Corporates

SCOPE Scope Ratings

Rating Action Release

16 September 2020

Scope confirms BBB-/Stable issuer rating on Ceconomy

The confirmation reflects the company's comparatively solid performance in the first nine months of its fiscal year in 2020 and the much faster-than-expected recovery from the Covid-19 shutdowns.

The latest information on the rating, including rating reports and related methodologies, is available on this LINK.

Rating action

Scope Ratings has today confirmed its BBB-/Stable issuer rating on German consumer electronics retailer Ceconomy AG and resolved the review for a possible downgrade. The S-2 short-term rating has also been confirmed.

Rating rationale

The rating action follows the stronger-than-expected results for the first nine months of Ceconomy's fiscal year in 2020 (ending 30 September). While the Covid-19 crisis' potential implications for Ceconomy's business risk profile assessment were not as significant for the ratings, which assumed only a temporary weakness in demand, the potential effects on the group's financial risk profile, including its liquidity, resulted in Scope's placement of the ratings under review for a possible downgrade on May 2020. This relatively stronger risk for the ratings relative to the business risk profile is no longer in place. As Scope deems its base case projections to be conservative, and the resulting key credit metrics are unlikely to breach Scope's ratio guidelines, Ceconomy's ratings have been confirmed.

With regard to Ceconomy's **business risk profile**, two key factors regarding the Covid-19 crisis, namely, its length and depth, were much less severe in the last few months than initially expected. Ceconomy's third-quarter sales (April to June 2020) only declined moderately, by about 8% year on year. This is a much better performance than Scope had initially expected for a quarter significantly burdened by the closure of a large number of Ceconomy's physical shops and their gradual opening only during mid-May. This robust development is explained by the online business, which greatly mitigated the sales lost by physical shops. In the third quarter, the online business increased by 150% year on year, driving up its share to about 35% of group sales compared to about 13% in the third quarter of the previous year. Thus, the length of the crisis appears to have been much shorter than Scope had expected. In addition, group sales even returned to growth in May (+3%) and June (+12%) in an annual comparison, again driven by the continued strong online demand as well as trends including 'cocooning' (home office, home upgrading) and innovations (mobile air conditioning). The depth of the crisis has thus also had positive effects, as its quick turnaround had effects on profitability and resulted in no reliance on external liquidity support (see under financial risk profile). Helped by various cost-cutting measures such as the adoption of short-time working hours, management's full-year 2020 EBIT guidance is now expected to range between EUR165m-185m, while Scope's former base case incorporated a significant triple-digit loss. Ceconomy's guidance does not include restructuring expenses of up to EUR 180m in connection with additional job cuts announced recently (3,500 positions primarily outside of Germany) as well as the review of Ceconomy's store portfolio.

Ceconomy's **financial risk profile** is now more likely to show only a moderate deterioration than during fiscal-year 2019. This is driven by Scope's expectation that both revenues and operating profit will continue stabilising during August and September. Thus, contrary to Scope's former concern that Ceconomy's credit quality might suffer strongly in fiscal-year 2020, and including an uncertain trend of an operating recovery in the following year, Scope now thinks that credit metrics for fiscal-year 2020 are unlikely to deteriorate to levels critical for the rating (i.e. a leverage significantly above 2.5x). In addition, the group's liquidity continued to look healthy at the end of June due to good cash generation and only very little draw-down (EUR 75m) of the newly arranged EUR 2.7bn syndicated loan (including the EUR 1.7bn KfW loan which remained totally undrawn) signed in May 2020, granted as part of pandemic support measures in Germany. Thus, Scope deems it unlikely that this revolving line will need an extension. Supported by the good operating conditions in the first nine months of the current year, Ceconomy's cash at the end of June was at a comfortable EUR 933m. Thus, only about EUR 430m of financial debt reported on the balance sheet at the end of June 2020 represents capital markets debt (private placements, local bank loans), with the vast majority (about EUR 2.1bn) due to the conversion of formerly off-balance sheet operating leases under IFRS 16. As Scope deems its base case projections to be conservative and the resulting key credit metrics to not breach its ratio guidelines, Ceconomy's ratings have been confirmed.

Outlook and rating-change drivers

The Stable Outlook reflects Scope's expectations that Ceconomy's financial risk profile will not significantly deteriorate in the coming years as the Covid-19 crisis appears to be less impactful than initially expected. Specifically, current credit metrics continue to be reflective of the BBB category, as indicated by a Scope-adjusted debt/EBITDA ratio of below 2.5x (with the exception of a potential small deviation as a consequence of the Covid-19 crisis in fiscal-year 2020).

A higher rating could be triggered by an improved business risk assessment, for example, through better operating margins and free cash flow, possibly achieved by the successful execution of the introduced restructuring measures, or financial metrics sustainably exceeding aforementioned levels. A positive rating action is likely should the Scope-adjusted debt/EBITDA ratio improve to below 2x on a sustained basis.

A negative rating action could result from a more aggressive financial policy or a sustained, negative deviation from ratios commensurate with the present ratings, ie SaD-to-EBITDA of above 2.5x, on a sustained basis.

Rating driver references

none

Long-term and short-term debt ratings

There is no debt category rating.

The short-term rating of S-2 reflects Ceconomy's sound credit quality and is supported by adequate internal liquidity.

Stress testing

No stress testing was performed.

Cash flow analysis

Scope performed its standard cash flow forecasting for the company.

Methodology

The methodology used for these ratings and rating outlooks (Corporate Rating Methodology, 26 February 2020) is available on https://www.scoperatings.com/#!methodology/list.

Information on the meaning of each rating category, including definitions of default and recoveries can be viewed in the "Rating Definitions - Credit Ratings and Ancillary Services" published on https://www.scoperatings.com/#!governance-and-policies/rating-scale. Historical default rates of the entities rated by Scope Ratings can be viewed in the rating performance report on https://www.scoperatings.com/#governance-and-policies/regulatory-ESMA. Please also refer to the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope's definitions of default and rating notations can be found at https://www.scoperatings.com/#governance-and-policies/rating-scale. Guidance and information on how Environmental, Social or Governance factors (ESG factor) are incorporated into the rating can be found in the respective sections of the methodologies or guidance documents provided on https://www.scoperatings.com/#!methodology/list.

The rating outlook indicates the most likely direction of the rating if the rating were to change within the next 12 to 18 months.

Solicitation, key sources and quality of information

The rating was requested by the rated entity or its agents. The rating process was conducted:

With Rated Entity or Related Third Party Participation	yes
With Access to Internal Documents	yes
With Access to Management	yes

The following substantially material sources of information were used to prepare the credit rating: issuer, public domain and Scope internal sources.

Scope considers the quality of information available to Scope on the rated entity or instrument to be satisfactory. The information and data supporting Scope's ratings 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.

Prior to the issuance of the rating or outlook action, the rated entity was given the opportunity to review the rating and/or outlook and the principal grounds on which the credit rating and/or outlook is based. Following that review, the rating was not amended before being issued.

Regulatory disclosures

This credit rating and/or rating outlook is issued by Scope Ratings GmbH, Lennéstraße 5, D-10785 Berlin, Tel +49 30 27891-0.

Lead analyst Olaf Toelke, Managing Director

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The ratings/outlooks were first released by Scope on 10. September 2017. The ratings/ outlooks were last updated on 06 May 2020

Potential conflicts

Please see www.scoperatings.com for a list of potential conflicts of interest related to the issuance of credit ratings.

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