"KazTransOil" JSC reports that the international rating agency Fitch Ratings upgraded KazTransOil to 'BBB', Outlook Stable

On August 28, 2013, the international rating agency Fitch Ratings published the Credit Opinion upgrading JSC KazTransOil's (KTO) long-term foreign currency Issuer Default Rating (IDR) to 'BBB' from 'BBB-'. The Outlook is Stable.

The upgrade of KTO is driven by its strong operating and credit profile, which the Agency expects to be maintained at least over the medium term, and its strategic importance to the economy of Kazakhstan (BBB+/Stable). KTO's ratings are capped by those of its parent JSC National Company KazMunayGas (NC KMG, BBB/Stable). In 2012, KTO became the national operator of oil pipelines in Kazakhstan. It transported 53m tons of oil that year, equivalent to about 1.1m barrels per day (mmbbl/d), and generated KZT61bn (USD410m) in EBITDA. At end-2012, the company had KZT72bn in cash and no balance-sheet debt, and we expect leverage to remain under 0.5x in 2013- 2017.

The rating actions are as follows:
Long-Term IDR: upgraded to 'BBB' from 'BBB-', Outlook Stable.
Local currency Long-Term IDR: assigned at 'BBB', Outlook Stable.
Short-Term IDR: affirmed at 'F3'.
National Long Term Rating: assigned at 'AA+(kaz)', Outlook Stable.
Senior unsecured rating: assigned at 'BBB'.
National senior unsecured rating: assigned at 'AA+(kaz)'.

KTO's ratings reflect its dominant position in the oil transportation sector in Kazakhstan, and the Kazakh economy's dependence on oil revenues. In 2012, KTO received the 'national operator' status. KTO shipped 60% of Kazakhstan's crude that year, excluding the volumes shipped by its two joint ventures (JVs) with China National Petroleum Corporation (CNPC, A+/Stable) that operate the major parts of the Kazakhstan-China oil pipeline.

The Agency Capped KTO's ratings at NC KMG's level because the latter exercises a significant influence over KTO's free cash flows (FCF) through dividends, which NC KMG needs to service its standalone debt of KZT1,748bn (USD11.6bn) at end-2012.

Fitch Ratings consider that KTO's uncapped ratings are in the low-'A' category, limited by country-specific corporate governance issues and its concentration of assets in one country. The Agency believes that in the event of financial stress, the state will support KTO, either directly through equity contributions or loans from state-owned banks, or indirectly through higher tariffs.

In 2012, KTO's crude turnover (excluding JVs) was flat yoy at 34.5bn tonne-kilometres, and in H113 it increased by 10% yoy. The Agency expects that KTO's volumes and turnover will remain stable over the medium term, as most volumes from the Kazakhstan's giant Kashagan field, which NC KMG expects to be launched later this year will bypass KTO. While KTO may start shipping up to 0.14mmboe/d of Russian crude to China in 2014, the Agency does not include these volumes in their rating case for KTO as transit terms and tariffs are presently still unknown.

KTO's tariffs are regulated by Kazakhstan's Agency for Regulation of Natural Monopolies (AREM), which reviews them from time to time. In December 2012, AREM increased KTO's domestic tariffs by 50% for the first time since 2004, which partially removed crosssubsidisation between profitable export and loss-making domestic operations. Fitch Ratings view timely tariff indexation as essential for KTO’s sound financial performance.

In 2012, KTO paid out special dividends of KZT60bn and in 2013, it declared dividends of KZT29bn, or 86% of its 2012 net income. The Agency believes that KTO’s dividends will stabilise at 50%-60% of its net income in 2014-2017.

The Agency expects that KTO’s annual capex may exceed KZT50bn in 2013-2017. Fitch Ratings expects KTO to report negative FCF until 2017 due to higher capex, but its FFO adjusted net leverage should remain under 0.5x in the medium term.

The Agency continues to treat the indebtedness of Kazakhstan-China Pipeline LLP (KCP), KTO’s 50% JV, as non-recourse to KTO. These borrowings include a USD300m Eurobond due in 2020 and a USD900m unguaranteed bank loan due in 2018. KCP had a solid financial position at end-2012. Its net debt/EBITDA stood at 4x and in 2012 its FCF reached KZT24bn (USD163m). The Agency believes that the JV will be able to service its debts without any help from KTO.

At end-2012, KTO maintained significant cash balances and deposits of KZT113bn (USD751m), mainly with Kazakh banks. It had no financial debt at this time.

Rating sensitivities
Positive: A positive rating action on NC KMG’s ratings will likely lead to a positive rating action on KTO.
Negative: A negative rating action on KMG NC will likely be replicated on KTO.
KTO’s aggressive capex and/or dividend payments exceeding our expectations resulting in a significant and sustained deterioration of its credit metrics, including FFO gross adjusted leverage above 2x, would also be negative for its ratings.