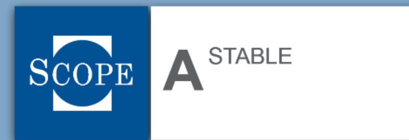
BASF SE
Germany, Specialty Chemicals



Corporate profile

BASF SE is a chemicals company which also operates in related areas such as agriculture, nutrition, and the exploration and production of oil and natural gas. The company is organised into five business segments: Chemicals, Performance Products, Functional Materials & Solutions, Agricultural Solutions, and Oil & Gas. About half of the company's revenues are generated by specialty chemicals while the remainder comes from commodity chemicals and the Oil & Gas segment.

Key metrics

			Scope estimates	
Scope credit ratios	**2016**	**2017**	**2018F**	**2019F**
EBITDA/interest cover (x)	12x	19x	15x	15x
SaD/EBITDA	2.0x	1.3x	1.7x	1.4x
Scope-adjusted FFO/SaD	39%	62%	45%	56%
FOCF/SaD	27%	38%	27%	37%

Rating rationale

On 12 September 2017, Scope affirmed the corporate credit rating of A for Germany-based chemicals company BASF SE and its financing subsidiary BASF Finance Europe N.V. Senior unsecured debt issued by either BASF SE or BASF Finance Europe N.V. is rated A. The short-term rating is S-1. The Outlooks are Stable.

Following the release of the final numbers for 2017, we have updated our forecasts for 2018F and provide Scope-adjusted figures for 2017. The figures reported for 2017 were slightly better than our forecast, with Scope-adjusted debt (SaD)/EBITDA of 1.3x compared to our estimate of 1.4x, primarily due a strong fourth quarter result. Free operating cash flow (as defined by BASF) of EUR 4.8bn was perfectly in line with our forecast.

Going into 2018, we have slightly adjusted the key forecast parameters that affect our financial risk profile assessment and our base case still suggests a slight weakening of credit metrics in 2018F. Effectively, however, we think that BASF's leverage will change only moderately, keeping in mind that earnings and cash flows from announced acquisitions (Bayer's seed and non-selective herbicide business and Solvay's global polyamide) will only be consolidated pro-rata upon closing of the respective transaction. For our assessment of the two bolt-on acquisitions announced last year please see our publication from October 2017.

Our forecast for 2018F includes a minor earnings (EBITDA) contribution from both transactions. At the same time, we have included the cash consideration of EUR 7.5bn for both transactions in the calculation of Scope-adjusted debt. Integration risks for both assets, notably regarding the Bayer deal (EUR 5.9bn), appear manageable and low in our view. The Bayer transaction is structured as an asset deal and we expect a disproportionate effect on EBIT after closing. Overall, our base case for 2018F is roughly in line with BASF's public guidance. For 2018F, BASF expects a "slight decline" in reported EBIT, suggesting a decrease in a magnitude of 1%-10%. This compares with our updated forecast of EUR 8.3bn (versus EUR 8.5bn reported for 2017).

Ratings & Outlook

Corporate ratings	A/Stable
Short-term rating	S-1
Senior unsecured rating	A

Analysts

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Related Research

BASF SE Corporate and Instrument Rating, October 2017

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Our forecast does not include the effects from a potential deconsolidation of Wintershall. In December 2017, BASF announced its intention to merge its oil and gas subsidiaries (Wintershall Group) with the oil and gas activities of LetterOne to form the joint venture Wintershall DEA. Initially, BASF would hold 67% of the joint venture. This shareholding does not include Wintershall's gas transportation business. Upon closing of the planned joint venture, BASF would receive a mandatory convertible bond issued by Wintershall DEA, eventually leading to a BASF stake in Wintershall DEA exceeding 67%.

The formation of the joint venture and completion of the transaction is subject to customary regulatory approvals and closing is expected for the second half of 2018. The joint venture parties (BASF and LetterOne) are currently performing due diligence and the transaction may eventually still fall through. For our thought process, we have assumed that the creation of the joint venture is successful and that the deal is closed in 2018.

Following the closing of the transaction, BASF expects to account for its stake in the Wintershall DEA joint venture under the equity method. In our forecast, we have not de-consolidated the earnings (EBITDA) from the Oil & Gas division (EUR 1.6bn in 2016 and EUR 2.1bn in 2017) and have likewise not de-consolidated the proportionate share of financial debt that is likely to be transferred to the joint venture. The capital structure of Wintershall DEA is still under negotiation and the parties involved have not indicated a target leverage at Wintershall DEA which, in turn, would tell us more about the proportionate share of financial debt to be deconsolidated at the BASF level.

In view of BASF's announcement that an initial public offering for Wintershall DEA is envisaged following formation of the joint venture, we see a good chance that BASF's financials could be influenced positively by the transaction. Much of this potential positive effect, either through the transfer of financial debt from the BASF level to the joint venture or through a secondary placement of a partial stake in conjunction with the IPO of the joint venture, is, however, still not concrete enough to draw conclusions at this stage. We do note, that BASF's management described the potential option of share buybacks in the event of significant deleveraging as "not intelligent" in its full-year results call. Overall, we think that BASF is very likely to use the potential headroom for its financial risk profile that may result from the Wintershall DEA transaction to continue with its portfolio realignment. BASF has a public strategy of continuing its portfolio management witht the goal of achieving a balance of 50% revenues with specialty chemicals and 50% with differentiated commodities. We believe that any financial headroom created by the Wintershall DEA JV is therefore very likely to be used for further bolt-on acquisitions in the future (rather than share buybacks).

Rating drivers

Positive rating drivers	Negative rating drivers
• Strong market position, holding between first and third position for about 70% of its business	• High dependence on general economic environment and on economic development in emerging markets in particular
• Large share of specialty chemicals that are less subject to cyclicality risks and changing feedstock prices	• Risks of sudden negative changes in feedstock prices and exposure to changes in global commodities and food prices
• Broad and globally diversified business; one of the largest integrated chemical companies globally; diversification benefits from presence in agrochemicals, bulk and specialty chemicals	• Still some overrepresentation of business in Europe, a region that is projected to show lower growth rates for chemicals
• History of solid, resilient free cash flow generation, high financial flexibility and proven management commitment to a solid 'A'-rating	• Exposure to very cyclical end markets, such as transportation (automotive) and construction, in the Functional Materials & Solutions segment
• Benefits from large integrated sites worldwide providing higher product yields ('Verbund' concept)	• Dependence on oil and gas price changes for highly cash-generative Oil & Gas division; oil and gas operations not fully controlled and subject to political risks
• Substantial coverage of future pension payments with accumulated pension plan assets covering payments for far more than a decade	

Rating-change drivers

Positive rating-change drivers	Negative rating-change drivers
• Sustainable improvement of debt protection measures to levels of about 1.5x (SaD/EBITDA) and 50% (FFO/SaD)	• Sizeable debt-funded acquisitions leading to a material deterioration in debt protection measures
• Substantial increase in share of specialty chemicals or agrochemicals and reduction in oil-production exposure	• Risks of global oversupply of commodity chemicals, leading to price pressure and margin squeeze in Chemicals division
	• Deterioration in credit protection measures such as SaD/EBITDA to levels of about 2.5x and FFO/SaD of roughly 30%

Financial overview

			Scope estimates	
Scope credit ratios	**2016**	**2017**	**2018F**	**2019F**
EBITDA/interest cover (x)	12x	19x	15x	15x
SaD/EBITDA	2.0x	1.3x	1.7x	1.4x
Scope-adjusted FFO/SaD	39%	62%	45%	56%
FOCF/SaD	27%	38%	27%	37%
Scope-adjusted EBITDA in EUR m	**2016**	**2017**	**2018F**	**2019F**
EBITDA	10,259	12,164	12,625	13,464
Operating lease payment in respective year	446	448	362	362
less: disposal gains fixed assets included in EBITDA	-667	-359	-500	-500
Scope-adjusted EBITDA	**10,038**	**12,253**	**12,487**	**13,326**
Scope funds from operations in EUR m	**2016**	**2017**	**2018F**	**2019F**
EBITDA	**10,259**	**12,164**	**12,625**	**13,464**
less: (net) cash interest as per cash flow statement	-459	-409	-460	-485
less: cash tax paid as per cash flow statement	-1,495	-2,147	-1,884	-2,050
less: pension interest	-190	-176	-180	-180
add: depreciation component operating leases	381	386	302	302
add: dividends received from at-equity	225	498	225	250
less: disposal gains fixed assets included in EBITDA	-667	-359	-500	-500
less: capitalised interest	-92	-68	-150	-150
Change in provisions	-183	185	-150	50
Scope FFO	**7,779**	**10,074**	**9,828**	**10,702**
Scope-adjusted debt in EUR m	**2016**	**2017**	**2018F**	**2019F**
Reported gross financial debt	16,312	18,032	20,032	21,032
less: cash and cash equivalents	-1,911	-6,547	-2,905	-6,785
Cash not accessible	400	400	400	400
add: pension adjustment	2,773	2,119	2,133	2,133
add: operating lease obligation	1,270	1,193	1,193	1,193
add: asset retirement obligations	973	972	972	972
SaD	**19,816**	**16,169**	**21,825**	**18,946**

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