

Weekly Digest

- The Constitutional Court has struck down key anti-graft legislation
 - Ukraine's CA deficit in September amounted to \$0.2bln
 - Consolidated budget revenues in October increased by 9% YoY
-

The Constitutional Court has struck down key anti-graft legislation.

On October 27, Ukraine's highest court came out with a ruling declaring it illegal to hold officials criminally liable for false information in their asset declarations. Additionally, the anti-corruption body NAZK was stripped of its powers to check the accuracy of such financial disclosures as well as to post them online for public access. The move was immediately met with backlash from civil society activists and, a day later, from President Zelensky, who stated that the ruling threatens national security and submitted a law to parliament aiming to dissolve the Constitutional Court (CC) altogether.

Our view: The CC's decision has indeed delivered another blow to Ukraine's anti-graft infrastructure by not only removing the accusatory grounds for current illicit enrichment cases, but also by precluding the possibility of these types of prosecutions in the future. Such a rollback also means that the country no longer fulfills the necessary requirements to continue receiving support from the IMF and other IFIs. While a strong reaction from Zelensky is certainly a welcome change (the Presidential Office essentially kept quiet when the appointment of the NABU chief was declared illegal and questionable delegates were selected by the Rada to choose the new SAPO head a few weeks back), the submitted law to parliament is quite controversial, as it directly contradicts the Constitution (CC judges can only be relieved of duties by the CC). Given additionally that mustering enough votes to pass it seems problematic so far, we think that other avenues of conflict resolution are more likely (such as cancelling judge appointments and increasing the required majority to deliver rulings). These, as well as actions required to restore the previous legislation are going to take time, which means that the probably of Ukraine receiving donor support this year is quickly becoming very slim.

Ukraine's CA deficit in September amounted to \$0.2bln, down \$1.6bln YoY. The LTM figure (excluding the \$2.9bln arbitration payment to Naftogaz) landed at a \$2.7bln surplus versus a \$7.7bln deficit a year ago. The monthly trade balance (of goods and services) improved by \$1.1bln YoY to -\$0.4bln. The FA demonstrated a \$1.7bln increase in net assets over the month.

Our view: The reported CA deficit came, on the whole, in line with our estimates. The deterioration relative to the previous month occurred primarily on the back of a temporary peak in state interest payments (predominantly relating to eurobonds) and higher energy imports. Worker remittances somewhat surprised on the upside, as these were substantially revised (+22% for August), but were counteracted by higher dividends. Though the spread between export and import commodity prices has narrowed significantly from the start of the COVID-19 pandemic (which will negatively affect the TB going forward), net services continued to generate c. \$0.3bln of surplus per month more than last year, owing travel restrictions. All in all, we see few reasons to deviate from our previous CA surplus projection for the year of \$5.0bln or 3.4% of nominal GDP.

The FA in September demonstrated a substantial increase in net assets, primarily owing to state eurobond redemptions of \$1.9bln, which were partially counterbalanced by \$0.3bln worth of project financing from the WB. FX cash outside of the banking system grew by another \$0.5bln to \$3.8bln in total for the 10 months (almost double YoY).

Consolidated budget revenues in October increased by 9% YoY to UAH105bln. Compared to the annual plan the figure exceeded projections by 10%. Over 9m20, the state's total deficit amounted to UAH59bln (3.9% of GDP in LTM terms), up from an UAH9bln surplus for the same period of 2019.

Our view: The total monthly income of the general government landed broadly in line with our estimates. Most of the growth relative to last year was brought about by higher domestic tax collections. Based on September data, we think that largest contributors were once again VAT (the gross amount on locally produced goods was up by an impressive 15%, possibly due to improved administration) and PIT (no doubt aided by the double-digit increase in average wages). Although 10m20 revenues are still lagging 2% behind the FinMin's annual plan, we continue to believe that the probability of this gap closing or even becoming negative remains high.

Expenditures for September (this data is delayed), turned out to be somewhat higher than expected, mostly due to larger capex and "other operational" spend (this includes everything that remains after wages, R&D, debt servicing, grants, and social protection are subtracted out). Compared to last year, top-line growth accelerated to 23% from 11% in August. Taking into account that the state's financing sources remain limited (unless there are surprise moves either from the IMF or the EU, we still find a deficit of over 3.5% of GDP to be unfeasible), we expect this trend to reverse over the fourth quarter.

BoP summary for September, \$mln					
	Sep-20	Aug-20	Jul-20	LTM	LTM-1
Exports:	5,065	5,149	4,667	59,962	62,934
MoM	-2%	10%	12%		
YoY	-4%	-6%	-16%	-5%	9%
Imports:	5,437	5,254	5,249	64,495	75,149
MoM	3%	0%	18%		
YoY	-19%	-22%	-26%	-14%	9%
TB:	-372	-105	-582	-4,533	-12,215
MoM	-267	477	-289		
YoY	1,054	1,121	934	7,682	-1,234
CA ¹ :	-211	501	-29	2,774	-7,700
MoM	-712	530	102		
YoY	1,628	1,382	982	10,474	-2,213
FA:	1,749	150	60	2,399	-13,157
MoM	1,599	90	1,167		
YoY	3,682	1,097	2,326	15,556	-7,462
BoP:	-1,957	353	-88	3,292	5,493
MoM	-2,310	441	-1,066		
YoY	-2,050	284	-1,380	-2,201	5,264
Funding flow ² :	414	204	725	4,546	10,201

Note: LTM and LTM -1 stand for last twelve months and last twelve months a year ago, respectively

(1) Excludes the \$2.9bln one-off arbitrage payment received by Naftogaz from Gazprom in December of 2019

(2) Private sector financing: an estimated amount of capital flowing into the private sector (including banks) via lending and investment

Source: NBU, Adamant Capital estimates

October budget revenue performance, UAHbln						
	Oct-20	YoY	A/P	10m YoY	10m A/P	
Revenues	105	9%	10%	4%	-2%	
State budget	77	8%	10%	4%	-1%	
General fund	65	6%	15%	1%	0%	
Fiscal service	32	15%	42%	17%	9%	
Customs	30	-1%	-4%	-11%	-13%	
NBU transfers	0	nm	nm	-34%	0%	
Other	3	6%	9%	-5%	-10%	
Special fund	12	21%	-11%	23%	-5%	
Local budget	28	11%	12%	4%	-4%	

Note:

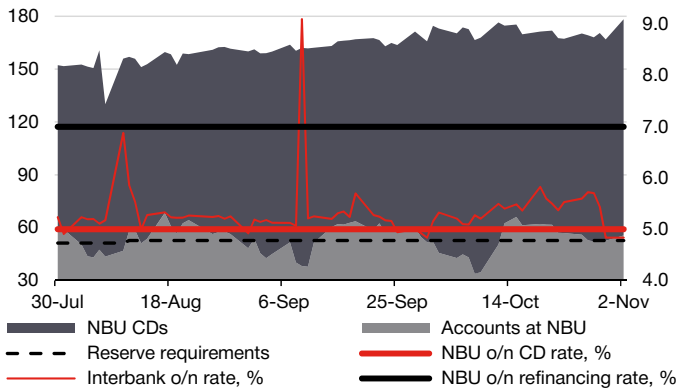
(1) Profit transfers and dividends from state-owned corporates

A and P stand for actual and planned figures, respectively

Source: SSSU, State Treasury, Adamant Capital estimates

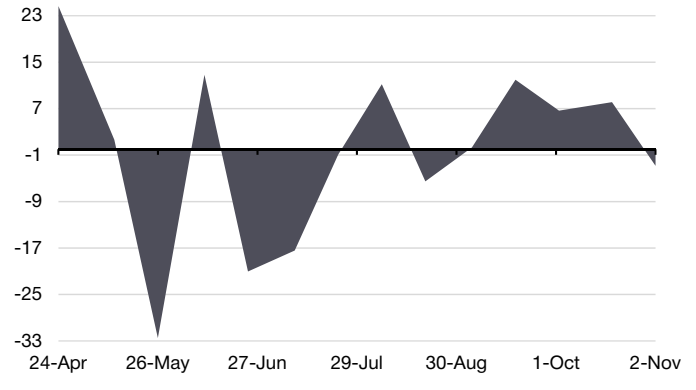
Appendix

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

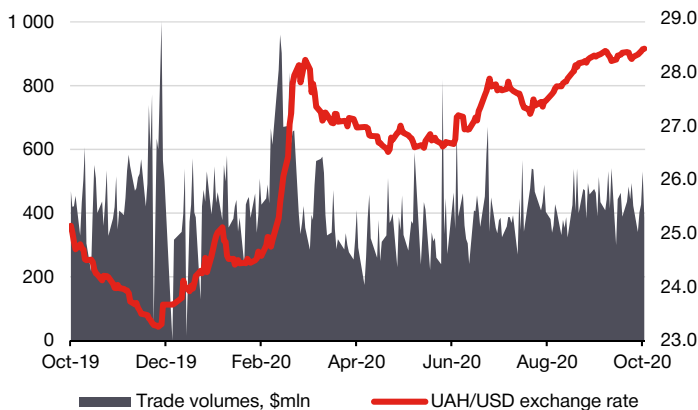


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has increased by UAH 8.1bln to UAH 178.3bln over the last week. On November 3 the Ministry of Finance conducted local hryvnia denominated placement maturing in March 2021 and November 2023 with yields of 7.50% and 10.95% respectively. A total of UAH 2.0bln was raised as a result.

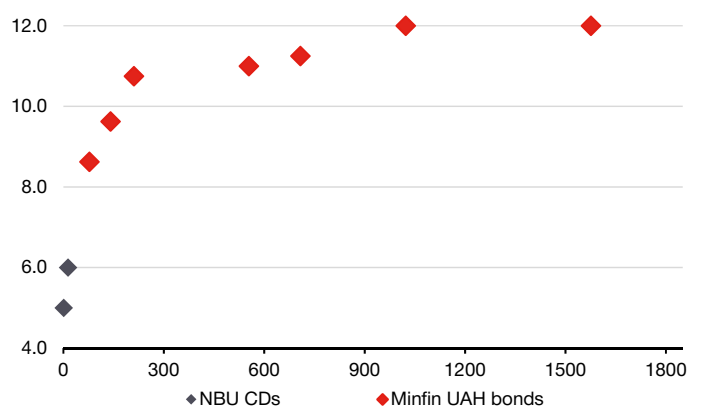
The UAH/USD interbank rate over the last week depreciated by 0.80%, starting out with 28.33 and ending at 28.56.

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



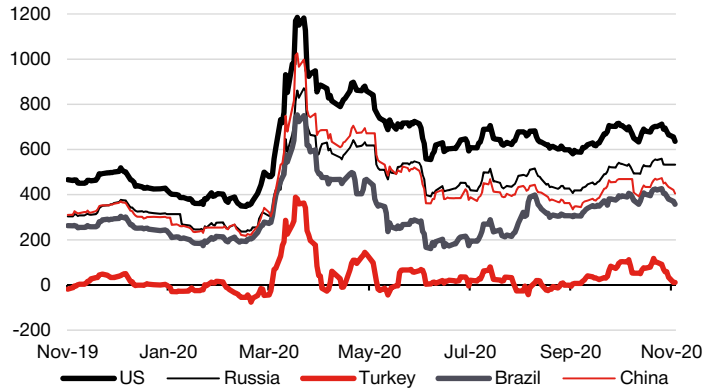
Note: Exchange rate figures are from official interbank data
Source: NBU

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



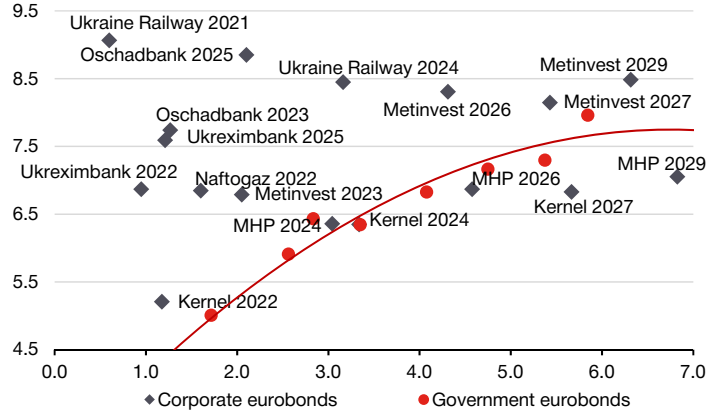
Source: NBU, Bloomberg, Adamant Capital estimates

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



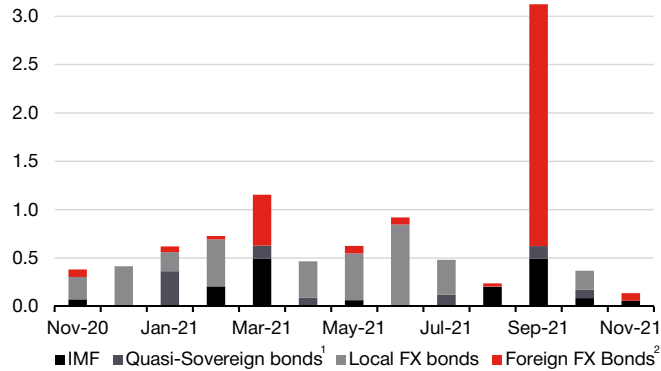
Source: Bloomberg, Adamant Capital estimates

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



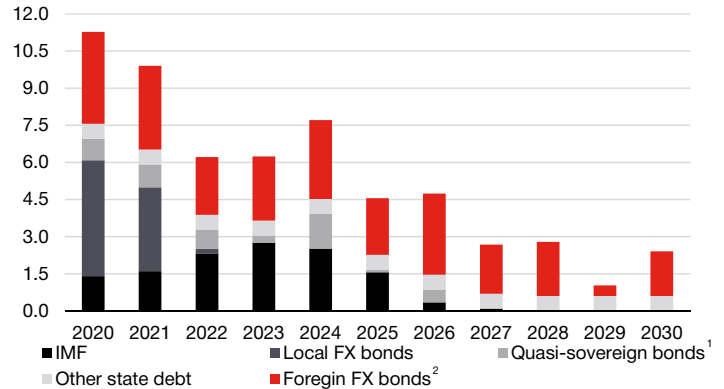
Source: Bloomberg, Adamant Capital estimates

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



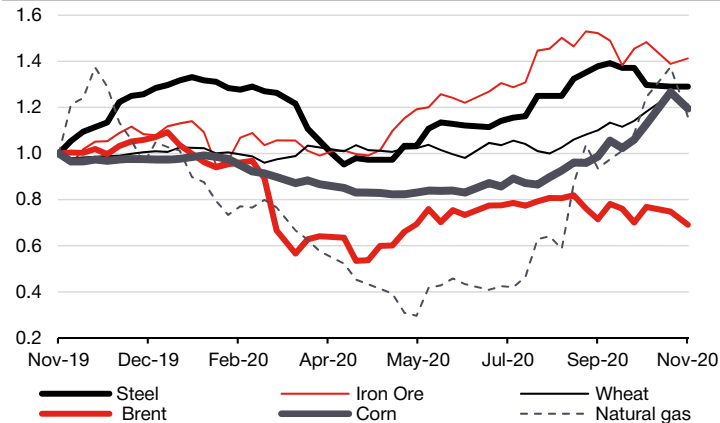
Note: Interest included in each category
 (1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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



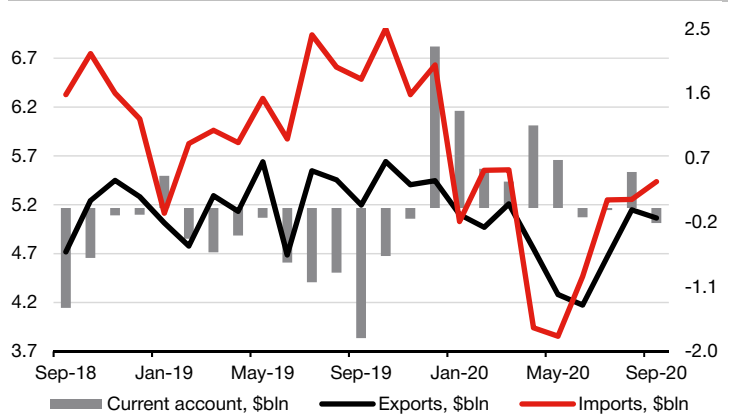
(1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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								
	2Q19	3Q19	4Q19	2019	1Q20	2Q20	3Q20E	2020E
Real GDP growth, YoY	4.7%	3.9%	1.5%	3.2%	-1.3%	-11.4%	-6.0%	-5.0%
Nominal GDP, UAHbln	933	1,112	1,115	3,975	846	868	1,077	3,927
Nominal GDP, \$bln	35	44	46	154	34	32	39	145
GDP deflator growth YoY, %	9.9%	7.6%	4.7%	8.1%	5.1%	5.0%	3.0%	4.0%
Period average CPI YoY, %	9.1%	8.5%	5.2%	7.9%	2.6%	2.1%	2.4%	2.4%
End of period CPI YoY, %	9.0%	7.5%	4.1%	4.1%	2.3%	2.4%	2.3%	3.0%
Consolidated budget deficit, % of GDP ¹	2.5%	2.4%	2.1%	2.1%	2.3%	1.7%	3.4%	3.5%
Broad public sector deficit, % of GDP ²	2.7%	2.5%	2.1%	2.2%	2.3%	2.2%	4.0%	4.3%
Public debt as % of LTM GDP, UAH	55.4%	51.1%	50.3%	50.3%	56.3%	57.6%	59.0%	59.9%
Public external debt as % of LTM GDP, \$ ³	36.0%	32.9%	31.6%	31.6%	31.6%	31.7%	32.5%	37.1%
Total external debt, \$bln	116	118	122	122	120	123	128	130
Export of goods and services, \$bln	15.5	16.3	16.5	63.4	15.3	13.2	14.9	62.4
Import of goods and services, \$bln	18.3	20.3	20.0	75.5	16.1	12.3	15.9	62.4
Trade balance, \$bln	-2.8	-4.0	-3.5	-12.1	-0.9	0.9	-1.1	0.0
Current account, \$bln	-0.5	-2.2	1.8	-1.1	2.3	1.7	0.3	5.0
Financial account, \$bln ⁴	-0.9	-3.8	-2.1	-7.3	2.4	0.4	2.0	1.7
End of period NBU reserves, \$bln	20.6	20.1	25.3	25.3	24.9	28.5	26.5	28.0
Average interbank exchange rate, UAH/\$ ⁵	26.6	25.2	24.2	25.8	25.2	26.9	27.6	27.0
EOP interbank exchange rate, UAH/\$	26.2	24.2	23.7	23.7	27.6	26.7	28.3	28.0
EOP key policy rate NBU, %	17.5%	16.5%	13.5%	13.5%	10.0%	6.0%	6.0%	6.0%

(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	104.7	1.3	2.6	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	6.4	107.4	1.5	2.8	750
Ukraine 2027	Hold	-	7.8	Sep-27	7.3	102.4	2.4	5.4	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	8.0	110.4	2.3	5.8	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	7.7	97.8	2.9	7.7	3,000
Avangard in default	Sell	9-Apr-19	10.0	Oct-18	nm	3.5	-0.2	nm	214
DTEK 2024 in default	Buy	1-Sep-20	10.8	Dec-24	26.4	65.2	-0.5	2.8	1,344
Kernel 2022	Hold	27-Oct-20	8.8	Jan-22	5.2	104.2	-0.5	1.2	500
Kernel 2024	Hold	27-Oct-20	6.5	Oct-24	6.3	100.5	-0.5	3.3	300
Kernel 2027	Hold	27-Oct-20	6.8	Oct-27	6.8	99.6	-0.4	5.7	300
Metinvest 2023	Hold	27-Oct-20	7.8	Apr-23	6.8	102.2	-0.2	2.1	311
Metinvest 2025 (EUR)	Hold	27-Oct-20	5.6	Jun-25	7.3	93.3	-0.3	4.0	333
Metinvest 2026	Hold	27-Oct-20	8.5	Apr-26	8.3	100.8	-0.4	4.3	648
Metinvest 2027	Hold	27-Oct-20	7.7	Oct-27	8.1	97.4	-0.4	5.4	333
Metinvest 2029	Hold	27-Oct-20	7.8	Oct-29	8.5	95.5	-0.2	6.3	500
MHP 2024	Hold	27-Oct-20	7.8	May-24	6.4	104.3	-0.1	3.0	500
MHP 2026	Hold	27-Oct-20	7.0	Apr-26	6.9	100.4	-0.2	4.6	550
MHP 2029	Hold	27-Oct-20	6.3	Sep-29	7.1	94.8	-0.4	6.8	350
Naftogaz 2022	Buy	29-Sep-20	7.4	Jul-22	6.8	100.8	-0.3	1.6	335
Naftogaz 2024 (EUR)	Buy	29-Sep-20	7.1	Jul-24	8.5	95.6	-0.1	3.3	672
Oschadbank 2023	Buy	11-Aug-20	9.4	Mar-23	7.7	102.0	0.0	1.3	175
Oschadbank 2025	Buy	11-Aug-20	9.6	Mar-25	8.8	101.6	0.0	2.1	225
Privatbank in default (10.250)	Not rated	-	10.3	nm	35.2	29.1	0.0	nm	160
Privatbank in default (10.875)	Not rated	-	10.9	nm	36.1	30.1	-0.1	nm	175
Ukraine Railway 2021	Sell	27-Oct-20	9.9	Sep-21	9.1	100.4	0.3	0.6	100
Ukraine Railway 2024	Sell	27-Oct-20	8.3	Jul-24	8.4	99.4	0.5	3.2	595
Ukreximbank 2021 (UAH)	Buy	11-Aug-20	16.5	Mar-21	18.8	99.1	0.0	0.3	150
Ukreximbank 2022	Buy	11-Aug-20	9.6	Apr-22	6.9	102.5	0.0	0.9	188
Ukreximbank 2025	Buy	11-Aug-20	9.8	Jan-25	7.6	102.5	0.0	1.2	600
Ukrlandfarming in default	Sell	13-Jun-17	10.9	nm	229.0	4.7	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
NBU - International reserves monthly data	Exact	6-Nov
SSSU - Monthly inflation	Exact	9-Nov

Contacts

Adamant Capital

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

Portfolio Management

Yuriy Sozinov | urs@adamant-capital.com

Research

Konstantin Fastovets | fks@adamant-capital.com

PR

Inna Zvyagintseva | zin@adamant-capital.com

Disclaimer

This report has been prepared solely for information purposes and is not intended to be an offer, or a solicitation of an offer, to buy or sell any securities. Descriptions of any company or companies or/and their securities, or markets, or developments mentioned herein are not represented to be complete. There is no responsibility on our part to revise or update any information or correct any inaccuracies contained in this report on an on-going basis. Although the information in this material has been obtained from sources that Adamant Capital believes to be reliable, we do not guarantee its completeness or accuracy. In making their investment decisions investors are expected to rely on their own analysis of all risks associated with investing in securities. Adamant Capital, its top executives, representatives and employees accept no liability whatsoever for any direct or consequential loss arising from the use of the material or its contents. Adamant Capital, third parties related to it, its directors and/or employees, and/or any persons connected with them, may have interests in the companies or provide services to one or more companies discussed herein and/or intend to acquire such interests and/or to provide any such services in the future. All estimates and opinions expressed in this report reflect the judgment of each research analyst, who is fully or partially responsible for the contents of the document, and may differ from the opinions of Adamant Capital. This document, or any part hereof, may not be reproduced or copies circulated without the prior express consent of Adamant Capital.