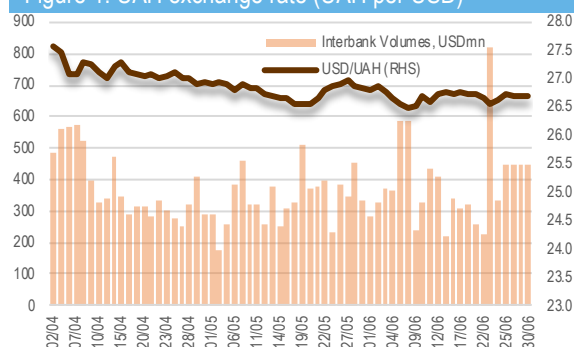
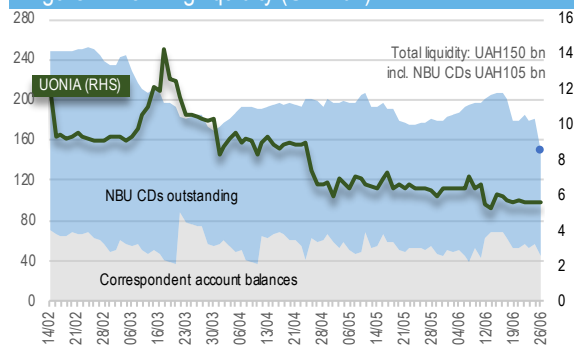


	Rating	Outlook	Last update	This week in focus: Ukraine's' BoP improving but risks are inside
Fitch	B	STABLE	22.04.2020	Ukraine's CA keeps running a surplus as consumer and energy related imports showed higher vulnerability to the pandemic implications than commodity exports. FA also performed well, with official funding from IFI's to be complemented by freshly printed Ukraine Eurobond. Mid-term outlook for balance of payments is clouded by resignation of NBU management.
S&P	B	STABLE	13.03.2020	
S&P (N)	uaA	-	13.03.2020	
Moody's	B3	STABLE	12.06.2020	

Figure 1. UAH exchange rate (UAH per USD)

FX and interest rates: UAH again trades in a sideways manner against USD

The USD/UAH pair returned in a familiar trading range as speculative forces weakened. The pair continue showing some resilience around 26.7 figure, and last week gained some positive traction on the back of increased FX supply from exporters and state owned company Naftogaz for the subsequent payments to the State treasury. Though most of the Naftogaz's foreign currency injections were consumed by the National bank of Ukraine (NBU), some amounts did appeared on the marked and had its impact on the pair movement.

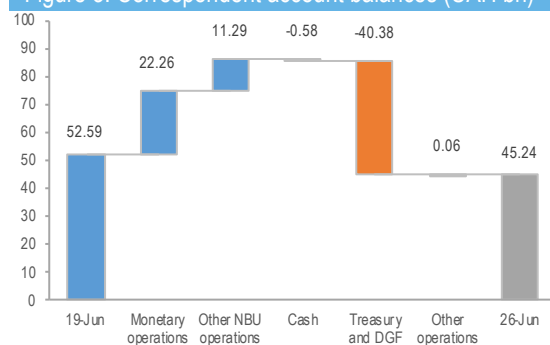
Being extensively supplied with FX, the NBU last week increased volume of interventions in the interbank market by 3.9 times to USD424.5mn.

Figure 2. Banking liquidity (UAH bn)

The second half of the year usually starts with declined trading volumes.

Though this year the COVID outbreak does not allow for setting the usual summer lull, many businesses in this period embark on revising their annual budgets, market forecasts and assumptions. The market becomes more vulnerable to speculative movements and we might see some downside pressure on the hryvnia against rising fears about a growing number of coronavirus cases.

The resignation of Yakiv Smolii as governor of the NBU is another source of uncertainty, that might increase volatility in the market.

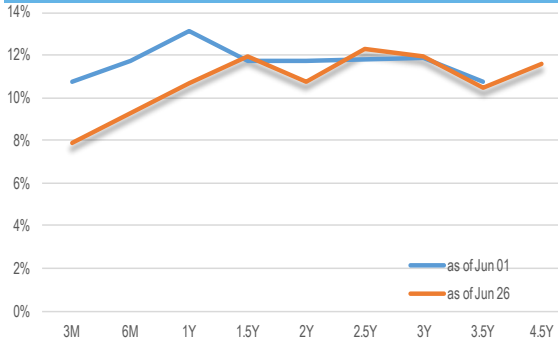
Banking liquidity last week dropped to UAH150bn from UAH200bn seen two weeks ago (June 17). The sharp change has mostly to do with large-sum annual dividend payments by the state-owned PrivatBank and Naftogaz. Together with seasonal taxes, total outflow to the state treasury amounted to more than UAH60bn. The way these funds will be redistributed by the government might set a trend for FX rate and inflation development in 2H20.

Figure 3. Correspondent account balances (UAH bn)


The central bank's FX interventions were the major source of fresh UAH liquidity. In turn, monetary operations largely represent reallocation of funds from NBU certificates deposits to correspondent accounts. As a result, total funds held in central bank's deposit facilities contracted to UAH105bn.

Note, that **the NBU has substituted the Ukrainian index of interbank rates (UIIR) with Ukrainian Overnight Index Average (UONIA).** The new indicator is calculated since 23rd of June. The preceding values starting from 2019 have been calculated retrospectively. According to the NBU, the UONIA index fully complies with IOSCO's principles regarding financial indicators.

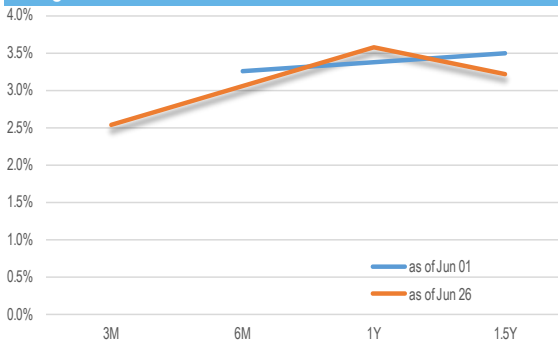
Figure 4. Local UAH bonds market



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	7.24%	7.24%	7.24%	7.24%	3	3	800.93	500.00
UAH	6M	7.74%	7.74%	7.74%	7.74%	2	2	800.00	500.00
UAH	9M	-	-	-	-	-	-	0.00	0.00
UAH	1Y	0.00%	0.00%	10.00%	10.00%	2	0	600.00	0.00
UAH	1.5Y	10.40%	10.39%	10.49%	10.29%	6	5	289.30	239.30
UAH	2.5Y	10.47%	10.47%	0.00%	0.00%	1	1	5.00	5.00

Figure 5. Local USD bonds market

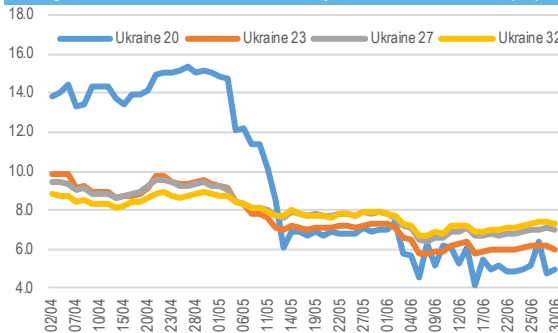


FinMin faced resistance in yield movement. Another primary debt auctions by the Finance Ministry received a tepid demand, discouraging the issuer from further aggressive rates cuts for government bonds. The ministry offered solely local currency bonds with tenor ranging from 3 months to 2.5 years.

The highest demand was seen for short-term 3m and 6m bonds, proposal of which as usual is limited at UAH500mn each. Yet, if compared with previous auctions, the bid-to-cover ratio, the ratio of the total amount of bids and the amount of new debt allocated, declined to 1.6 from respectively 1.85 and 2.15 seen at the previous auctions. As a result, cut-off rates and average rates for the securities remained at 7.24% for 3m bonds and 7.74% for 6m ones.

The rest of securities barely attracted attention at current yields. The ministry refused to place 1y bonds for UAH600mn at 10%, which it sold at 9.7% a week ago, and there was no demand for 9m bonds. For comparison, secondary market looks more generous, registering deals in bonds with similar tenor at yields exceeding 10.7% per annum.

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



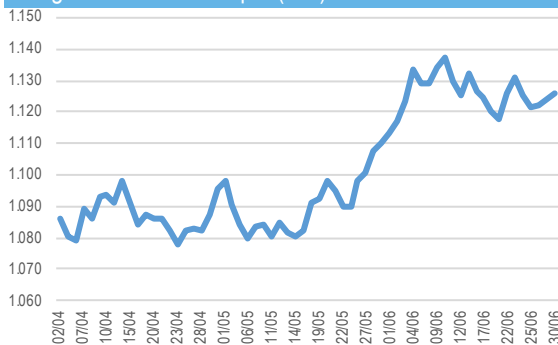
EUR/USD seesaws in a choppy range around 1.125

The EUR/USD pair has been showing some two-way price moves since our latest report (June 17) in the wide range between the 1.118 and 1.13 levels. Concerns over coronavirus cases around the world were the main factor behind the markets swings for the best part of this time, driving flows to and from safe haven currencies.

Incoming statistics signaled about gradual recovery in major global economies from the shock caused by the coronavirus pandemic, with China, U.S. and Eurozone revealing positive stats on manufacturing activity.

Besides, U.S. President Donald Trump assured markets, saying the Phase 1 trade deal struck with China in January remains fully intact.

Figure 7. EUR USD spot (mid)

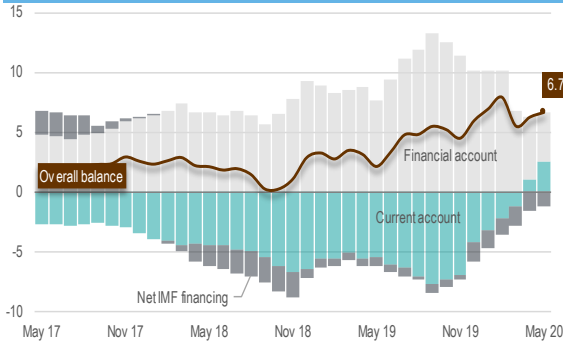


Across the pond, the ECB said it will offer euro loans against collateral to central banks outside the euro area to backstop funding markets amid the coronavirus pandemic

Looking at the fixed income markets, normally Treasury yields would rise due to an improving economy, but **benchmark 10-year yields have moved in a narrow range around 0.65% since mid June, when Federal Reserve Chairman Jerome Powell said policymakers discussed yield curve control, which can be used to cap bond yields.**

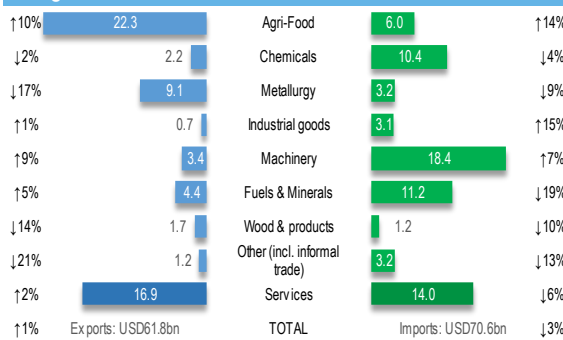
Figure 8. Cumulative balance of payments, USDbn

Ukraine's' BoP improving but risks are inside



Ukraine's current account (CA) keeps running a surplus as consumer and energy related imports showed higher vulnerability to the pandemic implications than commodity exports. Financial account (FA) also performed well, with official funding from international financial institutions (IFIs) to be complemented by freshly printed Ukraine Eurobond. Mid-term outlook for balance of payments is clouded by resignation of NBU management.

Figure 9. Cumulative trade balance breakdown, USDbn

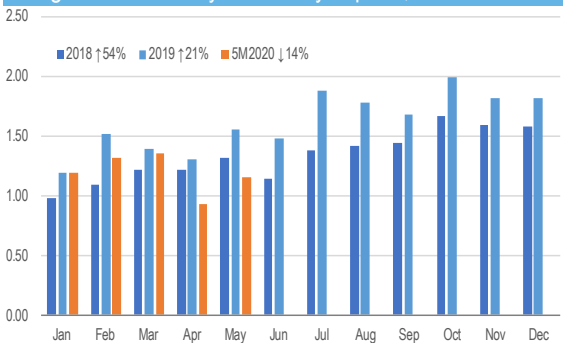


A passing improvement. The National Bank of Ukraine said on Tuesday that the trade balance (goods and services) in May second straight month landed in a surplus, with total exports exceeding imports by USD373mn. Agri-food exports and saved costs for energy commodities were the major contributors to the improvement. Sustainable sales of services, mainly benefiting from the favorable gas transit deal struck between Ukraine's Naftogaz and Russian Gazprom in late 2019, were also supportive.

Steel and mining export sales remain subdued and is likely to keep contracting amid expected slowdown in global industrial activity.

Meantime, machinery imports tumbled 25.4% y/y in May after 28.6% y/y drop in April. Extensive cuts in capex amid the novel coronavirus outbreak, largely driving the figure down, can make much of a dent on economic recovery in 2021. The government fiscal policy stimulus still falls short of business needs, while reform agenda seems to be relegated to the background on the pretext of fighting the pandemic.

Figure 10. Monthly machinery imports, USDbn

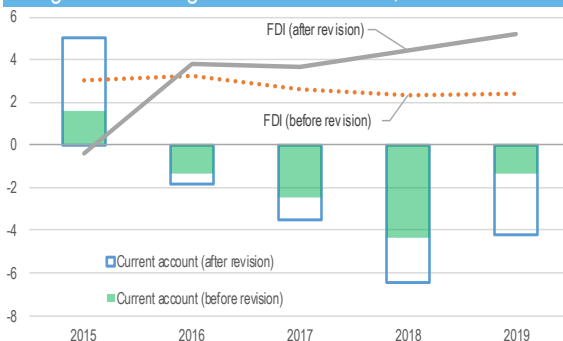


Financial account stats lag news flow. Though financial account saw another USD1.2bn outflow in May after USD2.1bn drain in April, the recent IMF deal and followed up financial support from other IFI's should have reversed the flow in the next reporting period. Moreover, yesterday's announcement by FinMin of a fresh 12-year Eurobond print might result in additional USD1bn inflow in July.

The debt deal came earlier than we expected (see report of June 17). On the one hand, fast-changing investment sentiment on fresh coronavirus figures does not allow for flexible timing of tapping into the debt market.

On the other hand, improved foreign cash position might incentivize the authorities to postpone with implementation of IMF's requirements. Announced on Wednesday's evening Ukraine's central bank governor resignation due to continuous political pressure supports the case.

Figure 11. Foreign direct investments, USDbn



Continued NBU independence is among the four priorities of the new IMF bailout. Though the central bank's board is going to hold positions in order to safeguard macrostability, the departure of Yakiv Smolii as governor is a serious blow and treat to further cooperation with the Fund.

NBU has revised approaches to calculating foreign direct investments (FDI). In particular, attributable to direct investors retained earnings were added to both primary income in the capital account and foreign direct investments inflow in the financial account, entailing no effect on the balance of payments. As a result of the new calculations, FDI outflow in 1Q20 amounted to USD1.6bn versus USD560mn inflow estimated previously and the current account's balance was revised up by circa USD1bn.

Data for FDI was revised to show the real impact of funds reinvested, according to the central bank. The NBU specifies, that reinvested earnings under new approach account for circa 50% of FDI, which correspond to the average level among foreign countries.

We put our forecast for CA and FDI under revision.

UKRAINIAN CAPITAL MARKETS WEEKLY

Key Macroeconomic Indicators								
	2014	2015	2016	2017	2018	2019	2020E	2021F
Real sector								
Real GDP (%YoY)	-6.6	-9.8	2.4	2.5	3.4	3.2	-4.5	3.8
Industrial production (%YoY)	-15.0	-5.1	6.6	-0.5	1.1	-6.7	-1.8	0.0
Retail sales (%YoY)	-11.0	-25.0	4.0	8.8	6.2	10.5	-10.9	9.2
Unemployment rate end of year (ILO, working age)	9.3	9.1	9.3	9.5	8.8	8.2	10.1	9.3
Nominal GDP (UAH bn)	1 587	1 989	2 385	2 983	3 559	3 975	4 117	4 633
Nominal GDP (USD bn)	131	90	93	112	131	154	144	154
Prices								
CPI (average %YoY)	12.1	48.7	16.5	14.4	10.5	7.9	6.0	5.5
CPI (end of year %YoY)	24.9	43.3	12.4	13.7	9.8	4.1	7.5	6.0
Real average wage growth (%YoY)	-6.5	-35.0	10.0	18.9	9.7	9.8	-5.5	3.5
Fiscal balance (% of GDP)								
State budget deficit (without Naftogaz)	4.9	2.3	2.9	1.6	2.4	1.8	7.5	3.0
Total public debt (% of GDP)	69.4	79.4	81.0	71.8	61.0	51.6	64.4	64.6
External balance								
Exports of goods and services (USD bn)	65.4	47.9	46.0	54.0	59.0	63.4	50.5	55.6
Imports of goods and services (USD bn)	70.0	49.6	51.8	60.8	70.5	75.5	59.5	66.6
Current account balance (USD bn)	-4.6	1.6	-1.3	-2.4	-4.7	-1.1	-1.0	-2.1
Current account balance (% of GDP)	-3.4	1.8	-1.4	-2.1	-3.3	-0.7	-0.7	-1.3
Net FDI (USD bn)	-0.3	3.0	3.3	2.6	2.4	2.5	1.0	3.5
Foreign exchange reserves (end of year)	7.5	13.3	15.5	18.8	20.8	25.3	23.5	26.5
Imports coverage (months of imports of goods)	1.5	4.4	3.7	3.6	3.4	3.9	4.7	4.8
Interest and exchange rates								
NBU discount rate (% end of year)	14.0	22.0	14.0	14.5	18.0	13.5	6.0	5.0
Exchange rate (UAH/USD) end of year	15.8	24.0	27.2	28.0	27.7	23.7	29.5	31.0
Exchange rate (UAH/EUR) end of year	23.0	26.2	28.3	33.5	31.8	26.4	33.0	34.7

Note: Figures on current account (CA) and foreign direct investments (FDI) to be updated.

Two Weeks Ahead

Mon	Tue	Wed	Thu	Fri	Sat	Sun
29.06.2020	30.06.2020	01.07.2020	02.07.2020	03.07.2020	04.07.2020	05.07.2020
	Ukrstat: Nominal & Real Wage NBU: Balance of Payments NBU: Direct Investments					
06.07.2020	07.07.2020	08.07.2020	09.07.2020	10.07.2020	11.07.2020	12.07.2020
	NBU: FX Reserves (deadline - 7th day)		Ukrstat: Price Indexes	NBU: Monetary Statistics (Preliminary)		



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