FitchRatings

RATING ACTION COMMENTARY

Fitch Assigns 'BB-' First Time Rating to Movida; Outlook Stable

Mon 25 Jan, 2021 - 15:10 ET

Fitch Ratings - Rio de Janeiro - 25 Jan 2021: Fitch Ratings has assigned first time Long-Term Foreign and Local Currency Issuer Default Ratings (IDRs) of 'BB-' to Movida Participacoes S.A. (Movida) and to its proposed benchmark sized unsecured notes to be issued by Movida Europe, a wholly owned subsidiary of Movida. The notes will be unconditionally and irrevocably guaranteed by Movida Participacoes S.A. Proceeds will be used to refinance existing debt and general corporate purposes. The corporate Rating Outlook is Stable. Fitch currently rates Movida's National Long-Term Rating 'AA-(bra)/Outlook Stable.

The rating reflects Movida's solid business position within the competitive car and fleet rental industry in Brazil, with adequate operational efficiency. Its size, as the third largest industry player in Brazil, results in good bargaining power with automobile manufacturers, enabling Movida to better capture economies of scale. The rating also incorporates the company's improved business and operating performance in the last couple of years and solid financial performance during the coronavirus pandemic. A key factor in the ratings is the company's sizable pool of unencumbered vehicles that bolster its access to funding during periods of restricted availability of credit in debt capital markets.

Movida's market-share oriented strategy and its aggressive growth, leads to recurring negative FCF generation, which has been funded primarily through debt. The car and fleet rental industry is capital intensive, largely exposed to credit availability and interest rate levels and to the economic cycle, particularly to unemployment. Over the past few years, favorable industry dynamics in the local market for fleet and car rental and the used car sales business have been supporting strong growth opportunities and mitigated the poor macroeconomic conditions in Brazil. The local industry faces fierce competition and is currently experiencing a period of consolidation after the announced merger of the two largest players during 2020.

Partially offsetting financial and sector risks, is Movida's ability to adjust its operations and growth to economic cycles at its discretion, as it has done in the past, in order to generate positive FCF and enhance its fiscal flexibility. The company has demonstrated an improving access to lower cost credit lines, mostly in the domestic market, and with the current issuance it seeks to diversify its funding sources.

The Stable Outlook reflects our expectation that Movida's revenues will grow while maintaining an adequate credit profile commensurate with its rating level. Fitch projects that the company's adjusted net debt/EBITDA ratio will remain between 3.5x and 3.8x across our rating horizon. For 2020 and 2021, respectively, Fitch forecasts net revenues of BRL4.2 billion and BRL5.3 billion, EBITDA of BRL818 million (19% margin) and BRL1.2 billion (21% margin), and net debt/EBITDA of 3.0x and 3.5x.

KEY RATING DRIVERS

Solid Competitive Position: As the third largest player in the car and fleet rental industry in Brazil, Movida has a solid business position, underpinned by its large scale, operating expertise, a national footprint and an adequate used car sale operation. As of September 2020, Movida's fleet of 108,709 vehicles, consisting of 67,978 in rent-a-car (RaC) and 40,731 in fleet management (FM), secured market shares of approximately 15% in RaC and 8% in FM, by fleet size. As a result, the company has good bargaining power with automobile manufacturers and is able to capture economies of scale. At YE 2020 and 2021, Movida's total fleet should be around 112,092 and 130,947 vehicles, respectively.

Capital Intensive Industry: The capital-intensive nature of the rental industry, which demands sizable and regular investments to grow and renew the fleet, pressures the financial profile of the companies in the sector. Therefore, lower funding costs and strong access to credit markets are key competitive advantages. On the other hand, the business model allows the companies to postpone fleet renewal and adjust, if needed. Main risks for this industry in 2021 are the uncertainty regarding the pace of the recovery of the Brazilian automobile industry, which may constrain vehicle supply in the first quarter, constrained credit markets, an unexpected increase in interest rates, worse than expected economic activity and deterioration in the used car sale market.

Improving Operating Performance: Fitch expects Movida to continue to improve operating performance in the following years, supported by a healthy price environment, stronger demand, new mobility trends and maintenance costs per operating vehicle, utilization rate, and selling cost per vehicle closer to market benchmarks. Fitch forecast the RaC utilization rate at 77% in 2020 and 78% in 2021 compared to 76% in 2019, while fleet utilization rate should be higher than 95%. Fitch expects to see the company's EBITDA margins evolving from pre-crises levels in 2021-2022, as car and fleet rental regained traction after the worst period of lockdown restrictions.

Fitch forecasts EBITDA of BRL818 million (19% margin) in 2020, with strong growth in 2021. Fitch estimates EBITDA at BRL1.2 billion (21% margin) and BRL1.7 billion (22% margin), in 2021 and 2022, respectively. We project negative FCF during the rating horizon, due to higher growth capex, around BRL365 million in 2020 and BRL1.5 billion in 2021. In the LTM ended on September 2020, Movida's EBITDA and FCF were, respectively, BRL705 million (17% margin) and negative BRL400 million.

Growth to Continue to Pressure Leverage: Movida's growth-oriented strategy, to enhance and consolidate its business position, may pressure the company's leverage levels over the rating horizon. Fitch expects Movida's commitment to a sound capital structure alongside its robust cash generation will enable the company to manage its growth while keeping leverage levels aligned with current ratings. Fitch forecast net debt/EBITDA around to 3.5x depending on the stage of the investment cycle, being 3.0x in 2020, 3.5x in 2021 and 3.8x in 2022.

Coronavirus Limited Impact: The coronavirus outbreak containment measures, such as social distancing and mobility restrictions had a lower impact in the industry than initially anticipated. During the worst period of lockdown restrictions, contract cancelations and the slight increase in delinquency were not meaningful. Fitch projects a resumption of growth and increase in the car and fleet rental industry penetration from 2021, as a result of mass vaccination, new mobility habits, and companies choosing to lease and preserve liquidity.

Parent and Subsidiary Linkage: Fitch rates Movida on a standalone basis but acknowledges that Simpar's ownership has benefited the company's financial flexibility. In addition to its 55.1% controlling stake, Simpar determines the business and financial strategies of Movida, selects its management, and has some freedom to manage its cash as there is no restriction on upstream dividends. Restrictions do apply to intercompany loans.

DERIVATION SUMMARY

Movida's ratings reflect the company's sound capital structure and business profile but relatively weaker competitive position when compared with its bigger domestic peer Localiza Rent a Car S.A. (BB/Negative). The company has 280 thousand vehicles, being almost two times bigger than its closest domestic peers, such as Companhia de Locação das Américas - Locamérica e Unidas S.A with 158 thousand cars and Ouro Verde Locacao e Servico S.A. (BB-/Stable) with 22 thousand vehicles.

Fitch believes that Movida's bargaining power and business position is weaker than that of the industry's benchmark, Localiza, but stronger than that of Ouro Verde. Compared with Localiza, Movida has a weaker financial profile with moderately higher leverage and relatively higher refinancing risks. Compared with Ouro Verde, Movida has a similar leverage and liquidity position, but a larger scale and stronger business profile alongside better access to credit markets.

KEY ASSUMPTIONS

Fitch's Key Assumptions Within Our Rating Case for the Issuer:

--Average consolidated annual revenue growth at 24% from 2020 to 2022;

--Consolidated EBITDA margin at 21%, on average, from 2020 to 2022;

--Consolidated net capex at around BRL1.2 billion, on average, from 2020 to 2022;

--Cash balance remains sound compared to short-term debt;

--Dividends at 35% net income.

RATING SENSITIVITIES

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

--Strengthening of the company's scale and competitive position, without jeopardizing the company's profitability or capital structure.

--Improvement in the company's financial profile, with adjusted net debt / EBITDA below 3.0x on a regular basis.

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

--Failure to preserve liquidity and inability to access adequate funding;

--Prolonged decline in demand coupled with inability to adjust operations, leading to a higher-than-expected fall in operating cash flow;

--Increase in adjusted net debt/EBITDA to more than 4.0x on a regular basis;

--Downgrade of Simpar's National Long-Term Rating to a level below that of Movida.

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

Adequate Liquidity: Movida's adequate liquidity position and track record of a proactive liability management is a key credit consideration. Movida's cash to short-term debt ratio has been 1.5x on average during the last three years. The company's expected negative FCF, a result of its growth strategy, will be financed by debt in Fitch's rating scenario. As of Sept. 30. 2020, Movida had BRL1.6 billion of cash and BRL4.1billion of total adjusted debt, BRL943 million of which is due in the short-term debt (1.8x cash coverage ratio).

The company's debt profile is mainly comprised of local debentures and promissory notes (69%), bank loans and working capital (18%), and FINAME and leasing operations (1%). Currently, less than 2% of Movida's debt is secured. Additionally, Movida's financial flexibility is supported by the company's ability to postpone growth capex to adjust to the economic cycle and to the considerable number of the group's unencumbered assets, with a book value of fleet over net debt at 1.3x.

SUMMARY OF FINANCIAL ADJUSTMENTS

--Growth capex was moved from the CFO to the CFI;

--OEM receivables related to vehicle acquisitions added to capex.

SOURCES OF INFORMATION

Movida Participacoes S.A.

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.

RATING ACTIONS

ENTITY/DEBT	RATING		
Movida Europe			
• senior unsecured	LT	BB-	New Rating
Movida Participacoes S.A.	LT IDR	BB- Rating Outlook Stable	New Rating
	LC LT IDR	BB- Rating Outlook Stable	New Rating

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Corporates Notching and Recovery Ratings Criteria (pub. 14 Oct 2019) (including rating assumption sensitivity)

Corporate Rating Criteria (pub. 21 Dec 2020) (including rating assumption sensitivity)

APPLICABLE MODELS

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

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

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Movida Participacoes S.A.	EU,UK Endorsed

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