Global Refuse Holding Zrt.
Hungary, Business Services

B+ STABLE

Corporate profile

Global Refuse Holding Zrt. (GRH) has been active in the Hungarian waste management market since 1993. It manages a group of companies that operate in waste management, public cleaning, landfill management and waste trading. GRH is the direct owner of Tappe Kft. (Tappe), Békéscsabai Városüzemeltetési Kft (BVÜ), Global Refuse Nonprofit Kft. (GRN) and Global Refuse Metal Kft. (GRM). GRH's operations are performed through these subsidiaries.

The ownership structure of GRH is as follows: 80% owned by Central European Opportunity PE Fund, 20% owned by Coactore Kft.

Tappe is responsible for waste collection, transportation, and winter road cleaning, while its subsidiary, BVÜ is responsible for waste treatment. According to the 'Dél-Alföld' regional waste management plan, all the municipal waste of Békés county must be placed at the disposal site operated by BVÜ in the period to 2030. The whole facility is 21.33 hectares in size. By April 2021, around 1.3m tons of waste had been deposited at the landfill site.

Moreover, GRN has been contracted by DAREH (the regional waste management authority) to provide waste collection and treatment activities in Békés county. These operations have been assigned to GRN's subcontractor and shareholder, Tappe Kft.

GRM joined the GRH group in 2021. Its main activity is waste material trading, which adds a new and growing segment to the group's operations.

Key metrics

			Scope estimates		
Scope credit ratios	2019	2020	2021E	2022E	2023E
EBITDA/interest cover (x)	68.1x	101.6x	51.1x	12.9x	16.5x
Scope-adjusted debt (SaD)/EBITDA	0.5x	0.4x	3.2x	2.3x	1.7x
Scope-adjusted FFO/SaD	165%	212%	28%	37%	51%
FOCF/SaD	182%	219%	2%	13%	37%

Rating rationale

Scope Ratings GmbH (Scope) has today assigned a first-time issuer rating of B+/Stable to Global Refuse Holding Zrt. (GRH). Scope has also assigned a first-time rating of B+ to senior unsecured debt issued by GRH.

Global Refuse's rating is driven by its strong financial risk profile, especially its strong ability to generate free cash flows driven by its strong position as a regional municipal waste management company.

Ratings & Outlook

Corporate ratings	B+/Stable
Short-term rating	NA
Senior unsecured rating	B+

Analyst

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Related Methodology

Corporate Rating Methodology: July 2021

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Outlook and rating change drivers

The Stable Outlook reflects Scope's view on GRH's comparatively stronger credit metrics over the next three years with a strong ability to generate free cash flows. The Stable outlook also considers GRH's considerable ability to deleverage after the proposed acquisition, with a leverage expectation of not above 4.0x. The outlook is further driven by GRH's strong revenue generation capacity driven by its strong position as a regional municipal waste management company.

A positive rating action rating could be warranted if the group strengthened its size significantly through the proposed organic and inorganic growth opportunities.

A negative rating action could result from a deterioration in the group's leverage (Scope-adjusted debt/EBITDA) above 4.0x for a prolonged period, as the result of a contracted profitability or a further increased debt profile.

Rating drivers

Positive rating drivers	Negative rating drivers
• Leader in municipal waste management in the Békés county • Increasing need for recycling, especially for industrial waste • Long-term contracts with a high likelihood of being renewed • Large exposure to municipal waste collection and transportation, which is less volatile • Sole operator of the Békéscsaba regional waste disposal plant since 1996 (BVÜ) • The planned organic growth related project in the field of recycling provides substantial growth potential to the group	• Geographically limited to one region of Hungary (very limited diversification) • Use of landfill (credit-negative ESG factor) • Sub-sovereign counterparty risk as contracts are signed with the regional waste management authority DAREH (only recently developed), which is part of the Hungarian national municipal waste management system • Regulatory changes proposed for July 2023 create some uncertainty with regard to current contracts • Very volatile cash flow cover, constrained by high debt-funded capex needs

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Strengthened BRP through the potential acquisitions, possibility of having the -1 notch adjustment removed in the peer context and achieving a SaD/EBITDA of not above 4.0x	• SaD/EBITDA increasing above 4.0x over a prolonged period

Financial overview

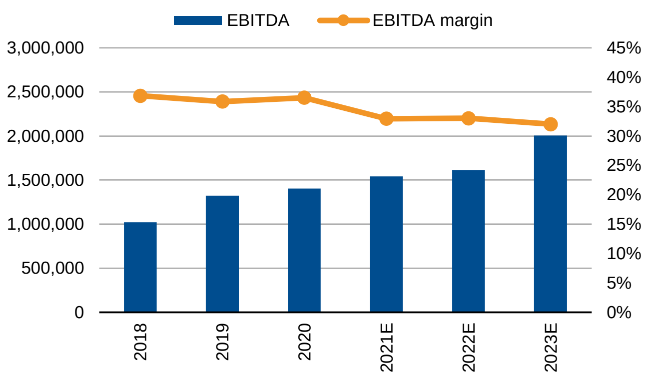
			Scope estimates		
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**	**2023E**
EBITDA/interest cover (x)	68.1x	101.6x	51.1x	12.9x	16.5x
Scope-adjusted debt (SaD)/EBITDA	0.5x	0.4x	3.2x	2.3x	1.7x
Scope-adjusted funds from operations/SaD	165%	212%	28%	37%	51%
Free operating cash flow/SaD	182%	219%	2%	13%	37%
Scope-adjusted EBITDA in HUF ‘000s	**2019**	**2020**	**2021E**	**2022E**	**2023E**
EBITDA	1,324,334	1,403,673	1,540,714	1,612,155	2,005,653
Operating lease payments in respective year	-	-	-	-	-
add: share of current net income from joint ventures and associates	-	-	-	333,282	369,806
Scope-adjusted EBITDA	1,324,334	1,403,673	1,540,714	1,945,437	2,375,459
Scope-adjusted funds from operations in HUF ‘000s	**2019**	**2020**	**2021E**	**2022E**	**2023E**
EBITDA	1,324,334	1,403,673	1,540,714	1,945,437	2,375,459
less: (net) cash interest as per cash flow statement	-19,712	-13,897	-30,225	-150,846	-143,743
less: cash tax paid as per cash flow statement	-108,778	-53,544	-126,608	-143,172	-174,374
add: share of current net income of joint ventures and associates	-	-	-	-	-
Scope-adjusted funds from operations	1,195,844	1,336,231	1,383,880	1,651,419	2,057,343
Scope-adjusted debt in HUF ‘000s	**2019**	**2020**	**2021E**	**2022E**	**2023E**
Reported gross financial debt	582,823	455,182	4,681,870	4,261,895	3,871,239
less: hybrid bonds	-	-	-	-	-
less: cash and cash equivalents	-	-	-	-	-
add: cash not accessible	-	-	-	-	-
add: pension adjustment	-	-	-	-	-
add: operating lease obligations	-	-	-	-	-
Asset retirement obligation	141,000	175,000	176,875	178,656	180,348
Scope-adjusted debt	723,823	630,182	4,858,745	4,440,551	4,051,587

Business risk profile

Business risk profile assessed at B+

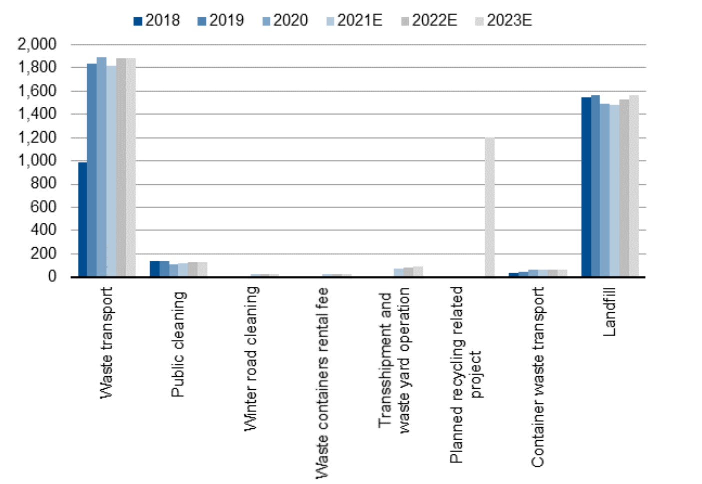
GRH's business risk profile is supported by the added cash-flow generation capacity created by near-term organic growth opportunities. This is further driven by the increasing need for recycling, especially of industrial waste, in line with global sustainability megatrends with regard to a circular economy (positive ESG factor). GRH's market position is secured by its regional key player position in municipal waste management in the Békés region in Hungary, despite its rather limited size. The group's cash flows are protected by its large exposure to municipal waste collection and transportation, which is less volatile, and long-term contracts with a high likelihood of being renewed, given the limited competition in the service territory.

Figure 1: EBITDA and EBITDA margins 2018-2023



Source: GRH, Scope

Figure 2: Revenue breakdown per segment 2018-2023 (HUF m)



Source: GRH, Scope

Well-represented throughout the waste management value chain

GRH's geographical diversification remains limited to a single region in Hungary. However, the group is improving diversification in its services portfolio by combining supplementary business services, such as winter road cleaning, waste container rental and waste yard operations, with its municipal waste management segment. The newest addition to the group, GRM, which is active in waste material trading, together with the planned project related to recycling are expected to bring substantial growth potential to the group.

Limited geographical and contract diversification

With GRH serving about 92% of the region's population and operating the only major landfill site in Békés county, the group holds a strong position in its service territory. However, diversification of contracts by source is weak. Almost all of the group's contracts are municipal contracts and there are no existing major contracts with industrial clients, signalling some customer concentration risk.

Margin profile is expected to improve

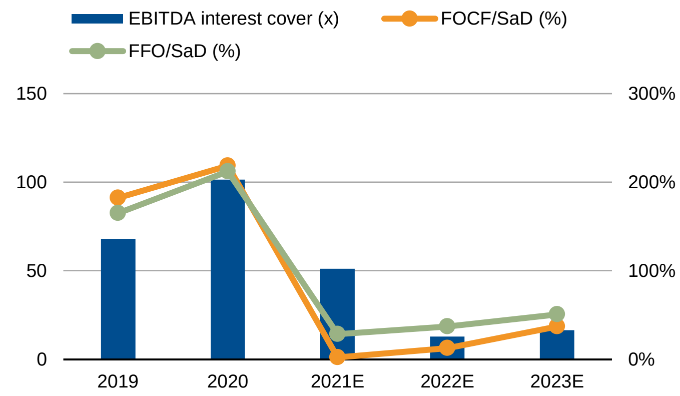
The sustainability of landfill – the group's highest margin activity – is questionable due to the EU's intention and directives to decrease the volume of landfill waste. This activity also creates some margin concentration. The newest addition to the group, GRM, which is active in waste material trading, together with the planned project related to recycling are expected to bring substantial growth potential to the group. However, these additional businesses will only lead to an EBITDA margin of about 32% due to high pressure from significantly increasing material and staff expenses.

Financial risk profile

Financial risk profile hindered by high leverage and volatile free operating cash flow

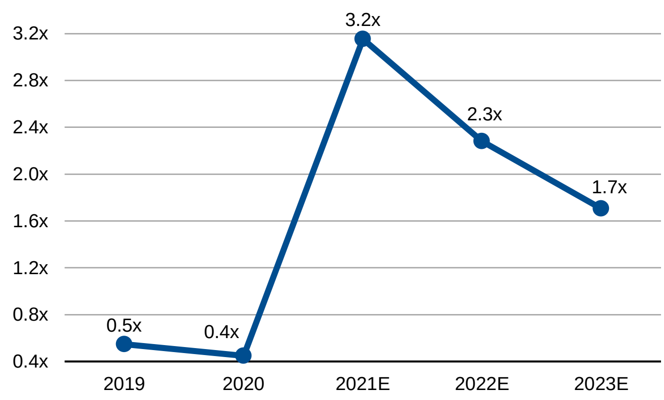
GRH's financial risk profile is stronger than its business risk profile driven by GRH's comparatively stronger credit metrics over the next three years with a strong ability to generate free cash flows. Our view also considers GRH's significant ability to deleverage after the proposed acquisition. Despite good debt protection and solid leverage, the group's financial risk profile is constrained by its relatively low cash flow cover. Scope's rating case incorporates the group's plans to issue a HUF 3.5bn senior unsecured corporate bond under the MNB Bond Funding for Growth Scheme. Scope assumes that the planned bond will have a fixed-rate coupon with a 10-year tenor followed by amortisation from fifth year, with a 50% bullet payment at maturity. Proceeds from the bond are earmarked to finance an acquisition. Scope expects GRH's financial leverage ratio to remain in the 1-3x range and its interest cover ratio to be above 12x in the next three-year period.

Figure 3: Scope-adjusted debt protection and cash flow cover



Source: GRH, Scope

Figure 4: Scope-adjusted leverage



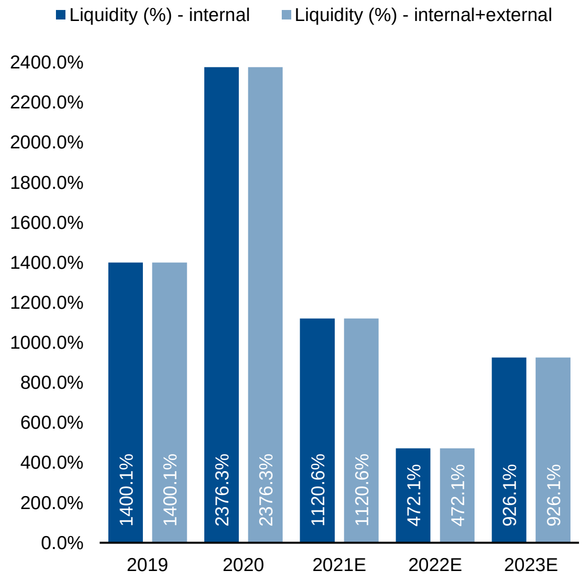
Source: GRH, Scope

Adequate liquidity

GRH's liquidity, as measured by internal and external liquidity, remains above 100% at all times. This has even been the case in 2021, when liquidity has been constrained by low free operating cash flow due to the high capex needs for the planned recycling related project. Therefore, we do not envisage any difficulty in the timely reimbursement of GRH's debt schedule, which remains fairly well balanced over the next three-year period.

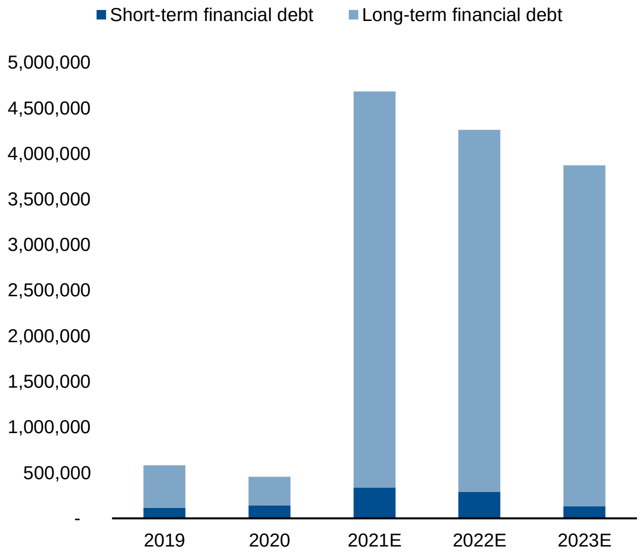
Liquidity is also adequate based on the group's good relationships with banks, as demonstrated by the current diversified set of loan facilities (working capital and other) and its good working capital management strategy. This view is also supported by GRH's unrestricted cash balance of HUF 1.5bn in 2020. However, GRH does not have any revolving credit facilities at present.

Figure 5: Liquidity



Source: GRH, Scope

Figure 6: Debt composition 2018-2023 (HUF m)



Source: GRH, Scope

Supplementary rating drivers

GRH's limited size and outreach compared to other entities rated in the BB rating category hinder it to exceed the assigned B+ issuer rating (reflected by a negative one notch adjustment on the standalone rating).

The financial policy is rating neutral. Moreover, we did not encounter any risk factors related to GRH's governance. Its governance is supported by a well experienced and committed top management. Thus, we assess GRH's governance to be rating neutral.

The minority shareholder - Ferenc Figura engages in executive management of the company and he will continue to remain in the management, and thus there is no key-person risk attached to the owners.

Long-term debt ratings

Scope expects an 'average' recovery for senior unsecured debt, for instance the HUF 3.5bn bond issued under the Hungarian National Bank's programme. This recovery expectation translates into a B+ rating for the senior unsecured debt category, at the same level as the issuer rating. Scope's recovery expectations are based on an anticipated liquidation value in a hypothetical default scenario at the end of 2023. Short-term and long-term debt (excluding the bond issue) raised from financial institutions, other financial liabilities such as tax and interest payables, as well as trade payables rank higher than senior unsecured debt. Hence, such debts would be repaid first.

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