

Rating Action: Moody's upgrades ISA's Issuer rating to Baa2; outlook stable

Global Credit Research - 05 Aug 2014

New York, August 05, 2014 -- Moody's Investors Service today upgraded the Issuer ratings of Interconexion Electrica S.A. E.S.P. (ISA) to Baa2 from Baa3. Concurrently, Moody's raised ISA's baseline credit assessment (BCA) to baa2 from baa3. The rating outlook is stable.

RATINGS RATIONALE

Because the Colombian government is ISA's majority shareholder, ISA falls under the scope of Moody's rating methodology for Government-Related Issuers (GRIs). The Baa2 Issuer rating reflects the application of Moody's joint default analysis (JDA) framework for government related issuers (GRIs). This takes into account the following four input factors: i) the Colombian government sovereign rating as the support provider that was recently upgraded to Baa2 (from Baa3), ii) our estimates of a high default dependence and iii) a medium degree of implied government support in the case of financial distress as well as iv) a BCA of baa2 as a measure for the rated entity's standalone creditworthiness.

The BCA is a representation of ISA's intrinsic creditworthiness before taking into account possible extraordinary support from the sovereign. The raising of ISA's BCA to baa2 from baa3 reflects its leading position in the transmission operations in Colombia with an aggregate market share of around 81% which includes the 10% share of its wholly-owned subsidiary Transelca. The baa2 BCA rating further reflects the visibility of its expected cash flows which is underpinned by the low business risk profile and limited volumetric exposure of its transmission operations and an overall credit supportive regulatory environment.

"ISA's BCA rating also factors that the recent reorganization of its Colombian electric transmission operations with the creation of the new operating company, INTERCOLOMBIA S.A. E.S.P., which Moody's views as credit neutral" said Natividad Martel, a Moody's Vice President. The cash flow split arranged with the system's grid operator wherein INTERCOLOMBIA and ISA directly receive 20% and 80% of the scheduled transmission remuneration, respectively, helps to mitigate somewhat the potential for structural subordination. This would have been the case if INTERCOLOMBIA were to receive 100% of the operating cash flows thus forcing ISA to fully rely on dividend distributions from its subsidiaries. It should be noted that ISA has retained all the outstanding indebtedness related to the Colombian transmission business and will incur any new indebtedness required to fund any new initiatives. No indebtedness is expected to be issued at INTERCOLOMBIA.

The raised BCA incorporates limited uplift from the group's important foreign operations given the limited dividends that ISA is expected to continue receiving from abroad. Importantly, it further assumes that these foreign subsidiaries' new projects will progress smoothly, including the multi-year transmission projects currently being pursued in Chile via Interchile S.A.. The BCA further anticipates that ISA's new corporate strategy that focuses on enhancing the group's profitability will contribute to a disciplined expansion as the group pursues new growth opportunities in Colombia, particularly in the toll-road sector, and abroad. To that end, the BCA assumes that these new investments will be funded in a prudent fashion. Importantly, while the BCA anticipates a deterioration in ISA's credit metrics as the company incurs new indebtedness to fund its equity contributions to these new projects it also assumes that they will remain well positioned within the Baa-rating category; Specifically, that its 3-year average Funds from Operations (FFO) to debt, interest coverage and Retained Cash Flow (RCF) to debt will hover around the mid-teens, and exceed 3.5x and 7%, respectively. The ratings further factor the group's limited foreign currency exchange rate risk. ISA's material dependence on the capital markets to meet unexpected cash flow shortfalls in the absence of committed credit facility tempers the rating albeit the ratings acknowledge that its current debt maturity profile is manageable.

The stable outlook of ISA's baa2 BCA and Baa2 Issuer rating reflects Moody's expectation for continued, predictable cash flow generation from its core Colombian transmission businesses, along with the prudent management of the group's capital expenditure programs for all the foreign subsidiaries. The stable outlook also factors in our expectation that future growth will be pursued only in regulated businesses and that they will be appropriately funded such that ISA continues to report metrics that are commensurate with the Baa rating category according to the guidelines provided in the regulated networks' methodology.

Upward rating pressure on ISA's rating is unlikely given that the Colombian government's sovereign rating is Baa2 with a stable outlook. Moreover, the rating is constrained by the expected deterioration of its key credit metrics albeit they are expected to remain commensurate with the Baa-rating category.

ISA's BCA could be lowered and/or Issuer rating downgraded as a result of a deterioration in the credit supportiveness of the Colombian regulatory framework. A negative rating action could be also triggered if our key assumption regarding the smooth progress of its foreign subsidiaries' new growth initiatives, particularly in Peru and Chile, is not proven to be correct. A downgrade could also occur if leverage ends up being higher than currently expected or by a material deterioration in the credit metrics. Specifically, if its 3-year average FFO to debt, interest coverage and RCF to debt fall below 12.5%, 3.0x, and 7%, respectively, on a sustainable basis.

The methodologies used in this rating were Regulated Electric and Gas Networks published in August 2009 and Government-Related Issuers: Methodology Update published in July 2010. Please see the Credit Policy page on www.moodys.com for a copy of these methodologies.

Headquartered in Medellin, Interconexion Electrica S.A. E.S.P. (ISA) is the largest electricity transmission company in Colombia. It also holds direct and indirect ownership-stakes in a portfolio of power transmission subsidiaries including the 99.99% owned Colombian Transelca and ISA Bolivia as well as the 65.58% owned (excluding preferred stock) in ISA Capital do Brasil. The latter controls 89.5% of the common voting stock (37.8% of the capita stock) of the Brazilian Companhia de Transmissao de Energia Electrica Paulista (CTEEP). In Peru, it holds direct and indirect ownership stakes in ISA Peru (100%), Red de Energia del Peru (60%) and Consorcio TransMantaro (60%; Baa3 stable) whose collective market shares currently aggregate around 65%. ISA further holds directly or indirectly a 100% interest in Interchile that was incorporated in 2013 and is currently pursuing four transmission projects in Chile with an aggregated length of 1,905.8 km, including 1,503km of 500KV networks (single-circuit) in three projects. ISA further holds a 50% interest in Interconexion Electrica Colombia-Panama, a 99.7% stake in the Colombian coordinator of power operations, Compania de Expertos en Mercados XM. It also provides telecommunication data transport services via optic fiber in Colombia, Peru, Venezuela, Chile, Brazil, Argentina and Ecuador through its subsidiaries Internexa and Transnexa. The group's operations further include five concession toll-roads held via Intervial Chile (between 75% and 100% indirect ownership).

The Colombian government is ISA's majority shareholder (51.41% ownership-stake). Other major shareholders include Empresas Publicas de Medellin E.S.P. (10.17%), Ecopetrol (5,32%) and Empresa de Energia de Bogota (1.67%). As of June 30, 2014, ISA reported consolidated assets, indebtedness and Last Twelve Month (LTM) cash flows of around US\$13,5 billion, US\$4.5 billion, and US\$600 million, respectively. At year-end 2013, ISA recorded on a standalone basis assets, indebtedness and cash flows of around US\$5.4 billion, US\$744 million and US\$164 million, respectively. This equated to around 40%, 20%, and 21% of the consolidated assets, indebtedness and cash flows, respectively.

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