

# RatingsDirect®

---

## Research Update:

# Pesquera Exalmar Downgraded To 'B-' From 'B' On Weaker Credit Metrics; Outlook Negative

### Primary Credit Analyst:

Pablo Buch, Mexico City; pablo.buch@spglobal.com

### Secondary Contact:

Luis Manuel M Martinez, Mexico City (52) 55-5081-4462; luis.martinez@spglobal.com

## Table Of Contents

---

Overview

Rating Action

Rationale

Outlook

Ratings Score Snapshot

Related Criteria And Research

Ratings List

## Research Update:

# Pesquera Exalmar Downgraded To 'B-' From 'B' On Weaker Credit Metrics; Outlook Negative

## Overview

- Volatile weather conditions and a delay in the opening of the first fishing season of 2016 have reduced fishmeal production volumes of Peru-based fishing company Pesquera Exalmar, resulting in low cash flow generation, weak liquidity, and high leverage metrics.
- We're lowering our corporate credit and issue-level ratings on Exalmar to 'B-' from 'B' and removed them from CreditWatch with negative implications.
- The negative outlook reflects the potential downgrade for the next 12 months if external factors continue to constrain Exalmar's production volumes and cash flow generation prospects, further eroding its liquidity.

## Rating Action

On Aug. 26, 2016, S&P Global Ratings lowered its corporate credit and issue-level ratings on Pesquera Exalmar S.A.A. to 'B-' from 'B' and removed them from CreditWatch negative, where we placed on June 16, 2016. The outlook is negative.

## Rationale

The downgrade on Exalmar reflects the decline in its cash flow generation given volatile weather conditions and a delay in the opening of the first fishing season of 2016 that have reduced fishmeal production volumes. The lower-than-expected cash flow is pressuring Exalmar's liquidity and constrains the company's capacity to reduce its high leverage. In addition, we consider that the lengthy unfavorable conditions in Peru's industry heighten Exalmar's vulnerability to external factors, which weakened its profitability metrics and other key financial indicators.

The issue-level rating incorporates the company's announcement that it will cap the tender offer on its senior unsecured notes due 2020 to \$30 million, which it would fund with a new secured debt. In our view, Exalmar's priority liabilities will continue to represent less than 15% of total adjusted assets even if the notes are validly tendered, which mitigates a potential structural subordination per our criteria.

Exalmar's business risk profile reflects the vulnerability to external factors such as weather conditions, the start of fishing seasons, and the quota approval process by Peruvian authorities. In addition, given that Exalmar has a limited scale of operations and is heavily dependent on production volumes along the Peruvian coast, in our view, the company has limited flexibility to withstand adverse dynamics beyond its control that could impair its performance.

Exalmar's profitability metrics have weakened from declining production volumes and somewhat lower fishmeal prices. Although the company's EBITDA margins remain above

the industry's average, Exalmar's five-year historical average return on capital of 4.5% is lower than that of its rated global peers.

Exalmar's financial risk profile remains highly leveraged, reflecting our expectation that leverage ratios will remain above 5.0x for the next couple of years despite an expected normalization of fishing conditions for upcoming seasons.

Our assessment continues to incorporate the potential for volatility in the company's cash-flow leverage ratios, as seen in the performance of recent quarters. For the 12 months ended June 30, 2016, Exalmar's adjusted debt-to-EBITDA ratio reached 8.1x, above our previous estimate of about 5.0x.

Our base-case scenario assumes the following factors:

- China's GDP growth of more than 6% in 2016 and 2017.
- Peru's GDP growth of 4% in 2016 and 2017.
- Consumer Price Index in Peru to remain close to 3.0% in the next couple of years.
- Exchange rate of PEN3.5 per \$1 in 2016 and PEN3.6 per \$1 in 2017. Exchange rate affects local currency costs (e.g. labor) due to the dollar-denominated revenue.
- Peru's real exports to increase by about 9.3% in 2016 and 4.4% in 2017, reflecting a recovery in commercial trade (from less than 1% in 2015).
- The company's production volumes to decline in 2016 following a delayed start of the first fishing season of the year, which led Exalmar to realize only 50% of the catch of its assigned quota (6.17% of 1.8 million tons) of 1.11 million. For 2017, we expect a recovery in fishmeal and fishoil production volumes.
- In light of improving weather and biomass reports, we expect global fishing quotas to gradually trend towards 2 million tons per fishing season.
- Exalmar's participation in the Global Quota for 2016 through owned quota and third-party purchases to remain in line with 2015 for a total market share of about 12%.
- Fishmeal prices to remain between \$1,550 and \$1600 per ton in 2016 and 2017.
- Fishoil prices in excess of \$1,800 per ton throughout the forecast period.
- Revenue growth about 8.5% in 2016 and 18.2% in 2017.
- EBITDA to decline in 2016 as a result of lower fishmeal prices for the forecasted period and reduced efficiency rates despite the sharp decline in fuel prices. (Labor and fuel represent approximately 50% of production costs (catch + processing)).
- Annual capital expenditures to remain close to \$12 million in 2016 and 2017.
- No dividend payments in 2016, and resuming at \$10 million starting in 2017.

Based on these assumptions, we arrive at the following metrics for 2016 and 2017, respectively:

- EBITDA margin of 16.5% and 23.5%;
- Debt to EBITDA of 9.4x and 5.9x;
- Funds from operations (FFO) to debt of 3% and 9.4%; and
- EBITDA interest coverage above 1.4x and 2.2x.

## Liquidity

We're revising our assessment of Exalmar's liquidity to weak from less than adequate because we now forecast sources-over-uses ratio to be a considerable deficit for the next 12 months due to sluggish production volumes following a long delay in the start of the first fishing season of the year and relatively low fishmeal inventories as of June 2016.

Principal Liquidity Sources:

- Cash and liquid investments of \$17.2 million as of June 2016;
- FFO of about \$12 million for the next 12 months; and
- Committed credit facility of \$20 million, of which \$15 million was available as of June 2016.

Principal Liquidity Uses:

- Debt maturities of \$33.3 million as of June 2016 mainly related to bank notes;
- Working capital outflows of \$6.3 million for the next 12 months;
- Maintenance capital expenditures of about \$7 million for the next 12 months; and
- Dividend distributions of about \$5 million.

Exalmar has a debt incurrence covenant that consists of a leverage ratio below 3.5x. Currently, the company is in breach of this limitation, and we expect this breach for the next 12 months. However, the financing documents include a provision under which Exalmar could still incur debt consisting of receivables financing. This financing has to be in connection with the company's working capital needs in an aggregate principal amount of no more than \$70 million or 14.5% of the company's consolidated assets. In our view, this provides Exalmar with a degree of flexibility to fund its operations.

All modifiers are neutral to Exalmar's anchor.

## Outlook

The negative outlook reflects a one-in-three chance of another downgrade within the next 12 months if external factors continue to constrain Exalmar's production volumes and cash flow generation prospects, further eroding its liquidity. This could be triggered by fishing quotas in the North Center region of less than 2 million tons per season or if delays in the opening of fishing activities continue. We could also lower the ratings if we deem the issuer's financial commitments appear to be unsustainable in the long term.

## Downside Scenario

### Upside Scenario

We could revise the outlook to stable in the next 12 months if a sustained recovery in production volumes strengthens Exalmar's liquidity position and key financial indicators, with a debt to EBITDA approaching 5.0x and an FFO to debt close to 20%. This could occur if improving weather conditions and biomass reports lead to an

annual fishing quota greater than 4 million tons while demand from China continues to support fishmeal prices above \$1,500 a ton.

## Ratings Score Snapshot

	To	From
<b>Corporate Credit Rating</b>	B-	B
<b>Business Risk</b>	Vulnerable	Weak
Country Risk	Moderately High	Moderately High
Industry Risk	Intermediate Risk	Intermediate Risk
Competitive Position	Vulnerable	Weak
<b>Financial Risk</b>	Highly Leveraged	Highly Leveraged
Cash Flow/Leverage	Highly Leveraged	Highly Leveraged
<b>Anchor</b>	b-	b
<b>Modifiers</b>		
Diversification/Portfolio effect	Neutral/Undiversified	Neutral/Undiversified
Capital structure	Neutral	Neutral
Financial policy	Neutral	Neutral
Liquidity	Weak	Less than Adequate
Management and Governance	Fair	Fair
Comparable rating analysis	Neutral	Neutral

## Related Criteria And Research

### Related Criteria

- Criteria - Corporates - Industrials: Key Credit Factors For The Agribusiness And Commodity Foods Industry - January 29, 2015
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers - December 16, 2014
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments - November 19, 2013
- General Criteria: Methodology: Industry Risk - November 19, 2013
- General Criteria: Group Rating Methodology - November 19, 2013
- Criteria - Corporates - General: Corporate Methodology - November 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions - November 19, 2013
- General Criteria: Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers - May 07, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers - November 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009
- General Criteria: Rating Implications Of Exchange Offers And Similar Restructurings, Update - May 12, 2009
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue -

April 15, 2008

## Ratings List

	Rating	
	To	From
Pesquera Exalmar S.A.A.		
Corporate Credit Rating		
Foreign and Local Currency	B-/Negative/--	B/Watch Neg/--
Senior Unsecured		
Foreign Currency	B-	B/Watch Neg

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](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.globalcreditportal.com](http://www.globalcreditportal.com) and at [spcapitaliq.com](http://spcapitaliq.com). All ratings referenced herein can be found on S&P Global Ratings' public Web site at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.

Copyright © 2016 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgment as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, [www.standardandpoors.com](http://www.standardandpoors.com) (free of charge), and [www.ratingsdirect.com](http://www.ratingsdirect.com) and [www.globalcreditportal.com](http://www.globalcreditportal.com) (subscription) and [www.spcapitaliq.com](http://www.spcapitaliq.com) (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at [www.standardandpoors.com/usratingsfees](http://www.standardandpoors.com/usratingsfees).

STANDARD & POOR'S, S&P and RATINGSDIRECT are registered trademarks of Standard & Poor's Financial Services LLC.