

# BRC Ratings

A Company of **S&P Global**

Colombia

## Rating report

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### GRUPO ARGOS S.A.

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# GRUPO ARGOS S.A.

## I. SUMMARY

- We upgraded the long-term debt rating on Grupo Argos' ordinary bonds to AAA from AA+ and affirmed the short-term debt rating on commercial paper at BRC1+. We have withdrawn our positive outlook.
- The rating upgrade is the result of the adequate results that the company would maintain in the medium term, which are evidenced by a leverage ratio between 2x (times) and 3x. This is the result of a 9.7% average annual growth in EBITDA and an 8% average annual reduction in debt between 2022 and 2024.
- The rating also incorporates Grupo Argos' solid business position, which we do not expect to change in the medium and long term. This is reflected in the diversification by type of business and the relevant market share of each of its subsidiaries in the geographies it serves.
- The projected source-to-use ratio is 1.2x and 1.1x for the next 12 and 24 months. This shows that Grupo Argos has sufficient capacity to meet its operating and financial commitments and reflects a cushion margin in the face of any unfavorable macroeconomic scenario.

## II. RATING ACTION

Bogotá, May 3, 2022.- The Technical Committee of BRC Ratings - S&P Global S.A. Sociedad Calificadora de Valores, in a periodic review raised the long-term debt rating to AAA from AA+ of the ordinary bonds, and confirmed the short-term debt rating of BRC 1+ of commercial paper.

## III. BASIS FOR THE RATING

In 2021 Grupo Argos reported favorable results in terms of revenues and EBITDA, which were above our projections. Thus, these two variables recorded values of COP 16.3 trillion Colombian pesos (COP) and COP 4.3 trillion, representing annual increases of 16.6% and 29.3%, respectively. In the same line, leverage (measured as net debt to EBITDA) was 3.2x<sup>1</sup> which is better than our estimates in previous reviews which were above 3.5x.

The sound leverage results are the result of the increase in EBITDA, which is associated with the favorable dynamics of all subsidiaries, as a result of the economic rebound observed in all the geographies served by the conglomerate, and the successful implementation of the strategy of each of the companies. The net debt to EBITDA indicator also benefited from the 1.6% reduction in financial liabilities, which is in line with Grupo Argos' guideline in all the conglomerate's companies.

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<sup>1</sup> According to Grupo Argos' calculations, this ratio would be 2.9x when including as part of the cash the Treasury bonds of the Dominican Republic Government that Odinsa received as payment for the termination of its interest in the road concessions in this country.

In 2021, Grupo Argos met some key milestones that allowed it to reduce debt and will be an important part of the conglomerate's efforts to optimize its capital structure and reduce indebtedness by an annual average of 8% between 2022 and 2024:

- **Divestment of non-strategic assets:** On the one hand, Cementos Argos continued to divest non-strategic assets and in 2021 sold concrete assets located in the United States, the proceeds of which were used to repay debt. On the other hand, Odinsa ended its interest in the road concessions in the Dominican Republic. Some of these resources have already been allocated to the payment of financial obligations and a new amortization of approximately COP 1 trillion is expected for 2022.
- **Consolidation of investment platforms to leverage growth:** This is the case of the closing of the transaction known as the road vertical, through which Odinsa and Macquarie Asset Management form an investment vehicle which, in principle, incorporates the road concessions in which Odinsa has an interest in Colombia. This transaction will allow the infrastructure subsidiary to reduce its capital needs in new projects and to have the knowledge and trajectory of this player that participates in international markets. It is worth mentioning that in the past we had already witnessed the execution of this type of investment agreements in Celsia through the execution of Caoba, with the private investment fund Cúbico. This reflects the conglomerate's ability to enter into such transactions and benefit from both the capital and the know-how of its strategic partner.

The expected reduction in debt does not imply a slower rate of growth of the subsidiaries. In line with Grupo Argos' guideline, this increase would originate from its operational generation and from alternative sources such as investment platforms that provide resources and experience, as is the case of Caoba and the recent road investment platform entered into by Odinsa.

The current scenario of macroeconomic volatility poses a factor of uncertainty regarding compliance with EBITDA projections. Despite this, we upgraded the rating taking into account the group's ability to flexibly operate in adverse conditions as shown during the pandemic. The rating also considers the cushion margin that the conglomerate would have by reducing its indebtedness, which would allow it to maintain the indicators defined for its rating, even in an event of lower operating generation.

As other corporations in the country, restrictions in global logistics and the international conflict have impacted Grupo Argos' operations. However, companies have been able to mitigate these impacts by increasing prices, sourcing and diversifying their suppliers, and sourcing and diversifying their raw materials.

We estimate EBITDA generation between COP 4.4 trillion and COP 5.7 trillion for the period 2022-2024 and an EBITDA margin between 25% and 30%, which remains in line with our previous estimates. This projection incorporates an average annual increase of 6% in revenues, resulting from the continuation of the positive trend observed in all businesses in 2021, albeit at a slower growth rate.

EBITDA generation would also benefit from the lower increase in operating expenses (costs and expenses) compared to revenues (4% annual average), which is due to a continuity in the cost and expense control policy defined by the conglomerate and to the deconsolidation in Odinsa's financial statements of the concessions that were incorporated in the road vertical and that

would be recorded under the equity method.

One of Grupo Argos' main competitive advantages is its diversification by business and geography. This condition was key to the performance of the conglomerate after the pandemic, as the magnitude of the impact and the speed of recovery of each of the subsidiaries was different.

Cementos Argos recorded an annual increase in sales and EBITDA of 9.1% and 33.9% at the end of 2021, which is due to the higher volumes sold in all geographies served, as a result of the economic rebound observed in all countries and the continuity of commercial strategies focused on customer service, such as the sale of products in digital media.

The cement subsidiary's sound results are also due to price adjustments that allowed it to pass on to the entire supply chain cost increases associated with global logistics constraints. An additional element that boosted EBITDA growth is the continuity in its plan to generate efficiencies that will be relevant in the future, given the volatile macroeconomic outlook.

For the next three years, sales performance will be associated with the sound dynamism of the housing sector in some geographies and the boost that local governments will continue to give to the infrastructure segment, as this is a sector that boosts the economy. In addition, we anticipate that the company could largely pass on further cost increases to the supply chain.

Celsia, a company in the electric power sector, reported a 16.3% and 10.7% increase in revenues and EBITDA, respectively, at the end of 2021. The sound financial dynamics are the result of the increased demand for electricity, which boosted the generation segment in Colombia and Central America. These results are also explained by the operational improvements of the transmission and distribution network in the two geographies served, resulting in an increase in the remuneration of this activity.

Celsia would continue to increase its installed generation capacity in non-conventional renewable energies and would complement its portfolio with the entry of its gas-fired generation plant. It would also continue to benefit from stable and predictable flows from the transmission and distribution business, which would increase as it maintains its investment path to improve service quality. Finally, the company has ventured into complementary businesses such as the sale of internet service and products and services focused on energy efficiency and the use of environmentally friendly fuels; however, we do not foresee relevant participations in the next three years.

Odinsa reported a 25.1% increase in revenues and a 40.7% reduction in EBITDA. It is worth mentioning that EBITDA incorporates an accounting effect associated with the divestment of the assets in the Dominican Republic. Without this effect, EBITDA would have been close to COP 699 billion, representing an annual growth of 76%.

Going forward, we foresee a favorable performance for Odinsa as air traffic continues its recovery path and road traffic continues its positive path linked to GDP growth. In the long term, the company's revenues would increase through the consolidation of new projects it is currently working on. This growth would also come from new projects to increase the country's logistics competitiveness, such as the Fifth Generation of Concessions (5G) program, whose dynamism will be linked to the Government's guidelines, which will begin in August 2022.

According to public information, the Gilinski Group acquired 31.5% and 30.8% of the shares of Grupo Suramericana and Grupo Nutresa, shareholders of GA, and as of the date of this report, the results of a third tender offer were pending. In principle, we do not foresee a direct impact on Grupo Argos' operations given the presence of these two organizations as shareholders of the Group and as part of the investment portfolio. However, we will follow up on this aspect and any changes that may occur on the rating.

In December 2021 Grupo Argos disclosed a series of strategies aimed at improving the profitability of its shareholders, which are still under development. We will monitor their implementation and the impact it may have on the conglomerate and/or its subsidiaries.

## **IV. LIQUIDITY**

The favorable results in terms of operating generation in 2021 led to cash flow from operating activities of COP 4.3 trillion, higher than the COP 2.8 trillion observed in 2020, which was sufficient to cover its CAPEX requirements. The greater dynamics in the execution of investment projects and the amortization of debt resulted in the use of cash of COP 177,164 million, but this was covered by the 2020 cash flow, which closed at COP 2.7 trillion.

Our projections allow us to anticipate an adequate generation of operating cash flow (COP 3 trillion - COP 4 trillion) which, together with the additional resources from divestments, would be sufficient to meet the debt amortization schedule proposed by the company, investment needs and to pay dividends to shareholders.

The sources and uses projection exercise shows a ratio of 1.2x and 1.1x for the next 12 and 24 months. These results reiterate Grupo Argos' ability to meet its commitments. Likewise, this liquidity indicator shows a maneuverability margin for the company in an adverse scenario.

For this exercise we took, in addition to the profitability scenario described above, the following assumptions:

- The company's total CAPEX. This is a change from the last review where we only included maintenance works.
- The incorporation of resources of COP 1 trillion derived from the divestment of Odinsa in the Dominican Republic and the creation of the investment platform called road vertical.
- Dividend payments in accordance with Grupo Argos' projections.

We believe that GA would have other sources of liquidity in a stress event such as:

- Proven access to the capital market and the financial sector, through available quotas of COP 2.4 trillion out of a total amount allocated COP 8.6 trillion.
- Execution of its maintenance capex. This is especially true for Cementos Argos and Celsia, whose expansion projects have some flexibility in a stress scenario.
- The possibility of paying dividends in shares.

## **V. FACTORS TO MODIFY THE RATING**

What can lead us to affirm the rating

- The use of alternative and stable sources of financing to leverage the expansion plan without generating pressure on its debt indicators.
- Sustainability of the net debt/EBITDA ratio below 3x over the next three years.
- Strengthening the group's growth in its three strategic areas.

What could lead to a downgrade

- Delays in the development of infrastructure projects that significantly impact the fulfillment of revenue and EBITDA projections of subsidiaries.
- Deterioration of the organization's liquidity level.
- Changes in its business position, which may imply loss of market share, relevant exposure to geographies with lower credit quality levels than Colombia or changes in business lines that in our opinion represent greater risks for the conglomerate.

## IV. ISSUER AND ITS ACTIVITY

Grupo Argos (GA) is a conglomerate with strategic investments in the infrastructure sector in the following industries: cement (Cementos Argos - CA), energy (Celsia) and road and airport concessions (Odinsa). In addition, it is a partner in a real estate fund (Pactia), owns a land bank for urban development (Grupo Argos Desarrollo Urbano) and has a solid investment portfolio in the financial and food sectors.

At the end of 2021, Cementos Argos maintained a share of around 50% by EBITDA level in Grupo Argos, similar to the previous year. We positively weight Celsia's share in Grupo Argos' EBITDA (30%) because, as mentioned, this company benefits from a stable and predictable flow from the transmission and distribution business.

The concession business showed a recovery in terms of share of total EBITDA. Thus, at the end of 2021 it showed an increase to levels of 10% from the 1% observed the previous year. This is explained by the continued good performance of road traffic and the recovery observed in the number of passengers in the air infrastructure.

In addition to its operations, Grupo Argos receives income from its real estate business and its portfolio, which represented close to 10% of EBITDA. These investments provide a higher level of diversification and greater availability of resources in stress scenarios.

## VII. INDUSTRY RISKS

The general characteristics of the sectors in which Grupo Argos participates remained relatively stable compared to the previous year:

- High capital requirements and energy use.
- Barriers to entry in terms of infrastructure (plants, access to raw materials, equipment), knowledge, experience, financial muscle, and ease of access to financing sources.
- Strong correlation with economic cycles and population dynamics.

- Long business cycles, which implies long payback periods for its investments.
- Exposure to regulatory and policy changes.
- Dependence on public policies.

The ratings of the most relevant countries for the organization are summarized in the following table, as well as the growth projections for 2022 and 2023 made by S&P Global Ratings:

Table 1. Ratings and GDP growth projections in the countries in which Grupo Argos operates						
Country	Long-term sovereign rating in foreign currency for S&P Global Ratings Outlook	Outlook	2022 (%)	2023 (%)	Date of last review	
Colombia	BB+	Stable	4.6	3.0	05 May 22	
United States	AA+	Stable	3.4	2.4	08 Mar 22	
Panama	BBB	Negative	7.5	5.0	04 Aug 21	
Aruba	BBB	Stable	9.9	5.2	22 Mar 22	
Dominican Republic	BB-	Stable	6.0	5.0	02 Dec 21	
Honduras	BB-	Stable	3.5	3.6	26 May 21	
Costa Rica	B	Stable	3.6	3.2	17 Mar 22	
Ecuador	B-	Stable	3.0	2.0	26 Aug 21	

Source: S&P Global Ratings

## VIII. ADDITIONAL INFORMATION

Type of rating	Long-term and short-term debt
Minute number	2115
Committee date	May 3, 2022
Type of review	Periodic review
Issuer	Grupo Argos S.A.
Committee members	María Carolina Barón
	Fabiola Ortiz
	Maria Soledad Mosquera

### Rating history

Periodic review May /22: AAA / BRC1+  
 Periodic review May./21: AA+ PP / BRC1+  
 Initial rating May/14: AAA / BRC1+

*The technical visit for the rating process was carried out with sufficient advance due to the availability of the issuer or entity and the information was delivered on time and in accordance with the requirements of BRC Ratings - S&P Global S.A. SCV.*

*BRC Ratings - S&P Global S.A. SCV does not perform auditing functions; therefore, the entity's management assumes full responsibility for the completeness and truthfulness of all the information provided and which has served as the basis for the preparation of this report. On the other hand, BRC Ratings - S&P Global S.A. SCV reviewed the publicly available information and compared it with the information provided by the entity.*

The financial information included in this report is based on audited financial statements for the last three years. The financial information included in this report is based on the financial

statements of the unconsolidated bank.

If you have any questions regarding the indicators included in this document, please consult the glossary at [www.brc.com.co](http://www.brc.com.co).

For definitions of our ratings, please visit [www.brc.com.co](http://www.brc.com.co) or click [here](#).

## **IX. MEMBERS OF THE TECHNICAL COMMITTEE**

The resumes of the members of the Technical Rating Committee are available on our website [www.brc.com.co](http://www.brc.com.co).

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