

Rating Action: Moody's takes rating actions on specific issuers of the Brazilian infrastructure sector

Global Credit Research - 05 Jul 2016

Action follows the downgrade of the state of Minas Gerais to B1 from Ba3 with a negative outlook, and the outlook change on the state of Parana (Ba3/A1.br) to negative from stable.

Sao Paulo, July 05, 2016 -- Moody's America Latina Ltda. ("Moody's") took the following rating actions on specific electric and water utilities as a result of the downgrade of the global scale issuer rating of the state of Minas Gerais to B1 from Ba3 with a negative outlook, and of the outlook change for the issuer ratings of the state of Parana (Ba3/A1.br) to negative from stable. For more information, please see [https://www.moody's.com/research/Moodys-downgrades-Minas-Gerais-issuer-rating-to-B1-from-Ba3--PR_351488] and [https://www.moody's.com/research/Moodys-downgrades-ratings-of-the-state-of-Bahia-to-Ba3A2br--PR_350980]

The issuers and ratings impacted are as follows :

Companhia Energética de Minas Gerais (CEMIG)

Issuer ratings downgraded to B1/Baa1.br from Ba3/A1.br (on the global scale and on the national scale, respectively) with a negative outlook on all ratings.

CEMIG Distribuição S.A. (CEMIG-D)

Issuer ratings downgraded to B1/Baa1.br from Ba3/A2.br.

Ratings of backed senior unsecured Brazilian debentures downgraded to B1/Baa1.br from Ba3/A2.br, with a negative outlook on all ratings.

CEMIG Geração e Transmissão S.A. (CEMIG-GT)

Corporate Family Ratings (CFR) downgraded to B1/Baa1.br from Ba3/A1.br

Ratings of backed senior unsecured Brazilian debentures downgraded to B1/Baa1.br from Ba3/A1.br, with a negative outlook on all ratings.

Companhia de Saneamento de Minas Gerais S.A. (COPASA)

CFRs downgraded to B1/Baa1.br from Ba3/A2.br.

Ratings of senior unsecured Brazilian debentures downgraded to B1/Baa1.br from Ba3/A2.br, with a negative outlook on all ratings.

Companhia de Saneamento do Paraná -- (SANEPAR)

Issuer ratings affirmed at Ba3/A1.br.

Ratings on senior unsecured Brazilian debentures affirmed to Ba3/A1.br.

Outlook changed to negative from stable on all ratings.

RATINGS RATIONALE

The downgrade of ratings for CEMIG, CEMIG-D, CEMIG-GT and COPASA reflects primarily the downgrade of the state of Minas Gerais to B1 from Ba3 with a negative outlook as a result of the quick deterioration of the state's fiscal position. Likewise the outlook change for the ratings of SANEPAR follows the change in the outlook of the Ba3/A1.br ratings for the state of Parana to negative from stable.

Moody's believes that because of the strong influence the regional government as the controlling shareholder

exerts on these utilities' governance and financial condition, the rating of these utilities is constrained by the ratings of their controlling parent, respectively the Brazilian states of Minas Gerais for CEMIG, CEMIG-D, CEMIG-GT and COPASA; and the state of Parana for SANEPAR.

Those issuers are Government-Related Issuers or GRIs, as defined in Moody's rating methodology "Government-Related Issuers: Methodology Update", published in October 2014. Moody's methodology for GRIs incorporates into the rating both the stand-alone credit risk profile or Baseline Credit Assessment (BCA) of the company as well as an assessment of the likelihood that its government owner would provide extraordinary support to the company's obligations.

In addition to the impact from the change in the supporting regional government's ratings, the downgrade of CEMIG, CEMIG-GT and CEMIG-D's ratings also reflects materially lower operating margins, as a result of the ongoing challenging domestic economic conditions, as well as significantly higher leverage and cost of capital, which we expect will continue throughout the next 18 -- 24 months. According to Moody's standard adjustments, in the last 12 months ended on 31 March 2016, CEMIG's Net Debt to EBITDA increased to 4.7x from 3.0x in FY2015, while cash flow from operations (CFO) pre-working capital (W/C) to Debt decreased to 21.0% from 24.7%, and interest coverage ratio decreased to 3.4x from 3.8x. The ratings also reflect a more pressured liquidity position. As of 31 March 2016, CEMIG reported cash and cash equivalents of BRL1,989 million against debt maturing in the next 12 months of BRL4,911 million.

While directly exposed to the continuing effects from Brazil's economic recession, Moody's expects some improvements in COPASA's credit metrics going forward driven by a return to revenues growth resulting from more favorable hydrology conditions and by the benefit of cost cutting measures taken by the company late in 2015. COPASA's ratings continue to be constrained by high leverage position, evidenced by a debt/EBITDA ratio (as adjusted by Moody's) of 4.3x in the last twelve months ended 31 March 2016. The Ba3/A1.br issuer ratings for SANEPAR have been affirmed, based on Moody's view that the company's credit metrics evidenced by a FFO to Net Debt ratio of 32% and an interest coverage ratio of 4.3x in the last twelve months ended 31 March 2016 remain strong for the rating category.

WHAT COULD CHANGE THE RATING UP/DOWN

In light of the rating actions with the maintenance of the negative outlook, an upgrade of the ratings is unlikely in the short to medium term.

A deterioration of Brazil's sovereign credit quality could exert downward pressure on the assigned ratings. Further deterioration in the respective sub-sovereign's credit quality could exert downward pressure on these issuers. A sustained deterioration in the relevant credit metrics of the issuers on a standalone basis and/or, perception of a material deterioration in the regulatory frameworks under which these companies operate could also exert downward pressure.

The principal methodology used in rating Cemig Distribuicao S.A. and Cemig Geracao e Transmissao S.A. was Regulated Electric and Gas Utilities published in December 2013. The methodologies used in rating Companhia Energetica de Minas Gerais - CEMIG were Regulated Electric and Gas Utilities published in December 2013, and Government-Related Issuers published in October 2014. The methodologies used in rating Companhia de Saneamento do Parana - SANEPAR and Companhia de Saneamento de Minas Gerais - COPASA were Regulated Water Utilities published in December 2015, and Government-Related Issuers published in October 2014. Please see the Ratings Methodologies page on www.moodys.com.br for a copy of these methodologies.

Moody's National Scale Credit Ratings (NSRs) are intended as relative measures of creditworthiness among debt issues and issuers within a country, enabling market participants to better differentiate relative risks. NSRs differ from Moody's global scale credit ratings in that they are not globally comparable with the full universe of Moody's rated entities, but only with NSRs for other rated debt issues and issuers within the same country. NSRs are designated by a ".nn" country modifier signifying the relevant country, as in ".za" for South Africa. For further information on Moody's approach to national scale credit ratings, please refer to Moody's Credit rating Methodology published in May 2016 entitled "Mapping National Scale Ratings from Global Scale Ratings". While NSRs have no inherent absolute meaning in terms of default risk or expected loss, a historical probability of default consistent with a given NSR can be inferred from the GSR to which it maps back at that particular point in time. For information on the historical default rates associated with different global scale rating categories over different investment horizons, please see

https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_189530 .

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The date of the last Credit Rating Action for Cemig Distribuicao S.A. was 25/2/2016

The date of the last Credit Rating Action for Cemig Geracao e Transmissao S.A. was 9/5/2016

The date of the last Credit Rating Action for Companhia Energetica de Minas Gerais - CEMIG was 9/5/2016

The date of the last Credit Rating Action for Companhia de Saneamento do Parana - SANEPAR was 9/5/2016

The date of the last Credit Rating Action for Companhia de Saneamento de Minas Gerais was 25/2/2016

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