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Research Update:

Empresa de Energia de Bogota Debt Rating Raised To 'BBB-' From 'BB+'; 'BBB-' Corporate Credit Rating Affirmed

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Overview

- Colombia-based electricity company EEB's financial performance has remained within our expectations.
- We are affirming our 'BBB-' corporate credit rating on EEB, at the same time we are raising our issue-level ratings on its senior unsecured debt to 'BBB-' from 'BB+', which reflects the mitigants of structural subordination of EEB's debt.
- The stable outlook reflects our expectation that EEB's investment strategy will not compromise the company's key financial ratios and that the company will report debt to EBITDA of about 2.9x and FFO to debt of 27% by year end 2014.

Rating Action

On Aug. 28, 2014, Standard & Poor's Ratings Services affirmed its 'BBB-'corporate credit rating on Empresa de Energia de Bogota S.A. E.S.P. (EEB). We also raised our ratings on EEB's senior unsecured debt to 'BBB-' from 'BB+'. The outlook on the corporate credit rating is stable.

Rationale

The rating on EEB reflects its 'bbb-' stand-alone credit profile (SACP) which stems from our view of its "satisfactory" business risk profile. Its financial risk profile remains "intermediate" and its liquidity is "adequate".

The rating also reflects our opinion that there is a high likelihood that the city of Bogota, (Bogota Distrito Capital; BBB-/Stable/--), would provide timely and sufficient extraordinary support to EEB in the event of financial distress given the link between the two entities. In accordance with our criteria for government-related entities (GREs), the government's support is based on our assessment of EEB's important role as Bogota's integrated energy provider, its very strong link with the government due to its majority shareholder position (76.3%), and the city's influence on the company's strategic and business plans.

The rating on EEB's senior unsecured debt reflects the diversity of EEB's assets both geographically and in the industries in which its subsidiaries participate. We believe this provides EEB with greater opportunities for asset dispositions, transfers, or recapitalization of subsidiaries in case of

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financial distress. EEB also has operating assets at the holding company and its debt is fairly concentrated at its subsidiary Transportadora de Gas Internacional S.A. E.S.P. (TGI; BBB-/Stable/--), which are mitigants of its structural subordination.

The company's "satisfactory" business risk profile reflects EBB's strong competitive position mainly due to its low risk regulated businesses and the favorable institutional and regulatory framework in Colombia, where the company generates about 90% of its consolidated EBITDA. The company's satisfactory competitive position reflects its adequate to strong scale, scope and diversification, which mainly reflect its important presence in the Colombian electric and natural gas markets, and its adequate operating efficiency. EEB enjoys moderate geographic and business line diversification in regulated markets, which provide stable and predictable cash flow generation. The company also benefits from a relatively large dividend stream mainly from its minority ownership in Colombian electric companies Emgesa S.A. E.S.P. (BBB/Stable/--) and CODENSA S.A. E.S.P. (not rated) and gas distribution company Gas Natural Fenosa (not rated).

The company's "intermediate" financial risk profile reflects its relatively strong and stable cash flow generation and good financial metrics, "adequate" liquidity and good financial flexibility. We expect the company to report EBITDA interest coverage of about 7.4x, debt to EBITDA of about 2.9x, and funds from operations (FFO) to debt of about 27% by year-end 2014. These ratios consider adjusted debt by subtracting 75% of cash and liquid investments from gross debt and adjusted EBITDA that includes the company's dividend cash flows from its equity investments, Emgesa S.A. E.S.P., CODENSA S.A. E.S.P., Gas Natural Fenosa, Promigas (not rated) and other smaller investments. EEB depends on these dividends as they represent about 47% of its adjusted EBITDA.

Our base case assumes:

- Revenue growth of 28% and 9% in 2014 and 2015; revenue growth is driven mainly by growth at its subsidiaries TGI and Gas Natural de Lima y Callao S.A. (Calidda) (BBB-/Stable/--).
- Gross margins at about 55% in the next two years; and
- Capital expenditures (capex) according to EEB's investment plan for COP900 billion in 2014 and COP930 billion in 2015.

Based on these assumptions, we arrive at the following credit measures for 2014 and 2015, respectively;

- Debt to EBITDA of 2.9x and 2.8x;
- FFO/Debt of 27% for both years; and
- Interest coverage of 7.4 and 5.6x.

We also expect EEB to extend its geographic footprint in Colombia and the rest of the region through acquisitions and greenfield projects. However, this expansion shouldn't affect its overall creditworthiness. We base this assumption on our expectation that any potential expansion would be limited to growth within its areas of expertise. If the company acquires entities that extend its reach in weaker markets, we don't expect these smaller acquisitions to affect the company's business risk profile. We also expect potential acquisitions to maintain a debt to EBITDA ratio of less than 3.0x.

According to our criteria, we assess EEB's financial policy as negative. Our financial policy modifier refines the view of a company's risks beyond the conclusions arising from the standard assumptions in the cash flow/leverage, capital structure, and liquidity analyses. The financial policy assessment is a measure of the degree to which managerial decision-making can affect the predictability of a company's financial risk profile. We believe there is potential for weaker financial ratios beyond our base-case forecast due to the company's aggressive expansion strategy. Nevertheless, we believe this potential increase in debt will most likely maintain the investment grade rating on EEB.

EEB's financial performance has been in line with our expectations. For the 12 months ended June 30, 2014, the company posted an EBITDA interest coverage ratio of 9.0x, debt to EBITDA of 1.9x, and FFO to debt of 45%. During the same period, EEB posted revenues of COP3.1 trillion, which was a 20% increase over the same period in 2013. The EBITDA increase is mainly due to growth at its subsidiaries in Peru and TGI's revenue growth.

EEB is an integrated energy group with interests in the natural gas and electricity sectors, and operations in Colombia, Peru, and Guatemala. The city of Bogota holds 76.2%. of EEB. The majority of EEB's investments are concentrated in natural monopolies regulated by their respective governments. EEB participates directly or indirectly in the transmission, distribution, and generation of energy and in the transportation and distribution of natural gas following its 2007 diversification strategy.

Liquidity

We view the company's liquidity as "adequate." Under our base-case scenario, sources should cover uses by 1.2x in 2014 and by 1.4x in 2015.

Principal Liquidity Sources

- As of June 30, 2014, the company reported cash and short-term investments of approximately COP2 trillion;
- FFO generation of about COP1.5 trillion;
- Dividends from its subsidiaries of about COP860 billion in 2014; and
- Debt issuance as of August 2014 of COP1.6 trillion.

Principal Liquidity Uses

- Working capital outflows of about COP80 billion;
- Capex for COP900 billion;
- Dividend payment of COP590 billion; and
- Acquisition of remaining shares in TGI for COP1.7 trillion.

EEB's 2014 capex will likely be high given its subsidiaries' (Contugas, Cálidda, Trecsa, and TGI) continued expansion and needs at EEB's other transmission projects.

In our view, the tenor of EEB's debt maturity profile mitigates short- and medium-term refinancing risks. The next major maturity, of more than $100 million, is in 2019. The company has raised additional debt to finance its expansion strategy and future capex, because its internal cash flow generation won't be sufficient to cover them. However, we consider the company's expansion capex to be flexible.

Outlook

The stable outlook reflects our expectation that EEB's "intermediate" financial risk profile will remain unchanged. We expect a 28% increase in operating revenue during 2014 and debt-to-EBITDA ratio of about 2.9x and FFO to debt of 27% due to expected high capex and additional debt from the acquisition of TGI's minority stake. We expect leverage ratios to remain the same in 2015 with debt-to-EBITDA ratio of about 2.8x and FFO to debt of 27%. We expect EEB will continue to implement prudent debt management.

Upside scenario

The rating upside is constrained by the rating on its controlling shareholder, the city of Bogotá. We could raise the ratings if the company internally finances capex and dividends, maintains its financial risk profile of intermediate, and we upgrade the city of Bogotá.

Downside scenario

A continued increase in debt from additional acquisitions or capex needs that lead to a deterioration in the company's financial risk profile or which pressure its liquidity, resulting in debt to EBITDA of more than 4.5x and FFO to debt of less than 13%, could lead to a downgrade.

Ratings Score Snapshot

Corporate Credit Rating: BBB-/Stable/--

Business risk: Satisfactory
- Country risk: Moderately high
- Industry risk: Low
- Competitive position: Satisfactory

Financial risk: Intermediate
- Cash flow/Leverage: Intermediate

Anchor: bbb

Modifiers
- Diversification/portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Negative (-1 notch)

- Management and governance: Fair (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb-
- Related government rating: BBB-
- Likelihood of government support: High (no impact)

Related Criteria and Research

Related Criteria
- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Jan. 2, 2014
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Rating Government-Related Entities: Methodology And Assumptions, Dec. 9, 2010
- Rating Each Issue, April 15, 2008

Related Research
- The Credit Outlook On Colombian Electric Utilities Is Stable Amid A Market-Oriented Regulatory Framework, July 21, 2014

Ratings List

Ratings Affirmed

Empresa de Energia de Bogota S. A. E. S. P.	
Corporate Credit Rating	BBB-/Stable/--

Upgraded

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

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