Research Update:

Orbia Advance Corp. S.A.B. de C.V. 'BBB-/A-3' And 'mxAA/Stable/mxA-1+' Ratings Affirmed; Outlook Remains Stable

May 29, 2024

Primary contact

Humberto Patino
Mexico City
52-55-50814485
humberto.patino
@spglobal.com

Secondary contact

Fabiola Ortiz
Mexico City
52-55-5081-4449
fabiola.ortiz
@spglobal.com

Rating Action Overview

- Orbia Advance Corp. S.A.B. de C.V. (Orbia) will continue to confront stressed market and price conditions given oversupply of petrochemical production in Asia, delays in governments' investments in the telecom and agriculture projects, and potential supply-chain disruptions.
- On May 29, 2024, S&P Global Ratings affirmed its global scale 'BBB-/A-3' and national scale 'mxAA/mxA-1+' issuer credit ratings on Orbia.
- We also affirmed our 'BBB-' and ‘A-3’ issue-level ratings on the company's debt.
- The outlook remains stable, reflecting our expectations that Orbia's recently weakened leverage metrics will recover in the next 12-18 months, and remain in line with the revised assessment of the company's financial risk profile.

Rating Action Rationale

We assume that the petrochemical industry's periodic volatility dents the players' operations and cash generation. The industry is currently in the low-price and constrained-demand cycle due to geopolitical frictions, difficult economic conditions, and oversupply/high inventories mainly in China and the U.S. In addition, the company still compares positively with 'BBB-' rated peers, and since the latter are posting weaker metrics than Orbia, we can assume that pressures are taking a toll on all industry players. Across most of Orbia’s segments, we believe the following will continue to weigh on revenue for the next 12-18 months:

- Oversupply in the market leads to weaker demand and lower sale prices. Although lower prices also reduce Orbia’s raw material costs, fixed costs take longer to fall.
- Some projects in global agriculture, telecommunication, auto, and construction sectors tend to be funded through debt, and currently higher interest rates have delayed most of these projects, hampering Orbia’s sales growth.
- The company generates 5% of its total revenue from Israel, which is currently in the conflict with Hamas. Indirectly, the supply-chain problems forced Orbia to increase logistics costs to

achieve the delivery of products and raw materials. As of this report's date, the conflicts hasn't had a significant impact on the company's sales to Israel, but if it escalates, it could depress growth prospects for the company.

We revised our assessment of Orbia's financial risk profile to significant from intermediate because leverage metrics will remain weaker than expected throughout the low-price cycle and pressured market conditions. Given the industry's downturn, Orbia's fourth-quarter EBITDA declined 27% from the same period in 2022 and its debt to EBITDA averaged 2.7x last year. However, the company posted a significant recovery in the first quarter of 2024, and we expect this trend to continue for the remainder of the year, reducing leverage metrics slightly below 3x for the next 18 months. We expect Orbia to continue implementing cost-optimization initiatives to mitigate a further decline in EBITDA and resume deleveraging toward its target of 2.5x.

Amid turbulent market and economic conditions, Orbia secured additional liquidity sources. On April 2, 2024, the company entered into a new committed revolving credit facility of $1.4 billion with a five-year tenor, granted by a syndicate of leading global financial institutions. This will continue to support our view of the company's liquidity as strong.

The prolonged Middle East conflict could indirectly have a negative effect on Orbia's operations. Historically, the company's Precision Agriculture unit's revenue from Israel only accounts for slightly higher than 5% of overall global revenue, and there have not been material disruptions from the conflict. In the event of its prolonged duration, Orbia has planned alternative logistics channels, and diversify production from North America. We will continue monitoring to see if the conflict causes changes to our revenue forecast of 5% coming from Israel.

Outlook

The stable outlook reflects our base-case scenario of weaker metrics recovering in the next 12-18 months, given that cost-optimization initiatives will ease the impact of the low-price and weaker-demand cycle, keeping Orbia's EBITDA stable. This will allow Orbia to maintain debt to EBITDA slightly below 3x for the next two years, which is in line with our current assessment of its financial risk profile.

Downside scenario

We could revise the outlook to negative or lower the ratings in the next 12-24 months if:

- The company fails to protect EBITDA and free operating cash flow (FOCF) from turbulent economic and market conditions, resulting in debt to EBITDA above 3x and FOCF to debt below 0% on a consistent basis.
- Orbia adopts a more aggressive financial policy, weakening its liquidity position due to higher capital expenditure (capex) and/or dividend payments, while also taking on additional debt.
- The company's operations will deviate from our base-case scenario, such as moving away from prudent risk management, along with greater industry volatility, which could prompt us to revise our assessment of the company's financial risk profile to a weaker category.
- The company starts comparing negatively with its 'BBB-' rated peers based on its revenue growth and EBITDA margins.

Upside scenario

An upgrade in the next 12-24 months would require:

- A longer record of prudent financial discipline, with debt to EBITDA below 2x and FOCF to debt above 25% consistently. This would be reflected in disciplined approach to cash flow allocation; and/or
- A larger scale, and wider product and geographic diversification, aligning Orbia with higher-rated peers.

Company Description

Orbia is a Mexico-based industrial conglomerate. The company's activities are divided into five business groups: Precision Agriculture, Building & Infrastructure, Fluor & Energy Materials, Connectivity Solutions, and Polymer Solutions. The Precision Agriculture business includes the Netafim brand, and develops irrigation systems and related services, as well as offers farming digitalization. The Building & Infrastructure unit offers pipes for multiple building applications through its Wavin brand. The Fluor & Energy Materials segment operates the Koura brand, and manufactures fluorine-based materials used in such industries as healthcare, construction, and transportation. The Connectivity Solutions business produces and installs communication and power cables through its Dura-Line brand. The Polymer Solutions unit includes Vestolit and Alphagary brands, and provides plastic resins and other compounds. Orbia is headquartered in Mexico City and is a subsidiary of Kaluz S.A. de C.V. that owns 44.83% of capital stock. Members of the Del Valle family control approximately 54.1% of the company's outstanding voting capital.

Our Base-Case Scenario

Assumptions

Our economic assumptions include:

- Mexico's GDP to grow 2.5% in 2024 and 1.8% in 2025, and Consumer Price Index (CPI) of 4.5% and 3.5%, respectively.
- U.S. GDP to expand 2.5% in 2024 and 1.5% in 2025, and CPI of 2.8% and 2.0%, respectively.
- The eurozone GDP to grow 0.7% in 2024 and 1.3% in 2025, and CPI of 2.6% and 2.1%, respectively.
- The Middle East and North Africa region's GDP to rise 2.3% in 2024 and 3.8% in 2025, and CPI of 8.0% and 5.6%, respectively.
- Brazil's GDP to expand 1.8% in 2024 and 2.0% in 2025, and CPI of 4.1% and 3.7%, respectively.
- Orbia's sales are mainly driven by the industrial sector's growth, and by household and individual spending. We expect that economies of the regions in which Orbia operates will grow but will face some inflationary pressures that could dent growth in the next 12 months.
- The company generates its sales from the U.S. (27.5%), the eurozone (32.7%), Mexico (11.5%), the Middle East, Africa, and Asia (11.8%), Brazil (8%), and other countries (16.4%).
- Average foreign exchange rates of MXN17.5 per US$1 in 2024 and MXN17.8 per US$1 in 2025.
- Orbia's reporting currency is the dollar for comparable reasons. Seventy five percent of its debt was in the greenback and the rest was mainly in Mexican pesos as of March 31, 2024. We

do not think this poses any foreign-exchange risk, since most of the company's revenue is directly linked to the same currency.

- Brent prices to remain at $80 per barrel in 2024 and $80 per barrel in 2025.

Our assumptions for Orbia's segments include the following:

- Polymer Solutions' operations will most likely reflect price constraints due to Asia's oversupply in petrochemicals.
- Building & Infrastructure will continue to expand in Latin America, while the optimization in costs to mitigate lower sale prices.
- Connectivity Solutions to take advantage of decreasing market inventories and strengthening volumes through upcoming infrastructure projects, especially in the U.S.
- Precision Agriculture to launch new products and taking higher relevance on its farming solutions.
- Fluor & Energy Materials will continue maximizing installed capacity and trimming operating costs.
- Total revenue to decrease by 2.7% to $7.99 billion in 2024 and grow 4.4% to $8.34 billion in 2025.
- Adjusted EBITDA at about $1.3 billion in 2024 and $1.6 billion in 2025.
- Capex to represent about 8.5% of total revenue, leading to $520 million in 2024 and $876 million in 2025 for production and maintenance.
- Dividends for 2024 and 2025 will be about $160 million annually, down from $240 million in 2023.
- The company will have minimal debt maturities until 2026. Total debt mainly consists of senior unsecured notes in international markets (69%), local bonds (25%), and the rest consists of bank loans with bullet amortizations in 2024. Therefore, we expect total debt to remain between $4.7 billion and $5.0 billion for the next two years.

Key metrics

Orbia Advance Corporation S.A.B. de C.V--Forecast summary

Period ending	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023	Dec-31-2024	Dec-31-2025	Dec-31-2026
(Mil. $)	2020a	2021a	2022a	2023a	2024e	2025f	2026f
Revenue	6,420	8,783	9,648	8,204	7,986	8,341	8,755
Gross profit	2,444	3,054	2,986	2,612	2,465	2,797	3,059
EBITDA (reported)	1,318	2,047	1,909	1,457	1,275	1,583	1,817
Plus: Operating lease adjustment (OLA) rent	--	--	--	--	--	--	--
Plus/(less): Pension and postretirement expenses	11	7	--	5	5	5	5
EBITDA	1,329	2,053	1,909	1,462	1,280	1,588	1,822

Orbia Advance Corporation S.A.B. de C.V--Forecast summary

Less: Cash interest paid	(231)	(271)	(258)	(388)	(378)	(388)	(388)
Less: Cash taxes paid	(281)	(243)	(488)	(371)	(168)	(337)	(469)
Plus/(less): Other	--	--	--	--	--	--	--
Funds from operations (FFO)	817	1,540	1,163	703	733	863	965
EBIT	742	1,473	1,225	949	701	981	1,184
Interest expense	242	250	287	393	382	391	392
Cash flow from operations (CFO)	872	965	1,030	1,009	500	736	996
Capital expenditure (capex)	236	313	537	684	519	876	613
Free operating cash flow (FOCF)	636	651	493	325	(19)	(140)	383
Dividends	230	200	299	240	154	158	263
Share repurchases (reported)	42	166	142	(8)	--	--	--
Discretionary cash flow (DCF)	364	286	52	93	(173)	(299)	120
Debt (reported)	3,626	3,520	4,696	4,886	4,712	5,004	4,954
Plus: Lease liabilities debt	345	367	369	489	513	539	566
Plus: Pension and other postretirement debt	174	124	72	62	62	62	62
Less: Accessible cash and liquid Investments	(875)	(782)	(1,546)	(1,456)	(1,093)	(1,066)	(1,110)
Plus/(less): Other	--	--	--	--	--	--	--
Debt	3,270	3,229	3,591	3,981	4,195	4,540	4,473
Equity	3,180	3,404	3,323	3,218	3,144	3,167	3,157
FOCF (adjusted for lease capex)	553	510	381	184	71	(50)	473
Interest expense (reported)	239	248	285	389	378	387	388
Capex (reported)	236	313	537	684	519	876	613
Cash and short-term investments (reported)	875	782	1,546	1,456	1,093	1,066	1,110
Adjusted ratios							
Debt/EBITDA (x)	2.5	1.6	1.9	2.7	3.3	2.9	2.5
FFO/debt (%)	25.0	47.7	32.4	17.7	17.5	19.0	21.6
FFO cash interest coverage (x)	4.5	6.7	5.5	2.8	2.9	3.2	3.5
EBITDA interest coverage (x)	5.5	8.2	6.7	3.7	3.4	4.1	4.7
CFO/debt (%)	26.7	29.9	28.7	25.3	11.9	16.2	22.3
FOCF/debt (%)	19.4	20.2	13.7	8.2	(0.4)	(3.1)	8.6
DCF/debt (%)	11.1	8.8	1.4	2.3	(4.1)	(6.6)	2.7
Lease capex-adjusted FOCF/debt (%)	16.9	15.8	10.6	4.6	1.7	(1.1)	10.6
Annual revenue growth (%)	(8.1)	36.8	9.8	(15.0)	(2.7)	4.4	5.0
Gross margin (%)	38.1	34.8	30.9	31.8	30.9	33.5	34.9
EBITDA margin (%)	20.7	23.4	19.8	17.8	16.0	19.0	20.8
Return on capital (%)	11.5	22.5	18.1	13.4	9.6	13.0	15.4
Return on total assets (%)	7.3	14.2	11.0	8.2	6.1	8.5	10.2
EBITDA/cash interest (x)	5.7	7.6	7.4	3.8	3.4	4.1	4.7
EBIT interest coverage (x)	3.1	5.9	4.3	2.4	1.8	2.5	3.0
Debt/debt and equity (%)	50.7	48.7	51.9	55.3	57.2	58.9	58.6
Debt fixed-charge coverage (x)	5.5	8.2	6.7	3.7	3.4	4.1	4.7
Debt/debt and undepreciated equity (%)	50.7	48.7	51.9	55.3	57.2	58.9	58.6

Liquidity

We continue to view Orbia's liquidity as strong. Despite the industry's low-price and constrained-demand cycle, Orbia has mitigated liquidity pressures, while we expect its EBITDA to fall this year. The company has taken actions to further reduce liquidity uses for the next 12-24 months, such as lower dividend payments, tightening costs to strengthen EBITDA, as well as maintaining debt capital structure free of short-term debt. These factors, in our view, will allow Orbia to withstand low-probability events such as a prolonged period of low prices. We expect sources of liquidity to exceed uses by at least 1.5x for the next 12 months, and 1.0x for the subsequent 12 months, even if EBITDA were to decline by 30% from our expectations. Orbia's prudent risk management and access to additional sources of liquidity, such as its renewed committed revolving credit facility, have reflected positively in markets as its bonds continue trading close to par.

Principal liquidity sources

- Available cash of $1.05 billion as of March 31, 2024.
- Committed credit lines with an undrawn amount of $1.4 billion available for the next 24 months.
- Expected cash FFO of $820 million for the next 12 months.

Principal liquidity uses

- Minimal short-term debt maturities of $295 million as of March 31, 2024.
- Working capital requirements of MXN145 million for the next 12 months.
- Seasonal working capital requirements of MXN100 million for the next 12 months.
- Expected capex of $600 million for the next 12 months.
- Dividends of MXN160 million for the next 12 months.

Covenants

Environmental, Social, And Governance

Environmental factors have a negative consideration in our credit rating analysis of Orbia. This is captured in our assessment of the petrochemical industry's risk associated with highly energy-intensive production facilities, as well as gas emissions, pollution, waste, and climate change. Although Orbia manufactures products that by their nature can cause some environmental damage, we consider that the company is in compliance with regulators and continuously invests in environmental solutions in the markets where it participates. In 2023, Orbia achieved significant progress in mitigating environmental risks by:

- Reducing its greenhouse gas emissions (scope 1 and 2) by 28% from 2019.
- Reducing its sulfuric oxide emissions by 84% from 2018 and surpassing its sustainability-linked bond target by 24%.
- Consumption of renewable energy increased by 52% from 2022.

Issue Ratings--Subordination Risk Analysis

Capital structure

As of March 31, 2024, Orbia's capital structure consisted of global and local senior unsecured notes, which represented 94% of total debt with maturities in 2025, 2026, 2027, 2031, 2032, 2042, 2044, and 2048. Bank loans represented the remaining 6% of the consolidated debt.

Analytical conclusions

We continue to rate Orbia's senior unsecured notes 'BBB-', the same as our issuer credit rating on the company. Most of the debt is at the holding level, with only about 7% of the debt at the subsidiaries' level. Given that this ratio is less than 50%, the senior unsecured notes are not subordinated. Additionally, Orbia's largest subsidiaries fully and unconditionally guarantee the notes, which mitigates the subordination risk.

Rating Component Scores

Foreign currency issuer credit rating	BBB-/Stable/A-3
Local currency issuer credit rating	BBB-/Stable/A-3
Business risk	Satisfactory
Country risk	Intermediate
Industry risk	Moderately High
Competitive position	Satisfactory
Financial risk	Significant
Cash flow/leverage	Significant
Anchor	bbb-
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Strong (no impact)
Management and governance	Positive (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	bbb-

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- General Criteria: National And Regional Scale Credit Ratings Methodology, June 8, 2023
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- 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
- 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
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Tear Sheet: Orbia Advance Corporation S.A.B. de C.V., Nov. 28, 2023
- Orbia Advance Corporation S.A.B. de C.V., June 6, 2023

Ratings List

Ratings list

Ratings Affirmed

Orbia Advance Corp. S.A.B. de C.V.

Issuer Credit Rating	BBB-/Stable/A-3
CaVal (Mexico) National Scale	mxAA/Stable/mxA-1+
Senior Unsecured	BBB-
Commercial Paper	A-3

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.spglobal.com/ratings for further information.

Complete ratings information is available to RatingsDirect subscribers at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.spglobal.com/ratings.