

Q1 2016 Earnings Call

Company Participants

- Anamelia Medeiros, Market Relations Manager - Engie Energy Latin America
- Eduardo Antonio Gori Sattamini, Finance and Investor Relations Director

Other Participants

- Marcelo Sah, Analyst
- Miguel Rodrigues, Analyst
- Vinicius Canheu, Analyst

Presentation

Operator

Good morning. This is Tractebel Energia's Conference Call, where we will discuss the Results of the First Quarter of 2016. All participants are connected only as listeners and later on, we will open the Q&A session when instructions for participation will be given. (Operator Instructions) You should remember that this teleconference call is being recorded. This presentation, followed by slides will be simultaneously transmitted through the Internet through www.tractebelenergia.com.br Investor's section. A slide presentation and the company's earnings release are also available on that website.

Before proceeding, I would like to clarify that forward-looking statements that may be made during this conference call regarding the business outlook of the company should be treated as forecast that depends on that country's macroeconomic conditions. The performance and regulation of the electric sector, in addition to other variable, therefore they are due to changes.

With us today are Eduardo Sattamini, Tractebel's Finance and Investor Relations Director, and Mr. Rafael Bosio, Investor Relations Manager, who will talk about company's performance in the first quarter of 2016 and Anamelia Medeiros, Market Relations Manager of Engie Energy Latin America, who will present an update on the development of Jirau Hydro Power Plant. Right after, we will have a Q&A session.

It is now my pleasure to turn it over to Mr. Sattamini. You have the floor.

Eduardo Antonio Gori Sattamini {BIO 16648085 <GO>}

Good morning to everyone. It's a pleasure being with you once again here. This has been not very surprising quarter, highly aligned with our plan. So we will start on presentation from the highlights with our main financial and operational index. Net revenue from sales

proactively had a slight drop mainly due to a lower amount of energy sold and lower amount of energy that was liquidated in the short-term market, offset by the improvement of the average price that you can see 5.9% quarter-after-quarter, a slight variation of minus 15 -- 16 million, 0.9% quarter-after-quarter.

Now the EBITDA. The EBITDA increased 0.4%, highly aligned with last quarter. We had a cost reduction that was significant with a contribution of a reversion of taxes, if we see the evolution of the -- evolution of quarter-after-quarter that was a real reduction. So this means that we are discipline in cost and this is a year of crisis, this is why we are doing this.

Now, our margin from 48.8 to 49.5, net income 0.7 higher, net debt dropping significantly. This is a result of our plan, because of the difficulties that the capital markets were facing during 2015. Therefore, we -- because of the investment plan that the company has for the upcoming year.

Now power production. Well, there was a drop of 8% due to the reduction of thermal generation. Last year, in the middle a hydrological crisis, 2015, the thermal plants were at their total capacity, we also had a slight drop in hydro and -- and this is why we had a drop in unconventional and renewable. Energy sold, a slight drop because of bilateral contracts and this is due to some drop in contract, so we have the distributor. Now, we had a 5.9 increase in average net sales price, well, because of inflation in 2015.

During the first quarter, there was an impact of short-term contract at PLD price of BRL180 [ph] per megawatt hour. This is why the price haven't -- didn't follow the inflation, but if you analyze during the quarter and the quarter -- the same quarter last year, we had twice -- the inflation doubled from 2014 to 2015.

Number of employees, a slight drop, this already reflects the voluntary retirement plan that has been taking place. We have had some vacancies during the replacement process of the people and we will have a slight drop of our personnel. And so, our voluntary retirement plan is affecting our cost reduction and our personnel possibly.

Now let's go, here we have the highlights of the quarter and subsequent event. The research and development project of photovoltaic solar energy received the 23rd Expression in Ecology Award, Technological Innovation category. A subsequent event Fitch Ratings reiterated its Long Term National Rating at AAA with a stable outlook and in the International scale we were also reiterated at BBB for our local currency issue with stable outlook and BBB minus with negative outlook for currency issues, the latter reflecting the recent downgrading in sovereign debt to BB, well, our sovereign dropped BB plus. This is something that we see in the press. Though we also guarantee here after a long analysis of Fitch, with long relationship with us AAA Brazil.

And now a subsequent event, on 19th of April, the company acquired 50% of the capital stock of ENGIE Solar, which is part of the other Araxa Group, one of the leaders in the Brazilian market for the distribution solar generation. In reality, the enterprises responsible and has as an objected to grow into generation market to work with distributed solar

generation in residency and this is something of the direct market with the consumer and this is an injection resource plan for the company that have been working capital and quality management for its growth. And we will start this transformation of the company and it will -- to be goes to our end customers.

Within our projects, Pampa Sul TPP hired the suppliers of the coal conveyor and transmission line and whose DUP was issued by Aneel. So this shows the normality of our projects and also reassures us that everything is according to what it is expected.

At the Santa Monica Wind Complex, the assembly of the first wind turbine tower was concluded using the uniform Eolift mechanism. This is an elevator and it builds the tower from a fixed base, so this is very interesting. And you will have an image in the presentation to show you.

Now when you go to page six, I believe there is no great changes within the shareholding structure of Tractebel. I believe that no major explanations are needed here.

On slide seven, we do have a very interesting fact. We had a drop of capacity in the last quarter to the date. We had a redefinition of the installed capacity of Charqueadas plants, it had 72 megawatt, now with 36. We're only working with two machines, because we want to reduce the panel -- the penalization of the reimbursement of coal. And we decided yesterday within the company to deactivate this plant that has reached the end of its life. It has been working for 54 years, but we have (inaudible) men and they have been working for up to [ph] 300,000 hours.

And the idea here of the Group is, with this process shut it down as of the end of August. So, I believe during the first quarter, we will prevent a drop of the 36 machines that were operating up to the date.

But we -- this is aligned with the -- and with -- and in view throughout the world, little by little to diminish its footprint regarding emission and this plant is an old plant and the emission was relatively high when you compare it to the generated energy.

On slide eight, where we talk about our leading position in the generating sector. We continue being leaders in the market. Today, we have a new player in the market that is close to us. Nevertheless, our impression is to continue being a leader in the market, not at any cost, but yes, we want add capacity to be where we want to be profitable and that makes sense to the long-term strategy of the company.

And on slide number nine, here we are showing our customer portfolio between free customers and regulators. Customers, trading companies we say that's a strategy of the companies to work on both market, to work with long-term for cash flow and the other one that allows us to capture opportunity like the free market.

So, within the importance of the free market and as we have to sell energy of existing plants to the regulated market at low prices and as you can see on page 10 of the

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presentation, we have a diversification of segments that we service in a systemic fashion and here we have a very positive result. And we've had zero level of default. It's not that there are no delays, there are delays, but generally the contracts are covered with guarantees and these short-term defaults are always paid at the end.

Now on slide 12. Here we will talk a bit about the market. We have reserve -- on the left-hand chart, there is a surplus of energy -- of energy available and this has generated pressure on a low PLD. Due to this view, our price calculation of the future surplus, the PLD is also at a low level and this has pressured the short-term price.

Here, we find at the beginning of the year very low prices, and now they've started improving with two components. One would be, rumors of a reassessment of the PLD price. And number one, would be -- that would be the -- a worst hydrological situation in the month of April, for the month of May. So these two components in a certain way affect the PLD going up to BRL80 something megawatt hour and in terms of long-term, we start observing that the market is practicing higher prices than that of last month. The PLD, as we mentioned during the first week of May, is around BRL36 megawatt hour and we have had lower PLD because of supply and demand and our hydrological reality that we had in January that improved in the different reservoirs.

Now on slide 12, here we have energy balance of the company. We have 5% of the energy of 2016 uncontracted, unhired. This is also a theoretical situation, we consider that the thermal plants are being dispatched within their trade capacity. And in reality if they're not dispatched there is a need to buy, so we are very close to a breakeven prone or a bit short. In 2016, the thermal plants aren't dispatching. Now, if this increases, well these thermal will be dispatched and they would cover this risk.

To be more accurate, in -- we have a low volume of energy in 2017, we are carrying our commercialization strategy for 2017. But this takes place normally (inaudible) sale and that purchase activity, that complements our portfolio for 2018. So here we have our results for 2016. And if may be we will have to buy for this year -- on the right hand side, this is how the company manages, if energy risk sold higher energy, so we are buying energy in such a way diminish the movement of price oscillation.

On 15th we have in our energy balance, so basically this is a modeling tool and this reflects our portfolio, perhaps we have no major highlights on this slide. We continue with the purchase activity for resale. And we have been very active in the sales, if you see on our vision of sold energy.

This quarter, vis-a-vis the past quarter, you will see a significant amount, you will see 17, 18, less than 19. We have had little selling activity and we believe that this allows us to maintain our portfolio. And in a certain way, this is also connected to an energy purchase of strategy to gain more margins.

Now we will go to expansion. And in expansion, we will have some novelties. We will start with Jirau project update. This is a project within the state that is in, almost the end of construction. We believe that it is a project that will initiate its process and believe the

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transparent process of ENGIE to Tractebel Energia. We also changed Anamelia, that is she is the person that follows up the project and communicate to the market and she is assuming new challenges within the headquarter of ENGIE in Paris.

And with this, we will concentrate the information of the project, so that Tractebel interacts more with the project. Together with Rafael, I'm going to give the floor to Anamelia and this is her farewell within the function of relationship with the market for ENGIE. Anamelia, you have the floor.

Anamelia Medeiros {BIO 16881348 <GO>}

Thank you very much. Good morning to everyone. And just an update of Jirau project. Regarding our last call, where we announced an increase of assured energy. In the back, we had 2,185 average megawatt of assured energy. We went 2,205 average megawatt due to the revision of the hydraulic expansion, 72% is contracted under 30 year PPAs. A-8 [ph] and A-3 Auctions indexed by inflation with protection of the hydro generation deficit higher than 8% and 10% respectively.

We want to differentiate the products for this contract. The point A, for instance, contracted under the three year PPAs that had an increase of 20 megawatt average of capacity. This was also contracted in the last Auction A-1, this is 0.8% of total assured energy under three year PPAs indexed by inflation. As everybody here knows the balance of energy available to be sold by ENGIE, Chesf and Eletrosul.

Now regarding legal decision issued in the first instance. We don't have novelties regarding the last calls of result and they were recognition of 535 days of force majeure, but the lawsuit remains under analysis in the second instance. Financing conditions have been continuously announced, but there is no difference regarding the press conference calls.

I would like to draw the attention to the following, to the chart on the right hand side. Here, we -- within our array, ESBR shareholders, we have 18 megawatts average. This is the portfolio and this is the contracted amount in the A-1 Auction from 2016 to 2018.

When we go to slide 18, this is an update of the hydro project under construction. Here we -- two are being conditioned and advanced. We would like to remind you that assured energy was reached with the 33rd [ph] units, so we've had assured energy, we have 42 units installed to that date. Now regarding Jirau project, it's that the -- HPP is the project with more availability indexed in the national system, almost 99.4%. This is the result of the quality processes and of the good engineering of the project.

Now the work will be concluded in the second semester of 2016 and as I mentioned, we have 22.5 [ph] megawatt -- additional megawatt as a result of hydraulic losses revision, so there we have options to create additional value -- additional assured energy to the operations of reservoir at constant levels that today is a variable reservoirs that varies according to the hydrological review of (inaudible) reservoir. While we want to do to negotiate with the government, this with the government, so without investments to

increase such additional assured energy of the plant. Additional long-term tax incentives in the region like COFINS and the ICMS.

Now, I will give the floor back to Sattamini to talk about the expansion plan. Hello?

Eduardo Antonio Gori Sattamini {BIO 16648085 <GO>}

I would like to add something. We want to complete this project. Here you can see the images that are highlighted here. And you can see that the construction -- what the hydro project under construction looks like. This is a timely moment to start analyzing to merging Tractebel's plan to ENGIE. And this process will start by a proposal given by the Board of the company, where we will have different committees and through this committee we will see the renegotiation of the prices and the transference condition and we have (Technical Difficulty).

Here we have Pampa Sul TPP thermal project under construction. This construction is at (inaudible), the installed capacity is 340 megawatts. This is from an Auction of 2014 and this is a 25 year Auction and the hired price of 202 a per megawatt hour base in 2014.

On slide 21, we have wind project under construction Campo Largo Wind Complex in A-5 Auction, 82.6 average megawatts were sold. This is a total of 148.5 megawatts that had been added that is for the free market.

And now, Santa Monica Wind Complex. We have four wind complexes and they total 36 machines and an installed capacity of 97.2 megawatt. This complex, the areolift that is the blue structure that you see that goes up to the tower. What it does is it lifts the tower and places the other segment below. This is new technology that is being used here, within Santa Monica Wind Complex. When you work with new technologies, you deal with some difficulties, but we have overcome these difficulties and the project will be operational until the end of the year.

Now 23, we have Assu Photovoltaic Central. We have the marginal price of the Auction. This is an auction from 2015 of reserved energy and the installed capacity of 36.7 megawatt-peak here and the price is BRL32 of megawatt hour. This contracted average price. And the contracted term is 20 years as from November 2018.

Now on page 24, the project pipeline that we have to deal with the government, that we are here maintaining our portfolio to capture the opportunities that may emerge. Here we have more photovoltaic centrals. Here we have Assu; here we have Santo Agostinho that are wind complexes from Rio Grande do Norte; CampoLargo Stage II, that is the continuation of same side of Campo Largo 330 megawatts; also, here we have our other Photovoltaic Complex from Bahia, that is we have a complex of Campo Largo. We have Norte Catarinense TPP, where we have been developing and it's a gas thermal plant and therefore, we continue with this project.

Now, we're working with distributed solar generation. In April, the company acquired 50% of the capital stock of ENGIE Solar and we will invest in management, in working capital in

order to develop this new activity of distributed energy up to 24.3 million and we believe that we will have a high rate of growth and a high rate of adoption of this type of energy in the upcoming years.

Now slide 27, here we have our financial performance. We will present the growth figures. As of 2015, we expect to go back to the years of ever growing profit. This did not happen between 2012 to 2013 and 2013 to 2014. These were difficult years, because of hydrology and regulatory changes. Our expectation here is that our results will go back to being growing and consistent result as we had before the problems that we had in 2013-2014.

In 28, we will talk about the net revenue from sales, it increased -- it dropped slightly, I apologize, but there was a positive component in terms of price. There was a drop in the short-term market, because of a lower PLD. As I already mentioned, when we see, the average PLD of 380 in 2015 and an average PLD of 30 something in 2016.

Naturally, we had less allocation in 2016. This revenue in the short-term market would have dropped. We had higher sales, we reduced megawatts in sales. These contracts were going to be terminated and they were part of the -- migration of this part of energy and this will be part of our reserve for 2017.

Now on page 29, here we have the EBITDA evolution. We had a slight increase of approximately BRL3 million. The first component that we present is our position -- we had positions in the first quarter of 2015 regarding expenses with fuel and legal questionings regarding the price. Here we have the position of the volumes and due to the magnitude of a potential loss, where our assessment is at the loss would be -- will be likely. This year, we didn't have high thermal generation and these figures are lower. And in the plan to be reviewed its figures and this follows the plans of the company.

Now there was also higher net revenues from sales of contracted energy, although not very much, netly, it's positive. Here, we had tax incentive, we recovered a bit in terms of taxes, but yes, we have had cost reductions in the company and our costs are according to reality. And we also have a very negative component, greater allocation from 2015 vis-a-vis 2016, which contributed a drop of a 113 of the EBITDA, when we compare it quarter-after-quarter.

When we go to page 30, here we talk about net income. I believe that there are no major surprises quarter-after-quarter. Here, we have a contribution of approximately 30 something million regarding a lawsuit that we won. Here, we are talking about regulatory matters and monetary correction of amount that we had to receive. We weren't able to receive part of this value that are contributing for that in the amount we have to receive. So consider this a definite expected revenue of 37.2 million.

Another part, here we have a possibility to withdraw and this will increase our cash position, but we still have not taken a final decision. We have to feel more reassured regarding these credits would belong to us. So with this we have an evolution of our net income of 0.7 or 345 million to 347 million.

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Page 31 and our indebtedness, low net debt, low robust cash position. Here we have a commitment until the end of the year, operation, liquidations and the short-term to finance projects. We're going to liquidate these operations. We hope that some financial operations will replace this short-term operation. The market now is showing relief in terms of cash. Yesterday, we dropped the PLD, so the market conditions that existed in the past are coming back. This is when we -- that are working with projects, with Campo Largo. And we do feel, we want to liquidate the short-term operations and the cash position will support the dividend payout throughout 2016 and 2017.

On page 32, here we have the average -- the evolution of the net debt, then we have our operating cash and here, we have the payout of dividends or on capital, the investments that were carried out. And here the operation that has been a reversion of operation, the reversion of the trends of the currency depreciation created this effect. Now the operation are 100% hedged, both the financial operation of debts in dollars and the debts regarding projects, we hedged for the equipment, in the profile of disbursement of each one of the projects.

Now on page 33, here we can see a concentration of long-term debts of 2016. We -- the value is high, slightly below 1 billion and this is a component of the remaining debt. Here we have the MDS, but the maturity of these operations will be paid through CDI. The cost of the debt a 12.2% nominal -- 11.2% nominal, mostly LDS, CLP, so we're talking TJLP and IPCA.

Page 34, here we have our investment plans. We have low indebtedness, low investment, although we believe that this Jirau operation will start in the end of the year, at the beginning of next year and this will also add some type of indebtedness to the company. But here in 2017-2018, we have almost BRL6 billion in investments, most of this will be financed and with this we will have a leverage level that will be higher. And capital structure. This was done on purpose and this was one of the company's concerns of having liquidity and to maintain its ratings, because these ratings are necessary for the company to guarantee its competitive position in the market.

On slide 35, here we have our dividend policy known by everyone. By-law minimum payout 30% of payable net income and 55% of management commitment. This is a minimum payout, but when our cash position allows us, we don't want to retain cash. This only happens in special situation, so I believe that we will stabilize our cash position, so we will start working with a more robust cash.

And this presentation of the quarter is -- well, this is our presentation. We are open to your questions now.

Questions And Answers

Operator

Ladies and gentlemen, we will initiate our Q&A session. (Operator Instructions) The first question from Mr. Vinicius Canheu of Credit Suisse.

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Q - Vinicius Canheu {BIO 6300903 <GO>}

Sattamini, good morning. Thank you very much for the presentation. You mentioned that there was an impact of the differentiation [ph] of the PLD? I would like to know if you can quantify what this loss was and what is the impact like if you have a relevant sales to the Nordic. Any other type of consequence during the quarter, because of this?

A - Eduardo Antonio Gori Sattamini {BIO 16648085 <GO>}

Yes, there is an expansion in the Nordic. This is not information that we announced and its exposure value varies. It depends on the amount of generation of our complexes. Yes, there was an effect, and we don't include this in the information. This is information that we do not disclose.

Q - Vinicius Canheu {BIO 6300903 <GO>}

Thank you very much.

Operator

Next question Miguel Rodrigues, Morgan Stanley.

Q - Miguel Rodrigues {BIO 16533007 <GO>}

Good morning. Sattamini, I have two questions here. Number one, I would like you to elaborate on the change of the PLD methodology. You believe that is necessary to increase the risk reduction, and if the correct way occurring of this change is through the reduction of LFA [ph] or do you believe that the price model has other deficiencies that should be revealed in a broader fashion.

My second question is regarding your energy portfolio, you've presented a significant increase in bilateral sales, reaching 6% of your costs of 2018. So the lack of liquidity in the past is behind, and now we have more appetite from industrial consumers. I would just wanted to confirm this and if you could share with us the timelines and prices that have been practiced when you deal with long-term?

A - Eduardo Antonio Gori Sattamini {BIO 16648085 <GO>}

Now regarding PLD changes, the company has divided this within the different associations. I do not want to advance the company's position. Now regarding the price levels, what we have observed is that this change in prices, and the calculation of price methodology is affecting shortly then long-term prices. We're talking about price levels above 130 or 135 already proposed for the upcoming year. I would say with an ever growing trend you do know that the first-three years, we will have a great influence on the PLD and the excess that as of 2020-2021. We will have marginal expansion dispatched and this will not be lower than what it was in the recent past. There is lots of pressure, lots of material has been commoditized, the price is in dollar.

So you can see when our plans are 120 -- electrical plant 160 above is going to depend on the type. So what we see here is that in the short-term price trend is high. It is a high

market in the short-term there will be a reduction in the consumption and industrial consumption. And depending on the economy, perhaps we will have a rebound of the economy. The -- another factor that may bring -- in fact that can affect us is the hydrology. Hydrology hasn't -- isn't strong yet. You will see, we are going through a period of drought in April and perhaps in May. We can see that the prices are better than the last quarter's prices because of a number of factors, but the mark -- though, we have as of 2021-2022, the prices will be higher.

Operator

The next question Marcelo Sah from UBS.

Q - Marcelo Sah

What about energy allocation throughout the year, I would just like to confirm that you were showing not only internal, during this quarter and the trend that this will be reserved throughout the rest of the year, what drove -- you talked about long-term price 130, 135. So, I think prices of BRL125 for three year contracts?

A - Eduardo Antonio Gori Sattamini {BIO 16648085 <GO>}

Marcelo, let's go there. Let's see. Yeah, we've been talking about prices, so the prices are a bit higher. As you said, new cap prices are 120 or 125 a month and a half ago, but we are observing a reaction of prices. That are going to the levels that you just mentioned, 135 throughout the upcoming three years, 135 onwards. Now regarding our allocation position we do not provide information, because as quarters go by, we'll (inaudible) the price -- the low price level and low PLD, our thermals are not dispatched. That is what I can say about our position of allocation. Thank you very much.

Q - Marcelo Sah

Thank you very much.

Operator

(Operator Instructions) Our next question is from Miguel Rodrigues.

Q - Miguel Rodrigues {BIO 16533007 <GO>}

Sattamini, one other question. You spoke about the generation assets in the market. I would like an update of how you want to grow there can be merger and acquisition. How do you see, do you have an appetite for growth, do you believe this is the pathway of growth that makes sense or you will be not looking into these possibilities?

A - Eduardo Antonio Gori Sattamini {BIO 16648085 <GO>}

We are not -- we do not see the assets that are for sale and something likely to do this more. Currently, we are not strongly inclined toward a M&A. Now, of course, if there is a good opportunity, we will try to capture it. But we don't feel very reassured with the opportunity that have emerged in that market. We have given priority to the growth of our

Greenfield project, controlled -- that are controlled by us and controlled in terms of their deployment on how the deployment processes work, more than through an M&A.

Q - Miguel Rodrigues {BIO 16533007 <GO>}

Okay. Thank you very much.

Operator

We bring our Q&A session to an end right now. I would like to give the floor to Mr. Eduardo Sattamini for his final comments.

A - Eduardo Antonio Gori Sattamini {BIO 16648085 <GO>}

I would like to thank everybody for your attention -- for attention and questions. And we are at your disposal for -- through our Investor Relations team to provide you more information and more detail that you would be interested in. Have a very good morning.

Operator

Tractebel Energia's conference call has come to an end. We thank everybody for their participation. Have a very good morning and thank you very much for using Chorus Call.

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