

Weekly Digest

- Real GDP in 2Q21 grew by 5.7% YoY (final data)
- Draft 2022 consolidated budget submitted to parliament: planned deficit at 3.5% of GDP
- DTEK posted a \$5mIn EBITDA loss in 2Q21

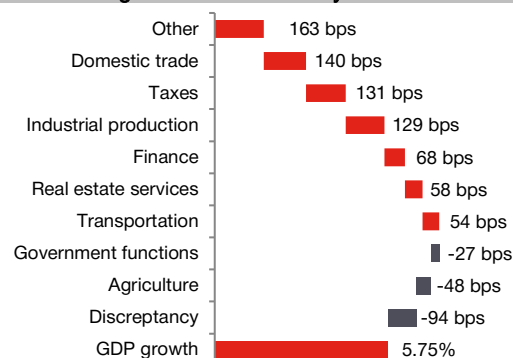
Real GDP in 2Q21 grew by 5.7% YoY (final data). This figure was bumped up by 30bps from the SSSU's preliminary estimate in August.

Our view: Taking into account our initial sub-consensus projection of 6.3%, the overall GDP dynamic ended up landing within reasonable bounds of the expected level. As anticipated, growth was driven primarily by a low base induced by COVID-19 lockdowns in 2020. Impeding factors included lacklustre performance of industrial production (up just 6.3% YoY despite an 11.8% contraction last year), which suffered, in part, from a lower output of consumer goods, a delayed start to the crop harvesting campaign, and a smaller state sector footprint (budget expenditures dropped in real terms). What we did find surprising, however, is that high frequency indicators for domestic trade and transportation ended up leading us somewhat astray. In the case of the former, we anticipated that a double-digit drop in wholesale volumes over May and June would impact the value-added figure to a greater degree. The latter, on the other hand, seems to have largely shrugged off the fact that passenger volumes have quadrupled YoY (sector GDP expanded by just 9.6%). We attribute both of these instances to low quality of early data.

With regard to the expenditure side, it is worth noting that capex as a share of GDP rebounded from last year's 16.5% level to 18.2%, which is much closer to the 2018-19 pre-pandemic amount. A nominal breakdown of the totals from a different set of SSSU accounts implies that extra funds went towards industrials (makes sense given high commodity prices) and retail (this sector was actually boosted by COVID).

All in all, the reported data not deliver any major surprises, and though actual figures did come in somewhat below projections, we feel that the deviation is not large enough to require a revision of our 4.0% growth forecast. In nominal terms, GDP is likely to receive a much larger boost (c. 26%) this year from domestic inflation, a fact that Ukraine's VRI investors are likely to appreciate.

Real GDP growth contribution by sector in 2Q21



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

Draft 2022 consolidated budget submitted to parliament: planned deficit at 3.5% of GDP (UAH 188bln). According to the document, central budget revenues are expected to grow by 14.4% YoY to UAH1,267bln. Macroeconomic assumption used include real GDP growth of 3.8% and average CPI at 7.2%. Financing envisions \$1.5bln raised via eurobonds, \$2.5bln worth of net local T-bill sales, and \$2.9bln received from donor programs (the IMF and other IFIs).

Our view: Taking into account that we expect actual 2021 consolidated revenues to outperform the official target by as much as 13%, the draft 2022 figures look surprisingly tame. We think that the main reason for this is that the government is significantly underestimating the rate of deflator growth (surpassed 26% in 2Q21), and thus the size of the nominal GDP. The deficit target was set fully in line with the earlier approved medium-term (2022-24) budget declaration, and should thus be palatable for the IMF. Financing sources look the least realistic, in our view, especially with respect to fundraising on the local market, where the FinMin was so far (YTD) unable to fully roll-over existing obligations.

2022 consolidated budget draft, UAHbln			
	2022P	2021E	YoY
Revenues	1,672	1,606	4%
VAT	565	499	13%
Net local VAT	166	151	10%
Import VAT	398	348	15%
CIT ¹	152	171	-11%
Excise tax	171	162	5%
PIT ²	408	358	14%
Royalties	52	75	-30%
Import duties	36	35	2%
Local taxes	96	91	6%
Non-tax revenues	178	194	-8%
NBU transfers	24	24	0%
Corp profit transfers	49	27	82%
Other	13	21	-40%
Expenditures	1,846	1,814	2%
Wages	552	489	13%
Services received	163	186	-12%
Debt servicing	189	122	54%
Social protection	348	333	5%
Capex	185	230	-20%
Other	409	641	-36%
Net loans	13	5	195%
Deficit	188	213	-12%
as % of GDP	3.5%	4.0%	-0.5pps
Nominal GDP assumption	5,369	5,319	1%
Avg CPI assumption	7.2%	9.0%	-1.8pps
Avg UAH/\$ rate assumption	28.6	27.7	3%

Note:

(1) Corporate income tax

(2) Personal income tax

P and E stand for officially planned and estimated by Adamant Capital, respectively

Source: SSSU, State Treasury, Adamant Capital estimates

DTEK posted a \$5mln EBITDA loss in 2Q21. According to condensed unaudited results, revenues grew by 16% YoY to \$330mln and net income came in just below breakeven (vs -\$291mln last year). Operating cash flow contracted by \$22mln to -\$31mln. Free cash flow slipped by \$31mln to -\$67mln, as capex was up by 35% to \$36mln. Net debt to LTM EBITDA decreased by 8% to 4.8 (down 15% QoQ), reflecting the placement discount on the new bonds. During its conference call for investors, the company announced that it expects full-year EBITDA to reach the level presented in its business plan (\$389mln). Profitability in 2H21 should improve on the back of higher electricity prices on the local market.

Our view: The EBITDA figure for the quarter came in weaker than anticipated primarily owing to a c. 35% QoQ surge in estimated generation costs. According to management, production overheads went up on the back of more expensive coal, roughly 20% of which, over 1H21, the company had to purchase from third parties (the share was probably even larger for 2Q21 alone). Additional pressure was created by higher natural gas prices, though the latter is currently only being used to start blocks and not during operations. That said, the electricity price outlook for 2H21 currently looks quite a bit stronger than we previously budgeted (up some 35% YoY for 3Q21 so far), which means that DTEK's generation margin may grow YoY despite higher expenses per MWh. Although we are somewhat doubtful that 2021 EBITDA will end up reaching the \$389mln business plan target (though it is noteworthy that our EBITDA calculation slightly differs from that of the company), we feel that our previous \$300mln guidance remains valid. With regard to DTEK's 2027 eurobond, which is currently quoted at just 62% of par, we maintain our recommendation at a 'Buy'. As before, we think that the company and its majority shareholder possess a sufficient amount of political clout to pressure the government into shaping Ukraine's budding electricity market into one which will enable profit generation, at least in the medium term. The recent electricity price surge, which followed an administrative 50-60% DAM price cap increase, is a testament to this fact, in our view.

DTEK 2Q21 financial results, \$mln					
	2Q21	2Q20	YoY	1Q21	QoQ
Revenues	330	285	16%	516	-36%
EBITDA ¹	-5	39	nm	91	nm
EBITDA margin	-2%	14%	-15pp	18%	-19pp
Net income	-6	-291	nm	-12	nm
Net income margin	-2%	-102%	100pp	-2%	1pp
Operating cash flow	-31	-9	nm	63	nm
Capex	36	26	35%	36	0%
Free cash flow	-67	-36	nm	28	nm
Elec. price ² , UAH/MWh	1,435	1,171	23%	1,417	1%
Elec. price, \$/MWh	52.0	43.5	20%	50.7	3%
Elec. generation, TWh	4.2	5.0	-16%	7.4	-43%
EBITDA/MWh output, \$	-1.2	7.8	nm	12.3	nm
Net debt	1,522	1,986	-23%	2,071	-27%
Net debt/LTM EBITDA	4.8	5.2	-8%	5.7	-16%

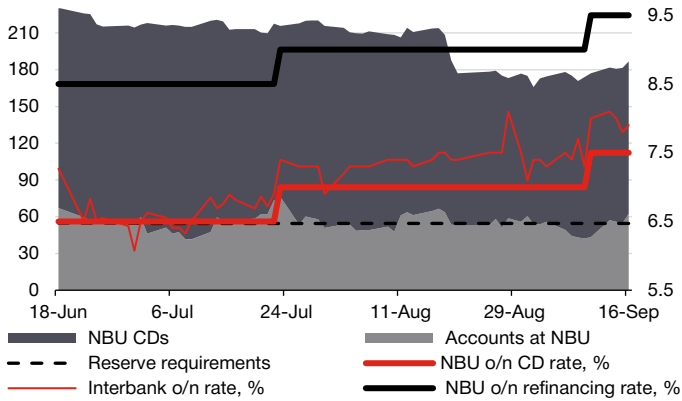
(1) Excludes impairments and other non-cash items that are part of operating profit

(2) The average realized domestic wholesale electricity price reported by DTEK

Source: Company data, Adamant Capital estimates

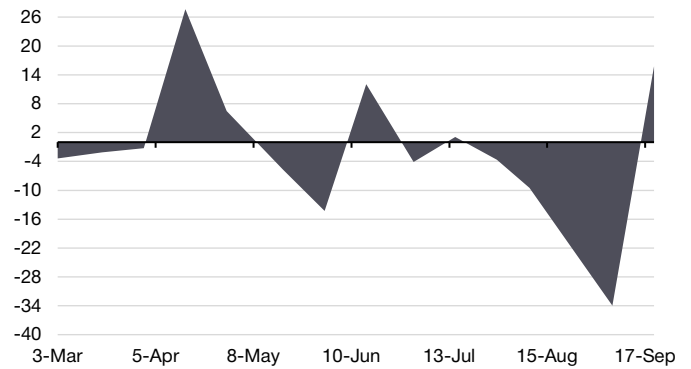
Appendix

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

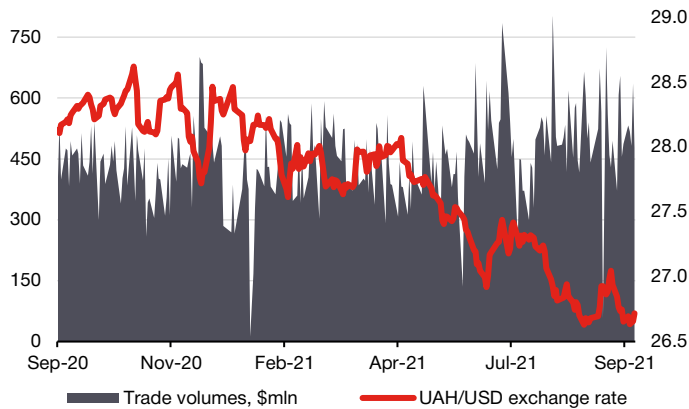


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has increased by UAH 14.39bln to UAH 191.3bln over the last week. On September 21 the Ministry of Finance conducted local hryvnia bond denominated placements maturing in February 2022, August 2022, November 2022, November 2023, and July 2024 with yields of 9.70%, 11.49%, 11.47%, 12.34%, and 12.49% respectively. Dollar denominated bonds maturing in October 2023 were sold at a yield of 3.90%. In total, an equivalent of UAH 5.0bln was raised as a result.

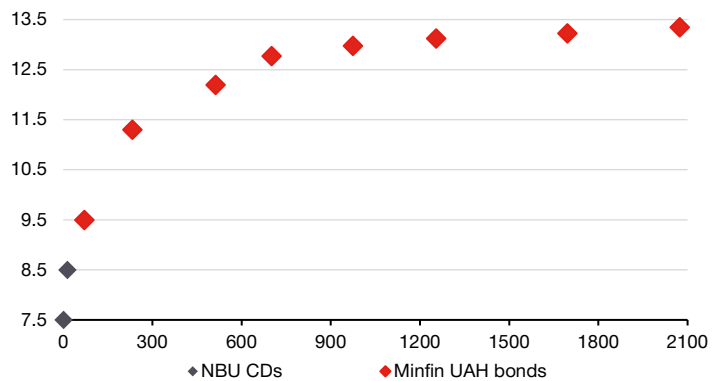
The UAH/USD interbank rate over the last week appreciated by 0.09%, starting out with 26.69 and ending at 26.72.

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



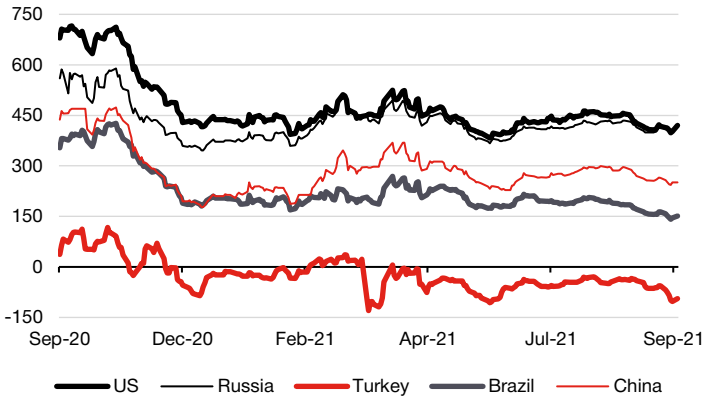
Note: Exchange rate figures are from official interbank data
Source: NBU

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



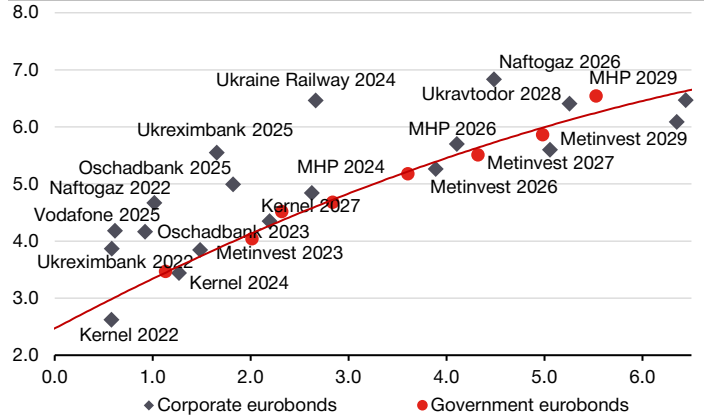
Source: NBU, Bloomberg, Adamant Capital estimates

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



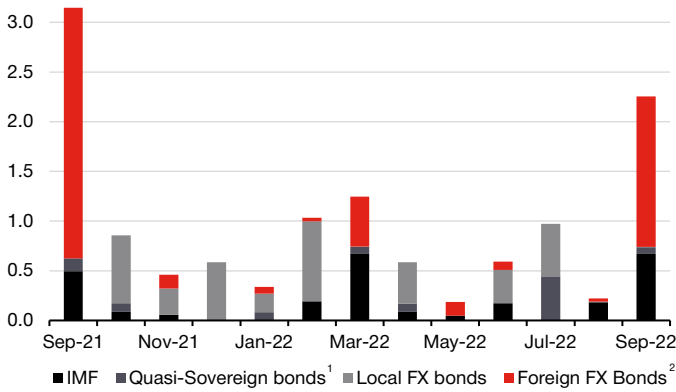
Source: Bloomberg, Adamant Capital estimates

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



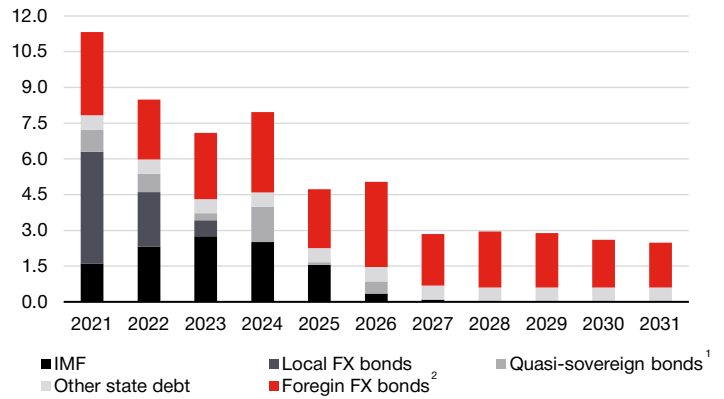
Source: Bloomberg, Adamant Capital estimates

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



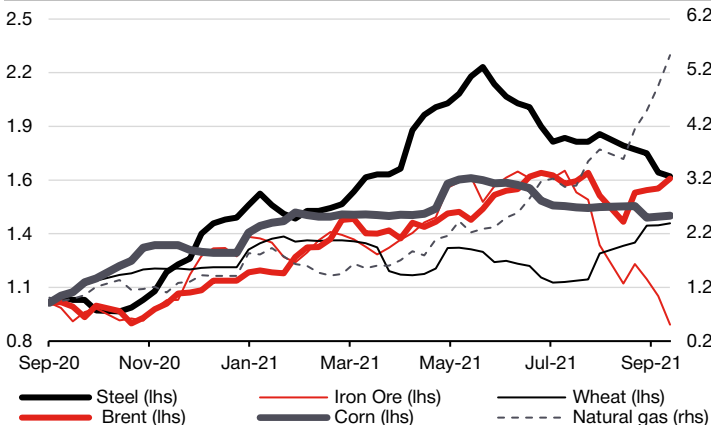
Note: Interest included in each category
 (1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

State and NBU FX debt repayment schedule 2021-31, \$bln



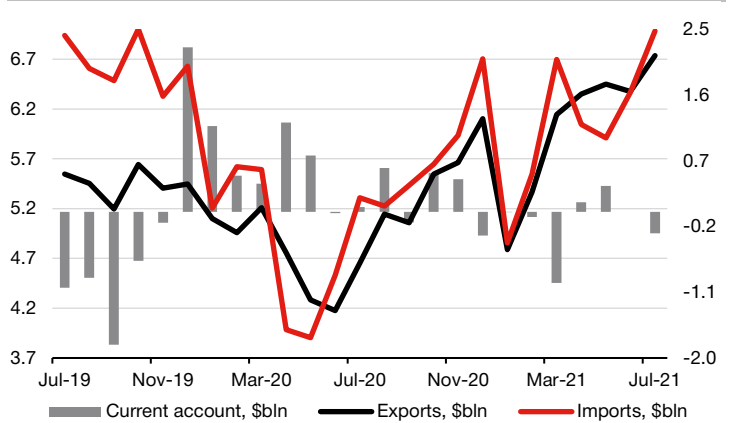
(1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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								
	2Q20	3Q20	4Q20	2020	1Q21	2Q21E	3Q21E	2021E
Real GDP growth, YoY	-11.2%	-3.5%	-0.5%	-4.0%	-2.2%	5.7%	6.0%	4.0%
Nominal GDP, UAHbln	875	1,162	1,301	4,192	1,009	1,169	1,571	5,503
Nominal GDP, \$bln	33	42	46	155	36	42	58	199
GDP deflator growth YoY, %	5.6%	8.4%	17.5%	9.8%	20.7%	26.4%	27.5%	26.2%
Period average CPI YoY, %	2.1%	2.4%	3.8%	2.7%	7.4%	9.1%	10.1%	9.0%
End of period CPI YoY, %	2.4%	2.3%	5.0%	5.0%	8.5%	9.5%	10.0%	9.0%
Consolidated budget deficit, % of GDP ¹	1.7%	3.3%	5.3%	5.3%	4.9%	5.1%	3.1%	4.0%
Broad public sector deficit, % of GDP ²	2.3%	4.1%	6.5%	6.5%	6.2%	6.3%	4.6%	4.3%
Public debt as % of LTM GDP, UAH	57.4%	58.6%	60.9%	60.9%	57.8%	54.2%	51.4%	50.7%
Public external debt as % of LTM GDP, \$ ³	31.6%	33.1%	34.8%	34.8%	33.2%	32.6%	30.9%	29.0%
Total external debt, \$bln	122	122	126	126	123	125	127	130
Export of goods and services, \$bln	13.2	14.9	17.3	60.6	16.3	19.2	22.5	82.6
Import of goods and services, \$bln	12.3	15.9	17.8	62.3	17.1	18.3	20.1	77.5
Trade balance, \$bln	0.9	-1.1	-0.5	-1.7	-0.8	0.9	2.4	5.1
Current account, \$bln	1.7	0.3	1.6	6.6	-1.0	1.4	1.0	3.0
Financial account, \$bln ⁴	0.8	2.4	-0.9	4.6	-0.1	0.2	3.5	-0.5
End of period NBU reserves, \$bln	28.5	26.5	29.1	29.1	27.0	28.4	25.9	32.2
Average interbank exchange rate, UAH/\$ ⁵	26.9	27.6	28.3	27.0	27.9	27.6	27.2	27.7
EOP interbank exchange rate, UAH/\$	26.7	28.3	28.2	28.2	27.8	27.2	27.2	27.6
EOP key policy rate NBU, %	6.0%	6.0%	6.0%	6.0%	6.5%	7.5%	8.5%	8.5%

(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	4.0	107.7	-0.5	2.0	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	4.5	110.9	-1.0	2.3	750
Ukraine 2027	Hold	-	7.8	Sep-27	5.9	109.6	-1.4	5.0	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	6.5	118.5	-1.5	5.5	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	6.9	103.7	-2.1	7.4	3,000
DTEK 2027	Buy	21-Sep-21	5.0	Dec-27	na	64.0	0.1	na	1,645
Kernel 2022	Hold	27-Jul-21	8.8	Jan-22	2.6	103.6	0.1	0.6	213
Kernel 2024	Hold	27-Jul-21	6.5	Oct-24	3.4	107.0	0.0	1.3	300
Kernel 2027	Buy	27-Jul-21	6.8	Oct-27	4.4	108.3	-0.1	2.2	300
Metinvest 2023	Hold	07-Sep-21	7.8	Apr-23	3.8	106.8	0.0	1.5	195
Metinvest 2025 (EUR)	Hold	07-Sep-21	5.6	Jun-25	4.1	105.5	-0.5	3.6	333
Metinvest 2026	Hold	07-Sep-21	8.5	Apr-26	5.3	113.6	-0.3	3.9	648
Metinvest 2027	Hold	07-Sep-21	7.7	Oct-27	5.6	110.7	-0.4	5.1	333
Metinvest 2029	Hold	07-Sep-21	7.8	Oct-29	6.1	110.7	-0.6	6.4	500
MHP 2024	Buy	14-Sep-21	7.8	May-24	4.8	107.7	-0.3	2.6	500
MHP 2026	Buy	14-Sep-21	7.0	Apr-26	5.7	105.1	-0.4	4.1	550
MHP 2029	Buy	14-Sep-21	6.3	Sep-29	6.5	98.6	0.0	6.4	350
Naftogaz 2022	Buy	11-May-21	7.4	Jul-22	4.7	102.8	0.2	1.0	335
Naftogaz 2024 (EUR)	Buy	11-May-21	7.1	Jul-24	5.7	103.8	-0.3	2.7	672
Naftogaz 2026	Buy	11-May-21	7.6	Nov-26	6.8	103.5	-0.4	4.5	500
Oschadbank 2023	Buy	10-Aug-21	9.4	Mar-23	4.2	104.8	-0.2	0.9	140
Oschadbank 2025	Buy	10-Aug-21	9.6	Mar-25	5.0	108.5	0.0	1.8	200
Ukraine Railway 2024	Buy	3-Aug-21	8.3	Jul-24	6.5	104.8	0.2	2.7	595
Ukravtodor 2028	Hold	22-Jun-21	6.3	Jun-28	6.4	99.1	0.0	5.3	700
Ukreximbank 2022	Buy	10-Aug-21	9.6	Apr-22	3.9	103.3	-0.2	0.6	104
Ukreximbank 2025	Buy	10-Aug-21	9.8	Jan-25	5.6	107.1	0.0	1.7	192
Vodafone 2025	Hold	18-May-21	6.2	Feb-25	4.2	104.3	-0.5	0.6	451

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-Sep
Naftogaz - 1H19 results	Indicative	23-Sep
SSSU - Transportation monthly data	Exact	27-Sep
Treasury - Monthly state budget performance	Indicative	27-Sep

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