30 November 2023 | Corporates

LR Global Holding GmbH
Germany, Retail

BB- STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2021**	**2022**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover (x)	4.0	3.3	2.6	2.8
Scope-adjusted debt/EBITDA (x)	3.2	4.2	3.9	3.6
Scope-adjusted funds from operations/debt (%)	16	14	8	13
Scope-adjusted free operating cash flow (FOCF)/debt (%)	0	-1	-2	4

Rating rationale

The rating reflects our increased confidence that the negative effects of the Russia-Ukraine war and other macroeconomic events are over for LR. While these events depressed sales and EBITDA in 2022, the company's operating performance has improved since then. We expect credit metrics to bottom out for the full year 2023 and to improve thereafter. In 2023, LR's interest coverage ratio is expected to remain higher than 2.5x, which is the downside threshold for present ratings.

The issuer rating continues to reflect our business risk assessment, supported by the company's good position as a manufacturer and distributor of premium non-durable consumer goods with health and lifestyle attributes. LR mostly produces the goods it sells itself and then distributes them through direct selling. The risks posed by LR's small absolute size (under EUR 300m of annual sales) are effectively mitigated by a favourable positioning both on the product side and regarding its addressable direct-selling market, with limited-to-no competition on the point of sale. LR's comparatively good operating margins (11% EBITDA margin in H1 2023) provide additional rating support. Lack of diversification continues to hinder credit quality, as LR is only active in one niche market and has relatively high product concentration.

Outlook and rating-change drivers

The Outlook is Stable, reflecting our expectation that credit metrics will stabilise after 2024 and that further macroeconomic/ geopolitical crisis will not harm the business environment further.

A positive rating action could be warranted if the company continued to exhibit significant sales growth even in challenging market conditions. In addition, cash interest cover sustained at above 4x could be supportive, which may be driven by extended/continued acceleration of sales and operating performance.

A negative rating action could be possible if the cash-interest cover were consistently below 2.5x, which may result from deteriorated operating performance.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
8 Nov 2022	Outlook change	BB-/Negative
9 Dec 2021	Affirmation	BB-/Stable
7 Dec 2020	Upgrade	BB-/Stable

Ratings & Outlook

Issuer	BB-/Stable
Senior secured debt	BB-

Analyst

Olaf Tölke
+49 69 6677389 11
o.toelke@scoperatings.com

Related Methodologies and Related Research

General Corporate Rating Methodology; October 2023

Retail and Wholesale Rating Methodology; April 2023

Consumer Products Rating Methodology; November 2022

Scope Ratings GmbH

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

Bloomberg: RESP SCOP

Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• One of largest direct-selling companies in Europe • Favourable product positioning creating strong growth	• Overall small size in underlying large consumer goods and retail markets • Strongly dependent on leading brands (Aloe Vera based) • Concentration on a core product

Positive rating-change drivers	Negative rating-change drivers
• Interest cover sustained at above 4x	• Interest cover sustained at below 2.5x

Corporate profile

Founded in 1985, LR Global Holding GmbH is a producer and seller of various consumer goods focusing on health, nutrition and beauty. LR has a niche orientation product-wise and a premium pricing strategy. The exclusive brand used is LR Health and Beauty consisting mainly of Aloe Vera and Aloe Via product ranges. LR's unique selling point is its distribution form as a direct seller via the internet and using a large number of sales partners (about 300,000) to generate revenue in what the company calls social selling. The company has no physical stores. Based in Germany, the company markets about 300 different beauty and health care products in a total of 32 countries. Customers are usually quality and lifestyle-oriented individuals conscious looking for non-mass produced, natural products with price being of lesser importance.

The company is fully owned by German private equity investors Quadriga Capital and Bregal Capital (not represented anymore), which took over LR Global from Apax Partners in 2012.

The rating entity is LR Global Holding GmbH, directly owned by Luxemburg-based Aloco, which is Quadriga's ownership vehicle.

Financial overview

				Scope estimates		
Scope credit ratios	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
Scope-adjusted EBITDA/interest cover (x)	19.3	4.0	3.3	2.6	2.8	3.4
Scope-adjusted debt/EBITDA (x)	7.2	3.2	4.2	3.9	3.6	3.2
Scope-adjusted funds from operations/debt (%)	13	16	14	8	13	14
Scope-adjusted FOCF/debt (%)	8	0	-1	-2	4	1
Scope-adjusted EBITDA in EUR m						
EBITDA	37	37	31	34	36	41
Other items	**0**	0	**0**	**0**	0	**0**
Scope-adjusted EBITDA	**37**	**37**	**31**	**34**	**36**	**41**
Funds from operations in EUR m						
Scope-adjusted EBITDA	37	37	31	34	36	41
less: (net) cash interest paid	-1	-14	-9	-13	-13	-12
less: cash tax paid per cash flow statement	-1	-4	-4	-10	-6	-10
Change in provisions	0	0	0	0	0	0
Funds from operations	**35**	**19**	**18**	**11**	**17**	**19**
Free operating cash flow in EUR m						
Funds from operations	35	19	18	11	17	19
Change in working capital	-4	-4	1	-3	0	-4
Non-operating cash flow	3	-3	-4	1	0	0
less: capital expenditure (net)	-6	-6	-6	-5	-5	-6
less: lease amortisation	-6	-6	-10	-6	-6	-7
Free operating cash flow	**22**	**0**	**1**	**-3**	**6**	**2**
Net cash interest paid in EUR m						
Net cash interest per cash flow statement	-1	-14	10	13	13	12
Change in other items	-1	5	0	0	0	0
Net cash interest paid	**-2**	**-9**	**10**	**13**	**13**	**12**
Scope-adjusted debt in EUR m						
Reported gross financial debt	290	142	150	149	151	151
less: cash and cash equivalents	-29	-30	-20	-20	-23	-23
add: non-accessible cash	3	3	20	20	23	23
Other items	1	1	0	1	1	2
Scope-adjusted debt	**262**	**117**	**131**	**130**	**129**	**130**

Table of Content

Environmental, social and governance (ESG) profile[1]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	Grey leaf
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	Grey leaf
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	Grey leaf
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	Grey leaf

Legend

Green leaf (ESG factor: credit positive)
Red leaf (ESG factor: credit negative)
Grey leaf (ESG factor: credit neutral)

ESG neutral

LR has a general ESG strategy and focuses on the provision of sustainable products manufactured in Germany aiming at improving customers' health and wellbeing. However, we assess LR's ESG positioning as neutral as we are not in a position to compare the company with its direct peers in the ESG space.

[1] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BB-

Industry risk profile: BBB+

We have assigned a blended industry risk of BBB+ to LR as the company is both a producer (90% of products sold are produced in house) and a distributor (through online channels). The two industries that apply are therefore consumer products (assessed at A) and retail (assessed at BBB). Within the consumer product market, LR concentrates on the niche segment of health, nutritional additives, and beauty while in the context of its retail profile it focuses on specialised multi-layer marketing and social selling.

LR has good market shares

While LR is a relatively small company in the context of the multi-billion underlying retail and non-durable consumer goods markets, its addressable market based on its selling concept is also small. LR's products are not represented in supermarkets or pharmacies, which account for a large part of the underlying market. The company has two distinct features mitigating this disadvantage. First, it is positioned in specific health-related niche segments, which have attractive growth characteristics due to prevailing green and healthy shopping trends. Secondly, its potential for revenue growth is underscored by its large self-employed sales force (about 300,000 partners), incentivised through individual discounts on their own sales as well as additional cash bonus payments depending on their overall sales from their referral network. In addition, as it progresses, LR provides more and more benefits to sales partners such as company car eligibility.

Direct/social selling only represents a fraction – although an increasing one – of a product's global demand. LR had been generating significant above-market growth before the Covid-19 crisis and strong growth continued in 2021 (gross sales grew by 4%). This came to an abrupt end in 2022, as the war in Ukraine disrupted the country's supply chains and the effect also spilled over into Russia, also an LR market. While in H2 2022, LR saw a recovery in sales and a reduced exposure to Russia and Ukraine, the total year 2022 contracted in business volume YoY. LR's market share in its five main countries of operation based on the market available for direct selling ranges between 5% and 40% according to PwC.

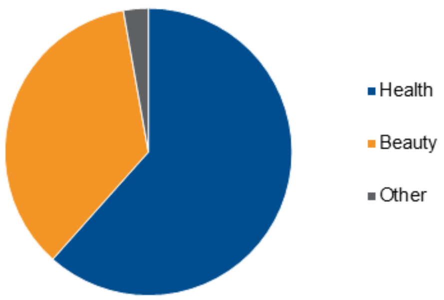
Weak diversification

We believe diversification continues to be LR's weakest point as product concentration is high. The two large health-related product groups of aloe vera products and nutritional additives together account for about 60% of total group sales, a share that has been increasing (about 40% in 2016).

Geographic exposure is credit-positive. LR is active all over Europe and made an entry into South Korea in March 2021. It currently sells products in 32 countries. Since 2023, the company has streamlined its sales structure into two regions (from formerly three) as follows:

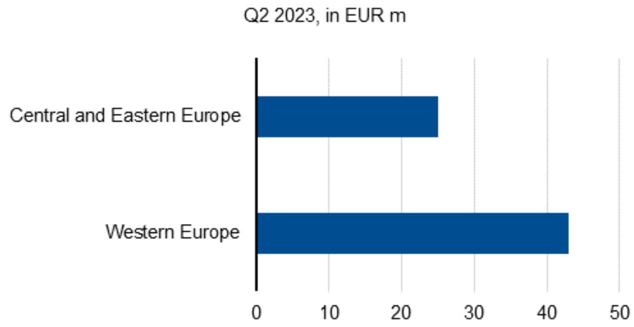
- **Western Europe:** Austria, Belgium/Luxembourg, Denmark, UK, Finland, France, Germany, Italy, the Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, and Türkiye
- **Central and Eastern Europe:** Albania, Bulgaria, Czech Republic, Greece/Cyprus, Hungary, Poland, Romania, Russia/Kazakhstan, Slovakia, and Ukraine

Figure 1: Revenue breakdown by product segment



Source: LR Global, Scope estimates

Figure 2: Revenue breakdown by operating regions



Source: LR Global, Scope estimates

Comparatively good profitability

As a highly integrated non-durable consumer goods retailer, LR has good operating margins in a peer context. It has achieved EBITDA margins in the range of 9%-13% for the last five years. The company not only compares well with its retailing peers but also shows little volatility given recent macroeconomic turmoil. This was supported by good sales growth over the last five years (revenue increasing from EUR 223m in 2019 to more than EUR 280m projected for 2023 in our base case) as well as its ability to raise prices if needed. This enables the company to address raw material and other input cost inflation, a key advantage in the last few years. During the Covid-19 crisis, the company initially benefitted from increased demand for health-related products, while in H1 2022, the Russia-Ukraine war affected sales negatively not only in Ukraine and neighbouring countries, but also in other regions due to supply chain disruptions. This initial negative customer behaviour was however only short lived and demand started to recover in Q4 2022. Despite the negative sales performance in 2022 as a whole, profitability stayed relatively stable, helped by the launch of innovative product ranges. The same held true in H1 2023, when revenue expanded by 12% YoY. For the full year 2023, we assume an EBITDA margin of 11.6%, slightly up from the 11.1% reached in H1 2023.

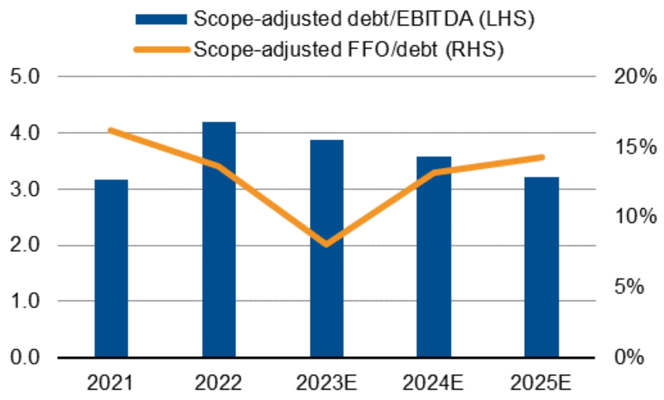
The main growth drivers are the company's incentivisation programme that focuses on involving key sales partners early on in the process (thereby strengthening their entrepreneurial role) as well as innovations – presently accounting for about 15% of sales, which has accelerated in recent years. LR's cost structure benefits from comparatively lower fixed costs compared to peers as the sales force is self-employed. Revenue increases therefore have a larger impact on profitability than for most competitors. Raw materials do not play a critical role for LR's profitability either as the company only purchases limited volumes of raw materials. This translates into limited raw material price dependency.

Financial risk profile: BB-

Credit metrics expected to bottom out

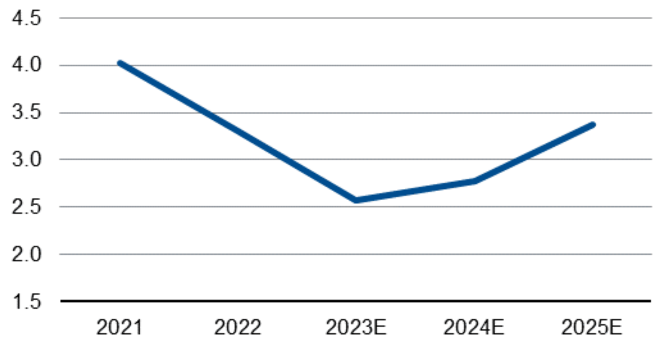
Credit metrics are very likely to stabilise from 2024 after a phase of operational weakness in H1 2022 induced by the Russia-Ukraine war. While this had led to some deterioration of credit metrics in 2022, there was a good recovery of operating trends in H1 2023. Both YoY sales and EBITDA growth were quite strong. This was chiefly generated in the company's Western European segment (up 16% YoY), while the Central and Eastern European division saw negative growth in H1 2023 (down 4.8% YoY). H2 2023 might additionally benefit from price increases. We project that 2023 EBITDA will increase by 7% YoY, as H2 is traditionally supported by the Christmas business. Our projections are thus more optimistic than those of management, which assumes stable earnings for the full year. We expect Scope-adjusted debt/EBITDA to improve to 3.9x in 2023, equivalent to a slight deleveraging from the end-2022 level of 4.2x (assuming 50% of cash netting against debt). The interest coverage ratio, which is the main credit ratio in the context of the rating, is expected to decrease to 2.6x in 2023, but remains commensurate with the current rating category. In last year's review, we expected that in 2022, the interest coverage ratio would decrease to the point of triggering a downgrade, which was conservative, based on an EBITDA projection of EUR 26m (actual: EUR 31m).

Figure 3: Improving leverage



FFO: funds from operations
Sources: LR Global, Scope estimates

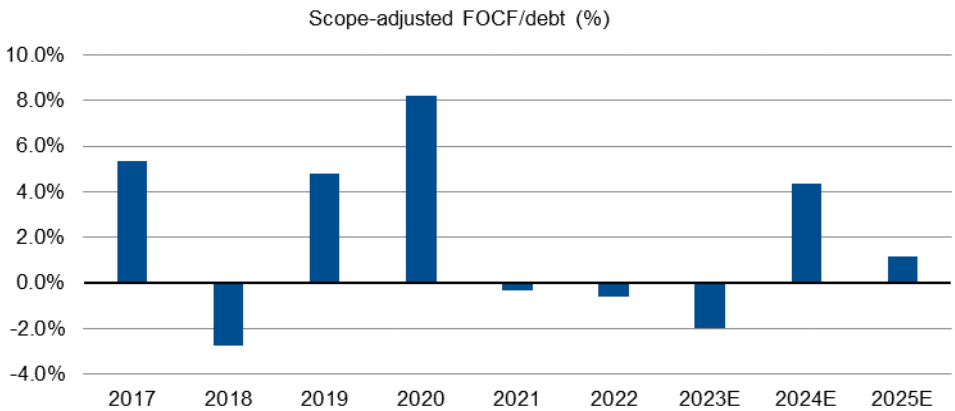
Figure 4: Interest cover expected to bottom out in 2023



Sources: LR Global, Scope estimates

The company's ability to generate FOCF via its very low-maintenance capital expenditure and historically well-managed working capital came to a halt in 2021, partly as a consequence of rising interest payments. For 2023, interest payments are likely to show a strong increase to about EUR 13m, from EUR 9.5m in 2022, reflecting the higher interest rate environment. We expect a gradual improvement of free cash generation (see Figure 5), based on our assumption of rising operating cash flow from 2024 and a continued controlled working capital management. The less favourable trend in projected 2023 free cash flow (compared to other credit metrics) is mainly due to higher tax payments for previous years, which increased payments by about EUR 5m in H1 2023. We consider this a one-off effect and there should be no further aperiodic payments in H2 2023. However, in a retail context, Scope-adjusted FOCF/debt should not be over-weighted as retail companies do not compare favourably on that ratio to sector peers on account of comparatively lower margins and operating cash flow. As LR is not a pure retailer, this point is somewhat mitigated but still relevant.

Figure 5: FOCF depressed through the crisis years



Ample covenant cushion

The issued bond has a maintenance covenant (leverage ratio equal to or under 4.5x), which provides the company with ample headroom, even in crisis years.

Adequate liquidity

LR's liquidity profile benefits from a solid cash buffer of around EUR 30m on average (EUR 29m on 30 June, 2023), positive FOCF and immaterial short-term debt (only leases). While the Nordic bond is due in 2025 and we assume a successful refinancing as soon as 2024, we continue to assess LR's liquidity profile as 'adequate'.

Balance in EURm	2023E	2024E	2025E
Unrestricted cash (t-1)	17	20	23
Open committed credit lines (t-1)	0	0	0
Free operating cash flow	-3	6	2
Short-term debt (t-1)	0	0	120
Coverage	**No short-term debt**	**No short-term debt**	**20%**

Supplementary rating drivers: +/- 0 notches

We have not identified any reasons for differentiating the rating with a supplementary ratings consideration.

Long-term debt ratings

Senior secured debt rating: BB-

Based on hypothetical default in 2025, the recovery analysis done under a going concern approach indicates an 'above-average' recovery expectation. While this would open up the possibility for an up-notching of the bond in relation to the issuer rating, we decided to put the ratings pari passu to each other, reflecting the calculated recovery rate's positioning at the bottom the respective category (50-70%).

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

10 avenue de Messine
FR-75008 Paris

Phone +33 6 6289 3512

Oslo

Karenslyst allé 53
N-0279 Oslo

Phone +47 21 09 38 35

Madrid

Paseo de la Castellana 141
E-28046 Madrid

Phone +34 91 572 67 11

Milan

Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Scope Ratings UK Limited

London

52 Grosvenor Gardens
London SW1W 0AU

Phone +44 20 7824 5180

info@scoperatings.com
www.scoperatings.com