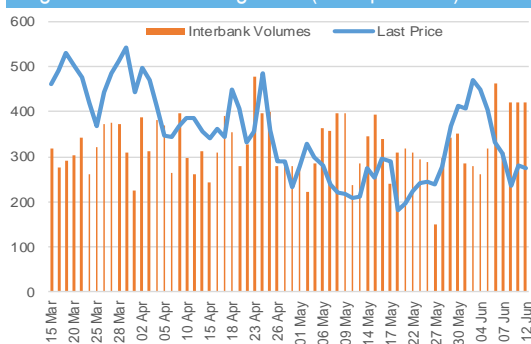


	Rating	Outlook	Last update	This week in focus: Inflation back on downward pace, but new risks loom up
Fitch	B-	STABLE	08.03.2019	Inflation in Ukraine in May 2019 slowed down to 0.7% m/m after two-month growth, thanks to deceleration of growth of food and non-alcoholic products prices. In annual terms, consumer price growth in May accelerated to 9.6% from 8.8% in Apr due to a statistical low-base effect. At the moment we stick to our conservative year-end CPI forecast at 8.5%.
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 regained ground on fresh FX inflow

The USD/UAH regained positive traction after the dip below 27 level last week. The upside movement was induced by exporters, who started to sell FX revenues after hryvnia reached two-month low levels. Then, at the beginning of this week, foreign accounts increased FX supply, buying UAH ahead of FinMin Tuesday's auctions. There is also stable inflow of foreign currency from the cash market.

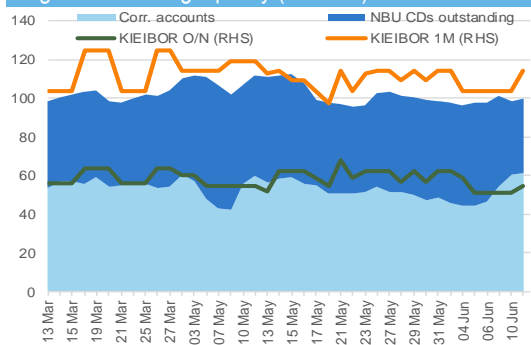
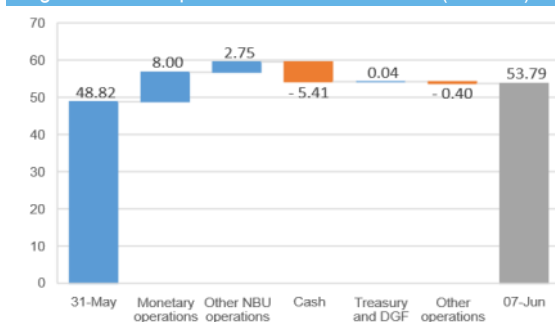
On Tuesday, after clinching fresh day highs in the 26.2 neighborhood, some active buyers have dragged USD/UAH to daily lows in the vicinity of 26.5.

We saw also the NBU increased interventions in the interbank foreign exchange market in order to build-up reserves. The central bank bought USD102.5mn during the last week, and has been actively intervening the market since beginning of this week.

In spite of such strong demand for USD, we expect UAH will hold positions by the end of the week on the back of stable export revenue inflow.

Banking liquidity restored to UAH100bn by the end of last week. According to the NBU the amount of cash deposited by banks at the central bank increased by 10% to UAH53.8bn as of May 31, while investments in CDs decreased by 5.22% to UAH49.6bn.

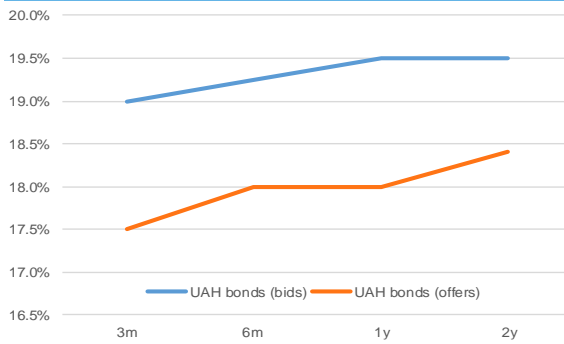
We saw autonomous factors continued to drain liquidity from the system, mainly through the cash channel, which represents salaries withdrawals from banks accounts. FinMin had a basically neutral impact on the system.

Figure 2. Banking liquidity (UAH bn)

Figure 3. Correspondent account balances (UAH bn)


The amount of liquidity restored due to central bank's monetary operations and FX interventions. The NBU provided a refinancing loan to three banks for a total amount of UAH6.6bn and was actively purchasing foreign currency in the interbank exchange market.

We expect banking liquidity will continue contracting by the end of the week as banks used to pile money in cash before prolonged holidays.

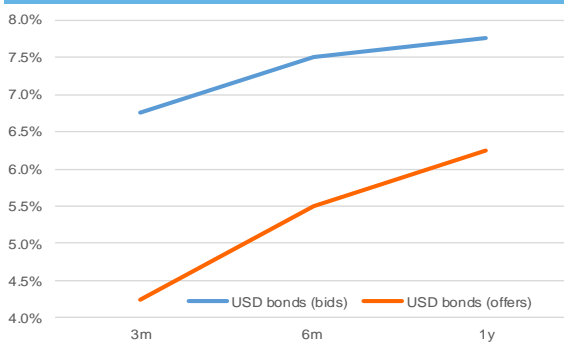
Figure 4. Local UAH bonds market



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	18.00%	17.95%	18.00%	17.90%	10	10	483.64	483.64
UAH	6m	18.39%	18.36%	18.50%	18.35%	14	8	1 166.72	500
UAH	1y	18.45%	18.45%	18.50%	18.45%	9	5	901.83	869.65
UAH	2y	17,95%	17,95%	17,95%	17,95%	11	11	1 362.23	1 362.23
UAH	6y	15.85%	15.84%	16.00%	15.70%	11	8	3 488.28	3 284.28
USD	10m	7.25%	7.25%	7.25%	7.25%	14	14	3.96	3.96
USD	1.5y	7.25%	7.25%	7.50%	7.25%	10	8	1.02	0.66

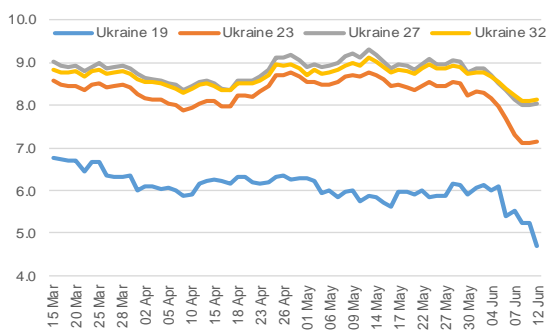
Figure 5. Local USD bonds market



FinMin attracted UAH6.6bn (equivalent) on the primary auction held on Jun 11. The highest demand was for brand-new 6y UAH bonds for UAH3.28bn, which were placed at 15.85%, and over the half of the securities were bought by nonresidents. Worth mentioning, that the ministry decided not to accept 3 applications for a total of UAH200mn, in which the rates reached 16%. FinMin also placed 2y securities for UAH1.36bn, 1y bonds for UAH0.9bn, 3m and 6m bonds for UAH0.5bn each. Compared with the auction a week ago, the ministry managed to slightly reduce the rate of placement of 6m and 1y bonds – respectively from 18.5% to 18.39% and from 18.5% to 18.45% per annum. As for the U.S. dollar-pegged papers, the rate remained at the level of 7.25% per annum, and the volume of placement fell to USD4.4mn.

This week FinMin is conducting meetings with investors in Europe about placement of 7y eurobonds denominated in euros. We expect these meetings will increase interest of foreign investors also to local government bonds.

Figure 6. Ukraine's Eurobond yields, bid/ask mid (%)



USD lost strength on week data

The U.S. dollar fell to a three-month low against the Euro since the mid of last week after weak private jobs data increased expectations of Federal Reserve interest-rate cuts in 2019. At the same time the ECB lent extra support to the European currency. The ECB did not sound as dovish as expected despite revising slightly lower its forecasts for inflation and economic growth in the region for the next years and after members discussed restarting QE or even cutting rates at the meeting.

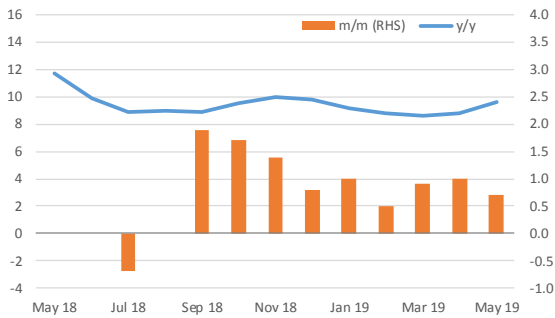
Since beginning of the week the dollar found some support after United States and Mexico reached a deal to avoid tariffs and U.S. president Donald Trump expressed optimism over making a trade deal with China. Though the rebound was limited as Trump again threatened to increase tariffs on Chinese goods if no agreement is reached.

Figure 7. EUR USD spot (mid)



10-year U.S. Treasury note rebounded to 2.126% after global trade concerns eased and investors looked toward riskier assets. However, on Wed resumed downward track after U.S. government report showed that prices consumers pay across the U.S. economy inched higher in May.

Figure 8. Consumer price index growth, %



Inflation back on downward pace, but new risks loom up

Inflation in Ukraine in May 2019 slowed down to 0.7% m/m after two-month growth, the UkrStat has reported. In annual terms, consumer price growth in May accelerated to 9.6% from 8.8% in Apr and 8.6% in Mar.

The smaller m/m increase in the CPI in May compared with Apr was mostly attributable to deceleration of growth of food and non-alcoholic products prices after a seasonal leap in early spring. An upside pressure on the index had transport segment, with m/m growth of fuel and lubricants prices accelerated to 4.1% in May from 2.7% in Apr and 0% in Mar. A 1.3% rise in prices for alcoholic and tobacco also contributed to the increase in CPI.

The y/y rise in the CPI in May is attributed to a statistical low-base effect.

In particular, last year there was a seasonal deflation of food and non-alcoholic beverages prices in May, while this year the growth still stays on positive side. Moreover, we are in doubt whether we have downside dynamic during summer months, taking into account a political uncertainty, which puts pressure on FX rates, and a worse weather conditions this year, comparing to the previous one, for ample supply of vegetables.

Mentioned in our previous inflation commentary risks for the next NBU's key rate cut, namely temporary acceleration of the CPI growth and a moderate progress in cooperation with the IMF, did take place and the central bank leaved its monetary policy unchanged on Jun 6.

The next meeting of the NBU's monetary policy committee will be held on Jul 18. Looking forward, we see new inflation risks have arisen and the key policy rate cuts is likely be kept unchanged again. Among these risks we point out the Russian government's decision to ban exports of oil and petroleum products to Ukraine from Jun 1, and the Ukrainian government's plans to launch a new electricity market from Jul 1.

According to the Ukrainian state officials, Russia has reduced shipments of oil products by 30-50% after the ban became effective. Taking into account a large share of Russia's oil products in the Ukrainian market (incl. around 40% of diesel fuel supplies), the embargo may cause further acceleration of fuel and lubricants prices.

Regarding launching of a new electricity market, so far we see there is no common understanding among its major stakeholders about readiness of the new model. We assume, such disaccord might signal to business community to revise its inflation expectations and, as a consequence, stimulate further price increase on wide range of goods and services.

At the moment we stick to our conservative year-end CPI forecast at 8.5%.

Figure 9. Main contributors to CPI m/m growth

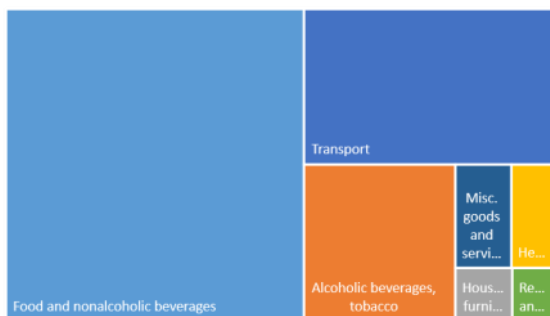


Figure 10. Main contributors to CPI y/y growth

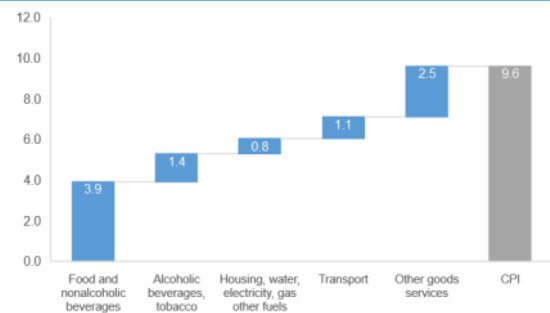
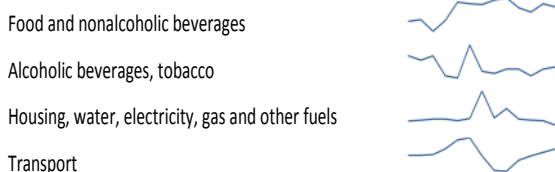


Figure 11. Main CPI components dynamic



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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