SAF-HOLLAND
Germany, Automotive Suppliers

SCOPE BBB- STABLE

Key metrics

			Scope estimates	
Scope credit ratios	**2021**	**2022**	**2023E**	**2024E**
Scope-adjusted EBITDA/interest cover	17.9x	16.8x	5.5x	7.1x
Scope-adjusted debt/EBITDA	2.1x	3.9x	2.9x	2.3x
Scope-adjusted funds from operations/debt	38%	25%	23%	30%
Scope-adjusted free operating cash flow/debt	-1%	17%	11%	10%

Rating rationale

The rating reflects the BBB- business risk profile and BBB- financial risk profile assessments of SAF-HOLLAND including its recent acquisition of the Swedish braking system specialist Haldex AB (Haldex).

The main support for SAF-HOLLAND's competitive position is the group's global/regional leadership in oligopolistic markets protected by high entry barriers. Product diversification will be enhanced by the merger and supports the group's positioning as a one-stop solution provider offering an enlarged portfolio of axles & suspensions, brake & chassis control and telematics. The low customer concentration and higher share of high-margin aftermarket business strongly support the business risk profile. Key restraining factors are the cyclicality of the global commercial vehicle markets and the modest operating profitability.

The financial risk profile is supported by expected leverage between 2-3x and interest coverage above 5x, while being constrained by a relatively weak cash flow cover as measured by Scope-adjusted free operating cash flow/debt ratio.

Outlook and rating-change drivers

The Stable Outlook reflects our expectation that the combined group will be able to withstand moderate fluctuations in the cyclical global commercial vehicle market thanks to a higher share of aftermarket business, further strengthened by cross selling, cost savings and pricing opportunities brought in by the merger with Haldex. Furthermore, the Outlook reflects our anticipation of Scope-adjusted debt/EBITDA improving thanks to a gradual deleveraging.

A positive rating action could be warranted if SAF-HOLLAND managed to reduce leverage as measured by Scope-adjusted debt/EBITDA towards 2x while improving free cash flow generation after a successful merger with Haldex. This could be achieved thanks to higher profitability through Haldex integration combined with enhanced free cash flow generation through capex discipline and net working capital optimisation

We may consider a negative rating action if leverage, as measured by Scope-adjusted debt/EBITDA, remains above 3x on a sustained basis. A negative rating action could also be triggered by a sustainable deterioration in free cash flow generation or if profitability deteriorates due to much weaker business conditions, unforeseen revenue decline or unexpected execution risks related to the merger with Haldex.

Rating & Outlook

Issuer BBB-/Stable

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Related Methodologies

General Corporate Rating Methodology; July 2022

Rating Methodology: European Automotive Suppliers; February 2023

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Bloomberg: RESP SCOP

Rating and rating-change drivers

Positive rating drivers	Negative rating drivers
• Leading market positions in oligopolistic markets for chassis-related systems and components • Resilient business model thanks to a significant share of less volatile, highly profitable aftermarket business (~34% of group sales including Haldex) • Low customer concentration: top 3 customers account for less than 10% of combined group's revenues • Growth and cost synergy potential with Haldex • Management's commitment to reduce reported net debt to EBITDA to below 2x by YE 2024	• Strong exposure to highly cyclical commercial vehicle industry • Weak presence in large Asian markets (e.g. China) • Execution risks associated with the Haldex integration • Volatile and relatively weak cash flow cover

Positive rating-change drivers	Negative rating-change drivers
• Scope-adjusted debt/EBITDA moving towards 2x and improvement in cash flow generation after successful merger	• Scope-adjusted debt/EBITDA above 3x on a sustained basis • Deterioration in cash flow or deterioration in profitability

Corporate profile

Headquartered in Bessenbach (Germany), SAF-HOLLAND SE is the parent company of the SAF-HOLLAND group. SAF-HOLLAND SE holds 100% of SAF-HOLLAND GmbH, which holds the interests in all operating entities (regional subsidiaries and majority shareholdings). SAF-HOLLAND stems from the 2006 merger of two regional champions, the German Otto Sauer Achsenfabrik GmbH and the North American Holland Group Inc. As such, the group has a longstanding history dating back to 1881 and 1910, respectively. It has built up its global presence and expanded its product portfolio through an active acquisition strategy, which was accelerated between 2016 and 2019.

SAF-HOLLAND is one of the leading suppliers to the global commercial vehicles industry. The group develops, manufactures and supplies chassis-related assemblies and components for trailers (semi-trailers, full trailers), trucks and buses. Its product range consists of axle and suspension systems for trailers, fifth wheels for trucks, coupling systems, kingpins, and landing gears. These products are marketed under the SAF, Holland, Neway, KLL, V. Orlandi, TrailerMaster and York brands. The group serves original equipment manufacturers (OEMs) of trailers and trucks, which represent 73% of sales. The remaining 27% corresponds to the aftermarket business, comprising sales of spare parts to manufacturers' service networks (OES), wholesalers, end-customers and service centres through an extensive proprietary global service and distribution network (around 12,000 spare parts and service stations in more than 80 countries).

SAF-HOLLAND primarily operates in Europe-Middle East-Africa (52% of 2022 sales) but has a solid presence in the Americas (38%) and to a less extent in Asia Pacific (10%). Its manufacturing footprint includes 22 production and assembly facilities across the globe. In 2022, SAF-HOLLAND generated revenues of EUR 1.57bn and company-adjusted EBIT of EUR 124.6m (adjusted margin of 8%).

On 8 June 2022, SAF-HOLLAND announced a voluntary cash tender offer for the Swedish company Haldex AB (Haldex) to create a new global champion for chassis-related commercial vehicle components. The acquisition was completed on 28 February 2023 after the squeeze-out of outstanding minority shares. After full clearance from all relevant anti-trust authorities (USA, Germany, Poland), the merger became effective as of 21 February 2023, which marks the first consolidation date of Haldex.

The combined group generated pro-forma revenues of around EUR 2bn in 2022.

Financial overview

				Scope estimates		
Scope credit ratios	**2020**	**2021**	**2022**	**2023E**	**2024E**	**2025E**
Scope-adjusted EBITDA/interest cover	14.2x	17.9x	16.8x	5.5x	7.1x	7.1x
Scope-adjusted debt/EBITDA	3.2x	2.1x	3.9x	2.9x	2.3x	2.1x
Scope-adjusted funds from operations/debt	33%	38%	25%	23%	30%	33%
Scope-adjusted free operating cash flow/debt	39%	-1%	17%	11%	10%	14%
Scope-adjusted EBITDA in EUR m						
EBITDA	81	123	150	185	210	229
Disposal losses (gains) on fixed assets	0	0	-1	0	0	0
less: capitalised development costs	**-3**	-3	**-5**	-8	-8	-9
Scope-adjusted EBITDA	**79**	**120**	**144**	**178**	**202**	**221**
Funds from operations in EUR m						
Scope-adjusted EBITDA	79	120	144	178	202	221
less: (net) cash interest paid	-6	-7	-9	-33	-29	-31
less: cash tax paid per cash flow statement	-7	-20	-27	-24	-32	-36
add: dividends from associates	2	1	4	0	0	0
Change in provisions and other	14	1	26	0	0	0
Funds from operations (FFO)	**82**	**95**	**138**	**121**	**141**	**153**
Free operating cash flow in EUR m						
Operating cash flow	130	30	140	119	114	138
less: capital expenditure (net)	-24	-24	-33	-55	-60	-63
less: lease amortisation	-9	-9	-9	-9	-9	-9
Free operating cash flow (FOCF)	**97**	**-3**	**98**	**55**	**45**	**65**
Net cash interest paid in EUR m						
Net cash interest per cash flow statement	-5	-6	-8	-32	-28	-30
add: interest expenses, pensions	-1	0	0	-1	-1	-1
Net cash interest paid	**-6**	**-7**	**-9**	**-33**	**-29**	**-31**
Scope-adjusted debt in EUR m						
Reported gross financial debt	368	363	754	585	538	476
less: cash and cash equivalents	-171	-165	-243	-119	-125	-65
add: non-accessible cash	0	0	0	0	0	0
add: pension adjustment	12	7	4	14	14	14
add: factoring	40	44	44	40	40	40
Scope-adjusted debt (SaD)	**249**	**249**	**559**	**520**	**467**	**465**

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Environmental, social and governance (ESG) profile[1]

Environment		Social		Governance	
Resource management (e.g. raw materials consumption, carbon emissions, fuel efficiency)		Labour management		Management and supervision (supervisory boards and key person risk)	
Efficiencies (e.g. in production)		Health and safety (e.g. staff and customers)		Clarity and transparency (clarity, quality and timeliness of financial disclosures, ability to communicate)	
Product innovation (e.g. transition costs, substitution of products and services, green buildings, clean technology, renewables)		Clients and supply chain (geographical/product diversification)		Corporate structure (complexity)	
Physical risks (e.g. business/asset vulnerability, diversification)		Regulatory and reputational risks		Stakeholder management (shareholder payouts and respect for creditor interests)	

Legend
Green leaf (ESG factor: credit positive)
Red leaf (ESG factor: credit negative)
Grey leaf (ESG factor: credit neutral)

ESG considerations

Material ESG factors relevant for the automotive supplier industry include the need to reduce the environmental impact of products and production, improve resource management (optimised use of energy and natural resources), and enhance supply chain oversight in terms of social standards and responsible sourcing. We assess these factors as credit-neutral as far as SAF-HOLLAND is concerned.

SAF-HOLLAND has set targets for reducing energy consumption in the company's global manufacturing footprint. The company's total energy consumption was reduced by 21% in 2022. Furthermore, the company plans a global roll-out of energy management software across major SAF-HOLLAND and Haldex facilities in 2023 and 2024.

Regarding CO_2 emissions, the EMEA region has reduced its emissions by over 14% in 2022 compared to 2021. The region targets a 10% reduction in CO_2 emissions related to production facilities between 2023 and 2026.

In 2021, Haldex committed through the Science Based Targets Initiative (SBTi) to set emissions targets in line with climate science. The group's stated ambition was to be carbon neutral for Scope 1 and 2 by 2025 thanks to various initiatives aimed at reducing energy consumption, using renewable sources of electricity and investing in offsetting projects.

[1] These evaluations are not mutually exclusive or exhaustive as ESG factors may overlap and evolve over time. We only consider ESG factors that are credit-relevant, i.e. those that have a discernible, material impact on the rated entity's cash flow and, by extension, its credit quality.

Business risk profile: BBB-

Industry risk profile: BB

SAF-HOLLAND is a supplier of chassis-related systems and components to the global commercial vehicle industry. The recently acquired Haldex AB (Haldex) is a manufacturer of braking systems supplied to the global truck and trailer industry. We therefore classify the combined group as an automotive supplier, with an industry risk profile rated BB. As detailed in our European Automotive Suppliers Rating Methodology, this industry is characterised by high cyclicality, high entry barriers and medium substitution risk.

The BB industry risk profile is mitigated by the group's high share of highly profitable aftermarket business, which provides a strong protection against the industry's cyclicality, thus supporting the BBB- business risk profile assessment.

Assessment includes the recently acquired Haldex

Our assessment is based on the whole SAF-HOLLAND group including its recent acquisition of Haldex. The takeover received its final merger control clearance on 21 February 2023 and was finalised with the completion of the squeeze-out of all remaining outstanding Haldex shares on 28 February 2023.

This acquisition is a transformational move for SAF-HOLLAND. This combination makes a lot of sense for both companies which are complementary in terms of regional presence and product portfolio while addressing similar Original Equipment (OE) customers (large manufacturers of trucks, buses and trailers) and end-customers (fleet operators). We deem integration risks to be low to medium based on complementary product portfolios and SAF-HOLLAND's proven ability to integrate acquired companies.

Market leading positions

The main support for SAF-HOLLAND's competitive position is the company's global/regional leadership in oligopolistic markets protected by high entry barriers with Haldex also having been a market leader in several product categories standalone. The company hold top three market positions in North America and EMEA for key products and systems. As Haldex and old-SAF Holland address the same industry and end-markets with a complementary product portfolio, the combined group is well positioned to meet the future needs of the global commercial vehicle sector. Furthermore, the combined group owns one of the largest spare parts and service network in Europe and North America, which constitutes a significant barrier to market entry.

Diversification to be enhanced with Haldex's integration

SAF-HOLLAND's diversification was historically moderate but will improve thanks to the integration of Haldex. The product range will be enlarged by adding foundation brakes, air controls and EBS, thus covering a wider range of chassis-related components. This will help bundle the offering and position the combined group as a one-stop solution provider offering an enlarged portfolio of axles & suspensions, brake & chassis controls and telematics. The group will thus be well equipped to provide additional solutions such as predictive maintenance or 'smart functions' such as temperature measurement in refrigerated trucks or burglary protection.

Low customer concentration

Unlike most automotive suppliers, SAF-HOLLAND has a relatively low customer concentration, with the top ten customers representing less than 25% of combined revenues. The company has a broad customer base in its dominant trailer segment (over 80% of OE sales), a diversified end-customer base (fleet operators) and much greater customer granularity in the service and spare parts business.

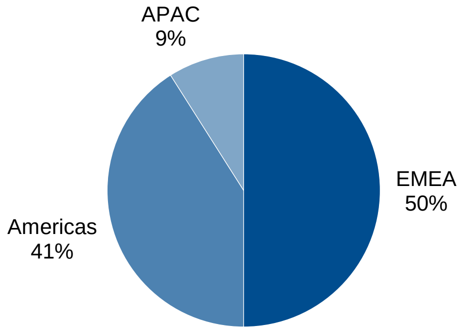
High share of high-margin aftermarket business

Its large exposure to the highly profitable and resilient aftermarket business is a strong support to the business risk profile. As Haldex generated over 50% of its sales in the aftermarket (versus 27% for SAF-HOLLAND), the combined group will derive around 34% of revenues from this more stable business, which should provide a solid protection against the inherent cyclicality of the global commercial vehicle industry.

Solid presence in the Americas and Europe, low exposure to APAC

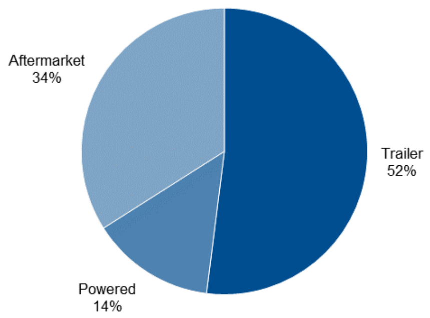
SAF-HOLLAND standalone had a global geographical outreach, which will be further enhanced by Haldex's international set-up. The combined group generates around 50% of its revenues in Europe-Middle East-Africa (EMEA), 40% in the Americas (North and South America), and 10% in Asia-Pacific (APAC). However, the group remains underrepresented in large Asian markets such as China.

Figure 1: Pro forma revenues by geography - 2022



Sources: SAF-HOLLAND, Scope

Figure 2: Pro forma revenues by end-market – 2022



Sources SAF-HOLLAND, Scope

Key restraining factors for the business risk assessment are the cyclicality risks attached to the fluctuations in global commercial vehicle markets (trucks/trailers/buses) and the relatively modest operating profitability.

Moderate profitability

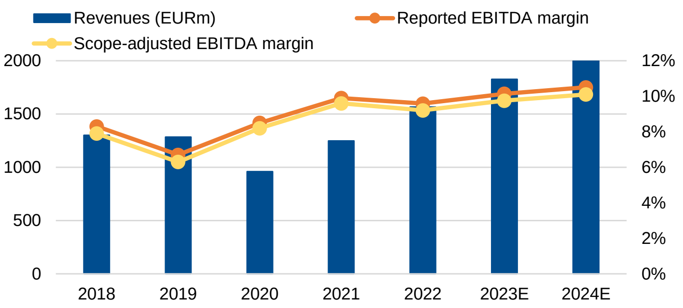
Profitability, assessed with our automotive suppliers rating grid is moderate, with combined Scope-adjusted EBITDA margins expected around 10% in the coming years. Over 2018-2021, the Scope-adjusted EBITDA margin has ranged between 6% and 9.6%. SAF-HOLLAND managed to navigate the volatile environment triggered by the Covid-19 pandemic and the subsequent disruptions.

Solid 2022 results

In 2022, despite persistent supply chain bottlenecks and macroeconomic challenges, SAF-HOLLAND exceeded its revenue forecast, with sales up 25.6% (+17.9% organically), driven by a strong rebound in demand for commercial vehicle components, notably in North America (sales up 47%) and APAC (sales up 45%). The adjusted EBIT margin, as defined by the company, rose by 50 bp to 8%, reflecting favourable product mix, efficiency gains and price increases which offset cost inflation (steel, freight rates, energy). With EBIT margins up 3.5pp to 9.5%, North America was a key driver, together with APAC (10.1% up 8.4 pp) which bounced back thanks to lower losses in China and a strong business development in India and Australia. This rebound more than offset the weaker performance in EMEA (adjusted margin down 2.7 pp to 6.5%). All in all, SAF-HOLLAND achieved, one year in advance, the financial objective set in the Strategy 2025 plan presented in November 2020, which was to raise the adjusted EBIT margin from 6.1% in 2019 to around 8% by 2023.

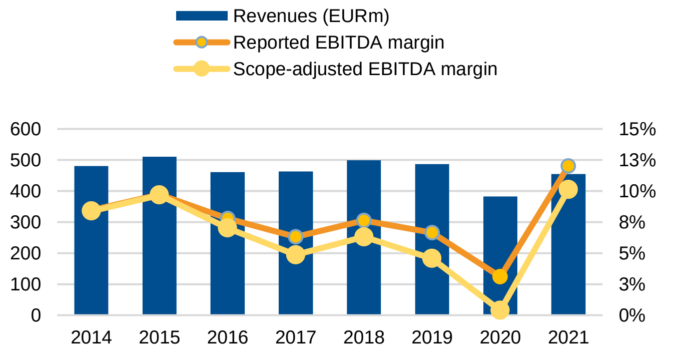
Haldex had to cope with numerous internal issues and external constraints over 2018-2021. The company took aggressive measures to adapt its cost structure accordingly. This involved transferring some production from high-cost countries to low cost countries (from Western Europe to Hungary, from US to Mexico), adjusting the supply chain and streamlining the cost structure across the board. The multiyear cost savings programme launched in 2019 proved to be effective, as Haldex started to reap the benefits in 2021 and get back on track in 2022, reaching an adjusted EBIT margin at 9.9% in Q3, up 1.6 pp YoY. Haldex's standalone IFRS financial statements for FY 2022 to be released by the end of May 2023 will reflect the application of SAF-HOLLAND's more conservative accounting approach and reporting principles.

Figure 3: SAF-HOLLAND - Scope-adjusted EBITDA margin



Sources: SAF-HOLLAND, Scope estimates. 2023E and 2024E refer to the combined group

Figure 4: Haldex - Scope-adjusted EBITDA margin



Sources: SAF-HOLLAND, Scope

Challenging industry outlook in 2023

In 2023, the macroeconomic and industry outlook remains challenging. While demand for trucks and trailers is expected to decline by around 5% in the group's core markets of the Americas and Europe, aftermarket demand is expected to remain stable overall. The group's order book remains solid and SAF-HOLLAND looks well positioned to gain shares in its key markets. This is also supported by Haldex's new product deliveries (fourth generation of EBS systems) and air disc brakes production ramp-up at two major European trailer manufacturers from Q4 onwards. We have nonetheless adopted a cautious stance regarding the revenue development of the combined group and forecast revenues slightly above EUR 1.8bn for 2023, net of intercompany eliminations. This forecast is at the lower end of the EUR 1.8-1.95 bn guidance corridor released by SAF-HOLLAND on 31 March 2023. We assume that cost inflation will be partially offset by continued price increases, complemented by cost optimisation and quick gains from the integration of Haldex.

Scope-adjusted EBITDA margin expected around 10% in 2023-2025

We forecast Scope-adjusted EBITDA margin at 9.7% in 2023 for the combined group, compared to 9.2% for SAF-HOLLAND alone in 2022. We anticipate a slight margin improvement to 10.1% in 2024 and 10.5% in 2025.

In terms of regional performance, a significant recovery in EMEA, back to double digit adjusted EBIT margins, would strongly support profitability improvement at SAF-HOLLAND standalone. As Haldex's situation in EMEA remains challenging (2.6% adjusted EBIT margin over 9M 2022), reducing the profitability gap between the two companies will also help move the combined EMEA EBIT margins closer to the double digit level in the years ahead.

Financial risk profile: BBB-

We assess the financial risk profile at BBB-, constrained by a relatively weak cash flow cover, as measured by Scope-adjusted free operating cash flow/debt ratio.

In accordance with Scope General Corporate Rating Methodology, we make the following adjustments to credit metrics:

- EBITDA is adjusted by subtracting capitalised development costs;
- Debt is adjusted by adding back factoring and 50% of the pension deficit net of deferred tax assets and deducting unrestricted cash and cash equivalents.

Sharp increase in Scope-adjusted debt due to the funding of the Haldex acquisition

SAF-HOLLAND's gross financial debt comprises several promissory note loans ('schuldschein' with various maturities, fixed and variable interest rates), term loans and lease liabilities. In 2022, Scope-adjusted debt increased by EUR 310m to EUR 559m, reflecting the EUR 300m additional debt raised to finance the acquisition of Haldex.

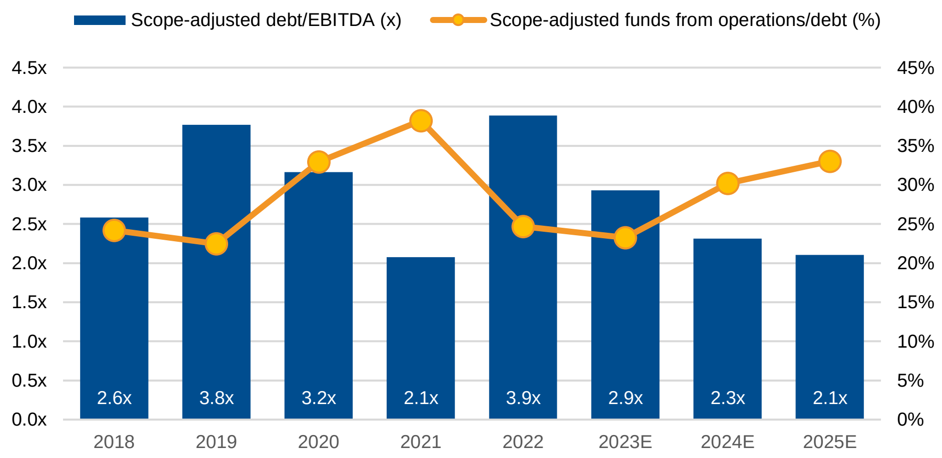
Scope-adjusted debt/EBITDA to improve towards 2x by 2025

Leverage, as measured by Scope-adjusted debt/EBITDA, increased to around 3.9x in 2022 compared to an average 2.9x over 2018-2021. This ratio was significantly inflated as Haldex was not yet consolidated and therefore did not contribute to the group's EBITDA in 2022. Scope-adjusted debt/EBITDA for the combined group is expected to decrease gradually towards 2x by 2025.

Scope-adjusted FFO/debt to improve towards 35% by 2025

Scope-adjusted funds from operations/debt reached 25% in 2022 versus an average 29% over 2018-2021. This metric is expected to move towards 35% by 2025.

Figure 5: Scope-adjusted debt/EBITDA and Scope-adjusted funds from operations/debt



Sources: SAF-HOLLAND, Scope estimates

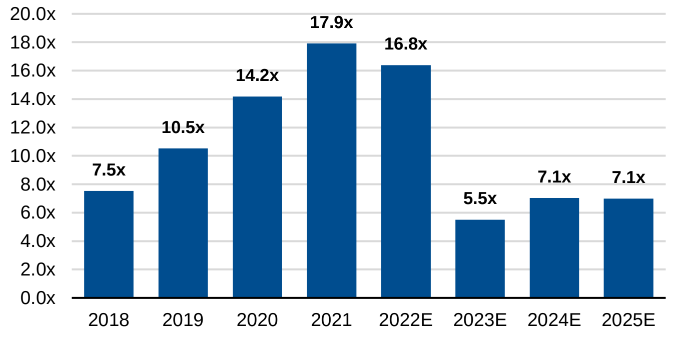
Interest cover: declining but still solid

EBITDA interest cover was historically strong, at around 12.5x over 2018-2021, with a peak at 18x in 2021. Rising interest rates will lead to a deterioration of this debt protection metric in 2023, trending towards 7x in 2025. This reflects more expensive charges on variable rate financial debt (around 75% of total debt) and higher refinancing rates in the years ahead.

Weak cash flow cover

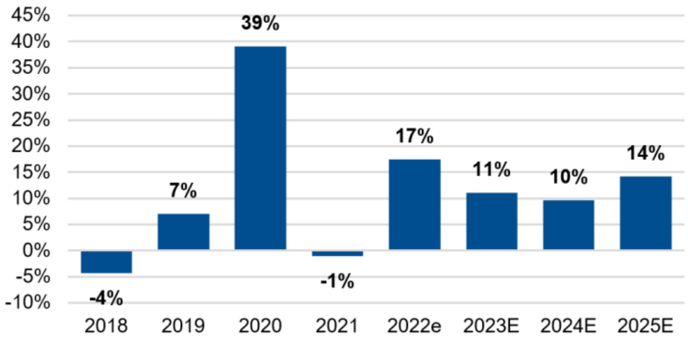
Cash flow cover is a weaker credit metric for SAF-HOLLAND, due to the volatility of free operating cash flow (FOCF) in the past few years. Cash flow cover peaked at 39% in 2020, before falling to minus 1% in 2021 and bouncing back to 17% in 2022, thanks to improved cash flow generation, driven by a noticeable reduction in net working capital ratio. We expect cash flow cover to stay in the 10-15% range over the forecast period. Capex discipline and net working capital management will be the key drivers of FOCF improvement in the coming years. SAF-HOLLAND's asset-light business model (capex to sales ratio around 2%) contrasts with Haldex's higher capex intensity (over 4% of sales), leading to an estimated capex ratio of 3% in 2023-2025. Net working capital management will be a challenge (and a mid-term opportunity) due to the stark difference between the two companies. At the end of September 2022, Haldex posted a net working capital ratio of 24.6% of sales (28.5% excluding sales to SAF-HOLLAND) compared to 15.9% at SAF-HOLLAND. The midterm plan is to reduce this ratio to 15-16% for the combined entity, thanks to the implementation of SAF-HOLLAND's best practices and the deployment of the new ERP across the group.

Figure 6: Scope-adjusted EBITDA/interest cover



Sources: SAF-HOLLAND Scope estimates

Figure 7: Scope-adjusted FOCF/debt



Sources: SAF-HOLLAND, Scope estimates

Adequate liquidity

Liquidity is adequate, supported by available liquidity sources. At year-end 2022, SAF HOLLAND had EUR 244m in cash on hand and a EUR 250m undrawn committed credit line. This new syndicated credit facility negotiated in August 2022 and maturing in 2027 can be extended twice up to 2029 and increased by EUR 100m. In November 2022, SAF-HOLLAND issued a new promissory note loan ('Schuldschein') of EUR 176m, with 3-year and 5-year maturities. This promissory note will, inter alia, refinance all 2023 maturities (EUR 161m) from the EUR 250m promissory notes issued in March 2020. The next large maturities fall due in 2025 and include around half of the EUR 300m term loans taken in 2022 to finance the acquisition of Haldex.

SAF-HOLLAND usually prepares the refinancing of upcoming maturities well in advance via the most appropriate instruments, typically promissory note loans. The debt maturity profile is manageable in our view. For the future, SAF HOLLAND intends to optimise its financing structure by using more actively its cash balances to reduce debt, while keeping the RCF as a safety buffer.

Balance in EURm	2023E	2024E	2025E
Unrestricted cash (t-1)	243	119	125
Open committed credit lines (t-1)	250	250	250
Free operating cash flow	55	45	65
Short-term debt (t-1)	102	245	314
Coverage	**> 200%**	**168%**	**140%**

Supplementary rating drivers: +/- 0 notches

Supplementary rating drivers are neutral for the issuer rating.

We view SAF-HOLLAND's capital allocation policy as credit-neutral, with a moderate risk appetite. The company's dividend policy is shareholder-friendly, with a 40%-50% payout ratio range, at the upper end of long-term target corridors set by most automotive players (25%-40%). However, this policy has been relatively stable over time and proved to be flexible as evidenced by the board's decision to waive dividend payments during the Covid-19 crisis. Share buybacks are not part of the group's shareholder remuneration policy for now. Management is committed to deleveraging and reducing its reported net debt/EBITDA ratio to below 2x by 2024. Lastly, no material acquisition is expected following the Haldex deal.

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