Research Update:

Nexans Outlook Revised To Positive On Successful Restructuring And Improving Credit Metrics; 'BB/B' Ratings Affirmed

February 17, 2021

PRIMARY CREDIT ANALYST

Pierre-Henri Giraud
Paris
+ 33(0)140752566
Pierre-Henri.Giraud
@spglobal.com

SECONDARY CONTACT

Tuomas E Ekholm, CFA
Frankfurt
+ 49 693 399 9123
tuomas.ekholm
@spglobal.com

Rating Action Overview

- French cable manufacturer Nexans S.A.'s credit metrics continue to improve, thanks to revised working capital management and profitability growth due mainly to the ramping down of its successful restructuring.
- Nexans demonstrated a solid credit profile in 2020 with a significant buffer and significantly better ratios than we forecast in our previous review, resulting in a funds from operations (FFO)-to-debt ratio at about 25%-30%, expected at 40.0%-45.0% in 2021.
- We are therefore revising our outlook on Nexans to positive from negative and affirming our 'BB' long-term issuer credit rating.
- We are also affirming the 'BB' long-term issue rating on the group's senior unsecured notes and the '3'(65%) recovery rating.
- We could raise our rating during the next 18-24 months if Nexans further improves its profitability while reaching FFO to debt comfortably above 35% with positive free operating cash flow (FOCF).

Rating Action Rationale

Nexans' 2020 credit ratios are in line with our threshold for the current rating and we expect they will strengthening in 2021-2022. The group's successful transformation resulted in an estimated S&P Global Ratings-adjusted funds from operations (FFO)-to-debt ratio of about 27% in 2020 (from below 10% in 2019). We expect further improvement in 2021 to about 40%-45% because of:

- The cumulative effect of market and margin recovery;
- The return of the restructuring costs in 2021 back to a recurring historical level of €70 million; and

- The benefit of a high cash balance with an expected deleveraging.

We forecast the group will use its excess cash (€1.142 billion at the end of 2020, excluding an undrawn €600 million revolving credit facility [RCF]) to proceed with the anticipated repayment in first-half 2021 of the €250 million bond (maturing in 2021), as well as the €280 million loan from the government (PGE; Prêt Garanti par l'Etat). This will result in S&P Global Ratings-adjusted debt of about €550 million to €600 million in 2021. In our view, its strong balance sheet will allow the group to consider some potential acquisitions in the coming years in order to participate in the market's consolidation.

In our base case we foresee that Nexans will continue to generate positive FOCF in 2021 and 2022. The group focused on working capital management and managed to generate positive FOCF in both halves of 2020, despite the COVID-19 pandemic. This ended a historical cycle of cash negative first halves and recovery in the second halves. The group implemented a new strategy requiring stricter terms for receivables collection (90 days). It also capped its growth in some countries to better control its margin though stricter project selection. These measures enabled the group to reduce the working capital-to-sales ratio to about 5% in 2020, versus 12% previously and improve profitability. The group generated positive adjusted FOCF of about €200 million in 2020 versus about €30 million in 2019, despite high capital expenditure (capex) of about 4% of total revenue, offset by about €366 million of change in working capital. Furthermore, we expect the group will continue this trend in 2021, given a reduction in capex together with an expected €50 million working capital reduction.

S&P Global Ratings expects Nexans' profitability to remain below average despite improvements. The three-year transformation program that the group announced in January 2019 resulted in roughly €107 million of restructuring charges for 2020 (€170 million cash out), which marked a significant reduction compared with €250 million in 2019. S&P Global Ratings-adjusted EBITDA for 2020 was about €266 million, up by €100 million over 2019, benefiting from the transformation measures and the progressive reduction in restructuring costs. However, we expect recurrent restructuring costs of about €70 million per year from 2021 to continue to drag margins, resulting in an EBITDA margin at about 5.5%-6.0% in 2021 and 2022, versus about 4.5% in 2020.

The group's capex on vessel construction will start to bear fruit. Nexans' new cable vessel, which should be delivered in May 2021, will have a high utilization rate through second-half 2021. We expect this will support the offshore wind turbines installation and marine cables installation businesses, and give the group a competitive advantage.

Nexans remains the world's second-largest cable manufacturer. We view positively Nexans' diversified customer base (no customer accounts for more than 10% of revenue), its established footprint in its core market, and its maintenance of the No.2 position behind Italy-based Prysmian (which had €11.5 billion of revenue and €907 million of reported EBITDA in 2019). Nexans lost market share due to the Prysmian-General cable consolidation, but it remains the No.2 manufacturer in terms of revenue and retains an advantage of scale in competition with many smaller players.

Nexans' margins are exposed to cyclical end markets and metals prices. The group sells its cables mainly in the building and territories sector via the industry and solutions segment. The sector in which the group operates is highly competitive and fragmented. Nexans relies on copper and aluminum for its production, which can decrease profit and increase the working capital volatility during periods of rapidly moving metals prices. We recognize, however, that the group's strongly improved working capital and contract management helps offset that risk. Operating margins could also be affected by slower end-market demand or higher-than-expected competitive pressures.

S&P Global Ratings believes there remains high, albeit moderating, uncertainty about the evolution of the coronavirus pandemic and its economic effects. Vaccine production is ramping up and rollouts are gathering pace around the world. Widespread immunization, which will help pave the way for a return to more normal levels of social and economic activity, looks to be achievable by most developed economies by the end of the third quarter. However, some emerging markets may only be able to achieve widespread immunization by year-end or later. We use these assumptions about vaccine timing in assessing the economic and credit implications associated with the pandemic (see our research here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

Outlook

The positive outlook on Nexans reflects our view that the group's ratio of adjusted FFO to debt will exceed 35% in 2021 with recovery of profitability and positive FOCF.

Upside scenario

We could raise the rating if we believe Nexans can sustainably achieve:

- FFO to debt above 35%;
- A solid recovery through the cycle with an adjusted EBITDA margin around 6%;
- Positive FOCF; and
- A supportive financial policy without significant restructuring needs.

Downside scenario

We may revise the outlook to stable if Nexans' FFO-to-debt ratio remains below 35% without signs of improvement. This could happen if Nexans' revenue or margin development is weaker than our expectation, due to a more severe COVID-19 impact or operational setbacks. This could also happen if the group undertakes substantial debt-funded expansion, acquisitions, or aggressive dividend payments; if it incurs higher restructuring costs; or if FOCF turns negative.

Company Description

France-based Nexans is the world's second-largest cable manufacturer, with €6.0 billion of revenue and €347 million of reported EBITDA in 2020. The group has more than 26,000 employees and is present in more than 30 countries. It operates through five divisions:

Building and territories (about 42% of sales): This division covers markets such as building, e-mobility, rural electrification, and decentralized energy systems. It aims to furnish cabling systems and energy solutions for buildings and territories to improve efficiency and sustainability.

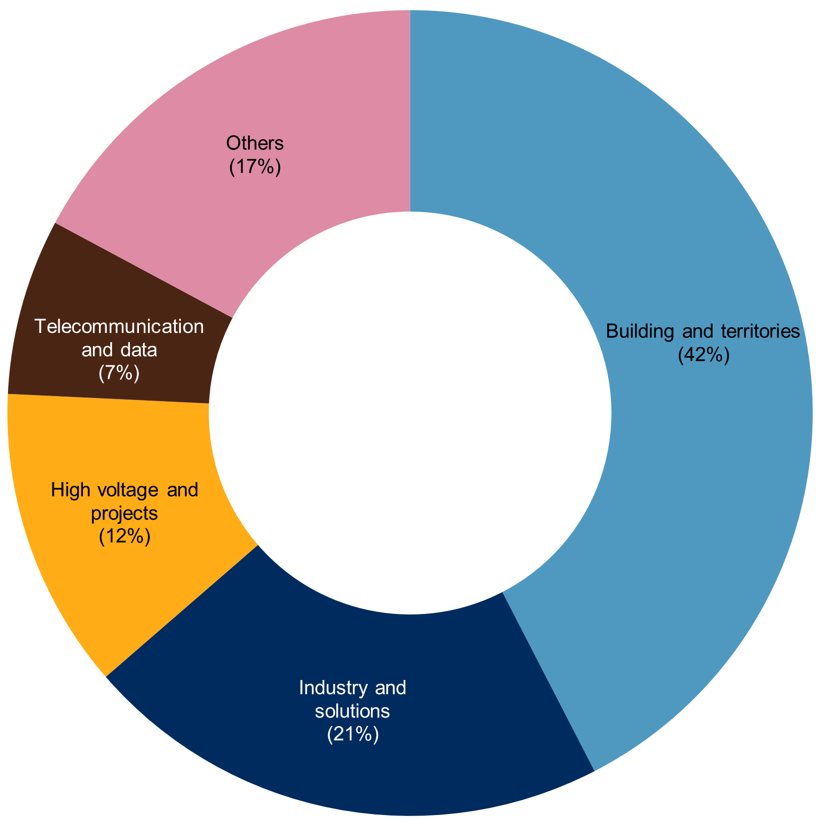
Industry and solutions (about 21%): This segment provides support to original equipment manufacturers (OEMs) and industrial infrastructure projects, offering customized cabling and connection solutions. It covers the transportation, automation, renewables (solar and wind power), resources (oil and gas and mining), and high-tech (nuclear and medical) end markets.

High voltage and projects (about 12%): This division covers end markets such as offshore wind farms, land high voltage, and smart solutions for the oil and gas sector (direct electric heating and subsea heating cables).

Telecommunications and data (about 7%): This division supports customers deploying copper and fiber optic infrastructure within the data transmission (subsea, fiber), telecom networks, hyper scale data centers, and local area network cabling solutions end-markets.

Other activities (about 17%): This division covers wire rods, electrical wires, and winding wire production operations.

Revenue Repartition As Of 2020



Source: S&P Global Ratings.

Our Base-Case Scenario

Assumptions

- Estimated sales increase in 2021 of about 2% supported by the high voltage business as the vessel is deployed and the fiber segment is developed after sales reduction in 2020 of about 11%. We estimate that the advance of 5G will drive revenue growth from 2022.
- Adjusted EBITDA margin of about 5.5% in 2021, after about 4.5% in 2020, as the transformative measures are implemented, with restructuring charges estimated at about €107 million for 2020 (€170 million cash out), and €70 million in 2021 and thereafter.
- A positive €366 million change in working capital in 2020 and €50 million in 2021.
- Capex of about €224 million in 2020, decreasing to about €200 million in 2021 thanks to the vessel's expected delivery in May 2021.
- About €31 million of dividends in 2021.
- We consider an amount of €20 million of bolt-on acquisitions in 2021, factoring in some opportunities the group may have. In 2020 there were no acquisitions but a divestment of Berk-Tek and in the metallurgy sector in September 2020 for €150 million.

Key metrics

Nexans S.A. -- Key Metrics

	--Fiscal year ended Dec. 31--			
(Mil. €)	**2018a**	**2019a**	**2020e**	**2021f**
Revenue growth	1.90%	3.80%	About (11%)	1.5%-2.0%
EBITDA margin (%)	5.1	2.4	About 4.5%	5.5%-6.0%
Capex	207	238	About 224	200-210
FOCF	35	27	About 200	110-120
Debt to EBITDA (x)	3	6	About 2.5x	1.5-2.5x
FFO to debt (%)	23.4	7.4	About 27%	40%-45%

*All figures adjusted by S&P Global Ratings. Note: 2020 year-end debt consists of net financial debt of €1.216 billion with key adjustments being €105 million in leases, €300 million in pension, €74 million litigation, and €1028 million of net cash (we considered 10% cash trapped). a--Actual. e--Estimate. f--Forecast.

Liquidity

The short-term issuer credit rating is 'B'. We view Nexans' liquidity as strong, based on our expectation that sources of liquidity will exceed uses by more than 1.5x over the next 12 months and remain above 1.0x over the subsequent 12-month period. We expect liquidity sources will exceed liquidity uses even if forecast EBITDA declines by 30%.

We think Nexans has well-established relations with banks and demonstrates prudent liquidity management, with sizable cash balances, an undrawn long-term RCF, and a focus on working capital reduction.

Principal liquidity sources from the end of 2020:

- About €1.142 billion of cash and cash equivalents.
- €600 million fully undrawn RCF, which was extended to 2023.
- About €250 million-€300 million of forecast FFO in 2021 and 2022.
- About €50 million inflow from working capital in 2021.

Principal liquidity uses:

- About €530 million debt repayments in 2021. This includes repayments of €250 million 3.25% bonds maturing in 2021 and €280 million loan from government.
- About €50 million of seasonal variation in working capital.
- Between €150 million-€200 million annual capex in 2021 and 2022.
- About €31 million of annual dividends.

Covenants

On Dec. 12, 2018, an amendment to the €600 million syndicated credit facility was signed. The amended syndicated credit facility is subject to the following two covenants, applicable since June 30, 2019. Further the €280 million PGE is also subject to the following covenant limits:

- The consolidated net debt-to-equity ratio (including no-controlling interests) must not exceed 1.20x.
- Consolidated debt is capped at 3.2x consolidated EBITDA.

No covenant was breached in 2020. We consider the group has ample headroom, given its high cash balances.

Issue Ratings - Recovery Analysis

Key analytical factors

- The senior unsecured notes (comprising the €250 million notes due in 2021, €325 million notes due in 2023, and €200 million notes due in 2024) are rated 'BB' with a recovery rating of '3' (capped due to unsecured nature of obligations). The ratings are based on our expectation of 50%-70% recovery (rounded estimate of 65%) in the case of a payment default.
- The recovery rating on the facilities is supported by limited priority ranking debt, while it is constrained by the notable quantum of pari-passu unsecured debt.
- Our hypothetical default scenario stems from a severe global recession in key markets, tightening credit markets, and significant contraction in demand due to an overall economic slowdown.
- We value the group as a going concern, given its strong brand and strong competitive position.

Simulated default assumptions

- Year of default: 2026
- Jurisdiction: France

Simplified waterfall

- Emergence EBITDA: €243 million.
- Minimum capex at 2%, based on the group's average minimum capex requirement trend: €120 million.
- Standard cyclicality adjustment of +15%.
- Implied enterprise value multiple: 5.5x.
- Gross enterprise value at default: €1.185 billion
- Net enterprise value after administrative costs (5%): €1.126 billion
- Estimated senior unsecured debt: 1.55 billion
- Value available for senior unsecured claims: €1.126 billion
- Recovery expectations: 50%-70%; rounded estimate: 65%

Note: All debt amounts include six months of prepetition interest accrued and assumed 85% drawn on the RCFs.

Ratings Score Snapshot

Issuer Credit Rating: BB/Positive/B

Business risk: Fair

- Country risk: Moderately high
- Industry risk: Low
- Competitive position: Fair

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: bb

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Strong (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Fair (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bb

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed; Outlook Action

	To	From
Nexans S.A.		
Issuer Credit Rating	BB/Positive/B	BB/Negative/B
Senior Unsecured	BB	BB
Recovery Rating	3(65%)	3(50%)