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Coca-Cola HBC AG

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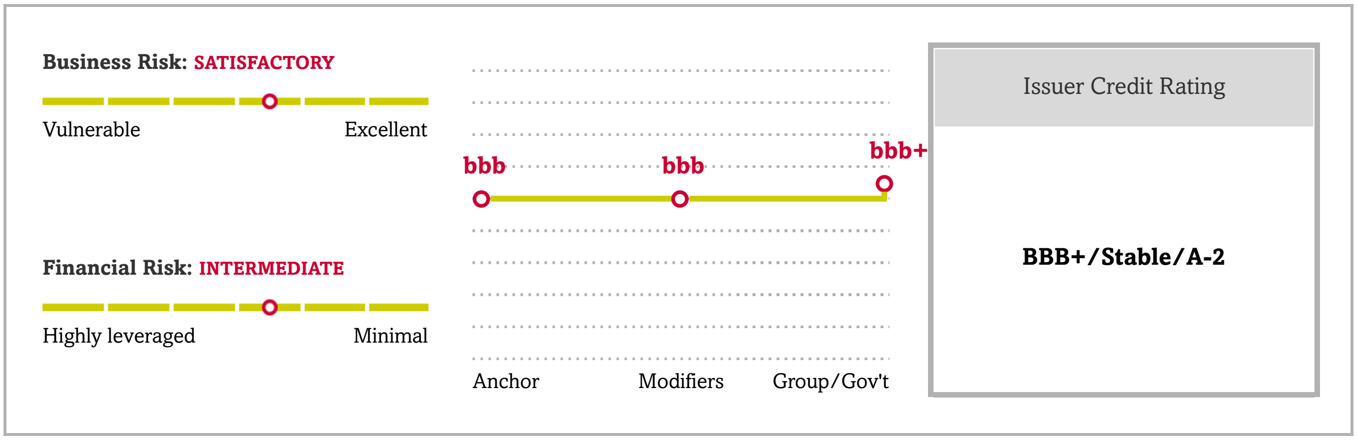

Credit Highlights

Overview

Key strengths	Key risks
Leading market position in 28 countries, supported by a portfolio with a very strong brand equity.	Near term headwinds from the COVID-19 pandemic due to high exposure to the out-of-home (mostly cafes, bars and restaurants) channel.
Presence in large emerging markets, with positive long-term growth prospects in, for example, Nigeria.	Exposure to low-volume-growth Western European markets with changing consumer habits, and stricter health regulations.
Strategy of shifting toward low-calorie sparkling beverages, energy, water, and coffee aligned with The Coca-Cola Company (TCCC).	Foreign-exchange volatility due to large operations in Nigeria and Russia.
Relatively low risk from large acquisitions in the near term, and a prudent financial policy.	Capital expenditure (capex) intensity, driven by investments into production capacity and growth markets.

Coca-Cola HBC AG (CCH) exited a turbulent 2020 in the same fashion as it entered it--with a very strong balance sheet. CCH maintained stable reported debt leverage at the low end of its 1.5x-2.0x target level, with a very strong liquidity position and no near-term refinancing needs until November 2024, when its €600 million of its senior unsecured notes are due. During 2020, CCH outperformed our base-case in terms of operating profitability and free cash flow generation. This was thanks to some decisive cost saving actions undertaken by management, leveraging on the leading market position of its sparkling product portfolio, lack of pressure from raw material costs (low sugar, aluminium, and PET resin prices), and advanced payments by certain customers. Volume-wise, the company registered a more mild decline of about 5.7% for the full year (versus our expectations of a 9% decline), supported by its exposure in emerging (mostly Nigeria and Russia) and developing (mostly Poland, Hungary, and the Czech Republic) markets, where governments did not undertake prolonged lockdowns.

Notwithstanding continued near-term headwinds in the out-of-home channel, we anticipate a return to volume and revenue growth in 2021. Our forecasts incorporate volume growth of 3%-5% in 2021, supported by normalization of the out-of-home activity in most end markets from the second quarter. This assumes global vaccination rollout continues to gather pace and there are no large-scale prolonged lockdowns, particularly in emerging and developing markets from third-quarter 2021, when we would therefore expect to see to better earnings and revenue than in the same period in 2020. We anticipate more pronounced foreign-exchange volatility (emerging currencies, but likely also from a weaker Swiss Franc and stronger U.S. dollar versus the euro) in 2021 to moderate the expected positive impact from an improved product mix (more sales of higher revenue-per-case single-serves). This should translate into overall revenue growth of 6.5%-8.5% in 2021.

We anticipate certain financial indicators will normalize in 2021. We forecast adjusted EBITDA margins and free operating cash flow (FOCF) will normalize in 2021, broadly returning to 2019 levels. This implies adjusted margins of 15.5%-15.9% and FOCF of €380 million-€395 million. Approximately €80 million of the €120 million cost savings achieved in 2020 related to a reduction in advertising and promotion activity, which we anticipate will not recur in 2021, given the company will need to defend its high market share across geographies and categories. We also anticipate some headwinds from raw material costs, particularly for aluminium and PET resin. We assume that likely price increases will broadly offset the sugar tax implementation in Poland, with no material impact on profitability. The effect of the advanced payments by some customers in the second half of 2020 will reverse in 2021 and we anticipate moderate annual outflows from working capital, while capex (excluding lease payments) will likely remain broadly flat at about 6.7% of revenue.

We think that the business will remain capex-intensive in the near-to-medium term. This is despite the announced rationalization of offerings across certain product categories. We expect product line investments will continue to support the ongoing geographical rollout of Costa Coffee, and Topo Chico within the alcoholic beverages' category. The company is also heavily investing in sustainability initiatives, notably in-house production lines for recycled PET bottle preforms to address related market challenges and achieve its environmental goals. As a result, we assume adjusted debt to EBITDA of 1.8x-1.9x and FOCF to debt of 19.5%-20.5%, which we consider very solid for the current rating level.

The risk of large mergers and acquisitions (M&A) in the near term remain limited. The company capital allocation and financial policy is clear. We think that large M&A risk remains limited, at least in the near term, because an ultimate decision on the availability of Coca-Cola licenses in nearby countries rests on the TCCC. While we think that the ongoing Coca-Cola European Partners and Amatil (both non-rated) tie-up could raise the prospects in the future for further consolidation of the Coca-Cola bottling system, we think that it will likely take time to materialize. Furthermore, CCH has a consistent public financial policy of maintaining reported net debt to comparable adjusted EBITDA of 1.5x-2.0x. While external growth will remain part of CCH's long-term business strategy, we think the strategy will revolve around small bolt-on acquisitions to complement the existing product portfolio. We have factored in €100 million-€200 million of bolt-on spending in our forecast horizon, with continued low-to-mid- single-digit growth in ordinary dividend distributions, which should lead to the company's debt leverage increasing toward the upper end of its target policy. We view CCH's shareholder remuneration as consistent with extraordinary dividends, occurring only if net leverage remains in check, as was the case in 2019.

Outlook: Stable

The stable outlook reflects our view that, despite the near-term headwinds from the ongoing COVID-19 pandemic, CCH has sufficient operational and financial flexibility to maintain stable adjusted debt to EBITDA of about 2.0x over the next 24 months. This is supported by the company's very strong market position in the soft drinks category, a defensive consumer staples category, that should enable it to generate positive FOCF of well over €300 million per year.

Downside scenario

CCH's ratios reflect comfortable headroom under the 'BBB+' rating. Given the company's resilient performance since the start of the COVID-19 pandemic, we believe that the most likely downward rating scenario relates to an unforeseen large debt-funded acquisition, such that adjusted debt to EBITDA reaches 3.0x with no prospect for a rapid improvement.

Upside scenario

We could raise the rating on CCH if we see sustained stronger-than-expected free cash flow growth, resulting in FOCF to debt comfortably above 25% and adjusted net debt to EBITDA remaining at the lower end of the policy range of 1.5x-2.0x. This could occur if trading conditions in the affected out-of-home channel recover more quickly than we anticipate. Under such a scenario, however, an upgrade is also contingent on a commitment of the company maintaining the ratios in this range on a sustained basis. This would therefore entail an amendment to its stated target policy.

Our Base-Case Scenario

Assumptions

Our base-case for 2021-2022 assumes:

- Overall revenue increase of 6.5%-8.5% in 2021 compared with 2020, to €6.53 billion-€6.65 billion, with volume growth of 3%-5%. We forecast further revenue growth of 5%-6% in 2022, assuming normalization of activity in the out-of-home channel across key geographies.
- Normalization of S&P Global Ratings' adjusted EBITDA margin to 15.5%-15.9% in 2021 and 2022, compared with 2020 (17.3%), as the company restores advertising and promotion activity to normal levels. We anticipate input cost movements will also be less favourable in 2021 compared with 2020.
- FOCF of €380 million-€395 million in 2021, and €370 million-€390 million in 2022. Our expectations for 2021 incorporate €420 million-€440 million of capex and a partial reversal of the working capital inflows registered during 2020 from prepayments of orders by some customers.
- Common ordinary dividend distribution of about €229 million in 2021, and our assumption for 35%-45% of ordinary dividend distribution in 2022, in line with the company's publicly stated target policy.

Key Metrics

Coca-Cola HBC AG--Key Metrics*			
	--Fiscal year ended Dec. 31--		
(Bil. EUR)	**2020a**	**2021e**	**2022f**
Revenue growth (%)	(12.7)	6.5-8.5	5.0-6.0
Revenue	6.1	6.5-6.7	6.8-7.0
EBITDA margin (%)	17.3	15.5-15.9	15.5-15.9
Debt to EBITDA (x)	1.7	1.8-1.9	1.8-1.9
FFO to debt (%)	45.8	42-43	42-43
FOCF to debt (%)	21.8	19.5-20.5	19.5-20.5

*All figures adjusted by S&P Global Ratings.FFO--Funds from operations.FOCF--Free operating cash flow. a--Actual. e--Estimate. f--Forecast.

Company Description

Headquartered in Switzerland, CCH is soft drinks, beverages, waters, coffee, and juices branded manufacturer. The company produces and distributes most of its products under an exclusive license from The Coca-Cola Company (TCCC; A+/Negative/A-1). CCH in its current form traces its formation back to 2000, when Greece-based Hellenic Bottling Company S.A. merged with Coca-Cola Beverages Limited.

CCH produces over 2 billion unit cases per year from 56 manufacturing plants. It has operations in 28 countries with its main markets being Russia, Italy, and Nigeria, which together accounted for about 39% of the total volumes and 33% of revenue in 2020 (39% and 35% in 2019, respectively). In 2020, CCH reported net sales revenue of about €6.1 billion (€7.0 billion in 2019) and S&P Global Ratings-adjusted EBITDA of approximately €1.04 billion (€1.1 billion in 2019).

As of Dec. 31, 2020, approximately 23% of CCH's share capital is owned by TCCC, a further 23% by Luxembourg-based private investment holding company Kar-Tess Holding, with the remainder freely floating on the London and Athens stock exchanges.

Financial summary

Table 1

Coca-Cola HBC AG--Financial Summary					
Industry sector: Beverages					
	--Fiscal year ended Dec. 31--				
	2020	**2019**	**2018**	**2017**	**2016**
(Mil. €)					
Revenue	6,131.8	7,026.0	6,657.1	6,522.0	6,219.0
EBITDA	1,059.7	1,115.9	1,029.3	967.2	903.4
Funds from operations (FFO)	811.8	832.6	863.1	793.8	729.9
Interest expense	75.6	76.7	59.3	64.4	89.4
Cash interest paid	64.7	71.8	49.7	45.0	81.3
Cash flow from operations	806.1	860.3	800.7	801.8	728.0

Table 1

Coca-Cola HBC AG--Financial Summary (cont.)

Industry sector: Beverages	--Fiscal year ended Dec. 31--				
	2020	**2019**	**2018**	**2017**	**2016**
Capital expenditure	419.2	473.2	438.7	411.7	347.8
Free operating cash flow (FOCF)	386.9	387.1	362.0	390.1	380.2
Discretionary cash flow (DCF)	161.0	(739.4)	135.2	229.4	235.2
Cash and short-term investments	1,284.0	1,531.8	887.8	753.3	412.2
Gross available cash	1,284.0	1,531.8	891.3	757.0	415.8
Debt	1,773.1	1,849.9	908.9	1,066.8	1,419.0
Equity	2,633.3	2,700.2	3,116.4	3,012.2	2,870.1
Adjusted ratios					
EBITDA margin (%)	17.3	15.9	15.5	14.8	14.5
Return on capital (%)	14.7	17.1	16.6	14.8	12.4
EBITDA interest coverage (x)	14.0	14.5	17.4	15.0	10.1
FFO cash interest coverage (x)	13.5	12.6	18.4	18.7	10.0
Debt/EBITDA (x)	1.7	1.7	0.9	1.1	1.6
FFO/debt (%)	45.8	45.0	95.0	74.4	51.4
Cash flow from operations/debt (%)	45.5	46.5	88.1	75.2	51.3
FOCF/debt (%)	21.8	20.9	39.8	36.6	26.8
DCF/debt (%)	9.1	(40.0)	14.9	21.5	16.6

All figures adjusted by S&P Global Ratings.

Reconciliation

Table 2

Coca-Cola HBC AG--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €)

	--Fiscal year ended Dec. 31, 2020--						
Coca-Cola HBC AG reported amounts							
	Debt	**Shareholders' equity**	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**	**Cash flow from operations**
Reported	2,741.3	2,630.7	1,049.7	660.7	73.6	1,059.7	961.5
S&P Global Ratings' adjustments							
Cash taxes paid	--	--	--	--	--	(183.2)	--
Cash interest paid	--	--	--	--	--	(64.7)	--
Trade receivables securitizations	90.9	--	--	--	--	--	(90.9)
Reported lease liabilities	184.2	--	--	--	--	--	--
Postretirement benefit obligations/deferred compensation	40.7	--	(5.8)	(5.8)	2.0	--	--
Accessible cash and liquid investments	(1,284.0)	--	--	--	--	--	--

Table 2

Coca-Cola HBC AG--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €) (cont.)							
Share-based compensation expense	--	--	9.5	--	--	--	--
Dividends received from equity investments	--	--	29.1	--	--	--	--
Income (expense) of unconsolidated companies	--	--	(21.4)	--	--	--	--
Nonoperating income (expense)	--	--	--	6.8	--	--	--
Reclassification of interest and dividend cash flows	--	--	--	--	--	--	(64.5)
Noncontrolling interest/minority interest	--	2.6	--	--	--	--	--
EBITDA: Gain/(loss) on disposals of PP&E	--	--	(1.4)	(1.4)	--	--	--
Total adjustments	(968.2)	2.6	10.0	(0.4)	2.0	(247.9)	(155.4)
S&P Global Ratings' adjusted amounts							
	Debt	**Equity**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**
Adjusted	1,773.1	2,633.3	1,059.7	660.3	75.6	811.8	806.1

All figures adjusted by S&P Global Ratings.

Liquidity : Strong

We assess CCH's liquidity as strong, reflecting our calculation that sources of cash should exceed uses by more than 1.5x over the next 24 months, with no material large debt maturities until 2024. This is supported by the group's well-established track record in accessing capital markets and bank financing. There are no maintenance financial covenants on the debt.

Principal liquidity sources

- €800 million of committed available undrawn revolving credit facility (RCF) maturing beyond the next 12 months;
- Available cash and cash equivalents of about €1.284 billion as of Dec. 31, 2020; and
- Our forecast of cash funds from operations (FFO) of €800 million-€820 million.

Principal liquidity uses

- €315.2 million of short-term debt;
- Our forecast of net annual working capital outflows of €20 million-€30 million;
- Intrayear working capital requirements of about €50 million;
- Our forecast of capex requirements of about €420 million-€440 million; and
- Cash dividends of about €229.4 million.

Environmental, Social, And Governance

Similar to other beverage bottling companies, CCH has moderate exposure to environmental risks related to plastic packaging waste, water scarcity, and health concerns. Governments are increasingly enforcing more stringent recycling rules, which could mean higher operating costs for CCH if it has to pay to collect and recycle plastic waste. For instance, in 2018 the EU introduced the first regional-wide plastics strategy to achieve 100% recyclable plastic packaging by 2030 and reduce consumption of single-use plastics. CCH is committed to collecting and recycling 75% of primary packaging by 2025 (48% in 2019; 44% in 2020). It also aims to increase the share of recycled PET (or that from renewable sources) to 35% by 2025 and 50% by 2030 (12% in 2019; 9% in 2020). Changing consumer tastes and stricter health regulations on sugar content in drinks are risks for its sparkling beverages business. Therefore, CCH continues to invest in the expansion of its no- and low-sugar content drinks. The company is currently investing in own in-house production lines for recycled PET bottle preforms from cheaper feedstock--hot-washed PET flakes. While COVID-19 has hindered the progress toward achieving some of its targets, notably on primary packaging collection and use of recycled PET, we believe that CCH is taking proactive steps in the environmental aspects of sustainability.

As a beverage bottler, CCH could also face rising operating costs to source water and face rising tensions with local communities as natural resources become more scarce. The company is aiming to reduce water usage by 20% by 2025 (7% in 2019 and 2020 from 2017 baseline) in plants located in high-risk areas such as Nigeria, Russia, Greece, Cyprus, and Armenia.

Our assessment of CCH's management and governance as satisfactory is supported by the consistency of the business strategy, a strong track record of improving profitably in volatile emerging markets and a balanced board composition.

Ratings Score Snapshot

Issuer Credit Rating

BBB+/Stable/A-2

Business risk: Satisfactory

- **Country risk:** Intermediate
- **Industry risk:** Low
- **Competitive position:** Satisfactory

Financial risk: Intermediate

- **Cash flow/leverage:** Intermediate

Anchor: bbb

Modifiers

- **Diversification/portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Neutral (no impact)
- **Liquidity:** Strong (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Stand-alone credit profile : bbb

- **Group credit profile:** bbb+
- **Entity status within group:** Moderately strategic (+1 notch from SACP)

Related Criteria

- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria - Corporates - Industrials: Key Credit Factors For The Branded Nondurables Industry, May 7, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	**Intermediate**	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	**bbb/bbb-**	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

Ratings Detail (As Of April 26, 2021)*

Coca-Cola HBC AG		
Issuer Credit Rating		BBB+/Stable/A-2
Issuer Credit Ratings History		
10-Apr-2019	*Foreign Currency*	BBB+/Stable/A-2
19-May-2016		BBB+/Positive/A-2
22-May-2015		BBB+/Stable/A-2
10-Apr-2019	*Local Currency*	BBB+/Stable/A-2
19-May-2016		BBB+/Positive/A-2
22-May-2015		BBB+/Stable/A-2

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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