

**RATING ACTION COMMENTARY**

# Fitch Affirms Interconexion Electrica at 'BBB'; Outlook Stable

Wed 13 Apr, 2022 - 2:09 p. m. ET

Fitch Ratings - New York - 13 Apr 2022: Fitch Ratings has affirmed Interconexion Electrica S.A. E.S.P.'s (ISA) Long-Term Foreign and Local Currency Issuer Default Ratings (IDRs) at 'BBB' with a Stable Outlook. Fitch has also affirmed ISA's USD330 million senior unsecured note due 2033 at 'BBB' as well as its local bond and CP program ratings at 'AAA(col)' and 'F1+(col)', respectively, with a Stable Outlook.

ISA's ratings reflect the company's low business risk profile, a characteristic of the power transmission business. The ratings incorporate the strong geographic and business diversification of its revenue, which, along with the high predictability of cash flow from operations (CFO), translates into a strong financial profile. ISA's ratings also reflect its adequate liquidity position and aggressive growth strategy. Fitch considers ISA's business and financial profile strong enough to be rated two notches above its owner, Ecopetrol (BB+/Stable). A negative rating action on Ecopetrol's ratings would impact ISA's ratings to preserve the two-notch differential.

**KEY RATING DRIVERS**

**Low Business Risk Profile:** ISA's low business risk profile stems from its participation in regulated natural monopolies with no demand risk, as well as its geographic diversification across six countries in Latin America. During 2021, around 60% of the company's consolidated revenues came from Colombia and Brazil. Peru and Chile made up 38.6%, excluding construction activity. The electricity transmission business, which historically has represented the bulk of ISA's consolidated cash flow generation, contributed 81.8% of EBITDA during the 2021, excluding construction activity.

**Highly Predictable CFO:** ISA's CFO stability benefits from its strong and diversified portfolio of energy transmission assets, along with its participation in other businesses that have limited demand risk. ISA's energy transmission business is not exposed to volume risk, as its revenues are not dependent on the amount of energy transported but on the availability of the transmission lines. In the road concession business, the second largest business for ISA, the company operates one concession in Colombia (Ruta Costera) and four concessions in Chile that incorporate a compensation mechanism that either extends the concession period (Maipo, Bosque, Araucania) or offers a minimum income guarantee (Rios) should the concessions register low traffic volumes.

**Manageable Regulatory Risk:** ISA's businesses and geographic diversification effectively hedge its exposure to regulatory risk, as the vast majority of its revenues are regulated. The company's cash flow generation exhibits resilience against some adverse regulatory scenarios. The analysis incorporates the upcoming regulatory reset in the electricity transmission tariff in Colombia. Although there is limited visibility on the final tariff scheme that will be approved in Colombia, Fitch does not believe the final outcome will result in material pressure on ISA's financial metrics. This is due to the fair and balanced nature of the local regulation as well as the limited portion of the company's consolidated revenues exposed to a new regulatory change.

**Aggressive Growth Strategy:** ISA's growth strategy is based on its active participation in bidding for energy transmission and other infrastructure projects, as well as inorganic growth through acquisitions. ISA's long-term goal is to reach COP8.6 trillion in EBITDA by 2030, as well as invest USD10.5 billion in current businesses and geographies as well as in new geographies, of which 27% has been executed. Fitch expects the company's FCF to continue to face pressure over the next two years as ISA's most recent consolidated capex plan for 2022-2026 implies investments of around COP12.7 trillion, mostly concentrated in 2022-2023 in projects in Brazil, Colombia and Chile.

**Adequate Credit Metrics:** ISA's credit metrics reflect solid cash flow generation, moderate debt levels and adequate liquidity. Fitch forecasts the company's leverage will increase to 4.3x by YE 2022, returning below 4.0x from 2023, considering only current projects

underway and the scheduled start of new projects over the next few years. This leverage is commensurate with ISA's ratings, given the stability and predictability of its cash flow generation. The company's aggressive growth strategy is not expected to affect ISA's credit metrics. As of Dec. 31, 2021, ISA's leverage increased to 3.9x, given the higher indebtedness to fund the capex and the acquisitions made during the year.

**Standalone Credit Profile:** ISA's credit profile is commensurate with its current 'BBB' rating and not capped by the credit profile of its controlling owner, Ecopetrol. Fitch considers the presence of regulatory ring-fencing mechanisms, material minority shareholders and a track record of strong governance practices diminish the parent's capacity to extract value from its stronger subsidiary. ISA continues to be managed with independency and autonomy which is positively incorporated in the ratings. Under Fitch's Parent-Subsidiary Rating Criteria, the assessment of these factors allows Fitch to rate ISA two notches above Ecopetrol's consolidated profile.

Fitch has the expectation that ISA will maintain its operational independence and dividend distribution practice, which has historically been approximately 50% of its net income. A change in ISA's corporate governance, business or financial strategy may put downward pressure on the company, particularly in the event of a structural increase in its dividend payout ratio.

**Applicable Country Ceiling:** ISA's applicable Country Ceiling is Peru which is BBB+, as the cash flow generated by its Peruvian subsidiaries are sufficient to cover HC gross interest expense in Fitch's forecast horizon. Therefore, a lowering of Peru's Country Ceiling has the potential to affect ISA's ratings, particularly in a multiple-notch downgrade scenario.

## **DERIVATION SUMMARY**

ISA's credit profile compares with peers in the region, such as Transelec S.A. (BBB/Stable), Consorcio Transmantaro S.A. (CTM: BBB/Stable), Empresa de Transmision Electrica, S.A. (ETESA: BBB-/Stable), Alupar Invertemiento S.A. (Foreign Currency IDR: BB; Local Currency IDR: BBB-/Negative), and Transmissora Alianca de Energia Eletrica S.A. (Taesa; Foreign Currency IDR: BB; Local Currency IDR: BBB-/Negative). All of these companies benefit from a low business risk profile and predictable cash flow generation.

ISA is rated at the same level as Transelec and CTM, even though ISA's credit profile benefits from a larger and more diversified operation, as well as from a more conservative capital structure. ISA's ratings are constrained by the linkage between the company and Ecopetrol (BB+/Stable). As per Fitch's methodology, a stronger subsidiary can be rated a maximum of two notches above the consolidated profile if a weak linkage is established.

Compared with ETESA, Taesa and Alupar, ISA's higher rating is mainly a result of its geographic diversification. Most of ISA operations are namely located in Colombia, Brazil, Chile and Peru, while Taesa's and Alupar's operations are concentrated in Brazil and their ratings are negatively impacted by the Country Ceiling of Brazil (BB). ETESA's ratings reflect its strong ties with the Panamanian government and linkage to the sovereign (BBB-/Stable).

ISA is also well positioned among the national peers that participate in the electricity transmission business, such as Grupo Energia Bogota S.A. E.S.P. (GEB; BBB/Stable) and Empresas Publicas de Medellin E.S.P. (EPM; BB+/Rating Watch Negative). Together, these companies own and operate the vast majority of the electricity transmission network in Colombia. ISA's and EPM's credit profiles benefit from a higher business and geographic diversification, as well as limited dependence on dividends received from their noncontrolling stakes within their CFO structure. ISA's cash flow generation is stronger given its predictability, while EPM's Rating Watch Negative reflects the uncertainty related to the development of its key project, Ituango.

## **KEY ASSUMPTIONS**

- Revenue and EBITDA projected for 2022-2025 incorporate the development of projects already granted;
- Changes in the regulatory remuneration of the power transmission business in Colombia with neutral effect;
- Electricity transmission business continues to account for more than 70% of ISA's consolidated revenues over the rating horizon;
- Capex for the next several years reflects the construction stage in new projects awarded to the company and subsidiaries;
- Dividend distributions of 50% of the previous year's net income.

## **RATING SENSITIVITIES**

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- Although a positive rating action is unlikely in the short to medium term given the company's credit metric expectations and its growth strategy, one may be considered if total consolidated leverage is below 2.5x.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--A sustained increase in leverage above 4.5x on a consolidated or nonconsolidated basis, as a result of a progressive deterioration in cash generation, or increased debt levels above Fitch's base case scenario;

--Regulatory changes that put significant pressure on ISA's cash flow generation;

--A change in the company's business and financial strategy, particularly with regards to dividends distribution practices, as well as changes in corporate governance practices;

--A negative rating action on Ecopetrol;

--A multi-notch downgrade of Peru's Country Ceiling.

## **BEST/WORST CASE RATING SCENARIO**

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit <https://www.fitchratings.com/site/re/10111579>.

## **LIQUIDITY AND DEBT STRUCTURE**

Adequate Liquidity: Fitch considers ISA's liquidity adequate and characterized by healthy cash on hand, strong and predictable CFO, manageable debt amortizations and strong access to local and international capital markets. As of YE 2021, ISA had approximately COP4.7 trillion of cash on hand to service COP2.9 trillion of short-term debt. At the holding company level, cash on hand totaled COP546 billion and short-term debt COP158 billion.

ISA's maturity profile is manageable, as its long-term debt amortization schedule is spread until 2056. At the holding company level, ISA's debt maturities for 2022 were comprised of local bond issuances, which is manageable. At the consolidated level, ISA will continue to record negative FCF in 2022-2023 given the required capex of around USD2 billion in awarded projects. The recent USD330 million senior unsecured notes allowed the company to partially refinance outstanding debt and strengthened its financial flexibility.

## **ISSUER PROFILE**

ISA is a Colombian holding company that, directly and through its 48 affiliates and subsidiaries, focuses its activities on energy transmission, road concessions, telecommunication and ICT (Information and Communications Technology). The company has operations in six countries in Latin America.

## **SUMMARY OF FINANCIAL ADJUSTMENTS**

--Restricted cash was excluded from the cash and equivalents.

--EBITDA adjusted by the cash component of the RBSE revenues.

## **REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING**

The principal sources of information used in the analysis are described in the Applicable Criteria.

## **PUBLIC RATINGS WITH CREDIT LINKAGE TO OTHER RATINGS**

ISA is rated two-notches above Ecopetrol's consolidated profile (BB+/Stable). A change in Ecopetrol's credit profile has the potential to affect ISA's ratings.

## **ESG CONSIDERATIONS**

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit [www.fitchratings.com/esg](http://www.fitchratings.com/esg).

## RATING ACTIONS

ENTITY / DEBT	RATING	PRIOR
<input type="text"/>	<input type="text"/>	<input type="text"/>
Inte conexion Elect ica S.A. E.S.P.	LT IDR BBB Affi med	BBB
enio un ecu ed	LT BBB Affi med	BBB
enio un ecu ed	Natl LT AAA(col) Affi med	AAA(col)
enio un ecu ed	Natl ST F +(col) Affi med	F +(col)

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### APPLICABLE CRITERIA

[Non-Financial Corporate Exceeding the Country Ceiling Rating Criteria \(pub. 8 Jan 2022\)](#)

[Corporate Rating Criteria \(pub. 5 Oct 2022\) \(including rating assumption sensitivity\)](#)

[Parent and Subsidiary Linkage Rating Criteria \(pub. Dec 2022\)](#)

### APPLICABLE MODELS

Number in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

[Corporate Monitoring & Forecasting Model \(COMFORT Model\), v8.02](#)

### ADDITIONAL DISCLOSURES

[Dodd-Frank Rating Information Disclosure Form](#)

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### ENDORSEMENT STATUS

Inte conexion Elect ica S.A. E.S.P.

EU Endorsed, UK Endorsed

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