

Research Update:

Simpar S.A. Outlook Revised To Stable From Positive On Persistently High Leverage; Ratings Affirmed

September 18, 2024

Rating Action Overview

- We expect Simpar S.A. will likely continue to face a high interest burden in the next two years considering its high debt and elevated interest rates. We now forecast EBIT interest coverage of 1.3x and funds from operations (FFO) to debt around 10% by the end of 2024, versus 1.8x and 15% previously.
- We expect the group to increase its cash flow in the coming years given its efforts to improve efficiency with higher utilization rates, new long-term contracts, and mostly organic growth.
- On Sept. 18, 2024, S&P Global Ratings revised the outlook on Simpar S.A. to stable from positive and affirmed the global and national scale ratings on Simpar at 'BB-' and 'brAA+', respectively. We also affirmed the issue-level ratings on the company's senior unsecured debentures and senior notes, with a recovery rating of '4' (35%).
- The stable outlook indicates our view that Simpar will remain focused on efficiency measures to balance continued high interest rates. We forecast FFO to debt of 10%-15% and EBIT interest coverage of 1.2x-1.5x in the next two years.

PRIMARY CREDIT ANALYST

Fabiana Gobbi
Sao Paulo
+ 55 11 3039 9733
fabiana.gobbi
@spglobal.com

SECONDARY CONTACTS

Luciano D Gremone
Buenos Aires
+ 54 114-891-2143
luciano.gremone
@spglobal.com

Luisa Vilhena
Sao Paulo
+ 55 11 3039 9727
luisa.vilhena
@spglobal.com

Rating Action Rationale

We believe high interest rates on the company's significant debt will continue to pressure

credit metrics. Moreover, Simpar faces continued elevated depreciation rates. The group ended June 2024 with consolidated gross debt of Brazilian real (R\$) 49.6 billion, of which R\$6.7 billion was debt at the holding company.

Our forecasts for Simpar's EBIT interest coverage of 1.2x-1.5x and FFO to debt of 12%-15% in 2024-2025 are commensurate with its current 'BB-' rating. In addition, we expect the group's measures to manage its liabilities, combined with higher cash flow in the next few years (mostly from internal growth), will help to control leverage.

For example, the group's rental car subsidiary Movida Participacoes S.A. (BB-/Stable/--) issued debt in the domestic market at an average interest rate of 2.3% over the Brazilian interbank deposit rate (CDI) to prepay debt at CDI + 2.8%.

We expect long-term contracts and a focus on efficiency measures to boost the company's

growth. We expect Movida to continue working on improving utilization rates while modestly expanding its fleet to approximately 230,000 – 255,000 vehicles 2024-2026. We expect the company will allocate 60% of this fleet to long-term contracts and use the rest as shorter-term rental cars.

We therefore expect Movida to maintain an average operational utilization rate of 85%-90% coupled with average rental price adjustments--supporting an EBIT margin consistently above 20%, versus almost 16% in 2023 due to impairments.

At the group's truck rental subsidiary, Vamos Locacao de Caminhoes, Maquinas e Equipamentos S.A. (BB-/Stable/--), we expect continued efforts to sign new contracts to expand the company's backlog while it manages inventory at dealerships. We forecast a net revenue increase of approximately 30% in 2024, mostly from truck rentals sufficiently balancing the weak dealerships (the ones with exposure to agribusiness). We expect Vamos' EBIT margin will be comfortably around 40% in the next few years.

We expect logistics services provider JSL S.A. (BB-/Stable/--) will post an EBITDA margin near 20%, with the consolidation of assets it acquired in the past 18 months, management to remain focused on efficiencies, and net revenue expansion from its solid existing backlog. We also expect JSL to continue signing contracts with new clients or cross-selling. The company added R\$2.3 billion in new contracts to its backlog in the first half of 2024, with an average term of 57 months, which provides important cash flow predictability.

Finally, we believe the group's car dealership subsidiary Automob will continue expanding through strategic acquisitions.

We expect continued heavy capital expenditure (capex) to be more directed to fleet renewal

and meeting new contracts than mergers and acquisitions. We assume net capex of about R\$8.5 billion–R\$10.5 billion in 2024–2026, mostly directed to Movida and Vamos.

For Movida, we forecast net capex of about R\$2.6 billion this year for fleet renewal and modest fleet expansion, but in 2025 and 2026 we forecast higher capex mostly for expected new long-term contracts. We anticipate Vamos' net capex will be around R\$4.5 billion this year and R\$3 billion–R\$3.5 billion in 2025–2026 to meet growing market demand. Our forecasts for the main subsidiaries indicate that they will continue financing capex with internal cash flow and new debt.

Outlook

The stable outlook reflects our view that the group will remain focused on efficiency measures to balance continued high interest and depreciation rates. We don't envision large mergers or acquisitions in the next few years, so we expect the company to grow mostly organically. We forecast FFO to debt of 10%-15% and EBIT interest coverage of 1.2x-1.5x in the next two years.

Downside scenario

We could lower the ratings in the next 12-18 months if the group's cash flow remains pressured amid higher interest rates or weaker market conditions for its largest subsidiaries, or if Simpar adopts a more aggressive growth strategy that it funds with debt or shareholder returns. In this scenario, we would see EBIT interest coverage below 1.3x and FFO to debt below 12% on a sustained basis.

Upside scenario

We don't expect to raise the ratings on Simpar in the next 12-18 months due to the high interest rates pressuring Simpar's credit metrics. To raise the ratings, we would need to see the company maintain an EBIT margin above 20% and much lower leverage. We would expect it to reach and maintain EBIT interest coverage of at least 1.7x and FFO to debt approaching 20%.

Company Description

Simpar is a privately owned entity headquartered in Sao Paulo. The group was founded in 1956 and provides transportation and logistics services in Brazil and other countries through its subsidiaries: JSL, Movida, Vamos, CS Brasil Participacoes e Locacoes Ltda., Automob, BBC Bank, CS Infra, and Ciclus Ambiental.

We expect the group to post consolidated revenue of about R\$40.2 billion and EBITDA of close to R\$10.6 billion in 2024, with the following EBITDA breakdown: Movida (42%), Vamos (33%), JSL (22%), and other subsidiaries (3%).

- Movida is the second-largest car rental company in Brazil, offering rental cars, fleet management services, and sales of used vehicles. The subsidiary ended June 2024 with a total fleet of 246,364 vehicles (44% rental cars and 56% for long-term contracts) and 347 stores (89 for used car sales).
- Vamos is a Brazilian truck, machinery, and equipment rental company, operating 72 new truck and equipment dealerships and 16 used truck and equipment dealerships across the country. It had a total fleet of 50,384 assets (39,790 trucks and 10,594 units of equipment) as of June 30, 2024.
- JSL is the main provider of logistics services and freight transportation in Brazil. Its portfolio consists of asset-light (53% of 2023 revenue) and asset-heavy (47%) contracts.
- Automob is one of the largest authorized car dealerships in Brazil, operating 120 stores and 28 brands across 23 cities.
- BBC Bank mainly offers leasing, freight payments, and financial services to customers and suppliers.
- CS Brasil provides fleet management and outsourcing services to the public sector, as well as public passenger transport.
- CS Infra operates public concessions of ports, toll roads, and urban mobility infrastructure.
- Ciclus Ambiental, formed by Ciclus Rio and Ciclus Amazônia, operates in the waste and sanitation management and recycling sector.

Our Base-Case Scenario

Assumptions

- GDP growth in Brazil of about 2% in 2024-2026
- Average inflation in Brazil of about 4.2% in 2024, 3.8% in 2025, and 3.5% in 2026, affecting

labor-related costs and fleet maintenance prices

- Average base interest rates of 10.25% in 2024, 9.13% in 2025, and 9% in 2026, influencing funding costs and rates of new fleet management contracts
- Consolidated net revenue expansion mostly from the higher average prices and modest fleet expansion at Movida, with Vamos and JSL signing long-term contracts and expanding their fleets.
- Simpar consolidated EBIT margin of about 20% in the next few years, as Movida increases its occupancy rate, Vamos' dealerships represent less of its total revenue, JSL absorb synergies from past acquisitions, and cost inflation passes through across all subsidiaries
- Lower working capital needs in 2024, reflecting lower inventory at Vamos
- Cash payments related to past acquisitions totaling about R\$270 million in 2024, R\$115 million in 2025, and R\$181 million in 2026
- No dividends from Simpar this year, and dividend payout of 25% of the previous year's net income in the following years.

Key metrics

Simpar S.A.--Forecast summary

Industry sector: misc. transportation

(Mil. R\$)	--Fiscal year ended Dec. 31--								
	2020a	2021a	2022a	2023a	2024e	2025f	2026f	2027f	2028f
Revenue	9,807	13,866	24,382	31,844	40,219	47,487	55,478	61,234	66,512
EBITDA (reported)	2,221	4,246	7,013	8,373	10,597	12,814	14,855	16,315	17,809
Plus/(less): Other	136	-129	-75	-175	134	134	134	134	134
EBITDA	2,357	4,117	6,938	8,198	10,731	12,948	14,989	16,449	17,943
Less: Cash interest paid	-1,134	-1,540	-3,126	-4,554	-5,697	-5,548	-5,494	-5,499	-5,504
Less: Cash taxes paid	-348	-174	-465	-482	-414	-692	-1,043	-1,243	-1,822
Funds from operations (FFO)	874	2,404	3,347	3,163	4,621	6,707	8,452	9,706	10,617
EBIT	1,804	3,706	6,270	5,575	8,153	9,709	11,086	12,091	13,251
Interest expense	1,073	2,090	3,904	4,475	6,321	6,159	6,100	6,105	6,111
Cash flow from operations (CFO)	1,821	2,830	2,363	2,162	3,768	5,846	7,514	8,740	9,713
Capital expenditure (capex)	3,358	9,886	13,462	7,940	9,125	10,240	8,547	8,738	9,149
Free operating cash flow (FOCF)	-1,537	-7,056	-11,099	-5,778	-5,357	-4,393	-1,033	2	564
Dividends	49	227	415	482	--	201	420	633	754
Discretionary cash flow (DCF)	-1,640	-7,566	-11,532	-6,297	-5,358	-4,594	-1,453	-631	-190
Debt (reported)	16,892	33,264	37,901	43,166	50,435	52,232	54,178	54,123	54,068
Plus: Lease liabilities debt	806	1,114	1,924	2,137	2,291	2,387	2,477	2,564	2,654
Less: Accessible cash and liquid Investments	-5,845	-13,634	-12,742	-10,946	-12,209	-8,855	-8,502	-7,422	-6,791
Plus/(less): Other	-2,287	-3,682	6,020	5,007	3,497	3,305	2,819	2,699	2,653

Simpar S.A.--Forecast summary (cont.)

Industry sector: misc. transportation

(Mil. R\$)	--Fiscal year ended Dec. 31--								
	2020a	2021a	2022a	2023a	2024e	2025f	2026f	2027f	2028f
Debt	9,566	17,061	33,102	39,364	44,013	49,070	50,972	51,964	52,584
Cash and short-term investments (reported)	8,328	18,652	12,742	10,946	12,209	8,855	8,502	7,422	6,791
Adjusted ratios (%)									
Debt/EBITDA (x)	4.1	4.1	4.8	4.8	4.1	3.8	3.4	3.2	2.9
FFO/debt	9.1	14.1	10.1	8.0	10.5	13.7	16.6	18.7	20.2
FFO cash interest coverage (x)	1.8	2.6	2.1	1.7	1.8	2.2	2.5	2.8	2.9
EBITDA interest coverage (x)	2.2	2.0	1.8	1.8	1.7	2.1	2.5	2.7	2.9
CFO/debt	19.0	16.6	7.1	5.5	8.6	11.9	14.7	16.8	18.5
FOCF/debt	-16.1	-41.4	-33.5	-14.7	-12.2	-9.0	-2.0	0.0	1.1
DCF/debt	-17.1	-44.3	-34.8	-16.0	-12.2	-9.4	-2.9	-1.2	-0.4
Annual revenue growth	1.2	41.4	75.8	30.6	26.3	18.1	16.8	10.4	8.6
EBITDA margin	24.0	29.7	28.5	25.7	26.7	27.3	27.0	26.9	27.0
EBIT margin	18.4	26.7	25.7	17.5	20.3	20.4	20.0	19.7	19.9
Return on capital	15.4	20.8	20.4	13.1	16.7	17.7	18.4	19.0	19.6
EBIT interest coverage (x)	1.7	1.8	1.6	1.2	1.3	1.6	1.8	2.0	2.2
Debt/debt and equity	74.8	74.6	85.6	85.4	85.4	84.5	82.1	79.3	75.4

All figures include S&P Global Ratings adjustments' unless stated as reported. a--Actual. e--Estimate. f--Forecast.

Liquidity

We view Simpar's liquidity as adequate. The group's sources of cash comfortably exceed its liquidity needs in the next 12-24 months, mostly because of its significant cash holdings, extended debt amortization profile, and committed credit lines. We forecast a sources-to-uses ratio of about 1.6x despite considerable capex for expansion.

In addition, we believe that the group has proven access to diversified sources of funding at a reasonable cost. We believe Simpar and its subsidiaries will maintain wide access to banks and domestic capital markets.

Principal liquidity sources as of June 30, 2024:

- Cash position of R\$11.8 billion
- Total available credit lines across the group of R\$3.7 billion (Vamos: R\$640 million, JSL: R\$817 million, and Simpar: R\$2.2 billion)
- Cash FFO of R\$5.4 billion in the next 12 months
- Movida and Vamos' debt issuances of R\$2.7 billion after June 2024
- Vamos' agribusiness credit rights certificates of R\$856 million in September 2024

- The group could contract uncommitted secured funding of up to 70% of the operating leasing subsidiaries' net capex related to vehicle purchases

Principal liquidity uses as of June 30, 2024:

- Short-term debt maturities of R\$6 billion
- Short-term acquisitions payable of R\$262 million
- Working capital needs of R\$1 billion in the next 12 months
- Net capex of R\$9.7 billion in the next 12 months
- Dividend payments of R\$100 million in the next 12 months
- Assignment of credit rights of R\$1.7 billion in the next 12 months

Covenants

Simpar's financial flexibility is limited by financial covenants on its debt, which require:

- Net debt to EBITDA-A (EBITDA plus cost of assets sold) of 3.5x and EBITDA-A to net interest at a minimum of 2.0x. These covenants apply to the local debentures and agribusiness receivable certificates, and they would accelerate debt payment if triggered.
- Net debt to EBITDA below 4.0x. This is applicable to the group's bond issuance. It doesn't trigger debt acceleration; it's an incurrence covenant that limits the company's ability to contract additional debt.

We expect Simpar to comply with the net debt-to-EBITDA requirement with a cushion of only 10% in 2024, before increasing that to above 15% in coming years amid higher EBITDA generation. We expect Simpar to maintain a cushion of above 30% for the interest coverage ratio in the next two years. We also believe Simpar has some levers, such as reducing capex, to control covenant measurement if needed.

Environmental, Social, And Governance

Governance factors are now a neutral consideration in our credit analysis of Simpar. The CEO of the group and indirect controlling shareholder have been implicated in alleged fraud in bidding for contracts, corruption, and bribery. Most of the lawsuits have already been ruled off and some dismissed because of lack of proof. The amounts associated with the remaining lawsuits are immaterial.

Issue Ratings--Recovery Analysis

Key analytical factors

- We rate the group's senior unsecured bond and local market debentures 'BB-' and 'brAA+', respectively (the same as our issuer credit ratings on the company), with a '4' recovery rating. The '4' recovery rating reflects our expectation for average (30%-50%; rounded estimate: 35%) recovery in the event of a payment default, considering the expected recovery at each of Simpar's subsidiaries as well as the resulting debt structure of the nonoperating holding

company.

- Our simulated default scenario contemplates a payment default in 2028. The simulated default scenario encompasses high default rates at Vamos' and JSL's portfolios of contracts, lower utilization rates of Movida's rental car business, and an erosion of Brazil's used-car and truck market, lowering the group's cash generation and limiting its asset sales. This would hamper its capacity to service interest and principal payments. We also account for limited access to refinancing amid a long period of fragile credit conditions.
- We value the group by considering a combination of the EBITDA multiple and discrete asset valuation approaches. We value its logistics and other business using a 6.0x multiple applied to our projected emergence-level EBITDA, reflecting Simpar's continued solid growth prospects.
- The projected emergence-level EBITDA is R\$2 billion, resulting in an estimated gross emergence value of about R\$11.8 billion. We have valued Simpar's operating lease business segment with the discrete asset valuation approach, applying an overall haircut of around 25%-30% to the asset bases of those subsidiaries, arriving at a stressed valuation of about R\$36.2 billion.
- We assume that the secured debt and the debt at JSL, Vamos, and Movida have priority over Simpar's unsecured debt in a hypothetical default scenario because those subsidiaries are not guarantors of the debt at the holding company level.

Simulated default assumptions

- Year of default: 2028
- Jurisdiction: Brazil

Simplified waterfall

- Consolidated enterprise value (net of 5% administrative expense): R\$45.7 billion, R\$19.2 billion of which is attributed to Movida, R\$15.3 billion of which is attributed to Vamos, and R\$11.2 billion of which is attributed to JSL and other subsidiaries
- Debt position at subsidiaries: R\$43.3 billion
- Senior unsecured debt at the holding company level: R\$7.4 billion
- Recovery expectations for bonds and debentures at the holding company level: 30%-50% (rounded estimate: 35%)

Note: All debt amounts include six months of prepetition interest.

Ratings Score Snapshot

Issuer Credit Rating: BB-/Stable/--

Business risk: Satisfactory

- Country risk: Moderately high
- Industry risk: Intermediate
- Competitive position: Satisfactory

Financial risk: Aggressive

- Cash flow/leverage: Aggressive

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: Neutral (no impact)
- Comparable rating analysis: Negative (-1 notch)

Stand-alone credit profile: bb-

Related Criteria

- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- 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 | Industrials: Key Credit Factors For The Operating Leasing Industry, Dec. 14, 2016
- Criteria | Corporates | General: Recovery Rating Criteria For Speculative-Grade Corporate Issuers, Dec. 7, 2016
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- 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
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Simpar S.A.		
Issuer Credit Rating	BB-/Stable/--	BB-/Positive/--
Brazil National Scale	brAA+/Stable/--	brAA+/Positive/--

Ratings Affirmed

Simpar S.A.	
Senior Unsecured	brAA+
Recovery Rating	4(35%)

Simpar Europe

Senior Unsecured	BB-
Recovery Rating	4(35%)

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