A-	ISSUER RATING Long-Term
Outlook	Stable
EF1	ISSUER RATING Short-Term
Initiation date	29/11/2022
Rating date	26/06/2023

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RATING ACTION AND RATIONALE

- EthiFinance Ratings has reaffirmed its long-term corporate rating of A- for Compagnie Générale des Etablissements Michelin SCA, the ultimate holding company of Michelin Group, with a Stable outlook. EthiFinance Ratings has also reaffirmed its short-term rating of EF1.
- These ratings are in line with the consistent financial performance that the company has demonstrated throughout the past year. A revenue growth of 20.2% was achieved driven by the strong price-mix effect and effective cost pass-throughs mechanisms, which mitigated the impact of a 2% decline in sales volume relative to the prior financial year. A foreign exchange tailwind has also contributed 6.2% to the overall growth. Consequently, Michelin has reinforced its robust market position as a mass-market leader amidst a slight downturn in demand for the standard <17" tyre segment. Michelin's strategic expansion around and beyond the tyre industry is a key driver for future organic growth, facilitated in part by its subsidiaries such as BEV premium tyre segment and the hydrogen systems specialist SYMBIO. Michelin has maintained a steady EthiFinance Ratings-adjusted net leverage ratio of 1.3x, a testament to its measured leverage profile and adherence to sound financial policies. Our projections suggest that this ratio is poised to remain stable by 2025.
- However, our ratings are constrained by our industry assessment as well as by significant M&A expected in the years ahead, which will therefore limit the potential improvement in credit metrics.
- In line with our updated methodology, the "auto components" industry has medium-to-high ESG risks (heatmap score of between 3.5 and 4) given its impact on the environment, which slightly constrains our industry assessment. Meanwhile, our assessment of the company's ESG policy is advanced (company ESG score of between 0 and 1), which weighs positively on our financial assessment and therefore more than offsets the impact resulting from our industry assessment.

ISSUER DESCRIPTION

Headquartered in France, Michelin is a first-rank French automotive supplier specializing in tyres. Within its three divisions, Michelin designs, manufactures, and sells tyres for vehicles such as cars, trucks, aircraft, off-road machines, motorbikes, and bicycles. The group possesses not only the premium Michelin brand, which many car owners choose for its reputation, quality, and durability, but also a set of cheaper brands (tier-2) such as Kleber and BFGoodrich. Michelin is also active in data-enabled services to fleets, polymer-based high-tech materials, and develops new disruptive projects in the hydrogen power field through its joint venture (JV) with Faurecia and Stellantis (SYMBIO). The group has 125,000 employees spread across 123 factories and 9 R&D centres in 26 countries; its products are sold in 170 countries. For FY22, Michelin reported revenues of €28.6bn and EBITDA of €5.3bn, equivalent to an 18% margin. Michelin's market capitalisation was €19.11 bn as of June 20, 2023.

FUNDAMENTALS

BUSINESS RISK PROFILE

INDUSTRY RISK ASSESSMENT

- **Tyre market outlook: opportunities and challenges amidst the automotive industry's shift to electrification, and supply chain disruptions**

The automotive industry has been shaken for the past two-and-a-half years. The period started with the Covid lockdowns, which halted production lines. Then, the industry was hit by the shortage of electronic components that began in 2021 and persisted into early 2022. More recently, the rise in raw material costs in 2H22 as a result of the macro-environment added to the challenges. For 2022, the global automotive tyre market recorded a 1.7 % drop in volumes mainly due to a lower demand in the aftermarket segment. However, the original equipment market has offset some of this decrease and the industry key players such as Pirelli and Michelin were forced to counter-balance the inflation impact on raw materials costs by passing it on to end-customers. The auto components industry has also been involved in a shift from conventional thermal engines to electrification for a few years now as electric vehicle registrations in Europe increased by 15% from 2021 to 2022 (EV-Volumes.com), a trend we expect to continue in the years ahead. Electrification represents a sound growth potential for the tyre industry as tyres will need to be adapted to EV's characteristics (higher load index, energy consumption and noise reduction).

- **Challenges and barriers to entry in the competitive tyre market**

The tyre market is highly competitive by nature and we believe that the significant capital investments required along with the ability for traditional tyre players to diversify their product range will continue to weigh on margins going forward. That will also constitute rather strong barriers to entry as not all competitors nor new entrants will be able to deal with the burden of high capex in a context of limited margin increase and volatile demand.

- **The shift towards eco-friendly materials to meet consumer demand while reducing environmental impact**

Tyre making is an essential part of the automotive industry, but the manufacturing process requires the use of significant amounts of energy, water, and raw materials, such as natural rubber, synthetic rubber, and carbon black. However, the car-making ecosystem (manufacturers and customers) is leaning towards the use of sustainable raw materials over traditional ones especially when considering the tyres disposal process. Consequently, the integration of innovative operational means becomes imperative to facilitate the production of increasingly environmentally friendly and easily disposable tyres.

COMPANY'S COMPETITIVE POSITIONING

- **A Leading player in the global tyres market**

Michelin is one of the largest tyre makers in the world, with a c. 14% market share. It runs neck-and-neck with its closest competitor, Japan's Bridgestone, for outright leadership of the tyre market. Michelin's growth is driven by both organic and external growth since the group has undertaken over 50 acquisitions during the past 10 years, reinforcing the company's market positioning.

- **Great diversification with a wide range of offerings**

Michelin offers a wide range of products, from different sizes of car tyres to mining tractors tyres. The company is also present in the aerospace industry and the industrial sector by selling aircraft tyres and producing conveyor belts. In the long run, Michelin will be targeting growing, high value-added market segments, such as the premium segment for its automotive business and specialty markets. The group is also renowned for having a strong global presence, with its products being sold in 170 countries and production sites spread over 26 countries. Michelin's revenues are mainly generated in the EU and the US, accounting respectively for c. 36% and 38% of FY22 revenues.

- **A well positioning for beyond-tyre activities**

We remain confident in Michelin's ability to convert its innovative capacity and solid expansion strategy into a growing market share, not only in the tyre business but also in high-tech materials and new energy solutions such as electric and hydrogen power. The group has indeed reaffirmed its ambition to derive between 20% and 30% of revenues from non-tyre businesses by the end of the decade. The ongoing acquisition of Flex Composite Group (announced in June 2023) is only one milestone in a €5-10bn acquisition program envisaged over the decade. Michelin has recently affirmed that Symbio will start supplying French car manufacturer Stellantis with fuel cell systems from 2Q23. The yet-to-be completed gigafactory located in St-Fons (France) will produce the fuel cell systems with an initial annual capacity of 15k units and a target to reach of 100k by 2028. In addition, the demand for low rolling resistance tyres is being driven by environmental legislation that requires car and truck manufacturers to reduce carbon emissions. Michelin is a world-leading manufacturer of such tyres.

GOVERNANCE

- **Shareholder profile: family fund as one of the top shareholders**

Michelin's top shareholders mainly comprise large asset managers such as Blackrock, Aristotle Capital Management, and Vanguard, to name a few. Mage Invest, the holding company of the Michelin family, is still a shareholder (c.4%) behind the main asset managers. Compagnie Générale des Etablissements Michelin is a 'société en commandites par actions' (SCA) which is a specific French type of company through which the 'commandités' (general partners) control the company and manage it while having unlimited joint and personal liability for the company's debts. In Michelin's case, Florent Menegaux is the managing general partner ('gérant'). Meanwhile, the company SAGES, represented by Vincent Montagne, heir of Edouard Michelin, is a non-managing general partner who is in charge of ensuring good governance over the group and the nomination of qualified managers, respectful of Michelin's values.

- **Management quality: prudent financial policy with a good track record**

Michelin's management has a very good track record of maintaining stable margins under its M&A strategy mainly financed with the company's FCF. We assess the management team's financial policy as prudent given Michelin's robust financial profile, excellent liquidity profile, and a stable EthiFinance Ratings-adjusted net leverage ratio below 2.0x.

- **ESG policy: committed to reduce emissions**

Michelin's ESG score has improved as the group has committed to a significant reduction of CO_2 emissions and energy consumption: it has reduced by 17% its scope 1 and 2 emissions compared to 2021. Compared to 2010 as a base year, it has succeeded to reduce 41% of its CO_2 emissions and expects a 50% overall reduction by 2030 and, in fine, to be fully carbon-neutral by 2050. It has also committed to using more sustainable raw materials and increasing tyre recycling processes with the objective of reaching 100%-recycled tyres by 2050, which we do view as a rather distant time horizon.

FINANCIAL RISK PROFILE

CASHFLOW AND LEVERAGE

- **Medium-term growth constrained by low standard segment volumes**

Michelin reported total sales of €28.6bn in FY22, representing 20.2% growth vs. FY21. The increase was mainly due to some mix effect along with price increase (c.+13.7%), as many of Michelin's price tags are indexed to raw materials prices. Volumes decreased by c.2% due to the direct and indirect impacts of the geopolitical crisis in Ukraine (exit of the Russian operations, supply chain issues) and the lockdown in China that occurred in 2Q22. Yearly growth was supported however by a favourable FX tailwind of c.+6.2% attributable to the strengthening of the US dollar. In our forecasts, we have assumed that sales will be still impacted by flattish volumes in 2023. As a consequence, we anticipate Michelin to achieve 1.2% sales growth in FY23 followed by an increase of around 5.2% for FY24 and 4.5% for FY25, on the back of car production and related aftersales growth, including the impact of newly-acquired businesses.

The group reported EBITDA of €5.3bn in FY22 vs. €4.7bn in FY21, giving a margin of 18.4% vs. 19.8% in FY21, a contraction of c.140bps. The slight drop in EBITDA margin resulted from rising COGS as they increased by €4.2bn in 2022 (double the increase in 2021, whereas revenues only increased by c.20% at the same time). Assuming an ongoing cost inflation in raw materials, energy and labour, we expect the 2023 reported EBITDA margin to slightly deteriorate to 18% before gradually improving again in 2024 (18.2%) and 2025 (18.4%), still far from the 19.8% reported in 2021.

Adjusted free cash flow (excluding M&A) for 2022 was a negative €1.1bn, significantly hampered by a €2.1 bn change in working capital (+€1.2bn compared to 2021), resulting from the impact of inflation on inventory. Given its ability to contain the effects of inflation, we expect Michelin's adjusted FCF to return to a positive level as of 2023, before settling around c.€0.5bn for 2024 and 2025.

- **Solid financial profile**

Our ratings are supported by Michelin's solid financial profile. The EthiFinance-Ratings adjusted net leverage ratio was unchanged (1.3x) at end-2022. and is expected to slightly improve by 2025 (1.2x expected). The interest coverage ratio was at 21.3x for 2022 lower than the previous year's ratio of 23.4x, due to a higher interest rate-environment. This is expected to weigh on the coverage ratio for the next two years (2023 and 2024). For 2025, we could see an improvement of the interest coverage ratio on the back of debt reduction.

SOLVENCY AND LIQUIDITY PROFILE

- **Very good solvency ratio**

As of end-2022, Michelin's gross reported debt stood at €7.5bn, slightly down from €8.0bn at end-2021. Our debt adjustments amounted to €2.3bn (vs €3bn in FY21), the major part being employee benefits. Net adjusted debt stood at €6.6bn at end-2022, to be compared with €5.9bn one year before, mainly due to a deteriorated level of cash stemming from the inflated working capital as highlighted in the FCF analysis. The group's solvency ratio stood at 176.3% at end-2022, broadly in line with its peers within the industry, and is expected to improve over our forecast period.

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

We assess Michelin's liquidity profile to be 'Superior' as the company can repay all its upcoming debt without refinancing for more than two years.

MODIFIERS

- **Controversies**

Over the course of our review, we found no significant controversies for Michelin.

- **Country risk**

Michelin is well diversified geographically and does not have specific country risk exposure.

MAIN FINANCIAL FIGURES AND FORECASTS

Main financial figures. €m	2021	2022	2023E	2024E	2025E	22vs21
Turnover	23,795	28,590	28,946	30,452	31,808	*20.2%*
EBITDA (Adjusted) (1)	4,486	5,081	5,106	5,438	5,749	*13.3%*
EBITDA Margin	18.9%	17.8%	17.6%	17.9%	18.1%	*1.1pp*
EBIT	2,752	3,215	3,217	3,451	3,673	*16.8%*
EBIT Margin	11.6%	11.2%	11.1%	11.3%	11.5%	*-0.4pp*
Interest expenses	(192)	(239)	(248)	(263)	(241)	*24.5%*
EBT	2,560	2,976	2,969	3,188	3,431	*16.3%*
Total Assets	34,701	35,346	35,852	36,850	37,488	*1.9%*
Equity (Adjusted)	14,965	17,116	18,308	19,441	20,675	*14.4%*
Total Financial Debt (2)	11,066	9,711	8,982	8,668	7,909	*-12.2%*
Net Financial Debt (2)	5,927	6,634	6,683	6,779	6,748	*11.9%*
Equity/TFD (2)	135.2%	176.3%	203.8%	224.3%	261.4%	*41.0pp*
NFD/EBITDA (2)	1.3x	1.3x	1.3x	1.2x	1.2x	*0.0x*
Funds From Operations	3,730	4,007	4,150	4,414	4,686	*7.4%*
FFO/NFD	62.9%	60.4%	62.1%	65.1%	69.5%	*-2.5pp*
EBITDA/Interest (1)	23.4x	21.3x	20.6x	20.7x	23.8x	*-2.1x*

(1) EBITDA is mainly adjusted for recurring restructuring costs

(2) Net debt adjustments : Pension benefits and a portion of financial assets are included in net debt.

RATING SNAPSHOT

CREDIT RATING	
Business Risk Profile	**BBB**
Industry Risk Assessment	BB+
Competitive Positioning	A-
Governance	A-
Industry 's ESG	***Negative***
Financial Risk Profile	**A+**
Cash flow and leverage	A+
Solvency	A
Company's ESG	*Positive*
Anchor Rating	**A-**
Modifiers	-
Final Rating	**A-**

CREDIT METRICS EXPECTED EVOLUTION (CMEE)

- **Stable CMEE although affected by upcoming debt refinancing**

We expect Michelin's credit metrics to remain steady and broadly unchanged over the next twelve months - as automotive production grows along with aftermarket volumes - despite the recent M&A activity.

RATING SENSITIVITY

- **List of ratings:**
  - **LT Rating: A-**
  - **ST Rating: EF1**

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

We could upgrade the current rating should credit metrics improve above our forecasts level. A trigger for such an upgrade could be an EthiFinance Ratings-adjusted net leverage ratio below 1.0x on a sustainable basis and a solvency ratio exceeding 250%. Moreover, any rating upgrade would be contingent upon the tyre industry's overall stability, which hinges on the global automotive production outlook.

An upgrade of the short-term rating is contingent upon a long-term rating upgrade with a stable CMEE.

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

We could downgrade our long-term rating should Michelin's credit metrics deteriorate (EthiFinance Ratings adjusted net leverage ratio > 2.0x) or if the interest coverage ratio falls below 15.0x. Additionally, a less cautious financial strategy pursued by the company, such as undergoing debt-financed M&A, could constitute another catalyst for a potential rating downgrade.

A downgrade of our short-term rating is less likely to occur in the near future. It could happen in the event of a severe economic downturn leading to several downgrades of the long-term rating.

REGULATORY INFORMATION

LEI: 549300SOSI58J6VIW052

Initiation report: No

Rating initiation: 25 November 2022 at A- and EF1

Last rating action: Initiated at A- and EF1 on November 25, 2022

Rating nature: Unsolicited long-term and short-term corporate ratings (this report is paid for by investors, not the issuer)

With rated entity or related third party participation: Yes - The report was published after having been reviewed by the issuer.

With access to internal documents: No

With access to management: No

Ancillary services with the rated 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 provided ancillary services to related third parties of the rated entity, but not to the rated entity. However, according to our Conflict-of-Interest Policy, it does not involve a conflict of interest, since the aggregate sale does not exceed 5% of net turnover.

Name of the rating committee chair: Marc PIERRON, Senior Director

Material sources used to support the rating decision:

- Annual reports 2020, 2021,2022
- Half-year reports 2020, 2021, 2022
- Investor presentations and press releases 1H20, FY20, 1H21, 2021, 1H22, FY22

Limitation of the Rating action:

- EthiFinance Ratings believes that the quality and quantity of information available on the rated entity is sufficient to provide a rating
- EthiFinance Ratings has no obligation to audit the data provided

Methodology used for these ratings:

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

https://files.ethifinance.com/documents/methodologies/CRA_191.Corporate_Rating_Methodology_Short_Term.pdf

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