FitchRatings

Fitch Affirms ISA's Long-Term IDR at 'BBB+'; Outlook Stable

Fitch Ratings-Chicago-03 May 2019: Fitch Ratings has affirmed Interconexion Electrica S.A. E.S.P.'s (ISA) Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) at 'BBB+'. In addition, Fitch has affirmed ISA's senior unsecured local bond and commercial paper program rating at 'AAA(col)' and 'F1+(col)', respectively. The Rating Outlook is Stable.

ISA's ratings reflect the company's low business risk profile, which is a characteristic of the power transmission business. The ratings incorporate the strong geographic and business diversification of its revenue source, which along with the high predictability of cash flows from operations, translate into a strong financial profile. Also factored in ISA's ratings are its adequate liquidity position and its aggressive growth strategy.

KEY RATING DRIVERS

Low Business Risk Profile: ISA's low business risk profile stems from its participation in regulated natural monopolies, as well as its geographic diversification across seven countries in Latin America. As of December 2018, around 62% of its consolidated revenues came from investment grade countries, namely Colombia, Peru and Chile, while Brazil represented 36.5%. The electricity transmission business, which historically has represented the bulk of the ISA's consolidated cash flow generation, contributed 82.2% of EBITDA in 2018. ISA maintains low business risk as its revenues are regulated in each country and has no exposure to demand risk.

Highly Predictable Cash Flow Generation: ISA's cash from operation stability benefits from its strong and diversified portfolio of electricity transmission assets, along with its participation in other businesses that have limited demand risk. ISA is not exposed to volume risk in the electricity transmission business since its revenues are not dependent on the amount of electricity transported but on the availability of its transmission lines in each country where it operates. In the road concession business, the second largest business for ISA, the company maintains five concessions in operation in Chile, that incorporate a compensation mechanism should the concessions register low traffic volumes.

Manageable Regulatory Risk: ISA's businesses and geographic diversification effectively hedges its exposure to regulatory risk, given that the vast majority of its revenues are regulated. To the extent there is no material correlation among the different regulatory frameworks that drive ISA's revenues, Fitch views ISA's cash flow generation as resilient against some adverse regulatory scenarios. Fitch incorporates in its analysis the expected regulatory reset in the electricity transmission tariff in Colombia. Although there is limited visibility at this point of the final tariff scheme that will be approved by the regulator, Fitch does not believe the final outcome would result in material pressures in ISA's financial metrics. This is due to the fair and balanced nature of the regulation in Colombia, which include the participation of market participants, as well as the company's limited consolidated revenues portion, which the new regulatory tariff would immediately affect. In Brazil, in line with Fitch's expectations, ISA's subsidiary CTEEP continued to collect COP1.3 trillion in 2018 for the compensation from the early renewal of its concession in 2012. These compensation payments will last until 2025.

Aggressive Growth Strategy: ISA's growth strategy is based on its active participation in bidding for electric transmission and other infrastructure projects, as well as inorganic growth through the acquisition of stakes in companies that operate in ISA's core businesses. Recently, the company announced a joint venture with Construcciones El Condor S.A. (CEC: AA-(col)/Negative Watch) through which ISA intends to expand its road concession business in Colombia and Peru. Also, after reaching its 2020 net income targets three years early, ISA released its long-term goals of reaching at least 70% growth in EBITDA by 2030, as well as investing USD10.5 billion in current and new businesses and geographies over the next 13 years. Fitch expects the company will continue to face pressure on FCF in the next two years, as ISA's most recent capex plan for 2019-2023 implies around COP 11.4 trillion in investments, mostly concentrated in 2019-2020 in Chile and Peru projects.

Adequate Credit Metrics: ISA's credit metrics reflect solid cash flow generation, moderate debt levels and adequate liquidity.

Fitch expects that the company will maintain leverage ratios in the 3.5x and 4x range over the rating horizon, considering only current projects underway and the scheduled start of new projects in the next years. Fitch considers this leverage performance consistent with ISA's ratings, given the strong predictability of its CFO performance. Fitch base case projection does not incorporate equity injection or incremental debt to fund ISA's expected incursion in the concession road business in Colombia and Peru, along with CEC, given that this joint venture is still in the preliminary stage. Nevertheless, ISA's ratings factor in Fitch expectation this new business for ISA will not deteriorate its financial credit metrics.

Stand Alone Approach: Under Fitch's Government Related Entities (GRE) Criteria, ISA's ratings are derived from the company's creditworthiness on a standalone basis, as it is considered moderately linked to the Colombian government, which has a 51.4% stake in the company. ISA is a financially strong Government Related Entity (GRE), which has had no need for support. In addition, Fitch considers the regulatory framework fair and balanced. Auction processes in the electricity transmission segment are competitive and open to different market participants. Other shareholders that own roughly 49% of the company are mostly controlled by private and institutional investors. Currently, seven out of nine ISA's board members are independents.

DERIVATION SUMMARY

ISA's credit profile positively compares to peers in the region, such as Transelec S.A. (BBB/Stable), Alupar Investimento S.A.'s (Alupar: Local-Currency IDR BBB-/Foreign-Currency IDR BB/Stable), Transmissora Alianca de Energia Eletrica S.A.'s (Taesa: Local-Currency IDR BBB-/Foreign-Currency IDR BB/Stable) and Consorcio Transmantaro (CTM: BBB-/Stable). All of these companies benefit from a low business-risk profile and predictable cash flow generation. ISA is rated one notch higher than its closest peer Transelec, and two notches above CTM given its large scale of geographically diversified operations in the transmission business and road concessions, which together accounts for around 97% of its EBITDA generation, as well as its more conservative capital structure.

Compared with Taesa and Alupar, ISA's higher rating is mainly a result of the countries from which its main revenues are generated. Most of ISA operations are located in investment-grade countries, namely Colombia, Chile and Peru, while Taesa and Alupar ratings are negatively impacted by the country ceiling of Brazil (BB).

ISA is also well positioned among the national peers that participate in the electricity transmission business, such as Grupo Energia Bogota S.A. E.S.P. (GEB: BBB/AAA(col)/Stable) and Empresas Publicas de Medellin E.S.P. (BBB/AAA(col)/Rating Watch Negative). Together, these companies own and operate the vast majority of the electricity transmission network in Colombia. ISA and EPM's credit profiles benefit from a higher business and geographic diversification, as well as limited dependence on dividends received from their non-controlling stakes within their CFO structure. ISA's cash flow generation is stronger given its predictability, while EPM's rating watch negative reflects the uncertainty related to the development of its key project Ituango.

KEY ASSUMPTIONS

Fitch's Key Assumptions Within Its Rating Case for the Issuer
--Revenue and EBITDA projected for 2019-2022 incorporates the development of projects already granted to the company;
--Changes in the regulatory remuneration of the power transmission business in Colombia have neutral effect on ISA's credit metrics;
--Capex for the next several years reflects the construction stage in new projects awarded to the company and subsidiaries.

RATING SENSITIVITIES

Developments That May, Individually or Collectively, Lead to Positive Rating Action
--A positive rating action is not likely in the short to medium term given the company's credit metrics expectations and its growth strategy.
Developments That May, Individually or Collectively, Lead to Negative Rating Action
--A sustained increase in leverage above 4.5x, on a consolidated or non-consolidated basis, as a result of a progressive deterioration in cash generation, or increased debt levels above Fitch's base case scenario;
--Regulatory changes that put significant pressures on ISA's cash flow generation;

--A change in the company's strategy resulting in a more aggressive strategy in terms of leverage, capex or acquisitions;
--A negative rating action in Colombia's rating may impact ISA's ratings.

LIQUIDITY

Adequate Liquidity: ISA's liquidity is considered adequate and is characterized by healthy cash on hand, strong and predictable cash from operations, manageable debt amortization and strong access to local and international capital markets. At the end of 2018, ISA had approximately COP1.5 trillion of consolidated cash on hand, of which COP434 billion was recorded at the holding level. This compares with around COP1.8 trillion in consolidated short-term debt, of which around COP137 billion was recorded at the holding level.

ISA's maturity profile is manageable, as its long-term debt amortization schedule is spread until 2047. At holding level, ISA's debt maturities for 2019-2021 comprises only credit loans with a maximum annual amortization of COP 169 billion, which is manageable for the company. During 2018, ISA received the regulator's approval to increase in the available local bond program to COP6.5 trillion from COP4.5 trillion. In the coming years, the proceeds of the issuances included in this program should contribute to finance capex and extend debt maturities. At consolidated level, Fitch expects ISA to continue recording negative FCF in 2019-2020, given the required capex of around COP 7.4 trillion in granted projects. Therefore, Fitch expects consolidated debt maturities to be mostly refinanced.

FULL LIST OF RATING ACTIONS

Interconexion Electrica S.A. E.S.P.
--Long-Term Foreign-Currency IDR at 'BBB+';
--Long-Term Local-Currency IDR at 'BBB+';
--Local bond and commercial paper program at 'AAA(col)'/'F1+(col)';

The Rating Outlook is Stable.

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Applicable Criteria
Corporate Rating Criteria (pub. 19 Feb 2019)
Government-Related Entities Rating Criteria (pub. 29 Mar 2019)

National Scale Ratings Criteria (pub. 18 Jul 2018)
Non-Financial Corporates Exceeding the Country Ceiling Criteria (pub. 17 Jan 2019)

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