

Weekly Digest

- Real GDP in 1Q20 dropped by 1.3% (final data)
- Output of key economic sectors in May declined by 11.3% YoY
- Ukraine has prolonged social distancing measures until July 31

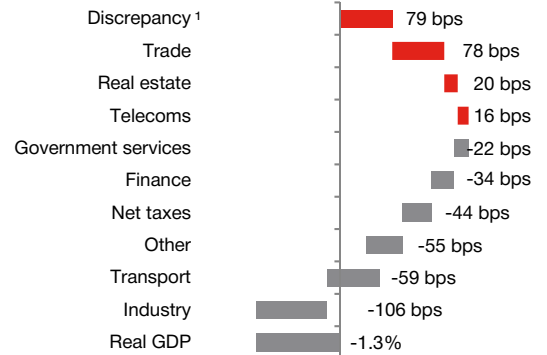
Real GDP in 1Q20 dropped by 1.3% (final data). The figure was revised upwards by 20bps from the SSSU's preliminary estimate in May.

Our view: Compared to our original -2.2% projection, the largest deviation occurred in the discrepancy factor, which contributed almost +0.8% to the growth figure (we budgeted zero) and reflects the structural differences between the updated GDP composition (from 2019) and that of the base year. The previously unobserved part of the economy performed somewhat worse than anticipated overall, though only a small portion of this dynamic can be traced back to COVID-19 effects. The banking system in March, for example, posted practically flat operating profits YoY and the sector's contraction in value-added is most likely due to a drop in net interest income generated by the NBU. Restaurants, which were hit by the lockdown in earnest, decreased output by 8.8%. Given that restrictions lasted for only 2 weeks of the quarter, we believe this to be equivalent to a c. 50% reduction. In contrast, education and sports & entertainment posted losses at just 1.1% and 1.7%, respectively. Real estate services were up by 2.9%. Sectors for which high frequency data is reported ended up contributing mostly in line with expectations. Transportation contracted by 8.8% and industrial output as a whole was down by 2.1% (lower demand for electricity, steel, and machinery were the main culprits).

From the demand side, first quarter capex as a share of GDP contracted to a 3-year low of 15.2%. While part of this may have been due to COVID-19, we think that a large portion is most likely related to a halt in investment into renewable power projects (the sector is currently going through a crisis and will likely see a considerable reduction in feed-in tariffs in the future).

Overall, the reported figures together with the already available high frequency output data suggest that the COVID-19 fallout in 2Q20 might actually be smaller than previously anticipated. That said, we now also think that some form of lockdown is likely to stay in place during a large part of 3Q20, which means that economic recovery will be more prolonged. Thus, on balance, we retain our annual real GDP growth forecast at -3.5%, but increase it for 2Q20 to -9.0% from -15.0% previously.

Real GDP growth contribution by sector in 1Q20



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

Output of key economic sectors in May declined by 11.3% YoY, as measured by our COI indicator. Industrial production fell by 11.2% (11.7% after seasonal adjustments), demonstrating a moderate recovery versus March (-16.2% and -16.7%, respectively). According to our estimates, transportation and domestic trade contracted by 29.2% YoY and 4.0%, respectively (retail lost just 3.1% versus last year). Agriculture slipped by 4.0%. Data for construction was not yet reported.

Our view: The consolidated output dynamic of observable sectors (measured by the COI) came in moderately lower than predicted, owing predominantly to weaker performance of industrial production and transportation. Though to a smaller degree than in April, the former continued to suffer from weak demand for machinery and metals. Electricity generation was also down by almost 13% YoY, although the share of the more expensive thermal power grew by 8ppts MoM to 39%. The latter surprised us with a lack of recovery in cargo shipment volumes, which remained some 20% below last year despite a substantial relaxation of lockdown restrictions as of May 12. That said, retail trade did rebound as anticipated and already stands at almost pre-pandemic levels.

More broadly, the data supports our view that the economy has started to recover in May (the COI improved by nearly 5ppts) and we expect to see a similar dynamic in June, given that less strict social distancing measures will last for the entire month. Moreover, steel prices have continued to grow since our last overview, suggesting that domestic mills may soon increase utilization (which will also increase demand for electricity). A negative contribute might come from the agricultural sector, as wheat harvest forecasts indicate a possible decline in volumes in YoY terms (up to 10%). Even after accounting for this factor, however, we still expect the COI to land at -7.4%.

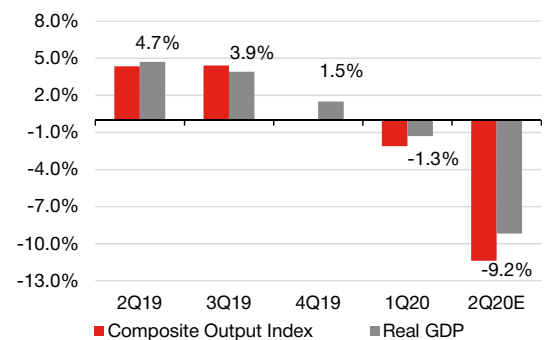
All in all, we feel that the reported figures allow us to maintain our annual real GDP growth projection at -3.5%. Our estimate of the economic decline in 2Q20, however, has been altered based on 1Q20 results (please see the relevant discussion included in this report for more details).

Ukraine has prolonged social distancing measures until July 31.

According to the relevant Cabinet decree, all persons visiting public spaces and travelling via public transport will need to continue wearing masks. It is also recommended that service sectors such as supermarkets, restaurants, education centers, and repair shops delay opening hours until 10 in the morning. Over the past week, official data indicates that the average number of new individuals infected per day has increased by c. 20% to roughly 800 people (this is a 59% increase from 2 weeks ago).

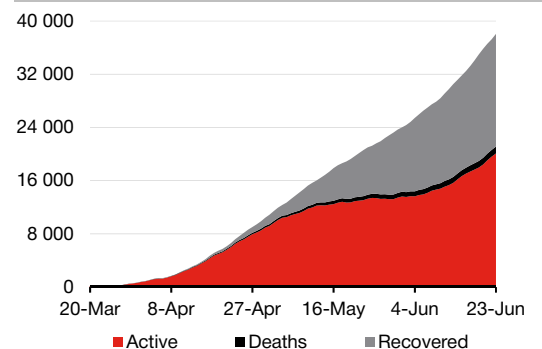
Our view: Although some COVID-19 restrictions are being prolonged, the country is clearly moving towards a substantial relaxation of the lockdown. As of June 15, international flights out and into Ukraine have already been launched and as of June 19 all border crossings with the EU and Moldova have been opened. That said, taking into account the recent increase in incidence rates, we do not exclude a temporary return to stricter measures. We would expect these to affect certain cities or administrative regions, however, rather than Ukraine as a whole.

Real GDP growth vs the COI indicator



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

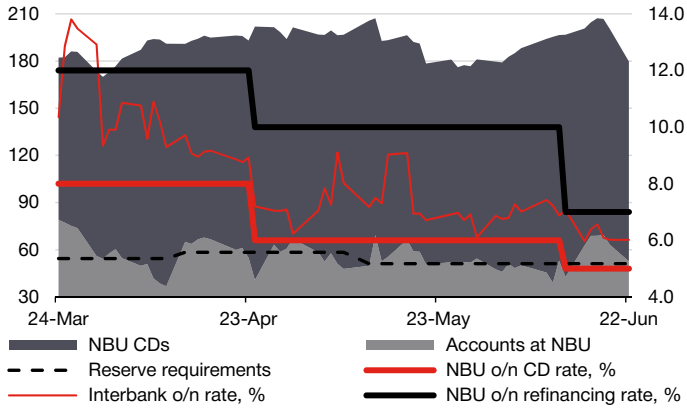
COVID-19 cases in Ukraine as of March 20



Source: Ministry of Health, minfin.com.ua, Adamant Capital estimates

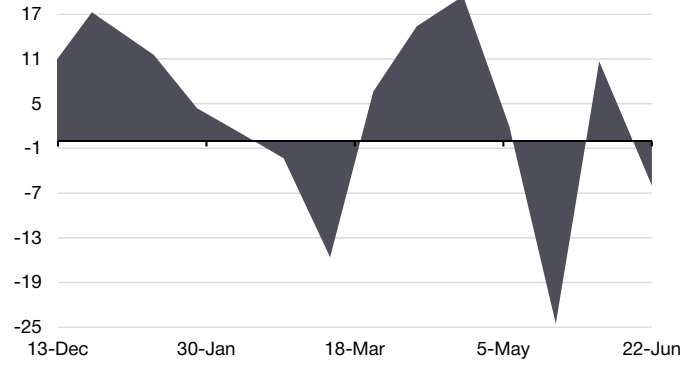
Appendix

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

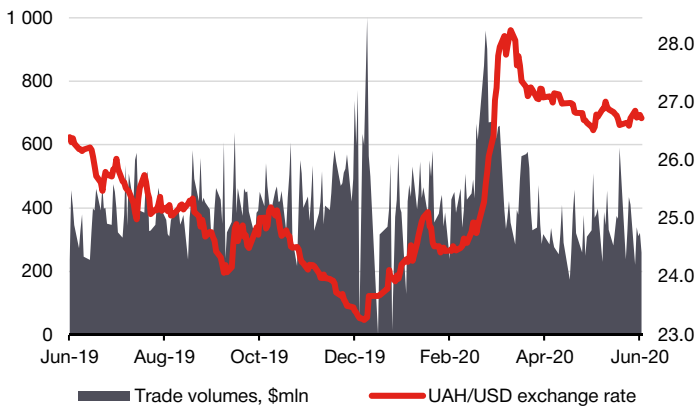


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has decreased by UAH 21.0bln to UAH 179.6bln over the last week. On June 23 the Ministry of Finance conducted local hryvnia denominated placement maturing in September 2020, November 2020, February 2021, May 2021, February 2022 and February 2023 with yields of 7.24%, 7.71%, 9.50%, 9.70%, 10.39% and 10.47% respectively. A total of UAH 6.2bln was raised as a result.

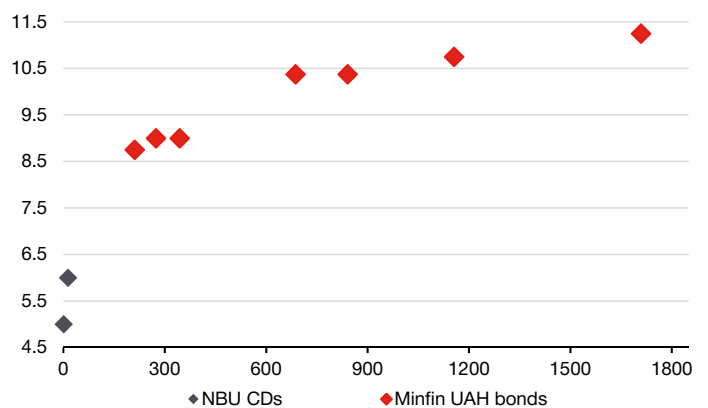
The UAH/USD interbank rate over the last week appreciated by 0.65%, starting out with 26.85 and ending at 26.67.

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



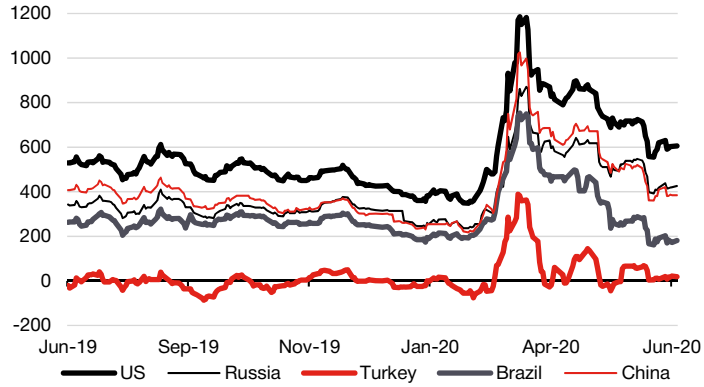
Note: Exchange rate figures are from official interbank data
Source: NBU

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



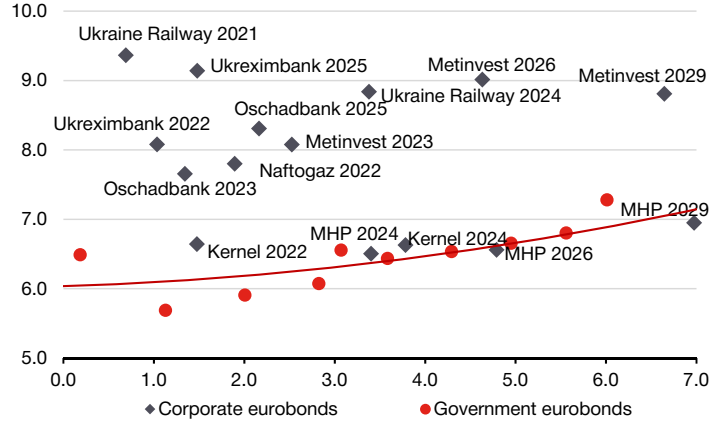
Source: NBU, Bloomberg, Adamant Capital estimates

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



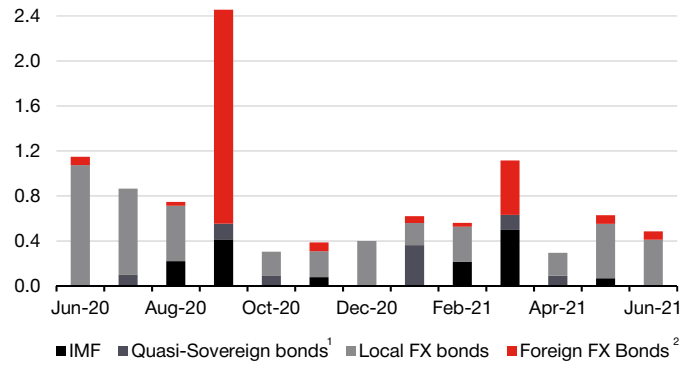
Source: Bloomberg, Adamant Capital estimates

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



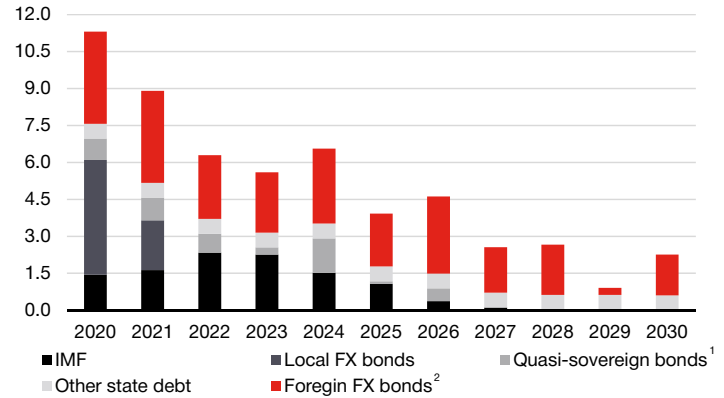
Source: Bloomberg, Adamant Capital estimates

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



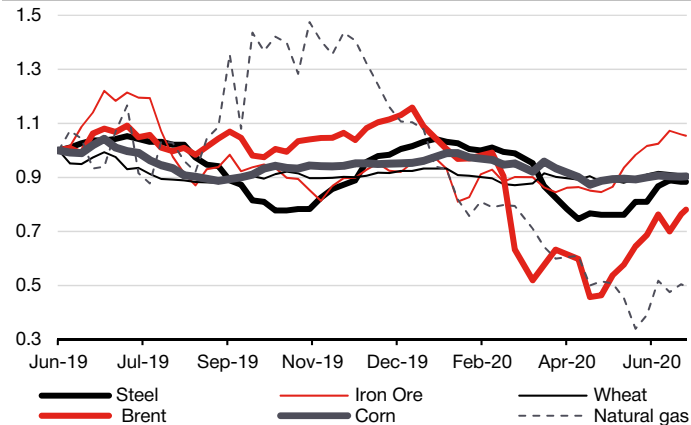
Note: Interest included in each category
(1) Debt of state owned enterprises
(2) Includes USAID guarantees
Source: Bloomberg, Adamant Capital estimates

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



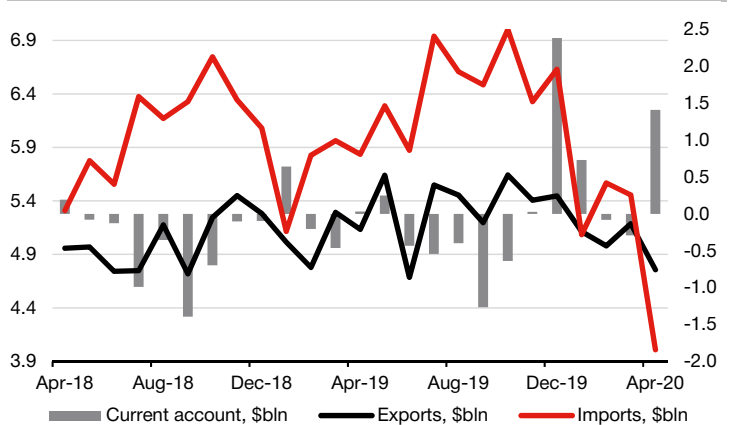
(1) Debt of state owned enterprises
(2) Includes USAID guarantees
Source: Bloomberg, Adamant Capital estimates

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); Brent Crude Oil Futures; Corn Futures (Black Sea); Dutch TTF Gas Futures
Source: Bloomberg, Adamant Capital estimates

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



Source: NBU

Key macroeconomic indicators								
	1Q19	2Q19	3Q19	4Q19	2019	1Q20	2Q20E	2020E
Real GDP growth, YoY	2.9%	4.7%	3.9%	1.5%	3.2%	-1.3%	-9.0%	-3.5%
Nominal GDP, UAHbln	815	933	1,112	1,115	3,975	846	870	3,989
Nominal GDP, \$bln	30	35	44	46	154	34	33	151
GDP deflator growth YoY, %	12.2%	9.9%	7.6%	4.7%	8.1%	5.1%	2.5%	4.0%
Period average CPI YoY, %	8.9%	9.1%	8.5%	5.2%	7.9%	2.6%	1.9%	2.6%
End of period CPI YoY, %	8.6%	9.0%	7.5%	4.1%	4.1%	2.3%	2.1%	4.0%
Consolidated budget deficit, % of GDP ¹	2.0%	2.5%	2.4%	2.1%	2.1%	2.3%	3.8%	4.5%
Broad public sector deficit, % of GDP ²	2.3%	2.7%	2.5%	2.1%	2.2%	2.3%	4.2%	5.3%
Public debt as % of LTM GDP, UAH	58.5%	55.4%	51.1%	50.3%	50.3%	56.3%	57.3%	60.0%
Public external debt as % of LTM GDP, \$ ³	37.4%	36.0%	32.9%	31.6%	31.6%	31.6%	31.7%	35.8%
Total external debt, \$bln	114	116	118	122	122	120	124	130
Export of goods and services, \$bln	15.1	15.5	16.3	16.5	63.4	15.3	13.5	60.5
Import of goods and services, \$bln	16.9	18.3	20.3	20.0	75.5	16.2	13.2	68.7
Trade balance, \$bln	-1.8	-2.8	-4.0	-3.5	-12.1	-0.9	0.3	-8.2
Current account, \$bln	-0.2	-0.5	-2.2	1.8	-1.1	0.2	2.1	-1.5
Financial account, \$bln ⁴	-0.5	-0.9	-3.8	-2.1	-7.3	0.4	-2.8	-5.2
End of period NBU reserves, \$bln	20.6	20.6	20.1	25.3	25.3	24.9	27.9	32.6
Average interbank exchange rate, UAH/\$ ⁵	27.3	26.6	25.2	24.2	25.8	25.2	26.7	26.5
EOP interbank exchange rate, UAH/\$	27.2	26.2	24.2	23.7	23.7	27.6	26.5	26.5
EOP key policy rate NBU, %	17.5%	17.5%	16.5%	13.5%	13.5%	10.0%	6.0%	5.0%

(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	6.1	104.8	-0.4	2.8	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	6.6	107.7	-0.8	3.1	750
Ukraine 2027	Hold	-	7.8	Sep-27	6.8	105.3	-0.4	5.6	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	7.3	115.3	-1.2	6.0	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	7.2	101.8	-1.4	7.8	3,000
Avangard in default	Sell	9-Apr-19	10.0	Oct-18	nm	4.4	0.6	nm	214
DTEK 2024 in default	Buy	9-Jun-20	10.8	Dec-24	29.8	58.9	0.0	2.9	1,344
Kernel 2022	Buy	2-Jun-20	8.8	Jan-22	6.6	103.1	-0.5	1.5	500
Kernel 2024	Buy	2-Jun-20	6.5	Oct-24	6.6	99.5	0.7	3.8	300
Metinvest 2023	Buy	2-Jun-20	7.8	Apr-23	8.1	99.2	1.3	2.5	505
Metinvest 2025 (EUR)	Buy	2-Jun-20	5.6	Jun-25	8.1	90.1	0.9	4.4	333
Metinvest 2026	Buy	2-Jun-20	8.5	Apr-26	9.0	97.7	2.3	4.6	648
Metinvest 2029	Buy	2-Jun-20	7.8	Oct-29	8.8	93.4	2.0	6.6	500
MHP 2024	Sell	2-Jun-20	7.8	May-24	6.5	104.2	0.9	3.4	500
MHP 2026	Sell	2-Jun-20	7.0	Apr-26	6.6	101.8	0.5	4.8	550
MHP 2029	Sell	2-Jun-20	6.25	Sep-29	6.9	95.3	0.9	7.0	350
Naftogaz 2022	Buy	9-Jun-20	7.4	Jul-22	7.8	99.2	-0.1	1.9	335
Naftogaz 2024 (EUR)	Buy	9-Jun-20	7.1	Jul-24	7.8	97.6	-0.1	3.4	672
Oschadbank 2023	Buy	16-Jun-20	9.4	Mar-23	7.7	102.3	-0.1	1.3	245
Oschadbank 2025	Buy	16-Jun-20	9.6	Mar-25	8.3	102.8	0.0	2.2	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	30.3	0.0	nm	175
Ukraine Railway 2021	Buy	5-May-20	9.9	Sep-21	9.4	100.3	-0.1	0.7	200
Ukraine Railway 2024	Buy	5-May-20	8.3	Jul-24	8.8	98.0	0.3	3.4	595
Ukreximbank 2021 (UAH)	Buy	16-Jun-20	16.5	Mar-21	15.3	100.7	4.0	0.6	150
Ukreximbank 2022	Buy	16-Jun-20	9.6	Apr-22	8.1	101.5	0.0	1.0	313
Ukreximbank 2025	Buy	16-Jun-20	9.8	Jan-25	9.1	100.9	0.0	1.5	600
Ukrlandfarming in default	Sell	13-Jun-17	10.9	Mar-18	nm	5.0	-0.2	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-Jun
Metinvest - Monthly report for April	Indicative	29-Jun
MHP - Non-financial Report FY 2019 (GRI Standard)	Exact	30-Jun
NBU - Balance of payments monthly data	Exact	30-Jun

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