

**Rating Action: Moody's upgrades Embratel to Baa2**

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**Global Credit Research - 26 Apr 2010**

Sao Paulo, April 26, 2010 -- Moody's Investors Service has upgraded Empresa Brasileira de Telecomunicações S.A. ("Embratel") senior unsecured issuer ratings to Baa2 from Baa3 on the global scale and to Aaa.br from Aa1.br on the Brazilian national scale, thus concluding the review process initiated on January 15, 2010. The ratings outlook is stable.

The upgrade reflects primarily the company's improved business profile with increased revenue diversification and its consistently strong debt protection metrics. Also, we believe that the recent ownership restructuring that turned Embratel an indirect subsidiary of América Móvil (rated A2, outlook stable) is beneficial as Embratel could benefit from América Móvil's strong cash generation, if needed.

Supported by the strong performance in local telephony and data transmission, Embratel reported 8.4% increase in consolidated net revenues in 2009 reflecting the company's successful strategy to diversify its operations from the shrinking long distance business. Also, management focus on cost control has translated into EBITDA margin (as defined by Moody's) improving further to 27.7% in 2009 (26.5% in 2008) despite an increasingly competitive environment. Embratel's financial discipline is evidenced by the lack of dividends distribution in 2009 and use of improved free cash flow to reduce indebtedness. Leverage as measured by Total Debt to EBITDA dropped to 0.9x (1.4x in 2008), while liquidity improved based on cash balance of BRL 1.1 billion covering 1.3x short term debt.

In our view, relevant additional synergy gains from the organizational restructuring are not expected since Embratel's operation has been integrated with the group's strategy for the region.

Embratel's Baa2 rating reflects its strong brand equity, especially in the corporate segment, and its position as Brazil's largest data transmission and long distance carrier. Although the company faces significant competitive challenges in its relevant long-distance business segment, it has managed to gradually reduce its reliance on that business segment by growing the data transmission and local services, in addition to launching a DTH video service in December 2008. The Baa2 rating also factors our view of Embratel's key strategic importance to América Móvil as the main conduit for its growth strategy in Brazil. The rating is constrained by the large amount of off-balance sheet tax and regulatory contingencies and by uncertainties arising from the changing regulatory framework, although we note that so far the regulation has been supportive of adequate returns to the industry players.

The stable outlook is based on our expectations that Embratel will continue to focus on revenue diversification away from the declining long distance business, while maintaining good financial discipline and strict cost control resulting in further EBITDA margin improvement. We also expect that Embratel will be able to maintain adequate liquidity through a combination of free cash flow generation (excluding capex with committed funding), cash balances and timely refinancing.

Embratel's ratings and outlook could experience upward pressure if the company continues to diversify its revenues, so that revenues from long-distance are less than 35% while simultaneously increasing EBITDA margin (as defined by Moody's) to above 30% and maintaining Debt / EBITDA below 1.5x and Free Cash Flow to Debt in the low teen range.

The rating or outlook could come under downward pressure if Embratel experiences significant market share erosion due to increased competition or revenues and margins decline on a sustainable basis. Quantitatively, the ratings could be downgraded if EBITDA margins fall below 25% or if Total Debt rises above 2.5x EBITDA.

The last rating action on Embratel was on January 15, 2010, when Moody's placed Embratel's ratings on review for possible upgrade.

The principal methodology used in rating Embratel was Moody's Global Telecommunications Industry rating methodology (December 2007), which can be found at [www.moodys.com](http://www.moodys.com) in the Rating Methodologies sub-directory under the Research & Ratings tab. Other methodologies and factors that may have been considered in the process of rating this issuer can also be found in the Rating Methodologies sub-directory on Moody's website.

Headquartered in Rio de Janeiro, Brazil, Empresa Brasileira de Telecomunicações S.A. is the incumbent long-distance service provider in Brazil and offers a wide array of advanced communications services over its own

network. In 2009, Embratel reported consolidated net revenues of BRL 10.6 billion (USD 5.3 billion converted by the average exchange rate).

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