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Research Update:

Controladora Mabe 'BB+' Ratings Affirmed; Outlook Remains Positive

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Research Update:

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Overview

- We still consider that Mabe is on track to bring its leverage ratio below 3.0x before the end of the year. However, up to now the company's deleveraging has been slower than what we originally expected and hasn't yet hit the required leverage threshold to reach the investment-grade rating.
- We're affirming our 'BB+' corporate credit and issue-level ratings on Mabe. The recovery rating of '3' remains unchanged.
- The positive outlook continues to reflect our view that Mabe will maintain its financial discipline and commitment to improve leverage metrics through debt repayments, which would reduce its adjusted debt to about \$775 million within the next five months. An upgrade would follow the completion of Mabe's debt reduction plan that results in a debt-to-EBITDA ratio below 3.0x by the end of 2017.

Rating Action

On July 31, 2017, S&P Global Ratings affirmed its 'BB+' corporate credit and issue-level ratings on Controladora Mabe S.A. de C.V. (Mabe). The outlook remains positive. Our recovery rating of '3', indicating our expectation of a meaningful (50% to 70%; the upper half of the range) recovery for bondholders in a payment default scenario, remains unchanged.

Rationale

We revised the outlook on Mabe to positive from stable in September 2015, reflecting our view that the company could improve its key credit metrics through stronger cash flow generation to gradually reduce debt. Since then, we have expected the company's debt to EBITDA ratio to trend below 3.0x. Mabe's credit metrics have actually improved over the past couple of years, but Latin America's sluggish economy and the company's capital investments for growth have delayed its deleveraging. In our opinion, Mabe's credit metrics are not quite yet at a level that we deem in line with the investment-grade rating, but we still consider that the company has a credible debt reduction plan that would bring its debt to EBITDA below 3.0x before the end of the year. In particular, we expect a more rigorous working capital management to increase inventory turnover and accelerate the collection of receivables, which would boost cash flow generation for debt repayment in excess of \$100 million.

Mabe's business risk profile continues to reflect a strong position in most of

the markets where it operates, as well as its geographic diversification throughout the Americas, with a broad portfolio of brands. We're also incorporating the relationship that Mabe has with its new shareholder Haier (not rated) and our expectation that the company will continue to manufacture and sell finished home appliances under the GE brand in the U.S. Our assessment captures the intense competition from international and regional players, the company's vulnerability to global economic downturns as part of a cyclical industry, and its exposure to foreign currency and raw material cost fluctuations. The latter is partly mitigated through a natural hedge because the company generates more than 40% of its revenue in dollars. We expect Mabe to continue posting EBITDA margins of about 10%, above the consumer durables industry's average, reflecting the company's operating efficiencies, the consolidation of operations, and less volatile raw material prices. Additional synergies and economies of scale from Mabe's relationship with Haier could also strengthen the company's cost structure.

Mabe's current key credit metrics are still in line with our significant financial risk profile assessment, particularly with debt to EBITDA slightly above 3.0x for the 12 months ended March 31, 2017. However, we consider that management's efforts to increase cash flow generation and its commitment repay debt would strengthen the company's financial risk profile to intermediate by the end of 2017.

Our base-case scenario includes the following assumptions:

- Our baseline GDP growth forecast for Latin America in 2017 is at 1.0%. We have reduced our real GDP growth forecasts for Chile, Colombia, Uruguay, and Peru. However, in Mexico, where Mabe generates about 25% of its revenue, private consumption has remained solid, growing 3.1% during the first quarter of 2017. We expect this trend to continue in the next 18 months, which should support Mabe's volume sales.
- Resilient spending in the U.S. continues to support Mabe's volume sales in North America. We expect real GDP growth in the U.S. of 2.2% this year, and in the 2.0%-2.5% range through the end of the decade. Although personal income growth remains sluggish--and consumers reduced their savings to increase spending in the first quarter of 2017--household purchasing power got a lift from increases in full-time hiring, and this has extended into the second quarter. North American sales would continue to represent almost half of Mabe's total revenue.
- Mid-single digit revenue growth in 2017, reflecting a still positive performance in Mexico and the U.S. supported by the company's market position. Performance in Mexico would be supported by the incremental contribution from the sale of A/C units. Also, starting in 2018, top-line growth in North America would benefit from the completion of capacity expansion projects.
- Adjusted EBITDA trending above \$300 million in two years.
- Capital expenditures close to \$150 million in the next two years, mainly reflecting the investments in new projects and maintenance activities.
- Enhanced working capital management to increase inventory turnover and accelerate collection of receivables that will boost cash flow generation for debt repayment in excess of \$100 million.

- Reported debt close to \$724 million in 2017 and \$676 million in 2018, given debt repayments and scheduled amortizations in the next two years.
- Free operating cash flow (FOCF) generation close to \$140 million in 2017 and \$209 million in 2018.
- A dividend of \$20 million starting in 2017, as the company begins to make payments once its leverage ratio drops below 3.0x. In our view, these payments won't significantly affect discretionary cash flow (DCF).

Based on these assumptions, we arrive at the following credit measures for 2016 and 2017:

- EBITDA margins of around 10.0%;
- Debt to EBITDA of 2.7x and 2.1x, respectively; and
- FOCF to debt of about 24.2%.

Liquidity

We assess Mabe's liquidity as adequate because we expect sources to exceed uses by more than 1.2x during the next 12 months, and that this ratio will remain above 1.0x even if EBITDA falls by 15%. Our liquidity analysis also incorporates our view that the company has the capacity to withstand high-impact, low-probability events, its sound relationship with banks, good standing in the international debt markets, and an overall prudent financial risk management.

Principal Liquidity Sources:

- Cash of \$46 million as of March 31, 2017; and
- FFO of about \$287.8 million for the next 12 months.

Principal Liquidity Uses:

- Debt maturities of \$74.2 million as of March 31, 2017;
- Working capital needs of about \$9.4 million for the next 12 months, including intra-year requirements;
- Capex of about \$148.9 million for the next 12 months; and
- Dividend payments of \$20 million.

Mabe's credit agreements include financial covenants requiring EBITDA net interest coverage of 2.5x and net debt to EBITDA of maximum 3.5x. We believe the cushion for these covenants is ample and could withstand a drop in EBITDA of more than 25%.

Outlook

The positive outlook continues to reflect our view that Mabe will maintain its financial discipline and commitment to improve leverage metrics through debt repayments, which would bring adjusted debt to about \$775 million within the next five months. An upgrade would follow the completion of Mabe's debt reduction plan by the end of 2017, coupled with our expectation that the company will consistently maintain its debt-to-EBITDA ratio below 3.0x.

Downside scenario

We would revise the outlook to stable before the end of the year if Mabe is unable to complete its debt repayment plan and improve its credit metrics in line with our expectations, with a debt-to-EBITDA ratio staying above 3.0x and FOCF to debt below 15%. Such a scenario would likely relate to lower-than-expected cash flow generation due to slow inventory turnover and delays in the collection of receivables, or if Mabe accelerates its capital investment plan that leads to either incremental funding needs or lower debt payments.

Ratings Score Snapshot

Corporate Credit Rating: BB+/Positive/--

Business Risk: Satisfactory

- Country Risk: Intermediate
- Industry Risk: Intermediate
- Competitive Position: Satisfactory

Financial Risk: Significant

- Cash Flow/Leverage: Significant

Anchor: bb+

Modifiers

- Diversification/Portfolio effect: Neutral
- Capital structure: Neutral
- Financial policy: Neutral
- Liquidity: Adequate
- Management and Governance: Fair
- Comparable rating analysis: Neutral

Recovery Analysis

Key analytical factors

The issue-level rating on Mabe's senior unsecured bonds due 2019 is 'BB+'. We're keeping the recovery rating at '3', indicating our expectation of a meaningful (50% to 70%; the upper half of the range) recovery under a hypothetical default scenario, unchanged. The '3' recovery rating doesn't have an impact on Mabe's issue-level rating. We consider that an EBITDA decline of 55% from the 2016 figures would likely lead to a payment default. Such EBITDA decline would follow a deterioration in the company's margins and cash flow generation, potentially as a result of higher raw material prices and lower volume sales due to weaker economic conditions in Mexico and other Latin American markets where the company operates.

Our recovery analysis assumes that, in a hypothetical default scenario, the \$481 million senior unsecured notes due 2019 would rank equally with all of

Mabe's and its subsidiary guarantors' existing and future senior unsecured indebtedness.

We have valued the company on a going-concern basis, using a 5.0x multiple applied to our projected emergence-level EBITDA, and estimate a gross emergence value of about \$526 million.

Simulated Default Assumptions

- Simulated year of default: 2019
- EBITDA at emergence: \$105.2 million
- Implied EV multiple: 5.0x
- Estimated gross EV at emergence: about \$526 million

Simplified Waterfall

- Net EV after 5% administrative costs: \$499.5 million
- Priority claims: --
- Total Unsecured claims: \$755.7 million
- Recovery expectation: 50%-70%

Note: All debt amounts include six months of prepetition interest, which correspond to the coupon that should be paid at default.

Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Corporates - General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Consumer Durables Industry, Dec. 12, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Ratings List

Ratings Affirmed

Controladora Mabe, S.A. de C.V.

Corporate Credit Rating	BB+/Positive/--
Senior Unsecured	BB+
Recovery Rating	3(65%)

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.

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