B+N Referencia Zrt.
Hungary, Business Services

BB- POSITIVE

Corporate profile

B+N Referencia Zrt. (B+N) is a facility management company operating in Hungary and CEE. It provides cleaning services, technical services, document management, uniform management, textile management, laundry services, winter works and horticulture services.

Key metrics

			Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**
EBITDA/interest cover (x)	>10.0x	>10.0x	>10.0x	>10.0x
Scope-adjusted debt (SaD)/EBITDA	1.9x	1.5x	1.9x	2.0x
Scope-adjusted FFO/SaD	50%	60%	47%	42%
FOCF/SaD	44%	189%	24%	30%

Rating rationale

Scope Ratings has upgraded B+N Referencia Zrt.'s issuer rating to BB- from B+ under review for a possible upgrade and changed the Outlook to Positive. Scope has also upgraded the senior unsecured debt rating to BB- from B+ in line with the issuer rating.

The rating action reflects the removal of the negative one-notch adjustment previously made for execution risk related to B+N's M&A activity (supplementary rating driver). The rating action also incorporates the company's improved business risk profile supported by robust credit metrics. The Positive Outlook reflects the strong likelihood that B+N's financial risk profile will improve based on its continued growth.

B+N's issuer rating benefits from two main factors: i) a robust financial risk profile supported by a dynamic growth rate and a large share of recurring revenues from procured contracts; and ii) the acquisition of the ISS Group's subsidiaries. These acquisitions have afforded B+N leading market positions in several regional countries while simultaneously lessening its geographical concentration and dependence on Hungarian state procurement contracts. Furthermore, the second bond issued under the Hungarian Central Bank's Bond Funding for Growth Scheme to finance the group's M&A activity is not expected to significantly impact credit metrics as it is partially offset by B+N's substantial growth. We thus forecast that leverage, as expressed by Scope-adjusted debt (SaD)/EBITDA, will deteriorate to around 2.0x for the medium term. The issuer rating is constrained by B+N's improved but still comparatively weak business risk profile, key person risk and limited transparency on its financial policy as regards dividend payments (ESG-related rating drivers).

Ratings & Outlook

Corporate ratings	BB-/Positive
Senior unsecured rating	BB-

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Related Methodology

Corporate Rating Methodology: July 2021

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Outlook and rating change drivers

The Outlook for B+N Referencia Zrt. is Positive and incorporates Scope's view of the strong likelihood that continued growth together with the successful integration of subsidiaries will improve the company's financial risk profile.

An upgrade could be warranted if SaD/Scope-adjusted EBITDA consistently trends below 2.0x. The rating could also benefit from an improvement in B+N's financial policy, which is, however, unlikely as this negative rating driver also reflects key person risk.

The Outlook could move to Stable if SaD/Scope-adjusted EBITDA consistently remains above 2.0x. A downgrade could be prompted by a deterioration in credit metrics, with SaD/EBITDA of above 3.5x, e.g. stemming from a loss of major contracts.

Rating drivers

Positive rating drivers	Negative rating drivers
• Strong growth: procurement contracts won (2-3 years in duration) afford good standing in the facility management market • Market leader in Hungary, with top market positions in several CEE countries • Stable profitability provides flexibility upon a downturn or when major contracts end • Robust financial risk profile	• Facility management market is highly fragmented and has low entry barriers • Weak diversification and concentration on Hungarian market with dependence on government-related entities • Limited transparency regarding financial policy • Key person risk

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• SaD/EBITDA below 2.0x on a sustained basis • More transparent financial policy	• SaD/EBITDA of above 3.5x on a sustained basis, e.g. due to loss of major contracts

Financial overview

			Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**
EBITDA/interest cover (x)	>10.0x	>10.0x	>10.0x	>10.0x
Scope-adjusted debt (SaD)/EBITDA	1.9x	1.5x	1.9x	2.0x
Scope-adjusted funds from operations/SaD	50%	60%	47%	42%
Free operating cash flow/SaD	44%	189%	24%	30%
Scope-adjusted EBITDA in HUF '000s	**2019**	**2020**	**2021E**	**2022E**
EBITDA	5,214,304	7,537,813	15,722,952	14,855,041
Operating lease payments in respective year	-	-	1,086	1,206
Other	-0	-9	-	-
Scope-adjusted EBITDA	5,214,304	7,537,804	15,724,038	14,856,246
Scope-adjusted funds from operations in HUF '000s	**2019**	**2020**	**2021E**	**2022E**
EBITDA	5,214,304	7,537,813	15,722,952	14,855,041
less: (net) cash interest as per cash flow statement	240,619	-290,057	-152,500	-992,000
less: cash tax paid as per cash flow statement	-481,664	-617,198	-1,342,045	-1,146,304
add: depreciation component, operating leases	-	-	869	965
Other	-0	-9	-	-
Scope-adjusted funds from operations	4,973,259	6,630,558	14,229,276	12,717,701
Scope-adjusted debt in HUF '000s	**2019**	**2020**	**2021E**	**2022E**
Reported gross financial debt	10,010,108	11,105,661	30,303,996	30,303,996
less: hybrid bonds	-	-	-	-
less: cash and cash equivalents	-	-	-	-
add: cash not accessible	-	-	-	-
add: pension adjustment	-	-	-	-
add: operating lease obligations	-	-	4,344	4,822
Other	-	-	-	-
Scope-adjusted debt	10,010,108	11,105,661	30,308,340	30,308,818

Business risk profile

Improved business risk profile assessed at BB-

B+N grew strongly in 2016-2020, driven by successful tenders for major contracts and small acquisitions. The outsourcing of public sector projects through public-private partnerships in the past years has allowed B+N (and other players) to increase their footprint. In 2020 the coronavirus crisis further increased the demand for B+N's services, which also supported the company's strong growth in revenue and generated cash flow. We expect the impact of the pandemic to contribute to 2021 sales as well.

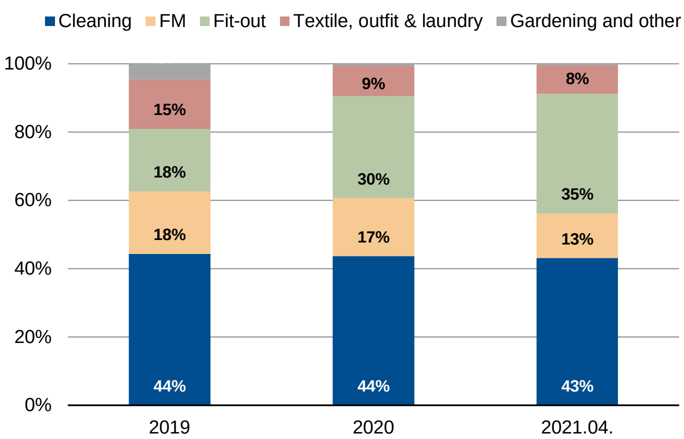
The facility management market is characterised by very low entry barriers, owing to easily replicable services, and a dependence on labour. However, labour is in short supply in Hungary. B+N distinguishes itself in the market by ensuring reliability and the ability to meet increasing demand, even during the pandemic. This confirms that the company is gradually overcoming the prevailing labour shortage and enhancing its efficiency.

In addition to being market leader in Hungary, B+N has gained market leading positions in several countries in CEE. Furthermore, it has reduced its concentration on Hungary, supporting its geographical diversification and reducing its dependence on Hungarian state procurement contracts. However, the large exposure to the Hungarian market and high customer concentration remains, exposing B+N to the risk of changes in macroeconomic conditions or a loss of major contracts. This is partially mitigated by the company's multi-year service contracts with major clients. These are credit-positive, providing good cash flow visibility over the next two to three years.

The ISS Group acquisitions have also broadened the company's service portfolio by adding catering and security services. This will allow B+N to participate in tenders for clients that prefer to contract fully integrated facility management providers. Along with the cleaning segment, there is an increasing proportion of revenue from other segments such as facility management and fit-out, although the latter is not expected to play such a dominant role as in 2020 and 2021. Profitability in terms of the EBITDA margin ranges from 10% to 13% as operating costs have risen with increasing sales.

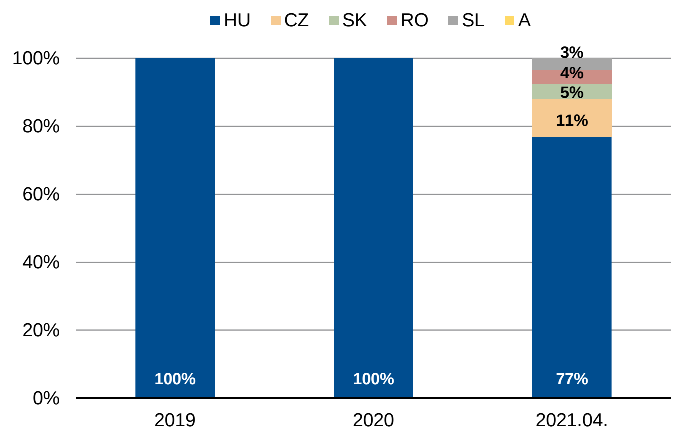
B+N's business risk profile has improved due to the acquisition of the ISS Group's CEE subsidiaries, prompting an upgrade to BB- from B+. Even so, the company's business risk profile constrains its issuer rating.

Figure 1: Revenue breakdown by activity



Source: B+N, Scope estimates

Figure 2: Revenue breakdown by country



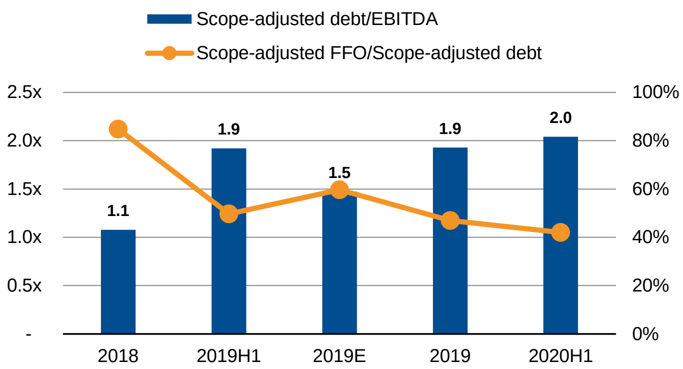
Source: B+N, Scope estimates

Financial risk profile

Robust financial risk profile assessed at BBB+

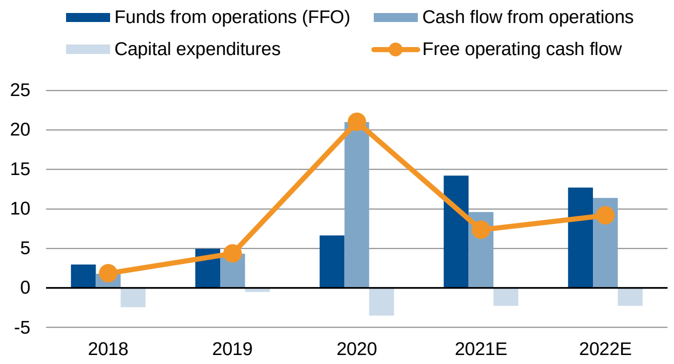
B+N's financial risk profile continues to be the strongest rating driver. Credit metrics improved slightly for 2020 backed by: i) strong performance thanks to increased demand for B+N's services during the pandemic, public procurement contracts won and robust cash flow generation; and ii) the unused portion of the issued bond proceeds in 2019. We expect credit metrics to remain stable following the issuance of the HUF 13.2bn bond, as its impact will be offset by B+N's strong performance. The second bond issuance and the utilisation of the bond proceeds, which we expect to prompt B+N to utilise short-term debt again, have increased SaD in 2021. We expect leverage, as measured by SaD/EBITDA, to deteriorate to around 2.0x and debt protection, in terms of EBITDA/interest coverage, to remain at a very comfortable level of above 10x.

Figure 3: Leverage



Source: Scope estimates

Figure 4: Cash flow generation (HUF bn)



Source: Scope estimates

Adequate liquidity profile

B+N's liquidity profile remains neutral for the rating. Following the refinancing of existing short-term loans in 2019 with some of the proceeds of the planned bond, short-term debt was negligible in 2019 and 2020. However, we expect B+N to utilise short-term loans once the bond proceeds have been fully used for the financing of its M&A activity. We expect liquidity to remain adequate, reflecting the marginal amount of long-term repayments scheduled for the forecasted years, coupled with a solid cash flow generation.

Supplementary rating drivers

Negative supplementary rating drivers

B+N's financial policy is a negative rating driver (ESG factor). Moreover, there is key person risk (ESG factor) regarding the CEO, whom we regard as instrumental not only for contract renewals and success in tenders but also for dividend policy. We have assumed a 50% payout ratio for the future and no other form of shareholder remuneration.

B+N has stated its intention to suspend M&A activity in the short term. We have no reason to believe that management will deviate from this position. Therefore, for technical reasons, we have removed the negative one-notch adjustment for execution risk as it is reflected in the rating case through conservatively calculated credit metrics (non-netting of cash for SaD).

Long-term debt ratings

Senior unsecured debt rated at BB-

B+N issued a HUF 10bn senior unsecured bond (ISIN: HU0000359419) in 2019 and a HUF 13.2bn senior unsecured bond (ISIN: HU0000360623) in 2021 under the Hungarian Bond Funding for Growth Scheme. Our recovery assessment is based on a hypothetical default scenario in 2023 and assumes outstanding senior unsecured debt of HUF 24.3bn, including a convertible bond of HUF 1.1bn (ISIN: HU0001300313). Our recovery analysis indicates an 'average' recovery (30%-50%) for B+N's outstanding senior unsecured debt.

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