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Fitch Rates PPF Arena 1 Senior Secured 'BBB-'; EUR550m Senior Secured Note 'BBB-'

Fitch Ratings-Frankfurt am Main-25 March 2019: Fitch Ratings has assigned PPF Arena 1 B.V. a senior secured rating of 'BBB-' and its EUR550 million senior secured notes a final rating of 'BBB-'.

PPF Arena 1 B.V. has issued EUR550 million senior secured notes due in 2026. The notes' security package includes share pledges over certain Telenor CEE subsidiaries in Hungary, Serbia, Montenegro and Bulgaria. The net proceeds from the notes are being used to refinance current bank debt. The notes' security package may be released if there is no other secured debt ranking pari passu in the Company's capital structure. Bank facilities are currently the only other secured debt ranking pari passu to the notes. The bank's security package may be released if Pro Forma Net Debt to EBITDA is less than 2x, calculated on a proportionate basis relative to equity ownership.

Key Rating Drivers

Strong Czech Operations: PPF Arena 1 owns the incumbent Czech telecoms infrastructure, which includes the local-access network and the ability to deploy convergent product propositions. The company's Czech operations accounted for 51% of total EBITDA in 2018 on a pro-forma basis for the acquisition of Telenor's CEE assets. PPF Arena 1 has a solid position in the mobile market with a Fitch-estimated service revenue market share of 37% (1H18). The mobile market is growing, supported by increasing consumer spending and macroeconomic factors. Combined with a stable mobile market structure, this enables mobile operators to monetise data usage and increase service revenue.

Broadband Market More Competitive: PPF Arena 1's retail broadband revenue market share in the Czech Republic is lower than its mobile market share at a Fitch-estimated 31% (1H18) but broadly stable. This reflects a more competitive market structure as a result of alternative WiFi, and cable/fibre local access network infrastructures. Investment plans to increase the depth and breadth of its fibre network to the kerb should support the company's market position.

Structural Separation, Increased Focus: PPF Arena 1 separated its fixed and mobile network infrastructure and retail operations into two companies in the country. Ceska telekomunikacni infrastruktura a.s. (CETIN, BBB/Stable) focuses on infrastructure wholesale, while O2 CR provides

retail services. The separation aims to increase operational focus, efficiency and scale in network investments while reducing regulatory overheads. Mobile network-sharing with T-Mobile, which includes radio access equipment, improves the company's cost structure compared with other European mobile operators and is likely to provide an efficient platform for deploying 5G network services over the next three-to-four years.

Well-Positioned CEE Mobile Assets: PPF Arena 1 acquired Telenor's mobile assets in Hungary, Bulgaria, Serbia and Montenegro in mid-2018 for an enterprise value (EV) of EUR2.8 billion, adding to existing international mobile operations in Slovakia. The acquired assets have number one or two market positions and operate in a three-operator mobile market structure that should support service revenue growth through data monetisation and pre- to post-paid migration. While a lack of fixed network ownership may create disadvantages compared with a convergent network strategy, we see the risks as manageable through partnerships and mobile network infrastructure-sharing.

Limited Headroom but Proactively Managed: We expect PPF Arena 1's FFO adjusted net leverage to increase to 4.1x at end-2019 from 4.0x on a pro-forma basis in 2018. The increase, following the acquisition of Telenor's CEE assets last year, will temporarily breach our downgrade sensitivity of 4.0x and is primarily driven by a higher rate of dividend payments in 2019 and potential spectrum costs in the Czech Republic. We expect that leverage will fall back to 4.0x in the subsequent years as a result of FFO growth and lower dividend payments. This leaves limited headroom in the rating for managing operational pressures in the short term and exploiting new investment opportunities.

Retained Financial Flexibility: PPF Arena 1 manages its leverage profile through a flexible dividend policy, while its financial policy is to manage leverage, based on its definition of net debt-to-EBITDA, at 2.8x-3.2x. This corresponds to 3.8x-4.2x on a FFO adjusted net leverage basis. PPF Arena 1 has pre-dividend free cash flow (FCF) margin around 8%-9%. This provides an organic deleveraging capacity of up to 0.3x-0.4x (FFO adjusted net leverage) a year, if no dividends are distributed and assuming our base case EBITDA growth. The company's intention and ability to adjust dividend payments to maintain leverage within the thresholds of the rating is an essential driver of its investment-grade rating.

Potential FX Risks to Leverage: At end-2018, PPF Arena 1 had about 76% of its total group debt denominated in euros and 24% of its EBITDA (assuming the peg between the euro and Bulgarian lev is maintained) denominated in euros. This creates FX mismatch to leverage. PPF Arena 1 is able to hedge the cash flows it receives in foreign currencies so as to largely mitigate fluctuations in relation to the debt servicing of its current loan. However, a lack of visibility on medium- to long-term FX fluctuations raises risks to leverage.

Consolidated Rating, No Subordination: PPF Arena 1's rating assumes a fully consolidated business scope with no structural subordination as a result of existing subsidiary-level debt. The consolidated basis of the rating reflects the ownership structure and the existence of one-way cross default obligations for PPF Arena 1 on behalf of its operating subsidiaries in the Czech Republic. These factors, on balance, underpin our consolidated assessment as opposed to an approach that deconsolidates the Czech operating companies due to subsidiary-level covenants and financial policies that could restrict dividend upstreaming in extreme situations.

The lack of structural subordination of parent-level debt reflects the low quantum of operating subsidiary-level debt that is sizeably below Fitch's threshold of 2.0x EBITDA.

Standalone Rating Profile: We rate PPF Arena 1 on a standalone basis with no influence from other parts of the PPF Group. The standalone profile reflects a lack of legal, financial and operational ties between PPF Arena 1 and other parts of the group. PPF Group has three main business divisions covering telecommunications, banking and financial services, and real estate. All three units are independently managed and financed.

Derivation Summary

The rating of PPF Arena 1 reflects the strong position of its incumbent telecoms assets in the Czech Republic and its leading mobile position in three central and eastern European (CEE) markets. Funds from operations (FFO)-adjusted net leverage is likely to temporarily exceed our negative sensitivity of 4.0x for the rating in 2019 before declining to this level within the next 12-18 months. This leaves limited headroom within the rating to absorb unforeseen financial and operational pressures.

PPF Arena 1, however, retains significant financial flexibility to manage its leverage profile as a result of dividend flexibility. This flexibility, together with the management's willingness to adjust dividends if needed to sustain the company's leverage profile, has been essential to the company's investment-grade rating.

Key Assumptions

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

- Revenue of around EUR3.2 billion in 2019, growing at 1%-2% a year over the next three years.
- EBITDA margin just over 39% in 2019, gradually increasing to 40.5% over the next three years.
- Cash tax of EUR126 million in 2019 with a broadly stable effective tax rate over the next three years.
- Capex-to-revenue ratio (excluding spectrum costs) of 13% in 2019, increasing to 14% over the next three years.
- Dividend payment of EUR595 million in 2019, reducing to between EUR335 million and EUR390 million in the following three years. The higher dividend in 2019 is the result of the distribution of

cash flow generated in 2018 but delayed to 2019.

- Net debt-to-EBITDA maintained at around the low-to-middle range of the company's target of 2.8x-3.2x.
- Adjusted debt calculated using a weighted average operating lease multiple of 7.6x, reflecting a multiple of 8x for liabilities in the Czech Republic and Slovakia and 7x for liabilities in Bulgaria, Hungary, and Serbia and Montenegro.

RATING SENSITIVITIES

Developments That May, Individually or Collectively, Lead to Positive Rating Action

- Sustained growth in FCF leading to improved FCF margins and organic deleveraging capacity;
- FFO-adjusted net leverage falling below 3.5x on a sustained basis.

Developments That May, Individually or Collectively, Lead to Negative Rating Action

- A material and sustained decline in EBITDA or FCF driven by competitive or technology-driven pressure in core business segments;
- A change in the financial policy that results in reduced financial flexibility, higher long-term leverage targets, or contractual debt obligations to other parts of the PPF Group. Any substantive increase in PPF Group's dependency on PPF Arena 1's dividends would put pressure on the rating.
- FFO-adjusted net leverage trending above 4.0x on a sustained basis.

Liquidity and Debt Structure

Comfortable Liquidity: PPF Arena 1 is refinancing part of its term loan facilities in 2019 with a bond. Prior to this refinancing, PPF Arena 1 had cash and cash equivalents of EUR441 million and an undrawn five-year revolving credit facility of EUR200 million at end-2018. These comfortably cover short-term debt amortisation costs of EUR103 million in 2019. PPF Arena 1 has no other debt maturities in 2019 and pre-dividend FCF provides a further source of liquidity if needed.

PPF Arena 1 BV

---senior secured; Long Term Rating; New Rating; BBB-

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Applicable Criteria

[Corporate Rating Criteria \(pub. 19 Feb 2019\)](#)

[Parent and Subsidiary Rating Linkage \(pub. 16 Jul 2018\)](#)

[Corporates Notching and Recovery Ratings Criteria \(pub. 23 Mar 2018\)](#)

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