S&P Global Ratings

RatingsDirect®

Research Update:

Swedish Steelmaker SSAB Outlook Revised To Positive On Strengthened Credit Metrics; Affirmed At 'BB-/B'

Primary Credit Analyst:
Lena Liacopoulou Staad, Paris 01 44 20 67 39; lena.liacopoulou@spglobal.com

Secondary Contact:
Tommy J Trask, Dubai (971) 4-372-7151; tommy.trask@spglobal.com

Table Of Contents

Research Update:

Swedish Steelmaker SSAB Outlook Revised To Positive On Strengthened Credit Metrics; Affirmed At 'BB-/B'

Overview

- Stronger demand for steel and company-driven initiatives such as cost reduction and improving product mix emanating from growth in high strength steel, have resulted in improved earnings, cash flow, and credit metrics for Swedish steelmaker SSAB over the past years.
- We expect that the company will continue to generate healthy discretionary cash flow in the next 12 months.
- We are therefore revising our outlook on SSAB to positive from stable and affirming our 'BB-/B' ratings.
- The positive outlook reflects our expectation that SSAB's leverage will continue to decline over the coming 12 months on the back of a supportive industry environment and positive discretionary cash flow generation.

Rating Action

On Feb. 15, 2018, S&P Global Ratings revised its outlook on Swedish steelmaker SSAB AB to positive from stable. We affirmed the 'BB-' long-term and 'B' short-term issuer credit ratings on the company.

We also affirmed our issue ratings on SSAB's senior unsecured debt at 'BB-'. The recovery rating on this debt is unchanged at '3', indicating our expectation of meaningful recovery (50%-70%; rounded estimate: 65%) in the event of a payment default.

Rationale

The outlook revision follows SSAB's report of its strong results for full-year 2017 and reflects our view that SSAB has made good progress in debt and cost reduction amid improved steel market conditions in Europe and the U.S. following the introduction of import duties, notably on steel from China.

The positive outlook also points to SSAB having exceeded its net debt reduction target of Swedish krone (SEK) 10 billion (about €1 billion) by achieving a SEK12.2 billion reduction at end- 2017. We expect SSAB will repay at least another SEK2 billion of debt maturing in 2018 with existing cash and short-term deposits. SSAB achieved full-year EBITDA of SEK7.8 billion (versus SEK5.2 billion in 2016), driven primarily by higher prices and growth in high-strength steel in the automotive segment within SSAB Europe.

We continue to view favorably SSAB's 35% net debt-to-equity target, compared with the reported ratio of 22% on Dec. 30, 2017, and understand that the company is pursuing lower leverage than this target under current favorable market conditions. The company has generated positive discretionary cash flow over the past three years, helped in 2016 and 2017 by positive working capital movements and no dividends. In 2017, positive discretionary cash flow more than doubled (compared with 2016), supported by higher earnings, a SEK300 million cash inflow from working capital, continued low capital expenditures (capex), and no dividends.

In our base case for SSAB for 2018 and 2019, we assume:

- Continued favorable industry margins in the U.S. and Europe following the introduction of antidumping measures in the EU and U.S., and taking into account our GDP growth expectation of 2.1% for the EU and 2.8% for the U.S. in 2018, which should support demand growth in both markets.
- EBITDA of around SEK8 billion and an EBITDA margin of about 12%. This improvement from SEK4 billion and 7%, respectively, in 2015 reflects a full run rate of cost savings following the merger with Rautaruukki, in addition to a better industry environment.
- Capex of slightly more than SEK2 billion annually.
- SEK1 billion in dividends in 2018 and 50% of net income thereafter.

Based on these assumptions, we arrive at the following S&P Global Ratings-adjusted credit measures in 2018 and 2019:

- Funds from operations (FFO) to debt of around 40% in 2018 and 50%-60% in 2019.
- Debt to EBITDA of around 2.0x in 2018 and approximately 1.5x in 2019.

SSAB operates in the highly cyclical steel industry, with end markets such as heavy transportation, construction, machinery, and mining. Metal prices typically move in line with demand and supply over the long term, and can be volatile in the short term, as happened in the second half of 2015.

SSAB's key strength is its strong market position in special-grade steel products. For example, it has a global market share of about 40% in quenched and tempered steels, along with about 5% in some advanced high strength steels, and around 25% market share in heavy plates in North America, according to its own estimates. Following the merger with Rautaruukki, it also commands a 40%-50% share in the flat carbon steels and tubes market in the Nordic region.

In our opinion, the main challenges for SSAB are the risk of new specialty-grade steel capacity from competitors and the pace of take-up of special-grade steel products by equipment manufacturers.

Liquidity

We assess SSAB's liquidity as strong because we forecast the company's liquidity sources will cover its uses by more than 2x over the next 24 months. The company passes its new net debt to equity covenant of 60% comfortably in this assessment.

Principal liquidity sources for the 12 months from Dec. 31, 2017, are:
- Cash and cash equivalents of SEK6.7 billion, including SEK2.5 billion of pledged cash.
- Availability under long-term committed credit lines of SEK7.2 billion.
- Our estimate of FFO of about SEK6.0 billion-SEK6.5 billion over the coming 12 months.

Principal liquidity uses for the same period are:
- Short-term debt of SEK3.3 billion, including off-balance-sheet receivable securitization.
- Capex of just over SEK2 billion.
- From 2018, a dividend payment of 50% of profit before tax.

Outlook

The positive outlook reflects our expectation that SSAB will have strong credit metrics in the next two years thanks to a supportive industry environment. We expect SSAB to maintain debt to EBITDA in the 2x-3x range (2.3x in 2017) and FFO to debt in the 30%-45% range (34% in 2017) through the cycle, although we could see the company posting stronger metrics if conditions remain supportive beyond 2018.

Downside scenario

We could lower the rating if SSAB's credit ratios fail to remain in the aforementioned ranges, under mid-cycle market conditions, or leverage above 4x and FFO to debt below 20% at a cyclical low. This could be the result of operational setbacks, combined with weaker market conditions, or a more aggressive financial policy, including debt-financed acquisitions.

Upside scenario

We could consider a higher rating through the revision of SSAB's competitive position assessment, if SSAB demonstrates margin stability over the cycle, or under weaker market conditions than we see today. In addition, we would expect margins to remain in the peer group average. An upgrade could also stem from a positive reassessment of the company's financial risk profile, if credit metrics were to strengthen further such that debt to EBITDA remains sustainably below 2x and FFO to debt above 45% over the cycle. We will likely review the rating on the company over the coming 12 months.

Ratings Score Snapshot

Issuer Credit Rating: BB-/Positive/B

Business risk: Weak
- Country risk: Very low
- Industry risk: Moderately high
- Competitive position: Weak

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: Satisfactory (no impact)
- Comparable ratings analysis: Neutral (no impact)

Issue Ratings--Recovery Analysis

Key analytical factors

- SSAB's senior unsecured debt has an issue rating of 'BB-' and recovery rating of '3'. The recovery rating is underpinned by SSAB's substantial asset base, and minor prior-ranking liabilities, offset by the unsecured nature of the debt and substantial debt at pari passu level. Recovery is about 65% and may come under downward pressure if SSAB incurs additional secured debt.
- In our hypothetical payment default scenario, we take into account our view of the cyclicality of the markets in which SSAB operates, and sustained weakness in steel demand that leads to a drop in volumes, utilization rates, and prices.
- We value SSAB as a going concern, given its strong position in the heavy plate market in North America and in special-grade steel products, and its competitive assets.

Simulated default assumptions

- Year of default: 2023
- EBITDA at emergence: SEK3.5 billion
- Implied enterprise value multiple: 5.5x
- Jurisdiction: Sweden

Simplified waterfall

- Net value available to creditors (after administrative costs): SEK18.1 billion
- Priority claims: SEK3.1 billion
- Senior unsecured debt claims: SEK22.0 billion*
- Recovery expectation: 65%

*All debt amounts include six months of prepetition interest.

Related Criteria

- 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
- Criteria - Corporates - Industrials: Key Credit Factors For The Metals And Mining Downstream Industry, Dec. 20, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed; Outlook Action

	To	From
SSAB AB		
Corporate Credit Rating	BB-/Positive/B	BB-/Stable/B
Senior Unsecured	BB-	BB-
Recovery Rating	3(65%)	3(55%)

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@spglobal.com

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.