

Research Update:

Becle S.A.B. de C.V. 'BBB-' Ratings Affirmed On Easing Liquidity Pressure; Outlook Remains Negative On Higher Leverage

December 6, 2023

Rating Action Overview

- Mexico-based and global leading tequila producer Becle S.A.B. de C.V. recently signed a five-year senior unsecured syndicated loan for up to \$535 million to prepay \$500 million of existing short-term debt. In our view, the transaction eases Becle's liquidity pressure and improves its average debt maturity profile.
- However, we expect Becle's adjusted leverage (measured as adjusted debt to EBITDA) to remain slightly above 3x at year-end 2023, before gradually improving toward 2.5x by the end of 2024 and 2025, thanks to several operating tailwinds.
- On Dec. 6, 2023, S&P Global Ratings affirmed its 'BBB-' global scale long-term issuer credit and issue-level ratings on Becle.
- The outlook remains negative, indicating a one-in-three chance of a downgrade in the next 12-24 months if Becle's main credit metrics don't return to our expected levels for the current ratings, including adjusted debt to EBITDA well below 3.0x and funds from operations (FFO) to debt close to 30%.

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Rating Action Rationale

Becle has eased its liquidity strain and improved its average debt maturity profile. The company recently announced it signed a dual-tranche senior unsecured syndicated loan for up to \$535 million, consisting of a \$385 million term loan and a \$150 million revolving credit facility, both with five-year bullet maturities. The company will use the proceeds to prepay \$500 million in short-term debt, easing near term liquidity pressure and improving its debt average maturity profile to 5.5 years, from 4.2 years previously. The transaction will also enable Becle to access a \$35 million undrawn committed revolving credit facility, giving the company some financial flexibility.

Over the next six to 12 months, we will also continue to monitor Becle's liability management plan

in relation to its outstanding \$150 million senior unsecured notes due May 2025.

We now expect Becele's adjusted leverage to remain slightly above 3x at year-end 2023, still posing downside risks to the ratings if it does not return well below 3x over the next two years.

Considering the company's operating performance through the first nine months of 2023 and recent spike in leverage, we have revised our year-end adjusted leverage expectation to slightly above 3.0x, versus 2.1x previously expected. In our view, this still poses downside risks to the ratings if external factors continue affecting margins and cash flows beyond our current estimates, or if the company implements a more aggressive financial policy.

We still believe that several operating tailwinds should support a gradual reduction in Becele's adjusted debt to EBITDA toward 2.0x-2.5x over the next two years.

We continue to expect Becele's EBITDA margins to rise by year-end 2024 and 2025, supported by several operating tailwinds. These tailwinds include substantially lower agave prices (around MXN10-MXN20/kilogram), easing inflationary pressures on other input costs (such as glass prices and distribution costs), and the company's lower inventory stock needs due to global supply chain normalization. We also expect these measures to lower working capital needs.

Moreover, our updated base-case scenario considers a stronger U.S. dollar versus the Mexican peso in 2024 and 2025, than the levels seen in 2023, which should boost the company's earnings and cash flows. Based on the above and the company's strategy to optimize its capital structure, we now believe that Becele's adjusted leverage should revert to 2.0x-2.5x in the next two years.

Becele's leading position globally in the tequila market supports its credit profile. In recent years, the company has strengthened its competitive position in the spirits and alcoholic beverage industry. It's the largest player in the global tequila market and continues to expand its tequila category through its different brands, specifically in the super premium category, which in recent years has had high demand and continues to gain traction and popularity among consumers.

The company diversified its beverage product portfolio mix in other categories such as whiskeys, spirits, and ready-to-drink beverages, strengthening its position in the global alcoholic industry--it has strong brands in various regions and high-growth categories. Additionally, it benefits from a strong distribution network and a well-diversified customer base. It's also the third-largest producer of Irish whiskey worldwide and the second-largest in the U.S.

We think the company's strategic positions in the tequila and whiskey categories allow it to take advantage of the rising trend of premium spirits. However, those strengths are somewhat counterbalanced by its smaller scale of operation than other global rated peers in the industry, such as Diageo PLC (A-/Stable/A-2) and Pernod Ricard S.A. (BBB+/Stable/A-2), and its high sales exposure in the tequila category, which represented about 70% of its sales in the 12 months ended September 2023.

Outlook

The negative outlook reflects our view that Becele's adjusted leverage will remain above our expected trigger for the current rating level at year-end 2023--which assumes leverage well below 3.0x on average--owing to the stronger-than-expected Mexican peso, challenging market conditions in Mexico for the spirit category, and economic slowdown in several key markets. Specifically, we now expect Becele's adjusted leverage to be slightly above 3.0x and its FFO to debt well below 30% at year-end 2023.

Downside scenario

We could lower our ratings on Beclé if its adjusted debt to EBITDA and FFO to debt don't return to well below 3.0x and closer to 30%, respectively, over the next 12-24 months. This could occur if:

- Beclé's operating performance continues to underperform, amid difficult global economic conditions, persistent input cost inflation, higher-than-expected agave prices, and if we see the stronger Mexican peso for a prolonged period; or
- Beclé implements an aggressive financial policy to fund unexpected working capital needs, capital expenditure (capex), mergers and acquisitions, dividend payments, or share repurchases.

Upside scenario

We could revise the outlook to stable in the next 12-24 months if Beclé consistently improves its credit metrics, such that its adjusted debt to EBITDA and FFO to debt are well below 3.0x and closer to 30%, respectively. We would also look for the company's sources of liquidity to exceed uses by more than 1.2x, at all times.

Company Description

Founded in 1758 and headquartered in Mexico City, Beclé has been led by 11 generations of the Beckmann family. Beclé is the world's largest producer of tequila, with well-known brands such as Jose Cuervo, 1800, Centenario, and Maestro Doblé. It is also the first and second-largest distributor of premium spirits and liquors in Mexico in terms of volume and value, respectively.

The company has more than 30 brands and produces, bottles, and sells spirits worldwide, with a presence in more than 85 countries.

In the past few years, the company has mainly grown through successful brand acquisitions, such as Three Olives, Hangar 1, Stranahan's, Bushmills, Boodles, Pendleton, and its recent investment in Proper No. Twelve whiskey.

Our Base-Case Scenario

Assumptions

- Mexico's GDP to grow 3.0% and U.S. GDP 2.3% in 2023. For 2024, we expect GDP to grow 1.7% and 1.3%, respectively.
- Consumer price index (CPI) to reach 5.6% in Mexico and 4.1% in the U.S. for 2023. In 2024, we expect 4.2% and 2.4%, respectively.
- Average exchange rate of Mexican peso (MXN) 17.84 per \$1 in 2023, and MXN18.75 per \$1 in 2024.
- Revenue in Mexican peso near -2.0% to 0% in 2023, versus 2022, and growth of about 7.5% in 2024. For 2024, we expect steady volume growth in the low single digits (about 1.5%), an ongoing shift toward premium spirits (referred to as the company's premiumization strategy),

and higher prices as high U.S. and Mexican inflation persists.

- EBITDA margin of about 16% in 2023 that gradually recovers to around 18.5% (or more) for 2024 on. We expect lower input costs, specifically for agave and glass prices, and distribution costs. Moreover, we expect Becele's product premiumization strategy, pricing initiatives, and strict cost control to somewhat offset inflationary pressures on some input costs.
- Capex of about MXN3.1 billion in 2023 and about MXN2.3 billion in 2024--mostly for innovation, product development, and to reinforce Becele's premiumization strategy. The company's capex plan also relates to the construction of its "1800 tequila distillery" project, which we expect it to finish during 2024. The company's minimum maintenance capex is about MXN1.0 billion.
- Dividend payments of MXN1.8 billion paid in August 2023, and about 30% of Becele's previous-year net income for 2024 on. Nonetheless, we believe the company has the flexibility to reduce dividend payments to protect its liquidity, if necessary.
- Share buyback activity that will depend on cash flow and market conditions.
- No large acquisitions over the projected horizon.
- About MXN25.3 billion in gross debt by the end of 2023 and no further increase in debt during the projected period. Around MXN8.9 billion (\$500 million) of incremental debt was disbursed this year mainly to fund the company's working capital needs to support its premiumization strategy. The company recently has refinanced the debt to a longer tenor.

Key metrics

Becele S.A.B. de C.V.--Key metrics*

	--Fiscal year ended Dec. 31--			
	2021a	2022a	2023e	2024f
Revenue growth (%)	12.5	16.0	(2.0)	7.5
EBITDA margin (%)	20.0	21.4	16.0	18.5
Debt to EBITDA (x)	1.1	1.6	3.1	2.5
Funds from operations (FFO) to debt (%)	56.4	37.7	19.1	28.0
Discretionary cash flow (DCF) to debt (%)	(25.9)	(46.4)	(26.3)	4.4

*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast.

Liquidity

We assess Becele's liquidity as adequate because we now expect its sources to exceed its uses of liquidity by more than 1.2x in the next 12 months, and this ratio to remain above 1.0x even if EBITDA declines by 15%. This mainly reflects the company's recent refinancing of short-term debt. Our liquidity analysis also incorporates qualitative factors, including our view that Becele maintains well-established and solid relationships with local and international banks through uncommitted and committed credit facilities.

Principal liquidity sources

- Cash and cash equivalents of MXN4.0 billion as of Sept. 30, 2023;
- Undrawn committed revolving facility of about MXN648 million (\$35 million);
- FFO of about MXN5.5 billion for the next 12 months; and
- Proceeds of about MXN9.3 billion (\$500 million) through the new senior unsecured syndicated loan recently signed.

Principal liquidity uses

- Short-term debt maturities of MXN9.0 billion (around \$514.1 million) as of Sept. 30, 2023;
- Working capital outflows of about MXN2.7 billion for the next 12 months;
- Maintenance and expansionary capex of around MXN2.5 billion for the next 12 months; and
- Dividend payments of about MXN1.2 billion for the next 12 months.

Covenants

As of Sept. 30, 2023, Becele didn't have any financial maintenance covenants. However, under the new long-term credit agreement of up to \$535 million (dual-tranche senior unsecured loan facility agreement) signed Nov. 30, 2023, the company will have to comply with two financial maintenance covenants:

- Net debt to EBITDA (excluding leases); and
- Minimum EBITDA interest coverage.

We expect Becele to maintain sufficient headroom under both covenants over the next two years.

Environmental, Social, And Governance

ESG factors have had no material influence on our credit rating analysis of Becele.

Issue Ratings--Subordination Risk Analysis

Capital structure

On a pro forma basis considering the new syndicated loan signed to refinance existing short-term debt for \$500 million, Becele's capital structure as of Sept. 30, 2023, consists of:

- \$150 million of outstanding senior unsecured notes due May 2025;
- \$800 million of senior unsecured notes due October 2031; and
- \$500 million senior unsecured loans due 2028.

Beclé issued and borrowed all of its debt instruments on a senior unsecured basis, and the 2025 senior notes benefit from guarantees from some of Beclé's subsidiaries that generated a limited portion of its consolidated revenue in 2022. Therefore, the 2025 senior notes have first priority over the other debt instruments outstanding only with respect to the cash flow from the subsidiaries that provided the guarantees. All the other outstanding debt instruments rank pari passu in right of order and payments vis-à-vis each other's.

Analytical conclusions

Based on Beclé's existing debt structure, and that there are no priority debt obligations that rank ahead of the company's senior unsecured debt obligations, we rate the senior unsecured notes 'BBB-', the same level as the issuer credit rating.

Ratings Score Snapshot

Issuer Credit Rating	BBB-/Negative/--
Business risk:	Fair
Country risk	Intermediate Risk
Industry risk	Low Risk
Competitive position	Fair
Financial risk:	Intermediate
Cash flow/leverage	Intermediate
Anchor	bb+
Modifiers:	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Satisfactory (no impact)
Comparable rating analysis	Positive (+1 notch)
Stand-alone credit profile:	bbb-

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014

- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Becele S.A.B. de C.V. Downgraded To 'BBB-' From 'BBB' On Increased Leverage And Tighter Liquidity; Outlook Negative, Sept. 6, 2023
- Becele S.A.B. de C.V., Sept. 9, 2022

Ratings List

Ratings Affirmed

Becele S.A.B. de C.V.

Issuer Credit Rating BBB-/Negative/--

Becele S.A.B. de C.V.

Senior Unsecured BBB-

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