

Rating Action: Moody's assigns a Baa3 rating to Mexichem's senior unsecured notes; stable outlook

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New York, September 28, 2017 -- Moody's Investors Service (Moody's) assigned a Baa3 rating to Mexichem, S.A.B. de C.V.'s (Mexichem) proposed up to \$1,120 million senior unsecured notes. The outlook is stable. The proceeds will be used to finance a portion of Mexichem's acquisition of an 80% stake in Netafim, Ltd, and general corporate purposes.

RATINGS RATIONALE

"The Baa3 rating is supported by Mexichem's strong credit metrics and market position, its ample liquidity and comfortable debt maturity profile. It also incorporates the company's adequate margins for the rating category coupled with the expectation that it will further benefit from (a) higher prices in fluorspar contracts, (b) higher polyvinyl chloride prices, (c) start of production of the ethylene cracker, and (c) the benefits from its acquisitions of high margin, value-added businesses." said Alonso Sanchez, a Vice President at Moody's.

"On the other hand, the rating reflects Mexichem's strategy to grow through acquisitions which increases its leverage and execution risk." added Sanchez. Execution risk is mitigated by Mexichem's good track record integrating acquisitions while capturing synergies and maintaining net debt/EBITDA below 2 times according to its internal policies. Also considered in the rating are the inherent volatility of the company's commodity linked cash flows and Mexichem's exposure to foreign exchange volatility in the countries in which it operates.

Mexichem will finance the approximately USD 1.5 billion related to the acquisition of its 80% stake in Israel-based Netafim with a combination of cash on hand and debt. The transaction will add about \$1,320 million in debt to Mexichem's balance sheet, raising its pro-forma adj. debt/EBITDA to 3.5 times; up from 2.8 times over the twelve months ended June 30, 2017. Still, Mexichem's management track record in integrating acquisitions eases execution risks. We estimate the company will be able to reduce its Moody's adjusted debt/EBITDA to around 2.6 times by year end 2018 through higher EBITDA generation from its current operations and synergies generated by Netafim's acquisition. We expect Mexichem's profitability will benefit from higher PVC prices, higher refrigerant gas prices in the US following the International Trade Commission favorable ruling against Chinese imports, and increased vertical integration with its ethylene cracker. At Netafim, Mexichem will obtain synergies from its strong clout with resin suppliers that should allow it to obtain better prices and from footprint rationalization with overlapping operations, amongst other.

The acquisition of Netafim is credit positive as it increases Mexichem's portfolio of value-added products and will broaden its geographic reach, while strengthening its presence in the irrigation market worldwide. Currently, Mexichem has a relatively small irrigation business, accounting for a modest 4% of sales in its Fluent business unit; which in turn contributes with around 53% of consolidated revenues. Following the acquisition, Mexichem will become the largest player in the \$3 billion worldwide micro-irrigation market; the acquisition will increase its revenue contribution to Mexichem's fluent business by over six times and will add around \$130 million of additional EBITDA per year. Netafim's irrigation solutions portfolio, including drip irrigation products, sprinklers and micro sprinklers, among others, will also complement Mexichem's actual product offering.

Mexichem's liquidity is strong. The company reported cash on hand of \$735 million as of June 30, 2017 that can cover 6.8 times its short-term debt. Pro-forma for the acquisition of Netafim, Mexichem will carry cash balances of around \$535 million that are enough to cover 4.9 times its short-term debt. In addition, Mexichem's liquidity position is also supported by its fully available \$1.5 billion committed credit facility that expires in 2019. While Mexichem will draw \$200 million from this facility to finance a portion of Netafim's acquisition it will continue to have ample availability under this credit facility.

For the twelve months ended June 30, 2017 Mexichem posted free cash flow (defined as cash from operations minus dividends minus capex) of \$129 million. As the company ended its large investment program for its ethylene cracker, capex will reduce to an average of around \$380 million per year in 2017-2019, down from an average of over \$630 million per year in 2014-2016. We anticipate Mexichem to maintain its dividend payout at

around \$105 million per year which will result in annual free cash flow of \$100 to \$200 million in 2018-2019. Pro-forma for the incremental debt for the acquisition of Netafim, Mexichem will continue to have a comfortable long-term debt maturity profile.

The stable outlook reflects our expectation that Mexichem's leverage will normalize towards historical levels over the next 12-18 months. It also incorporates our expectation that the company will maintain adequate liquidity and credit metrics for the rating category.

Mexichem's ratings could be upgraded if the company maintains a strong liquidity position and improves its profitability. Quantitatively, an upgrade would require EBITDA margins close to 20%, debt/EBITDA below 2.5 times and interest coverage above 11 times.

The ratings could be downgraded if the company's margins deteriorates such that EBITDA margin falls below 15%, or if leverage increases, for example due to a debt-finance acquisition, above 3 times on a sustained basis with no clear plan to de-lever. Deterioration in liquidity or an acquisition that is not accretive could also lead to a downgrade.

The principal methodology used in this rating was Global Chemical Industry Rating Methodology published in December 2013. Please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

Mexichem, S.A.B. de C.V. is one of the world's largest chemical and petrochemical company. A leader in the manufacture and supply of plastic piping, it contributes to global development by delivering an extended portfolio of products to high growth sectors such as infrastructure, housing, datacom and water cycle management. Mexichem manufactures its products under three divisions: (1) the Vinyl division produces chlorine, caustic soda, sodium hypochlorite, phosphate, ethylene, Vinyl Chloride Monomer, PVC resins and PVC compounds, (2) fluent division which produces PVC, polyethylene, polypropylene, geosynthetics (woven & no-woven), irrigation systems (water management) and datacom systems and infrastructure products, and (3) the Fluor division produces fluorinated products, hydrofluoric acid, and refrigerant gases. The company reported revenues of \$5.5 billion for the last twelve months ended June 30, 2017.

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