FitchRatings

RATING ACTION COMMENTARY

Fitch Revises Ambipar's Outlook to Positive; Affirms IDR at 'BB-'

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Fitch Ratings - Rio de Janeiro - 26 Sep 2024: Fitch Ratings has affirmed Ambipar Participações e Empreendimentos S.A.'s (Ambipar) Long-Term Foreign Currency and Local Currency Issuer Default Ratings (IDRs) at 'BB-'. Fitch has also affirmed the National Long-Term Rating (NLTR) of Ambipar and its subsidiaries Emergência Participações S.A. (Emergência) and Environmental ESG Participações S.A. (Environmental) at 'AA-(bra)'.

Fitch has affirmed Ambipar Lux S.a.r.l.'s senior unsecured green notes (guaranteed by Ambipar and its rated subsidiaries) at 'BB-'and the NLTR of the senior unsecured debenture issuances at 'AA-(bra)' of Ambipar and its rated subsidiaries. The Rating Outlook for the corporate ratings was revised to Positive from Stable.

The Positive Outlook reflects Fitch's expectation that Ambipar will successfully implement its ongoing deleveraging strategy by focusing on organic growth, reducing debt, and improving operating efficiency. Strong performance during the first half of 2024 further supports the company's credit profile and deleveraging capacity.

Ambipar's ratings reflects its solid position in the environmental services industry, growth potential, and geographic revenue diversification. The company benefits from a positive track record of contract renewals and reasonable margin protection from contractual cost pass-through mechanisms. The ratings are limited by high consolidated gross leverage and significant cash flow consumption by interest.

KEY RATING DRIVERS

Positive Strategy Change: Ambipar has implemented a new strategy to reduce capital intensiveness, improve its cash cycle, reduce working capital needs and focus on organic growth. This should allow the company to gradually achieve its deleveraging goals. Fitch expects Ambipar to reduce indebtedness by around BRL1 billion by the end of 2024 after concluding a sale lease back transaction on part of its fleet and using treasury shares for debt reduction. Fitch's base case also incorporates a prudent dividend policy with minimum upstream during the rating horizon.

Strong Business Model: Ambipar's business model includes service provisions in its two main operating segments: environment (mainly waste management and recovery) and response (mitigation of environmental damage from accidents). The environment segment (where the subsidiary Environmental operates) represents around 50% of the revenue and benefits from agreements with an average duration of five years and low contractual exposure to volume risk.

The response segment (where the subsidiary Emergência operates) corresponds to around 50% of revenue and is supported by contracts lasting around three years, which are renewable. Approximately 25% of this revenue comes from subscriptions, and the remainder is related to the number of occurrences. The company's current strategy, focused on organic growth, reduces its exposure to acquisition execution risks.

Geographic Diversification: Ambipar's international activities are mainly concentrated in low-risk countries in Latin America, in addition to North America and Europe, which represent, respectively, around 15%, 25% and 5% of its revenues. The record of contract renewals, at above 95%, reflects the reduced competition with similar geographic coverage and service provision, which gives the company a competitive advantage. The strategy is to work mainly with private clients and expand its operations based on complementary services, under an evolving industry, with low penetration, high competitiveness and important growth potential.

Moderate Profitability: Fitch expects Ambipar's EBITDA margins to improve to around 30% compared to 27% presented in 2021-2023, as the company continues to benefit from gains of scale and capture synergies from acquired companies in the past. The expenses associated with the fleet rental should reduce the potential margin expansion, despite some cost savings (e.g. fleet maintenance). Approximately 70% of the cost and expense structure is variable and mostly accounts for personnel, which allows greater flexibility to adjust and protect margins in scenarios of weak business demand. Service provision contracts incorporate the pass through of payroll and other non-manageable costs variations.

Increasing EBITDA: The base scenario considers increases in Ambipar's EBITDA to BRL1.7 billion in 2024 and BRL1.8 billion in 2025, from BRL1.3 billion in 2023, supported by business expansion and higher efficiency. Cash flow from operations (CFFO) should reach around BRL400 million and BRL500 million in the respective years, still negatively impacted by high interest payments. Estimated investments range from

BRL450 million to BRL500 million in the two-year period, resulting in negative FCF close to BRL50 million in 2024 and BRL80 million the following year.

High Gross Leverage to Decline: Fitch expects Ambipar to move its gross debt/EBITDA ratio to more conservative levels. Fitch projects that gross leverage will be 4.6x at the end of 2024, with around 4.0x or below in 2025 onwards, as the company expands its EBITDA generation and uses part of its cash to repay debt. Net financial leverage has been moderate, with Fitch's base case scenario considering a reduction to less than 3.0x in 2024 with gradual reduction thereafter. The high volume of debt should result on a modest interest coverage by EBITDA, below 2.5x until 2027.

Consolidated Approach: Fitch assesses Ambipar and its two subsidiaries on a consolidated basis due to the high legal ties between them, such as substantial guarantees and cross-default clauses in the group's financial obligations. This assessment is in accordance with Fitch's 'Parent and Subsidiary Linkage Rating Criteria'. Fitch also considers the strategic and operational incentives to be high for the holding company to support the two subsidiaries, if necessary. Both are important to the group's revenue and EBITDA, with broad growth potential and capturing synergies. Emergência and Environmental are managed in an integrated manner.

DERIVATION SUMMARY

Ambipar's credit profile is weaker than that of Aegea Saneamento e Participações S.A. (Aegea; BB/Stable). Both operate under long-term contracts, with relatively stable demand, although Aegea's business is more resilient. Aegea's EBITDA margins in the range of 50%-60% are higher than those of Ambipar (around 30%), although the geographic diversification of Ambipar's operations is superior, which strengthens its business model.

Ambipar's rating incorporates the expectation of a gradual increase in its operating cash generation, while Aegea's considers the important challenge of relevant investments and efficiency improvements in important recently incorporated assets. Aegea's financial profile presents moderate leverage due to the expectation of the company's strong investment cycle and should remain moderately higher to that of Ambipar throughout the rating horizon. Aegea's further demonstrated access to the debt market favors its financial flexibility.

The credit profile of Ambipar favorably compares to Waste Pro USA Inc (Waste Pro; B+/Stable) given its improved business model with more diverse geographical footprint and service provision, whereas Waste Pro is geographically focused on municipal solid waste collection in U.S. Southeast. Fitch expects both companies to achieve similar leverage levels.

KEY ASSUMPTIONS

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

--Average EBITDA margins close to 30% from 2024 to 2026;

--Average annual investments in the range of BRL460 million to BRL540 million from 2024 to 2026;

--Dividends of 25% of net income;

--No acquisitions;

--Buyback of BRL47 million in shares and sale of assets of about BRL700 million in 2024;

--Payment of acquisition obligations of BRL260 million in 2024 through the use of treasury shares (no cash disbursement).

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

--Net Debt/EBITDA below 3.0x and Gross Debt/EBITDA below 4.0x, sustainably;

--EBITDA margin sustained above 30%;

--Sustainably positive (CFFO-Capex)/Debt indicator.

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

The Outlook will be revised back to Stable if the sensitivities for an upgrade are not achieved.

In addition, the following sensitivities would lead to a downgrade:

--Net Debt/EBITDA above 4.0x and Gross Debt/EBITDA above 5.0x, sustainably;

--EBITDA interest coverage ratio below 1.5x, sustainably;

--Weakening of liquidity profile with refinancing risks increase;

--Deterioration of profitability with EBITDA margins below 22%.

LIQUIDITY AND DEBT STRUCTURE

Strong Liquidity: Fitch believes that Ambipar will maintain robust liquidity, with a consolidated cash balance above BRL2.5 billion, and diversified access to funding sources in the coming years. At the end of June 2024, the group had a strong cash balance and equivalents of BRL 3.9 billion, compared to short-term debt of BRL766 million, and Fitch's expectation of slightly negative FCF in 2024. The agency assumed Ambipar to use part of its liquidity position along with around BRL700 million in asset sales and BRL260 million in treasury shares to reduce indebtedness.

Ambipar's consolidated total debt, adjusted for acquisition obligations, was BRL 9.1 billion at the end of June 2024, which mainly consisted of notes (41%), debentures (30%) and working capital (19%). The parent company's debt was BRL1.2 billion (mainly debentures), guaranteed by its subsidiaries.

ISSUER PROFILE

Ambipar primarily provides environmental services in Brazil but also in the rest of Latin America, the U.S., Canada and the UK. It operates in two main segments: response (mitigating and preventing environmental damage from accidents) and environment (managing and recovering industrial waste from private clients).

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.

MACROECONOMIC ASSUMPTIONS AND SECTOR FORECASTS

Click here to access Fitch's latest quarterly Global Corporates Macro and Sector Forecasts data file which aggregates key data points used in our credit analysis. Fitch's macroeconomic forecasts, commodity price assumptions, default rate forecasts, sector key performance indicators and sector-level forecasts are among the data items included.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Ambipar Lux S.a.r.l.				
senior unsecured	LT	BB-	Affirmed	BB-
Environmental ESG Participacoes S.A.	Natl LT	AA-(bra) Rating Outlook Positive	Affirmed	AA-(bra) Rating Outlook Stable
senior unsecured	Natl LT	AA-(bra)	Affirmed	AA-(bra)
Ambipar Participacoes e Empreendimentos S.A.	LT IDR	BB- Rating Outlook Positive	Affirmed	BB- Rating Outlook Stable
	LC LT IDR	BB- Rating Outlook Positive	Affirmed	BB- Rating Outlook Stable
	Natl LT	AA-(bra) Rating Outlook Positive	Affirmed	AA-(bra) Rating Outlook Stable
senior unsecured	Natl LT	AA-(bra)	Affirmed	AA-(bra)

Emergencia Participacoes S.A.	Natl LT AA-(bra) Rating Outlook Positive Affirmed		AA-(bra) Rating Outlook Stable
senior unsecured	Natl LT AA-(bra) Affirmed		AA-(bra)

VIEW ADDITIONAL RATING DETAILS

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PARTICIPATION STATUS

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APPLICABLE CRITERIA

National Scale Rating Criteria (pub. 22 Dec 2020)

Parent and Subsidiary Linkage Rating Criteria (pub. 16 Jun 2023)

Corporate Rating Criteria (pub. 03 Nov 2023) (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), v8.1.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Ambipar Lux S.a.r.l.	EU Endorsed, UK Endorsed
Ambipar Participacoes e Empreendimentos S.A.	EU Endorsed, UK Endorsed

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The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. For more details on sector-specific best- and worst-case scenario credit ratings, please see Best- and Worst-Case Measures under the Rating Performance page on Fitch's website.

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