S&P Global
Ratings

RatingsDirect®

Summary:
Hibu Midco Limited

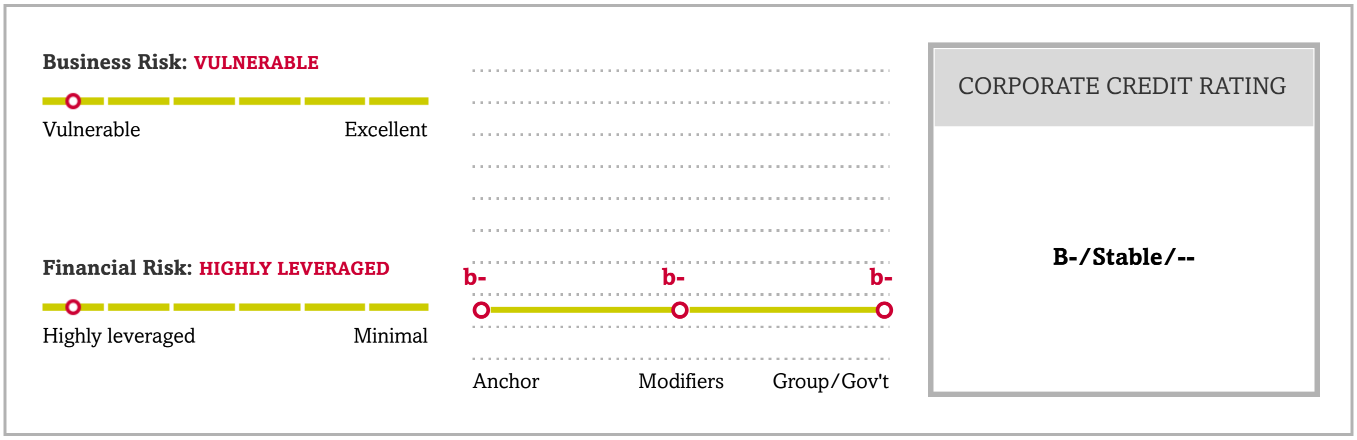
Primary Credit Analyst:
Mathieu Magaud, Paris +33 (0) 1 4420 6652; mathieu.magaud@spglobal.com

Secondary Contact:
Florence Devevey, Paris (34) 91-788-7236; florence.devevey@spglobal.com

Table Of Contents

Summary:

Hibu Midco Limited



Rationale

Business Risk: Vulnerable	Financial Risk: Highly leveraged
• Digital transformation not yet completed, together with declining printing and digital directories revenues. • Highly competitive and fragmented digital marketing services market. • Fair geographic diversification.	• Relatively low adjusted leverage, but highly volatile industry. • Positive free operating cash flow (FOCF).

Outlook: Stable

The stable outlook on Hibu Group Midco Limited (Hibu) reflects our expectation that the company will continue to progressively shift its business model toward a pure digital marketing services company. We also expect the company to maintain adequate liquidity over the next 12 months, thanks to positive and stable FOCF, an absence of short-term maturities, and adequate covenant headroom.

Upside scenario

A positive rating action would hinge on strengthening of the group's operations, such as we observed top-line and EBITDA growth stabilizing. It could also come from improvement in credit metrics, such as adjusted debt to EBITDA sustainably and comfortably below 3x.

Downside scenario

We could lower the rating if group's transformation is delayed, resulting in a prolonged deterioration in EBITDA beyond our expectation and leading to downward pressure on FOCF and an unsustainable capital structure. We would also view liquidity deterioration and an increasing risk of a debt restructuring that we would treat as tantamount to default as drivers for a downgrade.

Our Base-Case Scenario

Assumptions

- U.K. GDP growth of 1.4% in 2017 and 0.9% in 2018 and U.S. GDP growth of 2.2% in 2017 and 2.3% in 2018, underpinning the demand for digital services.
- Secular decline in the printing and digital directory industry; hence, we believe that part of Hibu's operation is delinked from GDP movement. A decline in revenues of 5%-10% in fiscal 2018 (ending March 30, 2018) and fiscal 2019 from £732.3 million generated in fiscal 2017, owing to weakening demand in printing and digital directories. This is only partially offset by growing demand for digital services. Indeed, we forecast Hibu's digital marketing segment to grow by 3%-5% over the same period.
- A decline in the adjusted EBITDA margin to about 25% on average in fiscal 2018 and fiscal 2019 from 29% in fiscal 2017 after restructuring costs primarily driven by revenue declines. We estimate Hibu will generate adjusted EBITDA of £160 million-£165 million in fiscal 2018 from more than £200 million in fiscal 2017.
- Working capital outflow of £15 million-£20 million in fiscal 2018, mainly coming from a legacy management incentive plan paid in the first quarter of fiscal 2018. We also believe that the group's working capital needs will increase as the company moves from an incumbent paper directory player--with payments booked and received well in advance---to a digital marketing services company with less favorable payment terms.
- Capital expenditures of £14 million-£15 million annually, translating into 2.2% of sales. The relatively low percentage compared with peers reflects our understanding that Hibu has chosen to outsource product and service, differentiating it from some of its peers that have chosen to keep these activities in house.

Key Metrics

	2017*	2018f	2019f
Revenues growth (%)	(8.1)	(5-10)	(5-10)
EBITDA margin (%)	28.5	24-25	24-25
Debt to EBITDA (x)	2.6	2.5-3.0	3.0-3.5

*Fiscal year. f--forecast.

Business Risk: Vulnerable

Hibu is a publisher of print and digital directories in the U.K. (Yellow Pages), in the U.S. (Yellow Book), and offers digital marketing services to small and midsize enterprises. The group focuses now essentially on the development of its digital solution, which is growing year on year.

As of year-end of fiscal 2017, printing and digital directories activities still represented 60% of Hibu's revenues. In our view, this is a declining business model. Indeed, people-finding and gathering and sorting information has radically evolved in the past few years, with the emergence of many online players. Printing and digital directories operations contributed negatively to the group's top line by 16% in fiscal 2017. The remaining 40% of the group's sales come from its digital solution offering to small and midsize enterprises, which we view as positive but still subject to high online competition, to the dominance of Google and Facebook in particular, and to somewhat limited barriers to entry.

We understand the company is still in the process of completing its digital transformation with the aim to operate solely as a provider of digital marketing services to local businesses. In September, the company announced it will exit its U.K. print directory business during fiscal 2019. We believe that margins will remain under pressure and will not recover to the historical level of 28.5% in 2017, given Hibu's transition to the highly fragmented, intensely competitive, and rapidly evolving online market. We believe that in its online business, Hibu will have significantly less pricing power than it had in its former leading or incumbent positions in the traditional classified directories business.

Financial Risk: Highly leveraged

We project that Hibu will maintain an about 3x debt-to-EBITDA ratio over the next two years on average, along with positive FOCF generation.

However, our assessment of Hibu's financial risk profile primarily reflects our view of the directory publishing industry as highly volatile, reflecting the risk that Hibu's capital structure could quickly become unsustainable if negative business trends accelerate, leading to quick deterioration in earnings, cash flow, and credit metrics.

Liquidity: Adequate

We assess Hibu's liquidity as adequate. We calculate that the ratio of sources to uses of liquidity will remain over 1.2x over the next 12 months. However, we also incorporate in our assessment our view of the group's low standing in credit markets, due to the group's history of debt restructuring and likelihood of the company not being able to absorb low-probability adversities.

Principal Liquidity Sources	Principal Liquidity Uses
• Cash on the balance sheet of about £62 million; and • Reported funds from operations of about £100 million	• About £15 million of capital expenditures; • Debt repayment of about £36 million using excess cash from the cash sweep mechanism; and • About £20 million of working capital outflow, of which £5 million is intra year.

Covenant Analysis

The group has one maintenance covenant under its cash paid facility agreement, which include a maximum net debt-to-EBITDA ratio of 4x. The covenant has comfortable headroom of more than 15% as of June 30, 2017, and thereafter.

Ratings Score Snapshot

Corporate Credit Rating

B-/Stable/--

Business risk: Vulnerable

- **Country risk:** Low
- **Industry risk:** Intermediate
- **Competitive position:** Vulnerable

Financial risk: Highly leveraged

- **Cash flow/Leverage:** Highly leveraged

Anchor: b-

Modifiers

- **Diversification/Portfolio effect:** Neutral
- **Capital structure:** Neutral
- **Financial policy:** Neutral
- **Liquidity:** Adequate
- **Management and governance:** Fair
- **Comparable rating analysis:** Neutral

Stand-alone credit profile : b-

Issue Ratings

Recovery Analysis

Key Analytical Factors

- The £300 million (of which £235 million is outstanding as of June, 30 2017) senior secured term loan is rated 'B-' with a '4' recovery rating. This reflects our expectations of average recovery (30%-50%: rounded estimate 30%). The recovery rating is supported by limited prior-ranking debt, but constrained by the weak security package, given the asset-light nature of the business.
- The £250 million (of which £223 million is outstanding as of June, 30 2017) subordinated payment-in-kind loan is rated 'CCC' with a '6' recovery rating. This reflects our expectations of negligible recovery (0%-10%; rounded estimate: 0%). The recovery rating reflects its subordination to the senior secured term loan.
- Our default scenario assumes increased competition from online marketing channels and the continuous structural

decline in directories.
- We value Hibu using discrete asset valuation, as we assume that the company would be liquidated rather than sold as a going concern in a hypothetical default scenario.

Simulated Default Assumptions

- Year of default: 2019
- Jurisdiction: U.K.

Simplified Waterfall

- Gross enterprise value at default: £102 million
- Net enterprise value after administrative costs (5%): £97 million
- Estimated senior secured claims: £315 million
- Value available for senior secured claims: £97 million
- Recovery rating: 4 (30%-50%; rounded estimate 30%)
- Estimated subordinated debt claims: £350 million
- Value available for subordinated debt claims: Zero
- Recovery Rating: 6 (0%-10%; rounded estimate 0%)

*All debt amounts include six months of prepetition interest.

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- 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
- Criteria - Corporates - General: The Treatment Of Non-Common Equity Financing In Nonfinancial Corporate Entities, April 29, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Media And Entertainment Industry, Dec. 24, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	Intermediate	Significant	Aggressive	**Highly leveraged**
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	bb+	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	**b-**

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@spglobal.com