24 Apr 2019 | Affirmation

Fitch Affirms Calidda's IDRs at 'BBB'; Outlook Stable

Fitch Ratings-Chicago-24 April 2019: Fitch Ratings has affirmed Gas Natural de Lima y Callao S.A.'s (Calidda) Long-Term Local and Foreign Currency Issuer Default Ratings (IDR) at 'BBB'/Stable Outlook. Fitch has also affirmed Calidda's USD320 million of senior unsecured notes due in 2023.

Calidda's ratings reflect the company's stable capital structure supported by its naturally monopolistic market position as Lima and Callao's sole natural gas (NG) distributor. The rating is further supported by sustained cash flow stability provided by the company's transparent, regulated tariff scheme designed to ensure adequate return on investment. Calidda's cash flow generation also continues to benefit from expected demand growth of around 125,000 residential client additions per year going forward, based on Fitch's estimates.

KEY RATING DRIVERS

Predictable and Stable Cash Flow: Calidda's stable and predictable cash flow generation is supported by its long-term take or pay, U.S. dollar-denominated contracts with top tier power generators and large industrial companies. During 2018, these contracts represented 90% of the total invoiced volume comprising seventeen clients. Additionally, the company's regulated tariff scheme assures cost recovery and fixed return over approved capital investments, further supporting cash flow predictability. The regulator reviews the distribution tariff every four years in order to set the base return rate at 12% over approved investments and operational expenses. Fitch expects that once the company reaches penetration rates close to 90% and revenues from installation and financial services falls overtime, its cash flow should remain strong as distribution revenues gradually replace these services.

Adequate Credit Metrics: Calidda's credit metrics are solid and supportive of its investment grade rating. Leverage, measured as total debt/EBITDA was 3.0x in 2018 down from 4.4x in 2013. Fitch expects the company will maintain leverage metrics between 3.0x and 3.5x during the 2019-2022 period, while partially financing capex with internal cash flow and paying moderate dividends in line with historical levels. Fitch's incorporates expectations for a substantial capex expansion program in the near to medium term of around USD100 million per year. As of 2018, the company generated USD159 million of EBITDA, up from USD138 million in 2017 mainly due to higher volumes and tariffs.

Adequate Gas Supply: Calidda gas supply and transportation is secured through 2033. The company increased its contracted volume to 248 mmcfd (take or pay and interruptible) with the Camisea consortium, 40% higher than in 2016. The company also has a long-term contract with Transportadora de gas del Peru, S.A. (BBB+/Stable) for 228 mmcfd (take or pay and interruptible) through 2033. Single-source exposure is mitigated by the fact that Pluspetrol, the consortium operator, is obliged to prioritize NG supply to cover local demand according to its concession agreement. As of December 2017, according to Peruvian Ministry of Energy and Mines, Camisea (Lots 56 &88) and the nearby Lot 57 had approximately 12.9 trillion cubic feet (TCF) of NG proved reserves.

Strong Market Position: Calidda is the largest NG distribution company in Peru and the sole gas distributer in Lima and Callao. The service area under its concession concentrates more than 35% of the country's population and over 50% of its GDP. The concession term lasts through 2033, and may be renewed upon request from Calidda in 10-year increments up to 2060. Its total network reaches 9,691 km with a 79% penetration rate and installed capacity of 420 mmcfd. The company expects to increase penetration rate to 85% by 2023, reaching approximately 1.4 million customers as it continues to expand its distribution capacity.

Neutral Shareholder Support: Calidda's risk profile benefits from the expertise and support of its shareholders Grupo de Energia de Bogota S.A. E.S.P. (GEB BBB/Stable) (60%) and Promigas S.A. E.S.P.(Promigas, BBB-/Stable) (40%). GEB is a leading energy holding company with interests across the electricity and natural gas sectors in Colombia, Peru and Guatemala, while Promigas is one of the largest NG transportation and distribution companies in Colombia and Peru. Although Fitch's forecast incorporates annual dividends through the rating horizon, the agency expects the shareholder to continue maintaining leverage below 3.5x. Absent parent support, Calidda's ratings are still commensurate with a 'BBB' credit profile.

DERIVATION SUMMARY

Calidda's ratings are similar to Elektra Noroeste, S.A. (BBB/Stable), Promigas S.A. E.S.P. (ENSA) (BBB-/Stable) and Companhia de Gas de Sao Paulo (Comgas, LC IDR of BBB-/Stable) due to the low business risk that stems from this companies' participation in regulated utilities businesses leading to somewhat predictable cash flow generation.

Calidda's ratings are in line with those of ENSA given the similar capital structure at 3.5x through the investment cycle. Calidda is rated one notch above Comgas LC IDR due to the different operating environment despite stronger capital structure at 2.0x through the rating cycle. Calidda is rated one notch above Promigas due to Promigas more aggressive capital structure and negative cash flow generation expectations. Promigas debt to EBITDA ratio was around 4.5x as of 2018.

KEY ASSUMPTIONS

Fitch's Key Assumptions Within its Rating Case for the Issuer
--The company will add an average of 125,000 residential/commercial clients per year during the next four years;
--Annual volumes increase by around 1% on average over the next four years.
--Pass-through of costs and inflation in the tariffs;
--Annual capex of approximately $100 million on average for the next four years;
--Dividend distribution of 85% of previous year net income

RATING SENSITIVITIES

Developments That May, Individually or Collectively, Lead to Positive Rating Action
--Significant and sustained deleveraging to about 2.0x;
--Growth and consolidation of the regulated demand (NGV and residential and commercial segments);
-- Improved credit quality of off-takers.

Developments That May, Individually or Collectively, Lead to Negative Rating Action
--Sustained total debt/EBITDA above 3.5x due either to operational deterioration or unexpectedly large dividend distributions;
--Material negative changes in BOOT agreement and accomplishment, tariff scheme and applicable regulations;
--Material decline in new connections that negatively impact revenues not followed by increased gas invoiced to residential/commercial users.

LIQUIDITY

Adequate Liquidity: The company's liquidity position is adequate as a result of cash on hand, adequate internal cash flow generation, comfortable debt amortization profile and unused uncommitted credit lines of USD111 million as of Dec. 31, 2018. Calidda's policy is to maintain a minimum cash of USD10 million to USD15 million.

Since 2015, the company has been adding medium-term debt to fund the distribution system expansion as well as for annual dividends payments of around USD30 to 52 million. Fitch expects the company to continue distributing dividends to shareholders, although leverage should not surpass 3.0x-3.5x through the medium term. As of year-end 2018, Calidda showed gross leverage of 3.0x and interest coverage of 9.8x.

As of Dec. 31, 2018, the company reported USD478 million of debt. Around 87% of it is USD-denominated, and its tariff is calculated in USD, and the balance has a currency swap. Exchange rate risk is limited to the collection period (approximately 30 days). The company hedges expected net proceeds and some client financing based on the exchange rate forecast on a monthly basis.

FULL LIST OF RATING ACTIONS

Fitch has affirmed the following ratings:

Gas Natural de Lima y Callao S.A (Calidda)
--Long-Term Foreign Currency IDR at 'BBB';
--Local Currency Long-Term IDR at 'BBB';
--USD320 million due 2023 senior unsecured notes at 'BBB'.

The Rating Outlook is Stable.

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Summary of Financial Statement Adjustments - Non-recurrent arbitrary expenses were added back to 2018 EBITDA.

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Additional information is available on www.fitchratings.com

Applicable Criteria

[Corporate Rating Criteria (pub. 19 Feb 2019)]

[Parent and Subsidiary Rating Linkage (pub. 16 Jul 2018)]

Additional Disclosures

[Dodd-Frank Rating Information Disclosure Form]

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