MOODY'S
INVESTORS SERVICE

Rating Action: Moody's downgrades Ericsson's ratings to Baa2; ratings on review for further downgrade

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London, 14 October 2016 -- Moody's Investors Service ("Moody's") has today downgraded to Baa2 from Baa1 the senior unsecured debt ratings and to (P)Baa2 from (P)Baa1 the MTN program rating of Telefonaktiebolaget LM Ericsson ("Ericsson"). At the same time, the agency has placed the company's Baa2/(P)Baa2 ratings on review for further downgrade. Moody's expects to conclude the review within a maximum timeframe of three months.

"The ratings downgrade to Baa2 reflects the continuation and acceleration of Ericsson's sales and earnings decline, evident in the company's preliminary Q3 2016 results, which we expect will persist into 2017, leading to credit metrics that are no longer commensurate with the previous Baa1 rating" says Alejandro Núñez, a Moody's Vice President -- Senior Analyst and lead analyst for Ericsson.

"The ratings remain on review for further downgrade. The review process will focus on (1) the extent of and possible mitigants to Ericsson's negative free cash flow generation over the next twelve to eighteen months; (2) the assessment of how the company's financial policies (including its dividend policy) may evolve as Ericsson adjusts to a reduced sales environment; (3) clarity on Ericsson's management structure and any potential changes in operating strategy; and (4) the management of its liquidity position in light of the expected cash burn," adds Mr. Núñez.

RATINGS RATIONALE

The ratings downgrade and the review for downgrade principally reflect the continued decline in Ericsson's operating performance and markets outlook as announced by the company in its preliminary Q3 2016 results release.

Ericsson reported a year-over-year revenue decline of 14% (of which Networks comprised a 19% yoy decline on a reported basis), a drop in its gross margin to 28% from 34% yoy and quarterly operating income of only SEK300 million (compared with SEK5.1 billion in Q3 2015). The underlying drivers of the revenue and earnings declines included continued macroeconomic weakness in key emerging markets such as Brazil, Russia and the Middle East as well as reduced Networks coverage and capacity sales in Europe as multi-year mobile broadband projects such as Vodafone's Project Spring were completed.

In addition, Ericsson's management now forecast a continuation of these weak operating trends over the next two to three quarters. The announcements made at the company's preliminary Q3 results indicate that revenue growth and operating income for the year ending 31 December 2016 will be markedly lower compared with management's and Moody's previous expectations. Moody's notes that Ericsson's ratings were already weakly positioned at the Baa1 level prior to today's rating actions.

Following the company's Q3 preliminary results, Moody's now anticipates sustained revenue decline for Ericsson in FY16 (contrasted with +8% reported growth in FY15), with material operating margin compression and negative free cash flow generation for a second consecutive year.

Nevertheless, Moody's continues to view the company's position as a global leading telecoms equipment vendor and its good liquidity position as supportive credit factors although the rating agency notes that its declining operating cash flow and restructuring charges are likely to continue to erode Ericsson's cash pile over the coming year.

The company has embarked on a cost efficiencies program, which aims to save a net SEK9 billion of costs compared to FY14. In addition, it has increased its operating expense savings target to reach an opex base of SEK 53 billion by H2 2017. Although Ericsson may be in a position to achieve a material portion of these savings by year-end 2017, the targeted savings measures, including headcount reductions, will take time to effect.

The Baa2 rating reflects: (1) the company's weaker revenue and earnings growth outlook for FY16 and FY17, particularly in the Networks division, which continues to be impacted by softening end market demand and intense competition; (2) the lack of sufficient offsetting growth or earnings contribution from the Global Services division; balanced against (3) Moody's expectations that most, if not all, of the company's cost savings initiatives are delivered by year-end 2017; (4) a maintenance of the company's good liquidity position; and, (5) financial policies within the limits of the company's free cash flow generation and liquidity resources.

WHAT COULD CHANGE THE RATING UP/DOWN

Prior to the downgrade to Baa2 and the review process, Moody's had indicated that Ericsson's ratings could be downgraded if: (1) the group were to continue exhibiting a sustained erosion in the company's market positions; (2) operating margins remained in single-digit territory; (3) leverage were sustained above 1.75x; or (4) RCF/gross debt (Moody's-adjusted) remained below 20%.

The review process will focus on (1) the extent of and possible mitigants to Ericsson's negative free cash flow generation over the next twelve to eighteen months; (2) the assessment of how the company's financial policies (including its dividend policy) may evolve as Ericsson adjusts to a reduced sales environment; (3) clarity on Ericsson's management structure and any potential changes in operating strategy; and (4) the management of its liquidity position in light of the expected cash burn.

LIST OF AFFECTED RATINGS

Downgrades:

..Issuer: Telefonaktiebolaget LM Ericsson

....Senior Unsecured Medium-Term Note Program, Downgraded to (P)Baa2 from (P)Baa1; Placed Under Review for further Downgrade

....Senior Unsecured Regular Bond/Debenture, Downgraded to Baa2 from Baa1; Placed Under Review for further Downgrade

Outlook Actions:

..Issuer: Telefonaktiebolaget LM Ericsson

....Outlook, Changed To Rating Under Review From Stable

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Diversified Technology Rating Methodology published in December 2015. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

With revenues of SEK246.9 billion in FY2015, Telefonaktiebolaget LM Ericsson ("Ericsson") is a world-leading provider of telecommunications equipment and related services to mobile and fixed network operators globally. Its equipment is used by over 1,000 networks in more than 180 countries and around 40% of the global mobile traffic passes through its systems. Networks represented 50%, Support Solutions 6% and Global Services 44% of group revenues in FY2015. The company's largest shareholders are Investor AB (Aa3 stable) and AB Industrivärden (unrated), with voting rights of 21.5% and 15.2%, respectively.

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