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Research Update:

Georgia Capital Upgraded To 'BB-' On New Capital Structure; Outlook Stable; New $150 Million Unsecured Notes Rated 'BB-'

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Rating Action Overview

- Georgia Capital JSC successfully raised $150 million of sustainability-linked senior unsecured notes, due 2028. The company used the proceeds alongside cash at hand to fully redeem the $300 million notes due in March 2024.
- We see the new capital structure as supportive for Georgia Capital's credit standing because the company has now meaningfully extended its debt maturity profile and reduced its outstanding absolute debt in a context of rising interest rates. As of the end of June 2023, pro forma the $150 million bond issued and the full redemption of its $300 million notes due 2024, we estimate that Georgia Capital's loan-to-value (LTV) ratio reached 8.8%, meaningfully improving from 13.3% as of the end of December 2022.
- In addition, we anticipate a relatively supportive macroeconomic scenario for the government of Georgia, where all the company's assets are located, and hereby expect the holding to continue to receive stable to improving dividends of about Georgian lari (GEL) 180 million–GEL200 million per year from its investee assets in 2023-2024.
- We therefore raised our long-term issuer credit rating on Georgia Capital to 'BB-' from 'B+' and removed the rating from CreditWatch positive, where it was placed on July 12, 2023. We also assigned a 'BB-' issue rating to the $150 million senior unsecured notes, in line with the preliminary rating we assigned on July 12, 2023.
- The stable outlook reflects our view that Georgia Capital's LTV ratio will remain materially below 25% over the next 12 months, and that its cash adequacy ratio will remain above 3.0x.

Rating Action Rationale

The upgrade follows Georgia Capital's completed refinancing and the resulting extension of its debt maturity profile. Georgia Capital has completed the issuance of the $150 million sustainability-linked senior unsecured notes in the Georgian market. The notes are U.S.

dollar-denominated with a five-year bullet maturity, due August 2028 (callable after two years at the company's discretion) and carry an 8.5% fixed coupon. The proceeds, together with liquid funds at the holding, were used to fully redeem and cancel the $300 million notes due March 2024. We see Georgia Capital's new capital structure as supportive for its credit standing because the company has now meaningfully extended its debt maturity profile and reduced its outstanding absolute debt in a context of rising interest rates. As of the end of June 2023, pro forma the $150 million bond issuance and the full redemption of its $300 million notes due in 2024, we estimate that Georgia Capital's LTV ratio reached 8.8%--meaningfully improving from 13.3% as of the end of December 2022. Finally, the terms and conditions of the transaction are in line with the preliminary documentation. We therefore raised the issuer credit rating on Georgia Capital to 'BB-' from 'B+', and removed the rating from CreditWatch positive, where we placed it on July 12, 2023. At the same time, we assigned a 'BB-' issue rating to the new bond, in line with the preliminary issue rating assigned on July 12, 2023 (see "Georgia Capital On CreditWatch Positive On Debt Refinancing; Preliminary 'BB-' Rating Assigned To Proposed Notes," published July 12, 2023, on RatingsDirect)

The relatively supportive economy in Georgia, where all the company's assets are located, should continue to support Georgia Capital's assets' operating performance, dividend payments, and ultimately its leverage over 2023-2024. Georgia Capital saw an 11.8% increase in its net asset value (NAV) during the first half of 2023. The main contributor for NAV growth in the portfolio was the Bank of Georgia, with the share price up 12.3% during the first half of 2023. We also note that the private portfolio companies' value increased by 4.8% during the same period.

We also anticipate a relatively resilient Georgian economy. The government of Georgia's real GDP grew by 7.6% over the first half of 2023. This points to continued financial and migration inflows, particularly from Russia, alongside a strong recovery in the tourism sector. We expect growth to ease to a still solid 6.1% in 2023 from last year's 10.1% (see "Georgia 'BB/B' Ratings Affirmed; Outlook Stable," published Aug. 11, 2023, on RatingsDirect). As a result, Georgia Capital's assets should benefit from relatively supportive demand drivers as well as continue to generate a good level of dividends that could support organic deleveraging.

We expect dividends will grow in 2023-2024 and view the holding's liquidity post-refinancing as adequate. Cash interest and dividends for the full year will reach about GEL200 million ($77 million) in 2023, up from about GEL130 million ($50 million) in 2022. Considering that the pharmacy business paid an extraordinary dividend of about GEL27 million in 2023, we expect cash interest and dividends to moderate to about GEL180 million ($69 million) in 2024. In addition, the new capital structure reduced gross debt by about GEL390 million ($150 million), implying interest payments of about GEL32 million per year going forward, down from GEL70 million in 2022. As a result, we project Georgia Capital's cash adequacy ratio to be 3x-4x over 2023-2024, up from 1.2x in 2022. In addition, thanks to the company's meaningfully extended debt maturity profile, we anticipate that Georgia Capital's sources of cash over uses to be about 1.8x for the first 12 months after the refinancing is complete.

We expect Georgia Capital to maintain relatively low leverage for the rating, supported by its financial policy. At the same time, the NAV discount remains high and the company's debt remains exposed to U.S. dollar exchange rate fluctuations. In May 2022, Georgia Capital updated its capital management framework to prioritize deleveraging and reduce its debt and risk exposure. The holding is also implementing this deleveraging strategy across its private portfolio companies, with individual leverage targets established. The holding has a financial policy based on a net capital commitment (NCC) ratio. The NCC ratio stood at 17.4% on June 30, 2023, and the group aims to achieve a ratio of below 15% by end of 2025. The NCC ratio guides the group's share buybacks and investment policy, and we understand that an NCC ratio ranging between 15%-40% will result in tactical share buybacks or investments, while we expect an NCC ratio below 15% to generate more substantial share buybacks or investments. Given the holding's near-term deleveraging target, we expect the NCC ratio, as calculated by the company, will remain at roughly 15% and its minimum liquidity balance above $30 million. However, the discount on the NAV per share remains relatively high at about 58% and we do not exclude the possibility of material share repurchases when the refinancing has completed. Nevertheless, we anticipate the holding will balance its repurchases and investments. We also see Georgia Capital's exposure to exchange rate fluctuations between the GEL and the U.S. dollar as a risk. This is because its debt is in U.S. dollars and all its dividend income is GEL-denominated--if we exclude the renewable energy business that has cash flow in U.S. dollars and consequently pays dividends in hard currency.

Georgia Capital's business risk remains constrained by its concentration in Georgia and relatively low share of listed assets. The companies in Georgia Capital's portfolio are all based in Georgia. The Bank of Georgia, where the group holds a 20% stake, is its only listed asset. The stake in the bank was valued at GEL883 million at the end of June 2023, representing about 26% of Georgia Capital's total portfolio by value. The company has also retained a 20% stake in Georgian Global Utilities JSC, on which it has a put option with a pre-agreed enterprise value/EBITDA multiple, which can be exercised within 2025-2026. The value of this stake stood at GEL159 million ($61 million) on June 30, 2023, and is about 5% of the portfolio. The remaining 70% of the company's portfolio is represented by unlisted assets. This, in our view, could limit its ability to quickly monetize its investments to repay debt, which could be important if liquidity unexpectedly becomes constrained. Additionally, we estimate that Georgia Capital's weighted average creditworthiness of investee companies is in the high 'B' rating category. Georgia Capital's three largest assets, the Bank of Georgia, retail pharmacy, and hospitals constitute about 61% of its portfolio. However, the company is well-diversified by industry, in our view, and has investments in banking, pharmaceuticals and health care, insurance, utilities, real estate and hospitality, private education, and renewable energy generation.

Outlook

The stable outlook reflects our view that Georgia Capital's S&P Global Ratings-adjusted LTV ratio will remain sustainably below 25% in the next 12 months. We also expect solid dividends from its assets, which should translate to a cash flow adequacy ratio of about 3x.

Downside scenario

We could lower the rating if Georgia Capital's LTV ratio approaches 25%. LTV ratio deterioration would most likely be the result of a material weakening in equity values, large negative currency fluctuations, or material share buybacks signaling a more aggressive stance toward leverage.

Ratings pressure could also result from a material deterioration of the credit quality of any of Georgia Capital's core investments, which would erode valuations and increase the likelihood of Georgia Capital having to inject fresh capital for support or shareholder loans.

Upside scenario

We view upside as relatively remote at this stage given the holdings concentration and exposure to the Georgian economy. We could however consider upgrading Georgia Capital if the holding establishes a positive track record of deleveraging, such that its LTV ratio remains materially below 10% even at the bottom of the cycle. In addition, an upgrade will hinge on the company establishing a track record of conservative financial policies aimed at strengthening its capital structure over time. These include, but are not limited to, keeping a long-dated debt maturity profile, and establishing a track record of active foreign exchange management.

Company Description

Georgia Capital JSC is an investment holding company based in the Republic of Georgia. Its parent company, Georgia Capital PLC, is listed on the London Stock Exchange. At the end of the second quarter of 2023, Georgia Capital's portfolio had a value of GEL3.4 billion ($1.3 billion).

The companies in Georgia Capital's portfolio are all based in Georgia; the Bank of Georgia is its only listed asset. The 20% stake in the bank was valued at GEL883 million ($340 million) on June 30, 2023, representing 26% of Georgia Capital's total portfolio by value. The company has also retained a 20% stake in Georgian Global Utilities JSC, on which it has a put option. The value of this stake stood at GEL159 million ($61 million) on June 30, 2023. The company is well-diversified by industry, and has investments in banking, pharmaceuticals and health care, insurance, utilities, real estate and hospitality, private education, and renewable energy generation.

Our Base-Case Scenario

Assumptions

- Real GDP growth in Georgia to ease to a still solid 6.1% in 2023, down from the strong 10.1% growth seen in 2022.
- Dividend income and interest income of about GEL200 million in 2023 and GEL180 million in 2024, up from GEL130 million in 2022.
- Operating costs, including management fees and taxes, of about GEL20 million–GEL25 million per year. This compares with GEL40 million in 2022 as share based payments, amounting to GEL19 million in 2022, will be covered by treasury shares in the near term.
- Cash interest expense of about GEL35 million in 2023 and about GEL32 million in 2024, down from GEL60.4 million in 2022 as a result of lower debt.
- No dividend distributions to shareholders, in line with previous years.
- We do not exclude material share buybacks of up to GEL100 million a year, but expect the holding will maintain a minimum cash balance of GEL30 million and its NCC ratio around 15%.

Key metrics

Table 1

Georgia Capital JSC--Key metrics*

	2022a	2023e	2024e
Loan-to-value ratio (%)	13.3	<25	<25
Cash flow adequacy (x)	1	3-4	3-4

*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate.

Liquidity

We assess Georgia Capital's liquidity post-refinancing as adequate. We estimate its sources of liquidity will cover uses by about 1.8x in the 12 months following completion of the refinancing, even if including substantial share repurchases.

We believe Georgia Capital has sound relationships with local banks, given its position as a key investor in the country.

We estimate principal liquidity sources over the 12 months from Sept. 1, 2023, will include:

- About GEL99 million ($38 million) of cash and liquid funds.
- Unstressed dividends from portfolio companies and interest income of GEL180 million-GEL200 million.

We estimate the principal liquidity uses over the same period include:

- Operating costs of GEL20 million–GEL25 million.
- Interest expense of about GEL32 million.
- Share repurchases of up to GEL100 million over the next 12 months.

Covenants

The bond documentation contains an incurrence ratio of net debt to adjusted equity valued below 45%. There are also restricted payments, including dividend distribution and capital stock redemption exceeding 50% of retained earnings as of Dec. 31, 2022, and 50% of consolidated net profit thereafter. The issuer shall also, at all times, maintain in cash and liquid investments an amount equaling at least 100% of the interest to be paid on the next interest date. We believe the company has adequate headroom within these thresholds.

Environmental, Social, And Governance

Governance factors are a moderately negative consideration in our credit rating analysis of Georgia Capital because we believe the holding's risk tolerances and liquidity management are relatively more relaxed when compared to the industry norms. For example, in the past the company was not able to protect its LTV ratio because of asset value deterioration notwithstanding a financial policy in place and we observed a more aggressive liquidity management for the refinancing of its $300 million notes. Environmental and social factors are overall neutral considerations in our analysis. The group's major sector exposure is represented by retail pharmacy (22% of the adjusted portfolio value) and hospitals (13%), which we assess as having low environmental and social risks.

Issue Ratings - Subordination Risk Analysis

Capital structure

Georgia Capital's capital structure includes the $150 million sustainability-linked senior unsecured bond due in August 2028.

Analytical conclusions

We rate the notes in line with our 'BB-' long-term issuer credit rating on the group, because no elements of subordination risk are present in the capital structure.

Ratings Score Snapshot

Issuer Credit Rating	**BB-/Stable/--**
Business risk:	Vulnerable
Country risk	Moderately high
Industry risk	Intermediate
Investment position	Vulnerable
Financial risk:	Intermediate
Cash flow/leverage	Intermediate
Anchor	bb-
Modifiers:	
Liquidity	Adequate (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Neutral

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- Criteria | Corporates | Industrials: Methodology: Investment Holding Companies, Dec. 1, 2015

- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Georgia 'BB/B' Ratings Affirmed; Outlook Stable, Aug. 11, 2023
- Georgia Capital On CreditWatch Positive On Debt Refinancing; Preliminary 'BB-' Rating Assigned To Proposed Notes, July 12, 2023
- Georgia-Based Investment Holding Company Georgia Capital 'B+' Rating Affirmed On Low Leverage; Outlook Remains Negative, April 5, 2023

Ratings List

Upgraded; Outlook Action

	To	From
Georgia Capital JSC		
Issuer Credit Rating	BB-/Stable/--	B+/Watch Pos/--

Not Rated Action

	To	From
Georgia Capital JSC		
Senior Unsecured	NR	B+

New Rating

Georgia Capital JSC	
Senior Unsecured	BB-