# Global Refuse Holding Zrt.
# Hungary, Business Services

BB- STABLE

## Key metrics

| | | | Scope estimates | |
|---|---|---|---|---|
| Scope credit ratios | 2020 | 2021 | 2022E | 2023E |
| Scope-adjusted EBITDA/interest cover | 101.6x | 93.8x | 10.6x | 7.6x |
| Scope-adjusted debt/EBITDA | 0.4x | 0.5x | 2.1x | 2.9x |
| Scope-adjusted funds from operations/debt | 212% | 189% | 40% | 28% |
| Scope-adjusted free operating cash flow/debt | 215% | 85% | 34% | 17% |

## Rating rationale

The issuer rating reflects Global Refuse Holding Zrt.'s (GRH) improved financial risk profile and the well-integrated acquisition of Eltex Kft. Its leading position in municipal waste management also supports the ratings. The rating however is constrained by its business risk profile due to its limited size and outreach and low geographical diversification.

## Outlook and rating-change drivers

The Stable Outlook reflects our view on GRH's comparatively stronger credit metrics in 2023-2025. The Outlook also considers GRH's ability to maintain the leverage below 3.0x. The Outlook is further driven by GRH's strong revenue generation capacity driven by its prominent position as a regional municipal waste management company and the well-integrated recent acquisition of Eltex Kft.

A positive rating action rating could be warranted if the group strengthened its business risk profile, which could possibly remove the negative one notch adjustment due to its limited scale.

A negative rating action could result from a deterioration in the group's leverage (Scope-adjusted debt/EBITDA) above 3.5x for a prolonged period, as the result of weaker profitability or a further increase in debt.

## Rating history

| Date | Rating action/monitoring review | Issuer rating & Outlook |
|---|---|---|
| 20 Dec 2021 | New | B+/Stable |

### Ratings & Outlook

| | |
|---|---|
| Issuer | BB-/Stable |
| Senior unsecured guaranteed debt | BB |


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### Related Methodologies

Corporate Rating Methodology; July 2022


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## Rating and rating-change drivers

| Positive rating drivers | Negative rating drivers |
|---|---|
| • Leader in municipal waste management in Békés county, in southeaster Hungary<br>• Increasing need for recycling, especially for industrial waste<br>• Contribution towards a circular economy (credit positive ESG factor)<br>• Long-term contracts with a high likelihood of being renewed<br>• Large exposure to municipal waste collection and transportation, which is stable<br>• Sole operator of the Békéscsaba regional waste disposal plant (BVÜ) since 1996<br>• No sub-sovereign counterparty risk once the new concession system is implemented in July 2023<br>• Possibility of increased business if the regional coordinator position is offered under the new concession system in 2023 | • Geographically limited to one region of Hungary (very limited diversification)<br>• Use of landfill (credit-negative ESG factor)<br>• Very volatile cash flow cover, constrained by high debt-funded capex needs<br>• Regulatory changes proposed for July 2023 create some uncertainty with regard to current contracts |

| Positive rating-change drivers | Negative rating-change drivers |
|---|---|
| • Strengthened business risk profile,  which could possibly remove the negative on notch adjustment | • Scope-adjusted debt/EBITDA increasing above 3.5x over a prolonged period |

## 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 owner of Tappe Kft. (Tappe), Békéscsabai Városüzemeltetési Kft (BVÜ), Global Refuse Nonprofit Kft. (GRN) and Global Refuse Metal Kft. (GRM). GRH's operates through these subsidiaries.

The ownership structure of GRH is as follows: 80% is owned by Equilor Fund Management Co. through their Central European Opportunity PE Fund and 20% is 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 Southern Great Plains 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.

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.

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. The waste management system in Hungary will be converted into a concession system and will be handled by MOL Group from July 2023 onwards. Following this transformation, the national authority NHKV's involvement in the municipal waste management process is likely to be eliminated.

## Financial overview

| | | | | Scope estimates | | |
|---|---|---|---|---|---|---|
| **Scope credit ratios** | **2019** | **2020** | **2021** | **2022E** | **2023E** | **2024E** |
| Scope-adjusted EBITDA/interest cover | 68.1x | 101.6x | 93.8x | 10.6x | 7.6x | 9.3x |
| Scope-adjusted debt/EBITDA | 0.5x | 0.4x | 0.5x | 2.1x | 2.9x | 2.3x |
| Scope-adjusted funds from operations/debt | 165% | 212% | 189% | 40% | 28% | 35% |
| Scope-adjusted free operating cash flow/debt | 173% | 215% | 85% | 34% | 17% | 28% |
| Liquidity | >200% | >200% | >200% | >200% | >200% | >200% |
| **Scope-adjusted EBITDA in HUF m** | | | | | | |
| EBITDA | 1,324 | 1,404 | 1,693 | 1,181 | 1,049 | 1,347 |
| Operating lease payments | - | - | - | - | - | - |
| add: dividends from associates | - | - | - | 890 | 377 | 337 |
| **Scope-adjusted EBITDA** | **1,324** | **1,404** | **1,693** | **2,071** | **1,426** | **1,684** |
| **Funds from operations in HUF m** | | | | | | |
| Scope-adjusted EBITDA | 1,324 | 1,404 | 1,693 | 2,071 | 1,426 | 1,684 |
| less: (net) cash interest paid | (19) | (14) | (6) | (195) | (187) | (181) |
| less: cash tax paid per cash flow statement | (109) | (54) | (149) | (157) | (96) | (120) |
| Change in provisions | - | - | - | - | - | - |
| **Funds from operations (FFO)** | **1,196** | **1,336** | **1,538** | **1,719** | **1,142** | **1,383** |
| **Free operating cash flow in HUF m** | | | | | | |
| Funds from operations | 1,196 | 1,336 | 1,538 | 1,719 | 1,142 | 1,383 |
| Change in working capital | 379 | (209) | (2) | (77) | 84 | (125) |
| Non-operating cash flow | (4) | 310 | (177) | 25 | 25 | 25 |
| less: capital expenditure (net) | (318) | (82) | (665) | (225) | (556) | (164) |
| **Free operating cash flow (FOCF)** | **1,253** | **1,356** | **693** | **1,442** | **696** | **1,119** |
| **Net cash interest paid in HUF m** | | | | | | |
| Net cash interest per cash flow statement | 19 | 14 | 18 | 195 | 187 | 181 |
| Change in other items | - | - | - | - | - | - |
| **Net cash interest paid** | **19** | **14** | **18** | **195** | **187** | **181** |
| **Scope-adjusted debt in HUF m** | | | | | | |
| Reported gross financial debt | 583 | 455 | 614 | 4,064 | 3,863 | 3,656 |
| less: subordinated (hybrid) debt | - | - | - | - | - | - |
| less: cash and cash equivalents | - | - | - | - | - | - |
| add: non-accessible cash | - | - | - | - | - | - |
| add: pension adjustment | - | - | - | - | - | - |
| add: operating lease obligations | - | - | - | - | - | - |
| add: asset retirement obligations | 141 | 175 | 200 | 225 | 250 | 275 |
| **Scope-adjusted debt** | **724** | **630** | **814** | **4,289** | **4,113** | **3,931** |

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## 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)

### ESG strategy

All the governance-related factors are credit neutral while 'resources management' is credit positive due to GRH's importance in the Hungary towards a circular economy (credit positive ESG factor).

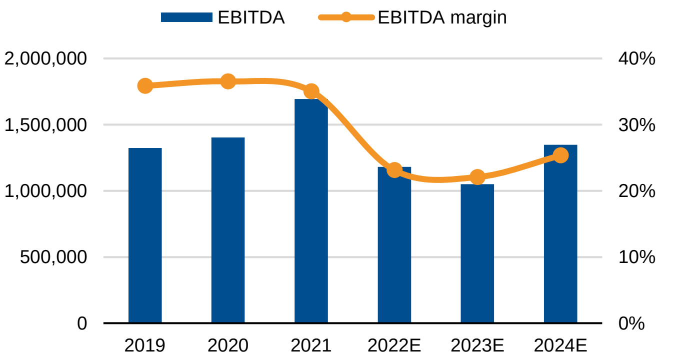
However, we also highlight the negative effects of using landfills (credit negative ESG factor). In 2021, 34% of GRH's revenues came from BVÜ – the subsidiary that is the sole operator of the Békéscsaba regional waste disposal site since 1996. Hungary has imposed a landfill tax since 2013 and the tax remained at HUF 6,000/t (EUR 19.35/t) in 2021. Moreover, according to the IPCC permit that gives BVÜ the permission to operate its landfill states that the site must be covered with a temporary sealing layer by 31 December of the year following the abandonment, and the landfill must be covered and recultivated with a permanent sealing layer no later than 30 years after the abandonment of the entire landfill. In the meantime, aftercare is also needed. The calculated provision of aftercare was HUF 200m as of FYE 2021. Due to the stringent EU policies and the high regulatory expenses associated with such landfills, the robustness of the landfill revenue streams is questionable, making this a credit-negative ESG factor.

[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: B+

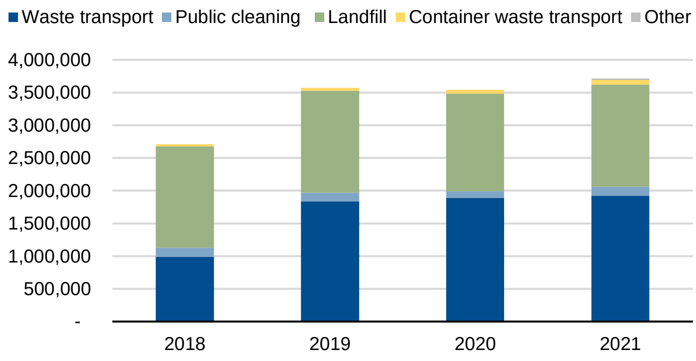
GRH's business risk profile is supported by its continuous cash-flow generation capacity stemming from its secure market position. GRH's business risk profile is further supported by the increasing need for recycling, especially of industrial waste, in line with global sustainability megatrends with regard to a circular economy (positive ESG factor). GRH's market position is secured by its strong position in the Békés region in Hungary despite the region's limited size. The group's cash flows are protected by the large exposure to public cleaning, municipal waste collection and transportation, which is less volatile, and long-term contracts with a high likelihood of being renewed, given its strong position in waste services and possession of key infrastructure. However, the business risk profile that is comparatively weaker due to GRH's limited size continues to constraint the overall issuer rating.

**Figure 1: EBITDA & EBITDA margins 2019-2024 (HUF '000)**




Sources: GRH, Scope estimates

**Figure 2: Revenue breakdown per segment 2018-2021 (HUF '000)**




Sources: GRH

**Well-represented throughout the waste management value chain**

GRH's geographical diversification remains limited to a single county in Hungary where it is the leader in handling municipal waste. However, the group is improving diversification in its services portfolio by combining supplementary business services with municipal waste management, such as winter road cleaning, waste container rental and waste yard operations. The newest addition to the group, GRM, which is active in waste material trading, has improved the outreach of 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. However, Tappe (as a direct subsidiary of GRH) has applied for a regional coordinator position under the new concession system that will be launched in July 2023. If the application is accepted, GRH (via Tappe) would have the possibility of serving two additional counties, improving geographical diversification as well as revenues and profitability.

**Margins under pressure from rising inflation and cancellation of recycling-related project**

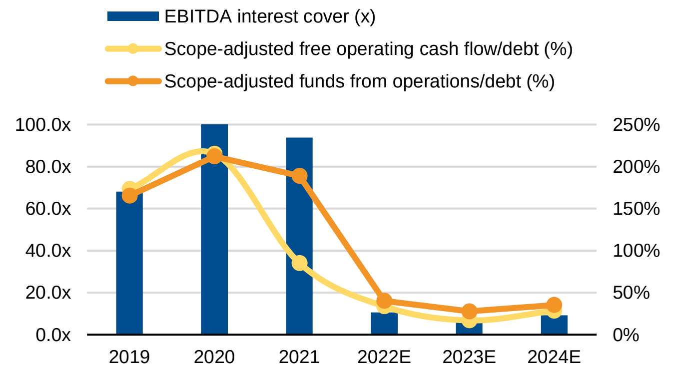
The sustainability of landfill – the group's highest margin activity – is questionable due to the EU's intention and directives to decrease the volume of landfill waste. This activity also creates some margin concentration. Moreover, a recycling-related project was not realised due to the current adverse economic conditions, while reduced revenue contributions are expected from GRM as the prices of recycled waste have significantly softened. Therefore, the robust margin profile that GRH has maintained in the past is expected to take a turn in 2022 and 2023 followed by the actual inflation pressure giving rise to soaring energy and staff expenses. Moreover, loss of additional margins that were intended from the recycling-related project due to the cancellation of the project, will also contribute to the margin contraction. The EBITDA margin is expected to gradually recover towards 25% in 2024.

## Financial risk profile: BBB-

**Strong credit metrics drive the rating**

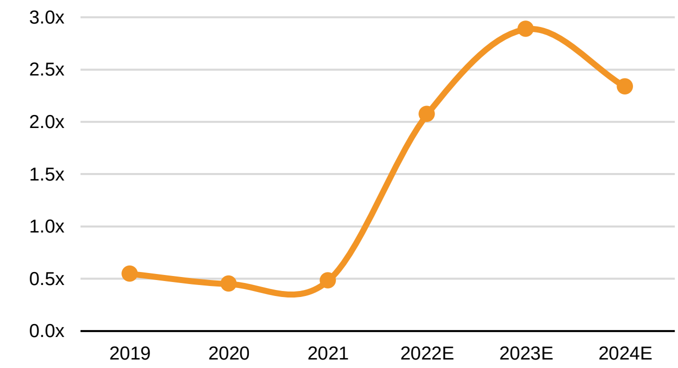
The BB-/Stable issuer rating reflects GRH's financial risk profile that is stronger than its business risk profile driven by GRH's comparatively stronger credit metrics in 2023-2025. Scope's also considers GRH's ability to maintain its leverage in the 2-3x range as measured by Scope-adjusted debt/EBITDA. Scope expects GRH's interest cover ratio to be above 7x in the period 2023-2025.

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




Sources: GRH, Scope estimates

**Figure 4: Scope-adjusted leverage**




Sources: GRH, Scope estimates

**Adequate liquidity**

GRH's liquidity as measured by internal and external liquidity remains above 100% at all times, even in 2023 when the liquidity is hindered by low FOCF due to high capex needs. Nonetheless, despite rising debt levels, high capex and also shareholder dividends (that have not been captured in the business plan by the management), we do not envisage any difficulty in timely reimbursement of GRH's debt over the next 3-year period.

Moreover, pertaining to its good relationships with banks as demonstrated by the current diversified set of loan facilities (working capital and other) and good working capital management strategy, we assess its liquidity as adequate. This view is also supported by its unrestricted cash balance of HUF 1.2bn as at FY2021. GRH does not currently have any revolving credit facilities.

| Balance in HUF m | 2021 | 2022E | 2023E |
|---|---|---|---|
| Unrestricted cash (t-1) | 1,453 | 1,152 | 808 |
| Open committed credit lines (t-1) | - | - | - |
| Free operating cash flow | 693 | 1,442 | 696 |
| Short-term debt (t-1) | 139 | 289 | 256 |
| **Coverage** | **>200%** | **>200%** | **>200%** |

## Supplementary rating drivers: minus one notch

GRH's limited size and outreach compared to other entities rated in the BB rating category hinder its issuer rating, which is 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, which 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

**Senior unsecured guaranteed debt rating: BB**

The debt instrument rating of BB for GRH's senior unsecured guaranteed bond is one notch above the group's issuer rating, reflecting an 'above-average' recovery for this bond in the event of a hypothetical default. Scope's recovery expectations are based on an anticipated liquidation value in a hypothetical default scenario at the end of 2024. Short-term and long-term debt (excluding the bond issue) raised from financial institutions and other financial liabilities such as trade payables rank higher than senior unsecured debt. Hence, such debt would be repaid first.

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