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**Research Update:**

# Empresa de Energia de Bogota S. A. E. S. P. Outlook Revised To Positive From Stable, 'BB+' Credit Rating Affirmed

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## Overview

- Empresa de Energia de Bogotá announced capitalization for up to 1 trillion Colombian pesos (approximately $500 million) and a bond issuance to refinance its $610 million notes due 2014.
- We revised the outlook on the company to positive from stable and affirmed our 'BB+' corporate rating.
- We assigned our 'BB+' rating to EEB's proposed $610 million senior unsecured notes due 2021.
- We expect that EEB will continue to increase its cash flow generation and manage its debt prudently, while consolidating its business strategy and geographical outreach.

## Rating Action

On Oct. 31, 2011, Standard & Poor's Ratings Services revised its outlook on Colombian energy operating holding group Empresa de Energia de Bogotá (EEB) to positive from stable following its ongoing capitalization for up to 1 trillion Colombian pesos (COP) and bond issuance to refinance its $610 million notes due 2014. In addition, we assigned a 'BB+' rating on the company's proposed bond issuance for up to $610 million due 2021. At the same time, we affirmed the 'BB+' corporate credit rating. The outlook revision reflects our view that EEB has shifted its financial policy towards a more prudent use of debt to deleverage its capital structure, and that profitability and cash flow metrics will remain strong in the intermediate term. After the debt issuance is completed, we will withdraw our exisiting 'BB' rating on EEB´s senior unsecured notes due 2014.

## Rationale

The 'BB+' corporate credit rating on EEB 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 current links 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, its very strong link with the government due to its majority shareholder position (81.5%), and the city's influence on the company's strategic and business plans. Upon closing of the equity issuance, we expect that Bogota will remain the majority shareholder with an ownership stake of approximately 75%.

We assess EEB's stand-alone credit profile (SACP) at 'bb+'. EEB's SACP reflects our view that the company continues to improve its financial profile and consolidate its business profile. The company has not only maintained solid cash flow generation and profit margins, but also has adjusted its financial policy towards a more prudent debt management. As part of its business growth strategy, in October 2011, EEB placed equity shares in the domestic market for up to COP1 trillion and announced that it will issue debt to refinance the $610 million unsecured bonds maturing 2014. In our view, these actions reflect a moderating stance of EEB´s financial policy. The company maintains a fair business risk profile based on its core gas transportation operation and power generation and distribution units, via its non-controlled companies Emgesa S.A. E.S.P. (BBB-/Stable/--) and Codensa S.A. E.S.P. (not rated). We expect that the company won't finance its expansion strategy and future capital expenditures through new debt as evidenced by the recent equity issuance. In our view, an asset acquisition via equity is reflective of a more moderate financial policy and suggests a more consistent commitment to credit quality. This compares favorably with the company's highly leveraged financial risk profile, which we previously viewed as aggressive.

EEB´s highly profitable natural gas transportation and hydro-power generation and distribution units are due to a growing electricity and natural gas demand and the company's efficient operating performance. EEB has reported attractive consolidated EBITDA plus dividends margins above 70%, and we expect that the organic growth in EEB's gas transportation business through its consolidated subsidiary Transportadora de Gas Internacional S. A. E.S.P. (TGI; BB/Stable/--) will result in EBITDA plus dividends margins that are in line with its historical trend. In addition, the gas transportation business provides a high degree of stability and predictability to EEB's consolidated revenues, as more than half of its consolidated revenue base comes from fixed-capacity payments with an average maturity of 10 years. Also, the transportation segment's contribution to EBITDA would partially mitigate the revenue volatility of the cyclical or seasonal hydro-power generation and distribution segment. Finally, as the natural gas transportation segment moves forward in its strategy of expanding its system by 56%, EEB will rely less on dividend payments from its non-controlling companies, Emgesa S.A. E.S.P. (BBB-/Stable/--) and Codensa S.A. E.S.P. (not rated).

For the 12 months ended June 30, 2011, EEB's key financial metrics remained within our expectations. In particular, the company posted EBITDA-plus-dividends interest coverage, total debt-to-EBITDA plus dividends, and funds from operations (FFO) plus dividends-to-total debt of 3.2x, 3.6x, and 18%, respectively. We believe that operating income will continue to improve as a result of the consolidation of recently acquired assets and additional revenues from TGI's Cusiana Phase I expansion of its transportation system. Under our base-case scenario, we expect EEB's cash flow generation to increase rapidly during 2011-2013, mainly through its transportation unit, resulting in stronger key financial metrics, such as EBITDA-plus-dividends interest coverage, total debt-to-EBITDA plus dividends, and FFO-plus-dividends to total debt ratios of 5.4x, 2.1x, and 27%, respectively. We expect the key measures of cash flow protection to remain in line with our base-case for EEB before the proposed equity issuance and debt refinancing announcement.

### Liquidity

EEB's liquidity position is adequate. As of June 2011, the company reported cash and short-term investments of approximately $390 million; we expect free operating cash flow of $230 million for the next 18 months, which compares favorably with short-term debt of $70 million. EEB has a smooth debt maturity schedule, with nearly no debt amortization given the recent refinancing of its senior unsecured notes due 2014.

## Outlook

The positive outlook reflects our expectation that EEB will maintain a satisfactory business and operational performance and continue to consolidate its operations and geographic outreach, which should translate into revenues and EBITDA- plus dividends margins of above 65%. In addition, EBITDA-plus-dividends interest coverage, total debt-to-EBITDA plus dividends, and FFO-plus-dividends to total debt should remain approximately 5.4x, 2.1x, and 27% by 2011. However, highly debt-financed expansions that cause the company's financial risk profile to deteriorate and pressure its liquidity, resulting in a consolidated debt-to-EBITDA of more than 4.0x and FFO-to-interest coverage of less than 3.0x, could lead us to revise the outlook back to stable.

## Related Criteria And Research

- Methodology And Assumptions: Standard & Poor's Standardizes Liquidity Descriptors For Global Corporate Issuers, July 2, 2010
- Enhanced Methodology and Assumptions For Rating Government-Related Entities, June 29, 2009
- 2008 Corporate Criteria: Analytical Methodology, April 15, 2008

## Ratings List

Ratings Affirmed; CreditWatch/Outlook Action

| | To | From |
|---|---|---|
| Empresa de Energia de Bogota S. A. E. S. P. | | |
| Corporate Credit Rating | BB+/Positive/-- | BB+/Stable/-- |

New Rating

| | |
|---|---|
| Empresa de Energia de Bogota S. A. E. S. P. | |
| Senior Unsecured | BB+ |

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