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Credit Opinion: Empresa de Energía de Bogotá S.A. ESP. (EEB)

Global Credit Research - 19 Nov 2012

Bogota, Colombia

Ratings

Category	**Moody's Rating**
Outlook	Stable
Senior Unsecured	Baa3
Transportadora de Gas Internacional	
Outlook	Stable
Senior Unsecured	Baa3

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Key Indicators

[1]**Empresa de Energía de Bogotá S.A ESP. (EEB)**

	2008	**2009**	**2010**	**2011**	**LTM 3Q'12**
(CFO Pre-W/C + Interest) / Interest Expense	**3.8x**	**3.8x**	**8.8x**	**2.3x**	**4.6x**
(CFO Pre-W/C) / Debt	**23.9%**	**28.8%**	**67.4%**	**14.6%**	**36.3%**
(CFO Pre-W/C - Dividends) / Debt	**6.6%**	**9.9%**	**0.3%**	**14.6%**	**14.5%**
Debt / Book Capitalization	**21.8%**	**19.1%**	**17.3%**	**16.1%**	**14.5%**

[1] All ratios calculated in accordance with the Global Regulated Electric Utilities Rating Methodology using Moody's standard adjustments.

Note: For definitions of Moody's most common ratio terms please see the accompanying User's Guide.

Opinion

Rating Drivers

- Material structural subordination

- High reliance on cash upstreams from non-controlled subsidiaries

- Controlled subsidiaries expected to slowly grow in importance with successful completion of projects in Guatemala and Peru

- EEB's deleveraging strategy and prudent dividend policy expected to result in robust credit metrics

Corporate Profile

Headquartered in Bogota, Colombia, Empresa de Energia de Bogota S.A. E.S.P. (EEB) is a Colombian transmission company subject to the purview of the Comisión de Regulación de Energía y Gas (CREG). It is also a holding company with material equity interests in controlled and non-controlled subsidiaries that conduct their electric and natural gas operations in Colombia (Baa3, stable), Peru (Baa2, positive) and Guatemala (Ba1, stable).

EEB's controlled subsidiaries include the Colombian natural gas transportation company, Transportadora de Gas Internacional S.A. E.S.P. (TGI; Baa3, stable; 68.1% ownership stake); the holding company Decsa S.A. E.S.P. (51% interest) which holds a 82% equity interest in the electric utility Empresa de Energia de Cundinamarca S.A. E.S.P. (EEC); Peruvian natural gas transportation and distribution subsidiaries: Calidda (total in- and direct interest 66.2%) and Contugas S.A.C. (total in- and direct interest 90%; including TGI's 25%); as well as the Guatemalan subsidiaries: EEB Ingenieria y Servicios S.A. (EEBIS; 100%) and Transportadora de Centroamerica S.A. (Trecsa; 98%). These companies are pursuing material investment programs.

EEB's non-controlled subsidiaries include the Colombian unregulated generation company Emgesa S.A. E.S.P. (43.6% of voting rights), as well as the electric and natural gas utilities Codensa S.A. E.S.P. (42.85% of voting rights) and Gas Natural S.A. E.S.P. (25%). Early 2011, EEB also acquired a 15.6% interest in the Colombian natural gas transportation company Promigas which holds majority stakes in natural gas distribution companies and the remaining 40% equity interest in Calidda. EEB also holds 40% equity interest in the Peruvian electric transmission companies Red de Energia del Peru (REP) and Consorcio TransMantaro (CTM).

The District of Bogota (Baa3, stable) remains EEB's majority shareholder with 76.3% ownership stake (before: 81.54%) after the November 2011 share issuance (gross proceeds of around US$400 million). EEB's remaining shareholders consist of Ecopetrol (Baa2, stable; 6.87%), Corficolombiana S.A. (3.6%), local pension funds (6%) and retail investors (7.3%). As of September 30, 2012, EEB recorded assets of approximately US$6billion (about 75% of the consolidated assets), and funds from operations of around US$310million for the last twelve months ended the same period (around 60% of the consolidated FFO).

For more details about the group's subsidiaries and operations refer to the presale report published on EEB in November 2011 available in www.moodys.com

Rating Rationale

The Baa3 senior unsecured rating reflects EEB's ownership structure and linkages with the District of Bogota (Baa3, stable). It is our understanding that pursuant to Agreement nr 01, 1996, the District of Bogota is required to hold at least a 51% ownership stake in the issuer. Given the District's majority ownership stake, EEB falls under the scope of Moody's rating methodology for government-related issuers (GRIs). The rating reflects Moody's assessment of a strong probability of extraordinary support from the municipality and a moderate level of dependence. The latter reflects the degree to which the District is exposed to the same risks as those that would affect credit quality at EEB. It also factors some potential risk of political interference by the District, particularly in the absence of a governance framework agreement that clearly outlines EEB's relationship with the District of Bogota; however, our concerns are mitigated by the country's legal and regulatory requirements that EEB needs to comply with before implementing any material corporate reorganizations. As evidence of the latter we observe the newly elected Mayor of Bogota's plans end of 2011 for a possible legal re-organization of EEB and two other companies in which the Municipality also holds majority ownership stakes did not materialize.

EEB's Base Credit Assessment (BCA), which is a representation of its intrinsic creditworthiness before taking into account possible extraordinary support from the municipality, is ba1. EEB's BCA largely reflects the structural subordination that results from its strong dependence on the cash up-streamed from its subsidiaries to service its debt, particularly from its non-controlled subsidiaries, despite its own profitable transmission operations. However, the BCA also captures the regulated nature of the operations of most of its subsidiaries and the aggressive dividend policy of its key non-controlled subsidiaries that enhances EEB's cash flow visibility. The BCA assumes the successful completion of the material electric transmission and natural gas capital expenditure (capex) projects currently pursued in Peru and Guatemala. It acknowledges the resulting diversification benefits and the slowly growing relevance of the controlled subsidiaries as a source of cash flows. It also incorporates the assumption that EEB will further pursue new growth opportunities in Colombia and other regional countries with transparent regulatory frameworks. The BCA assumes that EEB will fund them in a prudent fashion, and maintain a reasonable dividend policy that allows it to continue to report robust credit metrics. In the absence of committed bank credit facilities the BCA also captures EEB's reliance on the capital markets to meet unexpected cash flow shortfalls albeit its current debt maturity profile is manageable.

DETAILED RATING CONSIDERATIONS

GROWING OWN TRANSMISSION OPERATIONS

EEB reports around US$30 million of gross margin associated with its transmission operations. Around 60% of its transmission assets became operational before 2000. Their tariffs include a 11.5% rate of return to be applied on the assets' replacement value and are subject CREG's reviews every five years with the next one not anticipated before 2015. We believe the Colombian regulatory framework compares well to those in other Latin American countries in terms of predictability and transparency. Albeit it is still subject to some development it has been in place for over fifteen years, and we believe CREG's decisions are overall credit constructive. The balance of EEB's transmission assets started operations after 2000 For the first 25 years of concession, the remuneration of the assets is based on the winning bid that included estimated annual revenues in USD, as well as Administration, Operation and Maintenance expenses, as well as opportunity costs of the capital invested. After 25 years, these assets will be also subject to the CREG's transmission charges. During 2012, EEB continued growing its transmission asset base after winning three new projects under the National Transmission System expansion plan that were allocated under competitive auctions by the Colombian planning authority (UPME). The planned multi-year investments aggregate around US$170 million (additional annual gross margin of around $15 million). EEB estimates that upon their successful completion its market share will grow by 2015 to about 11% (currently 8%) in terms of total assets. Despite the inherent construction risk of the new projects the enhancement of EEB's ability to generate its own operating cash flows is credit positive.

BUT STRUCTURAL SUBORDINATION WILL REMAIN SUBSTANTIAL

While the BCA acknowledges EEB's own cash flows generation it also takes into accountthat those associated cash flows are insufficient to fully cover EEB's aggregate obligations, including interest and expenses incurred in connection not only with its own operations but also its holding company's activities. Therefore, the BCA is capped by the degree of structural subordination that exists for parent level debt-holders relative to the existing debt outstanding at its various subsidiaries given EEB's dependence on the dividend and interest payments from its controlled and non-controlled subsidiaries to meet its own obligations. As of September 30, 2012, EEB's parent only indebtedness remains substantial and represented about 43% of the consolidated indebtedness, a credit negative. However, we acknowledge the declining trend (historically around 50%) following the scheduled repayment of EEB's loans (US$34 million) and the group's growing indebtedness (net:+US$32 million) during the first nine months of 2012. We also note that around 75% of EEB's outstanding standalone indebtedness was incurred to aid TGI to fund the acquisition of its natural gas transportation assets. EEB made a US$340 million equity contribution and granted a US$370 million subordinated loan. The terms of the latter, including its interest rate (now 6.125% compared to 8.75%) and maturity (December 2022 versus October 2017), were amended after TGI's 10-year US$750 million 5.7% yankee-bond issuance in March 2012 for the early redemption of its outstanding 9.5% unsecured notes due in 2017.

RELATIVELY PREDICTABLE CASH UPSTREAMS FROM ITS SUBSIDIARIES

The BCA assumes that its non-controlled subsidiaries - particularly, Emgesa, Codensa and Gas Natural - will remain EEB's main source of cash flow (i.e. accounting for over 90% of its up-streamed dividends) over the foreseeable future. The lack of control over their operations, is a credit negative; however, this concern is mitigated by their record of an aggressive dividend policy (including capital reductions), the absence of any distribution tests, and EEB's voting rights, affecting Emgesa's and Codensa's dividend distributions of less than 50% of their net distributable profits. . We also acknowledge that their ability to generate robust and predictable cash flows is underpinned by their leading position in their respective market segments and the regulated nature of the operations of most of these Colombian companies with tariffs in place until at least 2014. While Emgesa's operations are unregulated, we believe its overall prudent commercial policy helps to offset the cash flow volatility typically associated with power generation activities, and we anticipate its dividend distributions will remain material despite its material capex (around US$837 million) associated with the construction of the 400MW El Quimbo hydro-plant (expected completion in December 2014). During 2011, EEB received around US$190 million in dividends from these non-controlled subsidiaries, a significant decrease compared to 2010 (around US$600 million) when those companies split their financial statements into two separate accounting periods to be able to distribute additional dividends. EEB's BCA assumes that going forward the dividends received from these subsidiaries will be more similar to historical levels aggregating over US$250 million annually. During the first nine months 2012, EEB received around US$316 million in dividend and interest payments. We do not expect these companies will pursue over the near to medium term capital distributions via new capital reductions, as Emgesa did during 2010 (around US$250 million), as we understand they do not currently meet the legal requirements to do so. The Peruvian subsidiaries REP and CTM are not expected to payout any dividends before the completion of their material capex program (over $800 million) scheduled for 2013.

SLOW BUT GROWING RELEVANCE OF THE CONTROLLED SUBSIDIARIES

Historically, the cash received by EEB from its controlled subsidiaries was associated with the interest payments under the intercompany loans granted by EEB to the natural gas transportation companies Transcogas and TGI (around US$45 million p.a.). TGI's indebtedness is declining after the repayment last year of a second US$230 million loan granted by EEB via an SPV to fund its Cusiana-Vasconia expansion project, and as it is using the remaining proceeds from the CVCi $400 million equity offering in 2011 (40% stake) to fund its remaining capital outlays. TGI's cash flows are further enhanced as the new projects under its substantial capex program progressively start operations. CREG's decision regarding TGI's petition for the regulatory body to review certain items included in the September 2011 proposed new maximum regulated natural gas transportation charges is still pending. A positive outcome would further improve TGI's cash flows with new tariff review not due before the end of 2016. Over time, we anticipate that TGI will become free cash flow positive, and that it will also start making dividend distributions during 2013 with a target dividend payout ratio of 50% (over US$60 million p.a.).

We understand that satisfactory progress is being made in Calidda's project to expand under a concession agreement the natural gas systems in the Peruvian Department of Lima and the Province of Callao. The current phase consists of investing US$500million to add 455,000 customers by 2016 (around 80,000 customers as of June 2012). Calidda has already executed the bulk of its financial arrangements with EEB's remaining equity contributions (60% direct interest) this year and next year limited to less than US$50 million. We do not anticipate EEB will receive payouts from Calidda until at least the second phase of its capital investment starts operations. We note that Cálidda's up-streamed cash flows will be subject to distribution tests under its current financial documentation but we anticipate the company will be able to comply with the requirements to report prospective debt service coverage and retained cash on hand of at least 1.3x and US$3 million, respectively.

EEB's rating also captures the anticipated successful completion of the significant electric transmission project in Guatemala (Trecsa; capex: US$373 million) as well as natural gas transportation and distribution networks under a 30 year concession in Peru (Contugas; capex: US$326 million) that are not without execution risks. While we understand that Contugas is also making satisfactory progress with its expected completion before end of June 2013 (over 60% completed; partial operations started during the first quarter of 2012), Trecsa has faced some delays in connection with the challenges to attain rights of ways in the indigenous areas. We understand that despite the delay (up to six months) which is considered force majeure and not anticipated to have any financial consequences, the project is expected to be completed before year-end 2013, and that it. EEB's BCA incorporates the assumption that the shareholder equity contributions into Trecsa (EEB's stake: 98%) and Contugas (EEB:75%/TGI:25%) will amount to 40% and 30%, respectively, of the planned capex, respectively, and that EEB's remaining equity injections during 2013 will be less than US$50 million. EB is considering different options for the long-term financing of Trecsa, while EEB and TGI are also in the process of arranging long-term indebtedness for Contugas to replace during 2013 the outstanding short term financing.

We expect that EEB will pursue new investment opportunities in the region by exclusively focusing on regulated operations in stable and predictable regulatory environments where EEB can secure a controlling position. In this regard, we note that its subsidiary EEBIS is focusing in new electric transmission projects in Guatemala (up to US$50 million over the three years), and that EEB participated during 2012 in two auctions to build transmission assets in Chile (planned investments aggregated around US$1 billion). While EEB's bids were not successful, the company intends to pursue new opportunities in that country.

ROBUST CREDIT METRICS AMID SOME PROGRESSIVE DELEVERAGING AMID PRUDENT DIVIDEND POLICY

Given EEB's dependence on its subsidiaries' dividend distributions to service its debt we consider in our assessment mainly EEB's standalone credit metrics. The significant deterioration during 2011 of its CFO pre-W/C to debt and interest coverage compared to the metrics recorded at year-end 2010 is largely driven by the significant changes in the cash inflows received from its key non-controlled subsidiaries cited above. EEB used the 2010 extraordinary cash inflows to also distribute additional dividends to its shareholders in 2010 which impacted its recorded Retained Cash Flow (RCF) to debt metric. While EEB's shareholders received no dividend distributions during 2011, they receive around US$110 million in connection with EEB's capital reduction on account of Emgesa's equity reduction.

Going forward, EEB's ba1 BCA assumes the company will continue to generate credit metrics that are robust for the rating category which we believe is necessary to somewhat offset the substantial structural subordination EEB's cash flows, particularly, its material dependence on its non-controlled subsidiaries' dividend distributions. We also consider in our assessment the subsidiaries' indebtedness to fund the greenfield projects in Peru

(Contugas) and Guatemala (Trecsa). EEB's BCA rating captures our expectation that EEB will be able to report RCF to debt and interest coverage ratios in the high teens and 4.5x, respectively, on a sustainable basis.

To that end and following the 2011 equity issuance (around US$400 million) as well as the financial indebtedness incurred in connection with the Calidda acquisition (around US$117 million) that was recently fully refinanced, EEB's BCA rating assumes that the company will continue over the medium term to progressively deleverage its balance sheet such that it will largely use its own cash balances and internally generated cash flows to fund its currently planned investments in its own transmission business, as well as its remaining planned equity contributions. That said, we acknowledge that this may change should EEB identify a substantial investment opportunity such as winning the auction for a material new transmission project. However, EEB's BCA is predicated on the assumption that any new project will be funded in a prudent fashion, including a reasonable dividend policy. EEB has publicly disclosed it plans to continue distributing at least 50% of its distributable net income, and will pursue new capital reductions only in conjunction with its subsidiaries' future capital distributions.

Liquidity Profile

After the refinancing of its US$610 million global notes in November 2011 and the recent repayment of two local bank loans (around US$70 million) that were due mid November and 2014, respectively, EEB's standalone indebtedness approximates US$710 million. In the absence of committed credit facilities EEB's reliance on the capital markets to meet its funding requirements, is credit negative.

However, we acknowledge that EEB's capital requirements to fund its investments have dropped significantly compared to 2011 when EEB used its balance sheet cash to fund the acquisition of its current equity interests in Promigas and Cálidda. We also consider that EEB reported US$136 million in cash and short-term investments as of September 30, 2012 and has a manageable debt maturity profile with total annual scheduled repayments of around US$15 million starting next year under its US$100 million term loan due in 2020. Also we consider the debt maturity profile of EEB's controlled subsidiaries manageable given that Cálidda has annual repayments under its loan obligations of around US$18 million, and TGI's indebtedness is bullet maturing in 2022. As mentioned earlier, for Contugas and Trecsa long-term funding arrangements are currently under consideration. These will be used to refinance the debt executed to bridge Contugas' funding needs that are scheduled to mature between late 2013 and early 2014. In the extreme case that the funding arrangements would not succeed, we believe that EEB's cumulated cash and cash equivalents would suffice to repay at least half of the aggregated amount of Contugas' maturing indebtedness and Trecsa's external funding requirements; this helps offset to some degree the related concerns.

Rating Outlook

EEB's stable outlook reflects our expectation that EEB will continue to benefit from the strong cash distributions received from its uncontrolled subsidiaries, the successful completion of its ongoing major capex programs in Guatemala and Peru, and the slowly growing relevance in terms of cash flow contributions of the controlled subsidiaries, including TGI. It also incorporates our expectation that any new material investments will focus exclusively on regulated operations which will be funded in a prudent fashion, such that EEB reports key credit metrics that compare well with its current BCA rating. If further reflects our expectation that EEB will continue reporting robust credit metrics.

What Could Change the Rating - Up

EEB's BCA rating could be upgraded if over the long term its reliance on its controlled subsidiaries' dividends increases significantly such that they exceed the dividends received from its non-controlled subsidiaries in terms of cash flows contributions. Quantitatively, an upgrade could be triggered if EEB reports unconsolidated RCF over in the high teens, on a sustainable basis. EEB's senior unsecured rating could experience some upward momentum if the rating of the District of Bogota is upgraded, and that Moody's continues to consider that a strong probability of extraordinary support by the District of Bogota, and/or a moderate level of dependence remain appropriate.

What Could Change the Rating - Down

EEB's BCA could be downgraded if the current capex program being pursued via Trecsa (Guatemala) and/or Contugas (Peru) is poorly executed. Negative momentum could be triggered if the cash up-streams received by EEB deteriorate substantially and/or indebtedness increases significantly above anticipated levels such that the credit metrics deteriorate; Specifically, if CFO pre-W/C interest coverage and CFO pre-W/C to debt fall below 2.0x and the mid teens, respectively, on a sustainable basis. Apart from a change in the standalone fundamental credit quality of the issuer, the rating of the notes could be downgraded if EEB decided to incur significant amounts of secured debt as a proportion of its total debt, the proportion of EEB's stand alone debt over consolidated indebtedness does not continue declining, and/or upon a substantial increase in the group's exposure to unregulated operations or subsidiaries that operate under less credit supportive regulatory environments. Moreover, a downgrade in the District of Bogota's rating and/or a perception that a lower degree of extraordinary support from the District is applicable could also negatively affect EEB's rating.

Other Considerations

We note that after EEB's US$610 million 6.125% 10-year notes due in November 2011 attained its second investment grade rating the financial covenants under the indenture that limited EEB's ability to incur new indebtedness and make restricted payments do not currently apply.

The bulk of EEB's indebtedness (around 90%) is denominated in foreign currency, mainly US dollars. It is our understanding that EEB has not executed new derivatives on top of its 2008 swap with a notional amount of US$133 million that helps offset its foreign exchange risk in combination with the natural hedges associated with the indexation of a portion of its transmission revenues to US$ and TGI's interest payments under the intercompany loan (over 50% of TGI's revenues are indexed to US$).

Moody's evaluates EEB's BCA mainly relative to Moody's Regulated Electric and Natural Gas Utilities methodology published in August 2009. As depicted in the grid below, the issuer's indicated BCA rating based on both historical and projected credit metrics is Baa. The assigned ba1 BCA results after applying notching for the above mentioned material structural subordination.

Rating Factors

Empresa de Energía de Bogotá S.A. ESP. (EEB)

Regulated Electric and Gas Utilities Industry [1][2]	**Current LTM 09/30/2012**		**Moody's 12-18 month Forward View* As of November 2012**	
Factor 1: Regulatory Framework (25%)	**Measure**	**Score**	**Measure**	**Score**
a) Regulatory Framework		Ba		Ba
Factor 2: Ability To Recover Costs And Earn Returns (25%)				
a) Ability To Recover Costs And Earn Returns		Ba		Ba
Factor 3: Diversification (10%)				
a) Market Position (10%)		Ba		Ba
b) Generation and Fuel Diversity (0%)				
Factor 4: Financial Strength, Liquidity And Key Financial Metrics (40%)				
a) Liquidity (10%)		Ba		Ba
b) CFO pre-WC + Interest/ Interest (3 Year Avg) (7.5%)	4.8x	A	4.5x-6.0x	A
c) CFO pre-WC / Debt (3 Year Avg) (7.5%)	31.1%	Aa	30%-40%	Aa
d) CFO pre-WC - Dividends / Debt (3 Year Avg) (7.5%)	2.4%	Ba	9-17%	Baa
e) Debt/Capitalization (3 Year Avg) (7.5%)	18.3%	Aaa	25%-35%	Aa
Rating:				
a) Indicated Rating from Grid		Baa		Baa
b) Actual BCA Assigned		ba1		ba1

* THIS REPRESENTS MOODY'S FORWARD VIEW; NOT THE VIEW OF THE ISSUER; AND UNLESS NOTED IN THE TEXT

DOES NOT INCORPORATE SIGNIFICANT ACQUISITIONS OR DIVESTITURES

[1] All ratios are calculated using Moody's Standard Adjustments. [2] LTM 09/30/2012; Source: Moody's Financial Metrics

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