

Fireside Friday with... Clearstream's Jan Willems

Early this year, Clearstream announced plans to expand its existing link to the Ukrainian capital market with additional asset classes. Global Custodian speaks to Jan Willems, head of product management, global markets at Clearstream about the ICSD's experience in Ukraine over the past few years.



Clearstream began offering a service in Ukraine in 2019, is that right?

Yes, but we were active in the region long before that. Together with Euroclear, we began working on ICSD access to Russia as of 2004, 2005 on the loan process that culminated in 2012 with the opening of the Russian bond market. After this we wanted to further expand our footprint in the region.

At that stage, the markets concerned were developing with limited market infrastructure. They all had their own challenges when it came to KYC, AML and so on. As of 2016, we started our offering and broader strategy with Armenia and Georgia. Although they were relatively small markets, we developed an interesting dynamic with the local central banks and Ministries of Finance.

Usually, as an ICSD, we like to come into a market with a comprehensive offering, covering all asset classes and all services. In those two cases, we decided with the local stakeholders to focus on one asset: local currency-denominated government bonds. We'd also learned from experience that when the investment community enters a market, the first exposure they take is on local "govvies", government bonds. They're not going to start with local corporate bonds or local equities.

Local 'govvies' we know are simple and, in most emerging

markets, free of tax. There's no really complex asset servicing. We went live with Georgia and Armenia and that was an instant success. Volumes at start were not huge, because the markets themselves were small, but we managed to create something there; as soon as the markets were connected to Clearstream, conversations with large buy-side communities became easier. It was a bit of a chicken and egg story.

We then tackled a bigger market, which was Kazakhstan, where volumes were bigger. We did that in 2018, and again it was an immediate success. Today we have a very healthy franchise in Kazakhstan.

Ukraine as a market was an interesting one because it already had several links into Europe with a good presence of European banks locally that could help us out.

Together with our local partners, the Ministry of Finance and the

National Bank, we built a post-trade infrastructure that's suitable for non-resident investors. Bear in mind that after Maidan in 2014, Ukraine was in the position to substantially grow their economy. There was already quite a lot of foreign direct investment flowing into the country; it was seen as an agricultural powerhouse, with commodities and IT also attracting interest.

We launched our service in Ukraine in 2019 and it also became an instant success. We were able, thanks to the link, to increase levels of non-resident investment well above the equivalent of US\$3 billion in a couple of months.

With more investors coming in, you have yield compression; you start to create a secondary market on those bonds in Clearstream and all of a sudden it becomes easier for the Ukrainians to start talking with large index providers, the likes of MSCI and the JP Morgan

Global Government bond Index.

All the big household names started to use Clearstream for the Ukraine connection.

Didn't Covid get in the way?

We went through Covid, which didn't have a major impact on volumes. Of course, there's the usual emerging markets volatility to contend with and, sometimes, US dollar risk. When US dollar interest rates go up, money flows out and when interest rates go down, money flows in. We saw the usual pattern of an emerging market.

But then came the rising tension around the military build-up on the Russia-Ukraine border in 2021 and early 2022. Like a large majority of Western Europe, we didn't have a catastrophic scenario in mind with a true invasion, but that's what we had last February.

The post-trade industry has gone through crises before: Argentina, Asian debt prices, and Greece, to name three, but these were all financial crises. We'd never been faced with a situation where we were active in a country where, all of a sudden, we didn't know if we'd be able to reach our local provider, in that case, Citibank Ukraine or the National Bank of Ukraine, our place of custody.

As it happened, we always remained operational in Ukraine. Not once did we have to go back to our clients and say, "We don't know what's going on," or "We cannot guarantee the continuation of our activities."

Many things locally were already done in the cloud. So basically, you saw the whole capital market moving across and remaining completely functional. Thanks to Covid, of course, a lot of the remote tools were there and could be replicated, albeit in more dramatic circumstances.

What was happening to cross-border volumes over that period?

For a couple of weeks, the government stopped the auctions and the local secondary markets. Within Clearstream, transactions could always take place, but it was not possible for clients to sell their positions to local banks in Ukraine. Little by little, the central bank reintroduced the possibility to interact with non-residents. First, we had the auctions of the so-called war bonds, perhaps an unfortunate name, because when you try to reach out to institutional investors, it sets off a lot of ESG alarm bells, but basically those war bonds were standard Ministry of Finance instruments meant to add to the overall budget. Three or four months after the start of the war, these war bonds were launched and could be settled in Clearstream.

On those instruments, our clients could again start doing cross-border transactions with local Ukrainian counterparts. Then during the summer of last year, the entire bond market was reopened and gradually we went back to business as usual. The only restrictions at a certain moment were FX restrictions on income. It took a while before the FX market was reopened on the 1st of April of this year.

Even today, the transaction volumes are more intense than before the war. The investors are there, the auctions take place every week. They're pretty successful and a lot of non-resident investors participate. You're starting to see investors that are looking beyond the war and just want to take positions today



in hryvna bonds.

So as far as govies are concerned, it's nearly, from an operational point of view, business as usual. We went through all the scares when Kyiv was attacked and they were targeting the electricity facilities; we learned a lot about how much diesel you need to have available for your generators and how many generators you need, but it has been amazing that all the banks have been operational throughout. We had zero seconds of outage even during the worst situations around November, December, January of this year. It is really a credit to the guys over there that they managed to keep it afloat and recognised the importance of keeping financial market infrastructures open. There was never any panic. That was thanks to the dedication of their people in the most stressful conditions imaginable and done with great professionalism. This will pay dividends as we enter the period of reconstruction by guaranteeing a path for both private and public external investment.

Now moving forward, there's a lot of money that is earmarked for reconstruction from the likes of the EBRD, EIB and World Bank among others. There are various initiatives. We want to make sure through the connectivity we already have in Ukraine that whatever securitised reconstruction products come on the market, those instruments can be settled and safekept on our platform.

Operationally, from Clearstream's point of view, is there anything that you've had to do that you wouldn't have to do in

the other markets in the region?

It's really the same template. We focused in the initial stages only on government bonds, thereby avoiding certain challenges such as companies that go bust or tax issues. A govvie is a govvie. It's a very simple instrument. We have our custody with the National Bank of Ukraine, which is the safest possible environment.

Also, having had that flexibility from the National Bank before the war to have our own safekeeping account at the National Bank, we were able to provide that additional level of confidence. Big credit is also due to our local partner, Citibank. They operate our accounts in Ukraine because they have people on the ground and the triangle of National Bank, Citibank Ukraine and Clearstream has been super-solid.

It's a market where everyone knows each other and where literally you have all your partners on speed dial on the mobile. Whether it's a Sunday morning or a Friday evening, you'll always find someone to help you out there during those exceptional circumstances.