S&P Global
Ratings

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Evonik Industries

Primary Credit Analyst:
Oliver Kroemker, Frankfurt + 49 693 399 9160; oliver.kroemker@spglobal.com

Secondary Contact:
Wen Li, Frankfurt + 49 69 33999 101; wen.li@spglobal.com

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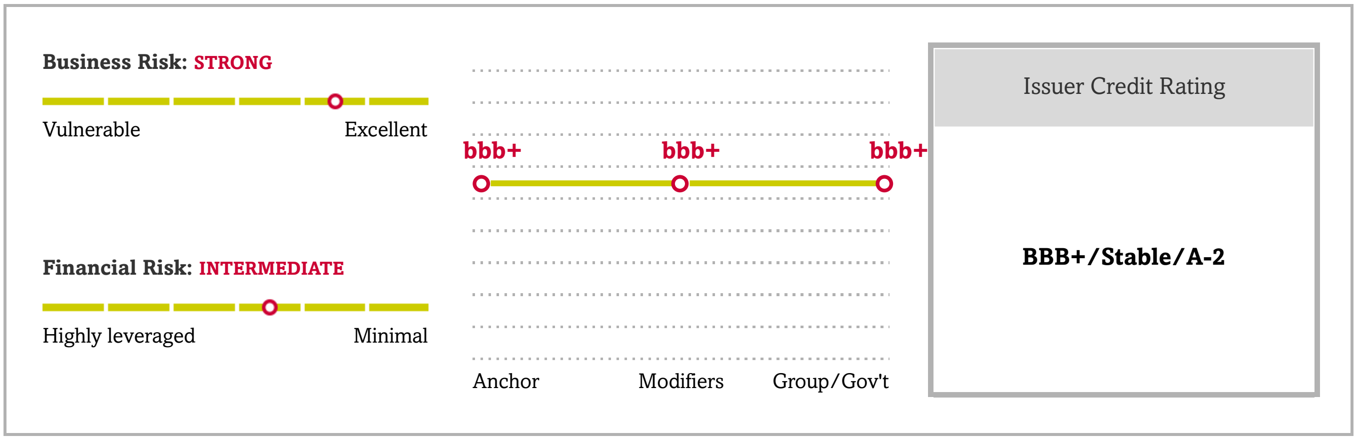
Evonik Industries



Credit Highlights

Overview

Key strengths	Key risks
Leading global specialty-chemicals manufacturer with healthy market positions and 2019 EBITDA of €2.1 billion.	High concentration of revenue from the developed markets of Western Europe and North America (about 65% of 2019 revenue).
Significantly reduced exposure to cyclical and/or commoditized products following disposal of methyl methacrylates (MMA) business.	Cyclicality of some activities and exposure to volatile raw material prices are pressuring overall operating performance.
Average but resilient profitability overall, with potential improvement over the medium term thanks to cost-saving initiatives.	Significant post-retirement obligations and limited flexibility of dividend payments.
Successful integration of recent acquisitions.	
Supportive financial policy and management's commitment to a solid investment-grade rating.	

Evonik Industries maintains moderate headroom under its rating despite market headwinds due to the pandemic. We anticipate that the company's ratio of adjusted funds from operations (FFO) to debt will be in the 30%-35% range at end-2020, recovering further to 35%-40% in 2021. This is down from 40% at year-end 2019 but well within the range of 30%-40% we view as commensurate with the 'BBB+' rating. We forecast €1.8 billion-€2.0 billion EBITDA for 2020, in line with Evonik's guidance for 2020 and compares with the €2.1 billion in 2019. In line with our macroeconomic scenario, we factor in a gradual recovery into 2021.

Resilient performance in growth divisions during 2020. In the first nine months of 2020, Evonik's Performance Materials business was mostly affected by weak demand and pricing for petrochemical derivatives, while its Nutrition and Care division was resilient, due to its exposure to less cyclical end-markets and positive momentum in Animal Nutrition. The company further benefits from measures to support cash flow and adapt cost structures implemented in the second half of 2019 and extended into 2020, and its ongoing structural efficiency measures such as its sales, general, and administrative cost program. EBITDA declined by 10% during this period with the third quarter showing already a sequential earnings recovery.

Self-help measures improving Evonik's cash generation. The company's credit metrics should be supported by its strong focus on keeping or improving its cash conversion rate by capital expenditure (capex) discipline, strict working capital management, lower bonus payments in 2020, and overall strict cost management. We factor in strong S&P Global Ratings adjusted free operating cash flow (FOCF) of about €700 million in 2020 and 2021.

Outlook: Stable

The outlook is stable because we expect Evonik will generate solid adjusted EBITDA of €1.8 billion-€2.0 billion in 2020, despite headwinds due to the COVID-19 pandemic, and above €2.0 billion in 2021. We also factor in Evonik's financial policy commitment to a solid investment-grade rating and anticipate that dividends and acquisitions (if any) will be financed prudently. For 2020, we factor in a ratio of adjusted FFO to debt of 30%-35%, well within the 30%-40% range we view as commensurate with the rating.

Downside scenario

We could lower the ratings if we anticipate that our adjusted FFO to debt would decline below 30% without the near-term prospect of recovery. This could be caused by a significant drop in profit due to a weaker market environment or come through material debt-funded acquisitions.

Upside scenario

Upside rating potential could emerge over time if Evonik can maintain resilient performance via a higher share of specialty chemicals in its product portfolio, visible EBITDA contributions from acquisitions and expansion projects, and a financial track record of adjusted FFO to debt in the 40%-45% range--including increased free cash flow after dividends. A financial policy commitment to a higher rating would be important for any upgrade considerations.

Our Base-Case Scenario

Assumptions

- Global GDP expected to decline by 4.0% in 2020 and rebounding at 5.4% in 2021.
- Revenues to decline by 5%-7% in 2020 versus 2019 due to its exposure to Auto, petrochemical derivatives, and coatings followed by a 4%-6% rebound in 2021.
- We expect S&P Global Ratings' adjusted EBITDA to be €1.8 billion to €2.0 billion for 2020 and above €2 billion in 2021. PeroxyChem and Porocel acquisitions support the EBITDA.
- Dividends of €0.5billion-€0.6 billion per year in 2020-2021.
- Capex of €0.8 billion-€0.9 billion per year.

Key metrics

Evonik Industries--Key Metrics*

	--Fiscal year end Dec. 31--				
(Bil. €)	**2018a**	**2019a**	**2020e**	**2021f**	**2022f**
EBITDA margin (%)	16.1	16.2	15.0-16.0	15.5-16.5	16.0-17.0
Funds from operations (FFO)	2.0	1.8	1.5-1.7	1.6-1.8	1.8-2.0
FFO-to-debt (%)	34.6	40.2	30-35	35-40	35-40

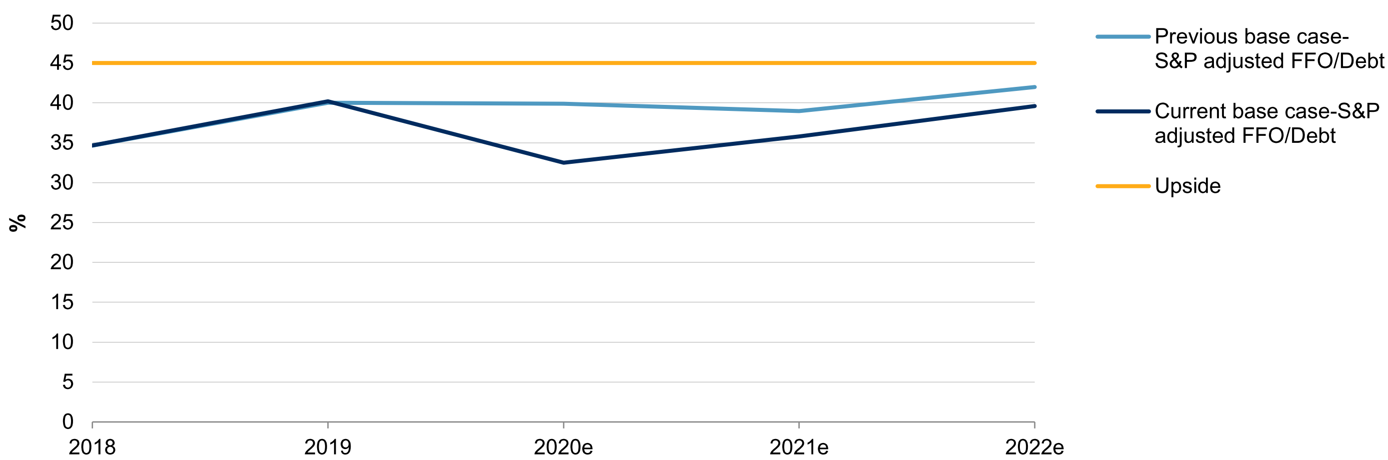
*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast.

The specialty focused strategy is somewhat paying off with credit metrics expected to be within our guided range for the current ratings. In the downturn for cyclical industries and commodity chemicals, less diversified players are heavily affected. We view Evonik as more resilient supported by its cost-cutting measures and steps to realign its portfolio like sale of its MMA business and acquisitions of PeroxyChem and Porocel.

Chart 1

S&P Adjusted FFO/Debt

Credit metrics is positioned within our outlook range



e--Estimate. FFO--Funds from operations. Source: S&P Global Ratings.

Evonik still has significant exposure to automotive and oil derivatives, which weigh on performance in 2020. The company generates about 20% revenue from the mechanical engineering and automotive sector, of which the latter suffered a cyclical slowdown already in 2019 and was also severely affected in 2020 due to COVID-19 countermeasures. The second major factor that is affecting Evonik is its remaining commodity chemical business (C4), where the lower butadiene spreads is heavily affecting the margins of the petrochemicals segment.

Company Description

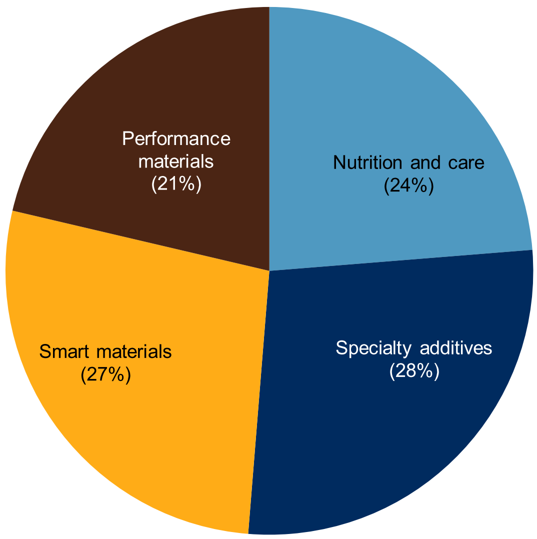
Evonik is one of the leading specialty chemical companies, with about €13 billion of revenue reported in fiscal 2019. Evonik produces products like methionine, cosmetic ingredients, superabsorbent material, silica, polyamide 12, hydrogen peroxide, C4 derivatives, etc.

Evonik has regrouped its businesses into four new divisions:

- Nutrition & Care: Animal nutrition, as well as health and personal care.
- Specialty Additives: Crosslinkers, coating additives, oil additives.
- Smart Material: Silica, catalysts, high performance polymers, etc.
- Performance Material: Baby care, performance intermediates, etc.

Chart 2

New Divisions
Pro-Forma 2019 revenue



Source: S&P Global Ratings.

Peer Comparison

Table 1

Evonik Industries--Peer Comparison					
Industry sector: Chemical companies					
	Evonik Industries	**BASF SE**	**Solvay S.A.**	**Eastman Chemical Co.**	**LANXESS AG**
Ratings as of Dec. 16, 2020	BBB+/Stable/A-2	A/Negative/A-1	BBB/Stable/A-2	BBB-/Stable/A-3	BBB/Stable/A-2
	--Fiscal year ended Dec. 31, 2019--				
(Mil. €)					
Revenue	13,108.0	59,316.0	10,244.0	8,263.4	6,802.0
EBITDA	2,126.0	7,705.0	2,164.0	1,777.8	910.0
Funds from operations (FFO)	1,802.3	6,291.0	1,719.4	1,364.4	662.1
Interest expense	131.7	807.0	260.6	207.5	90.0
Cash interest paid	114.7	515.0	181.6	220.0	55.0
Cash flow from operations	1,287.3	7,439.0	1,361.4	1,392.1	605.0
Capital expenditure	872.0	3,789.0	716.0	375.2	508.0

Table 1

Evonik Industries--Peer Comparison (cont.)

Industry sector: Chemical companies

	Evonik Industries	BASF SE	Solvay S.A.	Eastman Chemical Co.	LANXESS AG
Free operating cash flow (FOCF)	415.3	3,650.0	645.4	1,016.9	97.0
Discretionary cash flow (DCF)	(155.0)	586.0	(533.0)	421.6	(193.0)
Cash and short-term investments	2,368.0	2,871.0	809.0	181.8	1,160.0
Debt	4,472.3	23,974.2	6,470.6	6,013.8	2,290.0
Equity	9,308.5	42,350.0	8,724.0	5,375.2	2,892.0
Adjusted ratios					
EBITDA margin (%)	16.2	13.0	21.1	21.5	13.4
Return on capital (%)	8.3	5.9	7.5	9.9	8.7
EBITDA interest coverage (x)	16.1	9.5	8.3	8.6	10.1
FFO cash interest coverage (x)	16.7	13.2	10.5	7.2	13.0
Debt/EBITDA (x)	2.1	3.1	3.0	3.4	2.5
FFO/debt (%)	40.3	26.2	26.6	22.7	28.9
Cash flow from operations/debt (%)	28.8	31.0	21.0	23.1	26.4
FOCF/debt (%)	9.3	15.2	10.0	16.9	4.2
DCF/debt (%)	(3.5)	2.4	(8.2)	7.0	(8.4)

Business Risk: Strong

Evonik's business risk profile is underpinned by the size and strong market position of its specialty chemicals activities, as well as global market reach. The specialty business portfolio was further strengthened by the sale of the mature and cyclical MMA business and acquisitions of PeroxyChem and more recently Porocel, a U.S.-based company active in the field of desulfurization catalysts and absorbents.

Evonik benefits from greater diversity in terms of end markets and product ranges than most of its peers, while at the same time there are limited synergies between its business units. About one quarter of its sales comes from nutrition and care products, about 20% from the more cyclical auto end markets and has well-diversified exposure toward other end markets. The group also has a good track record in research and development, which accounts for 3.0%-3.5% of its annual sales.

We view Evonik's profitability as average within the specialty chemicals industry, supported by efficiency programs in groupwide selling, general, and administrative (SG&A) functions. The cost position for 2020-2021 is further supported by much lower one-time costs and acceleration in its SG&A saving program by about a year.

The company's exposure to commoditized and/or cyclical products including amino acids, C4 derivatives, and superabsorbers for baby care has materially reduced compared with a few years ago, due to the company's portfolio management and as methionine prices have reached a historical low level, having reduced the share of EBITDA contribution of this single product substantially. We view these trends as having improved Evonik's portfolio quality, given the higher volatility of these products compared with the rest of its offerings and their sensitivity to economic cycles and supply-demand balances. Accordingly, the proportion of specialty businesses in Evonik's portfolio has increased to about 80% of EBITDA which should result in somewhat lower earnings volatility going forward.

We note the enhancements to portfolio quality thanks to recent acquisitions, and recognize Evonik's strategy to accelerate growth and attain a sustainable EBITDA margin of 18%-20% on average over the cycle through cost efficiencies and a further shift toward specialty chemicals. In our view, a track record of sustainably better and stable margins would be a key indication of the strengthening business profile.

Financial Risk: Intermediate

Our view of Evonik's financial risk profile takes into account our forecast of adjusted FFO to debt of 30%-35% in 2020 under our base-case scenario, down from 40% at year-end 2019. This leaves the company with some moderate headroom which should expand in 2021 on the back of an anticipated operational recovery and continued strong FOCF generation to 35%-40%.

We expect an EBITDA decline of about 10% in 2020 versus 2019. But even with the expected decline, we expect significant improvement in FOCF supported by the management's focus on improving Evonik's cash conversion rate by cutting capex, strict working capital management, and lower bonus payments. We expect Evonik will generate strong FOCF of about €0.7 billion in 2020-2021.

We note Evonik's financial policy commitment to a solid investment-grade rating and assume that capex, dividends, and future acquisitions (if any) will be balanced appropriately or prudently funded, as demonstrated in previous transactions.

Financial summary

Table 2

Evonik Industries--Financial Summary					
Industry sector: Chemical companies					
	--Fiscal year ended Dec. 31--				
	2019	**2018**	**2017**	**2016**	**2015**
(Mil. €)					
Revenue	13,108.0	15,024.0	14,419.0	12,732.0	13,507.0
EBITDA	2,126.0	2,414.0	2,361.0	2,194.0	2,433.0
Funds from operations (FFO)	1,802.3	1,991.2	1,891.1	1,570.7	1,999.5
Interest expense	131.7	155.8	167.9	164.3	173.5
Cash interest paid	114.7	155.8	156.9	131.3	97.5
Cash flow from operations	1,287.3	1,783.2	1,624.1	1,819.7	2,019.5
Capital expenditure	872.0	1,026.0	1,036.0	942.0	908.0
Free operating cash flow (FOCF)	415.3	757.2	588.1	877.7	1,111.5
Discretionary cash flow (DCF)	(155.0)	182.9	16.4	317.7	620.5
Cash and short-term investments	2,368.0	1,128.0	1,163.0	4,940.0	2,733.0
Gross available cash	2,368.0	1,068.0	1,052.0	4,668.0	2,655.0
Debt	4,472.3	5,747.4	5,770.6	2,176.8	1,829.1

Table 2

Evonik Industries--Financial Summary (cont.)

Industry sector: Chemical companies					
	--Fiscal year ended Dec. 31--				
	2019	**2018**	**2017**	**2016**	**2015**
Equity	9,308.5	8,073.0	7,777.0	7,750.0	7,576.0
Adjusted ratios					
EBITDA margin (%)	16.2	16.1	16.4	17.2	18.0
Return on capital (%)	8.3	10.7	11.7	13.4	15.4
EBITDA interest coverage (x)	16.1	15.5	14.1	13.4	14.0
FFO cash interest coverage (x)	16.7	13.8	13.1	13.0	21.5
Debt/EBITDA (x)	2.1	2.4	2.4	1.0	0.8
FFO/debt (%)	40.3	34.6	32.8	72.2	109.3
Cash flow from operations/debt (%)	28.8	31.0	28.1	83.6	110.4
FOCF/debt (%)	9.3	13.2	10.2	40.3	60.8
DCF/debt (%)	(3.5)	3.2	0.3	14.6	33.9

Reconciliation

Table 3

Evonik Industries--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €)

	--Fiscal year ended Dec. 31, 2019--								
Evonik Industries reported amounts									
	Debt	**Shareholders' equity**	**EBITDA**	**Operating income**	**Interest expense**	**S&P Global Ratings' adjusted EBITDA**	**Cash flow from operations**	**Dividends**	**Capital expenditure**
Reported	3,805.0	8,970.0	2,128.0	1,081.0	63.0	2,126.0	1,352.0	548.0	880.0
S&P Global Ratings' adjustments									
Cash taxes paid	--	--	--	--	--	(209.0)	--	--	--
Cash interest paid	--	--	--	--	--	(114.0)	--	--	--
Reported lease liabilities	650.0	--	--	--	--	--	--	--	--
Intermediate hybrids reported as debt	(248.5)	248.5	--	--	(5.3)	5.3	5.3	5.3	--
Postretirement benefit obligations/deferred compensation	2,510.0	--	(7.0)	(7.0)	68.0	--	--	--	--
Accessible cash and liquid investments	(2,268.0)	--	--	--	--	--	--	--	--
Capitalized interest	--	--	--	--	6.0	(6.0)	(6.0)	--	(6.0)
Capitalized development costs	--	--	(2.0)	(2.0)	--	--	(2.0)	--	(2.0)
Dividends received from equity investments	--	--	15.0	--	--	--	--	--	--

Table 3

Evonik Industries--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. €) (cont.)									
Nonoperating income (expense)	--	--	--	17.0	--	--	--	--	--
Reclassification of interest and dividend cash flows	--	--	--	--	--	--	(62.0)	--	--
Noncontrolling interest/minority interest	--	90.0	--	--	--	--	--	--	--
Debt: Guarantees	23.8	--	--	--	--	--	--	--	--
EBITDA: Gain/(loss) on disposals of PP&E	--	--	(12.0)	(12.0)	--	--	--	--	--
EBITDA: Foreign exchange gain/(loss)	--	--	4.0	4.0	--	--	--	--	--
Depreciation and amortization: Impairment charges/(reversals)	--	--	--	63.0	--	--	--	--	--
Total adjustments	667.3	338.5	(2.0)	63.0	68.7	(323.7)	(64.7)	5.3	(8.0)
S&P Global Ratings' adjusted amounts									
	Debt	**Equity**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from operations**	**Cash flow from operations**	**Dividends paid**	**Capital expenditure**
Adjusted	4,472.3	9,308.5	2,126.0	1,144.0	131.7	1,802.3	1,287.3	553.3	872.0

PP&E--Plant, property and equipment.

Liquidity: Strong

Our short-term issuer credit rating on Evonik remains at A-2. We view Evonik's liquidity as strong based on our estimate that sources will exceed uses by 1.8x over the 12 months from Sept. 30, 2020, and 2.5x over the subsequent 12 months. Evonik's debt documentation does not include any covenants and the group has a track record of addressing its maturities well ahead of time.

Principal liquidity sources

- At Sept. 30, 2020, about €1 billion of cash and €0.6 billion of marketable securities.
- A €1.75 billion undrawn revolving credit facility (RCF) maturing in 2024. The facility is not subject to any financial covenants.
- FFO of €1.5 billion-€1.6 billion over the next 12 months, according to our base-case credit scenario.

Principal liquidity uses

- Short-term debt of €1.0 billion at Sept. 30, 2020.
- Assumed capex of €0.8 billion-€0.9 billion.
- US$210 million for the acquisition of Porocel Group, completed in November 2020.
- Dividends of €0.5 billion-€0.6 billion.
- Moderate working capital outflows of about €0.1 billion in the next 12 months, including €0.1 billion of peak intrayear working capital needs.

Environmental, Social, And Governance

We consider Evonik's exposure to environmental risk factors as on par with the chemical sector. The company has established a groupwide environment, safety, health, and quality management system based on statutory and normative frameworks, including ISO standards, the UN Sustainable Development Goals, and internal regulations.

Scope 1 Green House Gas (GHG) emissions fell 13% in 2019, mainly due to Evonik's divestment of its MMA business. As a result, the company achieved its environmental target for 2012-2020, one year ahead of schedule. The company remains committed to its target of 50% reduction in absolute Scope 1 and 2 emissions by 2025 versus 2008 levels and remains committed to the Paris Agreement on Climate Change.

In addition, Evonik introduced internal CO2 pricing as additional criteria in the management of major investments. Evonik uses co-generation plants at several of its large sites. It announced plans to replace the last coal-fired power plant at its Marl site by 2022 and to build a new reserve power plant. Moreover, the company has integrated structures linking chemical production and energy generation. The company also generates more than 30% of its sales with products and solutions that exceed or even significantly exceed market reference in terms of their positive sustainability profile. We believe social factors are currently not a material risk for the rating. Furthermore, we view Evonik's governance as a supportive factor for the ratings, reflecting management's experience and expertise, governance fully in line with best practices, and the balance of different stakeholders' interests.

Ratings Score Snapshot

Issuer Credit Rating

BBB+/Stable/A-2

Business risk: Strong

- **Country risk:** Low
- **Industry risk:** Intermediate
- **Competitive position:** Strong

Financial risk: Intermediate

- **Cash flow/leverage:** Intermediate

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)

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 And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, 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

- Industry Top Trends 2021 Chemicals, Dec. 10, 2020
- Top 20 EMEA Chemical Companies And COVID-19: The Credit Impact Relies Largely On Subsector Exposures And Responses, Oct. 22, 2020
- Issuer Ranking: EMEA Chemical Companies, Strongest To Weakest, Aug. 21, 2020
- Q&A: EMEA Chemicals Face A Long Climb Back From COVID-19 Disruption, June 29, 2020
- Industry Top Trends Update: EMEA Chemicals July 16, 2020
- ESG Industry Report Card: Chemicals, Feb. 11, 2020

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-

Ratings Detail (As Of December 16, 2020)*

Evonik Industries	
Issuer Credit Rating	BBB+/Stable/A-2
Senior Unsecured	BBB+
Short-Term Debt	A-2
Subordinated	BBB-
Issuer Credit Ratings History	
09-May-2012	BBB+/Stable/A-2
06-May-2011	BBB/Stable/A-2
21-Sep-2010	BB+/Positive/B

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@spglobal.com