CSABAcast Kft.
Hungary, Automotive Supplier

B+ STABLE

Corporate profile

CSABAcast Kft., based in Hungary, was founded in 2008 as the successor of ADAcast Könnyűfémöntöde Kft. Its main activities are the production of high-pressure aluminium die casts, surface treating, machining and assembly. CSABAcast is a tier-one supplier to German car OEMs such as BMW and Volkswagen. It offers gear parts (e.g. engine brackets), motor parts (e.g. cylinder head covers) and transmission parts (e.g. housing for transmission). CSABAcast is a limited liability company with no subsidiaries. The company is managed by Bela Hetzmann (CEO and second largest shareholder) and László Boronkay. The Majoros family owns 50% of CSABAcast Kft. CSABAcast has around 450 employees and reported preliminary revenues of HUF 14.6bn and adjusted EBITDA of HUF 2.9bn in 2019P[1].

Key metrics

			Scope estimates	
Scope credit ratios	**2018**	**2019P**	**2020F**	**2021F**
EBITDA/interest cover (x)	35.5x	45.3x	27.2x	22.1x
Scope-adjusted debt (SaD)/EBITDA	1.6x	1.5x	2.0x	1.8x
Scope-adjusted funds from operations/SaD	55%	72%	45%	51%
Free operating cash flow/SaD	-6%	0%	3%	3%

Rating rationale

Scope Ratings assigns a B+ first-time issuer rating to CSABAcast Kft., with Stable Outlook. Scope also assigns a first-time credit rating of B+ to the senior unsecured debt category.

CSABAcast plans to issue a HUF 1.5bn bond under the Bond Funding for Growth Scheme of the Hungarian National Bank (MNB) and to use the proceeds for financing investments in its new factory.

CSABAcast's B rated business risk profile is constrained by its weak market position, low diversification and high concentration on the customer side. With revenues of HUF 14.6bn in 2019 (~EUR 45m) and EBITDA of HUF 3.3bn (~EUR 10m), CSABAcast is a very small automotive supplier in Europe, in a very fragmented market. With aluminium castings accounting for around 92% of total revenues, CSABAcast is largely a single-product company with a narrow range of additional products. Diversification is also weakened by the high dependence on a few products, with its top-selling product accounting for around 13% of revenues in 2019 and the top five for 37%. Another credit-negative is the very limited share of aftermarket activities, at 0.25% of revenues, which usually help to reduce volatility and boost profitability. Negatively, we note CSABAcast's lack of offerings in the growing segment of full electric cars. Diversification is also held back by the excessive dependence on a small number of customers.

Profitability is the major supportive factor for the business risk profile. The company's Scope-adjusted EBITDA margin has ranged between 16% and 20% in last five years. CSABAcast's one-off adjusted EBITDA margin was 19.9% in 2019P.

[1]P denotes the use of preliminary figures.

Ratings & Outlook

Corporate ratings	B+/Stable
Senior unsecured rating	B+

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Related Methodologies

Corporate Rating Methodology, February 2020

Rating Methodology European Automotive Suppliers January 2020

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Volatility is medium as CSABAcast's flexible cost structure can mitigate negative effects from its high dependence on highly cyclical OEM volume sales, very low share of aftermarket business and high exposure to fluctuations in aluminium prices. We hold a positive view on the solid order backlog of around HUF 40bn (sales backlog ratio of 2.8x).

CSABAcast plans to reduce its cost base to counteract the expected drop in revenues in 2020F[2]. Specifically, it plans to reduce leased-employee headcount, working hours, and salaries. In view of the flexible cost structure, we expect a decrease in EBITDA margin to be limited, to around 17.5% in 2020F.

CSABAcast's overall rating is supported by its BBB- rated financial risk profile. The group's financial debt amounted to HUF 4.8bn at year-end 2019P. We expect Scope-adjusted debt (SaD) of HUF 3.9bn at year-end 2020F. We also calculate a SaD/EBITDA ratio of 1.5x at year-end 2019P and around 2.0x at year-end 2020F. We believe the flexible cost structure will help to avoid a sharper increase. The investment cycle has weighed on cash flow cover, resulting in a very weak free operating cash flow (FOCF)/SaD ratio between 2016 and 2019P. Due to the expected fall in earnings, we anticipate the FOCF/SaD ratio to remain weak in 2020F and 2021F.

CSABAcast's liquidity and financial flexibility are adequate. Liquidity is supported by available cash sources (cash balance of around HUF 526m at year-end 2019P and undrawn credit lines of around HUF 1.2bn) and no significant debt payments due in 2020F and 2021F.

Outlook and rating-change drivers

The Stable Outlook reflects the successful placement of the HUF 1.5bn MNB bond, the solid order backlog at year-end 2019 and our expectation of a recovery in CSABAcast's operations after the 2020F slump. The Outlook further reflects the successful ramp-up of the new plant and CSABAcast's ability to retain its main customers. It also reflects our current expectation that the SaD/EBITDA ratio will remain within the 1.5x-2.0x range in 2021F and the FOCF/SaD ratio will continue to be weak.

While currently considered as a remote possibility, the rating may be upgraded if CSABAcast can improve its business risk profile, for instance, through customer concentration risks and/or product diversification while maintaining the current credit metrics.

A negative rating action could result if operations do not recover in 2021F and/or a major customer is lost. A downgrade is also possible if SaD/EBITDA reached above 3.5x on a sustained basis, for instance, due to acquisitions. A more aggressive-than-anticipated dividend policy could also trigger a negative rating action.

[2] F denotes the use of forecasted figures.

Rating drivers

Positive rating drivers	Negative rating drivers
• Good profitability, shown by a Scope-adjusted EBITDA margin of between 16% and 20% in last five years, and a one-off adjusted EBITDA margin of 19.9% in 2019P • Relatively flexible cost structure, which helps to mitigate volatility from dependence on highly cyclical OEM volume sales and very low share of aftermarket business • Sound financial profile with a SaD/EBITDA ratio of 1.5x at year-end 2019P • Solid order backlog with around HUF 40bn (sales backlog ratio: 2.8x) • Ramp-up of new site expected to increase revenues and support profitability in the medium term	• Very small niche automotive supplier in Europe, a very fragmented market, with revenues of HUF 14.6bn in 2019 (~EUR 45m) and EBITDA of HUF 3.3bn (~EUR 10m) • Low diversification and high dependence on a few products (five top-selling products: 37% of revenues in 2019); 81% of revenues in a single country • High concentration of customers, with largest accounting for 52% in revenues in 2019 • No offerings in the growing segment of full electric cars • Very limited aftermarket activities (0.25% of revenues), which usually help to reduce volatility and boost profitability • High substitution risk

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Improvements of the business risk profile, for instance, through customer concentration risks and/or product diversification; however, this is a remote scenario	• No business recovery in 2021F and/or loss of a major customer • SaD/EBITDA of above 3.5x on a sustained basis, for instance, due to acquisitions • More aggressive-than-expected dividend policy

Financial overview

			Scope estimates	
Scope credit ratios	**2018**	**2019P**	**2020F**	**2021F**
EBITDA/interest cover (x)	35.5x	45.3x	27.2x	22.1x
Scope-adjusted debt (SaD)/EBITDA	1.6x	1.5x	2.0x	1.8x
Scope-adjusted funds from operations/SaD	55%	72%	45%	51%
Free operating cash flow/SaD	-6%	0%	3%	3%
Scope-adjusted EBITDA in HUF m	**2018**	**2019P**	**2020F**	**2021F**
EBITDA	2,047	3,250	1,967	2,514
Operating lease payments in respective year				
Other	100	-350		
Scope-adjusted EBITDA	2,147	2,900	1,967	2,514
Scope-adjusted funds from operations in HUF m	**2018**	**2019P**	**2020F**	**2021F**
EBITDA	2,047	3,250	1,967	2,514
less: (net) cash interest as per cash flow statement	-60	-64	-72	-114
less: cash tax paid as per cash flow statement	-14	-26	-3	-12
add: depreciation component, operating leases				
Other items	-121	-72	-120	-120
Scope-adjusted funds from operations	1,852	3,088	1,771	2,269
Scope-adjusted debt in HUF m	**2018**	**2019P**	**2020F**	**2021F**
Reported gross financial debt	4,137	4,808	5,970	5,008
less: hybrid bonds				
less: cash and cash equivalents	-782	-526	-2,069	-576
add: cash not accessible				
add: pension adjustment				
add: operating lease obligations				
Other				
Scope-adjusted debt	3,355	4,282	3,901	4,432

Business risk profile: B

CSABAcast's business risk profile is rated B, constrained by its weak market position, low diversification, and high concentration risks in terms of customers.

Very small niche automotive supplier in Europe

With revenues of HUF 13bn in 2018 (~EUR 36m) and EBITDA of HUF 2.0bn (~EUR 5.6m), CSABAcast is a very small niche automotive supplier in Europe. The relevant market on the supply side is highly fragmented. CSABAcast's main competitors are Hungarian companies Fémalk Metal Casting, Ecseri Aluminium Casting, Prec-Cast Casting, and Csaba Metál Casting as well as dozens of aluminium die-casting companies in Germany, Austria, Poland, Slovakia, Slovenia, Italy, Turkey, Israel and India. The company's market position is supported mainly by its central European location, which affords access to lower-cost labour than in western Europe, and by longstanding relations with its main customers, BMW, Volkswagen, Audi, Škoda, and SEAT (25 years).

Largely a single-product company with a narrow range of additional products

With aluminium castings accounting for around 92% of total revenues, CSABAcast is largely a single-product company with a narrow range of additional products. However, CSABAcast's aluminium die-castings are used for different car components such as motors, gears and chassis parts, with a smaller portion (12% of revenues in 2019) used for white goods.

High dependence on a few products

Diversification is constrained by the relatively high dependence on a few products: the top-selling product accounted for around 13% of revenues in 2019 and the top five for 37%. Product diversification is also weakened by the limited number of aftermarket activities (0.25% of revenues), which usually help to reduce volatility and boost profitability.

Limited geographical diversification

Geographical diversification is another rating constraint. 81% of CSABAcast's revenues in 2019 stemmed from Germany, mainly from automotive OEMs, with the rest distributed among eight European countries. Also, the company's manufacturing capacities are exclusively in Hungary but around 98% of revenues are generated in foreign currencies, in particular euros. According to company, it does not use hedging instruments. However, there is a natural hedge to a certain extent, as 90%-95% of purchases (such as of aluminium, energy, auxiliary materials, machines and spare parts) are in euros. Moreover, all credit lines and leasing contracts are in euros. Only salaries (~17% of revenues) and taxes are paid in Hungarian forint.

Currently no offerings in the growing full electric cars segment

Credit-negative is CSABAcast's lack of offerings in the growing segment of full electric cars. The company, however, plans to launch projects to gain a foothold in this market, with more details to be announced in H2 2020.

Excessive dependence on a few customers

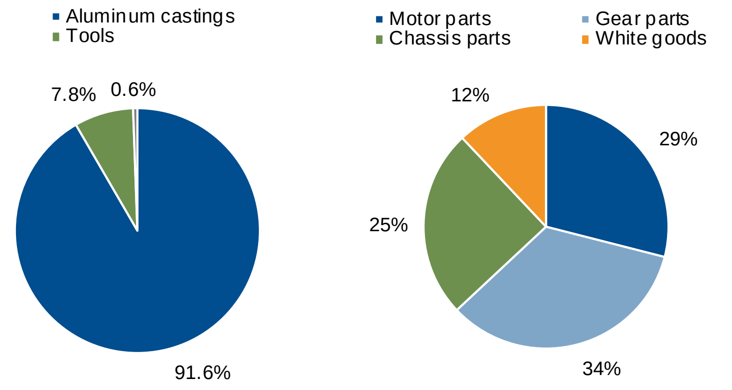
Customer diversification is also weak. CSABAcast had only four customers in 2019: BMW AG, Volkswagen Group, Miele and NIDEC GPM. BMW AG accounted for the largest share of 2019 revenues (52%). Around 24% of 2019 revenues stemmed from Volkswagen Group, but this dependency is relativized by the fact that CSABAcast supplies to different companies and brands at different manufacturing sites, which order on a separate basis. Customer concentration will increase in 2020, as CSABAcast expects to lose its third largest customer, Miele, as it has decided to use stainless steel instead of aluminium for its washing-machine drum flanges due to the chemical structure of new detergents.

Significant risk of substitutability

We believe substitution risk to be significant as CSABAcast's products are relatively unsophisticated. This risk is mitigated by CSABAcast's provision of around 60 different products to its main customer, BMW, which would make the company's substitution with another supplier complex, costly and lengthy (CSABAcast estimates additional costs of EUR 8m-10m and the process to take at least two years).

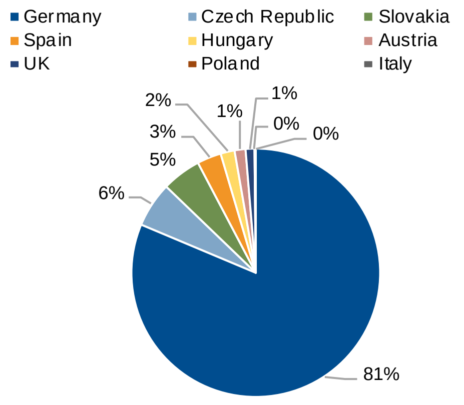
Figure 1: Revenue breakdown 2019P

By product group **By product application**



Source: CSABAcast, Scope

Figure 2: Revenue breakdown by geography 2019P



Source: CSABAcast, Scope

Profitability a major support for the business risk profile

Profitability is the major supportive factor for the business risk profile. Volatility is medium as the company's flexible cost structure can mitigate negative effects from its dependence on highly cyclical OEM volume sales, very low share of aftermarket business and high exposure to fluctuations in aluminium prices.

Order backlog of around HUF 40bn at year-end 2019

After restarting with new management in 2008, CSABAcast's revenues increased significantly and reached full capacity (EUR 30m-35m in revenues) in 2015 (Figure 3). In 2016, CSABAcast started to build a new, larger plant with a capacity of up to EUR 55bn in revenues. According to preliminary numbers, revenues in 2019P grew by around 10% to HUF 14.6bn. In addition, CSABAcast has an order backlog of around HUF 40bn.

Figure 3: **12-year trend in revenue and EBITDA**

HUF m	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019P
Revenues	**2,437**	**3,697**	**3,310**	**4,403**	**4,256**	**5,600**	**8,123**	**10,256**	**9,710**	**10,702**	**13,247**	**14,605**
Year over year		*51.7%*	*-10.5%*	*33.0%*	*-3.3%*	*31.6%*	*45.0%*	*26.3%*	*-5.3%*	*10.2%*	*23.8%*	*10.2%*
EBIT	**145**	**295**	**115**	**245**	**75**	**407**	**949**	**1,478**	**1,397**	**935**	**929**	**1,779**
Margin	*6.0%*	*8.0%*	*3.5%*	*5.6%*	*1.8%*	*7.3%*	*11.7%*	*14.4%*	*14.4%*	*8.7%*	*7.0%*	*12.2%*
Depreciation and amortisation	-4	-49	-101	-151	-199	-300	-404	-535	-566	-701	-1,118	-1,471
EBITDA	**150**	**345**	**217**	**396**	**274**	**706**	**1,353**	**2,013**	**1,964**	**1,885**	**2,147**	**2,900**
Margin	*6.1%*	*9.3%*	*6.5%*	*9.0%*	*6.4%*	*12.6%*	*16.7%*	*19.6%*	*20.2%*	*17.6%*	*16.2%*	*19.9%*

Source: CSABAcast, Scope

Transition period in 2018 and 2019

It should be noted that the 2018-19 years marked a transition period in which production took place at two sites. From 2020F, CSABAcast will produce only at the new site. Based on preliminary numbers, CSABAcast's one-off adjusted EBITDA margin was 19.9% in 2019P. The increase compared to the 2018 level of 16.2% was due to a lower material cost ratio (62.2% in 2019 vs 64.1% in 2018), reflecting lower aluminium alloy prices. Lower margins during 2017-18 were due to higher personnel expenses stemming from production at two sites. The company expects to reach full capacity utilisation in 2023F, which equates to EUR 50m-55m in revenues (HUF 16.5bn-18bn).

Expected revenue drop in 2020F; recovery in 2021F

The shutdown of plants combined with weak demand expected in the automotive sector, particularly in 2020F, is expected to have a negative impact on CSABAcast's revenues, which we forecast to drop by 23% in 2020F to around HUF 11.2bn. We foresee a recovery by 16% in 2021.

Cost-cutting to support profitability

CSABAcast plans to reduce costs to counteract the expected drop in revenue during 2020F. Specifically, it plans to reduce the leased-employee headcount, working hours, and salaries. We therefore expect the decrease in EBITDA margin to be limited to just 17.5% in 2020F, before recovering to around 19% in 2021F on the back of higher expected revenues. Profitability should also benefit from i) the lower material cost ratio due to the loss of Miele as a customer, as the parts used for Miele products (special shafts for washing machines) had a higher value; and ii) the loss of rental payments (around HUF 160m annually), as CSABAcast fully owns the new site.

Ramp-up of the new site should drive revenues in the mid-term

The new site should drive CSABAcast's revenues and support profitability in the medium term. Moreover, proceeds from the planned MNB bond are intended for projects to automate processes, which should also support profitability in the medium term.

Financial risk profile: BBB-

BBB- rated financial risk profile

CSABAcast's overall rating is supported by its BBB- rated financial risk profile. Debt of HUF 4.8bn at year-end 2019P included HUF 1.4bn of investment and development credits and a HUF 1.7bn working capital loan. According to CSABAcast, it has no operating leases and does not use factoring.

The increase in debt since 2016 is due to the new plant's construction. The increase by around HUF 900m compared to year-end 2018 is due to negative free operating cash flow reflecting mainly the higher net working capital. We expect SaD of HUF 3.9bn at year-end 2020F. CSABAcast plans to gradually reduce debt in the coming years using cash flow.

Figure 4: Composition of external financing at end-December 2019P

Debt instrument	Currency	Amount (EUR m)	Drawn (HUF m)	Coupon	Maturity	Issuer	Leverage
Investment and development credit	EUR	6	1,269		2023	CSABAcast Kft.	0.4x
Other bank debt			3,271		Amortising	CSABAcast Kft.	1.1x
Financial leasing			268		Amortising	CSABAcast Kft.	0.1x
Senior secured debt			**4,808**				**1.7x**
Total debt (as reported)			**4,808**				1.7x
Adjustments for:							
Pensions							
Operating leases							
Factoring							
Scope-adjusted gross debt (HUF m)			**4,808**				**1.7x**
Unrestricted liquidity			-526				-0.2x
Scope-adjusted debt (HUF m)			**4,282**				**1.5x**

Source: CSABAcast, Scope

SaD/EBITDA ratio of 1.5x at year-end 2019P

We calculate a SaD/EBITDA ratio of 1.5x at year-end 2019P. While showing some fluctuation, this ratio has remained below 2.0x over the last six years (Figure 5). We expect the SaD/EBITDA ratio to reach around 2.0x at year-end 2020F. However, we believe the flexible cost structure will help to avoid a sharper increase. We expect the anticipated recovery in earnings to lead to a lower SaD/EBITDA ratio of 1.8x at year-end 2021F.

The investment cycle has weighed on cash flow cover, resulting in a weak FOCF/SaD of between 2016 and 2019P. Based on the expected fall in earnings, we expect the FOCF/SaD ratio to remain weak in 2020F and 2021F.

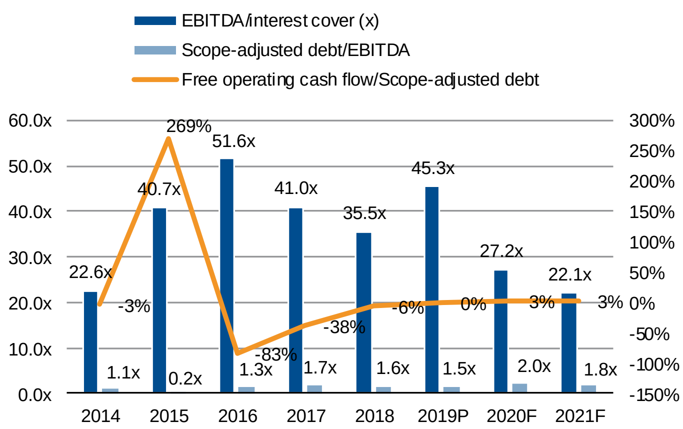
CSABAcast's operating cash flow was HUF 1.9bn in 2019P. The decrease from HUF 2.5bn in 2018 was due to a significant increase in net working capital. Net capex of HUF 2.1bn remained flat year-on-year, still significantly above the maintenance capex of around HUF 1.0bn, due mainly to investments in tools. The increase in net working capital also resulted in FOCF turning negative to -HUF 177m (2018: HUF 371m).

High capex in 2016 and 2017 is associated with the new plant's construction.

Slightly positive FOCF expected for 2020F and 2021F

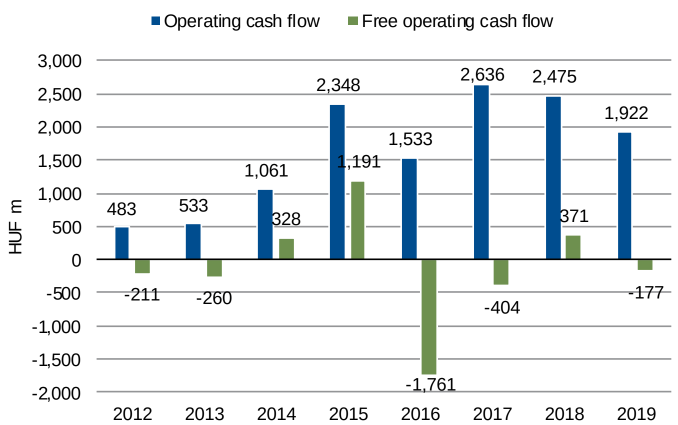
In 2020F, we expect lower net working capital and lower capex to offset most of fall in profits and anticipate FOCF to be only slightly negative. In line with the expected increase in earnings, we anticipate a slightly positive FOCF in 2021F.

Figure 5: Key credit metrics 2014 to 2021F



Source: CSABAcast, Scope

Figure 6: Eight-year trend in cash flow



Source: CSABAcast, Scope

Covenants

No financial covenants

There are no financial covenants, according to CSABAcast. The main non-financial covenants are as follows:

- Under the loan agreement with Unicredit Bank Hungary, the bank must provide its consent before CSABAcast raises a credit or concludes a lease contract with another financial institution, or sells shares;
- Dividend payout level must remain below 30% of profits;
- 70% of revenues must stem from exports, of which 50% must be manufactured in Hungary; and
- Export restrictions to certain countries must be complied with.

Liquidity

Adequate liquidity and financial flexibility

CSABAcast's liquidity and financial flexibility as adequate.

Cash sources comprise:

- HUF 526m of cash at year-end 2019P;
- EUR 1.25m (~ HUF 450m) undrawn overdraft facility due in September 2020, which will be replaced with a new facility;
- EUR 2m (~ HUF 720m) credit line available for any use, even for dividends (but not in 2020), due in March 2025;
- HUF 250m of cash from state subsidies; and
- Around HUF 150m of free operating cash flow in 2020F and 2021F.

We expect the following contractual and potential uses of liquidity:

- Around HUF 660m of dividend payments in FY 2021F; and
- Around HUF 340m of debt maturities in 2020F (including HUF 146m in lease payments) and around HUF 960m in 2021F.

At the beginning of 2020, CSABAcast entered into the following new credits:

- EUR 5.2m working capital loan to replace the existing working capital loan due in September 2022;
- EUR 2.0m loan available for any use, even for dividends, due in March 2025; and
- EUR 1.25m overdraft facility.

These new lines will have no financial covenants and rank pari passu with existing loans.

Assuming the successful placement of the MNB bond, we expect a cash balance of around HUF 2.1bn at year-end 2020F.

Short-term debt coverage (internal and external) of more than 1x for 2020F and 2021F

Based on the moratorium on corporate and household loan instalments as well as available cash sources (assuming the successful placement of the HUF 1.5bn MNB bond), we expect short-term debt coverage (from internal and external sources) of more than 1x for 2020F and 2021F.

Financial policy

Dividend policy is being monitored

CSABAcast's financial policy is credit-neutral. There were no aggressive M&A or dividend payments in previous years. The balance sheet is solid, reflected in the low SaD/EBITDA ratio and sufficient disposable credit lines available for any use. Having said that, we will continue to monitor CSABAcast's dividend policy, which is limited by a bank covenant that requires payouts to be below 30% of the net result. However, CSABAcast's main bank has consented to HUF 1bn in extra dividends after the new plant is completed. Around HUF 330m of dividends were paid in 2019P in advance (official approval has to be provided at the annual general meeting) on top of the normal dividend of HUF 220m. The remaining HUF 660m, initially planned for 2020E, will be paid in 2021E after CSABAcast's main bank requested its postponement. Based on the dividend covenant and our projections, we anticipate HUF 200m of dividend payments in 2022F.

Long-term and short-term debt ratings

'Average' recovery for senior unsecured debt

B+ rating for senior unsecured debt (HUF 1.5bn)

CSABAcast plans to issue a HUF 1.5bn bond under the MNB Bond Funding for Growth Scheme. We have assumed the planned bond to be senior unsecured. Bond proceeds are planned for investments in the new plant. According to CSABAcast, its available loans are secured by mortgages. Our recovery analysis is based on a liquidation value in a hypothetical default scenario in 2021 of HUF 5.6bn. This value assumes a 50% haircut and 10% in liquidation costs on assets. We assume the business plan can be executed without the need for additional bank debt or other senior-ranked financing. We expect an 'average' recovery for senior unsecured debt (HUF 1.5bn) and therefore assign a debt class rating at the same level as the issuer rating of B+.

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