Adama Agricultural Solutions Ltd.

March 23, 2021

Primary Credit Analyst:

Hila Perelmuter, 972-3-7539727 hila.perelmuter@spglobal.com

Additional Contact:

Tom Dar, 972-3-7539722 tom.dar@spglobal.com

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Adama Agricultural Solutions Ltd.

Issuer Credit Affirmed	ilAA-/Stable/ilA-1+

Overview

Key Strengths	Key Risks
• High business position in the global crop protection products market. • Ability to increase operations thanks to new product development and distribution capabilities. • Wide geographical spread of operation. • Financial flexibility supported by low maturities and by long-term committed credit facilities.	• Exposure to cyclicality and seasonality in the crop protection market. • Competitive environment, aggravated in recent years due to consolidation processes. • High working capital volatility, mainly due to sale seasonality and different accounts receivable days. • Exposure to exchange rate and commodity price fluctuations.

The Company materially expanded its real scope of operations in 2020 compared with past year, due to robust product demand. On the other hand, its profitability weakened due to the effects of the coronavirus crisis on global currencies, and due to increasing raw materials and logistic costs. The Company's free operating cash flow was negative due to large working capital needs, and its leverage increase, but remained commensurate with the current rating.

We expect the Company's profitability to remain similar in the short term to its 2020 level, i.e. lower than its pre-coronavirus levels. This is due to increased costs, especially logistic costs, and the continued global effects of the coronavirus crisis, although these gradually decrease as the pace of global immunization increases. We expect a more meaningful recovery from the coronavirus crisis in 2022, including in regions such as Brazil and India currently experiencing outbreaks, and later, towards 2023, an improvement in the Company's profitability.

We expect Adama's debt to EBITDA ratio to remain commensurate with the rating in 2021, although at the higher end of this range, as we estimate that its free operating cash flow will remain negative in the short term due to high capex and working capital needs. We believe that, if the Company's EBITDA remains stable or moderately grows in the next two years, alongside a decrease in capex needs and lack of material acquisitions or aggressive dividend distributions, the Company will be able to decrease its debt to EBITDA ratio back to the middle of the range which we consider to be commensurate with the current rating.

We believe there remains high, albeit moderating, uncertainty about the evolution of the coronavirus pandemic and its economic effects. Vaccine production is ramping up and rollouts are gathering pace around the world. Widespread immunization, which will help pave the way for a return to more normal levels of social and economic activity, looks to be achievable by most developed economies by the end of the third quarter. However, some emerging markets may only be able to achieve widespread immunization by year-end or later. We use these assumptions about vaccine timing in assessing the economic and credit implications associated with the pandemic (see our research on S&P Maalot website as well as on S&P Global Ratings website). As the situation evolves, we will update our assumptions and estimates accordingly.

Outlook

The stable outlook reflects our assessment that the Company will maintain an adjusted debt to EBITDA ratio in the 2.0x-4.0x range, commensurate with the current rating. This is assuming that the Company will not endeavor into material mergers and acquisitions or distribute material dividend amounts.

The stable outlook also reflects our assessment that the Company will maintain its large customer base and its leading position in the non-patented crop protection products market. It will do this by continuing to develop new, differentiated products, quickly registering product rights and maintaining wide distribution channels.

We expect pressure on the Company's operation in some global regions in 2021 due to the coronavirus pandemic, and recovery in these regions in 2022 as the rate of global vaccination increases. We still expect the Company to maintain coverage ratios commensurate with the rating despite these effects.

The stable outlook also reflects our assessment that, under the current Israeli regulatory framework, we do not expect any negative intervention by ChemChina which would jeopardize the Company's stability, and that ChemChina's stand alone credit profile (SACP) will remain at a level that continues to allow its insulation from the rating on Adama.

Downside Scenario

We may consider a negative rating action if we see a deterioration in the Company's operating performance or if the Company's EBITDA margin materially declines. We may also consider a negative rating action if the Company's adjusted debt to EBITDA increases to 4.0x and above, or if the Company's free operating cash flow remains negative on a sustainable and long-term basis. This scenario could materialize, for example, if the Company makes materially larges leverage acquisitions

than our base case scenario assumes, or aggressively distributes dividends. This scenario could also materialize if we see that the effects of the coronavirus pandemic on the Company's performance is wider and longer-lasting than we expected, e.g. if global supply chains are jeopardized, if demand decreases in pandemic-ridden regions, or if commodity prices sharply increase from their current level.

We may also consider a negative rating action of ChemChina's SACP materially deteriorates, such that we cannot continue to insulate the Company's rating according to our Group Rating Methodology.

Upside Scenario

We may consider a positive rating action if the Company's financial risk profile continues to improve such that its adjusted debt to EBITDA ratio is consistently lower than 2.0x and its adjusted free cash flow to debt ratio is about 25%, and the Company consistently and robustly generates positive free operating cash flow. A positive rating action would also depend on maintaining the current business risk profile and at least adequate liquidity, and is subject to our assessment that ChemChina's SACP has materially improved.

Base Case Scenario

Key Assumptions

- S&P Global's assumptions regarding global recovery. Expected GDP growth of about 6.5% in 2021 and 3.1% in 2022 in the U.S.; 4.2% and 4.4%, respectively, in the Eurozone; and 5.5% and 4.2%, respectively, globally.
- A 4%-5% increase in revenues in 2021, alongside continued moderate decline in gross profitability to about 27%. In 2022 we expect continued global recovery and an additional ~5% increase in revenues.
- The EBITDA margin will decline accordingly to about 12%-13%.
- Adjusted EBITDA of about $520 million - $530 million in 2021 and about $540 million - $550 million in 2022.
- Large capital expenditure (capex) of about $200 million - $300 million per year in 2021-2022.
- Large working capital needs of about $200 million in 2021-2022 to support growth.
- No material dividend distributions and acquisitions in 2021-2022.

Key Metrics

	2020A	2021E	2022E
EBITDA margin	13.5%	12.5%-13.0%	13.0%-13.5%
Debt/EBITDA	3.7x	3.8x-4.0x	3.3x-4.0x
FFO/debt	20.1%	20%-23%	~20%-25%

A - actual. E – Estimate. FFO – funds from operations.

Base Case Projections

A ~4%-5% increase in revenues, continued weakness in profitability

We expect strong demand for the Company's product to maintain existing scope of operations, supported by recovery of markets from the coronavirus crisis and higher GDP in most regions of operations. However, we believe there could be pressure on demand in coronavirus-ridden regions such as Brazil and India, as well as on input costs (raw materials, shipping and logistics). We also believe that intense competition will prevent the Company to fully transfer the cost increase to the customer final price. The adverse effects of exchange rates may also continue. We therefore believe that gross profitability will only return to pre-coronavirus levels towards 2023.

Negative free cash flow in the short term

The Company has large short-term capex and working capital needs to support its growth in operation. We therefore expect the coverage ratio debt to EBITDA not to decline in the short term, but remain commensurate with the rating barring material acquisitions or dividend distributions.

We believe that in 2022-2023, with global recovery and lower capex needs, and thanks to moderate EBITDA growth, the Company may be able to decrease its debt to EBITDA to the middle of the range we consider to be commensurate with the current rating, i.e. to 3.5x. This assumes no material acquisitions or dividend distributions.

Company Description

Adama Agricultural Solutions Ltd. operates in the agrochemical industry. The Company develops, produces and markets non-patented but 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 and controlled by China National Chemical Corporation Limited ("ChemChina", BBB/Positive) owned by the Chinese government.

Business Risk Profile

Adama's business risk profile is underpinned by a high business position in the global agrochemical industry. The Company is the seventh largest in this industry in terms of revenue and the larges among companies that focus on non-patented products. Adama's revenue base and products are mainly concentrated in the crop protection segment. Despite this concentration, we expect the agrochemical industry in general, and the crop protection product market in particular, will remain lucrative in the medium- to long term. This is due to the fact that the agrochemical industry benefits from demand underpinned by long-term demographic trends and by changes in nutrition habits, that lead to intensive use of crop protection products in order to increase land yield.

The industry is characterized by high barriers to entry stemming from strict product licensing regulatory requirements. Crop protection products are sold under state authority supervision in each country. Strict licensing requirements make it difficult for new companies to enter the industry.

Adama benefits from high reputation among customers and suppliers. However, the Company operates in a competitive market and thus is only partly able to adjust product prices to raw material prices and thus limit the decline in profitability when raw material prices are on the rise. Several leading global companies operate in the crop protection product industry, some of which have become even stronger in recent years following consolidation processes. These companies have substantial financial resources which they invest, among other things, in research & development.

The Company has global marketing and distribution abilities reflected in wide geographical spread of sales which decreases exposures inherent to the Company's operations and limits dependence on conditions in single markets. Among other things, the Company is exposed to cyclicity and seasonality in the agrochemical industry. Sales change with agricultural seasons and with yield cyclicity. Volatility in farmers' revenue and their decision to purchase crop protection products are affected by changes in agricultural product prices. The Company is exposed to weather changes, as its products target the agricultural market such that extreme weather conditions and natural catastrophes (floods, frost, drought) directly affect their demand. The Company is also exposed to increases in the price of raw materials, especially oil prices, and extreme changes in oil prices and energy costs may weaken its profitability.

Financial Risk Profile

In the first quarter of 2021, the Company's debt to EBITDA increased to 4.0x, following an increase to 3.7x in 2020 due to the adverse effects of the coronavirus crisis, the increase in raw material prices, and high logistics costs. The increase in this ratio was also due to weakness in currency rates,

especially for the Brazilian Real. However, the leverage ratio is still in the range commensurate with the current rating, albeit at its upper end.

We believe the Company's debt to EBITDA ratio will remain stable in the short term given the Company's large capex and working capital needs which will continue to lead to negative free cash flows. We believe the Company will deleverage to the middle of our target range once it completes these growth actions and moderately improves its EBITDA.

The Company is exposed to exchange rate fluctuations, which affect the volatility of financial ratios. The Company publishes its statements in U.S.D., while its operations and obligations use other currencies as well, such as Euro, New Israeli Shekel and Brazilian Real. The Company uses hedging instruments that mitigate part of this exposure.

Table 1.

ADAMA Agricultural Solutions Ltd. – Financial Summary (Mil. $)

Industry Sector: Chemical Cos

	2020	2019	2018	2017	2016
Revenue	3,867.9	3,679.2	3,535.7	3,137.4	3,070.2
EBITDA	523.7	595.2	554.9	551.4	501.0
Funds from operations (FFO)	388.4	423.3	400.3	423.8	362.9
Interest expense	102.9	121.1	106.1	110.1	118.5
Cash interest paid	93.2	92.1	79.8	85.8	94.3
Working capital changes	(286.9)	(510.5)	(162.7)	(99.3)	107.5
Cash flow from operations	146.5	(50.9)	90.0	420.1	445.6
Capital expenditure	205.5	192.6	176.7	204.4	187.9
Free operating cash flow (FOCF)	(59.1)	(243.6)	(86.7)	215.7	257.7
Dividends paid	5.0	6.3	4.4	26.5	22.7
Discretionary cash flow (DCF)	(64.1)	(249.9)	(91.1)	189.2	235.0
Cash and short-term investments	348.3	379.0	594.0	873.0	480.0
Gross available cash	348.3	379.0	594.0	873.0	480.0
Debt	1,934.6	1,694.9	1,182.5	1,383.3	1,365.3
Equity	2,446.3	2,382.5	2,266.2	1,854.7	1,654.3
Adjusted ratios					
Annual revenue growth (%)	5.1	4.1	12.7	2.2	0.2
EBITDA margin (%)	13.5	16.2	15.7	17.6	16.3
Return on capital (%)	6.6	9.8	10.6	13.4	12.2
EBITDA interest coverage (x)	5.1	4.9	5.2	5.0	4.2
FFO cash interest coverage (x)	5.2	5.6	6.0	5.9	4.8
Debt/EBITDA (x)	3.7	2.8	2.1	2.5	2.7
FFO/debt (%)	20.1	25.0	33.8	30.6	26.6
Cash flow from operations/debt (%)	7.6	(3.0)	7.6	30.4	32.6
FOCF/debt (%)	(3.1)	(14.4)	(7.3)	15.6	18.9
DCF/debt (%)	(3.3)	(14.7)	(7.7)	13.7	17.2

Liquidity

The Company's liquidity is adequate, underpinned by adequate long-term committed credit facilities and cash on hand compared with maturities. We estimate that the ratio between the Company's sources and uses in the 12 months starting April 1, 2021, will be 1.2x-1.5x.

Following are the Company's main sources and uses for the period between April 1, 2021, and March 31, 2022:

Principal Liquidity Sources	Principal Liquidity Uses
• About $407 million in cash and cash equivalents. • About $470 million in unused committed credit facilities for a period of over 12 months • About $400 million in FFO (funds from operations) (our estimate).	• Ongoing maturities and bonds and short- and long-term bank loans of about $500 million. • Capital expenditures (capex) of about $250 million - $300 million. • Seasonal working capital needs of about $200 million.

Debt Maturities

Period	1/4/2021-31/3/2022 (*)	1/4/2022-31/3/2023	1/4/2023-31/3/2024	1/4/2024-31/3/2025	1/4/2025 onwards
Maturities (Mil $)	~505	~155	~150	~125	~965

(*) including short-term debt maturities.

Covenant Analysis

The Company has several covenants vis-a-vis banks and in a securitization transaction. We understand that, as of the first quarter of 2021, the Company has sufficient headroom on its financial covenants, and we estimate that it will maintain sufficient headroom in the short term.

Modifiers

Diversification/portfolio effect: Neutral

Capital structure: Neutral

Liquidity: Neutral

Financial policy: Neutral

Management and governance: Neutral

Comparable ratings analysis: Neutral

Group Influence

Adama Agricultural Solutions' rating reflects both its stand-alone credit profile and its relationship with ChemChina in the context of our Group Rating Methodology.

We believe Adama Agricultural Solutions' strategic importance to its ultimate parent, ChemChina, remains moderate. ChemChina's credit rating is underpinned by potential extraordinary support from the Chinese government in times of need, due to ChemChina's strategic importance. Due to this support factor, ChemChina's credit rating is higher than its SACP.

However, government support for ChemChina does not support the rating on Adama Agricultural solutions, as Adama Agricultural Solutions and its parent company, Adama Ltd., generate a relatively small portion of ChemChina Group's consolidated EBITDA. Therefore, our reference point in rating the Company in the context of our Group Rating Methodology is ChemChina's SACP. However, we still consider our rating on Adama Agricultural Solutions to be somewhat isolated from ChemChina's SACP, due to regulatory limitations that apply to reported private companies whose bonds are traded on the Tel Aviv Stock Exchange and that may prevent the Company from supporting ChemChina Group in a way that would jeopardize the Company's stand-alone credit quality.

Recovery Analysis

Key analytical factors

- We are affirming our 'ilAA-' rating, identical to the issuer rating, on Adama's Series B bonds. The recovery rating for this series is '3', reflecting our assessment that in the case of a hypothetical default, the recovery rate would be 50%-70% (in the middle of this range).

Simulated default assumptions

- Simulated year of default: 2026
- Demand for the Company's product will decrease due to a global recession, increased competition and an increase in raw material prices which the Company will not be able to impose on its customers.
- The Company will continue to operate as a going concern.
- In the deterioration process, the Company will repay part of its financial debt, owing to its large cash reserves and its cash flow generation abiity.
- Later in the deterioration process, the Company will use about 85% of its committed credit facilities.
- The receivables securitization balance will be about $300 million, similarly to its year-end 2020 level, and the Company will use 80% of it in the deterioration process.

Simplified Waterfall

- EBITDA on emergence: about $320 million
- Industry EBITDA multiplier: 5.0x
- Gross enterprise value as going concern: about $1.6 billion
- Administrative costs: 5%
- Enterprise value available for primary unsecured debt: about $1.52 billion
- Total primary unsecured debt (including use of committed facilities and receivables securitization): about $740 million
- Enterprise value available for secondary unsecured debt: about $780 million
- Total secondary unsecured debt (including Series B bonds and bank debt): about 1.46 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.

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, December 7, 2016, for further detail). ICR--Issuer credit rating.

Reconciliation

In order to create a basis for comparison with other rated companies, we adjust the data reported in the financial statements which we use to calculate financial ratios. The main adjustments we made to Adama Agricultural Solutions Ltd’s consolidated data for 2020 are as follows:

- Deducting about $260 million in cash and cash equivalents available for debt service from financial debt.
- Adjusting debt by about $300 million due to receivables securitization.
- Adjusting debt by about $60 million due to post retirement benefits obligations.

Table 2.

ADAMA Agricultural Solutions Ltd.--Reconciliation Of Reported Amounts With S&P Global Ratings' Adjusted Amounts (Mil. $) for the Fiscel Year Ended Dec 31, 2020

ADAMA Agricultural Solutions Ltd. reported amounts

	Debt	EBITDA	Interest expense	S&P Global Ratings' adjusted EBITDA	Cash flow from operations
Reported	**1,752.8**	**505.6**	**101.2**	**523.7**	**142.6**
S&P Global Ratings adjustments					
Cash taxes paid	--	--	--	(42.1)	--
Cash interest paid	--	--	--	(93.2)	--
Trade receivables securitizations	301.9	--	--	--	(3.9)
Reported lease liabilities	80.5	--	--	--	--
Postretirement benefit obligations/deferred compensation	60.6	3.5	1.7	--	--
Accessible cash and liquid investments	(261.2)	--	--	--	--
Share-based compensation expense	--	2.7	--	--	--
Dividends received from equity investments	--	7.8	--	--	--
Nonoperating income (expense)	--	--	--	--	--
Reclassification of interest and dividend cash flows	--	--	--	--	7.8
EBITDA: Other	--	4.1	--	--	--
Total adjustments	**181.8**	**18.1**	**1.7**	**(135.3)**	**3.9**

S&P Global Ratings adjusted amounts

	Debt	EBITDA	Interest expense	Funds from operations	Cash flow from operations
Adjusted	**1,934.6**	**523.7**	**102.9**	**388.4**	**146.5**

Related Criteria And Research

- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, November 13, 2012
- Methodology: Industry Risk, November 19, 2013
- Country Risk Assessment Methodology And Assumptions, November 19, 2013
- Corporate Methodology, November 19, 2013
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, December 16, 2014
- Recovery Rating Criteria For Speculative-Grade Corporate Issuers, December 7, 2016
- Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Group Rating Methodology, July 1, 2019
- S&P Global Ratings Definitions, January 5, 2021

Ratings List

Adama Agricultural Solutions Ltd.	Rating	Date when the rating was first published	Last date when the rating was updated
Issuer rating(s)			
Short term	ilA-1+	09/09/2019	26/05/2020
Long term	ilAA-/Stable	27/11/2001	26/05/2020
Issue rating(s)			
Commercial Papers			
Commercial Papers $30 million	ilA-1+	10/12/2019	26/05/2020
Senior Unsecured Debt			
Series B	ilAA-	19/05/2008	26/05/2020
Issuer Credit Rating history			
Long term			
July 01, 2014	ilAA-/Stable		
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	23/05/2021 11:02		
Time when the event was learned of	23/05/2021 11:02		
Rating requested by	Issuer		

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