

## Weekly Digest

- Ukraine's CA surplus in October amounted to \$0.8bln
- Ukraine's foreign currency reserves remained flat in November at \$26.1bln
- Naftogaz 3Q20 EBITDA declined by \$57mln YoY to -\$157mln
- Metinvest's EBITDA in September increased by 23% MoM to \$207mln

**Ukraine's CA surplus in October amounted to \$0.8bln**, up \$1.7bln YoY. The LTM figure (excluding the \$2.9bln arbitration payment to Naftogaz) landed at \$4.3bln versus -\$7.3bln a year ago. The monthly trade balance (of goods and services) improved by \$1.4bln YoY to zero. The FA demonstrated \$1.1bln increase in net assets.

**Our view:** The reported CA surplus came in moderately above estimates. Key deviations include slightly lower actual energy product purchases (most notably of coal and oil) as well as a negative value for reinvested income (a \$150mln difference MoM). While these do alter our outlook on the remaining two months of the year to a degree, our model experienced the largest changes due to more favorable iron ore and soft commodity price forecasts. Taking into account that the Black Sea corn and wheat futures have already outpaced last year's levels by 30% and 20%, respectively, and that the 62% CFR China benchmark is up by almost 70%, we think that the overall trade balance in November and December turn positive (last time this happened in April and May). This implies that the CA surplus may reach \$6.5bln or 4.5% of nominal GDP (a 1.0ppt upgrade from our previous forecast).

The increase in net assets registered by the FA in October primarily reflects a surge in foreign cash balances outside of the banking system (up by \$530mln, which is 35% above the monthly average for 2020). Other contributors include changes to net trade credit, and local hryvnia bond sales by nonresidents.

**Ukraine's foreign currency reserves remained flat in November at \$26.1bln.** Outflows stemmed primarily from local debt amortizations, which were offset by similarly sized placements.

**Our view:** The reported figure came in on par with expectations, with only intervention sales landing moderately below projections. Taking into account that the IMF has seemingly green-lit the possibility of a staff-level agreement on the next tranche with Ukraine by the end of December and that the PM has already announced at \$1.0bln eurobond placement in the works, we raise our year-end reserves forecast to \$27.8bln from \$25.9bln previously. Our outlook also includes the disbursement of EUR0.6bln by the EU, which we find to be likely if the Fund indeed provides its approval.

### BoP summary for October, \$mln

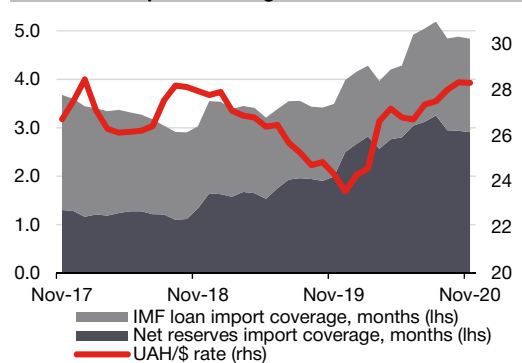
|                             | Oct-20 | Sep-20 | Aug-20 | LTM    | LTM-1   |
|-----------------------------|--------|--------|--------|--------|---------|
| Exports:                    | 5,523  | 5,041  | 5,100  | 59,691 | 63,363  |
| MoM                         | 10%    | -1%    | 10%    |        |         |
| YoY                         | -3%    | -5%    | -7%    | -6%    | 8%      |
| Imports:                    | 5,549  | 5,367  | 5,217  | 62,820 | 75,476  |
| MoM                         | 3%     | 3%     | 0%     |        |         |
| YoY                         | -22%   | -20%   | -22%   | -17%   | 8%      |
| TB:                         | -26    | -326   | -117   | -3,129 | -12,113 |
| MoM                         | 300    | -209   | 484    |        |         |
| YoY                         | 1,389  | 1,100  | 1,109  | 8,984  | -559    |
| CA <sup>1</sup> :           | 817    | -195   | 498    | 4,274  | -7,262  |
| MoM                         | 1,012  | -693   | 513    |        |         |
| YoY                         | 1,473  | 1,644  | 1,379  | 11,536 | -1,048  |
| FA:                         | 1,159  | 1,765  | 147    | 4,130  | -12,443 |
| MoM                         | -606   | 1,618  | 73     |        |         |
| YoY                         | 1,704  | 3,698  | 1,094  | 16,573 | -6,010  |
| BoP:                        | -343   | -1,957 | 353    | 3,058  | 5,220   |
| MoM                         | 1,614  | -2,310 | 441    |        |         |
| YoY                         | -234   | -2,050 | 284    | -2,162 | 4,982   |
| Funding flow <sup>2</sup> : | -366   | 367    | 243    | 3,690  | 9,708   |

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 arbitration 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

### Reserves import coverage vs UAH/\$ rate



Note: import coverage is calculated using average LTM imports  
 Source: NBU, Adamant Capital estimates

**Naftogaz 3Q20 EBITDA declined by \$57m YoY to -\$157m.** The largest contribution drop occurred in the exploration and production division, which lost c. \$180m compared to last year. The commercial segment was actually able to cut losses, partially owing to smaller provisions for non-recoverable receivables. Sales grew by 50% due to a restatement, which excluded the transit segment from 2019 figures (in 2020 the company continues to receive revenue from transit, but only as an intermediary between Gazprom and the unbundled GTS operator). Operating cash flow was surged by \$320m to \$18m on the back of significantly smaller working capital needs (an almost \$0.5bn difference YoY). Capex dropped by 43% to \$143m. Free cash flow landed at -\$125m (up \$427m YoY) as a result. Net debt to LTM EBITDA tripled to 2.0. During the company's conference call with investors, Naftogaz noted that it had a difficult year so far, but is happy to report that profitability is improving owing to a recovery in gas prices and the abolishment of the PSO for households (though not for heating utilities) as of August 1. Management is also expecting to receive \$1.1bn worth of PSO compensation from the state, which will, in turn, be used to offset tax debt accumulated by Ukrnafta (Naftogaz will pre-pay \$0.9bn worth of Ukrnafta's gas production to make this happen). Capex guidance for 2021 was given at \$0.9-1.1bn, out of which \$0.4bn will go towards maintenance.

**Our view:** Quarterly EBITDA came in once again below projections, reflecting a surprisingly poor commercial segment result. In fact, taking into account that the estimated average realized price of natural gas increased QoQ by some 55% (\$47/kcm in absolute terms), it is not entirely clear why margins remained practically unchanged. That said, in 4Q20 we expect not only the operating side of the business to report much stronger figures owing to a seasonal jump in sales volumes (we anticipate a 2.5-3.0x increase) together with even better pricing, but also for earnings to reflect the abovementioned \$1.1bn of PSO compensation from the government. It is not entirely clear, however, whether a significant portion of the latter will be offset by a \$700m write-down of receivables (due to non-payments). On balance, we currently retain on 2020 full year EBITDA forecast at \$1.0bn.

Though a significant portion of the company's earnings remains quite unpredictable (no indication has so far been given on the size of the GTS operator's 2021 payment, for example), we think that credit metrics remain indicative of relatively low default risks (base case net debt to EBITDA at the end of December below 1.0, and loans due over 2021-22 are all with state-owned banks). Given that its eurobonds trade at a c. 200bps yield premium to the sovereign curve, we reiterate our 'Buy' recommendation on the name.

| Naftogaz 3Q20 financial results, \$m |       |       |       |      |       |
|--------------------------------------|-------|-------|-------|------|-------|
|                                      | 3Q20  | 3Q19  | YoY   | 2Q20 | QoQ   |
| Revenue                              | 1,150 | 767   | 50%   | 998  | 15%   |
| EBITDA <sup>1</sup>                  | -157  | -100  | nm    | -482 | nm    |
| Production                           | 197   | 374   | -47%  | 114  | 73%   |
| Commercial                           | -264  | -514  | nm    | -333 | nm    |
| Other                                | -90   | 40    | nm    | -263 | nm    |
| EBITDA margin                        | -14%  | -13%  | -1pps | -48% | 35pps |
| Net profit                           | -199  | -134  | nm    | -547 | nm    |
| Net profit margin                    | -17%  | -18%  | 0pps  | -55% | 38pps |
| Net debt                             | 694   | 1,483 | -53%  | 539  | 29%   |
| Net debt/EBITDA                      | 2.0   | 0.7   | 186%  | 1.2  | 61%   |
| Operating cash flow                  | 18    | -302  | nm    | 176  | -90%  |
| Capex                                | 143   | 250   | -43%  | 149  | -4%   |
| Free cash flow                       | -125  | -552  | nm    | 27   | nm    |
| Avg gas price, \$/t                  | 138   | 182   | -24%  | 89   | 55%   |

(1) Includes net movement in provisions for trade accounts receivable, prepayments, VAT balances, and other current assets  
Source: Company data, Adamant Capital estimates

**Metinvest's EBITDA in September increased by 23% MoM to \$207mln**, excluding JVs. The monthly contribution of the metals division expanded by 36% to \$114mln. Mining EBITDA grew by 5% to \$98mln. Operating cash flow surged by 8.5x to \$298mln, additionally reflecting a \$93mln working capital release (as opposed to a \$63mln injection in August). Capex increased by 20% to \$65mln, which nonetheless allowed the FCF to grow by \$214mln MoM to \$233mln. The LTM leverage ratio contracted by 19% to 2.0.

**Our view:** EBITDA in September came in 15% above our projections primarily because of a 35% MoM surge (\$35 in absolute terms) in the margin per ton of metals sold (excluding resales). Taking into account that the average realized price increased by \$28, the mean cost of production and delivery had to contract from August levels, which is something that we did not anticipate. One possible explanation for this is a delayed cost saving effect on natural gas, which, due to the COVID-19 pandemic, bottomed out at less than \$7 per MWh in June (TTF, as opposed to over \$15 at the beginning of the year). If this is indeed the case, expenses are also likely to reflect the recent changes in benchmarks (already at \$21 per MWh) more slowly than we previously thought. As the iron ore segment performed more or less on par with projections, on balance, we upgrade our full year EBITDA estimate for Metinvest to \$1.9bln (from \$1.7bln previously).

Although the company's credit metrics are now looking stronger than ever (LTM net debt to EBITDA may go down to as low as 1.1 by December), these are likely to fluctuate significantly going forward, given the nature of the business. Moreover, we feel that prolonged negotiations of the sister issuer DTEK with creditors elevate shareholder risks. Our recommendation on Metinvest remains a 'Hold'.

**Metinvest's September financial results, \$mln**

|                                    | Sep   | Aug   | MoM  | 9M20   | YoY  |
|------------------------------------|-------|-------|------|--------|------|
| Revenues                           | 912   | 838   | 9%   | 7,628  | -10% |
| EBITDA <sup>1</sup>                | 207   | 168   | 23%  | 1,164  | 14%  |
| margin                             | 23%   | 20%   | 3pp  | 15%    | 3pp  |
| Metals EBITDA                      | 114   | 84    | 36%  | 533    | 925% |
| Mining EBITDA                      | 98    | 93    | 5%   | 721    | -27% |
| Metal sales <sup>2</sup> , kt      | 848   | 839   | 1%   | 6,918  | 4%   |
| Steel price <sup>3</sup> , \$/t    | 489   | 461   | 6%   | 478    | -15% |
| Iron ore sales <sup>4</sup> , kt   | 2,020 | 2,386 | -15% | 21,706 | 2%   |
| Iron ore price <sup>5</sup> , \$/t | 109   | 96    | 14%  | 92     | -7%  |
| OCF                                | 298   | 35    | 751% | 1198   | 60%  |
| Capex                              | 65    | 54    | 20%  | 617    | -11% |
| Free cash flow                     | 233   | -19   | nm   | 581    | 938% |
| Total debt                         | 2,927 | 3,017 | -3%  | 2,927  | 10%  |
| Net debt                           | 2,278 | 2,494 | -9%  | 2,278  | -7%  |
| Net debt/LTM EBITDA                | 2.0   | 2.5   | -19% | 2.0    | 25%  |

(1) Excluding JVs

(2) Excluding resales

(3) Calculated as revenues of finished and semi-finished goods divided by the volume sold

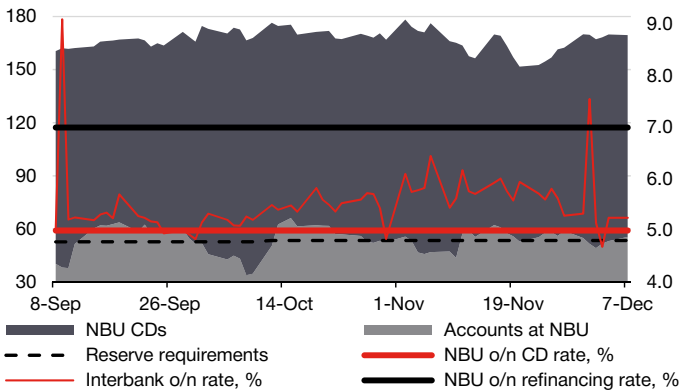
(4) Estimated, including internal sales and pellets in ore equivalent

(5) The average realized price, including pellets in ore equivalent

Source: Company data, Adamant Capital estimates

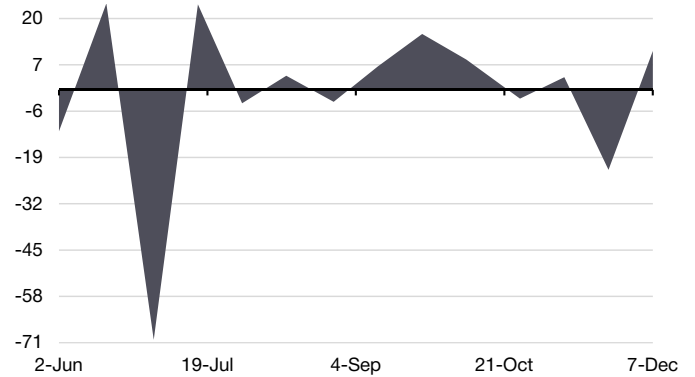
## Appendix

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

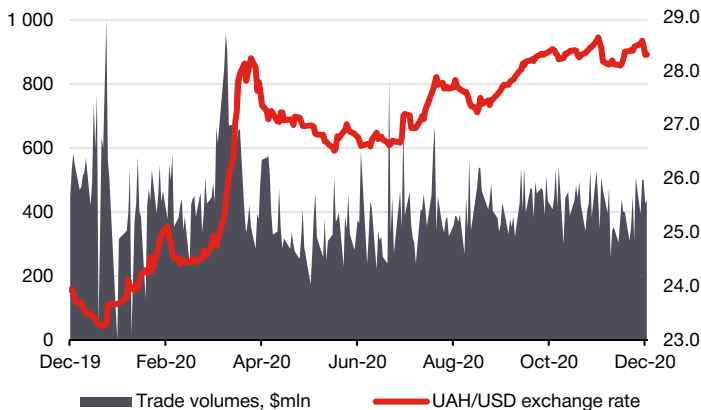


Note: in UAHbln, where each point represents a biweekly sum  
Source: NBU

**Local market liquidity** (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has decreased by UAH 0.5bln to UAH 169.5bln over the last week. On December 8 the Ministry of Finance conducted local hryvnia denominated placement maturing in March 2021, June 2021, October 2021, February 2023, May 2024 and February 2025 with yields of 10.00%, 10.49%, 11.22%, 11.67%, 11.89% and 12.04% respectively and USD denominated placement maturing in October 2021 with yield of 3.79%. A total of UAH 10.2bln and \$204mln was raised as a result.

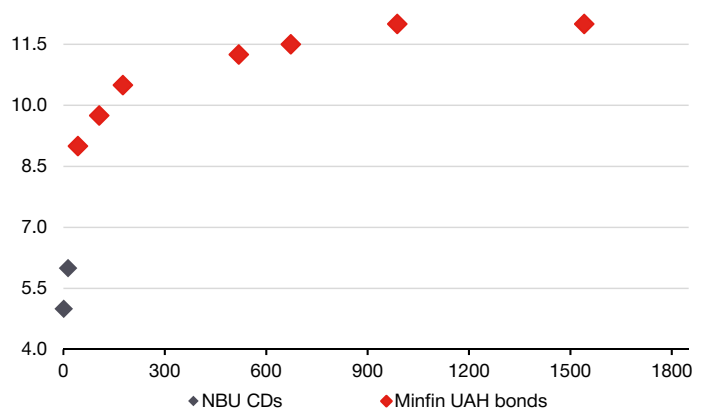
The UAH/USD interbank rate over the last week appreciated by 0.82%, starting out with 28.50 and ending at 28.26.

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

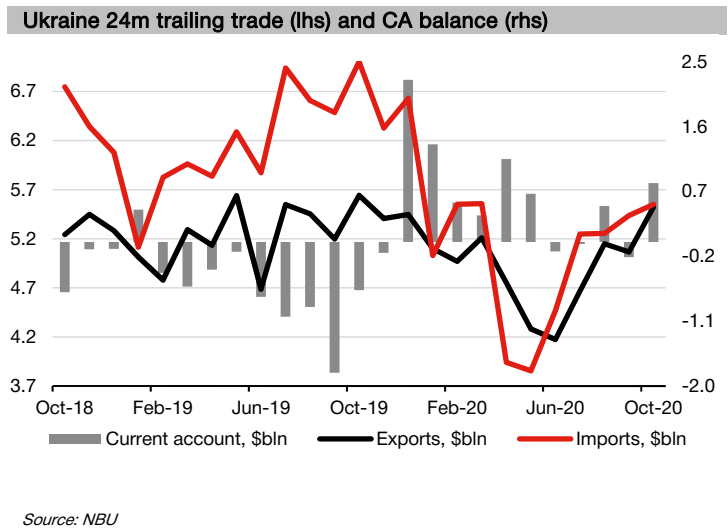
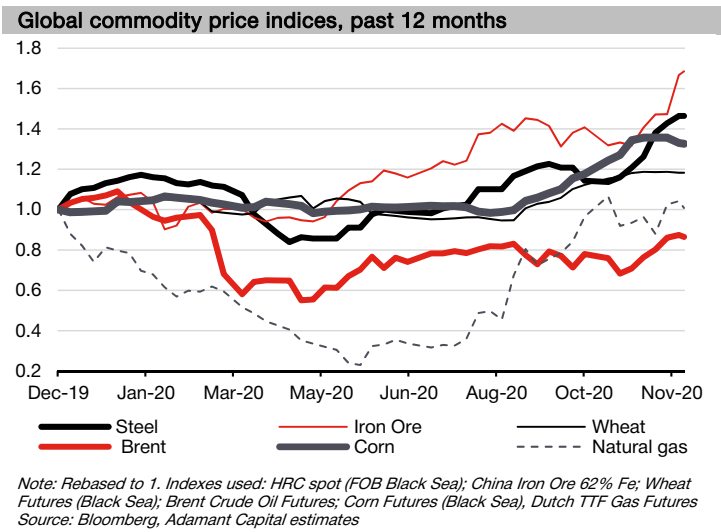
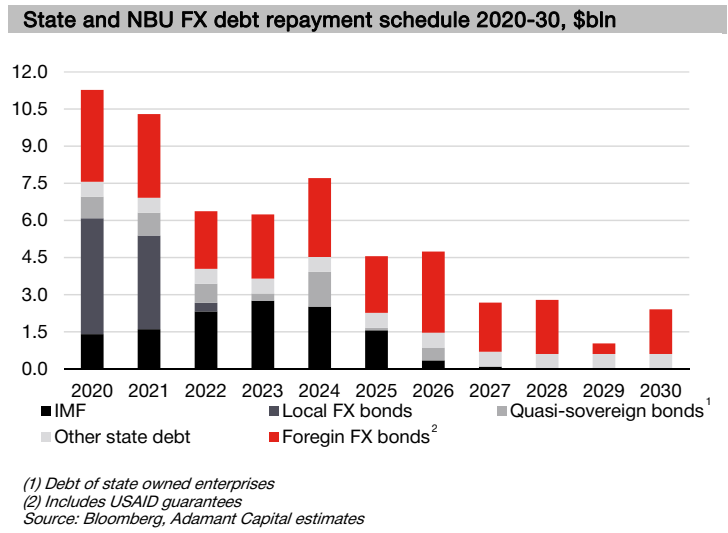
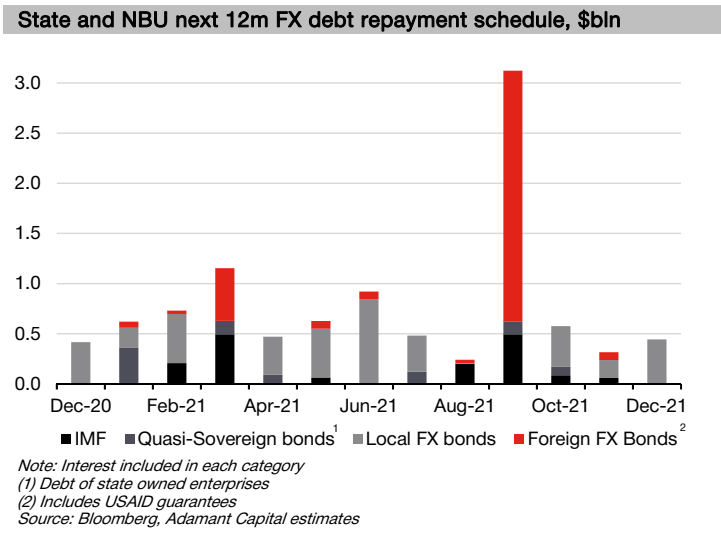
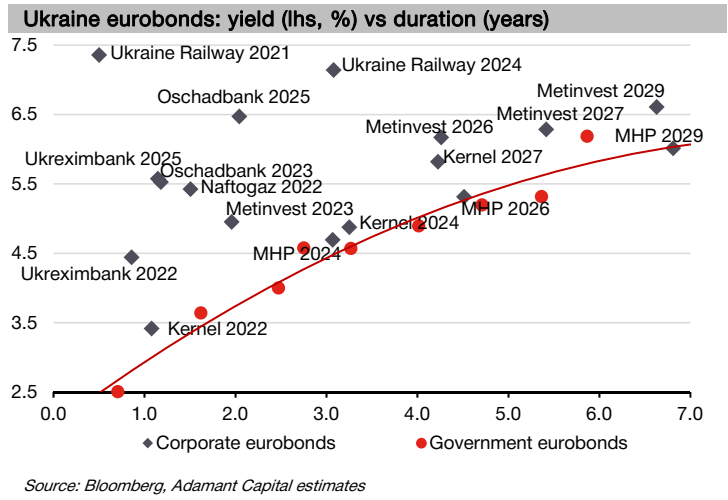
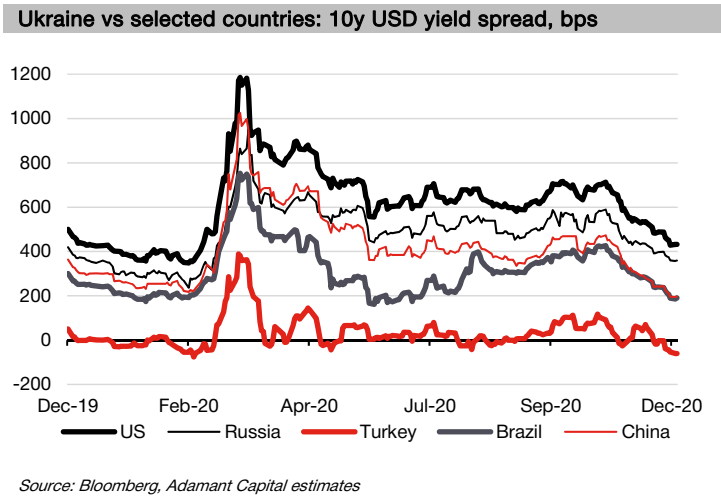


Note: Exchange rate figures are from official interbank data  
Source: NBU

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



Source: NBU, Bloomberg, Adamant Capital estimates



| Key macroeconomic indicators                          |       |       |       |       |        |       |       |       |
|---|-------|-------|-------|-------|--------|-------|-------|-------|
|   | 3Q19  | 4Q19  | 2019  | 1Q20  | 2Q20   | 3Q20E | 4Q20E | 2020E |
| Real GDP growth, YoY                                  | 3.9%  | 1.5%  | 3.2%  | -1.3% | -11.4% | -3.5% | -2.0% | -4.5% |
| Nominal GDP, UAHbln                                   | 1,112 | 1,115 | 3,975 | 846   | 868    | 1,105 | 1,138 | 3,968 |
| Nominal GDP, \$bln                                    | 44    | 46    | 154   | 34    | 32     | 40    | 41    | 147   |
| GDP deflator growth YoY, %                            | 7.6%  | 4.7%  | 8.1%  | 5.1%  | 5.0%   | 3.0%  | 4.2%  | 4.5%  |
| Period average CPI YoY, %                             | 8.5%  | 5.2%  | 7.9%  | 2.6%  | 2.1%   | 2.4%  | 3.5%  | 2.7%  |
| End of period CPI YoY, %                              | 7.5%  | 4.1%  | 4.1%  | 2.3%  | 2.4%   | 2.3%  | 4.2%  | 4.2%  |
| Consolidated budget deficit, % of GDP <sup>1</sup>    | 2.4%  | 2.1%  | 2.1%  | 2.3%  | 1.7%   | 3.4%  | 3.5%  | 3.5%  |
| Broad public sector deficit, % of GDP <sup>2</sup>    | 2.5%  | 2.1%  | 2.2%  | 2.3%  | 2.2%   | 3.7%  | 4.1%  | 4.1%  |
| Public debt as % of LTM GDP, UAH                      | 51.1% | 50.3% | 50.3% | 56.3% | 57.6%  | 59.0% | 60.0% | 60.0% |
| Public external debt as % of LTM GDP, \$ <sup>3</sup> | 32.9% | 31.6% | 31.6% | 31.6% | 31.7%  | 32.5% | 34.8% | 34.8% |
| Total external debt, \$bln                            | 118   | 122   | 122   | 120   | 123    | 128   | 127   | 127   |
| Export of goods and services, \$bln                   | 16.3  | 16.5  | 63.4  | 15.3  | 13.2   | 14.9  | 17.6  | 60.9  |
| Import of goods and services, \$bln                   | 20.3  | 20.0  | 75.5  | 16.1  | 12.3   | 15.9  | 16.8  | 61.1  |
| Trade balance, \$bln                                  | -4.0  | -3.5  | -12.1 | -0.9  | 0.9    | -1.1  | 0.8   | -0.2  |
| Current account, \$bln                                | -3.8  | 1.4   | -1.1  | 2.3   | 1.7    | 0.3   | 2.3   | 6.5   |
| Financial account, \$bln <sup>4</sup>                 | -5.2  | -2.3  | -10.2 | 2.4   | 0.4    | 2.0   | -1.3  | 3.4   |
| End of period NBU reserves, \$bln                     | 20.1  | 25.3  | 25.3  | 24.9  | 28.5   | 26.5  | 27.8  | 27.8  |
| Average interbank exchange rate, UAH/\$ <sup>5</sup>  | 25.2  | 24.2  | 25.8  | 25.2  | 26.9   | 27.6  | 28.1  | 27.0  |
| EOP interbank exchange rate, UAH/\$                   | 24.2  | 23.7  | 23.7  | 27.6  | 26.7   | 28.3  | 28.0  | 28.0  |
| EOP key policy rate NBU, %                            | 16.5% | 13.5% | 13.5% | 10.0% | 6.0%   | 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 6<sup>th</sup> 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   | 4.0       | 109.6     | 0.9      | 2.5      | 1,355      |
| Ukraine 2024  | Hold           | -         | 9.0    | Feb-24   | 4.6       | 112.8     | 1.0      | 2.8      | 750        |
| Ukraine 2027  | Hold           | -         | 7.8    | Sep-27   | 5.3       | 113.6     | 1.8      | 5.4      | 1,307      |
| Ukraine 2028  | Hold           | -         | 9.8    | Nov-28   | 6.2       | 122.0     | 2.0      | 5.9      | 1,600      |
| Ukraine 2032  | Hold           | -         | 7.4    | Sep-32   | 6.2       | 110.1     | 1.6      | 7.8      | 3,000      |
| Avangard in default                                     | Sell           | 9-Apr-19  | 10.0   | Oct-18   | nm        | 3.4       | -0.1     | nm       | 214        |
| DTEK 2024 in default                                    | Buy            | 1-Dec-20  | 10.8   | Dec-24   | 27.3      | 65.4      | -0.3     | 2.7      | 1,344      |
| Kernel 2022   | Buy            | 1-Dec-20  | 8.8    | Jan-22   | 3.4       | 105.9     | 0.3      | 1.1      | 213        |
| Kernel 2024   | Buy            | 1-Dec-20  | 6.5    | Oct-24   | 4.9       | 105.6     | 0.8      | 3.3      | 300        |
| Kernel 2027   | Buy            | 1-Dec-20  | 6.8    | Oct-27   | 5.8       | 105.2     | 1.2      | 4.2      | 300        |
| Metinvest 2023  | Hold           | 8-Dec-20  | 7.8    | Apr-23   | 5.0       | 106.2     | 0.2      | 2.0      | 311        |
| Metinvest 2025 (EUR)                                    | Hold           | 8-Dec-20  | 5.6    | Jun-25   | 5.1       | 101.9     | 1.0      | 4.0      | 333        |
| Metinvest 2026  | Hold           | 8-Dec-20  | 8.5    | Apr-26   | 6.2       | 110.5     | 2.0      | 4.3      | 648        |
| Metinvest 2027  | Hold           | 8-Dec-20  | 7.7    | Oct-27   | 6.3       | 107.5     | 2.1      | 5.4      | 333        |
| Metinvest 2029  | Hold           | 8-Dec-20  | 7.8    | Oct-29   | 6.6       | 107.6     | 2.9      | 6.6      | 500        |
| MHP 2024  | Hold           | 24-Nov-20 | 7.8    | May-24   | 4.7       | 109.5     | 0.7      | 3.1      | 500        |
| MHP 2026  | Hold           | 24-Nov-20 | 7.0    | Apr-26   | 5.3       | 107.5     | 1.5      | 4.5      | 550        |
| MHP 2029  | Hold           | 24-Nov-20 | 6.3    | Sep-29   | 6.0       | 101.6     | 1.3      | 6.8      | 350        |
| Naftogaz 2022   | Buy            | 8-Dec-20  | 7.4    | Jul-22   | 5.4       | 103.0     | 0.0      | 1.5      | 335        |
| Naftogaz 2024 (EUR)                                     | Buy            | 8-Dec-20  | 7.1    | Jul-24   | 6.0       | 103.4     | 0.9      | 3.2      | 672        |
| Oschadbank 2023   | Buy            | 10-Nov-20 | 9.4    | Mar-23   | 5.5       | 104.5     | 0.4      | 1.2      | 175        |
| Oschadbank 2025   | Buy            | 10-Nov-20 | 9.6    | Mar-25   | 6.5       | 106.4     | 0.0      | 2.0      | 225        |
| Privatbank in default (10.250)                          | Not rated      | -         | 10.3   | nm       | nm        | 30.0      | 0.8      | nm       | 160        |
| Privatbank in default (10.875)                          | Not rated      | -         | 10.9   | nm       | nm        | 30.0      | 0.0      | nm       | 175        |
| Ukraine Railway 2021                                    | Sell           | 27-Oct-20 | 9.9    | Sep-21   | 7.4       | 101.2     | 0.1      | 0.5      | 100        |
| Ukraine Railway 2024                                    | Sell           | 27-Oct-20 | 8.3    | Jul-24   | 7.1       | 103.4     | 0.9      | 3.1      | 595        |
| Ukreximbank 2021 (UAH)                                  | Buy            | 10-Nov-20 | 16.5   | Mar-21   | 20.0      | 99.1      | 0.1      | 0.2      | 150        |
| Ukreximbank 2022  | Buy            | 10-Nov-20 | 9.6    | Apr-22   | 4.4       | 104.4     | 0.6      | 0.9      | 104        |
| Ukreximbank 2025  | Buy            | 10-Nov-20 | 9.8    | Jan-25   | 5.6       | 104.7     | 0.0      | 1.1      | 384        |
| Ukrlandfarming in default                               | Sell           | 13-Jun-17 | 10.9   | nm       | nm        | 4.7       | 0.0      | 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 - Monthly inflation              | Exact | 9-Dec  |
| NBU - Decision on the key policy rate | Exact | 10-Dec |

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