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## Research Update:

# Alicorp S.A.A. 'BBB-' Corporate Credit Rating Affirmed, Outlook Remains Stable

**Primary Credit Analyst:**
Pablo Buch, Mexico City (52) 55-5081-4425; pablo.buch@spglobal.com

**Secondary Contact:**
Laura Martinez, Mexico City (52) 55-5081-4425; laura.martinez@spglobal.com

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## Overview

- As we had expected, Alicorp's financial indicators have improved due to a solid operating performance and active liability management which gradually reduced borrowing costs and total debt.
- We expect Alicorp's financial performance to continue benefitting from stable economic conditions in Peru and a recovery in volume sales and margins in its international and aquaculture business segments.
- We're affirming our 'BBB-' corporate credit rating on Peru-based packaged food maker.
- The stable outlook reflects our expectations that the company will maintain a moderate use of debt, and that any acquisition-based growth opportunities won't compromise its credit quality or liquidity position.

## Rating Action

On April 27, 2017, S&P Global Ratings affirmed its 'BBB-' long-term corporate credit rating on Alicorp S.A.A. The outlook remains stable.

## Rationale

The rating affirmation follows Alicorp's strengthening of its credit metrics throughout 2016, our view that its financial performance will continue to benefit from Peru's stable economic conditions, and our expectation of a gradual recovery in volume sales and margins in its international and aquaculture business segments. In our view, Alicorp has favorable cash flow generation prospects for the next two years, which coupled with moderate investment spending foreseen for the same period, should continue to support a further improvement in credit metrics. However, we don't discard the possibility that the company could pursue an acquisition-based growth strategy, potentially requiring external debt-like funding, resulting in incremental leverage.

Alicorp continues to focus on strengthening its highly renowned product portfolio through the launching of new products and formats and the integration of well-established brands. The company holds dominant market shares in most of its consumer goods product categories including laundry detergents and edible oils, which continue to represent close to 30% of total EBITDA. However, in our view, Alicorp has a smaller scale and global presence than those of global peers in a higher rating category, while it's moderately exposed to economies with a high-risk operating environment, such as Argentina and Ecuador (that together represent close to 20% of total revenues). These factors exacerbate the company's exposure to foreign exchange fluctuations and raw material price volatility.

We expect steady top-line growth and moderate price adjustments in Alicorp's consumer goods division and recovery of its animal nutrition business, which recently started to gain traction, to continue to support a moderate rise in margins in the next two years. This should temper the impact of the lower profitability of the company's Argentinean operation, which has yet to achieve break-even EBITDA and likely to remain pressured by a weak exchange rate and high inflation. We also expect low raw material prices and efficiencies in procurement and manufacturing to continue supporting Alicorp's overall profitability. As a result, we expect EBITDA margins to trend towards 13% over the forecasted period.

We expect Alicorp to continue to fund its working capital requirements and capital expenditures with internal cash flow. Although our base-case scenario doesn't consider acquisitions, given Alicorp's acquisitive track record, its credit metrics could exhibit volatility over our forecasted period. However, based on its favorable cash flow generation prospects and recent strengthening of its financial indicators, reflecting the company's debt reduction in 2016 by about PEN400 million, we believe Alicorp has more flexibility than in previous years to accommodate external financing to fund an acquisition-based growth strategy, as long as the company maintains a comfortable liquidity position and its debt to EBITDA remains below 3.0x.

Our base case assumes the following factors for 2017 and 2018:

- GDP growth in Peru of 3.5% and 3.8%, respectively, which will continue to bolster consumption, benefiting Alicorp's sales.
- Mid-single digit sales volume growth mainly driven by volume expansions in Alicorp's international and aquaculture business segments.
- Average price increases between 2% and 3%, primarily due to price adjustments and an improving portfolio mix amid the launching of new products and formats. We expect price adjustments in its Peruvian consumer goods division to be in line with our forecast for domestic inflation of 3.2% and 3.0% in 2017 and 2018, respectively.
- Mid-single digit revenue growth as a result of new product offerings in the consumer products segment and increasing demand for shrimp and salmon feed.
- Working capital requirements of PEN180 million and PEN215 million, respectively.
- Capex of about PEN220 million and PEN250 million, respectively, to support volume expansions and a new plant in Honduras.
- Dividend distributions in excess of 35% of previous year's net income.

Based on these assumptions, we arrive at the following credit metrics for 2017 and 2018:

- EBITDA margins between 12% and 13%;
- Debt to EBITDA of 1.4x and 1.1x, respectively;
- FFO to debt above 45%; and

- Discretionary cash flow (DCF) to debt of about 14.5%.

Our rating on Alicorp also incorporates Grupo Romero's 45.35% ownership stake in the company. In our view, Alicorp is a strategically important subsidiary of the group because it's a key driver of the group's long-term growth strategy and would be likely to receive support from its parent if necessary. Although we don't rate Grupo Romero, we view its credit profile as similar to Alicorp's stand-alone credit profile. Therefore, the rating is not constrained by the group's credit profile.

### Liquidity

Alicorp's liquidity remains adequate, in our view, because we expect sources of cash will continue to exceed uses by 1.2x in the next 12 months, and that this ratio will remain above 1.0x even if EBITDA were to decline by 15% from our current forecast.

Principal Liquidity Sources:

- Cash of PEN274 million as of December 2016; and
- FFO of about PEN704 million for 2017.

Principal Liquidity Uses:

- Short-term debt of PEN243 million as of December 2016;
- Working capital requirements including intra-year seasonal peaks of about PEN214 million for 2017;
- Capital expenditures of about PEN220 million for 2017; and
- Dividend payments of PEN120 million for 2017.

Our assessment of liquidity also incorporates the company's favorable standing in the global capital markets, its flexibility to reduce capex, and sound relationships with local and international banks. As of the end of 2016, Alicorp was in compliance with its incurrence covenant limitations and we expect it will maintain headroom of at least 30%.

## Outlook

The stable outlook reflects our expectations that Alicorp will maintain a moderate use of debt, and that any acquisition-based growth opportunities won't compromise its credit quality or liquidity position. It also reflects the company's favorable cash flow generation prospects and our expectation that the company will fund most of its investment requirements with its own resources. This should be reflected in EBITDA margins above 12%, debt to EBITDA below 2.0x, and DCF to debt above 15%.

### Downside scenario

A negative rating action could occur if the company pursues an aggressive expansion strategy that results in significant incremental debt, and/or if potential pricing pressures from increased competition and higher raw material prices push down EBITDA margins below 10% and its debt to EBITDA trends consistently above 3.0x. Additionally, we could lower the ratings if the company's liquidity tightens, which could occur if Alicorp increases the use of short-term debt to fund investments and growth plans.

### Upside scenario

An upgrade is unlikely in the next 12-18 months. However, a positive rating action could occur if Alicorp improves its scale of operations and geographic diversification while maintaining its credit metrics and liquidity position at current levels. Additionally, the company should demonstrate a longer-track record of maintaining financial discipline despite its expansion plans.

## Ratings Score Snapshot

Corporate Credit Rating BBB-/Stable/--

Business Risk: Satisfactory
- Country Risk: Moderately High
- Industry Risk: Low
- Competitive Position: Satisfactory

Financial Risk: Significant
- Cash Flow/Leverage: Significant

Anchor: bbb-

Modifiers
- Diversification/Portfolio effect: Neutral (no impact) Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Management and Governance: Fair (no impact)
- Comparable rating analysis: Neutral (no impact)

## Related Criteria

- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- Criteria - Corporates - Industrials: Key Credit Factors For The Branded Nondurables Industry, May 7, 2015
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013

- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

## Ratings List

Ratings Affirmed

| | |
|---|---|
| Alicorp S.A.A. | |
| Corporate Credit Rating | BBB-/Stable/-- |

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.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.