Industry Top Trends Update

Building Materials

Widespread growth in most European countries

Renato Panichi
Milan
renato.panichi@
spglobal.com
+39 02 72 111 215

What's changed?

We revised to stable three-quarters of negative outlooks in the speculative-grade category. At mid-2021, only 18% of speculative-grade companies had a negative outlook, down from 70% at end-2020. This reflects our expectation of continued solid performance in 2021, after a steady recovery in second-half 2020.

Rising raw material costs have only resulted in limited margin pressure. This reflects companies' focus on operating efficiency and ability to pass on higher raw material costs to final products, due to solid demand for building material products. As such, we expect EBITDA margins will remain at a high level within the cycle.

Dividend recapitalization has picked up. During the first half of 2021, about one-thirds of companies in the 'B' rating category paid dividends to their private equity owners, reflecting benign financial and operating conditions. As result, we anticipate no or limited financial deleveraging in 2021.

How is recovery taking shape?

Revenue will rebound to pre-pandemic levels by end-2021. This reflects strong volume growth in the first half of 2021 and healthy backlogs at least for the next couple of years, sustained by recovered consumer demand and fiscal stimulus.

Cheap debt and improved business confidence support more spending and mergers and acquisitions. Capital expenditure should increase 23% in 2021, following a 13% drop in 2020. As such, we expect limited or no deleveraging for investment-grade companies in 2021.

Infrastructure and residential building renovation are leading the recovery. We expect the rebound in residential construction to center on renovation rather than new construction, which also reflects Europe's demographic trends. Companies more exposed to commercial construction should recover to 2019 levels only in 2023.

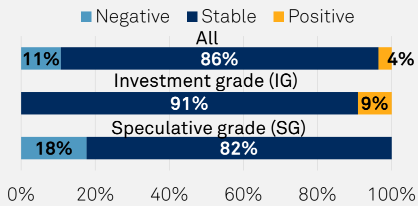
What are the key risks around the baseline?

A quick return to aggressive financial policies. Financial policy is among the key potential drivers of future rating actions on large companies; some have already announced they will return to their pre-pandemic shareholder friendly plans, which include larger dividends or share buybacks.

Persistently high cost inflation leading to a severe margin decline. Building material companies have so far been able to contain margin pressure from increased raw material costs, but persistently high cost inflation, for example spreading to energy and labor, could significantly reduce margins and cash flow.

"Carbon leakage" should be a limited risk for EU-based cement players in the medium term. The EU's carbon cross-border adjustment mechanism should mitigate the negative effects of the progressive phase-out of free carbon allowances. Still, there is a risk of EBITDA reduction if the phase-out is too quick and companies are unable to pass the higher carbon costs on to clients.

Outlook Distribution



Ratings Statistics*

	IG	SG	All
Ratings	11	17	28
Downgrades	0	1	1
Upgrades	2	0	2

Ratings data as of end-June 2021. *Year to date.

COVID-19 Heat Map

Building Materials	
Estimated recovery to 2019 credit metrics	H2 2021
Potential negative long-term industry disruption	No

2020 Versus 2019		
Revenue decline	EBITDA decline	Incremental borrowings
5%-10%	0%-10%	5%-10%

2021 Estimates Versus 2019	
Revenue decline	EBITDA decline
0%-10%	0%-10%

Capital Expenditure Outlook