

Kazakhtelecom Outlook Revised To Positive On Signs Of Improving Management And

Governance; 'BB' Affirmed

Дата публикации: 02-окт-2014 19:41:29 MST

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- Kazakhtelecom has recently approved a new strategy for its mobile
- business, which we view as a sign of improving management and governance.
- We are affirming our 'BB' rating on Kazakhtelecom and revising the
- outlook to positive.
- We are also raising the national scale rating on the company to 'kzA+' from 'kzA'.
- The positive outlook reflects the likelihood of an upgrade within the
- next 12-18 months if the company were to adhere to its strategy, notably
- in terms of capital spending, while preserving its debt leverage and
- liquidity at current levels.

MOSCOW (Standard & Poor's) Oct. 2, 2014--Standard & Poor's Ratings Services today revised its outlook on Kazakhtelecom JSC to positive and affirmed the 'BB' long-term corporate credit rating.

We also raised the national scale rating on Kazakhtelecom to 'kzA+' from 'kzA'.

The outlook revision reflects that we could revise our assessment on Kazakhtelecom's management and governance to "fair" from "weak" if the company were to adhere to its recently approved strategy for its mobile business. This improved assessment would also depend upon higher predictability in its business and financial decisions, which we think the company could achieve if it sticks to this strategy.

Kazakhtelecom is currently rolling out a nationwide 4G network, which will require meaningful investment. In our base-case scenario, we assume that this will result in just a moderate leverage increase for the company, which could remain commensurate with a higher rating. However, based on its track record, we still see a risk that the company's capital spending might become more aggressive, and, more importantly, that it could engage in this long-term project without fully securing long-term financing. We could raise the rating if the company demonstrates more prudent investment and financial management, in line with its strategy.

We believe that it will be fairly difficult for Kazakhtelecom to win a meaningful share of the 4G market over the next three years. The company's performance in the core fixed-line business has been historically volatile, notably in terms of profitability. Kazakhtelecom's public policy role requires

it at times to invest in projects with low profitability or long payback periods. Over the past several years, Kazakhtelecom has maintained a fairly high investment budget compared with its actual business requirements, and in 2012-2013 the company took steps to stabilize its operating performance. However, certain constraints, such as the inability to meaningfully reduce its headcount, still negatively affects the overall business risk score.

The positive outlook reflects the likelihood that we will raise the rating on Kazakhtelecom to 'BB+' if we were to revise our assessment of its management and governance to "fair" from "weak".

The upgrade would also be dependent upon Kazakhtelecom's credit metrics remaining at moderate levels, including a ratio of Standard & Poor's-adjusted debt to EBITDA of below 2x, and maintenance of adequate liquidity. Operating performance would also have to remain within the boundaries of our base-case scenario, notably in terms of profitability.

We could revise the outlook to stable if we saw no progress in management and governance, or if Kazakhtelecom's debt leverage were to increase well above our base-case scenario expectations as a result of higher investments or extraordinary dividend distribution.

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