

Research Update:

SSAB Outlook Revised To Positive On Substantial Reduction In Net Debt; 'BB+' Rating Affirmed

July 23, 2021

Rating Action Overview

- We project record-high EBITDA of about Swedish krona (SEK) 16 billion for Swedish steelmaker SSAB AB in 2021. This follows EBITDA of SEK7.8 billion in the first half of the year, on the back of strong steel conditions that are likely to persist for the rest of the year.
- Thanks to its ability to translate profitability into cash flows, and limited pressure to increase dividends and capital expenditure (capex), SSAB is likely to reduce its net debt, thereby supporting a higher rating over time.
- We have therefore revised our outlook on SSAB to positive from stable and affirmed our 'BB+' long-term issuer credit rating on the company.
- The positive outlook reflects a potential upgrade in the coming six-to-12 months as the company accelerates toward a debt-free position on the back of extremely strong steel industry conditions.

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Rating Action Rationale

The steel industry has completed an unprecedented turnaround from trough to peak in 12 months. After posting very weak results in 2020, with EBITDA of only SEK3.4 billion, we now expect SSAB to post EBITDA of around SEK16 billion in 2021. This is thanks to a recovery in demand in all regions and for all products after muted demand in the automotive, construction, and capital goods industries during the COVID-19 pandemic in 2020. Support for demand also comes from the rollout of global stimulus programs, including the rebuilding of infrastructure and the transition to a more sustainable low-carbon economy, and from supportive regulations, such as controls on steel production in China and exports. The extraordinary market conditions are also evident from a hike in steel prices. For example, hot-rolled coil steel sold for €1,060 per ton in the second quarter of 2021 in Europe, compared to €340 per ton a year ago, an increase of close to 150%. During the first half of 2021, steel companies ran their facilities at full capacity, and the order books for the rest of the year look promising. During the first half of 2021, SSAB, like other steel companies, seized on the healthy demand, promoting its value-added products, for example,

quenched and tempered steels and advanced high-strength steels. That said, at some point during 2022, demand and prices will soften toward normal levels, and we expect that 2023 will reflect mid-cycle industry conditions.

SSAB will reduce its net debt substantially in 2021, which could lead to an upgrade to 'BBB-'.

The company's journey to reduce its reported net debt started a few years ago and has seen some delays. However, we expect that SSAB will translate the record-high profitability in 2021 into cash flows from operations of about SEK10 billion. With a relatively modest capex budget and no pressure to increase it, we expect that SSAB's net reported debt will decline to about SEK4 billion by the end of 2021 from SEK10 billion on Dec. 31, 2020, and that it will have limited debt by mid-2022, well below its public gearing target of 35%. In our view, if SSAB maintains minimal reported net debt, it will be able to withstand volatility in the steel industry. For example, with reported net debt of up to SEK4 billion--equivalent to S&P Global Ratings-adjusted debt of about SEK7 billion--and multiyear EBITDA of SEK8 billion-SEK9 billion, the company's adjusted funds from operations (FFO) to debt would be 100%, compared to 60% that we expect for the 'BBB-' rating. It would be above 50% with depressed EBITDA of SEK4.5 billion at the bottom of the cycle, compared with 45% that we see as commensurate with the bottom of the cycle. In our view, once it reaches a debt-free position, SSAB is likely to allocate excess free operating cash flow to its shareholders, rather than increasing its capex substantially or pursuing mergers and acquisitions (M&A). We continue to view the company's liquidity as strong (see "SSAB 'BB+' Rating Affirmed And Removed From CreditWatch On Strong Recovery In The Steel Industry; Outlook Stable," published Feb. 26, 2021).

SSAB continues to convert its basic oxygen furnace (BOF) in Oxelösund, Sweden, to an electric arc furnace, but some challenges persist. We continue to see the conversion of the Oxelösund BOF to an electric arc furnace as the next milestone on the company's environmental, social, and governance journey, allowing it to produce fossil-free steel. SSAB aims to commission the project by 2026. At the moment, the company is yet to secure all the environmental permits and the necessary electricity. However, strong support from the government to complete the project and reduce Sweden's overall CO2 emissions should help the company to meet its target. Lastly, we understand that delays will not have any operational consequences.

Outlook

The positive outlook reflects a potential upgrade in the coming six-to-12 months as SSAB accelerates toward a debt-free position on the back of extremely strong steel industry conditions. We view the company's ability to maintain limited reported net debt and average EBITDA of about SEK8.5 billion as underscoring its ability to maintain its competitive position and achieve adjusted FFO to debt of 60% under less favorable market conditions. Under our base case, we project EBITDA of around SEK16 billion in 2021 and SEK8.5 billion-SEK10.5 billion in 2022, translating into a net-debt-free position by mid-2022. An upgrade also depends on further improvements in SSAB's business model, which will better position the company for the next downturn.

Upside scenario

Some of the triggers for an upgrade to 'BBB-' include:

- No sudden change in the current market conditions that would delay SSAB's ability to achieve limited reported net debt by mid-2022 and undermine its ability to maintain a robust balance

sheet over time.

- Adjusted FFO to debt of 60% or more, together with positive discretionary cash flow (after capex and dividends) under normal industry conditions. In our view, the company would be able to meet this target even at the low point of the cycle if its reported net debt remained limited.
- Better visibility on the company's capital allocation between dividends and capex for 2022.
- Progress with the company's conversion of the BOF in Oxelösund, and later on, with converting its other BOFs, as an important part of ensuring it has the assets to operate sustainably in the long term.

Downside scenario

We may revise the outlook to stable if we see a material change in steel industry conditions, or if SSAB contemplates a sizable debt-funded acquisition that would delay its deleveraging.

Company Description

SSAB produces high-strength steel, quenched and tempered steel, as well as strip, plate, and tube products, and provides construction solutions. It had sales of SEK65 billion and annual production capacity of 8.8 million tons in Sweden, Finland, and the U.S. in 2020. The company serves a number of end markets, such as industrial applications, automotive, heavy transport, construction, and energy. The company operates through five divisions:

- Special Steels (about 55% of EBITDA);
- Europe (15% of EBITDA);
- Americas (10% of EBITDA);
- Tibnor (6% of EBITDA); and
- Ruukki Construction (12% of EBITDA).

SSAB is headquartered in Stockholm, and its shares are traded on NASDAQ Stockholm and Helsinki, with 21.8% of the shares held by long-term strategic investors Industrivarden (11.8%) and Solidium (10%). The remaining shares are free float. Notable rated peers include U.S. Steel Corp., BlueScope Steel Ltd., ArcelorMittal, and Evraz PLC.

Our Base-Case Scenario

We have revised our base case to take account of the extraordinary industry conditions. We expect SSAB to report EBITDA of around SEK16 billion in 2021, up from SEK7.5 billion-SEK8.5 billion in February 2021. In our view, the current level of demand is not sustainable, and a mean reversion of prices and industry activity could take place in the second half of 2022. We continue to see multiyear EBITDA of SEK8.5 billion as a proxy for the company's profitability to test its leverage and cash conversion.

Assumptions

- Capex of SEK3.0 billion-SEK3.5 billion annually, of which SEK1.0 billion-SEK1.5 billion is for the

capacity extension of the quenched and tempered steel line at the steel mill in Mobile, Alabama, and the conversion of the BOF in Oxelösund.

- A substantial negative working capital outflow of up to SEK2.5 billion.
- No dividends in 2021. Over time, we expect that the company will maintain a dividend distribution of 30%-50% of the previous year's net income, in line with its dividend policy, with the potential for special dividends if its reported net debt remains limited.
- No M&A.

Key metrics

	2020A	2021E	2022E	Mid-cycle steel industry conditions
Iron ore price (\$/ton)	103	190	120	--
Eurozone GDP growth (%)	(6.7)	4.4	4.5	--
U.S. GDP growth (%)	(3.5)	6.7	3.7	--
Eurozone steel demand growth (%)	(15.0)	10.0	4.0	--
U.S. steel demand growth (%)	(16.0)	7.0	4.0	--
Adjusted EBITDA (bil. SEK)	3.4	15.5-16.5	8.5-10.5	8.5
Adjusted EBITDA margin (%)	5.2	17.3-18.5	10.0-12.5	--
Adjusted debt to EBITDA (x)	4.1	<1.0	<1.0	<1.0
Adjusted FFO to debt (%)	24	>60	>60	>60
Capex	2.2	3.5	4.0	2.0-2.5
FOCF (bil. SEK)	2.2	6.6-7.5	3.7-5.3	3.0-4.0
Dividends (bil. SEK)	10.0	0.0	4.5-4.9	30%-50% of net income
Adjusted debt (bil. SEK)	14.0	<8.0	<8.0	4.0-8.0
Cash position (bil. SEK)	7.0	14.5-15.2	11.0-12.9	--
Reported net debt (bil. SEK)	7.9	<2.0	<2.0	0.0-4.0*

*Based on the company's financial policy of maximum gearing of 35% over the cycle. A--Actual. E--Estimate. SEK--Swedish krona. FFO--Funds from operations. FOCF--Free operating cash flow.

Ratings Score Snapshot

Issuer Credit Rating: BB+/Positive/--

Business risk: Fair

- Country risk: Very low
- Industry risk: Moderately high
- Competitive position: Fair

Financial risk: Intermediate

- Cash flow/Leverage: Intermediate

Anchor: bb+

Modifiers

- Diversification/Portfolio effect: Neutral/Undiversified
- Capital structure: Neutral
- Financial policy: Neutral
- Liquidity: Strong
- Management and governance: Satisfactory
- Comparable rating analysis: Neutral

Stand-alone credit profile: bb+

Related Criteria

- 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 And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, 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: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
SSAB AB		
Issuer Credit Rating	BB+/Positive/B	BB+/Stable/B

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

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