

**Rating Action: Moody's assigns a Ba2 rating to AEGEA's proposed up to USD 500 million Notes; outlook negative**

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21 Apr 2022

New York, April 21, 2022 -- Moody's Investors Service ("Moody's") assigned a Ba2 rating to the up to USD500 million senior unsecured Notes due 2029 to be issued by Aegea Finance S.à r.l. ("Aegea Finance") and guaranteed by AEGEA Saneamento e Participacoes S.A. ("AEGEA" or "the company"). At the same time, Moody's affirmed Aegea Finance's Ba2 senior unsecured rating as well as AEGEA's Ba1 Corporate Family Rating (CFR). The outlook remains negative for all ratings.

The assigned rating is based on preliminary documentation received by Moody's as of the rating assignment date. Moody's does not expect changes to the documentation reviewed over this period nor does it anticipate changes in the main conditions that the notes will carry. Should issuance conditions and/or final documentation of the notes deviate from the original ones submitted and reviewed by the rating agency, Moody's will assess the impact that these differences may have on the ratings and act accordingly.

**Assignments:**

..Issuer: Aegea Finance S.a r.l.

....Gtd Senior Unsecured Notes, Assigned Ba2

**Outlook Actions:**

..Issuer: Aegea Finance S.a r.l.

....Outlook, Remains Negative

..Issuer: AEGEA Saneamento e Participacoes S.A

....Outlook, Remains Negative

**Affirmations:**

..Issuer: Aegea Finance S.a r.l.

....Gtd Senior Unsecured Notes, Affirmed Ba2

..Issuer: AEGEA Saneamento e Participacoes S.A

.... Corporate Family Rating, Affirmed Ba1

**RATINGS RATIONALE**

The proposed up to USD500 million Notes are senior unsecured, with a fully unconditional guarantee from AEGEA, pari-passu to the outstanding and future unsecured debt of AEGEA. The proposed issuance has a similar structure to that of the company's senior unsecured notes due in 2024, which will be redeemed with the proceeds from the offering (approximately \$400 million outstanding) with the remaining amount used for general corporate purposes, likely funding capital expenditures of existing projects. The transaction structure encompasses a financial covenant test, where AEGEA's consolidated Net Debt to EBITDA ratio has to be below 3.5x for the company to incur in additional debt, except for certain permitted indebtedness.

The Ba2 rating assigned for the USD500 million Notes stands one notch lower than AEGEA's CFR because of structural subordination considerations since AEGEA does not hold any operations and is strictly a vehicle for controlling stakes on the operating subsidiaries. AEGEA largely depends on the regular payment of dividends up-streamed by its operating subsidiaries to meet its obligations, equity investment commitments and potential cash requirements related to its guarantees. Following the successful issuance of the proposed notes and redemption of the 2024 notes, Moody's anticipates debt at the holding company level will represent around 30% of

total debt.

The Ba1 CFR reflects the stable consolidated credit profile of AEGEA's business, derived from the company's solid market position and relatively strong pricing power. The company benefits from very limited competition of the operating subsidiaries in their service areas. Also, incorporated in the rating is Moody's view of the geographic diverse operations, resulting in lower exposure to water scarcity problems shown by overall lower volume fluctuations and consolidated stable cash flows in times of unfavorable rainfalls. AEGEA's tariff mechanism and contractual framework are overall transparent and predictable with annual automatic tariff adjustments for inflation. In addition, its diversified debt profile combined with shareholders support evidenced by continuous equity injections further sustain the rating.

The rating is balanced by AEGEA's aggressive capital spending plan amid continued growth in the Brazil's sanitation sector, leading to a prolonged deterioration of leverage metrics. Particularly, as related to the acquisition of Aguas do Rio ("AdR" ex CEDAE), which initiated operations last November. Moody's acknowledges that Aguas do Rio is performing ahead of the management's initial financial and operational forecast. Still, our projected consolidated net debt-to-EBITDA ratio, including 100% of AdR, remains in the range of 4.0x-4.5x until at least 2023, before gradually improving to below 3.5x. Additionally, AEGEA can be required to extend extraordinary support to non-consolidated businesses, through certain off-balance equity support agreements, which could add further pressure on leverage metrics. The Government of Brazil's rating (Ba2 stable) is also a rating constraint, given the domestic nature of the company's operations.

The negative outlook reflects the still high execution risk to improve operating performance and implement its capital spending plan in the new concessions, and at the same reduce leverage to maintain credit metrics in line with the current rating category. In 2021, Moody's calculates the company's FFO interest coverage was at 1.9x while the adjusted debt/capitalization ratio was at 53%. For the next 12-18 months, Moody's anticipates coverage to remain around 1.8x and the leverage at 60%.

#### FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

A rating upgrade is unlikely at this time. But rating stabilization could be triggered by more visibility into the deleveraging of new concessions. Quantitatively, upward rating pressure would arise if adjusted FFO interest coverage stays above 3.0x and debt/capitalization stays below 75% on a sustained basis, however such pressure is somewhat limited to the sovereign credit quality.

On the other hand, lower than anticipated financial support from the shareholders, higher capital spending or operating costs combined with deterioration in the liquidity profile, could exert downward pressure on AEGEA's ratings. AEGEA has cross-default clauses within the group and operates through a centralized cash management system. In light of that, ratings could be revised downwards if there are material delays or cost overruns in its capital investment program that hurt its revenue or lead to non-compliance with contractual targets. Our perception of deteriorated stability and transparency of the regulatory regime, or a deterioration in the credit quality of the sovereign, could also exert downward pressure on the ratings. Quantitatively, the ratings could be downgraded if the adjusted FFO interest coverage ratio stays below 2.0x and debt/capitalization remains above 75% on a sustained basis.

Moody's perception of reduced financial flexibility of the operating subsidiaries to support debt service at the holding company level, or a material increase in the proportion of debt outstanding at the holding level in proportion of total debt combined with sustained lower cash availability to service its debt could also imply further notching down of the Notes due to structural considerations.

#### COMPANY PROFILE

AEGEA is one of the largest private water and sewage players in Brazil, with 49% market share of the private sector. The company is present in 154 municipalities in 13 states, through 43 concessions, 6 public-private-partnerships (PPPs) and 1 sub-concession, with 29 years of average remaining concession period. In December 2021, the company serviced 7.3 million active households (including Aguas do Rio). In 2021, AEGEA reported net revenue of BRL2.9 billion and EBITDA of BRL1.8 billion. FFO interest coverage was 1.9x in the year and Debt to Capitalization 53%, as per Moody's standard adjustments.

AEGEA's shareholders are Equipav (52.8% stake), the Government of Singapore Investment Corporation (GIC, 34.3% stake) and Itausa S.A. (Itaúsa, not rated, 12.9% stake).

The principal methodology used in these ratings was Regulated Water Utilities published in June 2018 and available at [https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC\\_1121971](https://www.moody.com/researchdocumentcontentpage.aspx?docid=PBC_1121971).

Alternatively, please see the Rating Methodologies page on [www.moodys.com](http://www.moodys.com) for a copy of this methodology.

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