MOODY'S
RATINGS

Rating Action: Moody's Ratings downgrades Frigorifico Concepcion S.A.'s rating to B2; rating under review for downgrade

25 Oct 2024

New York, October 25, 2024 -- Moody's Ratings (Moody's) has downgraded Frigorifico Concepcion S.A.'s corporate family rating to B2 from B1. The rating is under review for further downgrade. Previously, the outlook was stable.

RATINGS RATIONALE

The downgrade of Frigorifico Concepcion S.A.'s (FriCon) rating to B2 from B1 reflects higher refinancing and liquidity risk stemming from the company's increased reliability on short term debt to fund its growth-related negative free cash flow, with limited access to long-term financing to extend the maturity of its obligations. Additionally, to preserve cash, the company will likely need to continue to slow growth of its slaughtering activity at least through 2025, which in turn will keep leverage metrics higher for longer, until the company is able to gradually decrease debt levels and increase internally generated cash flow.

The rating is under review for further downgrade as we assess the risk of additional liquidity drains, the refinancing risk associated with short-term debt, and the potential for bond repurchasing at distressed levels. During this review, we will examine whether the company can substantially reduce its cash burn, demonstrating strong operational performance and access to local financial institutions and domestic capital markets.

FriCon's reliance on short-term financing has raised its refinancing risk and heightened its financial strategy's inherent risk. As of June 30, 2024, FriCon had $49.3 million in cash and $210 million in short-term debt, mostly from bank credit lines for working capital ($58 million as of September 2024 according to its operational update in October 2024). FriCon generated $240 million in negative free cash flow as of LTM June 2024, mainly because of $253 million working capital requirements which resulted in $187 million in negative cash from operations, which was largely funded by a $161 million long term facility granted by Bank of America (BofA). During our review, we will assess the company's ability to improve operating cash flow that in turn would lower liquidity pressures. In this regard, the company's ability to deliver higher EBITDA from operations will be key for reducing cash burn, as well as a gradual reduction in working capital requirements.

The temporary qualified opinion given by its new external auditor, PricewaterhouseCoopers (PwC), for the fiscal year 2023 financial statements – which was subsequently replaced with an unqualified opinion on May 28th, 2024 – harmed investors' perception of the company. The rating action reflects our view that this will likely limit the company's ability to access long-term cross-border capital markets until they regain the markets' confidence.

It's worth noting that during 2024 FriCon has successfully refinanced its short-term debt obligations by using local capital markets and financial institutions. The company issued three local bonds in Bolivia totaling $65 million with 3-year terms and 6.2%-6.6% coupons. Additionally, it increased its term loan facility with BofA by $81 million, reaching a total of $161 million with an interest rate of SOFR + 5.5%. To boost liquidity, FriCon reduced its slaughtering activity in mid-2024, particularly in Brazil.

FriCon has enhanced its financial transparency by successfully completing its 2023 PwC and forming a new independent audit committee to improve corporate governance starting mid-2024. Additionally, the company has been providing interim quarterly financial reviewed by PwC for 2024. The Audit Committee, composed of independent members, will report to the Board and work with auditors and management to oversee financial reporting, internal controls and auditing. The committee will ensure financial accuracy, risk management, and regulatory compliance. These changes underscore the importance of gradually introducing governance measures that build investor trust.

The rating of FriCon continues to be supported by its leading position in the production and sale of fresh beef and pork, with regional diversification of production through facilities located in Paraguay, Bolivia and Brazil, which in turn supports the company's access to a diversified pool of export markets. The rating also incorporates the company's ability to significantly increase revenues through expansion of processing capacity and strategic acquisitions since 2020, while at the same time maintaining strong profitability aided by a good operating environment in Latin America, particularly in Paraguay, where the company benefits from a lower tax burden relative to regional peers.

FriCon's ratings are mainly constrained by its small scale relative to LatAm based peers with global operations. This risk is partially offset by the diversification provided by the company's export revenue. In this regard, FriCon's credit profile would benefit from a longer track-record as it continues to ramp up new beef and pork operations in Brazil and Bolivia in 2025-2026. Also constraining the rating is the company's exposure to the cyclical nature of the protein industry and overall volatility of protein prices, particularly because of the concentration in beef, which is the company's main protein in terms of revenue today, because EBITDA and working capital requirements may suffer significantly in response to a sudden rise in cattle costs.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATING

The rating is unlikely to be upgraded given the review for downgrade process. The rating would be confirmed if FriCon is able to deliver a substantial reduction its cash burn, demonstrating strong operational performance and access to local financial institutions and domestic capital markets to refinance debt maturities and lower liquidity risk.

The rating could be downgraded if the rating review process determines there is an increase in the risk of liquidity drains and refinancing risk associated with short-term debt, and the potential for bond repurchasing at distressed levels. The rating could be downgraded if FriCon's liquidity worsens, such as facing refinancing restrictions on short-term debt.

The principal methodology used in this rating was Protein and Agriculture published in August 2024 and available at https://ratings.moodys.com/rmc-documents/426548 . Alternatively, please see the Rating Methodologies page on https://ratings.moodys.com for a copy of this methodology.

Founded in 1997 and headquartered in Asunción, Paraguay, FriCon has a leading position in the production and sale of fresh beef and pork in Paraguay, Bolivia and Brazil, with a diversified portfolio of clients around the world. Since 2017, FriCon has also incorporated industrialized product lines such as burgers, premium burgers, meatballs and sausages. As of LTM Jun-24, around 52% of revenues were derived from exports to 37 countries through its plants in Paraguay, Bolivia and Brazil, and the remaining balance were sales to the local markets.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on https://ratings.moodys.com/rating-definitions .

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