S&P Global Ratings

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Research Update:

Georgia Global Utilities Upgraded To 'B+' From 'B' Post-Acquisition By FCC Aqualia; Outlook Positive

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Rating Action Overview

- In October 2022, Spanish water utility FCC Aqualia became the 80% owner of Georgia Global Utilities (GGU) through Aqualia Georgia LLC, with some of the renewables assets spun off to Georgia Capital (GCAP; the remaining 20% shareholder).
- Throughout the process, GGU refinanced entirely the $250 million bond due 2025 partly with a shareholder loan totaling $164 million from FCC Aqualia and a shareholder loan by Georgia Capital, therefore lowering its debt quantum.
- Given the shareholder support, we see GGU as a moderately strategic asset for FCC Aqualia and therefore benefitting from shareholder support.
- We therefore raised our long-term issuer credit rating on GGU to 'B+' from 'B'.
- The positive outlook indicates that we could upgrade GGU should it continue to maintain strong rating headroom, with constantly improving funds from operations (FFO) to debt.

Rating Action Rationale

FCC Aqualia as GGU's new 80% shareholder translated into its lower debt quantum. The first stage of the transaction was complete in February 2022, with FCC Aqualia (BBB-/Negative/--) purchasing 65% of GGU from GCAP for $180 million. The final step concluded with FCC Aqualia owning 80% of GGU and GCAP 20%--following the full repayment of the $250 million bond. In August 2022, GGU signed two intercompany loans with its shareholders amounting to their pro rata share of debt. As a result, FCC Aqualia and GGU signed a $164 million intercompany facility maturing in August 2024, which represents the sole financial debt on GGU's balance sheet. GCAP's intercompany loan is on the renewable business's balance sheet. As a result, GGU's long-term liability decreased to $164 million from $250 million, improving our S&P Global Ratings-adjusted ratios.

GGU is now composed of the water utility business (about 80% of EBITDA) in addition to the retained 149 megawatts (MW) of renewables assets (about 20%). The remaining renewable assets (71 MW operating) were spun off and are fully owned by GCAP, a transaction that we see as credit positive from a financial perspective.

We view GGU as a moderately strategic subsidiary for FCC Aqualia, which provides one notch of uplift to GGU's stand-alone credit profile. Since October 2022, GGU is 80% owned by FCC Aqualia and 20% by GCAP. We believe GGU exhibits significant features that qualify it for a one notch uplift upon extraordinary support from FCC Aqualia including:

- GGU operates in line with FCC Aqualia's business of water distribution and supply;
- It operates a regulatory asset base based water supply network that provides stable cash flows and therefore is unlikely to be sold in the medium to long term;
- GGU will be fully consolidated into FCC Aqualia and will represent 10%-15% of Aqualia's EBITDA over the next two years;
- A long-term strategy will be jointly defined at the GGU level by FCC Aqualia's management and GGU's personnel; and
- FCC Aqualia is committed to supporting GGU, as demonstrated by the intercompany loan signed to repay the bond.

The lack of a clearly defined and transparent financial policy and strategy at GGU prevents us from viewing it as more than strategic for FCC Aqualia. Should we see a record of support, the extension of shareholder loan, or a refinancing of the intercompany loan at group level in addition to a defined and supportive financial policy, we could review our assessment of GGU's importance within the FCC Aqualia group.

We expect a favorable framework to enable full recovery of increasing investments over the new regulatory period (2024-2026) and to support metrics including FFO to-debt well above 12%. Following the repayment of the $250 million bond with two intercompany loans as part of the transaction, GGU's long-term liability materially decreased in October 2022 to $164 million from $250 million at year-end 2021. In addition, although we expect GGU to enter another investment cycle with investments higher than GEL150 million over 2023-2024, we believe investments will be recovered through higher tariffs over 2024-2026 (as was done in 2021-2023 when we saw a 47.8% increase for commercial customers and a 52% increase for residential customers). Lastly, we believe GGU's electricity generation business will continue to benefit from high power prices over 2022-2023, which will reduce the effect of lower generation following the spin-off of 30% of the renewable generation capacity and enable GGU to maintain strong annual EBITDA generation of GEL130 million-GEL140 million (about €50 million). This leads to our forecast of GGU's S&P Global Ratings-adjusted FFO to debt substantially above 12% over the next two years.

We view GGU's capital structure as pressured by the short-term intercompany loan and skewed toward foreign currency debt. While we view the refinancing of GGU's $250 million 7.75% bond due 2025 with a $164 million intercompany loan due 2024 provided by FCC Aqualia as positive for ratios, we believe the loan's short length (two years) will pressure the utility's capital structure. However, we understand there might be a commitment by the new owner to extend the loan's maturity, although it has not been contractually signed. Also, GGU's interests will decrease to quarterly payments of $3.3 million (GEL9 million) from semiannual payments of $9.3 million (GEL25.3 million) that we believe can be covered by the electricity generation business under current conditions. Should electricity prices materially fall, we could see the utility as more exposed to foreign exchange (FX) risks as its U.S. dollar-denominated business might not fully cover coupon payments; however, this is not in our base case. We will reassess our base-case scenario in the upcoming months.

Outlook

The positive outlook indicates that GGU could report stronger metrics derived from high electricity prices and a supportive regulatory framework with adjusted FFO to debt expected above 12% over 2022-2024, or could benefit from a higher group status upon integration within the FCC Aqualia group--including a detailed and supportive financial policy.

Downside scenario

We could change the outlook to stable if we see lower metrics including FFO to debt below 12% on a sustainable basis. This could stem from a less supportive financial policy, demonstrated by high dividend extraction or an intensive capital expenditure (capex) program not compensated for by higher tariffs.

Upside scenario

Several elements could lead to an upgrade of GGU, including:

- FFO to debt consistently above 12% with substantial headroom. This could derive from higher tariffs upon the new regulatory period starting January 2024, continuous high electricity prices benefitting the generation business, and flexibility in dividends and investments.
- No material exposure to foreign currency risk and an extension of debt maturities to above two years.
- Improvement of our regulatory framework assessment for water utility in Georgia upon the new period starting January 2024.
- Proof of stronger group support that could stem from a clearly defined and supportive financial policy as well as commitment to support GGU in case of distress.

Company Description

GGU is one of the largest privately owned utility companies in Georgia, which historically included natural monopoly water utility business and electricity generation. Following the transaction between FCC Aqualia and GCAP, GGU is now mostly composed of the water utility segment that provides water supply and wastewater services to 1.4 million customers in the capital of Georgia, Tbilisi, and its surrounding area as well as 149 MW of hydro power plants. The remaining generation capacity (71 MW operating) has been demerged and is fully owned by GCAP.

GGU's annual EBITDA should reach GEL130 million-GEL140 million (€40 million-€50 million) in 2022-2023 and grow once the new regulatory period for water networks starts in January 2024.

Our Base-Case Scenario

Assumptions

- GGU's $250 million bond successfully refinanced with shareholder support in 2022 through two shareholder loans:
- --$164 million from FCC Aqualia
- --$90 million from Georgia Capital
- Successful spin off of three renewable assets with their pro rata share of debt (e.g., GCAP's shareholder loan) leading to GGU's end of year gross debt of $164 million (GEL456 million equivalent at current FX of 2.80 USD/GEL).
- Stable revenues from the water regulated business of GEL170 million-GEL180 million combined with GEL30 million-GEL40 million from the electricity business, driven by higher prices over 2022-2023.
- EBITDA margin of 60%-65%.
- GGU's capex staying at about GEL90 million annually until the end of the regulatory period and increasing in line with FCC Aqualia's expectations to GEL150 million-GEL160 million annually.
- GEL20 million of dividends in line with historical distribution. This is subject to GGU's updated dividend policy that will be defined by FCC Aqualia throughout 2023.

Liquidity

We currently assess GGU's liquidity as less than adequate as we believe sources will not cover uses by more than 1.2x over the next 12 months--notably should investments or dividends increase in 2023 from our current base case. We also incorporate the short-term length of the shareholder loan, maturing in summer 2024, and GGU's healthy relationships with local banks and supranational institutions into our liquidity assessment.

We estimate that principal liquidity sources as of Sept. 30, 2022, include:

- GEL46 million of cash and cash equivalents.
- Our estimate of cash FFO of GEL70 million-GEL80 million.

We estimate that principal liquidity uses for the same period include:

- Up to GEL90 million of capex; and
- No dividends in 2022 but about GEL20 million dividends in 2023, in line with the historically paid amount.

Ratings Score Snapshot

Issuer Credit Rating	B+/Positive/--
Business risk:	Weak
Country risk	Moderately high
Industry risk	Very low

Issuer Credit Rating	B+/Positive/--
Competitive position	Weak
Financial risk:	Aggressive
Cash flow/leverage	Aggressive (standard volatility table)
Anchor	b+
Modifiers:	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Negative (-1 notch)
Financial policy	Neutral (no impact)
Liquidity	Less than adequate (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile:	b
Group credit profile	bbb-
Entity status within group	Moderately strategic (+1 notch)

ESG credit indicators: E-4, S-2, G-3

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | Industrials: Key Credit Factors For The Unregulated Power And Gas Industry, March 28, 2014
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011
- General Criteria: Stand-Alone Credit Profiles: One Component Of A Rating, Oct. 1, 2010

Ratings List

Upgraded

	To	From
Georgia Global Utilities JSC		
Issuer Credit Rating	B+/Positive/--	B/Stable/--
Issue-Level Ratings Withdrawn		
Georgia Global Utilities JSC		
Senior Unsecured	NR	B

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; or Stockholm (46) 8-440-5914