Research Update:

UNACEM Corp. S.A.A. 'BB' Rating Affirmed On Stable Credit Metrics; Outlook Remains Positive

June 26, 2023

Rating Action Overview

- Despite tough economic conditions and political turmoil in some of its key markets, we expect Peru-based building materials producer UNACEM Corp. S.A.A. (UNACEM) to maintain a steady operating performance and credit metrics in the next 12 months, even amid tight financing conditions and greater capital expenditures (capex).
- We also estimate UNACEM's liquidity will remain adequate in the next couple of years due to its solid cash flow. Nonetheless, larger debt maturities scheduled in the next 24 months increase its reliance on rolling over debt to fund expansionary capex.
- On June 26, 2023, S&P Global Ratings affirmed its 'BB' issuer credit rating on UNACEM.
- The positive outlook on UNACEM reflects a potential upgrade in the next six to 12 months if the company's liquidity cushion over debt maturities increases, while it keeps its net debt to EBITDA below 3.0x, consistently.

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Rating Action Rationale

The positive outlook reflects a potential upgrade of UNACEM to 'BB+' in the next 12 months if it increases its liquidity cushion and relies less on short-term financing. We expect the company to consistently improve its liquidity position in the next 12-24 months by maintaining adequate liquidity sources, including its cash reserves and funds from operations (FFO, defined as EBITDA minus cash interest and tax payments), and by proactively refinancing or extending upcoming debt maturities in 2023 and 2024. Currently, about PEN2.2 billion of UNACEM's debt, broken into different bank credit lines, matures within this timeframe. We estimate that the company's cash reserves and FFO for the next 12-24 months is sufficient to cover these debt maturities and minimum maintenance capex of close to $40 million. Nonetheless, we note that the higher use of short-term financing in the past few quarters has reduced the company's liquidity cushion.

We note UNACEM's capacity to postpone expansionary capex and dividend distributions, if needed. A more robust liquidity cushion of sources over uses, considering intra-year working capital needs and full capex, would prompt us to upgrade the company. In addition, we think

UNACEM has solid relationships with a diversified pool of creditors, which could enable some medium- to long-term refinancing, depending on the company's management's strategy to keep financing costs low.

We foresee that UNACEM's operating performance will remain resilient, despite tough economic conditions and political turmoil in some of its key markets. We anticipate a slowdown in cement demand in Peru and Ecuador (64% and 11% of UNACEM's consolidated revenues in 2022, respectively) due to record-high demand between 2021 and 2022, as well as social unrest and weaker economic activity. However, UNACEM's operations have proven resilient and maintained top-line growth. We expect the company's cement volumes in Peru to stabilize in the next few quarters, resulting in a contraction in volumes of 7%-8% for the fiscal year ending Dec. 31, 2023. Countrywide cement dispatches have contracted close to 12% year-to-date as of May 31, 2023. Moreover, concrete volumes have picked up in Peru, and we expect operations in the U.S. and Chile to remain fairly resilient in the next 12 months, although we have less certainty about Ecuador's performance. Overall, we estimate UNACEM's revenue will grow about 4% in the next 12 months, with concrete and energy revenues (including Termochilca's operations) and cement pricing offsetting a contraction in cement volumes, which remains UNACEM's key product.

On the other hand, profitability took a hit last year due to higher input costs, such as raw materials, fuel, and electricity. However, we now anticipate that inflationary pressures will ease in the next 12 months, which along with the company's pricing strategy, should gradually improve margins. Thus, we estimate that UNACEM's EBITDA margins will be close to 28% in the next 12 months, similar to its first-quarter 2023 result.

We expect UNACEM's strategy for the next couple of years to remain focused on operating efficiencies at different business units and pursuing opportunistic acquisitions or investments, while keeping its adjusted leverage below 3.0x. The company's latest acquisition of Termochilca S.A. (Termochilca; not rated) was completed earlier this year for about $140 million, of which $40 million will be paid in 2028. The acquisition includes a 300 megawatt (MW) combined-cycle gas plant. In our view, the assets acquired fit into UNACEM's energy division, which is consolidated under its subsidiary, Compañía Eléctrica El Platanal S.A. (CELEPSA; not rated). The division currently has 248 MW of capacity and modestly diversifies the company's business lines away from building materials. We expect UNACEM to keep pursuing small and midsize opportunistic acquisitions in the next couple of years, mostly targeting building materials or energy assets, while maintaining its net debt to EBITDA below 3.0x.

Outlook

The positive outlook on UNACEM reflects a potential upgrade in the next six to 12 months if the company's liquidity position improves, increasing its cushion of liquidity sources over uses by more than 20%, when considering short-term debt maturities and full capex. A rating upgrade would also require UNACEM to keep its net debt to EBITDA below 3.0x on a consistent basis.

Downside scenario

We could revise the outlook to stable in the next 12 months if UNACEM's net debt to EBITDA deteriorates from our base-case assumptions or if its liquidity position worsens. This could occur if the company's EBITDA and cash flows weaken, or if use of short-term debt increases. As a result, we could revise the outlook to stable if:

- UNACEM's net debt to EBITDA is consistently above 3.0x;
- Its discretionary cash flow-to-debt ratio is below 10% on a consistent basis; or
- Its liquidity position worsens beyond our expectations, with cash sources over uses below 1.2x in a 12-month period.

Company Description

UNACEM mainly operates in Peru, producing and selling cement, clinker, concrete, and energy--and to a lesser extent--in Ecuador, the U.S., Chile, and Colombia with concrete operations of ready-mixed and precast industrialized concrete structures. In Peru, the company offers bagged cement under several brands such as Cemento Andino, Cemento Sol, Cemento APU, and others. The company also provides bulk cement to construction, energy, and oil and gas companies.

Furthermore, through its subsidiaries--UNICON, CONCREMAX, and PREANSA--it sells ready-mix, manufactured cement, aggregates, pumps, concrete prefabs, and other byproducts. UNACEM was founded in 1916 and is based in Lima, Peru. In the 12 months ended March 2023, UNACEM reported revenue of PEN6.0 billion and an adjusted EBITDA margin of 25.8%.

Our Base-Case Scenario

Assumptions

- UNACEM's key markets in Latin America to have modest growth in 2023 and 2024: Peru's GDP to grow 2.0% and 2.8%, respectively; Ecuador's 2.5% in both years; and Chile's to contract 0.4% in 2023 and grow 2.6% in 2024. We also forecast the U.S. GDP to grow 0.9% in 2023 and 1.2% in 2024.
- We expect inflation to ease from 2022 in UNACEM's key markets, although still relatively high, keeping financing conditions tight in 2023. We assume consumer price index (CPI) levels in 2023 and 2024 of 5.8% and 3.0% in Peru, 4.2% and 2.4% in the U.S., 3.5% and 1.0% in Ecuador, and 7.9% and 4.1% in Chile, respectively.
- UNACEM's revenue to grow about 3.7% in 2023, mostly derived from higher prices across all segments and higher concrete volumes in Peru and the U.S., which would offset volume contraction in Peru. Moreover, income from the energy division will grow about 20%-30% due to the acquisition of Termochilca.
- UNACEM's profitability to remain near 28% in the next two years, improving close to 200 basis points from last year due to lower raw material, electricity, and fuel costs.
- Capex of about PEN630 million in the next 12 months, aimed toward the revamping and debottlenecking projects in its Ecuador facilities, the Puzzolana and Florence projects in Skanon, Solimana in Celepsa, and other strategic initiatives.
- Annual dividends of PEN290 million in 2023 and PEN200 million in 2024.
- Net debt remaining near PEN3.5 billion in the next two years.

Key metrics

UNACEM Corp. S.A.A.--Key Metrics*

Industry sector: Building materials & products

	--Fiscal year ended Dec. 31--						
	2019a	2020a	2021a	2022a	2023e	2024f	2025f
Adjusted ratios							
Debt/EBITDA (x)	3.4	4.4	2.3	2.2	2.1	1.8	1.7
FFO/debt (%)	19.2	13.4	33.9	33.6	32.4	41.5	41.1
DCF/debt (%)	5.9	8.2	15.2	4.5	7.6	11.5	6
EBITDA margin (%)	29.1	25.3	31.2	26.4	28.1	28.4	28.5
EBITDA interest coverage (x)	5.2	4.3	8.3	8.1	10.1	10.7	11.3

*All figures are adjusted by S&P Global Ratings, unless stated as reported. a--Actual. e--Estimate. f--Forecast.

Liquidity

We view UNACEM's liquidity as adequate, reflecting our expectations that sources of liquidity will exceed its uses by more than 1.2x in the next 12 months and that liquidity sources will exceed uses even if forecast EBITDA declines by 15% from our base case scenario. In addition, our liquidity analysis captures qualitative factors that reflect UNACEM's likely ability to absorb high-impact, low-probability events without refinancing, given its ability to reduce its capital spending and postpone dividend payments, if necessary. It also maintains sound relationships with banks, as seen in its access to financing from various creditors.

Principal liquidity sources:

- Cash and cash equivalents of PEN447 million as of March 31, 2023; and
- FFO of about PEN1.1 billion for the next 12 months.

Principal liquidity uses:

- Debt maturities of PEN919 million for the next 12 months, including recent rollovers carried out by the company.
- Working capital requirement of about PEN15 million for the next 12 months; and
- Maintenance capex of about $40 million (or PEN150 million-PEN160 million) for the next 12 months.

Covenants

As of the first quarter of 2023, UNACEM complied with all of its financial maintenance covenants at the consolidated and subsidiary levels.

On a consolidated basis, UNACEM must comply with the following covenants:

- A maximum debt-to-equity ratio of 1.5x.
- A minimum debt service coverage ratio of 1.20x.
- A maximum net debt-to-EBITDA ratio of 3.75x.

In addition, several subsidiaries must comply with similar ratios at their level.

We expect the company to maintain ample covenants headroom in the next 12 months, with headroom above 80% for its consolidated covenants.

Environmental, Social, And Governance

ESG credit indicators: E-3, S-2, G-2

Environmental factors are a moderately negative consideration in our credit rating analysis of UNACEM. Although environmental-related regulatory scrutiny is progressing slower in Peru and Latin America than in developed markets, we consider that the company's U.S. operations could be exposed to tighter regulations, potentially requiring greater investments in the medium term, although its assets are relatively new.

The bulk of UNACEM's operations are in Peru--accounting for 64% of sales--while 16% are in the U.S. and 19% in other Latin American countries. Therefore, we expect potential regulatory requirements to be relatively mild for UNACEM and its cash generation to provide sufficient cushion. On average, the company has deployed about PEN30 million annually for environmental investments; about 6% of its total capex. In 2022, it emitted 650 kg of carbon dioxide equivalent (CO_2e) per ton of cement produced, similar to those of regional peers. Moreover, the company has a commitment to decrease its CO_2e emissions per ton of cement produced to 500 kg by 2030 and to reach carbon neutrality by 2050.

Ratings Score Snapshot

Issuer Credit Rating	BB/Positive/--
Business risk:	Fair
Country risk	Moderately high
Industry risk	Intermediate
Competitive position	Fair
Financial risk:	Intermediate
Cash flow/leverage	Intermediate
Anchor	bb+
Modifiers:	

Issuer Credit Rating	**BB/Positive/--**
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Negative (-1 notch)
Stand-alone credit profile:	bb

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Peruvian Cement Group UNACEM Corp Outlook Revised To Positive On Continued Deleveraging; 'BB' Rating Affirmed, June 27, 2022
- Peruvian Cement Producer UNACEM Outlook Revised To Stable From Negative On Deleveraging; 'BB' Rating Affirmed, June 25, 2021

Ratings List

Ratings Affirmed	
UNACEM Corp. S.A.A.	
Issuer Credit Rating	BB/Positive/--

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such