MARSO Kft.
Hungary, Retail

SCOPE BB- STABLE

Corporate profile

MARSO Kft is a leading wholesale tyre retailer in Hungary. MARSO developed its position through strong relationships with both suppliers and customers. The company has closed exclusive agreements with some of the largest global tyre retailers (e.g. Michelin, Bridgestone, Continental) and deepened customer loyalty via different selling networks.

Key metrics

			Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**
EBITDA/interest cover (x)	13.3x	19.8x	7.4x	8.1x
Scope-adjusted debt (SaD)/EBITDA	2.1x	1.8x	4.0x	3.9x
Scope-adjusted funds from operations/SaD	41%	51%	21%	22%
Free operating cash flow/SaD	-18%	24%	-51%	1%

Rating rationale

Scope Ratings GmbH (Scope) has affirmed the BB-/Stable issuer credit rating on Hungarian tyre wholesaler MARSO Kft. along with its BB long-term senior unsecured debt rating.

The affirmation reflects MARSO's resilient business model and stable performance amid both the Covid pandemic and the general decline in the imported tyre market. With investment in its new logistics centre in Dunaharaszti set to conclude in 2021, MARSO will have expended bond proceeds and will thus utilise long-term debt to refinance its short-term debt and finance its increased working capital needs. This will result in a deterioration of the company's financial risk profile, though to a level commensurate with the rating. The Stable Outlook reflects the expectation of a Scope-adjusted debt (SaD)/EBITDA ratio of between 3-4x for the coming years, assuming no further debt is utilised.

The issuer rating continues to reflect MARSO's high market share. The comparatively strong financial risk profile also supports the rating. The rating is, however, hindered by MARSO's small size, weak diversification and weak cash flow cover.

We expect an 'excellent' recovery for senior unsecured debt, which supports the BB rating for the debt category.

Ratings & Outlook

Corporate rating	BB-/Stable
Senior unsecured rating	BB

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Related Methodologies

Corporate Rating Methodology: July 2021

Rating Methodology: Retail and Wholesale Corporates March 2021

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Bloomberg: RESP SCOP

Outlook and rating-change drivers

The Stable Outlook reflects Scope's expectation that MARSO will have expended its bond proceeds by the end of 2021 due to the end of the investment programme and will thus utilise long-term loans. The increased SaD/EBITDA as a result is still likely to remain commensurate with the rating, at an expected range of 3-4x for the coming years.

A positive rating action could be triggered if MARSO's premiumisation strategy strengthened the Scope-adjusted EBITDA margin and SaD/EBITDA reached below 3x on a sustained basis, for example, through an efficient management of working capital.

A negative rating action could be triggered if SaD/EBITDA reached above 4x on a sustained basis, as a potential consequence of the new strategy not lifting the EBITDA margins or a further significant working capital expansion.

Rating drivers

Positive rating drivers	Negative rating drivers
• Dominating market share • Comparatively strong financial risk profile with high interest cover • High share of products sold exclusively	• Low diversification • Small company size in niche market with limited expansion possibility and high competition • Increased SaD and leverage after bond proceeds used due to higher-than-expected increase in long-term debt

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• SaD/EBITDA of below 3.0x on a sustained basis • Premiumisation strategy strengthens profitability	• SaD/EBITDA of above 4.0x on a sustained basis

Financial overview

			Scope estimates	
Scope credit ratios	**2019**	**2020**	**2021E**	**2022E**
EBITDA/interest cover (x)	13.3x	19.8x	7.4x	8.1x
Scope-adjusted debt (SaD)/EBITDA	2.1x	1.8x	4.0x	3.9x
Scope-adjusted funds from operations/SaD	41%	51%	21%	22%
Free operating cash flow/SaD	-18%	24%	-51%	1%
Scope-adjusted EBITDA in EUR m	**2019**	**2020**	**2021E**	**2022E**
EBITDA	1,114	1,322	1,258	1,325
Operating lease payments in respective year	474	559	582	543
Other	-	-	-	-
Scope-adjusted EBITDA	1,588	1,882	1,840	1,867
Scope-adjusted funds from operations in EUR m	**2019**	**2020**	**2021E**	**2022E**
EBITDA	1,114	1,322	1,258	1,325
less: (net) cash interest as per cash flow statement	-25	17	-131	-122
less: cash tax paid as per cash flow statement	-76	-95	-63	-51
add: depreciation component, operating leases	379	447	465	434
Other	2	2	-4	-
Scope-adjusted funds from operations	1,395	1,693	1,526	1,585
Scope-adjusted debt in EUR m	**2019**	**2020**	**2021E**	**2022E**
Reported gross financial debt	4,542	4,001	5,300	5,300
less: hybrid bonds	-	-	-	-
less: cash and cash equivalents	-3,181	-3,087	-381	-325
add: cash not accessible	100	100	100	100
add: pension adjustment	-	-	-	-
add: operating lease obligations	1,897	2,237	2327	2,170
Other	48	48	48	48
Scope-adjusted debt	3,407	3,301	7,394	7,293

Business risk profile

Business risk profile remains broadly unchanged, assessed at B+

MARSO has so far withstood the depressed conditions in automotive-related industries thanks to its dominance of the relevant wholesale tyre markets. Even so, the pandemic, combined with general market changes including the digitalisation of retail and customers' increased price sensitivity, has prompted MARSO to redefine its pricing strategy, though we expect no significant short-term impact. MARSO plans to cater to its extensive network of wholesalers by protecting their margins in comparison to retail customers.

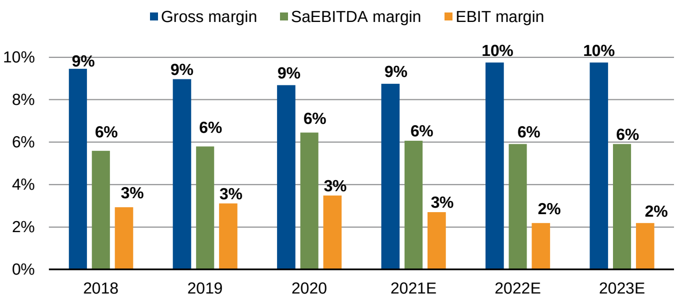
MARSO's business risk profile is supported by its dominant market position in Hungary. However, its company size and diversification remain negative rating drivers.

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 strong market position is mainly due to two factors: good relationships with suppliers, and a progressive integration of customers into a streamlined process.

MARSO has long-term commercial agreements with most major global tyre suppliers, leading to numerous exclusivity agreements (with Michelin, Nokian Tyres, and Continental, among many others). We consider these relationships to be durable as MARSO's relatively low margins enhance the related market shares of the suppliers. As of 31 December 2020, exclusive products represented close to 50% of total sales.

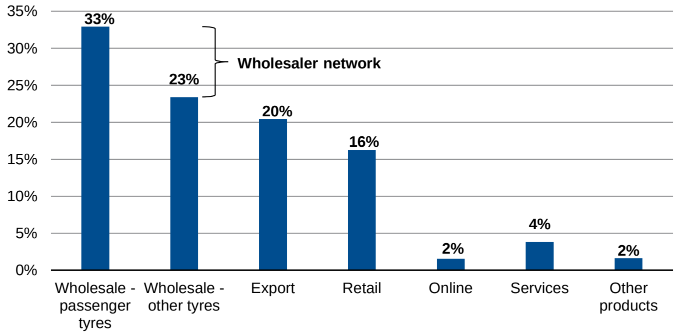
MARSO attracts customers with different types of offers. In 2020, close to 30 shops were operated as franchises, doubling the shop network from the previous year. These franchises, called MARSOponts, obtain the full product range and receive financial support from MARSO if needed. The company has also developed a network of customers under the 'MARSO Network Partner' label. These customers receive exclusive products and favourable commercial agreements in exchange for a royalty paid to MARSO. The two systems are supported by MOND, a web-shop platform.

Figure 1: Profitability



Source: Scope estimates

Figure 2: Sales diversification (YE 2020)



Source: MARSO, Scope

While MARSO's market share is high, which is a positive rating driver, it remains a small retailer due to its market's small absolute size and fierce competition, even with the benefits afforded by MARSO's exclusivity programme (e.g. low substitution risk).

Diversification is one of the weakest factors in MARSO's business risk profile. MARSO is involved in only one category of consumer goods (automotive) and mainly one sales channel (bricks and mortar; 94% of sales). On the other hand, sales to international customers are higher than among rated peers, at around 20% of total sales, which is credit-positive.

The country with the highest sales, following Hungary, represents only 6% of total sales. This is too low to offset any negative macro developments in the company's core market of Hungary. We recognise the presence of multiple sales channels (wholesale, retail, online) but the predominance of wholesale does not help to strengthen diversification, as MARSO appears to be far from establishing an omnichannel sales structure.

MARSO's operating profit is expected to improve after the logistics centre is complete, through cost savings generated by lower rents and the company's ability to deliver products with its own fleet instead of through external companies. The new logistics centre will also allow MARSO to better service Budapest and the surrounding area and execute same-day shipping.

Financial risk profile

Financial risk profile assessed at BB+

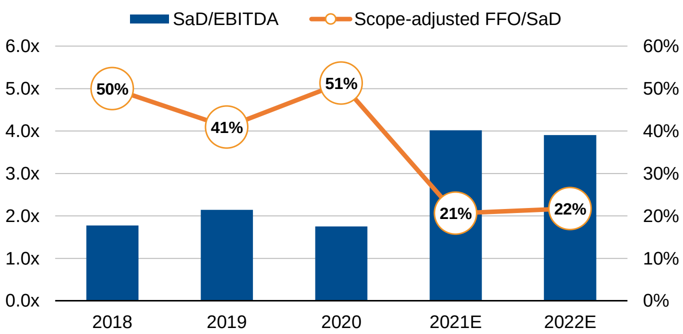
Our assumptions regarding the group's financial risk profile include the fact that MARSO Kft. and MARSO Holding Kft. hold a cross-guarantee system. Based on our assessment of the financial metrics of MARSO Holding Kft, a scenario in which only the holding entity falls into bankruptcy is unlikely.

Credit metrics are expected to remain commensurate with the current issuer rating. SaD/EBITDA is expected to remain within 3-4x, albeit with deterioration due to the higher-than-expected increase in long-term loans for 2021, funds from operations (FFO)/SaD at above 20%, and EBITDA interest cover at above 7x.

As is typical for companies in expansion, capex has taken a toll on free operating cash flow (FOCF) in 2021 and is expected to remain under pressure in the short to medium term. The construction of the warehouse is expected to be completed by YE 2021; therefore, we forecast that capex will be high until YE 2021.

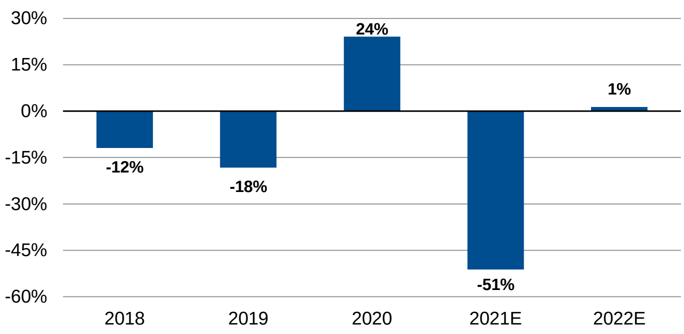
Liquidity is adequate. The temporary burden on the FOCF/SaD ratio due to negative FOCF during the current investment period and inventory stocking is not considered a negative rating driver.

Figure 3: Evolution of leverage metrics



Source: Scope estimates

Figure 4: Evolution of FOCF/SaD



Source: Scope estimates

Long-term debt ratings

The BB rating for senior unsecured debt has been affirmed. Recovery expectations for senior unsecured debt are 'excellent', even after senior secured debt (primarily consisting of the amortised long-term loan) has fully been covered, which supports the BB rating for the debt category. Recovery expectations are based on an expected liquidation value in a hypothetical default scenario in 2023.

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