MOODY'S INVESTORS SERVICE

Credit Opinion: Ineos Group Holdings plc

Global Credit Research - 02 Sep 2010

Southampton, United Kingdom

Ratings

Category	Moody's Rating
Outlook	Positive
Corporate Family Rating	Caa1
Bkd Senior Secured	Caa3/LGD5
Ineos Holdings Limited	
Outlook	Positive
Sr Sec Bank Credit Facility	B2/LGD3/Caa2/LGD5
Ineos Finance plc	
Outlook	Positive
Bkd Senior Secured	B2/LGD3

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Key Indicators

Ineos Group Holdings plc

	2007	2008	2009
FCF/Debt	8.6%	0.1%	3.1%
RCF/Net Debt	17.3%	-0.3%	6.3%
EBITA/Avg.Assets (Exc. Cash)	12.4%	0.1%	2.6%
Debt /EBITDA	4.3	10.8	9.4
EBITDA/Interest Expense	2.7	1.1	1.2
EBITDA Margin %	7.8%	2.8%	5.2%

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Corporate Profile

Ineos group was established in 1998 through a management buy-out of the former BP petrochemicals asset in Antwerp, which was led by Mr Ratcliffe, Chairman of Ineos Group Holdings. The group has subsequently grown through acquisitions and at the end of 2005 acquired Innovene Inc., a 100% subsidiary of BP, in a USD 9 billion buy-out, transforming Ineos into one of the world's largest chemical companies (measured by turnover) with aggregate chemical production capacity of 23.800 kte per annum and refining capacity of over 410,000 barrels a day.

Ineos facilities include two large-scale refineries in Grangemouth (Scotland) and Lavera (France). It operates more than 37 sites in 9 countries, while eight large-scale petrochemical sites account for c.69% of the petrochemical production volumes, of which seven are integrated. The group derives c.37% of its EBITDA from commodity polymers, c.19% from refining and c.44% from intermediate chemicals. In 2009, Ineos reported revenues of EUR 18.1 billion.

Recent Developments

In July 2010, Ineos reported semi-annual results that reflected its strong operating performance supported by record profitability in several key intermediate products and strong performance in O&P, both in the US and Europe, while conditions in the refining segment remained weak.

The Chemical Intermediates segment posted record capacity utilisation and profitability generally driven by volumes on the back of recovery in demand, supported by attractive export opportunities, and tight global supply (particularly in Nitrites and Phenol). The segment represented 58% of H1 EBITDA.

O&P North America continued to benefit from advantageous ethane-based cracker margins, that together with tighter supply conditions on the back of several closures, supported strong profitability in 1H 2010. By the same token, O&P Europe benefited from a recovery in demand, especially from the automotive industry, and high margins (including in 2Q when ethylene prices started to decline). Shortages of product, as well as the strong demand from China, and the slow start in the Middle East, all contributed to very strong results. We note that additional capacity from the Middle East and Asia and/or a pronounced decline in export demand present a downside profitability risk for European O&P in the near term.

The refining business remained relatively weak and has not yet materially improved from the low levels of 2009.The industry continues to suffer from overcapacity as players in the sector have been slow in reducing their production while we have seen only modest improvement in demand since 2008/2009.

Moody's maintain a positive outlook on the ratings as we await a sustained improvement in the credit profile. In particular, we note that some signs of recovery in the refining business would offer support to the financial profile into 2011.

Rating Rationale

Moody's recognizes the large size and high degree of upstream integration of the business, while the current Caa1 corporate family rating largely reflects the group's substantial absolute amount of debt, raised at the time of the Innovene acquisition in 2005, and a high level of debt service payments relative to the cash flow generation. We continue to closely monitor continued and sustained improvements in the group's operating performance, reported in the last several quarters, and maintain a positive outlook on the ratings. The Caa1 ratings also take into account the lagging operating performance of the refining division and Ineos' high leverage reflected at the end of 2009 with Debt/EBITDA at 9.4x times and (FFO + Interest) / Interest at below 2.0x times. Looking ahead, the credit assessment will be largely driven by the pace and scope of deleveraging that is expected to be underpinned by the sustained strength in the intermediates, solid performance in O&P, as well as some improvements in refining margins.

The key rating factors influencing Moody's assessment are:

1. Business Profile - the strong position of Ineos in its peer-group is underpinned by the relatively broad diversity of its operations that comprise refining, O&P and production of a variety of chemical intermediates as well as its established presence in a large number of markets. Moody's notes that Ineos' facilities are generally well positioned and are not expected to be significantly affected by potential capacity rationalization anticipated at the trough of the current cycle. Operations include refining crude oil and the cracking and production of olefin, polymer and specialty materials. Prior to the cyclical downturn, commodity chemicals and refining delivered c.54% of its EBITDA, contributing to relative volatility in cash flow generation while the group is also exposed to raw material price movements. Ineos' reports leading global positions including: #1 in Phenol, Nitriles and Ethylene oxide; #3 in Polyethylene and Polypropylene.

2. Size and Stability - Ineos is a strong positive outlier in its current rating category with regard to revenues and the diversity of it divisions of equal size. The assessment, however, also recognizes the relatively high cyclicality of the polyolefins business (compared to other chemical products covered by the same rating methodology), as well as the large contribution of refining. While Moody's recognizes that some of the key products of the company (refining, polyolefins, phenol, olygomers) follow different cycles, the company also remains exposed to the economic fluctuations which translate into an EBITDA featuring a relatively high degree of volatility.

3. Cost Position - prior to the current downturn, Ineos implemented a programme of cost cutting measures across its chemicals and refining portfolio and managed to achieve further fixed cost reduction in 2009 that safeguarded the liquidity position of the group during the recent adjustment in pricing levels and inventory. Ineos' strategy remains focused on managing the fixed-cost element to position the company to withstand trough conditions. Ineos estimates that the majority of its chemicals facilities enjoy cost positions in 1st and 2d quartiles, particularly in Phenol, Vinyls, ACN, Alpha Olefins, as well as strong positions in polyolefins. This competitive cost position allowed the company to benefit from strong export markets that supported improvements in the utilisation rates since the end of 2009. In the medium term, refining margins are expected to remain under pressure, affected by weaker demand levels for middle distillates and some uncertainty regarding the scope of adjustment in the European refining capacity. In polyolefins additional capacity from the Middle East and Asia and/or a pronounced decline in export demand present a downside risk in the second half of 2010/2011, while we maintain positive outlook on intermediates. Overall, we expect Ineos to outperform European peers during the recovery in the cycle.

4. Ineos Management Strategy and 5. Financial Strength - the absolute size of the liabilities and the substantial cash debt service obligations remain one of the main factors underpinning current financial assessment.

We recognise that the performance of the group has stabilised in 2009 and 1H 2010 and the rating outlook is positioned towards an expectation of an improvement in the credit profile in 2010. We also note that Ineos will need to maintain the recent trend of improved cash flow generation to maintain financial flexibility under more stringent financing covenants in 2011. As we expect some slowdown in the polyolefins area, following the exceptionally strong results of 1H 2010, we believe that some recovery in the refining operations is required to maintain the improved credit profile in the near term.

Ineos took steps to reduce refinancing pressure in the medium term. The recent refinancing of part of the senior secured facilities offered additional support to the liquidity position of the group through the extension of the maturities of the working capital and securitisation facilities allowing additional financial flexibility, including increased headroom under its financial covenants pending the anticipated recovery in 2011/2012. The transaction has also extended the company's refinancing schedule from 2012/2013 to 2013/2014, when Ineos expects to benefit from stronger chemicals cycle conditions.

Liquidity Position

Ineos liquidity position remains satisfactory and is supported by improved cash and working capital management, as well as by recent disposals (the latest one being the Global Films business for EUR 100 m). At the end of June 2010, the company reported EUR 677 m in cash balances and further EUR 30 m in availability under its RCF and EUR 400 m under its securitisation facility.

We expect that the recent disposals and strong performance will likely trigger some prepayment of the facilities through the cash sweep mechanism in 2011 (such prepayments would offset EUR 500 m prepayment requirement agreed with the senior lenders by 2012).

Rating Outlook

The positive outlook reflects the improved operational trends in the industry that benefits both from the broad restocking, as well as improved demand, particularly in the emerging markets. The strong performance in 1H 2010 underpinned the trend for stabilisation in the credit profile, that should be further supported through some debt reduction, and improved flexibility under the financial covenants in 2010/2011.

What Could Change the Rating - Up

A sustained improvement in cash flow generation with (FFO + Interest) / Interest sustained above 2.5x and Debt/ EBITDA trending towards 5.0x times would put a positive pressure on the ratings.

What Could Change the Rating - Down

A deterioration in operating performance leading to a sustained weakness in cash flow generation leading to (FFO + Interest)/ Interest at or below 2.0x and/or a sustained negative FCF generation would put a negative pressure on the ratings.

Rating Factors

Ineos Group Holdings plc

Chemical Industry	Aaa	Aa	A	Baa	Ba	B	Caa
Factor 1: Business Profile							
a) Business Position Assessment				X			
Factor 2: Size & Stability							
a) Revenue (Billions of US$)		$ 23.5					
b) # of Divisions of Equal Size				4			
c) Stability of EBITDA							47%
Factor 3: Cost Position							
a) EBITDA Margin (4 Yr. Avg.)						5%	
b) ROA - EBIT / Assets (4 Yr. Avg.)						3%	
Factor 4: Management Quality							
a) Debt / Capital							100%
b) Debt / EBITDA (4 Yr. Avg.)							6.9
Factor 5: Financial Strength							
a) EBITDA / Total Interest Expense (4 Yr. Avg.)						1.7	
b) Retained Cash Flow / Debt (4 Yr. Avg.)						7%	
c) Free Cash Flow / Debt (4 Yr. Avg.)					4%		
Rating:							
a) Indicated Rating from Grid					Ba		
b) Actual Rating Assigned							Caa1