FitchRatings

RATING ACTION COMMENTARY

Fitch Revises Outlook of ColTel to Negative; Affirms Ratings

Fri 09 Jun, 2023 - 3:16 p. m. ET

Fitch Ratings - Chicago/Bogota - 09 Jun 2023: Fitch Ratings has affirmed all of Colombia Telecomunicaciones S.A. E.S.P.'s (ColTel) ratings, including the Long-Term Foreign Currency (FC) and Local Currency (LC) Issuer Default Ratings (IDR) at 'BBB-' and the National Scale rating at 'AAA(col)'. The ratings on ColTel's USD500 million of notes due 2030 and on local issuances of bonos ordinarios were affirmed at 'BBB-' and 'AAA(col)', respectively . The National Short-Term rating was affirmed at 'F1+(col)'. The Rating Outlook has been revised to Negative from Stable.

The Negative Outlook reflects the increased likelihood that the company's cash flow generation will continue to be pressured due to cost pressures, intense competition and spectrum payments, which could reduce the company's ability to deleverage to levels within sensitivities for its 'BBB-' rating.

KEY RATING DRIVERS

High Leverage: ColTel's net leverage will remain around 3.5x, which is weak for the rating assuming no material improvement in its cash flow generation due to cost pressures, spectrum renewal license fees and higher interest rates. Fitch expects net debt to increase due to negative FCF projected at about COP400 billion in 2023. Fitch adjusted EBITDA is forecast to remain flat at COP1.1 trillion in 2023 when compared with 2022 and to recover to COP1.3 trillion in 2024. This compares with COP1.4 trillion in 2021.

Intense Price Competition: The Colombian mobile market should continue to show significant pricing pressure as incumbent operators maintain promotional activity. Industry average revenue per user (ARPU) is likely to be particularly pressured in postpaid as WOM Colombia S.A.S. seeks to become a relevant player. The country's mobile penetration, which is above 150% compared with 135% in 2019, is also contributing to lower ARPU. Competition is growing in fixed broadband as well, although Fitch expects ColTel to be a challenger in this segment, with fiber-optic expansion accelerating customer acquisitions and leading to market share gains over the rating horizon.

Upcoming Spectrum Renewals Add Pressure: Fitch expects already depressed industry cash flows to face added pressure as a result of license renewals. During 2023-2024, Colombia's main four operators face renewal processes of around 50% of their combined spectrum holdings. The cost of renewal and the timing of payments are unknown. ColTel renewed 15 MHz of its 1,900MHz spectrum permit for COP555 billion in 2022. The company has paid 30% of this amount, with the remaining 70% to be paid in equal yearly instalments through 2037.

Good Market Positions: ColTel enjoys good market position as the second-largest mobile operator in Colombia, behind America Movil S.A.B. de C.V.'s (A-/Positive) subsidiary Claro Colombia S.A., which is roughly twice the size, and is the third-largest in broadband internet. The company's competitive position is supported by subscriber shares of 25% in mobile and 15% in broadband. These market shares have stayed generally stable over time. In addition, the company has a solid business-to-business offering, which generates approximately 25%-30% of its consolidated revenue.

Parent and Government Linkages: A link exists between the company and its 67.5% owner, Telefonica SA (BBB/Stable); however, the ratings of ColTel are on a standalone basis and do not assume support from Telefonica, as legal, strategic and operational support incentives are low. There are no debt guarantees or cross-default clauses between the two, and ColTel accounts for only about 3% of Telefonica's consolidated revenues. Operational incentives are relatively weak, as the company's subsidiaries tend to be independently managed and financed. The Colombian government has a 32.5% stake in the company but does not exert control over the management of ColTel; therefore, the ratings are also not directly linked.

DERIVATION SUMMARY

ColTel's overall business and financial profile is similar to direct competitor Tigo Une, with a similar revenue share of the overall Colombian market, although Tigo Une has a longer history of maintaining lower leverage. Tigo Une is also relatively stronger in the fixed broadband and PayTV business, which could imply more subscription-like cash flows, as the Colombian mobile market is mostly pre-paid. Tigo Une's ratings are constrained by Colombia's 'BBB-' Country Ceiling.

Telefonica del Peru, S.A.A. (TdP; BB-/Negative), has a strong market share in fixed, at approximately 60%, while Peru's relatively uniform four operator mobile market is competitive. ColTel carries lower leverage than TdP and has a superior cash flow profile as TdP's profitability has suffered even more than ColTel's in recent years.

Compared with Telefonica Moviles Chile S.A. (BBB+/Negative), ColTel has weaker market share and a less conservative financial structure. Empresa Nacional de Telecomunicaciones S.A.'s (ENTEL; BBB/Stable) has strengthened due to increased penetration in the Peruvian market and debt reduction. ENTEL benefits from its status as the largest Chilean mobile operator with a leading post-paid market share and ARPUs, and continues to operate in two very competitive markets. ColTel's greater scale and diversified revenue streams compare favorably with Colombian fixed-line provider Empresa de Telecomunicaciones de Bogota, S.A., E.S.P. (BB+/Stable), which has a conservative financial structure.

KEY ASSUMPTIONS

Fitch's Key Assumptions Within the Rating Case for the Issuer Include

--Net mobile subscriber additions of 500,000 in 2023 and 300,000 in 2024;

--Mobile ARPUs declining by mid-single digits in 2023 and begin to stabilize in 2024;

--Fixed RGU's grow high-single digits in 2023 and low-single digits in 2024;

--Blended fixed ARPUs grow 2% in 2023 and in 2024;

--Fiber take-up rate at 25.0% in 2023 and 25.5% in 2024;

--Operating costs and expenses grow high-single digits in 2023 and moderate in 2024;

--Capex of around 12% of revenue, including spectrum renewal.

RATING SENSITIVITIES

Factors that could, individually or collectively, lead to positive rating action/upgrade:

--A positive action in ColTel's FC IDR is unlikely absent a positive action to Colombia's sovereign rating;

--Total debt/EBITDA falling below 2.00x or net debt/EBITDA falling below 1.75x on a sustained basis due to strengthening of the competitive position and/or FCF being used to pay down debt, along with an improvement in the strength of ColTel's broadband and Pay TV market position could lead to an upgrade in the LC IDR.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

--Total debt/EBITDA rising above 3.0x or net debt/EBITDA rising above 2.75x on a sustained basis due to a weakening of competitive position, dividends and/or debt-financed acquisitions;

--Capitalization-adjusted net leverage over 3.25x, on a sustained basis;

--A downgrade of Colombia's sovereign rating.

BEST/WORST CASE RATING SCENARIO

International scale credit ratings of Non-Financial Corporate issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

LIQUIDITY AND DEBT STRUCTURE

Adequate Liquidity: Liquidity is supported by operating cash flow generation and a manageable debt amortization profile. The company had cash and equivalents of COP160 billion as of 1Q23 and maintains good access to bank debt. The company faces COP348 billion of local notes and COP298 billion bank debt, which Fitch expects the company to refinance over the next twelve months. ColTel repaid COP526 billion in bank debt due 2023 during 1Q22 with the proceeds from the sale of its fiber optic broadband assets. ColTel's USD500 million 2030 bond is fully hedged, which reduces FX risk.

ISSUER PROFILE

ColTel is an integrated telecommunications provider that offers mobile, fixed voice, Pay TV and broadband services to consumers, businesses, and government customers in Colombia. The company is 67.5% owned by Telefonica S.A. of Spain and 32.5% owned by the Colombian government.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

ESG CONSIDERATIONS

Unless otherwise disclosed in this section, the highest level of ESG credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

RATING ACTIONS

ENTITY / DEBT	RATING			PRIOR
Colombia Telecomunicaciones S.A. E.S.P. BIC	LT IDR	BBB- Rating Outlook Negative	Affirmed	BBB- Rating Outlook Stable
	LC LT IDR	BBB- Rating Outlook Negative	Affirmed	BBB- Rating Outlook Stable
	Natl LT	AAA(col) Rating Outlook Negative	Affirmed	AAA(col) Rating Outlook Stable
	Natl ST	F1+(col)	Affirmed	F1+(col)
senior unsecured	LT	BBB-	Affirmed	BBB-

senior unsecured	Natl LT	AAA(col)	Affirmed	AAA(col)

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Government-Related Entities Rating Criteria (pub. 30 Sep 2020)

National Scale Rating Criteria (pub. 22 Dec 2020)

Parent and Subsidiary Linkage Rating Criteria - Effective from 1 December 2021 to 16 June 2023 (pub. 01 Dec 2021)

Corporate Rating Criteria (pub. 28 Oct 2022) (including rating assumption sensitivity)

Sector Navigators: Addendum to the Corporate Rating Criteria (pub. 12 May 2023)

APPLICABLE MODELS

Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.1.0 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

Colombia Telecomunicaciones S.A. E.S.P. BIC	EU Endorsed, UK Endorsed

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