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Research Update:

Transmissora Alianca de Energia Eletrica S.A. 'BB-' And 'brAA-' Ratings Affirmed; Outlook Remains Stable

Primary Credit Analyst:
Vinicius Ferreira, Sao Paulo + 55 11 3039 9763; vinicius.ferreira@spglobal.com

Secondary Contacts:
Marcelo Schwarz, CFA, Sao Paulo (55) 11-3039-9782; marcelo.schwarz@spglobal.com
Alvaro Landi, Sao Paulo (55) 11-3039-9757; alvaro.landi@spglobal.com

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Overview

- We expect Taesa's credit metrics to temporarily deteriorate, with debt to EBITDA around 3.5x-4.0x and FFO to debt between 15%-20% by 2019 especially due to higher investments to build new transmission lines. In spite of the increased leverage, we are maintaining the 'bbb-' SACP as a result of Taesa´s strong profitability, shown by its EBITDA margins above 95%, and very resilient and predictable cash flow generation, which compare favorably with its peers.
- We affirmed our 'BB-' global scale and 'brAA-' Brazil national scale ratings on Taesa, since the rating on the company cannot exceed the sovereign rating, given the regulated nature of its business.
- The stable outlook on Taesa reflects that on the sovereign rating on Brazil.

Rating Action

On May 25, 2018, S&P Global Ratings affirmed its 'BB-' global scale and 'brAA-/brA-1+' Brazil national scale corporate credit ratings on Transmissora Alianca de Energia Eletrica S.A. (Taesa). The outlook remains stable. The company's 'bbb-' stand-alone credit profile (SACP) remains unchanged.

At the same time, we also affirmed the 'brAA-' issue-level rating on Taesa's third debenture issuance of R$2.2 billion in three series due 2024.

Rationale

The rating affirmation on Taesa incorporates a rating cap as a result of the ratings on the Federative Republic of Brazil (Brazil: BB-/Stable/B foreign and local currency global scale ratings; brAA-/Stable/-- Brazil national scale rating). In our view, Taesa has an appreciable likelihood of strife in a sovereign default scenario, given the regulated nature of its business. We believe that, in this scenario, Taesa could ultimately be subject to tariff controls, negatively affecting the company's revenue collections and access to credit.

Taesa has a R$ 3.2 billion investment plan to perform in the next five years on greenfield transmission lines, as part of the company's strategy to diversify growth from acquisitions. This, in our view, will help the company to substitute cash flows of certain transmission lines that are approaching the middle of their concession, when revenues drop by 50% according to the terms of their concession contracts. Taesa will build eight new transmission lines in Brazil (five of them in partnership with other players) and will finance the required investments with debt. In addition, we made the following assumptions in our base-case scenario:

- We incorporated that the permitted annual revenues (RAPs: Receita Anual Permitida) will be reduced by 50% for certain transmission lines: TSN, Novatrans, Gtesa, and EATE in 2018; Patesa, STE, NTE, and ERTE in 2019; and Munirah, ATE I, ETAU, ENTE, and Transleste in 2020. Contracts determine this reduction in the 16th year of these concessions. For the other lines, we expect their RAPs to grow in line with inflation for Brazil of 3.6% in 2018 and 4.0% from 2019 on.
- In addition to the new R$ 3.2 billion expansion plan, concentrated in 2019 and 2020, we incorporated maintenance investments of about R$ 20 million per year.
- We assumed that Taesa will continue distributing the maximum available of the previous year's net income as dividends.

These assumptions shall result in the following credit metrics:

	2016A	2017A	2018E	2019E	2020E
Adjusted EBITDA (R$ million)	1,389.10	967.2	1,000-1,050	775-825	825-875
Debt to EBITDA (x)	2.1	2.5	2.0-2.5	3.5-4.0	4.5-5.0
FFO to debt (%)	33.3	28	30-35	15-20	10-15

A: Actual. E: Estimate

We expect Taesa to temporarily increase its leverage in the next few years as a result of (i) higher investments on its greenfield projects, and (ii) a reduction of the RAP in the existing concessions mentioned above. The company has lower cash flow generation, and all its investments are debt-financed. It has more leverage than previously. We believe that Taesa will reach its historic leverage levels once its greenfield assets become operational.

We view the regulatory framework in Brazil for electric power transmission companies as proven and favorable, allowing stable and predictable cash flow generation derived from the RAP model related to the availability of the transmission lines, rather than the actual volume of power that each line transmits. In our view, this shields the segment from electricity demand volatilities and an adverse macroeconomic scenario.

Companhia Energetica de Minas Gerais – CEMIG (B/Positive/--;

brBBB/Positive/--) and Interconexion Electrica S.A.E.S.P. (ISA: BBB-/Stable/--) have jointly controlled Taesa since 2017 through their shareholders' agreement. We view Taesa as a stand-alone company-- neither part of CEMIG nor ISA--because any decision about the company requires the approval of nine board members out of the eleven, requiring ISA and CEMIG to always be in agreement in all strategic matters. CEMIG has the right to nominate five members, while ISA nominates four--the remaining two are independent.

Liquidity

We expect Taesa's sources of cash to continue to surpass its uses of cash by more than 10%, and sources should continue to exceed uses even if EBITDA were to decline by 10% in the next 12 months. In addition, Taesa doesn't have financial covenants on its debt anym longer.

The company has good relationship with banks and access to debt markets, as seen in the sizable amount of debentures issued in the market. Although Taesa's operations are stable and predictable, which don't demand a large liquidity cushion, we believe Taesa will have the appropriate mechanisms to face any high-impact, low-probability event with limited need for refinancing, in which case we expect it to reduce dividend payout and to postpone investments.

Principal liquidity sources:

- R$93.1 million in cash and liquid investments, as of March 31, 2018; and
- Around R$850 million of cash flow generation in the next 12 months.

Principal liquidity uses:

- Short-term debt maturities of about R$430 million in the next 12 months;
- Minimum maintenance investments of about R$20 million in the next 12 months; and
- Minimum dividend distribution.

Outlook

The stable outlook on Taesa reflects that on the sovereign rating of Brazil.

Downside scenario

We could lower Taesa's ratings in the next 12 months if a similar rating action occurs on the sovereign rating of Brazil. We could also downgrade the ratings if the company's leverage increases significantly to FFO to debt below 9% or debt to EBITDA above 5.5x. This could occur if the company further expands its investment program with new debt financed projects while maintaining maximum dividend distribution.

Upside scenario

We expect the sovereign ratings to continue to cap those on Taesa.

Ratings Score Snapshot

Corporate Credit Rating:
Global scale: BB-/Stable/--
Brazil national scale: brAA-/Stable/brA-1+

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

Financial risk: Significant
- Cash flow/leverage: Significant

Anchor: bbb-

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

Stand-alone credit profile: bbb-

Related Criteria

- Criteria - Corporates - General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables, Aug. 14, 2017
- Criteria - Corporates - General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: National And Regional Scale Credit Ratings, Sept. 22, 2014

- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, 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
- Criteria - Corporates - General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Group Rating Methodology, Nov. 19, 2013
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities And Insurers, Nov. 13, 2012
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

Ratings List

Ratings Affirmed

Transmissora Alianca de Energia Eletrica S.A.	
Corporate Credit Rating	
Global Scale	BB-/Stable/--
Brazil National Scale	brAA-/Stable/brA-1+
Senior Unsecured	brAA-

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column.