

May 8, 2018

Lead analysts:

Elena Anisimova, Expert  
+7 (495) 139-0486  
elena.anisimova@acra-ratings.ru

Andrey Piskunov, Senior Director  
+7 (495) 139-0485  
andrey.piskunov@acra-ratings.ru

## Key rating assessment factors

# ACRA affirms A(RU) to the Republic of Sakha (Yakutia) and its bonds, outlook downgraded to Negative, and withdraws rating on repurchased bond

ACRA has downgraded the credit rating outlook for the [Republic of Sakha \(Yakutia\)](#) (the Region) to Negative based on a possible failure to collect budget revenues under the current macroeconomic conditions and a change in the Region's debt policy against ACRA's expectations actual at the rating assignment date.

The Republic of Sakha (Yakutia) is a part of the Far-Eastern Federal District and the largest region of Russia in terms of area. The Republic occupies almost one fifth of Russia's territory and is located in the Extreme North area. 0.7% of Russia's population live in the Region, and around 1.2% of the total GRP of Russian regions is generated in the Region.

**Mining industry behavior and natural and climatic conditions determine the Region's economy.** The largest diamond deposits, as well as gold and fossil fuels deposits are located in the Region. The mining industry accounts for up to a half of the Region's GRP. Diamond mining and extraction of crude oil have the highest share in the mineral production structure. Harsh climate limits social and economic development in the Region as well as diversification of its economy.

**Failure to collect taxes in 2018 and beyond may affect the regional budget<sup>1</sup>.** The regional budget depends largely on the performance of major taxpayers, i.e. mining companies, including the CGT members, who, in their turn, depend on the commodity market conditions and the foreign exchange rates. In 2017, the profit tax collections amounted to 82% of the planned tax amount (as amended). Tax expectations turned out to be overestimated, which is a result of the overestimated foreign exchange rate indicated in the Social and Economic Forecast for the Russian Federation for 2017–2019 and certain tax refund claims. Taking into account certain budget indicators for 2018, ACRA is of the opinion that there are risks of declining tax earnings, which may push up the debt burden (amid limited possibilities to apply cash balances). Although, in 1Q2018, the largest mining company of the Region showed record revenue, ACRA notes that the revenue was generated largely due to the sale of stocks, and therefore ACRA conservatively assesses budget tax revenues by the end of the year. The share of mandatory budget expenditures has been slowly increasing and, at the end of 2017, it amounted to 76% of the total expenditures. The share is expected to remain unchanged in 2018. At the end of 2017, the operating balance was low (16% of regular revenues) and it is expected to reach 20%, provided that taxes are collected as planned.

**The decision not to participate in the budget loans restructuring program and the failure to comply with the two agreements with the Ministry of Finance of Russia have led to the need for early substitution of budget debt by market loans.** The Region does not participate in the budget loans restructuring program due to the restrictions contemplated by the terms of restructuring agreements, and the Region has decided to stick to the existing budget loan agreements concluded with the Ministry of Finance of Russia in 2015–2016. In 2017, the Region failed to meet the ratio of debt to tax and non-tax revenues under two budget loans of RUB 3.3 billion obtained in 2017, therefore, such loans are to be prepaid and refinanced by market instruments. This will increase the Region's interest expenses, but will not affect the debt service ratio in the long term, provided that budget loans are regularly substituted by bond issues or bank loans with comparable maturities. Nevertheless, due to the risk of failure to collect taxes

<sup>1</sup> Budget indicators were analyzed excluding the transfers from RusHydro PJSC in 2017–2020 under the program aimed at the attainment of base tariffs in the Far East Federal District.

and the need to prepay a part of budget loans, other Region's debt load indicators may deteriorate relative to the expected figures. At the end of 2018, the Region's debt will amount to 1.62x of the operating balance. The operating balance after interest will be 2.5 times higher than the volume of debt repayments in 2018. A negative rating effect is caused by overdue payables accrued due to insufficient tax revenues in 2017. About a quarter of the Region's debt portfolio are guarantees issued for public sector enterprises. Taking into account the social importance and financial condition of public sector enterprises, the Agency considers it expedient to take into account the some of their debts as indirect obligations of the Government of the Region. According to ACRA estimations, at the end of 2017, the debt of such enterprises amounted to RUB 13.7 billion.

## Key assumptions

- The Region's economy will continue to depend on the key mining sector;
- Low volatility of gratuitous funding from the federal budget in the forecast period;
- The Region will maintain a well-balanced debt policy in the forecast period, including long-term loans with comfortable maturities.

## Potential outlook or rating change factors

**The Negative outlook** assumes that the rating may be downgraded within the 12 to 18-month horizon.

### A positive rating action may be prompted by:

- A countercyclical budget spending policy;
- Coverage of overdue payables out of own funds;
- Growth of tax revenues following a launch of large investment projects.

### A negative rating action may be prompted by:

- A failure to collect taxes planned as of the rating analysis date;
- Further growth of overdue payables;
- A change in debt policy and temporal debt structure;
- Deterioration of financial position of public sector enterprises and the need to provide unplanned support.

## Issue ratings

**Credit rating rationale.** The below listed bond issues by the Republic of Sakha (Yakutia), in ACRA's opinion, have a status of senior unsecured debt, with their credit ratings corresponding to the credit rating of the [Republic of Sakha \(Yakutia\)](#).

[Republic of Sakha \(Yakutia\), 35006 \(ISIN RU000A0JUQH4\)](#), maturity date: July 02, 2021, issue volume: RUB 2.5 billion — **A(RU)**.

[Republic of Sakha \(Yakutia\), 35007 \(ISIN RU000A0JVEH8\)](#), maturity date: May 14, 2020, issue volume: RUB 5.5 billion — **A(RU)**.

[Republic of Sakha \(Yakutia\), 35008 \(ISIN RU000A0JWGT6\)](#), maturity date: May 18, 2021, issue volume: RUB 5.5 billion — **A(RU)**.

[Republic of Sakha \(Yakutia\), 35009 \(ISIN RU000A0JXR43\)](#), maturity date: May 16, 2024, issue volume: RUB 5.0 billion — **A(RU)**.

The A(RU) rating on the bond (ISIN RU000A0JTVM6) issued by the Republic of Sakha (Yakutia) has been withdrawn without affirmation in view of the bond redemption on April 24, 2018.

## Regulatory disclosure

The credit ratings have been assigned to the Republic of Sakha (Yakutia) and to bonds issued by the Republic of Sakha (Yakutia) (RU000A0JTVM6, RU000A0JUQH4, RU000A0JVEH8, RU000A0JWGT6, RU000A0JXR43) under the national scale for the Russian Federation based on the [Methodology for Credit Ratings Assignment to Regional and Municipal Authorities of the Russian Federation](#) 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 issues.

The credit ratings assigned to the Republic of Sakha (Yakutia) and to the bonds of the Republic of Sakha (Yakutia) (RU000A0JTVM6, RU000A0JUQH4, RU000A0JVEH8, RU000A0JWGT6, RU000A0JXR43) were first published by ACRA on November 08, 2017. The credit rating and credit rating outlook of the Republic of Sakha (Yakutia) and the credit ratings of the bonds of the Republic of Sakha (Yakutia) (RU000A0JTVM6, RU000A0JUQH4, RU000A0JVEH8, RU000A0JWGT6, RU000A0JXR43) are expected to be revised within 182 days following the rating action date (May 04, 2018) in accordance with the [2018 calendar of planned sovereign credit rating revisions and publications](#). The credit rating on the bond (RU000A0JTVM6) of the Republic of Sakha (Yakutia) was withdrawn on May 04, 2018.

The credit ratings were assigned based on the data provided by the Republic of Sakha (Yakutia), information from publicly available sources (the Ministry of Finance, the Federal State Statistics Service, and the Federal Tax Service), as well as ACRA's own databases. The credit rating is solicited, and the Government of the Republic of Sakha (Yakutia) participated in its assignment.

No material discrepancies between the data provided and the data officially disclosed by the Republic of Sakha (Yakutia) in its financial report have been discovered.

ACRA provided no additional services to the Government of the Republic of Sakha (Yakutia). No conflicts of interest were discovered in the course of credit rating assignment.

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Analytical Credit Rating Agency (Joint-Stock Company), ACRA (JSC)  
75, Sadovnicheskaya embankment, Moscow, Russia  
www.acra-ratings.com

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