WEEK IN REVIEW

November 7, 2017

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FOCUS

WEEK INSIGHT

The Week in Review showed the increasing political tension in the country negatively impacting upon the standing of the public sector, as well as upon the global positions of the country.

The nine-month Interim corporate reports witness about the beneficial outcome of the economic recovery on business results. Banks have consolidated their position thanks to the dynamically strengthening economic sectors. In the meantime, the economic sectors most highly exposed to the eastern Ukrainian conflict continued dragging the respective businesses down.

The overall external balance sees business development to be restrained by a complicating political and regulatory environment, especially ensuing from the delay in the implementation of critical reforms.

Moreover, the sluggish domestic development has restrained the ability of businesses and the country’s economy to fully benefit from the supportive global trade environment.

The current pattern may likely endure through the quarter, considering the signs of a new round of political bargaining at the top level of the country’s governance.

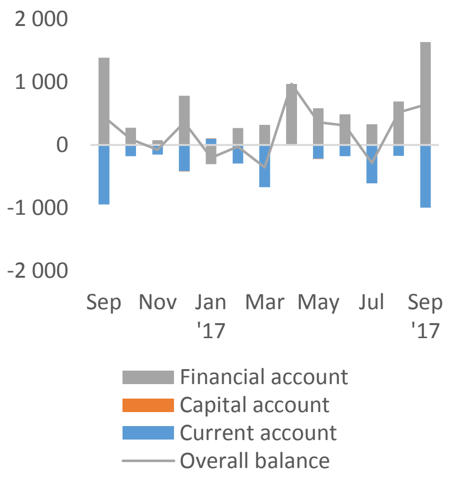
POLITICS

Ukraine gained four positions in the Doing Business 2018 ranking, ranking 76th among the 190 economies studied by the World Bank. The country advanced 105 positions as to the issue of obtaining construction permits, 41 positions for "tax payment," 2 in terms of "connection to power grids" and 1 in terms of "settlement of insolvency." In the meantime, the country lost 32 positions on the issues of creating new companies, 11 positions on protection for minority shareholders, 9 positions in the ease of obtaining loans, 4 in the ease of international trade and 1 in the ease of registering property and enforcement of contracts. ***The Government has been decisive in its efforts at improving the country’s ranking. Nevertheless, the overall result reflects improvement in the overall operational environment, however leaving open the issues of investment policy. A positive development in the latter highly depends upon comprehensive judiciary and law enforcement reforms, which have lately become a matter of contention. The country’s ranking will however come under pressure from the starting long electoral campaign of 2018-2019.***

ECONOMY

On October 27, 2017, Fitch Ratings affirmed Ukraine's Long-Term Foreign- and Local-Currency Issuer Default Rating (IDR) at 'B-' with a Stable Outlook. At the same time, the rating agency affirmed the country’s Short-Term Foreign- and Local-Currency IDR at 'B'. The Country Ceiling is affirmed at 'B-'. Fitch affirmed the country’s senior unsecured bonds at 'B-'. The rating assessment reflects Ukraine's weak external liquidity, a high public debt burden and structural weaknesses, in terms of a weak banking sector, institutional constraints and geopolitical and political risks, according to the rating report. In the meantime, the rating agency notes the country’s improved policy credibility and coherence, the sovereign's near-term manageable debt repayment profile and a track record of bilateral and multilateral support. Near-term financing risks are limited thanks to debt restructuring and active debt management policy. Fitch expects the current account deficit to increase to 4.1% of GDP in 2017 and average 4% in 2018-2019. Inflation will average 12.9% in 2017, however, it is seen to decline gradually and average 7.8% in 2019. Fitch forecast growth at 2% for 2017 and expects Ukraine to accelerate to 3.2% and 3.7% in 2018 and 2019, respectively, driven by domestic demand. Ukraine will record a lower general government deficit (2.7% of GDP) than peers (4.7%) in 2017. Fitch expects deficits to average 2.8% of GDP in 2018-2019. On the back of primary surpluses, reduced financial sector outlays and moderate FX depreciation, Fitch forecasts general government debt to peak at 71.5% of GDP (83.3% including guarantees) in 2017, and to decline, for the first time since 2007, to 67.3% in 2018. Fitch expects neither resolution of the conflict in eastern Ukraine nor escalation of the conflict to the point of compromising overall macroeconomic performance. ***The rating assumptions stress the remaining gap between the benchmarking group and Ukraine's achievements. Despite improving general economic and debt conditions, the country's rating is restrained by lack of progress in fixing the structural imbalance and institutional weaknesses of its financial system, i.e. banking and public finances.***

Balance of Payments, USD BN



Ukraine's current account deficit amounted to USD 3.0 BN in 9M2017 (3.9% of GDP), increasing by 12.7% y/y, according to NBU preliminary data. The export of goods grew by 20.7% y/y to USD 28.8 BN over the period, mostly at the account of export to the EU (+31.3% y/y or +USD 2.4 BN) and to Asia (+11.5% y/y or USD 950 MN). In the meantime, imports of goods marked a strong growth of 21.9% y/y to USD 34.7 BN. The EU has increased its share out of Ukraine's total export from 32.4% to 35.2%, while its share of imports grew from 36.7% to 37.6%. A gradual increase in the trade with Russia took place over the period, seeing the country's exports growing by 16.1% y/y and imports by 34.6% y/y. Meanwhile a net inflow of USD 4.9 BN is recorded in nine months, representing a growth of 37.7% y/y. Foreign direct investments declined by 35.8% y/y to USD 2.0 BN, mostly made of debt to equity swap. The Central Bank notes a reduction in the volume of off-bank foreign currency by 47.3% y/y to USD 2.2 BN. The surplus of the country's balance of payment increased by 96.6% y/y and amounted to USD 1.9 BN in January-September. ***A stronger increase in imports of energy resources in compensation of the lost supplies from the breakaway territories of Eastern Ukraine and investment goods offset the gains from the supportive global trade environment (agricultural and metal), therefore conditioning the deeper current account deficit. The deepening trade deficit was largely offset by foreign borrowing of the Government on background of limited inflow into the corporate sector. A further improvement in the trade relations with Russia is conceivable in the medium-term, generating support to the trade and payment balance. Overall, however, no substantial improvement in the trade and payment balance is to be expected given the growing country risk coming from the starting electoral campaign and the remaining uncertainties with economic and regulatory reforms.***

AGRICULTURE

On October 30, 2017, Avangardco Investments Public Limited (AVG or Avangard) warned the holders of its Eurobonds due in 2018 that the interest payment on the notes scheduled for October 30, 2017 is not to be executed. Avangard and its UkrLandFarming PLC ("ULF") parent company, together with their advisors, Latham & Watkins LLP and Ziff-Ivin Associates Ltd, are negotiating a restructuring of the interest payments with an ad hoc committee of the bondholders, according to Avangard. Hogan Lovells International LLP and Ernst & Young LLC act as advisor to the committee which represents the holders of approximately 50% of the AVG and 40% of ULF's notes, the statement reads. The negotiation on the interest payment stems from the overall discussion concerning the potential restructuring of the company's debt including the notes, according to the Company. ***Though unveiling existing liquidity pressure on the company and the group, the announcement could be considered a technical measure stemming from the ongoing debt reprofiling negotiations***

between the group and its creditors. Nevertheless, the development still shows the group in a dim light compared with its more successful competitive peers in Ukraine. Overall, a recovery of the group from its current distressful state its functional upon a revision of the business strategy and market positioning.

INDUSTRIALS

On November 2, 2017, Metinvest B.V. (Metinvest or the Group), the parent company of a vertically integrated group of steel and mining companies disclosed its operational results for 3Q2017 and 9M2017 ended September 30, 2017. In 9M2017, crude steel production fell by 10% y/y and amounted to 5.7 Mt, iron ore concentrate by 11% y/y to 20.4 Mt, and coal concentrate by 13% y/y to 2.0 Mt. In the metal segment, Yenakiieve Steel predominantly drove hot metal production down, offsetting growth in the company's remaining production facilities throughout the country. Overall, a strong decrease in the output for railway and long products conditioned the decline in this production segment. In 9M 2017, the overall output of merchant semi-finished products climbed by 15% y/y, whereas the production of finished products decreased by 11% y/y. The company reported an increase in coke output by 3% y/y to 3.4 Mt. In the mining segment, the production of iron ore concentrate dropped by 11% y/y to 20.4 Mt. ***The interim Report shows the Company struggling against the negative impact of the asset losses in the breakaway territories of Donbas and the production disruption caused by the war in the facilities located in the conflict zone. Additionally, the sluggish economic recovery restrains the Company's activities on the domestic market. With global markets seen to remain supportive and the country's economy to recover, further spurring demand, Metinvest should benefit from its current policy of redistributing the production mix towards the facilities located in the safer areas of Ukraine.***

BANKING AND FINANCES

The net profit of the State-owned Oschadbank (Kyiv) increased by 9.3% y/y in January-September 2017 and amounted to UAH 448.7 MN, according to the interim report of the bank. Net interest income expanded five-fold to UAH 2.7 BN, while net income from fees and commissions grew by nearly 30% y/y to UAH 1.9 BN. Oschadbank reported a net profit of 909.7 MN from foreign currency transactions, emerging from a UAH 2.3 BN FX loss in January-September 2016. The bank's Assets were up 5.2% y/y to UAH 221.6 BN, with the loan portfolio growing by 6.9% y/y to UAH 70.4 BN. Oschadbank's liabilities increased by 4% y/y to UAH 150.9 BN. ***The interim report witnesses about the bank's successful transformation. Especially notable are the improvements in the loan portfolio quality and in business segmentation, as well as the bank's reduced exposure to government bonds and public companies, including the Naftogaz oil and gas monopoly. The bank has managed to strengthened its positions in the dynamically growing economic sectors of Ukraine, while realigning its costs to the market environment. The bank has also benefitted from its strong ties with local communities, which contributed to additional cheap funding.***

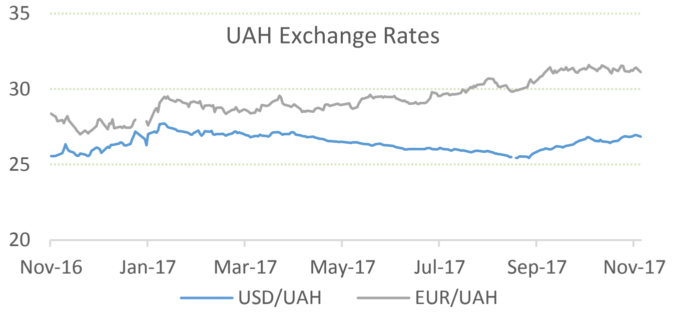
PrivatBank (Kyiv), which was nationalized in December 2016, reported a net loss of UAH 1.6 BN in January-September 2017, plunging from a net profit of UAH 592 MN in the corresponding period of the previous year, according to the interim report of the bank. Interest income grew by 43.8% y/y to UAH 4.9 BN, however leaving a net interest loss of UAH 2.2 BN after reserve provision, compared with a net interest income of UAH 2.7 BN in the corresponding period of the previous year. Net income from fees and commissions grew by 23.4%, to UAH 7.0 BN. Privatbank's assets expanded by 23.5% y/y, to UAH 253.3 BN, including a rise in loan portfolio by 9.3% y/y to UAH 47.6 BN. Acquisition of securities in the tune of UAH 32.2 BN mostly contributed to asset growth. The bank's deposit portfolio grew by 11.9% y/y, to UAH 202.6 BN, while the total liabilities of the bank increased by 12% y/y to UAH 202.7 BN.

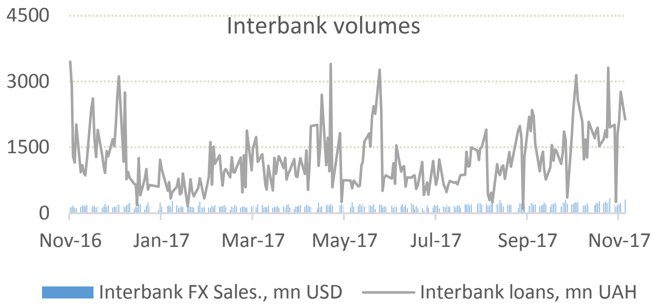
Meanwhile, on October 27, 2017 the National Bank of Ukraine (NBU) approved the changes in the structure of PrivatBank. The changes, withdrew SIA PrivatLizings (Latvia), Privatofice LLC (Dnipro), UK SPV Credit Finance PLC (UK) and Ukraine Mortgage Loan Finance No.1 Plc (UK) from the corporate structure of the bank, leaving only 10 entities in the Group. Therefore, Privatbank Group currently consists with PJSC commercial bank PrivatBank, AS PrivatBank, SIA PrivatConsulting, SIA Privat Investment, SIA Amber Real (Lativa), PrJSC Kobos, Ukrainian Credit Histories Bureau LLC (Kyiv), Estategarant LLC, LT Group LLC, and A-Lex law firm (Dnipro).

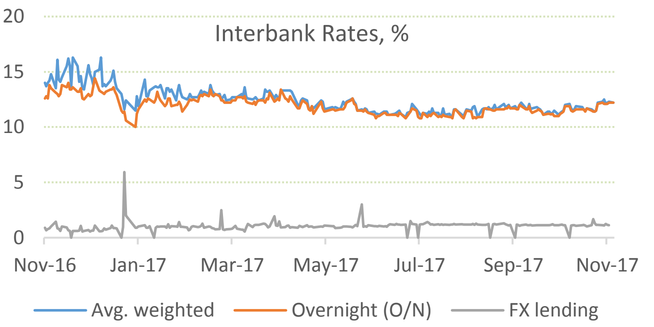
On November 1, 2017, Fitch Ratings upgraded the Long-Term Foreign Currency Issuer Default Rating (IDR) of PJSC CB PrivatBank (Privat) to 'B-' from 'RD' (Restricted Default), Outlook Stable. Additionally, the rating agency upgraded the bank’s Long-Term Local Currency IDR to 'B-' from 'CCC', Outlook Stable. The Short-Term Foreign Currency IDR was upgraded to 'B' from 'RD'. Fitch warns about potential risks to capital from the litigation claims of the bailed-in senior creditors of the bank in an approximate volume of USD 390 MN. Non-performing loans (NPLs) equaled 88% of gross loans at end-1H17 and largely included a stock of legacy exposures issued to formerly related parties. It will take the bank time to originate higher-yielding assets (loans) and reduce deposit rates, which are necessary steps to achieve a reasonable level of profitability, according to Fitch estimations.

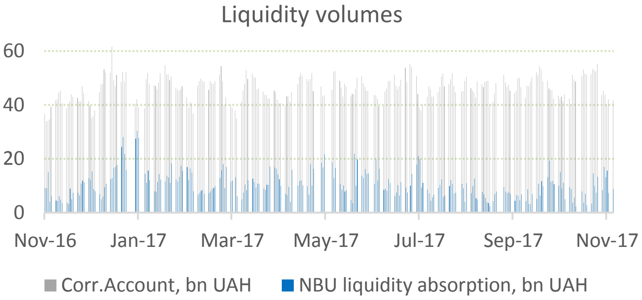
The interim results show the bank to continue struggling to rehabilitate its lending portfolio. Moreover, Privatbank still failed to design a new business model after its nationalization and has increased its exposure to government bonds. A notable escalation of the standoff between the bank, its former shareholders and creditors leaves the medium term outlook of the bank under question.

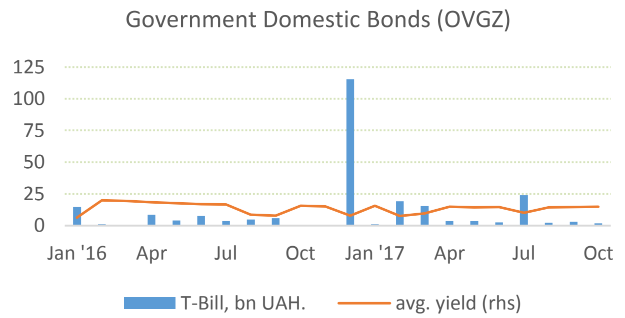
MARKETS

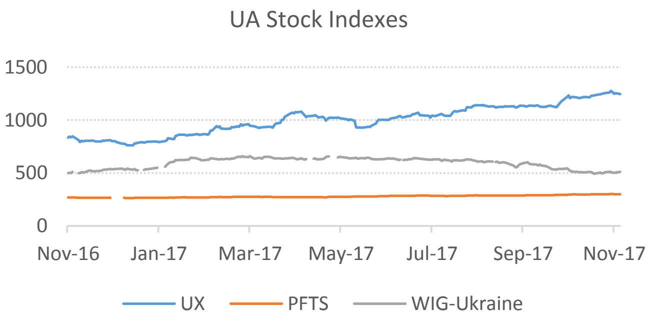


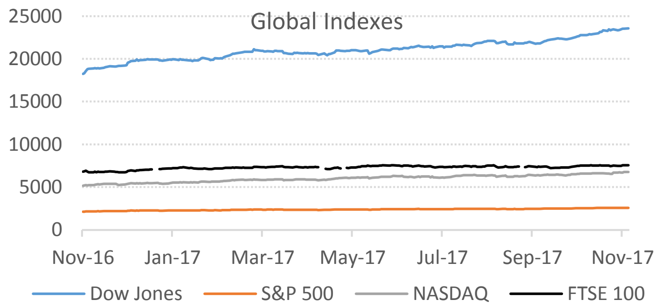


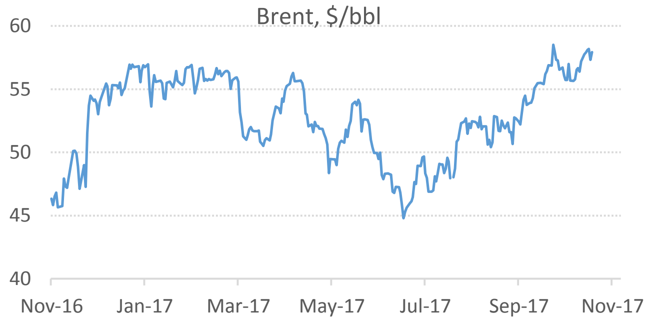


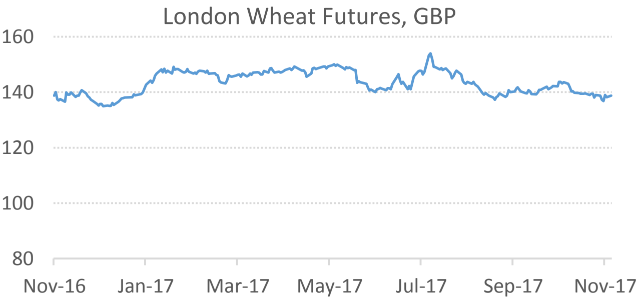












Sources: NBU; State Statistics Service of Ukraine; UX; PFTS; WSE; LSE; NASDAQ; NYSE:ICE; InvestFunds/CBonds

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