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Research Update:

Minerva S.A. 'BB' Ratings Affirmed On Announced Acquisition Of Marfrig's Plants; Outlook Still Stable

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Rating Action Overview

- On Aug. 28, 2023, Minerva S.A. announced it had acquired 16 plants and one distribution center from Marfrig Global Foods S.A. (BB+/Stable/--) for R$7.5 billion, of which R$1.5 billion was paid upon announcement. Minerva will pay the rest once the transaction is concluded.
- We forecast debt to EBITDA to peak slightly above 3x in 2024 with the closing of the transaction, but then quickly return to 2.5x in 2025 and below 2.5x afterward, when the company will likely resume a higher dividend payout.
- On Aug. 30, 2023, S&P Global Ratings affirmed its 'BB' global scale and 'brAAA' national scale issuer credit and issue-level ratings on Minerva.
- The stable outlook reflects our view that Minerva will be able to quickly improve leverage after it peaks in mid-2024, and will be able to keep debt to EBITDA below 3x on a consistent basis, benefiting from discretionary dividend payments, favorable industry conditions in South America, and strong operational track record of asset integration.

Rating Action Rationale

Minerva will continue to grow its scale and will add lamb operations in Chile. With the acquired assets, Minerva will increase its slaughtering capacity by 44%. The assets will be fully integrated by the end of 2024, and will include Minerva's entrance into production in Chile, where it previously only had a commercial base. Higher volumes will dilute fixed costs, with potential operating synergies reaching 200 basis points (bps). This, along with favorable cattle availability in Brazil, Paraguay, and Argentina to a lesser extent, as well as improving global meat prices, should allow Minerva to operate with margins between 10% and 12%.

We highlight the company's track record of internal and acquisitive growth and its ability to improve margins of acquired assets. More importantly, Minerva has historically been more resilient and stable than industry peers, even considering only South American operations. On the other hand, the acquisition will increase the company's exposure to China through its larger capacity in Brazil, which adds event risk in case of trade barriers, as occurred in March 2023 and for a prolonged period in 2021.

Minerva's leverage has consistently been 2x-3x since 2020, despite recurrent small acquisitions and the recent increase in dividends to 50%-60% of previous year's net income. We think management is committed to keeping debt to EBITDA near 2.5x and using countercyclical measures such as cutting dividends to achieve this target. Also, the company will continue to generate free operating cash flow (FOCF) in excess of R$700 million this year and more than R$1 billion starting in 2024, which will help fund the acquisition. Funds from operations (FFO) to debt has been weaker and will likely remain close to 20% due to high interest payments and higher debt until next year.

Minerva historically has had a strong cash position. As part of the funding needs to complete the acquisition, JP Morgan Chase & Co. provided a committed credit facility of R$6 billion to Minerva valid for the next 18 months, which is in line with our view of Minerva's conservative approach toward holding cash to cushion against industry and market volatility.

The deal is subject to antitrust approvals, which should happen in the next three to 12 months. In our forecasts, we consider about 60% of revenue and EBITDA of the acquired assets in 2024 and full contribution in 2025, while all-cash payment occurs in 2024. We also estimate consolidated annual capital expenditures (capex) to grow to R$1.0 billion-R$1.1 billion and higher working capital needs to integrate all assets.

Outlook

The stable outlook reflects our view that Minerva will be able to quickly improve leverage after it peaks in mid-2024, and will be able to maintain debt to EBITDA below 3x on a consistent basis. It should benefit from the discretionary dividend payments, favorable industry conditions in South America, and its strong operational track record of integrating assets.

Downside scenario

We could lower the ratings on Minerva in the next 12-18 months if we see more stringent trade barriers, especially in China, hurting demand and distorting prices, while the company maintains high investments, working capital needs, and dividends. In this scenario, Minerva's debt to EBITDA would approach 4x and FFO to debt would be below 20%. Also, we could downgrade Minerva to the level of our rating on Brazil due to a weaker cash position if refinancing conditions tighten. Despite the company's good track record in past acquisitions, we could also lower the ratings if it faces integration issues that pressure margins and cash flows.

Upside scenario

An upgrade in the next few years could result from broader business scale and diversification, along with resilient EBITDA margins above 10% across industry cycles. It could also occur amid lower interest payments and FOCF of more than R$2 billion per year consistently, which would bring debt to EBITDA to below 2x and FFO to debt above 45%, despite dividend payments.

Company Description

Minerva is the largest beef exporter in Latin America by volume, accounting for about 20% of the regional beef trade thanks to the combination of its Brazilian operations with those of its fully-owned subsidiary Athena Foods, a Chile-based company that operates in Chile, Argentina, Colombia, Paraguay, and Uruguay, and which generates about half of Minerva's total revenues. With the acquisition, the company's share will reach close to 35%, and it will add a lamb production in Chile, which should complement its lamb facilities in Australia. Minerva is a public company traded on B3 (the São Paulo stock exchange). Currently, Minerva's largest shareholders are Saudi Agricultural and Livestock Investment Company (SALIC; a Saudi investment fund) with a 30.55% stake and VDQ Holdings S.A. (not rated; a family-owned holding company) with 22.36%. Although SALIC has the largest stake, VDQ controls the company, according to the shareholders' agreement between both parties until 2031.

Our Base-Case Scenario

Assumptions

- Brazil's GDP growth of 1.7% in 2023, 1.5% in 2024, and 1.8% in 2025.
- Argentina's GDP decline of 2.0% in 2023, and growth of 0.5% in 2024 and 2.0% in 2025.
- Australia's GDP growth of 1.4% in 2023, 1.2% in 2024, and 2.5% in 2025.
- Colombia's GDP growth of 1.4% in 2023, 2.0% in 2024, and 2.9% afterward.
- Paraguay's GDP growth of 5.0% in 2023, and 3.5% in 2024 and 2025.
- Uruguay's GDP growth of 1.0% in 2023, 3.0% in 2024, and 2.2% afterward.
- Volume growth in Minerva's current operations in Brazil of 1.0%-1.5% in 2023 and 5%-10% in 2024, due to cattle herd availability, with flat growth starting in 2025 as the cattle cycle reverts.
- Volume growth in Athena's current operations of 3.0%-5.0% in 2023 because of a better cattle cycle, particularly in Paraguay and Uruguay.
- Inorganic volume growth of about 45%, to be fully incorporated starting in 2025, given that we expect that the closing of Marfrig's deal will occur in the second quarter of 2024.
- Inflation in Brazil of about 5.2% in 2023, 4.2% in 2024, and 3.8% in 2025.
- Inflation in Argentina of about 121% in 2023, 125% in 2024, and 75% in 2025.
- Inflation in Australia of about 6.0% in 2023, 3.8% in 2024, and 3.0% in 2025.
- Inflation in Colombia of about 11.4% in 2023, 4.3% in 2024, and 3.3% in 2025.
- Inflation in Paraguay of about 5.5% in 2023, 4.5% in 2023, and 4.0% in 2025.
- Inflation in Uruguay of about 7.4% in 2023, 6.5% in 2024, and 6.2% in 2025.
- Average reference cattle prices in Brazil at R$220–R$270 per arroba in 2023, but prices to vary across regions.
- Capex of R$700 million–R$800 million per year, plus about R$300 million for the newly acquired operations in the next few years.

- Dividend payouts of 25% of the previous year's net income in 2023 and 2024, returning to above 50% in 2025 and 2026.
- Cash outflow of about R$600 million for the acquisitions of lamb operations in Australia; and R$1.5 billion paid for Marfrig's assets in 2023 and R$6 billion at the closing of the deal in 2024.
- Newly contracted debt of R$1.5 billion after June 30, 2023, and R$6 billion in 2024, including the bridge loan to fund the acquisition.

Key metrics

Minerva S.A.--Forecast summary

Industry sector: Food & kindred products

	--Fiscal year ended Dec. 31--								
(Mil. R$)	**2019a**	**2020a**	**2021a**	**2022a**	**2023e**	**2024f**	**2025f**	**2026f**	**2027f**
Revenue	17,123	19,406	26,965	30,978	32,041	45,797	54,674	55,723	57,575
EBITDA (reported)	1,726	2,102	2,382	2,838	3,182	4,791	5,670	6,320	6,874
Plus/(less): Other	(3)	2	(5)	(71)	(71)	(71)	(71)	(71)	(71)
EBITDA	1,724	2,104	2,377	2,767	3,111	4,719	5,598	6,249	6,803
Less: Cash interest paid	(990)	(1,047)	(1,014)	(1,223)	(1,428)	(1,960)	(2,058)	(2,029)	(2,003)
Less: Cash taxes paid	--	--	--	--	(60)	(60)	(60)	(60)	(60)
Funds from operations (FFO)	733	1,057	1,363	1,544	1,624	2,700	3,480	4,160	4,739
Cash flow from operations (CFO)	1,155	2,201	1,659	2,244	1,499	2,101	3,040	3,887	4,511
Capital expenditure (capex)	242	327	468	764	700	1,000	1,200	1,200	1,200
Free operating cash flow (FOCF)	913	1,874	1,191	1,480	799	1,101	1,840	2,687	3,311
Dividends	--	138	603	328	164	338	980	1,711	2,126
Discretionary cash flow (DCF)	915	1,526	588	1,152	635	763	860	975	1,186
Debt (reported)	10,478	11,572	13,405	13,766	14,233	19,072	18,579	17,936	17,936
Plus: Lease liabilities debt	46	47	40	38	39	54	55	55	56
Less: Accessible cash and liquid Investments	(4,470)	(6,391)	(7,302)	(7,071)	(5,766)	(5,000)	(5,000)	(5,000)	(5,854)
Plus/(less): Other	193	188	223	329	285	322	396	396	396
Debt	6,247	5,415	6,365	7,063	8,791	14,448	14,030	13,387	12,534
Cash and short-term investments (reported)	4,470	6,391	7,302	7,071	5,766	5,000	5,000	5,000	5,854
Adjusted ratios									
Debt/EBITDA (x)	3.6	2.6	2.7	2.6	2.8	3.1	2.5	2.1	1.8
FFO/debt (%)	11.7	19.5	21.4	21.9	18.5	18.7	24.8	31.1	37.8
FFO cash interest coverage (x)	1.7	2.0	2.3	2.3	2.1	2.4	2.7	3.1	3.4
EBITDA interest coverage (x)	1.8	2.0	2.3	2.3	2.2	2.4	2.7	3.1	3.4
FOCF/debt (%)	14.6	34.6	18.7	21.0	9.1	7.6	13.1	20.1	26.4
DCF/debt (%)	14.7	28.2	9.2	16.3	7.2	5.3	6.1	7.3	9.5

Minerva S.A.--Forecast summary (cont.)

Industry sector: Food & kindred products

	--Fiscal year ended Dec. 31--								
(Mil. R$)	2019a	2020a	2021a	2022a	2023e	2024f	2025f	2026f	2027f
Annual revenue growth (%)	5.6	13.3	39.0	14.9	3.4	42.9	19.4	1.9	3.3
EBITDA margin (%)	10.1	10.8	8.8	8.9	9.7	10.3	10.2	11.2	11.8
EBITDA/cash interest (x)	1.7	2.0	2.3	2.3	2.2	2.4	2.7	3.1	3.4

All figures are adjusted by S&P Global Ratings, unless stated as reported. a--Actual. e--Estimate. f--Forecast.

Liquidity

We continue to view Minerva's liquidity as strong. Sources over uses of cash for the next 12 months remain above 1.5x, even considering the R$1.5 billion cash outflow related to the acquisition of Marfrig's assets, as well as somewhat higher capex and working capital required to integrate the new plants. Minerva has secured a R$6 billion bridge loan to fund the main portion of the acquisition, to be paid at the closing of the deal, which we expect to occur in the next 12 months, making this neutral to the liquidity analysis. We expect Minerva to raise new long-term debt, either in the local or international capital markets or from banks to replace the bridge loan. If this occurs, combined with the company's cash flow, it should continue to support liquidity. We also consider that Minerva has a well-established relationship with banks and a high standing in credit markets, given its solid operations and historical access to credit lines, as well as generally prudent risk management and the ability to absorb high-impact, low-probability events without refinancing.

Principal liquidity sources:

- Cash position of R$6.2 billion as of June 30, 2023;
- Cash FFO of about R$2.5 billion for the next 12 months from June 30, 2023, and about R$3.5 billion for the following 12 months; and
- New already contracted trade finance lines of R$1.5 billion after June 30, as well as the commitment of a R$6 billion bridge loan for our 24-month analysis.

Principal liquidity uses:

- Short-term debt of R$3.3 billion as of June 30, 2023;
- Working capital outflows of about R$500 million in the next 12 months from June 30, 2023, considering only a portion of the working capital needed for Marfrig's plants, and about R$1.2 billion for the following 12 months;
- Cash outflows of R$1.8 billion for the acquisitions of BPU, ALC, and the first installment for Marfrig's plants for our 12-month analysis, and R$6.1 billion for our 24-month analysis;
- Capex of about R$700 million for the next 12 months from June 30, 2023, including expansion and maintenance capex, and excluding the capex for Marfrig's plants, and about R$1.1 billion for the following 12 months; and
- Dividend payments of about R$250 million for the next 12 months from June 30, 2023, and about R$650 million for the following 12 months

Covenants

The company has acceleration covenants in its senior notes and local bonds that require net debt to EBITDA (excluding foreign exchange variation) lower than 3.5x. After the acquisition, we expect a cushion below 30% for its covenant clauses in 2023 and 2024, but above 30% in 2025.

Rating Above the Sovereign

Our global scale rating on Minerva is currently one notch above our 'BB-' foreign and local currency ratings on Brazil. With the acquisition, the company will generate 50%-55% of its revenue in the country, so we assume a hypothetical default scenario for Brazil to test Minerva's ability to continue paying its obligations. In our hypothetical scenario, Minerva passes the stress test especially because of the export nature of its business, with a large portion of its cash position in foreign currency. This, along with its low short-term debt maturities, allows it to withstand the impact of macroeconomic downturns such as a decline in domestic and export demand and higher cattle prices.

Issue Ratings - Recovery Analysis

Key analytical factors

The recovery rating of '4' (rounded estimate: 40%) reflects our expectation of an average recovery for the company's unsecured debt (30%-50%). The default scenario considers a payment default in 2028. This scenario considers a jump in cattle prices, pressures on demand in Brazil and other countries in South America where Minerva operates, disruptions in the global demand for protein, and supply imbalances that would affect international beef prices. We added R$7.5 billion of debt in this scenario. The subsidiary, Athena, has a limited debt amount, but if it increases, it could reduce the recovery prospects for Minerva. This is because the subsidiary doesn't guarantee the bonds at the parent's level and Athena would benefit from priority cash flows to pay down its debt. We value Minerva on a going concern basis, using a 5.0x multiple (the standard multiple for the agribusiness sector) applied to our projected emergence-level EBITDA of R$2.1 billion, with a stressed enterprise value of about R$10.3 billion.

Simulated default assumptions

- Simulated year of default: 2028
- EBITDA at emergence: R$2.1 billion
- Implied enterprise value multiple: 5.0x
- Estimated gross enterprise value at emergence: R$10.3 billion

Simplified waterfall

- Net enterprise value after 5% administrative costs: R$9.8 billion
- Priority and secured debt: R$437 million (export financing lines and secured loan agreement)

- Senior unsecured debt: R$21.7 billion
- Recovery expectation: 30%-50% for its unsecured debt (rounded estimate: 40%)

Ratings Score Snapshot

Issuer Credit Rating	BB/Stable/--
Business risk:	Fair
Country risk	Moderately High
Industry risk	Intermediate
Competitive position	Fair
Financial risk:	Significant
Cash flow/leverage	Significant
Anchor	bb
Modifiers:	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Strong (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile:	bb

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- 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 | 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
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013

- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed	
Minerva S.A.	
Issuer Credit Rating	BB/Stable/--
Brazil National Scale	brAAA/Stable/--
Minerva S.A.	
Senior Unsecured	brAAA
Minerva Luxembourg S.A.	
Senior Unsecured	BB
Ratings Affirmed	
Minerva S.A.	
Senior Unsecured	
BRL200 mil fltg rate deb due 05/15/2024	brAAA
Recovery Rating	4(40%)
BRL400 mil fltg rate 11a Emissao deb due 10/15/2026	brAAA
Recovery Rating	4(40%)
Minerva Luxembourg S.A.	
Senior Unsecured	
US$1.4 bil 4.375% nts due 03/18/2031	BB
Recovery Rating	4(40%)
US$500 mil 5.875% nts due 01/19/2028	BB
Recovery Rating	4(40%)

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.