FitchRatings

# FITCH EXPECTS TO RATE CALIDDA'S USD320MM PROPOSED ISSUANCE 'BBB-'

Fitch Ratings-Chicago-14 March 2013: Fitch Ratings expects to rate Gas Natural de Lima y Callao S.A's (Calidda) USD320 million senior unsecured proposed debt issuance 'BBB-'. Fitch has also assigned foreign and local currency Issuer Default ratings (IDRs) of 'BBB-' to Calidda. The Rating Outlook is Stable.

The company expects to use the proceeds from the debt issuance to repay approximately USD197 million of debt outstanding and to finance approximately USD123 million of capital expenses.

KEY RATING DRIVERS

Calidda's investment grade ratings reflect the company's strong market position in the Peruvian natural gas industry due to its exclusive right to distribute natural gas in Lima and Callao, the largest market in Peru with a high potential growth. The ratings also factor in Calidda's diversified client base, and its predicable and stable cash flow generation. Calidda's cash flow stability and predictability is supported by a regulated tariff scheme, which aims at assuring an adequate return on investment. Calidda's cash flow generation will also benefit from expected demand growth.

The ratings incorporate the company's increase in leverage resulting from the transaction. Fitch expects the company to use the incremental debt to partially finance its capital expenditure plan and for leverage to decrease to a level more in line with the assigned rating over the short to medium term. Leverage, on a pro forma basis and after given effect to the transaction, is expected to be approximately 4.9 times (x) when compared to 2012 cash flow generation levels. For 2013, Calidda's leverage is expected to decrease to approximately 4.5x and to range between 3.5x and 3.0x thereafter.

Strong Market Position: Monopoly Concession Area

Calidda is the largest natural gas distribution company in Peru. It has exclusive right to distribute natural gas in Lima and Callao, a metropolitan area with approximately 10.4 million people and where one third of the country's population resides. Calidda was granted a 33-year concession starting 2000. The concession may be renewed upon request from Calidda after 2033 in 10-year increments and up to 2060. As of today, Calidda has complied with all the commitments established in the concession.

Natural Gas (NG) Industry of National Strategic Importance

NG is the second most demanded power source in Peru after hydroelectric energy. Approximately 42% of Peru's electricity is generated using NG-fired thermoelectric plants, 89% of which is generated in Lima. Calidda distributes the NG used to generate 97% of the country's thermoelectric generation. The government of Peru, through Law 1999, declared the development of NG infrastructure of national interest and has been promoting the use of gas at large scale by establishing a goal of connecting 500 thousand households by 2016. As of December 2012, there were a few more than 100 thousand clients.

Regulated Industry: The Single Tariff Scheme Guarantees Return on CapEx and OpEx

Tariff scheme recognizes future efficient investments and costs applying an annual discount rate of 12% so it assures the payment of Calidda's main grid and secondary network expansions. Tariffs are indexed to U.S. dollars and reviewed every four years by the regulator OSINERGMIN. Tariffs are also annually adjusted considering variations in exchange rate, US PPI, Steel Price Index, Polyethylene Price Index and Peruvian Wholesale. The next four-year tariff will take place in 2014, and an increase is expected due to higher levels of CapEx.

Diversified Client Base with a Predicable and Stable Cash Flow

Calidda has a diversified client base by serving four types of segments: Power generators, industrial companies, natural gas powered vehicles (NGV) and commercial and residential. In 2012, transported volumes were mainly explained by power generators (69%) while revenues are more diversified as power generators represented only 34% of revenues, installation services mainly for commercial and residential represented 26%, industrial companies 19%, and NGV 15%. The regulated clients (such as NGV, commercial and residential clients) provide stable and predictable cash flow while 48% of distribution revenues come from firm take-or-pay contracts with top tier companies (power generators and large industries) with an average life of 19 years.

High Potential Sector Growth

Fitch expected Peru's GDP growth rates of 6.2% and 6.3% in 2013 and 2014, respectively. Lima and Callao represent 44% of Peru's GDP (estimated at USD180 billion) and are the largest market in Peru in terms of clients, industrial activity and power generation. The potential market for residential NG connections is estimated at approximately 1.4 million households. As of December 2012, Calidda served approximately 103,723 clients and the company had an estimated market penetration of around 43%. Of the 49 Lima districts, Calidda actually serves residential customers in 13 districts, and industrial, NGV and power generators in 34 districts.

The company expects that new clients per year would increase at a pace higher than previously estimated at 60,000 in 2013 and 85,000 in 2014 versus 40,000 in 2012. Penetration is expected to gradually improve to up to 57% in the next two years. This expected demand growth is supported by the government initiative to provide incentives to increase gas usage through promotional discounts as well as by its commercial strategy to increase access in new districts through more aggressive CapEx in its secondary grid network. Also, NG's competitive advantage versus alternative fuel sources should boost demand for NG.

Revenues would grow around 20% during the next two years as a result of higher installation services and new gas fired power generators (Fenix Power & Termochilca), which may begin operations in April and July 2013, respectively. Fitch expects Calidda's EBITDA for 2013 to be around USD70 million, up from USD 65 million in 2012, while the new tariff allocation would also bolster EBITDA in 2014.

Concentration on Natural Gas Supply

In order to serve the regulated demand (28.2% of total volumes), Calidda needs to negotiate its gas supply contract. In 2004, Calidda entered into a master supply contract with the Camisea Consortium (mostly interruptible capacity) since 2015 from block 88 with an expiration date in December 2016. Gas supply risk 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. Calidda is currently in negotiations with other producers (Petrobras / Repsol - Block 57) to diversify NG supply and improve commercial agreement terms, including lengthening the contract term and additional firm capacity.

Leverage Increase due to Large Capex for Expansion

Calidda's Gross Debt to EBITDA leverage will increase to 4.9x on a pro forma basis after given effect to the transaction and using 2012 EBITDA. Fitch expects leverage to decrease overtime and to range between around 3.0x and 3.5x in the medium to long term as EBITDA increases. The deleveraging speed would depend on Calidda's ability of promoting and capturing the potential demand.

Nominal debt reduction is not anticipated, since FCF is expected to remain negative in the next years due to Capex. Around USD90 million of Capex has already been invested for an additional 40km of main grid, which will increase the minimum capacity from 255 million CFD to 420 million CFD. Capex would be around USD120 million in 2013, and USD100 million in 2014 mainly directed to the expansion of the secondary grid network.

Manageable Debt Maturity Profile and Liquidity

As of December 2012, total debt was USD197 million including USD 47 million shareholders' subordinated debt. The company expects to use the proceeds from the proposed issuance to repay this debt and to extend debt average life from three to 10 years and remove restricted covenants and over collateralization, i.e. concession mortgage, revenues trustee, shares pledge and debt service reserve account. Additionally, liquidity would be strengthened by Calidda's availability of uncommitted credit lines from banks. Calidda's policy is to maintain at least USD3 million in cash.

Like most growing companies, Calidda has been focused on reinvesting its cash flow generation. As a result of this, the company has not distributed dividends to its shareholders. Calidda expects to pay dividends starting in 2016 of around USD25 million depending on available cash after funding future Capex and maintaining the historic leverage.

Shareholders with Proven Track Record in the Sector

Fitch considers positively that the company is part of Empresa de Energia de Bogota-EEB (60% ownership). The remaining 40% is owned by Promigas. Both companies' Issuer Default Ratings (IDR) are 'BBB-'/Stable Outlook. EEB 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 natural gas transportation and distribution companies in Colombia with international presence in Panama, Peru and Costa Rica. To support the company's growth, shareholders had USD47 million subordinated loan as of December 2012 that would be repaid with the transaction and USD60 million was injected as equity between November 2012 and February 2013.

RATING SENSITIVITIES:

Considerations for a Positive Outlook would be a significant and sustained deleveraging along with the growth and consolidation of the regulated supply and demand (NGV and residential and commercial segments) including a major penetration.

A negative rating action could be taken if leverage, as measured by total debt/EBITDA, increased and remained at a level of more than 3.5x for a prolonged period of time either due to operational deterioration or unexpectedly large dividend distributions.

Material changes in the concession agreement, tariff scheme and applicable regulations would also be considered in future rating actions.

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Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

Applicable Criteria and Related Research:
--'Corporate Rating Methodology' dated Aug. 8, 2012.

Applicable Criteria and Related Research
Corporate Rating Methodology
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=684460