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Research Update:

Maima Grupe UAB 'BB+' Rating Affirmed On Improved Credit Metrics; Outlook Stable; Subordination Risk Elevated

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Rating Action Overview

- Lithuania-based Maxima Grupe UAB recently released its annual results for 2023 showing a strong recovery in credit metrics with free operating cash flow (FOCF) after leases of €150 million and a decline in S&P Global Ratings-adjusted leverage to 2.2x from 2.8x in 2022.
- Revenue increased by 13.4% to €5.8 billion, and S&P Global Ratings-adjusted EBITDA margins recovered by 110 basis points (bps) to 8.2% on the back of easing energy prices and tight control of the operating costs.
- According to our methodology, the subordination risk of the senior unsecured notes issued by Maxima Grupe has increased with a rise in share of secured debt in the capital structure over recent months. However, we expect that management will address this subordination risk in the next few months, and thereby avoid a downgrade of the issue ratings on the unsecured notes.
- We therefore affirmed the 'BB+' long-term issuer credit rating (ICR) and 'BB+' issue ratings.
- The stable outlook reflects Maxima's earnings growth, resulting in debt to EBITDA of about 2.0x-2.5x in the next 12-18 months and positive FOCF largely covering dividend payments.

Rating Action Rationale

We affirmed our 'BB+' issue rating on Maxima Grupe's senior unsecured notes due 2027 but imminent reduction in the share of secured debt in the capital structure is a key to maintain that rating level. In 2022, the group raised €240 million of senior unsecured notes and in 2023 €100 million of bank facilities that were secured by cash deposited in certain bank accounts to refinance the then outstanding €300 million notes that were repaid in September 2023. As of end-2023, the total of the group's €520 million financial debt including accrued interest comprised the €244 million unsecured notes (47%) and the €98 million bank facilities both issued by the parent, Maxima Grupe; and €178 million of secured and unsecured debt issued by the operating subsidiaries that are closer to the group's income-generating assets and that we consider as ranking structurally ahead. Maxima Grupe's bank facilities, that benefit from the bank accounts' pledge, and total debt at subsidiaries (together €276 million) account for the priority debt ratio of 53%. While this exceeds the 50% threshold, we derive the notching outcome as per our methodology expecting that the group will reduce the priority ratio in the next few months. This is mainly due to the mandatory debt amortization at the operating subsidiary level with €66 million due for repayment in 2024 and the group's ample liquidity. Maxima has the means, supported by its solid cash flow profile and high cash balance of €331 million, to reduce the share of secured debt in the capital structure. However, if the priority ratio is not reduced to below 50% by end-2024, we could downgrade the issue rating on the senior unsecured notes by one notch.

In 2023, Maxima's operating performance exceeded our expectations with growth driven by expansion in Poland and Bulgaria that keeps leverage at about 2.2x. High like-for-likes sales of 10.4% and 65 net new store openings in 2023 support Maxima's trading performance. At the same time, the easing of energy and fuel costs as well as slower growth in its fixed costs, led to an improvement in EBITDA margins by 110 basis points (bps) to 8.2% in 2023. We expect annual revenue growth of more than 5% in the next two years supported by 2%-3% like-for-like growth and similar revenue contribution from about 90-100 store openings per year mainly in Poland and Bulgaria. We expect further pressure from labor costs, following the high inflation in the Baltics and Poland between 2022 and 2023, offset by tight cost management and the expected benefits of exiting the loss-making delivery business. This underpins EBITDA margins remaining stable at 8.2%-8.3% in our forecast. Consequently, Maxima's adjusted leverage will stay flat in 2024 at about 2.2x achieved in 2023, down from 2.8x in 2022. We forecast financial debt to remain largely stable on higher growth investments and increases in dividends, and lease liabilities to expand with earnings.

With the successful expansion in Poland and Bulgaria, Maxima is progressively strengthening its business operations. The group has increased its revenue base by 46% to €5.8 billion in 2023 from €4.0 billion in 2019, mainly driven by the meaningful store expansion, operating a total of 1,599 own and franchise stores across five countries as of the end of 2023, of which 976 are in Poland and 124 are in Bulgaria. Revenue growth also benefited from the price increases in the last two years because of high inflation in all Maxima's operating markets, ranging between 13.0% to 19.5% in 2022 and between 8.6% to 10.9% 2023. The delay in price increases, but also steep increases in energy costs, led to a temporary margin contraction to 7.1% in 2022 that recovered swiftly to 8.2% in 2023 on the back of less pronounced growth in operating costs and lower energy prices year on year. We anticipate that the growth trajectory and profitability support the business risk. We see the group's focus on emerging markets characterized by generally higher volatility and lower GDP per capita; overall smaller scale relative to higher rated peers; and limited expansion prospects in Maxima's core geographies as constraining factors. The entrance of new competitors could challenge the group's long-term market leadership in its core markets or profitability. For example, the discount chain LIDL entering Lithuania in 2016, Latvia in 2021, and Estonia in 2022, led to a moderate contraction of Maxima Grupe's respective market shares, even though the group kept its leading positions and still high shares in those markets.

Maxima's financial policy supports the current rating but limits the upside. Due to sizable discretionary spending on dividends and growth investments, Maxima's credit metrics will only improve modestly from earnings growth in 2024-2025. The group has resilient adjusted FOCF to debt of about 20% in 2024 and 2025, which demonstrates high cash generation and a robust ability to withstand potentially stronger-than-expected operating setbacks. This is somewhat lower than 2023 but incorporates the groups ambition to increase its real estate ownership. Currently the group owns more than 30% of its store space, with an even higher share in the Baltics. This is coupled with our view of a supportive financial policy framework and the management and shareholder commitment to maintain leverage broadly within our expectation for the rating.

Maxima's credit quality is closely associated with that of its parent company, Vilniaus Prekyba (VP). Maxima is part of a wider, more diversified group, but remains the principal asset within it. Historically, Maxima's dividends to VP have partly funded VP's diversification and expansion into new businesses. This has enabled VP to increase its EBITDA base largely through self-funded investments, translating into more robust debt to EBITDA of about 2.2x in 2023. In our view, this gives VP a cushion in case of operating setbacks affecting Maxima's credit metrics. We would expect the group to adopt a more conservative financial policy to preserve Maxima's credit metrics and its long-term investment capacity. In the last two years VP has started to pay dividends to its ultimate holding Metodika and this will likely continue, so long as the payout allows both VP and Maxima to maintain similar leverage metrics as achieved in 2023.

Outlook

The stable outlook reflects our expectations that Maxima will maintain its leading market position in the Baltics, despite intensifying competition; and soundly execute its planned store expansion in Poland and Bulgaria, leading to revenue growth and a steady EBITDA margin of up to 8.3% in 2025. The outlook also considers Maxima's dividend distributions, funded with FOCF, and our expectation of adjusted funds from operations (FFO) to debt of more than 30% and adjusted debt to EBITDA of about 2.0x-2.5x over the next 12-18 months. In addition, we expect VP's debt to EBITDA of about 2.0x-2.5x and annual FOCF after leases to largely cover dividend payments.

Downside scenario

We could lower the ratings on Maxima if its leverage increased to 3.0x or higher, FFO to debt fell to below 25% at either Maxima or the wider group, FOCF after leases sharply fell, or Maxima's or VP's liquidity deteriorated. These could happen if:

- The group underperforms our base case, including a material decline in operating performance with diminishing profitability because of intensifying market competition, or a weaker macroeconomic environment in the Baltics or Poland weighing on margins or cash flows; or
- Maxima or VP adopted a more aggressive financial policy, leading to either increased dividends or large-scale, debt-funded acquisitions.

Upside scenario

We could raise the ratings on Maxima if the group successfully expands its scale, gains market position, and improves profitability translating into the following metrics:

- Adjusted debt to EBITDA falling sustainably below 2.0x for Maxima and VP;
- Maxima's FOCF after leases substantially exceeding its dividend payments, resulting in debt reduction; and
- Robust liquidity and capital structure with at least adequate headroom and weighted average

debt maturity.

We would also need to see a financial policy commitment from Maxima and its parent to sustain these credit metrics.

Company Description

Lithuania-based Maxima is the leading food retailer in the Baltic countries, with a market share of about 25%. Operating since 1998, the group expanded rapidly in its home market and started to develop internationally, entering Bulgaria in 2005 and Poland in 2012. In 2023, Maxima generated more than €5.8 billion in sales, with about €479 million of S&P Global Ratings-adjusted EBITDA. Maxima is fully owned by VP, a holding company with interests in other retail and restaurant businesses and a real estate group. Maxima is VP's most important asset, generating about 75% of its overall EBITDA.

Our Base-Case Scenario

Assumptions

- An expansion in real GDP in Lithuania and Latvia of about 2.0% in 2024 and 3.0% in 2025; after negative 0.3% in 2023.
- An expansion in real GDP in Poland of 2.8% in 2024 and 3.3% in 2025, after a stagnation in 2023.
- Inflation of about 2%-3% in the Baltics in 2024 and 2025, down from about 9% in 2023. Inflation in Poland to remain higher at 4.6% in 2024 and 4.2% in 2025.
- Food inflation could remain below the overall inflation levels across Maxima's key markets.
- An increase in revenue of 5.2% in 2024 and 5.5% in 2025, reflecting partially passed on inflation-related costs, leading to like-for-like growth of about 2.5%-3.0% in 2024. This is complemented by 90-100 store openings per year translating into 2.5%-3.0% revenue growth from store openings in the next two years, mainly in Poland and Bulgaria.
- Stable EBITDA margins of about 8.2%-8.3% in the next two years, which is mainly driven by our expectations of further pressure from labor costs, following the high inflation in the Baltics and Poland between 2022 and 2023. Higher costs are offset by the increased scale of its growing business in Poland and Bulgaria, logistics efficiency, and cost management at its loss-making delivery business, where the group stopped operations in Poland in March 2024.
- Positive working capital of about €20 million-€25 million per year.
- Capital expenditure (capex) to increase to 3.5% of revenue from 3.0% in 2023. This is mainly driven by the accelerating store expansion in Poland and Bulgaria and the increase in discretionary real estate investments.
- Dividends of more than €120 million, which reflects the higher end of the group's dividend policy to pay out 50%-70% of last year's net income leading to break even discretionary cash flows after leases and stable financial debt.
- No material acquisitions.

Key metrics

Table 1

Maxima Grupe UAB--Forecast summary

Period ending	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025	Dec-31-2026	Dec-31-2027
(Mil. EUR)	2020a	2021a	2022a	2023a	2024e	2025f	2026f	2027f
Revenue	4,226	4,485	5,154	5,845	6,147	6,483	6,839	7,203
Gross profit	522	541	538	677	715	761	813	868
EBITDA (reported)	385	367	369	479	506	541	581	624
Plus: Operating lease adjustment (OLA) rent	--	--	--	--	--	--	--	--
Plus/(less): Other	1	-3	0	0	--	--	--	--
EBITDA	387	364	368	479	506	541	581	624
Less: Cash interest paid	-33	-37	-44	-64	-75	-75	-76	-78
Less: Cash taxes paid	-25	-22	-23	-25	-33	-35	-38	-42
Plus/(less): Other	--	--	--	--	--	--	--	--
Funds from operations (FFO)	328	304	301	390	398	431	467	504
EBIT	221	190	183	278	293	310	330	356
Interest expense	35	39	49	65	74	74	75	77
Cash flow from operations (CFO)	277	325	319	428	422	456	493	531
Capital expenditure (capex)	100	106	128	175	215	227	239	252
Free operating cash flow (FOCF)	178	219	192	253	207	229	254	279
Dividends	87	106	95	70	123	130	140	152
Share repurchases (reported)	--	--	--	--	--	--	--	--
Discretionary cash flow (DCF)	91	113	97	183	84	99	114	127
Debt (reported)	495	504	567	520	519	519	519	519
Plus: Lease liabilities debt	689	683	683	768	798	831	865	900

Table 1

Maxima Grupe UAB--Forecast summary (cont.)

Period ending	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025	Dec-31-2026	Dec-31-2027
Plus: Pension and other postretirement debt	--	--	--	--	--	--	--	--
Less: Accessible cash and liquid Investments	-134	-172	-218	-251	-229	-219	-222	-236
Plus/(less): Other	44	--	--	--	--	--	--	--
Debt	1,095	1,015	1,032	1,037	1,088	1,131	1,162	1,183
Equity	387	415	417	555	618	688	765	850
FOCF (adjusted for lease capex)	77	135	102	91	74	90	111	133
Interest expense (reported)	35	39	49	65	74	74	75	77
Capex (reported)	100	106	128	175	215	227	239	252
Cash and short-term investments (reported)	184	219	287	331	311	303	308	324
Adjusted ratios								
Debt/EBITDA (x)	2.8	2.8	2.8	2.2	2.2	2.1	2	1.9
FFO/debt (%)	30	30	29.2	37.6	36.6	38.1	40.2	42.6
FFO cash interest coverage (x)	10.8	9.2	7.8	7.1	6.3	6.7	7.2	7.5
EBITDA interest coverage (x)	11.1	9.4	7.5	7.4	6.8	7.3	7.8	8.1
CFO/debt (%)	25.3	32	31	41.2	38.8	40.3	42.4	44.9
FOCF/debt (%)	16.2	21.6	18.6	24.4	19	20.2	21.8	23.6
DCF/debt (%)	8.3	11.1	9.4	17.6	7.7	8.7	9.8	10.7
Lease capex-adjusted FOCF/debt (%)	7	13.3	9.9	8.8	6.8	8	9.6	11.3
Annual revenue growth (%)	5.8	6.1	14.9	13.4	5.2	5.5	5.5	5.3
Gross margin (%)	12.3	12.1	10.4	11.6	11.6	11.7	11.9	12.1
EBITDA margin (%)	9.1	8.1	7.1	8.2	8.2	8.3	8.5	8.7
Return on capital (%)	15.4	13	12.7	18.3	17.8	17.6	17.6	18

Table 1

Maxima Grupe UAB--Forecast summary (cont.)

Period ending	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025	Dec-31-2026	Dec-31-2027
Return on total assets (%)	9.5	8.2	7.5	10.5	10.3	10.4	10.5	10.7
EBITDA/cash interest (x)	11.5	9.8	8.3	7.4	6.8	7.2	7.7	8
EBIT interest coverage (x)	6.3	4.9	3.7	4.3	4	4.2	4.4	4.6
Debt/debt and equity (%)	73.9	71	71.2	65.1	63.8	62.2	60.3	58.2
Debt fixed-charge coverage (x)	11.1	9.4	7.5	7.4	3	4.2	7.8	8.1
Debt/debt and undepreciated equity (%)	73.9	71	71.2	65.1	63.8	62.2	60.3	58.2

All figures are adjusted by S&P Global Ratings, unless stated as reported. a--Actual. e--Estimate. f--Forecast. EUR--euro.

Liquidity

We assess Maxima's liquidity as adequate. This reflects our calculation that Maxima's sources of liquidity will exceed its uses by more than 1.2x over the next 12 months, and our expectation that sources would cover uses, even if EBITDA declined by 15%. We estimate Maxima's liquidity sources for the 12 months started Jan. 1, 2024, include:

- Unrestricted cash and liquid investments of about €251 million;
- €44 million undrawn bilateral lines;
- Forecast cash FFO of €300 million (after leases); and
- Working capital inflow of up to €25 million.

Liquidity uses for the 12 months started Jan. 1, 2024, include:

- Debt amortization of about €66 million;
- Seasonal working capital requirements of about €50 million;
- Our estimate of maintenance and committed capex of up to €100 million; and
- Dividends to VP of €123 million.

Covenants

Requirements

While there are no maintenance covenants, Maxima must comply with incurrence-of-debt covenants stipulating a fixed-charge coverage ratio of below 2.0x and a group-defined net leverage ratio of below 4.25x.

Compliance expectations

We expect that Maxima will maintain sufficient headroom above the level of leverage over the next 24 months.

Environmental, Social, And Governance

Governance factors are a moderately negative consideration in our credit rating analysis of Maxima due to a greater number of senior management changes than the industry average. Although we generally associate frequent changes with the risk of strategic and operational missteps, we note that Maxima's operating performance has been stable. Moreover, most of the leaving personnel have remained part of the group in different positions. We also note that Maxima's governance structure includes the same person in the CEO and chairman position.

Environmental factors are a neutral consideration in our analysis of Maxima. Like other European food retailers, Maxima focuses on improving its environmental impact. The group aims to minimize food waste, reduce greenhouse gas emissions, and reduce its recourse to plastic packaging. In February 2024, Maxima received its Science Based Targets initiative (SBTi) validation because of its commitment to several targets to meet these challenges, including reducing scope 1 and 2 carbon dioxide emissions by 42% by 2030.

Social factors are a neutral consideration. Retail is a labor-intensive industry, and the political and societal focus on paying a living wage has increased. In retail, labor costs are one of the largest expenses and employers have been raising wages and benefits to attract and retain workers. Maxima employs 37,828 people in Europe. Collective bargaining agreements are in place for 46.5% of total employees. Markets in which Maxima operate have experienced the highest inflation in the eurozone varying between 8.6%-10.9% in 2023 compared with 5.4% for the eurozone. We estimate that inflation will remain slightly higher in Maxima's operating markets than in the eurozone in 2024. The elevated inflation implies further pressure to raise wages, which is reflected in our guidance that the S&P Global Ratings-adjusted EBITDA margin will stay at 8.2% in 2024.

Issue Ratings - Subordination Risk Analysis

Capital structure

As of December 2023, Maxima's capital structure comprises about €520 million of financial debt, of which €240 million is a senior unsecured bond due in 2027 issued by the parent holding company, Maxima Grupe. In addition, the group still has about €280 million of secured debt and/or unsecured debt at subsidiaries. This includes the €100 million raised with SEB and Swedbank at Maxima Grupe in 2023 that are secured, although only with a pledge of cash on certain bank accounts.

Analytical conclusions

The 'BB+' issue rating on the senior unsecured notes due 2027 is in line with the long-term ICR on Maxima. The priority ratio stood at 53% as of Dec. 31, 2023, indicating an elevated subordination risk for the senior unsecured notes. We expect that the company will take imminent measures to reduce the priority ratio to less than 50% within the next few months, underpinning the rating. Should the cumulative share of secured debt and unsecured debt at operating subsidiary level in the capital structure exceed 50% of the group's total financial debt at the end of 2024 or shortly after, we could downgrade the senior unsecured notes by one notch. Maxima has the means, supported by its solid cash flow profile and high cash balance of €331 million, to reduce the outstanding secured and structurally senior debt, of which €66 million is due in 2024. We will monitor this analytical point over the next months.

Ratings Score Snapshot

Issuer credit rating	BB+/Stable/--
Business risk:	Fair
Country risk	Intermediate
Industry risk	Intermediate
Competitive position	Fair
Financial risk:	Intermediate
Cash flow/leverage	Intermediate
Anchor	bb+
Modifiers:	
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Moderately Negative (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	bb+

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global

Corporate Issuers, Dec. 16, 2014

- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Industry Credit Outlook Update Europe: Retail and Restaurants, July 18, 2024
- Peer Comparison: European Food Retailers Resilient Amid Operating Shocks, Feb. 12, 2024

Ratings List

Ratings Affirmed	
Maxima Grupe UAB	
Issuer Credit Rating	BB+/Stable/--
Senior Unsecured	BB+