



Fitch Revises Net Holding's Outlook to Negative; Affirms and Withdraws Rating

Fitch Ratings - Madrid - 25 November 2019:

Fitch Ratings has revised the Outlook on Net Holding A.S.'s Long-Term Issuer Default Rating (IDR) to Negative from Stable and affirmed the IDR at 'B'. Fitch has subsequently withdrawn the rating.

The revision of the Outlook reflects the fact that the company underperformed Fitch's expectation over the last 15 months. This is mainly due to the impact on revenues of a small number of players recording large gains, a sign of vulnerability of the revenue stream leading to cash flow volatility. This high concentration of customer base, has ultimately driven lower funds from operations (FFO) and increased leverage metrics above our expectations and negative rating sensitivity for the next 12 to 18 months.

We expect the company to improve profitability as international business develops and matures, thanks to a development strategy implemented by an experienced management team. This should enable it to deleverage below its sensitivity level in line with its rating within two years, supporting the affirmation of the rating at 'B'. The headroom has materially reduced though.

The ratings were withdrawn with the following reason: Commercial Purposes

Key Rating Drivers

High Customer Concentration: Net Holding had a severe decline of revenues in Northern Cyprus in 2H18 due to the wins achieved by small groups in their main casino, and similar issues in Montenegro in 1H19, although of more limited amounts. Fitch believes these were the result of a still high customer concentration despite the growing number of players and the internationalisation, showing the company remains vulnerable to such events. This led Net Holding to underperform compared with previous years and Fitch's expectations.

Higher Than Expected Leverage: The underperformance during the past 15 months, as well as a delay in its expansion plan, have led to higher leverage and slower deleveraging than previously expected. Growth plans in Northern Cyprus and the Balkans, as well as a positive impact from new projects in Albania and Macedonia, have now been delayed by one year. We expect the company to remain above our negative leverage sensitivity over the next 12 to 18 months. The company has not made any public statement on deleveraging commitment.

International Expansion Delayed: Net Holding's geographical expansion has suffered some setbacks in the last 15 months. In some countries such as Croatia and Montenegro, revenues and EBITDA are still far from what was initially planned, while other projects such as Albania and

Macedonia have been delayed and are expected to be operational by 2020 instead of 2019 initially planned. This has increased the company's geographic concentration. Importantly, these projects do not involve high cash outflows and capex is capped at USD5 million for new projects.

No Material Impact from FX Exposure: Customers continue to pay in hard currencies, driving sound revenue growth and some profitability improvements given that the group's cost base is predominantly in Turkish lira. This is neutral for leverage as it is offset by debt growth, which is predominantly foreign-currency based. Further Turkish lira depreciation could impact revenue from Turkish players.

Volatile Cash Flow Generation: The group's free cash flow (FCF) generation is constrained by the capex plan carried on a major development in Northern Cyprus over the next two years. We forecast FCF would improve in FY21, assuming no further unexpected large-scale investments. FCF in FY19 is also expected to be positive thanks to a working capital inflow.

Derivation Summary

Net Holding's 'B' rating reflects a weaker credit profile than larger casino operators such as Las Vegas Sands Corp (BBB-/Positive) and MGM Resort International (BB/Stable), which benefit from stronger financial profiles with much larger scale and high-quality assets in more attractive markets, as well as from greater geographical diversification of operations.

Net Holding is smaller and displays higher FFO adjusted leverage than gaming technology provider Inspired Entertainment, Inc. (B/Stable), but is less exposed to regulatory changes.

Key Assumptions

- Firm revenue growth to TRY1.4 billion by 2022, mainly driven by Turkish lira depreciation, with low- to mid- single digit organic growth and higher growth in the Balkans
- Steady improvement in EBITDA, mainly due to the impact from international operations from 2020. However, Northern Cyprus's EBITDA margin is expected to decrease slightly due to a change in customer base playing lower-margin games.
- Capex as per management guidance
- FY19 working capital inflow due to receivables management. From FY20 cash outflows in line with increasing revenue

RATING SENSITIVITIES

Not applicable

Liquidity and Debt Structure

Reducing but Still Satisfactory Liquidity: At end-September 2019, we estimate that Net Holding had around TRY360 million readily available cash. Additionally, the company states it has access to undrawn committed credit lines of around TRY750 million, mainly denominated in hard currencies. The main source of external liquidity is a committed secured facility provided by Denizbank, with an undrawn portion of EUR105 million as of end-September 2019, offering loans with maturity of up to eight years (of which the first two years are non-amortising). This is sufficient to cover short-term debt of around TRY422 million as of end-September 2019. We estimate that large capex over the next three years would consume but not exhaust this liquidity buffer. All debt is provided by local banks and more than 90% is expressed in hard currencies.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or to the way in which they are being managed by the entity.

For more information on our ESG Relevance Scores, visit www.fitchratings.com/esg

RATING ACTIONS		
ENTITY/DEBT	RATING	PRIOR
Net Holding A.S.	LT IDR B Affirmed	B
	LT IDR WD Withdrawn	B

Additional information is available on www.fitchratings.com

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Applicable Criteria

Corporate Rating Criteria (pub. 19 Feb 2019)

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