

Weekly Digest

- The current account (CA) in September landed in deficit of \$875mln, while the financial account (FA) demonstrated a \$1.3bln surplus
- The NBU has decreased the discount rate by 1.0ppt to 14.0%
- Metinvest reported a 10% MoM decrease in August adjusted EBITDA
- DTEK has announced its preliminary Eurobond restructuring terms
- Ukraine's 9M16 consolidated budget and public sector broad deficit reached 2.0% and 3.2% of GDP

The current account (CA) in September landed in deficit of \$875mln, while the financial account (FA) demonstrated a \$1.3bln surplus.

Exports of goods and services declined by 1% MoM and 5% YoY, with the largest annual contractions occurring in sales of food, energy, and chemical products (oil and soft commodity prices were down by 11-22% over the period). Imports decreased by 3% MoM but were up by 7% YoY with machinery & vehicle purchases having the largest impact on both indicators (12m trailing machinery imports are up by 21% YoY; the recoil in September came on the back of fewer agricultural equipment shipments). The CA this month was also impacted by \$0.5bln worth of coupon payments on government Eurobonds. September's FA surplus was largely driven by the \$1.0bln bond placement guaranteed by the USAID and c. \$470mln worth of retail FX currency sales. We estimate the total outflow of external capital from the private sector at \$384mln.

Our view: Corrected for the coupon payment on government Eurobonds the CA deficit in September amounted \$375mln, out of which c. \$300mln were imports of natural gas. Assuming a similar trend going forward together with a 4Q16 gas import figure of c. 3.0bln m³ priced at \$200/m³ yields an annual CA deficit figure of \$2.4bln (includes a correction for updated monthly data), which we set as our new forecast. We retain our EOP reserves guidance at \$16.9bln due to a slightly more optimistic view on FA inflows (largely from retail FX currency sales).

The NBU has decreased the discount rate by 1.0ppt to 14.0%.

According to the press release, the change was made possible by relative price stability in September (CPI growth stood at 7.9% YoY), which implies few risks for the year-end inflation target of 12±3%.

Our view: The rate drop comes in line with our previous guidance and was likely enacted due to relative exchange rate stability in October (as lending is limited inflation is mostly imported). Despite the fact that the yield curve is normally shaped, we anticipate another 0.5-1.0ppt rate decrease to occur after the NBU Board Meeting on December 8.

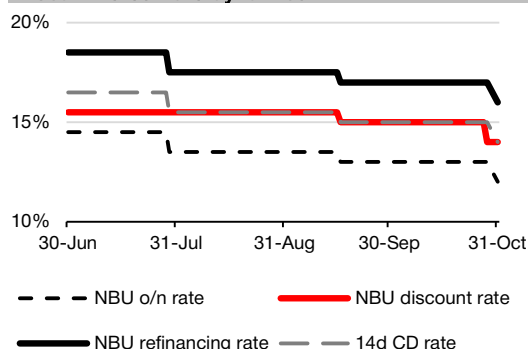
Ukraine September BoP summary, \$mln

	Sep-16	Sep-15	Sep-14	Sep-13	Sep-12
Exports:	3,989	4,211	5,231	7,083	7,558
MoM	-1%	6%	0%	-4%	-3%
YoY	-5%	-19%	-26%	-6%	3%
Imports:	4,579	4,281	5,953	9,397	8,335
MoM	-3%	3%	12%	7%	-6%
YoY	7%	-28%	-37%	13%	0%
TB:	-590	-70	-722	-2,314	-777
MoM	82	99	-615	-865	288
YoY	-520	652	1,592	-1,537	204
CA inflows:	-875	145	-840	-2,498	-1,141
MoM	-461	106	-737	-691	333
YoY	-1,020	985	1,658	-1,357	-59
FA inflows:	1,343	198	476	2,394	36
MoM	926	-268	419	792	-2,050
YoY	1,145	-278	-1,918	2,358	1,000
BoP inflows:	474	347	-360	-105	-1,103
MoM	458	-166	-318	127	-1,719
YoY	127	707	-255	998	939
Capital flow ¹ :	-384	195	177	739	818

(1) An estimate of the total amount of capital flowing into the country (includes IFI funding, except the IMF)

Source: NBU, Adamant Capital estimates

Local interest rate dynamics

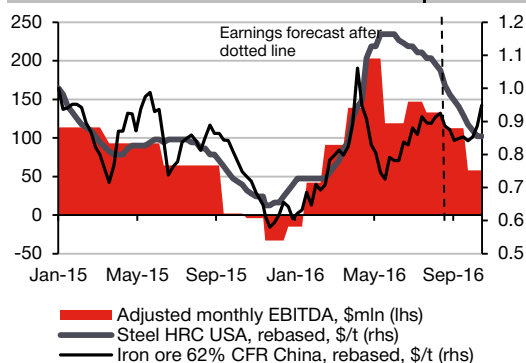


Source: NBU

Metinvest reported a 10% MoM decrease in August adjusted EBITDA. Including JVs, the figure dropped by \$20mln compared to July, landing at \$113mln. Operating cash flow grew by \$130mln to \$175mln (largely on the back of a \$64mln decrease in WC compared to a \$75mln increase last month), with free cash flow growing by \$131mln to \$153mln.

Our view: This month's decline in Metinvest's earnings came as somewhat of a surprise, as the company's average EBITDA per ton of steel contracted by substantially more than the average realized price (\$31 MoM vs \$16). Taking into account the continued decline in global price benchmarks, we reiterate our view on an upcoming earnings weakness for the issuer in 4Q16. Having said that, we still expect FY16 EBITDA to advance some 2.3x YoY to \$1.2bln, which should place the company's leverage coefficient at close to 2.0x. All in all, we currently retain our Buy recommendation on Metinvest's notes, expecting the market to reward a successful restructuring campaign, though note that the upside may be limited by poor financial performance that will start to become apparent already in the fourth quarter.

Metinvest EBITDA vs steel and iron ore prices



Note: EBITDA includes JVs; iron ore and steel prices; forecasted starting February 2016

Source: Company data, Bloomberg, Adamant Capital estimates

DTEK has announced its preliminary Eurobond restructuring terms.

According to the company's presentation the agreement reached with the noteholder steering committee includes (1) a merger of all current bonds into a single issue, 50% of which amortizes in December 2023 and the rest in December 2024, (2) a new coupon of 10.5%, that is paid partly in cash and partly via PIK, (3) a 1% restructuring fee with an additional early bird compensation of 25bps, and (4) clauses that limit maximum capex and dividend payment possibilities. DTEK has also published its forward looking business plan projection that guides for 2016 and 2017 EBITDA at \$553mln and \$791mln, respectively.

Our view: We calculate that assuming a discount rate of 15% (a 5% spread to the current yield of Ferrexpo and government bank bonds to account for dependence on favorable state regulation), the fair post restructuring value of DTEK's notes stands at 78% of par, which implies limited upside to the present market value and warrants a Hold recommendation. We remark, however, that the estimate is very sensitive to the discount rate assumption (setting it at 13% boosts the outcome to 87% of par) and that the market price may thus grow rapidly if risk perception declines. Finally, we note that our view on the issuer may improve if the management's newly disclosed 2016 EBITDA projection materializes (currently stands 20-30% above our forecasts).

Ukraine's 9M16 consolidated budget and public sector broad deficit reached 2.0% and 3.2% of GDP, respectively. Consolidated budget revenues have increased by 12% YoY to UAH525bln and have outpaced originally planned figures by 8%. Likewise, expenditures are up by 29% YoY to UAH557bln and have surpassed original guidance by 12%. Over the first nine months of the year the state has emitted UAH14.3bln of local debt in order to recapitalize government banks and provided UAH5.3bln worth of sovereign guarantees.

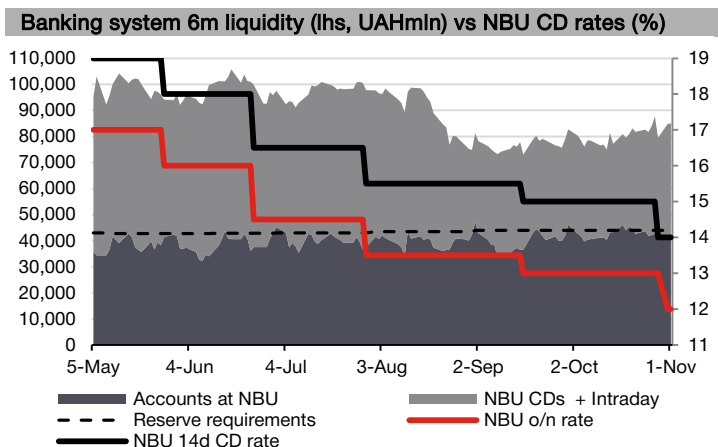
Our view: Public deficit figures look good on the whole, with no indicator surpassing quantitative performance criteria agreed upon with the IMF. State bank and DGF funding quota of up to UAH166bln has practically not been tapped. Somewhat concerning, however, is the current annual budget plan, which does breach the IMF guidance on deficit (UAH95bln excluding loans vs the fund's UAH85bln target), though this may be revised over the next few months.

Public sector budget performance, UAHbln					
	9M16	Plan	A/P	9M15	YoY
Revenues	525	488	8%	468	12%
VAT	168	164	2%	130	29%
Income tax on business	40	35	13%	32	27%
Excise tax	65	58	12%	45	44%
Personal income tax	98	73	33%	70	40%
Royalties	31	43	-28%	23	32%
Import duties	14	14	2%	27	-48%
Local taxes	30	17	79%	19	55%
Non-tax revenues	35	65	-46%	105	-67%
Expenditures	557	499	12%	433	29%
Debt servicing	77	71	7%	61	25%
General government	101	98	0%	82	23%
Defence	40	43	-6%	33	23%
Civil order and courts	45	42	8%	35	29%
Economic activity	36	36	0%	32	11%
Communal services	9	6	66%	7	29%
Healthcare	47	35	33%	45	3%
Education	88	70	0%	76	15%
Social protection	177	158	12%	110	61%
Other	14	11	22%	13	7%
Consolidated budget deficit	32			-35	
as % of GDP	2.0%			2.5%	
Naftogaz financing	0			30	
Bank recapitalization & DGF	14			29	
Guarantees given	5			0	
Broad public sector deficit	52			24	
as % of GDP	3.2%			1.7%	

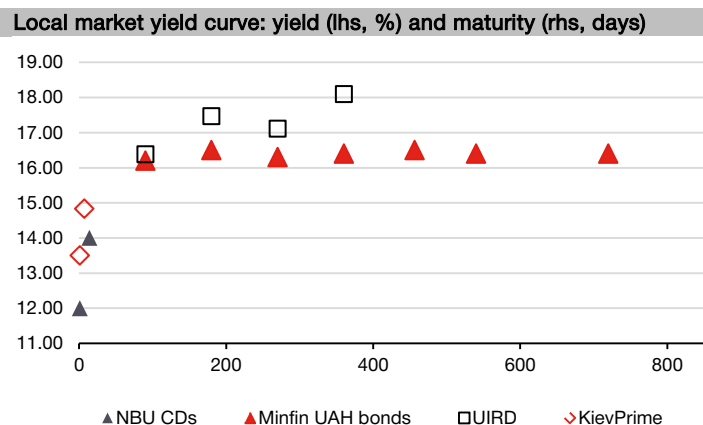
Notes: The broad public sector deficit includes the consolidated budget deficit, Naftogaz financing, Bank & DGF recapitalization, and state guarantees given

Source: Company data, Adamant Capital estimates

Appendix



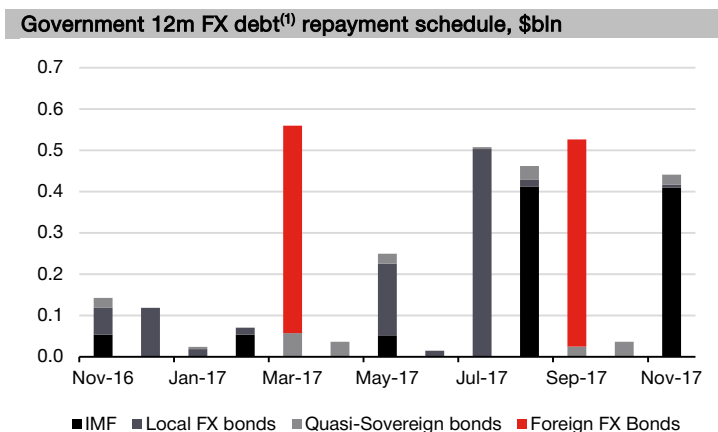
Source: NBU, Adamant Capital estimates



Source: NBU, Bloomberg, Adamant Capital estimates

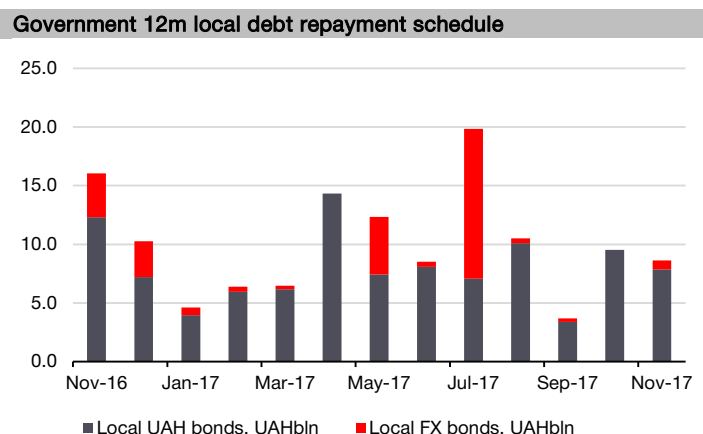
Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts, investment CDs, and other intraday changes) has increased by UAH3.4bln to UAH85.0bln over the last week. On November 1 the Ministry of Finance attempted to place local hryvnia bonds maturing in 2017 and 2021 with a yield of 15.20-16.10%, but placements were unsuccessful due to a lack of demands at the offered yields.

The UAH/USD interbank rate continued to strengthen over the week, starting out with 25.64 and closing at 25.51 (a 0.5% revaluation).



(1) Quasi-sovereign debt includes body and interest of state banks, Ukrzaliznytsya, and municipal bonds

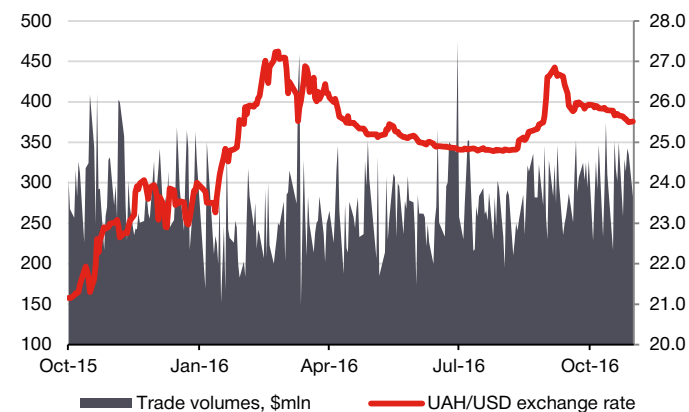
Source: Bloomberg, Adamant Capital estimates



Note: UAH/\$ exchange rate set at 25; EUR/USD exchange rate set at 1.13

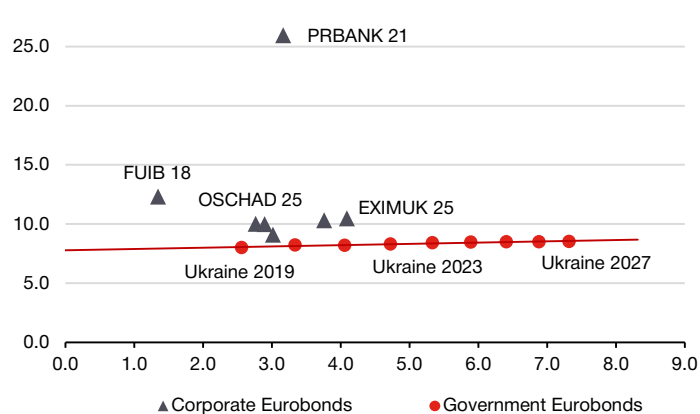
Source: Ministry of Finance

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



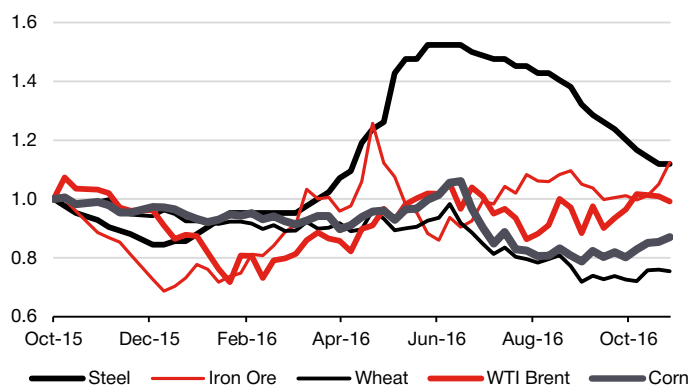
Note: Exchange rate figures are from official interbank data
Source: NBU

Eurobonds: yield (lhs, %) vs duration (years)



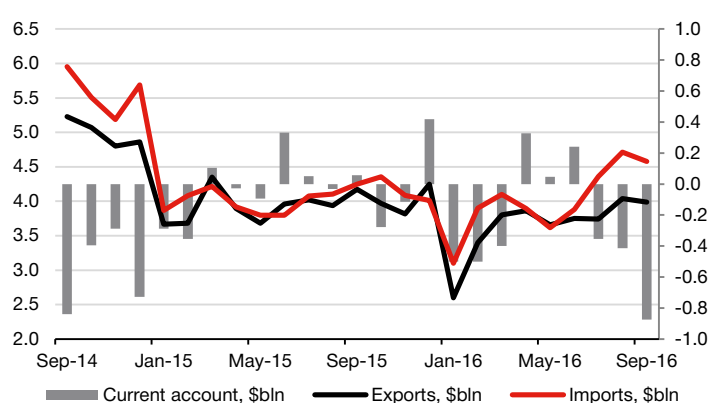
Source: Bloomberg, Adamant Capital estimates

Global commodity price indices, past 12 months



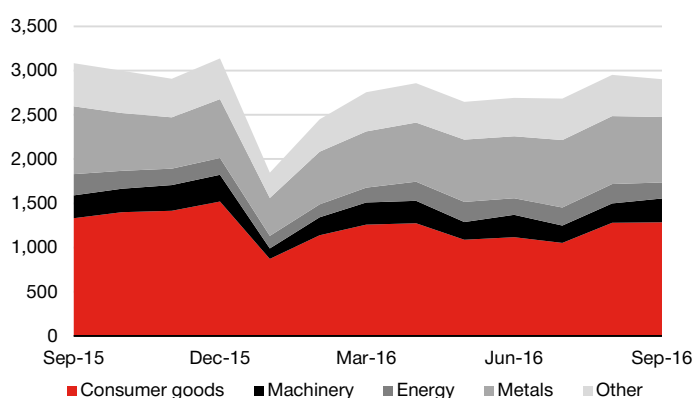
Source: Bloomberg, Adamant Capital estimates

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



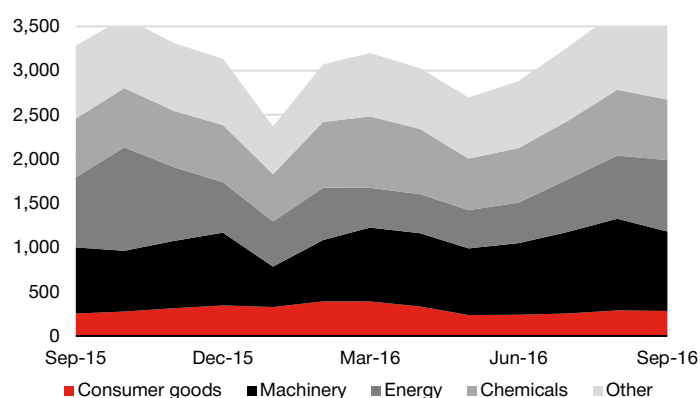
Source: NBU

Ukraine 12m trailing monthly export breakdown, \$mln



Source: NBU

Ukraine 12m trailing monthly import breakdown, \$mln



Source: NBU

Key macroeconomic indicators								
	2014	2Q15	3Q15	4Q15	2015	1Q16	2Q16	2016E
Real GDP growth, YoY	-1.6%	-14.7%	-7.2%	-1.4%	-9.9%	0.1%	1.3%	1.2%
Nominal GDP, UAHbln	1,567	455	564	585	1,979	453	532	2,273
Nominal GDP, \$bln	132	21	25	25	90	18	21	89
GDP deflator growth YoY ¹ , %	14.8%	42.0%	40.0%	33.9%	40.2%	20.5%	15.2%	13.3%
Period average CPI YoY, %	12.1%	58.9%	53.3%	45.4%	48.5%	31.3%	8.1%	13.3%
End of period CPI YoY, %	24.9%	57.5%	51.9%	43.3%	43.3%	20.9%	6.9%	8.9%
Budget deficit, % of nominal GDP ^{1,2}	-4.6%	-0.4%	3.6%	-10.8%	-1.6%	0.7%	-2.6%	-2.9%
Public sector broad deficit, % of GDP ³	-13.6%	-10.3%	1.7%	-10.8%	-5.8%	-2.5%	-2.6%	-3.7%
Public debt as % of nominal GDP, UAH	51.8%	84.2%	82.8%	79.4%	79.4%	56.2%	78.2%	78.0%
Public external debt as % of nominal GDP, \$ ⁴	30.7%	42.2%	49.2%	47.8%	47.8%	50.0%	49.4%	52.3%
Total external debt, \$bln	137.1	125.7	125.1	125.1	118.7	117.4	115.0	130.0
Export of goods and services, \$bln	68.5	11.6	12.3	12.2	47.8	9.8	11.3	43.1
Import of goods and services, \$bln	73.8	11.7	12.7	12.9	49.5	11.1	11.4	46.4
Trade balance, \$bln	-5.3	-0.1	-0.4	-0.7	-1.7	-1.3	-1.5	-4.6
Current account, \$bln	-5.3	0.3	0.2	-0.3	-0.2	-1.1	0.9	-2.2
Capital and Financial accounts, \$bln	8.0	-0.2	-1.0	-1.1	-0.6	0.3	0.3	2.2
End of period NBU reserves, \$bln	7.5	10.3	12.8	13.3	13.3	12.7	14.0	16.9
Average interbank exchange rate, UAH/\$ ⁵	11.9	21.8	22.4	22.9	21.9	25.8	25.2	25.6

(1) Quarterly figures use 12m trailing data

(2) Excludes any deficit not included in the official figure, but includes net budget loans given to state enterprises

(3) Estimated figures. Includes such below the line budget expenditures as recapitalization of Naftogaz and state banks, state guarantees given, etc

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

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

Source: NBU, SSSU, Minfin, IMF, Adamant Capital estimates

Indicative Eurobond prices, yields, and recommendations									
Bond name	Recommendation	Coupon	Maturity	Bid Yield	Bid Price	1 week Δ	Dur. yrs	Out. \$mln	Currency
Ukraine 2019	Hold	7.8	Sep-19	8.0	99.4	-1.0	2.6	1,743	USD
Ukraine 2023	Hold	7.8	Sep-23	8.4	96.7	-1.5	5.3	1,355	USD
Ukraine 2027	Hold	7.8	Sep-27	8.5	94.6	-1.6	7.3	1,307	USD
MHP 2020	Buy	8.3	Apr-20	9.1	97.6	-0.2	3.0	750	USD
DTEK 2018 (7.875)	Hold	7.9	Apr-18	nm	79.2	5.2	nm	793	USD
DTEK 2018 (10.375)	Hold	10.4	Mar-18	nm	78.2	3.3	nm	156	USD
Ferrexpo 2019	Sell	10.4	Apr-19	10.2	100.4	0.0	1.8	160	USD
Metinvest 2016	Buy	10.3	May-16	nm	86.1	1.4	nm	89	USD
Metinvest 2017	Buy	10.5	Nov-17	nm	85.5	2.0	nm	304	USD
Metinvest 2018	Buy	8.8	Feb-18	nm	84.8	1.3	nm	795	USD
Ukrlandfarming 2018	Sell	10.9	Mar-18	125.0	32.0	0.0	1.3	521	USD
Avangard 2018	Sell	10.0	Oct-18	109.7	23.3	0.0	1.8	213	USD
FUIB 2018	Hold	11.0	Dec-18	12.3	97.6	0.0	1.3	197	USD
Privatbank 2018 (10.250)	Hold	10.3	Jan-18	27.2	83.4	-2.2	0.7	160	USD
Privatbank 2018 (10.875)	Hold	10.9	Feb-18	26.9	83.0	-1.7	1.2	175	USD
Privatbank 2021	Hold	11.0	Feb-21	25.9	62.7	-0.4	3.2	220	USD
Oschadbank 2023	Buy	9.4	Mar-23	10.0	97.2	-0.3	2.8	700	USD
Oschadbank 2025	Buy	9.6	Mar-25	10.3	96.3	-0.3	3.8	500	USD
Ukreximbank 2022	Hold	9.6	Apr-22	10.0	98.5	-0.3	2.9	750	USD
Ukreximbank 2025	Hold	9.8	Jan-25	10.4	96.2	-0.4	4.1	600	USD
Ukrzaliznytsia 2021	Hold	9.9	Sep-21	10.9	96.1	-0.5	2.8	500	USD
Mriya 2018	n/a	9.5	Apr-18	nm	6.8	-0.1	nm	400	USD

Note: data as of November 1, 2016

Source: Bloomberg

Fixed Income 2 week event calendar		
Event	Type	Date
NBU - International reserves monthly data	Indicative	7-Nov
SSSU - Monthly inflation	Exact	8-Nov
SSSU - Quarterly GDP preliminary estimate	Exact	14-Nov
SSSU - Agricultural production monthly data	Exact	15-Nov
MHP - Q3 and 9M 2016 financial results	Exact	16-Nov

Source: NBU, SSSU, Adamant Capital estimates, company data

Contacts

Adamant Capital

5-B Volodymyrska Street, 2nd floor
01001 Kyiv, Ukraine
+380 44 585 52 36

Portfolio Management

Konstantin Viushynskyi | vka@adamant-capital.com
Yuriy Sozinov | urs@adamant-capital.com

Research

Konstantin Fastovets | fks@adamant-capital.com

PR

Inna Zvyagintseva | zin@adamant-capital.com

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