



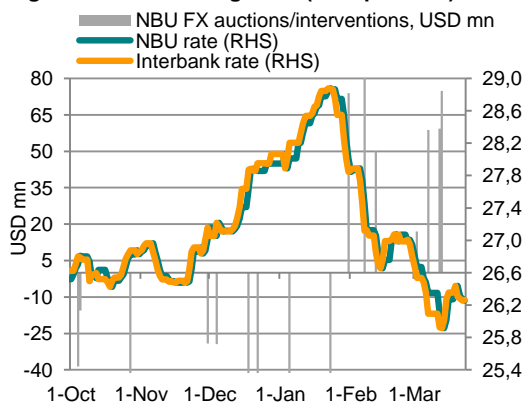
**This week in focus: Growth to accelerate**

The recent slate of economic data suggests that economy is on track to outpace prior year result. We treat a retail sales slowdown as temporary due to its inherent volatility. Industrial production will likely be in the forefront this year, as the effect of trade blockade is poised to fade away in 2018, with a statistical effect reversing to the tailwind. We keep our GDP and IP growth forecasts in 2018 unchanged at 3.1% and 3.0%, respectively.

*Please see page 3 for more details*

**FX and interest rates: NBU increased estimates of money transfers**

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



Source: NBU, Reuters

**USD/UAH closed at 26.27 as of Friday the 23<sup>rd</sup>.** The exchange rate dynamic was almost flat during the week.

**Average daily FX volumes on the market amounted to the equivalent of USD 225.6mn,** USD 26.4mn lower compared to previous week.

**NBU held no currency auction during the week,** as market remained almost balanced. NBU bought USD 74.9mn on March 13<sup>th</sup> last time via currency auctions.

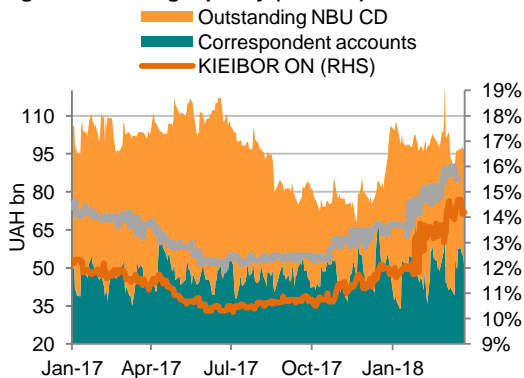
**Aggregate banking liquidity amounted to UAH 96.9bn as of Friday the 23<sup>rd</sup>,** growing merely by UAH 0.2bn during the week.

**Money market rates remained flat:** cost of ON funds is around 13.0/15.25, 1 week is 14.0/16.25 while 1M is 15.0/17.0, according to our calculations.

**MoF proceeds from the auction yielded UAH 6.4bn of proceed.** For 3M bonds the Ministry of Finance increased previously set cap from UAH 0.5bn to UAH 1bn, at the same time demand rose also, reaching UAH 1.8bn. In contrast to that limit for 6M issue remained at UAH 0.5bn, meanwhile, demand accounted for UAH 0.7bn. Among hryvnia denominated issues 3m bonds took the top spot by proceeds to the budget, while 9m issue was ranked first by applied demand. On Friday 27<sup>th</sup>, MoF's to issue USD denominated bonds, along with UAH-denominated 3m, 6m, 9m, 12m and 5y bonds.

**Currently, yields (bids) of local OVDP in UAH at 17.75% (for 6m), 17.75% (for 2Y).** 1Y USD bids were at 5.50%, while bids for VAT bonds were at 17.95%.

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

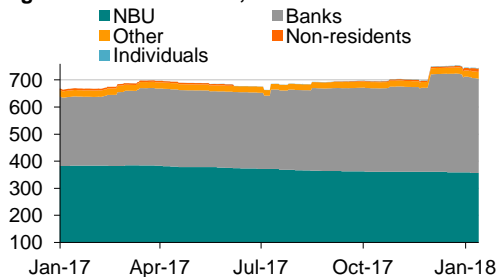


Source: Reuters, NBU, UkrSibbank, Minfin

**Figure 5. OVDP auction combined results, 20<sup>th</sup> of March 2018**

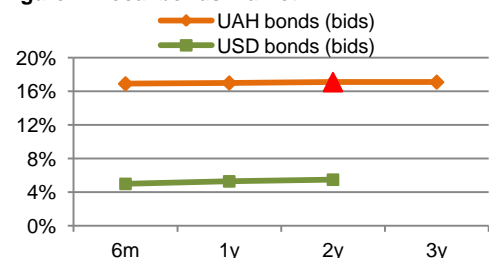
CCY	Maturity	Cut-off rate	WA rate	Max bid rate	Min bid rate	Number of bids	Bids accepted	Bid size	Placement size
UAH	3m	17.44%	17.44%	18.00%	17.39%	19	9	1.8bn	964.5mn
UAH	6m	17.00%	17.00%	17.20%	17.00%	8	7	703.4mn	463.7mn
UAH	9m	17.10%	17.01%	17.49%	17.00%	8	6	2.0bn	749.8mn
UAH	2y	16.10%	16.10%	16.40%	16.10%	5	4	102.5mn	2.5mn
UAH	3y	16.15%	16.15%	16.25%	16.05%	6	5	270.7mn	173.0mn
EUR	1.5	4.17%	4.12%	4.17%	3.95%	7	7	121.8mn	123.3mn

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



Source: NBU

**Figure 4. Local bonds market**



Source: UkrSibbank

**Ukraine's state property fund had withdrawn from the auction stakes in two state electricity distribution companies.** Initially, state's fund planned to sell 25% stakes in Odesaoblenergo and Sumyoblenergo companies as of March 20<sup>th</sup> and as of March 30<sup>th</sup>, respectively. The main reason of that is newly adopted legislation, which changed the process of privatization significantly. Beginning price of blocking stake of Odesaoblenergo and Sumyenergo was UAH 149.1mn and UAH 106.3mn. In August, State property fund offered this stakes for sell at UAH 631.3mn and UAH 370.3mn, respectively.

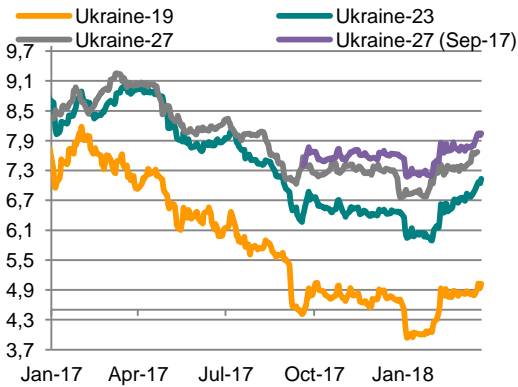
**NBU had revalued previously reported figures about money transfers from abroad due to new available data,** which points out to changes in migration flows. The largest revaluation was due to changed estimates of informal flows, which were assessed by special polls, as opposed to official flows which go directly through banks and international payment systems. As a result of that, NBU revised previously reported figures of money transfers by USD 1.8bn in 2015 (to USD 7.0bn), by USD 2.1bn in 2016 (to 7.5bn) and by USD 2.0bn in 2017 (USD 9.3bn). Which in turn caused the C/A deficit to improve from 0.2% of GDP to 1.8% of surplus in 2015, from deficit of 3.7% of GDP to 1.4% of deficit in 2016 and from a deficit of 3.7% of GDP to deficit of 1.9% of GDP in 2017. We welcome review of NBU methodology, as prior estimates obviously failed to capture the flow of transfers from Poland, the most active direction of Ukraine's labor force migration to EU. With the new methodology, we put out BoP forecasts on review, revising data for current account (transfers) and financial account (cash outside banks).



**Global markets:**

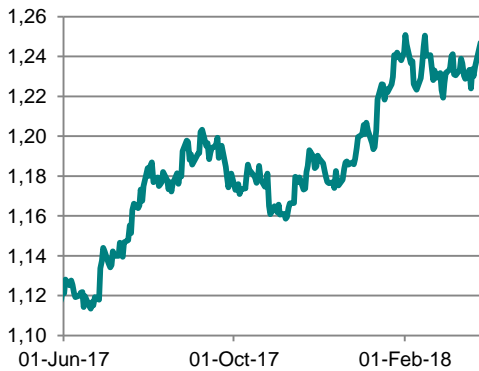
**U.S. bracing for a trade war with China**

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



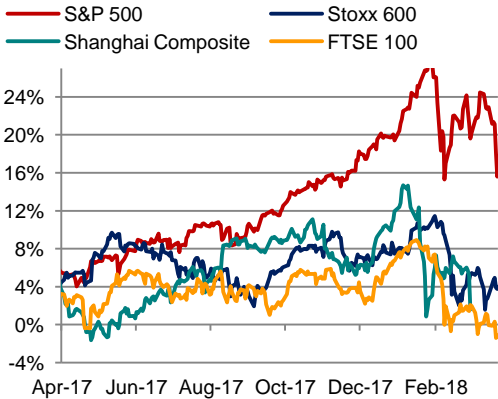
Source: Reuters

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



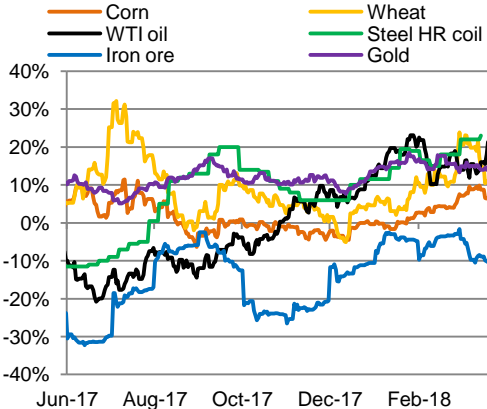
Source: Reuters

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



Source: Reuters

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



Source: Reuters

Having fallen by around 6% week-on-week, U.S. markets were permeated by the fear of growing possibility of a full-scale trade war with China. The main fear came primarily from memorandum signed by Donald Trump, targeting up to USD 60bn in Chinese goods with tariffs reflecting misappropriation of U.S. intellectual property. At the same time, U.S. tariffs provoked retaliation from China, targeting USD 3bn of U.S. import. Meanwhile, EU leaders gathered in Brussels and backed Britain in blaming Moscow for former spy poisoning.

**Bond benchmarks advanced**, with U.S. 10y Treasuries' yield lower by 3bp week-on-week falling to 2.81%, while German 10y Bunds' yields fell by 5bp, landing at 0.53%, Japanese 10y bonds yield's declined and ended the week at 0.023%.

**US equities are on the downside again, as fear of trade war had sent U.S. stock lower.** U.S. stock indices fell sharply on Friday, with the S&P 500 down over 2%, bringing its loss on the week to around 5% for the year, and almost 10% below its record highs reached in January. In line with S&P, Nasdaq Composite was down 2.4% on Friday and over 6% on the week, as Cambridge Analytica scandal party contributed to the downside. The main concern for the market was growing tensions over trade and tariffs between U.S. and China and its ramifications on the health of American business.

**In prior week, U.S. President Donald Trump signed a memorandum which target up to USD 60bn in Chinese goods with tariffs** aimed at misappropriation of U.S. intellectual property, which take effect only after 30-day consultation period after it was published. U.S. treasury department was given a 30-day consultation period to develop fresh investment restrictions with a purpose of preventing Chinese-controlled companies and funds from acquiring U.S. firms the valuable technologies.

**EUR/USD rate landed at 1.2351 as of Friday the 23<sup>rd</sup>**, higher than the last week closing level of 1.2287, as the USD underperformed against its main peers.

**Stoxx 600, a broader gauge of European equity performance fell strongly by 3.1% during the week, while German DAX plunged even stronger by 4.1% week-on-week.**

**EU leaders of 28 of 28 member states met on 22-23 March in Brussels to discuss such issues as poisoning, trade, tariffs, Eurozone reform, Brexit, digital taxation.** They backed Britain in blaming Moscow over agent attack of former Russian spy. At the same time, the leaders postponed a decision on trade, as they lacked a clarity on that issue. Moreover, leaders of the member states renewed pledges to complete a banking union and develop a bailout fund. In regard to Brexit, leaders are expected to sign off a broad agreement for the U.K. leaving the union.

**U.S. tariffs provoke retaliation from Chinese authorities.** After Trump signed his presidential memorandum, imposing a USD 60bn of tariffs, China's embassy in the Washington answered on that with a promise to retaliate. Not so long after that, China introduced reciprocal tariffs on U.S. import, targeting a USD 3bn. According to Chinese officials, import which levied by newly introduced restrictions will include products from steel to pork. On top of that, China plans to take legal actions against the U.S. under World Trade Organization rules. Namely, Commerce Ministry plans a 25% tariff on United States pork import and 15% tariff on U.S. steel pipes.

**Crude oil prices gained**, as WTI futures increased by 5.8% week-on-week and closed at USD 65.9 per barrel, while Brent 1m futures rose by 6.4%, closing at USD 70.5 per barrel.

**Gold prices increased**, as NYMEX 1m futures gained by 2.9% week-on-week and finished the week at USD 1349.3 per troy ounce.

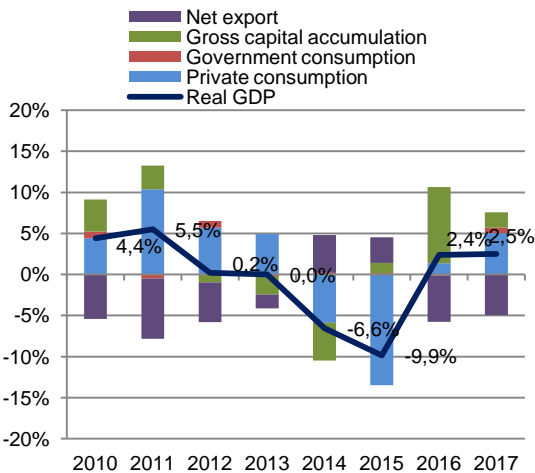
**Grains were in the red**, as CBOT Corn 1m futures fell 1.4% week-on-week and closed at USD 377.3 per bushel, while CBOT Wheat 1m futures landed at USD 460.3 per bushel, 1.6% lower week-on-week.

**Iron ore declined** as NYMEX Iron ore 62% Fe 1m futures fell by 3.3% week-on-week and closed at USD 70.3 per ton.



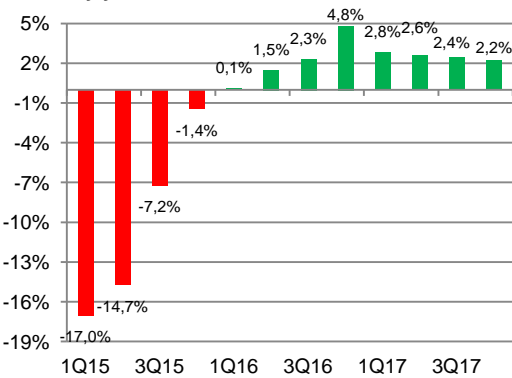
**This week in focus: Growth to accelerate**

**Figure 9. Ukraine's real GDP growth in 2010-2017**



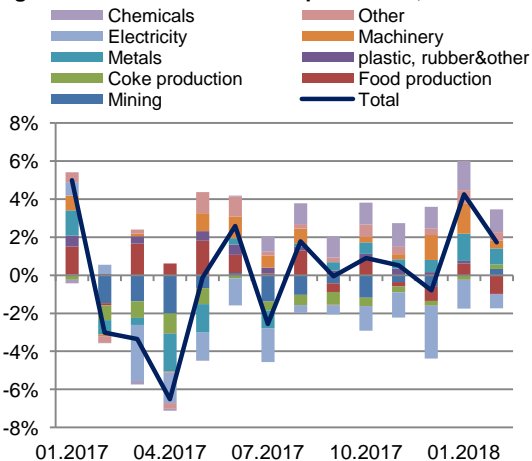
Source: Ukrstat

**Figure 10. Ukraine's real GDP quarterly in 2015-2017, % y/y**



Source: Ukrstat

**Figure 11. Ukraine's industrial production, %**



Source: Ukrstat

The recent slate of economic data suggests that economy is on track to outpace prior year result. We treat a retail sales slowdown as temporary due to its inherent volatility. Industrial production will likely be in the forefront this year, as the negative effect of trade blockade is poised to fade away in 2018, with statistical effect reversing to the tailwind. We keep our GDP and industrial production growth forecasts unchanged at 3.1% and 3.0%, respectively.

Having risen by 5.6% y/y in February, retail sales reading indicated slowdown in its expansion, falling for a two month in a streak. Having kept weaker on a year-on-year basis, on a month-over-month basis retail sales declined by 5.4% in February. For 2M2017, retail sales growth amounted to 7.5% YTD, much higher than 0.3% YTD a year ago. Retail sales dynamic proved to be volatile but consumer spending at the start of the year was at a much solid footing compared to a year ago.

The average wage growth, according to latest available Ukrstat reading, rose by 28.4% y/y in January, slowing its pace of expansion from 35.5% y/y growth reached in December 2017. The slowdown primarily due to the fact that Cabinet of Ministers increased minimal wage to UAH 3200 or almost twofold since January 1, 2017. Following this decision, average nominal wage surged by 37.7% y/y in January 2017, up from 23.8% y/y in December 2016. Due to statistical effect starting from January 2018 this wage growth is destined to fall further, reflecting statistical effect of higher comparison base. But due to minimum wage increase to UAH 3723 since January 1<sup>st</sup>, 2018, it was partly offset, as this increase in percentage terms is much lower compared to a year ago. Ukraine's President mentioned about possibility of further minimal wage increase to UAH 4100 in second or third quarters of this year, strengthening consumer spending one more time at the expense of fiscal balance. Until the slate of economic data tells us otherwise, we treat this possibility as to be highly likely.

Last week Ukstat revised its estimates of GDP growth. Previously, Ukrstat reported 1.8% y/y growth in 4Q 2017, implying around 2.1-2.2% y/y growth for the full 2017. All in all, we consider Ukraine's economy on track to post more solid footing this year.

Last week release revealed that Ukrstat drastically increased its previously reported numbers by 12% (to 2.8% y/y) in 1Q 2017, by 13% (to 2.6% y/y) in 2Q 2017, by 14% (to 2.4% y/y) in 3Q 2017 and by 22% (to 2.2% y/y) in 4Q 2017. Moreover, GDP growth for the full 2017 year amounted to 2.5% y/y. Interestingly, that 4Q 2017 real GDP reading estimate was revealed only in February, at the same time it was changed the most significantly among all estimates. On top of that, Ukrstat also increased its previously estimated GDP growth in 2016 to 2.4% y/y from 2.3% y/y reported previously.

Breaking down GDP by final use category, private consumption increased by 7.8% y/y in 2017, up from 1.8% y/y in 2016, supported primarily by higher wages. The effect of twofold minimal wage increase effective January 1, 2017 is in the front seat here as it contributed the most to nominal (and real) wage growth in 2017. While we observed that gross capital accumulation landed at 9.0% in 2017, from 42.8% y/y in 2016, it was not due to several times declined business investments in the country, which accounts for the major share in this category. These investments in fixed capital rose by 18.2% y/y in 2017, down from 20.1% y/y reported in 2016, highlighting that they remained effectively at the same level as in prior year. The foregoing landing to 9% was a result of decrease in inventories by the end of the year, as accumulated grain inventory fell lower by the end of 2017 compared to a year ago level. In contrast to 2017, inventories accumulation skyrocketed in 2016, leading to a surge in gross capital accumulation.

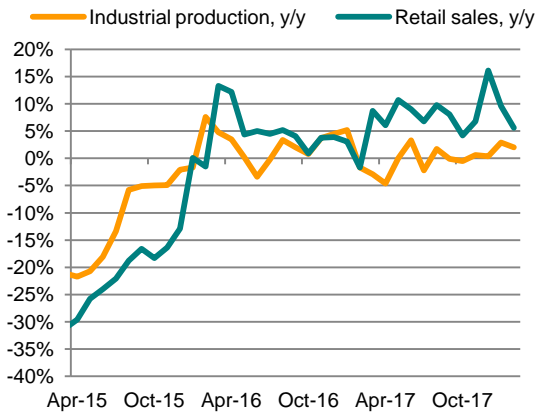
Notwithstanding dramatic increase in private consumption, the negative effect of trade (with services) balances was not so pronounced, as should be expected. In particular, export rose by 3.5% y/y and import advanced by 12.2% y/y in 2017. Having declined in 2016, government consumption also positively contributed to GDP in 2017 in line with consumption and investments. Although, official trade blockade had started in the beginning of 2017, economy was doing quite well, even amid the lower harvest of crops, which hit economic growth primarily in fourth quarter. We expect to see even more healthy footing for Ukrainian economy this year. We keep our real GDP growth forecast unchanged at 3.1% in 2018.

On Thursday, Ukrstat said that Ukraine's industrial production gained by 1.9% y/y (and by 2.0% y/y adjusted for calendar day effect) in February. For 2M 2018, industrial production rose by 2.8% y/y, down from 3.6% y/y in prior month.

Growth in mining sector turned positive for the first time since June 2017 at the same time posting the highest growth since November 2016. Having broken an 8

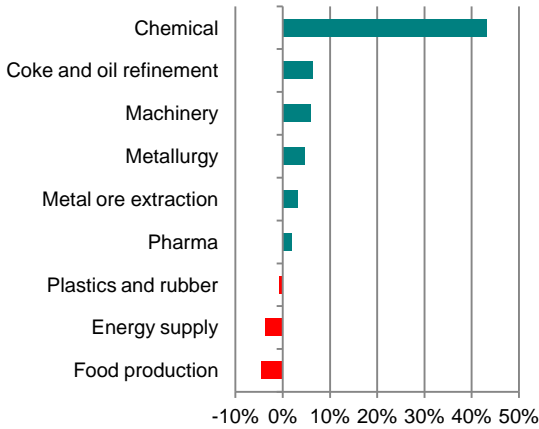


**Figure 11. Industrial production and retail sales in 2015-2018, % , y/y**



Source: Ukrstat

**Figure 11. Output of key industries in February 2018, % , m/m,**



Source: Ukrstat

consecutive month of losses, mining demonstrated upbeat performance, as statistical drop due to Donbas blockade faded away. Mining activity delivered growth of +2.3% y/y, outpacing -0.2% y/y decline in prior month. The main factor behind that was meaningfully improved decline in coal mining to -2.2% y/y, from -22.9% y/y decline in prior month. We expect the mining to pick up its steam further in the coming months.

**Having grown by 9.7% y/y in January, manufacturing sector delivered less upbeat results in February**, as the effect of lower 2017 year harvest more strongly had been reflected in statistics.

**Food production had turned around strongly also**, in line with mining, but instead demonstrated more weak footing, being the heaviest drag on IP's growth. Having weighted on the industrial production growth by 4,6% in February, food production reflected the effect of 2017 year harvest more strongly than in January.

**Although chemical production growth slowed to 43.1% y/y in February**, from 55.9% y/y in January, at the same time it kept its pace of growth at the high level. Chemical production, which was a subject to high volatility since July 2017 (when Ostchem launched its chemical plants), contributed around percentage point to the IP February's reading, being at the same time almost the largest single contributor to IP growth since the second half of 2017, according to Ukrstat's research. Historically, Ukraine's experienced strong decline in chemical production since 2013, exacerbated in 2014 and 2015. The main raw material in chemical production is natural gas, which accounts for the largest part of costs for chemical plants. When Ostchem group had lost its access to cheap Russian gas, the crisis for the chemical production in Ukraine had effectively unfolded. Increased price of oil poses a threat to profitability of such plants, which walking on the edge to breaking even, if prices are to increase further.

**Production of metals delivered also smaller gains in February** than a month ago, growing by 4.6% y/y during the month, down from 7.9% in January. International prices of steel, which Ukraine exported the most, advanced in recent time, putting some upward pressure on growth perspective in the short-term for local producers. HRC prices are hovering around 615 USD/tone now, up from of 507 USD/tone average price in 2017.

**Machinery output in line with the performance of the largest sectors demonstrated less growth in February compared to an upswing posted in January**. It output growth landed at 5.9% y/y, down from 22.1% y/y a month ago.

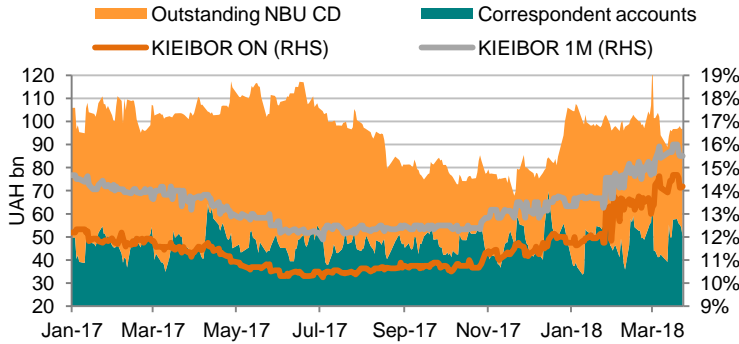
**Having been acted as the largest drag on industrial production output in 2017, growth in utilities output reduced that negative contribution strongly in February**, being in decline at 3.8% y/y, improving from 8.1% y/y drop in January.

**Our production growth forecast at 3.0% for the year looks feasible at this juncture with some upside potential and we keep it unchanged.**



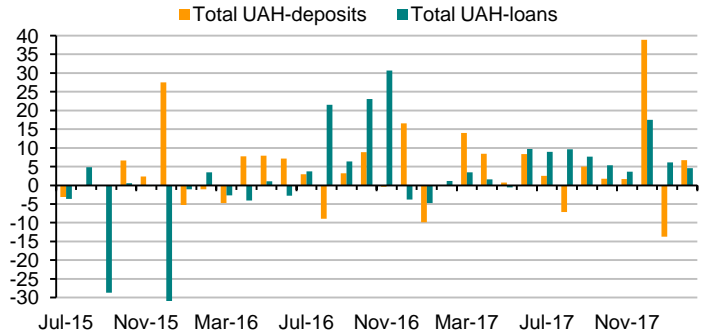
**Money market**

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



Source: Reuters, NBU, UkrSibbank estimates

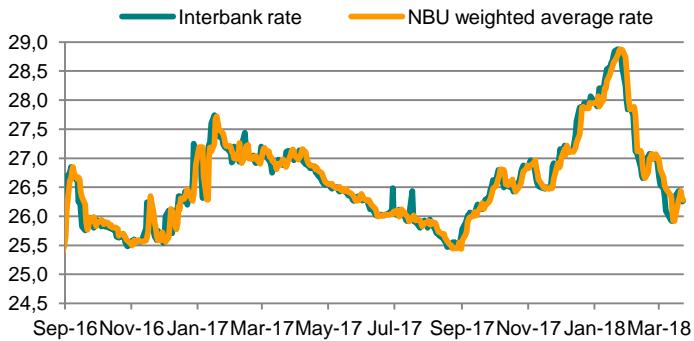
**Monthly change in local currency loans and deposits, UAHbn**



Source: the NBU

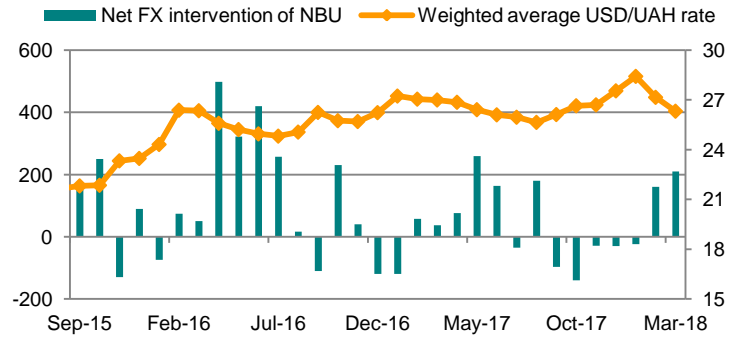
**Currency market**

**UAH exchange rate, UAH/USD**



Source: Reuters

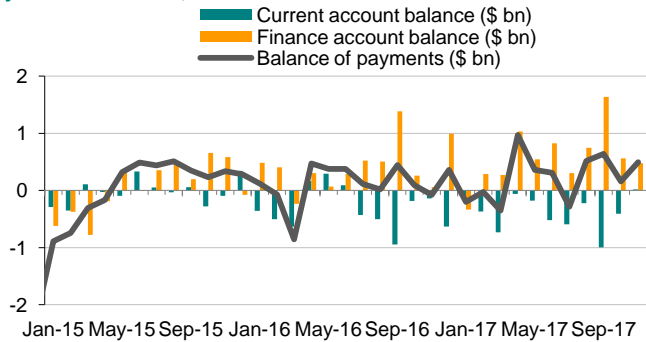
**Net retail FX interventions of the NBU in 2015-2017, USDmn**



Source: NBU

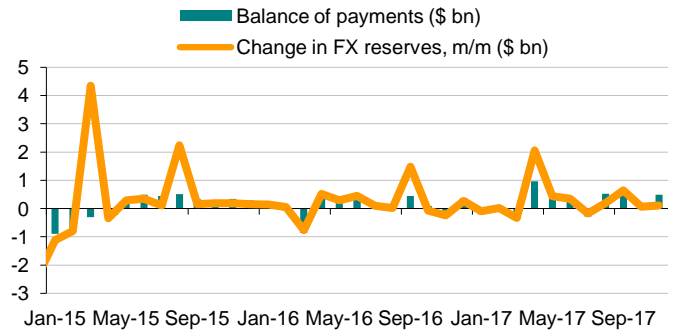
**Balance of payments**

**Major BoP accounts, USDbn**



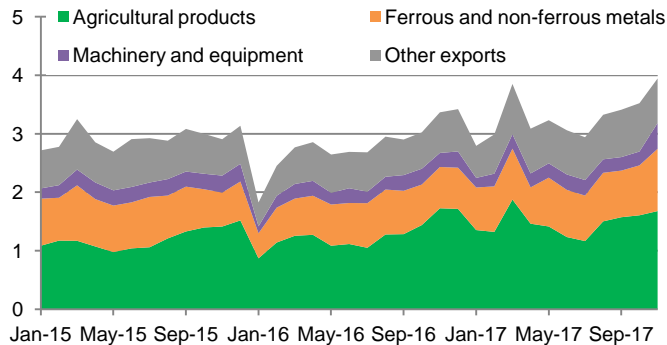
Source: NBU

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



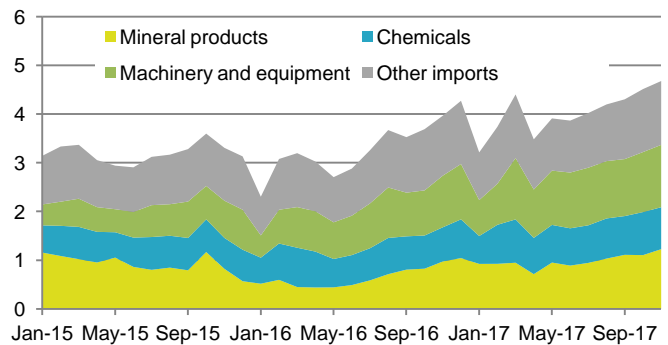
Source: NBU

**Exports components dynamic, USDbn**



Source: NBU

**Imports components dynamic, USDbn**



Source: NBU

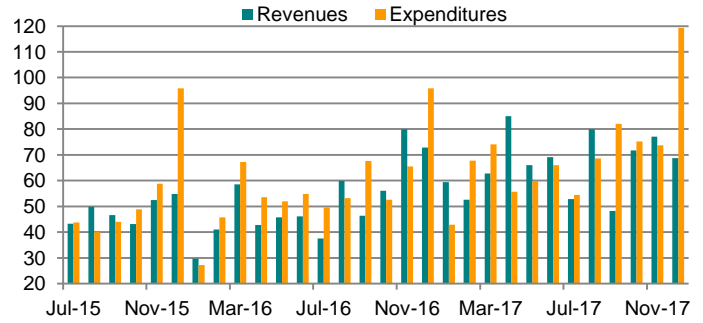


**Budget performance**

**Budget performance, UAHbn**

	Jan – Dec 2016	Jan - Dec 2017
<b>Budget revenues</b>	<b>616,3</b>	<b>793,3</b>
VAT proceeds	329,9	183,5
Corporate income tax	54,3	66,9
<b>Budget expenditures</b>	<b>684,7</b>	<b>839,2</b>
Deficit / Surplus	-68,5	-46,0

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

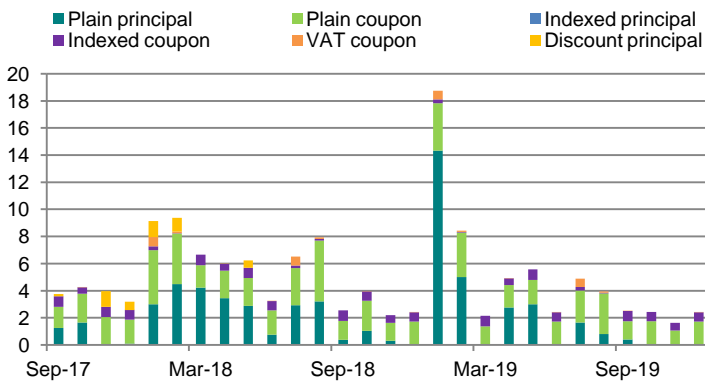


Source: NBU

Source: NBU, State Treasury

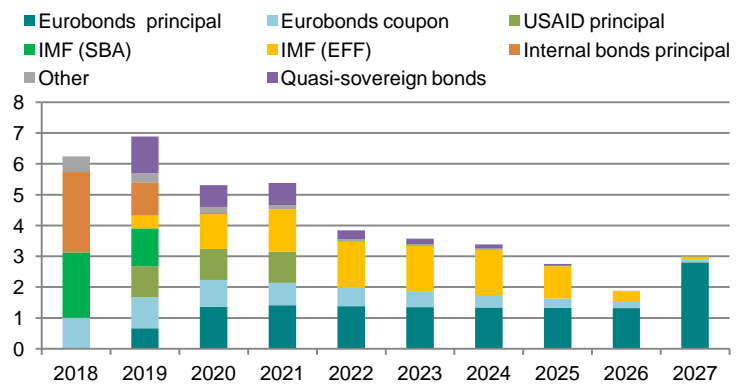
**Sovereign debt**

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



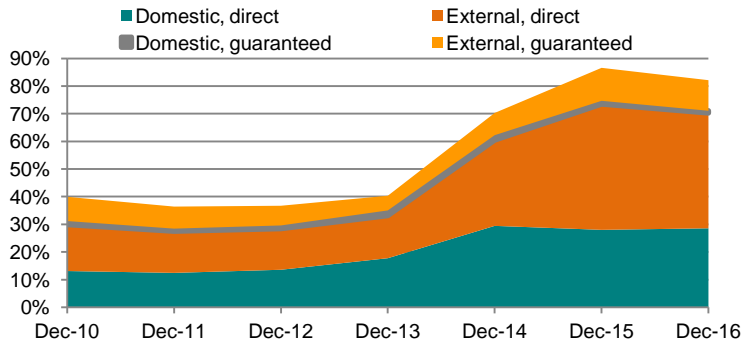
Source: NBU, UkrSibbank estimates

**FX-denominated debt repayments schedule, USDbn**



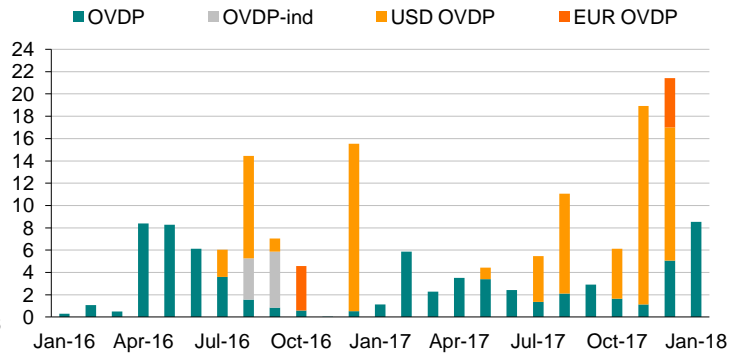
Source: Reuters, IMF, UkrSibbank estimates

**Total government debt, % GDP**



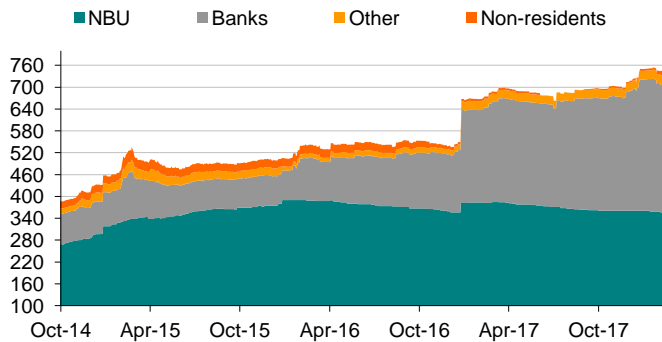
Source: MinFin

**Local borrowings, UAHbn equivalent**



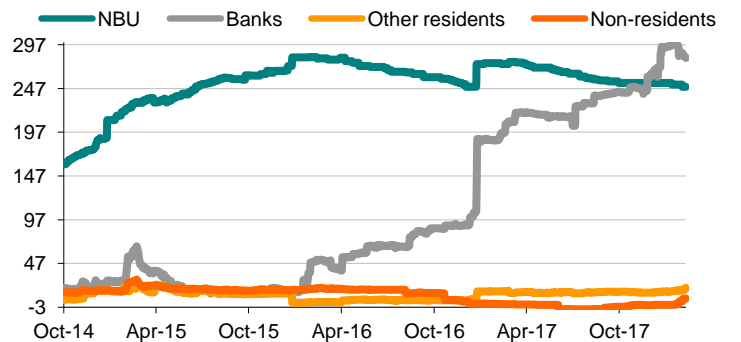
Source: NBU

**Outstanding OVDP owners structure, UAHbn**



Source: NBU

**Outstanding OVDP changes in holding, UAHbn**

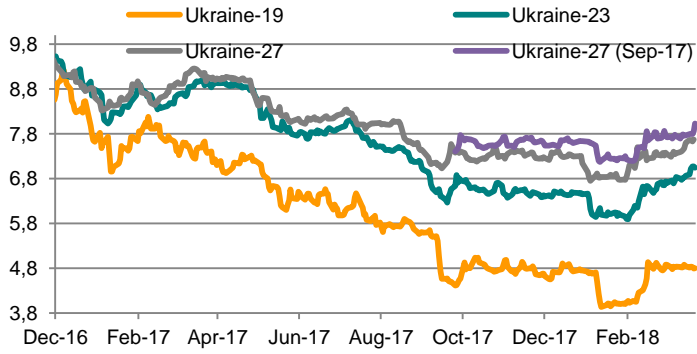


Source: NBU



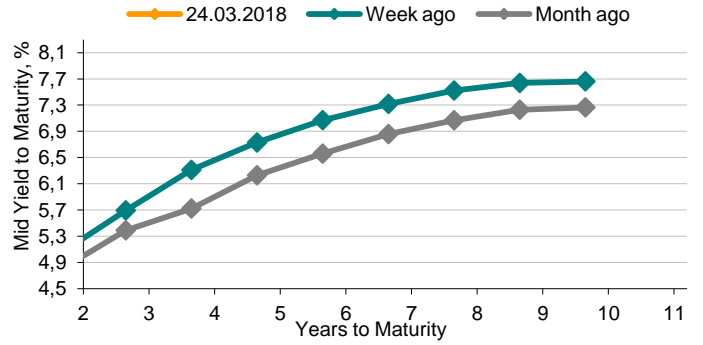
### Eurobond market

Ukraine's sovereign Eurobond yields, %



Source: Reuters

Ukraine's sovereign Eurobond yield curve



Source: Reuters

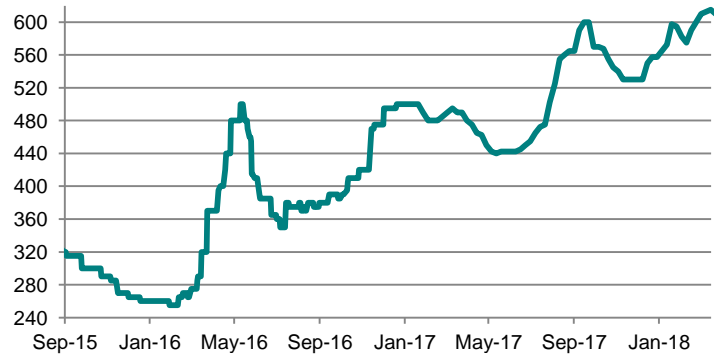
### Commodity markets

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



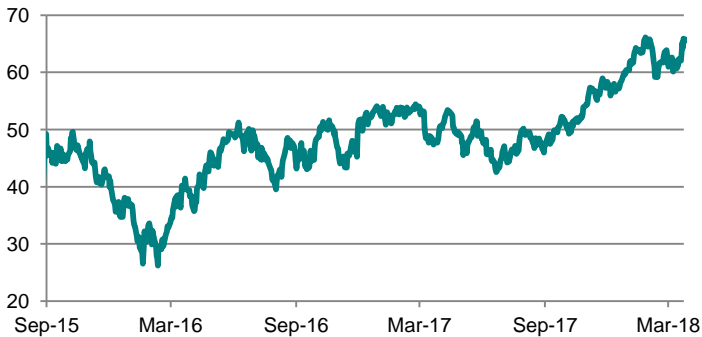
Source: Reuters

Steel CIS export HR coil, USD per ton



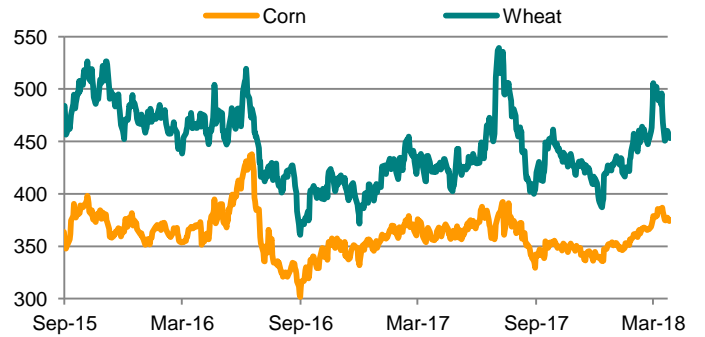
Source: Reuters

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	-0.1	3.0
Retail sales (%YoY)	17.3	-20.9	10.1	13.2	12.3	6.1	-11.0	-25.0	4.0	8.8	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	14.4	11.9
CPI (end of year %YoY)	22.3	12.3	9.1	4.6	-0.2	0.5	24.9	43.3	12.4	13.7	10.9
Real average wage growth (%YoY)	6.3	-9.2	10.2	8.7	14.4	8.2	-6.5	-35.0	10.0	18.9	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	1.6	2.4
Total public debt	20.0	34.8	39.9	36.3	36.7	39.9	69.4	79.4	81.0	72.0	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	54.0	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	60.8	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	-3.8	-5.3
Current account balance (% of GDP)	-7.1	-1.5	-2.2	-6.3	-8.1	-9.0	-3.4	-0.2	-4.1	-3.6	-4.4
Net FDI (USD bn)	9.9	4.7	5.8	7.0	7.2	4.1	0.3	3.0	3.4	2.3	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	3.6	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	27.95	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	33.50	32.5*

Source: UkrStat, NBU, MinFin, UkrSibbank

\* Broad estimate





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