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Ukraine 'B-/B' Ratings Remain On CreditWatch Negative

Overview

- Russia's military intervention in Ukraine continues to pose significant risks to the country's economic growth, financial stability, external position, and public finances.
- We expect the government's debt service and borrowing needs will be fully covered by international financial support over at least the next 12 months; its ability to receive such support and make debt service payments, including to nonresidents, remains uninterrupted for now.
- Our 'B-/B' long- and short-term foreign and local currency ratings remain on CreditWatch with negative implications.
- The CreditWatch status indicates that we could lower the ratings if the military conflict were to significantly weaken Ukraine's economy, its external liquidity, its financial system, or the government's administrative capacity.

Rating Action

On March 11, 2022, S&P Global Ratings said its 'B-/B' long- and short-term foreign and local currency sovereign credit ratings on Ukraine remain on CreditWatch with negative implications.

Our 'uaBBB-' national scale rating on Ukraine also remains on CreditWatch negative.

CreditWatch

The CreditWatch negative reflects multiple risks to Ukraine's economy, external balances, public finances, and financial and political stability stemming from Russia's military operations.

We expect to resolve the CreditWatch placement within 90 days. We could lower the ratings should we expect military actions to prevent the authorities from servicing commercial debt. The rating might also come under pressure should the conflict lead to a drain on Ukraine's external liquidity or a rise in fiscal contingent liabilities from its commercial banking system.

Rationale

The ratings on Ukraine are constrained by Russia's military operations within the country, which bring about significant downside risks for the economy and financial sector. We see the potential for governance disruptions, putting commercial debt servicing at risk. The ratings are also constrained by Ukraine's low GDP per capita income and developing institutions.

Despite the conflict, Ukraine is continuing to honor its domestic and foreign debt service obligations and has pledged to continue doing so. On March 1, the Ministry of Finance made a scheduled coupon payment of roughly $290 million on one of its eurobonds. At the same time, strong committed international financial support to Ukraine and still relatively high foreign exchange (FX) reserves support the sovereign ratings.

Ukraine's GDP proved relatively resilient to the COVID-19 pandemic during both 2020 and 2021. However, the ongoing armed conflict with Russia has upended the gradually improving economic outlook. Ukraine now faces disruption to key economic sectors, significant loss of life, and broad damage to essential infrastructure.

The ultimate economic fallout caused by the current events is difficult to quantify, but a double-digit contraction in output for 2022 appears almost inevitable. Economic consequences from the conflict have already started to take hold via the suspension of commercial shipping from ports. This will weigh on Ukraine's export capacity and its ability to benefit from the currently favorable global prices for the country's key exports goods, including metals and wheat.

Output contraction, as well as military and emergency spending needs, will add significant pressures, increasing government financing requirements in 2022 severalfold compared with those expected before the conflict.

At the same time, even these elevated borrowing needs will likely be covered by different types of international financial support. The National Bank of Ukraine (NBU) estimates the overall international financial and humanitarian support committed to date at about $15 billion (some 8.6% of 2021 GDP). This includes international loans, grants, and guarantees, namely:

- A $1 billion guarantee from the U.S. government;
- A €1.2 billion emergency macrofinancial assistance program from the EU;
- A loan for budgetary purposes of up to $500 million from the Canadian government, in addition to a $120 million loan announced on Jan. 21, 2022;
- A $500 million guarantee from the U.K. government to support Ukraine and mitigate the economic effects of the Russian military actions;
- €300 million in financial aid from Germany;
- $100 million in emergency loans from Japan;
- $350 million disbursement from the World Bank to support short- and long-term financing needs.

The above come on top of Ukraine's $5 billion Stand-By Arrangement with the IMF, of which, $2.2 billion remains undisbursed. The IMF program was agreed in June 2020 and extended until end-June 2022. Ukraine has requested emergency financing of $1.4 billion under the IMF's Rapid Financing Instrument. In addition, the National Bank of Poland has offered NBU a currency swap equivalent to $950 million. The recent statements by the international community and international financial institutions suggest that the size of donor support could be further increased. We assume it will at least cover Ukraine's financing requirements in 2022.

Nevertheless, as the conflict continues, Ukraine's technical ability to use international financial support and meet its ongoing debt service obligations could erode.

The NBU has adopted several measures to mitigate exchange rate and financial market volatility as well as the resulting risks to macroeconomic stability stemming from the ongoing military conflict. These measures include the suspension of Ukraine's FX market (except for FX sales by customers), cash withdrawal limits, unlimited unsecured refinancing loans to banks, a moratorium on cross-border financial transactions (excluding those related to debt service), and a fixed hryvnia exchange rate. As of March 2, the NBU had official reserve assets of $27.5 billion. As per international convention, these are kept outside the country, mostly in G-7 counties.

Ahead of the military conflict, we estimated nonperforming loans in the Ukrainian banking system would decline to about 25% by year-end 2022 from 30% at end-2021. However, given the substantial fallout of current events on the private sector, the outlook for asset quality has deteriorated substantially, while confidence could also weigh on banks' liquidity positions. The potential recapitalization needs of Ukraine's state-owned banks will likely put additional pressure on the government's budget.

S&P Global Ratings acknowledges a high degree of uncertainty about the extent, outcome, and consequences of the military conflict between Russia and Ukraine. Irrespective of the duration of military hostilities, sanctions and related political risks are likely to remain in place for some time. Potential effects could include dislocated commodities markets--notably for oil and gas--supply chain disruptions, inflationary pressures, weaker growth, and capital market volatility. As the situation evolves, we will update our assumptions and estimates accordingly. See our macroeconomic and credit updates here: Russia-Ukraine Macro, Market, & Credit Risks. Note that the timing of publication for rating decisions on European issuers is subject to European regulatory requirements.

Key Statistics

Table 1

Ukraine Selected Indicators

	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
MIL. UAH										
ECONOMIC INDICATORS (%)										
Nominal GDP (bil. LC)	2,385	2,984	3,561	3,978	4,194	4,748	4,630	6,440	7,371	8,123
Nominal GDP (bil. $)	93	112	131	154	155	174	125	155	173	187

GDP per capita (000s $)	2.2	2.6	3.1	3.7	3.7	4.2	3.3	3.9	4.3	4.6
Real GDP growth	2.4	2.5	3.4	3.2	(4.0)	3.3	(22)	7.0	5.0	3.0
Real GDP per capita growth	2.8	2.9	3.9	3.8	(3.5)	4.1	(13.3)	0.9	4.0	2.5
Real investment growth	20.4	16.1	16.6	11.7	(24.4)	40.0	(25)	20.0	10.0	5.0
Investment/GDP	21.7	19.9	18.6	14.9	7.5	10.7	3.4	2.5	1.5	0.1
Savings/GDP	19.7	16.9	13.7	12.2	10.9	9.5	(4.2)	(0.2)	(1.1)	(2.5)
Exports/GDP	49.3	48.0	45.2	41.2	39.0	37.8	36.1	38.0	37.4	36.0
Real exports growth	(1.8)	3.8	(1.3)	7.3	(5.6)	4.5	(40)	22.0	10.0	3.5
Unemployment rate	9.7	9.9	9.1	8.6	9.9	9.5	40.0	25.0	20.0	15.0
EXTERNAL INDICATORS (%)										
Current account balance/GDP	(2.0)	(3.1)	(4.9)	(2.7)	3.4	(1.2)	(7.6)	(2.7)	(2.6)	(2.6)

Current account balance/CARs	(3.2)	(5.1)	(8.5)	(4.9)	6.7	(2.0)	(13.4)	(5.0)	(4.8)	(4.9)
CARs/GDP	61.6	60.7	58.1	54.9	50.5	59.6	56.9	54.1	53.7	52.3
Trade balance/GDP	(7.4)	(8.6)	(9.7)	(9.2)	(4.4)	(3.8)	(1.6)	0.3	(0.0)	0.0
Net FDI/GDP	4.2	3.1	3.7	3.4	(0.0)	3.4	(4.5)	2.0	2.0	2.0
Net portfolio equity inflow/GDP	0.2	0.1	(0.0)	0.0	0.1	(0.2)	(1)	0.0	0.0	0.0
Gross external financing needs/CARs plus usable reserves	118.8	115.3	114.8	106.6	94.6	99.9	107.8	106.7	107.0	107.0
Narrow net external debt/CARs	134.8	112.4	96.9	85.3	88.7	70.4	119.2	103.4	96.2	94.6
Narrow net external debt/CAPs	130.6	107.0	89.4	81.4	95.1	69.0	105.2	98.5	91.8	90.2
Net external liabilities/CARs	60.7	47.4	34.8	32.7	24.0	18.7	35.4	35.0	36.3	39.5

Net external liabilities/CAPs	58.8	45.1	32.1	31.2	25.8	18.3	31.2	33.3	34.6	37.6
Short-term external debt by remaining maturity/CARs	42.1	35.7	33.9	27.3	31.0	25.3	40.2	32.9	31.1	30.5
Usable reserves/CAPs (months)	2.6	2.5	2.7	2.7	4.0	3.2	4.5	3.4	3.1	3.0
Usable reserves (mil. $)	15,062	18,252	20,331	24,677	28,368	30,208	24,626	25,149	25,931	27,293
FISCAL INDICATORS (GENERAL GOVERNMENT; %)										
Balance/GDP	(2.2)	(1.4)	(2.1)	(2.1)	(5.7)	(4)	(16.0)	(10)	(6.0)	(4.0)
Change in net debt/GDP	15.3	6.1	1.0	(4.0)	12.6	4.1	36.1	20.0	7.4	5.3
Primary balance/GDP	1.9	2.4	1.2	0.9	(2.7)	(1.0)	(12.7)	(6.2)	(1.4)	0.9
Revenue/GDP	38.5	40.3	39.8	39.4	40.0	38.5	33.0	37.0	38.0	40.0
Expenditures/GDP	40.7	41.7	41.9	41.6	45.6	42.5	49.0	47.0	44.0	44.0

Interest/revenues	10.6	9.3	8.2	7.7	7.3	7.8	9.9	10.2	12.2	12.1
Debt/GDP	81.1	71.8	60.9	50.2	60.8	57.8	95.4	88.6	84.9	82.3
Debt/revenues	210.3	178.1	153.0	127.4	152.2	150.2	289.0	239.5	223.3	205.8
Net debt/GDP	78.7	69.0	58.8	48.6	58.7	55.9	93.4	87.2	83.6	81.2
Liquid assets/GDP	2.3	2.7	2.1	1.6	2.1	1.9	1.9	1.4	1.2	1.1
MONETARY INDICATORS (%)										
CPI growth	13.9	14.4	11.0	7.9	2.7	9.6	25.0	12.0	9.0	7.0
GDP deflator growth	17.1	22.1	15.4	8.2	9.9	9.6	25.0	30.0	9.0	7.0
Exchange rate, year-end (LC/$)	27.30	28.10	27.72	23.81	28.34	27.29	40.93	42.00	43.00	44.00
Banks' claims on resident non-gov't sector growth	(1.6)	1.2	5.4	(9.7)	(3.0)	5.0	(15)	10.0	5.0	5.0
Banks' claims on resident non-gov't sector/GDP	42.8	34.6	30.5	24.7	22.7	21.1	18.4	14.5	13.3	12.7

Foreign currency share of claims by banks on residents	38.9	32.2	30.5	26.3	22.0	18.3	N/A	N/A	N/A	N/A
Foreign currency share of residents' bank deposits	46.3	46.0	42.0	40.0	37.7	32.4	N/A	N/A	N/A	N/A
Real effective exchange rate growth	(0.5)	5.2	6.4	15.2	(0.6)	4.9	N/A	N/A	N/A	N/A

Sources: State Statistics service of Ukraine (economic indicators), National Bank of Ukraine, State Statistics service of Ukraine (external indicators), Ministry of Finance of Ukraine, State Statistics service of Ukraine (fiscal indicators), and National Bank of Ukraine, IMF (monetary indicators).

Adjustments: Usable reserves calculated by subtracting required reserves for resident foreign-currency deposits from reported international reserves. General government expenditures calculated as reported expenditure plus expenditure related to Naftogaz. Government debt calculated as reported state debt plus state guarantees.

Definitions: Savings is defined as investment plus the current account surplus (deficit). Investment is defined as expenditure on capital goods, including plant, equipment, and housing, plus the change in inventories. Banks are other depository corporations other than the central bank, whose liabilities are included in the national definition of broad money. Gross external financing needs are defined as current account payments plus short-term external debt at the end of the prior year plus nonresident deposits at the end of the prior year plus long-term external debt maturing within the year. Narrow net external debt is defined as the stock of foreign and local currency public- and private- sector borrowings from nonresidents minus official reserves minus public-sector liquid claims on nonresidents minus financial-sector loans to, deposits with, or investments in nonresident entities. A negative number indicates net external lending. N/A--Not applicable. UAH--Ukrainian hryvnia. LC--Local currency. CARs--Current account receipts. FDI--Foreign direct investment. CAPs--Current account payments. The data and ratios above result from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information.

Ratings Score Snapshot

Table 2

Ratings Score Snapshot

KEY RATING FACTORS	SCORE	EXPLANATION
Institutional assessment	5	Reduced predictability of future policy responses because of moderate risk of challenges to political institutions. Relatively weak transparency and uncertain checks and balances between institutions.
Economic assessment	5	Based on GDP per capita ($) as per Selected Indicators in Table 1.
External assessment	5	Based on narrow net external debt and gross external financing needs as per Selected Indicators in Table 1.
		There is a risk of marked deterioration in the cost of or access to external financing.

Fiscal assessment: flexibility and performance	6	Based on the change in net general government debt (% of GDP) as per Selected Indicators in Table 1.
		The ability of the government to raise taxes has weakened due to economic disruptions caused by the military conflict.
Fiscal assessment: debt burden	6	Based on net general government debt (% of GDP) and general government interest expenditure (% of general government revenue) as per Selected Indicators in Table 1.
		About 60% of government debt is denominated in foreign currency.
		The banking sector's exposure to the government is about 28% of its assets.
Monetary assessment	5	The hryvnia generally floats freely with intermittent interventions from the National Bank of Ukraine.
		The transmission mechanism is weak, as demonstrated by still-weak real credit growth.
		The central bank has imposed capital and exchange controls to mitigate the financial market fallout from the conflict.
Indicative rating	b-	As per Table 1 of "Sovereign Rating Methodology."

Notches of supplemental adjustments and flexibility	0	
Foreign currency	B-	
Notches of uplift	0	Default risks do not apply differently to foreign- and local-currency debt.
Local currency	B-	

S&P Global Ratings' analysis of sovereign creditworthiness rests on its assessment and scoring of five key rating factors: (i) institutional assessment; (ii) economic assessment; (iii) external assessment; (iv) the average of fiscal flexibility and performance, and debt burden; and (v) monetary assessment. Each of the factors is assessed on a continuum spanning from 1 (strongest) to 6 (weakest). S&P Global Ratings' "Sovereign Rating Methodology," published on Dec. 18, 2017, details how we derive and combine the scores and then derive the sovereign foreign currency rating. In accordance with S&P Global Ratings' sovereign ratings methodology, a change in score does not in all cases lead to a change in the rating, nor is a change in the rating necessarily predicated on changes in one or more of the scores. In determining the final rating the committee can make use of the flexibility afforded by §15 and §§126-128 of the rating methodology.

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018

- Criteria | Governments | Sovereigns: Sovereign Rating Methodology, Dec. 18, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Methodology: Criteria For Determining Transfer And Convertibility Assessments, May 18, 2009

Related Research

- Russia-Ukraine Military Conflict: Key Takeaways From Our Articles, March 8, 2022
- Sovereign Ratings Score Snapshot, March 8, 2022
- Sovereign Ratings List, March 3, 2022
- Sovereign Ratings History, March 3, 2022
- Cyber Threat Brief: How Worried Should We Be About Cyber Attacks On Ukraine? Feb. 22, 2022
- Sovereign Risk Indicators, Dec. 13, 2022; a free interactive version is available at http://www.spratings.com/sri
- Default, Transition, and Recovery: 2020 Annual Sovereign Default And Rating Transition Study, April 12, 2021

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee's assessment of the key rating factors is reflected in the Ratings Score Snapshot above.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria And Research').

Ratings List

RATINGS REMAIN ON CREDITWATCH	
UKRAINE	
Sovereign Credit Rating	B-/Watch Neg/B
Ukraine National Scale	uaBBB-/Watch Neg/--
Transfer & Convertibility Assessment	B-
Senior Unsecured	B-/Watch Neg
Senior Unsecured	D
STATE ROAD AGENCY OF UKRAINE (UKRAVTODOR)	
Senior Unsecured	B-/Watch Neg

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P

Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; or Stockholm (46) 8-440-5914

Regulatory Disclosures For Each Credit Rating Including Ratings List Table

Disclosures include requirements relating to press releases or reports published in accordance with Article 10(1), 10(2), and 10(5), and Annex I, Section D, I, 1, 2, 2a, 4, and 5. These requirements are available by rating via the link titled "Regulatory Disclosure" and include, but are not limited to:

- Key Elements Underlying The Credit Rating
- ESG Credit Factors
- Solicited Or Unsolicited Status
- Analysts Primarily Responsible For The Credit Rating
- Office Responsible For The Credit Rating
- Materials Used In The Credit Rating Process
- Criteria Applied
- Models Applied, Loss, And Cash Flow Analysis Performed
- Scenario Analysis
- Sensitivity Analysis
- Risk Warning, Understanding Credit Rating Categorizations, And Criteria
- Rated Entity Notification
- Ancillary And Additional Services
- Attributes And Limitations Of The Credit Rating
- Information Specific To Structured Finance And Securitization Instruments

Contact the analysts:

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