MOODY'S INVESTORS SERVICE

Credit Opinion: Localiza Rent a Car S.A.

Global Credit Research - 02 Mar 2016

Belo Horizonte, Brazil

Ratings

Category	Moody's Rating
Outlook	Negative
Corporate Family Rating	Ba2
Senior Unsecured -Dom Curr	Ba2
NSR Corporate Family Rating	Aa2.br
NSR Senior Unsecured	Aa2.br

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Key Indicators

[1]**Localiza Rent a Car S.A.**

	9/30/2015(L)	12/31/2014	12/31/2013	12/31/2012
Revenue (USD Billion)	$1.3	$1.7	$1.6	$1.6
Pretax Income % of Sales	13.7%	14.8%	15.4%	10.3%
Debt / EBITDA	2.5x	2.5x	2.4x	2.3x
FFO / Debt	14.8%	17.2%	21.1%	20.5%
EBITDA / Interest	3.3x	4.2x	5.4x	4.9x

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Source: Moody's Financial Metrics

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

-Stable operating performance and history of resilient business model during stress scenarios

-Large unencumbered asset base with good liquidity

-Strong market share position both in the car and fleet rental segments

-Steep slowdown in the Brazilian economy and in the automotive market

-Positive fundamentals supporting continued growth of the Brazilian car rental industry

Corporate Profile

Localiza Rent a Car S.A. (Localiza), founded in 1973 and headquartered in Belo Horizonte, Minas Gerais, Brazil, operates car rental, fleet rental, and used car businesses in Brazil. It also franchises rental car operations throughout Latin America. As of September 30, 2015, Localiza had a total fleet of 104,274 company-owned cars and 13,175 cars from franchisees in Brazil and other seven countries. Localiza is the market leader in Brazil for both car and fleet rental with the largest number of car rental locations and presence at the principal Brazilian airports. For the last twelve months ended September 30, 2015, Localiza reported net revenues of BRL 4.0 billion and net income of BRL 399 million.

SUMMARY RATING RATIONALE

Localiza's rating is supported by the company's stable operating performance and resilient business model, which entails relatively stable cash flows and more flexible operations - a positive, especially during the current scenario of auto market slowdown. Localiza's leading market share position in both the car and fleet rental segments also supports the rating. The company continues to maintain robust profitability as a result of low fleet maintenance requirements, high utilization rates, attractive discounts from automobile manufacturers and expertise on the used cars sales market. The ratings also reflect the company's adequate corporate governance practices and strong liquidity position.

On the other hand, the capital intensive nature of the car rental business constrains Localiza's ratings, as does the company's small size when compared to its global industry peers and the lack of significant international footprint. The rating is further pressured by the expected more challenging environment for the automotive industry until at least the end of 2016 and weaker than expected economic prospects for Brazil for the next couple of years.

DETAILED RATING CONSIDERATIONS

CONSOLIDATED LEADING POSITION IN ATTRACTIVE SEGMENTS

Although Localiza is one of the smallest globally rated car rental companies in terms of revenues, it enjoys a dominant position in the fragmented Brazilian car and fleet rental industry, with a market share of approximately 25.7% in the car rental segment. We estimate that this market share, supported by its strong brand name, is more than twice the share of its next-largest competitor. Localiza operates in four main businesses: short-term car rental, fleet rental, franchising and used-car sales.

On the car rental segment, the company has 490 agencies in Brazil as of September, 2015, benefiting from a well-diversified distribution network with strategic locations across the country granting access to both the on and off-airport markets, including the replacement car market for insurance companies. The fleet rental business is also likely to experience consistent growth rates supported by the low penetration of rented fleet in Brazilian companies.

SLOWDOWN IN THE BRAZILIAN ECONOMY AND IN THE AUTOMOTIVE MARKET

The Brazilian economy is expected to contract around 3.5% in 2015 and another 3.0% in 2016 while the automotive industry is being severely impacted. The sale of new vehicles decreased by almost 24% in 2015 and the slowdown is expected to persist through 2016 with expectations of another 7.5% decrease, according to ANFAVEA.

The integrated business model allows Localiza to minimize losses at the regular disposal of the used vehicles and to guarantee a structured market for a large fleet divesture, especially in the current scenario of economic deceleration. For example, during the downturn caused by the credit crisis in 2009, the company sustained strong margins and increased liquidity by unloading its fleet. This time around, the company has been able to replicate the strategy and in the first nine months of 2015, Localiza purchased 42,372 cars and sold 49,258 cars, mainly through its used car network of 76 stores, reducing its fleet size while increasing liquidity and maintaining utilization rates at sustainable levels, demonstrating the management's expertise in navigating through the cycles.

While Localiza's growth strategy and cash flow generation is concentrated in its car and fleet rental businesses, responsible for around 47% of net revenues, the company's franchising business, that represents less than 1% of net revenues, is strategic in terms of consolidating Localiza's brand, exploring new markets and increasing distribution. The other 53% of net revenues comes from the used-car sales division, that has been gaining space in 2015, emerging as an alternative to the purchase of a new car during periods of rising interest rates, weak consumer confidence and lower credit availability as buyers become more conservative and concerned about indebtedness.

In the first nine months of 2015, Localiza's sold fleet age averaged 14.5 months in the car rental division. The company's high inventory turnover evidences its ability to reduce its fleet in a timely manner, maintaining low depreciation expenses. The return of the IPI tax rates on new cars since January 1st, 2015, the increase of industry costs and higher inflation raised the price of new vehicles and ended up reflecting on the prices of used cars as well, increasing the value of Localiza's fleet. At the end of 2014, Localiza anticipated the purchase of 7,600 cars in order to make the most of the lower IPI taxes and keep renewing its fleet.

A worse than expected deterioration in used car sales for a prolonged period could negatively impact Localiza's profitability and liquidity. The company's experience towards pricing of its used vehicles will play a key role in maintaining liquidity, profitability and fleet size at adequate levels.

LARGE SIZE, SCALE AND DIVERSIFICATION PROVIDE BARGAINING POWER

The capital intensive nature of the automobile rental industry requires companies operating in this sector to have strong oversight towards fleet management and secondary market prices. Car manufacturers in Brazil do not provide repurchase or guaranteed depreciation arrangements. As the single largest car buyer in Brazil, Localiza benefits from large purchase discounts from car manufacturers, which can be as high as 20%. In the nine months ended September 30, 2015, the company invested BRL 1.4 billion to buy 42,372 cars. Localiza is Brazil's largest single auto purchaser with 4% of the five largest car manufactures (GM, VW, Renault, Ford and Fiat) sales in Brazil in the nine months ended September 30, 2015.

GOOD LEVEL OF CORPORATE GOVERNANCE STANDARDS

Localiza has a good level of transparency and adequate quarterly financial disclosures. The company's shares are traded on BM&FBovespa and comply with the Novo Mercado standards, the highest corporate governance level in the local equity market. Localiza has a board of directors comprised of eight members, of which four are considered independent by the BM&FBovespa standards. Additionally, the company has a permanent audit committee with three members, being two independent members.

ADEQUATE LIQUIDITY SUPPORTED BY LARGE UNENCUMBERED ASSET BASE

At the end of September 2015 Localiza had BRL 1.3 billion in cash and equivalents on its balance sheet, more than enough to pay down its short term debt of BRL 369 million. Such large cash position adequately covers all debt maturities until the end of 2018. Additionally, Localiza's consolidated fleet of 104,274 vehicles (both in the car and fleet rental divisions) is mostly unencumbered with an estimated value of BRL 3.3 billion, being an alternative source of liquidity. Localiza's cash balance plus its unencumbered fleet value comfortably covers its total Moody's adjusted debt of around BRL 3.1 billion by 1.4 times.

Rating Outlook

The negative outlook reflects the change in outlook of Brazil's government bond rating to negative.

What Could Change the Rating - Up

An upgrade of Localiza's ratings would depend on an upgrade of Brazil's government bond rating. In addition, positive rating momentum would be triggered by further gains in market share, geographic diversification and revenues while maintaining healthy credit metrics on a sustained basis. The implementation of financial policies that include maximum leverage and minimum cash amounts, as well as a long-term committed bank credit facility that would reduce reliance on capital markets to refinance existing debt maturities, would also be considered as an enhancement to the company's liquidity profile and overall credit quality.

What Could Change the Rating - Down

Localiza's ratings could come under downward pressure if Brazil's government bond rating should be further downgraded, or if Localiza fails to reduce its fleet size during a major downturn in the Brazilian car rental market, such as car rental utilization rates fall below the 60% range for a prolonged period (70.7% in September 2015). Quantitatively, Localiza's rating could come under downward pressure if EBITDA interest coverage falls below 3.0 times or if Gross Debt to EBITDA exceeded 3.5 times on a sustained basis.

Other Considerations

MAPPING TO MOODY'S EQUIPMENT AND TRANSPORTATION RENTAL INDUSTRY METHODOLOGY

The grid implied rating from Moody's 12-18 month forward view of the Equipment and Transportation Rental Industry Methodology is Ba1, which is one notch higher than Localiza's assigned senior unsecured ratings. The one notch difference from Localiza's Ba2 rating and the grid implied rating of Ba1 is explained by the constraint deriving from Brazil's Ba2 government bond rating due to Localiza's operations being highly correlated with the Brazilian economy.

Rating Factors

Localiza Rent a Car S.A.

Equipment and Transportation Rental Industry Grid [1][2]	**Current LTM 9/30/2015**		[3]**Moody's 12-18 Month Forward ViewAs of 2/18/2016**	
Factor 1 : Scale (10%)	**Measure**	**Score**	**Measure**	**Score**
a) Revenue (USD Billion)	$1.3	Ba	$1 - $5	Ba
Factor 2 : Business Profile (20%)				
a) Business Profile	A	A	A	A
Factor 3 : Profitability (10%)				
a) Pretax Income % of Sales	13.7%	Ba	10% - 15%	Ba
Factor 4 : Leverage and Coverage (45%)				
a) Debt / EBITDA	2.5x	Ba	2x - 3x	Ba
b) FFO / Debt	14.8%	B	8% - 20%	B
c) EBITDA / Interest	3.3x	B	2x - 4x	B
Factor 5 : Financial Policy (15%)				
a) Financial Policy	Baa	Baa	Baa	Baa
Rating:				
a) Indicated Rating from Grid		Ba1		Ba1
b) Actual Rating Assigned		Ba2		-

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] As of 9/30/2015(L); Source: Moody's Financial Metrics [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

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the ratings tab on the issuer/entity page on http://www.moodys.com for the most updated credit rating action information and rating history.

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