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Rating Action: Moody's upgrades Avon's ratings to Ba3; outlook changed to stable

03 Mar 2021

New York, March 03, 2021 -- Moody's Investors Service, (Moody's) has today upgraded Avon Products, Inc. (Avon)'s corporate family rating and the ratings of the senior unsecured notes issued by Avon to Ba3 from B1. The outlook for the ratings was changed to stable from negative.

Ratings upgraded:

..Issuer: Avon Products, Inc.

...Corporate Family Rating, Upgraded to Ba3 from B1

...5.000% Senior Unsecured Notes due 2023, Upgraded to Ba3 from B1

...6.950% Senior Unsecured Notes due 2043, Upgraded to Ba3 from B1

Outlook:

...Outlook, changed to stable from negative

RATINGS RATIONALE

The upgrade of Avon's ratings to Ba3 from B1 follows several pieces of evidence over the past few months of stronger support from the parent Natura & Co Holding S.A. (Natura) to Avon. As an example, Natura has provided intercompany loans to Avon including a \$960 million to pay Avon's outstanding notes due 2022. The consent solicitation to include Natura as a guarantor of Avon's outstanding notes due 2023 granted in January 2021 that will become valid in the future, and a more centralized debt and cash management within the group are also practical examples of Natura supporting Avon. Accordingly, Avon's ratings should map closer to Natura's credit quality assuming that Natura will continue to provide support to Avon in case of need.

Avon's Ba3 ratings reflect primarily the close ties between the two companies and the expected support from Natura to Avon, given the company's relevance to the group. Natura has a stronger credit profile than Avon on a standalone basis and a proven track record of financial discipline. Natura's operating performance has been much stronger and more resilient than Avon's because of Natura's know-how in managing the direct selling network model and the group's strong digital capabilities and online presence. Natura has also shown a conservative approach to leverage and liquidity overtime, with a reported total debt/EBITDA of about 4.0x and BRL8 billion in cash at the end of September 2020, sufficient to cover debt amortizations through 2022 (all figures pro forma to the capital increase and debt payment concluded in November 2020). Avon's ratings also reflect Natura's size and scale as the fourth largest pure cosmetics group globally, its leading market position in several markets where it operates and good geographic diversification, although with a high concentration of operations in growing, but potentially volatile, developing markets.

The ratings are constrained mainly by the execution risk stemming from Avon's ongoing turnaround process, and its potential impact on Natura's consolidated credit metrics and liquidity. Avon's sales and earnings in the first nine months of 2020 were hurt by the coronavirus outbreak because of social distancing measures that have impaired the company's ability to recruit its sales force and hampered the ability of its representatives to meet customers and collect orders. We forecast that Avon's operating performance will recover in 2021-22, supported by the benefits from its integration with Natura, with leverage approaching 6.0x by the end of this period (3.0x excluding the intercompany loan with Natura), after peaking at 15.4x in the twelve months ended September 2020 (7.6x excluding the intercompany loan). However, execution risks remain high.

Avon contributed 52% of Natura's consolidated revenue in the twelve months ended September 2020. The company will become a significant source of cash generation to the group in the future as Natura collects top line and cost synergies, which it currently estimates at about \$300-400 million through 2024. Avon's operating performance was weak even prior to the pandemic outbreak, hurt by a continued decline in the number of

sales representatives. In the twelve months ended September 2020, Avon's revenue declined nearly 20% from 2019, reflecting the pandemic's impact. Profitability was also impaired, which led to a material increase in Avon's standalone leverage to 15.4x in the twelve months ended September 2020 from 6.7x in 2019. Natura on the other hand posted relatively stable results in constant currency in the twelve months ended September 2020 in all its preexisting businesses (Natura, The Body Shop and Aesop), leveraging on the group's omnichannel strategy, brand strength and leading market positions.

Natura was also able to reduce reported gross leverage to a pro forma 4x in Q3 2020 from 6.7x in the first quarter of the year and net leverage to a pro forma 1.5x from 3.9x in the same period, mainly because of a \$1 billion capital increase concluded in October 2020 that was used to fund the call option for Avon's \$900 million secured notes due 2022. Going forward, we expect Natura to maintain a conservative approach to leverage and liquidity, reporting net leverage between 1.5-2.0x and maintaining a solid liquidity profile to mitigate execution and liquidity risks for Avon.

LIQUIDITY

Avon's liquidity is adequate, although it deteriorated following a cash burn of approximately \$124 million in the twelve months ended September 2020. Liquidity comprises available cash of \$321 million as of September 2020 and a \$60 million availability under a revolving credit facility maturing in 2022 provided by Natura's financing entity. The \$960 million intercompany loan and the revolving credit facility to Avon reduced the risks associated with cash burn at Avon. Avon has around \$1 billion in debt maturing in 2021, predominantly the intercompany loan provided by Natura, which we expect the company could roll-over partly or fully.

Natura's liquidity is currently strong, backed by BRL8.0 billion (\$1.4 billion) in available cash at the end of September 2020, enough to cover debt amortizations through 2022 and investments required to integrate Avon's business. We believe refinancing risks are low for Natura given the company's longstanding relationship with Brazilian and international banks and access to both the international and local capital markets. We also expect Natura to pursue liability management initiatives to lengthen its debt amortization schedule and equalize the group's capital structure in the next months, and to reduce cash needs during the execution of the turnaround process of Avon.

RATING OUTLOOK

The stable outlook reflects our view that despite the high execution risks on Avon's turnaround process, Natura would provide financial support to the company, thus eliminating immediate liquidity and leverage risks.

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

Additional positive pressure on the ratings could develop in case there is a successful execution of Avon's turnaround initiatives leading to material operating performance improvement, with EBITA margin approaching 10%, Moody's-adjusted gross Debt/EBITDA improving to below 4.0x (from 15.4x in the twelve months ended September 2020) on a sustained basis, and materially positive free cash flow on a sustained basis. A sustained improvement in Natura's credit metrics or credit profile could also translate into additional positive rating actions for Avon.

The ratings could be downgraded in case of weaker perceived support from Natura to Avon, or if Natura fails to restore Avon's operating performance, such that Natura's credit metrics or credit worthiness deteriorate. Natura adopting financial policies that are detrimental to Avon's creditors, such as large cash upstreaming, would also lead to negative rating actions for Avon.

The principal methodology used in these ratings was Consumer Packaged Goods Methodology published in February 2020 and available at https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_1202237. Alternatively, please see the Rating Methodologies page on www.moody.com for a copy of this methodology.

Avon is a global beauty product company and one of the largest direct sellers with around five million active representatives. Avon's products are available in over 70 countries and are categorized as color cosmetics, skin care, fragrance, fashion and home. Following the completion of the acquisition in January 2020, Avon is now a fully owned subsidiary of Natura. Avon generated about \$3.8 billion in revenue and \$121 million in EBITDA (Moody's-adjusted) in the twelve months ended September 2020.

Natura & Co is the fourth largest pure cosmetics group globally, with presence across 100 countries and in the skincare, haircare, body care, men care, fragrances, color, fashion and home segments. The company has a

leading market position in several markets, with a particular focus on emerging markets such as Brazil, other Latin American countries and Russia, and operates through a multi-channel strategy through its four brands Avon, Natura, The Body Shop and Aesop. In the twelve months ended September 2020, Natura &Co reported \$7.2 billion in revenues and EBITDA margin of 9.5%.

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 at: https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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