

Weekly Digest

- Shevchenko has been voted in as the new NBU governor
- The parliament has extended the ban on recovering FX mortgages until 2022
- Kernel Holding reported 4Q20 operating results largely in line with expectations

Shevchenko has been voted in as the new NBU governor by parliament. On July 16, 332 lawmakers (226 were required) supported the Ukrgasbank CEO, after his candidacy was put forward by Zelensky that very morning. During his official press-briefing Shevchenko stated that his key areas of focus would be restarting bank lending, resolving NPLs, retaining macrofinancial stability, and further strengthening the cooperation with Ukraine's external partners. He also praised the NBU's transformation over the past few years, but noted that he believes that the discount rate needs to be brought down further and that FX policy must support economic growth.

Our view: As noted earlier, we find Shevchenko to be an unpredictable persona, as although he does possess extensive banking experience, he spent most of his time working for state-owned institutions, which are notorious for widespread corruption. Moreover, his background is unlikely, in our view, to have provided him with much macroeconomic insight, which might make him prone to underestimating monetary policy risks. While on the one hand he has officially stated that the central bank's targets will on the whole remain unchanged, Shevchenko clearly believes that rates need to go down further and that the hryvnia should not be allowed to significantly appreciate from current levels (or perhaps should even devalue). Whether or not these convictions will be transformed into NBU actions will become apparent over the next few months. We think that the next monetary decision on Thursday should already provide some insight (we expect a 50bps key rate cut to 5.5%).

The parliament has extended the ban on recovering FX mortgages until 2022. The measure was initially introduced in 2014, when, following an over 70% devaluation of the hryvnia, many retail borrowers found themselves unable to service foreign currency loans. Although new bankruptcy legislation for individuals was introduced in 2018 and allowed for a degree of restructuring to take place, some UAH39bln (\$1.3bln) worth of facilities remain outstanding (according to data provided by the NBU).

Our view: We calculate that the amount of unresolved mortgages of this kind is equivalent in size to roughly 3.5% and 6.5% of the banking system's entire gross and net loan portfolios, respectively, which we believe to be significant. The adoption of the law is thus clearly a negative development, as it essentially ensures that these remain nonperforming and unresolved. Additionally, it elevates forward-looking lending risks, as creditor rights has been de facto violated. Taking into account that NPLs remain one of the main stumbling blocks to unlocking internal financing, we also find the initiative to be negative for future economic growth.

Kernel Holding reported 4Q20 operating results largely in line with expectations. Edible oil sales increased by almost a third QoQ to 916kt, having outpaced last year's level by 10%. Crushing plants continued to operate at full capacity. Grain trading and transshipment volumes both totaled c. 1.9mlnt, up by 30% and 54% YoY, respectively. According to data provided by Bloomberg and APK-Inform, the average quarterly price of corn dropped by 20% YoY, while sunflower gained 7% and wheat remained flat.

Our view: The reported figures did not significantly differ from our projections. Though oil sales volumes did come in slightly stronger than we modelled, the impact of this alteration on EBITDA amounts to c. \$5mln. Grain exports were on par with the company's announced target at the beginning of the year. Assuming that Kernel delivers on its latest \$100mln (ex-IFRS 16) farming contribution guidance, we think that EBITDA for the year should land at roughly \$410mln (including IFRS 16, but excluding IAS 41). This estimate, of course, assumes no contributions from Avere, which have historically proven to be quite volatile and unpredictable. Although Kernel's credit metrics continue to look solid, the recent shifts in market eurobond pricing (namely, the current 100-150bps yield discount to quasi-sovereigns) force us to downgrade our recommendation on the name to a 'Hold'.

Kernel Holding 4Q20 operating update

	4Q20	4Q19	YoY	3Q20	QoQ
Edible oil sales, kt	489	445	10%	381	28%
Oilseed crush, kt	916	896	2%	941	-3%
Grain sales ¹ , mlnt	1.86	1.44	30%	2.15	-14%
Export terminal ¹ , mlnt	1.84	1.20	54%	1.94	-5%
Corn price ² , \$/t	130	163	-20%	150	-14%
Wheat price ² , \$/t	191	194	-1%	203	-6%
Sunflower oil price ³ , \$/t	737	687	7%	727	1%

(1) Ukraine only and excluding Avere

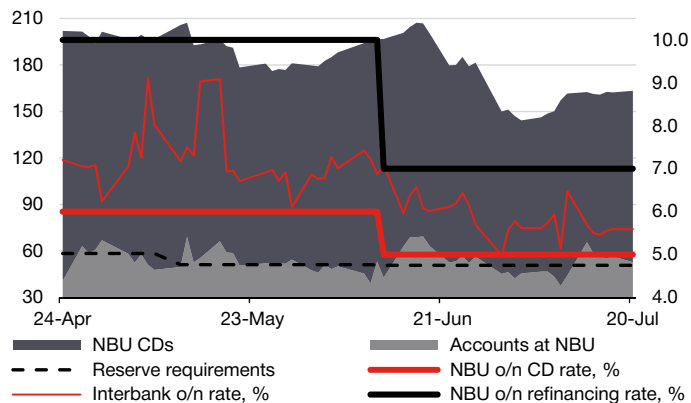
(2) Black Sea futures

(3) FOB export price (ask) from APK-Inform

Source: Company data, Bloomberg, APK-Inform

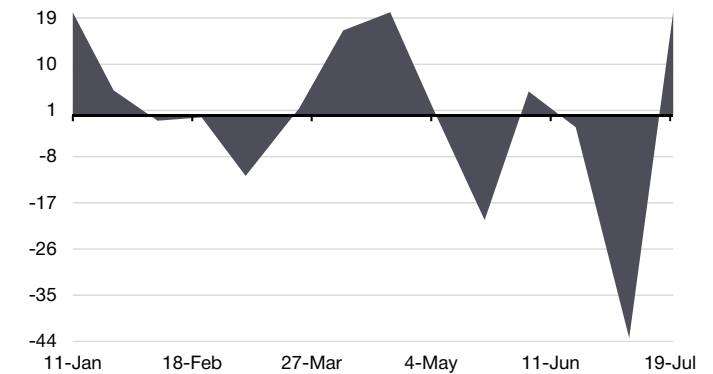
Appendix

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

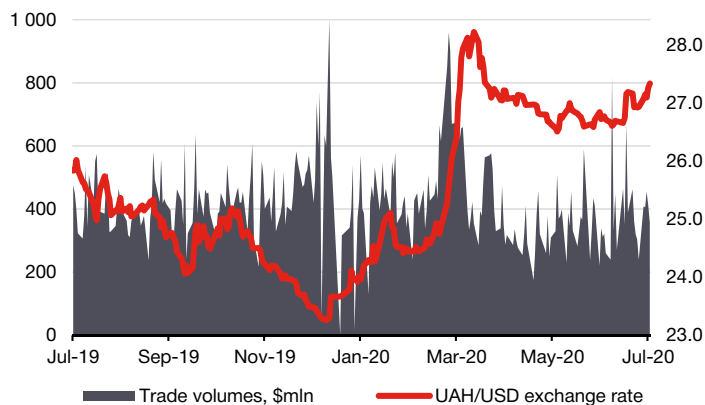


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has increased by UAH 0.8bln to UAH 163.2bln over the last week. On July 21 the Ministry of Finance conducted local hryvnia denominated placement maturing in January 2021 and February 2022 with yields of 7.74% and 10.25% respectively and USD denominated placement maturing in February 2021 with yield of 3.39%. A total of UAH 6.8bln and \$171mln was raised as a result.

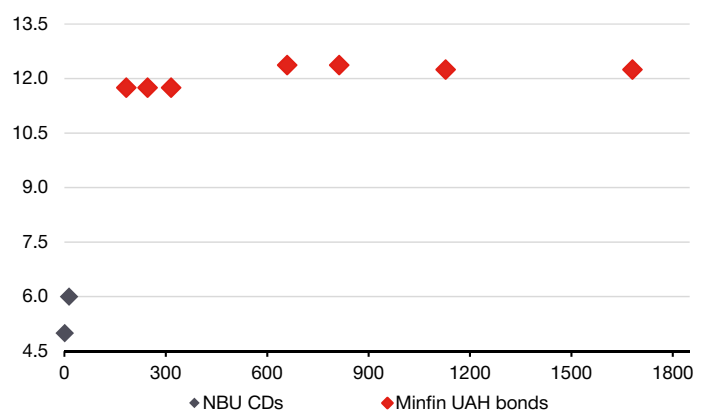
The UAH/USD interbank rate over the last week depreciated by 1.82%, starting out with 27.09 and ending at 27.58.

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



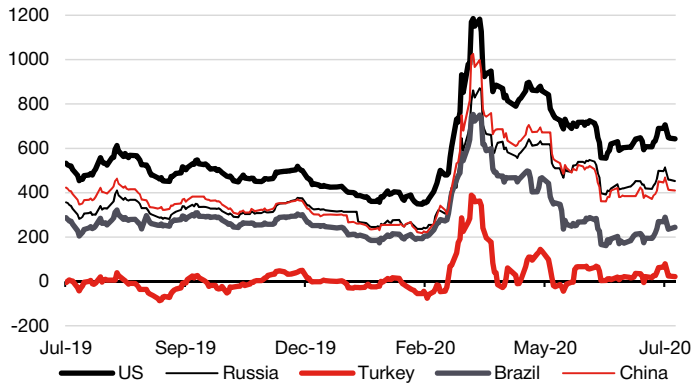
Note: Exchange rate figures are from official interbank data
Source: NBU

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



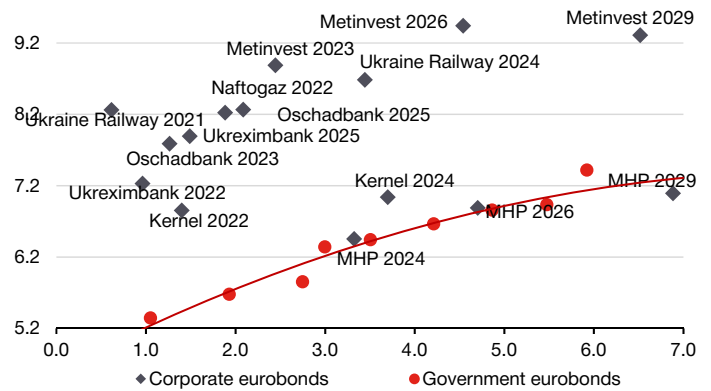
Source: NBU, Bloomberg, Adamant Capital estimates

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



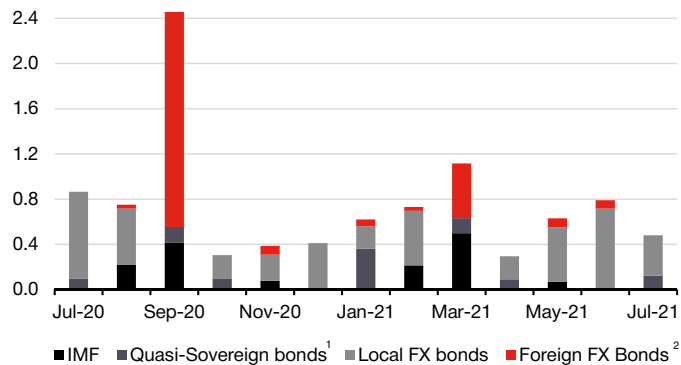
Source: Bloomberg, Adamant Capital estimates

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



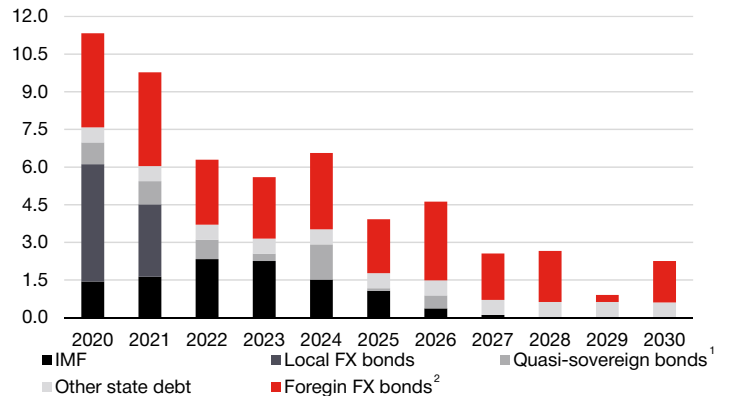
Source: Bloomberg, Adamant Capital estimates

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



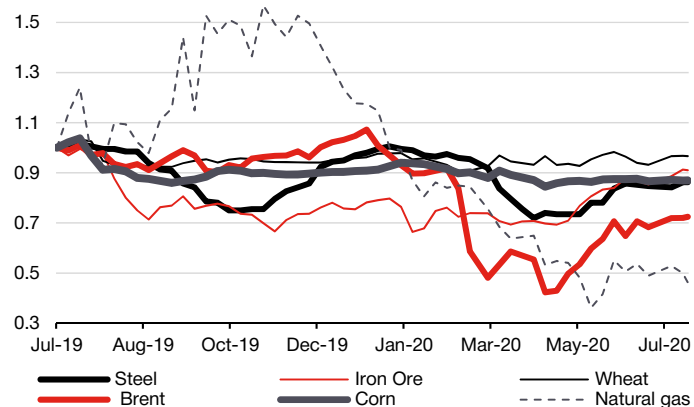
Note: Interest included in each category
 (1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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



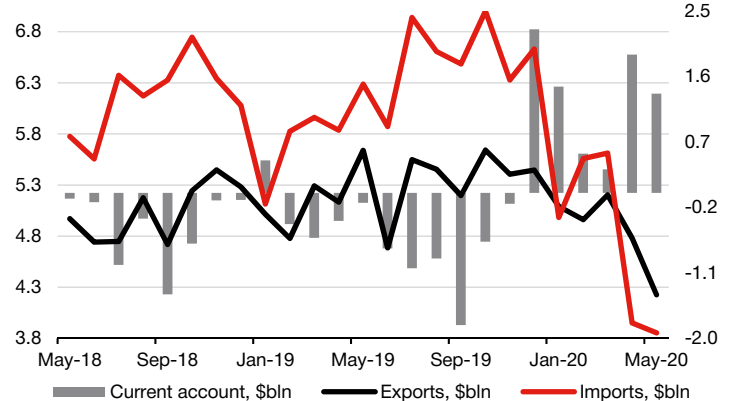
(1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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	32	148
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%	36.5%
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	27.0
EOP interbank exchange rate, UAH/\$	27.2	26.2	24.2	23.7	23.7	27.6	26.7	28.0
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	5.9	105.3	2.5	2.7	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	6.3	108.3	2.9	3.0	750
Ukraine 2027	Hold	-	7.8	Sep-27	6.9	104.5	4.6	5.5	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	7.4	114.2	5.1	5.9	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	7.3	100.7	5.3	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	29.9	57.3	0.3	2.9	1,344
Kernel 2022	Hold	21-Jul-20	8.8	Jan-22	6.9	102.7	0.7	1.4	500
Kernel 2024	Hold	21-Jul-20	6.5	Oct-24	7.0	98.0	0.2	3.7	300
Metinvest 2023	Hold	7-Jul-20	7.8	Apr-23	8.9	97.3	0.0	2.4	505
Metinvest 2025 (EUR)	Hold	7-Jul-20	5.6	Jun-25	8.3	89.6	1.2	4.3	333
Metinvest 2026	Hold	7-Jul-20	8.5	Apr-26	9.4	95.9	0.2	4.5	648
Metinvest 2029	Hold	7-Jul-20	7.8	Oct-29	9.3	90.5	-0.2	6.5	500
MHP 2024	Sell	2-Jun-20	7.8	May-24	6.5	104.3	0.6	3.3	500
MHP 2026	Sell	2-Jun-20	7.0	Apr-26	6.9	100.3	0.7	4.7	550
MHP 2029	Sell	2-Jun-20	6.25	Sep-29	7.1	94.4	0.7	6.9	350
Naftogaz 2022	Buy	9-Jun-20	7.4	Jul-22	8.2	98.5	0.7	1.9	335
Naftogaz 2024 (EUR)	Buy	9-Jun-20	7.1	Jul-24	8.2	96.4	1.2	3.6	672
Oschadbank 2023	Buy	16-Jun-20	9.4	Mar-23	7.8	102.0	0.7	1.3	245
Oschadbank 2025	Buy	16-Jun-20	9.6	Mar-25	8.3	102.8	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	8.3	101.0	0.5	0.6	200
Ukraine Railway 2024	Buy	5-May-20	8.3	Jul-24	8.7	98.6	0.3	3.4	595
Ukreximbank 2021 (UAH)	Buy	16-Jun-20	16.5	Mar-21	16.1	100.2	0.0	0.6	150
Ukreximbank 2022	Buy	16-Jun-20	9.6	Apr-22	7.2	102.3	0.4	1.0	313
Ukreximbank 2025	Buy	16-Jun-20	9.8	Jan-25	7.9	102.7	0.0	1.5	600
Ukrlandfarming in default	Sell	13-Jun-17	10.9	Mar-18	nm	5.1	-0.1	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 - Industrial production monthly data	Exact	22-Jul
NBU - Decision on the key policy rate	Exact	23-Jul
MHP - Pre-close trading update for Q2 2020	Exact	24-Jul
DTEK - Operational results for 6m20	Indicative	24-Jul
Treasury - Monthly state budget performance	Indicative	27-Jul

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