MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns B2 CFR to F-Brasile S.p.A. (Forgital); stable outlook

29 Jul 2019

Frankfurt am Main, July 29, 2019 -- Moody's Investors Service ("Moody's") Moody's Investors Service ("Moody's") has today assigned a B2 corporate family rating (CFR) and B2-PD probability of default rating (PDR) to F-Brasile S.p.A. ("F-Brasile" or "the Issuer"), an indirect holding company of Italian advanced aerospace forgings supplier Forgital Italy ("Forgital"). At the same time, Moody's has assigned B2 instrument ratings to the Issuer's proposed USD505 million 7-year senior secured notes, issued by F-Brasile S.p.A. and F-Brasile US, LLC, and a Ba2 rating to the Issuer's proposed EUR80 million 7-year super senior secured revolving credit facility (SSRCF). The outlook on the ratings is stable. This is the first time that Moody's has rated F-Brasile.

The proceeds from the proposed notes issue and EUR512 million of sponsor cash equity will be used to finance the approximately EUR950 million enterprise value of Forgital (9.5x multiple based on EUR99.7 million normalized EBITDA as of LTM March 2019) and relevant transaction fees and expenses.

RATINGS RATIONALE

The rating is well positioned at the outset, reflecting (1) Forgital's exposure to successful engine programs which are shortly reaching full-rate production, including the Trent XWB and LEAP; (2) its sizeable backlog from the sale of forged engine components of around EUR659 million (2020-2026) and long-term agreements with customers, which provide good revenue visibility; (3) healthy profitability with an average Moody's-adjusted EBITDA margin of 20% over the last three years, which Moody's expects to further strengthen thanks to robust growth in the higher-margin aerospace business; (4) solid barriers to entry related to the significant capital intensity of the forging business, established relationships with customers facing high switching costs, and Forgital's proven track record of meeting customers' high quality and timely delivery requirements; (5) strong competitive position thanks to its vertically integrated production model and recent significant investments in new capacity in a supply-constrained commercial aerospace market; (6) end-market diversification through the group's complementary industrial division (35% of group sales in 2018), which however in Moody's view will display greater demand cyclicality than the aerospace business; and (7) Moody's positive outlook for the global commercial aerospace and defense industry, based on expected passenger miles growth in excess of global GDP growth.

Factors constraining the rating include Forgital's (1) small size with group sales of EUR387 million in 2018; (2) concentration on few customers in the aerospace business, especially Rolls-Royce plc (c.45% of 2018 group sales); (3) reliance on a smooth production ramp-up of major engine programs such as the Trent XWB, which represented over 50% of the group's 2018 aerospace revenues, although should boost topline and earnings growth over the next two years; (4) lack of an aftermarket business, which could help mitigate a potential slowdown in new engine production; (5) limited free cash flow generation in 2019 and 2020 due to ongoing sizeable extraordinary capital investments to meet expected strong engine production growth over the next three years; (6) initially high leverage of around 5.8x Moody's-adjusted gross debt/EBITDA (pro forma) for the 12 months through March 2019, although Moody's expects this to decline to below 5x by 2020, driven by strong growth in aerospace profits; (7) most of Forgital's raw material purchases in the aerospace business (around 78%) are covered by price pass-through mechanisms, so negative effects from price increases are mitigated, but there are some challenges associated with passing on rising raw material costs to industrial customers; and (8) risk of potential debt-funded acquisitions. In addition, the rating considers the fairly lenient terms of the new debt instruments, which, for instance, allow for incremental indebtedness of the greater of EUR100 million or 100% of consolidated EBITDA.

LIQUIDITY

Forgital's liquidity is adequate, considering the absence of short-term debt maturities following the proposed transaction and only limited prospect for free cash flow generation over the next 12-18 months. The group has access to a sizeable new EUR80 million super senior RCF, which Moody's expects to be partly utilized to provide some starting cash at closing of the transaction (the transaction structure assumes a zero cash balance).

The super senior RCF is subject to a springing super senior net leverage covenant, tested when the facility is drawn down for more than 40%. The covenant is set with ample initial headroom at closing of the transaction and Moody's expects Forgital to ensure covenant compliance at all times.

STRUCTURAL CONSIDERATIONS

Upon completion of the acquisition, the USD505 million senior secured notes will be guaranteed by subsidiaries accounting for approximately 80% of the group's consolidated EBITDA and will be secured by certain assets (mainly share pledges and bank accounts) of the guarantors.

The proposed EUR80 million SSRCF benefits from the same security package and guarantor coverage as the senior secured notes, but receives enforcement proceeds in case of liquidation prior to senior secured notes holders. Hence, Moody's has ranked the SSRCF ahead of the secured notes.

Trade payables, as well as unsecured lease rejection claims and pension obligations, are ranked at the same level as the senior secured notes. Assuming a standard 50% recovery rate for capital structures with both bond and bank debt, the senior secured notes are rated B2 in line with the CFR, while the senior ranking SSRCF is rated Ba2, three notches above the CFR.

RATIONALE FOR THE STABLE OUTLOOK

The stable outlook is predicated on the expectation that Forgital's aerospace sales and earnings will grow at least in line with global air traffic volumes and aircraft production at mid-single-digit rates, and that its industrial division will remain broadly stable. While forecasted profit growth should enable the group to steadily de-lever to below 5x debt/EBITDA by 2020, free cash flow generation should turn slightly positive, supporting a consistently adequate liquidity profile.

WHAT COULD CHANGE THE RATING UP/DOWN

Moody's would consider to upgrade F-Brasile, if (1) leverage reduces to well below 5x Moody's-adjusted debt/EBITDA, (2) Moody's-adjusted FCF/debt exceeds 5%, (3) liquidity strengthens to more solid levels, all on a sustainable basis.

Moody's would consider a rating downgrade, if (1) leverage increased towards 6x Moody's-adjusted debt/EBITDA, (2) Moody's-adjusted FCF turns negative, (3) liquidity deteriorates, all on a sustainable basis.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Aerospace and Defense Industry published in March 2018. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

COMPANY PROFILE

Headquartered in Vicenza, Italy, F-Brasile S.p.A. is an intermediate holding company of the Forgital group ("Forgital"), a leading vertically integrated forging company servicing the commercial and military aerospace industries and select industrial end-markets. The group operates nine facilities in Italy, France and the USA with around 1,200 employees worldwide.

Forgital specialises in forging, laminating and machining of rolled rings and has advanced capabilities across various materials including carbon steels, alloy steels, stainless steels, aluminium, nickel and titanium alloys. The group supplies its products to aerospace (around 65% of 2018 group sales) and various industrial end-markets (35%). In the 12 months ended March 2019, Forgital reported sales of EUR415 million and company-adjusted EBITDA of EUR83.5 million (20% margin).

In May 2019, global investment firm The Carlyle Group (Carlyle) announced the acquisition of Forgital from members of the founding Spezzapria family and a minority stake held by Fondo Italiano d'Investimento.

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