Greenergy Holding Vagyonkezelő Zrt
Hungary, Utilities

SCOPE

B+ POSITVE

Key metrics

			Scope estimates	
Scope credit ratios	**2020**	**2021**	**2022E**	**2023E**
Scope-adjusted EBITDA/interest cover	27x	26x	14x	14x
Scope-adjusted debt (SaD)/Scope-adjusted EBITDA[1]	2.2x	3.0x	2.3x	2.3x
Free operating cash flow/SaD	-35%	23%	-20%	12%
Liquidity	negative	>200%	>200%	>200%

Rating rationale

Greenergy's B+/Positive issuer rating is supported by its operation of small-scale, decentralised power generation assets across Hungary and our expectation of consistently improving financials throughout its ongoing expansion phase. The company strongly benefits from a positive pricing environment in power generation, particularly in the provision of balancing capacity to Hungary's national grid operator and its flexible pricing strategy that results in solid operating cash flow, improved leverage and robust interest coverage. The rating is however constrained by the company's very small scale and outreach, which are likely to change over the next few years with the envisaged expansion.

Outlook and rating-change drivers

The Positive Outlook reflects our expectation that Greenergy's leverage (SaD/Scope-adjusted EBITDA) can remain below 3.0x while interest coverage remains above 10x. The Outlook also incorporates a successful asset expansion within the growth areas of power generation and energy storage, which is consistently enhancing the company's size and outreach.

A positive rating action may be conducted if the company's leverage settled at below 3.0x for the next few years following the expected growth to a recurring EBITDA of over HUF 4.0bn. This can be the result of persistently high energy prices enabling the company to maintain the strong operating results of 2021 and expand the overall asset portfolio in power generation and storage.

A negative rating action such as a reversion of the Outlook to Stable could be required if Greenergy would not manage its growth trajectory on the EBITDA and Scope-adjusted leverage stayed above 3.0x. This could be the result of significantly lower earnings contributions from newly integrated power generation assets; a considerable deterioration of achievable energy prices for energy supply and balancing; or significant operational disruptions stemming from gas procurement issues. Given the material headroom of Greenergy's expected credit metrics to a lower rating and a solid liquidity profile, a rating downgrade is deemed remote.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
17 Jun 2022	Outlook change	B+/Positive
15 Jun 2021	New	B+/Stable

[1] No netting of cash for2021-2023E

Ratings & Outlook

Issuer	B+/Positive
Senior unsecured debt	BB

Analyst

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Related Methodologies and Research

Corporate Rating Methodology; July 2021

European Utilities Rating Methodology; March 2022

ESG considerations for the credit ratings of utilities; April 2021

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Bloomberg: RESP SCOP

Positive rating drivers	Negative rating drivers
• Power generation portfolio comprising decentralised small-scale energy generation units (heat and electricity) with sufficient granularity and significant growth trajectory related to the ramp-up of generation capacity and storage with limited execution risk • Robust business exposure to quasi-monopolistic heat generation and supply to district heating networks and reputable industrial/commercial customers under multi-year contracts • Cash flow enhancement through the company's virtual power plant and its ability to provide reserve capacity to Hungarian transmission grid operator MAVIR, including volatile renewables and peak-load eligible gas-fired power plants (ESG factor: credit-positive environmental factor) • Recurring EBITDA margin in an expected range of 15-25% which is forecasted to remain at the upper end of the range for the next few years in the context of good tailwinds from energy prices for the company's power generation • Strengthened financial risk profile bolstered by strongly improved operating cash flow, leading to forecasted Scope-adjusted leverage of below 3.0x, solid debt protection and limited concerns on liquidity • Operation & Maintenance and EPC exposure for own and third-party generation assets	• Very limited size, scale and outreach even when doubling energy generation capacity over the next few years • Material dependency on achievable power prices for outright electricity production (which are fairly volatile on the Hungarian power exchanges OTC/HUPX) and significant dependence of achievable EBITDA margin on non-controllable price related to gas procurement • Material potential exposure to adverse foreign exchange developments • Business exposure entirely linked to core market Hungary for the near future • Rating adjustment for peer group comparison

Positive rating-change drivers	Negative rating-change drivers
• Upgrade: our expectations of leverage settling below 3.0x materialise alongside an increased recurring EBITDA of over HUF 4.0bn (~EUR 10bn)	• Outlook back to Stable: Expectations about leverage do not materialise and leverage stays at above 3.0x • Downgrade: deemed unlikely over the next 12-18 months

Corporate profile

Greenergy Holding Vagyonkezelő Zrt (Greenergy) is a small Hungarian utility. It operates about two dozen small-scale power plants with a total combined capacity of about 50 MW, primarily CHP (combined heat and power) plants, across Hungary. The company's business model is supplemented by O&M (operation and maintenance) services for its own and third-party power plants, energy services and energy trading.

Greenergy's is directly owned by Hungarian construction company KÉSZ Group (51%) and its two Directors Mr Dósai and Mr Dajbukát (24.5% each). We consider the rated entity as steered largely independently from its majority shareholder.

Financial overview

				Scope estimates		
Scope credit ratios	**2019**	**2020**	**2021**	**2022E**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover	11x	27x	26x	14x	14x	11x
SaD/Scope-adjusted EBITDA (netting of cash)	2.4x	2.2x	3.0x	2.3x	2.3x	2.2x
SaD/Scope-adjusted EBITDA (no netting of cash)	2.8x	2.4x	3.0x	2.3x	2.3x	2.7x
Free operating cash flow/SaD	32%	-35%	23%	-20%	12%	29%
Liquidity (internal and external)	67%	negative	>200%	>200%	>200%	>200%
Scope-adjusted EBITDA in HUF m						
Reported EBITDA	13,867	1,106	2,789	4,150	4,363	3,240
One-offs[2]	-13,172	0	0	0	0	0
Other adjustments[3]	232	-136	64	-124	-112	-101
Scope-adjusted EBITDA	**928**	**970**	**2,853**	**4,026**	**4,251**	**3,140**
Free operating cash flow in HUF m						
Operating cash flow	806	35	2,546	1,781	2,769	2,365
less: capital expenditure (net)	-114	-760	-595	-3,596	-1,614	-360
Free operating cash flow	**692**	**-725**	**1,951**	**-1,816**	**1,155**	**2,005**
Net cash interest paid in HUF m						
Cash interest paid per cash flow statement	99	36	112	280	301	295
Cash interest received per cash flow statement	-12	-1	-1	-	-	-
Net cash interest paid	**88**	**36**	**111**	**280**	**301**	**295**
Scope-adjusted debt in HUF m						
Reported gross financial debt	1,580	1,616	7,737	8,252	8,920	7,923
less: cash and cash equivalents	-358	-282	-7,683	-2,292	-1,590	-1,174
add: non-accessible cash (earmarked for investments)	-	-	7,683	2,292	1,590	-
add: contingent liabilities (75% of provisions for asset overhauls)	974	755	933	839	756	680
Scope-adjusted debt	**2,196**	**2,088**	**8,670**	**9,091**	**9,676**	**7,430**

[2] Debt restructuring of an unused development loan in 2019
[3] Adjustments for profit/loss on derecognising fixed assets, net changes in provisions, non-cash revenue

Table of Content

Environmental, social and governance (ESG) profile[4]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	
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)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend

Green leaf (ESG factor: credit positive)

Red leaf (ESG factor: credit negative)

Grey leaf (ESG factor: credit neutral)

CHP capacity and virtual power plant enhances Greenergy's market position and cash flow

Our assessment of a credit-positive environmental credit risk driver relates to Greenergy's combined operations of robust CHP facilities and volatile renewable energy power plants that are operated individually but also as a combined virtual power plant through the company's own power plant control centre. The virtual power plant is a technical and commercial solution that allows multiple small standalone power plants to enter the electricity and system services market as a single, large power plant, thereby implementing very effective, flexible and economical energy production technology. Greenergy is able to cover both base and peak demand (particularly important in Hungary as the market is chronically short of generation capacity), which supports its market position, cash flow profile and credit quality.

Credit-neutral regulatory and governance risk

Regulatory risks are credit neutral. The company is not exposed to electricity supply for residential customers for which prices are legally capped in the interest of energy affordability. Moreover, the company's overall cash flow is not significantly exposed to regulated income from renewable energy generation capacities, which could be affected by adverse regulation. Governance factors are not expected to negatively affect Greenergy's creditworthiness.

[4] 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-

Business risk profile supported by solid business proposition related to CHP

The issuer rating primarily reflects Greenergy's solid cash flow in the context of the company's size and its changing financial risk profile amid its current strategic investment phase. While small, with a generation capacity of only about 45 MW, primarily related to gas-based CHP assets, Greenergy's cash flow and credit quality are supported by its solid position in electricity and power generation. Heat generation and supply provide stable cash flow, bolstered by local oligopolistic or even monopolistic positions, a robust and flexible tariff setting framework and medium- to long-term contracts with industrial/commercial off-takers or municipal off-takers for district heating.

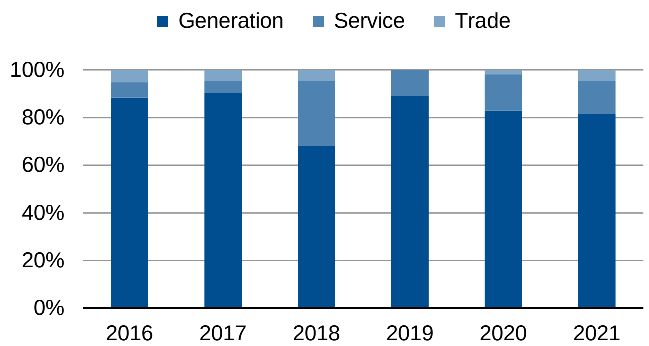
Industry-inherent volatility of largely unregulated power generation

In contrast, Greenergy's exposure to electricity generation and supply, which provides about 50% of the company's revenue, is subject to industry-inherent volatility related to merchant risks. Such potential earnings volatility can only be partly offset by Greenergy's ability to provide balancing capacity to Hungary's transmission grid operator MAVIR via its virtual power plant. Consequently, the company's power generation fleet with a peak- and baseload-capable decentralised CHP portfolio, enhanced by renewable energy capacities, is a positive environmental ESG rating driver that supports the stability and diversity of Greenergy's business model and limits regulatory risk.

Limited scale as key rating constraint

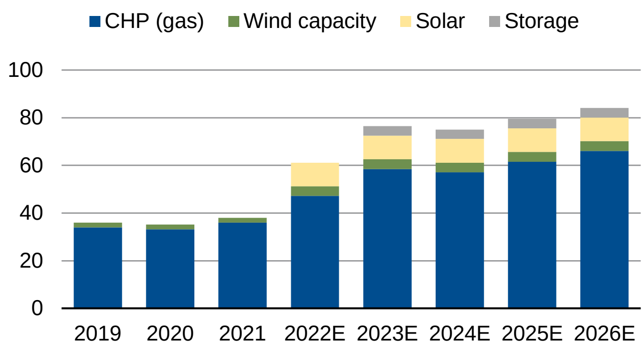
Greenergy's rating is held back to some extent by its limited scale and regional risk mitigation. Although we expect a steep growth trajectory, with a doubling of generation capacity in CHP and unregulated renewables, supplemented by additional growth in energy storage and energy services, the company will remain small in terms of cash flow. We judge execution risks related to the capacity ramp-up and envisioned strengthening of the business services segment to be low. The integration of new greenfield and brownfield power plants should not be overly challenging, given the company's long-standing expertise in operating small-scale, decentralised CHP plants. Similarly, we do not expect the integration of selective brownfield wind or solar parks to raise major concerns.

Figure 1: Revenue split across segments



Sources: Greenergy, Scope

Figure 2: Envisioned portfolio ramp-up (MW)



Sources: Greenergy, Scope

Achievable margins and cash flow support the rating

The company's solid cash flow is evidenced by its sound recurring EBITDA margin, which we expect to settle between 20% to 25% over the next few years. The margin is largely supported by the higher-margin generation business and somewhat diluted by the services and trading business.

We expect Greenergy group's EBITDA margin to be above 20% in the foreseeable future, bolstered by:

i) Persistently high energy prices (wholesale and balancing)

ii) A larger share of higher-margin power generation activities, expected to counterbalance the growing absolute exposure to business services and the thin margin in the power supply segment

iii) Low likelihood of generating operating losses in energy supply due to the flexible pricing model that does not contain hedging positions, and which ensures timely price adjustments for varying procurement costs.

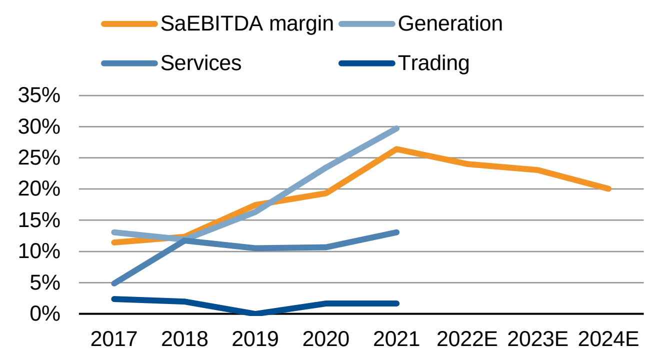
As we expect the pricing environment for power generation (particularly balancing) to ease at some point, group margin is forecasted to revert back to about 20% by 2024.

Industry-induced margin volatility cannot be ruled out

Greenergy displays some business-model inherent margin volatility related to raw material procurement. While price developments in gas procurement can regularly be passed on to the customers through annual tariff updates, achievable prices for electricity sales, which are set at the exchanges, can hardly be influenced. The same applies to prices for balancing fees that prove to be more volatile amid the ongoing energy transition in Hungary.

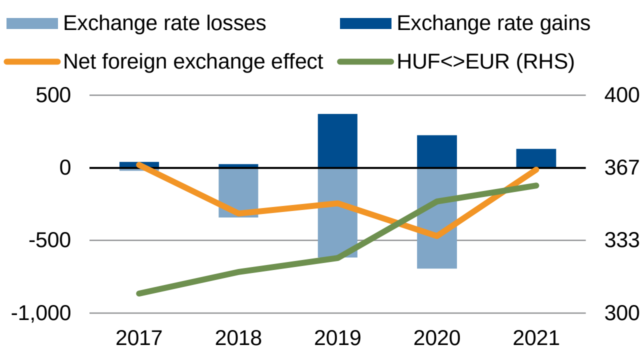
In addition, material cash flow risk arises from potential adverse forex effects and a non-controllable pricing environment for gas procurement.

Figure 3: Scope-adjusted EBITDA and segment margin



Sources: Greenergy, Scope estimates

Figure 4: Significant net foreign exchange losses following persistent HUF depreciation (HUF m)



Sources: Greenergy, ECB, Scope

Gas flow disruptions not in our base case scenario

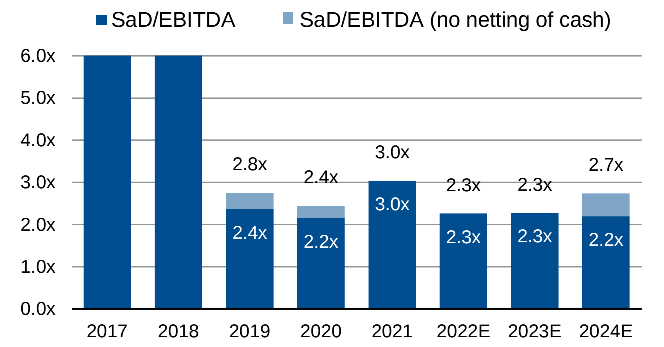
Whilst Greenergy's power generation and supply depend on steady gas flow and sufficient gas storage in Hungary (more than 80% of Hungarian gas supplies come from Russia), we believe that Greenergy's position would be partially protected should Russian gas flows come to a halt. These event risks do not determine our base case given the close ties between Hungary and Russia. Greenergy's exposure to district heating (more than 60% of combined heat and power plants are contracted for municipal district heating or providing energy to hospitals) and grid balancing would put them in a favourable position should gas flows be rationed.

Financial risk profile: BB+

Consistently improved financial profile reflected in Positive rating Outlook

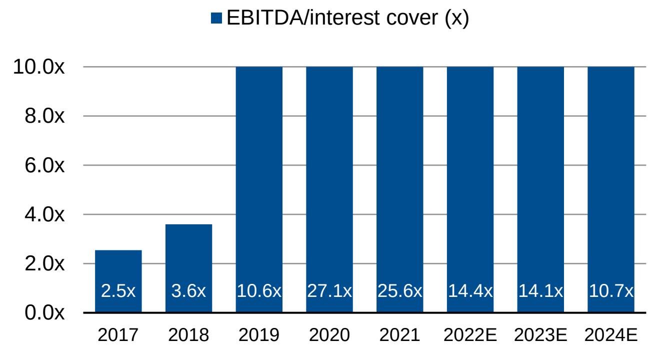
Greenergy's credit quality is supported by its operational performance in 2021, which we expect will remain as solid over the next two years. The company's overall size and outreach are expected to improve gradually through organic and dynamic investment in its focus segments power generation (combined heat and power and renewables) and storage. Greenergy's solid operating cash flow is strongly supported by macro-economic tailwinds from high energy prices for electricity and heat generation and balancing services for grid stabilisation. As we believe that the pricing situation in Hungary will persist into 2023, Greenergy's financial risk profile is expected to strengthen over the next few years, much beyond our initial rating case. We assume that the company will retain a large portion of operating cash flow, limiting external financing needs for its assumed HUF 10bn-11bn investment programme and contributing to Scope-adjusted leverage improving to below 3.0x (SaD/Scope-adjusted EBITDA) and EBITDA interest coverage to above 10x for the next few years (even if new debt is raised at a much higher interest rate than the current average interest rate of about 3.0%). Such improvements are reflected in the Positive rating Outlook that could give way to a higher rating should our expectations about sustainedly improved financials materialise over the next year.

Figure 5: Expected development of Scope-adjusted leverage



Source: Greenergy, Scope estimates

Figure 6: Expected development of EBITDA interest coverage

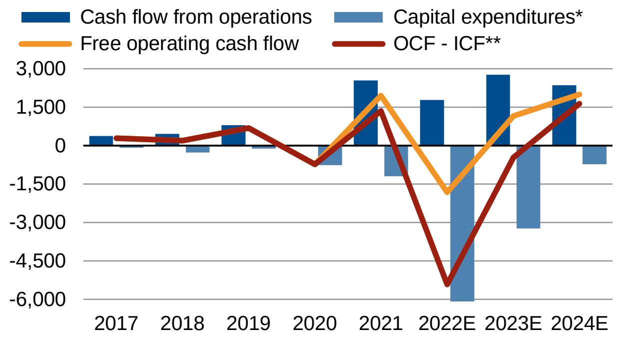


Source: Greenergy, Scope estimates

Solid expected operating cash flow limiting external funding for dynamic investment phase

The company has reacted to the exceptionally strong earnings growth through i) scaling back its shareholder loan exposure; ii) stepping up its investment programme; and iii) starting dividend payouts in 2022. Retained earnings are expected to support the financial risk profile. We believe that the company will balance higher capex and shareholder remuneration against operating cash flow to keep leverage moderate. The stepped-up investment programme of about HUF 10bn-11bn will likely be concluded by YE 2023 with most investments conducted in 2022. Execution risks are limited for greenfield projects such as new solar farms and battery storage capacity and for the integration of brownfield projects (acquired wind farms, additional cogeneration capacity or acquired ventures such as INT-NRG Zrt) given the company's long experience in most of these activities.

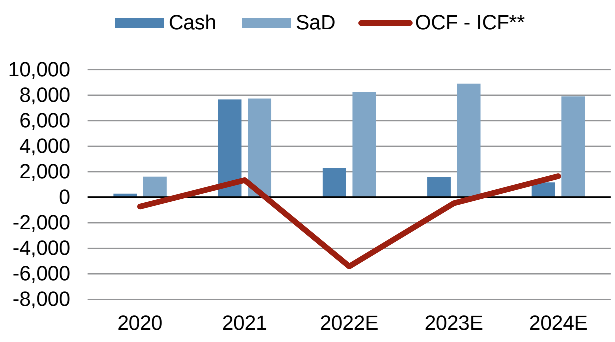
Figure 7: Investment phase buffered by stronger-than-expected operating cash flow (in HUF m) …



* For organic and dynamic growth
** Operating cash flow minus investing cash flow

Source: Greenergy, Scope estimates

Figure 8: … not overly burdening expected debt levels (HUF m)

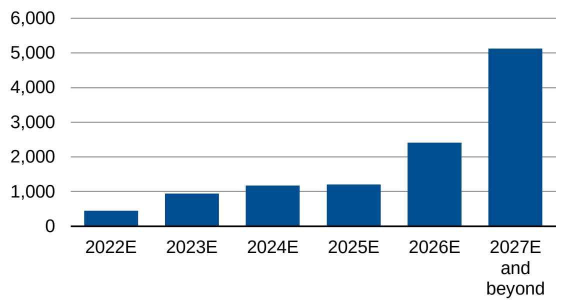


Source: Greenergy, Scope estimates

Adequate liquidity

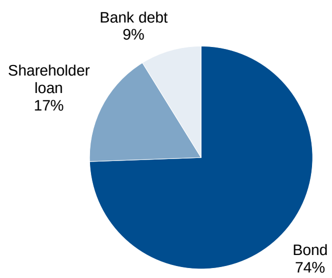
Following the deconsolidation of its amortising shareholder loan from Paratus Energy Kft, scheduled debt repayments over the next few years are primarily related to bank loans of around HUF 500m-1bn per year. These volumes together with forecasted capex are expected to be solidly covered by available cash sources such as operating cash flow and a significant cash buffer (HUF 7.7bn at YE 2021).

Figure 9: Expected maturity schedule (HUF m)



Sources: Greenergy, Scope expectations

Figure 10: Funding structure at YE 2021



Sources: Greenergy, Scope

Adequate access to funding, considering small corporate size

Despite its comparatively small size, Greenergy has sufficient and reliable access to external financing though established relationships with Hungarian banks such as MKB and CIB. We believe that an increased refinancing volume starting in 2026 – when bond amortisation of about HUF 580m will come on top of annual refinancing needs of bank loans – can be covered by Greenergy's operating business. Greenergy will also likely develop fallback opportunities for refinancing with new debt issuances backed by its business model and a largely unencumbered asset base.

Balance in HUF m	2021	2022E	2023E
Unrestricted cash (t-1)	282	7,683	2,292
Open committed credit lines (t-1)	1,260	-	-
Free operating cash flow (t)	1,951	-1,816	1,155
Short-term debt (t-1)	-	267	945
Coverage	**>200%**	**>200%**	**>200%**

Sources: Greenergy, Scope estimates

Supplementary rating drivers: -1 notch

Rating cap at B rating category

The rating continues to reflect a negative adjustment of one notch related to the company's limited size and outreach compared to other entities in the BB rating category. While the company's outreach has increased significantly, as displayed by a doubling of revenue and an increase of its EBITDA by 2.5x from 2020 to 2021, this has been largely due to external factors such as rising energy prices. Due to expected improvements in the financial risk profile, a BB category rating is now in reach if the company can achieve a recurring EBITDA of at least HUF 4.0bn.

Credit-neutral financial policy

Greenergy's financial policy is considered neutral for the rating, neither materially weakening nor strongly supporting the company's financial risk profile.

- The company's strategy shows a strong growth trajectory that is likely be executed through acquisitions of single project companies with operating power generation assets. This is largely covered by cash and expected operating cash flow. Moreover, the M&A strategy bears limited execution/integration risks due to the nature of the acquisition targets and Greenergy's expertise in operating such assets.
- Following the strong operating performance but also the strong reduction of Greenergy's exposure to shareholder loans in early 2022, the company is expected to start dividend payouts. This is a substitution for the interest on shareholder loans that have been paid over the years. While the expected dividend payouts are well above the level of historical interest on shareholder loans, they are not overly detrimental to Greenergy's financial profile given the company's strongly improved financials and the total amount of dividends within a range of 40%-60% of the previous year's net income.

Long-term debt rating

Senior unsecured debt rating at BB

The BB rating for senior unsecured debt issued by Greenergy reflects a two-notches rating uplift against the issuer rating that mirrors our expectations of a robustly superior recovery for senior unsecured debt, even once potential senior secured debt and payables have been fully covered by expected liquidation proceeds. Our recovery expectations are based on a liquidation value in a hypothetical default scenario of around HUF 11.5bn after administrative claims. The recovery expectations incorporate sufficiently high discount rates on the book value of recoverable assets.

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