

## **FITCH AFFIRMS C.A. LA ELECTRICIDAD DE CARACAS' IDR AT 'B+'**

Fitch Ratings-New York-01 March 2010: Fitch Ratings has affirmed the following ratings of C.A. La Electricidad de Caracas (EDC):

- Foreign currency Issuer Default Rating (IDR) at 'B+';
- Local currency IDR at 'B+';
- USD13.2 million outstanding senior notes due 2014 at 'B+/RR4';
- USD650 million outstanding senior notes due 2018 at 'B+/RR4';
- Long-term national scale rating at 'AAA(ven)';
- Short-term national scale rating at 'F1+(ven)'.

The Rating Outlook is Stable.

Strong Linkage to the Sovereign:

EDC's ratings reflect the company's strong credit linkage with its majority shareholders, Petroleos de Venezuela S.A. (PDVSA), as well as with the Bolivarian Republic of Venezuela, its ultimate shareholder. The company receives explicit support from both PDVSA and the government in the form of subsidized fuel costs, access to foreign currency and government assistance with capital expenditure programs. In FY 2009 transfers from the government are expected to be approximately USD500 million and to more than double in the future. By May 2, 2010, the Venezuelan government plans to spin off EDC from PDVSA to Corpoelec, a new state-owned entity that will consolidate all of the country's power assets. The Venezuelan government controls directly 75% of Corpoelec while PDVSA controls the remaining 25%. Fitch expects the government to continue supporting EDC and the sector due to its strategic importance to the country.

Further, Dramatic Credit Metrics Deterioration Expected:

Fitch expects EDC's credit metrics to continue to deteriorate sharply due to the lack of tariff increases since 2006, the recent devaluation of the local currency and high inflation levels. Tariff increases remain dismal due to the government's efforts to curb inflation, particularly in 2010 which is an election year. Since EDC was nationalized by the government in 2007, the company has begun several investment projects aimed at increasing its generation capacity and improving its distribution and transmission assets. In the last 12 months (LTM) ended Sept. 30, 2009 capital expenditures were USD900 million up from USD536 million and USD203 million in 2008 and 2007, respectively. These investments together with EBITDA declines have resulted in net leverage of 3.2 times (x) compared to 1.5x in 2008 and 0.5x in 2007.

Declining Margins May Turn Negative:

Significant deterioration in cash flow generation is also explained by a tariff freeze since 2006 while costs increases reflect inflation levels of more than 20% per year. During the LTM ended Sept. 30, 2009, EDC's EBITDA declined to approximately USD129 million from USD203 million and USD334 million in 2008 and 2007, respectively. The company's EBITDA margin has also declined to 15% as of the LTM ended Sep. 30, 2009 from 24% and 33% for 2008 and 2007, respectively. Absent a tariff increase, EBITDA margins are likely to turn negative within the next 2 years. By the second quarter of 2009 LTM funds from operations (FFO) turned negative, and as a result the LTM free cash flow burn run rate of USD928 million at September 2009, has been higher than capital expenditures. This situation is sustainable only with the support of the Venezuelan government which is expected to transfer to the company more than USD500 million per year to fund its operations and investments.

Solid Liquidity Dependent on Government Transfers:

As of Sept. 30, 2009, EDC had USD240 million in cash on hand and USD2 million in short-term debt. EDC was able to maintain a solid cash position due to asset sales despite negative free cash flow generation. A tariff increase would possibly turn FFO positive and allow the sector as well as EDC to be profitable and self-sufficient. EDC's solid cash position depends on the government's support due its aggressive capex plans and lack of access to other sources of financing. Total debt of USD654 million is comprised primarily of the USD650 million notes due in 2018 that were issued during 2008 so debt maturities are quite manageable until this notes are due.

#### Factors That Could Trigger a Downgrade:

- A downgrade of the Bolivarian Republic of Venezuela;
- A sustained leverage increase, liquidity deterioration and/or absence of a tariff increase within the next 18 months.

#### Factors That Could Trigger an Upgrade:

- An upgrade of the Bolivarian Republic of Venezuela;
- Lower leverage levels and/or the implementation of a tariff structure that reflects inflation increases and fuel costs.

EDC is a vertically integrated electricity company in Venezuela with operations in generation, transmission and distribution of electricity services to the metropolitan Caracas area. As the sole provider of electricity in Caracas, the company is viewed to be a strategic asset of the Venezuelan government. PDVSA, the state owned oil company, currently owns 93.62% of EDC.

These rating actions reflect the application of Fitch's current criteria which are available at '[www.fitchratings.com](http://www.fitchratings.com)' and specifically include the following reports:

- 'Corporate Rating Methodology', (Nov. 24, 2009);
- 'Credit Rating Guidelines for Regulated Utility Companies', (July 31, 2007);
- 'Rating of Public Sector Entities', (Feb. 1, 2007);
- 'Parent and Subsidiary Linkage' (June 17, 2007).

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