Moody's Investors Service

Credit Opinion: Daimler AG

Global Credit Research - 01 Sep 2011

Stuttgart, Germany

Ratings

Category	Moody's Rating
Outlook	Positive
Issuer Rating -Dom Curr	A3
Senior Unsecured	A3
Commercial Paper -Dom Curr	P-2
Other Short Term -Dom Curr	(P)P-2
Daimler Finance North America LLC	
Outlook	Positive
Sr Unsec Bank Credit Facility	A3
Senior Unsecured	A3
Bkd Commercial Paper	P-2
Bkd Other Short Term	P-2
Daimler Canada Finance Inc.	
Outlook	Positive
Bkd Senior Unsecured -Dom Curr	A3
Commercial Paper -Dom Curr	P-2
Daimler Japan Ltd.	
Outlook	Positive
Bkd Sr Unsec MTN	(P)A3
Bkd Other Short Term	(P)P-2
Mercedes-Benz Australia/Pacific	
Outlook	Positive
Bkd Senior Unsecured	A3

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Key Indicators

Daimler AG[1]

	06/30/2011(L)	12/31/2010	12/31/2009	12/31/2008	12/31/2007	12/31/2006
Debt / EBITDA	0.9x	1.1x	9.3x	2.5x	1.3x	1.1x
Debt / Book Capital	23.4%	30.3%	52.1%	46.3%	34.6%	35.7%
(Cash & marketable securities) / Debt	109.4%	116.7%	73.3%	31.9%	105.1%	54.3%
EBITA / Margin	7.8%	6.9%	-1.5%	4.5%	7.9%	4.5%
EBITA / Avg Assets	9.3%	8.5%	-1.5%	5.5%	8.2%	4.1%
FCF / Debt	5.4%	50.8%	18.7%	-42.3%	-9.3%	-13.7%
RCF / Debt	76.7%	83.7%	4.8%	3.6%	42.4%	55.6%
RCF / Net Debt	-819.9%	-501.2%	18.2%	5.2%	-833.0%	121.6%
EBIT / Interest Expense	12.8x	8.5x	-1.5x	5.1x	11.7x	8.0x

[1] Standard adjustments in accordance with "Rating Methodology: Moody's Approach to Global Standard Adjustments in the Analysis of Financial Statements for Non-Financial Corporations, December 21, 2010". In addition, Moody's adjusts for one time items. Source: Moody's Financial Metrics

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Corporate Profile

Headquartered in Stuttgart, Germany, Daimler AG ("Daimler" or "the company"; rated A3/P-2/positive outlook) develops, manufactures, distributes and sells a wide range of automotive products, mainly passenger cars, trucks, vans and buses. It also provides financial and other services to its automotive businesses. Daimler's key activities are divided into the following segments: i) Mercedes-Benz Cars ("MBC"); ii) Daimler Trucks; iii) Mercedes-Benz Vans iv) Daimler Buses; and v) Daimler Financial Services. In fiscal year 2010 the group generated revenues of EUR97.8 billion.

Rating Rationale

On August 30, 2011 Moody's affirmed the A3 long-term and Prime-2 short-term ratings of Daimler and its rated subsidiaries and changed the outlook to positive from stable.

The outlook change to positive reflects Daimler's stronger and faster than anticipated recovery in operating performance and financial metrics to a level that positions them very strongly in the current rating category. Should Daimler be able to sustain its current operating performance and financial metrics despite rising challenges and risks from a slowing economic growth in many of Daimler's key car and truck markets we could upgrade the ratings within the next 12-18 months.

Daimler's A3 rating is supported by (i) the company's highly valued Mercedes brand in premium passenger cars; (ii) its well diversified truck business positioning as the global market leader with leading market positions in Europe, North America, South America and Japan as well as the division's growth potential in emerging markets, particularly in Russia together with its local joint venture partner Kamaz; as well as (iii) Daimler's strong market positions in Busses and in the European Van business and (iv) a strong rebound of Daimler's operating performance in 2010 resulting in a substantial reduction of overall indebtedness and leverage measured as debt/ EBITDA.

The rating also takes into consideration (i) the challenge to comply with various emission legislations in most markets in particular the CO2 emission target set by the European Union by 2015 for Mercedes-Benz passenger cars as well as (ii) the costs coming along with the applied technologies and the potential impact on the mix of Daimler's product line, both effects could materially impact future profitability and cash generation on a sustainable basis, (iii) the expectation of moderate free cash flow generation given a higher capex and an increasing dividend which was exceptionally low in 2010.

DETAILED RATING CONSIDERATIONS

Mercedes-Benz cars gains ground in Europe and keeps benefitting from Emerging Markets

The premium car manufacturer brand Mercedes which in the last year contributed around 64% to Daimler's reported EBIT was able to stabilise its market share in its Western European markets in 2010, up 20 basis points to 5.1% from 4.9% in 2009, as Daimler was able catch up against the mass market car manufacturers which benefitted from scrapping bonuses in 2009 which were running out in most European countries in 2010. Looking beyond Europe we see that most of the improvement in sales volumes in 2010 was generated in North America and China. Even though we see ongoing volume growth in these markets we caution that the pace of growth in markets such as China is slowing down given rising interest rates and a lower anticipated growth of the overall economy. At the same time we take comfort that demand is supported by the introduction of new models such as the B-class coming on stream in 2011.

Substantial recovery in unit sales of Truck division

Daimler Trucks which contributed around 18% to Daimler's reported EBIT showed a strong rebound in 2010 on the back of a positive overall economic environment and the introduction of new engines which are already used in the new Actros coming on stream in 2011. All main markets positively contributed to the growth in unit sales by 37% in 2010; Brazil, Eastern Europe and Turkey have been particularly strong. Even though we believe that the high growth rate in 2010 was partly due to a low base in 2009 we expect further growth in Daimler's key markets North America, South America and Europe in the current year. The rating also incorporates Daimler's market leading position in the Western European heavy duty and medium duty truck market with a market share of 24.3% in 2010.

We are closely monitoring the price development of used trucks and the discounts offered on new trucks, as we believe any deterioration in pricing could directly impact earnings and cash flows of the truck manufacturer and therefore offset any improvements in the cost structure of the manufacturer. At the same time we expect Daimler to act prudent and we do not foresee a price decline in 2011.

Market leading position of Mercedes-Benz Vans in Europe; Buses benefit from chassis business

Mercedes-Benz Vans benefits from the positive economic recovery in Western Europe, North America and China. In Europe the Van business is market leading with a market share of around 18% before Volkswagen. The Daimler Bus business is supported by the chassis business in Emerging Markets whilst the business for complete buses is still negative.

Material improvements in credit metrics in 2010 could be extended into the first half 2011

In the first six months 2011 Daimler increased its total unit sales of light vehicles, trucks, vans and buses by 10% compared to H1 2010 leading to a 10% increase also in consolidated group revenues to EUR51 billion. Reported Group EBIT was up 40% in the first six months period 2011 versus the same period last year to EUR4.6 billion. The company reported a free cash flow of EUR613 million negatively impacted by EUR1.2 billion cash absorption for working capital needs.

Given the strong recovery of operating performance and leverage metrics from very weak levels achieved in 2009 and 2008 Daimler's is currently strongly positioned in the A3 rating category. Per LTM June 2011 Daimler had an adjusted operating margin of 7.2% (-2.6% in 2009) and leverage of 0.9x debt/ EBITDA (9.3x in 2009). At the same time we note a high degree of volatility in Daimler's operating performance through the crisis and hence caution the sustainability of the current performance.

Increasing headwinds from macroeconomic environment, input costs and foreign exchange effects

Key challenges for Daimler's operating performance are a declining pace of the economic growth in countries like China, rising raw material prices and stricter CO2 emission targets set by the European Union. We expect the new emission regulations to lead to higher expenditures for research and development and an adverse effect on the product mix towards smaller cars with smaller engines.

We view these headwinds as a key challenge for Mercedes-Benz Cars in achieving its EBIT margin targets of 10% from 2013 onwards on a sustainable basis. At the same time these effects could be mitigated by Daimler's modular product development strategy which Daimler expects to lower variable production costs by 11% by 2015. Moreover, on a group level, a substantial recovery in unit sales of Daimler's Truck and Van divisions in the key markets North America, South America and Europe should help to maintain a strong operating performance.

Liquidity Profile

Taking into account the payment of EUR2.0 billion into the German pension fund in H2/2011 -- a generally positive action - Daimler's liquidity is not fully sufficient to cover the next 12 months needs in a theoretical scenario of no access to debt markets for its manufacturing and finance services activities. The company has access to total cash sources of EUR 30.0 billion including EUR9.8 billion cash on balance sheet, EUR0.9 billion short-term marketable debt securities after 20% haircut, EUR1.6 billion from equity stake in EADS after 40% haircut from current market value as well as EUR7.0 billion syndicated credit facility which is fully undrawn. In addition we expect a sizable cash flow generation FFO from the operating business over the next 12 months. In Moody's liquidity scenario Daimler would require total funds of more than EUR30 billion over the next 12 months including capex, debt maturities, working cash for day-to-day operations, the planned EUR2.0 billion payment into the German pension fund as well as dividend payments. Moody's would expect Daimler to improve its liquidity profile over the short term to have a full 12 to 15 months coverage of its future needs with future sources again as in the past.

Rating Outlook

The positive outlook reflects Daimler's recent improvements in financial metrics to a level that position the company very strongly in the A3 rating category.

What Could Change the Rating - Up

An upgrade would require that the company evidences its ability to moderate the volatility of its operating performance as well as continue to deliver very solid results in times of cyclical peaks. Within the next 12 to 18 months and against an environment of increasing macro-economic risk, the company would have to defend its current solid credit profile with minimum metrics as follows: (i) an EBITA margin above 7%, (ii) a sustainable Free Cash Flow generation in the industrial business around 10 % of Debt and (iii) an interest cover above 8x. The company would need to pursue a balanced approach between shareholders' and bondholders' interests and preserve the financial services' conservative policies and profitability. Furthermore an upgrade would require an improved liquidity profile with cash sources covering more comfortably the next 12-15 months cash needs in Moody's stress case scenario on a rolling forward basis.

What Could Change the Rating - Down

Downward pressure would arise in case of (i) evidence that the market environment would become significantly more challenging than anticipated in terms of volumes or prices (ii) material deterioration in the recent improvements in profitability and financial metrics exemplified by Debt/EBITDA ratio above 2.5x and interest coverage ratio below 5x (all ratios as adjusted by Moody's). as well as in case of (iii) a sizeable cash absorption or (iv) a persistent weakening in Daimler's liquidity profile.

Rating Drivers

The application of Moody's Rating Methodology for the Global Automobile Manufacturer Industry (published on June 30, 2011), which identifies key areas of focus for assessing relative credit quality maps to a grid outcome of A2, one notch above Daimler's current A3 rating with a positive outlook. The grid outcome is a point-in-time snapshot based on metrics for the twelve months ending on 30/06/2011 and hence it does not take into account the cyclicality of the industry.

Rating Factors

Daimler AG [1]

Global Automobile Manufacturer Industry	Aaa	Aa	A	Baa	Ba	B	Caa
Factor 1: Market Position and Trend (35%)							
a) Trend in Global Unit Share over Three Years				x			
b) Product Breadth and Strength			x				
Factor 2: Leverage and Liquidity (20%)							
a) Debt / EBITDA		0.9x					
b) Debt / Capital		23.4%					
c) (Cash + Mkt Sec) / Total Debt			109.4%				
Factor 3: Profitability and Returns (15%)							
a) EBITA Margin				7.8%			
b) NPATBUI / Sales				4.8%			
c) EBITA / Average Assets			9.3%				
Factor 4: Cash Flow and Debt Service (30%)							
a) RCF / Debt		76.7%					
b) FCF / Debt					5.4%		
c) EBITA / Interest Expense		13.1%					
Rating:							
a) Indicated Rating from Grid			A2				
b) Actual Rating Assigned			A3				

[1] Market Share trend based on the period 2008-2010

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