

# Fitch Ratings

## Fitch Affirms ISA Capital's IDRs at 'BB+'/'AA-(bra)'; CTEEP's National Scale Rating at 'AA+(bra)'

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Fitch Ratings-Sao Paulo-25 August 2015: Fitch Ratings has affirmed ISA Capital do Brasil S.A.'s (ISA Capital) foreign and local currency Issuer Default Ratings (IDRs) at 'BB+', and its national scale rating at 'AA-(bra)'. In addition, Fitch has affirmed the company's USD31.6 million outstanding senior secured notes at 'BBB-'. The Rating Outlook is Stable.

Concurrently, Fitch has affirmed Companhia de Transmissao de Energia Eletrica Paulista S.A.'s (CTEEP) national scale long-term rating at 'AA+(bra)'. The rating action also applies to its first debenture issuance outstanding of BRL65 million due 2017. The Rating Outlook is Stable.

### KEY RATING DRIVERS

CTEEP's ratings reflect its strong credit quality attributable to the low business risk of the power transmission sector in Brazil, with predictable operating cash flow. The analysis also considered that the company is being efficient to manage its sound financial profile after the strong reduction of revenues consequence of the company's acceptance to early renew its main concession at the beginning of 2013. Fitch views as positive the use of the compensation received for the nondepreciated assets to pay down part of its debt. The ratings factored in a moderate regulatory risk.

ISA Capital's ratings reflect the credit profile of CTEEP, its sole operating asset and dividend source. ISA Capital's obligations are structurally subordinated to CTEEP's. The holding only owns 37.2% of CTEEP's total capital and does not receive the full amount of dividends paid by the transmission company. Fitch considers that ISA Capital's financial flexibility may benefit from the market value of its CTEEP's shares in case dividends received from CTEEP are not sufficient to meet its obligations.

The one-notch rating uplift for ISA Capital outstanding bonds reflects its enhanced recovery prospects due to the refinancing of the majority of its debt with (subordinated, debt like) preferred equity. The 2017 bonds are currently overcollateralized. The USD31.6 million (BRL87.1 million) of outstanding bonds are secured by 66% of ISA Capital's shares on CTEEP, a stake which is currently valued at approximately BRL1.4 billion based on CTEEP's current market cap value of BRL6.55 billion.

### CTEEP's Robust Credit Metrics

Fitch expects CTEEP's financial leverage and liquidity to continuously improve as a result of growing cash generation from a complementary compensation related to the acceptance to early renew its main concession and reinforcement investments related revenue. This additional compensation for the investments made before 2000 is expected to be paid over the remaining life of the new concession. The Brazilian regulatory agency for the power sector (ANEEL) has already signaled a minimum of BRL3.7 billion (as of 2012) as compensation. This amount can reach up to BRL5.2 billion (as of 2012), since the company has asked ANEEL to review its calculations.

For the latest 12 months (LTM) ended June 30, 2015, CTEEP's total adjusted debt (including BRL1.5 billion guarantees to non-controlling subsidiaries) was BRL2.7 billion, leading to total adjusted debt to EBITDA ratio of 7.1x, or 6.0x considering the net adjusted debt. Fitch expects corporate guarantees to non-controlling subsidiaries to be materially released after 2016, when net leverage should remain below 2.5x in the next three years.

### Increasing Operational Cash Flow

CTEEP's cash flow generation is very predictable, exhibiting the low business risk profile of a power transmission company. CTEEP's revenues are exempt from volumetric risk as its maximum permitted annual revenue (PAR) is based on the power transmission assets available to users, instead of the power transmitted. After a significant decrease in cash flow generation due to the company acceptance of the government proposal for early renewal of its main concession, cash flow has been benefited by additional revenues from reinforcement investments. For the LTM ended June 30, 2015, net revenues reached BRL1.2 billion, with EBITDA of BRL366 million, according to Fitch criteria. In 2014, net revenues and EBITDA were BRL1.1 billion and BRL366 million, respectively.

Fitch expects CTEEP's free cash flow (FCF) to turn negative after 2016 due to high CAPEX needs and annual dividends of BRL200 million-BRL230 million, even without additional transmission assets being added to its portfolio. For the LTM ended June 30, 2015, cash flow from operations (CFFO) of BRL324 million was not sufficient to cover capital expenditures of BRL26 million and dividends of BRL366 million leading to a negative FCF of BR67 million. As of June 2015, the company had a forecasted reinforcement capex of BRL1.2 billion until 2017 which associated to formerly realized investments since 2013 are expected to generate an increase of BRL1 billion in revenues until 2018. These investments as well as the revenues (PAR) associated to them shall be previously approved by ANEEL.

### Low Business Risk

Fitch considers the transmission segment as the lowest risk at the Brazilian power sector. CTEEP's credit profile benefits from its exclusive right to provide electricity transmission services through its multiple concessions. CTEEP currently participates in seven concessions in operation with an equivalent participation of 1.826 km. This scenario reduces the company's exposure to the risks associated with the construction phase.

## Structural Subordination

ISA Capital's credit quality reflects the company's structural subordination to CTEEP's obligations. ISA Capital owns only 37.2% of CTEEP's total capital and receives this proportional stake on the dividends paid by the transmission company. ISA Capital is expected to use the proceeds it receives from CTEEP, together with its cash on hand (BRL21 million as of December 2014) to partially pay its debt. At the end of 2014, ISA Capital's debt was BRL929 million, mostly comprised of the remaining portion of its 2017 bonds (BRL87 million) not tendered during 2010 and the obligations to redeem its preferred shares of BRL842 million.

Fitch believes that ISA Capital will have to raise additional cash to meet debt obligations, since dividends flow from CTEEP should not be sufficient. The concession renewal process has somewhat affected CTEEP's ability to upstream cash to its controlling shareholder through dividend payments. Annual dividends from the transmission company are expected to range from BRL200 million to BRL230 million. In 2014, in order to adjust its preferred share buying program to this new reality, ISA Capital renegotiated with the preferring shareholders the program repurchase schedule. The program of acquiring the BRL891 million of preferred shares has been extended to 2020 and the balance is BRL50 million in 2015 and BRL160 million per year from 2016 to 2020.

## KEY ASSUMPTIONS

Fitch's key assumptions within the rating case include:

- Payout dividend ratio of around 60% in 2015 and an average of 65% between 2016-2018;
- Annual average capex of BRL473 million between 2015-2018;
- Corporate guarantees to non-controlling subsidiaries fully released until the end of 2016.

## RATING SENSITIVITIES

Future developments that may individually or collectively lead to a negative rating action at CTEEP includes:

- Net leverage consistently above 3.5x;
- CFFO + Cash and equivalents/short-term debt ratio below 1.5x.

In the case of ISA Capital, a strong devaluation of CTEEP's value and a difficult scenario to negotiate a new schedule to redeem its preferred shares can pressure the ratings.

A positive rating action is unlikely until corporate guarantees to non-controlling are materially released.

## LIQUIDITY

CTEEP's financial profile benefits from its robust liquidity position. As of June 30, 2015, as per Fitch methodology, cash and cash equivalents of BRL397 million represented 15% of total adjusted debt of

BRL2.7 billion and were sufficient to cover short-term debt of BRL105 million by 3.8x. Liquidity should improve based on the pending BRL593 million to be received in 2015 from the initial compensation of BRL2.9 billion and the potential BRL3.7 billion from the complementary compensation to be approved by the regulator. CTEEP also presented a comfortable short-term debt coverage when considered the (CFFO + cash and cash equivalents)/short-term debt at 6.9x.

#### FULL LIST OF RATING ACTIONS

Fitch has affirmed the following ratings:

Companhia de Transmissao de Energia Eletrica Paulista S.A. (CTEEP)

--National Scale Rating at 'AA+(bra)';

--National Scale Rating Debentures 1st issuance of outstanding BRL65 million due in 2017, at 'AA+(bra)'.

ISA Capital do Brasil S.A. (ISA Capital)

--Local Currency and Foreign Currency Issuer Default Ratings (IDRs) at 'BB+';

--National Scale Rating at 'AA-(bra)';

--Senior secured notes outstanding USD31.6 million at 'BBB-'.

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Date of Relevant Rating Committee: Aug. 24, 2015.

Additional information is available on [www.fitchratings.com](http://www.fitchratings.com).

### **Applicable Criteria**

Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage (pub. 17 Aug 2015) ([https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=869362](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=869362))

National Scale Ratings Criteria (pub. 30 Oct 2013)

([https://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=720082](https://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=720082))

### **Additional Disclosures**

Dodd-Frank Rating Information Disclosure Form

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