Research Update:

French Automaker Renault Affirmed At 'BB+'; Outlook Still Negative On Delayed Recovery Of Credit Metrics

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Rating Action Overview

- Renault's progress on cost reductions and healthy pricing resulted in better credit metrics than we expected in 2021, including an adjusted EBITDA margin above 6% and lower free operating cash outflow (FOCF) after restructuring and before dividends from RCI.
- Although Renault is exposed to Russia because of its large operations there, we are more concerned about its capacity to maintain sound performance in light of likely supply disruptions, higher input costs, and reliance on the European auto market, which could be hurt by the Russia-Ukraine conflict.
- We are affirming our 'BB+' ratings on Renault and its debt and maintaining our negative outlook.
- The negative outlook indicates that uncertainty on the future of Renault's Russian business and the impact of Russia's military actions in Ukraine on Europe's auto market could lead us to lower our ratings.

Rating Action Rationale

Renault's 2021 performance largely surpassed our expectations. Despite the global supply disruption related to the shortage of semiconductors in the automotive industry, Renault demonstrated the capacity to quickly deliver on its fixed-cost reduction measures and deleveraging targets in 2021. Our adjusted EBITDA margin for Renault was 6.3% versus the 3.5% we previously forecast, and FOCF for its automotive operations was only slightly negative (after restructuring costs and without dividends from RCI) compared with a high three-digit negative figure. We had expected such a recovery would materialize only in 2022-2023. The group took advantage of the global supply shortage and solid demand for individual mobility and improved pricing by 5.7% versus 2020, further supported by the successful launch of new vehicles: Renault Arkana, Dacia Sandero, Dacia Spring, Renault Kangoo Van, and Alpine A110S. The Renault brand expanded the share of electric vehicles (EVs) in Europe to 31% from 20%, and was able to offset the related margin dilution by reducing its cash break-even by 40%.

We expect the recovery of credit metrics to stall in 2022 as a result of geopolitical tensions and further supply chain and cost pressure. Renault's direct exposure to the Russian market is material in terms of sales and production. Russia contributed approximately 500,000 light vehicles to Renault's total production in 2021, about 19% of the total. Most of the locally produced volume is sold under the Lada brand. In 2021, Avtovaz's contribution to Renault's automotive operating margin was as high as 50%, but this is magnified by very low depreciation and amortization. We estimate that the overall impact of the Russian business (including Avtovaz and Renault Russia) on the group's reported EBITDA and cash flow after investments is much lower, within the 10%-15% range. We consider that, in the longer term, Renault's competitive strength will rely more on its ability to establish itself as an EV challenger in the very competitive European market than on its access to the Russian market (1.5 million light vehicle sales per year). Also, we assume Avtovaz has not played a central role in Renault's "Renaulution" cost-cutting plan, which we assume is not substantially impaired by the decision to stop operations in Russia. In the short term, however, Renault's exit from Russia will dent the positive momentum in credit metrics observed during 2021. The group's revised guidance of an operating margin of 3%, down from 4%, reflects in our view expected operating losses of Avtovaz and Renault Russia during disrupted market conditions in Russia. In addition, Renault's other operations focus mainly on Europe and will likely face some supply chain disruptions, and spikes in input costs for energy, raw materials, and many components that well exceed initial expectations. At least for 2022, we continue to assume supply will be the main constraint to sales volumes, but deteriorating economic prospects in Europe may also weaken demand from late 2022 and in 2023. On a positive note, the Russia-Ukraine conflict has so far not impaired Renault's production outside Russia, unlike what we observe at its German peers. In our base-case scenario for Renault, we project adjusted EBITDA margins at about 6% in 2022 and 2023, and that for 2022 adjusted FOCF (after investments and before RCI dividend) would still be in negative territory, assuming the group continues cost reduction efforts to further reduce the break-even.

Renault is not directly exposed to financial liabilities in Russia. We understand that Avtovaz and Renault Russia have borrowings with local banks with gross debt, including bank loans and credit facilities, totaling more than €1.1 billion according to our estimates. We understand no cross-default clauses link the above-mentioned debt to the rest of the group's financial liabilities, and the parent company does not guarantee this debt. We also assume limited exposure of RCI, the group's sales financing business, which holds a 30% stake in RNO Bank, consolidated at equity, and 100% of RNL Leasing, a small leasing company. All in all, we do not expect the Russian exposure will impair RCI's capacity to distribute dividends to its parent company.

No ground-breaking developments expected within the Renault-Nissan-Mitsubishi Alliance. We acknowledge improving relations among the members of the Alliance. At the same time, we do not perceive any tangible additional support to any of the Alliance members' performance from profitable climate transition and technology initiatives beyond what was agreed in the past. Considering the scale of the Alliance versus competing peers like Volkswagen and Stellantis, we see limited strategic and operating tailwinds for Renault from its memberships in the near term.

Outlook

The negative outlook reflects the uncertainty on Renault's capacity to maintain profitability and protect free cash flow amid increasingly uncertain auto market conditions in Europe, as well as high input cost inflation and possible supply chain disruptions related to the Russia-Ukraine conflict. It also reflects delayed recovery of the group's credit metrics linked to the need to absorb the termination of its Russian operations.

Downside scenario

We could lower the rating over the next 12 months if the group's adjusted EBITDA margins and FOCF (after restructuring costs and before dividends paid by RCI) were significantly lower than our forecasts for 2022.

Rating pressure would materialize if EBITDA margins fall and stay below 6%, combined with adjusted debt to EBITDA above 3x and limited prospects for adjusted FOCF to sales of at least 1% from 2023.

We foresee this scenario materializing amid much weaker auto market conditions in Europe or more severe supply chain disruption than anticipated, potentially compounded by muted market acceptance of Renault's new products from 2022 resulting in market share losses in Europe.

Upside scenario

We could revise the outlook to stable if our adjusted EBITDA margins for Renault improved beyond 6% and adjusted FOCF (after restructuring costs and before RCI dividends) to sales was in the 1%-2% range on a sustainable basis.

Company Description

France-based Renault is the third largest automaker in Europe, behind Volkswagen and PSA Group, in terms of the number of cars sold. The company sells cars under seven brands: Renault, Dacia, Lada, Renault Korea Motors, Alpine, Jinbei & Huasong, and EVeasy. Its best-selling models include battery electric Zoe Duster, Sandero, Clio, and Captur. Renault formed an alliance with Nissan in 1999 and holds about 43% of the shares in the venture. Renault's main shareholders are the French government (15%) and Nissan (nonvoting share of 15%), while the remainder of its shares are free floating.

Our Base-Case Scenario

Assumptions

- Volume decrease close to 10% in 2022 and recovering thereafter to 3%-4%.
- Revenue decrease in the 5%-7% range in 2022 and 6%-7% average growth thereafter.
- Group operating margins below 4% in 2022, 4.1% in 2023, and 3.7% in 2024, incorporating:
- --Depreciation and amortization of 8.0%-8.5% of group revenue over 2022-2024,

- --Cash research and development costs rising to 5.8% of revenue in 2024 from 5.1% in 2022, and 45% of capitalization rate and steadily increasing amortization, and
- --Selling, general, and admin expenses representing 10% of group revenue.
- Capital expenditure (capex) of 6.5% of revenue in 2024, up from 5.5% in 2022.
- Dividends from Nissan from 2023.
- Dividends from RCI of €800 million in 2022.
- Dividend payout of 10% of the previous year's net income in 2023 and 15% in 2024.
- Cash restructuring charges of €700 million in 2022 declining to €400 million in 2023-2024.
- Negative working capital over 2022-2024.
- No acquisitions.

Key metrics

Renault S.A.--Key Metrics

	--Year ended Dec. 31--				
Mil. €	**2020a**	**2021a**	**2022e**	**2023f**	**2024f**
Revenue	40,315	43,254	39,000-41,000	44,000-45,000	45,000-46,000
Revenue growth (%)	(22.6)	7.3	(10)-(5)	9-12	2-3
EBITDA	520.0	2,709.0	2,200-2,400	2500-2600	2700-2800
EBITDA margin (%)	1.3	6.3	5.6-5.9	5.7-5.8	6.0-6.1
Funds from operations (FFO)	(207.0)	2,291.0	1,900-2,100	2,100-2,200	2,500-2,600
Capital expenditure	2,808.0	1,905.0	1,300-1,400	1,600-1,700	1,800-1,900
Free operating cash flow (FOCF)*	(4,389.0)	(171.0)	(400)-(300)	250-350	500-600
Debt	5,729.7	4,853.2	5,000-5,200	4,600-4,700	4,000-4,100
Debt to EBITDA (x)	11.0	1.8	2.4-2.1	1.8-1.9	1.5-1.4
FFO to debt (%)	(3.6)	47.2	38-40	45-48	61-65
FOCF to debt (%)	(76.6)	(3.5)	(8)-(5)	5.3-7.5	12-15
FOCF to revenues (%)	(11.0)	(0.4)	(1.0)-(0.7)	0.6-0.8	1.1-1.3

All figures adjusted by S&P Global Ratings. *Does not include RCI dividends. a--Actual. e--Estimate. f--Forecast.

Liquidity

The short-term rating is 'B'. We assess Renault's liquidity as strong, based on our ratio of sources to uses for the industrial division of about 2.8x over the next 12 months and about 2.1x for the subsequent 12 months.

As of Dec. 30, 2021, the industrial division's principal liquidity sources for the next 12 months included:

- Cash and marketable securities of €14.4 billion (after deducting our estimate of €0.5 billion as not immediately accessible for debt repayment).

- Available resources worth €3.4 billion under committed credit facilities maturing after one year.
- Automotive funds from operations of about €2 billion.

The group's principal liquidity uses on the same date included:

- Short-term debt of €3.9 billion in the automotive division.
- Seasonal intrayear working capital swings of up to €0.5 billion annually.
- Capex of €2.5 billion-€3.0 billion per year including capitalized development costs.
- Dividend payments that we assume will resume from 2023.

Environmental, Social, And Governance

ESG credit indicators: To E-2, S-2, G-2; From E-3, S-2, G-3

We have revised the G-score on Renault to G-2 from G-3 to reflect our view of enhanced transparency of financial reporting and communication, with an overall management and governance score unchanged at fair for now.

Issue Ratings--Recovery Analysis

Key analytical factors

- The rating on Renault's unsecured debt is 'BB+', with a '3' recovery rating. The recovery rating is constrained by priority liabilities including factoring, and debt at operating companies. We expect about 55% recovery in the event of a payment default.
- Our hypothetical default scenario contemplates a default in 2027 as the company faces a severe downturn, aggressive competition from new and existing competitors, and a loss of market share.
- We believe that if the company were to default, it would still have a viable business model because of continued demand for its light and commercial vehicles, its established network of dealerships, and strong brand. For this reason, we expect the company would reorganize and emerge with significant value.

Simulated default assumptions

- Simulated year of default: 2027
- EBITDA at emergence: €2.1 billion
- EBITDA multiple: 5.5x

Simplified waterfall

- Net enterprise value (after 5% administrative costs): €11.2 billion

- Priority claims: €5.1 billion
- Total value available to unsecured claims: €6.1 billion
- Senior unsecured debt claims: €10.5 billion
- --Recovery expectations: 50%-70%; rounded estimate 55%

Note: All debt amounts include six months of prepetition interest.

Ratings Score Snapshot

Issuer Credit Rating: BB+/Negative/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: Neutral (No Impact)
- Liquidity: Strong (No Impact)
- Management and governance: Fair (No Impact)
- Comparable rating analysis: Neutral (No Impact)

Stand-alone credit profile: bb+

Related Criteria

- 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
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- 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: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, 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

Ratings List

Ratings Affirmed	
Renault S.A.	
Issuer Credit Rating	BB+/Negative/B
Commercial Paper	B
Senior Unsecured	BB+
Recovery Rating	3(55%)

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