Fixed Income Weekly Monitor

June 27, 2022

Trends

There was another sharp drop in indicative quotes for Ukrainian sovereign Eurobonds last week. The benchmark 10-year issue lost 11% to close at 27.7 cents on the dollar (33.4% YTM). Although Ukraine got a blessing for its EU ambitions and a pledge of unwavering support from Britain, the country came under shell and missile attacks from russia in multiple locations. Meanwhile, the G7 leaders will commit to providing indefinite support to Ukraine for its defense against russia's invasion, according to the text of a draft statement from their summit in Bavaria. At the summit, the leaders were set to announce new bans on russian gold imports - the latest in a series of sanctions aimed at further isolating russia economically over the war.

The Ministry of Justice of Ukraine has filed a new lawsuit against russia with the European Court of Human Rights. The lawsuit stressed that every day throughout Ukraine, the aggressor country conducts indiscriminate and disproportionate use of military forces and means against the civilian population and property of citizens, violating all relevant norms of international law.

Ukraine-24s Eurobond issue fell 11.8% last week to 29.9 (97% YTM) and the actively traded Ukraine-28s slipped by as much as 22.6% to 25.0 (54.4% YTM). The VRI derivatives (linked to Ukraine's future GDP growth with expiration in 2040) plunged by 22% to 26.2 cents on the dollar.

Ukrainian corporate Eurobonds were little changed due to their low liquidity. Indicative quotes for Kernel-27s stood at 52.8 (23% YTM) and Metinvest-26s traded at 55.7 (27.4% YTM). The longer maturity Metinvest-29s declined by 1.7% to 59.0 (18.8% YTM). Quasi-sovereign NaftoGaz-24s stayed at 29.0 (101% YTM).

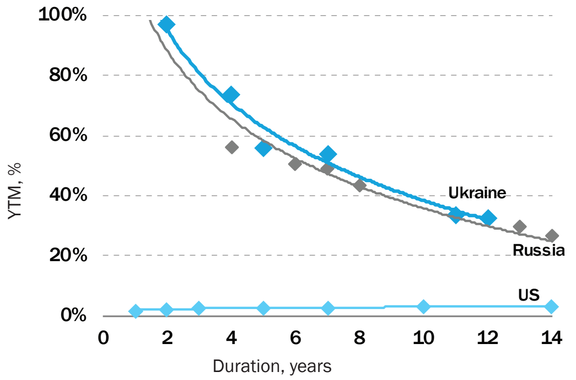
The Finance Ministry raised a total equivalent of UAH 7.7bn through the placement of special government bonds. The offered yield remained unchanged at 9.5% for the 3-month debt papers and 11.5% for the 1.5-year issue. The yield for the 6-month USD-denominated bond was 3.5% and for the EUR-denominated 1-year issue the yield was set at 3.7%. Also, the government received direct support from the National Bank in form of investing UAH 35bn in the government bonds. The National Bank has accumulated a portfolio of UAH 533bn of government bonds, having a share of 43% of the total outstanding government domestic bonds.

The hryvnia managed to gain by 0.3% to 35.5 UAH/USD on the OTC cash market amid the National Bank's intervention to sell USD 933mn on the interbank market at the official exchange rate of 29.25 UAH/USD.

The National Bank of Ukraine has opened a special fundraising account to support the Armed Forces of Ukraine. Please find more at the National Bank's official website under the link below:
www.bank.gov.ua/en/about/support-the-armed-forces

The National Bank also opened fundraising account for Humanitarian Assistance to Ukrainians. Please see details under the link below:
www.bank.gov.ua/en/about/humanitarian-aid-to-ukraine

SOVEREIGN BOND YIELD CURVES



Source: Bloomberg. Eavex Capital

FIXED INCOME

	Last	1W ch	YTD
NBU Key Rate	25.0%	0.0 p.p.	+16.0 p.p.
UAH 1-year war bond	11.0%	0.0 p.p.	0.0 p.p.
Ukraine-2026	56.0%	5.3 p.p.	47.1 p.p.
Ukraine-2032	33.4%	3.3 p.p.	24.2 p.p.

CURRENCY

	Last, UAH	1W chg.	YTD
USD/UAH	35.50	-0.3%	29.9%
EUR/UAH	37.40	0.0%	20.8%

Source: Eavex Capital

Highlights

- Russia Takes Control of Severodonetsk as G7 Promises to Continue Ukraine Support
- National Bank Publishes Assessment of Ukraine's Financial Sector Stability

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Russia Takes Control of Severodonetsk as G7 Promises to Continue Ukraine Support

by Will Ritter
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NEWS

The leaders of the G7 industrialized nations on Sunday (Jun 26) released a statement promising to continue to support Ukraine in its war against Russia “for as long as necessary” in the form of financial and weapons assistance. The leaders are meeting in southern Germany near the Austrian border. The summit kicked off with the announcement of a Western ban on the trading of Russian gold as a way to reduce funding for the Kremlin’s military machine. Gold is Russia’s largest export product after oil and natural gas. President Zelenskiy is due to address the summit by video link today (Jun 27). Meanwhile, in military news, the Ukrainian government admitted that it has lost control of the eastern city of Severodonetsk after weeks of defending it from the Russian advance, leaving besieged Lysichansk as the last town in Lugansk province still held by Ukrainian forces. Russian missile strikes have hit Ukrainian cities nationwide in recent days, including Odessa, Kharkiv, Zhytomir, Cherkasy, and Kyiv. The strike in the capital on Sunday (Jun 26) apparently targeted the Artyoma factory near the central area of the city. Zelenskiy warned in his nightly address that the Kremlin is trying bring Belarus into the war against Ukraine, and he appealed to Belarusian citizens to refuse to take part in hostilities.

COMMENTARY

The loss of Severodonetsk had been expected for some time, with Ukraine simply outgunned there by Russian artillery. The main military question now in the Donbass is whether Ukrainian forces will be able to prevent the cities in western Donetsk province - Slavyansk, Kramatorsk, Bakhmut, and Avdiyivka - from falling into Russian hands amid the ongoing deliveries of new Western weapons systems. In terms of the G7 statement, we note that this and other such public declarations of Western support conspicuously do not include specific language referring to Ukraine regaining all of the Russian-occupied territories as an endgame of the war. This is in quite sharp contrast to the public statements of Zelenskiy and other top Ukrainian officials, who always emphasize the condition of completely restoring Ukraine’s territorial integrity as the key element of “victory” over Russia. This apparent divergence in goals between Ukraine and its Western allies will continue to be a source of friction in the coming weeks and months, we think.

National Bank Publishes Assessment of Ukraine's Financial Sector Stability

by Dmitry Churin
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NEWS

The National Bank released its latest report on financial stability on Jun 21. According to the document, the regulator has identified the following main theses:
- despite the war shock in Ukraine, the banking system continues to operate, remains highly liquid, and has a high margin of safety;
- corporate lending grows exclusively with the support of the state; retail lending decreases, mortgage lending ceased;
- credit risks will increase in the short term, and the loss of the loan portfolio may exceed 20%;
- banks' capital reserves in February significantly exceeded the required minimum levels, so banks can absorb main losses from the rising non-performing loans. After the war, banks will have enough time to restore solvency fully;
- financial assistance from the Western world makes it possible to finance the budget deficit and maintain Ukraine's international reserves while foreign debt markets are not available for Ukraine.
- the National Bank conducted a stress test of credit risk in the banking system. On average, banks can cover the losses of 24.5% of the operating loan portfolio with existing capital.

COMMENTARY

In our opinion, the National Bank is quite optimistic about the current situation of the financial system, ignoring some of the macroeconomic risks directly related to the loss of business opportunities for Ukraine to conduct export-import operations through seaports as a result of the russian invasion. For the most part, the National Bank focuses on the fact that there are 85% of the country's bank branches in operation in June. This means that financial institutions have managed to withstand the pressure of numerous cyberattacks, which have intensified significantly over the past four months. There is also such a positive point that to save the data, Ukrainian banks have moved the data to cloud storage. As a result, of all the risks inherent in banks, the key is credit risk, and its implementation is the biggest threat to the sector. Financial institutions slowly began to recognize the already incurred and expected losses. For the first time in five years, the Ukrainian banking sector has become unprofitable due to a sharp increase in non-performing loan reserves. However, on the operational level, the country's banking system remains profitable. The regulator stressed that in case of violation of capital requirements or liquidity for individual banks, temporary measures of influence will not be applied giving banks time to adapt to the capital requirements amid the war.
Separately, there was reported the latest data from OschadBank shows that its regulatory capital adequacy ratio as of June 1 was 13% while the minimum required level is 10%.
Indicative quote for OschadBank Eurobond with maturity in March 2023 increased by an impressive 33% last week to 57 cents on the dollar (140% YTM). There is no information yet on whether OschadBank plans to restructure this issue of Eurobonds.

SELECTED UKRAINIAN EUROBONDS

Issue	Indicative Price	Price change in one week	YTM, %	Coupon	Maturity Date	Volume USD mn	Currency	Ratings[1]
Sovereign Eurobonds								
Ukraine, 2022	60.9	-11.1%	620%	7.75%	1 Sept 2022	1,384	USD	Caa3//
Ukraine, 2024	29.9	-11.8%	97%	7.75%	1 Sept 2024	1.339	USD	Caa3//
Ukraine, 2026	28.6	-10.1%	56.0%	7.75%	1 Sept 2026	1,318	USD	Caa3//
Ukraine, 2028	25.0	-22.6%	54.4%	9.75%	1 Nov 2028	1,600	USD	Caa3//
Ukraine, 2032	27.7	-10.9%	33.4%	7.38%	25 Sept 2032	3,000	USD	Caa3//
Ukraine, GDP-linked	26.2	-21.8%			31 May 2040	3,214	USD	//
Corporate Eurobonds								
MHP, 2026	52.9	1.5%	29.9%	6.95%	4 Apr 2026	550	USD	//
Kernel, 2027	52.8	0.0%	22.9%	6.75%	27 Oct 2027	300	USD	//
DTEK Energy, 2027	21.6	26.3%	53.0%	5.00%	31 Dec 2027	1,645	USD	//
Metinvest, 2026	55.7	0.9%	27.4%	8.50%	23 Apr 2026	648	USD	//
Metinvest, 2029	59.0	-1.7%	18.8%	7.75%	17 Oct 2029	500	USD	//
NaftoGaz, 2024	29.0	0.0%	101%	7.125%	19 Jul 2024	600	EUR	//
Ukrainian Railways	25.0	0.0%	122%	8.25%	9 Jul 2024	500	USD	//
Bank Eurobonds								
UkrEximBank, 2023	31.9	0.0%	543%	9.00%	9 Feb 2023	125	USD	//
UkrEximBank, 2025	31.3	-19.9%	80%	9.75%	22 Jan 2025	600	USD	//
Oschadbank, 2023	56.8	33.0%	140%	9.38%	10 Mar 2023	700	USD	//

[1] Moody's/S&P/Fitch

Source: Boerse-Berlin, Boerse-Stuttgart. cbonds, TR Data, Eavex Research

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