FitchRatings

Fitch Downgrades Famsa's IDRs to 'C' on Proposed Exchange Offer

Fitch Ratings - Mexico City - 29 October 2019:

Fitch Ratings has downgraded Grupo Famsa, S.A.B. de C.V.'s Long-Term and Local and Foreign Currency Issuer Default Ratings (IDRs) to 'C' from 'B-'.

The downgrades follow Famsa's announcement of the launching of a tender offer to exchange its unsecured notes due in 2020 for secured notes due in 2024, which Fitch considers to be a distressed debt exchange (DDE) as per its DDE criteria. In Fitch's opinion, the offering imposes to bondholders of existing notes, a material reduction in terms of the existing 2020 notes, as the exchange will eliminate restrictive covenants and certain events of default included in the 2020 senior notes indenture for the bonds that are not tendered. The offering also proposes an extension of the notes' maturity date by five years, which Fitch sees as necessary to avoid a traditional payment default.

If the proposed tender offer is completed, the IDR will be downgraded to Restricted Default (RD). Subsequently, Fitch will re-rate Famsa's IDRs and raise them to a rating consistent with the company's post-exchange capital structure and risk profile, which would be likely in a low speculative rating range.

RATING ACTIONS

ENTITY/DEBT	RATING	RECOVERY	PRIOR
Grupo Famsa, S.A.B. de C.V.	LT IDR C Downgrade		B-
	LC LT IDR C Downgrade		B-
	Natl LT C(mex) Downgrade		BB(mex)
	Natl ST C(mex) Downgrade		B(mex)
senior unsecured	LT C Downgrade	RR4	B-
senior unsecured	Natl ST C(mex) Downgrade		B(mex)

Key Rating Drivers

Exchange Offer Qualifies as DDE: The exchange offer, if agreed, will constitute a DDE under Fitch's criteria, as existing bondholders face a material reduction in terms and conditions if they do not tender and the transaction is being undertaken to prevent a possible future default on the 2020 notes. Fitch believes alternative options to be limited. Fitch recognizes the positive impact that the proposed exchange would have on Famsa's liquidity and debt service capacity, given the proposed extended maturity date.

According to Fitch's DDE criteria, exchanges that are conducted to avoid insolvency or a traditional payment default and that imply a material reduction in terms are considered DDE. According to the criteria, a material reduction in terms includes an extension of maturity date and exchange offers that are accepted if the tendering bondholder also consents to indenture amendments that materially impair the position of holders that do not tender.

The existing USD140 million of 7.25% notes due 2020 will be exchanged for 9.75% notes due 2024 secured by Famsa Inc. ordinary shares. The exchange offer is subject to 80% participation in terms of the aggregate outstanding principal amount. Fitch will reassess Famsa's IDR after completion of the exchange offer.

Challenged Environment: Famsa has been pursuing a number of initiatives to improve its financial profile. However, the increasingly challenged competitive environment along with a still weak portfolio quality, have hindered these initiatives to take off and significantly improve consolidated liquidity, profitability and therefore reduce leverage, as originally expected. Management's exchange proposal reflects the company's willingness to restructure its financial debt.

Derivation Summary

Famsa is one of the main retailers in Mexico, offering durable goods and consumer services primarily to the middle and lower-middle segments of the Mexican population. Connected with the retail operations, Famsa also offers financial services to the customers who opt to purchase its products on credit, many of whom do not typically have access to other forms of financing. However, the company's high leverage recurring negative FCF and tight financial flexibility had place Famsa's rating in the 'B-' category, before the announced exchange.

Famsa is less geographically diversified than Grupo Elektra S.A.B. de C.V. (BB+/Stable) and Grupo Unicomer Company Limited (BB-/Stable), but it is well positioned in its influence area of northern Mexico. The company also has smaller scale in number of stores than Grupo Elektra and Grupo Unicomer, with 401 stores compared to more than 1,000.

From a financial risk profile view, the company has similar adjusted leverage than J.C. Penney (JCP, CCC+) and Rite Aid (B/Negative) with ratios above the 6.0x (calculated pre-IFRS 16). The three companies present neutral to negative FCF, but JCP and Rite Aid have stronger liquidity position than Famsa's. On the other hand, Famsa operates in Mexico and the prospects for the Mexican retail industry are stronger than in the U.S.

Compared with Latin American peers, the company maintains a weaker financial position than Elektra and Unicomer. Famsa's operating margins are lower than Unicomer's, while Elektra has the best operating margins of the three companies.

Key Assumptions

The proposed tender offer for its unsecured notes is completed as expected.

RATING SENSITIVITIES

The completion of the proposed exchange offer will lead to a downgrade of the Long-term IDRs to 'RD'. The IDR would be subsequently upgraded to a rating level reflecting the post-DDE credit profile.

Liquidity and Debt Structure

Weak Liquidity: As of Sept. 30, 2019, Famsa had MXN2.0 billion of cash and marketable securities (mostly at BAF). This compares with MXN4.9 billion of short-term debt, mainly composed by the large debt maturity of USD140 million (approximately MXN2.8 billion) due in May 2020.

Summary of Financial Adjustments

Gains on fixed asset sales and non-recurring income were deducted from the operating income. Financial Statements were adjusted to revert IFRS 16 effect.

ESG Considerations

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of 3. ESG issues are credit neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity.

Famsa has an ESG Relevance Score of 5 for Management Strategy due to the number of operational restructures that have occurred due to challenges the company has faced in implementing its strategy, which has a negative impact on the credit profile and is highly relevant to the rating in conjunction with other factors.

Famsa has an ESG Relevance Score of 4 for Governance Structure due to board effectiveness and ownership concentration, which has an unfavorable impact on the credit profile and is relevant to the rating in conjunction with other factors.

Famsa has an ESG Relevance Score of 4 for Group Structure given that the company presents a below average transparency of related-party transactions. This has a negative impact on the credit profile and is relevant to the rating in conjunction with other factors.

Famsa has an ESG Relevance Score of 5 for Financial Transparency due to a track record of material differences from audited financial statements and the company's reported figures. This has a negative impact on the credit profile and is highly relevant to the rating in conjunction with other factors.

For more information on our ESG Relevance Scores visit www.fitchratings.com/esg.

Additional information is available on www.fitchratings.com

FITCH RATINGS ANALYSTS

Primary Rating Analyst
Maria Pia Medrano Contreras
Director
+52 55 5955 1615
Fitch Mexico S.A. de C.V.
Blvd. Manuel Avila Camacho No. 88, Edificio Picasso, Piso 10, Col. Lomas de Chapultepec,
Mexico City 11950

Secondary Rating Analyst
Jose Vertiz
Director
+1 212 908 0641

Committee Chairperson
Alberto Moreno Arnaiz
Senior Director
+52 81 8399 9100

MEDIA CONTACTS

Elizabeth Fogerty
New York
+1 212 908 0526
elizabeth.fogerty@thefitchgroup.com

Applicable Criteria

National Scale Ratings Criteria (pub. 18 Jul 2018)
Country-Specific Treatment of Recovery Ratings Criteria (pub. 18 Jan 2019)
Corporate Rating Criteria (pub. 19 Feb 2019)
Distressed Debt Exchange Rating Criteria (pub. 06 Aug 2019)
Parent and Subsidiary Rating Linkage (pub. 27 Sep 2019)
Corporates Notching and Recovery Ratings Criteria (pub. 14 Oct 2019)

Additional Disclosures

Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Policy

DISCLAIMER

COPYRIGHT

but are not solely responsible for, the opinions stated therein. The individuals are named for contact purposes only. A report providing a Fitch rating is neither a prospectus nor a substitute for the information assembled, verified and presented to investors by the issuer and its agents in connection with the sale of the securities. Ratings may be changed or withdrawn at any time for any reason in the sole discretion of Fitch. Fitch does not provide investment advice of any sort. Ratings are not a recommendation to buy, sell, or hold any security. Ratings do not comment on the adequacy of market price, the suitability of any security for a particular investor, or the tax-exempt nature or taxability of payments made in respect to any security. Fitch receives fees from issuers, insurers, guarantors, other obligors, and underwriters for rating securities. Such fees generally vary from US$1,000 to US$750,000 (or the applicable currency equivalent) per issue. In certain cases, Fitch will rate all or a number of issues issued by a particular issuer, or insured or guaranteed by a particular insurer or guarantor, for a single annual fee. Such fees are expected to vary from US$10,000 to US$1,500,000 (or the applicable currency equivalent). The assignment, publication, or dissemination of a rating by Fitch shall not constitute a consent by Fitch to use its name as an expert in connection with any registration statement filed under the United States securities laws, the Financial Services and Markets Act of 2000 of the United Kingdom, or the securities laws of any particular jurisdiction. Due to the relative efficiency of electronic publishing and distribution, Fitch research may be available to electronic subscribers up to three days earlier than to print subscribers.
For Australia, New Zealand, Taiwan and South Korea only: Fitch Australia Pty Ltd holds an Australian financial services license (AFS license no. 337123) which authorizes it to provide credit ratings to wholesale clients only. Credit ratings information published by Fitch is not intended to be used by persons who are retail clients within the meaning of the Corporations Act 2001
Fitch Ratings, Inc. is registered with the U.S. Securities and Exchange Commission as a Nationally Recognized Statistical Rating Organization (the "NRSRO"). While certain of the NRSRO's credit rating subsidiaries are listed on Item 3 of Form NRSRO and as such are authorized to issue credit ratings on behalf of the NRSRO (see https://www.fitchratings.com/site/regulatory), other credit rating subsidiaries are not listed on Form NRSRO (the "non-NRSROs") and therefore credit ratings issued by those subsidiaries are not issued on behalf of the NRSRO. However, non-NRSRO personnel may participate in determining credit ratings issued by or on behalf of the NRSRO.

SOLICITATION STATUS

The ratings above were solicited and assigned or maintained at the request of the rated entity/issuer or a related third party. Any exceptions follow below.

Endorsement Policy

Fitch's approach to ratings endorsement so that ratings produced outside the EU may be used by regulated entities within the EU for regulatory purposes, pursuant to the terms of the EU Regulation with respect to credit rating agencies, can be found on the EU Regulatory Disclosures page. The endorsement status of all International ratings is provided within the entity summary page for each rated entity and in the transaction detail pages for all structured finance transactions on the Fitch website. These disclosures are updated on a daily basis.

Fitch Updates Terms of Use & Privacy Policy

We have updated our Terms of Use and Privacy Policies which cover all of Fitch Group's websites. Learn more.