Cellfie Mobile LLC
Georgia, Telecommunication services

SCOPE BB- Stable

Key metrics

			Scope estimates	
Scope credit ratios	2021	2022	2023E	2024E
Scope-adjusted EBITDA/interest cover	55.0x	35.0x	9.3x	4.8x
Scope-adjusted debt/EBITDA	9.2x	10.7x	1.3x	1.3x
Scope-adjusted funds from operations/debt	11%	9%	70%	63%
Scope-adjusted free operating cash flow/debt	2%	1%	4%	-3%

Rating rationale

The rating is driven by Cellfie's low leverage and the low cyclicality of the telecommunications industry. It is somewhat constrained by low diversification, weak free operating cash flow and peer group considerations.

Cellfie's business risk profile, assessed at BB, is mainly supported by good profitability (EBITDA margin after leases of 33% in 2022). This is in line with that of most large European incumbent telecommunications operators but significantly below larger Georgian operators. The business risk profile is also supported by the low cyclicality of telecommunications services. Cellfie's market share moderately supports the rating, given a number three position in Georgia with 25% of the country's subscribers, although it only has 16% of national mobile retail revenues. Diversification is weak as Cellfie only offers mobile services in a single country.

The financial risk profile, assessed at BB, is supported by low leverage, with a Scope-adjusted debt/EBITDA anticipated at 1.3x at YE 2023. Following the company's structural and financial reorganisation in 2023, gross debt is expected to be limited to GEL 112m, of which GEL 27m of leases. We note that lease liabilities only represent about two years of lease payments, a rather low level. In parallel, interest coverage is good, and EBITDA interest cover is expected to be above 4x in the coming years. The company is implementing a significant capex programme to increase its market coverage and the capacity of its mobile network. The programme also includes a 5G rollout as Cellfie was the only operator in Georgia to receive 5G spectrum. We therefore expect free operating cash flow (FOCF) to remain weak for some time, with a Scope-adjusted FOCF/debt of close to 0% in the coming years. The company is not expected to pay any dividends until 2026. Liquidity is deemed adequate over the coming years.

The issuer rating also incorporates a one-notch negative adjustment for the peer comparison, as Cellfie is noticeably smaller and has a weaker marker position than relevant peers.

Outlook and rating-change drivers

The Outlook is Stable and incorporates progressive improvements in revenue and profitability while the company makes significant capex and pays no dividends.

A positive action could occur if the company improved its competitive positioning (market share and diversification), or if negative rating adjustment pertaining to peer context was withdrawn. We see both situations as remote.

A negative action could occur if leverage as measured by Scope-adjusted debt/EBITDA remained above 2x as a result of lower-than-anticipated profitability and/or higher capex.

Ratings & Outlook

Issuer BB-/Stable

Analyst

Jacques de Greling
+33 1 82 88 23 70
j.degreling@scoperatings.com

Related Methodology

General Corporate Rating Methodology; October 2023

Scope Ratings GmbH

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Low Scope-adjusted debt/EBITDA ratio, expected at around 1.3x after the capital increase • Stable and recurring business with 1.5m customers • Good profitability, with EBITDA margin of 45% (33% after leases) • Good interest coverage, expected to reach around 5x after the capital increase	• Very weak Scope-adjusted FOCF/debt ratio as the company is beefing up its mobile network • Exposure limited to the Georgian mobile market • Smallest player in the Georgian mobile market with 24% market share (16% of market revenues) • Negative rating-adjustment pertaining to peer context

Positive rating-change drivers	Negative rating-change drivers
• Improved competitive positioning (market share and diversification), or if peer comparison negative rating driver was withdrawn	• Scope-adjusted debt/EBITDA ratio sustainably above 2.0x

Corporate profile

Cellfie Mobile is the third largest mobile operator in Georgia, a three-player market. It has 1.5m subscribers representing about 25% of the market and revenue of GEL 141m (EUR 49m). It began operations in 2003 and was long a subsidiary of Russian group Veon. It has been controlled by Georgian businessman Khvicha Makatsaria since June 2022. After changing its name and brand to Cellfie in April 2023, it became the only Georgian mobile operator to receive a 5G licence in August 2023.

Financial overview

				Scope estimates		
Scope credit ratios	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
Scope-adjusted EBITDA interest cover	47.8x	55.0x	35.0x	9.3x	4.8x	5.0x
Scope-adjusted debt/EBITDA	10.6x	9.2x	10.7x	1.3x	1.3x	1.2x
Scope-adjusted funds from operations/debt	9%	11%	9%	70%	63%	66%
Scope-adjusted free operating cash flow/debt	2%	2%	1%	4%	-3%	3%
Scope-adjusted EBITDA in GEL '000s						
EBITDA	44,661	54,115	63,327	70,000	74,900	80,300
Operating lease payments	0	0	0	0	0	0
Other items	0	0	0	0	0	0
Scope-adjusted EBITDA	**44,661**	**54,115**	**63,327**	**70,000**	**74,900**	**80,300**
Funds from operations in GEL '000s						
Scope-adjusted EBITDA	44,661	54,115	63,327	70,000	74,900	80,300
less: (net) cash interest paid	-935	-984	-1,810	-7,500	-15,700	-16,150
less: cash tax paid per cash flow statement	0	0	0	0	0	0
add: dividends from associates	0	0	0	0	0	0
Change in provisions	0	0	0	0	0	0
Funds from operations (FFO)	**43,726**	**53,131**	**61,517**	**62,500**	**59,200**	**64,150**
Free operating cash flow in GEL '000s						
Funds from operations	43,726	53,131	61,517	62,500	59,200	64,150
Change in working capital	6,339	-7,854	1,884	-3,500	-1,000	-1,000
Non-operating cash flow	663	1,036	-1,279	150	200	200
less: capital expenditure (net)	-30,835	-28,457	-44,547	-44,000	-49,000	-47,000
less: lease amortisation	-9,359	-9,777	-11,687	-11,237	-12,045	-13,398
Free operating cash flow (FOCF)	**10,534**	**8,079**	**5,888**	**3,913**	**-2,645**	**2,952**
Net cash interest paid in GEL '000s						
Net cash interest per cash flow statement	935	984	1,810	7,500	15,700	16,150
add: interest component, operating leases	0	0	0	0	0	0
Change in other items	0	0	0	0	0	0
Net cash interest paid	**935**	**984**	**1,810**	**7,500**	**15,700**	**16,150**
Scope-adjusted debt in GEL '000s						
Reported gross financial debt	487,461	516,232	692,020	112,297	113,560	116,675
less: cash and cash equivalents	-11,840	-19,517	-17,422	-23,535	-18,890	-19,842
add: non-accessible cash	0	0	0	0	0	0
add: pension adjustment	0	0	0	0	0	0
add: operating lease obligations	0	0	0	0	0	0
Other items	0	0	0	0	0	0
Scope-adjusted debt (SaD)	**475,621**	**496,715**	**674,598**	**88,762**	**94,670**	**96,833**

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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)	Grey leaf
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)	Grey leaf
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)	Grey leaf
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	Grey leaf

Legend
Green leaf (ESG factor: credit positive)
Red leaf (ESG factor: credit negative)
Grey leaf (ESG factor: credit neutral)

No significant credit-relevant ESG factors

The corporate structure is quite simple as there are no subsidiaries or affiliates. The supervisory board has three members, of which one is independent (Temuri Kobakhidze). It is expected that the supervisory board will expand to five members, of which three will be independent.

[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

Industry risk profile: A

The industry risk profile for telecommunications services stands at A, based on low cyclicality (subscriptions are for a necessary basic service), medium entry barriers (licences, network rollout) and medium-to-low substitution risk (over-the-top service).

New structural setup since 2022

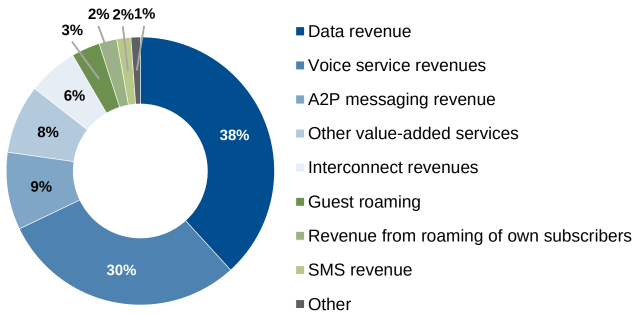
Cellfie Mobile LLC (formerly Veon Georgia LLC) received its first mobile licence in 2003 and began operations as the third mobile operator in Georgia and a subsidiary of Russian group Veon. Georgian businessman Khvicha Makatsaria took control of the company in June 2022 along with Mamuka Togonidze. The company changed its name and brand to Cellfie in April 2023 after this change of ownership. Cellfie became the only operator in Georgia to receive 5G spectrum (700 MHz, 2600 MHz and 3500 MHz) in August 2023. The other two main mobile operators, MagtiCom and Silknet, refused to join the auction process because it required them to open to mobile virtual network operators.

Dynamic telecommunication market in Georgia

Georgia's telecommunications market is estimated at GEL 1,064m (EUR 373m) in 2022, with mobile representing 70%. The country's mobile penetration rate is about 160%, a high level that means it is difficult to increase subscriber numbers. Following the Georgian telecom regulator (Comcom)'s removal of a retail price control mechanism in mid-2021, all operators have increased their prices significantly. This allowed Georgian mobile revenues to increase by 13% in 2021 and 26% in 2022, a rather unusual situation. As a result, average revenue per user (ARPU) in the country increased by 13% in 2021 and 22% in 2022, compared to about 2% annually over the three years before. Given that Georgia wants to join the European Union, its general regulatory framework is becoming more and more like that of the EU.

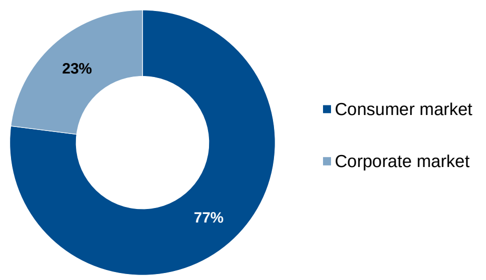
Cellfie has a customer base of 1.5m, of which 0.3m are corporate customers (mostly SMEs). Its revenues stood at GEL 140.7m in 2022.

Figure 1: Cellfie's revenue breakdown (%), 2022



Sources: Cellfie, Scope

Figure 2: Cellfie's customer base (%), 2022

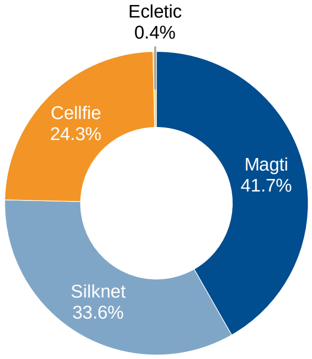


Sources: Cellfie, Scope

Number three in the Georgian mobile market

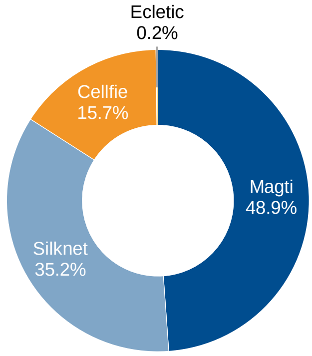
Cellfie's market share in terms of subscribers is at 24%, meaning a number three rank in the Georgian mobile market. In terms of mobile service revenue, Cellfie has a 16% market share.

Figure 3: Cellfie's mobile market share in Georgia (%), subscribers, June 2023



Sources: Comcom, Scope

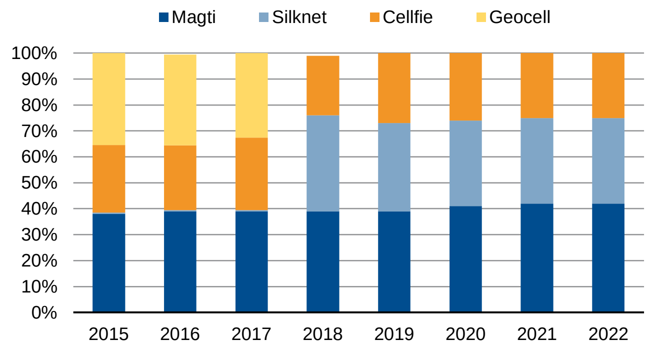
Figure 4: Cellfie's mobile market share in Georgia (%), retail service revenue, June 2023



Sources: Comcom, Scope

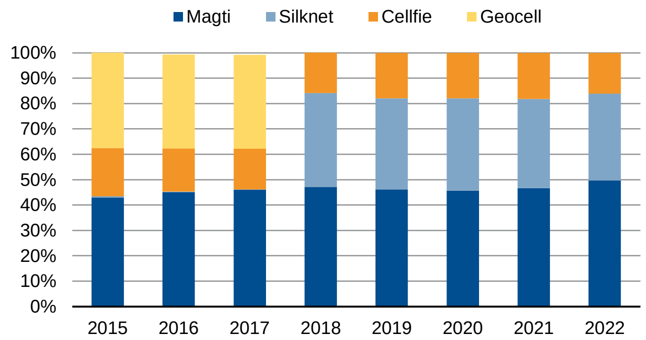
Cellfie's market share has been slowly eroding over the last year. After plateauing at 18% in terms of revenues over 2019-21, it is now close to 16%.

Figure 5: Mobile market shares in Georgia (%), subscribers, 2015-22



Sources: Comcom, Scope

Figure 6: Mobile market shares in Georgia (%), retail service revenue, 2015-22



Sources: Comcom, Scope

Diversification is weak …

Diversification is also weak as Cellfie only operates in Georgia, in a single industry, telecommunication services. In addition, it only offers mobile services, while whereas its two main competitors (MagtiCom and Silknet), also offer fixed broadband, fixed telephony and TV services.

….. while profitability is good

Profitability is good, with an EBITDA margin of 45% in 2022. In terms of adjusted EBITDA after leases, the margin stands at 33%, a level that is comparable to most large incumbent telecom operators in Europe. We note that this margin is significantly below those of Cellfie's two domestic competitors, however.

Financial risk profile: BB

New capital structure with reduced debt level

When Cellfie was purchased by its current shareholders as Veon Georgia, net financial debt (GEL 675m, of which GEL 24m referred to leases) was mostly related to shareholder loans. This financing was restructured in 2023 following the change in ownership, with a conversion of the shareholder loans into equity. At the end of 2023, Scope-adjusted gross debt is expected to be GEL 112m, of which GEL 27m is leases. Incorporating about GEL 23m of cash, this results in Scope-adjusted debt of GEL 89m.

Low level of lease liabilities

We note that the amount of leases capitalised by Cellfie represents about two years of repayments. This level is significantly lower than that of most European telecommunications groups (typically five to six years).

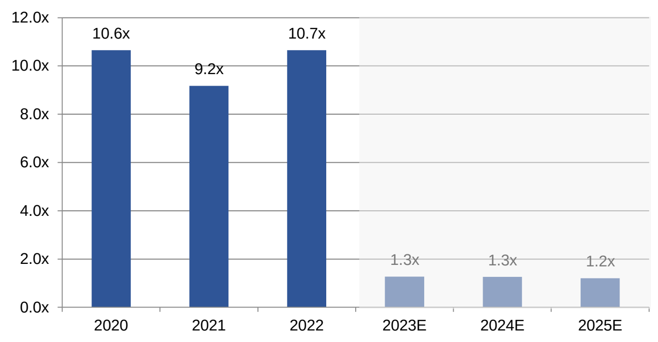
Significant network investment in the coming years

The main feature of the coming years is expected to be a high level of capital expenditure. This is because the company wants to significantly increase its network coverage in the country and increase its capacity in areas it already covers to narrow the gap compared with competitors. The investment will include a 5G rollout after having obtained 5G spectrum in August 2023. This network improvement, illustrated by capex of around 30% of revenues, will seriously limit free operating cash flow for the coming years. We expect this investment phase will end in 2026. The increase in network coverage will also lead to an increase in lease liabilities in the coming years as leases are mostly related to space for tower sites. The company does not intend to pay any dividends until 2026.

Scope-adjusted debt/EBITDA ratio around 1.3x

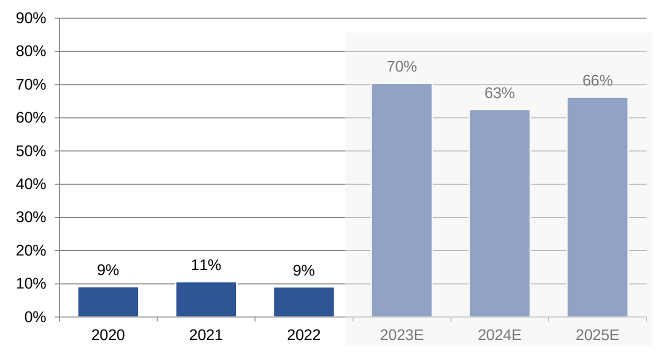
Based on the new capital structure, leverage is expected to remain good for the coming years, with a Scope-adjusted debt/EBITDA ratio around 1.3x. The expected increase in EBITDA is likely to be followed by an increase in Scope-adjusted debt, driven by very limited free operating cash flow and an increase in leases. Similarly, the Scope-adjusted funds from operations/debt ratio is expected to remain rather stable over the next three years, at an average of 66%, a strong level.

Figure 7: Scope-adjusted debt/EBITDA, 2020-25E



Sources: Cellfie, Scope estimates

Figure 8: Scope-adjusted funds from operations/debt, 2020-25E



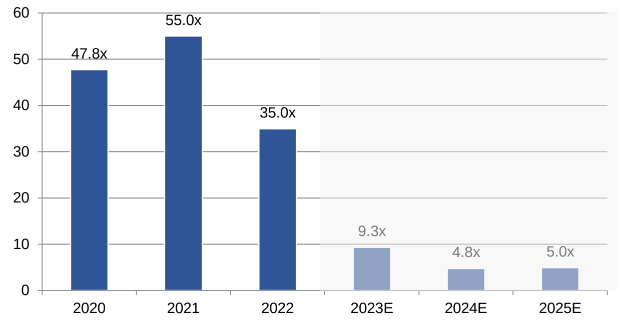
Sources: Cellfie, Scope estimates

EBITDA interest cover is expected to stand around 5x over the period 2024E-2025E period, after a transitory 2023E period, following the capital reorganisation.

Scope-adjusted FOCF/SaD debt expected to be close to 0%

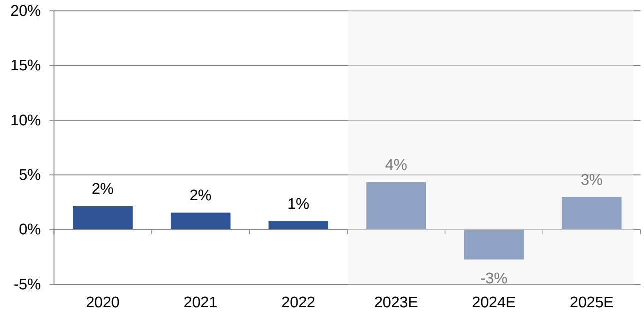
Due to the significant investment in the network improvements, cash flow cover – as measured by Scope-adjusted free operating cash flow/debt – is expected to be, on average, close, to 0% over the next three years. We believe that this weak point will not improve until around 2026, once most of the upgrades of to the network are finished.

Figure 9: EBITDA interest cover, 2020-25E



Sources: Cellfie, Scope estimates

Figure 10: Scope-adjusted free operating cash flow/debt, 2020-25E



Sources: Cellfie, Scope estimates

Adequate liquidity

Cellfie has no committed credit lines. The only short-term debt expected on the balance sheet (excluding leases) should be the partial repayment (GEL 2m) on the bank loan each year. As a result, liquidity is deemed as adequate over the next few years.

Balance in GEL '000s	2023E	2024E	2025E
Unrestricted cash (t-1)	17,422	23,535	18,890
Open committed credit lines (t-1)	0	0	0
Free operating cash flow (t)	3,913	-2,645	2,952
Short-term debt (t-1)	9,192	2,000	2,000
Coverage	**>200%**	**>200%**	**>200%**

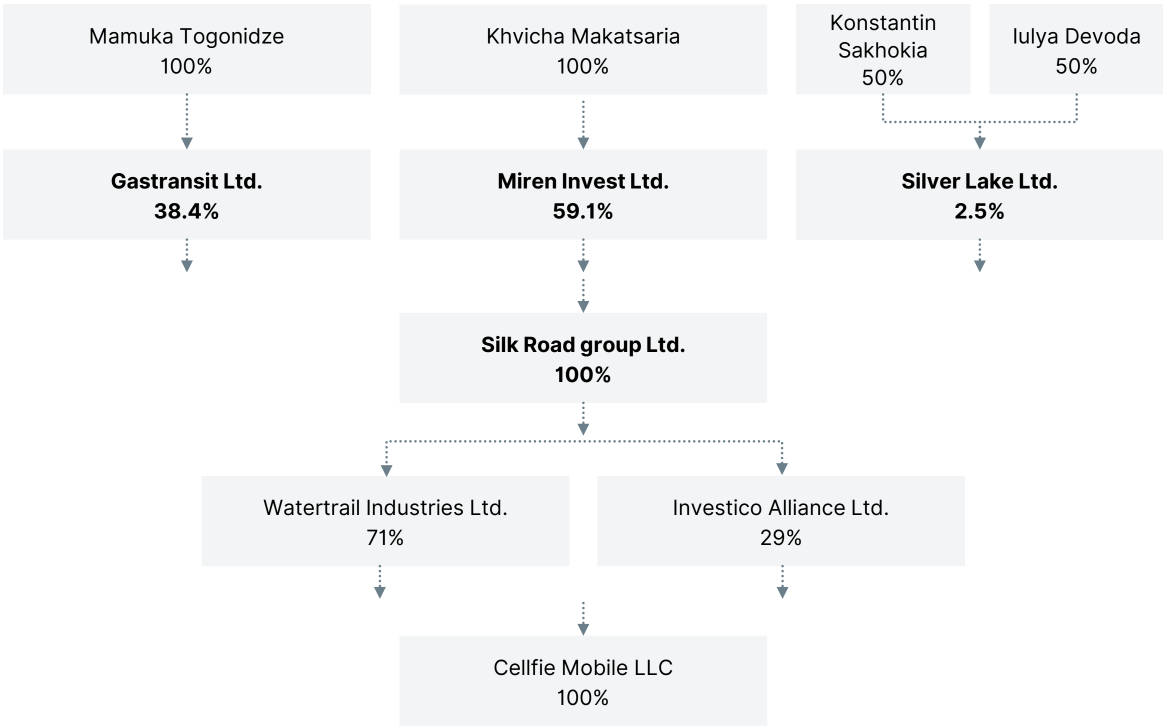
Supplementary rating drivers: -1 notch

The issuer rating also incorporates a one-notch negative adjustment for the peer comparison as Cellfie is noticeably smaller and has a weaker market position than other peers rated by Scope (all with an issuer rating between BB- and BB).

	Cellfie Mobile LLC	JSC Evex Hospitals	Tegeta Motors LLC	Georgian Beer Company JSC	4iG Nyrt
Issuer rating	**BB-/Stable**	**BB/Stable**	**BB-/Stable**	**BB-/Negative**	**BB-/Stable**
Last reporting date	31 December 2022	31 December 2022	31 December 2022	31 December 2022	31 December 2022
Business risk profile	BB	BB	BB-	BB-	BBB-
Industry	Telecommuni-cation services	Healthcare	Retail	Consumer products	Telecommuni-cation services
Revenues	GEL 141m	GEL 289m	GEL 970m	GEL 103m	HUF 277bn
Market position	No. 3 in Georgia mobile	No. 1 in Georgia	No. 1 in Georgia	No. 2 in Georgia	No. 2 in Hungary telecoms
Financial risk profile	BB	BB	BB-	B+	B+
Scope-adjusted EBITDA/interest cover	35.0x	2.1x	2.3x	4.1x	2.8x
SaD/Scope-adjusted EBITDA	10.7x	3.7x	3.9x	2.9x	6.9x
Funds from operations/SaD	9%	14%	13%	26%	10%
Free operating cash flow/SaD	1%	-4%	-10%	-14%	-2%
Supplementary risk drivers	-1 notch	0 notch	0 notch	0 notch	-1 notch

We did not access the financial accounts of Cellfie's parent companies as these companies do not engage in financial reporting. We believe any potential cash outflows from the company are effectively safeguarded by restrictions on transactions involving "affiliated persons" disclosed in debt documentation.

Figure 11: Cellfie Mobile's ownership structure



Source: Cellfie

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

10 avenue de Messine
FR-75008 Paris

Phone +33 6 62 89 35 12

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 09 38 35

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com

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