Fixed Income Weekly Monitor

March 23, 2020

Trends

Ukraine's sovereign Eurobonds were hit with a massive sell-off for the second week in a row, pushing yields up to levels not seen since the political instability of the EuroMaidan uprising six years ago. The selling was triggered by fears of global economic recession as the country went into lockdown to prevent an outbreak of the so-called Covid-19 virus. Kyiv closed all restaurants and shut down its subway system on Tuesday (Mar 17) in moves that put speculative pressure on the hryvnia, forcing the National Bank to intervene in the currency markets.

The NBU joined other central banks with a flurry of emergency packages, introducing long-term refinancing loans for the country's banks. The new instrument will provide an additional assurance that the country's banking system has sufficient liquidity. Long-term refinancing loans will carry a floating interest rate. It will be determined as the sum of the NBU's key policy rate and a constant percentage that will be in effect on the day the loan is granted. Currently Ukrainian banks have around UAH 200bn in hryvnia liquidity and USD 8bn equivalent in foreign hard currency liquidity.

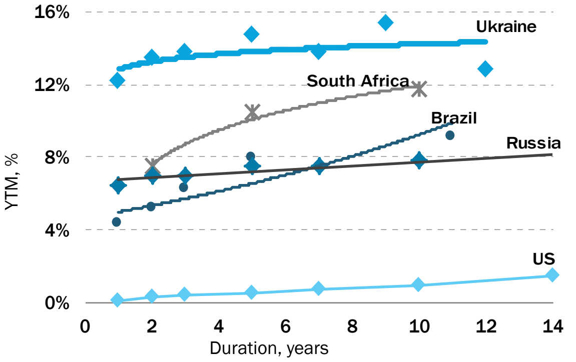
The longest Ukrainian Eurobond with maturity in 2032 plunged by another 18% to 68.5/71.5 (12.8%/12.2%), bringing its 2-week loss to 35%. Medium-term benchmark Ukraine-25s fell 22% to 74.6/77.6 (15.2%/14.2%), and the VRI derivatives (linked to Ukraine's future GDP growth with expiration in 2040) tanked by 28% to close at 50.0/55.0 cents on the dollar after having traded at par less than a month ago.

Prices for corporate bonds, both from stable borrowers and riskier companies, fell sharply. The EUR-denominated bonds of state-owned natural gas giant NaftoGaz with maturity in 2024 tumbled by 14% to 76.2/78.2 (14.9%/14.1%), and DTEK-24s issue plunged by 20% to 68.2/73.2 (22.4%/19.9%). Quasi-sovereign banking issue UkrEximBank-25s dropped by 9.6% to 85.4/87.4.

The bid-side yield on the government's 1-year UAH-denominated treasuries on the secondary market surged by 800 bps to 23.00% YTM as worries about hryvnia stability wrecked demand for domestic bonds. There is almost no liquidity in local bonds right now, as Ukrainian banks are unwilling to buy even at such an attractive yield as 20%, fearing that offshore investors which have built up a UAH 125bn bond portfolio in the last year could start to flood the market with papers. The Finance Ministry conducted its regular primary bond auction on Mar 17, offering only USD-denominated bonds, and managed a placement of short term USD-bonds for USD 72mn at 3.5%.

The hryvnia was under heavy attack last week from speculators as the dollar demonstrated broad gains against world currencies amid the turmoil on financial markets. The domestic currency briefly fell below the UAH/USD 29 level at midweek before massive interventions from the National Bank provided cover; the NBU acknowledged that its reserves have declined from USD 26.6bn at the beginning of March down to around USD 24bn as of Friday (Mar 20). The hryvnia ended the week 3.8% lower at 27.50 UAH/USD, a level last seen at the beginning of 2019.

SOVEREIGN BOND YIELD CURVES



Source: Bloomberg. Eavex Capital

FIXED INCOME

	Last	1W ch	YTD
NBU Key Rate	10.0%	0.0 p.p.	-3.5 p.p.
UAH 1-year bond	23.0%/13.0%	+4.0 p.p.	+4.5 p.p.
Ukraine-2024	15.7%	5.9 p.p.	9.1 p.p.
Ukraine-2028	15.3%	6.1 p.p.	8.3 p.p.

CURRENCY

	Last, UAH	1W chg.	YTD
USD/UAH	27.50	3.8%	16.1%
EUR/UAH	29.50	-0.5%	11.7%

Source: Eavex Capital

Highlights

- Kyiv in Emergency IMF Talks Amid Harsh COVID Restrictions

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Kyiv in Emergency IMF Talks Amid Harsh COVID Restrictions

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NEWS

National Bank governor Yakiv Smoliy revealed last Wednesday (Mar 18) that Ukraine is in discussions with the International Monetary Fund on an emergency lending facility to counteract the economic effects of the so-called "COVID-19" virus. Ukraine's government led by President Zelenskiy, and also its major cities, have entered a lockdown regime to stop the spread of the virus, although fewer than 100 cases have actually been confirmed in the country. Kyiv had already been in talks for the last 6 months to receive a new IMF Extended Fund Facility (EFF) loan in the total amount of USD 5.5bn, and is now also aiming to receive a "Rapid Financing Instrument" being made available to emerging-market nations by the IMF; the amount of such an emergency loan was not specified by the NBU, but we assume it could be several billion dollars. Like most of Europe, Ukraine has cancelled all commercial air traffic and closed its borders to entry by foreign citizens. Last Tuesday (Mar 17), when it was announced that Kyiv would close all restaurants and shut down its subway system by the end of the day, the hryvnia fell sharply against the dollar before being pushed back up by massive NBU interventions. The central bank acknowledged that its reserves have declined by some USD 2.6bn so far in March due to the need to maintain hryvnia stability. Ukrainian sovereign Eurobonds have seen their value plummet by some 30-35 percent over the past two weeks, with yields reaching distressed levels in the mid-teens, amid the larger global bond market crisis which sees the risk of numerous corporate defaults.

COMMENTARY

That Smoliy and the NBU are now out front for Ukraine on the IMF negotiations is not surprising, given that only two weeks ago, Zelenskiy removed key figures from the government, including the prior Finance Minister Oksana Markarova, and Smoliy will be viewed in international financial circles as Kyiv's "steady hand". In our view, Zelenskiy's position vis-a-vis the IMF has been strengthened by the COVID crisis, as we suppose that the IMF may drop its insistence on the implementation of a sweeping land reform bill that is stuck in Parliament and was due to take effect this autumn; the land reform, though much-needed, clearly has to take a back seat to the primary task of maintaining economic and political stability in an environment which could see both global and domestic GDP contracting by 10 percent or more in the coming months. The crisis will also give Zelenskiy and his powerful new administration chief Andriy Yermak more leeway in other political avenues where they might otherwise have faced stronger opposition, particularly in Yermak's conciliatory approach to Russia in the Donbass peace negotiations. We stress that unlike the United States and EU member states, Ukraine simply does not have the resources needed to weather a shutdown of its economy lasting several months. Given the relatively low fatality rate of the COVID virus (estimated by epidemiologists at between 0.1% and 1%), Kyiv might soon be faced with the choice of renewing economic activity and managing the fallout of the virus as best it can, or risking the country's economic and social collapse amid an indefinite lockdown.

SELECTED UKRAINIAN EUROBONDS

Issue	Price Bid	Price Ask	Price ch., W/W, %	YTM Bid, %	YTM Ask, %	Coupon	Maturity Date	Volume USD mn	Currency	Ratings[1]
Sovereign Eurobonds										
Ukraine, 2021	93.6	95.6	-6.8%	13.1%	11.4%	7.75%	1 Sept 2021	1,409	USD	Caa1/B/B
Ukraine, 2025	74.6	77.6	-21.7%	15.2%	14.2%	7.75%	1 Sept 2024	1,328	USD	Caa1/B/B
Ukraine, 2028	74.3	77.3	-23.0%	15.8%	14.9%	9.75%	1 Nov 2028	1,600	USD	Caa1/B/B
Ukraine, 2032	68.5	71.5	-17.8%	12.8%	12.2%	7.38%	25 Sept 2032	3,000	USD	Caa1//B
Ukraine, GDP-linked	50.0	55.0	-28.6%			0.00%	31 May 2040	3,214	USD	/B/
Corporate Eurobonds										
Kernel, 2022	83.8	88.8	-11.0%	20.4%	16.5%	8.75%	31 Jan 2022	500	USD	/B/BB-
MHP, 2026	71.8	76.8	-20.9%	14.5%	12.9%	6.95%	4 Apr 2026	550	USD	B3/B/B
MHP, 2029	75.0	80.0	-13.4%	10.7%	9.7%	6.25%	19 Sept 2029	350	USD	B3/B/B
DTEK, 2024	68.2	73.2	-20.0%	22.4%	19.9%	10.75%	12 Dec 2024	1,275	USD	//
Metinvest, 2026	71.5	76.5	-15.6%	16.6%	14.9%	8.50%	23 Apr 2026	648	USD	B3/B/BB-
Metinvest, 2029	72.0	77.0	-13.4%	12.3%	11.3%	7.75%	17 Oct 2029	500	USD	B3/B/BB-
NaftoGaz, 2024	76.2	78.2	-14.5%	14.9%	14.1%	7.125%	19 Jul 2024	600	EUR	//
Bank Eurobonds										
UkrEximBank, 2022	85.2	87.2	-9.6%	28.6%	25.6%	9.63%	27 Apr 2022	750	USD	Caa3//B
UkrEximBank, 2023	81.2	84.2	-10.9%	22.9%	19.9%	9.00%	9 Feb 2023	125	USD	Caa3//B
UkrEximBank, 2025	85.4	87.4	-9.6%	20.7%	19.0%	9.75%	22 Jan 2025	500	USD	Caa3//B
Oschadbank, 2023	87.0	89.0	-10.2%	19.7%	18.0%	9.38%	10 Mar 2023	700	USD	Caa3//B
Oschadbank, 2025	85.2	86.2	-12.6%	14.2%	13.9%	9.63%	20 Mar 2025	500	USD	Caa3//B

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

Source: TR Data, Eavex Research

UKRAINIAN DOMESTIC BONDS

Issue	Price (Bid)	Price (Ask)	YTM (Bid)	YTM (Ask)	Modified Duration	Coupon	Coupon Period	Maturity Date	Volume UAH mn
UAH denominated Bonds									
UA4000202469			23.0%	13.0%	n/a	n/a	S/A	30 Sept 2020	n/a
UA4000200174			23.0%	13.0%	n/a	n/a	S/A	20 Jan 2021	n/a
UA4000195176			23.0%	13.0%	n/a	n/a	S/A	11 Aug 2021	n/a
UA4000203236			23.0%	13.0%	n/a	n/a	S/A	05 Jan 2022	n/a
UA4000204002			23.0%	13.0%	n/a	n/a	S/A	11 May 2022	n/a
UAH denominated Bonds									
UA4000204853			4.50%	3.25%	n/a	n/a	S/A	29 Jul 2021	USD 350mn

Source: TR Data, Eavex Research

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