

Coca-Cola Femsa

Strong 4Q23 – upgrade KOF to Overweight on growth, execution, valuation

Rating Change - Credit

Guatemala volumes keep growing double digits

In 4Q23, total volumes were +6% YoY, with core markets (78% of total) Mexico and Brazil growing +5% and +8% YoY, respectively. Guatemala volumes grew double digits (+13% YoY) for the 7th quarter in a row, now accounting for 4% of total volumes. C. America South was +8% YoY while Argentina (5% of total vols) was -1% YoY on macroeconomic headwinds to consumption. And despite a sugar-added beverage tax that came into effect in Nov-23, Colombia volumes still grew +8% YoY. Avg. prices (US\$-terms) were +14% YoY in the quarter, partially due to a strong MXN. See Exhibit 7 through Exhibit 9.

EBITDA margins stable, despite sweetener cost inflation

Revenues in 4Q23 were US\$1.1bn (+21% YoY) on volume growth and a stronger MXN. Mexico/C. America revenues were +25% YoY, while S. America was +16% YoY. While COGS and Opex continued to experience inflationary pressure (+17% and +28% YoY, respectively), noting higher sweetener and labor/marketing/maintenance costs, packaging costs eased. EBITDA was +23% YoY, with margins expanding +37bps.

Leverage very conservative; no near-term maturities

Total debt in 4Q23 was US\$3.8bn (+1% QoQ), with no major maturities until beyond 2027 (Exhibit 12). We flag 61% of debt in MXN, 21% in BRL and only 16% in USD, noting KOF generates revenues in local FX only. The cash position was significant at US\$1.8bn (-17% QoQ) versus ST Debt of US\$8mm. Gross and net leverage were 1.5x and 0.8x (vs 1.5x and 0.6x in 3Q23). Free Cash Flow (FCF) in 4Q23 was -US\$344mm (vs -US\$174mm in 4Q22) on higher EBITDA, offset by higher capex (+30% YoY), cash taxes (+111% YoY) and dividends (+21% YoY).

24E: Mid-single-digit MX vol growth; sugar = headwind

We expect Mexico (50% of total vols) to grow at mid-single digits in 24E, and KOF expects “strong demand” in Brazil (30% of total vols). Argentina (5% of vols) is expected to face headwinds in 1H24E, with a gradual, sequential improvement in 2H24E. On pricing, KOF is focused on sustainable growth in a relative competitive position, while moving away from practices of pushing pricing. On costs, packaging is expected to continue easing, while sugar will continue to be a headwind. However, KOF has a “pretty healthy hedge position” for 2024E on most hedgeable raw materials.

Upgrade KOF to OW on growth, execution, valuation

We like KOF's track record and outlook for solid growth for a food company in core markets (Mexico, Brazil) as well as exposure to smaller, but higher-growth potential markets (Guatemala, Colombia). KOF has proven a very strong operator, executing successfully on affordability strategies, price/mix optimization, cost efficiencies with digitalization initiatives, and ESG-related targets/goals. We believe valuation is attractive versus US Single A Corporates Index (COA3), Mexico IG Index (EMXI) and LatAm IG Beverage peers (Exhibit 3 through Exhibit 6).

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Global Emerging Markets | Corporate Credit
LatAm | Mexico
Consumer Products

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Coca-Cola Femsa (KOF)			
Key Data	2021A	2022A	2023A
Operating (US\$ mm)			
Revenues	9,605	11,267	13,808
EBITDA	1,915	2,137	2,615
CapEx	684	977	1,205
Balance Sheet (US\$ mm)			
Cash	2,309	2,067	1,834
Total Debt	4,192	4,037	3,851
Short Term Debt	120	437	8
Net Leverage	1.0x	0.9x	0.8x

Source: Company filings & BofA Global Research.

Exhibit 1: Bond Pricing Table

We upgrade KOF bonds to Overweight.

Bond	Rec	Price	YTW	Z-Spr
KOF '30	OW	88.3	5.01	104
KOF '32	OW	77.7	5.04	115
KOF '43	OW	97.3	5.39	152

Source: BofA Global Research, Bloomberg.
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Refer to important disclosures on page 6 to 8. Analyst Certification on page 5. Valuation & Risk on page 4.

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Timestamp: 26 February 2024 03:46PM EST

Valuation

Exhibit 2: Bond Pricing Table

We upgrade KOF bonds to Overweight.

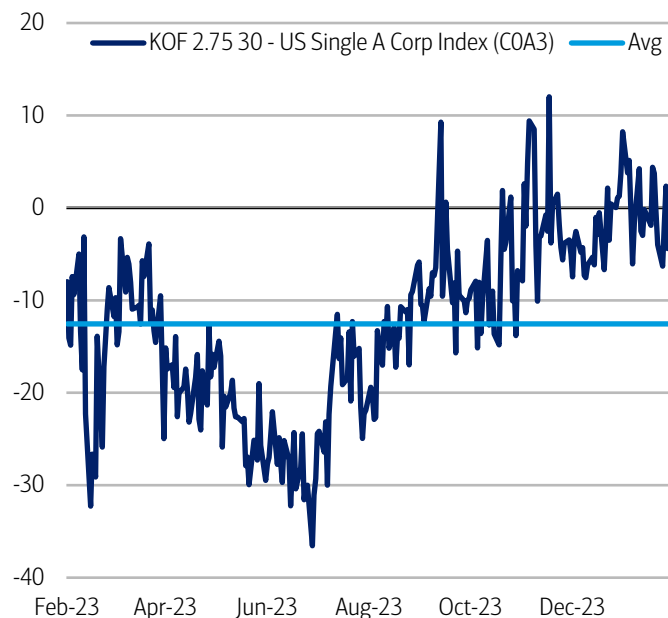
Bond	Rec	Coupon	Maturity	Amt O/S	Price	YTW	Z-Sprd	Mod Dur	Credit Rating
KOF '30	OW	2.750	1/22/2030	1,041	88.3	5.01	104	5.3	A3//A
KOF '32	OW	1.850	9/1/2032	705	77.7	5.04	115	7.5	A3//A
KOF '43	OW	5.250	11/26/2043	489	97.3	5.39	152	12.0	A3/A-/A
<u>LatAm IG Bev</u>									
ANDINA '50	NR	3.950	1/21/2050	300	74.8	5.75	198	14.4	/BBB/BBB+
CCUCI '32	NR	3.350	1/19/2032	600	85.3	5.55	164	6.7	/BBB/A-
<u>LatAm IG Food</u>									
SIGMA '26	MW	4.125	5/2/2026	1,000	96.7	5.69	118	2.0	Baa3/BBB-/BBB
SIGMA '28	MW	4.875	3/27/2028	500	97.3	5.51	139	3.6	Baa3/BBB-/BBB
BIMBOA '29	NR	6.050	1/15/2029	900	102.8	5.29	123	4.1	Baa1/BBB+/BBB+
BIMBOA '44	MW	4.875	6/27/2044	500	88.6	5.79	193	12.2	/BBB+/BBB+
<u>Mexico Sovereign</u>									
MEX '29	-	4.500	4/22/2029	3,086	96.3	5.21	119	4.5	Baa2/BBB/BBB-
MEX '44	-	4.750	3/8/2044	3,715	82.6	6.23	237	11.7	Baa2/BBB/BBB-
<u>Coca Cola (KO)</u>									
KO '30	-	3.450	3/25/2030	1,250	93.2	4.68	71	5.3	A1/A+/WD
KO '40	-	2.500	6/1/2040	1,000	72.0	5.01	113	12.4	A1/A+/WD

Source: BofA Global Research, Bloomberg, O/S = outstanding.

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Exhibit 3: KOF '30 – US Single A Corp Index (COA3): Historical Spread

KOF now looks cheap vs US A rated corporates.

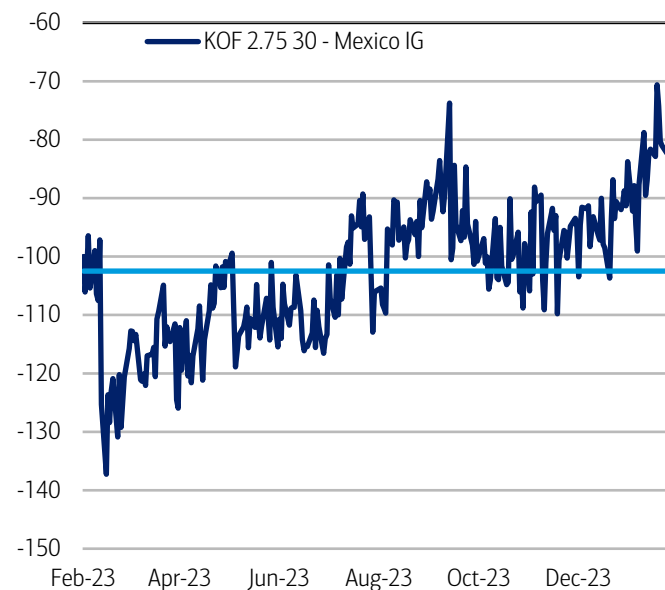


Source: BofA Global Research, Bloomberg.

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Exhibit 4: KOF '30 – Mexico IG Index (EMXI): Historical Spread

KOF also looks cheap vs EMXI.

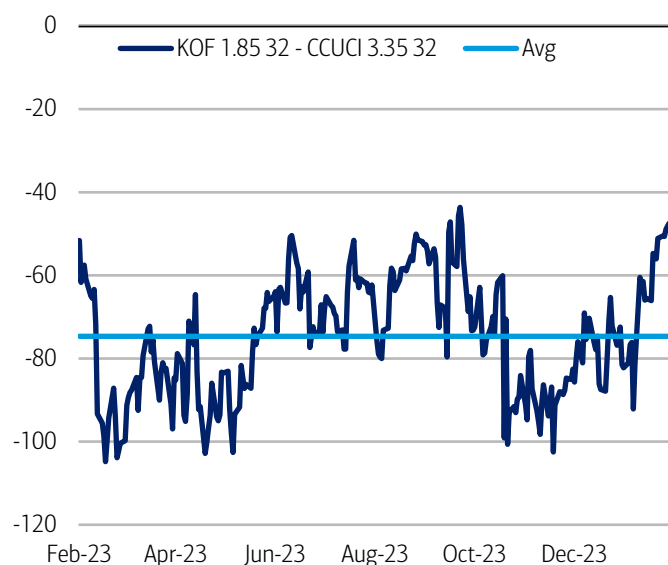


Source: BofA Global Research, Bloomberg.

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Exhibit 5: KOF '32 – CCUCI '32: Historical Spread

KOF looks cheap vs IG LatAm beverage peer, CCUCI.

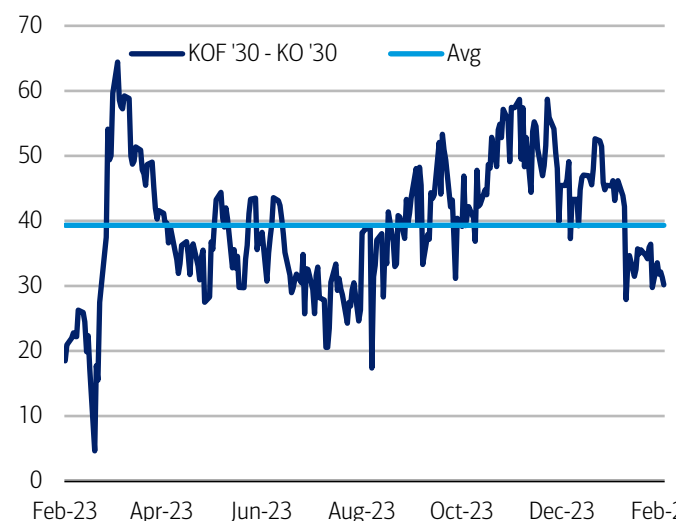


Source: BofA Global Research, Bloomberg.

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Exhibit 6: KOF '30 – KO '30: Historical Spread

KOF offers a 30bps spread pick-up over Coca-Cola (KO).



Source: BofA Global Research, Bloomberg.

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Appendix

Exhibit 7: KOF – Financial Summary (US\$ mm, unless noted)

Quarterly and LTM metrics.

	4Q22	3Q23	4Q23	LTM	YoY	QoQ
Vol (mn cases)	995	1,033	1,056	4,048	6.1%	2.2%
Revenues	3,110	3,683	3,765	13,989	21.1%	2.2%
EBITDA	607	693	749	2,652	23.3%	8.1%
EBITDA mg (%)	19.5%	18.8%	19.9%	19.0%	37	108
Int Expense	93	100	102	404	9.6%	2.0%
Capex	431	292	560	1,226	30.0%	92.2%
Cash	2,067	2,218	1,834	1,834	-11.3%	-17.3%
ST Debt	437	2	8	8	-98.1%	278.1%
LT Debt	3,600	3,805	3,843	3,843	6.8%	1.0%
Total Debt	4,037	3,807	3,851	3,851	-4.6%	1.2%
Net Debt	1,970	1,589	2,017	2,017	2.4%	26.9%
Equity	6,767	7,528	7,895	7,895	16.7%	4.9%
EBITDA/Int (x)	6.52	6.93	7.34	6.56		
Cash/ST Debt (x)	5	1,014	222	222		
TD/EBITDA (x)	1.89	1.52	1.45	1.45		
ND/EBITDA (x)	0.92	0.63	0.76	0.76		

Source: BofA Global Research, company reports.

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Exhibit 8: KOF – Key Metrics by Region (mm unit cases, unless noted)

C. America continues growing at double-digits YoY in 4Q23.

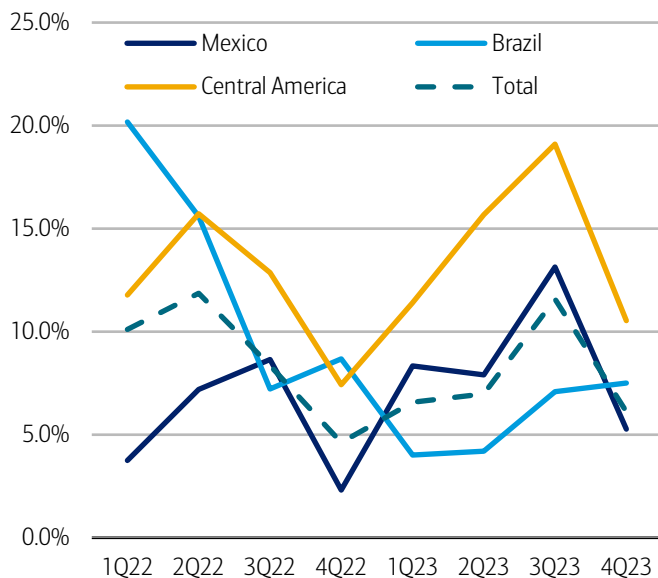
	4Q22	3Q23	4Q23	% YoY	% QoQ
Volume (mm cases)					
Mexico	468.7	545.3	493.4	5.3%	-9.5%
C. America	79.2	88.0	87.5	10.5%	-0.5%
Total Mexico & C. America	547.9	633.2	580.9	6.0%	-8.3%
Colombia	85.4	91.0	91.9	7.6%	0.9%
Brazil	295.8	255.9	318.0	7.5%	24.3%
Argentina	51.6	41.0	51.1	-1.0%	24.7%
Uruguay	14.7	12.0	14.4	-2.1%	20.4%
Total S. America	447.4	399.9	475.3	6.2%	18.9%
Total Volumes	995.3	1,033.1	1,056.2	6.1%	2.2%
Mexico & C. America					
Volume (mm unit case)	547.9	633.2	580.9	6.0%	-8.3%
Avg. price (US\$/unit case)	\$3.13	\$3.61	\$3.69	17.7%	2.1%
Revenues (US\$ mm)	1,717	2,287	2,143	24.9%	-6.3%
EBITDA (US\$ mm)	351	479	439	25.2%	-8.4%
M&CA EBITDA margin	20.4%	21.0%	20.5%	5	(48)
South America					
Volume (mm unit case)	447.4	399.9	475.3	6.2%	18.9%
Avg. price (US\$/unit case)	\$3.11	\$3.49	\$3.41	9.6%	-2.3%
Revenues (US\$ mm)	1,393	1,396	1,621	16.4%	16.2%
EBITDA (US\$ mm)	257	214	310	20.9%	45.1%
SA EBITDA margin	18.4%	15.3%	19.1%	71	382

Source: BofA Global Research, company reports.

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Exhibit 9: KOF Volume Growth (% YoY)

4Q23 volumes were +6% YoY.

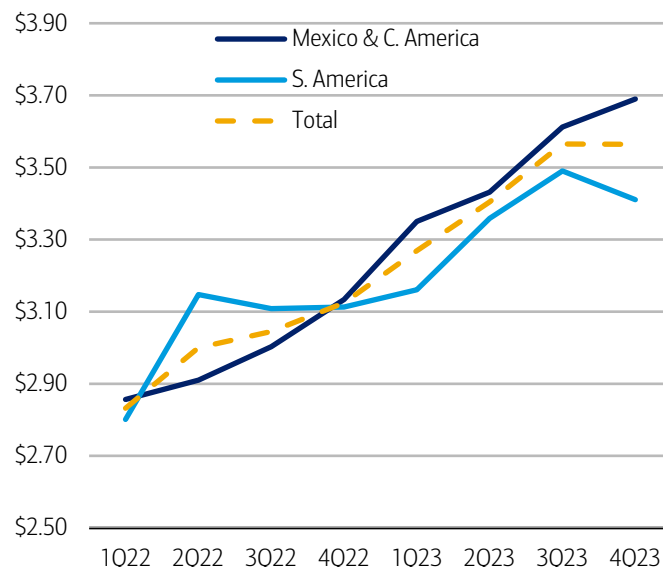


Source: BofA Global Research, company reports.

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Exhibit 10: KOF Average Price (US\$/case)

Avg price/case in 4Q23 was +14% YoY, partially driven by a strong MXN.

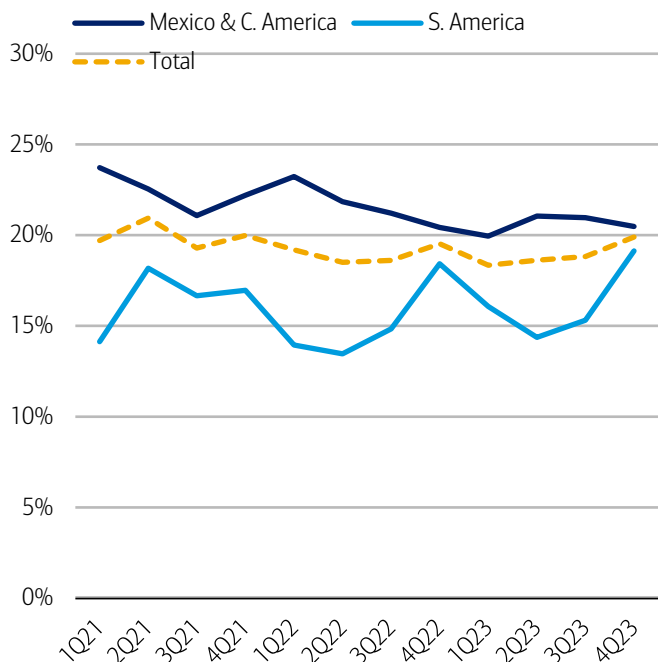


Source: BofA Global Research, company reports.

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Exhibit 11: KOF EBITDA Margin (%)

Consolidated EBITDA margin remains stable.

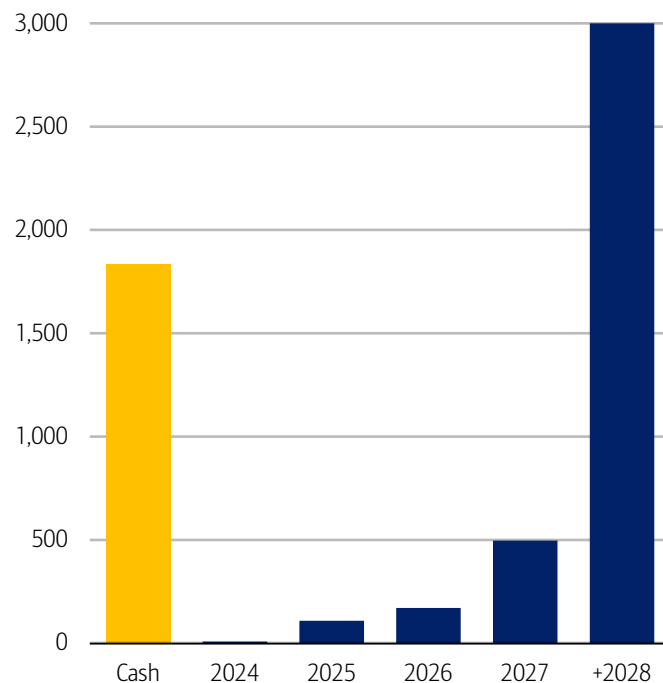


Source: BofA Global Research, company reports.

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Exhibit 12: KOF Cash and Debt Maturities (US\$ mm)

KOF has ample cash on hand and no major maturities until after 2027.



Source: BofA Global Research, company reports.

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Valuation & risk**Coca-Cola Femsa (KOF)**

KOF benefits from strong operations and strategic importance to The Coca-Cola Company (KO), as one of the largest bottlers outside the U.S. Fundamentals are strong and we expect credit metrics to remain in line with the company's A- rating category. We expect in 24E solid volume growth in core markets (Mexico, Brazil), and like exposure smaller, but higher-growth markets like Guatemala and Colombia. We expect packaging costs ease, while sugar cost remains a headwind in 24E, but note the company has much of its raw material costs hedged. We view valuation as attractive vs LatAm IG peers and Mexico IG index. Consequently, we are Overweight on KOF '30, '32 & '43s.

Upside risks: (1) continued traffic recovery of on-premise channel, (2) faster adoption of digital sales channels by customers, (3) successful expansion into distribution of alcoholic beverages, (4) faster adoption of profitable distribution pilot projects, (5) stronger macroeconomic performance in countries of operation, (6) stronger FX in countries of operation, (7) lower-than-expected raw material prices.

Downside risks: (1) weaker local currencies, (2) higher raw material costs, (3) adverse macro conditions in countries of operations, (6) increasing competition, (7) acquisitions and the risk of higher leverage, (8) unfavorable legislation towards consumption and/or labeling of sugar-containing beverages, (9) rating downgrades.

Analyst Certification

I, Peter Bowley, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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Security/Loan pricing

Coca-Cola Femsa / KOF

	Amt		Ratings			Yield	Spread
Security		Maturity date	Moody's/S&P/Fitch	Price	Price date	(%)	(bps)
5.25, Senior, USD, 2043:B	600	26-NOV-2043	A3/A-/A	96.88	23-Feb-2024	5.51	97
2.75, Senior, USD, 2030:B	1,250	22-JAN-2030	A3/NR/A	88.33	23-Feb-2024	5.06	78
1.85, Senior, USD, 2032:B	705	01-SEP-2032	A3/NR/A	77.73	23-Feb-2024	5.11	86

For pricing information refer to "Other Important Disclosures" below.

B=Bond; L=Loan; CS=Capital Security (Not including Equity Preferred); CDS=Credit Default Swap; EP=Equity Preferred

Disclosures

Important Disclosures

Credit opinion history

Coca-Cola Femsa / KOF

Security	Date ^{R1}	Action	Recommendation	Price
5.25, Senior, USD, 2043:B	31-Jan-2023		Marketweight	
2.75, Senior, USD, 2030:B	31-Jan-2023		Marketweight	
1.85, Senior, USD, 2032:B	31-Jan-2023		Marketweight	

Table reflects credit opinion history as of previous business day's close.^{R1} First date of recommendation within the last 36 months, if for an issuer or within the last 12 months, if for a security or loan. The investment opinion system is contained at the end of the report under the heading "BofA Global Research Credit Opinion Key."

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B=Bond; L=Loan; CS=Capital Security (Not including Equity Preferred); EP=Equity Preferred; CDS=Credit Default Swap

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Corporate Credit Issuer Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R2}	Count	Percent
Buy	144	37.21%	Buy	119	82.64%
Hold	193	49.87%	Hold	163	84.46%
Sell	50	12.92%	Sell	37	74.00%

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