STANDARD & POOR'S RATINGS SERVICES
McGRAW HILL FINANCIAL

Research

Summary:

Renault S.A.

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Summary:

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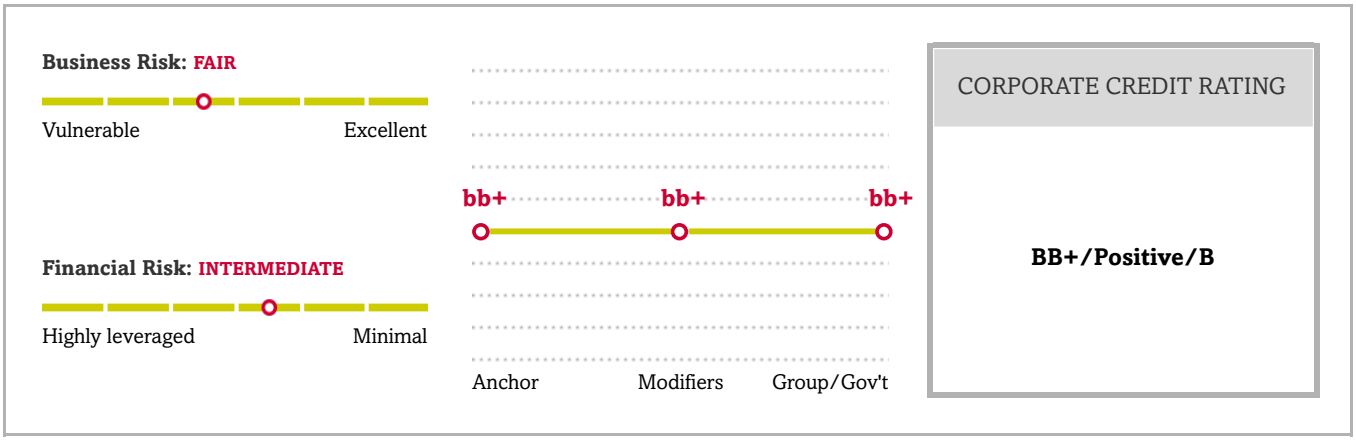

Rationale

Business Risk: Fair	Financial Risk: Intermediate
• Weak, albeit improving profitability of the group's core automotive operations. • Small size by global standards. • Good market positioning in the small car and entry segments. • Potential to improve scale and geographic spread through cooperation with Nissan.	• Robust credit ratios for the ratings. • Track record of positive free operating cash flow generation in recent years, expected again in 2015. • Positive contribution to cash flow from its captive finance arm, RCI Banque and, through dividends, from its equity associate Nissan.

Outlook: Positive

The positive outlook on Renault reflects our opinion that its financial policy will support credit metrics over the next 24 months and that the company will gradually improve the profitability of its automotive operations. As a result, we expect Renault's adjusted EBITDA margin to move closer to the middle of the 9%-10% range by 2015.

Upside scenario

We may raise our ratings on Renault if the company maintains an adjusted FFO-to-debt ratio above 45%. In that case, we would revise our financial risk profile assessment to "modest" from "intermediate." Such a scenario could unfold if, for instance, Renault moderately increases shareholder remuneration and does not make large debt-financed acquisitions. An upgrade would require that the profitability of automotive operations keeps improving, thanks to productivity gains and the recovery of the European car market.

Downside scenario

We could revise the outlook to stable if Renault was unable to preserve an adjusted FFO-to-debt ratio above 45%, as a result of a more aggressive financial policy or a sharp decline in earnings. We would also revise the outlook to stable if the operating margin of automotive operations deteriorated because of declining sales or an inability to contain costs.

Standard & Poor's Base-Case Scenario

Assumptions

- Car sales of global automakers will rise by 1.1% in 2014 and by 4.2% in 2015.
- Sales in Western European markets will increase by 4.2% in 2014 and by 4.4% in 2015 (see "Moderate Economic Growth Prospects Are Keeping Global Automakers And Suppliers On The Road," published on July 11, 2014, on RatingsDirect).
- Volume growth and cost savings will roughly offset negative currency effects in 2014.
- The company's financial policy will remain prudent, with a limited increase in shareholder remuneration and no large debt-financed acquisition.

Key Metrics

	2013A	2014E	2015E
EBITDA margin (%)*	8.3	8.3-9	8-10
FFO/debt (%)*	61.2	40-65	40-80
Debt/EBITDA (x)*	1.3	1-1.5	0.8-1.5

*Standard & Poor's adjusted.

A--Actual. E--Estimate.

Business Risk: Fair

The main factors supporting Renault's "fair" business risk profile, in our view, are a good market position in the entry segment of the car market, contributing positively to group earnings, and the company's strategic alliance with Nissan.

Joint purchasing, common research and development, and shared network management with Nissan have already generated meaningful synergies for Renault, and in the future we would expect the company to benefit further from platform-sharing with Nissan including in emerging countries with long-term growth potential.

These supporting factors are offset by the cyclicality of the car market industry and the low profitability of Renault's core automotive operations. We believe that the credit quality of mass-market car manufacturers is constrained by demand cyclicality, excess production capacity and intense competition in Western Europe, high capital intensity and a significant fixed-cost base that results in high operating leverage. Furthermore, the profitability of the automotive segment is low, although it has improved recently. This division achieved a reported operating margin of 1.9% during the first half of 2014, compared to 1.1% a year earlier. We expect that profitability will increase gradually in the next 18 months mostly thanks to productivity gains.

Even though emerging markets are currently weighing on earnings, we believe that these operations remain fundamentally supportive of Renault's credit quality. In 2014, we assume that Renault will partly offset the depreciation of emerging market currencies with price increases. Regarding Russia, we forecast a limited earnings decline owing to the renewal of the vehicle line-up and the high share of Russian production.

Financial Risk: Intermediate

Renault has markedly improved its financial profile in recent years. Between 2010--when we raised the company's long-term corporate credit rating to 'BB+'--and 2013, the adjusted funds from operations (FFO)-to-debt ratio climbed to 61% from 31%, thanks to asset disposals and earnings growth. Over that three-year period, the company's adjusted debt contracted to €4.0 billion from €5.7 billion. The automotive division had a €0.8 billion net cash position on a reported basis on June 30, 2014. We expect Renault will continue to generate positive free operating cash flows in 2014 and 2015 owing to supportive operating trends, capital expenditures in line with historical trends, and limited working capital cash outflows. We also assume that the company will maintain a disciplined approach toward shareholder remuneration and acquisitions.

Liquidity: Adequate

The short-term rating on Renault is 'B'. We view Renault's liquidity as "adequate" under our criteria. We calculate that the company's ratio of potential sources of liquidity to uses will exceed 1.2x in the next 12 months.

Principal Liquidity Sources	Principal Liquidity Uses
• €8.8 billion of cash and cash equivalents held in its automotive division on June 30, 2014, after applying a 25% haircut. • €3.3 billion in undrawn bilateral committed credit lines maturing in more than 12 months at the automotive division. • About €2.7 billion of FFO forecast over the next 12 months.	• €4 billion in automotive debt maturing in less than one year. • About €0.2 billion of working capital outflow. • About €2.8 billion of capital expenditures. • About €0.6 billion of dividends.

Covenant Analysis

The undrawn credit facilities have no financial covenants. We note that Renault also reported €24.4 billion of short-term liabilities related to its captive finance subsidiary, RCI Banque, on June 30, 2014. We expect this subsidiary will have sufficient liquidity to cover its funding needs.

Ratings Score Snapshot

Corporate Credit Rating

BB+/Positive/B

Business risk: Fair

- **Country risk:** Intermediate
- **Industry risk:** Moderately high
- **Competitive position:** Fair

Financial risk: Intermediate

- **Cash flow/Leverage:** Intermediate

Anchor: bb+

Modifiers

- **Diversification/Portfolio effect:** Neutral (no impact)
- **Capital structure:** Neutral (no impact)
- **Financial policy:** Negative (no impact)
- **Liquidity:** Adequate (no impact)
- **Management and governance:** Satisfactory (no impact)
- **Comparable rating analysis:** Neutral (no impact)

Recovery Analysis

Key analytical factors

- The issue rating on Renault's senior unsecured notes issued under the €7 billion Euro Medium-Term Note program is 'BB+', in line with our corporate credit rating on the company. The recovery rating on these notes is '3'.
- The recovery rating is supported by the company's substantial asset base but constrained by the unsecured nature of the notes, the possibility of capital structure changes on the path to default, and our opinion of the less creditor-friendly jurisdiction of France.
- In our hypothetical default scenario to calculate recoveries, we assume a payment default in 2019 as a result of material deterioration in operating performance and negative free cash flow at Renault's automotive operations. Moreover, under our path-to-default scenario, we assume that operating losses and restructuring expenses would require significant cash funding and would reduce the company's available liquidity. In this scenario, under tight credit conditions, we project that Renault would be unable to raise additional debt funding.
- We value Renault as a going concern because it has, in our view, a good market position, a widespread distribution network, and well-known brands. As such, we believe creditors would obtain greater recovery through reorganization as opposed to liquidation.

Simulated default assumptions

- Year of default: 2019
- Jurisdiction: France
- Gross enterprise value at default: €10.3 billion

Simplified waterfall

- Net enterprise value (after 9% administrative costs): €9.4 billion
- Priority claims: €2.4 billion
- Senior unsecured debt claims: €11.2 billion*
- --Recovery expectations: 50%-70%--

*All debt amounts include six months of prepetition interest.

Related Criteria And Research

Related Criteria

- Key Credit Factors For The Auto And Commercial Vehicle Manufacturing Industry, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013

Related Research

- French Automaker Renault Outlook Revised To Positive On Improved Credit Metrics; 'BB+/B' Ratings Affirmed, June 5, 2014

Business And Financial Risk Matrix

Business Risk Profile	Financial Risk Profile					
	Minimal	Modest	**Intermediate**	Significant	Aggressive	Highly leveraged
Excellent	aaa/aa+	aa	a+/a	a-	bbb	bbb-/bb+
Strong	aa/aa-	a+/a	a-/bbb+	bbb	bb+	bb
Satisfactory	a/a-	bbb+	bbb/bbb-	bbb-/bb+	bb	b+
Fair	bbb/bbb-	bbb-	**bb+**	bb	bb-	b
Weak	bb+	bb+	bb	bb-	b+	b/b-
Vulnerable	bb-	bb-	bb-/b+	b+	b	b-

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