



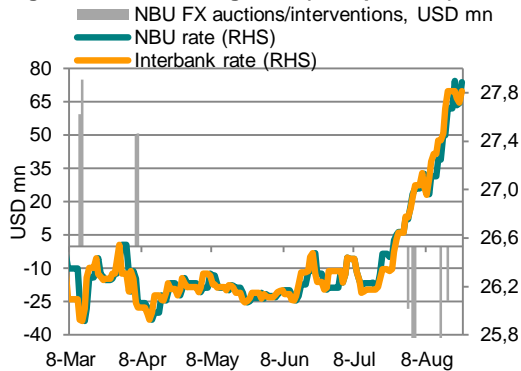
This week in focus: Ukraine main economic indicators hold gains in July

Ukraine's economy expanded by 3.6% y/y in 2Q18, according to Ukrstat preliminary reading or 0.9% seasonally adjusted on quarter over quarter basis. Internal demand and investment activity both were the main drivers of growth. At the same time, Ukraine started 3Q and 2H18 with a robust print in industrial production stemming from good performance of metal production rather than chemical and utility contribution.

Please see page 3 for more details

FX and interest rates: NBU broke a four weeks string of selling FX from reserves

Figure 1. UAH exchange rate (UAH per USD)



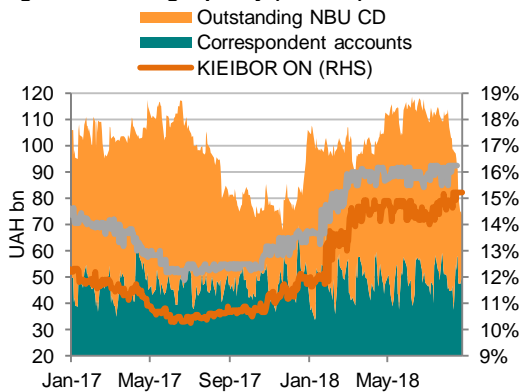
Source: NBU, Reuters

USD/UAH was at 27.89 as of Thursday the 23rd, as hryvnia fell by 0.8% on a week-on-week basis.

Average daily FX volumes on the market amounted to the equivalent of USD 229.2mn, down by USD 81.9mn week-on-week, provided there were less working days during the weekdays.

NBU refrained from conducting interventions through currency auctions, as of week ending August 23rd, following USD 91.4mn of sold FX in prior week. During the week NBU sold USD 10mn and bought USD 16.7mn, resulting in USD 6.7mn of bought currency to reserves on a net basis. The latest week ended the string of four consecutive weeks when NBU was selling USD on the market to support national currency weakening. As a result of that NBU sold USD 646.6mn of hard currency from reserves during this period of four weeks. Moreover, YTD reading of central bank interventions remained at USD 0.7bn of bought FX currency in 2018, as of August 23rd.

Figure 2. Banking liquidity (UAH bn)



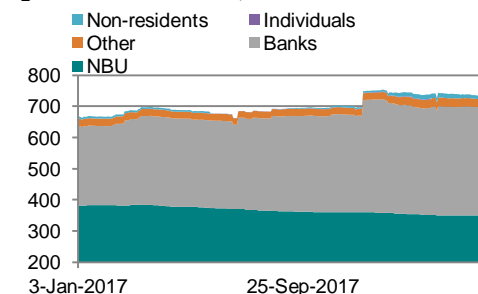
Source: Reuters, NBU, UkrSibbank, Minfin

Aggregate banking liquidity amounted to UAH 76.7bn as of Thursday the 23rd, down by UAH3.3bn during the week, following UAH 17.0bn fall a week ago. As of the end of August 23rd, State treasury reimbursed UAH 7.5bn of VAT cumulatively during the month, leaving some amount to be reimbursed in the last week of August.

Money market rates remained flat: cost of ON funds is around 16.00/16.50, 1 week is 16.25/16.75 while 1M is 17.00/18.00, according to our calculations.

Having conducted two primary auctions before, **MoF returned to the mode of only one auction during the week for the second week in a row**. This time MoF offered four bonds issues denominated in UAH, USD and EUR. The largest amount of proceeds to the state government injected bonds denominated USD or roughly 99%, which were placed at the same cut off rate at 5.95% as previously. At the same time, MoF refrained from placing EUR denominated bonds, as the volume of bid was much lower this time. Even though government wasn't placed a limit on the shortest UAH issue the amount of demand was very low. Moreover, MoF effectively satisfied all demand on UAH bonds. Aggregate proceeds from the auction amounted to UAH 2.4bn.

Figure 3. OVDP holders, UAH bn



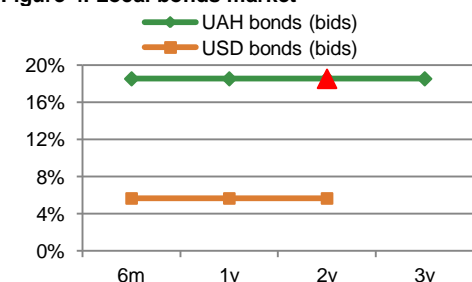
Source: NBU

Currently, yields (bids) of local OVDP in UAH at 19.50% (for 6m), 19.50% (for 2Y). 1Y USD bids were at 5.75%, while bids for VAT bonds were at 19.50%.

Figure 5. OVDP auction combined results, 21st of August 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	18.00%	18.00%	18.00%	18.00%	5	5	26.8mn	25.3mn
UAH	12m	17.90%	17.90%	17.90%	17.90%	1	1	2.4mn	2.1mn
USD	6m	5.95%	5.95%	5.95%	5.85%	13	13	88.0mn	85.4mn
EUR	6m			4.70%	4.70%	4	0	4.0mn	

Figure 4. Local bonds market



Source: UkrSibbank

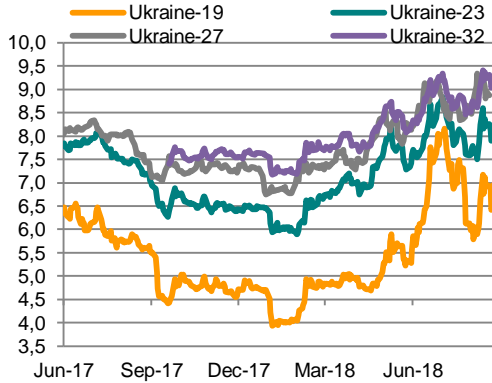
Ukraine's Finance Minister Oksana Markarova said that government revaluated midterm strategy regarding management of state debt. As a consequence, Ukraine will aim to reach 60% ratio of state debt to GDP by the end of that year, following by 52% in 2019 and 49% in 2020. In contrast to that, previous target for 2018 aimed state debt to GDP ratio at 62%, while in 2019 the ratio declined to 58%. In prior year, the share of Ukraine's state debt to GDP fell to 71.8% from 81.0% in prior year. **We welcome this government move, as it theoretically could prevent excessive public spending in the future.**



Global markets:

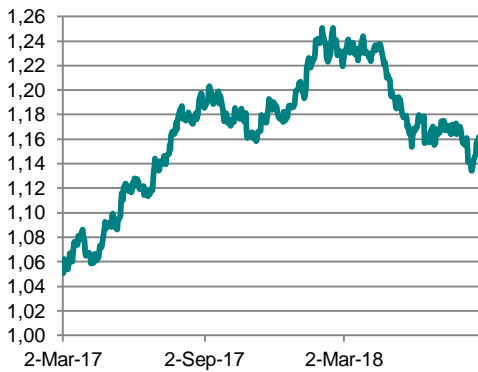
Fed remains on track to gradually increase interest rates

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



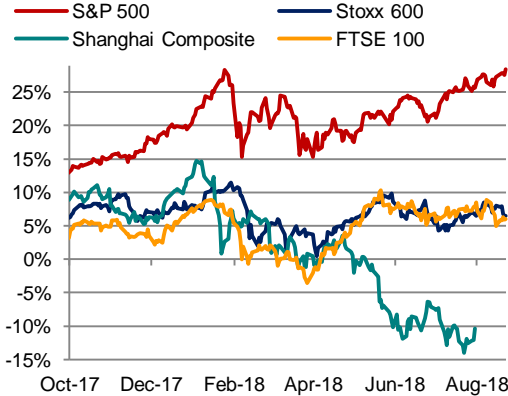
Source: Reuters

Figure 6. EUR USD spot (mid)



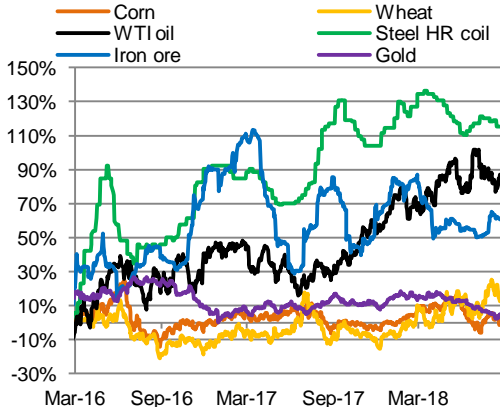
Source: Reuters

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



Source: Reuters

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



Source: Reuters

Remarks of Fed chair Jerome Powell at conference in Wyoming indicated that the gradual increase in interest rates remains on the agenda of policymakers in the nearest future, sending major global equity markets higher at the same time. Meantime, German economy minister expressed support for Turkey amid the backdrop of market turbulence after U.S. imposed tariffs.

Bond benchmarks were mixed, with U.S. 10y Treasuries' yield fell by 5bp week-on-week landing at 2.85%, while German 10y Bunds' yields declined by 4bp or slightly less than U.S. peers, landing at 0.34%, Japanese 10y bonds yield's ended the week at 0.10, slightly higher compared to the previous week.

Major US stock indices were broadly on the rise during the week, as S&P rose by 0.9%, while Nasdaq Composite gained by 1.7% week-on-week. More than a half of all gains during the week were concentrated during one single day, namely Friday. At the same time, gains on Friday stemmed mainly from Fed chair Jerome Powell, mentioning during the central bankers conference in Wyoming that he expects that gradual approach to raising interest rates will continue going forward.

On Friday, Federal Reserve chair Jerome Powell made remarks at an annual economic conference of central bankers in Wyoming. He said that he expects the Fed to continue gradually raising interest rates if the economic expansion in the country remains robust. At the same time he noted, that while annual inflation advanced to the level of 2%, it doesn't seem likely to increase further above that important point. He highlighted also that a gradual approach to rate increases is the best way to navigate between the risks of increasing rates too fast and acting too slowly.

EUR/USD rate landed at 1.1621 as of Friday the 23rd, up compared to last week closing level of 1.1437.

Stoxx 600 rose by 0.7% during the week ending August 24th, while German DAX increased by 1.5% week-on-weeks. Jerome Powell comments were widely reverberated on all global markets, supporting Europe's stock markets as well.

On August 26th, German economy minister expressed support for Turkey amid the backdrop of market turbulence after U.S. imposed sanctions and raised tariffs on Turkey. Peter Altmaier highlighted the importance of Turkey for Germany and for the European Union as whole. At the same time, he also didn't rule out possibility of assistance to Turkey, if country officials would ask support from Europe. While Altmaier acknowledged political differences between two countries ranging on a number issues, but he also expressed hope for overcoming them via dialogue.

Chinese central bank announced changes to how it manages the national currency. On top of that, authorities mentioned that they have no intention of using the yuan as a weapon in the trade war with United States. In particular, central bank announced that it introduced a calculation method called counter-cyclical factor in order to keep the yuan at a relatively stable value. PBOC also mentioned that the method previously helped mitigate a pro-cyclical market trends and stabilized market expectations.

Crude oil prices gained, as WTI futures increased by a mere 4.3% week-on-week and closed at USD 68.7 per barrel, while Brent futures gained more by 5.6%, landing at USD 75.8 per barrel.

Gold prices were on the rise as NYMEX 1m futures increased by only 2.5% week-on-week and finished the week at USD 1206.3 per troy ounce.

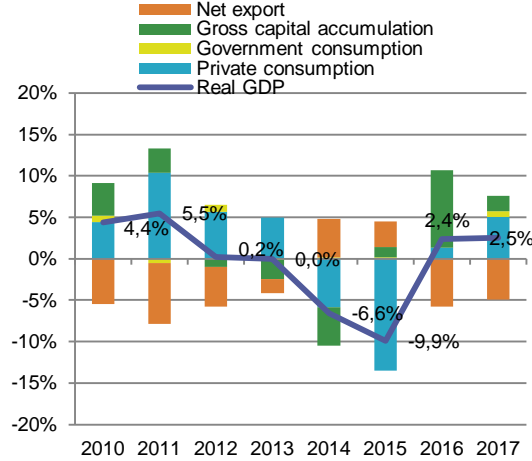
Grains plunged, as CBOT Corn 1m futures declined by 4.3% week-on-week and closed at USD 348.5 per bushel, while CBOT Wheat 1m futures landed at USD 514.8 per bushel, falling by 8.2%.

Iron ore declined, as NYMEX Iron ore 62% Fe 1m futures fell by a 0.8%, week-on-week and closed at USD 67.5 per ton.



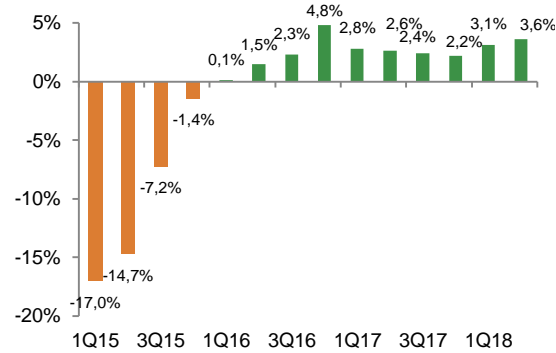
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Figure 9. Ukraine's real GDP growth in 2010-2017



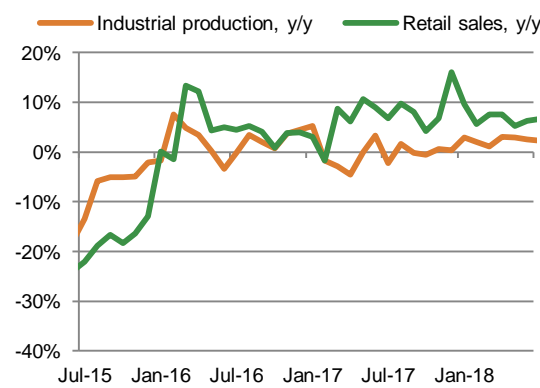
Source: Ukrstat

Figure 10. Ukraine's real GDP in 2015-2018, % y/y



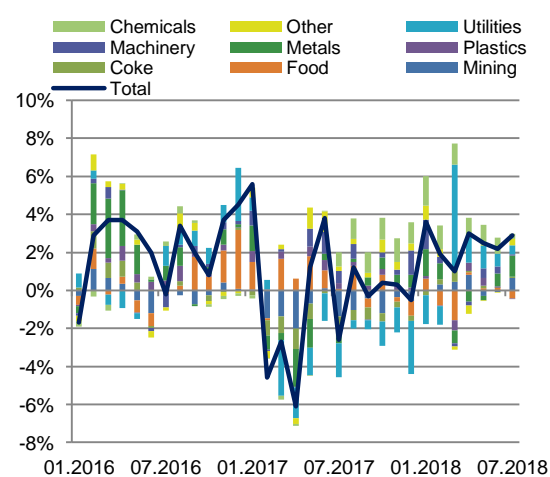
Source: Ukrstat

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



Source: Ukrstat

Figure 12. Industrial production 2016-2018, %



Source: Ukrstat

Ukraine's economy expanded by 3.6% y/y in 2Q18, according to Ukrstat preliminary reading or 0.9% seasonally adjusted on quarter over quarter basis. Internal demand and investment activity both were the main drivers of growth. At the same time, Ukraine started 3Q and 2H18 with a robust print in industrial production stemming from good performance of metal production rather than chemical and utility contribution.

Ukraine's reading of retail sales delivered gains of 6.6% y/y in July, following 6.3% y/y in prior month. In the meantime, YTD reading climbed down to 6.0% in 7M18 from 6.2% in 6M18. At the same time, the latest reading of wages growth showed increased by 24.2% y/y in June, following 27.6% y/y in May, while real average wages gained by 13.0% y/y, following 14.1% y/y increase in May.

The possibility of further increase of minimum wage remains in 2H18. If this happens, both the wages and retail sales growth and retail sales are to obtain new impulse of growth in 2018. We keep our forecast of retail sales growth at 7.0% in 2018.

Ukraine started 3Q and second half of the year with a robust print in industrial production. In contrast to prior month, when the bulk of growth came from utilities and chemical sector, this time metallurgy took the top spot, as measured by the share of contribution to the overall performance. It was followed by mining with growth concentrating in iron ore and oil and gas mining increase in July. At the same time, food production was the only major component putting downside pressure on the industrial production growth during the month.

On Wednesday, Ukrstat said that industrial production growth in Ukraine accelerated to 2.9% y/y in July, following 2.2% y/y increase in prior month. Meantime, the same statistic adjusted for a calendar day effect was 2.3% y/y in July, as in July 2018 there was 22 working days vs 21 a year ago. In 7M18, aggregate industrial production growth inched up to 2.6%, following 2.5% growth in 6M18.

Growth in mining jumped to 4.5% y/y, following two consecutive months of decline. It was stemming mainly from both mining of oil and mining of iron ore, which demonstrated bright performance the most during the month. In particular, oil mining gained by 5.7% y/y in July, while the mining of iron ore increased by 8.1% y/y. In the meantime, those gains were partly counterweighted by contribution coal mining, with declining mining by 1.8% y/y

Manufacturing subsector showed 2.3% growth in production in July, down from 2.8% y/y growth in June. The largest positive contribution came from metallurgical sector. Namely, metals production accelerated to 5.6% y/y, up from 3.3% y/y growth in June. Higher steel prices are supportive thus far, as average HRC price in 2018 was 14% compared to average price in 2017.

Chemicals production growth pared its gains to only 9.5% in July, dramatically down from more than 30% in prior month. At the same time it was a sharp slowdown from average reading in the last 12 months of roughly 40% gains. We attribute this slowdown to the effect of statistical base effect. In July 2017, Osthem officially launched its chemical plants, which resulted in healthy increase in chemical industry levels of production in the following months, provided the growth from a very low comparative base.

Food production was a weak spot of the July's statistic, as production fell by 1.9% y/y in July, following slight gains in June by 0.7% y/y.

Utilities production growth decelerated from 4.8% y/y in June to 3.2% y/y in July, with growth decelerating gradually from 22.8% reached in March, when the effect of statistical base and abnormally cold weather were fully unfolding.

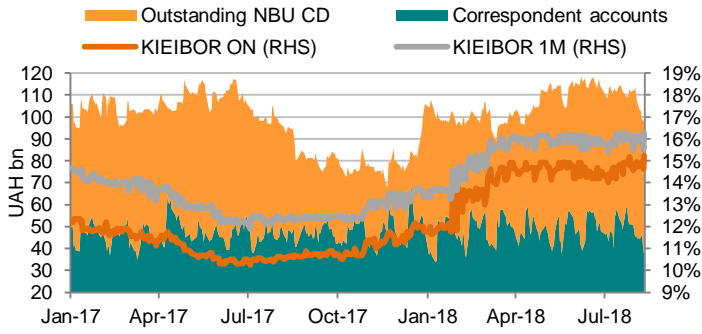
In the meantime, machinery industry also showed signs of decelerating growth, mainly due to auto transport category lower production at 14.3% y/y in July from 17.3% y/y in June. As a result, machinery output growth landed at 1.0% y/y in July.

While chemical and utilities were main growth drivers of industrial production in previous months, they passed the baton to metal production, which took the top spot, as measured by positive contribution to IP growth in July. All in all, we keep our industrial production forecast unchanged at 3.0% y/y in 2018.



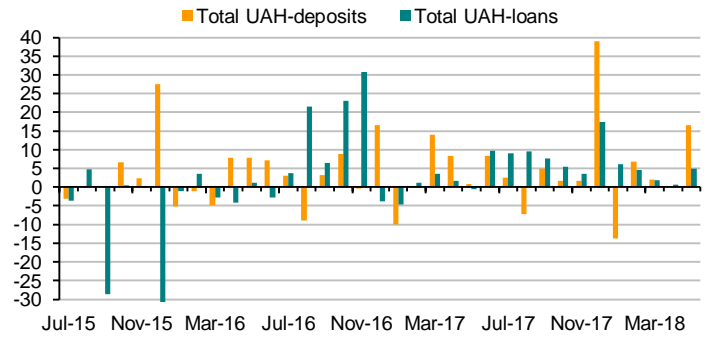
Money market

Banking liquidity vs. money market rates, %



Source: Reuters, NBU, UkrSibbank estimates

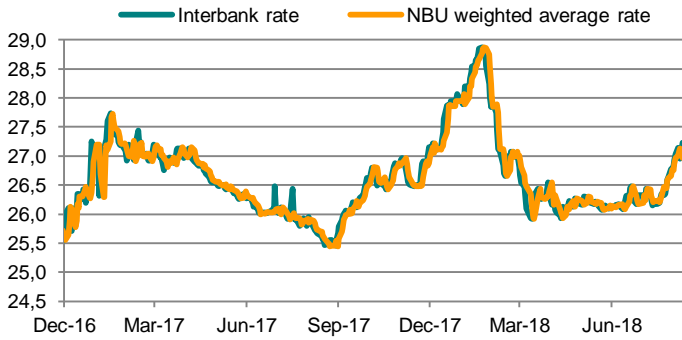
Monthly change in local currency loans and deposits, UAHbn



Source: the NBU

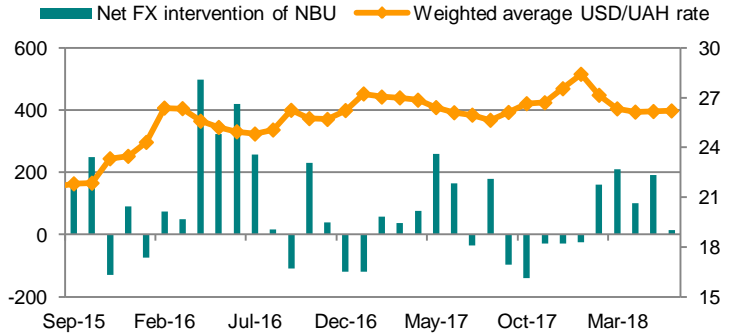
Currency market

UAH exchange rate, UAH/USD



Source: Reuters

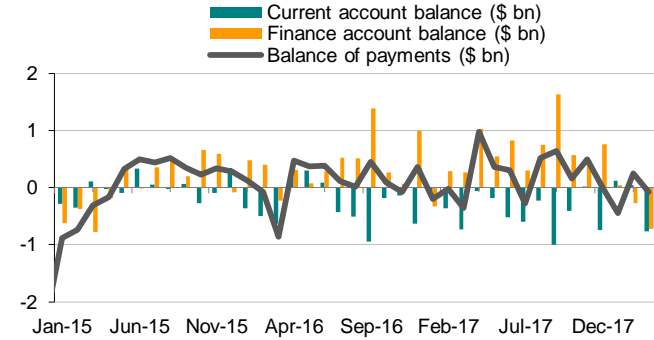
Net retail FX interventions of the NBU in 2015-2017, USDmn



Source: NBU

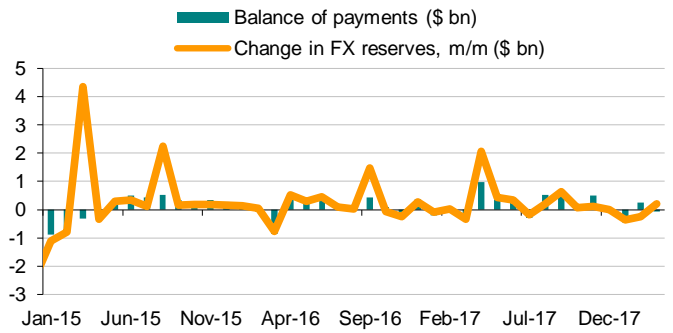
Balance of payments

Major BoP accounts, USDbn



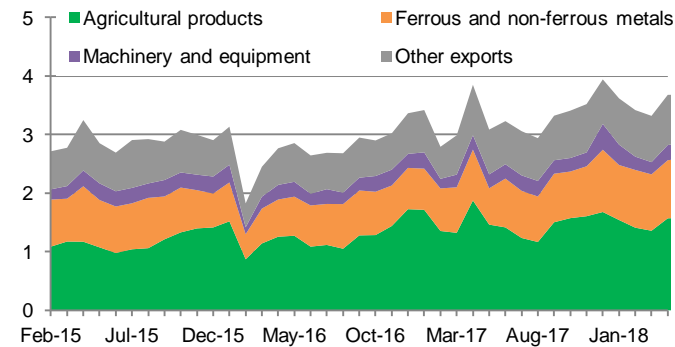
Source: NBU

BoP vs change in foreign reserves, USDbn



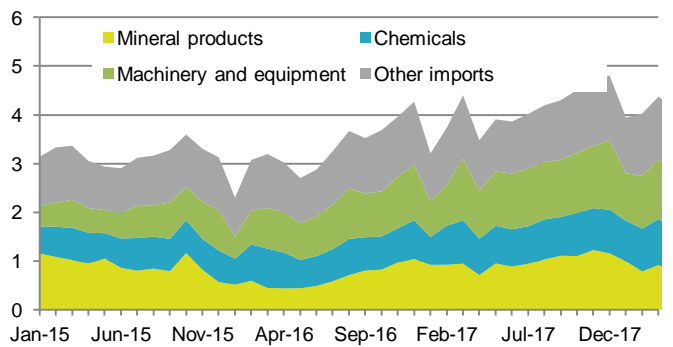
Source: NBU

Exports components dynamic, USDbn



Source: NBU

Imports components dynamic, USDbn



Source: NBU



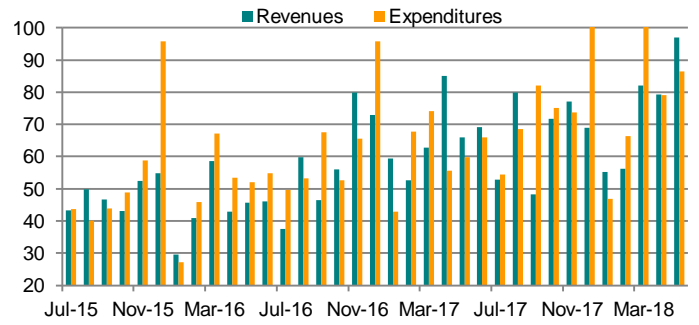
Budget performance

Budget performance, UAHbn

	Jan – May 2017	Jan - May 2018
Budget revenues	325,8	369,7
VAT proceeds	77,3	93,0
Corporate income tax	28,4	50,6
Budget expenditures	300,0	379,9
Revenues - Expenses	25,7	-10,2

Source: NBU

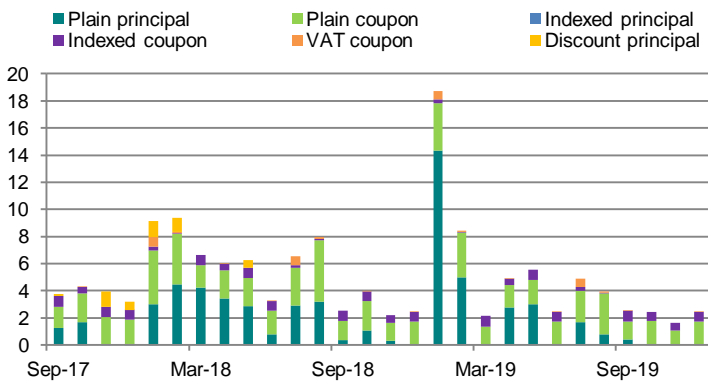
Monthly change in budget revenues and expenditures, UAHbn



Source: NBU, State Treasury

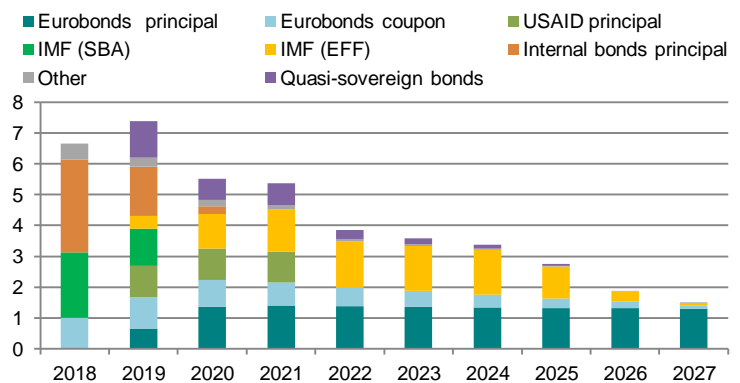
Sovereign debt

UAH- denominated debts' repayments schedule, UAHbn



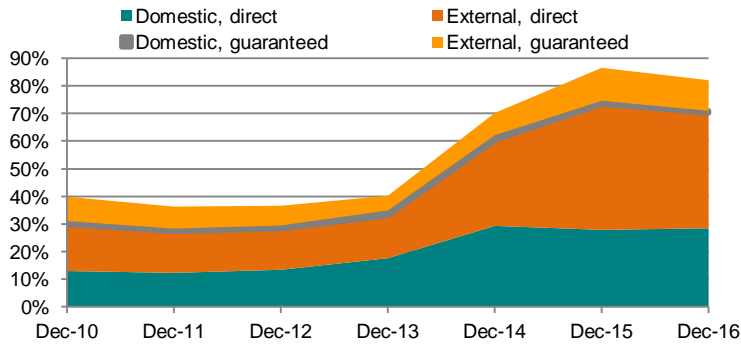
Source: NBU, UkrSibbank estimates

FX-denominated debt repayments schedule, USDbn



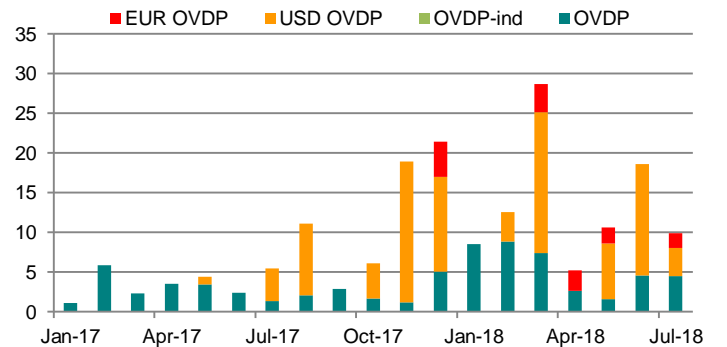
Source: Reuters, IMF, UkrSibbank estimates

Total government debt, % GDP



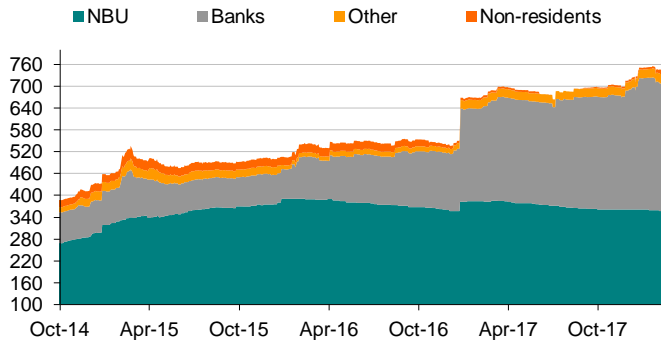
Source: MinFin

Local borrowings, UAHbn equivalent



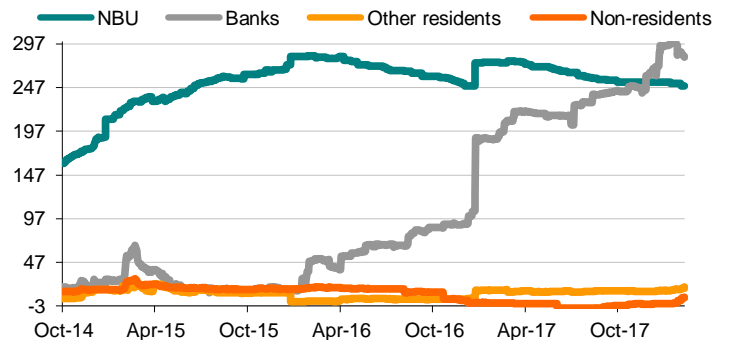
Source: NBU

Outstanding OVDP owners structure, UAHbn



Source: NBU

Outstanding OVDP changes in holding, UAHbn

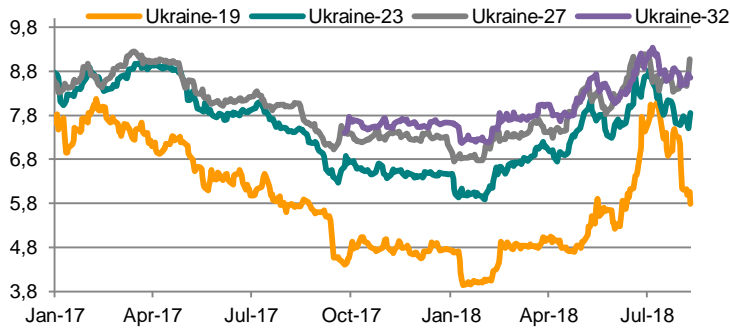


Source: NBU



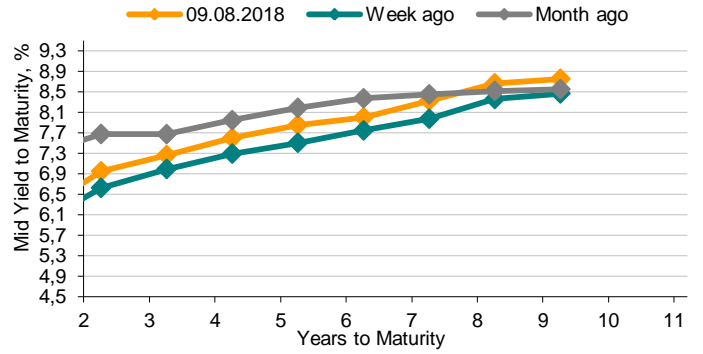
Eurobond market

Ukraine's sovereign Eurobond yields, %



Source: Reuters

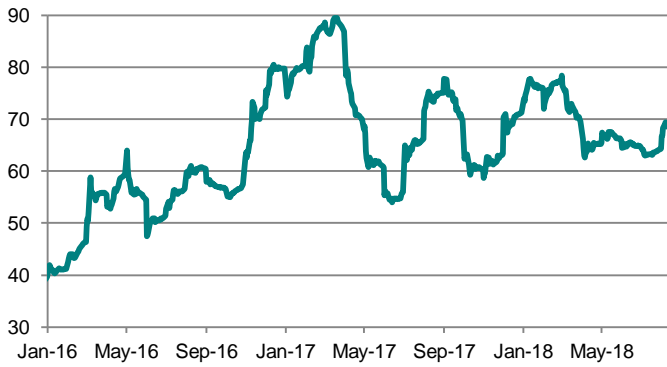
Ukraine's sovereign Eurobond yield curve



Source: Reuters

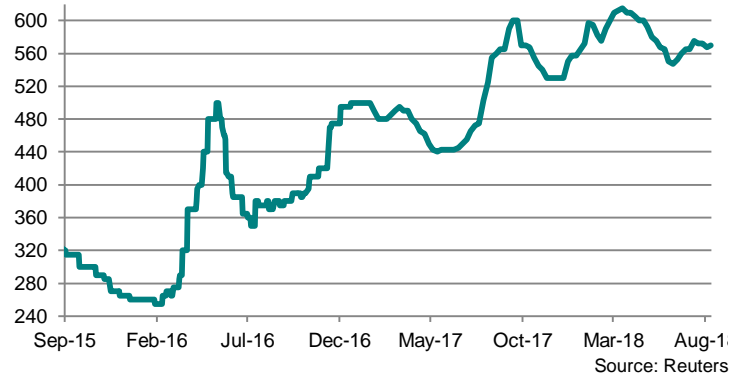
Commodity markets

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



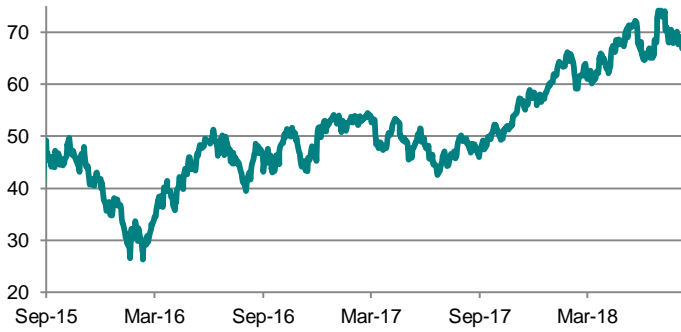
Source: Reuters

Steel CIS export HR coil, USD per ton



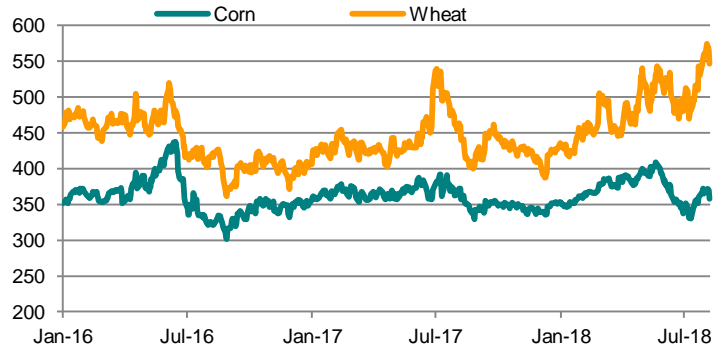
Source: Reuters

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	61.0
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	18.5
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	3.4
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	17.50*
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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