ISSUER RATING

Long-term Rating

BBB-

Outlook: Stable

First rating date: 25/04/2023

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Rating Action and rationale

- EthiFinance Ratings assigns for the first time a "BBB-" rating with a Stable outlook to Grupo Squirrel Media.
- The company presents an adequate economic-financial structure, highlighting the favourable evolution of its business, results, operating cash generation and maintenance of a balanced financial profile. However, it is in a stage of expansion, both organically and inorganically, having increased leverage levels in recent years, all as a result of the investment policy and M&A operations carried out. In this sense, a continuation and further progress in the consolidation of this growth is important to favour an improvement in its positioning and scale in the market (more limited in relation to other large players) as well as the operational and geographical diversification of its income.
- In line with our new methodology, the Media and Entertainment sector presents a medium-low risk in terms of ESG (heatmap sector between 2 and 2.9) given its impact on the environment. This valuation results in a sectoral analysis that is not affected by this factor. On the other hand, the company's ESG policies are considered neutral (the company's ESG score between 1 and 4), resulting in a rating that is not impacted by these factors.
- Although complete financial projections (balance sheet, income statement and cash flow) have been prepared and analysed for the period 2023-2024, these are not reflected in the report at the request of the company.

Issuer description

Squirrel Media is a technology group located within the Media and Entertainment sector that focuses its activity on four main business sectors: **i) Advertising**, with two agencies mainly that carry out, among other activities, marketing strategies for large clients as well as media advertising, **ii) Content**, with the production and distribution of audio-visual content that is also acquired from large independent production companies for subsequent use in different windows (Cinemas, DVD, VOD or TV), **iii) Media**, where it is observed that it has several free-to-air television channels (third private free-to-air TV operator in Spain) as well as on pay platforms, and **iv) Technology (TMT),** highlighting broadcasting services, retransmission of live events, two teleports and Technological support to the group. Since 2020, with the integration that the group had in Vértice 360º (reverse merger by which total control remained in the hands of Squirrel), a new approach to the business model is being carried out, developing an expansion strategy that is favourable to a more operationally and geographically diversified activity. The group had an average workforce of 177 employees in 2022, having achieved sales and EBITDA of €80MM and €13.5MM respectively, with an NFD/EBITDA ratio in controlled securities of 2.4x (+1.1x compared to 2021). During 2022, the group's share fell 36.2%, placing the market capitalisation at €210.1MM at the end of the year.

Fundamentals

Business Profile

Industry Risk Assesment

- **Highly competitive sector that reflects positive growth prospects for the coming years.** The entertainment and media industry is characterised, in general terms, by presenting low entry barriers (we highlight the necessary knowledge of the market, as well as the importance of the company's reputation and brand for greater business scalability) that lead towards a fragmented market with strong competition. In addition, this sector usually presents positive operating returns with more controlled volatility in times of stress or crisis, with favourable growth rates being estimated for the coming years, which in the case of Spain could reach

€36,000MM by 2026 ($CAGR_{22-26}$ of 5.1%).

On the other hand, given the role and importance it represents, we highlight the plan defined by the Government of Spain for the period 2021-2025 with a planned investment that could reach €1,600MM and that would focus on placing the country in the largest audio-visual Hub in Europe, an aspect that could also strengthen and boost the income of the industry.

- **In line with our new methodology, the Media and Entertainment sector presents a medium-low risk in terms of ESG (heatmap sector between 2 and 2.9) given its impact on the environment.** ESG trends are structural and there are associated business opportunities, however further adaptation is still needed to achieve financial or social benefits from them. On the contrary, low dependencies or negative impacts of ESG factors on stakeholders are expected. This valuation results in a sectoral analysis that is not affected by this factor.

Company's competitive positioning

- **Group that is strengthening its position in the market in recent years supported by its expansion strategy.** The company is immersed in a process of organic and inorganic growth that is strengthening its role in the market and industry as a reference player, with a highly scalable, multi-product and multi-territorial business model. We highlight, as the most significant acquisitions in the last year, the incorporation in January 2022 of Net TV and Veralia Distribución de Cine in the media and content divisions respectively, as well as the last one announced in December 2022 of Grupo Ganga also in the contents sector. With the full integration and consolidation of these new companies, Squirrel will reinforce its scale in the market (more limited at the moment) and will obtain operational synergies that will favour its business.

- **Somewhat more limited operational and geographical diversification that is recently improving with the strategy developed.** Although the advertising sector continues to be Squirrel's main source of income (45.3% at the end of 2022), the M&A operations carried out are improving the group's operational and geographical diversification, with a greater weight achieved for the media segment (34.9% of total income in 2022) and greater growth expected for content after the heavy investment that the company is making with the acquisition of new releases for its exploitation. In addition, although at a geographical level, Spain and Italy are the main markets of the group, 59% and 29% respectively of total income for the first half of 2022 (latest data available), greater diversification by country both in Europe and LATAM is expected given the greatest coverage that their titles or premieres will have at a geographical level (until 2021 they were only shown in Spain and Andorra, from 2023 a reach of more than 30 countries is expected).

  On the other hand, it should be noted that although the company continues to present a high concentration of clients at the end of the first half of 2022 (top 5 and top 10 represent 48.9% and 68.5% respectively), since the impact of the Covid-19 had over its activity, mainly the advertising sector, a portfolio diversification strategy is being carried out that is already reflected in this first half (the top 5 improve by +9.6pp in concentration compared to the end of 2021).

Governance

- **Concentrated shareholding with a management team that has extensive experience in the sector.** At the end of the first half of 2022, Pablo Pereiro is the main shareholder of Squirrel with a 91.97% stake. Despite the fact that concentration on decision-making could pose a risk, we highlight the high level of involvement and long-term permanence of the main shareholder. In addition, although the group's financial capacity to support the group is valued moderately, this is mitigated by the fact that Grupo Squirrel is a listed company (being able to resort to new capital increases on the market, as happened in 2022). Likewise, its main shareholder, board of directors and management of the group stand out for the solid experience reflected (more than 15/20 years on average), being an important aspect to promote the expansion strategy that it is currently developing. In addition, we consider that derived from this expansion policy, a greater reinforcement in the management structure could be necessary in the short/medium term for a better consolidation of the same. Additionally, this growth is being achieved under a conservative financial policy, carrying out M&A operations financed with own funds or an equitable mix between own and financial resources (50%-50%).

- **Neutral ESG policy**. Based on the ESG data analysed and once the methodology has been applied, EthiFinance Ratings values Grupo Squirrel Media's ESG policies as neutral (the company's ESG score between 1 and 4). As a result, the company's rating is not affected by this driver. However, we consider it necessary for the Grupo Squirrel Media to go further and define ESG policies, in accordance with the size it is reaching, since the assessment given in this aspect could be adjusted due to the mandatory nature of a greater definition and transparency at the ESG level.

Financial Profile

Cash-flow and leverage

- **Growing evolution of billing and positive margins generated with the business, driven by the new dimension reached by the group.** Squirrel is presenting a favourable trend for its income in recent years (€80MM in 2022 with a $CAGR_{20\text{-}22}$ of 57.9%) together with a notable increase in EBITDA (€13.5MM in 2022 with a $CAGR_{20\text{-}22}$ of 121.7%), which are being strengthened by the complete integration of all the company's business sectors (reverse merger carried out with Vértice 360º in 2020), as well as by the new corporate acquisitions that are being made. Although in the last year the evolution of its income in the advertising and content sectors continued to be impacted by the uncertainty generated by the pandemic and the war between Russia and Ukraine (the companies postponed their advertising investments for the second half of 2022 and especially 2023), it is highlighted that even so during the year, the company has mitigated this effect due to the inorganic growth achieved. Under this point, the incorporation of Net TV (acquired with an employee and without outsourcing) stands out for its greater push in figures, which boosted operating margins that stood at 16.8% for 2022 (+6.2pp YoY). Moreover, solid and adequate progress is being observed in the generation of a positive EBT in recent years that reached €10.8MM in 2022 (+100.8% vs 2021).

  For 2023 and future years, the group estimates a further journey and increase in income, profits and margins, all of this reinforced by the growth forecast for its four business lines, where the content sector stands out (with the investment already materialised years back).

- **Controlled levels of leverage.** Squirrel's debt figures have been increasing in recent years, reaching its maximum peak at the end of 2022, with a figure of €36.5MM (+340.7% compared to the end of 2020). All of this is due to the organic and inorganic growth plan that the group is developing, carrying out M&A operations that are either carried out with own funds or through an equitable mix between own and financial capital. In any case, despite the increase in its NFD/EBITDA ratio of 2.4x (+1.8x compared to the end of 2020), the company maintains values considered controlled. Thus, from EthiFinance Ratings we favourably assess its presented financial policy and structure, although it will be important to maintain it given the growth and/or new M&A opportunities that may arise. Additionally, it maintains a high interest coverage (16.8x), reflecting its more than adequate capacity to meet the interest on the debt with the operating income generated. However, the current context of rising interest rates, the disposition of a significant part of its financial debt at variable rates, as well as its increase, has caused an adjustment in this coverage ratio (-36x vs 2020) that should be checked in future exercises.

- **Business model that generates operating cash.** The company is presenting an upward trend in the Funds From Operations (FFO) generated, which stood at €11.1MM and the $CAGR_{20\text{-}22}$ being 109.9%. All this is motivated by the organic and inorganic growth that the group is achieving, and which places the values of the FFO/NFD ratio at adequate values (34.7% for 2022). However, a reduction in recent years has been reflected (-140.7pp vs. 2020), a longer run in the levels of operating cash generated by the group in the coming years being important, which will allow it to face the demanding maturities presented by the group in its financial debt (€13.5MM and €15.4MM for 2023 and 2024 respectively, representing 87.2% of total financial obligations).

Solvency

- **Positive solvency supported by its high levels of capitalisation.** Although the increase in financial debt is being proportionally greater than the increase in the group's net worth, Squirrel maintains solid and appropriate values for the relationship between the equity and the TFD, amounting to 145.3% (-184.6pp vs 2020). Thus, the last capital increase carried out in June 2022 for €10MM together with a self-financing policy (capitalisation of the profits achieved and without forecasting the distribution of dividends as in recent years), lead to a strong equity structure.

- **Significant weight of intangible assets within the company whose unforeseen deterioration could penalise its net worth.** The group's intangible assets made up mainly of the audio-visual rights of the acquired titles, as well as the goodwill derived from the corporate acquisitions carried out and which represent a weight of 62% within the total investment in 2022. This aspect, although it does not represent a mitigating fact in its structure at present, is considered that the existence of potential impairments that may arise with the expansion policy carried out, could limit its own capital figures. In any case, this situation is observed at a general level throughout the entertainment and media sector, with various mergers and acquisitions being a shared risk.

Modifiers

ESG Factors

- **The group does not present any controversy.** Our controversy assessment determines that there are no news or events that constitute a real problem that point to a weakness in Grupo Squirrel Media's operations or organisation and that require follow-up.

Liquidity

- **There is no liquidity risk.** At the end of 2022, the group presents a favourable cash position (€4.6MM) and a growing generation of operating funds with the activity (€11.1MM) that are improving their liquidity levels in recent years. Regarding the group's main obligations, it has some demanding financial commitments (mainly bank loan maturities, as well as deferred payments mainly for the purchase of Net TV and Grupo BF) and lower maintenance capex (focused on the content sector for the set-up of new releases). In any case, the assessment of the liquidity ratio is positive (1x/2x range).

Country Risk

- **It has not been determined that there is a conditioning country risk and that therefore it has a negative impact on the rating.** Squirrel concentrates most of its business in Spain and Italy (around 88% of its income for 2021 and for the end of the first half 2022), with the rest mainly spread across other European countries and LATAM.

Main financial figures

Main financial figures. Thousands of €.	2020	2021	2022 [1]	22vs21
Turnover	32,088	69,698	80,005	14.8%
EBITDA	2,742	7,436	13,480	81.3%
EBITDA Mg.	8.5%	10.7%	16.8%	6.2pp
EBIT	1,581	5,507	11,470	108.3%
EBIT Mg.	4.9%	7.9%	14.3%	6.4pp
EBT	1,469	5,382	10,808	100.8%
Total Assets	55,161	64,275	117,016	82.1%
Equity	27,292	30,476	52,974	73.8%
Total Financial Debt	8,274	12,687	36,467	187.4%
Net Financial Debt	1,434	9,367	31,890	240.5%
Equity/TFD	329.9%	240.2%	145.3%	-94.9pp
NFD/EBITDA	0.5x	1.3x	2.4x	1.1x
Funds From Operations	2,515	8,140	11,076	36.1%
FFO/NFD	175.4%	86.9%	34.7%	-52.2pp
EBITDA/Interest	52.7x	33.0x	16.8x	-16.3x

[1] Latest consolidated and published financial statements for 2022 but without audit.

Rating Sensitivity

Factors that may (individually or collectively) impact the rating:

- **Positive factors (↑).**

  Improvement in ratios such as NFD/EBITDA and FFO/NFD with values less than 2x and greater than 40% respectively. Improvement or maintenance of the current figures for the interest coverage and Equity/TFD ratios. Expand the financial debt maturity schedule with longer commitments over time (currently payments are concentrated in 2023 and 2024). In general, compliance with the economic-financial projections analysed. Definition and greater scope of ESG policies.

- **Negative factors (↓).**

  Significant breach of the economic-financial projections analysed with worsening ratios such as NFD/EBITDA (>3x), FFO/NFD (<30%), interest coverage (<10x) and Equity/TFD below 100%. Absence of broader and more far-reaching ESG policies on the part of the group. Worsening of liquidity levels with higher payment obligations (debt and capex) in relation to operating cash and available cash (<1x).

Regulatory information

Sources of information

The credit rating assigned in this report has been requested by the rated entity, which has also taken part in the process. It is based on private information as well as public information. The main sources of information are:

- Annual Audit Reports.
- Corporate Website.
- Information published in the Official Bulletins.
- Rating book provided by the Company.

The information was thoroughly reviewed to ensure that it is valid and consistent, and is considered satisfactory. Nevertheless, EthiFinance Ratings assumes no responsibility for the accuracy of the information and the conclusions drawn from it.

Additional information

- The rating was carried out in accordance with Regulation (EC) N°1060/2009 of the European Parliament and the Council of 16 September 2009, on credit rating agencies, and in accordance with the Corporate Rating Methodology and Outlook Methodology that can be consulted on https://www.ethifinance.com/en/ratings/methodologies and according to the Long-term Corporate Rating scale available at https://www.ethifinance.com/en/ratings/ratingScale.
- EthiFinance Ratings publishes data on the historical default rates of the rating categories, which are located in the central statistics repository CEREP, of the European Securities and Markets Authority (ESMA).
- In accordance with Article 6 (2), in conjunction with Annex I, section B (4) of the Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009, it is reported that during the last 12 months EthiFinance Ratings has not provided ancillary services to the rated entity or its related third parties.
- The issued credit rating has been notified to the rated entity, and has not been modified since.

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