

Trends

Quotes for Ukraine's sovereign Eurobonds moved higher last week following the IMF's statement supporting the policies implemented by the government and the National Bank with the aim of bolstering the country's economy. The low budget deficit, the reduction of the country's Debt-to-GDP ratio, low inflation, and the accumulation of foreign currency reserves are all results of good policy and are important prerequisites for economic stability and growth, the IMF said. The Ukrainian government has a new preliminary 3-year loan program worth USD 5.5bn with the IMF, but Kyiv still needs to meet some requirements to receive the initial tranche payout, including the adoption of a number of laws by Parliament.

The longest outstanding Ukrainian sovereign bonds with maturity in 2032 gained 1.1% to 109.1/109.8 (6.3%/6.2%), and medium-term benchmark Ukraine-24s added 0.6% to 110.8/111.5 (6.0%/5.8%). The VRI derivatives (linked to Ukraine's future GDP growth with expiration in 2040) rose by 1.1% to close at 99.5/100.5 cents on the dollar, despite surprising comments from the Finance Ministry that 2021 payout conditions for the papers haven't been met, after Credit Suisse advised clients to take a closer look at these sovereign warrants.

In the corporate universe, Metinvest-29s rose by 1.1% to 104.8/105.8 (6.4%/6.3%), ignoring negative news that the Ukrainian Parliament passed a bill that raises the iron ore production tax from 8% to 12%. DTEK-24s picked up 1.3% to 103.1/104.1 (8.8%/8.5%) and MHP-26s added 0.5% to 104.0/105.0 (6.3%/6.1%).

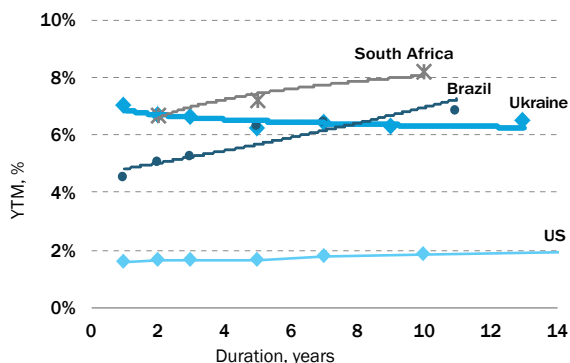
Banking issues were less active than sovereigns, with OschadBank-25s inching up by 0.2% to 102.8/103.8 (7.7%/7.0%) and UkrEximBank-22s increasing by 0.4% to 103.7/104.7 (6.6%/5.7%).

The yield on the government's 1-year UAH-denominated treasuries dropped by an impressive 150 bps to bid/ask of 12.00%/10.00% YTM after the Finance Ministry placed new 1-year domestic treasury issues at 10.44% on Tuesday (Jan 14), and 4-year bonds were placed at an even lower rate of 10.10%, continuing the inversion of the sovereign domestic yield curve.

The hryvnia experienced notable pressure for the second week in a row, devaluing by 1.8% against the dollar to 24.34 UAH/USD.

You can receive additional details about developments in Ukrainian fixed income from the Eavex Sales Team at research@eavex.com.ua.

SOVEREIGN BOND YIELD CURVES



Source: Bloomberg, Eavex Capital

FIXED INCOME

	Last	1W ch	YTD
NBU Key Rate	13.5%	0.0 p.p.	0.0 p.p.
UAH 1-year bond	12.0%/10.0%	-1.5 p.p.	-2.5 p.p.
Ukraine-2024	6.2%	-0.4 p.p.	-0.4 p.p.
Ukraine-2028	6.5%	-0.5 p.p.	-0.5 p.p.

CURRENCY

	Last, UAH	1W chg.	YTD
USD/UAH	24.34	1.8%	2.7%
EUR/UAH	27.02	1.1%	2.3%

Source: Eavex Capital

Highlights

- > Zelenskiy Refuses Honcharuk Resignation After Leaked Audio Scandal
- > MinFin Claims Triggers for Ukraine's VRI Payouts Haven't Appeared

Zelenskiy Refuses Honcharuk Resignation After Leaked Audio Scandal

by Will Ritter
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NEWS

President Zelenskiy on Saturday (Jan 18) refused the resignation of his hand-picked prime minister, Oleksiy Honcharuk, following leaked audio recordings in which the PM had made comments downplaying Zelenskiy's, and his own, understanding of economic issues. Honcharuk had offered his resignation on Friday morning (Jan 17). On the tapes, Honcharuk is heard using the words "incompetent" and "primitive" to describe his and Zelenskiy's economic knowledge. Zelenskiy has ordered security agencies to find out within two weeks who made the audio recordings, which appeared to have been edited and spliced together from different meetings to change the context of the statements.

COMMENTARY

We agree with the general consensus that Honcharuk's remarks were rather innocuous and blown out of proportion. We note that the Ukrainian and Russian word "necompetent" used by Honcharuk has a softer meaning than the direct English translation, and is more correctly translated as "not skilled" or "not experienced". As such, we believe that Honcharuk's resignation offer was merely a symbolic display of loyalty to Zelenskiy meant to defuse other, non-public tensions between the President and the Cabinet of Ministers, which has now been in office for just under 5 months. In general, we see 2020 as being a year in which political realities begin to catch up with Zelenskiy as his aura as a made-for-TV president fades and he becomes bogged down with the real-life grind of his office. After he initially handled the PS 752 airline disaster in Iran with impressive grace, questions have emerged about what Zelenskiy was actually doing in the small Middle Eastern kingdom of Oman at the time of the crash. Arthur Gerasimov, the head of the opposition European Solidarity faction in Parliament, claimed that Zelenskiy had held secret meetings with Russian officials there regarding the occupied Donbass territories, a charge denied by top presidential aide Andriy Yermak. The President has provided the rather weak-sounding explanation that he was on a private trip at his own expense. In either case, this story is negative, as Zelenskiy holding secret talks with the Kremlin in Oman would be a gigantic scandal, while if the charge is untrue, it shows the unscrupulous lengths to which opposition forces aligned with former President Poroshenko are willing to go to in order to undermine the standing of the new President.

MinFin Claims Triggers for Ukraine's VRI Payouts Haven't Appeared

by Dmitry Churin
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NEWS

The conditions that launch payments on Ukraine's "value recovery instruments" (VRIs), a security that was issued to compensate for the write-down on Ukrainian Eurobond debt in 2015, have not occurred, Finance Minister Oksana Markarova has said, news agency Interfax reported on Jan 16.

The Finance Ministry and the Cabinet of Ministers are discussing a strategy to handle the VRIs, which require Ukraine to make annual payments to holders of the papers in the case when yearly GDP growth is above 3%, Markarova said, without providing specifics.

The VRIs were issued as part of the restructuring of the public debt in 2015 in exchange for Eurobonds with a nominal amount of USD 3.2bn and are not currently counted as part of the national debt. Payments on the VRIs will be made annually in cash in US dollars, depending on the dynamics of growth of Ukraine's real GDP in 2019-2038, however, with a lag of two calendar years - that is, between 2021 and 2040.

The VRI mechanism begins to operate only if Ukraine's GDP reaches USD 125.4bn. The amount of the payments depends on GDP growth dynamics: at of 3% and below, no payments are due; from 3% to 4% they will amount to 15% of each percent of GDP growth exceeding 3%; from 4% they will be 40% of each additional percent. In addition, from 2021 through 2025 the payments are limited by 1% of GDP, but are uncapped from 2026 to 2040.

COMMENTARY

The payouts on the VRIs are potentially enormous - in the tens of billions of dollars - and far beyond the par value of the papers. Therefore, there has been considerable speculation that the Ukrainian government will try to buy the securities back to avoid such payouts. In this context, it is not surprising that MinFin would be trying to talk down the value of the VRIs. However, in our view, Markarova's statement regarding the VRIs is incorrect, as we see that both of the conditions to needed to trigger the first VRI payments in 2021 have been met. The first one is that nominal GDP has risen above USD 125.4bn. Our preliminary assessments implied that Ukraine's nominal GDP was near USD 150bn in 2019. We also believe that real GDP growth in the period was 3.3% YoY. The reported GDP growth for 9M19 was 3.7% YoY. This means that unless economic growth slowed to below 1% YoY in 4Q19 after the impressive rise of 4.1% YoY in 3Q19, the full-year figure will indeed activate the VRI payment mechanism. The bottom line here is that according to our estimates, Ukraine will need to pay the VRI holders USD 68mn in 2021, which would imply a 2% nominal return for the VRIs. The papers are currently traded very close their par value.

Ukraine's VRIs soared in value in 2019 amid the hopes that the government will quickly repurchase them to prevent large future payments, which as noted above will be uncapped after 2025. They are now quoted at 99 cents on the dollar, up from just 57 cents at the start of 2019.

SELECTED UKRAINIAN EURO BONDS										
Issue	Price Bid	Price Ask	Price ch., W/W, %	YTM Bid, %	YTM Ask, %	Coupon	Maturity Date	Volume USD mn	Currency	Ratings ¹
Sovereign Eurobonds										
Ukraine, 2020	99.9	100.4	-0.1%	8.1%	7.2%	7.75%	1 Sept 2020	1,365	USD	Caa1/B/B
Ukraine, 2024	110.8	111.5	0.6%	6.0%	5.8%	7.75%	1 Sept 2024	1,339	USD	Caa1/B/B
Ukraine, 2028	123.3	124.0	1.1%	6.3%	6.3%	9.75%	1 Nov 2028	1,600	USD	Caa1/B/B
Ukraine, 2032	109.1	109.8	1.1%	6.3%	6.2%	7.38%	25 Sept 2032	3,000	USD	Caa1//B
Ukraine, GDP-linked	99.5	100.5	1.5%			0.00%	31 May 2040	3,214	USD	/B/
Corporate Eurobonds										
Kernel, 2022	104.5	105.5	0.3%	6.5%	5.9%	8.75%	31 Jan 2022	500	USD	/B/BB-
MHP, 2026	104.0	105.0	0.5%	6.3%	6.1%	6.95%	4 Apr 2026	550	USD	B3/B/B
MHP, 2029	98.3	99.3	1.0%	6.6%	6.4%	6.25%	19 Sept 2029	350	USD	B3/B/B
DTEK, 2024	103.1	104.1	1.3%	8.8%	8.5%	10.75%	12 Dec 2024	1,275	USD	//
Metinvest, 2026	107.3	108.3	1.1%	7.2%	7.0%	8.50%	23 Apr 2026	648	USD	B3/B/BB-
Metinvest, 2029	104.8	105.8	1.4%	6.4%	6.3%	7.75%	17 Oct 2029	500	USD	B3/B/BB-
NaftoGaz, 2024	106.4	107.4	0.4%	5.5%	5.2%	7.125%	19 Jul 2024	600	EUR	//
Bank Eurobonds										
UkrEximBank, 2022	103.7	104.7	0.4%	6.6%	5.7%	9.63%	27 Apr 2022	750	USD	Caa3//B
UkrEximBank, 2023	96.9	97.9	-0.1%	11.0%	9.7%	9.00%	9 Feb 2023	125	USD	Caa3//B
UkrEximBank, 2025	103.2	104.2	0.4%	8.2%	7.7%	9.75%	22 Jan 2025	500	USD	Caa3//B
Oschadbank, 2023	102.6	103.6	-0.1%	7.8%	7.1%	9.38%	10 Mar 2023	700	USD	Caa3//B
Oschadbank, 2025	102.8	103.8	0.2%	7.7%	7.0%	9.63%	20 Mar 2025	500	USD	Caa3//B

¹ Moody's/S&P/Fitch

Source: TR Data, Eavex Research

UKRAINIAN DOMESTIC BONDS

Issue	Price (Bid)	Price (Ask)	YTM (Bid)	YTM (Ask)	Modified Duration	Coupon	Coupon Period	Maturity Date	Volume UAH mn
UAH denominated Bonds									
UA4000202469			12.00%	10.00%	n/a	n/a	S/A	30 Sept 2020	n/a
UA4000200174			12.00%	10.00%	n/a	n/a	S/A	20 Jan 2021	n/a
UA4000195176			12.00%	10.00%	n/a	n/a	S/A	11 Aug 2021	n/a
UA4000203236			12.00%	--	n/a	n/a	S/A	05 Jan 2022	n/a
UA4000204002			12.00%	--	n/a	n/a	S/A	11 May 2022	n/a
UAH denominated Bonds									
UA4000201743			4.75%	3.25%	n/a	5.65%	S/A	22 Jul 2021	USD 83mn

Source: TR Data, Eavex Research

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