LR Group
Germany, Consumer Products

BB- NEGATIVE

Key metrics

			Scope estimates	
Scope credit ratios	2022	2023	2024 E	2025 E
Scope-adjusted EBITDA/interest cover	3.3x	2.4x	1.9x	2.2x
Scope-adjusted debt/EBITDA	4.2x	4.5x	4.6x	4.1x
Scope-adjusted funds from operations/debt	13%	6%	9%	12%
Scope-adjusted free operating cash flow/debt	-1%	-9%	-4%	1%

Rating rationale

The issuer rating continues to reflect our moderate business risk assessment of BB- and a weaker financial risk profile of B+ (revised from BB-). Supplementary rating drivers are credit neutral.

The **business risk profile** is characterised by moderate profitability with limited cyclicality, broad geographical diversification, and a good position in the European direct selling niche market of premium nutritional and cosmetics products. The business risk profile is constrained by the company's relatively small size, reliance on a single distribution channel, competitive environment, and high but decreasing concentration on few product groups.

The **financial risk profile** primarily reflects the deterioration of EBITDA interest cover below 2.5x, driven by higher interest expenses, a weak Scope-adjusted debt/EBITDA currently above 4.0x and cash flow cover below 5% despite low capex needs. Liquidity is adequate.

Outlook and rating-change drivers

The **Negative Outlook** reflects the observed deterioration in profitability in recent years, which has put pressure on credit metrics that are not commensurate with the previously established financial risk profile. We expect a slow recovery in EBITDA from the trough in 2024E based on soft consumer demand, and only a moderate reduction in interest expense going forward. This could result in leverage remaining above 4.0x and EBITDA interest cover below 2.5x over the medium term. In addition, the Outlook assumes that LR remains in compliance with its leverage financial covenants and does not assume any further business disruptions due to the current geopolitical tensions in Ukraine.

The **upside scenario** for the ratings and Outlook includes EBITDA interest cover recovering at or above 2.5x on a sustained basis

The **downside scenario** for the ratings and Outlook involves EBITDA interest cover remaining below 2.5x on a sustained basis

Rating history (LR Health & Beauty SE)

Date	Rating action/monitoring review	Issuer rating & Outlook
4 Nov 2024	New	BB-/Negative

Rating history (LR Global Holding GmbH)

Date	Rating action/monitoring review	Issuer rating & Outlook
4 Nov 2024	Outlook change and subsequent withdrawal	BB-/Negative
6 Nov 2023	Outlook change	BB-/Stable
8 Nov 2022	Outlook change	BB-/Negative

Ratings & Outlook

Issuer	BB-/Negative
Senior secured debt	BB-

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Related Methodologies

General Corporate Rating Methodology; October 2023

Consumer Products Rating Methodology; October 2024

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Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• One of largest direct-selling companies in Europe • Resilient but moderate profitability even during economic downturn • Favourable product positioning towards consumer trends of healthy nutrition and anti-aging • No material debt maturity in the medium term thanks to recent refinancing, but maturity wall in 2028	• Relatively small size in underlying large consumer products and retail markets, with focus on a market niche • Increased interest burden given exposure to variable rates • Currently weak leverage with Scope-adjusted debt/EBITDA at above 4x • Soft consumer sentiment slowing EBITDA recovery • Heavily dependent on leading brands (aloe vera based) and a few product groups • Approximately 45% of sales are concentrated in the DACH region, but overall extensive geographic diversification throughout Europe.

Positive rating-change drivers	Negative rating-change drivers
• Interest cover recovering above 2.5x on a sustained basis	• Interest cover remaining below 2.5x on a sustained basis

Corporate profile

Founded in 1985, LR Global Holding GmbH is a producer and seller of various consumer goods product categories focusing on the health, nutrition and beauty segments. LR has a niche orientation product-wise and a premium pricing strategy. The exclusive brand used is LR Health and Beauty consisting mainly of Aloe Vera and Aloe Via product ranges. LR's unique selling point is its distribution form as a direct seller via the internet and using a large number of sales partners (about 300,000) to generate revenue in what the company calls social selling. The company has no physical stores. Based in Germany, LR markets about 300 different beauty and health care products in a total of 32 countries. Customers are usually quality and lifestyle-oriented individuals looking for non-mass produced, natural products with the price being of lesser importance. LR employs around 1,200 employees worldwide.

LR Group's parent company is LR Health & Beauty SE, which is in turn owned by Luxemburg-based Aloco Holding S.à r.l., which is Quadriga's ownership vehicle. The German private equity investors Quadriga Capital and Bregal Capital (no longer represented) took over LR Group from Apax Partners in 2014.

Financial overview

			Scope estimates		
Scope credit ratios	**2022[1]**	**2023**	**2024 E**	**2025 E**	**2026 E**
Scope-adjusted EBITDA/interest cover	3.3x	2.4x	1.9x	2.2x	2.4x
Scope-adjusted debt/EBITDA	4.2x	4.5x	4.6x	4.1x	3.8x
Scope-adjusted funds from operations/debt	13%	6%	9%	12%	13%
Scope-adjusted free operating cash flow/debt	-1%	-9%	-4%	1%	1%
Scope-adjusted EBITDA in EUR m					
EBITDA	31	31	31	34	35
Other items	-	-	-	-	-
Scope-adjusted EBITDA	**31**	**31**	**31**	**34**	**35**
Funds from operations in EUR m					
Scope-adjusted EBITDA	31	31	31	34	35
less: (net) cash interest paid	(10)	(13)	(17)	(15)	(15)
less: cash tax paid per cash flow statement	(4)	(8)	(2)	(2)	(3)
add: dividends from associates	-	-	-	-	-
Other non-operating charges before FFO	-	(1)	-	-	-
Funds from operations (FFO)	**18**	**9**	**13**	**16**	**17**
Free operating cash flow in EUR m					
Funds from operations	18	9	13	16	17
Change in working capital	1	(8)	(4)	(1)	(1)
Non-operating cash flow	(4)	-	-	-	-
less: capital expenditure (net)	(6)	(6)	(6)	(6)	(6)
less: lease amortisation	(10)	(8)	(8)	(8)	(8)
Free operating cash flow (FOCF)	**-1**	**(12)**	**(5)**	**1**	**2**
Net cash interest paid in EUR m					
Net cash interest per cash flow statement	10	13	17	15	15
Change in other items	-	-	-	-	-
Net cash interest paid	**10**	**13**	**17**	**15**	**15**
Scope-adjusted debt in EUR m					
Reported gross financial debt	150	152	150	150	149
add: shareholder loan	-	-	4	4	4
less: cash and cash equivalents	(20)	(12)	(12)	(16)	(21)
add: non-accessible cash	-	-	-	-	
Other items	1	0	-	-	-
Scope-adjusted debt (SaD)	**131**	**140**	**142**	**137**	**132**

[1] FY 2022 figures refer to LR Global Holding GmbH, which was the consolidating entity for the group before LR Health & Beauty SE.

Table of Content

Environmental, social and governance (ESG) profile[2]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend

Green leaf (ESG factor: credit positive)

Red leaf (ESG factor: credit negative)

Grey leaf (ESG factor: credit neutral)

Reputational risk

Describing itself as a 'social' direct selling company, the social component is a key determinant of LR's success. The company's business model relies on its ability to attract new partners and retain them. Therefore, negative publicity or a negative public perception of the company, its competitors, or the direct selling business model in general, can have a significant negative impact on LR's revenues. The increasing penetration of social media enhances the risks of misinformation, which can occur even if the company is in full compliance with the strict quality standards for cosmetics and food safety or the labour laws in each of its geographies. We believe LR is more exposed to reputational risks than other consumer products companies because its business model relies on social interaction.

Product innovation

LR's key markets of nutrition and cosmetics require companies to continuously innovate to generate consumer interest and meet their evolving demands. However, we believe the company's R&D spending is sufficient to mitigate the risk of product obsolescence. LR's product portfolio is well positioned to address the increasing consumer demand for healthy nutrition and anti-aging.

Resource management

In line with most consumer product companies, management of natural resources is a relevant ESG factor. LR has set itself itself several environmental goals, including obtaining energy from renewable sources (and generating renewable energy), water reduction, and sustainable fishing.

[2] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BB-

LR's business risk profile, assessed at BB- (unchanged), is characterised by moderate profitability with limited cyclicality, broad geographical diversification, and a good position in the European direct selling niche market of premium nutritional and cosmetics products. The business risk profile is constrained by the company's relatively small size, reliance on a single distribution channel, the competitive market environment, and high but falling concentration on a few product groups.

Direct selling business model

LR sells its products exclusively via its sales representatives. As an independent sales partner with LR Health & Beauty, individuals can purchase products at discounted rates and resell them to customers, thereby earning a trading margin from the difference between the purchase and sales prices. Each product sold accrues "Points Value" (PV), which is standardised internationally to ensure fair assessment. As partners accumulate PVs, their Bonus Level increases, enhancing their earnings beyond the trading margin. These earnings are disbursed mid-month following the sales period. Additionally, partners can expand their business by recruiting new members into their team, which further increases their bonus potential. The more successful the team, the higher the individual bonuses at the end of each month.

Industry risk profile: A

Following the revised consumer product methodology, we have attributed to LR the industry risk profile of non-discretionary consumer products (A). This is because the company manufactures the majority of the items it sells (90% of its products are produced internally) and exclusively distributes its own branded merchandise. LR focuses on the niche market of health, nutrition, and beauty within consumer products. The business model built on specialised Multi-layer Marketing (MLM) or social selling shares traits with the retail industry due to the critical role of developing its unique distribution channel for long-term growth.

Good market shares

Although LR is relatively small within the vast non-discretionary consumer goods market, its addressable market is more limited due to its selling approach. LR has no presence in supermarkets or pharmacies, which dominate a large portion of the overall market. However, two notable features help offset this size constraint. Firstly, the company operates within specific health-related niche segments that benefit from current "green and healthy" consumer trends, driving growth. Secondly, future revenue generation potential depends on the growth of its large self-employed sales force (about 300,000 partners), who are increasingly motivated by entrepreneurial incentives. Partners enjoy individual discounts on their private sales and receive bonus payments based on the total revenue from their customer network. Additionally, career progression offers further benefits like eligibility for a company car. These factors somewhat counterbalance LR's smaller market share since direct selling and social media channels represent a growing, albeit small, portion of the global product demand. In its key markets, LR's market share in the direct selling channel ranges between 5% and 40%, according to PWC. Larger competitors in direct selling include Amway (a generalist), Herbalife, and Avon, which focus on the nutrition and beauty segments, respectively.

Positive revenue development despite challenging environment

LR managed to grow its sales by low-to-mid single digits percentage points in 2023 and during the first half of 2024, despite soft consumer demand in Europe, outperforming even larger direct selling peers. The development was bolstered by several new product launches in 2023, including the introduction of subscription-based health products, and by increasing the focus on the distribution network. Innovations at LR are driven by moderate but consistent R&D investment, maintained at approximately 1% of revenues. On the other hand, advertising is entirely managed by sales representatives, which somewhat limits the brand's broader market resonance but provides exclusivity (product not available elsewhere).

The company's product portfolio is invested in the long-term customer trend for increased healthcare awareness with a range of sustainable, quality-oriented products, led by innovations such as the recently offered Zeitgard and subscription-based health products (LR Health Mission, LR Body Mission). Customers are generally fairly affluent and less price-sensitive than traditional retail consumers.

Table 1: Recent product launches

Year	Product	Description
2022	Zeitgard Pro	Advanced skincare device designed for deep cleansing and anti-aging treatments.
2023	LR Body Mission	Weight management program including dietary supplements and meal plans (subscription).
2023	LR Lifetakt Mind Master Gold	New drinking gel variant (Gold) to complement the existing Mind Master portfolio.
2024	LR Health Mission	A subscription-based product range focusing on intestinal, liver, and cellular metabolism.

Source: LR, Scope

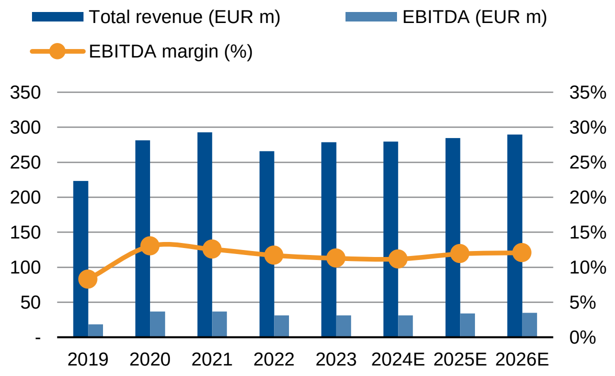
Limited diversification

Diversification continues to be the weakest competitive positioning element for LR. This is because the underlying market is a niche market, with regard to both the product portfolio and the addressable market (direct sales concept). There is a relatively high concentration of sales on certain product groups, notably the aloe vera products (drinking gels, skincare, and personal care items); however, several product launches in recent years are gradually reducing this reliance.

Asset risk is also a constraint. The company's production facilities are located at the headquarters in Ahlen, from where all subsidiaries are supplied and a significant share of products are manufactured and/or packaged.

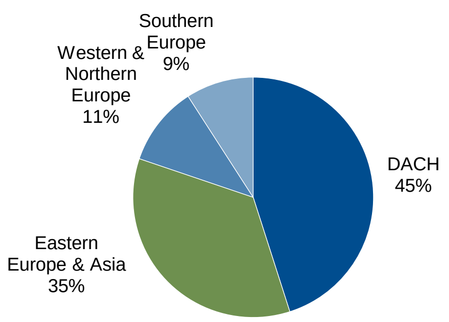
Diversification is partly mitigated by customer granularity and the moderate geographical distribution of sales across Europe (LR entered the UK market in 2023) and South Korea, with a significant portion of sales (around 45%) deriving from DACH countries. We assume no major concentration on the supplier side.

Figure 1: Revenue and EBITDA development



Source: LR, Scope estimates

Figure 2: LR sales based on geographical split



Source: LR, Scope

Moderate profitability

Profitability supports LR's business risk profile. The EBITDA margin has ranged between 9% and 13% over the past five years, demonstrating resilience even during periods of high inflation and the pandemic. Since the start of the ongoing conflict in Ukraine in 2022, EBITDA has stabilised at approximately EUR 31m annually (revenue exposure to Russia and Ukraine has since been reduced to the high single digits percentage points). We anticipate that this level will continue through 2024, improving to around EUR 34m in 2025 despite persistent soft consumer demand. This growth will be driven by the expansion of subscription-based products, the launch of new products, and a moderate recovery in Eastern European markets. The EBITDA margin remained stable at around 11.5% in 2023. Looking ahead, we project a moderate increase in the EBITDA margin to approximately 12%, supported by declining raw material prices and efficiencies from the completion of investment projects in a new logistics center and a digital platform for sales partners (both projects went live in 2024).

Generally, the company has pricing power, as its customers are not price sensitive. This means that it can transfer price increases to its customers in an inflationary environment. Additional growth drivers are innovations as well as the company's intensified incentivisation programme. The cost structure benefits from lower fixed costs as the sales force is self-employed. Thus, revenue increases have a greater chance of directly affecting profitability than for most competitors. Raw materials do not play a critical role for LR's profitability either as the company only purchases limited volumes of raw materials. This reflects well on limited raw material price dependency.

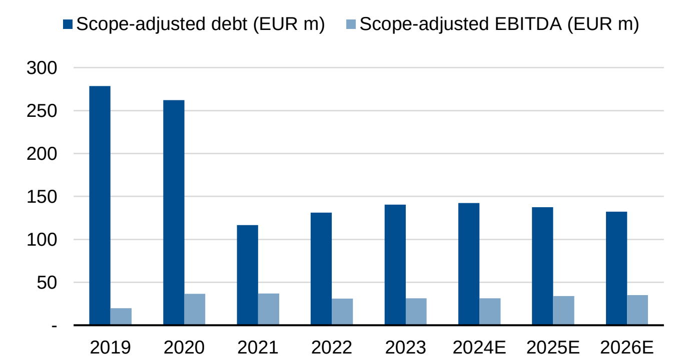
Business model reduces cyclicality

Economic downturns or periods of weak growth typically dampen consumer sentiment. However, LR's business model provides a dual advantage. Beyond product sales, LR offers a compelling and flexible income opportunity for individuals as sales partners (many sales partners operate on a part-time basis to earn extra income alongside a full-time job). This dual approach allows the LR Group to strategically emphasize either the consumer product segment or the distribution model, depending on prevailing economic conditions.

Financial risk profile: B+

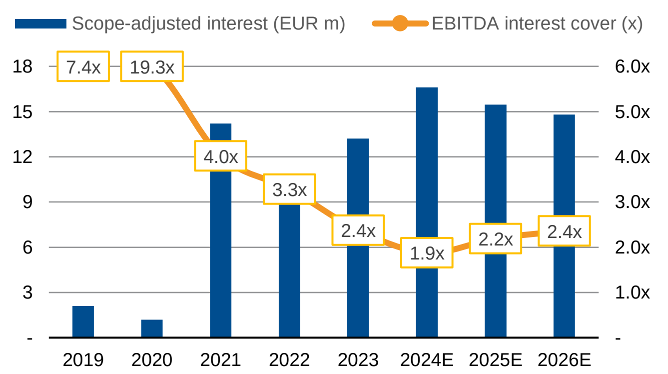
The **financial risk profile** of B+ (revised from BB-) primarily reflects the deterioration of EBITDA interest cover below 2.5x, driven by higher interest expenses, a weak Scope-adjusted debt/EBITDA currently above 4.0x and cash flow cover below 5% despite low capex needs.

Figure 3: Scope-adjusted debt and EBITDA



Sources: LR, Scope estimates

Figure 4: EBITDA interest cover



Sources: LR, Scope estimates

EBITDA interest cover below 2.5x

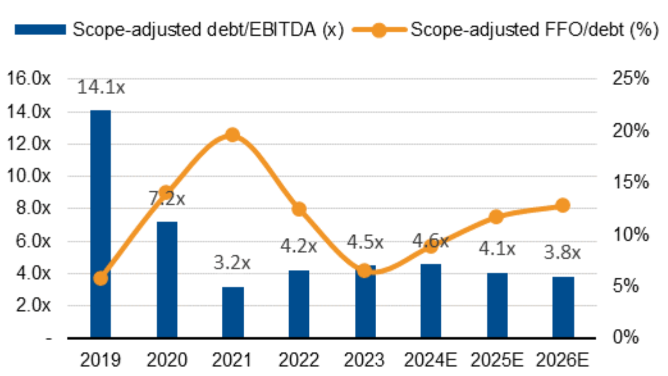
In 2023 EBITDA interest cover deteriorated below 2.5x, which was the existing negative rating trigger. The metric was negatively impacted by higher interests paid, up to around EUR 13m in 2023 from EUR 9m in 2022. This was driven by the increase of the Euribor reference rate applied to the EUR 125m bond, which represents over 80% of LR's gross debt. As of June 2024, debt also includes a EUR 8m fixed-rate amortising loan with Deutsche Anlagen Leasing GmbH maturing in 2042, around EUR 18m of lease liabilities and a EUR 4m shareholder loan linked to the refinancing transaction in Q1 2024 (PIK interests). With Euribor rates peaking in H1 2024, we project that interest expenses – including interests on leases and other loans – will rise to close to EUR 17m in 2024 but gradually decline afterward on decreasing reference rates. The bond refinancing in Q1 2024 resulted in a small increase of the nominal value by EUR 5m and a slightly higher applicable margin of 7.5% (compared to the previous 7.25%), hence leading to only a minimal impact on interests. We see EBITDA interest cover remaining below 2.5x based on the assumption of a slow EBITDA recovery and only a moderate reduction in interest rates.

Weak leverage at above 4x

Scope-adjusted debt/EBITDA rose to 4.5x in 2023, up from 4.2x in 2022, due to stable EBITDA and reduced cash (we continue to apply a 50% cash haircut). Contrary to our earlier projections of a significant improvement starting in 2024, we now expect leverage to remain stable in 2024 and to stay at or above 4.0x in the medium term. This is despite a slight decrease in Scope-adjusted debt owing to gradually increasing cash reserves.

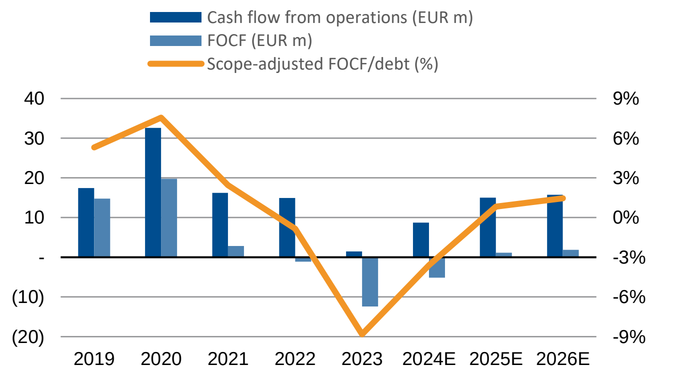
Similarly, Scope-adjusted funds from operation/debt declined to 6% in 2023 driven by higher taxes paid in previous years. We see a recovery towards 15% in the medium term.

Figure 5: Leverage metrics



Sources: LR, Scope estimates

Figure 6: Cash flows and FOCF/debt



Sources: LR, Scope estimates

Limited cash flow cover

Thanks to its relatively light asset structure, with capex averaging around 2% of revenues over the past few years, LR usually generates positive free operating cash flow (FOCF). Nevertheless, higher tax payments and large working capital needs, primarily driven by inventory build-up due to challenges in the logistic market, led to negative Scope-adjusted FOCF of EUR -12m in 2023. With gradual working capital normalisation, we expect FOCF/debt to again become positive from 2025 although remaining constrained at below 5%. Dividend payments are restricted by the terms of the bond.

Adequate liquidity

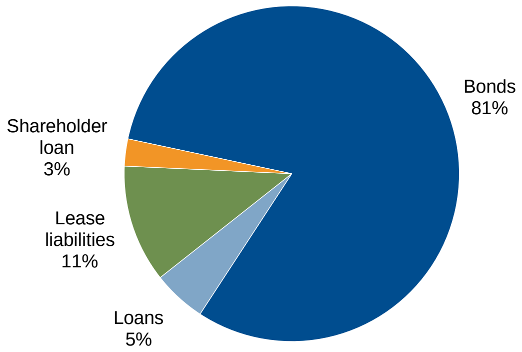
Liquidity benefits from a cash buffer of around EUR 13m as of June 2024, usually positive FOCF and immaterial short-term debt. The early refinancing in 2024 of the EUR 125m senior secured bond maturing in 2025 with a new EUR 130m senior secured bond expiring in March 2028 alleviated liquidity concerns over the forecasted horizon. Nevertheless, the maturity wall in 2028 could lead to increasing refinancing risk over time.

Balance in EUR m	2024 E	2025 E	2026 E
Unrestricted cash (t-1)	24	24	33
Open committed credit lines (t-1)	-	-	-
Free operating cash flow	-5	1	2
Short-term debt (t-1)	0.4	0.5	0.5
Coverage	**>200%**	**>200%**	**>200%**

Financial covenants

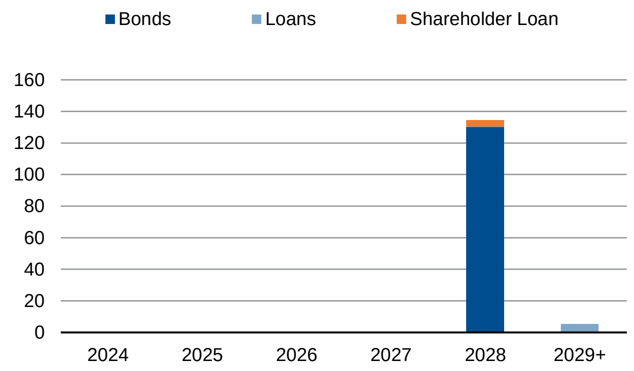
The new bond requires quarterly compliance tests with financial covenants concerning the leverage ratio (net debt/EBITDA) and the pre-IFRS16 leverage ratio. The buffer to the 5.0x leverage bond covenant was a moderate 13% as of June 2024, while it was considerably higher for the 6.0x pre-IFRS leverage covenant. We estimate that the buffer to the leverage covenant will gradually improve to well above 20% over time, even though the leverage covenant requirement tightens to 4.5x in 2026.

Figure 7: Debt split as of June 2024



Source: LR, Scope

Figure 8: Debt maturities (excluding leases) in EUR m



Source: LR, Scope

Supplementary rating drivers: +/- 0 notches

We have made no adjustments related to financial policy, peer group considerations, parent support, or governance and structure.

Long-term debt ratings

Senior secured debt rating: BB-

We haves affirmed the senior secured bond rating of BB- on LR Global Holding GmbH and subsequently withdrawn it for business reasons. At the same time, we have assigned a senior secured debt rating of BB- to LR Health & Beauty SE, in line with its issuer rating.

On 19 February 2024, LR Health & Beauty SE placed a senior secured bond with a nominal issue volume of EUR 130m and issue proceeds of approximately EUR 125m. These proceeds were be used to refinance, on 11 March 2024, the existing senior secured bond of LR Global Holding GmbH (ISIN NO0010894850), which was due to expire in 2025. Like the previous one, the new bond is issued in the so-called "Nordic bond format" under Swedish law and with the involvement of Nordic Trustee & Agency AB as trustee. The bond is traded on the Open Market of the Frankfurt Stock Exchange (ISIN: NO0013149658). The terms of the corporate bond require a listing on the regulated market of Nasdaq Stockholm by March 2025.

Average bond recovery

The recovery analysis is based on a distressed enterprise value of EUR 97m in a hypothetical default scenario in 2026. Despite the ‘above-average’ recovery expectation (50-70%), we refrain from up-notching the debt rating due to LR’s asset-light business model and the material uncertainty regarding its asset value in a hypothetical default scenario, which may be driven by increasing competition and/or a loss of confidence in the business and resulting departure of sales partners.

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