Ukraine Macro & Fixed Income Update

Things are getting better

September 30, 2022

CONCORDE CAPITAL

Summary

Many positive developments happened in Ukraine since late August. Among **good economic news**, there are:

- Better than earlier estimated Ukraine's GDP reported in 2Q22 (still a disastrous 37% decline yoy)
- Ukraine received large financial support from the U.S. government in late August, and the government outlined an optimistic support plan of the state budget for the next year - about USD 3.3 bln per month from the U.S., the EU and the IMF. This is not yet officially confirmed by the Western partners, but at least it gives an understanding where the government is going to take financing for most of its USD 4.5 bln expected monthly gap in the next year. On-going financial assistance is also encouraging for the outlook of Ukrainian currency, as it will help the central bank to keep its exchange rate fixed while building up gross international reserves.
- Partial removal of the blockade of sea ports due to grain convoys eases pressure on Ukrainian balance of payments. This will improve financial position of the companies exposed to farming & food: MHP (MHPSA) and Kernel (KERPW).

Even more encouraging news came from the battlefields as Ukraine made very successful counteroffensive and liberated most part of Kharkiv region in the north, as well as gained progress in the southern Kherson region. Its military success proves Ukraine is able to liberate its territories and demonstrates high efficiency of the Western military assistance. This should result in even more military supplies and, therefore, higher chance for Ukraine winning the war.

This also decreases security risk in the entire Kharkiv region as well as in Ukraine's second-largest city of Kharkiv. The development is also encouraging for Naftogaz (NAFTO, as now vast majority of its gas-producing assets are out of occupied territories and distant from the battlefields) and Kernel (KERPW, who regained control over its two seed cursing plants which used to be occupied).

Positive news came from other Eurobond issuers:

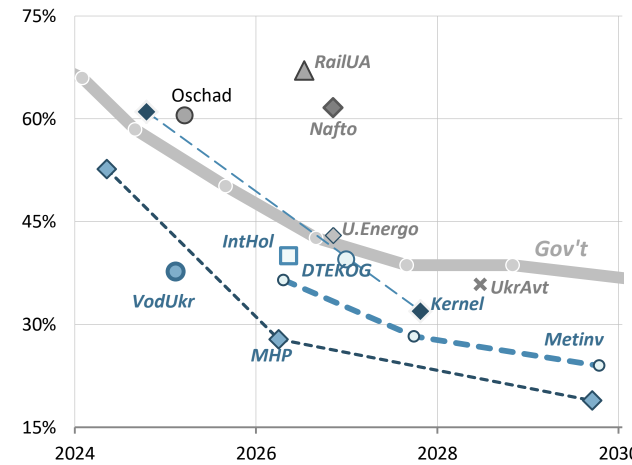
- MHP (MHPSA) reported the fourth month in raw of poultry sales recovery in August, as well as a radical improvement in EBITDA in 2Q22.
- Vodafone Ukraine (VODUKR) surprised with its EBITDA and a record-high margin in 2Q22.
- DTEK Oil & Gas is likely to pay less subsoil taxes since August, being able to further boost its P&L in 2022.
- DTEK Renewables got an increased share of payments from a state-controlled power buyer, and it is continuing to service its bonds despite its status of the most suffered Ukrainian bond issuer. Its behavior looks like a general strategy of the parent SCM to continue servicing related Eurobonds, including those of Metinvest and DTEK Energy.

Among the biggest risks and threats that recently emerged is Russia's reaction to Ukraine's successful offensive:

- Increased missile attacks on power and other vital infrastructure in central Ukraine.
- Announcement of massive mobilization of Russians to the war.
- Moves to "officially" annex four regions of Ukraine, with a threat to "defend" the newly grabbed territories by "using all means," thus implicitly threatening with a nuclear attack on Ukraine.

That indicates Putin is determined to continue the war, even though it is becoming more harmful to Russians and more risky to Russia's statehood. With this, the outlook of the war's development is becoming less optimistic: the war will become more bloody and most likely it won't end in 2023 (at the same time, the likelihood of Russia's internal collapse is increasing). Ukraine is going to cope with the first two actions with the help of the intensified supplies of Western equipment. Meanwhile, the efficient response to the indirect nuclear threat from Russia will demand an active involvement of all the top global leaders, in the West and the East.

Eurobond yield map



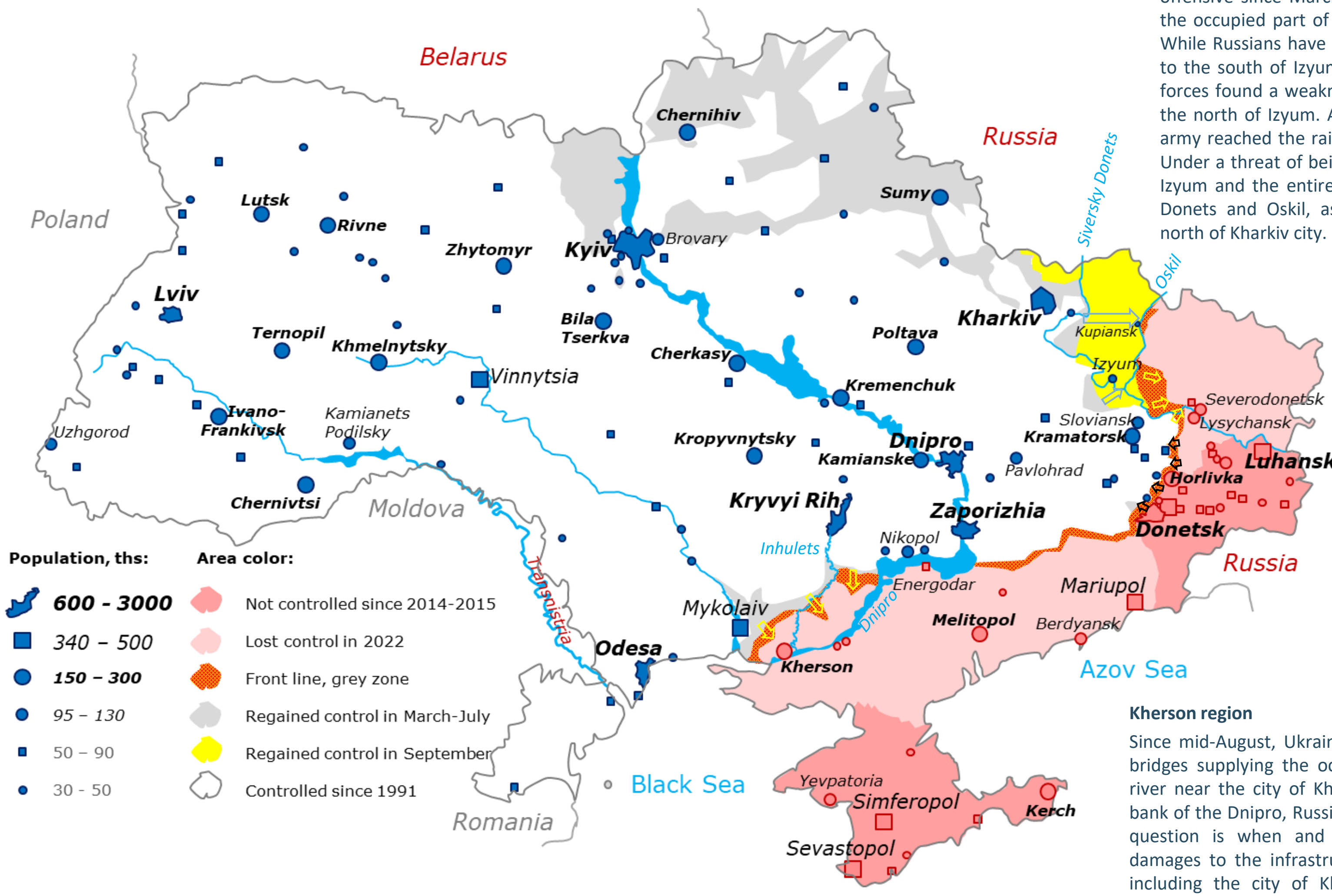
In the Eurobond universe, our top picks remain the instruments of the issuers that have a high chance to go through the hardships with minimal losses (**DTEKOG**, **VODUKR**), as well bonds of state banks (**OSCHAD** and **EXIMUK**) which have enough liquidity to repay the remainder of their bonds.

We also see a good speculative opportunity in the shortest bond of Metinvest (**METINV**), maturing in April 2023 and yielding over 150%. Things seem to go better in the company than we earlier assumed (taking into account its demonstrated activity in financial support of Ukraine's resistance). Its parent group, SCM, indicates its determination to avoid any debt restructuring even for the assets that are performing worse than Metinvest.

Source: Bloomberg, Concorde Capital estimates

War update

War update: Ukraine gains success in Kharkiv, Kherson regions



Kharkiv region

On September 8-13, Ukraine made its most successful offensive since March 2022 managing to liberate most of the occupied part of Kharkiv region (see the yellow area). While Russians have concentrated its most capable troops to the south of Izyum, targeting Sloviansk area, Ukrainian forces found a weakness in the occupants' defense line to the north of Izyum. As a result, in five days the Ukrainian army reached the railway hub Kupiansk on the Oskil river. Under a threat of being encircled, Russian troops have left Izyum and the entire area between the rivers of Siversky Donets and Oskil, as well as "voluntarily" left the area north of Kharkiv city. Since then, Ukrainian army managed to develop its success to the east of the Oskil.

Donetsk region

The only apparent territorial losses for Ukraine in the last month were detected in Donetsk region, on the frontline between Donetsk and Lysychansk. Here, the invaders are still able to use their tactics of heavy artillery shelling to gain couple of square kilometers along the frontline.

After leaving most of their positions in Kharkiv region, most likely, Russians will concentrate even more efforts to "develop their success" in Donetsk region.

Kherson region

Since mid-August, Ukraine forces managed to destroy all the bridges supplying the occupants in the area west of Dnipro river near the city of Kherson. Being trapped in the western bank of the Dnipro, Russians have lost their initiative. The only question is when and with what losses (and with what damages to the infrastructure) will they leave this territory, including the city of Kherson (the only Ukraine's regional center that Russia has captured since February 2022).

Source: Ukraine's General Staff, Institute for the Study of War (ISW), media, Concorde Capital research

Ukraine’s counteroffensive: Effect on economy & business

Ukraine’s victory near Kharkiv will have important military effect, as it:

- Proves to the western partners that Ukraine is capable of liberating its territories once it receives western weapon and ammunition.
- In this way, it increases motivation of the western countries to supply new weapon to Ukraine, thus potentially making Ukrainian army more capable to implement new attacks.
- Decreases Russian occupants’ morale and therefore spoils the aggressor state’s plans to hire new motivated combatants, making new potential counter-attacks of the Ukrainian army more efficient.

Also, Ukrainian army was reportedly able to gain control over a village of Bilohorivka (near Lysychanks) in Luhansk region. Now Russia no more controls 100% of Luhansk region, which is an important political and psychological gain.

The main effect for economy is improvement of security situation near Kharkiv, Ukraine’s second-largest city. The city will be out of the reach of Russian short-range artillery. Using the experience of the city of Sumy (attacks on which have been decreased significantly since the Russians left the area around it in early April), we can assume that everyday shelling of Kharkiv will stop. If so, people will likely start returning to the city and business activity will gradually restore there.

Naftogaz: decrease of operation risk for gas production

As we described in the August 17 note, Naftogaz is developing large natural gas fields to the south of Kharkiv. With movement of the frontline to the east, about 11% of its gas-producing fields are no more under risk of artillery attacks, and about 3-4% are no more occupied (see also the map on slide 23). This improves security situation for many gas-producing assets of the company and improves its ability to produce more natural gas.

Kernel: liberation of all seed crushing plants

As we described in the August 17 note, two Kernel’s small seed crushing plants (14% of the company’s crushing capacity) are located on the recently liberated (yellow) area (see the map on slide 24). Liberation of the territories around Vovchanks and Prykolotne crushing plants is encouraging news, but condition of the plants’ assets is unclear at the moment. Also, it is unlikely that they will resume their operations soon, as their location is a likely target for the aggressor's artillery from the Russian territory. Some more encouraging news is that the leased Chuhuiv plant (6% of capacity, located south-east of Kharkiv) is no more in the zone of reach of the aggressor's short-range artillery.

DTEK Oil&Gas: some chance for restoring of new field’s development

The company has a prospective gas filed in the southern outskirts of Kharkiv, for which the security situation has been improved (see the map on slide 22).

Russia’s immediate response to counteroffensive: Infrastructure attacks

Russia responded to Ukraine’s military success with a terroristic attacks against Ukrainian infrastructure. Among the most remarkable missile attacks, there were:

- On September 11, damaged energy infrastructure of Kharkiv region, including Kharkiv’s Heat & Power Plant #5 (the biggest heat producer of the city). Attacked were also power transmission facilities near Zmiyivska Thermal Power Plant (TPP), the biggest power producer in Kharkiv region. As a result of the attacks, Kharkiv and the nearby regions had troubles with power supply.
- On September 14, water dam was damaged on the Inhulets river in Kryviy Rih (the native city of president Zelensky) causing flood in the city and water shortages. The attacks repeated on the next day there, as well as on water infrastructure upstream on the Inhulets in the neighboring Kirovohrad region.
- Attacks were also reported on Slovianska TPP in Donetsk region on Sept. 17 and Kryvorizka TPP of DTEK on Sept. 29.
- On September 19, missile strike of South-Ukrainian Nuclear Power Plant was reported, with explosions in about 300 m near nuclear reactors.

As we highlighted before, Ukraine’s energy infrastructure is among key targets of possible Russian attacks. Such attacks are especially dangerous ahead of the heating season, when shortages of heat and power can cause humanitarian crisis. Risk of such attacks is among the biggest threat that comes from the on-going Russian aggression.

To protect Ukraine’s critical infrastructure, its western partners will increase supply of air defense. However, no defense system can cover all the critical objects.

Therefore, other possible responses to such attacks are considered, which are more “understandable” to the terrorist state. In his article on September 7, Ukraine’s chief of army Valeriy Zaluzhny explicitly stated that Russia is attacking Ukrainian territory because it feels its impunity. The sole fact of supply to Ukraine of weapon that can target distant locations in Russia could change Russia’s war tactics. We expect the West will approve supplies of more powerful attacking equipment to Ukraine.

Russia's response to counteroffensive: Mobilization, "referenda" and nuclear threat

Having lost the initiative in Ukrainian warfare, the rashist government decided to raise its stakes in the offensive:

- On Sept. 21, Putin announced a "**partial mobilization**" in Russia to recruit at least 300k soldiers for the Ukrainian war (according to the defense minister, while the actual target could be 4x and up to 10x larger). This is a desperate move which the government was trying to avoid for many months, taking into account its low popularity among Russian citizens. At least, such a move implies Putin is not ready to give up.
  - On the one hand, an increase of Russian troops in Ukraine means the war will go on longer than Ukraine could have expected. And it will be definitely more bloody for both sides. At the same time, entering of poorly trained and ill-motivated troops won't change the strategic situation much, especially if Ukraine's western partners increase their supply of modern weapon.
  - On the other hand, such a desperate move will significantly decrease popularity of the war in Russia, as well as the government's popularity. It increases the chance for internal protests, especially in the regions distant from Moscow and those populated by non-Russian ethnic groups. In this way, it increases the probability of sooner collapse of the Russian empire. Catalysts for such collapse could be new victories of Ukrainian army which would lead to increase of mortality among Russians and thus deepen the internal crisis.

- On Sept. 20, Russia and its proxies in four occupied regions of Ukraine (Donetsk, Luhansk, Kherson and Zaporizhia) announced **"referenda" to join the regions to Russia**. The "votes," with pre-determined "results," were completed on Sept. 27. Russia is going to use their "results" to ground the regions' "joining" to Russia. With this move, Russia stops hiding its ultimate goal of the war: grab as much territories of Ukraine as it can.

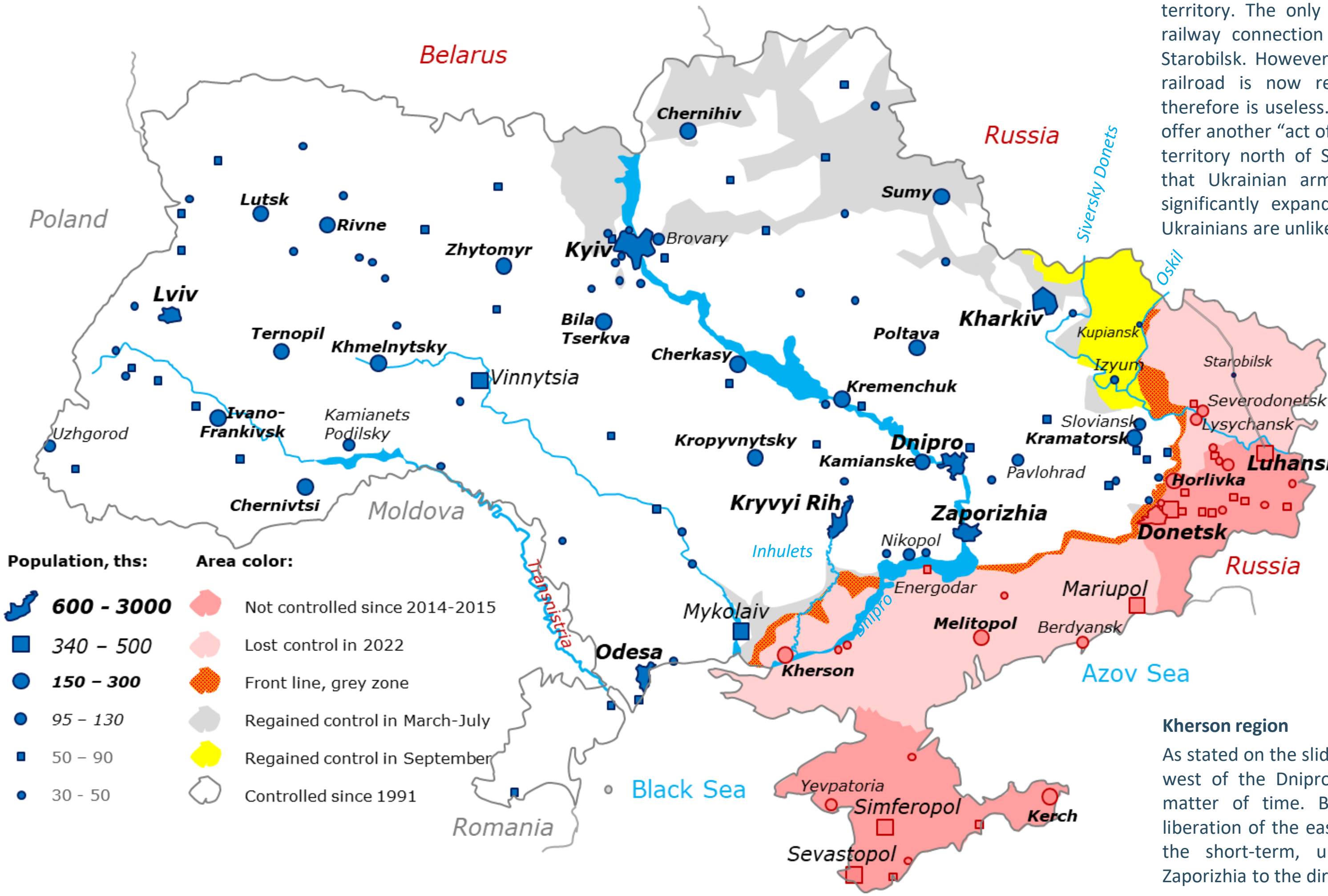
- With such a "joining," the "new territories" will become a "constitutional part" of Russia, and the Russian government threatens to protect them with "all available means," possibly including the **use of nuclear weapon**.

The Ukrainian side clearly stated that it won't accept such annexation, thus indicating its willingness to continue liberating the occupied territories.

For Russia, the annexation looks as risky as the mobilization:

- In case it continues losing the occupied territories of Ukraine (which it will be declared as part of Russia), its inability to "protect its new territories" will question its overall ability to hold any region within the empire. This, by itself, will question Russia's sustainability.
- In case it continues to threaten with nuclear weapon, it will turn the entire world against it, thus will totally isolate itself and will loose the war sooner.

That said, we see the recent desperate moves of Putin as too late to change the situation on the frontlines and rather risky for its statehood. Although it will allow Putin to postpone his defeat, it will make such defeat much more painful. Therefore, collapse of the Russian state becomes more likely and its timing looks less distant now.



Northern occupied area: no one’s land

As we stated before, there is little economic or strategic importance in the area to the east of the (yellow) liberated territory. The only military value for Russia here is the railway connection that goes through a small town of Starobilsk. However, with the liberation of Kupiansk, this railroad is now reachable by Ukrainian artillery, and therefore is useless. We do not rule out that Russians will offer another “act of good will” and move from most of the territory north of Severodonetsk-Luhansk line in a hope that Ukrainian army will acquire a new headache to significantly expand its front line there. In their turn, Ukrainians are unlikely to concentrate their forces there, except using some of the area to establish a bridgehead for attacking Severodonetsk, Lysychansk and Luhansk.

Lysychansk to Zaporizhia: Main battlefield

As Russians are likely to concentrate all their forces there (and so will the Ukrainian army), most of military activity of the next months will be on this line. The invaders will try to occupy the territory to the west of the Lysychansk-Donetsk line, while the Ukrainian army will likely try to liberate territories to the south from the Zaporizhia-Donetsk line.

Kherson region

As stated on the slide 4, liberation of the area to the north-west of the Dnipro (including the city of Kherson) is a matter of time. Beyond that, Ukrainian advance (i.e. liberation of the eastern bank of the Dnipro) is unlikely in the short-term, unless Ukrainian army attacks from Zaporizhia to the direction of Melitopol.

Source: Ukraine's General Staff, Institute for the Study of War (ISW), media, Concorde Capital research

Economy update

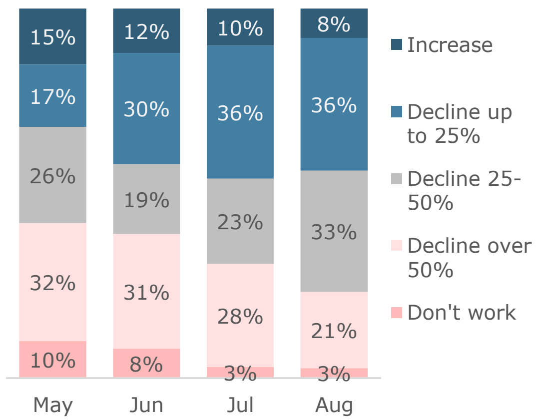
GDP performs slightly better than expected in 2Q22

Preliminary data for Ukraine's GDP in 2Q22, as stated by UkrStat, shows a 37.2% yoy decline. This is better than the National Bank (-39.3%) and the Economy Ministry (-40.6%) estimated.

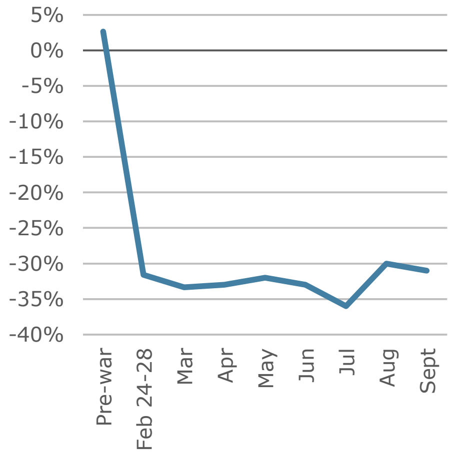
The trend allows us to confirm our estimate of a 31.0% decline of Ukraine's GDP in 2022 (vs. so far estimates of the NBU and Economy Ministry of a 32.4% and 33.2% decline, respectively).

We still expect the 2023 real GDP will increase by about 8% yoy (vs. the government's expectation of 4.6% growth and NBU's estimate of 5.5%), but the downside risks for such estimate have increased with the recent Russia's attempt to mobilize more people for the war.

Enterprises output since war start, IER survey*



Power generation in 2022, yoy



*Results of Monthly Enterprise Survey by IER (change vs. pre-war levels).
Source: NBU, DTEK, UkrStat, IER

Budget deficit: Likely to be covered by international support in 2023

After peaking at about USD 7.5 bln in June, Ukraine's budget gap decreased to about USD 4.1 bln in July and August. In September-December, the gap (the difference between own incomes of the budget and its all expenditures, including debt repayments) will be USD 18 bln (or USD 4.6 bln per month, on average), we estimate. This amount Ukraine is going to cover by:

- EU macro financial assistance and other programs - about USD 8 bln
- U.S. support for about USD 6 bln
- IMF support for about USD 1.4 bln
- Financing from the NBU for about USD 3 bln

Ukraine's drafted state budget for 2023 assumes a gap of UAH 1710 bln (USD 43 bln, assuming average exchange rate of 40 UAH/USD), implying monthly average gap of about USD 3.6 bln.

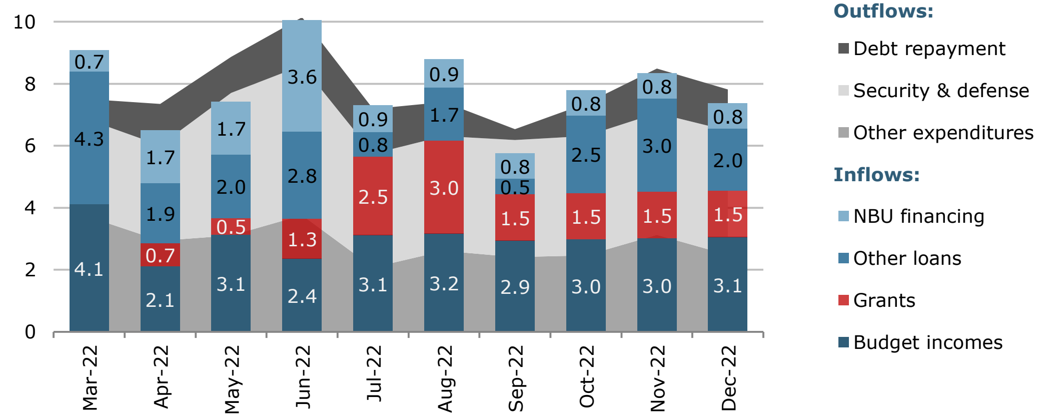
According to the Finance Ministry, such monthly gap is going to be covered by the support from:

- the U.S. (USD 1.5 bln per month),
- the EU (USD 0.4 bln per month, on average),
- the IMF (about USD 1.25 bln per month, on average).

If such support plan is realized (so far, there are no strong commitments to that, as we can see) Ukraine will secure coverage of most of its gap for the entire 2023.

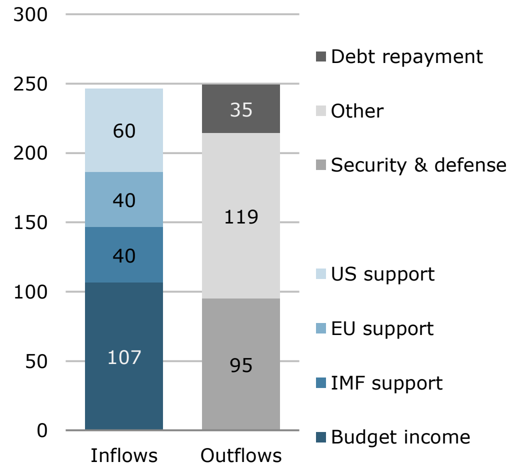
The draft budget assumes decline in monthly expenditures for security and defense to UAH 95 bln in 2023 (vs. about UAH 130 per month in summer 2022). As we do not expect significant de-escalation in the next year, such a reduction in costs does not look realistic, meaning the monthly budget gap will be as high as USD 4.5-4.8 bln in 2023. It looks like the government will be able to find additional international financing of the gap. Meanwhile, financial support from the NBU will always remain the option.

Budget inflows and outflows in 2022, USD bln



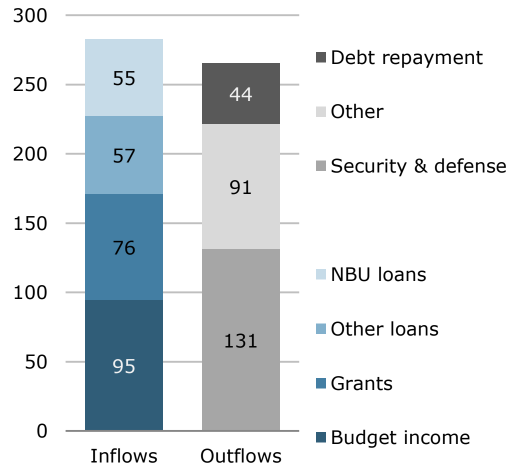
Drafted parameters for 2023 budget

Average UAH bln per month



Actual budget parameters for Jun-Aug 2022

Average UAH bln per month



Source: Finance Ministry, Cabinet of Ministers, Concorde Capital estimates

Increased financing gap of the state budget and worsened economy has led to increase of the ratio of the state debt to GDP to about 71% as of early September, from 43% at the start of 2022.

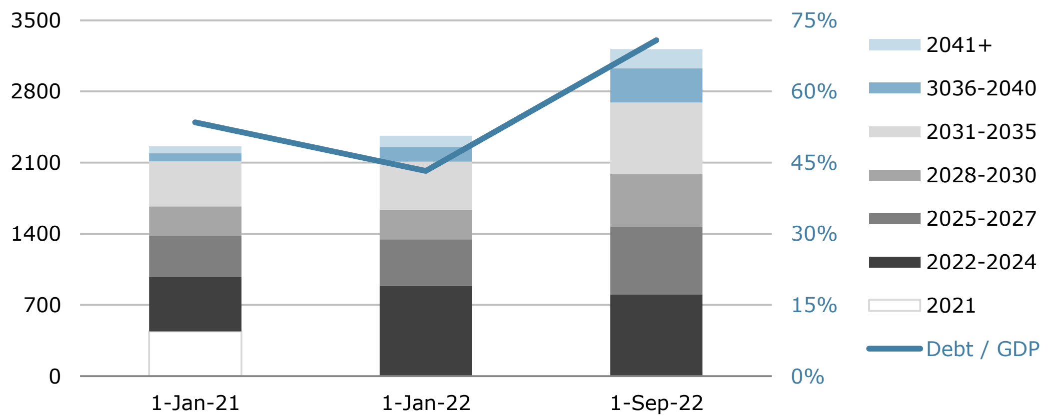
Good news is that most of debt attracted in 2022 is much longer than that attracted before:

- In the previous years, key source of debt financing were local bonds, vast majority of which were due in 1-2 years. However, since Russian invasion, MinFin preferred to issue long-term local bonds (with maturity from 11 to 30 years). Drawbacks of such policy are that the only buyer of such bonds is the National Bank (implying some additional inflation pressure) and that such bonds currently have much higher coupon rate (the rate is pegged to the NBU rate, which is 25% now) than the shorter "market" bonds (offering 12%-16% coupons).
- All the international debt attracted in 2022 is official debt with long maturity.

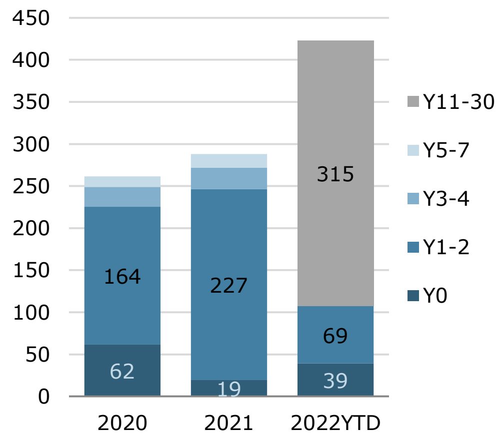
With attraction of longer debt, as well as with the recent restructuring of government's Eurobonds (2Y maturity extension) sustainability of Ukraine's debt has improved. Namely, despite an increase of Ukraine's state debt by 36% YTD as of beginning of September (in local currency terms), amount of debt that is due by 2027 have increased insignificantly.

Also, luckily for Ukraine's budget, it received USD 10 bln of support in the form of grants in 9M22 (with key contributor being the USA with its USD 8.5 bln). This is equivalent to about 7% of Ukraine's current GDP.

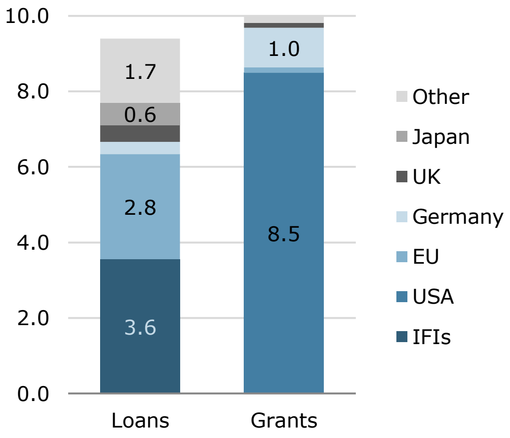
Development of maturity structure of state debt, UAH bln



Maturity of local debt raised, UAH bln



International support in 2022 YTD, USD bln



Source: Finance Ministry, Concorde Capital estimates

Trade balance: Grain corridor is improving result

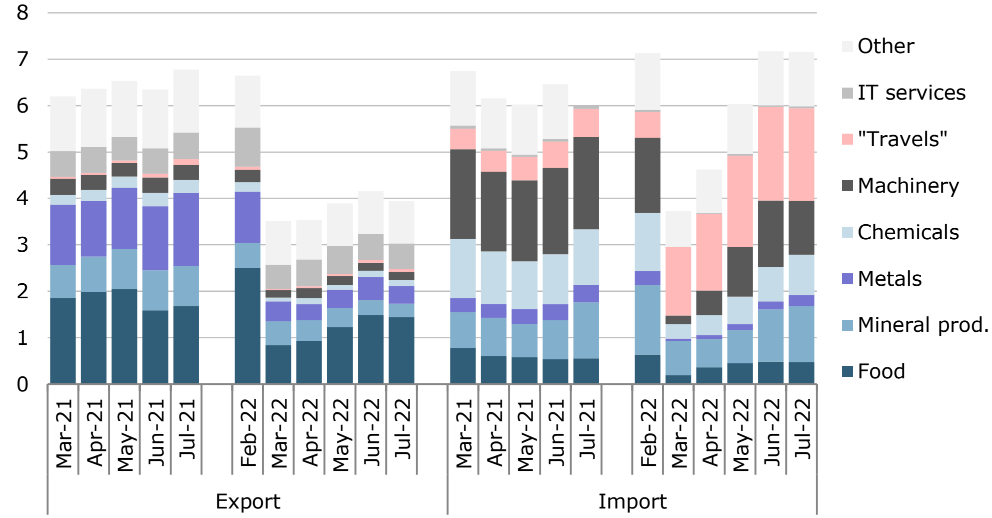
July's trade balance remained the same as in June, with food being a dominant export item, while import was driven by spending of Ukrainian temporary refugees.

On July 23, Turkey and the UN signed agreements with Ukraine and Russia forcing the latter to remove a blockade of some Ukrainian seaports for export of grains (the "grain corridor"). The corridor allowed Ukraine to more than double exports of crops and vegetable oils in August, as compared to June. Even more increase of food exports is expected in September. Therefore, food export will remain the dominant contributor of hard currency to Ukraine, at least in September-November.

The agreement on the grain corridor was signed for 120 days, meaning it will expire on about Nov. 20. Taking into account Putin's Sept. 7 negative remarks about the corridor's efficiency, we see the Russian side will try to close it ones the deal expires.

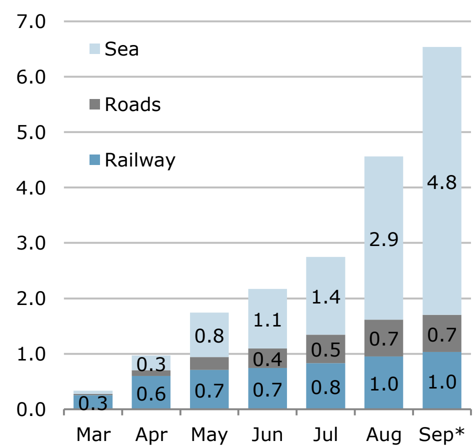
While Ukraine is actively developing alternative ways to supply grains to global market, they still cannot substitute the seaports.

External trade of goods and services, USD bln

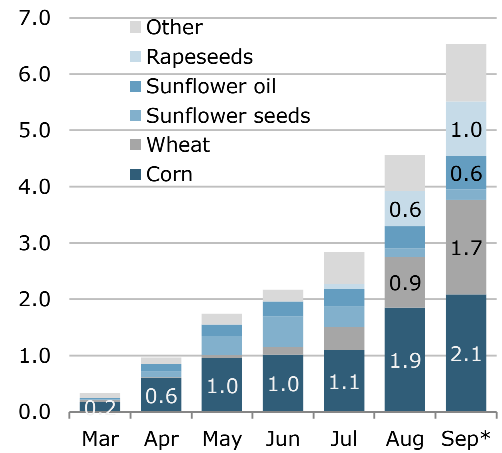


Crops and oils exports in 2022, mmt:

By routes:



By goods:



** Extrapolated data from Sept. 1-18*
Source: NBU, State Customs Service, Agriculture Ministry

Balance of payments: Western support allows to increase gross reserves in August

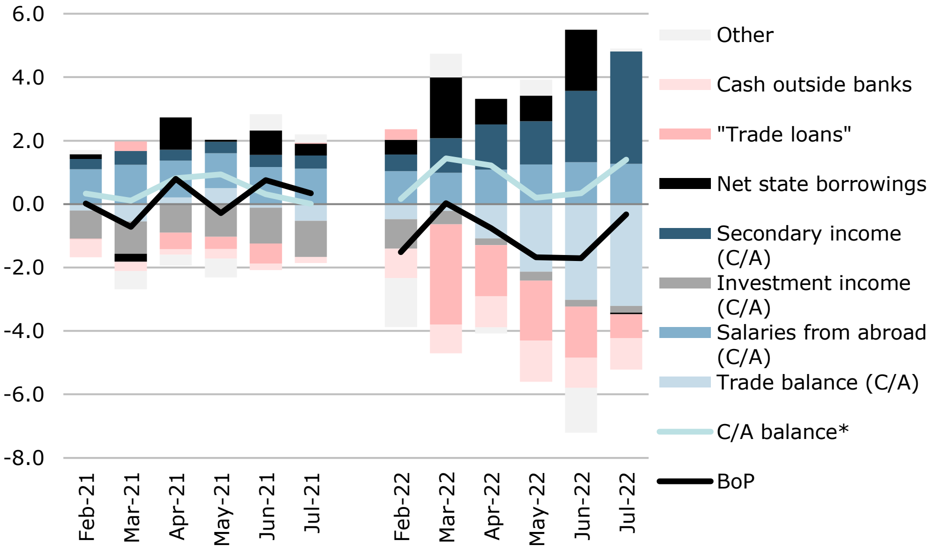
Deficit of Ukraine's balance of payments decreased in July as monetary support from western partners almost offset the hard currency outflows related to weak trade balance.

With the central banks' correction of fixed UAH/USD rate by 25% to 36.6x in late July, excess demand for foreign currency inside the country has noticeably decreased. In July-August, the NBU spent USD 1.2-1.3 bln for the support of fixed exchange rate, vs. 2.2-4.0 bln spending in the previous three months.

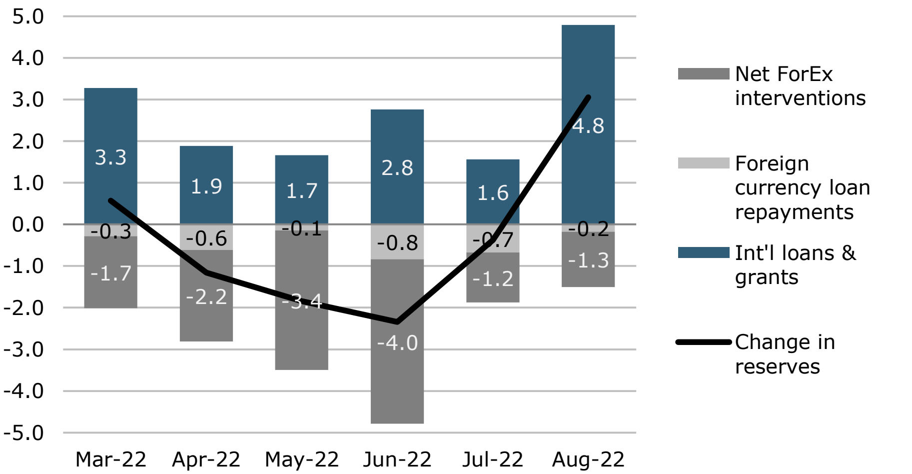
In August, the stabilization of demand for foreign currency, as well as increased international support for the nation (mainly due to USD 3 bln in the U.S. grant for Ukraine's Independence Day) allowed the National Bank to increase its gross international reserves for the first time since April. The reserves now stay at a comfortable level of four months of future imports.

We expect that in October-December, the NBU will be able to continue building up its gross reserves as international financial support will exceed the size on NBU's ForEx interventions. This will allow the NBU to keep the official UAH/USD rate at the fixed level of 36.6x at least by the end of 2022 (and probably for longer period), providing no new shocks happen.

Balance of payments, USD bln



Key factors of NBU reserves change, USD bln



** C/A balance adds back "reinvestment incomes" which the NBU subtracts in its reports since last year.*
Source: NBU, Concorde Capital estimates

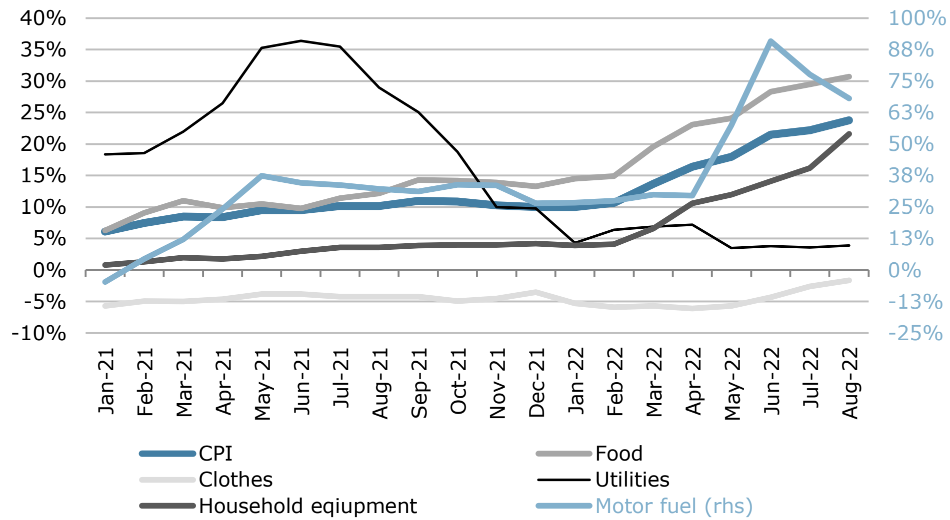
Annual CPI reached 23.8% in August (up from 22.2% in July), and the inflation is moving closer to the number forecasted by the NBU (31% in December).

While motor fuel inflation slowed down in August and inflation of utilities did not speed up, key drivers for increased CPI were household goods and food. Their prices increased mostly due to weakened UAH rate vs. key currencies in late July, which made prices for imported goods growing faster. Food prices, as well as expected speed up of inflation for clothes and footwear, will likely drive inflation further in September-October.

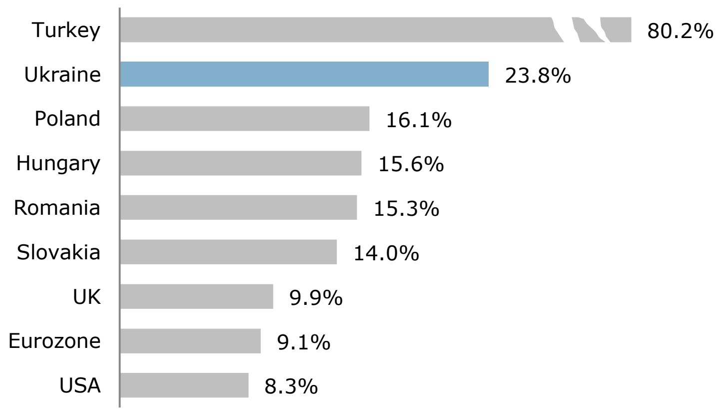
We expect the CPI will find its ceiling somewhere in October-November 2022. We estimate Ukraine's CPI will reach 28%-29% yoy as of December 2022.

The NBU's attempts to fight inflation with hiking its key rate to 25% in early June still has not led to broad increase of price of money in Ukraine. Placement rates of government 0.5-2Y bonds increased to 12%-16% in August-September, from 10%-11.5% in spring. MinFin decided to count on issue of long-term bonds for the NBU instead of issuing much shorter bonds for private holders. Meanwhile, banks do not hurry to raise their deposit rates too.

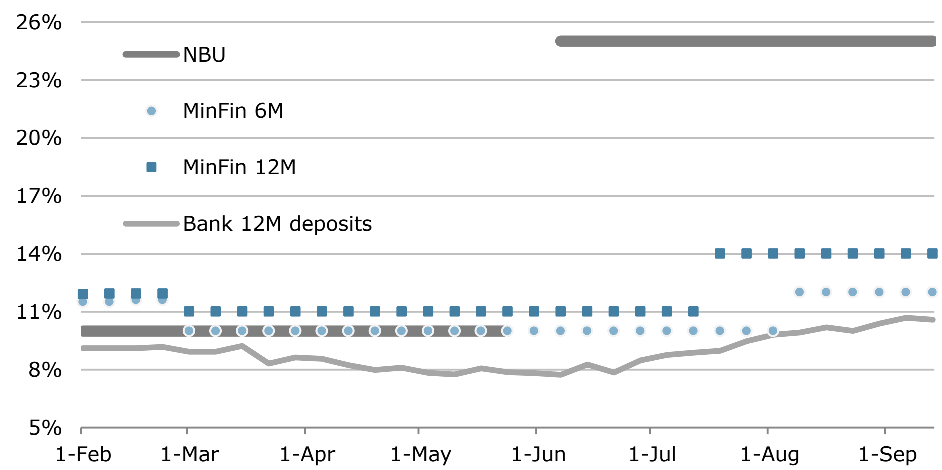
CPI and its selected components, yoy



CPI in August: Ukraine & its key partners



Interest rates, UAH



Source: NBU, UkrStat, Bloomberg

Eurobond Issuers Update

MHP: Poultry volumes restored, margin declines

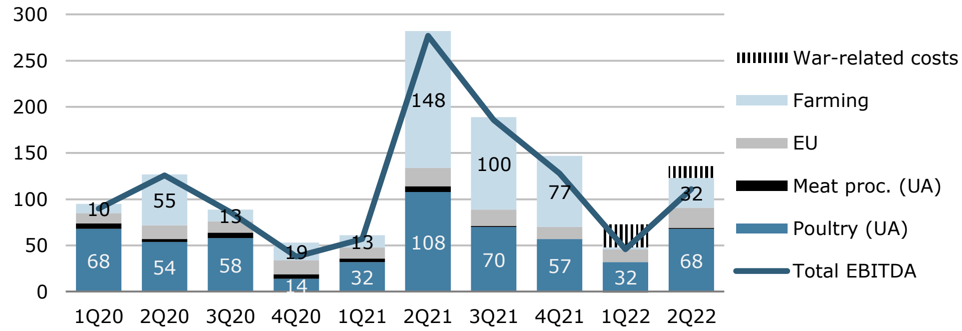
In 2Q22, MHP was able to generate USD 111 mln in EBITDA, which is not the worst result in its history, even though it looks poor compared to the booming year of 2021. The direct war–related expenses have eaten away USD 13 mln, or 10% of the result in 2Q22.

The company's volumes of poultry sales are increasing each month staring May:

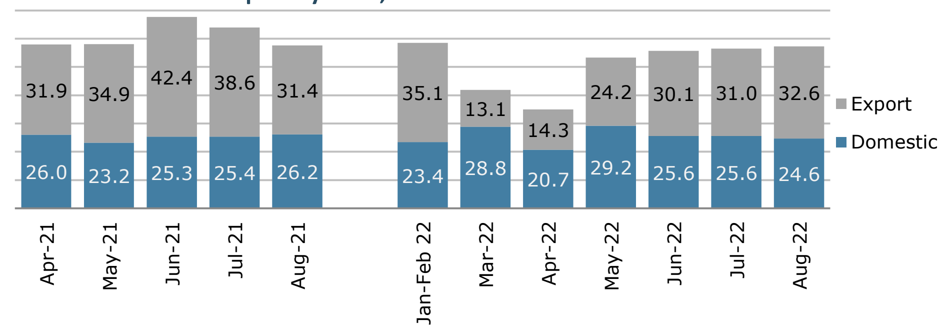
- Domestic sales of poultry meat were slightly higher yoy in May-July, which is a great achievement (though, some of the result can be explained by free humanitarian deliveries, which might have accounted for up to 11% of total poultry supplies in Ukraine).
- Its export supplies, after a shock of March-April (before the war, more than 2/3 of poultry meat was exported from Ukraine by sea) have been restored to about 3/4 of last year amounts in June-July and increased yoy in August. At the same time, costs of such supplies should have increased. Good news is that increased costs, as well as slow adjustment of domestic chicken prices, did not kill MHP's poultry segment EBITDA margin in 2Q22.

No doubt, MHP's P&L will worsen in 2022, as its key segments, farming and poultry, will perform weaker yoy. Nevertheless, the company remains fundamentally stronger than average Ukrainian business.

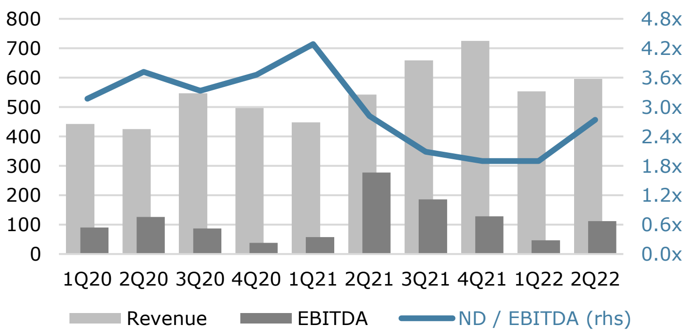
EBITDA structure, USD mln



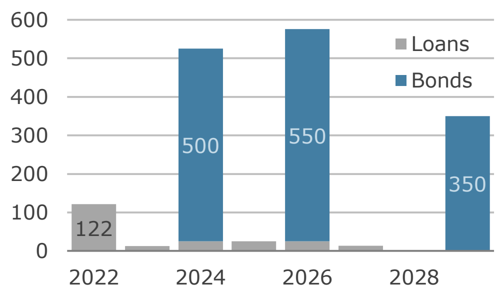
MHP's Ukraine-made poultry sales, kt



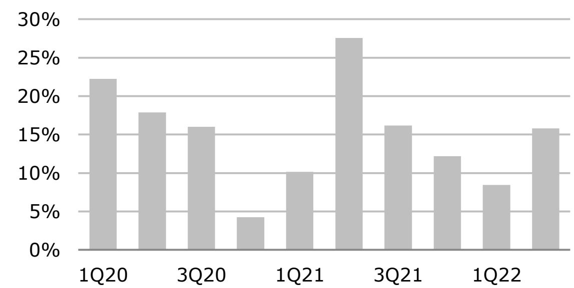
Selected financials, USD mln



Debt schedule (end-2021), USD mln



Poultry segment EBITDA margin



Source: Company data, Concorde Capital estimates

VF Ukraine: 2Q results are above expectations

The company's 2Q22 results turned to be better than we initially expected:

- While its mobile customer base decreased 10% qoq and 12% yoy (which is what we expected),
- Its revenue declined just 4% yoy as mobile ARPU was higher 2% yoy and qoq.
- Its EBITDA fell 1% yoy. Remarkably, its EBITDA margin increased to a record-high level of 60% in 2Q22.

In 1H22, the company reported an 1% yoy decline in revenue and a 2% increase in EBITDA, in USD terms (and better in local currency terms).

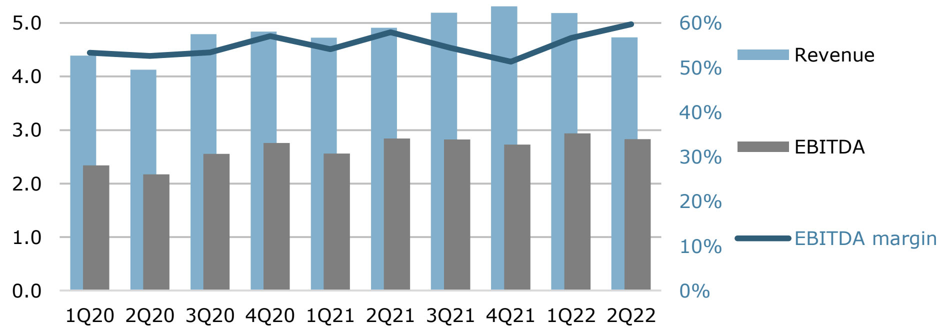
Clearly, the decreased customer base (with a further decline by up to 5% is likely by the end of the year) will worsen its 2H22 results, but not too much, taking into account that the company looks able to partially offset the decline in customer base with a better revenue per user.

With 1H22 results in hands, we upgrade our estimate of Vodafone revenue to USD 614 mln and EBITDA to USD 344 mln. This will be a decline of 17% and 14% yoy, respectively, with the biggest driver will be the weakened exchange rate of the hryvnia.

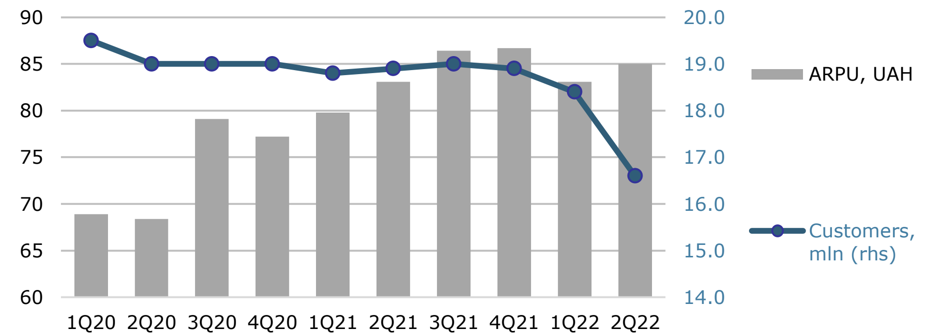
Meanwhile, we see the company's net debt to EBITDA ratio, which decreased to 1.0x as of end-June (from 1.2x at the year's start) will remain at about the same level by the end of 2022.

With such fundamentals, Vodafone-Ukraine is among fundamentally strongest companies in Ukraine's fixed income universe.

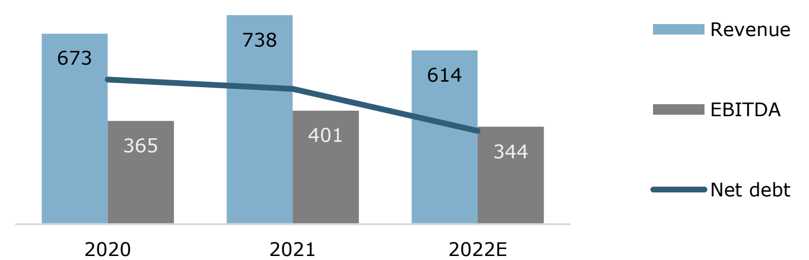
Selected financials, UAH bln



Key operating metrics



Financial outlook, USD mln



Source: Company data, Concorde Capital estimates

Akhmetov-related companies: Seem willing to service their bonds

Our general observation is - companies controlled by SCM holding of Rinat Akhmetov are doing all their best to continue smoothly servicing their Eurobonds. Even such a fundamentally distressed company as DTEK Renewables is doing so.

Perhaps this is related to a stressful experience of negotiations with creditors that Metinvest and DTEK Energy gained over their restructurings in 2017-2021. Also, the holding's owner might have expectations that the security situation in Ukraine will improve soon, within one year or so.

DTEK Renewables: Collections for electricity improved

On Sept. 15, the company asked bondholders to amend certain bond covenants and reiterated its intention to continue servicing its bonds. On top of that, it:

- Confirmed that all its wind power stations (located on occupied territories) are not operational. Wind stations account for 53% of its installed capacity and 70% of power generation potential.
- \+ Reported that its power output decreased 64% yoy in March-August, implying that its solar plants are working close to full capacity. This looks encouraging, taking into account that its solar assets are located in a zone of almost everyday shelling (see the map on slide 22).
- \+ Reported that the payment discipline of the sole buyer of renewable power, GarPok, increased from 17% in March-May to 25%, 33% and 50% in June, July and August. This is perhaps the most encouraging development for the company.
- \+ According to GarPok statistics, its payment level for the green energy increased from 46% in August to 66% (on average) in September, which allows to expect that settlement level to DTEK Renewables is growing further in September.

Meanwhile, its smallest generation asset, Tryfonivska Solar Plant, located between the Inhulets and Dnipro rivers, is now in the area of hot military actions.

We estimate that, if payment discipline of GarPok remains at 50% level in the rest of 2022, the company's cash revenue this year will reach EUR 50 mln. This, as well as EUR 95 mln in payment from GarPok that the company received in January will be enough to cover all this years' expenses, including OpEx (about EUR 15 mln), interests to non-related creditors (about EUR 35 mln), and debt repayments (EUR 62 mln). That means the company seems to be able to pay its bills from own cash flow this year.

Next year, the company won't generate enough cash to pay its bills, unless the situation on electricity market improves. With no improvements, DTEK Renewables will generate no more than EUR 3 mln from operations each month in 2023. That will be enough to pay interests, but not enough for debt repayments (EUR 46 mln due next year, according to the company's data as of June 2021). But if, in such situation, the company chooses to avoid debt restructuring, it still can do payments from its cash balance (which, according to S&P estimates, was about EUR 70 mln as of end-2021).

Metinvest: Increasing ore production, investing in Ukraine's victory

On Aug. 24, Metinvest reported that it has spend about UAH 1.9 bln (USD 60 mln) for aid to Ukrainian defense and society during the past six months. The company is unlikely to spend for such purposes its "last money," meaning our previous assumption that Metinvest was not generating cash is not valid.

That allows us to assume that the company's cash balance did not decrease from the last reported level of USD 483 mln in April, meaning Metinvest should have enough money to repay its nearest Eurobond (USD 176 mln) in April 2023. If so, **the company's nearest Eurobond, yielding currently over 150%, is a good (albeit risky) speculating opportunity.**

We expect to see more information about Metinvest's ability to go through the crisis in October, when its semi-annual accounts will be published.

The company also reported about a re-launch of iron ore production at Northern GOK in August to about 40% of the last year's level, meaning its total iron ore output increased to about 30% of the 2021 level in August-September, from about 13% in July.

DTEK Oil & Gas

The company provided no operating update, so we continue to assume its natural gas production remains flat yoy.

On Sept. 20, Ukraine's parliament approved a law changing the tax base for applying subsoil tax. Since August 2022, and while a ban on gas exports exists, the tax base will be internal gas price, not the average between imported price and "front month settlement price" at the TTF hub (the latter is about 2x higher than the domestic price now). If the bill is signed into law the decreased tax base will improve DTEK Oil & Gas EBITDA to over USD 500 mln this year (vs. about USD 150 mln in 2021).

DTEK Energy

No updates from the company.

Issuers ranking. The weakest continues servicing bonds

We continue to rank Ukrainian Eurobond issuers based on criteria offered in our August report, paying attention to the following:

- Apparent effect of the war on companies' cash-generating assets (whether they have been damaged, or located on the occupied territories, or very close to Russian border or the frontline. See also the maps on slides 22-24).
  - Among the recent changes here is a decline of share of risky Naftogaz assets (gas production assets that are either occupied or located close to the front line) from 17% to 3% due to the movement of the front line in Kharkiv region.
- Assessment of the sensitivity of companies' operations to the closure of seaports.
  - With emergence of grain convoys, this factor becomes less distressed for food companies Kernel and MHP.
- Rough estimate of companies' revenue change (in functional currency) as of now, as compared to pre-war levels.
  - We estimate some smaller than before revenue declines for MHP, Metinvest and DTEK Renewables.
- Existence of large debt repayments in 2022 and 2023 that can trigger default or require soon active talks with creditors on restructuring. No changes here.
- We add a new parameter to improve our ranking. This is estimated leverage multiplier (assessed EV/EBITDA in mid-2023) - an indicator of a company's ability to repay its debt in the mid-term, assuming no significant improvement in Ukraine happens.

Thus far, our conclusions remain unchanged :

- **DTEK Oil & Gas** and **VF Ukraine** are fundamentally strongest Eurobond issuers.
- **Naftogaz**, **Kernel**, **Interpipe** and **DTEK Energy** have same or more than the Ukrainian government fundamental reasons to ask for debt restructuring.
- **DTEK Renewables, Metinvest**, **DTEK Energy** and **Ukrainian Railways** are fundamentally weakest issuers.

Will behavior of the weakest issuers set the trend?

We are observing the implicit **willingness of fundamentally weakest issuer**, DTEK Renewables, **to continue servicing its Eurobond**. Other weak issuers (Metinvest, DTEK Energy) also do not indicate any intention to try restructuring their public debts.

Perhaps such behavior of fundamentally weak companies will set a trend on the market, so that other Eurobond issuers won't dare to approach the bondholders with their restructuring offers (or, the holders will demand high consent fees).

This is a contrast with our previous expectation that many issuers will try to offer debt restructuring as an alternative to refinancing (as the latter option is not available now, and there is no clarity when debt markets will be opened to Ukrainian companies).

Ranking of Eurobond issuers as compared to sovereign

	Assets under risk*	Output dependence on seaports	Revenue change since invasion	Sizeable debt due in 2022-2023	Est. 2023 leverage	Score, vs. sovereign
Ukraine	**15%**	**Medium**	**-35%**	**No**	n/m	=
Ukravtodor**	18%	No	n/m	No	n/m	=
Ukrenergo**	18%	No	n/m	No	n/m	=
Oschadbank	12%	No	n/m	No	n/m***	+2
Ukreximbank	16%	Low	n/m	No	n/m***	+2
Naftogaz	3%	No	n/m	Yes	>3x	=
Ukrainian Railways	25%	High	-45%	No	>5x	-4
DTEK Oil&Gas	0%	No	+	No	<1x	+5
VF Ukraine	12%	No	-10%	No	<2x	+3
MHP	2%	Medium	-5%	No	>3x	+1
Interpipe	13%	Medium	-45%	No	>3x	-2
Kernel	3%	High	-50%	Yes	>3x	-2
DTEK Energy	25%	No	-40%	No	>5x	-3
Metinvest	49%	High	-65%	Yes	>3x	-5
DTEK Renewables	100%	No	-78%	No	>5x	-6

While we do not rule out that any of the issuer can offer debt restructuring any time in the near future, we see that:

- The highest chance for restructuring offer has **Ukrainian Railways**, which is likely to follow other state-controlled corporates (Naftogaz, Ukravtodor, Ukrenergo).
- The lowest chances have **DTEK Oil & Gas**, **VF Ukraine** and two **state banks**.

** Estimated percentage of cash-generating assets that are either damaged, or located on the occupied territory, or located close to the frontline (Russian border).*
***There is no sense to consider Ukrenergo and Ukravtodor as separate entities, as their dependence on state budget is huge and their bonds are state-guaranteed.*
****The banks have enough foreign currency liquidity to repay their bonds . Source: Company data, UkrStat, NBU, Concorde Capital research*

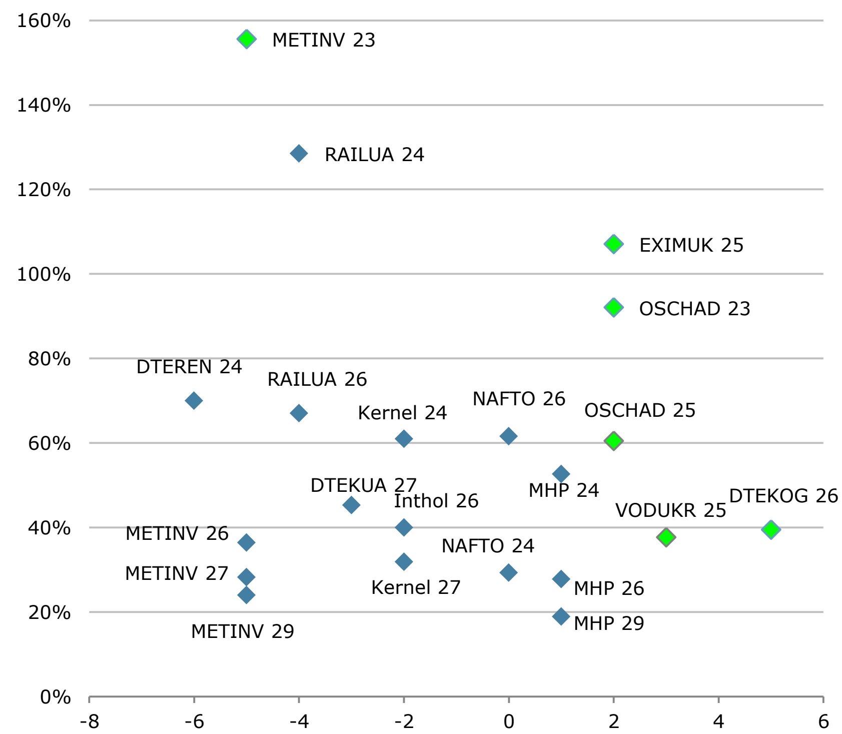
Corporate bond picking

To select our top picks, we are mapping bond yields against fundamental scores of their issuers, as derived on the previous slide.

Our top picks are:

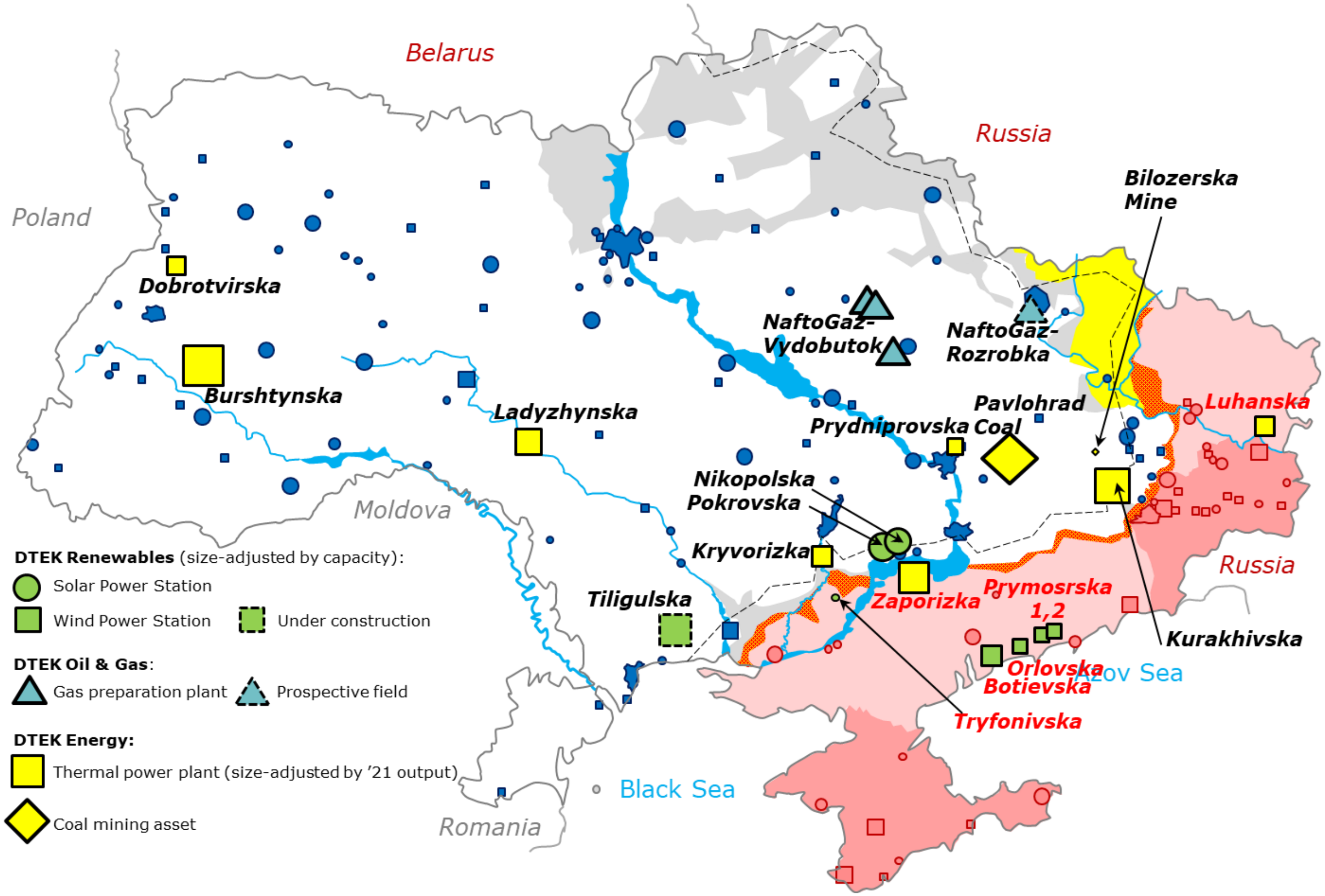
- Bonds of the issuers that offer a combination of high fundamental scores and high yields:
    - Ukreximbank 2025 (**EXIMUK 25**),
    - Oschadbank bonds (**OSCHAD 23, OSCHAD 25**)
    - DTEK Oil & Gas (**DTEKOG 26**)
    - VF Ukraine (**VODUKR 25**)
- Shortest bond of Metinvest (**METINV 23**) with a speculative expectation that it will be matured on schedule.

Fundamental scores and bond yields



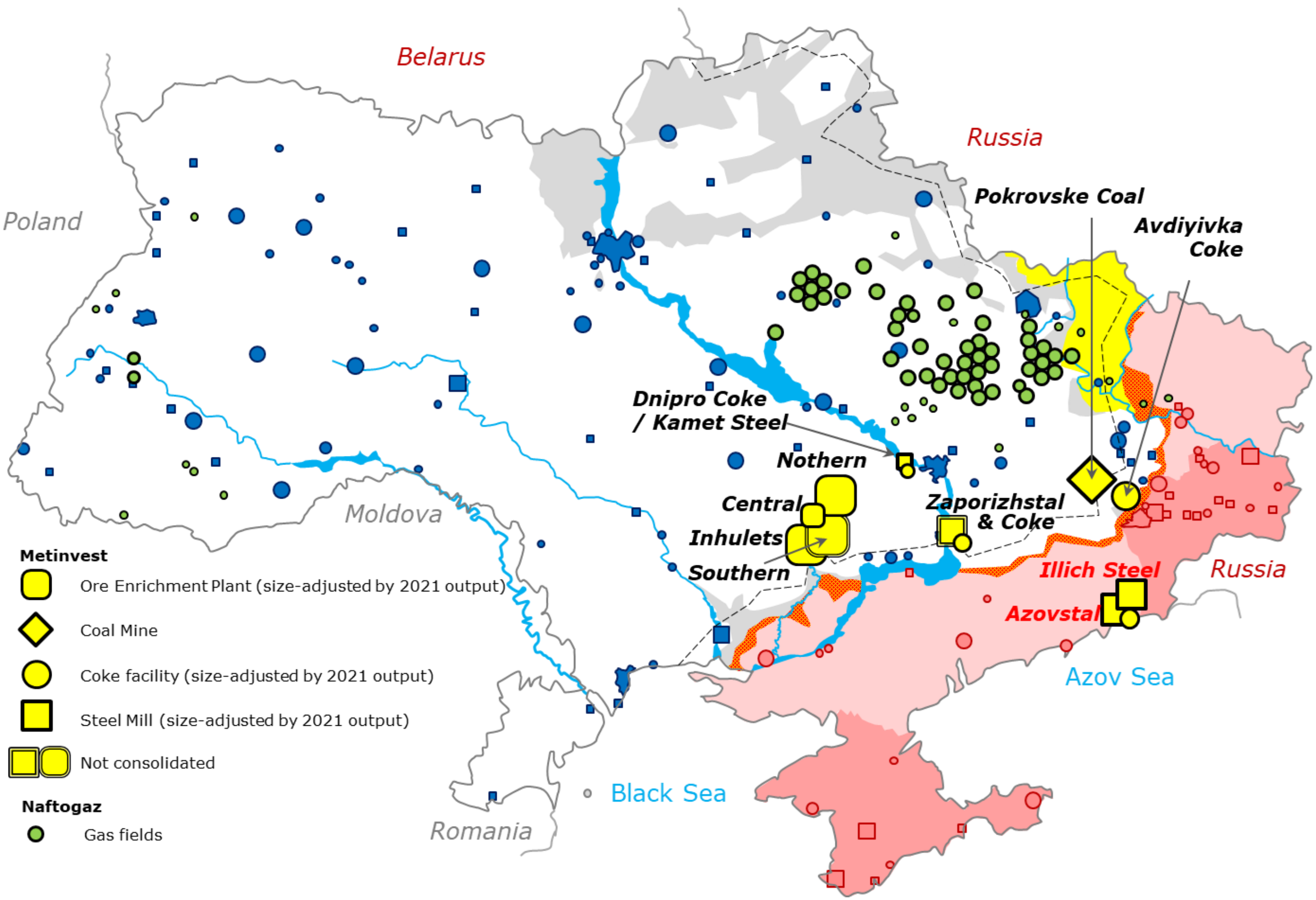
Source: Bloomberg, company data, Concorde Capital research

Key assets map: DTEK



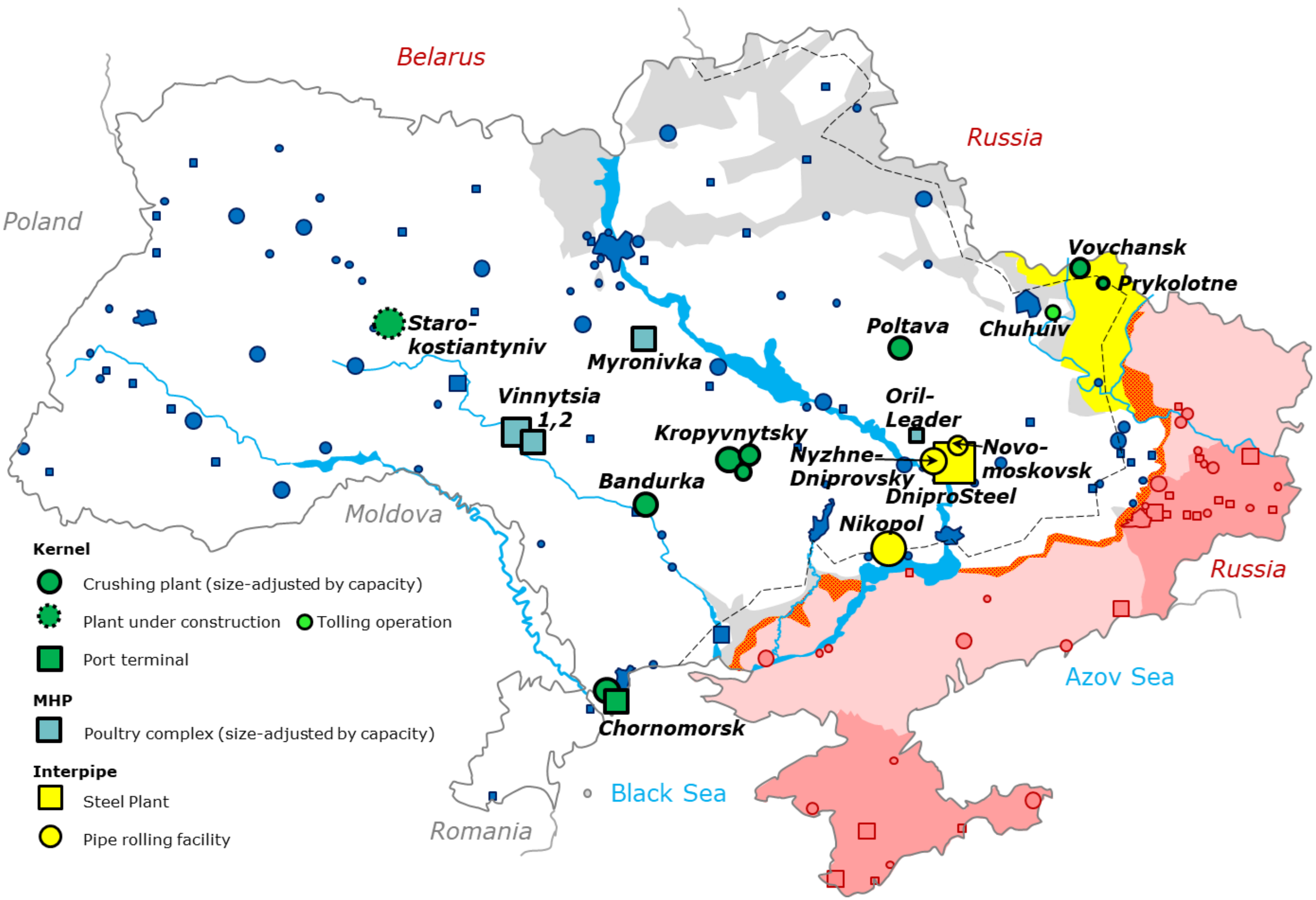
Source: Company data, Ukraine's General Staff, ISW, Concorde Capital research

Key assets map: Metinvest, Naftogaz



Source: Company data, Ukraine's General Staff, ISW, media, Concorde Capital research

Key assets map: Kernel, MHP, Interpipe



Source: Company data, Ukraine's General Staff, ISW, Concorde Capital research

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