



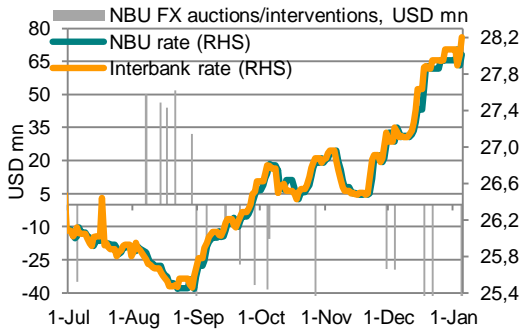
**This week in focus: Ukraine sees some stabilization in current account, FX reserves**

Having narrowed strongly in October, Ukrainian current account displayed a minor surplus of USD18 mn in November (vs USD154 mn deficit last year and USD315 mn deficit in October), spurred by lower trade disbalance and growing remittances. On a 12 month basis, this implies (temporary) stabilization of current account deficit in range of USD 4.4bn, or 4.1% of GDP.

*Please see page 3 for more details*

**FX and interest rates: Local currency likely to remain on depreciation trend**

**Figure 1. UAH exchange rate (UAH per USD)**



Source: NBU, Reuters

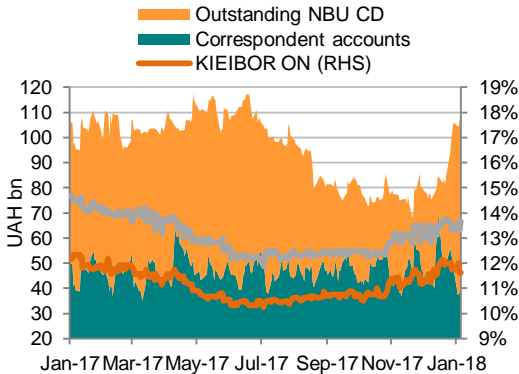
USD/UAH increased to 28.20 as of Friday the 5<sup>th</sup>. Week-on-week local currency declined by 0.5 % against the USD. **Provided generous injection of liquidity from the treasury account, we believe that UAH is likely to remain on depreciation trend**, although recent macroeconomic data suggest that pressure on hryvnia stemming from underlying balance of payment factors is losing its steam.

**Aggregate banking liquidity amounted to UAH 106.9bn as of Friday the 5<sup>th</sup>, increasing by UAH 21.2bn for the last two weeks.** All of increase in liquidity levels happened at the end of 2017. This comes in line with our expectations (please see our Weekly report dated Dec 4th). During December, MoF's treasury account was almost completely emptied, leaving UAH 5.1bn of residuals, as of January 1. In December, budget revenue amounted to UAH 69bn, according to provisional data. This implies that MoF spent all of the proceeds obtained from tax collections and other and even dug deep into its prior accumulations to finance record end year expenditures. During the month pension expenses reached UAH 36bn, up several times compared to average pension outlay during first 9 months, and up more than 2 times compared to average level of October and November, when pensions of millions were effectively increased.

**Money market rates remained flat:** cost of ON funds is around 10.50/12.50%, 1 week is 11.5/13.0% while 1M is 12.5/14.00%, according to our data. Increase in liquidity should weigh on interest rates this week.

**On its latest auction in 2017, MoF managed to attract UAH 1.6bn of proceeds. At this time, EUR-denominated bonds took the top spot** (see table below), attracting in excess of 80% from overall demand at the auction, followed by UAH-denominated issues trailing far behind their peer denominated in hard currency. The next placement is scheduled for tomorrow (January 10), with offerings of 3m, 6m, 9m, 12m and 2y maturities. We expect muted demand due to ongoing tightening cycle of NBU.

**Figure 2. Banking liquidity (UAH bn)**



Source: Reuters, NBU, UkrSibbank, Minfin

**Figure 5. OVDP auction results, 26<sup>th</sup> of December 2017**

CCY	Maturity	Cut-off rate	WA rate	Max bid rate	Min bid rate	Number of bids	Bids accepted	Bid size	Placement size
UAH	3m	16.00%	16.00%	16.00%	16.00%	4	4	190.0mn	183.2mn
UAH	6m	16.00%	15.93%	16.00%	15.89%	3	3	70.0mn	65.8mn
UAH	1y	15.85%	15.85%	15.85%	15.85%	1	1	1.1mn	1.1mn
EUR	1.5y	3.95%	3.95%	3.95%	3.95%	4	4	40.1mn	40.2mn

**Average daily FX volumes on the market landed at the equivalent of USD 169.7mn,** USD 11.6mn lower than in the previous week.

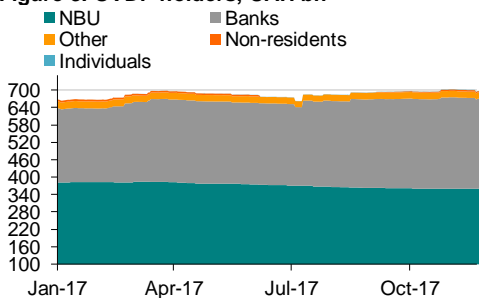
**The NBU intervened on the market once via currency auction.** On Friday, the central bank choose to interfere, declaring auction with possibility to sell up to USD 100mn. Having initially applied for USD 66.7mn from banks, the NBU sold only USD 50.5mn from international reserves at the auction.

**In November, average wages in Ukraine rose by 38.3% y/y, while the same wage adjusted for inflation demonstrated strong gain increasing by 21.2% y/y,** as the pace of inflation in Ukraine moved downside starting from October, extending the string of strong readings. Average nominal wage increased by 0.5% m/m, and was led, as was in the previous cases by agriculture (+46.5% y/y), industry (+31.6% y/y), trade (33.1% y/y), construction (+31.4% y/y), while the government sector contributed positively as well.

**Naftogaz wins arbitration over Gazprom.** The court rejected Gazprom's claim regarding take or pay clause, which amounted to USD 56bn during period from 2012 to 2017. Moreover, the court cancelled the moratorium on re-export of Gazprom's gas. According to the ruling, Naftogaz should not pay for gas supplied to a non-controlling territory. In its turn, Gazprom claimed that Naftogaz should pay USD 2.2bn for gas underpaid in 2013-2014. According to the court decision, this amount Ukraine is obliged to pay. But Naftogaz expects to obtain additional money from USD 16bn claim to Gazprom related to transit contract, which is expected to be finalized in February 2018.

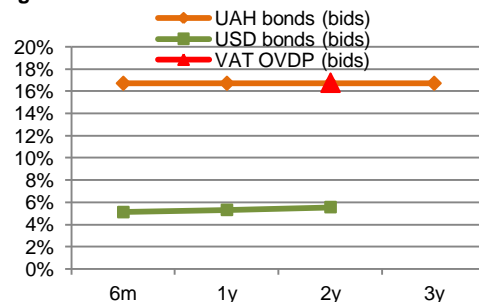
**Currently, yields (bids) of local OVDP in UAH at 16.70% (for 6m), 16.70 (for 2Y).** 1Y USD bids were at 5.55%, while bids for VAT bonds were at 16.75%.

**Figure 3. OVDP holders, UAH bn**



Source: NBU

**Figure 4. Local bonds market**



Source: UkrSibbank



**Global markets: US jobs growth fell to 2.1mn in 2017, down from 2.2mn in 2016**

**Figure 5. Ukraine's sovereign Eurobond yields, bid/ask mid (%)**



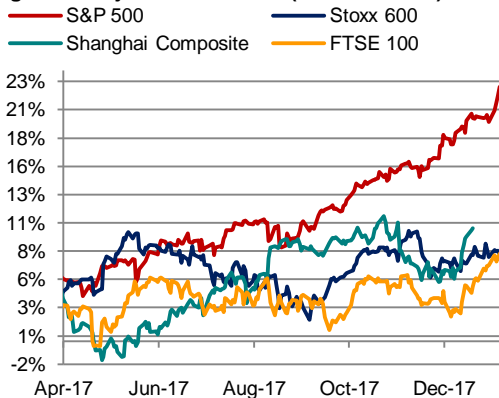
Source: Reuters

**Figure 6. EUR USD spot (mid)**



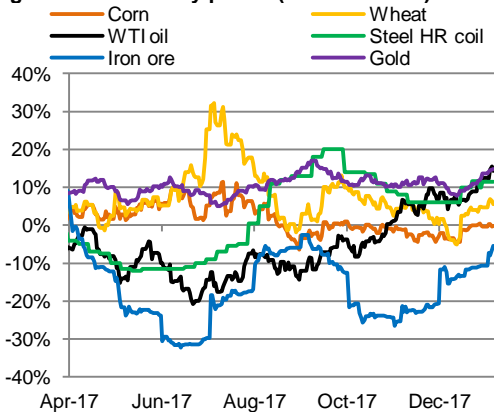
Source: Reuters

**Figure 7. Major stock indices (Jan-2017=100)**



Source: Reuters

**Figure 8. Commodity prices (Jan-2017=100)**



Source: Reuters

On Friday, the Bureau of Labor Statistics issued its latest jobs report for 2017. In 2017, the US jobs growth fell to 2.1mn from 2.2mn in 2016. This result maintained a seven year streak of adding at least 2 million jobs. Meanwhile, unemployment rate remained unchanged at 4.1% for a third month. From the side of Europe, inflation declined away from ECB 2% target, landing at 1.4 y/y in December, down from 1.5% in November.

**Bond benchmarks fell**, with 10y Treasuries' yields rose 7 bp week-on-week to the level of 2.48%, while German 10y Bunds' yields increased 1bp, landing at 0.44%, Japanese 10y bonds closed the week at 0.059.

**US equities mixed**, with S&P added 2.6%, while Nasdaq Composite gained by 3.4% week-on-week.

**The Bureau of Labor Statistics reported Friday that the US economy added 148 000 jobs in December**, which was below than the estimated 190 000. The unemployment rate remained unchanged at 4.1% for a third month, a result that was in line with economists' expectations. At the same time, average hourly earnings increased by 2.5 percent from a year ago, following 2.4% gain in prior month. The last jobs report for 2017 brings the 2017 total to 2.06 million jobs, remaining below 2016. Increase in wages was led by health care (+31 000), construction (+30 000), manufacturing (+25 000).

**EUR/USD rate landed at 1.2030 as of Friday the 5<sup>th</sup>**, higher than the last week closing level of 1.1998, as the USD mainly over performed against its main counterparts.

**Stoxx 600, a broader gauge of European equity performance increased by 2.1% week-on-week.**

**Eurozone's inflation declined away from the European Central Bank's target in December**, highlighting the challenge that central bank facing as it wants to maintain price increases to proceed further with quantitative easing program. Prices rose 1.4% y/y in December, down from 1.5% in prior month. Decline in prices was due to energy, food, alcohol and tobacco prices. At the same time, producer price inflation increased 0.6% m/m, bringing the y/y rate to 2.8%.

**Chinese core consumer prices rose 0.9% y/y in November**, beating an estimate of 0.8% rise. While Japanese inflation unexpectedly increased in November but prices are still rising at less than half of the rate targeted by BoJ. Meanwhile, the unemployment rate fell to 2.7%, which is the lowest level since 1993. The main concern for policymaker is that prices remained well below of the Bank of Japan's 2% target.

**Crude oil fell broadly**, as WTI 1m futures increased by 1.7% week-on-week and closed at USD 61.4 per barrel, while Brent 1m futures added by 1.1%, closing at USD 67.6 per barrel.

**Gold prices gained**, as NYMEX 1m futures drop by 1.17% week-on-week and finished the week at USD 1320.3 per troy ounce.

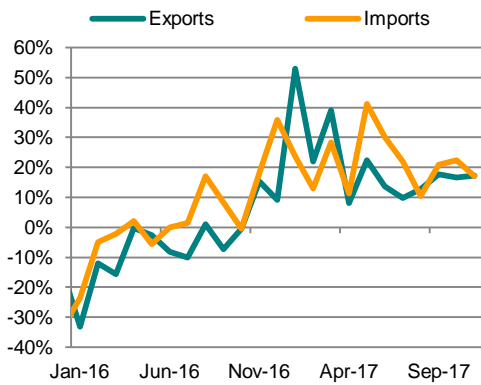
**Grains finished the week in black**, as CBOT Corn 1m futures rose 0.1% week-on-week and closed at USD 351.3 per bushel, while CBOT Wheat 1m futures laded at USD 430.8 per bushel, 0.9% higher week-on-week.

**Iron ore increased**, as NYMEX Iron ore 62% Fe 1m futures rose 5.8% week-on-week and closed at USD 75.39 per ton. China's Industry and Information Technology Ministry said in its statement that it would allow one tone of new capacity to be built for each of 1.25 tones closed in China. That statement reinforced expectations that state's authorities will deepen the efforts to curb steel production and capacity and keep it from increasing.



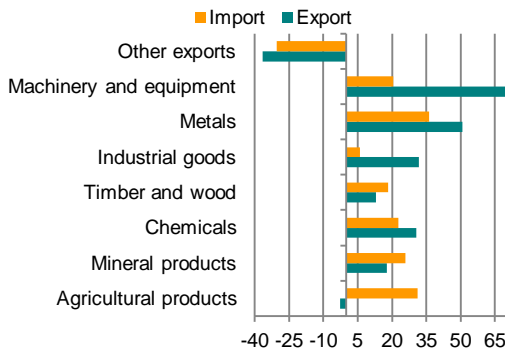
**This week in focus: Ukraine sees some stabilization in current account, FX reserves**

**Figure 9. Exports and imports, y/y, %**



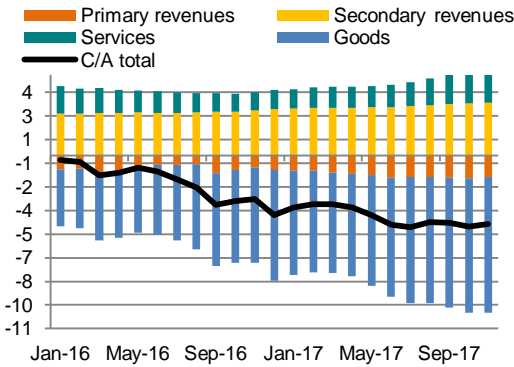
Source: NBU

**Figure 10. Change in export and import by category in value, % y/y**



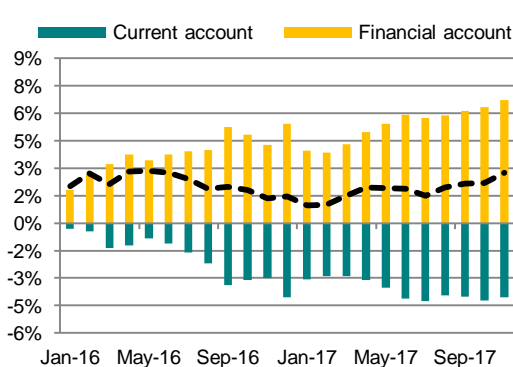
Source: NBU

**Figure 11. Current account, USD bn (12m rolling)**



Source: NBU

**Figure 12. BoP 12m rolling, as a % of GDP**



Source: NBU

Having narrowed strongly in October, Ukrainian current account displayed a minor surplus of USD18 mn in November (vs USD154 mn deficit last year and USD315 mn deficit in October), spurred by lower trade disbalance and growing remittances. On a 12 month basis, this implies (temporary) stabilization of current account deficit in range of USD 4.4bn, or 4.1% of GDP.

**Exports of goods grew by +17.3% y/y in November (USD 3.9bn).** Metals export advanced by 51% y/y, machinery export surged by 1.8x times, chemical export increased by 31% y/y. Meanwhile, agricultural export showed decline by 2.8% y/y in November, after increase of 11.7% y/y in October. For 11M 2017, export increased by 20.1% y/y, reaching USD 36.2bn. Out of which, EU accounted for the major part with a share of 35.3%, followed by Asia – 32.6% and Russia – 8.5%.

Export of metals was underpinned by both increased production and higher steel prices. In November, prices of hot rolled coils were up by 17%/y/y, while prices of billet were higher by around 30% y/y. Going forward, our Group analyst expect good performance of steel market based on leading indicators (primarily linked to Chinese GDP performance).

Agricultural products exports (USD 1.7bn) are still in the woods, having posted a decline of 2.8% y/y, having decreased from 11.7% y/y growth in prior month. Ukraine exported 16.8mnt of grains from the start of new marketing season of 2017/2018, which is 7% lower compared to a year ago, as of the end of November. Wheat export declined 2.7%, barley contracted by 6.0%. Corn export shrank by 18.6%. Overall, during 2017/2018 marketing year Ukraine's farmers exported in excess of 21.4mnt of grains, as of January 1, down from 23.8mnt for the same period a year ago, according to preliminary figures.

**Import growth decelerated to 17.1% y/y in November**, from 22.1% recorded in prior month, as machinery import, mineral import and chemical import slowed its expansion. Machinery import reached USD 1.3bn, but growth rates collapsed to 20.6% y/y, from 33.1% y/y recorded in prior month. In terms of imports, we observe a mixed picture of growing personal incomes which drive up the volume of imports, which are (arguably) offset by decrease in number of consumers in the country due to active migration.

As a result trade balance displayed a reasonable USD 734mn deficit.

In November, **primary incomes rose to USD 119mn, up from USD 69mn and secondary incomes reached USD 349mn**, which in combination with USD 284mn surplus in balance of trade of services helped to bring current account balance to positive numbers.

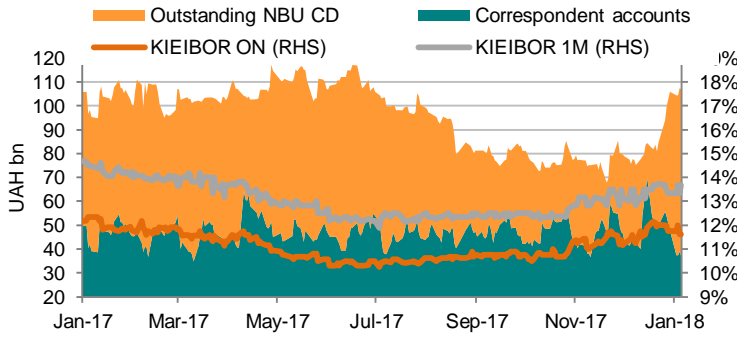
**The financial account proceeds amounted to USD 478mn of surplus**, slightly growing from prior month level. Meanwhile, on a yearly basis it expanded several times. It was led by FDI, which rose to USD 169mn. Banks were the main source of FDI in NBU statistic this month, accounting for USD 105mn (or 62%) from total investments. For 11M 2017, net FDI inflow to Ukraine reached USD2.1bn, down from USD 3.2bn a year ago. In November, real sector reduced its external borrowing by USD 193mn, especially long term by USD 215mn.

**Combined, Ukraine's balance of payment printed USD 491mn of surplus** in November boosted by stronger current account. Also, in November, Ukraine paid USD 364 mn to IMF, which resulted in USD 18.9bn international reserves at the beginning of December 2017. **As of Jan 01 2018, gross international FX reserves stood with virtually no change at USD 18.8bn.**



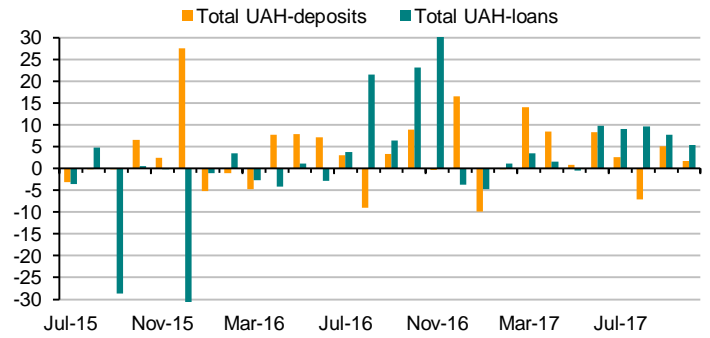
**Money market**

**Banking liquidity vs. money market rates, %**



Source: Reuters, NBU, UkrSibbank estimates

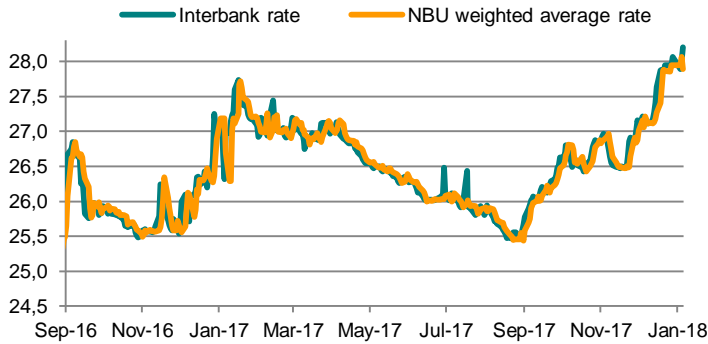
**Monthly change in local currency loans and deposits, UAHbn**



Source: the NBU

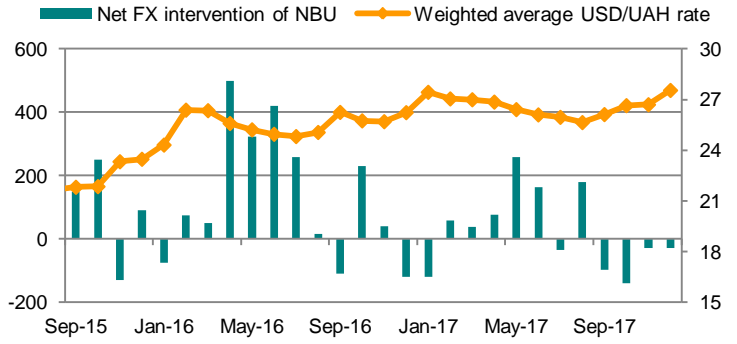
**Currency market**

**UAH exchange rate, UAH/USD**



Source: Reuters

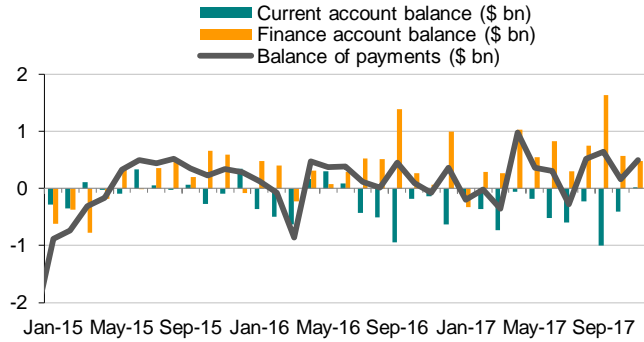
**Net retail FX interventions of the NBU in 2015-2017, USDmn**



Source: NBU

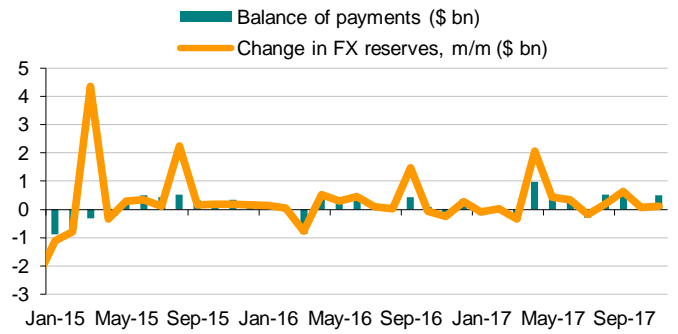
**Balance of payments**

**Major BoP accounts, USDbn**



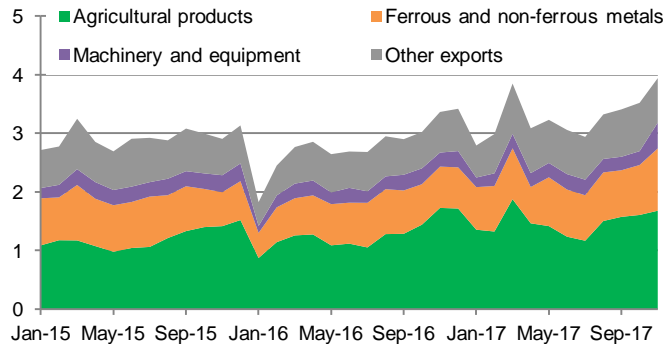
Source: NBU

**BoP vs change in foreign reserves, USDbn**



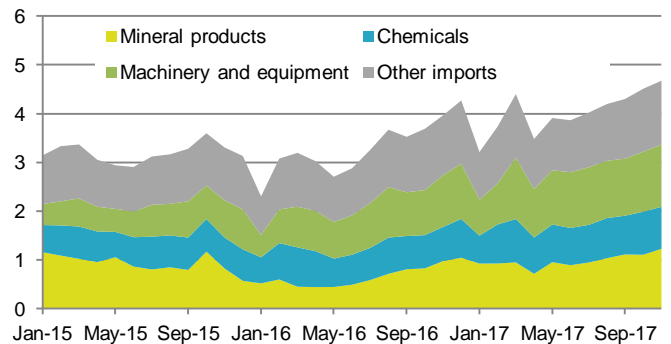
Source: NBU

**Exports components dynamic, USDbn**



Source: NBU

**Imports components dynamic, USDbn**



Source: NBU

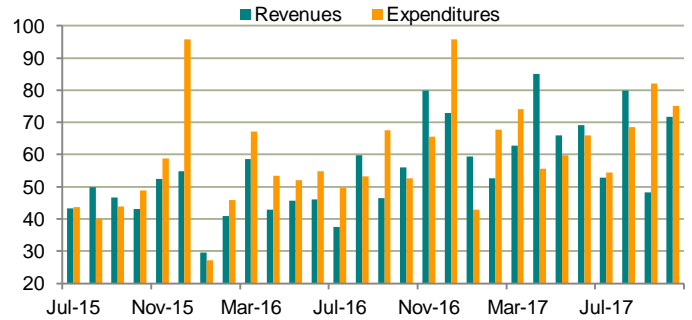


**Budget performance**

**Budget performance, UAHbn**

	Jan - Oct 2016	Jan - Oct 2017
<b>Budget revenues</b>	<b>463,6</b>	<b>647,5</b>
VAT proceeds	261,7	150,2
Corporate income tax	37,0	49,6
<b>Budget expenditures</b>	<b>523,4</b>	<b>646,2</b>
Deficit / Surplus	-59,8	1,2

**Monthly change in budget revenues and expenditures, UAHbn**

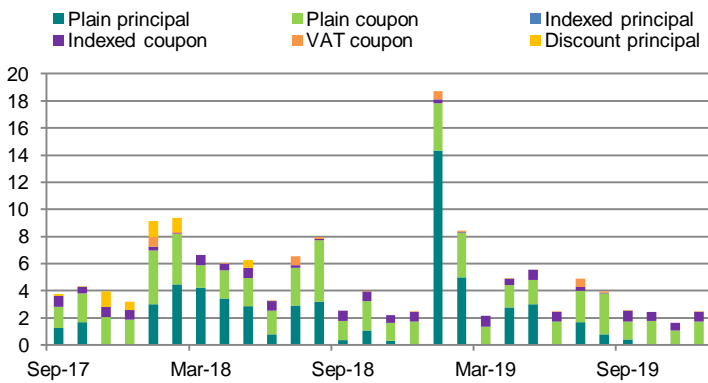


Source: NBU

Source: NBU, State Treasury

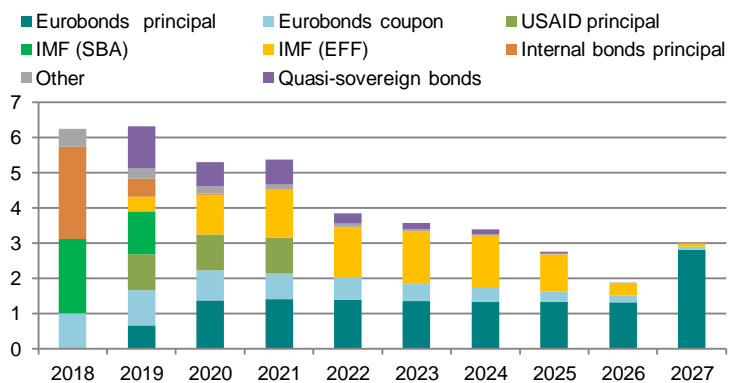
**Sovereign debt**

**UAH-denominated debts' repayments schedule, UAHbn**



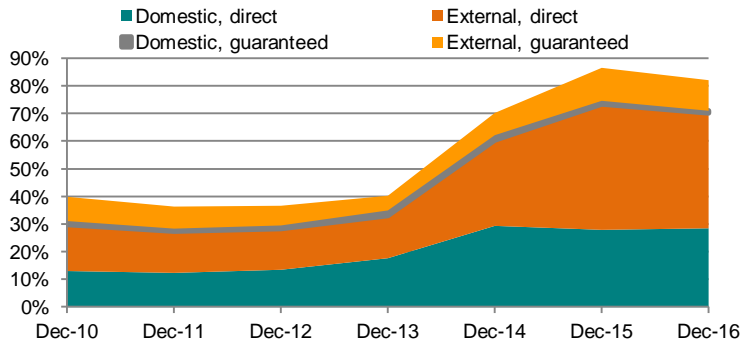
Source: NBU, UkrSibbank estimates

**FX-denominated external debts' repayments schedule, USDbn**



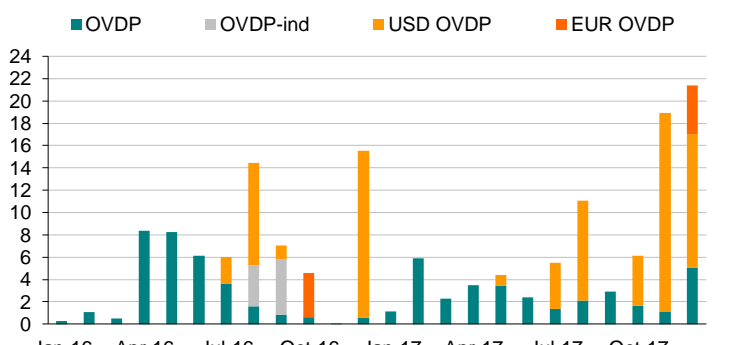
Source: Reuters, IMF, UkrSibbank estimates

**Total government debt, % GDP**



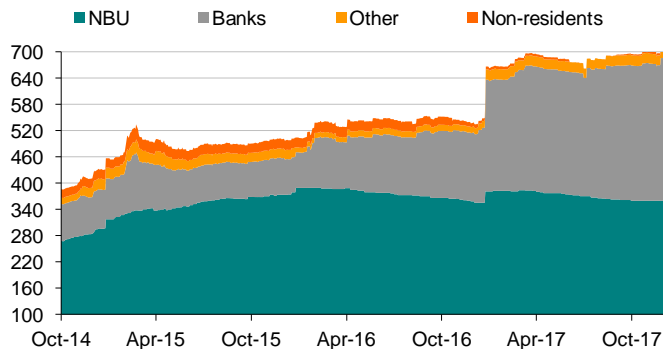
Source: MinFin

**Local borrowings, UAHbn equivalent**



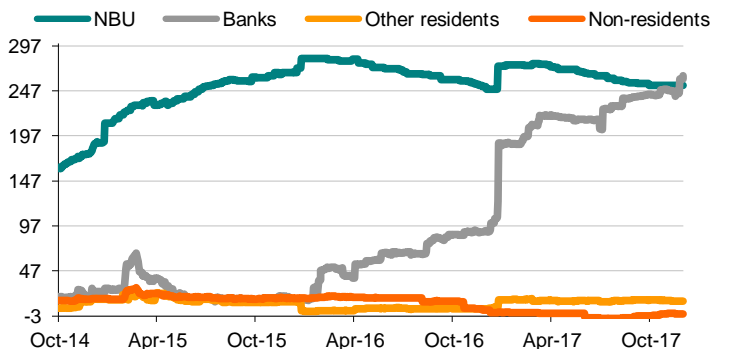
Source: NBU

**Outstanding OVDP owners structure, UAHbn**



Source: NBU

**Outstanding OVDP changes in holding, UAHbn**

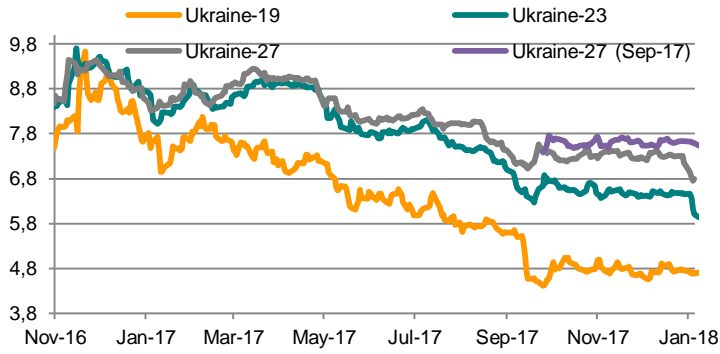


Source: NBU



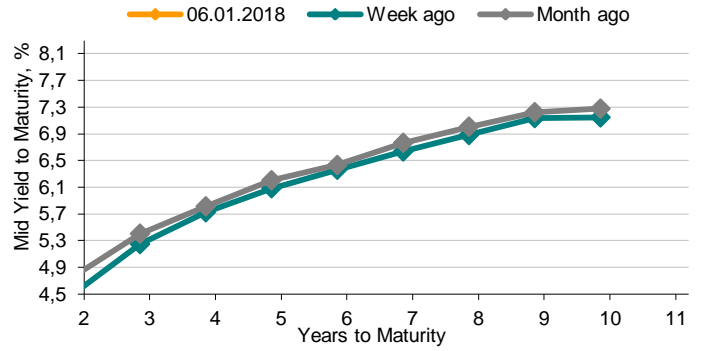
### Eurobond market

Ukraine's sovereign Eurobond yields, %



Source: Reuters

Ukraine's sovereign Eurobond yield curve



Source: Reuters

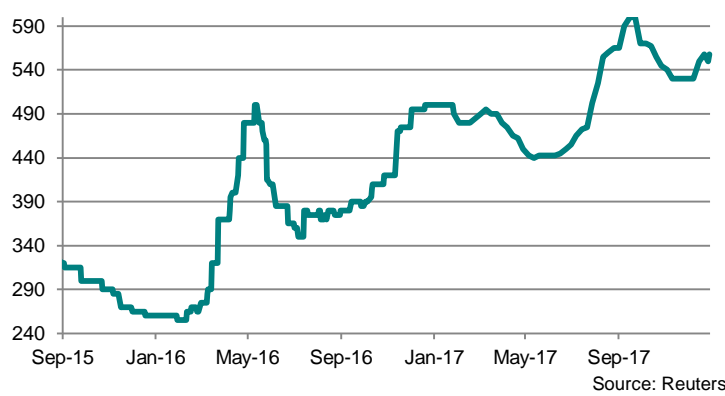
### Commodity markets

Iron ore 62% Fe (nearest active future at NYMEX), USD per ton



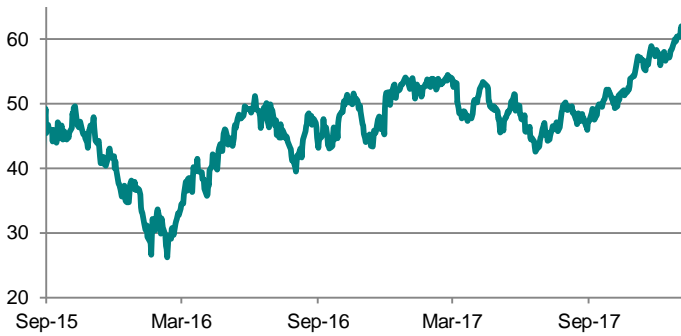
Source: Reuters

Steel CIS export HR coil, USD per ton



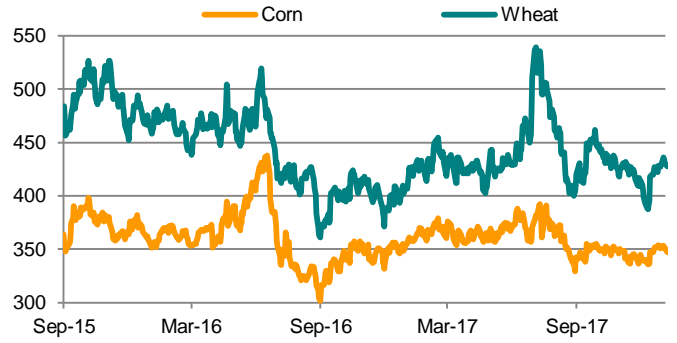
Source: Reuters

WTI oil (nearest active future at NYMEX), USD per barrel



Source: Reuters

Corn and wheat (nearest active future at CBT), USD per bushel



Source: Reuters



Key Macroeconomic Indicators											
Ratings (M/S&P/F) Caa2/B-/B-	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017E	2018F
<b>Real sector</b>											
Real GDP (%YoY)	2.3	-14.8	4.1	5.2	0.2	0.0	-6.6	-9.8	2.3	2.0	3.1
Industrial production (%YoY)	-5.2	-21.9	11.2	8.0	-0.7	-4.3	-10.7	-6.0	2.4	0.9	3.0
Retail sales (%YoY)	17.3	-20.9	10.1	13.2	12.3	6.1	-11.0	-25.0	4.0	8.0	7.0
Unemployment rate end of year (ILO, working age)	6.9	9.6	8.8	8.6	8.1	7.7	9.7	11.5	9.3	8.7	8.5
Nominal GDP (UAH bn)	948.1	913.3	1079.4	1299.9	1404.7	1465.8	1586.9	1979.5	2383.2	2855.5	3239.8
Nominal GDP (USD bn)	178.9	112.8	136.1	163.1	175.8	183.5	133.7	91.2	93.1	106.9	120.0
<b>Prices</b>											
CPI (average %YoY)	25.2	15.9	9.4	8.0	0.6	-0.2	12.1	48.7	16.5	12.5	9.0
CPI (end of year %YoY)	22.3	12.3	9.1	4.6	-0.2	0.5	24.9	43.3	12.4	13.0	9.0
Real average wage growth (%YoY)	6.3	-9.2	10.2	8.7	14.4	8.2	-6.5	-35.0	10.0	12.0	7.0
<b>Fiscal balance (% of GDP)</b>											
State budget deficit (without Naftogaz)	1.3	3.9	5.9	1.8	3.7	4.2	4.9	2.3	2.9	2.9	2.5
Total public debt	20.0	34.8	39.9	36.3	36.7	39.9	69.4	79.4	81.0	77.0	76.0
<b>External balance</b>											
Exports of goods and services (USD bn)	67.7	40.4	65.6	83.7	86.5	81.7	65.4	47.9	46.0	53.0	53.5
Imports of goods and services (USD bn)	83.8	44.7	69.6	93.8	100.9	97.4	70.0	49.6	51.8	59.3	62.3
Current account balance (USD bn)	-12.8	-1.7	-3.0	-10.2	-14.3	-16.5	-4.6	-0.2	-3.8	-4.5	-5.1
Current account balance (% of GDP)	-7.1	-1.5	-2.2	-6.3	-8.1	-9.0	-3.4	-0.2	-4.1	-4.2	-4.3
Net FDI (USD bn)	9.9	4.7	5.8	7.0	7.2	4.1	0.3	3.0	3.4	2.2	2.5
Foreign exchange reserves (end of year)	31.5	26.5	34.6	31.8	24.5	20.4	7.5	13.3	15.5	18.8	22.0
Imports coverage (months of imports of goods)	4.5	7.1	6.8	4.5	3.3	2.9	1.5	4.4	3.7	4.4	4.7
<b>Interest and exchange rates</b>											
NBU discount rate (% end of year)	12.00	10.25	7.75	7.75	7.50	6.50	14.00	22.00	14.00	14.50*	14.00*
Exchange rate (UAH/USD) end of year	8.1	8.0	7.9	8.0	8.1	8.2	15.8	24.0	27.2	27.5*	29.5*
Exchange rate (UAH/EUR) end of year	10.9	11.5	10.5	10.4	10.6	11.3	23.0	26.2	28.3	31.5*	32.5*

Source: UkrStat, NBU, MinFin, UkrSibbank

\* Broad estimate



## Contacts

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### **Dmytro Tsapenko**

Head of ALMT&Capital Markets  
(+38044) 537 5015

### **Serhiy Yahnych**

Head of Investment Business  
(+38044) 537 5082 [serhii.yahnych@ukrsibbank.com](mailto:serhii.yahnych@ukrsibbank.com)

### **Oleksandr Duda**

Head of FX Sales  
(+38044) 537 5002 [oleksandr.duda@ukrsibbank.com](mailto:oleksandr.duda@ukrsibbank.com)



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