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Research Update:

Controladora Mabe Outlook Revised To Positive From Stable, 'BB+' Ratings Affirmed

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Table Of Contents

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Overview

- Mexico-based home appliance company, Mabe, continues improving its cash flow generation and key credit metrics despite still challenging market dynamics and currency volatility in most Latin American countries.
- We are revising our outlook on the company to positive from stable. At the same time, we are affirming our 'BB+' corporate credit and debt ratings on Mabe.
- The positive outlook reflects our view that Mabe will continue improving its operating performance despite a more challenging economy in most markets it operates, supported by a favorable environment of raw materials globally and the company's operating efficiencies which could maintain its debt to EBITDA below 3.0x and lead its free operating cash flow (FOCF) to debt above 15% on a consistent basis.

Rating Action

On Sept. 18, 2015, Standard & Poor's Ratings Services revised its outlook on Controladora Mabe, S.A. de C.V. (Mabe) to positive from stable. At the same time, we affirmed our 'BB+' corporate and issue-level ratings on the company.

Rationale

The outlook revision reflects Mabe's enhanced operating performance that has strengthened its cash flow generation and liquidity, leading to debt to EBITDA slightly below 3.0x on a quarterly basis as of June 30, 2015. We believe Mabe will continue to improve its operating performance during the second half of 2015, considering its large presence in Mexico and the U.S., as well as the favorable environment of raw materials globally. The company operates in the U.S. through its joint venture with General Electric Co. (GE; AA+/Stable/A-1+); these two markets are the main revenue drivers for the company because we expect they will continue generating about 60% of total sales. On the other hand, despite the Mexican peso's recent depreciation that has led to a currency mismatch between debt and sales for some Mexican companies, we believe Mabe is less vulnerable given that about 50% of its revenues are dollar-denominated from the sales in the U.S. and exports. Moreover, we expect the company will continue to sell its non-core assets, and we expect Mabe will use these proceeds to pay down debt. Therefore, we could revise our financial risk profile on Mabe to "intermediate" from "significant" in the next 12 months and raise the ratings.

Mabe's business risk profile reflects the company's strong market position in most of the countries where it operates and its geographic diversification throughout the Americas with a broad portfolio of brands, which it customizes to meet local demand preferences. Through the joint venture with GE, which holds a 48.41% equity interest in Mabe, the latter manufactures and sells finished home appliances to GE for sale in the U.S. In addition, the company obtains certain benefits from accessing GE's supplier base and purchasing and licensing of certain GE trademarks, designs, and production procedures. In 2014, GE announced that it reached an agreement with AB Electrolux (Electrolux; BBB/Stable/A-2) for the sale of its appliance division including its equity interest in Mabe. This transaction could be completed during the second half of 2015, although it's still subject to the approval of the corresponding authorities. If this transaction materializes, we don't foresee a significant impact on Mabe's business plan, strategy, and its financial policy in the near term. Our assessment also incorporates our view of the intense competition from international and regional industry players, Mabe's vulnerability to global economic downturns as part of a cyclical industry, and its exposure to foreign currency and raw material cost volatilities, which is partially mitigated by Mabe's natural hedge. We expect the company will continue posting EBITDA margins near 10% in the next 12 months, which are above the the consumer durables industry's average, according to our criteria for the consumer durables industry.

Mabe's financial risk profile reflects our expectations that despite the company's improved cash flow generation, its adjusted FOCF to debt will continue to be below 15% by the end of 2015. However, we believe that if the company continues posting a favorable cash flow generation, this ratio, along with our expectation of a debt to EBITDA below 3x, could improve further in the following months and lead to a revision of the company's financial risk profile to "intermediate" from "significant."

Our base-case scenario includes the following assumptions:

- Latin America's GDP growth of 0.4% in 2015 and 1.9% in 2016. We forecast a recession in Venezuela, and our growth forecasts for Latin America are lower than we previously expected. However, we still have favorable perspective for economic growth in Mexico and the U.S., which correspond to about 55% of the company's total sales. We expect GDP in both countries to grow 2.5% and 2.3%, respectively, in 2015 and 3.0% and 2.7% in 2016. For South America (about 20% of total sales), we expect GDP in Chile and Colombia to grow 2.7% and 3.0%, respectively, in 2015 and 3.0% and 3.5% in 2016.
- The U.S., Mexico and South America to continue to be the main revenue drivers for Mabe, representing about 80% of total sales
- Almost flat revenue growth in 2015 and a low-single-digit revenue growth in 2016 despite the likely slower economic growth in Latin America and the foreign exchange volatility, supported by Mabe's more resilience due to its natural hedge, as well as its solid market position.
- Adjusted EBITDA of $290 million - $300 million in 2015, reflecting relatively stable commodity prices, the operating efficiencies related to the Saltillo facility and the implementation of SAP technology in all of the company's operations.
- Capital expenditures of about $90 million in the next two years, which correspond to about 3% of total revenues (versus 1.9% in 2014), mainly reflecting the investments in new projects and the conclusion of the SAP technology implementation.
- No dividend payments because we expect the company will continue to focus on investing in new projects, strengthen its liquidity and deleverage.

Based on these assumptions, we arrive at the following credit measures for 2015 and 2016:

- EBITDA margins between 10.2% and 10.5%;
- Debt to EBITDA below 3x; and
- FOCF to debt below 15%.

Liquidity

We assess Mabe's liquidity as "adequate" because we expect sources will 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%. The company has a comfortable debt maturity profile, and we expect it will continue seeking to improve this profile through payment of its debt with cash flow generation and/or asset sales and/or refinancing. 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 $56 million as of June 30, 2015 (excluding the cash held in Venezuela); and
- FFO and other sources of cash of about $240 million.

Principal Liquidity Uses:

- Debt maturities of $96 million as of June 30, 2015;
- Working capital needs of about $43 million for the next 12 months; and
- Capex of about $88 million for the next 12 months.

We also expect Mabe will maintain an adequate cushion for its financial covenants and withstand a drop in EBITDA of more than 25% in the next 12 months.

Outlook

The positive outlook reflects our expectation that Mabe will continue improving its operating performance in its most important markets, supported by a favorable global environment of raw materials along with the company's improved operating efficiencies, maintaining its solid market position and "adequate" liquidity; this, despite the lower economic growth we expect in Latin America and the U.S. in 2015 compared to our previous expectations. We also expect the company will continue seeking to improve its capital structure in the next 12 months, that will further improve its key credit metrics . We believe that if Mabe continues bolstering its cash flow generation with a FOCF to debt above 15% along with a debt to EBITDA below 3x on a consistent basis, we could revise its financial risk profile to "intermediate."

Downside Scenario

We could revise the outlook to stable from positive if the company's operating performance is below our expectations and its cash flow generation doesn't improve with FOCF to debt below 15%. A downgrade is possible if Mabe's operating results, profitability, liquidity and cash flow generation deteriorate, reflecting weaker-than-expected global economic conditions or higher competition that results in lower demand for the company's products, or if raw material prices increase significantly. A negative rating action could also occur if the company's debt rises due to a more aggressive financial policy of Mabe. This would result in adjusted debt to EBITDA greater than 4.0x and FOCF to debt below 10% consistently.

Upside Scenario

Ratings Score Snapshot

	To	From
Corporate Credit Rating	BB+/Positive	BB+/Stable
Business Risk	Satisfactory	Satisfactory
Country Risk	Intermediate	Intermediate
Industry Risk	Intermediate	Intermediate
Competitive Position	Satisfactory	Satisfactory
Financial Risk	Significant	Significant
Cash Flow/Leverage	Significant	Significant
Anchor	bb+	bb+
Modifiers		
Diversification/Portfolio effect	Neutral/Undiversified	Neutral/Undiversified
Capital structure	Neutral	Neutral
Financial policy	Neutral	Neutral
Liquidity	Adequate	Adequate
Management and Governance	Fair	Fair
Comparable rating analysis	Neutral	Neutral

Recovery Analysis

Key Analytical Factors

The issue-level rating on Mabe's senior unsecured bonds due 2015 and 2019 is 'BB+'. The recovery rating is '4H', indicating our expectation of an average (30% to 50%) recovery, in the upper half of the range, for bondholders in a payment default scenario. For the company to default, EBITDA would need to decline significantly (56%) from 2014 results. This would cause a steep decline in the company's margins and cash flow generation, as a result of a significant reduction in profitability amid higher raw material prices and a weakening of the Mexican and other Latin American economies in which the company operates.

Our recovery analysis assumes that, in a hypothetical default scenario, the $200 million (outstanding $69 million) and $481 million senior unsecured notes due 2015 and 2019, respectively, 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 4.3x multiple applied to our projected emergence-level EBITDA, and estimate a gross emergence value of about $464 million.

Simulated Default Assumptions

- Simulated year of default: 2019
- EBITDA at emergence: $107.8 million
- Implied EV multiple: 4.3x
- Estimated gross EV at emergence: about $464 million

Simplified Waterfall

- Net EV after 3% administrative costs: $449.8 million
- Priority claims: --
- Total Unsecured claims: $706.8 million
- Recovery expectation: 30%-50%*

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

*In the upper half of the range

Related Criteria And Research

Related Criteria

- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Consumer Durables Industry - December 12, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- General Criteria: Group Rating Methodology - November 19, 2013
- Criteria - Corporates - General: Corporate Methodology - November 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13, 2012
- Criteria - Corporates - Recovery: Criteria Guidelines For Recovery Ratings On Global Industrials Issuers' Speculative-Grade Debt - August 10, 2009

- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue - April 15, 2008

Ratings List

	Ratings	
	To	From
Controladora Mabe, S.A. de C.V.		
Corporate credit rating		
Foreign and Local Currency	BB+/Positive/--	BB+/Stable/--
Senior Unsecured		
Foreign Currency	BB+	BB+
Recovery Rating	4H	4H

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 Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.