Rating Action: Moody's changes outlook on MAHLE's ratings to negative from stable, affirms Ba1 ratings

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Frankfurt am Main, April 26, 2022 -- Moody's Investors Service ("Moody's") has today changed the outlook on the ratings of German automotive parts supplier MAHLE GmbH (MAHLE) to negative from stable. Concurrently, Moody's affirmed MAHLE's Ba1 corporate family rating (CFR), the senior unsecured Ba1 instrument rating, the (P)Ba1 senior unsecured euro medium term note programme rating and a Ba1-PD probability of default rating (PDR).

"The outlook change reflects the slower than expected recovery of global light vehicle sales and increasing uncertainty regarding macroeconomic growth from the second half of 2022 onwards, which results in weak margins and slightly elevated leverage for MAHLE longer than we expected", said Matthias Heck, a Moody's Vice President – Senior Credit Officer and Lead Analyst for MAHLE. "The affirmation considers MAHLE's strong market position as a leading automotive parts supplier, its conservative financial policy that should support gradual deleveraging and its good liquidity profile", added Mr. Heck.

RATINGS RATIONALE

In 2021, MAHLE's revenues increased by 11.9% to €10.9 billion, outperforming global light vehicle sales (+4.7%) by more than 700 basis points. The company's reported EBIT turned positive again, to €169 million, implying however a still slim margin of only 1.5%. On a Moody's adjusted basis, MAHLE's EBITA margin amounted to 2.2%, which is still low compared to the minimum of 4% expected for the Ba1 rating.

At the end of December 2021, MAHLE's debt (Moody's adjusted, including pension provisions) amounted to €3.2 billion, which leads to a debt/EBITDA (Moody's adjusted) of 4.1x. In 2021, MAHLE issued €750 million of senior unsecured bonds to pre-finance a €500 million bond maturity in May 2022. Excluding the pre-financing, MAHLE's debt / EBITDA was at 3.5x, still above the maximum of 3.0x, which Moody's expects for the Ba1.

The automotive sector environment remains challenging, and the recovery of global light vehicle sales from the 2020 trough is more protracted than Moody's had initially expected. On April 04, 2022, Moody's revised its growth expectation for global light vehicle sales in 2022 to 3.3%, from 6.2%. This includes a cut for the EMEA region to 0.5%, from 8.5%, reflecting disruption of supply chains due to Russia's invasion of the Ukraine. In this environment, Moody's expects a slight improvement of MAHLE's margins and leverage in 2022, and it will take at least until 2023 to achieve metrics commensurate with the Ba1.

The negative outlook reflects the slow recovery of global light vehicle sales after the trough in 2020, which will leave MAHLE's margins and leverage weakly positioned for the Ba1 in 2022 at least. The negative outlook also reflects challenges for MAHLE to recover margins into a range of 4%-6% (Moody's adjusted EBITA) and reduce debt/EBITDA (Moody's adjusted) to a maximum of 3x by 2023, which is required for the Ba1.

The Ba1 CFR reflects as positives the company's (1) size & scale as one of the world's 25 largest tier 1 automotive parts suppliers, with annual revenues of around €12 billion during the years 2016-19 and a well-diversified Original Equipment Manufacturer (OEM) customer base, (2) top 3 market position in its main product categories of engine systems and coolings, filtration and engine peripherals and thermal management, (3) positive strategic alignment with a dual strategy to address the disruptive automotive industry trend of electrification by using cash flow generated in the internal combustion engines (ICE) business to further broaden and grow its exposure to electric vehicle platforms and products that are not dependent on the powertrain (4) conservative financial policy, as reflected in a history of relatively low financial leverage and modest shareholder distributions, and (5) good liquidity profile.

The rating reflects as negatives the company's (1) exposure to the cyclical nature of automotive production, which has passed its peak in 2018 and is expected to return to previous peak levels only at around mid-decade, (2) relatively low margins, given the highly competitive sector environment, and weak free cash flow generation over the last few years, (3) relatively low exposure to automotive aftermarket business, which is less cyclical and more profitable, (4) high investment needs into R&D and capex to make the product portfolio more independent from ICEs, and (5) challenges related to carbon transition, given the high dependency on...
products for internal combustion engines, at a time where automakers have accelerated their electrification targets.

LIQUIDITY

Moody's considers MAHLE's liquidity position to be good. The company's main sources of liquidity include (1) cash on the balance sheet of €1.1 billion (as of December 2021, excluding restricted cash) and (2) Moody's estimate of annual funds from operations of around €400 million. The company also has a €1.8 billion revolving credit facility (RCF) maturing in 2024 (€0.3 billion) and 2025 (€1.5 billion), which is undrawn. With this, MAHLE's liquidity sources over the next 12 months amount to approximately €3.3 billion under the stressed assumption of no access to capital markets.

These liquidity sources comfortably exceed liquidity uses of around €1.5 billion, mainly comprising of capital spending, which Moody's expects at around €600 million, and a €634 million short-term debt maturities, including €500 million medium term notes maturing in May 2022. Uses of liquidity further include Moody's working cash assumption of €300 million.

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

A downgrade of the ratings could arise for MAHLE if debt/EBITDA (Moody's adjusted) failed to improve to below 3x, EBITA margins remained below 4% (Moody's adjusted), FCF sustained negative, or liquidity weakened.

Moody's would consider an upgrade of the ratings should MAHLE achieve sustainably Debt/EBITDA (Moody's adjusted) below 2.0x, EBITA margins (Moody's adjusted) above 7%, and positive free cash flow (FCF).

LIST OF AFFECTED RATINGS:

..Issuer: MAHLE GmbH

Affirmations:

.... LT Corporate Family Rating, Affirmed Ba1

.... Probability of Default Rating, Affirmed Ba1-PD

....Senior Unsecured Medium-Term Note Program, Affirmed (P)Ba1

....Senior Unsecured Regular Bond/Debenture, Affirmed Ba1

Outlook Actions:

....Outlook, Changed To Negative From Stable

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Automotive Suppliers published in May 2021 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1276105.

Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

COMPANY PROFILE

MAHLE GmbH, headquartered in Stuttgart, Germany, is one of the top 25 global automotive parts suppliers. MAHLE's three main business segments are Thermal management (37% of 2021 sales), Engine Systems and Components (24%) and Filtration and Engine Peripherals (18%). In 2021, MAHLE generated revenues of around €10.9 billion. MAHLE, which employed around 71,000 employees and produced in around 160 locations worldwide in 2021, is owned by the MAHLE Foundation.

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 at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.
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