

**Rating Action: Moody's downgrades MAHLE's ratings to Ba2 from Ba1, outlook negative**

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Frankfurt am Main, September 30, 2022 -- Moody's Investors Service ("Moody's") has today downgraded the corporate family rating (CFR), and the senior unsecured instrument ratings of German automotive parts supplier MAHLE GmbH ("MAHLE" or "the company") to Ba2 from Ba1. Concurrently, Moody's downgraded the company's senior unsecured euro medium term note programme rating to (P)Ba2 from (P)Ba1 and the probability of default rating (PDR) to Ba2-PD from Ba1-PD. The outlook on the ratings remains negative.

"The rating downgrade reflects challenges to pass-on higher raw material and energy costs and the ongoing challenges in the Thermal Management and Electronics and Mechatronics divisions, reflected in weak margins and elevated leverage, which are not commensurate with the expectations for the Ba1 rating category", said Matthias Heck, a Moody's Vice President – Senior Credit Officer and Lead Analyst for MAHLE. "The negative outlook reflects challenges for the company to improve its margins in an increasingly difficult macroeconomic environment to at least 3% and restore currently negative free cash flow within the next 12-18 months", added Mr. Heck. "We positively recognize MAHLE's good liquidity profile, which provides the company with a solid cushion until performance is restored to adequate levels for the Ba2 rating category", Mr. Heck continues.

**RATINGS RATIONALE**

In the first half of 2022, MAHLE's revenues increased by 4.1% to €5.9 billion, outperforming global light vehicle sales (minus 9.6%) by approximately 1,370 basis points. At the same time, however, the company recorded an EBIT loss of €182 million, as higher cost for materials, freight and energy could not be passed on to customers. Free cash flows amounted to even minus €417 million, including an expansion of working capital and cash outs for restructuring. Concurrently, MAHLE's net debt increased to €1,682 million at the end of June, compared to €1,056 million at the end of December 2021.

Moody's expects that global light vehicle sales will recover in the second half, so 2022 sales will almost reach previous year's level. This volume recovery, and price increases (due to the pass-on of higher raw material cost) should enable MAHLE to recover the losses seen in the first half and achieve a small operating profit margin of around 1% (Moody's adjusted EBITA) this year, a considerable decline versus the 2.1% achieved in 2021 and well below 4%, which Moody's considered as the minimum for the Ba1.

For 2023, Moody's expects a recovery of global light vehicle sales, in an overall more difficult automotive sector environment, where increasing interest rates and weaker consumer affordability dampen light vehicle demand and profitability of automakers. In this environment, Moody's expects a modest recovery of MAHLE's operating profit margins.

At the end of June 2022, MAHLE's debt (Moody's adjusted, including pension provisions) amounted to €3.0 billion, which leads to a debt/EBITDA (Moody's adjusted) of 9x, given the weak profitability. Including the operating improvements expected in the second half of 2022, Moody's expects debt/EBITDA to decrease to around 4.5x, which is still well above the maximum of 3.0x, which Moody's expected for the Ba1 rating category. In 2023, Moody's expects a further de-leveraging to a range of 3.0x-3.5x, which is commensurate with a Ba2.

The negative outlook reflects the slow recovery of global light vehicle sales in an increasingly difficult macroeconomic environment. This might make it challenging to improve margins (Moody's adjusted EBITA) to at least 3% and to reduce debt/EBITDA (Moody's adjusted) to a maximum of 3.5x within the next 12-18 months.

The Ba2 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 limited ability to timely and completely pass-on higher production cost, and weak free cash flow generation over the last few years, (3) relatively low exposure to the 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 €431 million (as of June 2022) 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), of which €1.4 billion was undrawn. In addition, the company entered into a €300 million 10-year term loan with EIB in August. With this, MAHLE's liquidity sources over the next 12 months amount to approximately €2.5 billion under the stressed assumption of no access to capital markets.

These liquidity sources comfortably exceed liquidity uses of around €1.2 billion, mainly comprising of capital spending, which Moody's expects at around €600 million, and €300 million short-term debt maturities. Uses of liquidity further include Moody's working cash assumption of €300 million.

## STRUCTURAL CONSIDERATIONS

MAHLE's Ba2 senior unsecured instrument rating recognizes trade claims and pension provisions at the level of operating subsidiaries which are in aggregate material in size and have higher seniority in the debt structure of MAHLE. The debt has nonetheless not been notched as a reflection of the investment-grade debt structure of the group, and its good liquidity. Moody's might, however, introduce a notching if MAHLE's CFR were to be downgraded below the Ba2 level.

## 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 3.5x, EBITA margins remained below 3% (Moody's adjusted), retained cash flow (RCF) / net debt below 15%, or liquidity weakened.

Moody's would consider an upgrade of the ratings should MAHLE achieve sustainably Debt/EBITDA (Moody's adjusted) below 3.0x, EBITA margins (Moody's adjusted) above 5%, and RCF/net debt of more than 20%.

## PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Automotive Suppliers published in May 2021 and available at <https://ratings.moodys.com/api/rmc-documents/72204>. Alternatively, please see the Rating Methodologies page on <https://ratings.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 on <https://ratings.moodys.com/rating-definitions>.

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