

## **FITCH AFFIRMS ISA CAPITAL DO BRASIL'S IDRS AT 'BB+'/'AA-(BRA)'; CTEEP'S IDR AT 'AA+(BRA)'**

Fitch Ratings-Sao Paulo-27 August 2014: Fitch Ratings has affirmed ISA Capital do Brasil S.A.'s (ISA Capital) foreign and local currency Issuer Default Ratings (IDRs) at 'BB+', and its national scale rating at 'AA-(bra)'. In addition, Fitch has affirmed the company's USD31.6 million of senior secured notes outstanding at 'BBB-'. The Rating Outlook is Stable.

Concurrently, Fitch has affirmed Companhia de Transmissao de Energia Eletrica Paulista S.A.'s (CTEEP) national scale long-term rating at 'AA+(bra)'. The rating action also applies to its first debenture issuance in the amount of BRL500 million maturing in 2014 and 2017. The Rating Outlook is stable.

### **KEY RATING DRIVERS**

CTEEP's ratings reflect its strong credit quality attributable to the low business risk of the power transmission sector in Brazil, with predictable operating cash flow. The analysis also considered that the company is being efficient to manage its sound financial profile after the strong reduction of revenues consequence of the company's acceptance to early renew its main concession starting in January 2013. Fitch views as positive the use of the compensation received for the non-depreciated assets to pay down part of its debt. The ratings factored in a moderate regulatory risk.

ISA Capital's ratings reflect the credit profile of CTEEP, its sole revenue source and operating asset, and the company's structural subordination to CTEEP's obligations, given that ISA Capital only owns 37.8% of its total capital and does not receive the full amount of dividends paid by the transmission company. Fitch considers that ISA Capital's financial flexibility may benefit from the market value of its CTEEP's shares as well as from its linkage with its parent Interconexion Eletrica S.A. E.S.P - ISA (rated by Fitch at 'BBB', Outlook Stable) in case dividends received from CTEEP are not sufficient to meet its obligations.

The one-notch rating uplift for ISA Capital outstanding bonds reflects its enhanced recovery prospects due to the refinancing of the majority of its debt with (subordinated, debt like) preferred equity. The 2017 bonds are currently over-collateralized. The USD31.6 million (BRL76.8 million) of outstanding debt is secured by 66% of ISA Capital's shares on CTEEP, a stake which is currently valued at approximately BRL1.1 billion based on CTEEP's current market cap value of BRL5.8 billion.

### **CTEEP's Credit Metrics to Improve**

Fitch expects CTEEP's financial leverage to improve as a result of growing cash generation from new reinforcement investments in existing assets, as well as the company starts to receive the complementary compensation related to the acceptance to early renew its main concession. The company estimates BRL5.2 billion additionally to the BRL2.9 billion that the company is already receiving. The regulatory agency ANEEL still needs to approve this complementary compensation. For the last 12 months (LTM) ended June 30, 2014, the total debt-to-recurring EBITDA ratio was 3.8 times (x), with 2.4 considering the net debt. Fitch expects net leverage below 2.5x in the next years, considering that the company will not enter into new projects.

### **Predictable Cash Flow Generation**

CTEEP's cash flow generation is very predictable, exhibiting the low business risk profile of a power transmission company. CTEEP's revenues are exempt from volumetric risk as its maximum permitted annual revenue (PAR) is based on the power transmission assets available to users, instead of the

power transmitted. The company's cash flow generation saw a significant decrease at the end of 2012 after the company acceptance of the government proposal for early renewal of its main concession which would expire in 2015. For the LTM ended June 30, 2014, net revenues reached BRL1.1 billion, in accordance with IFRS, with recurring EBITDA of BRL380 million. In 2012, net revenues and EBITDA were BRL2.8 billion and BRL1.4 billion, respectively.

Fitch expects a positive free cash flow (FCF) for CTEEP in the next couple of years, considering annual dividends of BRL200 million-BRL250 million and no additional transmission assets being added to its portfolio. For the LTM ended June 30, 2014, cash flow from operations (CFFO) of BRL383 million was sufficient to cover capital expenditures of BRL19 million and dividends of BRL200 million leading to a FCF of BRL164 million.

#### Strong Liquidity Position

CTEEP's financial profile benefits from its robust liquidity position. As of June 30, 2014, as per Fitch methodology, cash and marketable securities of BRL533 million represented 36% of total debt of BRL1.5 billion and were sufficient to cover short-term debt of BRL403 million by 1.3x. Liquidity should improve based on the pending BRL1 billion to be received until July 2015 from the initial compensation of BRL2.9 billion and the potential BRL5.2 billion from the complementary compensation to be approved by the regulator. CTEEP also presented a comfortable short-term debt coverage when considered the (CFFO + cash and marketable securities)/short-term debt at 2.3x.

#### Low Business Risk

Fitch considers the transmission segment as the lowest risk at the Brazilian power sector. CTEEP's credit profile benefits from its exclusive right to provide electricity transmission services through its multiple concessions. CTEEP currently participates in seven concessions in operation with an equivalent participation of 1.842 km. In addition, there is one concession with the start-up forecasted to 2015 that will add 383 km to the portfolio. This scenario reduces the company's exposure to the risks associated with the construction phase.

#### Structural Subordination

ISA Capital's credit quality reflects the company's structural subordination to CTEEP's obligations.

ISA Capital owns only 37.8% of CTEEP's total capital and receives this proportional stake on the dividends paid by the transmission company. ISA Capital is expected to use the proceeds it receives from CTEEP, together with its cash on hand (which stood at approximately BRL745 million as of December 2013 in consolidated terms) to pay its debt. At the end of 2013, ISA Capital's consolidated debt was BRL2.37 billion, comprised of the remaining portion of its 2017 bonds (BRL77 million) not tendered during 2010 and the obligations to redeem its preferred shares (BRL891 million).

Fitch believes that ISA Capital will have to raise additional cash to meet debt obligations, since dividends flow from CTEEP should not be sufficient. The concession renewal process has somewhat affected CTEEP's ability to upstream cash to its controlling shareholder through dividend payments. Annual dividends from the transmission company are expected to range from BRL200 million to BRL250 million, down from the previous expectation of between BRL250 million to BRL300 million, which reflects CTEEP's revised cash flow profile. In 2013, in order to adjust its preferred share buying program to this new reality, ISA Capital renegotiated with the preferring shareholders the program repurchase schedule. The program of acquiring the BRL891 million of preferred shares has been extended to 2020 and consists of BRL100 million in 2014-2015 and BRL160 million per year from 2016 to 2020.

#### RATING SENSITIVITIES

Positive rating actions are unlikely in the short term for CTEEP and ISA Capital. Considerations that could lead to negative rating actions for CTEEP include a net leverage sustainably above 3.0x and a (CFFO + cash and marketable securities)/short-term debt ratio below 2.5x. In the case of ISA

Capital, a strong devaluation of CTEEP's value and a difficult scenario to raise additional cash to meet its preferred shares redemption program can pressure the ratings.

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Additional information is available at '[www.fitchratings.com](http://www.fitchratings.com)'.

Applicable Criteria and Related Research:

--'Corporate Rating Methodology' (May 28, 2014);

--'National Scale Ratings Criteria' (Oct. 30, 2013).

Applicable Criteria and Related Research:

Corporate Rating Methodology - Including Short-Term Ratings and Parent and Subsidiary Linkage

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National Scale Ratings Criteria

[http://www.fitchratings.com/creditdesk/reports/report\\_frame.cfm?rpt\\_id=720082](http://www.fitchratings.com/creditdesk/reports/report_frame.cfm?rpt_id=720082)

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