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# San Martin aims for USD 100m market-testing bond debut - Deal Preview

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PROPRIETARY
**Latin America**

Mining
Peru

**Issuer**
LatAm Primary New Issuance

**Issuer**
San Martin Contratistas Generales S.A.

The small size of San Martin Contratistas Generales's (B+/B) planned USD 100m bond will be the main challenge as the Peruvian construction and mining services provider looks to make its market debut, a bond investor and two bankers following the transaction said. Weighed against the borrower's strong client profile, its near-single-market exposure during a difficult political period is also a consideration, the investor said.

San Martin is aiming for a USD 100m five-year non-call three-year senior unsecured issuance of up to USD 100m and has been holding investor calls since 26 July, as reported. BCP Securities and Santander are managing.

The size will likely mean a high yield, the bankers said. "I'd say they pay in the high single-digits or low double-digits, the first banker said. "It depends if they get local demand. International buyers would want at least double-digits."

The engineering and construction sector could also be a challenge with investors, the two bankers noted, and the expected size of the deal is reminiscent of Paraguayan meat company Frigorifico Concepcion (B+/B). Concepcion debuted with a USD 100m 10.25% 2025 bond in January 2020, to which it later added in retaps and is in the process of refinancing.

"USD 100m is illiquid and like any small deal, they will have to pay up," the second banker said, noting a yield could be as much as 10%.

The borrower is seeking to diversify its funding sources and extend the average life of its debt, and plans to use proceeds to refinance about USD 47m in existing debt, cancel about USD 20m of operating leases, and spend the remainder on general corporate purposes including capex, as reported.

"If they had 100m outstanding and they are cleaning up their capital structure that would be one thing, but here use of proceeds is partially for capex and part for contingencies," the first banker said.

San Martin did not respond to requests for comment.

Incorporated in 1990 from the merger of Transportes Caravana and Considex – two companies involved in the transport of minerals and the leasing of machinery – San Martin specializes in construction and large earth movement services for mining projects, according to information on its website. It counts more than 12 active mining services contracts, mostly in Peru, but also in Colombia and Spain.

Clients include miners Minas Buenaventura, Minsur and subsidiaries of Glencore, as well as cement companies Pacasmayo, Unacem and Cementos Argos, according to the website.

San Martin was contracted for nine of the 13 active open-pit mining projects in Peru in 2019, according to a source close to the matter. It is controlled by the Siucho family, who has more than 40 years of experience in mining operation services. The CEO is Alfonso Brazzini Visconti.

The company posted about USD 233m in revenues in the 12 months ended 31 March, with 81% coming from mining services and the 19% from construction projects for mining and non-mining clients, with a focus on the private sector, according to S&P. Revenue from ordinary activities was USD 214m in 2020 and USD 33m in EBITDA, with 15.5% EBITDA margin, according to the source close to the mater. San Martin reached USD 76m in revenue in 1Q21 and USD 14m in EBITDA with 18.8% margin.

Low diversification raises exposure concerns

Peru's mining segment includes both domestic and international operators, in contrast to an industry such as cement, Fitch wrote in a rating report. As most of the foreign miners have strong credit profiles, a small service company like San Martin faces a structural disadvantage when negotiating contracts.

San Martin's 2020 operating and financial performance was severely affected by the COVID-19 pandemic and strict lockdown measures in Peru, postponing about USD 68.8m in revenues, S&P wrote. This was reflected in a large contraction in revenues, a spike in adjusted gross leverage to 5.1x, and tight liquidity at year-end 2020. S&P expects San Martin's gross adjusted leverage ratio to be about 3.0x by the end of 2021 and slightly below that level afterwards.

The company pushed back several contracts, growing the backlog to USD 1.2bn as of 1Q21, from approximately USD 300m in December 2018, according to the source close to the matter. This represented more than five years of backlog. Mining services represented 90% of the backlog, the source said, most importantly the contract with China's Shougang, for up to 50 years.

The high exposure of contracts to Peru and too few large clients is something of a concern, the investor said. "The portfolio balance could easily be erased in Peru, especially looking at the political situation that can offset even the big mining players in the country and San Martin seems to put all its bets on them," the investor said.

About 75% of revenue comes from five customers, S&P wrote, and San Martin is exposed to economic and mining industry cycles, making sales and cash flows highly volatile. Some 95% of revenues are from Peru, and 80% from the mining sector, the agency said, with little sign of diversification in the next two years.

Challenging political backdrop

A high coupon on San Martin's debut bond would pressure already tight liquidity. The company reported USD 77m in net debt at the end of 1Q21, according to the source close, and USD 138m pro forma. Net debt to EBITDA was 2.1x at 2Q21, and 2.9x pro forma.

San Martin had capitalization of USD 133m and USD 7m in cash and cash-equivalents as of 1Q21, and will have USD 30m cash pro-forma.

All three of the sources pointed to a difficult backdrop in Peru. The election of leftist Pedro Castillo has pressured corporate and sovereign bonds for months. Despite Castillo's lack of congressional allies, there are particular concerns for what his desired policies could mean for the mining industry. There was additional panic last week, on concern that the market's choice for economy minister, Pedro Francke might not take the job, though his appointment was later announced.

"To some extent this is bet on Peru with President Castillo, whose rhetoric has had a tougher play on the mining sector and promised to increase royalties upon election," the first banker said. "He has been bland and diplomatic in his rhetoric and is much better right now, but there is a risk. The provinces that elected him and supported him have come from strong mining regions of the country and they want mining companies to pay more, so the backdrop is not good. This is a country in a transition and in the middle of a political shift. Things could turn out to be fine, but it could also go badly."

by Ero Partsakoulaki and Mariana Santibanez