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DBRS Confirms Codelco at “A” with a Stable Trend

Industry: Natural Resources

DBRS has today confirmed the Issuer Rating and Senior Unsecured Debt of the Corporación Nacional del Cobre de Chile (Codelco or the Company) at “A” with a Stable trend. The rating confirmations and Stable trends reflect Codelco’s position as a world-leading and cost-competitive copper producer, with large reserve and resource bases. Codelco’s ratings also incorporate the support of the Republic of Chile.

Codelco is wholly owned by the Republic of Chile (rated AA (low) by DBRS), but its debt is not guaranteed by the Chilean government. In addition, as a state-owned entity, Codelco faces higher payments to the government than a normal, non-government company (about 85% of EBITDA for the past five years), making the Company reliant on the government or external debt to fund an ambitious capital expenditure program.

Codelco’s financial metrics have weakened but remain adequate for its current ratings, with good coverage metrics, although debt leverage and return measures are poor. Generally steady copper production and sales volumes, combined with sharply rising costs and, since 2011, declining copper and molybdenum prices, have shrunk Codelco’s earnings and operating cash flow in 2012 and in 2013. Combined with high capital expenditures and the acquisition of a 20% interest in Anglo American Sur S.A. (AA Sur), net debt has increased by \$3.9 billion since the end of 2011, despite special funding allowances by the Chilean government.

The Company’s business profile remains stable, although cost competitiveness has weakened. Codelco’s 2013 five-year plan included approximately \$27 billion of investment to refurbish and extend operations, as well as to increase copper production to about 2.0 million tonnes by 2017 (2012 production was 1.8 million tonnes). The need for additional funding is expected as a result of continued cost pressures and volatile but weaker copper prices in the near to medium term.

Codelco’s earnings before non-recurring items recovered strongly from the 2008-2009 recession, as average annual copper prices rose from \$2.34 per pound in 2009 to \$4.00 per pound in 2011. The upswing masked a rapid rise in the Company’s unit cost of copper production. With prices trending downward in 2012 and to date in 2013, and despite more stable costs in 2013, margins and earnings have contracted.



Codelco's business model, in which it returns its net income to the state except for depreciation, amortization and deferred taxes, requires special consideration in times when the Company is seeking to expand operations. It also results in relatively high debt leverage, as equity financing is unavailable and dividend payouts tend to be high, reducing its equity base. 2012 and 2013 represent such periods and, despite special funding considerations, Codelco's debt has risen and its financial metrics have weakened.

Codelco earnings in the near term are expected to continue to deteriorate in the face of lower copper prices and stabilized costs, partially offset by income from AA Sur and higher output at Ministro Hales. Cost savings programs implemented in 2013 are expected to stabilize unit costs, but a recovery of molybdenum prices will be required to materially reverse the trend towards growing unit cash costs. Accordingly, Codelco's near-term credit metrics are expected to weaken further as a result of lower operating cash flow, due to lower copper prices and the need to fund a heavy capex programs.

DBRS therefore expects Codelco's debt levels will increase further, despite the Chilean government's continued provision of additional financial support for the Company's expenditure plans and its funding needs.

Notes:

All figures are in U.S. dollars unless otherwise noted.

This rating is endorsed by DBRS Ratings Limited for use in the European Union.

The related regulatory disclosures pursuant to the National Instrument 25-101 Designated Rating Organizations are hereby incorporated by reference and can be found by clicking on the link to the right under Related Research or by contacting us at info@dbrs.com.

The applicable methodology is Rating Companies in the Mining Industry, which can be found on our website under Methodologies.

Issuer	Debt Rated	Rating Action	Rating	Trend	Latest Event
Corporación Nacional del Cobre de Chile	Issuer Rating	Confirmed	A	Stb	Jan 20, 2014
Corporación Nacional del Cobre de Chile	Senior Unsecured Debt	Confirmed	A	Stb	Jan 20, 2014

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Ernie Lalonde, P. Eng., CFA
Senior Vice President - Mining
+1 416 597 7562
elalonde@dbrs.com

Eric Eng, MBA
Vice President - Corporate Research & Analysis
+1 416 597 7578
eeng@dbrs.com

Peter Schroeder
Group Managing Director - Global Corporate
+1 416 597 7579
pschroeder@dbrs.com

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