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Watershed Bond Issuance for Grupo Elektra Subsidiary[1]

By Douglas A. Doetsch, Juan P. Moreno, Gabriela Sakamoto, and Daniel P. Whitmore

Douglas A. Doetsch
ddoetsch@mayerbrown.com
+1 312 701 7973

Juan Pablo Moreno
jmoreno@mayerbrown.com
+1 312 701 8141

Gabriela Sakamoto
gsakamoto@mayerbrown.com
+1 202 263 3029

Daniel P. Whitmore
dwhitmore@mayerbrown.com
+1 312 701 7134

Nueva Elektra del Milenio's Rule 144A/Regulation S capital markets offering in January 2021 featured a future flow offshore structure, excellent coverage levels, and a parent guarantee that resulted in an historic and landmark transaction for Nueva Elektra del Milenio, Mexico and Latin America. This article provides background and further detail.

Nueva Elektra del Milenio's ("NEM") debut bond offering in January 2021 was a milestone financing for the capital markets in Mexico and the Latin American region. The US$500 million 4.875% fixed rate notes were issued by a special purpose vehicle in the form of a fiduciary estate organized in Luxembourg (the "SPV") and secured by remittance flows originated in the US, processed through designated money transfer operators (each, an "MTO") and delivered by NEM to beneficiaries in Mexico.

The notes were offered and sold in the US in accordance with Rule 144A under the United States Securities Act of 1933 and outside the US in accordance with Regulation S under the Act. BCP Securities, LLC, Credit Suisse Securities (USA) LLC, and Jefferies LLC acted as initial purchasers. The notes were listed on the Securities Official List of the Luxembourg Stock Exchange. They have a tenor of seven years with an initial two-year interest-only period.

NEM is the retail subsidiary of Grupo Elektra, a major Mexican retail and financial services conglomerate with operations in Mexico, Guatemala, Honduras, Panama and Peru. NEM's money transfer business has a well-established track record and accounts for more than 40% of the international remittance flows into Mexico for the 12 months ending December 31, 2019.

The transaction was structured to transfer the receivables to the offshore SPV, thus achieving the bankruptcy-remote structure favored by rating agencies that resulted in a credit rating uplift. Fitch assigned the notes a rating of "BBB-," one notch above NEM's "BB+" credit rating, while HR Ratings of Mexico gave the notes a rating of "BBB+." The notes represented NEM's first investment-grade issuance.

At closing, NEM contributed and assigned all of its rights to all existing and future-generated receivables, and the related collections, to the Luxembourg SPV. Receivables are generated when NEM pays the beneficiary of a remittance transaction before NEM is reimbursed by a designated MTO the next business day. The SPV used the proceeds of the notes to make a payment to NEM for NEM's contribution of the receivables and to fund a reserve account. Local Mexican counsel confirmed that NEM's contribution and assignment of the receivables constituted a "true sale" of such receivables under Mexican law. Accordingly, upon a bankruptcy of NEM, the receivables would not constitute assets of NEM's estate but rather would belong to the SPV.

NEM instructed the designated MTOs to make Peso payments in respect of the receivables to a pass-through account at a local account bank in Mexico City, which were then swept to a London-based collection account of the collateral agent. Amounts deposited into the collection account are allocated on each business day according to a waterfall to pay for upcoming debt service and program expenses with any excess being paid to NEM as a deferred payment for the contribution of the receivables.

Credit Highlights.

NEM's Track Record. NEM has a long track record in the remittance business with over 25 years of processing remittance flows with a compound annual growth rate of flows between 2010 and 2019 of 16.8%. The company's growth has been fueled by an expansion of stores, where most of the cash payments to remittance beneficiaries are made. NEM offers remittance services to beneficiaries at approximately 1,800 point-of-contact locations in Mexico.

COVID-19 Impact. Given the impact of the COVID-19 pandemic and the concomitant economic upheaval, the World Bank has estimated that remittances from migrant workers will decline by 14% in 2021 as compared to 2019. However, for Latin America, it is only expected to decline by 0.2% and for Mexico, the trend is positive. For the first 11 months of 2020, remittances from the US to Mexico rose 11% over the prior year. NEM benefited from this trend as well: for the last 12 months ending with the third fiscal quarter of 2020, remittance volumes increased by 5.2% for the company.

Coverage Levels. Like other future flow financings, collections from existing and future reimbursement remittance transactions must be greater than debt service under the notes to mitigate the risks associated with a decline in collections, loss of a designated MTO, declines related to migration patterns or a regional or global economic downturn.

When comparing the maximum debt service amounts under the notes with the cash flows generated between December 2015 and November 2020 from designated MTOs, the actual coverage ratios exceed by a significant amount the minimum coverage ratios set forth in the legal documents. This overcollateralization enables the company to withstand a serious decline in cash flows and still cover the maximum principal and interest payments, thus reducing the risk to investors in the notes.

Parent Guarantee. Unique among future flow financings, Grupo Elektra provided an unconditional and irrevocable parent guarantee on a senior basis in favor of the collateral agent on behalf of the investors. The guaranteed obligations are the obligations of NEM, as originator, to pay when due any default payment or taxes under the legal documents. Upon the occurrence of any default, the SPV will be entitled to immediate payment of the default payment (for further payment to the investors) by Grupo Elektra, as guarantor.

For Fitch, because of the unconditional and irrevocable nature of the parent guarantee, the transaction rating will always be the higher of Grupo Elektra's rating and NEM's rating plus the one-notch uplift.

Landmark Transaction.

NEM's future flow issuance secured by remittance flows was an historic and landmark transaction. It represented NEM's first investment-grade issuance. The transaction is one of the largest future flow financings completed in Mexico, the first future flow financing based on remittances in Mexico since the early 2000s, and one of the largest financings of cross-border remittance flows closed in Latin America. Based on the strength of NEM's cash flows and the strength of the transaction structure, the company was able to successfully access the capital markets in the midst of a worldwide pandemic and an economic crisis.

Endnotes

[1] Mayer Brown acted as New York counsel for the Initial Purchasers in the transaction.