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## Research Update:

# Celeo Redes Operacion Chile S.A. 'BBB' And 'clAA' Senior Secured Rating Affirmed, Outlook Remains Stable

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## Research Update:

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## Rating Action Overview

- We expect Chile-based electricity transmission Company Celeo Redes Operacion Chile S.A. (or the project) to continue generating solid and stable cash flows over the next few years following the incorporation of the third line that boosted cash flows.
- On Feb. 28, 2019, S&P Global Ratings affirmed its 'BBB' issue-level ratings on Celeo Redes' dollar-denominated senior secured notes as well as our Chilean national scale 'clAA' issue-level rating on its UF-denominated senior secured notes.
- The stable outlook on the ratings reflects our view that Celeo Redes should maintain its cash flow stability given its strong availability levels above the minimum regulatory requirement of 99.85%, which should result in minimum and average debt service coverage ratios (DSCR) around 1.30x and 1.40x, respectively, during the debt's term.

## Project Description And Key Credit Factors

Celeo Redes owns three trunk transmission lines located in Chile's power grid. The assets benefit from perpetual concessions granted by the Ministry of Energy in which revenues under the contractual agreement are not subject to any demand risk and are not based on utilization rate of the lines. The project's 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, which is entitled to receive fixed availability payments until 2035, and AJTE circuit 2 that receives same type of payments until 2020. AJTE circuit 1 is operational since September 2015 and AJTE circuit 2 since January 2016.
- Charrúa Transmisora de Energía, S.A. (CHATE): A single 198-km circuit that started commercial operations in December 2017 and is entitled to receive fixed availability payments until 2038.
- Diego de Almagro Transmisora de Energía (DATE): A 52-km 220kV transmission line, which started commercial operations on Jan. 16, 2019.

Under the special purpose entity (SPE), Celeo Redes Operacion Chile S.A., AJTE and CHATE are restricted subsidiaries and guarantors of the project, while

DATE is an unrestricted subsidiary. There is a legal separation between AJTE, CHATE, and the issuer (holdco) and the non-restricted asset (DATE). In addition, there are no joint liabilities related to DATE's operations that could be considered a priority or senior liability to the issuer in relation to its obligation to repay the senior notes, guaranteed by AJTE and CHATE. Nevertheless, now that DATE is operational, it could enter into the restricted asset group, thus expanding offering collateral. In addition, DATE could raise its debt pari passu with the project's existing notes based on pre-defined criteria such as rating re-affirmation and equivalent or better-consolidated portfolio DSCR.

Based on the concession contracts, Celeo Redes receives fixed revenue based on its availability, providing predictable and stable revenue flow with no exposure to market risk. Rates are in place for a 20-year period since commencement of operations (COD) of AJTE and CHATE lines. The regulator revises AJTE circuit 2 rates every four years and will revise those for AJTE circuit 1 20 years after the start of operations based on the trunk transmission annuity value (VATT) that consists of two components. First, an investment value annuity (AVI) for AJTE is 44.6% denominated in dollars and adjusted to U.S. inflation and the remainder denominated in UF, while for CHATE, it's entirely denominated in dollars and linked to U.S. inflation. The second component of the rate is a reimbursement for operating expenses (COMA) indexed to Chile's inflation.

In practice, all energy market participants in Chile contribute to the payment of the trunk transmission toll, meaning that in case one of the parties doesn't meet its obligation, the rest of the players should fulfill it with the final aim of ensuring the stability of the system. Hence, in our view, Celeo Redes doesn't have revenue off-takers because we view the system as jointly liable.

### **Strengths**

- Revenue base dependent on lines' availability levels eliminating market risk and providing stable cash flow.
- Relatively low operational complexity with proven technology.
- No exposure to counterparty risk as payments come from the electric system.

### **Risks**

- Exposure to fixed-rate recalculation before the notes' maturity in 2047.
- U.S. inflation's sustained decreases in the long term, given its direct impact on revenues.
- Although unlikely, a natural disaster--usually an earthquake in Chile--could damage the project's transmission lines.

## Rating Action Rationale

The rating affirmation on Celeo Redes reflects its strong operational and financial performance due to its favorable concession agreement that stipulates the project's annual revenue based on its availability, eliminating market risk and providing predictable and solid revenue flow. We expect a minimum DSCR of around 1.30x and an average of 1.50x during the term of the notes maturing in June 2047.

The project benefits from 20-year fixed rates since COD of AJTE and CHATE that are regularly adjusted to U.S. and Chilean inflation, and revised by the regulator as mentioned above. Furthermore, these availability compensations are provided by the electric system, thus any particular delay in the payment chain wouldn't hurt the project's cash flow available for debt service.

The rating is also supported by a relatively low operational complexity and an experienced operator, Celeo Redes Chile Limitada (not rated), under a fixed-price contract for five years, automatically renewed at maturity.

## Liquidity

We assess the project's liquidity as neutral, because of a six-month debt service reserve account (DSRA) and a three-month operations and maintenance (O&M) reserve account, funded through issuances of about \$15 million and \$780,000, respectively. In addition, there's a backward- and forward-looking distribution lock-up of 1.15x until 2035, which will be 1.15x backward-looking and 1.2x forward-looking after January 2036.

## Outlook

The stable outlook reflects our vi

ew of stable cash flow generation during the next 12-24 months, resulting in DSCR metrics of 1.29x-1.35x, given Celeo Redes' long-term concession contracts at fixed prices and availability levels above the minimum regulatory requirement of 99.85%.

### **Downside scenario**

A downgrade in the next two years is possible if the project's revenues are lower than expected, for instance, if annual U.S. inflation decreases below 1.8% in the long term or if costs or income taxes are higher than our projections, resulting in a minimum DSCR below 1.25x.

### **Upside scenario**

Although unlikely, we could upgrade Celeo Redes if its resilience to a downside-case scenario increases, while maintaining a minimum DSCR of about 1.30x.

## **Performance Update**

Celeo Redes' performance in the last 12 months was above our projections with a total annual revenue of \$56.3 million thanks to CHATE's start of operations. In addition, availability levels of Celeo Redes were around 99.9%, in line with the minimum required under the technical rule.

The construction of DATE was completed, and it started commercial operations on Jan. 16, 2019. Therefore, we are no longer considering fines related to possible delays in DATE's construction in our projected scenarios, which slightly improves Celeo Redes' expected DSCR.

## **Base Case**

### **Assumptions**

- We are considering key macroeconomic variables, particularly inflation in the U.S. and Chile, and exchange rate. We expect CPI for Chile of 3.2% in 2019 and 3% afterwards; CPI for the U.S. of 2.2% in 2019, 2.3% in 2020, and 2.2% afterwards; and average exchange rate of Chilean peso (CLP) 685 per \$1 in 2019, CLP690 per \$1 in 2020, and CLP695 per dollar in 2021.
- Fixed rates adjusted by inflation in Chile and/or the U.S., depending on the asset. After the initial fixed-rate period, the regulator will recalculate the asset remuneration incorporating the asset's replacement value and an after-tax return on investment that will range from 7% to 10%. We calculate the new rate, incorporating an after-tax return of 8%, a depreciable life for transmission lines of 50 years, and the abovementioned macroeconomic variables.
- O&M agreements with Celeo Redes Chile Limitada, totaling about UF47,000 per year for AJTE's two circuits and about UF31,000 per year for CHATE, adjusted to Chilean inflation. The agreements include an automatic renewal clause unless either party chooses to terminate them.
- No penalties due to unavailability of the assets, given the transmission lines' and the operator's solid track records.

## Key metrics

Under these assumptions, we expect a minimum DSCR of 1.29x in 2019 and an average DSCR of 1.40x) during the notes' term.

## Downside Case

### Assumptions

- We stress both U.S. inflation and foreign exchange, because U.S. inflation has a positive effect on the project's revenues. We assume a 50 basis point (bps) decrease in the U.S. rate from our base-case scenario and a 15% appreciation of the Chilean peso for a five-year period starting in 2019, the most vulnerable phase of the project. This would weaken its financial performance, given that the project's costs are denominated in domestic currency.
- After the initial regulated period, we calculated the new rate based on a 7% after-tax return, the stressed macroeconomic variables, and a depreciable life for transmission lines of 50 years. In addition, we incorporate a two-month delay in payment from the largest generator for a five-year period starting in 2019.
- Operational expenses 12% costlier than in our base-case scenario.
- Penalties ranging from \$1.4 million to \$1.7 million for a five-year period starting from the weakest phase of the project due to a 3% unavailability.

### Key metrics

Under the downside-case scenario, we expect a minimum DSCR of 1.04x and average DSCR above 1x during the life of the notes; nonetheless, any shortfall will be covered with the reserve accounts' funds.

## Rating Score Snapshot

### Operations phase SACP (Senior Debt)

- Operations phase business assessment: bbb
- Preliminary SACP: bbb
- Downside impact on preliminary SACP: None
- Liquidity: Neutral
- Comparative analysis assessment: Neutral
- Adjusted preliminary operations phase SACP: bbb
- Operations counterparty ratings adjustment: N/A
- Financial counterparty ratings adjustment: N/A
- Operations phase SACP: bbb

## Modifiers (Senior Debt)

- Parent linkage: De-linked
- Structural protection: Neutral
- Senior debt issue rating: bbb

## Related Criteria

- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- Criteria - Corporates - Project Finance: Key Credit Factors For Power Project Financings, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Project Finance Framework Methodology, Sept. 16, 2014
- Criteria - Corporates - Project Finance: Project Finance Operations Methodology, 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 - 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

Ratings Affirmed

Celeo Redes Operacion Chile S.A.

Senior Secured

BBB/Stable

Senior Secured

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.capitaliq.com](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://www.standardandpoors.com). Use the Ratings search box located in the left

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