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Research Update:

Dutch Equipment Rental Group Boels Topholding B.V. Upgraded To 'BB' On Continuous Develeraging; Outlook Stable

November 9, 2022

Rating Action Overview

- Boels Topholding B.V. (Boels) continues to gradually deleverage following the transformative acquisition of Cramo in 2019, with S&P Global Ratings-adjusted debt to EBITDA declining toward 3x.
- We believe that management is committed to maintaining leverage below 3.5x, and that Boels is relatively well protected against rising interest rates, given the hedging policy management is following on its term debt.
- We anticipate that the group will continue to grow revenue and profitability, with positive free operating cash flow (FOCF) and stronger credit metrics in 2023.
- Therefore, we raised our long-term issuer credit rating on Boels to 'BB' from 'BB-'. The '3' recovery rating on the term loan is unchanged, with a recovery expectation in the event of a payment default of 55%.
- The stable outlook reflects our expectation that the group will maintain adjusted EBITDA margins of more than 30% and leverage sustainably below 3.5x, coupled with good cash interest cover and adequate liquidity.

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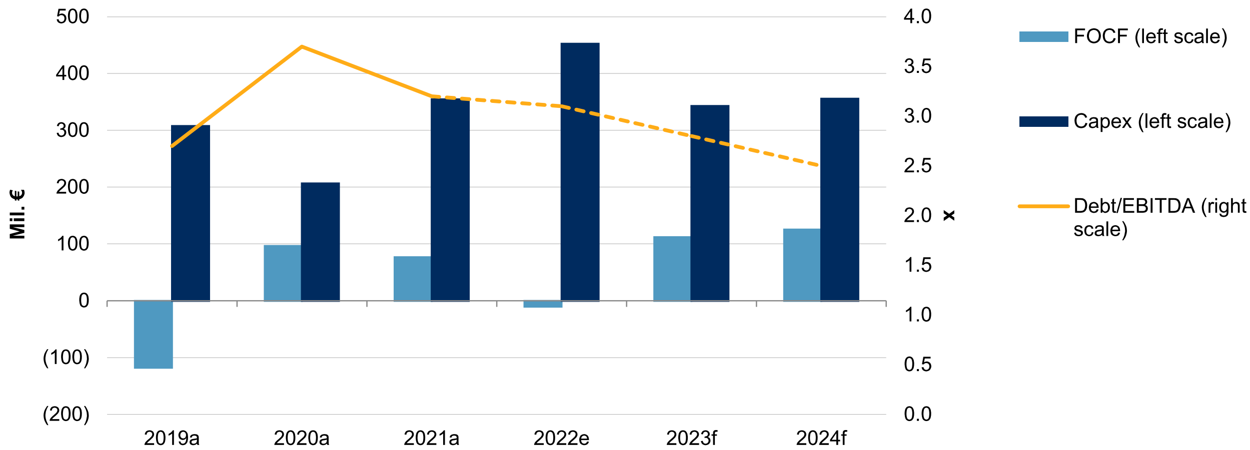
Rating Action Rationale

Following the acquisition of Cramo in 2019, Boels' management has prioritized deleveraging. Absent any large-scale mergers and acquisitions (M&A), which we do not include in our base case, Boels' leverage will continue to decline toward 3x. After a period of heavy investment in fleet through 2021 and 2022, we expect that management will likely lower capital expenditure (capex) through 2023, which would support free cash flow generation and deleveraging prospects for the group.

Chart 1

Boels Topholding B.V. Is Deleveraging As Planned

The group is committed to a 3.5x leverage target



a--Actual. e--Estimate. f--Forecast. Capex--Capital expenditure. FOCF--Free operating cash flow. Source: S&P Global Ratings.

We anticipate that the group will maintain leverage below 3.5x. Boels benefits from a capital structure that is significantly hedged against rising interest rates and comprises €900 million debt that has been hedged (3.25% + 0.17%) and €550 million unhedged. The group is therefore relatively well protected against rising interest rates versus some of its peers. Given that the rental equipment market continues to consolidate, it is possible that Boels could make opportunistic acquisitions in 2023, but we anticipate that any such moves would be more bolt-on in nature. In our view, the group is well positioned as the No. 2 European player, behind the leader Loxam SAS, and still ahead of Kiloutou, despite the latter's recent acquisition of Danish player GSV.

We expect S&P Global Ratings-adjusted debt of about €1.5 billion as of year-end 2022. This includes the €1.45 million term loan B, plus about €200 million of obligations related to operating leases, and about €4 million of pension obligations. We then net about €5 million of unrestricted cash from gross debt to arrive at our final adjusted debt figure of about €1.6 billion. We expect our adjusted debt to be at about €1.4 billion-€1.5 billion in 2023, because we do not anticipate any major acquisitions or dividend payouts during the year, while we forecast positive FOCF generation given the expected capex reduction.

After increasing capex in 2022 to expand its fleet and meet rising demand, we expect Boels to benefit in 2023, resulting in positive FOCF. Demand was relatively favorable in 2021 and the outlook for 2022 is bright, supporting our view that Boels is likely to invest heavily in its fleet. The investment in new equipment will also allow Boels to reduce the age of its fleet, which is average compared with peers' (see "Cost Discipline And Flexible Capex Keep Cash Flows Healthy For European Equipment Rental Companies," published Oct. 13, 2021). Capex is expected to increase to about €440 million-€450 million in 2022, causing free cash flow for the year to turn negative to minus €70 million. We predict it will be positive again in 2023. We estimate that Boels will benefit from its capex investment in 2023 (we estimate the average fleet age at between 4.5 and five years), but will continue to spend about €350 million in capex, of which we estimate €250 million is dedicated to maintenance capex. We believe that the group will develop through accretive internal growth, focusing on its fleet and depots' development, rather than via an acquisitive strategy and external growth. We view this positively, because it will support the group's deleveraging. Furthermore, we understand that the group has managed to pass through part of the inflation cost to customers through price increases, thus reducing the energy cost impact by managing it on a shop-by-shop basis. As Boels and many of its peers demonstrated during the pandemic, they can rapidly reduce capex to generate positive free cash flow if markets suddenly cool. We consider the group's liquidity profile to be adequate, supported by its available €200 million revolving credit facility (RCF), coupled with a long-dated debt maturity profile.

Boels has no direct exposure to the Russia-Ukraine conflict, according to management. Nevertheless, we anticipate that volatile and elevated energy and commodity prices could affect the group's customers and its supply chains in the coming months. Many industries are grappling with the same challenges--this issue is not specific to Boels or the capital goods sector. At present, we understand that the company's supply chain is not materially affected, suggesting that, for now, the impact on operating performance will be limited.

Outlook

The stable outlook indicates that we expect that the group's profitability and credit metrics will remain commensurate with a significant financial risk profile. Specifically, we expect adjusted EBITDA margins of above 30%, with adjusted debt to EBITDA sustainably below 3.5x and adjusted funds from operations (FFO) to debt of more than 20% over our 12-month rating horizon.

Downside scenario

We could lower our rating in the next 12 months if, on a sustained basis:

- Adjusted debt to EBITDA rises above 4x;
- Adjusted FFO to debt falls below 20%;
- FOCF remains negative; and
- Profitability falls below 30%.

This could occur if an economic downturn and weaker industrial production weakens the rental market more than we currently expect. We could also downgrade the group if it makes another sizable acquisition that significantly increases its debt.

Upside scenario

We currently see an upgrade as unlikely. However, we could raise our rating if:

- The group demonstrates a commitment to maintain debt to EBITDA near or below 2x and FFO to debt above 30%, on a sustainable basis;
- The company maintains positive FOCF; and

- Adjusted debt to EBITDA has a limited risk of increasing above 3x.

Company Description

Boels, headquartered in Sittard, the Netherlands, is the second-largest generalist rental equipment provider in Europe. The group was formed in 1977 as Pierre Boels B.V. by Pierre Boels Sr. It is a family-owned, conservatively managed, and diversified regional market leader, which has over 7,600 unique rental products, serves 260,000 customers across a fleet of 790,000 units, and has a presence in 18 countries across Europe.

As of end-2021, the group generated revenue of about € 1.3 billion, almost double the reported 2019 revenue of €651 million--supported by the integration of Cramo--and adjusted EBITDA of approximately €475 million, with an adjusted EBITDA margin of 36.4%.

The group, through its subsidiaries, leases machinery and equipment for construction, gardening, lifting, and material handling, drilling, and breaking, among other industries. As of end-2021, Boels had diversified exposure to the following end markets: construction (42%); industrial and service activities (26%); small to midsize enterprises and consumer (24%); and other segments (8%).

Boels is family owned, with Pierre Boels as its sole shareholder.

Our Base-Case Scenario

Assumptions

- Eurozone GDP growth of 3.1% in 2022 and 0.3% in 2023. We expect the Netherlands to grow by 4.3% in 2022 and by 0.2% in 2023. We expect Germany to see GDP growth of 1.5% in 2022 followed by negative growth of 0.3% in 2023, and Belgium to grow by 2.4% in 2022 and by 0.4% in 2023. In the Nordics, we expect Boels will continue to benefit from a positive economic environment, with GDP increasing by 2.8%-2.4% in Sweden in 2022-2023, and in 2022 in Finland by 1.7%.
- About 10% revenue increase in 2022 as result of full recovery in the equipment rental market following the COVID-19 pandemic. For 2023, as result of the deteriorated macroeconomic environment in major EU countries, we expect lower growth of 3%-4% on the prospect of a slow rental-equipment market.
- Adjusted EBITDA margin of about 36.5% in 2022 and back to about 38% in 2023, reflecting input cost increases linked to energy, staff, and spare parts for equipment negatively affecting final year results in 2022, but partially easing over the next year.
- Annual capex of about €450 million in 2022 as the group fully seizes investment opportunities from the market recovery in 2022. We expect capex to return to normal levels in 2023, at about €350 million.
- Working capital inflow of about €10 million in 2022.
- No dividends.

Key metrics

Boels Topholding B.V.--Key Metrics*

	--Fiscal year ended Dec. 31--				
Mil. €	**2019a**	**2020a**	**2021a**	**2022f**	**2023f**
Revenue	651.6	1171	1303.7	1,425-1,450	1,475-1,495
Revenue growth (%)	12.6	79.7	11.3	8-11	3-4
EBITDA margin (%)	36.6	34.8	36.4	36.4-36.8	37-38
Funds from operations (FFO)	211.2	298.4	370.8	425-445	445-465
Capital expenditure	307.7	206.5	354.5	445-455	345-355
Free operating cash flow (FOCF)	(127.4)	69	34.8	(20)-(10)	100-110
Debt to EBITDA (x)	2.7	3.7	3.2	~3.0	3.0-2.5
FFO to debt (%)	33.4	19.6	24.2	25-30	~30

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

Liquidity

We assess Boels' liquidity as adequate. This is based on our expectation that available liquidity sources, including cash and FFO, will cover expected cash outflows by more than 1.2x over the 12-month period starting Sept. 30, 2022. Moreover, we anticipate that liquidity sources would cover liquidity uses even if EBITDA were to decline by 15%.

Boels will benefit from its long-dated term debt maturity profile. Its €200 million RCF matures in 2026, followed by the next significant maturity of its €1,450 million term loan B in 2027.

Principal liquidity sources

- Cash and liquid investments of about €18 million
- Positive cash FFO of about €395 million
- Undrawn RCF of €200 million

Principal liquidity uses

- Working capital outflows of about €10 million
- Capex of about €370 million
- No dividends

Covenants

Requirements

Boels' term loan has a covenant stipulating that the company should ensure total net leverage does not exceed 6.5x.

Compliance expectations

In our view, the covenant provides significant headroom, and we do not expect any breach of the covenant in the next two years.

Environmental, Social, And Governance

ESG credit indicators: E-2, S-2, G-2

Environmental, social, and governance factors are an overall neutral consideration in our credit rating analysis of Boels and its subsidiaries. Boels leases machinery and equipment for construction, gardening, lifting and material handling, drilling, and breaking, among other industries. It is present in 18 European countries and well-diversified by end market, with a fleet of more than 790,000 pieces of equipment. In our view, Boels can comfortably afford to invest in a new fleet to meet rising demand from its customers for more environmentally sustainable rental equipment.

Issue Ratings - Recovery Analysis

Key analytical factors

- Recovery rating of '3' and an issue rating of 'BB' to the €1,450 million term loan B, based on our expectation of meaningful recovery prospects at 50%-70% (rounded estimate: 55%) in the event of default.
- In our hypothetical default scenario, we assume an overall negative business landscape, a rise in competition leading to market share losses, and an inability to effectively reduce costs.
- We continue to analyze the company's recovery prospects on a going-concern basis because we think it would likely restructure in a default scenario, instead of being liquidated. We base this on a customer shift to a new rental model, rather than ownership; the company's strong position in the European market; and its flexibility in managing the size of its fleet and product offerings.

Simulated default assumptions

- Year: 2027

- Jurisdiction: Netherlands

Simplified waterfall

- Gross enterprise value: €1,012 million
- Net enterprise value after 5% administrative expenses: €961.4 million
- Total first-lien debt: €1.7 billion
- Expected recovery of first-lien debt: 50%-70% (rounded estimate: 55%)
- Implied recovery rating: 3

All debt amounts include six months of prepetition interest accrued and assume the RCF is 85% drawn.

Ratings Score Snapshot

Issuer credit rating	BB/Stable/--
Business risk:	Fair
Country risk	Very low
Industry risk	Intermediate
Competitive position	Fair
Financial risk:	Significant
Cash flow/leverage	Significant
Anchor	bb
Modifiers:	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile:	bb

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: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016

- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- 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

- Finland-Based Rental Equipment Company Renta Group Assigned 'B' Rating; Outlook Stable, Oct. 19, 2022
- Boels Topholding B.V., July 8, 2022
- French Rental Equipment Group Kiloutou Upgraded To 'B+' On Performance Recovery And Acquisition Of GSV; Outlook Stable, May 23, 2022
- French Rental Equipment Group Loxam Upgraded To 'BB-' From 'B+' On Performance Recovery; Outlook Stable, April 20, 2022
- Cost Discipline And Flexible Capex Keep Cash Flows Healthy For European Equipment Rental Companies, Oct. 13, 2021

Ratings List

Upgraded

	To	From
Boels Topholding B.V.		
Issuer Credit Rating	BB/Stable/--	BB-/Stable/--
Senior Secured	BB	BB-
Recovery Rating	3(55%)	3(50%)