

Weekly Digest

- The IMF mission has started holding remote meetings with the Ukrainian authorities
- Real GDP in 3Q20 contracted by 3.5% YoY (final data)
- The Parliament has adopted the 2021 state budget with a 5.5% of GDP deficit

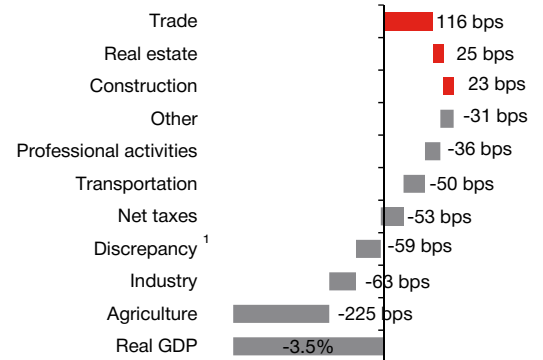
The IMF mission has started holding remote meetings with the Ukrainian authorities. According to the Fund's Resident Representative Ljungman, discussions will concern "economic developments, and policies and reforms to underpin the completion of the review." Talks will pause over the holidays after Dec 23, but will resume in January. As per PM Shmyhal, the government is expecting a new loan tranche to be disbursed in February or March.

Our view: The announced schedule confirms our earlier view that a staff-level agreement will not be reached by the end of 2020. Despite the fact that the 2021 state budget seems to have been agreed upon, the Fund is likely to ask Ukraine for more actions on anti-corruption. Additionally, amendments to the bank law (a November structural benchmark) will probably also need to be voted on by Parliament (so far it has only been submitted for review). While overall, we think that disbursement by end of 1Q21 is realistic, we do not exclude additional missteps from Zelensky's team, which can transform into further delays. That said, it is also possible that the IMF could agree to increase the tranche size significantly from the \$0.7bln stipulated in the memorandum, as the SBA will expire in October (\$3.0bln remains to be distributed) and most of the requirements scheduled for 2021 are relatively lax.

Real GDP in 3Q20 contracted by 3.5% YoY (final data). The updated figure did not deviate materially from the SSSU's preliminary estimate in November.

Our view: Based on the value-added contributions of each sector, we conclude that our original projections in October did not sufficiently capture the post-COVID recovery both with respect to the production side (tracked by the COI) as well as the service side of the economy. Real GDP also seemed to perform better than leading economic indicators. Trade, for example, demonstrated an overall increase of 9.7% YoY, despite wholesale volumes boasting a much more modest 6.5% growth. Transportation contracted by only 8.4% even though passengers travelled 40-60% less YoY. Finance generated a contribution equal to last year in spite of a 13% drop in the operating profit of the banking system (if revaluations and LLR formation is excluded). Other surprise rebounds in terms of magnitude include real estate services, which went from -5.9% to +4.3%, telecoms (-4.2% to +4.5%) and hospitality (-58% to -18%). On the whole, these observations allow us to adopt a slightly more positive view on growth prospects in 4Q20. That said, the difference is not large enough to significantly impact our -4.5% real GDP contraction forecast for the full year. That said, we do upgrade our growth outlook for 2021 by 50bps to 4.0%.

Real GDP growth contribution by sector in 3Q20



(1) The difference between total real GDP and the sum of the GDP contributions by sector
 Source: SSSU, Adamant Capital estimates

The Parliament has adopted the 2021 state budget with a 5.5% of GDP deficit. According to our estimates, consolidated (i.e. including local budget) revenues have been revised upwards, compared to the earlier draft, by 1% to UAH1,430bln (+6% YoY). Expenditures remained practically flat at UAH1,666bln (+11% YoY). Financing now assumes smaller net borrowing locally (UAH128bln vs UAH207bln previously), but a larger amount externally (UAH106bln vs UAH57bln before). Anticipated privatization proceeds were doubled to UAH12bln.

Our view: After conducting talks with the IMF, the FinMin ended up reducing the deficit target by 0.5ppts of GDP, practically without touching the expenditure side. We think that such a compromise became possible owing to an improved outlook on revenues in 2020, as these are now poised to surpass planned levels by almost 5%. That said, although growth now stands at just 6% YoY (compared to the 14% increase in nominal GDP), a sharp drop in non-tax income will need to be compensated by even higher proceeds from VAT, the administration of which seems to have recently toughened quite significantly (3Q20 net VAT to GDP ratio at 9.5% vs 8.4% last year). Financing assumptions on the domestic side look dependant on a loose monetary policy by the NBU (net borrowing slightly above 2020 levels at \$4.4bln net), which may actually need to toughen in light of the M1 money supply already being 40% above last year. External borrowing levels and privatization proceeds are contingent on restoring the reform momentum. Overall, we estimate 2021 budget execution risks to be elevated, but manageable.

2021 consolidated budget summary, UAHbln					
	2021F	2021D	F/D	2020E	YoY
Revenues	1,430	1,409	1%	1,345	6%
VAT	469	463	1%	396	18%
Net local VAT	136	131	4%	123	10%
Import VAT	333	333	0%	273	22%
CIT ¹	118	116	2%	116	1%
Excise tax	154	154	0%	149	4%
PIT ²	349	351	0%	294	19%
Royalties	46	45	1%	36	25%
Import duties	32	30	8%	30	7%
Local taxes	84	84	0%	75	12%
Non-tax revenues	167	155	8%	230	-27%
NBU transfers	33	33	0%	43	-23%
Corp profit transfers	29	25	17%	76	-62%
Other	11	11	0%	18	-37%
Expenditures	1,666	1,668	0%	1,498	11%
Wages	514	514	0%	442	16%
Debt servicing	162	163	-1%	130	25%
Social protection	323	331	-2%	318	1%
Other	667	660	1%	608	10%
Net loans	11	11	0%	11	-6%
Deficit	247	270	-9%	165	50%
as % of GDP	5.5%	6.0%	0.5ppts	4.1%	1.4ppts
Nominal GDP	4,506	4,506	0%	4,009	12%
Average CPI	8.1%	8.1%	0pps	2.7%	5.4ppts
UAH/\$ rate assumption	29.1	29.1	0%	27.0	8%

Note:

(1) Corporate income tax

(2) Personal income tax

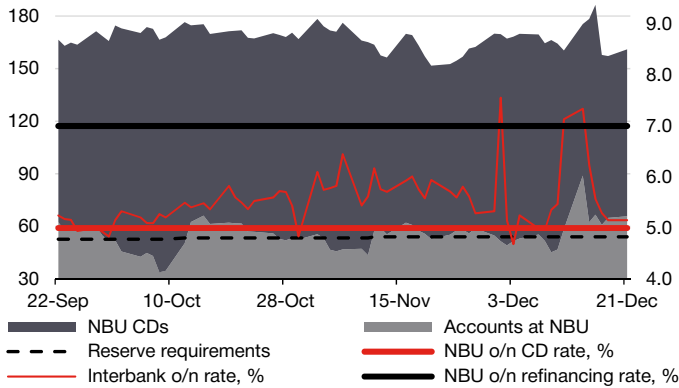
F and D stand for the final and draft versions of the 2021 budget.

Figures for 2020 represent Adamant Capital estimates

Source: SSSU, State Treasury, Adamant Capital estimates

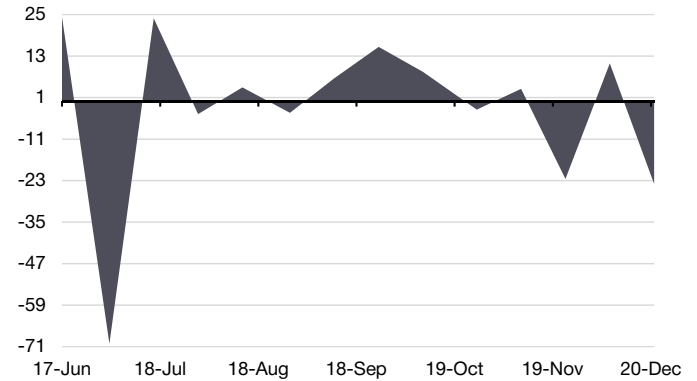
Appendix

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

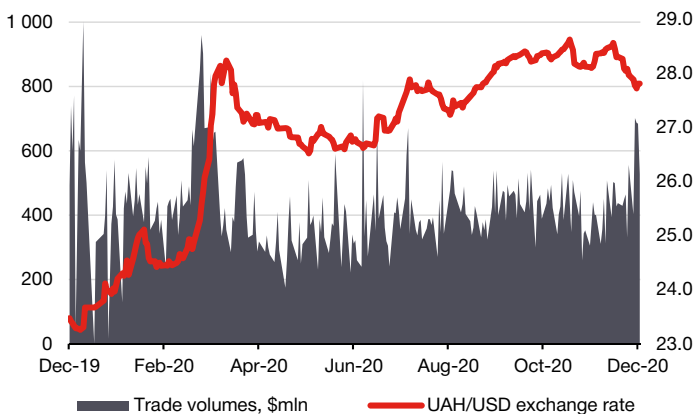


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has decreased by UAH 14.4bln to UAH 161.0bln over the last week. On December 22 the Ministry of Finance conducted local hryvnia denominated placement maturing in March 2021, April 2021, July 2021, December 2021, June 2022, February 2023, November 2023, May 2024 and February 2025 with yields of 10.00%, 10.25%, 10.75%, 11.62%, 11.75%, 11.85%, 12.00%, 12.15% and 12.25% respectively and USD denominated placement maturing in December 2021 with yield of 3.80%. A total of UAH 18.3bln and \$138mln was raised as a result.

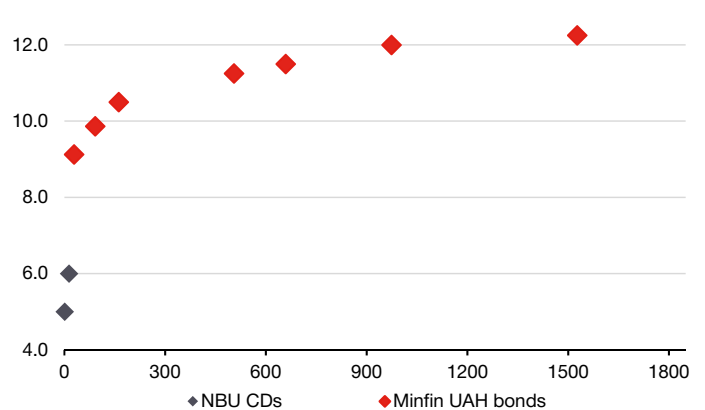
The UAH/USD interbank rate over the last week depreciated by 0.39%, starting out with 27.88 and ending at 27.99.

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



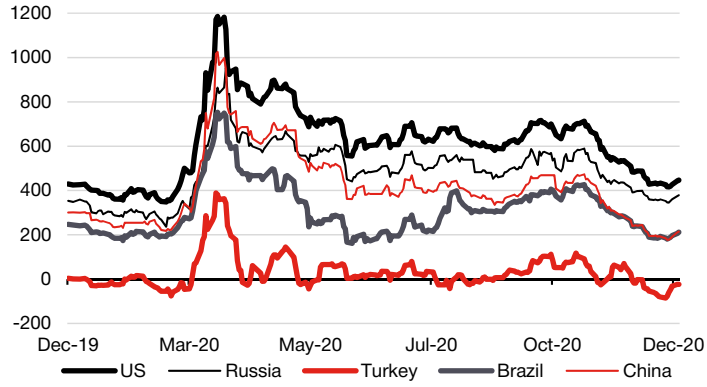
Note: Exchange rate figures are from official interbank data
Source: NBU

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



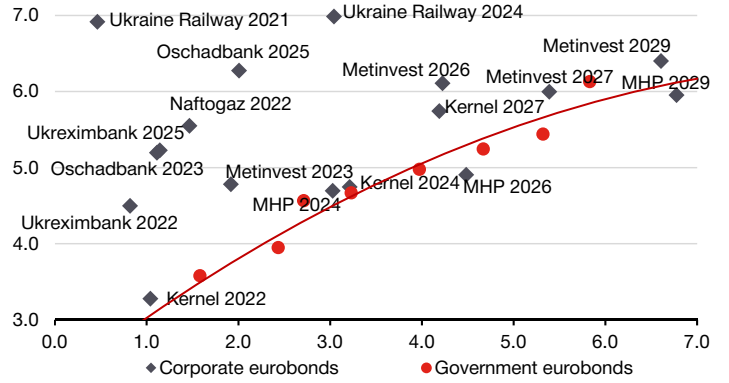
Source: NBU, Bloomberg, Adamant Capital estimates

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



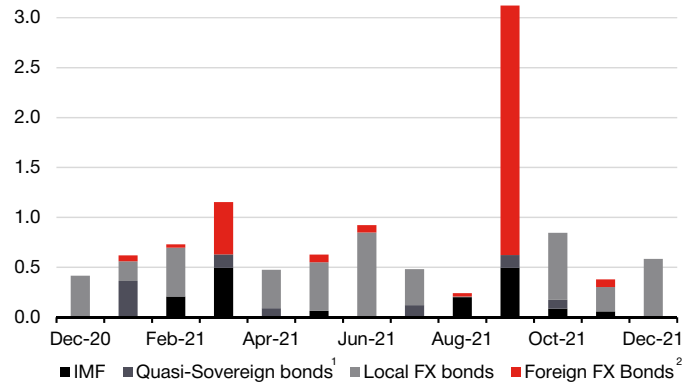
Source: Bloomberg, Adamant Capital estimates

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



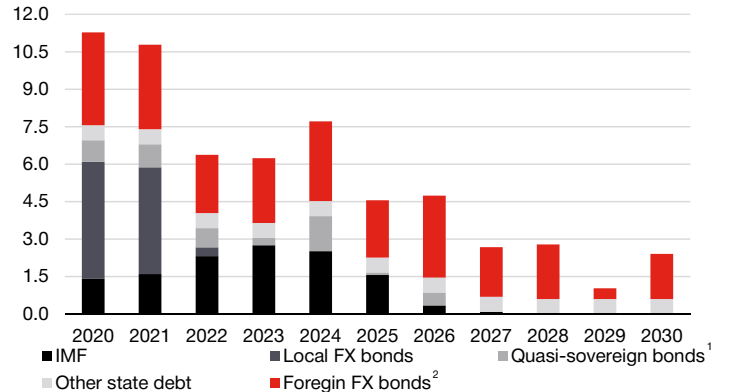
Source: Bloomberg, Adamant Capital estimates

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



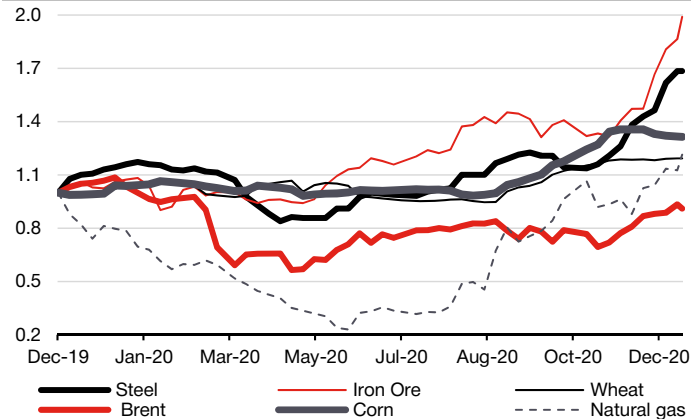
Note: Interest included in each category
 (1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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



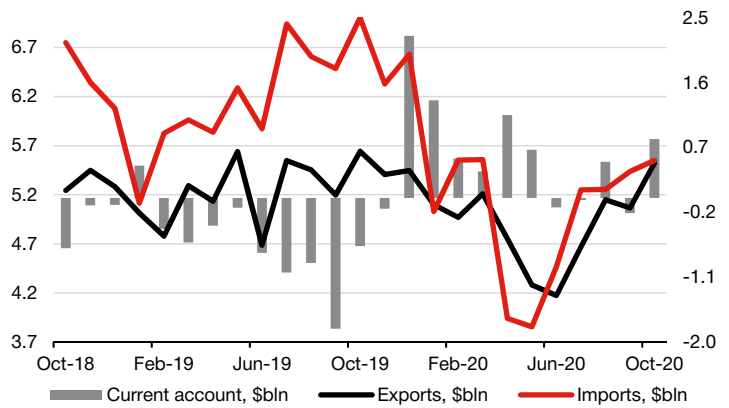
(1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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								
	4Q19	2019	1Q20	2Q20	3Q20	4Q20E	2020E	2021E
Real GDP growth, YoY	1.5%	3.2%	-1.3%	-11.4%	-3.5%	-2.0%	-4.5%	4.0%
Nominal GDP, UAHbln	1,115	3,975	846	868	1,158	1,138	4,009	4,420
Nominal GDP, \$bln	46	154	34	32	42	41	149	152
GDP deflator growth YoY, %	4.7%	8.1%	5.1%	5.0%	7.9%	4.2%	5.6%	6.0%
Period average CPI YoY, %	5.2%	7.9%	2.6%	2.1%	2.4%	3.8%	2.7%	6.6%
End of period CPI YoY, %	4.1%	4.1%	2.3%	2.4%	2.3%	4.9%	4.9%	6.2%
Consolidated budget deficit, % of GDP ¹	2.1%	2.1%	2.3%	1.7%	3.3%	5.8%	5.8%	5.3%
Broad public sector deficit, % of GDP ²	2.1%	2.2%	2.3%	2.2%	3.9%	6.4%	6.4%	5.6%
Public debt as % of LTM GDP, UAH	50.3%	50.3%	56.3%	57.6%	58.8%	60.0%	59.3%	61%
Public external debt as % of LTM GDP, \$ ³	31.6%	31.6%	31.6%	31.7%	33.3%	34.8%	34.4%	36%
Total external debt, \$bln	122	122	120	123	123	127	127	133
Export of goods and services, \$bln	16.5	63.4	15.3	13.2	14.9	17.6	60.9	67.2
Import of goods and services, \$bln	20.0	75.5	16.1	12.3	15.9	16.8	61.1	70.5
Trade balance, \$bln	-3.5	-12.1	-0.9	0.9	-1.1	0.8	-0.2	-3.3
Current account, \$bln	1.4	-1.1	2.3	1.7	0.3	2.3	6.5	2.2
Financial account, \$bln ⁴	-2.3	-10.2	2.4	0.4	2.0	-1.5	3.2	-2.2
End of period NBU reserves, \$bln	25.3	25.3	24.9	28.5	26.5	28.0	28.0	32.0
Average interbank exchange rate, UAH/\$ ⁵	24.2	25.8	25.2	26.9	27.6	28.1	27.0	29.0
EOP interbank exchange rate, UAH/\$	23.7	23.7	27.6	26.7	28.3	28.0	28.0	29.5
EOP key policy rate NBU, %	13.5%	13.5%	10.0%	6.0%	6.0%	6.0%	6.0%	8.0%

(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	3.9	109.6	-0.5	2.4	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	4.6	112.7	-0.6	2.7	750
Ukraine 2027	Hold	-	7.8	Sep-27	5.4	112.8	-1.9	5.3	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	6.1	122.3	-1.6	5.8	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	6.3	108.9	-1.9	7.7	3,000
Avangard in default	Sell	9-Apr-19	10.0	Oct-18	nm	3.6	0.7	nm	214
DTEK 2024 in default	Buy	1-Dec-20	10.8	Dec-24	29.8	62.0	-3.6	2.6	1,344
Kernel 2022	Buy	1-Dec-20	8.8	Jan-22	3.3	105.9	0.3	1.0	213
Kernel 2024	Buy	1-Dec-20	6.5	Oct-24	4.7	106.1	-0.1	3.2	300
Kernel 2027	Buy	1-Dec-20	6.8	Oct-27	5.7	105.6	-0.3	4.2	300
Metinvest 2023	Hold	8-Dec-20	7.8	Apr-23	4.8	106.5	-0.3	1.9	311
Metinvest 2025 (EUR)	Hold	8-Dec-20	5.6	Jun-25	4.8	103.5	0.2	4.0	333
Metinvest 2026	Hold	8-Dec-20	8.5	Apr-26	6.1	110.7	0.1	4.2	648
Metinvest 2027	Hold	8-Dec-20	7.7	Oct-27	6.0	109.1	-0.4	5.4	333
Metinvest 2029	Hold	8-Dec-20	7.8	Oct-29	6.4	109.0	-0.6	6.6	500
MHP 2024	Hold	24-Nov-20	7.8	May-24	4.7	109.4	-0.2	3.0	500
MHP 2026	Hold	24-Nov-20	7.0	Apr-26	4.9	109.4	-0.2	4.5	550
MHP 2029	Hold	24-Nov-20	6.3	Sep-29	6.0	102.0	-0.3	6.8	350
Naftogaz 2022	Buy	8-Dec-20	7.4	Jul-22	5.5	102.7	-0.4	1.5	335
Naftogaz 2024 (EUR)	Buy	8-Dec-20	7.1	Jul-24	6.0	103.5	-0.2	3.2	672
Oschadbank 2023	Buy	10-Nov-20	9.4	Mar-23	5.2	104.7	-0.1	1.1	175
Oschadbank 2025	Buy	10-Nov-20	9.6	Mar-25	6.3	106.7	0.0	2.0	225
Privatbank in default (10.250)	Not rated	-	10.3	nm	nm	30.0	0.0	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	6.9	101.3	-0.1	0.5	100
Ukraine Railway 2024	Sell	27-Oct-20	8.3	Jul-24	7.0	103.9	0.0	3.0	595
Ukreximbank 2021 (UAH)	Buy	10-Nov-20	16.5	Mar-21	20.7	99.1	0.0	0.2	150
Ukreximbank 2022	Buy	10-Nov-20	9.6	Apr-22	4.5	104.2	-0.2	0.8	104
Ukreximbank 2025	Buy	10-Nov-20	9.8	Jan-25	5.2	105.0	0.0	1.1	384
Ukrlandfarming in default	Sell	13-Jun-17	10.9	nm	nm	4.0	-0.7	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	23-Dec
Metinvest - Monthly report for October	Indicative	28-Dec
Treasury - Monthly state budget performance	Indicative	28-Dec

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