Fitch Ratings

FITCH AFFIRMS TUPRAS AT 'BBB-'; STABLE OUTLOOK

Fitch Ratings-London/Istanbul/Warsaw-20 January 2012: Fitch Ratings has affirmed Turkiye Petrol Rafinerileri A.S.'s (Tupras) Long-term local and foreign currency Issuer Default Ratings (IDR) at 'BBB-'. The National Long-term rating is also affirmed at 'AAA(tur)'. The Outlooks are Stable.

The affirmation reflects Tupras's leading position in the Turkish oil refining and marketing sector and above-average cash flow from operations for a refining business, primarily due to its domestic sales margin and favourable position in terms of crude oil supply costs and product slate. The ratings also incorporate the company's solid funds from operations in 9M11 despite weak benchmark refining margins.

The ratings incorporate Fitch's expectations of a weakening in credit metrics in 2012-2014 from historically strong levels until the residuum upgrading project (RUP), the main part of Tupras's large capex plan, will start to generate cash flow in 2015.

The large, primarily debt-funded USD3.4bn capex plan for 2012-2014 will, according to Fitch's projections, result in a weakening of funds-from-operations (FFO)-adjusted net leverage above the guideline for the rating (2.5x). The ratios are projected to return to levels commensurate with the current ratings in 2015. While Fitch rates the company based on long-term leverage projections, any delays in ratio recovery or material underperformance in terms of FFO would put pressure on the ratings.

The RUP will enhance the company's business profile due to an improvement in the refining product mix as a result of increased production of diesel and gasoline and lower output of heavy products, in particular fuel oil. The company expects this project to generate additional EBITDA of USD550m per annum, compared with Tupras's average EBITDA for 2007-2010 of USD946m.

In October 2011, Tupras signed a USD2.1bn long-term financing for the RUP with 10 international banks. The majority of the funding will be insured by export credit agencies. Fitch currently expects that Tupras will have sufficient headroom under the financial covenants included in the bank loan documentation. However, potential large adverse movements in the TRY/USD rate or inventory holding losses may reduce the company's headroom under the financial covenants.

Fitch understands that Tupras has some flexibility to lower working capital needs, if required, for example for financial ratio covenant compliance in case of unexpected adverse movements in external conditions.

The ratings are constrained by Tupras's generous dividend policy, which is unlikely to change in 2012-2014 despite negative free cash flow driven by high capex.

The ratings also take into account the high business risks in the refining sector, given its cyclicality and capital intensity. Despite weak refining margins in Europe, the company reported solid EBITDA in 9M11 when its net refining margin averaged USD5.5/bbl compared with the benchmark Mediterranean Ural complex margin of USD1.1/bbl.

One possible negative development for Tupras's margins would be a ban on purchases of Iranian crude due to new US sanctions on institutions that deal with Iran's central bank. At the moment it is not certain whether Turkey will be subject to the US sanctions against Iran. Supplies from Iran accounted for 38% and 20% of Tupras's oil supplies in 2010 and 2009 respectively.

Fitch understands that a scenario in which Tupras is not allowed to buy Iranian crude should not impact the company's security of supply given several possible alternative supply sources. However, it may worsen the company's refining margins through lower discounts on purchased crude oil. This is because crude from alternative sources may be priced at a lower discount to Brent oil than Iranian crude oil. A substantial reduction in Iranian imports by Tupras would be treated as an event risk and could lead to a review of the company's ratings depending on the circumstances.

The rating affirmation reflects the company's sufficient liquidity. At end-September 2011, Tupras had unrestricted cash of TRY1.8bn against short-term debt of TRY989m. Negative free cash flow in 2012-2014 due to the RUP will be covered with the recently signed bank funding.

Tupras is one of a few refining and marketing companies globally, which are rated by Fitch in the 'BBB' rating category on a stand-alone basis. This is due to its strong business profile and market position for a refining company and moderate financial policy. Most independent refiners possess credit profiles below the 'BBB' category given the refining industry's cyclicality, capital-intensity and high competitiveness.

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Additional information is available on www.fitchratings.com. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

In accordance with Fitch's policies, the issuer appealed and provided additional information to Fitch that resulted in a rating action which is different than the original rating committee outcome.

Applicable criteria; 'Corporate Rating Methodology' dated 12 August 2011 are available at www.fitchratings.com

Applicable Criteria and Related Research:
Corporate Rating Methodology
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=647229

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