

Research Update:

Swiss Chemicals Company Clariant 'BBB-/A-3' Ratings Placed On CreditWatch Negative On Süd-Chemie Acquisition

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Overview

- Swiss-based specialty chemicals company Clariant AG has announced its intention to acquire German chemical company Süd-Chemie AG.
- The acquisition's enterprise value is significant, in our view, at Swiss Franc (CHF) 2.5 billion, but 40% of this will be funded through shares.
- We are placing the 'BBB-/A-3' ratings on Clariant on CreditWatch negative.
- The CreditWatch reflects our view of the downward pressure on Clariant's currently robust credit metrics that we believe will arise as a result of the acquisition.

Rating Action

On Feb. 17, 2011, Standard & Poor's Ratings Services placed the 'BBB-' long-term and 'A-3' short-term corporate credit ratings on Swiss-based specialty chemicals company Clariant AG on CreditWatch with negative implications.

Rationale

The CreditWatch placement follows Clariant's acquisition offer for German chemicals company Süd-Chemie AG and reflects the increased debt and lower credit metrics that we anticipate will result from this sizeable acquisition. We view the enterprise value of Swiss franc (CHF) 2.5 billion that Clariant has offered for Süd-Chemie as high compared to Süd-Chemie's reported 2010 EBITDA of €191 million (about CHF250 million). However, we also recognize Süd-Chemie's high EBITDA growth of 12% per year over the past six years. In addition, we take into account Clariant's pre-acquisition financial leeway and the fairly prudent way in which we think the transaction has been structured, with 40% (or CHF1.1 billion) of the acquisition price to be paid in shares.

As a consequence of the acquisition, we believe that Clariant's ratio of Standard & Poor's-adjusted funds from operations (FFO) to debt could drop to about 30% in 2011 and 2012 under our preliminary credit scenario, from a robust 56% at year-end 2010. The combined group's free cash flow is likely to be negative in 2011, in light of planned increases in capital expenditures, and expected cash outflows for working capital and ongoing restructuring. At the same time, we think that Clariant's business profile will benefit from greater diversity, higher profitability, and better growth potential, thanks

to Süd-Chemie's product range of catalysts and adsorbents.

Clariant's strong 2010 cash generation has resulted in material financial headroom: its reported net financial debt decreased to a low CHF126 million at year-end 2010 from CHF545 million at the end of 2009. Fully adjusted debt, net of surplus cash, stood at CHF937 million at the end of 2010.

We take a positive view of management's effectiveness in reducing costs and focusing on profitability. For instance, Clariant's reported EBITDA margins before restructuring jumped to 12.7% in 2010, up from a low 7.5% in 2009 and 9.7% in 2008, albeit in the context of a record year for the whole industry. In addition, FFO recovered to CHF530 million in 2010 (despite ongoing restructuring costs) from CHF300 million in 2009.

Liquidity

We project that Clariant's liquidity will be adequate after the acquisition, in view of its large cash balances and assuming that the company puts an acquisition bridge facility into place in the coming month. We also factor in our view that the bridge facility will be refinanced with longer-term debt within 6 to 12 months after the acquisition.

At end-December 2010, we estimated liquidity sources for the next 12 months at about CHF1.7 billion, including:

- A large CHF1.4 billion in reported cash and securities, of which we treat CHF150 million as tied to operations; and
- FFO of about CHF600 million.

This compares with potential liquidity uses in the same period comprising:

- CHF240 million of short-term debt. Maturities in 2012 are also modest, at CHF250, whereas a large €600 million bond matures in April 2013;
- Capital spending that we assume will rise to above CHF300 million; and
- A sizeable cash outlay of about CHF1.5 billion in relation to the Süd-Chemie acquisition. We understand that about CHF0.9 billion will be funded through a new acquisition facility, and about CHF0.5 billion from cash balances.

As Clariant cancelled its syndicated back-stop facility in early 2010, we understand that the company's policy consists of maintaining material cash balances in excess of CHF0.5 billion, which we understand will continue post acquisition. If and when liquidity decreases, we anticipate that the company will put some committed back-up lines in place again.

CreditWatch

We aim to review the CreditWatch in the coming weeks, once we have further analyzed the group's business plan, acquisition funding, and Süd-Chemie's chemicals activities.

We anticipate that the sizeable and part-debt-financed acquisition will result in lower credit metrics as stated above. A downgrade or affirmation would, in the first instance, depend on the extent to which we reassess the group's business risk profile as a result of the acquisition and the improved profitability at Clariant; and on how we think the credit metrics are likely to improve post acquisition under our credit scenario.

Related Criteria And Research

All articles listed below are available on RatingsDirect on the Global Credit Portal, unless otherwise stated.

- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Business Risk/Financial Risk Matrix Expanded, May 27, 2009
- Key Credit Factors: Business And Financial Risks In The Commodity And Specialty Chemical Industry, Nov. 20, 2008

Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

	To	From
Clariant AG		
Corporate Credit Rating	BBB-/Watch Neg/A-3	BBB-/Stable/A-3
Senior Unsecured Debt	BBB-/Watch Neg	BBB-
Clariant Finance (Luxembourg) S.A.		
Senior Unsecured Debt*	BBB-/Watch Neg	BBB-

*Guaranteed by Clariant AG.

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Complete ratings information is available to subscribers of RatingsDirect on the Global Credit Portal at www.globalcreditportal.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) 495-783-4011.

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