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## Lead analysts:

Maxim Khudalov, Director  
+7 (495) 139-0496  
maxim.khudalov@acra-ratings.ru

Vasilii Tanurcov, Director  
+7 (495) 139 0344  
vasilii.tanurcov@acra-ratings.ru

Key rating assessment  
factors

## ACRA affirms AAA(RU) to PJSC ROSSETI, outlook Stable

The affirmed credit rating assigned to [PJSC ROSSETI](#) (hereinafter, the Company, or Rosseti) is on par with the financial obligations of the Russian Government due to the Company's very high systemic importance for the Russian economy and very high state influence on the Company.

Rosseti's standalone creditworthiness assessment (SCA) at aa- is due to the Company's monopoly management of the Russian power grid complex, very high profitability, moderate debt load, and very high liquidity. Negative cash flow due to substantial capital expenditures limits the Company's SCA.

PJSC ROSSETI is a power grid operator in Russia. It consolidates 15 power grid companies: FCG UES (managing high-voltage power transmission lines in Russia) and 14 subsidiaries that manage grid distribution complexes in various regions of Russia. The Company's power transmission services represent a natural monopoly and are regulated by government rates. The Company manages nine utilities companies as well. The state, represented by Rosimuschestvo, is the controlling shareholder with an 88% stake.

**Strategic importance for the nation and state control over the Company.** Rosseti is the monopoly operator of Russia's power grid complex - the only sector in the power industry where the state retained shareholding control and direct government regulation after electricity market liberalization. Rosseti performs quasi-government functions in terms of social risk insurance (it assumes electricity retail sales if energy retailers go bankrupt), social support (cross subsidies in rates), technical policy, and power infrastructure development. The government invested RUB 72 bln into the Company's capital in 2010-2017, with subsidies totaling RUB 6.5 bln; [The government development corporation VEB.RF \(AAA\(RU\), outlook Stable\)](#) purchased RUB 156 bln worth of infrastructure bonds of the group's companies in the same period.

**Infrastructure monopoly with moderate regulatory risk.** The practice of holding down grid tariffs in order to sustain the overall electricity prices in Russia was used extensively in previous years as the share of the transmission tariff in the ultimate electricity price was high, and the state has retained direct regulation of grid tariffs. Tough tariff policy in the grid complex, including two tariff freezes in 2012 and 2014, has been in place since 2012. However, Rosseti improved its profitability in the above period and reduced its debt load by optimizing operational and capital expenditures. The low inflation mode could make the Company less susceptible restrictive tariff policies but more sensitive to non-payments as the devaluation of problem debt would slow down.

**Moderate debt load.** According to ACRA's estimates, the Company's total debt to cash flow could be moderate in 2019-2021 (ratio of total debt to FFO before net payments at 2.03x-2.2x). The Company will maintain the volume of its investment program in 2019-2020 at the levels of previous years, which will not lead to significant growth in the debt load in the base case scenario. All of the Company's debt is unsecured and ruble denominated; the bond debt accounts for 63% of the total debt. The average loan maturity is 9 years.

**Negative cash flow.** The Company's free cash flow could remain negative in 2019-2021. High capital expenditures are the key factor for the negative cash flow. The investment to revenue ratio peaked in 2011-2012. The ratio declined from 53% to 27% from 2012 to 2018. On average, 40% of the investment program is used for fixed assets maintenance, 37% for technological connections, and the remaining part for new construction, etc. As part of the company's strategy for building a digital network before 2030, growth in the capital program is possible after 2021, but it will be provided with a corresponding cash flow.

**Key assumptions**

- Average tariff indexation rate remaining at 3%, the average inflation at 3.9% in 2019-2021;
- The Company successfully implementing its capital investment program with annual investments of RUB 230-260 bln in 2019-2020;
- Dividend payments at 50% of the IFRS net profit excluding the investment component.

**Potential outlook or rating change factors**

The **Stable outlook** assumes that the rating will most likely stay unchanged within the 12 to 18-month horizon.

**A negative rating action may be prompted by:**

- Loss of state control, for instance through the privatization of the Company;
- Significant decline of the Company's systemic importance for the Russian economy;
- Substantial decrease in the financial support from the state and an increase of dividends in favor of the budget.

**Rating components**

**Standalone creditworthiness assessment (SCA):** aa-

**Support:** on par with RF.

**Issue ratings**

No outstanding issues have been rated.

**Regulatory disclosure**

The credit rating has been assigned under the national scale for the Russian Federation and is based on the [Methodology for Credit Ratings Assignment to Non-Financial Corporations under the National Scale for the Russian Federation](#), the [Methodology for Analyzing Relationships Between Rated Entities and the State](#), and the [Key Concepts Used by the Analytical Credit Rating Agency Within the Scope of Its Rating Activities](#).

The credit rating assigned to PJSC ROSSETI was published by ACRA for the first time on March 2, 2018. The credit rating and its outlook are expected to be revised within one year following the publication date of this press release.

The assigned credit rating is based on the data provided by PJSC ROSSETI, information from publicly available sources as well as ACRA's own databases. The assigned credit rating is based on the IFRS consolidated reporting of PJSC ROSSETI. The credit rating is solicited, and PJSC ROSSETI participated in its assignment.

No material discrepancies between the provided data and the data officially disclosed by PJSC ROSSETI in its financial statements have been discovered.

ACRA provided no additional services to PJSC ROSSETI. No conflicts of interest were discovered in the course of credit rating assignment.

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75, Sadovnicheskaya embankment, Moscow, Russia  
[www.acra-ratings.com](http://www.acra-ratings.com)

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