S&P Global Ratings

Research

Research Update:

Packaging Group Huhtamaki Oyj Outlook Revised To Positive On Sustained Improvement In Credit Metrics; Affirmed At 'BB+'

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Rating Action Overview

- Finland-based packaging company Huhtamaki met our upgrade triggers in 2023 with S&P Global Ratings-adjusted debt to EBITDA of 2.4x (2.7x in 2022) and funds from operations (FFO) to debt at 31.4% (30.6% in 2022).
- We expect Huhtamaki will achieve similar credit metrics in 2024 and a slight improvement for 2025.
- We therefore revised the outlook on Huhtamaki to positive from stable and affirmed our 'BB+' long-term issuer rating on the company as well as our 'BB+' issue rating on the company's unsecured notes due 2027 and 2028.
- The positive outlook reflects the potential for an upgrade in the next 12 months if adjusted debt to EBITDA remains below 2.5x and FFO to debt remains above 30%, supported by the group's operating performance and financial policy.

Rating Action Rationale

We expect Huhtamaki's 2024 credit metrics to remain in line with our upgrade triggers, which the company met in 2023. Last year Huhtamaki achieved S&P Global Ratings-adjusted debt to EBITDA of 2.4x, compared with 2.7x in 2022, and its funds from operations (FFO) to debt reached 31.4% from 30.6% in 2022. These metrics, alongside positive discretionary cash flow (DCF) of €155 million, are in line with our upgrade triggers. The improvement stemmed from a substantial working capital inflow of €144 million (after a €161 million outflow in 2022), even though adjusted EBITDA declined slightly in 2023 due mainly to lower volumes. Unless the recovery in demand is slower than expected--which we cannot rule out--we expect adjusted debt to EBITDA and FFO to debt to remain at similar levels in 2024, at 2.3x and 32%, respectively.

We forecast free operating cash flow (FOCF) of about €126 million in 2024, versus €260 million in 2023. Last year's FOCF was supported by a sizable working capital inflow on the back of raw material price decreases. We estimate that working capital will stabilize and that there will be a €30 million outflow in 2024. The resulting reduction in FOCF in 2024 is, in our view, a more sustainable level.

We project that Huhtamaki's reported leverage is likely to remain at the lower end of its 2.0x-3.0x target range. This corresponds to S&P Global Ratings-adjusted 2.2x-3.2x. We think that any increase in reported leverage beyond 3.0x (in the case of, for example, a large debt-funded acquisition) would only be temporary and that Huhtamaki would seek to revert credit metrics to levels commensurate with an investment grade rating in a timely manner.

Currently, Huhtamaki's near-term maturities do not affect our adequate assessment of the company's liquidity. We assume Huhtamaki will successfully refinance upcoming debt maturities in a timely manner. These maturities include a €100 million bond due October 2024, a €125 million term loan due May 2025, and a €175 million bond due November 2026. Further ahead Huhtamaki will meet its €500 million notes due in 2027. We will exclude the €400 million revolving credit facility (RCF) due January 2026 from our liquidity calculations (as a liquidity source) from January 2025 onwards.

Outlook

The positive outlook reflects the potential for an upgrade over the next 12 months if Huhtamaki's operating performance and financial policy support adjusted debt to EBITDA remaining below 2.5x and FFO to debt above 30%.

Upside scenario

We could raise our ratings if:

- Huhtamaki's financial policy and track record help adjusted debt to EBITDA remain below 2.5x and FFO to debt above 30% on a sustained basis;
- We expected a sustained gradual improvement in EBITDA margins and FOCF; and
- The group successfully refinances the debt maturing in 2024 and 2025 (including the RCF).

Downside scenario

We could revise our outlook to stable if:

- The group's operating performance is weaker than expected or the company pursues a more aggressive financial policy that results in adjusted net debt to EBITDA exceeding 2.5x and FFO to debt falling below 30% without any expectation of improvement; or
- Our liquidity or capital structure assessment weakened due, for example, to the lack of a timely refinancing of the company's RCF or a short-term weighted capital structure.

Company Description

Huhtamaki is a Finland-based provider of packaging for food and consumer products. The products target several end-markets: quick service restaurants, food delivery, fast moving consumer goods, and retail. Sales are equally split between food-on-the-go and food-on-the-shelf. The company reported revenue of €4.2 billion and S&P Global Ratings-adjusted EBITDA of €578 million in 2023. The group is publicly listed on the Nasdaq Helsinki.

Huhtamaki operates through the following segments: fiber packaging and foodservice in Europe, Asia, and Oceania; North America; and flexible packaging. Each of the three segments accounts for about one-third of sales. In 2023, sales were split between the U.S. (39%), Germany (11%), the U.K. (8%), and India (6%); all other countries accounted for less than 5% of sales individually in 2023. Huhtamaki's main raw materials are paperboard, recycled fiber, and plastic resins.

Our Base-Case Scenario

Assumptions

- About 1% growth in 2024 as slightly higher volumes (mainly in the second half of the year) offset somewhat lower average selling prices (reflecting the passthrough of lower raw material prices in 2023). In 2025 we assume that improved demand leads to 3% growth while selling prices remain broadly stable.
- In 2024, S&P Global Ratings-adjusted EBITDA margin of about 13.8% (13.9% in 2023) as the benefits from slightly higher volumes and cost-savings are offset by efficiency program costs. In 2025, we estimate an improvement in adjusted EBITDA margins towards 14% supported by a recovery in volumes and cost efficiencies.
- We expect capital expenditure (capex) at €280 million in 2024 with roughly €80 million relating to maintenance and €200 million for growth initiatives mainly in the U.S. We forecast about €320 million capex for 2025, when we anticipate similar growth initiatives.
- A €30 million working capital outflow per year in 2024-2025 reflecting volume growth and some inventories increase due to the ramp-up of new production facilities.
- Dividends of €110 million in 2024 and €112 million in 2025, in line with the company's target payout ratio of 40%-50%.

Key metrics

Huhtamäki Oyj--Forecast summary

	--Fiscal year ends Dec. 31-						
(Mil. €)	**2019a**	**2020a**	**2021a**	**2022a**	**2023a**	**2024f**	**2025f**
Revenue	3399	3302	3575	4479	4169	4201	4328
EBITDA (reported)	449	465	470	615	621	570	597
Plus/(less): Other	2.9	10.0	(9.2)	(31.7)	(43.6)	10.0	10.0

Huhtamäki Oyj--Forecast summary (cont.)

	--Fiscal year ends Dec. 31-						
(Mil. €)	2019a	2020a	2021a	2022a	2023a	2024f	2025f
EBITDA	452	475	461	583	578	580	607
Less: Cash interest paid	23	23	25	36	59	64	61
Less: Cash taxes paid	39	45	83	71	84	81	76
Funds from operations (FFO)	390	406	352	476	435	435	470
Capital expenditure (capex)	204	224	259	319	319	280	320
Free operating cash flow (FOCF)	222.5	205.1	(36.7)	2.9	259.5	125.5	119.8
Dividends	88	93	96	98	105	110	112
Discretionary cash flow (DCF)	135	112	(147.8)	(95.2)	155	16	8
Debt (reported)	957	1012	1509	1617	1493	1317	1317
Plus: Lease liabilities debt	164	154	176	159	161	163	165
Plus: Pension and other postretirement debt	142	141	104	71	78	78	78
Less: Accessible cash and liquid investments	199	305	179	309	348	198	189
Debt	1063	1029	1628	1558	1384	1360	1371
Adjusted ratios							
Debt/EBITDA (x)	2.4	2.2	3.5	2.7	2.4	2.3	2.3
FFO/debt (%)	36.7	39.5	21.6	30.6	31.4	32.0	34.3
FFO cash interest coverage (x)	18.2	18.4	14.9	14.2	8.4	7.8	8.6
EBITDA interest coverage (x)	20.0	17.3	18.3	15.0	7.5	8.8	9.5
FOCF/debt (%)	20.9	19.9	(2.3)	0.2	18.7	9.2	8.7
DCF/debt (%)	12.7	10.9	(9.1)	(6.1)	11.2	1.2	0.6
Annual revenue growth (%)	9.5	(2.9)	8.3	25.3	(6.9)	0.8	3.0
EBITDA margin (%)	13.3	14.4	12.9	13.0	13.9	13.8	14.0

All figures are adjusted by S&P Global Ratings, unless stated as reported. a--Actual. e--Estimate. f--Forecast.

Liquidity

We assess Huhtamaki's liquidity as adequate and expect liquidity sources to cover liquidity uses by more than 1.2x in the 12 months ending June 30, 2025. Our view is supported by €353 million available under the RCF, our forecast for FFO, and cash available on the balance sheet. Our assessment is somewhat constrained by sizable debt maturities.

From January 2025 on, we will not consider the €400 million RCF due January 2026 as a liquidity source in our calculations. All things being equal, this would lead us to negatively reassess the company's liquidity profile.

Principal liquidity sources as of July 1, 2024, for the subsequent 12 months include:

- Available cash of €300 million;
- €353 million available under the €400 million RCF maturing in January 2026; and

- Cash FFO of about €435 million.

Principal liquidity uses for the same period include:

- Capex of €300 million;
- Debt maturities and amortization of about €280 million;
- Working capital-related outflows of €40 million (including seasonal needs); and
- A €110 million dividend payment.

Covenants

Huhtamaki's €400 million multi-currency RCF is subject to a 3.75x net leverage covenant (tested quarterly). We forecast the company will have sufficient headroom under this covenant for the next 12 months.

Environmental, Social, And Governance

Environmental, social, and governance (ESG) factors are an overall neutral consideration in our credit rating analysis of Huhtamaki. Since two-thirds of its packaging is sustainably sourced and recyclable, we see the company's exposure to environmental and social risks as comparable with the broader industry. However, about one-third of Huhtamaki's production is plastic resin-based, and we view plastic packaging companies with single-use or single-serve applications as exposed to substitution risk from other substrates. As a producer of single-use plastic products that are under scrutiny, the company may be subject to future restrictive policies and regulations.

Issue Ratings - Recovery Analysis

Key analytical factors

- Our issue rating on the €500 million unsecured sustainability-linked notes due 2027 and the €300 million senior unsecured notes due 2028 is 'BB+'. The '3' recovery rating reflects our expectations of meaningful recovery prospects (50%-70%; rounded estimate: 65%) in the event of a default.
- The issue rating is supported by the limited amount of prior ranking debt, but constrained by the large amount of pari passu debt and the unsecured nature of the notes.
- Under our hypothetical default scenario, we assume rising raw material costs that the group is not able to pass on to customers or a seismic shift by customers to different packaging solutions.
- We value the group as a going concern, given its entrenched relationships with suppliers and clients, global footprint, presence in molded fiber, food service and flexible packaging, and innovation in sustainable solutions.

Simulated default assumptions

- Year of default: 2029
- Jurisdiction: Finland
- Emergence EBITDA: €242 million
- Implied enterprise value multiple: 6.0x

Simplified waterfall

- Gross enterprise value: €1,453 million
- Net recovery value for waterfall, after 5% admin. expenses: €1,380 million
- Total first-lien debt: €524 million
- Value available to unsecured debtholders: €856 million
- Total unsecured claims: €1,249 million
- Recovery expectations: 50%-70% (rounded estimate: 65%)
- Recovery rating: 3

Ratings Score Snapshot

Foreign currency issuer credit rating	BB+/Positive/--
Local currency issuer credit rating	BB+/Positive/--
Business risk	Satisfactory
Country risk	Low
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)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Neutral (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	bb+

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- 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
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Outlook Action; Ratings Affirmed

	To	From
Huhtamaki Oyj		
Issuer Credit Rating	BB+/Positive/--	BB+/Stable/--
Senior Unsecured	BB+	BB+
Recovery Rating	3(65%)	3(60%)

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.spglobal.com/ratings for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/sourceId/504352. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings. Alternatively, call S&P Global Ratings' Global Client Support line (44) 20-7176-7176.