MOODY'S
INVESTORS SERVICE

Rating Action: Moody's downgrades Coty's CFR to B1; outlook negative

26 Nov 2018

New York, November 26, 2018 -- Moody's Investors Service ("Moody's") downgraded Coty Inc.'s ("Coty") Corporate Family Rating ("CFR") to B1 from Ba3 and Probability of Default Rating to B1-PD from Ba3-PD. At the same time, Moody's downgraded Coty's first lien revolving credit facility and term loan to Ba3 (LGD3) from Ba2 (LGD3), its unsecured notes to B3 (LGD5) from B2 (LGD5) and its Speculative Grade Liquidity Rating to SGL-4 from SGL-3. The rating outlook on all ratings is negative.

The downgrade of Coty's CFR reflects meaningful operational challenges as Coty continues to integrate Procter & Gamble Beauty ("P&G Beauty"), which it acquired in 2016. Coty recently announced unexpected supply chain disruptions that Moody's expects will continue over the near term. These disruptions negatively affected the company's first quarter sales and profitability. As such, Moody's expects that the company's 2019 results will be negatively impacted because it will take management time to assess and resolve Coty's supply chain challenges. The company's profitability will also be adversely affected by high promotional activity needed to support sales during the holiday season. Coty is attempting to streamline its supply chain while simultaneously integrating P&G Beauty, and restructuring its operations to restore growth and improve operating performance. Coty has also had significant turnover in its senior management ranks. The company has a new chief executive officer, which brings some level of uncertainty to the company's overall strategy. The company is also searching for a permanent chief financial officer.

The downgrade also reflects continued weakness in Coty's consumer beauty business, exacerbated by its recent supply chain headwinds, and very slow progress at deleveraging following the acquisition of P&G Beauty. Moody's estimates that Coty's 2019 debt to EBITDA will reach a high of 6.5x, and expects near-term leverage reduction to be hampered by low organic earnings growth.

The Ba3 rating on Coty's senior secured debt is one notch higher than the B1 CFR and reflects cushion provided by the company's unsecured debt.

The negative outlook reflects Moody's uncertainty regarding Coty's ability to stabilize its operations quickly given its near term challenges and ongoing competitive industry pressures. Moody's believes that Coty's operating performance and resulting credit metrics will remain weak over the next year. Continued operating challenges leading to an inability to meaningfully lift earnings and generate comfortably positive free cash flow would pressure the ratings.

The following is a summary of Moody's rating actions:

Coty Inc.

Downgrades:.

Corporate Family Rating downgraded to B1 from Ba3

Probability of Default Rating downgraded to B1-PD from Ba3-PD

First Lien Senior Secured Bank Credit Facility downgraded to Ba3 (LGD3) from Ba2 (LGD3)

Guaranteed Unsecured Global Notes downgraded to B3 (LGD5) from B2 (LGD5)

Speculative Grade Liquidity Rating downgraded to SGL-4 from SGL-3

The outlook on all ratings is changed to negative from stable.

RATINGS RATIONALE

Coty's B1 CFR reflects the company's high debt to EBITDA financial leverage, estimated at about 6.5x. The high financial leverage is in part due to earnings weakness reflecting lackluster demand for the company's domestic consumer beauty products. The rating also reflects Moody's expectation that the company will generate negative free cash flow over the next several quarters due to its ongoing restructuring costs and dividends. Moody's recognizes Coty's concentration in fragrance and color cosmetics. This concentration creates exposure to discretionary consumer spending. It also requires continuous product and brand investment to minimize revenue volatility as these categories tend to be more fashion driven than other beauty products. Coty will remain more concentrated than its primary competitors in mature developed markets. This creates growth challenges and investment needs to more fully build its global distribution capabilities and brand presence. The ratings are supported by the company's large scale, its portfolio of well-recognized brands, and good product and geographic diversification. Moody's expects that Coty will generate modest revenue and organic earnings growth over the next year.

The SGL-4 Speculative Grade Liquidity Rating reflects Moody's view that Coty's liquidity is weak. Coty's ongoing restructuring actions will consume large amounts of cash and Moody's expects the company's free cash flow to remain negative in 2019. The company relies on a $3.25 billion secured revolving credit facility that had $885 million drawn as of September 30, 2018. Moody's expects the revolver to be used to fund the projected cash flow deficit and the company's dividend in 2019. The revolver is subject to a total net leverage financial covenant with step downs. As of September 30, 2018 the total net leverage covenant was at 4.6x with a 5.5x maximum. The covenant maximum will step down to 5.25x in March 2019. Moody's projects that the company will have weak headroom under the total net leverage covenant over the next 12 months.

Coty's ratings could be downgraded if the company is unable to stabilize its operations or if the company does not make meaningful progress in reducing debt to EBITDA below 6.0x. A downgrade could also occur if there is a deterioration in the company's liquidity or if the company pursues material debt funded acquisitions or shareholder returns.

Coty's ratings could be upgraded if the company stabilizes its operations. An upgrade would also require the company to generate positive free cash flow and improve its credit metrics.

The principal methodology used in these ratings was Global Packaged Goods published in January 2017. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Coty Inc. ("Coty"), a public company headquartered in New York, NY, is one of the leading manufacturers and marketers of fragrance, color cosmetics, and skin and body care products. The company's products are sold in over 130 countries. The company generates roughly $9.2 billion in annual revenues.

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