

Q3 2018 Earnings Call

Company Participants

- Andrea Fernandes, Investor Relation Manager
- Marcello Guidotti, Chief Financial, IR Officer & HR Management and Member of Executive Board
- Unidentified Speaker, Unknown

Other Participants

- Alexandre Pfrimer Falcao, SVP
- Renato Ramos de Almeida Hallgren, Banco de Investimento S.A., Research Division
- Ricardo L. Alves, Equity Analyst
- Stephen Trent, Director
- Thiago Audi Casseb, Research Analyst
- Victor Mizusaki, Research Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Welcome to EcoRodovias' Third Quarter of 2018 Earnings Conference Call. With us here today are Mr. Marcello Guidotti, CFO and IRO; Ms. Andrea Fernandes, IR Officer; and executives of the company. This presentation is being recorded. (Operator Instructions)

The audio and the slides of this conference call are being broadcasted simultaneously at www.ecorodovias.com.br/ir, where you will find the presentation for download from the webcast platform in the Investor Relations section.

Before proceeding, we would like to clarify that the forward-looking statements that may be made during this conference call relating to EcoRodovias' business prospects, projections and operational and financial targets are based on the management's beliefs and assumptions as well as on currently available information. They involve risks, uncertainties and assumptions as they refer to future events and hence depend on circumstances that may or may not occur. Investors should understand that general economic conditions, industry conditions and other operating factors may affect the future performance of EcoRodovias and lead to results that differ materially from those expressed in such forward-looking statements.

I will now turn the floor over to Mrs. Andrea Fernandes, who will discuss the Third Quarter of 2018's results. Ms. Andrea, you may proceed.

Andrea Fernandes {BIO 21294199 <GO>}

Good morning. Welcome to Grupo EcoRodovias conference call regarding the Third Quarter of 2018's results. We thank you for your interest and your participation. Before we begin the presentation about the results, we would like to mention some important events.

In July, we concluded the issue of debentures in the amount of BRL 350 million by EcoRodovias Concessões e Serviços with a term of seven years. In August, we concluded the issue of 2-year debentures in the amount of BRL 225 million for ECO135. In this quarter, the company's board approved the payment of dividends in the amount of BRL 194 million, pertaining to 50% of the results until the month of September 2018 and the remaining dividends from 2017.

Regarding the conclusion of the acquisition of MGO, the company is waiting for the ANTT's approval for the transfer of concession. As for the North -- Rodoanel Norte, we realize that the works are delayed. And we are waiting for a position by the government of São Paulo regarding the conclusion of the work and finish of the contract. As for ECO135, the existing system has already been transferred to the concessionaire. And it is expected to start collection in the Second Quarter of 2019.

The results of the Third Quarter of 2018 were impacted by the beginning of toll exemption for suspended axles at Ecovia Caminho do Mar, Ecocataratas, Ecovias dos Imigrantes and Ecopistas. The toll exemption for suspended axles will be addressed in a contractual rebalancing.

We can see on Slide two that the consolidated traffic of equivalent paying vehicles in the Third Quarter of 2018 went down 2.2%. Excluding the toll exemption for suspended axles, the comparable consolidated traffic posted an increase of 0.5% in the quarter and of 1.7% in the first nine months of 2018. It's important to note that the consolidated traffic presented a reduction of 1.3% in July, 1% in August and 4.1% in September. Excluding toll exemption for suspended axles, consolidated traffic was up 1.4% in July, 1.8% in August and down 1.6% in September.

Comparable traffic of heavy vehicles presented an increase at Ecopistas and ECO101 due to the recovery of industrial production and at Ecocataratas and Ecosul due to higher flow of grain exports.

In addition, the traffic of light vehicles was affected by a decrease in the flow of tourists due to the unfavorable weather conditions in the majority of our concessions. Ecopistas made up in part for the decrease in traffic of the other concessions, due to the increase in the regional trade and an increase of tourist flow in the 9th of July holiday.

As for the group's consolidated performance on Slide 3, the pro forma net revenue amounted to BRL 630 million in the quarter. The highway concessions net revenue was BRL 595 million in the Third Quarter due to the reduction in traffic impacted by the

beginning of the toll exemption for suspended axles. In the 9 -- first nine months of 2018, the concessions net revenue was also affected by the truckers' strike.

Moving on to Slide 4. Consolidated cash cost for the quarter amounted to BRL 184 million, an increase of 1.6% in the quarter, excluding the cost of operational startup of ECO135 in the amount of BRL 4.4 million. It's worth noting that the comparable cash costs of highway concessions, the most relevant segment in the group, presented an increase of 0.6% compared to the Third Quarter of 2017, below the inflation of 4.5% in this period, a result of the continuous search for operational efficiency that we carry out over the last years.

Pro forma EBITDA amounted to BRL 442 million with the margin of 70%. In spite of the impact of the truckers' strike and the exemption of suspended axles, the majority of concessions presented growth of EBITDA in the first nine months of 2018, as you can see on Slide five and 6 with special notice to the 9% increase at Ecopistas, 8% at Ecosul, 12% at ECO101 and 7% increase in the EBITDA of Ecoponte.

On Slide 7, we see the evolution of the comparable net income in the amount of BRL 219 million, a 24% reduction compared to the same period of the last year, negatively impacted by the financial results due to the increase on IPCA and by the EBITDA due to the decrease in traffic.

Now about the investments on Slide 8. CapEx in this quarter was BRL 219 million. The estimated CapEx for 2018 is approximately BRL 819 million. But we maintain the company's commitment to invest according to the contracts and the business needs, noting the beginning of work, the connection of Ponte Rio-Niterói³ to the Red Line and to the Port Avenue at Ecoponte, the beginning of works and the amendment at the Ecovias dos Imigrantes, initial works at ECO135 and the continuation of application works at ECO101.

Moving on to Slide 9, we closed September of 2018 with cash of BRL 2.9 billion and loan/debt profile strengthening our financial soundness. The indicator net debt over comparable pro forma EBITDA was 2.57x. These numbers enable us to implement the commitments in -- of investing in the assets recently acquired as well as evaluating future privatization programs.

Debt by index was 53% in CDI and 39% in IPCA. And the average debt cost was of 8.28% in September 2018.

We would like to conclude by highlighting that we remain focused in the authority of contractual amendments and participation in federal and state auctions. Yesterday, we turned in the proposal for the auction of the Rodovia de Integração do Sul and its results will be released tomorrow. The recent acquisitions and the delivery of the proposal for RIS demonstrate our commitment to our growth strategy, aiming towards extending the duration of our concession portfolio that currently stands at 17 years and three months. It's worth noting that the investment opportunities are always analyzed considering the capital discipline and are considered according to our financial capacity and the return for each project.

The company informs that the independent committee continues developing their investigation works with an expanded scope after the meeting of the board of administration in October 24 due to the second phase of the integration operation. And the results will be reported to the board of administration as soon as the process is concluded.

With that, we end our presentation. And we would like to go to the questions-and-answers session.

Operator, we're ready for the questions. Thank you.

Questions And Answers

Operator

(Operator Instructions) Thiago Casseb from Credit Suisse.

Q - Thiago Audi Casseb {BIO 20503269 <GO>}

My question is about the RIS auction if you can give us the details of the opportunities that you see in this asset in terms of cost reductions and CapEx. If you expect a traffic curve above the cover -- auction and the assets.

A - Unidentified Speaker

Thiago, thank you for your question. We turned in our proposal yesterday, tomorrow it's going to be open. So (wage) expected is above 90% -- 10% in the project. Our proposal was good. And we will wait for tomorrow. I believe that tomorrow we will have a position. And we'll be able to talk in more detail.

Operator

Filipe Pereira, Morgan Stanley.

Q - Ricardo L. Alves {BIO 16840901 <GO>}

This is actually Ricardo Alves. Two questions. First, about the highway operations considering the decrease in traffic due to the suspended axle, the recurrent margin except from ECO135 was close to 75%. I wanted to know in normal traffic conditions, what can we work on for the future now considering 2019. What can we work on as a recurrent margin for highways? And my second question, very specific. The small decrease that we saw in traffic in September. If you can give me a little bit more detail, we understand the effect of comparison bases. But if you can put more color. And if you can tell us a little bit about how October has been, just for us to get a better understanding of what we can expect for the Fourth Quarter.

A - Marcello Guidotti {BIO 16618352 <GO>}

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As for traffic, this year will be impacted by the truckers' strike and the beginning of the toll exemption for suspended axle. And we are affected by the weather conditions. The weather was mild in September. Cold weather in the holidays affected the traffic at EcoRodovias. And we expected traffic to -- and we are at around 1.5% positive, collecting the effect of the suspended axle. For 2019, I think we can be optimistic. We will have the comparison base adjusted as of May. We shall have the exact axles from 2018 and 2019. There won't be a new strike. And we understand that the GDP has been recovering -- will be recovering faster than it did this year. We believe we will continue to grow at around 1.5%. And we can remain optimistic for 2019. As for October, it continued negative, especially -- or the comparison base from 2017, we can't forget that 2017 was a very good year, especially in the month of October. October 2017, we had a growth of 7.2% compared to 2016. So we are now at about 1% down. So we need to consider the comparison base. But October's -- I think, with the strike and all these effects have not been fully absorbed by the economy. So it has an effect in the market. But now we are going to start with a season of holidays and summer. And we will enter 2019 optimistic.

Q - Ricardo L. Alves {BIO 16840901 <GO>}

I don't know if you could, I think you were talking about the traffic but could you talk a little bit more about the profitability on margin that we can expect for highways next year. Do you think with these levels even with the decrease in traffic in the Third Quarter, we would maintain the current level excluding ECO135?

A - Marcello Guidotti {BIO 16618352 <GO>}

Yes, I think we can work with the margin of the quarter and the nine months in terms of revenue. The fourth is usually the best quarter because -- though the Third Quarter is one of the best. And we have the cost, I believe the concessions are controlled, although there've been some additional cost about consultancy and legal advisory. But I would say that they shall not have a significant impact on margin. So we could work with the same margins that we are posting now in the Third Quarter and in the nine months.

Operator

Victor Mizusaki, Bradesco BBI.

Q - Victor Mizusaki {BIO 4087162 <GO>}

I have two questions. First, regarding the rebalancing processes, especially for Ecopistas BRL 284 million with a favorable result for the company so far. What can we expect from this rebalancing? Will it be on a medium term or can you give us an estimation of how many years we can expect for this concession? And as for Paran i and the suspended axle. In this specific case, should we expect a rebalancing on toll increase -- toll tariff increase rather than extension of the term? And on Rodoanel Norte, when do you expect to sign the contract? And is there a deadline considering the delays by the government of S o Paulo?

A - Unidentified Speaker

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Victor, about Ecopistas rebalancing, we're negotiating with the grantor. And the rebalancing that we had in the extension of Carvalho Pinto, we are negotiating the rebalancing probably with an extension of the term. We haven't closed the numbers and values. But the negotiation's moving along very well. So we will be able to get the balancing required for EcoRodovias. As to the suspended axle exemption in Paraná, I believe the chance for EcoRodovias -- Ecocataratas will come on tariff increase, the 2 concessions to balance the investment. And the concession term is also -- is something -- these are federal highways. So I will say that we are working in tariff increases until the end of the concession to balance the level of the suspended axle. And finally, we are clear that the works are delayed. There is a new government taking office now. So I think we will get greater visibility in the beginning of the year. But I will say that throughout 2019, closer to the end of 2019, we will have a definition considering the information that we have about the works.

Operator

Alexandre Falcao, HSBC.

Q - Alexandre Pfrimer Falcao {BIO 5515455 <GO>}

My question is about future projects. There were a lot of candidates that have been elected for state governments that are important to you and in the federal level. And they've been talking about privatizations. And I would like to understand if you have any type of pipeline or estimate, considering that you win RIS, for example. How much balance do you think you have to enter these new projects? And how would you fund new projects in case there is leverage for it?

A - Unidentified Speaker

Alexandre, thank you for your question. About the projects, at the federal level, what we have in the pipeline is 364/365 BR on Santa Catarina in the state of São Paulo. The section of EcoRodovias that may go to auction and the federal government, of course, has the clear pipeline, which will probably be maintained and increased in the new year. The state plans are less defined but we already participated in Minas Gerais, São Paulo. There are many states becoming structured, Rio Grande do Sul, for example. But there is -- we have less visibility of the federal government's plans. But I would say that the pipeline both in the state levels and the federal level will be important in the coming years. We're monitoring very closely our capacities and the flows, as I just said, we are doing now. We'll feel the delay even negotiating with the grantor. But that led to a delay in the payment for MGO, we're waiting for approval. We're monitoring our capacity. And we will certainly have to act in the sense of having the ability for the coming years to be able to take advantage of this portfolio.

Q - Alexandre Pfrimer Falcao {BIO 5515455 <GO>}

And in terms of increase or the growth of portfolio, how is the possibilities?

A - Unidentified Speaker

Alexandre, we did not understand.

Q - Alexandre Pfrimer Falcao {BIO 5515455 <GO>}

Between a dilution or equity offer to be able to participate in all the auctions that you preserve participation and not participate on auctions, how do you think the controllers are thinking?

A - Unidentified Speaker

Alexandre, in 2018 and '17 have been participating in auctions, secondary case, we closed the contract or highways of interest. But we need to gain efficiency, needs to generate cash. But there's also cost. I think that we'll have the discussions about this but the alignment for '18 is what EcoRodovias has been doing. Yesterday, we just submitted the proposal for RIS. So that's what we have now with the shareholders and the strategy for EcoRodovias.

Operator

Renato Hallgren, Banco do Brasil.

Q - Renato Ramos de Almeida Hallgren {BIO 17989415 <GO>}

My question is about the average tariff at ECO101, there was a 4.9% reduction. And the (NTP) reduction was of 7.2%, if I'm not mistaken. I'd like you to remind me if there has been other reductions in 2018? If this 4.9% was the remaining? Or if there will be more reductions in the next quarters? And how do you see the tariff adjustments for ECO101 for 2019?

A - Unidentified Speaker

In 2018, that was due to the contract at ECO101 being positive with inflation. There is a mechanism for rebalancing of the contract for the delays that -- irrespective of the responsibility, the delay is corrected by factor D. ECO101 is accelerating investment program. Probably in '19, we will have an effect of this factor. We don't know the exact value. But the factor D will be corrected and the cash flow of the project with delays in investments. And 12 months later, the investment will be integrally concluded. So it's part of the projects dynamic. It's important that ECO101 has important document and does have priority for the next months for ECO101.

Operator

Stephen Trent, Citigroup.

Q - Stephen Trent {BIO 5581382 <GO>}

Most of my have been answered. But just a follow-up to Falcao's question. When we think about the competition that you are facing on tomorrow's auction, 5 somewhat parties submitted bids. I think in the São Paulo auctions last year for example it was just EcoRodovias and one other party. So my question is how are you guys thinking about the competition risk going forward? Do you think that we should see some elevated level of competition for upcoming auctions versus what had been the case over the last 1.5 years?

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A - Unidentified Speaker

Thank you, Steve. And Steve asked about EcoRodovias' opinion about the level of competitiveness in the next auctions, considering that in tomorrow's RIS proposal there is already 5 players. And in the past auctions, it was always between 2 and 3. The answer that it is certainly to be expected an increase in the competition entering. In the moment where we're recovering growth with interests under control and investments expected for infrastructure, it's the ideal process for other players to enter. On the other hand, with the contracts that we have in São Paulo, for example, they're very well designed, they're complex contracts, difficult with obligations. So these are 30-year contracts with a high CapEx volume, that require qualification. And I think we can expect more competition but I believe that it's qualified competition. It's an environment that we like because we understand and see ourselves as efficient, prepared operators. And I think this is the type of competitiveness that we desire. And it will proper -- probably be what we will see in upcoming months in Brazil. On the other hand, there is one more player for us to be able to make our best proposal.

Operator

Ladies and gentlemen, we'll now close the question-and-answer session. And I will turn over to Ms. Andrea Fernandes for her final remarks. Please, Ms. Andrea.

A - Andrea Fernandes {BIO 21294199 <GO>}

I would like to thank you all for your participation. If you have any further doubts, myself and the IR team are available to answer them, thank you. Have a great day.

Operator

EcoRodovias' conference call is now closed. Thank you very much for your participation. Have a very good day.

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