FitchRatings

20 Oct 2020 | Affirmation

Fitch Affirms Mabe's IDRs at 'BBB-'; Outlook Revised to Positive

Fitch Ratings-Chicago-20 October 2020: LEAD PARAGRAPH

Fitch Ratings has affirmed Controladora Mabe S.A. de C.V.'s (Mabe) Long-Term Foreign and Local Currency Issuer Default Ratings (IDRs) at 'BBB-'. In addition, Mabe's senior unsecured debt was affirmed at 'BBB-'. The Rating Outlook was revised to Positive from Stable.

The revision of the Outlook to Positive reflects Fitch's expectation that Mabe's capital structure should strengthen over the next two years, due to increasing EBITDA resulting from rising exports to the U.S. and Canada, higher profitability in South America, as well as organic launches of new product lines. EBITDA expansion combined with projected FCF of USD50 million annually, would allow Mabe's net debt/EBITDA to reach around 1x in 2022 compared with 1.8x in 2019.

Fitch's base case suggests that positive FCF over the next two years, if used to reduce debt, would lead to a decline in the debt/EBITDA ratio to below 2x by 2022, from 2.7x in 2019. Mabe's appliance sales are forecast to exceed 12,000 units in 2022 from 11,400 in 2019, mainly due to rising exports to the U.S. and Canada. Higher exports combined with more stable profitability in South America resulting from efficiencies and EBITDA contribution from new products, would lead EBITDA to increase to about USD350 million from USD290 million in 2019.

The materialization of EBITDA growth and debt repayment expectations combined with decreasing uncertainty surrounding the containment of the coronavirus in North America and its effects on employment and consumption could lead to an upgrade of the ratings. Conversely, the Outlook could be revised to Stable should expected trends in EBITDA and debt reduction fail to materialize, leading to leverage expectations above 1.5x on a net basis and 2.0x on a gross basis.

Mabe's ratings reflect its low-cost structure, geographic diversification and strong business position throughout most of the Americas. A broad product portfolio and sourcing synergies from Mabe's relationship with Haier Smart Home Co., Ltd. also support the ratings and complements the company's solid market position, resulting from strong brand recognition of the Mabe and General Electric Company brands. Mabe's ratings are tempered by a highly competitive environment and exposure to commodity price and foreign exchange volatility.

Key Rating Drivers

Coronavirus Crisis Manageable: Mabe's balance sheet was strong at the start of the pandemic, and the company had sufficient leverage headroom to withstand the downturn. In addition, improved cash generation, due to efficiencies from consolidated manufacturing in fewer sites of larger scale in the last few years, had positioned it well. Significant reductions in the prices of various raw materials including steel, aluminium, plastics and resins boosted profitability. Fitch expects input cost declines will counter weaker sales in 2020.

Mexico's main appliance distribution channels, including large home improvement stores, wholesale clubs, supermarkets, as well as some department stores, remained open during the pandemic, which allowed Mabe to continue to distribute and sell products despite weak economic conditions. During this period, various plant shutdowns in the U.S., including those of Mabe's competitors, contributed to increased demand for Mabe's exports, partially compensating for volume weakness.

Lockdowns most severely restricted the markets in Peru, Ecuador and several in Central America including, Panama, El Salvador and Honduras. These markets combined with Colombia and Argentina represented approximately 15% of Mabe's total consolidated sales in 2019. This figure had previously come down by more than 20% in 2017, as markets contracted due to weak demand and steep currency depreciation.

Exports Remain Strong: Mabe's operating EBITDA increased to USD290 million in 2019 from USD270 million in 2018 largely due to higher exports to the U.S. Fitch forecasts EBITDA to climb solidly above USD300 million over the next two years due to increased demand for all categories of Mabe's exports into this market, as well as organic expansion of new product lines. In addition, increased exports to Canada and efficiencies resulting from a scale up in Mabe's Colombian plant, should also contribute to an increase in EBITDA.

Leverage Expected to Trend Down: Mabe's Net debt/EBITDA leverage ratio is projected to decline to 1.3x in 2021, and around 1x in 2022, compared to 1.8x in 2019. The decline in leverage will be driven by higher EBITDA generation of around USD350 million in 2022 and yearly FCF on average of about USD50 million, which would be used for debt reduction. Mabe paid down approximately USD50 million of debt during 2019 and raised USD190 million of short-term debt in 1Q20 to boost its cash balance during the pandemic. The company paid down USD50 million in 2Q20 and had available cash of USD290 million.

More Certain Trade Framework: Mabe is an important manufacturer and exporter with major exposure to North America. The company manufactures a significant quantity of GE-branded products through its joint venture with Haier. The trade agreement signed between the U.S., Canada and Mexico has reduced the trade uncertainty among the countries. The agreement improves the visibility of Mabe's exports into the U.S., which combined with exports to the Canadian market, represent approximately 55% of Mabe's consolidated revenues. The agreement provides a 16-year lifespan and did not entail substantial changes to the rules for appliances industry, when compared to the NAFTA agreement.

Strong Market Position: Mabe holds a strong business position in most of Latin America. The company has seven manufacturing facilities throughout Mexico, Ecuador, Colombia and Argentina, which allows it to compete in the region. Mabe focuses on offering a wide product portfolio under a multi-brand strategy that targets all socioeconomic levels. The company also has long-term contracts to manufacture and export appliances under the GE brand, and holds exclusive rights to distribute Haier and GE products in Latin America and Canada.

Appliance-Focused Shareholder: Haier is a large international appliance manufacturer. It has owned the GE appliances business, including a 48% stake in Mabe, since 2016. Mabe and Haier have expanded their product portfolios and implemented synergies since Haier acquired its stake in Mabe. The relationship has resulted in new manufacturing contracts and a broader product line for Mabe that includes split-system air conditioners and front-load washers.

Derivation Summary

Mabe's major competitors in the region are Whirlpool Corp. (BBB/Negative) and Asian manufacturers such as LG Electronics Inc. (BBB-/Stable), Daewoo Electronics and Samsung Electronics Co., Ltd. (AA-/Stable), as well as local producers. Mabe's solid business position is supported by its low-cost structure, proprietary brands, the strength of GE's appliances brand and Haier's technical capability and brand recognition. Mabe's relatively smaller scale and lower geographic diversification against higher-rated peers such as Whirlpool is mitigated by its strong brand recognition. Sourcing and technical capabilities that result from being partly owned by Haier, a large appliance manufacturer, are also positive factors. Mabe has higher leverage than Whirlpool and LG Electronics, and its profitability is comparable to Whirlpool's but higher than that of LG Electronics.

Mabe has a more volatile cash flow profile when compared with a subset of Mexican corporates such as Grupo Bimbo, S.A.B. de C.V. (BBB/Stable) and Sigma Alimentos, S.A. de C.V. (BBB/Stable), which are focused on more stable consumer staples. Mabe's products are more discretionary in nature. However, over the long term, demand is stable and expected to grow due to the favorable demographics and growth profiles of Mabe's key markets. Fitch expects Bimbo and Sigma to maintain net leverage below 3.0x, compared with expectations of 1.5x or below for Mabe.

Key Assumptions

Revenues grow by low-single digits in 2020 and grow by mid-high single digits in 2021 and 2022;

Operating EBITDA margins above 9% in 2021 and 2022;

Debt/EBITDA leverage declines over the medium term;

The company does not undertake meaningful shareholder distributions;

Positive FCF over the rating horizon.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--A track record of maintaining a stronger capital structure, with net debt /EBITDA at or below 1.5x and gross debt to EBITDA below 2.0x, combined with larger operating scale.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Deterioration in profitability and cash flow from lower demand or competitive or input cost pressures;

--Expectations of net leverage above 2.5x or gross leverage above 3.0x;

--A weakening in Mabe's relationship with Haier;

--Large debt financed acquisitions.

Best/Worst Case Rating Scenario

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

Liquidity and Debt Structure

Sound Liquidity: Mabe should generate slightly more than USD200 million of normalized CFFO over the intermediate term, which combined with capex expectations of around USD120 million to USD150 million and dividends of around USD25 million results in expectations of FCF of around USD30 million to USD50 million. The company has good access to bank debt and capital markets, demonstrated by public and private notes issuances over the last two years as well as by frequent access to bank debt at attractive terms.

The company raised USD190 million of short-term debt to bring its available cash to USD290 million in 1Q20 during the pandemic. The company paid back USD40 million in 20Q20 and expects to pay the remaining USD150 million before year-end. Total financial debt was USD890 million as of June 30, 2020 and cash USD290 million. Mabe's debt consists mainly of USD370 million of notes due 2028, USD175 million of private notes due 2026 and bank debt. Supporting Mabe's liquidity, is the continued demand for the company's products and strong name recognition of the GE and Mabe brands

Fitch includes non-recourse factoring of accounts receivable of approximately USD50 million in its debt calculations. The factoring adjustment allows Fitch to compare issuers that may use different sources of funding, as immediate replacement funding is required if the receivables financing shuts down or eligible receivables decline in quality and the facility ceases to fund ongoing receivables.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

Controladora Mabe S.A. de C.V. (Mabe); Long Term Issuer Default Rating; Affirmed; BBB-; Rating Outlook Positive
; Local Currency Long Term Issuer Default Rating; Affirmed; BBB-; Rating Outlook Positive
----senior unsecured; Long Term Rating; Affirmed; BBB-

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Additional information is available on www.fitchratings.com

Applicable Criteria
Corporate Rating Criteria (pub. 01 May 2020) (including rating assumption sensitivity)

Applicable Model

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v7.9.0 (1)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form

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