

Weekly Digest

- Real GDP growth in 4Q19 amounted to 1.5%
- Ukraine's authorities held talks with the IMF to double aid and submitted a required bank law to parliament
- Output of key economic sectors in February grew by 1.5% YoY

Real GDP growth in 4Q19 amounted to 1.5%. The figure came fully in line with the SSSU's preliminary estimate from February.

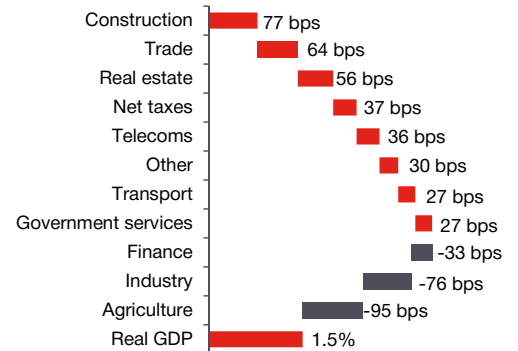
Our view: The SSSU decided to change the base year for all of the price data from 2010 to 2016, which had a significant impact on the entire dataset, and partially explains why growth turned out to be more robust than we predicted back in December. For instance, based on the previous methodology, agricultural output contracted in 4Q19 by over 10%, as opposed to just 6.5% suggested by the new metric. Similarly, the updated figure for industrial production stands at -3.8% versus -5.2% reported previously.

Overall, however, supply side indicators moved mostly in anticipated directions. Top sectors contributing to growth were construction (up 24.2% YoY) and trade (+5.1%), followed by, somewhat surprisingly, real estate (+8.9%). Negative impact was felt mostly from the already mentioned industry and agriculture. Finance also reported a slowdown, largely in line with the dynamic of banking system operating profits (excluding impairment charges). The correction factor, which arises as a result of chain-weighting, as expected, turned out to be negative and smaller than in 3Q19. We continue to believe it to have been most affected by iron ore production and pricing.

From the demand side, fourth quarter capex as a share of GDP set another record as of 2010, having hit 18.9%. While undeniably strong, this figure has been somewhat inflated by the influx of one-off investments into green energy projects. Implication for economic growth from these is also undercut by the fact that new capacities will end up phasing out some of the ones that already operate.

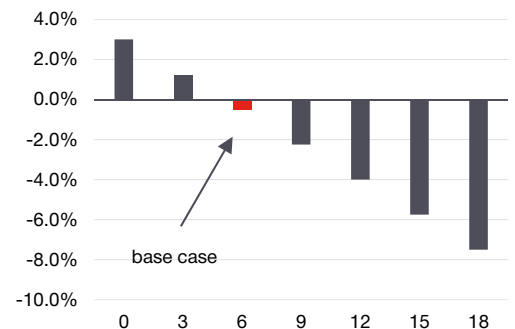
Our outlook for 2020 has entered into a phase of a constantly evolving narrative in light of how the world as a whole and Ukraine in particular is adapting to the coronavirus epidemic. Last week we estimated that a three-week lockdown in Ukraine will cost the economy some 1.0-1.5% of real GDP, but given that the containment measures have since then become even stricter, we up this projection to 1.5-2.0%. Moreover, we now think that the quarantine is likely to be prolonged for at least another three weeks, which means that total costs in our base-case forecast stand on the order of 3.0-4.0%. A longer or an even more intensive lockdown, such as one that affects industrial producers, would naturally drive this figure even higher. We updated estimate for 1Q20 and FY20 real GDP growth currently stand at -5.0% and -0.5%, respectively.

Real GDP growth contribution by sector in 4Q19



(1) The difference between total real GDP and the sum of the GDP contributions by sector
 Source: SSSU, Adamant Capital estimates

Lock-down length (weeks) vs FY20E real GDP



Note: horizontal axis represent the number of weeks of assumed lock-down of current intensity due to the coronavirus epidemic
 Source: Adamant Capital estimates

Ukraine's authorities held talks with the IMF to double aid and submitted a required bank law to parliament. The Deputy Head of the Presidential Office Kovaliv stated in two interviews to media that Zelensky has held a call with the Fund's Manager Director Georgieva, during which a substantial increase in the aid (the figure was said to increase 'almost twofold') has been agreed. Earlier Kovaliv mentioned that due to the coronavirus the government expects the economy this year to contract by at least 5% and for the budget deficit to reach 7% of GDP, instead of the 2.2% targeted earlier. According to a local news outlet, a new version of the bank law (dubbed by local media as 'anti-Kolomoisky'), which aims to prevent the reversal of the NBU's and FinMin's earlier liquidation and nationalization decisions via courts, has been submitted to parliament, after allegedly receiving IMF approval.

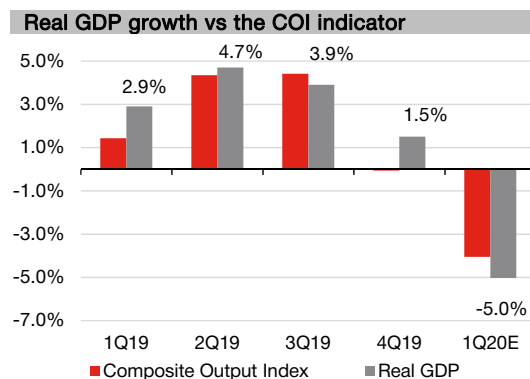
Our view: Though agreed on a staff level back in the beginning of December, the new \$5.5bln IMF program was held back from proceeding by the parliament's inability to vote on the abovementioned bank legislation. Now, pressured by very unfavorable markets for raising capital and increased budget spending needs, it seems that Ukraine's leadership has decided to finally tackle vested interests. Taking into account that the initiative comes from Zelensky himself, we believe that the probability of mustering a sufficient number of votes in parliament to pass the bill is high. We view the news for Ukraine's entire eurobond universe as very positive.

Output of key economic sectors in February grew by 1.5% YoY, as measured by our COI indicator. Industrial production fell by 1.5% (4.1% after seasonal adjustments), demonstrating an improvement versus December (-5.1% and -4.7%, respectively). Agriculture remained unchanged at +0.1%. According to our estimates, transportation was down by 3.5% YoY, while domestic trade surged by 6.7% (retail grew by a record-setting 15.7%). Data for construction was not yet reported.

Our view: The consolidated output dynamic of observable sectors (measured by the COI) came in moderately better than predicted, largely owing to a recovery in the steel industry, where the production gap versus year last shrank to zero from 10% in January. Thermal power generation also surprised on the upside, having contracted by just 2% YoY as opposed to a 25% drop on average over the past 3 months. Additionally, the retail sales dynamic turned out to be even more robust than anticipated (we modelled a 13.5% bump), though was counterbalanced by a negative contribution of wholesale (-3.1%). All results were partially boosted by a positive calendar effect due to 2020 being a leap year.

Looking ahead into March, we face the difficult challenge of assessing the impact of a two-and-a-half-week lockdown on this part of the economy. As mentioned previously, domestic trade, and retail specifically, is likely to be the biggest loser from the social distancing initiatives. That said, we expect Ukraine to suffer less from these measures than higher income countries, such as Italy, given that roughly 50% of the domestic consumer basket is composed of food (consumer goods supermarkets remain open). The other sector that will likely come under severe strain is transportation, as most public transit routes have been closed as of March 18. Additionally, we think that a negative effect will be felt in electric power generation and, possibly, construction (some projects may be put on hold due to a demand shock). Taking into account that most industrial plants continue to so far operate without interruptions, we expect other businesses that make up the COI to be affected only marginally, allowing for a 12% decline of the indicator overall.

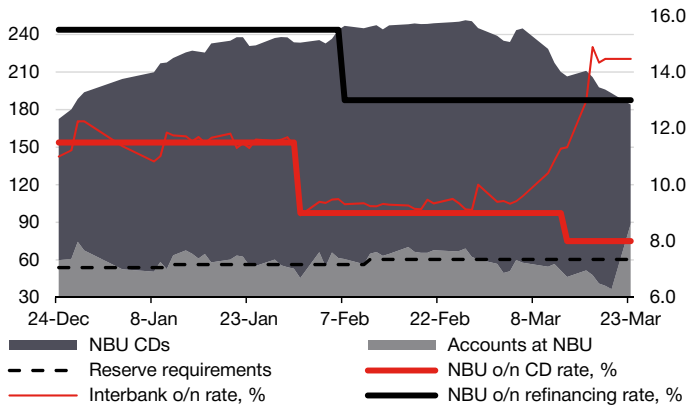
All in all, our baseline real GDP growth projection for 1Q20 currently stands at -5.0%. Having made the assumption of another three-week quarantine in 2Q20, we have so far reduced our estimate for 2020 to -0.5%.



Note: The Composite Output Index represents the weighted average growth of industrial production, retail sales, wholesale sales, transportation, and agricultural output
Source: SSSU, 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

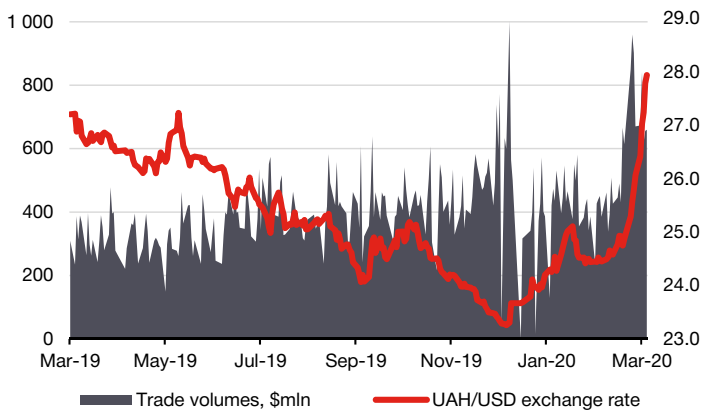


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has decreased by UAH 22.0bln to UAH 184.0bln over the last week. On March 24 the Ministry of Finance conducted a local USD denominated placement maturing in June 2020 with a yield of 3.0% and EUR denominated placement maturing in May 2021 with yield of 2.22%. A total of UAH 24.8bln was raised as a result.

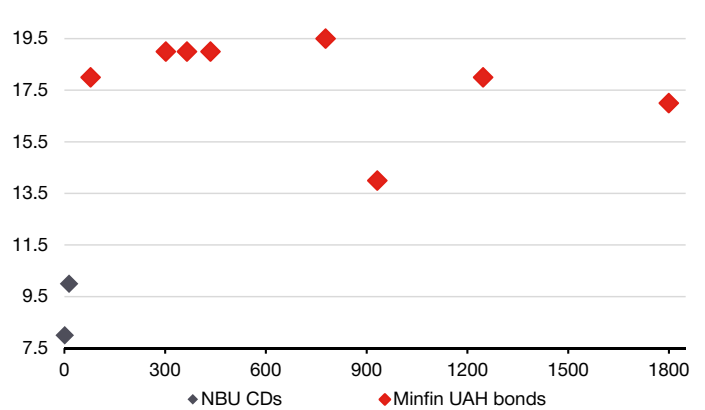
The UAH/USD interbank rate over the last week depreciated by 6.48%, starting out with 26.42 and ending at 28.13.

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



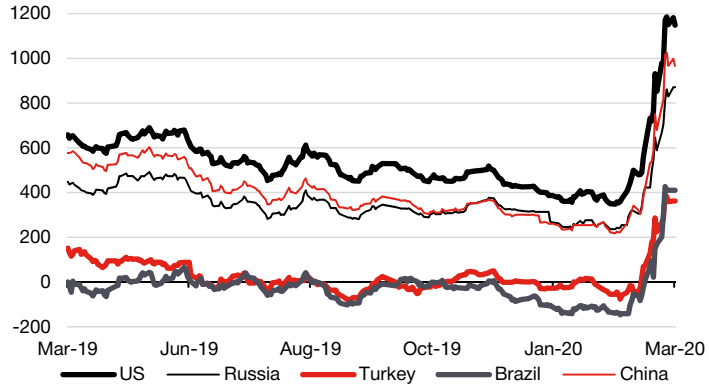
Note: Exchange rate figures are from official interbank data
Source: NBU

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



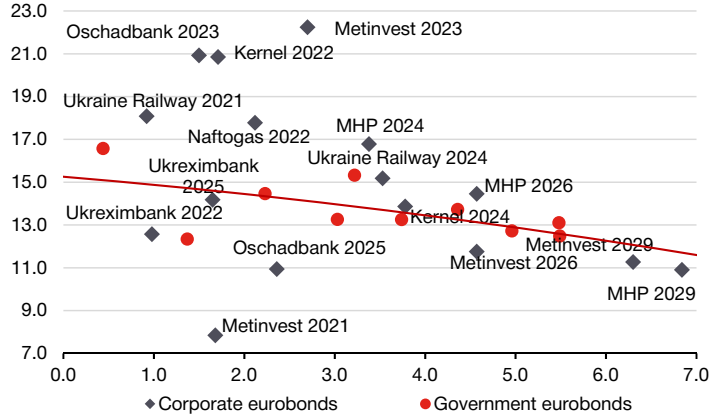
Source: NBU, Bloomberg, Adamant Capital estimates

Ukraine vs selected countries: 10y USD yield spread, bps



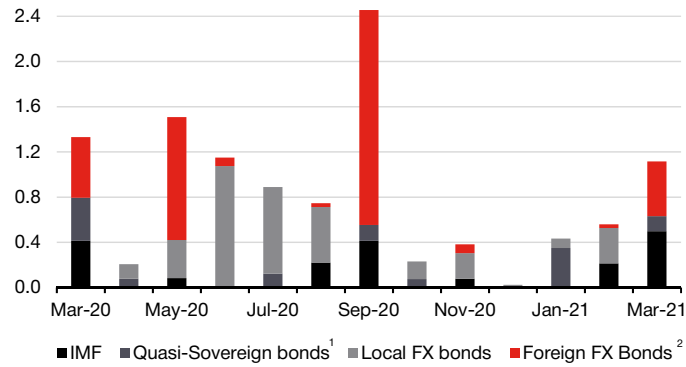
Source: Bloomberg, Adamant Capital estimates

Ukraine eurobonds: yield (lhs, %) vs duration (years)



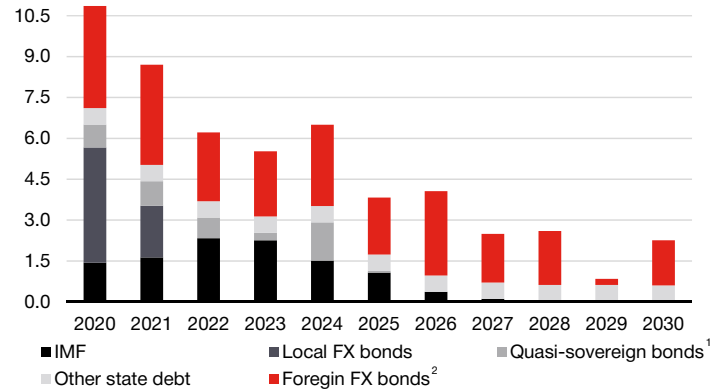
Source: Bloomberg, Adamant Capital estimates

State and NBU next 12m FX debt repayment schedule, \$bln



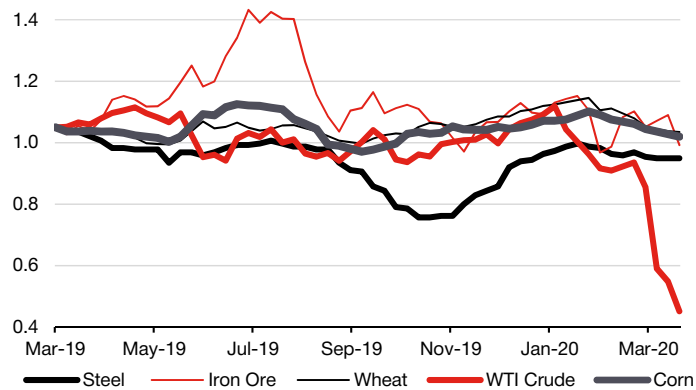
Note: Interest included in each category
 (1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

State and NBU FX debt repayment schedule 2020-30, \$bln



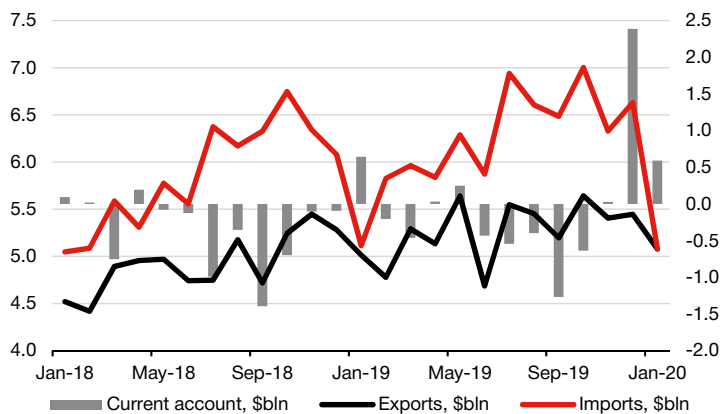
(1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

Global commodity price indices, past 12 months



Note: Rebased to 1. Indexes used: HRC spot (FOB Black Sea); China Iron Ore 62% Fe; Wheat Futures (Black Sea); WTI Crude Oil Futures; Corn Futures (Black Sea)
 Source: Bloomberg, Adamant Capital estimates

Ukraine 24m trailing trade (lhs) and CA balance (rhs)



Source: NBU

Key macroeconomic indicators								
	2018	1Q19	2Q19	3Q19	4Q19	2019	1Q20E	2020E
Real GDP growth, YoY	3.3%	2.9%	4.7%	3.9%	1.5%	3.2%	-5.0%	-0.5%
Nominal GDP, UAHbln	3,559	810	929	1,104	1,108	3,951	793	4,187
Nominal GDP, \$bln	131	30	35	44	46	153	32	164
GDP deflator growth YoY, %	15.0%	11.7%	9.4%	6.8%	4.2%	7.6%	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%	55.6%	51.3%	50.6%	50.6%	50.6%	49.8%
Public external debt as % of LTM GDP, \$ ³	38.6%	37.4%	36.1%	33.0%	31.8%	31.8%	31.8%	31.0%
Total external debt, \$bln	115	114	116	118	122	122	121	124
Export of goods and services, \$bln	59.1	15.1	15.5	16.3	16.5	63.4	14.8	60.3
Import of goods and services, \$bln	70.4	16.9	18.3	20.3	20.0	75.5	17.0	75.1
Trade balance, \$bln	-11.3	-1.8	-2.8	-4.0	-3.5	-12.1	-2.2	-14.8
Current account, \$bln	-4.3	-0.2	-0.5	-2.2	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	25.0	25.5
EOP interbank exchange rate, UAH/\$	27.7	27.2	26.2	24.2	23.7	23.7	27.5	25.5
EOP key policy rate NBU, %	18.0%	17.5%	17.5%	16.5%	13.5%	13.5%	10.0%	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	13.3	85.2	-5.1	3.0	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	15.3	82.1	-7.2	3.2	750
Ukraine 2027	Hold	-	7.8	Sep-27	12.5	77.5	-6.1	5.5	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	13.1	83.0	-5.3	5.5	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	11.0	75.7	-2.4	7.4	3,000
Avangard in default	Sell	9-Apr-19	10.0	Oct-18	nm	4.2	0.0	nm	214
DTEK 2024	Buy	11-Feb-20	10.8	Dec-24	27.1	59.6	0.0	3.0	1,344
Kernel 2022	Hold	3-Mar-20	8.8	Jan-22	20.9	82.2	-9.1	1.7	500
Kernel 2024	Hold	3-Mar-20	6.5	Oct-24	13.9	75.7	-7.2	3.8	300
Metinvest 2021	Hold	17-Mar-20	7.5	Dec-21	7.8	99.3	0.0	1.7	115
Metinvest 2023	Hold	17-Mar-20	7.8	Apr-23	22.2	68.9	-26.7	2.7	505
Metinvest 2025 (EUR)	Hold	17-Mar-20	5.6	Jun-25	9.4	84.7	-1.3	4.5	333
Metinvest 2026	Hold	17-Mar-20	8.5	Apr-26	11.8	86.2	-4.1	4.6	648
Metinvest 2029	Hold	17-Mar-20	7.8	Oct-29	11.3	79.7	-3.5	6.3	500
MHP 2024	Buy	4-Feb-20	7.8	May-24	16.8	73.9	-17.1	3.4	500
MHP 2026	Buy	4-Feb-20	7.0	Apr-26	14.5	70.5	-15.5	4.6	550
MHP 2029	Buy	4-Feb-20	6.25	Sep-29	10.9	72.9	-12.3	6.8	350
Naftogas 2022	Hold	1-Oct-19	7.4	Jul-22	17.8	80.9	-11.9	2.1	335
Naftogas 2024 (EUR)	Hold	1-Oct-19	7.1	Jul-24	13.9	79.0	0.0	3.6	672
Oschadbank 2023	Buy	18-Feb-20	9.4	Mar-23	20.9	84.7	-4.3	1.5	245
Oschadbank 2025	Buy	18-Feb-20	9.6	Mar-25	10.9	97.1	0.0	2.4	500
Privatbank in default (10.250)	Not rated	-	10.3	Jan-18	nm	30.7	0.0	nm	160
Privatbank in default (10.875)	Not rated	-	10.9	Feb-18	nm	31.0	-0.2	nm	175
Ukraine Railway 2021	Buy	8-Oct-19	9.9	Sep-21	18.1	93.1	-2.5	0.9	200
Ukraine Railway 2024	Not rated	-	8.3	Jul-24	15.2	78.7	-10.7	3.5	595
Ukreximbank 2021 (UAH)	Buy	18-Feb-20	16.5	Mar-21	53.5	75.2	-18.8	0.9	150
Ukreximbank 2022	Buy	18-Feb-20	9.6	Apr-22	12.6	97.2	0.0	1.0	313
Ukreximbank 2025	Buy	18-Feb-20	9.8	Jan-25	14.2	93.1	0.0	1.7	600
Ukrlandfarming in default	Sell	13-Jun-17	10.9	Mar-18	nm	5.1	0.0	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
Treasury - Monthly state budget performance	Indicative	26-Mar
SSSU - Construction monthly data	Exact	30-Mar
NBU - Balance of payments monthly data	Exact	31-Mar

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