FITCH DOWNGRADES CAP S.A.'S IDRS TO 'BBB-' & NATIONAL RATING TO 'A+(CL)'; OUTLOOK STABLE

Fitch Ratings-Chicago/Santiago-22 September 2015: Fitch Ratings has downgraded CAP S.A.'s (CAP) Foreign and Local currency Issuer Default Ratings (IDRs) to 'BBB-' from 'BBB' and National Scale Rating to 'A+(cl)' from 'AA-(cl)'. The National Equity Rating has also been downgraded to Second Class Level '2(cl)' from First Class Level '1(cl)'. The Rating Outlook has been revised to Stable from Negative. A full list of rating actions follows at the end of this release.

A primary consideration in the downgrades is Fitch's more negative view of the long term price for iron ore. The drop in Fitch's long-term outlook for iron ore from $70/t to around $60/t per ton decreases CAP's annual EBITDA by around $180 million when production ramps up to above 18 million tonnes per year in 2018. At this pricing level, CAP's capital structure exhibits elevated leverage for a longer duration than previously envisaged. CAP's ratings were placed on Negative Outlook during March 2015 following weaker than expected financial performance and corresponding deterioration in credit metrics.

KEY RATING DRIVERS

Leverage Higher Through-the-Cycle

CAP's capital structure has weakened through-the-cycle to a level more consistent with a 'BBB-' rating, following the completion of its large investment program coinciding with a period of lower iron ore and steel pricing. Fitch expects CAP's net debt/EBITDA ratio to be around 3.0x in 2015 and 3.4x in 2016, improving to around 2.5x in 2017. These levels remain significantly above the company's historical average of below 1.0x for this ratio. While CAP's iron ore unit, CMP, exhibits iron ore pellet premiums close to those of the lowest cost pellet producer, Samarco (IDR 'BBB'/ Outlook Stable), overall profitability is diluted due to CMP's relatively lower margin products, such as sinter feed and lumps. CMP accounted for 70% of CAP's consolidated EBITDA during 1H15; while its steel business, CSH, accounted for 8%; steel processing, Cintac, for 8%; and the company's fledgling infrastructure division comprising 15% (from zero in 2014).

Product Mix Improvement

CMP's EBITDA/tonne in 2014 was $24/t compared to CSN at $20/t, Vale at $36/t, and Samarco at $63/t. The lower consolidated iron ore EBITDA/tonne in 2014 for CMP was a result of an inefficient product mix due to contractually committed sales for lower margin products. Going forward, CMP is increasing its shipments of high margin pellets to account for around 25% of the sales mix in 2015 from 14% in 2014. Sinter feed and lumps sales will also decrease from around 15% in 2014 and 12% in 2015 to below 10% from 2016 onwards. Fitch expects CMP's consolidated EBITDA/tonne to be $16/t in 2015, $10/t in 2016, $13/t in 2017 and $18/t in 2018. CMP's sales volumes are expected at close to 14 million tonnes in 2015, 15 million in 2016, 17 million in 2017 and over 18 million from 2018 based Fitch's mid-cycle commodity price assumptions for iron ore. Taking into account CMP's pellet product sales only, EBITDA/tonne was $63/t in 2014 compared to Samarco at $66/t and Vale's pellets at $61/t illustrating the company's competiveness for pellet products and the premium it commands for its magnetite pellets. Fitch expects CMP's pellet's to average EBITDA/tonne of around $35/t from 2016 - 2019 compared Samarco and Vale's pellets at above $40/t on average over the same period.

Cash Cost Improvement

CMP is on track to reduce its cash cost to around $37/t in 2015 from $49/t in 2014 on a FOB basis, and remain at similar levels going forward. CMP's cash cost was $36/t in 1H15 compared with $52/t in 1H14. The significant reduction has been achieved due to the depreciation of the Chilean Peso to around CLP/USD 660 in 2015 from CLP/USD 575 in 2014, with approximately 40% of CMP's COGS being denominated in local currency, combined with more efficient product mix and management focus on cost cutting measures. CSH's cost reduction followed a significant reduction in headcount mainly related to the exit from the flat steel business. Cintac has also been reorganized to exhibit a streamlined group structure with lower costs.

Return to FCF Generation

Fitch expects CAP's FCF to turn positive in 2015 and remain positive due to capex decreasing closer to maintenance levels of around $100 million following a three year period of major expansionary investments that totalled $2.2 billion between 2012 and 2014. The major components of these large investments were $1.2 billion for the new mine Cerro Negro Norte with fresh pellet feed production of 4 million tonnes a year; $442 million for the brownfield expansion at the Los Colorados mine to increase pellet and pellet feed production by 2 million tonnes annually; and $400 million and $70 million relating to the company's desalination plant (Cleanairtech) and electric transmission line (Tecnocap), respectively. No major new investments are planned by the company at present, with the El Romeral expansion project on hold due to current prices of iron ore. Fitch's expectations for CAP include that the company reduces its dividend payments through 2015 - 2017 in line with the lower net income generated during the lower price environment.

Long Life Reserves and Resources, Strong Assets

CAP has 2.3 billion tonnes of iron ore reserves and 6.4 billion tonnes of resources that equate to 57 years of mine life at an expected production rate of 15 million tonnes per year. The current ramp-up plan projects production to reach over 18 million tonnes per year by the end of 2018. The company owns and operates four mines distributed across two regions in northern Chile. These operations are complemented by three ports at equal distances across the two regions, a pellet plant with current capacity of 5.2 million tonnes per year, a magnetite plant, a desalination plant, a power transmission line, and an 80 km iron ore slurry pipeline that results in low logistical costs for the company. In addition, CAP owns a long steel mill with one operating blast furnace, and a specialty steel company with operations in Chile, Peru and Argentina.

National Equity Rating Rationale

CAP has a long trading history with over 30 years in the Santiago stock exchange market, standing out as a valuable company in the local market. As of Sept. 21, 2015 the company's market capitalization decreased to USD470 million from USD2.3 billion in March 2014. The company's shares are highly liquid with a market presence of 100% with last year's average volume estimated at USD 1,960 million as of September 2015. The downgrade to level 2 from level 1 is related to the deterioration of CAP's solvency to 'A(cl)' category, despite highly liquid equity indicators.

KEY ASSUMPTIONS

Fitch's key assumptions within the rating case for CAP include:

--Improved product mix with self-fluxing and direct reduction iron ore pellets comprising around 25% of sales in 2016 and beyond;
--Iron ore volumes increasing incrementally from around 14 million in 2015 to over 18 million by 2018;
--Iron ore cost of production of around $38/t;

--EBITDA of around $300 million in 2015;
--$50/t iron ore in 2016 and $55/t in 2017 with $60/t being the long-term price;
--Positive EBITDA from CSH and Cintac amounting to around $40 -$50 million per year;
--Cleanairtech and Tecnocap EBITDA of around $45 million per year, on average;
--Successful refinancing of $350 million syndicated loan in the long term during 2016.

RATING SENSITIVITIES

CAP is exposed to inherent risks within the mining and steel industries. A negative rating action -- in either the form of a downgrade, Negative Outlook, or both -- could result from deterioration in the company's capital structure that is not addressed in the short term. A sustained period of depressed iron ore prices and/or a significant loss of sales volumes due to a more accelerated slowdown in Chinese iron ore consumption that prevents the company's net debt to EBITDA ratio from declining to 2.5x and below on a sustained basis could also result in a negative rating action, as could a significant and prolonged deterioration in CAP's liquidity position and persistent negative FCF.

Positive rating action on CAP could follow significant improvement in the company's scale and growth of higher margin magnetite pellet sales, while maintaining consistently positive FCF generation and conservative credit metrics with an average net debt to EBITDA ratio below 1.0x through-the-cycle.

LIQUIDITY

Covenant Headroom and Robust Liquidity:

CAP has renegotiated financial covenants relating to its syndicated loan of approximately $200 million (of which $100 million has been amortized) and three RCFs totalling $500 million, of which $300 million remains undrawn, providing significant headroom. This was a pro-active measure taken by management following a drop in the average price of iron ore to below $60/t during 1H15 from an average of $97/t in 2014. The revised net financial debt/EBITDA covenant has been increased to 5.5x for the rest of 2015 and 2016, reverting back to 4.0x in 2017 following the maturity of the syndicated loan in April 2016, allowing for a significant buffer should prices fall below $50/t on a sustained basis during that time. The company held cash and equivalents of $398 million as of June 30, 2015 and has the additional $300 million of committed lines of credit still available. Short term debt of $460 million mostly relates to CAP's syndicated loan facility due in April 2016 and CMP's short-term facilities for working capital purposes.

FULL LIST OF RATING ACTIONS

Fitch has downgraded the following ratings:

CAP S.A.

--Foreign currency IDR to 'BBB-' from 'BBB';
--Local currency IDR to 'BBB-' from 'BBB';
--Yankee bonds due 2036 to 'BBB-' from 'BBB';
--National-scale to 'A+(cl)' from 'AA-(cl)';
--National equity ratings to Primera Clase Nivel '2(cl)' from '1(cl)';
--Local bonds No. 434 (series F) and No. 435 to 'A+(cl)' from 'AA-(cl)';
--Local debt issuance program No. 591 to 'A+(cl)' from
'AA-(cl)';
--Local debt issuance program No. 592 to 'A+(cl)' from
'AA-(cl)'.

The Rating Outlook is Stable.

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Date of Relevant Rating Committee: September, 21, 2015.

Additional information is available on www.fitchratings.com.

Applicable Criteria
Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage (pub. 17 Aug 2015)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=869362
National Scale Ratings Criteria (pub. 30 Oct 2013)
https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=720082