

January 30, 2020

ACRA affirms BBB-(RU) to PJSC Evropeyskaya Elektrotekhnica, outlook Stable

Lead analysts:

Anastasia Malyugina, Associate
Director
+7 (495) 139-0480 ext. 192
anastasia.malyugina@acra-
ratings.ru

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

Key rating assessment factors

The credit rating of [PJSC Evropeyskaya Elektrotekhnica](#) (hereinafter — Evropeyskaya Elektrotekhnica, the Company, or the Group) is based on good profitability, high debt coverage and liquidity as well as low leverage. At the same time, ACRA points to the lower than average size of the Company's business as compared to the largest Russian companies, its medium cash flow, and assesses its market position as modest in view of the high granularity of the Russian engineering market.

Evropeyskaya Elektrotekhnica is one of Russia's leading companies in terms of production of energy and power supply systems, lighting and low-current systems. Since its creation in 2004, Evropeyskaya Elektrotekhnica has transformed from a trading company into a full-fledged engineering one with its own production facilities (40% of products and equipment sold by the Group are manufactured using its own production facilities). In 2018, the Company purchased oil and gas production facilities in the Republic of Bashkortostan. In the nine months of 2019, the Company's revenues ran into RUB 2.6 billion (-1.5% compared to the same period in 2018) with simultaneous growth of FFO before fixed charges and taxes to RUB 348.3 million (a 1.6x increase), which was driven by focusing on high-margin business lines. The Group's future development plans are related to the launch of a new high-margin business, lease of innovative oil and gas equipment.

Moderate assessment of operating risk profile. The market share of Evropeyskaya Elektrotekhnica does not exceed 0.5%. However, it occupies a leading position in some sectors (up to 25% of the market for hot-dip galvanized reinforced cable systems and cable holders for ultra-deep mines). The Group's order book covers from one to two years of its operations; occasionally, some contracts may be postponed for a few months, which may result in a loss of revenues in a given period. However, the potential effect from postponing contracts will not exceed 10% of the revenues, in ACRA's opinion, owing to a good diversification of the order book by customers. The Company's target markets exhibit moderate cyclicity: the electric power industry is currently undergoing an investment pause, which drives up the share of revenues from oil and gas (48% for the nine months of 2019) as well as chemical and food industries (28% in the above period) in total revenues of the Company. Dependence on subcontracting and components is assessed as moderate, in general: dependence on subcontracting is minimal (less than 3%), and the resale of components and equipment accounts for up to 60% of revenues. Local project offices (with some of them classified as related parties operating under an agent agreement and not consolidated within the Group) generate orders and expand the Company's presence in the key consuming regions. Geographical diversification of production sales markets is at a moderate level, with around 10% of production being exported, mainly oil production and refining equipment.

Moderate level of corporate governance. The Group's strategy is sufficiently formalized; it is approved by the board of directors; it is, however, subject to significant changes from time to time in response to the developments in external factors and the market environment. The strategy includes reaching the key financial and operating targets by 2021. The strategy implies a substantial increase in the higher-margin business line's share (equipment manufacturing for oil and gas and hydrocarbon processing industries) in the Group's total revenues. The risk management system of Evropeyskaya Elektrotekhnica is assessed as moderate: the FX and interest rate exposure is minimal, while the purchase of components in overseas markets is offset by export revenues (natural hedge).

ACRA notes that the Company's board of directors (six members) is exposed to the key-man risk. In view of this and considering the involvement of independent directors in the

Company's day-to-day operations, ACRA assesses the corporate governance quality as moderate. The structure of the Group is complicated but justified by the nature of its business. It is worth noting the existence of related-party transactions, the size of which, however, is insignificant in the total operations of the Group. ACRA assesses the Company's level of financial transparency as high: financial reporting is published on a quarterly basis, and regular meetings with investors are held, at which information on the Group's current operations and development plans is disclosed.

Lower than average business size and high profitability. ACRA estimates FFO before fixed charges and taxes at RUB 445 million in 2019. The Agency forecasts that the weighted average value of this indicator will be RUB 500-550 million in 2016-2021 given the Company's entry into the oil and gas sector. In the same period, FFO margin before interest and taxes will average 14.5%. This figure will be achieved thanks to the growth in profitability buoyed by the increase in the share of oil and gas equipment in the Company's sales structure. Evropeyskaya Elektrotekhnica has available credit lines worth RUB 750 mln, the majority of which, however, expire within 2020; credit lines are either extended or replaced with new ones immediately before the expiry. ACRA assesses the quality of liquidity as moderate. The Company has the opportunity to raise funds not only in the debt market, but also use equity financing.

According to ACRA estimates, the Group's net cash flow will be positive in 2019-2021, even considering the payment of dividends of at least 20%. At the same time, the share of capital expenditure in total revenue will be low, which, however, ACRA believes to be reasonable in view of the current business development strategy.

Low leverage and a high level of debt service. The Company currently has no significant external debt obligations. Given the change in its development strategy, ACRA expects that Evropeyskaya Elektrotekhnica's debt burden, weighted between 2016 and 2021, will be 0.5x (the ratio of total debt to FFO before net interest payments). Debt service costs will be at a very high level in the same period thanks to low interest rates.

Key assumptions

- The forecast period includes figures for 2019-2021 with weights of 30%, 15% and 5%, respectively;
- The 2020 revenues from the oil and gas segment are estimated at RUB 1.5 bln, and RUB 4.9 bln in 2021;
- Maintaining EBITDA margin in the electrical and classic oil and gas equipment segments at 11-12% and 21-23 % respectively in the forecast period;
- EBITDA margin in the innovative oil and gas equipment lease segment of at least 50%.

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:

- Increase in the estimated FFO before net interest payments and taxes above RUB 500 million;
- Increase in the actual annual FFO margin before interest and taxes above 15%;
- Increase in the average weighted FCF margin above 5%.

A negative rating action may be prompted by:

- Decrease in FFO margin before interest and taxes below 5% coupled with simultaneous growth in the debt burden (the ratio of total debt to FFO before interest and taxes) above 1.0x;
- Simultaneous decline in the short-term liquidity indicator below 1.5x, deterioration of debt service quality (FFO before net interest payments to interest payments) below 5.0x, decrease in FCF margin below 2%, and growth in the share of capital expenditure in total revenue above 5%.

Rating components

SCA: bbb-.

Adjustments: none.

Issue ratings

There are no outstanding issues of the Company's financial debt instruments.

Regulatory disclosure

The credit rating has been assigned under the national scale for the Russian Federation and is 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 credit rating of PJSC Evropeyskaya Elektrotekhnica was first published by ACRA on October 11, 2018. The credit rating and its outlook are expected to be revised within one year following the publication date of this press release.

The assigned credit rating is based on data provided by PJSC Evropeyskaya Elektrotekhnica, information from publicly available sources, as well as ACRA's own databases. The credit rating is solicited, and PJSC Evropeyskaya Elektrotekhnica participated in its assignment

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

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

(C) 2020

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.

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.