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State Transport Leasing Company PJSC

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Credit rating components	
SCA factors	
Business profile (weight: 15%)	3
Capital adequacy (weight: 15%)	2
Risk profile (weight: 35%)	4
Funding and liquidity (weight: 35%)	3
SCA	**bb**
Adjustments	
Adjustments	1 notch up to SCA (competitive advantage)
Support	
Group	-
State	On par with RF minus 4 notches
Credit rating	**A+(RU)**
Credit rating outlook	**Stable**

Key rating assessment factors

High likelihood of extraordinary support by the state is attributable to the role STLC (hereinafter, STLC, or the Company) plays in the implementation of the state industrial and transportation development programs. The Company capital was formed through a series of capital injections by the state (over RUB 59 billion in total) used to finance transport vehicle leases granted to certain industries, which the state views as its priorities but whose growth is held back by high costs of corporate funding, long-term and capital intensive nature of the projects. In ACRA's opinion, the likelihood of state support to STLC is high, taking into account growing importance of STLC in the transportation industry of Russia and potential further capital inflow from the government. At the same time, ACRA notes that in case of deteriorating financial standing of the Company, budgetary injections would be high enough but not burdensome for the national economy. The ACRA's opinion about state support is expressed in that the final rating is four notches down against the rating of the Russian Federation.

Adequate business profile is based on the Company's strong standing at the Russian leasing market (STLC is among top five leasing companies in Russia) and the vehicle lease segment. The factor assessment is limited by the business-specific high concentration of the Company's lease portfolio on lessees (as of end-March 2017, ten largest clients comprised 77% of the total lease portfolio) and types of equipment (aviation and railway rolling stock comprised 78% of the portfolio).

Substantial loss absorption buffer is coupled with limited internal capital generation capacity. STLC has a sizable capital cushion due to step-by-step capital increases in 2015–2016 aimed at implementing the SSJ 100 aircraft leasing program and other state-run projects. As of end-March 2017, the Company's capital adequacy ratio (CAR) amounted to 25.5%. We expect more capital increases for the total of RUB 9.3 billion by end-2017 with additional capital injection of RUB 10 billion in 2018 for the purposes of certain state-run programs. STLC's internal capital generation capacity is assessed as low: in 2012–2016, the average capital generation ratio (ACGR) was 9 bps.

Low risk profile. As at end-September 2016, the Company's lease portfolio contained a large share of lease agreements with payments 90+ days overdue: 16.4% including accounts receivable on terminated lease agreements. This year, due to settlement of overdue debts under a number of contracts, the total amount of overdue payments decreased significantly (4.2% at end-March 2017). However, the specifics of the Company's strategy and risk management can potentially result in the increased credit risks. ACRA notes that certain large lessees do not have sufficient cash flow to timely make repayments on the long-term horizon, which may result in restructuring of relevant lease contracts. ACRA also notes that a moderately high share of funding attracted at floating interest rates (about 20% of total liabilities as of the beginning of June 2017) is not properly formalized in lease agreements.

Balanced funding structure. Company's liabilities are well diversified: as at end-March 2017, they included mainly bank loans (25%), finance lease liabilities (16%), and bonds issued (52%). The Company's dependence on certain lenders is moderate: payables due to the largest lender amounted to 16% of the total liabilities of STLC, while payables due to five largest lenders stood at 38%.

Satisfactory liquidity position. Under the ACRA base case scenario (and accounting for STLC's plans to build up its leasing business), the Company shows positive cash balances (the current liquidity ratio is around 1–1.1) at the end of each quarter within the 12 to 24-month horizon. There is no need for significant refinancing of current liabilities throughout this period. Under the ACRA stress scenarios, the Company shows a moderate demand for attracting emergency liquidity (its current liquidity ratio is less than 1 in certain quarterly periods).

STLC plays a crucial supporting role in terms of implementing a number of state-run programs in the transportation sector, which provides the Company with guaranteed demand for its services, mainly in niche segments. ACRA regards this factor as a significant competitive advantage, which is not reflected in the Company's SCA. This translates into a higher creditworthiness, which in turn, results in one notch up to the SCA.

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:

- Increased systemic importance of the Company resulting from growing state funding and higher Company's involvement in the state transportation policy.

A negative rating action may be prompted by:

- Loss of controlling share in the Company by the Russian Federation, or a lower propensity of the controlling shareholder for support the Company;
- Lower systemic importance of the Company for the national economy.

Brief information about the Company

STLC is a single-purpose company focused on finance and operating leasing services of transportation vehicles. As a fully state-owned company, STLC is instrumental in implementation of the state transportation development program that includes certain anti-crisis measures.

In 2016, STLC held the leadership in terms of new business volume and was among top five leasing companies in Russia in terms of lease portfolio size.

Rating assessment factors

Business profile: adequate

The adequate business profile is based on the Company's leading positions in the commercial vehicle lease market and its role of a cornerstone company it plays in a range of state transportation programs implemented in the Russian Federation. The assessment is limited by a high business concentration conditioned by the specifics of the Company and by some shortcomings in the risk management system, which lead, in our opinion, to increased credit risks taken by STLC.

High business sustainability assessment hinges on the strong competitive positions of

STLC in both the Russian leasing market as a whole and the key business lines of the Company:

- Aircraft leasing,
- Rolling stock leasing,
- Ship leasing.

Taking into account the plans envisaged by the development strategy, as well as the current and expected levels of capitalization, we believe that the positions held by the Company will remain stable within the next 12–18 months. Our assessment of this factor is further supported by the Company's role as an instrument of public policy in the Russian transport industry: STLC has priority access to certain leasing segments and also exclusively implements a number of state leasing programs, namely:

- Sukhoi Superjet 100 (SSJ 100) operational leasing program;
- Regional transport energy efficiency programs;
- Ship leasing and ferry development programs;
- Suburban passenger railcar leasing programs.

Due to the fact that the shareholder does not require STLC to maintain a certain level of profitability, the Company is able to operate with a low margin, offering customers more competitive rates.

ACRA assesses the strategy implemented by STLC as sufficiently adequate, taking into account the objectives set forth for it by its shareholder. The Company's activities are subject to a long-term development program, the implementation of which is confirmed annually by an auditor's opinion. The objectives of the first two years of the program (2014–2015) have been achieved in full. ACRA notes that the Company is not restricted in its choice of funded projects, provided that the focus is on priority sectors (their share should not be lower than 75% in the leasing portfolio).

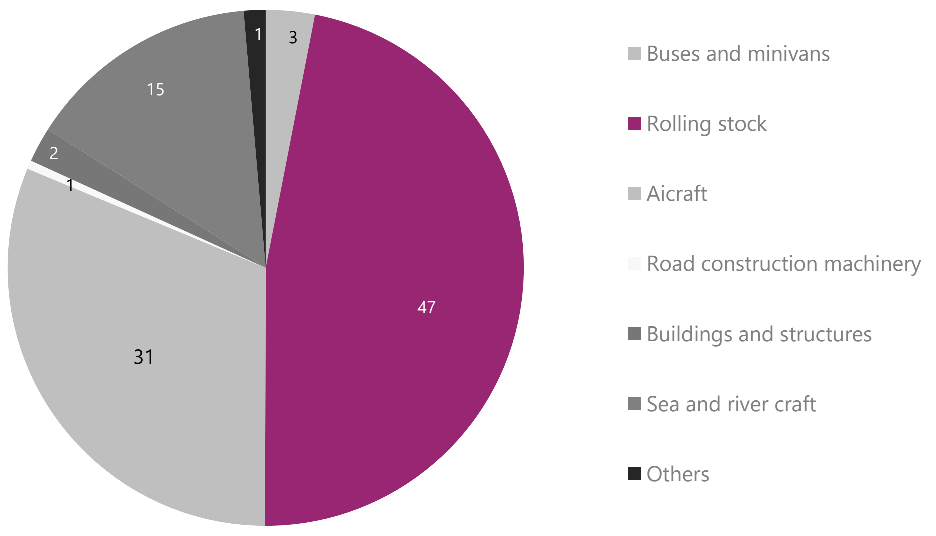
The business profile assessment is limited by the strong concentration of the Company's business on a narrow spectrum of leased items and a small number of lessees (which is caused by the specificity of the Company's activities). As of the end of March 2017, the largest segments — rolling stock leasing and aircraft leasing — accounted for 47% and 31% of the total leasing portfolio,[1] respectively. The liquidity of these segments is estimated by us as medium under current conditions. For other segments (in particular, the ship leasing segment), the level of liquidity is lower than in the aircraft leasing segment. At the same time, the aircraft leasing prospects are largely dependent on the implementation of the SSJ 100 operational leasing program financed from the budget. In the event of a reduction or complete cessation of budget financing, the Company's business is expected to stagnate in this segment, which will affect its market positions and profitability.

We also draw attention to the very high concentration of the leasing business on a small number of clients: as of the end of March 2017, the top ten lessees accounted for 77% of the leasing portfolio.

The corporate governance quality is assessed as adequate as compared to peers. The Agency notes that, before the management team was changed in 2012, the Company made a number of risk management mistakes that resulted in too much non-core assets accumulated on the balance sheet, the majority of which are non-performing. Despite a number of changes that have taken place in the risk management system over the past few years, we underline that there are certain shortcomings in the decision-making process that may lead to increased credit risks taken by STLC.

[1] Total lease payments due

Figure 1. Leasing portfolio profile (1Q2017), %



Source: STLC, ACRA estimates

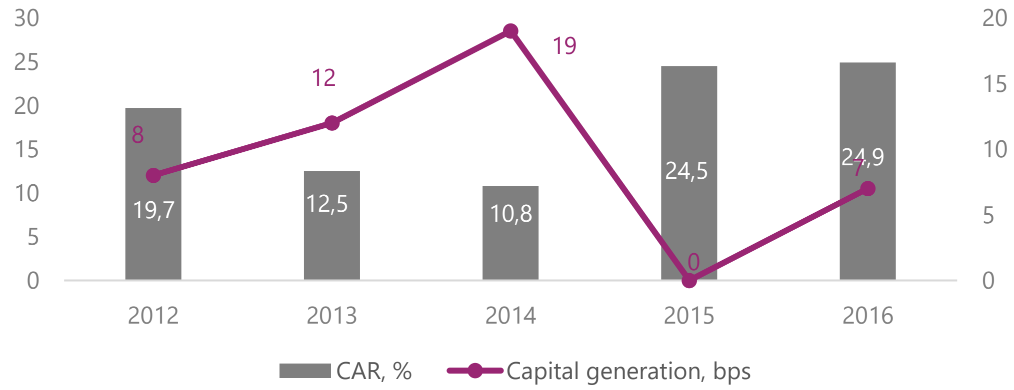
Capital adequacy: adequate

ACRA estimates the capital adequacy of STLC as adequate: a significant capital adequacy margin is combined with a limited capacity to generate capital internally.

The Company has a substantial capital reserve: at the end of March 2017, the capital adequacy ratio (CAR) was about 25.5%, therefore, the Company may absorb potential losses even in the case of the higher-than-the-market-average growth of its business. Such level of capitalization was reached through a phased capitalization made in 2015–2016 for the purpose of implementing the SSJ 100 aircraft leasing program (totaling RUB 34 billion) and other state programs (RUB 13.3 billion). The capital will be increased by RUB 9.3 billion by the end of 2017 with additional increase by RUB 10 billion to follow in 2018 in the framework of other state programs.

The Company's own capital generation capabilities are assessed as weak: the averaged capital generation ratio (ACGR) for 2012–2016 is 9 bps. ACRA notes that the Company's role as an agent for implementing state policy does not imply the profitability to be high.

Figure 2. Capital adequacy and capital generation



Source: STLC, ACRA estimates

Risk profile: weak

As of the end of September 2016, the Company's leasing portfolio contained a high share of contracts with payments overdue for 90+ days (16.4%, including terminated leasing agreements). Certain efforts have resulted in a significant decrease of arrears down to 4.2% (as of the end of March 2017). However, the specifics of the Company's strategy and risk management can potentially lead to increased credit risk taking by the Company. ACRA notes that some large lessees have no cash flows sufficient to make payments timely under lease contracts on the long-term horizon, which increases the likelihood of debt restructuring. In determining the amount of bad debts, the Agency takes into account the total contract amount, since a small amount of arrears often coincides with a prolonged non-payment, which, in fact, indicates the total inability of a lessee to make payments under a contract.

The quality of assets outside the leasing portfolio (funds placed with credit institutions) is assessed as high. The Company does not have any investments in securities or non-core assets.

The Company's market risk exposure is estimated by the Agency as moderate: as of early June 2017, about 20% of liabilities featured floating rates amid absence of corresponding leasing contracts.

The operational risk is insignificant.

Funding and liquidity: satisfactory

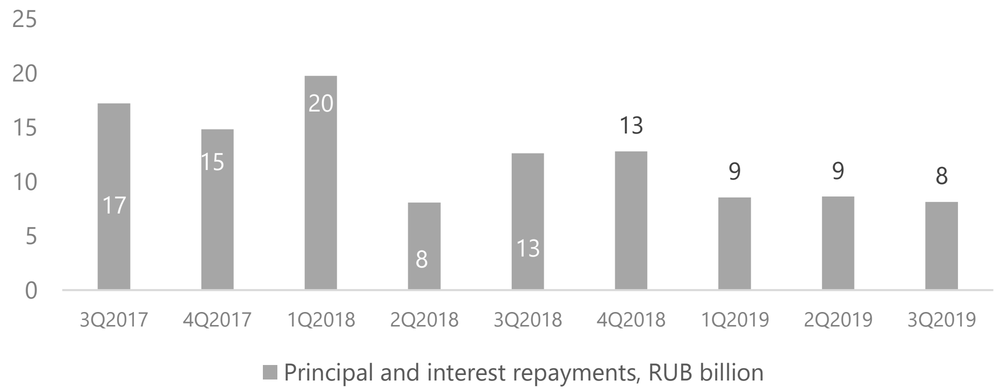
A balanced funding profile is combined with a satisfactory liquidity position.

The Company's liabilities are diversified relatively high: at the end of March 2017, such liabilities included mainly bank loans (25%), financial lease obligations (16%) and bonds issued (52%). The dependence of the Company on individual creditors is moderate: the share of the largest creditor amounted to 16% of the total liabilities, and the share of the five largest creditors was 38%.

In ACRA's opinion, the Company's funding profile will not undergo significant changes in the next 12–18 months, while the Company plans to increase the share of market funding and to reduce the share of bank loans.

The current and forecasted liquidity position is assessed as satisfactory. In the base case scenario of ACRA (taking into account the expected growth of leasing business), the Company has a positive cash reserve (the current liquidity ratio is about 1–1.1) in each quarter on the 12 to 24-months horizon, with no need for significant refinancing of current liabilities. In the stress scenarios of ACRA, the need for emergency liquidity is moderate (the current liquidity ratio is less than 1 in certain calendar quarters).

Figure 3. Debt repayment schedule



Source: STLC

ACRA notes that, except its own cash reserve, STLC has no other sources of emergency liquidity. The Company has no portfolio of liquid securities that could be used to take securities-based loans. Possibilities to obtain emergency liquidity from the shareholder are limited, as unplanned capital contributions would require amendments to be introduced in the federal budget, which are difficult to approve. ACRA does not consider currently undrawn limits under unsecured loans as a source of emergency liquidity, because, in case of deterioration of the financial standing of the Company, such limits may be cancelled fast.

Within the next 18 months, the Company is expected to make a range of large repayments/put options (exceeding 2% of the capital): 1) put options on its local RUB bond issues for RUB 5 billion in September 2017, RUB 4 billion in December 2017, and RUB 4 billion in November 2018; 2) repayment of par under two bond issues for RUB 5 billion each in January 2018; 3) redemption of par under two bond issues RUB 2.4 billion and RUB 4.8 billion in March and September 2018, respectively. The analysis of the forecasted cash flow showed that the risk of non-repayment under the above liabilities is assessed as minimal.

Additional adjustments to SCA: +1 notch

ACRA notes the Company's key role for the Russian Federation in implementing a number of state programs in the transport sector, which provides a guaranteed demand for the Company's services, mainly in the niche segments of the transport industry. The Agency regards this factor as a significant competitive advantage not reflected in the SCA. This leads to a higher level of creditworthiness, which is expressed in an additional rating notch up to the SCA.

Support

Group

The Company is not part of an identifiable group as defined in Methodology for Analyzing Member Company Relationships Within Corporate Groups, which results in no additional support to the SCA.

State

ACRA considers the Company as a state-related entity.

High systemic importance. The systemic importance of the Company is estimated by the Agency as high. The assessment is due to the role the Company plays in the state industrial and transport policy. The Company is the dominant player in the strategically important market of leasing services provided to the transport machine building sector. From the viewpoint of the national transport infrastructure, this sector is a priority for the state, however, high commercial funding costs restrain the sector. The Company's default would endanger a number of transport and engineering sectors and entail reputational risks for the state. At the same time, a deterioration in the financial position of the Company would not have critical consequences for the national economy, although it would require significant capital injections from the budget.

Very strong state influence. ACRA assesses the degree of state influence on the Company as strong, which is based on the 100% shareholding and operating control over the Company on the part of state authorities. The state provides regular financial assistance to the Company in the form of capital inflow from the federal budget (about RUB 59 billion in total). Taking into account the growing role the Company plays in the Russian transport industry and the expected capital injections into the Company, ACRA assesses the likelihood of further state support as high. At the same time, the Agency notes that no extraordinary support procedure exists with respect to the Company.

ACRA's opinion about the Company's systemic importance and the state influence on its creditworthiness is expressed in the final credit rating on par with the RF, adjusted 4 notches down.

Issue ratings

July 25, 2017 — 001R-04 (RU000A0JXPG2), 001R-03 (RU000A0JXE06) and 001R-02 (RU000A0JX199) series certified exchange-traded interest-bearing unregistered bonds — A+(RU).

Rating history

June 26, 2017 — A+(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 Credit Ratings Assignment to Leasing Companies Under the National Scale for the Russian Federation, the Methodology for Analyzing Relationships Between Rated Entities and the State, the Key Concepts Used by the Analytical Credit Rating Agency Within the Scope of Its Rating Activities, as well as the Methodology for Assigning Credit Ratings to Individual Issues of Financial Instruments Under the National Scale of the Russian Federation.

A credit rating has been assigned to State Transport Leasing Company PJSC for the first time. The credit rating and its outlook are expected to be revised within one year following the rating action (June 26, 2017).

The assigned credit rating is based on the data provided by State Transport Leasing Company PJSC, information from publicly available sources, as well as ACRA's own databases. The rating analysis was performed using IFRS consolidated statements of STLC and statements of STLC composed in compliance with RAS. The credit rating is solicited, and STLC participated in its assignment.

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

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

Appendix

Table 1. Consolidated balance sheet items, RUB thousand

	2013	2014	2015	2016
Assets	**82,217,200**	**97,086,111**	**185,203,057**	**232,096,904**
Cash and equivalents	5,485,860	2,777,893	19,627,448	9,494,726
Financial instruments available for sale	1,775,922	-	-	-
Bank deposits	2,000,000	-	60,119	-
Net leasing investments (net of impairment reserve)	53,345,080	55,600,285	42,349,750	70,891,502
Overdue amounts under terminated leasing agreements	1,224,437	1,549,447	2,686,927	8,370,129
Advances issued to suppliers of leased equipment	2,341,404	5,741,837	32,544,252	39,653,900
Derivatives	-	-	-	449,059
Loans issued	-	-	219,929	254,335
VAT receivables	567,965	-	1,242,982	6,592,868
Profit tax receivables	145,424	-	39,248	269,734
Assets in operating lease	13,512,708	28,755,339	83,915,237	88,140,320
Inventories	978,681	1,701,315	1,230,112	1,147,977
Fixed assets	38,928	38,075	35,759	33,259
Intangible assets	8,684	7,766	28,629	31,933
Investment property	192,976	189,017	186,048	5,973,555
Deferred tax assets	291,780	725,137	1,036,617	793,607
Other assets	241,475	-	-	-
Liabilities	**71,931,043**	**86,628,087**	**139,776,355**	**174,211,887**
Derivatives	-	-	116,854	-
Loans borrowed	42,361,897	52,680,169	57,561,890	52,323,450
Debt securities issued	20,381,018	20,902,340	40,188,938	86,138,164
Financial lease liabilities	7,346,909	11,775,292	40,292,797	31,020,933
REPO payables	994,263	-	-	-
Trade and other payables	236,844	472,394	805,083	3,637,536
Payables to leasing equipment suppliers	27,323	-	-	31,517
Advances received from leaseholders	339,159	541,727	750,162	944,289
Profit tax payables	-	133,760	-	60,533
Non-profit tax payables	184,755	64,206	60,631	55,465
Other liabilities	58,875	58,199	-	-
Own funds	**10,286,157**	**10,458,024**	**45,426,702**	**57,885,017**
Charter capital	10,001,000	10,001,000	44,945,410	57,358,790
FX differences reserve	-	-	6,371	(118,840)
Retained earnings	285,157	457,024	474,921	645,067

Source: IFRS consolidated financial statements of STLC

Table 2. Consolidated profit and loss statement items, RUB thousand

	2013	2014	2015	2016
Interest income, including	**7,286,712**	**8,245,995**	**9,522,671**	**9,000,015**
Financial lease income	6,886,106	7,960,888	7,914,356	7,826,092
Funds in credit institutions	400,606	285,107	1,608,315	1,173,924
Interest expense	**(5,083,677)**	**(6,749,605)**	**(10,130,745)**	**(13,809,372)**
Net financial income	**2,203,035**	**1,496,390**	**(608,074)**	**(4,809,357)**
Restoration / formation of interest asset impairment reserve	(704,758)	(1,285,907)	(1,871,927)	1,572,493
Net financial income after impairment and loss provisions	**1,498,277**	**210,483**	**(2,480,001)**	**(3,236,864)**
Net income from trade operations	-	31,864	18,347	-
Net income from foreign currency transactions	14,973	2,804,452	2,771,660	(544,416)
Net fee income	-	-	-	-
Income from operating lease	163,391	1,290,318	3,767,915	6,936,077
Loss from retirement and write-off of inventories before net value of possible sale	(402,522)	(843,866)	(408,592)	5,067
Formation of non-interest asset impairment reserve	(104,656)	(2,603,130)	(3,213,551)	(1,114,181)
Other operating income	328,542	612,724	1,194,942	564,629
General and administrative expenses	**(961,955)**	**(975,751)**	**(1,428,310)**	**(1,977,952)**
Earnings before tax	**244,727**	**333,209**	**167,138**	**632,360**
Profit tax expenses	(116,495)	(68,115)	(128,232)	(427,150)
Net profit	**128,232**	**265,094**	**38,906**	**205,210**

Source: IFRS consolidated financial statements of STLC

Table 3. Key ratios

	2014	2015	2016	3M2017
Capital adequacy				
CAR	10.8%	24.5%	24.9%	25.5%
Capital generation, bps	19	0	7	-
ACGR, bps	N/A	N/A	9	9
Risk profile				
NPL90+	N/A	N/A	N/A	4.2%
Share of NPL	N/A	N/A	N/A	13.0%
Share of 10 largest leaseholders (groups of leaseholders)	N/A	N/A	N/A	89%
Share of three largest types of leased property in the leasing portfolio	N/A	N/A	N/A	77.0%
Funding and liquidity				
Share of the largest funding source in liabilities	54.3%	31.10%	37.1%	38.7%
Share of the largest lender (group of lenders) in liabilities	N/A	N/A	N/A	12.2%
Share of 10 largest lenders (groups of lenders) in liabilities	N/A	N/A	N/A	28.5%

Source: ACRA estimates