# Heineken N.V.

European beer brewer and distributor. Third largest beer brewer globally.

**Company Rating based on TresVista Rating Criteria: BBB+**

**Industry – Breweries**

| | |
|---|---|
| Ticker | HEIA NA |
| Market Cap | €40,435.4 |
| EV | €52,047.4 |
| Revenues (FY2014) | €19,257.0 |

**Debt Highlights:**

| HEIA Bonds | Bloomberg Identifier | Maturity | S&P Rating | Amount Issued (Millions) | Price | Yield |
|---|---|---|---|---|---|---|
| HEIA 1.4% Oct 2017 USD | EJ389440 | 10/1/2017 | BBB+ | $1,250.0 | 99.93 | 1.4% |
| HEIA 2.5% Mar 2019 EUR | EJ070365 | 3/19/2019 | BBB+ | €850.0 | 106.61 | 0.6% |
| HEIA 2.125% Aug 2020 EUR | EJ300550 | 8/4/2020 | BBB+ | €1,000.0 | 105.84 | 0.9% |
| HEIA 2.725% Apr 2023 USD | EJ389450 | 4/1/2023 | BBB+ | $1,000.0 | 97.53 | 3.1% |

**Validation**:

Heineken N.V. is rated BBB+ based on the TresVista Rating Criteria (TRC) and is expected to maintain the rating going forward.

Free operating cash flow amounted to €486 million, in the first half of 2015, this was lower than last year partly due to a higher level of capital expenditure. Capital expenditure related to property, plant and equipment amounted to €602 million in the first half of 2015 representing 6.1% of revenues. The Company continues to focus on capital investment in higher growth markets and plans to increase capital expenditure on property, plant and equipment to approximately €1.7 billion in 2015, reflecting investment in additional capacity and the renewal and expansion of its returnable bottle fleet in higher growth markets. As a result, the Company expects a cash conversion ratio below 100% in 2015.

In 2015 Heineken expects a continued challenging external environment, however, delivering on strategic priorities is expected to drive further organic revenue and profit growth. Continued volume growth in developing markets will offset more subdued volume growth elsewhere.

The global beer industry has undergone a steady trend of consolidation. Ten years back, the beer industry was highly fragmented. In 2013, Heineken was expected to have a market share of 9.2% as compared to its market share of 5.7% in 2003. The global beer market is expected to grow at 2.97% in terms of revenue and 1.24% in terms of volume, as per Technavio report.

The bonds of the Company are trading in line with its European peers.

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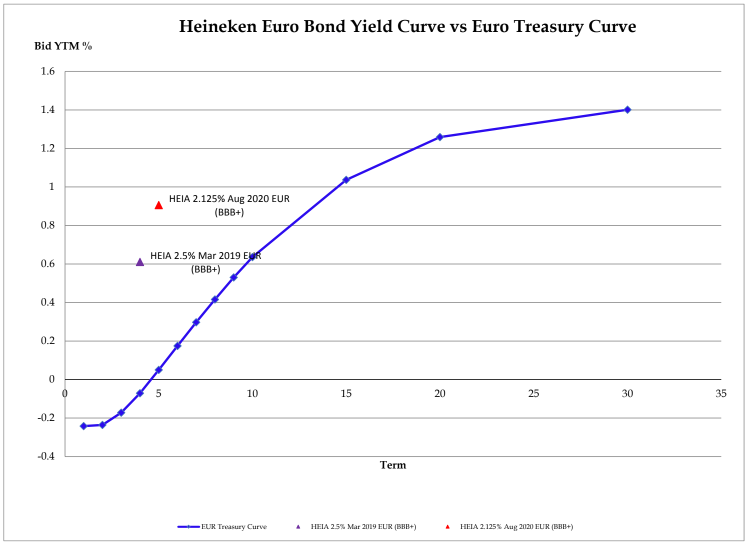
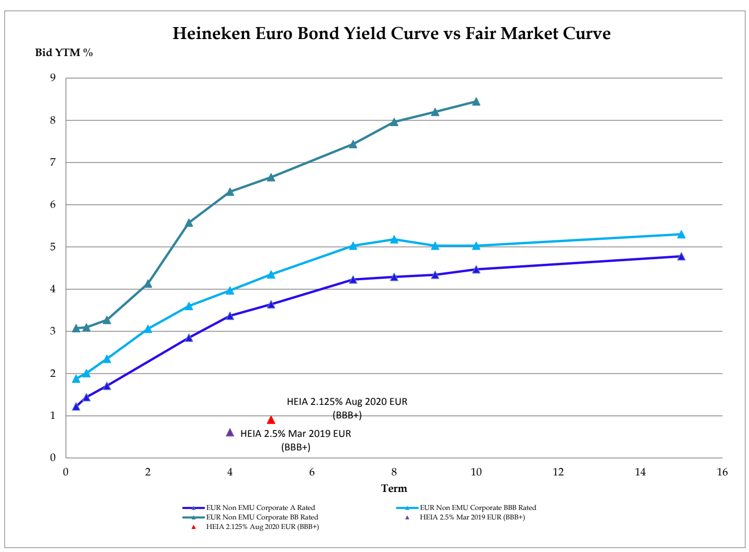
## Fixed Income Overview: Heineken N.V. Yield Curve for EUR Bonds




Source: Bloomberg.

The Heineken bonds are trading at a significant discount to the Euro Treasury:

- The Mar 2019 bond is trading at a spread of 68 bps
- The Aug 2020 bond is trading at a spread of 86 bps

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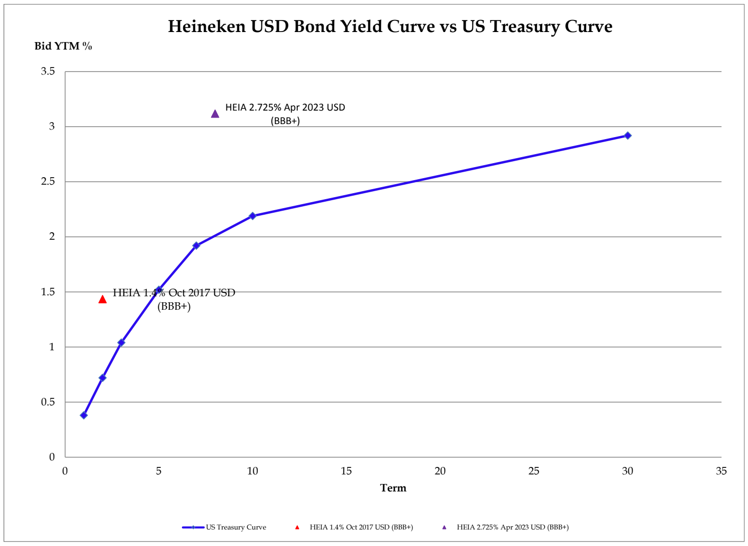
Source: Bloomberg. Respective EUR Miscellaneous used as applicable Fair Market Curves.

The Heineken bonds are trading at a significant premium over European Corporate A, BBB and BB rated bonds.

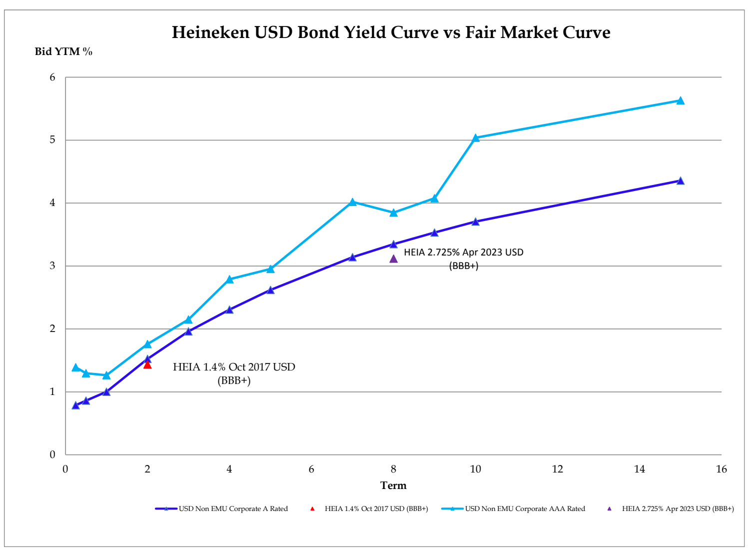
## Heineken N.V. Yield Curve for USD Bond




Source: Bloomberg.

The Heineken bonds are trading at a significant discount to the US Treasury:

- The Oct 2017 bond is trading at a spread of 72 bps
- The Apr 2023 bond is trading at a spread of 120 bps

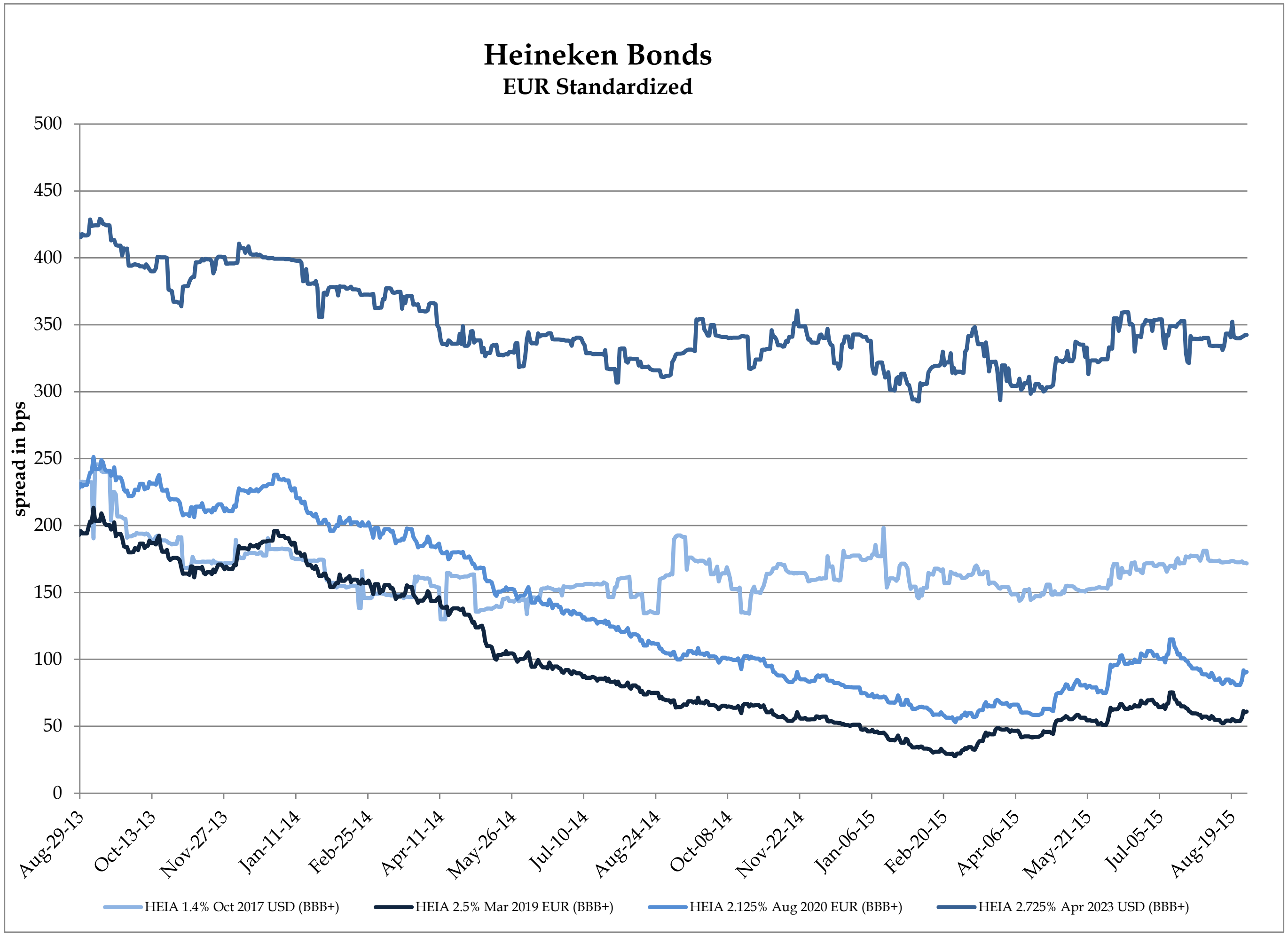



Source: Bloomberg. Respective USD Miscellaneous used as applicable Fair Market Curves.

The Oct 2017 Heineken bond is trading at par with Corporate A bond, whereas it is trading at a premium to Corporate AAA bonds.

## Heineken N.V. Bond Analysis

**All Trading Bonds of Heineken N.V.**




Source: Bloomberg.

Although, the Heineken 2023 bond has a longer maturity term, it is trading at a discount to other bonds.





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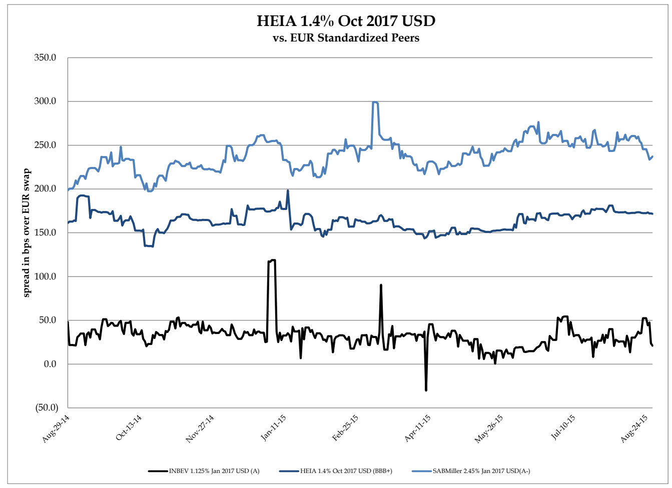
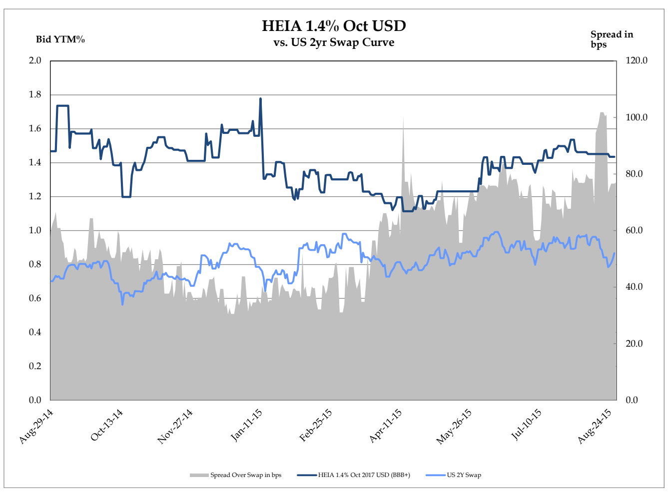
## Heineken N.V. (HEIA) Bond Issues

### 1. HEIA 1.4% Oct 2017 USD (BBB+)

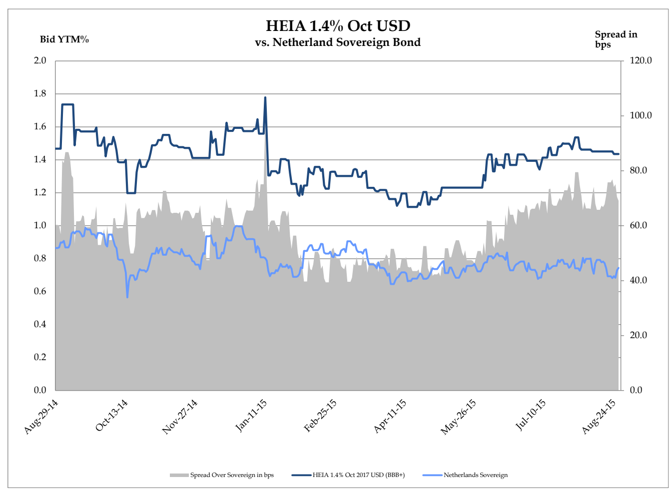
| Summary Information | |
|---|---|
| Bloomberg Code | EJ3894403 |
| Issuer | Heineken N.V. |
| Collateral Type | Senior Unsecured |
| First Coupon Date | April 1, 2013 |
| Amount Issued (USD mn) | 1,250 |
| Spread in bps over: | |
| US 2 year Swap Curve | 56.8 |
| Adjusted Netherland Sovereign Bond | 69.1 |
| Peer Comparison | In Line |
| TRC | Neutral |




The Heineken bond – Oct 2017 is trading at a premium over SABMiller and discount over INBev bonds.




Source: Bloomberg.



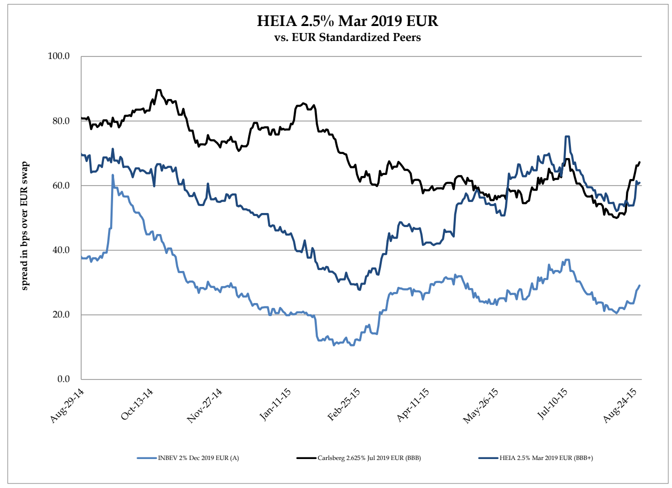

The bond is trading at a spread of 57 bps to the US 2 year Swap curve.

The bond is trading at a spread of 69 bps to the Netherland Sovereign bond.

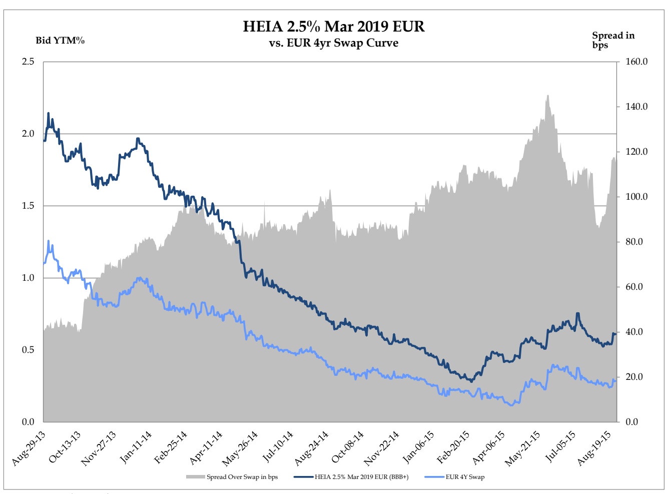
## Heineken N.V. (HEIA) Bond Issues

### 2. HEIA 2.5% March 2019 EUR (BBB+)

| Summary Information | |
|---|---|
| Bloomberg Code | EJ0703656 |
| Issuer | Heineken N.V. |
| Collateral Type | Senior Unsecured |
| First Coupon Date | March 19, 2013 |
| Amount Issued (Euro mn) | 850 |
| Spread in bps over: | |
| Euro 4 year Swap Curve | 32.6 |
| Adjusted Netherland Sovereign Bond | 64.7 |
| Peer Comparison | In Line |
| TRC | Neutral |

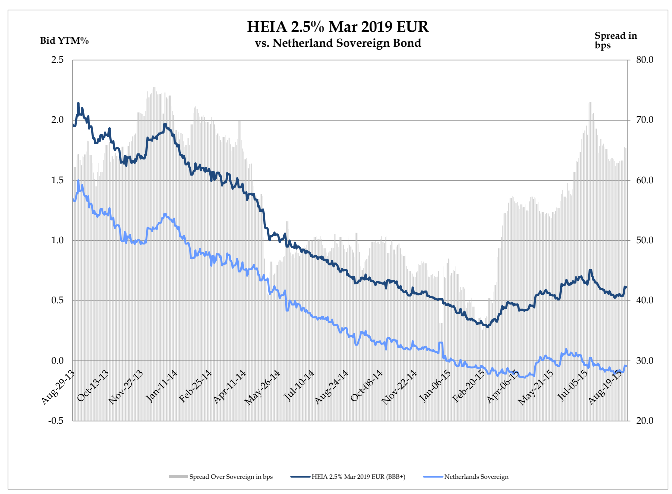



The Heineken bond – Mar 2019 is trading at a premium over Carlsberg and discount over INBev bonds.




Source: Bloomberg.

The bond is trading at a spread of 33 bps to the Euro 4-year Swap curve.




The bond is trading at a spread of 65 bps to the Netherland Sovereign bond.





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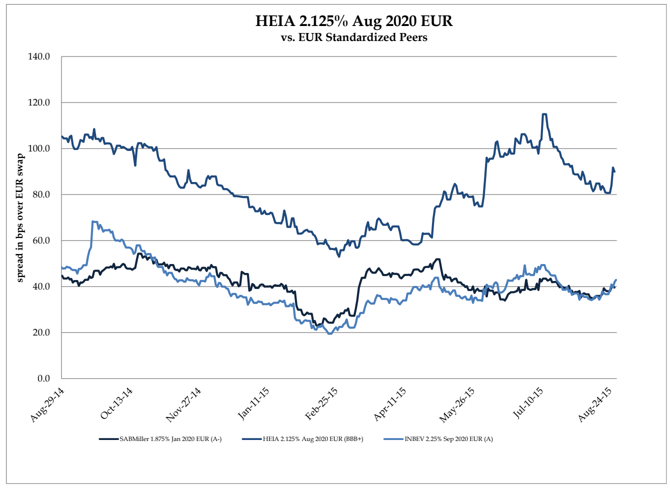
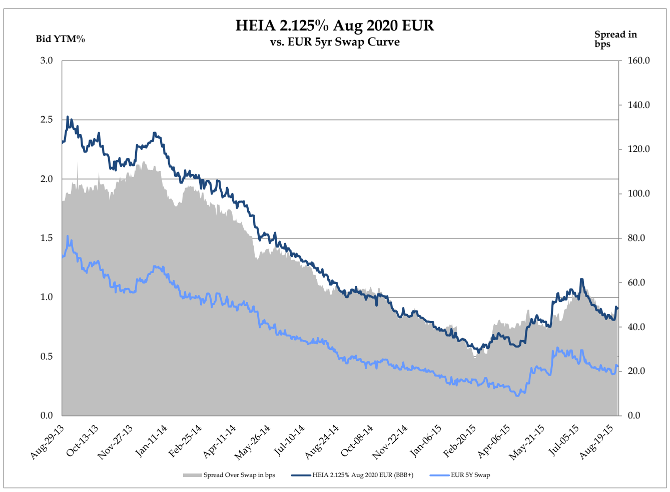
## Heineken N.V. (HEIA) Bond Issues

### 3. HEIA 2.125% August 2020 EUR (BBB+)

| Summary Information | |
|---|---|
| Bloomberg Code | EJ3005505 |
| Issuer | Heineken N.V. |
| Collateral Type | Senior Unsecured |
| First Coupon Date | August 4, 2013 |
| Amount Issued (Euro mn) | 1,000 |
| Spread in bps over: | |
| Euro 5 year Swap Curve | 48.1 |
| Adjusted Netherland Sovereign Bond | 76.7 |
| Peer Comparison | In Line |
| TRC | Neutral |

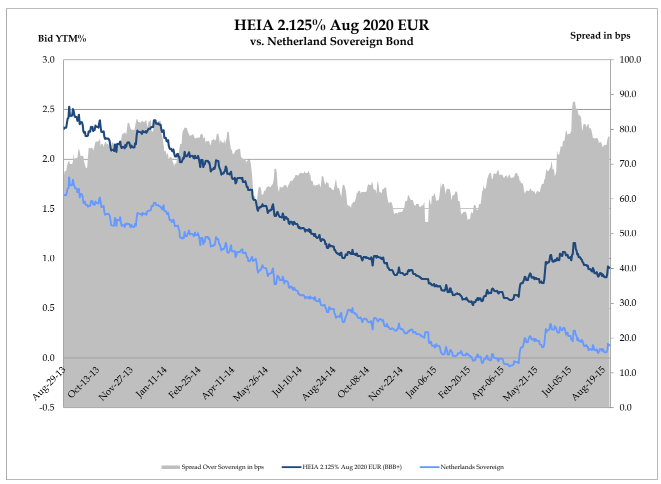



The Heineken bond – Aug 2020 is trading at a discount over its peers.




Source: Bloomberg.

The bond is trading at a spread of 48 bps to the Euro 5-year Swap curve.

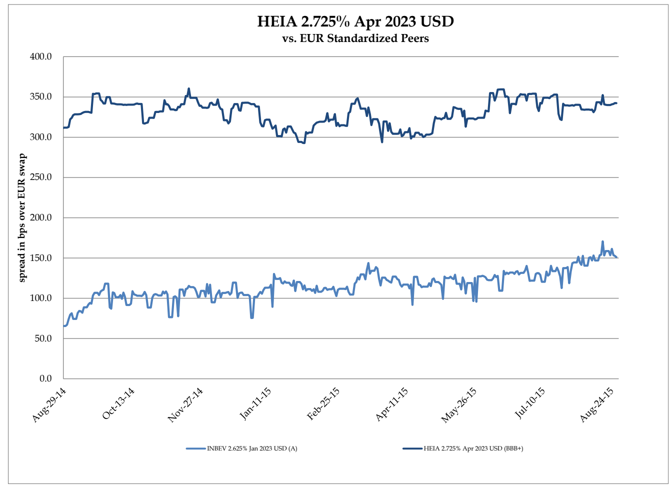



The bond is trading at a spread of 77 bps to the Netherland Sovereign bond.

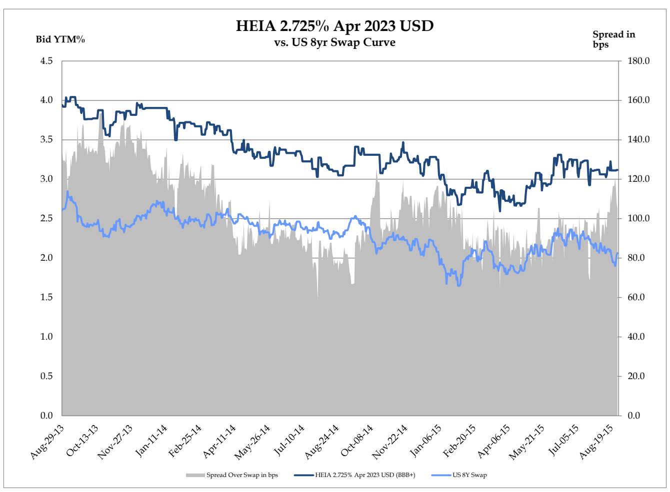
## Heineken N.V. (HEIA) Bond Issues

### 4. HEIA 2.7250% April 2023 USD (BBB+)

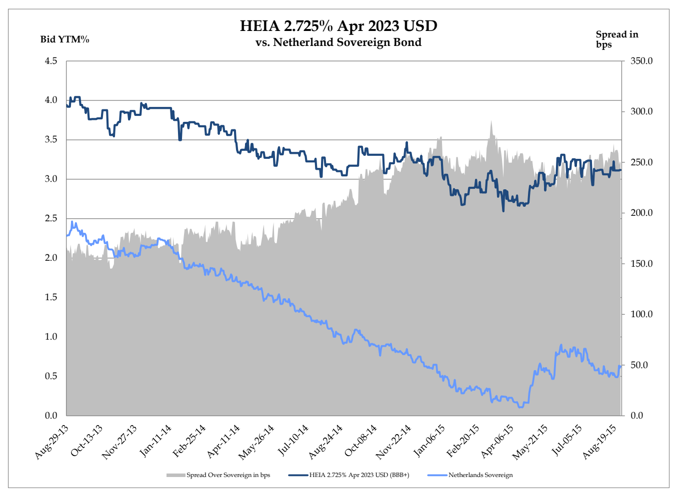
| Summary Information | |
|---|---|
| Bloomberg Code | EJ3894502 |
| Issuer | Heineken N.V. |
| Collateral Type | Senior Unsecured |
| First Coupon Date | April 1, 2013 |
| Amount Issued (USD mn) | 1,000 |
| Spread in bps over: | |
| US 8 year Swap Curve | 106.0 |
| Adjusted Netherland Sovereign Bond | 248.8 |
| Peer Comparison | In Line |
| TRC | Neutral |




The Heineken bond – Nov 2013 is trading at a significant discount over its peer.




Source: Bloomberg.




The bond is trading at a spread of 106 bps to the US 8-year Swap curve.

The bond is trading at a spread of 249 bps to the Netherland Sovereign bond.

## Financial and Operational Analysis

| Ratings | 2010 | 2011 | 2012 | 2013 | 2014 | 2015E | 2016E |
|---|---|---|---|---|---|---|---|
| Interest Expense Coverage | 5.4x | 6.7x | 6.4x | 6.8x | 9.0x | 11.2x | 14.0x |
| Leverage | 1.6x | 1.7x | 2.0x | 1.8x | 1.7x | 1.4x | 1.3x |
| Financial Leverage | 2.6x | 2.8x | 3.1x | 2.9x | 2.8x | 2.5x | 2.4x |
| Cash Flow to Total Debt | - | - | - | - | - | 17.9% | 20.5% |
| Current Ratio | 0.8x | 0.8x | 0.9x | 0.9x | 0.8x | 0.8x | 0.9x |
| ROE (%) | 14.1% | 14.6% | 24.8% | 12.0% | 12.2% | 12.9% | 12.5% |
| ROA (%) | 5.4% | 5.3% | 8.1% | 4.1% | 4.4% | 5.1% | 5.2% |
| EV/EBITDA | 9.3x | 9.0x | 12.1x | 10.5x | 11.0x | 9.7x | 9.5x |
| Operating Margin | 12.7% | 12.6% | 11.9% | 12.1% | 14.0% | 14.5% | 14.5% |
| CFO/Interest Expense | - | - | - | - | - | 8.2x | 10.5x |
| **TRC Ratings** | **BBB+** | **BBB+** | **BBB+** | **BBB+** | **BBB+** | **BBB+** | **BBB+** |

Source: Company filings, TresVista ratings.

**Profitability**

The Company's profitability has stabilized from past two years with Net Profit Margin of about 7.9%. In 2014, the Company experienced stable ROE and ROA of 12.2% and 4.4% respectively, in comparison with the previous fiscal. Operating margin of 14.0% was better than the previous year. EBIT grew 15.4% due to higher revenues and operating efficiency in 2014. These tailwinds were impacted by increased input costs and higher planned investments in marketing and global business services.

**Liquidity**

The Company has marginally reduced the amount of leverage, from 2.0x at the end of 2012 to 1.7x at the end of 2014. Interest coverage ratio has improved significantly from 6.4x in 2012 to 9.0x in 2014 bringing lenders in a comfortable zone. The net debt/EBITDA ratio of 2.5x was lower than last year and closer to the Company's long-term target of below 2.5x. The Company has also guided a reduction in the number of employees for 2015. In 2014, the Company generated strong free operating cash flows of €1,574.0 million, representing an increase of €56.0 million compared to 2013. This increase was driven by higher cash flow from operations and lower interest paid, only partly offset by higher capital expenditure and income taxes. The cash conversion ratio for 2014 was 78.9% and cash conversion ratio of below 100% is expected in 2015

**Company Rating**

Heineken N.V. is rated BBB+ based on our proprietary model and is expected to maintain its rating going forward.

**Geographical Mix Comments (As of First Half, 2015):**

- **Western Europe:** The "Not an Inch Back" strategy continues, with cost savings reinvested back into the business to drive growth. This was the region that, in the first half, faced the toughest comparatives, as it was the main beneficiary of the weather and football World Cup last year. Volumes in the first half were down 3%, with positive growth in Spain, France, and The Netherlands, more than offset by the high single-digit decline in the UK. Revenue per hectoliter was up 0.5% organically, despite deflationary pressure and pricing pressure in the off-trade in a number of key markets, and most notably, in the UK and France
  - UK: Volume in the UK declined in the high-single digit due to challenging market conditions, and promotional pressures. Prior year comparatives were particularly demanding given favourable weather and the football World Cup. During the period the successful launches of new flavour variants under the Strongbow and Bulmers brands performed well. Within the beer portfolio Heineken and Amstel saw solid volume growth
  - Netherlands: In the Netherlands volumes were up in the low single digit ahead of the overall market. This reflected continued strengthened commercial execution, combined with slightly better market conditions
  - France: Volume grew in the – in France, the volume grew in the low single-digits, with positive Heineken, Desperados, and Affligem growth
    - Spain: Continues to show signs of an improving economic environment, with positive volumes underpinned by growth in the on-trade

- **Central & Eastern Europe:** Despite Group beer volumes down 2% for first half of the year, our strategy of focusing on driving value and premiumization delivered results. Revenue per hectoliter improved 2.7%, and the region saw double-digit profit growth. Organically, the region's consolidated operating profit, beia, was up an impressive 15%
  - Russia: Despite volume down double-digit in Russia, operating performance improved as a result of the premiumization of the portfolio through Heineken, Krusovice, and Amstel Premium Pilsner
  - Poland: Whilst the underlying market remains difficult, volumes were up in the high-single digits, with some share gain
  - Austria: Volume in Austria was down in the low single digit because of favorable weather conditions and higher promotional intensity in the off trade in the second quarter last year
  - Romania: Growth in volume in the high single-digits, led by the strong brand performance of Bucegi, which for the first time exceeded 2 million hectoliters
  - Greece: Volumes remains under pressure in Greece and was down mid-single digit in the first half of the year

- **Africa & Middle East:** Beer volume in Africa Middle East grew 2.8% organically. Volume in the second quarter improved primarily due to slightly better volumes in Nigeria. Ethiopia and South Africa contributed positively to volume growth. Revenue per hectoliter declined 1.1%, primarily due to higher volume growth in the lower revenue per hectoliter countries.
  - Nigeria: Volume was down in the low single-digit for the half year, with some slight market share loss. The value segment continues to outpace the beer market and our volume growth was led mainly by theirr value brand portfolio, which puts adverse pressure on mix. Fuel scarcity also had an impact on the volumes in the period. Margins were impacted by adverse product mix, the naira devaluation and increased inflation. The merger of their majority-owned subsidiaries, Nigerian Breweries and Consolidated Breweries, which completed at the end of last year, continues to progress well
  - Ethopia: Volume more than doubled in Ethiopia, with the key brands Bedele and Walia driving growth. Opened its third brewery in Addis Ababa last July 2014, and intends to add additional production capacity to capture increased beer demand in the market
  - South Africa: Despite a challenging beer market, volume of the brandhouse joint venture in South Africa grew in the mid-single digit supported by healthy growth of the Heineken and Amstel brands

  - Egypt: Volume declined double digit in the first half of the year, with Q2 trading adversely impacted by last year's excise duties increase and the timing of Ramadan

- **Americas:** Group beer volume was up 3.6% organically, with positive growth in Mexico, Brazil and the U.S. Revenue per hectoliter improved by 2.8% with consolidated operating profit growth up a strong 8.6%
  - Mexico: Volume was up in the low-single digit with higher pricing, cost savings, and mix, all contributing to profit growth. Easter timing and increased competitive price competition led to more subdued volume in the second quarter
  - Brazil: despite the World Cup last year, the company performance was strong with double-digit growth in Heineken volume and market share gain
  - US: Sales and depletions were both slightly up, continuing to outperform the overall U.S. beer market
- **Asia Pacific**: Company witnessed good volume growth for the first half and up 6.1%. Vietnam was the key driver of this growth and was complemented by strong performance in Cambodia, China, Korea and Taiwan. Revenue per hectoliter was down 1.1%, adjusting from negative or adjusting for negative counter mix. This would have been up 3.4%
  - Vietnam: Star performer with continued double-digit volume growth in the second quarter. These followed strong first quarter boosted by a successful Vietnamese New Year period
  - Indonesia: Remained weak, with similar trends to the first quarter, mainly due to the implementation in April of the new alcohol regulation relating to the sale of alcohol in minimarts
  - China: saw volume growth in the mid-single digits, with double-digit Heineken growth
  - Taiwan: Volumes grew in the double-digits
  - Cambodia: Was strong, with volumes up double digit, boosted by successful implementation of the portfolio strategy
  - India: Volume in India in the second quarter was slightly down across all major states, with stable market share

**Key Risks:**

- **Rising Competitive Threats:** Rising presence of SABMiller is becoming a potential threat in Nigeria, second largest profit center for Heineken. Mexico, Heineken's no. 1 profit center, will also face pressure for CCM's volume market share from its main competitor Modelo
- **Poor Performance in Nigeria:** Volume was down in the low single-digit for the half year, with some slight market share loss. The value segment continues to outpace the beer market and Heineken's volume growth was led mainly by its value brand portfolio, which puts adverse pressure on mix. Fuel scarcity also had an impact on the volumes in the period. Margins were impacted by adverse product mix, the Naira devaluation and increased inflation. The merger of its majority-owned subsidiaries, Nigerian Breweries and Consolidated Breweries, which completed at the end of last year, continues to progress well
- The Central & Eastern Europe remains structurally challenged, with unfavorable demographics, high competition and low to no inflation, resulting in weak pricing and low scope for further underlying margin progression.

**Key Positives for Heineken:**

- **Positive Organic Growth:** The firm has witnessed a continuous organic growth. Heineken expects positive organic revenue growth in 2015 with volume growth at a more moderate level than 2014
- **Continued Cost Savings:** Heineken is committed to delivering further cost savings and will continue its focus on driving cost efficiencies across the company. These are an important driver of the medium term margin guidance
- **Global Business Services:** Further efficiencies to come from Global Business Services. The Global Business Services ("GBS") organization was established in October 2010 and was a key enabler of the TCM2 cost savings program
- **Lower Input Costs:** Input costs in 2015 are still expected to be slightly lower, excluding the transactional effect of currency movements
- In recent years Heineken has benefitted from mix improvement, revenue management and inflation-led price

increases in many of its emerging markets during a period of declining input cost inflation. This has resulted in 80bps to 90bps margin expansion in the past two years. There is still significant potential to reap fixed and variable cost savings through rollout of GBS and cost control in an environment where price/mix continues to increase

- Heineken is combining Western and Central & Eastern divisions into one region, which is expected to generate savings in central functions
- Innovation rate of 8.6%, ahead of the 6% long-term target

  **Note:** The innovation rate is calculated as revenues generated from innovations (introduced in the past 40 quarters for a new category, 20 quarters for a new brand and 12 quarters for all other innovations, excluding packaging renovations) divided by total revenue

**Recent Updates:**

- **Heineken buys more shares of United Breweries:** In July 2015, Heineken NV increased its stake in India's biggest beer maker to 42.1 percent, spending INR 8.72 billion (~$138 million) for additional shares in United Breweries Ltd. The acquisition of a 3.2% holding from a unit of Diageo Plc reflects the Dutch brewer's confidence in the long-term potential of India's beer market. Heineken is strengthening its ties with a business that has distributed its namesake beer in India since 2011
- **Heineken acquires a majority stake in leading Slovenian brewer Pivovarna Laško d.d.:** In April 2015, Heineken N.V. to acquire 4,471,054 shares in Pivovarna Laško d.d. ("Pivovarna Laško"), representing 51.1% of the issued share capital, for a price per share of €25.56, or a total consideration of €114.3 million. Pivovarna Laško is Slovenia's leading brewer. Slovenia is centrally positioned between other markets where HEINEKEN has operations. The company operates two modern and well-invested breweries and owns and brews the renowned Laško and Union beers, with strong heritage across the Adria region. The acquisition will strengthen their position within the region and will bring two complementary strong local brands into their existing portfolio
- **Heineken N.V. has rejected an acquisition offer from SABMiller**, a multinational brewing and beverage company, headquartered in London. The Dutch brewer announced the decision to spurn the takeover proposal from SABMiller, saying that the company wants to remain independent and that it does not intend to make any further public statements about the bid. SABMiller reportedly approached Heineken in September 2014. The deal would have made the Heineken family one of the largest shareholders in the combined company, while SABMiller would have added more than $25 billion in sales

## Company Outlook

In 2015 Heineken expects a continued challenging external environment, however, delivering on strategic priorities is expected to drive further organic revenue and profit growth. Continued volume growth in developing markets will offset more subdued volume growth elsewhere. Revenue per hectoliter is expected to increase driven by revenue management. Pricing will be limited by deflationary and off premise pressure in some markets

Heineken will continue its targeted higher commercial investments across the regions, and expects a slight increase in marketing and selling spend. In 2015, capital expenditure related to property, plant and equipment is expected to be approximately €1.7 billion. TCM will continue to deliver further cost savings driving margins, and strong cash flow. Heineken is targeting a Net debt/EBITDA ratio of below 2.5x and a cash conversion ratio of below 100% in 2015.

## Disclosure Appendix

Analysis prepared by TresVista Financial Services, Pvt. Ltd. as of August 28, 2015.

**TresVista Rating Criteria (TRC):**
TRC classifies bonds on Company's credit profile, financial stability, management capabilities, and experience to react to systematic and unsystematic risk.

**Bond Call Criteria:**
The bond call recommendations are based on current market yields versus the required return, which is estimated based on the Company rating, the benchmark fair market curves, the respective treasuries, and the issuer's sovereign bond valuations.

**Other Important Disclosures:**
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TresVista Financial Services Pvt. Ltd. is a Mumbai-based firm that provides research, analytics, M&A advisory, and other customized services. TresVista partners with financial institutions globally to enable them to rise above the competition in today's crowded marketplace. Through our team of highly trained associates, our clients are able to increase and manage their operational capacity in a cost-effective manner. TresVista role is to be decided upon by the clients' needs and the tasks at hand, be it exploring an arbitrage opportunity, analyzing prospective investments, or conducting due-diligence on a cross-border acquisition. TresVista flexibility is instrumental to its goal of helping clients reach higher heights. Our clientele include investment banks, private equity firms, hedge funds, debt lenders, and other financial services institutions.