MARSO Kft.
Hungary, Retail

SCOPE B+ STABLE

Key metrics

			Scope estimates	
Scope credit ratios	2022	2023	2024E	2025E
Scope-adjusted EBITDA/interest cover	14.1x	7.9x	5.6x	6.0x
Scope-adjusted debt/EBITDA	2.1x	3.5x	4.5x	4.1x
Scope-adjusted funds from operations/debt	43%	25%	18%	20%
Scope-adjusted free operating cash flow/debt	13%	22%	0%	4%

Rating rationale

Marso operates as a discretionary retailer (industry risk profile assessed at BB). Its business risk profile (assessed at B+) is characterised by Marso's leading market position, extensive supplier network and moderate profitability but is constrained by Marso's small size, strong competitors and weak diversification (both geographically and product-wise). The company's Scope-adjusted EBITDA margin is negatively impacted by economic headwinds, oversupply from manufacturer's excess inventories and the proliferation of low-cost Asian products which have led to its sustained deterioration. The Scope-adjusted EBITDA margin is expected to bottom out at around 4% before a steady but slow recovery towards 5%.

The company's financial risk profile (assessed at BB-, revised from BB) is expected to deteriorate further due to the pressure on profitability from the unfavourable market conditions. Its long-term loan profile is expected to remain broadly unchanged. However, the seasonality of the business model requires Marso to draw on working capital loans twice a year (typically in Q1 and Q3). The financial risk profile is supported by relatively strong interest cover but hindered by high leverage and volatile working capital requirements.

Outlook and rating-change drivers

The Stable Outlook incorporates our view that, although economic headwinds will continue to negatively impact MARSO's operating profitability and its credit metrics in 2024 and beyond, the company's EBITDA margin will not decline below 4% and Marso will maintain a relatively stable loan profile during the next 18 months. This is exemplified by the company's debt/EBITDA ratio remaining in the 4-6x range. In addition, the Outlook reflects continued high intra-year volatility in working capital and net debt due to the seasonality of the issuer's business.

The upside scenario for the ratings and Outlook would require: (1) Scope-adjusted debt/EBITDA improving to below 4.0x on a sustained basis. The downside scenario for the ratings and Outlook would require: (2) Scope-adjusted debt/EBITDA moving close to or above 6.0x.

Rating history

Date	Rating action/monitoring review	Issuer rating & Outlook
19 Sep 2024	Downgrade	B+/Stable
20 Sep 2023	Outlook change	BB-/Negative
21 Sep 2022	Affirmation	BB-/Stable

Ratings & Outlook

Issuer B+/Stable

Senior unsecured bond (ISIN HU0000359393) BB-

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Related Methodologies and Related Research

General Corporate Rating Methodology; October 2023

Retail and Wholesale Rating Methodology; April 2024

ESG considerations for the credit ratings of retail corporates; November 2021

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Strong market position • Comparatively strong financial risk profile • High share of exclusive products	• Low diversification • Small company size in niche market with limited expansion possibilities and stiff competition • Negative impact of supply chain disruptions and inflationary environment on working capital management

Positive rating-change drivers	Negative rating-change drivers
• Scope-adjusted debt/EBITDA improving to below 4.0x on a sustained basis	• Scope-adjusted debt/EBITDA moving to or above 6.0x

Corporate profile

MARSO Kft. is a leading retail and wholesale tyre dealer in Hungary offering products in all three main tyre segments (passenger, truck and agriculture). Marso developed its position through strong relationships with both suppliers and customers. The company has exclusive agreements with some of the largest global tyre manufacturers (e.g. Michelin, Bridgestone) and has a long-term business development agreement with Continental. Marso has deepened its customer loyalty via different sales networks, which include its own brick-and-mortar store network, a franchise network of around 30 partners and the Marso Partner Network distribution network of more than 100 members.

Financial overview

				Scope estimates		
Scope credit ratios	**2021**	**2022**	**2023**	**2024E**	**2025E**	**2026E**
Scope-adjusted EBITDA/interest cover	15.8x	14.1x	7.9x	5.6x	6.0x	6.7x
Scope-adjusted debt/EBITDA	3.7x	2.1x	3.5x	4.5x	4.1x	3.6x
Scope-adjusted funds from operations/debt	24%	43%	25%	18%	20%	23%
Scope-adjusted free operating cash flow/debt	-41%	13%	22%	0%	4%	6%
Scope-adjusted EBITDA in HUF m						
EBITDA	1,444	2,498	1,447	1,033	1,158	1,356
Operating lease payments	590	515	552	563	586	609
Other items (i.e. changes in provisions)	-1	-3	11	-	-	-
Scope-adjusted EBITDA	**2,033**	**3,010**	**2,010**	**1,596**	**1,744**	**1,965**
Funds from operations in HUF m						
Scope-adjusted EBITDA	2,033	3,010	2,010	1,596	1,744	1,965
less: (net) cash interest paid	-128	-213	-254	-285	-291	-293
less: cash tax paid per cash flow statement	-95	-32	-15	-21	-32	-50
Funds from operations (FFO)	**1,809**	**2,765**	**1,742**	**1,290**	**1,421**	**1,621**
Free operating cash flow in HUF m						
Funds from operations	1,809	2,765	1,742	1,290	1,421	1,621
Change in working capital	-261	-651	+828	-248	-55	-95
less: capital expenditure (net)	-4,182	-875	-537	-625	-625	-625
less: lease amortisation	-472	-412	-442	-450	-468	-487
Free operating cash flow (FOCF)	**-3,106**	**827**	**1,591**	**-33**	**272**	**414**
Net cash interest paid in HUF m						
Net cash interest per cash flow statement	10	110	143	172	173	171
add: interest component, operating leases	118	103	110	113	117	122
Net cash interest paid	**128**	**213**	**254**	**285**	**291**	**293**
Scope-adjusted debt in HUF m						
Reported gross financial debt	5,302	5,250	5,725	5,646	5,641	5,650
less: cash and cash equivalents	-1,441	-2,111	-4,102	-3,821	-4,024	-4,349
add: non-accessible cash incl. haircut[1]	100	100	2,051	1,910	2,012	2,174
add: operating lease obligations	2,360	2,059	2,208	2,252	2,342	2,436
Other items[2]	1,257	1,167	1,207	1,207	1,207	1,207
Scope-adjusted debt (SaD)	**7,578**	**6,466**	**7,089**	**7,195**	**7,178**	**7,118**

[1] From 2023 onwards we have applied a 50% haircut to the company's cash amount as it is not considered to be permanent due to (i) the business contraction in 2023; (ii) the high cash absorption of the company's business model (Marso finances its biannual inventory build-up – typically in Q1 and Q3 – through its cash reserves and additional short-term credit lines.); and (iii) the overall declining credit quality.

[2] Other items include off-balance sheet commitments.

Table of Content

Environmental, social and governance (ESG) profile[3]

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)	
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)	
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)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend

Green leaf (ESG factor: credit positive)

Red leaf (ESG factor: credit negative)

Grey leaf (ESG factor: credit neutral)

Adequate ESG profile

Reputational risk is a major criterion for the social aspect of a retailer. For example, product or labour management that has a negative social impact can prompt consumer boycotts, affecting sales, margins and inventory value. However, we believe Marso's position as a national wholesaler decreases this risk substantially. It has initiated several social responsibility projects (such as operating a tennis court in Nyíregyháza and establishing IMKE, a community development association).

Discretionary goods companies such as Marso are also under increasing pressure to ensure the sustainability of their products, namely in terms of durability and repairability. Strong commitment in this regard is likely to improve brand value. Although Marso does not offer tyre retreading, the company has partnered with Continental and collects used tyres to ensure their proper disposal and recycling. In 2020 it collected more than 4,400 tonnes of used tyres.

Lastly, the environmental footprint of a company's brick-and-mortar shops will remain fundamental to its development. Marso is well protected against environmental risks as it has a low number of stores across the country.

[3] 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: B+

Industry risk profile: BB

Marso is categorised as a discretionary retailer. Its industry risk profile remains assessed at BB given the medium cyclicality, low entry barriers and low substitution risk of the automotive parts wholesale segment.

Marso's business risk profile is supported by its dominant market position in Hungary and moderate albeit deteriorating profitability. However, its relatively small size (revenue of EUR 98m in 2023), strong competitors and weak diversification remain negative rating drivers.

Strong market positioning

The company's market shares for the import of light and heavy vehicle tyres in Hungary give it a dominant national position. Marso also sells agricultural tyres. Its relatively strong market position is mainly due to two factors: good relationships with suppliers and integrating customers into a streamlined process. While Marso's market share is high, which is a positive rating driver, its small absolute size and fierce competition restrain the market share assessment, even with the benefits afforded by Marso's exclusivity programme (e.g. low substitution risk).

Low diversification

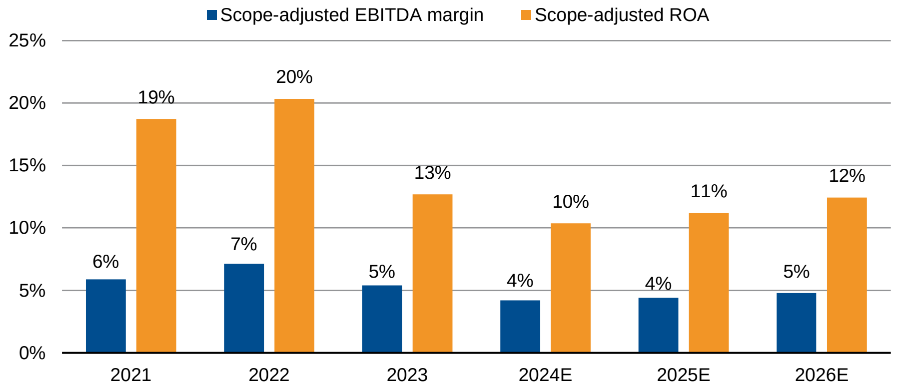
Marso's diversification is low as the company is involved in only one category of consumer goods (automotive parts) and one main sales channel (brick and mortar, >90% of sales). We recognise the presence of multiple sales channels (wholesale, retail, online) but the predominance of wholesale does not help strengthen diversification as Marso appears to be far from establishing an omnichannel sales structure.

Historically Marso's export sales were considered high in peer context at around 20% of total sales, however this has since changed as the company's competitors have entered new markets. In 2023 export sales accounted for 18% of total sales and is forecast to further decrease in 2024. This is considered as too low to offset any negative macro developments in the company's core market of Hungary.

Although Marso has long-term commercial agreements with most major global tyre suppliers, leading to numerous exclusivity agreements (with Michelin and Continental, among others), supplier concentration is high (the top five suppliers account for more than 60% of cost of goods sold). However, we consider these relationships to be durable because Marso is competitive compared to other wholesalers. Exclusive products have historically represented close to 50% of total sales.

Marso attracts customers with several types of offers. In 2023, approximately 30 shops were operated as franchises. These franchises, called Marsoponts, carry the full product range and receive financial support from Marso if needed. The company has also developed a network of customers under the 'Marso Network Partner' label. These customers receive exclusive products and favourable commercial agreements in exchange for paying a royalty to Marso. The two systems are supported by MOND, an e-commerce platform. This multi-channel sales strategy results in a low concentration of customers (top 10 customers excluding affiliates account for less than 15% of sales).

Figure 1: Profitability



Sources: Marso, Scope estimates

Moderate profitability

Marso's relatively strong profitability has so far been a supportive feature of the company's business risk profile, but several factors have put pressure on the Scope-adjusted EBITDA margin leading to its sustained deterioration. Economic headwinds, oversupply from manufacturer's excess inventories and the proliferation of cheap Asian products negatively impacted both revenue and Scope-adjusted EBITDA in 2023. The margin was also negatively impacted by the delayed inclusion of ERP (extended producer responsibility) fees in pricing. The unfavourable market conditions are expected to continue in 2024, slowing down recovery. In 2023, the EBITDA margin has declined to 5.4% from the exceptional level of 7.1% in 2022 and is forecast to decline further to 4.2% in 2024. In the medium-term we expect Marso's EBITDA margin to recover and increase steadily towards 5%, which is below historical, pre-pandemic profitability levels of around 6%.

Financial risk profile: BB- (revised from BB)

Our assumptions regarding the group's financial risk profile include the fact that MARSO Kft. and MARSO Holding Kft. have cross-guarantees. As evidenced by the decline in export sales in 2023 and its expected further decrease, MARSO Holding Kft. (Marso's sister company, an operating company that sells tyres in the CEE region, outside of Hungary) may fall into financial distress separately from Marso.

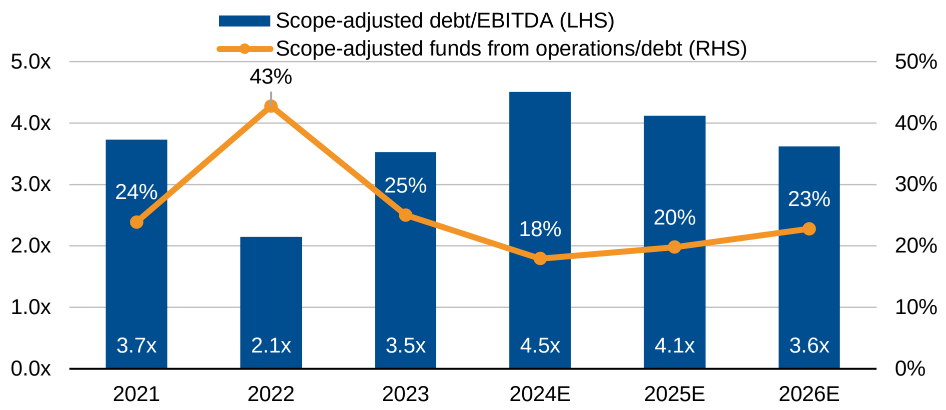
Marso's credit profile includes the HUF 3.6bn MNB bond issued in 2019 and an additional HUF 2.1bn in working capital loans under the Baross Gabor loan programme (which provides favourable, fixed interest rates to SMEs), complemented by the HUF 1.2bn warranty Marso has provided for MARSO Holding Kft.'s loans. The profile is forecasted to remain broadly unchanged. The company is expected to utilise short-term working capital loans seasonally during the year when needed, typically twice (in Q1 and Q3), repaying as soon as cash generation allows, thus historically not impacting the year-end profile.

Relatively strong interest coverage

The financial risk profile continues to benefit from relatively high interest coverage as the majority of company debt has fixed interest rates (both for the NKP bond and for the Baross Gabor loans). The refinanced, fixed-rate loans are scheduled to mature in 2025 and 2026, which will sustain relatively strong interest coverage between 4x-7x in the coming years.

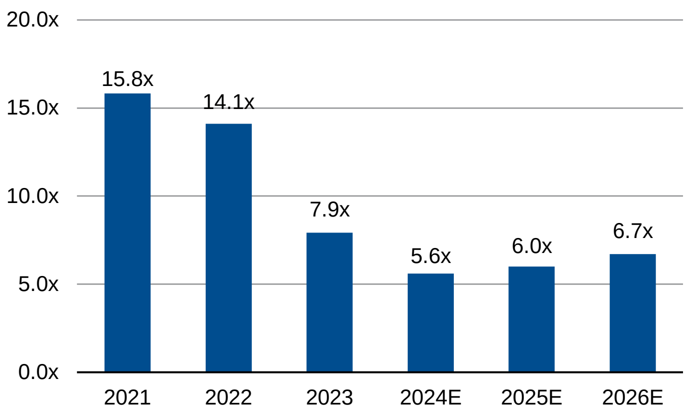
Credit metrics are forecasted to continue to deteriorate with the sustained decline in profitability, they will be negatively impacted by the unfavourable market conditions in 2024 and 2025. In 2023, debt/EBITDA increased to 3.5x from 2.1x in 2022. From 2023 onwards we have applied a 50% haircut to the company's cash amount as it is not considered to be permanent due to (i) the business contraction in 2023; (ii) the high cash absorption of the company's business model (Marso finances its biannual inventory build-up – typically in Q1 and Q3 – through its cash reserves and additional short-term credit lines.); and (iii) the overall declining credit quality. In addition, the exceptionally high cash balance at YE 2023, resulting from the decline in net working capital due to the experienced business contraction, is not considered to represent a sustainable level of cash going forward. These adjustments, together with the depressed Scope-adjusted EBITDA are expected to result in further increase in debt/EBITDA to around 4.5x in 2024. The funds from operations/debt ratio and cash flow coverage are also expected to deteriorate in 2023 dropping to 18% and 0% respectively from 25% and 22% in 2023.

Figure 2: Leverage



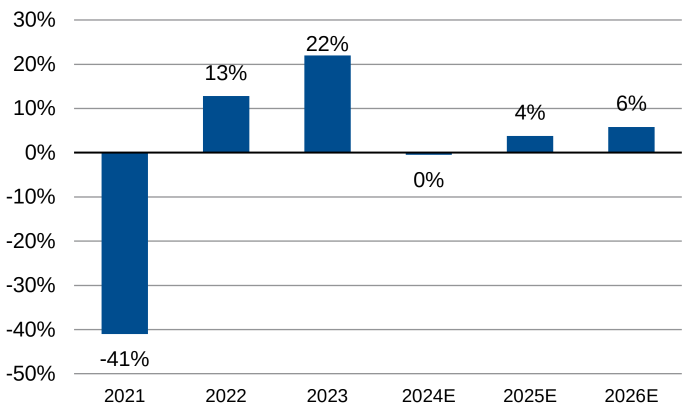
Sources: Marso, Scope estimates

Figure 3: Interest cover



Sources: Marso, Scope estimates

Figure 4: Cash flow cover



Sources: Marso, Scope estimates

Adequate liquidity

Liquidity is adequate, the assessment is supported by the ample cash and cash equivalents and moderate free operating cash flow after 2024, which is expected to cover two large upcoming maturities scheduled for 2025 and 2026 (HUF 1.3bn and HUF 0.8bn Baross Gabor loans respectively). However, we note that Marso's interim cash levels are volatile due to the highly seasonal nature of the business. Nevertheless, the liquidity is still considered to be adequate as inventories can also be seen as an alternative source of liquidity.

We highlight that Marso's senior unsecured bond has a covenant requiring the accelerated repayment of the outstanding nominal debt amount (HUF 3.6bn) if the debt rating of the bond stays below B+ for more than two years (grace period) or drops below B- (accelerated repayment within 10 business days after public announcement). Such a development could adversely affect the company's liquidity profile. The rating headroom to entering the grace period is 1 notch. We therefore see no immediate risk of the rating-related covenant being triggered.

Balance in HUF m	2023	2024E	2025E
Unrestricted cash (t-1)	2,011	4,102	3,821
Free operating cash flow	1,591	-33	272
Short-term debt (t-1)	50	79	1,255
Coverage	**>200%**	**>200%**	**>200%**

Long-term debt rating

Senior unsecured bond rating (ISIN: HU0000359393): BB-

In December 2019, Marso issued a HUF 3.6bn senior unsecured bond through the Hungarian central bank's Bond Funding for Growth Scheme. The bond is guaranteed by MARSO Holding Kft., which belongs to the same corporate group as Marso. The bond proceeds were used for warehouse capex. The bond has a tenor of 10 years and a fixed coupon of 2.3%. Bond repayment is in three tranches starting from 2027, with 33.3% of the face value payable yearly. Bond covenants in addition to the rating deterioration covenant include non-payment, insolvency proceedings, cross-default, pari passu, negative pledge, change of control and dividend payment covenants.

Our recovery analysis indicates an 'above-average' recovery estimated in a hypothetical default scenario in 2026, which is based on the issuer's liquidation value and an assumed outstanding senior secured debt of HUF 2.0bn and warranty of HUF 1.2bn with available credit lines fully drawn. This allows for a one-notch uplift compared to the underlying issuer rating, leading to the debt rating of BB-.

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