

December 27, 2018

Lead analysts:

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

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

Key rating assessment
factorsACRA assigns BBB-(RU) to "RZD Trading Company" JSC,
outlook Stable

The credit rating assigned to "[RZD Trading Company](#)" JSC (hereinafter, RZD Trade, or the Company) is based on very high debt load and volatile free cash flow, as well as a high likelihood of extraordinary support from the key shareholder, strong liquidity and its strong business profile.

RZD Trade is a subsidiary of "Russian Railways" JSCo ([AAA\(RU\), outlook Stable](#); hereinafter, RZD, the Group, the Supporting Institution, or the SI), which main goals are the supply of rolling stock to the Group, the recycling of rolling stock, and sales of used and repaired spare parts, as well as the provision of logistics services to RZD enterprises. The Company carries out the development of the Port of Rajin (DPRK) through the "RasonConTrans" joint venture. Apart from RZD, the non-state pension fund "BLAGOSOSTOYANIE" has a stake in RZD Trade.

The likelihood of extraordinary support from the key shareholder is based on a high level of creditworthiness of the Supporting Organization and the degree of the Company's connection with the SI. The Company provides material support to RZD subsidiaries. RZD is the key shareholder in RZD Trade, i.e. the Group holds 50% plus one share in the Company with the remaining part owned by the NPF "BLAGOSOSTOYANIE", which is controlled by RZD. The Group has operational control due to a significant number of its representatives in the Board of Directors of RZD Trade (five out of seven). ACRA points to a heavy dependence of the Company on the Supporting Institution since the overwhelming amount of the Company's operations is related to RZD. In the meantime, the strategic importance of RZD Trade for the Group is not so great because the Company can be replaced by another organization that performs similar functions in the medium-term. RZD has no guarantees, sureties or cross-defaults on the Company's obligations. According to the ACRA methodology, the final credit rating of RZD Trade is three notches higher than the standalone creditworthiness assessment (SCA).

Very high debt load with a significant share of funds from the shareholder. RZD Trade's debt consists of two parts, namely the funds raised to finance the Company's current activities (RUB 1.3 bln), and those raised by the JV "RasonConTrans" from RZD companies as long-term investments in the development of the Port of Rajin and related railway infrastructure (RUB 13.3 bln). Interest on loans provided by the Group is accrued but is not actually paid, which leads to the corresponding increase in the Company's debt obligations. The entire debt is represented by ruble-denominated liabilities with a fixed interest rate.

The ratio of the Company's total debt to its FFO (funds from operations) before net interest payments stood at 55.5x at the end of 2017, and the ratio of total debt to revenues amounted to 7.7x, which corresponds to very high debt load. Should the debt load be assessed only in terms of bank loans, these ratios would've been 3.3x and 0.5x respectively. According to ACRA estimates, RZD Trade's debt will remain at its current level in 2019-2020. Since the Company does not actually pay interest on loans granted by RZD and its subsidiaries, the interest payment coverage is at a low but still an acceptable level: the ratio of FFO before net interest payments to interest payments was 1.8x in 2017. ACRA expects this figure to remain in the 1.6x and 1.9x range in 2018-2020.

Strong liquidity with volatile free cash flow. The Company has obtained consent from RZD to postpone all payments on loans granted by the Group's enterprises until 2020, which helped significantly reduce the pressure on RZD Trade's liquidity. The Company's bank loans worth RUB 1.3 bln are short-term and due in September 2019. On September 30, 2018, the Company had undrawn credit lines worth RUB 2.2 bln that were granted by Sberbank ([AAA\(RU\), outlook Stable](#)) and "SMP Bank" JSC. RZD Trade's free cash flow (FCF) is characterized by a high level of volatility. As such, it ranged from RUB -1.1 bln to RUB 1.6 bln in 2015-2017. ACRA does not rule out the FCF entering a negative zone in the

forecast period, which determines a weak assessment of the factor. As a result, ACRA assesses RZD Trade's liquidity as high in 2018-2020 due to the lack of significant loan repayment, a high likelihood of further postponement of the loan repayment and the availability of access to liquidity sources to cover the possible negative FCF.

Strong business profile. The dynamics of demand for goods supplied by RZD Trade does not have a pronounced cyclical nature and is based on the needs of RZD subsidiaries, which are the Company's key counterparties. RZD's highest possible credit rating suggests a low level of the counterparty risk. ACRA points to a significant amount of overdue receivables in the range between 10% and 20% of all receivables in 2018. The settlement structure envisages a mirror reflection of the terms and the order of payment for buyers and suppliers, and if there is the lack of payment from buyers, the Company employs short-term loans to pay suppliers should the need arise.

In addition to trading activities, RZD Trade is involved in the development of a logistics hub in DPRK, namely the Port of Rajin and the Tumangan-Rajin railway line. The Port of Rajin has a capacity of 5 million tons per year for coal transshipment. The current low loading of the Port is due to sanctions on North Korea. However, in accordance with UN Security Council Resolution 2371 as of August 5, 2017, sanctions do not apply to coal that was extracted outside DPRK and transported through its territory for exporting from the Port of Rajin. The absence of such restrictive measures can contribute to the growth of the port's cargo turnover, which in turn can lead to the improvement in the assessment of the Company's business profile in the future.

Key assumptions

- Restructuring of a loan provided by the Supporting Institution with the postponement of repayment dates until 2020 and the payment of accrued interest on the respective repayment dates;
- Maintenance of the systemic importance level;
- Maintenance of the current settlement structure with suppliers and buyers;
- Maintenance of a significant amount of available credit lines;
- Transshipment volume of coal in the Port of Rajin will be 0.7-1 mln tons in 2019-2020 with an average annual transshipment price of USD 7.5 per ton.

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 growth of the Company's strategic importance for RZD;
- The transfer of loans provided by the Group into the capital of RZD Trade;
- A significant increase in the Company's performance indicators (revenue growth to RUB 100 bln, and FFO to net interest payments and taxes up to RUB 30 bln).

A negative rating action may be prompted by:

- The Company's lower strategic importance for the Group;
- No restructuring of a loan provided by the Supporting Institution with the postponement of repayment dates until 2020 and the payment of accrued interest on the respective repayment dates;
- Transshipment volume of coal in the Port of Rajin will be below 700,000 tons in 2019-2020 with an average annual transshipment price below USD \$7 per ton;
- The deterioration of debt structure;
- A significant deterioration in access to external liquidity;
- The deterioration of the settlement structure with counterparties.

Rating components

SCA: bb-.

Adjustments: none.

Support: group — SCA plus 3 notches.

Issue ratings

There are no outstanding issues.

Regulatory disclosure

The credit rating has been assigned to "RZD Trading Company" JSC 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](#), the [Methodology for Analyzing Member Company Relationships Within Corporate Groups](#), and the [Key Concepts Used by the Analytical Credit Rating Agency within the Scope of Its Rating Activities](#).

The credit rating has been assigned to "RZD Trading Company" JSC for the first time. The credit rating and its outlook are expected to be revised within one year following the rating action date (December 25, 2018).

Disclosure of deviations from approved methodologies: the geographical diversification factor was assessed with a deviation from the assessment range as specified in the methodology.

The credit rating is assigned based on data provided by "RZD Trading Company" JSC, information from publicly available sources, as well as ACRA's own databases. The credit rating is solicited, and "RZD Trading Company" JSC participated in its assignment.

No material discrepancies between provided data and data officially disclosed by "RZD Trading Company" JSC in its financial statements were discovered.

ACRA provided no additional services to "RZD Trading Company" JSC. No conflicts of interest were discovered in the course of credit rating assignment.

(C) 2018

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.