FitchRatings

RATING ACTION COMMENTARY

Fitch Affirms UNE EPM Telecomunicaciones S.A. at 'BBB-'

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Fitch Ratings - Chicago/Bogota - 12 Jul 2022: Fitch Ratings has affirmed all of UNE EPM Telecomunicaciones S.A.'s (Tigo UNE) ratings, including the Long-Term (LT) Foreign Currency (FC) Issuer Default Rating (IDR) rating at 'BBB-', Local Currency (LC) IDR at 'BBB', National LT Rating at 'AAA(col)', and the COP unsecured notes rating at 'AAA(col)'. The Rating Outlook is Stable.

The ratings reflect Tigo UNE's position as the third largest player in an increasingly competitive Colombian market, as well as the company's strong capital structure and financial flexibility. The ratings are constrained by the Country Ceiling of Colombia.

KEY RATING DRIVERS

Country Ceiling: Tigo UNE's FC IDR is constrained by the 'BBB-' Country Ceiling of Colombia (BB+/Stable). Following the downgrade of the Colombian sovereign in July 2021, Fitch downgraded Tigo UNE, as the company does not have substantial assets or operations abroad to reduce transfer and convertibility risk. The LC IDR reflects the company's strong financial structure and is not constrained by the Country Ceiling.

Strong Financial Structure and Flexibility: Tigo UNE has been able to maintain a solid financial profile, evidenced by consistently low leverage and stable cash flow generation.

Fitch expects the company to maintain relatively conservative leverage, with debt/EBTIDA and net debt/EBITDA to remain relatively steady over the rating horizon at around 2.2x and 2.0x, respectively. These levels are relatively strong for a 'BBB-' operator and compares well to regional peers. Tigo UNE benefits from its long-dated and well-spread amortization profile.

Market Position and Competitive Intensity: Tigo UNE is the third-largest telecom operator in Colombia in terms of revenue, approximately 60% smaller than Claro Colombia (subsidiary of America Movil S.A.B. de C.V.) and 10% smaller than Colombia Telecomunicaciones S.A. E.S.P (BBB-/Stable). Tigo UNE is the second-largest provider of broadband internet services, pay TV and fixed telephony, and the third-largest provider of mobile services in terms of subscribers. Tigo UNE's relative strength in fixed line, strong spectrum position aligned with its coverage strategy, and mobile network buildout should enable the company to weather WOM Colombia's entry into the country's mobile market.

Network Investments Drive Growth: The company has seen rapid growth in its hybrid/fiber broadband and postpaid mobile subscribers in 2021 and into 2022 following significant network investments. Longer term, Fitch expects the company to maintain its strong position in the fixed business despite heavy investments by competitors in fiber deployment, as increasing broadband penetration and ARPUs should drive higher B2C fixed revenues. These dynamics should help offset WOM's entry into the mobile market.

Cash Flow Compression: Fitch expects the company's EBITDA margins to be constrained in the mid-20% range in the medium term as strong postpaid subscriber growth is offset by competitive pressures on ARPUs while inflation weighs on operating expenses. Fitch also expects the company to post modestly negative FCF over the rating horizon on continued large network investments, which will likely lead to additional debt financing in the coming years. Fitch expects capital intensity to remain above 20% over the forecast horizon, an increase from the 18% average capital intensity during 2015-2019. The company's profitability is in line with the median of 'BBB-' operators.

Broad Offerings Offset Weak Geographic Diversification: Tigo UNE is well-diversified across fixed, mobile, and B2B, with respective revenue shares of 40%, 36%, and 20% during 2021. The company's service diversification compares well with other investment-grade operators in the region. Tigo UNE operates entirely within the Colombian telecommunications market, which has continued to grow more competitive following the entry of WOM Colombia. The company does not benefit from the stronger diversification of its parent, Millicom, which has operations across Latin America.

Parent Subsidiary Linkages: Tigo UNE's ratings incorporate weak linkages with both Empresas Publicas de Medellin E.S.P. (EPM; BB+/RWN) and Millicom International Cellular S.A. (Millicom, BB+/Stable). The ratings of these two entities are limited by sovereign risks, the first as a Colombian government related entity and the second by the majority of its cash flows from speculative grade countries. While UNE EPM is structured as a 50/50 JV, of the two parent entities, Millicom exerts greater influence. With open legal ring-fencing and insulated access and control, Tigo UNE can be rated up to two notches above Millicom.

DERIVATION SUMMARY

Tigo UNE's overall business is similar to that of direct competitor Colombia Telecomunicaciones (BBB-/Stable), with similar revenue shares 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 pay-TV business, which could imply more subscription like cash flows, as the Colombian mobile market is mostly prepaid. Tigo Une's ratings are constrained by Colombia's 'BBB-' Country Ceiling.

Tigo UNE has a similar profile to Empresa Nacional de Telecomunicaciones S.A. (ENTEL; BBB/Stable). ENTEL's profile 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 leading post-paid market share and ARPUs, while continuing to operate in two very competitive markets.

Similarly, Tigo UNE's overall credit profile is much stronger than 'BB' category domestic telecom peers, such as Empresa de Telecomunicaciones de Bogota, S.A., E.S.P. (ETB; BB+/Stable). Fitch estimates ETB will find it difficult to improve EBITDA performance given its low network penetration and rapidly contracting cash flow generation. Another 'BB' category peer, Telefonica del Peru, S.A.A. (TdP; BB+/Negative), has a strong market share in fixed, at approximately 60%, while Peru's relatively even four-operator mobile market is even more competitive than Colombia's. Tigo UNE carries lower leverage than TdP and has a superior cash flow profile as TdPs profitability has suffered in recent years.

Tigo UNE's 'BBB-' ratings are two notches below Telefonica Moviles Chile S.A. (BBB+/Stable), the leading integrated telecommunications service provider in Chile. In comparison, Tigo UNE holds a secondary position in Colombia behind Claro in the fixed business, and is the third-largest mobile player, by market share.

Tigo UNE's ratings incorporate a linkage with Millicom (BB+/Stable), which holds the controlling majority of shares in the company. Despite the absence of a ring-fencing mechanism to limit Tigo UNE's cash upstream to its controlling shareholder, Fitch does not expect this relationship to impair Tigo UNE's ability to execute its capex strategy while maintaining a credit profile in line with the current rating. Tigo UNE is one of Millicom's most important EBITDA contributors to the consolidated Millicom group, highlighting its financial importance to the parent's credit profile.

KEY ASSUMPTIONS

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

--100k-160k incremental homes passed each year through 2024; HC/HP around 31%-32%;

--Broadband and pay TV RGUs growing in the low-mid-single digits; overall Home bundling ratio steady around 2.45x;

--Home ARPU growth roughly flat due to positive broadband ARPU growth offset by declining TV and Fixed Line ARPUs; home revenue growing in the low-to-mid-high single digits;

--B2B Revenue growth in the low single digits;

--Total mobile RGUs growing in the low single digits longer term after a strong 2021, while conversion of customers from prepaid to postpaid continues;

--Blended mobile ARPUs rebounding in 2022 from mix-shift effects from strong postpaid growth; overall mobile revenues higher in 2022 driven by strong postpaid performance, growing low-single-digits longer term;

--EBITDA margins recovering modestly from 2021, but will remain constrained due to high levels of competition;

--Capex of >COP1.1T per year, at roughly 21% of revenues; 2023 expected to be relatively higher due to spectrum renewals;

--Debt/EBITDA of around 2.1x-2.3x and net debt to EBITDA of around 1.9x-2.0x, consistent with historical levels;

--No material dividends over the rating horizon as the company focuses on investments.

RATING SENSITIVITIES

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

--An upgrade of the Colombian sovereign rating would lead to an upgrade for Tigo UNE's FC IDR;

--Total debt/EBITDA falling below 2.0x or net debt/EBITDA falling below 1.5x on a sustained basis due to a strengthening of the competitive position and/or FCF being used to pay down debt due to successful implementation of growth strategy and response to competitive threats.

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

--Deterioration in market position due to higher than expected increase in competition;

--Persistently negative FCF generation due to higher than expected shareholder distributions and/or capex;

--Total debt/EBITDA increasing to over 3.5x, or net debt/EBITDA above 3.0x on a sustained basis.

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

Solid Liquidity: Tigo UNE has strong liquidity, with COP235 billion in cash and equivalents as of March 31, 2022. The company benefits from its conservative capital structure, relatively stable cash flow generation, and well-spread maturity schedule. These factors contribute to a financial structure flexibility that is strong for the rating level.

As of March 31, 2022, the company's debt totaled COP2.8 trillion, of which 93% was COP denominated, with the remainder comprised of a USD50 million syndicated loan. The company's debt is evenly split between bank loans and COP bonds.

The cash balance represents a decrease from COP804 billion at the end of 2021; mainly due to the reduction of debt during 1Q22. Fitch expects the company to generate modestly negative FCF over the coming years as competitive pressures and investment requirements reduce cash flow generation.

ISSUER PROFILE

UNE EPM Telecomunicationes S.A. (Tigo UNE) is an integrated telecommunications services provider in Colombia. The company offers mobile, broadband internet, fixed telephony, and Pay-TV. The company operates as a JV between Millicom International Cellular S.A. and Empresas Publicas de Medellin (EPM).

SUMMARY OF FINANCIAL ADJUSTMENTS

Standard lease adjustments.

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 ⬍

UNE EPM Telecomunicaciones S.A.	LT IDR	BBB- Rating Outlook Stable Affirmed	BBB- Rating Outlook Stable
	LC LT IDR	BBB Rating Outlook Stable Affirmed	BBB Rating Outlook Stable
	Natl LT	AAA(col) Rating Outlook Stable Affirmed	AAA(col) Rating Outlook Stable
senior unsecured	Natl LT	AAA(col) Affirmed	AAA(col)

VIEW ADDITIONAL RATING DETAILS

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APPLICABLE CRITERIA

Country Ceilings Criteria (pub. 01 Jul 2020)

National Scale Rating Criteria (pub. 22 Dec 2020)

Corporate Rating Criteria (pub. 15 Oct 2021) (including rating assumption sensitivity)

Sector Navigators - Addendum to the Corporate Rating Criteria (pub. 15 Oct 2021)

Parent and Subsidiary Linkage Rating Criteria (pub. 01 Dec 2021)

APPLICABLE MODELS

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

Corporate Monitoring & Forecasting Model (COMFORT Model), v8.0.2 (1)

ADDITIONAL DISCLOSURES

Dodd-Frank Rating Information Disclosure Form

Solicitation Status

Endorsement Policy

ENDORSEMENT STATUS

UNE EPM Telecomunicaciones S.A.	EU Endorsed, UK Endorsed

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Technology, Media, and Telecom Corporate Finance Latin America Colombia

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