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State Company Russian Highways

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Key rating assessment factors

Credit rating components	
SCA	No
Support	
State support	On par with RF minus 2 notches
Credit rating	AA(RU)

The credit rating of [State Company Russian Highways](#) (hereinafter – the Company, or Avtodor) is based on the decisive state influence on Avtodor's creditworthiness: absolute operational and financial control over the Company on the part of the state, as well as state financing of the major part of the Company's development program. Avtodor is of high systemic importance for the state; however, the Agency notes that the degree of the Company's systemic importance is not ultimate due to the limited impact of Avtodor's potential default on the entire economy.

High systemic importance. Although Avtodor is not the only entity that builds and operates toll highways, the Company acts as the federal government's principal agent in the sphere of toll highway development and currently it operates the major part of toll federal highway sections. The Agency assesses the Company's strategic importance as high due to the fact that transportation infrastructure is among top priorities of the state economic policy. Although Avtodor's potential default would not entail serious risks for the entire economy, it is still associated with significant reputational and financial risks for the state, taking into account the latter's direct responsibility under the concession agreements. ACRA points out that, in case of an economic downturn, the Avtodor's development program may be curtailed; however, the Agency expects that the state will provide the Company with funds sufficient to maintain its creditworthiness.

Very strong state influence on the Company's creditworthiness. The Company was founded in pursuance of a federal law and enjoys a special legal status. The state is Avtodor's sole owner, which exerts an absolute operational and financial control over the Company. The Supervisory Board of the Company incorporates representatives of various government departments (including the Ministry of Transport, the Accounts Chamber, the Council of the Federation, and the Ministry of Finance). The Supervisory Board approves strategy and development program of the Company, which are subsequently approved by the Government, and provide the basis of Avtodor's activities.

The Company is financed primarily out of the federal budget and state funds, in particular, the Investment Fund of the Russian Federation, and the National Welfare Fund of the Russian Federation. Subsidies are included into the federal budget in accordance with the Company's development program approved by the Government and these funds are channeled into Avtodor's capex, organization of its activities, and debt refinancing. The amount of subsidies is determined on a custom-made basis for each project, with traditional preponderance of budget funds over private financing in relation to projects marked by high capital intensity, or social significance. The decision to raise commercial financing is made only after approval of federal budget expenditures. The Agency notes the Company's limited ability to obtain extraordinary budget financing due to a time-consuming program revision procedure and mandatory alteration of the federal budget. Despite the gradual growth of Company's own income via toll collections (RUB 7 bln in 2016), the Agency does not expect the degree of Avtodor's dependence on budget financing to significantly decrease as, by ACRA estimates, this type of income will make up no more than 16% of total income by end-2020.

Comfortable funding structure and adequate liquidity. The Agency highlights Avtodor's adequate liquidity – as of January 1, 2017, the Company had RUB 15.4 bln in cash, of which only RUB 2.3 bln was held on the Federal Treasury accounts, with the rest being deposited in state-owned banks. The Company's funding structure is well-balanced. The total amount of investments estimated for 2017–2020 amounts to RUB 1 trillion, of which 60% is planned to be financed by the federal budget and the National Welfare Fund, 30% is to be raised from investors and through market bond placement, and 10% will be obtained via tolling and Company's own activities.

As of the date of this report, the Company issued bonds for RUB 31.7 bln, including a RUB 10 bln market bond issue maturing in November 2020, and a RUB 21.7 bln bond issue maturing in April 2042 that was purchased at the expense of the National Welfare Fund. According to the current borrowing plan, in 2017–2020, the Company plans to place up to RUB 227 bln in bonds, of which about RUB 99 bln will be attributed to market borrowing. Despite the absence of explicit state guarantees pertaining to existing and future market-originated debt as well as the lack of formal state guarantees related to Avtodor's obligations (Federal Law N 145-FZ), the Agency expects that, under the Company's operations program, its principal debt and at least 50% of coupon payments will be serviced at the expense of the federal budget. At the same time, ACRA highlights that, after 2020, the Company plans to gradually transit to debt servicing out of its own incomes, which will entail additional risks for the creditors.

Key assumptions

- Retaining current amounts of subsidies allocated from the federal budget;
- Debt servicing at the expense of the federal budget (principal debt and at least 50% of coupon payments).

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:

- An increase in the Company's systemic importance for the state and significant expansion of its functions.

A negative rating action may be prompted by:

- A material decline in allocated budgetary subsidies, specifically those related to debt servicing;
- A decrease of Avtodor's systemic importance, in particular due to transferring its functions to other market players.

Brief information about the Company

Avtodor is the largest Russian toll highway operator. The Company was established in 2009 by virtue of Federal Law N 145-FZ. Avtodor aims at developing the major highway network via various public and private partnership mechanisms, and the Company's main projects include development of such federal highways as M-1 "Belarus," M-4 "Don," M-11 "Moscow–Saint Petersburg," and the Central Ring Road of Moscow (CRR). The current Avtodor's portfolio is comprised of 16 projects (four of which are operational) with total value exceeding RUB 800 bln (of which 24% being received from private investors). The group includes nine subsidiaries, which maintain Avtodor's activities, in particular, in segments of tolling, property management, investment projects support and others.

Rating assessment factors

Assessment of relationships with the state

State Company Russian Highways was established by the Russian government in order to provide public services and perform other management functions in respect of federal road infrastructure. Such road infrastructure includes existing federal highways transferred to the Company under asset management arrangements, and motorways being constructed by the Company. The Company is assigned a special legal status, therefore it may not be wound up unless a relevant federal law is adopted. There are other toll road

Systemic importance is assessed as high.

builders and operators, but the Company is a key agent of the federal government tasked with the development of highways, and, currently, the Company operates most toll sections of federal highways. ACRA assesses the strategic importance of the Company as high, because the development of transport infrastructure is one of key priorities of the state economic policy.

The degree of state influence is assessed as very strong.

The government exercises operational and financial control over the Company. The key managing body of the Company is the Supervisory Board, which approves corporate strategy, development program, and operating and financial plans. The Supervisory Board consists of twelve members and includes representatives from various governmental bodies, including the Ministry of Transport, the Audit Chamber, the Federation Council, and the Ministry of Finance. The Russian Government appoints seven members of the Supervisory Board, the Federal Assembly appoints four members, and the Audit Chamber appoints one member. The Supervisory Board established the following committees: the Strategic Planning and Development Committee, the Audit Committee, the Budgeting and Finance Policy Committee, and the Remuneration Committee. ACRA assesses the Company's corporate governance as adequate.

The main document regulating the operations of the Company is the *Long-Term Operations Program (for 2010–2020)* approved by the Russian Government. The Program establishes the key development areas and targets for the Company and funding sources for each project. The Program serves a basis for annual budget and triennial financial plan of the Company. The Program may be subject to adjustments initiated generally by the Company's investment policy department and approved by the Supervisory Board and then by the government.

Federal budget subsidies are the main funding source of the Company. There are three types of subsidies: for asset management purposes, for road construction and reconstruction, and for own operations of the Company. The total amount of subsidies received in 2010–2016 is over RUB 550 billion (i.e. over RUB 80 billion annually). The amount of each subsidy is determined individually for each project, taking into account the capital intensity, social significance and finance structure. The decision to attract commercial finance may be taken only after the federal budget expenditures are approved. According to the current practices in the Company, any project of high capital intensity or social significance is financed out of subsidies from the federal budget. Despite the gradual growth of Company's own revenue sources in the form of road tolls (about RUB 7 billion or 6% of total revenues in 2016), the Agency does not expect a significant decrease in the Company's dependence on the budgetary funding as, according to ACRA estimates, road tolls will form not more than 16% of the total revenues of the Company by late 2020.

The Agency notes that Avtodor has no significant sources of extraordinary funding. If project costs are higher than originally planned, the Company has to introduce changes to its operations program. Such changes are not only subject to approval by the Company's supervisory board and the RF Government, but also require changes in the federal budget, which, in turn, may take a lot of time. It is worth noting that there have been such cases of increased project costs, in particular, in respect to the 15–58 km section of the federal route M-11 "Moscow-Saint Petersburg."

For federal budget funds included in the Company's operations program to be transferred to the Company, Avtodor and the Ministry of Transport of Russia annually conclude agreements on granting state subsidies. Subsidies are transferred to accounts in the Federal Treasury, and the funds are spent on clearly established targets only, which is controlled by the Federal Treasury. Undrawn funds can be carried forward to the next calendar year, however, for the same purposes only. Temporarily free cash flows from own activities, as well as funds raised as part of bond placement, are placed on deposits and settlement accounts with state-owned banks (usually Sberbank, VTB and Gazprombank).

The Agency notes significant risks the state may face in the event of a potential default of the Company. Despite the fact that the state is formally not liable for the Company's obligations (according to Federal Law No.145-FZ) and a potential default of Avtodor will not be associated with significant risks to the national economy, it may cause significant reputational and financial risks for the state, taking into account the state's direct responsibility under concession agreements. The Agency notes that, in the event of a significant deterioration in the economic environment, the Company's operations program may be reduced, but, according to Avtodor, in case funding is reduced, unlaunched projects are deferred first, while the funding of current projects remains unchanged. Moreover, concession or long-term investment agreements are subject to a "special circumstances regime" (Federal Law No.115-FZ), which includes penalties in case of a breach of funding obligations. Therefore, the Agency expects that in the event of a deterioration in the economic situation, the state will provide funds sufficient to support the Company's creditworthiness.

Projects

The Company's strategy is in line with the Transport Strategy of the Russian Federation until 2030 and implies formation of a backbone network of high-speed freeways by 2030. One of the strategy goals is to improve the radial road system through creating chord roads between million-plus cities and prospective economic growth zones. By 2030, the total length of new roads to be constructed and reconstructed by the Company can reach up to 12,000 kilometers. In accordance with the current Avtodor's long-term operations program (for 2010-2020), the total length of roads under the Company's management should be equal to 3,905 km (including 1,788 km of toll roads) by 2020.

As part of its investment activities, Avtodor applies five different arrangements of public-private partnerships, including: concession agreements with direct collection of payments and concession agreements with concessionaire charges; long-term investment agreements, as well as investment agreements at the pre-project stage and operator agreements. Concession agreements imply the longest terms (20-30 years) and maximum involvement of the investor in the project (usually over 25% of the project costs). An important distinctive feature of concession agreements is full responsibility of the state for obligations of the Company. Long-term investment agreements are similar to concession agreements in many respects, but investor participation is relatively small (10-15%) and state responsibility is excluded. Pre-project investment agreements and operator agreements imply attracting investors as contractors for engineering surveys and pre-design works, and maintenance, repair and operation of roads. Under each agreement, except for concessions with direct collection of fees, the risk of traffic always lies with the Company.

The main projects implemented by the Company include federal routes M-1 "Belarus," M-4 "Don," M-11 "Moscow-Saint Petersburg" and the Central Ring Road. The current portfolio consists of 16 projects (including four roads put into operation), including mainly construction of new toll roads with a total length of over 1,750 kilometers. The total costs of existing projects exceeds RUB 800 billion, with the 24% share of private investments. The most common form of public-private partnership the Company is involved in is a long-term investment agreement (currently, nine of eleven contracts), while the Company's portfolio contains only five concession agreements.

The Agency notes that some Avtodor projects were postponed, in particular, tenders for the third and fourth sections of the Central Ring Road, caused by the limited investor demand for the Company's projects in 2015-2016. According to the annual report, in 2015, the Company attracted investments for only RUB 2.6 billion (10.4% of the planned volume), in 2016 — RUB 4.6 billion (10.8% of the planned volume). In the Agency's opinion, the delay in project implementation is associated with a potential risk of growing project costs due to inflation, which may require a review of the Avtodor operations program. At

the same time, ACRA assesses this factor as neutral for the Company's creditworthiness, as Avtodor's funding scheme is structured in such a way that the decision to raise investments is made only after the federal budget expenditures are agreed, and bond loans are placed after private investments are attracted. In such a way, the Company synchronizes cash flows and deadlines under each project to reduce the risks of underfunding.

Avtodor actively uses bank guarantees in order to minimize project risks. Thus, according to the Contractual Work Regulations of the Company, all advances paid to contractors and at least 10% of the total contract amounts shall be covered by bank guarantees. The maximum amount of advance payment may not exceed 30% of contract value, with all advance payments exceeding 10% are subject to approval by the Company's management. The Company applies standard industry forms (KS-2 and KS-3) in monitoring work progress and accepting deliverables.

Financial profile

According to the long-term operations program of the Company (2010–2020), the total investments are estimated at RUB 1.0 trillion (for 2017–2020), of which RUB 598 billion is planned to be financed from the federal budget and the National Wealth Fund, RUB 298 billion to be attracted from private investors and through market bond issues, and RUB 110 billion to be received in the form of road tolls collected and own activities.

The Agency assesses the financial transparency of Avtodor as acceptable: the Company prepares consolidated IFRS financial statements on a semi-annual basis (the auditor is a Russian audit company). The reporting of the Company reflects its lines of business: the main asset is investments in road construction and reconstruction, which, as of December 31, 2016, amounted to RUB 279.5 billion (75% of assets); another RUB 70.4 billion (19% of assets) account for advances paid to contractors. The own capital, taking into account subsidies received from the federal budget, amounts to RUB 316.3 billion (85% of liabilities). The borrowed funds amount to RUB 47.4 billion and include bond loans and obligations to investors under investment agreements. The Agency notes an adequate liquidity of the Company: as of January 01, 2017, cash funds amounted to RUB 15.4 billion, of which only RUB 2.3 billion was held on the accounts in the Federal Treasury, and the remaining funds were held in state-owned banks.

As of May 31, 2017, the volume of bonds issued by the Company amounted to RUB 31.7 billion, including a market bond issue for RUB 10 billion (to mature in November 2020) and bonds purchased at the expense of the NWF for RUB 21.7 billion (to mature in April, 2042) (with a coupon grace period until 2022 and repayments starting in 2032). In November 2016, Avtodor repaid, out of its own revenues, a previous bond issue for RUB 3 billion. According to the current borrowings plan, in 2017–2020, the Company is expected to issue bonds for the amount of up to RUB 227 billion, of which RUB 128.3 billion will be purchased at the expense of the National Welfare Fund, and RUB 98.5 billion will constitute market borrowings that the Company plans to attract for a term of up to three years. The Agency notes that there are no government guarantees for the current RUB 10 billion issue, and Avtodor does not plan to recourse to such guarantees for future market bond issues.

At the same time, according to the long-term operational program of the Company until 2020, the entire principal and 50% of coupon payments under current and planned bond issues are planned to be repaid from the federal budget.

Despite a moderately low mid-term credit risk in respect of market borrowings, the Agency notes that, with the growth of own incomes, the Company intends to gradually transit to debt servicing on account of own sources of funds (after 2020). For example, in 2022, Avtodor plans to make, out of its own funds, deferred coupon payments under the RUB 21.7 billion bond issue. The expected transition to debt servicing using own funds will

create additional risks for the Company's creditors in the event Avtodor receives less than planned own revenues or in case of a delay in its projects.

The Agency notes that the Company is not exposed to currency risks, because the entire amount of funds raised by Avtodor and most investment project costs are denominated in rubles. At the same time, the Company is exposed to interest rate risk, as the coupon rate on the bond loan purchased by the NWF is tied to inflation.

Analytical adjustments

None.

Support

State — on par with RF minus 2 notches.

Issue ratings

No outstanding issues have been rated.

Rating history

May 31, 2017 — AA(RU), outlook Stable.

Regulatory disclosure

The credit rating has been assigned under the national scale for the Russian Federation and is based on the [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](#).

A credit rating has been assigned to State Company Russian Highways for the first time. The credit rating and its outlook are expected to be revised within one year following the rating action date (May 31, 2017).

The assigned credit rating is based on the data provided by State Company Russian Highways, information from publicly available sources, as well as ACRA's own databases. The rating analysis was performed using consolidated IFRS financial statements of State Company Russian Highways. The credit rating is solicited, and State Company Russian Highways participated in its assignment.

No material discrepancies between the provided data and the data officially disclosed by State Company Russian Highways in its financial statements have been discovered.

ACRA provided no additional services to State Company Russian Highways. No conflicts of interest were discovered in the course of credit rating assignment.

Appendix

Table 1. Operations Program of Avtodor for 2010–2020*

RUB mln	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2010–2020
Total expenditures, including	64,102	80,576	115,265	109,779	116,210	130,413	125,910	206,265	310,360	223,986	267,918	1,750,783
asset management	4,961	11,260	12,348	13,165	20,263	17,292	22,378	29,627	37,291	48,548	60,586	277,719
road construction and reconstruction	58,643	68,349	101,300	94,601	93,795	110,213	101,162	172,496	270,311	173,266	205,147	1,449,282
own operations	498	967	1,617	2,013	2,152	2,908	2,371	4,143	2,757	2,172	2,185	23,783
Funding sources, incl.	64,155	80,993	115,259	110,307	117,006	131,559	125,674	204,923	309,273	223,986	267,918	1,751,054
federal budget subsidies	44,446	43,503	76,250	94,288	109,967	99,732	100,532	103,667	109,507	114,581	141,913	1,038,386
tolling income	49	513	833	1,525	2,473	3,845	7,143	9,821	17,135	28,861	43,663	115,861
bonds purchased at the expense of the NWF						21,727		40,853	66,466	20,954		150,000
market bonds			3,000				10,000	20,000	26,000	9,500	43,000	111,500
funds from investors	3,778	17,894	20,388	12,496	2,237	2,605	4,567	26,682	88,025	47,918	37,157	263,747
funds from the RF Investment Fund	15,377	17,986	13,074									46,437
own operations	504	1,097	1,715	1,998	2,329	3,649	3,432	3,900	2,139	2,172	2,185	25,123
Shortage/Surplus	53	417	-6	528	796	1,146	-236	-1,342	-1,087	0	0	270
Cumulative	53	471	464	992	1,789	2,935	2,699	1,357	270	270	270	270

* The current version of the Program is approved by the Supervisory Board of Avtodor and sent to the RF Government for endorsement.

Source: Long-Term Operational Program of Avtodor for 2010–2020

Table 2. Borrowings Plan of Avtodor for 2010–2020

RUB mln	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2010–2020
Bond loans, incl.	0	0	3,000	0	0	21,727	10,000	60,853	92,466	30,454	43,000	261,500
funds from the NWF						21,727		40,853	66,466	20,954		150,000
market bonds			3,000				10,000	20,000	26,000	9,500	43,000	111,500
Bond loan repayments, incl.	0	6	293	292	325	363	3,409	1,367	4,056	17,683	50,603	78,396
coupon payments and fees	0	6	293	292	325	363	409	1,367	4,056	7,683	7,603	22,396
principal							3,000			10,000	43,000	56,000
Repayment sources, incl.	0	6	293	292	325	363	3,409	1,367	4,056	17,683	50,603	78,396
federal budget subsidies								513	1,913	13,733	46,698	62,855
asset management		6	293	292	325	363	3,409	854	2,144	3,950	3,906	15,541

Source: Long-Term Operational Program of Avtodor for 2010–2020

Table 3. Balance sheet items

RUB mln	2014	2015	2016
Intangible assets	739	1,277	1,533
Fixed assets	142	187	217
Construction in progress	180,063	238,283	279,514
Other non-current assets	9	174	170
Non-current assets	180,953	239,921	281,434
Inventories	44	121	110
Receivables	71,841	74,789	70,620
Cash	12,301	15,566	15,441
Other current assets	462	6,230	6,716
Current assets	84,648	96,706	92,887
Total assets	265,601	336,627	374,321
Capital	244,830	289,733	316,273
Long-term borrowings	9,932	29,919	44,826
Other long-term liabilities	3,463	3,301	2,257
Long-term liabilities	13,395	33,220	47,083
Short-term liabilities	186	5,550	2,531
Payables	7,073	8,030	8,301
Other short-term liabilities	117	94	133
Short-term liabilities	7,376	13,674	10,965
Total liabilities and capital	265,601	336,627	374,321

Source: Consolidated IFRS financial statements of Avtodor

Table 4. Avtodor projects

Section	Section length, km	Status	Type of PPP	Agreement date	Value, RUB bln*	Agreement term, years	Commissioning	Private capital
M-11 "Moscow-Saint-Petersburg"								
15-58 km	43.0	Operation	Concession	July 2009	59.6	31	Dec. 2014	61%
258-334 km	72.7	Operation	LTIA ¹	December 2011	49.6	23	Nov. 2014	11%
208-258 km	47.9	Construction	LTIA	December 2014	32.3	23	2018	11%
334-543 km	217.0	Construction	LTIA	December 2013	144.6	28	2018	11%
543-684 km	138.8	Construction	Concession	November 2014	76.8	27	2018	25%
58-149 km	89.0	Construction	LTIA	August 2016	74.6	22	2018	10%
Central Ring Road								
1 section	49.5	Construction	LTIA	May 2014	48.9	23	2018	14%
5 section	76.4	Construction	LTIA	December 2014	42.2	24	2018	11%
3 section	105.3	Construction	Concession	September 2016	80.1	26	2019	43%
4 section	96.5	Construction	Concession	June 2017	77.1	26	2019	38%
M-1 "Belarus"								
Odintsovo bypass road	18.5	Operation	Concession	July 2009	25.5	31.5	Nov. 2013	57%
33-132 km	99.5	Preparations	Concession		109.3	34		38%
M-3 "Ukraine"								
124-194 km	71.6	Reconstruction	LTIA	December 2014	17.2	23	2018	11%
M-4 "Don"								
225-633 km	408.0	Operation	Operator	December 2011	6.6	10	Dec. 2015	100%
517-544 km	29.2	Construction	LTIA	December 2013	17.3	23	2017	11%
1091-1319 km	207.4	Construction	Operator	December 2016	7.1	16	2017	40%
633-715 km	85.2	Construction	LTIA	December 2016	62.3	24	2017	10%
M-7 "Volga"								
Balashikha bypass road	69.4	Preparations	Concession		60.9	30		50%

* Prices as of relevant year

Source: Company data

¹ Long-term investment agreement

(C) 2017

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