EthiFinance Ratings

SONEPAR SAS

585580202

CORPORATE

EF1+

INSTRUMENT RATING
Neu CP

Initiation date 28/11/2022
Rating Date 17/09/2024

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RATING ACTION AND RATIONALE

- EthiFinance Ratings affirms Sonepar's short-term rating for the NEU CP instrument (of up to €1.5bn) at EF1+
- The rating remains underpinned by the confirmed strong business profile of Sonepar, the world's largest B2B distributor of electrical products, solutions and services, and its global presence, with a strong local footprint and distribution network, as well as a diversified product offering and limited customer concentration. Moreover, Sonepar has an excellent financial profile with solid cash flow generation and an EthiFinance Ratings-adjusted net leverage ratio of 1.1x at end-2023. We expect this ratio to remain around 1.2x over our forecast period (until 2026).
- However, the rating is constrained by the industry risk assessment that derives from the group's exposure to the construction and renovation end-markets for residential and commercial buildings, which are subject to some degree of cyclicality.
- Under our methodology, the retailing industry has medium ESG risks (sector heatmap score between 3 and 3.5). This results in a sector assessment which is not impacted by industry-related considerations. Regarding environmental factors, the sector has a low impact on climate issues, except for logistics, and on biodiversity. The industry has a medium impact on resources linked to the distribution means and on pollution with significant packaging issues. In addition, it presents a high impact via suppliers given the concentration in the sector, which can weaken bargaining power.
- Our assessment of the company's ESG policy is favourable (company ESG score of between 1 and 1.5), resulting in a half-notch upgrade of the financial risk profile. Sonepar stands out in terms of governance with the separation of the roles of chairman and CEO, and the prioritization of ESG issues. Regarding environmental considerations, it also stands out with a reduction of its water and energy consumption. However, the social assessment is weakened by the unfavourable three-year trend regarding turnover and absenteeism rates.

ISSUER DESCRIPTION

Family-owned Sonepar is the world's largest B2B distributor of electrical products, solutions, and related services. The group's product offering (generally marketed under the manufacturers' brands) includes the following main segments: i) Infrastructure & Industrial Automation (37% of 2023 sales), which includes equipment for coupling and circuit protection, energy conversion and storage, sensors, actuators and consumption devices; ii) Cables & Wires (18%), including raceways, mouldings and cable trays; iii) Lighting (12%): lighting sources, interior & exterior lighting systems; and iv) Building Automation & Construction (9%), where products are essentially designed for the utilities industry. The majority of customers are installers (61% of sales in FY23), which act as intermediaries to end-users. They are usually construction firms in the residential and commercial building markets or specialist installers. Other customers are end-users in various industries (including parts manufacturers, public facilities and infrastructure), sourcing their products directly from Sonepar. The group has a presence across 42 countries with around 2.4k branches, 182 distribution centres, and 45.6k employees at end-2023.

Over 2023, Sonepar generated €33.3bn of revenues, with EthiFinance Ratings-adjusted EBITDA of €2.8bn, equivalent to an 8.4% margin, and a net adjusted leverage ratio of 1.1x.

FUNDAMENTALS

Business risk profile

Industry risk assessment

- **Long-term growth drivers supported by rising energy needs and demand for electrical appliances**

The industry is anticipating positive long-term trends on the back of rising energy needs and demand for electrical appliances. This points towards further growth in all regions where the group is present, including in emerging markets where B2B electrical product distribution has had a low penetration rate so far. We expect Sonepar to benefit from these trends, especially in fragmented markets where the group is already present and well positioned to drive market consolidation.

- **Exposure to residential and commercial buildings end-markets comes with a certain cyclicality**

Sonepar's sales are subject to some degree of cyclicality due to the group's exposure to the construction and renovation end-markets for residential and commercial buildings.

- **Significant size and CapEx required are effective barriers to entry**

The barriers to entry have been relatively low but are rising significantly due to the CapEx required in the fields of digitalization & logistics, which small players cannot afford. Size is an important factor allowing stronger bargaining power vis a vis suppliers, better absorption of fixed costs, and the capacity to deploy large CapEx. These factors all lead to good price positioning, and superior services for customers.

Company's competitive positioning

- **World's largest B2B distributor of electrical products, solutions and services**

Sonepar benefits from its large scale, operating in four continents, with the bulk of sales being generated in Europe and North America (together contributing to c. 92% of 2023 revenues), where the group continues to focus its M&A activity to consolidate its leading market positions.

Sonepar has gone a long way to digitalizing its operations - and on this front the group is ahead of peers, which is expected to bring further efficiency gains and support margins. In 2023, digital sales accounted for c. 33% of total revenues (vs c. 28% reported by Rexel, its main competitor). These include online sales (web and mobile) and "system to system" sales. This is a key factor, as intense competition results in low operating margins, making scale a major driver for profitability.

- **Sonepar has historically outperformed its direct competitors**

Sonepar has displayed resilience both in terms of operating margins and cash generation during past economic downturns, outperforming its main peers over the past few years. It has consistently achieved a high level of free cash flow, a positive factor that we expect to continue over the medium term.

- **Global presence with a diversified product portfolio and limited customer concentration**

The rating of Sonepar is supported by its strong local footprint and distribution network, which is reflected in the high numbers of branches (c. 2.4k) and distribution centers (182) operated by Sonepar globally.

The group benefits from a diversified product offering across various segments. It has been recently focusing on developing its renewable energy product range, which generated sales of €2.2bn in FY23 (c. 7% of total sales vs c. 5% in FY22).

Customer concentration is limited. The top 10 clients for each key country represent only a modest share of that country's sales (around 5-15%). Concentration could be more important for segments which serve specific industries, but these activities have limited scope.

Governance

- **Shareholders**

The group was founded in 1969 by Henri Coisne and his brothers. Sonepar is still a family group largely owned by the founding families (Coisne & Lambert) via the holding company Colam Entreprendre as well as other vehicles, bringing together around 500 shareholders from the two legacy families. The remaining capital was held by employees and management at end-2023. Some members of the family are present in the Corporate Board.

- **Prudent financial policy with an excellent track record**

The group has an excellent track record for growth combined with a prudent financial strategy. The group's EBIT has almost tripled from 2016 to 2023 while our net adjusted leverage ratio has gradually decreased from 2.5x to 1.1x. The financial policy involves (i) a reasonable level of indebtedness with a net reported leverage below 2.5x historically, and (ii) limited shareholder distributions as most earnings are reinvested to support growth.

M&A is a key component of Sonepar's development strategy, with the group completing 200 acquisitions over the past twenty years, representing more than €10bn of sales and around 60% of total revenue growth during that period. In 2023, Sonepar made 13 acquisitions totalling €1bn of turnover, incorporating both generalist and specialist companies mostly in Europe and North America. We are reassured by Sonepar's solid track record for integrating acquired companies while adhering to its disciplined financial policy. This has been facilitated by its policy to involve local management in the acquisition and integration processes.

- **ESG policy**

Sonepar's ESG strategy is centered on three core pillars. First, helping customers reduce their impact, mainly through the launch of its "Green Offer". This consists of a methodology and environmental label enabling customers to measure the ecological footprint of products, helping them choose the most sustainable ones. Second, training all its associates, through its Energy Transition Academy, to promote best practices and be prepared to properly advise customers. Third, reducing its environmental footprint. In that regard, Sonepar has committed via SBTi-validated targets to reduce, by 2030, its scope 1 and 2 emissions (buildings and fleet) by 46.2% (-8.6% in 2023 vs 2019 baseline). In addition, it aims to reduce its scope 3 emissions from purchase, use, end of life, and transportation of products from suppliers to Sonepar's customers by 13.5% (-14.9% in 2023 vs 2019 baseline).

Financial risk profile

Results and profitability

After a very strong FY22, Sonepar posted growth in revenues of 2.7% yoy to €33.3bn in 2023. Electrical sales increased by 5.4% yoy to €33.1bn, of which 0.2% was related to higher volume growth, 3.0% to price inflation, and 4.3% to M&A activity, partially offset by a 1.7% negative FX impact. Overall, the group reported solid revenues growth in Western Europe (6.7% yoy), Central Europe & Nordics (3.6% yoy), and South America (15.2% yoy), while revenues remained relatively flat in North America and decreased in Asia-Pacific (by 2.4% yoy).

In terms of profitability, EthiFinance Ratings-adjusted EBITDA decreased by 6.7% to c. €2.8bn, equivalent to a margin of 8.4% (vs 9.2% in FY22 and 8.4% in FY21), returning to more normalized levels. The group has managed to mitigate the impacts of inflationary pressures on profitability, mainly by passing input cost increases on to customers, as well as through cost reductions, which are also a result of its investment efforts in supply chain automatization and developing its digital platform.

Cash flow and leverage

Over 2023, Sonepar generated €296m in free cash flow (after M&A, before dividends), mainly driven by strong cash generation from operations, which compensated for significant CapEx of €412m, crucial to the modernization and automation of its supply chain, and higher net cash paid for M&A (€791m in 2023 vs €150m in 2022).

Sonepar has low leverage with an EthiFinance Rating's net adjusted debt/EBITDA ratio of 1.1x at YE23 (vs 0.9x at YE22), which included IFRS 16 lease liabilities. We expect our adjusted leverage ratio to remain around 1.2x going forward, despite sizable acquisition expenditure expected over our forecast period.

Capitalisation

As of end-2023, Sonepar's consolidated gross debt amounted to €3.8bn, mostly related to private placements (€1.1bn at end-2023), on-balance sheet factoring in France (€155m), securitization programs in Germany, Austria and the Netherlands (around €652m drawn at end-2023), and commercial paper (€365m outstanding at end-2023). The remaining debt mostly consisted of IFRS 16 lease liabilities. Our adjusted gross debt amounted to €4.4bn, and included adjustments related to the company's pensions obligations (€260m at end-2023) as well as other financial liabilities (€319m at end-2023), primarily consisting of payables on company acquisitions and put options granted to non-controlling interests. Nearly all financing, mostly denominated in EUR and USD, has been raised at the level of the parent company Sonepar S.A.S. Additionally, at end-2023 the group had access to €2.1bn of undrawn committed, sustainability-linked revolving credit facilities, in addition to a cash position of €1.3bn.

Liquidity

- **Strong liquidity**

We assess the liquidity profile of Sonepar as "Superior", reflecting its strong refinancing profile and its high liquidity availability. Sonepar has a significant amount of cash on balance sheet, large undrawn committed credit lines, a long-term debt maturity profile, and a capacity to generate strong free cash flow after dividends.

CREDIT METRICS EXPECTED EVOLUTION (CMEE)

Our Stable CMEE reflects our view that credit metrics will probably remain strong and broadly unchanged over the next twelve months.

MODIFIERS

Country risk

Taking into account Sonepar's excellent geographic diversification, no specific country risk has been identified.

Controversies

Over the course of our review, we found no significant controversies regarding the group.

SONEPAR SAS

MAIN FINANCIAL FIGURES

Main financial figures. millions of EUR	FY21	FY22	FY23	23vs22
Turnover	26 366	32 408	33 299	2,7%
EBITDA	2 222	2 996	2 794	-6,7%
EBITDA Margin	8,4%	9,2%	8,4%	-0,9pp
EBIT	1 726	2 461	2 213	-10,1%
EBIT Margin	6,5%	7,6%	6,6%	-0,9pp
EBT	1 417	2 463	2 086	-15,3%
Total Assets	17 118	19 424	20 468	5,4%
Equity	6 864	8 360	9 162	9,6%
Total Financial Debt	3 747	3 794	4 415	16,4%
Net Financial Debt	2 117	2 567	3 114	21,3%
Equity/TFD	183,2%	220,3%	207,5%	-12,8pp
NFD/EBITDA	1,0x	0,9x	1,1x	0,3x
Adj Funds From Operations	1 834	2 316	1 984	-14,3%
Adj FFO/NFD	86,6%	90,2%	63,7%	-26,5pp
EBITDA/Interest	25,3x	28,8x	16,3x	-12,5x

RATING SENSITIVITY

- **Rating list:**
  - NEU CP: EF1+

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

- **Positive factors (↑)**

Sonepar already has the highest short-term rating under our methodology.

- **Negative factors (↓)**

A downgrade to EF1 may come from a sustained deterioration of credit metrics, should margins fall or should the group adopt a more aggressive financial policy, for example in the event of a large debt-funded M&A deal. An EthiFinance Ratings-adjusted net leverage ratio above 1.5x, on a sustainable basis, could lead to a downgrade of our short-term rating to EF1. Moreover, a downgrade of the CMEE to “Negative” – which would be based on a deterioration in the outlook for key credit metrics - would also point towards a rating downgrade.

Sources of information

The credit rating assigned in this report has been requested by the rated entity, which has also taken part in the process. It is based on private information as well as public information. The main sources of information are:

1. Annual Audit Reports.
2. Corporate Website.
3. Information published in the Official Bulletins.
4. Rating book provided by the Company.

The information was thoroughly reviewed to ensure that it is valid and consistent, and is considered satisfactory. Nevertheless, EthiFinance Ratings assumes no responsibility for the accuracy of the information and the conclusions drawn from it.

Additional information

- The rating was carried out in accordance with Regulation (EC) N°1060/2009 of the European Parliament and the Council of 16 September 2009, on credit rating agencies. Principal methodology used in this research are :
  - Corporate Rating Methodology - Long Term : https://files.qivalio.net/documents/methodologies/CRA 190 V3 Corporate%20Methodology 2023-10-06.pdf
  - Corporate Rating Methodology - Short Term : https://files.qivalio.net/documents/methodologies/CRA 191.Corporate Rating Methodology Short Term-202303.pdf
  - Corporate Rating Methodology - Short Term : https://files.qivalio.net/documents/methodologies/CRA 191.Corporate Rating Methodology Short Term-202303.pdf
- The rating scale used in this report is available at https://www.ethifinance.com/en/ratings/ratingScale.
- EthiFinance Ratings publishes data on the historical default rates of the rating categories, which are located in the central statistics repository CEREP, of the European Securities and Markets Authority (ESMA).
- 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.
- The issued credit rating has been notified to the rated entity, and has not been modified since.