



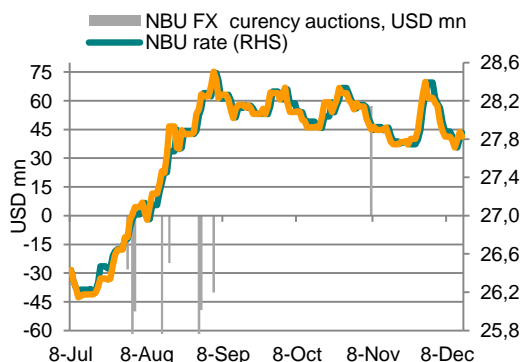
This week in focus: Budget: good performance in October

In October, budget collections amounted to UAH 72.6bn (+17.7% y/y). At the same time, budget expenses comprised UAH 71.7bn, resulting in roughly UAH 1bn budget surplus in October. The results indicated reverse from a prior month deep dive of UAH 18.9bn of deficit.

Please see page 3 for more details

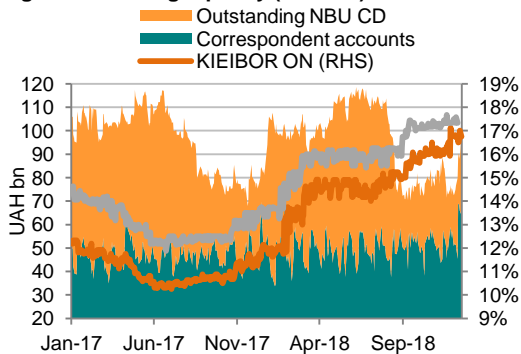
FX and interest rates: Liquidity is coming

Figure 1. UAH exchange rate (UAH per USD)



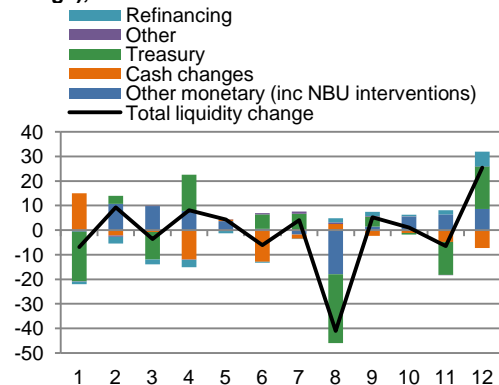
Source: NBU, Reuters

Figure 2. Banking liquidity (UAH bn)



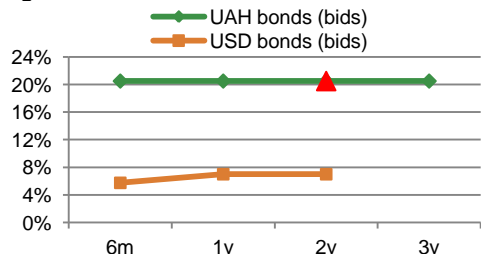
Source: Reuters, NBU, UkrSibbank, Minfin

Figure 3. Banking liquidity in 2018 (monthly change), UAH bn



Source: NBU

Figure 4. Local bonds market



Source: UkrSibbank

USD/UAH was at 27.87 as of Friday the 14th, as hryvnia were absolutely flat during the week, even despite dramatic surge in banking liquidity.

Central bank interventions resulted in USD 65.0mn of bought hard currency, as of December 14th. At the same time, NBU has sold USD30mn during the week, resulting in USD 35.0mn of bought hard currency on the market. It's quite remarkable that situation on the FX market allowed NBU to replenish its reserves in the first half of December, which is the month when central bank usually supports hryvnia with interventions. And YTD reading of central bank interventions remained USD 1.3bn of bought FX currency in 2018, as of December 14th.

Banking liquidity increased by roughly UAH 18bn during the week. Treasury operations added approximately UAH 16.0 during the week, followed by NBU refinancing (+5.7bn). At the same time, NBU interventions added approximately UAH 1.0bn to banking liquidity. As opposed to that, increased cash outside banks sliced UAH 4.6bn, as of week ended December 14th. Prior week result suggests budget end year increased spending in a full swing, with liquidity landing slightly below UAH 100bn threshold.

Money markets rate remained flat: cost of ON funds is around 18.00/19.00, 1 week is 18.00/19.00 while 1M is 18.50/19.50, according to our calculations.

Total proceeds from the auction yielded UAH 1.6bn. On December 11th, Ministry of finance issued bonds in UAH, USD and EUR, with the largest proceeds concentrated in EUR-denominated bonds. UAH bonds were issued with 3m, 6m and 1y maturity. The shortest among them, namely 3m attracted UAH 82.5mn of demand, out of which UAH 7.2mn were satisfied by MoF, with a cut off rate at 19.0%. At the same time, some portion of demand were applied for with 21% rate or above previously established 19.0% for 3m bonds, which was effectively rejected by MoF. 6m UAH bonds attracted several times less demand, but total proceeds to the budget exceeded the same of 3m bonds. As opposed to 3m UAH issues, all demand from USD denominated bonds were effectively satisfied at the auction. And last but not least, EUR-denominated issues took the top spot on the auction, as measured by total contribution to the proceeds. In particular, EUR bonds attracted EUR 43.0mn to the budget or more than 70% of all funds. On Wednesday (December 19th) are scheduled to be redeemed bonds for a total UAH 3.8bn. In the next month are concentrated heavy redemptions of UAH bonds, amounting to UAH 17.6bn. On top of that, USD 354mn of dollar denominated bonds is to be redeemed as well. The heavy payments of magnitude of that kind could cause fluctuations in banking liquidity at the beginning of 2019. And we expect demand on domestic bonds to be higher in January, compared to on average UAH 1.4bn placement proceeds in the previous three months.

Currently, yields (bids) of local OVDP in UAH at 21.50% (for 6m), 21.50% (for 2Y). 1Y USD bids were at 7.50%, while bids for VAT bonds were at 21.50%.

Figure 5. OVDP auction results, 11th of December 2018

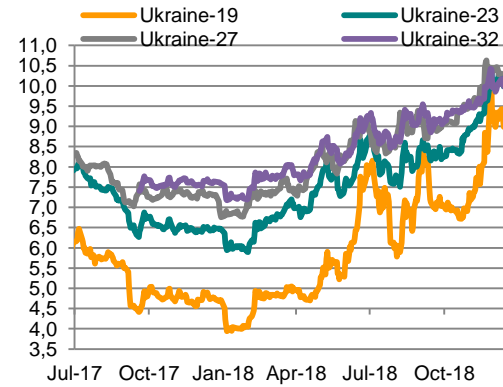
CCY	Maturity	Cut-off rate	WA rate	Max bid rate	Min bid rate	Number of bids	Bids accepted	Bid size	Placement size
UAH	3m	19.00%	19.00%	21.00%	19.00%	5	4	82.5mn	7.2mn
UAH	6m	18.50%	18.50%	18.50%	18.50%	7	7	14.7mn	13.5mn
UAH	1y	18.50%	18.50%	18.70%	6.70%	1	1	0.43mn	0.37mn
USD	6m	6.70%	6.70%	6.70%	6.70%	2	2	1.6mn	1.6mn
USD	1y	7.25%	7.25%	7.25%	7.25%	9	9	3.9mn	3.9mn
USD	1y	7.50%	7.50%	7.50%	7.50%	2	2	2.9mn	2.9mn
EUR	4m	4.50%	4.50%	4.50%	4.50%	4	4	43.6mn	43.0mn

Ukraine's central bank left its main interest rate on hold. As we expected (please see our Weekly report dated December 12th) NBU left interest rate unchanged. At the same time, in its press release NBU has noticed considerable progress made with IMF in reaching requirements established by the organization. In the meantime, there are some risks, which could potentially create headache to the central bank in reaching its midterm goal (inflation falling to 5.0% in 2020) going forward. The next monetary policy committee is scheduled to be on January 31st.



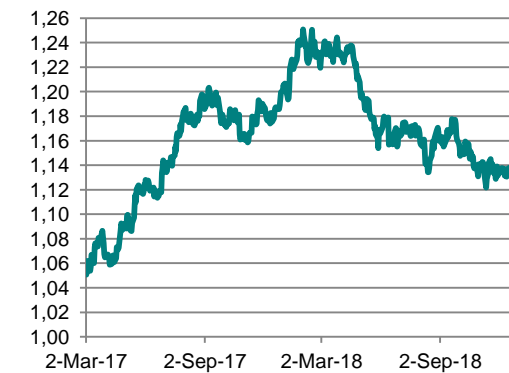
Global markets: EU inflation decelerated in November

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



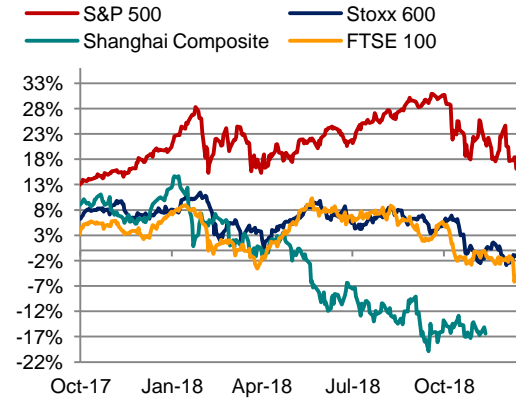
Source: Reuters

Figure 6. EUR USD spot (mid)



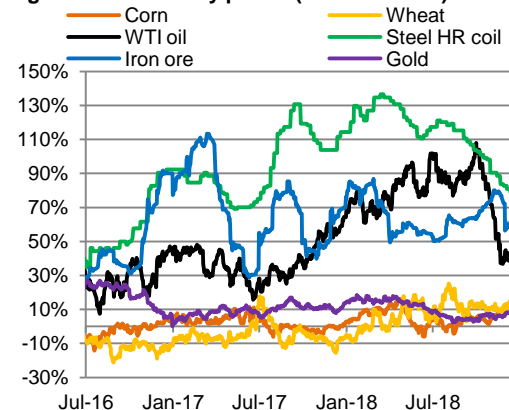
Source: Reuters

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



Source: Reuters

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



Source: Reuters

Producer prices index in the United States posted lower increase compared to previous month suggesting that inflation pressure declined. The European Union inflation reading showed deceleration in prices to 2.0%, down from 2.2%. On Tuesday, the Central Economic Work conference will be attended by top Chinese officials to discuss the economic policy for 2019

Bond benchmarks fell, with U.S. 10y Treasuries' yield increased by 3bp week-on-week landing at 2.83%, while German 10y Bunds' yields gained by 2bp, landing at 0.26%, Japanese 10y bonds yields ended the week at 0.03%.

The Labor Department said that the producer price index increased by 0.1% in November from October. The move indicated some deceleration, as in prior month prices advanced by 0.6% m/m. At the same time, prices gained by 2.5% y/y, which was the smallest increase in 2018. On top of that, core consumer prices increased by 0.3% in October and 2.7% on y/y basis. The latest available numbers suggest that inflation pressures declined from last year and could affect the Fed's thinking about a manner of increase of short-term rates. The latest data about consumer prices indicated that prices increased by 2.5% in October, while the more preferred Fed inflation gauge increased by 2.0% in October.

Equity indexes decelerated, as S&P dropped by 1.3%, while Nasdaq Composite declined by 1.6 % week-on-weeks. Prior week performance resulted in 2.8% decline in S&P 500 from the start of the year.

EUR/USD rate landed at 1.1307 as of Friday the 14th, down compared to last week closing level of 1.1355.

Main stock indexes in Europe gained as opposed to U.S peers, as Stoxx 600 increased by 2.4% during the week, while German DAX advanced by 2.3% week-on-week.

The European Union November inflation reading indicated a drop in y/y reading to 2.0% from 2.2% reported in prior month. On a month-on-month basis prices indicated a drop of 0.2%, according to Eurostat. The lowest increases in prices on an annual basis were registered in Denmark (0.7%), Ireland (0.9%), followed by Portugal (0.9%). Having registered 3.2% inflation in November, Estonia placed itself among the three European Union country with the highest inflation reported in November.

On Tuesday, the Central Economic Work conference will be attended by top officials to discuss the economic policy for the next year. The meeting is expected to last for two days. Once the meeting will be finished, economic policies discussed will be gathered in report issued by state owned news agency. At the conference policymakers are expected to discuss ways to stabilize Chinese economy and trade war with United States.

Crude oil prices slightly advanced, as WTI futures increased by 0.4% week-on-week and closed at USD 51.2 per barrel, while Brent futures advanced by 0.5%, landing at USD 60.3 per barrel.

Gold prices fell as NYMEX 1m futures decreased by 0.5% week-on-weeks and finished the week at USD 1237.0 per troy ounce.

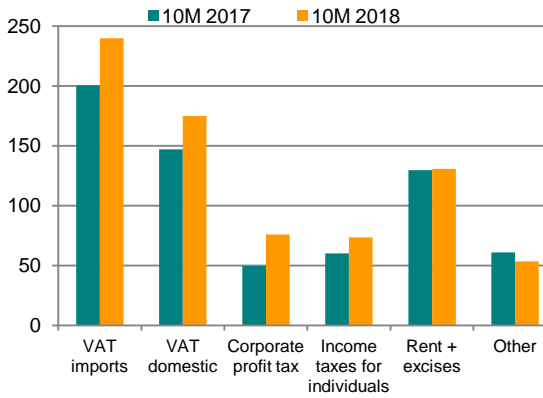
Grains prices increased, as CBOT Corn 1m futures rose by 0.7 % week-on-week and closed at USD 376.8 per bushel, while CBOT Wheat 1m futures landed at USD 527.8 per bushel, gaining by 2.5% during the week.

Iron ore advanced, as NYMEX Iron ore 62% Fe 1m futures increased by a 2.1% on a week-on-week basis and closed at USD 67.9 per ton.



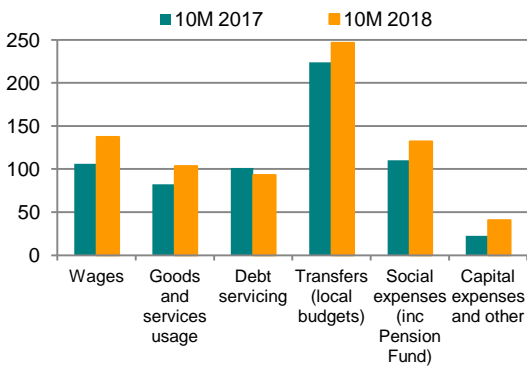
This week in focus: Budget: good performance in October

Figure 9. Main state budget revenue components, UAHbn (cumulatively)



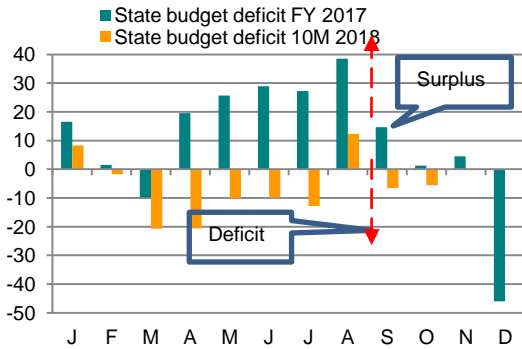
Source: Treasury

Figure 10. Main state budget expenses components, UAHbn (cumulatively)



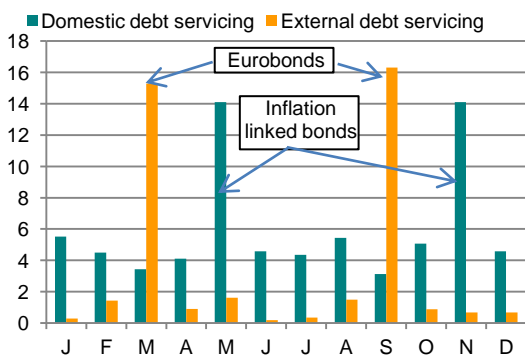
Source: Treasury

Figure 11. State budget deficit, UAHbn (cumulatively)



Source: Treasury

Figure 11. Debt servicing, UAHbn



Source: Treasury

In October, budget collections amounted to UAH 72.6bn (+17.7% y/y). At the same time, budget expenses comprised UAH 71.7bn, resulting in roughly UAH 1bn budget surplus in October. The results indicated reverse from a prior month deep dive of UAH 18.9bn of deficit.

Assessing the budget from the standpoint of actual results compared to planned performance we can conclude the same, namely the stronger performance in October exceeds the planned collections by the Ministry of Finance by 1.8% during the month. And what's more important is that preliminary data about performance of collections in November showed higher percentage of overfulfilment of budget collections in November. In particular, state budget incomes exceeded previous plans of the Ministry of Finance by 2.5%. At the same time budget collections showed even stronger acceleration to 24.3% in November from 17.7% in October.

It should be noted that from the beginning of the year, actual budget collections fell short from expectations of the Ministry of Finance, which in some periods undershot expectations by more than 3% (in 6M 2018). But the second part of the year proved to be healthier, with 11M 2018 reading improving to 1.9% of gap.

Improvements in budget collections in October were driven mostly by stronger incomes from taxes (+ 26.9% y/y in October vs 13.1% y/y in September), as opposed to non-tax sources of revenue, which were in the state of decline in aggregate in October. In regard to taxes, almost all major components showed increase in performance based on y/y basis. In particular, taxes from individuals gained by 21.9% y/y in October from 19.2% y/y reported in prior month. Rent payments increased, gaining by 2.5x times in October vs October 2017. But from the beginning of the year rent payments showed decline of 18.5% in 10M 2018 vs 10M 2017. In regard to excises, collections from both types of them accelerated during the last month, namely tax coming from domestic sources showed 17.6% y/y increase in compared to 9.8% y/y increase in September. While the other, with taxable base coming from imports, showed even stronger footing in October gaining by 21.1% y/y. Import duty, in line with performance of import based excises, advanced to 17.6% y/y from 11.6% y/y reported in prior month. Last but not least, the VAT taxes, the major source of revenue stream from taxes, were on the rise in October too. In particular, VAT tax from imports advanced the most by 30.9% y/y, from 25.7% y/y in September. It was followed by VAT from domestic sources, showing increased collections by 10.7% y/y, up from 9.7% y/y in prior month.

Non-tax revenue stream posted decline in y/y terms. The main reason of that was central bank. NBU transfers were absent in October, as central bank managed to allocate its transfers in the first half of the year. At the same time, NBU transferred UAH 5bn to the budget in October 2017. Non-taxed incomes were partly supported by enlarged dividends from the state companies, namely they increased to UAH 0.5bn compared to UAH0.1bn reported in October of prior year.

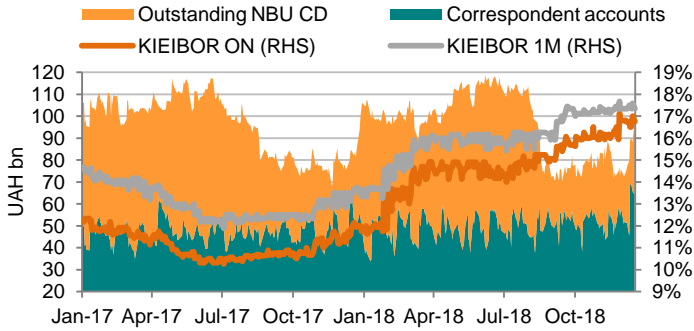
Importantly, the record widening of the state budget deficit to UAH 18.9bn in September was driven by increased spending on debt servicing. We observed the similar pattern in May and March. In September, and March Ukraine is to pay coupons under its restructured Eurobonds of about USD 0.5bn, which resulted in the same number of deficit of UAH 18.9bn in September and in March for the state budget. In contrast to servicing external debt in March and September, the increased debt servicing in May was driven by recent OVDP reprofiling. According to it, inflation linked UAH bonds for a total UAH 150bn were divided into two equal parts, namely with coupon payments in May and November.

Healthy state budget revenue growth resulted in UAH 1bn surplus in the budget in October. Meantime, November's preliminary data indicates that budget remains in the strong shape, with actual revenue exceeding planned by 2.5% or by UAH 2.3bn. In November, increase in revenue partly was driven by quarterly income tax payments.



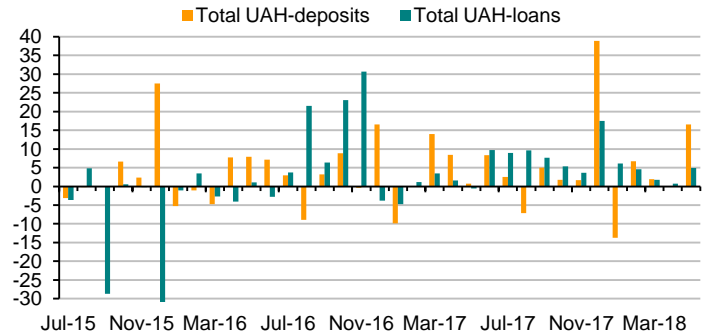
Money market

Banking liquidity vs. money market rates, %



Source: Reuters, NBU, UkrSibbank estimates

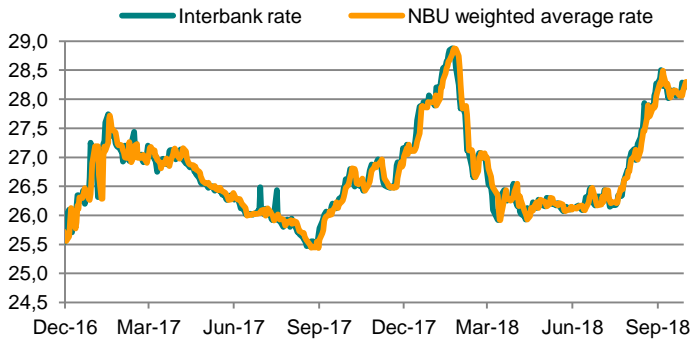
Monthly change in local currency loans and deposits, UAHbn



Source: the NBU

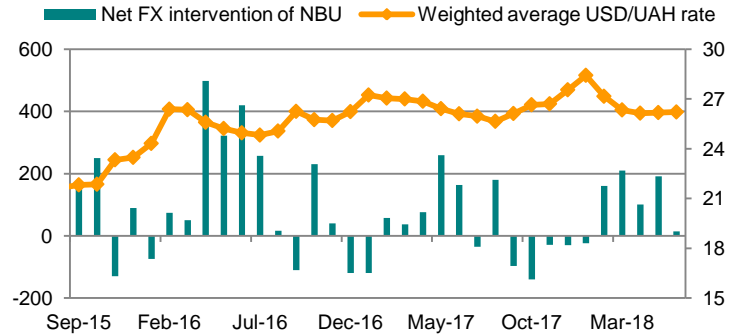
Currency market

UAH exchange rate, UAH/USD



Source: Reuters

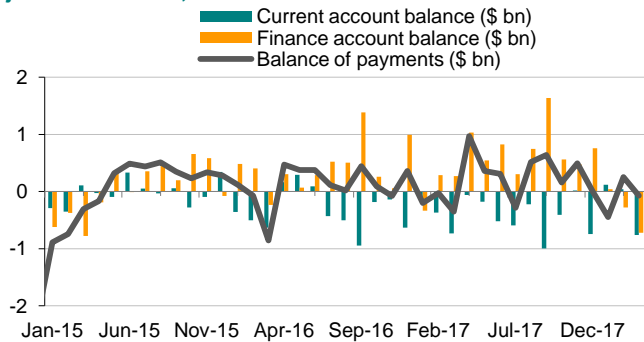
Net retail FX interventions of the NBU in 2015-2017, USDmn



Source: NBU

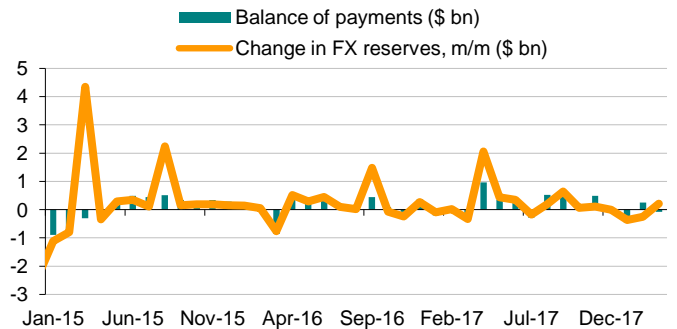
Balance of payments

Major BoP accounts, USDbn



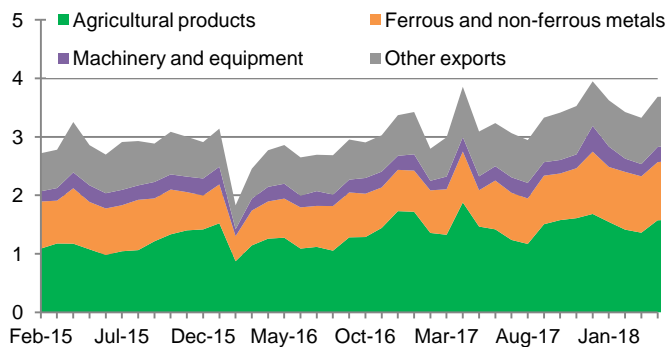
Source: NBU

BoP vs change in foreign reserves, USDbn



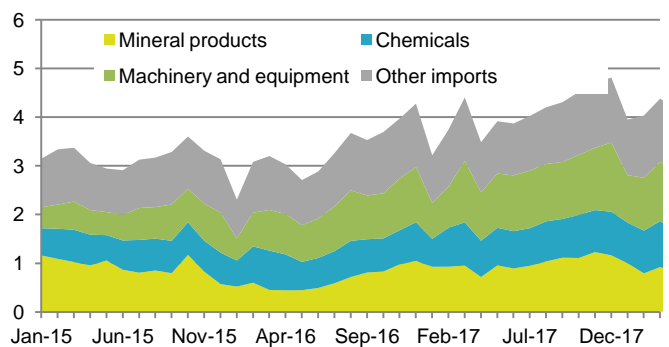
Source: NBU

Exports components dynamic, USDbn



Source: NBU

Imports components dynamic, USDbn



Source: NBU



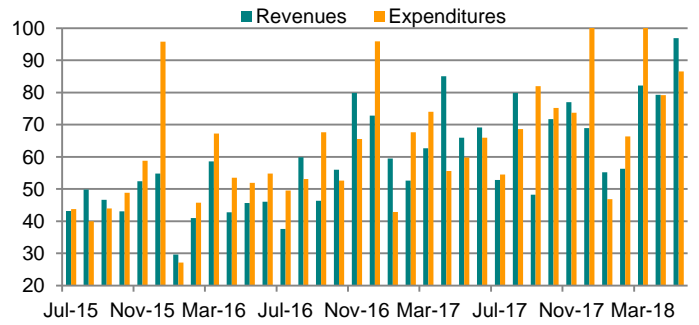
Budget performance

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

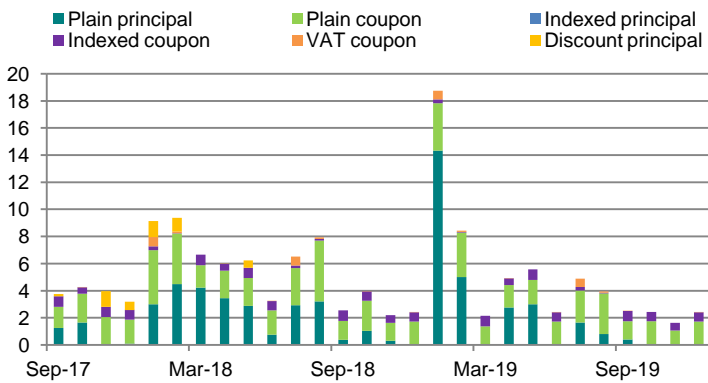
Monthly change in budget revenues and expenditures, UAHbn



Source: NBU, State Treasury

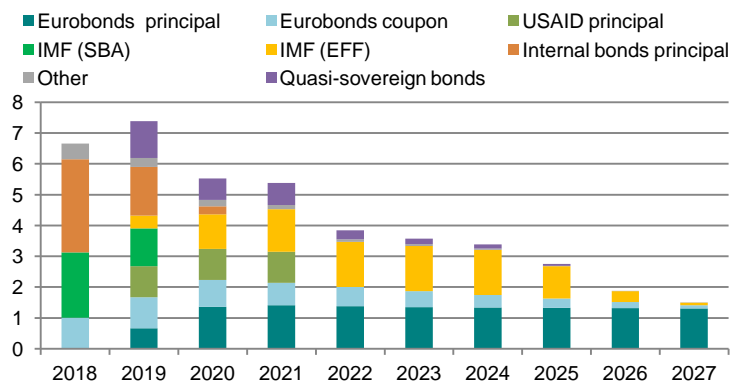
Sovereign debt

UAH-denominated debts' repayments schedule, UAHbn



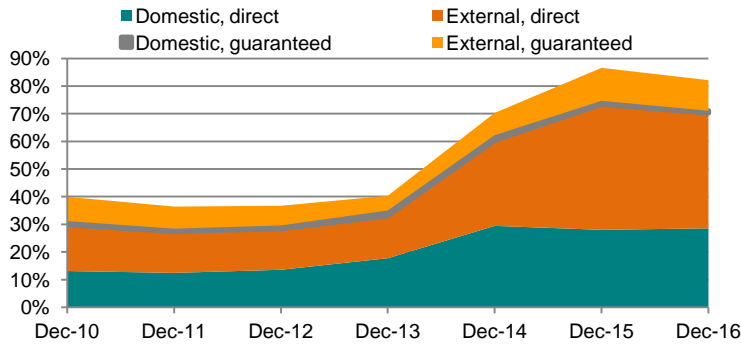
Source: NBU, UkrSibbank estimates

FX-denominated debt repayments schedule, USDbn



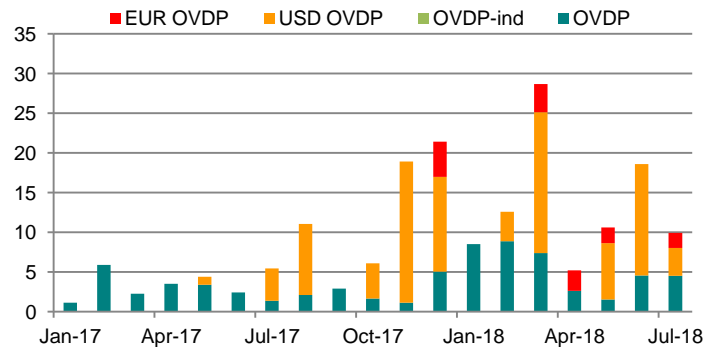
Source: Reuters, IMF, UkrSibbank estimates

Total government debt, % GDP



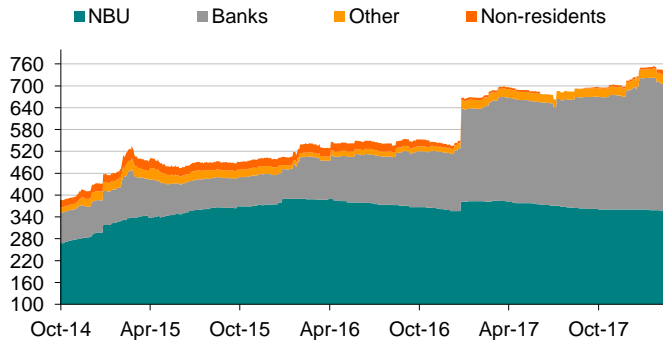
Source: MinFin

Local borrowings, UAHbn equivalent



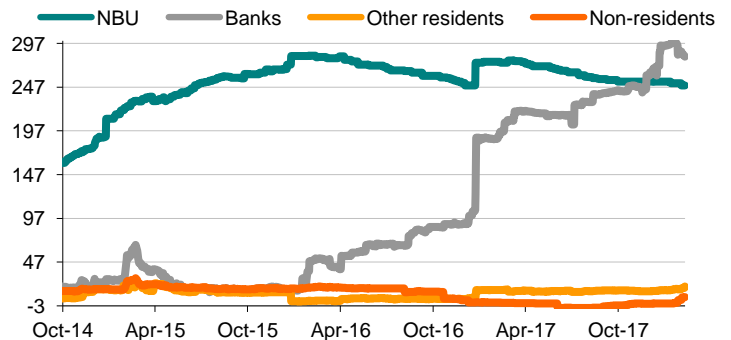
Source: NBU

Outstanding OVDP owners structure, UAHbn



Source: NBU

Outstanding OVDP changes in holding, UAHbn

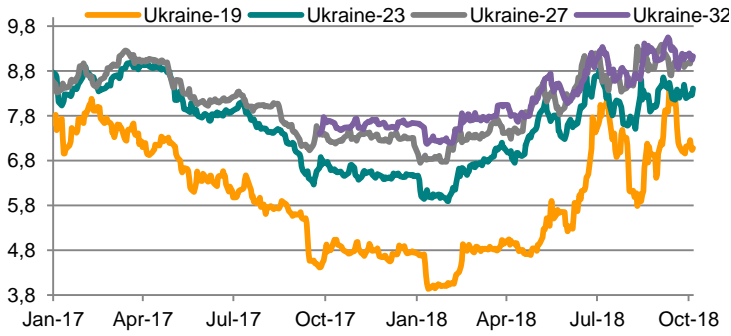


Source: NBU



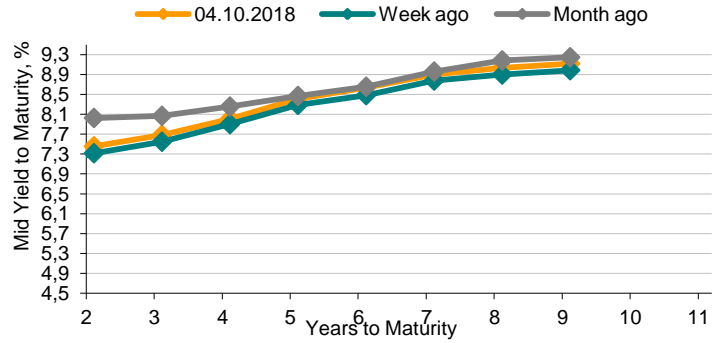
Eurobond market

Ukraine's sovereign Eurobond yields, %



Source: Reuters

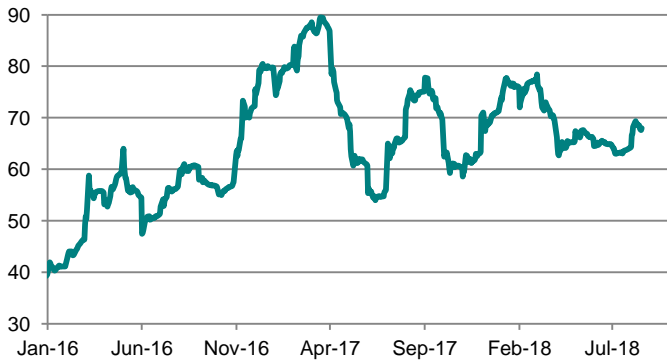
Ukraine's sovereign Eurobond yield curve



Source: Reuters

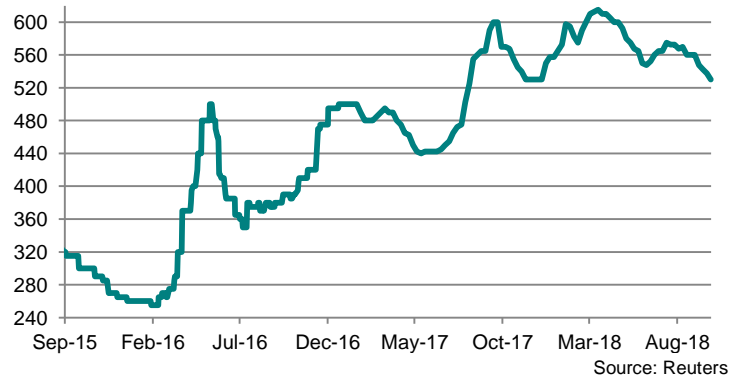
Commodity markets

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



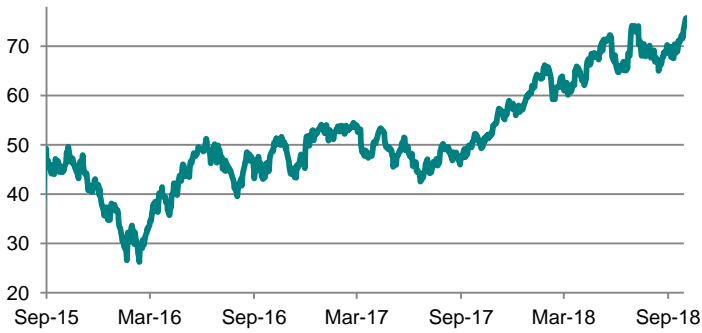
Source: Reuters

Steel CIS export HR coil, USD per ton



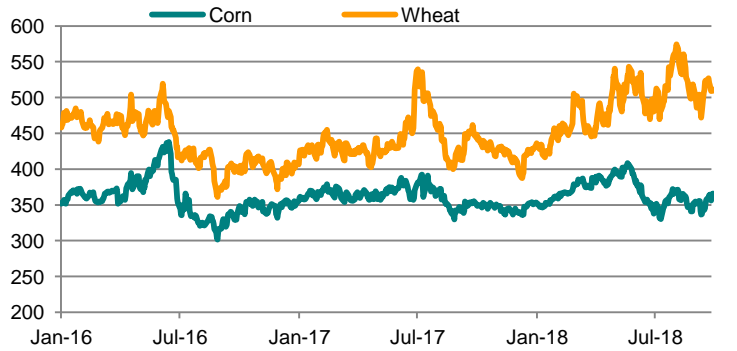
Source: Reuters

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	3.4
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	3393.0
Nominal GDP (USD bn)	178.9	112.8	136.1	163.1	175.8	183.5	133.7	91.2	93.1	112.1	125.0
Prices											
CPI (average %YoY)	25.2	15.9	9.4	8.0	0.6	-0.2	12.1	48.7	16.5	14.4	11.5
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	10.3
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	1.6	-1.3	-2.4	-4.9
Current account balance (% of GDP)	-7.1	-1.5	-2.2	-6.3	-8.1	-9.0	-3.4	1.8	-1.4	-2.1	-3.3
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	19.5
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	3.2
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	18.00*
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



Contacts

Investment Business

Serhiy Yahnych

Head of Investment Business

(+38044) 537 5082 serhii.yahnych@ukrsibbank.com

Maksym Burynskyi

Research Analyst

(+38044) 230 48 54 maksym.burynskyi@ukrsibbank.com

Viktoriia Nebeska

Brokerage Local Securities & Custody Sales

(+38044) 201 22 74 viktoriia.nebeska@ukrsibbank.com

Platon Yachmenov

Advisor Local Securities

(+38044) 230 48 54 platon.yachmenov@ukrsibbank.com



FX Business

Oleksandr Duda

Head of FX Sales

(+38044) 537 5002 oleksandr.duda@ukrsibbank.com

Corporate Business

Ievgen Kulikov

Head of MNC team

ievgen.kulikov@ukrsibbank.com

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