FitchRatings

Fitch Rates JSL's Proposed Reopening of Notes 'BB'

Fitch Ratings-Chicago-08 January 2018: Fitch Ratings has assigned a 'BB' rating to JSL Europe's proposed add-on issuance of USD175 million in a reopening of its US$325 million, 7.75% notes due 2024 to new and existing investors. The notes are unconditionally and irrevocably guaranteed by JSL S.A (JSL). The bond will not be guaranteed by Movida Participacoes S.A. (Movida - National scale rating A+(bra)/Stable Outlook), JSL's 65.6% owned car rental subsidiary. This subsidiary accounts for 28% of the company's consolidated EBITDA and 22% of its debt. Proceeds from these notes will be used for debt refinancing and for general corporate purposes. Fitch currently rates JSL's Long-Term Foreign and Local Currency Issuer Default Ratings (IDR) 'BB'/Stable Outlook. A full list of ratings follows at the end of this release.

JSL's ratings reflect its strong business profile, supported by a leading position in the Brazilian logistics industry and diversified and resilient portfolio of products. The company's cash flow generation has been improving despite the recession in Brazil.

Fitch's base case scenario projects that JSL's leverage ratio, as measured by FFO adjusted leverage will remain around 2.5x in the next two years. Fitch expects JSL to pursue managed growth for Movida Participacoes S.A and does not incorporate material dividends from this subsidiary in its projections.

KEY RATING DRIVERS

Prominent Market Position and Diversified Portfolio

JSL has a leading position in the Brazilian logistics industry with a diversified portfolio of services with relevant presence in multiple sectors of the economy. The company's main services include: supply chain management (40% of its gross revenue), car rental and fleet management (32%), dealerships (14%), passenger transportation (7%) and general cargo transportation (5%). JSL's strong market position, coupled with long-term contracts for most of its revenues, minimizes its exposure to more volatile economic cycles. The company's significant operating scale has made it an important purchaser of light vehicles and trucks, giving it a significant amount of bargaining power versus other competitors in the industry.

Solid Operating Cash Flow Generation

JSL has been efficiently managing its business growth and profitability during the recession period in Brazil. The integration of its business and cross-selling opportunities has supported growth and gains in scale. Between 2015 and the latest-12-month period (LTM) ended Sept. 30, 2017, JSL's net revenue increased by 21%, to BRL7.2 billion. During the same period, the company's EBITDA remained almost stable at BRL1.2 billion while its FFO rose to BRL2.5 billion from BRL1.4 billion. Excluding Movida, Fitch calculates that EBITDA was almost stable at around BRL806 million while FFO grew to BRL860 million from BRL587 million.

More Rational Capex Growth to Ease Pressure on FCF

On a consolidated basis, BRL2.8 billion of gross capital expenditures led to negative FCF of BRL390 million during the LTM ended Sept. 30, 2017. FCF is expected to remain negative in the range of BRL200 million to BRL300 million in the next two years. JSL has the flexibility to improve FCF by reducing growth capex, as most of its capital investments are geared toward increasing the size of its fleet/equipment and are linked to specific contracts. Considering only renewal capex, JSL's operating cash flow generation is sufficient to support these investments. Excluding growth capex, JSL generated BRL799million of positive FCF during LTM Sept. 30, 2017. Excluding Movida, gross capex was BRL566 million and FCF was negative at BRL13 million.

Moderate Leverage

JSL's leverage, as measured by FFO adjusted leverage, was 2.8x as of LTM Sept. 30, 2017. This FFO ratio is considered moderate to low for the rating category. Fitch does not expect a material reduction in the near term with leverage expected to be around 2.7x in 2017, declining to 2.4x by 2018, considering a rational growth at Movida. Fitch's calculation of EBITDA does not add-back the non-cash cost of the vehicles sold. As a result, leverage as measured by EBITDA is higher than leverage measured by FFO. In Fitch's base case, JSL's net debt-to-EBITDA ratio will remain around 4.0x to 4.5x in the next two years.

DERIVATION SUMMARY

JSL's ratings reflect its solid position in the Brazilian logistic industry with a diversified and resilient portfolio of services/products. JSL's large business scale allows an important negotiating power with the automobile manufacturers and it is a key competitive advantage. Given the nature of its business, Fitch believes JSL has an above-average ability versus its 'BB' rated peers to post

FCF generation, given its flexibility to postpone capital expenditures related to new vehicles (growth capex). The company's relatively higher leverage and weaker financial flexibility are key differentiators to Localiza Rent a Car S.A (Long-Term Foreign Currency IDR BB+; Long-Term Local Currency IDR BBB-; National Long-Term rating AAA(bra)).

KEY ASSUMPTIONS

Fitch's Key Assumptions within Our Rating Case for the Issuer
--Mid-single-digit revenue growth in 2017;
--FFO margins at around 32%;
--Net capex at around BRL750 million in the next two years;
--Cash balance remains sound compared to short-term debt;
--Dividends at 25% net income;
--No large-scale M&A activity.

RATING SENSITIVITIES

Future Developments That May, Individually or Collectively, Lead to Positive Rating Action:
--FFO-adjusted net leverage around 2.0x on a sustained basis;
--Solid and consistent operating results from its retail rent a car business (Movida), with FFO margin above 27%.

Future Developments That May, Individually or Collectively, Lead to Negative Rating Action:
--FFO-adjusted leverage consistently above 3.0x;
--Deterioration of sound liquidity compared to short-term debt, leading to refinancing risk exposure;
--Deterioration in used car sales in Brazil and/or in the coverage ratio fleet value/net value to below 1.0x;
--Large debt-funded M&A acquisition or entering into a new business in the logistics sector that adversely affects JSL's capital structure on a sustained basis or increases its business risk exposure;
--Secured debt relative to FFO above 2.0x could lead to a downgrade of the unsecured debt.

LIQUIDITY

Improved Liquidity: JSL's adequate liquidity position vis-a-vis its short-term debt obligations is a key credit consideration, with cash covering short-term debt by an average 1x during the last five years. JSL has a recurring need for debt refinancing, since its debt amortization schedule had been historically concentrated in the next three years. During the first nine months of 2017, JSL has issued over BRL3.8 billion in a series of debt instruments, including the BRL1.019 billion of cross-border bond issuance (USD325 million) due to 2024 and Movida's BRL400 million of local debentures due to 2022.

On a pro forma and consolidated basis, including recent debt issuances, JSL had BRL3.3 billion of cash and BRL2.4 billion of short-term debt as of Sept. 30, 2017. Excluding Movida's cash and short-term debt, JSL's cash-to-liquidity position is adequate with BRL2.3 billion of cash and BRL1.2 billion of short-term debt. JSL has BRL2.5 billion of debt coming due up until year-end 2018 (BRL1.4 billion, when excluding Movida). As of Sept. 30, 2017, JSL reported total debt of BRL8.7 billion. The company's debt profile is mainly composed of banking credit lines (29%), local debentures, promissory notes and CRA issuances (36%), FINAME and leasing operations (16%), bond issuance (12%) and others (7%). Currently, about 14% of JSL's debt is secured.

FULL LIST OF RATING ACTIONS

JSL S.A.
--Long-Term Foreign Currency IDR 'BB';
--Long-Term Local Currency IDR 'BB';
--National Long-Term Rating 'AA-(bra)';
--Local debentures issuance 'AA-(bra)'.

The Rating Outlook is Stable.

JSL Europe
--USD325 million senior unsecured notes due to 2024 'BB'.

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Date of Relevant Rating Committee: Sept. 5, 2017

Summary of Financial Statement Adjustments:
--Total debt was adjusted by net derivatives, floor plan and accounts payables referred to acquisitions.
--EBITDAR measures was adjusted by rental obligations from Movida.