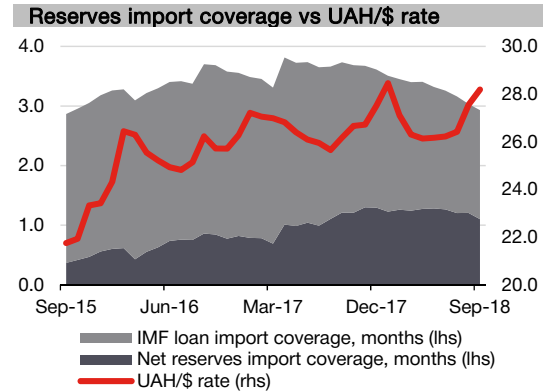


Weekly Digest

- Foreign currency reserves of the NBU in September decreased by \$0.6bln MoM to \$16.6bln
- Ferrexpo's 3Q18 pellet output increased by 6% QoQ to 2.7kt
- Ukrainian Railway's 1H18 EBITDA decreased by 18% YoY to \$269mln
- Metinvest's EBITDA in July decreased by 3% MoM to \$199mln

Foreign currency reserves of the NBU in September decreased by \$0.6bln MoM to \$16.6bln. Outflows came on the back of \$0.7bln of state debt interest and amortization payments. Inflows were caused primarily by the regulator's net interventions worth of \$53mln, local FX bond placements by the government that raised \$49mln and a \$14mln gain on revaluation of financial instruments.

Our view: This month's figure came fully in line with our expectations, having decreased largely on the back of substantial interest and amortization payments made by the state. The sum of net local FX bond placement and NBU interventions amounted to zero, suggesting that the private sector's BoP result was neutral, which is in line with our annual guidance for this indicator. Taking into account the lack of clarity on Ukraine's agreement with the IMF, we base our end-of-year reserves forecast on two scenarios. According to the positive one, which estimates the figure at \$19.5bln, authorities will reach a consensus with the Fund over the next few weeks and thus receive a \$2.0bln tranche from the IMF, EUR0.5bln from the EU, 0.5bln from the World Bank and raise \$1.0bln net via Eurobond placements. The alternative envisions a standstill in negotiations until December, which locks up all sources of external funding, leading to much more conservative estimate of \$15.4bln. Weighing both possibilities equally yields our adopted forecast of \$17.4bln. We note additionally that reserves have dropped below 3.0x average monthly imports for the first time in three years, which increases the probability of negative sentiment settling in the local FX market, in our view.



Source: NBU, Adamant Capital estimates

Ferrexpo's 3Q18 pellet output increased by 6% QoQ to 2.7kt. The share of higher quality 65% Fe produce has rebound back to 94% of the total volume. The 62% Fe CFR China price index grew by 2% QoQ to \$66/t.

Our view: The QoQ production boost came in line with expectations and reflects a low base effect created by the 65-day refurbishment program of one of Ferrexpo's facilities. As mentioned earlier, we expect output over 2H18 to land at 5.3mlnt, which should allow the company to sell c. 10.2mlnt of ore in total for the year (practically flat YoY). Taking into account current market prices and pellet premium estimates (c. \$60/t for the latter), we increase our FY18 EBITDA guidance by 8% to \$485mln (\$260mln for 2H18). Despite excellent credit metrics (forward looking leverage at just 0.3x), however, the recent appreciation of Ferrexpo's eurobonds leads us to downgrade our recommendation to a 'Hold' (yield discount to the sovereign curve stands at 100bps).

Ferrexpo 3Q18 pellet production summary, kt

	3Q18	2Q18	1Q18	4Q17	3Q17
Pellet production	2,660	2,511	2,585	2,791	2,493
QoQ	6%	-3%	-7%	12%	-2%
YoY	7%	-1%	-1%	-3%	-4%
Share of 65% Fe	94%	93%	94%	95%	94%
62% Fe ore price ¹ , \$/t	66	65	74	65	71
QoQ	2%	-12%	13%	-8%	13%
YoY	-6%	4%	-12%	-6%	23%

(1) The 62% CFR China Iron Ore price index

Source: Company data, Bloomberg, Adamant Capital estimates

Ukrainian Railway's 1H18 EBITDA decreased by 18% YoY to \$269m. The change in contributions of the cargo, passenger, and other business segments amounted to +\$30m, -\$54m, and -\$36m, respectively. Net income landed practically at breakeven (margin at 1%), as D&A and interest ate away at operating profits. OCF was down by 32% YoY due to a simultaneous injection of working capital (which remains negative). Free cash flow fell to -\$54m on the back of \$274m in capex. The company's net debt to LTM EBITDA stood unchanged at 1.6x.

Our view: The Railway's EBITDA underperformed our projections by c. 32% on the back of higher than expected running costs that stemmed from a 33% bump to average wages (represent 50% of the company's total COGS), lower than anticipated cargo turnover, a delay in the previously planned increase of passenger transportation tariffs (occurred in June instead of April), and relatively weak performance of the 'auxiliary' ('other') segment. Updating our model for the above differences yields a full year EBITDA figure of just \$600m, which stands 33% below our previous estimate and 23% below the management's budget plan. Despite the negative outlook on earnings, however, we do not expect leverage to spin out of control, as the initially announced capex guidance of \$1.0bn (which would have required extra borrowing) seems to be delayed as well (just 27% of the designated annual amount spent in 1H18). Additionally, financial performance should even out going forward, in our view, as the margin on passenger transportation increases due to an extra pricing hike in October. All in all, our recommendation on Ukrainian Railway's eurobonds remains at a 'Buy', taking into account the massive (c. 250bps) yield premium to the sovereign curve, which seems inappropriate for a state-owned company.

Ukrainian Railway 1H18 results summary, \$m

	1H18	1H17	YoY	2H17	HoH
Revenue	1,527	1,318	16%	1,463	4%
Adjusted EBITDA ¹	269	329	-18%	451	-40%
Cargo	518	488	6%	556	-7%
Passenger	-162	-108	nm	-110	nm
Other	-87	-51	nm	5	nm
Adj. EBITDA margin	18%	25%	-7pp	31%	-13pp
D&A	-266	-287	nm	-264	nm
FX gain/loss	88	53	65%	-97	nm
Net profit	18	5	291%	0	nm
Net profit margin	1%	0%	1pp	0%	1pp
Operating cash flow	220	321	-32%	335	-34%
Capex	274	164	67%	245	12%
Free cash flow	-54	157	-135%	90	-161%
Cargo segment					
Turnover, bn tkm	92.3	94.9	-3%	97.0	-5%
Tariff, UAH/tkm	0.35	0.31	16%	0.32	11%
Tariff, c/tkm	1.36	1.14	19%	1.21	12%
EBITDA/tkm, c	0.56	0.51	9%	0.57	-2%
Passenger segment					
Turnover, bn pkm	14.5	13.8	5%	14.2	2%
Tariff, UAH/pkm	0.26	0.25	4%	0.28	-7%
Tariff, c/pkm	0.98	0.92	7%	1.04	-6%
EBITDA/pkm, c	-1.12	-0.78	nm	-0.77	nm
Net debt	1,132	1,222	-7%	1,035	9%
Net debt/LTM EBITDA ¹	1.58	1.60	-1%	1.41	12%

Note: c stands for US dollar cents

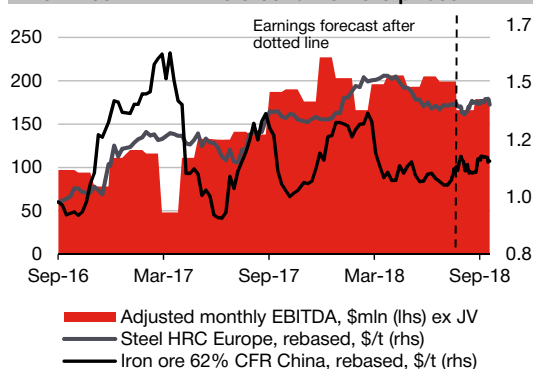
(1) EBITDA adjusted for revaluation and asset impairment

Source: Company data, SSSU, Adamant Capital estimates

Metinvest's EBITDA in July decreased by 3% MoM to \$199m (excluding JVs). Contribution of the mining segment was up by 16% on the back of a 4% bump to the average realized price (despite the 62% Fe CFR China benchmark remaining flat). Metals profits were down by 11%, as turnover volumes, excluding resales, slipped by a similar amount (likely due to one-off factors). Eliminations contributed an unusually high \$32m to the total (typically occurs at the end of a financial quarter). Operating cash flows came in at a record \$313m on the back of an \$126m release of working capital. Capex stood at \$60m. Period-end cash balances grew by 53% MoM, landing at \$566m.

Our view: July EBITDA came in 21% above our estimates primarily on the back of atypically sizeable eliminations (\$32m), which we expect to reverse in future periods and consider to be a one-off event. As production costs together with prices remain largely unchanged from our last review at the beginning of September, we still find our previously voiced annual EBITDA projection of \$2.1bn to be reasonable (the 3Q18 figure should stand at c. \$500m). Unless capex picks up significantly or working capital (at 15.5% of LTM revenues currently, which falls in between the 2016 and 2017 average) receives another sizeable injection, we continue to see potential for net debt to drop to c. \$1.9bn by December, which would bring leverage down to 0.8x. That said, despite fundamentals remaining solid, we retain a 'Hold' recommendation on Metinvest's notes, given their current yield spread to the sovereign curve of 80-90bps. Compared to Kernel, which trades at similar levels, Metinvest is exposed significantly more to commodity price fluctuations, is less transparent, and carries higher corporate governance risks.

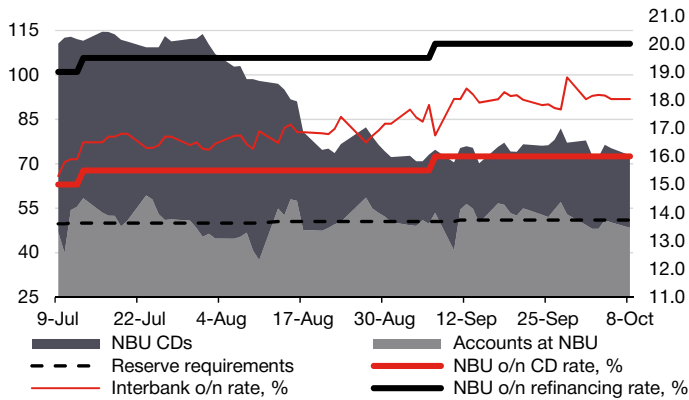
Metinvest EBITDA vs steel & iron ore prices



Source: company data, Bloomberg, Adamant Capital estimates

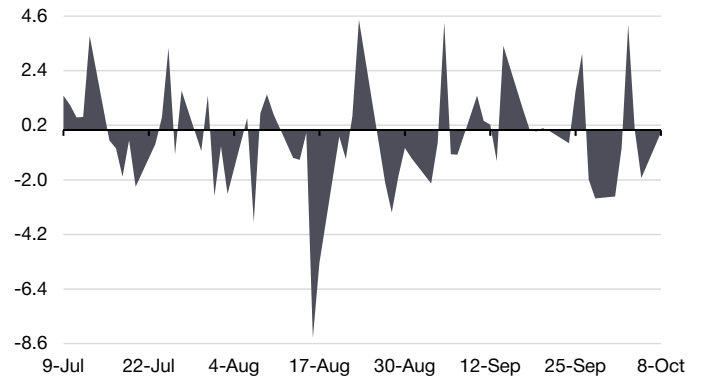
Appendix

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



Source: NBU, Adamant Capital estimates

Banking system inflows from the state treasury and the DGF

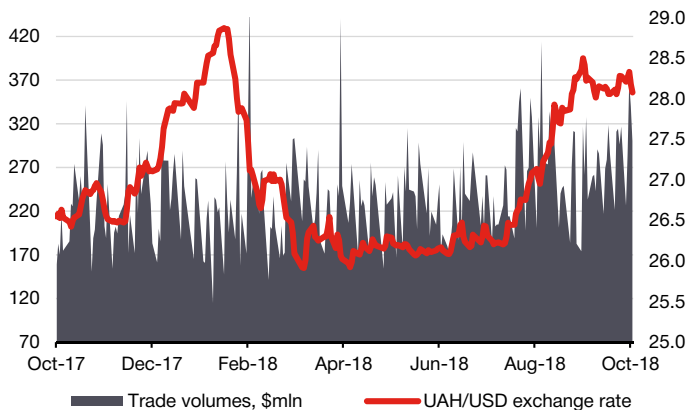


Note: in UAHbln
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has decreased by UAH 5.0bln to UAH 72.8bln over the last week. On October 9 the Ministry of Finance conducted local hryvnia denominated placement maturing in December 2018, April 2019, July 2019 and April 2020 with yields of 19.0%, 18.5%, 18.5% and 18.5%, respectively, and USD denominated placement maturing in June 2019 and January 2020 with yields of 7.0% and 7.5%, respectively. Moreover, euro denominated notes yielding 4.6% and maturing in June 2019 were also sold. A total of UAH 1.5bln, \$127.2mln and EUR 30.0mln was raised as a result.

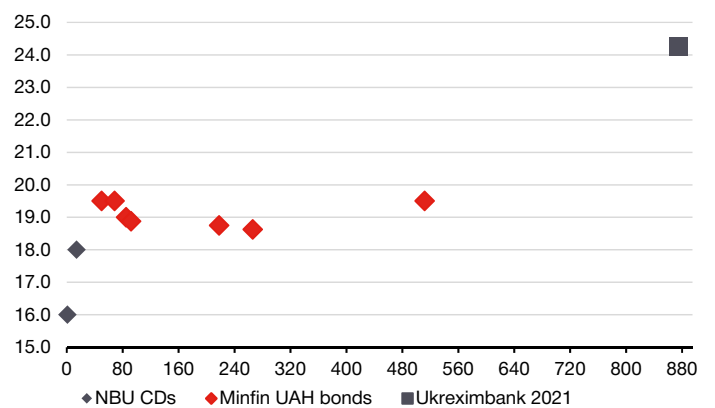
The UAH/USD interbank rate appreciated by 0.7% over the week starting out with 28.27 and ending at 28.08.

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

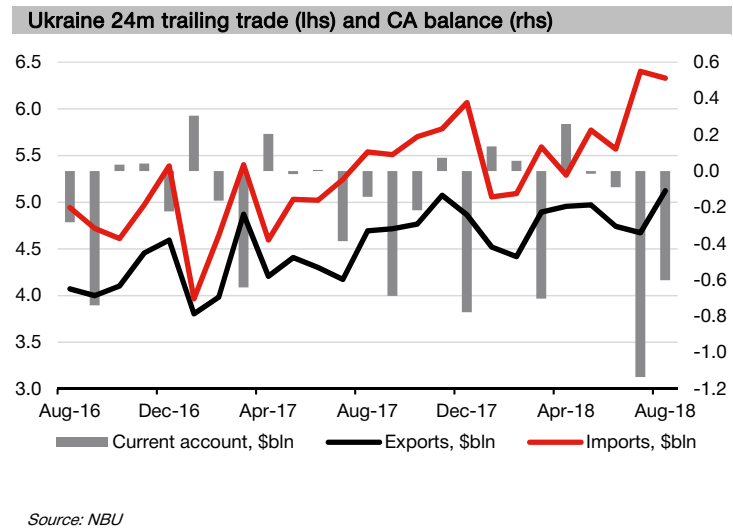
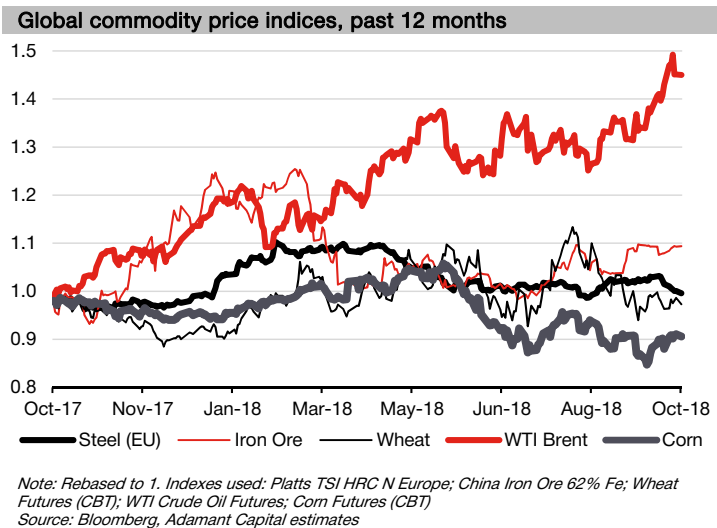
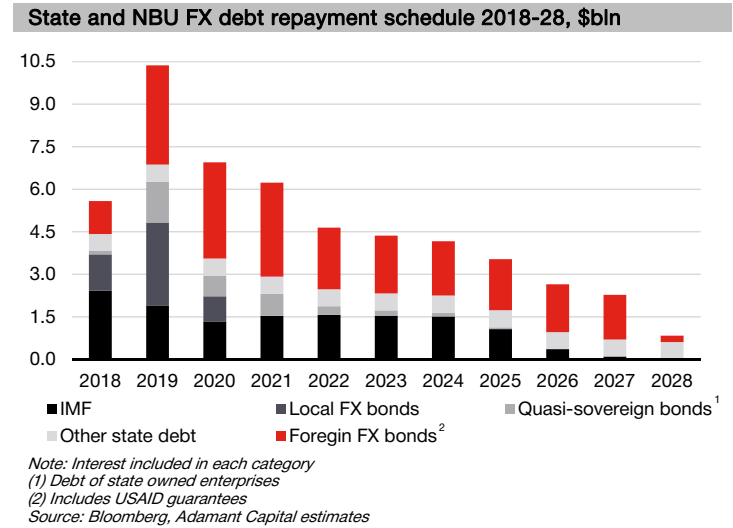
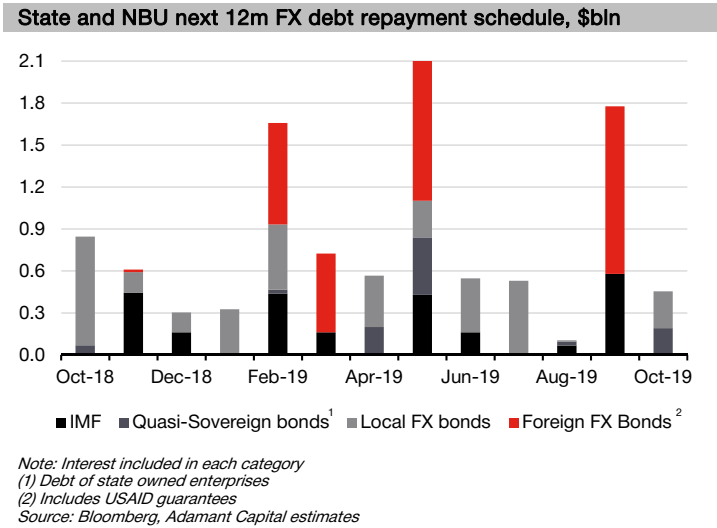
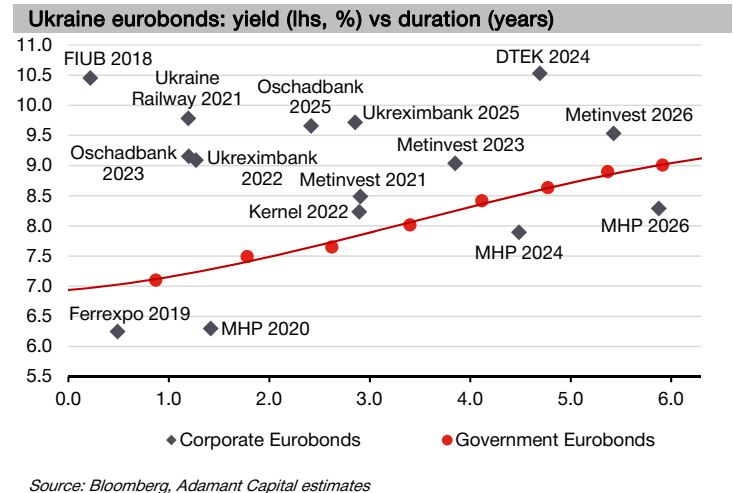
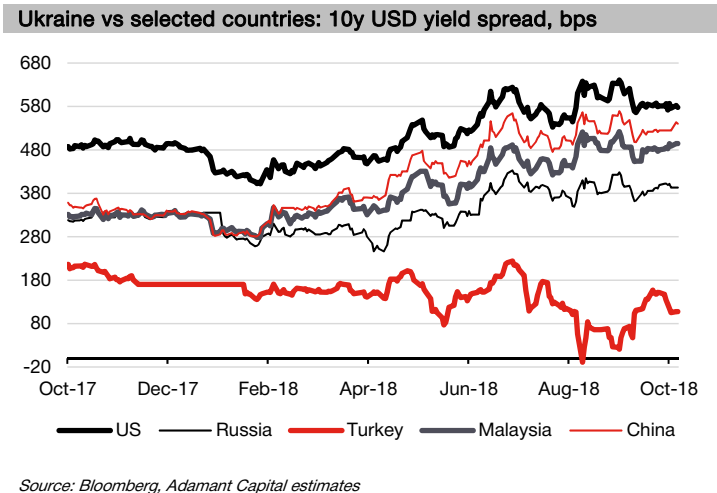


Note: Exchange rate figures are from official interbank data
Source: NBU

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



Source: NBU, Bloomberg, Adamant Capital estimates



Key macroeconomic indicators								
	1Q17	2Q17	3Q17	4Q17	2017	1Q18	2Q18E	2018E
Real GDP growth, YoY	2.8%	2.6%	2.4%	2.2%	2.5%	3.1%	3.8%	3.4%
Nominal GDP, UAHbln	591	665	833	894	2,983	700	807	3,543
Nominal GDP, \$bln	22	26	32	33	112	26	31	129
GDP deflator growth YoY, %	26.2%	20.9%	21.1%	20.9%	22.0%	14.9%	17.0%	14.9%
Period average CPI YoY, %	14.0%	13.8%	16.1%	14.0%	14.5%	13.8%	11.6%	11.5%
End of period CPI YoY, %	15.1%	15.6%	16.4%	13.7%	13.7%	13.2%	9.9%	9.5%
Consolidated budget deficit, % of GDP ¹	-0.7%	-7.2%	1.3%	9.4%	1.4%	0.4%	-1.6%	2.5%
Broad public sector deficit, % of GDP ²	3.8%	-7.2%	4.0%	12.7%	4.1%	0.4%	-1.2%	2.6%
Public debt as % of LTM GDP, UAH	77.4%	73.9%	72.7%	71.8%	71.8%	66.4%	61.8%	63.1%
Public external debt as % of LTM GDP, \$ ³	46.9%	47.4%	46.5%	43.7%	43.7%	41.7%	38.7%	38.9%
Total external debt, \$bln	114	115	116	115	115	115	114	117
Export of goods and services, \$bln	12.6	12.9	13.6	14.9	60.8	13.8	14.6	54.8
Import of goods and services, \$bln	13.7	14.2	15.9	17.0	54.0	15.7	16.6	65.1
Trade balance, \$bln	-1.1	-1.3	-2.3	-2.1	6.8	-1.9	-2.0	-10.3
Current account, \$bln	-0.8	-0.3	-1.7	-1.0	-3.8	-0.7	0.0	-3.5
Financial account, \$bln ⁴	-0.2	-1.9	-2.5	-1.7	-6.4	-0.4	-0.5	-3.5
End of period NBU reserves, \$bln	15.1	18.0	18.6	18.8	18.8	18.2	18.0	17.4
Average interbank exchange rate, UAH/\$ ⁵	27.1	26.0	25.9	26.9	26.6	27.3	26.2	27.5
EOP interbank exchange rate, UAH/\$	27.0	26.0	26.6	28.1	28.1	26.3	26.3	29.0
EOP key policy rate NBU, %	14.0%	12.5%	12.5%	14.5%	14.5%	17.0%	17.0%	19.0%

(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 2019 (bullet)	Not rated	-	0.0	Feb-19	10.2	96.3	0.0	0.4	725
Ukraine 2019	Hold	1-Dec-16	7.8	Sep-19	7.1	100.5	-0.1	0.9	661
Ukraine 2023	Hold	1-Dec-16	7.8	Sep-23	8.4	97.4	-0.4	4.1	1,355
Ukraine 2027	Hold	1-Dec-16	7.8	Sep-27	9.1	91.9	-0.7	6.4	1,307
Ukraine 2032	Hold	1-Dec-16	7.4	Sep-32	9.3	85.2	-1.0	8.2	3,000
MHP 2024	Hold	24-Jul-18	7.8	May-24	7.9	99.4	-0.5	4.5	500
MHP 2026	Hold	24-Jul-18	7.0	Apr-26	8.3	92.7	-0.4	5.9	550
DTEK 2024	Buy	25-Sep-18	10.8	Dec-24	10.5	101.2	0.4	4.7	1,344
Ferrexpo 2019	Hold	9-Oct-18	10.4	Apr-19	6.2	102.0	-0.2	0.5	346
Metinvest 2023	Hold	9-Oct-18	7.8	Apr-23	9.0	95.3	-0.3	3.8	945
Metinvest 2026	Hold	9-Oct-18	8.5	Apr-26	9.5	94.5	-0.3	5.4	648
Ukrlandfarming 2018	Sell	13-Jun-17	10.9	Mar-18	nm	21.0	0.7	2.4	543
Avangard 2018	Sell	5-Jun-18	10.0	Oct-18	nm	20.5	0.1	0.1	214
FUIB 2018	Buy	7-Aug-18	11.0	Dec-18	10.5	100.1	-0.7	0.2	59
Privatbank in default (10.250)	Not rated	7-Aug-18	10.3	Jan-18	nm	22.1	-0.3	2.7	160
Privatbank in default (10.875)	Not rated	7-Aug-18	10.9	Feb-18	nm	22.4	0.0	2.6	175
Oschadbank 2023	Buy	7-Aug-18	9.4	Mar-23	9.2	100.8	-0.1	1.2	700
Oschadbank 2025	Buy	7-Aug-18	9.6	Mar-25	9.7	99.8	-0.2	2.4	500
Ukreximbank 2021 (UAH)	Buy	7-Aug-18	16.5	Mar-21	25.4	84.7	-0.7	2.0	150
Ukreximbank 2022	Buy	7-Aug-18	9.6	Apr-22	9.1	101.6	-0.1	1.3	750
Ukreximbank 2025	Buy	7-Aug-18	9.8	Jan-25	9.7	100.1	-0.2	2.9	600
Ukrainian Railway 2021	Buy	9-Oct-18	9.9	Sep-21	9.8	100.2	-0.3	1.2	500
Mriya 2018	Hold	19-Jun-18	9.5	Apr-18	nm	7.1	-0.6	1.3	400
Kernel 2022	Buy	17-Jul-18	8.8	Jan-22	8.2	101.4	-0.2	2.9	500

Source: Bloomberg, Adamant Capital estimates

Fixed Income 2 week event calendar		
Event	Type	Date
SSSU - Agricultural production monthly data	Exact	17-Oct
MHP - Pre-close trading update for Q3 2018	Exact	18-Oct
Kernel - FY 2018 Financial Report	Exact	22-Oct
SSSU - Wholesale and retail turnover monthly data	Exact	22-Oct
SSSU - Transportation monthly data	Exact	22-Oct
SSSU - Industrial production monthly data	Exact	23-Oct

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