

Weekly Digest

- New PM vowed cooperation with the IMF, as the parliament fired prosecutor general Ryaboshapka
- Consumer inflation in February amounted to -0.3% MoM and 2.4% YoY
- Ukraine's foreign currency reserves increased over February by \$0.3bln to \$26.6bln
- Metinvest's EBITDA in December dropped by \$57mln MoM to -\$61mln

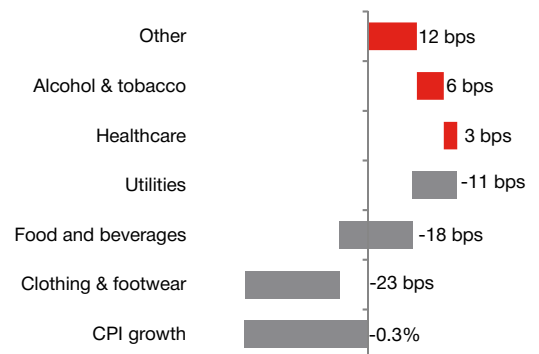
New PM vowed cooperation with the IMF, as the parliament fired prosecutor general Ryaboshapka. The latter was supported by ambassadors of G7 countries and local anti-corruption activists, which called the move a "huge roll-back". On March 4 PM Smyhal held an official meeting with the IMF office in Kyiv, which was followed up by a statement claiming commitment to continue with Fund's \$5.5bln program. Talks may continue in Washington in the coming weeks.

Our view: Ukraine's authorities delivered a set of conflicting moves over the week, which, in combination with the global selloff, sent sovereign bonds into a downward spiral. That said, official commitment to stay on track with the IMF program, despite Shmyhal and Umansky (the new FinMin head) previously voicing contrarian personal views in the media, gives hope that some of the damage from firing a reform-oriented government may be contained, as long as top-line goals are unaffected.

Consumer inflation in February amounted to -0.3% MoM and 2.4% YoY. Key categories contributing to the drop in the CPI relative to January were clothing & footwear (impact of -23 bps), food (-18 bps), and utilities (-11 bps). Prices growth was recorded in healthcare, alcohol & tobacco, and a few smaller items (+21 bps in total).

Our view: Headline CPI trailed our projections once again (at 3.0% in annual terms) due to unexpectedly strong food deflation, which occurred despite a 4% hryvnia devaluation during the first two months of the year. A contraction in meat prices by 1.3% MoM was a key surprise, though eggs also demonstrated a very unseasonal adjustment (-17.6% MoM vs -6.6% on average since 2010 and -4.6% last February). A portion of the correction can be explained by global trends as the FAO index also contracted by 1.0% MoM. Looking ahead towards March, we identify two conflicting forces at play – a further drop in commodity prices (including grains and vegetable oil) on the back of a major financial market selloff and a weakening exchange rate (already slipped by 1.8% since March 1). So far, we expect both drivers to be of similar magnitude, which suggest an overall neutral impact and thus flat inflation at 2.4% YoY. Despite an outlook which places the CPI below the NBU's official target, we anticipate no changes in the regulator's monetary policy on March 12. Global economic uncertainty and local political risks sparked by the recent government reshuffle are likely to take center stage in the upcoming announcement. In this light, we also increase our end-of-year key rate projection by 200bps to 9.0%.

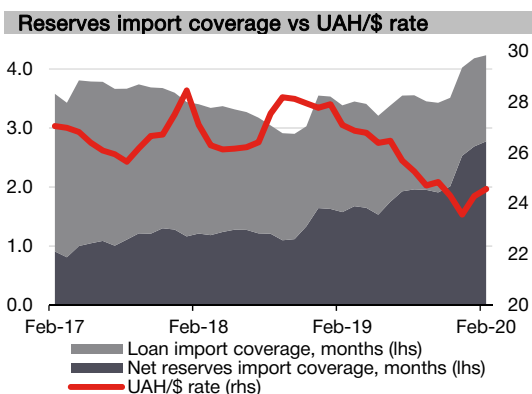
MoM CPI growth contributions by category



Source: SSSU, Adamant Capital estimates

Ukraine's foreign currency reserves increased over February by \$0.3bln to \$26.6bln. Outflows came primarily on the back of debt servicing and amortizations of \$0.8bln. Inflows resulted mostly from the NBU's net purchases on the interbank market totaling \$0.7bln and from \$0.2bln worth of local bond placements by the FinMin. An extra \$0.2bln was generated by the price appreciation of assets, in which reserves are invested.

Our view: February reserves came in somewhat lower than projected at the beginning of the month primarily due to a delay in EU financing (the first EUR0.6bln tranche of the MFA IV program). Taking into account that disbursement will now likely be linked to the awaited IMF board approval, the timing of which has recently been made even more unpredictable by a government reshuffle, further postponement is likely. Moreover, despite the fact that the shortfall was this time partially compensated by higher than anticipated net NBU FX purchases, the presence of a sharp global financial market correction suggest a much more pessimistic outlook for the coming months than before (the regulator's net interventions stand at c. \$400mln so far). We identify a further slip in prices of exported commodities (oil has been hardest hit so far, but metals and agricultural products may follow suit) and capital flight (especially from local hryvnia bonds, where non-resident holdings increased by c. \$4.3bln in 2019) as key risks for elevated demand for foreign currency. In this light, we slash our end-of-year reserves forecast by \$2.5bln to \$27.5bln. We expect the figure in March to drop by some \$1.4bln MoM to \$25.2bln.



Note: import coverage is calculated using average LTM imports
 Source: NBU, Adamant Capital estimates

Metinvest's EBITDA in December dropped by \$57mln MoM to -\$61mln, excluding JVs. The full-year figure decreased by 54% YoY to \$1.0bln. The monthly contribution of the metals division amounted to -\$94mln, compared to +\$37mln of the mining segment. Operating cash flow increased by \$55mln QoQ to \$37mln on the back of a working capital divestment. Capex grew by 83% to \$119mln, which drove FCF down to -\$82mln. The LTM leverage ratio was up by 26% MoM to 2.7x. During the company's annual conference call with investors, management delivered an overall upbeat outlook on future performance despite volatile markets, and guided for EBITDA to grow in 2020. Intent to acquire the remaining shares in Pokrovska Mine (by exercising an option with a strike price of \$570mln) was confirmed and approval from the Antimonopoly Committee was said to be likely. Total planned capex for the next 12 months, excluding the abovementioned transaction, was voiced at \$650mln.

Our view: EBITDA in December underperformed our projections yet again, largely due to even greater losses in the steel segment than anticipated. According to our calculations, the average realized price per ton contracted by 17% MoM to \$392, which put it almost \$100 below estimated production and delivery costs. Taking into account that the HRC Black Sea benchmark has recovered by close to 30% from its low in October, we believe that a similar dynamic (albeit with a c. 2-month lag) will materialize in Metinvest's financials. This assertion seems to coincide with 1Q20 earnings recovery observations reported by management during the conference call. That said, we do not share the CEO's optimism regarding YoY profitability growth for the full year, as margins in both segments will, in our view, remain subdued if market prices remain at current levels (and especially if they being to drop back due to effects of the coronavirus). Our EBITDA forecast still remains at \$500mln excluding JVs. As noted earlier, we calculate that forward-looking leverage may rise to over 5.0x EBITDA, which puts the company into the moderate-risk category. We reiterate our 'Hold' recommendation for all of Metinvest's eurobonds.

Metinvest's December financial results, \$mln

	Dec	Nov	MoM	2019	YoY
Revenues	778	693	12%	10,757	-9%
EBITDA ¹	-61	-4	nm	1,027	-54%
margin	-8%	-1%	-7pp	10%	-9pp
Metals EBITDA	-94	-33	nm	-68	nm
Mining EBITDA	37	31	19%	1,117	2%
Metal sales ² , kt	715	670	7%	8,824	-1%
Steel price ³ , \$/t	392	472	-17%	537	-12%
Iron ore sales ⁴ , kt	2,646	2,215	19%	29,296	8%
Iron ore price ⁵ , \$/t	75	76	0%	93	6%
OCF	37	-18	nm	814	-26%
Capex	119	65	83%	943	119%
Free cash flow	-82	-83	nm	-129	nm
Total debt	3,032	2,971	2%	3,032	11%
Net debt	2,758	2,618	5%	2,758	12%
Net debt/LTM	2.7	2.1	26%	2.7	144%

(1) Excluding JVs

(2) Excluding resales

(3) Calculated as revenues of finished and semi-finished goods divided by the volume sold

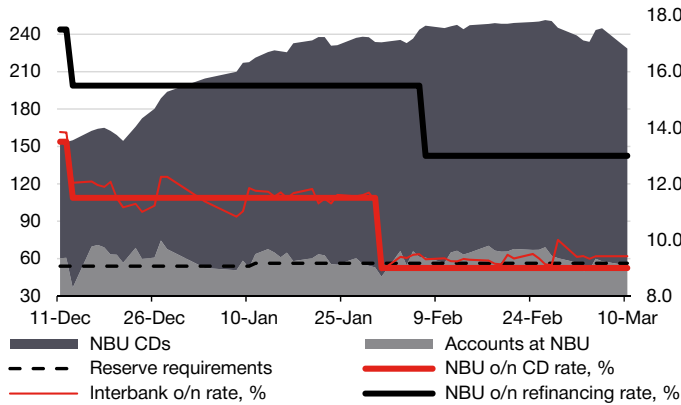
(4) Estimated, including internal sales and pellets in ore equivalent

(5) The average realized price, including pellets in ore equivalent

Source: Company data, Adamant Capital estimates

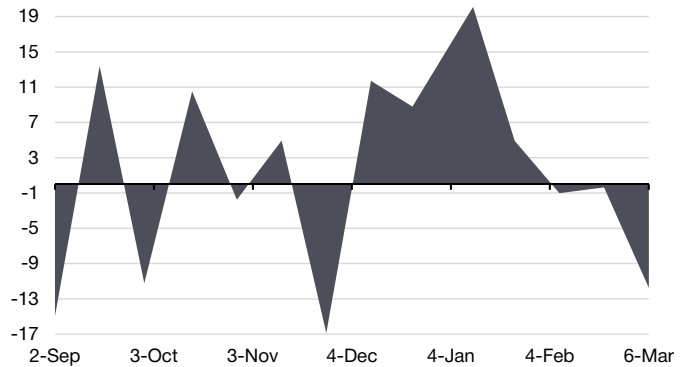
Appendix

Banking system 3m liquidity (lhs, UAHbln) vs NBU CD rates (%)



Source: NBU, Adamant Capital estimates

Banking system 6m inflows from the state treasury and the DGF

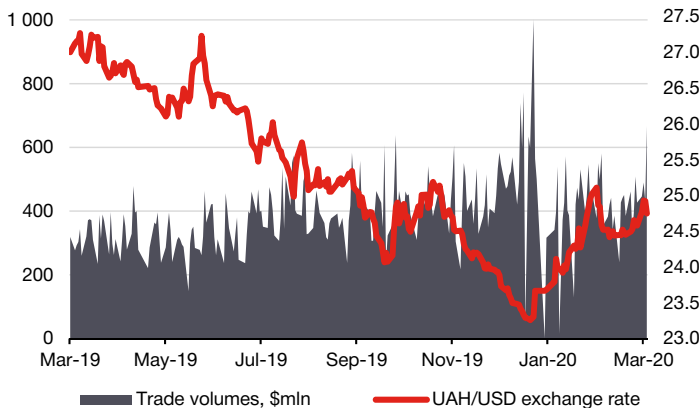


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has decreased by UAH 10.5bln to UAH 228.5bln over the last week. The FinMin's government bond auctions were cancelled.

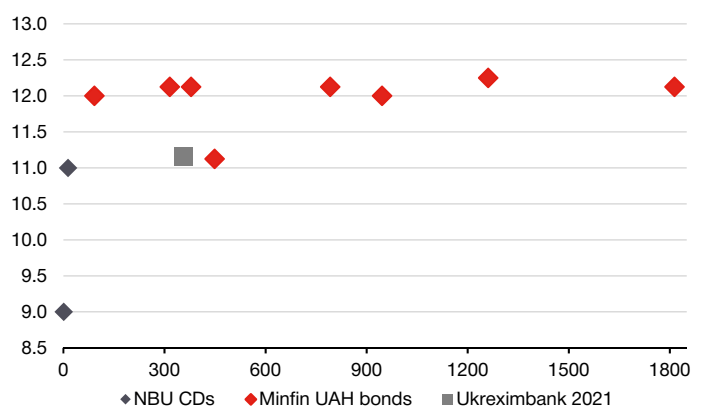
The UAH/USD interbank rate over the last week depreciated by 2.08%, starting out with 24.77 and ending at 25.29.

FX interbank trade volume (lhs) and FX rate (rhs), past 12 months

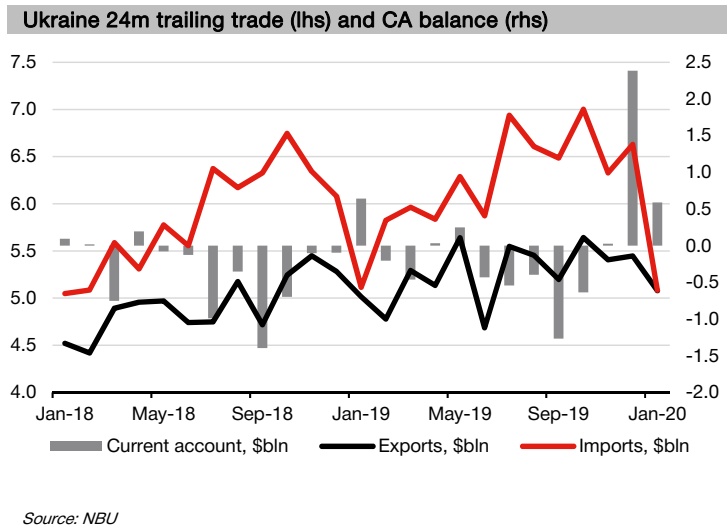
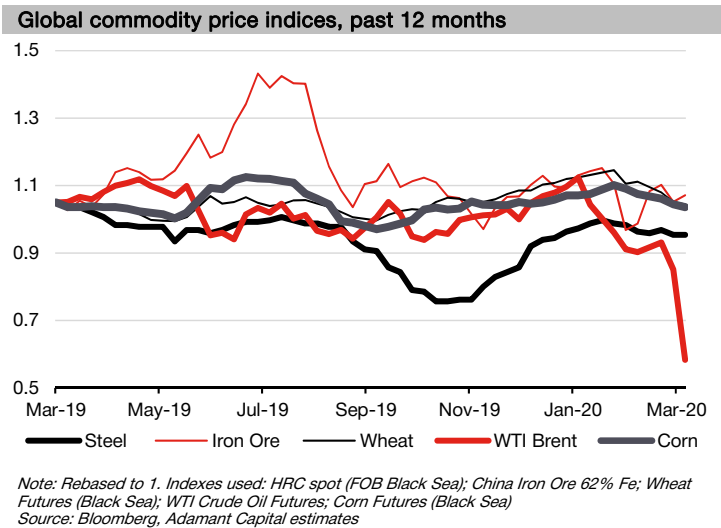
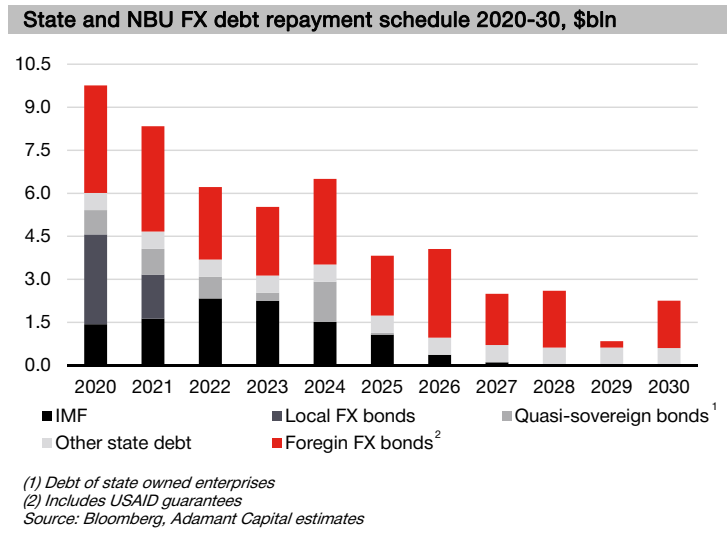
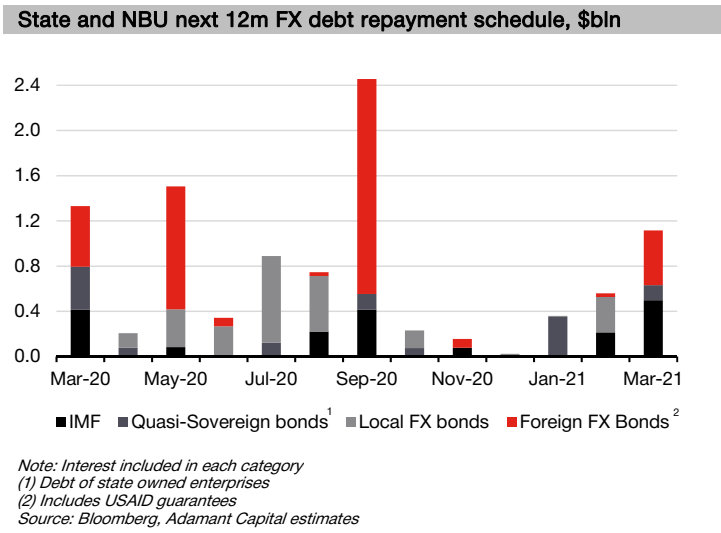
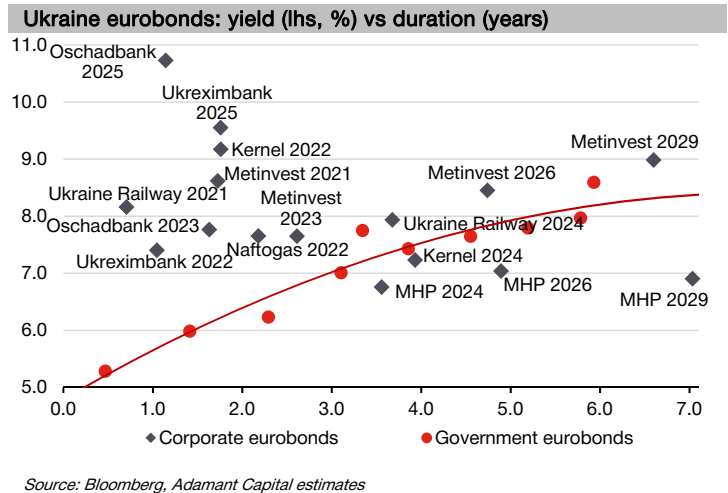
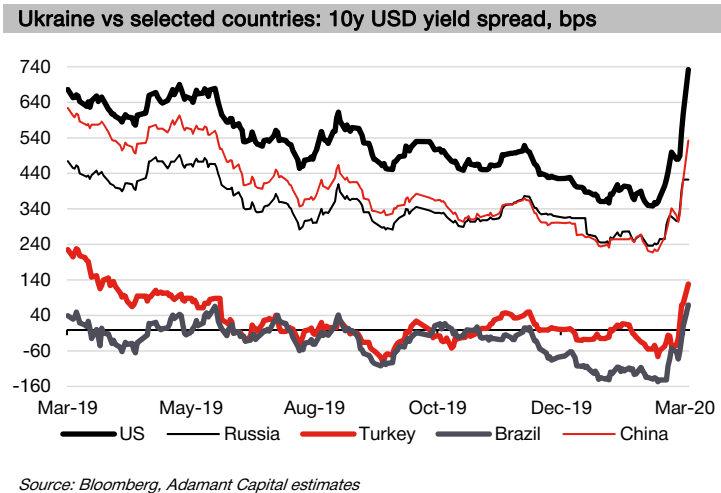


Note: Exchange rate figures are from official interbank data
Source: NBU

Local market yield curve: yield (lhs, %) and maturity (rhs, days)



Source: NBU, Bloomberg, Adamant Capital estimates



Key macroeconomic indicators								
	2018	1Q19	2Q19	3Q19	4Q19E	2019E	1Q20	2020E
Real GDP growth, YoY	3.3%	2.5%	4.6%	4.1%	1.5%	3.2%	2.0%	3.0%
Nominal GDP, UAHbln	3,559	807	928	1,106	1,108	3,950	848	4,332
Nominal GDP, \$bln	131	30	35	44	46	153	35	173
GDP deflator growth YoY, %	15.0%	11.7%	9.4%	6.8%	4.2%	7.5%	3.0%	6.5%
Period average CPI YoY, %	11.0%	8.9%	9.1%	8.5%	5.2%	7.9%	3.3%	3.3%
End of period CPI YoY, %	9.8%	8.6%	9.0%	7.5%	4.1%	4.1%	3.4%	4.4%
Consolidated budget deficit, % of GDP ¹	1.9%	1.1%	1.0%	-0.9%	8.9%	2.1%	1.1%	2.1%
Broad public sector deficit, % of GDP ²	2.2%	1.1%	1.0%	-0.9%	8.9%	2.1%	1.1%	2.1%
Public debt as % of LTM GDP, UAH	60.9%	58.6%	55.7%	51.4%	49.4%	49.4%	49.4%	47.0%
Public external debt as % of LTM GDP, \$ ³	38.6%	37.5%	36.2%	33.3%	31.6%	31.6%	31.6%	29.2%
Total external debt, \$bln	115	114	116	120	120	120	121	122
Export of goods and services, \$bln	59.1	15.1	15.5	16.2	16.5	63.4	14.8	60.3
Import of goods and services, \$bln	70.4	16.9	18.3	20.2	20.0	75.5	17.0	75.1
Trade balance, \$bln	-11.3	-1.8	-2.8	-3.9	-3.5	-12.1	-2.2	-14.8
Current account, \$bln	-4.3	-0.2	-0.5	-2.1	1.8	-1.1	-0.2	-5.0
Financial account, \$bln ⁴	-7.1	-0.5	-0.9	-3.6	-3.5	-6.2	-0.7	-6.6
End of period NBU reserves, \$bln	20.8	20.6	20.6	20.1	25.3	25.3	25.2	27.5
Average interbank exchange rate, UAH/\$ ⁵	27.2	27.3	26.6	25.2	24.2	25.8	24.0	25.0
EOP interbank exchange rate, UAH/\$	27.7	27.2	26.2	24.2	23.7	23.7	25.0	25.0
EOP key policy rate NBU, %	18.0%	17.5%	17.5%	16.5%	13.5%	13.5%	11.0%	9.0%

(1) Includes net loans given out to state enterprises from the central budget

(2) Includes quasi-fiscal expenditures such as the recapitalization of Naftogaz, state banks, and the DGF. Also accounts for state guarantees.

(3) GDP calculated in \$ according to the average UAH/\$ exchange rate for the year

(4) As per the 6th edition of the IMF's Balance of payments and international investment position manual

(5) Based on official NBU data of average daily interbank rates. Not weighted by volume traded

Source: NBU, SSSU, State treasury, Ministry of Finance, IMF, Adamant Capital estimates

Indicative eurobond prices, yields, and recommendations									
Bond name	Recommendation	Rec date	Coupon	Maturity	Bid Yield	Bid Price	1 week Δ	Dur, yrs	Out, \$mln
Ukraine 2023	Hold	-	7.8	Sep-23	7.0	102.3	-7.5	3.1	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	7.7	104.1	-9.2	3.3	750
Ukraine 2027	Hold	-	7.8	Sep-27	8.0	98.8	-12.6	5.8	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	8.6	106.9	-15.5	5.9	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	8.4	92.5	-16.6	7.6	3,000
Avangard in default	Sell	9-Apr-19	10.0	Oct-18	nm	4.1	0.5	nm	214
DTEK 2024	Buy	11-Feb-20	10.8	Dec-24	13.1	92.5	-4.1	3.4	1,344
Kernel 2022	Hold	3-Mar-20	8.8	Jan-22	9.2	99.3	-6.8	1.8	500
Kernel 2024	Hold	3-Mar-20	6.5	Oct-24	7.2	97.2	-6.3	3.9	300
Metinvest 2021	Hold	10-Mar-20	7.5	Dec-21	8.6	98.0	-1.7	1.7	115
Metinvest 2023	Hold	10-Mar-20	7.8	Apr-23	7.6	100.3	-3.2	2.6	505
Metinvest 2025 (EUR)	Hold	10-Mar-20	5.6	Jun-25	7.0	94.0	-5.6	4.5	333
Metinvest 2026	Hold	10-Mar-20	8.5	Apr-26	8.5	100.2	-4.5	4.7	648
Metinvest 2029	Hold	10-Mar-20	7.8	Oct-29	9.0	92.2	-7.5	6.6	500
MHP 2024	Buy	4-Feb-20	7.8	May-24	6.8	103.5	-4.1	3.6	500
MHP 2026	Buy	4-Feb-20	7.0	Apr-26	7.0	99.6	-4.8	4.9	550
MHP 2029	Buy	4-Feb-20	6.25	Sep-29	6.9	95.5	-3.3	7.0	350
Naftogas 2022	Hold	1-Oct-19	7.4	Jul-22	7.7	99.4	-5.3	2.2	335
Naftogas 2024 (EUR)	Hold	1-Oct-19	7.1	Jul-24	8.0	96.9	-10.9	3.7	672
Oschadbank 2023	Buy	18-Feb-20	9.4	Mar-23	7.8	102.5	-1.8	1.6	245
Oschadbank 2025	Buy	18-Feb-20	9.6	Mar-25	10.7	98.7	-5.2	1.1	500
Privatbank in default (10.250)	Not rated	-	10.3	Jan-18	nm	30.8	0.0	nm	160
Privatbank in default (10.875)	Not rated	-	10.9	Feb-18	nm	31.2	0.0	nm	175
Ukraine Railway 2021	Buy	8-Oct-19	9.9	Sep-21	8.2	101.2	-2.7	0.7	200
Ukraine Railway 2024	Not rated	-	8.3	Jul-24	7.9	101.1	-6.0	3.7	595
Ukreximbank 2021 (UAH)	Buy	18-Feb-20	16.5	Mar-21	14.0	102.2	-1.8	0.9	150
Ukreximbank 2022	Buy	18-Feb-20	9.6	Apr-22	7.4	102.3	-2.4	1.0	313
Ukreximbank 2025	Buy	18-Feb-20	9.8	Jan-25	9.6	100.3	-4.7	1.8	600
Ukrlandfarming in default	Sell	13-Jun-17	10.9	Mar-18	nm	5.0	-0.1	nm	543

Note: all bonds are rated in relation to the sovereign, which is assumed to have a 'Hold' rating

Source: Bloomberg, Adamant Capital estimates

Fixed Income one-week event calendar

Event	Type	Date
NBU - Decision on the key policy rate	Exact	12-Mar
SSSU - Agricultural production monthly data	Exact	17-Mar

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