



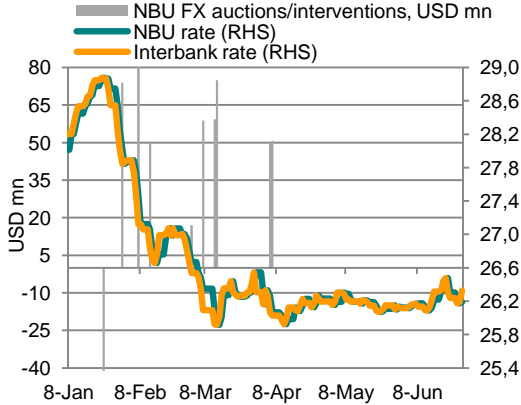
This week in focus: Worsening trade weighs on C/A

Ukraine's current account was reported in slight deficit USD 41mn, reversing marginally from USD 23mn of surplus a year ago. We retain moderate pessimistic view on UAH through year end.

Please see page 3 for more details

FX and interest rates: VAT refund slightly pushed hryvnia lower

Figure 1. UAH exchange rate (UAH per USD)



Source: NBU, Reuters

USD/UAH closed at 26.33 as of Wednesday the 27th, higher compared to a previous week. Hryvnia slightly fell in value during the week, provided large concentration of VAT reimbursements by the state treasury during the week.

Average daily FX volumes on the market amounted to the equivalent of USD 260.6mn, up by USD 61.8mn week-on-week.

NBU managed to increase international reserves via interventions on the market only by USD 1.5mn on a net basis during shortened week ending June 27th. As opposed to a week ago, central bank resorted to only one tool, namely matching, avoiding using others. In particular, NBU bought USD 10mn, and sold simultaneously USD 8.5mn, increasing reserves by a mere USD 1.5mn during the week. As a result, YTD reading of cumulative purchased currency on the market were not changed materially, remaining at USD 1.3bn, as of week ending June 27th.

Aggregate banking liquidity amounted to UAH 113.8bn as of Wednesday the 27th. While amount of VAT refund cumulatively for June was only UAH 3.1bn, as of week ending June 22nd, state treasury reimbursed UAH 5.4bn during the two days of week ending June 27th (we do not see the amount of reimbursement effective on Wednesday as of today). As we pointed out in the previous report (please see Weekly effective June 25th), tight refund could accelerate in the end of the month, bringing hryvnia under pressure on the short term basis. At the same time, state treasury said that the amount of residuals on treasury account fell by 18.3% during the month to UAH 9.4bn, as of July 1st.

Money market rates remained flat: cost of ON funds is around 14.0/16.00, 1 week is 14.5/16.50 while 1M is 15.00/17.50, according to our calculations.

On June 26th, the shortest type of the bonds took the top spot by demand as well as by placement size, attracting to the budget amount of proceeds close to UAH 1bn. While primary dealers initially applied for 3 bids, only 2 of them were satisfied by the MoF. As a result, MoF managed to reduce the cut off rate on the shortest bonds to 17.35% on the latest placement. Moreover, MoF issued bonds with much longer maturity close to 3 year. While primary dealers applied for around UAH 51mn in demand for those bonds, only UAH 1mn were satisfied by the Ministry of Finance. In July, MoF is to offer also two USD denominated bonds on July 10th offering maturity around 2y and July 24th with a maturity 1.5y, according to the latest schedule of placements effective on 3rd quarter. Moreover, in August and September MoF is going to offer only one USD denominated issues in both months.

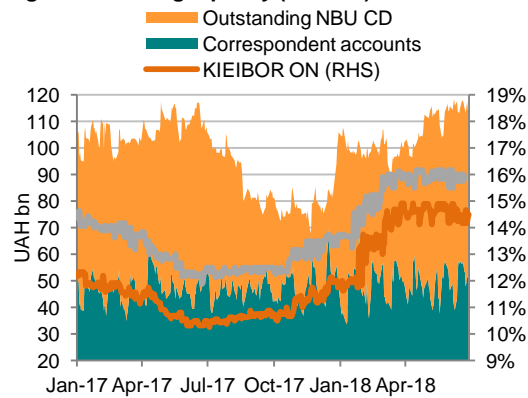
Currently, yields (bids) of local OVDP in UAH at 17.75% (for 6m), 17.70% (for 2Y). 1Y USD bids were at 5.35%, while bids for VAT bonds were at 17.95%.

Figure 5. OVDP auction combined results, 26th of June 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 | 17.35% | 17.35% | 17.40% | 17.35% | 3 | 2 | 1.0bn | 0.96bn |
| UAH | 3y | 15.00% | 15.00% | 16.45% | 15.00% | 2 | 1 | 51.0mn | 1.0mn |
| UAH | 7m | - | - | - | - | 2 | 0 | 9.3mn | 0mn |
| UAH | 12m | - | - | - | - | 0 | 0 | 0mn | 0.0mn |
| UAH | 1y | - | - | 16.35% | 16.35% | 3 | 0 | 56.1mn | 0.0mn |

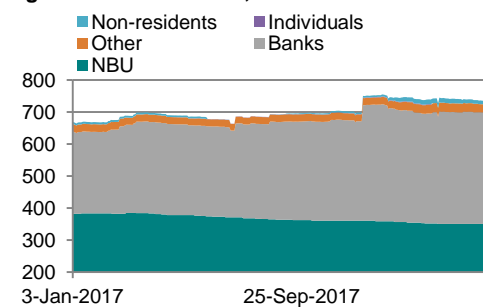
In May, nominal wages in the country rose by 27.6% y/y, remaining almost in line with 27.3% y/y increase reported a month ago. At the same time, the same measure adjusted for inflation indicated acceleration with growth amounting to 14.1% y/y in May, exceeding prior month 12.5% y/y gains. On a y/y basis the largest gains among sectors (belonged to private sector) were reported in transportation (30.6% y/y), agriculture (+27.2% y/y), industry (28.8% y/y). Meantime, among sectors included in the government orbit the defence sector outperformed by far the most, with average growth in wages reaching 47.5% y/y in May.

Figure 2. Banking liquidity (UAH bn)



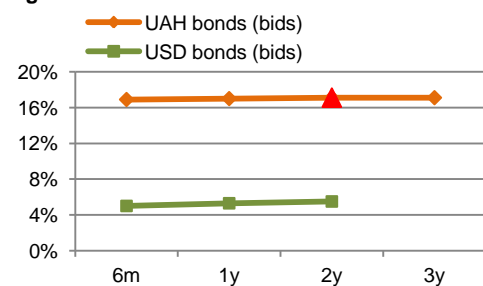
Source: Reuters, NBU, UkrSibbank, Minfin

Figure 3. OVDP holders, UAH bn



Source: NBU

Figure 4. Local bonds market



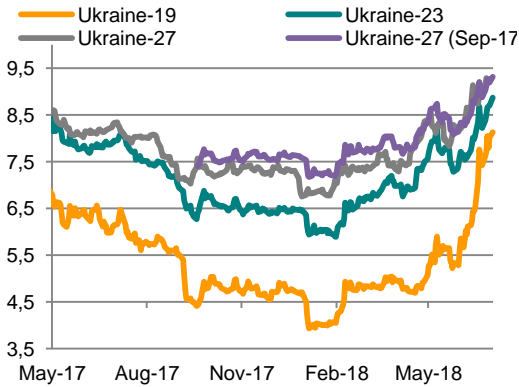
Source: UkrSibbank



Global markets:

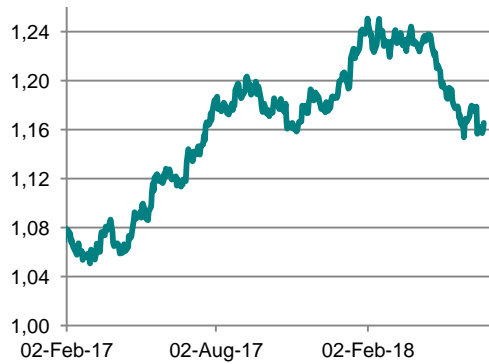
U.S. PMI showed weaker performance in June

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



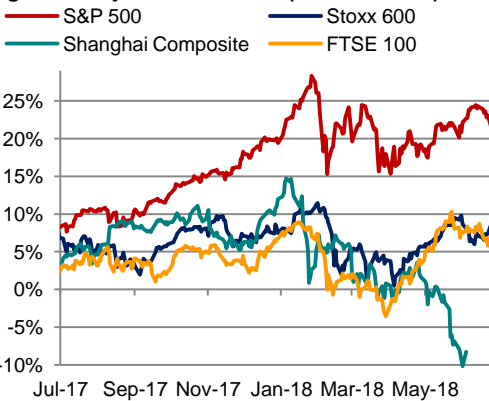
Source: Reuters

Figure 6. EUR USD spot (mid)



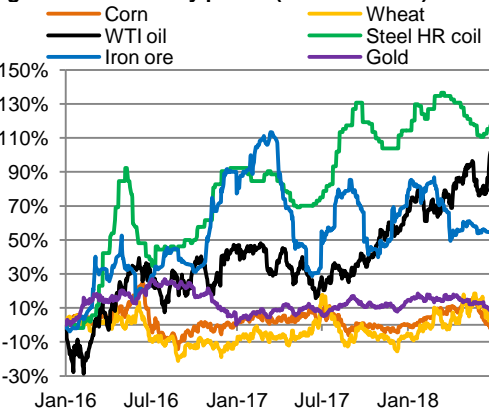
Source: Reuters

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



Source: Reuters

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



Source: Reuters

In U.S. purchasing manager index in June displayed that exports orders fell in recent time, suggesting that the trade war is clearly impacting economy in the real time. Meantime, euro zone manufacturing PMI slowed to 18-month low, signaling a weakening in the pace of expansion in each month since the start of the year.

Bond benchmarks rose, with U.S. 10y Treasuries' yield lower by 5bp week-on-week landing at 2.9%, while German 10y Bunds' yields fell by 3bp, landing at 0.31%, Japanese 10y bonds yield's ended the week at 0.031.

It's interesting that during the first half of the year **S&P barely managed to grow, increasing by symbolic 1.7% on the back of fears of potential trade war**. At the same time, Nasdaq Composite managed to rise by 8.8% in the first half of 2018, proving to be more immune to the headwinds stemming from U.S. trade rhetoric and rising borrowing costs. At the same time, the most recent wave of trade controversy also weighed on tech sector too. During the last week of 1H 2018, S&P fell by 1.3%, while Nasdaq Composite by more meaningful 2.4%. At the same time, corporate profits in the United States at the highest level in 2018, albeit partly due to the effect of tax reform.

According to latest data, purchasing manager index (or PMI) in June, which was released on Saturday, showed that exports orders fell in recent time, suggesting that the trade war is clearly impacting economy in the real time. Meantime, China and United States are set to begin charging higher tariffs as soon as of Friday this week, highlighting a culmination in the ongoing trade war by far. In contrast to that in previous months companies hastened its export orders because they anticipated such situation with trade. The manufacturing PMI landed at 51.5 in June, versus 51.9 in May. At the same time, non-manufacturing PMI rose to 55, up from 54.9 in May.

EUR/USD rate landed at 1.1683 as of Wednesday the 27th, slightly up compared to last week closing level of 1.1655.

Stoxx 600, a broader gauge of European equity performance fell by 2.4% during the first half of the year, indicating much weaker performance of the European stock comparing to the U.S. While euro fell in the 1H 2018, at the same time it increased on a twelve month basis, curbing to some extent advances in the index, provided that around half of the European companies get sales abroad. At the same time, stocks in Europe could outperform if the ECB strikes more dovish tone, weakening the euro further. Moreover, U.S. stock market was led by far the upheaval of tech sector, which accounts around 25% of the index, comparing to only 4.5% in Europe. On top of that, U.K. exit from EU also restrained equities in the EU, as a lot of uncertainties loomed on that path.

In June, Euro zone manufacturing PMI slowed to 18-month low, landing at 54.9 in June, down from 55.5 a month ago. At the same time, the gauge was signaling a weakening in the pace of expansion in each month since the start of the year, according to survey showed on Monday. Moreover, with ongoing trade war the risks tilted toward output growth fading further in months to come. Separate reading also showed that unemployment in the euro zone was unchanged in May. The rate of unemployment was stable at 8.4% in May, while the number of job seekers decreased comparing to April to 13.7mn

On July 6th is a deadline when the United States is set to impose tariffs on USD 34bn worth of goods from China. At the same time, Beijing is expected to respond with tariffs of its own on U.S. goods at the trade fight between two largest economies threatening to damage global trade flows. On top of that, expectations for the country's economic growth worsened meaningfully, with anticipation that risk stemming from abroad increase in the second half of the year. Meantime, in June was the sharpest drop in the Chinese stock in more than two years, accompanied with a yuan's biggest monthly fall on record.

Crude oil prices gained, as WTI futures rose by 8.1% week-on-week and closed at USD 74.2 per barrel, while Brent 1m futures increased by 5.1%

Gold prices were lower, as NYMEX 1m futures tumbled by 1.3% week-on-week and finished the week at USD 1251.3 per troy ounce.

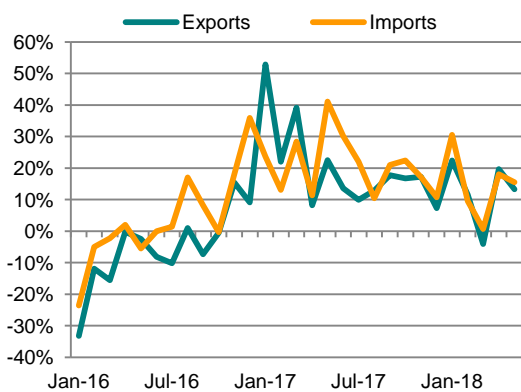
Grains were mixed, as CBOT Corn 1m futures fell 2.0% week-on-week and closed at USD 350.3 per bushel, while CBOT Wheat 1m futures landed at USD 497.5 per bushel, increasing by 1.3%.

Iron ore was flat as Iron ore 62% Fe 1m futures were flat week-on-week.



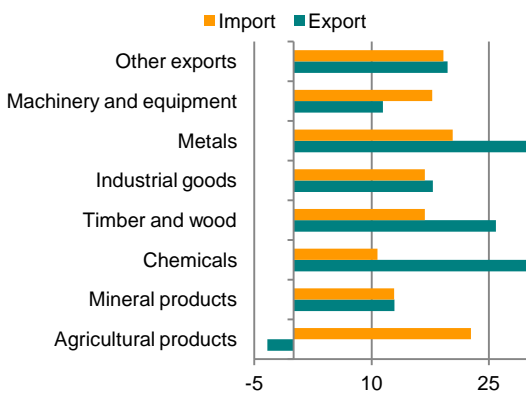
This week in focus: Worsening trade weights on C/A

Figure 9. Exports and imports change, %



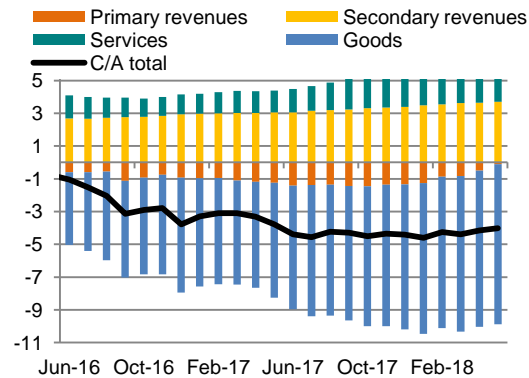
Source: NBU

Figure 10. Exports and imports main components change, %



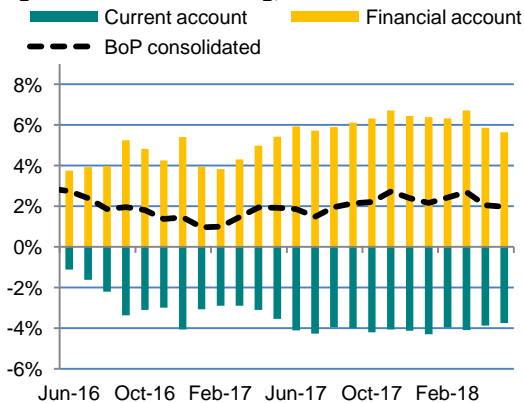
Source: NBU

Figure 11. C/A 12m rolling, USDbn



Source: NBU

Figure 11. BoP 12m rolling, % from GDP



Source: NBU

Ukraine's current account was reported in the slight deficit of about USD 41mn, reversing marginally from USD 23mn of the surplus a year ago. We retain moderate pessimistic view on UAH through year end.

Total exports amounted to USD 3.6bn, growing by 13.2% y/y in May. At the same time, exports amounted to USD 15.9bn, increasing by 26.8% in 5M 2018.

Agricultural and food export fell by 3.3% y/y in May, following 8.1% increase in April. As a result, USD proceeds to the country were reduced to USD 1.4bn. In 5M 2018, Ukraine's farmers exported 5.1mn t of wheat, down by 4.4% y/y and 10.7mn t of corn, down by 9.7% y/y in 5M 2018. Meantime, higher prices by roughly 9% and 5%, respectively brought export revenue by around 5% less in corn, while the revenue from wheat managed to stay higher compared to a year ago by 5% y/y in 5M 2018.

Metallurgical exports pared its gains to 30.2% y/y increase from 65.8% y/y advance reported a month ago. The exports of semi-finished products increased by 4.2% y/y for 5M 2018, while a rise in average selling price by 24.8% allowed to report 30% y/y gains in exports revenue. Moreover, the gains in physical volume of sold HRC amounted to 5.7% y/y, while the strong gain in prices resulted in 24.5% y/y increase in export revenue (in 5M 2018). At the same time, Ukraine exported by 4.4% more cold rolled steel, as measured by tonnage, which coupled with higher prices resulted in 12.3% increase in exports revenue. Meantime, Ukraine almost doubled the amount of pig iron exported to other countries. In particular, metallurgical companies increased sales of pig iron by around 84% YTD in 5M 2018, following 88% YTD in 4M 2018, slightly slowing on that path. In line with preceding month, growing prices were more important factor in determining the exports revenue performance.

It's relevant to note, that the pig iron performance was the only major component of Ukraine's steel exports, which showed quite different drivers of upswing. While in almost all other cases, higher exports proceeds in USD was driven by higher prices and to a lower extent higher volume. The case involving pig iron was the only major component of steel export which showed reverse performance. In particular, gains as measured by physical volume (around 84%) by far outstripped gains from increased prices (around 13%), bringing amount of proceeds in USD by 108% higher in 5M 2018.

Total imports amounted to USD 4.6bn in May, up by 15.5% y/y. The energetic imports advanced by 12.4%, while non-energetic rose by 16.5%. Imports of gas decreased meaningfully by 37% in 5M 2018. At the same time, in prior month the same gas imports bill cutting accounted for 49% y/y of drop in 4M 2018. Meantime, higher prices by about 15% y/y resulted in lower reduction of imports as measured in USD terms. Despite falling international prices (with prices on average falling by 16% y/y in 5M 2018), Ukraine kept ramping up its imports of coal. While in 4M 2018 in physical volume import increased by around 30%, in 5M 2018 imports advanced by 43% y/y. As a result, bringing bill in USD terms by 21% higher compared to a year ago.

Machinery imports rose by 17.8% y/y in May, decelerating from 21.6% y/y in prior year. While in 4M 2018 import rose by 32% as measured by tonnage, in 5M 2018 the same reading landed at 30% y/y growth. At the same time it continues to be driven by strong consumer demand in the country.

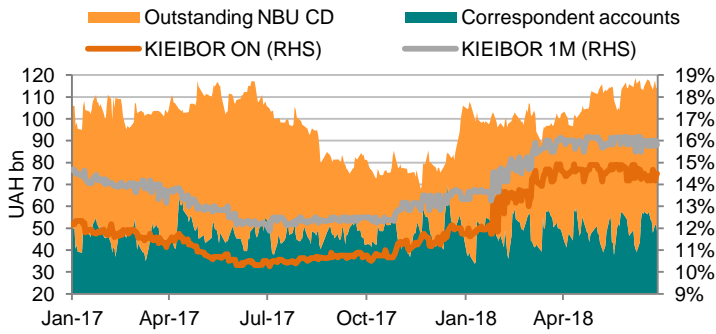
Financial account surplus amounted to USD 307mn in May, up compared to a month and slightly down compared to a year ago. FDI amounted USD 150mn, with major part allocated to the banking system in contrast to the previous month allocation concentrated in real sector.

Combined BoP was in surplus by USD 266mn vs USD 357mn of surplus a year ago. Moreover, international reserves comprised USD 18.2bn, covering 3.2 months of future imports. Ukraine also paid USD 0.4bn to the IMF in May, which contributed to NBU reserves reduction during the month. At the same time, the latest payment brought YTD reading at USD 0.9bn, as of May.



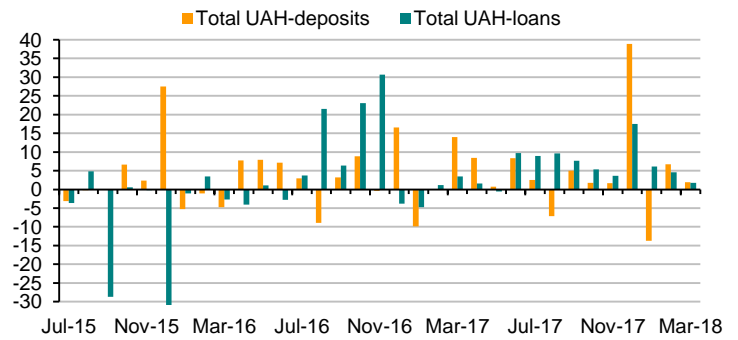
Money market

Banking liquidity vs. money market rates, %



Source: Reuters, NBU, UkrSibbank estimates

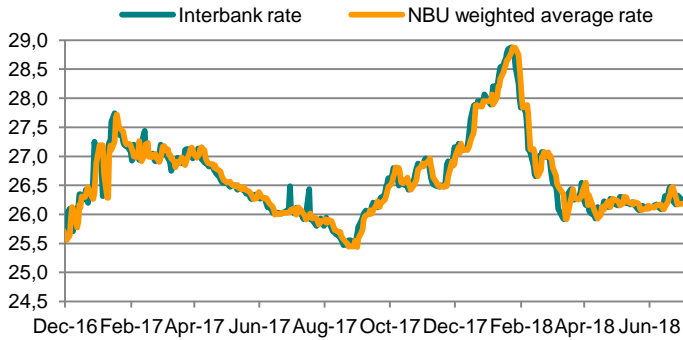
Monthly change in local currency loans and deposits, UAHbn



Source: the NBU

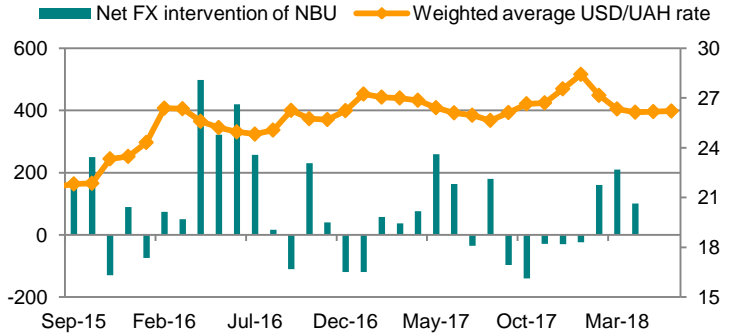
Currency market

UAH exchange rate, UAH/USD



Source: Reuters

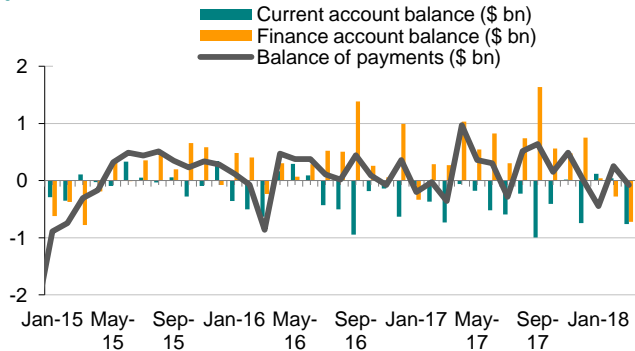
Net retail FX interventions of the NBU in 2015-2017, USDmn



Source: NBU

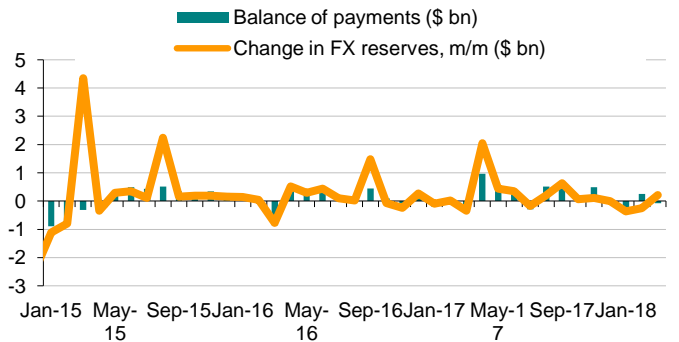
Balance of payments

Major BoP accounts, USDbn



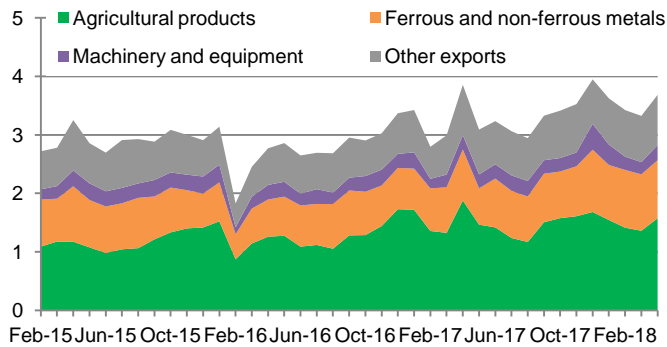
Source: NBU

BoP vs change in foreign reserves, USDbn



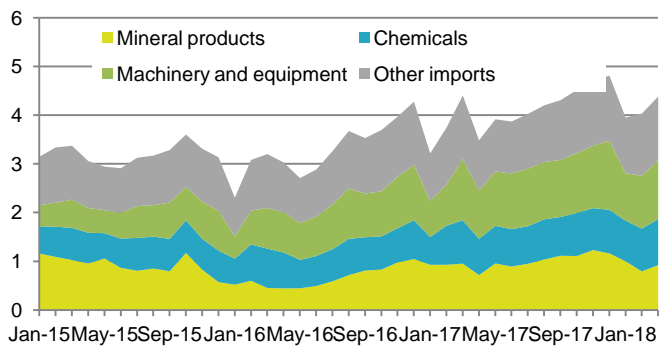
Source: NBU

Exports components dynamic, USDbn



Source: NBU

Imports components dynamic, USDbn



Source: NBU



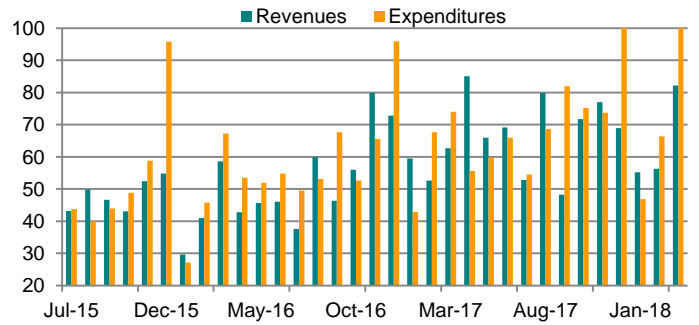
Budget performance

Budget performance, UAHbn

| | Jan – Apr 2017 | Jan - Apr 2018 |
|----------------------------|----------------|----------------|
| Budget revenues | 259,8 | 272,8 |
| VAT proceeds | 140,6 | 77,5 |
| Corporate income tax | 14,1 | 30,0 |
| Budget expenditures | 240,2 | 293,4 |
| Deficit / Surplus | 19,5 | -20,6 |

Source: NBU

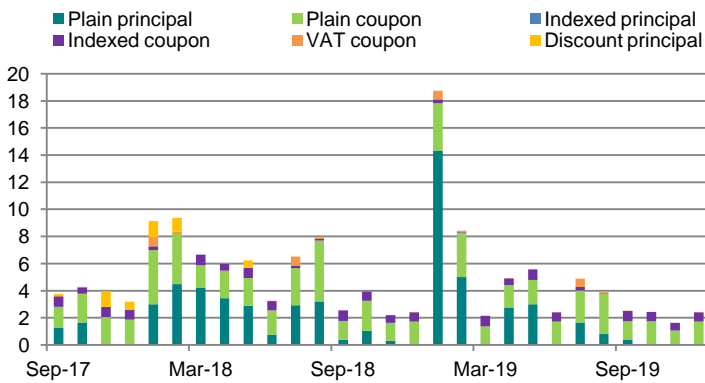
Monthly change in budget revenues and expenditures, UAHbn



Source: NBU, State Treasury

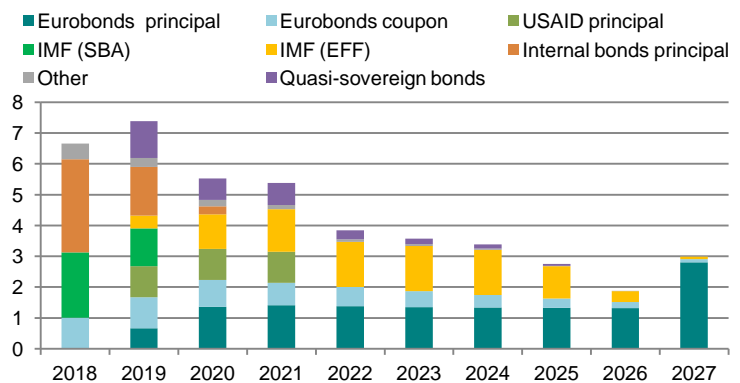
Sovereign debt

UAH- denominated debts' repayments schedule, UAHbn



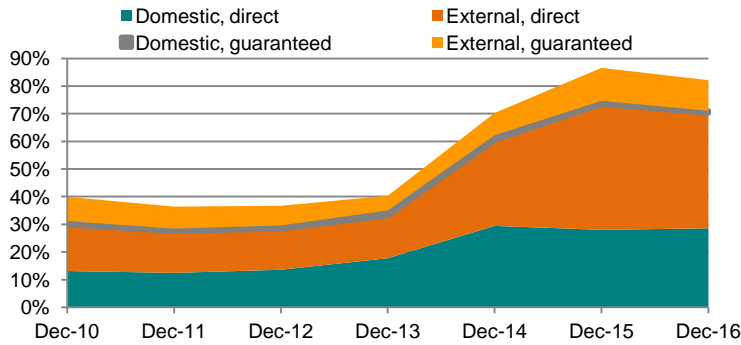
Source: NBU, UkrSibbank estimates

FX-denominated debt repayments schedule, USDbn



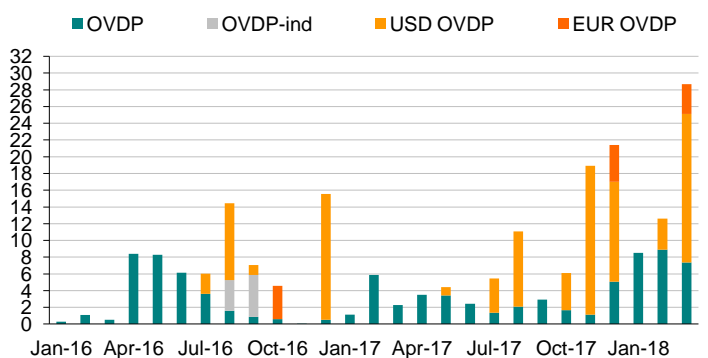
Source: Reuters, IMF, UkrSibbank estimates

Total government debt, % GDP



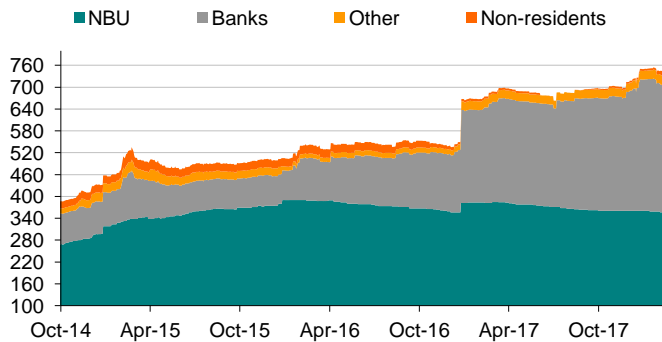
Source: MinFin

Local borrowings, UAHbn equivalent



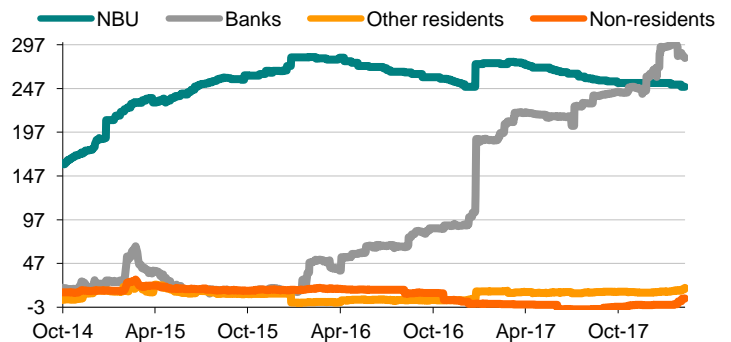
Source: NBU

Outstanding OVDP owners structure, UAHbn



Source: NBU

Outstanding OVDP changes in holding, UAHbn

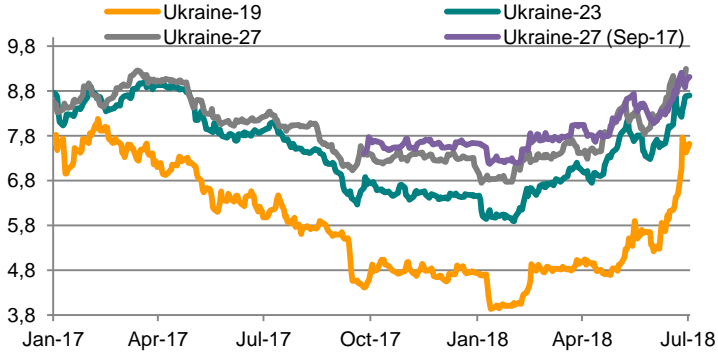


Source: NBU



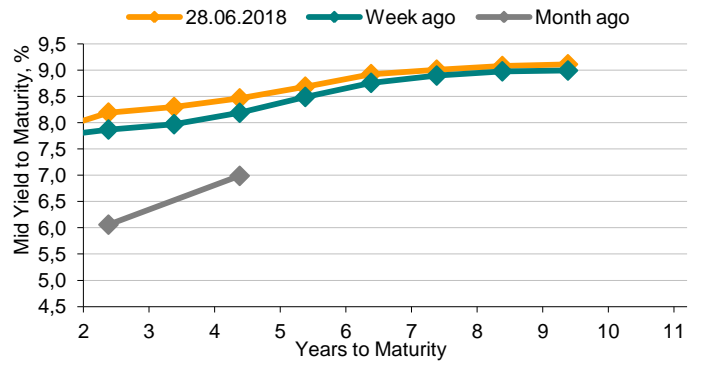
Eurobond market

Ukraine's sovereign Eurobond yields, %



Source: Reuters

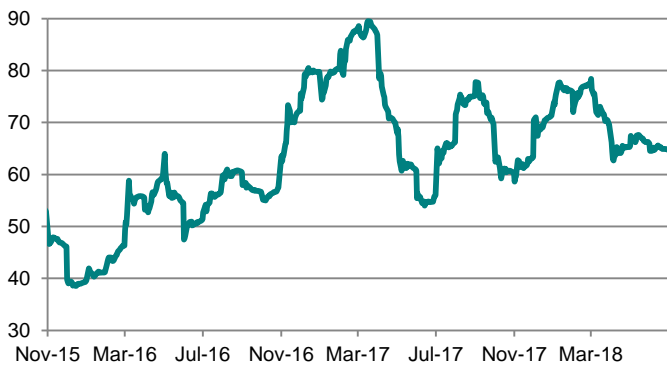
Ukraine's sovereign Eurobond yield curve



Source: Reuters

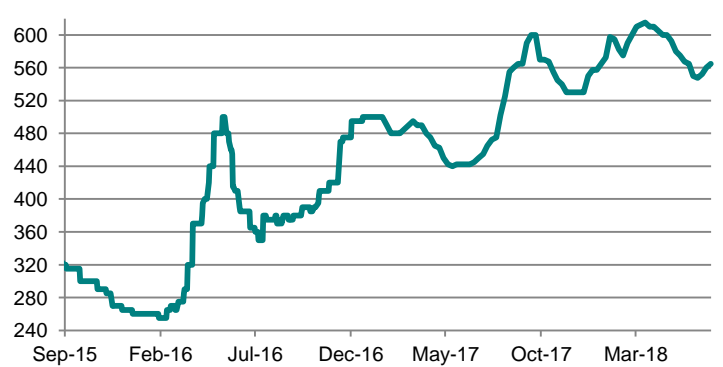
Commodity markets

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



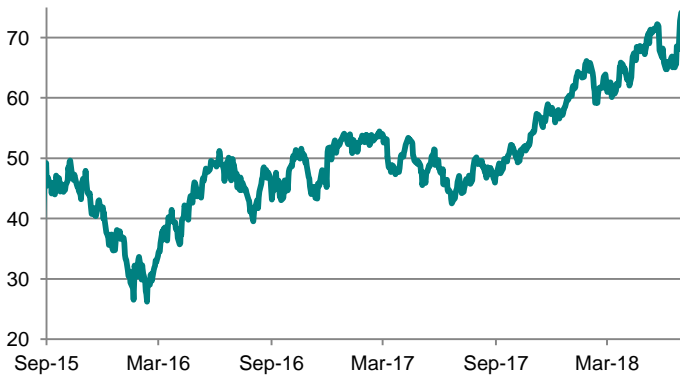
Source: Reuters

Steel CIS export HR coil, USD per ton



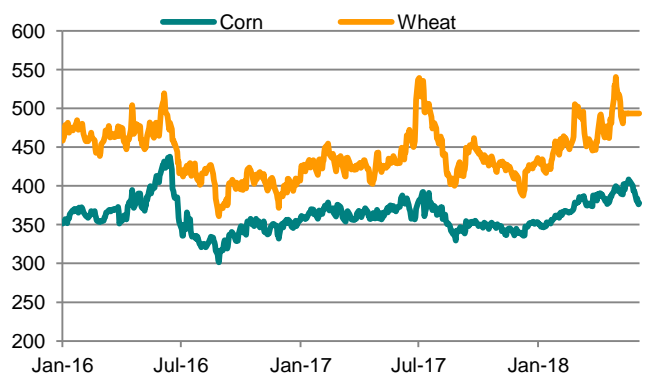
Source: Reuters

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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