

Rating Action: Moody's assigns B1 CFR to Pro-Gest; stable outlook

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Moody's assigns (P)B2 rating to the proposed EUR250 million senior unsecured notes due 2024

London, 01 December 2017 -- Moody's Investors Service, (Moody's) has today assigned a B1 corporate family rating (CFR) and a B1-PD probability of default rating (PDR) to the Italian paper packaging producer Pro-Gest S.p.A. ("Pro-Gest" or the "company"). Concurrently, Moody's has assigned a (P)B2 rating to the EUR250 million senior unsecured notes due 2024 to be issued by Pro-Gest.

The outlook on all ratings is stable.

The proceeds from the notes will be used to refinance part of the existing indebtedness, to pre-fund capital expenditures, and to pay transaction fees. The capital structure also includes a secured export credit facility of EUR50 million, medium and long term facilities of EUR49 million, Italian mini-bonds of EUR90 million, and finance leases of EUR16 million. At close, Moody's expects Pro-Gest to have EUR175 million of cash in the balance sheet, and approximately EUR70 million of it will be contributed to Cartiere Villa Lagarina as equity to fund capital expenditures in connection with the refurbishment and development of the Mantova Mill.

This is the first time that Moody's has assigned a rating to Pro-Gest. Moody's issues provisional ratings in advance of the final sale of securities and these ratings reflect Moody's preliminary credit opinion regarding the transaction only. Upon a conclusive review of the final documentation, including any possible changes during the syndication process, Moody's will endeavor to assign a definitive rating to the facilities. A definitive rating may differ from a provisional rating.

The list of affected ratings is included at the end of this press release.

RATINGS RATIONALE

Moody's considers that Pro-Gest is solidly positioned in the B1 category.

The assignment of the B1 CFR to Pro-Gest reflects (1) its limited scale and geographic diversity compared to other rated peers such as Smurfit Kappa (Ba1 stable); (2) the risk of price pressure and/or volatility owing to the highly competitive and fragmented paper packaging industry, particularly for more standardised containerboard products, demand-supply dynamics and growth in industrial production; (3) exposure to fluctuations in input costs, namely recycling paper and energy, and the ability to pass through increases to customers; and (4) negative free cash flow generation in 2017-2018 due to the planned but pre-funded investments in the Mantova mill, but expected to reverse thereafter.

Pro forma Moody's-adjusted leverage at close is expected to be high at around 4.8x but there is potential for rapid de-gearing below 4.0x in the next 12 to 18 months from a combination of organic EBITDA growth and mandatory debt repayments under the existing Italian mini bonds and bank debt facilities. However, one of the main drivers of organic growth is the ramp-up of the paper mill in Mantova from mid-2018, a project which presents a degree of execution risk and could suffer from delays, and operational and administrative challenges.

Conversely, the B1 rating is positively supported by (1) the company's defensive leading position as one of the largest and vertically integrated producer of containerboard and corrugated boards in Italy; (2) the well-diversified customer base with 10 largest customers accounting for 17% of FY2016 revenues and not a single customer accounting more than 2.8%; (3) the attractive features of the Italian paper packaging industry, being Italy a net importer and expected to continue to remain so at least until 2020; and (4) its LTM Sep 2017 Moody's-adjusted EBITDA margin of c.21%, which is higher than most global competitors and could further improve from 2019 with the ramp-up of the Mantova mill.

LIQUIDITY

Moody's considers Pro-Gest liquidity position to be good for its near term requirements, including working

capital needs and mandatory debt repayments. The company does not have a revolving credit facility, but the balance sheet cash will increase to EUR175 million with this transaction. However, approximately EUR70 million will be used to fund planned investment at the Mantova paper mill. Excluding these pre-funded expenditures, we expect the company to generate positive free cash flow and not distribute any dividends.

The majority of the credit agreements related to the existing debt, which will remain in place post-refinancing, include financial covenants, consisting in a maximum net leverage ratio of 4.0x-4.25x and a net debt to equity ratio of 2.5x. The non-compliance with these covenants or other obligations could trigger cross default clauses.

Moody's also notes that, Cartiere Villa Lagarina, is prohibited from paying any dividends until 6 September 2019 and it can only make dividend payments not exceeding 50% of its net income after that date. Cartiere Villa Lagarina, is a non-guaranteeing subsidiary representing a substantial part of the group EBITDA (31% of LTM Sep 2017 aggregated EBITDA), and its contribution to the EBITDA is expected to increase further with the ramp-up of the Mantova mill. Considering that the interests of the new notes will be in the region of EUR7 million and total interest expenses for the group will be equal to EUR17 million, Moody's expects Pro-Gest, excluding Lagarina, will be comfortably able to service its debt.

STRUCTURAL CONSIDERATIONS

Using Moody's Loss Given Default (LGD) methodology, the B1-PDR is aligned to the B1 CFR. This is based on a 50% recovery rate, as is typical for transactions with both bonds and bank debt. The (P)B2 rating on the senior unsecured notes due 2024 is one notch below the CFR, reflecting the large amount of debt in the operating subsidiaries that are not guaranteeing the notes and considered senior to the notes.

The 2024 senior unsecured notes, issued by Pro-Gest S.p.A., will be unsecured and guaranteed by the issuer and certain subsidiaries which accounted for 57.2% of total assets on an aggregated basis, 82.6% of consolidated total revenues and 64.6% of EBITDA on an aggregated basis (gross of intragroup transactions) as of September 2017.

RATIONALE FOR THE STABLE OUTLOOK

The stable outlook reflects Moody's view that Pro-Gest will be able to withstand competitive pressure even at times of declining testliner prices, due to its vertical integration, and maintain its EBITDA margin around 20%. The stable outlook also assumes that the company it will not engage in material debt-funded acquisitions or shareholder distributions.

WHAT COULD CHANGE THE RATING UP/DOWN

Positive rating pressure on Pro-Gest's ratings could develop if (1) the company successfully ramp-ups the production at its Mantova mill from mid-2018; (2) it maintains its high Moody's-adjusted EBITDA margin around 20%; (3) the debt/EBITDA trends below 4.0x; and (4) RCF/debt remains above 15%, while maintaining a good liquidity profile.

Negative pressure on the ratings could arise if (1) the company's operating performance is under pressure as a result of increased competition including prolonged periods of supply-demand imbalances reflective in its EBITDA margin declining towards the mid-teens; (2) debt/EBITDA rises above 5.0x for an extended period of time; and (3) the liquidity materially deteriorates.

The principal methodology used in these ratings was Global Paper and Forest Products Industry published in October 2013. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Headquartered in Treviso (Italy), Pro-Gest S.p.A. is an Italian vertically integrated producer of recycled paper, containerboard, corrugated cardboard and packaging solutions. The company operates 2 recycling plants, 5 paper mills, 4 corrugators and 8 packaging plants, for overall 19 production facilities, all located in Italy, and it employs approximately 1,000 people.

For the last twelve months (LTM) to 30 September 2017, the company reported revenues of EUR467 million and EBITDA of EUR96.7 million. The company is family owned and Mr. Bruno Zago, who founded Pro-Gest in 1973, is also its CEO.

RATINGS:

Assignments:

..Issuer: Pro-Gest S.p.A.

.... Corporate Family Rating, Assigned B1

.... Probability of Default Rating, Assigned B1-PD

...BACKED Senior Unsecured Regular Bond/Debenture, Assigned (P)B2

Outlook Actions:

..Issuer: Pro.Gest S.p.A.

....Outlook, Assigned Stable

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