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## Research Update:

# Empresa de Energia de Bogota 'BBB-' Credit Rating Affirmed; Issue-Level Rating Cut To 'BB+' From 'BBB-' And Off UCO

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## Table Of Contents

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Overview

Rating Action

Rationale

Outlook

Ratings Score Snapshot

Related Criteria

Related Research

Ratings List

## Research Update:

# Empresa de Energia de Bogota 'BBB-' Credit Rating Affirmed; Issue-Level Rating Cut To 'BB+' From 'BBB-' And Off UCO

## Overview

- Financial performance of Colombia-based energy company, EEB, remains in line with our expectations.
- We're affirming our 'BBB-' corporate credit rating on EEB.
- We are removing the UCO designation on EEB's senior unsecured notes due 2021 and are lowering our issue rating on this debt to 'BB+' from 'BBB-'. The rating action on EEB's senior unsecured debt stems solely from the application of our revised issue rating criteria.
- The stable outlook on EEB reflects our view that it will pursue growth opportunities in the region and focus on maintaining debt to EBITDA below 4.5x.

## Rating Action

On Oct. 20, 2017, S&P Global Ratings affirmed its 'BBB-' corporate credit rating on Empresa de Energia de Bogota S.A. E.S.P. (EEB). We also reviewed the senior unsecured issue-level rating on EEB, which we labeled as "under criteria observation" (UCO) after publishing our revised issue ratings criteria, "Reflecting Subordination Risk In Corporate Issue Ratings," on Sept. 21, 2017. With our criteria review complete, we're removing the UCO designation from this rating and are lowering it to 'BB+' from 'BBB-'.

## Rationale

EEB's financial performance for the past 12 months has been in line with our expectation. As we had expected, the group has focused on its internal expansion, which combined with a stable Colombian peso-to-dollar exchange rate and the steady dividend flow from EEB's unconsolidated investments, has allowed it to strengthen its balance sheet and liquidity. The aforementioned factors have allowed the group to regain its financial flexibility. We now expect it to pursue some investment opportunities, particularly outside Colombia. Based on our conversations with management, we expect that funding of these investments would occur through operating cash flow, debt, and third-party equity in order to maintain a pro forma debt to EBITDA below 4.5x.

The rating action on EEB's senior unsecured debt stems solely from the application of our revised issue rating criteria. Our rating action takes into consideration EEB's capital structure, which consists of COP1.042 trillion of

secured debt and COP4.56 trillion of unsecured debt at the operating company level, and COP3.47 trillion of unsecured debt at the holding company level. We have therefore arrived at the following analytical conclusion:

- EEB's notes due 2021 are now at 'BB+', a notch below the corporate credit rating. This debt's class ranks behind a significant amount of secured debt and debt issued by subsidiaries in the capital structure.

The city of Bogota has approved EEB to divest its shares in Grupo Nutresa, Banco Popular S.A., Interconexion Electrica S.A. E.S.P., and Promigas S.A. E.S.P. Therefore, the company has designated these investments as non-core assets, and we believe that it could raise several hundred million dollars in proceeds.

EEB is one of the largest integrated energy groups in Latin America with interests in the natural gas and electricity sectors and operations in Colombia, Peru, Brazil, and Guatemala. Through its subsidiaries and minority investments, the company holds leading positions in most of the markets that it serves, particularly in the cities of Bogota and Lima, which are two of the largest metropolitan areas in Latin America. EEB is the second-largest operator of transmission lines and the largest operator in the gas transportation sector in Colombia. It's the only natural gas distributor in Lima, Peru. This, along with our view that EEB operates under stable and predictable regulatory regimes with an operating efficiency that we view as adequate, supports our assessment of EEB's business risk profile as satisfactory.

For the 12 months ended June 30, 2017, EEB posted debt to EBITDA of 2.8x, funds from operations (FFO) to debt of 25%, and free operating cash flow (FOCF) to debt of 2.6%. Our base-case projections consider the following factors:

- Exchange rate of COP2,922 per \$1 in 2017 and COP2,956 per \$1 in 2018;
- Double-digit revenue growth in 2017 and single-digit growth for the following years, based on our individual forecasts for the company's subsidiaries, Transportadora de
- Gas Internacional S.A. E.S.P. (TGI) and Gas Natural de Lima y Callao S.A. (Calidda).
- Dividends from equity investments of COP710 billion and COP855 billion in 2017 and 2018, respectively; and
- Dividends of COP908.9 billion in 2017 and about COP850 billion expected in 2018.

Based on these assumptions, we arrive at the following credit metrics for 2017 and 2018:

- Debt to EBITDA of 3.3x and 3.5x;
- FFO to debt of 21.9% and 20.7%; and
- Free operating cash flow (FOCF) to debt of -1.9% and -6.8%

## **Liquidity**

We assess EEB's liquidity as adequate based on our view that sources will exceed uses by 1.1x in the upcoming 12 months, and its source-to-uses ratio

will be positive even if EBITDA declines by 10%. All figures are for the next 12 months as of June 30, 2017.

**Principal Liquidity Sources:**

- Cash and equivalents of COP2.24 trillion; and
- Cash FFO of COP1.74 trillion.

**Principal Liquidity Uses:**

- Debt maturities of COP253 billion;
- Capex of about COP1.36 trillion; and
- Dividend distribution for about COP883 billion.

We believe that the company has the ability to absorb high-impact, low-probability events with limited need for refinancing, given that its next major debt maturity is in 2019. We also believe that EEB has satisfactory standing in credit markets and sound relationship with banks. EEB isn't subject to the restricted covenants stipulated in its 144A notes, given that they're rated investment grade by at least two of the three major rating agencies.

### **Group Rating Methodology**

We consider TGI to be EEB's core subsidiary. This reflects our view that it's highly unlikely that EEB would sell TGI, the latter is integral to the group's strategy, and it has a strong long-term commitment from EEB's senior management. Due to the lack of meaningful regulatory mechanisms or other structural barriers that restrict EEB's access to TGI's assets and cash flow, we align the corporate credit rating on TGI with that on the parent. Our stand-alone credit profile (SACP) on TGI is 'bbb-'. We consider Calidda to be a strategically important subsidiary because it's unlikely that EEB would sell Calidda in the near term, the company is important for the group's long-term strategy and senior group management has made a long-term commitment to Calidda. In our opinion, EEB will continue to support Calidda mainly through its business expertise and commitment to prudent financial management. Our SACP on Calidda is 'bbb-'.

### **Government-Related Entity**

Our rating on EEB incorporates our view of a high likelihood that the city of Bogota, (Bogota Distrito Capital; BBB-/Stable/-- ) would provide timely and sufficient extraordinary support to the company in the event of financial distress, given the link between the two entities. In accordance with our criteria for government-related entities, the government's support is based on our assessment of EEB's important role as Bogota's integrated energy provider, very strong link with the government due to its majority shareholder position (76.28%), and the city's influence on the company's strategic and business plans. The city now plans to reduce its ownership in EEB to 56.2% from 76%. This doesn't impact our assessment of likelihood of support, given that Bogota will continue to be the controlling shareholder of EEB.



## Related Criteria

- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, Sept. 21, 2017
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings , April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria - Corporates - Industrials: Key Credit Factors For The Midstream Energy Industry, Dec. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- Criteria - Corporates - Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

## Related Research

- Gas Natural de Lima y Callao S. A. (Calidda) 'BBB-' Ratings Affirmed, Outlook Remains Stable, Feb. 24, 2017
- Transportadora de Gas Internacional S.A. E.S.P. 'BBB-' Ratings Affirmed, Outlook Still Stable, Dec. 22, 2016

## Ratings List

### Downgraded

	To	From
Empresa de Energia de Bogota S. A. E. S. P. Senior Unsecured	BB+	BBB-

### Rating Affirmed

Empresa de Energia de Bogota S. A. E. S. P. Corporate Credit Rating	BBB-/Stable/--
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Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at [www.standardandpoors.com](http://www.standardandpoors.com) for further

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