

Weekly Digest

- The current account swung to a \$0.2bln surplus in August
- Kernel Holding 4Q21 EBITDA grew by 10% YoY to \$161mln
- Metinvest's EBITDA in July remained flat MoM at \$0.8bln

The current account swung to a \$0.2bln surplus in August, up \$0.4bln YoY. In LTM terms the figure landed at a \$0.3bln deficit, versus a \$1.4bln surplus a year ago (excluding the \$2.9bln arbitration payment to Naftogaz). The monthly trade balance (of goods and services) improved by \$0.4bln YoY to -\$0.2bln. The FA demonstrated a \$0.1bln increase in net assets.

Our view: The reported CA surplus for August landed below our projection, primarily owing to an overly optimistic outlook on exports, especially with regard to agriculture. Wheat was one such item, where the average realized price unexpectedly contracted instead of growing in line with the Black Sea index. Sunflower oil shipments slipped to just 0.2mlnt versus 0.3mlnt last year. Metals prices turned out to be higher than anticipated, but this difference was compensated by weaker sales of machinery and goods in the 'other' category. Imports fared mostly in line with estimates, with an uptick in travel-related services being the only sizeable surprise. This deviation occurred predominantly due to a revision of historical figures by the NBU and is significant, as it demonstrates a quicker recovery from COVID-19 effects than was previously believed. Together with a deterioration in the overall terms of trade for Ukraine (energy prices are skyrocketing while other commodities have started to trend downward), we find these arguments to be strong enough to warrant a downward revision of our annual CA surplus guidance from a \$3.0bln to just \$0.5bln (0.4% of GDP). Early customs data for September, which demonstrates a \$0.9bln MoM deterioration in the TB for goods is a sign of things to come. The increase in net assets registered by the FA during the month primarily reflects a jump in FX cash stocks outside of the banking system. According to NBU estimates, these grew by \$0.7bln, marking a 16-month record, and were sufficient to counterbalance the decrease in non-resident holding of hryvnia denominated debt.

BoP summary for August, \$mln

| | Aug-21 | Jul-21 | Jun-21 | LTM | LTM-1 |
|---------------------------|--------|--------|--------|--------|--------|
| Exports: | 7,450 | 6,748 | 6,339 | 72,082 | 60,201 |
| MoM | 10% | 6% | -3% | | |
| YoY | 45% | 45% | 52% | 20% | -3% |
| Imports: | 7,373 | 7,218 | 6,450 | 74,175 | 66,239 |
| MoM | 2% | 12% | 7% | | |
| YoY | 41% | 36% | 42% | 12% | -11% |
| TB: | 77 | -470 | -111 | -2,093 | -6,038 |
| MoM | 547 | -359 | -581 | | |
| YoY | 149 | 176 | 250 | 3,945 | 6,363 |
| CA ¹ : | 205 | -378 | -112 | -286 | 1,442 |
| MoM | 583 | -266 | -444 | | |
| YoY | -402 | -454 | -89 | -1,728 | 8,508 |
| FA: | 76 | -861 | -864 | -1,727 | -989 |
| MoM | 937 | 3 | -1,481 | | |
| YoY | -178 | -1,026 | 135 | -738 | 10,853 |
| BoP: | 126 | 484 | 753 | 1,440 | 5,342 |
| MoM | -358 | -269 | 1,033 | | |
| YoY | -227 | 572 | -225 | -3,902 | 524 |
| Funding flow ² | 611 | 924 | 665 | 5,693 | 5,753 |

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

Kernel Holding 4Q21 EBITDA grew by 10% YoY to \$161m (excluding IAS 41 effects). Extra profits were generated by the infrastructure and trading division (+\$47m overall, with Avere alone at an estimated +\$100m) as well as farming (+\$38m). Oilseed processing posted a loss on the operating level and dropped its contribution by \$74m versus last year. OCF contracted by 51% YoY, owing to a significantly smaller working capital release. Free cash dropped by 69%, stemming additionally from a 146% bump in capex. LTM net debt to EBITDA (including IAS 41 and IFRS 16) eased back to just 0.9 from 2.2 in 4Q20. In his annual statement, Kernel's chairman announced the completion of the company's Strategy 2021, which saw over \$1.0bn invested in greenfield and M&A projects and targeted a 12-month EBITDA level of \$500m as an outcome, and presented a new action plan for the next 5 years. The business will now be aiming to crush 6 mlnt of oilseeds, export 15mlnt of grain, and cultivate crops on 0.7mln hectares per year by 2026 (up c. 90%, 90%, and 40% from current levels, respectively). Additionally, according to the new capital allocation policy, in the foreseeable future Kernel will maintain a baseline dividend of \$35.6m, continue to execute its recently announced \$250m 2-year share buyback program, and re-invest the remaining funds into the business (anything not spent will go towards de-leveraging). Finally, in 2022 the company will attempt to export 11mlnt of grain, transship 10mlnt of soft commodities through its terminal, and process 3.7mlnt of oilseeds (+38%, +23%, and +16% YoY, respectively). Margins are expected to increase owing to a record crop harvest in Ukraine, though skyrocketing energy prices were noted as a concern.

Our view: Despite crushing margins coming in below our estimates and management guidance, Kernel ended up generating 23% more in absolute EBITDA during the final quarter of the year than we projected. The main reason for this is the performance of Avere, which surprised with another set of very strong results. Over the last 12 months this financial trading operation was able to deliver an astonishing \$325m, which is equivalent to 50% of the company's consolidated total. While such performance is no doubt good news for all stakeholders this year, we find it hard to believe that it can be repeated in 2022 or, for that matter, the foreseeable future. Budgeting for a reduced impact, and taking into account the current level of soft commodity prices, we see no reason to deviate from our previous FY22 EBITDA projection of \$600m at this time (including IFRS 16, but excluding IAS 41). Accounting for the updated capex guidance from management, we estimate end-of-year leverage at 1.5, which still looks very strong. That said, as its 2022 and 2024 notes currently trade at sub-sovereign levels, we maintain our recommendation to 'Hold' them (including the 2027 issue, which we previously preferred).

| Kernel Holding 4Q21 IFRS results, \$m | | | | | |
|---------------------------------------|-------|-------|-------|-------|-------|
| | 4Q21 | 4Q20 | YoY | 3Q21 | QoQ |
| Revenue | 1,651 | 1,183 | 40% | 1,729 | -5% |
| EBITDA | 224 | 123 | 81% | 111 | 101% |
| IAS 41 gain/loss | 63 | -23 | nm | -58 | nm |
| EBITDA adjusted ¹ | 161 | 147 | 10% | 170 | -5% |
| Oilseed processing | -6 | 64 | -110% | 7 | -188% |
| Infrastructure & trade | 102 | 55 | 86% | 122 | -16% |
| Farming | 93 | 55 | 67% | 61 | 51% |
| IFRS 16 effect | 3 | 27 | -89% | 11 | -73% |
| Other | -28 | -28 | 0% | -20 | nm |
| Adj EBITDA margin | 10% | 12% | -3pp | 10% | 0pp |
| Net profit | 186 | 40 | 362% | 53 | 251% |
| Net profit margin | 11% | 3% | 8pp | 3% | 8pp |
| Net debt | 836 | 980 | -15% | 1,073 | -22% |
| Net debt/EBITDA | 0.9 | 2.2 | -58% | 1.4 | -31% |
| Net debt/Adj EBITDA ¹ | 1.1 | 2.1 | -48% | 1.4 | -24% |
| Adj net debt/EBITDA ² | 0.7 | 1.6 | -54% | 0.7 | 7% |
| Operating cash flow | 218 | 449 | -51% | 151 | 44% |
| Capex | 98 | 40 | 146% | 31 | 220% |
| Free cash flow | 127 | 412 | -69% | 231 | -45% |
| Vegetable oil sales, kt | 273 | 489 | -44% | 372 | -27% |
| Oil EBITDA/t, \$ | -22 | 131 | -117% | 19 | -220% |

(1) Excluding IAS 41

(2) Net debt adjusted for readily marketable inventories and LTM EBITDA for IAS41

Source: company data, Adamant Capital estimates

Metinvest's EBITDA in July remained flat MoM at \$0.8bln (excluding JVs). Contribution of the metals segment remained unchanged at c \$370mln, while that of mining dropped by 12% to \$489mln. Operating cash flow grew by 35% MoM to \$964mln, owing to a c. \$200mln working capital release (versus a similarly sized injection in June). Free cash flow remained mostly flat due to an 8.5x increase in capex. Net debt to EBITDA contracted by 57% to just 0.1.

Our view: Total EBITDA for the month landed broadly in line with estimates. We expect the company to deliver another similarly-sized earnings figure in August, after which margins should begin to reflect more modest price levels for steel, and, especially, for iron ore. The latter's benchmark (62% Fe CFR China) has already dropped by almost 50% to \$115/t from its peak in early July. Skyrocketing energy prices are another reason why Metinvest's profitability should, in our view, see a material contraction going forward. That said, the latter effect will only fully come into effect at the very end of the financial year. Thus, all in all, we continue to believe that our earlier 2021 EBITDA projection of \$6.0bln (excluding JVs) remains valid.

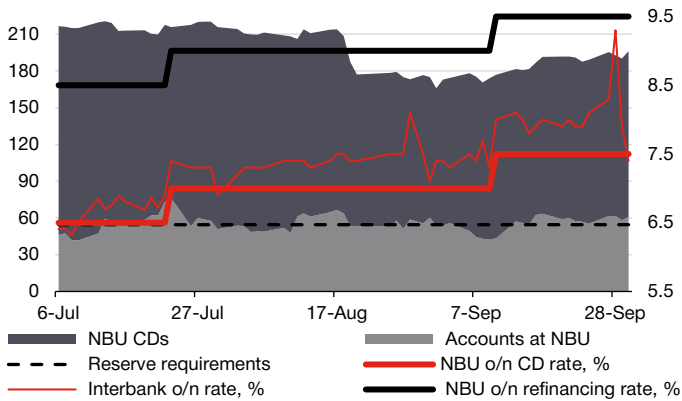
From the point of view of credit, Metinvest currently looks essentially debt-free with over \$2.0bln in cash reserves on its balance sheet at the end of July. A portion of these funds will be directed towards the DMK acquisition (\$340mln) and shareholder dividends (\$590mln), but internal generation should counterbalance these outflows, in our view. Thus, looking ahead, leverage will mostly depend on the company's capital allocation strategy and how quickly EBITDA levels normalize. Although room for maneuverability is large and earnings should not contract by more than 50% in 2022, we do think that Metinvest's shareholder risks are elevated, which makes us prefer other issues with low-risk credit metrics. Thus, despite its eurobonds somewhat depreciating on the market over the past month, we maintain our recommendation on the name at a 'Hold'.

Metinvest's financial results for July, \$mln

| | July | June | MoM | 7M21 | YoY |
|------------------------------------|-------|-------|------|--------|------|
| Revenues | 1,749 | 1,722 | 2% | 10,219 | 74% |
| EBITDA | 791 | 806 | -2% | 3,951 | 401% |
| margin | 0 | 0 | -2pp | 39% | 25pp |
| Metals EBITDA | 369 | 373 | -1% | 1,953 | 481% |
| Mining EBITDA | 489 | 553 | -12% | 2,474 | 367% |
| Metal sales, \$mln | 1,200 | 1,165 | 3% | 6,991 | 73% |
| Metal sales, kt | 1,179 | 1,254 | -6% | 8,975 | 0% |
| Iron ore production, kt | 2,690 | 2,690 | 0% | 18,554 | 5% |
| Steel price ¹ , \$/t | 1,051 | 957 | 10% | 1817 | 94% |
| Iron ore price ² , \$/t | 229 | 205 | 12% | 401 | 114% |
| OCF | 964 | 713 | 35% | 3,699 | 328% |
| Capex | 314 | 37 | 749% | 934 | 88% |
| Free cash flow | 650 | 676 | -4% | 2,765 | 653% |
| Total debt | 2,449 | 2,459 | 0% | 4,908 | -19% |
| Net debt | 375 | 1,016 | -63% | 1,391 | -72% |
| Net debt/LTM EBITDA | 0.1 | 0.2 | -57% | 0.3 | -94% |

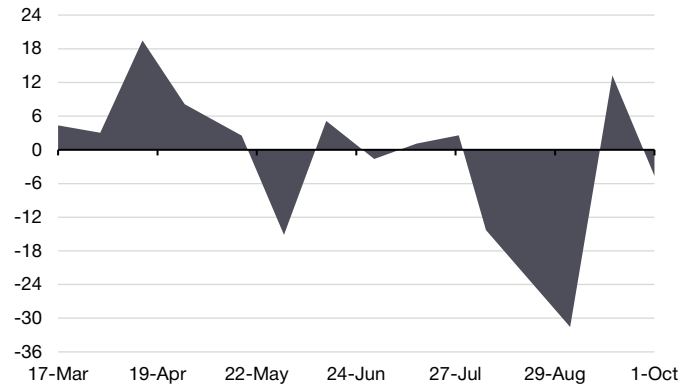
Appendix

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

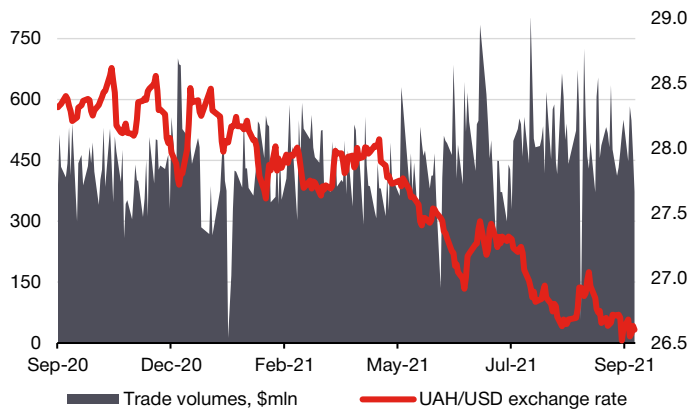


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has increased by UAH 7.15bln to UAH 196.2bln over the last week. On October 5 the Ministry of Finance conducted local hryvnia bond denominated placement maturing in April 2022, August 2022, November 2022, November 2023, July 2024 and May 2026 with yields of 9.70%, 11.50%, 11.57%, 12.40%, 12.49% and 12.75% respectively. A total of UAH 2.46bln was raised as a result.

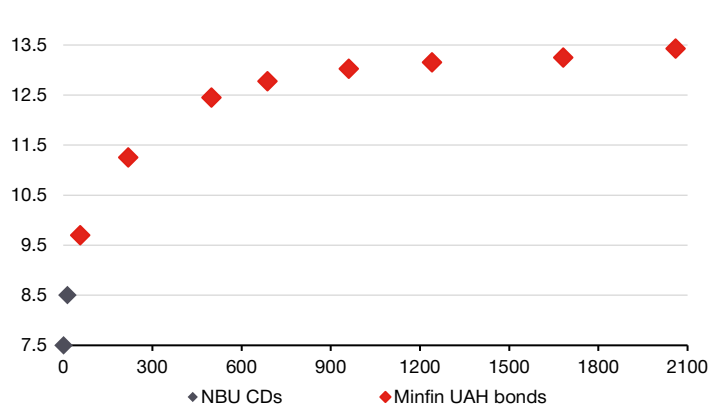
The UAH/USD interbank rate over the last week appreciated by 0.3%, starting out with 26.68 and ending at 26.60.

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



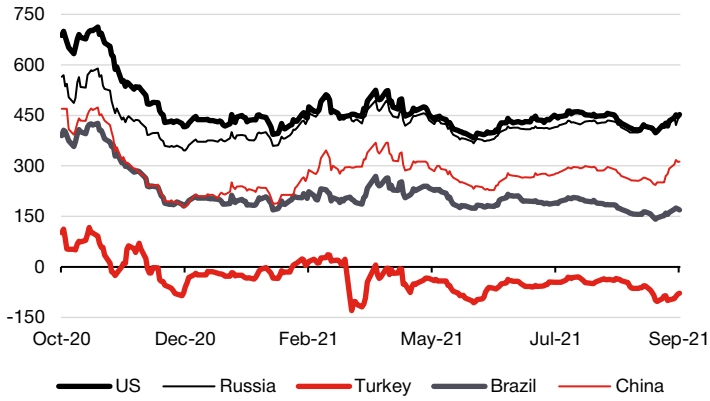
Note: Exchange rate figures are from official interbank data
Source: NBU

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



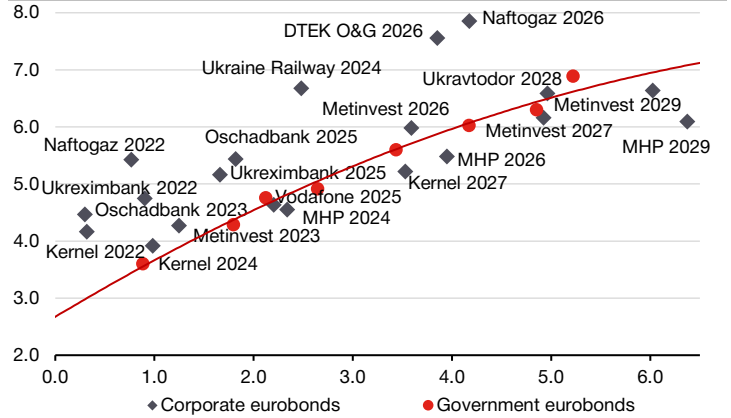
Source: NBU, Bloomberg, Adamant Capital estimates

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



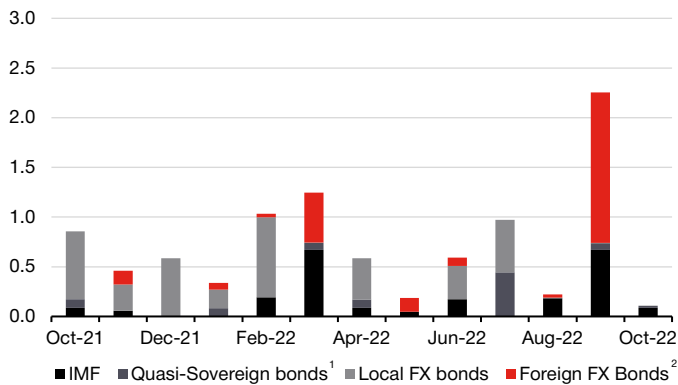
Source: Bloomberg, Adamant Capital estimates

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



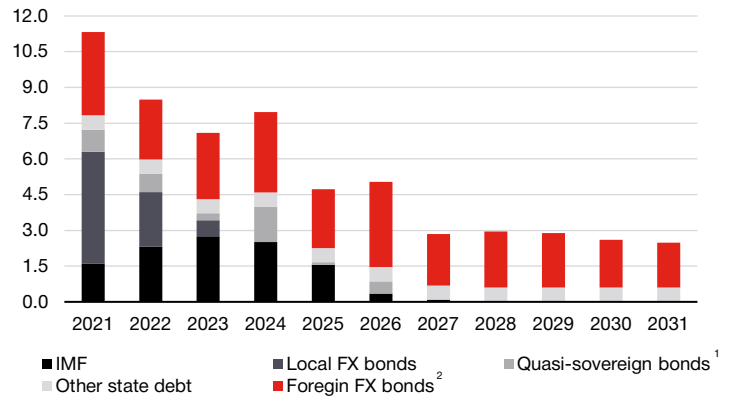
Source: Bloomberg, Adamant Capital estimates

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



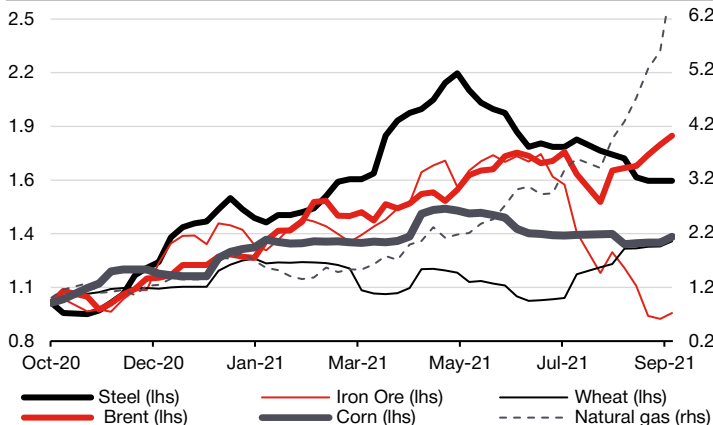
Note: Interest included in each category
 (1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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



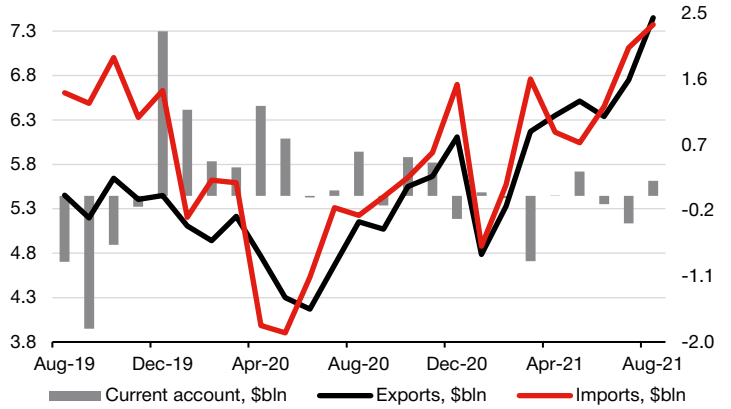
(1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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% | 2.7% | 4.0% |
| Nominal GDP, UAHbln | 875 | 1,162 | 1,301 | 4,192 | 1,009 | 1,169 | 1,522 | 5,454 |
| Nominal GDP, \$bln | 33 | 42 | 46 | 155 | 36 | 42 | 56 | 197 |
| GDP deflator growth YoY, % | 5.6% | 8.4% | 17.5% | 9.8% | 20.7% | 26.4% | 27.5% | 25.1% |
| 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% | 51.9% | 51.1% |
| Public external debt as % of LTM GDP, \$ ³ | 31.6% | 33.1% | 34.8% | 34.8% | 33.2% | 32.6% | 31.2% | 29.3% |
| 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 | 83.8 |
| Import of goods and services, \$bln | 12.3 | 15.9 | 17.8 | 62.3 | 17.1 | 18.3 | 20.1 | 82.5 |
| Trade balance, \$bln | 0.9 | -1.1 | -0.5 | -1.7 | -0.8 | 0.9 | 2.4 | 1.2 |
| Current account, \$bln | 1.7 | 0.3 | 1.6 | 6.6 | -1.0 | 1.4 | 1.0 | 0.5 |
| Financial account, \$bln ⁴ | 0.8 | 2.4 | -0.9 | 4.6 | -0.1 | 0.2 | 2.2 | -1.7 |
| End of period NBU reserves, \$bln | 28.5 | 26.5 | 29.1 | 29.1 | 27.0 | 28.4 | 28.7 | 33.1 |
| 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 | 4.3 | 106.2 | -0.5 | 1.8 | 1,355 |
| Ukraine 2024 | Hold | - | 9.0 | Feb-24 | 4.8 | 109.2 | -0.5 | 2.1 | 750 |
| Ukraine 2027 | Hold | - | 7.8 | Sep-27 | 6.3 | 107.0 | -1.0 | 4.9 | 1,307 |
| Ukraine 2028 | Hold | - | 9.8 | Nov-28 | 6.9 | 115.8 | -1.1 | 5.2 | 1,600 |
| Ukraine 2032 | Hold | - | 7.4 | Sep-32 | 7.3 | 100.6 | -1.2 | 7.3 | 3,000 |
| DTEK 2027 | Buy | 21-Sep-21 | 5.0 | Dec-27 | na | 60.4 | -0.5 | na | 1,645 |
| Kernel 2022 | Hold | 05-Oct-21 | 8.8 | Jan-22 | 4.2 | 101.4 | -0.1 | 0.3 | 213 |
| Kernel 2024 | Hold | 05-Oct-21 | 6.5 | Oct-24 | 3.9 | 105.7 | -0.1 | 1.0 | 300 |
| Kernel 2027 | Hold | 05-Oct-21 | 6.8 | Oct-27 | 5.2 | 105.5 | -1.3 | 3.5 | 300 |
| Metinvest 2023 | Hold | 05-Oct-21 | 7.8 | Apr-23 | 4.3 | 105.1 | -0.4 | 1.2 | 195 |
| Metinvest 2025 (EUR) | Hold | 05-Oct-21 | 5.6 | Jun-25 | 4.5 | 103.8 | -1.0 | 3.3 | 333 |
| Metinvest 2026 | Hold | 05-Oct-21 | 8.5 | Apr-26 | 6.0 | 109.9 | -2.0 | 3.6 | 648 |
| Metinvest 2027 | Hold | 05-Oct-21 | 7.7 | Oct-27 | 6.2 | 107.3 | -2.1 | 4.9 | 333 |
| Metinvest 2029 | Hold | 05-Oct-21 | 7.8 | Oct-29 | 6.6 | 106.8 | -2.2 | 6.0 | 500 |
| MHP 2024 | Buy | 14-Sep-21 | 7.8 | May-24 | 4.6 | 107.7 | -0.4 | 2.3 | 500 |
| MHP 2026 | Buy | 14-Sep-21 | 7.0 | Apr-26 | 5.5 | 105.8 | -0.4 | 3.9 | 550 |
| MHP 2029 | Buy | 14-Sep-21 | 6.3 | Sep-29 | 6.1 | 101.0 | -0.5 | 6.4 | 350 |
| Naftogaz 2022 | Buy | 11-May-21 | 7.4 | Jul-22 | 5.4 | 101.5 | -0.4 | 0.8 | 335 |
| Naftogaz 2024 (EUR) | Buy | 11-May-21 | 7.1 | Jul-24 | 7.3 | 99.5 | 0.5 | 2.6 | 672 |
| Naftogaz 2026 | Buy | 11-May-21 | 7.6 | Nov-26 | 7.9 | 99.0 | 1.0 | 4.2 | 500 |
| Oschadbank 2023 | Buy | 10-Aug-21 | 9.4 | Mar-23 | 4.8 | 104.1 | -0.3 | 0.9 | 140 |
| Oschadbank 2025 | Buy | 10-Aug-21 | 9.6 | Mar-25 | 5.4 | 107.6 | 0.0 | 1.8 | 200 |
| Ukraine Railway 2024 | Buy | 3-Aug-21 | 8.3 | Jul-24 | 6.7 | 103.9 | -0.1 | 2.5 | 595 |
| Ukravtodor 2028 | Hold | 22-Jun-21 | 6.3 | Jun-28 | 6.6 | 98.2 | -0.7 | 5.0 | 700 |
| Ukreximbank 2022 | Buy | 10-Aug-21 | 9.6 | Apr-22 | 4.5 | 101.5 | -0.2 | 0.3 | 104 |
| Ukreximbank 2025 | Buy | 10-Aug-21 | 9.8 | Jan-25 | 5.2 | 107.6 | 0.0 | 1.7 | 192 |
| Vodafone 2025 | Hold | 18-May-21 | 6.2 | Feb-25 | 4.6 | 103.4 | -0.2 | 2.2 | 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 |
| NBU - International reserves monthly data | Exact | 7-Oct |
| SSSU - Monthly inflation | Exact | 8-Oct |

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