

Weekly Digest

- The parliament may vote on a new NBU head on July 17
- Consumer inflation in June amounted to 2.4% YoY and 0.2% MoM
- Ukraine's Constitutional Court has prolonged its hearing on DGF legitimacy

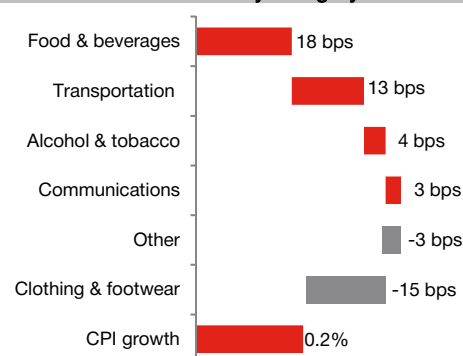
The parliament may vote on a new NBU head on July 17. Such estimates were provided by a number of MPs from Zelensky's political party Sluha Narodu to local media. Although very little clarity is currently present with regard to the lead candidate, names that have been circulated around by different sources include Bohdan Danylyshyn (currently in the NBU Council), Volodymyr Lavrenchuk (former head of Reiffeisen Bank's Ukraine division), Olena Scherbakova (also in the NBU Council), Artem Shevchuk (an alternate director at the EBRD and supervisory board member of both Privatbank and Ukrgasbank), and Kyrylo Shevchenko (the CEO of Ukrgasbank).

Our view: Of the abovementioned candidates, we favor Volodymyr Lavrenchuk, who is a professional with no ties to any of the political parties and Artem Shevaljev, who possesses similar qualities and has also briefly served as a Deputy Minister of Finance to the reform-oriented Natalie Yaresko back in 2015. Given the rift in views on monetary policy with the current NBU Board, we find both of the current Council members to be a poor fit for the role (fiscal dominance and uncontrolled hryvnia printing are clear risks). Shevchenko seems relatively independent, but as he spent most of his time working for inefficient state-owned companies that are notorious for corruption issues, we believe him to be quite unpredictable. On the whole, while the nature of Smoliy's departure together with signs of political pressure do imply that the new central bank head will need to demonstrate a higher degree of loyalty to Zelensky, the currently rumored list of candidates and the fact that Ukraine needs to continue to cooperate with external donors, leaves room for the possibility that the regulator's independence will end up being preserved.

Consumer inflation in June amounted to 2.4% YoY and 0.2% MoM. Food and transportation stood as the key items contributing to a positive CPI relative to May (impact of 18 and 13bps, respectively). Prices declined primarily for clothing & footwear, owing largely to seasonal trends.

Our view: Headline CPI came in practically on par with expectations. Compared to last year, largest differences in MoM price moves were demonstrated by eggs (flat vs a 10% decline), which completely defied historical trends, and vegetables (just -5% vs -15% previously), possibly reflecting lower domestic harvest volumes. Globally, food indexes moved ahead for the first time since the beginning of the COVID-19 pandemic (up 2.4% MoM, as calculated by FAO), which provides grounds for mild inflation shocks in the near term. Over the next six months, however, we believe loose monetary policy and record budget expenditures to be key factors that will push the CPI to 4.5% YoY by December. The recent resignation of the NBU head Smoliy further increases the upside risks to this projection, in our view, as a more politically dependent regulator is more likely to flood the banking system with extra hryvnia liquidity. We anticipate July inflation to land at 2.6% YoY.

MoM CPI contributions by category



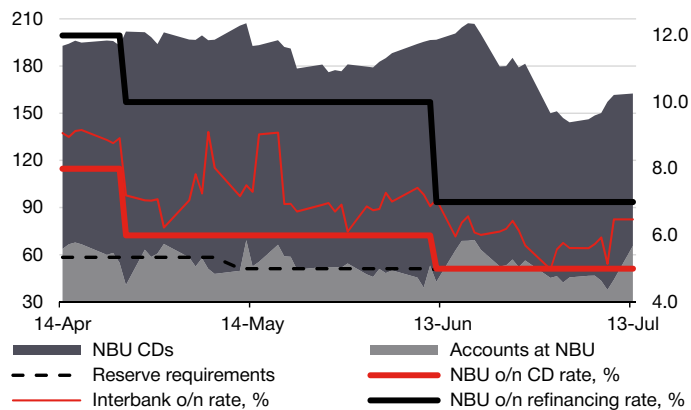
Source: SSSU, Adamant Capital estimates

Ukraine's Constitutional Court has prolonged its hearing on DGF legitimacy. According to local mass media, the process will now essentially restart and involve open discussions. The status of the Deposit Guarantee Fund has been originally called into question back in 2016, when the country's Supreme Court decided that it cannot rule in a case that involves the institution, as its legal standing as a government body has not been clearly defined. The DGF played a central role in liquidating over 100 banks with dubious business practices since 2013. It was also heavily involved in the nationalization process of Privatbank.

Our view: The decision to prolong the hearing and to transform the discussion into an open debate is very much a positive outcome, as a ruling that would have declared the DGF unconstitutional could have had catastrophic consequences not only for Privatbank, but also for the financial system as a whole (the entire post-2014 bank cleanup process could have been called into question). Over the past few years the Constitutional court has demonstrated time and again how Ukraine's poorly functioning legal system can lead to systemic shocks. In 2019 one of its rulings led to the annulment of a landmark law on illicit enrichment, which essentially created a loophole to end numerous anti-corruption proceedings. In a similar vein, a claim regarding the legality of the appointment of the NABU head Sytnyk back in 2015 is now being reviewed. The Constitutional court will also provide its opinion on the so-called Bank Law, which was a pre-requisite for the current IMF program. In case of a negative outcome, Ukraine's cooperation with external donors can be substantially undermined.

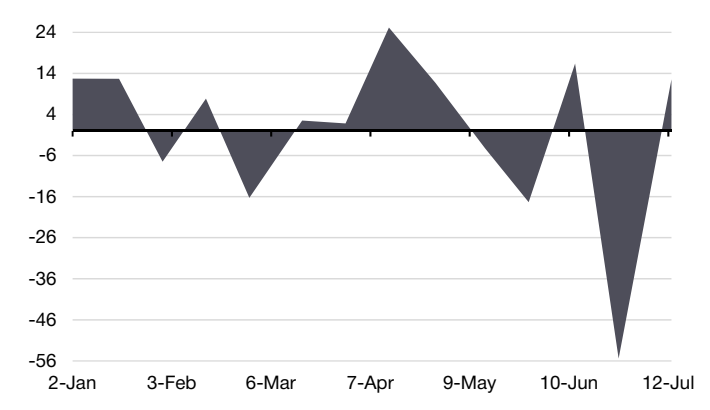
Appendix

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

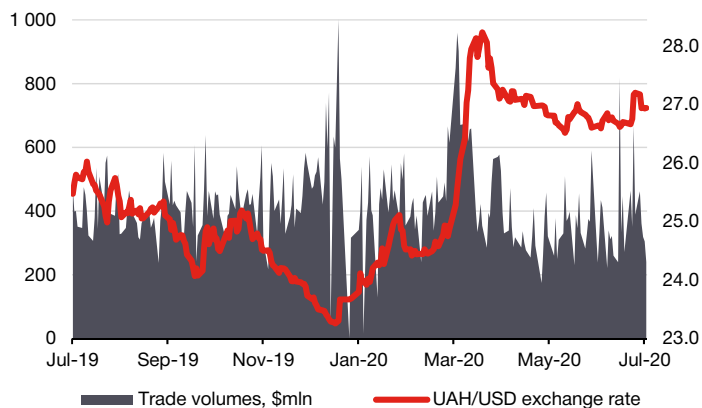


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has increased by UAH 16.3bln to UAH 162.5bln over the last week. On July 14 the Ministry of Finance conducted local hryvnia denominated placement maturing in September 2020, June 2021 and February 2023 with yields of 7.00%, 9.20% and 10.00% respectively and USD denominated placement maturing in June 2021 with yield of 3.50%. A total of UAH 10.6mln and \$306mln was raised as a result.

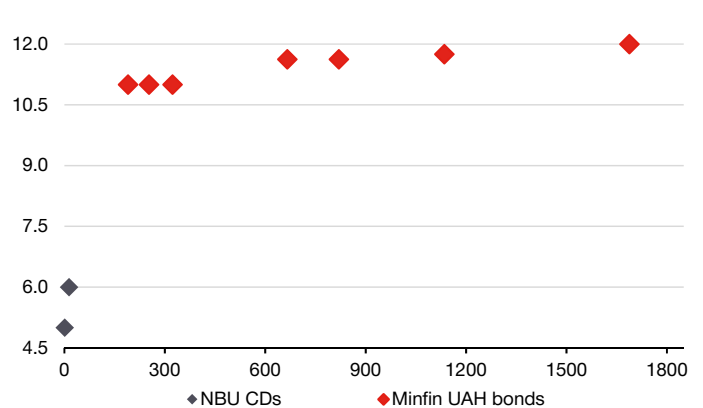
The UAH/USD interbank rate over the last week appreciated by 0.32%, starting out with 27.17 and ending at 27.09.

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

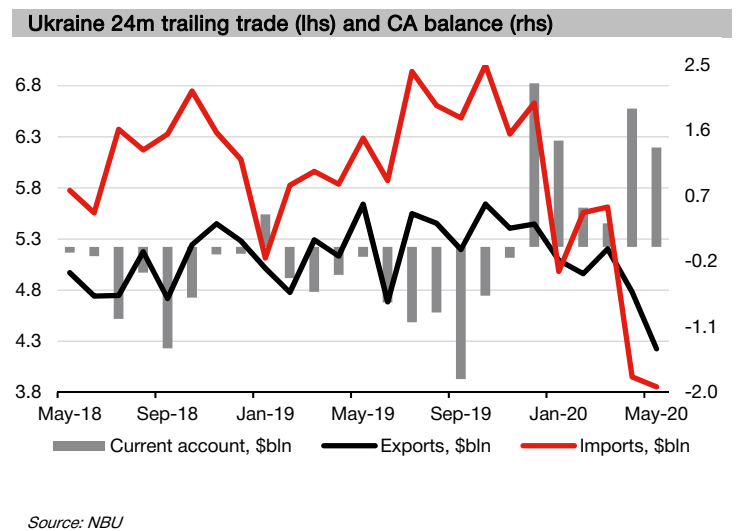
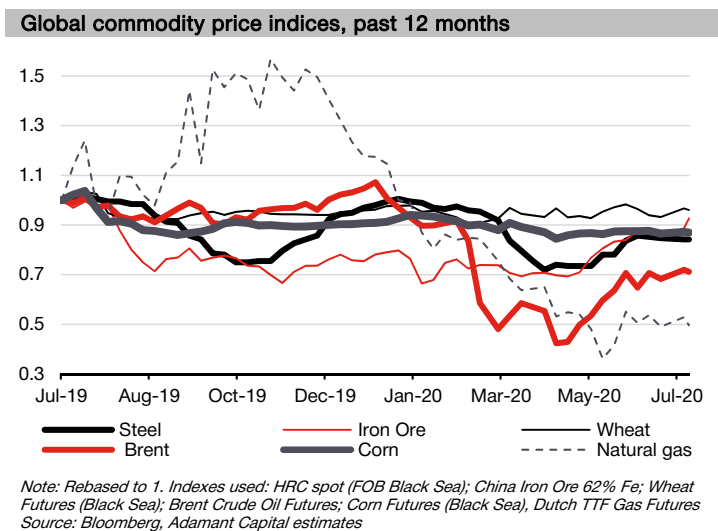
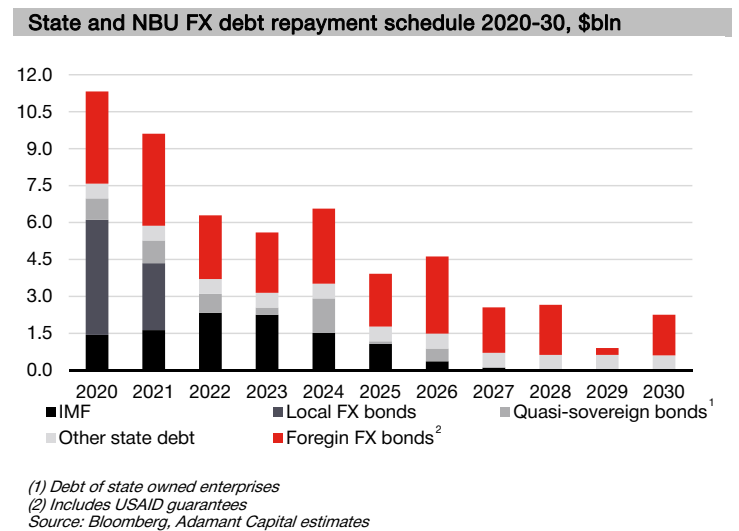
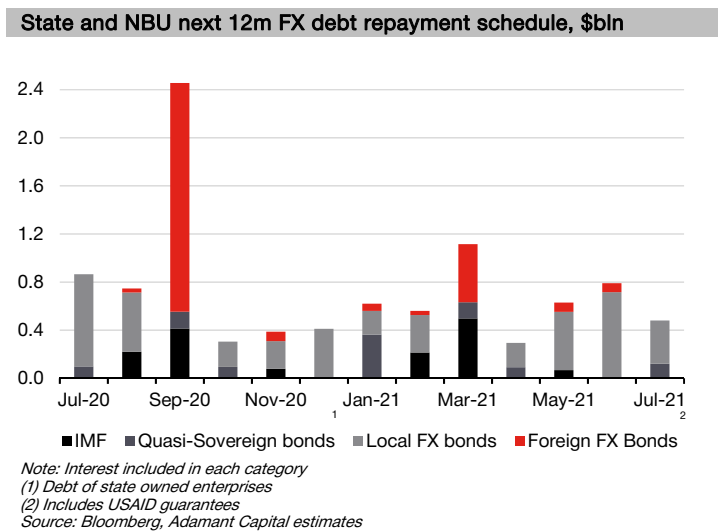
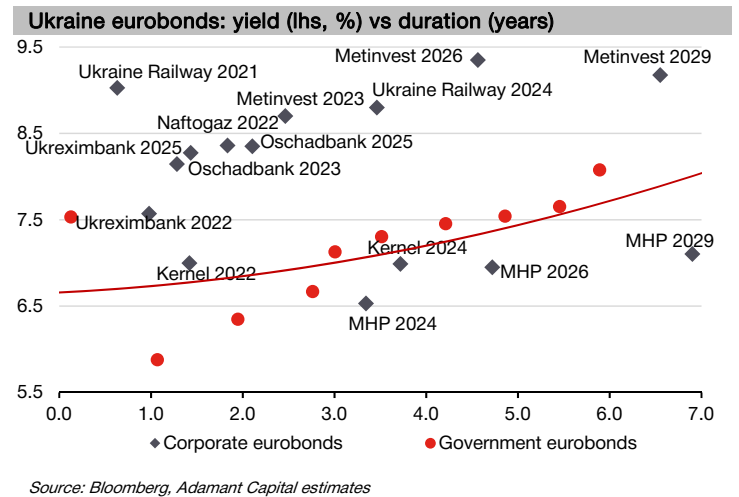
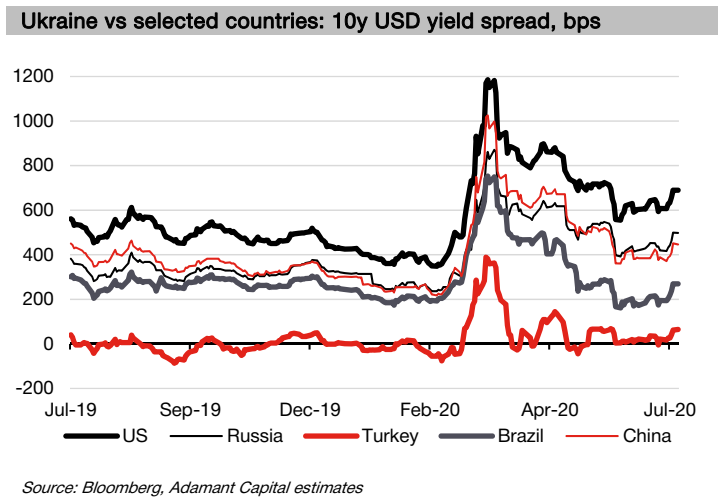


Note: Exchange rate figures are from official interbank data
Source: NBU

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



Source: NBU, Bloomberg, Adamant Capital estimates



Key macroeconomic indicators								
	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	32	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%	2.1%	2.8%
End of period CPI YoY, %	8.6%	9.0%	7.5%	4.1%	4.1%	2.3%	2.4%	4.5%
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	13.1	59.6
Import of goods and services, \$bln	16.9	18.3	20.3	20.0	75.5	16.2	12.2	64.4
Trade balance, \$bln	-1.8	-2.8	-4.0	-3.5	-12.1	-0.9	0.9	-4.8
Current account, \$bln	-0.2	-0.5	-2.2	1.8	-1.1	0.2	3.9	6.4
Financial account, \$bln ⁴	-0.5	-0.9	-3.8	-2.1	-7.3	0.4	-1.6	4.0
End of period NBU reserves, \$bln	20.6	20.6	20.1	25.3	25.3	24.9	28.5	31.3
Average interbank exchange rate, UAH/\$ ⁵	27.3	26.6	25.2	24.2	25.8	25.2	26.9	26.5
EOP interbank exchange rate, UAH/\$	27.2	26.2	24.2	23.7	23.7	27.6	26.7	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	6.7	103.0	-1.9	2.8	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	7.1	105.7	-2.3	3.0	750
Ukraine 2027	Hold	-	7.8	Sep-27	7.7	100.5	-3.7	5.5	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	8.1	110.0	-4.2	5.9	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	7.9	95.9	-4.3	7.7	3,000
Avangard in default	Sell	9-Apr-19	10.0	Oct-18	nm	4.2	0.0	nm	214
DTEK 2024 in default	Buy	9-Jun-20	10.8	Dec-24	30.4	56.3	-2.5	2.9	1,344
Kernel 2022	Buy	2-Jun-20	8.8	Jan-22	7.0	102.5	-0.2	1.4	500
Kernel 2024	Buy	2-Jun-20	6.5	Oct-24	7.0	98.2	-0.3	3.7	300
Metinvest 2023	Hold	7-Jul-20	7.8	Apr-23	8.7	97.7	-1.3	2.5	505
Metinvest 2025 (EUR)	Hold	7-Jul-20	5.6	Jun-25	8.3	89.2	-0.8	4.3	333
Metinvest 2026	Hold	7-Jul-20	8.5	Apr-26	9.3	96.3	-1.2	4.6	648
Metinvest 2029	Hold	7-Jul-20	7.8	Oct-29	9.2	91.2	-2.1	6.6	500
MHP 2024	Sell	2-Jun-20	7.8	May-24	6.5	104.1	-0.5	3.3	500
MHP 2026	Sell	2-Jun-20	7.0	Apr-26	6.9	100.0	-1.1	4.7	550
MHP 2029	Sell	2-Jun-20	6.25	Sep-29	7.1	94.3	-0.9	6.9	350
Naftogaz 2022	Buy	9-Jun-20	7.4	Jul-22	8.4	98.2	-0.6	1.8	335
Naftogaz 2024 (EUR)	Buy	9-Jun-20	7.1	Jul-24	8.4	95.9	-1.3	3.4	672
Oschadbank 2023	Buy	16-Jun-20	9.4	Mar-23	8.1	101.5	-0.9	1.3	245
Oschadbank 2025	Buy	16-Jun-20	9.6	Mar-25	8.4	102.6	0.0	2.1	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	30.3	0.0	nm	175
Ukraine Railway 2021	Buy	5-May-20	9.9	Sep-21	9.0	100.5	-0.3	0.6	200
Ukraine Railway 2024	Buy	5-May-20	8.3	Jul-24	8.8	98.2	-0.3	3.5	595
Ukreximbank 2021 (UAH)	Buy	16-Jun-20	16.5	Mar-21	16.1	100.2	-0.1	0.6	150
Ukreximbank 2022	Buy	16-Jun-20	9.6	Apr-22	7.6	102.0	-0.2	1.0	313
Ukreximbank 2025	Buy	16-Jun-20	9.8	Jan-25	8.3	102.1	0.0	1.4	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
SSSU - Agricultural production monthly data	Exact	17-Jul
Kernel - Operational results for Q4 2020	Exact	20-Jul
SSSU - Transportation monthly data	Exact	20-Jul
MHP - Pre-close trading update for Q2 2020	Exact	21-Jul
SSSU - Wholesale and retail turnover monthly data	Exact	21-Jul

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