FITCH AFFIRMS VOLCAN'S IDRS AT 'BBB-'; OUTLOOK STABLE

Fitch Ratings-Chicago-08 January 2013: Fitch Ratings has affirmed the long-term Issuer Default Rating (IDR) of Volcan Compania Minera S.A.A. (Volcan) at 'BBB-'. The Rating Outlook is Stable. Fitch has also affirmed the 'BBB-' rating on the company's USD600 million senior unsecured 5.375% notes due 2022. A complete list of ratings is provided at the end of this release.

Ratings Supported by Strong Capital Structure:

The ratings reflect Volcan's diversified mining operations, historical track record of maintaining a conservative capital structure, strong cash flow generation, and low cash cost of production. The company's operations are located in Peru (rated 'BBB'; Outlook Stable by Fitch), which has vast mineral resources. According to Wood Mackenzie and the Peruvian Ministry of Energy and Mining production figures for 2011, Volcan ranks as the largest producer of zinc, silver and lead in Peru and the sixth largest producer of these metals globally. The company's size relative to its peers allows it significant negotiating leverage due to its ability to provide large volumes of a variety of metals. The company is listed on the Lima, Santiago and Madrid Stock Exchange.

Modest Leverage and Strong Liquidity:

Volcan has historically maintained a very low leverage position with an average total debt-to-EBITDA ratio from 2011 to 2007 of just 0.3x. As of the LTM ended Sept. 30, 2012, Volcan's total debt to EBITDA and net debt to EBITDA ratios increased to 1.6x and 0.2x, respectively, following the issuance last year of USD600 million 5.375% notes due 2022 to fund its expansionary capex program to 2015. The company has a good track record of making early prepayments of debt and holding a comfortable cash position to maintain strong liquidity, in addition to access to credit lines with banks. Volcan's cash and marketable securities as of Sept. 30, 2012, was USD607 million.

Product and Mine Diversification Supports Ratings:

Volcan's revenues are diversified over eight mining operations and six concentrator plants spread across the Cerro de Pasco, Yauli, and Chungar regions of the Peruvian Central Highlands. Volcan has exhibited solid revenue growth to USD1.1 billion for the LTM to Sept. 30, 2012 from the trough of USD627 million in 2008. In 2011, zinc accounted for 42% of total sales, silver 48%, lead 7%, and copper 3%. The diversification by mine and product is positive as it minimizes the company's exposure to labor strikes and provides it with a relatively assorted end-customer base.

Revenue growth has been fuelled by robust commodity demand, especially from China, and a sustained period of high prices. Volcan's sales are mostly made through stable long-term contracts around four years in length, with the contract prices adjusted annually based on average prices for the year. The company's largest customer is Glencore, which is also a minority shareholder in Volcan with 6.3% interest and holds a seat on the company's Board of Directors. The structure of these contracts, as well as the company's relationship with Glencore, the world's largest commodity trading house, minimizes demand risk to a degree.

High Profitability due to First-Quartile Production Cost Position:

Volcan is well positioned at the bottom of the cost curve as a first-quartile, low cost, polymetals producer. This allows it to generate positive operating cash flows through troughs in the demand cycle. For the period spanning January to September 2012, Volcan had a total cash cost for its overall zinc ore production of USD54 per metric ton, or just USD0.02 per pound. Helping to achieve this low production cost for zinc are the by-products of silver, lead and copper. For silver, the by-products include zinc and copper. With the production of fine zinc at 228,095 metric tons and fine silver at 16,348 thousand troy oz during the first nine months of 2012, the company is well placed to achieve strong cash flows. Total production volumes for pure zinc and silver during 2011 were 318,435 metric tons and 21,136 thousand troy oz, respectively.

Cash Flow Generation is Historically Strong but Negative FCF Expected 2012-2014:

Volcan has generated positive levels of free cash flow (FCF) during 2009 to 2011, a period that included two years of great volatility. Fitch projects that the company will generate cash flow from operations (CFFO) in the region of USD350 million to USD375 million in 2012. Capex in 2012 is anticipated in the USD450 million to USD500 million range, resulting in negative FCF of between USD150 million to USD200 million. This compares to FCF of USD21 million in 2011, which followed CFFO of USD470 million, capex of USD328 million and dividends of USD122 million. Fitch expects FCF to remain negative throughout the four year expansion capex program totalling USD1.1 billion and turn positive in 2015.

Volcan has exhibited high EBITDA margins historically, averaging around 49% for the last four years. EBITDA has grown at a CAGR of 15.1% to USD453 million for the LTM to Sept. 30, 2012 from USD241 million in 2008. Fitch's base case scenario for EBITDA generation in 2012 is conservative at around USD400 million, with total expected debt of around USD700 million. This equates to a total debt to EBITDA ratio of 1.7x. Fitch's revenue and EBITDA base case expectations for 2013 are around USD1 billion and USD480 million, respectively, with a net debt to EBITDA ratio of around 0.4x. Key assumptions are prices for zinc of USD1,900 million per tonne in 2013 and USD2,050 long term, and copper of USD7,500 per tonne and USD6,500 long term (see Fitch's Special Report: 'Initiating Mid-Cycle Metals Price Assumptions, published Sept. 14, 2012, available at www.fitchratings.com).

Ambitious Investments to Diversify into Copper by 2015:

The company's ambitious expansionary capital expenditure project will more evenly distribute sales of silver and zinc while expanding further into copper and gold and will make the company over 100% self-sufficient in energy by 2015. The company's capital expenditure plan began in 2011 and is scheduled to complete in 2015 at a cost of approximately USD1.1 billion over the period. Funding for this investment will be met through the USD600 million 5.375% notes issued in January 2012, combined with internal cash flow generation.

Volcan is positioned well for future growth in Peru. The company has 341,230 hectares of mining concessions across a region of significant geological reserves and is currently exploiting 12%, with a further 11% currently being explored. This equates to 18 years of reserves at current production levels or 37 years when including resources. As of Dec. 31, 2011, Volcan had over 136 million metric tons of proven and probable reserves, and over 224 million metric tons of additional resources.

Steady Demand Expected for Silver, Zinc and Copper:

Fitch's long-term outlook for silver and zinc is favorable, with silver prices correlated to gold as a less expensive investment, but also supported by its industrial uses such as for batteries and electronic components, among others. Zinc is well supplied at present, yet demand remains consistent. Stocks of zinc are declining and long-term supply is constrained due to a lack of projects in the pipeline. In addition to being an alloying agent for steel, zinc also has uses as an additive to fertilizers and in health supplements for human consumption. Volcan's expansion into copper, which also has good long-term fundamentals, and as a by-product of gold, will further diversify the company's revenues.

Location in Rating Scale:

Volcan's historical leverage and debt coverage ratios are strong within its 'BBB-' profile. The company's leverage ratios will increase during 2012 to 2015 compared to previous years as a result of its USD1.1 billion expansionary capex program, but they are expected to remain consistent within the rating category. Deterioration in the company's net debt to EBITDA ratio above 2.5x over a sustained period and/or a decline in profitability due to increased operating costs, could put negative pressure on the ratings. Swift deleveraging of total debt to EBITDA below 1.0x combined with successful execution of planned diversification of revenues substantially into copper would put positive pressure on the ratings.

Fitch affirms the following ratings of Volcan:

--Long Term IDR at 'BBB-';
--Local Currency Long Term IDR at 'BBB-';
--Senior Unsecured 5.375% Notes due 2022 at 'BBB-';

The Rating Outlook is Stable.

Fitch affirms and withdraws the following rating:

--National Long Term Rating at 'AA+(per)'.

This rating is withdrawn as it is no longer considered analytically meaningful.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

Applicable Criteria and Related Research:
--'Corporate Rating Methodology' (Aug. 8, 2012);
--'Parent and Subsidiary Rating Linkage' (Aug. 8, 2012);
--'National Ratings Criteria' (Jan. 19, 2011);
--'Evaluating Corporate Governance' (Dec. 12, 2012);
--'Initiating Mid-Cycle Metals Price Assumptions, Sept. 14, 2012.

Applicable Criteria and Related Research:
Evaluating Corporate Governance
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=694649
National Ratings Criteria

http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=595885
Parent and Subsidiary Rating Linkage
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=685552
Corporate Rating Methodology
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=684460
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