S&P Global Ratings

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Various Rating Actions On Brazilian Car Rental And Transport Companies On COVID-19 Impact; Off Watch Negative

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- Considering the initial impact of COVID-19 and related mobility restrictions in Brazil, we currently expect rent-a-car companies' utilization rates to be about 65%-70% on average for 2020 and lower average tariffs due to a different client mix, resulting in weaker operating cash flows this year.
- Despite some resiliency in the past two months, we also see downside risks for the renewal of corporate leasing contracts, depending on the severity of the economic contraction. On the other hand, we expect car rental and transportation companies to maintain a prudent approach in face of current challenges, with cash inflows from the sale of used cars and announced reductions in investments used to preserve liquidity.
- As a result, on May 19, 2020, S&P Global Ratings affirmed the ratings on Localiza Rent a Car S.A., JSL S.A., Movida Participações S.A., Companhia de Locacao das Americas S.A. (Unidas S.A.), and LM Transportes Interestaduais Serviços e Comércio S.A. We also assigned negative outlooks on JSL S.A., Movida Participações S.A., Companhia de Locacao das Americas S.A. (Unidas S.A.), and LM Transportes Interestaduais Serviços e Comércio S.A. The outlook on Localiza is now stable. Finally, we lowered our national scale issuer credit and issue-level ratings on Vix Logística S.A. to 'brA+' from 'brAA-', with a negative outlook. We removed all these ratings from the CreditWatch listing with negative implications.
- The negative outlooks reflect the potential weakening in each companies' credit quality amid the still uncertain extent of the outbreak and the recession, as well as the path for economic recovery, which could take a toll on demand for rent-a-car services and corporate leasing contracts.

SAO PAULO (S&P Global Ratings) May 19, 2020--S&P Global Ratings today took the rating actions detailed above.

Rating Action Rationale

Market conditions for rent-a-car services in Brazil are challenging, but operations proved to be more resilient than global peers. Brazilian rent-a-car (RaC) companies saw utilization rates fall from their normal 75%-80% levels to 55%-60% in April with a marginal improvement in the first weeks of May, mainly because of mobility restrictions and the overall decline in economic activity. In addition, average tariffs are currently about 25% lower than pre-COVID-19 levels due to changes in the mix of clients and discounts applied to retained customers. We assume a gradual recovery in utilization rates mainly in the fourth quarter, which should result in an average of 65%-70% for the year. This will lead to weaker operating cash flows in 2020. Still, compared with global peers, the impact on Brazilian companies will likely be much lower given the higher proportion of fleet management in their businesses, lower revenue dependency on airline passenger traffic (about 10%-20% for each RaC business), and a higher proportion of individual and corporate monthly clients. Cash flows from corporate leasing contracts have been stable in the past few weeks since the government imposed mobility restrictions. Nevertheless, we believe the companies could face difficulties renewing contracts or delinquency increases going forward, depending on the recession's impact on each sector.

The extent of the recession and the path to recovery will drive our ratings. In our base-case scenario, we forecast EBITDA declines between 10% and 20% in 2020, depending on each company's exposure to the RaC segment and other business divisions, with slow but recovering levels in 2021 as the economy recovers and transport demand returns to levels similar to those in the past few years. Still, we see downside risks to our forecasts, and if we were to expect rent-a-car utilization rates to remain at 55%-60% for the rest of the year under current tariff prices, we would observe steeper EBITDA declines of 20%-30%, which could lead to downgrades.

We see higher downside risks on the operational side and increases in leverage, rather than on liquidity. Used car sales had slow but increasing activity in April and the first few weeks of May, with low price discounts performed by some players. We expect companies to use cash inflows from vehicle sales, combined with significant reductions of investments, to preserve their liquidity. We will monitor how the used car market behaves in the context of weaker consumer purchasing power in the coming quarters. Along with the capital spending flexibility, most of the Brazilian entities in the sector accessed credit markets in the first few weeks of the pandemic, increasing their cash position. In our view, such access, along with a smooth amortization profile for the year for most of the companies, should provide an adequate liquidity cushion for them to handle 2020's turbulence.

Environmental, social, and governance (ESG) credit factors for the rating changes:

- Health and safety

The rating actions for each company in the sector are detailed below.

Localiza Rent a Car S.A (Localiza)

We affirmed the 'BB+' global scale and 'brAAA' national scale ratings on Localiza with a stable outlook, reflecting our view of adequate cushion on the company's leverage metrics for the rating level, even amid the demand shock this year. This is because the final rating is currently one notch lower than company's 'bbb-' stand-alone credit profile (SACP) because we cap the rating two notches above the sovereign rating on Brazil (BB-/Stable/B). We see higher risk of us revising downward the SACP by one notch in the short term if cash flows from the RaC segment are weaker than what we currently forecast, due to the impact of mobility restrictions, social distancing measures, and the economic downturn. Considering the impact of COVID-19 in the last two months, we expect revenues and EBITDA declines of about 10%-15% and 15%-20%, respectively, in 2020. We also incorporate Localiza's capacity to reduce its current fleet in 2020 by 5% to 10% compared to 2019, generating additional cash flows from car sales. We expect EBIT interest coverage of 2.3x-2.6x in 2020, recovering in 2021 to 2.7x-3.0x as mobility restrictions ease.

In our base-case scenario, the long-term nature of fleet management contracts tend to mitigate the expected impact of depressed rental demand on Localiza's overall cash flow generation. Nevertheless, if due to the economic contraction we were to expect a reduction of these contracts, or potential breaches and increased delinquency, it could harm the company's operational performance and credit quality. Although cash position continues to be robust, we have revised our liquidity assessment to adequate from strong. This reflects the challenges Localiza could face in maintaining its cash reserves if economic and refinancing conditions worsen at a steeper-than-expected pace.

Outlook

The stable outlook reflects our view that Localiza's competitive advantages in the sector and comfortable credit metrics will help it overcome the expected weaker operating cash flows caused by the mobility restrictions and economic downturn in Brazil. We incorporate lower levels of used cars sales this year compared to pre-pandemic levels. Despite that, we expect Localiza to drastically reduce car acquisitions in 2020 and marginally increase them in 2021, following stronger economic activity. We expect EBIT interest coverage of 2.3x#2.6x and funds from operations (FFO) to debt at 15%#20% in 2020, recovering respectively to 2.7x#3.0x and above 20% in 2021.

Downside scenario

We could downgrade Localiza if higher mobility restrictions significantly reduce the already depressed utilization rates and the company is unable to sell used cars. In this scenario, we would expect EBIT interest coverage below 1.3x and FFO to debt below 12% in 2020 and 2021. We could revise downward the company's SACP to 'bb+' if the impact to its rental car utilization rates is higher than we currently predict, fleet management contracts are not renewed, and Localiza faces greater difficulties in selling its used fleet. That scenario could occur if mobility restrictions in Brazil increase or if we see deeper effects of the recession on customers' purchasing power. In that scenario, we would see cash flow reduction pointing to EBIT interest coverage below 1.7x.

Upside scenario

A positive rating action would depend on an upgrade of Brazil, which has a stable outlook, given that the rating on Localiza is already at the maximum two#notch differential above the sovereign.

JSL S.A.

We affirmed our 'BB-' global scale and 'brAA+' national scale ratings on JSL. The negative outlook on both ratings reflects our view that despite the significant impact on some of its subsidiaries' cash flow generation in 2020, JSL has some business resiliency that should contribute to recovery in 2021. The long-term contracts on its fleet management services and truck and heavy equipment rentals should partially offset the expected reduction in JSL's cash flows. We see its exposure to rental cars (about 30%#35% of JSL's consolidated EBITDA) as a factor that would pressure credit metrics if mobility restrictions are exacerbated in the next few months, or lower economic activity lasts for longer than expected. In 2020, we project a drop in consolidated revenues and EBITDA of about 10% and 10%-15%, respectively, compared with 2019.

Considering COVID#19's impact on the company's 2020 cash inflows and its capacity to reduce the size of its fleet in order to adapt to market conditions, we expect JSL's debt to EBITDA to increase to about 4.0x-4.5x and FFO to debt to be slightly lower than 12%. Despite the reduced cash flow generation, we expect EBIT interest coverage at 1.4x-1.7x in 2020. Because we forecast Brazil's economy to rebound in 2021, JSL's leverage metrics should follow the recovery, with EBIT interest coverage at 1.6x-1.8x, debt to EBITDA at 3.5x-4.0x, and FFO to debt above 12% next year.

Outlook

The negative outlook reflects our view that JSL's cash flow generation, and consequently its leverage metrics, could be more pressured in the medium term if mobility restrictions are exacerbated in Brazil in the next few months or if the economic contraction lasts for longer than predicted.

Downside scenario

We could downgrade JSL in the next 6-12 months if we perceive that Brazil's recession will be more severe and the impacts will be more lasting for JSL's business, leading to weaker cash flow generation in its different segments, with EBITDA falling more than 30% compared to 2019. In that scenario, we would expect EBIT interest coverage below 1.1x, debt to EBITDA above 5.0x, and FFO to debt below 12% in 2020 and 2021.

Upside scenario

We could revise the outlook to stable in the next 12 months if the impacts of the pandemic are shorter than expected, rental car use rates recover at a rapid pace in the next few months, and we have more clarity on 2021 Brazilian economic activity. In this scenario, EBIT interest coverage would remain about 1.7x , debt to EBITDA below 4.0x, and FFO#to#debt ratio consistently above 12%.

Movida Participações S.A.

We affirmed our 'brAA' national scale ratings on Movida with a negative outlook. The outlook reflects the risks of weaker economic activity leading to RaC utilization rates at lower levels for a longer period, and reduced fleet management business and used car sales. Our current scenario points to a deterioration in credit metrics in 2020, with EBIT interest coverage at about 2.0x compared with 2.3x in 2019. This scenario incorporates our forecast of a 70% utilization rate for its RaC business in 2020, higher car depreciation rates, somewhat stable cash flows from its fleet management business, and a 5%-10% decline in used car sales compared to 2019.

We expect Movida to maintain an adequate liquidity position even amid weaker cash flow generation. Its latest cash position of R$1.3 billion, including issuances in April and May,, more than covers its short-term debt of R$581 million in March 31, 2020. Movida's ability to maintain used car sales while temporarily suspending vehicle acquisitions in the initial stages of the pandemic--adapting its fleet size to the current market conditions--also support its liquidity position. We also observe that its negotiations with carmakers and banks for suppliers' financing, which would reduce working capital consumption this year, would provide further liquidity cushion. In our base case, we expect Movida to comply with acceleration-type financial covenants for its debentures and promissory notes in 2020, but with a limited cushion of about 13%.

Outlook

The negative outlook reflects the possibility of a downgrade should utilization rates for Movida's RaC business not improve in the coming months because of an extended impact of the pandemic while fleet management and used car sales activity worsen, hurting the company's cash generation and credit metrics.

Downside scenario

We could lower the ratings in the next 6-12 months if RaC utilization rates were to remain close to 55%-60% and/or if we were to expect weaker cash flows from fleet management and used car sales, resulting in an overall EBITDA reduction of about 25% this year. In this scenario, we would see EBIT interest coverage below 1.7x and FFO to debt below 12% in 2020 and 2021.

Upside scenario

We could revise the outlook to stable if the impacts of the pandemic are shorter than expected, RaC utilization rates recover rapidly in the next few months, and we gain more clarity about Brazil's economic activity in 2021. In this scenario, EBIT interest coverage would remain above 2.0x and FFO to debt consistently above 12%. At the same time, Movida would keep an adequate liquidity position, with sources over uses of cash consistently above 1.2x.

Companhia de Locação da Américas S.A. (Unidas S.A.)

We affirmed our 'brAAA' national scale rating on Unidas with a negative outlook. Even though Unidas is less exposed to the rental car segment compared to other players, the negative outlook on the company also reflects our expectation of weaker cash flow generation from its RaC business and downside risks to its fleet management and used car sales businesses. We forecast about 10% decline in EBITDA stemming from the RaC impact and higher car depreciation rates (20% increase year-over-year), which should result in EBIT interest coverage ratio of 2.0x-2.3x and FFO to debt close to 17%-20% by the end of 2020. We currently forecast somewhat improved RaC, fleet management, and used cars industry conditions in 2021, which would allow the company to post credit metrics similar to pre-pandemic levels, with an EBIT interest coverage ratio of 2.5x-3.0x and FFO-to-debt ratio close to 25%-30%.

Unidas' equity follow-on in late 2019 allowed the company to enter the pandemic with a strong cash position. The company used part of the proceeds to pay down suppliers, while its latest cash position of about R$1.5 billion, including issuances in April , comfortably covers short-term debt of R$120 million and could even allow for some increase in fleet size, should market conditions improve.

Outlook

The negative outlook reflects the possibility of a downgrade should rental car utilization rates for Unidas not improve in the coming months because of an extended impact of the pandemic while fleet management and used car sales activity worsen, hampering the company's cash generation and credit metrics.

Downside scenario

We could lower the rating in the next 12 months if the rent-a-car, fleet management, and used car market don't recover as expected after the impacts of the pandemic diminish, resulting in Unidas' EBIT interest coverage staying below 1.7x and its FFO-to debt-ratio remaining below 12% on a sustained basis.

Upside scenario

We could revise the outlook to stable if the impacts of the pandemic are shorter than expected, RaC utilizationrates recover quickly in the next few months, and we have more visibility about Brazil's forecasted economic recovery in 2021. In this scenario, EBIT interest coverage would remain above 3.0x and FFO-to-debt ratio consistently above 20%.

Vix Logística S.A.

The downgrade of Vix to 'brA+' from 'brAA-' and the negative outlook reflect that we expect much weaker EBITDA and cash flow generation for Vix's parent company, Águia Branca Participações (GAB; not rated), due to mobility restrictions and lower economic activity. We expect a severe demand contraction of about 50% in GAB's bus passenger transport division and about 30% in its auto and truck dealer division in 2020 compared with 2019. However, we believe the group will burn cash in the bus passenger transport division only in the second quarter, because it's reducing its operations and selling assets. Still, because of much weaker operations in these two segments, combined with a decline in Vix's EBITDA of about 5% in 2020, we expect GAB's gross debt to EBITDA to peak near 6.0x in 2020, compared with 4.2x in 2019.

Even amid the reduction of some contracts due to lower economic activity, we expect a lower impact on Vix's cash flows compared with the overall group, given its exposure to more resilient businesses, such as its dedicated logistic and fleet management businesses. The company has shown active risk management, lowering investments while selling assets. Nevertheless, the negative outlook on the rating reflects the potential downward pressure on Vix's and the group's cash generation amid lower demand for transport because of depressed economic activity this year and an uncertain path for recovery. We expect Vix to post gross debt to EBITDA of close to 5.0x in 2020 compared with 4.6x in 2019.

We don't see significant liquidity pressures in the next 12 months. As of March 31, 2020, GAB and Vix each had a cash position of R$900 million and R$400 million, respectively, compared with R$431 million and R$368 million of short-term debt, and both have accessed credit markets to reinforce cash position in the past few weeks. We also expect Vix to comply with its acceleration-type covenant of net debt to EBITDA below 4x with a cushion of about 20% in 2020.

Outlook

The negative outlook reflects our expectation of higher leverage in 2020 because of the depressed economy and mobility restrictions hurting the company and group's businesses, resulting in gross debt to EBITDA close to 5.0x for Vix and about 6.0x for the group in 2020.

Downside scenario

We could lower the ratings on Vix in the next 6-12 months if the company's cash flow generation and liquidity position worsen because of the prolonged effect of the pandemic, resulting in gross debt to EBITDA above 5x for both Vix and the group throughout 2020 and 2021.

Upside scenario

We could revise the outlook to stable if we have a clearer view of the path of economic recovery in 2021 and the company is able to improve its operating performance such that we would expect leverage below 4.5x consistently for both Vix and the group.

LM Transportes Interestaduais Serviços e Comércio S.A. (LM)

We affirmed our 'brA' rating on LM with a negative outlook. The outlook reflects our view of downside risks to the company's cash flow generation due to uncertainties about the impact that the economic recession will have on different sectors of the economy over the next few quarters, and the unclear recovery path. Still, the affirmation reflects the somewhat stable cash flows forecast from its fleet management business, which has some concentration in the more resilient food and utilities sectors. We expect EBIT interest coverage ratio to remain close to 2.0x and FFO to debt to be 10%-15% in 2020.

The company has a less than adequate liquidity position, with sources of cash covering short-term needs by about 1.15x over the next 12 months as of March 2020. Additionally, we expect a tight cushion of less than 10% on LM's financial covenant that requires debt to EBITDA below 3.0x. On the other hand, we believe that LM has some ability to adjust its debt position to comply with covenants due to high liquid nature of part of its assets, mainly the light vehicles.

Outlook

The negative outlook reflects the possibility of a downgrade should an extended impact from the pandemic translate into weaker cash flow generation for LM because of deterioration drop in its fleet management and used car sales activity.

Downside scenario

We could lower the ratings on LM in the next 6-12 months if we were to expect weaker cash flow generation resulting in FFO to debt below 12% and EBIT interest coverage close to 1.3x. In addition, we could lower the ratings if LM's liquidity profile worsened due to such conditions and it faced restrictions to refinance, potentially breaching its covenants.

Upside scenario

We could revise the outlook to stable if we have a clearer view of the path of economic recovery in 2021 and the company's operating performance improves such that EBIT interest coverage would remain above 2.0x and FFO to debt above 15% in a consistent manner. In this scenario, we would also see a higher cushion on LM's financial covenants.

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- 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
- Criteria | Corporates | Industrials: Key Credit Factors For The Railroad And Package Express Industry, Aug. 12, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed; Outlook/CreditWatch Action

	To	From
Localiza Rent a Car S.A.		
Issuer Credit Rating	BB+/Stable/--	BB+/Watch Neg/--
Brazil National Scale	brAAA/Stable/--	brAAA/Stable/--
Senior Unsecured		
Brazil National Scale	brAAA	brAAA
Recovery Rating	3(65%)	3(65%)
	To	**From**
JSL S.A.		
Issuer Credit Rating	BB-/Negative/--	BB-/Watch Neg/--
Brazil National Scale	brAA+/Negative/--	brAA+/Watch Neg/--
Senior Unsecured		

Brazil National Scale	brAA+	brAA+/Watch Neg
Recovery Rating	3(60%)	3(60%)
	To	**From**
JSL Europe		
Senior Unsecured	BB-	BB-/Watch Neg
Recovery Rating	3(60%)	3(60%)
	To	**From**
Movida Participações S.A.		
Issuer Credit Rating		
Brazil National Scale	brAA/Negative/--	brAA/Watch Neg/--
Senior Unsecured		
Brazil National Scale	brAA	brAA/Watch Neg
Recovery Rating	3(65%)	3(65%)
	To	**From**
LM Transportes Interestaduais Servicos e Comercio S.A.		
Issuer Credit Rating		
Brazil National Scale	brA/Negative/--	brA/Watch Neg/--
	To	**From**
Companhia de Locacao das Americas S.A.		
Issuer Credit Rating		
Brazil National Scale	brAAA/Negative/--	brAAA/Watch Neg/--
Senior Unsecured		
Brazil National Scale	brAAA	brAAA/Watch Neg
Recovery Rating	3(65%)	3(65%)
	To	**From**
Unidas S/A		
Issuer Credit Rating		
Brazil National Scale	brAAA/Negative/--	brAAA/Watch Neg/--
Senior Unsecured		
Brazil National Scale	brAAA	brAAA/Watch Neg
Recovery Rating	3(65%)	3(65%)
Downgraded; Outlook/CreditWatch Action		
	To	**From**
Vix Logística S.A.		
Issuer Credit Rating		
Brazil National Scale	brA+/Negative/--	brAA-/Watch Neg/--
Senior Unsecured		
Brazil National Scale	brA+	brAA-/Watch Neg
Recovery Rating	3(60%)	3(60%)