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Tagging Info

Fitch Affirms Emgesa's IDR at 'BBB'; Outlook Stable

Ratings Endorsement Policy

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Fitch Ratings-Chicago-07 May 2015: Fitch Ratings has affirmed the foreign and local currency Issuer Default Ratings (IDRs) for Emgesa S.A. E.S.P. (Emgesa) at 'BBB'. This rating applies to the company's senior unsecured COP736.760 million notes due 2021. Fitch has also affirmed Emgesa's long-term national scale rating and debt ratings at 'AAA(col)'. The Rating Outlook is Stable. A full list of debt ratings follows at the end of this release.

KEY RATING DRIVERS

Emgesa's ratings reflect the company's strong business model, supported by its assets diversification and solid competitive position. The company maintains a robust cash flow generation, which underpins Fitch's expectations of a moderate financial leverage amid an intensive capital expenditures program. Also factored into the ratings are the positive expected cash flows that will result after El Quimbo's completion during 2015 and the Emgesa's strategic importance to Enel Group.

Solid Business Position
Emgesa's ratings are supported by the company's business position as one of the largest generation companies in Colombia (based on installed capacity and electric generation). At end of 2014, the company had 19.1% of Colombia's total installed generation capacity and accounted for 21.2% of the country's total generation. The combination of Emgesa's low marginal cost hydro-electric generating based, along with its complementary watershed and some thermal generating capacity (85.5% hydro and 14.5% thermal), make the company less exposed to severe weather conditions and hydrology risk.

Strong Operational Results
Emgesa's commercial strategy matches its business profile and operating assets, which provides more revenue predictability coupled with strong and stable EBITDA margins. The company's commercial strategy has aimed at selling around 70% of its volume at contracted prices for a one- to three-year term. Revenues coming from reliability charge also contribute with the stability of cash generation.

Although the energy generation business is more vulnerable to changes in hydrology and in prices of both energy and fuel, Emgesa's administration has demonstrated strong and conservative management, which has achieved to maintain EBITDA margins within a range of 59%-66%. In 2014, the company took advantage of favorable rainfall conditions where its facilities are located, along with historically high prices in the spot market in order to boost its revenues and EBITDA. Ratings incorporate the expectations that the company will maintain a solid cash flow operation, with EBITDA margin around 60%.

Leverage is Still Moderate
Fitch expects Emgesa will maintain leverage within acceptable levels for the current rating category, even considering higher pressures in free cash flow (FCF) generation during 2015. The company recently announced new cost overruns in El Quimbo hydroelectric project (400Mw) mostly explained by social and environmental costs. Emgesa adjusted its construction budget upwards by approximately 12.6% compared to the last budget revision last year, to reach USD1.231 billion, including contingencies, which will be financed with additional debt. The company expects to start operations of this new facility during the second half 2015, which will consolidate Emgesa as the second largest generator in Colombia, with an installed capacity of 3,459Mw.

At end of 2014, the company reported COP3.7 trillion in financial debt, with a moderate leverage ratio, as measured by total debt-to-EBITDA of 2.2 times (x). Fitch expects that the additional capex projected for El

Quimbo will take leverage up to around 3x at end of 2015. Following Quimbo's start of commercial operations in late-2015, leverage is expected to decrease to a range of 2.5x to 3x from 2016.

Robust Liquidity Position
Emgesa maintains strong liquidity levels, supported by a sound cash generation, high cash balance and a manageable debt payment schedule. At end of 2014, the company closed with a cash balance of COP960 billion and positive FCF generation, while short-term debt stood at COP356 billion. Excluding short-term debt, the next sizable debt payment amortization the company faces is in 2017 for approximately COP211 billion.

Fitch considers refinancing risk as low, given the moderate leverage levels and the manageable debt profile, which compensate the pressures in the FCF generation expected during 2015. In addition, the company has available credit lines of COP1.794 trillion and proven access to local and international capital markets, which reinforce its liquidity position. The company's long-term debt of COP3.390 trillion is mainly composed of local bond issuances with maturities between 2015 and 2030. The company's balance sheet is not exposed to foreign exchange volatility since 100% of its debt is denominated in local currency.

Emgesa's modest leverage together with solid cash generation has allowed the company to historically present dividend pay-out-ratio of 100%, which is considered high, yet manageable.

Strategic Importance for Shareholders
Emgesa is indirectly controlled by Enel S.p.A.(IDR 'BBB+' Outlook Stable), through Endesa's subsidiary Enersis (IDR 'BBB+' /Outlook Stable) and Endesa Chile (IDR 'BBB+'/Outlook Stable), which together control the company and have a 48.5% economic interest in the company and 56.5% of voting rights. Endesa's relationship with Emgesa is considered positive because of the transfer of know-how, technology integration and business practices. Emgesa is a sizable asset for Enel and represents 38% of Enel's EBITDA of the generation assets in Latin America.

Despite not having the control of Emgesa, Empresa de Energia de Bogota S.A. ESP. (EEB; 'BBB' IDR) also participates in the company, with 51.5% of economic rights and 43.6% of voting rights. EEB also owns non-controlling majority participation in the electric distribution company Codensa, and a controlling participation in Colombia's largest natural gas pipeline transportation company, Transportadora de Gas International.

KEY ASSUMPTIONS

Fitch's key assumptions within the rating case for the issuer include:

--Revenues incorporate the start of the operation of El Quimbo in the second half 2015, as well as a reduction in prices in the medium term dragged by a slower demand and the planned capacity increase. Revenues also reflect a revenues mix of 70% by contract sales and the balance in the spot market.
--EBITDA margin remains above 60%.
--CAPEX incorporate the final disbursement of El Quimbo, including the cost overrun already announced by the company

RATING SENSITIVITIES

Fitch considers a positive rating action unlikely in the near term. However, a material improvement in credit metrics that could be sustained over time and more conservative dividend policy would be seen as positive to the credit.

On the other hand, the main factors that individually or collectively could lead to a negative rating action are:

--A steep decrease in electricity prices, coupled with low generation and poor electricity demand;
--A sustained increase in leverage above 3.5x as a result of investments in El Quimbo project;
--Additional delays in the completion of El Quimbo project that put pressure on the cash flow generation of the company;
--A change in the company's strategy that results in a more aggressive one in terms of leverage and capital expenditures.

Fitch affirms Emgesa's debt ratings as follows:

--COP 3.065 trillion bond program at 'AAA(col)';

--COP736.760 million notes due 2021 at 'BBB'.

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Additional information is available at 'www.fitchratings.com'.

Applicable Criteria and Related Research:
--'Corporate Rating Methodology', May 28, 2014.

Applicable Criteria and Related Research:
Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage

Additional Disclosure
Solicitation Status