MOODY'S

HD **Moody's upgrades Fortescue to Ba1; Outlook stable**

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Approximately USD11 **billion** of debt securities affected

Moody's Investors Service has today upgraded Fortescue Metals Group Limited's corporate family rating (CFR) to Ba1 from Ba2. At the same time Moody's has upgraded FMG Resources (August 2006) Pty Ltd's senior unsecured notes ratings to Ba2 from Ba3. The senior secured rating of Baa3 is not affected by today's rating action and is affirmed. The outlook on all ratings is stable.

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The upgrade follows today's announcement that Fortescue has issued two voluntary redemption notices in relation to the outstanding notes of USD1.04 **billion** due 2015 and USD600 **million** due 2016.

RATINGS RATIONALE

"The one-notch upgrade in the CFR to Ba1 reflects our expectation for continued strengthening in Fortescue's credit profile following the progress made on the **company**'s debt reduction strategy and the near completion of its substantial expansion program", says Matthew Moore -- a Moody's Vice President and Senior Analyst. "The announced notes redemption and reduction in finance leases - following the decision to assume ownership of Christmas Creek **ore** processing facility - further demonstrates the **company**'s commitment to its debt reduction strategy, which we previously highlighted as a factor that would **lead** to improvements in the **company**'s ratings", Moore adds.

Fortescue has reduced its adjusted debt by around USD3.1 **billion** through voluntary debt reduction initiatives and we expect debt to reduce further as the **company** continues to work its gearing down to its targeted level of around 40%. The **company** has announced that its debt reduction initiatives, combined with the re-pricing of its term loan facilities, will reduce its annual interest expense by around USD300 **million**.

"The upgrade also reflects Fortescue's continued progress on its expansion activities, which are nearing completion and will **lead** to further improvements in production and cash flow generation supporting financial metrics in line with the Ba1 rating", adds Moore. Under our base case assumptions of **iron ore** prices of around USD110 to USD120 (based on 62% Fe) for the second half of the fiscal year ending 30 June 2014, we now expect Fortescue's debt-to-EBITDA to improve to close to 2.0x.

"The stable outlook reflects our expectation that Fortescue will continue to generate solid cash flow and achieve its production targets following the completion of the current expansion activities", says Moore.

The announced notes redemption is a further step in Fortescue's announced intention to reduce its debt levels and improve its gearing levels towards its desired level of 40%. As of FY13, Fortescue's debt-to-capital was around 68%, and under our base case we expect the ratio to decline to 50% to 55% in FY14.

Fortescue is nearing completion of its massive expansion plans, which has led to a step change in the **company**'s production profile and revenue generation ability. Upon completion, production will increase to around 155mtpa, almost triple the levels achieved in FY12. This drives substantial improvements in the cash flow generation ability and unit costs of production for the **company**. We expect full year production for FY14 to be around 125mt, resulting from the completion and ramp up of the Firetail mine at the Solomon Hub in the June 2013 quarter and the expected completion of the Kings mine in early calendar 2014.

The notes redemption significantly improves Fortescue's near term maturity profile, with the **company**'s first major maturity now in FY17 when USD1billion of senior unsecured notes comes due.

The affirmation of the Baa3 rating on the senior secured term loan facility reflects the reduction of debt in the capital structure ranking below the senior secured.

The ratings are not expected to be upgraded in the near term, however, the ratings could face positive pressure if Fortescue demonstrates a track record of 1) consistently producing at the full expanded 155mtpa capacity and 2) maintaining a conservative financial profile such that Debt-to-EBITDA is maintained below 2.0x through the cycle. In addition, a critical issue for a rating upgrade will be the **company**'s growth intentions post completion of the current phase of expansion. Achieving a more geographically diversified customer base would also be supportive of a rating upgrade.

The outlook or rating could face negative pressure if the **company** experiences any unexpected execution challenges with the remaining expansion activities, is unable to sustain production levels near the 155mtpa target, embarks on any material further expansions, and/or adapts more aggressive shareholder-friendly initiatives, such that credit metrics do not remain in line with Moody's expectations. **Iron ore** prices sustained materially below our base case assumptions could also **lead** to negative pressure on the rating or outlook. Financial metrics that Moody's would consider for a downgrade include Debt-to-EBITDA exceeding 2.5x and FFO-to-Interest falling below 4.0x on a consistent basis

The principal methodology used in this rating was the Global **Mining** Industry published in May 2009. Please see the Credit Policy page on www.moodys.com for a copy of this methodology.

Fortescue Metals Group Limited based in Perth, is an **iron ore** producer engaged in the exploration and **mining** of **iron ore** for export, mainly to **China**. Fortescue is Australia's third largest **iron ore** producer and exporter as well as one of the world's largest producers and sea-borne traders. Fortescue has around 15.6 **billion** tonnes of **iron ore** Resources, including 2.2 **billion** tonnes of reserves, and its tenement holdings span an area of over 85,000 square km in the Pilbara region of Western Australia. For the September 2013 quarter, Fortescue achieved and annual run rate of around 104mtpa of production. Moody's expects full year shipments for FY2014 to be around 125mt.

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