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CREDIT OPINION
7 November 2023

Update

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RATINGS

Empresa de Transmision Electrica, S.A.

Domicile	Panama
Long Term Rating	Baa3
Type	LT Issuer Rating - Fgn Curr
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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Empresa de Transmision Electrica, S.A.

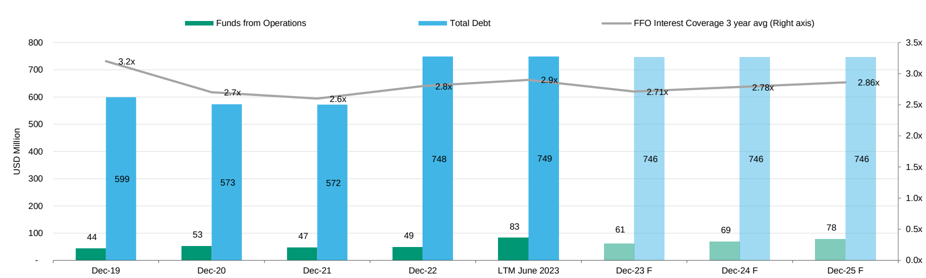
Update following downgrade to Baa3, outlook changed to stable

Summary

Empresa de Transmisión Electrica S.A. de C.V. (ETESA, Baa3 stable) credit profile mainly reflects the supportive regulatory framework within which it operates and the regulated tariff setting process that allows the company to recover a fixed return on its investments. ETESA does not bear volume or commodity risk, instead its revenues derive from the periodic regulated tariffs that factor the company's productive assets and capital expenditure. ETESA's Baa3 ratings results from the application of Moody's Joint Default Analysis ("JDA") framework for GRIs, which takes into account the (i) baseline credit assessment of baa3, (ii) the Baa3 rating of the Government of Panama as ETESA's support provider, (iii) our estimates of high implied government support in case of extraordinary financial distress and (iv) a very high default dependence between ETESA and the GOP.

The rating reflects the relatively high leverage and coverage metrics that arise from the planned capital expenditure program. As of June 2023, ETESA reported an average cash interest coverage ratio of 2.9x and a FFO/Net Debt leverage metric of 8.6%. Moody's expectation considers a gradual implementation of the planned investment capital program that will project cash interest coverage ratio of 2.8x and FFO/Net Debt of 10% on average by 2024.

Exhibit 1
Leverage increase to fund planned capital investment program



All ratios are based on "Adjusted" financial data and incorporate Moody's global standard adjustments for non-financial corporations. Forecasted financial metrics based on Moody's Base Case scenario.
Source: ETESA and Moody's Investors Service

Credit strengths

» Sole company with exclusive rights to operate the transmission system in Panama under a recently extended concession until 2049.

» Stable and predictable regulated revenues derived from a transparent and clear tariff setting process.

» Wholly-owned by the Government of Panama, providing a high level of extraordinary support under our Government Related Issuers framework.

Credit challenges

» Large capital expenditure program that will require external funding via debt, maintain the company's relatively high leverage and also exposing ETESA to execution risks.

» Electricity not delivered due to transmission system failures cause penalties that must be covered by ETESA.

» Very high level of default dependency with the Government of Panama due to exposure to common credit risks and reliance on same revenue base.

Rating outlook

ETESA's rating outlook is stable, in line with the rating outlook of the Government of Panama, the company's sole owner and extraordinary support provider in the event of financial distress. Additionally, it reflects our expectations of a stable and predictable revenues sustaining a cash interest coverage ratio above 2.8x and a FFO/Net Debt ratio of higher than 11% in the medium term, while also maintaining adequate liquidity for the next 12-18 months.

Factors that could lead to an upgrade

» Upward pressure on ETESA's rating would require the company to continue recording a cash interest coverage and FFO/Net Debt above 3.5x and 13%, respectively, on a sustained basis in conjunction with an improvement in the credit quality of the sovereign rating.

Factors that could lead to a downgrade

» The rating would downgrade if we see deterioration in the credit quality of the sovereign rating, or a deterioration of the domestic regulatory framework. Downward pressure on ETESA's rating would also be caused by higher leverage or lower than anticipated cash flows, such that its cash interest coverage and FFO/Net Debt were to be below 2.8x and 9% respectively, on a sustained basis.

Key indicators

Exhibit 2

Empresa de Transmision Electrica, S.A.

3-year average metrics

	Dec-20	Dec-21	Dec-22	LTM June 2023	Dec-23 F	Dec-24 F	Dec-25 F
FFO Interest Coverage	2.7x	2.6x	2.8x	2.9x	2.71x	2.78x	2.86x
Net Debt / Fixed Assets	66.8%	63.6%	62.7%	63.7%	67.3%	75.0%	82.7%
FFO / Net Debt	9.3%	9.6%	9.5%	8.6%	9.5%	10.0%	11.2%
RCF / Net Debt	9.3%	9.6%	9.5%	8.6%	9.5%	10.0%	11.2%

Source: Moody's Investors Service. All ratios are based on "Adjusted" financial data and incorporate Moody's global standard adjustments for non-financial corporations. Forecasted financial metrics based on Moody's Base Case scenario.

Profile

Founded in 1998, Empresa de Transmision Electrica (ETESA) operates the country's transmission network as a monopoly and is wholly owned by the Government of Panama. ETESA, granted by law, owns and oversees the operation and maintenance of the transmission system, which consists of three transmission lines that span roughly 3,000 kilometers and 18 substations, providing interconnection between the power generation plants and regulated customers, which are primarily the three distribution companies in Panama. Additionally, the company dispatches energy according to market rules, performs energy demand planning activities and coordinates public auctions to secure supply to regulated customers.

Recent developments

On October 31, 2023, the Government of Panama rating was downgraded from Baa2 to Baa3 with a stable outlook reflecting the lack of an effective policy response to structural fiscal challenges that have been rising over time, a condition that denotes weak governance and reduced fiscal policy effectiveness, a governance-related element under Moody's analytical framework. As a consequence of the downgrade of ETESA's support provider under Moody's analytical framework of Government Related Issuers, ETESA's rating has been downgraded to Baa3 with a stable outlook. In line with this action, Moody's downgraded the Baseline Credit Assessment (BCA) to baa3, a measure of ETESA's standalone creditworthiness.

Detailed credit considerations

Regulatory framework and cash flow visibility to remain supportive of credit quality

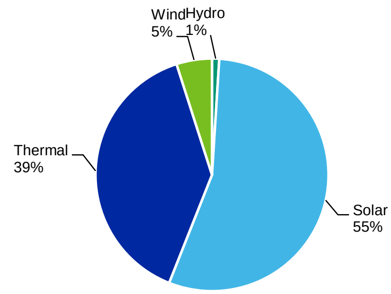
ETESA benefits from an advantageous position as it operates in a monopolistic structure, being the sole company in Panama that has exclusive rights to own and operate the transmission system under a long term concession authorized by the regulatory body Autoridad de los Servicios Públicos (ASEP). The concession was set to expire in October 2024; however, the regulator has recently granted a 25-year extension until 2049 under the existing terms and conditions to ETESA so it can continue enforcing its exclusive rights, granted by the law, to own, operate and develop the Panamanian transmission system - a credit positive.

The strategic nature of this regulated activity is supported by a tariff setting process that remunerates ETESA on its productive asset base. The tariff regime is revised every four years and sets a minimum allowed income that considers a fixed return of a 7% premium plus the last twelve months annual interest rate of the 30-year US Treasury bonds (with an allowed 2% deviation). This regime allows ETESA to recover a rate of return that allows a profitability level after covering its operating and maintenance expenses. ETESA is not exposed to volume or resource risk as the tariffs are charged to generating and distribution companies, and in the event any of those companies fail to carry out a payment, it is redistributed among the participants of the electricity system based on their market shares. Currently, the regulator has approved the tariffs for the 2021-2025 period according to the tariff setting methodology.

Increased leverage due to large capital investment program planned to cover growing capacity penetration and energy demand

In Panama, the electricity demand between the period 2000-2020 has grown approximately at an average annual rate of 4% with a slowdown in the last four years. After a decline in electricity demand of roughly 6% in 2020 due to pandemic lockdowns and restrictions; however, electricity demand has strongly rebounded with growth rates of roughly 8% in 2021 and 3.9% in 2022, in line with Moody's GDP growth forecasts and with ETESA's long-term moderate demand scenarios on its generation expansion plan of 2022-2036. Distribution companies in Panama require to secure and contract future energy supply in line with projected peak demand levels to maintain a reserve margin, therefore we expect that there will be relevant capacity additions in the system in the short and medium term. In the 2024-2025 period, the expected capacity additions in the country according ETESA's expansion plan consider a total penetration of 1,218 MW of capacity, mainly from non-conventional renewables and thermal plants (see exhibit below).

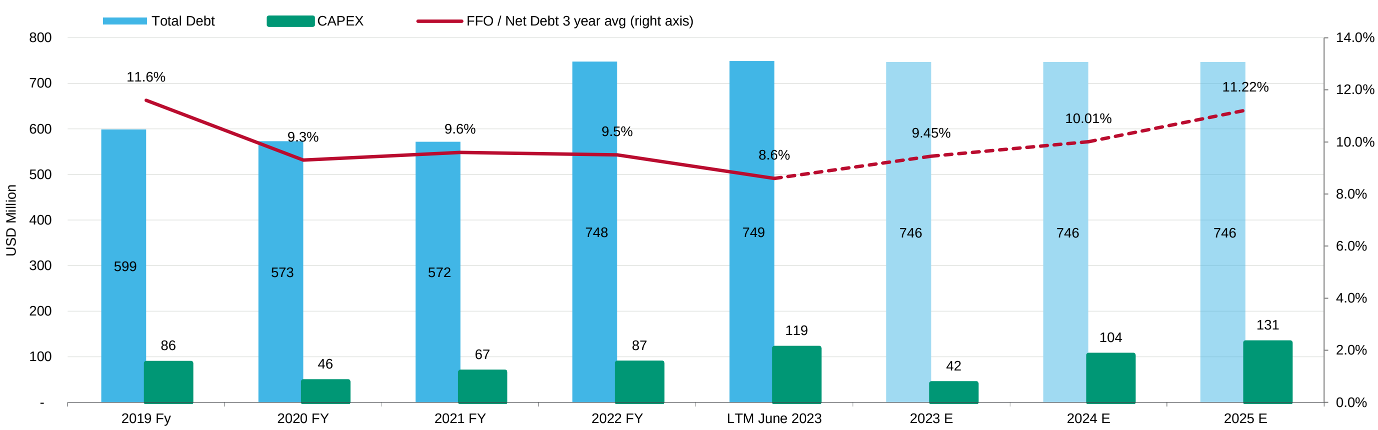
Exhibit 3
Projected capacity additions mainly solar and thermal projects
1,218 MW in additional installed capacity



Source: ETESA Expansion Plan 2022-36

This growth in capacity requires ETESA to expand and maintain the interconnection grid to avoid congestion issues. As a result, ETESA's capital expenditure program for the upcoming years will average around $120 million per year. These capital investment needs will be funded with a combination of cash and additional debt, thus we project a relatively high leverage. Under our base case ETESA will average a FFO / Net Debt of 10% through 2024.

Exhibit 4
Gradual de-leverage as tariffs recognize new investments



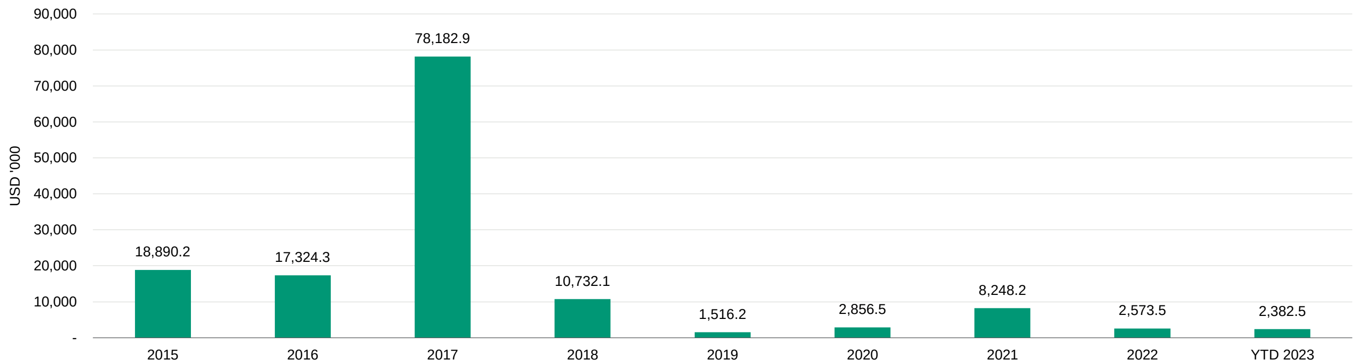
Source: ETESA and Moody's Investors Service

An important assumption embedded in our rating is that the planned fourth transmission line with an estimated cost of $700 million will be developed through a design, construction, financing and maintenance scheme without recourse to ETESA. Delays of this major project combined with execution risks of the current capital expenditure plan could increase congestion and transmission shortfall risks. In the event of a transmission shortfall, ETESA is required to compensate the affected parties for the electricity that was not delivered (this event is called Generación Obligada under local regulation). In the following exhibit it can be observed the amount of payments ETESA has been required to compensate as a consequence of these type of events.

Exhibit 5

Shortfall event in 2017 led to an extraordinary cost

Annual transmission shortfalls



Source: Centro Nacional de Despacho statistics

Important linkages with the Government of Panama

ETESA's baa2 BCA is a measure of its standalone creditworthiness. Because the company is wholly owned by the Government of Panama, we apply the Government-Related Issuers methodology, which incorporates our view of a high level of implied government support in the event of financial distress, as well as a very high level of default dependence with the Government of Panama. These factors incorporate the importance of the company's services to the country's overall economic development and security.

The company's very strong credit linkages with the GOP derives from the strategic and essential nature of the services that the company provides as the sole operator and owner of the country's electricity transmission system. The rating also factors the government control through its 100% ownership, and direction of the company, along with past evidence of financial support via tariff adjustments and capital contributions.

The government has supported ETESA with capital contributions of $68.7 million since 2011, as well as approved an extraordinary tariff increase, which resulted in an additional $80 million in revenue, to compensate for the Generación Obligada expense incurred because of the delay in the construction of the third transmission line. However, about half of the $80 million plus interest costs will be deducted from future tariff adjustments. The high level of implied support mitigates some of the potential credit profile deterioration for ETESA.

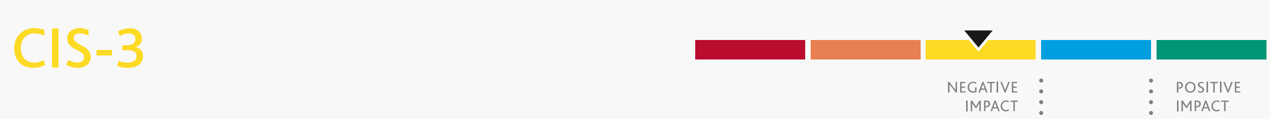
ETESA does not have a mandatory dividend distribution policy, and it often reinvests all of its net income in further development and expansion of more efficient transmission lines, which allows the company to set more competitive tariffs. Moreover, the board of directors is presided by the Minister of Economy and Finance, another evidence of linkages with the Government of Panama.

ESG considerations

Empresa de Transmision Electrica, S.A.'s ESG Credit Impact Score is Moderately Negative CIS-3

Exhibit 6

ESG credit impact score



ESG considerations have a limited impact on the current rating, with potential for greater negative impact over time.

Source: Moody's Investors Service

CIS-3 indicates that its ESG attributes are overall considered as having a limited impact on the current rating, with greater potential for future negative impact over time, especially through exposure to social risks. Exposure to adverse regulatory or political interference could weaken ETESA's credit quality.

Exhibit 7
ESG Issuer Profile Scores

ENVIRONMENTAL	SOCIAL	GOVERNANCE
E-2	S-3	G-3
Neutral-to-Low	Moderately Negative	Moderately Negative

Source: Moody's Investors Service

Environmental
ETESA's **E-2** score reflects the limited exposure to environmental risks related to carbon transition, physical climate risks being a large transmission system company with country-wide coverage.

Social
ETESA's **S-3** score reflects its exposure to social risks related to demographics and societal trends that increase public concern over affordability issues that could lead to adverse regulatory political intervention.

Governance
ETESA's **G-3** score reflects governance risks related to management credibility, track record, board structure, policies and procedures being a state-owned company with the possibility of the government in course exercising significant influence.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Liquidity analysis
The tariff-setting process that allows ETESA to achieve a rate of return after expenses mitigates liquidity risks. In addition, as of June of 2023, ETESA held cash, equivalents and other short-term investments that roughly amount to $112 million and had no short-term debt maturities, with the next maturity being the principal repayment of $75 million senior local bonds due in 2026. The $500 million senior unsecured notes issued from international bonds amortize until 2035.

Ratings

Exhibit 8

Category	Moody's Rating
EMPRESA DE TRANSMISION ELECTRICA, S.A.	
Outlook	Stable
Issuer Rating	Baa3
Senior Unsecured	Baa3

Source: Moody's Investors Service

Methodology and scorecard

The methodologies used in these ratings were our Regulated Electric and Gas Networks, published in April 2022, and Government-Related Issuers Methodology, published in February 2020.

Exhibit 9

Rating Factors

Empresa de Transmision Electrica, S.A. -Private

Regulated Electric and Gas Networks Industry [1][2]	Current LTM 6/30/2023		Moody's 12-18 Month Forward View As of 12/31/2023 [3]	
Factor 1 : Regulatory Environment and Asset Ownership Model (40%)	**Score**	**Metric**	**Score**	**Metric**
a) Stability and Predictability of Regulatory Regime		A		A
b) Asset Ownership Model		Baa		Baa
c) Cost and Investment Recovery (Ability and Timeliness)		A		A
d) Revenue Risk		A		A
Factor 2 : Scale and Complexity of Capital Program (10%)				
a) Scale and Complexity of Capital Program		Ba		Ba
Factor 3 : Financial Policy (10%)				
a) Financial Policy		Baa		Baa
Factor 4 : Leverage and Coverage (40%)				
a) FFO Interest Coverage (3 Year Avg)	2.9x	Baa	2.78x	Ba
b) Net Debt / Fixed Assets (3 Year Avg)	63.7%	Baa	75%	Ba
c) FFO / Net Debt (3 Year Avg)	8.6%	Ba	10%	Ba
d) RCF / Net Debt (3 Year Avg)	8.6%	Baa	10%	Baa
Rating:				
Scorecard-Indicated Outcome Before Notch Lift		Baa2		Baa3
Notch Lift	0	0	0	0
a) Scorecard-Indicated Outcome		Baa2		Baa3
b) Actual Rating Assigned		Baa3		Baa3
Government-Related Issuer		**Factor**		
a) Baseline Credit Assessment		baa3		baa3
b) Government Local Currency Rating		Baa3		Baa3
c) Default Dependence		Very High		Very High
d) Support		High		High
e) Actual Rating Assigned		Baa3		Baa3

[1] All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for non-financial corporations. [2] As of 2Q2023 and metrics reflect the last 3 year average. [3] This represents Moody's forward view, not the issuer's and unless noted in the text, does not incorporate significant acquisitions and divestitures.
Source: Moody's Investors Service

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