S&P Global
Ratings

RatingsDirect®

Celeo Redes Operacion Chile S.A.

March 22, 2023

PRIMARY CONTACT

Gaston Falcone
Buenos Aires
54-11-4891-2147
gaston.falcone
@spglobal.com

ADDITIONAL CONTACT

Marcelo Schwarz, CFA
Sao Paulo
55-11-3039-9782
marcelo.schwarz
@spglobal.com

Project Description

Celeo Redes Operación Chile S.A. (CROCH) operates two trunk transmission lines in Chile's power grid. The assets benefit from perpetual concessions granted by the Ministry of Energy in which revenues aren't subject to any demand risk and aren't based on the 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 is entitled to receive fixed availability payments until 2035, and AJTE circuit 2 receives the same type of payments with reviews every four years. AJTE circuit 1 has been operating 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 2037.

Based on the concession contracts, CROCH receives fixed revenue based on its availability, providing predictable revenue flow with no exposure to market risk. Rates are in place for a 20-year period since the commercial operations date (COD) for AJTE circuit 1 and CHATE lines, whereas the regulator revises rates for AJTE circuit 2 every four years. The latter represents about 20% of total revenues.

Credit Highlights

Overview

Key strengths	Key risks
Perpetual concession agreement that stipulates the project's revenue based on its availability, eliminating market risk.	After a first 20-year fixed tariff period, the regulation will reset and apply a new tariff for the project’s main assets in 2035-2037.
Project's business model results in stable and predictable cash flows.	Although we see them as one-off events in nature, delays in the 2020-2023 tariff review process negatively affected metrics in 2021 and 2022.

We expect the project to post stable and predictable metrics due to the availability-based remuneration of its assets, regardless of utilization rate. CROCH benefits from a dollar-denominated, 20-year fixed tariff period since the assets started operating, which the regulator will subsequently revise every four years. These assets represent around 80% of CROCH's total assets. The tariff or trunk transmission annuity value (VATT) includes two components: an investment value annuity (AVI) that's adjusted to U.S. inflation and a reimbursement for operating expenses (COMA) indexed to Chile's inflation and foreign currency movements. For expansion assets, the regulator revises the VATT every four years since the COD, following the same procedure as for CROCH's main assets. As a result, fixed tariffs and CROCH's availability-based business model allow the project to post predictable, stable cash flows and credit metrics. The availability payments come from the electricity system, and in our view, delays in payment chain wouldn't hurt the project's cash flow available for debt service (CFADS).

Regulation assures a strong and stable financial performance during the 20-year fixed tariff period and subsequently with the tariffs resetting every four years. In our base-case scenario, the project will reach a minimum debt service coverage ratio (DSCR) slightly above 1.20x in 2023, and a median DSCR of about 1.38x during the notes' term, helped by higher U.S. inflation rates. We consider U.S and domestic inflation as relevant variables that could affect the project's metrics, because its revenues are adjusted to them. We also incorporate some risk of volatility in our analysis because the fixed-tariff period for AJTE and CHATE ends in 2035 and 2037, respectively, when there will still be 10 years until the total amortization of the notes in 2047. This exposes the project to the regulatory tariff review every four years for its main assets. When the fixed tariff period ends, the regulator will recalculate the transmission line's remuneration, incorporating the asset's replacement value and an after-tax return on investment ranging between 7% and 10%.

The lengthy regulatory delays resulted in unexpected changes for CROCH. Delays around the tariff setting process for 2020-2023 resulted in unexpected swings in CROCH's DSCRs in 2020-2022 (please see "**Chilean Electricity Transmission Firm Celeo Redes Operacion Chile 'BBB' Debt Rating Affirmed, Outlook Still Stable**," Feb. 25, 2021). Even though the final tariff decree was recently published, we don't view these delays as positive, despite considering them as one-off events somewhat affected by the pandemic. Absent unexpected regulatory hiccups, we expect CROCH to post steady cash flows and metrics through the notes' term. In our view, the higher volatility in CROCH's performance in 2020-2022 was mostly due to factors that were out of the project's control, and those have been addressed and mostly overcome.

We still view the Chilean regulatory framework for the transmission lines as robust and predictable. We also consider the context of Chile's energy matrix decarbonization and the country's focus on that goal. However, if the regulator incurs further delays for the upcoming 2024-2027 tariff period, or if it introduces more material changes, our view of the regulatory framework may weaken.

Outlook

The stable outlook reflects our view of CROCH's stable cash flow in the next 12-24 months, resulting in a DSCR of 1.21x in 2023 and higher thereafter. We base this on our view of the unusual one-time delay related to the 2020-2023 tariff period and consider the project's long-term concession contracts at fixed prices for most of its assets and availability levels above the minimum regulatory requirement.

Downside scenario

A downgrade in the next two years is possible if the project's revenues are lower than we expect, for instance, if annual U.S. inflation decreases substantially in the next few years or if costs or income taxes are higher than we project, resulting in a minimum DSCR below 1.15x and a median DSCR below 1.25x while the project's downside resilience diminishes. We could also lower our rating if there are further, recurrent regulatory delays in the next tariff period, which could weaken our assessment of the regulatory framework.

Upside scenario

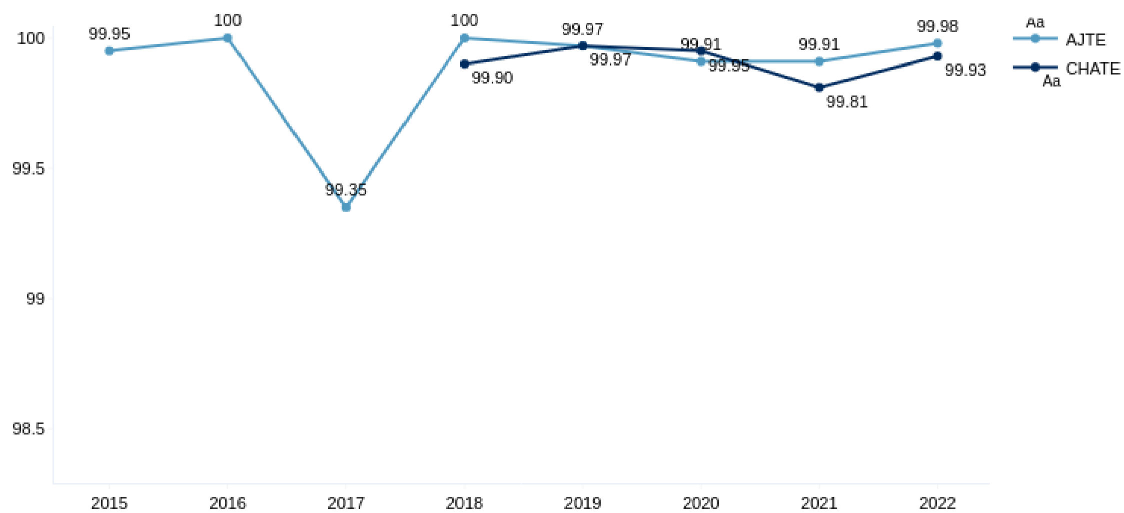
Although unlikely at this stage, we could upgrade Celeo Redes if its resilience to a downside-case scenario increases while it maintains a minimum DSCR above 1.30x.

Performance Update

The rating on CROCH reflects our expectation that it will post stable operating and financial performance in the next few years, supported by its availability and stable regulation. We expect a minimum DSCR of 1.21x and median DSCR of 1.38x during the notes' term thanks to relatively low operating complexity, its business model based on availability, and the current high inflation, which affects the cumulative inflation adjustment in the long term.

From an operational standpoint, the assets' availability in 2022 was in line with our expectations (above 99.8%), complying with the established limits with no penalties, fines, or accidents reported. We expect a similar operating performance going forward, which supports the project's cash flow predictability. Availability has remained steady since the assets began operating (see the chart below).

Availablity Evolution



Source: S&P Global Ratings, company filings.

From a financial standpoint, despite the stable operational performance, we highlight the somewhat bumpy road seen in 2021 and 2022, which we attribute to the regulatory delays for the 2020-2023 tariff review and the lower remuneration from the regulator for the expansion work on AJTE 2, partly offset by increased revenues from the fiber optic contract and a higher inflation. We already considered these factors in our articles "**Chilean Electricity Transmission Firm Celeo Redes Operacion Chile 'BBB' Debt Rating Affirmed, Outlook Still Stable**," published April 4, 2022, and "**Chilean Electricity Transmission Firm Celeo Redes Operacion Chile 'BBB' Debt Rating Affirmed, Outlook Still Stable**," published Feb. 25, 2021. With the official tariff decree finally published in February 2023, this process is concluded. We continue to view the regulatory delay as a one-off event, and we expect the upcoming 2024-2027 tariff review period to be smoother.

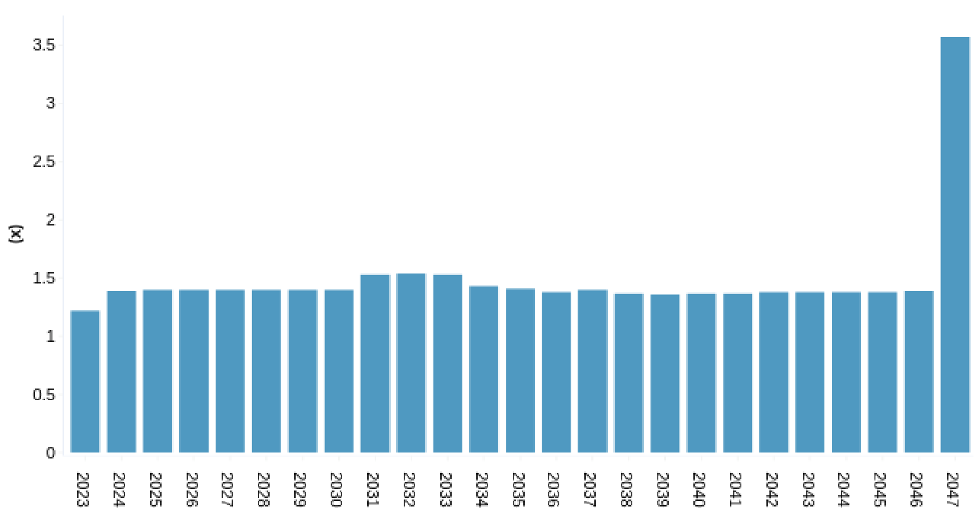
Base-case assumptions

- We consider key macroeconomic variables, such as inflation in the U.S. and Chile per our articles "**Economic Outlook U.S. Q1 2023: Tipping Toward Recession**," published on Nov. 28, 2022, and "**Economic Outlook Latin America Q1 2023: A Shift To Lower Growth**," published Nov. 28, 2022. We expect Chile's year-end consumer price index (CPI) of 5.5% in 2023 and 3.0% afterward; and U.S. CPI of 4.3% in 2023, 2.7% in 2024, 2.3% in 2025, and 2.1% afterward.
- Fixed rates adjusted to 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%. The new rate incorporates an after-tax return of 8%, the transmission lines' depreciable period of 50 years, and the relevant macroeconomic variables.
- We consider the revenues from the fiber optic agreement in place, which is within the scope of the project's business. This service contract has been approved by the regulator. The collection started in 2022 and CROCH will receive the balance in 2023 for a total of $4.75 million.
- The project will maintain the operations and maintenance (O&M) agreements with Celeo Redes Chile Ltd. (not rated), totaling about UF47,000 per year for AJTE's two circuits and about UF31,000 per year for CHATE, adjusted to Chile's 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 solid track record of the transmission lines and the operator.

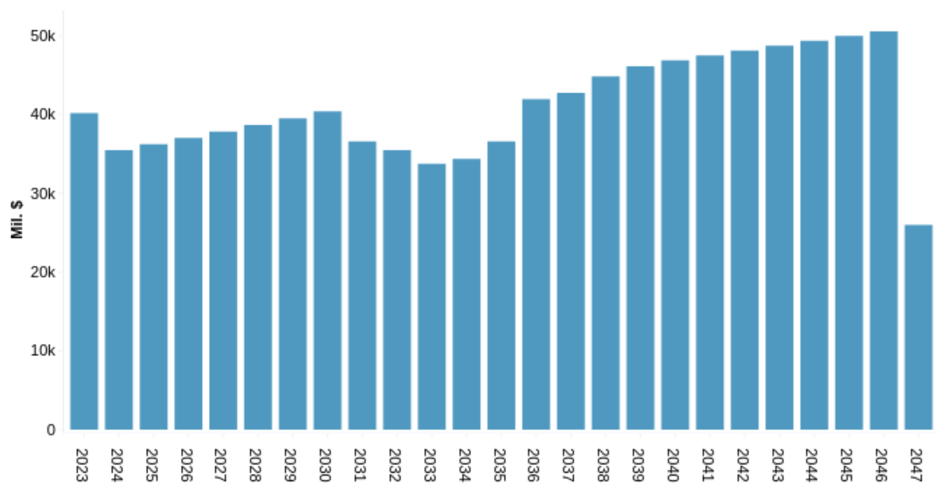
Key metrics

With these assumptions, we expect a minimum DSCR of 1.21x in 2023 and a median DSCR of 1.38x during the notes' term.

CROCH's DSCRs



CROCH's Debt Repayments



Source: S&P Global Ratings.

Deriving The Preliminary Operations Phase SACP

	--Minimum DSCR ranges*--				
	aa	a	bbb	bb	b
OPBA					
1-2	=> 1.75	1.75-1.20	1.20-1.10	1.10-1.05	<1.05
3-4	N/A	=> 1.40	1.40-1.175	1.175- 1.10	<1.10
5-6	N/A	=> 1.75	1.75-1.30	1.30-1.15	<1.15
7-8	N/A	=> 2.50	2.50-1.60	1.60-1.35	<1.35
9-10	N/A	=> 5.00	5.00-2.50	2.50-1.50	<1.50
11-12	N/A	N/A	N/A	=>3.00	<3.00

*DSCR ranges include values at the lower bound, but not the upper bound. For example, 1.20x-1.10x includes 1.10x, but excludes 1.20x. SACP--Stand-alone credit profile. N/A--Not applicable. DSCR--Debt service coverage ratio.

Downside-case assumptions

- We stress U.S. inflation because it has a positive effect on the project's revenues. We assume a 100 basis point (bps) decrease in the U.S. rate from our base-case scenario.
- We don't stress for foreign exchange exposure due to the natural hedge in place (the share of dollar-denominated versus local currency-denominated debt mimics the share of dollar/local currency revenues) and the active cash management that results in an extremely low intra-month exposure.
- After the initial regulated period, we apply a 10% haircut on the base case annual tariff revenue to capture a lower after-tax return (7%). We also keep a two-month delay in payment from the largest generator for a five-year period starting in 2022.
- Operational expenses 12% higher than in our base-case scenario.
- Penalties of about $1.8 million for five years, starting from the weakest phase of the project due to unavailability (3.5%).

Key metrics

We expect a minimum DSCR of 1.06x in 2023 and median DSCR above 1.14x during the notes' term. Although the metrics remain above 1.00x, they don't provide additional upside to the ratings at this level.

Liquidity

We assess the project's liquidity as neutral because it has sufficient cash sources (cash on hand, available liquidity reserves, and forecast CFADS) to cover expected debt service payments over the next 12 months by at least 1x. The six-month debt service reserve account and three-month O&M reserve accounts are funded with cash. 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.

Rating Component Scores

Senior debt issue rating: BBB

Operations phase (senior debt)

- Asset class operating stability: 3
- Operations phase business assessment: 3

Preliminary operations phase SACP: bbb-

- Downside resiliency assessment and impact: Moderate (Neutral)
- Median DSCR impact: Neutral
- Debt structure impact: Neutral
- Liquidity impact: Neutral
- Refinancing impact: Neutral
- Future value modifier impact: Positive (+1 notch)
- Holistic analysis impact: Neutral
- Structural protection impact: Neutral
- Counterparty assessment impact: No impact at this stage

Operations phase SACP: bbb

Parent linkage and external influences (senior debt)

Parent linkage: Delinked

Project SACP: bbb

- Extraordinary government support: N/A
- Sovereign rating limits: N/A
- Full credit guarantees: N/A

Related Criteria

- Criteria | Infrastructure | General: Sector-Specific Project Finance Rating Methodology, Dec. 14, 2022
- Criteria | Infrastructure | General: General 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 March 22, 2023)*

Celeo Redes Operacion Chile S.A.	
Senior Secured	BBB/Stable
US$379 mil 5.20% nts ser A due 06/22/2047	
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.