EULER HERMES Rating

Issuer rating

SAF-HOLLAND SE		20 April 2020	BBB
		Issuer rating	
		Outlook	Negative
Industry	Motor vehicle supply industry / supplier for the commercial vehicle industry, especially components for trucks and trailers	Revenue in 2019	€ 1,284 mn
		Employees in 2019	4,218

BUSINESS RISK: slightly increased
FINANCIAL RISK: low / moderate
→ ANCHOR RATING: BBB → Modification 1: Operational risks → STANDALONE RATING: BBB → Modification 2: External influences → ISSUER RATING: BBB

BUSINESS RISK	slightly increased

- Leading market position with oligopolistic competitive structures
- Strategic advantage from global service network
- Fierce competition and increased sector volatility due to cyclical dependencies
- Moderate diversification

OPERATIONAL RISKS	± 0

- Operational risks are generally managed in a manner commensurate with the rating

FINANCIAL RISK	low / moderate

- Satisfactory earnings power, capital structure and deleveraging potential
- Good interest coverage ratios
- Solid financial flexibility
- Stable results and cash flows from growing spare parts business

EXTERNAL INFLUENCES	± 0

- No external influences of relevance for the rating

Financial ratios *	2014 actual	2015 actual	2016 actual	2017 actual	2018 actual	2019 actual
EBITDA margin (%)	8.6	9.9	10.1	9.5	8.2	8.9
ROCE (%)	18.4	23.1	22.3	22.4	15.5	12.6
Equity-to-total assets ratio (%)	37.0	41.1	40.5	27.3	29.9	28.5
Leverage (%)	41.0	33.9	31.5	32.6	46.3	53.0
Total liabilities / EBITDA	4.1	3.3	3.5	6.2	5.9	5.6
Net debt / EBITDA	1.7	1.2	1.1	1.1	2.2	2.5
EBIT interest coverage	6.6	9.3	6.7	6.4	8.3	9.4
EBITDA interest coverage	8.6	11.7	8.5	8.3	11.5	15.8

Rating rationale

Euler Hermes Rating reaffirms its BBB rating for SAF-HOLLAND SE. We expect the rating to deteriorate over the next twelve months. Financial ratios deteriorated in the 2019 financial year due to the progressive weakening of economic conditions within the sector in individual markets (particularly EMEA, India), the trade war between China and the US and extensive exceptional factors (especially reorganisation expenses). In the current financial year, the direct and indirect consequences of the COVID-19 pandemic are generating additional pressure.

Slightly elevated business risk from dependence on cyclical commercial vehicle sector with moderate diversification

It is our assessment that SAF-HOLLAND SE (SAF-HOLLAND) still has a slightly increased business risk. Rating strengths include sustainable growth prospects from the increasing global transport volumes and the Group's leading market positions in core markets and segments in Europe and North America. Other strengths, in our view, are its global production and service network, ongoing product innovation and the less cyclical high-margin spare parts business that is experiencing secular growth. As a result, we rate the strategic risk as moderate overall. However, in our view, fierce competition and high dependency on the cyclical commercial vehicle sector pose increased market risks that the COVID-19 pandemic is intensifying. SAF-HOLLAND compensates for some of these pressures through a global positioning with different industry and demand cycles, increasingly efficient global production and procurement processes and a comprehensive cost-cutting program. In the dominant trailer segment, SAF-HOLLAND has a broad customer base that it mainly serves with relatively small lot sizes. That means its overall production supply chain is less complex and fragile than those operated by conventional automotive parts suppliers who rely heavily on serial manufacturing. SAF-HOLLAND is also classified as systemically important for several product groups and so is more likely to be given priority in starting up production capacity and maintaining supply chains.

Low to moderate financial risk based on stable earnings power and good financial flexibility

The Group's financial risk has recently increased from a low level to a low to moderate level overall, in our opinion. Rating weaknesses included one-time factors, the impact of the US-China trade war and the momentum of the softening business cycle within the sector in individual markets (Europe, China, India). We expect the COVID-19 pandemic to accelerate the weakening of the business cycle in the sector over the short to medium term. In an environment characterised by lockdowns, we expect earnings power to decline from the middle to low end of the 'satisfactory' range. We currently expect the pandemic to produce U-shaped cyclical effects in core markets. Earnings power may deteriorate even more over the short term, depending on the type of recession phase and ongoing disruptions in production processes. As a result, we expect the planned deleveraging to be delayed and the capital structure and repayment periods to weaken from good to satisfactory over the medium term. One strength, in our view, is that SAF-HOLLAND mounted a rigorous, comprehensive response to its declining earnings power back in 2019, drove operational excellence and conducted an exhaustive global cost-cutting program. SAF-HOLLAND should benefit from its more efficient structures and earnings power as recovery tendencies pick up. In addition, the company generally has a high internal financing potential, solid financing and a less cyclical high-margin spare parts business that is experiencing secular growth.

No modifications to the anchor rating

In our view, SAF-HOLLAND has adequate structures, processes and systems in place in order to achieve its strategic goals. It is our opinion that operational risks are handled appropriately and are consistent with the anchor rating. There are no external factors of relevance to the rating. No modifications were made to the anchor rating.

Upgrade / downgrade factors

Factors that could lead to an upgrade

- Sustained improvement in the diversification profile and integration of business models that run counter to the business cycle in the sector (e.g. agricultural machinery) or are less dependent on the business cycle (e.g. data-based) and generate a significant portion of income
- Sustained improvement in operational performance due to actions such as the envisaged implementation of an operational excellence system
- Euler Hermes Rating adjusted EBITDA margin sustainably above 11 per cent
- Sustained improvement in deleveraging potential (Euler Hermes Rating adjusted net debt / EBITDA less than 1.5)
- Sustained increase in the cash flow basis and positive free cash flow performance

Factors that could lead to a downgrade

- Major, prolonged recession phase associated with significant declines in orders and production interruptions as a result of the COVID-19 pandemic
- Significant decline in market share in core markets
- Sustained deterioration in operational performance due to factors such as a significant decline in the spare parts business
- Euler Hermes Rating adjusted EBITDA margin sustainably below 9 per cent
- Sustained deterioration in deleveraging potential (Euler Hermes Rating adjusted net debt / EBITDA greater than 2.0)
- Decline in cash flow generation and negative free cash flow performance

Rating history

	24/09/2012	04/09/2013 – 19/04/2020	20/04/2020
Rating	BBB-	BBB	BBB
Outlook	Stable	Stable	Negative

Company

Manufacturer of systems and components for tractors and trailers

SAF-HOLLAND SE specialises in the development, production and sale of high-quality systems and components for tractors (trucks/ revenue share: 15 per cent), trailers (semi-trailers, full trailers/ revenue share: 60.3 per cent) and buses (OEM business). Its operations also include the associated service and spare parts business (revenue share: 25 per cent). In the 2019 financial year, the company generated € 1,284.2 mn in Group revenues in *EMEA* (revenue share: 48.8 per cent), the *Americas* (revenue share: 41.6 per cent) and *APAC/China* (revenue share: 9.6 per cent) with an average headcount of 4,218. In addition to roughly 10,000 spare parts and service stations worldwide, SAF-HOLLAND has 26 production sites in countries such as the United States, Canada, Germany, Australia, China and India.

Leading market position in EMEA and India for axle and suspension systems

In the *EMEA and India* regions, SAF-HOLLAND maintains a leading position in the market for axle and suspension systems, landing gears and kingpins. The company supplies major customers such as Krone and Kögel as well as a large number of smaller regional suppliers and manufacturers of specialty vehicles. The company's main global competitors for axle and suspension systems are BPW (Germany), FUWA (China) and Hendrickson (US).

Leading market position for fifth wheel couplings in North America

SAF-HOLLAND holds a leading position in the market for fifth wheel couplings and suspension systems in *North America*. The acquisition of coupling specialist V.ORLANDI (Italy) strengthened the company's number two position – behind Jost – in this segment in EMEA. The company's biggest customers in this segment include Paccar, Daimler and Navistar. Aside from Jost, the company's biggest global competitors are Fontaine (US) and FUWA (China).

Growing market share in China

In *China*, SAF-HOLLAND ranks second to BPW in market position in the premium segment. It aims to progressively increase its market share over the medium term by commissioning its new factory in Yangzhou, China. Its product portfolio currently consists of landing gears and axle and suspension systems for trailers and buses.

Full-coverage service and spare parts business

SAF-HOLLAND keeps customers reliably supplied with spare parts in the supra-regional *spare parts business*. The customer structure in this market is fragmented and ranges from end customers (fleet operators) to spare parts dealers and repair shops. In the core markets of Europe and North America, its aftermarket network covers a wide area and is denser than that of the competition.

The shares of SAF-HOLLAND SE have been listed since 2007 with 100 per cent in free float according to the definition of Deutsche Börse AG. The members of the Group Management Board and Board of Directors collectively held 0.14 per cent of the shares as of 31 December 2019. The current members of the Group Management Board are: Alexander Geis (Chief Executive Officer), Dr Matthias Heiden (Chief Financial Officer) and Dr Andre Philipp (Chief Operating Officer).

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Execution

Analysts

- Joerg F. Walbaum, Senior Analyst (Lead Analyst)
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Rating committee

- Kai Gerdes, Director
- Matthias Peetz, Senior Analyst

Rating, Cooperation, Principle sources of information

- This credit rating has been issued in accordance with the CRA Regulation

  [x] Solicited rating
  [ ] Unsolicited rating
    [ ] No participation of the rated entity or related third party
    [x] Involvement of the valued entity or related third parties
      [x] With access to internal documents
      [x] With participation of the rated entity or related third party

- Prior to its publication the rating was disclosed to the rated entity. During this period, the rated entity had the opportunity to review the rating and to verify the underlying assumptions. Following this review, the rating was not amended

- Principle sources of information:

  - Consolidated financial statements (audit reports) 2017, 2018, 2019
  - Excerpts from internal reporting (e.g. business development 2019, financing overview, etc.)
  - Market analyses
  - Information on strategy and company planning
  - Documents on the corporate structure
  - Interviews with the management

Rating methodology and Definitions

- Euler Hermes Rating GmbH Issuer Rating Methodology of May 2016 (https://www.ehrg.de/seiten/Methodik_Emittentenrating_20171114.pdf)
- Basic Principles for Assigning Credit Ratings and Other Services (https://www.ehrg.de/seiten/Principles_2020.pdf)
- Guidance Regarding the Consideration of ESG Factors in Euler Hermes Rating Credit Ratings (https://www.ehrg.de/seiten/ESG_2020.pdf)

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Rating categories*

Category	Explanation
AAA	In the opinion of EHRG, AAA rated entities demonstrate an excellent credit quality and the lowest default risk.
AA	In the opinion of EHRG, AA rated entities demonstrate a very high credit quality with a very low default risk.
A	In the opinion of EHRG, A rated entities demonstrate a high credit quality with a low default risk.
BBB	In the opinion of EHRG, BBB rated entities demonstrate a medium credit quality with a moderate default risk.
BB	In the opinion of EHRG, BB rated entities demonstrate a medium to low credit quality with a slightly increased default risk.
B	In the opinion of EHRG, B rated entities demonstrate a low credit quality with an increased default risk.
CCC	In the opinion of EHRG, CCC rated entities demonstrate a very low credit quality with a high default risk.
CC	In the opinion of EHRG, CC rated entities demonstrate a very low credit quality, an event of default is very likely.
C	In the opinion of EHRG, C rated entities demonstrate a very low credit quality, an event of default is imminent.
D / SD	D rated entities have defaulted, as defined by the rating agency. The rated entity is assigned an SD rating (Selective Default) if it has only defaulted on certain debt obligations.
PLUS (+) MINUS (–)	Rating categories from AA to CCC are modified by a PLUS (+) or MINUS (-), where required, in order to show their relative position within the rating category.

* For more explanations and definitions please refer to: Basic principles for Assigning Credit Ratings and Other Services (https://www.ehrg.de/seiten/Principles_2020.pdf)

Definition of financial ratios

Earnings power

EBITDA margin

EBITDA margin
Numerator
EBITDA
Denominator
Total revenues

Returns

ROCE
Numerator
Adjusted operating result (= EBIT)
Denominator
Net debt + economic equity (= capital employed)

Return on total assets
Numerator
Adjusted operating and financial result + interest expense
Denominator
Adjusted total assets

Cashflow-Return on Investment

Cash flow return on investment (Cash flow ROI)
Numerator
EBITDA
Denominator
Adjusted total assets

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Capital structure

Indebtedness

Equity-to-total assets ratio
Numerator
Adjusted equity (= economic capital)
Denominator
Adjusted total assets

Leverage
Numerator
Net debt
Denominator
Net debt + economic equity (= capital employed)

Net debt

Net debt
Bonds
+ Liabilities to banks
+ Bill liabilities
+ Other interest-bearing liabilities
+ Operating lease liabilities
+ Adjustments for ABS/factoring transactions
- Cash and cash equivalents

Deleveraging potential

Total liabilities / EBITDA
Numerator
Total assets - economic capital (= total liabilities)
Denominator
EBITDA

Net debt / EBITDA
Numerator
Net debt
Denominator
EBITDA

Interest coverage

EBIT interest coverage
Numerator
Adjusted operating result (= EBIT)
Denominator
Interest expenses

EBITDA interest coverage
Numerator
EBITDA
Denominator
Interest expenses

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Disclaimer

SAF-HOLLAND S.A. engaged Euler Hermes Rating GmbH to conduct a rating on 05/02/2014. The company was visited on 06/03/2019.

The Rating Committee of Euler Hermes Rating GmbH reviewed the rating process, issued the rating notation and approved the rating report in its current form on 03/04/2019. This rating report was given to the client on 12/05/2020, thereby concluding the rating process.

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Hamburg, 12/05/2020