

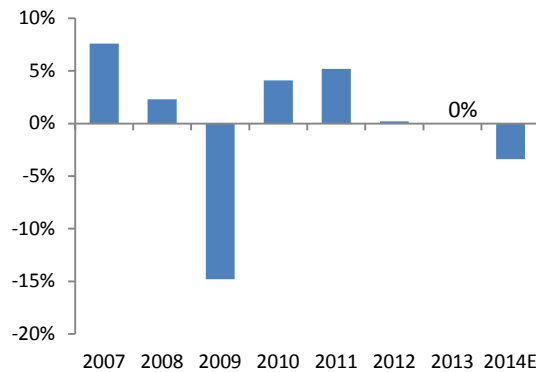
Ukraine Monthly

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Economy

Real GDP, chg. yoy



Sources: UkrStat, SP Advisors

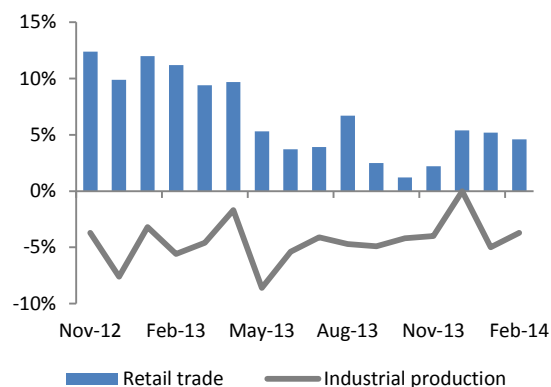
Real GDP and its components, chg. yoy

	2013	2014E (new)	2014E (old)*
GDP	0.0%	-3.4%	1.2%
Household consumption	7.8%	-3.5%	4.5%
Gross fixed capital	-6.6%	-15.0%	0.1%
Export	-8.8%	-14.0%	0.8%

* early-January projections

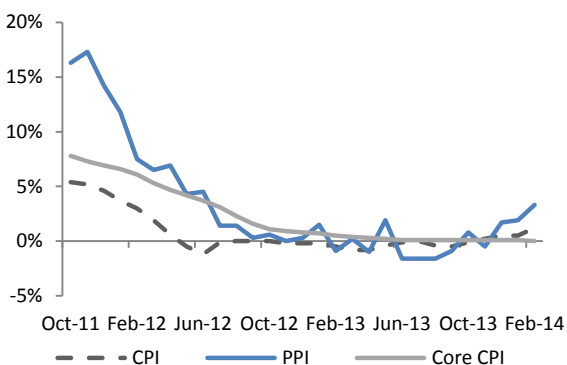
Sources: UkrStat, SP Advisors

Monthly retail trade and industrial production, chg. yoy



Source: UkrStat

CPI and PPI, yoy



Source: UkrStat

The Ukrainian economy is entering a period of painful adjustment following the historical change in the political landscape and against the backdrop of the Russian military intervention. Economic activities will slow and we expect GDP to decline 3-4% in 2014, an unpleasant fall, but still a far cry from 2009's 14.8% drop. The current recession is mainly the result of accumulated structural flaws and uncertainties related to the Russian military threat. That it is happening against a backdrop of accelerating global growth offers hope that the recovery will be swift and pronounced once Ukraine returns to the path of reforms and if fears of a full-fledged military invasion fade. A new IMF-Ukraine program with severe strings attached will be launched in the coming weeks. The recent hryvnia depreciation will drive a swift adjustment in the C/A gap to some 3.5-4.5% of GDP from last year's 8.9%. We now expect an average exchange rate of UAH 10.1/USD in 2014. The government will be forced to narrow the state budget deficit to 3.0-3.5% of GDP and we expect it will service all sovereign debt without disruption thanks to international financial support.

GDP to decline as growth pillars weaken on broad-based uncertainties

By our estimates the Ukrainian economy re-entered recession in 1Q14 and we expect GDP will shrink 3-4% in 2014. Household and business sentiment turned cautious in recent weeks on the back of political uncertainty, the sharp hryvnia depreciation and related financial market distress, and the military threat from Russia. Households are freezing expenditures while businesses are delaying investment projects. Many local companies will be hit by the breaking of ties with Crimea. Also large Ukrainian corporates may be hurt by broad investigations by US and EU authorities against Ukrainian oligarchs connected with ex-President Yanukovich.

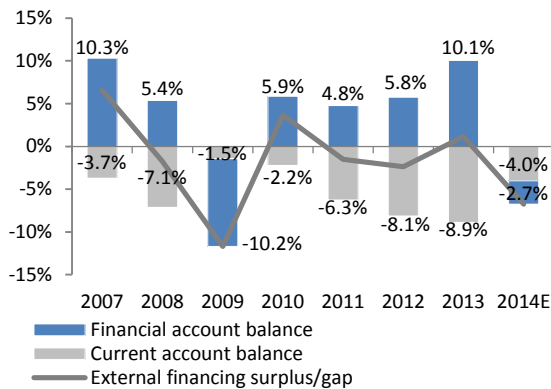
Below we provide our view on key GDP component trends (see please projections in the left column):

Household consumption will decline 3.5% yoy in real terms in 2014, by our estimates, following robust 7.8% growth in 2013. Nominal salaries, both public and private, will be frozen or will fall slightly. Social payments should also remain flat under our base scenario. Even so, an increase in consumer prices will push real household income into negative territory. The sweetener here is that an adjustment in household incomes and expenditures will first and foremost weaken consumer goods imports, paving the way for a substitution effect that will favor domestic producers.

Investment will be depressed as heightened political and macroeconomic risks take their toll. Credit will remain practically unavailable for the private sector as debt investors and banks remain in a holding pattern until the country re-starts IFI lending programs, sovereign default risks diminish, and interest rates normalize. Weakening domestic demand and bleak prospects for a recovery of exports will also deter new investments.

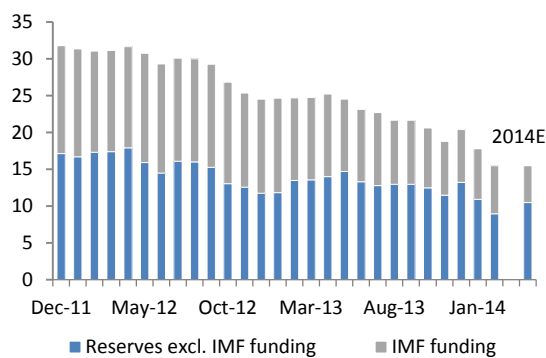
We revise our projections for 2014 **exports** down considerably as the key growth drivers we had hoped for have vanished entirely. Russia abolished the gas price discount for Ukraine, which leaves industry with perhaps the most expensive gas in Europe. Russia will also reportedly not cancel non-tariff barriers for Ukrainian companies in the foreseeable future. The EU-Ukraine free trade agreement will not provide a significant bump in the short-term and will not offset a partial loss of the Russian market.

External financing balance, % of GDP



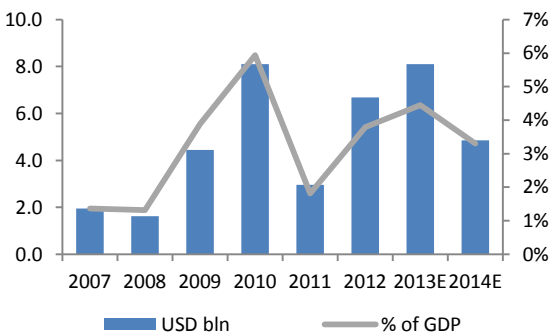
Sources: NBU, SP Advisors

NBU gross international reserves, USD bln



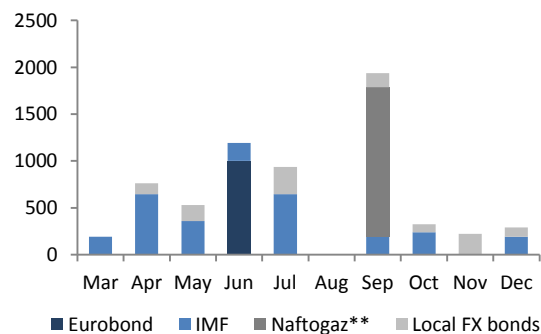
Sources: NBU, Finance Ministry

State budget deficit



Sources: Finance Ministry, SP Advisors

Sovereign FX debt redemption, USD mln*



* excludes interest payments on FX debt (USD 1.2-1.4 bln)

** state-guaranteed Naftogaz Eurobond

Sources: Finance Ministry, IMF, SP Advisors

We underscore the growing risk of upcoming distortions in macro data as the Crimean statistics agency is likely to stop providing input to the central office in Kyiv. We expect UkrStat to start publishing pro forma reports that exclude Crimea from the general profile. Crimea accounts for c. 3.7% of Ukraine's GDP, so national accounts will see a corresponding decline in nominal terms. Real numbers will be affected to a much lesser extent.

Inflation to pick up on hryvnia depreciation, regulated tariff hikes

Consumer inflation has remained below 5% for the past two years – an unprecedented period of muted price growth in Ukraine's history. That trend is set to reverse course in the coming months. The recent fall of the hryvnia is already fuelling inflationary pressures, but a robust second wave is coming. On top of that, the government has made it clear it plans to hike gas-linked utility tariffs to narrow Naftogaz's cash deficit. We see this year's hike at some 40-50%, which will add 3-4ppts to inflation this year. Overall we expect CPI growth to reach 8.9% by end-2014 before abating to a more reasonable 5-6% in subsequent years.

C/A deficit to narrow on weaker hryvnia, anemic domestic demand

We expect an average hryvnia rate 20% weaker yoy in 2014 (UAH/USD of 10.1 vs. 8.1 in 2013) which will squeeze the C/A shortfall to an estimated 3.5-4.5% of GDP from last year's 8.9%. The narrowing of the C/A deficit will also be helped by a decline in household demand and a slump in imports of investment goods. Overall, we expect imports to fall by more than exports.

Even though we expect it to halve yoy, the C/A gap will still pose a risk for the economy as raising debt and attracting FDI to cover the shortfall will be a huge challenge. Global capital markets will be effectively closed for Ukraine's government, to say nothing of private issuers, at least until September 2014 when political risks fade following the presidential election and the IMF-Ukraine program gains a head of steam.

We expect the financial sector and non-financial corporate sector will see net capital outflows this year as most borrowers will fail to roll over maturing external debt obligations. Meanwhile, the government should be able to raise a substantial amount of debt from IFIs and other states. We think the IMF may approve a program of USD 15-20 bln overall, with about USD 8 bln disbursed this year. Based on that, we expect the NBU's end-2014 reserves at USD 15.5 bln (-24% yoy), roughly the current level.

The hryvnia exchange rate will remain volatile over the next couple of months within a range of UAH 9.5-11.0/USD. The NBU may re-enter the market after the first IMF funds are disbursed to smooth fluctuations and re-introduce certainty, visibility, and stability to market participants. We expect an average exchange rate of UAH 10.1/USD.

Budget deficit to narrow to 3.0-3.5% of GDP, government to service sovereign debt smoothly

We see central budget revenues declining 3% yoy in 2014. Even though the economy should expand marginally in nominal terms, huge tax prepayments from last year imply lower receipts in the current year. We see tax collection falling c. 10% yoy in 2014 but a surge in non-tax revenues will partly offset that decline. We expect the NBU to hike transfers from its net income and equity to the budget as it did in 2013 and account for up to 12% of all central budget revenues.

State budget funding in 2014, USD bln

Total funding needs	15.9
Budget deficit	4.8
Redemptions due	11.1
Domestic debt	5.9
Foreign debt*	5.2
Funding sources	15.9
External borrowings	6.5
EU (macro financial assistance)	2.2
USA (loan guarantees)	1.0
World Bank (budget assistance)	1.0
Other governments	0.3
IMF (budget assistance)	2.0
Domestic borrowings	8.9
Privatization	0.5

* including USD 1.6 bln in state-guaranteed Naftogaz Eurobond

Source: SP Advisors, Law on 2014 State Budget

In addition to falling revenue collection, the government will face huge difficulties raising debt. Local banks are facing liquidity constraints due to a run on deposits, and external public debt markets will remain closed at least until 3Q14. Against that backdrop, the government will be forced to slash expenses 5-6% yoy and narrow the fiscal gap to 3.0-3.5% of GDP (USD 4.4-5.1 bln) in 2014 from 4.4% in 2013, in our view.

We remain confident Ukraine will be able to service its debt smoothly thanks to hefty borrowings from IFIs and direct loans from other governments. We estimate the total funding needs of the Ukrainian government at USD 15.9 bln in 2014 (USD 4.8 bln for the budget deficit and USD 11.1 bln in debt redemptions), of which roughly USD 6.5 bln will be sourced as external loans (see please table on the left).

The US has committed USD 1 bln in loan guarantees, the EU plans to release a EUR 1.6 bln in macro financial assistance, and the World Bank may come in with another USD 1.0 bln in budget assistance. We also expect the IMF will agree to provide a part of its loan as direct budget support, just as in 2008-09.

This will provide the government with sufficient FX liquidity to fully service sovereign debt, facilitate the redemption of the state-guaranteed USD 1.6 bln Naftogaz Eurobond, and repay FX-denominated domestic t-bills. Domestic borrowings may total USD 8.9 bln, according to our projections. This is equal to 7.4% of banking sector assets, a manageable amount providing the NBU supports bank liquidity via the purchase of t-bills in open market operations.

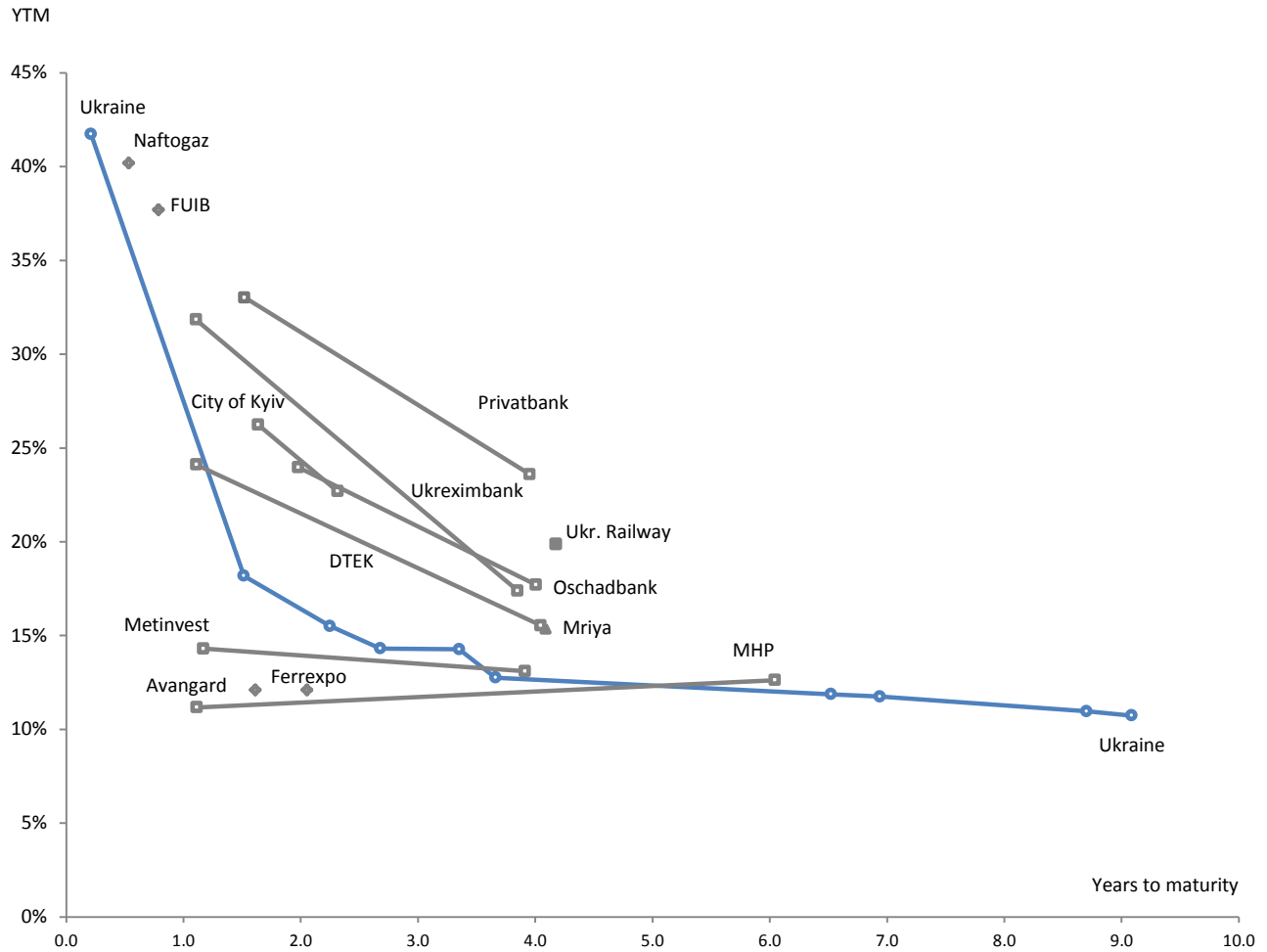
Appendix A. Key macro data and projections

	2007	2008	2009	2010	2011	2012	2013	2014E
Business cycle indicators								
Real GDP, chg yoy	7.6%	2.3%	-14.8%	4.1%	5.2%	0.2%	0.0%	-3.4%
Household consumption, chg yoy	17.1%	11.8%	-14.9%	7.1%	15.7%	11.7%	7.8%	-3.5%
Investments in fixed capital, chg yoy	23.9%	1.6%	-50.5%	3.9%	7.1%	0.9%	-6.6%	-15.0%
Industrial output, chg yoy	7.6%	-5.2%	-21.9%	11.2%	7.6%	-1.8%	-4.7%	-5.8%
Nominal GDP, UAH bln	721	948	913	1,083	1,302	1,409	1,455	1,484
Nominal GDP, USD bln	143	180	117	136	163	176	182	147
GDP per capita, USD	3,078	3,891	2,550	2,982	3,585	3,875	4,002	3,237
CPI, eop	16.6%	22.3%	12.3%	9.1%	4.6%	-0.2%	0.5%	8.9%
CPI, avg	12.8%	25.2%	15.9%	9.4%	8.0%	0.6%	-0.3%	4.1%
Unemployment (ILO methodology, avg)	6.9%	6.9%	9.6%	8.8%	8.6%	8.1%	7.6%	7.8%
External accounts								
Current account balance, USD bln	-5.3	-12.8	-1.7	-3.0	-10.2	-14.3	-16.1	-5.9
% of GDP	-3.7%	-7.1%	-1.5%	-2.2%	-6.3%	-8.1%	-8.9%	-4.0%
Financial account balance, USD bln	14.7	9.7	-12.0	8.0	7.8	10.1	18.2	-4.0
% of GDP	10.3%	5.4%	-10.2%	5.9%	4.8%	5.8%	10.0%	-2.7%
FDI net, USD bln	9.2	9.9	4.7	5.8	7.0	6.6	3.3	1.9
% of GDP	6.5%	5.5%	4.0%	4.2%	4.3%	3.8%	1.8%	1.3%
Gross NBU reserves (eop), USD bln	32.5	31.5	26.5	34.6	31.8	24.5	20.4	15.5
Monetary and banking indicators								
Monetary base, UAH bln	142	187	195	226	240	255	307	320
Monetary base, chg. yoy	46%	32%	4%	16%	6%	6%	20%	4%
Money supply (M3), UAH bln	396	515	487	598	683	773	906	1,025
Money supply, chg. yoy	52%	30%	-5%	23%	14%	13%	17%	13%
Monetary multiplier (M3/MB, eop)	2.8	2.8	2.5	2.6	2.8	3.0	3.0	3.2
Bank loans, chg. yoy	74%	72%	-2%	1%	10%	2%	12%	11%
Bank deposits, chg. yoy	52%	28%	-8%	26%	18%	16%	17%	10%
Loan-to-deposit ratio	152%	205%	219%	175%	162%	143%	136%	138%
Exchange rate								
Official UAH/USD (eop)	5.05	7.70	7.99	7.96	7.99	7.99	7.99	9.90
Official UAH/USD (avg)	5.05	5.27	7.79	7.94	7.97	7.99	7.99	10.10
Market UAH/USD (eop)	5.05	7.82	8.01	7.97	8.04	8.05	8.24	9.90
Budget and debt indicators								
State budget revenues, USD bln	32.9	44.0	26.9	30.3	39.5	43.3	42.5	32.6
% of GDP	23.0%	24.4%	23.0%	22.2%	24.2%	24.6%	23.3%	22.2%
State budget expenditures, USD bln	34.8	46.4	31.5	38.4	42.4	50.0	50.5	37.5
% of GDP	24.4%	25.8%	26.8%	28.2%	26.0%	28.3%	27.8%	25.5%
State budget balance, USD bln	-1.9	-2.4	-4.6	-8.1	-3.0	-6.7	-8.1	-4.8
% of GDP	-1.4%	-1.3%	-3.9%	-5.9%	-1.8%	-3.8%	-4.4%	-3.3%
Public debt, USD bln	17.6	24.6	39.8	54.3	59.2	64.5	73.1	76.9
% of GDP	12.3%	13.7%	34.0%	39.8%	36.3%	36.6%	40.1%	52.3%

Sources: NBU, UkrStat, Ministry of Finance, Bloomberg, SP Advisors

Appendix B. Ukraine Eurobond universe (1)

Ukraine Eurobond yield map*



*as of Mar. 18, 2014.
Source: Bloomberg

Appendix B. Ukraine Eurobond universe (2)

Key parameters of Ukrainian Eurobonds

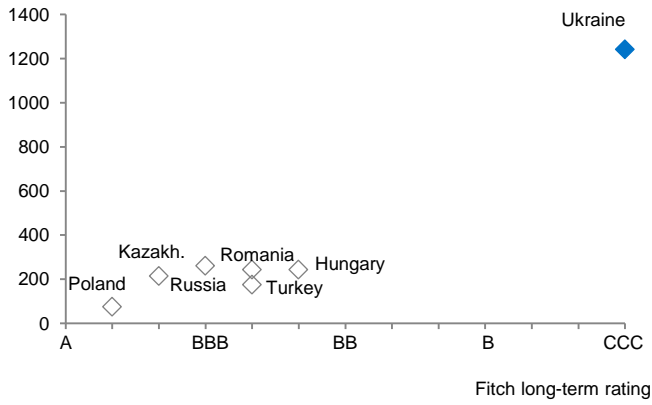
Name	Currency	Amount USD mln	Maturity	YTM,%		Mid. YTM change, pp		Rating		
				Mid	Spread	1 M	YTD	Fitch	Moody's	S&P
Sovereign										
Ukraine-14	USD	1,000	04.06.2014	41.73	11.16	21.18	-	CCC	Caa2	CCC
Ukraine-09/15	USD	500	23.09.2015	18.19	1.54	3.69	8.04	CCC	Caa2	CCC
Ukraine-10/15	EUR	600	13.10.2015	18.08	5.03	6.10	7.44	CCC	Caa2	CCC
Ukraine-12/15	USD	3,000	20.12.2015	5.30	0.61	0.01	-	CCC	Caa2	CCC
Ukraine-06/16	USD	1,250	17.06.2016	15.51	0.61	2.77	5.65	CCC	Caa2	CCC
Ukraine-11/16	USD	1,000	21.11.2016	14.31	0.52	1.36	4.44	CCC	Caa2	CCC
Ukraine-07/17	USD	2,600	24.07.2017	14.27	0.42	0.97	-	CCC	Caa2	CCC
Ukraine-11/17	USD	700	14.11.2017	12.76	0.69	1.54	2.36	CCC	Caa2	CCC
Ukraine-20	USD	1,500	23.09.2020	11.87	0.45	1.10	1.56	CCC	Caa2	CCC
Ukraine-21	USD	1,500	23.02.2021	11.75	0.43	0.94	1.75	CCC	Caa2	CCC
Ukraine-22	USD	2,250	28.11.2022	10.96	0.51	0.20	-	CCC	Caa2	CCC
Ukraine-23	USD	1,250	17.04.2023	10.74	0.30	0.54	-	CCC	Caa2	CCC
Infrastr. projects-11/17	USD	568	03.11.2017	16.27	0.87	3.67	4.06	-	Caa2	-
Infrastr. projects-12/17	USD	550	07.12.2017	16.46	0.55	1.30	-	-	(P)Caa2	-
Infrastr. projects-18	USD	690	20.04.2018	14.52	1.26	2.48	2.11	-	Caa2	-
Municipal										
City of Kiev-15	USD	250	06.11.2015	26.24	3.81	11.33	11.59	CCC	Caa2	CCC
City of Kiev-16	USD	300	11.07.2016	22.69	2.76	7.41	7.15	CCC	Caa2	CCC
Banks										
VAB Bank-14	USD	112	14.06.2014	-	-	-	-	WD	Caa2	-
FUIB-14	USD	252	31.12.2014	37.69	-	-	20.90	NR	Caa2	-
Ukreximbank-15	USD	750	27.04.2015	31.84	-	3.58	18.70	CCC	Caa2	-
Ukreximbank-16	USD	125	09.02.2016	30.59	-	5.66	13.17	C	Caa3	-
Ukreximbank-18	USD	600	22.01.2018	17.39	1.09	-0.94	-	CCC	Caa2	-
Oschadbank-16	USD	700	10.03.2016	23.97	1.81	2.56	9.58	CCC	Caa2	-
Oschadbank-18	USD	500	20.03.2018	17.71	0.37	-0.52	-	CCC	Caa2	-
Privatbank-15	USD	200	23.09.2015	33.04	-	12.48	15.15	CCC	Caa1u	-
Privatbank-16	USD	150	09.02.2016	30.18	6.09	4.73	9.48	-	Caa2u	-
Privatbank-18	USD	175	28.02.2018	23.61	1.62	4.70	-	CCC	Caa1u	-
Corporate										
Naftogaz-14	USD	1,595	30.09.2014	40.18	-	11.22	27.97	CCC	-	-
Avangardco-15	USD	200	29.10.2015	12.09	-	2.59	-7.18	CCC	-	-
MHP-15	USD	235	29.04.2015	11.17	-	0.95	-2.00	CCC	Caa1	-
MHP-20	USD	750	02.04.2020	12.63	-	-0.06	-	CCC	-	CCC
DTEK-15	USD	200	28.04.2015	24.11	-	12.85	12.00	CCC	Caa1	-
DTEK-18	USD	750	04.04.2018	15.54	-	2.44	-	CCC	Caa1	-
Metinvest-15	USD	500	20.05.2015	14.31	-	5.11	2.41	CCC	Caa1	-
Metinvest-18	USD	750	14.02.2018	13.10	-	0.60	0.24	CCC	Caa1	-
Mriya-16	USD	72	30.03.2016	-	-	-	-	CCC	-	CCC
Mriya-18	USD	400	19.04.2018	15.37	-	-0.16	-	CCC	-	CCC
Ferrexpo-16	USD	500	07.04.2016	12.09	-	-0.55	-	CCC	Caa1	CCC+
Ukrainian Railway-18	USD	500	21.05.2018	19.89	-	3.72	-	CCC	-	CCC
Ukrlandfarming-18	USD	500	26.03.2018	17.26	-	-	-	CCC	-	CCC

*as of Mar. 18, 2014.

Source: Bloomberg

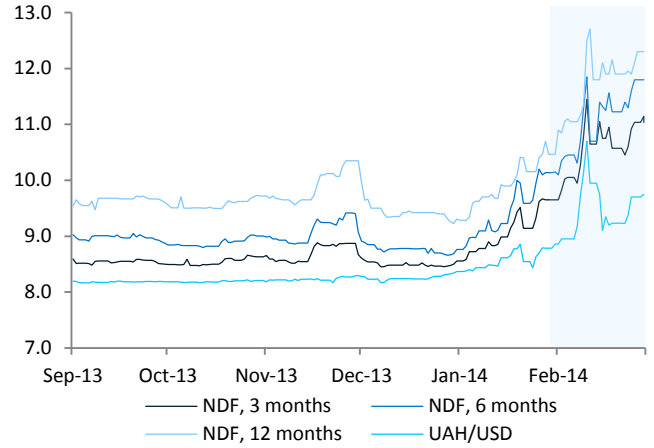
Appendix C. NDF and CDS

5Y CDS vs. Fitch long-term rating*



*data as of Mar. 18, 2014
Source: Bloomberg

HAH/USD spot and NDF rates, 6-m development



Source: Bloomberg

Ukraine sovereign Eurobond YTM, 6-m development



Source: Bloomberg

Appendix D. Ukrainian equity multiples

Ukrainian stock multiples*

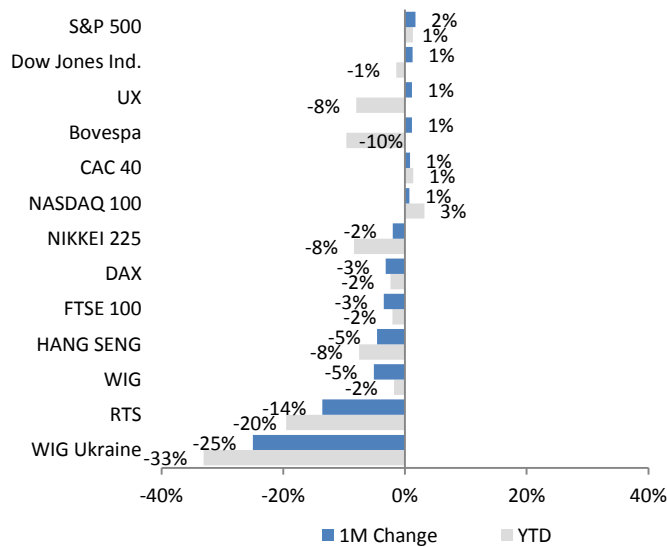
Sector / Company	Ticker	MCap, USD mln	EV/EBITDA		EV/Sales		P/B		P/E		Net Debt / Book Value	
			2013E	2014E	2013E	2014E	2013E	2014E	2013E	2014E	2013E	2014E
Agriculture												
Kernel	KER PW	712	4.5	3.2	0.5	0.4	0.5	0.4	6.8	3.9	0.39	0.27
MHP	MHPC LI	1,416	6.1	4.6	1.7	1.4	1.1	1.1	6.9	5.1	0.91	0.70
Mriya	MAYA GR	778	-	-	-	-	-	-	-	-	-	-
Astarta	AST PW	358	6.4	3.5	1.4	1.0	0.7	0.5	6.1	3.0	0.56	0.39
IMC	IMC PW	87	4.6	3.4	1.3	0.9	0.6	0.5	4.6	3.6	0.67	0.45
KSG Agro	KSG PW	29	-	-	-	-	-	-	-	-	-	-
Agroton	AGT PW	22	-	-	-	-	-	-	-	-	-	-
Median		-	5.4	3.5	1.3	0.9	0.6	0.5	5.5	3.7	0.62	0.42
Food												
Avangard	AVGR LI	558	2.3	1.9	1.0	0.8	0.4	0.4	2.5	2.7	0.07	-0.02
Ovostar	OVO PW	133	5.5	3.3	1.9	1.4	1.0	0.9	5.1	3.6	0.16	0.10
Milkiland	MLK PW	82	4.5	3.4	0.4	0.3	-	-	4.6	4.5	-	-
UkrProduct	UKR LN	5	2.8	1.9	0.2	0.2	0.2	0.2	2.9	1.8	0.39	0.24
Median		-	3.6	2.6	0.7	0.5	0.4	0.4	3.8	3.1	0.16	0.10
Oil & Gas												
JKX Oil & Gas	JKX LN	176	1.7	1.5	0.8	0.6	0.3	0.3	5.4	4.9	-0.01	-0.07
Kulczyk Oil	SEN PW	227	2.7	1.8	1.6	1.1	1.1	0.9	8.3	5.3	-0.08	-0.18
Regal Petroleum	RPT LN	58	-	-	-	-	-	-	-	-	-	-
Cadogan Petroleum	CAD LN	37	-	-	-	-	-	-	-	-	-	-
Median		-	2.2	1.6	1.2	0.9	0.7	0.6	6.9	5.1	-0.04	-0.13
Mining												
Coal Energy	CLE PW	24	-	-	-	-	-	-	-	-	-	-
Sadvaya Group	SGR PW	12	-	-	-	-	-	-	-	-	-	-
Median		-	-	-	-	-	-	-	-	-	-	-
Metals & Mining												
Ferrexpo	FXPO LN	1,440	4.2	4.6	1.2	1.3	0.7	0.7	5.8	7.3	0.29	0.25
Median		-	4.2	4.6	1.2	1.3	0.7	0.7	5.8	7.3	0.29	0.25
Real Estate												
TMM	TR61 GR	22	-	-	-	-	-	-	-	-	-	-
Median		-	-	-	-	-	-	-	-	-	-	-
Industrials												
Westa ISIC	WES PW	8	-	-	-	-	-	-	-	-	-	-
Median		-	-	-	-	-	-	-	-	-	-	-
Transportation												
KDM Shipping	KDM PW	42	-	-	-	-	-	-	-	-	-	-
Median		-	-	-	-	-	-	-	-	-	-	-

* as of Mar. 18, 2014.

Source: Bloomberg

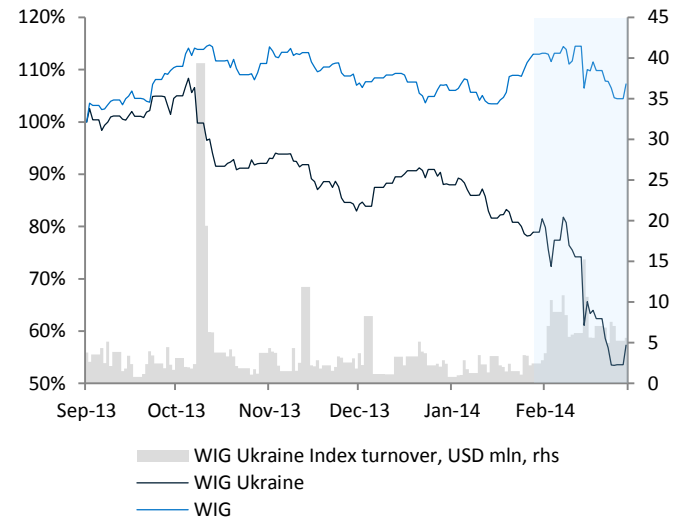
Appendix E. Stock market summary

Ukraine indexes (UX, WIG Ukraine) vs. global majors



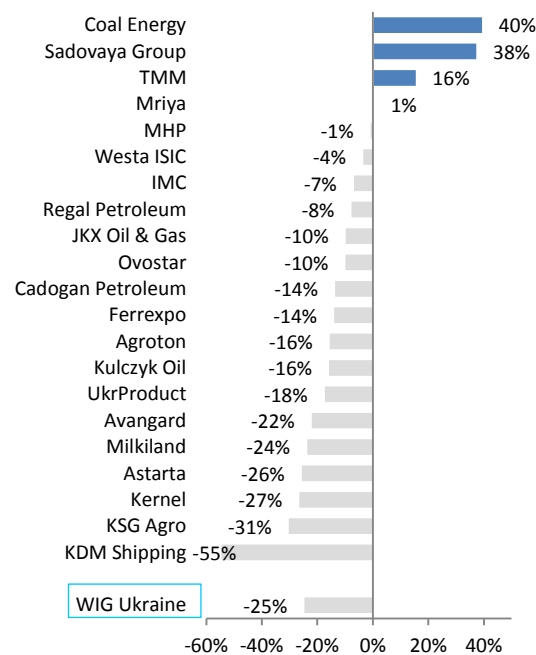
Data as of Mar. 18, 2014
Source: Bloomberg

WIG Ukraine vs. WIG, 6-month development



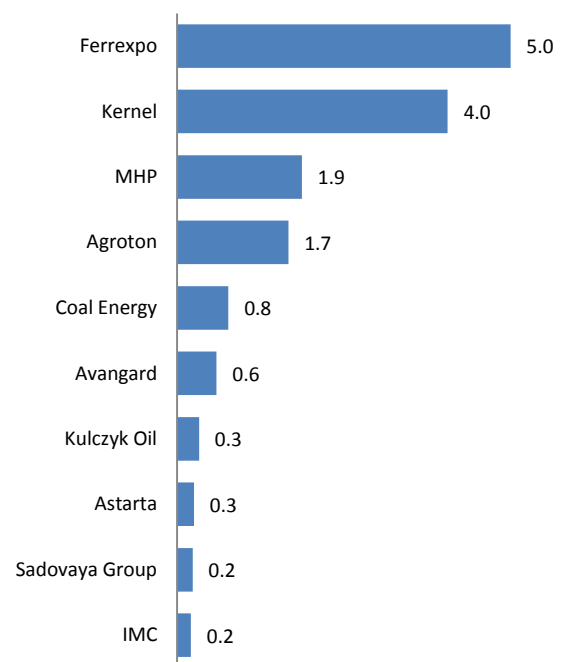
Source: Bloomberg

Ukrainian stock price change, mom*



* as of Mar. 18, 2014
Source: Bloomberg

Average daily trading in Ukrainian stocks, USD mln*



* Only top-10 stocks are shown, data are for Feb. 18, 2014 - Mar. 18, 2014
Source: Bloomberg

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