Corporate and Corporate Bond Rating
MITEC Automotive AG
Germany, Automotive suppliers

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Corporate profile

Founded in 1990, MITEC Automotive AG ('MITEC') is a German auto supplier specialising in automobile propulsion technology, which reduces noise emissions and vibrations, and enhances powertrain efficiency. MITEC's product portfolio comprises auto parts such as balancer systems, gear wheels and bevel gear sets, along with adjustable oil pumps and camshaft timing devices. The company operates production sites in Germany, China and the USA.

Rating

Corporate Issuer Credit Rating:	BB-
Outlook:	Stable
Corporate Bond Rating:	BB-
Outlook:	Stable
Sector:	Automotive suppliers
Monitoring:	yes

Analysts

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Rating rationale

The rating affirmation is based particularly on MITEC's positive operating performance in line with expectations, improved EBITDAR margin and leverage, as well as its continued strong market position.

Scope Ratings ('Scope') affirms the BB- rating of the EUR 25m senior unsecured corporate bond (7.75% 2012/2017) of MITEC. The instrument rating is based on a Corporate Issuer Credit Rating ('CICR') of BB-. Both Outlooks are Stable.

The BB- rating of the German based automotive supplier MITEC is supported by its strong market position as a small tier 1 supplier in the growing market for balancer systems, its well-diversified geographical spread and ample order backlog. MITEC's adjusted EBITDAR stood at 8.9% in FY 14 from 8.3% in FY 13, impacted by the postponement of substantial orders from a core customer. Scope expects it to increase to over 12% by FY 16, bolstered by materialisation of MITEC's sizable order backlog and the conversion of recent R&D activities as new products turn into future revenue streams (R&D ratio up to 2.0% in FY 14).

Negative rating factors include MITEC's relatively small size, with an adjusted EBITDAR of EUR 13.5m in FY 14, and relatively limited product offering, with 76% of total revenues derived from its core product, balancer systems. Driven by cash flows buoyed by its order backlog, Scope expects MITEC to further reduce its high lease-adjusted net debt/EBITDAR to 4.5x in FY 16 (FY 14: 6.9x). For the same reason, Scope assumes MITEC's EBITDAR fixed charge cover to improve to 2.7x in FY 16 (FY 14: 1.8x).

The BB- rating of the senior unsecured corporate bond is based on MITEC's CICR and reflects the structural subordination to the secured debt issued by MITEC Automotive AG and its US subsidiary MITEC Powertrain Inc.

Outlook

The Outlooks for the CICR and bond rating are Stable. The Stable Outlooks are based upon MITEC's strong market position and supportive backlog, backed by overall favourable market conditions in Europe and the US.

Current ratings could come under pressure if adverse market conditions weaken the company's cash flows and ability to reduce its high leverage below a threshold of 5.0x (net debt/EBITDAR) by YE 16.

A positive rating action would require a faster-than-expected deleveraging with stronger credit metrics, such as an adjusted debt/EBITDAR below 3.5x and an improved EBITDAR fixed charge coverage above 4.0x. An upgrade would also depend on MITEC's ability to significantly improve its customer diversification (Top 3 of revenues <50%).

Rating drivers

Positive	Negative
Strong position within the market for balancer systems	Small scale tier1 supplier in a market with well-positioned global competitors
Excellent geographical diversification	Strong customer concentration combined with deterioration in customer structure
Improving innovative power	Almost single-product supplier associated with high project concentration
Sufficient liquidity and limited risks in debt structure	High leverage of 6.9x (net debt/EBITDAR (adj.)) in FY 14 combined with balloon maturity profile
Ample order backlog of 5.1x FY 14 sales providing business stability and visibility on future cash flows	Capital intense business with large pre-financing requirements
Expected continuous improvements of margins and leverage (EBITDAR margin > 12%; net debt/EBITDAR of 4.5x by FY 16)	Comparably low fixed charge cover of 1.8x (EBITDAR (adj.) fixed charge cover) in FY 14

Financial overview

	2012	2013	2014	2015E	2016E	2017E
P & L statement (EURm)						
Revenue	137.9	137.7	148.8	151.6	178.6	213.0
EBITDAR (adj.)	22.3	11.7	13.5	18.5	23.0	26.8
EBITDA (adj.)	21.7	11.1	12.8	16.4	20.0	23.8
Interest expense	-6.9	-6.6	-6.7	-5.7	-5.5	-5.3
Net interest income (NII)	-6.7	-6.4	-6.7	-5.7	-5.5	-5.3
Balance sheet (EURm)						
Total financial debt	107.2	95.7	102.9	108.3	108.2	105.7
Net financial debt	81.4	80.0	93.9	99.9	102.2	98.6
Cash flow statement (EURm)						
Funds flow from operations (FFO) (adj.)	15.0	4.3	5.8	10.6	12.9	15.6
Changes in working capital	9.0	-5.0	5.9	0.5	4.5	5.8
Operating cash flows	-5.4	11.1	0.3	6.8	6.9	8.4
Capex	-5.4	-8.6	-10.4	-7.5	-8.4	-6.0
Free cash flow (FCF)	-10.7	2.6	-10.1	-0.6	-1.5	2.4
Key financial ratios						
EBITDAR (adj.) margin	15.9%	8.3%	8.9%	12.1%	12.8%	12.5%
EBITDA (adj.) margin	12.9%	6.4%	6.8%	8.8%	9.3%	9.6%
Total debt/EBITDAR (adj.)	4.8x	8.2x	7.6x	5.9x	4.7x	3.9x
Net debt/EBITDAR (adj.)	3.6x	6.9x	6.9x	5.4x	4.5x	3.7x
FFO (adj.) fixed charge cover	3.1x	1.6x	1.8x	2.4x	2.5x	2.9x
EBITDAR (adj.) fixed charge cover	3.1x	1.7x	1.8x	2.4x	2.7x	3.2x
FFO (adj.)/total debt	20.8%	11.8%	12.9%	17.0%	19.8%	22.5%
Liquidity	16.9%	89.2%	73.3%	70.0%	73.9%	73.9%
R&D ratio	0.0%	0.9%	2.0%	3.1%	3.1%	3.1%

Source: MITEC Automotive AG, Scope

Rating change drivers

Positive	Negative
Faster-than-expected deleveraging (adjusted debt/EBITDAR below 3.5x)	Ability not to reduce the leverage below a threshold of 5.0x (net debt/EBITDAR) by YE 16
Improvement of EBITDAR fixed charge coverage above 4.0x	
Improvement of customer diversification (Top 3 of revenues <50%)	

Business Risk Profile

Small but strong market share in the niche market for balancer systems

With an adjusted EBITDAR of EUR 13.5m in FY 14 MITEC is a very small automotive supplier. Despite its size, Scope considers MITEC to be well positioned as the European leader in the niche market for balancer systems. The company's global market share for balancer systems is approximately 10%. Scope considers MITEC's market position as very solid, partly offsetting inherent cyclicality and substitution risks in the global automotive supplier sector.

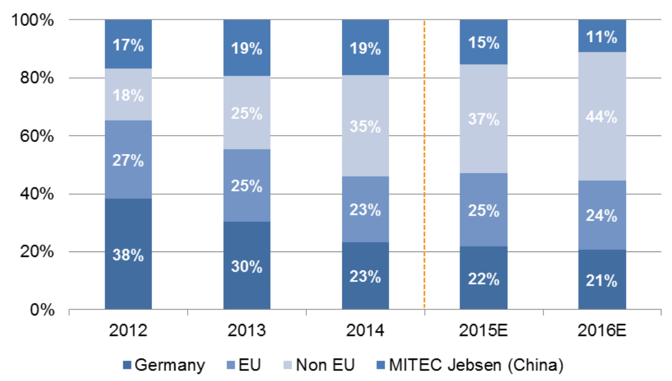
High customer and product concentration risks

MITEC's customer and product diversification is limited. The company currently shows a strong customer concentration with the three largest customers accounting for a high 83% of FY 14 sales and nearly 76% of sales attributable to the core division, balancer systems. Given the order backlog to FY 18, Scope expects customer concentration to remain above 80% with an increasing bias towards automotive manufacturers with weaker financial profiles. The latter is seen as credit negative. Scope expects this bias to improve slightly in the medium term following recent negotiations with premium car makers.

Solid geographical diversification to broaden further

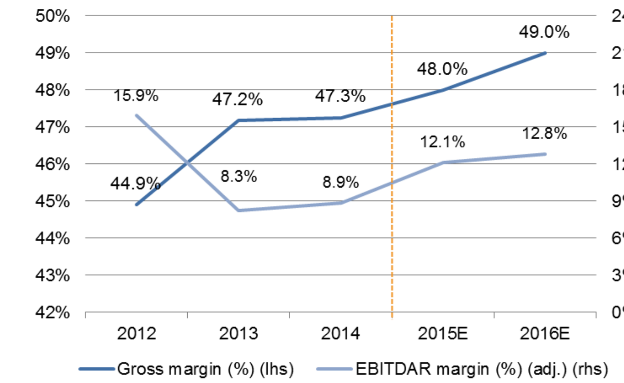
In FY 14, 46% of MITEC's revenues were generated in Europe; 19% through its Chinese joint venture and the remaining 35% in ROW, predominantly for US automotive manufacturers. With the help of the US and Chinese subsidiaries, Scope expects MITEC to globalise its footprint with expected sales from Europe to fall below 40% as a proportion of total sales by FY 18.

Figure 1 – Geographical diversification 2010 to 2016E



Source: MITEC, Scope

Figure 2 – Margin development of margin



Source: MITEC, Scope

EBITDAR margin expected to improve further

MITEC's adjusted EBITDAR margin declined from 17.8% in FY 10 to a bottom level of 8.3% in FY 13, due to material delays in order deliveries to a core customer and associated high pre-financing costs. In FY 14, MITEC's EBITDAR margin recovered to 8.9%. With the order backlog materialising and the conversion of recent R&D activities into new innovative products, Scope expects MITEC's EBITDAR margin to improve above 12% in FY 16.

Financial Risk Profile

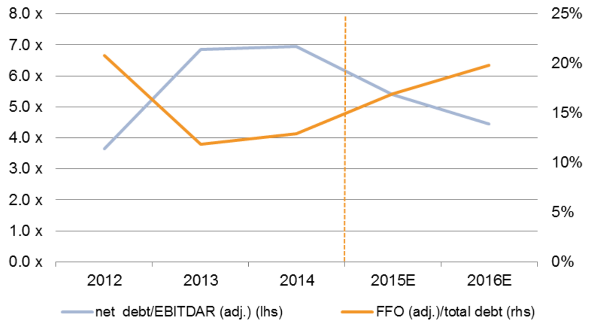
Peaking leverage to decrease

The rating incorporates the company's high lease-adjusted leverage (debt/EBITDAR) of 7.6x in FY 14, an improvement on 8.2x in FY 13 (net debt/EBITDAR FY 14: 6.9x). Scope expects MITEC's peaking net leverage to decrease to 4.5x in FY 16, backed by improving profitability, stable debt development and the company's cash cushion.

Positive operating cash flows and modest fixed charge coverage

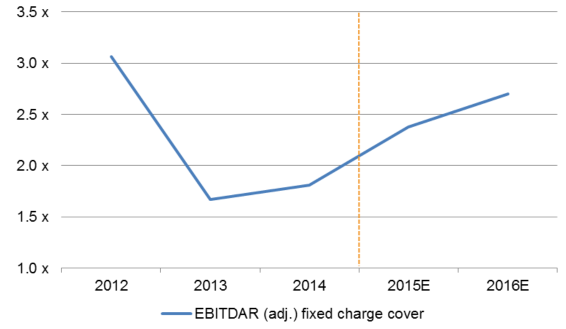
MITEC shows a track record of positive operating cash flows in the last five FYs (2010-2014). MITEC displays a reasonable fixed charge coverage as a result with EBITDAR fixed charge cover FY 14: 1.8x vs 1.7x in FY 13. Scope estimates an EBITDAR fixed charge cover of 2.7x in FY 16, driven by revenue growth and improving profitability.

Figure 3 – Development of financial leverage



Source: MITEC, Scope

Figure 4 – Development of fixed charge coverage



Source: MITEC, Scope

Ample order book provides cash flow visibility

The company's long-term order backlog for FY 15-FY 18 totals EUR 760m, representing 5.1x MITEC's FY 14 sales. Although it carries some execution risk – particularly in light of its customer concentration – the order backlog provides strong visibility and stability on MITEC's future revenues and cash flows.

Sufficient liquidity

MITEC's interest-bearing debt amounted to EUR 95m in June 2015. The company's liquidity cushion of EUR 10m in June FY 15 (EUR 9.0m at YE 13) plus factoring line of EUR 10m are sufficient to cover FY 15 debt maturities of EUR 7.0m comfortably. Scope believes any risks arising from either refinancing/prolonging the EUR 33m bank debt facility from MITEC's house banks by the end of FY 16, or refinancing the EUR 25m corporate bond in March FY 17 are limited, given the order backlog and expected solid financial performance.

Senior secured corporate bond

Senior unsecured corporate bond rating of BB- at same level as CICR

The BB- corporate bond rating reflects MITEC's CICR as well as the seniority and asset pledges of MITEC's debt positions. Given the absence of a security package, MITEC's corporate bond is structurally subordinated to the secured debt issued by MITEC Automotive AG and its US subsidiary, MITEC Powertrain Inc., totalling roughly EUR 70.5m as of June FY 15. Scope expects an average recovery for MITEC's EUR 25m senior unsecured corporate bond in the theoretical case of a company default.

Outlook

Outlooks: Stable

The Outlooks for the CICR and bond rating are Stable. The Stable Outlooks are based on MITEC's strong market position and supportive backlog, backed by overall favourable market conditions in Europe and the US.

Current ratings could come under pressure if adverse market conditions weaken the company's cash flows and ability to reduce its high leverage below a threshold of 5.0x (net debt/EBITDAR) by YE 16.

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Regulatory disclosures

Important information

Information pursuant to Regulation (EC) No 1060/2009 on credit rating agencies, as amended by Regulations (EU) No. 513/2011 and (EU) No. 462/2013

Responsibility

The party responsible for the dissemination of the financial analysis is Scope Ratings AG, Berlin, District Court for Berlin (Charlottenburg) HRB 161306 B, Executive Board: Torsten Hinrichs (CEO), Dr. Stefan Bund.

The rating analysis has been prepared by Timo Schilz, Lead Analyst.
Responsible for approving the rating: Dr. Stefan Bund, Committee Chair.

Rating history

Date	Rating action	Rating
24.08.15	Affirmation	Corporate Bond | BB- Outlook Stable
24.08.15	Affirmation	CICR | BB- Outlook Stable
26.08.14	Initial	Corporate Bond | BB- Outlook Stable
26.08.14	Initial	CICR | BB- Outlook Stable

The rating outlook indicates the most likely direction of the rating if the rating were to change within the next 12 to 18 months. A rating change is, however, not automatically ensured.

Information on interests and conflicts of interest

The rating was prepared independently by Scope Ratings but for a fee based on a mandate of the rated entity.

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Key sources of Information for the rating

- ☒ Prospectus
- ☒ Annual reports/semi-annual reports of the rated entity / issuer
- ☒ Website of the rated entity / issuer
- ☒ Current performance record
- ☒ Data provided by external data provider
- ☒ External market reports
- ☒ Interview with the rated entity
- ☒ Detailed information provided on request
- ☒ Press reports / other public information
- ☒ Other opinions

Scope Ratings considers the quality of the available information on the evaluated company to be satisfactory. Scope ensured as far as possible that the sources are reliable before drawing upon them, but did not verify each item of information specified in the sources independently.

Examination of the rating by the rated entity prior to publication

Prior to publication, the rated entity was given the opportunity to examine the rating and the rating drivers, including the principal grounds on which the credit rating or rating outlook is based. The rated entity was subsequently provided with at least one full working day, to point out any factual errors, or to appeal the rating decision and deliver additional material information. Following that examination, the rating was not modified.

Methodology

The methodology applicable for this rating (Corporate Rating Methodology, Rating Methodology - European Automotive Suppliers) is available on http://www.scoperatings.com/. The historical default rates of Scope Ratings can be viewed on the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope's default rating, definitions of rating notations and further information on the analysis components of a rating can be found in the documents on methodologies on the rating agency's website.

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