S&P Global
Ratings

Research

Research Update:

Renault S.A. Ratings Placed on CreditWatch Negative On Expected Further Depressed Free Cash Flow Generation

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Rating Action Overview

- Amid weak demand and tightening environmental regulation, France-based automaker Renault S.A. will likely fail to report S&P Global Ratings-adjusted automotive free operating cash flow in excess of 1% of its sales in 2020.
- While we believe Renault has retained solid financial flexibility thanks to its comfortable cash reserves, several operational challenges could further depress its free cash flow generation over the next 18-24 months.
- We are therefore placing on CreditWatch with negative implications our 'BBB-/A-3' long- and short-term issuer credit ratings on Renault and our 'BBB-' issue ratings on the company's debt.
- At this time, we expect the potential downgrade to be limited to one notch. We aim to resolve the CreditWatch placement by the end of May 2020.

Rating Action Rationale

Renault's margin will continue to suffer in a challenging market environment. Renault's updated guidance points to flat sales and an operating margin between 3% and 4% for 2020 versus 4.8% in 2019. This compares with an earlier target of not less than 5% in any given year over 2018-2022. Last year's results showed a similar dip; Renault's EBITDA margin, as adjusted by S&P Global Ratings, dropped to about 6.3% in 2019 from 7.8% in 2018. This was because of lower volumes sales, increased regulatory costs, higher marketing expenses related to the launch of new car models (Clio V, Captur, and Zoe), and lower dividends from Nissan Motor Co. Ltd. Also, Renault's free operating cash flow (FOCF), as adjusted by S&P Global Ratings, waned to around negative €100 million despite a release of working capital of about €1,500 million. The reduction stemmed largely from lower earnings, but a moderate €330 million increase in capital expenditure to about €3 billion (excluding capitalized development costs) also had an impact. We would typically expect FOCF in excess of 1% of sales for our 'BBB-' rating level.

We believe that competition might get tougher in Europe. Renault has recently launched new versions of its best-selling models Clio and Captur (representing about 35% of its sales in Europe). While this should support volume growth, we see the risk of intensifying competitive pressures in Renault's important European market. Evidence of market share erosion in this region, while all automakers aggressively compete to steer their powertrain mix toward cleaner vehicles to meet their C02 targets, would be negative for Renault.

CO2 regulations represent a major challenge for Renault. With about half of its sales in Europe, Renault has a high exposure to the EU's tightening CO2 regulation. The company must show a CO2 reduction of 25 grams per kilometer (g/km) on 95% of its fleet by end-2020, from 118g/km in 2019, in order to avoid fines. Renault expects to bridge the 25g gap thanks to growing sales of its electrified vehicles (including the recently launched New ZOE and hybrid vehicles); the introduction of dual fuel (LPG/petrol) powered engines for its Dacia models; and the equipment of its traditional combustion engine cars with additional components that improve fuel efficiency. In our view, the availability of hybrid models only concentrated in the second half of the year adds to the risk of intensifying competition in Europe, and could make Renault's company-specific Co2 target difficult to achieve. Furthermore, we anticipate that volume producers such as Renault will find it hard to pass on incremental electrification cost to consumers.

Consumer acceptance on large scale is still untested. The combination of the above risks casts shadows on Renault's capacity to comply with European CO2 regulation as from 2020. We estimate the cost of missing the CO2 target by 1g/km at about €180 million for Renault and in our new base case for Renault we might consider CO2-specific stresses (as we do for Volkswagen and Daimler).

Dividends from Nissan could stop for longer. In our calculations of Renault's EBITDA and FOCF, we include dividends received from Nissan (€579 million in 2019) and other equity affiliates (€46 million). Dividends received from affiliates significantly increased to €828 million in 2018, then dropped to €625 million in 2019. We expect further strain on Renault's profitability and cash flow generation given Nissan's indications that it will not pay any additional dividend to Renault in the first half of 2020. We do not expect Nissan to resume paying dividends absent a material recovery of Nissan's own profit and cash flow generation. Nissan will release results for its fiscal year ending March 2020 in May, and we anticipate it will provide an update on its midterm plan, including guidance on financial policy.

Renault's announced countermeasures may not be enough. The company has identified a set of initiatives to improve its operational performance. These include the optimization of its industrial footprint and outsourcing activities, the review of non-core assets, and the new leader-follower strategy with alliance partners Nissan and Mitsubishi Motors. We understand that Renault targets costs-savings of at least €2 billion (representing about 20% of its total fixed costs) by 2022, but we don't have any visibility on the scope, timing, and cost of implementation. We expect the company to publish a detailed plan in May 2020.

CreditWatch

The CreditWatch reflects our belief that a recovery in free cash flow generation in line with our earlier expectations (FOCF to sales above 1%) might take longer than 24 months. We believe that the company's intended countermeasures could be difficult to implement given the unfavorable market conditions, and this could stir up resistance from various stakeholders.

We plan to resolve the CreditWatch by the end of May 2020, after reviewing the pending details of Renault's efforts, including the restructuring plan, the company's ability to meet its CO2 target in Europe, and on Nissan's dividend policy.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology: The Impact Of Captive Finance Operations On Nonfinancial Corporate Issuers, Dec. 14, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- Criteria | Corporates | Industrials: Key Credit Factors For The Auto And Commercial Vehicle Manufacturing Industry, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- Renault S.A. Downgraded To 'BBB-' On Tougher Market Conditions; Outlook Negative, Oct. 25, 2019

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Renault S.A.		
Issuer Credit Rating	BBB-/Watch Neg/A-3	BBB-/Negative/A-3
Renault S.A.		
Senior Unsecured	BBB-/Watch Neg	BBB-
Commercial Paper	A-3/Watch Neg	A-3

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors,

have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.