Research Update:

Netherlands-Based Cementir Holding N.V. Assigned 'BBB-' Rating; Outlook Stable

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Rating Action Overview

- Cementir Holding N.V.--which produces and distributes grey and white cement, ready-mix concrete, and aggregates--reported revenues of €1.2 billion and EBITDA of €261 million at end-2020.
- Cementir's operating performance remained resilient throughout 2020, despite the COVID-19 pandemic fallout, enabling significant debt reduction. As a result, its S&P Global Ratings-adjusted funds from operations (FFO) to debt improved to about 125% from about 73% in 2019.
- We anticipate that Cementir will maintain robust operating performance in most of its regions over 2021-2022. We forecast strong credit metrics in 2021-2022, supported by revenue growth of about 5%-7% and an EBITDA margin of 22.0%-22.5%.
- We expect that management will maintain its prudent financial policy, with a strong focus on deleveraging and margin improvements.
- We are therefore assigning our 'BBB-' long-term issuer credit rating to Cementir.
- The stable outlook indicates that we expect Cementir's FFO to debt to remain well above 45% in 2021-2022 and management to maintain a prudent financial policy.

Rating Action Rationale

Our assessment of Cementir's business risk continues to factor its broad geographic diversification and leading position as a white cement producer. The group has operations in Europe, North America, and Asia-Pacific. We note that its high exposure to Scandinavian countries was one of the differentiating factors that, historically, contributed to top-line results being better than the industry average, especially compared with other European cement players. Although the group also has sizable exposure to high-risk countries, such as Turkey and Egypt, we consider that performance in these regions has recently improved. Our assessment of the business risk also factors in Cementir's world-leading position in producing white cement, with 3.3 million tons of installed capacity and a global market share of about 12%. White cement is a more sophisticated niche product than traditional grey cement, with a higher margin and more flexibility for international distribution. Cementir is also the leading producer of cement in Denmark and of ready-mixed concrete in the Scandinavian region. It is the third largest player in Belgium and among the main international producers of grey cement in Turkey.

The group's smaller size and exposure to the cyclical building material industry constrain the assessment. Our assessment is constrained by the group having smaller revenue and EBITDA base compared with peers across the industry. While we note that Cementir's geographic diversification is lower than that of other building materials companies, we believe its exposure to white cement provides wider product diversification than cement manufacturers focused on grey cement. Our assessment also reflects some key risks, such as the high capital and energy intensity of the heavy building materials industry, and Cementir's operations in a competitive and fragmented industry with limited pricing flexibility. The commoditized nature of the group's products represents a competitive risk. However, we believe this is partially mitigated by its solid local positions in relatively consolidated markets.

We believe that Cementir's competitive advantage and profitability may benefit from planned green investments. The group's new business plan accounts for €107 million cumulative investments in sustainability by 2023 for specific projects concerning the reduction of CO2 emissions at its plants. Specifically, the group aims to reduce emissions to below 500kg per ton of grey cement by 2030, which is broadly in line with most peers. In our view, Cementir has demonstrated a good record of product innovation, for example, launching new types of sustainable cement based on a patented technology. This allows it to lower the clinker ratio by 40% and thus reduce CO2 emissions in its products by around 30%. We believe that the planned improvement in sustainability may significantly boost Cementir's competitive advantage versus small players. Furthermore, lower emissions may result in reduced operating costs for cement production, particularly in countries with an emissions-trading framework, such as the EU. Nevertheless, the cement sector worldwide is far from achieving carbon neutrality by 2050, and we believe that cement companies will likely face high capex spending related to CO2 emissions reduction over the current decade to comply with more stringent regulations.

We anticipate Cementir's resilient 2020 operating performance will continue into 2021. Resilient top-line growth and an improved EBITDA margin, combined with strong deleveraging, helped Cementir achieve robust operating performance last year. This resulted in FFO to debt increasing to about 125% in 2020, compared with 73% in 2019. The group reported overall revenue growth of 1.1% in 2020 and its margins were largely in line with the previous period. We expect Cementir will continue to perform well in 2021, with good cash flow generation from top-line results, solid working capital management, and efficiency improvement initiatives that will more than offset the resumption of capital expenditure (capex) and increasing energy and raw material prices.

Our rating on Cementir reflects its focus on deleveraging and margin improvements. We forecast the group will post FFO to debt of about 95%-115% and adjusted debt to EBITDA of below 1x in 2021-2022. In its 2019 business plan, Cementir's management committed to reaching a net cash position by 2022. The group is making good progress toward this target; in 2020, Cementir's leverage position improved substantially and adjusted debt to EBITDA fell to 0.6x. It also managed to implement several efficiency improvements and cost containment measures in 2020 that should support margin improvement. We project an EBITDA margin of about 22.0%-22.5% in 2021 and 2022. The deleveraging trend is also supported by management's decision to refinance its debt maturities of about €330 million in 2021, with amortized debt of about €150 million. We expect this to underpin lower leverage in the future capital structure. Overall, these changes should support FFO to debt of about 95%-155% and adjusted debt to EBITDA of below 1.0x in 2021 and 2022.

We consider Cementir's commitment to preserve credit metrics in line with a 'BBB-' rating and its prudent financial policy. In our view, the group will achieve this by keeping the amount of debt in the capital structure low, and through moderate shareholder remuneration and prudent investments. Cementir's commitment to reducing leverage is embedded in its capital allocation strategy, which states that it will only consider new expansion projects and acquisitions if they do not impair its balance sheet. The dividend payout ratio averaged 22% over the past five years. We consider this in line with the market average, rather than aggressive. Given the current rating headroom, we believe that Cementir's credit metrics are unlikely to fall below the rating triggers despite some bolt-on acquisitions and future capex investments related to reducing carbon dioxide (CO_2) emissions.

Our ratings incorporate potential moderate acquisitions, which could increase the volatility of credit metrics. In recent years, Cementir has shown a consistent record of large debt-funded acquisitions, which increased volatility in credit metrics. For instance, financial leverage increased in 2016 as result of two debt-financed purchases, causing FFO to debt to fall below 30% from 50% in 2015. We note that the group has undertaken fewer acquisitions over the past two years, although Cementir could pursue larger strategic acquisitions in the next few years to maintain its competitive position in the market. However, we view this as unlikely at this stage and do not factor it into our base-case scenario. Although a large debt-funded acquisition could significantly increase volatility in credit metrics, we believe that FFO to debt would remain comfortably above 45%.

Outlook

The stable outlook reflects our view that Cementir will sustain FFO to debt well above 45% and adjusted debt to EBITDA below 1.5x. We view the group's financial policy and capital allocation strategy as consistent with a 'BBB-' rating.

Downside scenario

We could consider lowering the rating if:

- Large debt-funded acquisitions, capital investments, or shareholder distributions led to credit metrics dropping significantly below our base case, such that FFO to debt fell below 45%, with limited possibility of a swift recovery.
- The group seems likely to follow a financial policy that does not support FFO to debt above 45% and debt to EBITDA below 1.5x on a sustained basis.

Upside scenario

We consider an upgrade unlikely in the next couple of years, as it would require Cementir to achieve significantly larger business diversification, while keeping the same profitability and credit metrics.

Company Description

Founded in 1947, Cementir is a Netherlands-based producer and distributor of grey and white cement, ready-mix concrete, and aggregates. It is the world leader in white cement; the leading producer of cement in Denmark, and of concrete in the Scandinavian area; the third larger player in Belgium; and among the main international grey cement operators in Turkey. The group operates in Belgium as one of the largest aggregate quarries in Europe, with 10 million tons extracted each year. The group is also active in urban and industrial waste processing. Cementir's international growth over the years has mainly been driven by investments and acquisitions totaling a combined €1.7 billion. These have transformed the company from a domestic to a multinational player with production sites and products marketed in more than 70 countries. As of end-2020, the group reported total revenue of about €1.2 billion and adjusted EBITDA of about €254 million.

Cementir is owned and controlled by the Caltagirone family (directly and indirectly), with about 29% of shares being free float.

Our Base-Case Scenario

Assumptions

In 2020-2021, we assume in our base case:

- Real GDP growth of 6.5% in North America in 2021 followed by 3.1% in 2022; in the eurozone, 4.2% real GDP growth in 2021 and 4.4% in 2022; and in Asia Pacific, GDP growth of 6.7% in 2021 and 4.7% in 2022.
- Revenue growth of 5%-7% in 2021 and 3%-4% in 2022. This is based on our positive view of the business conditions for the construction industry in most of the regions where Cementir operates, supported by public stimulus on infrastructure works, as well as positive price developments.
- Adjusted EBITDA margins of about 22.0%-22.5% in 2021 and 2022, which compares with about 21.0% in 2020. The improving margins reflect the improved pricing expected in Turkey and in Benelux, combined with continued efficiency improvements, which will more than compensate for the increasing cost of raw materials and energy.
- Small to neutral working capital inflow.
- Capex of about 7%-8% of revenue.
- About €22 million of dividend payments and moderate share buyback, in line with management guidance.
- Moderate acquisitions over the next few years.

Key metrics

Based on these assumptions, we arrive at the following credit measures for the year 2021:

- S&P Global Ratings-adjusted debt to EBITDA below 1.0x;

- Adjusted FFO to debt at around 95%-115%; and
- Adjusted free operating cash flow to debt of 55%-75%.

In our base-case scenario, we do not include any significant debt-funded acquisitions. Due to the current very limited net debt position, leverage is very sensitive to any material increase in debt, which would substantially weaken credit metrics.

Our adjusted debt figure is slightly higher than the group's reported debt figure. This is because we add in about €86 million of reported lease liabilities and €28 million related to pension liabilities. However, we net about €397 million of surplus cash, which we consider available for debt repayment.

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.

Liquidity

We continue to view Cementir's liquidity as adequate, because we forecast that the group's sources of liquidity will cover its uses by more than 1.2x in the next 12 months. We believe that Cementir will have adequate headroom under its leverage and coverage covenants. In our view, the group lacks experience in capital markets, despite sound banking relationships, and might not be able to absorb high-impact, low-probability events without refinancing.

Principal liquidity sources over the next 12 months starting Jan. 1, 2021, are:

- Cash and cash equivalents of about €413 million;
- Cash inflow of about €8 million-€12 million from working capital; and
- Our forecast of cash FFO of about €216 million.

Principal liquidity uses over the same period are:

- Short-term debt maturities of about €344 million;
- Maintenance capex of about €60 million-€65 million;
- Seasonal requirements at about €50 million;
- Dividend payments of about €20 million-€30 million; and
- Moderate share buyback.

Covenants

We expect Cementir to maintain adequate (that is, greater than 15%), headroom against all of its covenants over the next two years, therefore meeting our criteria for adequate liquidity.

Ratings Score Snapshot

Issuer credit rating: BBB-/Stable/--

Business risk: Fair

- Country risk: Low
- Industry risk: Intermediate
- Competitive position: Fair

Financial risk: Minimal

- Cash flow/Leverage: Minimal

Anchor: bbb-

Modifiers:

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

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- 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

New Rating	
Cementir Holding N.V.	
Issuer Credit Rating	BBB-/Stable/--