Stavmat Zrt.
Hungary, Wholesale

Corporate profile

Stavmat Építőanyag Kereskedelmi Zrt. (Stavmat) is primarily a wholesaler of construction materials for professional use, with an approximate 10% leading position in the small Hungarian market and leadership in the industrial segment. Around 25% of sales are generated by retail consumers (private professionals). Stavmat owns 35 stores across Hungary and employs around 400 people. The company provides a full range of high-quality building materials and solutions for both outdoor and interior design work, renovation and house construction. In December 2016, Stavmat became part of IN Group, a Slovakia-based diversified construction group that trades building materials in Slovakia, the Czech Republic and Hungary.

Key metrics

			Scope estimates	
Scope credit ratios	**2020**	**2021**	**2022E**	**2023E**
Scope-adjusted EBITDA/interest cover	131.5x	46.9x	15.7x	17.3x
Scope-adjusted debt (SaD)/Scope-adjusted EBITDA	0.5x	2.1x	2.5x	2.3x
Scope-adjusted funds from operations/SaD	177%	44%	36%	40%
Free operating cash flow/SaD	31%	-29%	8%	22%

Rating rationale

Scope Ratings has affirmed its B+ issuer rating on Stavmat and revised the Outlook to Positive from Stable. The rating for senior unsecured debt issued by Stavmat has also been affirmed at BB-.

The rating action reflects stable credit metrics in difficult market conditions caused by the Ukrainian-Russian war. The company faces volatile materials prices and potential shortages in raw materials, which lead to lower forecasted profitability for 2022. The Outlook change reflects our view of a less aggressive financial policy (supplementary rating driver).

Stavmat's business risk profile (assessed at B+) continues to be constrained by its limited size, concentration on the small domestic market for building materials, high dependency on construction industry cycles and the volatile cost of materials. In 2021, revenue grew by more than 25% due to rising materials prices (contributing about half of revenue growth) and favourable market conditions created by government grants to households. This led to a significant increase in the Scope-adjusted EBITDA margin to 8.2%. We expect the construction market, the company's key business driver, to stagnate because the Ukraine-Russia war is likely to exacerbate the volatility in materials prices and the shortage of raw materials. Stavmat has adapted to current market conditions by implementing daily pricing for many product types, which has also had a slight impact on its working capital management. Overall, we forecast lower profitability of 6.6% in 2022 followed by a return to previous levels in 2023 after the concrete paving production plant is operational and thus, we expect operating profitability becoming Stavmat's main business risk profile driver.

Ratings & Outlook

Corporate rating	B+/Positive
Senior unsecured debt rating	BB-

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Related Methodologies

Corporate Rating Methodology, July 2021

Rating Methodology: Retail and Wholesale Corporates April 2022

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Bloomberg: RESP SCOP

The financial risk profile (assessed at BBB-) benefitted from the record-high Scope-adjusted EBITDA in 2021, resulting in an improvement in credit metrics such as Scope-adjusted debt (SaD)/EBITDA, which was 2.1x instead of the forecasted 3.1x. For 2022, we forecasts credit metrics to deteriorate due to unfavourable market trends expected and Stavmat's acquisition of a Debrecen site that was not included in the previous business plan. The construction of the Dabas paving plant has no cost overruns as Stavmat has been able to adapt (e.g. by changing suppliers). Still, we expect its completion to be delayed by a few months against the initial deadline. Once the plant is fully operational, expected in Q4 2022, we expect improving credit metrics, including a SaD/Scope-adjusted EBITDA decreasing below 2.5x by 2024. We assess Stavmat's liquidity as adequate, based on the current cash reserves (HUF 4.6bn as of end-December 2021) in combination with the solid cash flow expected and no debt repayment scheduled until 2026.

Although Stavmat has included an annual HUF 500m dividend payout in its business plan, the company has stated its intention to refrain from dividend payouts in the next years. We have no reason to believe that management will deviate from this position. Furthermore, 90% of the planned investment capex for the Dabas plant, the primary use of the bond proceeds, has been paid for, thus the execution risk related to the plant has been reduced. As such, we view the financial policy as less aggressive but would need a longer track record before we could consider removing the negative one-notch adjustment. In our view, the company compares negatively (with a standalone rating of BB-) against peers regarding its size, but the associated risk (i.e. volatile cash flow, weaker competitive power) does not exceed the risk expressed by the B+ rating.

Outlook and rating-change drivers

The Outlook for Stavmat is Positive and incorporates our view that business growth will benefit from the recently acquired Debrecen site in addition to the start of production of the concrete paving plant in Q4 2022. We also assume Stavmat's ability to largely pass on inflationary pressures to its customers, which should support future growth. We expect an established track record of less aggressive financial policy, especially in light of the worsening market conditions (i.e. inflation, bottlenecks in supply-chains, volatility in Hungarian construction market). All should contribute to a SaD/Scope-adjusted EBITDA ratio of around 2.5x and stable operating cash flow.

The revision of Outlook to Stable may occur if none of the above were to materialise or if the company's business were to become more correlated to the construction industry through a higher share of construction materials production.

A positive rating action could be warranted by a SaD/Scope-adjusted EBITDA at around 2.5x on a sustained basis while an extended positive track record of Stavmat's less aggressive financial policy is obtained, Similarly, a positive action may occur if the company were to improve its business risk profile by expanding geographically to neighbouring countries, which is less likely in the near future.

A negative rating action may occur in the case of a SaD/EBITDA sustained above 3.5x. This could be triggered by a reversal of the current positive multi-year business cycle in the Hungarian construction market.

Rating drivers

Positive rating drivers	Negative rating drivers
• Leading wholesaler of construction materials for professional customers in Hungary • Adequate profitability margins in recent years, supported by the positive business cycle, expected to be sustained in medium term • Strong interest cover despite the issued bond of HUF 5bn in 2021 • Adequate internal liquidity with bond repayment risk only materialising in the long term	• Limited revenue size • Concentration on small domestic market • Margins highly dependent on the construction industry cycle and volatile cost of materials (representing over 90% of sales) • Weaker leverage after bond issuance • Limited cash flow cover in medium term amid construction of paving production plant • Lack of bank relationships or capital markets standing in case of need

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Positive track-record on less aggressive financial policy while keeping SaD/Scope-adjusted EBITDA sustained around 2.5x • Material increase in geographical diversification	• SaD/Scope-adjusted EBITDA sustained above 3.5x

Financial overview

			Scope estimates	
Scope credit ratios	**2020**	**2021**	**2022E**	**2023E**
Scope-adjusted EBITDA/interest cover[1]	131.5x	46.9x	15.7x	17.3x
Scope-adjusted debt (SaD)/Scope-adjusted EBITDA	0.5x	2.1x	2.5x	2.3x
Scope-adjusted funds from operations/SaD	177%	44%	36%	40%
Free operating cash flow/SaD	31%	-29%	8%	22%
Scope-adjusted EBITDA in HUF m	**2020**	**2021**	**2022E**	**2023E**
EBITDA	1,619	2,240	1,843	2,313
Operating lease payments in respective year	401	446	473	504
Other (including cash discounts)[2]	289	499	400	200
Scope-adjusted EBITDA	**2,309**	**3,185**	**2,716**	**3,017**
Scope-adjusted funds from operations in HUF m	**2020**	**2021**	**2022E**	**2023E**
EBITDA	1,619	2,240	1,843	2,313
less: (net) cash interest as per cash flow statement	3	-46	-149	-149
less: cash tax paid as per cash flow statement	-78	-113	-77	-81
add: depreciation component, operating leases	381	424	449	479
Other (including cash discounts)[3]	282	476	400	200
Scope-adjusted funds from operations	**2,206**	**2,981**	**2,466**	**2,763**
Scope-adjusted debt in HUF m	**2020**	**2021**	**2022E**	**2023E**
Reported gross financial debt	0	5,000	5,000	5,000
less: hybrid bonds	0	0	0	0
less: cash and cash equivalents	2,901	4,560	2,443	3,469
add: cash not accessible[4]	-2,901	-4,560	-2,443	-3,469
add: pension adjustment	0	0	0	0
add: operating lease obligations	1,246	1,578	1,681	1,773
Other	0	142	142	142
Scope-adjusted debt	**1,246**	**6,720**	**6,823**	**6,915**

[1] Scope-adjusted EBITDA/interest cover includes adjustments made for the interest component of operating leases.
[2] Others include disposal gains on fixed assets and cash discounts related to earlier payments to suppliers.
[3] Others include disposal gains on fixed assets, cash discounts related to earlier payments to suppliers and other financial expenses and income.
[4] Netting of cash: generally only applicable to ratings in the BB category or higher, and only if the cash is permanent and accessible.

Business risk profile: B+

Key drivers for Stavmat's business risk profile are its limited revenue size, concentration on a small domestic market, high dependency on construction industry cycles and vulnerability to the volatile cost of materials (representing over 90% of Stavmat's sales). However, the rating benefits from Stavmat's leading position as a wholesaler of construction materials for professional customers in Hungary.

Industry risk profile impacted by medium cyclicality

We assess the industry risk profile for the retail and wholesale industry at BB, as it is characterised by medium cyclicality and generally low market entry barriers. Substitution risk is considered low.

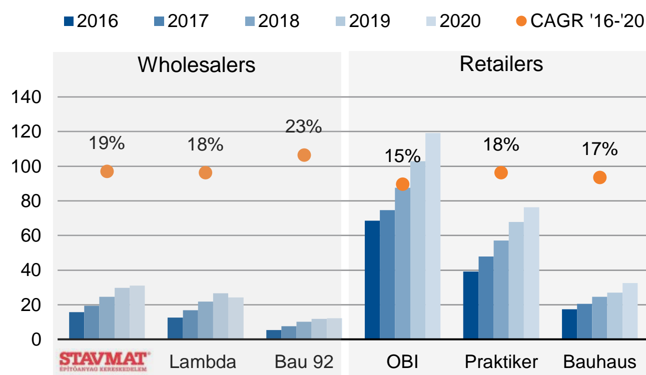
Business cycle benefits from the extension of favourable government policies

The construction industry in Hungary experienced robust and rapid growth between 2016 and 2021, one of the fastest rates in Europe. This growth was mainly due to government-driven orders, increasing disposable income, and low interest rates. 2020 saw a contraction in the market due Covid-19, but the industry promptly recovered by year-end. In 2021, the Hungarian government extended and strengthened its 'CSOK' family subsidy scheme launched in 2015, continuing its construction-friendly policies aimed at improving demographic trends within the country. State subsidies are expected to fuel demand for construction materials in the near term. The only risk could be capacity constraints on the part of local construction companies.

Leading 10% market share as a wholesaler despite small size

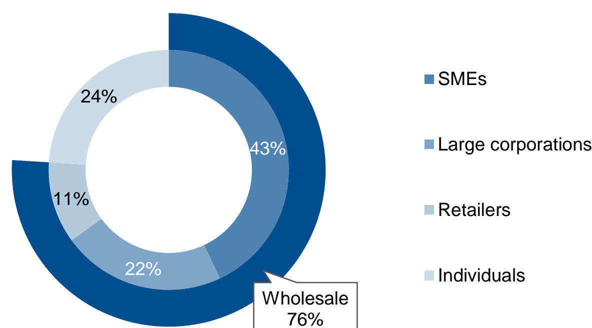
The Hungarian building materials trading industry is rather fragmented. Stavmat holds a leading 10% market share in the wholesaling of construction materials for professional use. The second largest competitor (Lambda) is close in terms of revenues but has almost 50% fewer stores. Stavmat also produces construction materials, which indicates that the real gap in terms of wholesale-only market shares is even wider. Stavmat's revenues are still small (HUF 38.8bn as of YE 2021) in an international context. However, even though Stavmat does not operate in a protected industry, we still assess the risk of new entrants in its market as only moderate in view of the high investment needs.

Figure 1: Revenue development versus peers (HUF bn)



Sources: Stavmat, Scope estimates

Figure 2: Revenue split by customer segment



Sources: Stavmat, Scope

Sustained revenue growth for all peers

Stavmat's revenue development in the past years has been in line with its direct peers': all the main players have benefited from the extremely positive multi-year cycle, which we expect to continue into the medium term.

Limited geographical and business diversification

Stavmat's concentration on the Hungarian wholesale market for the wholesale of building materials makes it vulnerable to shifts in the local economy and the construction business cycle (including the impact of government policies). Stavmat operates entirely in its national market, although its presence is broad. Export sales are currently negligible but may increase amid plans to export to neighbouring countries. In addition, sales are entirely via physical stores (i.e. no online).

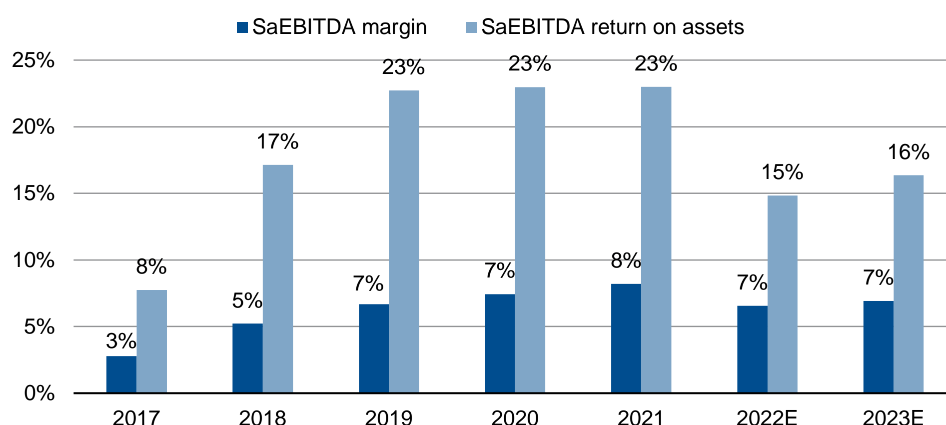
Varied product offering within construction materials

The company offers a varied range of construction solutions, including over 65,000 products covering the full range of both heavy and light classic construction materials. However, we consider the company to operate in only one product category. There are no major dependencies on the supplier or customer side.

Margins have been volatile over the decade

The development of the Scope-adjusted EBITDA margin in 2018-21, driven by government orders, is extremely positive for our assessment. Reported EBITDA margins fluctuated in the lower 1%-4% range in 2015-17. EBITDA was negative in the 10 years before 2015.

Figure 3: Scope-adjusted EBITDA margin and Scope-adjusted EBITDA return on assets



Sa = Scope-adjusted; Sources: Stavmat, Scope estimates

Cost of materials a key profitability driver

Overall, Stavmat's profitability is highly dependent on the cost of materials, representing around 92% of its revenues in 2017-21. For 2022, we expect the cost of materials to moderately increase due to current market trends before returning to historical levels in 2023 in view of continued market demand.

Moderate impact from supplier bonuses and credit management

Stavmat benefits from larger supplier bonuses than those of smaller peers as these are linked to order sizes, although the impact on overall profitability is moderate. Stavmat has strict credit management practices, resulting in a less risky receivables portfolio, as proved by the limited credit losses of within 0.1% in the past few years.

Profitability to remain adequate in the medium term on the back of solid demand…

The market is facing multiple challenges in 2022 with the Ukraine-Russia war resulting in volatile material prices and potential material shortages. The construction of the paving production plant in Dabas is supposed to boost profitability, although the impact will be limited initially. We anticipate a Scope-adjusted EBITDA margin of 6.6%. We expect the margin to increase to 6.9% once the impact of the production facility kicks in.

…but it can still be very volatile

Our profitability assessment reflects the implied volatility the company faces in terms of demand and the cost of materials, which could cause margins to deteriorate rapidly due to the small revenue base. Nevertheless, since the establishment of new ownership in 2016, the EBITDA margin has been positive and growing.

Financial risk profile: BBB-

Successful bond issuance in 2021

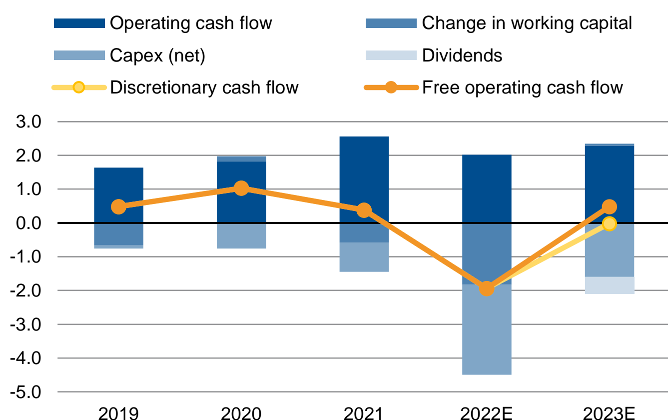
In 2021, Stavmat successfully issued the HUF 5bn bond under the Hungarian Central Bank's Bond Funding for Growth Scheme with a fixed 3% coupon rate. This pushed up the debt balance substantially as debt in previous years consisted only of operating leases. The bond proceeds are primarily being used to finance the construction of the concrete paving production plant in Dabas. Stavmat expects production to start in Q4 2022 instead of Q2, but the company does not expect cost overruns.

In addition, the property of Stavmat's Budapest headquarters was carved out in 2021 and is now owned by Parklife Kft., a member of IN Group (Stavmat's group), from which the company has been renting its Budapest headquarters.

Operating cash flows cover expansionary capex planned in 2021/22

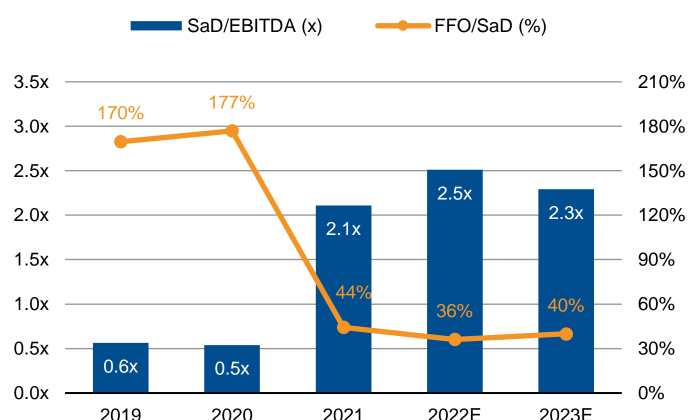
Stavmat has benefited from robust operating cash flow in the last few years, which peaked in 2019 at HUF 1.9bn and then decreased moderately in 2020 and 2021 due to working capital changes. Going forward, we see working capital needs remaining a constraint on operating cash flow growth, but the company generally has no issues with covering recurring maintenance capex. However, the planned expansionary capex has interrupted the positive free operating cash flow generation of the last three years and is expected to continue to do so in 2022.

Figure 4: Cash flow generation (HUF bn)



Sources: Stavmat, Scope estimates

Figure 5: Scope leverage metrics



Sources: Stavmat, Scope estimates

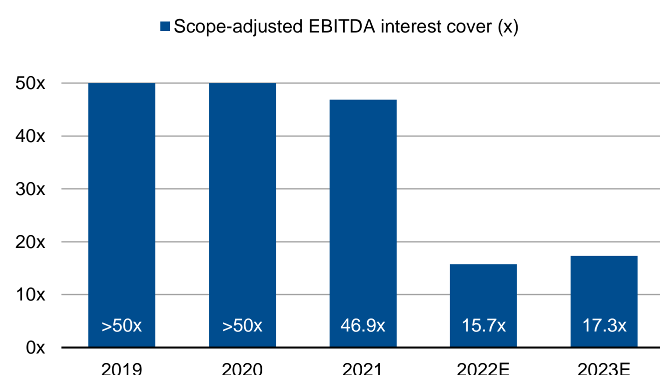
Deteriorating leverage upon bond issuance but still acceptable

Until 2020, leverage was sound as liabilities consisted only of leases. The bond issuance in 2021 cause financial metrics to deteriorate; yet, the unprecedented profitability resulted in better financial metrics than previously expected. Due to current market trends, we expect SaD/Scope-adjusted EBITDA to increase and remain around 2.5x in the next years. This will be driven by gradually increasing EBITDA amid the broadly stable debt. Funds from operations generation has been quite consistent for Stavmat, at 6%-7% of revenues over the last three years, benefiting from low financial expenses and taxes. We expect funds from operations/SaD to remain at around 40% over the next couple of years and Scope-adjusted EBITDA interest cover to remain above 10x.

Cash flow cover remains constrained in 2022

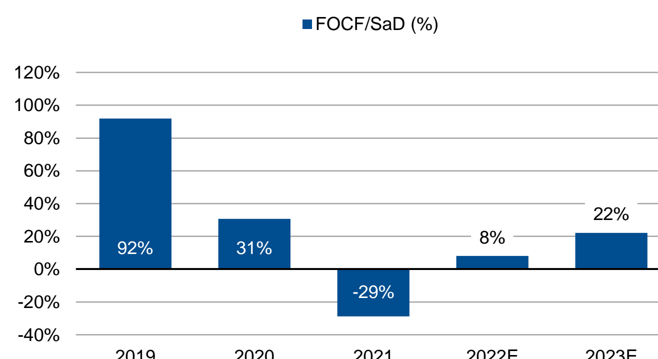
The cash flow cover metric for 2021 is considered exceptional at negative 29%, given the high net capex of HUF 2.7bn. In 2022, capex is expected to be lower at HUF 1.6bn, but a large part of it still includes the expansionary investment in the production plant. Going forward, capex will reduce and will mostly comprise maintenance capex. In the medium term, free operating cash flow/SaD will remain constrained below 10% in 2022.

Figure 6: Interest cover



Sources: Stavmat, Scope estimates

Figure 7: Cash flow cover



Sources: Stavmat, Scope estimates

Adequate liquidity

We assess liquidity as adequate in the medium term. This is based on current cash reserves in combination with the robust cash flow generation expected. Expansionary capex impacted liquidity in 2021 and will do so again in 2022 along with the acquisition of a site in Debrecen. However, no debt repayments are scheduled for the coming years since the bond will only start amortising in 2026 (bond amortisation will be HUF 500m a year until the 2030 balloon payment of HUF 2.5bn).

Figure 8: Liquidity table

Liquidity in HUF m	2020	2021	2022E	2023E
Cash and cash equivalents (t-1)	2,747	2,901	4,560	2,443
Restricted cash (t-1)	700	700	1,000	1,000
Committed unused bank facilities (t-1)	0	0	0	0
Short-term debt (t-1)	0	0	0	0
Free operating cash flow (t)	382	-1,940	549	1,527
Liquidity (%)	**No short-term debt**	**No short-term debt**	**No short-term debt**	**No short-term debt**

Sources: Stavmat, Scope estimates

Supplementary rating drivers: -1 notch

Financial policy is credit negative

Stavmat's risk appetite was limited until 2020. The company operated without bank debt (only leases) and followed a prudent approach, including owning most of its stores.

In 2020, however, on the back of the HUF 1.4bn in Covid-related government subsidies and the HUF 5.0bn planned bond issuance, the company decided to return to its shareholders HUF 1.8bn of committed reserves that had been granted by previous owners to back past losses. A more prudent approach would have been to compensate shareholders after the completion of the large capex plan.

Even though Stavmat has incorporated an annual HUF 500m dividend payout in its forecasts, management indicated that no dividend payout is planned for the following years. No dividend was paid in 2021 and we have no reason to believe management will deviate from this position, leading us to view the company's financial policy as less aggressive. Once an extended positive track record is gained, the removal of the negative one-notch assessment will be re-evaluated.

Parent support is neutral

Stavmat Zrt. is currently 100% indirectly owned by IN Group via the 100% ownership by Stavmat Stavebniny (Czech Republic). IN Group is a Slovakian investment holding company with diversified interests within the construction industries in Slovakia, the Czech Republic and Hungary. Its activities include the wholesaling and production of building materials, construction, and the development of real estate. The ultimate beneficial owner is Mr Pavol Kollar (67% share in IN Group). Stavmat Zrt. had operated independently from the group until now and we have therefore assessed it on a standalone basis. We expect the parent to have significant willingness to support Stavmat in case of need since Hungary is becoming an increasingly important market for the group. However, we assess parent support as neutral, also since we do not have visibility on the financial strength of IN Group.

In our view, the company compares negatively (with a standalone rating of BB-) against peers regarding its size, but the associated risk (i.e. volatile cash flow, weaker competitive power) does not exceed the risk expressed by the B+ rating.

ESG profile

Wholesalers are exposed to reputational risk indirectly. For example, product or labour management that has a negative social impact may prompt buyer renegotiations due to consumer boycotts, affecting sales, margins and inventory value. Also, the environmental footprint of a wholesaler with a wide network of brick-and-mortar shops (as Stavmat does) will remain fundamental to its development. Such companies will have to continue balancing the challenges of improving the energy efficiency of their large shops (comparable to hypermarkets) with increasing the flexibility of their space to incorporate additional distribution channels (e.g. click and collect).

Once the paving production plant is operating, Stavmat will also be exposed to the construction materials industry. Producers of construction materials have a significant environmental footprint: aside from the issues regarding the sustainability of raw materials, the production of construction materials regularly requires large amounts of energy and fuel, which often generate pollution and large amounts of waste (some of which is hazardous). These companies also face the risk of consumer behaviour shifts, with customers opting for more environment-friendly solutions and products.

Long-term debt ratings

Senior unsecured debt rating: BB-

We have affirmed Stavmat's senior unsecured debt rating at BB-, one notch above the issuer rating. Our recovery assessment includes the HUF 5bn senior unsecured bond (ISIN HU0000360714). We expect an 'above average' recovery (50%-70%) for outstanding senior unsecured debt in a hypothetical default scenario in 2024 based on a liquidation value method.

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