

Fitch Affirms Taesa at 'BB'/'AAA(bra)'

Fitch Ratings-Sao Paulo-27 August 2018: Fitch Ratings has affirmed Transmissora Alianca de Energia Eletrica S.A.'s (Taesa) Foreign Currency (FC) and Local Currency (LC) Issuer Default Ratings (IDRs) at 'BB' and 'BBB-', respectively. Fitch has also affirmed the Long-term National Scale Rating 'AAA(bra)' for Taesa and its senior unsecured debenture issuances. The Rating Outlook is Stable. A full list of rating actions follows at the end of this release.

Taesa's ratings reflect its low business risk relative to its strong and diversified portfolio of power transmission assets, with predictable and robust cash flow generation and high operating margins. In addition, none of the 35 concessions that it participates expire before 2030, which gives sustainability to its operations. The analysis also incorporates Fitch's expectation that the company will keep a solid financial profile in the medium term, with credit metrics strong for the existing IDRs when compared to its peers in Latin America. On a pro forma consolidated basis, Taesa presents low leverage for a company within the power transmission sector, as well as an adequate liquidity profile. Taesa's FC IDR is capped by the country ceiling, and Fitch considers a three-notch difference between the company's LC IDR and the sovereign IDR (BB-/Stable) as appropriate for a regulated sector.

Taesa's ratings are not constrained by the credit quality of one of its shareholders, Companhia Energetica de Minas Gerais (Cemig) (LC and FC IDRs B/Stable), since Cemig shares the company's control with Interconexão Eletrica S/A E.S.P. (ISA) (LC and FC IDRs BBB+/Stable), and its access to Taesa's cash is limited to dividends. The moderate regulatory risk of the Brazilian power sector was considered, and Fitch views the risks associated with the construction phase of eight projects under development as manageable.

KEY RATING DRIVERS

Low Business Risk: Taesa's ratings are based on the low business risk of its asset portfolio and no exposure to concession renewals over the short to medium term. Taesa is one of the largest power transmission companies in Brazil, with 9.3 thousand km of transmission lines across the country, with 1.5 thousand km under construction, considering proportional participation in the concessions. The company participates in 35 concessions, including 15 fully owned, which dilutes potential operational risks. Taesa benefits from a diversified client base and guaranteed payment structure.

Leverage to Remain Low: Fitch expects Taesa to maintain its consolidated net financial leverage below 3.5x in the coming three years, which may temporarily go above this level in case of new relevant acquisitions or greenfield projects. The company was able to manage historically low consolidated leverage in the last five years despite substantial dividend payments and significant acquisitions. For the latest 12 months (LTM) ended June 30, 2018, Taesa reported total debt/EBITDA of 2.1x and net debt/EBITDA of 1.6x, based on regulatory accounting rules and proportional consolidation of all transmission assets Taesa participates in directly or indirectly. Considering IFRS accounting rules and Fitch's criteria, those ratios were 2.8x and 2.1x, respectively.

Predictable Revenues and High Margins: Taesa's credit profile benefits from highly predictable power transmission revenues, which are based on lines availability, rather than volume transported. EBITDA margin should be at the range 80%-90% in the coming years despite of the gradual higher impact of around BRL200 million on revenues until 2023 from the 50% PAR reduction for some assets once the 15th year of operation is completed. Fitch's base case scenario considers an EBITDA of BRL1.3 billion in 2018, declining to BRL1.2 billion in 2021, compared to BRL1.5 billion in 2017, on a regulatory basis. The company should resume its consolidated EBITDA growth in 2022 due to additional contribution on revenues and dividends received coming from the conclusion of the projects under development. Taesa's proportional stake on these projects' PARs corresponds to BRL584 million.

Negative FCF on Investment Cycle: Fitch believes Taesa will present a positive free cash flow (FCF) of around BRL160 million in 2018, reverting to a negative annual average of around BRL300 million from

2019 to 2021. The negative FCF in this period reflects the forecasted PAR reduction, higher investments related to the 8 new projects and a strong dividends pay-out ratio corresponding to 91% of net income. Fitch considers that on a consolidated basis Taesa will have a cash need of BRL1.5 billion for capex from 2018 to 2021, increasing to BRL2.3 billion when adding-up capital injections in non-consolidated companies. In accordance with IFRS accounting rules, CFFO and FCF were BRL1.1 billion and BRL443 million, respectively, for the LTM ended June 30, 2018, after BRL669 million in dividends paid.

DERIVATION SUMMARY

Taesa has a stronger financial profile compared to its peers in Latin America, such as Interconexión Eléctrica S.A. E.S.P. (ISA, LC and FC IDR BBB+/Stable); Transelec S.A. (Transelec, LC and FC IDR BBB/Stable) and Consorcio Transmataro S.A. (CTM, LC and FC IDR BBB-/Stable). All of them have low business risk profiles and predictable cash flow generation, which is a characteristic of the power transmission companies operating in a regulated industry. The main differentiation in the IDRs of these companies is the country where their main revenues are generated and the location of their assets. While its peers are located in investment grade countries, Taesa's ratings are negatively impacted by the country ceiling of Brazil at 'BB'.

KEY ASSUMPTIONS

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

- PARs adjusted considering inflation and, in some cases, 50% reduction when the 15th operational year is completed;
- Operational expenses adjusted by inflation;
- Minimum cash of BRL200 million;
- Dividends corresponding to 91% of net income;
- No new acquisition or greenfield projects.

RATING SENSITIVITIES

Future Developments That May, Individually or Collectively, Lead to Positive Rating Action

- A positive rating action for the company's IDRs depends on an upgrade of Brazil's sovereign rating.

Future Developments That May, Individually or Collectively, Lead to Negative Rating Action

- Deterioration in Taesa's consolidated financial profile, with net leverage going above 3.5x on a sustainable basis;
- Negative rating actions on Brazil's sovereign rating will result on a downgrade of Taesa's IDRs.

LIQUIDITY

Liquidity Improved: Fitch expects Taesa to keep a robust liquidity profile, benefited from its robust CFFO and ample access to bank credit lines and capital market. By the end of June 2018, the cash and marketable securities, not considering the non-consolidated companies under IFRS, amounted to BRL805 million as per Fitch's calculations and short-term debt was BRL471 billion, representing a coverage of 1.7x against 0.7x at the end of June 2017. The seven-year debenture issuance of BRL526 million concluded in July 2018 and the cash position are important to fund the equity contribution in projects and the expected negative FCF from 2019 to 2021 on.

Taesa's consolidated debt is characterized by a manageable maturity profile and no foreign exchange risk. As of June 30, 2018, the company's pro forma debt was BRL3.6 billion, considering its proportional stake in all subsidiaries, or BRL3.2 billion by the IFRS consolidation rule and Fitch's adjustments. The BRL3.2 billion debt was mainly composed of debentures (BRL2.7 billion). According to Fitch's methodology the debt on the IFRS accounting rule also includes off-balance sheet debt of BRL5.7 million related to guarantees provided to non-consolidated companies.

FULL LIST OF RATING ACTIONS

Fitch has affirmed the following ratings:

Transmissora Alianca de Energia Eletrica S.A.

--Foreign Currency IDR at 'BB', Outlook Stable;

--Local Currency IDR at 'BBB-', Outlook Stable;

--Long-term National Scale Rating at 'AAA(bra)', Outlook Stable;

--BRL2,160 million third senior unsecured debenture issuance at 'AAA(bra)';

--BRL543 million fourth senior unsecured debenture issuance at 'AAA(bra)'.

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Date of Relevant Rating Committee: Aug. 24, 2018

Summary of Financial Statement Adjustments - Fitch adjusts Taesa's financial statement not considering the construction revenues and costs in its income statement.

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Additional information is available on www.fitchratings.com. For regulatory purposes in various jurisdictions, the supervisory analyst named above is deemed to be the primary analyst for this issuer; the principal analyst is deemed to be the secondary.

Applicable Criteria

Corporate Rating Criteria (pub. 23 Mar 2018)

National Scale Ratings Criteria (pub. 18 Jul 2018)

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ISSUERS

Transmissora Alianca de Energia Eletrica S.A.

ISSUER CONTENT

Fitch Downgrades Various Brazilian Corporates

Fitch 2018 Outlook: Latin American Electric-Corporates (Stability Amid Increased Participation from Renewables)

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SECTOR CONTENT

Codensa S.A. E.S.P.

South Carolina Electric & Gas Co. (Subsidiary of SCANA Corporation)

Indianapolis Power & Light Co. (Subsidiary of IPALCO Enterprises, Inc.)

Companhia Paranaense de Energia - Copel & Subsidiárias

Albanesi S.A.

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RATINGS KEY OUTLOOK WATCH

Positive

Negative

Evolving

Stable

Premium Content

* Long Term/Short Term Issuer Default Rating displayed in orange denotes EU Unsolicited and Non-Participatory Ratings

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