Credit Opinion: Servicios Corporativos Javer, S.A.P.I. de C.V.

Global Credit Research - 08 Apr 2013

Monterrey, Mexico

Ratings

Category	**Moody's Rating**
Outlook	Negative
Senior Unsecured	B1

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Key Indicators

Servicios Corporativos Javer, S.A.P.I. de C.V.

	[1]**2012**	**2011**	[2]**2010**	[2]**2009**	[2]**2008**
Total Revenues (Ps$ mil.)	**5,090**	**4,719**	**4,674**	**4,932**	**4,473**
Recurring EBITDA (Ps$ mil.)	**722**	**896**	**873**	**1,022**	**1,108**
Recurring EBITDA % Revenue	**14.2%**	**19.0%**	**18.7%**	**20.7%**	**24.8%**
Total Debt/Recurring EBITDA (X)	**4.31x**	**3.74x**	**2.98x**	**2.33x**	**1.99x**
Recurring EBITDA/Fixed Charges (X)	**1.41x**	**1.82x**	**2.04x**	**2.99x**	**3.35x**
Total Assets (Ps$ mil.)	**6,763**	**7,129**	**5,877**	**4,965**	**5,139**
Secured Debt % Gross Assets	**1.1%**	**1.5%**	**0.9%**	**2.2%**	**42.9%**
Total Debt % Total Assets	**46.0%**	**47.0%**	**44.3%**	**47.9%**	**42.9%**

[1] For the last twelve month period ended December 31, 2012. [2] Restated for IFRS, which Javer adopted 1/1/11

Opinion

SUMMARY RATING RATIONALE

Moody's B1 senior unsecured debt rating reflects Servicios Corporativos Javer, S.A.P.I. de C.V.'s ("Javer") leading presence in Northeastern Mexico, particularly the state of Nuevo Leon, which is home to Mexico's third-largest metropolitan area, as well as the company's excellent liquidity position. The company specializes in the construction and commercialization of affordable entry level housing units as well as middle income and residential housing units. These positive factors are offset by weaker sales progress in certain Northern cities due to increasing drug-related violence in the region as well as limited subsidies in Javer's target markets. Other challenges include the need to invest capital in land, licenses, permits and infrastructure, which depending on the region can be costly, as well as the risk of finding homebuyers.

In March 2013, Moody's confirmed the senior unsecured debt rating of Servicios Corporativos Javer, S.A.P.I. de C.V. ("Javer"). Moody's concurrently assigned a B1 rating to Javer's proposed US$50 million add-on to its existing senior unsecured notes dues 2021. The rating outlook is negative. This concluded the review which began on December 3, 2012. The confirmation of the B1 rating reflects the fact that Javer, upon completion of the proposed ViveICA, S.A. de C.V. ("ViveICA") transaction, will be one of the largest players in the industry with a more diversified portfolio, stronger leverage and interest coverage metrics and neutral to positive free cash flow.

Credit Strengths

The key credit strengths for Javer are:

- Over 35 years of real estate experience, with a dominant position in the state of Nuevo Leon

- Javer's debt maturity schedule post its US$ issuances has insignificant debt coming due until 2021, creating minimal liquidity risk

- Targets mainly low- and low to middle-income buyers, which are thriving demographic sectors

- As a result of the acquisition of ViveICA it will be one of largest players in the industry

Credit Challenges

The key credit challenges for Javer are:

- Concentration in Northern states of Nuevo Leon and, in particular, Tamaulipas, where drug-related violence has deterred home buying, which is somewhat mitigated with the acquisition of ViveICA

- Lack of subsidies in target markets has resulted in a shift to higher-income housing development

- Privately-owned developer, which deters transparency

- Heavy funding concentration with INFONAVIT take-out financing of low and middle-income housing, as timing of funding inflows could range from 3-6 months, which can create liquidity problems short-term

- Certain amount of speculative inventory as INFONAVIT allocates mortgages in certain regions and/or projects, however it is up to Javer to find buyers

Rating Outlook

The negative rating outlook reflects continued difficulty for Javer in meeting sales targets which has resulted in weaker than expected credit metrics, including Net Debt/EBITDA, Interest Coverage and EBITDA Margins. The fourth quarter of 2012 was challenging for the sector as a whole due to fewer subsidies allocated than what was projected as well as a new federal government that took office which slowed down the operations of the main housing agencies. In addition, demand for middle-income homes in the areas where Javer operates is still slow to recover and demand has not returned to pre-recession levels. Over 40% of Javer's revenues came from middle-income home sales in 2012. Competition is strong from regional players which has also factored into weak sales. Despite the ViveICA transaction, Javer continues to have a high concentration in the state of Nuevo Leon.

What Could Change the Rating - Up

Upward rating movement is unlikely in the intermediate term. A return to a stable rating outlook would be predicated upon the company maintaining EBITDA margins at or above 15%, while at least maintaining its current credit metrics. A smooth integration of the ViveICA portfolio would also be necessary for a stable rating outlook.

What Could Change the Rating - Down

A negative rating movement will occur should Javer encounter further challenges in reaching titling and sales targets which result in a weakening of credit metrics from current levels such that EBITDA margins fall below 15% and/or debt/EBITDA increases to or surpasses 4x, all on a sustained basis. Any challenges in the integration of the ViveICA acquisition would also cause negative rating pressure.

DETAILED RATING CONSIDERATIONS

Key factors influencing Javer's rating and outlook include:

Liquidity & Funding

Javer has an excellent liquidity position. A combination of cash flow from operations and one bank line are used primarily to fund construction. The company also has a US$210 million unsecured bond due in 2021 that was refinanced in 2011 through the execution of an exchange offer in which an additional US$30 million was issued under the same terms as the new notes. Currently, over 90% of the company's debt maturities are due in 2021, a credit positive. Mortgage financing as of December 31, 2012 comes mainly from government entities and is broken down as approximately 96% Mexican Workers' Housing Fund (INFONAVIT) and 4% sofoles/banks, FOVISSSTE and co-financing products. Javer expects its mortgage financings from INFONAVIT to remain stable in the future. This includes all of the INFONAVIT products such as "apoyo INFONAVIT" and "Cofinanciamiento". Concentration with INFONAVIT is a concern because the company relies on it and other government entities to fund the take-out financing for newly built homes. This process can often take 3-6 months which could create short-term liquidity problems.

Leverage & Capital Structure

Javer's capital structure remains solid for its rating category. Javer's total debt as a percentage of gross assets as of December 31, 2012, was approximately 46.0%, while Debt/EBITDA (LTM) was 4.31x. After considering cash on hand, Net Debt/EBITDA (LTM) was 3.74x.

Market Positioning

Javer has a leading presence in Northeastern Mexico, particularly in Nuevo León with a 15% market share in loans granted by INFONAVIT in the state. Nuevo Leon is home to Mexico's third-largest metropolitan area, Monterrey (the state's capital), which is considered the business and banking center of northern Mexico and which is a large driver of job growth in the region. However, Javer's sales have been negatively affected over the past two years in certain regions of Nuevo Leon as well as the state of Tamaulipas, both states which share a border with the U.S., where drug-related violence and thus security concerns have resulted in a decline in job growth. This challenge will be mitigated by the acquisition of ViVeICA's low-income housing developments as Javer will have 46 developments in 11 states nationwide, 20 of them from ViveICA, and further strengthen its presence in Central and Southern Mexico while diversifying out of Nuevo Leon, a market that has struggled over the past two years. As of December 31, 2012, the company's land reserves is sufficient to build approximately 117,804 units, or approximately seven years worth of construction. A considerable portion of this land bank is in troubled regions such as Tamaulipas and therefore is a concern. Positively, the company has made efforts to diversify into other states, including the State of Mexico, Queretaro and Jalisco, with the ViveICA acquisition adding to this effort.

Sustainability of Cash Flow & Earnings

Javer's EBITDA margins declined to 14.2% at YE 2012 from 19.0% at YE 2011 due to lower subsidy availability in the regions where the company operates coupled with lack luster demand. The low-income housing construction industry has also become increasingly competitive, particularly as most homebuilders shift to low-margin affordable housing construction, causing profit margin pressure for Javer. In 2012 32% of units were sold with a subsidy of which 76% was for vertical construction. Javer's sales mix for the year ended December 31, 2012 was approximately 44% affordable entry-level homes and 41% middle-income homes -- segments of the market where the greatest demand lies -- as well as 8% residential and 7% commercial lot sales. It is important to note that under Javer's operating model, its product mix pricing is lower than the standard market pricing, placing a majority of its sales in the low income to high-low income price range.

External Factors

Javer is a privately owned company, which in Moody's opinion deters the company's corporate governance and thus transparency. Moody's feels that management has implemented efficient controls and possesses good knowledge of the Mexican housing industry. The company does have audited annual financial statements and as of 1/1/11 reports under IFRS.