

Rating Action: Moody's assigns B3 rating to Pesquera Exalmar's senior unsecured notes; stable outlook

29 May 2018

New York, May 29, 2018 -- Moody's Investors Service (Moody's) assigned today a B3 rating to Pesquera Exalmar, S.A.A.'s (Exalmar) \$60.9 million senior unsecured notes due 2025. Proceeds from the notes were used to refinance existing debt. The outlook on the rating is stable.

RATINGS RATIONALE

Exalmar's B3 ratings incorporate primarily the company's vulnerability to climatic conditions and fishing quotas regulation; a pronounced cash flow seasonality; and its limited operating scale and modest business diversification compared to regional peers as well as other seafood and protein-industry companies. The rating also reflects the exposure to volatile volume and price trends of the commoditized global fishmeal and fish oil market. These credit negatives are to some extent offset by Exalmar's position as the third largest fishmeal producer in Peru, the world's leading fishmeal nation; a successful operating history in its current business configuration; and some revenue diversification from its direct human consumption business.

Exalmar's volumes and thus its cash flow critically depend on the level of the catch of anchovies, the company's main raw material, which varies with the total allowable catch set prior to each fishing season by PRODUCE, the Peruvian Ministry of Production. Anchovy catch levels vary because of changing climatic conditions, in particular by the El Niño or La Niña effects. The high presence of juveniles in anchovy biomass led to a low 2nd fishing quota in 2017 of 1.5 million metric tons (MT) and fishing bans in November-December 2017 which affected Exalmar's inventory levels in 2017 (0.6 thousand MT as of December 31, 2017). During January to March 2018 inventories recovered but were still low when compared to the year before. Exalmar's inventory as of March 31, 2018 were 20.5 thousand MT, down from 64.4 thousand MT a year before. We estimate that inventory levels will recover in 2018 as the 1st fishing season of the year was set at 3.3 million metric tons; more than double when compared to the last fishing season of 2017. In addition, according to the most recent report from Peru's federal climate agency ENFEN, seawater temperature in front of the Peruvian coast continues within normal levels. ENFEN estimates that in May-July some warm Kelvin waves could generate weak anomalies in seawater temperature. Nevertheless, it maintains its expectation that neutral conditions will remain with no alerts for a possible El Niño/La Niña event. As a result, we estimate that the next fishing season will be set around 2-2.5 million metric tons given this more stable environment.

The company's credit metrics in the 1Q18 were affected by low starting inventory levels in the year. Nonetheless, the higher fishing quota in the 1st season of the year combined with our expectation that normal seawater conditions will led to a stable 2nd fishing season will benefit Exalmar's operation in 2018. Exalmar's adj. debt/EBITDA was 6.4x as of March 2018 with adj. EBITDA margin of 17% over the twelve months ended March 2018. Absent severe weather conditions, we estimate adj. debt/EBITDA to decline below 4x by year-end 2018 and remain around 3.5x in 2019. Similarly, profitability will further improve with EBITDA margin recovering to 24%-25% in 2018-2019.

Exalmar's liquidity is negatively affected by cash flow seasonality caused by the working capital build-up that tends to occur during Peru's two anchovy fishing seasons in the second and fourth calendar quarters and the subsequent cash inflow when inventories are shipped in the first and third quarters. Exalmar typically funds these working capital needs with uncommitted credit facilities with local and international banks. In addition, the company has a \$20 million committed credit facility that is fully available. We note that the use of committed credit facilities is not a common practice in Latin America so we positively view Exalmar's actions to ensure a strong alternate source of liquidity.

Exalmar reported cash on hand of \$4 million as of March 31, 2018 that can cover only 13% short-term debt. However, short-term debt is comprised by working capital related debt that is secured by inventory and receivables. As a result, the company's cash on hand, inventory and receivables provide a 1x coverage of its short-term debt as of the same date. The company's lack of dividend payments and maintenance capex support its positive free cash flow over the twelve months ended March 31, 2018. Exalmar has a comfortable long-term debt maturity profile: \$110 million due 2020, \$23 million due 2022, and \$61 million due 2025.

The stable ratings outlook reflects our expectation that the company's profitability and credit metrics will improve absent any strong weather event that results in a decline on the fishing quota or cancellation of a fishing season.

An upgrade would require an improvement in the company's liquidity cushion to withstand adverse impacts on operations due to adverse weather conditions. An upgrade would also be dependent on the company's ability to generate positive cash flow while maintaining robust credit metrics on a sustainable basis with debt/EBITDA below 4.0 times.

A prolonged period of negative free cash flow generation with material additional external funding needs, for example because of the impacts of quotas cancellation, an abrupt deterioration of global fishmeal demand or anchovy supply would cause downward pressure on the ratings. An increase in adj. debt/EBITDA over 7.0 times for a prolonged period of time with no expectation of reduction in the medium term could also lead to a downgrade.

The principal methodology used in this rating was Global Protein and Agriculture Industry published in June 2017. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Founded in 1992, Pesquera Exalmar, S.A.A. is a Peruvian fishing company which produces fishmeal and fish oil used for indirect human consumption. In addition, Exalmar also sells fresh and frozen fish (mackerel, horse mackerel, giant squid, and mahi-mahi) for direct human consumption. Exalmar has a 6.7% assigned quota in the north-center of Peru and the ability to process third-party catch, which increases its overall participation in the market. This positions the company as the 3rd. largest fishing player in Peru in terms of processed anchovy. Exalmar is majority owned (71%) and controlled by its founder, Victor Matta Curotto, and the 29% balance is publicly traded in the Lima stock exchange. For the twelve months ended March 31, 2018, the company reported revenues of \$198 million.

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