FITCH UPGRADES FAURECIA TO 'BB+'; OUTLOOK STABLE

Fitch Ratings-Paris-20 February 2018: Fitch Ratings has upgraded Faurecia S.A.'s Long-Term Issuer Default Rating (IDR) and senior unsecured debt to 'BB+' from 'BB'. The Outlook on the Long-Term IDR is Stable.

The rating action reflects the improved and better-than-expected earnings and underlying cash generation of Faurecia, which positions the French auto supplier at the high-end of the 'BB' category, according to Fitch's revised Rating Navigator for auto suppliers.

Free cash flow (FCF) below 1.5% of sales remains weak for the rating. This is despite an improvement in 2017 to 1.1% of total sales (1.3% of value-added (VA) sales, excluding sales of catalytic converter monoliths), boosted by a working capital inflow that offset higher dividends and capex. However, we expect a gradual and modest strengthening towards 2% by 2020. We also assess FCF in combination with leverage, the latter of which has improved continuously since 2012 and is now firmly in line with the rating. Faurecia's credit metrics now compare more adequately with similarly-rated peers in Fitch's portfolio.

KEY RATING DRIVERS

Improving Earnings: The operating margin, based on VA sales and after restructuring expenses, has increased continuously to 6.4% in 2017 from 3.8% in 2014. We expect further improvement to more than 7% by 2020, a level more in line with peers' and a 'BB+' rating. All divisions have strengthened their earnings and all regions returned to profitability in 2017. The robust order book also provides support to earnings sustainability in the next two to three years. Underlying cash generation has also improved to levels more commensurate with the high end of the 'BB' category as the FFO margin is forecast to rise to about 9% of VA sales by 2020, from 7.9% in 2017 and 7.6% in 2016.

Leading Market Positions: The ratings of Faurecia are supported by its diversification, size and leading market positions as the eighth-largest global automotive supplier. Its large and diversified portfolio is a strength in the global automotive market, which is being reshaped by the development of global car manufacturing platforms and the acceleration of new technologies and demand from large manufacturers. Fitch also believes that the company is well- positioned in some fast-growing segments to outperform the overall auto supply market, notably by offering products that increase the fuel efficiency of its customers' vehicles.

Business Refocus: We believe that the exterior business (FAE) disposal in 2016 is an illustration of Faurecia's aim to gradually refocus the business. In particular, we expect the company to acquire businesses active in higher added-value and faster-growing segments and to accelerate investment in sustainable mobility and the interior business. This should help address some of the longer-term risks associated with Faurecia's smaller exposure to fast-growing and more profitable segments such as connectivity and autonomous driving, compared with large peers such as Continental and Bosch. Fitch's rating case includes several bolt-on acquisitions for about EUR350 million per year but no major purchases, which we would assess on a case-by-case basis.

Sound Diversification: Faurecia's healthy diversification by product, customer and geography can smooth potential sales decline in one particular region or lower orders from one specific manufacturer. Its broad industrial footprint matching its customers' production sites and needs enables Faurecia to follow its customers in their international expansion. The company has

greatly reduced its dependence on some of its large historical customers and no manufacturer now represents more than 20% of product sales.

Weak FCF: FCF increased to just over EUR220 million in 2017 (1.1% of total sales and 1.3% of VA sales) from about breakeven in 2015 and 2016. The improvement was driven chiefly by more than EUR200 million of working capital inflow and improved funds from operations (FFO) offsetting higher dividends and capex. Fitch expects FCF to remain at risk of a potential working capital reversal in the medium-term and increasing investment to meet the company's business refocus and accelerating demand arising from shifting automotive trends.

We expect the FCF margin to decline below 1% in 2018 before recovering towards 2% by 2020. This remains at the low end of Fitch's typical guidelines for a 'BB+' rating but we assess FCF in combination with leverage, the latter of which has improved continuously since 2012 and is now firmly in line with the current rating.

Stronger Financial Structure: Faurecia's FFO adjusted net leverage remained stable at 1.6x at end-2017 as positive FCF was absorbed by a few small acquisitions. Fitch expects leverage to remain broadly stable at around 1.5-1.6x in the foreseeable future in the absence of major acquisitions, which would be treated as event risk.

Weak Linkage with Peugeot S.A.: We applied our parent and subsidiary rating linkage (PSL) methodology and assessed that Faurecia has a credit profile similar to its parent Peugeot S.A. (PSA; BB+/Stable), which has a 46.3% stake and 63.1% voting rights. We also deem the legal, operational and strategic ties between the two entities weak enough to rate Faurecia on a standalone basis.

DERIVATION SUMMARY

Faurecia's business profile compares adequately with auto suppliers at the low-end of the 'BBB' category. The share of the company's aftermarket business, which is less volatile and cyclical than sales to original equipment manufacturers (OEMs), is smaller than tyre manufacturers such as CGE Michelin (A-/Stable) and Continental AG (BBB+/Stable). Faurecia's portfolio has fewer products with higher added value and substantial growth potential than other leading and innovative suppliers including Robert Bosch AG (F1), Continental AG and Aptiv PLC (BBB/Stable). However, similar to other large and global suppliers, it has a broad and diversified exposure to large international auto manufacturers.

With an EBIT margin around 6.5%, profitability is lower than that of investment grade-rated peers, such as Continental AG, BorgWarner, Inc. (BBB+/Stable) and Aptiv PLC and similarly rated Tenneco, Inc. (BB+/Stable). Faurecia's FCF is at the low end of Fitch's portfolio of auto suppliers in the 'BB+'/'BBB-' rating categories. Adjusted net leverage is just above 1.5x, lower than Tenneco's, and improving but still higher than investment-grade peers'. Fitch applied its PSL methodology and assessed that Faurecia can be rated on a standalone basis. No country-ceiling or operating environment aspects impact the ratings.

KEY ASSUMPTIONS

Fitch's Key Assumptions within Our Rating Case for the Issuer
-Revenues to increase in mid-single digits in 2018-2020. Fitch is now assessing revenue based on VA sales, excluding catalytic converter monoliths, in line with the company's new reporting method. Monoliths represented EUR3.2 billion sales in 2017.
-Operating margins to increase gradually to 7.2% of VA sales by 2020.
-Restructuring cash outflows of about EUR80 million in 2018, declining to about EUR60 million-EUR70 million per year in 2019-2020.

-Moderate cash outflow from working capital reversal in 2018, before stabilising in 2019-2020.
-Capex to remain broadly stable around EUR1.2 billion per year.
-Dividend pay-out ratio of 25%.
-Acquisitions to average around EUR350 million per year in 2018-2020.

RATING SENSITIVITIES

Rating sensitivities have been updated to reflect the upgrade and the latest Rating Navigator for the auto supply industry.

Developments That May, Individually or Collectively, Lead to Positive Rating Action
-FFO adjusted net leverage below 1.5x
-Operating EBIT margin above 8%
-FCF margin around 2%

Developments That May, Individually or Collectively, Lead to Negative Rating Action
-FFO adjusted net leverage above 2.5x
-Operating EBIT margin below 5%
-FCF margin below 0.5%

LIQUIDITY

Sound Liquidity: Liquidity is supported by EUR1.2billion of readily available cash according to Fitch's adjustments for minimum operational cash of about EUR0.4 billion. Total committed and unutilised credit lines maturing in June 2021 were EUR1.2 billion at end-2017, largely covering short-term debt of EUR0.4 billion at end-2017. The company's financial flexibility and liquidity is further supported by our expectations of positive FCF generation.

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Summary of Financial Statement Adjustments

- Debt Factoring: We adjust leverage calculations by including EUR1,039 million of off-balance-sheet factoring. We also move the cash flow effect from working capital cash movements to change in net debt.
- Adjustment to Cash: The reported cash and cash equivalents are reduced by the cash deemed necessary by Fitch to run the day-to-day operations (around EUR0.4 billion).
- Other Adjustments: Fitch viewed restructuring costs as operating costs.

Additional information is available on www.fitchratings.com. For regulatory purposes in various jurisdictions, the supervisory analyst named above is deemed to be the primary analyst for this issuer; the principal analyst is deemed to be the secondary.

Applicable Criteria
Corporate Rating Criteria (pub. 07 Aug 2017)
https://www.fitchratings.com/site/re/901296
Non-Financial Corporates Notching and Recovery Ratings Criteria (pub. 21 Dec 2017)
https://www.fitchratings.com/site/re/914144
Parent and Subsidiary Rating Linkage (pub. 15 Feb 2018)
https://www.fitchratings.com/site/re/10019836

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