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Research Update:

CAP S.A. 'BB+' Ratings Placed On CreditWatch Negative On Weak Iron Prices And Stiff Competition

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Overview

- Weak global iron ore prices, due to sluggish steel consumption, and high competition from imported steel are likely to reduce CAP's EBITDA generation and weaken its financial metrics over the coming quarters.
- We have placed our 'BB+' ratings on Chile-based steel and iron ore producer on CreditWatch with negative implications.
- The negative CreditWatch listing reflects our view of a downgrade potential in the next 60-90 days if current ore prices persist and the company's credit metrics further weaken, absent mitigating factors.

Rating Action

On Dec. 22, 2015, Standard & Poor's Ratings Services has placed its 'BB+' corporate and issue-level ratings on CAP S.A. on CreditWatch with negative implications.

Rationale

Ratings on CAP continue to reflect its small scale of operations and historically low leverage. Nonetheless, lower-than-expected iron ore prices continue to pressure CAP's profitability and cash flow generation, resulting in weaker credit metrics for the past several quarters. Furthermore, steel consumption in Chile has decelerated slightly in 2015, pressuring steel prices. These factors were only mitigated by the company's efforts to improve its cost structure and reduce cash flow needs.

We still see volatility in global iron ore and steel prices, which could remain at or below current price levels, reflecting not only the slowdown in demand from China but also the producers' efforts to reduce costs. Furthermore, there are some uncertainties regarding potential impact on pellet premiums since Samarco Mineração S.A. (BB-/Watch Neg/--) has stopped operating after one of its tailings dams ruptured. Nonetheless, it seems unlikely that the hole left by Samarco in the pellet market will be enough to have a positive impact on pellet premiums. CAP has made efforts to reduce its mining and steel costs, also benefitting from the depreciated local currency. However that, combined with lower capex needs for the coming years, will only partly compensate for the impact of weaker prices. If current prices persist, it's unlikely that CAP's financial metrics will remain in the "intermediate"

financial risk category, such as debt to EBITDA of about 3.0x and funds from operations to debt above 30%.

CreditWatch

We expect to resolve the CreditWatch in the next 60-90 days as we review the company's forecasts amid weaker iron ore prices and considering potential countermeasures CAP may take to further offset these negative factors in its financial metrics and liquidity. We may lower the ratings if our forecast indicates that CAP will maintain a debt to EBITDA consistently above 3.5x for 2016, and if further price reduction could impact covenants or liquidity.

Ratings Score Snapshot

Corporate credit rating: BB+/Watch Neg/--

Business Risk Profile: Fair

- CICRA: Moderately High
- Competitive Position: Fair

Financial Risk Profile: Intermediate

- Cash flow/Leverage: Intermediate

Anchor: bb+

Modifiers:

- Diversification/Portfolio Effect: Neutral
- Capital Structure: Neutral
- Financial Policy: Neutral
- Liquidity: Adequate
- Management and Governance: Satisfactory
- Comparable Rating Analysis: Neutral

Related Criteria And Research

Related Criteria

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, - December 16, 2014
- Key Credit Factors For The Metals And Mining Upstream Industry, Dec. 20, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Corporate Methodology, Nov. 19, 2013
- Use Of CreditWatch And Outlooks, Sept. 14, 2009

Related Research

- CAP 'BB+' Ratings Affirmed And Off CreditWatch Negative On Likely Stronger Credit Metrics, Outlook Stable, May 7, 2015

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
CAP S.A.		
Corporate Credit Rating	BB+/Watch Neg/--	BB+/Stable/--
Senior Unsecured	BB+/Watch Neg	BB+

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