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## Research Update:

# Celeo Redes Operacion Chile S.A.'s Senior Notes Rated 'BBB' And 'clAA-', Stable Outlook

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## Research Update:

# Celeo Redes Operacion Chile S.A.'s Senior Notes Rated 'BBB' And 'clAA-', Stable Outlook

## Overview

- Celeo Redes owns and operates two transmission lines in Chile, which are restricted assets and benefit from long-term fixed availability of revenue.
- The project has issued \$379 million 5.2% series A senior secured notes and UF5.4 million 3.35% series A senior secured notes.
- We're assigning our 'BBB' issue-level ratings to the dollar-denominated senior secured notes and our 'clAA-' issue-level rating to the UF-denominated senior secured notes.
- The ratings reflect our expectation that the transmission line currently under construction will begin operating before February 2018. As such, the stable availability payments received by the two operating transmission lines will support repayment of the project's fully amortizing debt maturing in June 2047.
- The outlook is stable and reflects our expectation that Celeo Redes will have steady income during the next 12-24 months. Our base-case scenario estimates a minimum debt service coverage ratio (DSCR) of 1.3x in 2030 and average DSCR of 1.5x.

## Rating Action

On May 11, 2017, S&P Global Ratings assigned its 'BBB' rating to Celeo Redes Operacion Chile S.A.'s (Celeo Redes) \$379 million 5.2% series A senior secured notes due June 2047. At the same time, we assigned the Chilean national scale rating of 'clAA-' to the UF5.4 million 3.35% series A senior secured notes due June 2047. The outlook is stable for both issuances.

## Rationale

The ratings reflect our expectation that the stable availability payments received by the project's two transmission lines will support repayment of its amortizing debt until its final maturity in June 2047. Our assessment is supported by our view that the Chilean regulatory framework for transmission lines is favorable, given its track record of contract execution and tariff review mechanism. The ratings also assume that the construction of Charrúa Transmisora de Energía, S.A. (CHATE) will be completed by September 2017, which was 95% completed as of March 2017.

Celeo Redes owns three transmission lines located in Chile's main power grid, Sistema Interconectado Central (SIC). The assets consist of:

- Alto Jahuel Transmisora de Energía, S.A. (AJTE) a 256-kilometer (km) 500 kilovolts (kV) transmission line, consisting of two circuits. AJTE circuit 1 started commercial operations (COD) in September 2015, and is entitled to receive fixed availability payment until 2036. AJTE circuit 2 started commercial operations in January 2016, and is entitled to receive fixed availability payments until 2020.
- Charrúa Transmisora de Energía, S.A. (CHATE) is a single 198-km circuit under construction. According to an independent engineer (IE) report prepared by Black & Veatch in April 2017, the project was 95% complete as of March 2017 and should be finished by September 2017. This is five months ahead of contractual COD, of Feb. 25, 2018.
- Cumbre-Nueva Diego de Almagro S.A. (DATE) a 52-km 220kV transmission line, which is also under construction and is expected to start commercial operations in April 2019.

AJTE and CHATE are restricted subsidiaries and guarantors under the project, while DATE is an unrestricted subsidiary.

The ratings on Celeo Redes' issuances also reflect the following factors:

- The historical performance of AJTE has always been above the minimum regulated requirement of 99.85%, and we expect it will continue at that level.
- The assets benefit from long-term agreements granted by the Ministry of Energy through the Executive Decree (Decree). The latter provide fixed annual revenues based on the lines' availability, which eliminates the risk of fluctuating demand and pricing. The tariff reset mechanism at AJTE's circuit 1 will begin in 2036, in 2020 at circuit 2, and in 2038 at CHATE. This will provide very predictable and stable revenues to repay the notes.
- The project benefits from having an experienced operator, and a five-year fixed O&M contract, which is renewable annually.
- The issuance presents adequate structural protection provisions, with a six-month DSRA and three-month O&M reserve account. It benefits from having some limitations, such as a dividend distribution test of 1.15x backward- and forward-looking until the end of 2035 and starting in January 2036 of 1.15x backward- and 1.2x forward-looking until the end of the notes. Mechanisms of cash retention and limitations on additional debt are also in place.
- There is a legal separateness of the two assets (AJTE and CHATE) and the issuer (holdco) to the non-restricted asset (DATE). In addition, there are no joint and several liabilities related to the construction of DATE that could be considered a priority or senior liability of the Issuer in relation to its obligation to repay the senior notes, guaranteed by AJTE and CHATE. Last, a failure to deliver the construction of DATE could not cause the bankruptcy or Chapter 11 proceedings (or similar proceedings that would result in an event of default of the bond issuance) of the Issuer, as the holdco of the three assets.
- Under our base case, we expect a minimum and average DSCR of 1.3x and 1.5x, respectively.

## **Construction Phase SACP: 'bbb+'**

We assign a construction phase stand-alone credit profile (SACP), given that the project is responsible for the construction of CHATE. According to the IE report prepared by Black and Veatch in April 2017, CHATE's construction was 95% complete as of March 2017 and should be finished by September 2017. There is an engineering, procurement, and construction EPC agreement with Elecnor Chile (not rated) for the construction of CHATE.

We typically assess the construction of transmission lines as a simple civil engineering task. In addition, we view the construction stage of CHATE as very advanced, with the majority of permits, including the environmental and rights-of-way ones, duly obtained. Therefore, we have assigned an 'a-' construction phase business assessment to the issuance.

### **Construction phase funding**

Considering the amount of the issuance and the advance of construction, the ratio of construction uses and sources is neutral in our analysis, because we believe that the project has financial flexibility to finalize the construction of CHATE, even if it requires replacing the contractor.

### **Construction counterparty dependency**

We consider the EPC contractor as a relevant counterparty to the project, limiting the construction sACP to bbb+, which considers the existing financial flexibility to replace the contractor, and related the additional time and mobilization costs.

## **Operations Phase SACP: 'bbb'**

The project's restricted assets consist of AJTE and CHATE, and each of which benefits from annual guaranteed revenues (the Decree agreement established at \$18.6 million per year for AJTE circuit 1 and \$16.9 million per year for CHATE circuit 1), based on availability. This eliminates demand risk because revenues don't depend on the effective utilization rate. The transmission lines use proven technology with low operating risks. Therefore, we have assigned an operations phase business assessment of '3' to the project, resulting from an asset class operations stability assessment of '3' (on a 10-point scale, which is typical for transmission line), with no impact from performance risk or market exposure assessments.

O&M activities are performed by Celeo Redes Chile Limitada (not rated). The O&M contract price is about UF47,000 per year for AJTE's two circuits and about UF31,000 per year for CHATE, adjusted by the same index as the project's revenues in local currency, which prevents a cost/revenue mismatch. The initial five-year contract includes an automatic renewal clause unless either party chooses to terminate the agreement. We view Celeo Redes Chile Limitada's

participation as positive and its credit quality does not impose a limitation to the transaction. There are other operators in the local market which could replace the operator at similar operational quality and price, and the project has the financial flexibility from its O&M reserve account to replace the operator if necessary.

Approximately 60% of tariffs are adjusted annually by inflation, linked to the U.S. consumer price index and 40% are linked to the Chile's consumer price index. In our view, the issuance has limited exposure to currency mismatch given the balance between the dollar- and UF-denominated debt. Moreover, the revenues linked to Chile's inflation should mitigate any cost increase incurred from inflationary pressures.

## **Operations Phase Finance Base And Downside Case Assumptions**

### **Base case scenario**

Our base-case assumptions include the following factors:

- A fixed tariff, according to the Decree, will drop 5% every four years upon the start of the reset period.
- An inflation rate of 3% for 2017, upon which the revenues will be adjusted.
- Exchange rate of CLP675 per dollar to the end of 2017 and CLP685 per dollar to the end of 2018.
- Our macroeconomic assumptions were based on the article: "Commodity Prices Give A Temporary Breath Of Fresh Air To Latin America, While U.S. Policy Uncertainty Lingers," published April 4, 2017.
- Availability of around 99.85%, based on the operator's track record of AJTE and other transmission lines in Chile.
- Fixed O&M expenses for five years.

Under these assumptions, we expect a minimum and average DSCR of 1.3x in 2030 and 1.5x, respectively.

### **Downside case scenario**

Our assumptions of the stressed scenario include:

- A fixed tariff according to the Decree, which drop 10% every four years upon the start of the reset period.
- A 3% deficit of availability.
- A 12% increase in O&M costs.
- A 15% appreciation in Chilean peso, which implies an increase in the project's costs.
- Penalties of up to \$30 million for any delay in the construction of DATE. According to a legal opinion provided, a contingency liability would be limited to a fine equivalent to a maximum 730 days to the expected COD set in the Decree.

Under the downside case scenario, we expect a minimum DSCR of 0.9x in 2022, and the shortfall to be covered with the reserve accounts' funds.

## **Counterparties**

We consider the counterparties paying the availability revenues of both AJTE and CHATE as relevant to the transaction. However, in our opinion, none of them represents a limitation for the rating of the transactions to date

## **Transaction Structure Profile**

Parent linkage analysis: De-linked

The Spanish infrastructure and energy company, Elecnor S.A. (51%, not rated), and Dutch pension fund, APG Asset Management NV (49%, not rated), own the issuer. According to the issuances documents, there are limitations and affirmative covenants preventing affiliate transactions. In addition, there are no cross-default or parent-dependency provisions.

Structural protection analysis: Neutral

The issuances presents neutral structural protection provisions, including limitation on additional debt in excess of \$25 million, otherwise subject to rating affirmation and other conditions; limitation to create any lien to project security in addition to preserve the collateral; maintain ownership of all restricted assets, including 99.99% of the equity of AJTE and CHATE; and maintain insurance coverage, in favor of the project.

## **Liquidity**

We assess the project's liquidity as neutral, as the project include a six-month DSRA and a three-month O&M reserve account which will be funded with the resources of the issue by an approximate amount of \$15 million and \$780,000, respectively. Under the DSRA, there is an additional \$820,000 reserve until the end of 2017, when construction of CHATE is expected to be completed. In addition, there is also a backward- and forward-looking distribution lock-up of 1.15x until the end 2035, and of 1.15x backward-looking and 1.2x forward-looking after January 2036.

## **Outlook**

The stable outlook reflects our expectation that Celeo Redes will generate stable income during the next 12 to 24 months given the availability on the project's transmission lines. The project has long-term concessions at fixed prices. These lead us to expect stable DSCR metrics, and our projections assume availability levels in line with the historical availability of other Chilean transmission lines and above the minimum regulatory requirement of 99.85%. That would result in an average DSCR of 1.5x and a minimum of 1.3x for 2030. In addition, the stable outlook also reflects our expectation that CHATE will be finished on time and on budget, and begin operating by September 2017.

### Downside scenario

We could downgrade Celeo Redes Outlook if the availability of the lines were consistently lower than expected or if costs were higher than expected, producing a minimum DSCR below 1.2x, or if there were delays in the construction of DATE which could produce fines greater than \$30 million. Lastly, we would consider a downgrade if there is construction delay for the delivery of CHATE beyond February 2018, when we would expect to see delay penalties applied.

### Upside scenario

At this point the upside scenario would be limited to the blended average credit quality of the counterparties paying the availability revenues of both AJTE and CHATE.

## Ratings Score Snapshot

### Construction phase SACP (Senior debt): bbb+

- Construction phase business assessment: a-
- Funding adequacy: Neutral
- Construction funding: Neutral (no impact)
- Counterparty assessment limitation: bbb+ (+4 notches for CDA)

### Operations phase SACP (Senior debt): bbb

- Asset class operations stability assessment: 3
- Performance risk assessment N/A
- Market exposure assessment N/A
- Operations phase business assessment: 3 (1=best to 12=worse)
- Preliminary SACP: bbb
- Downside impact on preliminary SACP: None
- Capital structure and average DSCR impact on preliminary SACP: None
- Liquidity: Neutral
- Comparative analysis assessment: Neutral
- Counterparty assessment limitation: None

### Modifiers (Senior Debt)

- Parent linkage: Delinked
- Structural protection: Neutral
- Extraordinary government support: None
- Sovereign rating limits: AA-
- Full credit guarantees: None
- Senior debt issue rating: BBB; clAA-

## Related Criteria

- General Criteria: S&P Global Ratings' National And Regional Scale Mapping Tables, June 1, 2016
- General Criteria: National And Regional Scale Credit Ratings, Sept. 22,

2014

- Criteria - Corporates - Project Finance: Project Finance Operations Methodology, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Project Finance Framework Methodology, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Key Credit Factors For Power Project Financings, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Project Finance Transaction Structure Methodology, Sept. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria - Corporates - Project Finance: Project Finance Construction Methodology, Nov. 15, 2013
- Criteria - Structured Finance - General: Counterparty Risk Framework Methodology And Assumptions, June 25, 2013
- Criteria - Corporates - Project Finance: Project Finance Construction And Operations Counterparty Methodology, Dec. 20, 2011
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009

## Ratings List

Celeo Redes Operacion Chile S.A.

\$379M 5.2% series A sr. sec. notes	BBB/Stable
UF5.4M 3.35% series A sr. sec. notes	clAA-/Stable

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](http://www.standardandpoors.com) for further information. Complete ratings information is available to subscribers of RatingsDirect at [www.globalcreditportal.com](http://www.globalcreditportal.com) and at [www.spcapitaliq.com](http://www.spcapitaliq.com). All ratings affected by this rating action can be found on the S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left column.



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