

Alfa Transmisora de Energía S.A.

December 27, 2022

Project Description

Alfa Transmisora de Energía S.A. (Alfa Transmisora, formerly known as Alfa Desarrollo SpA) is jointly owned by Celeo Redes Chile Expansion SpA (Celeo) and APG Energy & Infra Investments Chile Expansion SpA (APG). In 2021, Celeo and APG acquired Colbun Transmisión S.A.'s assets through a newly created company, Alfa Transmisora, which is the issuer of the senior secured notes. Alfa Transmisora now owns all the operating assets of Colbun Transmission:

- National assets (regulated): seven transmission lines totaling 335 kilometers (km) and five substations.
- Zonal assets (regulated): six transmission lines totaling 70 km and two substations.
- Dedicated assets (nonregulated): 16 transmission lines with a total length of 494 km and 20 substations.

Currently, these assets have a 4.2% market share in Chile in terms of transmission length. These lines are located across five of the country's regions that are home to 74% of Chile's population, generate close to 66% of the country's GDP, and account for 57% of the electricity demand in the country.

Credit Highlights

Overview

Key strengths

Stable and predictable cash flows, given favorable regulatory framework in Chile and the company's revenues from availability, preventing volume risk.

Adequate structural protections that include a six-month debt service reserve account (DSRA), a three-month operations and maintenance (O&M) reserve account backed by letter of credit (LoC), and a pre-funded interest reserve account during the notes' term that help the company to withstand a potential downside scenario.

Transmission lines have low operational complexity and commercially proven technology.

Key risks

Exposure to recontracting risk. While regulated revenues (about 38% of total as of June 2022) are not exposed to market risk, many dedicated contracts will come due before the notes mature in 2051, exposing the project to price volatility.

During the life of the notes, the regulator will outline a new tariff collection scheme.

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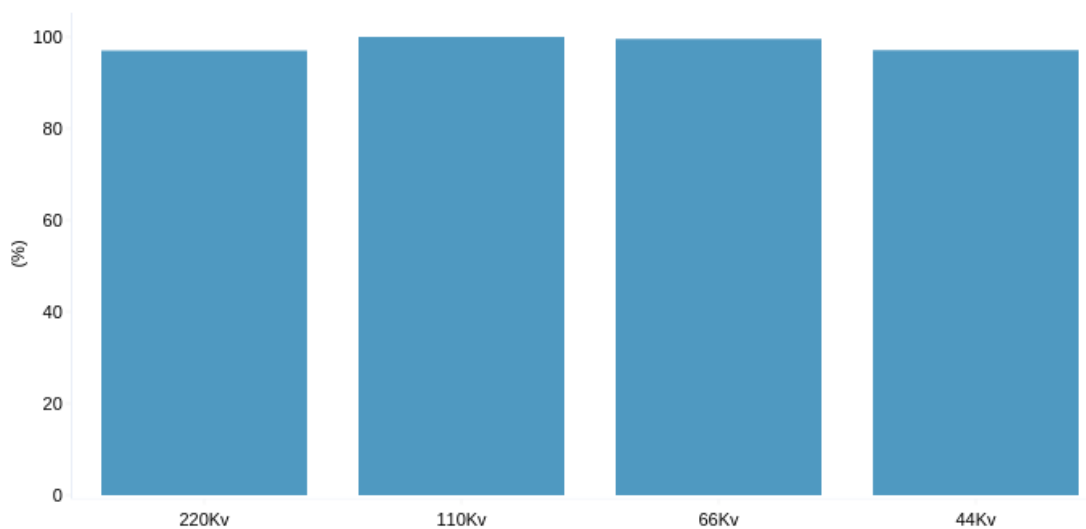
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Alfa Transmisora merged with its subsidiary, Alfa Transmisión S.A. On Feb. 17, 2022, Alfa Transmisora acquired Celeo Redes Chile Expansión SpA's share of Alfa Transmision (formerly Colbún Transmisión), becoming the owner of 100% of shares. On Feb. 28, 2022, Alfa Transmisora and Alfa Transmisión merged. The transactions were closed as expected and have no implications for the rating.

The project's operating performance and investments are in line with expectations. As of September 2022, availability levels were in line with our expectations at above 97% for all transmission lines, with no reported incidents.

Availability Of Lines YTD September 2022



Performance in 2022 is better than our previous base-case forecast, because of higher inflation in the U.S. and Chile. The latter improves the project's cash flows, increasing its revenue above growth of its operating costs, strengthening EBITDA margin that we now project at about 90%. Our updated base-case scenario incorporates new macroeconomic conditions and a minimum DSCR of 1.32x in December 2022, increasing to 1.36x in December 2023. Although we now expect this metric to be higher than 1.20x in our previous forecast, it's still consistent with the 'BBB-' rating. In terms of capital investments, Alfa Transmisora won a bid to construct expansion projects under the Chilean Ministry of Energy's Decree 231, which should become operational by 2025 and are currently under construction on time and within budget.

We will continue monitoring the assets' performance and we could raise the debt rating on Alfa Transmisora if the DSCR approaches 1.4x and investments through 2025 remain on track.

The regulated rate review will be completed in the first half of 2023. As of June 2022, about 38% of Alfa's total revenues were derived from the tariffs approved for the 2016-2019 period. The rate review is ongoing and Comision Nacional de Energia (CNE) has published the Definitive Technical Report for the 2020-2023 period. The Contraloria General de la Republica is reviewing the final decree, and we expect it to be approved during the first half of 2023. The purchase agreement of transmission lines with Colbun was signed during the rate review, and a price-adjustment mechanism is in place once the rate review is completed. The purpose of the adjustment is to compensate the seller in the event of higher rates and to protect the buyer against a possible reduction in the reference rate. According to CNE's report, transmission rates are higher than the reference rate. This means that Alfa Transmisora's cash flows will be higher than we expected and, on the other hand, the purchase price of transmission lines must be adjusted

upward. We expect the project to incur additional debt if necessary to compensate for the higher purchase price. This is in line with our expectations, and we will closely monitor the potential impact that this price adjustment could have on DSCRs, although we currently don't expect a significant change.

We don't expect changes in the regulatory framework. We believe that the risk related to political uncertainty that could eventually affect transmission companies is very low. Currently, Chile's Congress hasn't initiated any legislation related to the transmission sector, while the relevance of transmission lines has increased because of the country's decarbonization and the greater share of renewable energy in the Chilean power matrix.

Outlook

The stable outlook incorporates our expectation that the project will be able to maintain high availability of its transmission lines without major events that would result in penalties. We forecast a minimum DSCR in the 1.30x area in 2022 and we expect that investments will continue to be executed on time and within budget. Therefore, Alfa Transmisora's cash flows should remain stable and predictable, allowing the project to execute the planned investments that the Chilean regulator has requested to improve the system's reliability.

Downside scenario

In the next 12 months, we could lower the rating if the project posts a minimum DSCR of 1.15x or lower, which could result from lower inflation adjustments in its contracts (either Chilean or U.S. inflation), higher operating expenses, or investments above the budget. Although unlikely in the next 12 months, if we were to downgrade Colbun to 'BB+' or lower, the rating on the project would move in tandem, given that Colbun is Alfa Transmisora's largest individual offtaker.

Upside scenario

In the next 12 months, we could raise the rating if the project's minimum DSCR is consistently near 1.30x in 2023 and 2024 because of higher Chilean or U.S. inflation, greater cost savings, or if future investments are lower than we expect. In addition, if contracts maturing throughout the notes' term are renewed under better terms than in our base-case scenario, we could raise the rating.

Performance Update

The rating on Alfa Transmisora reflects our expectation that it will post solid operating and financial performance in the next few years thanks to its availability and stable regulation. We expect a minimum and median DSCR of about 1.3x and 1.6x, respectively, during the notes' term thanks to a relatively low operating complexity, a business model based on availability, and currently higher inflation, which affects the cumulated adjustment in the long term. From an operational standpoint, the assets' availability level in the first nine months of 2022 was in line with our expectations, complying with the established limits with no penalties, fines, or accidents reported. We expect a similar operating performance in 2023, which supports the project's cash-flow predictability.

Operations Analysis

The project's assets benefit from annual guaranteed revenues, eliminating demand risk, because revenues don't depend on the effective utilization rate. Moreover, transmission lines use proven technology, and overall, we view the operational risk as low. Therefore, we've assigned an operations phase business assessment of '4' to the project, resulting from an asset class operations stability assessment of '3' (on a 10-point scale, 10 being the highest risk), which is typical for transmission lines because, in our view, they require some specialized maintenance skills. In addition, we assess a very low market risk because some of the project's contracts are bilateral with private counterparties and mature during the notes' term, which exposes the project to some price

volatility during the recontracting period. Finally, the project generates all of its revenues and has all of its assets in Chile, the country risk of which we assess as intermediate.

Base-case assumptions

- We consider macroeconomic variables relevant for the project, particularly inflation in the U.S. and Chile, extracted from our recent articles "**Economic Outlook Latin America 1Q 2023: A Shift To Lower Growth**," published on Nov. 28, 2022, and "**Economic Outlook U.S. Q1 2023: Tipping Toward Recession**," published the same date. We expect U.S. inflation to be 8.1% in 2022, 4.3% in 2023, 2.7% in 2024, 2.3% in 2025, and 2.0% afterward. We expect Chile's inflation to be 12.5% in 2022, 5.5% in 2023, and 3.0% afterward. U.S. and Chile's inflation affects the project's revenue and rates, and Chile's inflation influences most of operating costs.
- The starting point for VATTs (Annual Transmission Value per Section) in 2022 is about \$30 million for the regulated revenue (both national and zonal) and close to \$50 million for the dedicated revenue. We maintain our assumption for a 15% haircut from the original rate in 2035, when the 20-year fixed rate period ends for CADA.
- Operating expenses comprise O&M costs, as well as commercial and administrative expenses, adjusted annually to Chile's inflation.
- We don't incorporate any penalties due to unavailability of assets, because we believe the Chilean transmission system has redundancies in place to prevent a blackout.

Key metrics

We expect the project to post a minimum DSCR of 1.3x and median DSCR of 1.60x during the notes' term, and 1.70x and 1.9x, respectively, in the refinancing period. For a minimum DSCR of 1.3x and an operating phase business assessment (OPBA) of '4', the preliminary operations phase SACP is 'bbb-'.

Downside-case assumptions

- Macroeconomic variables. We stressed U.S. and Chilean inflation. Given that inflation in both countries has a positive effect on the project's revenue, we assumed a 50-basis point decrease from rates in our base-case scenario in 2023, the year with the lowest DSCRs.
- Revenue. We have assumed that contracts renewed throughout the notes' term will face a haircut that will be double of that in our base-case scenario. Exceptions will be for Angostura, the rates of which have already set, and Santa Maria, for which we assume no renewal in the downside case.
- Operating expenses 12% higher than in our base-case scenario.
- Penalties equivalent to 1% of the project's revenue. This would result from maximum penalties (5% of the asset's revenues) for half of the portfolio in the regulated market.
- Given that notes have fixed interest rate, any changes in floating rates wouldn't affect the interest payments. During the refinancing period, we assumed the interest rate will be 200 basis points higher than in our base-case scenario, which is equivalent to 9%.

Key metrics

The most vulnerable phase of the project's life will start in 2040, given the 2039 expiration of Santa Maria-Charrua's contract. Our base-case scenario assumes that this contract will be renewed with a haircut of 15% as it turns regulated. However, under the downside-case scenario and because this asset is linked to a coal-fired generation unit, we assume the cancellation of this contract, which has a significant impact under our downside. The DSCRs are above 1.1x during the notes' term and the cash sweep mechanism from 2043 to 2051 aims to amortize about 10% of principal, which boosts the project's resiliency under the downside scenario, which we see as a credit positive.

Liquidity

We view the project's liquidity as neutral because of the funded six-month DSRA and three-month O&M reserve account. We also consider the cash lock-up mechanism, which ensures that the structure retains cash if the project-defined DSCR falls below 1.15x, which also supports the project's liquidity. This trigger is tested on a historical and projected 12-month basis.

Operation counterparties

The project has exposure to Chile-based generation company, Colbun. The latter was the former owner of transmission and substation assets that Alfa Transmisora acquired. The project has dedicated contracts with Colbun's power plants and these contracts represent about 35% of the project's total revenue. Because of the size of these contracts, Alfa Transmisora won't have a rating higher than 'BBB' due to its counterparty limitation. Currently, we don't believe this is affecting the project's credit quality.

Due to the simplicity of the operations, we consider O&M operators of transmission lines to be replaceable. In addition, the project has a three-month O&M reserve account, and there are many players in the market available to replace the O&M provider if needed.

Financial counterparties

None of the following counterparties constrain the rating: Citibank N.A. (A+/Stable/A-1) is the indenture trustee and offshore collateral agent, and Banco de Chile (A/Negative/A-1) is the onshore depository and collateral agent.

Parent linkage

The project's sponsors are APG and Celeo Redes. According to the notes' documentation, the existing debt will be the only debt in Alfa Transmisora's capital structure. In addition, there are provisions for additional debt, such as for working capital lines, but any new debt for new investments requested by the regulator is subject to rating confirmation. There are limitations and affirmative covenants, preventing affiliate transactions and no cross-default or parent-dependency provisions.

Structural protection

The project has a neutral structural protection because it has the typical protections for this type of structures, including:

- Limitation on additional debt, 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; and
- Maintain insurance coverage in favor of the project.

Rating Component Scores

Operations phase SACP (senior debt)

- Operations phase business assessment: 4

Preliminary operations phase SACP: bbb-

- Downside resiliency assessment and impact: High (+1 notch)
- Median DSCR impact: Neutral
- Debt structure impact: Neutral
- Liquidity impact: Neutral
- Refinancing impact: Neutral
- Future value modifier impact: Neutral
- Holistic analysis impact: (-1 notch)
- Structural protection impact: Neutral
- Counterparty assessment impact: Neutral

Operations phase SACP: bbb-

Parent linkage and external influences (senior debt)

- Parent linkage: Delinked

Project SACP: bbb-

- Extraordinary government: Neutral

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- Sovereign rating limits: A
- Full credit guarantees: Neutral

Senior debt issue rating: BBB-

Related Criteria

- General Project Finance Rating Methodology, Dec. 14, 2022
- Sector-Specific Project Finance Rating Methodology, Dec. 14, 2022
- Sector and Industry Variables: Project Finance Rating Methodology, Dec. 14, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Structured Finance | General: Counterparty Risk Framework: Methodology And Assumptions, March 8, 2019
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Global Investment Criteria For Temporary Investments In Transaction Accounts, May 31, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings Detail (as of December 27, 2022)*

Alfa Transmisora de Energia S.A.

Senior Secured

BBB-/Stable

US\$1.099 bil 4.55% bnds due 09/27/2051

Foreign Currency

BBB-/Stable

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country.

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