FITCH AFFIRMS CALIDDA'S IDR AT 'BBB-'; OUTLOOK STABLE

Fitch Ratings-New York-05 March 2015: Fitch Ratings has affirmed the local and foreign currency Issuer Default Rating (IDR) of Gas Natural de Lima y Callao S.A (Calidda) at 'BBB-'. The rating action covers the company's international bonds outstanding totaling USD320 million.

The Rating Outlook is Stable.

KEY RATING DRIVERS

Calidda's investment grade ratings reflect the company's strong market position 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 the issuer's diversified client base and predictable and stable cash flow generation, which is supported by a regulated tariff scheme that aims at assuring an adequate return on investment. Calidda's cash flow generation also benefits from expected demand growth based on expected 100,000 client additions per year going forward.

Calidda's leverage of 3.4x Total Debt:EBITDA in the last 12 months (LTM) September 2014 period is in line with its investment grade rating category. Fitch's forecast incorporates expectations for a substantial capex program in the near to medium term along with the start of dividend payments to the company's shareholders starting in 2015. Given these factors, Fitch expects that the company will be able to maintain leverage between 3.5x and 4.0x during the 2015-2018 period.

Predicable and Stable Cash Flow Generation

Calidda's regulated clients (such as natural gas for vehicles [NGV], commercial and residential) and steady growth perspectives provide the company with stable and predictable cash flow generation. The company's regulated tariff scheme, which assures cost recovery and adequate return over total capital investments, further supports cash flow predictability. Additionally, 31% of distribution revenues come from firm take-or-pay contracts with top tier power generators and large industries companies.

For the 12-month period ending September 2014, the company generated USD92 million of EBITDA on USD613 million of revenue (EBTIDA margin: 15.1%). Over 65% of the company's revenues are from pass-through services that carry no profit margin. The remaining revenues are divided primarily between gas distribution and connection fees, approximately 20% and 10% of total revenues, respectively.

Dividends to Begin in 2015

Fitch is projecting that the company will begin paying dividends to its shareholders starting in 2015. Fitch's conservative base case projections incorporate expectations for a 100% payout ratio along with a substantial capex program (approximately USD90 million annually for the next four years). Despite these substantial cash uses, Fitch is projecting that the company's leverage will be in the 3.5x-4.0x level in the short to medium term, which is generally in line with the rating category and with the company's own stated 3.5x leverage target.

Strong Market Position

Calidda is the largest natural gas (NG) distribution company in Peru. It has exclusive rights to distribute natural gas in Lima and Callao, an area that concentrates one third of the country's population and 44% of its GDP. The concession may be renewed upon request by 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.

Highly Strategic Industry for Peru

Natural gas is the second most prominent power source in Peru after hydroelectric energy. The government of Peru, through Law 1999, declared the development of natural gas infrastructure to be of national interest. Since then, the government has promoted the large scale use of gas with medium-term goal of connecting 500 thousand households. As of September 2014, Calidda had connected approximately 234 thousand clients.

Regulated Tariff Scheme Guarantees Return on Investments

The tariff scheme recognizes efficient investments and operating costs applying an annual discount rate of 12%, which guarantees the payment of Calidda's main grid and secondary network expansions. Tariffs are fixed in U.S. dollars by regulator entity OSINERGMIN every four years. Tariffs are also periodically adjusted considering variations in exchange rate, USPPI, Steel Price Index, Polyethylene Price Index and Peruvian Wholesale. A new tariff for the 2014-2018 cycle was approved last year, with a solid average tariff increase of 6.4% over the previous four-year period.

Concentration on Natural Gas Supply

In order to serve its regulated demand, 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. This 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. The company expects to renew the agreement in the short term. Calidda has reached other producers to diversify NG supply and improve commercial agreement terms, including lengthening the contract term and additional firm capacity.

Strong Shareholders with Proven Track Record in the Sector

Calidda's shareowners have strong, investment grade credit profiles. The company's majority shareowner (60%), Empresa de Energia de Bogota (EEB) is rated 'BBB' by Fitch and has an improving credit profile. The remaining 40% of Calidda's shares are owned by Promigas, which is rated 'BBB-'. Both companies have Stable Outlooks.

EEB is a leading energy holding company with interests across the electricity and natural gas sectors in Colombia, Peru and Guatemala. Promigas is one of the largest natural gas transportation and distribution companies in Colombia with an international presence in Panama, Peru and Costa Rica.

RATING SENSITIVITIES

A positive rating action could be triggered by a significant and sustained deleveraging to about 2.0x Total Debt-to-EBITDA. Another positive credit factor would be represented by the continued growth and consolidation of the regulated supply and demand (NGV and residential and commercial segments).

A negative rating action could be taken if leverage, as measured by total debt/EBITDA, increased and remained at a level of more than 4.0x for a prolonged period of time either due to operational deterioration or unexpectedly large dividend distributions.

Material negative changes in the terms of its Build-Own-Operate-Tranfer (BOOT) agreement or its satisfaction of said terms, or changes in the tariff scheme and applicable regulations would also be considered in future rating actions. The inability to secure gas supply for regulated clients, may also impact the rating.

KEY ASSUMPTIONS

Fitch's key assumptions within the rating case for the issuer include:

--Additional Residential & Commercial connections of 100k per year;
--Capex of around USD90 million per year;
--Dividend distributions for 2015 of approximately 100% of Net Income.

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Applicable Criteria and Related Research:
--'Corporate Rating Methodology' (Aug. 5, 2013).

Applicable Criteria and Related Research:
Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage
http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=749393