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Research Update:

Interconexion Electrica S.A. E.S.P. 'BBB-' Rating Affirmed, Outlook Remains Stable

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Overview

- We are affirming our 'BBB-' corporate credit rating on Colombia-based linear infrastructure operator Interconexion Electrica.
- We expect that the company will use the compensations for the early termination of the Brazilian concession to repay debt as it becomes due.
- The stable outlook reflects our expectation that the company's financial ratios will improve in 2014-2015 as overall debt drops and revenue continues to recover from the 2013 drop.

Rating Action

On July 2, 2013, Standard & Poor's Ratings Services affirmed its 'BBB-' rating on Interconexion Electrica S.A. E.S.P. (ISA). The outlook remains stable.

Rationale

The ratings on ISA reflect its "satisfactory" business risk profile, which benefits from a stable and generally predictable business environment in the countries in which it operates. In addition, ISA holds a strong market position by controlling a majority of Colombia's and Peru's electricity transmission grid, and it has continued to pursue further business diversification, which support its business risk profile and profitability. The stand-alone credit profile also reflects ISA's "intermediate" financial risk profile.

The ratings also incorporate our assessment that there is a "low" likelihood that the Colombian government would provide timely support to ISA, if needed, because the company generates significant cash flow and debt outside of Colombia. As its primary shareholder, the Colombian government holds a 51.4% stake in ISA. However, based on our government-related entity criteria, we also assess ISA to have a limited link to the government, given the independence of its management and corporate practices.

In its aim to cut electricity prices for end users, the Brazilian government approved provisional measure 579 (MP 579) and related regulations in December 2012, which offered electric utilities with concessions coming due between 2015 and 2017 the option for an early renewal for up to 30 years in exchange for a compensation payment and a significant reduction in prices and tariffs. The objective was to finance about 65% of the price reduction to end users through lower concession prices and tariffs, while the remaining 35% would

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come from the elimination or reduction of certain sector charges and taxes.

The companies that accepted the proposal received a new tariff from January 2013 onwards that aims to cover, among other things, operations and maintenance expenses, charges and taxes, and a compensation payment from the government equivalent to the unamortized value of the concession assets. The Brazilian government will pay part of the unamortized value of the concession assets upfront and finance the remainder for up to 30 years.

ISA is the controlling shareholder of CTEEP-Companhia de Transmissao de Energia Eletrica Paulista (CTEEP), which accepted the government's proposal. Our ratings on ISA incorporate the expectation that CTEEP will continue to use the proceeds from the early payment of the unamortized value of the assets to pay down its existing debt. CTEEP has already prepaid R$437.2 million with the received proceeds.

In light of the modification of the concession agreement in Brazil, we reviewed our base-case scenario for ISA. Due to CTEEP's future lower margins and the extraordinary inflow of cash from the indemnification proceeds, we expect high levels of cash and short-term investments to be parked in Brazil until debt becomes due. We also expect EBITDA and revenues to drop by 15%-20% during 2013. As a result, its debt to EBITDA will be 3.5x-4.2x in 2013-2015. Net debt to EBITDA, which includes the extraordinary levels of cash and short-term investments will be 2.9x-3.7x in the same period, more in line with ISA's peers.

During the first quarter of 2013, consolidated operating revenue fell by 28.5% mainly due to the 71% fall in ISA's Brazilian business. Prior to 2012, CTEEP's operations accounted for about 43% of ISA's revenues and 49% of its EBITDA. During the first quarter of 2013, only 18% of operating revenue and less than 8% of EBITDA were from the Brazilian operations. Colombia now represents ISA's largest portion of revenues, at 40% followed by Chile with 30%.

ISA is a regional holding group with headquarters in Colombia engaged in the construction, operation, and management of linear infrastructure systems, including electric power transmission, telecommunications, and toll roads.

Liquidity

ISA's liquidity is "adequate" based on the following assumptions:

- A sources-to-uses ratio of 1.9x in 2013 and of 1.5x in 2014.
- The company has benefitted from several individual debt refinancings throughout 2012-2013 and from the prepayment of a portion of CTEEP's debt, which lowered its financing costs and improved its debt maturity profile.
- High future capital expenditures of COP1.6 trillion in 2013 and COP861 billion in 2014.
- For the 12 months ended March 31, 2013, free operating cash flow was COP1.4 trillion due to the incorporation of the indemnification proceeds.
- ISA has flexibility in reducing dividend payments and capital

expenditures, if needed.
- As of March 31, 2013, ISA had cash and short-term investments of approximately COP2.87 trillion compared with COP1.7 billion in the fourth quarter of 2012. This significant increase is due to the Brazil government's compensation for the early termination of CTEEP's concession. We expect ISA to use these proceeds to repay CTEEP's debt.

Outlook

The stable outlook reflects our expectation that ISA's revenue and net income will fall 15%-20% during 2013 following the termination of the Brazilian concession agreements. We expect key financial metrics to improve in 2014-2015 as overall debt decreases and revenue recovers from the 2013 drop.

We could raise the ratings if the company's revenues and income increase faster than expected based on positive macroeconomic indicators in the countries where ISA operates and the strengthening of its operating margin. In addition, ISA's ability to expand and diversify, while posting a consolidated FFO to total debt above 30% and total net debt to EBITDA below 3.0x, could lead to an upgrade.

However, if ISA were to commit to heavily debt-financed acquisitions that deteriorate its financial risk profile, resulting in a consolidated net debt to EBITDA above 4.0x and an FFO to debt lower than 20%, we could lower the rating.

Related Criteria And Research

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Sept. 28, 2011
- Rating Government-Related Entities: Methodology and Assumptions, Dec. 9, 2010
- Key Credit Factors: Business And Financial Risks In The Investor-Owned Utilities Industry, Nov. 26, 2008
- 2008 Corporate Criteria: Analytical Methodology, April 15, 2008

Ratings List

Ratings Affirmed

Interconexion Electrica S.A. E.S.P. (ISA)

Corporate Credit Rating	BBB-/Stable/--

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