MOODY'S INVESTORS SERVICE

CREDIT OPINION
8 July 2020

Update

Rate this Research

RATINGS

JSC Georgia Capital

Domicile	Georgia
Long Term Rating	B2
Type	LT Corporate Family Ratings
Outlook	Negative

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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JSC Georgia Capital

Update following outlook change to negative

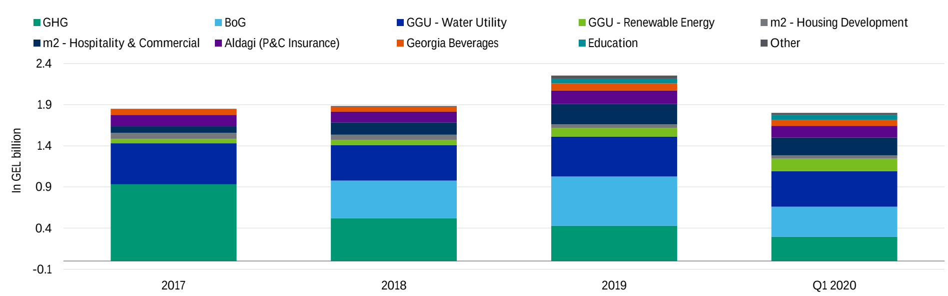
Summary

On 29 June 2020, we affirmed the corporate family rating (CFR) and the probability of default rating of JSC Georgia Capital (Georgia Capital) at B2 and B2-PD, respectively, and changed the outlook to negative from stable.

The rapid spread of the coronavirus pandemic, the deteriorating global economic outlook, low oil prices and high asset price volatility have created an unprecedented credit shock across a range of sectors and regions.

Georgia Capital's MVL has increased to slightly below 45% as of 22nd June 2020 (the 31 March 2020 valuation has been used for private assets) from around 29% as of year-end 2019. The issuer's interest cover — measured by (funds from operations [FFO] + interest)/ interest — is likely to drop well below 1.0x in 2020 from an average of around 2.0x over the last three years, before gradually recovering in 2021 and beyond. While Georgia Capital has some liquidity buffer, with GEL170 million cash on its balance sheet as of 31 March 2020 and no short-term maturities, a prolonged outbreak or economic downturn could weaken the group's MVL and liquidity. Therefore, a negative outlook was assigned to the ratings.

Exhibit 1
Bank of Georgia (BoG) and Georgia Healthcare Group (GHG) lost significant value in Q1 2020
Georgia Capital's recent portfolio value development



Sources: Company and Moody's Investors Service

Georgia Capital's B2 CFR remains supported by the company's clearly defined investment strategy, which is focused on the Georgian economy; good track record of raising capital (both debt and equity), which gives it a competitive edge in acquiring Georgian assets with little if any bidding competition from both local or international investors; portfolio of defensive investments with a stable dividend stream in normal economic conditions; and relatively good business diversification across its investment portfolio, especially in light of the small size of its portfolio.

Georgia Capital's rating is mainly constrained by its relatively small size of the investment portfolio; the strong geographic concentration of its portfolio in the Georgian economy, which is small and rated Ba2; its relatively high portfolio concentration, with the top two and three assets accounting for around 40% and 55%, respectively, of the overall value of the investment portfolio, notwithstanding the fact that Georgia Capital has made investments — with still-lower contributions to the overall portfolio value — in the auto service, education and digital businesses recently; its increasing MVL since the coronavirus outbreak; and its deteriorating interest cover because of lower dividend income from investments.

Credit strengths

- Clearly defined investment strategy
- Superior knowledge of the Georgian economy and privileged access to capital
- Portfolio focused on defensive assets (utilities, healthcare and education) with a stable dividend stream in normal economic conditions
- Relatively good business diversification across its investment portfolio, especially in light of the small size of its portfolio

Credit challenges

- Small portfolio concentrated in the Georgian economy
- Relatively short history of operating as a standalone company
- High portfolio concentration, despite the recent investments in the auto service, education and digital businesses, which account for a small portion of the overall portfolio value
- Increasing MVL since the coronavirus outbreak
- Deteriorating interest cover because of lower dividend income from investments

Rating outlook

The negative outlook assigned to the rating was prompted by a swift deterioration in the group's MVL since the coronavirus outbreak and our expectation that the issuer's interest cover will weaken substantially this year, leading to some erosion of Georgia Capital's still-adequate liquidity.

Factors that could lead to an upgrade

We do not expect positive pressure on the rating in the next 6 to 12 months at least because of the negative impact of the coronavirus pandemic on macroeconomic conditions and asset valuations, notwithstanding a successful exchange offer for Georgia Healthcare Group (GHG) and a revaluation of this asset, which could lead to an improvement in MVL.

Longer-term positive pressure could arise if Georgia Capital:

» demonstrates a prolonged track record of successfully managing its investment portfolio with a good balance between defensive and growth investments, as well as between listed and private assets, while generating value

» maintains its MVL below 35% at all times during the market cycle and an interest cover well in excess of 2.0x on a sustained basis

» maintains its strong liquidity on a sustained basis

Factors that could lead to a downgrade

Negative rating pressure would arise if:

» Georgia Capital fails to restore its MVL below 40%

» its interest cover remains below 2.0x on a sustained basis, leading to a deterioration in its liquidity

» the company has to support its underlying investments

Key indicators

Exhibit 2
JSC Georgia Capital

	2017	2018	2019	Mar-20
GAV in GEL Million	1,851	1,883	2,253	1,800
Net MVL (Moody's defined)	na	28.9%	31.1%	47.2%
Net MVL (Georgia Capital defined)	na	19.9%	27.9%	44.1%
Interest cover	1.8x	2.1x	2.3x	na

Net MVL includes guarantees issued and is based on management fair values; Georgia Capital-defined net MVL includes loans issued to portfolio companies.
Sources: Company and Moody's Investors Service

Profile

JSC Georgia Capital (Georgia Capital), the issuer of the rated bond, is a Georgia-based intermediate holding company of a number of investments focused on the Georgian economy. Georgia Capital is ultimately owned by Georgia Capital Plc (GCAP), the parent company of the group listed on the London Stock Exchange.

Georgia Capital actively manages a portfolio of companies solely operating in Georgia. The group's current portfolio (as of 31 March 2020) includes stakes in the following companies: Georgia Global Utilities (GGU), a water utility and renewable energy business (a 100% stake in both water utility and renewable energy; both managed by GGU); GHG, a UK listed healthcare business (a 70.63% stake); Aldagi, a property and casualty insurance company (a 100% stake); m2, a real estate company (a 100% stake); and Georgia Beverages, a beverage business focused on wine and beer (a 87% stake). Georgia Capital also owns a 19.9% stake in JSC Bank of Georgia (BoG, Ba2 stable), a Georgian bank listed on the London Stock Exchange.

Georgia Capital is likely to actively manage its investments, with a view to divest them within a time horizon of five to 10 years through IPOs, strategic sales or other available options. The group aims at achieving an internal rate of return of at least 25%.

Recent developments

Georgia Capital is in the process of finalizing an exchange offer for GHG. On 2 July 2020, GCAP announced that the offer had been declared unconditional as to acceptances. GCAP received necessary votes for offer to become unconditional, but not enough for reaching the squeeze out threshold. The threshold for the offer to become unconditional was 50% of free float and the squeeze out threshold was 97% of GHG's total issued shares. Valid acceptances in respect of 30,546,535 GHG shares were received, representing approximately 79% of free float and 93.83% holding of GHG's total issued shares. GCAP can delist GHG, as the offer is unconditional. The offer is still open until 16th of July for further acceptances though.

We expect GCAP to delist GHG and to initiate a revaluation exercise to be conducted by an independent third-party valuation firm. MVL metrics could fall back below our downgrade trigger if it is successful in assuming 100% control of GHG and if the revaluation of the business significantly increases the value of GHG. In Georgia Capital's view, GHG is currently trading at a significant discount to fair value because of the very low free float of the company (trading volume of less than £10,000 per day).

Detailed credit considerations

Clearly defined investment strategy focused on the Georgian economy and supported by good access to capital

In light of its strong knowledge and experience of the Georgian economy, Georgia Capital has focused its investment strategy on building a portfolio of assets solely exposed to the Georgian economy. We do not expect this strategy to change in the future as it has been successful so far.

Georgia Capital has a competitive edge as an investor in the local Georgian economy, mainly because of its strong access to capital. Foreign capital remains scarce in the Georgian economy because of its small size. Therefore, Georgia Capital has faced very little competition, if any, when bidding for assets because there are no local investment firms with sufficient capital to compete for the same assets as the company and foreign investors might have limited interest because of the small size of the investments and the economy. BGEO Group Plc (the former parent of Georgia Capital), through its public listing on the London Stock Exchange, its access to the international public debt capital markets and its bank license, was able to raise around $5 billion in capital through different channels over the last 10 years. This has enabled the group to either make investments in relatively undervalued companies or generate incremental value, or both, by providing capital for value-accretive investment projects at its investments.

We expect Georgia Capital to continue to benefit from this competitive edge as foreign capital will remain scarce in the Georgian economy, and we do not expect significant competition for bidding assets to emerge over the foreseeable future. Georgia Capital has also started building a track record of generating value through the successful development of its assets. Its management team usually involves itself fairly actively in the management of investments during the early phase, with a strong focus on the strategic development of the assets, while its active involvement reduces over time when the investments mature.

In recent years, Georgia Capital's investment strategy has been focused on the service and defensive industries with high valuation multiples. Its focus on the service industry makes sense because the Georgian economy has no strong industrial businesses as the economy lacks scale and local industrial businesses cannot compete with large industrial conglomerates. The company's strategy will remain focused, to a large extent, on the service industry in Georgia, with a focus on investing in defensive businesses. Its recent investments have been in the auto service industry (an 80% stake in Amboli LLC, a Georgian importer, distributor, wholesaler and retailer of car consumables and spare parts, such as tires, oil, batteries and lubricants for light vehicles) and in the field of digital marketing (a 60% stake in Redberry LLC). Georgia Capital has also launched the organic development of a mandatory vehicle inspection service, an immature market in Georgia. Lastly, Georgia Capital has started investing in private education. Its investment in this sector increased to GEL56 million as of March 2020 from GEL7 million a year earlier, through three investments in private schools. The investment strategy in recent years has been successful; however, the group's track record as an independent investment holding company still needs to be built.

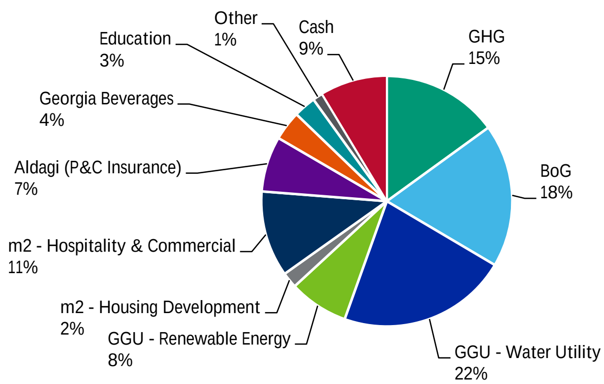
Georgia Capital will aim at divesting its investments after a five-to-ten year ownership period, with the preferred route to exit being a trade sale.

Focus on the Georgian economy and small size lead to high asset concentration and weak geographic diversification

While Georgia Capital will have a competitive edge in investing in Georgian assets, this strategy implies a high asset concentration, a lack of geographic diversification and a small overall portfolio (about $612 million as of 31 March 2020). Exhibit 3 illustrates that Georgia Capital's investment portfolio was highly concentrated, with its top two and top three largest holdings accounting for around 40% and 55%, respectively, of the overall portfolio value. This concentration is only partly mitigated by the defensiveness of some of the underlying assets, such as the group's investment in healthcare and utility.

Exhibit 3

Georgia Capital's top three investments accounted for 55% of the overall value of the investment portfolio
Georgia Capital's portfolio composition as of 31 March 2020



Other includes pipeline investments (auto and digital services).
Sources: Company and Moody's Investors Service

The focus on the Georgian economy also results in very weak geographic diversity and a strong exposure to the Georgian economy. The underlying investments are not only domiciled in Georgia but are almost solely exposed to the domestic economy.

We rate the Government of Georgia Ba2 stable. According to our latest credit opinion (published on 24 March 2020), the Georgian economy's resilience in the wake of regional economic shocks demonstrates the increasing strength of its economy and institutions. Reasonably high economic growth is underpinned by strong inflows of foreign direct investments, partly offsetting the country's small, low-income economy. However, significant banking sector risks and external vulnerability risks continue to constrain the rating. Georgia has responded to the coronavirus pandemic in a decisive manner; however, restrictions will reduce its 2020 growth rate.

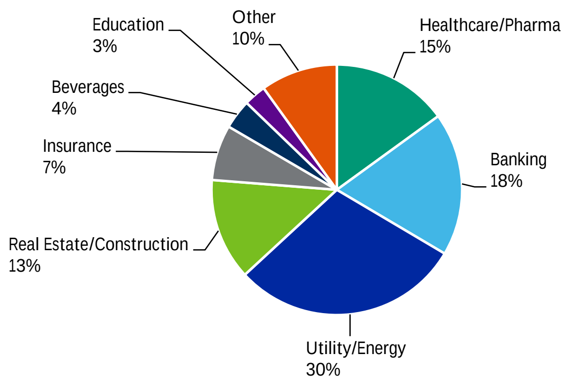
Reasonably good business diversification, but investment portfolio transparency could deteriorate upon the delisting of GHG

Despite an investment strategy focused on the Georgian economy and the service sector, with a bias toward defensive end-industries, the investment portfolio of the investment arm of Georgia Capital is relatively well diversified across sectors. As illustrated in Exhibit 4, as of 31 March 2020, Georgia Capital had exposure to the healthcare (15% of the portfolio value), utility (30%) and the banking (18%) sectors, with real estate and insurance accounting for the remaining value of the portfolio. This is a reasonably good diversification level in light of the overall small size of the investment portfolio. While we consider the utility and healthcare assets as one sector, there is some diversification within the utility sector (water distribution and electricity generation) and the healthcare sector (hospitals, pharmacy and the small medical insurance business).

Exhibit 4

Reasonably well-diversified investment portfolio in light of its small size (<$1 billion)

Business sector contribution to the overall value of the investment portfolio (as of 31 March 2020)

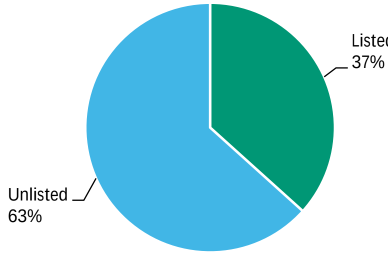


Other includes GEL170 million cash on its balance sheet as of 31 March 2020.
Sources: Company and Moody's Investors Service

If the exchange offer can be completed successfully, we estimate on a point-in-time basis that only 20% of the asset value will be from listed companies, which could lead to less flexibility when it needs additional liquidity, notwithstanding the fact that the market liquidity of GHG was rather limited as a publicly listed company.

Exhibit 5

Share of listed and unlisted assets in the investment portfolio (as of 31 March 2020)

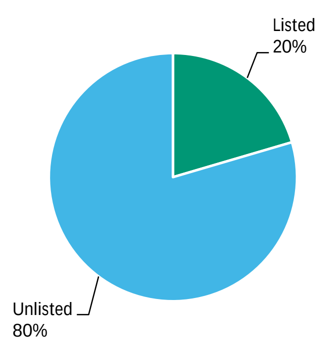


Sources: Company and Moody's Investors Service

Exhibit 6

Investment transparency will deteriorate upon completion of the delisting of GHG

Pro Forma calculation as of 22 June 2020



Source: Moody's Investors Service

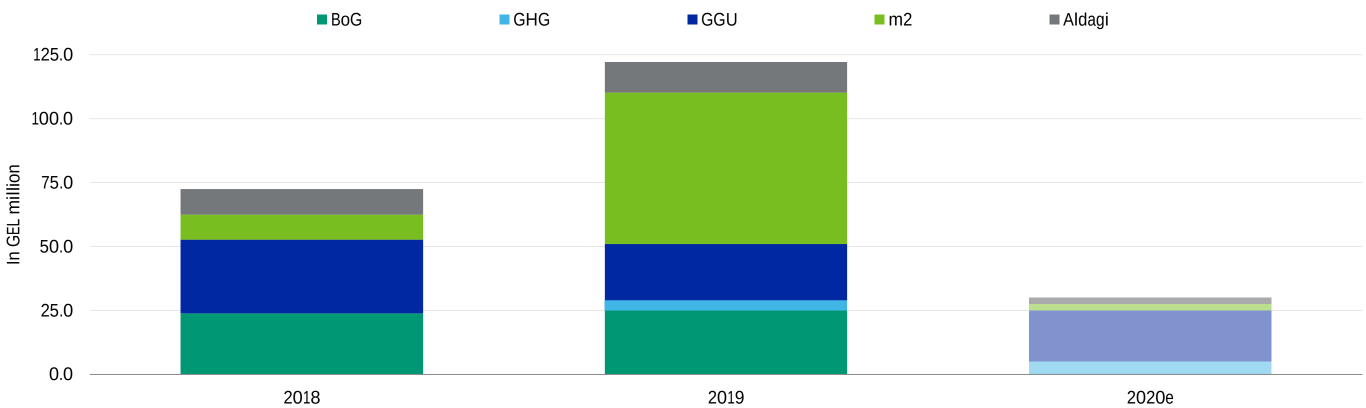
Swift increase in MVL has diminished the capacity for further deterioration in asset value

The market value of Georgia Capital's investments can be volatile because its businesses operate in frontier economies. In this regard, the value of Bank of Georgia dropped significantly during Q1 2020 and recovered only marginally in Q2, while GHG's value also dropped. Georgia Capital's MVL has increased to slightly below 45% as of 22nd June 2020 (the 31 March valuation has been used for private assets) from around 29% as of year-end 2019. GCAP indicated that it would revalue GHG after its delisting by an independent valuation firm. A significant revaluation of the business could have a positive impact on its MVL and bring its MVL back below our downgrade trigger assuming that the valuation of other investments in GCAP's portfolio does not change in the meantime.

The issuer's interest cover, as measured by (FFO + interest)/interest, is likely to drop well below 1.0x in 2020 from an average of around 2.0x over the last three years, before gradually recovering in 2021 and beyond. While Georgia Capital has some liquidity buffer, with GEL170 million cash on its balance sheet as of 31 March 2020 and no short-term maturities, a prolonged outbreak or economic downturn could weaken the group's MVL and liquidity. Therefore, a negative outlook is assigned to the ratings.

Exhibit 7

Georgia Capital's interest coverage will remain weak over the next 12-18 months; its cash on balance will provide some liquidity buffer



Sources: Company and Moody's Investors Service

Liquidity analysis

Georgia Capital's liquidity was adequate as of 31 March 2020. It had GEL170 million (around $53 million) of cash and liquid funds on its balance sheet as of 31 March. Georgia Capital will not face any maturity before 2024 when the senior notes become due. GCAP's senior notes are denominated in US dollars. The depreciation of the Georgian Lari against the US Dollar since the outbreak has led to a significant increase in the local currency value of the notes. We do not exclude further increases in the local currency value of these notes. Maturities at the portfolio company level are also fairly manageable in 2020, with only GEL76 million becoming due (GEL242 million in 2021 and GEL210 million in 2022).

Methodology and scorecard

In assessing the credit quality of Georgia Capital, we apply our Investment Holding Companies and Conglomerates rating methodology, published in July 2018. In our 12-18-month forward-looking view, the scorecard indicates a B1 rating, one notch above the actual assigned rating.

The difference between the scorecard-indicated rating outcome and the assigned rating reflects the small size of the overall investment portfolio (less than $1 billion), as well as the lack of a track record of operating as a rated investment holding company and within the financial policy target of maintaining an MVL below 30% (excluding intercompany loans from the gross asset value of the investment portfolio) at all times during the market cycle. At the same time, Georgia Capital has built a track record of managing a portfolio of investments while generating value.

Exhibit 8

Rating factors

JSC Georgia Capital

Investment Holding Companies Industry	Current LTM March 2020		Moody's 12-18 Month Forward View As of 6/23/2020 [1]	
Factor 1 : Investment Strategy (10%)	**Measure**	**Score**	**Measure**	**Score**
a) Investment Strategy	Ba	Ba	Ba	Ba
Factor 2 : Asset Quality (40%)				
a) Asset Concentration	B	B	B	B
b) Geographic Diversity	Caa	Caa	Caa	Caa
c) Business Diversity	Ba	Ba	Ba	Ba
d) Investment Portfolio Transparency	Ba	Ba	B	B
Factor 3 : Financial Policy (10%)				
a) Financial Policy	Ba	Ba	Ba	Ba
Factor 4 : Estimated Market Value-based Leverage (MVL) (20%)				
a) Estimated Market Value-Based Leverage	B	B	B	B
Factor 5 : Debt Coverage and Liquidity (20%)				
a) (FFO + Interest Expense) / Interest Expense	2.3x	Ba	0.3x	Caa
b) Liquidity	Baa	Baa	Baa	Baa
Rating:				
a) Scorecard-Indicated Outcome		Ba3		B1
b) Actual Rating Assigned				B2

[1] This represents Moody's forward view, not the view of the issuer, and unless noted in the text, does not incorporate significant acquisitions and divestitures.
Source: Moody's Investors Service

Appendix

Exhibit 9

Peer comparison

JSC Georgia Capital

	JSC Georgia Capital		Koc Holding A.S.		Ordu Yardimlasma Kurumu (OYAK)		Kagiso Tiso Holdings Proprietary Limited		Svyazinvestneftekhim JSC*	
Current rating	**B2 Negative**		**B1 Negative**		**B1 Negative**		**B2 Ratings Under Review**		**Ba1 Stable**	
Country of Domicile	**Georgia**		**Turkey**		**Turkey**		**South Africa**		**Russia**	
	LTM Q1 2020	**FWD**	**FY 2019**	**FWD**	**FY 2019**	**FWD**	**6/30/2019**	**FWD**	**FY 2018**	**FWD**
Investment Strategy (10%)										
a) Investment Strategy	Ba	Ba	Baa	Baa	Baa	Baa	Ba	Ba	B	B
Asset Quality (40%)										
a) Asset Concentration	B	B	Baa	Baa	Baa	Baa	B	B	Caa	Caa
b) Geographic Diversity	Caa	Caa	B	B	B	B	B	B	Caa	Caa
c) Business Diversity	Ba	Ba	Baa	Baa	Baa	Baa	B	B	B	B
d) Investment Portfolio Transparency	Ba	B	A	A	Baa	Baa	B	B	Ba	Ba
Financial Policy (10%)										
a) Financial Policy	Ba	Ba	A	A	A	A	Ba	B	B	B
Estimated MVL (20%)										
a) Estimated Market Value-Based Leverage	B	B	Aaa	Aaa	Aaa	Aaa	A	A	Aaa	Aaa
Debt Coverage and Liquidity (20%)										
a) (FFO + Interest Expense) / Interest Expense	Ba	Caa	Aa	Ba	Aaa	Caa	Caa	Caa	Aaa	Aaa
b) Liquidity	Baa	Baa	Aaa	Aaa	Aaa	Aaa	B	Caa	Ba	Ba

* Government-related entity.

Source: Moody's Investors Service

Ratings

Exhibit 10

Category	Moody's Rating
JSC GEORGIA CAPITAL	
Outlook	Negative
Corporate Family Rating	B2
Senior Unsecured	B2/LGD4

Source: Moody's Investors Service

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