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Ukrainian banking system shows signs of improvement

- NBU's regulations on banking system liquidity to contain inflation and the recent downward pressures on hryvnia
- Lending activity continues to recover driven by corporate lending while household loans still contract, albeit at a slower pace

NBU's regulations on banking system liquidity to contain inflation and the recent downward pressures on hryvnia

In line with the IMF recommendation, the National Bank of Ukraine (NBU) at the end of May liberalized the FX market, allowing banks to carry out swaps and forward FX operations as well as forward contracts, despite breaches in their FX position limits. What's more, intraday buying and selling foreign currency by banks were allowed (until then banks could only buy or sell in a day), as well as unlimited FX operations between banks and households. Consequently, banks have started more aggressively buying dollars and increasing their long-term foreign currency positions. As a result of the stronger demand for dollars, pressures on hryvnia intensified and forced the NBU to spend an estimated \$1.2bn of reserves in June on intervention to protect exchange rate stability. In late June, the NBU response to Ukrainian banks' speculative appetite was to cut the limit for open foreign currency positions from 20% of capital previously to 5% and switched to daily reporting from monthly. This measure came into effect on June 29, 2011 and provided banks with 30 days to adjust their position. Moreover, the NBU also announced monetary policy tightening, through deposit rates and reserve requirements hikes, which is estimated to remove over UAH 3bn in liquidity. This aimed to contain inflation as well as the recent downward pressures on domestic currency.

Lending activity continues to recover driven by corporate lending while household loans still contract, albeit at a slower pace

Total credit growth continues to recover driven by loans to corporates while household lending is still in the red. Namely, total credit grew by 9.1% yoy in May (up from 8.0% yoy a month earlier) and 4.7% year-to-May; corporate lending stood at 16.9% yoy (up from 15.7% yoy in April) and 7.2% year-to-May while household loans continued to contract, albeit at an increasingly slower pace 7.1% yoy in May and -0.7% year-to-May (vs. 8.2% yoy contraction in April and 9.5% yoy recorded in the prior month). On the deposits front, the first notable decline in total deposits posted in May, by -0.5% mom (down from +2.6% mom in April) driven mainly by corporates' deposits decline by -2.4% mom (down from +5.1% a month earlier). Nevertheless, total deposits grew by 8.6% year-to-May while corporates' deposits increased by 9.5% year-to-May.

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