S&P Global Ratings

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Research Update:

JSL's Stand-Alone Credit Profile Raised To 'b+' And National Scale Ratings To 'brAA' On Leverage Reduction After IPO

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Rating Action Overview

- JSL S.A. raised around R$700 million in an IPO, which will allow it to keep an active M&A strategy while maintaining leverage at manageable level. We now expect Brazil-based logistics provider to post debt to EBITDA at 3.5x-4.0x in the next few years.
- On Sept. 9, 2020, S&P Global Ratings revised upwards JSL's stand-alone credit profile (SACP) to 'b+' from 'b' and raised the national scale ratings to 'brAA' from 'brAA-'.
- We also affirmed our global scale rating at 'B+', now at the same level as the SACP, with no uplift from its controlling shareholder, Simpar S.A.
- Finally, we have assigned a stable outlook on the national scale rating and revised the global scale rating to stable from negative, reflecting the improved capital structure following the IPO.

Rating Action Rationale

JSL's IPO has reshaped its capital structure. The group's recent reorganization with the spin-off of its business raised JSL's leverage. Now, with the proceeds from the shares issuance, JSL has bolstered its cash position. And given our expectation of phased cash outflows for new acquisitions, we believe the company will maintain lower-than-expected leverage. We now forecast adjusted debt to EBITDA at around 4.0x at the end of 2020, compared with our previous expectation of 4.7x-5.0x. As a result, we revised upwards the company's SACP to 'b+' from 'b', raised our issuer credit and issue-level ratings on Brazilian national scale to 'brAA' from 'brAA-', assigned a stable outlook to the national scale rating, revised the global scale rating outlook to stable from negative, and affirmed the 'B+' global scale rating. This rating previously incorporated a one-notch uplift of potential support from its parent, Simpar (BB-/Negative) given the difference of two notches between JSL's SACP and the group credit profile. Given that the difference now narrowed to only one notch after we revised upwards JSL's SACP, we don't equalize the ratings on Simpar and JSL because we don't expect Simpar to support JSL under any foreseeable circumstances.

We believe the company will actively pursue M&A activity while maintaining adjusted leverage below 4x. JSL has historically expanded its portfolio by acquiring companies with complementary logistics/transportation services. Given the Brazilian market's fragmentation, transportation's heavy dependence on roadways in Brazil, and management's appetite for growth, we expect JSL to maintain such a strategy. We believe that the recent capitalization provides the company with sufficient funding to maintain an active M&A pipeline while maintaining somewhat stable credit metrics. We assume that the company will perform acquisitions in similar size to recent ones--such as those of Fadel and Transmoreno together totaling around R$500 million--but with payments in installments along the years. This should allow for the maintenance of JSL's adjusted leverage at 3.5x-4.0x.

Outlook

The stable outlook reflects our expectation of lower leverage following the shares' issuance. Over the next few years, we expect the company to maintain adjusted debt to EBITDA below 4.0x even amid likely future acquisitions. We expect revenues and EBITDA to increase 25% in 2021 following the full incorporation of acquisitions and recovery of transported volumes in the country, while JSL maintains a controlled cost structure given its predominantly asset-light model.

Downside scenario

A downgrade is unlikely at this point because it would require a simultaneous lower SACP for JSL and a downgrade of Simpar. If we were to downgrade Simpar to 'B+', ratings on JSL wouldn't change because its SACP is now at the same level as the group credit profile. And if we were to revise downwards JSL's SACP to 'b', assuming no change in Simpar's credit quality, the final rating on JSL would still be 'B+' due to expected support from the higher rated parent.

We could revise downwards JSL's SACP if we were to expect adjusted debt to EBITDA approaching 5x and/or funds from operations (FFO) to debt below 12% and lower cash flows, harming the company's liquidity. These metrics could be a result of:

- The economic contraction lasting longer than predicted, resulting in a deterioration of the company's operational performance, reflected in lower cargo transportation and commodity services levels; and/or
- An aggressive acquisitive or dividend distribution strategy, rapidly consuming the company's cash position and increasing leverage.

Upside scenario

An upgrade is unlikely in the short term because we expect JSL to maintain an acquisitive strategy that would prevent an improvement in leverage metrics. Nevertheless, we could revise upwards the company's SACP and raise the final rating if we were to expect adjusted debt to EBITDA of 3.0x-4.0x and FFO to debt above 20% even amid acquisitions.

Company Description

JSL is the main provider of logistics services and freight transportation in Brazil. The company serves around 16 sectors with no significant concentration. Its portfolio consists of asset-light and asset-heavy contracts, accounting for 65% and 35% of revenues, respectively. We expect the company to post net revenue of about R$2.85 billion and EBITDA close to R$480 million in 2020.

JSL is a subsidiary of the Brazilian transportation group, Simpar, which controls the company with a 74% stake following the IPO. We expect JSL to contribute around 30% and 20% of the group's revenue and EBITDA, respectively, in 2020.

Our Base-Case Scenario

- Brazil's real GDP contraction of about 7.0% in 2020 and growth of 3.5% in 2021.
- Inflation in Brazil close to 2.7% in 2020 and increasing to 3.2% in 2021, affecting costs and contract prices, and rates on existing contracts due to clauses that allow for inflation pass-through.
- Revenue and EBITDA falling 5%-10% in 2020. We attribute the impact to the automotive stoppages as well as slightly lower output of some of the company's commodities-extracting clients during the initial stages of the pandemic. The long-term contracts (varying from 2 to 10 years) and new acquisitions to mitigate the impact this year.
- Revenue and EBITDA increasing around 25% in 2021 with the full-year results of recent acquisitions and linked to economic recovery.
- The company's cost structure shows asset-light flexibility with small exposure to fixed costs, which should allow for almost stable gross margin in 2020 and afterwards.
- Net capex of R$200 million in 2020 and R$250 million in 2021, incorporating contract renegotiations and higher investments in 2021 through new contracts at its asset-heavy portfolio with the economic recovery.
- Acquisition of Fadel Holding (Fadel) for about R$160 million, with 50% of it in 2020 and 50% in 2021 and net debt incorporation of around R$120 million.
- Transmoreno's acquisition for R$310 million, with R$120 million paid in 2020 and the remainder in semi-annual installments in the next five years, with no debt increase.
- Our adjusted debt figures incorporate future obligations related to recent acquisitions, totaling R$248 million in 2020 and R$125 million in 2021.
- Extraordinary dividend payments of around R$250 million in 2020 and distribution at 25% of previous year's net income in 2021.
- Net proceeds from share offering totaling around R$700 million.

These assumptions result in the following credit metrics:

- Adjusted debt to EBITDA of around 4x in 2020 and 3.0x-3.5x in 2021;
- FFO to debt of 5%-10% in 2020 and 15%-20% in 2021; and
- EBITDA interest coverage above 2x in 2020 and 2021.

Liquidity

We continue assessing JSL's liquidity as adequate. Following our latest publication on August 6 ("Simpar Rated 'BB-' After Approval Of JSL's Group Reorganization, Outlook Negative"), the company will strengthen its liquidity sources through the share issuance, but we also expect higher uses given the outflows for acquisitions and higher capex. Therefore, we continue forecasting sources of liquidity to exceed uses by more than 1.2x in the next 12 months, and to remain positive even if EBITDA were to decline 15%.

Group Influence

We view JSL as a highly strategic subsidiary of the group. We understand that the IPO reaffirms Simpar's strategy of separating each business line, diluting its stake but maintaining control of its subsidiaries, while each subsidiary should independently fund its own growth. Still, we expect JSL to benefit from the group's long-term commitment as the subsidiary represents a relevant portion of consolidated EBITDA. Therefore, JSL is likely to receive support during stressed conditions.

Ratings Score Snapshot

Issuer credit rating:

- Global scale: B+/Stable/--
- National scale: brAA/Stable/--

Business risk: Fair

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

Financial risk: Aggressive

- Cash flow/Leverage: Aggressive

Anchor: bb-

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Management and governance: Fair (no impact)
- Comparable rating analysis: Negative (-1 notch)

Stand-alone credit profile: b+

Group credit profile: bb-

Entity status within group: Highly strategic

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Railroad And Package Express Industry, Aug. 12, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Transportation Cyclical Industry, Feb. 12, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, 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: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
JSL S.A.		
Issuer Credit Rating	B+/Stable/--	B+/Negative/--
Brazil National Scale	brAA/Stable/--	brAA-/Negative/--

Upgraded

	To	From
JSL S.A.		
Senior Unsecured	brAA	brAA-
Recovery Rating	3(65%)	3(65%)

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 for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.