Franz Haniel & Cie. GmbH
Germany, Investment Holdings

SCOPE BBB- STABLE

Corporate profile

Franz Haniel & Cie. GmbH (Haniel) is an investment holding company. Haniel manages a diversified portfolio and pursues a long-term investment strategy as a value developer with no operating activities of its own. The investment holding focuses on the receipt of recurring dividend payments from its different shareholdings, in addition to value creation. Additional cash flows can be generated from the full or partial sale of shareholdings and other assets. The current portfolio comprises controlling stakes in CWS, ELG, TAKKT, BekaertDeslee, ROVEMA, Optimar and minority positions in CECONOMY and METRO. The closing for most recent acquisition of Emma is pending.

Key metrics

			Scope estimates		
Scope credit ratios	**2018**	**2019**	**2020E**	**2021E**	**2022E**
Total cost coverage (x)	1.8	1.6	0.6	1.0	1.1
Loan-to-value (Scope-adjusted debt/portfolio's market value)	14%	3%	Depending on new investments and market developments (<20%)		
Liquidity	>200%	>200%	>200%	>200%	>200%

Scope Ratings affirms its issuer ratings of BBB-/Stable on Germany-based Franz Haniel & Cie. GmbH and its financing subsidiary Haniel Finance Deutschland GmbH. Senior unsecured debt is affirmed at BBB-; short-term debt is affirmed at S-2.

The affirmation reflects our view on Haniel's solid financial profile, backed by low a loan-to-value that provides good headroom for bridging lower income from portfolio companies and an expected temporary shortfall in total cost coverage below 1.0x in 2020

The Stable Outlook reflects our view that the expected drop in total cost coverage in 2020 will be only temporary, with the level recovering to at least 1.0x in 2021 and beyond. This incorporates an assumed recovery of income from portfolio companies or, in case the former scenario is subdued, a reduction in portfolio costs such as dividend pay-outs.

A positive rating action is remote in the short term given the limited visibility on the potential for a significant improvement in total cost coverage, which would entail achieving at least 1.3x on a sustained basis. This, however, could be the result of a more granular investment portfolio.

A negative rating action could result if we were to expect a deterioration in total cost coverage to below 1.0x on a sustained basis. This could be the result of continued pressure on subsidiaries' income streams beyond 2020 or a lack of effort to reduce total costs at the holding company level. Moreover, the rating could come under pressure if the communicated net debt target of EUR 1.0bn was exceeded without being offset by dividend streams from new investee companies.

Ratings & Outlook

Corporate ratings	BBB-/Stable
Short-term rating	S-2
Senior unsecured rating	BBB-

Analyst

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Related Publications

Monitoring Note on Franz Haniel & Cie. GmbH, Sep 2019

Scope affirms BBB-/Stable/S-2 issuer rating of Haniel, Apr 2019

Monitoring Note on Franz Haniel & Cie. GmbH, Aug 2018

Scope Ratings affirms its issuer rating of BBB-/Stable on Germany-based Franz Haniel & Cie. GmbH, Jun 2018

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Bloomberg: SCOP

Rating drivers

Positive rating drivers	Negative rating drivers
• Buy-and-hold investment approach with primary focus on recurring income streams, e.g. dividends and other income from portfolio companies and financial assets • Portfolio companies which are largely market leaders in their respective industries and with well-established business models in mature markets • Sharpened investment focus on companies which follow global megatrends • Ongoing rebalancing of investment portfolio in line with investment strategy, bolstered by current liquidity, good access to unused, committed credit lines and further investment headroom of more than EUR 1.5bn at YE 2019 • Balanced industry allocation in the investment portfolio, which contains uncorrelated exposures to non-cyclical and cyclical industries • Strong geographical diversification across revenue streams in the investment portfolio • Commitment to keeping net debt up to EUR 1bn over the medium to long term, even after new investments • Expectation of a sustained total cost coverage at above 1.0x, although expected to drop to below 1.0x in 2020 • Strong liquidity and limited short-term refinancing needs, allowing for substantial acquisitions and/or further debt reduction	• Number of shareholdings remains limited (currently eight excluding financial assets), resulting in high concentration risks in terms of income sources and net asset value • Limited asset liquidity due to large share of unlisted subsidiaries which cannot be sold immediately if liquidity is urgently needed, partly offset by Haniel's buy-and-hold investment approach and comfortable liquidity • Increased focus on SMEs resulting in stronger earnings volatility, partly offset by improved diversification • Volatile leverage (loan-to-value) stemming from market volatility • Expected temporary shortfall in total cost coverage in 2020 as the result of dividend cuts at major income-generating portfolio companies

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Remote possibility in the short term given the limited visibility on a potential significant improvement in total cost coverage to a sustained level of 1.3x or above	• Total cost coverage of below 1.0x on a sustained basis • Breach of the company's net debt target of EUR 1bn if not justified by equivalent dividend income

Financial overview

			Scope estimates		
Scope credit ratios	**2018**	**2019**	**2020E**	**2021E**	**2022E**
Total cost coverage (from recurring income)	1.8	1.6	0.6	1.0	1.1
Total cost coverage without dividend payments (recurring)	3.6	3.4	1.1	2.0	2.6
Loan-to-value ratio (Scope-adjusted debt/portfolio market value)	14%	3%	Depending on new investments and market developments (<20%)		
Liquidity	>200%	>200%	>200%	>200%	>200%
Cash flows (EUR m)	**2018**	**2019**	**2020E**	**2021E**	**2022E**
Recurring cash inflows (dividends and profit transfers)	218	178	67	114	144
Non-discretionary cash outflows (incl. net interest payments)	122	112	118	117	126
Balance sheet/indebtedness (EUR bn)	**2018**	**2019**	**2020E**	**2021E**	**2022E**
Scope-adjusted debt (incl. pension adjustments)	0.6	0.1	<1.0	<1.0	<1.0
Net asset value	4.0	4.5	n/a	n/a	n/a

Sharpened investment focus likely leading to more stable income in the medium term

Focus on ES(G)-relevant investments

Haniel's rating reflects the continued execution of its finetuned investment strategy, which focuses on investments in controlling stakes of mature SMEs. The investments also need to align with Haniel's new People-Planet-Progress strategy, oriented towards companies or investments with a business purpose addressing global and sustainable megatrends in four areas: i) health and well-being; ii) the circular economy; iii) climate change; and iv) robotics and automation. Recent investments in Emma and the Gilde Healthcare V growth capital fund (both in 2020) but also the full takeover of CWS (2019) and the portfolio additions from 2017 in ROVEMA and Optimar fully fit these criteria.

Figure 1: Focus areas under Haniel's People-Planet-Progress investment strategy

People: Health & well-being | Planet: Circular economy and climate change | Progress: Robotics and automation

Source: Haniel

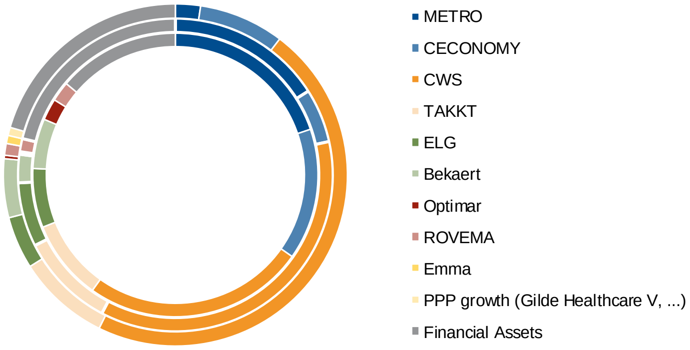
Concentration risks on income stream likely to increase in 2020 …

However, Haniel remains dependent on just a few dividend- and income-generating investments, despite ongoing portfolio reshuffling (eight investments in the portfolio as of April 2020) having led to a higher exposure to less correlated industries. However, an improved diversification among dividend- and income-generating assets remains subdued. Specifically, 54% of 2019 income stemmed from CWS dividends, and 93% from the top three income-generating entities. This will likely be amplified in 2020 by Covid-19's effect on Haniel's major dividend- and income-generating portfolio companies, which are expected to cut dividends to preserve cash or which are likely to generate lower profits that can be distributed to the holding company.

… but still expected to improve in the medium term

Over a longer time horizon, however, we are confident that Haniel's income diversity will strengthen through the use of its large investment headroom, especially when Haniel uses improved conditions for portfolio additions (we expected conditions for buyers to be better than over the past three years in light of less stretched valuations and lower competition between potential bidders for potential M&A targets). Although the further sale of METRO holdings have significantly reduced portfolio liquidity and fungibility, the sale proceeds have provided further headroom to acquire controlling stakes in mature European SMEs. We continue to put less emphasis on Haniel's reduced exposure to liquid/listed portfolio companies for as long as total cost coverage and liquidity are sufficient to avoid forced asset sales.

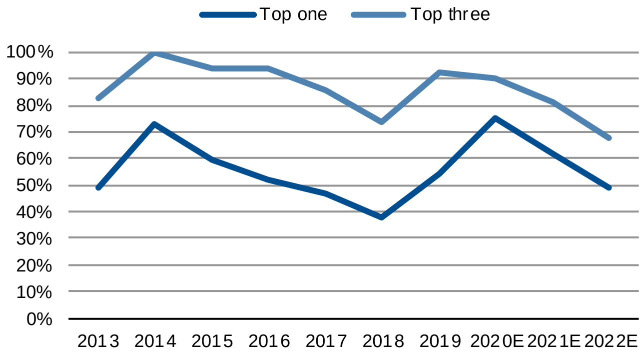
Figure 2: Persistently high asset concentration (outer circle Scope's estimate for Q2 2020E*; middle circle = Dec 2018; inner circle = Dec 2017;)



* The investment in Emma is pending

Source: Haniel, Scope

Figure 3: Concentration risk as measured by income contributions from portfolio companies



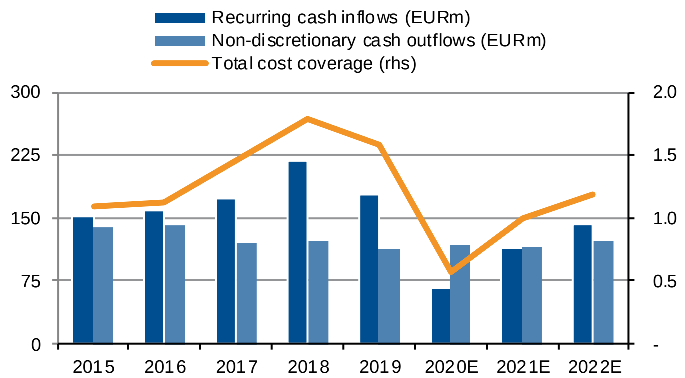
Source: Haniel, Scope

Solid financial risk profile with expected deterioration in total cost coverage to be offset by a very low loan-to-value and sound liquidity

Expected drop in Haniel's total cost coverage below 1.0x in 2020

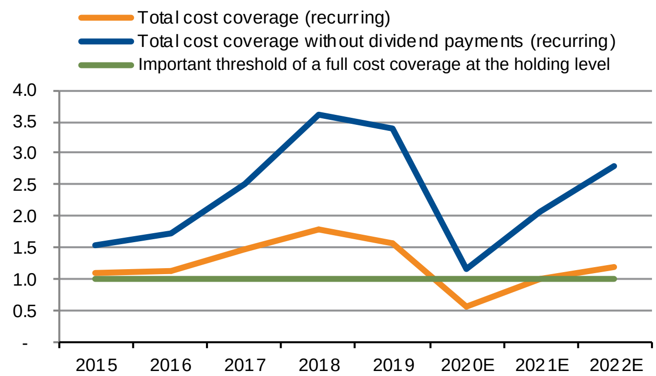
While Haniel's total cost coverage in 2019, at 1.6x, has again comfortably exceeded the 1.3x threshold for a positive rating action for a third year in a row, 2020 will likely show a different picture. Dividend income from METRO has reduced by EUR 28m, but the Covid-19 lockdowns will likely have an even bigger impact on Haniel's most lucrative income-generating portfolio holdings, with a dividend cut already announced at TAKKT (minus EUR 25m), reduced net profit expectations at CWS, and little or no profit-sharing likely from smaller portfolio companies looking to preserve liquidity. We expect the ratio to drop to 0.6x in 2020, which incorporates a continued EUR 60m dividend pay-out to Haniel shareholders within the total cost base of the holding company.

Figure 4: Total cost coverage



Source: Haniel, Scope estimates

Figure 5: Total cost coverage (base case without any cuts on dividend pay-outs going forward)



Source: Haniel, Scope estimates

Full cost coverage at holding level expected over the medium term

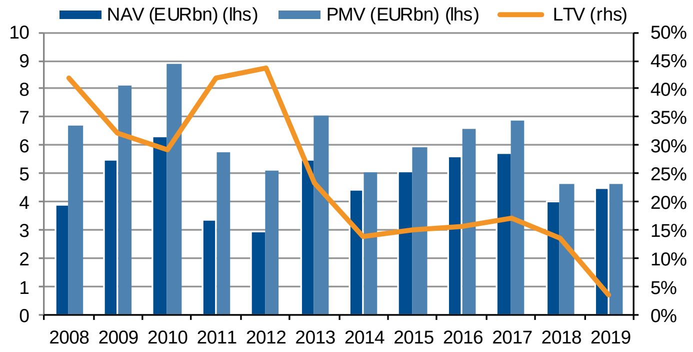
Nonetheless, we remain confident that total portfolio income (as displayed by our forecasts of a total EUR 67m in 2020) will continue to fully cover operating expenses and maintenance capex, resulting in positive free operating cash flow for 2020. How quickly the major income-generating portfolio companies can return to a dividend/income-paying mode will depend on the duration of Covid-19-related lockdowns and the speed of an assumed macroeconomic recovery. However, the expected temporary shortfall in the full coverage of total costs needs to be seen in conjunction with i) the significantly improved leverage (see next paragraph); ii) the large cash buffer; and iii) the holding's approach on dividends to the Haniel family. Overall, we remain optimistic about a likely recovery in 2021 and beyond for key income-generating portfolio companies, which would return Haniel's total cost coverage to at least 1.0x, thereby justifying the current rating level. Our view is backed by the following:

- The low loan-to-value at YE 2019 would provide debt headroom of around EUR 800m before a 20% loan-to-value ratio would be reached (assuming an unchanged portfolio market value). This is certain to increase total holding costs through increased interest. However, raising debt to cover operating costs, without leading to a significant deterioration of leverage, could bridge a few years of meagre income from portfolio companies.
- We believe that if income from portfolio holdings continued to stay below the level needed for full cost coverage, Haniel would reduce costs, with its biggest lever being the reduction of dividend payments to shareholders. A dividend cut for 2021 (not yet expected in our base case) would halve costs from around EUR 120m to EUR 60m, thereby increasing the likelihood of full cost coverage even in meagre income years. Haniel's shareholders have already shown flexibility on dividends in times of insufficient total cost coverage: during 2013-15, they accepted no dividends in one year and lower dividends in the other two years. Shareholders are therefore more likely to compromise on dividends in 2021 and beyond if it proves necessary to keep financial resources within the holding company.

Large debt headroom stemming from an all-time-low market value gearing

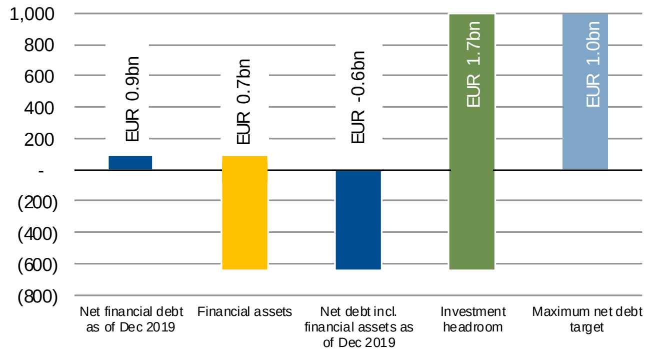
Following significant asset disposals in 2019, Haniel's indebtedness, as measured by the loan-to-value ratio, now stands at an all-time low (3.4% at YE 2019 vs 14% at YE 2018). Although portfolio market gearing remains strongly exposed to the volatility of share prices and applicable valuation multiples for non-listed portfolio companies (with major impacts from recent corrections in value of listed portfolio companies but also from deteriorated valuation multiples for non-listed subsidiaries), the holding company's leverage is unlikely to deteriorate beyond the 25% threshold in the rating case. This is for two reasons: Scope-adjusted debt is very low at about EUR 0.2bn at YE 2019; and Scope's sensitivity analysis shows that the portfolio's market value can decrease by more than 80% before a 25% loan-to-value ratio is reached.

Figure 6: Market value gearing



Source: Haniel, Scope

Figure 7: Potential investment headroom before reaching the maximum net debt target (in EUR m) at YE 2019



Source: Haniel, Scope

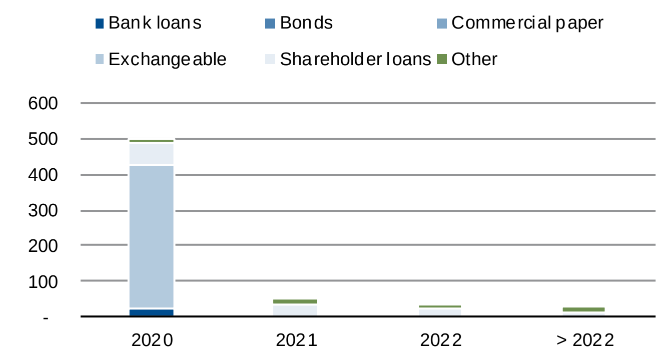
Investment headroom increased to above EUR 1.7bn

Taking into account Haniel's communicated net debt ceiling of EUR 1bn and the net financial position at YE 2019 of EUR 600m (comprising net financial debt of EUR 0.1bn and financial assets of EUR 0.8bn), there is potential for investments of EUR 1.7bn. The use of this investment headroom would go hand in hand with increased portfolio market value through new investments, unless the buffer is used for bridging an extended period of insufficient cost coverage or a significant amount of the buffer is used for supporting majority-owned portfolio companies through cash injections.

Robust liquidity

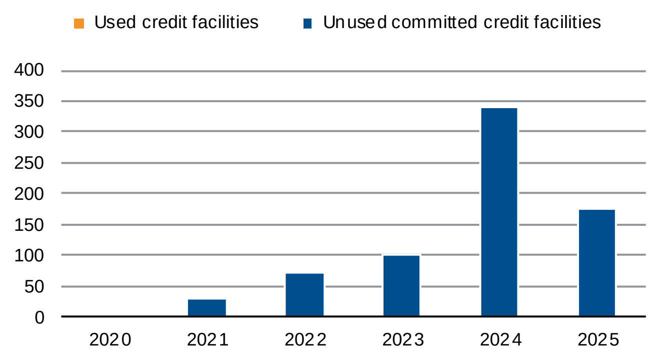
Haniel's liquidity continues to be robust. The holding company's debt burden primarily comprises the remaining portion of the EUR 500m exchangeable bond and shareholder loans, adding up to around EUR 500m of gross upcoming debt repayments between 2020-22 (2020E: EUR 0.5bn; 2021E: EUR 0.05bn; 2022E: EUR 0.05bn). We expect the upcoming redemption (May 2020) of the remaining loan value of the exchangeable bond (~EUR 400m at YE 2019) to be covered fully by the cash cushion (EUR 532m at YE 2019), without the need to draw on the unused multi-year credit facilities (around EUR 700m at YE 2019). Haniel also has no need to deploy its EUR 500m commercial paper programme or issue a new or exchangeable bond. Once the exchangeable bond is redeemed, around EUR 200m of interest-bearing debt will remain, resulting in very limited refinancing risks over the next 2-3 years. In light of this, but also given the aforementioned significant headroom and positive free operating cash flows going forward, Haniel is also not expected to be forced into selling company stakes to cover maturing debt.

Figure 8: Maturity profile (EUR m)



Source: Haniel, Scope

Figure 9: Committed undrawn revolving credit facilities (in EUR m)



Source: Haniel, Scope

Long-term and short-term debt ratings

BBB- for senior unsecured debt

Long-term debt is affirmed at BBB-, the level of the issuer rating.

S-2 short-term rating

Haniel's short-term rating for the EUR 500m commercial paper programme reflects our view on the company's robust liquidity profile. This view is based on internal and external liquidity sources, as well as the company's good standing in public and private debt markets and well-established banking relationships, partly evidenced by the broad mix of committed long-term credit lines from different banks.

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