12 November 2024

Corporates

Kometa 99 Zrt.
Hungary, Consumer Products

B+ STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2022**	**2023**	**2024E**	**2025E**
Scope-adjusted EBITDA/interest cover	35.5x	Net cash interest received	7.9x	5.1x
Scope-adjusted debt/EBITDA	4.5x	4.5x	4.6x	4.7x
Scope-adjusted funds from operations/debt	26%	28%	18%	17%
Scope-adjusted free operating cash flow/debt	-1%	5%	-8%	-28%

Rating rationale

The issuer rating reflects Kometa's moderate business risk profile (assessed at BB-) and weaker financial risk profile (assessed at B+) with adequate liquidity. Supplementary rating drivers are credit-neutral.

The business risk profile remains indicative of Kometa's moderate market position, resilient demand in its industry, concentration on domestic sales and pork products, and a low-margin business that is highly dependent on livestock prices. However, profitability is partly supported by the operational efficiency afforded by having all production processes in one facility. Kometa's margin is also stabilising due to the acquisition of pig breeder Triagro Kft. at the end of 2023, which enhances vertical integration.

The financial risk profile continues to reflect high leverage and weak cash flow cover, with the latter expected to deteriorate further due to the deployment of large project capex from 2024. These are only partly offset by good EBITDA interest cover and a solid liquidity buffer.

Outlook and rating-change drivers

The Stable Outlook reflects our expectation that debt/EBITDA will remain below 5.0x despite the deployment of significant expansionary capex from 2024 onwards which will be primarily covered by existing cash reserves, with no significant cost overruns or delays expected. The Outlook assumes that EBITDA will remain above HUF 5bn per year and will show a less volatile pattern thanks to the recent consolidation of the subsidiary pig breeder Triagro Kft.

A positive rating action could be triggered if Scope-adjusted debt/EBITDA improves to or below 3.5x on a sustained basis, coupled with positive Scope-adjusted free operating cash flow (FOCF)/debt.

A negative rating action could occur if Scope-adjusted debt/EBITDA deteriorates to over 5.0x on a sustained basis or EBITDA interest cover weakens to below 4.0x.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
12 Nov 2024	Affirmation	B+/Stable
13 Nov 2023	Affirmation	B+/Stable
15 Nov 2022	Affirmation	B+/Stable
21 Dec 2021	New	B+/Stable

Ratings & Outlook

Issuer	B+/Stable
Senior unsecured debt	B+

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Related Methodologies

General Corporate Rating Methodology; October 2023

Consumer Products Rating Methodology; October 2024

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Bloomberg: RESP SCOP

Positive rating drivers	Negative rating drivers
• Third largest pork meat processor in Hungary, with a strong domestic position in selected categories, such as modified atmosphere packaging (MAP) meat and cold cuts • Resilience of the consumer food sector, as demonstrated during the Covid-19 pandemic • Comfortable liquidity cushion, supported by prudent decision to postpone expansionary capex in 2022 and 2023 while parking a significant portion of recent bond proceeds in fixed-term deposits • Higher operational efficiency compared to local peers as slaughtering and processing activities are performed in a single location. • Extensive diversification across pork products • Increased vertical integration after acquisition of affiliate livestock breeder Triagro	• High leverage and weak FOCF in the medium term amid expansionary capex • Still small absolute size • Limited inherent profitability of core business (fresh meat), with only around 20% of quantities coming from the higher-value-added processed products segment • Historically volatile and price-dependent margins, highly dependent on raw material prices (primarily pork prices) • Competitive industry despite good position in some meat categories; still limited bargaining power with large international food retailers, especially abroad • Limited diversification outside pork products (some processed turkey products) • Concentration on Hungary for almost 60% of revenues; reliance on a few export countries (Italy, Croatia, Slovenia) • Moderate dependency on top customer Lidl for around 15%-20% of sales in recent years • Relatively weak brand value, as the core business is mostly based on private-label agreements (conversely, around 70% of processed products are branded Kometa) • Tail risk, with asset concentration in one plant

Positive rating-change drivers	Negative rating-change drivers
• Scope-adjusted debt/EBITDA sustained at or below 3.5x and positive Scope-adjusted FOCF/debt	• Scope-adjusted debt/EBITDA sustained above 5.0x • Scope-adjusted EBITDA interest cover below 4.0x

Corporate profile

Kometa 99 Zrt. was established in 2000 and is owned by the Pedranzini and Ruffini families. It is one of Hungary's largest meat processing companies, ranking among the top three in pork processing. The company operates in Kaposvár, in one of the most modern and efficient processing plants in Central Europe. All production processes (slaughtering, butchering, meat processing and packaging) occur under one roof, recently reinforced by a new by-product processing plant. In addition, Kometa acquired the entirety of shares in Hungary-based affiliate Triagro in 2023, extending its activities into pig breeding.

Processing activities are divided into two segments: meat and processed products. The meat segment (roughly 80% of volumes sold) sells unprocessed meat including fresh, frozen, MAP meat and food service industry products. The processed product segment sells a variety of pork and poultry products, including cold cuts, ham, salami and sausages. Clients operate in food retail, hospitality and meat processing. Kometa exports to over 40 countries, with exports accounting for around 40% of sales. The company's main export markets in order of size are Italy, Croatia, Slovenia and Germany.

Financial overview

				Scope estimates		
Scope credit ratios	**2021**	**2022**	**2023**	**2024E**	**2025E**	**2026E**
Scope-adjusted EBITDA/interest cover	8.4x	35.5x	Net cash interest received	7.9x	5.1x	4.7x
Scope-adjusted debt/EBITDA	3.2x	4.5x	4.5x	4.6x	4.7x	4.6x
Scope-adjusted funds from operations/debt	29%	26%	28%	18%	17%	17%
Scope-adjusted free operating cash flow/debt	4%	-1%	5%	-8%	-28%	-22%
Scope-adjusted EBITDA in HUF m						
EBITDA	3,177	2,886	3,187	5,013	5,304	5,747
Operating lease payments	116	156	242	250	250	250
Gains/losses on disposals	4	(13)	46	-	-	-
Scope-adjusted EBITDA	**3,296**	**3,029**	**3,475**	**5,263**	**5,554**	**5,997**
Funds from operations in HUF m						
Scope-adjusted EBITDA	3,296	3,029	3,475	5,263	5,554	5,997
less: (net) cash interest paid	(390)	(85)	671	(664)	(1,098)	(1,287)
less: cash tax paid per cash flow statement	(86)	(90)	(211)	(169)	(144)	(124)
add: dividends from associates	-	-	-	-	-	-
Other items (mainly changes in provisions)	263	654	458	-	-	-
Funds from operations (FFO)	**3,082**	**3,508**	**4,393**	**4,430**	**4,312**	**4,586**
Free operating cash flow in HUF m						
Funds from operations	3,082	3,508	4,393	4,430	4,312	4,586
Change in working capital	(982)	(954)	(1,753)	(793)	(836)	(993)
Non-operating cash flow	-	-	-	-	-	-
less: capital expenditure (net)	(1,628)	(2,618)	(1,726)	(5,440)	(10,540)	(9,520)
less: lease amortisation	(95)	(132)	(199)	(206)	(206)	(206)
Free operating cash flow (FOCF)	**377**	**(197)**	**715**	**(2,008)**	**(7,270)**	**(6,132)**
Net cash interest paid in HUF m						
Net cash interest per cash flow statement	370	61	(714)	619	1,053	1,243
add: interest component, operating leases	20	24	43	44	44	44
Change in other items	-	-	-	-	-	-
Net cash interest paid	**390**	**85**	**(671)**	**664**	**1,098**	**1,287**
Scope-adjusted debt in HUF m						
Reported gross financial debt	10,019	19,115	22,339	27,145	27,146	27,146
less: subordinated (hybrid) debt	-	-	-	-	-	-
less: cash and cash equivalents	-	(6,000)	(7,454)	(3,974)	(2,157)	(624)
add: non-accessible cash	-	-	-	-	-	-
add: pension adjustment	-	-	-	-	-	-
add: operating lease obligations	410	553	858	886	886	886
Other items (contingencies)	55	28	-	-	-	-
Scope-adjusted debt (SaD)	**10,484**	**13,696**	**15,743**	**24,058**	**25,876**	**27,409**

Table of Content

Environmental, social and governance (ESG) profile[1]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend

Green leaf (ESG factor: credit positive)

Red leaf (ESG factor: credit negative)

Grey leaf (ESG factor: credit neutral)

Limited ESG risks

Although Kometa is exposed to several relevant ESG factors, these are credit-neutral for the time being. In general, the key environmental risks for a meat processor come from intensive energy and water consumption in the production process as well as carbon emissions, especially from livestock breeding. On the social side, the major risks are decreasing meat consumption and litigation and/or reputational risks related to product safety and animal welfare (supply chain control).

Investment in sustainability

Kometa's environmental investments in a water treatment plant and a by-products plant support a better use of raw materials and the circular economy, while also benefiting operating efficiency to a certain extent. On the social side, Kometa has initiated the Honest Food/Honest Pig programme, which consists of animal welfare certifications and the reduced use of antibiotics. The issuance of a green bond indicates a sustainable path, which will involve further green investments, including the construction of more energy-efficient technologies and the installation of solar panels.

[1] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BB-

The business risk profile remains indicative of Kometa's moderate market position, resilient demand in its industry, concentration on domestic sales and pork products, and a low-margin business that is highly dependent on livestock prices. However, profitability is partly supported by the operational efficiency afforded by having all production processes in one facility. In addition, Kometa's EBITDA margin is stabilising due to the acquisition of pig breeder Triagro at the end of 2023, which enhances vertical integration.

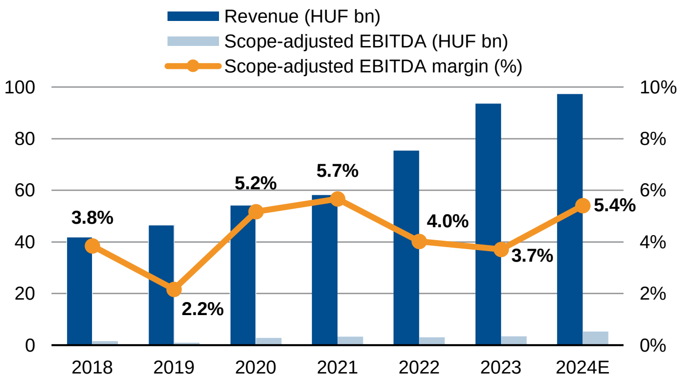
Blended industry risk profile: A-

Kometa acquires livestock and meat mostly from suppliers (which breed and feed the animals) and subsidiary Triagro (pig breeder). The company then slaughters, processes and packages the final product. In view of Kometa's business model and recent acquisition of Triagro at the end of 2023, we applied a blended industry profile of non-discretionary consumer products and agriculture, based on the EBITDA breakdown of the respective businesses. The industry risk profile for non-discretionary consumer products is rated A, based on low cyclicality, medium market entry barriers and low substitution risk. The industry risk profile for agriculture is BBB, based on high cyclicality, high market entry barriers and low substitution risk.

Increasing capacity

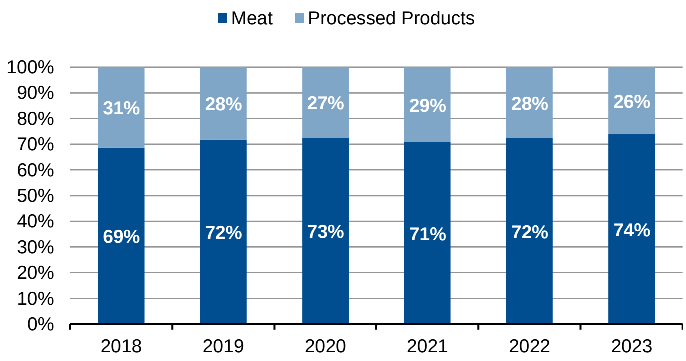
Kometa has a yearly production capacity of one million pigs for slaughtering and processing. Its meat segment has a capacity of 80,000 tonnes/year (planned to increase by 50% in the long term), and its processed products segment has a capacity of 17,000 tonnes/year (planned to increase by 200% in the long term). With around 1,000 employees and HUF 94bn of revenue in 2023 (around EUR 240m), Kometa is one of the largest employers in the Hungarian counties of Kaposvár and Somogy (reflected by the minority municipal shareholders). However, it is still small in an international context.

Figure 1: Revenues and EBITDA development



Sources: Kometa, Scope

Figure 2: Revenue split by segment



Sources: Kometa, Scope

Top third pork processor in Hungary

Kometa has been growing faster than its peers in recent years and now ranks third in Hungary in terms of volume of pork sold. Of the other top three companies, Pick focuses on the processed products segment, where it dominates the traditional Hungarian winter salami product category, while Hungary Meat operates in the fresh meat segment.

Size and pressure from large international discounters still constrain market position

Our market share assessment factors in Kometa's small absolute size and the competitive nature of its business, including margin pressure from large food retailer customers. The company will be able to improve its market position once it expands production and establishes itself as a reliable large-scale meat supplier in Hungary and abroad.

Leader in domestic MAP meat, weaker in processed products

Kometa's market shares are best assessed by considering specific product categories. Within the meat segment, Kometa dominates domestically in MAP (modified atmosphere packaging) meat, commanding around 70% of the Hungarian market. This category is still relatively underpenetrated, as it makes up only around 20% of total meat sales. It is worth noting that MAP (along with the food service industry) is one of the two highest-margin product categories in meat, together with gastro (convenience products). Within processed products, Kometa is active in several categories, but its overall position is weaker than in its core meat business. Kometa's highest domestic market share is in cold cuts (above 20%). Other product categories rank substantially lower.

Partial vertical integration affords production flexibility

Partial vertical integration between meat and processed products, along with the company's concentration of production in one location, provides advantages over competitors in terms of flexibility, since it allows Kometa to switch production between different products (e.g. meat versus processed products) to follow market demand. Owning the spice-mixing technology also allows Kometa to switch between different types of production and reduces dependence on procurement, since it can source the raw spices directly.

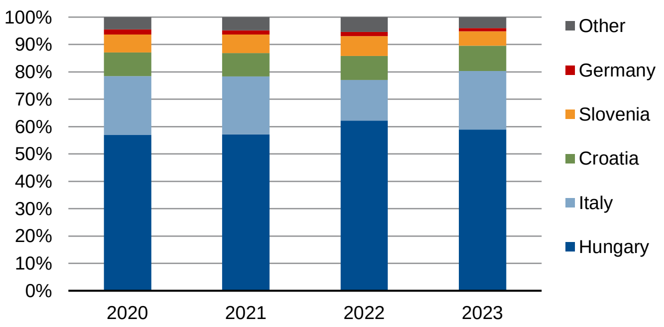
Limited bargaining power

Kometa has limited bargaining power, especially with its main customers, which are large international discounters and hypermarkets. Size matters to large customers as they need reliable suppliers to provide large quantities. Kometa is becoming an increasingly strategic partner for Lidl in the region and has gained permanent positions for Kometa-branded products with the discounter as well as with other discounters. The superior growth of discounters in Hungary compared to other retailers has helped increase Kometa's market share in the past couple of years.

Around 60% reliance on domestic sales

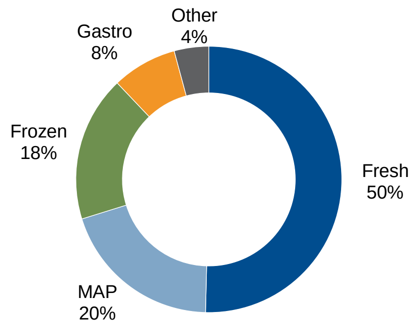
Exports made up around 40% of sales in 2023, stable year-on-year. Although Kometa exports to over 40 countries, sales are concentrated in just a few, with Italy the largest (around 20% of total sales) followed by Croatia and Slovenia. Abroad, the issuer's overall market position is more limited, with some exceptions for specific products (for example, roasted turkey breast ham in Italy). Kometa plans to increase sales in Italy, expand in Germany (thanks to increasing production from affiliate Zito) and Spain (which saw good progress in H1 2024), and increase MAP sales in Croatia and Slovenia.

Figure 3: Geographical split of sales



Sources: Kometa, Scope

Figure 4: Volume split within meat segment (2023)

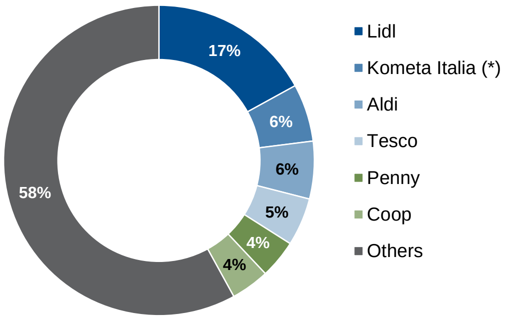


Sources: Kometa, Scope

Key role of large international food retailers

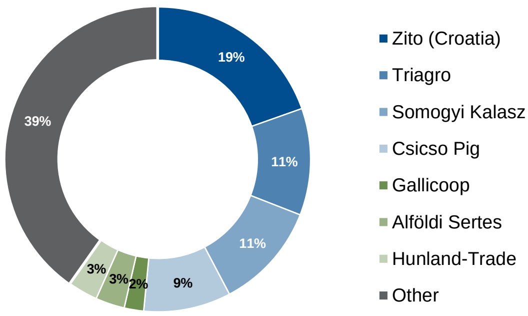
Kometa's customer base is moderately diversified and includes several hundred partners, but large international food retailers hold a key position. Other clients include small, domestic retail chains, meat processors and wholesalers serving the hospitality industry. The top five customers accounted for less than 40% of sales in H1 2024, the largest being Lidl at 17%. In Hungary, customer concentration is noticeable in meat: Lidl (37%) and Aldi (11%) together account for around 45% of sales and the top five account for almost 70%. Local processed product sales have a slightly more granular customer base, with the top three (Lidl, Coop and Tesco) accounting for around 40% of sales and the top five for around 55%. In exports, customer structure is more diversified, Kometa Italia being the largest client. It effectively acts as a distributor to the Italian market, covering over 200 clients, including small wholesalers and clients within the hotel, restaurant and catering industries.

Figure 5: Top customers (H1 2024)



(*) Kometa Italia distributes to over 200 hospitality industry clients in Italy.
Sources: Kometa, Scope

Figure 6: Top livestock suppliers (H1 2024)



Sources: Kometa, Scope

Moderate supplier concentration, partially integrated via Triagro

Kometa's key raw materials are livestock and meat, and pork prices are based on weekly market data from Germany (ZMP). The company has over 150 suppliers, with the top five accounting for around 50% of its total livestock supplies in H1 2024. By agreeing to acquire the totality of shares in pig breeder Triagro at the end of 2023, Kometa is now vertically integrated across its value chain, providing around 11% of its livestock needs. Auxiliary materials – including packaging – represent a much smaller portion (less than 10%) of livestock costs and have a more diversified distribution.

Strategic alliance with largest livestock supplier Zito

Kometa has a strategic partnership with Zito, based on which the export sales from its meat processors are channelled through Kometa (excluding ex-Yugoslavian territories). Additionally, the partnership gives Kometa a secure source of livestock for its own production, providing around 20% of its needs. Nevertheless, an unexpected termination of this strategic partnership could have moderate negative short-term effects on production levels.

Highly diversified and flexible pork production, complemented by poultry

Although most of its sales are pork, Kometa's major strengths compared to peers include its ability to produce a large variety of products from pork and use every part of the animal except its blood. Nails and fur, along with other meat waste, are processed in the by-products facility to produce meat powder and industrial lard, mostly for pet food. Less popular parts, such as the head and legs, are sent to the Asian market. In addition to pork, Kometa sells processed poultry products, which are not slaughtered in house. The poultry category has been gradually increasing and Kometa expects it to reach nearly 10% of sales in the long term.

Fresh meat segment represents over 70% of sales

The company offers a dozen fresh meat product groups and even more within processed products. Within the meat segment, the volume of value-added products produced in 2023 included 20% for MAP products and 8% for gastro products, while the remainder was lower-margin fresh or frozen meat. Within the processed products segment, Kometa's product portfolio is diversified and includes cold cuts, hams (including poultry meat), salami, sausages, Parisian ham and bacon.

Distribution mostly via food retailers

Kometa's distribution channels are quite concentrated, with around two-thirds distributed to retailers. There is a wide variety among retailers, which primarily include large international discounters (especially for meat), hypermarkets and cash and carry (especially for processed products), but also local retail chains. The remainder comprises meat processors and distributors for the hospitality sector. Online sales are not available.

Assets concentrated in one location

Asset concentration in one plant somewhat constrains the overall diversification assessment. While running everything under one roof does save on costs, a catastrophic event in the Kaposvár plant could disrupt the business.

Profitability sensitive to livestock price volatility

Kometa’s profitability remains volatile and susceptible to changes in raw material prices. The purchase of livestock and meat makes up a large share of costs at around 68% of revenue in 2023 (aggregate cost of goods sold: around 85% of revenue in 2023). Prices are contracted weekly in meat but are negotiated three to four times a year in processed products, which is also due to the shorter expiration period of meat products (days/weeks) compared to processed products (months). This means that margins in the processed product segments are more volatile in case of steep and persisting changes in livestock prices. Product segmentation, along with strategic relations with suppliers Zito and Triagro, helps reduce price volatility.

Acquisition of Triagro partly mitigates dependency on livestock prices

The acquisition of Triagro will contribute to stabilising margins, given the complementary nature of pig breeding and slaughtering activities (pig price movements generally impact the profitability margins of these businesses in opposite ways). At the end of 2023, Kometa purchased the remaining 76% of Triagro's shares (adding to its previous 24%), with two payment instalments scheduled in the period to Q1 2024. The acquisition price was agreed at EUR 6.5m (HUF 2.5bn), 80% of which was financed through debt. However, the transaction was initially covered by internal funds, and the loan was only drawn in July 2024.

Meat segment has lower margins but is less volatile

The meat segment generally has lower margins than processed products but has been less volatile in recent years as it can adjust more quickly to livestock prices. However, it displays some seasonality, with the period between October and April being the strongest. In line with the general food industry, demand for Kometa’s products is resilient, with processed products facing more competition as they are more exposed to export markets. Within meat, the segments with higher marginality are MAP and gastro products. Both of these segments have increased their contribution to the company’s product mix in the past five years, with consequent improvements in the meat segment’s profitability.

Limited forex risk

Kometa is mostly a price taker, with exposure to foreign exchange movements being mostly limited to euros. Foreign exchange gains or losses have had a limited impact in the last few years; imports in euros (mainly from Croatia) are generally higher than euro export sales (mainly to Italy).

EBITDA margin down to below 4% in 2023 due to high livestock prices...

Scope-adjusted EBITDA rose to HUF 3.5bn in 2023, up from HUF 3.0bn in 2022, although the margin decreased slightly to 3.7% from 4.0%. This decline occurred because higher selling prices did not entirely offset the increases in pork prices and salaries. For the full year 2024, we predict that Scope-adjusted EBITDA will be roughly HUF 5.3bn, with the margin rising to over 5%. This improvement should come from a fall in raw material costs, which, although still high, will more than offset further increases in labour costs. Additionally, the consolidation of Triagro will enhance profitability, as the pig breeding business benefited from high pork prices and generated an EBITDA margin above 15% over the past two years.

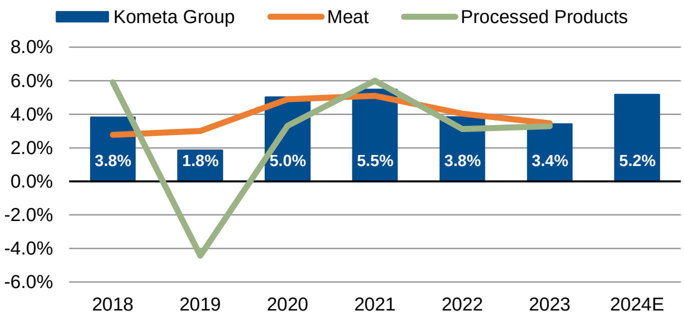
…but should improve and stabilise at around 5% thanks to Triagro acquisition

Going forward, we see Scope-adjusted EBITDA growing to HUF 6.0bn in 2026 thanks to volume growth, also supported by the utilization of the new Triagro site in Csemő and moderate export growth. The EBITDA margin is expected to stabilise, given that Triagro’s pig breeding operations complement Kometa’s existing slaughtering business. Typically, fluctuations in pig prices affect the profitability of these two segments inversely. Kometa has also made investments in energy-efficient technologies to lower costs.

Profitability margins are adequate based on product mix

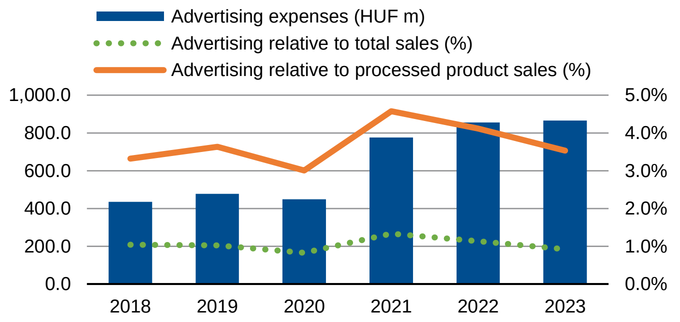
Overall, profitability is adequate based on the product mix, considering that slaughtering constitutes a drag on profitability. Kometa outperforms local peers within the meat segment, also thanks to its positioning in high-margin MAP meat. However, Kometa still has room to improve within processed products. It lags behind leader Pick (even including its unconsolidated slaughterhouse), which benefits from a stronger brand and a higher-value-added product (longer maturation for main salami product). It is also behind local peers that do not have slaughterhouses and focus on a single product.

Figure 7: EBITDA margin by segment



Sources: Kometa, Scope estimates

Figure 8: Advertising spending



Sources: Kometa, Scope

Having everything under one roof saves operating costs

Whilst differing business models among peers makes margins hard to compare, Kometa's single facility and newer technology provide operating cost savings. Its personnel and logistics costs are much lower and can be leveraged if production capacity increases as planned. However, the advantage in operating efficiency is partly offset by the company's broad product range, which constrains overall capacity utilisation more than if it focused on one standard process. Margins could reach near to 10% if the company expanded capacity significantly and increased its product mix towards processed products and added-value meat products while strengthening its brand.

Emerging brand within the processed products segment

Kometa's brand is still emerging. Fresh meat is a business primarily based on private labels and brand recognition is limited for end-consumers. The processed products segment is in the low to medium price range and tries to attract a younger customer group than more traditional brands such as Pick, while focusing on sustainability (efficient use of natural resources, support to local communities and animal welfare). The brand is known in Hungary but less so in its export markets. Within processed products, Kometa-branded products make up around 70% of sales, with an adequate investment in advertising over the past few years (averaging 4% based on processed product sales).

Financial risk profile: B+

Kometa's financial risk profile continues to reflect high leverage and weak cash flow cover, with the latter expected to deteriorate further due to the deployment of large project capex from 2024. These are only partly offset by good Scope-adjusted EBITDA interest cover and a solid liquidity buffer.

Key adjustments

Our key adjustments to credit metrics include:

- EBITDA adjusted for operating lease payments of HUF 250m per year;
- Capex considered net of received subsidies (assumed at 40% of project capex);
- Netting of cash: 45% of cash is netted from debt until 2023, 25% from 2024 to reflect the deployment of capex;
- Debt includes operating lease adjustments of around HUF 0.9bn per annum;
- Interests include HUF 44m of operating lease interests per annum.

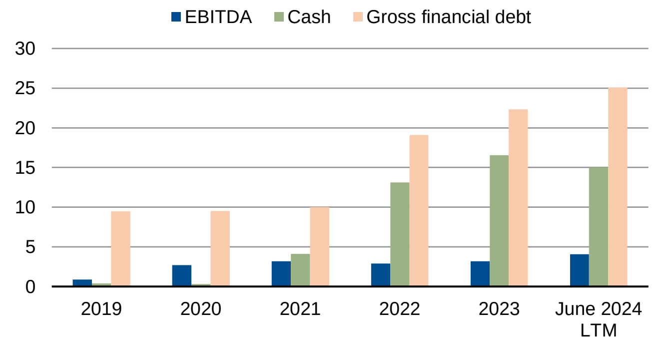
HUF 12bn bond issued in 2022

Kometa issued a HUF 12bn green bond under Hungary's Bond Funding for Growth Scheme in February 2022. The bond has a tenor of 10 years with 10% of its face value subject to amortisation in 2027, 10% yearly in 2028-2031 and the remaining 50% in 2032. The coupon of 5% is fixed and payable yearly, which is beneficial in the current high-interest rate environment in Hungary. Funds from the bond will be mainly used for investments to expand production capacity and to replace around HUF 2bn of existing long-term investment loans.

Scope-adjusted debt/EBITDA to remain below 5x

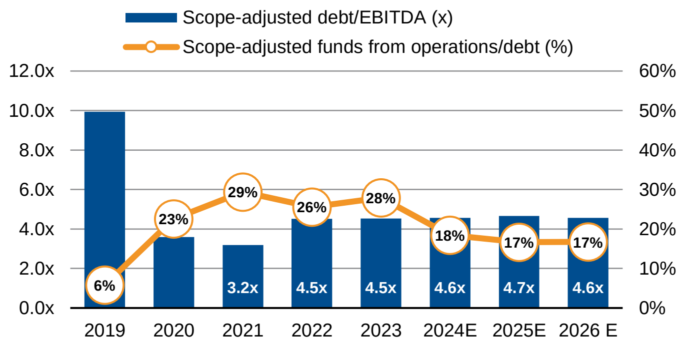
Scope-adjusted debt/EBITDA was stable at 4.5x in 2023 with higher EBITDA compensating for the rise in debt. As in last year's review, we expect gross financial debt to rise by approximately HUF 5bn in 2024, reaching HUF 27bn and staying relatively stable thereafter. This should ensure that the Scope-adjusted debt/EBITDA ratio remains under 5.0x in the medium term (with the application of a lower cash netting of 25% from 2024, since cash is projected to be largely used up by 2026). Leverage is supported by Scope-adjusted funds from operations/debt, which is expected to range between 15% to 20% over time.

Figure 9: Reported EBITDA, cash, gross debt (HUF bn)



Sources: Kometa, Scope

Figure 10: Scope-adjusted leverage metrics

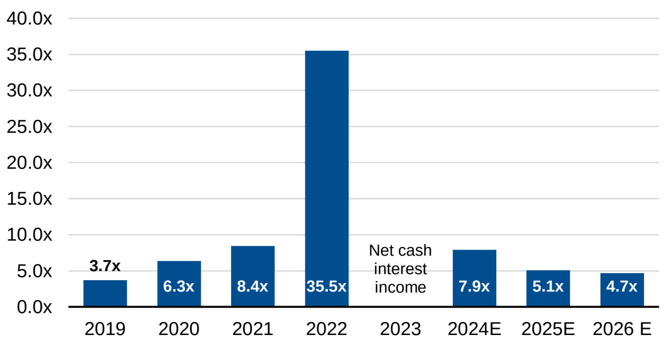


Sources: Kometa, Scope estimates

Good EBITDA interest cover on high interest income

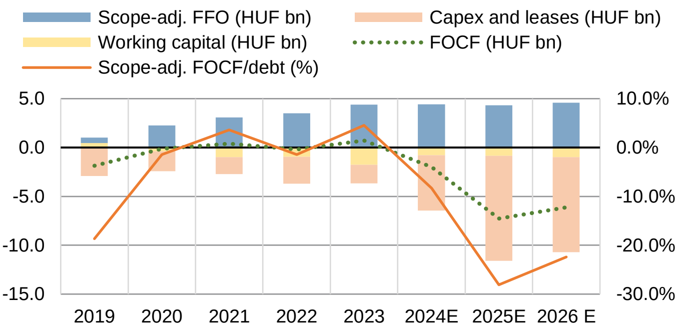
EBITDA interest coverage was notably strong in 2023 due to an outstanding net interest income of HUF 0.7bn. Considerable interest income of HUF 1.8bn was derived from substantial liquid assets (primarily related to unused proceeds from the bond issued in 2022), which were temporarily parked mostly in high-yield fixed-term deposits earning rates above the borrowing cost. Nonetheless, Kometa initiated its multi-year expansionary capex plan in 2024, targeting a substantial increase in the production capacity at its Kaposvar facility, primarily financed through existing cash reserves. The initial phase of this project focuses on enhancing logistics and slicing capacities and entails a total investment of approximately HUF 31bn by the end of 2026. Due to the combined effect of declining cash reserves and falling interest rates, Scope-adjusted interest is forecasted at roughly HUF 0.7bn in 2024, increasing to approximately HUF 1.1bn in 2025 and HUF 1.3bn in 2026. Consequently, we expect Scope-adjusted EBITDA interest coverage to decline to nearly 8x in 2024 and further weaken to around 5x in the medium term.

Figure 11: EBITDA interest cover



Sources: Kometa, Scope estimates

Figure 12: Cash flow cover (%), cash flows (HUF bn)

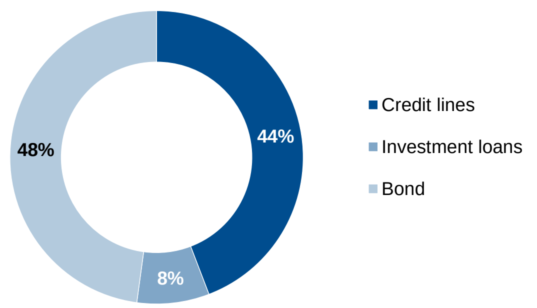


Sources: Kometa, Scope estimates

Weak FOCF to deteriorate further on expansionary capex

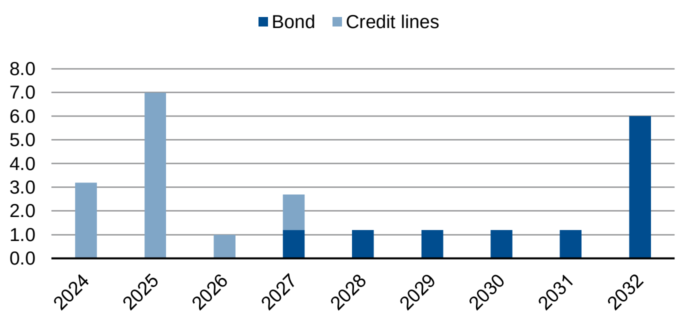
Due to low profitability and substantial working capital and capex needs, Scope-adjusted FOCF/debt has generally been weak in the last few years, oscillating between slightly negative values and 5%. With the deployment of large project capex from 2024, we predict persisting and largely negative Scope-adjusted FOCF over 2024-2026. This assumes net capex ranging between HUF 5.0bn and HUF 10.5bn per year (capex acceleration in 2025) after deducting subsidies received (subsidies assumed at around 40% of the investment projects), compared to an average of HUF 2bn over the past three years. Cash outflows for 2024 also include around HUF 2bn for the acquisition of the remaining shares in subsidiary Kometa Italia (which was already 51% owned).

Figure 13: Interest bearing debt split as of June 2024



Sources: Kometa, Scope

Figure 14: Debt maturity schedule (excluding leases) as of June 2024 (HUF bn)



Sources: Kometa, Scope

Adequate liquidity

Liquidity is adequate and supported by cash and equivalents of HUF 15bn as of June 2024 (versus HUF 17bn as of December 2023), a strong liquidity buffer against around HUF 3bn of short-term maturities in 2024 and HUF 7bn in 2025. We expect liquidity ratios to stay above 110% over the forecast period.

Balance in HUF m	2024E	2025E	2026E
Unrestricted cash (t-1)	16,565	15,897	8,628
Open committed credit lines (t-1)	-	-	-
Free operating cash flow	(2,008)	(7,270)	(6,132)
Short-term debt (t-1)	3,194	6,999	1,000
Coverage	**>200%**	**123%**	**>200%**

Financial covenants

We expect Kometa to remain in compliance with the financial covenants related to its senior secured debt. These include a net debt/EBITDA ratio of below 6x and a debt service coverage ratio above 1.25x.

We note that Kometa's senior unsecured bond issued under the Hungarian National Bank's Bond Funding for Growth Scheme has a covenant requiring the accelerated repayment of the outstanding nominal debt amount (HUF 12bn) if the debt rating of the bond stays below B+ for more than two years (grace period) or drops below B- (repayment within 15 days). Such a development could adversely affect the company's liquidity profile. There is limited rating headroom as the senior unsecured bond is rated B+, the same level as the issuer rating. This means that a downgrade of the issuer rating or worsening recovery expectations, for example due to an increase in secured debt, may result in a downgrade of the bond, which would trigger the rating deterioration covenant.

Supplementary rating drivers: +/- 0 notches

Financial policy

Management delayed capex in 2022 and 2023 to preserve liquidity and comply with its net debt/EBITDA target of below 4x. Its approach towards discretionary spending is also conservative: in recent years, management has only pursued a few small acquisitions of established business partners (the acquisition of Triagro follows this logic) and has not been distributing dividends to founding shareholders.

Parental support

We assume no impact from parent support, although the founding families and majority shareholders have shown a commitment to growing the business. Moreover, owners include government-related entities, but these stakes do not affect the rating as they are either temporary (MFB Invest's 18% stake) or minor (the Municipality of Kaposvar's 3.7%).

Corporate structure

The majority shareholders are the founding families of Pedranzini (54% via Komfin) and Ruffini (17% via Ruf Carni). HUF 5bn in equity was injected in 2021 when the Hungarian development bank's subsidiary MFB Invest (18%) and Zito (7.7%) became shareholders. This was accompanied by a partial exit of the other (historical) minority shareholder, the City of Kaposvár, which reduced its stake to 3.7%. The equity participation from Zito was dissolved in 2023. As of June 2024, Kometa owns 100% of consolidated subsidiaries Kometa Italia Srl and Triagro (fully consolidated by end-2023 after the acquisition of the remaining 76% of shares). Subsidiaries in Spain and Germany were established in 2022. Kometa also has minority ownership of smaller entities Pannon Pig Farm Kft. (consulting services) and Kaposvári Informatika Ágazati Képzőközpont Nonprofit Kft. (educational services).

Long-term debt rating

Senior unsecured debt rating: B+

The senior unsecured debt rating stands at B+, the same level as the issuer rating. This reflects an 'average' recovery in a hypothetical default scenario based on the liquidation value in 2026. We applied a conservative recovery assumption in view of the risk of additional secured debt entering the financing structure in case of a significant increase in capacity, as well the presence of real estate pledges for the subsidy providers (state-linked).

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