

Research Update:

MAN SE 'A-' Long-Term Rating On CreditWatch Negative After CEO And CFO Resignations And On Review Of Business Risk

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Overview

- The recent resignation of MAN's CEO and CFO casts uncertainty over its future financial direction and constitutes risks for the rating, in our view.
- We are placing the 'A-' long-term rating on CreditWatch Negative.
- Our resolution of the CreditWatch could also be influenced by developments regarding the ongoing investigations by German prosecutors on suspicion of alleged bribery at MAN.
- The outcome of the CreditWatch could also be linked to our ongoing review of MAN's business risk profile given our opinion of the currently weak state of the truck sector.

Rating Action

On Dec. 3, 2009, Standard & Poor's Ratings Services placed its 'A-' long-term corporate credit rating on Germany-based diversified industrial company MAN SE on CreditWatch with negative implications. At the same time, the 'A-2' short-term corporate credit rating was affirmed.

Rationale

The CreditWatch placement follows the resignations of the CEO Hakan Samuelsson, CFO Karlheinz Hornung, and head of the commercial vehicles division Anton Weinmann over the past few days. It also reflects our ongoing review of MAN's business risk profile given our opinion of the currently weak state of the truck sector.

The resignations were each at the individual's own request, according to MAN. The company says the resignations are not related to the investigations into the bribery allegations against the company that have been conducted by German prosecutors since spring 2009. We also understand that the individuals who resigned have not been personally accused by prosecutors.

In our opinion, the departure of the CEO and CFO creates uncertainty about MAN's strategic and business execution as well as the company's future strategic direction and financial policy. For the interim, Georg Pachta-Reyhofen, currently CEO of MAN Diesel, will assume responsibility as CEO of MAN SE. We expect that the successors will be appointed in MAN's next supervisory board meeting on Dec. 11, 2009.

We cannot assess to what extent the management upheaval is related to a possible truck alliance involving Scania (publ.) AB (A-/Negative/A-2) and MAN.

Although we have no information to indicate that such a transaction may take place in the short term, we believe the likelihood of any such transaction materializing still exists, even though we consider it neither quantifiable nor estimable to any degree. We might take negative rating actions on MAN if Scania and MAN were to possibly combine, depending on the structure of any such transaction.

The ratings on MAN reflect our assessment of the group's leading market positions, ability to generate good free operating cash flow, and solid geographic diversification. The ratings are tempered by our view of the capital intensity and pronounced cyclicity of MAN's end markets, notably commercial vehicles, and the continuously challenging market conditions for its bus segment.

MAN reported sharply lower operating profits in the first three quarters of 2009. The operating margin before depreciation (excluding investment income) was about 4% after 12% in the comparable period of 2008. This year's low margin likewise compares with peak-of-cycle margins of 10%-11% achieved in 2007-2008. For 2009, we continue to expect a low- to mid-single-digit EBIT margin for the group.

We consider MAN's underlying financial performance to be in line with our expectations. We expect MAN to show funds from operations (FFO) to debt of slightly below 40% for 2009. Debt to EBITDA will most likely be about 2.6x in 2009, in our estimation, which is weak for the rating. Our current base case assumes that FFO to debt is likely to exceed 40% in 2010 and that debt to EBITDA could fall below 2.0x in 2010.

Liquidity

In our opinion, MAN's liquidity is strong, underpinned by cash and marketable securities of about €1.1 billion in its industrial unit on Sept. 30, 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. This facility was unused as of June 30, 2009. Also as of Sept. 30, 2009, the group had about €1.2 billion in committed and bilateral credit lines with different banks. These bilateral lines mostly have maturities of one to two years.

In March 2009, MAN had drawn down €1.5 billion on a €2.0 billion syndicated bank facility that was arranged in conjunction with the acquisition of the Volkswagen AG (A-/Negative/A-2) 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 European medium-term note (EMTN) program is €3.5 billion. We understand that bank lines are not subject to financial covenants, rating triggers, or material adverse change clauses. We expect MAN's capacity to serve its outstanding debt to be supported by free operating cash flow generation. On Sept. 30, 2009, short-term maturities in its industrial unit were €0.5 billion and MAN's funding sources considerably exceeded upcoming debt maturities in the medium term.

From Jan. 1, 2010, MAN can exercise its put option for the remaining stake in Ferrostaal. If the put option were to be exercised, MAN would receive proceeds of about €300 million.

CreditWatch

To resolve the CreditWatch Negative placement, we will seek further clarity on the company's future management structure and objectives. The rating could also be negatively influenced by developments in the ongoing investigations on suspicion of alleged bribery and other alleged criminal offenses.

The magnitude of the bribery investigations and its potential impact on the ratings currently remains uncertain to us. We understand that to date, MAN has expensed €50 million for specialists engaged in conjunction with the investigation. However, MAN has not quantified the potential financial risks related to the investigations. Accordingly, we do not have any further information regarding the investigation and are therefore unable to assess its potential impact on the ratings.

Meanwhile, we view as positive, the steps that the company has taken internally to identify and remedy procedural and control weaknesses.

We will continue to monitor the allegations of bribery and the investigations closely. Developments that could impair the company's credit quality and result in negative rating actions include:

- Evidence of systematic bribery practices across the MAN group and/or further broadening of external investigations to include more business units;
- Further unexpected and substantial changes at the management board level that may impair our assessment of strategic execution at the company; and
- Significant fines related to the alleged bribery or other alleged criminal offenses.

We are also in the process of reviewing our assessment of the business risk and financial risk profile of MAN. When completed, this review of the industry characteristics and business risk profile may also negatively affect our ratings on MAN.

At this stage, we currently believe that upon resolution of the CreditWatch, a potential downgrade would likely be limited to two notches.

Related Research

- Principles Of Corporate And Government Ratings, June 26, 2007
- Key Credit Factors: Business And Financial Risks In The Automaker Industry, Sept. 25, 2008
- Business Risk/Financial Risk Matrix Expanded, May 27, 2009

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
MAN SE		
Corporate Credit Rating	A-/Watch Neg/A-2	A-/Stable/A-2
Senior Unsecured (5 issues)	A-/Watch Neg	A-

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