EF1

INSTRUMENT RATING

Neu CP

Initiation date	02/12/2022
Rating date	27/11/2023

Contacts

Associate
Mickael KEREZEON
mickael.kerezeon@ethifinance.com

RATING ACTION AND RATIONALE

- EthiFinance Ratings has reaffirmed its short-term rating for the €1.75bn NEU CP programme of Sodexo Finance DAC (Sodexo), at EF1. Sodexo S.A. is guarantor of the NEU CP instruments issued by Sodexo Finance DAC.
- The reaffirmation of our EF1 rating, outlines the company's extensive global footprint and its diverse range of services, spanning from food services to facility management. These activities cater to a broad spectrum of end-markets, including Education, Corporate Services, and Healthcare. This comprehensive portfolio positions Sodexo favorably against local competitors, granting it a competitive edge, and the ability to deliver integrated services across multiple countries. In a strategic move, Sodexo rebranded its BRS activity, encompassing prepaid cards, restaurant vouchers, mobility passes, and leisure passes, as Pluxee in June 2023. This subsidiary, which generated €1.1bn revenue in FY23, was reported as a discontinued activity at end-August 2023, in anticipation of its upcoming spin-off, scheduled for early 2024. This corporate development is expected to adversely impact Sodexo's credit ratios. Nevertheless, we remain optimistic about Sodexo's dominant position in the market and expect a gradual financial recovery following the spin-off. Our adjusted leverage ratio increased from 2.3x at YE22 (inclusive of Pluxee), to 2.9x at YE23 (Sodexo on a standalone basis). Our forecast anticipates an improvement, projecting the adjusted leverage ratio to decrease to 2.4x at YE26, aligning with the guidance. Additionally, we value the group's credit profile, supported by a prudent financial policy and robust ESG commitments, with the company progressing steadily towards its ambitious targets.
- Our rating is, however, slightly constrained by the anticipated impact of the spin-off on credit metrics. The exclusion of Pluxee significantly influenced credit metrics for two primary reasons. Firstly, as of YE23, Pluxee exhibited a robust financial structure, boasting a net cash position of €1.8bn (after settlements of Intercompany payments). Secondly, it demonstrated strong growth historically (27.1% in FY23), and maintained a higher underlying operating profit margin (33.1% in FY23) compared to Sodexo's traditional business (4.3%). However, the negative impact of this exclusion is mitigated by our updated methodology. This now positively counts a company ESG score between 1 and 1.5 in our financial assessment, which applies to Sodexo.
- In line with our methodology, the Service & Retailing industry has medium ESG risks (heatmap score of between 2 and 3.5), which is neutral in our industry assessment.

ISSUER DESCRIPTION

Founded in 1966, Sodexo is a French company that offers food services and facility management services across various sectors, including business and administrations, healthcare and seniors, and education. As one of the leading global companies in its industry, Sodexo operated in 45 countries, as of August 2023. It's primary source of revenue, up to 96%, comes from its on-site services. Geographically, these services are distributed across three main regions, with North America accounting for around 46%, Europe c. 36%, and the Rest of the World the remaining c. 18%.

In June 2023, Sodexo's BRS activity (€1.1bn of revenue in FY23), which offers prepaid cards, restaurant vouchers, mobility passes, leisure passes, was rebranded as Pluxee, and was reported as discontinued activities; in preparation for a spin-off. This operation is expected to take place after being put to a shareholder vote in a dedicated General Meeting, through a distribution of shares to Sodexo shareholders in early 2024; along with a listing on Euronext Paris. From Sodexo's financial standpoint, this operation will be dilutive in terms of EBITDA, and will releverage the group. In FY22, EBITDA margin was at 7.2% (inclusive of Pluxee) versus 6.2% (Sodexo standalone). In addition, at the end of August 2023, Pluxee had a net cash position of €1.8bn after taking into account intercompany payments between Sodexo and Pluxee, which are expected to be settled just before the IPO date.

Sodexo's revenues for FY23 were €22.6bn (up by 11.7% compared to last year with Sodexo excluding Pluxee), along with an adjusted EBITDA of €1.4bn. At end-August 2023, our proforma adjusted net leverage ratio stood at 2.9x, compared with 2.3x last year. The weakening of this ratio is due to the expected spin-off.

FUNDAMENTALS

BUSINESS PROFILE

INDUSTRY RISK ASSESSMENT

- **Rather good prospects for the catering industry**

Over the past few years, catering activities have recovered well from the impact of the Covid-19 pandemic, due to the gradual reopening of collective catering. These are now essentially back to normal.

This industry is in a state of constant renewal in order to meet the changing expectations of customers, with more digitalized interactions. We believe that, given its comfortable positioning within the sector, with very good client retention (95.2% in FY23); Sodexo is well placed to take advantage of growth opportunities.

- **Brand image & size are moderately effective barriers to entry**

Although we consider that niche brands can emerge quickly in the market, becoming a leading company is more difficult. This is because of the multitude of long-term partnerships needed to develop global brands, and the efficient supply chain and operations needed to be built in order to be profitable. Consequently, we consider barriers to entry to be rather significant.

- **Moderate degree of volatility**

The majority of Sodexo's activities and its suppliers have exposure to food commodity price increases (such as grain or meat). However, a large portion of Sodexo's activities are based on contracts that are inflation-indexed. As a result, Sodexo can pass inflation through to clients, thereby driving the growth in revenues while maintaining profitability.

COMPANY'S COMPETITIVE POSITIONING

- **Sodexo has solid position & market share**

In a highly competitive market - due to a high number of players – we see Sodexo's large scale and global presence as strong competitive advantages compared to local, smaller rivals, enabling it to offer integrated services in many countries. These advantages provide it with greater pricing power, compared to others in the sector, and increasing the likelihood of client retention. Furthermore, we value it's exposure to non-cyclical sub-sectors such as healthcare, education or seniors care (together representing a significant portion of group sales), which provides good protection against the troughs of the economic cycles.

- **Good geographical diversification**

Sodexo's rating is supported by a good geographical diversification with a strong presence across Europe and the Americas. These regions provide the bulk of Sodexo's revenues (36% and 46% respectively for FY23).

- **Solid ESG policy**

Sodexo, is a leading global company in the food services sector. It is committed to addressing ESG issues through its strategy, "Better Tomorrow 2025". An example of their environmental commitment is their carbon reduction initiative, approved by the Science Based Targets initiative, aiming to reduce direct carbon emissions by 34% by 2025, from the 2017 base. At end-August 2023, Sodexo had almost achieved its target, with a significant reduction in direct GhG emissions of -32.9%. Furthermore, Sodexo launched the "WasteWatch" program in 2019, aimed at reducing food waste by 50% by 2025. Implemented in 57% of food sites based on raw material cost, this solution has already resulted in an average food waste reduction of 37.6% on the sites where it was implemented.

GOVERNANCE

- **Shareholders**

Sodexo is listed on Euronext Paris with a market capitalization of €14.7bn as of November 9th 2023. It is controlled by the family-owned holding company Bellon SA (42.8% of Sodexo shares and 57.8% of the voting rights as of end-August 2023). As of August 2023, the bulk of the rest of the capital was held by institutional investors, and the remainder by employees and individual investors.

- **Management quality**

Since September 2021, Sophie Bellon has been the CEO of Sodexo, in addition to her functions as chair of the board since 2016. However, this combination of roles is somewhat mitigated by her good track record. This is notably her management of the company through the Covid-19 pandemic.

In addition, we view Sodexo's financial policy as rather conservative. We view the dividend policy - which aims to distribute 50% of the underlying net profit - as reasonable given the recurrent nature of the company's revenues. This is in addition tothe low CapEx (below 2% of its sales historically, 1.5% in FY23 excluding Pluxee).

FINANCIAL PROFILE

For comparability reasons, the following analysis will excludes Pluxee for FY22 figures

RESULT AND PROFITABILITY

- **Strong increase in revenues and slightly improved EBITDA margins**

Sodexo's revenues for FY23 were €22.6bn, up by 11.7% at current exchange rates (10.2% excluding currency effects). This increase is notably explained by the performance in North America, with revenues of €10.5bn versus €8.8bn last year, equivalent to a growth of 18.7%. In this continent, Sodexo benefited from Corporate Services revenues, boosted by resilient client retention, ongoing returns to the office, new contracts, and a favorable currency effect. Rest of the World was up by 11.7% supported by new openings and price adjustment. Finally, Europe was up by 3.8% at €8.1bn versus €7.8bn, negatively impacted by the closure of Covid testing in the UK, which partially the offset improvement in price revisions, and the return to office.

On the profitability side, our adjusted FY23 EBITDA stood at €1.4bn versus €1.2bn in FY22, equivalent to a growth of 13.2%. Our figures show a slight improvement in EBITDA margin at 6.2% versus 6.1%. This is due to a better operating mix towards North America, as well as inflation management resulting in price adjustments in all areas. Going forward, we expect margins to improve slightly to 6.3% over our forecast period (FY24-FY26).

CASH-FLOW AND LEVERAGE

- **Deteriorated YE23 leverage ratio (excluding Pluxee) that is expected to decrease with operating cash generation**

Operational cash generation was strong for FY23, with FFO amounting to €1.1bn versus €977m the previous year. The negative impact of the change in working capital requirements (WCR) of €222m weighed on cash generation. Our FY23 adjusted FCF (after leases repayments and dividends) amounted to €20m versus €22m last year. This was mainly due to some residual unwinding of government Covid-linked payment delays in North America and Northern Europe, a change in supplier payment delays in Europe, as well as a significant payroll timing impact in North America. As mentioned above, the adjusted leverage ratio of the group increased from 2.3x at YE22 (including Pluxee), to 2.9x at YE23 (excluding Pluxee). Moreover, Pluxee had a net cash position. However, in line with the guidance provided by the company, we forecast a gradually decreasing leverage ratio, to 2.4x at end-August 2026, closer to the pre-spin-off level.

SOLVENCY AND LIQUIDITY PROFILE

- **Well-spread maturities and significant sources of liquidity in its credit facilities**

As of end-August 2023, the group reported gross financial debt of €5.6bn, excluding IFRS 16 (€831m), as well as the deconsolidation of Pluxee’s debt (€645m). Our adjusted gross financial debt includes IFRS 16 and pensions (€265m), and we calculate a net adjusted debt of €4.0bn. Debt is almost exclusively composed of bonds with maturities ranging from January 2024 to April 2031.

In addition to the existing bonds, Sodexo has access to multicurrency credit facilities exceeding €1.8bn, which were all undrawn at end-August 2023. The main maturity of these facilities amounting to €1.4bn at end-August 2023, (of which $785m is in US dollar) will occur only in July 2026. In addition, Sodexo had bilateral credit facilities for a total of €450m, €300m maturing in December 2023 and €150m maturing in February 2024, with no drawings at the end of August 2023. Finally, it has two commercial paper programs (NEU CP), each amounting to €1.75bn, none of which were drawn at YE23. Note that the issuing companies are Sodexo SA and Sodexo Finance DAC. However, the NEU CP instrument of Sodexo Finance DAC benefits from the independent, autonomous, irrevocable, and unconditional guarantee of the parent company (Sodexo SA), which runs until 28th February 2025.

Please note that on November 10, 2023, following the end of the process of soliciting consent from creditors due to the spin-off, Sodexo redeemed a €300m bond maturing in May 2025.

- **Excellent liquidity and strong refinancing profiles**

We assess the liquidity profile of Sodexo as “Superior”, the best category according to our short-term methodology. This reflects Sodexo's strong refinancing profile and very strong liquidity, more than enough to cover debt maturities for more than two years.

MODIFIERS

- **Controversies**

Over the course of our review, we have not identified any significant controversies regarding Sodexo.

- **Country risk**

Sodexo operates essentially in the US and in Europe, and therefore does not present any particular country risk.

MAIN FINANCIAL FIGURES

Main financial figures. millions of (€ m)	FY21	FY22	FY22R	FY23	23vs22R	22vs21
Turnover	17 428	21 125	20 263	22 637	11.7%	21.2%
EBITDAR adjusted	957	1 526	1 235	1 398	13.2%	59.5%
EBITDA Margin	5.5%	7.2%	6.1%	6.2%	0.1pp	1.7pp
EBIT	420	1 049	815	976	19.8%	149.8%
EBIT Margin	2.4%	5.0%	4.0%	4.3%	0.3pp	2.6pp
EBT	529	1 158	923	1 135	23.0%	118.9%
Total Assets	18 991	20 920	n.a.	20 794	n.a.	10.2%
Equity	3 175	4 425	n.a.	4 554	n.a.	39.4%
Total Financial Debt	8 157	7 929	n.a.	6 689	n.a.	-2.8%
Net Financial Debt	3 556	3 447	n.a.	4 019	n.a.	-3.1%
Equity/TFD	38.9%	55.8%	n.a.	68.1%	n.a.	16.9pp
NFD/EBITDA	3.7x	2.3x	n.a.	2.9x	n.a.	-1.5x
Funds From Operations	753	1 243	977	1 130	15.7%	65.1%
FFO/NFD	21.2%	36.1%	n.a.	28.1%	n.a.	14.9pp
EBITDA/Interest	8.8x	14.0x	11.4x	8.8x	-2.6x	5.2x

FY22R corresponds to the restated figures for the expected spin-off, which have been added to this table to make it easier to understand developments in FY23. Please note that balance sheet figures have not been restated.

CREDIT METRICS EXPECTED EVOLUTION (CMEE)

- **Stable CMEE**

We assess the CMEE to be Stable, as we expect Sodexo's credit metrics, after being impacted by the spin-off, to change in a contrasting manner. We anticipate a slight improvement in the adjusted leverage ratio, while the interest coverage is expected to weaken slightly due to the rise in interest rates.

RATING SENSITIVITY

- List of rating:
- **ST Corporate Rating: EF1**

- **Instrument rating positive factors (↑).**

An upgrade to EF1+ is rather improbable at present. It would require a material improvement of the group’s financial metrics, in particular a net adjusted leverage below 1.0x on a sustainable basis.

- **Instrument rating negative factors (↓).**

A downgrade to EF2 could be considered if the net adjusted leverage ratio remains at the current level (2.9x) on a long-term basis, which could result from a deterioration of the operating cash flow generation. Other factors that could lead to this scenario include debt-funded acquisitions, which would also impact our assessment of the group's financial policy. Such evolution would entail a downgrade of our long-term rating used as a reference for the short-term rating.

REGULATORY INFORMATION

LEI: 969500LCBOG12HXPYM84

Initiation report: No

Rating initiation: 2 December 2022 at EF1.

Last rating action: 2 December 2022 at EF1.

Rating nature: Solicited NEU CP instrument public rating

With rated entity or related third party participation: Yes

With access to internal documents: No

With access to management: Yes

Ancillary services provided to the rated entity: In accordance with Article 6 (2), in conjunction with Annex I, section B (4) of the Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009, it is reported that during the last 12 months EthiFinance Ratings has not provided ancillary services to the rated entity or its related third parties.

Name of the rating committee chair: Marc Pierron, Senior Director.

Material sources used to support the rating decision:

- Consolidated financial statements FY23, FY22, FY21
- Company presentation and 2023 annual and integrated reports
- Bloomberg

Limitation of the Rating action:

EthiFinance Ratings believes the quality and quantity of information available on the rated entity is sufficient to provide a rating.

EthiFinance Ratings has no obligation to audit or verify the accuracy of data provided.

The rating was carried out in accordance with Regulation (EC) N°1060/2009 of the European Parliament and the Council of 16 September 2009, on credit rating agencies, and in accordance with the short-term and long-term corporate rating methodologies that can be consulted on https://www.ethifinance.com/en/ratings/methodologies and according to the short-term corporate rating scale available at https://www.ethifinance.com/en/ratings/ratingScale

ETHIFINANCE RATINGS S.L.

18 Calle Velazquez

CP 28001 Madrid (SPAIN)

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