



ISSUER RATING

Long-Term

Outlook Positive

Initiation date 29/11/2022
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RATING ACTION AND RATIONALE

- EthiFinance Ratings has reaffirmed at BBB its long-term corporate rating for Prysmian S.P.A. (Prysmian), the Italian manufacturer of electric cables. The group's rating outlook was changed from Stable to Positive.
- The upgrade in the rating outlook is driven by the significant improvement in Prysmian's main credit ratios, particularly in terms of profitability. This is during our forecast period (2023-2025), when compared to the historical data.
- The rating is supported by: i) Prysmian's large scale (#1 global market position) in the fragmented cables manufacturing market; ii) a good geographical diversification, with a material operating presence across two continents (Europe and North America) and some presence in Latam and Apac; iii) the strong growth drivers for cables supported by secular trends related to energy transition, electrification and digitalization; and iv) a solid financial profile, with the group managing to considerably improve its EthiFinance Ratings-adjusted net leverage to 1.5x at YE22 (vs 2.7x at YE21 and 3.5x at YE20).
- Our rating is mainly constrained by i) the tough competition and less buoyant demand in low value-added cyclical activities, such as Trade & Installers and Power Distribution incorporated in the Energy & Infrastructure business, representing 49.5% of Prysmian's EBITDA; and ii) execution risks on large high-voltage projects, as shown with several technical issues encountered a few years ago on the Western Link project.
- In line with our methodology, the capital goods industry has medium-to-high ESG risks (heatmap score between 3.5 and 4) given its impact on the environment. This slightly constrains our industry assessment. Our assessment of the company's ESG policy is advanced (company ESG score between 0 and 1). This weighs positively on our financial assessment, more than offsetting the impact resulting from our industry assessment.

ISSUER DESCRIPTION

Prysmian Group is the world's #1 cable and systems company headquartered in Italy. With a c. 31k workforce and 108 plants worldwide, the group designs, produces, and installs cables for the energy and telecom industries. Prysmian has a global presence and conducts business with many high-profile customers, from national power operators to telecom companies. The group operates through three divisions: 1) Projects (13.4% of revenue and 16.3% EBITDA in FY22), including high-tech and high-value-added businesses, servicing large projects such as offshore wind farms and interconnectors; 2) Energy Products (74.9% of revenue and 65.5% EBITDA in FY22), which manufactures cables for power connection, distribution, and industrial uses; and 3) Telecom (11.7% of revenue and 18.2% EBITDA in FY22), producing cable systems and connectivity products for telecom operators to transmit sound and data.

Over 2022, Prysmian generated consolidated revenue of €16.1bn, with adjusted EBITDA of €1.5bn (9.2% margin), and an EthiFinance Ratings-adjusted net leverage ratio of 1.5x.

FUNDAMENTALS

BUSINESS RISK PROFILE

INDUSTRY RISK ASSESSMENT

- Strong growth drivers for cables supported by secular trends related to energy transition, electrification and digitalization**

Cable is a central part of powering modern lives, transmitting energy from electricity suppliers to households and factories, and data from servers to local drives. As energy transition is accelerating around the globe, infrastructure such as wind farms and charging hubs are being built, further boosting demand for cables. Offshore wind, in particular, requires a significant amount of cables. The need for faster internet speeds stemming from digitalization also increases the use of cables, providing yet another demand driver to the industry. Prysmian has a global impact on natural resource consumption, as it consumes 2- 3% of the world's copper production, and about 7% of the metal used in electrical and electronic sectors.

- Barriers to entry vary between low to medium in the basic cable activity, and are high in the projects segment**

Price can be a key driver for demand for cables that follow industry standards, and therefore competition is high and industrial efficiency an important factor. High-value segments, such as submarine cables,

require advanced technology, cable-laying vessels, know-how, and a good track record of execution for projects over a long period.

- **High cyclicity as demand depends on clients' capex and raw material price volatility**

Demand for cables is reliant on capex, such as telecom operators building optical fibre transmission, and energy suppliers constructing new sites. Therefore, demand can have high cyclicity, as clients may cut spending or suspend new projects in economic slowdowns. The sector also faces frequent, sizable swings in metal (copper, aluminium, and lead) prices, which affect their cost as well as average selling price.

COMPANY'S COMPETITIVE POSITIONING

- **Leading player in several markets**

Prysmian is the largest player in the global cables and systems industry. The group has many high-profile clients ranging from national power operators to telecom companies. As the market leader, Prysmian is well positioned to benefit from global trends of digitalization and energy transition. Thus, it has enjoyed healthy growth (15.3% revenue CAGR from FY17 to FY22) driven by both acquisitions and organic increases in demand. However, the competitive environment weighs on prices for lower value-added and cyclical businesses. This is namely the Energy Infrastructure segment (49.5% of FY22 EBITDA), which is included in the Energy Products division. It produces cables connecting houses to power grids to distribute power within buildings. The execution risks of projects are also material, as evidenced by c. €300m negative impact through FY14 to FY18.

- **Large geographical footprint with broad product range**

The group has strong geographical diversification, albeit with some concentration in EMEA (50.4% of FY22 revenue, of which 9.9% in Italy). It has a significant presence in North America (33.6%) while operating in both Asia (7.6%) and Latam (8.5%). The company is a full-range player, providing various products and services to diverse industries, including telecom, energy, mining, and transportation.

GOVERNANCE

- **Shareholder profile: institutional ownership**

Prysmian's largest shareholders are large asset managers such as BlackRock (7.2%), Credit Agricole (4.8%), and the Vanguard Group (4.7%). According to the company, around 71% of capital is held by investment funds with a medium & long-term investment approach. The group is listed on the Milan Stock Exchange since 2007, with a free float equal to 100% of outstanding shares and a market cap of €10.3bn (at market close on 03, September 2023).

- **Prudent financial policy with an adequate management track record**

We assess Prysmian's financial policy as prudent, aside from the impact of General Cables acquisition in FY18, which resulted in a surge in leverage to above 4x, despite a capital increase. Since this major acquisition Prysmian's net adjusted leverage has improved to 1.5x as of end-2022. Valerio Battista has been Prysmian's CEO since 2005 when the group was formed as a spin-off of Pirelli's cables activity. Since FY17, revenue has more than doubled, thanks to organic growth and to a greater extent M&A activities, in particular the acquisition of General Cable in 2018 for c. \$3bn. Despite material acquisitions, the group managed to continue improving its profitability, with the adjusted EBITDA margin increasing from 8.0% in FY19 to 9.2% in FY22, representing a 17% CAGR in EBITDA.

- **Strong ESG policy dedicated to reducing emissions but with some controversies**

Prysmian introduced new ESG guidelines in 2021 that are to guide the group's actions over the medium-to-long term. It wants to invest in low-carbon production technologies and targets becoming carbon-neutral between 2035 and 2040 for its scope 1 and 2. Also, the group aims to continue to invest in its workforce to improve diversity, equality, community empowerment, and employee training. However, Prysmian has been the subject of multiple accusations about price cartels and has been fined at least €104m by the authorities since 2014. In January 2022, the German Federal Cartel Office (FCO) carried out inspections at some of Prysmian's facilities due to "alleged coordination in setting the standard metal surcharges applied by the industry in Germany", to which the company indicated that it was co-operating. At YE22, it had €179m of provisions for antitrust investigations, and related matters. These controversies have not yet impacted the rating.

FINANCIAL RISK PROFILE**CASHFLOW AND LEVERAGE**

- **Strong growth on the back of a strong order book**

Despite a challenging macroeconomic environment in 2022, the group delivered record figures in terms of revenues and EBITDA. Order intake was solid in the Projects segment, with €3.4bn of projects awarded in 2022. This led to a record order backlog of €6.6bn at end-2022 (vs €4.4bn at end-2021). It reported sales of €16.1bn in FY22, representing a 26.2% increase versus FY21 of this growth 14.4% was organic, 6.6% due to a positive FX effect, 4.6% from sales price increases due to favourable fluctuation in price of metals, and 0.6% from M&A. All business areas reported growth; with the segments exposed to energy transition, electrification and digitalisation trends delivering the best performances. Thus, by segment, Projects registered the highest revenue growth at +35.6% yoy (30.3% yoy organically), followed by Energy Products at +25.9% yoy (12.3% yoy organically) and Telecom at +18.2% yoy (+10.9% yoy organically). For FY23, we expect revenues to remain relatively stable at €16.1bn, as strong revenue growth for Projects (organic growth of +23.5% yoy in 1H23) should be offset by the negative performance of the Telecom (as already observed in 1H23 with an organic growth of -5.2% yoy). This is mainly due to the slowdown in volumes for optical cable & fibre in the US market, as well as the decline in the construction market for multimedia specials (MMS). After that, we have assumed revenue growth of around 1% yoy for FY24 and FY25.

In terms of profitability, adjusted EBITDA for FY22 increased by 54.7% yoy to €1.5bn in FY22 (vs €955m in FY21), with a significant improvement in EBITDA margin to 9.2% (vs 7.5% in FY21). Despite significant increases in raw material prices, Prysmian's margin did not suffer. This is since it managed to increase prices to the point that it overcompensated for the loss in material costs, particularly in Energy Products. The higher profitability in Telecom, which delivered a record 14.5% EBITDA margin (vs 13.9% in FY21), and Energy Products, with an 8.1% EBITDA margin (vs 5.7% in FY21) compensated for the impact of cost increases affecting the Projects segment, with a 11.2% EBITDA margin (vs 13.2% in FY21).

For FY23, we expect the adjusted EBITDA margin to increase to around 10%, mainly as: i) the Projects segment continues to benefit from a favourable mix of high-value projects, with the company targeting for a c. 12% EBITDA margin for the segment in FY23; ii) demand for Power Distribution and Renewables cables remains strong and enables the group to benefit from structural price gains, supporting the Energy & Infrastructure profitability; and iii) the Telecom segment EBITDA margin remains relatively stable at 14.3%, a very good level, as the group continues to pass cost increases to its clients. After that, we expect the group's EBITDA margin to remain fairly stable at around 9% for 2024 and 2025.

Altogether, Prysmian generated an adjusted free cash flow (after dividends) of €300m in FY22 (vs €258m in FY21). This was driven by the strong operating performance, partially offset by a higher CapEx (€454m vs €283m in FY21). This was in addition to a working capital cash outflow of €105m (vs €28m in FY21), caused by higher inventories due to non-metal raw material inflation, and a higher dividend payment (€145m vs €132m in FY21). For 2023, we project the group's adjusted free cash flow (after dividends) to decrease to €203m (vs €300m in FY22). This is as the solid cash flow from operations is partially offset by higher capital expenditure (management expects around €500m yearly CapEx in 2023-2025 period). This is in addition to a higher working capital cash outflow of €166m, still negatively impacted by higher stocks due to inflation, and a higher dividend payment (€158m vs €145m in FY22). For the remainder of our forecast period, we expect the group's adjusted free cash flow (after dividends) to remain relatively stable at around €190m FY24 and FY25, respectively. This should be supported by solid cash generation from operations and normalization of working capital. capital expenditure should remain high. We note that Prysmian's dividend policy remains unchanged, and we expect the group's dividend pay-out ratio to remain at around 30% in our forecast period.

At YE22, Prysmian's adjusted liquidity position remained solid at around €1.5bn, including €1.3bn of cash in hand and €193m of money market funds (maturing within one year). We include these in our adjusted net debt calculation. In addition, the group had an undrawn €1bn revolving credit facility at end-2022. All in all, we calculate the group's EthiFinance Ratings-adjusted net leverage ratio at 1.5x end-2022 (vs 2.7x at end-2021), confirming the group's good financial profile.

SOLVENCY AND LIQUIDITY PROFILE

- **Solid solvency ratio at end-2022**

Total adjusted debt amounted to €3.7bn at end-2022, including adjustments related to employee benefits (€329m), the equity component of the €750m convertible bond (€32m), and factoring (€296m). Around 67% of Prysmian's gross debt relates to bank facilities, with several term loans. The rest is mostly related to the €750m convertible bond, which has a conversion price of €40.2 (vs share price of €37.3 at close on September 3, 2023) as well as €214m of IFRS 16 lease liabilities.

The group's solvency ratio stood at 100.4% at end-2022, and we expect this ratio to further improve during our forecast period.

We note that Prysmian has to comply with the following financial covenants under the RCF, the CDP, EBI, Unicredit, Mediobanca, Intesa loans, tested every 6 months (June and December) on an LTM basis:

- * Leverage (net financial position/EBITDA): Maximum 3.0x (tested at 0.83x at end-2022).
- * Interest coverage (EBITDA/net finance costs): Minimum 4.0x (tested at 27.26x at end-2022).

Note that the credit agreement allows leverage to go as high as 3.5x up to three times, following extraordinary transactions like acquisitions.

- **Excellent liquidity profile with strong refinancing capacities**

We assess the liquidity profile of Prysmian as "Adequate" (the best of the three profiles according to our long-term methodology), reflecting the company's strong refinancing profile and high liquidity level.

MODIFIERS

Controversy

- Not applicable

Liquidity

- Not applicable

Country Risk

- Not applicable

MAIN FINANCIAL FIGURES AND FORECASTS

Main financial figures. Millions of €.						
	2021	2022	2023E	2024E	2025E	22vs21
Revenues	12 736	16 067	16 086	16 247	16 409	26,2%
EBITDA	955	1 477	1 575	1 430	1 444	54,7%
EBITDA Margin	7,5%	9,2%	9,8%	8,8%	8,8%	1,7pp
EBIT	620	1 074	1 173	1 025	1 035	73,2%
EBIT Margin	4,9%	6,7%	7,3%	6,3%	6,3%	1,8pp
EBT	539	1 001	1 066	910	918	85,7%
Total Assets	12 016	12 756	13 628	13 180	13 200	6,2%
Equity	3 046	3 739	4 033	4 016	4 080	22,8%
Total Financial Debt	4 522	3 724	3 717	3 259	3 187	-17,6%
Net Financial Debt	2 620	2 246	2 060	2 296	2 535	-14,3%
Equity/TFD	67,4%	100,4%	108,5%	123,2%	128,0%	33,0pp
NFD/EBITDA	2,7x	1,5x	1,3x	1,6x	1,8x	-1,2x
Funds From Operations	752	1 068	1 133	1 019	1 027	42,0%
FFO/NFD	28,7%	47,6%	55,0%	44,4%	40,5%	18,8pp
EBITDA/Interest	11,8x	20,2x	14,6x	12,5x	12,3x	8,4x

RATING SCORECARD

Credit Rating	
Business Risk Profile	BB+
<i>Industry Risk Assessment</i>	<i>BB-</i>
<i>Industry ESG Assessment</i>	<i>Negative</i>
<i>Competitive Positioning</i>	<i>BBB</i>
<i>Governance</i>	<i>BBB+</i>
Financial Risk Profile	A-
<i>Cash flow and leverage</i>	<i>A-</i>
<i>Solvency</i>	<i>BBB</i>
<i>Company's ESG Assessment</i>	<i>Positive</i>
Anchor Rating	BBB
<i>Modifiers</i>	<i>-</i>
Rating	BBB

RATING SENSITIVITY

- **LT rating: BBB**

Factors that may (individually or collectively) impact the ratings:

- **Long-term rating positive factors (↑)**

A rating upgrade could be possible with a sustained improvement in Prysmian's financial profile. For the same business risk profile, an increase in the group's EthiFinance Ratings-adjusted net leverage ratio to below 1.3x, for a sustained period of time, could entail a long-term rating upgrade to BBB+.

- **Long-term rating negative factors (↓)**

A rating downgrade could result from a sustained deterioration in Prysmian's financial profile. This could be a consequence of a more aggressive financial policy, particularly in the event of a transformative debt-funded acquisition. For the same business risk profile, an increase in the group's EthiFinance Ratings-adjusted net leverage ratio to above 3.0x, for a sustained period of time, could lead to a long-term rating downgrade to BBB-.

RATING DISCLOSURES

LEI: 529900X0H1IO3RS1A464

Initiation report: No

Rating initiation: BBB for long-term rating on 29 November 2022.

Latest rating action: Initiation of long-term rating at BBB on 29 November 2022.

Rating nature: Unsolicited (this report is paid by investors, not the issuer).

With rated entity or related third party participation: No, the report was published without having been reviewed by the issuer

With access to internal documents: No

With access to management: No

Ancillary services provided to the entity: In accordance with Article 6 (2), in conjunction with Annex I, section B (4) of the Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009, it is reported that during the last 12 months EthiFinance Ratings has not provided ancillary services to the rated entity or its related third parties.

Name of the rating committee chair: Thomas Dilasser, Head of Corporate Ratings France

Material sources used to support the rating decision:

- Annual report (2020, 2021, 2022)
- Quarterly reports, presentation slides and conference call
- Bloomberg

Limitation of the Rating action:

EthiFinance Ratings believes the quality and quantity of information available on the rated entity is sufficient to provide a rating.

EthiFinance Ratings has no obligation to audit or verify the accuracy of data provided.

Principal methodology used in this research available at:

https://files.qivalio.net/documents/methodologies/CRA_190_V3.CorporateRatingMethodology_Long_Term.pdf

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