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Ratings

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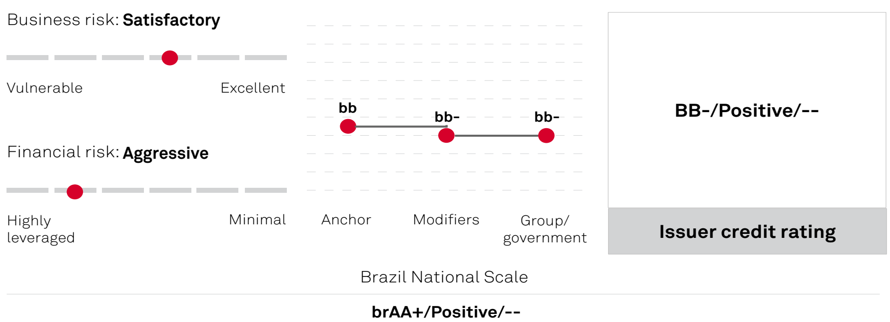
Companhia Energetica de Minas Gerais - Cemig

December 12, 2024

Ratings Score Snapshot



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Credit Highlights

Overview

Key strengths	Key risks
One of the largest utilities in Brazil, distributing electricity to 9.3 million clients in Minas Gerais, and benefiting from 4.5 gigawatts (GW) of installed generation capacity and over 5,000 kilometers (km) of transmission lines.	Potential capex execution risks as CEMIG will need to raise additional debt to finance investments, especially in 2026.
Strong cash generation from its business segments and recent asset sales have supported sound credit metrics in recent years, positioning the company to execute its capex plan.	Higher interest rates in Brazil hurt cash flow.
Regulation and restriction in debt contracts limit potential interference from the controlling shareholder.	Exposed to hydrological conditions risk and the volatility of energy spot prices, since CEMIG is a net buyer of energy to honor its power purchase agreements (PPAs).
Adequate regulatory framework.	Exposed to political cycles and fiscal strains in the state of Minas Gerais, although the state hasn't interfered in the company's operations in the past few years.

CEMIG's positive outlook reflects the chance of an upgrade if it improves cash generation while maintaining comfortable credit metrics. For 2024-2028, CEMIG plans to invest approximately R$35.6 billion in its core businesses--especially distribution, but also generation, and transmission of energy--located mainly in the state of Minas Gerais. This investment strategy is expected to result in an annual shortfall in free operating cash flow (FOCF) of R$1.5 billion – R$2.7 billion in 2025-2027, necessitating a potential doubling of debt from R$12 billion in 2024 to around R$24 billion by 2027, absent additional asset sales. While this raises execution risks, particularly in 2026 when investments peak at R$7 billion and negative FOCF reaches R$2.7 billion, we believe that if CEMIG maintains its strong operational performance and effectively obtains revenue from these investments, it could reduce its cash needs and sustain favorable credit metrics. In this sense, the positive outlook on CEMIG reflects our view that we could upgrade it on the global and national scale to 'BB' and 'brAAA' if it reports only moderately negative FOCF in the next few years, while maintaining adjusted net debt to EBITDA at 3.0x-3.5x and FFO to debt above 20%.

Operating performance is gradually improving. In 2024, the group received tariff adjustments above inflation (Brazil's Consumer Price Index as of October 2024 was 4.76%) for CEMIG-D and the transmission lines of CEMIG-GT of 7.32% and 5.2%, respectively, boosting our expectation of cash flow. In addition, CEMIG completed in 2024 the sale of its 45% stake in Aliança Energia S.A. to Vale S.A. for R$2.7 billion. The proceeds support the group's deleveraging, as it didn't have to access capital markets in the very short term to fully amortize CEMIG-GT's $381 million outstanding international notes, the repayment of which was completed on Dec. 5, 2024. In addition, the company is selling four hydro plants to Âmbar Hidroenergia Ltda. for R$52 million, which we expect to be completed by mid-2025. As a result, we expect CEMIG's adjusted net debt to EBITDA of about 2.5x and FFO to debt of 30% in 2024, and about 3.0x and 20%, respectively, in 2025 and 2026, considering that energy spreads will gradually normalize because of currently lower energy sales prices, basic interest rates will remain at higher levels for longer time in Brazil, and because of CEMIG's sizable investments.

The concession's expiration could pressure metrics in the medium term. We expect CEMIG's debt to EBITDA and FFO to debt to deteriorate in 2027 and 2028 to 3.5x and 15%-20% (from 3.0x and 20%) because the concession for 1,780 megawatts (MW) of CEMIG-GT's installed capacity will expire in 2027 (for the Emborcação, Nova Ponte, and Sá Carvalho hydro plants). While CEMIG intends to renew it, the process also depends on the granting authority. If CEMIG is unable to renew the concession, which could also require renewal fees depending on the renewal format, EBITDA could shrink by up to R$900 million, and the group would have to buy additional energy in the market to honor its PPAs. This could increase the group's exposure to electricity prices in the long term, in our view.

The privatization process is still uncertain. On Nov. 14, 2024, the state of Minas Gerais notified CEMIG that it proposed a bill for its privatization. Unless a proposed change to the state constitution is accepted, the privatization would require approval from a popular referendum, which is unlikely given the public's low acceptance of the matter. Finally, it would also depend on legislative approval, which is uncertain. We'll monitor any new development and reassess the implications for CEMIG, especially in terms of governance in case it is privatized.

Our rating on CEMIG incorporates the risks of political cycles stemming from its state ownership. Although the state of Minas Gerais hasn't interfered in CEMIG's operations in the past few years, we capture in the M&G assessment political risks that stem from the company's control by the state, which owns 50.97% of voting shares and 17.04% of total shares of CEMIG. In the past, the company faced refinancing issues after its controlling shareholder drained cash from the company through dividends. The new management team, in place since 2019, has been improving CEMIG's operating and financial position, as seen in the anticipated partial refinancing of CEMIG-GT's international bonds, although we believe the group remains exposed to political cycles, especially because the current administration has only two years of its second mandate remaining, and can't be reelected.

Outlook

The positive outlook reflects our view that we could upgrade CEMIG and its subsidiaries in the next 12-24 months if its sizable investments bolster cash generation, which would narrow its FOCF shortfall, while maintaining debt to EBITDA at less than 3.5x and FFO to debt of more than 20% in the medium term.

Downside scenario

We could revise the outlook back to stable or even lower the ratings on CEMIG and its subsidiaries if the group's credit metrics worsen, with debt to EBITDA consistently above 4.5x, FFO to debt below 13%, and negative FOCF. In our view, cash flow could worsen due to consistently higher energy costs if hydrological conditions weaken throughout 2025. Weaker credit metrics could also result from much higher-than-expected investments or a large debt-financed acquisition without the offsetting cash flow. We could also downgrade CEMIG if its liquidity worsens either because of refinancing challenges or due to tight covenant headroom.

Upside scenario

We could upgrade CEMIG to 'BB' and to 'brAAA' if it reports a narrower FOCF shortfall in the next few years, especially in 2026, while maintaining strong credit metrics. Specifically, we would need to see FFO to debt above 20% and debt to EBITDA below 3.5x on a consistent basis, provided that the state of Minas Gerais continues to refrain from interfering in the group's operations. Credit metrics could strengthen, for instance, if CEMIG generates higher cash from its investments or if it continues selling its assets to prepay the outstanding debt.

Our Base-Case Scenario

Assumptions

- Brazil's GDP to grow 3.1% in 2024, 1.9% in 2025, and 2.1% in 2026, in line with "Economic Outlook Emerging Markets Q1 2025: Trade Uncertainty Threatens Growth", Nov. 26, 2024. Nevertheless, we expect CEMIG's energy consumption at the distribution business to grow below the GDP rate, at about 1.5% in 2024 and 0%-1% afterward as a result of the migration of captive clients to the distributed generation segment and free market.
- In 2024, we incorporate the rate adjustment of 7.32% for CEMIG-D, which has been approved by Brazil's electricity regulator. We forecast rates increasing in line with inflation of previous year--4.3% in 2025 and 4.2% in 2026.
- The average cost of energy in the distribution business will be R$295 per megawatt hour (MWh) and increasing in line with inflation starting in 2025. We assume favorable hydrological conditions in 2025 as a result of the recovery of the reservoir capacity during the wet season in 2024-2025.
- A global scaling factor, which determines the group's level of energy delivery, of roughly 85% starting in 2024.
- The average sale price of energy at R$175/MWh - R$180/MWh in 2024, R$170 - R$175 in 2025, and around R$180 in 2026, considering the existing contracts. We assume average energy purchase costs of R$90/MWh - R$100/MWh starting in 2024, reflecting still favorable hydrological conditions.
- RAP of CEMIG's transmission lines of about R$1.36 billion in the 2024-2025 cycle and increasing in line with inflation starting in 2025. New projects and the modernization and reinforcement of the transmission lines should support

higher RAP going forward. We expect net revenue in the segment of about R$1.20 billion in 2024, R$1.26 billion in 2025, and R$1.3 billion in 2026.

- Annual investments of about R$5.8 billion in 2024, R$5.7 billion in 2025, and peaking at R$7.0 billion in 2026, assuming 90% of the group's budget plan, because the capex execution has historically been below target.
- The basic interest rate at the end of the year of 11.75% in 2024, 11.25% in 2025, and 9.5% in 2026, affecting the group's interest expenses.
- Although the group plans additional minority stakes divestments, we don't incorporate them, given the uncertain timing. We incorporate the sale of noncore equity investments that were completed in 2024, such as Aliança Energia (R$2.7 billion) and 15 small power plants (R$100.5 million), and the sale of four hydro plants to Ambar in 2025 for R$52 million.
- The payment of CEMIG-GT's outstanding $381 million notes in December 2024.
- Dividends received from affiliates of R$380 million - R$430 million in the next few years.
- The dividend payout of 50% of the previous year's net income starting in 2024, totaling R$2.7 billion this year.
- Our adjusted debt figures include pension-related liabilities (about R$5.4 billion) and financial guarantees provided to Belo Monte, CEMIG's equity affiliate, for R$3.3 billion.

Key metrics

Company Description

CEMIG is one of the largest utility groups in Brazil. It operates in the electricity and gas distribution (about 60% of EBITDA), generation and energy trading (25%-30%), and transmission (10%-15%) segments. The group is responsible for distributing electricity to its roughly 9.3 million clients in the state of Minas Gerais, which is one of the most densely populated states in Brazil. In addition, CEMIG has 4.5 gigawatts (GW) of installed capacity across 61 power plants and benefits from 5,060 km of power transmission lines, including stakes in equity method investments. CEMIG is controlled by the state of Minas Gerais, which has 50.97% of voting shares and 17.04% of total shares.

Peer Comparison

Companhia Energética de Minas Gerais – CEMIG --Peer Comparisons

	Companhia Energética de Minas Gerais – CEMIG	CPFL Energia S.A.	Equatorial S.A.	Energisa S.A.	Neoenergia S.A.
Foreign currency issuer credit rating	BB-/Positive/--	-	-	BB/Stable/--	BB/Stable/--
Local currency issuer credit rating	BB-/Positive/--	-	-	BB/Stable/--	BB/Stable/--
National Scale	brAA+/Positive/--	brAAA/Stable/--	brAAA/Stable/--	brAAA/Stable/--	brAAA/Stable/brA-1+
Period	Annual	Annual	Annual	Annual	Annual
Period ending	12/31/2023	12/31/2023	12/31/2023	12/31/2023	12/31/2023
Mil.	R$	R$	R$	R$	R$

Revenue	30,089.1	34,753.8	31,030.3	23,770.2	35,387.0
EBITDA	6,239.9	12,268.6	8,759.7	7,398.0	10,499.0
Funds from operations (FFO)	4,607.8	8,034.2	3,982.5	4,308.6	6,990.0
Interest expense	1,782.3	2,237.8	4,856.7	2,830.8	4,398.0
Cash interest paid	1,031.4	1,901.2	4,400.7	2,513.7	3,044.0
Cash flow from operations	6,644.3	8,861.1	3,139.2	4,168.7	1,632.0
Capital expenditure	4,942.1	4,452.3	9,148.1	4,887.0	8,903.0
Free operating cash flow (FOCF)	1,702.2	4,408.8	-6,008.9	-718.3	-7,271.0
Discretionary cash flow (DCF)	-120.8	838.3	-6,805.6	-151.6	-8,688.0
Cash and short-term investments	2,311.5	5,532.6	12,237.7	7,388.6	7,522.0
Debt	16,341.3	27,094.8	40,538.1	25,954.9	44,860.0
Equity	24,655.2	19,998.8	25,062.7	15,135.5	30,076.0
Adjusted ratios					
EBITDA margin (%)	20.7	35.3	28.2	31.1	29.7
Return on capital (%)	12.9	24.2	12.9	17.5	13.8
EBITDA interest coverage (x)	3.5	5.5	1.8	2.6	2.4
FFO cash interest coverage (x)	5.5	5.2	1.9	2.7	3.3
Debt/EBITDA (x)	2.6	2.2	4.6	3.5	4.3
FFO/debt (%)	28.2	29.7	9.8	16.6	15.6
Cash flow from operations/debt (%)	40.7	32.7	7.7	16.1	3.6
FOCF/debt (%)	10.4	16.3	-14.8	-2.8	-16.2
DCF/debt (%)	-0.7	3.1	-16.8	-0.6	-19.4

We compare CEMIG's to other integrated energy players that also operate in Brazil's electric sector, such as CPFL Energia S.A., Neoenergia S.A., Equatorial Energia S.A., and Energisa S.A. All of them operate in the distribution, generation, and transmission segments. CEMIG compares well to these peers in terms of diversification and scale.

The regulated segment, which includes distribution and transmission, contributes the bulk of revenue for all the players, although the generation segment is responsible for 25%-30% of CEMIG's EBITDA, similar to CPFL. For Neoenergia and Equatorial, the generation segment's EBITDA share grew in the past few years due to acquisitions and newer projects, but it only accounts for 10%-15% of EBITDA. Lastly, Energisa has the smallest generation-linked portion of EBITDA, less than 5%.

Overall, energy groups in Brazil are planning to invest heavily in the next couple of years, which weighs on their financial risk profile. This is the case for CEMIG, Neoenergia, and Equatorial. CPFL and Energisa also plan sizable capex, but in their case, we expect consistently stronger credit metrics and positive free operating cash flows. Although CEMIG's credit metrics are strong at this point, we expect them to slip in the medium term, while cash deficits will be financed with additional debt. In this sense, we still view CEMIG as more comparable to peers with aggressive growth strategies, such as Equatorial and Neoenergia.

Business Risk

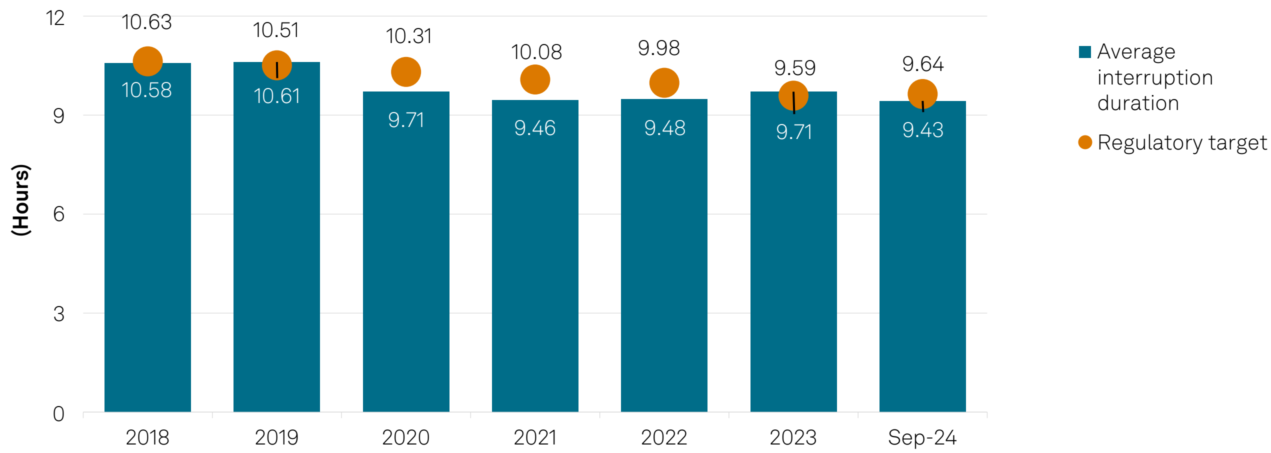
We view the regulatory framework in Brazil as credit supportive. The electricity regulator sets the rates for distribution and transmission companies to remunerate the investments made in the concession area. Rate setting for transmitters is simpler, because these companies receive revenue according to their availability to the system. Distribution companies currently operate under a model of pass-through costs, along with the remuneration of their investments. They receive rate readjustments every four to five years (depending on the concession contract; CEMIG-D's rate reviews occur every five years and its latest cycle began in May 2023). Rate adjustments allow the companies to pass through to the clients the electricity costs incurred, and general and administrative-related expenses, which are pegged to inflation. In each cycle, the regulator sets a new weighted average cost of capital to remunerate the investments during the concession.

In the past few years, CEMIG-D has been implementing cost-reduction and efficiency measures in its concession area, as well as investing to connect new clients and renovate its distribution network. This has allowed the distributor to reach its regulatory EBITDA target in the third quarter of 2021. CEMIG-D plans to invest roughly R$23 billion in 2024-2028, which will allow the company to incorporate efficiency gains in the next rate review cycle, beginning in May 2028.

That also includes investments to improve quality indicators in CEMIG-D's concession area. CEMIG's average interruption duration index has been within the regulatory targets since the first quarter of 2024, after it breached the limit in 2023 mainly due to extreme weather in Minas Gerais. We expect the company to continue investing in new distribution substations, system reinforcement and redundancy, and preventive maintenance, aiming to maintain quality indicators within regulatory limits. Improved quality metrics help the distributors because this lowers discounts applied to electricity bills as well as the risk of not distributing dividends (in case of noncompliance for more than two years) and even concession termination (for more than three years of noncompliance).

Moreover, the company continues investing in reducing energy losses. In the 12 months ended September 2024, energy losses were slightly above regulatory targets, underpinned by higher consumption as a result of higher temperatures. We expect the company's efforts to upgrade obsolete energy metering, disconnect delinquent customers, broaden payment options, and renegotiating outstanding bills with customers will help reach the regulatory target going forward.

System Average Interruption Duration (DEC) Index



Source: S&P Global Ratings and CEMIG.

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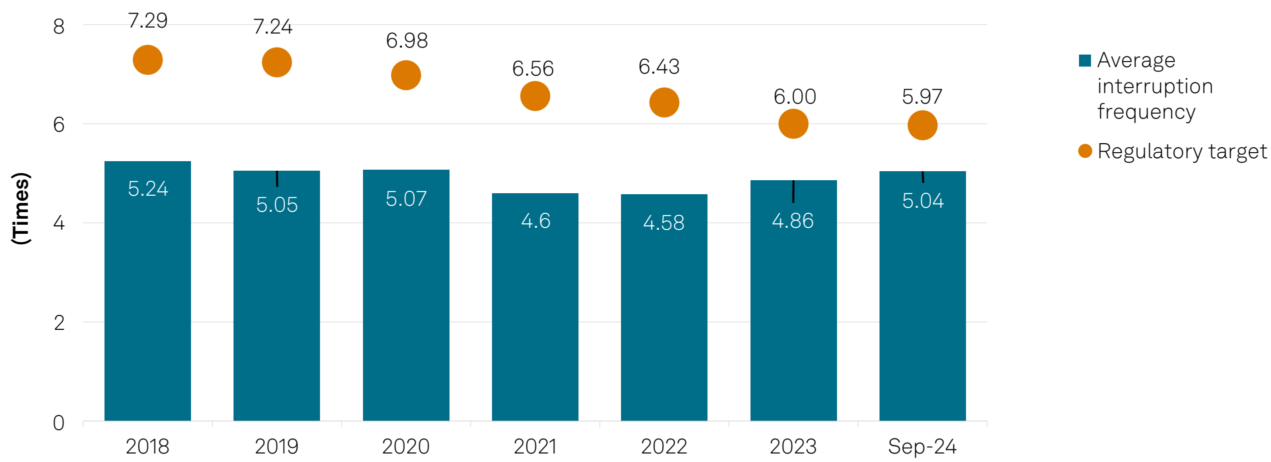
System Average Interruption Frequency (FEC) Index



Source: S&P Global Ratings and CEMIG.

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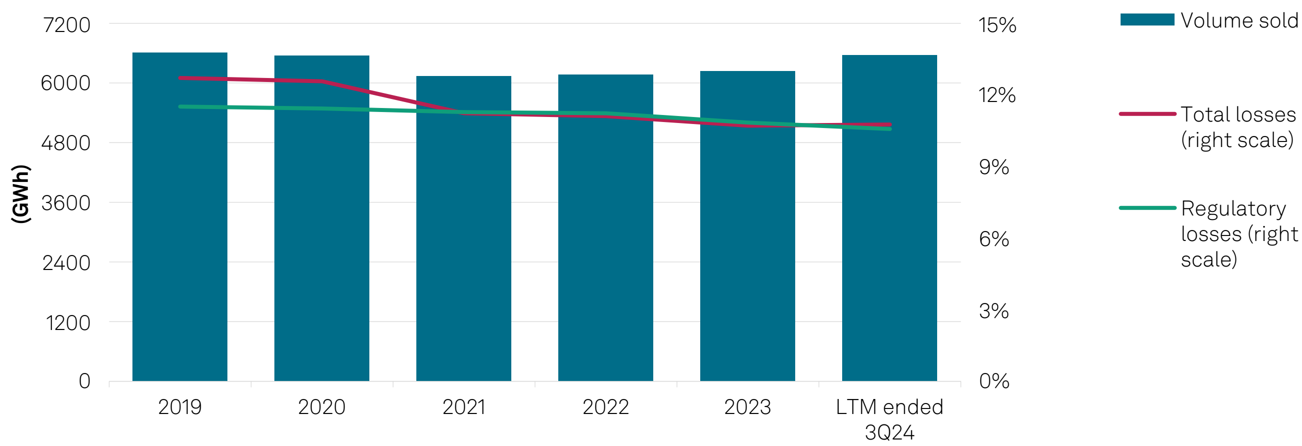
CEMIG - Eletricity Losses



Source: S&P Global Ratings and CEMIG.

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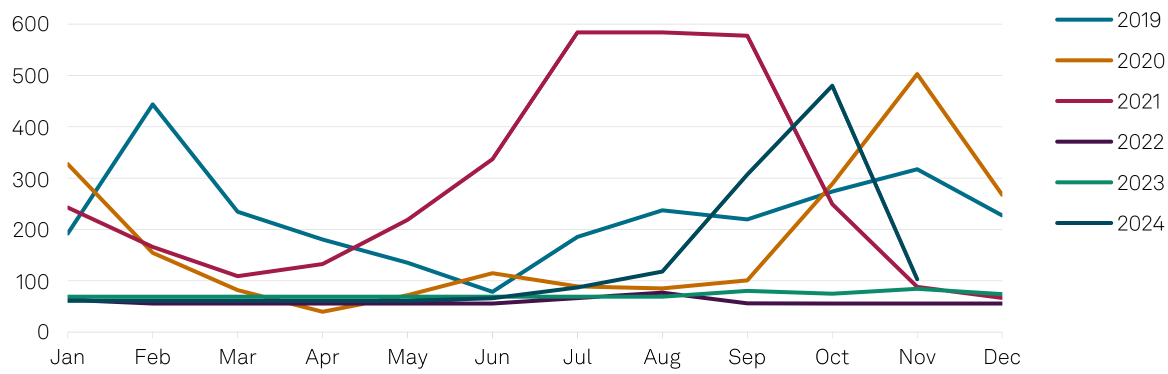
In the transmission segment, CEMIG-GT benefits from about 5,060 km of power transmission lines through 73 lines and 40 substations, with a gross RAP of R$1.36 billion in the 2024-2025 cycle. CEMIG-GT also holds a 21.68% stake in Transmissora Aliança de Energia Elétrica S.A. (Taesa; not rated), contributing roughly R$400 million annually in dividends to CEMIG. CEMIG-GT plans to invest about R$3.8 billion to reinforce and upgrade its transmission lines, which should also increase RAP. We expect these investments will result in stable cash flow in the transmission segment, given that CEMIG has maintained over 99.9% availability on its lines.

Power generators tend to mitigate cash-flow volatility through long-term power sale contracts to distribution companies and unregulated consumers. CEMIG-GT, which is responsible for the company's generation capacity, has an asset base mostly consisting of hydro plants and sells its energy mostly in the unregulated market through a mix of short- and long-term contracts. The company's generation capacity meets 30%-40% of its PPAs, making it a net buyer of energy. In our view, this is a risk relative to peers that have a more balanced energy portfolio, because it exposes CEMIG's cash flow to volatile energy prices. That will be exacerbated in case the company is unable to renew 1,780 MW of installed capacity that will expire by 2027.

We continue expecting overall low energy prices, assuming average rainfalls in 2024 and 2025 wet period that has just started. That should benefit CEMIG-D with low working capital requirements, while the generation segment will face lower spreads, after benefiting from high PPA prices in 2022-2024 that were negotiated at higher levels during the 2021 drought, and low energy purchase prices that followed.

Energy spot prices in the Southeast/Midwest subsystem (in R$/MWh)

In the period 2019-2024



Source: S&P Global Ratings and CCEE.

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Financial Risk

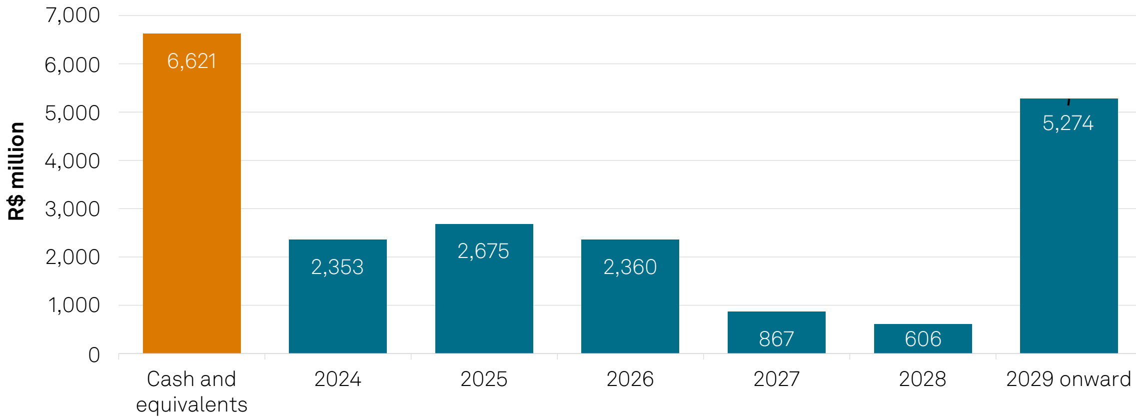
The company has a sizable capex plan of R$35.6 billion until 2028 that will require additional debt to finance. As a result, we expect negative FOCF ranging between R$1.5 billion and R$2.7 billion in 2025-2027, and gross debt increasing from R$12 billion in 2024 to R$24 billion in 2027, absent additional asset sales. Because CEMIG hasn't historically disbursed its target capex, we assume 90% of capex execution in our forecasts relative to the company's budget, as works might be delayed.

In addition, we incorporate the company's dividend payout policy of 50%, which should result in dividends between R$1 billion and R$1.3 billion starting in 2025. Considering the abovementioned aspects and higher interest rates in Brazil, we expect CEMIG to post net debt to EBITDA of about 3.0x and FFO to debt of about 20% in 2025 and 2026, and about 3.5x and 15%-20%, respectively, in 2027 and 2028, considering the termination of hydro plants concession, absent new asset sales.

Debt maturities

CEMIG - Debt amortization profile

As of Sep. 30, 2024, Cemig reported R$ 14.1 billion in gross debt and a cash position of R$ 6.6 billion



Source: S&P Global Ratings.

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Companhia Energetica de Minas Gerais - CEMIG--Financial Summary

Period ending	Dec-31-2018	Dec-31-2019	Dec-31-2020	Dec-31-2021	Dec-31-2022	Dec-31-2023
Reporting period	2018a	2019a	2020a	2021a	2022a	2023a
Display currency (mil.)	R$	R$	R$	R$	R$	R$
Revenues	20,903	22,225	24,273	29,245	28,392	30,089
EBITDA	3,454	4,382	6,326	4,756	4,995	6,240
Funds from operations (FFO)	1,513	1,350	5,001	2,662	3,277	4,608
Interest expense	1,734	1,758	1,703	1,269	1,642	1,782
Cash interest paid	1,290	1,265	1,085	1,593	1,014	1,031
Operating cash flow (OCF)	1,008	2,037	8,609	3,683	6,613	6,644
Capital expenditure	877	1,927	1,538	2,032	3,405	4,942
Free operating cash flow (FOCF)	130	110	7,072	1,652	3,208	1,702
Discretionary cash flow (DCF)	(378)	(591)	6,473	235	1,114	(121)
Cash and short-term investments	1,594	1,276	5,041	2,549	3,185	2,311
Gross available cash	1,594	1,276	5,041	2,549	3,185	2,311
Debt	22,348	23,895	19,457	19,584	17,708	16,341
Common equity	15,939	16,103	17,477	19,462	21,783	24,655
Adjusted ratios						
EBITDA margin (%)	16.5	19.7	26.1	16.3	17.6	20.7
Return on capital (%)	6.7	9.2	15.4	13.0	11.2	12.9
EBITDA interest coverage (x)	2.0	2.5	3.7	3.7	3.0	3.5
FFO cash interest coverage (x)	2.2	2.1	5.6	2.7	4.2	5.5
Debt/EBITDA (x)	6.5	5.5	3.1	4.1	3.5	2.6
FFO/debt (%)	6.8	5.7	25.7	13.6	18.5	28.2
OCF/debt (%)	4.5	8.5	44.2	18.8	37.3	40.7

Companhia Energetica de Minas Gerais - CEMIG--Financial Summary

FOCF/debt (%)	0.6	0.5	36.3	8.4	18.1	10.4
DCF/debt (%)	(1.7)	(2.5)	33.3	1.2	6.3	(0.7)

Reconciliation Of Companhia Energetica de Minas Gerais - CEMIG Reported Amounts With S&P Global Adjusted Amounts (Mil. R$)

		Debt	Shareholder Equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
Financial year	Dec-31-2023										
Company reported amounts		9,831	24,649	36,850	8,496	7,230	1,191	6,240	6,644	1,823	4,942
Cash taxes paid		-	-	-	-	-	-	(601)	-	-	-
Cash interest paid		-	-	-	-	-	-	(1,031)	-	-	-
Lease liabilities		433	-	-	-	-	-	-	-	-	-
Accessible cash and liquid investments		(2,311)	-	-	-	-	-	-	-	-	-
Dividends from equity investments		-	-	-	592	-	-	-	-	-	-
Income (expense) of unconsolid. cos.		-	-	-	(432)	-	-	-	-	-	-
Nonoperating income (expense)		-	-	-	-	378	-	-	-	-	-
Noncontrolling/ minority interest		-	6	-	-	-	-	-	-	-	-
Debt: Guarantees		3,340	-	-	-	-	-	-	-	-	-
Debt: Workers comp/ self insurance		5,417	-	-	-	-	-	-	-	-	-
Debt: Fair value adjustments		(368)	-	-	-	-	-	-	-	-	-
Revenue: other		-	-	(6,761)	(6,761)	(6,761)	-	-	-	-	-
COGS: other nonoperating nonrecurring items		-	-	-	4,072	4,072	-	-	-	-	-
EBITDA - Gain/(loss) on disposals of PP&E		-	-	-	(318)	(318)	-	-	-	-	-
EBITDA: other		-	-	-	591	591	-	-	-	-	-
Interest expense: other		-	-	-	-	-	591	-	-	-	-
Working capital: Taxes		-	-	-	-	-	-	-	601	-	-
Working capital: other		-	-	-	-	-	-	-	621	-	-
OCF: Taxes		-	-	-	-	-	-	-	(601)	-	-

Reconciliation Of Companhia Energetica de Minas Gerais - CEMIG Reported Amounts With S&P Global Adjusted Amounts (Mil. R$)

	Debt	Shareholder Equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
OCF: other	-	-	-	-	-	-	-	(621)	-	-
Total adjustments	6,510	6	(6,761)	(2,256)	(2,037)	591	(1,632)	-	-	-
S&P Global Ratings adjusted	**Debt**	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from Operations**	**Operating cash flow**	**Dividends**	**Capital expenditure**
	16,341	24,655	30,089	6,240	5,193	1,782	4,608	6,644	1,823	4,942

Liquidity

We expect CEMIG's sources of liquidity to surpass uses by more than 10% in the next 12 months. CEMIG's cash position was healthy at approximately R$6.6 billion as of Sept. 30, 2024, considering the proceeds from asset sales and the new debentures of R$2.5 billion issued by CEMIG-D. The group refinanced CEMIG-GT's dollar-denominated bonds in stages in the past years and repaid the outstanding $381 million on the notes on Dec. 5, 2024. Moreover, the group's capex will increase the financing needs in the next few years, but we believe CEMIG's improved operating and financial performance supports its access to debt and capital markets, enabling the refinancing and placing new debt to fund its investments. This is evidenced by the recent issuances of debentures at CEMIG-D for R$4.5 billion in March and September 2024. We believe CEMIG's cash generation will also support the continuity of its dividend distribution of 50% of the previous year's net income going forward, in line with its bylaws.

Principal liquidity sources

- Cash and cash equivalents of R$6.6 billion as of Sept. 30, 2024; and
- Projected FFO of R$4.0 billion - R$4.5 billion in the next 12 months.

Principal liquidity uses

- Short-term debt maturities of about R$4.8 billion as of Sept. 30, 2024;
- Maintenance capex of about R$2.3 billion in the next 12 months;
- Seasonal working capital needs of about R$500 million annually; and
- Dividend payment of R$1.6 billion - R$1.8 billion in the next 12 months, assuming a 50% dividend payout.

Covenant Analysis

Requirements

The covenants include a consolidated maximum debt to EBITDA threshold of 3.5x at CEMIG-GT from 2024 until December 2029--related to the ninth debentures issuance--considering the amortization of the international notes in December 2024. For CEMIG-D, the covenant is 3.5x until June 2029 and 4.0x afterward, and on a consolidated basis, the threshold is 3.0x until June 2026, 3.5x from December 2026 to June 2029, and 4.0x afterward. The covenants are measured semiannually.

The covenant's calculation methodology is different from credit metrics we consider, because financial metrics related to debt include the deficit at Forluz, the employee pension plan, carrying liabilities related to put options, and exclude the fair value of hedges and cash equivalents, while EBITDA includes the financial assets related to the distribution concession.

Compliance expectations

We expect the group to comply with the required thresholds comfortably in the next three years.

Environmental, Social, And Governance

Governance factors are a negative consideration in our credit rating analysis of CEMIG, due to its efforts to enhance risk management. The company faced refinancing issues in the past while its controlling shareholder, the state of Minas Gerais, drained cash from the company through dividends. The new management team, in place since 2019, has been improving CEMIG's operating and financial position, although we believe the group remains exposed to political cycles.

At this point, we believe the risk of government interference is limited, because CEMIG's debt documentation limits upstreaming dividends, and therefore the state's ability to access the group's cash flow. In addition, the Brazilian electric sector operates under the federal regulatory framework, providing a shield against the state's interference in CEMIG's operations.

Although we see environmental and social factors as neutral influences on the rating of CEMIG, severe weather conditions may cause prolonged energy interruptions for clients. For instance, CEMIG's average interruption duration exceeded the regulatory target during 2023, but the group was able to improve it and reduce below regulatory levels thanks to its sizable investments, including to improve network reinforcement and redundancy.

Despite the generation segment's lower EBITDA contribution (at about 25%-30% considering the energy trading contribution), CEMIG needs to purchase energy to honor its contracts in the free market. This poses some risks, because hydrological conditions can cause volatility in energy prices and increase the group’s operating costs. On the other hand, and in line with peers such as CPFL and Neoenergia, we believe CEMIG is well positioned in terms of the energy transition, given that all of its generation capacity is renewable. In addition, CEMIG plans to continue investing to expand its renewable generation segment in the next five years.

Group Influence

CEMIG-D and CEMIG-GT are, in our view, CEMIG's most important subsidiaries. We believe it's highly unlikely that CEMIG will sell these subsidiaries, given they fulfill core activities for the company--distribution and generation and transmission, respectively.

Government Influence

We rate CEMIG and its subsidiaries 'BB-' on the global scale and 'brAA+' on the national scale, above the ratings on its controlling shareholder, the state of Minas Gerais (CCC+/Stable/--). We don't expect an extraordinary action from Minas Gerais that could further impair the company's liquidity and credit metrics because:

- Although the state controls 51% of CEMIG, it operates under the supervision of the federal regulator, ANEEL.
- The financial covenants for a large portion of CEMIG's debt have restrictions, including limiting dividends distribution to the minimum amount, as defined in the company's bylaws, and prohibiting any amendment of those bylaws. Following the full amortization of CEMIG-GT's international notes, this is the case for CEMIG-D's seventh and eighth local debenture issuances, totaling R$3.1 billion as of Sept. 30, 2024.

These factors reinforce our view that despite Minas Gerais' currently weak fiscal position, CEMIG will continue operating and servicing its debt. Therefore, we continue to rate it at a higher level than our rating on the controlling shareholder.

Issue Ratings--Subordination Risk Analysis

Capital structure

We also rate CEMIG-D's seventh debentures due 2026 with a balance of approximately R$2.04 billion at the end of the third quarter of 2024. The distributor reported approximately R$9.9 billion in debt in the same period.

Analytical conclusions

All of CEMIG-D's debt is at its own level, and it doesn't have subsidiaries. As a result, we rate this debt at the same level as the subsidiary, 'brAA+'.

Rating Component Scores

Foreign currency issuer credit rating	**BB-/Positive/--**
Local currency issuer credit rating	**BB-/Positive/--**
Business risk	**Satisfactory**
Country risk	Moderately High
Industry risk	Low
Competitive position	Satisfactory
Financial risk	**Aggressive**
Cash flow/leverage	Aggressive
Anchor	**bb**
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Moderately Negative (-1 notch)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	**bb-**
Group Status of CEMIG-D to CEMIG	**Core**
Group Status of CEMIG-GT to CEMIG	**Core**

Related Criteria

- Criteria | Corporates | General: Sector-Specific Corporate Methodology, April 4, 2024
- Criteria | Corporates | General: Corporate Methodology, Jan. 7, 2024
- Criteria | Corporates | General: Methodology: Management And Governance Credit Factors For Corporate Entities, Jan. 7, 2024
- General Criteria: National And Regional Scale Credit Ratings Methodology, June 8, 2023
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- Companhia Energetica de Minas Gerais – CEMIG, Dec. 18, 2023

Ratings Detail (as of December 12, 2024)*		
Companhia Energetica de Minas Gerais - CEMIG		
Issuer Credit Rating		BB-/Positive/--
Brazil National Scale		brAA+/Positive/--
Issuer Credit Ratings History		
26-Nov-2024		BB-/Positive/--
28-Jan-2021		BB-/Stable/--
10-Jul-2020		B/Positive/--
26-Nov-2024	*Brazil National Scale*	brAA+/Positive/--
28-Jan-2021		brAA+/Stable/--
10-Jul-2020		brA+/Positive/--
Related Entities		
Cemig Distribuicao S.A.		
Issuer Credit Rating		BB-/Positive/--
Brazil National Scale		brAA+/Positive/--
Cemig Geracao e Transmissao S.A.		

Ratings Detail (as of December 12, 2024)*

Issuer Credit Rating	BB-/Positive/--
Brazil National Scale	brAA+/Positive/--

*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. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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