EULER HERMES

Summary of
Rating Report

SAF-HOLLAND S.A.

4 September 2013

Ein Unternehmen der Allianz

EULER HERMES

Rating rationale

Rating of 4 September 2013

Company Rating:	**BBB**
Outlook:	**Stable**

Subject of rating:

SAF-HOLLAND S.A. develops, produces and markets axle and suspension systems, tractor and trailer couplings, kingpins and landing gear for the truck and trailer industry. Its core markets are Europe and North America. With over 3,000 employees, the company generated sales of € 859.6 million in 2012.

Strengths:

- Large market share in Europe and North America
- Established business relations with OEMs
- Comprehensive network of service stations in core markets

Weaknesses:

- Exposure to the cyclical commercial vehicle industry
- Weak presence in the BRIC nations

Opportunities:

- Growth prospects due to growing road haulage volumes and heightened statutory safety requirements
- Improvement in earnings potential in the *Trailer Systems* segment
- Expansion of *Aftermarket* business

Threats:

- Economic slowdown
- Competitive and price pressure
- Rising commodity prices

Euler Hermes Rating is upgrading the corporate rating for SAF-HOLLAND S.A. from BBB- to BBB. We expect the rating to remain stable over the next twelve months.

The main rationale for the upgraded rating is SAF-HOLLAND's increasingly stable earnings thanks to expanding spare parts and service business, the strong improvement in its capital structure following the capital market transactions and its good financial flexibility. In addition, we assess the company's large share of the market in Europe and North America favourably. With its global production capabilities and extensive service network, SAF-HOLLAND was able to reinforce and broaden its good market position in the *Trailer Systems* and *Powered Vehicle Systems* segments in 2012. In view of the growth in order intake in these segments and the stable macroeconomic conditions in its core markets, we expect a continued increase in market penetration for the main products and sustained impetus for growth for the less cyclical *Aftermarket* business with its broader margins. For this reason, we are upgrading the rating.

We see opportunities in the prospects for growth as well as the increase in global transportation volumes and particularly an improvement in earnings potential in the *Trailer Systems* segment as well as further expansion in spare-parts business. In this connection, SAF-HOLLAND is seeking to stand apart more distinctly from the competition by means of innovations and regional technology transfers in response to mounting price and competitive pressure in the sector, to improve established relations with OEMs and final customers and to reinforce its long-term profitability.

Aside from its exposure to the cyclical commercial vehicle sector, we consider the main threat to the company to lie in the low real net output ratio in the *Trailer Systems* segment. Only insufficient use can be made of the growth potential offered by the BRIC nations at the moment due to the company's minimal presence in these regions.

Threats include heavy cyclical exposure, increases in commodity and energy prices, currency fluctuations, the mounting price and innovation pressure being exerted by OEMs, heightened competition and growing shortfalls in the sourcing of materials.

Financial ratios	**2010**	**2011**	**2012**
EBITDA margin	8.4	8.5	8.3
Return on capital employed (ROCE)	10.8	17.1	17.2
Equity ratio	-7.8	27.9	32.6
Debt to equity ratio	111.8	56.4	49.1
Total liabilities / EBITDA	8.5	4.7	4.3
Net financial liabilities / EBITDA	5.9	2.3	2.0
EBIT interest coverage	1.1	2.7	3.9
EBITDA interest coverage	1.9	3.7	5.6

* adjusted in accordance with EHRG's analysis principles.

© Euler Hermes Rating Deutschland GmbH 2013

Company

SAF-HOLLAND S.A. (SAF-HOLLAND) specialises in developing, producing and marketing high-quality systems and components for tractors (*Powered Vehicle Systems*) and trailers (*Trailer Systems*). In addition, its activities include related service and spare-parts business (*Aftermarket*). In 2012, the company generated consolidated sales of € 859.6 million with an average of 3,118 employees in the *Powered Vehicle Systems* (18.3 % of sales), *Trailer Systems* (55.1% of sales) and *Aftermarket* (26.6 % of sales) segments. SAF-HOLLAND has approximately 9,000 service stations around the world and a total of 16 production facilities including in the United States, Canada, Germany, Australia, China and India. Its most important sell-side markets are Europe, which contributes 50.6% to sales, and North America with 42.6% of sales.

In the ***Trailer Systems* segment**, SAF-HOLLAND holds a leading market position in axle and suspension systems, landing gear and kingpins. It supplies major customers such as Krone and Kögel as well as numerous smaller regional operators and producers of special-purpose vehicles. The *Trailer Systems* segment reported sales of € 473.5 million and adjusted EBIT of € 14.3 million (EBIT margin of 3.0%) in 2012. Local competitors in axle and suspension system business include BPW in Europe, Hendrickson in North America and FUWA in China.

The ***Powered Vehicle Systems* segment** reported sales of € 157.6 million and adjusted EBIT of € 15.6 million (EBIT margin of 9.9%). In contrast to the *Trailer Systems* segment, the *Powered Vehicle Systems* segment is characterised by a greater sell-side concentration and the dominant position of the OEMs over the suppliers. The largest customers in this segment are Paccar, Oshkosh, Daimler, Volvo and Navistar. The main global competitor is Jost, whereas at the local level Fontaine in North America and FUWA in China play a particularly dominant role.

SAF-HOLLAND's ***Aftermarket* segment** is responsible for supplying the transport industry with spare parts. The customer structure is heavily fragmented, ranging from final customers (fleet operators) to spare parts traders and garages. A very dense service network has been established in the core markets of Europe and North America and is substantially broader than those of its competitors. The *Aftermarket* segment reported sales of € 228.5 million and adjusted EBIT of € 33.1 million (EBIT margin of 14.5%) in 2012.

SAF-HOLLAND S.A. was established on 21 December 2005 following the merger of the SAF Group and the HOLLAND Group. Venture capital company Pamplona Capital Partners had bought shares in both companies and initiated the merger. The SAF Group (Sauer Achsenfabrik) has its roots in a plough forge established in Keilberg in 1881. In 1950, SAF embarked on the industrial production of axles for the commercial vehicle industry. The HOLLAND Group's roots go back to a US producer of safety couplings established in 1910. In the wake of mounting industrialisation, it was renamed The HOLLAND Hitch Company and shifted its focus to coupling systems for heavy-duty commercial vehicles. The organisational merger of the two subgroups SAF and HOLLAND was completed in 2007. Further milestones in the company's history include the use of disc brake technology in trailers and the acquisition of a European producer of coupling products (Georg Fischer Verkehrstechnik) and a US producer of lading gear (Austin-Westran) in 2008. SAF-HOLLAND S.A. has been listed on the stock market since 2007 and included in the SDAX since 2010. The stock is mostly free float. The members of the Management Board and the Board of Directors held around 4.4% of the company's stock as of 31 March 2013. The Management Board currently comprises Mr. Detlef Borghardt (CEO), Mr. Wilfried Trepels (CFO) and the heads of the three business units *Powered Vehicle Systems* (Mr. Jack Gisinger), *Trailer Systems* (Mr. Steffen Schewerda) and *Aftermarket* (Mr. Alexander Geis).

Rating history	24.09.2012	04.09.2013			
Notation/outlook	BBB- / stable	BBB / stable			

© Euler Hermes Rating Deutschland GmbH 2013

Earnings potential and profitability

Contrary to the company's consolidated financial statements, our analysis classifies income from the disposal of assets (2010-2012), income from the deconsolidation of SAF-HOLLAND Slovakia (2010) and the reversal of impairments on intangible assets (2010-2012) as extraordinary items. Restructuring expense (2010-2012) and impairments of goodwill and intangible assets (2012) are also included in extraordinary expense.

Structural income statement*	2010		2011		2012		Change year on year (%)	
	T€	%	T€	%	T€	%	2011	2012
Sales	631,053	*100.0*	831,317	*100.0*	859,578	*100.0*	31.7	3.4
Total revenues	631,053	*100.0*	831,317	*100.0*	859,578	*100.0*	31.7	3.4
Cost of materials	407,620	*64.6*	551,497	*66.3*	566,683	*65.9*	35.3	2.8
Gross profit	223,433	*35.4*	279,820	*33.7*	292,895	*34.1*	25.2	4.7
Other operating income	1,136	*0.2*	768	*0.1*	1,161	*0.1*	-32.4	51.2
Personnel costs	121,397	*19.2*	147,597	*17.8*	159,433	*18.5*	21.6	8.0
Other operating expenditure	50,503	*8.0*	61,973	7.5	63,565	*7.4*	22.7	2.6
EBITDA	52,669	*8.3*	71,018	*8.5*	71,058	*8.3*	34.8	0.1
Depreciation/amortisation	22,808	*3.6*	20,676	*2.5*	20,884	*2.4*	-9.3	1.0
EBIT	29,861	4.7	50,342	*6.1*	50,174	*5.8*	68.6	-0.3
Net finance expense	-35,046	*-5.6*	-24,019	*-2.9*	-29,572	*-3.4*	-31.5	23.1
Of which interest expenditure	*28,053*	*4.4*	*19,009*	*2.3*	*12,736*	*1.5*	*-32.2*	*-33.0*
Profit from ordinary business activities	-5,185	*-0.8*	26,323	*3.2*	20,602	*2.4*	-607.7	-21.7
Net exceptional income/expense	1,043	*0.2*	322	*0.0*	-4,627	*-0.5*	-69.1	-1,537.0
Earnings before taxes (EBT)	-4,142	*-0.7*	26,645	*3.2*	15,975	*1.9*	-743.3	-40.0
Consolidated net profit for the year	-8,310	*-1.3*	26,619	*3.2*	7,418	*0.9*	-420.3	-72.1

* The income statement was derived from the reported cost-of-sales method.

In the wake of the financial and economic crisis, consolidated sales tumbled by 47.5% in 2009 due to a combination of a sharp decline in demand and high inventories in the commercial vehicle industry. Of this decline, the *Trailer Systems* segment accounted for over 90%. In response to the negative experience gained with high inventories, requirements-oriented production was increasingly implemented in the following years. In 2010 and 2011, SAF-HOLLAND benefited from the economic recovery as well as the substantial effects of pent-up demand being released in the transport industry. This was reflected in correspondingly dynamic sales, which grew by 50.4% and 31.7%, respectively, at the group level in these two years. A more muted economic outlook and weaker effects from the release of pent-up demand exerted pressure on the top line last year. Even so,the company's **consolidated sales** climbed by € 28.3 million to € 859.6 million, chiefly underpinned by the *Aftermarket* segment, which plays a crucial role for the group's earnings potential, with sales widening by € 24.0 million to € 228.5 million. This reflected the growing market penetration of the group products, additions to the dealer network and the availability of new logistics centres. In addition, the *Powered Vehicle Systems* segment reported an increase of € 3.6 million in sales to € 157.6 million, benefiting from rising capital spending and its strong competitive position in the North American market for coupling products. Despite the challenging market conditions in Europe, sales in the group's largest segment *Trailer Systems* rose by € 0.7 million to € 473.5 million. Consolidated sales by segment were as follows in 2012: *Trailer Systems* 55.1 % (2010: 51.1 %; 2011: 56.9 %), *Powered Vehicle Systems* 18.3 % (2010: 20.2 %; 2011: 18.5 %) and *Aftermarket* 26.6 % (2010: 28.6 %, 2011: 24.6 %).

Regionally, the increase in sales was chiefly underpinned by growth in *North America* and *other countries* in 2012. Sales in *North America* climbed by 10.6% to € 367.1 million, accounting for a slightly larger share of 42.7% (previous year 39.9%) of total sales. *Other countries*, which include the BRIC nations, achieved a 34.6% increase in sales to € 57.6 million. The share in total sales widened to 6.7% (previous year 5.2%). By contrast, the difficult

conditions in the European market exerted pressure on the *Europe* region, causing segment sales to shrink by 4.8% to € 434.9 million. Accounting for 50.6% (previous year 54.9%) of total sales, *Europe* is SAF-HOLLAND's largest market.

With respect to the **customer structure**, the largest customer accounted for around 6.5% of total sales last year, with the top ten customers contributing around 38.3% However, this sales dependence must be seen in the light of what in some cases is the final customer's extensive right to influence the selection of components for a trailer.

The decline of a total of 520 basis points in the **gross margin** from 2009 to 2011 was due to rising commodity prices (e.g. steel) on the one hand and a shift in sales in favour of the *Trailer* segment on the other. With its low real net output ratio, the *Trailer Systems* segment generates relatively small gross margins, meaning that the dynamic growth of this segment in 2010 (+87.0%) and 2011 (+47.0%) has increasingly exerted pressure on the gross profit at the group level. By the same token, the disproportionately strong growth in the *Trailer Systems* segment indicates growing market penetration of the group's products, resulting in heightened future demand for spare parts (*Aftermarket* segment) For this reason, the dilution of the gross margin has predominantly precipitated the strategic corporate decision to substantially step up spare-parts business with its considerably wider margins. The absence of top-line growth in the *Trailer Systems* segment and the disproportionately strong growth in the *Aftermarket* segment were the main reasons for the improved gross margin in 2012.

With respect to the supplier structure in 2012, almost one third of the total cost of materials can be attributed to the main suppliers in Europe and North America. For this reason, we see a certain degree of dependency on key suppliers particularly for brake and bearing systems. An increase in sourcing prices can be passed onto customers with a delay of around six months.

Personnel expenses were reduced substantially in response to the financial crisis via layoffs, reduced working hours and management salary waivers. In the wake of the dynamic economic recovery in the ensuing years, personnel expenses rose to € 159.4 million up until 2012. The business-induced increase in **other operating expenses** was disproportionately small compared with sales, causing the corresponding ratio to contract to 7.4%.

EBIT adjusted for analytic purposes was largely stable in 2012, coming to € 50.2 million. In this connection, it should be noted that the previous year's figure of € 50.3 million included earnings contributions from a major contract which had been completed as planned. Allowing for this special effect, adjusted EBIT would have been € 7.3 million lower in 2011. With adjusted EBIT of € 33.1 million (previous year € 32.1 million), the ***Aftermarket*** **segment** was by far the most **important** and **most stable earnings mainstay** in the Group. The adjusted EBIT margin in this segment came to 14.5% (previous year 15.7%). The *Power Vehicle Systems* segment had to fill the gap left by a major contract but was still able to increase earnings to € 15.6 million (previous year € 14.2 million). The adjusted EBIT margin widened to 9.9% (previous year 9.2%). In the *Trailer Systems* segment, adjusted EBIT dropped slightly to € 14.3 million (previous year € 14.8 million). The adjusted EBIT margin contracted to 3.0% (previous year 3.1%). Various measures (see section on strategy and planning) are being planned to improve earnings potential in the *Trailer Systems* segment.

Interest expense on interest-bearing loans and other borrowings was lowered in the previous year due to a reduction in financial liabilities and a contraction in the interest margins. At the same time, **net finance expense** came under pressure from non-recurring effects in connection with the funding (€ 9.3 million) and settlement of interest-rate hedges (€ 3.0 million). All told, net finance expense rose by € 5.6 million to € 29.6 million. Restructuring and impairment expense simultaneously resulted in an extraordinary loss of € 4.6 million. Against this backdrop, **earnings before tax** declined by € 10.7 million to € 16.0 million.

Earnings potential (%)	2010	2011	2012
EBITDA margin	8.4	8.5	8.3
Total return on capital	5.5	9.9	7.3
ROCE	10.8	17.1	17.2
Cash flow ROI	12.6	15.5	15.6

© Euler Hermes Rating Deutschland GmbH 2013

During the analysed period, the income and profitability ratios improved to a satisfactory level chiefly as a result of the strong market recovery. The decline in the total return on capital to a mutedly satisfactory level in 2012 was chiefly due to the funding-induced, non-recurring deterioration in net finance expense. The return on capital employed increased in the analysed period as a result of improvements in earnings potential (2011) and net debt (2011-2012), achieving a good level last year despite the increase in the equity base (2011-2012).

In the first half of 2013, consolidated sales dropped by € 4.8 million (-1.1%) over the previous year to € 435.6 million in line with expectations. In this respect, the *Trailer Systems* segment grew, performing better than expected and posting a small increase in sales to € 249.2 million (previous year € 242.8 million). The budged declines in sales in the *Powered Vehicle Systems* (down € 6.2 million to € 75.4 million) and *Aftermarket* (down € 4.9 million to € 110.9 million) segments were chiefly due to the high base-line effects in the previous year, which will continue to recede as the year progresses. In the *Aftermarket* segment, temporary personnel shortfalls in China as well as reduced stockpiling by customers exerted pressure. Despite the slight declines in sales, consolidated operating earnings rose to € 29.8 million (previous year € 29.7 million). The adjusted EBIT margin in this segment came to 6.8% (previous year 6.7%) With adjusted EBIT of € 18.8 million (previous year € 16.7 million), the *Aftermarket* segment remains the most important source of earnings. The *Power Vehicle Systems* and *Trailer Systems* segments contributed operating earnings of € 7.2 million (previous year € 7.2 million) and € 6.8 million (previous year € 7.9 million), respectively. The adjusted EBIT margin widened to 9.6% (previous year 8.7%) in the *Power Vehicle Systems* segment but narrowed to 2.7% (previous year 3.3%) in the *Trailer Systems* segment. The smaller adjusted EBIT margin in the *Trailer Systems* segment was predominantly caused by higher warranty costs reflecting the above-average production figures in 2006/2007. As well as this, higher research and marketing expense exerted pressure. In view of the planned price hikes on the part of one key-account customer, we expect the adjusted EBIT margin to stabilise in the *Trailer Systems* segment in the second half of 2013.

SAF-HOLLAND S.A.'s earning potential and profitability remained stable in 2012. The most important underpinnings for this are the growing earnings contributions by the *Aftermarket* and *Powered Vehicle Systems* segments, which are more than making up for the weaker earnings potential in the *Trailer Systems* segment. In addition to the favourable market conditions for the company in Northern America, the stable earnings potential is also the result of more flexible production and the growing importance of spare parts business. This business segment is characterised by weaker cyclicity and particularly also by wider operating margins, resulting in generally more stable profitability.

Capital structure and debt

Contrary to the consolidated financial statements, we have netted deferred income tax assets with deferred income tax liabilities (2010-2012) and deducted the surplus assets from equity (2011-2012) for the purposes of our analysis. In addition, we have reduced the value of the intangible assets by 25.0% for reasons of caution and lowered reported equity accordingly (2009-2011).

Structural balance sheet	31.12.2010		31.12.2011		31.12.2012		Change year on year (%)	
	T€	%	T€	%	T€	%	2011	2012
Assets	417,406	*100.0*	458,360	*100.0*	454,709	*100.0*	9.8	-0.8
Non-current assets	251,350	*60.2*	249,661	*54.5*	248,073	*54.6*	-0.7	-0.6
of which intangible assets	*140,859*	*33.7*	*139,821*	*30.5*	*139,091*	*30.6*	*-0.7*	*-0.5*
Current assets	166,056	*39.8*	208,699	*45.5*	206,636	*45.4*	25.7	-1.0
of which inventories	*68,082*	16.3	*90,400*	*19.7*	*88,163*	*19.4*	*32.8*	*-2.5*
of which trade receivables	*80,336*	*19.2*	*95,352*	*20.8*	*87,319*	*19.2*	*18.7*	*-8.4*
of which cash and cash equivalents	*8,546*	*2.0*	*15,345*	*3.3*	*18,579*	*4.1*	*79.6*	*21.1*
Equity and liabilities	417,406	*100.0*	458,360	*100.0*	454,709	*100.0*	9.8	-0.8
Equity	-32,543	*-7.8*	128,033	*27.9*	148,120	*32.6*	-493.4	15.7
Non-current liabilities	355,360	*85.1*	208,178	*45.4*	197,965	*43.5*	-41.4	-4.9
Current liabilities	94,589	*22.7*	122,149	*26.6*	108,624	*23.9*	29.1	-11.1
Financial liabilities	*316,604*	*75.9*	*180,907*	*39.5*	*161,407*	*35.5*	*-42.9*	*-10.8*

During the period covered by the analysis, adjusted total assets rose to € 454.7 million chiefly as a result of increased business activities. In terms of the structure of the company's assets, the proportion of **current assets** widened for business-related reasons. The sharp rises in sales in 2010 and 2011 show up in the balance sheet in the form of higher inventories and receivables. In the previous year, stable business performance and factoring operations of € 7.8 million resulted in a decline in receivables. This caused net working capital to drop by around € 10.0 million. Cash and cash equivalents rose particularly as a result of the growth in earnings and the proceeds from the capital market transactions. In absolute terms, **non-current assets** remained stable in the analysed period. **Intangible assets** are of material importance in this connection, accounting for 40.8% after the analysis-related adjustment of 25%. The intangible assets chiefly comprise goodwill and customer lists acquired in connection with the "SAF" and "HOLLAND" subgroups in 2006. We assume that this item has a recoverable value after the adjustment made and in the light of the sustained favourable underlying conditions and the medium-term outlook for growth.

Adjusted **economic capital** widened to € 148.1 million in 2012, chiefly underpinned by the capital market transactions in March 2011 (gross issue proceeds: € 139.4 million) and November 2012 (gross issue proceeds: € 21.6 million) and the net earnings recorded for the year. This resulted in an increase of € 159.4 million in the **share premium** to € 265.8 million. Charges of € 20.4 million were recognised within equity last year (previous year € 15.3 million) due to the early adoption of IAS 19R ("Employee benefits") and the resultant abolition of the corridor method. The **equity ratio** adjusted for the purposes of our analysis widened last year by 470 basis points to 32.6% (previous year 27.9%), particularly reflecting the repayment of bank loans and the settlement of interest-rate hedges using the proceeds from the capital market transactions, among other things. This resulted in a (net) € 19.5 million decline in **financial liabilities** in 2012. This was the main reason for the reported drop in non-current liabilities.

In connection with **restructuring of funding** in October 2012, an agreement was reached with the syndicate banks to adjust the existing loan arrangements, resulting in improved terms and more favourable interest margins in the current year. A key element of these restructuring efforts was the issue of a five-year bond of € 75.0 million.

© Euler Hermes Rating Deutschland GmbH 2013

The current loan agreements expire in October 2017 and provide for credit facilities totalling € 207.1 million (see section on internal financial potential and financial flexibility). The non-current liabilities also include pension provisions of € 39.2 million. In this connection, there are off-balance-sheet gaps of € 39.2 million due to interest and yield shortfalls as of 31 December 2012 (previous year € 33.5 million). With respect to current liabilities, trade payables declined by € 15.4 million to € 70.6 million for closing-day-related reasons.

Depending on the size of the adjustment to the intangible assets (0%, -25.0%, -50.0%), the equity ratio ranges from 24.9% to 38.8% and gearing from 42.3% to 58.4%. The scenario analysis underscores the solidity of the capital structure. Even in an extreme scenario providing for a 50.0% impairment, the equity ratio and gearing still achieve satisfactory levels.

As of 30 June 2013, SAF-HOLLAND S.A.'s non-adjusted total assets stood at € 556.3 million, equivalent to an increase of € 19.5 million over the annual financial statements for 2012. Inventories (€ +6.2 million) and trade receivables (€ +12.7 million) rose in particular for business-related reasons. Net working capital remained unchanged due to the increase of € 20.4 million in trade payables. At € 18.4 million, cash and cash equivalents were stable. Non-adjusted equity came to € 209.4 million, up on the year-end figure of € 197.9 million. The reported equity ratio stood at 37.6%, thus exceeding the 31 December 2012 figure (36.9%). Reported current and non-current financial liabilities fell by a further € 11.1 million to € 150.3 million.

Thanks to the capital market transactions and the net profits achieved over the last few years, SAF-HOLLAND S.A. exhibits a highly satisfactory capital structure as of the end of the analysed period. This capital structure still has satisfactory levels even in a scenario in which heavy adjustments are made to intangible assets. Deleveraging potential and interest coverage ratios were generally good or highly satisfactory. In this connection, it should be noted that the interest coverage ratios came under pressure last year as a result of unfavourable funding conditions.

© Euler Hermes Rating Deutschland GmbH 2013

Internal financial potential and financial flexibility

Cash flow (T€)	2010	2011	2012
Cash flow from operating activities	39,438	41,098	53,993
Cash flow from investing activities	-7,177	-12,109	-21,333
Free cash flow (total)	32,261	28,989	32,660
Cash flow from financing activities	-45,312	-22,344	-29,253

Cash flow from operating activities widened incrementally over the analysed period. Decisive factors in this respect were the improved earnings potential in 2011 and reduced working capital in 2012. Material non-recurring factors included pull-forward effects of € 6.0 million in 2011 and factoring operations of € 7.8 million in 2012. Cash flow from investing activities increased in 2010 through 2012 due to heightened replacement and extension spending. Last year, the increased capital spending particularly related to spending of € 6.0 million on the integration of local SAP systems. Cash flow from financing activities benefited from two equity issues in 2011-2012 of € 143.7 million (2011) and € 21.7 million (2012) as well as the placement of a bond with a value of € 75.0 million (2012). The proceeds from these capital market transactions were chiefly used to settle financial liabilities. In addition to non-recurring transaction costs in connection with the funding activities as well as payments for the settlement of interest-rate hedges, the settlement of financial liabilities resulted in a net cash outflow from financing activities.

SAF-HOLLAND S.A. has syndicated loans and facilities of € 207.1 million available to it; of these, a sum of € 75.7 million had been utilised as of 30 June 2013. In this connection, it should be noted that semi-annual repayments of € 3.9 million each are due in March and September. These loan agreements expire on 5 October 2017. As of the end of June, unused facilities of € 131.4 million were available. Including cash and cash equivalents, total liquidity stood at around € 149.7 million as of 30 June 2013. In addition, the company is able to utilise a factoring facility of € 25.0 million. Given the existing facilities and liquidity, SAF-HOLLAND currently exhibits very good financial flexibility.

Last year, SAF-HOLLAND S.A. was able to additionally improve its internal financing potential thanks to stable earnings potential and reduced net working capital. The facilities available to the company and the cash held in addition to the strategic liquidity reserve ensure very good financial flexibility. In addition, improved terms and conditions have been secured for the medium term following the renewal of the funding agreements with the syndicate banks.

© Euler Hermes Rating Deutschland GmbH 2013

Market conditions

The business performance of suppliers of components and parts for heavy-duty tractors and trailers is primarily dependent on the production and call-down volumes of OEMs, fleet operators, garage and spare parts dealers. This, in turn, generally hinges on underlying economic conditions in the target markets, particularly demand for road haulage and infrastructure development. Specifically, demand is also influenced by the financing possibilities available (leasing) and the individual preferences of the final customers (e.g. fleet managers). Moreover, exhaust and safety standards, fuel consumption, the life cycle of tractors and trailers and the resultant potential for the secondary market and spare parts business also play a role. The market is characterised by oligopolistic competition. A small number of players mostly specialising in a core product address niches with highly regional product characteristics tailored to the needs of individual OEMs/final customers.

Driven by the strong effects of unleashed pent-up demand following the financial and economic crisis, sharp growth was achieved in global cargo transportation volumes and production output in the global commercial vehicle industry in 2010 and 2011. The relevant segments - heavy heavy-duty tractors and trailers - benefited in equal measure from these trends. This resulted in disparate trends in SAF-HOLLAND's main sell-side regions over time. Whereas production output of medium/heavy commercial vehicles contracted slightly again in 2012 (2010: +42.9%; 2011: +22.2%; 2012; -4.6%), it climbed for the third consecutive year in North America (2010: +14.5%; 2011: +29.4%; 2012: +10.0%).

Following the global recovery, the IMF now expects global economic growth for 2013 to remain at 2012 levels in its latest outlook (July 2013). Further contraction is expected for the Eurozone (2012: -0.6%; 2013: -0.6%; 2014: +0.9%). The economy of the European Union shrank shank in the first quarter of 2013 (EU27: BIP -0.7%, Eurostat). The economic uncertainty moving forward as a result of the European sovereign debt and confidence crisis is currently placing a damper on capital spending. The IMF expects positive economic growth in the United States (2012: +2.2%; 2013: +1.7%; 2014: +2.7%). That said, growth may come under pressure from the current cuts in and the necessary future consolidation of the public sector budget.

We expect production figures in the European commercial vehicle industry to remain flat or increase slightly in 2013. On the other hand, the Northern American markets should continue to grow in 2013 at robust rates, which however will weaken due to the receding effects of unleashed pent-up demand against the backdrop of generally more favourable macroeconomic expectations.

Production of middle/heavy commercial vehicles (in thousands of units)	Act. 2012	2013e	2014e	2015e	2016e	2017e	2018e	CAGR (%) 2012-2018
Europe	619	633	765	820	808	876	936	7.1
North America	496	521	566	614	588	571	620	3.8
South America	197	242	259	271	274	270	277	5.8
Asia	1,977	2,128	2,196	2,325	2,324	2,438	2,512	4.1
Rest of the world	3	3	3	4	4	4	4	4.9
Total	3,293	3,526	3,790	4,033	3,998	4,159	4,348	4.7

Source: IHS Automotive, February 2013

In the medium to long term, we expect sales volumes to rise in all regions. The increase in road haulage volumes, exports of commercial vehicles to growth regions, the effects of unleashed pent-up demand and heightened replacement spending in response to the introduction of more stringent emission rules (e.g. EPA 10 in the United States, Euro 6 in the EU) should generate a CAGR of +7.1% and +3.8% in the European and Northern American markets, respectively, moving forward to 2018. Production volumes in the countries of South America and Asia should also increase as a result of the relocation of commercial vehicle production, extensions to infrastructure and a sharp rise in transport volumes (consumer goods and commodities).
The future global business environment for suppliers of components for tractors and trailers is particularly dependent on a global increase in (road) haulage volumes. In this connection, the availability of funding and fleet operators' expectations of high-quality product characteristics play a key role. Both groups pay particular attention to stable values and optimised total cost of ownership, with these aspects also influencing the appeal of the sec-

ondary market for used tractors and trailers. In this connection, we particularly see opportunities for suppliers holding a large share of the market and with an established market presence. Established distribution channels to OEMs are important in this respect as a means of distributing components to as broad a base of final vehicles as possible, followed in a second step by a dense distribution and service network in order to participate in after-sales spare parts business. In our view, ongoing product innovation and sector standards make a key contribution to reinforcing market presence. We consider innovative sector trends to encompass weight reduction (materials, design), reduced maintenance requirements, robust handling, modular structures (e.g. axles and braking systems), standardisation (e.g. wheel connections), automatic systems (e.g. for trailer couplings, landing gearing) and heightened safety. Moreover, suppliers of high-quality components have an opportunity of developing product characteristics giving them a competitive edge due, among other things, to the growing structural complexity of the products and rising demands of just-in-time delivery and quality. Geographically diversified suppliers (following OEMs) with a product range tailored to different target markets (e.g. the growing logistics markets in India and China) have an advantage in our view.

Market risks particularly arise from the economic uncertainties in the core European and Northern American markets. The possibility of recessionary trends spreading from crisis-afflicted countries to hitherto largely unscathed regions cannot be ruled out. In addition, there are considerable investment risks for quality and innovation leaders due to the high ratio of fixed to total assets and recurring spending on research, development and capacity extensions. The main materials used, namely steel and aluminium, are also subject to cyclical price fluctuation. Where there are special requirements with respect to raw materials (e.g. special steels), a dependency on specialised suppliers and delivery shortfalls may arise. In addition, we generally expect a steady increase in pressure on prices in the components industry as a result of partnerships and mounting concentration as well as changes in price structures and sell-side market behaviour.

Following high rates of growth in 2010 and 2011, global demand for tractors and trailers weakened in 2012. With the exception of North America, the markets addressed by SAF-HOLLAND were unable to buck this trend. Given the current increase in order intake by leading commercial vehicle OEMs, we expect slight growth for 2013. With the global increase in transport volumes, we generally also see positive market potential in the medium to long term. We see short-term opportunities for growth particularly with innovative and high-margin operators by means of market displacement and market share growth. A coherent brand concept, spare parts business and efforts to address key trend such as light-weight construction, environmental concerns and safety are critical determinants of success in our view. In addition to economic uncertainty, the risks to which the sector as a whole is exposed entail heightened competition and fluctuations in commodity prices.

© Euler Hermes Rating Deutschland GmbH 2013

EULER HERMES

Strategy and planning

Strategic orientation

Business segment	Markets/customers
Trailer Systems and Powered Vehicle Systems ▪ Profitable growth thanks to expected market growth ▪ Development of new axle and suspension systems for core markets, particularly Europe ▪ Improvement in earnings potential in the *Trailer Systems* segment, particularly as a result of cost-cutting efforts and technology transfer. ▪ Greater differentiation via innovative new materials, electronics and niche products ***Aftermarket*** ▪ Further additions to distribution and service network ▪ Further expansion of spare parts business ▪ Further enlargement of range of spare parts through the introduction of secondary brands (“Sauer Quality Parts”)	▪ Reinforcement and expansion of market share in core markets in Europe and North America ▪ Expansion of market position in the BRIC nations
Organisation	**Financials**
▪ Ongoing optimisation of the production and logistics processes ▪ Intensification of research and development activities ▪ Ongoing optimisation of the production and logistics processes ▪ Selective examination of acquisition candidates	▪ Increase in sales of an average 6.7% p.a. in 2012 through 2015 to € 1,043 million. ▪ Improvement in adjusted EBIT margin to 8.4% in 2015 ▪ Increase in adjusted equity ratio to 48.5% in 2015 and reduction in financial liabilities and interest expense

SAF-HOLLAND is positioning itself as a leading supplier of high-quality system solutions and components for the commercial vehicle industry. With this strategic alignment, it is seeking technology and quality leadership in its core European and North American markets. In particular, it wants to hold and broaden its leading market position as a provider of high-quality products and services in the ***Trailer Systems***, ***Powered Vehicle Systems*** and ***Aftermarket*** segments. For this purpose, SAF-HOLLAND coordinates a global network of subsidiaries and alliance partners to address the strategically important spare-parts and service business on a comprehensive basis and to expand it selectively. In addition, it is seeking to build up a leading market position in new product segments, particularly those which offer synergistic effects within the range as a whole or make use of opportunities arising from market consolidation or heightened regulatory requirements.

SAF-HOLLAND S.A.’s core skills in the ***Trailer Systems* segment** include the development of innovative axle and suspension systems as well as welding, painting and assembling. The modular structure of the axle and suspension systems allows the company to flexibly address different customer requirements and to offer special products for niche markets. Given the already very large share of the European market for axle and suspension systems which it holds (2012: 36-40%), SAF-HOLLAND is to particularly make use of the opportunities for growth in **North America** and the BRIC nations, in which it currently holds only a small share of the market and has only limited production capacities. The company’s share of the North American market is to be widened to 30.0% (2012: 15.0%) in the medium term through the establishment of its own axle production activities and the utilisation of experience gained in Europe with the integration of axle production with disk brake technology (technology

transfer).

In this connection, SAF-HOLLAND particularly wants to benefit from a structural change in the US trailer market, which will be triggered by the more stringent requirements with respect to braking performance as of 2013. This rule stipulates a roughly 30.0% cut in the maximum braking distance. This requirement will spur demand for disk brakes as these offer superior braking performance and generate less heat compared with drum brakes. On the other hand, additional demand for both braking systems (drum and disk brakes) is expected as the more stringent rules are likely to result in shorter maintenance intervals. Against this background, SAF-HOLLAND has already widened its North American production capacity from 40,000 to 80,000 axles a year. SAF-HOLLAND is well positioned to benefit from the expected structural change in North America thanks to European skills in disk brake technology and the sustained extensions to production capacity in North America.

In addition to structural growth opportunities in North America, the *Trailer Systems* segment is to expand in **Europe** chiefly for market-related reasons. This assumption is being confirmed by commercial vehicle OEMs' current order intake figures. As of 2015, crucial impetus for growth will be generated by the newly developed European axle and suspension system. In addition to other measures, the planned market launch of this system is to boost the low earnings potential (EBIT) in the *Trailer Systems* segment by up to 300 basis points. The planned cost cuts are to be primarily achieved by consolidating facilities in Germany and North America and by increasing efficiency in the production process, e.g. in the ball bearing system segment. Via leaner production processes, SAF-HOLLAND additionally wants to boost productivity.

In the suspension systems market, SAF-HOLLAND has a large share of the European market but only a small share of the North American market. However, the planned launch of new suspension systems on the North American market should improve the opportunities for regional growth. Given the large share held in the core markets for kingpins and landing gear, scope for additional regional growth is primarily to be found in the BRIC nations.

Future developments in the *Trailer Systems* segment in the core European and North American markets will continue to focus on weight reduction, heightened modularisation and the growing integration of electrical and electronic components. In addition, local development and production capacities are to be expanded, special products for niche commercial vehicle markets developed and strategic partnerships forged with international trailer OEMs.

In the ***Powered Vehicle Systems*** **segment**, SAF-HOLLAND S.A.'s core skills are defined as entailing innovative trailer coupling and suspension systems as well as welding, painting and assembling. The market for suspension systems for tractors is dominated mainly by the large component suppliers and OEMs. SAF-HOLLAND should be able to generate additional growth impetus in the Northern American market with the launch of a newly developed suspension system. The company holds a large share of the North American market for trailer coupling systems (approx. 51.0%) as this is the former HOLLAND's domestic market. It should be possible to tap further potential for growth in Europe in particular by means of a regional technology transfer and selective additions to business. Against this backdrop, the EBIT margin should remain stable.

SAF-HOLLAND S.A.'s ***Aftermarket*** **segment** boasts the world's largest service network, thus ensuring a high degree of customer proximity as a core skill. With the large network of fleet operators, garages and spare parts dealers, SAF-HOLLAND is able to arrange repairs for its customers at short notice and deliver the necessary spare parts. It has more than 9,000 service partners around the world, which gives it a lead over its competitors. With the steadily growing market penetration of SAF-HOLLAND products, demand for spare parts is expected to widen in the future. At the same time, the service network is to be extended in all key regions, resulting in a positive effect for the network. The successful start-up of a new spare parts distribution centre for the South American market highlights the systematic implementation of this expansion strategy. In the medium term, at least one further distribution centre is to be established for the Asian market. As well as this, the regional marketing activities are to be boosted and the range of training and skills development offerings broadened. The range of spare parts is to be enlarged with the introduction of "A2" secondary brands ("Sauer Quality Parts"). These parts will be particularly targeted at markets with a high proportion of tractors and trailers of an advanced age. In this way, SAF-HOLLAND wants to offer its customers spare parts which are more appropriate for the life cycle of the products. Secondary-market products are covered by the statutory guarantee rather than the substantially longer six-year guarantee offered on the company's premium products. With this secondary-brand strategy, SAF-HOLLAND is particularly seeking to address the markets of the Middle East to benefit from the later life cycle phase of the

© Euler Hermes Rating Deutschland GmbH 2013

products in use there and to avert potential substitution risks. Expansion of the relatively stable aftermarket business with its wide margins is the most important factor in the company's efforts to boost the gross and operating margin at the group level and to lessen exposure to cyclical fluctuation.

In addition to widening its share in the core markets of Europe and North America, SAF-HOLLAND also wants to strengthen its position in the BRIC nations. To this end, it wants to revise its original plans of tailoring its range more closely to the less stringent quality and safety requirements of these markets. Accordingly, SAF-HOLLAND wants to increasingly offer higher-quality products in selected markets in the BRIC nations and thus leverage its core skills. In this connection, for example, a suspension system designed for the US market is to be adapted for China. However, given the intense competition and low quality requirements in the BRIC nations, we remain sceptical as to whether the expansion plans in these countries will be successful in the medium term.

In our view, SAF-HOLLAND S.A. has a systematic strategy differentiated by product segment and region which takes due allowance of the opportunities and risks arising in the market environment, its own market position and the available resources and skills. An improvement in earnings potential in the *Trailer Systems* segment is to be assigned particularly high priority in the short term. As we see it, opportunities are arising from the growing importance of spare parts business, mounting sell-side potential in all regional markets and the ability for the company to set itself apart from the competition via innovation and a broader range of products. The risks to SAF-HOLLAND's business performance comprise the aforementioned market uncertainty as well as mounting competitive pressure, possible quality problems leading to impaired customer confidence, product liability risks and development and pricing risks.

© Euler Hermes Rating Deutschland GmbH 2013

Execution of the rating

The rating request was submitted by SAF-HOLLAND S.A. (client) on 13 May 2013. The company was visited on 14 August 2013. This rating report was presented to the client on 20 September 2013, meaning that the rating process has now been concluded. The notation proposal and the report on which it was based were reviewed by the Rating Committee on 4 September 2013 and approved in their current form. If this rating is not made public, the rating assessment refers to this date. If the rating assessment is published on the rating agency's website (www.eulerhermes-rating.com), it will be followed by a subsequent one-year monitoring process. During this period, the company and the environment in which it operates remain under observation. The rated company is subject to unrestricted disclosure obligations during this period. Any change in the rating agency's assessment will result in a change in the published rating, meaning that the rating as shown on the internet represents the current rating assessment at all times. Continued publication after the expiry of the monitoring period is contingent upon a follow-up rating being conducted.

The client is solely and exclusively liable for any errors or omissions in the documents and information supplied openly and willingly in response to our requests for information. The client has reviewed the rating report and confirms that all of the information which it contains is correct and complete in all significant respects, that no major aspects have been concealed and that any forward-looking statements which it may include are based on plausible, verifiable and current data and have been prepared by the client with the diligence of a prudent businessman. However, the client cannot be held liable if actual results differ from the forward-looking statements, in particular the projections, presented in this document. Changes in the economic environment and unforeseen events may impair the validity of the forward-looking statements and projections.

The rating report may not be construed as constituting a recommendation to participate in certain facilities. All recipients of the information should conduct their own independent analyses, credit assessments and other reviews and evaluations which are customary and necessary to reach a final decision about the participation in certain facilities. It should be noted that the summaries of contracts, legislation and other documents included in the report are no replacement for examination of the corresponding full texts. As of the date on which this information is published, it is not possible to guarantee that the information has not changed since being collected and that all information provided is still valid. The client is under no obligation to update the information.

The publication of this rating report may be prohibited by law in certain jurisdictions. The client therefore requests that any persons who gain possession of this information enquire about and comply with any such restrictions. The client does not assume any liability of any kind towards anyone with respect to the dissemination of this rating report in any jurisdiction whatsoever.

The client's management has submitted to Euler Hermes Rating Deutschland GmbH a written letter of representation.

We have prepared this report to the best of our abilities and knowledge.

Euler Hermes Rating Deutschland GmbH

Hamburg, 20 September 2013

© Euler Hermes Rating Deutschland GmbH 2013

EULER HERMES

Analysts

Torsten Schellscheidt, Senior Analyst and Project Manager
Kai Gerdes, Director
Matthias Peetz, Rating Analyst

Rating Committee

Gundel Bergknecht, Senior Analyst
Jörg Walbaum, Senior Analyst

Principal sources of information

- Consolidated financial statements for 2010, 2011, 2012
- Extracts from internal reports
  (e.g. business performance in 2012, analysis of bank liabilities etc.)
- Market analyses
- Strategy paper and corporate planning
- Documents on corporate structure
- Conversations with management

Rating method

Issuer rating, company rating manual of Euler Hermes Rating GmbH, March 2012 version

© Euler Hermes Rating Deutschland GmbH 2013

Rating Notation

category	explanation
AAA	AAA rated companies demonstrate an excellent credit quality. Such companies are characterized by an extremely positive future outlook and are viewed as being “first class” business partners. Although the various security elements can certainly change, such changes – to the extent this can be assessed - are highly unlikely to adversely affect the fundamentally strong position of such companies.
AA	AA rated companies demonstrate very high quality with respect to future security. Along with the AAA rated companies, this group forms the socalled “quality class.” Security margins may, however, be comparatively thinner, the solidity of the security elements may fluctuate more or individual assessment components may indicate a greater long-term risk than is the case for AAA rated companies.
A	A rated companies demonstrate high quality with respect to future security. They show many favourable features which secure their future. Nevertheless, there may be isolated factors which reveal a slightly in-creased susceptibility to the worsening of circum-stances and general economic conditions in the future.
BBB	BBB rated companies demonstrate reasonable quality with respect to future security. Compared to A rated companies, however, it is more likely that worsening of general economic conditions could weaken the capability of fulfilling financial obligations.
BB	BB rated companies still have structures adequate to secure their future. Yet they are subject to greater insecurities. Negative business developments or changes in the general financial and economic conditions can make it impossible for them to fulfil their financial obligations in a suitable manner.
B	B rated companies lack the usual structures to secure their future. Negative business developments or changes in the general financial and economic conditions will most likely make it impossible for them to fulfil their financial obligations in a suitable manner.
CCC	CCC rated companies have structures which greatly endanger the security of their future. Capital service is in jeopardy. Such a company is dependent on a favourable development of general economic conditions if it is to be able to meet its financial obligations in the long term.
CC	Companies receiving a CC rating have very little security for their future. Capital service is in great jeopardy.
C	C rated companies have the least future security of all. The basic conditions enabling such debtors to fulfil their financial obligations are extremely poor. Default is imminent.
D	Companies with a D rating are already in default of payment or have filed for bankruptcy. The D rating is irrelevant for the future; it documents solely the bankruptcy of the company.
SD	If an issuer defaults with respect to a certain financial liability or class of liabilities but is still able to honour its payment obligations under other financial liabilities or classes of liabilities within the requisite period, it is assigned SD (selective default) status.
NR	A debtor or an issuer not rated by Euler Hermes Rating is classified as NR (Not Rated).
PLUS (+) MINUS (-)	Rating notations from AA to CCC may be complemented by a PLUS (+) or MINUS (-) if required, in order to show their relative position within the respective rating category.

© Euler Hermes Rating Deutschland GmbH 2013