STANDARD & POOR'S RATINGS SERVICES
McGRAW HILL FINANCIAL

RatingsDirect®

Research Update:

Polish Soda Ash Producer Ciech Upgraded To 'BB-' On Strong Operating Performance And Lower Leverage; Outlook Stable

Primary Credit Analyst:
Paulina Grabowiec, London (44) 20-7176-7051; paulina.grabowiec@standardandpoors.com

Secondary Contact:
Andrey Nikolaev, CFA, Paris (33) 1-4420-7329; andrey.nikolaev@standardandpoors.com

Table Of Contents

Research Update:

Polish Soda Ash Producer Ciech Upgraded To 'BB-' On Strong Operating Performance And Lower Leverage; Outlook Stable

Overview

- We anticipate that Poland-based soda ash producer Ciech SA will report strong results in 2015 and 2016, benefiting from high soda ash prices and an increase in sales volumes.
- As a result, we anticipate that Ciech's leverage will decline to about 2.1x-2.4x in 2015 and further to about 2.1x-2.3x in 2016, from 2.4x in 2014.
- We are therefore raising our corporate credit rating on Ciech to 'BB-' from 'B+'.
- The stable outlook reflects our expectation that Ciech will maintain strong operating performance, demonstrated by reported EBITDA margins of at least 18% in the coming years, and that it will generate material positive free operating cash flows from 2017, leading to further reductions in leverage.

Rating Action

On Nov. 25, 2015, Standard & Poor's Ratings Services raised its long-term corporate credit rating on Poland-based soda ash producer Ciech SA to 'BB-' from 'B+'. The outlook is stable.

At the same time, we raised to 'BB-' our issue rating on Ciech's €245 million bond. The issue rating will be withdrawn after the company redeems the bond on Nov. 30.

Rationale

The rating actions indicate that we expect Ciech to report strong results in 2015 and 2016, and anticipate that it will sustain reported EBITDA margins of at least 18%.

Over the past 12-18 months, Ciech has benefited from favorable industry conditions, including:

- Strong soda ash prices supported by growing demand for soda ash in Central and Eastern Europe (CEE) and capacity curtailments at competitors such as Solvay Pavoa and Tata Chemicals;
- Higher sales volumes as a result of capacity additions in Poland and Romania; and
- A reduction in the cost of important raw materials, especially coal, and

energy.

Management has maintained its focus on cost control and internal efficiencies, which we consider has supported operating performance.

Ciech expects to expand capacity in its key profit-generating soda ash business in 2016, producing an additional 140 kilotons of soda ash per year. Once this expansion has come onstream in the first quarter of next year, we understand that it intends to focus on organic growth, notably in its Organika Sarzyna business. This includes further development of its crop protection products distribution network in Poland, and registration of these products for sale in Western European markets.

As a result, we anticipate that Ciech's capital expenditure (capex) should decline in 2017 from about PLN500 million in 2016. This reduction in investments, combined with the forecast stable performance, should lead to material positive free operating cash flows (FOCF) and a further reduction in leverage. Ciech's financial policy is to sustain net debt to EBITDA (as defined by the company) of 1x-2x; we view this as an important positive factor.

Under our prudent base-case scenario, we forecast that Ciech will report EBITDA of about PLN630 million-PLN650 million in 2015, and moderate growth in 2016. Based on pro forma Standard & Poor's-adjusted debt of about PLN1.5 billion at end-2015, we anticipate Ciech's leverage will decline to 2.1x-2.4x from 2.4x in 2014, and further to about 2.1x-2.3x in 2016 as the company's EBITDA grows.

In our base-case scenario, we assume:
- Reported EBITDA margin of above 20% in 2015 and 19%-20% in 2016, supported by favorable soda ash and feedstock prices;
- Capex of about PLN500 million in 2015 and 2016;
- No dividends in 2015, as announced, with modest amounts in 2016; and
- No acquisitions.

Based on these assumptions, we arrive at the following credit metrics:
- Adjusted debt-to-EBITDA of 2.1x-2.4x in 2015, and about 2.1x-2.3x in 2016; and
- Moderate negative FOCF in 2015 (including refinancing costs) and positive in 2016.

Based on the above ratios, we revised upward our financial risk profile assessment to significant.

We continue to view Ciech's business risk profile as constrained by high exposure to the cyclical packaging and construction industries, which are Ciech's key end-markets; its limited product diversity through its core soda ash production; and its reliance on a small number of suppliers for key raw materials such as brine and limestone. We factor this into our comparable rating analysis, constraining the rating by one notch. However, we recognize that there is some backward integration, notably of the company's Polish operations into steam production and electricity, and its German operations into limestone, brine, and also into steam and electricity.

Liquidity

We assess Ciech's liquidity as adequate. We estimate that liquidity sources should cover liquidity uses by more than 1.2x over the next 12-18 months. We also anticipate that Ciech will comply with the net leverage covenant of 4x incorporated in its new revolving and term facility documentation.

We anticipate the company will have the following principal liquidity sources over the next 12 months:

- About PLN500 million of funds from operations under our base case;
- Full availability under the PLN250 million long-term committed RCF; and
- PLN190 million of cash, pro forma the refinancing transaction.

We anticipate the company will have the following principal liquidity uses over the same period:

- About PLN500 million of capex in the next 12 months;
- No material short-term debt maturities (the series 02 PLN160 million domestic notes mature in 2017);
- PLN60 million of intrayear working capital outflows; and
- Modest dividends.

Outlook

The stable outlook reflects our view that Ciech will be able to maintain strong operating performance, with reported EBITDA margins of at least 18% in the coming years, and that it will generate material positive FOCF from 2017, leading to further deleveraging. We view an adjusted ratio of debt to EBITDA of about 2.5x-3.0x on average as commensurate with 'BB-' rating.

Upside scenario

We do not exclude the possibility of raising the rating in 2016-2017. Supportive factors could include Ciech increasing its track record of strong operating performance and positive FOCF as the company finalizes its heavy investments in soda ash capacity expansion. We could also raise the rating if we saw evidence of successful diversification into the crop protection business as well as supportive financial policies. We view an adjusted debt to EBITDA of about 1.5x-2.5x as commensurate with a higher rating.

Downside scenario

We could consider a negative rating action if we observed a deterioration in Ciech's leverage to 3.5x-4.0x, for example, as a result of weaker-than-anticipated margins, unexpected dividends or acquisitions, or higher capex.

Ratings Score Snapshot

Corporate Credit Rating: BB-/Stable/--

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

Financial risk: Significant
- Cash flow/Leverage: Significant

Anchor: bb

Modifiers
- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Financial policy: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Management and governance: Fair (no impact)
- Comparable Rating Analysis: Negative (-1 notch)

Structural Subordination

The issue rating on the €245 million senior secured notes issued by Ciech Group Financing AB is 'BB-', in line with the corporate credit rating. We consider that the structural subordination of the notes is not material, and is effectively mitigated by an extensive security package.

In terms of the insolvency jurisdiction, any insolvency proceedings against Ciech would most likely originate in Poland. Although we have assigned an issue rating to the €245 million notes, we have not assigned a recovery rating because our review of Poland's insolvency regime is not complete.

For detailed structural subordination analysis, please see "Poland-Headquartered Soda Ash Producer Ciech Assigned 'B' Rating; Outlook Stable," published on Dec. 18, 2012, on RatingsDirect.

Related Criteria And Research

Related Criteria
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Key Credit Factors For The Commodity Chemicals Industry, Dec. 31, 2013
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013

- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Ratings List

Upgraded

	To	From
Ciech SA		
Corporate Credit Rating	BB-/Stable/--	B+/Stable/--
Ciech Group Financing AB		
Senior Secured	BB-	B+

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@standardandpoors.com

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.