

Research Update:

# Metropolitano de Tenerife S.A. 'A/A-1' Ratings Affirmed; Outlook Stable

October 31, 2022

## Overview

- We think that there is an almost certain likelihood that Metropolitano de Tenerife S.A (Metrotenerife), a government-related entity of the Cabildo de Tenerife (CIT), would receive extraordinary government support if needed, given its critical role and integral link with its owner.
- We do not believe CIT's creditworthiness could be above Spain's; nor do we think that Metrotenerife's creditworthiness could be stronger than that of CIT, from which it receives ongoing support.
- We therefore affirmed our long- and short-term issuer credit ratings on Metrotenerife at 'A/A-1'.
- The stable outlook mirrors that on Spain.

## Rating Action

On Oct. 31, 2022, S&P Global ratings affirmed its 'A/A-1' long- and short-term issuer credit ratings on Spain's Metropolitano de Tenerife S.A. (Metrotenerife). The outlook is stable.

## Rationale

We consider Metrotenerife to be a government-related entity (GRE) of the Cabildo de Tenerife (CIT), a local government in the Autonomous Community of the Canary Islands (A/Stable/--). Metrotenerife is a public transport company that operates the tramlines in the metropolitan areas of Tenerife, and it is fully owned by its local government.

In our opinion, local governments in Spain generally cannot be rated above the sovereign, and in this case, we believe Metrotenerife could not be rated higher than the creditworthiness of its related government, from which it receives ongoing support. Consequently, we cap our ratings on Metrotenerife at the same level as the rating on Spain.

In our opinion, CIT would almost certainly provide timely and sufficient extraordinary support to

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Metrotenerife in the event of financial distress. We base this rating approach on our view of Metrotenerife's:

- Critical role for CIT. Metrotenerife provides public transport services in the metropolitan area of Tenerife and is instrumental to the local government's policy of fostering its use. Public transport is one of the core responsibilities of CIT. In our view, the essential and subsidized nature of Metrotenerife's activities, and CIT's ownership of its infrastructure, make it highly unlikely that a private entity could undertake its responsibilities.
- Integral link with CIT. The local government fully owns Metrotenerife and supervises its strategy and operations. The company executes its investments in close coordination with CIT and operates under an agreement set by both Metrotenerife and CIT in 2003. This stipulates that CIT is responsible for safeguarding the economic and financial balance of Metrotenerife.

As a result of our view of an almost certain likelihood of support, we believe Metrotenerife's credit quality is equivalent to that of its related government, CIT, which in turn is limited by Spain's. In addition, we continue to assess Metrotenerife's stand-alone credit profile (SACP) above our long-term rating, at 'a+'. Metrotenerife has shown resilience to the effects of the COVID-19 pandemic thanks to its lower exposure to tourism and extraordinary support from its government owner. Furthermore, we anticipate Metrotenerife will post strong results in 2022 mainly thanks to the ongoing ridership recovery, and substantial financing cost savings.

Metrotenerife operates in an industry that we consider low risk and offers an essential service in its catchment area, by linking the two largest cities on Tenerife and helping to relieve pressure on the metro area's congested roads. We believe the entity's market position, which we view as very strong, could be reinforced in the medium-to-long term given CIT's mobility strategy to expand Metrotenerife's presence in Tenerife. This could be via the potential expansion of its lines and promoting reduced usage of private car.

However, we believe that the economic fundamentals of Metrotenerife's catchment area are weaker than those of other Spanish peers. We believe that economic indicators on Tenerife are very much in line with the regional level, given that about 43% of the Canary Islands' population live on Tenerife. The province of Santa Cruz de Tenerife has higher unemployment than Spain, at 17.8% versus 12.7% as of September 2022. Its GDP per capita levels of about €17,448 are consistently below the national average (about 74% of Spain's at year-end 2020), according to the latest public available data from the national statistics institute.

Metrotenerife benefits from strong and stable demand for its services, and we believe it will likely reach about 15.5 million riders in 2023, fully recovering to normal pre-pandemic activity levels. In our view, ridership in 2023 could benefit from high fuel prices, which would mean public transport is less costly than private transport.

During 2022, Spain's central government decided to decrease public transport tariffs 50% to support demand for these services amid high inflation. Accordingly, Metrotenerife has reduced the price of monthly frequent passengers passes 50%, with lost revenue covered by the central government. We expect this measure will be in place until 2023. However, we think tariffs will remain low thereafter with the difference supported by CIT. This shift will lead to a change in the composition of Metrotenerife's revenue, which will become more dependent on government transfers. We expect subsidies to represent about 44% of total fare revenue in 2022, up from a low of 24% in 2013.

We view Metrotenerife's management and governance in the context of its solid standards of operating performance and prudent debt and liquidity management. The company's financial planning is conservative and supported by continuous updates to long-term business projections,

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including conservative assumptions. In 2021, management successfully issued Metrotenerife's first green bond, making it the first entity in the Canary Islands to do so.

In our view, Metrotenerife's refinancing of its long-term debt with the €130 million green bond issuance, strengthened its long-term financial position. Metrotenerife now has higher cash levels, since the previous debt architecture forced it to hold restricted cash, while it will also benefit from large interest savings. Metrotenerife secured 15-year financing at a 1.23% fixed interest rate (versus over 5% previously), taking advantage of extremely favorable market conditions at the time. Moreover, Metrotenerife's previous financing structure stipulated a block on about €5 million-€6 million of liquidity reserves, which are now fully available to the entity.

Given that the new financing is in the form of a bullet bond, Metrotenerife has decided to create a sinking fund that it will endow on an annual basis. Metrotenerife has decided to invest the sinking fund in low-risk assets, such as government bonds or highly rated corporates. The return on such investments will partially cover the entity's interest costs.

The sinking fund will remain freely available to Metrotenerife throughout the 15-year period until the bond is due, with no self-imposed legal restrictions on its use. That said, we understand the entity does not intend to sell it except in case of acute need.

Given the new structure of Metrotenerife's debt, which is composed of nonamortization debt with a single bullet repayment in 2036, EBITDA to debt service coverage ratios will materially improve. However, we believe this coverage to be somewhat overstated versus that of peers with fully amortizing debt structures. In any case, inclusion of assumed principal payments to the sinking fund as synthetic amortization does not result in a change in our assessment at this time, since we also expect the ratio to be supported by increasing EBITDA in the coming years. Therefore, we continue to view Metrotenerife's financial performance as strong.

Despite the very high rise in energy prices during 2022 because of the Russian-Ukraine conflict, Metrotenerife's EBITDA won't be negatively affected. This is because it bought futures on energy stocks in the secondary market in 2021 and 2022, limiting the effects of the rise and generating proceeds. We expect Metrotenerife to use part of these proceeds to cover expected higher energy costs in 2023.

Until we have greater certainty on whether Metrotenerife will expand its metro lines in the Canary Islands, we consider no immediate need for additional debt. In turn, we expect Metrotenerife's debt to remain low in an international context, with debt to net revenue below 15x over the next two years.

### Liquidity

Metrotenerife's liquidity is strong and has been enhanced after its refinancing transaction. The refinancing allowed Metrotenerife to free up liquidity held in its debt service reserve account, which on average represented over 55% of total available cash in recent years. We estimate unrestricted cash on hand at comfortably above 400 days in 2022 and available liquidity to debt of about 13x, proving its strong liquidity position.

We consider Metrotenerife to have satisfactory access to external liquidity. The company proved its ability to place a sustainable bond in the markets with ample demand and a very diversified order book (both geographically and in terms of investor type). Although we do not expect Metrotenerife to require additional funding, we expect the entity would have no difficulties tapping bank funding, if needed.

## Outlook

The stable outlook mirrors that on Spain (unsolicited; A/Stable/A-1). This reflects our opinion that local and regional governments and their GREs can only be rated above the sovereign in exceptional circumstances.

## Downside scenario

We could lower our rating on Metrotenerife if we downgrade Spain.

## Upside scenario

We could raise our rating on Metrotenerife if we upgrade Spain.

## Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- Criteria | Governments | General: Global Not-For-Profit Transportation Infrastructure Enterprises: Methodologies And Assumptions, Nov. 2, 2020
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Rating Government-Related Entities: Methodology And Assumptions, March 25, 2015
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 20, 2013
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

## Related Research

- Spain, Sept. 19, 2022
- Metropolitano de Tenerife Outlook Revised To Stable From Negative After Similar Action On Spain, April 1, 2022

## Ratings List

### Ratings Affirmed

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**Metropolitano de Tenerife S.A.**

Issuer Credit Rating A/Stable/A-1

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**Metropolitano de Tenerife S.A.**

Senior Unsecured A

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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](http://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](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](http://www.capitaliq.com). All ratings affected by this rating action can be found on S&P Global Ratings' public website at [www.standardandpoors.com](http://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

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