MOODY'S

Rating Action: Moody's confirms Transnet's Ba3 CFR; negative outlook

14 Oct 2022

London, October 14, 2022 -- Moody's Investors Service ("Moody's") has today confirmed those ratings of Transnet SOC Ltd. ("Transnet" or "the company") that had been on review for downgrade. This includes the company's corporate family rating (CFR) of Ba3, the national scale senior unsecured MTN programme (Medium-Term Note) rating of A2.za and the national scale other short-term rating of P-1.za. The Baseline Credit Assessment (BCA), a measure of standalone credit quality prior to any assessment of potential extraordinary government support has also been confirmed at b2. The outlook on all ratings has been changed to negative from ratings under review. This rating action concludes the review that was initiated on Transnet on 8 June 2022.

A full list of affected ratings is provided towards the end of this press release.

RATINGS RATIONALE

Transnet's ratings were confirmed because the company's liquidity has improved after it raised new financing in the form of a $685 million 5-year amortizing term loan and a bridge to bond facility that allowed it to repay its $1 billion international bond maturity on 26 July 2022. The outlook was changed to negative because the company's liquidity profile remains under pressure, albeit not as acute as before the new financings were raised. Transnet remains reliant on accessing debt capital markets to refinance the bridge facility and other maturing debt within the next twelve months. Given ongoing volatile market conditions Moody's expects that it will be challenging to access capital markets within a narrow timeframe. Moody's however also continues to believe that strong support from the South African government exists in case it would be required.

Moody's expects that as of the end of September, Transnet had sufficient liquidity to meet investment needs and debt amortization payments coming due over the next twelve months. These liquidity sources are comprised of the company's cash balance, cash expected to be generated from operations, proceeds from the sale of some non-core assets, as well as its fully available ZAR13.3 billion short term call facilities. Although most of the call loans can be canceled by lenders upon 365 days' notice, these loans have historically always been rolled over. Transnet has not received any notice of cancellation so far and therefore the loans remain available until at least October 2023. Debt maturities until the end of September 2023 amount to ZAR22 billion, when including drawings under the bridge to bond, which Moody's expects to have a short term maturity. Transnet's debt maturity profile remains concentrated beyond the next twelve months, with an additional ZAR12 billion of debt maturing between September 2023 and March 2024, which Moody's expects can only be repaid if Transnet succeeds in raising additional debt. Overall maturities over the next 4.5 years, from October 2022 until March 2027 amount to ZAR76 billion. Apart from refinancing risk, this also exposes the company to materially rising interest costs.

With regards to corporate governance, Transnet has achieved incremental improvements in terms of compliance and reporting, but Moody's continues to monitor improvements in the company's financial and liquidity risk management where the company remains vulnerable to refinancing exposure over the next 12 to 18 months. After the National Treasury granted an exemption for the reporting of legacy breaches under the Public Finance Management Act (PFMA), the company was able to release audited financial statements for the financial year ending March 2022 within a timely manner following the end of the financial year and obtained an unqualified audit opinion for the first time since 2018. The timely reporting and clean audit opinion avoided a debt covenant breach, which over the past four years frequently caused delays in securing new financing. Moody's however notes that most of the company's debt agreements also contain a cash interest coverage maintenance covenant that the company is at risk of breaching in the near term, especially as interest costs on new debt are rising. While Moody's expects lenders to remain generally supportive as demonstrated in the past, any covenant breaches would delay the company's access to refinancing.

Transnet's Ba3 CFR continues to reflect the company's solid business profile with ownership of long-term infrastructure assets and a monopoly position in South Africa that provides a degree of cash flow visibility.

Transnet falls under Moody's Government-Related Issuers Methodology given its 100% government ownership and importance to the South African economy. The strong link between Transnet and the Government of South Africa (Ba2 stable) is reflected by Moody's assumptions of 'Very High' default dependence with the Government of South Africa and 'Strong' extraordinary support from the government, which supports a two notch uplift from the BCA.

Transnet's Ba3 CFR is supported by its (1) monopoly on the South African railway infrastructure and freight services; (2) ownership of South Africa's eight seaports and operation of a large part of South Africa's stevedoring services; and (3) operation of strategically important hydrocarbon pipelines. At the same time, the ratings also reflect (1) liquidity pressure over the short term and large debt maturities over the next five years which requires strong access to debt markets to refinance; (2) weak free cash flow generation due to high capital spending requirements; (3) aging infrastructure causing operational disruption and reducing capacity; and (4) regulatory uncertainty on tariff structures.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Given the negative outlook, an upgrade is unlikely at this time. Moody's would consider stabilizing the outlook at the current rating level if Transnet secures long term financing to replace the short term bridge loan that was used to redeem a $1 billion bond maturity in July 2022. To consider a rating upgrade, we would further expect to see a sustainably restored liquidity profile and improved liquidity management. We would also expect to see operational improvements and EBIT/ interest expense to exceed 1.0x on a sustained basis. An upgrade of the CFR would require raising the BCA by at least two notches while the sovereign bond rating of South Africa remains Ba2 or improves.

Transnet's BCA is likely to face downward pressure if Transnet's liquidity weakens. A downgrade of the BCA is likely to lead to a downgrade of Transnet's ratings. A downgrade of South Africa's government bond rating would also likely lead to a downgrade of Transnet's ratings given our assessment of strong credit linkages between the two.

LIST OF AFFECTED RATINGS

Confirmations:

..Issuer: Transnet SOC Ltd.

....LT Corporate Family Rating, Confirmed at Ba3

....Probability of Default Rating, Confirmed at Ba3-PD

....Baseline Credit Assessment, Confirmed at b2

....BACKED Senior Unsecured Regular Bond/Debenture, Confirmed at Ba3

....Senior Unsecured Medium-Term Note Program, Confirmed at (P)Ba3

....NSR Senior Unsecured Medium-Term Note Program, Confirmed at A2.za

....Subordinate Medium-Term Note Program, Confirmed at (P)B1

....NSR Subordinate Medium-Term Note Program, Confirmed at Baa2.za

....NSR Other Short Term, Confirmed at P-1.za

Outlook Actions:

..Issuer: Transnet SOC Ltd.

....Outlook, Changed To Negative From Rating Under Review

The methodologies used in these ratings were Surface Transportation and Logistics published in December 2021 and available at https://ratings.moodys.com/api/rmc-documents/360641, and Government-Related Issuers Methodology published in February 2020 and available at https://ratings.moodys.com/api/rmc-documents/64864. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of these methodologies.

Moody's National Scale Credit Ratings (NSRs) are intended as relative measures of creditworthiness among debt issues and issuers within a country, enabling market participants to better differentiate relative risks. NSRs differ from Moody's global scale credit ratings in that they are not globally comparable with the full universe of Moody's rated entities, but only with NSRs for other rated debt issues and issuers within the same country. NSRs are designated by a ".nn" country modifier signifying the relevant country, as in ".za" for South Africa. For further information on Moody's approach to national scale credit ratings, please refer to Moody's Credit rating Methodology published in August 2022 entitled "Mapping National Scale Ratings from Global Scale Ratings Methodology". While NSRs have no inherent absolute meaning in terms of default risk or expected loss, a historical probability of default consistent with a given NSR can be inferred from the GSR to which it maps back at that particular point in time. For information on the historical default rates associated with different global scale rating categories over different investment horizons, please see https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1280297.

The local market analyst for this rating is Lisa Jaeger, +971 (423) 796-59.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form.

Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the issuer/deal page for the respective issuer on https://ratings.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website https://ratings.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://ratings.moodys.com/documents/PBC_1288235.

At least one ESG consideration was material to the credit rating action(s) announced and described above.

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the EU and is endorsed by Moody's Deutschland GmbH, An der Welle 5, Frankfurt am Main 60322, Germany, in accordance with Art.4 paragraph 3 of the Regulation (EC) No 1060/2009 on Credit Rating Agencies. Further information on the EU endorsement status and on the Moody's office that issued the credit rating is available on https://ratings.moodys.com.

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