

Fitch Affirms ISA Capital do Brasil's IDRs at 'BB+'/'AA-(bra)' Ratings Endorsement Policy 25 Jun 2012 11:24 AM (EDT)

Fitch Ratings-Chicago-25 June 2012: 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 of '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.

ISA Capital do Brasil's ratings reflect the strong credit quality of CTEEP [Fitch IDR of 'AA+(bra)'], its sole revenue source and only operating asset. CTEEP's strong credit quality is attributable to its monopoly position, its stable and predictable operating cash flow and its financially sound credit profile. The ratings also reflect the noteholders' structural subordination to CTEEP's obligations, as well as the company's concession renewal and refinancing risks.

The one-notch rating difference for ISA Capital's 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 (BRL57 million) of outstanding debt is secured by a significant portion of ISA Capital's shares of CTEEP.

STRONG CREDIT METRICS:

ISA Capital's credit quality reflects the company's structural subordination to CTEEP's obligations given that ISA only owns 37.8% of its total capital and does not receive the full benefits of operating cash flow. CTEEP's leverage is considered adequate for the rating category, and ISA Capital's capital structure has marginally improved after the company repurchased the bulk of its debt outstanding and refinanced it with preferred equity. As of Dec. 31, 2011, ISA Capital consolidated debt amounted to approximately BRL4.0 billion. This debt consisted of approximately BRL2.8 billion at CTEEP and BRL1.2 billion at ISA Capital (including its preferred shares). This translates into a leverage ratio of 2.8 times (x) on a consolidated basis.

CTEEP's cash flow generation and cash flow distributions (dividends) to ISA Capital are stable and predictable. ISA Capital's consolidated FFO interest coverage ratio of approximately 7.2x as of Dec. 31, 2011 was considered strong for the rating category. During 2011, ISA Capital received approximately BRL340 million of dividends from CTEEP. Going forward, distributions from CTEEP's are expected to range between BRL250 million and BRL300 million per year, which ISA Capital will use to pay dividends on preferred equity and service the remaining portion of the 2017 bonds not tendered during 2010. Alternatively, ISA Capital is contemplating growth alternatives outside CTEEP that could demand use of liquidity. The company expects to fund acquisitions with cash on hand and dividends received from CTEEP, without raising significant amounts of additional debt at the holding company level.

LOW BUSINESS RISK AND STABLE CASH FLOW GENERATION:

CTEEP's monopoly position stems from its exclusive right to provide electricity transmission services through its two concessions, which expire in 2015 and 2031. Furthermore, two CTEEP's concessions are located in the state of Sao Paulo, which accounts for one-third of Brazil's overall GDP, making it one of the largest electricity consumers in the country. CTEEP's strong market position should further benefit the company when it participates in future bids for new transmission lines. Whether or not the regulator renews the company's concession in 2015 is uncertain.

CTEEP cash flow generation is very stable and predictable, exhibiting the low business risk profile of an electric transmission utility company. CTEEP's tariff-setting mechanism is straightforward, receiving minor intervention from its regulator. The company's tariffs are fixed and adjusted by inflation every year, and 77.3% of its revenues will not be revised by the regulator until 2015. The balance is revised every four years. Furthermore, CTEEP's revenues are exempt from volumetric risk as its maximum permitted annual revenue (PAR) is based on the electricity transmission assets available to users, instead of the transmitted electricity.

CONCESSION RENEWAL RISK:

CTEEP generates the majority of its revenue through a concession that expires in 2015, which is automatically adjusted annually by inflation and regulator-approved investments. Whether or not the government renews the

company's concession in 2015 is uncertain, and this risk has been incorporated in the rating. This concession can be renewed for a period of 20 years at the government's discretion. Should the government not renew CTEEP's concession in 2015, the company is entitled to receive compensation for the value of its assets net of depreciation. If this were to happen, the expected compensation plus CTEEP's retained earnings are expected to generate enough distributions for the holding company to service its financial obligations.

KEY RATING DRIVERS:

Any ISA Capital rating changes will reflect changes in CTEEP's credit quality, which could be negatively affected by a significant, or above-expectation increase in leverage; regulatory intervention in the tariff adjustment process; heightened uncertainty regarding concession renegotiation process; and if relevant off-balance-sheet contingencies become mandatory. Improving macroeconomic conditions in Brazil coupled with a Sovereign rating upgrade and a continuously strong corporate financial profile could lead to a positive ratings impact. A significant change in ISA Capital stand-alone capital structure that could result from the company's expansion plan could also impact the rating.

Contact:

Primary Analyst

Lucas Aristizabal
Director
+1-312-368-3260
Fitch, Inc.
70 W Madison, Street
Chicago, IL 60602

Secondary Analyst

Mauro Storino
Director
+55-21-4503-2600

Committee Chairperson

Ricardo Carvalho
Senior Director
+55-21-4503-2600

Media Relations: Elizabeth Fogerty, New York, Tel: +1 (212) 908 0526, Email: elizabeth.fogerty@fitchratings.com.

Additional information is available at 'www.fitchratings.com'. The ratings above were solicited by, or on behalf of, the issuer, and therefore, Fitch has been compensated for the provision of the ratings.

Applicable Criteria and Related Research:

--'Corporate Rating Methodology' (Aug. 16, 2010);
--'Parent and Subsidiary Rating Linkage Criteria Report' (July 14, 2010);
--'Equity Credit for Hybrids & Other Capital Securities' (Dec. 29, 2009).

Applicable Criteria and Related Research:

Corporate Rating Methodology
Parent and Subsidiary Rating Linkage
Equity Credit for Hybrids and Other Capital Securities: Market Feedback and Fitch's Responses

ALL FITCH CREDIT RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTP://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS](http://FITCHRATINGS.COM/UNDERSTANDINGCREDITRATINGS). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE 'WWW.FITCHRATINGS.COM'. PUBLISHED RATINGS, CRITERIA AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. FITCH'S CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE 'CODE OF CONDUCT' SECTION OF THIS SITE.