MOODY'S

Rating Action: **Moody's affirms MAHLE's Ba2 ratings, outlook remains negative**

18 Oct 2023

Frankfurt am Main, October 18, 2023 -- Moody's Investors Service (Moody's) has today affirmed the long term corporate family rating (CFR), and the senior unsecured instrument rating of German automotive parts supplier MAHLE GmbH ("MAHLE" or "the company") at Ba2. Concurrently' Moody's affirmed the company's senior unsecure euro medium term note programme rating at (P)Ba2 and the probability of default rating (PDR) at Ba2-PD. The outlook remains negative.

"The affirmation of the ratings reflects the recent progress the company made in terms of profitability, as well as measures taken to reduce the company's debt burden", said Matthias Heck, a Moody's Vice President – Senior Credit Officer and Lead Analyst for MAHLE. "The negative outlook reflects ongoing challenges to achieve margins to levels commensurate with the Ba2 and to generate positive free cash flows within the next 12-18 months", added Mr. Heck.

RATINGS RATIONALE

In the first six months of 2023, MAHLE's revenues increased by 12% to €6.6 billion, achieving a company-defined EBITDA margin of 6.1%, a considerable improvement versus the first half of 2022 (2.1%). The improvement was driven by higher volumes (including around 10% higher global light vehicle production) and the pass-on of higher production cost to its customers. Margins remained, however, constrained by weak profitability in the thermal management division as well as negative one-offs and high upfront cost in the electronics and mechatronics division. On a Moody's adjusted basis, MAHLE's EBITA margin in the last twelve months to June 2023 improved to 3.0%, which marks the very low end of Moody's expectations for a Ba2 rating.

MAHLE's debt (Moody's adjusted) increased to €3.4 billion at the end of June, compared to €3.2 billion at the end of December. This was primarily driven by a high working capital expansion, which Moody's expects to largely revert during the second half of this year. MAHLE's debt/EBITDA (Moody's adjusted) improved to 3.8x at the end of June, from very high levels of 5.2x at the end of December 2022. Continued operating improvements and a release of working capital should bring MAHLE's leverage closer to the level of 3.5x, which Moody's considers as a maximum for the Ba2.

The company is also working on asset disposals to de-lever its balance sheet. These include the sale of MAHLE's 50% stake in the BHTC joint venture, which was announced on 2 October, and which Moody's expect to improve leverage by around 0.2x. On 8 October, MAHLE Metal Leve, which is publicly listed in Brazil and 70% owned by MAHLE, announced that it is evaluating the feasibility of a primary and/or secondary offering of shares in Brazil. A partial sale of MAHLE's stake in this subsidiary could further de-lever MAHLE's balance sheet. Moody's therefore considers that disposal proceeds can reduce MAHLE's leverage to levels more in line with the range of 3.0x-3.5%, which is commensurate with the Ba2.

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 €12.4 billion in 2022 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 cyclicality 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, limited ability to timely and completely pass-on higher production cost, and weak free cash flow generation over the last few years, (3) high investment needs into R&D and capex to make the product portfolio more independent from ICEs, (4) 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, and (5) credit metrics, which are currently weakly positioned compared to Moody's requirements for the Ba2 rating category but expected to improve within the next 12-18 months.

RATIONALE FOR THE NEGATIVE OUTLOOK

MAHLE's rating remains weakly positioned at this point. The negative outlook reflects challenges to achieve EBITA margins (Moody's adjusted) of at least 3% within the next 12-18 months. It also reflects challenges to generate positive free cash flows, which are, in addition to asset disposals, needed to reduce leverage to levels that are more comfortable within the range of 3.0x-3.5x debt/EBITDA (Moody's adjusted), which Moody's expects for the Ba2.

LIQUIDITY

Moody's considers MAHLE's liquidity position to be good. The company's main sources of liquidity include (1) cash on balance of €577 million (as of June 2023) and (2) Moody's estimate of annual funds from operations of more than €500 million. The company also has a €1.8 billion revolving credit facility (RCF), of which €1.5 billion have been extended to mature in mid-2025. The remainder will mature in July 2024 already. Around €0.5 billion was drawn, so the available RCF available for the next six quarters amounts to €1.0 billion. With this, MAHLE's liquidity sources over the next 12 months amount to approximately €2.1 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 €550 million, and around €200 million short-term debt maturities to June 2024. Use of liquidity further include Moody's working cash assumption of €360 million and dividend payments to own and minority shareholders.

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 failed to reach at least 3% (Moody's adjusted), retained cash flow (RCF) / net debt remained 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%. Moreover, an upgrade would require a reduced exposure to products used for internal combustion engines only, including plug-in hybrids.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Automotive Suppliers published in May 2021 and available at https://ratings.moodys.com/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 (36% of 2022 sales), Engine Systems and Components (21%) and Filtration and Engine Peripherals (16%). In 2022, MAHLE generated revenues of around €12.4 billion. MAHLE, which employed around 72.000 employees and produced in around 152 locations worldwide in

2022, is owned by the MAHLE Foundation. The company owns a 70% stake in the MAHLE Metal Leve S.A., which is publicly listed in Brazil.

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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Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://ratings.moodys.com/documents/PBC_1355824.

At least one ESG consideration was material to the credit rating action(s) announced and described above.

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the UK and is endorsed by Moody's Investors Service Limited, One Canada Square, Canary Wharf, London E14 5FA under the law applicable to credit rating agencies in the UK. Further information on the UK endorsement status and on the Moody's office that issued the credit rating is available on https://ratings.moodys.com.

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