WEDNESDAY, 25/01/2023 - Scope Ratings GmbH

Scope affirms Sun Group Kft's B+/Stable issuer rating

The updated corporate strategy and financial policy are in line with the current rating levels.

The latest information on the rating, including rating reports and related methodologies, is available on this **LINK**.

Rating action

Scope Ratings GmbH (Scope) has today affirmed the B+/Stable issuer rating on Hungarian HR services and real estate company Sun Group Kft. The rating for the senior unsecured long-term debt was also affirmed at B+.

Rating rationale

The affirmation reflects the credit neutral impact of the updated corporate strategy and financial policy.

The issuer rating mainly reflects Sun Group's leading position in Hungarian HR services via the majority ownership in Prohumán 2004 Kft. acquired in 2022, followed by small bolt-on acquisitions in the CEE region coupled with changes in the internal group structure and a shareholder-friendly financial policy.

In addition to regular dividends, the amended financial policy includes an updated mechanism for early payment of purchase price and dividend liabilities towards minority investors totaling HUF 2.55bn in period 2023-25. These cash outflows have limited impact (at most +0.2x) on leverage measured by Scope-adjusted debt/EBITDA as Scope previously deemed the cash to not be permanent and hence limited cash netting was applied. Nevertheless, these actions sustain the agency's negative assessment of financial policy.

The updated corporate strategy entails transforming Sun Group Kft. into a pure holding company. As a result, approximately 60% of the 80.22% quota holdings in Prohumán will be transferred to a newly established subsidiary of Sun Group. The ownership and control of Sun Group over Prohumán does not change, however the cash flow of Prohumán used for the debt service of the Sun Group bond will be more remote by going through a newly established, wholly owned and consolidated entity. This is mitigated by providing a corporate guarantee for the bonds of the new intragroup entity, besides the existing corporate guarantee of Prohumán, which allows the possibility of channeling cash for debt service two levels within the same year. These changes are subject to approval of all bondholders, just like future changes to the ownership structure of Sun Group or Prohumán as guarantor, as regulated by the bond prospectus.

Furthermore, Sun Group's real estate portfolio is planned to be transferred to a second wholly owned and consolidated limited liability company incorporated in Hungary and Prohumán will be converted from a limited liability company into a private company limited by shares in preparation for a possible IPO. As all these changes are within the consolidated entity group and there is no change to group assets or group ownership, Scope considers them credit neutral.

Sun Group's business risk profile (rated B+) and financial risk profile (rated BB) are not affected by these changes. This is because the bolt-on acquisitions are focusing on small market participants with medium-term development potential, while the updated corporate strategy and financial policy still lead to Scope-adjusted debt/EBITDA between 3-4x (with limited cash netting), which is in line with the current rating levels.

Sun Group's liquidity is adequate, mainly driven by historically good cash flow and the repayment profile of the issued bond, allowing amortisation from year five and a 50% balloon payment at maturity. Liquidity could still deteriorate, for example, in the event of sharp working capital swings due to delayed customer payments, which could be partially mitigated by factoring receivables.

For supplementary rating drivers, Scope has still taken one notch off the issuer rating. This is due to limited transparency and loose financial planning due to ongoing group consolidation scheduled to be completed in 2023 and dividend leakage while cash is up streamed to the holding for debt service. (ESG factor: credit negative).

One or more key drivers of the credit rating action are considered an ESG factor.

Outlook and rating-change drivers

The Outlook is Stable and assumes the further development of HR services, resulting in a Scope-adjusted debt/EBITDA ratio between 3-4x taking into consideration annual revenue growth around 10%, low capex, small acquisitions and moderate shareholder remuneration.

A positive rating action could be warranted if Sun Group's financial policy becomes more creditor friendly and IFRS consolidation is executed or the issuer improved its diversification in the HR business by services or geographies, including achieving a top-three market share in its countries of operation, with Scope-adjusted debt/EBITDA not exceeding 3x.

A negative rating action could be triggered by macroeconomic disruptions resulting in a significant drop in demand for temporary staff followed by a deterioration in credit metrics, e.g. if Scope-adjusted debt/EBITDA increased and stayed above 4x, or liquidity weakened due to strong working capital fluctuations or increased shareholder remuneration. Credit metrics could also deteriorate in the case of another large debt-funded acquisition.

Scope notes that Sun Group Kft.'s senior unsecured bonds issued under the Hungarian Central Bank's bond scheme has several accelerated repayment clauses. The clauses require the issuer to repay the nominal amount (HUF 15.4bn) in case of rating deterioration (2-year cure period for B/B- ratings, immediate repayment below B-), breach of net debt/EBITDA ratio (max. 3x in 2023) or change of control (even partial) at the issuer level (Sun Group) or the guarantor level (Prohumán).

Long-term debt ratings

Scope expects an 'average' recovery for senior unsecured long-term debt including the HUF 15.4bn bond maturing in 2032. The recovery is based on an expected distressed enterprise value as a going concern in a hypothetical default scenario at YE 2024. This is based on the asset-light nature of HR services and the debt’s ranking behind the senior secured creditors of Sun Group’s real estate and the working capital and factoring creditors of Prohumán.

The recovery expectation translates into the same rating as the issuer rating, resulting in a B+ senior unsecured long-term debt rating.

Stress testing & cash flow analysis

No stress testing was performed. Scope Ratings performed its standard cash flow forecasting for the company.

Methodology

The methodology used for these Credit Ratings and/or Outlook, (General Corporate Rating Methodology, 15 July 2022), is available on https://scoperatings.com/governance-and-policies/rating-governance/methodologies.
Information on the meaning of each Credit Rating category, including definitions of default, recoveries, Outlooks and Under Review, can be viewed in ‘Rating Definitions – Credit Ratings, Ancillary and Other Services’, published on https://www.scoperatings.com/governance-and-policies/rating-governance/definitions-and-scales. Historical default rates of the entities rated by Scope Ratings can be viewed in the Credit Rating performance report at https://scoperatings.com/governance-and-policies/regulatory/eu-regulation. Also refer to the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope Ratings’ definitions of default and Credit Rating notations can be found at https://www.scoperatings.com/governance-and-policies/rating-governance/definitions-and-scales. Guidance and information on how environmental, social or governance factors (ESG factors) are incorporated into the Credit Rating can be found in the respective sections of the methodologies or guidance documents provided on https://scoperatings.com/governance-and-policies/rating-governance/methodologies.
The Outlook indicates the most likely direction of the Credit Ratings if the Credit Ratings were to change within the next 12 to 18 months.

Solicitation, key sources and quality of information

The Rated Entity and/or its Related Third Parties participated in the Credit Rating process.
The following substantially material sources of information were used to prepare the Credit Ratings: the Rated Entity, the Rated Entities' Related Third Parties and Scope Ratings' internal sources.
Scope Ratings considers the quality of information available to Scope Ratings on the Rated Entity or instrument to be satisfactory. The information and data supporting the Credit Ratings originate from sources Scope Ratings considers to be reliable and accurate. Scope Ratings does not, however, independently verify the reliability and accuracy of the information and data.
Prior to the issuance of the Credit Rating action, the Rated Entity was given the opportunity to review the Credit Ratings and/or Outlook and the principal grounds on which the Credit Ratings and/or Outlook are based. Following that review, the Credit Ratings were not amended before being issued.

Regulatory disclosures

These Credit Ratings and/or Outlook are issued by Scope Ratings GmbH, Lennéstraße 5, D-10785 Berlin, Tel +49 30 27891-0. The Credit Ratings and/or Outlook are UK-endorsed.
Lead analyst: Barna Szabolcs Gáspár, Director
Person responsible for approval of the Credit Ratings: Philipp Wass, Executive Director
The Credit Ratings/Outlook were first released by Scope Ratings on 21 December 2021. The Credit Ratings/Outlook were last updated on 14 December 2022.

Potential conflicts

See www.scoperatings.com under Governance & Policies/EU Regulation/Disclosures for a list of potential conflicts of interest related to the issuance of Credit Ratings.

Scope Ratings provided the following Other Services to the Rated Entity and/or its Related Third Parties within the two years preceding this Credit Rating action: Rating Assessment Service.

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CONTACT INFO

Barna Szabolcs Gáspár

Analyst

b.gaspar@scoperatings.com

Olaf Tölke

Team leader

o.toelke@scoperatings.com

Press contact

press@scopegroup.com

ISSUERS 1

INSTRUMENTS 1