Tecnocom, Telecomunicaciones y Energía, S.A. and consolidated companies Spain - ICT

BB STABLE
Corporate Rating

Tecnocom is an important player in the Spanish information and communication technology (ICT) market. The group, with the mother company listed on the Spanish Stock Exchange since 1987, offers a broad portfolio of technology and business solutions that covers a wide range of industries in both the public and the private sector. Its regional presence includes Spain, Portugal as well as countries in Latin America, such as Colombia, Mexico, Chile and Peru. Tecnocom's turnover reached €376 million in 2013.

Result

Corporate Rating:	BB
Outlook:	STABLE
Sector:	ICT
Release date:	March 24th, 2014
Monitoring:	yes

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Rating Rationale Summary

Scope Ratings assigned a BB rating to Tecnocom, Telecomunicaciones y Energía, S.A. and consolidated companies (herein after also referred to Tecnocom Group, Tecnocom or group) with a STABLE outlook.

The rating reflects Scope's opinion of Tecnocom's competitive position in its relevant markets, its diversified clients portfolio, the high level of recurring income, the access to financing resources and its high quality management. The rating is, however, constrained by key factors, including the existing industry risk, limited profit generation, its exposure to foreign exchange fluctuations and the group's development stage, considering that Tecnocom still needs to stabilize and consolidate its activities in different markets in Latin America.

In Scope's view, Tecnocom has a diversified business profile. The group's investment strategy has focused on organic growth as well as acquisitions, therefore, although its revenue is mostly generated in Spain (74%), the group's relative share in this market has declined steadily in recent years to the benefit of its activities abroad. Geographic diversification has resulted in a higher percentage of revenues generated in Latin America over the last few years. Geographically, Tecnocom covers 10 countries directly, including Spain, Colombia, Chile, Perù and Mexico but, through a partnership with Getronics, is present in more than 70 countries. Moreover, Scope positively evaluates Tecnocom's competitive position in its relevant markets, not only in terms of diversity of services and products, but also considering the wide range of industries covered both in the private and public sector.

The group is structured around three business lines: Projects and Applications, Application Management and Technology. Tecnocom offers in-house solutions and has focused on improving its position in niche markets and thus establishing long-term business relationships with its clients. Even though many of the contracts are negotiated on a yearly basis due to the high degree of customization of the services provided, Scope considers that Tecnocom has a solid and recurring revenue base (reported to be 70% of total revenues). At the same time, the group´s investment strategy focuses on increasing its Application Management activities, which would provide them with more stable cash flows.

Scope positively assesses Tecnocom's management team, which has proved very effective in integrating the newly acquired companies into the existing business. The group's acquisition strategy was built on two pillars: retaining key staff to preserve know-how and improving processes to stengthen efficiency.

Notwistanding the arguments above, in Scope's view, Tecnocom is still in an early stage of the consolidation process, thus the group needs to prove its strategy to be effective and profitable in the long run. The acceleration in worldwide operations experienced over the last years, and the financing of the investments in Latin America through proceeds originating in Europe, triggered a currency risk exposure which negatively affected net profits in the last year (EUR 1.9m as of December 2013). Approximately 22% of the group's revenues are generated in foreing currencies. Exposure to exchange rate fluctuations may increase if more revenues are generated abroad in the future. Additionally, since the group operates in a highly cyclical sector, the industry risk could potentially impact the stability of its returns over time and limit its earnings generation capacity.

The group has a solid equity ratio (50%) and positive operating cash flows (EUR 21m, as of December 2013). Nevertheless, Tecnocom's net profit was partially offset by the restructuring costs incurred in the last years (EUR 2.8m in 2013, in 2014, an additional EUR 6.5m is expected to be incurred), the financial expenses that created pressure on the cash flow and revenues margin, as well as on the profitability ratios. These margins are below average in a sector that has already suffered from constant margin reductions Short-term liabilities are high (78% of total) considering that the group faces costs related to seasonal cash flows. Financial expenses accounted for EUR 5.8m as of December 2013, and in Scope's opinion, no significant reduction is envisaged.

The stable outlook reflects the rating agency's opinion on the group's future development possibilities. On the one hand, it group might be able to benefit in terms of margins and market share, however, the funding required to finance short-term obligations of Tecnocom could limit net margins and the group´s cash flow generation capacity.

Rating Drivers

Strengths	Weaknesses
Favorable competitive position on its relevant markets, with a strategy oriented towards niche markets	Limited profit generation capacity, particularly affected by restructuring and financial costs
Combining diversification in clients portfolio with long-term relationships	Business sensitivity to economic cycles and risks in the industry
High percentage of recurring revenues	Early stage of the consolidation process
Access to stock market financing	Foreign exchange risk exposure affecting cash flows
High quality management, demonstrated by the successful integration of 10 companies in 5 years	

Financial Indicators

EUR millions	2011	2012	2013
Shareholders' equity	175,9	168,8	169,3
Equity ratio (%)	0,5	0,5	0,5
Total Debt	52,4	61,9	56,2
Net Financial Debt*	38,5	43,7	37,9
Total Assets	342,7	339,2	333,6
Turnover	395,9	383,0	376,0
Operative Income	100,3	92,0	92,4
Gross Margin	25,3%	24,0%	24,6%
ROE	2,7%	-2,1%	0,6%
ROA	1,4%	-1,0%	0,3%
Recurring EBITDA **	23,4	18,7	24,4
EBITDA	20,2	13,9	20,7
EBITDA Margin	5,1%	3,6%	5,5%
EBITDA / Financial Expenses**	4,7	2,4	3,6
NFD / EBITDA	1,6	2,3	1,6
Financial Expenses	-4,3	-5,8	-5,8
Net Profit	4,7	-3,5	1,0
Operating Cash Flow	27,2	16,6	21,3

Source: Tecnocom
* Adjusted to include other quasi liquid assets
** Adjusted by following the definition contained in the current syndicated financing contracts of the group.

The Group

Tecnocom undergone in-depth changes since 2005

Tecnocom is an important player in the Spanish Information and Communication Technology (ICT) market and is listed on the Spanish stock exchange since 1987. Founded in 1967, the group has undergone a profound transformation since 2005, when Tecnocom decided to change its strategy and to focus on the ICT market. Since then, the group has concentrated on growing the business through acquisitions and organic growth, which resulted in a restructuration process and R&D investment that should benefit the group in the future. Strategic partners include Oracle, HP and Microsoft. Furthermore, Tecnocom has a wide geographical coverage with direct presence in 10 countries, including Spain, Portugal, Colombia, Chile, Peru, Mexico and the Dominican Republic. It also has capacity in more than 70 countries through the Global Alliance with Getronics.

Rating Rationale

Sector Perspective

Tecnocom's market can be viewed from two perspectives. On the one hand, the Spanish market, which contributes 74% of the total revenue and, on the other, the Latin American market on which the group has focused its expansion in the last years.

Business sensitivity to the economic cycles and industry risks

In the first case, the sector contraction during the economic crisis considerably affected the group's profits, particulary regarding the reduction of the investment in technological improvements, which differ from current expenses that are less vulnerable to the cycle. Due to the pro-cycliclal behaviour of this industry, it is expected to recover once the Spanish economy begins showing positive growth. However, in the short run, according to the IDC (International Data Corporation) the sector in 2014 will decrease by 0.7% in Spain.

Opportunities vs. strong competition in the Latin American market

The Latin American market enabled the group to keep a stable level of revenues despite the decline in its domestic market. This greater dynamism is reflected in the IDC projections for 2014, which point to a 9.1% growth rate for sectoral investment in the region. The Latin American market has a higher growth potential in relation to developed markets because it has lower technology penetration ratios, with an IT investment of 2% of GPD as annual average. This is lower than the average for developed countries, and thus is a window of opportunity. This is the case for the banking sector and the industry of means of payment, which is currently going through in-depth change, due to the relatively low rate of bank use by the population, and because the growing economies will invest resources to modernize this sector. However, it is worth mentioning that the group is going to face a segmented industry with a high competition from local companies as well as big multinationals.

Business Diversification

In Scope's opinion, the group's business lines and geographic coverage provide adequate revenue diversification. In its evaluation, Scope considered the following criteria: i) the quality and concentration of the client portfolio, ii) geographical diversification and iii) revenue sustainability.

Tecnocom is an IT company with broad experience in comprehensive IT services and high technology platforms. The group develops applications with high replicability, which can be customized to meet the specific requirements of individual customers, and allows its use in enterprises from several sectors.

Most of the Tecnocom's consolidated revenues are derived from the Technology unit (47% in 2013), followed by Projects and Applications (28%) and Application Management (25%). The Technology business line includes the old System and Technology Integration and Infrastructure Management lines, which were merged to unify the product-service cycle. This unit also includes the services that Tecnocom offers through Metrocall, which include the design, supply and installation, operation and maintenance of network providing mobile telephone coverage in the Madrid metro system.

In 2013, revenues declined by 1.8% compared with 2012 (Table 1), mainly due to the lower revenues from Technology (-10.4%). However this reduction was compensated by the higher revenues from the Projects & Applications unit (10.3%).

TABLE 1
Revenues by business lines
EUR millions

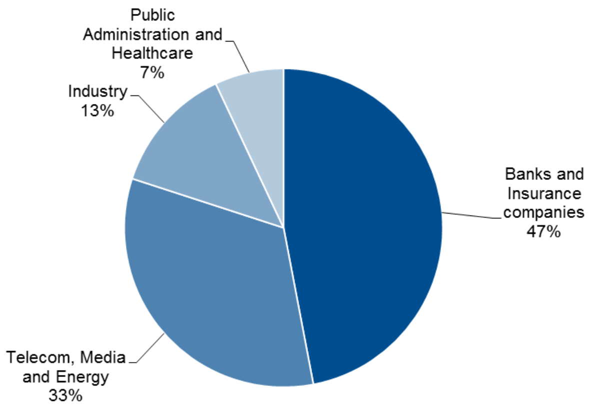
	2011	2012	2013
Projects & Applications	85.4	96.6	106.6
Application Management	91.0	87.9	91.5
Technology	219.5	198.5	177.9
Total Revenues	**395.9**	**383.0**	**376.0**

Source: Tecnocom

Fairly diversified clients portfolio

Due to the broad spectrum of services offered by Tecnocom, its revenues are reasonably diversified in relation to its customer base. Tecnocom had a portfolio of approximately 1600 customers at December 2013, from a wide range of industries, including large banks in Spain such as BBVA, Banco Santander, Grupo Banco Popular, companies from the IBEX 35, and major companies in Latin American countries where Tecnocom operates. The top 10 customers by revenue accounted for 39% of Tecnocom's consolidated annual revenue. This relative concentration of the portfolio has been reduced compared to recent years, and in our opinion, the group is adequately diversified. Chart 1 below illustrates Tecnocom's composition of sales by sector.

CHART 1
Revenues by sector (%), 2013



Source: Tecnocom

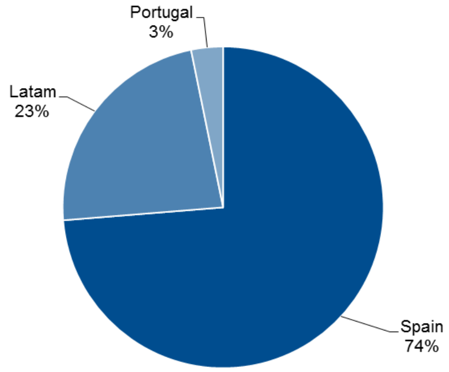
Tecnocom's client portfolio comes mainly from companies in the banking and insurance sector (47%), followed by the telecom, media and energy sectors (32%). The most significant change in the revenue structure corresponds to a reduction in revenues from contracts with the Spanish Public Administration from 12% in 2011 to 8% in 2013. This is the result of the local economic crisis, when the public sector entities were subject to severe budget cuts affecting the number of public tenders and IT consulting services.

With respect to trade receivables, the average accounts receivable collection period is about 58 days. The overdue debt for more than 180 days was 5.8% of the total (1.6% corresponding to the Spanish Public Administration). The group maintains an adequate coverage policy, by provisioning 56% of the trade receivables overdue by more than 180 days (not related to public administration).

Geographic diversification improves due to new contracts with important companies across Latin America

Despite the fact that most of the customers come from Spain, the group has expanded its customer base in recent years through its strategy of diversification and geographic expansion, obtaining strategic contracts in Latin American countries, including the Banco del Estado in Chile, the Ministry of Justice and Human Rights in Peru, Azteca Communications, and the Ministry of Finance both in Colombia, among others. Tecnocom has grown its activities in Latin America, focusing strategically on four countries: Colombia, Chile, Peru and Mexico. The percentage of total revenues from operations outside Spain reached 16% in 2010 and accounted for 26% in 2013. The most important improvement is the highest relative growth observed in Colombia, whose share accounted for approximately 7.9% of the Group revenue in 2012 and about 11.4% in 2013 (Chart 2).

CHART 2
Revenues by geographical area, 2013 (%)



Source: Tecnocom

A high proportion of recurring revenues

Regarding the sustainability of contracts and revenue generation, Tecnocom has established long-term relationships with its clients and has not lost clients in the banking sector despite the crisis. The group's cash flow shows some seasonality because, although 70% of its revenues stem from recurring sources, the group needs to renegotiate some of the contracts annually. Any delays in the processing and approval of these contracts can cause a certain delay in their respective billing and collection. As a result, Tecnocom is periodically exposed to a potential loss of contracts for non-renewal reasons. However, in Scope's view, this risk is mitigated, because the nature of the services provided means that changing the service provider or migratiing the platform can be quite costly.

Management

Management Track Record

Management composed of executives with substantial expertise and a high level of specialization

Tecnocom's management team consists of ten professionals with long-standing experience in the IT sector. Amoung them, the CEO and CFO, who joined the group in 2005 and 2012, respectively. The whole team has an average of 15 years management experience.

Scope considers that Tecnocom's management is well qualified to perform its duties. The quality of the management of the operational functions, processes and tools developed to manage projects and the group's human resources is very high. The management team has specialists in different areas and is sufficiently diversified, a fact that in our opinion reduces key man risk considerably. Another key point is the smooth integration of the nine companies acquired in recent years.

Investment strategy

Conservative investment approach

Tecnocom has a conservative investment strategy. The group only participates in projects with high added value and where it has a strategic partner. It competes in tenders based on quality criteria and seeks to maintain margins at appropriate levels.

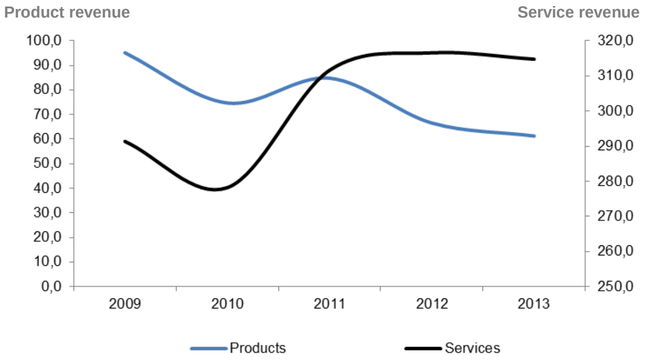
Tecnocom has based its strategy of expansion on organic growth and acquisitions. The group's acquisition strategy was built on two pillars: retaining key staff to preserve know-how and improving processes to stengthen efficiency.

Change in product mix contributes to stable revenues

The strategy also included a shift from a business model focused on products to one focused on services.The most representative example is the payment processing method (Chart 3). This means switching from short-term, higher margins but non-recurring revenue sources to the long-term stability of cash flows from recurrent, lower margin business.

Scope believes that this strategy has been carried out according to the defined plans. Since the 2005 decision to focus its activities on the ICT market, Tecnocom has implemented its strategy consistently, acquiring companies positioned in the different target markets. In our opinion, Tecnocom has implemented its strategy according to their conservative policy, for example by beginning operations gradually, focusing on niche markets in Latin America. In this region, part of its strategy has been to maintain flexibility in the staff composition. Although this represented a high withholding tax cost, it enabled the group to avoid oversizing in countries where it was in the early investment stage. Tecnocom tries to remain flexible and use its resources efficiently to increase fixed costs and labor gradually.

CHART 3
Change in the business mix
EUR million



Source: Tecnocom

Tecnocom needs to consolidated its strategy abroad

However, Tecnocom is still in the early stages in Latin America, especially in regard to some countries like Mexico (Table 2). Scope believes that after an intensive period of investments, which included acquisitions and restructuring, the group needs to consolidate the level of outdoor activities and to prove that it can successfully manage consolidation and growth while also improving profit margins.

TABLE 2
Net Business volume and pre-tax profit, by geographical area
EUR thousands

Country	Net business volume*		Pre-tax profit	
	2012	2013	2012	2013
Spain	319,038	310,410	-394	4,098
Colombia	21,843	30,383	-1,390	618
Portugal	12,242	12,222	166	586
Mexico	3,089	3,300	-217	-940
Peru	15,050	14,272	812	-217
USA	1,005	221	165	-39
Chile	5,725	6,376	-325	22
Dominican Republic	4,675	4,644	881	631
RoW	0	487	-316	-442
Total	**382,667**	**382,315**	**-618**	**4,317**

Source: Tecnocom
* Does not include variations in stock.

Dividend payout policy

The group paid cash dividends whenever the annual financial results and the cash in the balance sheet permitted. However, Tecnocom does not have an established dividend policy and there are no payouts planned for the current year. In the future, the group might consider paying dividends if the balance sheet accounts show a cash surplus, provided that these distributions do not affect its policy of financial prudence and depending on the trade-off between profitability and risk related to the allocation of those resources.

Scope believes that the criteria outlined by Tecnocom regarding its dividend policy is a sign of commitment from the shareholder group and that it demonstrates their interest in the long-term development of the group.

Financial Situation

Table 3 below provides an overview of the financial statements of Tecnocom, Telecommunications and Energy, S.A. for the period between 2009 and 2013.

Stable leverage

The group exhibits a solid equity ratio (50%) and positive generation of operating cash flows (EUR 21m, December 2013), as well as a stable level of leverage (total liabilities to total equity; around 95%) in the considered period, suggesting a stable funding strategy.

Stable revenues despite the crisis

Operating revenues from Tecnocom have fluctuated in recent years, but they have remained near EUR 400m. However, because Tecnocom began expanding during the economic crisis in Spain, the group's growth and profit generation have been limited. The gross margin is around 25%, and the EBITDA margin close to 5.5% (3.6% in 2012). Given the nature of the services offered in this industry, Tecnocom must regularly update and develop technological solutions in order to maintain its competitiveness in the market and to avoid technological obsolescence. The group invested up to EUR 12.5m in 2013.

Limited profit generation, affected by financial expenses and re-structuring costs

Regarding operating profits, the margins and cash flows of Tecnocom have been affected by restructuring costs in recent years (€2.8m in 2013, furthermore an estimated €6.5m is expected in 2014), financial costs (€5.8m) and the fluctuations in Latin American currencies against the euro (€1.9m, as at December 2013). This has curtailed its profitability ratios (0.6% to December 2013), which are below those of other companies in the sector, in an industry where margins have fallen in general.

Restructuring costs comprises mainly personnel restructuring after the merger of the business lines Infrastructure Management and System and Technology Integration. According to the group, 2014 will be the last year in which results will be significantly impacted by this item. The restructuring should improve competitiveness and generate significant savings through synergies. Lastly, Tecnocom estimates that tax expenses, which have weighed on results in Latin America, should decline once it has mostly local staff in these countries.

TABLE 3
Consolidated Financial Statements
EUR millions

	2009	2010	2011	2012	2013
Profit and loss account					
Revenues	**386,5**	**355,5**	**395,9**	**383,0**	**376,0**
Operating margin	102,5	90,3	100,3	92,0	92,4
Recurring EBITDA *	**28,7**	**21,9**	**23,4**	**18,7**	**24,4**
Restructuring costs	-6,6	-4,2	-3,2	-4,4	-2,8
EBITDA	**22,0**	**17,7**	**20,2**	**13,9**	**20,7**
Financial expenses	-4,6	-3,4	-4,3	-5,8	-5,8
Net exchange differences	-1,2	0,0	-0,2	0,5	-1,9
Pre-tax profit	8,8	5,7	6,4	-0,6	4,3
Consolidated Profit	**9,1**	**4,0**	**4,7**	**-3,5**	**1,0**
Balance Sheet					
Current Assets	**176,6**	**163,1**	**168,2**	**164,8**	**158,0**
Trade debtors and other	121,2	99,6	105,4	86,1	81,4
Stocks	27,2	39,2	42,6	48,5	46,5
Cash and other equivalent liquid assets	18,6	11,9	11,9	16,5	13,2
Other (IFT)	2,2	5,7	2,8	2,6	5,6
Other current assets	7,4	6,7	5,4	11,1	11,2
Non-current Assets	**170,8**	**170,4**	**174,5**	**174,4**	**175,6**
Goodwill	88,6	92,5	95,7	95,9	95,9
Intangible and tangible fixed assets	29,8	26,6	28,7	28,1	31,8
Other non-current assets	52,4	51,3	50,1	50,5	48,0
Total Assets	**347,4**	**333,5**	**342,7**	**339,2**	**333,6**
Current Liabilities	**121,9**	**128,1**	**145,9**	**133,9**	**128,6**
Trade creditors and other accounts payable	51,3	44,0	47,9	51,2	45,8
Debt payable to banks	24,4	34,5	38,5	30,0	24,6
Other current liabilities	30,3	34,1	42,1	33,9	41,0
Other	15,9	15,5	17,4	18,8	17,1
Non-current liabilities	**46,7**	**31,2**	**20,9**	**36,6**	**35,7**
Debt payable to banks	33,9	21,9	13,9	31,9	31,6
Other	12,7	9,3	7,0	4,7	4,1
Total liabilities	**168,5**	**159,3**	**166,8**	**170,4**	**164,3**
Total Equity	**178,8**	**174,2**	**175,9**	**168,8**	**169,3**
Net cash flow from operating activities	26,4	14,2	27,2	16,6	21,3
Changes in working capital	6,0	-3,8	7,1	4,9	2,2
Net cash flow from investment activities	-9,7	-7,4	-15,8	-9,9	-12,6
Capex **	-8,3	-7,9	-11,1	-8,6	-12,5
Net cash flow from financing activities	-10,8	-13,5	-11,4	-2,1	-11,5
Dividends	00,	-3,6	-3,6	-3,6	0,0
Net increase/reduction of cash or equivalents	5,9	-6,7	0,1	4,6	-3,3
Gross margin	26,5%	25,4%	25,3%	24,0%	24,6%
EBITDA margin	5,7%	5,0%	5,1%	3,6%	5,5%
Return on Equity	5,1%	2,3%	2,7%	-2,1%	0,6%
Return on Assets	2,6%	1,2%	1,4%	-1,0%	0,3%
Leverage (total liabilities/total equity)	94,2%	91,5%	94,8%	101,0%	97,0%
Net Financial Debt***	38,5	39,8	38,5	43,7	37,9
Financial Borrowings	0,3	0,3	0,3	0,4	0,3
Net Financial Debt / Recurring EBITDA	1,3	1,8	1,6	2,3	1,6
FFO / Financial expenses	5,7	4,2	6,3	2,9	3,7
EBITDA / Financial expenses	4,7	5,2	4,7	2,4	3,6
Liquidity ratio	1,4	1,3	1,2	1,2	1,2

Source: Tecnocom
* Adjusted by following the definition contained in the current syndicated financing contracts of the group.
** Does not consider other acquisitions
*** Adjusted to include other quasi-liquid assets

Liquidity profile

Pressure from refinancing of short-term debt

The group's cash flows show some seasonality due to the conditions under which the contracts are re-negotiated. As a result, although the group has 70% of recurring revenues, there may be some delays in billing and collection. Tecnocom therefore needs to finance these mismatches in the short term.

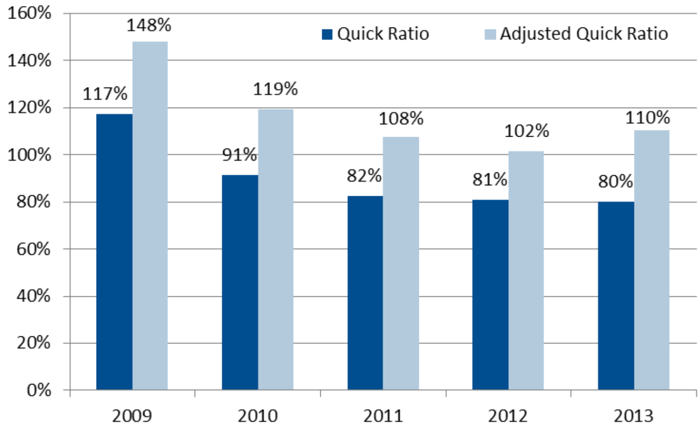
Access to a variety of financing sources

The liquidity analysis in Chart 4 below shows the quick ratio and an adjusted quick ratio for Tecnocom. As at December 2013, the group had a cash level of EUR 13.2m and other cash equivalents and derivatives amounting to approximately EUR 5.6m. As for the composition of current liabilities, 28.3% of the total liabilities correspond to deferred revenue obligations, i.e. advance billing projects to be developed during the course of the year; therefore Scope considers calculating the ratio by adjusting this item total short-term liabilities minus the corresponding amounts of deferred revenue. The quick ratio for 2013 shows that cash, fixed deposits and receivables represented approximately 80% of current liabilities, while the adjusted ratio was 110%. Both ratios reflect the fact that the group has maintained adequate liquidity, although it has fallen over the considered period. Additionally, it is important to mention that Tecnocom has several funding sources, both at bank level (syndicated loan and credit lines), factoring, and through issuing shares on the stock market.

Notwithstanding the limited rates of return, Tecnocom showed relative financial flexibility and generated positive free cash flows, estimated at EUR 7.5m at December 2013. In 2013, the group reduced its cash balance by EUR 3.3m, allocating these resources primarily to the repayment of its debt. Scope believes that the cash flow of the group might be affected by the estimated restructuring costs for 2014, but that it should remain positive (approximately EUR 5.9m).

CHART 4

Tecnocom Quick Ratio



Source: Tecnocom
Quick ratio: cash and equivalent + marketable securities + trade receivables / current liabilities.
Adjusted Quick ratio: cash and equivalents + marketable securities + trade receivables / current liabilities minus deferred income which corresponds to advance billings.

Refinancing / Maturity

Tecnocom operates with a diversified pool of banks that provide short and long-term financing. As at December 2013, long-term funding from financial institutions consists of a syndicated loan for a total of EUR 20.8m and other long-term liabilities of EUR10.8m. The short-term bank borrowing reaches EUR 24.6 Mill representing 43% of total debt.

Of the total short-term debt, 17% corresponds to the syndicated loan and the remaining to loans and other debt factoring, leasing and credits. Of note is that Tecnocom's customers are some of its credit providers, to which it provides essential services. Moreover, credit lines have remained stable during the crisis.

Higher financial expenses between 2010 and 2013

Financial debt is structured in euros, and at variable interest rates that are mostly tied to a 6-month Euribor, plus a spread that is on average between 4.0 % and 5.5%. In 2013, the interest expense remained at similar levels to that recorded in 2012 and was higher than in previous years (EUR 3.4m in 2010 and EUR 4.3m in 2011). The group uses swaps as a hedge mechanism, thus paying fixed and receiving floating interest in order to mitigate interest rate risk. Financial expenses between 2009 and 2013 have increased to EUR 5.8m, and Scope does not expect a significant reduction in the cost of funding.

Tecnocom has guaranteed debt through its companies Tecnocom, Telecomunicaciones y Energía S.A., Metrocall S.A., Tecnocom España Solutions, S.L.U., Softgal, S.A.U, Tecnocom Telefonía y Redes, S.L.U. y Primma Software and S.L.U. Debt contracts with banks set covenants related to debt and the ratio of net financial debt to EBITDA. To date, the group has fulfilled with all these covenants.

According to Tecnocom, part of its financial strategy is to create a new temporary debt profile, leading to longer term debt. The debt has remained at levels of 0.3 and this value is expected to increase in subsequent years. Scope believes that an increase in the group's debt level, without a significant increase in cash flows, could adversely affect its financial situation and considerably affect the cost structure associated.

Foreign exchange currency risk

Tecnocom's revenues and cash flows are exposed to FX risk

The current revenues and cash flow structure with strong international operations have exposed the group to forex risks. As a mitigating mechanism, the group has a policy of balancing the receipts and payments of its assets and liabilities denominated in foreign currency, trying to establish a natural hedge mechanism. However, the diffference betwwen receipts and payments is converted into euros, resulting in a cost of EUR 1.9m at December 2013. According to Scope, this risk could generate volatility in profits and cash flows for Tecnocom, which could be aggravated by the expected increase in revenues from Latin American markets.

Rating Outlook: Stable

Scope assigns a stable outlook to Tecnocom, Telecomunicaciones y Energía, S.A. This outlook is driven primarily by the group's positive prospects for its competitive position and the current business profile, focused on expanding its business in Latin America. The outlook is, however, counterbalanced by the fact that, although the group might benefit in terms of margins and market share, it will also have to consolidate the new operations, control the relative currency exposure of its profits in these countries and face strong market competition. The group also has to refinance short-term debt, a fact that could create pressure on net margins and Tecnocom's ability to generate cash flows in future periods.

Methodology

Scope applied the corporate rating methodology available on its website (www.scoperatings.com). The rating analysis takes into account the proposed amendments to Scope's rating approach announced in October 2013. These amendments aims to reinforce the scoring method that becomes more relevant and include in particular i) a weighting change in financial ratio affecting the results of its scoring model, ii) a finest sectorial breakdown with a weighting of the financial ratios better adapted to each industry, and iii) the inclusion of additional forward-looking analysis based on cash-flow forecasting, among other elements. Information used by Scope in its quantitative model includes Tecnocom's annual accounts from 2010 to 2013.

Important information

Information pursuant to Regulation (EC) No 1060/2009 on credit rating agencies, as amended by Regulations (EU) No. 513/2011 and (EU) No. 462/2013

Responsibility

The party responsible for the dissemination of the financial analysis is Scope Ratings GmbH, Berlin, District Court for Berlin (Charlottenburg) HRB 145472, directors: Thomas Morgenstern, Florian Schoeller.

Rating prepared by

Rosana Pfaffe, Managing Director
Rigel Scheller, Analyst

Rating committee responsible for approval of the rating

Thomas Morgenstern, Chair Rating Committee, Managing Director
Sebastian Zank, Senior Analyst

The rating is prepared for a corporation, which was evaluated for the first time by Scope Ratings GmbH.

Usually a credit rating is accompanied by a rating outlook, which can be Stable, Positive or Negative. The Positive and Negative outlooks would normally refer to a time period of 12-18 months. These outlooks do not necessarily signal that a rating upgrade or downgrade, respectively, will automatically follow. The probability of such a rating outcome, however, would be higher than 50%.

Information on interests and conflicts of interest

The rating was prepared independently by Scope Ratings but for a fee based on a mandate of the rated entity.

Scope has already performed a private preliminary rating for the same rated entity in accordance with Regulation (EC) No 1060/2009 on rating agencies, as amended by Regulations (EU) No 513/2011 and (EU) No 462/2013.

As at the time of the analysis, neither Scope Ratings GmbH nor companies affiliated with it hold any interests in the rated entity or in companies directly or indirectly affiliated to it. Likewise, neither the rated entity nor companies directly or indirectly affiliated with it hold any interests in Scope Ratings GmbH or any companies affiliated to it. Neither the rating agency, the rating analysts who participated in this rating, nor any other persons who participated in the provision of the rating and/or its approval hold, either directly or indirectly, any shares in the rated entity or in third parties affiliated to it. Notwithstanding this, it is permitted for the above-mentioned persons to hold interests through shares in diversified undertakings for collective investment, including managed funds such as pension funds or life insurance companies, pursuant to EU Rating Regulation (EC) No 1060/2009. Neither Scope Ratings nor companies affiliated with it are involved in the brokering or distribution of capital investment products. In principle, there is a possibility that family relationships may exist between the personnel of Scope Ratings and that of the rated entity. However, no persons for whom a conflict of interests could exist due to family relationships or other close relationships will participate in the preparation or approval of a rating.

Key sources of the rating

- ☒ Website of the rated entity/issuer
- ☒ Annual reports/semi-annual reports of the rated entity
- ☒ Annual financial statements
- ☒ Interview with the rated entity
- ☒ Valuation reports, other opinions
- ☒ Detailed information provided on request
- ☒ Press reports / other public information
- ☒ Comisión Nacional del Mercado de Valores - Spain

Scope Ratings considers the quality of the available information on the evaluated group to be satisfactory. Scope ensured as far as possible that the sources are reliable before drawing upon them, but did not verify each item of information specified in the sources independently.

Examination of the rating report by the rated entity prior to publication / Modification of the report after the examination

This report was prepared for informative reasons, to inform the rated entity only.

Methodology

The methodology applicable for the rating of Corporations is available at www.scoperatings.com. The historical default rates of Scope Ratings can be viewed on the central platform (CEREP) of the European Securities and Markets Authority (ESMA): http://cerep.esma.europa.eu/cerep-web/statistics/defaults.xhtml. A comprehensive clarification of Scope's default rating, definitions of rating notations and further information on the analysis components of a rating can be found in the documents on methodologies on the rating agency's website.

Conditions of use / exclusion of liability

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Competent supervisory authority

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