Turkiye Petrol Rafinerileri A.S. (Tupras) (/gws/en/esp/issr/80512806)

FitchRatings

Fitch Affirms Tupras at 'BBB-'; Outlook Negative

Fitch Ratings-London-01 February 2017: Fitch Ratings has affirmed Turkiye Petrol Rafinerileri A.S.'s (Tupras) Long-Term Local and Foreign Currency Issuer Default Ratings (IDRs) at 'BBB-' and National Long-Term Rating at 'AA+(tur)'. The Outlooks are Negative. Tupras's USD700m notes due in 2018 have been affirmed at 'BBB-'.

Tupras has a leading position in the rapidly growing Turkish oil refining market. Its operations and assets are concentrated in the country; however, its earnings are more driven by the global factors, such as crack spreads on refined products. Fitch's recent downgrade of Turkey's rating to 'BB+' hence does not affect the company's ratings. However, Tupras's foreign currency ratings are capped by the 'BBB-' Country Ceiling.

Tupras's Negative Outlook reflects a risk that its leverage may remain above Fitch's negative rating trigger due to generous dividends and volatile refining margins. Tupras's ability to generate free cash flow (FCF), due to falling capital intensity, partly offsets these negative pressures. We also forecast leverage will be reduced gradually on the back of positive FCF.

KEY RATING DRIVERS

Stronger Business, Higher Leverage: In November 2014, Tupras completed the modernisation of the Izmit refinery with the residuum upgrading project (RUP) consisting of a vacuum distillation, delayed coker and hydrocracker units. New units became fully operational in 2015 and are expected to add 3.5 million tonnes of higher-margin white products, which is positive for the company's credit profile. The completion of RUP also marks the end of a capex-intensive period.

We expect reduced investments of up to TRY800 million annually from 2016 compared with over TRY2 billion in 2012-2014, when RUP was being constructed. However, with generous dividend payouts and refining margins below our earlier forecasts, there is a risk that Tupras's net leverage metrics will be outside our guidance for the 'BBB-' rating, hence driving the Negative Outlook. Nevertheless we also forecast gradual deleveraging on the back of positive FCF, which drives today's affirmation.

Rating Above The Sovereign: Fitch downgraded Turkey's Long-Term Foreign Currency Issuer Default Rating (IDR) to 'BB+' from 'BBB-' on 27 January 2017. Higher volatility of Turkish lira, potential decrease in tourist arrivals and pressure on GDP growth may weaken Tupras's financial profile and reduce growth in Turkish fuel demand. Yet, uncertainties related to recent political developments in Turkey have had a limited direct impact on Tupras's operations, which is reflected in today's affirmation.

FX Risk Limited: Fuel prices in Turkey reflect changes in foreign exchange, which allows Tupras to pass on majority of foreign exchange risk to customers. Some risk remains, however, with respect to unfavourable foreign exchange movements towards the end of reporting periods, as sharp deterioration in Turkish lira may temporarily increase leverage metrics. Tupras has strong liquidity, which should offset temporary leverage spikes.

Stable Short-Term Industry Outlook: Depressed oil prices supporting demand for fuel, improved fuel oil crack spreads and slower global refining capacity additions than demand growth will support European refining margins. This underpins the stable outlook for the sector in 2017. Refinery closures in the past few years, coupled with healthy demand, have improved the market balance for refining products in Europe.

More Challenges over Medium Term: The longer-term sector outlook is more uncertain. Excess global refining capacity, and the structural decline in fuel consumption because of growing engine efficiency and environmental policies are likely to put pressure on the European refining sector. OPEC expects the pace of global capacity additions to accelerate after 2018, putting pressure on margins. Integrated companies with a strong petrochemical, upstream and retail presence will be better-positioned to withstand market pressure in the long term.

DERIVATION SUMMARY

Tupras is the sole refiner in a rapidly growing Turkish fuel market, which is the key factor supporting its ratings in the 'BBB' rating category. We view Tupras's business integration as weaker than direct peers such as Polski Koncern Naftowy ORLEN (BBB-/Stable) and MOL Hungarian Oil and Gas Company (BBB/Stable), which have stronger presence in the petrochemical or upstream segments.

KEY ASSUMPTIONS

Fitch's key assumptions within our rating case for the issuer include:
- Mediterranean refining margins moderating to USD2.5/bbl over the long term from USD4.9/bbl in 2015 and USD4/bbl in 2016;
- USD/TRY (annual average) 3.0 in 2016; 3.7 in 2017 and 3.8 in the long term;
- Low capital intensity in 2016 and thereafter following the completion of RUP modernisation.

RATING SENSITIVITIES
Positive: Future developments that may, individually or collectively, lead to a revision of the Outlook to Stable include:
- Funds from operations (FFO)-adjusted net leverage (adjusted for factoring of trade accounts receivable) comfortably below 2.5x (2016E: 3.2x) and FFO fixed charge cover above 5x (2016E: 5x);
- Consistently positive FCF.

Negative: Future developments that could lead to negative rating action include:
- FFO-adjusted net leverage (adjusted for factoring of trade accounts receivable) consistently above 2.5x and FFO fixed charge cover well below 5x;
- Consistently negative FCF;
- Substantially higher capex or dividends leading to higher-than-expected leverage.

LIQUIDITY
Adequate Liquidity: At end-September 2016 Tupras's cash balance TRY6.3 billion (excluding restricted balances) covered short-term debt of TRY3.4 billion. In addition, the company' liquidity is supported by uncommitted credit lines and our expectation of positive FCF in 2017. The company has access to both domestic and international banks, though political risks associated with Turkey could temporarily suspend its access to the international market.

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Summary of Financial Statement Adjustments

Tupras's factoring amounts are included into the company's indebtedness according to Fitch's methodology. At end-2015 the company's balance of factored trade receivables amounted to TRY0. 8 billion (TRY2.3 billion at end-2014), compared to its net balance sheet debt of TRY7.9bn.

Operating Leases: Fitch capitalises operating leases using a 5x multiple. As a result, at end-2015 the company's adjusted debt was increased by TRY94 million.

Additional information is available on www.fitchratings.com. For regulatory purposes in various jurisdictions, the supervisory analyst named above is deemed to be the primary analyst for this issuer; the principal analyst is deemed to be the secondary..

Applicable Criteria
Criteria for Rating Non-Financial Corporates (pub. 27 Sep 2016) (https://www.fitchratings.com/site/re/885629)

Additional Disclosures
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