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Research Update:

JAB Holding Company S.a r.l. Outlook Revised To Negative On Partial Tender Offer On Coty Shares; 'A-' Ratings Affirmed

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Rating Action Overview

- JAB Holding Co. S.A.R.L. (JAB) announced it is launching a partial tender offer on publicly traded Coty shares for $11.65 per share, which represents approximately a 20% premium on the latest closing price.
- As the result of this transaction, we believe Coty shares will no longer be immediately available to help maintain JAB's loan to value (LTV) ratio below 20%, as per its financial policy targets.
- We are therefore revising our outlook on JAB to negative from stable and at the same time are affirming our 'A-' ratings on the company.
- The negative outlook reflects that we could lower the rating if JAB is not able to reduce its LTV ratio to below 20% by the end of 2019.

Rating Action Rationale

The outlook revision reflects our view of JAB Holding Co. S.A.R.L.'s (JAB's) announcement that it will launch a partial tender offer on publicly traded Coty shares for $11.65 per share, which represents approximately a 20% premium on the latest closing price. JAB intends to acquire up to 150 million additional Coty shares. As the result of this transaction, we believe Coty shares will no longer be immediately available to help maintain JAB's loan-to-value (LTV) ratio below 20%, as per its financial policy targets. It further reflects our expectation that JAB's LTV ratio, which was at about 20% at year-end 2018 and slightly above our prior expectations of 18%, will struggle to further decrease because of this transaction.

U.S.-based fragrance and cosmetic player Coty's underperformance negatively affected JAB's overall portfolio, with Coty's market value declining by €1.5 billion since our last review in July 2018. After shareholders enforced a management change at Coty toward year-end 2018, JAB is launching a partial tender offer on Coty shares to increase its stake to above the 40% it currently owns.

The transaction includes the set-up of a dedicated special purpose vehicle (SPV), which will receive JAB's 301 million shares in Coty. The acquisition of additional shares offered in the context of the tender will be funded with bank debt, which we understand will be entirely and solely guaranteed by Coty shares, but not in any way guaranteed or supported by JAB. JAB, owner of the

SPV, retains the right to wind down the structure at any time during its three years maximum life, repay the debt, and receive the SPV net asset value. Repayment of the debt relies to a major extent on the sale of Coty shares in the SPV and, to a lesser extent, on potential excess cash generated from the difference between dividends distributed from Coty and the cost of funds. This implies that JAB will stop receiving dividends from Coty during the life of the transaction. Lenders will retain the right to enforce the sale of shares and/or call for equity injection should the LTV ratio exceed 70%. The trigger corresponds to a Coty share price level, below which JAB will have to sell part of its pre-existing 301 million shares to rebalance the LTV ratio.

From our perspective, the transfer of existing Coty stake into an SPV leaves JAB's bondholders at a temporary disadvantage during the life of the transaction. This is because, as long as the debt is outstanding, shares in Coty will not contribute to management's efforts to maintain the LTV below 20%. Because of the debt's overcollateralization, we acknowledge that the SPV will have a positive net asset value, as long as the Coty share price does not severely underperform versus the tendered share price. At the same time, visibility regarding the turnaround at Coty remains low. For the purposes of calculating JAB's LTV ratio after the closing of the tender, we will treat the SPV as an unlisted asset in JAB's portfolio. This is to reflect our assessment of the incremental risk of the transaction. We will wait to reassess the transaction at closing of the tender offer.

Outlook

The negative outlook reflects our view that the transaction could prevent JAB from reducing its LTV ratio to below 20% by the end of 2019.

Downside scenario

We would lower the rating if we believe the LTV ratio will remain over management's commitment of 20% over a prolonged period. This could occur if JAB undertakes further portfolio acquisitions without selling other portfolio assets.

Upside scenario

We would revise the outlook to stable if the LTV ratio was below 20% by the end of 2019.

Company Description

JAB is an investment holding company with a focus on defensive and fast-moving consumer goods and consumer retail assets. It pursues an active management approach to build global champions and challengers. In contrast to other holding companies, JAB focuses on actively managing most of its assets, allowing it significant control and influence over their capital structure and dividend flows.

Another distinguishing factor is JAB's access to JCF's consumer fund. JCF, a separate equity portfolio managed by JAB executives that roughly mimics JAB's investments, provides third-party equity.

Through such a partnership, JAB is able to undertake large and transformative transactions, such as the reverse takeover of Dr Pepper, while maintaining control over the dividend streams, and limiting the total leverage at JAB. In our base case, we believe that JCF represents not only an investment partner, but also an opportunity to address temporary market weaknesses and manage JAB's long-term LTV target (below 20%) without losing control over its assets. We see this as a unique advantage for JAB compared with other peers, and reflect this in the rating on JAB.

Liquidity

We assess JAB's liquidity as exceptional, given there are no debt maturities upcoming in the next two years. In liquidity sources, we include the large committed revolving credit facility (RCF; €2.6 billion undrawn as of December 2018), and we estimate that its liquidity sources exceed needs by 16x for the 12 months from Dec. 31, 2018. We consider that JAB's strong ties with banks support its ability to quickly obtain bank financing, if needed. We also believe it is likely that JAB would be able to absorb a high-impact event with limited need for refinancing. For JAB, such a scenario would likely be a severe correction of market values for its listed shares, which we consider manageable in view of its relatively low LTV ratio.

For the 12 months from Dec. 30, 2018, we estimate that principal liquidity sources comprise:

- Cash and cash equivalents exceeding €1 billion;
- Dividend inflow of about €400 million per year on average; and
- Access to a €2.6 billion of a committed RCF maturing beyond one year, currently undrawn.

For the same period, we estimate that liquidity uses comprise:

- Operating expenses of €30 million-€40 million;
- Interest expense of €140 million-€150 million; and
- Dividends of about €100 million.

We view headroom under the RCF covenant as comfortable.

Issue Ratings - Subordination Risk Analysis

Capital structure

JAB Holdings B.V. is the financing subsidiary of JAB, which is 100%-owned through an intermediate holding company. On a consolidated group level, gross debt, represented by bonds, totaled €6.0 billion at Dec. 30, 2018.

Analytical conclusions

JAB has a relatively low level of gross debt, and we assess its financial risk profile as modest. The syndicated RCF and unsecured bonds rank pari passu. As a result, there are no significant elements of subordination risk present in the capital structure, in our view, and we rate the senior unsecured debt 'A-', in line with the issuer credit rating.

Ratings Score Snapshot

Issuer Credit Rating: A-/Negative/--

Business risk: Satisfactory

- Country risk: Low
- Industry risk: Intermediate
- Investment position: Satisfactory

Financial risk: Modest
- Cash flow/Leverage: Modest

Anchor: bbb+

Modifiers
- Liquidity: Exceptional (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Positive (+1 notch)

Stand-alone credit profile: a-

Related Criteria

- 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

- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Outlook Action; Ratings Affirmed

	To	From
JAB Holding Company S.a r.l.		
Issuer Credit Rating	A-/Negative/--	A-/Stable/--
JAB Holdings B.V.		
Senior Unsecured	A-	A-

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. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.