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Credit Opinion: Sibur Holding, PJSC

Global Credit Research - 08 Apr 2015

St. Petersburg, Russia

Ratings

Category	**Moody's Rating**
Outlook	Negative
Corporate Family Rating	Ba1
Sibur Securities Limited	
Outlook	Negative
Bkd Senior Unsecured	Ba1/LGD4

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Key Indicators

[1]**Sibur Holding, PJSC**

	12/31/2014	12/31/2013	12/31/2012	12/31/2011	12/31/2010
Revenues (USD Billion)	$9.6	$8.5	$8.7	$7.8	$5.7
PP&E (net) (USD Billion)	$6.1	$9.5	$7.6	$5.1	$4.5
EBITDA Margin %	22.0%	27.7%	31.7%	39.3%	36.2%
ROA - EBIT / Average Assets	8.3%	13.5%	19.8%	25.8%	22.2%
Debt / EBITDA	4.2x	2.1x	1.6x	1.2x	1.2x
EBITDA / Interest Expense	8.5x	11.3x	16.5x	17.8x	12.8x
Retained Cash Flow / Debt	26.3%	34.6%	29.4%	76.3%	61.2%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Source: Moody's Financial Metrics

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

- Sovereign rating of Russia and its outlook, sovereign ceiling

- Exposure to volatile petrochemical industry

- Sizable export business and domestic leadership

- Sustainable profitability above that of global peers

- Financial profile to withstand pressure from a large investment project

Corporate Profile

Sibur Holding, PJSC (Sibur) is a Russian vertically integrated gas processing and petrochemicals company. As of end-September 2014, Mr. Mikhelson was the major shareholder with 50.2% of the shares, followed by Mr. Shamalov (21.3%) and Mr. Timchenko (15.3%). The company's current and former management holds the remaining 13.2%. In 2014, Sibur generated revenue and adjusted EBIT of $9.6 billion and $1.3 billion, respectively.

SUMMARY RATING RATIONALE

Sibur's Ba1 corporate family rating (CFR) is constrained by (1) Sibur's exposure to the weakening of Russia's credit profile, as captured by Moody's downgrade of the sovereign rating and Russia's country ceiling to Ba1 from Baa3 with negative outlook on 20 February 2015; (2) susceptibility to risks inherent to the petrochemical industry, heightened by Sibur's moderate size compared to that of its global peers; and (3) the risk of decreasing capex flexibility at later stages of ZapSibNeftekhim project implementation. Sibur remains subject to the Russian macroeconomic environment, despite high volume of exports, given that all of the company's production facilities are located within Russia.

More positively, Sibur's CFR reflects our expectation that Sibur will materially deleverage to 2.0x debt/EBITDA by mid-2016. The expectation factors in (1) Sibur's export potential and position as a leading petrochemicals business in Russia; (2) long-term contractual access to attractively priced feedstock translating into low costs, securing high margins through the cycle; (3) high flexibility with the implementation of ZapSibNeftekhim project; and (4) commitment to a conservative financial policy.

DETAILED RATING CONSIDERATIONS

EXPOSURE TO THE WEAKENING CREDIT PROFILE OF RUSSIA

The company's rating reflects the weakening of Russia's macroeconomic and financial climate, as captured by Moody's downgrade of Russia's government bond rating to Ba1/Not Prime (NP) from Baa3/Prime-3 (P-3) and Russia's country ceilings for foreign currency debt to Ba1/NP from Baa3/P-3 on 20 February 2015, with negative outlook. The ratings levels for corporate issuers reflect Moody's concerns about trends in the financial strength of the Russia government, and potential that domestic companies could face challenges in meeting their external debt obligations in the event of a severe erosion in the government and central bank's financial flexibility which is a driver for why the foreign currency ceiling has been aligned with the rating of the sovereign. A country ceiling generally indicates the highest rating level that any issuer domiciled in that country can attain for instruments of that type and currency denomination. For additional information, please refer to the related announcement https://www.moodys.com/research/--PR_318857.

Moody's believes that, even for corporates without material medium-term foreign currency refinancing needs, the likely continued severe deterioration of the operating environment might lead to a substantial weakening in their credit profiles.

The resilience of Russian non-financial corporates to the increased risk arising from the prevailing negative operating conditions in the domestic market is likely to be limited, as reflected by the alignment of the country ceiling for foreign currency debt with the sovereign rating.

EXPOSURE TO VOLATILE PETROCHEMICAL INDUSTRY

Sibur is exposed to the inherent risks of the petrochemical industry, price volatility and demand cyclicality. Our outlook for the North American and EMEA chemical industry in 2015 remains stable on the back of a projected 2.5% growth of global GDP and lower oil prices. At the same time, we expect that demand growth will be sluggish in Europe and below historical norms in Asia, which are major exports markets for Sibur, accounting respectively for 71% and 15% Sibur's export revenue. In this environment, individual company performance will depend on their product mix. We expect that pricing environment for Sibur's petrochemicals will be ranging from marginally weak to stable in 2015, excluding synthetic rubbers which have continuously faced weak prices. We see Sibur's exposure to the weak domestic market as manageable within the current rating, given that (1) the company generates a half of total revenue from exports and has a leading position in the domestic market; and (2) domestic sales are essentially linked to international benchmark prices for the majority of products.

Sibur's credit profile is likely to be stronger in this environment than those of some of its domestic and global peers because of its diversification into the feedstock and energy segment and access to attractively priced feedstock. This segment, which is not dependent on the cyclicality of the petrochemical industry, generates around 80% of

Sibur's reported unadjusted EBITDA, sustains high margins, reflecting attractively priced feedstock, and, on its turn, ensures a low cost base for the company's petrochemicals business. The weak rouble additionally supports Sibur's export competitiveness, given the company's largely rouble-denominated operating costs and mitigates the negative impact of lower oil prices on the company's energy business. As a result, we forecast that Sibur's total revenue in roubles will grow steadily in mid single digits annually in 2015-16, driven by an increase of export sales on the back of launch of new capacities under the completed investment programme, supported by the weak rouble.

LEADING PRODUCER OF ENERGY PRODUCTS AND PETROCHEMICALS IN RUSSIA

Sibur is a leading producer of energy products and petrochemicals in Russia, which makes its business more robust to the vulnerability of the Russian operating environment compared to domestic peers.

In 2013, Sibur accounted for 54% of the associated petroleum gas (APG) processing and 36% of the liquefied petroleum gases (LPG) production in Russia, and was the third-largest domestic supplier of natural gas (in volume terms) after Gazprom and Novatek (both Ba1 negative), according to the Central Dispatch Department of the Fuel and Energy Complex. In 2014, Sibur increased its share in the domestic APG following the increase of its stake from 51% to 100% in Yugragazpererabotka (YGPP), a joint venture with Rosneft International Holdings Limited (Ba1 negative), a subsidiary of Rosneft (Ba1 negative), engaged in the APG processing.

According to IHS, in 2013, Sibur's share in the domestic production capacity was 46% for monoethylene glycol, 50% for styrene-butadiene rubber, 35% for low-density polyethylene and 56% for polypropylene (including the production capacity of a joint venture with an affiliate of Gazprom Neft (Ba1 negative)).

According to management's data, there were no downward changes to Sibur's shares in key domestic market segments or industry capacities in 2014.

PROFITABILITY ABOVE THAT OF PEERS, SUPPORTED BY UNIQUE ACCESS TO FEEDSTOCK

Sibur has demonstrated high profitability through the cycle (with a five-year average adjusted EBITDA margin of around 30%, and above 20% during the 2008-09 global financial crisis), exceeding that of its major European peers. This is underpinned by Sibur's competitive cost position, which in turn is driven by its unique access to feedstock, i.e., low-cost APG and competitively priced natural gas liquids (NGL) in West Siberia. Long-term supply contracts with key suppliers and recently launched pipeline infrastructure are reinforcing these benefits.

Sales of energy products resulting from feedstock processing (natural gas, LPG, naphtha and others) enhance Sibur's profitability, as the company internally consumes only around 26% of produced NGLs volumes. In 2014, Sibur's energy products accounted for around 59% of total reported revenue and the EBITDA margin of the energy business was around 35%.

Strong margins derived from the nature of the product mix provide Sibur with greater resilience to the economic downturn than its less profitable peers. In addition, the sales and profitability of energy products are less volatile than those of petrochemical products, providing an additional degree of resilience to the downturn. Sibur's reported EBITDA margin in 2014 (adjusted for low margin naphtha trading) of 32.2% (2013: 29.2%) is very strong and above many of its European peers.

Sibur's mentioned increase in stake in YGPP additionally strengthens its long-term access to feedstock, while new volume and pricing arrangements of YGPP and Rosneft on supply and sales of APG will not adversely affect Sibur's profitability.

At the same time, we expect that the rising profitability of the petrochemicals business will mitigate the risk of a decrease in the energy segment's profitability over the next 3-5 years as a result of potentially changing feedstock composition, with the share of less profitable NGL increasing at the expense of most profitable APG, which has a limited production potential.

FINANCIAL PROFILE TO WITHSTAND PRESSURE DESPITE IMPLEMENTATION OF LARGE INVESTMENT PROJECT

Sibur has a new ZapSibNeftekhim investment project to establish a new capacity to produce 1.5 million tons per annum of various grades of polyethylene and 500 ktpa of polypropylene, valued at $9.5 billion as of September 2014, including the expenditure already incurred and costs budgeted for commissioning. Despite significant capex under the project, we expect that Sibur will decrease its leverage over the next 18 months to around 2.0x debt/EBITDA, while maintaining EBITDA margins of around 25% and the ratio of retained cash flow (RCF) to net

debt above 20% (the metrics include Moody's standard adjustments). This expectation factors in (1) Sibur's sustainable export operations at high margins, supported by attractively priced feedstock and the weak rouble; (2) high flexibility with the implementation of ZapSibNeftekhim project (demonstrated by a reduction of capex for 2015); and (3) shareholders-approved commitment to the conservative financial policy, with unadjusted net debt/EBITDA and EBITDA interest cover to remain below 2.5x and above 7x, respectively.

We see Sibur's end-2014 leverage of 4.2x debt/EBITDA (including Moody's standard adjustments) as temporary, reflecting a few one-off developments, including local currency shocks, which caused some distortion to the company's rouble based reporting, and the deferred payment to Rosneft for YGPP (executed in early April 2015).

However, we note the risk of potentially reduced capex flexibility at later stages of ZapSibNeftekhim project implementation leading to growth in negative free cash flow and debt funding needs.

Liquidity

Overall, we expect Sibur to maintain a good liquidity profile over the next 18 months through June 2016. We expect Sibur to continue generating operating cash flows of around $2.2 billion in dollar terms, which together with cash balances of around $490 million at end-2014 and availabilities under long-term credit facilities for general needs, will be sufficient to meet its basic obligations (including debt maturities, the payment for YGPP due to Rosneft, maintenance capex, and dividend payments) of approximately $3 billion.

We positively note that in December 2014, Sibur signed agreements with a consortium of European banks on committed facilities in the amount of Euro1.6 billion covered by Euler Hermes to finance EP contracts with German engineering companies under ZapSibNeftekhim project.

Rating Outlook

The outlook on Sibur's rating is negative, reflecting Sibur's exposure to the deteriorating Russian operating environment, which is also captured by the negative outlook on Russia's government bond rating. The negative outlook also takes into account potential erosion of Sibur's capex flexibility as the company progresses with ZapSibNeftekhim investment project implementation. We will also be monitoring the company's ability to address increasing country and foreign exchange risks.

What Could Change the Rating - Down

The rating is likely to be downgraded if (1) the Russian operating environment deteriorates further resulting in further downgrade of the sovereign rating and/or lowering the sovereign ceiling; (2) in our view, Sibur's EBITDA margins may decline to below 25% and/or the company is unable to deleverage over the next 18 months towards around 2.0x debt/EBITDA and maintain RCF/net debt at above 20%; and/or (3) Sibur's liquidity deteriorates.

What Could Change the Rating - Up

Given the deteriorating operating environment in Russia and pressure on the sovereign credit quality, upward pressure on Sibur's rating is unlikely at present.

Other Considerations

We consider Sibur's rating in the context of the key rating drivers cited in our Global Chemical Industry rating methodology, published in December 2013. Based on Sibur's historical metrics, the methodology's grid-indicated rating maps to a level a notch above the current rating, reflecting Russia's country risk. The gap may even increase by one notch over the next 12-18 months as Sibur will likely strengthen its financial metrics based on its low cost base, export potential and capex flexibility.

Rating Factors

Sibur Holding, PJSC

Chemical Industry Grid [1][2]	**Current FY 12/31/2014**		[3]**Moody's 12-18 Month Forward ViewAs of 4/8/2015**	
Factor 1 : Scale (20%)	**Measure**	**Score**	**Measure**	**Score**
a) Revenues (USD Billion)	$9.6	Baa	$6.7	Baa

b) PP&E (net) (USD Billion)	$6.1	Baa		$6 - $6.5	Baa
Factor 2 : Business Profile (20%)					
a) Business Profile	Baa	Baa		Baa	Baa
Factor 3 : Profitability (10%)					
a) EBITDA Margin %	22.0%	Baa		28% - 32%	A
b) ROA - EBIT / Average Assets	8.3%	Ba		10% - 12%	Baa
Factor 4 : Leverage & Coverage (30%)					
a) Debt / EBITDA	4.2x	B		2.2x	Baa
b) EBITDA / Interest Expense	8.5x	Baa		10.3x	Baa
c) Retained Cash Flow / Debt	26.3%	Baa		31% - 34%	A
Factor 5 : Financial Policy (20%)					
a) Financial Policy	Baa	Baa		Baa	Baa
Rating:					
a) Indicated Rating from Grid		Baa3			Baa2
b) Actual Rating Assigned					Ba1

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] As of 12/31/2014; Source: Moody's Financial Metrics [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures.

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