

### Research Update:

## ArcelorMittal Downgraded To 'BBB-' On Weak Credit Metrics; Outlook Stable

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## Research Update:

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## Overview

- The recovery in the steel sector appears to have stalled, in our view, and the prospects for further improvements in the credit metrics of Luxembourg-registered steel group ArcelorMittal are less likely.
- We are lowering our long-term corporate credit ratings on ArcelorMittal and subsidiaries to 'BBB-' from 'BBB'.
- We are affirming our short-term ratings on ArcelorMittal at 'A-3'.
- The stable outlook reflects our opinion that ArcelorMittal's financial risk profile will not deteriorate further as steel markets have stabilized.

## Rating Action

On Nov. 2, 2010, Standard & Poor's Ratings Services lowered to 'BBB-' from 'BBB' its long-term corporate credit and issue ratings on Luxembourg-registered steel group ArcelorMittal and its guaranteed subsidiaries. At the same time, we affirmed the short-term ratings on ArcelorMittal at 'A-3'. The outlook is stable.

In addition, we withdrew the ratings on subsidiaries Dofacso Inc. and Ispat Inland L.P., at the parent company's request.

## Rationale

The downgrade reflects our opinion that the prospects for further improvement in ArcelorMittal's operating results and credit metrics are more uncertain, and in our view, do not appear likely to reach a sustainable level commensurate with the 'BBB' rating.

The recovery that had been evident in steel markets in recent quarters appears to us to have stalled, and, together with intense margin pressures from higher-cost raw materials, in our view steel makers are facing a squeeze in margins and only a muted outlook for growth in 2011.

In the nine months to Sept. 30, 2010, ArcelorMittal reported much-improved profitability year on year, with adjusted EBITDA of \$7.2 billion, compared with \$3.2 billion a year earlier. However, management's guidance of EBITDA of \$1.5 billion-\$1.9 billion for the fourth quarter to Dec. 31, 2010, implies 2010 EBITDA of about \$8.7 billion-\$9.1 billion.

In the nine months to Sept. 30, 2010, funds from operations (FFO) was also

stronger year on year, at \$5.7 billion, but cash flow was fully invested in working capital of \$5.1 billion and capital expenditures (capex) of \$2.0 billion. This led to negative free operating cash flow (FOCF) of \$1.5 billion in the nine-month period, compared with positive FOCF of \$2.6 billion in the same period in 2009.

We estimate that adjusted debt remained substantial at \$35.3 billion on Sept. 30, 2010, which was \$3.2 billion higher than at year-end Dec. 31, 2009. Our adjusted debt figure includes significant adjustments of \$7.6 billion of pension and other postretirement obligations, as well as for trade receivables sold, and \$1.0 billion for nonsurplus cash.

The ratio of the last-12-months' FFO to adjusted debt remained weak for the ratings, at 20%, as did the ratio of adjusted debt to the last-12-months' adjusted EBITDA of 3.8x on Sept. 30, 2010.

In our credit scenario, we factor in only muted growth in steel volumes and prices, and we expect ongoing margin pressures from expensive raw materials. We also assume quite significant capex of \$4 billion-\$5 billion annually, as the group invests in developing its assets, notably in mining. We also factor in stable dividends of about \$1.3 billion and ongoing modest bolt-on acquisitions.

We do not factor in a potential spin-off of the group's stainless steel operations, which is under consideration, but do not consider this likely to be material to credit quality.

On this basis, we envisage broadly flat credit metrics in 2011 and 2012, with ratios of FFO to adjusted debt of 20%-25% and adjusted debt to EBITDA of about 3.5x-4.0x, which we consider to be commensurate with the 'BBB-' ratings.

The ratings on ArcelorMittal reflect our view of the group's satisfactory business risk profile and intermediate financial risk profile. Supportive factors include the group's leading global market positions, partial supply of own raw materials, and good supply discipline. Constraining factors include industry cyclicalities; volatile input costs, profitability, and cash flow; and substantial adjusted debt.

## **Liquidity**

We view ArcelorMittal's liquidity as adequate, as we envisage that liquidity sources will more than cover liquidity uses over the next year. We also regard ArcelorMittal as having a track record of regular new bond issuance to lengthen debt maturities, sound relationships with banks, and good standing in credit markets.

Liquidity sources over the next year include:

- Retained cash of \$3.5 billion as of Sept. 30, 2010, of which we view \$1.0 billion as tied to operations.
- Substantial \$11.4 billion availability under medium-term committed bank

facilities.

- Adequate financial covenant headroom and improved FFO.

This compares with the following liquidity uses over the next year:

- Short-term debt of \$5.4 billion as of Sept. 30, 2010, and a debt maturity profile that we regard as manageable.
- Annual capex of \$4 billion-\$5 billion and stable annual dividend payments of about \$1.3 billion.
- Possible modest working capital needs.

### **Recovery analysis**

ArcelorMittal makes active use of the bank loan and bond markets as sources of finance. Reported gross debt of \$22.8 billion on June 30, 2010 (which is the last date on which details are available), primarily comprised \$13.0 billion of bonds, \$6.4 billion of bank loans, and \$3.0 billion of other loans. Short-term debt included \$1.8 billion of commercial paper outstanding as of June 30, 2010. The main undrawn bank facilities are a €5.0 billion revolving credit facility (RCF), which expires in 2012, and a \$4 billion RCF, which expires in 2013.

All rated debt issued by ArcelorMittal and its subsidiaries is rated 'BBB-', the same as the corporate credit rating. By far the main borrower is the parent company ArcelorMittal, which significantly mitigates the risks of structural subordination. Priority liabilities, including subsidiary debt, trade payables, and other liabilities are moderate in our view, and are mitigated by the group's size and diversification.

## **Outlook**

The stable outlook reflects our opinion that ArcelorMittal's financial risk profile will not deteriorate further, as steel markets have stabilized. We consider ratios of FFO to adjusted debt of 20%-25% and adjusted debt to EBITDA of about 3.5x-4.0x in 2011 and 2012, as being commensurate with the ratings. Furthermore, downside risks are, in our view, mitigated by ArcelorMittal's business risk profile and liquidity, which help to underpin the ratings.

Upside rating potential is constrained by the muted industry outlook and by substantial adjusted debt, but could develop over the medium term if the group was able to demonstrate sustainably higher margins, positive FOCF, and lower debt.

Downward pressure on the ratings could occur if there were a further decline in the steel sector, without sufficient corrective actions from ArcelorMittal to mitigate the effect on its credit ratios, or if the group were to post persistently negative FOCF or undertake large debt-financed acquisitions.

## Related Criteria And Research

- Key Credit Factors: Methodology And Assumptions On Risks In The Metals Industry, June 22, 2009
- Criteria Methodology: Business Risk/Financial Risk Matrix Expanded, May 27, 2009
- Principles Of Corporate And Government Ratings, June 26, 2007

## Ratings List

Downgraded; CreditWatch/Outlook Action; Ratings Affirmed

	To	From
ArcelorMittal		
Corporate Credit Rating	BBB-/Stable/A-3	BBB/Negative/A-3
Senior Unsecured Debt	BBB-	BBB
Senior Secured Debt	BBB-	BBB
Commercial Paper	A-3	A-3

ArcelorMittal Finance		
Corporate Credit Rating	BBB-/Stable/--	BBB/Negative/--
Senior Unsecured Debt	BBB-	BBB

Mittal Steel USA Inc.		
Corporate Credit Rating	BBB-/Stable/--	BBB/Negative/--
Senior Unsecured Debt(1)	BBB-	BBB
Senior Secured Debt(1)	BBB-	BBB

Mittal Steel Europe S.A.		
Senior Secured Debt(1)	BBB-	BBB

Ispat Inland ULC		
Senior Secured Debt(2)	BBB-	BBB

Not Rated Action; CreditWatch/Outlook Action

	To	From
Dofasco Inc.		
Ispat Inland L.P.		
Corporate Credit Rating	NR/--	BBB/Negative/--
Dofasco Inc.		
Senior Unsecured Debt	NR	BBB

(1) Guaranteed by ArcelorMittal.

(2) Guaranteed by ArcelorMittal and Mittal Steel USA Inc.

NB: This list does not cover all ratings affected.

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Complete ratings information is available to RatingsDirect subscribers on the Global Credit Portal at [www.globalcreditportal.com](http://www.globalcreditportal.com) and RatingsDirect subscribers at [www.ratingsdirect.com](http://www.ratingsdirect.com). All ratings affected by this rating action can be found on Standard & Poor's public Web site at [www.standardandpoors.com](http://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) 495-783-4011.

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