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Research Update:

Barry Callebaut Lowered To 'BBB-' On Weaker-Than-Expected Credit Metrics On High Cocoa Price Volatility; Outlook Stable

November 18, 2024

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Rating Action Overview

- Barry Callebaut AG (BC), the world's largest chocolate producer and cocoa processor, finished fiscal 2024 with an S&P Global Ratings-adjusted debt-to-EBITDA of 5.7x and funds from operations (FFO) to debt of 10.6%, which is significantly weaker than our base-case projections.
- This deviation in credit metrics is due to BC's increased working capital needs and very strong increase in debt due to the unprecedented volatility in cocoa bean prices.
- Although the company is putting mitigating measures in place, we assume volatility in cocoa prices will remain throughout 2025 with free operating cash flow (FOCF) only being about neutral. As such, we don't expect credit metrics to improve until 2026-2027 with leverage to remain above 4.0x in 2025 before decreasing to 3x-4x in 2026-2027.
- We have therefore lowered our long-term ratings on BC and on the group's senior notes to 'BBB-' from 'BBB'.
- The stable outlook reflects our expectations that FOCF will recover in the next 12-24 months, with leverage stabilizing to 3.0x-4.0x over the forecast horizon assuming cocoa prices start to gradually decrease.

Rating Action Rationale

The rating action reflects an important deviation from our initial base case linked to cocoa bean market price volatility and BC's structurally long working capital cycle affecting cash flow generation. BC finished fiscal 2024 (year ended Aug. 31, 2024) with S&P Global Ratings-adjusted debt-to-EBITDA of around 5.7x, FFO to debt of around 10.6%, and negative FOCF of Swiss franc (CHF)2.5 billion (about €2.7 billion).

Although the company passed price increases directly for about 70% of its volume sold throughout 2024 (30% remaining under a price list), thanks to its cost-plus model and with revenue for fiscal 2024 increasing by more than 20% versus fiscal 2023, its EBITDA margins were below our expectations at around 7.7% (versus 10.9% the prior year), mainly reflecting some time-lag to negotiate and adjust prices, as well as higher-than-expected one-off costs linked to the cost optimization program.

We note the company's long structural working capital cycle (12-18-month timeline from bean contracting to receiving customer payments) affected its operating cash flows. In order for BC to hedge its exposure to cocoa bean price swings, the company simultaneously entered into future derivative contracts that required large initial margin call payments as well as variation margin call payments . Although these future derivatives did protect their profit and loss as inventory prices went up, it also affected operating cash flow substantially. In order to address these short-term liquidity needs that are driven by bean prices, BC had to raise enough cash over 2024. This is why the company increased debt by about CHF2.6 billion-CHF2.7 billion, bringing S&P Global Ratings-adjusted total net debt to CHF4.5 billion in 2024, from CHF1.9 billion in 2023.

Although cocoa bean market prices have since stabilized, cocoa crops for 2025 will be below historical levels with ongoing volatility in cocoa bean market prices over the next 12 months, thereby potentially challenging to the group's deleveraging prospects. We expect adjusted debt to EBITDA to remain above 4.0x in 2025 before reducing to around 3.0x-4.0x by 2026-2027, assuming a more gradual decrease in cocoa bean prices and recovery of solid positive FOCF. We forecast sales will increase by 10%-15% toward CHF11.3 billion-CHF11.8 billion in 2025 as the company manages to pass on ongoing high cocoa bean prices, offset by some volume stagnation with EBITDA margins of around 8.0%-9.0%, mainly on the back of additional one-off costs linked to the cost optimization program, together with some time-lag to fully pass on price increases. Assuming prices gradually recover toward the end of 2025, we forecast an improvement in our credit metrics over 2026-2027. Specifically, we forecast about 0%-1% of annual revenue growth on average on the back of a correction in pricing, offset by higher volume growth and with continued margin expansion toward 10%-11% in 2026-2027, assuming the company starts to successfully achieve cost synergies and material cost savings under its efficiency program. We also assume FOCF will continue being negative in 2025 before turning positive in 2026-2027. This is because we anticipate the company will continue securing its long-term exposure to inventory volatility and we expect important working capital outflows at least during the first half of the year together with liquidity swaps that will have an impact on operating cash flows in 2025.

We think the company remains well funded for the current level of cocoa prices for the next 12 months. We note the company has always had a diverse range of debt instruments that have allowed it to adequately fund its business needs, notably the large seasonal working capital needs. In fiscal 2024, the company built a liquidity position cushion to offset the large working capital outflows with the December 2023 issuance of a €262.5 million term loan as well as the issuance of Swiss bonds totaling CHF 1.330 billion. The company's liquidity buffer also grew thanks to the increase in its committed revolving credit facility to €1.312 billion (from €900 million) and the issuance of a euro senior bond of about €700 million. In total this year, BC has raised CHF2.0 billion in the bond markets with long-term maturity dates.

BC will remain focused on its planned cost-saving initiatives under its BC Next Level program as well as its high-value products that will allow the company to navigate this environment for now. Under its BC Next Level strategy, the company will remain concentrated on its immediate business needs and cost-cutting efforts that will help confront the extreme volatility of its main raw material, cocoa beans. As part of its strategy, BC will invest net CHF500 million in capital expenditure (capex) and operating expenditure (CHF171 million already invested in 2024), offset by capital benefits, in order to gain efficiencies, which we view positively. The key drivers around the cost efficiency plan will be to streamline factories and reduce SG&A, increasing cost-savings in production and overheads while also simplifying the supply chain structure. The company plans to achieve cost synergies of CHF250 million by the end of 2026.

We believe BC, as the industry leader in cocoa, retains very good sourcing capabilities (including in Latin America) and long-lasting relationships with partners as well as a solid position across its portfolio. The company caters to different price segments (from big food and beverage companies to private label) and different channels (from gourmet and specialties to more commoditized goods), which are also key. We understand that BC is focusing on contracting sufficient volumes for its business needs for the year ahead, deepening its outsourcing partnerships and increasing its Gourmet and specialties division over time. In our view, the company's ambition to continuously scale up and further expand its Gourmet and specialties division will boost margins. We view positively BC's capacity to capture new outsourcing chocolate contracts (planning to win two out of three outsourcing contracts) from a still-large captive market (60% of chocolate is still produced in-house) and increased penetration in emerging markets (especially in Asia).

Although the company will not cut dividends in 2025, we assume discretionary spending outside dividends will remain prudent, which supports deleveraging prospects in the next two years. Despite the current deviation in credit metrics, we consider that BC has kept a good track record of stable positive FOCF over recent years, averaging over CHF300 million annually under stable circumstances, a level that we expect BC will recover in 2026-2027. Besides the inherent large working capital swings, notably in its cocoa processing business, which we included in our forecasts, the business is actually moderately capex intensive (3.5%-4.0% of revenues on average) with a large share spent on enhancing manufacturing capabilities and quality investments in line the BC Next Level strategy (we factor in total capex of about CHF250 million in 2025 and around CHF300 million in 2026-2027).

That said, we assume BC will maintain its common dividend payment in absolute terms similar to 2024 (about CHF159 million) which is higher than the group's target payout ratio to shareholders (usually 35% to 40% of the net profit). We don't expect any share repurchases or extraordinary dividends. Regarding mergers and acquisitions (M&A), we don't believe BC will pursue large debt-funded acquisitions this year given its focus on the short-term operating challenges (no annual spending in 2024 and nothing forecast for 2025). We also expect the company to remain prudent on its bolt-on acquisition and discretionary spending once the situation improves, from 2026.

Outlook

The stable outlook on BC reflects our view that the group's operating performance should gradually recover over the next 12-24 months and FOCF turn positive again. We assume a gradual rebound of industrial demand for chocolate and cocoa from food and beverage companies, and we believe the large scale of operations, diverse customer base, raw materials pass-through capabilities, and cost efficiencies should enable the group to stabilize cash flows despite the current working capital inflation.

As such, we estimate BC will be able to maintain adjusted debt to EBITDA of 3x-4x on average over the next two years, with FFO to debt at 20%-25% during the same period. We also project the company will generate positive FOCF in fiscal 2026, assuming cocoa bean prices stabilize at a lower levels than currently.

Downside scenario

We could take a negative rating action if over the next two years we see adjusted debt to EBITDA rising above 4.0x with FFO to debt below 20% on a sustained basis.

This could stem from:

- Very high volatility in cocoa bean market prices for longer than expected such that the group needs to raise more debt in order to fund working capital needs and margin calls.
- Weaker-than-expected operating performance, possibly fueled by unforeseen supply chain disruptions, more intense competition in key markets, or weaker-than-expected growth prospects in chocolate manufacturing and the Gourmet and specialties business.
- Large debt-financed acquisition or material increase its shareholder remuneration.

Upside scenario

We would consider raising the rating if adjusted debt to EBITDA sustainably decreases to below 3.0x and FFO to debt rises to 30%-45%. This is contingent on a stabilization of cocoa bean prices and BC executing its growth plan and expanding its business while reducing commodity concentration, supporting strong profitable growth over the next two years. This would also imply the need to continue pursuing a consistent financial policy and M&A strategy.

Company Description

Headquartered in Switzerland, BC is the world's largest manufacturer of industrial chocolate, with about a 40% market share in volume terms, and the largest processor of cocoa beans with about 20% of market share. Its large production capacities, with full vertical integration from origination to manufacturing, and well-spread production footprint enable the company to achieve economies of scale and be close to end markets.

In fiscal 2024, the company generated revenue of CHF10.4 billion and adjusted EBITDA of CHF800 million.

BC operates in three main segments:

- Food manufacturers (56% of total sales): CHF5.8 billion of revenues generated from the sale of chocolate products to food producers.
- Global cocoa (27%): CHF2.9 billion of revenues generated from the sale of cocoa products to food producers. But it also generates CHF2.4 billion of revenues from internal transactions with other divisions for procuring key ingredients to produce chocolate.
- Gourmet (16%): CHF1.7 billion of revenues generated from the sale of chocolate products to artisans, chocolatiers, food chains, and distributors.

BC operates in Western Europe, Central and Eastern Europe, North America, Latin America, and AMEA (Asia, Middle East, Africa. Its cocoa processing activities, global cocoa, account for 16% of revenue. The group operates 62 factories selling products in over 147 countries.

BC is listed on the Zurich Stock Exchange, with about 64.9% of its shares in free float. Most of the shares are held by institutional investors but the largest shareholder by far remains family holding company Jacobs Holding, with 30.1% of the share capital and voting rights. Renata Jacobs of the Jacobs family also owns 5% separately.

Our Base-Case Scenario

Assumptions

- Revenue of CHF11.3 billion-CHF11.8 billion in 2025 and CHF11.5 billion-CHF 12.0 billion in 2026-2027. We believe sales volumes should remain flat throughout 2025 (we predict an increase of 0%-1%) with important price increases thanks to the cost-plus model. We expect volumes will pick up partially in fiscal 2026, supported by increased demand from emerging markets but offset by a readjustment of prices as we expect cocoa bean prices to normalize from 2026. As the company grows its gourmet section and value-added proposition, we expect growth to accelerate from 2026 with an increase in volumes as manufacturing outsourcing grows.
- S&P Global Ratings-adjusted EBITDA margins will continue being depressed in 2025 to around 8%-9% (S&P Global Ratings-adjusted) before recovering toward 10.0%-11.0% over 2026-2027. We assume some time-lag to pass on price increases (30% of volume is under a price list) and additional one-offs linked to the company's cost efficiency program. Offsetting these pressures, we expect certain efficiencies in input cost (labor, supply-chain, energy). We expect a greater contribution from high-margin and value-added segments like Gourmet that will slowly contribute to margin growth in the future.
- Negative FOCF of about CHF10 million in 2025 and positive CHF300 million-CHF500 million on average over 2026-2027, with negative working capital movements year on year, and capex of about 4.0% of revenue.
- Adjusted net debt of about CHF4.5 billion-CHF4.6 billion in 2025 and 2026. For 2025, we assume about CHF4.0 billion of reported net debt, CHF500 million of trade receivable securitizations, CHF327.5 million of lease liabilities, and CHF42 million of net pension deficit. We assume about CHF150 million-CHF170 million of annual cash dividends and do not factor in any acquisition spending over 2025-2026. In line with our criteria, we do not net from debt readily marketable inventories like cocoa beans because they are held for processing.

Key metrics

Barry Callebaut AG--Forecast summary

	--Period ending Aug. 31--				
(Bil. CHF)	**2023a**	**2024a**	**2025e**	**2026f**	**2027f**
Revenue	8.47	10.39	11.3-11.8	11.3-11.8	11.3-11.8
EBITDA	0.92	0.80	0.9-1.0	1.1-1.3	1.2-1.4
EBITDA margin (%)	10.9	7.7	8.0-9.0	10.0-11.0	10.0-11.0
Free operating cash flow (FOCF)	0.08	(2.45)	(0.03)-0	0.2-0.5	0.4-0.7
Adjusted ratios					
Debt/EBITDA (x)	2.1	5.7	4-5	3-4	3-4
FFO/debt (%)	36.5	10.6	12-17	20-25	20-25

Barry Callebaut AG--Forecast summary

	--Period ending Aug. 31--				
(Bil. CHF)	2023a	2024a	2025e	2026f	2027f
EBITDA interest coverage (x)	7.6	3.6	4-6	6-8	7-9

All figures are adjusted by S&P Global Ratings, unless stated as reported. a--Actual. e--Estimate. f--Forecast. CHF--Swiss franc.

Liquidity

We assess BC's liquidity as adequate under our criteria. We forecast that liquidity sources will exceed uses by 1.2x over the next 12 months. Even if EBITDA declined by 30%, we believe net sources would remain positive. We also value the strong banking relationships, diverse debt sources, and significant headroom under financial covenants.

Principal liquidity sources

- Cash and cash equivalent balances worth CHF978.4 million as on Aug. 31, 2024.
- Undrawn committed credit lines of CHF 1.3 billion for the next 12 months.
- Forecast cash FFO of approximately CHF 650 million-CHF700 million for the next 12 months.

Principal liquidity uses

- About CHF400 million-CHF500 million debt maturities within 12 months.
- Annual estimated maximum working capital needs of around CHF500 million.
- Estimated capex of about CHF230 million-CHF270 million in next 12 months.
- Dividend payments of around CHF159 million.
- No contracted share repurchases.

Environmental, Social, And Governance

Environmental, social, and governance factors are an overall neutral consideration in our credit rating analysis of BC. It is one of the most advanced agribusiness companies globally in terms of level of disclosure and proactively addressing environmental risks. Notably, since 2016 it has been implementing a comprehensive strategy to improve the sustainable sourcing of cocoa (as well as other raw materials) and preserve biodiversity.

We believe the progress of the sustainable sourcing and biodiversity program should help limit loss of business volumes for BC when its main customers and end consumers become increasingly sensitive to these issues in their purchasing decisions. BC's initiatives include the digital mapping--and thus improved traceability--of all the cocoa farms in its main origin regions of West Africa. In terms of social risks, the company is running a comprehensive program to reduce child labor in farming communities in Africa. BC also supports the professionalization of the cocoa farmers with the aim to improve their productivity and increase income.

Issue Ratings--Subordination Risk Analysis

Capital structure

BC issues most of its senior debt through Barry Callebaut Services N.V., its group financing vehicle. Most of the long-term debt instruments are senior unsecured and guaranteed by Barry Callebaut AG (BBB-/Stable/--).

Analytical conclusions

We rate the long-term senior unsecured debt 'BBB-', in line with our issuer credit rating on BC. This is because we assess limited structural subordination in the capital structure as total secured debt and debt held at the operating companies is below our 50% threshold.

Rating Component Scores

Rating Component Scores

Component	
Foreign currency issuer credit rating	BBB-/Stable/--
Local currency issuer credit rating	BBB-/Stable/--
Business risk	Satisfactory
Country risk	Low
Industry risk	Intermediate
Competitive position	Satisfactory
Financial risk	Significant
Cash flow/leverage	Significant
Anchor	bbb-
Diversification/portfolio effect	Neutral/Undiversified
Capital structure	Neutral
Financial policy	Neutral
Liquidity	Adequate
Management and governance	Neutral
Comparable rating analysis	Neutral
Stand-alone credit profile	bbb-

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

Industry Credit Outlook Update Europe: Consumer Products, July 18, 2024

Ratings List

Ratings list		
Downgraded		
	To	**From**
Barry Callebaut AG		
Barry Callebaut Services N.V.		
Issuer Credit Rating	BBB-/Stable/--	BBB/Stable/--
Senior Unsecured	BBB-	BBB