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ACRA upgrades JSC Avangard-Agro to BBB(RU), outlook Stable, and bond issues to BBB(RU)

The credit rating of [JSC Avangard-Agro](#) (hereinafter, Avangard-Agro, or the Company) has been upgraded based on the improvement of the Company's standalone creditworthiness assessment (SCA), which in turn is due to the improvement of the Company's financial metrics (liquidity and free cash flow in 2020), and the expectation that they will be maintained within the ranges established by the Agency's methodologies for this rating level, despite ACRA's forecast of lower grain prices in 2021–2023 compared to 2020.

The rating is based on the Company's bbb+ SCA, reduced by one notch to bbb due to event risk. This risk stems from a possible deterioration in the financial standing of other related companies controlled by the controlling shareholder, which may have negative consequences for Avangard-Agro.

The Company's bbb+ SCA is based on its medium size. The business profile assessment is average due to the high product diversification, medium level of vertical integration and average share of products with high added value. The high assessment of accessibility and diversification of sales markets and the fact that the Company grows its main crops in regions with moderate climate risks have a positive impact on the Company's operational business profile. Corporate governance is below average due to the lack of corporate procedures needed to balance the interests of shareholders and creditors, and also due to the concentration of shareholder risks on the sole beneficial owner and close financial relationship with ["AVANGARD" JSB](#) (ACRA rating [BB+\(RU\)](#), [outlook Stable](#), hereinafter, AVANGARD Bank).

The Company's high profitability and cash flow assessments were positive for the financial risk profile assessment. However, the medium size of business and average leverage and debt servicing combined with the low liquidity assessment were limiting factors in the assessment of the financial risk profile. In addition, the very high share of short-term debt (most of which is to be paid within the next two years) creates liquidity risks.

Avangard-Agro is an agro holding focused on cereals and technical crops in the northern and central areas of the Central Black Earth Region of Russia. The Company manages 450,000 hectares of farmland; its agricultural machinery fleet includes 500 combine harvesters, 1,300 tractors, and 1,600 vehicles. The ultimate beneficiary of the Company is K. Minovalov.

According to 2020 data, the gross volume of grain (wheat and barley) harvested by the Company was about 0.9% of the total Russian indicator (133.5 mln tons). Avangard-Agro is a competitive producer in a highly fragmented grain market. This means that the Company is unable to influence prices and is entirely dependent on prices that are set in the market as a result of the annual harvest.

The Company's medium business profile assessment is based on the average level of vertical integration (about 35% of revenue comes from selling malt made from its own barley and wheat), the high level of product diversification (the product portfolio consists of wheat, sunflower seeds, corn, barley, and sugar beet) and medium share of products with high added value. The Company's business profile assessment is also based on high geographical diversification due to good distribution logistics and high export levels (around 29% as of the end of 2020). At the same time, ACRA notes that the Company grows its main crops in regions with moderately favorable climate conditions in the Voronezh, Oryol, Kursk, Belgorod, Lipetsk, and Tula Regions.

The average assessment of corporate governance is a reflection of the concentration of shareholder risks on the sole owner, who plays an active role in the strategic and operational management of the Company. There are no formalized corporate procedures (including a dividend policy and a risk management policy). Operations with related parties represented by AVANGARD Bank is also a limiting factor in the assessment of corporate governance.

Key rating assessment factors

The financial risk profile assessment is set at a due to the medium size of business (the absolute value of the Company's weighted operating cash flow before changes in working capital (FFO) before net interest and taxes for 2018–2023 will be around RUB 9 bln) and very high business profitability (the weighted ratio of FFO before interest and taxes to revenue for 2018–2023 will be around 42%). This high profitability stems from: (1) the Company's measures to increase high crop yields and (2) the high profitability of key products — malt and high-quality wheat. The financial risk profile assessment is limited by the average liquidity assessment. The Company's capacity to carry out scheduled repayment of its debt obligations depends entirely on its free cash flow and possibilities for refinancing. According to ACRA's calculations, from 2021 to 2023, the weighted short-term liquidity ratio should be 1.1. The liquidity risks are partly compensated by the Company's stable relationship with its key external creditor, [Sberbank](#) (ACRA rating [AAA\(RU\), outlook Stable](#)).

Average debt load and medium interest payment coverage. The ratio of the Company's total debt to FFO before net interest decreased to 2.3x in 2020, compared to 3.2x in 2019 due to an increase in operating cash flow mainly driven by higher prices for cereals and sunflower seeds. ACRA expects a moderate decline in average prices for cereals in the period from 2021 to 2023, due to which the Company's leverage will slightly increase in 2021 to 3.1x and remain at this level in 2022–2023. The Agency also notes the average coverage of interest payments (ratio of FFO to net interest payments to interest payments): the weighted figure for 2018–2023 will be 4.8x.

Strong cash flow. Free cash flow (FCF) profitability increased to 23% in 2020 compared to 17% in 2019 due to higher operational cash flow and the moderate investment program. The Agency expects average FCF profitability at 5% in 2021–2023 amid high operating cash flow, dividend payments tied to net profits (no more than 50%), and moderate capital expenditures.

Key assumptions

- Cereal prices declining in 2021 to 2019 indicators and remaining at this level in 2022–2023;
- Stable area of farmland — around 450,000 hectares, no purchases of new plots over the next three years;
- Capital investments at RUB 2 bln a year;
- Annual dividend payments at no more than 50% of net profits.

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:

- Weighted average total debt to FFO before net interest ratio declining below 2.0x;
- Increase in short-term liquidity due to decrease of short-term financing and better terms of cooperation with counterparty banks;
- FFO before net interest payments to interest payments exceeding 5.0x.

A negative rating action may be prompted by:

- Ratio of total debt to FFO before net interest payments exceeding 3.5x and ratio of FFO before net interest payments to net interest payments falling below 2.5x;
- Decline in profitability of FFO before interest payments and taxes below 15%, decrease in FFO before net interest payments and taxes below RUB 5 bln, and decrease in net cash flow profitability below 2%;
- Significantly limited access to external sources of liquidity.

Rating components

SCA: bbb+.

Adjustments: event risk, SCA -1 notch.

Issue ratings

[JSC Avangard-Agro, BO-001R-01 series \(RU000A0ZYC31\)](#), maturity date: September 23, 2027, issue volume: RUB 3 bln — BBB(RU).

[JSC Avangard-Agro, BO-001R-02 series \(RU000A0ZYH02\)](#), maturity date: November 16, 2027, issue volume: RUB 3 bln — BBB(RU).

Rationale. The bonds listed above are senior unsecured debt instruments of JSC Avangard-Agro. Due to the absence of either structural or contractual subordination of the issues, ACRA regards them as *pari passu* with other existing and future unsecured and unsubordinated debt obligations of the Company. According to ACRA's methodology, the unsecured debt repayment level corresponds to the first category. Therefore, the credit rating of the issues is equivalent to that of [JSC Avangard-Agro: BBB\(RU\)](#).

Regulatory disclosure

The credit ratings have been assigned to JSC Avangard-Agro and the bonds (RU000A0ZYC31, RU000A0ZYH02) issued by JSC Avangard-Agro under the national scale for the Russian Federation based on the [Methodology for Credit Ratings Assignment to Non-Financial Corporations Under the National Scale for the Russian Federation](#) and the [Key Concepts Used by the Analytical Credit Rating Agency Within the Scope of Its Rating Activities](#). The [Methodology for Assigning Credit Ratings to Individual Issues of Financial Instruments on the National Scale for the Russian Federation](#) was also applied to assign the credit ratings to the above issues.

The credit ratings assigned to JSC Avangard-Agro and the bonds (RU000A0ZYC31, RU000A0ZYH02) issued by JSC Avangard-Agro were published by ACRA for the first time on July 31, 2017, October 9, 2017, and November 28, 2017, respectively. The credit rating of JSC Avangard-Agro and its outlook and the credit ratings assigned to the bonds are expected to be revised within one year following the publication date of this press release.

The credit ratings were assigned based on data provided by JSC Avangard-Agro, information from publicly available sources, and ACRA's own databases. The credit ratings are solicited, and JSC Avangard-Agro participated in their assignment.

In assigning the credit ratings, ACRA used only information, the quality and reliability of which was, in ACRA's opinion, appropriate and sufficient to apply the methodologies.

ACRA provided no additional services to JSC Avangard-Agro. No conflicts of interest were discovered in the course of credit rating assignment.

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