to 2021 growth rate, was deferred until August 2024 and capitalized at a 7.75% rate in line with the treatment of the external commercial cash bonds
- The cap on the 2025 payment, linked to 2023 growth rate, was lowered from 1% of GDP to 0.5% of GDP
- The Final maturity date was extended from 2040 to 2041
- A call option at par was introduced, which can be activated during a 3-year period starting in June 2024

Although these instruments do not constitute a part of Ukraine's state debt, Ukrainian authorities closely monitor the performance of these instruments and the expected future payouts based on the GDP growth prospects.