BRC
Standard & Poor's
S&P Global

Colombia

**Rating Report**

# GRUPO ARGOS S.A.

**Technical Committee:** May 7, 2021
**Minutes number:** 1914

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## GRUPO ARGOS S.A

### Summary


- We confirm the long-term debt ratings of AA+ of the bonds and BRC1+ of the commercial papers issued by Grupo Argos S.A. We assign a positive outlook.
- The rating confirmation considers the adequate payment capacity of Grupo Argos in adverse scenarios such as 2020. This is a product of the organization's quick decision-making in relation to its operations and its easy access to the financial sector and the capital market through innovative structures such as bond swaps.
- The positive outlook considers our projections of a recovery of leverage indicators to 3x (times) levels in the next two years, which responds to a favorable EBITDA performance, driven by the cement and energy businesses, coupled with low growth in debt levels.
- Our projection scenario assumes a gradual recovery of the economies in which Grupo Argos participates. This becomes relevant considering the uncertainty we identify in the performance of Latin American countries and particularly in Colombia, where the economy could be impacted by possible virus outbreak events and the current social situation.
- BRC will review the rating to the extent that current events have long-term impacts on the company's results.


### Rating Action

Bogota, May 7, 2021.- The Technical Committee of BRC Investor Services S.A. SCV in its periodic review confirmed the long-term debt ratings of AA+ of the bonds and BRC1+ of the commercial papers issued by Grupo Argos S.A. It also assigned a positive outlook.

### Rating Rationale:

The spread of the COVID-19 pandemic and the measures to contain it affected Grupo Argos' results, which we evidenced in most of the rated companies. In response to the situation, GA implemented a timely contingency plan, which allowed it to maintain adequate liquidity levels to meet its operating, financial and shareholder commitments.

At the end of 2020, the organization reported a reduction in EBITDA margin to levels of 24%, from 28%, annual average, in 2018 and 2019. This generated an increase in leverage towards 4.2x (times), a value that was close to our previous year's estimates and would be reduced towards 3x in the following two years. This projection supports the assignment of the positive outlook.

Our projections include the following assumptions:

- Revenues between $15 trillion Colombian pesos (COP) and COP16 trillion. This represents an increase of around 5% between 2021 and 2023.
- A gradual growth of EBITDA to COP5 trillion in 2023. These expectations take into account the increase in revenues and the benefits associated with the structural operating efficiencies achieved by the organization in 2020.

The deleveraging path projected for the organization is based on a recovery in profitability of around 30% and a level of indebtedness close to COP15 trillion. The resolution of the positive outlook will depend on the fulfillment of our projections in terms of EBITDA generation and the amount of debt in the next 12 to 18 months.

Our projections consider the continuity in the economic recovery path of the economies in which Grupo Argos participates. However, we identify factors that could impact this dynamic, especially in Latin America, such as strict quarantines as a result of new outbreaks of the virus. In the particular case of Colombia, in addition to possible outbreak events, the economy could be affected by the social crisis evidenced in recent weeks. Although we consider that there are elements that mitigate the unfavorable impact that these events may have on GA's results, we will closely monitor their evolution and the effect this may have on our credit risk opinion and particularly on the assigned outlook.

One of GA's key strengths is the diversification it maintains by business type and geography. Thus, the magnitude of the impact of 2020 was different for each of the businesses and, in the same sense, the speed of recovery to pre-pandemic levels will also be different.

In the case of the cement business, 2020 saw a contrast in terms of sales. In the second quarter, cement and concrete volumes fell 15% and 19%, respectively, as a result of strict quarantines in Latin America and some weather conditions in the United States. The gradual reopening of the economies promoted better revenue dynamics in the second half of the year; thus, the decline in cement volumes was reduced to 9%, and in the case of concrete, the rate of decline remained at the same levels as in the second quarter of the year.

In order to compensate for the lower sales volumes, the company implemented an operational efficiency plan, which contributed to an EBITDA generation close to COP1.6 trillion at the end of 2020, which meant a reduction of 8.4% compared to the previous year. The drop in this indicator is also explained by other specific aspects, such as the sale of plants in 2019, which has an impact on the calculation base. If these effects are eliminated, EBITDA would have grown by 4.5%.

In the next few years, the performance of the cement business would benefit from government policies in terms of housing and infrastructure incentives as measures to reactivate the economies, especially in the United States and Colombia. An additional variable that would boost local production, at least in 2021, is the high cost of freight, which would discourage the imports of construction materials.

The energy business evidenced a defensive position to the adverse conditions of the previous year; as a result of the higher share of Celsia's EBITDA in the distribution business (close to 60%), whose own characteristics translate into stable and predictable flows. The company's EBITDA at the end of 2020 was close to COP1.2 trillion, which represented a marginal drop of 2% compared to the previous year.

Hereafter, Celsia will continue its expansion strategy in the generation business with renewable technologies, through the construction of solar and wind projects. The company will also maintain its participation in the transmission and distribution business, with which it could participate in government initiatives similar to Plan 5 Caribe. Although these projects would represent for 2021 and 2022 investment amounts close to COP1.5 trillion, annual average, the increase in debt would not be in the same proportion, as some of these projects would be developed jointly with other partners.

Odinsa, on the other hand, recorded the greatest impact due to its participation in the airport infrastructure business, reflecting a 26% drop in EBITDA in 2020. In contrast to the performance of the air sector, road concessions were more resilient and at year-end most roads reported traffic levels close to those of 2019. This adaptability also came from each concession's contractual mechanisms to recover losses associated with the lower traffic between March and August 2020 and the suspension of toll collection during March and May 2020.

We project that the good road traffic dynamics evidenced in the second half of 2020 could be impacted by the strike events that have taken place between April and May in Colombia. However, we do not foresee any problems in the concessions to meet all their obligations. Air traffic is expected to fully recover between 2023 and 2024, with a greater dynamism in domestic flights.

One element that we consider positive is Grupo Argos' access to the capital market and the financial sector, through innovative mechanisms that are in line with market demand. Thus, in 2020 the conglomerate carried out the first bond swap and in 2021 Cementos Argos and Grupo Argos contracted loans whose interest rate will be linked to compliance with environmental, social and governance indicators.

**Liquidity**

Grupo Argos' shock plan allowed it to maintain adequate liquidity levels during the situation. This incorporated treasury credits and structural efficiencies, which will be relevant in the generation of operating cash flow, which we project at levels of COP3 trillion, annual average, for the period 2021-2023.

In order to estimate liquidity levels, we projected the sources over uses indicator for the next 12 to 24 months. The annual average indicator of 1.15x evidences the group's adequate capacity to meet all its financial and operating commitments.

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

- Maintenance capex.
- Dividend payments in accordance with Grupo Argos' projections.

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

- The proven access to the capital market and the financial sector, through available quotas for COP2.4 trillion out of a total allocated of COP7.4 trillion.
- The stock dividend payment mechanism, which provides certain flexibility in stress scenarios.

**Opportunities and Threats**

What could lead us to upgrade the rating

BRC identified the following opportunities that could improve the current rating:

- The use of alternative and stable funding sources to leverage the expansion plan without pressuring its debt indicators.
- The achievement of reductions in the Group's consolidated leverage level so that its net debt/EBITDA ratio remains steadily below 3x over the next three years.
- Strengthening the Group's growth in its three strategic pillars.

What may lead us to lower the rating

BRC identified the following aspects of company and/or industry improvement and/or follow-up that may affect the current rating:

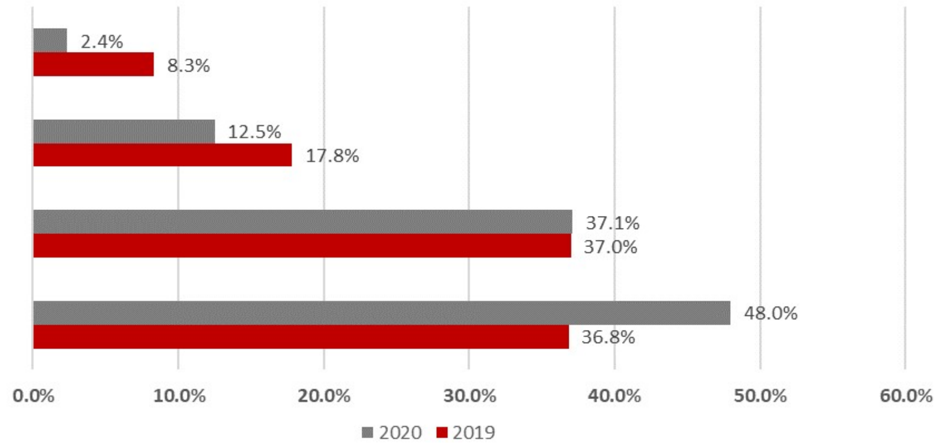
- The increase in consolidated debt so that the net debt/EBITDA ratio exceeds 4x in a sustained manner.
- Delays in the development of infrastructure projects that significantly impact the fulfillment of the revenue and EBITDA projections of the affiliates.
- The impairment of the organization's level of liquidity.
- The slowdown in the US economy that affects the countries of Central America and, therefore, has a negative impact on the operations that the group has in these regions.
- The long-term impacts of the short-term volatility that Colombia is currently facing.

**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 of a real estate fund (Pactia), owns land banks for urban development (Grupo Argos Desarrollo Urbano) and has a strong portfolio of investments in the financial and food sectors.

By the end of 2020, Cementos Argos and Celsia held the largest interest by EBITDA within the Group, figures consistent with those of the previous year. It is important to mention that the results of 2020 are impacted by the performance of airport concessions and a drop in the results of portfolio investments, which would reflect a gradual recovery in the following years.

**Figure 1.**
**Grupo Argos EBITDA Distribution**




Source: Grupo Argos

**Industry Risks**

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

- High capital requirements and energy use.
- Entry barriers by 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.
- Extensive business cycles, which implies long periods of recovery of its investments.
- Exposure to regulatory and normative changes.
- Public policy unit.

The impact that the economic slowdown due to the coronavirus and social factors may have could affect not only the different companies of the Group differently, but also differently in each of the countries in which they operate. The most relevant ratings of countries for the organization are summarized in the following table, as well as the growth projections for 2021 and 2022 made by S&P Global Ratings:

**Table 1. Ratings and GDP Growth Projections in Countries where Grupo Argos Operates**

| Country | Long-Term Foreign Currency Rating by S&P Global Ratings | Outlook | 2021 | 2022 |
|---|---|---|---|---|
| Colombia | BBB- | Negative | 6.0 | 3.5 |
| United States | AA+ | Stable | 6.5 | 3.5 |
| Panama | BBB | Stable | 7.0 | 4.5 |
| Aruba | BBB | Stable | 5.6 | 9.9 |
| Dominican Republic | BB- | Negative | 5.0 | 5.0 |
| Honduras | BB- | Stable | 3.8 | 3.5 |
| Costa Rica | B | Negative | 2.6 | 3.6 |

Source: S&P Global Ratings

*The technical visit for the rating process was carried out with sufficient opportunity by the availability of the rated entity and the delivery of the information was fulfilled in the expected times and in accordance with the requirements of BRC Investor Services S. A. SCV.*

*The financial information included in this report is based on the audited financial statements for the three years (2018-2020).*

*BRC Investor Services S.A. SCV does not perform audit functions, therefore, the management of the entity assumes full responsibility for the integrity and veracity of all the information provided and that has served as the basis for the preparation of this report. On the other hand, the rating agency reviewed the publicly available information and compared it with the information provided by the rated entity/rated issuer.*

*A risk rating issued by BRC Investor Services S.A. – Sociedad Calificadora de Valores – is a technical opinion and at no time is intended to be a recommendation to buy, sell or hold a given investment and/or security, nor does it imply a payment guarantee of the security, but rather an assessment of the probability that the capital thereof and its returns will be paid in a timely manner. The information contained in this publication has been obtained from sources that are presumed to be reliable and accurate; therefore, we assume no responsibility for errors or omissions or for results arising from the use of this information.*

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*To see the definitions of our ratings, please visit www.brc.com.co or click here.*

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*The resumes of the members of the Technical Rating Committee are available on our website www.brc.com.co*