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Serbia Government Bonds Overview

IV Cbonds Poland & CEE Bond Conference

15th October 2015, Warsaw Poland

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Managing Director

Serbia, like most sovereigns in the region, issues bonds in a number of denominations:



The USD denominated bonds are traded OTC and settled via Euroclear.

Most liquid of the three and have the tightest bid/ask spreads.

They are also the most volatile.



The €uro denominated bonds are traded and cleared locally via the central clearing registry in Belgrade.

They are less liquid and more costly to trade actively.

But much less volatile



The RSD denominated bonds are traded and cleared locally via the central clearing registry in Belgrade.

They are fairly liquid due to high percent of local participants (banks and insurance companies) and recently uptick with foreign interest.

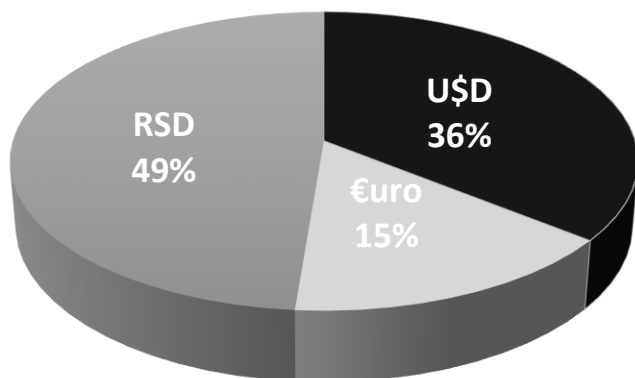
Carry FX risk but can be offset via FX swaps



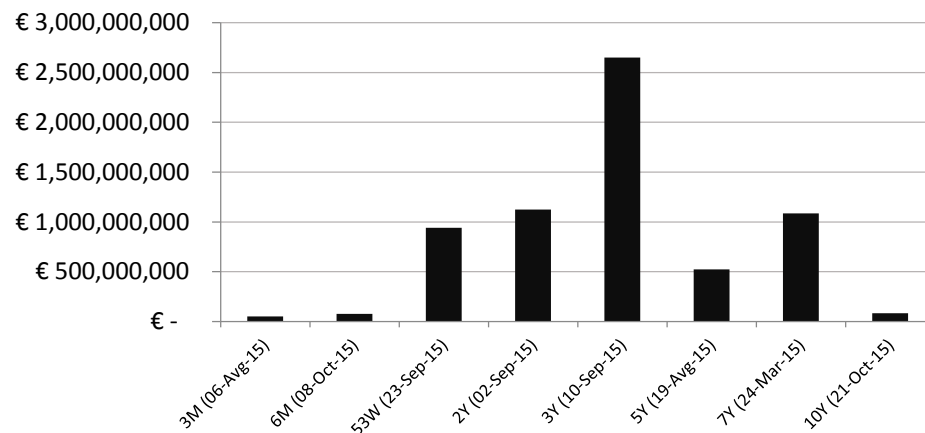
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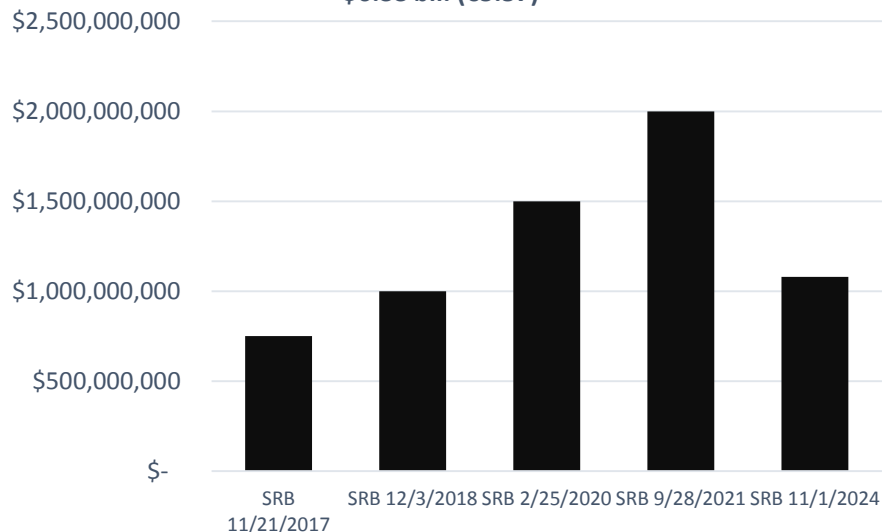
€15bil. of maturities outstanding



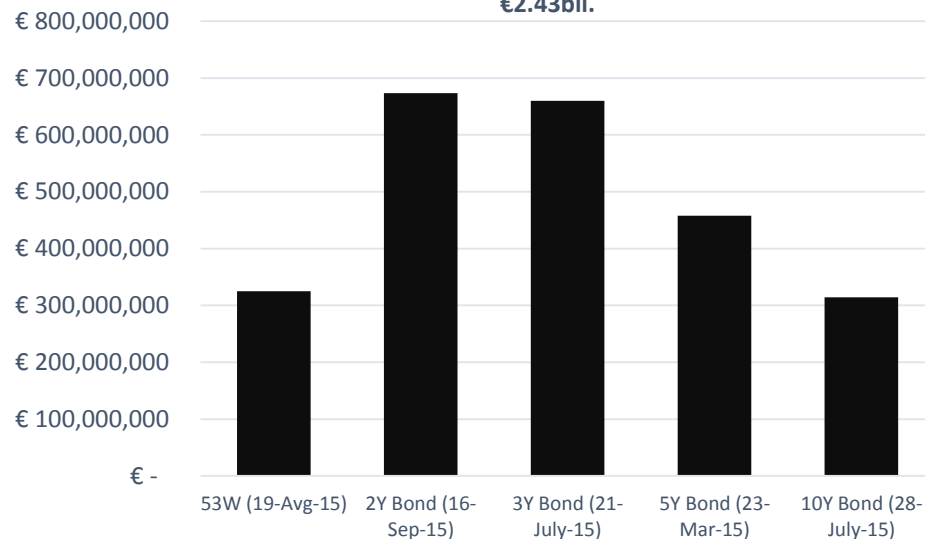
Outstanding Maturities - RSD Bonds in (€uro) €6.5 Bil.



**Outstanding Maturities U\$D Bonds
\$6.33 bil. (€5.57)**



**Outstanding Maturities - €uro Bonds
€2.43bil.**

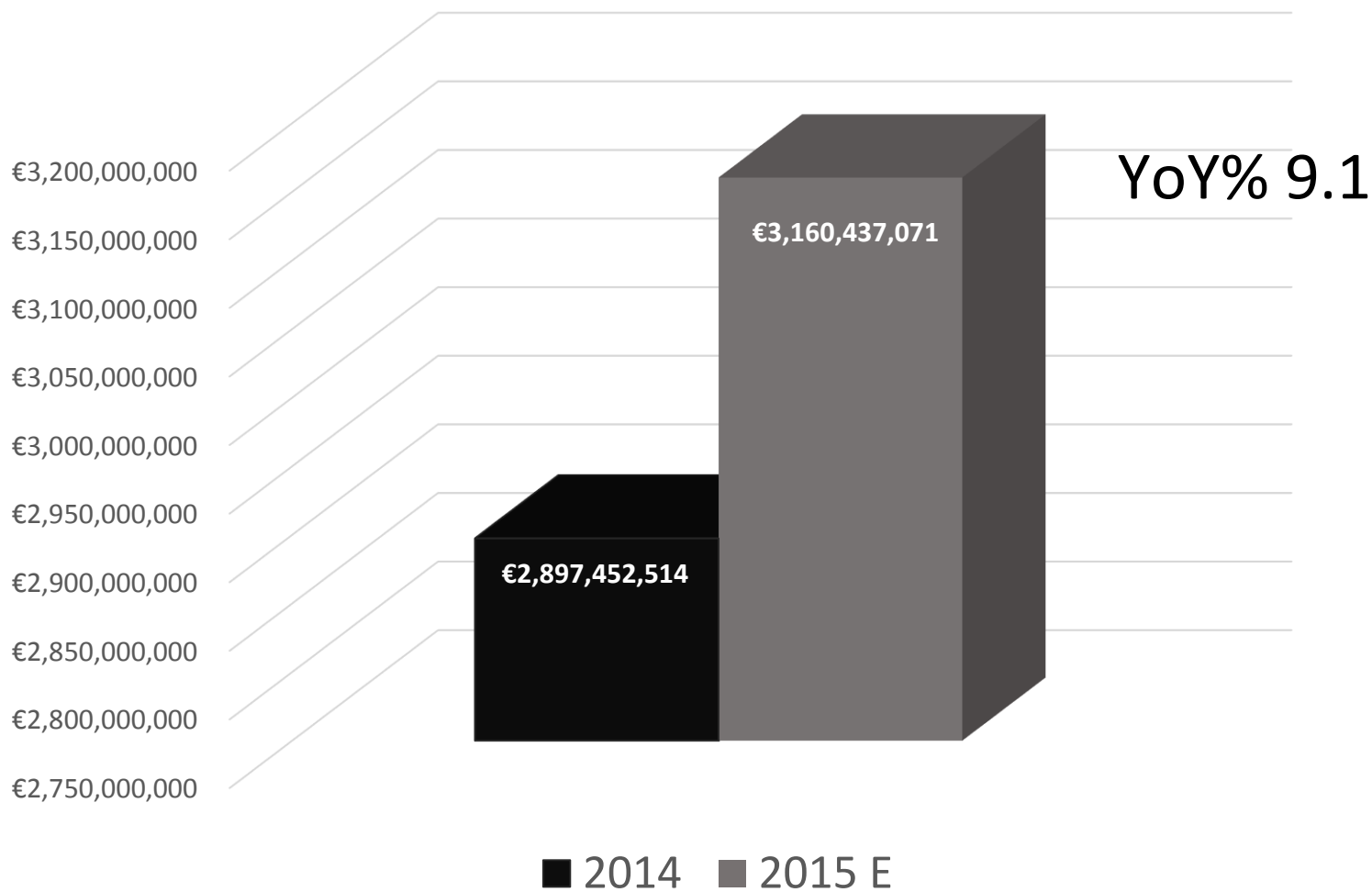




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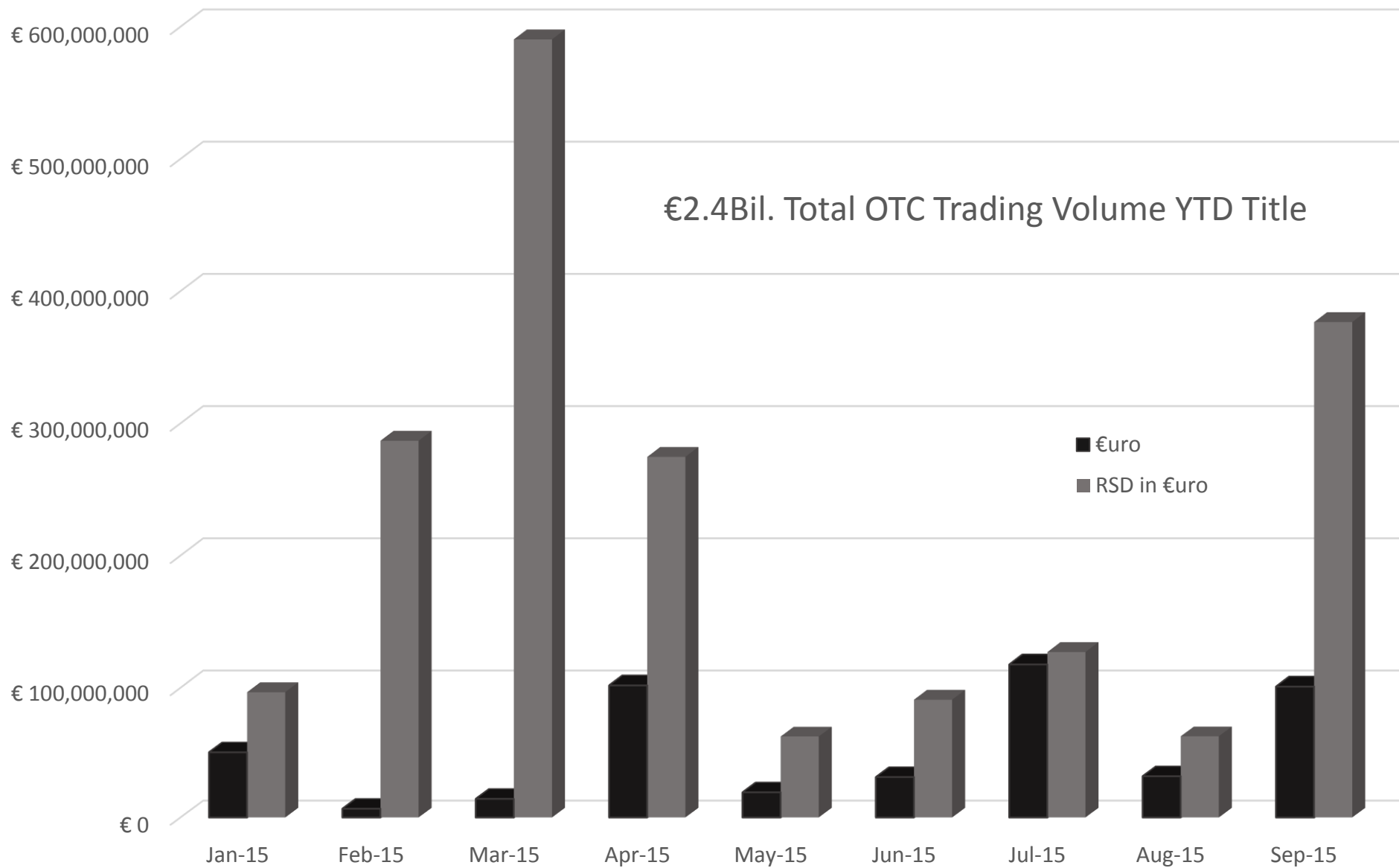
Total OTC Trading Volume





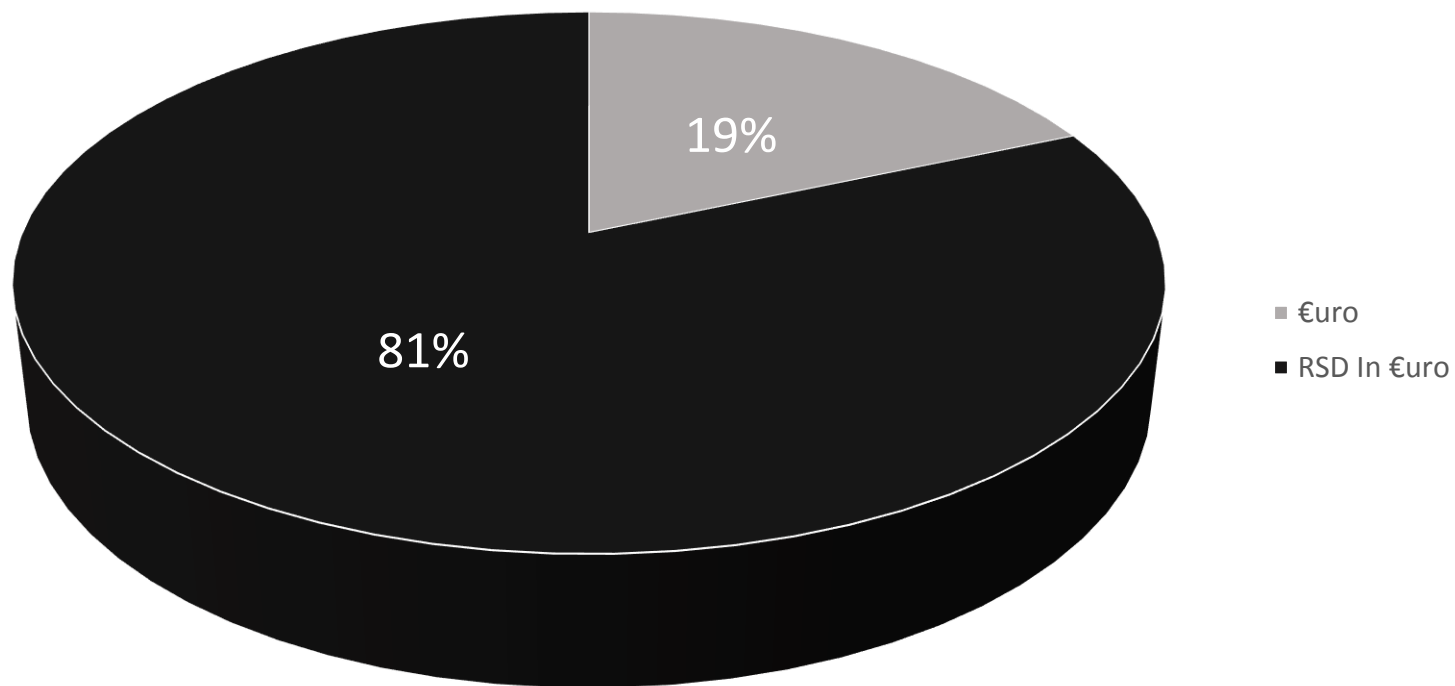
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€2.4Bil. Total OTC Trading Volume YTD



Currently RSD and Euro bonds are traded and cleared on the local OTC market.

Volume and Liquidity and thus foreign investors have been held back due to

Non transparent pricing
wide bid/ask spreads
High cost of transaction
Slow turnaround time with the central clearing registry. (can effectively clear only one trade per day)

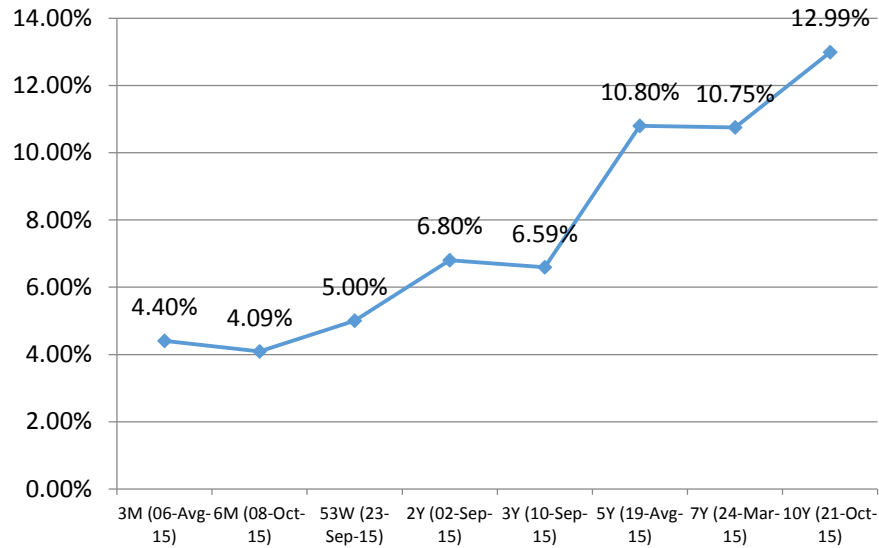
This will hopefully change in November when Bonds start trading over the Belgrade stock exchange.



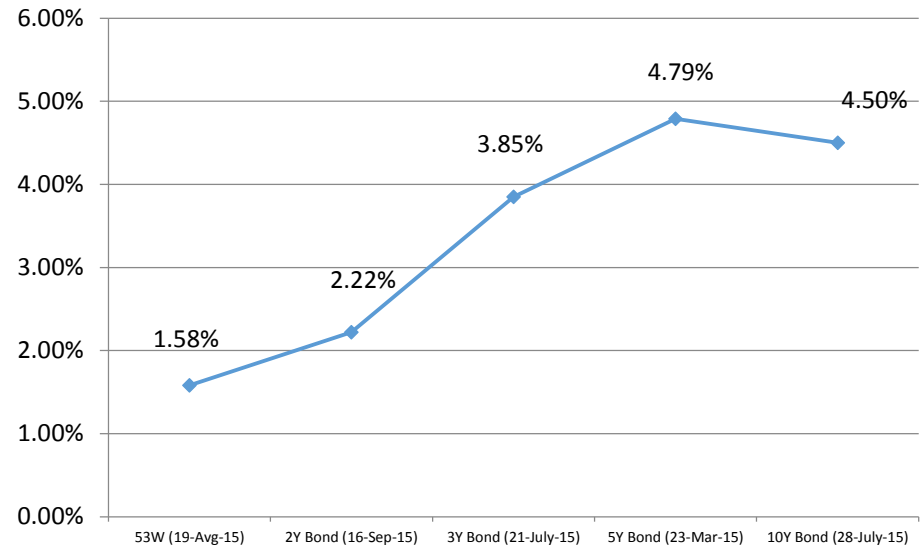
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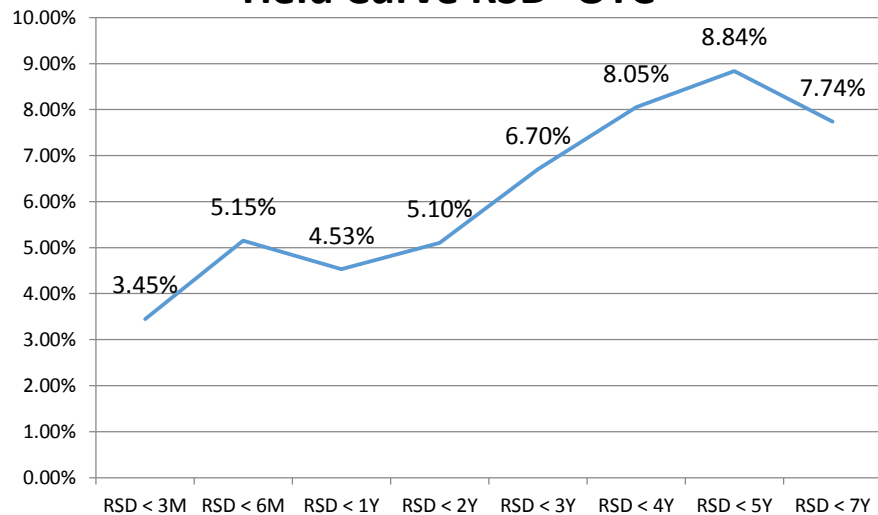
Yield curve RSD



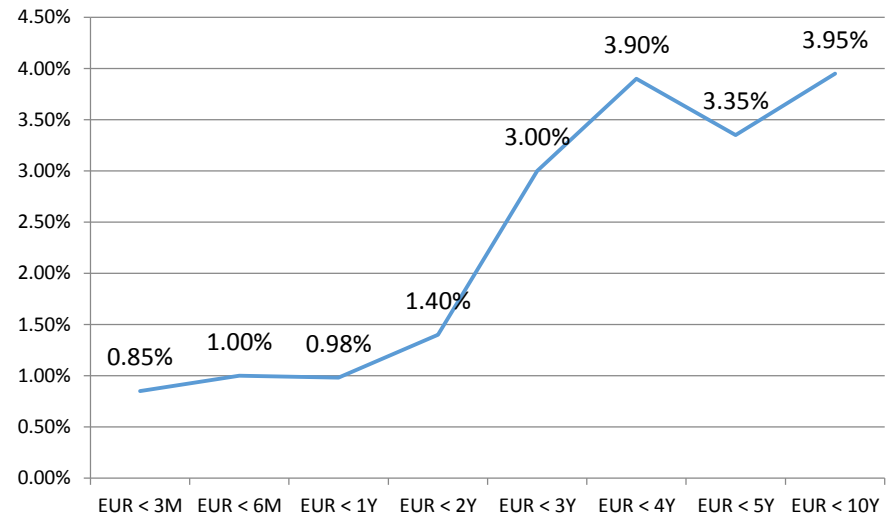
Yield curve EUR



Yield Curve RSD -OTC



Yield Curve EUR – OTC



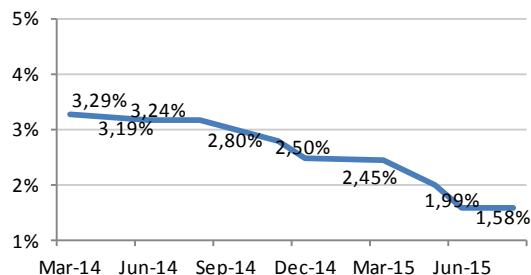


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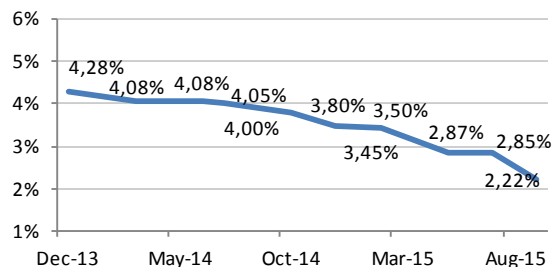
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What's the Story?

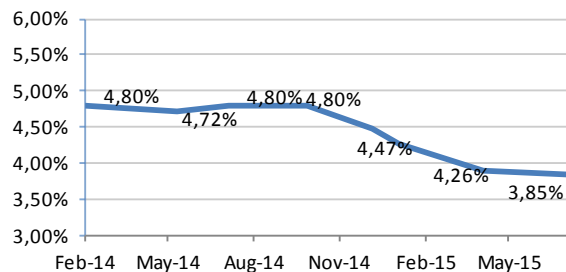
SRB€ 53W



SRB€ 2Y



SRB€ 3Y



The Serbian Government bond market, over the last few years has arguably been the best performing sector of the Serbian capital markets with total returns outperforming many equities.

Yields have been steadily declining over the last few years but in 2015 we have seen a acceleration in yield contraction in both local currency RSD and €uro denominated issues.

For example the core 1yr., 2yr. and 3yr €T-bonds have double digit contractions YoY

	Yields Yr. 2015	Yr. 2014	Bps	chng%
1Yr.€	1.580	3.1900	1.61	50.5%
2Yr.€	2.220	3.8000	1.58	41.6%
3Yr.€	3.850	4.8000	0.95	19.8%
5Yr.€	4.790	5.0000	0.21	4.2%



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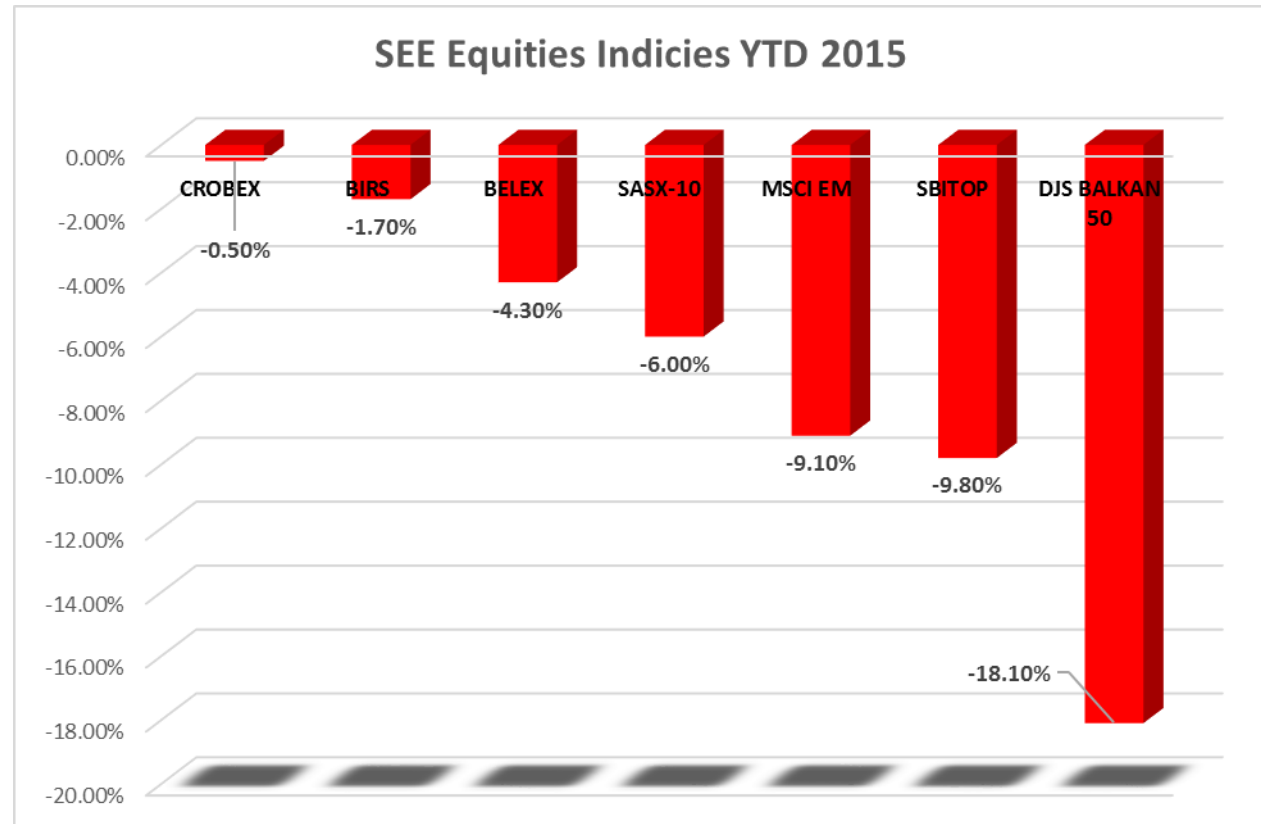
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Compared to negative performance of SEE equities.

Belex on of the better performers with only -4.3% YTD.

Not a single SEE equity index in the black.

Clearly the Serbia FI market is a better investment alternative.



NBS actions

NBS lowered key policy rate 300Bps to 5% YTD *with possibility of further easing in 1H16.*

Reduction of mandatory reserves requirements for RSD and FX. therefore releasing RSD and Euro Liquidity into the system(FX Reserves requirements reduced 1% per month for next 6 months)

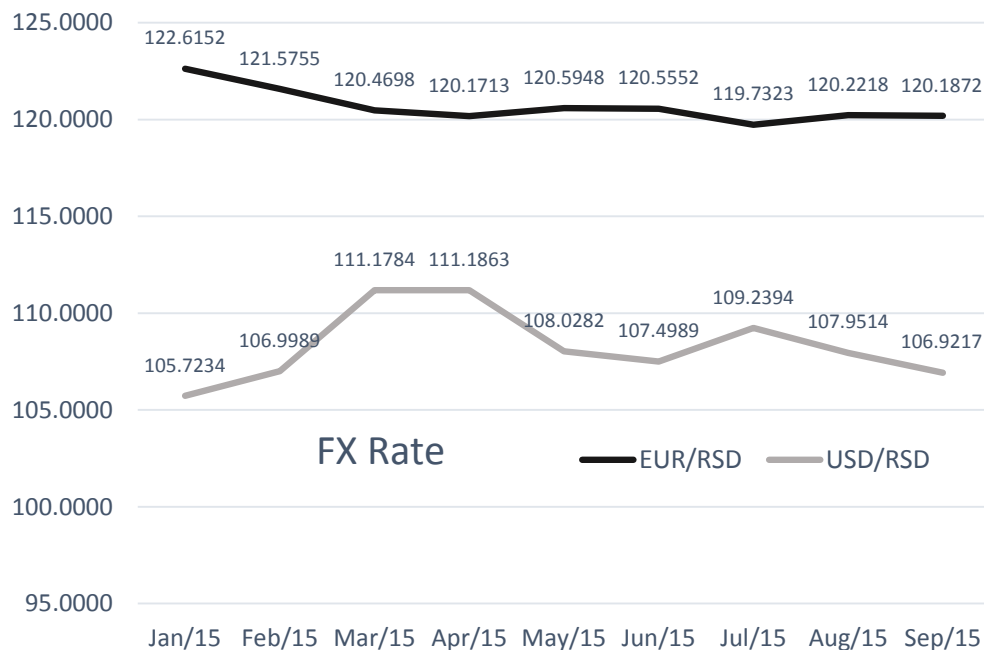
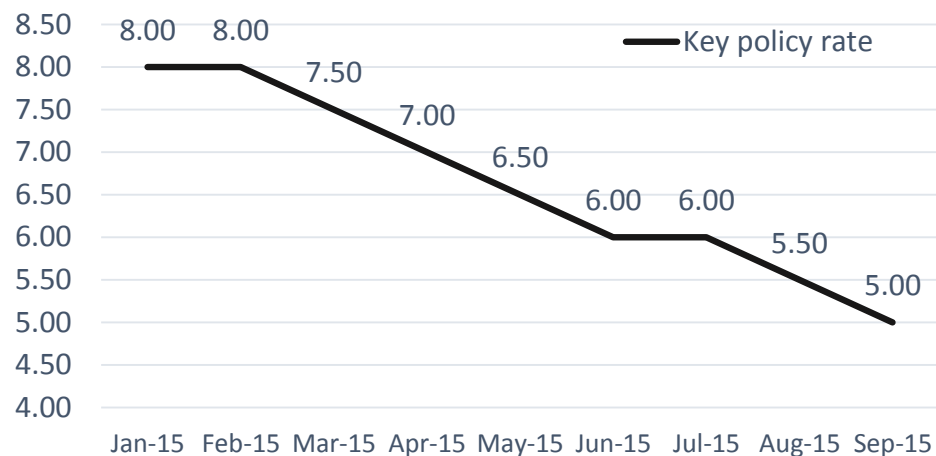
FY15 average inflation around just 1.7%, thus well below the target band of 2.5%.

FX stable with €640m FX accumulation YTD give NBS tool to manage Euro/RSD rate spike.

Credit rating and outlook stable and improving

MONEY MARKETS

EURIBOR		O/N	1W	1M	3M	12M
Level		-0.14	-0.15	-0.11	-0.05	0.14
ZIBOR		O/N	1W	1M	3M	12M
Level		0.35	0.35	1.00	1.10	1.80
BELIBOR		O/N	1W	1M	3M	12M
Level		3.11	3.57	4.18	4.56	4.83

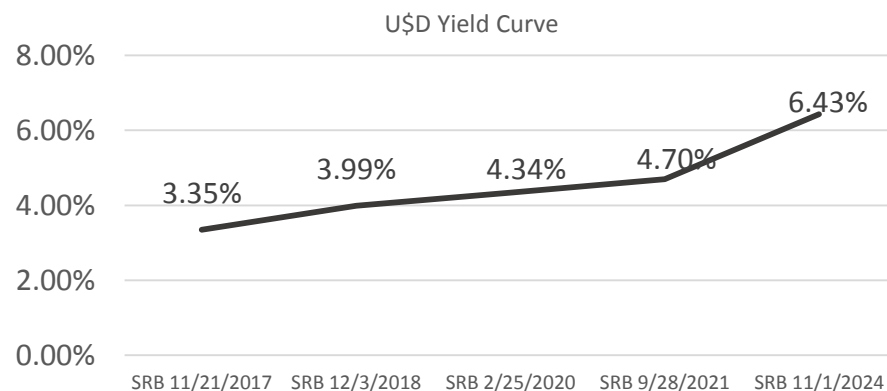
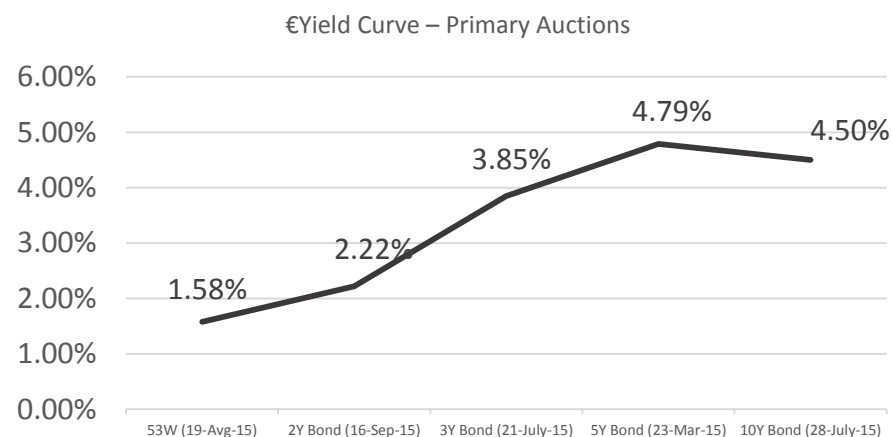
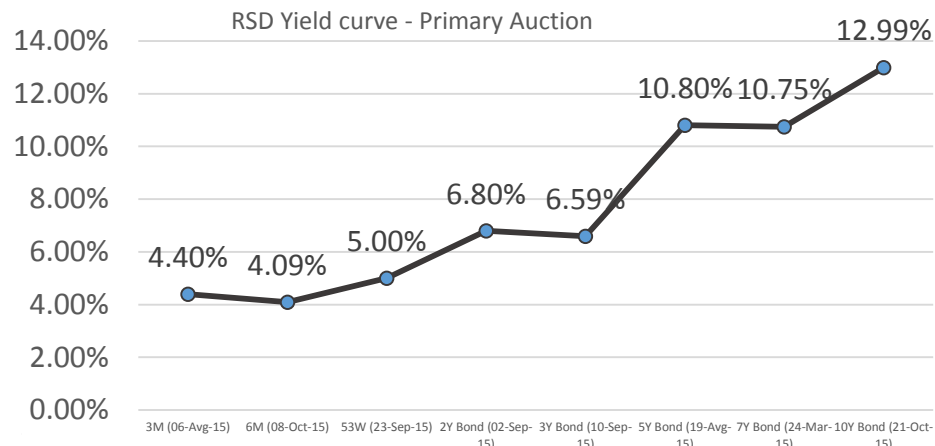


All SRB issues offer substantially higher yields relative to other sovereigns in the region. However, with marginally incremental risk.

	Foreign Currency Long Term			Local Currency Long Term		
Country	Moody's	S&P	Fitch	Moody's	S&P	Fitch
Bulgaria	Baa2	BB+	BBB-	Baa2	BB+	BBB
Croatia	Ba1	BB	BB	Ba1	BB	BB+
Hungary	Ba1	BB+	BB+	Ba1	BB+	BBB-
Romania	Baa3	BBB-	BBB-	Baa3	BBB-	BBB
Serbia	B1	BB-	B+	B1	BB-	B+
Slovakia	A2	A+	A+	A2	A+	A+
Slovenia	Baa3	A-	BBB+	Baa3	A-	BBB+

TREASURY BILLS

SLOVENIA	3M	6M	12M	18M					
Last yield	0.00%	0.01%	0.05%	0.15%					
CROATIA	3M	6M	12M	3M EUR, FX-linked	12M EUR, FX-linked				
Last yield	0.28%	0.50%	1.50%	0.20%	0.20%				
SERBIA	3M	6M	53W	2Y	3Y	53W, EUR	2Y, EUR	3Y, EUR	5Y, EUR
Last yield	4.40%	4.09%	4.89%	6.80%	6.59%	1.58%	2.22%	3.85%	4.79%

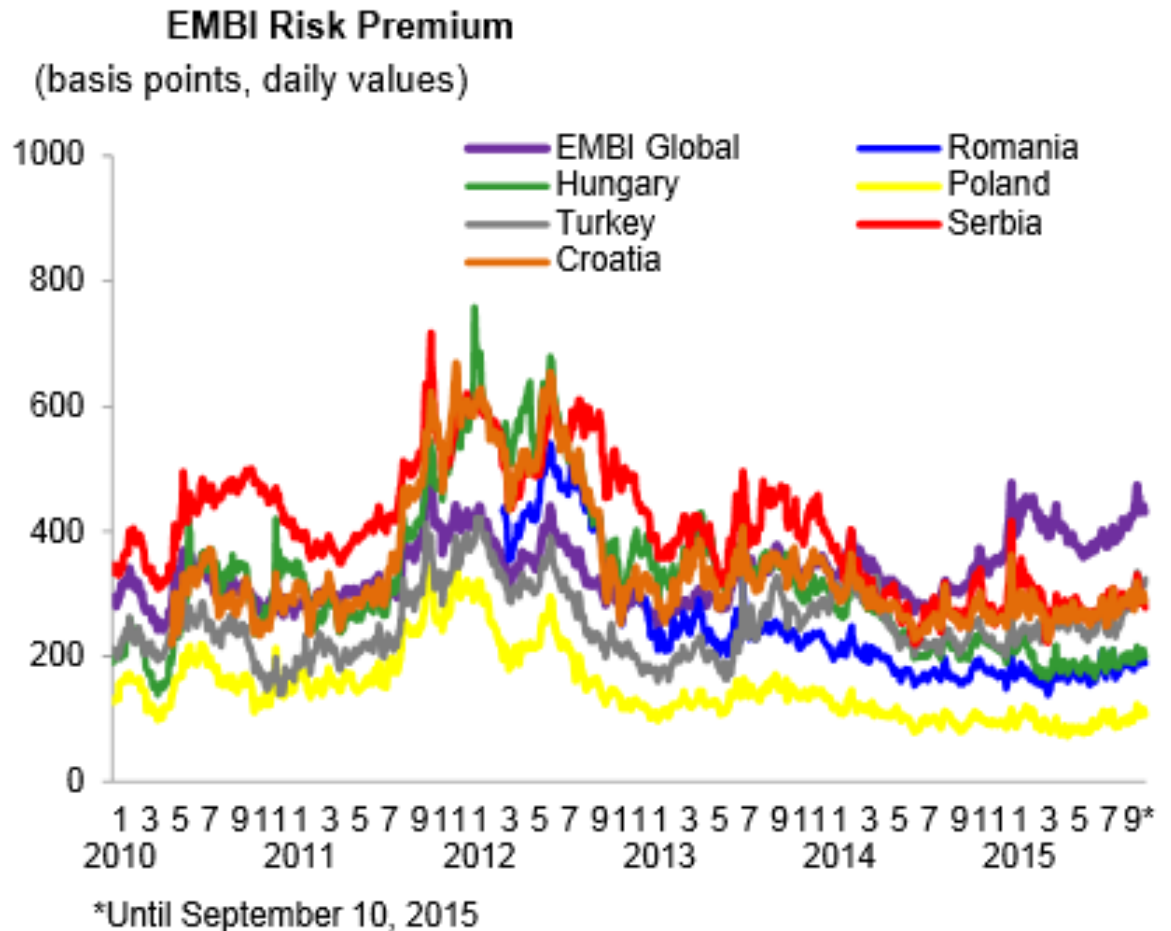




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Our view is that the perceived risk of Serbian sovereign debt is out of alignment with the actual risk...





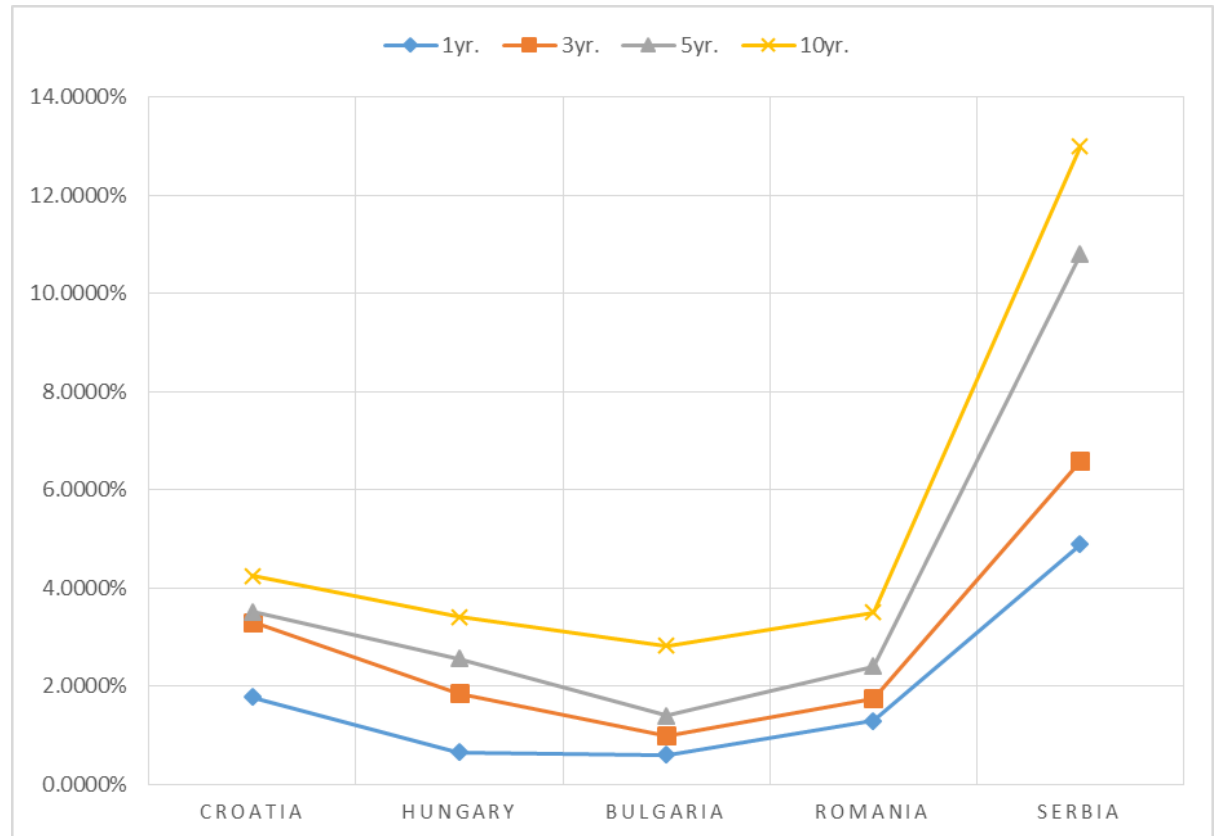
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and that the differentials, especially on the local currency issues, are too large.

However this has begun to change.

Local currency Yield Curves



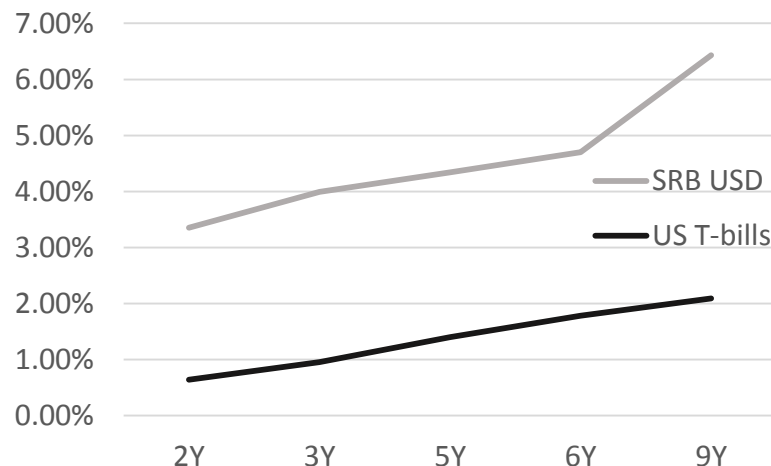
The interest on the \$ and € are at or near historical lows. And we do not see this changing in a significant way.

The same applies for local banks in Serbia.

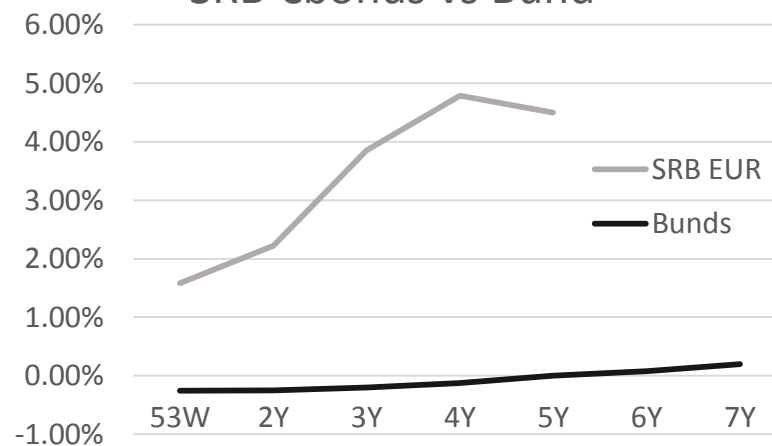
The NBS is driving the local rates downward so cost of funding is low in all three denominations.



SRB U\$D vs. US TBills



SRB €bonds vs Bund



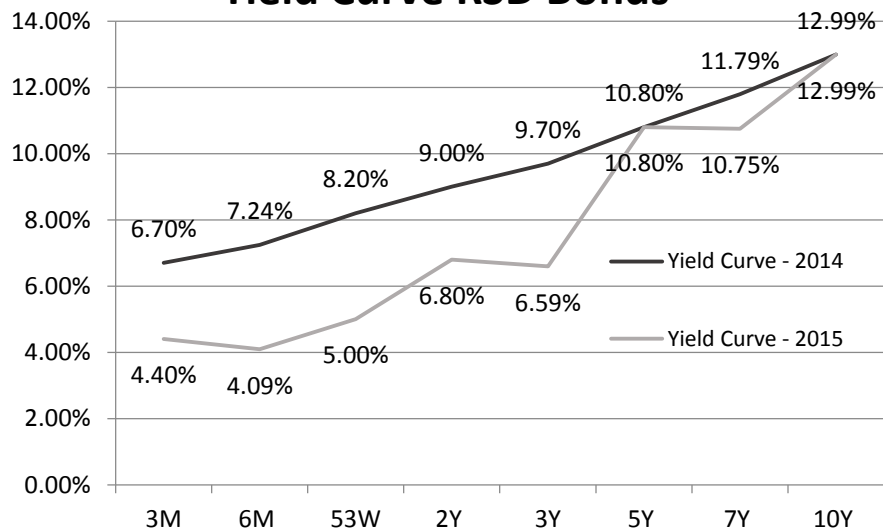


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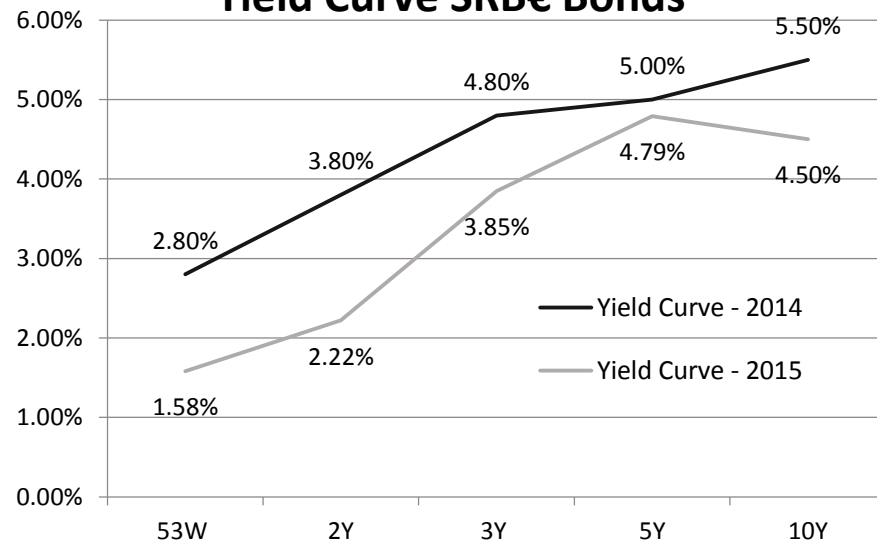
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Despite the recent contraction in Yields we feel that there still ample opportunity to take advantage of relatively higher yields and yield differentials.

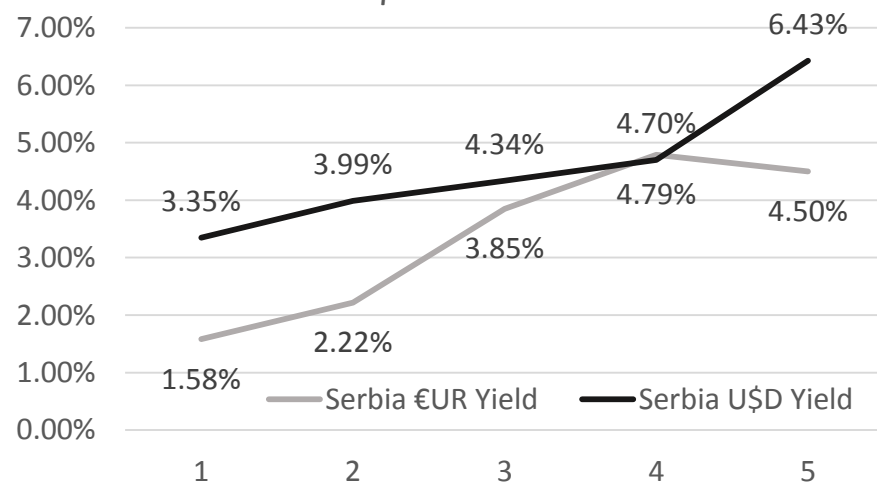
Yield Curve RSD Bonds



Yield Curve SRB€ Bonds



SRB€ vs SRB\$ Bonds Yield Curve



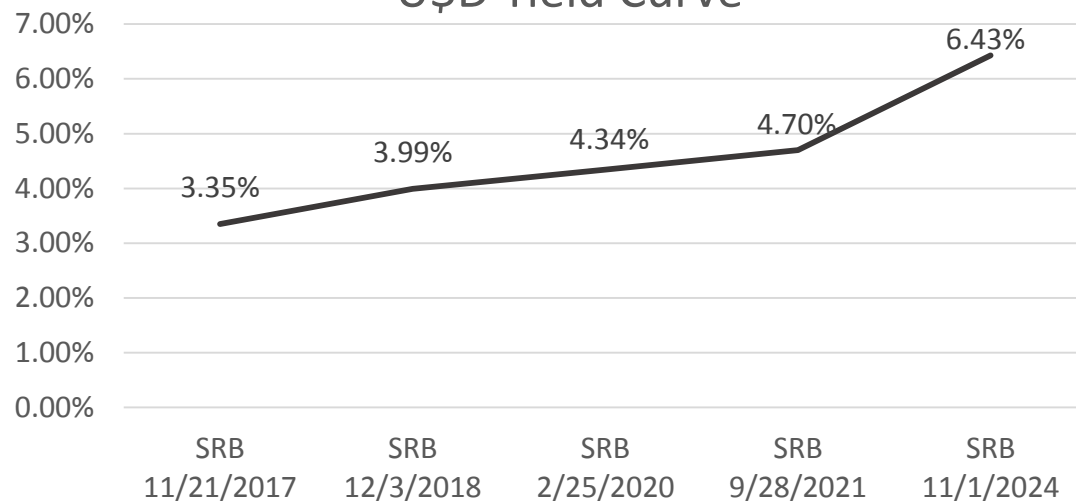


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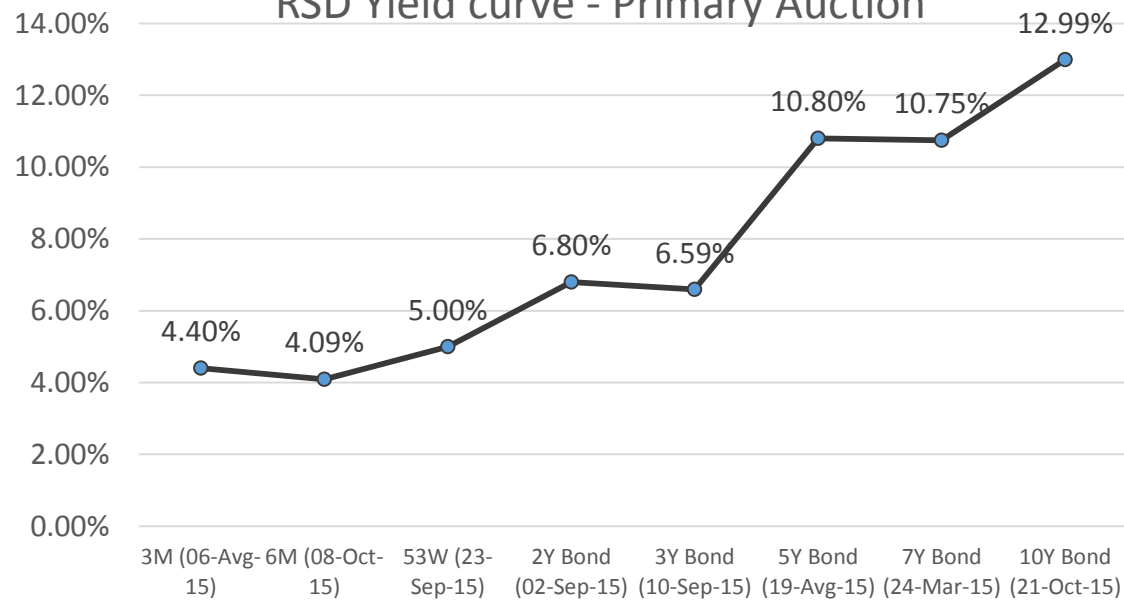
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Currently the most compelling opportunities are in the U\$D and RSD issues.

U\$D Yield Curve



RSD Yield curve - Primary Auction



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Recently, there has been a significant divergence between the U\$D/ €uro curves and with U\$D Yields increasing and €uro yields decreasing. Last year at this time the situation was exactly the reverse.

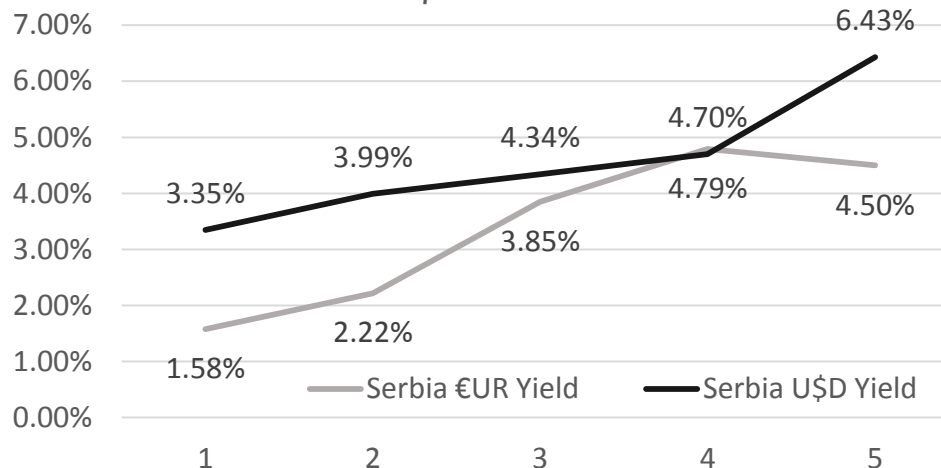
For example: At previous primary auction for 2Yr. €T-Bonds yielded 2.22% while at the same time the comparable SRB\$2017 was trading 107bps higher at a Yield of 3.29%. In relative terms a 48% yield premium. Trading on the OTC markets have seen this spread widen further.

The U\$Ds in addition to the Yields offer very attractive Coupons.

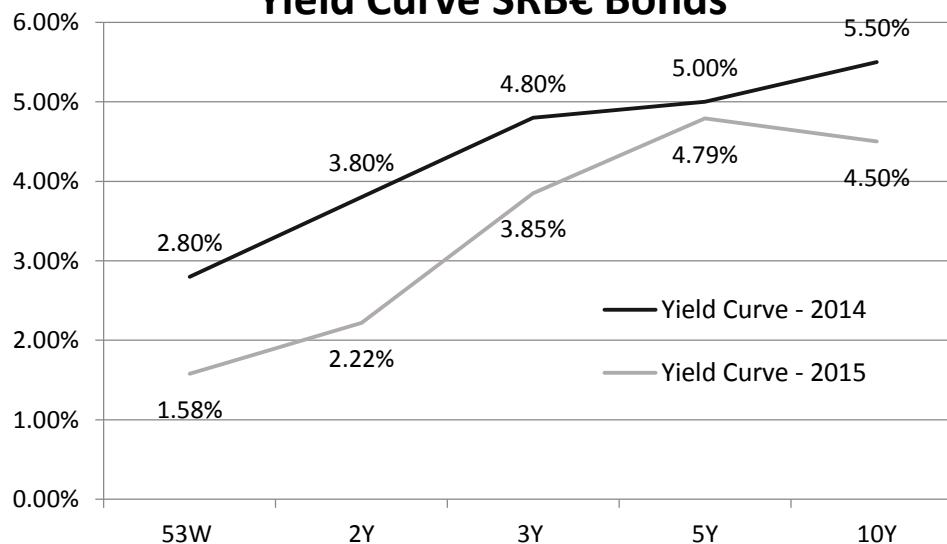
Description	Maturity date	Coupon
SERBIA17\$	21/11/2017	5.250
SERBIA18\$	03/12/2018	5.875
SERBIA20\$	25/02/2020	4.875
SERBIA21\$	28/09/2021	7.250
SERBIA24\$	01/11/2024	6.750

Given the sharp contraction over the past year and aggressive actions of the NBS and SRB MinFin we see much less upside potential for €Bonds.

SRB€ vs SRB\$ Bonds Yield Curve



Yield Curve SRB€ Bonds





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The other opportunity is in the mid and long end of the RSD curve.

The dinar continues to be stable and the NBS will continue its active management of the Key rate and the FX rate with its €640mil accumulated FX reserves YTD.

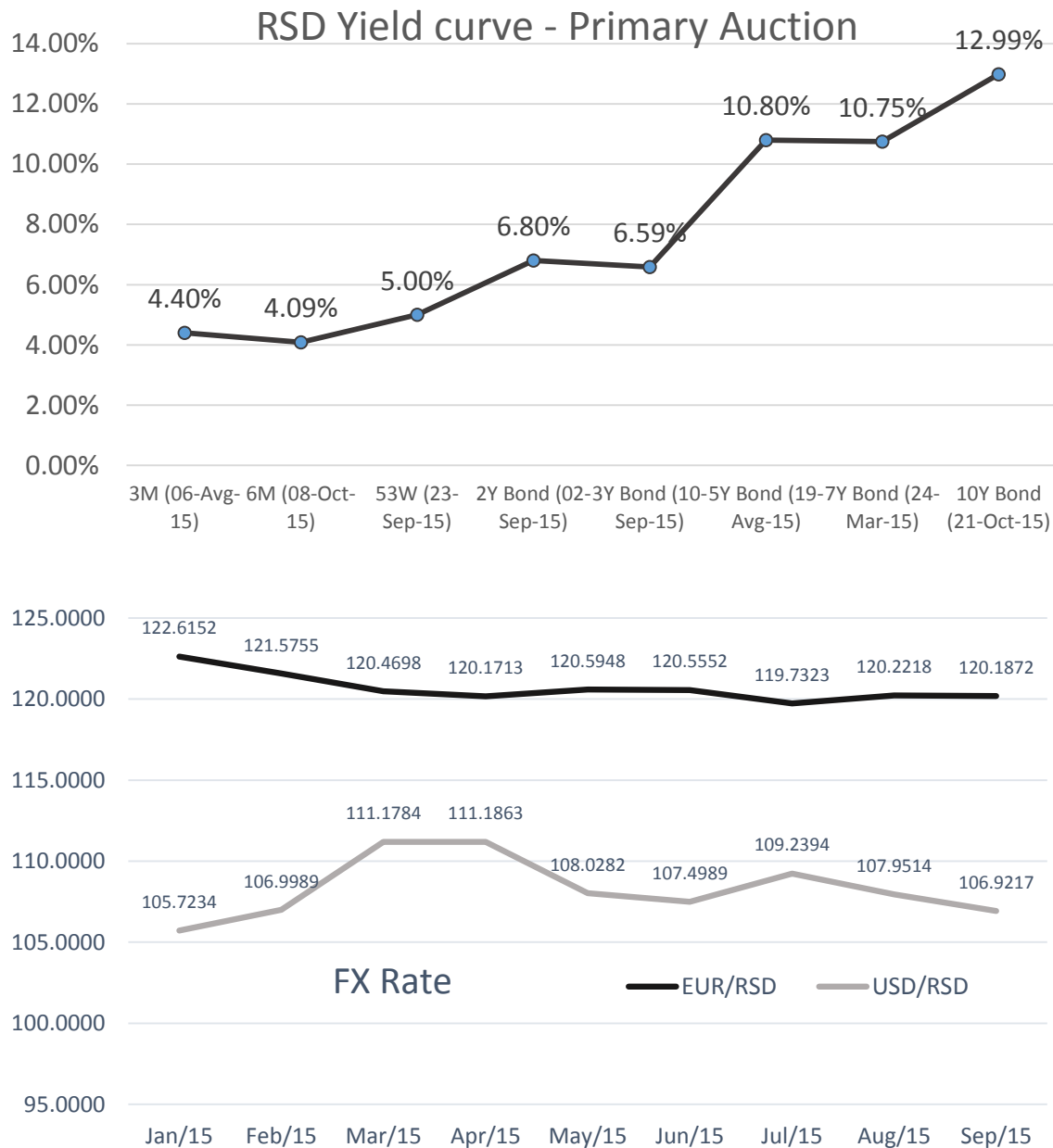
In addition swaps can be used to hedge FX risk as well.

EUR/RSD funding:

O/N +0,75pts (RSD 1,9%)

1M +27pts (RSD 2,60%)

3M +110pts (RSD 3,50%)



Serbia has a Positive outlook with good upside potential for growth.

To reach GDP per capita of Croatia SRB has GDP 50% upside for which we think this is a very realistic scenario.

Serbia exited recession: GDP rose 1,0% yoy (vs -2,0% yoy in Q1), marking an end to five quarters of contraction. GDP growth could accelerate in 3Q15 above 2% yoy.

GDP forecast upgraded to 0.7% and 1.3% in 2015 and 2016 respectively.

C/A narrowed – The 1H15 C/A deficit fell 30% yoy to EUR 728m. (thanks to 77% yoy higher service income, courtesy of stronger transport and travel income fees).

SELECTED ECONOMIC FORECASTS

		2013	2014	2015F	2016F	2017F
SLOVENIA	Nominal GDP (EURbn, current prices)	35.9	37.3	38.1	39.2	40.5
	Nominal GDP (USDbn)	47.7	49.6	41.9	39.2	38.5
	GDP per capita (EUR)	17,431	18,091	18,445	18,979	19,558
CROATIA	Nominal GDP (HRKbn, current prices)	329.6	328.4	329.9	334.5	342.5
	Nominal GDP (EURbn)	43.5	43	43.3	43.6	44.5
	GDP per capita (EUR)	10,225	10,114	10,188	10,294	10,490
SERBIA	Nominal GDP (RSDbn, current prices)	3.876	3.878	3.963	4.125	4.343
	Nominal GDP (EURbn)	34,3	33,1	32,7	33,3	34,4
	GDP per capita (EUR)	4.783	4.630	4.581	4.664	4.838

SELECTED ECONOMIC FORECASTS

		Real GDP (yoy, %)	Unemployment rate (ILO, %)	CPI Inflation (avg, yoy, %)	Budget balance (%/GDP)	Public debt (%/GDP)	Export of goods & services	Import of goods & services (EURbn)	C/A (%/GDP)	External debt (%/GDP)	EUR/local currency (avg)
SLOVENIA	2014	3.0	9.7	0.2	-4.9	80.9	27.0	-25.6	7.0	124.2	1.3
	2015F	2.5	9.4	-0.4	-2.7	86.8	28.6	-27.1	6.8	119.2	1.1
	2016F	2.2	9.1	0.8	-2.8	87.4	29.8	-28.5	7.0	118.8	1.0
	2017F	2.3	8.7	1.4	-2.4	86.8	30.8	-29.5	6.8	118.9	1.0
CROATIA	2014	-0.4	17.3	-0.2	-5.7	85.0	20.0	-19.1	0.7	108.4	7.6
	2015F	1.0	17.1	-0.2	-5.5	90.2	21.2	-19.7	1.9	109.9	7.6
	2016F	0.5	16.8	1.2	-5.7	94.4	22.0	-20.5	1.8	112.4	7.7
	2017F	1.3	16.0	1.5	-4.6	99.1	22.7	-21.3	2.1	114.8	7.7
SERBIA	2014	-1.8	18.9	2.1	-6.7	68.8	14.5	-18.1	-6.0	77.7	117.20
	2015F	0.7	18.2	1.7	-4.0	74.5	15.7	-19.1	-3.8	86.2	121.00
	2016F	1.3	17.8	2.6	-4.2	78.5	16.5	-19.8	-3.1	86.5	123.80
	2017F	1.5	17.0	3.5	-4.0	79.9	17.1	-20.2	-3.7	86.6	126.10

Serbia has a Positive outlook with good upside potential for growth (continued).

This year's average CPI will be at 1.7%, while next year inflation should push just inside the target band (2.6%)

NBS continues its aggressive cutting of the key rate – The global risk appetite has helped the NBS to boost FX reserves €640m ytd.

NBS cuts its key policy rate by 350bps ytd to a record-low 4.5%. NBS also lowered the mandatory FX reserves requirement in September by 1pp in each of the next six months furthering increasing liquidity.

MinFin continues to compress short-term rates in order to reduce borrowing costs and extend the mid and long end of the curve.

Recent rating assessments have been favourable, with Fitch and Moody's keeping Serbia's outlook on stable.

SELECTED ECONOMIC FORECASTS

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PRICES

		2013	2014	2015F	2016F	2017F
SLOVENIA	CPI Inflation (average % YoY)	1.8	0.2	-0.4	0.8	1.4
	PPI Inflation (average % YoY)	0.3	-0.6	0.6	1.5	1.8
CROATIA	CPI Inflation (average % YoY)	2.2	-0.2	-0.2	1.2	1.5
	PPI Inflation (average % YoY)	0.5	-2.7	-2.9	1.9	1.9
SERBIA	CPI Inflation (average % YoY)	7,8	2,1	1,7	2,6	3,5
	PPI Inflation (average % YoY)	3,6	0,7	0,9	3,7	4,9

FISCAL BALANCE (% of GDP)

		2013	2014	2015F	2016F	2017F
SLOVENIA	State budget balance (ESA-95)	-14.9	-4.9	-2.7	-2.8	-2.4
	Public debt	70.3	80.9	86.8	87.4	86.8
	Gross public funding needs	19.5	14.6	10.5	13.4	9.6
CROATIA	State budget balance	-5.4	-5.7	-5.5	-5.7	-4.6
	Public debt	80.6	85.0	90.2	94.4	99.1
	Gross public funding needs	16.3	21.3	21.5	19.4	22.1
SERBIA	State budget balance	-5.5	-6.7	-4.0	-4.2	-4.0
	Public debt	58.8	68.8	74.5	78.4	79.9
	Gross public funding needs	16.1	17.7	17.6	17.1	19.7

Additional talking Points

Big Ticket Privatizations:

- *Telecom Serbia target valuation (€2-2.4bil)*
- *EPS(National Electric Co.)*
- *Komercijalna Bank (Nomura selected as advisor)*
- *Dunav Insurance Group*

*Big International investors in the market: KKR 1bil.
buyout of SBB(cable, internet and telecom provider).
In discussions for buying of distressed assets/NPL's*

Opening of EU negotiations.

Conversion play relative to Cro & Slo and wider region.



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Takeaways:

Serbia has been in a strong bull market over the last few years with substantial acceleration in yield contractions and thus conversion to neighboring markets.

Our view is that this is the result of the perceived risk of Serbian sovereign debt is out of alignment with the actual risk. However this has begun to change.

Despite the recent contraction in Yields we feel that there still ample opportunity to take advantage of relatively higher yields and yield differentials.

And the most compelling opportunities are in the U\$D and RSD yield curves.



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Thank you

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