STANDARD & POOR'S

Recovery Report

Rockwood Specialties Group Inc. 's Recovery Rating Profile

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Standard & Poor's Ratings Services today assigned a recovery rating of '4' and raised its issue rating on Rockwood Specialties Group Inc.'s following senior subordinated notes:

- Eur375 million 7.625% senior subordinated notes due Nov. 15, 2014; and
- US$200 million 7.5% senior subordinated notes due Nov. 15, 2014.

We raised the issue rating to 'BB-' (the same as the corporate credit rating) from 'B'. The recovery ratings indicate our expectation of average (30% to 50%) recovery in the event of a payment default.

The issue rating on Rockwood's senior secured bank facility remains unchanged at 'BB+' (two notches above the corporate credit rating) along with an unchanged recovery rating of '1', indicating our expectation of very high recovery (90% to 100%) in the event of a payment default.

Rockwood Specialties Group Inc.—Credit Profile					
Corporate credit rating	BB-/Stable/—				
Estimated gross enterprise value at default	$2.6 bil.				
Year of default	2010				
Facility/Issue*	***Estimated principal at default (US$ mil.)***	***Issue rating***	***Recovery rating***	***Recovery***	***Maturity***
Secured Debt					
$250 million senior secured revolving credit facility	$250	BB+	1	90%-100%	2010
$250 million senior secured term loan A	$124	BB+	1	90%-100%	2011
$1.139 billion senior secured term loan E	$1,093	BB+	1	90%-100%	2012
EUR269.3 million senior secured term loan G**	$374	BB+	1	90%-100%	2012
Unsecured Debt					
US$200 million 7.5% senior subordinated notes	$200	BB-	4	30%-50%	2014
Eur375 mil 7.625% senior subordinated notes**	$535	BB-	4	30%-50%	2014

*Rockwood Specialties Group Inc. is the borrower on all debt, except for term loan tranche A-2 and certain revolving credit borrowings where U.K. subsidiary Rockwood Specialties Ltd. is the borrower. **Borrowings are in euros and converted into dollars at a conversion rate of 1 Eur=$1.45.

Recovery Analysis

In assigning recovery ratings, Standard & Poor's simulates a payment default scenario that incorporates a borrower's fundamental business risks and the financial risk inherent in its existing capital structure. Our methodology assumes that all committed debt is fully funded, but generally does not make any assumptions for the addition of any other debt prior to default.

In reality, companies that are not at risk of default in the near term may change their capital structure prior to default. However, such changes are not predictable and any changes may affect all aspects of our recovery analysis (i.e., the most likely path to default, valuation given default, and the standing and recovery prospects of different creditors). As a result, our recovery ratings are subject to re-evaluation if a company's capital structure changes materially, which is a key aspect of our ongoing ratings surveillance.

The Eur375 million 7.625% and $200 million 7.5% senior subordinated notes are issued directly by Rockwood Specialties Group Inc. and guaranteed on an unsecured senior subordinated basis by substantially all the existing U.S. domestic subsidiaries. Non-U.S. subsidiaries are not guarantors under the subordinated notes. The notes and the related guarantees rank behind all of the indebtedness of the issuers and guarantors, including the senior secured credit facilities. However, the guarantees are expressly not subordinated to nondebt claims. We note that Rockwood derives the majority of its earnings and cash flow from outside the U.S.

Rockwood's senior secured credit facilities are guaranteed by the parent holding company and the majority of Rockwood's direct and indirect domestic subsidiaries. In addition, foreign borrowings under the facility (term loan A-2 and potential revolving credit draws) are also guaranteed by certain direct and indirect foreign subsidiaries. All credit facility debt is secured by substantially all the assets of the issuer and the U.S. subsidiary guarantors, although the pledge of stock in foreign subsidiaries is limited to 65% of the common shares of the first-tier foreign subsidiaries due to tax reasons. All direct borrowings by foreign subsidiaries are also secured by substantially all the assets of the foreign borrower and guarantors.

The bank credit agreement includes a collateral allocation mechanism that will equalize the recovery rates of the bank lenders in the case of default. This is important because (1) it will adjust for the differences in the credit and collateral support provided to the U.S. and non-U.S. bank debt, and (2) it will align the interests of the U.S. and non-U.S. lenders to maximize the recovery for the bank lenders as a group.

Simulated default scenario

Our simulated default scenario is triggered by a severe economic global downturn affecting several of the company's markets simultaneously, together with raw material and other cost inflation that the company would be unable to pass along to customers in a depressed demand environment. Difficulty integrating acquisitions could also be a contributing factor to a default.

Our analysis assumes that the company's cash flow would need to decline to the point that its EBITDA is no longer sufficient to cover its fixed charges for interest costs, subsistence capital spending, and required debt amortization. This level of capital spending would include such items as required environmental outlays without which the company would be unable to operate or would severely damage its business.

Based on the company's capital structure and our assumed increases in borrowing costs, we estimate that EBITDA would need to decline meaningfully to approximately $375 million to trigger a default. For the purpose of our analysis, we have assumed that the company reaches this level in 2010, and that this prevents the company from being able to refinance its $250 million revolving credit facility at maturity. Other assumptions in our simulated default scenario include:

- The revolving credit facility is fully drawn at the point of default;
- A 350-basis-point increase in borrowing costs on its secured debt due to increases in LIBOR and borrowing rates resulting from credit deterioration and covenant violations; and
- All debt has six months' interest outstanding at default, resulting in total claims of $1.9 billion on the secured bank debt, about $75 million from the holders of other senior secured debt and capital leases, and $763 million on the subordinated notes.

Valuation

We have valued Rockwood on a going-concern basis after default, because we believe that the company's significant presence in niche specialty chemical markets along with its well diversified product portfolio and customer base would enable it to reorganize and that this would maximize recoveries for the company's creditors. Despite temporary softness caused by the industrial downturn in the default scenario, we would expect the markets in which Rockwood participates to continue to have relatively favorable long-term supply and demand fundamentals and good growth prospects associated with the recovery of key end markets and the development of new and more value-added product applications. As a result, we applied our enterprise-value methodology in assessing recovery prospects. We are assuming an emergence multiple of 7x default EBITDA and an enterprise value of about $2.6 billion.

Results

After a 5% reduction for estimated administrative expenses and $50 million for capital leases, the net enterprise value available to creditors totals about $2.45 billion.

Based on consolidated EBITDA contributions (which is how we estimate the enterprise value of the different subsidiaries), we estimate that 17%, or $425 million, of this value stems from Rockwood's domestic subsidiaries and 83%, or $2.07 billion, relates to the foreign subsidiaries.

The value captured by the secured credit facility as collateral is limited by:

- The limited amount of value represented by the U.S. entities that guarantee and secure all credit facility borrowings;
- The modest amount of bank debt borrowed by foreign subsidiaries (estimated at approximately $100 million term debt plus, potentially, certain revolving credit draws), which limits the direct claim against these entities; and
- The fact that 35% of foreign subsidiary equity value is not pledged to the U.S. tranches of the credit facility.

Even with these limitations, we estimate that the collateral value would total about $1.7 billion, which would provide the secured lenders with a recovery of nearly 90%. The remaining undistributed value totals about $680 million and relates to the 35% of foreign equity value that is not pledged as collateral. The remaining bank debt claim of about $200 million would have an unsecured claim against this unpledged value, which would rank pari passu with nondebt claims but be contractually senior to the subordinated note claims.

Potential nondebt claims could include the company's rejection of operating leases, the modification of its union contracts or postretirement benefit commitments, or litigation, regulatory, or other liabilities. While it is difficult to estimate the future amount of such claims at the time of default, we believe they could have a meaningful impact on our recovery estimates.

However, the contractual subordination of the noteholders would require them to turn over their portion of any unsecured recovery to the bank lenders. As a result, we expect the bank debt to have a very high (90% to 100%) recovery, consistent with a '1' recovery rating. Similarly, the subordinated noteholders' recovery would be impaired by this requirement. As a result, we expect that they may only receive an average (30% to 50%) recovery, consistent with a '4' recovery rating.

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