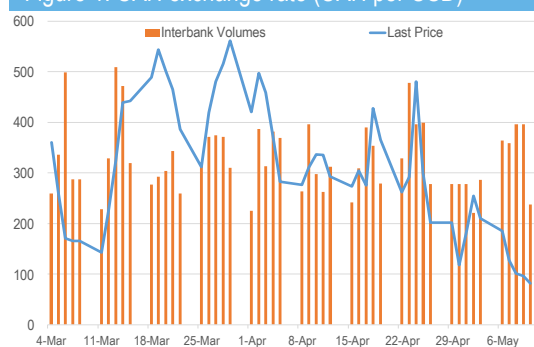


ECONOMICS | INTEREST RATES STRATEGY | FX

15 May 2019

UKRAINIAN CAPITAL MARKETS WEEKLY

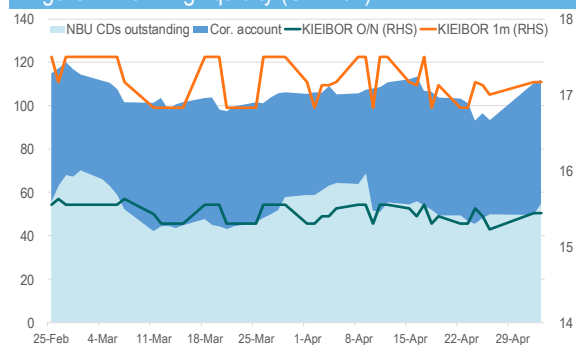
	Rating	Outlook	Last update	This week in focus: Ukraine inflation inches up in April
Fitch	B-	STABLE	08.03.2019	Inflation in Ukraine accelerated to 1.0% mm in Apr from 0.9% mm in Mar. The year's growth increased to 8.8% from 8.6% last month. The main factor behind was growth of prices within food segment. The current developments in CPI were generally caused by temporary factors. We underline, however, the case of growing salaries payments, which might push up prices across the board.
S&P	B-	STABLE	12.04.2019	
S&P (N)	uaBBB	-	12.04.2019	
Moody's	Caa1	STABLE	21.12.2018	

Figure 1. UAH exchange rate (UAH per USD)

FX and interest rates: UAH made rebound from 2019 record high

The UAH gained against the US Dollar during the last week: the local currency strengthened by 1% to 26.12 (as of May 14). The Ukrainian hryvnia seems to have entered traditional for spring season of appreciation, when agro producers increase sales of FX export revenues in order to finance sowing campaign.

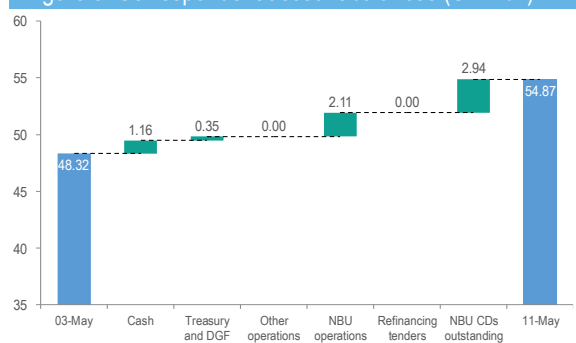
Besides, additional supply generated corporates, converting FX stocks into UAH in order to meet tax and salaries payments, as well as foreign investors, which continue to increase their portfolio of UAH-denominated government securities.

Despite NBU actively purchased FX during last week (USD80mn in total), due to ample supply these interventions didn't have material effect on the quotations of the currency market.

Figure 2. Banking liquidity (UAH bn)


On May 15 USD/UAH quotations rebounded to 26.3 levels. We expect some pressure on the market may come from multinationals, which are to purchase FX in order to meet dividend repayments.

In addition to that we would like to point out, that the IMF mission will arrive in Kyiv on May 21. The mission, allegedly, will hold regular consultations with Ukraine regarding Article IV of the IMF Agreement. Due to low clarity about further cooperation between Ukraine and the IMF, this factor might be a source of volatility on the FX market.

Figure 3. Correspondent account balances (UAH bn)


Banking liquidity stayed above USD110bn by the end of last Saturday (May 11). The amounts deposited on correspondent accounts increased by 4.6% to UAH59.7bn, investments in CDs decreased by 5.4% to UAH51.9bn.

Amount of liquidity was boosted by NBU interventions on the interbank FX market, amounted UAH2.1bn, and about UAH1.2bn came from the cash market.

At the same time, the main influence on the liquidity level in the system had MinFin operations, that drained about UAH6bn at the beginning of the week and ensured inflow of almost the same amount at the end.

We expect **quarterly payments of corporate taxes, that have recently started, will provide a major outflow of the liquidity from the system during this week.** At the same time, upcoming large amount redemptions of local government bonds will help to offset liquidity drains.

Figure 3. Local UAH bonds market

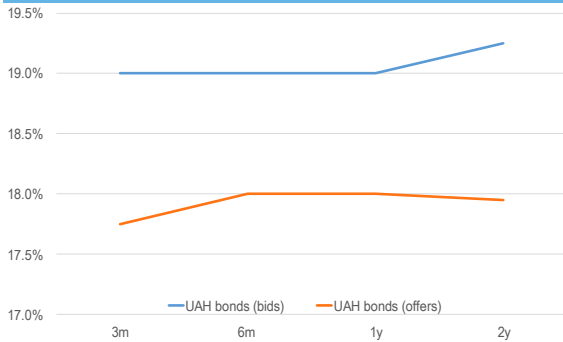
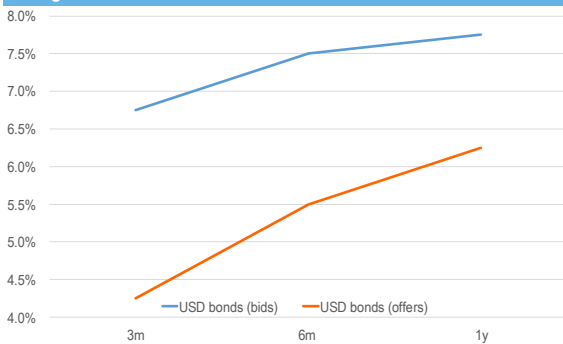


Figure 4. Local USD bonds market



Government bond market

CCY	Maturity	Cut-off rate	WA rate	Max bid rate	Min bid rate	Number of bids	Bids accepted	Bid size, mn	Placement size, mn
UAH	3m	18.50%	18.37%	18.50%	18.00%	22	22	442.45	442.45
UAH	6m	18.50%	18.40%	18.50%	18.25%	10	10	842.2	842.2
UAH	1y	18.50%	18.39%	18.50%	18.00%	16	16	798.83	798.83
UAH	2y	17.95%	17.81%	17.95%	17.75%	9	9	476.11	476.11
UAH	3y	17.00%	17.00%	17.00%	17.00%	3	3	90	90
USD	1y	7.25%	7.25%	7.50%	7.25%	21	20	62.28	61.28

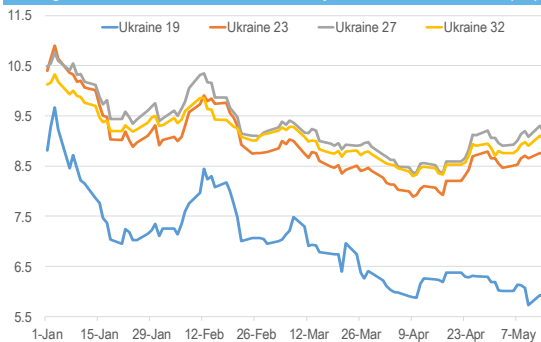
MinFin attracted about UAH4bn (equivalent) on the primary auction held May 14th, accepting all the bids for UAH bonds. The major demand for UAH bonds was for 6m and 1y securities, with amount UAH842mn and UAH799mn respectively. Cut-off rates stayed unchanged, comparing to the previous auction, at 18.50% per year.

The ministry also placed 2y and 3y UAH bonds at rate 17.81% and 17.00% respectively and attracted in total UAH0.56bn.

The demand for USD-denominated bonds amounted about USD63mn, but the ministry refused one application (for USD1mn) at the rate of 7.5%, while maintaining the yield at 7.25% per annum.

On the secondary market yields (bids) of local UAH bonds stayed at 19.00% (for 6m), 19.25% (for 2Y). 1Y USD bids were at 7.75%. Offers are 0.50%-0.75% below yields on the primary market.

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



USD gets stronger on hopes for a US-China trade compromise

The EUR/USD slipped last week to 1.12 as hopes for a U.S.-China compromise on trade talks. A resolution of the dispute would allow global economic growth to stay around trend (for the eighth year in a row) and traders pulled money from safe-haven assets.

At the same time, on Friday (May 10), the Labor Department reported that U.S. consumer prices rose in April but underlying inflation remained muted, suggesting the Fed could keep interest rates unchanged for a while.

The euro was resilient during last week. Despite there were Spanish and German positive stats published last week, it didn't provide much support to the euro currency.

Figure 6. EUR USD spot (mid)

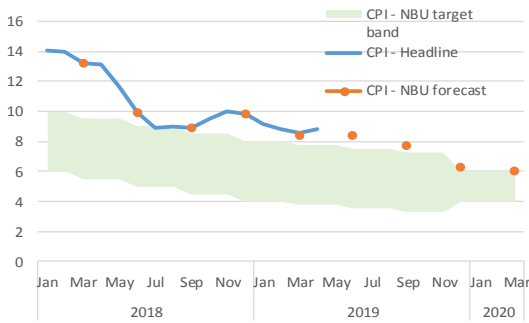


With U.S. and Chinese officials back at the negotiating table on Friday, investors have quietly revised bets of a Fed's interest rate cut. As a result, U.S. government debt prices were lower after President Trump said that a breakthrough with China, if it happens, will be announced in three to four weeks.

On Wednesday, market players seem have temporarily shifted focus from the trade war concerns on U.S. fundamentals. There will be retail sales, manufacturing numbers, industrial production and business inventories published throughout the day.

At the moment the yield on the benchmark 10-year Treasury note at around 2.4139%, while the yield on the 30-year Treasury bond at around 2.8501%.

Figure 7. CPI growth, % y/y



Ukraine inflation inches up in April

Inflation in Ukraine accelerated to 1.0% m/m in Apr from 0.9% m/m in Mar. The year's growth increased to 8.8% from 8.6% last month.

The main factor behind the dynamic was growth of prices within broad food segment (incl. alcoholic beverages), generally imposed by a speculative demand for certain raw food products due to their limited supply in early spring, and a slight seasonal acceleration in prices for alcoholic beverages.

Besides, a notable pro-inflation effect had continuing seasonal growth of closing and footwear prices, and expansion in transport prices. The last was driven both by growth in passengers' transport fares and fuel prices growth, which was caused by difficulties with energy imports from Belarus and Russia.

Decline in prices on miscellaneous goods and services, observed in Apr, helped to somehow curb inflation growth.

Despite months' readings grew for the second consecutive month, we see the current developments in consumer price inflation and its components were generally caused by temporary factors. The food prices used to decline during May-Aug as supply of raw products increases, and UAH strengthening, observed since beginning of the May, should help to maintain price stability.

We also saw in Apr abating of seasonal increase in closing and footwear prices, and expect easing inflation pressure from transport prices, as effect of oil products supply disruptions is likely to play out in May while the next stage of raise of tariffs for passenger railway transportation is scheduled for October.

At the same time, we underline the case of growing salaries and very tight labor market, which might push up prices across the board. Also, provided double elections this year, social payments continue to be on the rise. Subsequently, demand side factors will likely push inflation up whenever any supply shock appears (e.g. vegetables, fuel, etc).

Additionally, we believe that gradual UAH depreciation later this year, is likely to contribute to price growth, particularly in case if no-IMF scenario is realized and access of Ukraine to international markets becomes difficult.

The next meeting of the NBU's monetary policy will be held on Jun 6, before the May's inflation readings announcement (scheduled for Jun 10). At this point of time the odds are slightly to favor of another cut being on cards, although results of upcoming IMF mission, coupled with elevated inflation print last month provide reasons for no-change action.

Figure 8. Contribution to CPI growth, p.p.

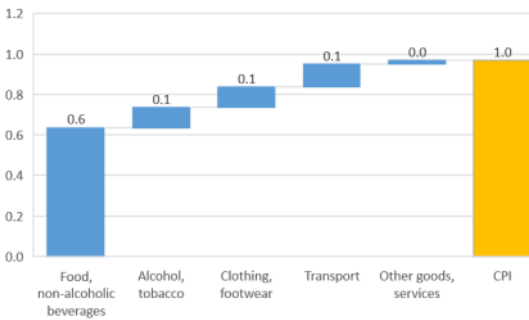


Figure 9. Main contributors to CPI growth

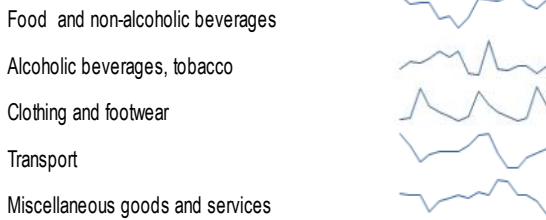


Figure 10. Nominal and real wages, % y/y



UKRAINIAN CAPITAL MARKETS WEEKLY

Key Macroeconomic Indicators

	2013	2014	2015	2016	2017	2018	2019F	2020F
Real sector								
Real GDP (%YoY)	0.00	-6.60	-9.80	2.30	2.50	3.30	2.70	3.00
Industrial production (%YoY)	-4.30	-10.70	-6.00	2.40	-0.10	1.60	0.00	1.20
Retail sales (%YoY)	6.10	-11.00	-25.00	4.00	8.80	6.10	5.00	4.00
Unemployment rate end of year (ILO, working age)	7.70	9.70	11.50	9.30	8.70	8.50	8.50	8.40
Nominal GDP (UAH bn)	1466	1587	1980	2383	2983	3393	3830	4321
Nominal GDP (USD bn)	183.50	133.70	91.20	93.10	112.10	125.00	129.50	135.90
Prices								
CPI (average %YoY)	-0.20	12.10	48.70	16.50	14.40	10.50	9.20	8.10
CPI (end of year %YoY)	0.50	24.90	43.30	12.40	13.70	9.80	8.50	7.20
Real average wage growth (%YoY)	8.20	-6.50	-35.00	10.00	18.90	9.70	8.00	6.00
Fiscal balance (% of GDP)								
State budget deficit (without Naftogaz)	4.20	4.90	2.30	2.90	1.60	2.40	2.40	2.30
Total public debt	39.90	69.40	79.40	81.00	71.80	61.00	60.00	61.00
External balance								
Exports of goods and services (USD bn)	81.70	65.40	47.90	46.00	54.00	59.00	61.50	63.70
Imports of goods and services (USD bn)	97.40	70.00	49.60	51.80	60.80	70.50	73.30	75.80
Current account balance (USD bn)	-16.50	-4.60	1.60	-1.30	-2.40	-4.70	-4.20	-4.80
Current account balance (% of GDP)	-9.00	-3.40	1.80	-1.40	-2.10	-3.30	-3.20	-3.50
Net FDI (USD bn)	4.10	0.30	3.00	3.40	2.30	2.50	2.30	2.40
Foreign exchange reserves (end of year)	20.40	7.50	13.30	15.50	18.80	20.80	19.50	20.50
Imports coverage (months of imports of goods)	2.90	1.50	4.40	3.70	3.60	3.40	3.30	3.30
Interest and exchange rates								
NBU discount rate (% end of year)	6.50	14.00	22.00	14.00	14.50	18.00	16.00	13.00
Exchange rate (UAH/USD) end of year	8.20	15.80	24.00	27.20	27.95	27.70	31.50	32.50
Exchange rate (UAH/EUR) end of year	11.30	23.00	26.20	28.30	33.50	31.80	37.80	39.00



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