

Summary:

Clariant AG

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Table Of Contents

Rationale

Outlook

Related Criteria And Research

Summary:

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Credit Rating: BBB-/Negative/A-3

Rationale

The ratings on Switzerland-based specialty chemicals manufacturer Clariant AG reflect Standard & Poor's Ratings Services' view of the company's "satisfactory" business risk profile and "significant" financial risk profile. Clariant's product portfolio comprises a very wide spread of industrial and consumer specialties and pigments used in paints, dyes, and plastics. It also has leading market positions in leather and textile chemicals, surfactants, and bleach activators for detergents. Its acquisition this year of Süd-Chemie added adsorbents and catalysts to Clariant's business mix as well as a portfolio of proprietary technologies in the high-growth areas of energy storage and renewable energy.

Clariant's "satisfactory" business risk profile is underpinned by its wide product range and its diversified global sales growth. We also factor in the positive impact of the Süd-Chemie acquisition on the business profile that added catalyst and adsorbents businesses to Clariant's portfolio. We believe this will enhance diversity as well as exposure to more stable end-markets with higher margins and growth rates. Other positive factors include Clariant's strongly improved profitability over the past 12 months. Nevertheless, we view as key negative credit factors Clariant's poor profitability historically, and the related large and recurring restructuring. Other main weaknesses, in our view, are the cyclical nature of the chemicals industry, margin sensitivity to economic conditions, and exposure to volatile raw material costs.

Our assessment of Clariant's financial risk profile as "significant" chiefly reflects the issuer's deteriorated credit ratios following the Süd-Chemie acquisition and our expectation that deleveraging will occur only in 2012 and 2013. We see as relative strengths Clariant's currently adequate liquidity, even though debt maturities are still concentrated in 2012-2013. We also view as positive management's financial track record and its focus on cash generation.

S&P base-case operating scenario

In our base-case assessment, we anticipate that Clariant's reported revenues, including eight months of consolidated Süd-Chemie figures, will exceed Swiss franc (CHF)7.0 billion (€5.7 billion) in 2011. We anticipate that Clariant will report EBITDA before exceptional items of about CHF900 million in 2011. This follows reported EBITDA of CHF734 million in the first nine months of 2011. We revised downward our previous expectation of CHF1 billion EBITDA, as Clariant has been materially negatively affected by foreign exchange developments as a result of the strong Swiss franc, and as we anticipate a weak fourth quarter with the sector likely to face destocking and margin pressure.

For 2012, our base case assumes zero sales volume growth for the sector, a strong Swiss franc-euro exchange rate as seen in 2011, and a reversal to mid-cycle margins. This results in a baseline rating assumption of mid-cycle 2012 EBITDA of approximately CHF900 million, including full consolidation of the Süd-Chemie acquisition, and compares with the CHF1.1 billion we forecast earlier this year. The full benefit of the company's ongoing cost reduction and network optimization program should, however, be visible only in 2013, in our view, as should

expected synergies from the Süd-Chemie acquisition.

S&P base-case cash flow and capital-structure scenario

We forecast unadjusted net financial debt rising to about CHF1.9 billion at the end of 2011 (or CHF2.7 billion after our adjustments) under our credit scenario. We consequently forecast that the ratio of adjusted funds from operations (FFO) to debt will drop to a mere 20% in 2011. Under our revised credit scenario, we expect the ratio to recover to 20%-25% in 2012 and to improve to about 30% in 2013 on the basis of decreasing debt. This is down from our forecasts earlier this year of 28% for 2012 and 33% for 2013.

Liquidity

We assess Clariant's liquidity position as "adequate" under our criteria. The ratio of liquidity sources to liquidity needs is comfortably above 1.2x over the next 12 months. Liquidity may, however, become less than adequate from April 2012, when the acquisition facility becomes short term, and in 2013 when debt maturities become lumpy.

Liquidity sources as of Sept. 30, 2011, consisted of:

- CHF1.1 billion in cash and equivalents, of which we treat CHF150 million as tied to operations;
- Availability of CHF420 million under the CHF820 million bridge facility, with a final maturity until April 2013;
- FFO of about CHF500 million-CHF600 million; and
- Proceeds from new debt issuance of €365 million (CHF450 million) in October 2011, with terms of three years (€242 million) and 4.5 years (€123 million).

This compares with liquidity sources over the next 12 months of CHF1.6 billion, including:

- CHF1.1 billion of short-term maturities (of which about CHF450 million relate to short-term working capital facilities). This excludes CHF400 million of short-term advances relating to the bridge facility maturing in April 2011, which could be extended by another year at the company's option. However, this would make 2013 maturities, including the bridge outstandings, amount to a lumpy CHF1.2 billion; and
- Investments of about CHF450 million.

So far, Clariant has made substantial progress in refinancing the financial liabilities acquired with the acquisition of Süd-Chemie and parts of the original CHF1.12 billion bridge facility due March 2013, notably by issuing two bonds in the second quarter of 2011 amounting to CHF300 million and four German certificates of indebtedness amounting to €365 million in October 2011.

The acquisition bridge facility includes a net debt-to-EBITDA covenant. We currently estimate covenant headroom to be comfortable, at about 30% under our scenario.

Outlook

The negative outlook on Clariant reflects our view of the uncertain pace of future deleveraging, as well as the deteriorating chemical business environment over the past few months, which has increased the likelihood that we could take a negative rating action over the coming quarters. We therefore anticipate that near-term adjusted FFO-to-debt ratios are likely to be closer to 20% versus the 30% that we see as consistent with the ratings. This ratio guidance is based on mid-cycle EBITDA, which we use in our credit scenario.

We could therefore lower the rating by one notch in the coming quarters, depending on management actions and

increased visibility for 2012. We would likely consider a downgrade in the event of a "double dip" macroeconomic scenario, accompanied by a material drop in volumes in 2012 and/or if Clariant's 2011-2012 EBITDA risked being below our base-case assumption of CHF900 million. A downgrade could also arise if the company did not make further progress in the next quarters in refinancing the April 2013 CHF1.12 billion acquisition bridge facility and/or in reducing lumpy debt maturities in 2012-2013.

We would consider revising the outlook to stable if Clariant made adequate progress on refinancing and if the company's deleveraging and improvement in credit ratios are better in 2012 than we currently assume. We would also consider as positive further structural improvements in profitability from ongoing restructuring and synergies from Süd-Chemie.

Related Criteria And Research

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

- Corporate Criteria: Analytical Methodology, April 15, 2008
- Criteria Methodology: Business Risk/Financial Risk Matrix Expanded, May 27, 2009
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Sept. 28, 2011
- Key Credit Factors: Business And Financial Risks In The Commodity And Specialty Chemical Industry, Nov. 20, 2008

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