

Weekly Digest

- Revised IMF program details: two more reviews by June
- Zelensky's press conference: Akhmetov may be implicated in a coup attempt, Ukraine army ready for Russian aggression
- Kernel Holding 1Q22 EBITDA grew by 26% YoY to \$230mln

Revised IMF program details: two more reviews by June. According to the new memorandum published by the Fund, the undisbursed \$2.2bln will be split into two halves of \$0.7bln and \$1.5bln scheduled for March and June of 2022, respectively. The first portion will require that the authorities approve the 2022 budget with a general government deficit target of 3.5% of GDP, improve regular and state-owned bank supervision practices, and produce a few reports/actions plans (comprehensive asset recovery strategy, PGO criminal proceedings results against former bank owners so far, and a roadmap for partial privatization of PrivatBank and Oschadbank). Conditions for the remaining disbursement include amendments to the SAPO law (improves selection of officials, strengthens capacity to regulate organizational activities, and establishes mechanisms of accountability), creating a consumer database for all gas suppliers to make billing households easy for new market players, completing one-off integrity checks of existing HCJ members by the Ethics Council, and approving a supervisory board for Energoatom (nuclear power SOE). Additionally, the memorandum will also include a new quantitative criterion, which targets the maximum arrears to renewable energy producers by the Guaranteed Buyer (at 0 by December of 2021).

Our view: Requirements for the March tranche seem quite lenient and unless there is further regress in reforms, we think that the probability of meeting them before the SBA runs out is rather high. The second portion looks more problematic as it tackles anti-corruption (namely the SAPO law), an area where progress has proven to be extremely slow under Zelensky so far. The HCJ member integrity check will also see a lot of pushback, though the judicial reform seems to be on the President's agenda. Of note, is that the memorandum includes no mention of fixed prices for households and heating utilities being a problem, even though Naftogaz has not actually hedged these, which, in our view, is equivalent to reinstating the previous PSO regime. The addition of RES arrears criterion seems positive for DTEK Renewables, though we don't expect the authorities to necessarily abide by the included timing.

Zelensky's press conference: Akhmetov may be implicated in a coup attempt, Ukraine army ready for Russian aggression. During a live 5-hour long Q&A event dedicated to having served 2.5 years in office (out of 5 in total) last Friday, the President reported that domestic intelligence services have obtained information that certain individuals close to Ukraine's richest man Akhmetov are planning to overthrow the government in early December. A day later, a reputable BuzzFeed journalist, citing sources within the Presidential Office, disclosed that the evidence essentially consists of audio recordings of one FSB operative and three Ukrainian defectors believed to be residing in Crimea. Their conversations seem to mention the oligarch, but do not actually imply his direct involvement. Answering a question regarding the possibility of a military escalation with Russia, Zelensky replied that the Ukrainian army is ready to deflect such attempts. The President also laid out his own version of events in relation to the failed sting operation conducted by military intelligence in 2020, which since then became a hot topic for discussion by the media (dubbed the 'Wagnergate'). He accused a top intelligence official (Vasyl Burba), who earlier implied that sources in the Presidential Office may have leaked some details of the operations to the Russians, of playing political games and being corrupt.

Our view: We draw three main conclusions from Zelensky's press marathon. First, his conflict with Akhmetov has entered a 'hot phase'. This spells out negative consequences for the valuation of the latter's assets. DTEK Renewables, which was the only company to not receive 'green tariff' compensation from the state (funded by Ukrenergo's recent placement) saw the price of its bonds lose c. 10% of par over the past 2 weeks. A similar dynamic was demonstrated by eurobonds issued by Metinvest and DTEK Energy. The direction in which this conflict will end up developing is difficult to predict, but we think that an eventual peaceful resolution is the most likely outcome. Second, the President does not seem to be too concerned over the possibility of a Russian military threat, which, in our mind, increases the probability of it never occurring. Third, Zelensky's version of some key events (such as the Wagner operation) seems to clash with findings reported by investigative journalists. We think that this most likely implies that he is starting to submerge in an information bubble created for him by his entourage. If true, this increases the probability of further political missteps, in our view.

Kernel Holding 1Q22 EBITDA grew by 26% YoY to \$230mln (excluding IAS 41 effects). Extra profits were generated predominantly by the farming division (+\$68mln), which benefited from significantly higher sales prices YoY. Oilseed processing performed worse than last year due to tight seed supply still persisting on the market (2021 calendar year volumes just started coming in). Infrastructure & trade was able to repeat 1Q21 results, owing to exceptional performance of Avere (generated \$96mln in EBITDA, which represents 82% of the segment total). Kernel's OCF remained roughly at breakeven, flat YoY, on the back of seasonally high working capital needs. Free cashflow came in at -\$94mln due to capex and financial asset purchases (likely related to Avere). Net debt to EBITDA contracted by 31% to 1.2. During its quarterly conference call for investors, management voiced concerns over FY22 margins in both oilseed crushing and grain exports citing reluctance on the side of the farmers to sell crops (sizeable profits in the previous season have allowed them to build solid cash positions). Kernel's own farming EBITDA was guided to 'exceed the previous year's result'.

Our view: The reported quarterly EBITDA exceeded our projection by almost 100%, owing primarily to another three months of exceptional Avere performance. While this earnings source is inherently unreliable and cannot be assumed to repeat on an ongoing basis, its YTD impact has already matched our forecast for the full-year. Taking into account a track record of no losses for 5 consecutive reporting periods, we find it plausible that Avere will increase its contribution by at least another \$50mln over the remaining 9 months. The other sizeable surprise came from the side of the farming business, which boasted an exceptionally high profit margin on crop sales (at 84% excluding IAS 41). Although we do not expect this phenomenon to repeat in the coming quarters either, we are also somewhat more positive on the overall EBITDA generation capacity for this division in FY22 than Kernel's management (crop costs per ton are essentially flat YoY, while prices are up 20-30%). Even though the company's crushing and export margins did come in lower than anticipated, we remain optimistic regarding their rebound going forward, as, in our view, farmers can only stall sales for so long (everything still needs to be shipped to customers before the next season starts).

All in all, we have decided to increase our FY22 EBITDA forecast for Kernel by 14% to \$680mln (excluding IAS 41). While such an earnings level spells out even more favorable credit metrics than before (leverage should be able to stay flat July to July even after accounting for \$265mln of capital expenditures, dividends, and an extra \$100mln in working capital needs), the current price level on the company's 2027 eurobond prevents us from upgrading the recommendation (we maintain it at a 'Hold').

Kernel Holding 1Q22 IFRS results, \$mln					
	1Q22	1Q21	YoY	4Q21	QoQ
Revenue	1,343	940	43%	1,651	-19%
EBITDA	315	290	8%	224	41%
IAS 41 gain/loss	85	107	-21%	63	35%
EBITDA adjusted ¹	230	183	26%	161	43%
Oilseed processing	15	31	-53%	-6	nm
Infrastructure & trade	117	111	5%	102	15%
Avere	96	83	15%	86	12%
Farming	122	54	127%	93	32%
Other	-24	-13	nm	-28	nm
Adj EBITDA margin	17%	19%	-2pp	10%	7pp
Net profit	246	233	5%	186	33%
Net profit margin	18%	25%	-6pp	11%	7pp
Net debt	1,111	1,017	9%	836	33%
Net debt/EBITDA	1.1	1.7	-32%	0.9	21%
Net debt/Adj EBITDA ¹	1.3	2.0	-34%	1.1	22%
Adj net debt/EBITDA ²	0.6	1.1	-40%	0.7	-12%
Operating cash flow	8	0	nm	218	-96%
Capex	49	52	-5%	98	-50%
Free cash flow	-94	-36	nm	127	-174%
Vegetable oil sales, kt	221	296	-25%	273	-19%
Oil EBITDA/t, \$	66	104	-36%	-22	nm

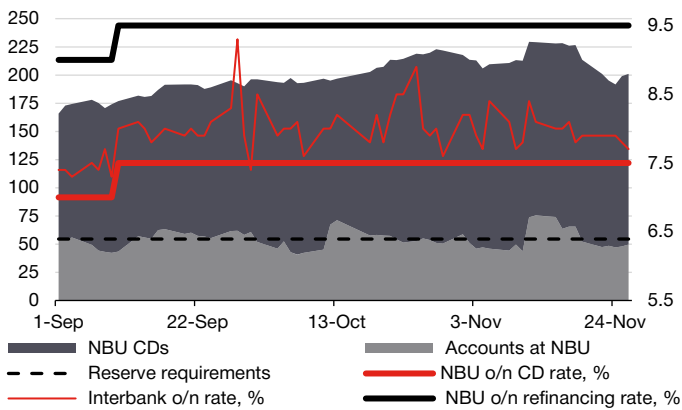
(1) Excluding IAS 41

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

Source: company data, Adamant Capital estimates

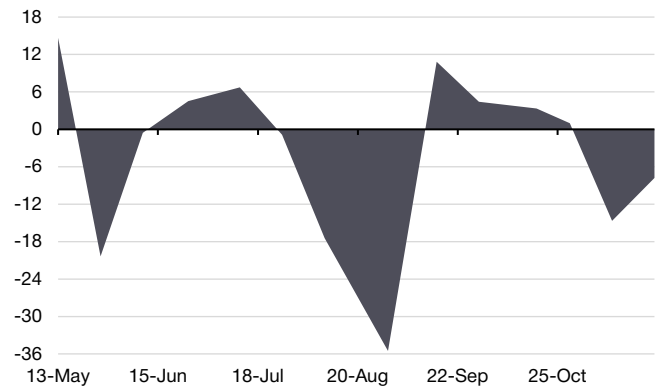
Appendix

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

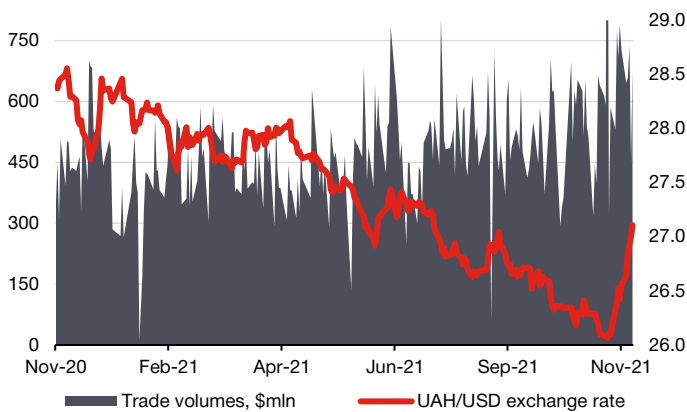


Note: in UAHbln, where each point represents a biweekly sum
Source: NBU

Local market liquidity (as measured by the aggregate amount of NBU correspondent accounts and investment CDs) has decreased by UAH 12.32bln to UAH 201.1bln over the last week. On November 30 the Ministry of Finance conducted local hryvnia bond denominated placements maturing in April 2022, December 2022, January 2023, November 2023, October 2024 and May 2027 with yields of 10.70%, 11.65%, 11.65%, 12.55%, 12.85% and 13.25% respectively. Dollar denominated bonds maturing in June 2022 were sold at a yield of 2.35%. In total, an equivalent of UAH 12.7bln was raised as a result.

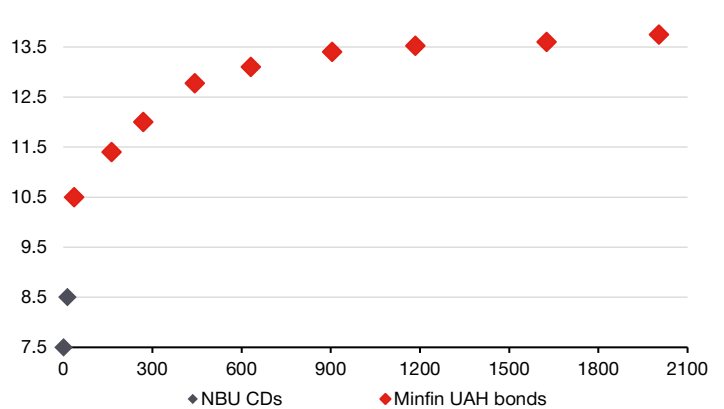
The UAH/USD interbank rate over the last week appreciated by 1.75%, starting out with 26.64 and ending at 27.11.

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



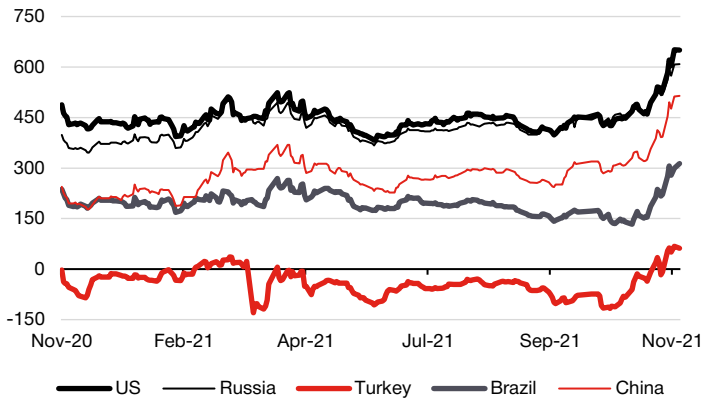
Note: Exchange rate figures are from official interbank data
Source: NBU

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



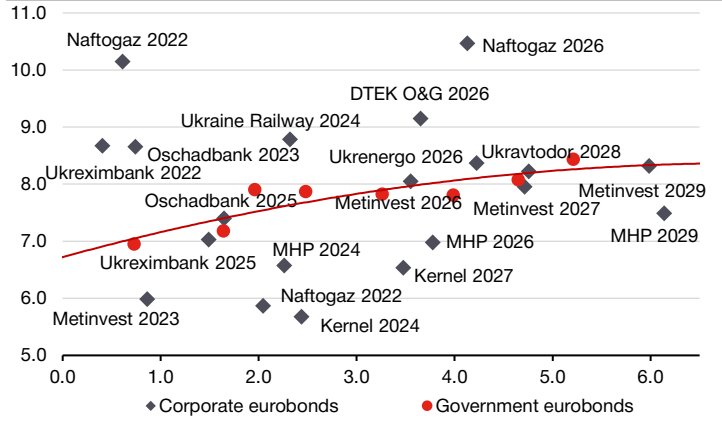
Source: NBU, Bloomberg, Adamant Capital estimates

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



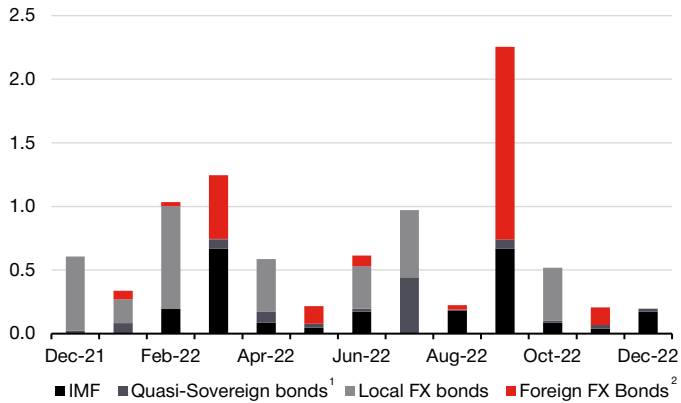
Source: Bloomberg, Adamant Capital estimates

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



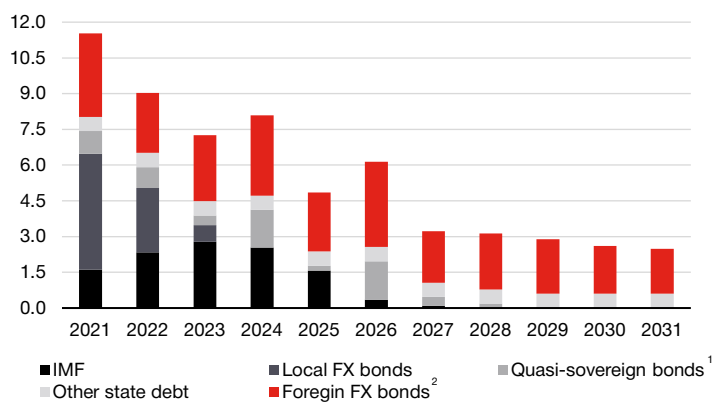
Source: Bloomberg, Adamant Capital estimates

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



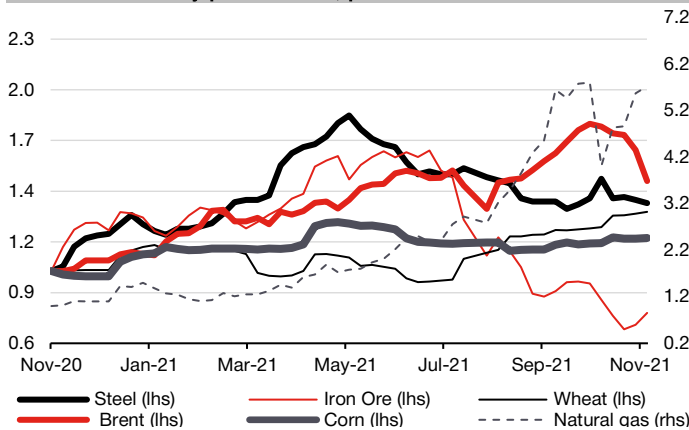
Note: Interest included in each category
 (1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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



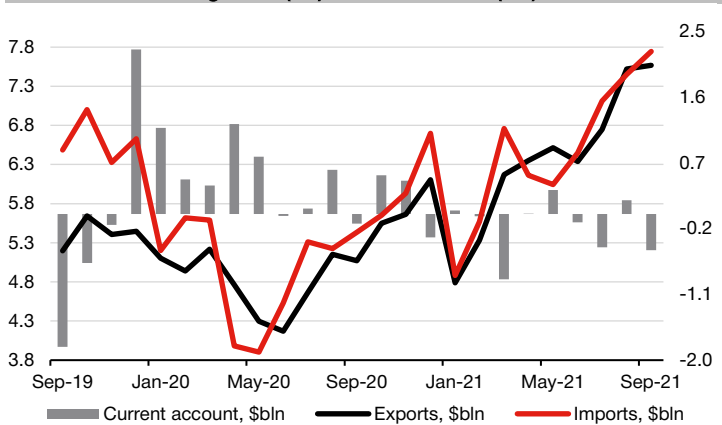
(1) Debt of state owned enterprises
 (2) Includes USAID guarantees
 Source: Bloomberg, Adamant Capital estimates

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								
	3Q20	4Q20	2020	1Q21	2Q21	3Q21E	4Q21E	2021E
Real GDP growth, YoY	-3.5%	-0.5%	-4.0%	-2.2%	5.7%	2.4%	7.9%	3.7%
Nominal GDP, UAHbln	1,162	1,301	4,192	1,009	1,169	1,518	1,797	5,493
Nominal GDP, \$bln	42	46	155	36	42	56	68	202
GDP deflator growth YoY, %	8.4%	17.5%	9.8%	20.7%	26.4%	27.5%	28.0%	26.4%
Period average CPI YoY, %	2.4%	3.8%	2.7%	7.4%	9.1%	10.5%	10.1%	9.3%
End of period CPI YoY, %	2.3%	5.0%	5.0%	8.5%	9.5%	11.0%	9.5%	9.5%
Consolidated budget deficit, % of GDP ¹	3.3%	5.3%	5.3%	4.9%	5.1%	3.1%	4.0%	4.0%
Broad public sector deficit, % of GDP ²	4.1%	6.5%	6.5%	6.2%	6.3%	4.6%	4.3%	4.3%
Public debt as % of LTM GDP, UAH	58.6%	60.9%	60.9%	57.8%	54.2%	52.0%	50.8%	50.8%
Public external debt as % of LTM GDP, \$ ³	33.1%	34.8%	34.8%	33.2%	32.6%	31.1%	28.6%	28.6%
Total external debt, \$bln	122	126	126	123	125	127	130	130
Export of goods and services, \$bln	14.9	17.3	60.6	16.3	19.2	21.8	26.5	83.8
Import of goods and services, \$bln	15.9	17.8	62.3	17.1	18.3	22.3	24.8	82.5
Trade balance, \$bln	-1.1	-0.5	-1.7	-0.8	0.9	-0.5	1.7	1.2
Current account, \$bln	0.6	0.7	5.3	-0.9	0.2	-0.8	1.9	0.5
Financial account, \$bln ⁴	2.4	-0.9	4.6	-0.1	0.2	-2.0	1.3	-1.7
End of period NBU reserves, \$bln	26.5	29.1	29.1	27.0	28.4	28.7	33.1	33.1
Average interbank exchange rate, UAH/\$ ⁵	27.6	28.3	27.0	27.9	27.6	26.9	26.5	27.2
EOP interbank exchange rate, UAH/\$	28.3	28.2	28.2	27.8	27.2	26.6	27.5	27.5
EOP key policy rate NBU, %	6.0%	6.0%	6.0%	6.5%	7.5%	8.5%	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	7.2	100.9	-0.6	1.6	1,355
Ukraine 2024	Hold	-	9.0	Feb-24	7.9	102.1	-1.3	2.0	750
Ukraine 2027	Hold	-	7.8	Sep-27	8.1	98.5	-0.6	4.6	1,307
Ukraine 2028	Hold	-	9.8	Nov-28	8.4	106.8	-0.8	5.2	1,600
Ukraine 2032	Hold	-	7.4	Sep-32	8.4	92.9	-2.5	7.0	3,000
DTEK Energy 2027	Buy	24-Nov-21	5.0	Dec-27	na	53.5	-3.6	na	1,645
Kernel 2024	Hold	30-Nov-21	6.5	Oct-24	5.7	102.0	-0.4	2.4	300
Kernel 2027	Hold	30-Nov-21	6.8	Oct-27	6.5	100.7	-0.6	3.5	300
Metinvest 2023	Hold	05-Oct-21	7.8	Apr-23	6.0	102.3	-0.2	0.9	195
Metinvest 2025 (EUR)	Hold	05-Oct-21	5.6	Jun-25	6.1	98.5	-1.4	3.2	333
Metinvest 2026	Hold	05-Oct-21	8.5	Apr-26	8.0	101.6	-2.1	3.6	648
Metinvest 2027	Hold	05-Oct-21	7.7	Oct-27	8.0	98.6	-2.6	4.7	333
Metinvest 2029	Hold	05-Oct-21	7.8	Oct-29	8.3	96.8	-2.8	6.0	500
MHP 2024	Hold	24-Nov-21	7.8	May-24	6.6	102.6	-0.3	2.3	500
MHP 2026	Hold	24-Nov-21	7.0	Apr-26	7.0	99.9	-0.3	3.8	550
MHP 2029	Hold	24-Nov-21	6.3	Sep-29	7.5	92.8	-0.4	6.1	350
Naftogaz 2022	Buy	2-Nov-21	7.4	Jul-22	10.1	98.3	0.1	0.6	335
Naftogaz 2024 (EUR)	Buy	2-Nov-21	7.1	Jul-24	11.0	91.5	-0.9	2.4	672
Naftogaz 2026	Buy	2-Nov-21	7.6	Nov-26	10.5	89.3	-1.5	4.1	500
Oschadbank 2023	Buy	9-Nov-21	9.4	Mar-23	8.7	100.5	-0.3	0.7	140
Oschadbank 2025	Buy	9-Nov-21	9.6	Mar-25	7.4	103.6	0.0	1.6	200
Ukraine Railway 2024	Buy	12-Oct-21	8.3	Jul-24	8.8	98.8	-0.3	2.3	595
Ukravtodor 2028	Hold	22-Jun-21	6.3	Jun-28	8.2	91.0	-1.5	4.8	700
Ukreximbank 2022	Buy	9-Nov-21	9.6	Apr-22	8.7	100.3	-0.5	0.4	104
Ukreximbank 2025	Buy	9-Nov-21	9.8	Jan-25	7.0	104.1	0.0	1.5	192
Vodafone 2025	Hold	16-Nov-21	6.2	Feb-25	5.9	100.7	-0.4	2.0	451
DOG 2026	Buy	19-Oct-21	6.8	Dec-26	9.1	90.4	-2.9	3.7	425

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 - Construction monthly data	Exact	1-Dec
Metinvest - Monthly report for September	Indicative	3-Dec
Metinvest - Financial results for 9M21	Indicative	3-Dec
NBU - International reserves monthly data	Exact	7-Dec

Contacts

Adamant Capital

5-B Volodymyrska Street, 2nd floor
01001 Kyiv, Ukraine
+380 44 585 52 37

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.