FitchRatings

RATING ACTION COMMENTARY

Fitch Downgrades Braskem's Ratings to 'BB+' On Increased ESG Risks; Places on Rating Watch Negative

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Fitch Ratings - São Paulo - 14 Dec 2023: Fitch Ratings has downgraded Braskem S.A.'s Local and Foreign Currency Issuer Default Ratings (IDRs) to 'BB+' from 'BBB-'. Fitch has also downgraded Braskem America Finance's senior unsecured long-term issue ratings to 'BB+' from 'BBB-' and Braskem Netherland Finance B.V.'s senior unsecured long-term issue rating and subordinated long-term issue rating to 'BB+' from 'BBB-' and to 'BB-' from 'BB', respectively. The ratings of Braskem S.A. as well as that of Braskem Netherlands Finance B.V. and Braskem America Finance Company have been placed on Rating Watch Negative.

The downgrade and Rating Watch Negative reflect the increase in environmental risks and new claims of BRL1 billion (USD200 million) associated with the possible collapse of a salt mine in the context of the geological event in Alagoas, which could worsen the company's cash flow profile. Fitch expects that FCF will be negative for a longer period than expected, while the company remains exposed to a prolonged downturn in the petrochemical sector, all of which resulted in material increase to net debt.

KEY RATING DRIVERS

Elevated Environmental Risks: Fitch has lowered several of the company's ESG Relevance Scores as a result of the mine incident, incorporating incremental environmental and social impacts that could potentially result in additional reparation costs and monetary fines. The geological event could be a catalyst of financial deterioration, increasing Braskem's liabilities, since the number of cases levied upon the company could build up.

In the past two weeks, the state government filed a BRL1 billion (USD200 million) lawsuit still to be judged and a fine of BRL72 million (USD14 million) from regulatory agencies was imposed. In addition, the municipality of Maceio announced the desire to review the BRL1.7 billion (USD340 million) deal settled in July, which still needs Braskem's consent, and a congressional inquiry has been installed in the senate, despite the fact that it does not have power to impose sanctions, but only recommend actions and remediations. Fitch believes these cases can negatively impact the company's FCF, beyond the previous forecast.

Operating Performance: Fitch's base case does not account for decrease in production in the near term as the salt mines have been decommissioned since 2019, and the company is in the process of stabilizing them through 2025. The caustic soda plant in the state is operating by acquiring feedstock from external producers and despite the geological event, no further backlash is anticipated to its core operations. Nevertheless, Fitch expects pressure on petrochemical spreads to continue into 2024 following challenging market conditions in 2023. The pent-up supply coming online, the excess production in Asia along with lower freight costs and concerns over demand due to a fragile global economy are more pronounced than anticipated and are now expected to spill over well into 2024.

Weakened Financial Flexibility: Fitch forecasts net leverage, excluding Braskem Idesa to be around 10.0x in 2023, declining to 5.5x in 2025, in comparison to 3.5x from our previous forecast. Fitch expects Braskem to remain committed to preserving its liquidity by maintaining its conservative dividend policy, particularly while leverage is above 2.5x. The company has the ability to reduce capex and fixed costs, optimize working capital and monetize tax credits if market conditions remain worse than anticipated in 2024.

Medium-Term FCF Negative: Fitch forecasts EBITDA to be USD800 million, USD750 million and USD1.4 billion in the next three years. Capex is estimated at USD725 million, USD400 million and USD650 million, respectively, in the same period, with no dividends in the next three years. Consequently, Fitch expects FCF to be negative in 2023, 2024 and 2025, at -BRL4.5 billion (-USD860 million), -BRL3.5 billion (-USD685 million) and -BRL 1 billion (-USD200 million), respectively, mostly due to disbursements related to the Alagoas settlements. FCF will turn positive in 2026 at BRL5 billion (USD1 billion) as resin prices recover and the disbursements reach an end.

ESG - Environmental and Social Impacts: Fitch understands that an increased exposure to environmental and ecological impacts due to the potential collapse of a salt mine in the context of the geological event in Alagoas could possibly pollute nearby landscapes, the lagoon and the soil. In addition to that, Fitch sees incremental exposure to social impacts from new claims and reparation costs to the victims and community living in neighboring areas on top of the 14,446 families relocated to other areas. This could have a negative impact on credit profile as it damages the company's reputation and could jeopardize FCF. Braskem has been committed to assisting people affected by the incident and has disbursed approximately BRL 10 billion (USD2 million) to date, in action fronts such as support for relocating and compensating, closing and monitoring the salt cavities, environmental and other technical matters, as well as social and urban measures.

DERIVATION SUMMARY

Braskem's leading position in the Americas in its core products, PE and PP, is a key credit strength, mitigating the commodity nature of its products, which are characterized by volatile raw material prices and price-driven competition. Braskem has medium scale compared with global chemical peers, such as Dow Chemical Company (BBB+/Stable), but it is well positioned relative to Latin American peers, such as Orbia Advance Corporation, S.A.B de C.V. (BBB/Stable) and Alpek, S.A.B. de C.V. (BBB-/Stable), in terms of scale, profitability and geographic diversification.

Around 43% of Braskem's EBITDA is generated outside Brazil, moving to around 50% in the medium term. Its thermoplastic resin operations in Brazil are integrated, which reduces cash flow volatility. The company's strong 60%-65% market share in Brazil is also a competitive advantage, as it allows Braskem to better withstand higher raw material prices and pass-through strategies.

Braskem's leverage, excluding Braskem Idesa, under Fitch's base case is expected to be around 8.0x in 2023. This is higher than its petrochemical peers, such as Orbia's at 2.3x, Alpek's at 1.4x and Dow's at 1.2x. All three Latin American players maintain strong cash positions, long-term debt-amortization profiles, and strong access to local and international debt markets.

KEY ASSUMPTIONS

--Brazil PE realized revenue/ton of USD1,420, USD1,385 and USD1,480 during 2023-2025;

--Brazil PP realized revenue/ton of USD1,040, USD1,120 and USD1,040 during 2023-2025;

--Brazil vinyls realized revenue/ton of USD1,530, USD1,430 and USD1,450 during 2023-2025;

--Brazil ethylene/propylene realized revenue/ton of USD1,030, USD1,200 and USD1,500 during 2023-2025;

--U.S. and Europe PP realized revenue/ton of USD1,790, USD1,915 and USD1,780 during 2023-2025;

--Mexico PE realized revenue/ton of USD1,160, USD1,130 and USD1,200 during 2023-2025;

--PE-ethane reference spreads of USD760/ton in 2023, USD750/ton in 2024 and USD 930 in 2025;

--PE-naphtha reference spreads of USD240/ton in 2023, USD210/ton in 2024 and USD300/ton in 2025;

--PP-propylene reference spreads of USD340/ton in 2023, USD325/ton in 2024 and USD370/ton in 2025;

--Capex according to management's guidance;

--No dividends to shareholders in 2023 and 2024.

RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

--Net debt/EBITDA below 2.5x on average through the cycle, excluding Braskem Idesa;

--Sustained consolidated net debt of less than USD5 billion.

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

--Additional contingent claims for the Alagoas incident;

--Net debt/EBITDA above 3.5x, on average through the cycle, excluding Braskem Idesa;

--Sustained negative FCF at the bottom of the cycle that results in incurring additional debt;

--Sustained EBITDA interest coverage below 1.0x;

--Material financial support to Braskem Idesa.

LIQUIDITY AND DEBT STRUCTURE

Adequate Liquidity: Braskem adopts a conservative and proactive financial strategy to limit the risks associated with exposure to the cyclical and capital-intensive nature of its business. The company has a strong cash position, with USD3.4 billion of readily available cash and marketable securities as of Sept. 30, 2023, excluding Braskem Idesa (USD287 million). Its gross debt excluding Braskem Idesa stands at USD8.4 billion, USD390 million of which was short-term debt as of 3Q23.

Braskem's strong cash position and its extended debt-amortization profile lead to manageable refinancing risks in the medium term. Over 2023 and 2024, the company faces debt amortization of BRL400 million (USD80 million) and BRL1.5 billion (USD300 million) per year. As of Sept. 30, 2023, about 87% of the company's total debt was denominated in U.S. dollars. Braskem has a track record of accessing both local and international debt markets. The company's financial flexibility is enhanced by a USD1 billion unused stand-by credit facility due in 2026.

ISSUER PROFILE

Braskem S.A. produces and sells chemicals, petrochemicals, fuels, steam, water, compressed air and industrial gases. The company has plants in Brazil, the U.S., Germany and Mexico that produce thermoplastic resins, such as polyethylene, polypropylene and polyvinyl chloride.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Braskem S.A. has an ESG Relevance Score of '5' for Waste & Hazardous Materials Management; Ecological Impacts due to the geological event in Alagoas that affected its salt mining operations, which has a negative impact on the credit profile, and is highly relevant to the rating, resulting in one notch downgrade.

Braskem S.A. has an ESG Relevance Score of '5' for Exposure to Environmental Impacts due to the potential collapse of a Salt Mine in the context of the geological event in Alagoas, which has a negative impact on the credit profile, and is highly relevant to the rating, resulting in one notch downgrade.

Braskem S.A. has an ESG Relevance Score of '5' for Exposure to Social Impacts due to the possibility of new relocation of local communities, which has a negative impact on the credit profile, and is highly relevant to the rating, resulting in one notch downgrade.

Braskem S.A. has an ESG Relevance Score of '4' for Governance Structure due to a past history of corruption scandals and shareholder's financial stress, which has a negative impact on the credit profile, and is relevant to the ratings in conjunction with other factors.

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit https://www.fitchratings.com/topics/esg/products#esg-relevance-scores.

RATING ACTIONS

ENTITY / DEBT	RATING		PRIOR
Braskem Netherlands Finance B.V.			
senior unsecured	LT	BB+ Rating Watch Negative Downgrade	BBB-
subordinated	LT	BB- Rating Watch Negative Downgrade	BB
Braskem America Finance Company			
senior unsecured	LT	BB+ Rating Watch Negative Downgrade	BBB-

Braskem S.A.	LT IDR	BB+ Rating Watch Negative Downgrade	BBB- Rating Outlook Negative
	LC LT IDR	BB+ Rating Watch Negative Downgrade	BBB- Rating Outlook Negative
	Natl LT	AAA(bra) Rating Watch Negative Rating Watch On	AAA(bra) Rating Outlook Stable
senior unsecured	Natl LT	AAA(bra) Rating Watch Negative Rating Watch On	AAA(bra)

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Corporate Hybrids Treatment and Notching Criteria (pub. 12 Nov 2020)

National Scale Rating Criteria (pub. 22 Dec 2020)

Corporate Rating Criteria (pub. 03 Nov 2023) (including rating assumption sensitivity)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Braskem America Finance Company	EU Endorsed, UK Endorsed

Braskem Netherlands Finance B.V.	EU Endorsed, UK Endorsed
Braskem S.A.	EU Endorsed, UK Endorsed

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