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Research Update:

Media Group Cyfrowy Polsat And Subsidiary Metelem Upgraded To 'BB+' On Expected Debt Refinancing; Outlook Stable

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Overview

- Cyfrowy Polsat S.A. plans to fully refinance its debt by January 2016 with a Polish zloty (PLN) 11.5 billion senior facility agreement and a PLN1.0 billion revolving credit facility.
- Following the refinancing, we expect Cyfrowy's capital structure will significantly improve, with adjusted debt to EBITDA gradually decreasing to less than 3.0x.
- We are therefore upgrading Cyfrowy and its core subsidiary Metelem Holding Company Ltd. to 'BB+' from 'BB'.
- Our stable outlook reflects our view that both entities will successfully defend their market position and maintain credit metrics commensurate with the rating.

Rating Action

On Sept. 25, 2015, Standard & Poor's Ratings Services raised its long-term corporate credit ratings on Polish media group Cyfrowy Polsat S.A. and its core subsidiary, wireless telecommunications company Metelem Holding Company Ltd., to 'BB+' from 'BB'. We removed the ratings from Creditwatch, where they were placed with positive implications on April 30, 2015. The outlook is stable.

At the same time, we raised our issue rating on Cyfrowy's Polish zloty (PLN) 2.5 billion term loan and PLN500 million senior secured revolving credit facility (RCF) to 'BB+' from 'BB', and withdrew them at the issuer's request, because Cyfrowy will refinance this debt on Sept. 28, 2015.

We have also raised our issue rating on the €542.5 million and US\$500 million high-yield bonds issued by Eileme 2 AB, Metelem's financing vehicle, to 'BB-' from 'B+' previously.

Rationale

We upgraded Cyfrowy because on Sept. 21, 2015, the group signed documentation to refinance its existing debt with a new secured PLN11.5 billion (about US\$3.0 billion) senior facility agreement (SFA) and a secured PLN 1.0 billion (about US\$0.3 billion) RCF. We expect that after the refinancing, which will be gradually executed and finalized by January 2016, Cyfrowy's capital

structure will significantly improve. In particular, we assume the following benefits:

- Cyfrowy will receive access to its core subsidiary Metelem's cash flows because the restrictions imposed by the existing debt documentation will be removed. Importantly, after the refinancing is fully finalized, Cyfrowy and Metelem's subsidiary Polkomtel will have a joint credit pool.
- Debt-related currency risk, a key rating constraint so far, will be removed since the new financing will be in the local currency, unlike the existing structure, which is partly denominated in euros and U.S. dollars. We are mindful of potential currency fluctuations within the next three months until the euro- and U.S. dollar-denominated high-yield bonds are redeemed; that said, we take into view that the exchange rate risk related to coupon on these bonds is mitigated by hedging agreements. We also understand that the group is now looking into options to mitigate exchange rate risk related to the principal amount.
- The cost of debt reduction (given a 3.6% blended interest rate after the refinancing versus 6.6% currently) will strengthen Cyfrowy's credit metrics. Furthermore, the margin on the new financing will step down depending on the group's leverage, which in our base case should gradually improve.

The upgrade of Metelem reflects our assessment of its status as a "core" subsidiary of Cyfrowy, which acquired the telecoms company in May 2014. In our view, the refinancing structure, creating a single credit pool, affirms our view of Metelem as a "core" group entity. We assess the stand-alone credit profile of Metelem at 'bb'. As per our criteria for rating groups, we equalize our corporate credit rating on Metelem with the 'bb+' group credit profile of the parent.

We continue to assess Cyfrowy's business risk profile as "satisfactory," supported by the group's diversity and scale, which materially increased after the Metelem acquisition as a result of combining Poland's largest direct-to-home pay-TV and mobile telecoms operators. The group benefits from Poland's largest--and Europe's fourth-largest--satellite platform and the highest long-term evolution (LTE) network coverage of 90% of Poland's population. After consolidating Metelem's operations, the group has become the leader in the pay-TV market, the contract segment of the mobile market, and the TV market in Poland. Furthermore, the group implements a multiplay strategy, which we anticipate will be successful in rural areas where there is limited availability of cable and fixed broadband. We view this as supportive of the group's above-average profitability, with an adjusted EBITDA margin (pro forma the acquisition) of 42.6% in 2014 and slightly above 42% in the first half of 2015.

These strengths are mitigated by the concentration of the group's operations in a single country, Poland, and by pronounced competition, notably in the mobile market, which, in our view, results in continued price pressure. We also noted a marginal weakening of Cyfrowy's EBITDA margin in the first half of 2015, which is largely the result of higher data-transmission costs in the mobile segment due to an increase in the number of mobile Internet service

users.

Cyfrowy's "significant" financial risk profile continues to reflect our view that the group had sizable debt of PLN13.9 billion at year-end 2014 and PLN13.7 billion as of June 30, 2015 (Standard & Poor's adjusted), which translates into adjusted debt to EBITDA of 3.2x. As most of debt is currently located at Metelem's level, we continue to assess Metelem's financial risk profile as "aggressive," primarily reflecting its still-meaningful debt burden and the high interest on its unsecured debt. That said, we understand that after the refinancing the cost of debt will decrease and Metelem will be part of a joint credit pool.

Under our base-case scenario for the Cyfrowy group (excluding the contemplated refinancing), we assume:

- GDP growth in Poland of 3.0% in 2015 and 3.3% in 2016;
- About PLN3.2 billion in revenues from Cyfrowy's retail and TV broadcasting segments;
- A 1%-2% revenue decline for Polkomtel in 2015-2016;
- Cost synergies supporting Cyfrowy's adjusted EBITDA margin at approximately 42%-43% in 2015-2016;
- A ratio of capital expenditures (capex) to revenues of about 8% in 2015 and 10%-11% from 2016 on; and
- Moderate dividends payout starting from 2017.

Based on these assumptions, we arrive at the following credit measures:

- Adjusted funds from operations (FFO) to debt of about 22%-25% in 2015-2016, broadly in line with 2014.
- An adjusted debt-to-EBITDA ratio of about 3.2x in 2015, down from about 3.4x in 2014, further improving in 2016.

Liquidity

We view Cyfrowy Polsat's liquidity on a pro forma basis (including Polkomtel) as "adequate" under our criteria, and we calculate that liquidity sources should exceed liquidity needs by around 1.2x over the next 12 months starting as of June 30, 2015 (pro forma the refinancing).

We calculate Cyfrowy Polsat's main sources of liquidity over the next 12 months as:

- Cash and cash equivalents of about PLN1.3 billion;
- New money from the refinancing of PLN11.5 billion and a RCF of PLN1.0 billion; and
- FFO of about PLN2.6 billion.

Over the same period, we calculate the following uses of liquidity:

- Working capital outflows of about PLN300 million;
 - Capex of about PLN900 million; and
- Debt amortization payments of about PLN12.2 billion (including around PLN0.6 billion scheduled repayments of the New SFA) related to the refinancing.

We also take into view that in August 2015 Cyfrowy issued PLN1.0 billion in

unsecured bonds which it fully used to prepay its SFA.

Furthermore, we believe that headroom under Cyfrowy's maintenance covenants in the new financing package will remain adequate over the medium term, even if EBITDA were to decline by 15%.

Outlook

The stable outlook reflects our view that Cyfrowy and Metelem will successfully defend their market positions. Also, we expect that, after finalizing the planned refinancing, Cyfrowy will be able to maintain credit metrics commensurate with the rating, such as an adjusted ratio of debt to EBITDA of 3.0x-3.5x.

Upside scenario

We could raise the rating if Cyfrowy achieves adjusted debt to EBITDA of less than 3x and adjusted free operating cash flow to debt of at least 15%, both on a sustainable basis.

Downside scenario

We could consider a negative rating action if weaker operating performance results in a weakening of Cyfrowy's credit metrics or liquidity position.

Ratings Score Snapshot

Cyfrowy Polsat S.A.

Corporate Credit Rating: BB+/Stable/--

Business risk: Satisfactory

- Country risk: Moderately High
- Industry risk: Intermediate
- Competitive position: Satisfactory

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: bb+

Modifiers

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

Metelem Holding Company Ltd.
Corporate Credit Rating: BB+/Stable/--

Business risk: Satisfactory

- Country risk: Moderately high
- Industry risk: Intermediate
- Competitive position: Satisfactory

Financial risk: Aggressive

- Cash flow/Leverage: Aggressive

Anchor: bb

Modifiers

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

Stand-alone credit profile: bb

- Group credit profile: bb+
- Entity status within group: Core (equal to group credit profile)

Related Criteria And Research

Related Criteria

- Country Risk Assessment Methodology And Assumptions - November 19, 2013
- Methodology: Industry Risk - November 19, 2013
- 2008 Corporate Criteria: Rating Each Issue - April 15, 2008
- Use Of CreditWatch And Outlooks - September 14, 2009
- Industrials: Key Credit Factors For The Telecommunications And Cable Industry - June 22, 2014
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- Corporate Methodology: Ratios And Adjustments - November 19, 2013
- Group Rating Methodology - November 19, 2013
- Criteria - Corporates - General: Corporate Methodology - November 19, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13, 2012

Ratings List

Upgraded; CreditWatch/Outlook Action

To

From

Cyfrowy Polsat S.A.		
Corporate Credit Rating	BB+/Stable/--	BB/Watch Pos/--
Senior Secured	BB+	BB/Watch Pos

Eileme 1 AB		
Metelem Holding Company Ltd.		
Corporate Credit Rating	BB+/Stable/--	BB/Watch Pos/--

Eileme 2 AB		
Corporate Credit Rating	BB+/Stable/--	BB/Watch Pos/--
Senior Unsecured	BB-	B+/Watch Pos

Ratings subsequently withdrawn		
Cyfrowy Polsat S.A.		
Senior Secured	BB+	BB/Watch Pos

Eileme 1 AB		
Corporate Credit Rating	BB+/Stable/--	BB/Watch Pos/--

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