Aranynektar Kft
Hungary, Business Services

B STABLE

Corporate profile

Aranynektar is an entity solely acting as a commercial partner to Fulmer Hungarian Branch (FHB), both entities are owned either directly or indirectly by Mr Ferenc Takács. Aranynektar's business consists of the preparation and packaging of honey – either in glass or PET containers. Acting as an integrated contractor, Aranynektar generates revenues fixed in advance by FHB to cover its operating expenses and generates a margin which is sufficiently high for the tax authorities.

Key metrics

Fulmer Hungarian Branch			Scope estimates	
Scope credit ratios	**2017**	**2018**	**2019e**	**2020e**
EBITDA/interest cover (x)	32.1x	12.5x	19.7x	4.9x
Scope-adjusted debt (SaD)/EBITDA	2.3x	5.6x	2.3x	2.7x
Scope-adjusted funds from operations/SaD	40%	15%	39%	28%
Free operating cash flow/SaD	-2%	-33%	31%	-25%

Rating rationale

Scope Ratings assigns a first-time issuer rating of B/Stable to Hungary-based business services company Aranynektar Kft. The planned bond (2020-2030), which is issued by Aranynektar Kft and guaranteed by Fulmer Hungarian Branch under the MNB Bond Funding for Growth Scheme, has been assigned a preliminary rating of (P) B+.

The rating of Aranynektar is determined by the credit quality of its sister company (FHB), owned by the same ultimate shareholder Mr Ferenc Takács. This is because we consider Aranynektar to be fully dependent on the relationship between the two entities. A severance in their business links would lead to an immediate bankruptcy of Aranynektar. The credit quality of FHB determines Aranynektar's issuer rating.

FHB's business risk profile (rated B) is constrained by its small market share on a European level (close to 1.5% of the continent's honey production). We assume that its total market share is even lower due to high European imports (representing 60% of total consumption). The company's small size also affects the magnitude of the impact which external events have on revenue (illustrated by the 15% drop in 2018, due to the bankruptcy of its Italian business partner). Diversification is weak due to the sale of a single type of product to consumers, despite a broad geographical outreach. We consider profitability to be relatively low for the fast-moving consumer goods industry (with the Scope-adjusted EBITDA margin averaging 9%), due to the high share of private labels FHB offers. Going forward, we expect profitability to recover somewhat, softening the decline in 2018.

Aranynektar's financial risk profile (rated B) is weak due to our expectation that the 2020-2030 HUF 1bn bond issuance will erode its historically strong credit metrics. The bond will be issued by Aranynektar, which will, in turn, extend an intercompany loan to FHB with exactly the same features (coupons, repayment schedule, maturity and others). The bond will partially be used to repay FHB's existing loans but also to finance some its operations, increasing its total gross debt by close to HUF 500m.

Ratings & Outlook

Corporate rating	B/Stable
Guaranteed bond 2020/30	(P) B+

Analysts

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Related Methodology

Corporate Rating Methodology

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Bloomberg: SCOP

YE 2018 already saw an overall deterioration in FHB's credit metrics due to a drop in revenue. We expect both revenue and profitability to recover somewhat by YE 2019, lessening the negative impact on credit ratios.

We forecast that Scope-adjusted debt (SaD)/EBITDA and funds from operations/SaD will face a slight deterioration in comparison with its 2017 levels from 2020 on. Interest cover is forecasted to drop from above 12x in 2018 to below 6x at YE 2020. Finally, we expect free operating cash flow/SaD to deteriorate in line with leverage metrics going forward. We expect liquidity to be under pressure at YE 2019 and negative at YE 2020, due to high capex in 2020. Despite Aranynektar being the issuer of the bond, the significant deterioration in its credits metrics is not a key factor in our rating case.

Preliminary bond rating

We assume a bond issuance of HUF 1bn (over the 2020/2030 duration) under the MNB Bond Funding for Growth Scheme. As Aranynektar has no significant assets, we conducted a recovery analysis on FHB. We assign a preliminary rating of (P) B+ to the planned guaranteed bond based on our expectations of an above-average recovery. This is one notch above the assigned issuer rating.

Outlook and rating-change drivers

The Outlook is Stable based on FHB's financials and operations. It also incorporates our view that liquidity will be weak over the next few years.

The possibility of a positive rating action is remote, given FHB's limited scope of operations, which means that low-probability events may potentially have a serious impact on the company. The diversification of FHB's operations is too limited to buffer large, unexpected developments (notably operationally).

A negative rating action may be taken if FHB's SaD/EBITDA increases above 4.5x on a sustained basis or if FHB's liquidity deteriorates as a result of unforeseen liquidity needs, such as working capital requirements.

Rating drivers

Positive rating drivers	Negative rating drivers
Aranynektar: • Guarantee provided by FHB on the planned bond **FHB:** • Modest geographical diversification • Development of a branded label • Absence of operating leases, alleviating Scope-adjusted debt	**Aranynektar:** • Semi-integrated supplier unable to develop without FHB's operations **FHB:** • Small company size makes it quite vulnerable to externalities • High historical variations in net working capital expected to continue putting pressure on liquidity • High share of private labels weighs on profitability

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Unlikely	• Increase in FHB's SaD/EBITDA above 4.5x or deterioration in liquidity situation

Financial overview of Fulmer Hungarian branch

			Scope estimates	
Scope credit ratios for FHB	**2017**	**2018**	**2019e**	**2020e**
EBITDA/interest cover (x)	32.1x	12.5x	19.7x	4.9x
Scope-adjusted debt (SaD)/EBITDA (x)	2.3x	5.6x	2.3x	2.7x
Scope-adjusted funds from operations/SaD	40%	15%	39%	28%
Free operating cash flow/SaD	-2%	-33%	31%	-25%
Scope-adjusted EBITDA in HUF m	**2017**	**2018**	**2019e**	**2020e**
EBITDA	587,678	330,784	432,236	477,500
Operating lease payments in respective year	0	0	0	0
Scope-adjusted EBITDA	587,678	330,784	432,236	477,500
Scope-adjusted funds from operations in HUF m	**2017**	**2018**	**2019e**	**2020e**
EBITDA	587,678	330,784	432,236	477,500
less: (net) cash interest as per cash flow statement	-18,298	-26,477	-21,934	-98,374
less: cash tax paid as per cash flow statement	-36,073	-18,446	-25,697	-21,953
Scope-adjusted funds from operations	533,307	285,861	384,605	357,173
Scope-adjusted debt in HUF m	**2017**	**2018**	**2019e**	**2020e**
Reported gross financial debt	1,492,246	1,868,857	1,023,239	1,472,095
less: cash and cash equivalents	-143,941	-13,694	-41,703	-185,092
Scope-adjusted debt	1,348,305	1,855,163	981,536	1,287,003

Business risk profile: B

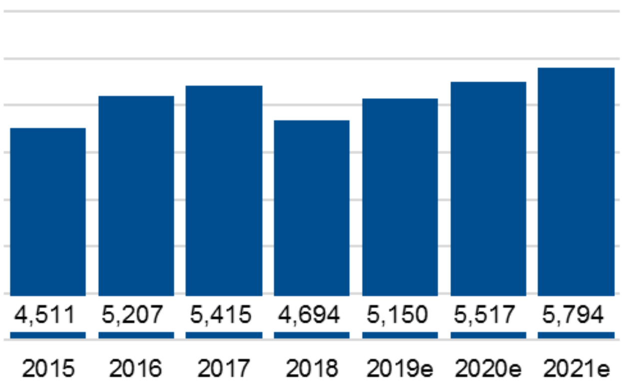
Symbiotic relationship between FHB and Aranynektar

Due to the close relationship between Aranynektar and FHB, we have performed a a credit quality assessment of the latter. Although Aranynektar is the issuing entity, the debt servicing obligations lie with FHB due to the intercompany loan matching the bond features issued by Aranynektar to FHB. As a consequence, and due to the codependence between the two entities and guarantee provided by FHB for the prospective bond, our rating focuses on the credit quality of FHB, and not on Aranynektar.

Weak market positioning detrimental to the rating

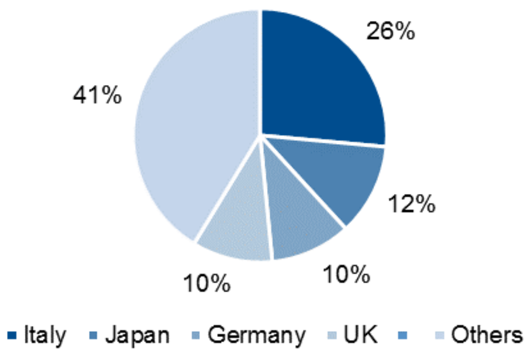
FHB has a relatively strong market position on the national market but a weak position in Europe, with market shares estimated at close to 20% and 1.5% respectively. FHB plans to boost its brand recognition by increasing the number of its own labels (currently representing 20% of the sales). Nonetheless, FHB's small size is detrimental to the rating due to the high impact of unexpected externalities on the group (illustrated by the 15% revenue decline in 2018 due to the bankruptcy of its Italian customer). Its market share is relatively low in Europe, as the abovementioned 1.5% only considers production within Europe, disregarding European imports (close to 60% of total consumption). Going forward, we expect FHB to grow its revenue, bolstered by: i) the normalisation of revenue growth post 2018; and ii) capex aimed at enhancing production capabilities.

Figure 1: FHB's revenue with forecasts (in HUF m)



Source: FHB, Scope estimates

Figure 2: FHB's geographical outreach

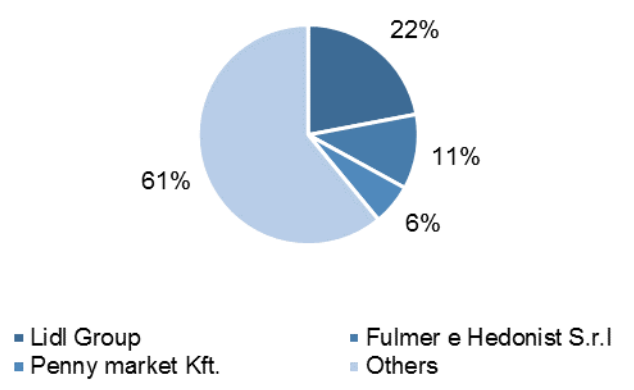


Source: FHB

Low diversification due to mono-product focus

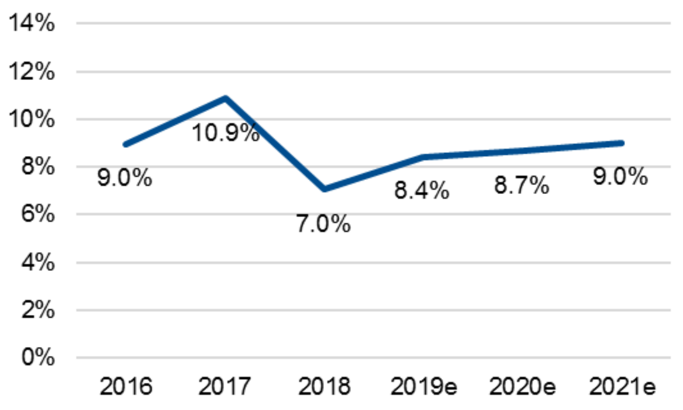
FHB benefits from a relatively wide geographical and customer outreach for a company of its size, supporting the rating. We expect the development of FHB's own label to ultimately represent an alternative to retail customers. While we view this as positive, we believe it will take several years before this product can properly mitigate weak overall customer diversification. Also, FHB's mono-product focus (honey related) is detrimental to the rating as poor harvesting could heavily impact group revenues, once its inventory is depleted. The group uses different formats (glass and PET containers). However, this does not represent real diversification because neither format has features which are countercyclical to the other format.

Figure 3: FHB's customer diversification



Source: FHB

Figure 4: FHB's profitability with forecasts (in %)



Source: FHB, Scope estimates

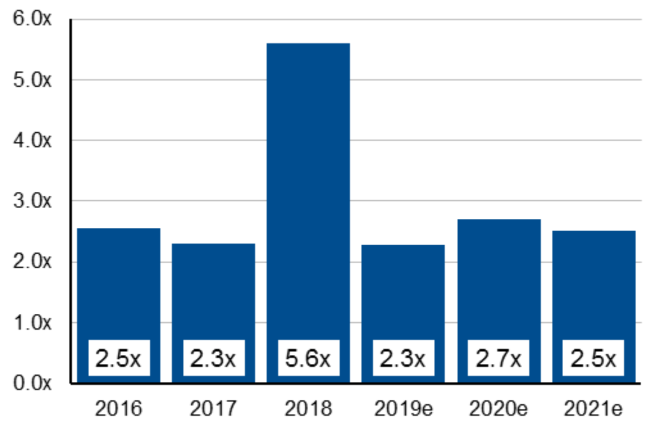
Profitability expected to recover in 2019 but remain below that of peers

FHB has a relatively low EBITDA margin (around 9%) for a company active in the fast-moving consumer goods sector, due to its high share of private labels. While it is gradually increasing the share of its own brands (currently representing around 20% to 30% of sales), we believe the impact on profitability will remain limited in the short term.

Financial risk profile: B

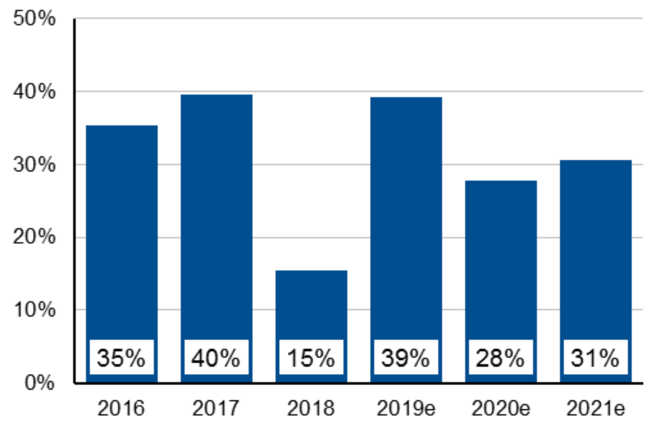
We understand that the bond issuance planned by Aranynektar will immediately be transferred to FHB via an intercompany loan, designed to have exactly the same features (including coupons, repayment schedule and maturity). The rationale behind this transaction is that FHB is not eligible to take part in the MNB programme. As Aranynektar does not have the financial capabilities to repay the coupons or the bond with its limited cash flow generation, FHB will pay the interests and repay the bond to Aranynektar, which will, in turn, repay the bondholders.

Figure 5: Evolution of SaD/Scope-adjusted EBITDA



Source: FHB, Scope estimates

Figure 6: Evolution of funds from operations/SaD

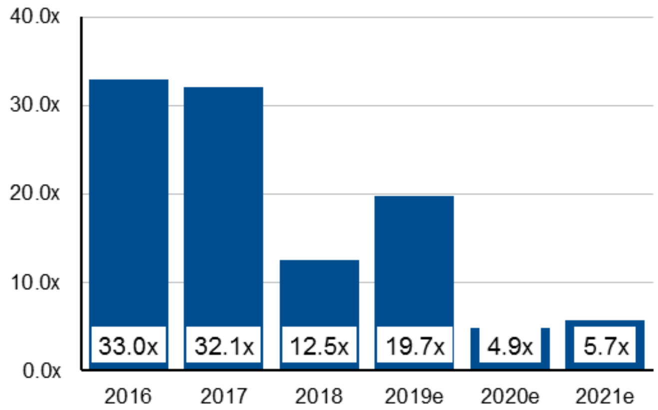


Source: FHB, Scope estimates

Deterioration in credit metrics due to intercompany loan

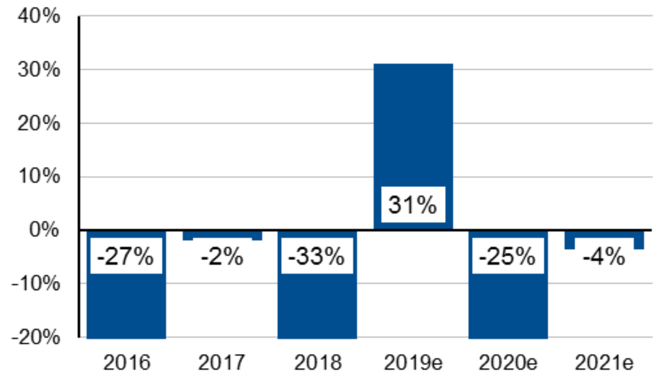
FHB benefited from relatively low historical leverage between 2015 and 2017 (including 2017), due to high margins and the absence of operating leases in our calculation of SaD. While metrics have historically been strong, the drop in revenues in 2018 negatively impacted metrics that year. We expect sales and profitability to normalise from 2019e onwards, notably thanks to the conversion of the intercompany loan provided by Fulmer GmbH into equity in December 2019. We expect leverage to deteriorate slightly in 2020, despite the net increase of HUF 500m in gross debt, with SaD/EBITDA reaching 2.7x (versus 5.6x in 2018 and 2.3x in 2017). Funds from operations/SaD is expected to follow a similar trend by decreasing to 28% at YE 2020, versus 15% at YE 2018 and 40% in 2017.

Figure 7: Evolution of interest cover



Source: Scope estimates

Figure 8: Evolution of free operating cash flow/SaD



Source: Scope

We expect interest cover to remain strong, remaining close to 5x in 2020, due to the absence of the operating leases interest component. Free operating cash flow/SaD is expected to remain negative due to: i) revenue growth translating into high negative variations in net working capital; and ii) significant capex plans aimed at increasing packaging capabilities.

Liquidity is one of the main negative drivers for FHB's credit assessment due to its high fluctuation in recent years. We expect liquidity to be at risk going forward due to negative free operating cash flows in 2020 and the potential consequences of externalities.

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