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Research Update:

Simpar 'BB-' Global Scale Ratings Affirmed On Solid Operations Despite Still High Leverage; Outlook Remains Positive

December 4, 2023

Rating Action Overview

- We expect that Simpar S.A. will maintain efficient operations and continue absorbing synergies from recent acquisitions. We think EBIT margin will be above 20% in coming years.
- On the other hand, because of debt-financed growth amid elevated interest rates in Brazil, improvement in the group's credit metrics has been slower-than-expected.
- Therefore, we affirmed our 'BB-' global scale and 'brAA+' national scale issuer credit and issue-level ratings on Simpar.
- The positive outlook indicates that we could raise the ratings in the next six to 12 months if Simpar delivers the expected improvements in its credit metrics, with EBIT interest coverage of at least 1.7x and funds from operations (FFO) to debt in the mid-teens.

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Rating Action Rationale

Simpar will continue its solid operating performance and scale gains. The group expanded operations significantly in recent years, both organically and through acquisitions. We forecast about 32.5 billion Brazilian reals (R$) in net revenue in 2023, compared with R$13.9 billion in 2021. We believe Simpar will continue consolidating itself as Brazil's largest transportation and logistics group, with leading positions in several of its businesses. The group made over 20 acquisitions in 2020-2023, adding significant scale and business diversification.

Simpar has a solid track record in consolidating acquisitions and absorbing synergies, maintaining solid profitability. The group's larger scale gives it more access to discounts and fast service from original equipment manufacturers--more access than what smaller players get, and similar access to what a main peer and market leader, Localiza, gets for light vehicles.

We expect the group to keep working on efficiency measures, gradually expanding EBIT margin to 22%-25% in 2024-2025 from about 21% in 2023. Additionally, the group has a high-quality asset base and adequate secondary market structure, and it operates predominantly medium-to-long-term contracts with high renewal rates and significant cross-selling opportunities. These factors supported our revision of the business risk profile to satisfactory from fair.

We expect different growth strategies among its subsidiaries to sustain Simpar's revenue growth in coming years. After Movida expanded aggressively in recent years helped by heated demand, we forecast that Movida will have a total fleet of about 215,000 vehicles in 2023-2024, lower than the 223,984 it had at the end of 2022 with a decrease in the Rent-a-Car (RaC) business and moderate growth in its fleet with long-term contracts (known as the GTF fleet). This should lead to an increase in the company's average utilization rate in the RaC business--to 80.0% in the next few years from 75.7% in 2022--spurred by efficiency gains with a smaller fleet.

We expect Vamos to expand mostly by signing new lease contracts, and to post consistent revenue growth of over 45% in 2023 and over 35% in 2024. We expect two other Simpar subsidiaries, JSL and Automob, to continue consolidating the market, increasing their solid market positions. We expect JSL revenue growth of about 25% in 2023 and about 30% in 2024, from new contracts signed, cross-selling opportunities, and the consolidation of recent acquisitions. Automob will continue expanding via strategic acquisitions. Because it's uncertain when any future M&A actions would take place or how large they would be, we don't incorporate future M&A activity in our base case.

Elevated interest rates still weigh on credit metrics. The group expanded in recent years mainly through debt issuances; that, coupled with Brazil's elevated interest rates, generated a significant interest burden over the past two years. We now forecast weaker EBIT interest coverage in 2023 and 2024 (1.2x and 1.8x, respectively) relative to what we previously expected (2x and 2.8x, respectively). The consistent delays in reaching stronger credit metrics are what limit rating upside at this point.

We expect some subsidiaries to finance investments with internal cash flows and to continue refinancing upcoming maturities at lower cost, while other entities continue to benefit from the group's good access to capital markets in order to fund growth at reasonable cost, decreasing interest burden.

Outlook

The positive outlook indicates that we could raise the ratings in the next six to 12 months if we see stronger cash flows and lower interest burden in coming years as Simpar continues to benefit from the diversification of its business segments and solid growth.

Upside scenario

For an upgrade, we would expect the company to maintain an EBIT margin above 20% and to meet our expectations regarding EBIT interest coverage and FFO to debt. We expect it to reach and maintain EBIT interest coverage of at least 1.7x and FFO to debt in the mid-teens.

An upgrade would also depend on whether the company can maintain comfortable liquidity, with limited short-term maturities. That would allow us to rate Simpar above the 'BB-' sovereign rating on Brazil.

Downside scenario

We could change the outlook to stable if the group's cash flows remain pressured amid higher interest rates or weaker market conditions for its largest subsidiaries, or if Simpar adopts a more aggressive growth strategy funded with debt. In this scenario, we would see EBIT interest coverage below 1.7x and FFO to debt below 12%, consistently.

Company Description

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

We expect the group to post consolidated revenue of about R$32.5 billion and EBITDA close to R$8.6 billion in 2023, with the following EBITDA breakdown: Movida (45%), Vamos (30%), and JSL (20%), with other subsidiaries accounting for the remainder.

- Movida is the second-largest car rental company in Brazil, offering RaC, fleet management services, and sales of used vehicles. The subsidiary ended September 2023 with a total fleet of 213,847 vehicles (44% RaC and 56% GTF) and with 345 stores (92 of which are for used car sales).
- Vamos is a Brazilian truck, machinery, and equipment rental company, operating 62 new truck and equipment dealerships and 14 used truck and equipment dealerships across the country. It had a total fleet of 45,161 assets (35,062 trucks and 10,099 units of equipment) as of Sept. 30, 2023.
- JSL is the main provider of logistics services and freight transportation in Brazil. Its portfolio consists of asset-light and asset-heavy contracts, accounting for 54% and 46% of its total revenue in 2022, respectively.
- Automob is one the largest authorized car dealerships in Brazil, operating 108 stores and 27 brands spread across 18 cities.
- BBC Bank operates mainly to offer 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, urban mobility infrastructure, and sanitation. Ciclus Ambiental do Brasil engages in solid waste management in the Rio de Janeiro metropolitan area.

Our Base-Case Scenario

Assumptions

- GDP growth in Brazil of about 2.9% in 2023, 1.5% in 2024, and 1.9% in 2025.
- Average inflation in Brazil of about 4.6% in 2023, 3.6% in 2024, and 3.7% in 2025, affecting

labor-related costs and fleet maintenance prices.

- Average base interest rates of 13.1% in 2023, 10.4% in 2024, and 9% in 2025, influencing funding costs and rates of new fleet management contracts.
- Simpar revenue increasing about 35% in 2023 from the consolidation of Automob's and JSL's acquisitions.
- We expect Vamos to have 45% revenue growth from new contracts with higher prices, and Movida to have moderate 10%-15% revenue growth from higher prices amid smaller fleets.
- Revenue growth for Vamos and JSL in coming years primarily from their sizable backlogs, new contracts, and price adjustments.
- Continued expansion by Automob, mostly from M&A--but because it's uncertain when any M&A would take place or how large any transactions would be, our base case assumes only organic growth, with openings of new dealerships and a better macro environment boosting vehicle sales.
- Simpar's consolidated EBIT margin of 20%-25% in the next few years, as Movida increases its occupancy rate, JSL absorbs synergies from acquired assets (through its strong bargaining power with suppliers), and cost inflation passes through across all subsidiaries.
- Lower working capital needs in 2024 as a result of lower inventory levels at Vamos.
- Cash payments related to recent acquisitions totaling R$450 million-R$500 million in 2024-2025.
- Dividend payout of 25% of the previous year's net income.

Key metrics

Simpar S.A.--Forecast summary

Industry sector: Misc. transportation									
	--Year ended Dec. 31--								
(Mil. R$)	2019a	2020a	2021a	2022a	2023e	2024f	2025f	2026f	2027f
Revenue	9,686	9,807	13,866	24,382	32,491	39,544	44,627	49,838	54,978
EBITDA, reported	2,148	2,221	4,246	7,140	8,565	10,632	13,331	14,365	16,126
Plus/less: Other	(14)	136	(129)	(75)	(3)	(3)	(3)	(3)	(3)
EBITDA	2,135	2,357	4,117	7,065	8,562	10,629	13,328	14,362	16,123
Less: Cash interest paid	(1,018)	(1,134)	(1,540)	(3,126)	(5,295)	(4,605)	(4,838)	(5,558)	(5,989)
Less: Cash taxes paid	(123)	(348)	(174)	(465)	(1)	(356)	(647)	(755)	(909)
Funds from operations (FFO)	994	874	2,404	3,474	3,265	5,668	7,843	8,049	9,226
EBIT	1,525	1,804	3,706	6,270	6,787	8,700	11,211	12,191	13,941
Interest expense	1,042	1,073	2,090	3,904	5,572	4,846	5,091	5,849	6,301
Cash flow from operations (CFO)	1,043	1,821	2,830	2,363	2,171	5,239	8,390	9,017	10,740
Capital expenditures	3,039	3,358	9,886	13,492	5,663	9,610	10,807	8,134	6,819
Free operating cash flow (FOCF)	(1,997)	(1,537)	(7,056)	(11,129)	(3,492)	(4,371)	(2,417)	883	3,921
Dividends	53	49	227	415	235	2	584	1,068	1,046

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

Industry sector: Misc. transportation									
	--Year ended Dec. 31--								
(Mil. R$)	2019a	2020a	2021a	2022a	2023e	2024f	2025f	2026f	2027f
Discretionary cash flow (DCF)	(2,061)	(1,640)	(7,566)	(11,562)	(3,871)	(4,373)	(3,001)	(185)	2,874
Debt, reported	13,594	16,892	33,264	37,901	41,851	48,313	55,114	60,370	62,291
Plus: Lease liabilities debt	919	806	1,114	1,924	2,013	2,085	2,162	2,238	2,316
Less: Accessible cash and liquid Investments	(3,848)	(5,845)	(13,634)	(12,742)	(11,911)	(13,832)	(17,562)	(22,634)	(27,479)
Plus/less: Other	(2,461)	(2,287)	(3,682)	6,020	3,240	2,886	2,698	2,502	2,425
Debt	8,204	9,566	17,061	33,102	35,192	39,453	42,413	42,476	39,553
Cash and short-term investments, reported	5,774	8,328	18,652	12,742	11,911	13,832	17,562	22,634	27,479
Adjusted ratios									
Debt/EBITDA (x)	3.8	4.1	4.1	4.7	4.1	3.7	3.2	3.0	2.5
FFO/debt (%)	12.1	9.1	14.1	10.5	9.3	14.4	18.5	18.9	23.3
FFO cash interest coverage (x)	2.0	1.8	2.6	2.1	1.6	2.2	2.6	2.4	2.5
EBITDA interest coverage (x)	2.0	2.2	2.0	1.8	1.5	2.2	2.6	2.5	2.6
CFO/debt (%)	12.7	19.0	16.6	7.1	6.2	13.3	19.8	21.2	27.2
FOCF/debt (%)	(24.3)	(16.1)	(41.4)	(33.6)	(9.9)	(11.1)	(5.7)	2.1	9.9
DCF/debt (%)	(25.1)	(17.1)	(44.3)	(34.9)	(11.0)	(11.1)	(7.1)	(0.4)	7.3
Annual revenue growth (%)	19.9	1.2	41.4	75.8	33.3	21.7	12.9	11.7	10.3
EBITDA margin (%)	22.0	24.0	29.7	29.0	26.4	26.9	29.9	28.8	29.3
EBIT margin (%)	15.7	18.4	26.7	25.7	20.9	22.0	25.1	24.5	25.4
Return on capital (%)	16.0	15.4	20.8	20.4	16.9	19.3	21.7	21.6	23.8
EBIT interest coverage (x)	1.5	1.7	1.8	1.6	1.2	1.8	2.2	2.1	2.2
Debt/debt and equity (%)	77.5	74.8	74.6	85.6	84.4	81.7	77.2	73.1	66.8

All figures are adjusted by S&P Global Ratings 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 high cash holdings, an extended debt amortization profile, and committed credit lines. We forecast a sources-to-uses ratio of about 2x despite considerable capital expenditures for expansion. In addition, we believe that the group has proven access to diversified sources of funding at reasonable cost. We believe Simpar and its subsidiaries will continue to have wide access to banks and domestic capital markets. But we would need to see consistent liquidity comfort to revise our liquidity assessment to a stronger category.

Principal liquidity sources as of Sept. 30, 2023:

- Cash position of R$8 billion.
- Total available credit lines across the group of R$4.1 billion (Vamos, R$1.4 billion; JSL, R$1.4 billion; and Simpar, the parent, R$1.3 billion).
- Cash FFO of R$5.1 billion in the next 12 months.
- JSL's new bank loans of R$430 million, disbursed in October 2023.
- Movida's recent real estate receivables certificates (known as CRI) and debentures, amounting to R$1.7 billion in October 2023.
- Vamos' recent agribusiness receivables certificate (CRA), amounting to R$700 million in November 2023.
- 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 Sept. 30, 2023:

- Short-term debt maturities of R$3.2 billion.
- Short-term acquisitions payable of R$233.7 million.
- Working capital needs of R$1.4 billion in the next 12 months.
- Net capex of R$7.6 billion in the next 12 months.
- Dividend payments of R$118.4 million in 2024.

Covenants

Simpar's financial flexibility is limited by debt-payment acceleration covenants on its debentures and notes, which require:

- Net debt to EBITDA-A of 3.5x and EBITDA-A to net interest at a minimum of 2.0x. These covenants apply to the local debentures and CRA, and they are of debt payment acceleration type.
- 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 ability to contract additional debt.

We expect Simpar to comply with the net debt-to-EBITDA requirement with a cushion of over 15% in 2023, but increasing to above 20% in coming years amid higher EBITDA generation. We expect Simpar to maintain a cushion of above 40% for the interest coverage ratio in the next two years.

Environmental, Social, And Governance

Governance factors are a moderately negative consideration in our credit rating analysis of Simpar. The chairman of the board, who is also the indirect controlling shareholder, has been implicated in alleged fraud in bidding for contracts, corruption, and bribery. Although the allegations could increase reputational risks and eventually result in fines, two civil lawsuits haven't been ruled on yet, while others were dismissed. Also, the group currently has processes to monitor and mitigate the key risks related to its public bidding activities, such as independent third-party audits.

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), 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 2027. The simulated default scenario encompasses a combination of high default rates at Vamos' and JSL's portfolios of contracts, the lower utilization rates of Movida's RaC business, and an erosion of Brazil's used-car and truck market, resulting in the group's lower cash generation and limited asset sales activity, which 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 EBITDA multiple and discrete asset valuation (DAV) approach. We value its logistics and other business using a 6.0x multiple applied to our projected emergence-level EBITDA, reflecting Simpar's high growth prospects given recent M&A and internal growth.
- The projected emergence-level EBITDA is R$1.2 billion, resulting in an estimated gross emergence value of about R$7.2 billion. We have valued Simpar's operating lease business segment by the DAV approach, applying an overall haircut of close to 50% to those subsidiaries' asset base, arriving at a stressed valuation of about R$27.6 billion.
- We assume that the secured debt and the debt at the subsidiaries--JSL, Vamos, CS Brasil, and Movida--have priority to 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: 2027
- Jurisdiction: Brazil

Simplified waterfall

- Consolidated enterprise value (net of 5% administrative expense): R$33.1 billion, R$13.8 billion of which is attributed to Movida, R$12.4 billion of which is attributed to Vamos, and R$6.9 billion of which is attributed to JSL and other subsidiaries
- Debt position at subsidiaries: R$32.6 billion
- Senior unsecured debt at the holding company level: R$3.9 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-/Positive/--
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	Fair (no impact)
Comparable rating analysis	Negative (-1 notch)
Stand-alone credit profile:	bb-

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: 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: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, 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

Ratings List

Ratings Affirmed	
Simpar S.A.	
Issuer Credit Rating	BB-/Positive/--
Brazil National Scale	brAA+/Positive/--
Simpar S.A.	
Senior Unsecured	brAA+
Recovery Rating	4(35%)
Simpar Europe	
Senior Unsecured	BB-
Recovery Rating	4(35%)

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.spglobal.com/ratings for further information. Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.