Research Update:

BevCo Lux Sarl 'BBB' Rating Affirmed, Despite Relaxed Financial Policy At Aguila; Outlook Still Stable

December 20, 2019

PRIMARY CREDIT ANALYST

Mikaela Hillman
Stockholm
+ 46 84 40 5917
mikaela.hillman
@spglobal.com

SECONDARY CONTACT

Per Karlsson
Stockholm
(46) 8-440-5927
per.karlsson
@spglobal.com

ADDITIONAL CONTACT

Industrial Ratings Europe
Corporate_Admin_London
@spglobal.com

Rating Action Overview

- As of June 30, 2019, BevCo's loan to value (LTV) ratio stood at 13% (11% excluding preferred equity certificates from its parent), in line with the rating.
- We perceive that Aguila, the 100% owner of BevCo, has relaxed its financial policy and we think management will steer it's LTV ratio to a maximum of around 15%, rather than 10% previously.
- We continue to view BevCo's investment portfolio as concentrated, given that AB InBev accounts for 75%-80% of the portfolio value, and that the restricted shares currently still weigh on our liquidity assessment.
- We note as positive factors the restriction of the AB InBev shares lapsing in October 2021, Acorn's plan to merge and IPO two of its subsidiaries, which will improve the share of listed assets at Aguila, and AB InBev's improving credit quality.
- We are affirming our 'BBB' rating on BevCo Lux Sarl.
- The stable outlook reflects our expectation that the maximum LTV ratio for Aguila will not materially exceed 15%, and remain below 20% for BevCo.

Rating Action Rationale

We affirmed the rating on BevCo despite a somewhat more relaxed financial policy at its 100% owner Aguila Ltd. The affirmation primarily reflects our view that the somewhat more relaxed financial policy at Aguila is offset by positive developments in Aguila's portfolio. We now understand that management will steer the LTV ratio at Aguila to a maximum of about 15%, rather than 10% previously. At the same time, we view positively that the restriction of the shares in Anheuser-Busch InBev S.A./N.V. (AB InBev; A-/Stable/A-2) will lapse in October 2021, that the plan for Acorn to merge and IPO two of its subsidiaries will improve the share of listed assets, and that AB InBev's credit quality has been improving.

We expect that BevCo will continue to be the most important investment vehicle in the Aguila group, incorporated only to carry out the group's investment strategy. BevCo is fully owned, controlled, and consolidated by Aguila. About 70%-75% of Aguila's assets are located in BevCo, including the largest asset, the 5% stake in AB InBev. We view Aguila's group credit profile at 'bbb' and we continue to rate BevCo at the same level, adding one notch to our stand-alone credit profile assessment of BevCo. We expect Aquila to support BevCo under all foreseeable events.

Our assessment on Aguila reflects a higher level of diversity compared with Bevco. Aguila's investment position is in line with that of other investment holding companies with satisfactory business risk profiles, albeit in the lower end. Aguila has net assets that exceed its investment in BevCo, therefore AB InBev constitutes between 50% and 60% of its assets, versus 79% for BevCo, as of Sept. 30, 2019. The three largest assets constituted 70% of Aguila's portfolio versus 98% for BevCo. Besides the stake in AB InBev, the portfolio is very diversified because typically all investments, except the $1.5 billion investment in Acorn, are below $1 billion in value. We also see a potential positive development in Aguila's portfolio liquidity in 2020 and 2021, partly from the plan for Acorn to merge and IPO two of its subsidiaries, Jacobs Douwe Egberts Group (BB/Positive/--) and Peet's Coffee (not rated), and partly because of the restriction of AB InBev shares that lapses in 2021, which will be transformational for the holding company's liquidity. On the negative side, we view the group's structure as fairly complex, and note material intercompany transactions, as disclosed in BevCo's financials.

The rating on BevCo depends heavily on AB InBev's performance. We continue to consider BevCo's portfolio as highly concentrated and exposed to AB InBev's performance, given that AB InBev accounts for 75%-80% of BevCo's total portfolio value. AB InBev's share price has been very volatile over the last two years. The portfolio's high concentration suggests that BevCo's LTV and cash flow adequacy ratios will correlate more strongly with AB InBev's share price and dividend payments to BevCo than with those of its other investments, such as Inmobiliaria Colonial (BBB+/Stable/A-2) and Acorn (not rated). The high concentration and restricted nature of the stake in AB InBev renders our view of BevCo's investment position as lower than that of peers, such as JAB Holding and Exor. A key strength of BevCo's portfolio is the high average credit profile of its investments, driven by AB InBev. AB InBev enjoys a strong competitive position as a global brewer, has a strong cash flow profile, and targets a reduction in leverage toward 2x reported net debt to EBITDA. We assess the average credit profile of the portfolio at 'BBB+', which is higher than usual for those investment holding companies we rate at 'BBB' or 'BBB-'.

We continue to see BevCo's portfolio as less liquid than that of peers. A constraint is the still illiquid nature of the AB InBev shares. Although almost all of BevCo's portfolio is comprised of listed assets, directly or indirectly, the majority of shares that BevCo holds in AB InBev are restricted and can therefore not be freely disposed until October 2021. This arrangement is unusual for an investment holding company; however, management has demonstrated that it can quickly use the restricted shares as collateral, and then use the proceeds for new investments. Management does not have the immediate ability to use the restricted shares in AB InBev to reduce debt if needed (though it may use the common shares), and so we don't treat them as fully liquid in our analysis. We believe this also restricts management's willingness to undertake major rotation or further diversification of the portfolio until 2021. That said, we believe management would not hesitate to use the shares to be in line with its stated financial policy.

Strong commitment to low financial gearing supports the ratings. BevCo's financial policy is a consequence of Aguila's group level financial policy, and we perceive management at the Aguila group level as very committed to its financial policy, despite the recent relaxation of the policy toward a maximum LTV of about 15% in case of a material decline in stock markets or for unique investment opportunities. We assess the LTV at Aguila today at 10%, and we also understand there is a track-record of keeping gearing at about 10% under normal circumstances. If share prices were to decline significantly over an extended period, we still expect management would sell shares in order to reduce net debt so as to maintain an LTV of about 15%. During 2019, management has sold assets of $490 million in total, including shares in Inmobiliaria Colonial, which supports its LTV value in the coming months.

BevCo will generate strong cash flow, notwithstanding lower dividends from AB InBev AB InBev has lowered significantly its dividend over 2019 and we now expect that BevCo will receive about €190 million in 2019, down from €287 million in 2018. In 2019, the drop will be compensated by higher dividend from Acorn of about €77 million, and we estimate a cash flow adequacy ratio of 7x-8x overall. We don't assume the same dividend from Acorn in 2020, and anticipate the ratios will therefore weaken further. Although the ratio is lower than in 2017 and 2018 (10x and 8x respectively), the ratio remains strong in our view and above that of many peers in our 'BBB' rating category, such as Wendel (0.9x forecast for 2019) and KOC (4.0-5.0x forecast for 2019). Exor's is, however, slightly higher at around 11x for 2019. Low interest and operating costs support BevCo's strong ratio. We notice, however, that most of the dividend received in 2019 has been used to pay dividend to Aguila, so it has not benefitted by any asset additions to the BevCo portfolio nor led to any meaningful debt reduction.

Outlook

The stable outlook on BevCo reflects our expectation that the maximum LTV ratio for Aguila will not materially exceed 15%, and remain below 20% for BevCo. We expect that management would take measures to maintain LTV if needed. We expect that BevCo's investment portfolio will continue to feature a large exposure to AB InBev over the medium term, and we also assume that BevCo will continue to be the largest and most important entity within the Aguila group, implying support to BevCo under all foreseeable circumstances.

Downside scenario

We could downgrade BevCo if the LTV ratio came under pressure, which could result from a sharp downward correction in equity markets, and if, at the same time and contrary to our expectation, the company did not take measures to prevent an increase in the LTV ratio. An LTV ratio above 15% for the Aguila group or 20% for BevCo for more than a few months would likely result in rating pressure, as would raising debt to fund shareholder-friendly measures, although we think the latter scenario is highly unlikely in the near term.

Upside scenario

We might raise the rating in the next 12-18 months if management is successful in meaningfully improving the diversification of BevCo's investment portfolio, while maintaining the LTV ratio. Upside would likely also depend on improved liquidity, namely through the lapse of the restrictions on shares in AB InBev, which is slated for October 2021.

Company Description

BevCo is an investment holding company ultimately owned by Santo Domingo Group. In June 2019, BevCo's portfolio value of about €8.9 billion included:

- AB InBev: The world's largest brewing company comprising eight of the 10 most valuable beer brands worldwide.
- Inmobiliaria Colonial: A eurozone real estate company with over 1.8 million square meters of primarily central business district office space in Madrid, Paris, and Barcelona. Total portfolio value is about €11.3 billion, market capitalization is about €5.8 billion, up from €3.6 billion at year-end 2018. BevCo owns 5.7% from 7.54% in Inmobiliaria Colonial following the sell-down in the third quarter of 2019.
- Acorn Holdings B.V. (not rated): The holding company of Jacobs Douwe Egberts and Keurig Green Mountain Inc. (not rated), a large pure-play Fast-Moving Consumer Goods coffee company and the leading single-serve coffee platform in the U.S., respectively, as well as Peet's Coffee (not rated).
- Upfield (B+/Stable/--): A global plant-based food spread business.
- The Kraft Heinz Company (BBB-/Negative/--): The fifth-largest food and beverage company in the world, held via a 3G Capital co-investment partnership.

Our Base-Case Scenario

- Dividends inflow of €190 million-€200 million for 2020.
- Low operating expenses of €2 million-€3 million.
- Interest expenses around €22 million-€27 million.
- No major acquisitions or disposals.
- Interests and management costs of €25 million-€35 million.
- Dividend paid from BevCo to Aguila of about €170 million.

	2018a	2019e	2020e
LTV (%)	17.5*	<15.0	<15.0%
Cash flow adequacy (x)	9.6	9.0-11.0	7.0-9.0

a--Actual. e--Estimate. LTV--Loan to value. *14.8% excluding preferred equity certificates.

Base-case projections

In our base case for 2019-2020, we expect BevCo will maintain an LTV ratio below 15%, in line with its leverage policy. We believe deviation, if any, will likely come from a drop in AB InBev's share price. As we perceive BevCo's management as committed to a strong balance sheet, we expect they will sell assets if needed to lower debt. We do note, however, the volatility of AB InBev's share price, and that BevCo's LTV ratio was above 15% in the first few months of 2019.

We anticipate healthy, albeit declining, cash flow adequacy. We expect BevCo's cash flow adequacy ratio will decline to 9x-11x in 2019, from 9.6x in 2018 and 13.0x in 2017, following lower dividend payments from AB InBev. In first-half 2019, BevCo paid €170 million of dividends to Aguila.

Liquidity

We assess BevCo's liquidity as strong, with a ratio of sources to uses of about 9x-11x in 2019 and 2020, since the company has a very limited amount of short-term debt and a large undrawn revolving credit facility (RCF), even if we stress dividend inflow with 50%. The first major debt repayment is slated for 2023 when the €800 million bond is due. We expect management to address the maturity well in advance of the maturity.

We believe BevCo's relationships with core banks are well established. We limit our assessment at strong, however, although the high cover ratio could warrant a higher assessment, given the high dependence on the financial performance of its main investee, AB InBev, which we see as a major restraining qualitative factor, as well as the restriction of share sales.

Principal Liquidity Sources

- Cash and cash equivalent of €12 million as of June 30, 2019.
- €1.48 billion undrawn RCF (we include only committed facilities with maturing beyond 12 months. The key facility amounts to €1.17 billion and is due 2024).
- Dividend and interest income over the next year of €200 million.

Principal Liquidity Uses

- Limited short-term debt (€6.5 million, including interest on debt securities over the next year) as of June 30, 2019.
- Interest and operating expense of €25 million-€35 million.
- Annual dividend payment of about €200 million-€250 million in 2019 and 2020.

Group Influence

BevCo is fully owned by Aguila, for which we assess a group credit profile of 'bbb'.

We consider BevCo a core subsidiary of Aguila. BevCo was incorporated to carry out the group's investment and financing strategy, and therefore essential to the group's strategy. We equalize our issuer credit rating on BevCo with our assessment of Aguila's group credit profile.

Issue Ratings - Subordination Risk Analysis

Our subordination risk analysis on BevCo's capital structure looks at potential structural subordination arising at the unsecured level from the existence of priority secured bank debt.

Capital structure

BevCo issued its first unsecured bond of €800 million on Feb. 9, 2018. The proceeds were used to repay part of its secured debt, and now constitute the largest part of BevCo's outstanding debt, which according to management was about €1.0 billion on June 30, 2019.

Analytical conclusions

In the capital structure mentioned above, the secured debt that we view as priority obligations will represent about 5% of the group's total outstanding debt, while the unsecured bond will count for the remainder. We conclude, on the basis that the priority ratio will be below 50%, that there is no notching of the unsecured debt at the BevCo level. We thus equalize the issue rating with our issuer credit rating on BevCo.

Ratings Score Snapshot

Issuer Credit Rating:	BBB/Stable/--
Business risk:	Fair
Country risk:	Very low
Industry risk:	Intermediate
Investment position:	Fair
Financial risk:	Modest
Cash flow/Leverage:	Modest
Anchor:	bbb-
Modifiers:	
Liquidity:	Strong (no impact)
Management and governance:	Satisfactory (no impact)
Comparable rating analysis:	Neutral (no impact)
SACP:	bbb-
Group credit profile:	bbb
SACP--Stand-alone credit profile.	

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: Methodology: Investment Holding Companies, Dec. 1, 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

Related Research

- Anheuser-Busch InBev Outlook Revised To Stable; 'A-/A-2' Ratings Affirmed; Oct. 31, 2019

Ratings List

Ratings Affirmed	
BevCo Lux Sarl	
Issuer Credit Rating	BBB/Stable/--
Senior Unsecured	BBB