FitchRatings

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Fitch Affirms Eurohold Bulgaria at 'B'; Outlook Stable

Fitch Ratings - Warsaw - 22 Jun 2022: Fitch Ratings has affirmed Eurohold Bulgaria AD Long Term Issuer Default Rating (IDR) at 'B' and removed it from Rating Watch Negative (RWN). The Outlook is Stable. Fitch has also affirmed the company's EUR70 million 6.5% notes due in December 2022 senior unsecured rating at 'B', with a Recovery Rating of 'RR4' and removed the rating from RWN.

The rating actions reflect our assessment of Eurohold's new group structure and business and financial profile following a largely debt-funded acquisition of the Bulgarian assets of Czech utility company CEZ, a.s. As a result of the acquisition, Eurohold's dominant business has changed to utilities from insurance. The rating also reflects Eurohold's weak liquidity at the parent level with reliance on short-term debt.

Key Rating Drivers

Acquisition of CEZ's Assets: In July 2021, Eurohold acquired the Bulgarian assets of CEZ via Eastern European Electric Company BV (EEEC), an investment vehicle controlled by Eurohold. The key assets acquired were 67% stakes in CEZ Distribution Bulgaria and CEZ Electro Bulgaria, as well as 100% of CEZ Trade Bulgaria. After subsequent calls for the remaining shares of CEZ Distribution Bulgaria and CEZ Electro Bulgaria, EEEC increased its shareholdings to 98.93% and 96.92%, respectively, in March 2022. Following the acquisition, the energy assets operate under the Electrohold brand.

New Business Structure: Following the acquisition of energy assets, Eurohold will focus on the utilities business, which will be the dominant contributor to consolidated EBITDA (around 65%-70%), and on insurance (around 30%), with the small remaining contribution to EBITDA from asset management and brokerage. Eurohold plans to divest its car selling and the leasing businesses, which we expect in 2022.

Change in Applied Criteria: Due to the acquisition of CEZ's assets and the disposal of car selling and leasing, Eurohold's business profile has changed to a non-financial corporate with material financial operations (insurance, asset management and brokerage) from an insurance-focused financial holding. As a result, Fitch has applied its Corporate Rating Criteria as the master criteria, together with its Corporates Recovery Ratings and Instrument Ratings Criteria. The previously applicable criteria was the Insurance Rating Criteria.

Rating Approach: Fitch rates Eurohold using a consolidated approach but excluding the insurance business's EBITDA and net debt (the deconsolidated group profile). This is because access to the insurance business's cash flow is limited, due to regulatory requirements to keep a minimum solvency ratio at insurance companies. We include dividends from the insurance business in the deconsolidated perimeter.

Eurohold's IDR is notched down two levels below the deconsolidated profile given its structural subordination. Eurohold's debt service capacity is contingent on dividend income streams from intermediate holding companies and operating subsidiaries (assuming covenant compliance) and does not have direct access to the underlying operating cash flows.

Corporate Governance Limitations: The rating reflects Eurohold's complex group structure, significant related party transactions and lower financial transparency than its EU peers, including a qualified audit opinion. Fitch's assessment of the links between Eurohold Bulgaria and its ultimate parent Starcom Holding under its Parent Subsidiary Linkage (PSL) Criteria leads to a standalone rating approach, as Fitch does not give credit for family ownership and does not rate private individuals or their family groupings.

Operating Cash Flows Support Deleveraging: We expect strong operating cash flows and moderate capex to support deleveraging in the medium term. We forecast deconsolidated net debt to EBITDA, to increase in 2022 due to the minority buyout, reaching about 6.1x at end-2022 (5.3x at end-2021). We then expect it to improve to about 4.7x in 2024-2026. This leverage level is commensurate with Eurohold's ratings.

Risks to Deleveraging: The company may consider organic growth in the renewables business and eventual expansion of the energy business outside Bulgaria only in the longer term as the company is committed to reducing debt. However, further large acquisitions, higher capex, high dividends, or negative regulatory or market changes would lead to slower deleveraging.

Derivation Summary

Eurohold is smaller than other rated central European utilities, such as Energa S.A. (BBB-/Rating Watch Positive), Bulgarian Energy Holding EAD (BEH; BB/Positive), although it is one of the largest utilities in Bulgaria. It has comparable size with ENERGO-PRO, a.s. (BB-/Negative). Eurohold is focused on distribution of electricity and supply. Historically, its EBITDA was more volatile than that of many peers, but the Fitch case assumes stabilisation of EBITDA after acquisition of CEZ assets, supported by cash inflow from regulated distribution EBITDA. Eurohold shares the same operating and regulatory environment as BEH, overall comparable with that of ENERGO-PRO. Energa operates in a more transparent regulatory framework.

Key Assumptions

Fitch's Key Assumptions Within Our Rating Case for the Issuer:

- Moderate growth of EBITDA in 2022-2025

- Capex at average of BGN91 million annually in 2022-2026

- Negative working capital movements in the rating horizon

- Net acquisitions of almost BGN175 million in 2022 and averaging BGN70 million in 2023-2026

Key Recovery Rating Assumptions

- The recovery analysis assumes that Eurohold would be liquidated in bankruptcy

- We assume a 10% administrative claim

Liquidation Approach

- As a holding company and including the ring-fenced insurance assets, the liquidation estimate reflects Fitch's view of the value of balance sheet assets that can be realised in sale or liquidation processes conducted during a bankruptcy or insolvency proceeding and distributed to creditors

- 0% advance rate applied to cash as it may be already gone upon bankruptcy

- 50% advance rate applied to net inventory

- 70% advance rate applied to trade receivables

- 50% advance rate applied to property, plant and equipment

- 80% advance rate applied to additional value from the insurance businesses

With these assumptions, our waterfall generated recovery computation (WGRG) for the senior unsecured notes of Eurohold is in the 'RR4' band, indicating a 'B' instrument rating. The WGRC output percentage on current metrics and assumptions was 41%.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Improved deconsolidated group financial profile with net debt to EBITDA below 4.5x on a sustained basis.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- Delay in refinancing of upcoming maturities;

- Net debt to EBITDA of the deconsolidated group above 6x on a sustained basis, for instance due to more aggressive financial policy, higher distributions to shareholders and lower profitability and cash generation;

- Significant weakening of the business profile with lower predictability of cash flows may lead to a tighter leverage sensitivity or a downgrade.

Best/Worst Case Rating Scenario

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

Liquidity and Debt Structure

Weak Liquidity: The rating is constrained by weak liquidity at the Eurohold holding company level. As of March-2021 Eurohold holding company had BGN0.6 million of cash and cash equivalents compared with BGN228.3 million of current financial liabilities. In May 2022 Eurohold refinanced the short-term ECP bonds of BGN60.9 million (EUR31 million) with newly issued ECP with maturity in mid-2023. Eurohold intends to refinance the EUR70 million (BGN133 million) bonds due in December 2022 in 4Q22 with a new bond issue, to also refinance other debt.

Liquidity may be also improved by leasing business disposal proceeds (BGN16 million assumed in our rating case) as well as dividends from subsidiaries (expected to be about BGN60 million in 2022).

Issuer Profile

Eurohold is a public company. It is majority-owned by Starcom Holding AD (50.65% at end-2021), which is ultimately owned by three individuals. The remaining shares are publicly listed on the stock exchange. The group core activity is the five segments including insurance, energy, asset management and brokerage, as well as car sales and leasing business.

Summary of Financial Adjustments

Eurohold's consolidated profile has been adjusted by deconsolidation of the insurance business, i.e. excluding the insurance business's EBITDA and net debt when calculating the main financial ratios of the issuer.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Eurohold has an ESG Relevance Score of '4' for Group Structure due to a fairly complex group structure, which has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Eurohold has an ESG Relevance Score of '4' for Financial Transparency due to lower financial transparency than EU peers and qualified audit opinion, which has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
Eurohold Bulgaria AD	LT IDR	B	Affirmed		B
• senior unsecured	LT	B	Affirmed	RR4	B

RATINGS KEY	OUTLOOK	WATCH
POSITIVE	⊕	⬘
NEGATIVE	⊖	⬙
EVOLVING	⊙	◆
STABLE	⊙	

Applicable Criteria

Corporate Rating Criteria (pub.15 Oct 2021) (including rating assumption sensitivity)

Corporates Recovery Ratings and Instrument Ratings Criteria (pub.09 Apr 2021) (including rating assumption sensitivity)

Country-Specific Treatment of Recovery Ratings Criteria (pub.05 Jan 2021)

Parent and Subsidiary Linkage Rating Criteria (pub.01 Dec 2021)

Sector Navigators - Addendum to the Corporate Rating Criteria (pub.15 Oct 2021)

Applicable Models

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.0.2 (1)

Additional Disclosures

Solicitation Status

Endorsement Status

Eurohold Bulgaria AD	EU Issued, UK Endorsed

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