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Despite Large Investments, Winning Auction Bids Among Four Rated Brazilian Utilities Won't Impair Their Credit Metrics

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SAO PAULO (S&P Global Ratings) Dec. 20, 2018--the Brazilian electric power regulator Agencia Nacional de Energia Eletrica - ANEEL auctioned today 16 transmission lines for R$1.2 billion in annual availability-based revenues, which are annually adjusted to inflation.

Among the winners, there are four entities that S&P rates: CPFL Energia S.A. (CPFL), Energisa S.A. (Energisa), Neoenergia S.A. (Neoenergia), and Transmissora Alianca de Energia Eletrica S.A. (Taesa). In general, we believe these companies will benefit from a wider diversification of revenues and the stable and predictable availability-based cash flows from the transmission segment. As part of the auction conditions, the four companies must invest R$8.1 billion, which we expect to mostly occur between 2021 and 2023, and could temporarily weaken their credit metrics. However, given the investments' amount and concentration, we expect a quick deleveraging once the cash flows of these assets come on stream. We don't expect any impact on liquidity either, because according to the conditions of the auction, the companies will have five years to complete building the lines and begin their operations, after the signing of the concession contracts, which we expect to happen in mid-2019.

Selected Indicators Of The Winning Bidders

	Global scale rating	Brazil national scale rating	Number of assets awarded	Extension (km)	Capex (mil. R$)*	Annual revenues (mil. R$)
CPFL Energia S.A.	--	brAAA/Stable/--	2	405	714.9	60.3
Energisa S.A.	BB-/Stable/--	brAAA/Stable/--	1	772	699.4	62.9
Neoenergia S.A.	BB-/Stable/--	brAAA/Stable/brA-1+	4	3,000	6,091.30	501.2
Transmissora Alianca de Energia Eletrica S.A.	BB-/Stable/--	brAAA/Stable/brA-1+	1	587	610.4	59
Others	--	--	8	2,387	5,058.90	474.5
Total	--	--	16	7,152	13,174.90	1,157.80

*According to ANEEL's estimates.

Finally, the sovereign ratings on the Federative Republic of Brazil (global scale: BB-/Stable/B; national scale: brAAA/Stable/--) currently cap the credit quality of these. However, their stand-alone credit profiles are higher than the sovereign rating, which gives a cushion to the ratings.

- CPFL: We don't consider the amount of the required investments to be considerable compared with the group's already robust investment plan (especially in the distribution segment). Therefore, they shouldn't impair CPFL's financial metrics. Moreover, CPFL could benefit from the support from its controlling shareholder, State Grid China Co., Ltd (A+/Stable/--), if intrinsic credit quality of the former falls below the sovereign level.
- Energisa: We also don't expect these investments to erode the company's currently comfortable credit metrics.
- Neoenergia: The group was the largest winner of the auction. It already has a very robust investment plan to perform, especially in its four electricity distribution companies. Although we acknowledge that the investments in the transmission segment could put some pressure on its credit metrics, we don't expect ratings to fall below the sovereign level because of the potential extraordinary support from its controlling shareholder, Iberdrola, S.A. (BBB+/Stable/A-2).
- Taesa: In addition to the today's awarded assets, on Dec. 17, 2018, the company announced the acquisition of four transmission lines (two of which with a 51% stake) for R$942.5 million, which will bring estimated revenues of R$130 million and EBITDA of R$100 million. The addition of the new concession and the acquisitions to the company's committed large investment program will in aggregate stretch its credit metrics, although not enough to change our assessment on the company´s financial risk profile at this point. For the next few years, we expect Taesa's funds form operations to Debt above 13% and debt to EBITDA of 4.0-4.5x. Taesa's latest acquisition is subject to some conditions precedent, including approvals by its shareholders, ANEEL, and the Brazilian anti-thrust

authority (CADE).

This report does not constitute a rating action.