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Research Update:

Transmissora Alianca de Energia Eletrica 'BBB-' Global Scale And 'brAAA' National Scale Ratings Affirmed; Outlook Stable

Primary Credit Analyst:
Marcelo Schwarz, CFA, Sao Paulo (55 11) 3039-9782; marcelo.schwarz@standardandpoors.com

Secondary Contact:
Sergio Fuentes, Buenos Aires (54) 114-891-2131; sergio.fuentes@standardandpoors.com

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Overview

- Brazil-based electricity transmission company TAESA improved its credit metrics as we expected and have reached levels that are aligned with its rating category following higher debt to fund its acquisitions in 2012 and 2013.
- We are affirming our 'BBB-' global scale and 'brAAA' national scale corporate credit ratings on TAESA. At the same time, we affirmed the national scale 'brAAA' long-term issue rating on the company's debt.
- The stable outlook reflects our expectation that TAESA will maintain its solid credit metrics over the next few years despite high dividend pay-outs and potential acquisitions.

Rating Action

On Oct. 1, 2014, Standard & Poor's Ratings Services affirmed its 'BBB-' global scale and 'brAAA' national scale corporate credit ratings Transmissora Alianca de Energia Eletrica S.A.'s (TAESA). We are also affirming our national scale 'brAAA' long-term issue rating on TAESA's debt. The outlook is stable.

Rationale

The ratings on TAESA reflect our view of its "satisfactory" business risk profile and "adequate" liquidity. We also incorporate our expectation that the company will maintain its solid credit metrics.

Our assessment of TAESA's business risk profile reflects its solid competitive position due to its monopoly rights on large electricity transmission assets (about 9,884 km) in Brazil, proven and favorable regulatory framework that supports a stable and predictable revenue stream, very low counterparty risk, and efficient operations.

Electricity transmission represents the lowest risk in the Brazilian electric sector, in our view. TAESA faces no competition or demand risk, and its exposure to counterparty risk is very low. TAESA benefits from a permitted revenues model (Receita Annual Permitida; RAP), which establishes that a transmission concession receives annual inflation-adjusted revenues from users in the National Interconnected System (SIN) based on the availability of the lines, rather than the actual volume of power it transmits. In our view, this shields the segment from the drought that has hit the Brazilian electricity sector since the end of 2012. Of a total 28 electricity transmission concessions that TAESA currently holds, 24 were contracted before 2006. These contracts stipulate that after 15 years of operation the regulator, Agencia Nacional de Energia Eletrica (ANEEL), will cut their revenues by 50%. This doesn't affect our analysis on TAESA over the next few years. On the other hand, only four of TAESA's concessions, which the company won after November 2006, are subject to regulatory tariff reviews, which we view favorably because it leads to stability and predictability of its revenues and cash flows.

TAESA's operating efficiency is superior to that of its local and global peers. The company has a strong track record in operating transmission assets in Brazil, which is reflected in availability rates above 99% and regulatory penalties below 1.5% of total revenues in the last seven years.

The company's credit metrics improved as we expected, supporting our assessment of an "intermediate" financial risk profile. After it took on more debt to finance acquisitions in 2012 and 2013, TAESA reported consolidated debt to EBITDA of 3.0x and funds from operations (FFO) to debt of 20% in the last 12 months ended June 30, 2014. Our base-case scenario projects debt to EBITDA to remain at 3.0x-3.5x and FFO to debt to continue to hold at 20%-25%. TAESA's aggressive dividend policy and acquisition-based growth strategy, which deplete its strong operating cash generation, somewhat limit the rating.

Companhia Energetica de Minas Gerais S.A. (Cemig; BB+/Stable/--) holds 42.4% of the voting shares of TAESA and investment fund FIP Coliseu (not rated) has 44.1%. We believe TAESA has some independence in terms of decision making and certain cash segregation from its main shareholders, therefore, the rating on Cemig doesn't limit the rating on TAESA.

Liquidity

We view TAESA's liquidity as "adequate." We expect sources of liquidity to exceed uses by at least 1.4x for the next 12 months. We also expect sources to exceed uses even if EBITDA declines by 10%. In our view, TAESA has the flexibility to reduce dividend payments in a stress scenario. TAESA has easy access to the bank and capital markets, as evidenced by the issuance of R$2.16 billion debentures in October 2012 and, more recently, of R$450 million term loans.

Principal Liquidity Sources:

- Consolidated cash and liquid investments of R$ 121 million as of Dec. 31, 2013;
- FFO of about R$800 million in 2014; and
- Debt issued in the first half of 2014 for about R$450 million.

Principal Liquidity Uses:

- Debt maturities with early debt amortization of about R$1 billion in 2014;

- Capital expenditures will remain low, at about R$35 million for the coming years;
- TAESA will use about R$200 million to pay for bids in 2014; and
- Above 90% dividend pay-out in 2014.

Outlook

The stable outlook reflects our opinion that TAESA will maintain its financial metrics aligned with its "intermediate" financial risk profile. We expect debt to EBITDA and FFO to debt to remain in the 3.0x-3.5x and 20%-25% ranges, respectively, over the next few years. In the short-term, we don't assume additional mergers and acquisitions or greenfield investments that could significantly weaken its financial metrics.

Upside scenario

We could raise the ratings if credit metrics improve further, leading to a debt to EBITDA consistently less than 3.0x, and FFO to debt consistently above 30%.

Downside scenario

We could lower the ratings if operating metrics decline considerably, leading to EBITDA margins of about 80% or if credit metrics deteriorate, with debt to EBITDA consistently greater than 3.5x and FFO to debt below 20%. We could also downgrade TAESA if liquidity becomes less than adequate or if financial flexibility deteriorates significantly as a result of additional acquisitions or a more aggressive than expected dividend policy.

Ratings Score Snapshot

Corporate Credit Rating
- Global scale: BBB-/Stable/--
- National scale: brAAA/Stable/--

Business risk profile: Satisfactory
- Country risk: Moderately high
- Industry risk: Very low
- Competitive position: Satisfactory

Financial risk profile: Intermediate
- Cash flow adequacy/Leverage: Intermediate

Anchor Score: bbb-

Modifiers
- Diversification/Portfolio-effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (no impact)
- Financial policy: Neutral (no impact)
- Management & governance: Satisfactory (no impact)

- Comparable rating analysis: Neutral (no impact)

SACP bbb-

Related Criteria And Research

Related Criteria

- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Jan. 2, 2014
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- Criteria - Corporates - Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Criteria - Corporates - General: Corporate Methodology: Ratios And Adjustments, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- Criteria - Corporates - General: 2008 Corporate Criteria: Rating Each Issue, April 15, 2008

Ratings List

Ratings Affirmed

Transmissora Alianca de Energia Eletrica S.A.	
Corporate Credit Rating	BBB-/Stable/--
Brazil National Scale	brAAA/Stable/brA-1
Transmissora Alianca de Energia Eletrica S.A.	
Senior Unsecured	brAAA
Commercial Paper	brA-1

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