FITCH PUBLISHES TURK TELEKOM'S 'BBB-'/STABLE RATING

Link to Fitch Ratings' Report: Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=749393

Fitch Ratings-London-03 June 2014: Fitch Ratings has published Turk Telekomunikasyon A.S.'s (TT) Long-term Foreign and Local Currency Issuer Default Ratings (IDRs) of 'BBB-' with Stable Outlook. A senior unsecured rating of 'BBB-' has also been published.

The ratings reflect TT's leading voice and broadband position in the Turkish telecoms market, with resulting high fixed-line EBITDA margin, which is partly offset by its third-placed position in the mobile market. FX risks and reliance on shorter-term maturity funding are TT's main credit weaknesses. The company has a sound pre-dividend free cashflow (FCF) generation capability.

KEY RATING DRIVERS

Strong Fixed-line Market Position
TT is Turkey's largest telecoms company and the fixed-line incumbent operator, with around a 93% subscriber market share in fixed voice and a 88% subscriber market share in fixed broadband services. It has a solid fixed-line franchise with less intense competition relative to other European incumbents. The Turkish fixed broadband market remains fairly under-penetrated at around 40% of households, lagging significantly behind the European average of around 65% and offers firm growth potential. TT owns 90% of Avea, Turkey's third largest mobile operator with around a 20% subscriber market share. Revenue growth as Turkish mobile penetration increases should lead to increased profitability in the mobile business.

Mobile to Offset Fixed Declines
Revenue growth from fixed broadband and data services is offsetting fixed-line voice revenues declines. Fixed EBITDA has come under pressure over the last two years, but this has been partly offset by mobile EBITDA growth. Fitch expects TT's EBITDA less capex (before spectrum costs) to grow over the next few years as the mobile business becomes more cash-generative, resulting in our expectations of pre-dividend FCF margin over 10% over the medium-term.

No Explicit Sovereign Linkage
The Turkish government owns 31.7% of TT. However, TT is rated on a stand-alone basis with no support from any of its shareholders. At this point in time, TT's rating is not linked to the Turkish sovereign rating (BBB-/Stable).

Long-term Uncertainty from Concession Expiry
The rating factors in some long-term uncertainty relating to the expiry of TT's fixed-line concession agreement with the Turkish government in 2026. Fitch does not rule out the risk that in the lead-up to the concession termination date, the views of TT's management, TT's main shareholder and the Turkish government on TT's operational and financial priorities may diverge. Fitch believes that TT's management will pursue a conservative financial policy to ensure that all debt could be repaid before the expiry of the concession agreement.

Significant FX Mismatch
TT has a significant currency mismatch as 95% of its debt at end-1Q14 was denominated in USD and EUR while its FCF is generated in local currency. This exposes TT to significant risks arising from potential adverse movements in foreign exchange rates. However, as the company can only

pay a dividend of up to a maximum of 100% of distributable net income (adjusted by TT's board of directors to 70% of net income in 2013), any FX losses will reduce net income, which will lead to a fall in dividends and cash taxes paid in the following year. With unadjusted net debt to EBITDA of 1.4x at end-1Q14, TT has low leverage compared with other European telecoms companies, but this FX risk is the main reason why the leverage thresholds for negative rating action are set at a lower level compared with other western European telecoms companies at a similar rating level.

Weak Liquidity Profile

TT has a sound liquidity profile in a Turkish context, with ready access to bank financing and other funding sources, but weak relative to the western European telecoms peer group. While the company may count on a strong cash flow generation profile, large cash balances of approximately TRL1.5bn as of end-1Q14 and some undrawn committed credit facilities, these could prove insufficient to service its short-term debt repayment obligations. This means TT is more reliant on regular refinancing of its short-term debt. This refinancing risk could be exacerbated by a further depreciation of the TRL against the EUR and/or USD.

RATING SENSITIVITIES

Negative: Future developments that could lead to negative rating action include:

-Funds flow from operations (FFO) net leverage trending above 2.25x (FYE13: 2.3x) or unadjusted net debt to EBITDA breaching 1.5x (FYE13: 1.5x) on a prolonged basis

-Material deterioration in TT's pre-dividend FCF margin, or in the company's regulatory or competitive environment

Fitch views positive rating action as unlikely in the medium-term; however, future developments that could lead to positive rating actions include:

-Improved visibility on how the termination of fixed-line concession agreement would be resolved, an improved liquidity profile and a reduced currency mismatch in its debt structure

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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, Corporate Rating Methodology, 28 May 2014, are available on www.fitchratings.com.

Applicable Criteria and Related Research:
Rating Sukuk
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