

RATING ACTION COMMENTARY**Fitch Affirms Coca-Cola Icecek AS at 'BBB'; Outlook Stable**

Fri 14 Jun, 2024 - 1:58 PM ET

Fitch Ratings - Milan - 14 Jun 2024: Fitch Ratings has affirmed Coca-Cola Icecek AS's (CCI) Long-Term Issuer Default Rating (IDR) at 'BBB'. The Outlook is Stable. A full list of rating actions is below.

The affirmation of CCI reflects continued strong operating profitability with successful execution of its expansion plan, leading to revenues and EBITDA growth. This is supported by CCI's leading positions in its core markets, the resilient nature of the soft drinks business and CCI's strong capital structure. CCI's ratings continue to benefit from a single-notch uplift for strategic support from its parent, The Coca-Cola Company (TCCC) in line with Fitch's Parent and Subsidiary Linkage (PSL) Criteria.

The rating remains constrained by a weak operating environment in a number of CCI's markets of operations. Inherent foreign-exchange (FX) risks related to hard-currency-denominated debt and some operating costs are key rating constraints.

KEY RATING DRIVERS

Inflation Accounting Modest Impact: CCI implemented inflation accounting in accordance with IAS29 for its Turkish operations (40% of revenues), while its international operations remain unaffected. Inflation accounting adjusts profit and loss for year-end inflation, with minor impact on depreciation and amortisation and inventory values, and reports monetary gains of TRY15.7 billion after EBITDA. Profitability remains within Fitch's sensitivity range even after adjusting for IAS29 (17.5% IAS29-adjusted versus 20% non-IAS29 adjusted in 2023).

CCI's interest coverage weakened to 5.0x in 2023, below its negative sensitivity of 6.5x, due to both the application of IAS29 and rising interest rates. However, we project the

Strong Revenue Growth: We have used inflation-adjusted numbers in our forecasts. We expect CCI to maintain a positive revenue trend, supported by organic growth. We project revenues will rise around 54% in 2024 as a result of low single-digit volume growth and pricing mix. In Türkiye we expect a rebound in demand driven by increasing purchasing power, while for international markets we project growth to be underpinned by new greenfield openings

Flat Profitability: For 2024 we estimate flat Fitch-adjusted profitability of 17.5%, driven by softening commodities prices and hedging partially offset by higher marketing spend. We expect profitability to gradually rise to above 18% from 2025 driven by proactive procurement, a premiumisation strategy that results in a better product mix, as well as maintaining cost-reduction initiatives and internal efficiencies.

High but Manageable FX Risks: As of end-2023, about 75% of CCI's debt and 25% of its production costs were denominated in hard currencies, in contrast with revenue, which is mainly in emerging markets' local currencies. This results in high FX risks, which are managed by CCI by improving geographic diversification towards less volatile countries.

Strong Cash Flow Generation: We project free cash flow (FCF) margin to temporarily weaken to low single digits in 2024, due to an increase in capex toward 10% of sales for greenfield projects. We project it to normalise to mid-single digits from 2025 as capex moderates and profitability improves. CCI will adhere to its maximum dividend pay-out of 50% of net distributable income, which favours cash accumulation and deleveraging, with the aim of building up financial flexibility to maintain a low-risk balance sheet. This flexibility may also be deployed for potential M&A to grow the business in new geographies.

Conservative Capital Structure Intact: CCI's conservative financial policy targets EBITDA net leverage at below 2x albeit with tolerance for a temporary breach for value-enhancing M&As. Even with this conservative target, CCI consistently pursued its expansion plan in 2023 and 2024, successfully completing the acquisition of Anadolu Etap Icecek, Coca-Cola Pakistan's minority stake and Coca-Cola Bangladesh and leaving ample leverage headroom. We project leverage ratios will remain well below target over the next four years, supported by sufficient FCF generation, resilient EBITDA and cash reserves to cover upcoming debt maturities.

'Medium' operational and strategic incentives for supporting CCI. This is based on shared brands and marketing functions, as well as strategic, operational and innovation support provided by TCCC. We assess legal incentives as 'Weak'.

Overall, TCCC's moderate ownership of CCI at 20% constrains the uplift to a single notch. In our view, this level of ownership creates some uncertainty at the current rating about the extent of potential support to CCI, on top of the presence of a majority shareholder, Anadolu Efes Biracilik ve Malt Sanayii A.S. (AEFES, BB+/Rating Watch Negative), and CCI's public listing.

Insulated Ring-Fencing from AEFES: Under its Parent-Subsidiary Linkage methodology, Fitch views CCI's credit profile as insulated from that of its weaker parent, AEFES, which holds 50.3% of CCI's shares. This is because AEFES's ability to control CCI is constrained by important voting rights of the other shareholder, TCCC. Moreover, CCI's and AEFES's treasury functions and debt structures are fully ring-fenced from each other.

Weak Operating Environment: The operating environments in CCI's core markets (Turkiye, Pakistan, Uzbekistan and Kazakhstan), which we assess at 'bb' and below continue to moderately affect its ratings. These countries are characterised by high volatility in geopolitical events and macro-economic conditions, which tend to result in high inflation and FX fluctuations. We see these dynamics as a threat to consumer sentiment across the region, even though CCI has a strong record of operating under these challenging conditions.

Kazakhstan Country Ceiling: We apply Kazakhstan's 'BBB+' Country Ceiling to CCI's rating instead of that of Turkiye where CCI is incorporated. Given CCI's conservative capital structure with projected hard-currency interest expenses of around TRY1400 million in 2024, we calculate that cash flows from Kazakhstan (2023: 24% of EBITDA) should continue to cover CCI's hard-currency interest charges with sufficient headroom. We expect this headroom to be maintained over the next four years.

Low T&C Risk: Fitch assesses transfer and convertibility risks for Kazakhstan as low and we do not foresee any difficulties for CCI to channel cash flows, either through dividends or intercompany loans, from Kazakhstan to Turkiye.

DERIVATION SUMMARY

Term IDR among Fitch-rated corporates in Turkiye. Compared with its main peers, Coca-Cola Europacific Partners plc (CCEP; BBB+/Stable), and Coca-Cola FEMSA, S.A.B. de C.V. (A/Negative), CCI is smaller and operates in more volatile emerging markets and has greater exposure to FX risks. This is balanced by improved profitability, now in line with or exceeding its main peers', and by CCI's conservative capital structure with leverage metrics that are commensurate with the 'A' rating category, in line with Fitch's Sector Navigator for Non-Alcoholic Beverages.

CCI's ratings benefit from a one-notch uplift for potential support from TCCC. This is in line with Fitch's approach to CCEP, whose ratings also benefit from our assessment of TCCC's 'Medium' operational and strategic incentives for supporting CCEP.

At the same time, CCI's SCP reflects moderate pressure from a weak operating environment in the markets in which it operates, effectively capping its rating at the current level.

KEY ASSUMPTIONS

Fitch's Key Assumptions within our Rating Case for the Issuer:

- Turkish lira/US dollar on average at 33.3 in 2024, weakening to 39.6 in 2024
- Turkish sales volumes to grow mid-single digits in 2024, driven by lower base last year and purchasing power recovery. Given higher inflationary pressure, we assume about a 50% increase of the average selling price in 2024, reducing to about 20% in 2025-2027
- International sales volumes to grow by low single digits between 2024 and 2027
- Consolidated EBITDA margin flat at 17.5% in 2024 (, gradually recovering to about 18% and above in 2025-2027
- Capex at about 9.8% of net sales in 2024 and about 6.5% in 2025-2027
- Dividends of TRY2 billion in 2024 and TRY3 billion in 2025

RATING SENSITIVITIES

Factors That Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

SCP, based on the following factors:

- EBITDA margin sustained above 20%
- Enhanced scale and geographic diversification, either organically or through M&A, without impairing the operating-environment score (currently bb-)
- Conservative financial structure with EBITDA net leverage remaining below 1.7x on a sustained basis

Factors That Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

- Adverse impact of weaker operating and macro environments in CCI's core markets on credit metrics not accompanied by adequate cash-preservation measures, such as dividend and capex reduction
- Increased volatility translating into mid-single digit FCF (after capex and dividends)
- EBITDA net leverage above 2.5x
- EBITDA interest coverage below 6.5x (2023: 5.0x)
- EBITDA margin towards 16%
- Weakening linkages with TCCC
- A downgrade of Kazakhstan's Country Ceiling or EBITDA generated in the country being insufficient to cover hard-currency interest expenses in the medium term would result in a downgrade of the Long-Term Foreign-Currency IDR

LIQUIDITY AND DEBT STRUCTURE

Strong Liquidity: At end-March 2024, liquidity was supported by a cash balance of USD597million-equivalent, with about 62% in hard currencies, of which about 93% was outside Turkiye.

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facilities in Turkiye, Pakistan, Kazakhstan, Turkmenistan and Azerbaijan, which can be utilised in hard currencies or local currencies according to market conditions. However, Fitch does not include availability under uncommitted credit lines in its liquidity calculation.

ISSUER PROFILE

CCI is among the top-10 largest bottlers in the Coca-Cola system by sales volumes, with the majority of sales generated in Turkiye, Kazakhstan, Pakistan and Uzbekistan.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

MACROECONOMIC ASSUMPTIONS AND SECTOR FORECASTS

Click here to access Fitch's latest quarterly Global Corporates Macro and Sector Forecasts data file which aggregates key data points used in our credit analysis. Fitch's macroeconomic forecasts, commodity price assumptions, default rate forecasts, sector key performance indicators and sector-level forecasts are among the data items included.

ESG CONSIDERATIONS

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit <https://www.fitchratings.com/topics/esg/products#esg-relevance-scores>.

RATING ACTIONS

ENTITY / DEBT ⚡

RATING ⚡

PRIOR ⚡

Coca-Cola Icecek AS		LT IDR	BBB Rating Outlook Stable		BBB Rating Outlook Stable
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		Affirmed			
		LC LT IDR	BBB Rating Outlook Stable		BBB Rating Outlook Stable
		Affirmed			
		Natl LT	AAA(tur) Rating Outlook Stable		AAA(tur) Rating Outlook Stable
		Affirmed			
senior unsecured		LT	BBB	Affirmed	BBB

VIEW ADDITIONAL RATING DETAILS

FITCH RATINGS ANALYSTS

Lisa Berardi

Associate Director
Primary Rating Analyst
+39 02 9475 6699
lisa.berardi@fitchratings.com
Fitch Ratings Ireland Limited Sede Secondaria Italiana
Via Morigi, 6 Ingresso Via Privata Maria Teresa, 8 Milan 20123

Jana Litovcenko

Senior Analyst
Secondary Rating Analyst
+44 20 3530 1182
jana.litovcenko@fitchratings.com

Elena Stock

Senior Director
Committee Chairperson
+49 69 768076 135
elena.stock@fitchratings.com

London

+44 20 3530 1128

tahmina.pinnington-mannan@thefitchgroup.com

Additional information is available on www.fitchratings.com

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APPLICABLE CRITERIA

[National Scale Rating Criteria \(pub. 22 Dec 2020\)](#)

[Parent and Subsidiary Linkage Rating Criteria \(pub. 16 Jun 2023\)](#)

[Corporates Recovery Ratings and Instrument Ratings Criteria \(pub. 13 Oct 2023\) \(including rating assumption sensitivity\)](#)

[Corporate Rating Criteria \(pub. 03 Nov 2023\) \(including rating assumption sensitivity\)](#)

[Sector Navigators – Addendum to the Corporate Rating Criteria \(pub. 03 Nov 2023\)](#)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 ([1](#))

ADDITIONAL DISCLOSURES

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