Envien Magyarország Kft.
Hungary, Integrated Chemicals

SCOPE BB STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2021**	**2022***	**2022 E**	**2023 E**
Scope-adjusted EBITDA/interest cover	0.4x	1.8x	3.0x	2.8x
Scope-adjusted debt/EBITDA	258%	42%	27%	29%
Scope-adjusted funds from operations/debt	162x	45x	7x	8x
Scope-adjusted free operating cash flow/debt	53%	12%	13%	15%

*Preliminary

Rating rationale

The issuer rating of Envien Magyarország Kft. is based on the credit metrics of its direct parent, Envien International, which is the holding company of Envien Group, the leading biofuel producer in Central and Eastern Europe (CEE). Within the group, Envien Magyarország is a pure trader of animal feed products that primarily uses the by-products of Envien Group's biofuel production. The rating is based on Envien International's implicit guarantee to Envien Magyarország given the shared name identity, brand responsibility, intercompany funding and Envien Magyarország's importance for the group, as well as the parent's explicit, unconditional and irrevocable guarantee on the bond issued by Envien Magyarország under the Bond Funding for Growth Scheme.

The issuer rating of Envien International reflects good but deteriorating financial credit metrics offset by a moderate business risk profile. The business risk profile is limited by low and volatile margins dependent on commodity market fluctuations, limited company size on an international scale despite strong market shares in small core markets and improving diversification.

Outlook and rating-change drivers

The Outlook is Stable and assumes no change in regulation, taxation and law. The outlook incorporates our assumption that the EBITDA will continue to decline in 2023 to around EUR 60m with margins pressured by volatile prices and persisting high energy and raw material costs. We expect leverage to deteriorate towards 3x in 2023, depleting the formerly built-in rating headroom, but remaining in the range 2-3x over the medium term.

A positive rating change is possible in case of Scope-adjusted debt/EBITDA sustained below 1.5x.

A negative rating action could be driven by SaD/EBITDA of Envien International deteriorating above 3.0x due to protracted pressure on production margins and/or the introduction of large capex investments to build second-generation facilities that are not included in Scope's base case. Additionally, liquidity risk may arise in case of a further large increase in working capital needs that unused overdraft lines cannot cover or the unexpected cancellation of one or more of such lines. Although a remote possibility - a change in parent ownership for Envien Magyarország (i.e. Envien International being replaced by a financially weaker entity) could also lead to a negative rating action.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
17 MAR 2023	Affirmation	BB/Stable
18 MAR 2022	Affirmation	BB/Stable
24 MAR 2021	New	BB/Stable

Ratings & Outlook

Issuer	BB/Stable
Short-term debt	-
Guaranteed senior unsecured bond rating ISIN: HU0000360193	BB

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Related Methodologies

General Corporate Rating Methodology; July 2022

Chemicals Rating Methodology; April 2022

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Past and future demand generated by regulatory requirements (biofuels) • Strong market presence in CEE, especially in Slovakia (100% market share), despite limited capacity at EU level • Good financial metrics despite increasing debt on working capital needs and recent Biopaliwa's acquisition • Production diversified across several plants in CEE (six production plants) as well agricultural commodity trading activities in Slovakia, Hungary and Switzerland.	• Limited EBITDA margins oscillating around 11% over time amid dependency on volatile prices and recent extremely high energy prices • Product portfolio mostly including commoditised products with limited pricing room • Concentration on single product group (biofuels) • Large single customer concentration on MOL Group, mitigated by the synergistic business relationship • Geographical concentration of sales to Slovakia and Hungary, expected drop below 50% after Biopaliwa's acquisition in Poland • High dividend payout in the past two years

Positive rating-change drivers	Negative rating-change drivers
• Scope-adjusted debt/EBITDA of parent improving below 1.5x on a sustained basis	• Scope-adjusted debt/EBITDA of parent reaching above 3.0x due to protracted pressure on production margins and/or large capex to build second-generation facilities • Liquidity risk from further large increases in working capital needs that existing unused overdraft lines cannot cover, or the unexpected cancellation of overdraft lines • Change of majority owner of Envien Magyarország (i.e. Envien International being replaced by a weaker entity)

Corporate profile

Envien Magyarország Kft. is a fully-owned subsidiary of Malta-based Envien International Ltd., the consolidating entity of Envien Group, one of the largest producer of first-generation biofuels (bioethanol and biodiesel) in Central and Eastern Europe (CEE). The activities of Envien Group group include the procurement of feedstock; the production and commercialisation of biofuels; the trade of the by-products of the production process (animal feeds and corn oil from bioethenol, chemicals such as glycerine from biodiesel) as well as the trade of related products acquired for resale; and the production of heat and energy.

Envien Group started in 2005 with the construction of the Enviral bioethanol plant in Slovakia and has gradually grown into a group of 12 interconnected companies in six countries (Slovakia, Czech Republic, Hungary, Poland, Switzerland and Croatia). It now employs over 600 staff and it is privately held.

Member companies are Enviral, Meroco, Enagro, Poľnoservis, Rossi Biofuels, Biodizel Vukovar, Biopaliwa Poland (since Q4 2022), Envien Hungary, Ethanol Energy Vrdy, RT Logistic and Envien Trading (Switzerland). Envien Magyarország is a pure trader of animal feed products, primarily using the by-products of Envien Group's biofuel production. Envien International provides an unconditional and irrevocable guarantee on the bond issued by Envien Magyarország.

Financial overview

				Scope estimates	
Scope credit ratios	**2020**	**2021**	**2022 Prelim.**	**2023 E**	**2024 E**
Scope-adjusted EBITDA/interest cover	0.4x	0.4x	1.8x	3.0x	2.8x
Scope-adjusted debt/EBITDA	255%	258%	42%	27%	29%
Scope-adjusted funds from operations/debt	67x	162x	45x	7x	8x
Scope-adjusted free operating cash flow/debt	145%	53%	12%	13%	15%
Scope-adjusted EBITDA inEUR '000s					
EBITDA	58,888	129,349	92,961	60,720	64,104
Losses (gains) on fixed assets disposal	-18	-298	-95	0	0
Scope-adjusted EBITDA	**58,888**	**129,349**	**92,961**	**60,720**	**64,104**
Funds from operations in EUR '000s					
Scope-adjusted EBITDA	58,870	129,051	92,866	60,720	64,104
less: (net) cash interest paid	-873	-797	-2,083	-8,150	-7,950
less: cash tax paid per cash flow statement	-5,174	-11,414	-32,524	-4,353	-4,725
add: dividends from associates	1,930	2,151	2,024	1,000	1,000
Other items	329	-1,611	9,988	0	0
Funds from operations	**55,082**	**117,380**	**70,271**	**49,217**	**52,429**
Free operating cash flow in EUR '000s					
Funds from operations	55,082	117,380	70,271	49,217	52,429
Change in working capital	12,786	-66,414	-30,436	-2,385	-1,279
Non-operating cash flow	0	0	0	0	0
less: capital expenditure (net)	-32,466	-23,337	-16,830	-20,000	-20,000
less: lease amortisation	-4,008	-3,365	-3,611	-3,500	-3,500
Free operating cash flow	**31,394**	**24,264**	**19,394**	**23,332**	**27,651**
Net cash interest paid in EUR '000s					
Net cash interest per cash flow statement	-873	-797	-2,083	-8,150	-7,950
Change in other items	0	0	0	0	0
Net cash interest paid	**-873**	**-797**	**-2,083**	**-8,150**	**-7,950**
Scope-adjusted debt in EUR '000s					
Reported gross financial debt	91,843	137,011	232,699	238,699	228,699
less: cash and cash equivalents	-72,311	-91,444	-66,106	-58,938	-50,089
Other items	2,075	0	0	0	0
Scope-adjusted debt	**21,607**	**45,567**	**166,593**	**179,761**	**178,610**

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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)	Grey leaf	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)	Grey leaf	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	Grey leaf	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)

Resource management

We assess ESG factors as neutral. As usual for chemical companies, the main ESG factors are environmental: greenhouse gas emissions and consumption of raw materials, in particular water and energy. We do not see Envien as an outlier within its industry.

Health and safety

Health and safety issues for the staff is a common factor in the chemicals industry and is a material ESG factor for Envien, given physical hazards (e.g. explosion risks) linked to its products. Since there has not been any major incident, health and safety is a neutral factor.

Regulation is relevant for Envien's sector

With regards to the specific sector of first-generation biofuels (Envien Group's core business), regulatory risk is a material ESG factor for Envien. While the regulatory-driven increase in use of biofuels has reduced carbon emissions and has supported the demand for Envien products so far, the use of first-generation biofuels (based on food and seed crops) poses a risk in terms of food security and the European Union is trying to gradually transition to second-generation biofuels. Until now, we did not see major regulatory changes concerning first-generation biofuels that would represent a material threat and therefore we consider it ESG neutral. Nevertheless, significant changes in future regulations may negatively impact the credit profile.

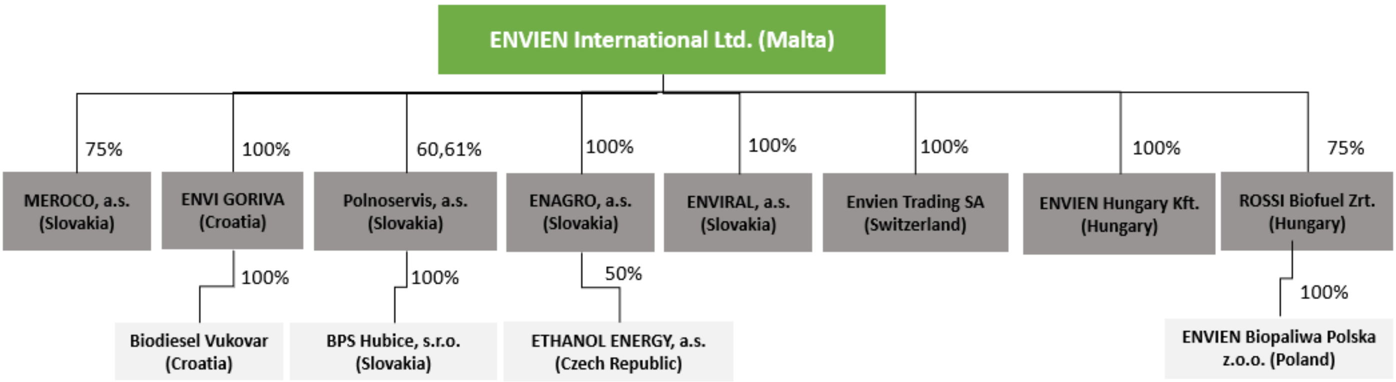
[1] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BB-

Industry risk profile: BBB

We place Envien Group in the integrated chemicals industry, which we rate at BBB. Price risks come from both upstream and downstream. The industry faces high cyclicality due to a great sensitivity to fluctuations in raw material prices, especially for commodity products. Market entry barriers are high due to extensive capex requirements and intellectual property rights. Substitution risk is low due to strict technical production requirements, a lack of alternative production methods, and product uniqueness (especially bespoke chemical solutions).

Figure 1: Envien Group structure



Source: Envien

Key product demand mandated by government regulations

The group's key products are biofuels mixed with conventional diesel and gasoline to meet EU requirements. They use agricultural commodities as inputs to produce oils and ethanol in large volumes. According to Envien Group, the group is ranked ninth for bioethanol production in the EU and 10th for fatty acid methyl esters for biodiesel. The EU Renewable Energy Directive II (Directive (EU) 2018/2001) mandates the increasing use of biofuels to promote renewable energies and meet EU emission reduction targets. As such, demand is primarily driven by changes in these mandates, with an increasing tendency to move away from supporting first-generation biofuels using traditional agricultural feedstocks such as sugar starch (e.g. sugar cane, corn) and edible oil (e.g. rapeseed, soybean), capped at 7% of consumption. Each country then has its own specific mandate within the EU directive.

Second-generation biofuels a long way away from replacing first-generation ones

The EU is promoting the use of advanced biofuels[2], which use non-food biomass. The industry is focused in developing second-generation biofuels, i.e. those generated from cellulose, agricultural residue and waste, although they are not yet commercialised on a large scale due to their higher costs and are therefore expected to influence the market only in the long term (maybe a decade). The EU Renewable Energy Directive II introduced a minimum target of 3.5% of advanced biofuels for transport energy by 2030 (gradually achieved via 0.2% in 2022, 1% in 2025). Within advanced fuels, those sourced from used cooking oil and animal fats (feedstock list B) are capped at 1.7% by 2030.

Recovering demand for biofuels post-Covid

Global biofuel production was 1.8m barrels a day in 2021 (1.7m in 2020), with the vast majority produced in the US and South America; Europe produced less than 15%. While in the medium term, we expect global fuel demand to remain sustained and supported by

[2] Advanced biofuel sources are classified by the EU in two feedstock lists. Feedstock list A (target of 3.5% by 2030): algae if cultivated on land in ponds or photobioreactors, biomass fraction of mixed municipal waste, biowaste from private households subject to separate collection, biomass fraction of industrial waste not fit for use in the food or feed chain, straw, animal manure and sewage sludge, palm oil mill effluent and empty palm fruit bunches, crude glycerin, bagasse, grape marc and wine lees, nut shells, husks, cobs cleaned of kernels of corn, Biomass fraction of wastes and residues from forestry and forest-based industries, other non-food cellulosic material, other ligno-cellulosic material except saw logs and veneer logs. Feedstock list B (capped at 1.7% by 2030): used cooking oil, some categories of animal fats.

regulatory forces, in the long run, we expect growth in biofuels to be constrained by generalised fuel efficiency despite growing transport use. The move away from fossil fuels and towards electric and hydrogen vehicles will also curb demand.

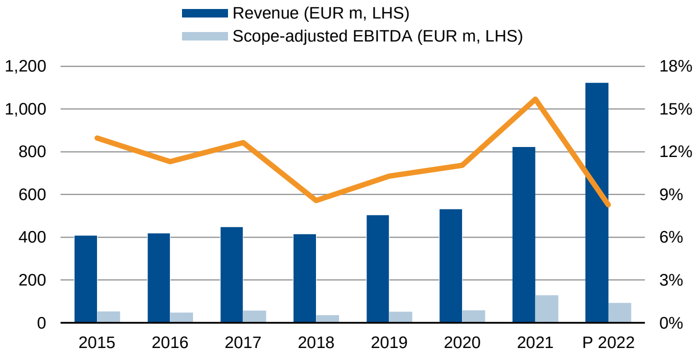
Strong position in CEE, limited market position within EU

Envien Group has strong positions in its core markets: it produces 100% of Slovakian biofuel (effectively a monopoly); its market share in Hungary is higher in biodiesel (around 30%), while in the Czech Republic is higher in bioethanol (around 40%). After a strong 2021, Envien Group reported a record EUR 1.12bn revenue in 2022 (EUR 822m) on the back of continued high prices and higher trading revenue. Generally, Envien Group's revenue has ranged between EUR 400m and 550m from 2015 to 2020.

Entry onto the Polish market in 2022

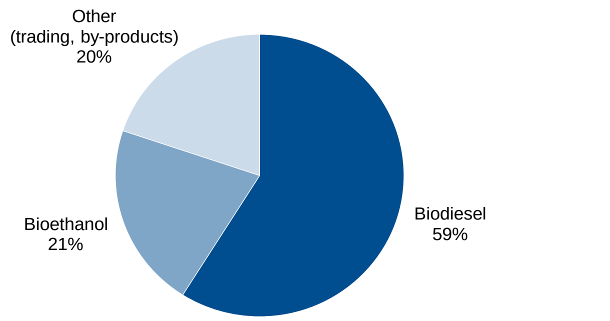
In October 2022, Envien finalised the acquisition of Lotos Biopaliwa in Poland from PKN Orlen for an estimated transaction value between EUR 30-45m through its joint venture in Rossi Biofuel (75% owned, remainder 25% held by MOL). PKN Orlen sold its 100% stake in Biopaliwa as part of the remedial measures approved by the European Commission in connection with the merger of PKN and Lotos Group. Biopaliwa (now Envien Biopaliwa Poland) – a producer of fatty acid methyl esters based on rapeseed oil used for biodiesel – has enabled Envien to enter the Polish market via one of the leading local producers (estimated market share below 10%). The ambition is to reach 10% market share thanks to increasing capacities at the existing plant. We assume the Polish business to cover around 10% to 15% of Group's EBITDA from 2023.

Figure 2: Envien International – key financial figures



Source: Envien, Scope

Figure 3: Envien International – sales by product (2022)



Source: Envien, Scope

Fairly protected and mature local markets

Envien Group has a strong position within the CEE region, albeit in a small niche, and is less strong in the EU. Nevertheless, the biofuel markets in which Envien operates are rather mature and protected from foreign players or new entrants/capacity: in fact, local players generally have lower logistic costs and each country has a specific set of product specifications that often can only be met by local producers. Additionally, the construction of new first-generation plants (which would potentially compete with Envien) is discouraged by the significantly more stringent requirements in terms of greenhouse gas savings (70% from 2021) compared to existing first-generation plants (50% savings only required). As the industry is set to gradually switch to advanced biofuels, building a new first-generation plant also presents risks in terms of estimated useful life. All the above-mentioned factors help to explain the relatively stable market share of the group in recent years.

Production and procurement spread across different sites

The business risk profile benefits from diversification as Envien Group's production capacity is spread across its CEE subsidiaries. There are now six biofuels production plants across Slovakia (Enviral and Meroco), Hungary (Rossi Biofuels), the Czech Republic (Ethanol Energy), Poland (Biopaliwa) and Croatia (Biodizel Vukovar); one rapeseed oil plant (intermediate process) in Slovakia (Polnoservis); and agricultural commodity trading in Slovakia (Enagro), Hungary (Envien Magyarország) and Switzerland (Envien Trading SA).

Limited product diversification

Portfolio diversification is concentrated into two main products: ethanol and biodiesel. These are commodities and their business cycles are strongly correlated as they are both directed towards the same transportation end-markets. Additionally, Envien sells by-products (including animal feed) and trades related products (including those not internally produced), yet these generally do not exceed 20% of revenues. Overall, the share of specialty products sold by Envien Group is negligible.

Start of advanced biofuel production in 2022

In 2022, the Hungarian subsidiary Rossi Biofuels opened a multi-feedstock plant at its facility in Komaron able to produce advanced (second-generation) biodiesel by adopting the Repcat process technology (patented by BDI). The annual capacity of this plant is around 50k tonnes, of which less than half is directed toward advanced biodiesel, therefore representing a very limited portion of the group's biodiesel capacity (about 450,000 tonnes).

Improving geographical diversification

Geographical diversification is moderate with over 55% of sales from Slovakia and Hungary as of FY 2021. Own products are sold only in CEE countries (including Czech Republic, Austria and Romania), while the trading activity of Envien Switzerland (trading of related agricultural products) is directed towards several EU countries. Nevertheless, diversification is set to improve in 2023 with the consolidation of Biopaliwa Poland, expected to contribute around 10-15% of EBITDA.

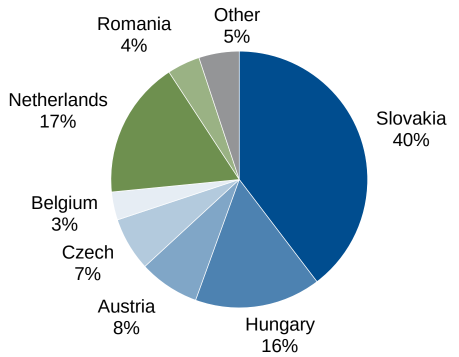
New joint venture in India

On March 15th, 2023, Envien signed the agreement for a 50/50 joint venture equity investment in India with Zuari Industries Limited for the construction and operation of a fully grain-based distillery with capacity of 150 kilo liters per day.

Customer concentration on MOL mitigated by synergistic relationship and recent M&A

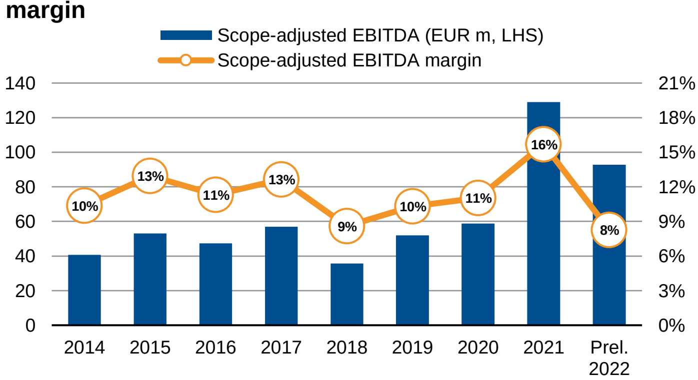
On the customer side, there is a concentration on the Hungarian oil and gas group MOL (including its subsidiary Slovnaft), which accounted for close to 70% of Envien Group's biofuel sales (trading sales are not included) in 2021, but decreased to around 50% after the Biopaliwa acquisition, which brought another large customer: PKN Orlen. Both customers together are estimated to cover around three-quarters of biofuel sales and around 60% of total group sales. The risk of a key client dependency on MOL is mitigated by the fact that a material part of the exposure derives from Rossi Biofuels, an entity owned by both Envien Group (majority) and MOL (minority), also located at MOL's site in Hungary. We consider this close and synergistic relationship as having little risk of deteriorating.

Figure 4: Envien International – sales by country (2021)



Source: Envien, Scope

Figure 5: Envien International – Scope-adjusted EBITDA margin



Source: Envien, Scope

Diversified suppliers

The supplier side is more diversified, with the largest supplier, Interagros, representing around 20% of supplies and the top five covering close to 50%. The pool of suppliers is further enlarging, with new relationships being established with Ukrainian suppliers (because of the Russia-Ukraine war) as well as Polish ones.

Profitability dependent on commodity price

The profitability of biofuel producers is closely related to their market prices, which in turn are linked to feedstock prices and crude oil prices. Because of this high dependency on market prices, it is generally difficult to predict margins beyond one year.

Some natural price hedge from the timing of purchases and the mix of long-term and spot contracts...

Price risk management is based mostly on buying most feedstock during harvest (when prices are generally lower), which would cover not only the production needs of the harvest period but also around 25% of needs for the rest of the year. Feedstock is represented by rapeseed (harvest period in July to August) and corn (harvest period at the end of September until December), whose prices tend to rise in the summer. The risk strategy also involves having a mix of long-term (five years) and spot contracts to diversify risk. The pricing of long-term contracts is modified based on market development: while sourcing contracts are mostly based on variable market prices, supply contracts use a price formula that includes premiums or discounts over a specific benchmark.

... but Envien has started using financial hedges since the Russia-Ukraine war

This mechanism based on timing has worked as a natural hedge for several years, but the start of the Russia-Ukraine war has altered the seasonal price development and made feedstock expensive also during harvest periods. This – together with the high price volatility of the past few years – has led Envien to start using financial hedges on rapeseed biodiesel in 2022 and will extend the use of hedging to bioethanol in 2023.

Profitability in 2022 hindered by high raw material and energy costs

The Scope-adjusted EBITDA margin fluctuated around 11% over 2014-2022. Prices for biofuels have been on the rise over the last few years, leading to record EBITDA levels of EUR 129m in 2021 and EUR 93m in 2022 (preliminary unaudited results), compared to below EUR 60m up to 2020. Envien International achieved a very strong performance in 2021 with an EBITDA margin at around 16% thanks to continuously increasing prices and favourable timing between the purchase and sale of raw materials. In 2022, biofuel prices remained high but had a volatile development and the EBITDA margin declined markedly to around 8%. Besides high feedstock prices, the other key driver for the weaker profitability was the extreme increase in energy costs (reaching around 5% of sales). Envien Magyarország decreased production, keeping output below full capacity due to higher production costs, hence limiting profitability. In addition, some of the production of dried distillers grains with solubles, which uses natural gas as feedstock, was switched to lower value added production of wet protein in order to save costs.

Margin pressure to remain in 2023

For 2023, we expect EBITDA to decline towards EUR 60m with profitability pressured by volatile prices and persisting high energy and raw material costs. Additionally, we expect a high single-digit increase in salaries as a consequence of general inflation. The base scenario sees the EBITDA margin further declining to below 7%in the short-term, which is a conservative assumption considering some energy price normalisation in recent months and the company track record over the past ten years. Our base case scenario assumes EBITDA will remain between EUR 60m and EUR 65m in the medium term amid gradually improving margins and declining biofuel prices.

Financial risk profile: BBB

Credit metrics based on Envien International

As mentioned earlier, we base the rating of Envien Magyarország on the credit metrics of Envien International, given the latter's unconditional and irrevocable guarantee for Envien Magyarország's bond issuance (no other material financial debt at Hungarian subsidiary).

Financial risk profile deteriorating

Envien International has generally shown strong financial metrics in the past thanks to its low Scope-adjusted debt. However, since last year, the financial risk profile has deteriorating amid the increase in debt mainly from higher working capital needs in the last two years but remains quite strong, assessed at BBB.

Base scenario assumptions

The main assumptions under our base scenario include:

- gradual and moderate decline in biofuel prices amid stable demand
- EBITDA between EUR 60m and EUR 65m per year in the medium term
- Interest expenses around EUR 8m per year
- Capex at EUR 20m per year
- Dividends payout ratio between 70% to 90% of previous year net profits
- No sizable acquisition

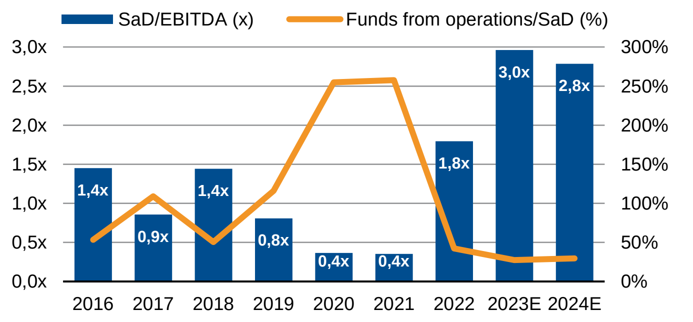
Debt increased in 2022

Scope-adjusted debt increased by around EUR 100m in 2022, leading to a deterioration in Scope-adjusted debt/EBITDA to 1.8x compared to only 0.4x a year earlier. we had foreseen this deterioration in leverage in last year's review based on rapid cost inflation. The key drivers of the Scope-adjusted debt increase were the persisting high working capital needs and the large dividend distribution of EUR 97m in 2022 year (corresponding to almost 100% of FY 2021 net profits); investment loans taken by subsidiary Polnservice for around EUR 20m; and the above-mentioned acquisition of Biopaliwa.

Leverage to increase towards 3.0x in the short term

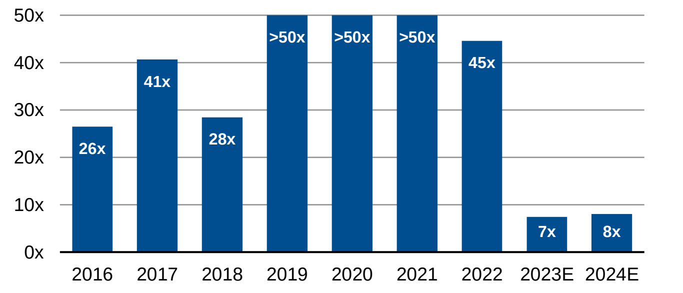
In 2023 we assume leverage to further increase to around 3.0x amid broadly stable debt but declining EBITDA at around EUR 60m. Similarly, Scope-adjusted funds from operations/debt declined in 2022 but remained strong, atabove 40%. We expect this metric to further deteriorate to around 30% in 2023. The recently announced joint venture agreement in India does not have a material impact on financial metrics, as the expected investment from Envien's side will remain below EUR 10m and accounted at equity.

Figure 6: Envien International's leverage



Source: Scope estimates

Figure 7: Envien International's EBITDA interest cover



Source: Envien, Scope estimates

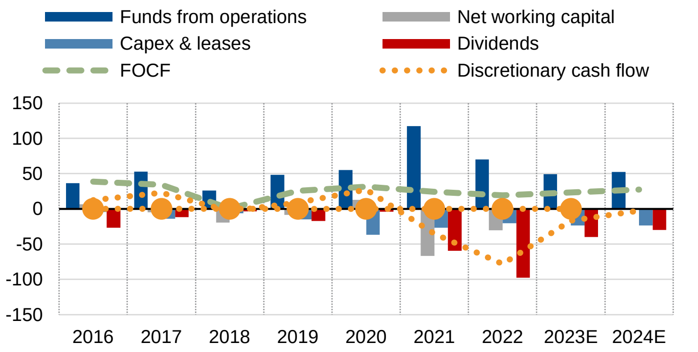
Interest cover deteriorating in 2023 to below 10x

Interest cover has been an extremely strong metric until 2022 given the low interest rate regime and lower gross debt levels. From 2023, a significant increase in interest expenses to around EUR 8m will be driven by the rising costs of bank overdrafts (increasing base rate based on Euribor), which we assume will bear a 3.5% interest rate over the forecasted period. Some gradual decline in interest expenses is assumed from 2024 as the amount of overdraft is expected to decline (the interest rate on overdraft is currently higher than the average for other borrowings, most of which have fixed rate), resulting in an EBITDA cash interest cover of around 8x over the medium term, still a strong metric but significantly lower than in previous years.

Cash flow cover to remain around 15%

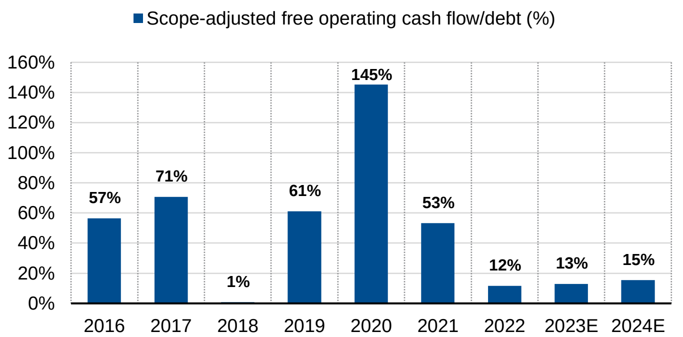
Scope-adjusted free operating cash flow/debt weakened in 2022 to 12% from around 50% in 2021, mainly driven by higher debt despite free operating cash flow maintained at around EUR 20m despite high working capital needs but lower capex at EUR 17m (the major capex project in 2022 was the construction of the degumming unit at Polnoservis). For 2023/24, we expect the cash flow cover to remain constrained at around 15%, since the expected decrease in EBITDA will only partly be compensated by normalising (i.e. lower) net working capital outflows, while capex is expected at around EUR 20m per year over the forecasted period. Our assumptions also include a yearly dividend distribution of EUR 30m to EUR 40m and the absence of material M&A.

Figure 8: Envien International – cash flow



FOCF: free operating cash flow
Source: Scope estimates

Figure 9: Envien International – cash flow cover

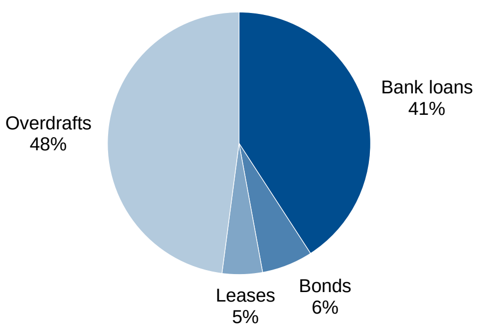


Source: Scope estimates

Investments in second-generation facilities would be credit negative

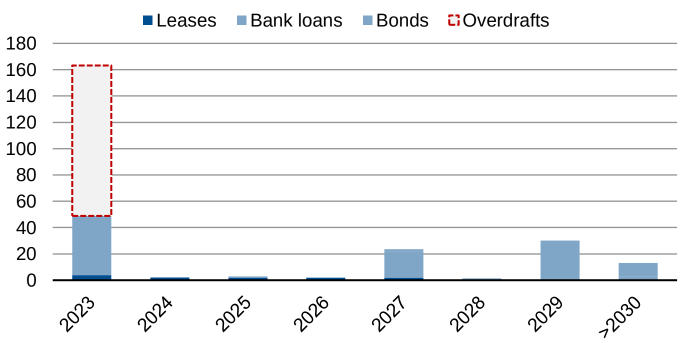
Management has not excluded the possibility of entering into large projects to build second-generation facilities in the coming years. Such projects usually require investment that runs into the hundreds of millions of euros, generally performed via a joint venture with a refinery. The investment would be funded partly by additional equity, but the significant expected increase in indebtedness could trigger a negative rating action. This event is not included in our base case scenario.

Figure 10: Envien International's gross debt split (Dec 2022)



Source: Envien, Scope

Figure 11: Envien International's debt maturity profile (EURm)



Source: Envien, Scope

Adequate liquidity

Liquidity is adequate, with short-term debt of EUR 163m primarily consisting of utilised overdraft lines of EUR 114m (covering around 50% of gross debt in 2022), half of which was kept as cash as of December 2022. In line with general practice in the country, Envien Group's has uncommitted short-term revolving overdraft lines with a handful of banks, with different maturities with each bank over the course of the year to reduce liquidity risk. Most of these lines have been in place for years (even decades) and primarily serve to finance inventory needs.

Internal liquidity coverage is greater than 100% over the next years even when applying very conservative recoverability assumptions on inventories, which in the case of Envien includes highly liquid raw and finished materials with a generally high expected recoverability ratio. Short-term bank loans maturing in 2023 are expected to be rolled over into 2024, while overdraft exposure should closely match working capital and is therefore expected to gradually decrease.

Balance in EUR '000s	2023 E	2024 E	2025 E
Unrestricted cash (t-1)	66,106	58,938	50,089
Inventory * 50% (t-1)	74,301	62,335	62,169
Open committed credit lines (t-1)	0	0	0
Free operating cash flow	23,332	27,651	30,749
Short-term debt (t-1)	163,617	139,617	139,617
Coverage	**100%**	**107%**	**110%**

Supplementary rating drivers: +/- 0 notches

Conservative financial policy

Envien Magyarország's financial policy is characterised by a minimal risk appetite. The company has no short-term debt and the issued bond is earmarked to repay an intercompany loan with the parent company. Dividend upstream to parent Envien International is not done automatically but only when financial results are sufficient.

Envien International does not explicitly commit to any credit metrics levels. Management has a record of being prudent since leverage has been kept within 2.5x over the past ten years, with a potential deviation expected in the short term due to market conditions. Moreover, we have not seen any major appetite for acquisitions in past years, except for Biopaliwa in 2022.

The company does not have a specific dividend policy. After several years of low dividends, high dividends were paid in the past two years (aggregate payout ratio in 2021/22 was above previous years' net profits) driven by unusually high EBITDA, but we expect Envien's management to reduce shareholder remuneration in the future in order to keep leverage below 3x.

Parent support

We have equalised the issuer rating of Envien Magyarország with that of 100% owner Envien International based on expected parent support. The company is privately owned by several individuals, none of which directly or indirectly controls Envien International with 25% or more shares and/or voting rights. Based on the applicable law, the members of the board of directors (R. Spisak, S. Toth, T. Jacobsen) are the ultimate beneficial owners.

Guaranteed bond rating

Envien Magyarország issued HUF 5.5bn in bonds in 2021

Envien Magyarország issued a HUF 5.5bn (EUR 15.7m) bond in May 2021 (ISIN HU0000360193), which was oversubscribed by 10% (company fully utilised the HUF 0.5bn overallotment provision). Envien International provided an unconditional and irrevocable guarantee for the issue. The bond has a 10-year tenor (due in 2031) and a fixed coupon of 2.5% per year (HUF 125,000 per year for the first five years, then decreasing according to scheduled amortisation). Amortisation will be 10% in 2026, 10% in 2027, 10% in 2028, 10% in 2029, 10% in 2030 and the remaining 50% in 2031. The guaranteed amount for the bond is HUF 6.1bn, representing the full value plus a contingency buffer.

We note that Envien Magyarország's bond – as per the Hungarian Central Bank's bond scheme - has an accelerated repayment clause in case of credit rating deterioration below B+ (2-year cure period to return to B+, but immediate repayment if rating falls below B-), which is currently deemed a remote occurrence for Envien's case.

Unconditional and irrevocable guarantee

Given the unconditional and irrevocable guarantee of the bond, we rate the guaranteed debt at the same level as the senior unsecured debt of guarantor Envien International.

Rating for guaranteed debt: BB

Based on a liquidation scenario at the level of Envien Group, we assess an average recovery for the senior unsecured bond. We therefore affirm the BB rating, which is in line with the issuer rating.

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