S&P Global
Ratings

RatingsDirect®

Research Update:

Solvay 'BBB/A-2' Ratings Affirmed, Outlook Remains Negative As Future Capital Structure After Demerger Announced

June 16, 2023

PRIMARY CREDIT ANALYST

Gaetan Michel
Paris
+ 33 14 420 6726
gaetan.michel@spglobal.com

SECONDARY CONTACTS

Renato Panichi
Milan
+ 39 0272111215
renato.panichi@spglobal.com

Wen Li
Frankfurt
+ 49 69 33999 101
wen.li@spglobal.com

Rating Action Overview

- On June 16, 2023, Solvay S.A. announced the targeted capital structure to be put in place and financial policies for the retained business, to be named EssentialCo, following the projected separation of its specialty chemicals businesses.
- After the partial demerger, we expect EssentialCo's business risk will be satisfactory, and that its credit metrics under the targeted debt structure will point to significant financial risk, including adjusted funds from operations (FFO) to debt close to 30%.
- We therefore affirmed our 'BBB/A-2' long- and short-term issuer credit ratings on Solvay.
- The negative outlook remains in place, reflecting that we are likely to lower our long term issuer credit rating on Solvay to 'BBB-' at completion of the partial demerger.

Rating Action Rationale

Rating headroom remains material at Solvay, prompting us to affirm the 'BBB' rating. The group reported record results in 2022, with revenue rising 32.9% and adjusted EBITDA margin improving to above 20%. Adjusted FFO to debt climbed to 59% versus the 45% we had expected, way ahead of the 25% downside trigger for the 'BBB' rating. The supportive trend continued in first-quarter 2023, with 2% revenue growth and further margin improvement, leading the company to revise full-year guidance upwards. The overperformance puts the company in a solid credit position, in our view, to lead its transformation into two separate businesses this year.

Solvay has clarified the group split, targeted capital structures, and liability management targets. On June 16, 2023, Solvay announced the targeted capital structure for its retained business, EssentialCo, once the specialty businesses has been demerged into a new legal entity, SpecialtyCo. The partial demerger transaction is set to be completed by the end of 2023, including the process of allocating assets and liabilities, retained at EssentialCo or transferred to

SpecialtyCo. Solvay has indicated that the capital structure implementation is expected to be communicated for both EssentialCo and SpecialtyCo in August 2023, and that final terms will depend on market conditions. We will take appropriate rating actions with respect to issue ratings when this information is available. The group expects to file the partial demerger proposal to the authorities by the end of October 2023, for a closing expected before year end.

EssentialCo will retain underlying gross debt of €2.5 billion. About €1.5 billion of this will be newly issued bonds after the separation is completed. When including our adjustments for retained pension obligations (€0.5 billion), third-party mining and drilling operations provisions (€0.1 billion), and minor litigation provisions, net of cash in excess of €40 million considered as restricted, we expect the company will carry about €2.8 billion-€2.9 billion S&P Global Ratings-adjusted debt, compared with €3.8 billion for the group at the end of 2022.

We expect to lower our rating on Solvay to 'BBB-' when the separation is completed. We expect to revise Solvay's business risk profile to satisfactory, from strong currently once the partial demerger occurs. Our base case factors in €1.1 billion-€1.2 billion adjusted EBITDA in 2024, the expected first year of EssentialCo operating independently from the specialty chemicals businesses, or about 20%-22% adjusted EBITDA margin. This compares with Solvay group's €2.7 billion of adjusted EBITDA in 2022 and a comparable level in 2023, per company guidance. EssentialCo's strong margins are underpinned by the retained business' leading market positions in its key segments (soda ash, silica, and peroxides), and strong cost positions across the product lines. In light of the strong track record of resilient EBITDA and margins for the contemplated business, we expect it will generate sizable and stable free cash flows in the coming years, after planned investments dedicated to capacity expansions and decarbonization of the footprint.

We see EssentialCo's proposed debt structure as commensurate with a significant financial risk profile. Our base case points to adjusted FFO to debt of about 30% pro forma in 2024, the first year of Solvay as EssentialCo, thus at the high end of the category. However, we expect the sizable and recurring free cash flows will be largely absorbed by the projected high dividends. Solvay's announcement confirms that EssentialCo intends to maintain Solvay's current dividend policy of stable or increasing dividends. We therefore expect that discretionary cash flow-to-debt metrics will be comparatively low versus the significant financial risk profile.

Solvay has stated that EssentialCo's financial policy will be committed to an investment-grade rating. This supports our expectation of a future 'BBB-' rating for the structure. We expect that further clarity may be provided by the new management on the new business' leverage targets or tolerances. We understand that leverage will be managed carefully and that the new management will be willing to take actions to preserve the metrics under all conditions.

We revised the equity content on Solvay's hybrids to minimal. This follows the company's announcement that, as part of the separation transaction, it plans to call the PNC 2023 (€800 million) hybrid and to consider a tender on the PN C2024 (€500 million) hybrid. In the absence of the permanence feature for these instruments, we are revising the equity-content to minimal for these hybrid instruments (including the PNC 2025 €500 million bond) and treating these entirely as debt. While this revised treatment affects our credit metrics, we believe that Solvay's very strong performance in 2022 and so far in 2023 largely absorbs the additional debt treatment without putting pressure on the rating. We understand that Solvay's approach to these instruments comes as part of the transformative split strategy, and does not reflect any future policies regarding hybrid instruments for the two resulting entities.

We expect Solvay's liquidity will remain strong through the separation process, Solvay had cash available of about €1.3 billion at the end of first-quarter 2023, and about €2.8 billion of available credit lines maturing over the next 12 months. In addition, we understand the group has secured sufficient liquidity reserves for the spin-off process and will secure bridge financing at EssentialCo well in advance of the spin-off. We expect that bridge could be drawn temporarily during the process and would be repaid from the 2024 projected long-term bonds issuances. We also expect EssentialCo post closing to carry sufficient cash and available credit lines to support strong liquidity.

Outlook

The negative outlook on Solvay SA reflects that we are likely to lower the rating to 'BBB-' once the separation transaction is completed.

Downside scenario

We will likely revise the rating to 'BBB-' at closing. Rating downside would stem from a change in scope of the remaining businesses as well as the projected capital structure or financial policies, such that its adjusted FFO to debt would approach 20%.

Upside scenario

We could revise the outlook to stable if the transaction does not take place, or if a change in the projected capital structure or financial policies for EssentialCo resulted in adjusted FFO to debt comfortably and sustainably exceeding 30%. Improved discretionary cash flow (DCF)-to-debt metrics could also release rating leeway.

Company Description

Incorporated in Belgium, Solvay is one of the largest chemical companies in Europe, selling various specialty, commodity, and intermediate chemicals. At year-end 2022, it reported €13.4 billion of revenue and €2.7 billion adjusted EBITDA. Market capitalization stood at €11.5 billion on June 14, 2023. Solvay benefits from serving diversified global end markets, including auto and aerospace, consumer goods and health care, energy and environment, electronics, building and construction, and industrial applications.

Solvay displays global leadership in a broad range of specialty polymers, and mature commodity product lines. Solvay has been growing its exposure to specialty chemicals following the acquisition of Rhodia in 2011 and Cytec in 2015; the disposal of its European polyvinyl chloride activities in 2016, and of Vinythai and Acetow in 2017; the sale of its polyamide division to BASF at the beginning of 2020, and most recently of Rusvynil in 2023. This has reduced its exposure to cyclical markets and increased its focus on high-growth, high-margin businesses. Solvay's portfolio optimization has reduced profit volatility. Specialty chemicals activities, which are less volatile and more predictable, now represent 70%-75% of EBITDA compared with less than 50% in 2010.

Ratings Score Snapshot

Issuer Credit Rating	BBB/Negative/A-2
Business risk:	Strong
Country risk	Low
Industry risk	Intermediate
Competitive position	Strong
Financial risk:	Significant
Cash flow/leverage	Significant
Anchor	bbb
Modifiers:	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Strong (no impact)
Management and governance	Strong (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile:	bbb

ESG credit indicators: E-2, S-2, G-1

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- 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 And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, 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: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

Ratings List

Ratings Affirmed	
Solvay S.A.	
Issuer Credit Rating	BBB/Negative/A-2
Solvay S.A.	
Senior Unsecured	BBB
Subordinated	BB+
Junior Subordinated	BB+
Cytec Industries Inc.	
Solvay Finance (America) LLC	
Senior Unsecured	BBB
Solvay Finance S.A.	
Junior Subordinated	BB+

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; or Stockholm (46) 8-440-5914