Ukraine

Country Report March 2019

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1.0 Executive summary

The National Bank of Ukraine (NBU) reviewed downwards the assessment of growth of real GDP of the country in 2018 to 3.3% from 3.4%, but the change is unimportant as Ukraine continues to grow well below its potential thanks to the war with Russia and the failure of the government to push through radical reforms.

The acting Minister of Finance Oksana Markarova nailed it in TV interview in February: Ukraine attracted about $2.5bn of foreign direct investment (FDI) in 2018 but needs at least $10bn a year if the country is going to transform and recover.

That is unlikely to happen this month as Ukrainians go to the polls to choose a president. With a record 44 candidates running at the time of writing it looks like a three-horse race that is lead by outsider and comic Volodymyr Zelenskiy followed by opposition leader, former Prime Minister and head of Batkivshchyna (Fatherland) party Yulia Tymoshenko and incumbent President Petro Poroshenko.

The election will almost certainly go a second round held in April but the result is impossible to predict as campaigning has already gotten dirty and the creaky Ukrainian election system is open to abuse.

Investment is unlikely to come after the presidential race is over as there are also parliamentary elections in October where pro-west liberals are likely to win, but the pro-Russia supporters will also do well and could form a powerful opposition block in the Rada. In the meantime a lot of the business of government will be on hold.

This uncertainty accounts for predictions of slower growth in the next two years of 2.5% and 2.9% respectively by the NBU.

Additional factors slowing down the economy will be a decline in the grain harvest after hitting the record in 2018, as well as a gradual slowdown in the global economy and trade, particularly due to the influence of protectionist measures being taken in the world, the NBU says.

On a more positive note private consumption will remain the key driver of economic growth thanks to a further increase in real incomes of the population – wages, pension payments, and remittances from abroad, which are believed to have maxed out now at some $10bn a year.

2019 will be a key year in the fight with Russia as both the controversial Nord Stream 2 pipeline will come online at the end of the year that means Russian gas can bypass Ukraine entirely and that will cost the budget some $3bn in lost revenues. A second Turk Stream pipeline that bypasses Ukraine to the south will also come online sometime in 2020.

On the business front things are beginning to move. In an encouraging sign the big international retail chains, like IKEA and Auchan, are moving into Ukraine. These companies are early movers as with their deep pockets they

tend to go into a market early in order to capture market share early on as they intend to never leave once established.

Likewise, JJLs reports that retail vacancy rates are falling and constriction is starting to pick up, in another sign of a slow revival in economic activity.

Of the macroeconomic issues, inflation remains the thorniest. Inflation ended 2018 at 9.8% after the central bank hiked rates twice, this year the regulator expects inflation to fall to 6.8%. That could lead to growth-boosting rate cuts. And on the funding front Kyiv says it will issue $2bn of Eurobonds this year, however, the debt burden rises from here.

2.0 Politics

2.1 Ukraine changes constitution to make NATO, EU membership a goal

Ukraine's parliament, the Verkhovna Rada, greenlighted on February 7 in the final readings the amendments to the nation's constitution regarding the strategic course of the state to secure Ukraine's full membership in the European Union (EU) and NATO.

The motion was backed by 334 lawmakers, exceeding the necessary minimum of 300 votes (the so-called constitutional majority). In November 2018, the Rada backed the amendment in the first reading.

Ukrainian President Petro Poroshenko told the parliament the same day that the country "will ensure its membership of NATO and its membership of the EU". "We are going our own way and this path, the path to Ukraine's membership of the EU and NATO," Poroshenko underlined, adding that over the past five years, the country has been reforming its security sector and doing everything necessary to meet NATO standards.

In 2018, NATO granted Ukraine the status of an aspirant country earlier this year, which means that Kyiv has officially declared its aspiration to join the military alliance. The alliance provided Ukraine with the status of an aspirant country after a significant delay - over the past years the Ukrainian leadership has repeatedly stated that the country's accession to the military alliance remains a strategic goal for the national leadership.

According to Kyiv, Ukraine's primary goal is to make its army more efficient and combat ready through cooperation with Nato because of the persistent threat of Russian invasion. Russia, in turn, remains firmly opposed to the further enlargement of the military alliance and the accession of more former Soviet republics after the three Baltic states joined in 2004.

On February 7, the Rada appealed to the NATO member states to support Ukraine's intentions to become members of the military alliance and to begin a formal dialogue at the NATO summit in London in December on the provision of an action plan on alliance membership.

2.2 Tymoshenko loses her early lead in presidential polls

Ukrainian comic and Volodymyr Zelenskiy and President Petro Poroshenko lead in a new survey conducted by the Kyiv International Institute of Sociology

(KIIS) on February 8-20, one of the most trusted of the various pollsters.

A quarter (26.4%) of respondents who will vote in the presidential election are planning to support Zelenskiy, and another 18% will vote for Poroshenko. Only 13.8% of Ukrainians are ready to vote for ex-PM and Batkivshchyna Party leader Yulia Tymoshenko.

Of the total number of those polled, 8.3% would not vote in the election, 30.5% were undecided regarding their vote, and 4.4% would scratch out all the candidates or spoil their ballot.

The KIIS polled 2,042 people in 110 populated localities throughout all regions of Ukraine, excluding Crimea and the rebel-held areas of the Donetsk and Luhansk regions, by means of face-to-face interviews.

Some other recent surveys confirm the fact that Tymoshenko is loosing public support ahead of the March presidential elections. Specifically, according to February's poll conducted by Kyiv-based Razumkov Center, 17.5% among all respondents plan to vote for Volodymyr Zelenskiy (19% among those who intend to take part in elections), 13.1% (and 16.8%) - for Poroshenko, and only 11.5% (and 13.8%) - for Tymoshenko.

On February 22, Tymoshenko accused Poroshenko of allegedly attempting to bribe voters using state budget funds.

"For the first time in Ukraine's history they have decided to bribe people using state budget funds. [...] They are allocating special subventions from the state budget to local budgets," Interfax news agency quoted Tymoshenko as saying. "Then, according to prearranged lists, they send people an invitation to receive the money at the mayor's office or in the governor's office as financial assistance in the amount of UAH1,000 [$37]."

Tymoshenko called this "bribery with illicit cash." She said agitators allegedly approach people and put their names in databases. Those who have already agreed to vote for Poroshenko first receive UAH500, half payment for their future vote, and are photographed with the money.

2.3 Ukraine's presidential elections Q&A with Tim Ash

Ukraine goes to the polls in just over a month and currently outsider and comic Volodymyr Zelenskiy is in a comfortable lead according to the latest polls.

An actor with no experience in government at all, analysts are asking what that will mean for Ukraine's development if he wins. However, Zelenskiy's lead is indicative of the wide spread disappointment among voters with all Ukraine's existing political elite and its manifest failure to deliver on any of the promises for a better life that the Maidan protestors fought, and died, for.

While it seems that Zelenskiy will get through to a second round of voting in April – none of the record 44 candidates has any hope to winning 50% of the votes needed to win in the first round – it is unclear who he will meet.

The other two leading candidates are incumbent President Petro Poroshenko and opposition leader, former Prime Minister and head of Batkivshchyna

(Fatherland) party Yulia Tymoshenko. But while Tymoshenko had a strong and early lead, she has fallen back to third place in the most recent polls – and Ukraine's polls are notoriously inaccurate to begin with.

Veteran emerging markets analyst Tim Ash, Senior Sovereign Strategist at BlueBay Asset Management, runs through what is known, what is likely, and what remains anyone's guess in the upcoming elections.

Q&A on Ukraine

Ukraine goes to elections on March 31 for presidential, with likely a second round run-off vote three weeks later on April 21, and then parliamentary elections are due by October. I thought it perhaps useful to discuss how a foreign investor views this set of elections, and the Ukraine story.

Q? What do you make to these elections?

Answer: Well I think we should celebrate the fact that despite everything Ukraine has been through over the past few years, it remains a vibrant, functioning democracy. We can debate the effectiveness of the constitution and the election law, which has elements of the British "rotten borough" about it with the single mandate constituencies, which unduly benefit oligarchic business interests. But with 40-odd candidates, we have a genuinely contested presidential election, from, which we really don't know who is going to emerge victorious. And unfortunately the trend in too many Emerging Market countries of late is in an entirely different direction, towards "managed democracy" or even more authoritarian rule – and sadly, too many people seem to be celebrating that as somehow optimal from a development perspective. I just don't agree.

I think it is also refreshing when all the media talk is about a crisis in liberal Western market democracy, that opinion polls show strong support – two thirds – for Ukraine's Western orientation, towards the European model with respect for human rights, democracy and the rule of law. This is despite difficult economic times: recession, devaluation, default, foreign annexation and invasion. Ukrainians are voting with their feet – well unfortunately actually many are doing literally that, with 4-5 million thought to be working overseas, mostly in the EU. But they know the model of development they want, and its orientation is Westwards.

Q? And what about the result, who is going to win?

Answer: No idea. I have now covered Ukraine for over thirty years and I hold my hand up and admit that these elections are genuinely impossible to call. But I guess my saving grace is that I am pretty sure that no one else either really knows who is going to win either.

I had been in the camp of thinking that Ukraine would benefit from a Macro factor, with a new fresh face emerging victorious. I thought that was the pop star Svyatoslav Vakarchuk, but after much soul searching he opted not to run – shame. A fresh face could still win, but now that looks more likely to be the comedian Volodymyr Zelenskiy, but whose real orientation is much less easy to discern than that of Vakarchuk.

I try not to read that much into opinion polls in Ukraine, as they seem to be

manipulated by Ukraine's business and political elites. But the torrent of opinion polls do suggest at this stage it is a three horse race between the "incumbent" President Petro Poroshenko, the "disruptor" former PM, Yulia Tymoshenko, and the "joker", literally, in the pack, Zelenskiy.

Poroshenko clearly has the benefit of incumbency on his side – the considerable weight of the state apparatus, and the state budget to wield, and there have been clear signs of fiscal pump priming early this year.

The power of patronage in Ukraine, given the dominance of oligarchic groups, should not be under-estimated. Poroshenko is also playing up his achievements, including macro stability/recovery, security – halting Russia's encroachment in Donbas, and the resurrection of the Ukrainian military into a fairly formidable fighting force – and autocephalous status for the Ukrainian Orthodox Church, the latter of, which is a huge victory against Moscow. He is pushing the idea that while he has his faults, he is a stable hand on the rudder at a still difficult time, and the greatest assurance of Ukraine's Western orientation.

Poroshenko though suffers big negative ratings – even higher than Tymoshenko – reflective I guess of the fact that most Ukrainians have not seen much of an improvement in their living standards over the past five years, and want something different – there is a sense the country wants change, something different, and I guess in an age when anti-establishment figures/movements (Trump, Five Star, Brexit, Syriza) are dominant.

Poroshenko is the archetypical representative of the Ukrainian oligarchic establishment – everything that many Ukrainians simply abhor. He has been in around power/the heights of the Ukrainian economy for much of the past two decades – serving as minister of foreign affairs, head of the national security-council, NBU council chair, et al, before becoming president in 2014.

And remember back in 2014 there was little enthusiasm for his presidency, even though he won a first round victory with 54% - rather he was seen as a safe pair of hands who could manage a crisis war economy.

And to give him huge credit, he did that – he stabilised the macro, and went for peace (the Minsk accords) at a time (2014-2015) when many people pushed for outright war with Russia, which likely Ukraine would have lost. But as noted above, it looks like Ukrainians want something different, which means Poroshenko is fighting an uphill battle to win re-election, and remember only one president in Ukraine's independence era has won a second term – Leonid Kuchma.

Tymoshenko, meanwhile, is hardly something new or that different, to Poroshenko, for voters. She has been in/around Ukrainian politics for as much time as Poroshenko, but actually only in office for 4-5 years (as dep PM, then PM). I guess therein she can claim not to be wholly responsible for Ukraine's current state – albeit she is part of the oligarchic political class (like Poroshenko), which have failed Ukraine over the past 30 years.

But perhaps what marks Tymoshenko out, unlike Poroshenko, is that she is seen as a disruptor – a women, in still a man's political world in Ukraine – much more of a populist (we can debate this, given the past two years of Poroshenko rule has been much more populist, as reflected in the IMF

programme going off track for 18 months). And let's not forget that Tymoshenko is one of the few oligarchs who have served jailed times for their sins – but in Tymoshenko's case it was for something she did not do.

Tymoshenko is selling a message of change, of populism, which seemed to be selling well at least earlier in the campaign, if opinion polls were to be believed – as up until very recently she headed polls and seemed a dead cert to be in the second round. Tymoshenko is a political dynamo, a political phoenix – never write her off, as I think we have all learned in the past to our costs.

Zelenskiy is the new kid on the block, a relative political unknown. He is the new fresh face, and taking the space that many of us thought would be occupied by Vakarchuk (whom I incorrectly called as the next president). But he has captured the imagination since his launch, playing on his youth, political inexperience, and his strong media presence already from his career as a successful comedian. He is currently topping the polls, in the 20% plus range, seemingly taking some votes from Tymoshenko, and suggesting now a dog fight for second place, and a run off place, between Poroshenko and Tymoshenko.

Opinion polls suggest that Zelenskiy would beat Poroshenko and Tymoshenko in any run-off vote, albeit many suggest his political and economic policy naiveté will cost him as the campaign develops. There are also question marks around his geopolitical orientation – given alleged business links to Moscow – his business orientation given his comedy show has appeared on the channel of the controversial oligarch, Igor Kolomoisky. He denies he is in the pocket of Moscow, Kolomoisky, or big business, but all this will be tested in the campaign.

If I had to put probabilities on the three candidates' chances of winning at this stage, I would cautiously put it 25:30:40 on Poroshenko, Tymoshenko and Zelenskiy in that order, with a 5% probability attached to some other outcome.

Q? What will you be watching for in the first round?

Answer: All the focus is who will come first or second, and hence gets thru to the run-off vote, but equally important will be who comes third and then the horse trading, which will go on for these votes. Remember the 2010 elections when [banker, oligarch and former National Bank of Ukraine governor] Serhiy Tigipko came a surprise third and then traded with Yanukovych to ensure his second round victory.

Assuming Zelenskiy secures first or second place, and then Poroshenko and Tymoshenko vie for second and third places, I just wonder what deal either would be prepared to do, to back other candidates in the run-off vote.

Interestingly, therein I guess Tymoshenko will be more prepared to deal, as she has made clear she favours constitutional reform, to move more powers to the Rada, plus electoral reform to go back to a full PR system. I guess she would cut a deal with either Poroshenko or Zelenskiy to ensure that. Guess her problem is that Zelenskiy lacks any deputies in the Rada to ensure passage of any such constitutional reform, and while Poroshenko could deliver such reform via his parliamentary backing (BPP), it's hard to see Tymoshenko trusting Poroshenko on anything given their long history of rivalry and bad blood. Equally, would Poroshenko want to head a government, with

Tymoshenko as president, when he has been president – it seems unlikely.

And what exactly would Zelenskiy demand for his support in a second round vote, if he came third? Hard to say – some deal around banking, to satisfy his oligarchic backers, but which would derail cooperation with the IMF?

Note though that if Tymoshenko or Zelenskiy are elected president, they would have little legislative room to manoeuvre, given they would not control a majority in parliament, could note change the structure of the [Ukrainian Prime Minister Volodymyr] Groysman government much before those elections (sway only over the ministers of foreign affairs and head of the national security council).

Q? What about the economy, and economic policy?

Answer: Poroshenko is banging the line that only he can be trusted with the economy, and macro stability and investment are only safe in his hands, while denigrating Tymoshenko et al for populism.

I think here it is important to focus on Poroshenko's achievements on the economy front, and I think it is fair to say that Ukraine is in a much stronger position today than in 2014, with macro-stability –the resumption of real GDP growth at over 3%, inflation back in single digits, the UAH stable and reserves back to around USD20bn, with much reduced fiscal and current account deficits (around 3% of GDP each). Contrast that with the recession, devaluation and default in the period 2014-2015.

And there have been some landmark reforms, including NBU reform, banking sector reform, energy sector reform, fiscal consolidation, pro-Zorro, pension reform et al. But many of these reforms were due to the reform zeal of the Yatsenyuk administration and due to the 'blood and tears' of key reformers such as [former Finance Minister Natalle] Jaresko, [former NBU governor Tatiyana] Gontareva, [current NBU governor Yakiv] Smolii, Kobylev, [former Ukraine Finance Minister Oleksandr] Danylyuk, [Economics Minister Max] Nefyodov, [head of UrkInvest Daniel] Bilak, et al – they might argue fighting against opposition elsewhere in the Poroshenko administration. These are all heroes in my mind.

But I think it is also fair to recognise that reform slowed under the Groysman premiership, and as reflected in the fact that the IMF [programme] was off track for 18 months until late last year with its revamp to a much smaller Stand by agreement (SBA).

Why? The answer is that there seemed to be vested interests at play to prevent key structural reforms such as the anti-corruption effort, land reform, and backtracking again around energy sector reform. And Poroshenko just did not do enough to fight those battles on key structural reforms. On that he failed.

Poroshenko's legacy is hence mixed – he did some great things, but failed in other areas, such as the fight against corruption. True the anti-corruption court should be up and running soon, but let's see how successful it is, and whether it will be allowed to function and not "captured" as seems to be a big risk. But the failure to address corruption, and push on with land reform, which should have been two slam-dunks and great positives about Ukraine to sell to the

world, have undermined the business environment, and stalled inward investment. Ultimately these have stalled the pace of real GDP growth, recovery – while officials acclaim 3%+ real GDP growth, the truth is that the economy should be growing at a much higher pace, given the low base (4-5% at least), and this reflects the failure of the Poroshenko administration to address corruption in a meaningful way.

Q? But what about economic policy under Tymoshenko and Zelenskiy?

Answer: Well we simply don't know that much about Zelenskiy's economic programme as he does not seem to have an economic policy team – he has been talking about crowd sourcing policy, which really is a joke. That's how the UK got the Brexit disaster. So if he wins he'd better learn fast, and get a decent team around him. He could, and he talks about being in favour of Ukraine's Western orientation, so let's hope. But my concern is that his experience means he will hire the wrong people, and under Zelenskiy we will see policy drift, policy error and time wasted, again. And Ukraine does not have this time.

Tymoshenko at least has a team, and the policy message has been more populist, albeit all the main candidates seem to agree on the idea of low taxes – talking about the exit capital tax hated by the IMF – holding energy prices low, and re-negotiating terms with the IMF, plus debt restructuring.

To be fair, the new IMF SBA is just a bridging loan, and I think the IMF would want to re-negotiate terms with whoever wins the presidential election and then the parliamentary elections. On energy prices, this would be a deal breaker with the IMF – but remember the Groysman team was equally populist in stalling agreed energy price hikes for 18 months from July 2018. And on debt restructuring, Tymoshenko seems to be talking about renegotiating the terms of the GDP warrants, which I think no one would object to, given their perverse initial structure, much to the benefit of bond holders.

Net-net, I think whoever wins the presidential election will have limited options on the policy front. Ukraine is not yet in a strong enough position in terms of public finances and external financing (FX reserve cover) to stand alone without the IMF. Indeed, without IMF financing for 2019-2020, it's hard to see Ukraine being able to service its liabilities, unless global market conditions are set extremely fair. So all might make populist commentary in the run up to elections, but the hard reality is once in office they would have to play the IMF tune.

Perhaps the biggest issue with respect to the relationship with the IMF will be candidate's plans for the NBU and the banking sector more generally. I think there is concern that Tymoshenko and Zelenskiy are backed by Kolomoisky and the price for that will be the return of Privatbank to former owners and then higher level personal changes at the NBU. In either case I think that will be a deal breaker for the IMF and official creditors, as banking sector reform including the nationalisation of Privatbank, and NBU reform (establishing and assuring its independence) have been amongst the biggest reform wins since independence. Returning Privatbank to its owners, after a cost of over 5% of GDP to the state in bailout costs, I think will/should be an anathema to the official creditors – and indeed, any new government will be required to recoup some/all of these bailout costs as a requirement of future cooperation with the IMF.

Q? What about Russia, is there a risk of Russian intervention in these elections?

Answer: Unfortunately Moscow is unlikely to be a constructive force, in and around these elections. Look let's not forget what Moscow's agenda is in regard to Ukraine – simply put, Moscow wants Ukraine back in its geopolitical orbit/sphere of influence. And the reality is since 2014 the country (Ukraine) has moved decisively, perhaps terminally, out of that orbit and into that of the West. Kyiv hence presents a clear challenge to Moscow. From these elections Moscow wants a government in Kyiv who will respect its views/wishes, and understands where its ultimate geopolitical orbit should rest – at least from Moscow's perspective. The political reality though is that after the annexation of Crimea and Russian military intervention in Donbas, no political leader in Kyiv can ever show allegiance to Moscow, without risking their own position at home. Indeed, any Ukrainian leader to try this now I think would risk social unrest at home, and perhaps risk being removed from office. I am not sure that Moscow understands this – but look at the latest opinion polls, which show two thirds of the population wanting a Western orientation and just single digits now wanting closer ties with Moscow. Perhaps Moscow is holding back from further intervention in Ukraine, but what happens once the realisation dawns that who-ever wins the presidential elections in Ukraine, they will continue the Western orientation. At that point Moscow will have to accept the permanent loss of Ukraine from its orbit, or look to escalate. This could be through further military intervention in eastern Ukraine, or through efforts to destabilise the domestic political scene in Ukraine, perhaps by seeking to challenge the election results, perhaps even by promoting street protests. But my strong sense is that Putin is not done with Ukraine, he is simply biding his time, waiting for new opportunities to present themselves to undermine Ukrainian sovereignty, and to try and pull all or bits of Ukraine back under Russia's orbit. Watch that space.

Q? Could the election result be challenged? Street protests?

Answer: Well after the Orange revolution, and the Euromaidan, I don't think such outcomes can ever again be entirely discounted in Ukraine. I think Ukrainians would protest in a scenario where one particular candidate ends up winning the election by administrative means even though the strong popular consensus is that they actually lost. In that scenario I think the reform vote would demonstrate and I think the pro-Russian constituency would seek to exploit any such scenario. The hope thus is that such administrative means are not used as they would be very destabilising – let's hope that all candidates realise this, and don't give outside actors an excuse to intervene in the domestic political scene more forcibly.

Tim Ash is the Senior Sovereign Strategist at BlueBay Asset Management. This comment first appeared as an email sent to clients

2.4 Poroshenko accused of "profiting on blood" in arms sales scandal

President Petro Poroshenko rivals in the upcoming presidential election

are accusing him of "profiting from blood" after an investigation revealed that the son of the president's close business partner has been selling arms to separatist rebels in the breakaway eastern region of Donbas, it was a revealed in a report broadcast on Ukrainian TV on February 25.

Award-winning investigative reporter Denys Bihus aired the results of an investigation on Ukrainian television citing documents and private messages from an anonymous leaker that described a fraud by a group allegedly including Ihor Hladkovskiy (aka Gladkovsky), the 22-year-old son of Oleh Hladkovskiy, who is formerly worked closely with Poroshenko and has been the First Deputy Secretary of National Security and Defence Council (NSCD).

Hladkovskiy senior immediately resigned his post on February 27 as the scandal swept the country that could spell the end to Poroshenko's re-election hopes. Despite the ties between the men, Poroshenko himself has not been personally implicated in the schemes to sell weapons that are widely seen as Kremlin-proxies and who are fighting the Ukrainian army. More than 10,000 Ukrainian service men have been killed in the four-year long undeclared proxy war against Russia.

"Just wonder if this will be a terminal blow for Poroshenko's campaign. [Rivals Yulia Tymoshenko] and Zelenskiy will milk this one to the full," Tim Ash, Senior Sovereign Strategist at BlueBay Asset Management said in an emailed note. "And assume given the focus of [oligarch Ihor] Kolomoisky's media channels they will look to reveal lots more kompromat. All sides have a lot to lose in this campaign, I guess it is going to be an ugly and dirty campaign. The gloves just came off.

With the presidential election only a month away Poroshenko's main rivals leapt on the case to lambaste the president.

With a record 44 candidate registered for the poll, the race is seen as a three-way affair between the incumbent president, ex-MP Yulia Tymoshenko and comedian Volodymyr Zelenskiy.

Tymoshenko accusing Poroshenko and his inner circle of "state treason" and called for his immediate impeachment. Zelenskiy said the president and his friends were "profiting on blood."

"This is state treason deliberately committed by a citizen of Ukraine to the detriment of Ukraine's sovereignty, territorial integrity and inviolability, defence capabilities and state and economic security," Tymoshenko said on February 25. "In essence, this is supporting the enemy in destroying the Ukrainian army. This supports the occupier-state in conquering our country. This is absolutely a case for prosecution."

Ihor Hladkovskiy was a direct participant in "schemes in the millions" that stole money from Ukraine's defence industry complex and illegally profited from the war, according to the Nashi Hroshi investigation broadcasted on February 25.

Among the most outrageous alleged schemes is organising contraband imports of Russian parts for Ukrainian military hardware, and then selling them at highly inflated prices to the armed forces.

The program demonstrated leaked text messages in, which Russian suppliers

reached agreements with Hladkovskiy associates, Vitaliy Zhukov and Andriy Rohoza.

These associates also sent texts to the junior Hladkovskiy in order to request that his father resolve contracts, or address these matters with the directors of Ukrainian factories. More than UAH250mn ($9mn) in profit was earned through three shell companies, including one directly owned by Poroshenko at the time, the report alleged. In one text exchange, Rohoza alleged UAH500mn was earned. Another mentioned scheme was reselling parts to the Ukrainian military that were designated for disposal.

"Profit on blood"

The same day, Zelenskiy wrote on his Facebook page that "the people who came to power on blood are making profit on blood". "Now I understand what the 'Army, Language, and Faith' slogan means: robbing the army and artificially dividing the people by language, and therefore there is no faith in you," Zelenskiy added.

Poroshenko has adopted the 'Army, Language, and Faith' slogan during his presidential campaign. The presidential election will take place on March 31.

According to latest surveys, Zelenskiy's presidential candidacy rating is growing. Specifically, according to the latest poll results published by the Kyiv International Institute of Sociology (KIIS), among decided voters, Zelenskiy has 26.9% support, compared to 17.7% for President Poroshenko and 15.8% for ex-PM Yulia Tymoshenko, according to the poll conducted between January 31 and February 10 of 2,007 respondents.

Zelenskiy would earn 39.6% of votes in the second-round runoff, compared to 18.1% for Poroshenko (a 21.5% gap), according to the poll. Tymoshenko would earn 27.0%, compared to 18.9% for Poroshenko (an 8.1% gap).

Zelenskiy, a close associate of controversial Ukrainian oligarch Ihor Kolomoisky, was officially registered as a presidential candidate by the CEC on January 30. The comedian was nominated by his newly-created party the Servant of the People.

Poroshenko's reaction

Meanwhile, Poroshenko has demanded Ukrainian law enforcements to check information reported by the Nashi Groshi programme and said he supports the temporary removal of First Deputy Secretary of the National Security and Defence Council (NSDC) Oleh Hladkovskiy.

"The President [...] supported the removal of Oleh Hladkovskiy from his duties during the investigation. Poroshenko demands that law enforcement agencies urgently check the information provided in Nashi Groshi's investigation to refute or confirm the report's findings," Interfax news agency quoted the president's spokesman Svyatoslav Tsegolko on February 25.

Zenon Zawada at Kyiv-based brokerage Concorde Capital believes that the scandal has the potential to boost the support for Tymoshenko and Zelenskiy at Poroshenko's expense.

"Poll ratings released yesterday showed that the candidacy of sketch comedian Zelenskiy has stolen the election momentum of Tymoshenko, whose support has plummeted directly and inversely to Zelenskiy's rise," he wrote in a note on February 25. "Therefore, Tymoshenko is desperate to give voters new reasons to support her. Illegal profit from the war is a particularly sensitive subject that can stir the emotions of the public, particularly among the military that continues to support Poroshenko, more or less."

2.5 Minsk in hot water for coal exports to Ukraine

Minsk is in hot water again for cheating on trade, but this time its not shrimps or apples being sent to Moscow, but coal mined in the breakaway regions of Donbas in Ukraine that is being sold to Ukrainian power plants.

Belarusian exports of anthracite coal to Ukraine jumped 340-fold y/y in 2018 to 102,200 tonnes, according to the state statistical service Belstat in Minsk.

Anthracite coal is a special form of coal used to fire many of Ukraine's power stations, but is only mined in the regions now occupied by the Russia-backed separatist rebels and inaccessible to the rest of the country. Ukrainian power stations have been forced to import the coal from Russia, which is a major producer, as well as some small amounts from the US.

The cost of anthracite imported by Ukraine from the republic last year was $9.3mn from a total of $50.4mn. Imports of all types of coal increased by 980 times y/y to 558,500 tonnes.

Kyiv-based independent broadcaster Hromadske is alleged that Belarus has exported to Ukraine anthracite coal that was originally mined in the rebel-controlled territories of the Donbas region, which were sent to Belarus before being rerouted back to the unoccupied Ukraine. There is no confirmation of this information from other sources.

Meanwhile, Ukrainian Energy and Coal Industry Minister Ihor Nasalyk said on February 27 that imported anthracite was not mined in the rebel-controlled territories. "I can say that it is definitely not from non-government controlled areas in Donbas," Interfax news agency quoted him as saying.

The minister said that his conviction is based on agreements with consumers of thermal generation plants, who pledged not to purchase anthracite from the occupied Donbas, to conduct an analysis of the origin and routes of the imported anthracite offered to them. "I think no one will risk their business," Nasalyk said.

Meanwhile, according to Belstat, the country imported 1.649mn tonnes of coal (against 762,400 tonnes a year earlier) for a total of $107.2mn in 2018. The most part of coal - 1.274mn tonnes - was supplied from Russia.

Imports of anthracite amounted to 173,000 tonnes for $17.1mn. Most of the coal of this grade - 172,800 tonnes - come from Russia.

2.6 Politics - misc

Ukraine's incumbent President Petro Poroshenko announced his candidature for president in the elections slated for March 31 at a press conference on January 29. "I have decided to run in the election once again," the incumbent said, addressing a forum dubbed "From Kruty to Brussels. We Follow Our Own Path," reports Tass. "I would like to ask voters for a mandate to ensure the irreversibility of the country's European and Euro-Atlantic integration, and our independence, as well as to restore Ukraine's territorial integrity, bring back peace, complete the construction of a strong state capable of providing prosperity to every Ukrainian," Poroshenko said. The president still has a lot of heavy lifting to do as he is currently trailing in fourth place with 8% in the most recent polls, 12 points behind opposition leader Yulia Tymoshenko with 20%. Poroshenko's first task will be to simply beat independent candidate comedian Vladimir Zelenskiy and head of the Opposition Bloc Yuriy Boyko (aka Boiko) to make it to a second round vote scheduled for April.

Ukrainian Constitutional Court has cancelled criminal responsibility for illicit enrichment, Ukrainska Pravda online outlet reported on February 26 quoting four separate unnamed sources. The court believes that criminal responsibility for such wrongdoing violates the presumption of innocence. The parliament passed the law in 2015 as one of the conditions for Ukraine to receive a visa-free regime with the European Union and to continue its cooperation with the International Monetary Fund (IMF). NIxing the law endangers both the IMF deal and the EU visa-free regime. Both Poroshenko and Tymoshenko immediately submitted bills to re-criminalise graft the next day.

Ukrainian President Petro Poroshenko was hit by a weapons smuggling scandal during the outgoing election campaign. The president was accused by ex-MP Yulia Tymoshenko and comedian Volodymyr Zelenskiy of "state treason" and "profit on blood" amid media reports that Poroshenko's associates allegedly illegally profited from the war in Donbas.

Ukraine is going to secure the NATO Membership Action Plan (MAP) by 2023, the nation's President Petro Poroshenko told a special session of the nation's parliament, the Verkhovna Rada, on February 19. The president also added that Kyiv will seek membership in the European Union (EU). "I believe my strategic mission is to ensure the irreversibility of European and Euro-Atlantic integration," Poroshenko's media office quoted him as saying. On February 7, the Verkhovna Rada, greenlighted in the final readings the amendments to the nation's constitution regarding the strategic course of the state to secure Ukraine's full membership in the EU and NATO. The Rada also appealed to the NATO member states to support Ukraine's intentions to become members of the military alliance and to begin a formal dialogue at the NATO summit in London in December on the provision of an action plan on alliance membership. In 2018, NATO granted Ukraine the status of an aspirant country earlier this year, which means that Kyiv has officially declared its aspiration to join the military alliance. The alliance provided Ukraine with the status of an aspirant country after a significant delay - over the past years the Ukrainian leadership has repeatedly stated that the country's accession to the military alliance remains a strategic goal for the national leadership.

The Kyiv district court that decided last week to temporarily remove Ulana Suprun as Acting Health Minister ruled on February 14 to overturn its decision and reinstate her. The US born Suprun has been championing reforms to the sector, as *bne IntelliNews* detailed in an exclusive interview "Gloves off for Ukraine's health minister as long-awaited reforms begin." Suprun has been actively closing down corrupt scams that brought her into conflict with the establishment. Following objections from Rada deputies, a court ruled she was ineligible to serve as minister due to her dual US, Ukrainian citizenship. The court decision provoked a backlash by Ukraine's international friends who heavily criticised the decision to suspend one of the few high officials left in the establishment that are actively fighting corruption.

Voters give President Poroshenko poor marks on the economy, according to a nationwide poll conducted in the second half of December for the International Republican Institute. With Poroshenko facing voters March 31 in a bid for a second term, he comes in third for "Best for the economy," with about 8.5% approvals, half those of Yulia Tymoshenko, who leads in the poll preferences. Poroshenko comes in 6th place for "Improving social protections of the poor" and "Fighting corruption in state bodies."

The main economic task of a second presidential term would be "overcoming poverty," President Poroshenko told the American Chamber of Commerce Tuesday evening. To get there, Ukraine needs foreign investment and decent paying jobs. "If you want to prevent people from going abroad, Ukraine should never again be the country of cheap labour," he said. Ukraine should process more of its farm production, "become the country of the biggest number of start-ups ," and should increase tourism seven fold, to 10% of GDP.

Young Ukrainians will be disappointed after rock start Sviatoslav Vakarchuk confirmed he won't run in the up coming Ukrainian presidential election with a posting on his Facebook page on January 27. At the same time an official tally of the number of eligable voters seems to overestimtate the total and opens up room for vote rigging, warn analysts in Kyiv.

Overall, public level of pessimism over the economy has changed little over the last four years. Asked if the country is 'going in the right direction,' 70% said 'no' – the same as in July 2015. Asked about their household finances, 39% said they had improved or stayed the same – virtually unchanged throughout 2018. Asked about joining the EU, 53% were in favour, little changed since March 2014. On joining the Moscow-led Eurasian Customs Union, 13% were in favour, virtually the same as the 14% registered in July 2015.

No Russian citizens will participate in the OSCE ODIHR mission observing the presidential elections in Ukraine, the Russian government confirmed on February 8 after parliament approved legislation the prior day forbidding their accreditation and the OSCE said it would comply.

Ukraine's parliament voted on February 7 to amend the Ukrainian Constitution to require the nation's integration into the European Union and NATO as part of the nations' "irreversible Euro-Atlantic course," according to the legislation. "The legislation's approval widens and deepens Ukraine's cooperation with the EU and NATO until the achievement of full membership and enhances Ukraine's national security, the bill said. The measure drew 334

votes, compared to the 300-vote majority needed to amend the constitution. Five of the parliament's six factions voted in favour, while none of the 38 Russian-oriented MPs of the Opposition Bloc offered their support. Embroiled in a tight election campaign, President Petro Poroshenko was sure to be in the session hall to witness the vote and commend parliament afterwards. "Today is a historic day in, which Ukraine's foreign policy orientation towards the EU and NATO was secured in the Constitution," he said after the vote. "NATO is not only about military security, but also the safety of the citizen, safety on the streets and the rule of law."

The Opposition Platform For Life party, which campaigns on a pro-Russia platform, nominated party head and former energy minister **Yuriy Boyko (aka Boiko), as its presidential candidate** at the party congress on January 29. In his remarks, Boyko said his first step as president would be initiating talks for peace and ending the bloodshed in the Donbas region. He also took a popularist swipe at the International Monetary Fund (IMF) and called for reducing natural gas prices for households that were recently hiked as part of IMF requirements. He guaranteed improved social payments for the most vulnerable groups of society.

A Kyiv district court ruled on February 5 to temporarily remove Acting Health Minister Ulana Suprun from continuing to serve in her post, citing her dual US-Ukrainian citizenship and her service as acting minister exceeding the one-month limit. The ruling came in response to a complaint filed by Radical Party MP Ihor Mosiychuk, whose fellow party members joined a chorus of prominent Ukrainians opposing her reforms in the medical sphere. (Dr. Suprun's reforms also have drawn many prominent supporters, particular among Ukraine's Euro-Atlantic advocates.) In late January, a prominent psychologist, Dr. Semen Gluzman, sent an email to his colleagues alleging that President Poroshenko was ready to remove Suprun from her post, which he supported. Yet after the court ruling, Poroshenko expressed his full support for Suprun and her reforms in remarks to the American Chamber of Commerce, stressing that she is a full citizen of Ukraine. Regarding the court ruling, Poroshenko said "the lower courts are not yet reformed, but I don't have any doubt that the reformed Supreme Court will establish the truth," as reported by the pravda.com.ua news site. Since becoming acting health minister in July 2016, Suprun has pursued dramatic reforms in Ukraine's ailing medical sphere such as financing of hospitals and clinics based on active patients, rather than number of hospitals beds. She led the establishment of a system of family medicine, encouraging Ukrainians to visit physicians at their practices and paying them directly, rather than going to overwhelmed hospitals for basic treatment. She also saved costs by merging children's hospitals with district hospitals in many regions and eliminated corruption schemes for acquiring pharmaceuticals and medical devices, with those affected fueling the criticism against her.

Ukrainian regional council head named suspect in Handziuk acid attack murder in what looks like election-related political, say Kyiv-based analysts The Prosecutor General's Office of Ukraine named Vladyslav Manher, the head of the Kherson Regional Council, a suspect on February 11 in the acid attack and murder of local civic activist Kateryna Handziuk.

The Prosecutor General's Office of Ukraine announced on February 5 it has opened a criminal case against Viktor Medvedchuk, the political council chair of the Opposition Platform For Life party, for alleged state treason

and separatism. Explaining the crime, spokeswoman Larysa Sarhan said that during the January 29 congress of the Russian-oriented party, Medvedchuk called for creating an autonomous region of Donbas with its own parliament and government, as well as amending the Constitution to preserve that status. Such calls for an autonomous region support Russia's subversion of Ukrainian statehood, Sarhan said. "In the current case, the declared calls for changes to the border of Ukraine's territory simultaneously offers aid to the Russian Federation in conducting subversive activity against Ukraine, as well as supports its aggressive activity and separatist sentiments," she said. The case was opened in response to a claim filed by Andriy Teteruk, a Donbas war veteran and MP with the People's Front party.

The number of registered voters decreased by only 80,000 since 2014, the CEC estimates, adding that voter registers are renewed every month. They will also be reviewed and updated ten and four days before the March 31 vote, he said. Analysts questioned the official voter tally pointing out that the population has shrunk since the last elections in 2014, as the mortality rate has far outstripped the birth rates. Moreover, at least 5mn Ukrainians are out of the country, working abroad, but still listed in the registrars. According to the official numbers there are only 80,000 fewer eligible Ukrainian voters compared to 2014, which analysts say is not creditable. "So given the large numbers of dead voters and absent voters still on the registers, the dominant political forces (Poroshenko Bloc, Opposition Bloc, Fatherland) have large flexibility in engaging in vote manipulations in those election commissions where they have an advantage in loyal representatives," Zawada said.

Ukraine's national gas company Naftogaz CEO Andriy Kobolev will donate all his salary and other income to three charitable funds this year, Interfax Ukraine reported on January 30. Kobolev salary has become a political issue in the election season as it is far in excess of average incomes in Ukraine.

2.7 Polls & Sociology

Eight out of ten (80%) of Ukrainian citizens believe Ukraine is moving in the "wrong direction," according to a poll from the Seetarget company it was reported on January 29. "The absolute majority estimate the direction of the country's movement as negative. Almost 80% choose "rather in the wrong direction" and "definitely in the wrong" answering the question about the country's way, but there are 14% who note the positive movement of the country," the institute's director Oleksiy Borovsky as cited by Interfax-Ukraine. According to the survey, 43.2% of respondents said Ukraine is definitely moving in the wrong direction, 37.1% of respondents believe that the country is heading "more likely in the wrong direction." At the same time, 2.3% of respondents are confident that Ukraine's direction is unequivocally correct, and 11.9% are convinced that Ukraine is moving 'rather in the right direction."

Consumer confidence of Ukrainians rose in December 2018 to 62 on a 200-point scale, GfK Ukraine reports. Across the board – propensity to consume, job prospects, and changes in personal finances – rose by an average of 3.5 points in December. Similarly, inflation expectations dropped.

3.0 Macro Economy

Main Macro indicators	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018F
Business cycle indicators											
Real GDP, chg yoy	2.30%	-14.80%	4.10%	5.20%	0.20%	0.00%	-6.60%	-9.80%	2.30%	2.50%	3.40%
Household consumption, chg yoy	11.80%	-14.90%	7.10%	15.70%	8.40%	6.90%	-8.30%	-20.70%	1.80%	7.80%	6.10%
Investments in fixed capital, chg yoy	1.60%	-50.50%	3.90%	7.10%	5.00%	-6.70%	-24.00%	-9.20%	20.10%	18.20%	12.00%
Industrial output, chg yoy	-5.20%	-21.90%	11.20%	8.00%	-0.70%	-4.30%	-10.10%	-13.00%	2.80%	0.40%	3.50%
Nominal GDP, UAH bln	948	913	1,079	1,300	1,405	1,465	1,587	1,989	2,383	2 983	3516
Nominal GDP, USD bln	180	117	136	163	176	183	134	91	93	112	131
GDP per capita, USD	3,891	2,550	2,972	3,580	3,865	4,030	3,117	2,134	2,193	2 638	3086
CPI (eop)	22.30%	12.30%	9.10%	4.60%	-0.20%	0.50%	24.90%	43.30%	12.40%	13.70%	8.90%
CPI average	25.20%	15.90%	9.40%	8.00%	0.60%	-0.30%	12.10%	48.70%	13.90%	14.40%	11.90%
Unemployment (ILO methodology, avg)	6.90%	9.60%	8.90%	8.70%	8.20%	7.80%	9.70%	9.50%	9.70%	9.50%	8.80%
Source: SP Advisors											

3.1 Macroeconomic overview

The National Bank of Ukraine (NBU) has reviewed downwards the assessment of growth of real GDP of the country in 2018 to 3.3% from 3.4%, according to a posting on the website of the central bank.

The forecast of GDP for the next two years remained unchanged: 2.5% and 2.9% respectively.

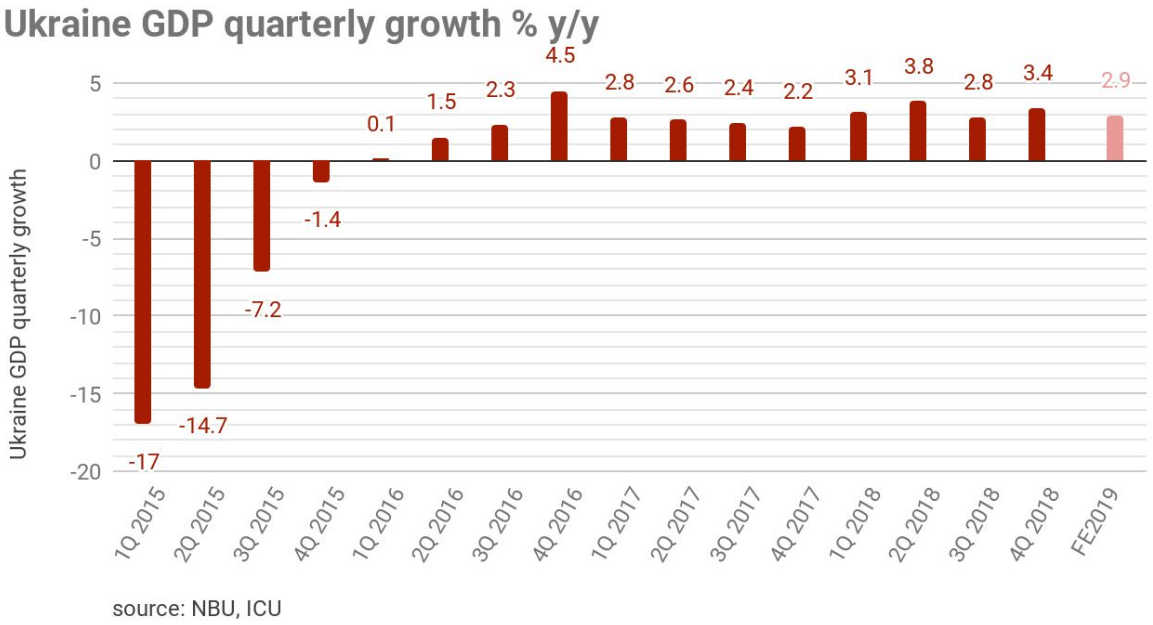
"As previously predicted, real GDP growth in 2019 will slow to 2.5%. This is due to tight monetary policies needed to reduce inflation to the target and restrained fiscal policy due to the repayment of significant amounts of public debt this year," the central bank said.

Additional factors slowing down the economy will be a decline in the grain harvest after hitting the record in 2018, as well as a gradual slowdown in the global economy and trade, particularly due to the influence of protectionist measures being taken in the world.

Private consumption will remain the key driver of economic growth thanks to a further increase in real incomes of the population – wages, pension payments, and remittances from abroad.

According to the NBU estimates, from 2019, the real growth of the economy will begin to accelerate: up to 2.9% in 2020 and 3.7% in 2021.

The shadow economy accounted for 32% of official GDP during the first nine months of 2018, the Economic Development and Trade ministry reports. This is 1% point below the level for the same period in 2017.



Ukraine: Key economic figures and forecasts							
	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017e**
Nominal GDP (EUR bn)	116.9	135.2	135.3	99.9	81.4	78.3	84.8
Nominal GDP per capita (EUR)	2,573	2,987	3,341	2,332	1,904	1,737	1,994
Real GDP (% yoy)	5.5	0.2	0	-6.6	-9.8	2.3	2.0
Consumer prices (avg, % yoy)	8	0.6	-0.2	12.1	48.7	14.9	14.5
Unemployment rate (avg, %)	8.7	8.2	7.8	9.7	9.7	9.7	9.3
General budget balance (% of GDP)	-1.8	-3.8	-4.4	-4.9	-2.3	-3.5	-3
Public debt (% of GDP)	36.4	37.1	40.7	52.9	72.6	81.3	84.9
Current account balance (% of GDP)	-6.3	-8.2	-9.2	-3.5	-0.2	-3.7	-5.2
Gross foreign debt (% of GDP)	77.6	76.5	79.3	95.2	131.5	142.9	142.5
EUR/LCY (avg)	11	10	11	16	24	30	31

Source: national sources, wiiw, RBI/Raiffeisen RESEARCH

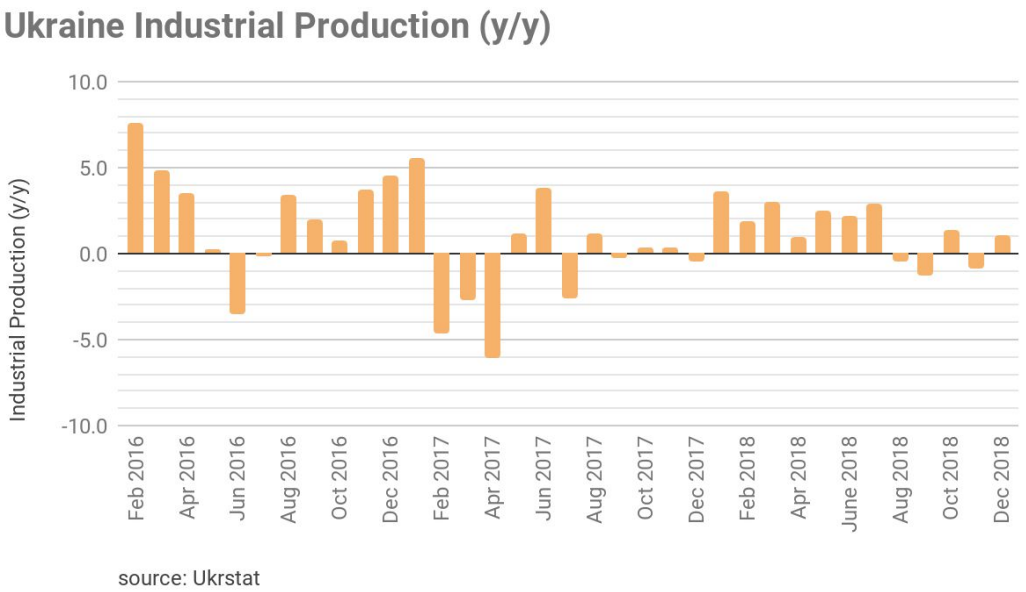
4.0 Real Economy

Ukraine - GDP growth breakdown (UAH mn)	2011	2012	2013	2014	2015	2016	2017
Annual GDP y/y growth	5.20	0.20	0.00	-6.80	-9.90	2.30	2.18
GDP per capita	3,569.76	3,855.42	4,029.72	3,082.46	2,125	2,186	2,640
Final consumption expenditure	1,094,231	1,221,163	1,337,048	1,410,177	1,715,636	2,018,854	2,592,546
Gross fixed investment capital formation	291,678	305,031	262,257	220,563	262,917	361,030	474,133
Exports	647,608	670,319	629,392	770,121	1,044,541	1,174,625	1,430,790
Imports	733,526	791,844	763,499	834,133	1,084,016	1,323,127	1,607,035

Source: CEIC

4.1 Industrial production

Ukraine's industrial output declined 3.3% year-on-year in January, after a 3.5% y/y drop in December, due to a continuing decline in manufacturing and a production drop in mining, the nation's state statistics agency Ukrstat reported on February 25. Seasonally adjusted output decreased 0.5% month-on-month. Manufacturing output decreased 5.5% y/y in January (after an 8.6% y/y drop in December). In particular, output in chemicals plunged 14.9% y/y while machinery declined 11.9% y/y. Output in metallurgy dropped 4.5% y/y, and food production dropped 1.9% y/y. Mining output dropped 1.6% y/y in January (after rising 1.8% y/y in December) due to ore production falling 7.1% y/y. Meanwhile, coal production grew 16.2% y/y while oil and gas output increased 4.3% y/y. The supply of electricity and natural gas increased 1.3% y/y in January. Regionally, growth was strongest in the Rivne (22.9% y/y), Vinnytiya (13.8% y/y) and Zakarpattia (9.6% y/y) regions. Declines were steepest in Chernihiv (-17.4% y/y), Khmelnytskiy (-15.5% y/y) and Ukrainian-controlled Luhansk (-13% y/y). Evgeniya Akhtyrko at Kyiv-based brokerage Concorde Capital wrote in a note on February 26 that that January brought no positive developments for Ukraine’s industrial production. "So far, we don’t see the positive effect of a record grain harvest on the food industry," she added. "Relatively warm weather in January restrained growth in electricity and natural gas consumption." Concorde forecasts Ukraine’s industrial output to increase 2% y/y in 2019 (vs. 1.1% y/y in 2018).



4.2 Inflation

Prices	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018F
CPI headline (%YoY, eop)	16.6	22.3	12.3	9.1	4.6	-0.2	0.5	24.9	43.3	12.4	13.7	9.4
CPI headline (%YoY, average)	12.8	25.3	16	9.4	8	0.6	-0.3	12.1	48.5	14.9	14.5	9.2
PPI (%YoY, eop)	23.2	21.1	15.3	18.8	17.4	0.4	1.7	31.8	25.4	35.7	16.5	9
PPI (%YoY, average)	20.5	33.6	7.4	21.4	19.9	6	-0.1	17	36.5	20.4	27.2	10.6

Source: ICU, CEIC

4.2.1 CPI dynamics

Ukraine's consumer prices increased 1.0% m/m in January, driven mostly by food, housing and utility prices, the State Statistics Service reported on February 8. Meanwhile, annual inflation slowed to 9.2% y/y from 9.8% y/y in December.

Prices for housing and utilities jumped 2.6% m/m, driven mostly by price hikes for heating and hot water (11.0% m/m) that were caused by previously increased residential natural gas rates.

Food prices grew 2.1% m/m in January (vs. 1.8% m/m growth in December), driven by vegetables (16.6% m/m), fruits (4.7% m/m) and milk (1.6% m/m). At the same time, prices for eggs slid 0.5% m/m.

Amid the growth, accelerated price declines for clothing and footwear (-4.6% m/m in January vs. -2.6% m/m in December) and transportation (-1.7% m/m in January vs. -1.6% m/m in December) served as restraining factors.

Core inflation (the consumer basket excluding goods and services with the most volatile prices) slowed to 0.3% m/m growth in January from 0.6% m/m in December. Annual core inflation slowed to 8.3% y/y.

“January consumer inflation was in line with our expectations. The hryvnia's appreciation by 0.5% in December, and mostly stable exchange rate in January, fostered the decline of prices for items with a high share of imports, namely clothing, footwear and gasoline,” Evgeniya Akhtyrko of Concorde Capital said in a note.

“In addition, seasonal sales amid enlarged supply also contributed to plunging clothing and footwear prices. Meanwhile, growing demand for food during the holiday season amid tighter supplies caused fruit and vegetable prices to surge. If January’s cooling annual inflation trend is maintained in February, the central bank is likely to cut its key policy rate by 0.5pp in March from 18.0% currently. We expect Ukraine’s consumer inflation to slow to 6.7% YTD in 2019 (from 9.8% YTD in 2018),” Akhtyrko added.

The National Bank of Ukraine (NBU) kept unchanged its consumer inflation forecast of 6.3% ytd for 2019 and 5% ytd for 2020, according to its quarterly inflationary report published on Feb. 7. Consumer inflation will drop to 6% – the upper end of the target inflation range – in the beginning of 2020, the NBU said.

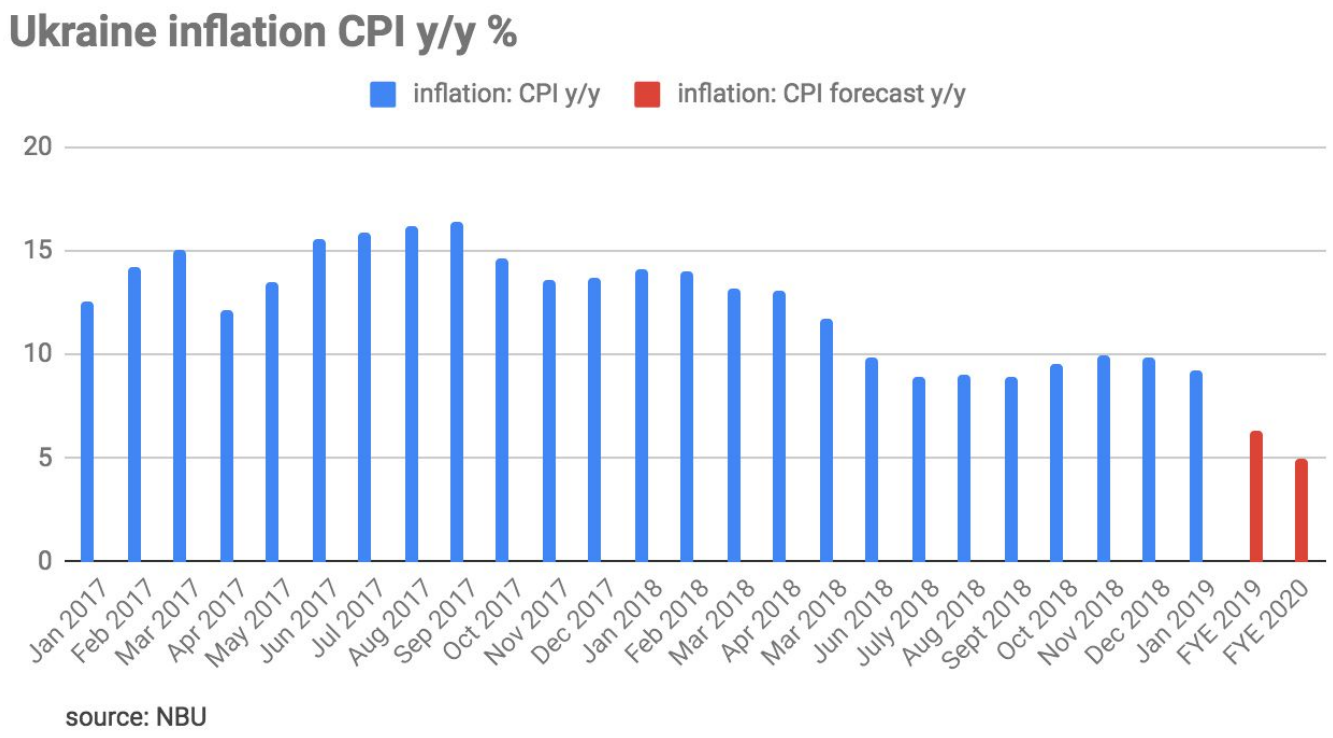
Rising utility prices and wages will be the major inflationary factors, as they will increase production costs and foster consumer demand. However, the influence of these factors will be diminishing, the central bank believes.

At the same time, the NBU’s tight monetary policy, coupled with the government’s prudential fiscal policy, will counteract consumer inflation. Lower exchange rate volatility, and moderate price growth for imported goods, will also curb inflation.

The NBU also kept unchanged its forecast of real GDP growth. In 2019, Ukraine’s economy will slow to 2.5% y/y growth. In 2020, it will accelerate to 2.9% y/y growth and 3.7% y/y in 2021 as a result of transition to softer monetary policy and the revival of investment activity amid lowered political uncertainty.

The central bank also improved its forecast of gross international reserves, expecting them to be around $21bn in 2019-2020.

“A bit better-than-expected 2018 consumer inflation result empowered the NBU with more confidence in its vision on inflation trends. Meanwhile, the major assumption of the NBU’s forecast is continuing Ukraine-IMF cooperation, including IMF financial assistance of $2.5bn in 2019. If this assumption doesn’t hold, this forecast will be subject to drastic revision,” Evgeniya Akhtyrko of Concorde Capital said.



4.3 Fixed investment

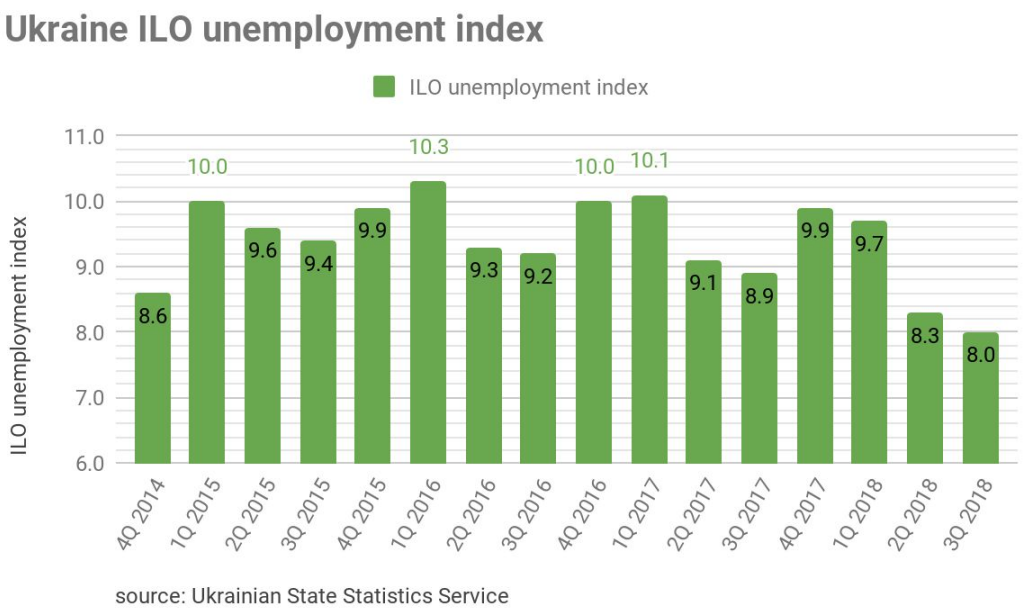
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Investments in fixed capital, chg yoy	1.6%	-50.5%	3.9%	7.1%	0.9%	-6.7%	-23.0%	-9.3%	6.0%	12.0%
Industrial output, chg yoy	-5.2%	-21.9%	11.2%	8.0%	-0.7%	-4.3%	-10.1%	-13.0%	2.1%	-0.1%

4.4 Labour and income

4.4.1 Labour market, unemployment dynamics

Unemployment rate (%)	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017 E	2018 F	2019 F
	6.4	6.4	8.8	8.1	7.9	7.5	7.2	9.3	9.1	9.3	9.4	9.3	8.8

Source: ICU



4.4.2 Nominal wages dynamics

Real wages in Ukraine grew 9.5% y/y in January, slightly slowing from a 9.7% y/y December advance, the State Statistics Service reported on February 28.

The average monthly nominal wage amounted to UAH9,223 a month ($331), dropping from UAH10,537 in December, or 13.6% m/m in real terms.

The leading regions for average monthly wages remained the city of Kyiv (UAH13,721), the Ukrainian-controlled Donetsk region (UAH10,045) and the Kyiv region (UAH9,772).

The largest nominal average wage growth was in information and communication services (25% y/y), the industrial sector (25% y/y) and construction (24% y/y). Within the industrial sector, the highest nominal wages were in pharmaceuticals (UAH17,663), mining (UAH13,883), and coke and oil production (UAH12,602).

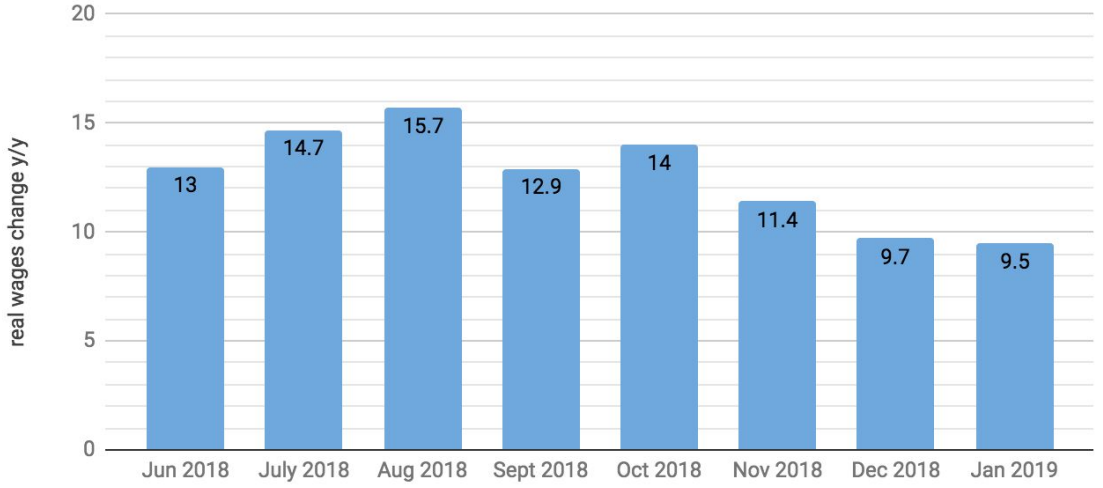
“The drop in average monthly nominal wages after a December surge was

caused by traditional bonus payments at the year end. Meanwhile, the year-on-year growth of real wages was almost unchanged. We expect real wages to climb 9-10% y/y in 2019," Evgeniya Akhtyrko of of Concorde Capital said in a note.

Ukrainian pensions will increase by 17-20% on March 1 – 30 days before the first round of the presidential elections. Pavel Rozenko, a vice prime minister, tells President Poroshenko's Channel 5 TV that March 1 will now be the annual date for pension increases. Much of this year's increase comes from $400mn in custom duties paid over the last 10 weeks by car owners regularizing 200,000 cars illegally imported from the EU. With the import duty amnesty to expire Friday, President Poroshenko said Monday that the state treasury has received 10 times more money than expected.

Ukraine gross average wages monthly USD equivalent

Ukraine real wages change y/y



source: Ukrstat

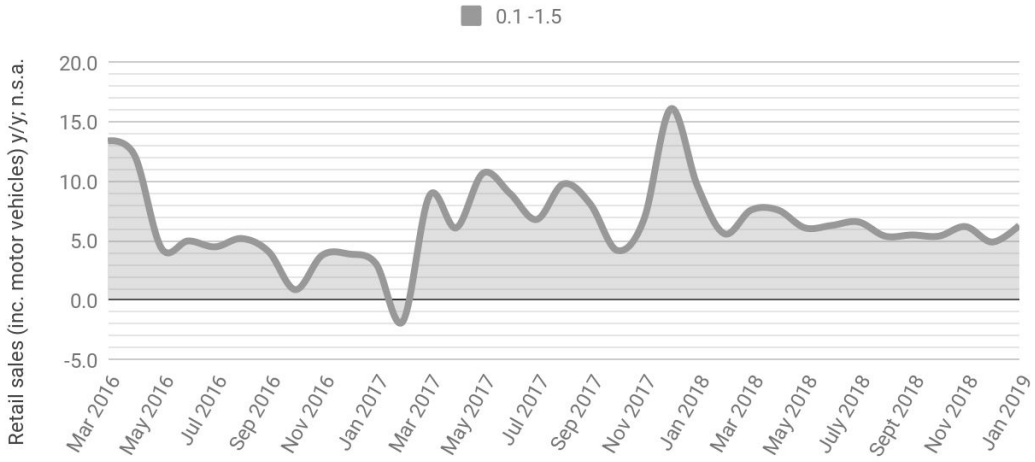
4.4.3 Retail sector dynamics

Ukraine's January retail trade increased 6.3% year-on-year in real terms, accelerating from 4.9% y/y in December, Ukraine's state statistics agency Ukrstat reported on February 20. At the same time, retail sales plunged 23% month-on-month in real terms. Regionally, highest retail growth occurred in January in Kyiv (11.3% y/y), Ivano-Frankivsk (10.8% y/y) and the Ukrainian-controlled Donetsk regions (9.8% y/y). It was slowest in the Chernihiv (1.3% y/y), Kirovohrad (1.6% y/y) and Volyn (2.0% y/y) regions. Evgeniya Akhtyrko Kyiv-based brokerage Concorde Capital believes that the accelerated growth of retail trade indicates that consumer demand remains high.

Retail trade in Ukraine increased 6.1% in real terms in 2018, slightly below the 6.5% increase for 2017. The biggest jumps were in Ukrainian-controlled Luhansk – up 27% -- and Donetsk – up 14%. fuelled partly by remittances from Ukrainians working abroad, retail was one of the three pillars of growth last year's 3.4% growth – led by agriculture – up 8.2%; and construction – up 6.3%. Concorde Capital's Evgeniya Akhtyrko writes: "We expect real retail to increase 6-7% y/y in 2019. It will be driven by real disposable income growth."

Ukrainians spend 44% of their income on food and non-alcoholic beverages, according to the latest household survey conducted by the State Statistical Survey. The average household cash income during the third quarter of 2018 was $335. The average household was 2.1 people.

Ukraine Retail sales (inc. motor vehicles) y/y



source: Ukrtat

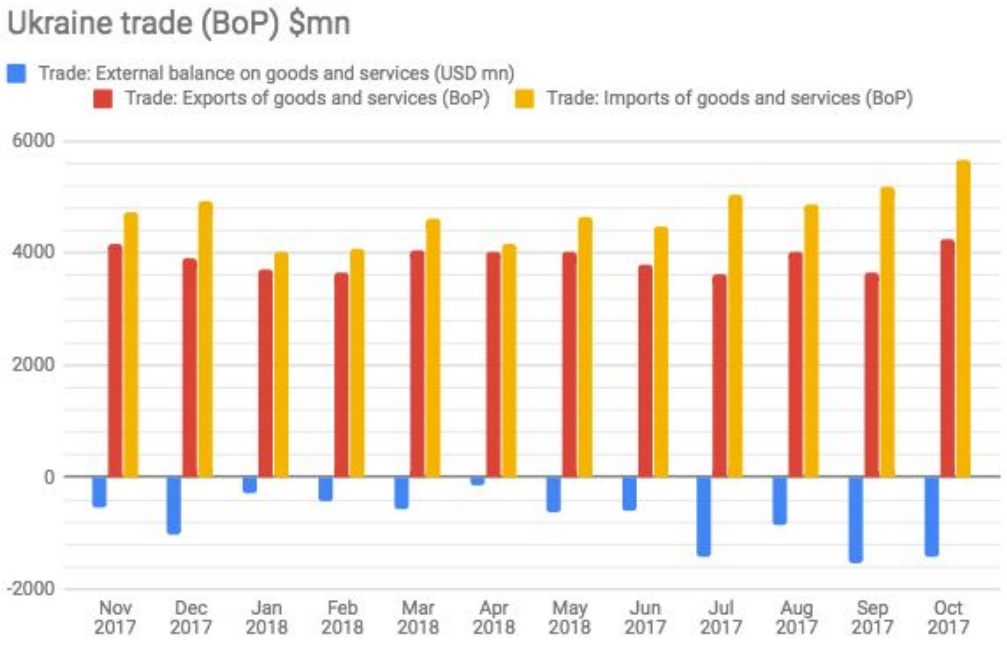
5.0 External Sector & Trade

Balance of payments	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018F
Current account balance, USD bln	-12.8	-1.7	-3	-10.2	-14.3	-16.5	-5.3	-1	-3.5	-2.1	-2.8
% GDP	-7.10%	-1.50%	-2.20%	-6.30%	-8.10%	-9.00%	-4.00%	-1.10%	-3.70%	-1.90%	-2.10%
Financial account balance, USD bln	9.7	-12	8	7.8	10.1	18.5	-8	0.8	4.7	4.7	2
% GDP	5.40%	-10.20%	5.90%	4.80%	5.80%	10.10%	-6.10%	0.90%	5.00%	4.20%	1.50%
FDI net, USD bln	9.9	4.7	5.8	7	6.6	3.4	0.3	2.5	3.3	1.2	2
% of GDP	5.50%	4.00%	4.20%	4.30%	3.80%	1.80%	0.20%	2.80%	3.50%	1.10%	1.50%
Gross NBU reserves (eop), USD bln	31.5	26.5	34.6	31.8	24.5	20.4	7.5	13.3	15.5	18.8	19

Source: SP Advisors

5.1 External sector overview

The EU may expand its Ukraine import quotas for beef, pork and poultry, Ukraine's Agrarian Confederation reports, drawing on comments to the Rada Agricultural Committee by Christian Ben Hell, head of Agriculture section of the EU Delegation to Ukraine. Noting that Ukraine's food exports to Ukraine have increased by one third since 2017, he reportedly said: "We are doing everything possible to enable Ukrainian products to enter the EU markets. In particular, we plan to expand the quotas for the supply of beef, pork, poultry products."



5.2 Balance of payments, current account

Ukraine's deficit in foreign trade of goods and services slightly more than doubled last year, hitting $5.8bn, reports the State Statistics Service. Exports of goods and services in 2018 grew by 8.6%, to $57bn, while imports rose by 14.3%, to $63bn, the statistics service said. Last year, the deficit in foreign trade in goods increased by 54.5%, to $10bn. By contrast, the surplus in foreign trade in services – largely IT – increased by 15.5% to $6bn.

Ukraine's current account (C/A) deficit reached $4.7bn in 2018, swelling from $2.4bn in 2017 due to a higher trade deficit, the National Bank of Ukraine (NBU) reported on February 1. According to NBU's estimate, the C/A deficit amounted to 3.6% of GDP in 2018 (vs. 2.2% of GDP in 2017).

The trade deficit surged to $11.5bn in 2018 from $8.6bn in 2017. In particular, goods imports increased 14.0% y/y (vs. 21.9% y/y in 2017), outpacing goods exports, which rose 9.2% y/y (vs. 18.3% y/y growth in 2017). Meanwhile, primary income balance increased to $3.2bn from $2.6bn and secondary income balance up to $3.7bn from $3.6bn.

In December alone, the C/A deficit swelled to $982mn from $962bn in November due to a decline in primary income balance to $304mn from $429mn in November. The trade deficit amounted to 1.2bn and almost didn't change from November. Goods exports increased 4.2% y/y in December, slowing from 6.8% y/y growth in November. Food exports surged 17.0% y/y amid record-high grain exports (in physical volume). At the same time, metals exports dropped 7.3% y/y.

Meanwhile, December's goods imports increased 1.0% y/y. Food exports surged 27.7% y/y amid record-high grain exports (in physical volume). Machinery imports rose 10.3% y/y (from 23.5% y/y growth in November). Mineral product imports declined 7.8% y/y (from 17.1% y/y growth in November).

The financial account surplus jumped to $2.2bn in December (from $1.6bn in November) reflecting a €349mn loan under the World Bank financial guarantee and €500mn loan from the EU under the MFA IV program. In addition, the private sector attracted $785mn under short- and long-term loans. The net inflow under trade credits increased to $745mn (vs. $222mn in November).

Due to the inflow under the financial account, the surplus of the balance of payments in December jumped to $1.8bn from $1.3bn in November. In 2018, the surplus of the balance of payments amounted to $2.9bn (vs. a surplus of $2.6bn in 2017).

"The 2018 C/A deficit turned out to be lower than our estimate due lower-than-expected imports in December. December's month-to-month decline in goods imports is not typical for Ukraine. Weaker demand for foreign currency by exporters could partially explain the hryvnia's appreciation at the year end," Evgeniya Akhtyrko of Concorde Capital said in a note. " We expect the C/A deficit to enlarge to $5.6bn in 2019 due to the ongoing swelling of the trade deficit."

Ukraine's goods trade deficit jumped by 54.5% year-on-year to $9.8bn in

2018, the state statistics service Ukrstat stated in its preliminary report on February 14.

Imports of goods reached $57.1bn, advancing 15.2% y/y, while exports amounted to $47.3bn, growing 9.4% y/y. The major contributors to import growth were machinery (20.7% y/y), energy (14.3% y/y) and metals (18.7% y/y).

Export growth was driven by ferrous metals (14.7% y/y), grains (11.4% y/y), and mineral products (9.9% y/y).

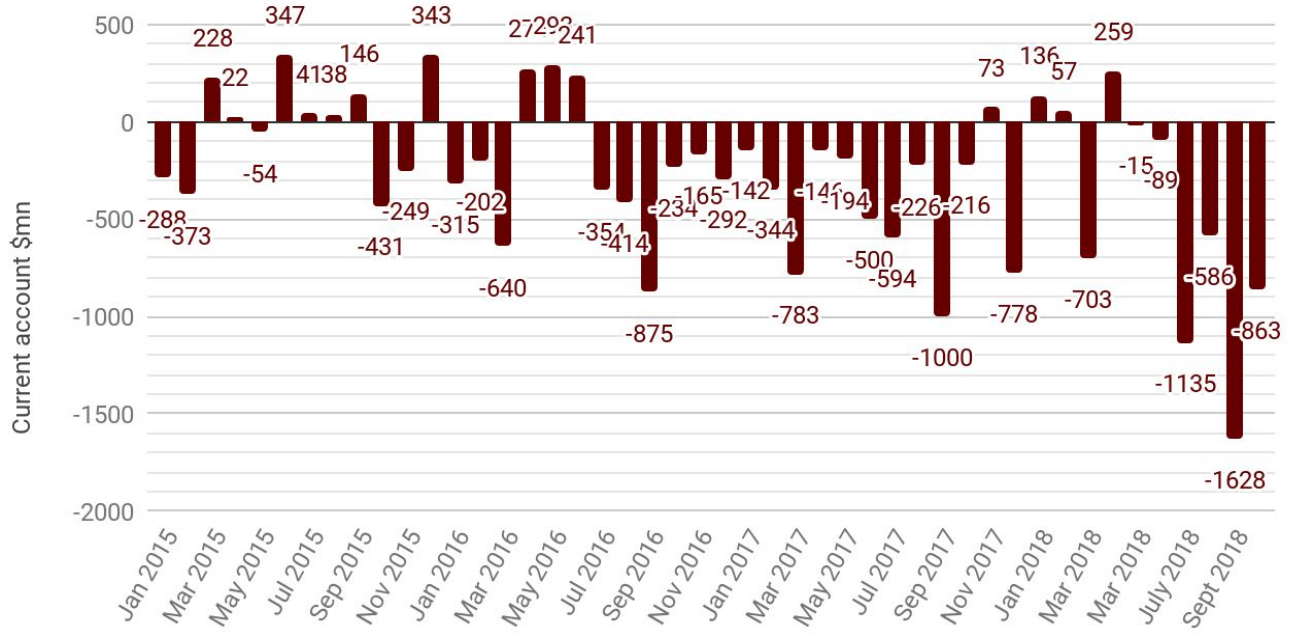
In December alone, the goods trade deficit amounted to $0.95bn, enlarging 10.8% month-on-month. Meanwhile, the seasonally adjusted goods trade deficit declined 19.5% m/m amid a 1.0% m/m drop in adjusted exports and a 4.3% m/m decline in adjusted imports.

Evgeniya Akhtyrko at Kyiv-based brokerage Concorde Capital wrote in a note on February 15 that the provisional customs statistics promise a small goods trade deficit of $79.4mn in January amid a significant month-to-month drop in imports.

"Lower imports volumes in the beginning of the year are usual in Ukraine's external trade balance, and the first-quarter results might be misleading in extending them for the rest of the year," he added.

Concorde forecasts the 2019 goods trade deficit (according to Ukrstat methodology) will swell to $11.5bn, with import growth outpacing export increases.

Ukraine Cumulative current account BPM6 (USD mn)



5.2.1 Import/export dynamics

External balance	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017 E	2018 F
Exports (US$bn)	61.4	82.5	52.1	65.6	83.7	86.5	81.7	65.4	47.6	44.9	60.2	60.8
Imports (US$bn)	69.5	96.8	54	69.6	93.8	100.9	97.4	70	49	50.3	54.6	57.2
Trade balance (US$bn)	-8.1	-14.4	-2	-4	-10.1	-14.3	-15.6	-4.6	-1.5	-2.9	-5.3	-6.4
Trade balance (% of GDP)	-5.7	-7.8	-1.7	-2.9	-6.2	-8.2	-8.7	-3.5	-1.6	-5.8	-4.4	-5.9

Source: ICU

Russian Federation remained Ukraine's main trade partner in 2018, despite mutual trade restrictions imposed in 2016. In 2018, Ukrainian exports to other countries amounted to $47.3bn, an increase of 9.4% compared with 2017, according to the figures released by the State Statistics Service on February 19. The biggest share of the country's exports ($3.7bn) still falls on Russia, despite a 7.2% decrease, which is followed by Poland ($3.3bn), Italy ($2.6bn), Turkey ($2.4bn), Germany and China ($2.2bn each). All in all, 42.5% of Ukrainian exports ($20.2bn) fell on EU countries last year. Among importers, Russia also remains the first. In 2018, imports of Russian goods to Ukraine rose by 12.3% compared with 2017 to $8.1bn. China was the second ($7.6bn), followed by Germany ($5.9bn), Belarus ($3.8bn), and Poland ($3.6bn). Total Ukrainian imports equaled $57.1bn last year, an increase of 15.2% compared with 2017, with 40% ($23.2bn) falling on EU countries.

In the first three weeks of January, Ukraine used up its entire 2019 quotas for duty-free exports to the EU for corn, honey, grapes and apple juice, reports, the Ukrainian Agricultural Business Association. Other quotas are going fast: starch – 17%; sugar – 38%; and wheat fiber --44%. Last year, Ukraine tied Argentina as the fourth largest food supplier to the EU.

Ukraine has passed the halfway marker in implementing the massive EU-Ukraine Association Agreement of 2017, according to Ivanna Klympush-Tsintsadze, deputy prime minister for European Integration. This year's priority sectors for harmonizing laws and rules are: judiciary, energy, customs, and the digital market. Of the overall task of shifting Ukraine from Russian and Soviet standards, the work is 52% done, she told a Kyiv conference reviewing the Agreement. Hugues Mingarelli, EU ambassador, said: "There are areas where progress has been very, very limited: customs, taxation, transport, intellectual property rights."

Over 15,000 Ukrainian companies have qualified to export to the EU. This business battalion expanded Ukraine's EU exports by two thirds since the Maidan – from 25% in 2014 to 42% last year. According to the EU-Ukraine conference, the main buyers are Ukraine's exports are: Poland – 17%; Italy - 14%; Germany – 10%; Hungary – 8%; and the Netherlands – 8%.

Food exports increased by 5% last year, to a record $18.8bn, reports the

Agrarian Policy and Food Ministry. In volume terms, Ukraine's farm production rose by 7.8%. For exports, the top three categories were: crops -- 38%; oils 23%; and oilseeds 10%. The top five buyers were: India -- $1.8bn; China -- $1.2bn; the Netherlands -- $1.2bn; Spain -- $1bn; and Egypt -- $890mn.

Ukraine's food exports to the United Arab Emirates hit almost $200mn IN 2018, Olha Trofimtseva, Acting Agrarian Policy and Food Minister, said in Dubai at the Gulfood exhibition. The number of Ukrainian companies participating in the fair more than doubled this year, to 69, she tells Ukrinform. Ukraine largely exports sunflower oil, milk, honey, and eggs to the UAE. With a population of 9.5mn people and a per capita income of $42,000, the Emirates import almost all their food. After signing an agricultural cooperation deal, Trofimtseva said: "Ukraine intends to become a strategic partner of the UAE to ensure food security of this country."

Ukraine wine exports were up 20% y/y in 2018 to $38mn, Deputy Agrarian Policy and Food Minister of Ukraine Olha Trofimtseva posted on Facebook on January 29.

Sunflower cooking oil exports could rise this year by 16% to 6.2mn tons, the USDA predicts. This follows a 15% rise in seed production last year, to 14mn tons. India emerges as the savior of Ukraine's industry, Fiscal Service statistics show. Last year, India bought 45% of Ukraine's total exports. Exports to the next 11 countries dropped.

Soy oil, long overshadowed by Ukraine's sunflower giant, achieved record exports in 2018 -- 215,000 tons, reports the Agrarian Economics Institute. By contrast, sunflower oil exports were 26 times greater -- 5.6mn tons. Last fall, both crops had record harvests: soy up 13% to 4.4mn tons, and sunflower seeds up 12% to 13.6mn tons. Vegetable oils and seeds accounted for one third of Ukraine's 2018 farm exports, reports the Ministry of Agrarian Policy and Food.

With walnuts leading the way, Ukraine's exports of fruits and berries rose by 17% last year, hitting $229mn, reports Ukrsadprom, the industry association. Walnut exports jumped by one third to 41,000 tons. With walnut plantings expanding in southern Ukraine, peeled walnuts fetch 10 times apples -- $3,670 per ton, versus $350 per ton. In the middle, frozen berries earn $1,640 per ton. The biggest buyers of Ukraine's fruits and berries are: Poland -- $40mn; Turkey -- $20.4mn; France -- $16mn; Belarus -- $14mn; Greece -- $13mn; the Netherlands -- $11.2mn; and Italy -- $10.2mn.

5.2.2 Gross international reserves

Ukraine's international reserves stayed unchanged at $20.8bn in January, the National Bank of Ukraine (NBU) reported on February 6.

Foreign currency outlays related to net debt repayments were compensated by foreign currency purchases by the regulator. The NBU reported that government payments in foreign currency on debt repayment and servicing amounted to $883.9mn (in the equivalent), including $808.1mn on the redemption and servicing of local Eurobonds. These outlays were partially compensated by new local Eurobond placements for $620.7mn.

International reserves during January were replenished through the purchase of foreign currency by the NBU at Ukraine's FX exchange. The net purchase of foreign currency amounted to $136.1mn. The NBU also reported on the increased value of its security portfolio by $126.3mn (adjusted to market value and exchange rate).

Ukraine's gross reserves amounted to 3.4 months of imports as of early February.

"The relatively stable situation at the FX helped the NBU to compensate currency outlays related to debt redemption despite its difficulties in attracting new local debt in foreign currency during the month," Evgeniya Akhtyrko at Kyiv-based brokerage Concorde Capital wrote in a note on February 7.

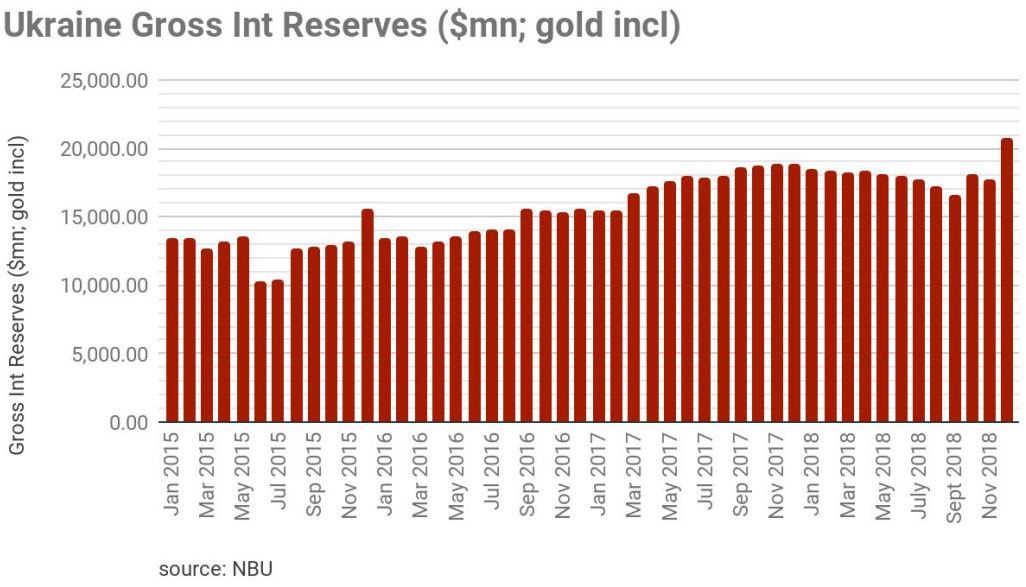
In February, Ukraine's government will face high debt repayments in foreign currency. It will have to repay around $440mn to the International Monetary Fund (IMF) and $745mn to the holders of local Eurobonds.

These outlays will be partially compensated by expected inflows of $600mn from international borrowing in February that will be secured by a guarantee of the World Bank, as reported by the finance ministry, Akhtyrko added.

At the same time, the foreign currency inflows from the new placements of local Eurobonds are not likely to be essential, as the latest local bond placement revealed the low capacity of local market players to generate foreign currency inflow through the purchase of local Eurobonds, the expert believes.

February's level of reserves will largely depend on the amount of foreign currency the NBU will buy at ForEx during the month. The current appreciation of the UAH/USD exchange rate (2.7% YTD) gives the central bank a solid opportunity to replenish its reserves this way, Akhtyrko added.

Concorde expects the balance of foreign currency flows in February will be negative, and gross reserves are likely to lose $100mn-$200mn.


Ukraine Gross Int Reserves ($mn; gold incl)
Gross Int Reserves ($mn; gold incl)
25,000.00
20,000.00
15,000.00
10,000.00
5,000.00
0.00
Jan 2015
Mar 2015
May 2015
Jul 2015
Sep 2015
Nov 2015
Jan 2016
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Jul 2016
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July 2018
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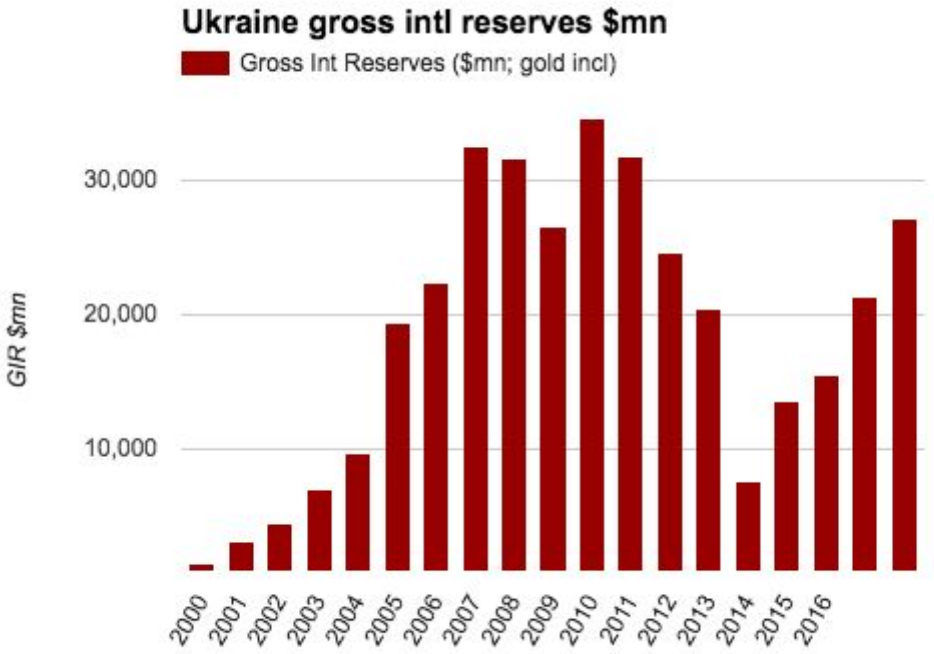
Nov 2018
source: NBU


Ukraine gross intl reserves $mn
Gross Int Reserves ($mn; gold incl)
GIR $mn
30,000
20,000
10,000
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016

5.3 FDI

FDI	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017 F	2018 F	2019 F
Net FDI (US$bn)	9.2	9.9	4.7	5.8	7	7.2	4.1	0.3	2.9	3.4	4.3	4.3	4.3
Net FDI (% of GDP)	6.4	5.4	4.1	4.2	4.3	4.1	2.3	0.2	3.3	3.7	4.3	3.9	3.5
C/A bal. + net FDI (% of GDP)	2.8	-1.6	2.6	2	-2	-4.1	-6.9	-3.3	3.1	0.3	1.6	-0.3	-0.1

Source: ICU

Ukraine net FDI grows $690mn in 2018, **but investment needs are ten-times higher**

The stock of foreign direct investment (FDI) into Ukraine in 2018 grew 2.2% y/y to $32.3bn as of end-2018, or a net increase of $0.69bn, the State Statistics Service reported on February 28.

At the same time the increase in FDI in 2017 was revised upwards to $380bn while the 2014-2016 drop in FDI stock was reduced $22.5bn.

Gross 2018 FDI inflow amounted to $2.87bn, while the outflow was $0.97bn. The agency wrote off $1.22bn from inflows due to exchange rate fluctuations, omissions, and changes in classification. In 2017, gross FDI inflow amounted to $2.51bn, while the outflow was $0.76bn.

In 2018, the Netherlands ($1.2bn), Cyprus ($0.5bn), and Russian Federation ($0.5bn) were the leading sources of investment to Ukraine in 2018. The top recipients were the finance ($1.2bn), trade ($0.6bn), and real estate ($0.4bn) sectors.

Ukraine's foreign direct investment totalled $2.5bn in 2018, reports the National Bank of Ukraine. About $1.5bn of the total went into the real sector. For an economy the size of Ukraine's -- $125bn – foreign direct investment should be five times higher, over $12bn economists say.

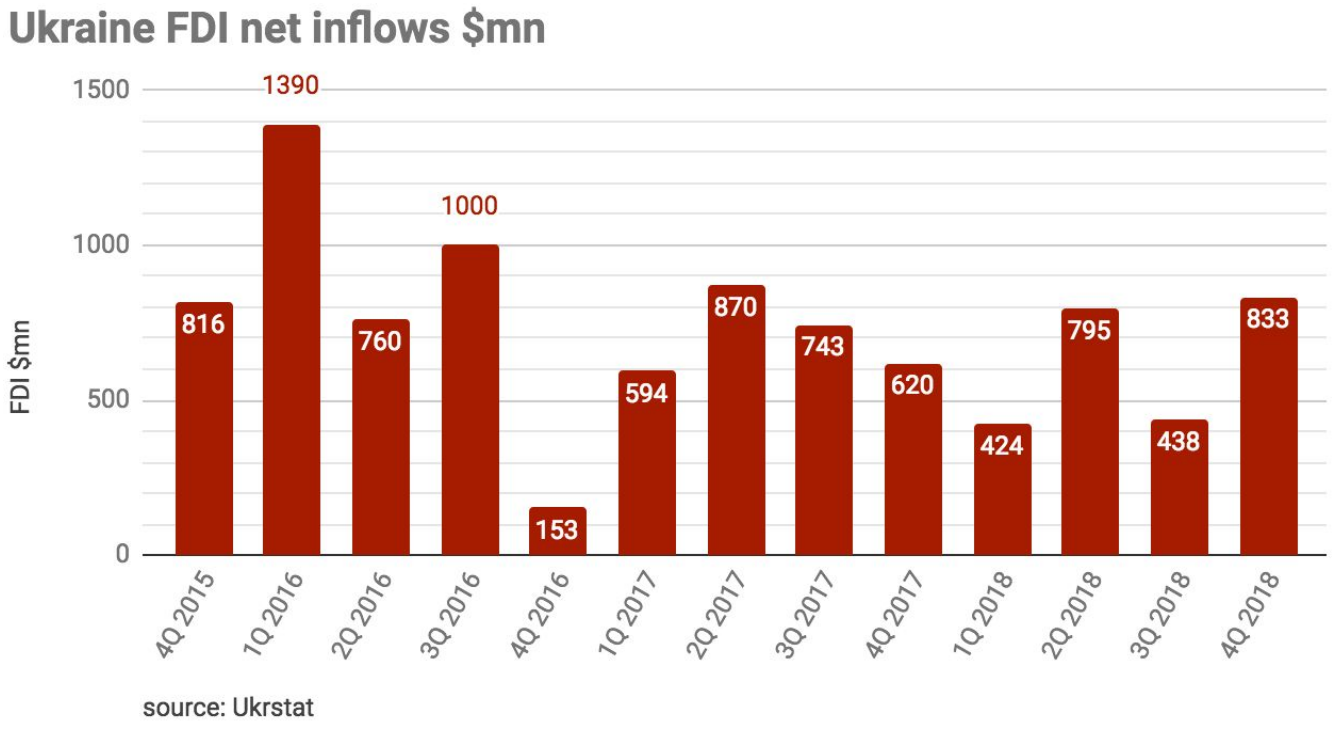
Ukraine's Finance Minister Oksana Markarova says Ukraine needs over $10bn in investment annually to accelerate its economic growth, which is 4-5 times up from the current investment. "Now we are attracting $1.5bn - $1bn - $3bn a year. This is not enough for a country and economy like ours. These investments should be plus $10bn," she told a Ukrainian TV channel on February 18 as cited by Unian. According to the minister, effective privatization of state property and a better business climate are required to attract such investment. The foreign direct investment in Ukraine's economy in 2018 was estimated at $2.5bn, with 60% of this amount channelled into the real sector, according to the National Bank of Ukraine (NBU).

Mergers and acquisitions increased by 78% in 2018 year over year, to $1.8bn, KPMG reports in its annual Ukraine M&A Review. The number of deals increased by 19%, to 80. Foreign investment increased by 47% to

$508mn in 25 transactions. “The Ukrainian economy is recovering” says the report. Noting the two elections this year, KPMG predicts that foreign investment growth in 2019 will be “modest.” “Ukraine is now on the verge of change,” the report says. “And if reforms continue, the number of mergers and acquisitions will only increase with the growing number of foreign investors considering access to the local market.”

New foreign direct investment in Ukraine was $1.9bn in 2017, the State Statistics Service said. About one quarter, or $506mn, was from Cyprus, presumably offshore Ukrainian or Russian money. The next four sources were: Russia -- $396mn; the Netherlands -- $262mn; Britain -- $212mn; and Germany -- $119mn.

Despite the lack of a farm land market, agriculture attracted the highest portion of foreign investment. Saudi Agriculture and Livestock Investment Company, or SALIC, bought Mriya Agro Holding for a reported $242mn. Switzerland’s Julius Baer paid $73mn for a stake in Kernel Holdings. Japan’s Sumitomo paid $45mn for a controlling 51% stake in Spectrum-Agro and Spectrum Agro-Engineering. Noting last year’s record 70mn ton grain harvest, KPMG says: “International investors are even more closely looking at the Ukrainian agricultural sector.”



6.0 Public Sector

6.1 Budget

Budget and debt indicators	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018F
State budget revenues, UAH bln	231.7	209.7	240.6	314.6	346	339.2	357	519	616.3	724	905.2
% of GDP	24.4%	23.0%	22.3%	24.2%	24.6%	23.2%	22.8%	26.9%	26.2%	26.3%	25.8%
State budget expenditures, UAH bln	244.2	245.2	304.9	338.1	399.4	403.9	435	552	686.4	806	1,001
% of GDP	25.8%	26.8%	28.3%	26.0%	28.4%	27.6%	27.8%	29.2%	28.9%	29.3%	28.5%
State budget balance, UAH bln	-12.5	-35.5	-64.3	-23.6	-53.4	-64.7	-78	-33	-70.1	-82	-96
% of GDP	-1.3%	-3.9%	-6.0%	-1.8%	-3.8%	-4.4%	-5.0%	-1.7%	-3.0%	-3.0%	-3.0%
Public debt, UAH bln	189	318	432	473	516	584	1,101	1,594	1,930	2,175	2,285
% GDP	20.0%	34.8%	40.1%	36.4%	36.7%	39.9%	70.3%	82.7%	82.1%	79.0%	65.2%

Source: SP Advisors

6.1.1 Budget dynamics - results

Ukraine's general budget switched to a surplus of UAH268mn ($10mn) in January from a UAH88.3bn deficit in December, the State Treasury reported on February 26.

General budget revenue increased 3.6% year-on-year to UAH73.9bn (vs 18.6% y/y growth in December). Budget expenditures surged 46.2% y/y to UAH73.7bn, speeding up from 19.6% y/y growth in December.

Tax revenue inched up 2.1% y/y (vs 13.3% y/y growth in December). In particular, net VAT revenue plummeted 66.1% y/y after 48.3% y/y growth in December. The decline was due to a 64.2% y/y surge in VAT reimbursement to exporters, while gross VAT revenue climbed 8.4% y/y, keeping the same growth rate as in December.

At the same time, personal income tax revenue accelerated to 22.8% y/y growth from a 19.7% y/y rise in December. In addition, the enterprise profit tax surged 52.1% y/y (vs. 30.8% y/y decline in December). Non-tax revenue increased 21.9% y/y (vs a 42.1% y/y surge in December).

The growth of non-tax revenue was mostly due to unclassified "other" revenues. Meanwhile, income from ownership and entrepreneurship declined 6.9% y/y after a 74.6% y/y surge in December.

Evgeniya Akhtyrko at Kyiv-based brokerage Concorde Capital wrote n a note on February 28 that the accelerated growth of budget expenditures is not a surprise as presidential elections are approaching. At the same time, budget revenues do not look very promising.

"VAT reimbursement to exporters is rising amid growing exports of agricultural produce," she added. "And we cannot ule out a situation in, which the government might resort to the practice of delaying VAT reimbursement in order to have more budget revenues in the short term."

Ukraine's budget ended 2018 with a deficit of UAH66bn ($2.4bn) or 1.7% of GDP, that comfortably meet the International Monetary Fund (IMF) demands to hold the deficit to not more than 2.5%, the treasury reported on January 28.

The end of year general budget deficit was recorded after the government's finances swung from profit to loss in the last two months of the year. The government reported a deficit of UAH88.3bn in December that followed from a surplus of UAH7.1bn in November, the State Treasury said.

The budget revenue increased 18.6% y/y to UAH109bn in December, slowing from 21.6% y/y growth in November. Budget expenditures rose 19.6% y/y to UAH198bn, speeding up from 16.7% y/y growth in November.

Tax revenue increased 13.3% y/y, slowing from 21.8% y/y growth in November. In particular, enterprise profit tax revenue dropped 30.8% y/y after 32.4% y/y growth in November. Personal income tax revenue slowed to 19.7% y/y growth from a 26.2% y/y improvement in November. Meanwhile, net VAT revenue jumped 48.3% y/y (vs. a 16.6% y/y decline in November) due to an 11.4% y/y decline in VAT reimbursement.

Non-tax revenue surged 42.1% y/y, speeding up from 21.6% y/y growth in November. In particular, income from ownership and entrepreneurship swelled 74.6% y/y (vs. 33.8% y/y growth in November).

All-in-all the budget posted a deficit of UAH65.9bn in 2018 amid revenue growth of 16.5% y/y and an expenditure increase of 18.3% y/y. The budget revenue met 98.6% of the 2018 plan in 2018, while expenditures were at 93.7%.

In related news, the State Treasury on January 30 reported that the state budget deficit amounted to UAH59.2bn in 2018, while the law on the state budget assumed a deficit of UAH94.1bn.

"We expected the budget deficit to swell in the last month of the year given the cautious budget spending through the most of the year. The drop in VAT reimbursement is a bit worrisome. The extension of this trend is likely to mean that the government returned to its poor habit of delaying VAT reimbursement to exporters," Evgeniya Akhtyrko of Concorde Capital said in a note. "The 2018 state budget deficit amounts to 1.7% of GDP, according to our estimates, which comfortably meets the IMF-required threshold of 2.5% of GDP."

Ukraine's state budget revenue declined 1.3% y/y to UAH55.2bn in January, which is 10.8% y/y below plan, the State Treasury provisionally reported on February 1. Net tax revenue declined 13.7% y/y to UAH19.9bn (27.8% below plan) amid a VAT reimbursement surge of 64.2% y/y. Customs revenue declined 10.4% y/y to UAH22.5bn (11.8% below plan). Other budget revenue increased 15.5% y/y to UAH1.3bn (37.7% above plan). Local fiscal revenue improved 20.8% y/y to UAH19.0bn, but underperformed plan by 5.6%.

Social payments (pension and other social fund contributions paid by employers) advanced 26.1% y/y to UAH19.1bn. Evgeniya Akhtyrko: The government improved its VAT reimbursement in January after underpayments in December. As for customs collections, uneven month-to-month revenue is a usual event reflecting the Ukrainian practice of "manual" management, as well as high corruption in this realm. So the poor customs performance in January is likely to be compensated by a better "performance" the next month.

6.1.2 Budget dynamics - funding

Ukraine's Finance Ministry is planning to attract UAH17.6bn (over $600mn) from international borrowing in February that will be secured by a guarantee of the World Bank, the ministry reported on Feb. 1. Initially, the ministry planned to raise funds in January. But instead, it reported that it replaced it with $587mn and EUR 33mn from the placement of local Eurobonds in January. Of the raised amount, the biggest portion was drawn from bonds maturing on Feb. 21 ($287mn in par value). Recall, the World Bank provided a $750mn loan guarantee to Ukraine on Dec. 18. Ukraine's MinFin used half of the guarantee to attract EUR 349mn in loans in late December.

U**kraine on February 28 raised a loan of €529mn from Deutsche Bank under the guarantee of the International Bank for Reconstruction and Development** (IBRD, the World Bank Group), according to the website of the Ministry of Finance. The funds were received in two tranches: an A tranche in the amount of EUR240mn with maturity in four years and a B tranche in the amount of EUR289mn with a final maturity in ten years (four years and six months after raising the funds, the loan is subject to gradual repayment with certain amounts every half a year). The second part of the guarantee in the amount of $375mn in the euro equivalent of the total amount of the World Bank guarantees of $750mn was used for the loan. As reported, the World Bank Board of Executive Directors on December 18, 2018 approved the provision of guarantees to Ukraine in the amount of $750mn in support of state policy.

Within two months, Ukraine hopes to win the second tranche of EU €500mn macro financial aid, Finance Minister Oksana Markarova told reporters at Dragon. At the same time, she is negotiating a new loan guarantee with the World Bank and new low interest loans with G7 countries. In December, the World Bank extended a $750mn guarantee, enough for the government to borrow $1bn at low rates. "Our priority is concessional lending," Markarova said. She aims to use low interest loans to help Ukraine lower its indebtedness to 50% of GDP by 2021.

President Trump has signed bills that increase aid to Ukraine to nearly $700mn, Ukraine's Embassy in Washington writes on Facebook. In February, USAID launched an $85mn program by TetraTech, a US-based engineering firm, to help implement free market changes and incentives to promote natural gas production, energy conservation, and renewable energy investment.

6.1.3 Budget dynamics - privatization

Ukraine's State Property Fund announced on January 28 that it lost its appeal against a court ruling that prohibits the fund from signing contracts with financial advisers selected to help arrange the privatization of five large

state companies. The fund will appeal this ruling, said Head Vitaliy Trubarov in the January 28 statement.

The fund completed tenders to select privatization advisers for six state companies in July 2018. Later on, the selection of the advisers of five of these companies was appealed in the courts by one of the tender's losers, prompting the courts to forbid the fund and Cabinet to sign contracts with the four winning firms.

Trubarov has characterized the litigation as an attempt to wreck the Big Privatization under the new progressive legislation approved in January 2018. This law requires the selection of advisers under the fund's tender procedure. The only company whose majority stake is being privatized under the old legislation is power GenCo Centrenergo, for whom the process started before the new law was adopted.

So far only one asset -- the President Hotel -- is being actively prepared for privatization with the involvement of its adviser, Concorde Capital.

"The hotel is among the smallest of assets on the privatisation list. If the courts continue to block the government from signing contracts with its advisers, the chances that Ukraine will reach its UAH17.1bn privatization target for 2019 (or even the IMF's expected level of UAH10.5bn) will fade," Alexander Paraschiy of Concorde Capital said in a note.

"The last time Ukraine met its budgeted privatization plan was in 2011, so the possible underperformance this year won't be surprising. At the same time, the failure to launch the Big Privatization campaign, as had been promised by the government in its recent memorandum with the IMF, may weaken the government's negotiating leverage with IFIs," Paraschiy added.

Ukraine's battered Odesa Port Plant (OPP) could be transferred to the management or lease to the nation's state-owned natural gas monopoly Naftogaz or the Agrarian Fund, head of Odesa regional state administration Maksym Stepanov believes. According to the official, such measures will contribute to the launch of the plant "not for a month or two, but for a long time", Interfax news agency reported on February 22. Stepanov added that possible transfer of the plant to the management or lease to the Agrarian Fund was discussed with the government in Kyiv earlier this month. Ukrainian and foreign investors have no interest in privatisation of OPP due to its disastrous financial conditions. In 2018, the starting price in the privatisation of OPP has been cut by 10-times to $54mn, however, even now there are serious doubts that the government will be able to sell its 99.567% stake in OPP. In December, Kyiv failed to sell the stake via a second privatisation tender.

6.2 Debt

DEBT	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017E*
External debt (US$bn, eop)	80	101.7	103.4	117.3	126.2	134.6	142.1	126.3	118.7	113.6	124.2
External debt (% of ann'd GDP, eop)	55.8	55.3	91	86.1	77.4	77.3	79.1	96.2	130.4	121.7	126.6
FX reserves (US$bn, eop)	32.5	31.5	26.5	34.6	31.8	24.5	20.4	7.5	12.4	11.9	15.6
FX reserves (% of ann'd GDP, eop)	22.6	17.2	23.3	25.4	19.5	14.1	11.4	5.7	13.6	12.8	13.3
External debt / FX reserves (x, eop)	2.5	3.2	3.9	3.4	4	5.5	7	17.7	9.6	9.5	8.0
FX reserves imports cov (months)	5.6	3.9	5.9	6	4.1	2.9	2.5	1.3	3.3	3.6	3.3

Source: ICU

Ukraine's state and state-guaranteed debt stayed flat at $78.3bn in January, the nation's Finance Ministry reported on February 25. A rise in state domestic debt was offset by declines in state-guaranteed foreign debt. In particular, the state domestic debt increased 0.2% m/m to $27.bn. Meanwhile, state-guaranteed debt dropped 1.1% m/m to $10.6bn. State foreign debt remained flat at $39.7bn. In UAH terms, overall state debt increased 0.2% m/m as domestic state debt rose 0.5% m/m and state foreign debt inched up 0.2% m/m. Evgeniya Akhtyrko at Kyiv-based brokerage Concorde Capital wrote in a research note on February 2t that state domestic debt increased in January as newly attracted government debt from the placement of local bonds exceeded redemptions. Specifically, the newly placed domestic debt reached UAH41.7bn while repayments amounted to UAH36.9bn. "Meanwhile, the state-guaranteed debt declined mostly due to reduced positions with several foreign banks," Akhtyrko added. "The increase of state debt in UAH terms was mostly due to a 0.3% depreciation of the national currency in January." Concorde projected state and state-guaranteed debt will increase to $80.8bn in 2019, or to around 62% of GDP. According to its estimate, state debt amounted to 61.5% of GDP in 2018.

Ukraine needs to pay off more than $15bn of its state debt in 2019, the Ministry of Finance said in a macroeconomic report, released on February 14. "State debt payments will peak in 2019-2021. The overall state debt payments due in 2019 are set at UAH417bn ($15.4bn), including about $9bn to be paid in foreign currencies," the report says. Internal debt payments will total UAH150.5bn ($5.57bn) and foreign debt payments, UAH121.8bn (4.5bn). Another UAH145.4bn ($5.4bn) is to be paid for servicing the internal and foreign debt. The Ministry of Finance vows Ukraine will manage to further reduce the state debt against the country's GDP. At the end of 2018 the ratio stood at 62%. The ministry says a 60% debt-GDP ratio is safe.

The state guaranteed debt of Ukraine fell from 71.8% to 62.7% of GDP in 2018, according to the Finance Ministry's preliminary estimates released via Facebook on January 31.

The Finance Ministry says that the aggregate state debt grew by UAH26.94bn in hryvnia's, to UAH2.169 trillion and by $2bn in US dollars, to $78.3bn in 2018.

The ministry said that direct state debt by the end of 2018 was 85.8% of the state guaranteed debt.

At the end of August 2018, the government of Ukraine reviewed the medium-term strategy of public debt management by setting more ambitious goals to reduce the direct state debt and GDP ratio, in particular, to 60% of GDP by the end of 2018, instead of the previously planned 62% of GDP. The figure should be cut to 52% by the end of 2019 and to 49% by 2020, the ministry says as cited by Interfax Ukraine.

Ukraine's state debt for the period of 2017 increased by 11.1%, to UAH1.834 trillion, or $65.3bn, foreign debt alone rose to $38.5bn. However, the ratio of the debt to the country's GDP decreased from 69.2% to 61.5%. If government-guaranteed debt is included, the ratio fell from 80.9% of GDP to 71.8% of GDP.

Ukraine's state and state-guaranteed debt rose 4.8% m/m to $78.3bn in December, the Finance Ministry reported on January 25.

The state domestic debt rose 5.3% m/m to $27.5bn, while foreign debt increased 2.1% m/m to $39.7bn. In addition, state-guaranteed debt jumped 14.1% m/m to $11.1bn.

In UAH terms, overall state debt increased 2.2% m/m as state-guaranteed debt rose 11.3% m/m. Meanwhile, state debt in UAH terms almost did not change as the increase of state domestic debt by 2.7% m/m was offset by the decline of state foreign debt by 0.5% m/m.

In 2018, state and state-guaranteed debt rose 2.6% y/y in dollar terms. In particular, state foreign debt increased 3.2% y/y and state domestic debt rose 2.4% y/y. State guaranteed debt increased 14.1% y/y.

"The surge in December state debt was prompted by Ukraine receiving a $1.38bn loan tranche under the 14-month IMF stand-by arrangement. In turn, that enabled the World Bank to provide a $750mn financial guarantee for the loans Ukraine is intending to attract in 2019 from Western financial institutions," Evgeniya Akhtyrko of Concorde Capital said in a note.

"As a third factor, MinFin intensified domestic borrowing with the placement of local bonds (including local Eurobonds) to deal with traditional surge of government spending in the end of the calendar year. Meanwhile, the lower growth rate of the state debt in UAH terms is explained by the 0.5% appreciation of the Ukrainian currency in December," Akhtyrko added.

The 2018 year-end state and state-guaranteed debt of $78.3bn was 61-62% of GDP vs. 71.8% of GDP in 2017, according to Concorde Capital's estimate.

Economists project state and state-guaranteed debt will increase to $80.8bn in 2019, or around 62% of GDP.

7.0 FX

Exchange rate	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Official UAH/USD (eop)	7.7	7.99	7.96	7.99	7.99	7.99	15.77	23.41	26.20	27.52
Official UAH/USD (avg)	5.27	7.79	7.94	7.97	7.99	7.99	11.89	21.84	22.55	26.60

Source: CEIC

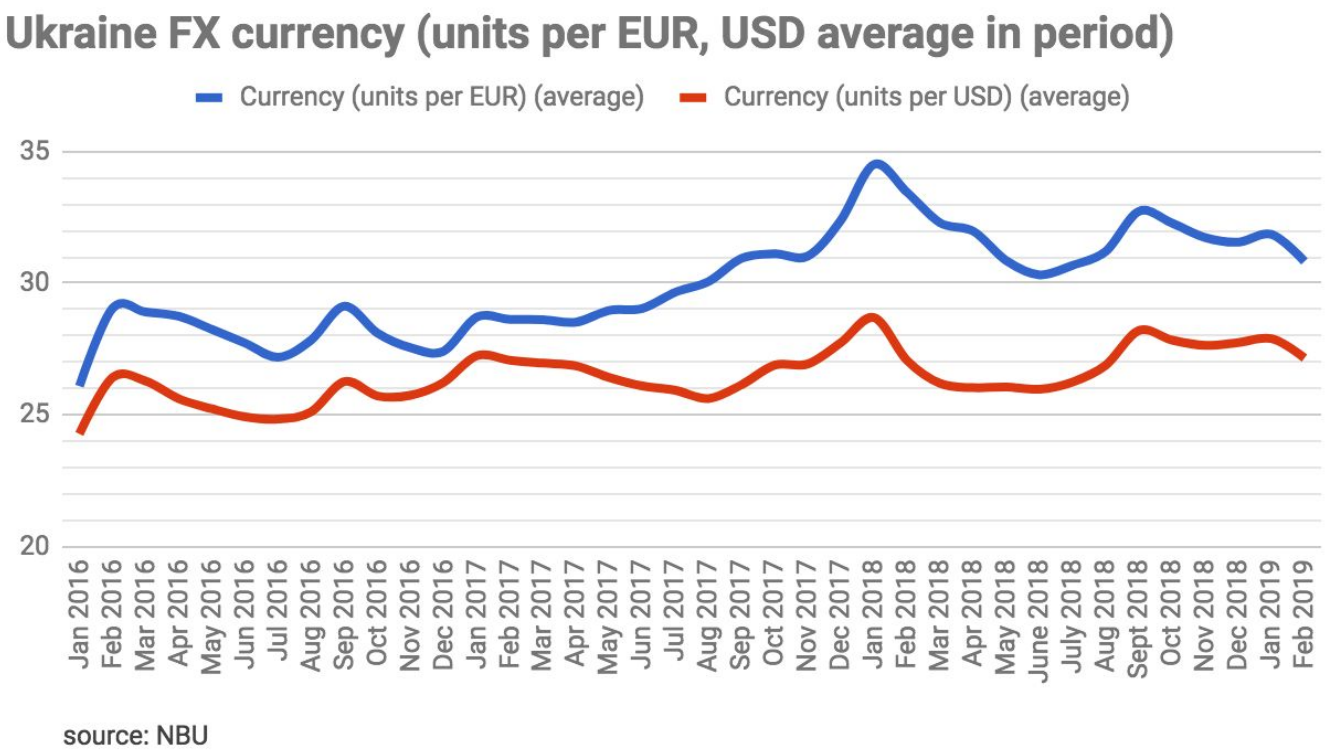
Wage remittances to Ukraine from labour migrants hit $11bn last year, according to Ekateryna Rozhkova, first deputy head of the National Bank of Ukraine. Assuming this figure is accurate, it means that money sent home by Ukrainians working outside the country increased by 50% since the summer of 2017, when the EU adopted a 'no visa' policy for 90-day stay stays by Ukrainians.

Farm exports account for 39% of foreign currency entering Ukraine, Prime Minister Groysman told the Cabinet of Ministers on February 13. President Poroshenko told the Dragon conference Tuesday that a key challenge for the 2020s is for Ukraine to add value to farm exports by increasing processing.

By sending $1bn a month home, Ukrainians working abroad maintain the hryvnia exchange rate little changed and offset Ukraine's growing trade deficit. This flow – far larger than IMF aid and foreign direct investment combined – gives the government breathing room to adopt market reforms that will stimulate real investment, experts tell UNIAN in a lengthy analysis. In a race against time, the government must create conditions for creating jobs with decent pay -- or risk losing 'temporary' migrants to permanent residence in the EU, the report warns.

Last year, 7-9mn Ukrainians worked outside the country, half of them living abroad permanently, according to the Social Policy Ministry. Separately, about one third of 40,000 Ukrainians surveyed in December by Rating polling group would like to get a job outside the country. Of these one half would like to earn enough money to come home and start a small business here, Alexey Antipovich, director of Rating, told a migration roundtable in Kyiv last week.

Starting Friday March 1, the central bank cuts the mandatory amount of foreign currency that businesses must sell for hryvnia to 30% of export earnings, from 50% today, Churiy said. Without specifying dates, he said the Bank will eventually abolish this limit and the limit of on repatriation of dividends. As a first step on dividend repatriation, he said the bank plans to raise the monthly limit to €10mn, from €7mn today.



8.0 Financial & capital markets

8.1 Bank sector overview

One quarter of Ukraine's 77 banks – 20 small and medium entities – are 'unviable', reports the National Bank of Ukraine. After a study of the market's 40 small and medium banks, Ekateryna Rozhkova, the the bank's First Deputy Governor, reports: "The main problem for small banks is the lack of a development strategy and, as a result, the unviability of the business model. Another important issue is the source of funds to support the bank's capital." After the 2014 financial crisis, the central bank closed half of Ukraine's banks.

Ukrainian banking sector reported UAH21.7bn (around $80mn) of net profit in 2018 following a net loss of UAH26.5bn a year ago, the National Bank of Ukraine (NBU) said in a statement published on February 7.

The country's banking system has return to profitability for the first time since 2013. Ukraine's central bank has transformed the entire banking sector of Ukraine after years of massive fraud over the past three years. The NBU has withdrawn the licences of around 100 lenders, many of them due to their involvement in money laundering, stealing depositors' money or for having a non-transparent ownership structure.

According to the NBU's first deputy governor Kateryna Rozhkova, the intensification of lending has added to the 2018 result, primarily retail in national currency, which increased by more than 30%.

At the time, the decline in interest rates on deposits of individuals during most

of the year and a significant reduction in allocations to reserves contributed to profitability of the banking sector. Analysts expect that the year 2019 will also be successful as lending will continue growing.

In 2018, the amount of payments to reserves more than halved, to UAH 23.7bn in 2018 from UAH49.2bn in 2017.

At the same time, the net interest and commission fee income of the banking system increased by an average of 38%. The main interest income, as before, is generated by corporate loans - 46% of the total amount, while investment in securities provided 27% of interest income, and retail loans - 26%. Commission fee incomes increased against the background of the development of cash settlement and other related lending payments, to 25% in the structure of all revenues.

Monetary and banking indicators	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**Jan-Sep 2017**
Non-performing loans, USD bn	57.23	63.90	67.87	81.48	70.48	64.53	63.00	65.93
Non-performing loans ratio	14.8	15.2	29.6	14.5	15.9	25.6	30.4	56.4
Total deposits, USD bn	608.3	741.5	831.3	984.7	729.5	415.0	380.6	362.4
Loan-to-deposit ratio	175%	162%	143%	135%	152%	151%	127%	119%
Capital adequacy ratio	20.6	19.2	18.0	18.1	15.6	9.2	13.0	13.8
Liquid asset ratio	18.8	18.6	22.1	20.6	26.4	33.0	48.5	53

8.1.1 NPLs

Rapid development of consumer lending reduced the non-performing loans portfolio of Ukrainian banks in October-December 2018 by 1.7 percentage points (pp) to 52.8%, the National Bank of Ukraine (NBU) said in its February's banking sector review.

The high NPL rate remains a major challenge for the Ukrainian banking sector, particularly, in state-owned banks, and was caused by the financial and economic crisis of 2014-2016. In 2018, the NBU urged bankers to step up their efforts to workout NPLs.

Over the past two years, the NPL share in five largest foreign banks has reduced by 2.7 times, to 13.9%. However, state-owned banks and banks with Russian capital have reported no progress in reducing nonperforming loans while accounting for 83% of the total NPLs, the review reads.

Since the beginning of 2019, the new rule has been applied for depreciation of collateral for loans remaining non performing for over two years. "Complete depreciation of collateral for the loans during the next two years will result in complete coverage of nonperforming loans with prudential provisioning," the central bank added.

Ukraine's Oschadbank makes most progress dealing with NPLs in 2018 but bad loans remains a big problem for the sector

Ukraine's banking sector returned to profit in 2018, but the sector is still not out of the woods as non-performing loans (NLPs) are still above 50% and represent a danger for the financial system.

Of all Ukraine's banks, the former Soviet-era savings giant Oschadbank (State Savings Bank of Ukraine) made the most progress in reducing the amount of bad loans on its books last year.

Ukraine's Finance Ministry addressed the progress of the four state banks in dealing with NPLs in 2018 in a report released on February 28, of Concorde Capital said in a note.

Regular reporting on state bank's NPLs is part of Ukraine's commitments to the International Monetary Fund (IMF) under the new stand-by loan program that was adopted at the end of last year.

According to the report, the four banks cut the amount of their overdue loans by UAH4.88bn ($181.8mn) in 2018 by collecting money from debtors through foreclosure and/or sale of pledged assets, including a UAH2.96bn reduction by Oschadbank and UAH0.41bn contraction by Ukreximbank.

The banks restructured UAH20.91bn in bad loans in 2018, including UAH16.03bn by Oschadbank and UAH0.23bn by Ukreximbank.

As of the beginning of 2019, Oschadbank had UAH97.9bn in NPLs (67% of gross loans). The value of NPLs at Ukreximbank was UAH83.7bn (59% of gross loans), the nationalized Privatbank had UAH224.8bn (83%) and Ukrgazbank had UAH8.8bn (17%).

The total amount of NPLs at four state bank was UAH435.2bn at the beginning of 2019, with contributions from Privatbank, Oschadbank and Ukreximbank being 56%, 23% and 19%, respectively.

"The data suggest that Oschadbank made the most progress among the four state banks in dealing with bad loans. Its share of the total amount of reduced overdue loans was 61%, while its share in total bad loan restructuring was 77%. The bank's balance sheet remains far from being perfect, but its progress promises it will be able to restructure or get repaid some portion of its bad loans this year as well (recall that in recent months, it announced another deal to restructure UAH4.4bn in debt to Ukrlandfarming). That allows us to remain bullish on OSCHAD Eurobonds," Alexander Paraschiy of Concorde Capital said in a note.

8.1.2 Bank news

Russia's retail banking powerhouse Sberbank increased the authorized capital of its Ukrainian subsidiary bank by UAH3.3bn ($122mn), or by 15.9%, to UAH24.065bn, the bank said on February 12. As a result of the increase in the authorized capital, the bank has formed additional reserves for loans, as well as increased capital adequacy, the bank said. Sberbank last year returned a loss of UAH7.6bn, after it was sanctioned by the National Bank of Ukraine (NBU). In January, the NBU fined the Ukrainian daughter bank UAH94.737mn for "risky activities." Sberbank is appealing the penalty in court. Sberbank established a subsidiary bank in Ukraine in 2001. According to the Ukrainian regulator, as of December 1 of last year, the bank held 11th place in the Ukrainian banking system in terms of net assets of UAH31.824bn.

Ukraine's state-owned Privatbank has secured a partial award in its favour in the Permanent Court of Arbitration at the Hague, where the lender is challenging Russia's expropriation of the bank's investments in Ukraine's Crimea.

Specifically, the arbitral tribunal found that it has jurisdiction over all of PrivatBank's claims against Russia, that Moscow breached its obligations under the Ukraine-Russia bi-lateral investment treaty by unlawfully expropriating PrivatBank's investments in Crimea, and that PrivatBank is entitled to full compensation for that expropriation, the bank said in a statement e-mailed to *bne IntelliNews* on February 15.

The arbitral tribunal reserved for the next phase of the arbitration the question of how much compensation is due to PrivatBank for Russia's "unlawful actions". PrivatBank seeks compensation in excess of $1bn.

In 2018, the International Court of Arbitration in Paris has ruled that the Russian government should pay compensation of $1.3bn for losses caused by the illegal military annexation of Crimea in 2014 to Ukraine's second biggest lender Oschadbank. Oschadbank filed a lawsuit in August 2016 with claims for the recovery of lost assets and remuneration for the lost of business and payable interest caused by Russia's take over of the peninsula.

Russia refuses to recognise the ruling, as it believes the court had no authority to consider Oschadbank's claim against Russia.

The move followed another Oschadbank lawsuit worth UAH15bn ($589mn) filed in 2015. Earlier, the Ukrainian leadership urged all Ukrainian state-owned companies to follow the example of Oschadbank and recover damages for the annexation of Crimea and the loss of Ukrainian property.

Canada's Fairfax Financial Holdings has bought France's AXA Insurance (Kyiv) for $16mn. In Ukraine's insurance market since 2007, AXA has 780 employees and 1,220 agents in Ukraine. At the end of last year, the company collected $68mn in insurance premiums. Toronto-based Fairfax has $65bn in total assets and an investment portfolio of $39bn.

8.2 Central Bank policy rate

The National Bank of Ukraine (NBU) kept the monetary policy interest rate on hold at 18% at its regular meeting on January 31, after the central bank had hiked the rate three times last year to battle persistent inflation.

Ukraine ended 2018 with inflation of 9.8% after it ticked up again at the end of the year, but the regulator set its target rate for inflation to 5%.

However, the regulator kept its October forecasts for the actual rate of inflation in 2019 to 6.3% from 9.8% in 2018.

"Inflation will continue to slow down gradually. As before, the NBU expects that it will fall to 6.3% by the end of 2019 and by 5.0% by the end of 2020. In addition, as it is planned earlier, by the beginning 2020, inflation will fall within the target range - 5% +/- 1 percentage point (p.p.)," the central bank reported on its website.

The last time the NBU cut rates was in May 2017 and the government was unhappy with the growth-killing hikes last year. But the NBU earned itself some kudos and demonstrated its independence from the government by hiking rates.

Some analysts polled by Reuters had expected a more benign inflation trend to prompt a cut. Inflation dropped into single digits at the end of last year.

The bank "has decided to keep its key policy rate at 18.0% per annum. The rate was maintained at the same level in order to drive inflation down to the target of 5% in 2020," the NBU said in a statement as cited by Reuters.

The central bank also announced a slight downward revision to its economic growth forecast for 2018 to 3.3% from 3.4% but kept its 2019 forecast unchanged at 2.5%.

It said that uncertainty caused by Ukraine holding elections this year posed a risk to its forecasts. It also said further planned increases in gas prices would impact inflation.

Eight of 15 analysts polled by Reuters had predicted a rate cut, while the other seven believed the central bank would hold fire ahead of a presidential election on March 31.

In related news the finance ministry said it will issue $2bn of Eurobonds in 2018, Deputy Central Bank Chief Dmitry Sologub told a press briefing.

Ukraine's NBU says room to cut rates if inflation targets are met. There is scope for the National Bank of Ukraine (NBU) to cut monetary policy rates if inflation falls into its target range, Central Bank Governor Yakiv Smolii said at a

conference on February 12.

Smolii expects inflation to ease to 6.3% in 2019. Inflation was 9.2% year-on-year in January, down from 9.8% in December and is expected to continue to fall this year to 5-5.5%. The central bank kept its key rate unchanged in January to help bring inflation down.

The minutes of the meeting revealed that eight committee members called for keeping the key rate unchanged at 18.0%, while only one member called for lowering it by 0.5pp to 17.5%.

The monetary committee members noted that keeping the key policy rate at 18.0% addresses the need to control inflation and reach the mid-term inflation target of 5% y/y in 2020. The NBU still sees risks that could prevent inflation from cooling to levels assumed by the central bank's forecast. In particular, the central bank cited uncertainty related to the election process, which might result in worsening inflationary pressures.

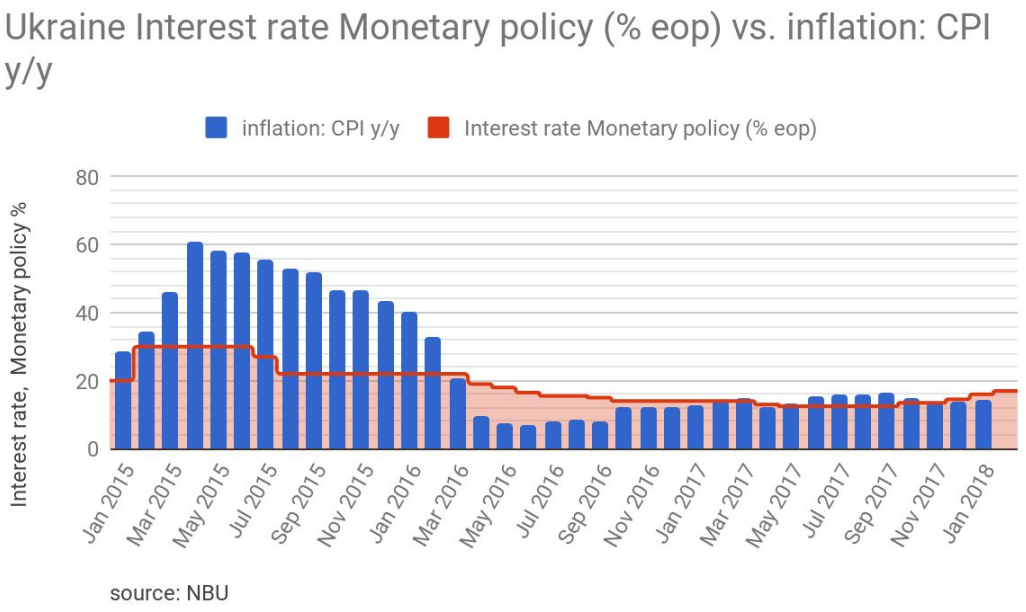
In addition, the majority of the committee noted that the current tight monetary policy should be able to counteract fundamental inflationary pressures. The decline of core inflation is slow amid high consumer demand fuelled by fast-growing wages. The worsening terms of trade, geopolitical risks, and uncertainty in the gas transit sphere in 2020 were mentioned as major external risks to its inflation forecast.

The committee members don't rule out the possibility of a key policy rate hike in case the fundamental inflationary pressure rises or other pro-inflation risks emerge.

Nevertheless, the committee sees a number of positive factors that could serve as a basis for cutting the key policy rate. They include more lending under a new IMF-Ukraine financing program, a favourable situation on the foreign currency market, renewed interest of foreign investors in Ukraine's government securities, and lower prices for imported energy resources. The positive results of a lowered key policy rate include the revival of crediting and a reduced deficit in the balance of payments.

The only committee member who spoke out for lowering the key policy rate said the implemented monetary policy has already restrained inflation. Meanwhile, a lowered interest rate would be a positive signal for the market to improve its expectations.

"January consumer inflation cooling to 9.2% y/y is likely to add more arguments for lowering the key policy rate during the next committee meeting on March 13. Should the downward inflation trend strengthen in February, the NBU is likely to resort to cutting its key policy rate by 0.5pp," Evgeniya Akhtyrko of Concorde Capital said in a note.



8.3 Stock market

8.3.1 Equity market dynamics

Sentiment on emerging markets and Russia turning as EM funds have second biggest inflows ever

After a terrible year in 2018 sentiment towards emerging markets (EMs), and Russia in particular, seems to be turning more positive after EM bonds funds had their second best week on record in terms of inflows and equities also attracted new money, Slava Smolyaninov Executive Director Chief of BCS Global Markets reports.

“EM assets still got a lot of love last week as it proved second best on record for EM bond funds. Inflows into stocks stayed at a steady healthy level with no signs of overheating – unlike those of bonds,” Smolyaninov said in a note to investors.

The stock trading company EPFR Global released its fund flows data through the week ending February 12 that reports Russian assets saw circa $370mn of net inflows from combined equity and bond fund flows in the reported week compared to circa $240mn in the previous one, BCS reports.

While Russian bonds have been an investors favourite in 2017 and for half of 2018 as well, until the US Treasury Department (USTD) slapped sanctions on Russian aluminium producer Rusal and Congress threatened to target bonds with “crushing” sanctions this year. However, after these sanctions failed to appear at the end of last year and Russia just put in record current account and federal budget surpluses of 2018 the interest in Russian bonds is perking up again.

The USTD decided to drop the sanctions on Rusal completely in December 2018, which has improved sentiment further. And confidence just got another boost: Moody’s returned Russia to “investment grade” in February, completing

the hat trick of investment grade ratings from the leading ratings companies.

Russia's equity market has been range bound with the dollar denominated Russia Trading System (RTS) oscillating around the 1,000 market since Russia annexed the Crimea in 2014, although the market did re-rate in 2016, returning 50% y/y, after investors became convinced the sanctions regime would not get much worse. While there have been some stellar returns to be made at the corporate level as the crisis caused a consolidation in many sectors, the overall market has remained the preview of the brave and inflows have been depressed from boom-year levels.

That said, Russia-dedicated funds managed to attract circa $30mn in last week, largest inflows since mid-October, vs $1mn outflows in the previous week, BCS reports.

"Finally, Russia-dedicated funds got some new money last week, while inflows into GEM funds continued at a solid pace. This made overall inflows into Russian stocks almost reaching $200mn, largest weekly intake since April last year. However, this was still well below the overheated start of 2018 when weekly inflows were roughly twice as big. The beginning of the year was outstanding for EM assets, including Russia, so some pull back would be healthy at this stage. However, we remain tactically positive still," Smolyaninov said.

A combined circa $190mn flowed into Russian bond and stock funds last week, up from $160mn in the previous week, which is the biggest inflow since last April, says Smolyaninov.

Bonds remain the favoured vehicle, which also suggests that the recovering of sentiment remains early in the cycle as interest bonds typically leads equities by months, and even years, when Russia is recovering from one of its periodic crises.

The flows into Russia are set against the backdrop of rising enthusiasm for EM assets. The combined inflows into EM bond and stock funds was the highest in the last two years, according to EPFR Global's data.

The RTS closed at 1,218 at the end of January was trading at 1,194 as of February 12, which is a 14% gain year to date. Its sister index, the ruble denominated Moscow Exchange Index (MOEX), was up 7% year to date as of the middle of February.

Using *bne IntelliNews's* rule of thumb that the RTS index level should be simply x20 the price of Brent oil then the market is currently over valued by about 80 points. However, the average price of oil in January was $56.6, which compared to last year is low. Analysts don't expect oil prices too fall from here, but depending on Russia's continued participation in the OPEC+ oil production cut deal (the next meeting with OPEC is scheduled for May) then the price of oil could increase as the year wears on.

8.5 Fixed income

8.5.1 Fixed income - bond news

Ukraine's largest pipe producer Interpipe intends to offer its international creditors a ten-year value-recovery instrument (VRI) linked to the greater of EBITDA and CFADS (cash available for debt service), Debtwire reported on February 26, as cited by Concorde Capital. The payouts would amount to 15% of CFADS or EBITDA in years 1-4, 20% in years 5-7, and 25% in years 8-10, Debtwire said, adding that Interpipe would retain an early settlement option. In addition, Debtwire reported that the restructuring fee would amount to $5.9mn, and that there would be additional lockup fees for several classes of creditors. Recall, February 20 was the deadline for Interpipe's creditors to enter into lockup agreements in relation to the company's latest restructuring proposal. Interpipe will be able to simply sign restructuring documents if it secures 100% creditor approval, Debtwire said. If not, the company will need to use an English scheme of arrangement. "We estimate that the VRI increases the value of Interpipe's proposal by up to 7-8% of nominal. In detail, Reorg Research previously reported that the international creditors, with a total of $936mn in debt (including $199mn in Eurobonds), will be offered a six-year $310mn bond and a $45mn loan. Using the recently-hiked bond coupon rate of 10.25%, and discounting the bond flows at 15%, we arrive at an NPV of $295mn, or 31.5% of the nominal amount of international creditor debt, and this is without the VRI," Dmytro Khoroshun of Concorde Capital said in a note. "Now, assuming as a reasonable better case yearly EBITDA of $120mn (the 2017 value reported previously by Reorg Research), and discounting the VRI flows to the creditors at 25%, we come to an NPV of $365mn, or 39.0% of nominal. Considering that Interpipe's bond is currently quoted at 28.7/33.5, according to Bloomberg, Interpipe's offer with such VRI parameters appears to offer up to 7-8pp in upside."

9.0 Industry & Sectors

9.1 Sector news

9.1.1 Oil & gas sector news

While Russian gas transit through Ukraine fell by 7% last year, it spiked up 26% year-on-year in January, to 7.6bn cubic meters. Today, about one third of Russia's gas exports to Europe cross Ukraine. Russian officials say they will not need Ukraine's gas pipelines in the 2020s. But recent years show they needed Ukraine as a back up when the Nord Stream pipeline had problems. Russia's 10-year gas transit contract with Ukraine expires at the end of this year. Russian officials say they will renegotiate seriously only after they know who will be Ukraine's next president.

Ukraine cut its gas imports by one quarter in 2018, Naftogaz reports. Imports fell from 14.1bn cubic meters in 2017 to 10.6bcm. Domestic production – overwhelmingly in the hands of state-owned Naftogaz – increased last year by only 2.5%, to 21bcm. At the same time, Ukraine's GDP grew last year by an estimated 3.4%. In this context, the most likely causes for the import drop were increased energy efficiency and shifts to other energy sources.

In a step toward closer integration with the EU gas market, a test export of 5,000 cubic meters of Ukrainian gas has been made to Slovakia, reports the Kyiv Post. In the 1970s, Soviet Ukraine was the largest gas producing region of the Soviet Union. Although the country now imports about one third of its gas needs, new production sharing agreements are designed to jump start stagnant production, returning Ukraine to gas self sufficiency in the 2020s.

In a move toward becoming a gas trading hub in the 2020s, tariffs on entry into Ukraine's gas transportation system were halved on Jan. 1, to $6.28 per thousand cubic meters per day. Western Ukraine has the largest underground gas storage caverns in Eastern Europe.

Washington sees Poland as a future hub for re-export of American liquefied natural gas to Ukraine and Eastern Europe, Georgette Mosbacher, US Ambassador to Poland, told a conference in Warsaw on LNG and the countries of the EU's Eastern Partnership. She said next year the US will export 120bn cubic meters a year, about 30% of world LNG. Poland is expanding its three-year-old LNG terminal at S´winoujs´cie, on the German-Polish border. In four years, Poland plans to stop importing gas from Russia. Referring to Poland's plan to "become a regional gas hub," Mosbacher said: "I support this fantastic initiative of Poland and Ukraine."

9.1.3 Transport sector news

- **Planes**

Wizz Air was the fastest growing airline in Ukraine last year, recording a 73% increase in flights, to 15,251, according to UkSATSE, Ukraine's air traffic control agency. For the other top five: UIA increased its flights by 8% to

61,691; Turkish up 9% to 29,972; Belavia up 10% to 16,003; and LOT Polish up 24% to 15,813. Ryanair launched flights last fall and was not counted in the year-on-year comparisons.

Kyiv Boryspil's 19.4% passenger growth rate last year was the highest of any European airport of its class, 10 to 25mn passengers. According to Airports Council International Europe, runners up were: Moscow Vnukovo -- +18.4%; Budapest -- +13.5%; Warsaw Chopin --+12.8%; and St Petersburg -- +12.1%. By comparison, the average growth rate for non-EU European airports last year was +8.3%. Boryspil handled 12.6mn passengers last year. With more growth expected, Boryspil reopens Terminal F in April.

To offer a Kyiv region alternative for air cargo, Bila Tservka airport is to win international status in May and is to receive international cargo flights in August, Minister Omelyan tells reporters. Noting the airport is 80 km south of Kyiv's Ring Road, near the E95 Kyiv-Odesa highway and near rail lines, Omelyan says the goal is to turn Bila Tserkva into an "international multimodal transport hub." Airport director Sergei Kandaurov predicts the airport will handle 15 cargo flights a month this fall. A maintenance hub for four Ukrainian airlines, the airport did repairs last year on 73 aircraft, largely Antonovs. Last year, an EU expert study recommended the government spend $63mn through 2022 to turn the airport into a hub for cargo and discount airlines.

To cope with booming air cargo, Boryspil starts work in May on a new cargo terminal designed to more than triple handling capacity to 100,000 tons, Pavel Ryabikin, general director, tells reporters. Ideally, the terminal, will be partially open in time for this year's Christmas rush. During the recent Christmas period, the airport was so overwhelmed with packages that it closed for air cargo for two weeks. Given air cargo growth rates, Minister Omelyan predicts this expansion will only be sufficient through 2022.

This summer, Vinnytsia starts a two-year, $78mn rebuild designed to make the central Ukraine airport capable of handling Boeing 767s. Resurfacing the runway and installing new lighting are part of the makeover, Mykola Bozhko, of the Infrastructure Ministry, tells reporters. Ukraine's 11th busiest airport, Vinnytsia handled 61,000 passengers last year, largely on UIA flights to Kyiv and Tel Aviv and charters to Egypt. SkyUp starts charter flights to Antalya, Turkey on May 1.

Southern Ukraine's Kherson airport has the best growth prospects for a regional airport in 2019. After passenger traffic grew last year by 69%, to 106,000, airport officials released their development plan to the centre for Transportation Strategies. The airport lists 20 'promising destinations' and targets Belavia and five discount airlines: Wizz Air, Ryanair, Ernest, Pegasus and Moldova's FlyOne. In addition to talks with Wizz Air and Ryanair, work is underway to create a Kherson-based low cost carrier. Omelyan says "four to five" passenger jets would be based at the airport, the gateway to a dozen increasingly popular Black Sea resorts.

This spring, works starts on Prydniprovye, the new regional airport designed to serve Dnipro, Zaporizhia and Kriviy Rih, Omelyan tells the American Chamber of Commerce. By 2022, the airport could handle 1.5-2mn passengers. This volume would place it among Ukraine's top five airports. Dnipro and Zaporizhia airports will stay open. But Omelyan cited Poland, which invested in two large airports 80 km apart. The rival airports cannibalized each

other's traffic and neither prospered.

Starting with the May 1 holidays, air travel further decentralizes when SkyUp, Ukraine's new discount airline, starts charter service to Antalya, Turkey from seven regional airports: Chernivtsi, Kherson, Kriviy Rih, Mykolayiv, Poltava, Vinnytsia and Zaporizhia. Last year, Turkey hosted 1.35mn Ukrainian tourists, up 13% over 2017.

Lviv plans to increase air passenger traffic by 38% this year, to 2.2mn people, airport director Tatiana Romanovskaya tells reporters in Kyiv. After boosting traffic by 48% last year, Romanovskaya says she now is negotiating new flights with Qatar Airways, UIA, an Asian airline and a European discount airline. By June, Ukraine's busiest regional airport will have flights to 33 cities, including three new ones: Wizz Air to Copenhagen on March 3; airBaltic to Riga on April 1 and SkyUp to Odesa on June 2. The airport is undergoing a $10mn upgrade this year.

This autumn, Kyiv region gains a cargo airport with the opening of international passport and customs controls at Bila Tserkva Airport, Infrastructure Minister Volodomyr Omelyan announced Monday. Belotserkovsky Cargo Aviation Complex, a new municipal enterprise, plans to handle cargo at the airport, one hour by truck from Kyiv's circle highway. The airport's new international status also will allow expansion of its existing jet maintenance and repair business. After Kyiv's Boryspil was unable suspended air cargo deliveries during the Christmas period, Omelyan decided to fast track the opening of Bila Tserkva and to push Boryspil to start construction this spring on a new air cargo terminal.

- **Trains**

In December, Leo Express, a private Czech rail carrier, plans to launch a Prague-Krakow-Przemysl-Lviv train, according to Rynek Kolejowy, a Polish news site. Trains would run four times a day on the seven hour route. Asked about the train, Infrastructure Minister Volodymyr Omelyan tells the UBN: "We are ready to accept it." Separately, Czech Airlines plans to restore on May 30 its direct flights between Prague and Odesa.

Container rail cargo increased by 13% last year, to 334,963 units. After Ukrzaliznytsya started container trains from Odesa last year, Yevgen Kravtsov, chairman of the state railroad, says: "The container transportation market in Ukraine has tremendous opportunities, and our primary task is to create new services for our clients and partners to realize these opportunities." Each container on a rail car means one less truck trip on the roads.

Russian Railways is asking Russia's government to temporarily lift a ban on the import of locomotives engines and generators from Ukraine, reports Belprauda, a Belarussian news site. The railroad asked Russia's Industry and Trade Ministry exemption from Moscow's Dec. 29 ban on the Ukrainian-made parts until Russian manufacturers learn how to make their own. Separately, Russian rail car manufacturers, barred from buying Ukrainian wheels, are turning to two Chinese companies to supply 400,000 wheels through 2022, reports Kyiv's centre for Transportation Strategies.

- **Ships**

Russia's interference with Ukrainian shipping in the Azov is costing Ukraine $350mn, Infrastructure Minister Omelyan says. Faced with delays costing $10-50,000 a day, shippers are shifting to Ukraine's Black Sea ports, shunning Berdyansk and Mariupol, Ukraine's big Azov ports. Last week, US envoy to Ukraine Kurt Volker told reporters the Trump Administration is considering imposing sanctions this spring against Russian ships servicing Russia's Azov ports. Last week, a EU fact finding mission visited Berdyansk and Mariupol. On Feb. 18, the European Commission is to discuss sanctioning Russia for blocking freedom of shipping in the Azov, a binational sea by treaty.

Russian interference with merchant shipping on the Azov cost Berdyansk port $4.6mn last year, Port Director Alexander Troshchenko told a visiting EU delegation. "In 2018, metal and clay [shipments' were completely lost - $840,000," he said. In response, he said the port activated a new grain handling unit and shipped 200,000 tons of grain.

France's largest container shipping company, CMA CGM Group, plans to invest €20mn to double the container handling capacity of Odesa's Brooklyn-Kiev Port. In a five-year project, capacity would grow to 500,000 standard 20-foot containers a year – the equivalent of 60% of all containers handled by Ukraine's Black Sea ports last year. The centre for Transportation Strategies quotes Jan Odin, a financial director for CMA CGM, saying: "Our company believes in the future of Ukraine. We are interested in increasing the freight traffic through the terminal in the port of Odesa and have the intention to invest in this."

Despite Russian pressure on shippers, Mariupol continues with its modernization plan, building a grain terminal capable of handling 2.5mn tons a year, Port Director Alexander Oleinik writes on Facebook. He says half of the foundation has been laid, four of the 10 silos are rising and a rail link is being built. "I have no doubt that the amount of grain transshipment in the Mariupol port will increase significantly," he writes of the port, which until last year handled 10% of Ukraine's steel exports. Last year, overall cargo was down by 10% as the number of ships dwindled in the second half.

Despite Russia's harassment of merchant ships in the Azov, Asket-Shipping increased its grain silo storage capacity in Berdyansk last year by 42%, to 100,000 tons, reports the centre for Transportation Strategies. Victoria Abreyeva, director of the Berdyansk branch, says of the export-oriented investments: "All our warehouses are equipped with truck weighing complexes and labouratory equipment." Asket has export warehouses in the ports of Kherson, Mariupol, and Mykolayiv.

- **Cars**

With EU aid, Hungary is preparing to build a 4-lane expressway to its Záhony crossing with Ukraine, at Chop, Zakarpattia. Mukachevo.net reports that three Hungarian companies are to build the project, an extension of the M4 east-west highway from Budapest. This could cut the Uzhogorod-Budapest drive to three hours. Hungary has expressways to all of its seven neighbors, but Ukraine. Separately, Poland is building a 4-lane expressway from Warsaw through Lublin to Hrebenne, a Polish border town facing Lviv's Rava Ruska crossing.

Through 2023, €4.5bn in low interest loans have been committed to

support 39 infrastructure projects to upgrade many of Ukraine's highways, ports, airports, and railroads to EU standards. Largely designed to speed freight and passengers on east-west lines between Ukraine and the EU and to move export goods to the Black Sea ports, the aid is coordinated by the European Commission and is composed of European Investment Bank and World Bank loans and some grants, Infrastructure Minister Volodymyr Omelyan tells reporters. The building package includes: 13 highways -- €2.15bn; nine ports -- €873mn; nine rail -- €851mn; six airports -- €470mn; and two river projects -- €112mn. Several projects will be open to public-private partnerships.

9.1.4 Construction & Real estate sector news

Construction last year grew by 4.4%, to nearly $5bn, the State Statistics Service reports. Residential construction was down slightly. But the largest segment, infrastructure was up 9%, to $2.6bn. Overall, the 2018 growth represented a cooling after 2017, when construction shot up by 26%. As usual, Kyiv region led the country, with $1bn, followed by Odessa region, with $550mn; then Dnipropetrovsk region – nearly $500mn; and Kharkiv region -- $455mn. The trend is down, with housing construction down 25% in December y/y.

After opening five stores on Kyiv's right bank last year, Rozetka.ua, Ukraine's largest online store, now finds it **cannot find warehouse space.** "Ukraine is growing fast enough - this is good - but the problem is that the infrastructure is not keeping up with such growth," Vladislav Chechetkin, co-owner of Rozetka, tells Interfax-Ukraine. "The vacancy of the warehouses is zero. Therefore, if you want a warehouse on the right bank, this means that you have to find (land), get approval, permission to build ... is a significant time lag." Two years ago, Rozetka bought a warehouse on Kyiv's left bank. Although that space is full, the retailer plans to open a sixth Kyiv store this year, on the left bank.

Six new shopping centres, containing a record 400,000 square meters of rentable space, are to open in Kyiv in 2019, according to the Ukraine Retail centre. This would be eight times the new leasable space of last year and a record for the capital, says Daryna Kulaga, a market analyst for Jones Lang LaSalle Ukraine. Although developers often do not reveal construction costs, the six could total around $350mn.

The overall vacancy rate at Kyiv shopping centres fell to 3.7% at the end of 2018, Jones Lang LaSalle reports. This is down from 5.6% at the start of 2018. Annual store rents rose to $1,140 per square meter, almost the level of 2013.

6-story business centre has opened at UNIT.City, effectively doubling the constructed area of this Kyiv IT hub to 30,000 square meters. Designed for 1,000 workers, the new business centre has two large corporate tenants: Metinvest Digital and DTEK Academy. Vasyl Khmelnytsky, the founder of UFuture investment group, said last week of UNIT.City: "We have already invested $50mn, and in the next year and a half we want to invest the same amount." Next month, his KAN Development starts construction of residences. At build out, this 46-hectare development, located between Dorohozhychi and Lukianivska stations on the Green Line, is to be 300,000 square meters – 10 times the size of today.

9.1.6 Agriculture sector news

Ukraine has said it harvested a record 70.1mn tonnes of grain in 2018, up from 61.3mn in 2017. Exports could rise to by 7.8mnt to 47.2mnt during the July 2018 to June 2019 marketing year, AGWeb.com reports. Total grain exports during the current marketing year from the Ukraine have risen by 3.8mnt to 27.5mnt from 23.8mnt during the same point last year. As of January 30, Ukraine has exported almost 12.2mnt of corn as of January 30, compared with 7.6mnt in the same period last season. Wheat exports declined by.7mnt to 11.5mnt as of January 30. Assisted by strong supplies of feed grains, corn and barley, and a strong US dollar the Ukrainian corn export program will be one of the strongest on record. The combination of large feed grain and corn supplies and a strong dollar should continue to displace US corn exports in to northern Africa and Middle East destinations.

With last year's 70mn ton bumper harvest overflowing silos, the government plans to spend $30mn this year to subsidize construction of 2mn tons of additional storage. In a first step, Grain Alliance, a large farming company in central Ukraine, intends to increase its elevator capacity by 40%, adding 100,000 tons, the company tells Interfax-Ukraine. Ukrzaliznytsia says it lost $18mn last year due to elevators not working on weekends.

Taking advantage of unseasonably warm weather, farmers in southern Ukraine have started spring sowing – one month earlier than last year, ProAgro reports. In Kherson, farmers are sowing spring barley. Separately, the Agrarian Policy Ministry reports that the supply of spring seeds, 684,000 tons, meets "100% of the demand." This year, farmers are expected to fill 27.7mn hectares, virtually the same area as last year.

Ukraine's corn harvest last year was up 50% y/y, to a record 35mn tons, reports the US Department of Agriculture's Foreign Agricultural Service. The Service reports that 5% of the corn may have been left to rot in the fields because silos were full. On Wednesday, the State Statistics Service reported that the nation's capacity for simultaneous storage of grain, beans and oil seeds grew last year by 7.3%, to 78.3mn tons. Of this amount, farms owned 58%.

Ukraine's sugar beet plantings are to drop 20% this season, to 220,000 hectares, S&P Global Platts reports from London, citing "a source close to the National Association of Sugar Producers." Sugar experts forecasts a similar drop in plantings in the EU and Russia. Platts notes that Germany's Suedzucker, the world's largest corporate sugar producer, said last month it is considering closing factories. In September, Tereos, France's largest sugar producer, said it was planning to cut plantings to cut sugar beet production by 5%.

Capital investments in farming hit $2bn during the first three quarters of last year, Elena Kovaleva, deputy minister of Agrarian Policy and Food, tells reporters. A major portion went into two declining areas of animal husbandry – cattle breeding and pig production. About $500mn was invested in dairy processing and baby food production. Kovaleva called this investment volume "amazing."

Ukrainian producers will likely cut the areas sown with sugar beets to

220,000-230,000 hectares in 2019 vs 280,000 hectares in 2018, according to estimates of the national association of sugar producers Ukrtsukor. The forecast of 220,000-230,000 hectares will be the lowest figure over the past five years. "This, accordingly, will affect sugar production and the number of sugar factories in operation," Interfax news agency quoted Ruslana Butylo, the deputy chairman of the board of Ukrtsukor, as saying on February 19. She added that the situation could still improve, since most of the farms and sugar factories have not yet decided whether they will work next season. Such uncertainty is due to the fluctuation of the foreign exchange market and producers' fears over the increase in production costs, both of sugar beets and sugar. Sugar prices also fell in 2018 causing other producers to cut back on production. Sugar prices have become a volatile commodity and the price offer in Ukraine and Russia is directly linked to international prices making pricing volatile. As of early February, sugar production in Ukraine in the 2018-2019 marketing year (September-August) decreased by 15% year-on-year, to 1.82mn tonnes.

Ukraine's 42 sugar mills produced 15% less sugar during the fall 2018 sugar making season than during the 2017 season, reports Ukrtsukor, the industry association. Due to low world sugar prices, 10% less land was planted in sugar beets than in 2017. Last year, Ukraine produced 1.8mn tons of sugar and exported 584,000 tons, a 2.4% fall from 2017. Top buyers were: Uzbekistan, Azerbaijan and Libya. Top producing regions were: Vinnytsia – 424,000 tons; Ternopil – 227,000 tons; and Poltava – 222,500 tons. In January, Ukraine exhausted its export quota to the EU – 20,000 tons.

Ukraine increased sunflower production last year by almost 16%, strengthening its lead over Russia as the world's largest producer of sunflower oil. Production increased to 14.2mn tons, according to the Statistics Service. Other oil seeds also increased: soy – up 14% to 4.5mn tons; and canola up 25% to almost 3mn tons.

9.1.7 TMT sector news

E-commerce grew by 31% in Ukraine last year, the second fastest rate in Europe, following only Romania's 37%, according to the Better Regulation Delivery Office, or BRDO, a regulatory advisory body funded by the EU. While growing faster than the world average of 24%, Ukraine has plenty of room to grow, Alexander Kubrakov, BRDO IT director, tells reporters. In 2017, online accounted for 3.2% of retail sales in Ukraine, compared to 8.8% in the EU, 10.2% in the US, 17.8% in Britain. To further promote online sales, the BRDO recommends the government allows online stores to email sales receipts, instead of requiring they issue printed paper receipts.

Confirming commercial real estate reports that IT companies account for nearly half of new office rentals in Kyiv, 43 of the top 50 IT companies have offices in the capital. Lviv has 21 major IT companies and Kharkiv has 20. Fourteen companies have more than 1,000 specialists. Two – EPAM and SoftServe – have more than 6,000.

Ukraine's online advertising grew by 40% last year, to $125mn, reports the Ukrainian Internet Association. In-stream video totalled 42% of spending, banners for 37%, in-page video for 9%, 'non-standard solutions' for 7%, and sponsorships for 5%. Social media and instant messaging platforms accounted

for 34.5% of the ad spend, up from 26% in 2017.

The number of Ukrainians using Facebook increased by 30% in 2018, to 13mn, according to a survey by Agency PlusOne. Since May 2017, when Ukraine banned the use of Russia-based social media networks, the number of Ukrainians using Facebook, a US-based network, increased by 57%. About half of all Ukrainians aged 13 (the minimum age) to 45 use Facebook: 68% of the 18-24 year group; 62% of the 25-35 year group; 48% of the 36 to 45 year group. Users are skewed by gender: 59% female; 41% male. About two thirds access Facebook exclusively through their smartphones. Only 9%% only through their computers.

Ukrposhta handled 34mn international parcels last year, up 45% y/y, the centre for Transportation Technologies writes, analyzing the state postal company's statistics. With e-commerce driving the parcel business, the top sources of shipments were: China, the Netherlands, Israel, and the US. Last year, Ukrposhta started partnerships with Hongkong Post and Alibaba's delivery platform, Cainiao Smart Logistics Network Ltd. This year, Ukrposhta plans to increase parcel deliveries by 27%.

Ukrainians are among the world's fastest adopters of contactless, cashless payments systems, Inga Andreeva, general director of Mastercard Europe SA, tells reporters. Last year, Ukraine registered the fourth fastest growth rate in the world for taking to this technology, which typically involves waving a smartphone or digital wrist watch in front of a terminal to pay with Google Pay or Apple Pay. Common in the Kyiv metro system, contactless terminals start working this week in the busiest station of Kyiv's suburban 'elektrichka' trains.

With 38% of Ukrainians businesses accepting cashless payments, there is room to grow. The EU average is 60%, Mastercard says. Some businesses resist going to credit cards and contactless because it means paying taxes. But 64% of business managers surveyed by Mastercard say they prefer cashless for its simplicity and potential to boost sales. By last September, according to National Bank of Ukraine estimates, cashless payments accounted for 44% of transaction in Ukraine – a 13% increase since the start of the year.

Ukraine's tech sector earned the country an estimated $4.5bn from exports of tech services in 2018, according to the "Tech Ecosystem Guide to Ukraine" factbook, published on January 29. That's almost $1bn up on the previous year's figure, when IT brought in $3.6mn and made up 3.4% of Ukraine's gross domestic product, according to the factbook, which was compiled by innovation park Unit.City and the Western NIS Enterprise Fund. The Ukrainian tech community aims to grow these numbers to $8.5bn by 2025, according to the factbook. According to the publication, most of this money, 70%, came from sales of software development services abroad — traditionally called outsourcing. The popularity of outsourcing to Ukraine can be seen in global rankings, with the 2018 Global Outsourcing-100 ranking included 18 Ukrainian firms, and foreign firms with offices here. Ukraine is 24th in the ranking of the best countries for software development. There are a total of 4,000 tech firms in Ukraine and 110 research and development centres of large tech companies such as Microsoft, Wargaming, ABBYY, Samsung, Huawei, Siemens, according to the factbook. About 45% of them are American; and the study ranks US giants Amazon and Snap as the most influential foreign tech companies here. Other figures also make Ukraine's IT

sector stand out: The country is home to 185,000 tech specialists, with 16,000 graduating each year. And apart from software development, Ukrainian techies have started up their own companies. The most successful of these are Depositphotos, which has 400 employees; Gitlab, which is worth $1bn; Looksery, which was acquired for $150mn; and Grammarly, which boasts 7mn daily users. Other big names on the list include Readle, Jooble, Petcube, MacPaw and Viewdle.

Ukraine's IT exports should double by 2025, to $8.5bn, according to a forecast prepared by App Annie, a multinational data research company. Last year, exports grew by 25% y/y, to $4.5bn, estimates the report, commissioned by Kyiv's UNIT.City innovation park and Western NIS Enterprise Fund. Barely visible a decade ago, IT now is Ukraine's fourth largest export – after agriculture, labour remittances, and metals. About 70% of the exports are computer outsourcing jobs performed in Ukraine for foreign companies.

Ukrposhta, the state company, plans to increase deliveries by 27%, to 28mn packages this year, Director Ihor Smilianskyi tells reporters. He says: "Today Ukrposhta delivers more parcels in a day than in all of 2016." Last year, Ukrposhta entered into an alliance with Rozetka, Ukraine's largest online store. After launching a mobile app, Ukrposhta delivered 6mn packages ordered online last year. To further democratize e-commerce, Ukrposhta plans to complete the computerization this spring of all post offices in towns with populations over 2,000. With the biggest commercial reach in the nation, Ukrposhta has 11,000 post offices.

9.1.8 Tourism sector news

Tourist visitors to Kyiv increased by 20% last year, to 4.9mn, Andrei Strannikov, head of the city tourism commission, tells the City Council, basing his numbers on tourism tax receipts. Of the recorded tourists, 1.9mn were foreigners and 3mn were Ukrainians. This spring and summer, foreign tourism is expected to further increase with the expansion of discount airlines flying from the EU to Kyiv.

9.1.9 Renewables sector news

The Rada is expected to vote in March on a bill that would replace high renewable energy feed in tariffs with energy auctions. Matteo Pattrone, the new EBRD representative in Ukraine, warns excessively high feed in tariffs have provoked some governments to retroactively change the rates, hurting EBRD financed projects. A supporter of auctions, he tells the Kyiv Post: "It's better to have sustainable compensation regime than one that is too good to be true." To jump start foreign investment, Ukraine adopted in 2015 some of Europe's highest feed in tariffs for renewable energy.

9.1.10 Utilities sector news

The EU backs construction of the two 1,000 MW reactors. To connect with the EU grid, power lines could be built either 250 km west to Poland, or 250 km southwest to Ukraine's Burshtyn 'energy island' In 1990, in the wake of the 1986 Chernobyl disaster, construction stopped on the two reactors, leaving one 75% complete and the other 28% complete. Two years ago, Korea Hydro

& Nuclear Power signed an agreement to work on the project. More recently, Energoatom prepared a feasibility study with China National Nuclear Corporation, a state-owned company familiar with Soviet-era nuclear power designs.

9.1.11 Metallurgy & mining sector news

Investments per ton of liquid steel have doubled since 2014, to $29.10 per ton today, Alexander Kalenkov, head of Ukrmetallurgprom, the metals trade association, tells the Ministry of Industry. The investments largely go for cutting costs and cutting environmental emissions. In one big investment, Metinvest is investing $1bn in Zaporizhstal, the nation's fourth largest steelmaker, largely to builder new converter blast furnaces.

9.2 Major corporate news

9.2.2 Automotive corporate news

Zaporizhia Automobile Plant, or ZAZ, has started assembling a test batch of South Korea's LS Mtron tractors. LS, South Korea's largest tractor maker, has factories in Brazil and China. "The creation of a joint venture with the manufacturer is not being discussed yet," Dmytro Skliarenko, spokesman for UkrAVTO, the ZAZ parent company, cautioned Interfax-Ukraine. ZAZ has signed a distribution agreement with LS and has presented LS tractors at agro fairs here. Priced between $38,000-70,000, the LS models under study would go head to head with MTZ Belarus tractors, imports popular among Ukraine's small and medium farmers.

9.2.3 Transport corporate news

UIA, Ukraine's flag carrier, carried more passengers – +15% -- and more freight – +12% -- but lost money last year, Yuri Miroshnikov, company president, tells Liga.Biznes. Without specifying the size of the loss, he blamed Ukraine's aviation fuel taxes and Russia's ban on Ukrainian airlines flying over its air space.

Ukrzalyznitsia plans to spend nearly $1bn on capital expenditures this year – one third more than last year. Spending is to go for 3,650 new freight cars, the repair of 7,000 freight cars and the purchase of 15 locomotives from GE. Rail chair Kravtsov says an EBRD loan guarantees renovation of almost 6,000 freight cars through the end of next year.

Ukraine's battered state-owned railway monopoly Ukrzaliznytsia sees the potential to increase its debt by $1bn and intends to offer a Eurobond, according to the company's CEO Yevhen Kravtsov. With the company's gross debt of UAH34.2bn as of August 2018, its net debt-to-Ebitda ratio was at 1.5x, Kravtsov said in a statement on February 15. The company has a leverage covenant of 3.0x, based on its agreements with the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB). "That means that with Ebitda at the current level, we are capable of increasing our debt level by UAH25bn to UAH30bn," he added. Kravtsov also confirmed that the company is now considering a Eurobond issue, on which he can further comment as soon as the government publishes a respective resolution (on its parameters).

With the state railroad due to pay $150mn on a Eurobond in March, the Cabinet of Ministers has re-authorized Ukrzaliznytsia to issue up to $500mn in Eurobonds at interest rates up to 11% a year, slightly higher than the level authorized last September. Last December, a Eurobond launch planned was postponed in an adverse environment marked by delay in reaching the IMF accord and nervousness around the one month imposition of martial law. Today, the lead managers are JP Morgan and Dragon Capital. Separately, Evhen Kravtsov, chairman of the railroad, said Friday that Ukrzaliznytsia cut its hrvynia debt last year by 10%, to the dollar equivalent of $1.1bn.

Kyiv's Antonov plans to resume production this year of three jets:

AN-178, a 70-seat regional passenger plane; AN-158, the 100-seat version; and AN-178, a medium range military transport. Production can restart due to near completion of a program to replace Russian parts with parts from Canada, China and the US. The state company's financial plan foresees a tripling of income from aircraft sales.

Hungary's low cost airline Wizz Air carried over 1.5mn passengers on its routes to and from Ukraine, which represents more than 107% growth compared to the similar period last year and makes the carrier the largest low-cost carrier in the country, the company said in a statement on February 19. The same day the carrier announced two new routes from Kyiv - to Athens and Thessaloniki in Greece. The low-fare connection Kyiv-Athens is commencing on May 21 with 2 weekly frequencies, on Tuesdays and Saturdays, while flights on a route Kyiv-Thessaloniki are commencing on May 20 and will be operated 2 times per week, on Mondays and Fridays.

9.2.4 Construction & Real estate corporate news

After a decade long drought in high rise construction starts in Kyiv, a Ukrainian group wants to build a 100-meter tall hotel and office complex at 107-109 Velyka Vasilkivska, facing the Palace of Ukraine metro station and concert hall. Located midway between St. Nicholas Roman Catholic Cathedral and Ocean Plaza shopping mall, the builders, Ukrzhitlobud, would need a city variance for rising higher than the 27-meter limit on buildings in the historic district. Nashi Groshi news site notes that building permits have been given for 'hotels' that end up being apartment buildings. Of the 11 buildings in Kyiv higher than 110 meters, eight are residential. All were built in the 2000s. The last one, No. 1 Obolon Embankment, was completed in 2013.

Dragon Capital has bought a cold storage warehouse complex on western Kyiv's Ring Road, raising the investment company's warehouse holdings to 300,000 square meters. With the purchase of the Arktika warehouse, "logistics space will constitute 48% of our total commercial property portfolio," says Volodymyr Tymochko, Dragon's managing director for private equity. "Ongoing growth in demand for warehouses, fuelled by the expansion of offline and online retailers, is making this particular real estate segment attractive for investment." Last week at Dragon's annual investor conference, Tomas Fiala, Dragon's CEO, said: "In logistics and retail -- not only in Kyiv, but across the country -- vacancies are close to zero, which we last saw in 2007–2008."

9.2.6 Agriculture corporate news

South Korea's Posco Daewoo is buying 75% of a 2.5mn ton a year grain export terminal under construction in Mykolayiv. South Korea, a nation of 52mn people, imports almost all its wheat and corn – about 15mn tons. This year, Ukraine is to export 47mn tons of grain. Last year, Choi Jeong-woo took over as Posco chairman and the steel giant on a path to become a global grain trader. Posco became a corporate member of President Poroshenko's National Investment Council and sent executives to Ukraine on fact finding visits here. In a deal where investment values were not made public, Ukraine's Orexim Group retains minority ownership of the terminal.

- **Kernel**

Ukrainian sunflower oil producer Kernel has acquired a 100% stake in RTK-Ukraine, a company that owns and operates a fleet of 2,949 grain railcars, Kernel said in a statement on February 18. The deal's enterprise value is $64mn, including $49mn cash consideration already paid. Kernel estimates the acquisition will contribute up to $20mn to its annual Ebitda. Andriy Perederey at Kyiv-based brokerage Concorde Capital agrees that with the estimate of the deal's $20mn annual effect on Ebitda, which implies an EV/Ebitda of about 3.2x. "As Kernel's forward-looking Ebitda multiple is more than 5x, the deal looks value-creative for the company. The new railcar fleet will improve the company's infrastructure and trading division and will augment its vertical integration. All in all, this deal looks positive for Kernel's equity story," he wrote in a note on February 19.

Ebitda of Ukraine's sunflower oil producer Kernel jumped by 67.9% year-on-year (a 28.5% quarter-on-quarter improvement)to $129.3mn in 2QFY19, the company reported on February 28. The company's 2QFY19 revenue was $1,115mn, more than double y/y and 2.2% less q/q. Its 2QFY19 Ebitda in its bulk oil segment improved 2.0-fold y/y (or 2.5-fold q/q) to $35.1mn in 2QFY19.The company's grain trading Ebitda decreased 14.5% y/y (or a 70.7% q/q plunge) to $7.1mn and its export terminals division's Ebitda slid 2.9% y/y (or 19.3% higher q/q) to $9.9mn in 2QFY19. Kernel's silo services division contributed $23.4mn to total Ebitda, which is a 21.5% y/y decrease (or 4.0-fold q/q surge). The company's farming division Ebitda advanced 3.4-fold y/y (and 17.0% q/q) to $61.8mn. In 1HFY19, the company's revenue more than doubled y/y to $2,255mn, while its total Ebitda jumped 1.9-fold y/y to $229.9mn. Andriy Perederey at Kyiv-based brokerage Concorde Capital wrote in a note on February 28 that the company's 1HFY19 Ebitda was higher than our estimates due to stronger sunflower oil segment Ebitda and better results in silo storage and farming. Also, the company's sunflower oil Ebitda margin was higher than our expectations.

Ukrainian farmer and leading sunflower oil producer Kernel reported on Feb. 18 the acquisition of a 100% stake in RTK-Ukraine, a company that owns and operates a fleet of 2,949 grain railcars. The deal's enterprise value is $64mn, including $49mn cash consideration already paid. Kernel estimates the acquisition will contribute up to $20mn to its annual EBITDA.

The European Bank for Reconstruction and Development (EBRD) and the Clean Technology Fund (CTF) will provide a $56mn package for the construction of four biomass plants in Ukraine by the nation's sunflower oil producer Kernel. The credit package is designed to support renewable energy and technology aimed at reducing carbon intensity. "This will be the second project supported under the Ukraine Agribusiness Waste Residues Window, funded by the CTF," the EBRD said in a statement e-mailed to bne IntelliNews on February 25. Specifically, the funding will support the construction and operation of biomass plants at Kernel's production facilities in the Kharkiv, Mykolaiv, Odessa and Poltava regions of Ukraine. The plants will jointly generate 338,500 MWh of electricity annually from around 228,000 tonnes of sunflower husks. As part of the investment project Kernel Group is planning to expand specialised agribusiness educational programmes for young people from rural agricultural areas.

- **Astarta Holding**

Betting that world sugar prices will rise, Florida-based Kopernik Global Investors LLC has bought 12,947 shares of Warsaw-listed Astarta Holding, raising its stake over 5%. Between February 2017 and August 2018, the price dropped in half. Since then, sugar prices recovered slightly, to 13 US cents a pound. Dragon Capital writes: "Kopernik's latest share accumulation may reflect bottom-fishing demand in anticipation of a bounce in the sugar market. Astarta's shares slid by 59% in $terms in 2018, hitting the lowest level since 2015 on a drop in global and domestic sugar prices."

Wine producer Bayadera Group plans to invest $3mn in wine production this year, matching last year's level. Bayadera plans to plant vineyards on 200 hectares in Mykolayiv and to invest in moving from corks to screw caps, Anatoliy Korchynsky, Bayadera director general, tells Interfax-Ukraine.

US-registered Kopernik Global Investors has acquired 12,950 shares in the share capital of the Netherlands-based Astarta Holding NV, the parental company of Ukraine's agricultural giant Astarta. On the completion of the deal, the Kopernik's direct share in the capital of Astarta Holding and in the total number of votes at the company's general meeting has increased from 5% to 5.04%. According to Astarta, the farmer received the notification from Kopernik on February 18. Astarta's share quotation as of February 19 was PLN25 per share, according to the Warsaw Stock Exchange (WSE). In 2017, Fairfax Financial Holdings, a Canadian asset manager, completed the acquisition of the second largest stake in Astarta, controlling 28% of the shares at the time. Astarta cut sugar production, the farmer's core segment, by 24% y/y to 352,000 tonnes in 2018, boosting grain and oilseeds harvesting by 35% y/y, to 1.65mn tonnes, according to the company's reports published earlier via the WSE.

- **MHP**

MHP, Ukraine's largest agricultural producer, is obtaining a €120mn loan from ING Bank NV. According to Interfax-Ukraine, the loan is guaranteed by Zernoproduct MHP, the company's grain unit with assets valued at €192mn. Based in Myronivka, 100 km south of Kyiv, Myronivsky Hliboprodukt is the nation's largest chicken producer.

Ukraine's largest poultry producer MHP has finalised its acquisition of a 90%-plus stake in Perutnina Ptuj, a poultry meat producer and processor in Southeast Europe headquartered in Slovenia. MHP said in a statement on February 21 that "final consideration amount is subject to completion of the audited results of Perutnina Ptuj due diligence" for 2018. "The company didn't specify any details about the deal's value and effect on its operations and financials. But we expect that MHP will bring to light the deal's details after finalizing the due diligence of its audited results," Andriy Perederey at Kyiv-based brokerage Concorde Capital wrote in a research note on February 22. He added that the European Bank for Reconstruction and Development (EBRD) said recently when announcing that it is considering to provide €100mn financing for MHP that €100mn is the "total project cost" (the project includes the acquisition of Perutnina and "subsequent capital investments in it"). The information from the EBRD is in line with our previous assessment that the deal's value range is $100mn-$120mn, Perederey believes.

Leading Ukrainian agro-concern MHP finalizes acquisition of 90% stake in EU-based poultry producer. Ukraine's leading poultry producer MHP has finalized its acquisition of a 90%-plus stake in Perutnina Ptuj, a poultry meat producer and processor in Southeast Europe headquartered in Slovenia, according to the company's Feb. 21 announcement. The company stressed that the "final consideration amount is subject to completion of the audited results of Perutnina Ptuj due diligence" for 2018. This was widely expected as MHP is finalizing an acquisition process that started in September 2018. The company didn't specify any details about the deal's value and effect on its operations and financials. But we expect that MHP will bring to light the deal's details after finalizing the due diligence of its audited results.

- **Other**

Ukraine's largest agricultural company Ukrlandfarming and its subsidiary Avangardco have inked a restructuring agreement for a UAH4.4bn ($162mn) debt owed to state-owned lender Oschadbank. At the same time, sides did not reveal parameters of the debt restructuring. The deal was reached under a special law on financial restructuring and was preceded by more than a year of negotiations, Ukrlandfarming reported. "Reaching a deal with largest state bank is a signal for international investors," Ukrlandfarming owner, oligarch Oleg Bakhmatyuk commented in the company's statement published on February 7. In a separate statement, Oschadbank said the same day that independent expert (Ernst & Young) concluded that restructuring is an economically viable solution. The firm considered two scenarios, restructuring and forceful collection of debt.

Ukrainian prosecutors have closed their criminal case for alleged fraud involving Mykola Huta, the former CEO of farming company Mriya Agroholding, the slovoidilo.ua new site reported on February 12, citing a letter from National Anti-Corruption Bureau of Ukraine (NABU). According to the letter, a criminal case was opened in 2014 naming Huta as a suspect in massive fraud.

The investigators suspected embezzlement of over $1.3bn by the farming holding led by Huta, which brought losses to its creditors. NABU was responsible for leading the investigation of that case since November 2018. However, on December 29, this criminal case was closed by a prosecutor citing no evidence of a criminal offense. NABU also reported that as of February 8, it has received no additional materials on the Mriya case from prosecutors.

Recall, Mykola Huta left Ukraine in 2014 after Mriya declared insolvency and a criminal case was opened against its owners. In November 2018, Huta was extradited to Ukraine from Switzerland, where the court released him on personal recognizance.

"Law enforcement bodies no longer suspect Huta in fraud, which we expected would be the most likely outcome after he returned to Ukraine. Recall, an Interior Minister spokesman mentioned already in November the low chances Huta would be prosecuted," Alexander Paraschiy of Concorde Capital said in a note. "While Ukrainian law enforcement may continue its

embezzlement investigation of Mriya Agroholding, we don't expect its outcome will bring anything to Mriya's former creditors. Such a precedent shows that the Ukrainian courts are reluctant to convict anybody for financial fraud, which definitely plays against Ukraine's investment climate.

9.2.7 TMT corporate news

Dragon Capital and AVentures Capital have acquired minority stakes in Ciklum, the London-based IT outsourcing company with about 3,000 employees in Kyiv. Andriy Nosok, Dragon's Managing Director and Co-Head of Private Equity, said: "We believe that ongoing global digital transformation will support increasing demand for IT solutions and services, and that Ciklum is very well positioned to capitalize on this sustainable trend." Michael Boustridge, Ciklum CEO, said: "This investment will continue to propel Ciklum's rapid growth in delivering cutting edge technologies to clients around the globe." All three companies are privately owned and the investment amounts were not made public.

Net profit of Ukrainian leading telecoms company Ukrtelecom shrank by 45.1% year-on-year to UAH474mn ($17.6mn) in 2018, the company's CEO Yuriy Kurmaz told journalists on February 27. The company's net income for the year decreased by 2.3% y/y to UAH6.449bn, while its Ebitda declined by 12% y/y to UAH1.618mn last year. The Ebitda margin was down by 2.7 percentage points (pp), to 25.1%. At the same time, the company's capital investments decreased by 36.2% y/y to UAH604mn, according to Interfax news agency. Earlier, Ukrtelecom attributed its shrinking net profit to the growth of resource taxes, negative fluctuations in the exchange rate and an increase in depreciation payments due to the commissioning of new equipment in the process of upgrading and developing the network, according to Interfax news agency.

Thieves steal copper telephone wires from Ukrtelecom at the rate of eight kilometers a day. The company, the largest fixed line operator in Ukraine, reported that almost 3,000 kilometers of cable were stolen last year. Thieves were responding to world copper prices which were $3 a pound for much of last year, 50% above the $2 lows of October 2016. Many thieves were repeat offenders and 30% of replaced wires were stolen, the telephone company says. Last August, Ukrtelecom launched a pilot program to move affected land line subscribers to cell service.

Nova Poshta increased package deliveries last year by 20%, hitting 174mn. Points of sale grew by almost quarter, to nearly 3,000 across Ukraine. Deliveries from the United States double and deliveries from Europe tripled, bring international shipments to 2.7mn, or 1.5% of the total. About 21% of Nova Poshta's deliveries come from internet shopping. Nova Poshta has signed a deal to provide warehouse and delivery service in Ukraine for IKEA. This summer, the Swedish furniture retailer plans to open its first store in a showroom 'city format.'

Ukraine's state-owned post operator Ukrposhta increased international shipment processing by 45% year-on-year to 34.4mn parcels and letter, which, among other factors, led to a 37% y/y jump in the company's revenues from international operations. The growth in imports was influenced by work with two new partners - the logistics platform of the Alibaba group of

companies Cainiao, as well as the Hong Kong national mail. Ukrposhta also joined China's initiative One Belt, One Road via the China Post pilot project for the transportation of mail by rail from China to Poland with further transhipment of mail to vehicles to transport by road within the European Union (EU). Last year, the also operator launched "accelerated delivery channels" for Chinese JD.com, Joom and British ASOS marketplaces. The company also significantly expanded the list of partner airlines that deliver shipments. Earlier, Ukrposhta unveiled its plans to invest $507mn in the modernisation of its infrastructure and improvement of its business processes by 2021. Specifically, $128mn is due to be channelled into purchasing of new vehicles, $70mn is earmarked for the reconstruction of 2,000 offices around the country, and $107mn will be spent on creating new hubs for sorting correspondence. A further $111mn will go towards the purchase of computers and IT equipment for Ukrposhta's offices.

9.2.9 Renewables corporate news

Ukraine has 64 operating small scale hydro plants and 100 more that can be restored, AICE says. Dedicated to reviving and modernizing existing plants, AICE aims at “combining Norwegian and Ukrainian competence within hydro energy.” Norway is the largest user of hydropower in Europe, getting 98% of its electricity from hydro dams.

Ukraine’s first solar panel production plant starts work in the middle of February in Vinnytsia. Using Chinese technology, the Kness factory starts production at an annual panel capacity of 200 MW. By the end of this year, capacity is be 400 MW, says plant director Oleh Dovboschuk. Located on a once abandoned industrial site, the €5mn plant now employs 120 workers. Currently, Vinnytsia region has 250 MW of solar power and plans to add 60 MW more by the end of this year. Through 2025, Ukraine grants a 5% premium on feed in tariffs for solar projects using 30-49% domestically made equipment. For equipment with 50% or more local content, the bonus is 10%.

Norway’s NBT plans to start building this year a $1.1bn, 742 MW wind power plant on Zaporizhia’s Azov coast, according to an agreement signed Monday in Oslo with Ukraine partners Andriy Zhovner and Yuriy Kizilov. If financing comes as planned, the project should be fully operational in 2022. Located in the Yakymivka district, the plant is to be 100 km east of a separate NBT wind power project: a $460mn, 250 MW plant on the north shore of Kherson’s Lake Sivash. That project is to be completed next year.

Norwegian wind and solar projects in Ukraine add up to $1.5bn in coming years, Prime Minister Groysman said Monday at the Norwegian-Ukrainian Business Forum in Oslo. By contrast, bilateral trade last year was $255mn, an 8% increase over 2017.

With $2bn in American, European and Chinese windpower investment planned for Ukraine’s Azov Sea coast, Troshchenko pitched visiting EU and European Investment Bank officials for financing for a German-made Liebherr LHM 550 mobile harbor crane to unload and store wind turbine blades. Logistics operator Holleman Ukraine is considering building a warehouse at Berdyansk for windpower equipment. Denmark’s Vestas Wind Systems A/S, General Electric Wind Energy and China Machinery Engineering Corporation are already using Berdyansk, the closest port to the three largest wind

projects. In the last year, 12 ships with oversized wind turbine cargo docked at Berdyansk.

DTEK Renewables is starting work on a €200, 240MW solar polar plant near Nikopol, only a few kilometers from a site where the company inaugurated a 200 MW solar station last month. Construction this summer is to create 1,000 jobs. The new solar station is part of a plan by Rinat Akhmetov's DTEK to invest €1bn in renewables in Ukraine by the end of this year. Already Ukraine's largest wind power producer, DTEK is building an additional 300 MW of wind power generating capacity at two sites on the coast of the Sea of Azov. To get Ukraine's high feed in tariffs, renewable projects have to be commissioned by Dec. 31.

Philipp Leckebusch, DTEK Renewables new CEO, signed a contract with Siemens to build the new solar plant on the site of a former manganese mine, in Pokrov, Dnipropetrovsk. Leckebusch flew to China, to sign a contract with Risen Energy Co. for supply of 874,000 solar modules, or panels. Hailing the deal, Zhao Zelin, Risen's vice president for sales, said: "Risen Energy plans to continuously drive the transformation of the Ukrainian energy market." Leckebusch, a German, said the new plant, called Pokrovskaya, will produce enough power for 200,000 households.

DTEK Renewables has opened the second largest solar power station in Europe, the 200 MW Solar Farm-1, in the Nikopol district of the Dnipropetrovsk region. The contractor was China Machinery Engineering Corporation. The National Regulatory Commission has awarded the project the relevant green feed in tariff -- €15.03 per MWh until 2030. The solar plant should power 100,000 households, about three times the population of Nikopol city. The largest solar plant in Europe is Cestas Solar Park, a 300 MW station in the Gironde region of southwest France.

In neighboring Kirovohrad region, DTEK plans to build three solar plants for a total of 190 MW by the end of next year. According to regional officials, DTEK plans to start building this year the 60 MW Morozivka station in Oleksandriia district. About 40 km to the west, in Dykivka, DTEK plans to start building next year Solar Farm 8 – two stations with a total capacity of 130 MW. Ultimately owned by Rinat Akhmetov, DTEK Renewables is already Ukraine's largest producer of wind energy.

9.2.10 Utilities corporate news

Ukraine's largest energy company DTEK actively supports the speedy transition to an auction system while encouraging the development of renewable energy sources and compete under these new conditions, Maksym Tymchenko, the director general of the energy holding, told Interfax-Ukraine in Davos. "We are not only not scared [by the transition to the auction system], but we actively support it and promote the relevant law at the expert level. The transition to auctions is what should happen in Ukraine in the near future, and we are ready to compete, however, as in other businesses," he said on the sidelines of the Davos Ukrainian Breakfast, organized by the Victor Pinchuk Foundation. Tymchenko expressed hope that the parliament would soon adopt at second reading the relevant law so that Ukraine could comply with international trends not only at the level of power generation technologies, but also in the regulatory environment. The head of DTEK noted that the company

since its inception has supported the world energy trends and has long ago announced a strategic decision to actively increase its presence in alternative energy, starting back in 2010 the first project in this area - Botiyevska Wind Power Plant with a capacity of 200 MW. According to him, by the end of this year it is planned to form a portfolio of assets in renewable energy at the level of 1 GW, of which 500 MW is wind power and 500 MW is solar power.

DTEK Energy power generation falls 5% in 2018 Ukraine's leading coal and power holding DTEK Energy generated 37.94 TWh of electricity in 2018, Concorde Capital calculated based on sector-wide data provided by the Energy Ministry. This is a 4.8% decrease y/y on like-to-like basis, but 0.6% above the ministry's plan. Total power generation in Ukraine increased 2.7% y/y to 154.41 TWh, with DTEK Energy's share being 24.6%. Power generation at DTEK's thermal power plants declined 1.9% y/y to 35.65 TWh in 2018, as coal consumption fell 2.1% y/y to 17.97mmt. In particular, the holding reduced its consumption of anthracite coal (which is not mined in the disputed Donbas region and not available to Ukrainian companies, but has to be imported from Russia) by 31% y/y to 2.10mmt, and raised its consumption of hard steam coal (produced by DTEK Energy's mines) by 3.6% y/y to 15.88mmt. Power generation at DTEK's combined heat and power plants fell 35% y/y to 2.29 TWh, which is mostly the result of the discontinued operation of two large Kyiv-based plants by DTEK's Kyivenergo since August 2018. In December alone, DTEK Energy generated 4.16 TWh of electricity, which is 14% more y/y.

9.2.11 Metallurgy & mining corporate news

Metinvest steel output drops 4% q/q in the fourth quarter of 2018 Ukraine's largest steelmaker Metinvest (METINV) reported on January 31 a 4% q/q drop in steel production to 1.725mmt at its subsidiaries in the fourth quarter of 2018. Azovstal's output dropped 8% q/q to 0.912mmt in the fourth quarter of 2018 due to a scheduled overhaul of basic oxygen converter No. 1. Ilyich Steel's output was flat q/q in the fourth quarter of 2018 at 813 kt, according to the holding's operational update. Metinvest's 2018 crude steel output slid 1% y/y to 7.323mmt due to a 4% y/y drop to 4.082mmt at Azovstal, which was mostly offset by a 5% y/y rise at Ilyich Steel to 3.241mmt. The holding's pig iron output in the fourth quarter of 2018, 1.971mmt, inched up 1% q/q. Its 2018 pig iron production rose 3% y/y to 8.205mmt due to an 8% y/y jump tdzo 4.498mmt at Ilyich Steel, which was offset by a 2% y/y decrease to 3.707mmt at Azovstal. The the fourth quarter of 2018 output of semi-finished products at Metinvest, 723 kt, grew 9% q/q (merchant pig iron output jumped 43% q/q to 452 kt, while slab output plunged 22% q/q to 270 kt). During 2018, the holding increased its semi-finished product output 10% y/y to 3.026mmt, owing to a 17% y/y rise in merchant pig iron output to 1.644mmt and a 3% y/y increase in slab output to 1.382mmt. The holding's finished product output dropped 6% q/q in the fourth quarter of 2018 to 1.367mmt due to a 94% q/q plunge in railway product output to 2 kt, a 2% q/q drop in flat product output to 1.144mmt, a 7% q/q loss in long product output to 188 kt, and a 27% loss in tubular product output to 33 kt. During 2018, finished product output increased 3% y/y to 5.769mmt owing to a 14% y/y increase in long product output to 817 kt and 2% y/y growth in flat product output to 4.747mmt. Total coke production in the fourth quarter of 2018 rose 9% q/q to 1.358mmt, while merchant coke output gained 13% q/q to 487 kt. During 2018, Metinvest boosted its total coke production 11% y/y to 5.269mmt, whereas output of merchant coke jumped 42% y/y to 1.717mmt. Total iron ore concentrate production in the fourth

quarter of 2018, 6.813mmt, rose 4% q/q, whereas output of merchant iron ore products slid 2% q/q to 3.794mmt due to a 14% q/q decrease in merchant pellet production to 1.730mmt, which was largely offset by a 10% q/q increase in merchant iron ore concentrate production to 2.064mmt. For 2018, total iron ore concentrate output was flat y/y at 27.353mmt, while production of merchant iron ore products inched up 1% y/y to 15.218mmt due to a 30% y/y jump in merchant pellet output to 7.484mmt, which was offset in large part by a 17% y/y drop in merchant concentrate production to 7.734mmt.

To retain skilled workers tempted to move to the EU, the Metinvest group raised salaries by 40-45% to the monthly hryvnia equivalent of $1,000-1,200, Alexander Pimkin, the steelmaker's personnel director, tells the Ministry of Industry. He lists the social benefits packages tailored to workers, the company's investments in parks and festivals, and concludes: "All this is intended to keep employees in their cities, fill their lives with interesting meaning and receive decent remuneration for their work."

S&P raises Metinvest outlook to Positive. The outlook on the long-term credit rating of Ukraine's largest steelmaker Metinvest (METINV) was upgraded by S&P to Positive from Stable on Jan. 29. The agency also affirmed its rating at B- (same as Ukraine's sovereign), adding that the Positive outlook indicates the possibility of an upgrade to B within six to twelve months. S&P said that in 2019-2020, "Metinvest is likely to resume paying dividends, which will provide some clarity regarding its future financial policy." Metinvest's approach to dividend payments would be one of the factors on which the possible rating upgrade would depend upon, S&P said. The ratings agency briefly mentioned that "until recently, the company had a $460mn shareholder loan, which we viewed as a subordinated instrument." Metinvest's two other long-term credit ratings are from Moody's – a B3/Stable grade that was raised from Caa1 on Dec. 27, 2018 and which is one notch above Ukraine's sovereign – and from Fitch, which offered a B/Positive assessment, also one notch above Ukraine's sovereign that was raised from RD on Apr. 6, 2017.

The owner of Ukraine's metal pellet producer Ferrexpo is suspected of hiding his business interests. Kostyantyn Zhevago, the CEO and majority owner of Ukraine's largest iron ore pellet exporter Ferrexpo, might face criminal charges for not declaring some of his business interests in his 2015 and 2016 state asset and income declarations, the ukranews.com news site reported on February 11, citing an anonymous law enforcement source. The National Anti-Corruption Bureau of Ukraine (NABU) has submitted a request to prosecutors for parliament to strip Zhevago, an independent MP, of his parliamentary immunity to face the possible charges, the report said. "We think that the probability of Zhevago losing his parliamentary immunity is low in the current parliament. Indeed, it has already rejected requests to strip more controversial MPs of their immunity," Dmytro Khoroshun of Concorde Capital said in a note. "Nevertheless, it remains to be seen whether Zhevago keeps his Rada seat in the upcoming October parliamentary elections, and whether charges against him are pressed in case he ceases to be an MP," Khoroshun added.

Ukraine's largest iron ore pellet exporter Ferrexpo saw pellet output decline by 11.5% month-on-month to 830 tonnes (which amounts to 26.8 tonnes per day) in January. Dmytro Khoroshun at Kyiv-based brokerage Concorde Capital tentatively expects Ferrexpo's 2019 production volume to be in line with the company's guidance of 10.6mn tonnes (about 29.1 tonnes per

day), which is flat year-on-year.

Ukraine's largest producer of steel pipes and railcar wheels Interpipe, boosted its sales volume 12% y/y to 857kt in 2018, the company reported in a February 12 press release. Sales of pipe products increased 12% y/y to 668 kt in 2018 due to growth in American (37% y/y to 124 kt), European (24% y/y to 169 kt) and Ukrainian (22% y/y to 179 kt) markets, according to Interpipe. These gains more than offset the loss of the CIS sales volumes (19% y/y to 113 kt). Sales of railway products rose 10% y/y to 189 kt in 2018, driven by the markets of Europe (76% y/y to 41 kt) and Ukraine (39% y/y to 62 kt), the company noted. Again, these gains more than compensated for the loss of CIS sales volumes (17% y/y to 74 kt). Recall on January 19, 2018, the Eurasian Economic Union (EEU) – led by Russia and uniting five former Soviet countries (including Belarus, Kazakhstan, Armenia and Kyrgyzstan) – hiked anti-dumping duties for Interpipe railcar wheels to 34.22% from 4.75%. "Following the introduction of the EEU duties, Interpipe was successful in 2018 in both maintaining decent CIS railway product sales volumes and boosting sales in Europe and Ukraine. The company noted that, having become a leader in the European wheel market for freight railcars, it plans to enter the EU passenger car wheel market and to continue selling wheels in Ukraine. Nevertheless, we think that its CIS sales volumes will continue decreasing," Dmytro Khoroshun of Concorde Capital said in a note. "We also think that Interpipe's pipe production might drop about 7% in 2019 because of the expected lower oil prices."

Pipe production at Ukraine's largest steel pipe producer Interpipe increased by 11.4% month-on-month to 2.14 tonnes per day (or 66.2 tonnes per month) in January, according to calculations of Kyiv-based brokerage Concorde Capital published on February 20. Interpipe NTRP pipe production slid 3.3% m/m to 0.75 tonnes per day in January. Interpipe NMPP output jumped 74% m/m to 0.28 tonnes per day. Interpipe Niko Tube output rose 12.9% m/m to 1.10 tonnes per day. Concorde's Dmytro Khoroshun believes that the 2019 pipe production volume at Interpipe to drop 7% year-on-year to 700 tonnes, or 1.92 tonnes per day.

Ukraine's largest steel pipe producer Interpipe has postponed the deadline for its lenders to join the lockup agreement to February 20 from February 8, according to distressed debt information provider Reorg Research. Interpipe and a coordinating lenders committee signed the agreement on January 11. In comparison with the mid-2018 proposition to the creditors, on which *bne IntelliNews* reported in August, Interpipe hiked the coupon rate on the new $310mn six-year bond to 10.25% from 9.35%, the outlet reported last week. Another change is the option for certain bank creditors to convert their debt into either a new loan or the new bond, instead of only into the new bond previously. Interpipe's restructuring plan has sufficient support to be implemented by way of an English scheme of arrangement or through a consent solicitation, according to a source close to the situation, Reorg Research added. According to earlier reports, Interpipe planned to offer a substantial restructuring fee and Ebitda-linked value-recovery instruments to creditors other than Ukrainian banks. "These restructuring parameters, on which the fair value of the deal depends heavily, remain unknown," Dmytro Khoroshun at Kyiv-based brokerage Concorde Capital wrote in a note on February 15. "In comparison with our August estimate of the NPV to Interpipe's bondholders, which is 32-35% of par, the 90 bps coupon rate hike increases the value by about 1.3 pp." Interpipe's bond is currently quoted at 28.7/33.5,

according to Bloomberg. "Pragmatically, after more than five years of Interpipe's default, it does not seem like its creditors have been successful in pressing the company for substantial concessions, like a debt-for-equity swap," Khoroshun added. "Therefore, a haircut to Interpipe's debt seems unavoidable, and we think that Interpipe's latest proposal is reasonable, in part because the company's leverage would remain substantial after the restructuring (3.3x using the 2017 Ebitda)."

Coal mining at Ukraine's leading coal and power holding DTEK fell 1.9% year-on-year to 27.19mn tonnes in 2018, according to the company's trading update published on February 18. The decline was caused solely by loss of control of three mines on the rebel-occupied territories of Ukraine's Donbas as of March 2017. On a like-to-like basis, the group's coal mining increased 5.3% y/y, including 4.9% y/y growth in Russia (to 3.05mn tonnes). DTEK's Ukrainian mines, boosted coal production 5.3% y/y on like-to-like basis to 24.13mn tonnes.

Canada's Black Iron Inc has signed a memorandum of understanding with Glencore, the Anglo-Swiss mining giant, to finance and develop Shymanivske iron ore deposite in Dnipropetrovsk. One of the world's largest iron deposits, Shymanivske has an estimated 833mn tons of reserves, with ore grading at 32% iron. The nonbinding memorandum contemplates Glencore funding all or part of construction in return for iron. A first phase envisages $436mn investment to produce 4mn tons of iron a year. Black Iron's CEO Matt Simpson says: "I am pleased to welcome Glencore as an external investor for the construction of the Shimanivske project, as well as their agreement to work with us to provide additional funding."