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CREDIT OPINION
5 April 2019

Update

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RATINGS

AES Tiete Energia S.A.

Domicile	Sao Paulo, Sao Paulo, Brazil
Long Term Rating	Ba2
Type	LT Corporate Family Ratings
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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AES Tiete S.A.

Update following rating assignment to 9th debenture issuance

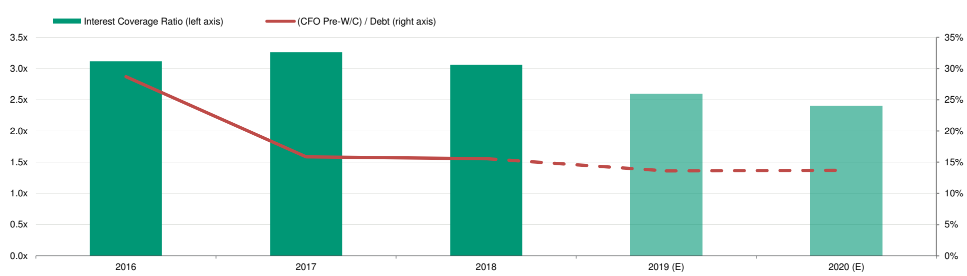
Summary rating rationale

AES Tiete Energia S.A.'s (AES Tiete) Ba2/Aa1.br ratings reflect AES Tiete's overall predictable and strong cash generation that leads to adequate credit metrics for the rating category as well as its resilient access to the local banking and capital markets together with management´s prudent administration of the generation business. The short-term leverage should be more pressured given the ongoing capacity increase, with a CFO Pre WC/Debt of average 2.5x according to Moody´s projections, which we expect to be temporary returning to historical levels in the medium-long term. The ratings also incorporate AES Tiete´s historical high dividend payout and the potential cash outflow of the judicial dispute over the spot market exposure during the hydrological crisis (BRL740 million net provision as of December, 2018).

AES Tiete´s ratings are further constrained by its expansion strategy in renewable energy coupled with the Capex pressures from the renewable projects still under construction. Brazil´s sovereign rating (Ba2 stable) also limits the company´s rating given the local revenue dependency and highly regulated business nature as well as the overall more challenging hydrological conditions.

Exhibit 1

Credit metrics to stabilize at a lower level in the short-medium term



All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations

Source: Moody's Financial Metrics™, Moody's estimates

Credit strengths

» Adequate credit metrics for the rating category

» Overall predictable and strong cash generation

» Resilient access to local banking and capital markets

Credit challenges

» High level dividend payout practice

» Expansion investments in renewable energy (non-hydro sources)

» Judicial dispute owing to its spot-market exposure during the 2015 hydrological crisis

» Relative higher leverage in the short to medium term

Rating outlook

The stable outlook largely reflects Brazil´s sovereign rating outlook given the company´s local-content profile. It also incorporates our view of AES Tiete´s relatively stable cash flows in the projected period and our expectation that dividend outflows and any acquisitions or M&A activity will be prudently managed to maintain adequate leverage and credit metrics for the rating category.

Factors that could lead to an upgrade

We could upgrade the ratings if AES Tiete´s operational performance surpass our expectations or if liquidity improves. If the credit metrics stay above our projections such that cash interest coverage (CFO Pre WC + Interest/ Interest) stays above 4.5x and the CFO Pre WC/Debt above 35% for a sustainable period, we could also consider an upgrade. Nevertheless, AES Tiete´s ratings are constrained by Brazil´s sovereign rating given its close linkages to the local economic/regulatory environment and ultimate credit quality.

Factors that could lead to a downgrade

A rapid or significant downturn in AES Tiete´s credit metrics such as cash interest coverage (CFO Pre WC + Interest/ Interest) stays below 2.5x and the CFO Pre WC/Debt below 14% on a sustainable basis could prompt a rating downgrade as well as the degradation of the liquidity and overall credit quality. The company's operating margin potentially coming under pressure from a significant mismatch on spot market exposure or on contracted levels could also weigh on the ratings. In addition, Moody´s could also review AES Tiete´s rating downwards if the company´s expansion plan continues to lead to higher leverage thresholds.

Key indicators

Exhibit 2

Key indicators

AES Tiete Energia S.A

	12/31/2018	12/31/2017	12/31/2016	12/31/2015	12/31/2014
(CFO Pre-W/C + Interest) / Interest	3.1x	3.3x	3.1x	4.8x	4.3x
(CFO Pre-W/C) / Net Debt	20.6%	23.8%	47.5%	117.6%	15.5%
RCF / Net Debt	11.8%	9.2%	-35.6%	68.6%	-9.8%
(CFO Pre-W/C) / Debt	15.6%	15.8%	28.7%	54.8%	9.5%
RCF / Debt	8.9%	6.1%	-21.5%	32.0%	-6.0%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Source: Moody's Financial Metrics™

Corporate profile

AES Tiete is mainly a hydropower generation company with a 30-year concession, granted in December 1999 to operate an installed capacity of 2,658 MW, equivalent to around 2% of Brazil's electricity capacity, and 1,247 MW of assured average energy. The company has 9 hydro-power plants (HPPs) and 3 small hydro-power plants (SHPPs) located in the State of Sao Paulo. The company also has a portfolio of wind and solar generation of 386 MW and 294 MW, respectively, totaling a capacity of 3,338 MW (end of 2019).

In 2017 the company started investing in non-hydro renewable sources generation with four new projects until date: (i) Alto Sertão II wind power plant with 386.1 MW of installed capacity located in the State of Bahia, (ii) Guaimbê solar complex 180 MWp of installed capacity and (iii) Ouroeste complex composed by Boa Hora project with 91 MWp as well as the AGV solar project acquired in Aneel´s auction held in December 2017 with 94 MWp installed capacity (total investments of BRL 280 million). These renewable contracts are supported by long-term PPA agreements maturing around 2033-40 with fixed prices yearly adjusted by inflation. AES Tiete´s expansion strategy is to continue investing in wind/solar power projects partially mitigating the company´s exposure to local hydrological conditions.

Since AES Tiete is an operational holding company with an adequate balance of the cash generation and debt at the holding level, we do not consider it structurally subordinated to the opcos. As of December 2018, AES Tiete had 80% of its energy contracted for 2019 and did not adhere to the law 13,203 that hedges the hydrological risk for a premium as negotiated with the regulator, Aneel, although we expect the company to maintain an uncontract cushion of around 20% through its portfolio.

According to Moody´s standard adjustments, AES Tiete reported (CFO Pre WC + Interest/ Interest) of 3.1x and CFO Pre WC/Debt of 16% in the FY ended December 2018. Also in the same period, net operating revenues reached BRL 1.9 billion and EBITDA of BRL 1,087 million while total debt amounted BRL 4.2 billion.

AES Tiete Energia is directly controlled by AES Holdings Brasil Ltda. (24%) as well as indirectly controlled by AES Corporation, (The) (Ba1 stable).BNDES Participacoes S.A. (BNDESPAR; Ba2 stable) (28%) represents a minority shareholder position.

Detailed rating considerations

Leverage credit metrics for the rating category to stay at lower thresholds but still adequate

AES Tiete has historically posted strong credit metrics, characterized by CFO pre-WC/debt of average 19.4% and interest coverage of 3.3x in the last three-year average. These levels are well below the historical metrics (2013-15) of 31.8% and 6.2x, respectively. The lower metrics, which we expect to continue in the short to medium term, are mainly driven by a combination of the operational challenge raised from the hydrological conditions that pressure EBITDA margins, combined with the investment plan the company has in order to expand its capacity with renewable energy projects.

We recognize lower ratios in our projections owing to the acquisitions performed in 2017 and the additional debt and investment needs related to those, which drive these metrics to around 14.5% and 2.6x, respectively, from 2019 to 2021.

In addition, the more challenging overall hydrological conditions in Brazil could further strain the company's cash generation because water reservoir levels are still below the historical levels at 32% of the National Integrated System (SIN) total storage capacity as per the FY2018 results.

AES Tiete maintained its uncontracted position of 20% in December 2018 in order to balance its exposure to the spot market, which presented increasing prices and lower generation scaling factor throughout the year. The company is expected to maintain a buffer of up to 20% for hedging purposes, from our previous range of 15%, and manage its portfolio to continue mitigating the hydrological risks. Furthermore, as the renewable projects become operational in the short term and fully contribute to the EBITDA, they should also contribute to lowering this exposure. As of December 2018, the company presented an uncontrated position of 20% for 2019 and 21% for 2020 and did not adhere to the Law 13,203, which hedges the hydrological risk as per the negotiation with Aneel.

Capacity expansion and new investments to strain leverage

The company's strategy is to increase the contribution of its wind/solar portfolio to the overall EBITDA. Such an increase will (1) contribute to a more stable cash flow because these projects have power purchase agreements with terms of 20 years, versus the company's average of three to five years; (2) diversify the power-generation mix away from its concentration in hydropower which also brings negative correlation given the wind/rain patterns, and (3) reduce the company's exposure to hydro deficits after it decided not to take advantage of the law that allows the hedging of hydrological risk by paying a premium negotiated with Aneel.

In 2017, the company acquired two solar complexes Guaimbê and Ouroeste (comprised of Boa Hora and AGV), which together addressed around 80% of the contractual obligation to increase its generation capacity in the State of Sao Paulo by 15% (considering MWp).

AES Tiete also acquired a wind power project, Alto Sertão II, in August 2017, the first in its portfolio. The company bought the 386 MW complex from Renova for BRL 600 million, plus an additional BRL 100 million earn-out depending on the project's performance over the next five years. More recently, AES Tiete announced the negotiation to buy Alto Sertão III wind project. Our projections do not incorporate additional debt to fund this new project, which could negatively pressure the ratings as we consider AES Tiete will finance it with alternative sources if the negotiation is successful. Nonetheless, it would represent additional investments in the following years.

Additional M&A activity that would further strain the company's leverage and EBITDA margin levels beyond our projections could lead us to revise the ratings downward, although we understand the expansion will be prudently managed to maintain adequate leverage and credit metrics for the rating category. In addition, the company's management should also balance its dividend distribution policy and retain more cash within AES Tiete if needed. AES Tiete has a high level historical dividend payout that could serve as an additional source to support its liquidity.

Judicial dispute outcome still uncertain also adds to the lower credit metrics

We expect AES Tiete's leverage increase also because we forecast the company is likely to pay the provisioned amount of BRL980 million (gross or BRL 740 million net) derived from its spot market exposure judicial dispute. AES Tiete could face a cash outflow in case of an unfavorable court ruling, which we incorporate in our projections for 2019. However, Law 10.985 that would regulate this matter, is still under discussion and the outflows could be within a period of time as well as the company could receive some positive compensation for it such as lengthening the concession period. The company reported a strong cash position of BRL 1.03 billion as of December 2018, which we understand would be adequate to meet this obligation, in case of need.

AES Tiete has a legal injunction preventing the payment of costs associated with its exposure to the spot market since May 2015. The merit of the suit filed by APINE (Brazilian Association of Independent Producers of Electric Energy), which represents the company as well as other generators, has not been decided yet.

The company's leverage, as measured by net debt/EBITDA, should increase to around 4.0x in our projections from 3.0x as of December 2018. AES Tiete´s outstanding debt stipulates the Net Debt/EBITDA covenant must be maintained at levels equal or below 4.0x and if AES Tiete performs any acquisition the ratio can go up to 4.5x for 12 months and 4.25x for another 12 months. Nonetheless, those are limited to the 4th, 5th and 6th (second series) debenture issuances´ Net Debt/EBITDA of 3.85x. Covenant breach in two consecutive quarters could accelerate the debt payment.

Liquidity analysis

Similar to other Brazilian companies, AES Tiete does not have committed banking facilities to face unexpected cash requirements but the company proved that it has strong access to the capital markets, which we deem will continue in the coming years, because the company will tap these markets to complement its funding needs.

AES Tiete has an adequate liquidity profile, given its BRL 1.03 billion cash position as of December 2018 and an outstanding short-term debt of BRL 127 million (as per Moody´s standard adjustments) that could be mostly paid with internal cash generation. The recent debenture issuance (9th) contributed to strengthen the company´s debt profile by lengthening its amortization schedule at a lower cost. We anticipate AES Tiete will continue to leverage, mainly to pay dividends and meet its capital spending needs, while management prudently manages its dividend distributions, financial leverage and liquidity, so that its credit metrics remain in line with its rating category.

The fully-amortizing 9th debenture issuance will have three tranches with up to 10-year maturity. The first tranche of BRL 1.38 billion will have two principal payments, 50% in the penultimate year of the tenor (2026) and the remaining at maturity (2027), with bi-annual interest payments starting after issuance. At the same time, the second and third tranches (BRL 820 million) will be amortized in three equal payments in the last three years of maturity from 2027 to 2029. The second tranche carries bi annual interest payments, while the third one has annual disbursements.

Proceeds from the transaction will be mostly used to refinance existing debt obligations as well as for payment and reimbursement of expenses related to the Guaimbe and AGV solar projects. The debentures will have cross-default clauses with the issuer's other debt as well as with relevant subsidiaries and will include acceleration clauses such as: (i) the non-payment of any financial obligation above USD 25 million, (ii) change of control in AES Tiete and termination of the hydropower concession contracts (iii) granting intercompany loans for up to 180 days if not previously approved by creditors, (iv) dividend payments above the minimum required by Brazilian Corporate Law if the company is not in compliance with its obligations including the financial covenants (v) covenant breach in two consecutive quarters on the following: Net Debt/EBITDA must be maintained at levels equal or below 4.5x and interest coverage ratio measured by EBITDA/ Net Interest expense equal to or above 1.25x.

Rating methodology and scorecard factors

Exhibit 3
Rating factors
AES Tiete Energia S.A.

Unregulated Utilities and Unregulated Power Companies Industry Grid [1][2]	Current FY 12/31/2018		Moody's 12-18 Month Forward View As of 3/31/2019 [3]	
Factor 1 : Scale (10%)	**Measure**	**Score**	**Measure**	**Score**
a) Scale (USD Billion)	B	B	B	B
Factor 2 : Business Profile (40%)				
a) Market Diversification	Ba	Ba	Ba	Ba
b) Hedging and Integration Impact on Cash Flow Predictability	Baa	Baa	Baa	Baa
c) Market Framework & Positioning	Ba	Ba	Ba	Ba
d) Capital Requirements and Operational Performance	Baa	Baa	Baa	Baa
e) Business Mix Impact on Cash Flow Predictability		NA		
Factor 3 : Financial Policy (10%)				
a) Financial Policy	Ba	Ba	Ba	Ba
Factor 4 : Leverage and Coverage (40%)				
a) (CFO Pre-W/C + Interest) / Interest (3 Year Avg)	3.3x	Ba	2.5x	B
b) (CFO Pre-W/C) / Debt (3 Year Avg)	19.4%	Ba	13.6%	Ba
c) RCF / Debt (3 Year Avg)	4.7%	B	6.8x	B
Rating:				
a) Indicated Rating from Grid		Ba2		Ba2
b) Actual Rating Assigned				Ba2

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
[2] As of 12/31/2018.
[3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions and divestitures
Source: Moody's Financial Metrics™

Ratings

Exhibit 4

Category	Moody's Rating
AES TIETE ENERGIA S.A.	
Outlook	Stable
Corporate Family Rating	Ba2
Senior Secured -Dom Curr	Ba2
Senior Unsecured -Dom Curr	Ba2
NSR Senior Secured	Aa1.br
NSR Corporate Family Rating	Aa1.br
NSR Senior Unsecured	Aa1.br
ULT PARENT: AES CORPORATION, (THE)	
Outlook	Stable
Corporate Family Rating	Ba1
Sr Sec Bank Credit Facility	Baa3/LGD3
Senior Unsecured	Ba1/LGD4
Speculative Grade Liquidity	SGL-2

Source: Moody's Investors Service

REPORT NUMBER 1166825

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EMEA	44-20-7772-5454

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