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S&P Global Ratings

Adama Agricultural Solutions Ltd.

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Research Update

Outlook Revised To Negative On Higher Leverage; 'ilAA-' Rating Affirmed On Mitigating Group Support

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Rating Action Overview

- The subdued industry conditions weighed on the profitability of Adama Agricultural Solutions Ltd. ("Adama" or "the Company") in 2023, with our forecast adjusted EBITDA declining to $300 million-$350 million in 2023 from $550 million in 2022, sharply increasing the Company's leverage ratio adjusted net debt to EBITDA to above 7.5x.
- At the same time, we forecast that modest recovery in the crop protection market and decisive management actions to cut costs and preserve cash, e.g. the Company's transformation plan, will underpin EBITDA growth in 2024 to $500 million-$520 million and lower Adama's leverage of 4.5x-5.0x, still above the 2.0x-4.0x range the Company had displayed on average until 2022.
- We are affirming our issuer ratings on Adama Agricultural Solutions Ltd., 'ilAA-/ilA-1+', as the benefits of the potential for extraordinary support from its parent group offset higher leverage. We continue to assess Adama as a moderately strategic subsidiary of Syngenta Group.
- The negative outlook indicates that we may lower the ratings if we fail to see a recovery in Adama's profit and credit metrics in 2024, so that adjusted debt to EBITDA remains above 5.0x; or if the Company's free operating cash flow (FOCF) remains materially negative. We could also lower our rating on Adama if the creditworthiness of the Syngenta Group deteriorates.

Rating Action Rationale

We forecast that oversupply conditions will challenge Adama's EBITDA in 2023. We forecast Adama's S&P Global Ratings-adjusted EBITDA will decline to $300 million-$350 million in 2023, from $550 million in 2022, leading to adjusted debt-to-EBITDA of 7.5x-8.0x. This contrasts with our previous forecast of a leverage ratio of about 4.0x. For context, Adama achieved adjusted EBITDA of over $520 million in each year from 2017 to 2022.

This decline is due to weaker demand for agrochemicals in 2023 owing to prolonged destocking which, coupled with the normalization of supply chains and new industry capacity that continues to come online, has resulted in oversupply conditions and led to an industry-wide deterioration in operating rates, prices and margins. The combination of soft demand and high-cost inventory, reflecting the sharp increase in raw material prices in 2022, also weakened Adama's EBITDA and

margins. At the same time, Adama entered this period of challenging supply and demand fundamentals with a weaker balance sheet owing to increased capital spending and elevated working capital requirements.

We forecast adjusted leverage to remain above the 4.0x in 2024, despite EBITDA growth owing to cost-reduction measures. Our base-case factors in modest top-line growth of 2%-3% in 2024, compared to our estimate of about 15% decline in 2023, and an increase in EBITDA to $500 million-$520 million, still below the levels achieved in 2020-2022. This corresponds to adjusted net debt to EBITDA of 4.5x-5.0x in 2024. Our expectation of improved profitability mainly hinges on management's actions to cut costs (including the Company's transformation plan), shift to higher margin products and take pricing actions, alongside improvement in gross profit margins owing to the gradual depletion of higher-cost inventory. We expect market conditions to modestly improve in 2024, thanks to still-reasonable farmer margins, albeit we foresee continuing challenges in market fundamentals – namely a supply surplus and an uncertain pace of stock replenishment. In our base case, we also consider Adama's exposure to the European and Latin American markets (55% of 2022 revenue), where channel inventory remains a risk, partly due to adverse weather conditions in Brazil at the end of 2023.

Current ratings reflect the benefit of potential extraordinary group support from its parent Syngenta Group, which offset the higher financial leverage on a stand-alone basis. We use our group rating methodology to assess our rating on Adama, which reflects our assessment of its creditworthiness and its relationship with Syngenta Group. As such, our issuer credit rating on the Company factors in potential for extraordinary support from its intermediate parent. Therefore, despite Adama's higher financial leverage, its credit rating benefits from the Company's relationship to Syngenta Group and the potential for extraordinary support from its parent.

Outlook

The negative outlook indicates that we could lower the rating if Adama's EBITDA and leverage were to fall short of our base-case assumptions.

Downside Scenario

We may lower our rating on Adama if its EBITDA margin, FOCF and credit metrics seem unlikely to improve in 2024. This may occur if:

- Adjusted debt-to-EBITDA remains above 5.0x, for example because of weaker-than-expected market rebound, or because management's measures to improve margins do not bring anticipated results;
- FOCF remains negative, without near-term prospects of recovery;

- Further covenant pressure emerges; or
- The Company makes material debt-funded acquisitions or aggressively distributes dividends.

We may also lower our rating on Adama if the creditworthiness of the Syngenta Group deteriorates, or if we change our view of Adama's status within the Syngenta group.

Upside Scenario

We may revise our outlook to stable if we see a recovery across the crop protection market leading to improving credit metrics for Adama to levels we see as healthy for its standalone credit profile, including adjusted leverage declining to 4.0x-5.0x.

Company Description

Adama Agricultural Solutions Ltd. operates in the agrochemical industry. The Company develops, produces and markets off-patented, license-requiring crop protection products. Adama sells its products in about 100 countries through 60 subsidiaries around the world. Adama Agricultural Solutions Ltd. is fully owned by Adama Ltd., a company traded on the Shenzhen stock exchange. In June 2020, Adama Group became a distinctive member of the newly established Syngenta Group Co. Ltd. (BBB+/Stable). The Syngenta Group is a world leader in agricultural inputs, spanning crop protection, seeds, fertilizers and additional agricultural and digital technologies. Syngenta Group is part of China National Chemical Corporation Ltd. (ChemChina, A-/Stable), which is held by Sinochem Holdings Co., Ltd. and ultimately owned by the Chinese government.

Base Case Scenario

Assumptions

- Revenue declining by 14%-15% in 2023, mainly driven by lower sale prices. In 2024-2025, we assume moderate revenue growth of 2%-3% per year.
- Adjusted EBITDA margin of 7.0%-8.0% in 2023. We assume EBITDA margins to improve in 2024-2025 to approximately 12.0%. This is due to our expectation that management actions will reduce costs, and higher-cost inventory will gradually deplete, underpinning an increase in gross profit margins.
- Adjusted EBITDA of $300 million-$350 million in 2023 and $560 million-$570 million in 2024, from $550 million in 2022.
- Capital expenditure (capex) of about $290 million per year in 2023 declining further to about $220 million in 2024, compared with $330 million in 2022.

- Working capital inflow of over $200 million in 2023, including the pay-down of receivables facilities, due to the forecast slowdown in revenue decline, followed by outflows of $30 million-$40 million going forward.
- No material dividend distributions and debt-funded acquisitions in 2023-2024.

Key Metrics

	2021a	2022a	2023e	2024f	2025f
EBITDA margin (%)	12.1	11.2	7-8	~12	12-13
Debt/EBITDA (x)	3.6	4.4	7.0-8.0	4.5-5.0	~4.5
FFO/debt (%)	19.7	13.5	0-5	10-15	10-15
OCF/debt (%)	26.6	(5.8)	~10	10-12	12-14

a--Actual. e--Estimate. f--Forecast. FFO--Funds from operations.

Liquidity

We assess Adama's liquidity as adequate. We forecast that liquidity sources will cover uses by about 1.7x over the 12 months starting Jan. 1, 2024. The Company's liquidity is underpinned by adequate long-term committed credit facilities and cash on hand compared with maturities.

We cap our liquidity assessment at adequate because we do not see enough of a track record, or a commitment from the parent company, to maintain strong liquidity under more adverse cyclical conditions.

Principal liquidity sources for the next 12 months include:

- Unrestricted cash and cash equivalents of about $600 million.
- Undrawn committed bank lines maturing beyond the next 12 months of $260 million.
- Positive cash FFO of about $295 million

Principal liquidity uses for the same period includes:

- Debt maturities of $224 million.
- Year-end working capital outflows of about $40 million.
- Seasonal working capital requirement of about $200 million.
- Capex of about $220 million.

Covenant Analysis

Adama has several covenants incorporated into its bank loan and a securitization agreements tested quarterly. As of December 31, 2023, the Company had received waivers and covenant relaxation for the test periods starting December 2023 and ending December 2024. We estimate that the Company will maintain sufficient headroom under its relaxed covenants, in the near term.

Modifiers

- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Neutral (no impact)
- Comparable ratings analysis: Neutral (no impact)

Recovery Analysis

Key analytical factors

- We affirm our 'ilAA-' recovery rating, identical to the issuer rating, on Adama's Series B bonds. The recovery rating for this series is '3', indicating our expectation of meaningful recovery (50%-70%; rounded estimate: 55%) in a hypothetical default scenario.
- Our recovery expectations reflect proportionately higher amount of subordinated debt in the structure.

Simulated default assumptions

- Simulated year of default: 2029
- In our simulated default scenario, we assume a supply-demand imbalance with demand for the Company's products deteriorating in the wake of a protracted economic downturn, alongside increased supply leading to lower prices, and an increase in raw material prices that the Company will not be able to pass through to its customers.
- We believe a viable business would remain after a default, so lenders would achieve their highest recovery through a reorganization, rather than liquidation.
- We assume that prior to default, the Company will refinance part of its financial debt, since we expect cash generation for debt repayment to remain broadly neutral.
- We assume the committed credit facilities to be 85% drawn at default.
- We assume that the available receivables securitization facility will be about $400 million, and the Company will use 80% of it at default.

Simplified Waterfall

- EBITDA on emergence: about $335 million
- Industry EBITDA multiple: 5.0x
- Administrative costs: 5%
- Enterprise value available for primary unsecured debt: about $1.68 billion
- Estimated priority claims (mainly securitization program outstanding): $330 million
- Estimated secured debt claim: $510 million
- Remaining recovery value: $750 million
- Total senior unsecured debt (including Series B bonds and bank debt): about $1.3 billion.
- Recovery expectations of secondary secured debt: 50%-70%
- Recovery rating for secondary secured debt (1 to 6): 3

All debt amounts include six months' prepetition interest. Securitization facility assumed 80% drawn at default. RCFs assumed to be 85% drawn at default.

Mapping Recovery Percentages To Recovery Ratings

Recovery expectations (%)	Description	Recovery rating	Notching above/below issuer rating
100%	Full recovery	1+	+3 notches
90%-100%	Very high recovery	1	+2 notches
70%-90%	Substantial recovery	2	+1 notch
50%-70%	Meaningful recovery	3	0 notches
30%-50%	Average recovery	4	0 notches
10%-30%	Modest recovery	5	-1 notch
0%-10%	Negligible recovery	6	-2 notches

Recovery ratings are capped in certain countries to adjust for reduced creditor recovery prospects in these jurisdictions. Recovery ratings on unsecured debt issues are generally also subject to caps (see Step 6, paragraphs 90-98 of "Recovery Rating Criteria For Speculative-Grade Corporate Issuers," published Dec. 7, 2016, for further detail). ICR--Issuer credit rating.

Related Criteria And Research

- Principles Of Credit Ratings, February 16, 2011
- Methodology: Industry Risk, November 19, 2013
- Country Risk Assessment Methodology And Assumptions, November 19, 2013
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, November 19, 2014
- Methodology: Jurisdiction Ranking Assessments, January 20, 2016
- Recovery Rating Criteria For Speculative-Grade Corporate Issuers, December 7, 2016

- Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Group Rating Methodology, July 1, 2019
- Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Methodology For National And Regional Scale Credit Ratings, June 8, 2023
- Corporate Methodology, January 7, 2024
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, January 7, 2024
- S&P Global Ratings Definitions, June 9, 2023

Ratings List

Adama Agricultural Solutions Ltd.	Rating	Date when the rating was first published	Date when the rating was last updated
Issuer rating(s)			
Short term	ilA-1+	09/09/2019	24/05/2023
Long term	ilAA-/Negative	27/11/2001	24/05/2023
Issue rating(s)			
Commercial Papers			
Commercial Papers $30 million	ilA-1+	10/12/2019	24/05/2023
Senior Unsecured Debt			
Series B	ilAA-	19/05/2008	24/05/2023
Issuer Credit Rating history			
Long term			
March 27, 2024	ilAA-/Negative		
July 01, 2014	ilAA-/Negative		
July 06, 2011	ilA+/Stable		
September 07, 2010	ilAA-/Negative		
June 29, 2010	ilAA-/Watch Neg		
December 03, 2009	ilAA-/Stable		
March 22 ,2009	ilAA/Negative		
December 11, 2008	ilAA/Watch Neg		
November 26, 2006	ilAA/Stable		
May 10 ,2004	ilAA		
November 27, 2001	ilAA-		
Short term			
September 09, 2019	ilA-1+		

Additional details	
Time of the event	27/03/2024 13:05
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Rating requested by	Issuer

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