Focus
Ukraine

Markets
Economics

Research team
Alexander Martynenko,
Taras Kotovych,
Mykhaylo Demkiv,
Dmytro Dyachenko

UkrFinForum-2018

On the eve of 2019 elections and IMF deal

THURSDAY, 27 SEPTEMBER 2018

ICU's 5th annual Ukrainian Financial Forum took place in Odesa on 20-21 September. As in previous years, world-famous speakers from politics, industry, and academia discussed Ukraine's achievements and pending reforms. However, this time, more attention was on the global macroeconomic situation, international trade issues, new trends in asset management and investment, and Ukraine's venture-capital landscape and startup potential. In many cases, Ukraine's 2019 elections and negotiations with the IMF dominated the discussion.

In the opinion of the keynote speakers, the conflict the US is embroiled in with its trade partners, in particular, China, is being used by the Trump administration for political purposes. However, China has the tools and policies in place to respond to the US and still maintain economic growth. Depending on how this conflict is resolved, there is the possibility of shifting the balance of power to Beijing. But, at the same time, possible disruptions in international trade can have a significant impact on other countries, including emerging markets and Ukraine.

Time and again, speakers gave credit to Ukraine's progress in achieving reforms, most of them delivered, remarkably, in the last four years, in contrast to the prior 20-year period. Yet, investors question if reforms will continue at this pace, particularly on the eve of presidential and parliamentary elections in 2019.

The panelists unanimously spoke of the necessity to cooperate with the IMF, as Ukraine remains heavily reliant on external borrowing. But, at the same time, Ukraine needs to focus on changes that will lead to stable money inflows from foreign direct investment (FDI).

One of ways to attract FDI is to put more emphasis on advertising stories of investors' success in Ukraine. More urgent than that, however, the government should take a more proactive role in creating investment opportunities, such as being more decisive about privatization. Several speakers indicated that a great deal of Ukraine's core assets remains under the control of the state and beyond the market's access. Also, speakers stressed the importance of the introduction of a land market, which alone could bring in at least $15-20bn of investments, and importance of reforms in the energy sector. Creating a predictable and transparent regulatory regime, developing a liquid stock market, and continuing pension reform were also named as key drivers that could deliver huge amounts of capital to the country.

Developing a local investor base is also important, and creation of attractive conditions for domestic banks and individuals in the domestic bond market can potentially bring an additional $20bn for private industry and the state. This year, NBU key rate hikes caused yields to rise, which added support for government bond demand. But to further strengthen the investor base, both corporate and government domestic bond markets should improve liquidity, support the secondary market, and insure transparency and credibility.

Ukraine's venture capital industry creates great opportunities for investors. This is particularly true for agritechnologies, cybersecurity, and blockchain infrastructure solutions. Founders of several Ukrainian top start-ups were on hand to tell their success stories to the Forum's audience. So, instead of the current zero support, the government should contribute to the IT sector by introducing tax incentives, creating fund of funds, and supporting tech education.

KEYNOTES SPEECH: US MONETARY POLICY

The US Fed should at least go slower in increasing rates to prevent another financial crisis

The key issue on everyone's mind is the state of the US economy. **Narayana Kocherlakota**, President of the Federal Reserve Bank of Minneapolis in 2009-2015, questions whether the US economy is as good as it seems. The longest bull market the US is still running, but it won't last forever. Kocherlakota believes the Fed should abstain from further rate hikes or at least go slower in increasing rates with an aim to preventing another financial crisis.

Recent reports from the Bureau of Labour Statistics indicate that the US has reached maximum employment, but Narayana is skeptical. During the previous recession of 2008-2009, record numbers of workers dropped out of the labour force, and they have started to come back. However, he believes the US economy will cross the line of maximum employment in 12 to 24 months. This will result in pressure on wage growth.

KEYNOTE PANEL: GLOBAL FINANCE AND THE WORLD ECONOMY: WHAT CAN UKRAINE EXPECT FROM THE TWO SUPERPOWERS?

Domestic politics motivate US authorities to put more pressure on China in the short term

According to **Narayana Kocherlakota**, the current trade conflict between the US and China is a containment policy in response to China's rapid economic growth. In the short term, he expects the US will continue to put pressure on China. More important, however, is if President Trump's vision of US foreign policy will extend beyond his presidency. Of particular concern is his aggressive use of trade tariffs, which can be construed as being used for domestic political purposes. Many observers are disappointed with this stance, and would like to see a more definitive response from the US's trading partners, and China could be the right one to take on this role.

The trade conflict has also changed the Chinese point of view on relations with the United States, says **Keyu Jin**, Associate Professor of Economics at London School of Economics. According to her, now every member of the Communist Party sees a threat coming from the United States. This strengthens the position of the left-wing element of the Communist Party, and creates an environment for increasing nationalism. As a way to strengthen its position in the conflict with the US, the Chinese government is fostering economic ties with EM economies, but this has political ramifications, especially with the smaller countries.

US-China trade conflict should be a secondary issue for both countries, which currently focus more on their internal economic situation

Nonetheless, both Kocherlakota and Jin consider the current trade war to be a second-order concern for both countries. The primary task for the US is to support economic growth through fiscal incentives, and by supporting its labour market. The Chinese government is now placing much more emphasis on financial stability and deleveraging the considerable debt in its system. The trade war doesn't have direct impact on its current goals, but it is one of the pressure points around which the government adjusts policy to maintain economic growth.

Panellists believe that Ukraine, as well as other small EM economies, will have to carefully watch the moves of the "two elephants in the china shop." Ukraine's government has to manage policy and business with an eye to the risks the policies of these two large economies can create.

PANEL 1: WILL POLITICS PREVENT PROGRESS? REFORMS IN AN ELECTION YEAR

While Ukraine's progress in reforms is significant, investors question its continuity, particularly on the eve of 2019 elections

From Ukraine's policymakers' point of view, significant progress has been made in reforms over the last four years. **Kateryna Rozhkova**, First Deputy Governor of the National Bank of Ukraine, considers macro-financial stability as the main achievement of the NBU. Moreover, introduction of inflation targeting and a floating exchange regime of the hryvnia enabled adoption of the Law on Currency, which gives huge opportunities to business. **Dmytro Shymkiv**, Former Deputy Head of the Presidential Administration and Secretary of the National Reforms and Investment Councils, recapped reform achievements that helped to attract foreign investment in Ukrainian projects, such as construction of a seed-processing plant by Monsanto, construction of ski plant by Head International, and construction of a grain sea-port terminal by Cargill. Both speakers emphasized that these reforms are permanent thanks to significant changes not only in the system of rules, but also in the business environment. But as **Lajos Bokros**, Professor at the CEU, and former Minister of Finance of Hungary indicated, the European experience shows many examples of what was thought at the time to be profound reforms that later reversed. Nevertheless, Lajos Bokros believes that the future of Ukraine is in the EU.

To achieve sustainable economic growth, Ukraine should secure the rule of law, speed up privatisation, and enhance productivity

Mr. Bokros stressed the critical importance of the following issues: 1) sustainable economic growth is impossible in a small economy like Ukraine without the rule of law, in particular the integrity of private property and the reliability of economic contracts; 2) more progress must be made with the privatisation of government assets; 3) due to the high level of labour emigration, in only a year or two, Ukraine may no longer be able to rely on an abundant domestic skilled and inexpensive labour force, hence, the country should promote productivity growth and pursue high-quality reforms in education.

To attract investment, Ukraine should put more effort into advertising its successful investment stories

From an investment standpoint, there is a huge difference between what potential investors read in the news, and what they see when actually visiting Ukraine. Press coverage of Ukraine tends to emphasise doom and gloom. The investor speakers subscribed to the view that Ukraine's progress remained under-advertised. The more successful stories become known, the more investors will come to Ukraine to explore opportunities. Particularly important is getting the word out about the expansion of current projects or additional investments by foreign companies already in the country, like SALIC's recent purchase of Mriya.

Ryad Yousuf, Managing Director of Goldman Sachs, opined that investors do not necessarily have to see the results of reforms immediately. But they definitely want to see the government acknowledge that more needs to be done. If a country is reliant on outside capital, it must fill investors' need for information.

Frank Heemskerk, Executive Director of the World Bank Group, is sure that Ukraine's glass is half-full. He gives the country a lot of credit for what it has accomplished in the last four years, particularly in contrast to prior decades. The question now is how this plays out in upcoming elections. Elections are never about the past, and always about the future, in his opinion.

The Ukrainian government plays a critical role in creating investment opportunities, such as more active privatization

Makar Paseniuk, Managing Partner of ICU, thinks that despite the progress achieved to date, Ukraine still needs to offer more opportunities to investors. The role of Ukraine's government in creating these opportunities is much more important than ever, and more important than it is in other countries. The private sector, with its heavy debt and high fragmentation, cannot secure a meaningful level of investment without government assistance. Paseniuk feels that the government should take a more proactive role in creating investment projects, because at the moment, it is hard to name a viable economic project where a private investor can put $1bn. The best example is the agriculture sector, which accounts for 15% of GDP. Lifting the moratorium on trading farm land may bring to market 10m ha of state-owned land. In just three years, this could attract $15–20bn of investment, an amount comparable with the IMF's latest EFF programme for Ukraine.

Paseniuk sees energy as the second important sector, with its 8% share in GDP and critical impact on the trade deficit of Ukraine. Ukraine's natural gas reserves of 600bcm are third largest in Europe. In order for Ukraine to become self-sufficient in natural gas, the country needs approximately $3bn of direct investments into gas exploration and production. As a result, Ukraine will save $2.5-3bn of import costs, which will dramatically reduce the current account deficit, most recently estimated at $3.5bn per year. The state has already made significant progress in the sector reforms by cutting rent taxes, deregulating the licensing process and introducing the framework of production sharing agreements. But the industry still needs market prices for gas for all consumers, transparent system of auctions for licenses and the whole regulation system modernized in accordance with the EU standards.

KEYNOTE SPEECH: UKRAINE'S ENERGY SYSTEM: REFORM PRIORITIES AND POLITICAL REALITIES

Edward Lucas, Senior Vice President at the Centre for European Policy Analysis, formerly a senior editor at the Economist, notes that Ukraine has demonstrated substantial progress despite considerable difficulties, including making significant progress in the energy sector.

Remaining one of the least efficient in Europe, Ukraine's energy sector could attract huge investment if it set up a predictable regulatory regime

However, the Ukrainian energy system remains one of the least efficient in Europe. With energy intensity of 0.318koe per dollar of GDP, it exceeds the European average by 2.2x. Back in 1989, Polish energy efficiency was about the same as Ukraine's currently, and Poland has now caught up and overtaken Sweden. Ukraine's incredible energy inefficiency implies that there is a big pool of money that could be freed up. Applying this energy inefficiency to the power of capital markets is one of the best ways to attract investment to Ukraine. All Ukraine needs is a predictable regulatory regime to bring this about.

To be successful with reforms, Ukraine's authorities must be diligent about transparency, accountability, and legality

An unavoidable issue with reform of the Ukrainian energy sector is that certain people have become very rich by extracting rent from the sector. This has caused considerable fury from the general public. So, when people hear the sector must undergo drastic change and raise prices, they assume someone is going to become rich on this. To be successful with reforms, authorities must be diligent about transparency, accountability, and legality because the reservoir of public trust is pretty much exhausted. One way to attack the oligarchs' dominance in the sector is to end the climate of impunity, so that diverting money, underinvesting, and outright stealing would involve serious consequences, including loss of licenses and prosecution. And the regulators must have really sharp teeth.

PANEL 2 A: UKRAINE'S ALTERNATIVE ENERGY EVOLUTION

Alternative energy is critical for Ukraine's energy independence

Panel speakers emphasized that alternative energy is critical for Ukraine's energy independence because it uses domestic sources: solar, wind, hydro- and biomass energy. Thus, it has the potential to improve the national balance of payments and boost employment. Although green energy currently comprises just 2% of the power generation mix, Ukraine plans to raise this share 11-12x to 25% by 2035.

Starting in 2009, Ukraine's legislators introduced so-called feed-in tariffs, which are pegged to the EUR and exceed even those of Germany, the highest feed-in green tariffs in EU. This makes this business highly attractive for both Ukrainian and foreign investors. While speakers admit that the current feed-in tariff level raises some questions, they noted that nuclear and hydro energy capex per MW will not be substantially lower than solar, wind, or biomass.

It is critically important to discuss with business the legislation package on electricity auctions currently registered in the Ukrainian parliament

However, tariffs will drop dramatically in 2020 after the introduction of the new electricity market in Ukraine, and the current investment sprint will likely fizzle out. According to **Marina Petrov,** Deputy Director in Ukraine EBRD, the number of investors planning to start projects in 2020–21 is very low. The market understands changes are inevitable, but the question is when, how, and what will be the tools to hedge risks. Hence, it is critically important to discuss with business the legislation package on electricity auctions currently registered in the Ukrainian parliament. And it is very important to formalize the law before year end to give investors vision.

PANEL 2 B: GOVERNMENT AS AN ACTIVE OWNER

Ukrainian state remains the key owner of some asset sectors despite the stated aim to privatize most SOEs

Twenty-seven years since the fall of communism, the state remains a key owner of some asset sectors in Ukraine despite the stated aim of privatising most state-owned enterprises (SOE). For example, the Ministry of Finance owns almost 60% of the banking sector. However, there is no single opinion on how much of SOE the government wants to keep and why.

Ivan Mikloš, Chairman of the Strategic Advisory Group for Supporting Ukrainian Reforms, argues that Ukraine should follow the path of his native Slovakia or Estonia and sell as much government property as possible. "There is no real reason why government has to own a bank. Everything should be private to increase efficiency. Government is never the best owner."

Government should step in to areas where the market fails to function due to costs that prevent profitability

However, **Andriy Pyshny**, CEO of state-owned Oschadbank, strongly believes government should step in to areas where the market fails to function due to costs that prevent profitability. “It is government’s role to provide services where people have no access to banking.” Yet, he is very skeptical of Ukrposhta’s aspiration for obtaining a banking license to expand financial services in villages. He believes Oschadbank should provide the services there, and Ukrposhta should work as an agent on a commission basis. In order to cut costs, Oschadbank will continue to downsize its branch network, predominantly those in small settlements with little business activity. **Kateryna Rozhkova**, First Deputy Governor of NBU, agrees that SOEs should have the goal congruence. Aggressive competition between them hurts the ultimate owner.

Pyshny is sceptical of the possibility to outsource all social functions to all market players and compensate them for losses. “Private banks do not go into the conflict zone in Donbass and provide services there in bullet-proof vehicles.”

Speaking of reform in corporate governance in SOEs, there remains a lot of scepticism among the authorities. **Şevki Acuner** Chairman of the Supervisory Board of Ukrzaliznytsia shocked the audience by his revelation. “For many members of parliament, corporate governance is like your 18-year-old daughter that you let go out, but expect to be home by 10 PM.”

The law on loan restructuring (Kyiv approach) has proved to be a success for Oschadbank. Its CEO stated that the bank has already restructured UAH10bn of NPLs. Another UAH12bn are in the works, and an additional UAH17bn are waiting for the process to start. However, state-owned banks cannot make haircuts due to legal limitations.

PANEL 3 A: BETTING ON THE FUTURE: ORGANIZED COMMODITY TRADING IN UKRAINE

Ukraine needs to create a set of clear rules, principles, and an enforcement mechanism, which will help the commodity market self-regulate

Ukraine is among the largest gas producers in Europe, producing 20bcm per year, and is among the three European countries with the biggest gas reserves, said **Roman Opimakh**, Executive Director of the Association of Gas Producers of Ukraine. In 1H18, growth in gas production was negligible, but the number of started wells in the private sector increased by 65% YoY. Considering that drilling a new well in Ukraine usually takes 6-12 months, he expects an increase in gas production in the near future, while by 2020, gas production should grow 35%. The gas sector requires significant investment, and the state should create favourable conditions for investors. Starting from 2018, the state cut tax rent rates by more than half for gas production from new wells and guaranteed tax rate stability through 2023. But regulatory policy needs higher transparency of licensing and mineral resource legislation harmonized according to EU standards.

Rostin Behnam, a representative of the US Commodity Futures Trading Commission, believes that Ukraine needs to create a set of clear rules, principles, and an enforcement mechanism that will help the market self-regulate. **Volodymyr Demchyshyn**, Partner of ICU, the former Minister of Energy and Coal Industry in Ukraine, emphasized that the government should continue to passively design rules for the energy sector without excessive interference. It should allow private businesses to take more initiative, which is critical for development of the sector.

PANEL 3 B: WHAT CAN HAPPEN IN A YEAR? A LOOK AHEAD FOR UKRAINE’S ECONOMY

Ukraine needs to focus on changes that will lead to higher stable reliance on FDI, rather than external borrowing

Panellists almost unanimously spoke of the necessity for cooperation with the IMF. The government still relies heavily on external borrowing to solve its current needs. But in the long run, it is necessary to focus on changes that will lead to stable money inflows from foreign direct investment. Ukraine has to concentrate on privatisation and land reform. A low level of FDI is evidence of some problems, and makes investors wonder if they want to be here.

Nevertheless, Ukraine has recently shown very good results, and the NBU's independence is high, which helps its struggle with inflation. It is easy to blame the NBU for high inflation, but it has made considerable progress developing mechanisms to increase competition that lead to better prices, which, in turn should result in lower inflation. The high level of dependence on foreign currency makes the economy very sensitive to the hryvnia exchange rate. The lack of derivatives for hedging risks creates a problem with attracting hryvnia-based resources, and, thereby, makes investments very risky. Launching derivatives could improve the situation on the local-currency bond market.

PANEL 4: UKRAINIAN PENSION REFORM IN LIGHT OF EUROPEAN PRACTICE

The main issue with the implementation of the second pillar remains trust in the financial sector and banks

The second pillar of the pension system is very important. Ukraine has yet to move to a full three-tier system, so this was the main idea propounded during the discussion. The experience of many countries suggests that there are three tasks to launch the second pillar: 1) diversification of risk, such that in the future, it will be less dependent on the labour market and deductions in a pay-as-you-go system, 2) development of the domestic capital market, and a large category of investors with long money like pension funds, and 3) educate people that pensions do not grow on trees, and they have to save now to get a pension later.

Ukraine should consider the experience of many countries that were forced to change their systems. Political risks have to be avoided, as well as balance created between the first and second pillars without abandoning the first pillar while developing the second.

It does not matter which of the existing concepts will be finally adopted, the main issue in the implementation of the second pillar remains trust. Trust in the financial sector, banks, and the like. And confidence that the system will not be changed as has happened in many other countries, with the money sent to the pay-as-you-go system. After all, political risk always remains high. It will take political will to take decisions on changing the pension system on the eve of elections, instead of postponing reform again.

KEYNOTE SPEECH: JEROME BOOTH

Emerging markets receive less attention than they should

Jerome Booth, Chairman of New Sparta Asset Management, and co-founder of Ashmore Group, believes we are relying too much on past results, and, therefore, are relatively blind to structural shifts that are underway. He expresses the idea that emerging markets receive less attention than they should. "The idea that the periphery has no impact on the core has been around for a long time, but it is changing." Two-thirds of the world's GDP come from EMs. For particular goods, such as base metals, most of the supply comes from those countries so it's the EMs that set prices.

"Passive investing is like driving a car with closed eyes. Both save you energy, but they're dangerous." Investors are simply following the indexes rather than identifying problems in a particular country.

Booth expressed a rather surprising idea that illiquid instruments have a significant advantage. In the wake of a crisis, investors run to safe heavens. And liquid instruments provide an excellent opportunity to do so, which drives their prices even further south.

PANEL 5 A: MISSED OPPORTUNITIES IN EMERGING MARKETS: KNOWN RISKS AND BETTER REWARDS

In the EM beauty contest for investors' money, Ukraine looks pretty good within its peer group

Mikhail Galkin, Credit Strategist at Goldman Sachs, says the bank's trading desk is very constructive for emerging markets as a source of investment opportunities. EMs currently pay excessive interest rates, and the longer this market inefficiency persists, the longer investors in EMs will receive excessive returns. Likening the competition for EM investors to a beauty contest, Galkin says Ukraine looks pretty good within its peer group. One issue that needs to be addressed over time is Ukraine's local investor base, which is fairly weak right now.

Oleksandr Lyubarev, Director, Corporate Finance and Treasury, Metinvest Group, subscribes to the view that the local bond market's role remains undervalued. He believes that the local bond market can potentially bring $20bn to Ukraine if the state creates attractive conditions for banks and individual investors.

To stand out in the crowd, Ukraine needs to prove its strength and opportunities over time

Yuriy Butsa, Government Commissioner for Public Debt Management, on the other hand, feels that in the EM beauty contest, it is very hard for Ukraine to stand out. Ukraine's progress in reforms, reducing inflation, and the independence of the central bank do not matter much to investors in EMs. One way to change this attitude over time is to prove Ukraine has enough opportunities to be worth more versus EM peers. But it is a long and tough job.

Privatization and reforms could bring huge amounts of capital to Ukraine

Jonathan Neill, partner of FPP Asset Management, thinks Ukraine is a frontier market for connoisseurs, so it would be unwise for an asset manager to speak about Ukraine first at the meeting with investors. However, the government is open to western capital, so privatisation of core assets, a liquid stock market, pension and land-market reforms would bring huge amounts of capital to Ukraine.

PANEL 5 B: TO SELL OR NOT TO SELL: HOW TO MOVE UKRAINIAN PRIVATISATION FROM THE CURRENT STANDSTILL?

Ukrainian privatization has been idle during the last four years despite all efforts

Ukrainian privatisation has been idle during the last four years despite all efforts. Acting Head of the State Property Fund of Ukraine **Vitaliy Trubarov** admitted there was only one real success story, Kryvorizhstal, back in 2005.

Vladyslav Rashkovan advocated for more radical steps arguing that there should be no list of SOEs ineligible for privatisation. "There is substantial risk this list will grow bigger as time passes." However, there is strong belief among authorities that particular entities—such as ecological, nuclear, and defence-sector companies—should remain state owned. Natural monopolies have obvious obstacles and risks if privatised. However, companies like Ukrzaliznytsia can be split to into two parts—"privatisable" and state owned. The privatisation of small entities valued at less than UAH250m (US$9m) are to be sold on electronic auctions, and they are easier to sell than large SOEs.

PANEL 6 A: BLOCKCHAIN: OPPORTUNITIES AND THREATS FOR CRYPTOCURRENCIES IN UKRAINE

Ukraine's market for cryptocurrencies remains largely unregulated

The trading volume of cryptocurrencies in Ukraine amounts to $1–2m a day. Over the past two years, companies with Ukrainian founders or teams have raised over US$100m at ICOs, per data from Better Regulation Delivery Office (BRDO). However, the market for cryptocurrencies remains unregulated. Ukrainian legislation is based on rules-based supervision, but **Maxim Libanov**, a member of the National Securities and Stock Market Commission (NSSMC), comments that regulation of such an innovative industry should be based on principles-based supervision, which will reduce the risks from fast-obsolete legislation.

To date, the NSSMC considers "cryptocurrencies" as a new type of intangible financial asset that is not a means of payment within the territory of Ukraine. Rather, it is a means of exchange, accounting, or preservation of property. From the NSSMC's point of view, regulating the operations of cryptocurrencies should take place only when exchanging cryptocurrencies for fiat money and vice versa as well as during ICOs, where transactions directly between cryptocurrencies are not subject to regulation. He also added that a "cryptohryvnia" project is in the development stage, and will be issued by the NBU.

PANEL 6 B: MEETING GLOBAL STANDARDS FOR CAPITAL-MARKET INFRASTRUCTURE AND THE TOOLS FOR DEVELOPING THE DOMESTIC MARKET

As Ukraine's capital market grows, infrastructure needs to be put in place for direct foreign investment

The Ukrainian capital market is not well developed by global standards, and the country has to learn from the experience of developed markets and gradually introduce changes. As the market evolves and grows, infrastructure needs to be put in place for direct foreign investment. Presently, the Ukrainian capital market is undergoing a period of tangible reform including the stock and bond market and the exchanges.

The Chinese Bohai Commodity Exchange (BOCE) has an interest in entering the Ukraine market to consolidate the exchanges. But most of the changes concern the government bond market. The panellists discussed changes in the primary market that would allow brokerage bids in the primary auctions, the reform of the national depositary, the introduction of nominees, and the like. In the spring, Clearstream is expected to enter the Ukrainian market, and open a link to the Ukrainian securities market. The experience that Clearstream has already gained in Armenia and Georgia can be applied in Ukraine.

Ukraine is moving towards improving and simplifying the infrastructure so that it can be accessed by foreign investors, bypassing domestic Ukrainian specifics

In addition, it is important to increase confidence in the National Depositary of Ukraine (NDU) and consolidate the accounting of all securities, including the transfer of T-bills and accounting from the NBU to the NDU. But the NBU will retain its significant role in oversight. Therefore, Ukraine is moving towards improving and simplifying the infrastructure so that it can be accessed by foreign investors, bypassing the domestic Ukrainian specifics.

Separately, they also drew attention to the fact that the law on the nominee holder is bilateral so it is now possible to confirm ownership of foreign securities in Ukraine. The NBU also has an account with Clearstream, and ownership of Ukrainian Eurobonds can be registered locally. So, the infrastructure has also been improved on this issue.

PANEL 7 A: A VIBRANT OPPORTUNITY: UKRAINE'S VENTURE CAPITAL INDUSTRY

Instead of zero support currently, the government should contribute to the IT sector by introducing tax incentives, creating fund of funds, supporting tech education, and providing incentives for foreign capital to come into the country

It is easier to start a company now anywhere else in the world with current infrastructure than it was in the Silicon Valley in 1999, according to **Vitaly M. Golomb**, Managing Director and Global Head of Principal Investments. The VC industry creates great opportunities. Research conducted by the Boston Consulting Group indicates that in 10 years, 75% of the Fortune 500 will be companies that haven't been started yet. In 2017, the value of venture capital deals in Ukraine reached US$259m, which is an almost three-fold increase compared with 2016. However, in searching for funds, Ukrainians are looking outside of the country.

The main task for VC funds is to create favourable conditions in Ukraine, which will stop the brain drain, believes **Roman Nikitov**, director of ICU. Among the top sectors for VC investing in Ukraine are agritechnologies, cybersecurity, and blockchain infrastructural solutions. In the next year or two in Ukraine, there will be five unicorns—a company with $1bn of market value—while in the whole of Europe, there were only 20 unicorns a year and a half ago. Ukraine is the only country in the world where the IT sector was built with zero government support. The government can contribute to the IT sector by introducing tax incentives, creating fund of funds, supporting tech education, and providing incentives for foreign capital to come into the country.

PANEL 7 B: OUTLOOK AND OPPORTUNITIES IN DOMESTIC SOVEREIGN AND CORPORATE BONDS

The market is getting deeper in terms of the number of investors, especially individuals

Sovereign bonds. The government bond market is actively developing. **Konstantin Stetsenko**, Managing Partner of ICU, pointed out that the market is getting deeper in terms of the number of investors, and over the past 12 months, the portfolios of individuals have grown sixfold, and will continue to grow at similar multiples, if not in dozens of multiples. Foreign investors' portfolios also rose over this period of time.

Investors receive significantly higher income from bonds compared with deposits, and this boosts the government bond market

This growth has been driven by the increase in rates that follow the NBU key rate, which currently exceeds 18% at a time when inflation is declining. At the same time, investors receive significantly higher income from bonds compared with deposits, and this is especially noticeable for FX-denominated T-bills. Simplifying the purchase of T-bills, including the possibility of purchasing bonds online through a mobile application, is expected to increase the investments of individuals in government bonds. For example, launching such a service, PrivatBank expects the migration of foreign currency deposits in FX-denominated government bonds in the amount of $1.5–2bn.

In addition to individuals and foreign investors, insurance companies are also increasing their investments in T-bills. The gradual change in terms and conditions that adhere to European norms contributes to the increase of their reserves and, consequently, investments in T-bills. After all, a significant part of the funds should be invested in low-risk assets, the main portion of which are T-bills.

The big problem is market disruptions, and we have to find solutions on how to consolidate information and build a yield curve

One of the problems, especially for foreign investors, is that T-bills are traded on several exchanges, often only over-the-counter. For the sake of transparency and confidence in the market, transactions should be consolidated, which would also facilitate calculating an accurate yield curve. The Bloomberg terminal already incorporates these technological solutions, which were presented to the participants of the discussion.

Primary dealers can play an important role in increasing transparency and trust by making markets, the beginnings of which were announced on Panel 6 B (see above). For them, there should be some preferences and obligations with sanctions for non-fulfilment. And the primary dealers themselves should be bidding on the Bloomberg system.

The corporate bond market faces the same issues as the government debt market: liquidity, secondary-market support, transparency, and credibility

Corporate bonds. The corporate bond market is closely linked to the government debt market. And here the same questions arise: market liquidity, secondary-market support, transparency, and credibility, the same as for government bonds. Most investors are banks, but this market needs to be expanded to include insurance companies and pension funds as well as foreign investors. It is also very important to restore interest in bonds issued by companies themselves, since the number of issues is very small. For better transparency and credibility, improvements in legislation and regulations, improvements in the issuance mechanism, introducing a simplified prospectus, and issuing procedures are ongoing.

As for investors, the interest of foreign investors was estimated at US$500m, and this may be a rather active interest. But in order to attract them, it is necessary to ensure market liquidity, sufficient volume of issues, and an active market.

At the same time, confidence in the issuer is important for domestic investors, in particular insurance companies. Currently, they are interested in bank bonds, followed by quasi-sovereign issues, and only then companies.

PANEL 8: THE SECRETS OF MY SUCCESS: UKRAINE'S TOP START-UPS IN THEIR OWN WORDS

Ukraine is one the world's best places to start a technology company thanks to a wide range of low-cost, highly educated specialists, and a generation of young people who want to prove themselves

A group of young Ukrainian entrepreneurs who run the most successful Ukrainian start-up companies came to the Ukrainian Financial Forum to share the stories of their success.

Yaroslav Azhniuk presents Petcube, a company that invented cameras for playing and communicating with pets. Yaroslav Aznhniuk is sure that Ukraine is one the world's best places to start a technology company thanks to a wide range of low-cost, highly educated specialists, and a generation of young people who want to prove themselves.

Oleg Naumenko is one of the cofounders of Pocketbook. The original idea to create a universal e-book able to read all formats proved very successful, and Oleg sold his stake in Pocketbook at the high-growth stage. Today, he and his team run Hideez, and have developed a strong security solution for physical and digital identity for the financial sectorб legal companies, and other sectors.

Hacken, founded by **Dmitriy Budorin**, is a company engaged in cybersecurity consulting and fraud investigation. The concept of distributed responsibility allows Hacken to gather the best talents throughout Ukraine. Hacken's services are in high demand and have a quite diversified sales geography.

Oleksandr Starovit runs Kwambio, which invented the technology of 3D printing of ceramics including human skeleton parts designed for implants. Oleksandr thinks that in the near future, everyone will have accounts that included a scan of their skeletons. And Kwambio will be ready to offer a 3D print-out to replace a damaged bone.

Andriy Sevriukov presented AGRIEYE, the company that offers revolutionary technology to the agri sector. AGRIEUE uses such technologies as DL technology, application programming interface connectivity, and artificial intelligence. Currently, AGRIEYE is monitoring more than 2m ha around the world using satellites.

11th floor, LEONARDO Business Centre
19-21 Bogdan Khmelnytsky Street
Kyiv, 01030 Ukraine
Phone/Fax +38 044 3777040

WEB www.icu.ua

INVESTMENT ADVISORY

Makar Paseniuk, CFA, Managing Partner
makar.paseniuk@icu.ua

Roman Nikitov, ACCA Director
roman.nikitov@icu.ua

Ruslan Kilmukhametov, Director
ruslan.kilmukhametov@icu.ua

Ivan Shvydanenko, Director
ivan.shvydanenko@icu.ua

Yuriy Kamarytskyi, Vice President
yuriy.kamarytskyi@icu.ua

Ruslan Patlavsky, Director
ruslan.patlavsky@icu.ua

ASSET MANAGEMENT

Grigoriy Ovcharenko, Director
Head of Local Asset Management
grigoriy.ovcharenko@icu.ua

Liliya Kubytovych
Head of Marketing and Sales
liliya.kubytovych@icu.ua

TRADE OPERATIONS

Konstantin Stetsenko
Managing Partner
konstantin.stetsenko@icu.ua

Sergiy Byelyayev
Head of Fixed-Income Trading
sergiy.byelyayev@icu.ua

Vitaliy Sivach
Trader, Fixed-Income & Forex
vitaliy.sivach@icu.ua

Vlad Sinani, Director
Strategy and Business Development
vlad.sinani@icu.ua

Yevgeniya Gryshchenko
Head of Brokerage Services Department
yevgeniya.gryshchenko@icu.ua

Bogdan Vorotilin
bogdan.vorotilin@icu.ua

RESEARCH

Alexander Valchyshen
Head of Research
alexander.valchyshen@icu.ua

Alexander Martynenko
Head of corporate research
alexander.martynenko@icu.ua

Dmitriy Dyachenko
Junior financial analyst
dmitriy.dyachenko@icu.ua

Taras Kotovych
Senior financial analyst (Sovereign debt)
taras.kotovych@icu.ua

Mykhaylo Demkiv
Financial analyst (Banks)
mykhaylo.demkiv@icu.ua

Artem Gladchenko
Junior financial analyst
artem.gladchenko@icu.ua

Investment Capital Ukraine LLC is regulated by Securities and Stock Market State Commission of Ukraine (license numbers: dealer activity AE 263019, broker activity AE 263018, underwriting activity AE 263020 dated 11 April 2013).

DISCLAIMER

Additional information is available upon request.