

RatingsDirect®

Research Update:

Ecopetrol 'BBB' Ratings Affirmed Despite Weaker Financial Risk Profile And Liquidity Assessments, Outlook Still Stable

Primary Credit Analyst:

Fabiola Ortiz, Mexico City (52) 55-5081-4449; fabiola.ortiz@standardandpoors.com

Secondary Contact:

Marcela Duenas, Mexico City (52) 55-5081-4437; marcela.duenas@standardandpoors.com

Table Of Contents

Overview

Rating Action

Rationale

Outlook

Ratings Score Snapshot

Related Criteria And Research

Ratings List

Research Update:

Ecopetrol 'BBB' Ratings Affirmed Despite Weaker Financial Risk Profile And Liquidity Assessments, Outlook Still Stable

Overview

- We are revising our financial risk profile assessment on Colombia-based national oil company Ecopetrol to "significant" from "intermediate" because we expect its credit metrics to weaken due to declining oil prices.
- We are also revising our liquidity assessment on Ecopetrol to "adequate" from "strong" based on our expectation that the company will maintain aggressive capital expenditures and dividend distributions despite lower operating cash flow generation.
- We are affirming our ratings on the company, including our 'BBB' long-term corporate credit rating. The 'bbb-' stand-alone credit profile remains unchanged.
- The stable outlook reflects our view that Ecopetrol will continue to play a very important role in the Colombian economy and maintain its very strong links with the government.

Rating Action

On Feb. 26, 2015 Standard & Poor's Ratings Services affirmed its 'BBB' long-term corporate credit rating on Ecopetrol S.A. At the same time, we affirmed our 'BBB' senior unsecured rating on the company. The outlook on the corporate credit rating remains stable.

Rationale

The rating on Ecopetrol is based on its stand-alone credit profile (SACP), which we assess at 'bbb-', and on our view of a "very high" likelihood that the government would provide timely and sufficient extraordinary support to the company in the event of financial distress. As a result, under our government-related entity (GRE) criteria, our ratings on Ecopetrol are one notch above its SACP.

- Ecopetrol's "very important" role in Colombia, given its position as the largest company in the country, its significant presence in the country's oil and gas sector, and its role as the main supplier of oil-derived products in the domestic market; and
- Its "very strong" link with the government, based on its controlling ownership and strategic oversight despite the company's clear corporate governance and independent management team.

Our view of Ecopetrol's "satisfactory" business risk profile reflects the company's leading position in Colombia's oil and gas industry, low production costs, a large reserve base, and strong reserve replacement ratio. The company's production continued to improve during the third quarter of 2014, reaching 755,000 barrels per day due to better operating conditions.

We have revised our financial risk profile assessment on Ecopetrol to "significant" from "intermediate" based on a decline in the company's EBITDA, cash flow, and credit metrics as a result of lower oil prices. Ecopetrol's debt to EBITDA will significantly increase, to about 3.3x during 2015 and 3.0x in 2016 from 1.0x as of Sept. 30, 2014. However, we estimate that as oil prices start to recover in the medium term, this metric will improve to the 2.5x-3.0x range. Our financial risk assessment also reflects Ecopetrol's aggressive capital expenditures (capex) and dividend distributions in the next few years.

Our "satisfactory" business risk profile and "significant" financial risk profile result in a split 'bbb-/bb+' anchor score. We have selected the 'bbb-' anchor based on the company's leading position in Colombia's oil and gas sector, low production costs, strong reserve replacement, and mix of reserves.

Our base-case scenario incorporates the following assumptions during the next two years:

- Approximately 760,000 barrels equivalent per day (mboed) in 2015 and about 800,000 mboed by 2016 as a result of the reversion of Rubiales field;
- A Brent price deck of \$55 per barrel for 2015 and \$65 per barrel for 2016, in line with our Jan. 9, 2015, price assumption;
- Annual investments of about \$7 billion in 2015 and \$7.7 billion in 2016; and
- Dividends payout ratio of about 70%.

These assumptions result in the following credit measures:

- Debt to EBITDA at 3.3x in 2015, and 3.0x in 2016;
- EBITDA margins, of 30%-35%, due to lower oil prices;
- Funds from operations (FFO) to debt of about 20% in 2015 and 22% in 2016; and
- Negative discretionary cash flow to debt of 25%-20% in the next two years.

Liquidity

We now assess Ecopetrol's liquidity as "adequate". We now expect lower operating cash flow generation due to lower oil prices. We expect that sources of liquidity to exceed uses by more than 1.2x in the next two years.

Principal Liquidity Sources:

- Cash balances of about \$2.6 billion as of Dec. 31, 2014
- FFO of about \$3.7 billion in 2015
- Working capital inflow of about \$700 million in 2015

Principal Liquidity Uses:

- Debt maturities of about \$600 million as of Dec. 31, 2014
- Capital spending of \$2 billion annually for 2015, which is higher than the company's maintenance capex
- Dividend payments of about \$2.5 billion

In addition, we view Ecopetrol as having the capacity to withstand high-impact low-probability events based on its sound banking relationships and satisfactory access to capital markets. Additionally, we believe that the company will continue to issue debt in domestic and international markets to increase its liquidity.

Outlook

The stable outlook reflects our view that Ecopetrol will continue to play a very important role in the Colombian economy and maintain its very strong links with the government. Therefore, we believe that the ratings on Ecopetrol would most likely move in tandem with those on the sovereign. On a stand-alone basis, we expect the company's debt leverage will be in line with its current financial risk profile with a debt to EBITDA below 3.5x.

Downside scenario

A downgrade is unlikely at this point, based on our assessment of the "very high" likelihood that the government would provide timely and sufficient extraordinary support to the company, if necessary. Moreover, the company's SACP would have to fall below 'bb' to result in a downgrade, which will occur if the company's debt leverage increases above 5x, leading to a "highly leveraged" financial risk profile.

Upside scenario

Any upgrade would depend on a sovereign upgrade, despite any improvement in the company's SACP because the sovereign foreign currency rating would continue to limit the one on Ecopetrol.

Ratings Score Snapshot

Corporate Credit Rating: BBB/Stable/--

Business risk: Satisfactory

- Country risk: Moderately High
- Industry risk: Intermediate Risk
- Competitive position: Satisfactory

Financial risk: Significant

- Cash flow/Leverage: Significant

Anchor: bbb-

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Adequate (No impact)
- Financial policy: Neutral (no impact)
- Management and governance: Strong (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb-

Sovereign rating: foreign currency: BBB/Stable/A-2; local currency: BBB+/Stable/A-2

Likelihood of government support: Very high, (+1 notches from SACP)

Related Criteria And Research

Related Criteria

- Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Key Credit Factors: For The Oil And Gas Exploration And Production Industry, Dec. 12, 2013
- Corporate Methodology, Nov. 19, 2013
- Corporate Methodology: Ratios and Adjustments, Nov. 19, 2013
- Rating Government-Related Entities: Methodology and Assumptions, Dec. 9, 2010

Related Research

- Standard & Poor's Revises Its Crude Oil And Natural Gas Price Assumptions, Jan. 9, 2015

Ratings List

Ratings Affirmed

Ecopetrol S.A.

Corporate Credit Rating	BBB/Stable/--
Senior Unsecured	BBB

Complete ratings information is available to subscribers of RatingsDirect at www.globalcreditportal.com and at www.spcapitaliq.com. All ratings affected by this rating action can be found on Standard & Poor's public Web site at www.standardandpoors.com. Use the Ratings search box located in the left column.

Copyright © 2015 Standard & Poor's Financial Services LLC, a part of McGraw Hill Financial. All rights reserved.

No content (including ratings, credit-related analyses and data, valuations, model, software or other application or output therefrom) or any part thereof (Content) may be modified, reverse engineered, reproduced or distributed in any form by any means, or stored in a database or retrieval system, without the prior written permission of Standard & Poor's Financial Services LLC or its affiliates (collectively, S&P). The Content shall not be used for any unlawful or unauthorized purposes. S&P and any third-party providers, as well as their directors, officers, shareholders, employees or agents (collectively S&P Parties) do not guarantee the accuracy, completeness, timeliness or availability of the Content. S&P Parties are not responsible for any errors or omissions (negligent or otherwise), regardless of the cause, for the results obtained from the use of the Content, or for the security or maintenance of any data input by the user. The Content is provided on an "as is" basis. S&P PARTIES DISCLAIM ANY AND ALL EXPRESS OR IMPLIED WARRANTIES, INCLUDING, BUT NOT LIMITED TO, ANY WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE OR USE, FREEDOM FROM BUGS, SOFTWARE ERRORS OR DEFECTS, THAT THE CONTENT'S FUNCTIONING WILL BE UNINTERRUPTED, OR THAT THE CONTENT WILL OPERATE WITH ANY SOFTWARE OR HARDWARE CONFIGURATION. In no event shall S&P Parties be liable to any party for any direct, indirect, incidental, exemplary, compensatory, punitive, special or consequential damages, costs, expenses, legal fees, or losses (including, without limitation, lost income or lost profits and opportunity costs or losses caused by negligence) in connection with any use of the Content even if advised of the possibility of such damages.

Credit-related and other analyses, including ratings, and statements in the Content are statements of opinion as of the date they are expressed and not statements of fact. S&P's opinions, analyses, and rating acknowledgment decisions (described below) are not recommendations to purchase, hold, or sell any securities or to make any investment decisions, and do not address the suitability of any security. S&P assumes no obligation to update the Content following publication in any form or format. The Content should not be relied on and is not a substitute for the skill, judgment and experience of the user, its management, employees, advisors and/or clients when making investment and other business decisions. S&P does not act as a fiduciary or an investment advisor except where registered as such. While S&P has obtained information from sources it believes to be reliable, S&P does not perform an audit and undertakes no duty of due diligence or independent verification of any information it receives.

To the extent that regulatory authorities allow a rating agency to acknowledge in one jurisdiction a rating issued in another jurisdiction for certain regulatory purposes, S&P reserves the right to assign, withdraw, or suspend such acknowledgement at any time and in its sole discretion. S&P Parties disclaim any duty whatsoever arising out of the assignment, withdrawal, or suspension of an acknowledgement as well as any liability for any damage alleged to have been suffered on account thereof.

S&P keeps certain activities of its business units separate from each other in order to preserve the independence and objectivity of their respective activities. As a result, certain business units of S&P may have information that is not available to other S&P business units. S&P has established policies and procedures to maintain the confidentiality of certain nonpublic information received in connection with each analytical process.

S&P may receive compensation for its ratings and certain analyses, normally from issuers or underwriters of securities or from obligors. S&P reserves the right to disseminate its opinions and analyses. S&P's public ratings and analyses are made available on its Web sites, www.standardandpoors.com (free of charge), and www.ratingsdirect.com and www.globalcreditportal.com (subscription) and www.spcapitaliq.com (subscription) and may be distributed through other means, including via S&P publications and third-party redistributors. Additional information about our ratings fees is available at www.standardandpoors.com/usratingsfees.