



## Rating Action: **Moody's downgrades Volcan's ratings to Caa1; outlook remains negative**

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New York, September 08, 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 Caa1 from B2. The outlook remains negative.

### Downgrades:

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

....Corporate Family Rating, Downgraded to Caa1 from B2

....Senior Unsecured Regular Bond/Debenture, Downgraded to Caa1 from B2

### Outlook Actions:

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

....Outlook, Remains Negative

### RATINGS RATIONALE

The downgrade of Volcan's ratings reflects increasing refinancing risk heightened by weak operating prospects that raise concerns over the company's cash flow generation capacity to meet upcoming debt maturities.

Moody's estimates that the company will generate USD 203 million of negative free cash flow (FCF) through 2024 (USD46 million during the second half of 2023 and USD157 million for the full year 2024) amid USD105 million in upcoming debt maturities through the end of 2024 (three USD35 million quarterly amortizations starting in 2Q23). This liquidity shortfall negatively compares to the company's USD 50 million in cash as of June 2023 and USD50 million in a committed revolving credit facility (RCF) available only until November 2023.

Other sources of liquidity include potential assets sales, advance payments of future production and the renewal of the company's RCF. However, it remains unclear when these potential transactions would be concluded and what amount the company could obtain out of these alternative funding sources.

While the company stated that it already engaged with market participants for asset sale and refinancing alternatives, Moody's believes that the announcement of Glencore plc ("Glencore", Baa1 positive), its controlling shareholder, that it commenced in February 2023 a process exploring the possible disposal of its 23.3% economic interest in Volcan, adds uncertainty to the already challenging operating and financial market environment.

The negative outlook reflects the limited financial flexibility to meet short-term debt maturities amid weakening cash flow generation capacity in the current global and domestic environment in Peru.

The downgrade also reflects governance considerations as key drivers of the rating action including the lack of visibility over a comprehensive plan to refinance upcoming maturities. The aggressive approach towards liquidity

management in tight credit conditions is reflected now in the company's Financial Strategy and Risk Management assessment that was changed to 5 from 4, the overall exposure to governance risks (Issuer Profile Score or "IPS") to 5 (G-5) and Volcan's Credit Impact Score to 5 (CIS-5), from 4. The ESG Credit Impact Score is CIS-5, revised from CIS-4, since ESG considerations are a major constraint for the rating.

The G-5 IPS also reflects Glencore's announcement that it commenced a process exploring the possible disposal of its economic interest in Volcan, which creates additional uncertainty around Volcan's financial strategy and ability to improve its liquidity profile.

Based on Moody's price sensitivity ranges of USD1.00 - USD 1.30 per pound in medium term, Volcan is expected to generate negative free cash flow of USD46 million in 2023 and USD 157 million in 2024. Negative free cash flow is a combination of: i) capex related to the expansion of Romina, a polymetallic project with an estimated investment of USD 145 million through 2024, ii) lower medium-term sensitivity ranges for zinc prices at USD1.0 – USD1.30 per pound from previous expectations of USD1.10 – USD1.40 per pound, and iii) persistent cost pressure, which will maintain the company's unitary cost of production at USD52 – USD53 / MT, a decrease versus USD55 /MT in 2022, but still high when compared to the 2017-2020 average of USD47 / MT. 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.

In August 16, 2023 Moody's lowered its price assumptions for certain metals and mining commodities, including zinc, to reflect softening economic growth, rising supplies on suspended production coming back on line, and mine expansions. Demand depends largely on the construction and automotive industries, which use zinc to galvanize steel. Low inventories point to potential higher prices later in 2023 and 2024 if demand recovers, but not to their 2022 highs.

Volcan's Caa1 ratings incorporate the company's high earnings volatility because of its exposure to commodity prices coupled with high cost structure, historically tight liquidity and aggressive financial policies, as well as its modest scale compared with that of its global peers and its concentration of operations in one country. At the same time, Volcan's Caa1 reflects the company's operational diversification in terms of metals produced and assets, with seven mines; an status as a leading producer of zinc and silver globally, with some of the largest zinc reserves.

#### 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 alternative liquidity sources 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 levels that would enable 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 7% and EBIT/interest expenses above 1.5x on a sustained basis.

Volcan's ratings could be downgraded if the company's liquidity worsens further or the company is unable to refinance the debt maturing in 2024, increasing the risk of a distressed exchange or debt restructuring.

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/rmc-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 USD754 million for the 12 months that ended June 2023. 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.

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At least one ESG consideration was material to the credit rating action(s) announced and described above.

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