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"Belgian companies have plenty, except for a cash problem"

"In 2018, a few large international companies struggled with their balance sheet. But Belgian companies in 2019 will mainly struggle with an excess of cash"

Debt difficulties at company level came to light in the second half of 2018, fuelling the premise that the historically low level of interest rates and slowdown in growth are leading to debt-related problems. In the US, General Electric had to resort to an emergency sale of assets to keep itself afloat and in Belgium, the situation at Nyrstar, Greenyard and AB Inbev has captured the attention.

However, we believe that there will not be a debt problem in 2019. Instead, the problem is more to do with cash. The financial debts of the (industrial) companies tracked by KBC Securities will fall on average to 11% of the balance sheet total (13% in 2018).

They could plummet to 6% by 2020, unless cash is utilised for takeovers or channelled to shareholders. Indeed, cash heavy companies could even become takeover targets.

AB Inbev, Nyrstar, bpost …

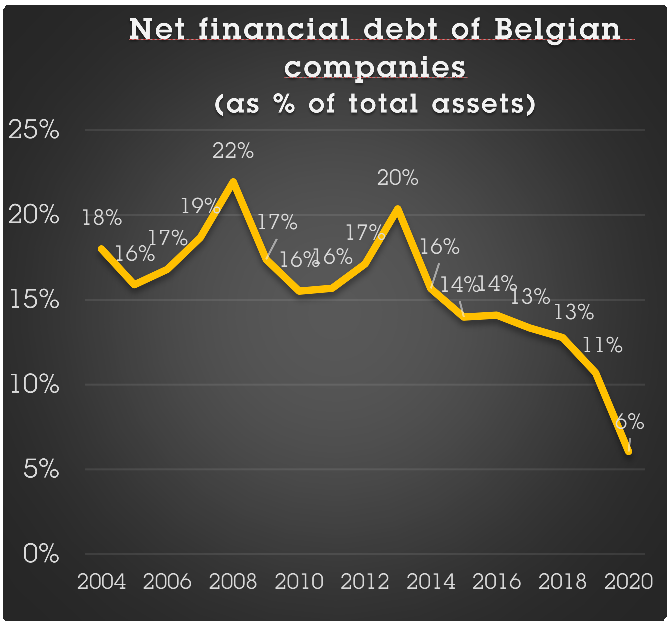
In Belgium, balance sheet problems were highlighted by the continuing decline in the share price of AB Inbev and bpost. In addition, the falling price of zinc turned Nyrstar's budget on its head and a very aggressive form of Listeria bacteria ate into Greenyard's share price and balance sheet.

AB Inbev reacted by slashing its annual dividend, a move that bpost CEO Van Gerven has ruled out. The royal dividend will continue to be paid by bpost, something that Nyrstar shareholders can only dream of at present. Greenyard took decisive action and sold off its potting soil unit, enabling it to face the future again with a healthy balance sheet.

Rising interest rates

KBC expects interest rates for all maturities to continue increasing in 2019 and beyond. This is – by definition – detrimental to companies with significant levels of debt, because the cost of refinancing will be higher than the original interest charge, or because the cost of variable-rate debt will follow the market trend.

In order to protect themselves against the whims of the interest rate market, a large majority of Belgian companies have decided to hedge themselves against rate rises through Interest Rate Swaps (IRS).



Even if short-term interest rates were to rise, there still wouldn't be a debt problem (although the value of these swaps would be reflected negatively on the income statement). The fact is that a climate of rising interest rates will convince analysts and investors to extrapolate this trend into the long term. Fortunately, the downward effect on value is offset by excessive earnings growth.

Well defended or highly vulnerable?

Despite a rise in interest rates, and the fact that companies are adequately protected against such a development, the big question remains to what extent balance sheets have not been eroded by acquisitions, inadequate cashflows or the over-friendly treatment of shareholders. We have examined all the Belgian companies monitored by KBC Securities, apart from financial institutions (banks and insurance companies), biotech firms and real estate players.

The top-three companies with the highest debt-to-total-assets ratio in 2018 are Telenet (98%), Fluxys Belgium (49%) and AB Inbev (45%), while Avantium (-59%), Picanol (-24%) and Roularta (-22%) are debt free and – relatively speaking – have the most cash of all the companies examined. These figures do not say anything about solvency, something that is reflected in the debt-to-cashflow ratio (net debt to EBITDA ratio) or the debt ratio in the context of covenants.

Conclusion

The figures show that Belgian industrial companies are overfinanced, even to the extent that the debt ratio is at its lowest level since the dotcom boom. Underlying, therefore, not enough is being invested, or not enough is being paid out, because more cash is being accumulated than invested. In principle, this is worrying, due to the fact that financial leverage and investments can be important engines of growth. A surplus of unused cash has an adverse effect on valuation.

We do not expect any fundamental change to this luxury problem, which is making Belgian listed companies vulnerable to acquisition in 2019. So, it comes as no surprise that companies such as EVS, Van de Velde, Agfa, Barco and Melexis are repeatedly tipped as takeover candidates.

Companies with significant levels of debt	Sector	2018	2019	2020
Telenet	Media	98%	95%	94%
Fluxys Belgium	Gas, Water & Multiutilities	49%	50%	
AB InBev	Beverages	45%	45%	44%
Elia Group	Electricity	39%	41%	43%
EXMAR	Industrial Transportation	37%	43%	37%
Euronav	Industrial Transportation	35%	27%	11%
Balta	General Retailers	33%	45%	39%
Nyrstar	Industrial Metals & Mining	32%	33%	31%
Kinepolis Group	Travel & Leisure	31%	25%	19%
Ter Beke	Food Producers	29%	26%	22%
Floridienne	Chemicals	28%	29%	28%
Sioen	General Industries	26%	15%	7%
Bekaert	General Industries	26%	25%	24%

Companies with little or no debt	Sector	2018	2019	2020
Avantium	Chemicals	-59%	-60%	-62%
Picanol	Industrial Engineering	-24%	-32%	-39%
Roularta	Media	-22%	-25%	-27%
Barco	Technology Hardware & Equipment	-22%	-24%	-27%
Smartphoto group	Consumer Goods	-20%	-29%	-36%
Jensen Group	Industrial Engineering	-17%	-19%	-21%
Van de Velde	Personal Goods	-14%	-17%	-27%
D'Ieteren	General Retailers	-13%	-10%	-8%
EVS	Media	-10%	-22%	-33%
Melexis	Technology Hardware & Equipment	-8%	-6%	-8%
Colruyt	Food & Drug Retailers	-2%	-1%	-3%
Agfa	General Industries	-1%	-2%	-5%
Resilux	General Industries	4%	-3%	-8%

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