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MAN SE

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Major Rating Factors

Corporate Credit Rating
BBB+/Stable/A-2

Strengths:

- Strong market positions in commercial vehicles in Europe and South America.
- Leading market positions in diesel engines.
- High financial flexibility.
- Diversification supported by business units prone to different economic cycles.

Weaknesses:

- Operations within industries characterized by high volatility, cyclicality, and capital intensity.
- Structural problems within the bus industry, which can negatively affect the bus division.
- Generally mature and competitive markets.
- High fixed-cost base for some operations.

Rationale

The ratings on Germany-based diversified industrial company MAN AG are underpinned by our view of the group's leading market positions in heavy trucks in Europe and South America, strong market positions in diesel engines and turbo machinery, ability to generate good free operating cash flow, and solid geographic diversification. We consider the ratings tempered however, by the capital intensity and pronounced cyclicality of MAN's end markets, notably commercial vehicles, and the challenging market conditions for its bus segment. We view the group's business risk profile as "satisfactory" and the financial risk profile as "modest" (for details on our business risk profile methodology, see "Criteria Methodology: Business Risk/Financial Risk Matrix Expanded," published May 27, 2009).

Key business and profitability developments

In 2009, MAN reported sharply lower operating profits. The operating margin before depreciation (excluding investment income) was 2.3% after 9.8% in the comparable period. This also compares to peak-of-the-cycle margins of 10%-11% achieved in 2007-2008.

The negative margin development is mostly attributable to significantly lower volume sales and low capacity utilization in the truck division. Order intake for trucks (in unit terms) was down 48% in 2009, reflecting low levels of industrial production, which in turn implies low freight volumes and low truck utilization in customers' fleets. MAN's Power Engineering unit (diesel and turbo) performed solidly in 2009, with margins slightly below the levels of 2008. Order intake in the late-cyclical Power Engineering unit showed declines of about one-third in 2009. Order backlog in the division provides some visibility for 2010 but we believe that lower order activity will eventually lead to a weaker earnings and cash contribution for the group.

Standard & Poor's Ratings Services expects orders in the European truck industry to show only moderate improvements in 2010 and our rating on MAN includes the assumption of a mid- to high-single-digit growth of the

European truck market in 2010.

For 2010, MAN expects sales and operating profit at similar levels to 2009. We are likewise working under the assumption of stable operating profits, mostly supported by the €700 million cost-reduction program completed in 2009 but also moderate declines in profitability at the Power Engineering unit. For the commercial vehicles division, we expect a positive operating margin, mostly due to lower under-absorption of costs, lower residual value charges, and the benefits from the cost-reduction program. For the group, we expect a low- to mid single-digit EBIT margin in 2010.

Key cash flow and capital-structure developments

In 2009, MAN's credit protection measures deteriorated markedly. Funds from operations (FFO) to debt and debt to EBITDA were down to 14% and 2.4x from levels of 300% and 0.3x in 2008. The deterioration is mostly attributable to lower operating earnings and, consequently, lower cash generation. Group debt increased in 2009 following the acquisitions of Sinotruck (payout of €0.6 billion) and the Volkswagen truck unit (€1.3 billion), only partly counterbalanced by the disposal proceeds for Ferrostaal. Free operating cash flow (FOCF) in 2009 was solid, partly supported by good management of capital expenditures, release of working capital, but also a reduction of the captive finance asset portfolio. The group, including captive finance, generated FOCF of about €1.1 billion. FOCF in the industrial unit, excluding the acquisition and disposal of business units, was €855 million. For 2010, MAN has guided for FOCF of at least €500 million, a figure that we view as attainable. Under our base case projections, financial debt protection measures such as FFO to debt and debt to EBITDA are expected to be commensurate with the rating in 2010 and beyond.

We still do not factor into the ratings a closer cooperation with Sweden-based truck manufacturer Scania (publ.) AB (A-/Negative/A-2). While we consider a truck alliance involving Scania and MAN to be possible, we have no information that indicates the heightened risk of such a transaction taking place over the short term.

Liquidity

We consider MAN's liquidity to be strong, underpinned by cash and marketable securities of about €0.6 billion in its industrial unit as of Dec. 31, 2009. The group has availability under a €2.0 billion variable-rate revolving credit facility (RCF), which was granted by a consortium of 25 banks and expires in December 2011. We understand that this RCF has a change-of-control clause but no financial covenants or rating triggers. This facility was unused as of Dec. 31, 2009. The group's liquidity position is also supported by an undrawn committed €300 million credit facility from the European Investment Bank, due in 2015, and bilateral credit lines of about €0.5 billion with different banks. The bilateral credit lines are mostly due in 2010.

In 2010, we believe MAN's capacity to serve its outstanding debt should be supported by FOCF. On Dec. 31, 2009, short-term maturities in its industrial unit consisted of a €0.2 billion bond due in December 2010. MAN's funding sources considerably exceed upcoming debt maturities in the medium term. MAN's debt maturities in its financial services division are matched with the underlying assets.

In March 2009, MAN drew down €1.5 billion on a €2.0 billion syndicated bank facility that was arranged in conjunction with the acquisition of the Volkswagen truck business. In mid-May 2009, the €1.5 billion drawdown was paid off with a €1.5 billion bond placement. The remaining availability under MAN's €5.0 billion EMTN program is €3.5 billion. We understand that bank lines are not subject to financial covenants, rating triggers, or material adverse change clauses.

MAN's decision to reduce dividend payments for 2009 is likewise instrumental to preserve liquidity, in our view.

Outlook

The stable outlook reflects our view that MAN will improve its group operating margin in the industrial division to a mid-single-digit level in 2010 and markedly improve its debt protection measures. This is based on our expectations of an increase in production by MAN and a moderate recovery of the truck market in Europe. To remain commensurate with the ratings, we would expect the industrial business to generate FFO of about 40% of industrial debt and industrial debt to EBITDA to be no higher than 2.0x. We believe that MAN would be able to exceed these ratios comfortably in a cyclical upturn. In a cyclical downturn, we believe it could recover to these levels within 18-24 months. We could lower the ratings if the company increases its industrial debt leverage beyond these levels or if its liquidity situation deteriorates. Our view on the group's business risk profile limits upside rating potential in the short term, assuming no major change to MAN's business model and business mix.

Business Description

MAN, based in Munich, is a listed industrial engineering group. The group comprises three core business areas: Commercial Vehicles (trucks and buses), Diesel Engines, and Turbo Machinery. MAN also has a majority stake in RENK, a producer of power transmissions, and a captive finance unit for its truck business (MFI).

Over the past few years, MAN has undertaken massive reconfiguration efforts and refocused the group on transport-related engineering products. The divestiture of its industrial services division Ferrostaal, announced in December 2008, was a continuation of the portfolio reconfiguration.

Business Risk Profile: Underpinned By Solid Market Positions And Geographic Diversification

The major supports for MAN's "satisfactory" business risk profile, according to our classifications, are:

- Solid and stable market positions in commercial vehicles in Europe and a strong position in South America. MAN is the third-largest heavy truck producer in Europe behind Volvo (publ), AB (BBB-/Negative/A-3) and Daimler AG (BBB+/Negative/A-2). The group is likewise a well positioned player in the market for medium-duty trucks. Over the past three years, MAN maintained a market share of about 16% in the 27 states of the EU, slightly ahead of Scania.

- Strong market position for diesel engines. MAN is the global market leader for two-stroke marine engines for the propulsion of large low-speed vessels and has maintained consistently high market shares between 77% and 90% over the past few years. In the market for four-stroke engines, MAN mainly competes with Finland-based Wärtsiliä (not rated), U.S.-based Cummins Inc. (BBB/Stable/--), and Caterpillar Inc. (A/Negative/A-1), and has kept a market share of about one-third over the past few years.

- The solid market position of MAN Turbo. This has as global market share of about one-fifth in a fairly concentrated market for turbo compressors and primarily competes with three industry players: Dresser-Rand Group Inc. (BB/Stable/--), GE Oil & Gas, a division of General Electric Co. (AA+/Stable/A-1+), and Siemens PGI.

- Solid geographic diversification due to the group's broad regional sales and increasing presence in the emerging economies of India and China. The Diesel Engine division has a high share of business in China, Japan, and Korea. The Turbo division has a solid share of business in the Middle East and China.
- Product and divisional diversification. The organizational set-up, with both early cyclical products (trucks) and late-cyclical products (diesel engines and turbo compressors) is supportive of the rating.
- Ability to generate solid profitability. Before the sharp downturn since fall 2008, MAN markedly improved profitability through structural cost improvements, the turnaround of its bus division, and divestiture of nonstrategic assets. In 2009, group profitability declined markedly mainly because of the sharp volume decline in the truck unit and the related margin compression. Operating margins in the late-cycle units, Diesel and Turbo, however, held up in 2009.
- Certain degree of cost flexibility. MAN has demonstrated an ability to adapt to strong volume swings in its truck unit. The unit (excluding the Latin American business) had a slightly negative operating result in 2009. Operating losses could have been worse without cost flexibility, notably given the volume decline of more than 50% in 2009.

These supports, however, may be challenged by:

- High volatility, cyclicality, and capital intensity. The cyclical nature of MAN's end markets, notably commercial vehicles, can severely affect profitability levels. European registrations for heavy-duty trucks tend to be cyclical, albeit not nearly to the same extent as in North America. The global bus industry, in particular, is subject to high volatility and event risk.
- Structural problems within the bus industry, which can negatively affect the bus division. The bus unit's business risk assessment is considerably below the group average. The global bus industry faces a number of challenges, including industry-wide overcapacity and low component commonality. Industry-wide profit margins are low at about 2%-4%.
- Generally mature and competitive markets in which MAN operates.
- High fixed-cost base for some operations.

Financial Risk Profile: History Of Solid Cash Generation And A Cautious Shareholder Remuneration Policy

The main strengths of MAN's modest financial risk profile are:

- Good FOCF generation management. MAN showed a solid FOCF and FFO in the economically strong years of 2006 and 2007. In 2008, FOCF was still positive at about €0.1 billion, although down from €1.3 billion in 2007. FOCF in the industrial business in 2009 was about €0.9 billion and considerably exceeded the reduced dividend payment (€0.3 billion). For 2010, MAN expects a FOCF of at least €500 million, again considerably above the dividend payment in 2010 (about €37 million).
- High financial flexibility. Strong liquidity is supported by cash and marketable securities of about €0.6 billion in its industrial unit and an unused €2.0 billion variable-rate revolving credit facility (RCF) available as of Dec. 31,

2009 free of covenants. Short-term maturities in the industrial unit are safely covered with existing liquidity and available committed lines.

- A solid maturity profile, with low short-term maturities after refinancing activities in early 2009. The placement of two bonds in May 2009 with four- and seven-year maturities and total proceeds of €1.5 billion has extended the company's maturity profile. The bond proceeds were used to pay off the bank facility that was used to pay for the acquisition of the Volkswagen Brazil truck business.
- Conservative to moderate dividend policy and conservative shareholder remuneration policy. Over the past years, MAN has refrained from share buybacks and does not appear to be in favor of this type of shareholder remuneration. Historically, dividend payouts were about 40%-50% of net income. As a result of the unfavorable market developments, MAN cut the dividend by about 35% in 2009 and further reduced dividend payments in 2010 to very low levels.
- Conservative financial policy and financial targets. MAN's financial policy targets a level of indebtedness of about 1.0x EBITDA and a maximum of about 2.5x EBITDA in case of major acquisitions. At this stage, no large acquisition other than a potential cooperation or acquisition of rival truck maker Scania appears likely in the medium term. We have, however, neither an indication nor the impression that any such transaction will materialize in the near future.

One factor moderating these strengths is MAN's exposure to generally highly cyclical commercial-vehicle industry, which can lead to strong fluctuations in cash flow generation.

Financial Statistics/Adjustments

MAN reports according to international financial reporting standard (IFRS). In its assessment of a company's financial leverage, Standard & Poor's takes into account off-balance-sheet liabilities, such as operating leases, guarantees, pension obligations, and securitizations. In MAN's case, the majority of adjustments relate to our captive finance methodology (see table 1).

Table 1

Reconciliation Of MAN SE Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. €)*

	--Fiscal year ended Dec. 31, 2009--					
MAN SE reported amounts						
	Debt	**Shareholders' equity**	**Operating income (before D&A)**	**Operating income (after D&A)**	**Cash flow from operations**	**Cash flow from operations**
Reported	3,270	5,079	590	(214)	1,349	1,349
Standard & Poor's adjustments						
Operating leases	725	--	32	32	162	162
Postretirement benefit obligations	104	--	3	3	(18)	(18)
Surplus cash and near cash investments	(289)	--	--	--	--	--
Capitalized development costs	--	--	(68)	(17)	(68)	(68)

Table 1

Reconciliation Of MAN SE Reported Amounts With Standard & Poor's Adjusted Amounts (Mil. €)* (cont.)						
Share-based compensation expense	--	--	6	--	--	--
Deconsolidation / Consolidation	(1,697)	(242)	34	(28)	(242)	36
Reclassification of nonoperating income (expenses)	--	--	--	49	--	--
Reclassification of working-capital cash flow changes	--	--	--	--	--	(1,172)
Minority interests	--	50	--	--	--	--
Non-recurring items	--	--	276	(70)	--	--
Total adjustments	(1,157)	(192)	283	(30)	(167)	(1,061)
Standard & Poor's adjusted amounts						
	Debt	**Equity**	**EBITDA**	**EBIT**	**Cash flow from operations**	**Funds from operations**
Adjusted	2,113	4,887	873	(244)	1,182	288

*Please note that two reported amounts (operating income before D&A and cash flow from operations) are used to derive more than one Standard & Poor's-adjusted amount (operating income before D&A and EBITDA, and cash flow from operations and funds from operations, respectively). Consequently, the first section in some tables may feature duplicate descriptions and amounts.

We make the following adjustments to MAN's financial position:

- Surplus cash and near cash investments. The balance of cash and cash equivalents reported for the industrials division (€589 million) is adjusted for the cash needs for ongoing operations (€300 million) to arrive at the cash balance that we deduct from reported debt.
- Capitalized development costs: We adjust reported financial statements for capitalized development costs. As a result, the methodology of expensing these costs leads us to decrease operating cash flows and FFO for the costs capitalized in the period (i.e., these are treated as an operating cost rather than capital expenditure) and reduce EBITDA and EBIT. In the year ended Dec. 31, 2009, MAN capitalized and amortized €68 million and €51 million of development costs, respectively.
- Deconsolidation captive finance: According to Standard & Poor's practice for companies with financial service operations, we analytically separate the group's industrial operations from its financial-service operations. The financial statistics published by Standard & Poor's refer to both the consolidated figures and the industrial data. We consider MAN's portfolio of receivables to be of strong quality. Hence, we determined a financial services debt leverage factor of seven-to-one as appropriate. This means that the captive finance company assets of €1.9 billion as of Dec. 31, 2009 (€2.2 billion as of Dec. 2008), were represented by €1.7 billion of debt and €0.2 billion of equity. For further details see the article "Credit FAQ: How Standard & Poor's Adjustments To Automotive Firms' Captive Finance Operations Affect Daimler AG," published on July 11, 2008, on RatingsDirect).
- Nonrecurring items: This line includes a variety of nonrecurring items and losses from investees carried at equity.

Table 2

MAN SE--Peer Comparison*

Industry Sector: Automotive - Parts Producers & Suppliers

	MAN SE	Atlas Copco AB	Scania (publ.) AB	Daimler AG
Corporate credit rating¶	BBB+/Stable/A-2	A-/Stable/A-2	A-/Negative/A-2	BBB+/Negative/A-2
(Mil. €)	**--Average of past three fiscal years--**			
Revenues	13,678	6,557	7,696	82,268
Net income from cont. oper.	605	767	608	1,282
Funds from operations (FFO)	1,327	979	901	2,188
Capital expenditures	678	225	430	1,779
Debt	915	2,298	836	8,335
Equity	4,918	2,057	1,792	26,469
Adjusted ratios				
Oper. income (bef. D&A)/revenues (%)	12.2	20.5	14.5	6.9
EBIT interest coverage (x)	12.7	9.7	11.5	4.7
EBITDA interest coverage (x)	18.8	10.9	14.3	6.3
Return on capital (%)	17.1	27.5	32.9	10.4
FFO/debt (%)	145.0	42.6	103.8	26.3
Debt/EBITDA (x)	0.6	1.8	0.8	1.5
Total debt/debt plus equity (%)	15.7	52.6	32.6	23.9

*Fully adjusted (including postretirement obligations). Excess cash and investments netted against debt. ¶Ratings as of April 23, 2010. N.M.--Not meaningful.

Table 3

MAN SE--Financial Statistics*

Industry Sector: Automotive - OEM'S

	--Fiscal year ended Dec. 31--				
(Mil. €)	**2009**	**2008**	**2007**	**2006**	**2005**
Rating history	A-/Watch Neg/A-2	A-/Stable/A-2	-/-/-	-/-/-	-/-/-
Revenues	12,026	14,945	14,063	13,049	11,079
Net income from continuing operations	(396)	1,141	1,070	743	405
Funds from operations (FFO)	288	1,939	1,754	669	516
Capital expenditures	614	806	614	390	291
Debt	2,113	633	0	1,168	832
Equity	4,887	4,925	4,943	3,963	2,802
Adjusted ratios					
Oper. income (bef. D&A)/revenues (%)	8.6	13.9	13.4	10.3	3.9
EBIT interest coverage (x)	(1.4)	(592.2)	21.6	8.4	1.8
EBITDA interest coverage (x)	5.0	(633.0)	24.7	9.3	3.2
Return on capital (%)	(3.6)	31.1	28.2	24.2	4.6
FFO/debt (%)	13.7	306.2	N.M.	57.3	62.0
Debt/EBITDA (x)	2.4	0.3	0.0	0.9	2.3
Debt/debt and equity (%)	30.2	11.4	0.0	22.8	22.9

*Fully adjusted (including postretirement obligations). Excess cash and investments netted against debt.

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Related Research

- "Credit FAQ: How Standard & Poor's Adjustments To Automotive Firms' Captive Finance Operations Affect Daimler AG," July 11, 2008.
- "Criteria Methodology: Business Risk/Financial Risk Matrix Expanded," published May 27, 2009.

Ratings Detail (As Of April 23, 2010)*	
MAN SE	
Corporate Credit Rating	BBB+/Stable/A-2
Senior Unsecured (3 Issues)	BBB+
Corporate Credit Ratings History	
07-Apr-2010	BBB+/Stable/A-2
03-Dec-2009	A-/Watch Neg/A-2
04-Feb-2008	A-/Stable/A-2
Business Risk Profile	Satisfactory
Financial Risk Profile	Modest
Debt Maturities	
As of Dec. 31, 2009 (including customer financing): 2010: € 1,040 mil. 2011-2014: € 1,710 mil. 2015 and beyond: €520 mil.	

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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