



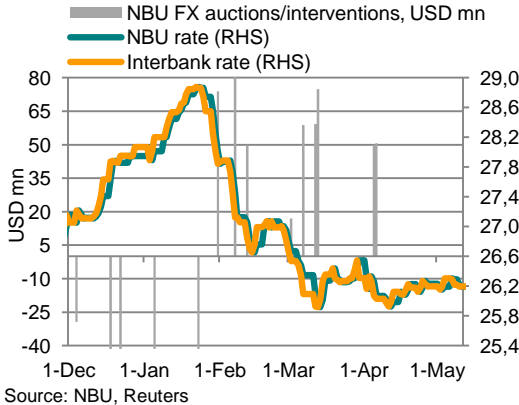
This week in focus: Economic growth is still strong

In 4M2018, retail sales continued to post strong performance, increasing by 7.0% y/y. At the same time, in 4M 2018, industrial production growth was driven by utilities, followed by chemical production and other. It's noteworthy, that almost all major industries were growing. At the same time we expect these industries to pass a baton to food industry in securing higher IP growth very soon. We keep our IP and real GDP growth at 3.0% and 3.1% in 2018 unchanged.

Please see page 3 for more details

FX and interest rates: NBU kept main rate on hold

Figure 1. UAH exchange rate (UAH per USD)



Source: NBU, Reuters

USD/UAH closed at 26.15 as of Friday the 25th, at the same exchange rate comparing to week ago, as hryvnia were flat during the week.

Average daily FX volumes on the market amounted to the equivalent of USD 250.1mn, almost the same compared to previous week.

NBU interventions resulted in net buying of foreign currency, amounting to USD 47mn during the week. At the same time, YTD reading remained at USD 1.2bn. In line with previous auctions, matching was the main tool through central bank made interventions on the market.

Aggregate banking liquidity amounted to UAH 113.6bn as of Friday the 25th, increasing by UAH 5.0bn during the week. Having declined due to tax payments a week ago liquidity advanced strongly in the week ending Friday 25th, stemming mainly from spike in VAT refund by the State treasury. In particular, state treasury reimbursed UAH 5.3bn (or 60% from monthly total reimbursement) in bulk on Thursday or closely the amount by which banking liquidity rose during the week. In aggregate, VAT was reimbursed for a total UAH 8.7bn during the month (the figure does not include the reimbursements on Friday). In prior month VAT reimbursements accounted for UAH 9.9bn.

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.

USD denominated issues were at the forefront on the latest primary auctions, while UAH placements took the back seat this time. In particular, MoF issued 3 USD placements, out of which two with maturities close to 2 years took the top spot on the latest auction, both attracting to the state budget in excess of USD 100mn, satisfying effectively all demand of primary dealers on both issues. In regard to UAH issues there was moderate demand. Moreover, MoF issued the only shortest bonds (3m), followed simultaneously by quite long (3y) bonds, refraining from issuance those who can fill the gap between those maturities. In June, are to be redeemed UAH issues totalling UAH 2.9bn, with concentration skewed toward the first week of June (on June 6th is to be redeemed UAH denominated bond placed in the beginning of March 2018 totalling UAH 2.2bn). At the same time, two USD denominated issues are to be redeemed totalling USD 437mn in June too. In particular, USD 387 is to be redeemed on June 13th during the second week of month.

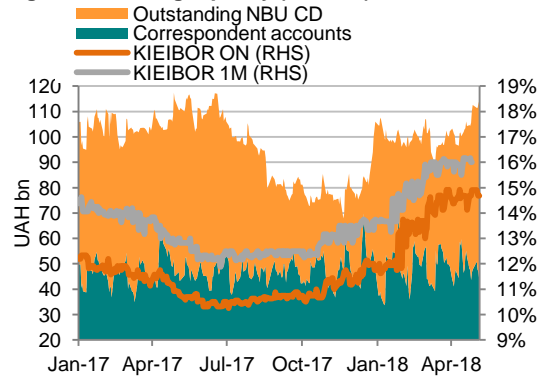
Currently, yields (bids) of local OVDP in UAH at 17.75% (for 6m), 17.70% (for 2Y). 1Y USD bids were at 5.35%, while bids for VAT bonds were at 17.95%.

Figure 5. OVDP auction combined results, 22th of May 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%	17.41%	17.75%	17.39%	10	9	85.8mn	82.8mn
UAH	3y	16.10%	16.10%	16.10%	16.10%	4	4	78.8mn	82.1mn
USD	2y	5.65%	5.63%	5.65%	5.40%	9	9	113.2mn	113.1mn
USD	1.8y	5.60%	5.60%	5.60%	5.40%	3	3	101.3mn	100.2mn
USD	1.4y	5.40%	5.32%	5.60%	5.30%	8	7	57.7mn	57.9mn

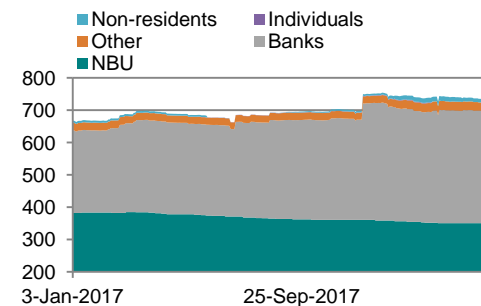
The NBU board decided to leave main interest rate unchanged effective May 24th at 17.0% in line with our expectations. NBU maintained its rhetoric and guidance that 'the current monetary conditions are sufficiently tight to bring inflation to its medium-term target'. NBU continued to expect inflation to land at 8.9% by the end of 2018. At the same time, the major risk on the current agenda is sustained progress in structural reforms implementation, in particular under current IMF program.

Figure 2. Banking liquidity (UAH bn)



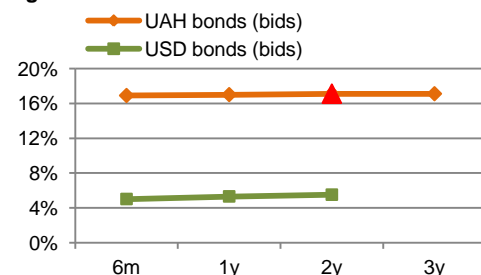
Source: Reuters, NBU, Ukrisibbank, Minfin

Figure 3. OVDP holders, UAH bn



Source: NBU

Figure 4. Local bonds market



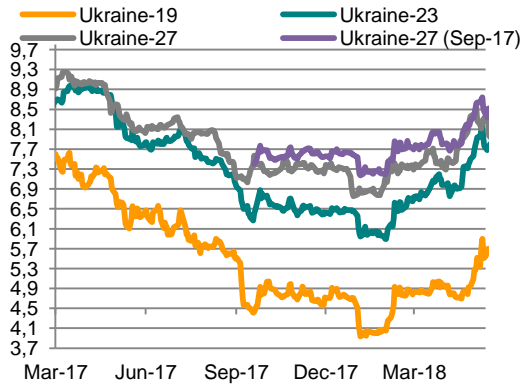
Source: Ukrisibbank



Global markets:

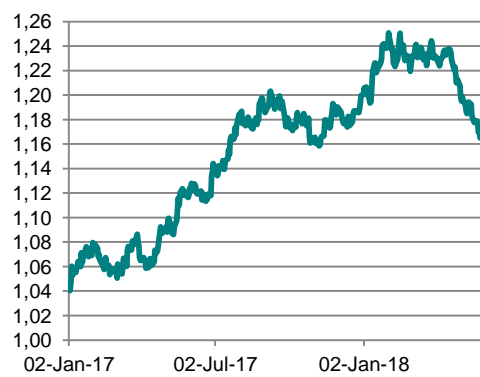
Fed minutes: no acceleration of rising interest rates

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



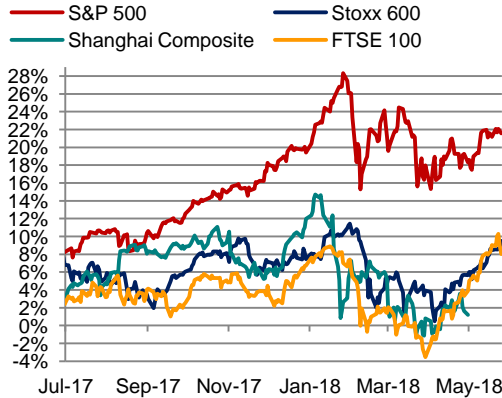
Source: Reuters

Figure 6. EUR USD spot (mid)



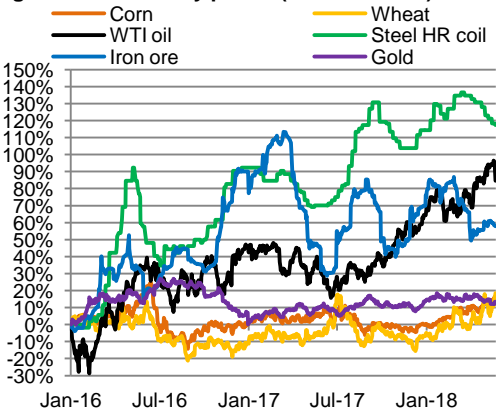
Source: Reuters

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



Source: Reuters

Figure 8. Commodity prices (Jan-2016=100)



Source: Reuters

Declining yields and growing stock market indices were the main theme of prior week, as minutes from May 2 Fed meeting, reaffirmed that the central bank will not be raising rates too aggressive. Meantime, U.S. Secretary Wilbur Ross will visit China next month for another round of talks between two countries.

Bond benchmarks increased, with U.S. 10y Treasuries' yield lower by 13bp week-on-week falling to 2.93%, while German 10y Bunds' yields decreased by 17bp, landing at 0.41%, Japanese 10y bonds yield's ended the week at 0.042. Yields declined after Fed minutes from May 2 meeting reaffirmed that the central bank will not be too aggressive with rising interest rates even amid the backdrop of inflation exceeding Fed target on a short term basis.

The U.S. stock markets were on the rise during the week, as S&P 500 increased week-on-week by 0.3%, while Nasdaq Composite gained by 1.1%. Some technological shares advanced much stronger comparing to other industries resulting in wide difference between two indexes. Meanwhile, flattening of the yield curve adds to the concern on the market.

The Fed policymakers gave no indication that they are likely to speed their pace of interest rate increases during the latest meeting. The key takeaway is that the Fed appears willing to slow the pace of rate hikes. At the same time, official's expressed optimism about prospects for growth and further employment gains this year. The Fed left its key rate unchanged at the May meeting. The Fed last raised its rates in March. At that meeting, officials indicated they expected to raise rates a total of three times this year, in line with hikes in 2017. The next FOMC meeting will take place on June 12-13.

EUR/USD rate landed at 1.165 as of Friday the 25th, lower than the last week closing level of 1.1775.

Stoxx 600, a broader gauge of European equity performance fell by 0.9%, while German Dax declined strongly by 1.1% during the week.

Turkey is in the midst of financial crisis. For month Erdogan pressed central bank not to raise interest rates in order to support the lira. The Turkish lira decline started with the strengthening of the U.S. dollar, which prompted investors to flee from emerging markets worldwide. While running one of the widest current account deficits in the world, staying at 6.5%, Turkey was especially vulnerable to headwinds from abroad. On May 23rd, the central bank delivered much needed rate increase (increasing its late liquidity window by 300 basis points to 16.5%), which fell short to save the national currency.

U.S. Commerce Secretary Wilbur Ross will visit China early next month for another round of talks amid ongoing trade frictions between the world's two largest economies. Ross is going to visit China from June 2 to June 4, according to media reports. In prior week trade dispute added complexity amid U.S. President Donald Trump announcing a national security investigation into imports of cars and trucks. According to Steven Mnuchin, Ross is aiming to negotiate a framework that could then turn into binding agreements.

Crude oil prices fell, as WTI futures declined by 4.8% week-on-week and closed at USD 67.9 per barrel, while Brent 1m futures decreased by 2.6% closing at USD 76.4 per barrel.

Gold prices gained, as NYMEX 1m futures rose by 1.0% week-on-week and finished the week at USD 1303.3 per troy ounce.

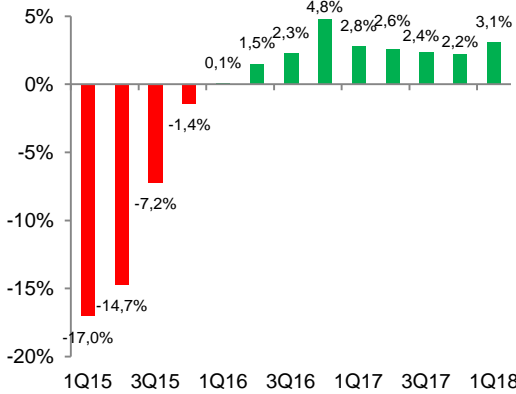
Grains increased, as CBOT Corn 1m futures rose 0.9% week-on-week and closed at USD 406.0 per bushel, while CBOT Wheat 1m futures landed at USD 543.0 per bushel, increasing by 4.8%.

Iron ore rose as NYMEX Iron ore 62% Fe 1m futures fell by 1.1% week-on-week and closed at USD 66.3 per ton.



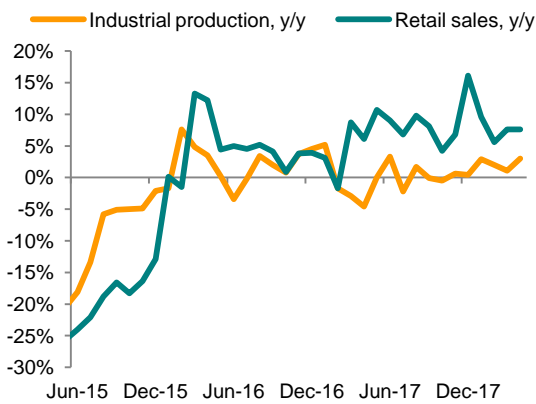
This week in focus: Economic growth is still strong

Figure 9. Ukraine's real GDP quarterly in 2015-2018, % y/y



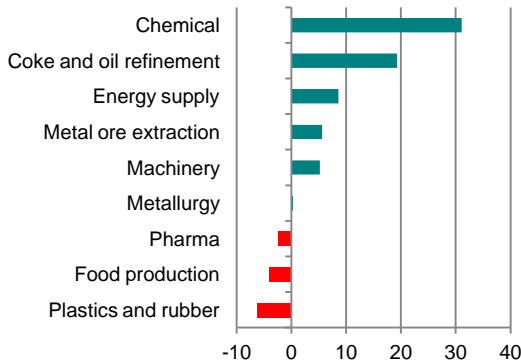
Source: Ukrstat

Figure 10. Industrial production and retail sales in 2015-2018, % y/y



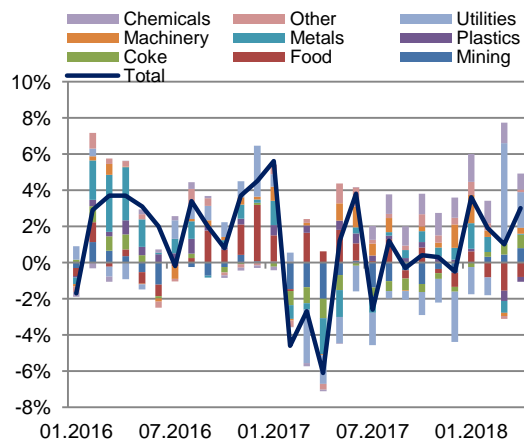
Source: Ukrstat

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



Source: Ukrstat

Figure 12. Ukraine's industrial production, %



Source: Ukrstat

In 4M2018, retail sales continued to post strong performance, increasing by 7.0% y/y. At the same time, in 4M 2018, industrial production growth was driven by utilities, followed by chemical production and other. It's noteworthy, that almost all major industries were growing. At the same time we expect these industries to pass a baton to food industry in securing higher IP growth very soon. We keep our IP and real GDP growth at 3.0% and 3.1% in 2018 unchanged.

According to Ukrstat's preliminary estimate real GDP managed to rise by 3.1% y/y in 1Q2018. Internal demand was pushing economy higher, with both retail and wholesale contributing the most to this performance. At the same time, industrial production added to growth positively too. We expect this trend to continue.

In 4M 2018, retail sales rose by 7.0% y/y, slightly down from 7.6% y/y for the 3M 2018. Having posted 7.6% y/y growth in March, retail sales delivered the same pace of expansion in April. Cabinet of Ministers, which initially expressed the possibility of a further increase in the minimum official wage in 2018, beyond the increase effective January 1st, 2018, said that there was no possibility to increase wages in 2018 to UAH 4200 for the second time during the year, according to Sergey Marchenko deputy finance minister. In particular, budget revenues fell short of the target by 3.1% in 1Q 2018, amounting to UAH 193.6bn. At the same time, government expenses were increased during the year due to higher interest rates in the country, as NBU tightened its monetary policy. All in all, internal consumption will remain high this year, amid growing real wages albeit much slowly comparing to 2017.

On Wednesday, Ukrstat revealed that industrial production growth gained healthier pace in April, reaching 3.0% y/y. The same reading adjusted for calendar day effect was in line with unadjusted or 3.0% y/y, as the number of working days was the same in both years. In prior month, even amid the backdrop of surging utilities' output, aggregate IP reading barely managed to grow, expanding by only 1.0% y/y. In 4M 2018, industrial output rose by 2.6% y/y, managing to outpace 2.4% y/y gains reached in 1Q 2018.

Growth in mining was picking up steam, increasing its pace of expansion as much as twice in April. Output in the subsector increased by 5.6% y/y in April, up from 2.3% y/y in prior month. The most prominent growth posted coal mining, increasing by 13.2% y/y. Moreover gaining traction in recent time iron ore production added to the good performance of mining subsector, expanding by solid 9.0% y/y. In contrast to flourishing foregoing sectors, oil and gas production were slightly in the red during the month, falling by 1.6% y/y in April.

Manufacturing subsector delivered lower growth in April, barely increasing by 0.8% y/y, while being partly weighted on by food output contraction.

Food production was getting hammered less in April comparing to March. The decline effectively halved during the month, amounting to 4.1% y/y, improving compared to 8.0% posted a month ago.

Having reached 55.9% growth in January, chemical production was in declining mode lasting 4 consecutive months in a row. At the same time, the paces of growth were much higher at this juncture than gains reported in other sectors. The gains amounted to 31.1% y/y in April, down from 39.4% in March. Increased oil prices which usually correspond with higher natural gas prices are providing to be major obstacles to a further upbeat performance of the chemical industry going forward.

Metals production was barely inching up in April. While in prior month the metallurgical sector delivered declining paces of growth, its performance changed to some degree better (limited degree better), increasing by 0.3% y/y in April. International prices declined in recent time, providing less solid ground to the industry, while remaining quite high for now.

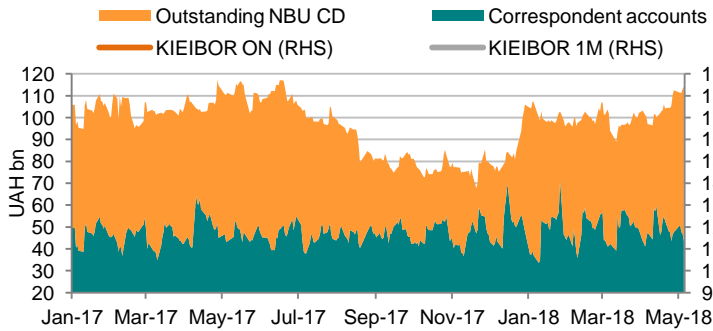
Utilities sector was the brightest spot in the last two months. While in March the strong gains were both due to effect of statistical base and abnormally cold weather in March, the increase in output in April were only by 8.6% y/y, following 20.1% y/y gains in prior month. At the same time, Ukrstat latest report indicated that machinery production delivered solid gains. It grew primarily due to auto industry increase in production by 26% y/y in April.

We expect a turnaround in food production in 2H2018 with new harvest coming. The latest data from Ministry of Agriculture suggested that winter crops are historically in the best shape, providing solid ground to agri sector in the second half of 2018. At the same time, wheat acreage (the king crop of winter crops) was increased in recent time, according to latest data to 6.5mn ha, from 6.4mn ha year ago.



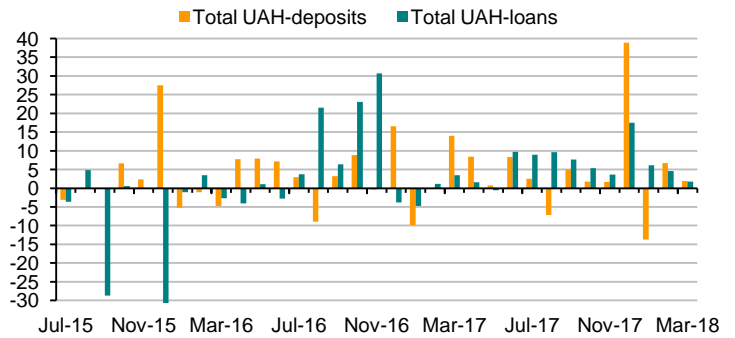
Money market

Banking liquidity vs. money market rates, %



Source: Reuters, NBU, UkrSibbank estimates

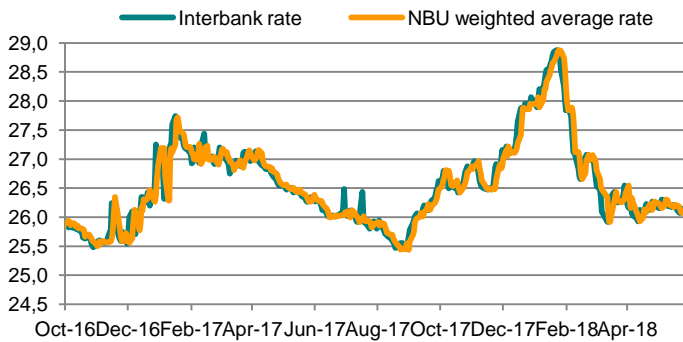
Monthly change in local currency loans and deposits, UAHbn



Source: the NBU

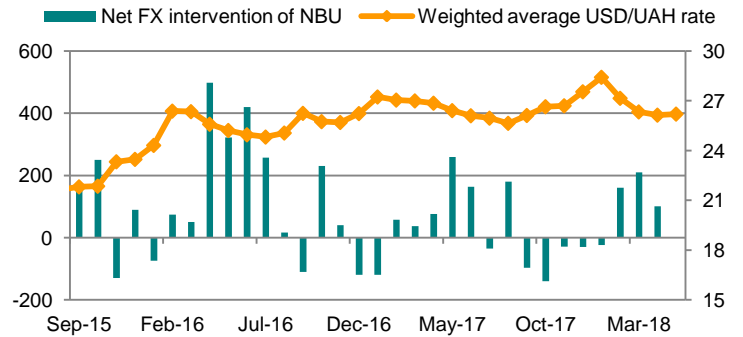
Currency market

UAH exchange rate, UAH/USD



Source: Reuters

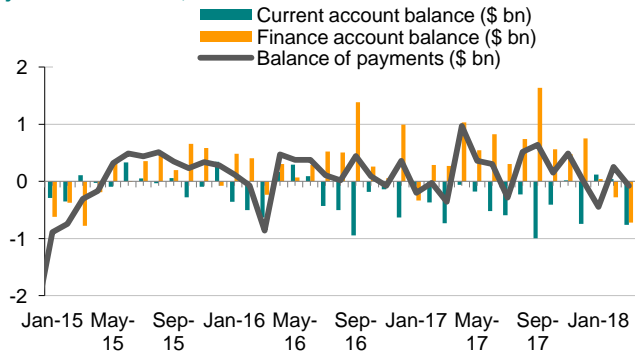
Net retail FX interventions of the NBU in 2015-2017, USDmn



Source: NBU

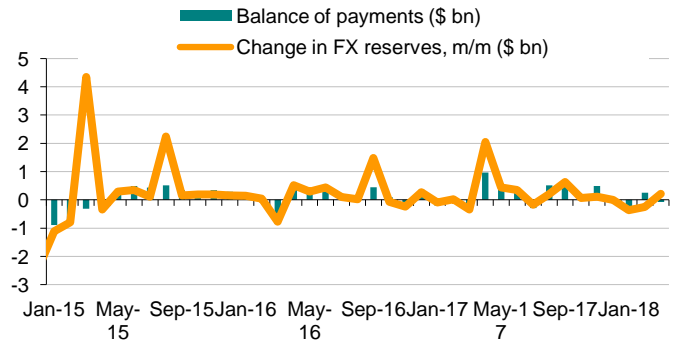
Balance of payments

Major BoP accounts, USDbn



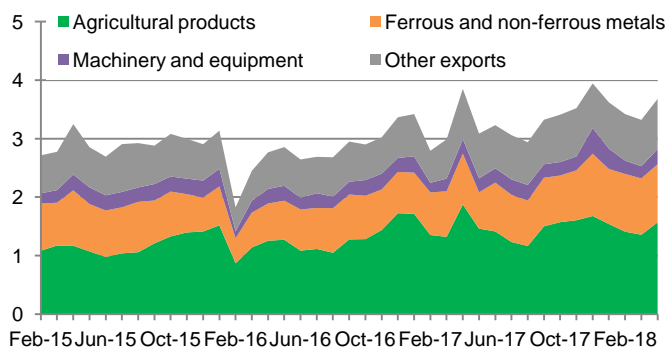
Source: NBU

BoP vs change in foreign reserves, USDbn



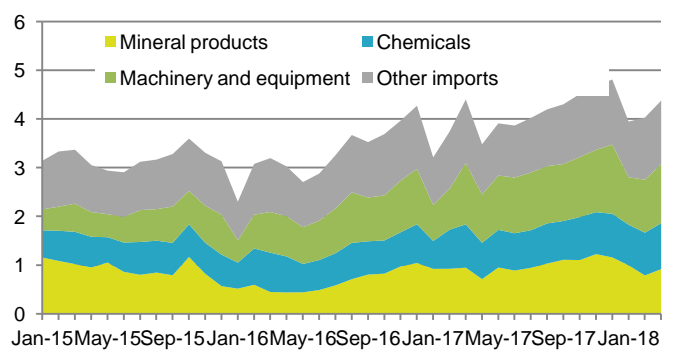
Source: NBU

Exports components dynamic, USDbn



Source: NBU

Imports components dynamic, USDbn



Source: NBU



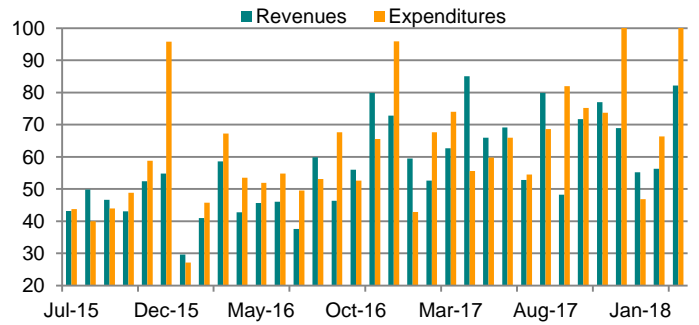
Budget performance

Budget performance, UAHbn

	Jan – Feb 2017	Jan - Feb 2018
Budget revenues	112,0	111,4
VAT proceeds	35,3	36,0
Corporate income tax	8,8	7,4
Budget expenditures	110,6	113,2
Deficit / Surplus	1,5	-1,8

Source: NBU

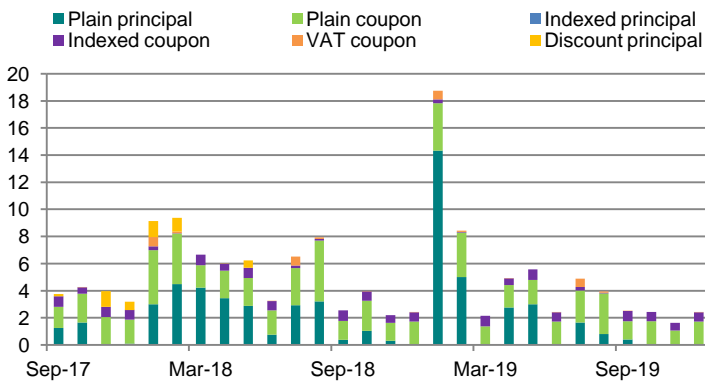
Monthly change in budget revenues and expenditures, UAHbn



Source: NBU, State Treasury

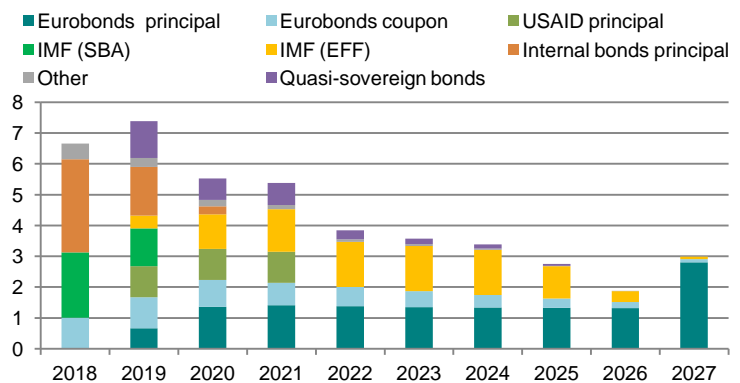
Sovereign debt

UAH- denominated debts' repayments schedule, UAHbn



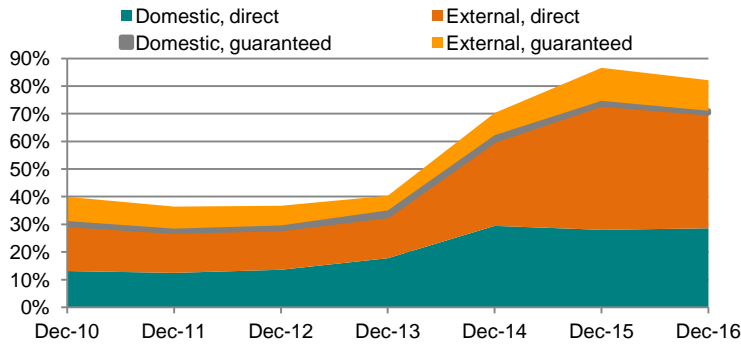
Source: NBU, UkrSibbank estimates

FX-denominated debt repayments schedule, USDbn



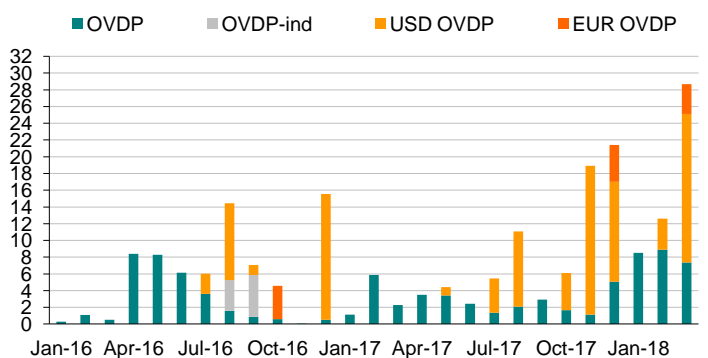
Source: Reuters, IMF, UkrSibbank estimates

Total government debt, % GDP



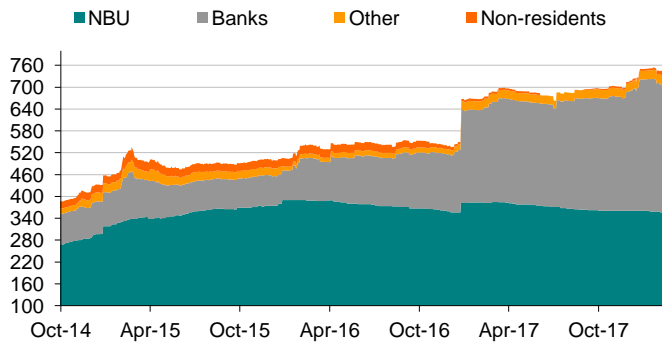
Source: MinFin

Local borrowings, UAHbn equivalent



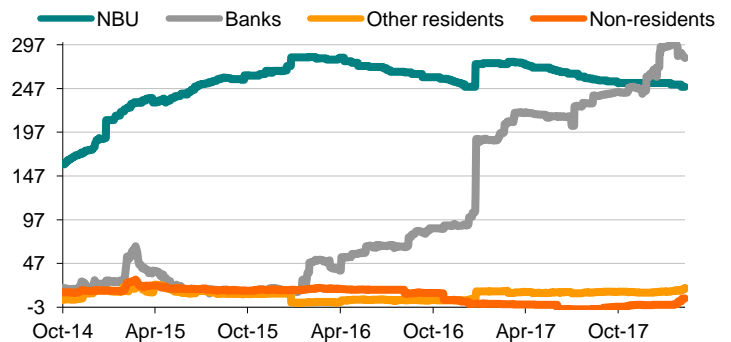
Source: NBU

Outstanding OVDP owners structure, UAHbn



Source: NBU

Outstanding OVDP changes in holding, UAHbn

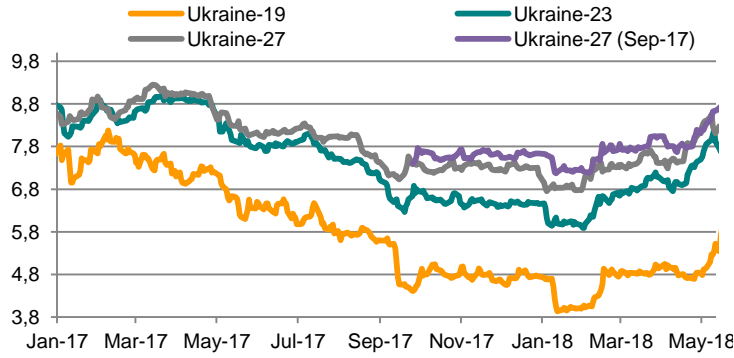


Source: NBU



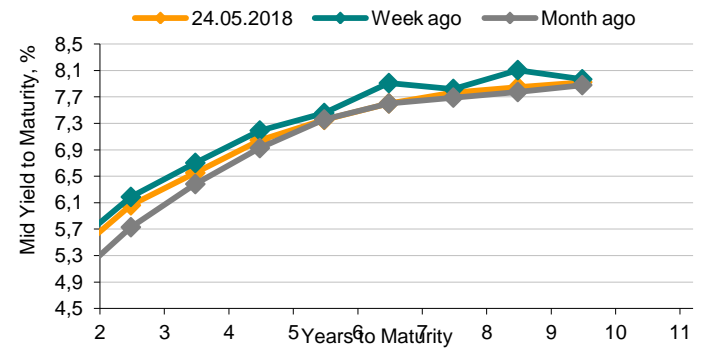
Eurobond market

Ukraine's sovereign Eurobond yields, %



Source: Reuters

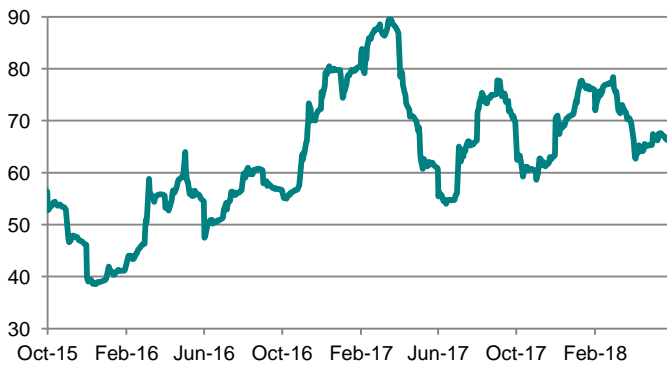
Ukraine's sovereign Eurobond yield curve



Source: Reuters

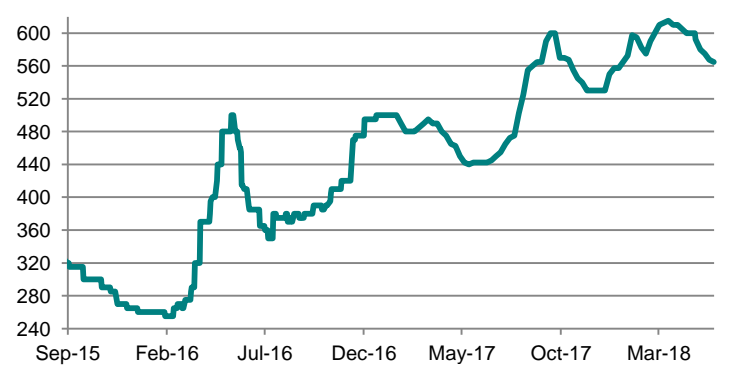
Commodity markets

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



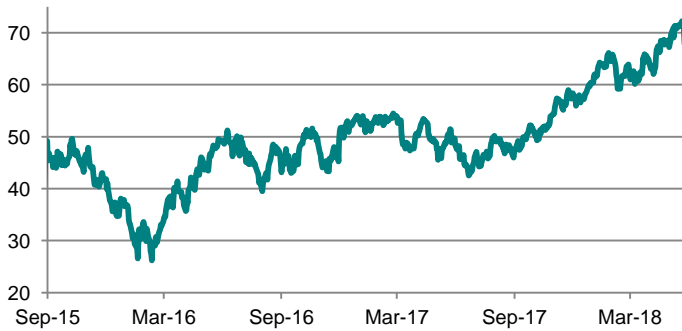
Source: Reuters

Steel CIS export HR coil, USD per ton



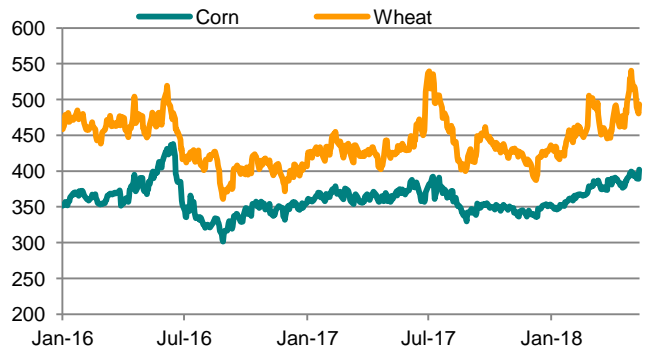
Source: Reuters

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	2017	2018F
Real sector											
Real GDP (%YoY)	2.3	-14.8	4.1	5.2	0.2	0.0	-6.6	-9.8	2.3	2.5	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	2982.9	3239.8
Nominal GDP (USD bn)	178.9	112.8	136.1	163.1	175.8	183.5	133.7	91.2	93.1	112.1	120.0
Prices											
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
Fiscal balance (% of GDP)											
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	71.8	70.0
External balance											
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	-3.3
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	-2.8
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
Interest and exchange rates											
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	17.00*
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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