

## Rating Action: Moody's downgrades Volcan's ratings to B2; changes outlook to negative

31 Mar 2023

New York, March 31, 2023 -- Moody's Investors Service ("Moody's") has downgraded today Volcan Compania Minera S.A.A. y Subsidiarias ("Volcan")s corporate family rating (CFR) and senior unsecured rating to B2 from B1. The outlook was changed to negative from stable.

### Downgrades:

...Issuer: Volcan Compania Minera S.A.A. y Subsidiarias

.... Corporate Family Rating, Downgraded to B2 from B1

....Senior Unsecured Regular Bond/Debenture, Downgraded to B2 from B1

### Outlook Actions:

...Issuer: Volcan Compania Minera S.A.A. y Subsidiarias

....Outlook, Changed To Negative From Stable

### RATINGS RATIONALE

The downgrade of Volcan's ratings reflects the deterioration of the company's liquidity and credit metrics driven by negative free cash flow expected for 2023 and 2024 and incremental debt to fund the company's growth plan.

Moody's estimates that the company needs to raise around \$270 million in debt, out of which \$170 million will be incremental debt to fund its growth plan and around \$100 million to refinance debt maturing in 2024. While the company stated that it already engaged with market participants, Moody's believes that the announcement of Glencore plc (Glencore, Baa1 positive), its controlling shareholder, that it has commenced a process exploring the possible disposal of its 23.3% economic interest in Volcan, adds uncertainty to the already challenging operating and market environment. Following Russia's invasion of Ukraine, the ability for Emerging Market corporate issuers to access the international capital markets has sharply declined and Moody's expects that these conditions are unlikely to improve significantly in the near term.

The negative outlook reflects increasing refinancing risk related to the company's \$105 million in debt coming due in 2024 coupled with operational challenges that will continue to pressure margins.

Based on Moody's assumption of average zinc prices of \$1.3 per pound in 2023 and \$1.25 per pound in 2024, Volcan is expected to generate negative free cash flow of \$62 million in 2023 and \$81 million in 2024 driven by higher capex related to the expansion of Romina, a polymetallic project with an estimated investment of \$145 million through 2024. While the growth capex is discretionary, it is unlikely that the company will delay this investment as it is needed to support cash flow generation from 2025 onwards.

Similar to other mining operators, Volcan is facing important inflationary pressures with unit cost of production at \$55.5/MT as of the end of 2022, up from \$52.3/MT in 2021 and \$48.2/MT in 2020. Although Volcan put in place a plan called "Volcan Avanza" to control and reduce costs there are operational risks including potential disruptions due to social and political turmoil in Peru, which could affect the company's production output increasing unit costs.

Other sources of liquidity include the company's \$50 million in committed facility fully available until October 2023, potential assets sales and advance payments of its greenfield project Romina. However, nothing has been closed yet.

Volcan's B2 reflects the company's operational diversification in terms of metals produced and assets; and status as a leading producer of zinc and silver globally, with some of the largest zinc reserves. Volcan's B2 ratings also incorporate the company's modest scale compared with that of its global peers and its concentration in one country, as well as its high earnings volatility because of its exposure to commodity prices coupled with high cost structure, historically tight liquidity and aggressive financial policies.

Governance and Social factors are key considerations for this rating action. Considerations include the company's aggressive financial policies and high tolerance to refinancing risk as reflected in its Governance G-4 score. Volcan's Social score at S-4 reflects the company's geographic concentration in Peru, the company is highly exposed to the current social unrest in the country. Volcan's sites or operations have not been directly affected by road blockades because these are mostly concentrated in the central highlands of Peru. However, the immediate risk of blockades, supply chain delays and even production stoppage would increase if social unrest resumes.

### FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

An upgrade is unlikely at this point given the negative outlook. However, Moody's could stabilize the outlook if there is evidence of liquidity improvements and the company manages to secure funds to address its negative FCF gap and debt maturities through 2024 at least 12 months in advance. In addition, Volcan's ratings could be upgraded if it restores its cost position to below \$50/MT, enabling the company to better weather significant declines in metal prices, and continues to invest for growth, achieving higher scale, while maintaining adequate liquidity. Quantitatively, an upgrade would also require an EBIT margin above 8% and EBIT/interest expenses above 2x on a sustained basis.

Volcan's ratings could be downgraded if the company is unable to improve its profitability and financial profile. The ratings could be downgraded if Volcan's liquidity deteriorates further or the company is unable to secure the additional funding for growth capex and address its 2024 maturities. The ratings could also suffer negative pressure if Moody's-adjusted EBIT margin remains persistently below 6% and interest coverage, measured as EBIT/interest expenses remains below 1.5x.

The principal methodology used in these ratings was Mining published in October 2021 and available at <https://ratings.moodys.com/api/mc-documents/76085>. Alternatively, please see the Rating Methodologies page on <https://ratings.moodys.com> for a copy of this methodology.

Volcan Compania Minera S.A.A. y Subsidiarias (Volcan) is a Peruvian mining company that primarily produces zinc and lead concentrate and some copper concentrate, all with high silver content. The company operates through five operating units including seven operating mines, five concentrator plants and one leaching plant for silver oxide production. All of Volcan's operations are located in Peru, and it reported revenue of \$951 million for the 12 months that ended December 2022. Volcan is a holding company listed on the stock exchanges of Lima, Santiago and Madrid (Latibex). Since November 2017, Glencore has held a controlling stake of 55% in Volcan's Class A voting shares, which is equivalent to a 23.3% economic interest in Volcan.

### REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found on <https://ratings.moodys.com/rating-definitions>.

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[Volcan Compania Minera S.A.A. y Subsidiarias](#)

### Related Research

[Credit Opinion: Volcan Compania Minera S.A.A. y Subsidiarias: Update to credit analysis](#)

[Announcement of Periodic Review: Moody's announces completion of a periodic review for a group of Metals and Mining issuers in Latin America](#)

[Peer Snapshot: Volcan Compania Minera S.A.A. y Subsidiarias - September 2022 \(LTM\): Peer Snapshot](#)

[Peer Snapshot: Volcan Compania Minera S.A.A. y Subsidiarias - June 2022 \(LTM\): Peer Snapshot](#)

[Peer Snapshot: Volcan Compania Minera S.A.A. y Subsidiarias - March 2022 \(LTM\): Peer Snapshot](#)

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Rosa Morales  
Asst Vice President - Analyst  
Corporate Finance Group  
Moody's de Mexico S.A. de C.V  
Ave. Paseo de las Palmas  
No. 405 - 502  
Col. Lomas de Chapultepec  
Mexico, DF 11000  
Mexico  
JOURNALISTS: 1 888 779 5833  
Client Service: 1 212 553 1653

Marcos Schmidt  
Associate Managing Director  
Corporate Finance Group  
JOURNALISTS: 0 800 891 2518  
Client Service: 1 212 553 1653

Releasing Office:  
Moody's Investors Service, Inc.  
250 Greenwich Street  
New York, NY 10007  
U.S.A.  
JOURNALISTS: 1 212 553 0376  
Client Service: 1 212 553 1653



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