MOODY'S INVESTORS SERVICE

CREDIT OPINION
21 April 2021

Update

Rate this Research

RATINGS

Coty Inc.

Domicile	United States
Long Term Rating	Caa1
Type	LT Corporate Family Ratings
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Coty Inc.

Update following change in outlook to stable from negative

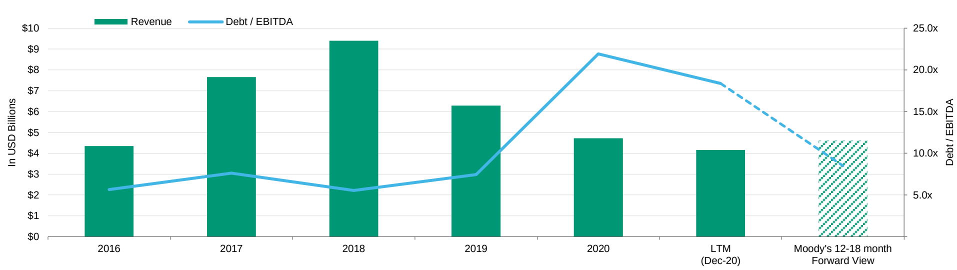
Summary

Coty's credit profile (Caa1; stable) reflects its gradual recovery over the next few quarters from weak revenue levels that were driven by efforts to contain the coronavirus and pressure on discretionary consumer income, contributing to high debt to EBITDA financial leverage that we estimate at about 8.5x in December 2021. The credit profile also reflects our belief that the company will generate weak free cash flow over the next several quarters due to its ongoing restructuring costs. Coty has been plagued by low demand for its products due to weaker than expected sales and earnings from its consumer beauty products (38% of sales) and from the company's luxury beauty and fragrance products (62% of sales). Over the next 3-6 months, demand will continue to be adversely impacted by the lingering effects of the coronavirus as worldwide consumer vaccination efforts remain uneven, as well as ongoing competitive pressures. That said, we expect demand for Coty's products to improve over the next year as the number of vaccinated consumers continues to increase, and as consumers slowly return to their everyday activities. Coty's credit profile is supported by its large scale, portfolio of well-recognized brands, and good product and geographic diversification.

Exhibit 1

Debt/EBITDA will improve as the company's earnings improve, debt is repaid, and the initial impact of the global pandemic is cycled out

Revenue (left scale) and Debt / EBITDA (right scale)



All figures and ratios are calculated using Moody's estimates and standard adjustments. Moody's Forward View is Moody's opinion and does not represent the views of the issuer. The company's fiscal year ends in June. LTM = Last Twelve Months.
Source: Moody's Financial Metrics™, Moody's Projections

Credit strengths

» Large scale and well-recognized brands in several beauty categories

» Strong public commitment to reducing net leverage to below 5.0x debt to EBITDA

Credit challenges

» High financial leverage and weak free cash flow

» Continued weak demand in the company's consumer beauty products

» Concentration in volatile fragrance and color cosmetics categories

» Need for constant innovation driven by portfolio composition

» Global diversification skewed towards slower growth mature developed markets

Rating outlook

The stable outlook reflects our expectation that Coty will continue to improve credit metrics over the next 12-to-18 months through an ongoing recovery in earnings from the weakness experienced during the coronavirus downturn. The outlook also reflects that the company's recent debt issuance is credit positive because it demonstrates continued progress with extending the significant 2023 debt maturities.

Factors that could lead to an upgrade

» Successful refinancing of remaining debt due 2023 in a timely manner

» Renewed revenue and earnings growth

» Significant reduction in financial leverage

» Generates comfortably positive free cash

Factors that could lead to a downgrade

» Inability to successfully refinance remaining debt due 2023 in a timely manner

» Inability to stabilize revenue and earnings or improve liquidity

» Ongoing weak or negative free cash flow over the next 12-18 months

» Inability to improve financial leverage

» Aggressive debt funded acquisitions or shareholder returns

Key indicators

Exhibit 2
Key Indicators
Coty Inc.

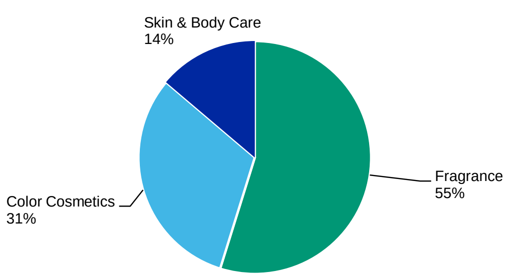
US Millions	Jun-16	Jun-17	Jun-18	Jun-19	Jun-20	LTM (Dec-20)	Moody's 12-18 month Forward View
Revenue	$4,349.1	$7,650.3	$9,398.0	$6,287.9	$4,717.8	$4,162.6	$4,536.0
EBITA Margin %	14.4%	8.9%	10.9%	8.4%	-3.4%	-3.4%	5.9%
Debt / EBITDA	5.7x	7.6x	5.5x	7.4x	21.9x	18.4x	8.5x
RCF / Net Debt	6.1%	-4.9%	4.3%	6.6%	-2.9%	-3.4%	2.7%
EBITA / Interest Expense	4.4x	2.6x	2.9x	1.6x	-0.6x	-0.5x	0.9x

All figures and ratios are calculated using Moody's estimates and standard adjustments. Moody's Forward View is Moody's opinion and does not represent the views of the issuer. Periods are Financial Year-End unless indicated. LTM = Last Twelve Months.
Source: Moody's Financial Metrics™, Moody's Projections

Profile

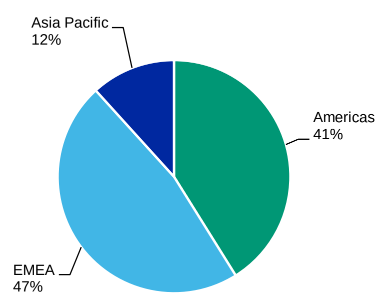
Coty Inc. ("Coty"), a public company headquartered in New York, NY, is one of the leading manufacturers and marketers of fragrance, color cosmetics, and skin and body care products. The company's products are sold in over 150 countries. The company generates roughly $4.0 billion in annual revenues. Coty is 60% owned by a German based investment firm, JAB Holding Company S.a.r.l. (JAB), with the rest publicly traded.

Exhibit 3
Revenue by segment
Twelve months ended December 31, 2020



Source: Company filings

Exhibit 4
Revenue by geography
Twelve months ended December 31, 2020



Source: Company filings

Detailed credit considerations

High financial leverage

We expect Coty's debt to EBITDA will improve to around 8.5x in the next 12-18 months from over 15x at December 2020. Coty will continue to improve credit metrics over the next 12-to-18 months through an ongoing recovery in earnings from the weakness experienced during the coronavirus downturn. Improved financial leverage reflects meaningful debt repayment from proceeds following the divestiture of a 60% interest in its Wella assets, continued cost reduction initiatives and efficiency improvements. The company estimates that 3rd quarter sales, ending March 31, 2021, will be down by low single digits, which represents meaningful sequential improvement from revenues that were down by mid to high double digits during the March, June and September quarters of 2020. All that said, demand will continue to be adversely impacted by ongoing competitive pressures and earnings improvement is still contingent on successful navigation through the store closures, reduced foot traffic, and changing consumer buying habits caused by the global coronavirus pandemic.

Weak free cash flow

Coty will struggle to generate positive free cash flow this fiscal year ended June 30 2021. Free cash flow will be adversely impacted by the company's declining sales and earnings in the first half of the fiscal year. We believe free cash flow will improve over time as the company stabilizes its operations and completes its restructuring program. We estimate the company to generate negative free cash flow in fiscal 2021 ending June 30, but modestly positive free cash flow in fiscal 2022.

Ambitious global restructuring carries high execution risk

Coty's ongoing restructuring will carry high execution risks given the company's historical execution challenges. As part of this restructuring the company sold 60% of its Professional business (Wella assets) to KKR in November 2020, proceeds of which were used to repay debt. The restructuring also includes the turnaround of its Consumer Beauty business, which has struggled over the last few years. The company will restructure its consumer beauty and fragrance businesses, which will include work force and product offering reductions. Coty will spend $500 million through 2023 on this turnaround plan, which is in addition to about $160 million of ongoing restructuring costs.

Concentration in volatile fragrance and cosmetics categories

Coty will continue to face risks associated with its significant reliance on revenues from the fragrance and color cosmetics categories, which tend to be volatile and vulnerable to fashion risk. We expect more volatility in these categories than in other consumer packaged goods sectors. To generate growth, Coty will have to continually reinvest and launch successful new products given its exposure to fashion driven fragrance (especially, designer brands) and color cosmetic products. Succeeding in an industry with high fashion risk requires continual investment in product development and brand support to sustain market share.

Good geographic diversification, but skewed towards developed markets

Coty will have good presence in large key beauty markets, including the U.S., the U.K., Germay and Brazil. However its geographic diversity is skewed toward developed markets. This puts the company at a growth disadvantage compared to peers with higher exposure to emerging markets. Around 60% of the company's revenues are generated from North America and Western Europe, presenting growth challenges in highly competitive markets, and about 40% of EMEA revenues are generated from Eastern Europe, Middle East and Africa. That said the company has announced plans to focus on increasing sales from developing markets over time. Although we view this strategy as favorable, we recognize that the company could face challenges in terms of distribution and brand awareness.

Large scale and well recognized brands in several categories

Coty will enjoy good scale relative to its peers in the beauty category. The company's mass consumer beauty products compete against those at Revlon (Caa3 negative; $2.0 billion in revenue). In contrast, some of Coty's luxury skin care and fragrance products compete against those at Estee Lauder (A1 stable; $14.0 billion). Scale benefits include leverage with suppliers and marketing efficiencies. Scale will also favorably affect the company's ability to obtain favorable terms with distributors, and create marketing efficiencies. The company's product portfolio enjoys good brand name recognition.

ESG considerations

The coronavirus outbreak, the government measures put in place to contain it, and the weak global economic outlook continue to disrupt economies and credit markets across sectors and regions. Our analysis has considered the effect on the performance of consumer sectors from the current weak U.S. economic activity and a gradual recovery for the coming months. Although an economic recovery is underway, it is tenuous, and its continuation will be closely tied to containment of the virus. As a result, the degree of uncertainty around our forecasts is unusually high. We regard the coronavirus outbreak as a social risk under its ESG framework, given the substantial implications for public health and safety.

Coty's credit profile also reflects governance considerations related to its financial policies and board independence. We view Coty's financial policies as aggressive given its appetite for debt financed acquisitions. In addition, the company's board of directors has limited independence given that four of the nine board members are related to JAB, Coty's majority shareholder.

Social considerations impact Coty in several ways. First, Coty is a “beauty” company. It sells products that appeal to customers almost entirely due to “social” considerations. That is, such products such as makeup and fragrance help individuals fit in to society and comply with social mores and customs. Hence social factors are the primary driver of Coty's sales, and hence the primary reason it exists. To the extent such social customs and mores change, it could have an impact -- positive or negative -- on the company's sales and earnings. However, we believe such risk is manageable as such customs and mores change at a measured pace, and as the company is able to adapt to changing “fashion” trends, and hence offset such social changes. The company engages with social media influencers, which is in line with demographic and societal trends. While negative product reviews for the company have historically been modest, we recognize that a high number of adverse product reviews could negatively impact product demand.

To help support the coronavirus relief effort, Coty adapted many of its factory operations to produce hydro-alcoholic gel, which the company distributed for free to medical and emergency services staff, care homes and pharmacies, as well as to Coty associates. The company also diverted resources, such as alcohol wipes and protective gloves, from a number of their brands for distribution.

Liquidity analysis

The SGL-4 Speculative Grade Liquidity Rating reflects our view that Coty's liquidity is weak because of negative free cash flow and significant required term loan amortization. Coty's ongoing restructuring actions will consume large amounts of cash (over $150 million), and therefore we expect the company to generate negative free cash flow in fiscal 2021 ending June 30. Free cash flow should turn positive in fiscal 2022 but required debt amortization remains significant at about $200 million annually. The company will rely on its $2.75 billion revolver expiring in 2023 to fund its working capital needs, projected free cash flow deficits and mandatory debt amortization. As of January 31, 2021, the company had about $2.1 billion available under its $2.75 billion revolver expiring in 2023. the revolver is subject to a maximum total net leverage financial covenant with step downs. The covenant's next step down to 5.0x is in March 2022. We project that the company will have weak headroom under the total net leverage covenant over the next 12 months. Assets are divisible as Coty could sell individual brands without materially affecting its remaining operations. However, alternate liquidity is limited because all material assets are pledged to Coty's bank credit facilities (revolver and term loan).

Structural considerations

The B3 rating on Coty's senior secured debt is one notch higher than the Caa1 CFR and reflects cushion provided by the company's effectively subordinated unsecured notes.

The Caa3 rating on the unsecured notes is two notches lower than the CFR. This reflects the effective subordination to about $3.9 billion of secured debt that would weaken recovery in the event of a default. The notes benefit from upstream guarantees from Coty's domestic subsidiaries.

Exhibit 5

December 31, 2020 Debt Capitalization Pro Forma for Issuance of $900m Notes

USD Millions	Outstanding	% Total
Revolving Credit Facility due April 2023	456	8.5%
Term Loan A due April 2023	1006.5	18.7%
Term Loan B due April 2025	1494	27.7%
US Senior Unsecured Notes due April 2026	550	10.2%
Euro Senior Unsecured Notes due April 2023	676.1	12.5%
Euro Senior Unsecured Notes due April April 2026	307.3	5.7%
New $900m Notes due April 2026	900	16.7%
Total Debt	**5389.9**	**100.0%**

Source: Company filings and Moody's estimates

Rating methodology and scorecard factors

The mapping to the scorecard in the Consumer Packaged Goods Methodology (February 2020) is shown below, including a 12-18 month forward view. The projected scorecard-indicated outcome of Ba3 is higher than the actual rating of Caa1. The difference primarily relates to liquidity risk including negative free cash flow and approaching maturities, and our concerns regarding how quickly Coty will be able to stabilize its operations.

Exhibit 6

Rating Factors

Coty Inc.

Consumer Packaged Goods Industry Scorecard [1][2]	Current LTM 12/31/2020		Moody's 12-18 Month Forward View As of April 2021 [3]	
Factor 1 : Scale (20%)	**Measure**	**Score**	**Measure**	**Score**
a) Revenue (USD Billion)	$4.2	Baa	$4.5	Baa
Factor 2 : Business Profile (30%)				
a) Geographic Diversification	A	A	A	A
b) Segmental Diversification	Ba	Ba	Ba	Ba
c) Market Position	Ba	Ba	Ba	Ba
d) Category Assessment	Ba	Ba	Ba	Ba
Factor 3 : Profitability (10%)				
a) EBITA Margin	-3.4%	Ca	5.9%	Caa
Factor 4 : Leverage and Coverage (25%)				
a) Debt / EBITDA	18.4x	Ca	8.5x	Caa
b) RCF / Net Debt	-3.4%	Ca	2.7%	Caa
c) EBITA / Interest Expense	-0.5x	Ca	0.9x	Caa
Factor 5 : Financial Policy (15%)				
a) Financial Policy	Ba	Ba	Ba	Ba
Rating:				
a) Scorecard-Indicated Outcome		B1		Ba3
b) Actual Rating Assigned				Caa1

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
[2] As of 12/31/2020(L);
[3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures
Source: Moody's Financial Metrics™

Appendix

Exhibit 7

Peer Comparison

Coty Inc.

	Coty Inc. Caa1 Negative			Avon Products, Inc. Ba3 Stable			Church & Dwight Co., Inc. A3 Stable			Revlon Consumer Products Caa3 Negative			Clorox Company (The) Baa1 Positive		
(in US millions)	FYE Jun-19	FYE Jun-20	LTM Dec-20	FYE Dec-18	FYE Dec-19	LTM Sep-20	FYE Dec-18	FYE Dec-19	LTM Sep-20	FYE Dec-18	FYE Dec-19	LTM Sep-20	FYE Jun-19	FYE Jun-20	LTM Dec-20
Revenue	$6,288	$4,718	$4,163	$5,403	$4,695	$3,775	$4,146	$4,358	$4,745	$2,565	$2,420	$1,977	$6,214	$6,721	$7,524
EBITDA	$1,176	$408	$331	$311	$345	$121	$965	$1,038	$1,231	$258	$310	$284	$1,387	$1,535	$1,830
Total Debt	$8,734	$8,937	$6,081	$1,889	$1,890	$1,875	$2,207	$2,248	$2,002	$3,453	$3,532	$3,965	$3,199	$3,316	$3,344
Cash & Cash Equiv.	$340	$308	$549	$533	$651	$321	$317	$156	$549	$87	$104	$268	$111	$871	$732
EBIT Margin	4.4%	-8.3%	-9.4%	2.9%	4.3%	-0.3%	19.3%	19.8%	22.0%	1.9%	5.0%	5.6%	18.4%	19.2%	20.9%
EBIT / Int. Exp.	0.9x	-1.4x	-1.4x	1.0x	1.3x	-0.1x	9.7x	10.6x	14.3x	0.2x	0.5x	0.4x	10.0x	11.4x	14.1x
Debt / EBITDA	7.4x	21.9x	18.4x	6.1x	5.5x	15.4x	2.3x	2.2x	1.6x	13.4x	11.4x	14.0x	2.3x	2.2x	1.8x
RCF / Net Debt	6.6%	-2.9%	-3.4%	15.1%	18.0%	2.4%	29.5%	29.0%	48.5%	0.3%	0.3%	-3.5%	18.3%	29.8%	36.8%
FCF / Debt	-1.9%	-6.0%	-5.8%	0.8%	2.0%	-6.6%	22.2%	25.2%	36.1%	-6.4%	-2.5%	-4.2%	11.2%	23.2%	24.8%

All figures & ratios calculated using Moody's estimates & standard adjustments. FYE = Financial Year-End. LTM = Last Twelve Months. RUR* = Ratings under Review, where UPG = for upgrade and DNG = for downgrade.
Source: Moody's Financial Metrics™

Exhibit 8

Moody's-Adjusted Debt Breakdown

Coty Inc.

(in US Millions)	FYE Jun-16	FYE Jun-17	FYE Jun-18	FYE Jun-19	FYE Jun-20	LTM Dec-20
As Reported Debt	**4,098.2**	**7,137.4**	**7,524.3**	**7,663.7**	**8,080.4**	**5,341.1**
Pensions	190.1	493.9	489.4	395.0	358.3	358.3
Operating Leases	404.9	653.2	643.9	593.1	422.4	381.4
Non-Standard Adjustments	71.9	78.2	98.9	82.1	75.9	0.0
Moody's-Adjusted Debt	**4,765.1**	**8,362.7**	**8,756.5**	**8,733.9**	**8,937.0**	**6,080.8**

All figures are calculated using Moody's estimates and standard adjustments.
Source: Moody's Financial Metrics™

Exhibit 9

Moody's-Adjusted EBITDA Breakdown

Coty Inc.

(in US Millions)	FYE Jun-16	FYE Jun-17	FYE Jun-18	FYE Jun-19	FYE Jun-20	LTM Dec-20
As Reported EBITDA	**483.7**	**116.7**	**871.6**	**-2,957.4**	**-517.8**	**-621.0**
Pensions	7.4	20.9	6.6	-1.1	-13.2	-17.7
Operating Leases	82.5	166.1	208.2	197.7	97.0	84.2
Unusual	269.5	796.0	495.0	3,936.3	841.7	885.5
Moody's-Adjusted EBITDA	**843.1**	**1,099.7**	**1,581.4**	**1,175.5**	**407.7**	**331.0**

All figures are calculated using Moody's estimates and standard adjustments..
Unusual items include impairment charges and one-time restructuring charges.
Source: Moody's Financial Metrics™

Ratings

Exhibit 10

Category	Moody's Rating
COTY INC.	
Outlook	Stable
Corporate Family Rating	Caa1
Sr Sec Bank Credit Facility	B3/LGD3
Senior Secured	B3/LGD3
Senior Unsecured	Caa3/LGD5
Speculative Grade Liquidity	SGL-4

Source: Moody's Investors Service

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