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Key rating assessment
factors

Key assumptions

ACRA affirms AA(RU) to PJSC Rostelecom, outlook Stable, and AA(RU) to bond issues

The credit rating of [PJSC Rostelecom](#) (hereinafter, the Company, or Rostelecom) is based on the Company's very strong business profile, very large scope and leading market positions, very high liquidity level, and moderate state support. At the same time, the Company's rating assessment is limited by medium leverage, the fact that some of Rostelecom's infrastructure sections are from different generations of telecommunications technology, and the Company's substantial presence in segments with declining revenues.

Rostelecom is the largest provider of digital services and solutions in all segments in Russia, a leading fixed-line services provider in the majority of regions, and the largest broadband operator. The Russian Federation is the Company's biggest shareholder. The state directly owns 48.71% of ordinary shares through the Federal Agency for State Property Management (Rosimushchestvo) and another 4.29% is owned by THE STATE DEVELOPMENT CORPORATION VEB.RF ("VEB") ([AAA\(RU\), outlook Stable](#)). 36.52% of ordinary shares are in free float.

The Company's medium leverage is determined by the low level of total debt to FFO (funds from operations) before net interest payments (at 2.25x) and debt adjusted for operating lease to FFO before fixed payments (at 2.38x) ratios. The FFO before fixed charges to fixed charges ratio stands at 4.3x. The Company's fiscal policy assumes maintaining the total debt to EBITDA ratio below 2.5x. Rostelecom does not expect the consolidation of the share package in the capital of T2 RTK Holding LLC ([A\(RU\), outlook Stable](#), hereinafter, Tele2) to lead to an increase above this level.

The strong business profile stems from Rostelecom's highly diversified activities. In 2018, the largest shares in Company's revenue structure were broadband Internet (25%) and fixed-line services (22%), despite declining demand for the latter over recent years. The Company almost entirely owns its infrastructure, making its activities more sustainable. However, some of its sections are from different generations of telecommunications technology, which limits the rating level.

Rostelecom's very large size and leading market positions are mostly determined by the large market shares the Company holds in both the Russian telecommunications services market and its key market segments. Rostelecom has a vast customer base: 17.0 mln subscribers in the fixed-line segment, 13.0 mln subscribers in the broadband segment, and 10.2 mln subscribers in the paid-TV segment (according to data from Q1 2019). In 2018, the FFO before fixed charges and taxes amounted to RUB 100.9 bln.

The Company's very strong liquidity position is based on substantial amounts of undrawn credit lines that exceed the Company's loan portfolio by 75%. At the same time, committed credit facilities account for 22% of the undrawn credit lines. ACRA expects that in 2019, the Company's FCF (free cash flow) after dividend payments will be negative while FCF profitability should stay above -4%.

Rostelecom's high profitability is based on a high blended ARPU (average revenue per user) value, which stood at RUB 543 in Q1 2019 (7% higher than in Q1 2018). FFO before fixed charges was 31% in 2018. Although this figure is fairly high, it is somewhat lower than similar indicators demonstrated by peers in the Russian telecommunications industry.

- No substantial expenses as part of consolidating the share package in the capital of Tele2 that could lead to an increase in debt load;
- Reducing the fixed-line telephony market by 5-6% annually;
- Maintaining a substantial amount of undrawn credit lines including committed facilities.

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:

- Decrease in the ratio of debt adjusted for operating lease to FFO before fixed charges below 2.0x; increase in the ratio of FFO before fixed charges to fixed charges above 5.0x.

A negative rating action may be prompted by:

- Substantial expenses as part of consolidating the share package in the capital of Tele2 that could lead to an increase in debt load;
- Increase in the ratio of debt adjusted for operating lease to FFO before fixed charges exceeding 3.0x;
- Reduction in annual average revenues from fixed-line and wholesale services by more than 6% in 2019–2021;
- Revenue growth from new services below planned levels;
- Considerably less access to external liquidity sources;
- Substantial capital expenditures caused by amendments to the Federal Law “On Counteracting Terrorism” and to the Criminal Code of the Russian Federation.

Rating components

Standalone creditworthiness assessment (SCA): aa-

Adjustments: none.

Support: +1 notch to SCA.

Issue ratings

[Exchange-traded interest-bearing certified unregistered bond issued by PJSC Rostelecom \(ISIN RU000A0ZYG52\)](#), maturity date: November 9, 2027, issue volume: RUB 10 bln — **AA(RU)**.

[Exchange-traded interest-bearing certified unregistered bond issued by PJSC Rostelecom \(ISIN RU000A0ZYEE3\)](#), maturity date: March 3, 2028, issue volume: RUB 10 bln — **AA(RU)**.

[Exchange-traded interest-bearing certified unregistered bond issued by PJSC Rostelecom \(ISIN RU000A100881\)](#), maturity date: March 21, 2029, issue volume: RUB 15 bln — **AA(RU)**.

Credit rating rationale. The above issues (RU000A0ZYG52, RU000A0ZYEE3, RU000A100881) represent senior unsecured debt of PJSC Rostelecom. Due to the absence of either structural or contractual subordination of the issues, ACRA regards them *pari passu* with other existing and future unsecured and unsubordinated debt obligations of the Company. According to ACRA’s methodology, the credit ratings of the bonds are equivalent to that of PJSC Rostelecom.

Regulatory disclosure

The credit ratings were assigned to PJSC Rostelecom and the bonds (RU000A0ZYG52, RU000A0ZYEE3, RU000A100881) issued by PJSC Rostelecom 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](#), [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 Methodology for Assigning Credit Ratings to Individual Issues of Financial Instruments under the National Scale of the Russian Federation was also applied to assign credit ratings to the above bond issues.

The credit ratings of PJSC Rostelecom and the bonds (RU000A0ZYG52, RU000A0ZYEE3, RU000A100881) issued by PJSC Rostelecom were first published by ACRA on July 14, 2017, November 21, 2017, March 16, 2018, and April 3, 2019, respectively. The credit rating of PJSC Rostelecom 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 PJSC Rostelecom information from publicly available sources, as well as ACRA's own databases. The credit ratings are solicited, and PJSC Rostelecom participated in their assignment.

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

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

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