Scope assigns issuer rating of B+ to AutoWallis, Stable Outlook

Market positioning and regional presence support the rating. The relatively high net leverage, low profitability and low product diversification are constraints. The Stable Outlook reflects the expected net leverage in the 4-5x range.

Rating action

Scope Ratings assigns a B+ first-time issuer rating to AutoWallis Nyrt., with a Stable Outlook. The senior unsecured debt category is rated B+.

Rating rationale

AutoWallis' issuer rating is supported by the BB- rated business risk profile. With approx. 70% of total revenues in 2018 generated through JaguarLandRover and BMW brands, AutoWallis is positioned towards the premium car segment. This segment is serviced by only a handful of manufacturers, with BMW the segment leader. AutoWallis has a five-year dealership contract with BMW, which we consider to represent a market entry barrier for competitors. In our view, AutoWallis' position as BMW retailer in Hungary is supported by its long partnership with BMW and the well-established brand. We note, however, that based on newly registered cars in Hungary, AutoWallis' market share was around 2% in 2018. This constrains the company's market positioning. In international distribution (this relates particularly to the wholesale segment for car marques JaguarLandRover, Isuzu and Ssangyong), the company benefits from being the exclusive distributor in several central and south-eastern European countries. AutoWallis' aftermarket business, though small in terms of revenues, is a major EBITDA contributor. Similar to the retail business, the company's aftermarket services are regulated by BMW, and we believe there are only a few contracted service providers for BMW in Hungary. AutoWallis has a solid market position in rental services, and is the only Hungarian company in the Sixt network. AutoWallis is market leader in airport car rental. Product diversification is a restraining factor for the company's business risk profile, with around 90% of revenues stemming from car sales. Some diversification is achieved through sales channels: retail accounts for around 30% of car sale revenues and wholesale for 60%. Diversification through the different marques is also limited, with the two premium ones, JaguarLandRover and BMW, accounting for around 70% of total revenues. The business risk profile benefits from the company's geographical positioning across 14 countries. Having said that, we note the strong dependence on two countries, Hungary and Croatia. Hungary represented 64% of total revenues in 2018, and the two countries combined represented 75%-80%. The low profitability is another constraint for the company's business risk profile. EBITDA margin was 3.4% in 2018, or around 4% when adjusting for operating leases. This is mainly attributable to automotive sales. The services business, on the other hand, is very profitable, contributing around 50% of total EBITDA in 2018 despite a very low revenue share.

AutoWallis' overall credit risk is held back by its B+ rated financial risk profile. Financial debt amounted to HUF 8.1bn at year-end 2018, mostly comprising inventory loans for the financing of the vehicle stock. We calculate Scope-adjusted debt (SaD) at HUF 10.0bn as at end-December 2018, derived by adjusting reported financial debt for operating leases totalling HUF 4.0bn. SaD to EBITDA was 3.7x at year-end 2018. The company is currently in a growth phase and we expect SaD to increase going forward. We expect SaD to rise to around HUF 14bn at year-end 2019, mainly due to the growth in Sixt leasing lines. AutoWallis plans to use the proceeds from the bond (we expect the company to raise HUF 3bn) to repay some of its existing credit lines, in particular to replace the operative leasing contracts of the Sixt franchisee and Wallis Motor Pest. We expect another increase for 2020E due to the planned acquisitions (AutoWallis plans to finance 70% of its acquisitions payment of around HUF 3bn through new debt). We understand that banks have signalled their willingness to provide additional debt for this purpose. The planned take-over of some entities from the parent company will be financed via a share exchange for in-kind contributions; cash will thus not be required. As result of the expected higher SaD, we anticipate that the group's net leverage will come in at around 4.7x at year-end 2019F. Leverage should remain above 4.5x in 2020F due to the relatively large M&A expected this year. Free cash flow was negative in 2017 and 2018 and we do not expect it to turn positive in the forecast period. Residual-value risk is limited as only 8% of the company's assets at year-end 2018 were exposed to this risk.

Based on our recovery analysis performed on the year 2020F we calculate a recovery rate of around 50% for senior unsecured debt. We therefore rate senior unsecured debt equal to the issuer rating.

Rating-change drivers

- Scope may upgrade the rating if profitability increased, for instance, through a higher percentage of services revenues and/or an improvement in SaD/EBITDA to below 3.5x on sustained basis.
- A negative rating action could be the result of a SaD/EBITDA of above 5.5x on a sustained basis, for example, due to higher-than-expected negative free cash flow and/or higher-than-expected payments for acquisitions. A negative rating action could be also triggered by the loss of important dealership/importer contracts and/or the usage of bond proceeds for purposes other than the aforementioned refinancing, e.g. larger debt-financed M&A transactions.

Stress testing

No stress testing was performed

Cash flow analysis

Scope performed its standard cash flow forecasting for the company.

Methodology

The methodologies used for these ratings and/or rating outlook (Corporate Rating Methodology) are available on www.scoperatings.com.

"Historical default rates of the entities rated by Scope Ratings can be viewed in the rating performance report on https://www.scoperatings.com/#governance-and-policies/regulatory-ESMA Please also refer to 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 definition of default as well as definitions of rating notations can be found in Scope's public credit rating methodologies on www.scoperatings.com.

The rating outlook indicates the most likely direction of the rating if the rating were to change within the next 12 to 18 months."

Solicitation, key sources and quality of information

The rating was not requested by the rated entity or its agents. The rated entity or its agents participated in the rating process. Scope had access to accounts, management and other relevant internal documents for the rated entity or related third party.

The following substantially material sources of information were used to prepare the credit rating: public domain, the rated entity and Scope internal sources.

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"Prior to the issuance of the rating or outlook action, the rated entity was given the opportunity to review the rating and outlook and the principal grounds on which the credit rating and outlook is based. Following that review, the rating was amended before being issued."

Regulatory disclosures

This credit rating and/or rating outlook is issued by Scope Ratings GmbH.

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The ratings/outlooks were first released by Scope on 17/09/2019.

Potential conflicts

Please see www.scoperatings.com. for a list of potential conflicts of interest related to the issuance of credit ratings.

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