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Research Update:

Ratings On Swedish Steelmaker SSAB Lowered To 'B+' On Weak Performance; Still On Watch Neg

Primary Credit Analyst:
Tommy J Trask, Dubai (971) 4-372-7151; tommy.trask@standardandpoors.com

Secondary Contact:
Gaetan Michel, Paris 33-1-4420-6726; gaetan.michel@standardandpoors.com

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Overview

- Weak conditions in the global steel industry have resulted in lower-than-expected earnings and credit metrics for SSAB.
- We consider that the company has a weak profitability record, prompting us to revise downward our assessment of its business risk.
- We are lowering our long-term ratings on SSAB to 'B+' from 'BB-', affirming the 'B' short-term rating, and keeping the ratings on CreditWatch negative.
- The CreditWatch reflects a possible further downgrade, unless market conditions and SSAB's earnings improve, such that it reduces adjusted debt to EBITDA to about 5x. Weakening in SSAB's current strong liquidity could also trigger a downgrade.

Rating Action

On Feb. 22, 2016, Standard & Poor's Ratings Services lowered its long-term corporate credit rating on Swedish steelmaker SSAB AB to 'B+' from 'BB-'. At the same time, we affirmed the 'B' short-term rating on the company. The ratings remain on CreditWatch with negative implications, where we placed them on Dec. 21, 2015.

At the same time, we lowered our issue ratings on SSAB's senior unsecured debt to 'B+' from 'BB-'. The issue ratings also remain on CreditWatch negative. The recovery rating on this debt is unchanged at '3', indicating our expectation of meaningful recovery in the lower half of the 50%-70% range in the event of a payment default.

Rationale

The downgrade follows SSAB's weaker-than-expected 2015 reported earnings. It also reflects a lowering of our expectations for SSAB's earnings in 2016 because Chinese, Russian, and Korean exports to Europe and the U.S. are dragging down European and U.S. steel prices and buyers have adopted a wait-and-see approach.

The prolonged downturn in the global steel markets has prevented SSAB from meeting the threshold for our 'BB-' rating of funds from operations (FFO) to debt of about 15% (compared with an actual figure of about 10.5% for 2015). We anticipate marginal improvement in 2016 compared with 2015, based on our view that synergies from the merger with Finnish steelmaker Rautaruukki Oyj

(Ruukki) and other cost efficiency measures should compensate for the impact of weaker market conditions. It remains to be seen how effective import tariffs are in protecting European and U.S. markets from the threat of cheap imports.

We continue to view favorably SSAB's 30% net debt-to-equity target, which is significantly lower than the current 52%. The company has generated positive discretionary cash flow over the past three years, accomplishing this in 2015 through positive working capital movements and not paying a dividend to shareholders. Shareholders have been supportive of lower dividend payments in times of weak cash generation.

SSAB operates in the highly cyclical steel industry, with end markets such as heavy transportation, construction, machinery, and mining. Volumes typically move in line with GDP over the long term, and can be volatile in the short term, as was evidenced in the last quarter of 2015.

SSAB's key strength is in its strong market position in special-grade steel products. For example, it has a global market share of about 40% in quenched and tempered steels, along with about 5% in some advanced high strength steels, and 20%-25% market share in heavy plates in the North and South America, according to company estimates. Following the merger with Ruukki, it also commands a 40%-50% share in the flat carbon steels and tubes market in the Nordic region.

In our opinion, key challenges for SSAB are the risk of new specialty grade steel capacity from competitors and the pace of take-up of special-grade steel products by equipment manufacturers.

In our base case for SSAB, we assume:
- A marginal year-on-year improvement in EBITDA to about Swedish krona (SEK) 3.7 billion-SEK4.0 billion, with unlocked synergies in line with the company's public guidance offsetting the negative impact of the weak market conditions.
- Capital expenditures (capex) of SEK1.5 billion-SEK2.0 billion per year in 2016 and 2017.
- No dividend payments in 2016 or 2017.

Based on these assumptions, we arrive at the following credit measures:
- FFO to debt of 10%-15%.
- Debt to EBITDA of 5x-6x.
- Positive discretionary cash flow.

Liquidity

We assess SSAB's liquidity as strong, based on our projection that the company's liquidity sources will cover its uses by 1.5x on a sustainable basis over the next 12 months?. Underpinning our assessment is the company's comfortable debt maturity profile, with an average term of 4.6 years. SSAB also has considerable undrawn committed long-term bank lines and no financial covenants in its loan agreements.

Principal liquidity sources:
- Cash and cash equivalents of SEK2.7 billion on Dec. 31,2015.
- Availability under long-term committed credit lines of SEK8.5 billion.
- Moderate working capital inflow in 2016.
- FFO of about SEK3.0 billion over the coming 12 months, by our estimate.

Principal liquidity uses:
- Short-term debt of about SEK6.4 billion, of which SEK3.6 billion is commercial paper.
- Capex of about SEK1.7 billion in 2016.
- Shareholders' demonstrated willingness to forego dividend payments when needed.

CreditWatch

The CreditWatch reflects the possibility of a further downgrade of SSAB in the coming three to six months, unless market conditions and SSAB's earnings improve, such that it reduces its Standard & Poor's-adjusted ratio of debt to EBITDA to about 5x. Weakening in SSAB's current strong liquidity could also trigger a downgrade.

We could consider affirming the ratings on SSAB if we see a sustained improvement in its operating margin and adjusted debt to EBITDA falls to about 5x.

We could lower our ratings on SSAB if adjusted debt to EBITDA remains at above 5x. This could occur if market conditions do not improve significantly, resulting in persistent stable or negative discretionary cash flow. Moreover, we could remove the one-notch uplift we currently factor into the ratings on SSAB if its currently strong liquidity weakened, potentially prompting a downgrade.

Ratings Score Snapshot

Corporate Credit Rating: B+/Watch Neg/B

Business risk: Weak
- Country risk: Very low
- Industry risk: Moderately high
- Competitive position: Weak

Financial risk: Highly leveraged
- Cash flow/Leverage: Highly leveraged

Anchor: b

Modifiers

- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Strong (+1 notch)
- Financial policy: Adequate (no impact)
- Management and governance: Satisfactory (no impact)
- Comparable ratings analysis: Neutral (no impact)

Recovery Analysis

Key analytical factors

- SSAB's senior unsecured debt has an issue rating of 'B+' and recovery rating of '3'. The recovery rating is underpinned by SSAB's substantial asset base, and minimal prior-ranking liabilities, offset by the unsecured nature of the debt and substantial debt at pari-passu level. Recovery is in the lower half of the 50%-70% range, and may come under downward pressure if SSAB incurs additional debt.
- In our hypothetical payment default scenario, we take into account our view of the cyclicality of the markets in which SSAB operates, and sustained weakness in steel demand that leads to a drop in volumes, utilization rates, and prices.
- We value SSAB as a going concern, given its strong position in the heavy plate market in North America, its dominant market position in special-grade steel products, and its highly competitive assets.

Simulated default assumptions

- Year of default: 2018
- EBITDA at emergence: SEK3.3 billion
- Implied enterprise value multiple: 5.0x
- Jurisdiction: Sweden

Simplified waterfall

- Net value available to creditors (after administrative costs): SEK15.4 million
- ---------------------------------
- Priority claims: SEK0.6 billion *
- Senior unsecured debt claims: SEK30.5 billion *
- --Recovery expectation: 50%-70% (lower half of the range)

*All debt amounts include six months of prepetition interest.

Related Criteria And Research

Related Criteria

- Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Revised Revolver Usage Assumptions For Recovery Analysis In Corporate

Ratings, Nov. 20, 2014
- Key Credit Factors For The Metals And Mining Downstream Industry, Dec. 20, 2013
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Group Rating Methodology, Nov. 19, 2013
- Methodology For Linking Short-Term And Long-Term Ratings For Corporate, Insurance, And Sovereign Issuers, May 7, 2013
- Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria Guidelines For Recovery Ratings On Global Industrials Issuers' Speculative-Grade Debt, Aug. 10, 2009

Ratings List

Downgraded; Ratings Affirmed; Remaining On CreditWatch

	To	From
SSAB AB		
Corporate Credit Rating	B+/Watch Neg/B	BB-/Watch Neg/B
Senior Unsecured	B+/Watch Neg	BB-/Watch Neg
Recovery Rating	3L	3L

Additional Contact:
Industrial Ratings Europe; Corporate_Admin_London@standardandpoors.com

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 criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following Standard & Poor's numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.