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Caola Zrt.

March 2023

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CREDIT RATING		Initial	Monitoring	Review
	Date of Rating Committee:	11.02.2022	17.02.2023	15.03.2023
	Date of Publication:	14.02.2022	17.02.2023	xx.03.2023
Issuer Rating	Long-term rating:	BB-	BB- (under review)	BB-
	Outlook:	Stable	-	Stable
Bond Rating	Long-term rating:	BB	BB (under review)	BB
	Outlook:	Stable	-	Stable

1) The credit rating and the rating outlook were disclosed to the rated entity or related third party. Following that disclosure amendments in the credit rating and rating outlook have not been executed;
2) During the last 2 years, BCRA Credit Rating Agency AD has not provided ancillary services to the rated entity or a related third party.

BCRA – CREDIT RATING AGENCY AD (BCRA) *is the third fully recognized rating agency in the EU, registered pursuant to Regulation No. 1060/2009 of the European Parliament and of the Council. The credit ratings, assigned by the BCRA are valid throughout the EU and are fully equal to those, of the other agencies, recognized by the European Securities and Markets Authority, without any territorial or other limitations.*

On March 15, 2023, the **Rating Committee** of BCRA had a session about the review of the credit ratings of Caola Zrt. The session was headed by Dr. Kiril Grigorov - chairmen of the Rating Committee. In accordance with the updated Methodology for assigning a corporate credit rating, the members of the Committee discussed the company's operations and financial performance and assessed the key rating factors. Based on the discussion, the Rating Committee decided the following:

BCRA removes the "under review" status and **confirms** the credit ratings of **Caola Zrt.** with stable outlooks:

- Long-term Issuer Rating: **BB-**, Outlook: **Stable**;
- Long-term Bond Rating: **BB**, Outlook: **Stable.**

The official Methodology for assigning a corporate credit rating of BCRA (effective as of February 2023) has been applied:
https://bcra.eu/files/corporate_methodology_2023_en.pdf

The users of the rating can find information on the meaning of each rating category, including the definition of default in the published Global rating scale on the BCRA's website:
https://bcra.eu/files/global_scale_en.pdf

Information from the rated entity, the BCRA database and other sources of public information has been used in the rating review process.

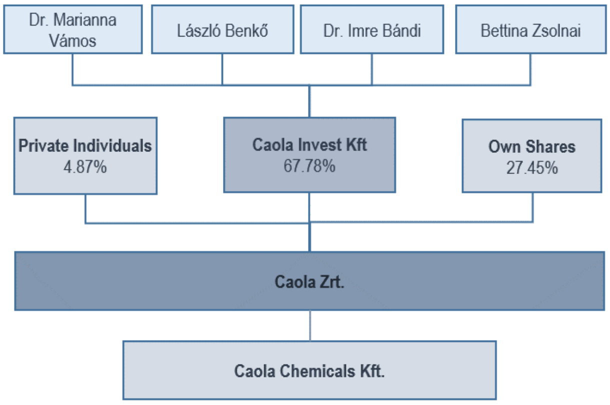
Table 1: General information about the rated entity

Issuer:	Caola Zrt.
Address:	Homokbanya ut 77, Diosd, Pest, Hungary
Registration number:	13-10-041783
Main business activity:	2042. Manufacture of perfumes and toilet preparations
Subscribed capital:	HUF 621 000 000
Bond ISIN:	HU0000361431

Company Overview

Caola is one of the oldest brands in Hungary and Caola Zrt. is the second oldest continuously operating Hungarian company as its legal predecessor was established back in 1831. The company's main activity is the production and sale of disifectants, beauty, personal, home and laundry care products. Given its outstanding history, Caola has contributed to the commercial and scientific development of the sector in Hungary in the last one and a half century.

Figure 1: Ownership structure of Caola Zrt. as of February 2023



Still owned by Hungarian individuals, the ownership of Caola group has changed throughout the years. In April 2020, Caola Invest Kft. acquired a majority stake in Caola Zrt. intending to bring the brand back among the market leaders.

The main activity of Caola Invest Kft. is leasing the real estate in Diósd to Caola Zrt. In addition, Caola Invest Kft. owns the Caola brand name for the use of which Caola Zrt. pays a royalty fee.

In September 2022, Coala Chemicals Kft. was established as a new 100% owned subsidiary of Caola Zrt. It is planned to be the distributor of the new product line (disinfectants for industrial livestock farming) in the future. Currently, Coala Chemicals is a non-active entity.

The management team is well qualified with adequate education profiles, long experience, and a wide range of expertise. Key management positions are held by Dr. Imre Bandi (Owner & CEO), Dr. Anikó Szaraz (Deputy-CEO), and Gyula Barta-Eke who joined the management team in April 2022 as a Board member.

Current leadership acquired the company in a weaker financial position but managed to revive the business via its new strategy shift in production to disinfectants in the depths of the COVID-19 pandemic. The mission of the management is to regain the old fame of Caola with a renewed product portfolio of well-known brands.

In addition, the group recently entered the market of disinfectants for large-scale livestock farming, being the only Hungarian producer of these products.

Caola Group currently has 2 production sites in Hungary - in Budapest and Diósd. After the completion of the new factory in Martonvásár, all machinery and equipment will be moved to it. The site in Budapest is leased, thus, the relocation to Martonvásár will result in a significant cost reduction for Caola Zrt.

The planned date of factory opening is scheduled in April 2023 while trial production is expected to commence in May 2023. The total cost of the greenfield investment was estimated at HUF 4.3 bln, jointly financed with a non-refundable state subsidy of HUF 2 bln and HUF 2.3 bln own funds. Due to the increased price of raw materials and the weakening of HUF, total investment costs increased by HUF 498 mln during the last year and the overrun was covered by unspent bond proceeds dedicated as a buffer for the investment.

At the beginning of 2023, Caola Zrt won a EUR 2 mln state grant (45% intensity) to establish a solar power plant at the newly developed Martonvásár factory. Thanks to this investment, the factory would turn into a self-sufficient green factory. Significant cost reduction can be realized not only for cosmetics and hygiene product production but for packaging material production as well. The operation of the solar power plant is planned to start in Q1 2024.

Market Position

The brand Caola is a respected Hungarian brand that is associated with quality, stability and tradition. Accordingly, Caola Zrt. has a strong, well-diversified product portfolio and committed partnerships with distributors and customers.

A snapshot of the company's flagship product lines is presented in the following figure.

Figure 2: Caola's flagship product lines

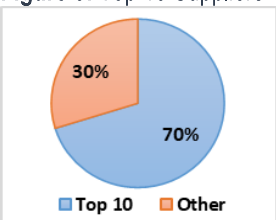
Professional disinfectants	Retail product portfolio	Professional cleaning productas	Disinfectants for livestock farming
• Disinfectants developed and produced for medical and government institutions	• Beauty & Personal Care Products • Home and Laundry Products	• New products, mainly used during commuting/ travelling	• Products that are specialized for fertilization of pig, cow and chicken farm

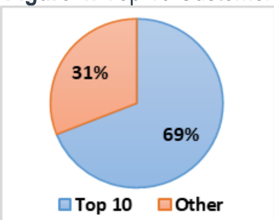
Regarding the Beauty Personal Care and Home Laundry Care market, Caola mainly focuses on the production and sales of Personal Care, Skin Care and Cosmetic products, while its most successful business segments are personal hygiene products and disinfectants.

Targeting in Retail Segment is well-diversified among the generation groups, as Caola is offering from classic cosmetics to household products and baby care products. The company's strategy envisages product development and rebranding. In the short term, the company plans to launch new products, namely luxury products, as well as new bio, vegan, and eco-friendly products. Rebranding is planned with new logos, a new portfolio outlet, and a change of packaging in Q1 2023. Reflecting the market trends, the management aims to increase B2C marketing through online communication channels and promotion campaigns with wholesalers.

Caola maintains good relations and cooperation with a range of suppliers of contracted manufacturing, raw materials, and packaging. The concentration is slightly elevated as the Top 10 suppliers accounted for 70% of total operational supplies in 2022. No significant disruption occurred in the supply chain due to the Russian-Ukrainian war.

Figure 3: Top 10 Suppliers **Figure 4:** Top 10 Customers





The company has a strong sales pipeline in the B2B channel. Most significant retail stores in Hungary are among the top customers which provide a reliable source of income.

In 2021, the Hungarian government launched a public tender for disinfectant procurement favoring Hungarian companies as suppliers. Being one of 15 selected companies, Caola successfully applied to participate in the procurement system announced by the Directorate General for Public Procurement and Supply. However, in September 2022, the government stopped all public payments to suppliers including KEF tender winners. Therefore, Caola's management decided not to deliver orders worth HUF 500 mln as it was uncertain when the government would pay.

In November 2022, the payments were resumed and Caola Zrt. won another KEF tender with a one-year framework agreement of HUF 4.3 bln, sighed in January 2023.

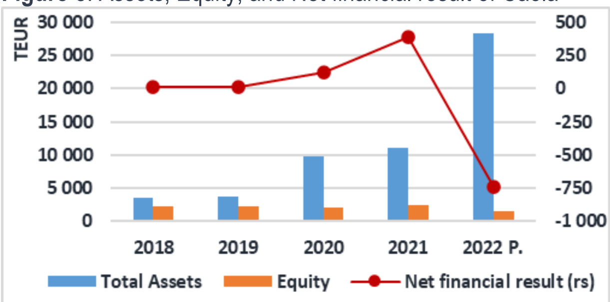
Concurrently, the sale of professional cleaning products is constantly rising and new contracts with major domestic and international players have been signed.

Traditionally the retail market in Hungary is ruled by multinational companies (Unilever, P&G, Henkel, Avon, and Johnson&Johnson), thus, Caola occupies an insignificant relative market share of about 1%. On the other hand, the rated company has specific strengths compared to multinational competitors, as its brand is well-known and nationally trusted, and can quickly respond to local consumer trends.

Concurrently, Caola has managed to become one of the TOP 5 market players regarding professional disinfectants in Hungary and aims to gain the leading market position by eliminating competitors through acquisition. The acquisition will be financed with the proceeds from the bond issued in April 2022. The management of Caola is currently negotiating the transaction terms.

Financial Analysis

Figure 5: Assets, Equity, and Net financial result of Caola



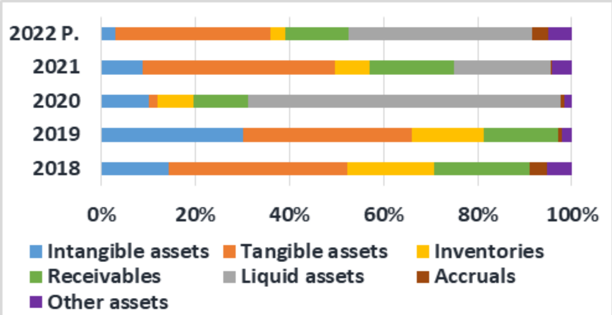
The assets of Caola have demonstrated a straight upward trend during the last four years. According to the preliminary financial statements for 2022, total assets peaked at a record high value of TEUR 28 286, increasing from EUR 11 145 at the end of 2021. The extraordinary increase mainly reflected the unspent bond proceeds that have been short-term deposited at a commercial bank.

In parallel, the shareholders' equity marked a moderate downward trend, annually decreasing by 32.5%[1] to TEUR 1 543 as of end-2022. Equity dynamics were determined by the accumulated

[1] Cited growth rates are calculated using the original values in forints, while the data presented in the report is converted in EUR using the official NBH's EOP exchange rate.

balance sheet loss. Following the record profit of TEUR 390 in 2021, the net financial result deteriorated to a loss of TEUR 743.

Figure 6: Structure of assets: 2018-2022

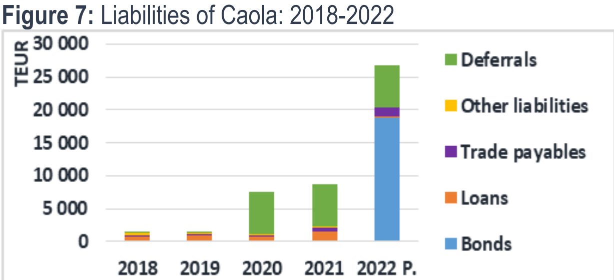


As the liquid assets expanded from TEUR 5 590 in 2021 to TEUR 16 752 at the end of 2022, they temporally overtook the leading position in the assets structure, accounting for 40.5% of total assets. Concurrently, the second largest assets group – tangible assets also recorded a large annual increase of 127.9%. In line with the construction of the factory in Martonvásár, the sum of tangible assets gradually peaked at TEUR 9 585 as of end-2022, representing 33.9% of total assets.

Receivables accounted for about 16% of total assets on average in 2018-2022, while in absolute terms their amount expanded from TEUR 747 at the beginning of the analysed period to TEUR 3 894 by the end of it. The most pronounced accumulation of receivables (+127.9% YoY growth) was recorded namely in the last financial year.

In 2022, inventories peaked as well, reaching TEUR 978. Accordingly, the inventories turnover ratio deteriorated to 2.9 (from 4.1. on average in 2016-2021), as the stocks grew by 27.8% and sales revenue dropped by 10.7% in annual terms. The accumulation of stocks partly reflected the above-mentioned stop of governmental payouts with part of KEF orders being produced but not delivered.

Figure 7: Liabilities of Caola: 2018-2022

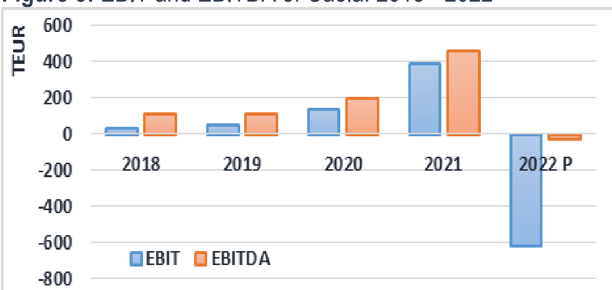


Mirroring the expansion of assets, the liabilities of Caola have been on the upside since 2018. Following the successful HUF 7.5 bln bond issuance, total liabilities (incl. accruals and deferrals) expanded to TEUR 26 743 at the end of 2022, from TEUR 8 666 a year ago. Passive accruals related to the received subsidies occupied the dominant share in the liabilities structure in 2020 and 2021 but after the accumulation of bond liabilities their relative share fell to 24%. Concurrently, loan liabilities annually declined by TEUR 1 326, to TEUR 194 or below 1% of total liabilities. Also, the relative share of Trade payables and advances declined to 5.1% in 2022, while their absolute value recorded a prominent annual increase of 153.3%.

The term structure of liabilities has been traditionally dominated by short-term liabilities, however, it changed in 2022 due to the accumulation of long-term bond liabilities. As the unspent bond proceeds inflated the cash, the current liquidity ratio only temporally peaked at 228%, compared to 118% on average for the period 2018-2021.

The net financial result has remained positive during the period 2016-2021, while in 2022 the company recorded a loss of TEUR 743. The deterioration reflected the combined effect of the negative EBITDA achieved and the large increase in depreciation costs.

Figure 8: EBIT and EBITDA of Caola: 2018 - 2022



The dynamics of net sales revenues have been less volatile but again with a negative trend as they declined by 10.7% YoY against the record high value in 2021. In parallel, total OPEX rose by 20.8% in annual terms mainly due to the higher depreciation, and to a smaller extent due to the increase in personal expenditures and inflated prices of raw materials, delivery, and energy. Given the renewal of machinery and equipment in the new factory, the company booked TEUR 595 depreciation cost in 2022, which is well above the average value of EUR 70 in the previous five years. Excluding the effect of depreciation, the EBITDA decreased from TEUR 458 in 2021 to TEUR -22 in 2022.

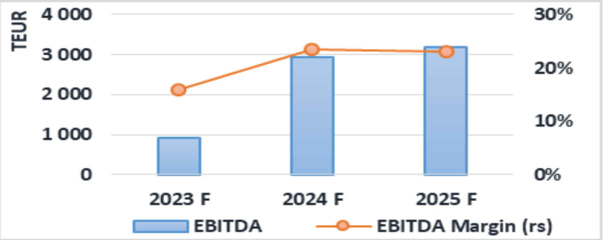
Amid the negative results and the accumulation of bond liabilities, the profitability indicators and some key credit metrics (presented in the Appendix table) temporarily deteriorated. However, Caola still positions relatively well among the peer companies group and demonstrates prerequisites for gaining a stronger market position in the medium term while preserving its financial soundness.

Financial Forecast

A financial forecast for the period 2023 – 2025 has been prepared based on the preliminary results for 2022 and a business plan provided by Caola's management which are considered relevant and broadly achievable. Namely, the following key assumptions have been adopted:

- Planned sales revenues in 2023 reflect the new public procurement tender of HUF 4.3 bln, signed in January 2023;
- The revenue growth in 2024 is explained by the strengthening of new product lines, new contracts, and partnerships that are in the pipeline in the field of professional cleaning and disinfectants for livestock farming;
- The ratio of turnover to material expenses is forecasted to decrease thanks to efficiency improvements related to the modernized machines and production lines in Martonvásár and the closure of the Budapest factory;
- Energy costs are expected to fall in 2024 due to the solar power plant investment;
- Caola Zrt will provide EUR 10 mln intercompany loan to Caola Invest Kft to finance the planned acquisition. The interest rate on the IC loan is set at 6.3%.
- No additional bank borrowing is assumed;
- Caola Zrt will receive a loan from its owner in 2023 for the development of the solar power plant. Interest will be capitalised, and no interest or principal repayment will be allowed before the maturity of the bond.

Figure 9: Forecasted EBITDA and EBITDA margin of Caola



If the revenue targets are successfully met, Caola is expected to record a constantly increasing EBITDA-expanding from TEUR 929 in 2023 to TEUR 3 178 in 2025. Also, the profitability will improve with EBITDA margin stabilising at about 23% from 2024.

Following the bond issuance, gross financial debt temporarily peaked and the Net debt-to-Equity ratio is expected to reach 13.8 as of end-2023, before gradually falling to 5.76 at the end of the forecasted period. However, the company is able to generate sufficient free cash flow to timely service its obligations without difficulties, with EBITDA interest coverage of above 2.5x from 2024.

Bond Rating

Table 2: Main bond parameters

Issuer	Caola Zrt.
Date of issue	04.04.2022
ISIN	HU0000361431
Face value	HUF 7.5 bln
Discounted value	HUF 7.06 bln
Currency	Forint (HUF)
Tenor	10 year
Coupon	fixed, 5.8% p.a.
Amortization	10% p.a. from the fifth year
Baloon	50% on maturity
Guarantor	Target company (yet not acquired)

In April 2022, Caola Zrt. issued a 10-year bond with a face value of HUF 7.5 bln (and HUF 0.4 bln discount) in an auction within the framework of the Bond Funding for Growth, launched by the National Bank of Hungary. The principal repayment schedule envisages a 10% annual amortisation starting from the fifth year after issuance and a 50% balloon payment at final maturity. The bond has a fixed annual coupon of 5.8%

Bond proceeds are earmarked to 1) indirectly finance Caola Invest Kft's (parent company) acquisition, and 2) partially finance the investment of the new production factory in Martonvásár. Following the acquisition, the acquired company(s) will be established as guarantor(s) of the bond, according to the bond prospectus.

As of end-2022, HUF 2.56 bln of the bond proceeds were spent to cover the investment in Martonvásár. Since the delay in the acquisition plan became apparent, the unspent bond proceeds of HUF 4.5 bln have been short-term deposited with a higher average interest rate than the bond coupon.

Table 3: Forecasted aggregated metrics of Caola + Target companies (guarantors of the bond)

ratios	2023 F	2024 F	2025 F
Leverage (TL/TA)	56.82%	51.32%	46.66%
Net Debt-to-equity	1.78	1.14	0.54
EBITDA Margin	13.45%	24.67%	24.99%
EBITDA interest coverage	1.85	4.96	6.15
Net Debt-to-EBITDA	9.51	2.73	1.51

As the management of Caola is still negotiating the acquisition terms, BCRA has assessed the creditworthiness of the potential bond guarantors. The medium-term financial forecast shows that the guarantors have a good capacity to serve additional commitments that may arise in case of activation of their guaranty on Caola's bond issue.

The combined credit metrics of the Issuer and the potential guarantor show that the debt service of the bond will be well secured with EBITDA interest coverage of above 180% during the whole forecasted period and a Net Debt-to-EBITDA ratio falling to 1.5 in 2025.

The forecasted aggregated metrics are better than the stand-alone metrics of Caola Zrt. Accordingly, BCRA has decided to apply **a one-notch upgrade** on the long-term issuer rating "of Caola Zrt

General Conclusions: The **issuer credit rating** of Caola Zrt. is backed by its longstanding history of successful business development and sound credit metrics. On the other side, the small market share and track record of moderate profitability represent rating constraints. The outlook is **stable**, indicating that current risks are broadly balanced. Despite the increase in gross financial debt, we believe that Caola Zrt. will be able to generate sufficient cash flow to timely service its obligations.

The following factors could lead to a **positive change in outlook** and/or a **rating upgrade;**
1) strengthening of the company's market position through expansion of business activities and product diversification;
2) higher profitability of operations;
3) reduction in indebtedness.

The following factors could lead to a **negative outlook change** and/or a **rating downgrade**:
1) unreached revenue targets in case of unsuccessful business development of new product lines and/or market turmoil, leading to sustained negative financial results;
2) material increase in leverage;

The long-term credit rating of the **guaranteed bond** is based on the specific acquisition plan, provided by Caola's management.

APPENDIX

Table 4: Key financial indicators of Caola: 2018 - 2022

TEUR	2022 P	2021	2020	2019	2018
Total assets	28 286	11 145	9 704	3 615	3 568
Fixed assets	10 514	5 539	1 171	2 402	1 945
Current assets	16 752	5 590	8 445	1 192	1 491
Cash and cash equivalents	11 454	2 296	6 495	1	3
Equity	1 543	2 480	2 112	2 197	2 247
Gross financial debt	18 933	1 521	767	829	670
Operating revenues	3 241	3 852	4 424	2 930	4 575
Net sales revenues	2 808	3 409	3 038	2 263	2 782
Net financial result	-743	390	123	11	14
EBITDA	-22	458	202	108	112
ratios					
ROA	-2.6%	3.5%	1.3%	0.3%	0.4%
EBITDA Margin	-0.7%	11.9%	4.6%	3.7%	2.5%
Total Leverage (TL /TA)	94.5%	77.8%	78.2%	39.2%	37.0%
Net Debt-to-Equity	4.85	-0.31	-2.71	0.38	0.30
Net Debt-to-EBITDA	-336.2	-1.7	-28.3	7.6	5.9
EBITDA interest coverage	-0.7	13.6	35.6	4.6	7.5
Current Liquidity	228.0%	69.4%	117.8%	119.6%	165.7%