

May 15, 2019

Lead analysts:

Alexander Gushchin, Associate
Director
+7 (495) 139-0489
alexander.gushchin@acra-ratings.ru

Ekaterina Mozharova, Senior Director
+7 (495) 139-0498
ekaterina.mozharova@acra-ratings.ru

Key rating assessment
factors

ACRA upgrades T2 RTK Holding LLC to A(RU), outlook Stable, and its bonds to A-(RU)

The credit rating of [T2 RTK Holding LLC](#) (the Company) has been upgraded on the positive dynamics in the operating and financial metrics and better coverage and leverage demonstrated by the Company in 2018. The Company is assessed as a large-scale company, characterized by the high operating profile assessment, high profitability, and medium liquidity position.

The Company is a mobile operator ranking 4th in terms of subscriber base and revenue in Russia. Currently, the Company shareholders include PJSC Rostelecom (45%) and Tele2 Russia Holding AB (55%), through which the Company's shares are held, as far as the Agency is aware, by PJSC Bank VTB (27.5%), INVINTEL B.V. controlled by Alexey Mordashov (22%) and ABR Investments B.V. (5.5%) controlled by BANK "ROSSIYA."

The leverage assessment has declined from high to medium. The total debt / FFO before net interest ratio declined to 3.17x in 2018 against 4.24x in 2017, which is caused mainly by a 35% increase in the FFO before net interest, while the volume of debt has remained virtually unchanged. The Company's debt obligations are denominated in rubles and a significant portion of them are floating interest rate obligations. The ratio of debt adjusted for operating lease to FFO before fixed charges has decreased from 4.3x to 3.2x in 2018, and this ratio may decline to 2.5–2.7x in the next three years. The Company's coverage has grown up to the medium level: the ratio of FFO before fixed charges to fixed charges went up to 3.75x in 2018 (2.33x in 2017). The Agency is of the opinion that the ratio may go up to 3.9–4.0x in the forecast period (2019–2021).

Liquidity deteriorating due to substantial repayments expected in 2019–2020. A significant portion of the loans borrowed by the Company will become due in 2019 and 2020 (25% and 34%, respectively), which is negative for the liquidity assessment. ACRA notes that the Company's debt includes mainly loans borrowed from shareholder banks (73%), which reduces the refinancing risks to some extent. In addition, the Company's liquidity is supported by the significant amount of undrawn credit lines.

High operating profile assessment is underpinned primarily by the strong business profile of the Company. In providing mobile phone and Internet services, the Company operates its own telecommunications infrastructure that supports various technologies (2G, 3G and 4G). ACRA notes that the geography of the Company's operations is wide and includes 67 regions of the Russian Federation. At the federal level, the Company's market share lags behind the three largest players. According to ACRA estimates, in 2018, the market share of the Company was about 17%, which is almost twice lower than the share of the market leader PJSC "MTS." ACRA assesses the quality of corporate governance as high. The Company has developed and implements the strategy for the period from 2018 to 2022. The shareholding structure is transparent, and the risk management functions are structured and formalized (however, the internal risk management regulations contain no restrictions on borrowings in currencies other than the currency of revenue). The Company composes its IFRS financial statements annually, but it has not published such statements since 2016. On the other hand, the Company publishes, in a quarterly basis, press releases that include its key financial and operating indicators.

Large-sized company with high profitability. The average annual growth in the Company's subscriber base amounted to 4.2% in 2017–2018. By December 31, 2018, the number of subscribers reached 42.3 million. This growth was accompanied by an increase in the monthly average revenue per user (ARPU) (+11.5% in 2018), which resulted in a 16.4% revenue increase in 2018. Last year, the Company showed a 44% increase in the FFO before fixed charges and taxes up to RUB 43.6 bln.

In 2019–2021, we expect that the growth in the Company's subscriber base, ARPU, revenues, and FFO before fixed charges and taxes will continue, but at a slower pace. Similar to 2017, the Company has managed to maintain its profitability high in 2018. The FFO margin before fixed charged and taxes reached 31% in 2018. We believe that in 2019–2021, the margin will remain close to its current level.

Free cash flow is low, which is caused by the considerable expenses under the corporate investment program. In 2018, the Company increased its capex (against 2017), which pushed the free cash flow (FCF) down, and the FCF margin declined from 6% to 1%. According to ACRA estimates for 2019–2021, the Company's capex will grow further, which will continue to put pressure on the FCF margin. An additional pressure on the cash flow may come from the debt financing required for PJSC Rostelecom to repurchase the Company shares held by other shareholders. As the common market practices show, in case such scenario becomes true, the Company is likely to pay dividend to its parent company, which may further reduce its FCF.

Key assumptions

- Revenue growth outrunning the market average, based on growing subscriber base and ARPU;
- The substantial amount of undrawn credit lines will remain unchanged;
- The aggregate expenses required to comply with the new regulations (amendments introduced to the Federal Law "On Countering Terrorism" and the Criminal Code of the Russian Federation) will be in the range of RUB 20–25 bln in 2019–2020.

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 positive rating action may be prompted by:

- The ratio of total debt adjusted for operating lease to FFO before fixed charges declining below 2.0x or the ratio of FFO before fixed charges to fixed charges growing above 5.0x;
- The FCF margin going up to 2%.

A negative rating action may be prompted by:

- The scenario where the parent company repurchases the Company's shares, which may affect the creditworthiness of the Company;
- The ratio of total debt adjusted for operational lease to FFO before fixed charges growing above 3.5x or the ratio of FFO before fixed charges to fixed charges declining below 2.5x;
- Shrinking annual average ARPU amid zero growth in the subscriber base;
- Deteriorating structure of debt obligations;
- Significantly deteriorating access to external sources of liquidity;
- A significant growth in the aggregate expenses required to comply with the new regulations (amendments introduced to the Federal Law "On Countering Terrorism" and the Criminal Code of the Russian Federation) in 2019–2020.

Rating components

Standalone creditworthiness assessment (SCA): a.

Adjustments: none.

Support: no.

Issue ratings

[Certificated interest-bearing non-convertible bearer bonds issued by Tele2-Saint-Petersburg OJSC \(RU000A0JRK4\)](#), maturity date: June 11, 2021, issue volume: RUB 5 bln — **A-(RU)**.

[Certificated interest-bearing non-convertible bearer bonds issued by Tele2-Saint-Petersburg OJSC \(RU000A0JS3L9\)](#), maturity date: January 31, 2022, issue volume: RUB 4 bln — **A-(RU)**.

Credit rating rationale. Bond issues (ISIN RU000A0JRK4, RU000A0JS3L9) are senior unsecured debt of Tele2-Saint-Petersburg OJSC (the Issuer), a subsidiary of [T2 RTK Holding LLC](#) (the Group). The bonds were rated following a public irrevocable offer from T2 RTK Holding LLC, the holding company of the Group. The Issuer is an operating company of the Group, but its share in the Group's returns is not high. In the absence

of a direct guarantee from T2 Mobile LLC, the main operating company, the Issuer's senior unsecured debt is deemed subordinate to other financial liabilities of the Group. According to the ACRA methodology, the reimbursement rate for Issuer's unsecured debt belongs to Category III, and therefore, the bond issues are rated A-(RU), i.e. one notch lower than the credit rating of T2 RTK Holding LLC.

Regulatory disclosure

The credit ratings of T2 RTK Holding LLC and the bonds (ISIN RU000A0JRKC4, RU000A0JS3L9) issued by T2 RTK Holding LLC were assigned under the national scale for the Russian Federation based on the [Methodology for Credit Ratings Assignment to Non-Financial Corporations under the National Scale for the Russian Federation](#) and the [Key Concepts Used by the Analytical Credit Rating Agency Within the Scope of Its Rating Activities](#). The Methodology for Assigning Credit Ratings to Individual Issues of Financial Instruments Under the National Scale of the Russian Federation was also used in the credit rating process.

The credit ratings assigned to T2 RTK Holding LLC and the bonds (ISIN RU000A0JRKC4, RU000A0JS3L9) issued by T2 RTK Holding LLC were first published by ACRA on June 9, 2018, July 11, 2018 and July 11, 2018, respectively. The credit rating of T2 RTK Holding LLC and its outlook as well as the credit ratings of the above bonds are expected to be revised within one year following the publication date of this press release.

The assigned credit ratings are based on the data provided by T2 RTK Holding LLC, information from publicly available sources, as well as ACRA's own databases. The credit ratings are solicited, and T2 RTK Holding LLC participated in the rating process.

No material discrepancies between the provided data and the data officially disclosed by T2 RTK Holding LLC in its financial statements have been discovered.

ACRA provided no additional services to T2 RTK Holding LLC. No conflicts of interest were discovered in the course of credit rating process.

(C) 2019

Analytical Credit Rating Agency (Joint-Stock Company), ACRA (JSC)
75, Sadovnicheskaya embankment, Moscow, Russia
www.acra-ratings.com

Analytical Credit Rating Agency (ACRA) was founded in 2015, with its 27 shareholders representing major Russian corporate and financial institutions and its authorized capital exceeding RUB 3 bn. ACRA's main objective is to provide the Russian financial market with high-quality rating products. Methodologies and internal documents of ACRA are developed in compliance with Russian legislation and with regard to global rating industry best practices.

The provided information, including, without limitation, credit and non-credit ratings, rating assessment factors, detailed credit analysis results, methodologies, models, forecasts, analytical reviews and materials, as well as other information placed on the ACRA website (further referred to as Information), coupled with the ACRA website software and other applications, are intended for information purposes only. Information must not be modified, reproduced or distributed by any means, in any way or form, either in whole, or in part, in marketing materials, as part of public relations events, in news bulletins, in commercial materials or reports without prior written consent from, and reference to, ACRA. Any use of Information in violation of these requirements or the law is prohibited.

ACRA credit ratings reflect ACRA's opinion about the ability of a rated entity to meet its financial obligations or about the credit risk of individual financial obligations and instruments of a rated entity at the time of publication of the relevant Information.

Non-credit ratings reflect ACRA's opinion about certain non-credit risks assumed by interested parties interacting with a rated entity.

The assigned credit and non-credit ratings reflect all material information pertaining to a rated entity and known by ACRA (including the information received from third parties), the quality and reliability of which ACRA considers appropriate. ACRA shall not be responsible for the accuracy of information provided by clients or relevant third parties. ACRA does not audit or otherwise verify the provided data and shall not be held responsible for their accuracy and completeness. ACRA conducts rating analysis of information provided by customers using its own methodologies, with the texts thereof available on ACRA's website – www.acra-ratings.com/criteria.

No credit rating and/or credit rating outlook is regulated by the Central Bank of the Russian Federation, unless distributed so that such credit rating and/or credit rating outlook is in the public domain.

The only source that reflects the latest Information, including the one about credit and non-credit ratings assigned by ACRA, is ACRA's official website – www.acra-ratings.com. Information is provided on an "as is" basis.

Information shall be considered by users exclusively as ACRA's statement of opinion and must not be regarded as advice, recommendation or suggestion to buy, hold or sell securities or other financial instruments of any kind, nor shall it be viewed as an offer or advertisement.

Neither ACRA, nor its employees and persons affiliated with ACRA (further referred to as the ACRA Parties) provide any direct or implied guarantee expressed in any form or by any means regarding the accuracy, timeliness, completeness or applicability of Information for making investment and other decisions. ACRA does not act as a fiduciary, auditor, investment or financial advisor. Information must be regarded solely as one of the factors affecting an investment decision or any other business decision made by any person who uses ACRA's information. It is essential that each of such persons conduct their own research and evaluation of a financial market participant, as well as an issuer and its debt obligations that may be regarded as an object of purchase, sale or possession. Users of Information shall make decisions on their own, involving their own independent advisors, if they deem it necessary.

ACRA Parties shall not be responsible for any action taken by users based on Information provided by ACRA. ACRA Parties shall under no circumstances be responsible for any direct, indirect or consequential damages or losses resulting from interpretations, conclusions, recommendations and other actions taken by third parties and directly or indirectly connected with such information.

Information provided by ACRA is valid only as of the date of preparation and publication of materials and may be amended by ACRA in the future. ACRA shall not be obliged to update, modify or supplement Information or inform anyone about such actions, unless the latter was recorded separately in a written agreement or is required by legislation of the Russian Federation.

ACRA does not provide advisory services. ACRA may provide additional services, if this does not create a conflict of interest with rating activities.

ACRA and its employees take all reasonable measures to protect all confidential and/or material non-public information in their possession from fraud, theft, unlawful use or inadvertent disclosure. ACRA provides protection of confidential information obtained in the course of its business activities as required by legislation of the Russian Federation.