Research Update:

PPF Telecom Group B.V. Upgraded To 'BBB-' On Majority Stake Acquisition By e&; Outlook Stable

October 24, 2024

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Rating Action Overview

- On Oct. 24, 2024, Emirates Telecommunications Group Co. PJSC (e&; AA-/Stable/A-1+) acquired a 50%+1 economic share in PPF Telecom Group B.V., known as e& PPF Telecom Group B.V. (e& PPF) after the transaction, e& PPF's assets in Bulgaria, Hungary, Serbia, and Slovakia.
- Under the new perimeter, e& PPF has reduced its size and scale of operations and geographical diversification, which weighs on our view of its business.
- This is offset by the less leveraged capital structure at the new e& PPF. The rating upgrade is also supported by e&'s better credit profile and the fact that it will now control and fully consolidate e& PPF.
- We therefore upgraded our long-term issuer credit rating on e& PPF and its senior unsecured debt to 'BBB-' from 'BB+'.
- The stable outlook reflects our expectation that e& PPF will increase revenue and EBITDA at a mid-single-digit rate in the next 12-24 months, leading to a S&P Global Ratings-adjusted leverage of about 3.0x and free operating cash flow (FOCF) to debt between 10%-15%, excluding spectrum payments.

Rating Action Rationale

The upgrade follows e&'s acquisition of 50%+1 economic share in e& PPF's assets in Bulgaria, Hungary, Serbia, and Slovakia, which are currently owned by PPF Group. In exchange for 50%+1 economic share in e& PPF, excluding its Czech assets, e& paid €2.36 billion. From now on, e& PPF will be fully consolidated within e&. In our view, e& PPF's business under the new perimeter excluding Czech assets will be somewhat weaker, but this is compensated by a more conservative financial policy, resulting in an unchanged stand-alone credit profile at 'bb+' on e& PPF. However, our final rating incorporates the strong credit quality of its new parent e&, leading to a one notch uplift to 'BBB-' for e& PPF. This assessment reflects our view that e& PPF is an important asset in e&'s long-term strategy to establish itself in the European telecom market, as such we view e& PPF as unlikely to be sold.

As part of the transaction, e& PPF has set a more conservative financial policy. e& PPF now targets a reported net leverage of 2.0x, which translates into an S&P Global Ratings-adjusted leverage of about 3.0x and supports its current rating. At the same time, the target net leverage at the 70%-owned infrastructure business will be higher at 3.0x reported net leverage (due to an intragroup loan) and GIC will keep the 30% minority stake in that business with a put option value estimated at about €650 million. We add the value of this put option to our calculation of adjusted debt at e& PPF. There are also preferred shares issues by e& PPF to e&, to grant e& an underlying economic stake of 50%+1 economic share in the infrastructure businesses. Distributions from these preferred shares will be subordinated and secondary to the debt service by e& PPF and we consider these as equity like. The group has also committed to a €1.2 billion revolving credit facility (RCF), providing funds to repay its bond maturing in 2025 and an additional liquidity cushion.

Following the separation of the Czech assets, e& PPF now has smaller scale. The group has roughly halved its EBITDA, to about €900 million from about €1.8 billion, which positions it as a relatively small player compared with many of its European peers, and even more so compared with some of its key competitors (Deutsche Telecom, Vodafone Group PLC, Orange S.A., and A1). The group will now operate in four countries, with the expected EBITDA contribution from Bulgaria, Serbia, and Hungary each representing about 28% and Slovakia about 16% in 2024.

Our business assessment of e& PPF is supported by its strong position in all its mobile markets. We consider the group's sound mobile network infrastructure and capacity, as well as the ongoing upgrade rollout of 5G to be a competitive strength. Through its Yettel Brand, e& PPF is the No. 1 mobile operator in Serbia with a 36% revenue market share and in Bulgaria with a 37% revenue market share and holds a strong No. 2 position with a 26% revenue market share in Hungary and a No. 3 position in Slovakia with a 25% revenue market share. In addition, we regard e& PPF, through Yettel (previously Telenor) to benefit from a strong brand recognition, which is exemplified by having the strongest average revenue per user (ARPU) in all its markets apart from Slovakia.

Our assessment also factors in e& PPF's strong profitability. With an S&P Global Ratings-adjusted EBITDA margin above 40%, which combined with relatively modest capital expenditure (capex) needs over the coming years at about 12%-17% of sales, leads the group to compare favorable to peers with an EBITDA after lease capex-to-sales ratio of about 26% which compares well with similarly sized peers.

We think that e& PPF's mobile markets are moderately competitive. Based on the presence of three mobile network operators in each country (only in Slovakia there is a smaller fourth player), we regard e& PPF's mobile markets as moderately competitive. Over recent years these markets have been characterized by stable market shares and broadly stable and gradually improving ARPU. Furthermore, we see the threat of a fourth player entering the market as fairly low given that key spectrum auctions have taken place in recent years.

e& PPF does not own a fixed broadband network in any of its markets. After the carve-out of the Czech operation, e& PPF will not own any fixed broadband assets. However, we view this as partially compensated by the group's growing fixed wireless access (FWA) offering and its signed wholesale agreements in Serbia and Slovakia. In addition, we regard these markets as less convergent than many Western and Central European markets. That said a rapid push toward convergence from existing fixed-mobile local competitors in these countries could have a significant effect on e& PPF's competitive advantage.

In our view, e& PPF is exposed to some relatively high country risk. e& PPF operates in countries regarded as having a certain degree of jurisdictional uncertainty. That said, we anticipate currency exposure on operations to be limited as we expect revenue streams in general to match operating expenditure and capex elements in the same currency. Furthermore, we factor in the relatively high country risk stemming from jurisdictional uncertainties of Eastern Europe as well as some currency exposure.

Outlook

The stable outlook reflects our expectation that e& PPF will increase revenue and EBITDA at a mid-single-digit rate because we expect the group to monetize its network upgrades, while maintaining its mobile market shares and growing ARPU. We forecast that leverage will remain at about 3.0x and FOCF to debt between 10%-15%, excluding spectrum payments.

Downside scenario

We could lower the rating if adjusted debt to EBITDA sustainably increases above 3.0x, along with FOCF to debt declining to below 10%. This could result from a more competitive market environment, a push toward convergence in markets where the group is a mobile-only operator, or an unexpected and more aggressive return to shareholders. We could also lower the rating if we no longer viewed e& PPF as a moderately strategic asset to e&.

Upside scenario

We could raise the rating if e& PPF's S&P Global Ratings-adjusted debt to EBITDA decreases to below 2.5x and FOCF to debt increases to more than 15%, excluding spectrum, and the group adopts a financial policy that would support such improved credit metrics on a sustainable basis.

Company Description

e& PPF Telecom Group B.V. (e& PPF) is a European telecom group operating in four markets: Hungary, Bulgaria, Serbia, and Slovakia. For retail activities, e& PPF uses its own Yettel brand in Hungary, Bulgaria, and Serbia; and the O2 brand in Slovakia. In all markets, it uses CETIN as an independent wholesale mobile infrastructure provider. The group offers mobile services, fixed broadband, and Pay TV services in all its operating countries. Fiber to the home (FTTH) is offered through a wholesale access in Slovakia and Serbia, and FWA through CETIN's mobile network in Slovakia, Hungary, and Bulgaria.

In 2023, the new perimeter of e& PPF generated about €2 billion of consolidated revenue, and €0.8 billion of consolidated reported EBITDA after leases. As of the end of 2023, e& PPF had 12.3 million mobile customers--including 3.2 million-3.7 million each in Hungary and Bulgaria, 3.0 million in Serbia, and 2.3 million in Slovakia as well as 0.3 million fixed customers.

e& PPF is now owned by 50%+1 economic share by e& and 50%-1 economic share by PPF Group N.V., an international investment conglomerate with four pillars: telecom, financial services, real estate, media, and e-commerce.

Our Base-Case Scenario

Assumptions

- GDP growth of 2%-4% in all its operating markets over the next two to three years.
- Revenue growth of about mid-single digit supported by the migration from prepaid to postpaid mobile services that feature a higher ARPU, increased footprint in fixed services (FTTH in Serbia and Slovakia, and FWA in other countries), and automatic inflation clauses in Hungary and Bulgaria that do not affect churn as competitors have similar clauses.
- Adjusted EBITDA margin to improve gradually over the next two to three years driven by the higher ARPU as well as a decrease in energy prices.
- Working capital outflows of about €90 million in 2024, €30 million in 2025, and €180 million in 2026, mainly driven by the topline growth.
- Capex excluding spectrum representing 17.5% of sales in 2024 and 2025 which will reduce to about 12.0% in 2026, mostly for mobile network maintenance and expansion of 5G coverage.
- Spectrum capex minimal in 2024 and 2026 but expected to be higher for the planned auctions in Serbia and Slovakia.
- Lease liability to remain in the range of €240 million-€260 million during 2024-2026.
- Total dividend payments of €370 million- €500 million per year during 2025-2026.
- Acquisition of the minority stake of the Hungarian business (25%), leading to a full ownership of the Hungarian subsidiary.

Key metrics

Table 1

e& PPF Telecom Group B.V.--Key metrics

	--Fiscal year ended Dec. 31--		
(Mil. €)	**2024f**	**2025f**	**2026f**
Revenue	2,128.0	2,226.0	2,313.0
Revenue growth (%)	6.5	4.6	3.9
Adjusted EBITDA margin on net rev (%)	44.3	44.9	45.8
Capital expenditure (excluding spectrum)	370.0	390.0	280.0
Reported FOCF after leases	293.0	383.0	457.0
FOCF to debt (%)	11.0	13.0	12.0
Debt to EBITDA	3.0	3.0	3.0
EBITDA interest cover	8.6	8.7	7.0

€--Euro. FOCF--Free operating cash flow. f--Forecast.

Liquidity

We assess liquidity as adequate, based on our expectation that liquidity sources to uses will be comfortably above 1.2x in the 12 months. In addition, the group has sound headroom with relation to its covenants, good relationships with banks, and a satisfactory standing in capital markets. We also think that e& PPF can absorb high-impact, low-probability events with a limited need for refinancing as we understand it has flexibility to adjust its capex and reduce its dividend distributions.

Our liquidity calculations include:

Principal liquidity sources:

- About €200 million of cash at closing;
- Fully undrawn committed RCF of €1200 million to be signed after the transaction closes; and
- Cash flow from operations of about €700 million.

Principal liquidity uses:

- Working capital outflows of €100 million;
- Capex of €370 million; and
- Dividend payment of €300 million-€400 million.

Notching Analysis

The unsecured bonds are rated at the same level as the long-term issuer credit rating on e& PPF at 'BBB-'. All of the group's external debt is senior unsecured and issued by e& PPF. We have not identified any significant elements of subordination risk present in the capital structure.

Ratings Score Snapshot

Issuer Credit Rating	**BBB-/Stable/A-3**
Business risk:	Fair
Country risk	Moderately high
Industry risk	Intermediate
Competitive position	Fair
Financial risk:	Significant
Cash flow/leverage	Significant
Anchor	bb
Modifiers:	
Diversification/Portfolio effect	Neutral
Capital structure	Neutral
Financial policy	Neutral
Liquidity	Adequate

Issuer Credit Rating	BBB-/Stable/A-3
Management and governance	Neutral
Comparable rating analysis	Positive
Stand-alone credit profile:	bb+
Group credit profile	bbb-
Entity status within group	Moderately strategic

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities, April 29, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Research Update: Point of Sale Solutions Provider Poseidon BidCo (Ingenico) Affirmed At 'B+' On Refinancing And Dividend; Outlook Stable, Feb. 16, 2024

Ratings List

Upgraded; Outlook Action

	To	From
PPF Telecom Group B.V.		
Issuer Credit Rating	BBB-/Stable/--	BB+/Watch Pos/--

Upgraded; Outlook Action

	To	From
Senior Unsecured	BBB-	BB+/Watch Pos
Recovery Rating	NR	3(50%)