MOODY'S RATINGS

Rating Action: Moody's Ratings downgrades Vestel to Caa1; outlook negative

15 Apr 2025

Paris, April 15, 2025 -- Moody's Ratings (Moody's) has today downgraded the long term corporate family rating (CFR) of Vestel Elektronik Sanayi Ve Ticaret A.S. (Vestel or the company) to Caa1 from B3 and the probability of default rating (PDR) to Caa1-PD from B3-PD. We have also downgraded to Caa1 from B3 the instrument rating on the $500 million guaranteed senior unsecured notes due 2029 issued by Vestel. The outlook has changed to negative from stable.

RATINGS RATIONALE

Today's rating action reflects our concerns about the company's weakening liquidity position. It also reflects Vestel's weak operating performance in 2024 that has substantially weakened the company's credit metrics and highlighted its vulnerability to macroeconomic volatility and competition.

Vestel's liquidity has weakened based on our assessment, which evaluates a company's ability to meet its liquidity requirements - including debt repayments and cash operating needs - over the next 12-18 months using liquidity sources such as cash, committed credit facilities and expected cash flow generation.

In 2024, the company's negative free cash flow increased to TRY22.7 billion from TRY5.5 billion a year earlier, leading to an increase in debt of TRY18.2 billion. Despite the company's $500 million (TRY17.7 billion) international bond issuance in May 2024 that was used to replace a significant portion of the company's short term debt with long term debt, Vestel's short term debt balance increased by the end of the year to TRY43.5 billion against TRY40.6 billion a year earlier. The large balance of short term debt compares to a cash balance of only TRY2.7 billion and no committed credit facilities.

We also expect that free cash flow will remain negative over the next 2-3 years. This makes the company dependent on the continued roll-over of maturing debt. While banks have so far remained supportive of rolling over maturing facilities, and we expect they will continue to remain supportive of domestic Turkish exporters such as Vestel, the company's high dependence on loan renewals heightens refinancing risk. Further liquidity risk emanates from restrictions the company has under its bond documentation on incurring additional indebtedness.

The company is subject to two incurrence-based covenants. The first restricts the company from incurring additional debt if its consolidated net debt to EBITDA ratio exceeds 3.5x. The second restricts the debt at its non-guarantor subsidiaries, primarily Vestel Beyaz Esya Sanayi Ve Ticaret A.S. (Vestel Beyaz), from exceeding 0.75x consolidated EBITDA. As of December 2024, both covenants were breached, with the company's reported net debt to EBITDA reaching 6.8x and net debt at Vestel Beyaz to consolidated EBITDA reaching 1.3x. The company aims to avoid further increases in debt over the next year by reducing its working capital needs and also has the ability to issue some additional debt under permitted debt baskets. However, this may not be sufficient to cover the company's additional financing needs if Vestel fails to substantially reduce its cash outflows over the next 12 months.

Vestel's operating performance has substantially underperformed our expectations in 2024, recording a decline in revenue of 12% and a decline in Moody's adjusted EBITDA of 72% to TRY3.6 billion from TRY12.8 billion a year earlier. As a result of the weak performance and increased indebtedness, debt to EBITDA increased to 17.9x from 3.6x a year earlier while EBIT interest coverage reduced to -0.1x from 0.9x a year earlier. Moody's adjusted EBITDA differs from the company's reported EBITDA of TRY 7.0 billion because it includes gains and losses on foreign exchange related to trading and operating activities, as well as interest income and gains and losses from equity-accounted associates.

The weak performance was driven by lower sales in both Europe and Turkiye, as well as compressed gross margins in the white goods segment. Exports to Europe account for around 49% of Vestel's sales and the company lost competitiveness there due to significant appreciation of the Turkish lira against the euro in real terms, meaning nominal depreciation of the lira remained significantly below still very high domestic inflation. At the same time, Vestel also faced intensifying competition from Chinese competitors in Europe, which could increase further if US-China trade tensions result in Chinese manufacturers diverting more products to Vestel's core European markets.

In Turkiye, sales declined because the company had benefitted from an increase in sales in the prior year as consumers brought large purchases forward in a highly inflationary environment. Inflation eased in 2024, but still remained high at around 40% on average. At the same time, the government's continued efforts to reduce inflation led to reduced spending power and lower purchases by consumers.

We expect some improvement in Vestel's operating performance and a reduction in its cash outflow over the next 1-2 years, driven by easing domestic inflation and continued nominal depreciation of the lira, combined with potential opportunities to grow sales to the US as Chinese manufacturers become less competitive there due to higher tariffs. While this should lead to an improvement in debt to EBITDA to around 7x and EBIT interest coverage to 0.5x by the end of 2026, these ratios remain weak. At the same time, we expect the company will remain free cash flow negative for the next 2-3 years at least, which will continue to strain its liquidity.

Vestel's Caa1 CFR continues to reflect (1) the company's good market position for televisions and household appliances in Turkiye and Europe; (2) its strong diversification in terms of customers, geographic reach, products and brands through a business model that combines own brands, licensed brands and original design manufacturing (ODM) for third party brands; (3) its high quality production facilities in Turkiye that provide it with logistical advantages over far Eastern producers to reach the European market and put it in a good position to benefit from near-shoring and supply chain diversification of manufacturing customers; and (4) growing mobility electronics and energy storage business that could benefit from the growth of electric vehicle (EV) usership and renewable energies over the coming years.

The rating also reflects (1) the highly competitive nature of Vestel's ODM business; (2) a structurally declining TV market in Europe, combined with volatile input prices; (3) high leverage and low profitability with Moody's adjusted debt to EBITDA of 17.9x as of 2024, expected to gradually decline to around 7x over the next 18 to 24 months and EBIT margin of -0.7% as of 2024, expected to improve to 3-5% over the next 2-3 years; (4) uncertainty over the effect of US trade tariffs on Vestel's competitiveness in its core European markets, which may face higher competition from Chinese manufacturers going forward, albeit combined with the potential opportunity to expand in the US; (5) free cash flow that has been negative since 2021 and our expectation that it will remain negative for the next 2 to 3 years; (6) execution risk in building up its mobility electronics business; and (7) weak liquidity due to material reliance on short term debt and limitations on incurrence of additional debt under its bond documentation.

NEGATIVE OUTLOOK

The negative outlook reflects Vestel's weak liquidity position and in particular the risk that Vestel may not be able to reduce its negative free cash flow to zero over the next 12 to 18 months and will continue to require increased debt funding. This in turn would further raise liquidity risk due to restrictions under the company's bond documentation on the incurrence of additional indebtedness.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Given the negative outlook, an upgrade of the rating is currently unlikely. We would consider stabilizing the outlook if Vestel significantly improves its liquidity position by, for example, reducing its reliance on short term debt or by obtaining repayment of some or all of its long term receivables from related parties, while improving its free cash flow generation.

Vestel's ratings could be downgraded if the company's liquidity deteriorates further and requires to raise additional debt and is prohibited from doing so under its bond documentation.

The principal methodology used in these ratings was Consumer Durables published in September 2021 and available at https://ratings.moodys.com/rmc-documents/74987. Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

The local market analyst for this rating is Lisa Jaeger, +971 (423) 796-59.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions.

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