

Fitch Affirms Legrand at 'BBB'; Outlook Stable

Fitch Ratings-London/Paris-16 November 2009: Fitch Ratings has today affirmed French-based Legrand SA's (Legrand) Long-term Issuer Default Rating (IDR) and senior unsecured rating at 'BBB' respectively, whilst affirming its Short-term IDR at 'F2'. The Outlook for the Long-term IDR remains Stable.

The rating affirmation reflects Legrand's proven resilience to the severe downturn in many of its end-markets. The ongoing weakness in many regional construction markets has led to a significant fall in demand for Legrand's products, resulting in a 16% year-on-year fall in sales as of Q309. However, the company has, to date, been successful at cutting costs to the extent that its EBITDAR margins have not eroded significantly. Fitch expects Legrand's EBITDAR margin to equal about 19% in FY09, compared with 21% in FY08. This, along with a temporary unwinding of working capital, has ensured robust free cash flow (FCF) (with FCF /sales totalling 11% as of Q309), which has helped to protect Legrand's credit metrics.

Nevertheless, challenges remain for Legrand's credit profile. Although the company's management reported signs of stabilisation in some of its core markets in Q309, notably its emerging markets, such as China and India and certain residential markets such as the US, markets exposed to commercial construction continue to experience weakness in many regions. Fitch currently expects group sales to decline by about 15% for the full-year 2009, with a further small contraction in 2010, followed by modest growth in 2011. This reflects the agency's belief that GDP will return to modest growth levels in Legrand's key regions over the coming 12 months, albeit at an anaemic rate, and that an improvement in construction investment - and thus demand for Legrand's products - would likely lag any GDP growth.

Fitch expects Legrand's adjusted net leverage to increase to about 2.7-2.8x at FYE09, but to then recover to between 2.2x-2.6x during 2010-2011 as market conditions slowly improve. Consistent with the agency's approach of rating through the cycle, a deleveraging of this nature is in line with the current ratings, although downside pressure could build if deleveraging is slow to materialise. Other metrics also currently remain in line with Legrand's existing ratings, namely funds from operations (FFO) interest cover of 5.7x (compared with 5.9x at FY08) and cash from operations (CFO)/total adjusted debt of 37% (22.5%).

Legrand's ratings also reflect its solid business profile, characterised by its leading global market positions, geographical diversification, strong and innovative product portfolio, and peer-leading margins. Its ratings also benefit from a robust liquidity position, with a liquidity score (sources of liquidity to uses of liquidity over the next 12 months) of 3.8x as of Q309. The company's short-term debt of EUR378m is comfortably covered by EUR1,447m of cash, undrawn facilities and expected FCF.

However, on the negative side, Legrand's ratings are limited by ongoing concerns about possible shareholder-friendly actions, notably high dividend payments relative to peers, possibly reflecting Legrand's shareholder structure which is 61%-owned by private equity investors. This is underlined by the fact that, as of FY08, Legrand's dividend payout ratio was 52% compared to a peer average of 13%, and is forecast by Fitch to rise further to approximately 70% as of FY09.

Looking forward, positive rating pressure could occur if Legrand achieves a sustained improvement in its credit metrics (either actual or forecast), such as leverage to below 1.5x-2.0x, CFO-to-total adjusted debt (excluding one-off working capital inflows) to about 35% and/or FFO interest coverage to about 10x. Absent an improvement in these metrics, positive pressure could occur if Legrand's business profile improves, such as improved geographical diversification. Conversely, negative rating pressure could result from a sustained deterioration in credit metrics (either on an actual or forecast basis), such as leverage to above 2.8x, CFO-to-total adjusted debt to around 20%, and/or FFO interest coverage to around 5x. The ratings could also be negatively affected by a liquidity score below approximately 2x, sustained negative free cash flow, or increased shareholder friendly policies, such as large debt-funded M&A, increased dividends or share buybacks.

Legrand is a leading manufacturer specialising in the design, manufacture and distribution of products and systems for electrical installations and information networks, headquartered in Limoges, France. In FY08, Legrand generated sales of EUR4.2bn with lease-adjusted debt of EUR2.6bn.

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