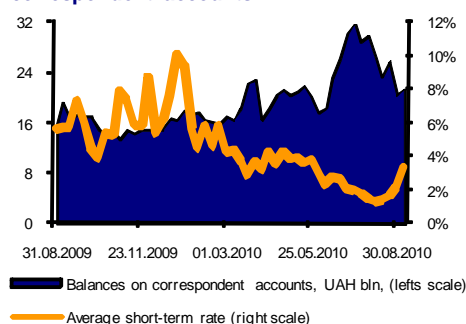


# UKRAINIAN FIXED INCOME WEEKLY

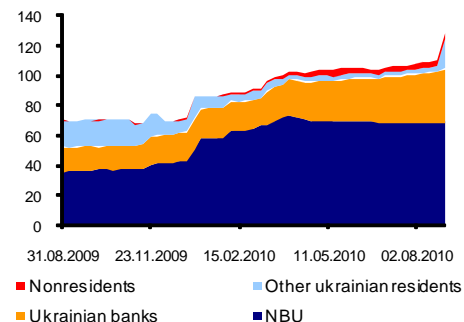
Artem Kost, [kost@ufc-capital.com](mailto:kost@ufc-capital.com)

September 8, 2010

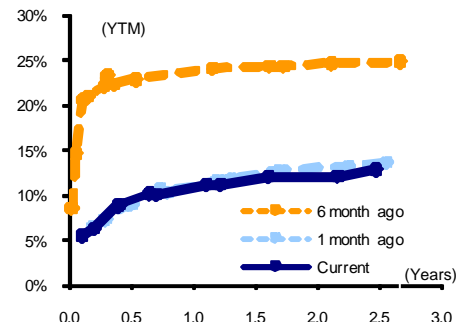
**Interbank rates and liquidity on banks correspondent accounts**



**OVDPs holders. UAH bln**



**Sovereign yield curve shift**



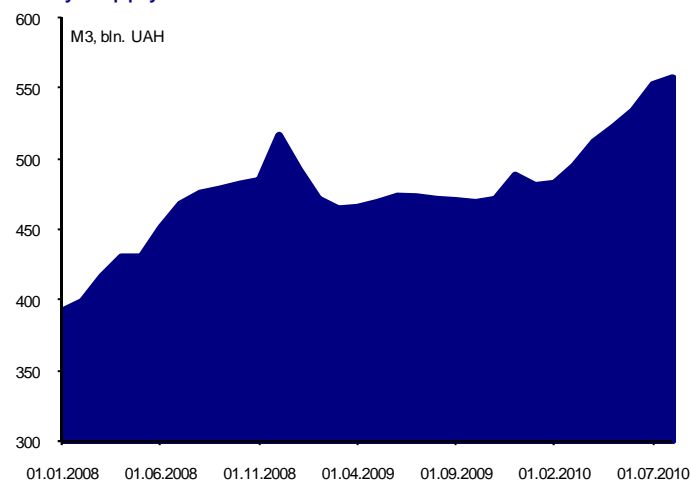
## Macroeconomic view

The macroeconomic situation in Ukraine has improved considerably since the beginning of 2010, illustrated by the significant surge in interbank liquidity, boosting of NBU currency reserves (growing by 23.3% since January 2010), weakened inflation (in April to July, deflation was observed), and a slight appreciation of national currency. **However, in our opinion, there are some signs that macroeconomic conditions will deteriorate beginning in September 2010, which should be reflected in the sovereign yield curve rising by 100-200 b.p. by the end of 2010.**

### Monetary statistics

The National Bank of Ukraine recently published monetary statistics for August 2010, which indicate some deceleration in positive monetary trends. The total volume of money in deposit accounts grew by just 1.5% to 380.6 bln hryvnia (after +3.3% in July). The main contributors to these dynamics in August were corporate clients, which increased their deposit holdings by 2.8%. Individuals added just 0.8%, confirming our previous forecast regarding the end of an aggressive deposit inflow since September. As a result, growth of the money mass (M3) decelerated +0.8% after recording +3.4% in July.

### Money supply in Ukraine



Major indicators			
	06.09	30.08	Change
Overnight	0.72%	0.73%	-0.01 p.p.
1-week	1.15%	0.92%	+0.24 p.p.
2-week	1.93%	1.88%	+0.04 p.p.
UAH/USD	7.90820	7.88700	0.27%
UAH/EUR	10.14938	10.02674	1.22%
UAH/RUR	0.25766	0.25693	0.28%

UFC fixed-income benchmarks			
	06.09	31.08	Change
Corporate bonds	14.8%	14.8%	0.0 p.p.
Municipal bonds	17.2%	17.2%	0.0 p.p.
UFC UAH depo	13.5%	13.6%	-0.1 p.p.
UFC USD depo	7.0%	7.0%	-0.0 p.p.

Bonds calendar: 09.09.2010-15.09.2010			
Coupon payment			
09.09.10	-	Swedbank, 1-D	
10.09.10	OAMSE	Amstor, 1-E	
10.09.10	OAMSF	Amstor, 1-F	
13.09.10	OALFF	Alfa-Bank, 1-F	
13.09.10	-	Alfa-Bank, 1-G	
15.09.10	63564	Ukraine, 12.09.2012	
15.09.10	64810	Ukraine, 14.03.2012	
15.09.10	64802	Ukraine, 14.09.2011	
Redemption/put option			
13.09.10	OALFF	Alfa-Bank, 1-F	
13.09.10	-	Alfa-Bank, 1-G	
15.09.10	60289	Ukraine, 15.09.2010	

## Public finances

The situation with public finances in 2010 remains quite difficult. The approved budget deficit amounted to 57.7 bln hryvnia or 5.3% of GDP, but was subsequently revised to 4.99% of GDP, which was envisaged in the agreement with IMF. Since the beginning of 2010, the Ukrainian Government managed to finance the effective budget deficit by making successful OVDP placements amounting to 40 bln hryvnia, while redeeming OVDPs in the amount of 15 bln hryvnia. At the moment, the outstanding OVDP debt, which should be repaid before the end of 2010, is equal to 7 bln hryvnia. **We consider this amount to be insignificant and expect that it will be refinanced through new OVDP placements in 2010.**

**Though the official budget deficit for January-July 2010 amounts to 27.7 bln hryvnia, corresponding to the government forecast, we consider it quite probable that the effective deficit for 2010 will widen, since some sources of state income look unreliable (inter alia privatization plans). We think that the main sources of covering the deficit will be the placement of OVDPs and new Eurobonds, in addition to IMF financing.**

## Inflation

Inflation in August was positive for the first time since April. Consumer prices increased by 1.2% basically due to the hike in gas tariffs and excise taxes. **We expect that inflation will accelerate as of September due to expected seasonal growth in food prices, which should create the preconditions for the toughening of NBU monetary policy.**

**We think that the drop in the inflow of deposits, expected as of September, together with inflation expectations, will provoke interbank money rates to surge, as well as OVDP yields, by the end of 2010. At the same time, the excess banking liquidity accumulated since the beginning of 2010 will limit this yield growth to 100-200 b.p.**

## Liquidity

The recent dynamics in short-term rates, which we see as among most powerful indicators of interbank liquidity, confirm our expectations so far. Over the last five working days, the 1-week rate added 0.24 p.p. to reach 1.15%, and the 2-week rate increased by 0.04 p.p. to 1.93%. At the same time, the average short-term rate calculated by the NBU skyrocketed with a growth of 1.3 p.p.

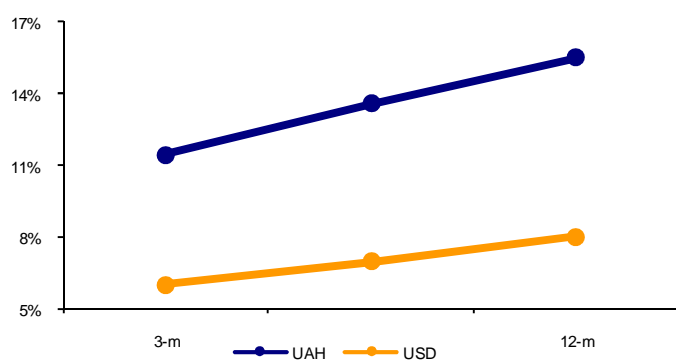
In spite of the above-described trends, commercial banks' balances in NBU correspondent accounts increased slightly, by 0.9 bln hryvnia, at the beginning of this week.

**Outlook: We expect interbank financing to become more expensive by the end of 2010, while the National Bank of Ukraine will refrain from refinancing the banking system.**

Ukrainian bonds market: (30.08.2010-03.09.2010)				
PFTS Ticker	Issuer	Coupon	Volume, UAH mln	YTM
74173	Ukraine, 02.02.2011	-	578.20	9.5%
63648	Ukraine, 26.01.2011	-	183.04	9.2%
61451	Ukraine, 31.10.2012	20.0%	74.02	18.2%
63309	Ukraine, 13.10.2010	-	69.07	7.7%
62012	Ukraine, 23.11.2011	20.0%	68.30	16.8%
53912	Ukraine, 11.04.2012	15.7%	55.29	17.9%
66526	Ukraine, 18.05.2011	-	48.73	10.5%
81202	Ukraine, 07.08.2013 (SP issue Euro-2012)	12.0%	48.33	12.8%
61089	Ukraine, 12.10.2011	25.1%	40.47	25.0%
66880	Ukraine, 04.09.2013	12.5%	22.32	15.0%
65403	Ukraine, 20.10.2010	-	19.83	6.9%
76780	Ukraine, 27.07.2011	-	13.69	11.3%
63564	Ukraine, 12.09.2012	20.0%	12.20	18.3%
61725	Ukraine, 17.11.2010	-	12.12	7.7%
64166	Ukraine, 28.01.2015	15.0%	11.05	15.9%
83075	Ukraine, 31.08.2011	-	4.51	11.5%
OOMAVA	Omega-avtopostavka, 1-A	25.0%	1.17	25.2%
OOMAVB	Omega-avtopostavka, 1-B	25.0%	1.13	24.3%
54456	Ukraine, 27.04.2011	20.0%	1.13	23.1%
OMAUPA	MAUP, 1-A	23.0%	0.90	-
OROMA	Roma, 1-A	15.0%	0.80	27.6%
OSENA2	Sevastopolenergo, 2-A	18.0%	0.54	-
OKIONA	Kirovogradoblenergo, 1-A	23.0%	0.53	-
OZHENB	Zhytomyroblenergo, 1-B	23.0%	0.53	26.2%
OOREA	Oreanda, 1-A	12.0%	0.50	-
OKIONB	Kirovogradoblenergo, 1-B	23.0%	0.50	26.2%
OSENB	Sevastopolenergo, 2-B	23.0%	0.50	26.2%
OZHENA	Zhytomyroblenergo, 1-A	17.0%	0.50	-
78141	Ukraine-VAT1	5.5%	0.18	18.1%
IPVENA	Vena, 1-A	20.0%	0.14	-
OBSSTA	Bank Business Standard,1-A	18.0%	0.12	-
22509	Ukraine, 28.09.2011	9.5%	0.02	13.0%

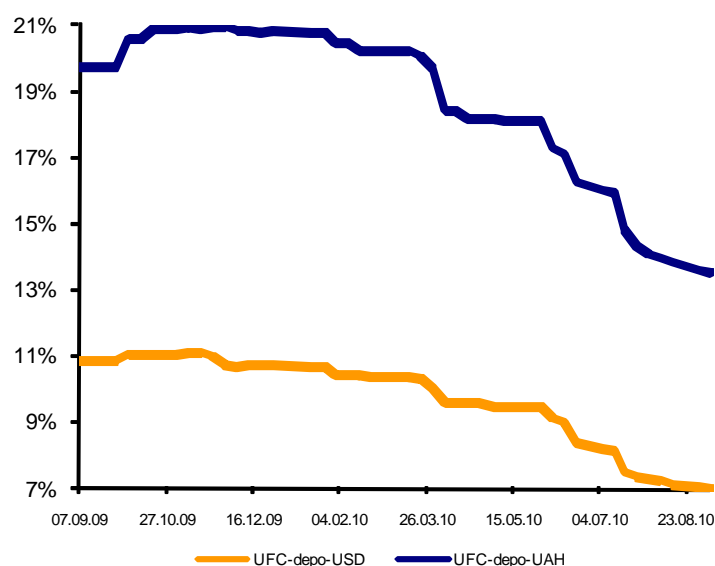
## Depo rates

### UAH depo/USD depo yield curve



The UFC-depo-UAH and UFC-depo-USD indices demonstrated the first signs of stabilization last week. The UFC-depo-UAH index declined by 0.1 p.p. and the UFC-depo-USD index remained unchanged. ***In our opinion, after a significant drop, depo rates should stay at the current levels for a while and may even surge afterwards in the case that liquidity is squeezed further.***

### UAH depo/USD depo rates dynamics



## Government bonds

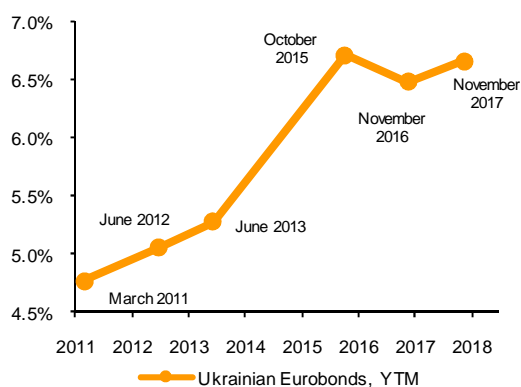
Activity in the sovereign Eurobonds segment has been improving since the beginning of September. At the same time, current levels of sovereign Eurobonds quotations seem to be rather high, leaving a very small upside potential – the main reason for the cautious attitude on the part of investors.

The government of Ukraine is still considering the organization of a new Eurobonds placement in the near future. ***There are strong chances that the new placement will succeed by exploiting the low yields for existing sovereign bonds. However, the possible toughening of the global debt market may cause the new issue to be rescheduled.***

Ukrainian bonds rating (internal methodology*)		
Corporate		
Agromat, 1-B	OAGMTB	ufcBB
Amstor, 1-E	OAMSE	ufcCCC
Bogdan, 1-B	OLUAZB	ufcBB
Galychina, 1-C	OGLCHC	ufcB
Galnaftogaz, 1-E	OGNGE	ufcBBB
Donetskstal, 1-A	CODSTA	ufcBB
Kirovogradoblenergo, 1-A	OKIONA	ufcB
Konti, 1-B	OKKOB	ufcB
MAUP, 1-A	OMAUPA	ufcB
Sevastopolenergo, 2-A	OSENA2	ufcB
Sumykhimprom, 1-A	OSUMHA	ufcCC
Favorit, 1-B	COFRAB	under revision
HARP Trading, 1-B	OHRPTB	ufcBB
Khlibprom, 1-D	OHLPD	ufcB
Financial		
Alfa Bank, 1-F	OALFF	ufcBBB-
Khreschatik Bank, 1-E	OBXRE	ufcBBB
Dongorbank, 3-C	ODGBC2	ufcB
Imexbank, 1-A	OIMEXA	ufcBB
Kreditprombank, 1-F	COKPBF	ufcCC
FUIB, 1-A	COPUMB	ufcA
Raiffeisen Bank Aval, 1-B	OBVLB	ufcA
Rodovid Bank, 1-C	ORODBC	ufcCC
Ukrgazbank, 1-A	OUGZBA	ufcCCC
Ukrsotsbank, 1-D	OUSCD	ufcA
Forum, 1-C	OPRXBC	ufcBBB

\*- Follow the link below to get to the internal methodology of UFC Capital for corporate bonds rating:  
[http://www.ufc-capital.com/en/analysis/bonds\\_rate.htm](http://www.ufc-capital.com/en/analysis/bonds_rate.htm)

## Ukrainian Eurobonds yield curve



This week's OVDP placement saw a small number of successful applications, while demand remained high. MinFin placed OVDPs for a total amount of 452.7 mln hryvnia, which is less than half of the volume placed last week.

The bulk of the demand at the auction was concentrated on the short end of the curve. A total of 17 applications were submitted for 3-month bonds in the amount of 1.2 bln hryvnia. However, most of them were uncompetitive. In this case, the Ministry of Finance lowered the cap rate to 6.75%, satisfying only two applications.

For bonds maturing in April 2011, five applications were submitted, two of which were satisfied. The yield of this series was 9.5% and the volume placed reached 108.6 mln.

Bonds maturing in 2012 attracted only one application with a yield of 11.75%, which the Finance Ministry left unsatisfied.

The 3-year special purpose government bonds, which are used by banks to cover their mandatory reserves, attracted three applications for a total of 196 million hryvnia, all of them satisfied at an effective yield of 12%.

**Outlook: *Despite the issuance of VAT bonds, demand for short-term bonds remains high. At the same time, we note the lack of demand for long bonds. In our opinion, the gradual appearance of VAT bonds on the secondary market will cause a drop in activity at primary OVDP auctions.***

## Secondary fixed income market

In the corporate Eurobonds segment, last week was marked by resumed price growth for high quality bonds, such as MHP, Metinvest and DTEK. We also draw investors' attention to the dynamics of Kyiv-15 bonds, which added one figure and are currently trading at an effective yield of 10%. We think that the City's bonds should be considered as quasi-sovereign debt and represent alternatives to sovereign Eurobonds.

Last week, the Standard & Poor's rating agency upgraded its forecast on the Alfa Bank (Ukraine) ratings from stable to positive, as well as improving its rating on the national scale from uaBB- to uaBB. The revision was connected to the improved liquidity of the country's financial institutions, its strong position on the Ukrainian market, and the Bank's recent additional capitalization.

**Outlook: *We expect that overall improvements in the Ukrainian banking sector will enable the Bank to record a positive net margin in 2010, which, together with support from its parent structure, is also reason to expect an upgrade in the long-term rating of Alfa Bank (Ukraine) to the B level in the near future (see also our flashnote *UFC Capital. Ukrainian Eurobonds: Banking sector*, dated August 16, 2010).***

## Eurobonds

Issuer	bid	ask	Yield (bid)	Yield (offer)	Coupon	Z-Spread* (bid/offer)	Mod. Duration	Volume, mln	Currency	Maturity
Ukraine, 2011	100.50	101.00	5.81%	4.77%	6.875%	2615/2240	0.47	600	USD	04.03.2011
Ukraine, 2012	102.00	102.25	5.20%	5.05%	6.385%	535/ 505	1.66	500	USD	26.06.2012
Ukraine, 2013	105.38	106.00	5.52%	5.28%	7.650%	590/ 580	2.43	1 000	USD	11.06.2013
Ukraine, 2015	92.00	92.50	6.83%	6.71%	4.950%	189/ 176	4.11	600	EUR	13.10.2015
Ukraine, 2016	100.00	100.50	6.58%	6.48%	6.580%	632/ 621	4.93	1 000	USD	21.11.2016
Ukraine, 2017	100.00	100.50	6.75%	6.66%	6.750%	460/ 451	5.50	700	USD	14.11.2017
IUD, 2010	20.00	40.00	-	-	9.250%	N/A	N/A	150	USD	23.09.2010
Azovstal, 2011	100.25	101.25	8.66%	6.47%	9.125%	807/ 589	0.44	175	USD	28.02.2011
Kyiv, 2011	100.00	100.75	8.60%	7.68%	8.625%	788/ 695	0.79	200	USD	15.07.2011
UkrSibbank, 2011	101.75	102.50	7.20%	6.34%	9.250%	759/ 701	0.85	250	USD	04.08.2011
Ukreximbank, 2011	100.75	101.50	6.86%	6.07%	7.650%	602/ 523	0.94	500	USD	07.09.2011
UkrSibbank, 2011	100.75	101.25	7.11%	6.70%	7.750%	693/ 652	1.19	500	USD	21.12.2011
Privatbank, 2012	98.50	99.25	9.15%	8.57%	8.000%	836/ 797	1.29	500	USD	06.02.2012
Alfa Bank (Ukraine), 2012	101.75	102.50	11.92%	11.47%	13.000%	1030/ 951	1.64	841	USD	30.07.2012
Ukreximbank, 2012	99.75	100.25	6.93%	6.67%	6.800%	620/ 594	1.85	250	USD	04.10.2012
Kyiv, 2012	97.00	98.00	9.78%	9.26%	8.250%	900/ 848	1.92	250	USD	26.11.2012
Finance and Credit, 2014	82.50	86.00	17.57%	16.01%	10.500%	1645/1489	2.61	100	USD	25.01.2014
VAB Bank, 2014	74.00	78.00	20.77%	18.91%	10.500%	870/ 846	2.79	125	USD	14.06.2014
Naftogaz of Ukraine, 2014	110.50	110.75	6.51%	6.45%	9.500%	2094/1947	3.26	1 595	USD	30.09.2014
PUMB, 2014	91.00	93.50	13.83%	13.01%	11.000%	1241/1160	3.25	275	USD	31.12.2014
Ukreximbank, 2015	103.50	104.00	7.46%	7.34%	8.375%	596/ 583	3.70	500	USD	27.04.2015
DTEK, 2015	101.75	102.38	9.02%	8.86%	9.500%	753/ 736	3.58	500	USD	28.04.2015
MHP, 2015	104.00	104.50	9.17%	9.03%	10.250%	735/ 722	3.53	585	USD	29.04.2015
Metinvest, 2015	105.25	105.75	8.85%	8.72%	10.250%	6750/3757	3.59	500	USD	20.05.2015
Kyiv, 2015	91.00	92.00	10.29%	10.02%	8.000%	864/ 837	3.96	250	USD	06.11.2015
Privatbank, 2016	91.50	93.00	10.86%	10.47%	8.750%	1207/1016	0.37	150	USD	09.02.2016
Ukreximbank, 2016	96.00	98.00	9.35%	8.87%	8.400%	764/ 715	4.21	125	USD	09.02.2016

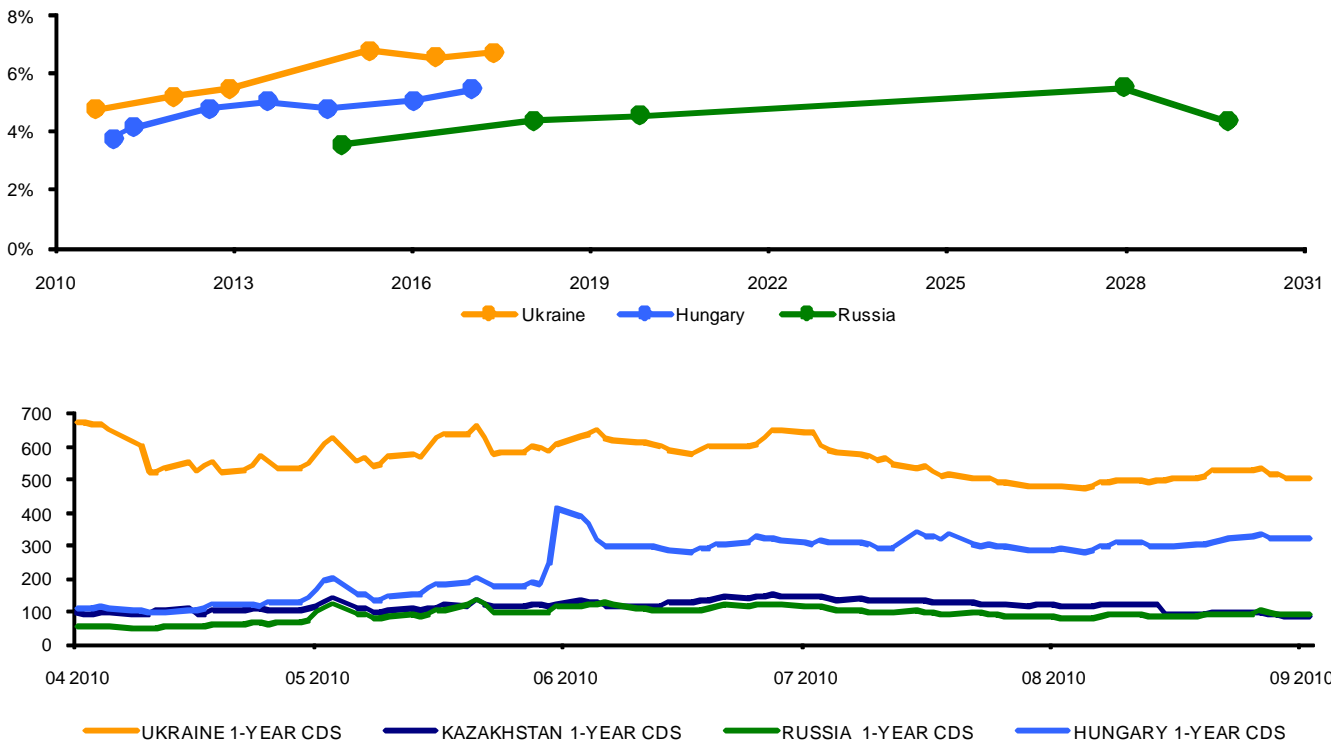
\* – Z-spread over US state bonds

## OVDPs

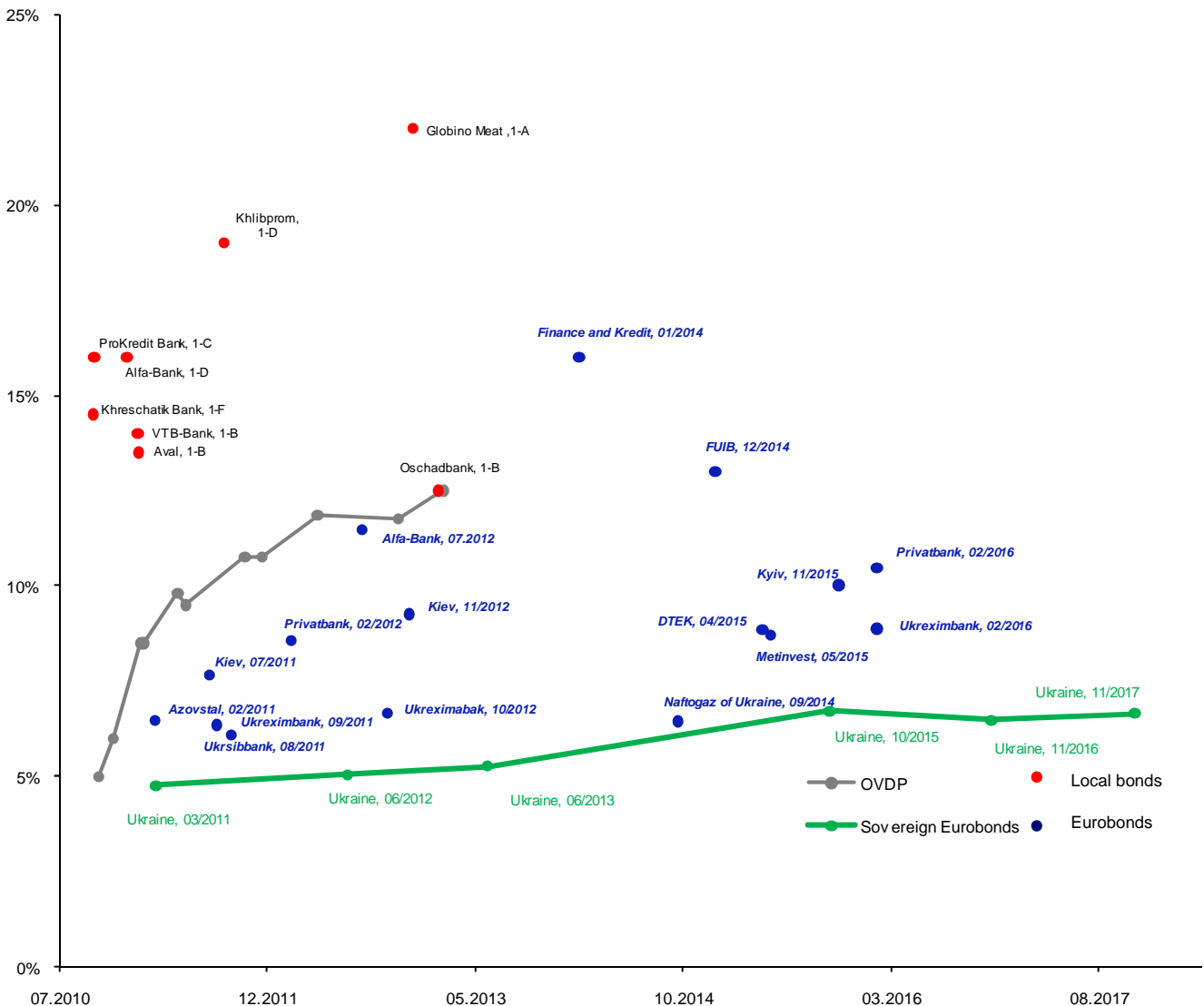
Issuer, ticker	bid	ask	Yield (bid)	Yield (offer)	Coupon	Mature
Ukraine, 63309*	993.95	994.96	6.00%	5.00%	-	13.10.2010
Ukraine, 61725*	987.34	988.30	6.50%	6.00%	-	17.11.2010
Ukraine, 63648*	965.26	967.99	9.25%	8.50%	-	26.01.2011
Ukraine, 74173*	962.67	966.46	9.50%	8.50%	-	02.02.2011
Ukraine, 54456	1 130.69	1 134.97	10.50%	9.80%	20.00%	27.04.2011
Ukraine, 66526*	930.40	937.99	10.75%	9.50%	-	18.05.2011
Ukraine, 61089	1 241.42	1 248.88	11.45%	10.75%	25.14%	12.10.2011
Ukraine, 62012	1 154.05	1 162.56	11.50%	10.75%	20.00%	23.11.2011
Ukraine, 53912	1 116.69	1 122.28	12.25%	11.85%	15.70%	11.04.2012
Ukraine, 61451	1 213.82	1 228.31	12.50%	11.75%	20.00%	31.10.2012
Ukraine, 64018	1 249.05	1 265.40	13.25%	12.50%	20.00%	20.02.2013

Note: For issues marked \* simple yields are specified, while for the rest issues – effective yields

## Sovereign Eurobonds yield curves and CDS dynamics



## OVDPs yield curve and effective YTM of Ukrainian hryvnia-denominated bonds vs. Eurobonds





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