Masterplast Nyrt.
Hungary, Construction Materials

B+ Stable

Corporate profile

Masterplast Nyrt. was founded in 1997 as a distributor of building materials, mainly roofing foils, glass mesh nets and additional construction products. In 2005 Masterplast started to manufacture its own construction materials and now operates four manufacturing plants. The company benefits from a direct presence in eight eastern European countries (Hungary, Romania, Serbia, Ukraine, Poland, Slovakia, Croatia and Macedonia) through its 11 subsidiaries. Its total geographical outreach comprises 41 countries including the company's export activity.

Key metrics

			Scope estimates	
Scope credit ratios	**2017**	**2018**	**2019F**	**2020F**
SaEBITDA interest cover (x)	10.9x	13.0x	11.3x	7.2x
Scope-adjusted debt (SaD)/EBITDA (x)	3.9x	3.7x	3.7x	3.5x
Scope-adjusted FFO/SaD (%)	22%	24%	22%	23%
FOCF/SaD (%)	-13%	-25%	-10%	7%

Rating rationale

Scope assigns first-time rating of B+ to Masterplast Nyrt

The B+ private issuer rating is driven by Masterplast's comparatively strong credit metrics, which benefit from a relatively high EBITDA-interest cover ratio as well as modest leverage. The rating is also supported by the company's high exposure to the maintenance end market, which is less cyclical than the construction materials market, leading to more stable cash flows and less volatile margins.

The rating is mainly constrained by the company's small overall scale, which lessens its ability to benefit from economies of scale or to offset the impact of economic cycles. The rating is also limited by relatively low but stable profitability. We judge diversification to be poor because Masterplast generates most of its revenues in one region (Europe) and is exposed to only one segment (construction materials).

Outlook

The Outlook is Stable and reflects our view that credit metrics will remain at the current levels, with ongoing strong EBITDA interest cover and Scope-adjusted debt (SaD)/EBITDA between 3.5x and 4.0x. The Outlook also incorporates the successful issuance of the HUF 6bn (EUR 18m) bond under the Hungarian national bank's Funding for Growth Scheme, leading to improved liquidity, with bond proceeds used to replace short-term debt.

A positive rating action may be warranted if the company can reduce its leverage to SaD/EBITDA of below 3.5x on a sustainable basis.

A negative rating action could occur if SaD/EBITDA exceeded 4x on a sustained basis or if the company does not succeed in issuing the HUF 6bn bond to repay most of its short-term debt.

Ratings & Outlook

Corporate ratings B+/Stable

Senior unsecured rating B+

Analysts

Philipp Wass
+49 69 6677389 11
p.wass@scoperatings.com

Alexander Kallenborn
+49 69 6677389 28
a.kallenborn@scoperatings.com

Related Methodology

Corporate Rating Methodology

Scope Ratings GmbH

Neue Mainzer Straße 66-68
60311 Frankfurt am Main

Tel. +49 69 6677389 0

Headquarters

Lennéstraße 5
10785 Berlin

Tel. +49 30 27891 0
Fax +49 30 27891 100

info@scoperatings.com
www.scoperatings.com

Bloomberg: SCOP

Rating drivers

Positive rating drivers	Negative rating drivers
• Relatively strong credit metrics • Stable cash flows and profitability due to high exposure to the maintenance end market and granular customer structure • Adequate liquidity following the targeted restructuring of liabilities	• Small scale and weak market position • Low profitability • Weak diversification across geographies • Exposed to cyclical industry

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• SaD/EBITDA of below 3.5x on a sustainable basis	• SaD/EBITDA of greater than 4x on a sustained basis • Ongoing weak liquidity

Financial overview

			Scope estimates	
Scope credit ratios	**2017**	**2018**	**2019F**	**2020F**
SaEBITDA interest cover (x)	10.9x	13.0x	11.3x	7.2x
SaD/EBITDA	3.9x	3.7x	3.7x	3.5x
Scope-adjusted FFO/SaD	22%	24%	22%	23%
FOCF/SaD	-13%	-25%	-10%	7%
Scope-adjusted EBITDA in EUR k	**2017**	**2018**	**2019F**	**2020F**
EBITDA	5,040	6,237	7,034	7,574
Operating lease payment in respective year	0	0	0	0
Restructuring costs	0	0	66	0
Scope-adjusted EBITDA	**5,040**	**6,237**	**7,101**	**7,574**
Scope funds from operations in EUR k	**2017**	**2018**	**2019F**	**2020F**
EBITDA	5,040	6,237	7,101	7,574
less: (net) cash interest as per cash flow statement	(462)	(481)	(629)	(1,056)
less: cash tax paid as per cash flow statement	(200)	(198)	(544)	(507)
add: depreciation component operating leases	0	0	0	0
Scope funds from operations	**4,378**	**5,558**	**5,937**	**6,011**
Scope-adjusted debt in EUR k	**2017**	**2018**	**2019F**	**2020F**
Reported gross financial debt	22,517	25,303	28,557	28,895
less: cash	(3,013)	(2,090)	(1,980)	(2,204)
add: pension adjustment	0	0	0	0
add: operating lease obligation	0	0	0	0
Other adjustments	0	0	0	0
Scope-adjusted debt	**19,504**	**23,213**	**26,577**	**26,690**

Business risk profile: B

Industry risk: B

We assess the fundamentals of the construction materials industry by examining the following industry drivers:

- Cyclicality
- Entry barriers
- Substitution risks

Cyclicality (high)

We consider the construction materials industry to be highly cyclical overall. Key drivers of demand for construction materials are consumer confidence, the availability of consumer credit, real estate prices, interest rates and the general economic environment. However, construction materials encompass a broad range of products such as basic building materials (e.g. cement or aggregates) and finished products (e.g. facade insulation or roofing elements) and serve different end markets:

- Residential and nonresidential construction
- Maintenance and extensions of existing buildings
- Public works (such as infrastructure)

Cyclicality also depends on the end market. Products which serve maintenance purposes are less cyclical because they are bought periodically. Other products such as high-end bath fixtures are of a more discretionary nature and therefore have more cyclical demand patterns.

Based on our analysis of Bloomberg data, revenues in the construction materials industry declined by more than 8% during the most recent recession in 2009.

Furthermore, profit margins developed cyclically during the last downturn. Construction materials companies are unable to reduce costs in step with revenue decreases during economic downturns, leading to rather volatile profit margins.

Market entry barriers (medium)

We consider entry barriers in the building materials industry to be medium overall. Entry barriers in the industry are typically determined by high initial capital expenditure (e.g. for manufacturing plants), manufacturing know-how, access to distribution channels, customer relations and, in some cases, permitting requirements (mainly for basic building materials companies).

However, entry barriers can differ, given the fragmented structure of the industry and broad spectrum of companies with regard to size and product range. Entry barriers for large manufacturers such as materials companies (e.g. cement) like 'Heidelberger Cement' are high as a result of the large initial expenditure needed for manufacturing plants. On the other hand, entry barriers for smaller finished product producers tend to require manufacturing know-how rather than large expenditure on manufacturing plants.

Substitution risk (low/medium)

We consider substitution risk for construction materials to be low to medium overall. Basic building materials have a rather low risk of substitution, whereas finished goods are impacted by global trends such as sustainability and energy efficiency.

Figure 1: Industry risk assessment: European construction materials sector

Cyclicality \ Barriers to entry	Low	Medium	High
High	CCC/B	**B**/BB	BB/BBB
Medium	B/BB	BB/BBB	BBB/A
Low	BB/BBB	BBB/A	AA/AAA

Source: Scope

Small company but strong market position in a fragmented market

Masterplast is a relatively small player in the construction materials industry with revenues of around EUR 100m and an EBITDA of EUR 6.2m, both for 2018. The company's small size limits its ability to benefit from economies of scale or to offset the impact of economic cycles. However, the company's market position is supported by i) its strong standing in Eastern Europe, the rather fragmented market structure in its main segment (insulation systems) and strong customer loyalty as well as ii) its dedicated growth strategy, underpinned by total capex of EUR 20m in the last three years, which was mainly used to acquire new production facilities. Relatively high capital expenditure has translated into some growth in terms of revenues (+16% since 2015) and EBITDA (+18%). However, we do not expect Masterplast to reach a critical size, which would enable it to defend its foothold if larger competitors enter the niche markets in which it operates[1].

Limited diversification bears the risk of a sharp decline in revenues if demand weakens

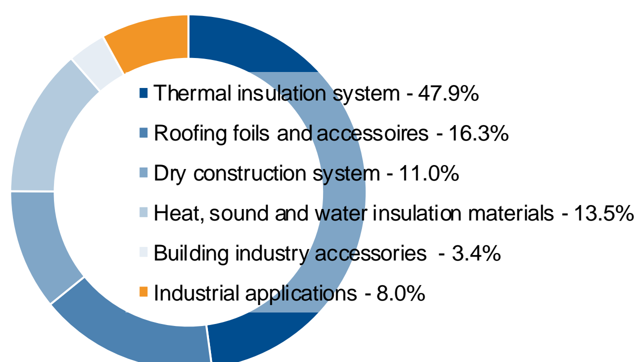
Masterplast's geographical diversification is rather poor, since the company generates most of its revenues in one region, Europe (with a strong focus on Eastern Europe).

Low geographical diversification bears the risk of exposure to the construction cycle of one region. In a cyclical industry such as construction materials, revenues and earnings are likely to come under pressure if there is a downturn in one region. Conversely, a wide spread of activities across various geographical regions with different demand patterns or cyclicality exposures tends to reduce cash flow volatility.

However, the company is diversified within Europe with exposure to several countries in that region. This supports our assessment of diversification because we expect demand patterns to differ at least a little between the countries to which the issuer is exposed. We acknowledge that Masterplast has a pan-European footprint, benefitting from its 'export activities' (around 16% of total revenues in FY 2018).

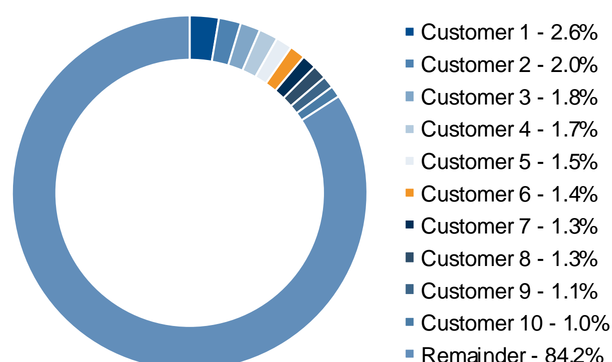
We judge segment diversification to be weak because Masterplast operates in just one segment (construction/building materials). However, this weak segment diversification is partially mitigated by the different end markets the issuer serves (including the less cyclical end market of real estate maintenance) as well as its the relatively broad range of products (Figure 2) with limited dependence on single customers. The largest customer contributes a mere 2.6% of total revenues (top 10: 16%, see Figure 3).

Figure 2: Product diversification by revenues (2018)



Sources: Masterplast, Scope

Figure 3: Diversification of customers by revenues (2018)



Sources: Masterplast, Scope

Weak profitability but stable cash flows

In comparison to its peers, Masterplast has relatively low profitability with an EBITDA

[1] These are: facade insulation systems (48% of 2018's revenues), roofing foils and roofing elements (16%), dry construction systems (11%), heat insulation, soundproofing and waterproofing materials (13.5%), construction industry accessory products (3.4%) and products for industrial use (8%).

margin of around 6% (2018: 6.4%). However, the company benefits from its significant exposure to the maintenance end market, which leads to more stable cash flows and less volatile margins.

We believe that profitability will improve slightly going forward on the back of higher existing capacities (new facilities acquired in 2016, 2018 and 2019) as well as automatisation, which should help to reduce costs and support profitability. In order to improve profitability Masterplast plans to invest in the automatisation of its production facilities. These investments are envisaged for 2022, however.

Low profitability and small scale would make it difficult to defend market shares if competition increases

Low profitability, in conjunction with small scale, entails the risk that Masterplast may not be able to protect its market shares if larger peers try to establish a foothold in the company's markets by initiating a fierce price war.

Financial risk profile: BB-

Our rating scenario assumes the following:

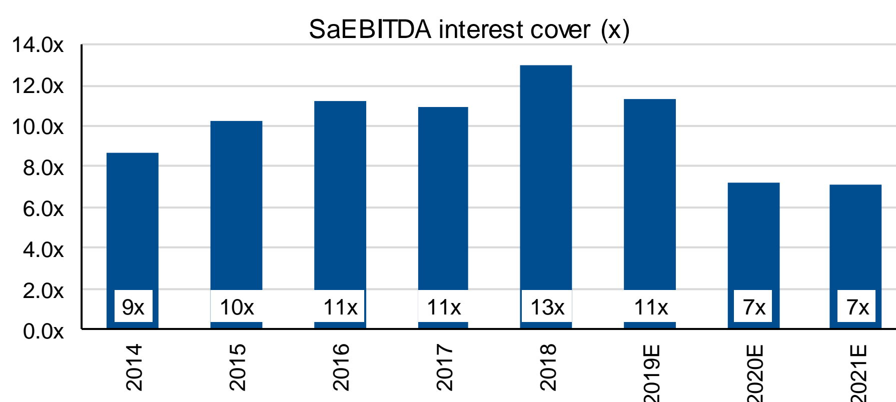
- Revenue growth of 10% (2019), 5% (2020) and 3% (2021)
- Slightly lower gross margin of 18.3% for FY 2019 and FY 2020 respectively (18.6% in FY 2018)
- Issuance of HUF 6bn bond in Q4 2019 with a coupon of 4%
- Capital expenditure of around EUR 5m in 2019 and EUR 3m for 2020 and 2021
- Dividend payout ratio of 50% from net income of the previous year

Strong debt protection

Masterplast has strong debt protection with EBITDA interest cover well exceeding 10x in the last few years (2018: 13x). The company has benefitted from the interest rate environment, which helped to reduce the weighted average cost of debt to 2.3% as at YE 2018, from 3.6% as at YE 2015, because most of its debt is short term and exposed to floating interest rates.

Masterplast plans to issue a HUF 6bn (EUR 18m) bond under the Hungarian national bank's Funding for Growth Scheme. This should improve liquidity, with proceeds used to repay a significant portion of short-term financial liabilities. It will also eliminate Masterplast's floating rate risk but increase financing costs, as the interest rate for the bond is expected to be significantly above the issuer's weighted average cost of debt as at YE 2018. We therefore expect a lower EBITDA interest coverage ratio in our forecast period.

Figure 4: Debt protection

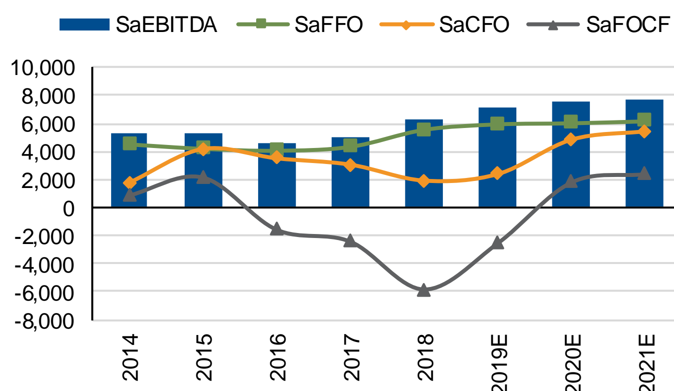


Sources: Masterplast, Scope estimates

Positive free operating cash flow due to decreasing capital expenditure

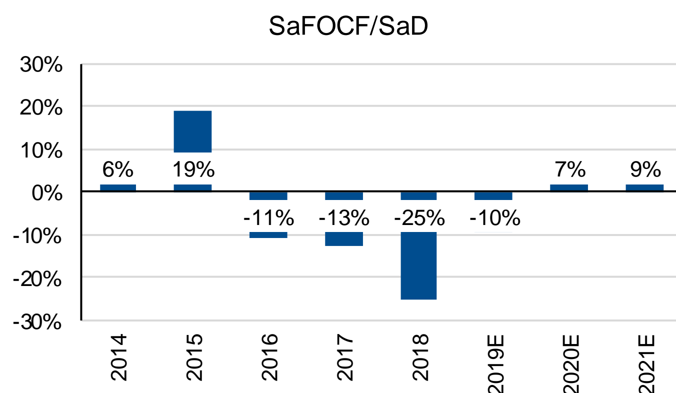
Over the last few years Masterplast has increased its capital expenditure significantly at the cost of free operating cash flows (FOCF), which turned negative from 2016 on, and led to a significant increase in SaD to EUR 23.2m as at YE 2018, from EUR 11.4m as at YE 2015. Spending has mainly focused on the acquisition of production facilities. However, Masterplast plans to reduce its capital expenditure to around EUR 2.5m to EUR 3.0m (maintenance capex) from EUR 7m on average for the last three years, thus lifting FOCF to break even in 2020 and reducing the company's dependence on external financing.

Figure 5: Cash flows (EUR m)



Sources: Masterplast, Scope estimates

Figure 6: Cash flow cover

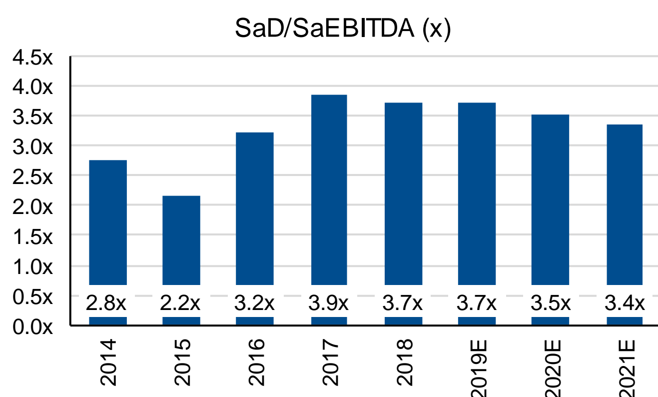


Sources: Masterplast, Scope estimates

Stable leverage

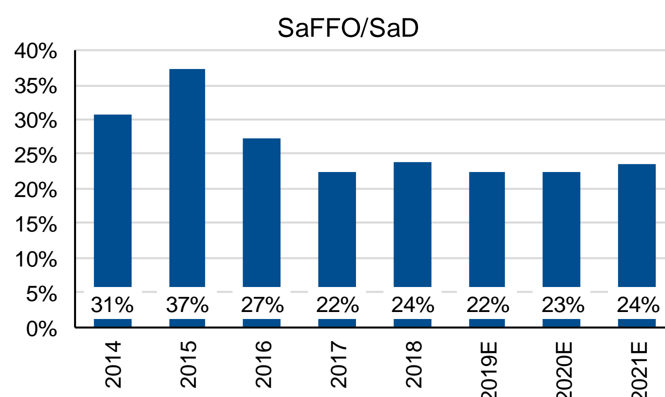
Masterplast's leverage, as measured by its SaD/EBITDA, stood at a relatively high 3.7x as at YE 2018. This follows a strong increase since YE 2015 caused by the growth strategy and subsequently negative FOCF financed with debt. We anticipate that the planned reduction of capital expenditure and the break-even FOCF will help to stabilise SaD in the next few years, also stabilising leverage as measured by SaD/EBITDA.

Figure 5: Leverage



Sources: Masterplast, Scope estimates

Figure 6: Leverage



Sources: Masterplast, Scope estimates

Currently, Masterplast's Scope-adjusted funds from operations (SaFFO)/SaD (which exceeded 20% throughout the period considered) benefit from relatively low interest payments driven by the low weighted average cost of debt. This has helped to balance the twofold rise in the company's indebtedness since YE 2015.

Despite the forecasted increase in the company's weighted average cost of debt, up to 4.0% from 2.3% as at YE 2018 due to the planned bond issuance, we anticipate stable SaFFO/SaD. Masterplast plans to use the proceeds to repay existing short-term debt.

This will significantly reduce the risk of rising interest rates and help to stabilise the company's FFO.

Liquidity: adequate

We consider liquidity to be adequate. In detail:

Position	YE 2018		YE 2019E	
Unrestricted cash	EUR	2.1m	EUR	2.0m
Open committed credit lines	EUR	0.0m	EUR	0.0m
Free operating cash flow (t+1)	(EUR	2.6m)	EUR	1.8m
Short-term debt	EUR	18.7m	EUR	1.2m
Coverage		**negative**		**3.2x**

Liquidity expected to improve due to changes in the financing structure and positive FOCF

Liquidity has been weak in the last couple of years, mainly driven by negative free operating cash flows resulting from high capital expenditure. However, we expect liquidity to come in above par in 2019. This is based on our assumption that the HUF 6bn (EUR 18m) bond will be issued successfully in Q4 2019, with the proceeds used to repay Masterplast's presently high portion of short-term debt. Aside from the repayment of short-term debt, we anticipate positive free operating cash flows, resulting from major cuts in the company's capex, thus further supporting future liquidity. We note that Masterplast has to meet several financial maintenance covenants for its interest-bearing liabilities. The headroom under these covenants is expected to be marginal in our base-case scenario. We therefore judge a covenant breach to be likely in the case of unforeseen events.

Senior unsecured debt: B+

Based on our recovery analysis, we expect an 'average recovery' for the company's senior unsecured debt, resulting in a B+ rating for this debt class (the same rating as the issuer rating).

Outlook

Outlook: Stable

The Outlook is Stable and reflects our view that credit metrics will remain at the current level, with ongoing strong EBITDA interest cover and SaD/EBITDA between 3.5x and 4.0x. The Outlook also incorporates the successful issuance of the HUF 6bn (EUR 18m) bond under the Hungarian national bank's Funding for Growth Scheme, leading to improved liquidity, with bond proceeds used to replace short-term debt.

A positive rating action may be warranted if the company can reduce its leverage to SaD/EBITDA of below 3.5x on a sustainable basis.

A negative rating action could occur if SaD/EBITDA exceeded 4x on a sustainable basis or if the company does not succeed in issuing the HUF 6bn bond to repay most of its short-term debt.

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

1 Cour du Havre
F-75008 Paris

Phone +33 1 8288 5557

London

Suite 301
2 Angel Square
London EC1V 1NY

Phone +44 203-457 0 4444

Madrid

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

Phone +34 914 186 973

Milan

Via Paleocapa 7
IT-20121 Milan

Phone +39 02 30315 814

Oslo

Haakon VII's gate 6
N-0161 Oslo

Phone +47 21 62 31 42

info@scoperatings.com
www.scoperatings.com

Disclaimer

© 2019 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: Torsten Hinrichs.