Fitch Affirms SIBUR at 'BB+'; Outlook Stable

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Fitch Ratings-London/Moscow-18 February 2015: Fitch Ratings has affirmed Russia-based petrochemical group PAO SIBUR Holding's (SIBUR) Long-term Issuer Default Rating (IDR) at 'BB+' with a Stable Outlook. Fitch also affirmed SIBUR's Short-term IDR at 'B', and SIBUR Securities Limited's five-year USD1bn guaranteed notes due 2018 at 'BB+'.

The affirmation and Stable Outlook reflects SIBUR's ability to withstand recent market challenges, namely the drop in the price of oil since late 2014 and rebased foreign-currency liabilities on a weaker rouble, which has contributed to funds from operations (FFO) net adjusted leverage of 2.4x at FY14. While higher than our medium-term downgrade guidance of 2.0x, we expect this to be a temporary spike which can be accommodated at the current rating level. Key drivers of SIBUR's financial flexibility include its increased export competitiveness as a result of a weak rouble, its flexibility on investments in the already committed ZapSib-2 project and its strong EBITDAR margin due to its low cost base.

SIBUR's ratings are constrained by higher than average systemic risks associated with the Russian business and jurisdictional environment. Excluding these risks, Fitch assesses SIBUR's credit profile in the 'BBB' category.

KEY RATING DRIVERS
Largest Russian Petrochemical Player
SIBUR's ratings reflect its leading market and cost position in the Russian petrochemical sector, its diversified portfolio and its access to competitively priced feedstock. Despite a balanced revenue split across product types, the EBITDA split is formed by feedstock and energy products. SIBUR remains highly exposed to Russia and CIS (2013: 63%) followed by the European market (27%). The export share is 43% and varies across products - from 25%-35% for plastics and basic polymers, and 50% for energy products to 60% for synthetic rubbers.

FX offsets Oil Price Shock
Up to 50% of SIBUR's sales at 9M2014 retained a material correlation with oil prices, and given the recent oil price shock we project a negative impact on EBITDA across SIBUR's product portfolio. However, the RUB/USD exchange rate has a negative correlation with the oil price and thus will largely mitigate the impact, as SIBUR's sales are either exports or linked to non-rouble export prices, while most of its costs are rouble-denominated. Sibur also has a long-term strategy to reduce its exposure to oil prices and the recent Tobolsk Polymer project (500kt of polypropylene capacity) reflects this.

2014 and 2015 Performance Outlook
We forecast SIBUR's 2014 sales to be above RUB350bn on the back of a weak rouble and aided by Ust-Luga's low-marginal trading operations. Rouble devaluation will not be fully reflected in EBITDAR margin which we expect to be 30%. We also expect SIBUR's capex to average 18%-20% of sales from 2014, while conservatively assuming SIBUR follows its dividend policy (25% payout) - resulting in low single digit free cash flow (FCF) margin in 2014. Taking into account the M&A outflows and joint venture financing (RUB30bn, mostly a payment to Rosneft for the acquired stake in Yugragazpererabotka) and debt revaluation on a weaker rouble, we forecast FFO net adjusted leverage at 2.4x at FY2014.

SIBUR's 2015 sales are forecast to remain above RUB350bn, as the Ust-Luga terminal deconsolidation is offset by higher contributions from the newly launched gas fractionating unit, the Purovsk-Pyt-Yach pipeline, and the Tobolsk polymer plant. The weaker rouble will affect the EBITDAR margin, pushing it up to 33%-35%, despite facing rouble cost inflation in the mid-teens. Moderated capex will offset the remaining USD1bn payment to Rosneft, and this will add to the positive factors keeping leverage flat at 2.4x in 2015, and allowing SIBUR to deleverage towards 2x from 2016.

Flexibility on ZapSib-2 Project
In 3Q14, SIBUR approved the USD9.5bn ZapSib-2 petrochemical project which is expected to add 1.5 million tonnes (mt) of cracking and 2mt of polymer capacity. The project will account for most of SIBUR's capex over the rating horizon, and the company's flexibility around it will be a crucial factor for its ability to withstand market challenges. SIBUR has demonstrated flexibility on its ZapSib-2 investments in 2015-2016 by moderating investments and adjusting the project implementation schedule. Should SIBUR demonstrate its inability to cut or delay its ZapSib-2 investments further in the case of the prolonged market downturn, this would create additional pressure on its leverage and ratings.

KEY ASSUMPTIONS

Fitch's key assumptions within our rating case for the issuer include:

- 2014 and 2015 sales of around RUB350bn impacted by new operations (Ust-Luga trade operations in 2014, Tobolsk polymer and new gas fractionation unit ramp up in 2015), and sustained rouble devaluation, compensating negative oil impact on sales.
- EBITDA margin to exceed 30% starting from 2015 due to sustained rouble devaluation and Tobolsk Polymer.
- RUB/USD expected to appreciate from 60 in 2015 to 53 in 2017.
- Oil price in line with Fitch's oil price deck, increasing from USD55 per barrel of Brent in 2015 to USD80 in the long run.
- Capex assumed at 18%-20% of sales in 2015-2016.
- Dividends are set as 25% of IFRS net profits, in line with dividend policy. FX loss impact is conservatively excluded.
- USD1bn M&A activity in 1Q15 (completion of Yugra acquisition) falls below FCF line resulting in a leverage spike in 2015 (2.4x) with deleveraging towards 2x from 2016.

RATING SENSITIVITIES

Positive: Future developments that could lead to positive rating action include:
- Further operational improvements and capacity expansion resulting in enhanced scale and product diversification and/or portfolio mix.
- FFO net adjusted leverage at, or below 1.5x through the cycle.
- Sustained positive FCF generation.

Negative: Future developments that could lead to negative rating action include:
- Material deterioration in the company's cost position or access to low-cost associated petroleum gas.
- Aggressive financial or investment strategy, which results in an increased financial burden or sustained negative FCF through the investment cycle.
- FFO adjusted net leverage materially over 2x for a protracted period, i.e. no move back towards 2x (2014: 2.4x) over the next two years.

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Additional information is available on www.fitchratings.com. For regulatory purposes in various jurisdictions, the supervisory analyst named above is deemed to be the primary analyst for this issuer; the principal analyst is deemed to be the secondary.

Applicable criteria, 'Corporate Rating Methodology', dated 28 May 2014, are available at www.fitchratings.com.

Applicable Criteria and Related Research:
Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage

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