Research Update:

Frigoglass SAIC 'B-' Rating Affirmed On Proposed Refinancing; Outlook Stable; Proposed Notes Rated 'B-'

January 24, 2020

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Rating Action Overview

- Frigoglass SAIC intends to issue €260 million of senior secured notes to refinance its existing first- and second-lien debt.
- The transaction should enable Frigoglass to lower its interest costs and improve its debt maturity profile. Still, we continue to forecast limited free operating cash flow (FOCF) until 2021, and see execution risks in the business plan.
- We are therefore affirming our 'B-' long-term issuer credit rating on Frigoglass, the parent company.
- We are also assigning our 'B-' issue rating to the proposed senior secured notes due 2025.
- The stable outlook reflects our view that Frigoglass should be able to maintain stable operating performance in its two divisions, with S&P Global Ratings-adjusted debt to EBITDA below 5.0x and broadly neutral FOCF.

Rating Action Rationale

Despite extending its debt maturity profile, a lack of committed credit lines under the new capital structure and a restricted ability to raise debt under the draft documentation post-transaction close limit Frigoglass' ability to cope with unforeseen events such as large cost overruns or working capital swings. Post-transaction close, which we expect to occur in the first quarter of the fiscal year ending Dec. 31, 2020, Frigoglass will have approximately €70 million of on-balance-sheet cash, limited short-term debt maturities, no maintenance financial covenants, and potentially lower interest costs.

We understand that Frigoglass has already secured most of its sales in 2020 with its major customers in the glass division (Coca-Cola bottlers and major breweries). We think the company has sufficient liquidity sources to cope with potential headwinds during the planned shutdown of one of its glass furnaces in Nigeria for four months in the first half of 2020. The shutdown will allow for capacity expansion.

Frigoglass continues not to expect any material disruption to supply during the shutdown period. It expects the furnace to be fully operational again by the end of the second quarter of 2020, with the resulting 50% production capacity increase supporting the company's top-line growth from 2021. As always with large projects in emerging markets, we think there is still a risk of potential delays and/or cost overruns. Nevertheless, we think that Frigoglass will remain adequately funded for the next 12 months.

In the next 12-18 months, Frigoglass' S&P Global Ratings-adjusted leverage should remain within the 4.0x-5.0x range, but with limited free operating cash flow (FOCF) generation. Frigoglass' credit metrics lie well within our base-case ranges, despite a higher top-line and EBITDA generation in 2019 due to a one-off customer order in the ice cold merchandisers (ICM) division in the final quarter. In terms of operating performance, we think that that the business strategy is starting to pay off. For 2019, we anticipate revenue growth of about 13.0%-14.0% (about €473 million) and adjusted EBITDA margins after restructuring costs of about 14.0%.

Despite the one-off impact on overall growth, the company's refreshed commercial focus since 2017 has led to increased market share with major breweries and other smaller local customers in its end markets. This is resulting in moderate diversification of its customer profile in the ICM division, with the share of Coca-Cola bottlers trending down to 64.4% of revenues as of the end of the third quarter of 2019, from 71.4% in the same period in the prior year.

In 2019, Frigoglass also completed the final round of its restructuring by closing its Greek plant, and in our view, its reduced manufacturing footprint should support future profitability. In the near-to-medium term, therefore, management intends to focus on pursuing further commercial opportunities, with both existing and new customers. In addition, it plans to continue outsourcing the manufacturing of lower-margin coolers to third parties and remains focused on other cost-cutting initiatives such as centralizing procurement.

For 2020, we see a revenue decline due to the one-off customer order in the last quarter of 2019, but broadly stable absolute EBITDA. Nevertheless, we do not anticipate that adjusted leverage will improve materially, but rather remain well within the 4.0x-5.0x range. Volatility of credit metrics could resume due to the company's large exposure to emerging markets, notably Nigeria, which has a history of currency volatility.

FOCF should gradually strengthen from 2021, once the large capital investment projects diminish. We forecast improved FOCF generation only from 2021 on the back of reduced capital expenditure (capex) requirements, particularly as the company concludes its glass furnace expansion in Nigeria, which will cost about €30 million in total between 2018 and 2020. In 2020, FOCF generation will likely be close to break-even levels, due to still-high capital investments. These include the final round of the expansion of the glass furnace in 2020, a rebuild in another of the company's plants in Nigeria (Delta), the implementation of the enterprise resource planning (SAP) system, and continued new product development in the ICM division.

Outlook

The stable outlook reflects our view that Frigoglass should be able to maintain adjusted debt to EBITDA of below 5.0x, while maintaining break-even to slightly positive absolute FOCF generation until 2021, as the company executes its capex program.

We assume that Frigoglass will successfully execute the expansion of the glass furnace in Nigeria, and maintain stable reported EBITDA margins of 14.0%-15.0% despite the temporary constraints on production capacity we expect in 2020 due to the furnace shutdown.

Downside scenario

We could lower the rating on Frigoglass if, contrary to our base case, the company's operating performance deteriorates markedly, with little prospect of a rapid improvement. In our view, this could occur if there is a large cost overrun or delay in the expansion of the glass furnace in Nigeria, together with other large stresses on the operating cost base, and pricing pressure from key customers. A downgrade could also occur from lower volume growth than we expect, despite the ongoing capacity expansion.

Under such a scenario, we would likely observe reported EBITDA falling closer to or below €60 million, thereby resulting in materially negative FOCF, with EBITDA cash interest coverage falling to closer to 2.0x, which could pressure the company's liquidity position.

Upside scenario

We could raise the rating on Frigoglass if the company continues to deliver strong profitable growth. We would need to have strong visibility on revenue generation, and see continued improvements in customer diversity and operating margins. In our view, operating margins could benefit from increased volume growth in the glass division, procurement savings, and continued outsourcing of the production of low-margin coolers in the ICM division. In this scenario, we would likely see, on a sustained basis, adjusted debt to EBITDA within the 4.0x-5.0x range, and a track record of materially positive FOCF. The latter would occur, in our view, once the company concludes its heavy capital investment plan in the glass division.

Company Description

Frigoglass engages in the manufacture, distribution, and sale of commercial refrigeration units (coolers), and glass packaging materials for the beverage industry.

The company operates through two divisions:

- The ICM division for beverage coolers and related services; and
- The glass division for glass bottles, containers, and other associated products.

The ICM division represented about 75% of total sales in 2018 and is supported by longstanding relationships with large customers in the soft drinks and alcoholic beverage industries in both mature and emerging markets.

The glass division (25% of sales in 2018) is a more capital-intensive business and is primarily focused on West African markets, with Nigeria being the main market. Both divisions have a similar client base and are heavily exposed to Coca-Cola bottlers, which represented about 60% of total annual sales in 2018, followed by breweries, representing 23% of sales.

In 2018, Frigoglass reported total sales of about €417 million and EBITDA of about €56 million, with an EBITDA margin of 13.5%. Emerging markets contribute the most to revenue--Africa and the Middle East represented 39% of sales in 2018, followed by Eastern Europe (34%), Western Europe (20%), and Asia (7%). The company is based in Athens, Greece, and is listed on the Athens stock exchange. It was spun-off from Coca Cola HBC in 1996.

Our Base-Case Scenario

In our base-case scenario for 2019-2021, we assume:

- An overall revenue decline of about 3.0%-4.0% in 2020, as in 2019, the top-line will see a positive impact from a one-off order in the ICM division in the fourth quarter of 2019.
- Revenue growth of 3.0%-4.0% in 2021, mostly driven by increased capacity in the glass division following the furnace expansion in 2020, as well as ongoing commercial efforts in Asia, Africa, and Europe in the ICM division. The company plans to introduce third-party manufactured coolers in Asia, and is actively seeking to increase its exposure to major breweries, such as Heineken and Diageo in Africa.
- Broadly stable reported EBITDA margins of around 14.0%-15.0% in 2020 and 2021. In 2019, we forecast a reported EBITDA margin after restructuring costs of close to 14.0%. Despite the decline we expect in revenues in 2020, we forecast broadly flat absolute EBITDA. EBITDA generation should be supported by the completion of the recent manufacturing footprint optimization, and a lack of restructuring costs in future. We also anticipate a gradual increase in the outsourcing of low-margin coolers and centralized procurement efforts to support profitability and broadly offset a likely increase in raw materials.
- An annual net working capital outflow of up to €20 million in 2019, partly due to the pre-purchase of raw materials ahead of the glass furnace shutdown at the beginning of 2020. We anticipate stabilized outflows of approximately €5 million-€10 million per year thereafter.
- Annual capex for 2019 and 2020 of about €29 million due to the furnace expansion and other capacity increases in the glass division, the renovation of existing plants in the ICM division, and the implementation of the common SAP system. Annual capex will then normalize to about €20 million-€24 million from 2021.
- No shareholder remuneration or acquisitions, as the company remains focused on pursuing value-accretive internal investment opportunities.

Based on these assumptions, we arrive at the following credit metrics:

- Adjusted debt to EBITDA of 4.0x-5.0x; and
- Adjusted EBITDA cash interest coverage of close to 4.0x.

Liquidity

We assess Frigoglass' liquidity as adequate, reflecting our estimate that the company's sources of cash should cover its uses by about 1.2x over the next 12 months, supported by the lack of meaningful near-term debt maturities. We have assessed Frigoglass' liquidity post-transaction close, which we expect in the first quarter of 2020.

We expect that Frigoglass' principal liquidity sources during the next 12 months will comprise:

- Cash and cash equivalents of about €70 million post-transaction close; and
- Annual cash funds from operations of €35 million-€40 million before capex and working capital movements.

We expect that Frigoglass' principal liquidity uses during the same period will comprise:

- Short-term bank debt at operating subsidiaries of about €37 million; and
- Our forecast of an annual net working capital outflow of about €5 million-€10 million.
- Our forecast of annual capex (both maintenance and growth) of about €25 million-€30 million.

Covenants

Under the proposed debt documentation, Frigoglass is subject to incurrence-based financial covenants stipulating pro forma consolidated EBITDA to fixed-charge coverage of no less than 2.0x, and net senior secured leverage (excluding the impact of International Financial Reporting Standard 16) of no more than 2.7x. The company is restricted from raising additional debt in the near term due to opening net leverage post-transaction close being above 3.0x.

Issue Ratings - Subordination Risk Analysis

Capital structure

Post-transaction close, Frigoglass' capital structure will comprise the €260 million senior secured notes due 2025, and approximately €37 million of short-term bank debt issued at operating subsidiaries in India, Russia, and Nigeria. The company rolls this debt over annually, and mostly uses it for working capital purposes.

Analytical conclusions

The issue rating on the proposed senior secured notes is 'B-', in line with the issuer credit rating on Frigoglass. The issue rating is supported by the lack of material priority-ranking debt liabilities in the company's capital structure, comprising the short-term bank debt issued at the operating subsidiaries.

Ratings Score Snapshot

Issuer credit rating: B-/Stable/--

Business Risk: Weak

- Country Risk: Moderately High
- Industry Risk: Intermediate
- Competitive position: Weak

Financial Risk: Highly leveraged

- Cash flow/Leverage: Highly leveraged

Anchor: b-

Modifiers:

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Management and governance: Fair (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: b-

Related Criteria

- 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 | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Consumer Durables Industry, Dec. 12, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Criteria For Assigning 'CCC+', 'CCC', 'CCC-', And 'CC' Ratings, Oct. 1, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Research Update: Frigoglass SAIC Outlook To Stable On Good Progress On Its Business Plan; 'B-' Ratings Affirmed, Sept. 24, 2019

Ratings List

New Rating	
Frigoglass Finance B.V.	
Senior Secured	B-

Ratings Affirmed	
Frigoglass SAIC	
Issuer Credit Rating	B-/Stable/--
Frigoglass Finance B.V.	
Senior Secured	B-
Senior Secured	CCC+

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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