EF1

INSTRUMENT RATING

Neu CP

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Contacts

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RATING ACTION AND RATIONALE

- EthiFinance Ratings has reaffirmed the rating of the NEU CP instrument of ITM Entreprises SAS (ITME), for up to €1,250m, at EF1.
- ITME, the NEU CP issuer, is a subsidiary of Les Mousquetaires SAS (SLM) which is the consolidating entity. Since most production assets are owned directly or indirectly by ITME, and most financial debt is located in ITME, our rating for ITME is therefore considered to be equivalent to the rating of SLM as per our methodology. Unless specified otherwise, when we refer to 'the group' or 'the company' we are referring to SLM.
- The rating is supported by the solid positioning of the group, being the n°3 retailer in France, as well as its good diversification in terms of stores' format and activities. Moreover, the group is active in a resilient sector. ITME has also a rather conservative financial policy characterized by limited leverage despite its capital-intensive activities (a 2.8x EthiFinance Ratings' net leverage ratio at end-2022). The liquidity profile of the group is also strong with significant cash available and undrawn credit lines. Finally, the food and staples retailing industry is considered to be a low volatile industry through the cycle, which weights favorably on our credit metrics.
- However, the rating remains constrained by other characteristics of the industry rating. The food retail sector has indeed limited levels of profitability, and has been recently impacted by high inflation, only moderate and slowing growth, and strong competition among players – a picture which is not expected to materially improve over the next 12 months. Moreover, governance and shareholding are in line with what one could expect from a group of this size despite limited transparency compared to a listed company.
- In 2023, the group has committed to acquire 195 stores from Casino, representing c. €1.5bn sales, over a 3-year period. The first wave, concerning 61 stores for c. €560m sales, was completed in October and has been factored in our analysis. The second wave (72 stores concerned for c. €510m sales) is expected to be finalized within a maximum of 3 years. The third wave (62 stores and c. €430m sales) is intended to be completed in the same timeframe but at the option of Casino. Therefore, the second and third waves have been excluded in our analysis.
- In line with our methodology, the foods & staples retailing industry has medium ESG risks (heatmap score of between 2 and 3.5), which is neutral for our industry assessment. Our assessment of the company's ESG policy is neutral as well (company ESG score of between 1.5 and 3.5), resulting in no adjustments based on ESG considerations.

ISSUER DESCRIPTION

Founded in 1969, Les Mousquetaires (SLM) is the third-largest food retail group in France. It gathers together over 3,000 independent associates (local entrepreneurs) and numbers around 150,000 employees and c.4,000 stores in Europe, being present in Poland, Portugal, and Belgium in addition to France. The brands operated by SLM are: Intermarché & Netto (food); Bricomarché, Brico Cash, Bricorama & BricoPrivé (do-it-yourself); and Roady & Rapid Pare-Brise (mobility). SLM is the sixth-largest food processor in France with c. 60 industrial sites. It has its own logistic and property companies.

The group operates a franchisee business model, with the group in charge of upstream activities (wholesale, purchasing & logistics) while downstream (the running of local stores) is not part of the consolidated scope and is operated by the associates. Our rating applies to the upstream operations.

The group reported revenues of over €36.5bn for 2022 with adjusted EBITDA of c. €757m and a net adjusted leverage ratio of 2.8x.

FUNDAMENTALS

BUSINESS PROFILE

INDUSTRY RISK ASSESMENT

- **A resilient market with limited growth prospects**

The rating is underpinned by the resilient nature of demand for food & grocery products - which correspond to basic needs - even though growth prospects, and specifically for volumes, are considered rather low.

In the current context of high inflation, food retailers' margins are under some pressure. We consider the situation as manageable as food retailers are able to pass on higher costs in the form of price increases. Indeed, over the last two years, food prices have increased by c. 21% in France, broadly in line with inflation (two-year accumulated inflation of 21.3% as of October). However, the main effects on consumption are a downmarket shift and a drop in volumes as disposable income is squeezed.

- **Strong competition among players with low barriers to entry**

Barriers to entry are considered as rather low even though the sector requires efficient logistic & supply chain operations, which are capital-intensive. Competition is fierce among players in terms of prices and locality. Size is an important factor allowing better bargaining power vis a vis suppliers, absorption of fixed costs, and capacity to deploy large capex, all leading to good price positioning in a competitive market. As a consequence, profitability remains limited within food retailing sector.

COMPANY'S COMPETITIVE POSITIONING

- **A solid positioning in the food retail sector in France with strong market share**

SLM is the third-largest food retail group in France. The food retail activity focuses on supermarkets, with a significant rural positioning and with a physical presence on average each 17km in France. The group benefits from good price positioning, which is made possible by, among other factors, its vertical diversification in food processing. The group has been strengthening its share of the French food retail market, reaching 15.9% at the end of March 2023 from c. 14.0% in early 2017. Following the acquisition of the 195 Casino's stores, SLM' market share should grow by c. 1.2pts.

The group clearly has a competitive position with a solid market share, and a good positioning characterized by low dependence on poorly performing large hypermarkets, which are characterized by a significant percentage of non-food products.

- **Good diversification**

SLM has diversified into Belgium, Poland and Portugal and, in terms of activities, towards do-it-yourself (DIY) and mobility. However, French food retail & food processing are its main activities. We consider that the group has a good diversification profile sustained by its various activities and stores' format, even if in terms of geography France remains by far its main market (c. 88% of FY22 revenues).

GOVERNANCE

- **Shareholders**

The group is ultimately owned by around half of its associates. We consider that the group has a lean structure, with associates committed to - and rewarded for - running well their local stores, and who are involved in the management of the group. We note, however, that the governance is less transparent than usual standards for listed companies of this size.

- **Management quality**

Despite a decrease in EBITDA (from €919m to €757m between 2021 and 2022), impacted by inflation, the level of net adjusted leverage remains manageable, deteriorating from 2.3x to 2.8x. Overall, we consider that the group's management has a good track record. SLM's operating model, with associates in charge of running local stores, is in our view efficient in terms of cost management and rewards/incentives. We consider that the group has a rather conservative financial policy.

- **ESG policy**

The group targets to reduce its greenhouse gas emissions by 55% by 2030 compared with 2019. At end-2021, the group had already reduced its carbon footprint by 14% vs 2019. Around 80% of the group's CO2 emissions are linked to its food processing activities along with logistics, stores, and utilisation of final products. The group is targeting 32% of renewable energies in its energy mix by 2030 as well as to reduce by 40% its energy consumption (against 2014) by 2030.

FINANCIAL PROFILE

RESULTS AND PROFITABILITY

In FY22, the financial performance of the group was impacted by high inflation in Europe. Sales grew by 9.9% to €36.5bn while EBITDA decreased by 17.6%, from €919m to €757m. The EBITDA margin (2.1% in FY22 vs 2.8% in FY21) was impacted by high inflation and the delay in passing on cost increases to customers in the form of higher prices. Following the acquisition of Casino's stores, even just the first wave of the 195 planned over the next three years, we expect revenues to grow over our forecast period while margin is expected to return to a higher level as the group implements price increases.

CASH-FLOW AND LEVERAGE

Free cash-flow net of asset sales and after dividends, as calculated by EthiFinance Ratings, was negative in FY22, linked to a negative working capital variation and lower asset sales while capex remained significant. The EthiFinance Ratings-adjusted net leverage ratio deteriorated to 2.8x at end-2022 from 2.3x at end-2021.

The financial indebtedness of the group is the result of significant investments made in real estate, including at the logistical centres. For its covenant calculation, the group disclosed a net corporate debt-to-EBITDA ratio (excluding the property's net debt and EBITDA) of 0.7x as of end-2022 (vs 0.6x at end-2021). In terms of LTV, our total net debt-to-real estate value rose to 62% from 53% with c. 85% coming from the decrease in portfolio value (c. €3.1bn) and c. 15% stemming from the increase in net debt.

Despite the acquisition of Casino's stores, we expect the leverage ratio to decrease over our forecast period as a consequence of lower capex, as capex related to Casino's stores will be supported by the associates.

CAPITALISATION AND DEBT STRUCTURE

Group indebtedness is concentrated in ITME, and in the property companies. ITME is the main holding company. At the statutory level, ITME has a limited real estate portfolio of c. €15m but it owns the other group subsidiaries. ITM Immo Log and IEM are the main property companies with respectively €1.5bn and €1.4bn real estate portfolios.

The group indebtedness encompasses (i) 8 relationship banks (syndicated facilities, amortizing loans, asset-backed facilities, representing c. 15% of the gross debt), (ii) private placements subscribed to by institutions (c. 31%), (iii) the NEU CP (c. 20%), along with (iv) associates (25%). The debt with associates includes mainly short-term deposits collected from the associates and their operating companies. The group has a partial hedging policy of its debts. We took into account a part of interest income that relates to the hedging into the calculation of the effective interest coverage ratio.

The group's banking facilities are restricted by covenants, including an LTV ratio capped at 50% at IEM perimeter (19% at end-2022), a net corporate debt-to-corporate EBITDA ratio capped at 2.75x (0.72x at end-2022), and a corporate debt-to-corporate equity ratio of up to 100% (22% at end-2022).

LIQUIDITY

The funding mostly relies on (i) long-term general corporate financing from relationship banks & financial institutions, and (ii) short-term financing. The tenure of the long-term financings runs between five and ten years, relatively long maturities but still shorter than usual for real estate-based financing and so this debt requires regular refinancing, which the group is used to.

The short-term financings mostly comprise the NEU CP program (€682m drawn at end-2022) and short-term debt with its associates (€830m being short-term deposits at end-2022).

At end-2022, the group had €1.8bn of undrawn RCFs with c. 21% maturing in 2024, c. 17% in 2025, c. 21% in 2026, and c. 30% beyond 2026. The group recently added an additional RCF of €600m following the Casino assets acquisition.

We consider that the group has an "adequate" liquidity position, reflecting a good financial profile coupled with a good level of liquidity. The liquidity assessment is somewhat impacted by the reliance on short-term financings. Our assessment also factors in the seasonal working capital variation.

CREDIT METRICS EXPECTED EVOLUTION (CMEE)

Despite the short-term impact of the Casino stores acquisition, our Credit Metrics Expected Evolution (CMEE) is Stable.

MAIN FINANCIAL FIGURES

Main financial figures. millions of EUR	FY20	FY21	FY22	22vs21
Turnover	30 399	33 245	36 524	9.9%
Adjusted EBITDA	868	919	757	-17.6%
EBITDA Margin	2.9%	2.8%	2.1%	-0.7pp
Adjusted EBIT	129	212	-63	-129.9%
EBIT Margin	0.4%	0.6%	-0.2%	-0.8pp
EBT	148	195	97	-50.4%
Total Assets	11 969	11 880	12 740	7.2%
Equity	2 917	2 972	3 037	2.2%
Total Financial Debt	3 993	3 465	3 535	2.0%
Net Financial Debt	2 490	2 127	2 118	-0.4%
Equity/TFD	73.0%	85.8%	85.9%	0.1pp
NFD/EBITDA	2.9x	2.3x	2.8x	0.5x
Funds From Operations	509	512	471	-8.0%
FFO/NFD	20.4%	24.1%	22.2%	-1.8pp
EBITDA/Interest	21.8x	22.1x	26.5x	4.4x

RATING SENSITIVITY

Factors that may (individually or collectively) impact the rating:

- **Positive factors (↑).**

All things being equal, an upgrade to EF1+ could be triggered if the credit metrics of the group improved therefore resulting in an upgrade of the long-term rating used as a reference. Such an upgrade, would, for instance, result in a net adjusted leverage around 0.5x over a certain period of time.

- **Negative factors (↓).**

A downgrade to EF2 could be triggered by a deterioration in credit metrics with an EthiFinance Ratings' adjusted net leverage ratio above 3.5x for a sustained period and a deterioration of the interest coverage ratio below 10x, considering a stable CMEE and a liquidity risk assessment of "adequate".

REGULATORY DISCLOSURES

LEI: 969500LMMR83QL6TLK43

Initiation report: No

Last rating action: Initiation at EF1 on November 28th, 2022

Rating nature: Solicited short-term public rating initiation

With rated entity or related third party participation: Yes (the rating was published after having been reviewed by the issuer).

With access to internal document: Yes

With access to management: Yes

Ancillary services provided to the rated entity: No

Name of the rating committee chair: Guillermo Cruz, Chief rating officer

Material sources used to support the rating decision:

- Financial statements 2022, 2021, 2020
- Discussions with management and management presentation

Limitation of the Rating action:

EthiFinance Ratings believes the quality and quantity of information available on the rated entity is sufficient to provide a rating.

EthiFinance Ratings has no obligation to audit or verify the accuracy of data provided.

The rating was carried out in accordance with Regulation (EC) N°1060/2009 of the European Parliament and the Council of 16 September 2009, on credit rating agencies, and in accordance with the short-term and long-term corporate rating methodologies that can be consulted on https://www.ethifinance.com/en/ratings/methodologies and according to the short-term corporate rating scale available at https://www.ethifinance.com/en/ratings/ratingScale

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