AutoWallis Nyrt.
Hungary, Retail

B+ POSITIVE

Corporate profile

AutoWallis Nyrt. is a Hungarian holding company operating in the retail and wholesale sales of vehicles, parts and accessories; repair and maintenance services; and short- and long-term vehicle rentals. Brands represented by the group include BMW passenger cars and motorcycles, Citroen, Dacia, Isuzu, Jaguar, Kia, Land Rover, Maserati, Mini, Opel, Peugeot, Renault, Ssangyong, Toyota, Saab and Sixt Rent a Car. AutoWallis is 72.5% owned by Mr Tibor Veres through private equity firm Wallis Asset Management Zrt. In 2019, AutoWallis generated revenues of HUF 75bn and an EBITDA of HUF 3.1bn.

Key metrics

* Restated			Scope estimates		
Scope credit ratios	**2018***	**2019**	**2020F**	**2021F**	**2022F**
EBITDA/interest cover	11.6x	10.7x	4.6x	11.3x	13.4x
Scope-adjusted debt (SaD)/EBITDA	3.9x	3.6x	8.6x	4.4x	3.1x
Scope-adjusted funds from operations/SaD	20%	23%	8%	18%	25%
Free operating cash flow/SaD	-5%	26%	-36%	-35%	10%

Rating rationale

Scope Ratings has affirmed the B+ issuer rating on AutoWallis Nyrt. and revised the Outlook to Positive from Stable. Scope has also affirmed the B+ rating for the senior unsecured debt category.

AutoWallis announced six major transactions during 2020. Particularly worth mentioning is the acquisition of the importer rights for the Opel brand in Hungary, Croatia, Slovenia, and Bosnia and Herzegovina, which will add sales of around 12,500 cars in Hungary and around 11,700 cars in the three other countries. This is substantially more than AutoWallis' sales in 2019 (3,210 new cars in Hungary and 1,996 cars in the relevant non-Hungarian markets) and will thus improve Hungarian market share markedly to more than 13% from currently 2%. This supports the company's unchanged BB- rated business risk profile. We have an unchanged view on the company's credit supportive diversification, and profitability remains a constraining factor. We expect the adjusted EBITDA margin at between 2-3% in 2020 and 2021 (2019: 4.2%).

AutoWallis' B+ rated financial risk profile remains unchanged. Lower EBITDA and higher Scope-adjusted debt (SaD) is expected to lead to a sharp increase in the SaD/EBITDA ratio to around 8.5x at year-end 2020 (3.6x at year-end 2019). This ratio, however, is distorted as the recent transactions will not be fully reflected in the EBITDA. We expect the SaD/EBITDA ratio to recover into the 4.0-4.5x range in 2021, driven in particular by higher EBITDA reflecting the full-year effect of the transactions in 2020. We note positively AutoWallis' strategy to finance the recently announced and future transactions through share exchanges and/or capital increases.

We view AutoWallis' liquidity and financial flexibility to be adequate. This view is supported by the substantial inventories of around HUF 14bn at year-end 2019. Based on a 20% discount for inventories, we calculate short-term debt coverage at more than 100%.

Ratings & Outlook

Corporate rating B+/Positive

Senior unsecured rating B+

Analyst

Gennadij Kremer
+49 69 6677389 84
g.kremer@scoperatings.com

Related Methodology

Corporate Rating Methodology, February 2020

Scope Ratings GmbH

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Headquarters

Lennéstraße 5
10785 Berlin

Phone +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

Bloomberg: SCOP

Outlook and rating-change drivers

The Positive Outlook reflects the improved market position following the recent transactions, as well as Scope's expectation that the company will execute its growth plans through share exchanges and/or capital increases, leading to the SaD/EBITDA ratio advancing towards 3.5x by 2022. The positive rating outlook also reflects no dividend payouts over the next several years.

Scope may upgrade the rating if AutoWallis increases its profitability, for instance, through a higher percentage of services revenues, and/or if Scope's expectation of the SaD/EBITDA ratio of around 3.5x on a sustained basis is met.

A negative rating action could be triggered by a failure to improve SaD/EBITDA to around 3.5x on a sustained basis, e.g. due to lower-than-expected profitability and/or higher-than-expected debt after transactions are completed. A negative rating action could be also triggered by the loss of major dealership or importer contracts.

Rating drivers

Positive rating drivers	Negative rating drivers
• Solid market position: Hungary's largest dealer for BMW (approx. 49% market share) and Mini (approx. 83%); exclusive distributor for several brands in several central and south-eastern European countries; 2020 transactions to substantially increase Hungarian market share (to more than 13% from 2% in 2019) • Solid presence of 14 countries • Financing strategy without straining the balance sheet	• Relatively high net leverage, expected to remain high due to the expansion • Weak internal cash flow generation due to growth in inventories, with negative free cash flow in 2020 and 2021 • Low profitability: expected EBITDA margin of 2-3% for 2020 and 2021 (around 4% in 2019) • Weak product diversification, with around 90% of revenues from car sales

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• SaD/EBITDA of around 3.5x on sustained basis • Higher profitability, e.g. through higher percentage of services revenues	• Failure to improve SaD/EBITDA to around 3.5x on a sustained basis, e.g. due to lower-than-expected profitability and/or higher-than-expected debt after transactions complete • Loss of important dealership or importer contracts

Financial overview

* Restated			Scope estimates		
Scope credit ratios	**2018***	**2019**	**2020F**	**2021F**	**2022F**
EBITDA/interest cover	11.6x	10.7x	4.6x	11.3x	13.4x
SaD/EBITDA	3.9x	3.6x	8.6x	4.4x	3.1x
Scope-adjusted funds from operations/SaD	20%	23%	8%	18%	25%
Free operating cash flow/SaD	-5%	26%	-36%	-35%	10%
Scope-adjusted EBITDA in HUF m	**2018***	**2019**	**2020F**	**2021F**	**2022F**
EBITDA	2,621	3,125	1,839	6,109	7,903
Operating lease payments in respective year					
Other			158		
Scope-adjusted EBITDA	2,621	3,125	1,997	6,109	7,903
Scope-adjusted funds from operations in HUF m	**2018***	**2019**	**2020F**	**2021F**	**2022F**
EBITDA	2,621	3,125	1,839	6,109	7,903
less: (net) cash interest as per cash flow statement	-226	-291	-430	-540	-590
less: cash tax paid as per cash flow statement	-364	-265	-151	-964	-1,341
add: depreciation component, operating leases					
Scope-adjusted funds from operations	2,031	2,569	1,257	4,605	5,972
Scope-adjusted debt in HUF m	**2018***	**2019**	**2020F**	**2021F**	**2022F**
Reported gross financial debt	11,876	13,048	20,872	28,170	32,081
less: cash and cash equivalents	-1,535	-1,891	-3,681	-1,557	-7,709
add: cash not accessible					
add: pension adjustment					
add: operating lease obligations					
add: advances					
add: guarantees					
Scope-adjusted debt	10,341	11,158	17,191	26,613	24,372

Business risk profile: BB-

BB- rated business risk profile remains unchanged

AutoWallis is in a phase of strong expansion, aiming to double revenues by 2024 based on the five-year strategy defined at the beginning of last year. Furthermore, AutoWallis plans to become the dominant mobility provider in Central and Eastern Europe by 2029. To this end, AutoWallis will broaden regional coverage, by introducing currently represented brands in additional countries while adding new car brands to its portfolio. Acquisitions play an important role in this context.

Six major transactions during 2020

As part of this strategy, AutoWallis announced six major transactions during 2020:

1. **Acquisition of Wallis Kerepesi Kft.,** Hungary's largest Opel dealer and third-largest Kia dealer, with a turnover of HUF 8.7bn in 2019. In 2019, Wallis Kerepesi sold the most new Opel vehicles in Hungary (903) and holds 6-7% of the market; sold 762 new Kia cars and holds 10-12% of the market. It also provides authorised repairs for Opel, Kia, and Isuzu as an independent workshop.
2. **Exclusive Jaguar and Land Rover importer rights in Hungary** to distribute vehicles and spare parts from April 2020, based on rights received in 2019.
3. **Acquisition of 60% of Iniciál Autóház Ltd.**, which sells and services seven car brands (Dacia, Nissan, Opel, Peugeot, Renault, Suzuki and Toyota) at four Hungarian sites (Győr, Mosonmagyaróvár, Sopron and Szombathely). In 2019, Iniciál Autóház sold 3,549 vehicles and had revenues HUF 19.3bn. In addition to the international expansion, the transaction will add further fleet brands to AutoWallis' portfolio. The acquisition took place in July and August.
4. **Acquisition of the largest BMW dealership in both Ljubljana and Slovenia** in October. Wallis Motor Ljubljana sells and services new and used BMW vehicles and is authorised to provide after-sales services for Mini vehicles. Slovenia is a new retail car market for AutoWallis.
5. **Opel importer rights in Croatia, Slovenia, and Bosnia and Herzegovina**. In 2019, 11,700 Opel vehicles were sold in these three countries. AutoWallis announced the transaction in September 2020.
6. **Opel importer rights in Hungary**. Nearly 12,500 Opel cars and vans were sold in the country in 2019.

Opel importer rights will add significant volumes and clearly improve Hungary market share

Particularly worth mentioning are the latter two acquisitions, which will add sales of around 12,500 cars in Hungary and around 11,700 cars in the other three countries. This is significantly more than AutoWallis' sales in 2019 (3,210 new cars in Hungary and 1,996 cars in the relevant markets outside of Hungary) and will thus lead to market share rising markedly to more than 13% from 2% in 2019. The company's market share outside of Hungary, however, should remain low at around 1.5%.

Preliminary agreement for additional transaction

In addition, AutoWallis announced on 13 November it had reached a preliminary agreement to acquire the automotive retail and servicing branches of Avto Aktiv d.o.o., a Slovenian company selling and servicing BMW, Mini, Jaguar, Land Rover, Toyota and Suzuki vehicles in four cities (Koper, Kranj, Nova Gorica, and Trzin). The company reported turnover of EUR 37m in 2019 and sold 877 new vehicles.

Improved market position following recent transactions

These transactions improve AutoWallis' market position and support the unchanged BB-rated business risk profile.

Unchanged view on diversification

We have an unchanged view on the company's diversification, as we believe that positive and negative impacts from recent transaction on diversification will offset each other.

Geographical positioning still a supportive factor

The business risk profile continues to benefit from the company's geographical positioning. In addition to Hungary, AutoWallis is present in 13 countries in Central and Eastern Europe: Albania, Bosnia and Herzegovina, the Czech Republic, Bulgaria, Croatia, Kosovo, Poland, Romania, Serbia, Slovakia, Slovenia, North Macedonia, and Montenegro. Recent transactions, in our view, have no impact on geographical diversification: transactions in Slovenia, Croatia, and Bosnia and Herzegovina, expanding the non-Hungarian market position are offset by domestic transactions (Iniciál Autóház and Wallis Kerepesi, as well as the start of the distribution of Jaguar, Land Rover and Opel vehicles in Hungary).

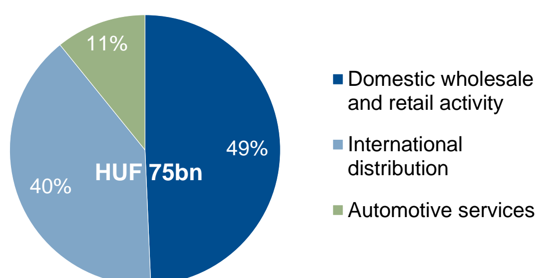
Product diversification still a constraining factor

Product diversification still constrains the company's business risk profile. We note that 89% of the company's revenues in 2019 stemmed from car sales, while services (mainly aftersales and car rentals) contribute a minor share with the remaining 11%. However, AutoWallis' services are very profitable, accounting for around 50% of the group's total EBITDA. Following the acquisition of Opel importer rights, we expect the share of services in the product mix to decrease and the share of wholesale to increase substantially. Some diversification is achieved through customers: around 52% of 2019 revenues were in retail and 48% in wholesale.

Brand diversification remains limited

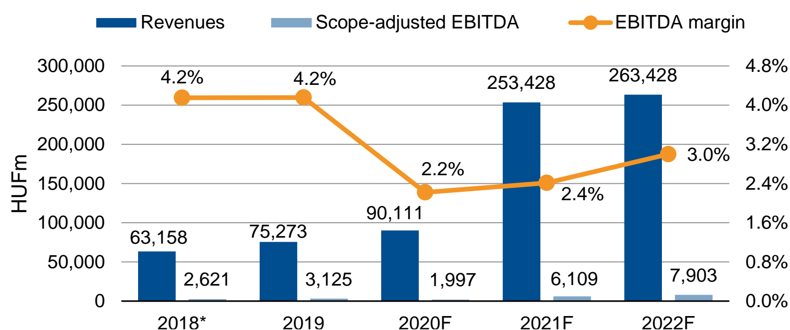
Diversification through different marques remained limited in 2019. The two premium marques, Jaguar Land Rover and BMW, accounted for around 67% of new vehicle sales. AutoWallis has a small exposure in the low-price segment with Isuzu (approx. 10%) and Ssangyong (approx. 17%). Three recent transactions are particularly positive for brand diversification: Wallis Kerepesi (largest Opel dealer in Hungary), Opel importer rights in Hungary, Croatia, Slovenia, and Bosnia and Herzegovina (total of 24,000 cars retailed last year), and Iniciál Autóház (seven car brands). Having said that, while AutoWallis will extend its brand portfolio and enter the mid-price segment, the share of Opel in total car sales is set increase to 60-70% following these transactions.

Figure 1: Breakdown of revenues by segment 2019



Source: AutoWallis, Scope

Figure 2: Five-year trend in revenues and EBITDA



* Restated; Source: AutoWallis, Scope

Profitability to decrease following recent transactions due to lower share of high-margin services

The low profitability also continues to limit the business risk profile. EBITDA margin has remained at 4.2% between 2018 and 2019. This is mainly attributable to automotive sales, which have very low and even negative margins. In H1 2020, the reported EBITDA margin decreased to 1.9% from 3.8% in H1 2019, due to a HUF 158m one-off item from the loss of unlawfully appropriated assets. Excluding this one-off item, the EBITDA margin was 2.3%, which still represents a decrease against the H1 2019 figure, driven by the sharp revenue decline in the high-margin automotive services. As a result of the recent transactions, we expect AutoWallis' revenues in 2020 to increase to around HUF 90bn (HUF 75bn in 2019). The full-year effects of the 2020 transactions are expected to drive up revenues in 2021 to around HUF 253bn. The sharp revenue decline in automotive services is expected to lead to a 2020 EBITDA margin, adjusted for one-off items, of 2.2%. As the share of high-margin services is set to decrease following the recent transactions, we expect the EBITDA margin to remain between 2-3% in 2021.

Financial risk profile: B+

B+ financial risk profile remains unchanged

The group's Scope adjusted debt (SaD) amounted to HUF 11.2bn at year-end 2019, mostly comprising inventory loans for the financing of vehicle stock (HUF 7bn) and operating leases (HUF 5.7bn). We calculate a slightly higher SaD/EBITDA ratio of 3.6x at year-end 2019 (2018: 3.2x) and an improved interest cover of around 11x (2018: 8.5x).

Financial debt expected to more than double until year-end 2021

AutoWallis is in a phase of strong expansion, for which we expect financial debt to more than double until the year-end 2021 due to the increasing inventory loans. We note positively that AutoWallis' financing strategy for acquisitions is to execute these via share exchanges and capital increases, without using cash, as seen in the recent acquisitions of Wallis Kerepesi Kft and Iniciál Autóház. Behind this backdrop, we note that on 30 November AutoWallis will ask shareholders to authorise the board to increase share capital to up to HUF 6bn, with the aim to improve future flexibility. We estimate SaD to increase to HUF 17bn at year-end 2020 and HUF 27bn at year-end 2021.

We expect the lower EBITDA and higher SaD to lead to a sharp increase in the SaD/EBITDA ratio to around 8.5x at year-end 2020. This ratio, however, will be distorted to some extent as the recent transactions will not yet be fully reflected in the EBITDA. We expect SaD/EBITDA to recover into the 4.0-4.5x range in 2021, driven in particular by higher EBITDA reflecting the full-year effects of the transactions. We expect interest cover to recover from 4.6x in 2020 to around 11x in 2021 on the back of higher EBITDA.

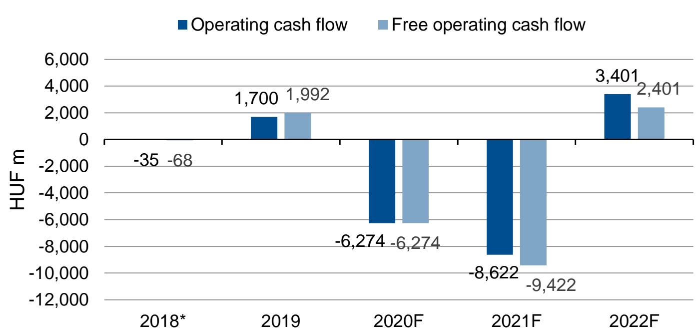
Exemption from loan covenant until the end of Q1 2021 due to Covid-19 crisis

All credit instruments have a financial covenant, namely, a 20% equity/total asset ratio for more than 90 inventory days, and a 15% equity/total asset ratio for below 90 inventory days. The covenant is calculated based on the subsidiaries' standalone financial statements prepared according to Hungarian accounting standards, and not AutoWallis' IFRS consolidated statements (no cross default). According to AutoWallis, the covenants are monitored quarterly. Furthermore, contracts allow subsidiaries to breach covenants two times in any given year. AutoWallis also informed us that it has been exempted from the covenant until the end of Q1 2021 due to the Covid-19 crisis. HUF 1.2bn in credit lines are affected by the covenant.

Deeply negative free operating cash flow expected due to growth-driven increase in inventories

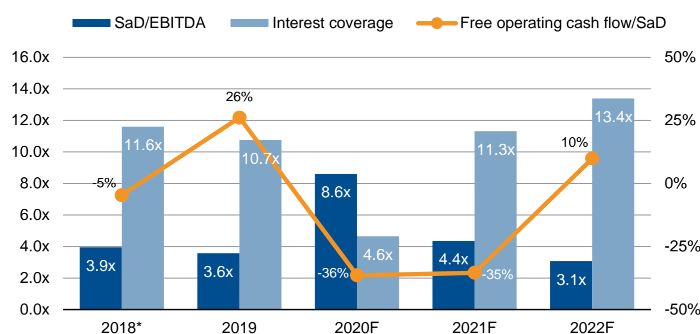
Operating cash flow turned positive at HUF 1.7bn (2018: -HUF 35m), reflecting the higher EBITDA and relatively unchanged net working capital. The lower expected EBITDA will weigh on cash flow in 2020. Moreover, AutoWallis is in a phase of strong expansion and inventories are expected to grow significantly. As a result, we expect operating cash flow and free operating cash flow to be deeply negative in 2020 and 2021. Inventory will be financed with additional inventory loans. According to AutoWallis, it has already received binding commitments from banks.

Figure 3: Trend in cash flow



* Restated; Source: AutoWallis, Scope

Figure 4: Key credit metrics, 2018 to 2022F



* Restated; Source: AutoWallis, Scope

We view AutoWallis' liquidity and financial flexibility to be adequate. AutoWallis had a cash balance of HUF 1.9bn at end-December 2019. Moreover, AutoWallis issued in April a HUF 3bn bond under the Hungarian Central Bank's Bond Funding for Growth Scheme. Our view on liquidity is supported by the substantial inventories, around HUF 14bn at year-end 2019. Here, AutoWallis' short-term debt consists largely of inventory loans. AutoWallis' strategy is to reduce automobile stock risks by directly financing each vehicle, documented individually at the financing agent (bank or leasing partner). This ensures an outstanding loan is fully covered by the particular vehicle's value. According to AutoWallis, this will also apply for automobile stock from the announced transactions. We calculate a short-term asset coverage of loans at year-end 2019 of 171% (2018: 139%), meaning stock can cover loans, even if vehicles are sold at around 40% of book value. Based on a 20% discount for inventories, we calculate short-term debt coverage at more than 100%. Positively, we note that financing institutions continued to provide credit lines during the automotive market downturn in 2008-09.

All in all, we expect a cash balance of around HUF 3.7bn at end-FY 2020.

Long-term and short-term debt ratings

B+ rating on senior unsecured debt class affirmed

We have affirmed the current B+ rating on senior unsecured debt, in line with the issuer rating. This is based on the 'average' recovery rate (30-50%) calculated for this debt class.

The recovery analysis used a liquidation value in a hypothetical default scenario in 2021 of HUF 51bn. This value is based on a haircut of around 20% on the assets and reflect asset liquidation costs of 10%. The majority of inventory assets are pledged as security for the underlying loans. The recovery analysis assumes that, in a hypothetical default, short-term loans and lease liabilities would be senior to the bond, while long-term liabilities and advances received would have the same seniority as the bond. In addition, we have assumed a higher seniority for the balance of trade payables covered by banks. The reasoning for this view is our belief that payables would have a first-ranking pledge (assignment) by auto manufacturers in a hypothetical default. We also assume importer trade receivables (around 80% of total trade receivables) to have 100% recovery as they are covered by third-party bank guarantees. Also, the issuer will be the holding company, which has no other assets apart from its investments.

Scope Ratings GmbH

Headquarters Berlin

Lennéstraße 5
D-10785 Berlin

Phone +49 30 27891 0

Frankfurt am Main

Neue Mainzer Straße 66-68
D-60311 Frankfurt am Main

Phone +49 69 66 77 389 0

Paris

23 Boulevard des Capucines
F-75002 Paris

Phone +33 1 8288 5557

London

3rd Floor
111 Buckingham Palace Road
UK-London SW1W 0SR

Madrid

Edificio Torre Europa
Paseo de la Castellana 95
E-28046 Madrid

Phone +34 914 186 973

Milan

Regus Porta Venezia
Via Nino Bixio, 31
20129 Milano MI

Phone +39 02 30315 814

Oslo

Karenslyst allé 53
0279 Oslo

Phone +47 21 62 31 42

info@scoperatings.com
www.scoperatings.com

Disclaimer

© 2020 Scope SE & Co. KGaA and all its subsidiaries including Scope Ratings GmbH, Scope Analysis GmbH, Scope Investor Services GmbH and Scope Risk Solutions GmbH (collectively, Scope). All rights reserved. The information and data supporting Scope's ratings, rating reports, rating opinions and related research and credit opinions originate from sources Scope considers to be reliable and accurate. Scope does not, however, independently verify the reliability and accuracy of the information and data. Scope's ratings, rating reports, rating opinions, or related research and credit opinions are provided 'as is' without any representation or warranty of any kind. In no circumstance shall Scope or its directors, officers, employees and other representatives be liable to any party for any direct, indirect, incidental or other damages, expenses of any kind, or losses arising from any use of Scope's ratings, rating reports, rating opinions, related research or credit opinions. Ratings and other related credit opinions issued by Scope are, and have to be viewed by any party as, opinions on relative credit risk and not a statement of fact or recommendation to purchase, hold or sell securities. Past performance does not necessarily predict future results. Any report issued by Scope is not a prospectus or similar document related to a debt security or issuing entity. Scope issues credit ratings and related research and opinions with the understanding and expectation that parties using them will assess independently the suitability of each security for investment or transaction purposes. Scope's credit ratings address relative credit risk, they do not address other risks such as market, liquidity, legal, or volatility. The information and data included herein is protected by copyright and other laws. To reproduce, transmit, transfer, disseminate, translate, resell, or store for subsequent use for any such purpose the information and data contained herein, contact Scope Ratings GmbH at Lennéstraße 5 D-10785 Berlin.

Scope Ratings GmbH, Lennéstraße 5, 10785 Berlin, District Court for Berlin (Charlottenburg) HRB 192993 B, Managing Director: Guillaume Jolivet.