

Y 2018 Earnings Call

Company Participants

- Marcelo Habibe, 'Chief Financial Officer'
- Pedro Zinner, 'Chief Executive Officer and Investor Relations Officer'
- Unidentified Speaker, ''

Presentation

Operator

Good morning and thank you for standing by. Welcome to the conference call of ENEVA to release the Results of the Fourth Quarter of 2018. Today, here with us, we have Mr. Pedro Zinner, CEO and CFO, and Ms. Flavia Heller, Investor Relations Manager. This conference call is being recorded and all participants will be connected in listen only mode during the company's presentation.

After it, we're going to start the questions and answers session when further instructions will be provided. (Operator Instructions). This conference call is also being simultaneously transmitted through a webcast at the address, ri.eneva.com.

br, and also at the platform MZiQ, where a slide presentation is available which you may control. A replay of this conference call will be available right it ends. We remind participants of the webcast that you may register in advance at the webcast to ask questions that will be answered during the Q&A session. Before continuing we would like to clarify that statements made during this conference call relative to ENEVA's business prospects, operational and financial projections and goals, are beliefs and assumptions of the company and are based on information currently available.

Forward looking statements are not guarantee of performance. They involve risks, uncertainties and assumptions because they refer to future events and therefore depend on circumstances that may or may not occur. Investors should understand that general economic conditions, industry conditions, and other operational factors, may affect the future performance of ENEVA, and may lead to results that will be materially different from those expressed in such forward-looking statements. Now, we would like to turn the conference over to Mr. Pedro Zinner, who is going to start the presentation.

Mr. Zinner, please, you may start.

Pedro Zinner {BIO 17260844 <GO>}

Thank you all very much. Good morning to everyone, and thank you very much for attending ENEVA's conference call for the fourth quarter of 2018. And before beginning, I

would like to take the opportunity to welcome Marcelo Habibe, who has joined the company as CFO earlier this year, who is going to speak to you.

Also, before we start, I would like you to pay attention to our disclaimer on slide number 2 of our presentation. Going on slide number 3, ENEVA has had an outstanding performance in 2018, not just financially speaking, but also in operational terms with the consolidation of the R to Wire. So we have delivered value to our shareholders and we have overcome our challenges in 2018. In terms of exploration and production of gas, we have increased our two key reserves by 4 bcms, with a reserve replacement index that was 286%, above our initial target.

For the first year in history, coal operations operated at a profit. As part of our asset integrity program, we have optimized the variable costs of our coal mines, and we have reached our objective of reaching variable margins that are interesting in terms of dispatch. We have reached significant marks of growth. We have completed the acquisition of Azulao field.

We have opened a new opportunity for growth and consolidation of our R2W. We were successful in our auction Y-6 with Parnaiba V with additional installed capacity and 326 -- 36 [ph] megawatts marketed, in the regulated market. Our objective of advancing with the company's restructuring thereby eliminating inefficiencies and maximizing our tax opportunities, and opening even more room to make use of the opportunities, was also reached. We have successfully completed the debt settlement plan with the funds that we raised in our Re-IPO in 2017, which also makes it possible for us to complete the restructuring of gas segment. When we access the capital market in 2017 through our Re-IPO, we had a short history of accomplishments, many challenges ahead of us.

But we were sure that the potential to create value was really significant. Not much longer than a year later, we have demonstrated concrete results that overcome by far the commitments that we assumed with those who invested in our company. Now moving to the next slide, you will see the highlights of the fourth quarter of 2018. On the fourth quarter of 2018, EBITDA -- adjusted EBITDA rather, in spite of low dispatch in a period, reached BRL311 million, driven by expansion of variable margins in coal generation.

With the early rainy season in Q4 '18, average dispatch was 38%, against 90% that we saw in Q4 '17. As a consequence of the drop in gas sales, the EBITDA of Parnaiba Complex has had a reduction of 44% as compared to Q4 '17. In terms of coal generation, we saw the opposite. In Itaqui, the margin, the variable margin went from BRL26 per megawatt hour in Q4 '17 to 1 -- of minus BRL26 to BRL1 per megawatt hour in Q4 '18.

In Pecem, the margin evolved to BRL31 per megawatt hour. In this manner, the EBITDA in Q4 '18 has reached BRL118 million with a growth of 61% as compared to Q4 '17. The good results also have reflected in our operational cash flow that totaled BRL629 million in the quarter. The company closed the year with a consolidated cash of BRL1.5 billion and 2.6 net debt over EBITDA. We should also highlight the evolution in our volume of reserves.

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As I said before, we have attained a reserve replacement index of 286%, closing the year with 21.4 bcm in terms of remaining reserves and the Azulao field that we acquired earlier that year, we also -- we had 3.6 bcm. Lastly, we completed in December the restructuring of natural gas segment, which led to a more efficient cash management, also made it possible for us to start compensating the tax losses in the holding. After this short summary, I would like to turn the conference over to talk about our operating performance.

Unidentified Speaker

Good morning, everyone.

Now moving to slide number 5, our operating performance. On the bar chart, on the left hand side, you can see the average net power generation, which -- where you can see the dispatch dropped to 42% because of reduction in net generation of 57%. In spite of that, in terms of availability of the power plants, both coal and gas plants increased considering that we had a 4% increase for gas plants and 3% increase for coal plants. We should also highlight that Pecem II dispatched to Operational Reserve Recomposition, which led to 4.2 weeks of dispatch with an average CVU of 126% in the CVU of the power plants.

These numbers are reflected in the variable margin for the power plants in Q4. Now moving to slide number 6, talking about operational performance, you can see the position of reserves of the company. (Inaudible) the fourth quarter of last year, reserves were 18.8 billion cubic meters. We have adding over 2018, more 4 billion of cubic meters, and this resulted in remaining reserves of 21.4 billion cubic meters.

Gas production over the last two [ph] months of the year dropped 58% due to the -- and average dispatch of our gas treatment unit of 38% gas production over the quarter, compared with the maximum production that the unit is able to deliver. Moving to slide 7, there's a brief summary of our exploration and development activities. The graph shows the seismic acquisition campaign that was started at the end of 2017 and concluded in the first half of 2018, with more than 4 kilometers of seismic acquisition. The processing and interpretation of this data has been completed in 2018 and we define the first prospects to be incorporated in four blocks in the 13th round, which will be incorporated over the course of 2019.

Also, we had four additional wells drilled and one drill -- one evaluation drill in Gaviao Preto, which helped to increase remaining reserves of the company. The construction of the third well of Gaviao Azul was completed and this was also connected to the gas production system of Parnaiba Complex. And finally, we had an encouragement of low permeability reserves in the Gaviao Azul after the connection and the company is already producing in this low permeability reservoir for the first time in history. I would like now hand you over to Marcelo Habibe, who will talk about financial performance.

Marcelo Habibe {BIO 20367888 <GO>}

Good morning, everyone. Some highlights about our financial performance. We are moving now to slide 8. As has been alluded to, this was a very atypical quarter due to the early rainy season.

Because of this, the dispatch of the fourth quarter [ph] was 42% and this explains the reduction that we had in net revenue -- in recurring net income compared to the previous -- the same period in the previous years with 98% dispatch. In figures, we are talking about BRL61 million in net revenue, BRL200 million with a 42% margin over the period, and BRL71 million in recurring net profit, which is the best [ph] -- around 10% margin over the period. Net revenue, non-recurring events that we had in this fourth quarter, the net -- accountable net revenue was BRL479 [ph]. We had approximately BRL399 million related to accountable impacts in tax and the further [ph] incorporation of ENEVA [ph] that happened at the very end of 2018.

ENEVA used to be operational activity holding and had a large volume of tax losses with no expectations, is now a traditional company with upstreams. And we use this tax period to have better impact on our future taxes and we had a completion of our assets to be deducted from taxes. And these are paid accountable in 2018, due to treatment of non-recurring debts. The cash impact grew due to the result of these fiscal changes and we will have less tax to pay in the future.

Another point to be highlighted is the better performance of the coal generation tax rate [ph], which progressed from 70% in the 4Q of 2017 to 37% in the 4Q of 2018. The dispatch level was 62% and 65% -- compared to 65% in 2018. The lower dispatch in 2018 is still -- allowed us to deliver strong EBITDA of BRL1.4 billion, and this is the result of our discipline in cost reductions and operational improvements. In slide 9, we can see the progression of our Parnaiba Complex.

At the beginning of the rainy season, we have significant lower dispatch in generation plants and we had a reduction in the net generation of the Complex and also this had the same impact on gas production. In gas generation, in the 4Q of 2017, we had a positive impact due to the ending of operations at Parnaiba II in contract termination. In this segment, in 2017, we had 29.6 million and this led to EBIT of between the fourth quarter of '17 and fourth quarter of '18. In coal generation, the EBITDA growth was related to the variable margin of both plants.

Initiatives for operational improvement still delivered very good results. In Itaqui, we will have operation in line with the original project and the impact of the price reduction of the ICMS coal imports will be reflected in coal and fuel costs. In Pecem II, we had reduction of costs at risk and we had positive impact in the regeneration -- recomposition of operational reserves. In the fourth trimester of -- fourth quarter of 2018, and we had variable revenue of 126 million.

In slide 10, we can see the investments of the company, BRL76 million in the quarter, BRL3 million upstream, and BRL40 million in generation units. The upstream investments were destined to the completion of preparation of the wells, and we reports of low permeability in Gaviao Azul, completion of the construction plan in Gaviao Azul, and also

the pipeline connecting to (inaudible) and the production complex in Parnaíba. Last in (inaudible) generation were concentrated at Pecem II, where we had the acquisition of some material for the constructions in 2019. In slide 11, in the 4Q of 2018, operational cash flow was BRL629 million, an increase of 61% compared to the same period in the previous year and this was due mainly to the reduction of our working capital, which reflects the reduction of the accounts receivable in the fourth trimester.

Cash flow from investing activities was negative compared to a worse result in the first quarter of the previous year. It was -- had an impact on the upstream segment. Financing activity was impacted by preventing [ph] of the gas segment compared to the -- which happened at the end of last year. And we had BRL1.5 billion in Parnaíba I and II, and these resources were used to pay debt that were acquired by Parnaíba II and PGN Closed the year with cash generation of BRL1.2 billion, which is 1.8% cash generation, equivalent to.

Consolidated cash position at the end of the year is BRL1 billion, 18% higher than what we had in December 2017. In slide 12, we can see the company indebtedness. The main cost of our debt in 2018 was 9.3%, with a tenure of 4.5 years. Over the year -- over the course of the year, our optimization or collected net debt reduction in cost and extension of the tenure, so we had net consolidated debt of BRL3 billion, which is equivalent to 2.6 times of EBITDA On slide 13, you can see our debt amortization schedule.

The first phase of debt restructuring, our debt schedule for amortization was smooth and without any fixed [ph] for payments. The current of liabilities is compatible for the growth that we are planning for the company, minimizing the risk of refunding the debt in the future and giving to the company the option of accessing the market debt, whenever we find a positive to swap our debt in the long term to make it even cheaper to reduce our costs, which will be reflected interest rates, release cash flow, reduce leverage and as a consequence, improve the company's risk and credit profile. All of this will create a virtual cycle of value generation and the reduction of the interest spread for the next years and will release more and more cash flow. So now, I turn the conference over for the closing remarks.

Pedro Zinner {BIO 17260844 <GO>}

Well, just as we did in 2017 as compared to 2018, so we'd like to close the year of 2018 and are now expressing our goals for 2019. With economic recovery and a more liberal energy market, we see major opportunities in the near future. And so, this year we will continue to work to position the company to grow and to generate long-term value for our shareholders. In terms of gas exploration and production, our objective is to keep our natural gas reserves at least 100% availability and to reduce our exploration portfolio in Parnaíba basin.

We want to drill 15 wells in 2019, two of them will be exploration wells. We want to start the implementation of Parnaíba V six months in advance as to our initial plan, and we intend to start construction work in the dry season of 2019 with the objective of expediting even further the beginning of our operations and to capture additional gains. We also hope to complete, still in the first half of this year, the restructuring of Parnaíba V with a hybrid structure, thereby minimizing cost, optimizing the utilization of tax losses,

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and keeping the flexibility in cash management. And although feasibility and attractiveness analysis is going on, and subject to approvals depending on the company's governance, we have described the integrated generation project Azulao in Roraima auction that is scheduled for May this year.

So we have A-4 and A-6 auctions that the company is assessing to monetize this project. We believe that there will be a wind of opportunity for the development of energy and association gas projects and we want to have options of generation project that are competitive in both modalities of gas supply. A more liberal market may also bring interesting opportunities for the segment of marketing of energy, and we are assessing the positioning of our marketing companies and we wanted to position it to maximize the return on our assets, and to capture the benefits that arise from potential liberalization. Along the year of 2018, we revisited our innovation strategy.

We're focused on research and development assets to first extract additional values of the existing businesses by using new technologies, and secondly, to create new businesses with models that are potentially disruptive. In this manner, we are developing our innovation strategy and we have established as a goal for 2019, to implement pilot projects in small scale, up to 3 megawatts, distributed solar generation in Parnaíba, and also to structure star-up accelerator in the our -- in the area of energy. That being said, we are now open for questions and answers. Thank you very much.

(Question And Answer)

Operator

Thank you very much. We're now going to start our Q&A session for investors and analysts. (Operator Instructions). We are going to answer questions in the order we receive them.

(Operator Instructions). Please wait while we poll for questions. Thank you very much. If there are no further questions, I would like to turn the conference over to the company for their closing remarks.

Thank you very much. The ENEVA's conference call has ended. Please disconnect your lines, and have a good day. Thank you.

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