

Research Update:

Pesquera Exalmar S.A.A. Ratings Lowered To 'B-' From 'B' And Placed On CreditWatch Negative On Weak Liquidity

April 2, 2020

Rating Action Overview

- Exalmar's liquidity has weakened during the past few months due to lower cash flows, a concern given the current macroeconomic uncertainty and potential commercial risks in the markets where it operates due to COVID-19.
- We expect a contraction in global consumption including demand for fishmeal, while the company's logistics and distribution process of fishmeal and fish oil could be temporarily disrupted because it generates most of its revenue abroad particularly in China.
- On April 2, 2020, S&P Global Ratings lowered its global scale issuer credit and issue-level ratings on Peru-based fishing company to 'B-' from 'B' and placed them on CreditWatch with negative implications.
- The CreditWatch negative listing reflects our view that Exalmar could face increasing refinancing risks in the upcoming months, which could further dent the company's liquidity.

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Rating Action Rationale

The likely contraction in consumption, coupled with higher operating costs, could reduce Exalmar's EBITDA further. During 2019, Exalmar's EBITDA decreased due to lower catch volumes and higher-than-expected costs, caused by an unusual dispersion of the anchovy biomass. The company also incurred higher costs related to anchovy purchases to third parties, which represented about 51% of the total processed volumes, steepening the drop in the company's margins. As a result, EBITDA margin fell to 22% in 2019 from 36% in 2018. As Exalmar's profitability took a hit and working capital requirements increased, the company's liquidity deteriorated due to lower cash flows and increasing short-term debt to support its operations.

We expect the company's cash flows to continue taking a hit due to a global economic slowdown triggered by COVID-19, which would shrink fishmeal consumption. In addition, the potential disruption in global logistics and a slowdown in shipments to the company's main customers in

Asia, Americas, and Europe could erode Exalmar's top-line growth prospects. Such disruptive business conditions could also intensify working capital needs as inventory and receivables could increase beyond our current expectation, which could ratchet pressure on the company's liquidity.

Liquidity risks are increasing due to lower cash flows and constant short-term debt

requirements. As of December 2019, the company had about \$82 million in short-term debt maturities in relation to its working capital facilities. Our liquidity assessment on Exalmar incorporates its access to domestic short-term debt financing, although the global financing crunch could represent a liquidity concern if the company also encounters more restrictive financing conditions in the upcoming months. Therefore, potential threats to Exalmar's ability to refinance debt would result in a downgrade. One factor supporting the company's access to short-term financing are warrants, which are credit facilities secured by the company's fishmeal inventories.

Recovery in biomass and favorable fishing quotas could enhance the company's cash flows and

credit metrics. Exalmar's business reflects its vulnerability to external factors such as weather conditions, the timely start of fishing seasons, approval of the respective quotas, and international demand for its products. However, we expect the north-center quota related to the first season of 2020 to be around 2 million tons. We also expect Exalmar to reach a higher fishing share of the global quota through owned quota and third-party purchases that are to increase around 18%. Favorable fishing conditions could support the company's 2020 revenue, enhancing cash flows while operating efficiencies could stabilize costs, raising EBITDA and EBITDA margins to around 23%. As a result, we expect the company to post debt to EBITDA of around 4.2x for 2020 and 4.0x in 2021.

CreditWatch

We plan to resolve the CreditWatch listing once we have greater clarity on Exalmar's refinancing plans and plans to enhance its liquidity. The CreditWatch negative listing reflects a downgrade potential due to adverse financing conditions and a global lockdown that will reduce the demand for Exalmar's key products.

Company Description

Exalmar is a Peruvian fishing company engaged in the extraction processing, and commercialization of hydro-biological resources for direct and indirect human consumption. It produces fishmeal for the growth of bovines, sheep, and pigs, as well as for the development of fish farming and poultry; and fish oil, which is primarily used as fish feed in the aquaculture industry. The company also processes various fish species, such as horse mackerel, mackerel, giant squid, and mahi-mahi. Exalmar operates five plants of fishmeal and fish oil, and two frozen plants of processing hydro-biological products for human consumption.

Liquidity

We're revising our assessment of Exalmar's liquidity to weak from less than adequate because we expect a substantial cash deficit for the next 12 months. Our liquidity analysis also includes qualitative factors, such as our view that current market conditions and lower credit availability could pose higher risks to access capital, particularly to fund working capital requirements in the

next 12 months.

Principal Liquidity Sources:

- Cash and cash equivalent of \$3 million as of December 2019; and
- FFO of about \$38.5 million for the next 12 months.

Principal Liquidity uses:

- Short-term debt of \$101.8 million as of December 2019;
- Working capital requirements of about \$12 million; and
- Capex of around \$9.5 million for the next 12 months.

Covenants

Under its senior unsecured notes due 2025, Exalmar is subject to a maximum debt to EBITDA of 3.5x financial incurrence covenants. At the end of 2019, the company complied with this covenant. Moreover, under its \$108 million syndicated loan, Exalmar is subject to financial maintenance covenants, including consolidated leverage ratio of maximum 1.5x, maximum debt to EBITDA of 3.5x, minimum debt service coverage ratio of 1.2x, and minimum liquidity ratio of 1.0x. Exalmar didn't comply with one financial covenant for this loan; however, it obtained the waiver approval. At the end of 2019, it was in compliance with these financial covenants, and we expect the same trend in the next 12 months.

Ratings Score Snapshot

Corporate Credit Rating: B-/Watch Neg/--

Business risk: Vulnerable

- Country risk: Moderately high risk
- Industry risk: Intermediate
- Competitive position: Vulnerable

Financial risk: Highly Leveraged

- Cash flow/Leverage: Highly Leveraged

Anchor: b-

Modifiers

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

Stand-alone credit profile: b-

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- Criteria | Corporates | Industrials: Key Credit Factors For The Agribusiness And Commodity Foods Industry, Jan. 29, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Downgraded; CreditWatch/Outlook Action

	To	From
Pesquera Exalmar S.A.A.		
Issuer Credit Rating	B-/Watch Neg/--	B/Stable/--
Pesquera Exalmar S.A.A.		
Senior Unsecured	B-/Watch Neg	B

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