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Research Update:

Minsur S.A. 'BBB-' Corporate Credit And Issue-Level Ratings Affirmed; Outlook Remains Negative

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Overview

- The ratings on Peru-based tin mining company Minsur continue to reflect the support from its parent, Inversiones Breca, because we consider Minsur as a highly strategic subsidiary and the driver of the latter's group credit profile.
- We continue to assess Minsur's stand-alone credit profile (SACP) at 'bb+' amid favorable metals prices and cost-reduction initiatives that have improved Minsur's cash flow generation.
- The negative outlook still reflects our view that, despite some recovery in the performance of Breca's core subsidiaries, the downgrade in September 2015 of one of its equity affiliates, BBVA Banco Continental S.A. (BBB/Stable/--), coupled with continued volatility in commodity prices, weakened Breca's credit quality and could deteriorate its profitability and cash flow metrics, resulting in a downward revision of the group's credit profile and therefore, the ratings on Minsur.

Rating Action

On Nov. 30, 2016, S&P Global Ratings affirmed its 'BBB-' corporate credit and senior unsecured debt ratings on Minsur S.A. The outlook remains negative.

Rationale

Our ratings on Minsur consider it as a highly strategic subsidiary of its parent because we believe it's unlikely to be sold in the near term, which underscores the miner's importance to the group's long-term strategy and its reasonably successful operations. As a result, the ratings on Minsur incorporate one notch of parent support. Breca, through its subsidiaries, operates in the mining, insurance, financing services, and fishing sectors, among others. Although core subsidiaries showed some improvement in their credit metrics, we believe the continued volatility in commodity prices could depress Breca's profitability and cash flow metrics.

Our ratings on Minsur indicate stronger credit metrics and cash flow generation as a result of some improvement in metals prices, coupled with the company's efforts to optimize San Rafael and Pitinga production and reduce cash costs through various initiatives such as ore sorting and the Niobium and Tantalum floating plants.

The ratings on Minsur reflect its status as the fourth-largest tin producer in the world, its high EBITDA margins (because of the low-cost structure at its main mine, San Rafael), and vertical integration in the smelting process. However, the ratings also reflect Minsur's heavy reliance on one tin mine, which contributes about 61% of revenue and has a relatively short reserve life. We believe San Rafael will continue to contribute the bulk of Minsur's revenue over the next few years, leaving the company susceptible to tin price volatility. Nevertheless, we recognize the company's diversification efforts to broaden through the growth of its Brazilian operations, alongside Minsur's expansion of its product portfolio into niobium and tantalum alloys. The company has also the intention to expand into copper following its announcement to consolidate Marcobre's shares. This company is developing the Mina Justa copper project. However, the project is still in the feasibility stage and we expect it to be operational until 2020.

In 2016, Minsur successfully implemented its ore sorting project and finished repairs of its hydroelectric plant at the Pitinga-Pirapora complex. The company also doubled its ferroalloys production capacity at this complex. As a result, we expect these measures to raise Minsur's EBITDA margins to 36% by the end of 2016, which we consider as above average in the upstream mining industry. However, its EBITDA margins can be somewhat volatile, given tin and gold price fluctuations.

The company bolstered its operating cash flow generation; however, high capital expenditures in the following years to develop the Mina Justa project will cause a shortfall in free operating cash flow (FOCF). We expect Minsur's net debt to EBITDA to remain below 1.0x for the next 12 months, but it could jump while the company finances the Mina Justa project if no additional capital is raised, hurting the company's financial risk profile.

Our base-case assumptions incorporate the following factors:

- Average tin prices at about $17,261 per metric ton (MT) in 2016, and $19,356 per MT in 2017; average gold prices of $1,269 per ounce in 2016 and $1,250 per ounce in 2017.
- Overall refined tin production of 26,300 MT in 2016 and decreasing 3%-6% in 2017.
- Refined gold production of 105,000 ounces in 2016 and similar levels in 2017 at the Pucamarca complex.
- About 1,700 tons of ferroalloys produced in 2016 at Pitinga, more than doubling its production in 2017, due to capacity expansion in Pitinga, which will help to reduce cash cost sharply.
- All-in cash cost at San Rafael of $9,400 per treated ton in 2016 and increasing 13%-16% in 2017, mainly due to declining ore grades.
- All-in cash cost at Pucamarca of $311 per ounce in 2016 and increasing around 20% in 2017, mainly due to lower ore grades in line with the mine natural evolution.
- Flat revenue growth in 2016 and 8% in 2017 as tin prices rise due to a continued deficit in global tin supply.
- Capital expenditures (capex) in the area of $119 million for 2016 and

more than doubling its capex in 2017. We expect capex to increase significantly in 2017-2020 due to the Marcobre project that will result in a FOCF shortfall for those years.
- A $60 million outflow for the acquisition of the remaining 30% of the Marcobre project in 2016.
- No dividend payments are considered.

We arrive to the following adjusted credit metrics:
- Net debt to EBITDA of 0.7x in 2016 and 2017.
- FFO to debt of around 82% for 2016 and 2017.
- FOCF to debt of 50% in 2016 and -23% in 2017.

Liquidity

We now view Minsur's liquidity as adequate, reflecting the company's significant capital investments required to develop its Marcobre project, which are poised to start in 2017. We expect its sources to exceed its uses by at least 1.2x in the next 12 months, and that its net sources will be positive even with a 15% decline in forecasted EBITDA. The company's fluid access to bank credit lines supports our assessment of its liquidity.

Principal liquidity sources:
- Cash position of $400 million as of September 2016;
- Projected cash FFO of $180 million for the next 12 months; and
- Working capital inflows of $40 million for the next 12 months.

Principal liquidity uses:
- Short-term maturities of $100 million as of September 2016;
- Capex of $236 million for the next 12 months;
- $60 million to purchase the 30% stake at Mina Justa.

Outlook

The negative outlook still reflects our view that, despite some recovery in the performance of Breca's core subsidiaries, the downgrade of BBVA Banco Continental, coupled with continued volatility in commodity prices, weakened Breca's credit quality and could deteriorate its profitability and cash flow metrics, resulting in a downward revision of the group's credit profile. A weaker group credit profile would lead to lower corporate credit ratings on Minsur because they are capped at one notch below our assessment of the group credit profile. We'll keep monitoring Breca's credit quality, and the overall performance of its main subsidiaries as well as its perceived incentives to support Minsur, in case the latter needs it.

Downside scenario

We could downgrade Minsur if we were to lower our assessment on Breca's credit profile. We could also lower the ratings if we believe Minsur's strategic importance to the group has weakened.

Absent any revision to Breca's group credit profile, and assuming our assessment of a highly strategic subsidiary remains unchanged, a downgrade would occur if the company's SACP were to fall to 'bb-' or lower. Although unlikely, such a scenario could stem from unanticipated production disruptions, lower-than-expected metals prices, higher capex, or increased cash cost per ton produced, or if the company engages in aggressive capex that jeopardize its current credit metrics, leading to debt to EBITDA above 3.0x.

Upside scenario

Assuming no changes to the company's SACP, we could revise the outlook to stable within 12 months if Breca's group credit profile remains resilient to commodity price volatility and economic risks, particularly in the sectors where the group operates, resulting in a sustained improvement in the performance of Breca's core subsidiaries.

Ratings Score Snapshot

Corporate Credit Rating: BBB-/Negative/--

Business risk: Fair
- Country risk: Moderately high
- Industry risk: Moderately high
- Competitive position: Fair

Financial risk:
- Cash flow/Leverage: Intermediate

Anchor: bb+

Modifiers
- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Strong (no impact)
- Financial policy: Neutral (no impact)
- Management and governance: Fair (no impact)
- Comparable rating analysis: Neutral (No impact)

Stand-alone credit profile: bb+
- Entity status within group: Highly strategic

Related Criteria

- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Metals And Mining Upstream Industry, Dec. 20, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- Criteria - Corporates - Industrials: Methodology For Standard & Poor's Metals And Mining Price Assumptions, Nov. 19, 2013

- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 01, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Ratings List

Ratings Affirmed

Minsur S.A.	
Corporate Credit Rating	BBB-/Negative/--
Senior Unsecured	BBB-

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on the S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.