

Scope Hamburg affirms KÉSZ Group's BB issuer credit rating; outlook stable

KÉSZ Holding Zrt.		26 October 2021	BB
		Issuer rating	
		Outlook	stable
Industry	Construction		

Rationale

Scope Hamburg has affirmed the BB issuer credit rating of KÉSZ Holding Zrt. taking into account the upcoming second bond issue (HUF 10bn) in 2021. The underlying factors remain slightly increased business risks, moderate financial risks and no further modifications. The rating outlook remains unchanged at stable.

Our assessment on the company's business risk profile remains unchanged at "slightly increased". The factors weighing on our assessment include the inherent exposure to the cyclical and competitive construction industry in Hungary and higher-risk CEE countries. Despite concerns about capacity constraints (e.g. labour, materials), which keeps the sector's profit margins tight in our view, we expect an upturn in construction activity for 2021/22 mainly fuelled by state incentives (VAT cuts, public procurement, subsidy schemes) and catch-up effects. Factors supporting our business risk assessment include KÉSZ' long-established and strong market position, a long track-record of stable project executions and KÉSZ' grown business model with a high potential for further expansion. KÉSZ' market position remains underpinned by a reputable project portfolio and international presence in the CEE region. Furthermore, we think that KÉSZ's long-pursued vertical integration strategy provides barriers to entry and creates strategic benefits for the access to raw materials, new markets and more profitable and complex tenders.

Our assessment on the company's financial risk profile remains unchanged at "moderate". As a key strength we value the track record of largely stable gross margins which indicates generally good project execution and cost management skills as well as a relatively flexible cost base and adaptable operations to us. Apart from positive one-off gains from the 2021 divestment of a long-term PPP project, we expect a strong operating result for 2021 since the reported half year result on ordinary business activities showed a remarkable uplift (YoY). Overall, we are confident that KÉSZ Group is capable of achieving its medium-term targets based on a fairly solid contracted backlog (2021: 98%; 2022: 67%), providing good visibility, while the current market outlook is fairly supportive in our view despite a lack of labour and building materials among most European contractors. The actual operating margins (EBITDA 5% to 7%), however, will stay slightly below average over the near-term in our opinion, due to market-wide high operating costs and highly competitive tenders. Another key financial strength for us is KÉSZ' solid capital structure, which is subject to moderately strong credit metrics such as a still moderate analytical equity ratio, a history of fairly stable current- and turnover ratios and a still relatively modest exposure to (long-term) financial debt, which will keep the expected EBITDA interest coverage sustainably above 8x (2017-20: 11.0x) post issuance of the upcoming second bond issue (HUF 10bn). KÉSZ' current financial flexibility rests on strong cash sources, unutilised over-draft/guarantee facilities and a good standing in credit markets, demonstrated by solid relationships with banks, prudent financial policies and a high investor appetite for the 2021/31 corporate bond issues. **The stable outlook** reflects our view that the group is able to maintain a moderate financial risk profile post issuance.

Our assessments on operational risks and external influences remain unchanged with no further modification to the issuer credit rating (BB / stable).

Company

KÉSZ Group (KÉSZ) is one of the largest construction companies in Hungary whose story started as a family business in 1982. Today, KÉSZ Group's two main divisions are KÉSZ Engineering & Technologies (KÉSZ ET; 90% of revenues), which includes the entire construction business of the group and KÉSZ Business Solutions (KÉSZ BS; 10% of revenues). The latter compiles all the economic services that support the operation of the group's own assets on the one hand, and, on the other hand, offers property management, business and commercial services. As an independent Hungarian group of companies KÉSZ aims to become one of the leading construction companies in the CEE region through equity investments and project developments in domestic and international markets. As the domestic leader in building constructions KÉSZ has built numerous prominent industrial facilities, office buildings, shopping and logistic centres, sports venues or hotels and housing facilities. As of today, KÉSZ has implemented more than 3,100 projects and has 5 million m2 references in more than 12 countries. The group employs more than 1,500 people and reported revenues of HUF 117.2bn for 2020 (2019: HUF 97.2bn). For 2021 and the years ahead KÉSZ Group expects annual revenues to grow to a level of around HUF 170bn based on an already contracted backlog of 98% for 2021 and 67% for 2022.

Upgrade / Downgrade Factors

Factors that could lead to an Upgrade

- Sustainable and lasting increase of the group's profit margins reflecting an improved competitive position or corporate growth through further diversification (e.g. EBITDA ratio > 8.0%)
- Substantial and lasting improvement of the group's capital structure and debt coverage potential (e.g. Scope Hamburg's adjusted EBIT interest coverage > 9.0)

Factors that could lead to a Downgrade

- Persistent market stress or deterioration of the group's competitive position combined with an adverse impact on the group's cash or working capital position (e.g. EBITDA ratio < 5.0%)
- Substantial and lasting deterioration of the group's capital structure and debt coverage potential (e.g. Scope Hamburg's adjusted EBIT interest coverage < 3.0)

Rating History



Appendix 1: Execution

Analysts	Rating committee (Chairperson)
<ul style="list-style-type: none">Matthias Peetz, Lead analyst	<ul style="list-style-type: none">Dörte Mähmann
Contact: Tel.: +49 (0) 40/60 77 81 200 info@scopehamburg.com	

Rating, Solicitation, Principal Sources of Information
<ul style="list-style-type: none">This credit rating has been issued in accordance with the CRA Regulation.<ul style="list-style-type: none"><input checked="" type="checkbox"/> Solicited Rating<input type="checkbox"/> Unsolicited Rating<ul style="list-style-type: none"><input type="checkbox"/> No participation of the rated entity or related third party<input type="checkbox"/> With participation of the rated entity or related third party<ul style="list-style-type: none"><input type="checkbox"/> Access to internal documents<input type="checkbox"/> Access to managementPrior to its publication the rating was disclosed to the rated entity. During this period, the rated entity had the opportunity to review the rating and to verify the underlying assumptions. Following this review, the rating was not amended.Principal sources of information:<ul style="list-style-type: none">- Consolidated financial statements 2018–2020 / Half Year 2021- Business plan provided by the issuer- Management interviews

Rating methodologies and definitions
<ul style="list-style-type: none">Methodology: Issuer Rating as of May 2016Basic Principles for Assigning Credit Ratings and Other Services as of October 2021Guidance Regarding the Consideration of ESG Factors in Scope Hamburg Credit Ratings as of March 2020 <p>Scope Ratings GmbH and Scope Ratings UK Limited apply the same methodologies/models and key rating assumptions for their credit rating services, while Scope Hamburg GmbH's methodologies/models and key rating assumptions are different from those of Scope Ratings GmbH and Scope Ratings UK Limited.</p>

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Appendix 2: Rating categories*

Category	Explanation
AAA	In the opinion of Scope Hamburg, AAA rated entities demonstrate an excellent credit quality and the lowest default risk.
AA	In the opinion of Scope Hamburg, AA rated entities demonstrate a very high credit quality with a very low default risk.
A	In the opinion of Scope Hamburg, A rated entities demonstrate a high credit quality with a low default risk.
BBB	In the opinion of Scope Hamburg, BBB rated entities demonstrate a medium credit quality with a moderate default risk.
BB	In the opinion of Scope Hamburg, BB rated entities demonstrate a medium-low credit quality with a slightly increased default risk.
B	In the opinion of Scope Hamburg, B rated entities demonstrate a low credit quality with an increased default risk.
CCC	In the opinion of Scope Hamburg, CCC rated entities demonstrate a very low credit quality with a high default risk.
CC	In the opinion of Scope Hamburg, CC rated entities demonstrate a very low credit quality, an event of default is very likely.
C	In the opinion of Scope Hamburg, C rated entities demonstrate a very low credit quality, an event of default is imminent.
D / SD	D rated entities have defaulted, as defined by the rating agency. The rated entity is assigned an SD rating (Selective Default) if it has only defaulted on certain debt obligations.
PLUS (+) MINUS (-)	Rating categories from AA to CCC are modified by a PLUS (+) or MINUS (-), where required, in order to show their relative position within the rating category.

* For more explanations and definitions please refer to:

[Basic Principles for Assigning Credit Ratings and Other Services as of October 2021](#)

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Hamburg, 26 October 2021