MOODY'S
INVESTORS SERVICE

Rating Action: Moody's downgrade Coty's CFR to Caa1; outlook negative

09 Apr 2020

New York, April 09, 2020 -- Moody's Investors Service, ("Moody's") today downgraded Coty Inc.'s ("Coty") Corporate Family Rating ("CFR") to Caa1 from B2 and its Probability of Default rating to Caa1-PD from B2-PD. At the same time, Moody's downgraded the company's senior secured term loan and revolver to B3 from Ba3 (LGD2), and its unsecured global notes to Caa3 from Caa1 (LGD5). Coty's Speculative Grade Liquidity Rating remains unchanged at SGL-4. The rating outlook is negative.

The downgrade reflects Moody's view that Coty's financial leverage will increase because of significant declines in revenue and earnings from retail store closures and reduced demand for the company's products related to efforts to contain the coronavirus. The company estimates that 3rd quarter sales, ending March 31, 2020, would be down by 20% and Moody's estimates that year-end sales ending June 30, 2020 will be down in excess of 15%. Moody's expects debt to EBITDA will increase to about 6.5x in 2020 from 5.7x from the twelve months ending December 31, 2019. Lower demand for Coty's products reflects weaker than expected sales and earnings from its consumer beauty products (40% of sales) and from the company's luxury beauty and fragrance products (38% of sales). Demand will be adversely affected by ongoing competitive pressures, closures at department stores and specialty retailers, and governmental recommended social distancing reflecting efforts to contain the coronavirus. Efforts to contain the coronavirus are weakening economic growth globally and add further operating pressure on Coty.

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

Coty Inc.

Ratings Downgraded:

Corporate Family Rating to Caa1 from B2

Probability of Default to Caa1-PD from B2-PD

First Lien Senior Secured Bank Credit Facility to B3 (LGD2) from Ba3 (LGD2)

Guaranteed Unsecured Global Notes to Caa3 (LGD5) from Caa1 (LGD5)

The rating outlook is negative

RATINGS RATIONALE

Coty's Caa1 CFR reflects revenue declines expected for the company's beauty products over the next few quarters driven by efforts to contain the coronavirus and pressure on discretionary consumer income, contributing to high debt to EBITDA financial leverage that Moody's estimates will increase to 6.5x in 2020. The rating also reflects Moody's belief that the company will generate weak free cash flow over the next several quarters due to its ongoing restructuring costs and dividends. Coty's concentration in fragrance and color cosmetics creates exposure to discretionary consumer spending and 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.

The negative outlook reflects Moody's belief that Coty faces high execution risk to improve operating performance and reduce leverage. This reflects the company's multi-step turnaround plan that includes the divestiture of its Professional and Hypermarcas businesses, proceeds of which are to be used to repay debt. The turnaround plans also includes the continued refocus of its Consumer Beauty business product mix away from low-value sales. Moody's also recognizes the challenges that Coty will face executing an operational turnaround given governmental mandates for social distancing that will keep department stores and specialty retail closed for about 6-12 months.

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 to generate negative free cash flow in 2020. The $2.75 billion revolver expiring in 2023 is subject to a maximum total net leverage financial covenant with step downs. The credit agreement is subject to a maximum 5.25x total net leverage covenant that declines to 5.00x in March 2022. The ratio was raised to 5.95x in March 2020, in conjunction with the company's majority acquisition of Kylie Cosmetics, and will return to 5.25x in January 2021. Moody's projects that the company will have weak headroom under the total net leverage covenant over the next 12 months.

In terms of Environmental, Social and Governance (ESG) considerations, the most important factor for Coty's ratings are governance considerations related to its financial policies and board independence. Moody's views 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.

The rapid and widening spread of the coronavirus outbreak, deteriorating global economic outlook, falling oil prices, and asset price declines are creating a severe and extensive credit shock across many sectors, regions and markets. The combined credit effects of these developments are unprecedented. The consumer products sector has been one of the sectors affected by the shock given its sensitivity to consumer demand and sentiment. More specifically, the weaknesses in Coty's credit profile, including its exposure to multiple affected countries have left it vulnerable to shifts in market sentiment in these unprecedented operating conditions and the company remains vulnerable to the outbreak continuing to spread. Moody's regards the coronavirus outbreak as a social risk under our ESG framework, given the substantial implications for public health and safety. Today's action in part reflects the impact on Coty of the breadth and severity of the shock, and the broad deterioration in credit quality it has triggered.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

Coty's ratings could be downgraded if the company is unable to stabilize revenue and earnings or continues to generate weak or negative free cash flow over the next 12-18 months. The ratings could also be downgraded if financial leverage continues to increase. A downgrade could also occur if the company is unable to improve liquidity or continues to pursue material debt funded acquisitions or shareholder returns.

Coty's ratings could be upgraded if the company generates renewed revenue and earnings growth such that comfortably positive free cash flow is restored. Coty would also need to significantly reduce its financial leverage before an upgrade would be considered.

The principal methodology used in these ratings was Consumer Packaged Goods Methodology published in February 2020 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1202237. Alternatively, 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 150 countries. The company generates roughly $8.4 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.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

For ratings issued on a program, series, category/class of debt or security this announcement provides certain regulatory disclosures in relation to each rating of a subsequently issued bond or note of the same series, category/class of debt, security or pursuant to a program for which the ratings are derived exclusively from existing ratings in accordance with Moody's rating practices. For ratings issued on a support provider, this announcement provides certain regulatory disclosures in relation to the credit rating action on the support provider and in relation to each particular credit rating action for securities that derive their credit ratings from the support provider's credit rating. For provisional ratings, this announcement provides certain regulatory disclosures in relation to the provisional rating assigned, and in relation to a definitive rating that may be assigned subsequent to the final issuance of the debt, in each case where the transaction structure and terms have not changed prior to the assignment of the definitive rating in a manner that would have affected the rating. For further information please see the ratings tab on the issuer/entity page for the respective issuer on www.moodys.com.

For any affected securities or rated entities receiving direct credit support from the primary entity(ies) of this credit rating action, and whose ratings may change as a result of this credit rating action, the associated regulatory disclosures will be those of the guarantor entity. Exceptions to this approach exist for the following disclosures, if applicable to jurisdiction: Ancillary Services, Disclosure to rated entity, Disclosure from rated entity.

The ratings have been disclosed to the rated entity or its designated agent(s) and issued with no amendment resulting from that disclosure.

These ratings are solicited. Please refer to Moody's Policy for Designating and Assigning Unsolicited Credit Ratings available on its website www.moodys.com.

Regulatory disclosures contained in this press release apply to the credit rating and, if applicable, the related rating outlook or rating review.

Moody's general principles for assessing environmental, social and governance (ESG) risks in our credit analysis can be found at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1133569 .

At least one ESG consideration was material to the credit rating outcome announced and described above.

The Global Scale Credit Rating on this Credit Rating Announcement was issued by one of Moody's affiliates outside the EU and is endorsed by Moody's Deutschland GmbH, An der Welle 5, Frankfurt am Main 60322, Germany, in accordance with Art.4 paragraph 3 of the Regulation (EC) No 1060/2009 on Credit Rating Agencies. Further information on the EU endorsement status and on the Moody's office that issued the credit rating is available on www.moodys.com.

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MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.