MOODY'S
INVESTORS SERVICE

Rating Action: Moody's assigns B3 CFR to Ideal Standard; outlook negative

20 Jul 2021

Stockholm, July 20, 2021 -- Moody's Investors Service (Moody's) has today assigned a B3 corporate family rating (CFR) and a B3-PD probability of default rating (PDR) to Ideal Standard International S.A. (Ideal Standard). Concurrently, Moody's has assigned a B3 instrument rating to the new €350 million guaranteed senior secured notes due in 2026 and to be issued by Ideal Standard. The outlook on the ratings is negative.

The proceeds from the new notes will be used to fund a shareholder distribution of €272 million, refinance €65 million of existing Bulgarian syndicated loan and cover associated transaction fees and expenses.

RATINGS RATIONALE

Ideal Standard's B3 CFR reflects the company's strong positions in the sanitaryware and fittings market in Europe and the Middle East and North Africa (MENA); broad product offering within its core segments with a number of well-established brands; long-term relationships with its largest customers; and some geographical and end-market diversification. The rating is also supported by the company's significant cost-saving initiatives achieved over the last few years, including the transfer of its manufacturing facilities to lower-cost locations; and the continued focus on improving the company's operations that should support further margin improvements. Finally the rating reflects the liquidity cushion, which Moody's views as adequate, supported by a solid level of cash on balance sheet as of March 2021.

At the same time the rating takes into account the high pro forma leverage of around 10.0x as of March 2021; the aggressive financial policy evidenced by the proposed debt-funded dividend payment; the limited track record of achieving sustained earning growth and a history of negative free cash flow (FCF) generation; and the exposure to raw material price and foreign exchange rate volatility, which poses risks to earnings stability. The rating also reflects the adverse effect of the coronavirus pandemic in 2020; the short-term headwinds from inflationary pressure and some supply shortages; the execution risks associated with the company's cost saving initiatives; the competitive and mature European bathroom and sanitaryware market which limits growth opportunities; and the high degree of customer concentration.

ESG CONSIDERATIONS

Governance risks mainly relate to the company's private-equity ownership, which tends to tolerate a higher level of leverage and risks. Moody's consider Ideal Standard's financial policy to be very aggressive given the size of the debt-funded dividend after a year of material revenue and profitability decline driven by the pandemic. While a large proportion of its transformational initiatives have been completed, the company is still in the restructuring phase, which will require relatively material investments over the next 18 months. The additional interest costs will further strain the company's ability to generate FCF.

LIQUIDITY

Ideal Standard's liquidity is adequate, largely supported by its solid cash on balance sheet of €90 million as of March 2021. However the liquidity position will likely weaken in 2021, given the expected negative FCF, partially driven by restructuring costs and higher working capital release, to support the company's sales growth. Besides the cash availability, the company will have access to an undrawn revolving credit facility (RCF) of €15 million. The RCF contains one springing senior secured net leverage covenant set at 7.0x and tested only when the RCF is drawn by more than 40%. The company benefits from several factoring lines, which are expected to be renewed to support intra-year fluctuations. The company will have no major debt maturing until 2026.

STRUCTURAL CONSIDERATIONS

The B3 rating on the senior secured notes reflects the fact that they represent the majority of the debt in the capital structure given the size of the super senior RCF, MENA and Bulgarian facilities, which are not sufficiently large to allow any notching. The MENA and Bulgarian facilities rank senior to the notes and super senior RCF. Both the notes and the super senior RCF share the same security and guarantees but the notes rank junior to the RCF upon enforcement under the provisions of the intercreditor agreement. Security includes pledges over share pledges, bank accounts, intercompany receivables, and intellectual property. Material subsidiaries, which guarantee the notes, represent at least 80% of the group's consolidated EBITDA. The company's B3-PD PDR is aligned with the CFR, reflecting the use of a 50% family recovery rate, as is typical for transactions that include both bonds and bank debt. Moody's also notes the presence of €1.76 billion of PECs and around €1.2 billion of SHLs as of December 2020 entering the restricted group, which have been treated as equity.

RATING OUTLOOK

Ideal Standard is weakly positioned in the B3 rating category. The negative rating outlook reflects the risks that Moody's adjusted leverage will remain above the 6.5x maximum leverage tolerance for the B3 rating category over the next 12 to 18 months. Moody's also expects FCF to be negative in 2021 and to break even in 2022, which would limit any liquidity improvement that would be essential in mitigating the highly-leveraged capital structure. There is limited headroom for any deviation from our current expectations. A material deterioration of the liquidity profile, or the failure by the company to swiftly reduce its leverage, will strain its rating.

The outlook could however be stabilised if the company demonstrates a clear deleveraging path to 6.5x, with a Moody's adjusted EBIT/interest above 1.0x and the maintenance of an adequate liquidity profile supported by a turnaround of FCF to positive levels over the next 12 to 18 months.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

An upgrade is unlikely in the short term, given the weak rating position of Ideal Standard at the closing of the transaction. Over time, the ratings could be upgraded if the company demonstrates a track record of positive FCF, revenue and earnings growth; Moody's adjusted debt/EBITDA reduces to below 5.0x on a sustained basis; and the liquidity profile is adequate.

Ideal standard's ratings could be downgraded if the company fails to achieve sustained revenue and earnings growth; Moody's adjusted debt/EBITDA remains above 6.5x on a sustained basis; FCF remains negative or the liquidity deteriorates with no signs of improvements.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Consumer Durables Industry published in April 2017 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1060509 . Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

CORPORATE PROFILE

Headquartered in Belgium, Ideal Standard is a manufacturer of sanitaryware and fittings products in Europe and MENA. The company operates under branded names including Ideal Standard, Jado, Porcher, Armitage Shanks, Ceramica Dolomite and Vidima. The company has 10 manufacturing plants in Europe and Egypt. It provides its products to both the residential and commercial markets. In 2020 Ideal Standard employed around 8000 staff and generated €621 million revenues. Since 2018 the company is majority owned by Anchorage Capital Group with 80% of shares and CVC Partners with the remaining 20%.

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 at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

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These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at http://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1288435 .

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 www.moodys.com.

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