

Q2 2018 Earnings Call

Company Participants

- Cristiano Prado Grangeiro, IR Manager
- JosÃ© Aloise Ragone Filho, Business Development Officer & Member of Executive Board
- Marcus Pereira AucÃ©lio, CFO, IR Officer & Member of Executive Board
- Unidentified Speaker, Unknown

Other Participants

- Marcelo SÃ¡, Associate Director and Analyst
- Maria Carolina Carneiro, Analyst
- Rafael Bezerra Dias, Banco de Investimento S.A., Research Division
- Thiago Silva, Research Analyst

Presentation

Operator

Good morning, ladies and gentlemen. Most welcome to the earnings presentation webcast for Taesa Second Q '18. We inform all participants that the presentation to be made now is available for download at the www.Taesa.com.br/RI site. (Operator Instructions)

Before going on, we would like to state that possible declarations that will be made during this webcast relating to the prospective business of the company, projections and financial and operating targets, are assumptions of the Taesa board as well as information currently available to them. Future considerations are not guarantee of performance and involve risks, uncertainties and assumptions. Please refer to future events and before depend on circumstances that may or may not happen.

Investors must understand that general economic conditions, industry conditions and other operating factors might affect future results of the company and lead to different results in material terms from those expressed in those future considerations.

I would now like to give the floor to Mr. Marcus Aucelio, who will start the presentation. Mr. Aucelio, you may go on, please.

Marcus Pereira AucÃ©lio

Good morning, to all. First of all, I would like to thank the participation and the interest of all of you in the webcast with the earnings presentation of Taesa Second Q '18. We have Directors Marco Faria, our Technical Director, with us; and also our Director for Implementation of New Businesses.

Before we go to the earnings results, I would like to stress Taesa's commitment with its main strategic pillars that are sustainable growth, financial discipline, operating efficiency and shareholder value generation. We know how important growth is for our business. And our history proves how competent and successful Taesa has been along this sense.

Please look our assets going from (8 concessions to 9) currently one of the largest transmission companies in the country, with 35 concessions and over 12,000 kilometers of lines throughout all the Brazilian states and the Federal District. And going out from our RAP allows annual revenue to (BRL 3 million), investing BRL 5 billion in acquisitions and buildings. And at the same time we found we distributed BRL 6.8 million in dividends to our shareholders.

Taesa will always go on after financial discipline, business sustainability. And mainly value generation to our shareholders. We believe in the Brazilian transmission market. And we will spare no efforts to pursue growth. We have been updated with great results in this difficult macroeconomic environment. And in a very competitive scenario in transmission. Our large experience in the sector and the operating situation that we know throughout the country, we know very well the power transmission business. Therefore, we will go on with our growth strategy by generating value. And also participating in the transmission auction for acquisitions in the area. And we will devote our time to these opportunities and as we saw or did in last quarter, we will actively participate in the transmission auctions of Eletrobras, in five of the eleven (SDF) that will go on auction.

We also have focused our attention to our eight projects in work in progress, with a very attractive return in the 2016 and 2017 auctions. And we will go after higher efficiency in constructing them.

Now going to slide number 3, I will speak about the main points in our second Q results.

The main point in this period was the growth of BRL 259.3 million and a growth of 2,059.9% (sic) (259.9%) in comparison, basically due to the monetary restatement of financial assets. And this increase in net profit was due to the increase in IGP-M that in the second Q '18 recorded an inflation of 2.6% when last year we had a deflation of 2%.

This increase in IGP-M also participated in the (union) and for the TBE group. Also it did in the direct interest of (Transmineiras), since we have direct stake in these assets since November 2017.

In terms of the remunerations to shareholders, the company paid in the first half of this year, a total of BRL 413.2 million, which represents BRL 0.46 per unit. And besides our ordinary shareholders' meeting approved yesterday the distribution of over BRL 188 million in dividends, interim dividends based on the first Q '18 results.

And the payment referring to this distribution will take place on August 20, based in the shareholders' position of August 9. Thus, Taesa maintains its commitment to distribute as much as possible its results to shareholders.

In terms of the regulatory results, we presented a solid operating cash generation. Our current cash balance reached BRL 832.8 million in the second Q, an increase of 14.3% in the annual comparison and a reduction of 8% in the sequential comparison. Therefore, our net debt totaled BRL 2,311,000 down 15.1%. And we -- the net that EBITDA recorded 1.4 times in this quarter against 1.7 times in 2Q 2017.

Our net revenue reached BRL 413.9 million in second Q, annual decrease of 4.5%, driven by the cut of 50% in the allowed annual revenue. And therefore, our EBITDA totaled BRL 361.3 million with a decrease of 6.1% versus last year, reporting margins of 87.3%. It's important to say that we remain very helpful with our strategy to provide the best qualities of financing. And therefore I want to mention that this year in May, the company renegotiated the credit agreement and postponing maturity for May 2023. And we also elongated the debt in the amount of BRL 350 million. And besides this, we also negotiated the elongation of the term reducing the interest part in this loan. So from 114% to 103%. And besides, in July we concluded our fifth debenture issuance, issuing BRL 525.8 million, representing at a cost of IPCA plus 5.95% and maturity in seven years.

(technical difficulty)

(foreign language) in Paraguacu. And a return in the concession of the new plant.

And last, I also want to highlight the credibility that the market has shown for Taesa. This is due to our daily work and the persistent financial discipline. And also S&P raised our credit rating in the national scale. Therefore, we are reaching an excellent rating, the top ratings in the three agencies. And these attest to our ability to earn our financial obligations and reaffirms our credibility vis-à-vis the market.

Now I give the floor to Cristiano, our RI manager, who will go into more details as to the results of the second Q.

Cristiano Prado Grangeiro {BIO 20213891 <GO>}

Thank you, Marcus. Good morning, to all. Let's go to slide number 4, where we will start to speak about the net profit in IFRS.

We closed our net revenue in BRL 351.2 million, 107.5% higher than the amount recorded in the same period last year. The main factor for the increase in that revenue was the restatement which increased in the amount of BRL 192.1 million in annual comparison. And I will go over in more detail the increase in the restatement, due to the high in IGP-M.

The revenue, remuneration revenue, naturally dropped due to the amortization of AF, which was amplified for a period of lower inflation in the last 12 months. On the other

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hand, the construction revenue increased by BRL 22.1 million, mainly due to the building of the concessions of Miracema and Mariana. Also in terms of the variable portion, there was a negative variation of BRL 5 million in the annual comparison. One of the events was caused by the automatic shutoff of (inaudible) Sao Joao do Piaui and the other was called for by the corrective maintenance of the reactor banks with the aim of resolving oil leakage. It's important to mention that the company has been working towards reversing the provisioning. I also want to remind that 2017 we had our variable portion at 0.5% of RAP. And consequently due to the good work of Taesa.

And in other expenses, we had an increase of BRL 2.7 million, mostly explained by the receipts in (O&M) referring to the sectioning of the concession line TSN, just in the (Ibicoara 3) station.

Now we go to slide number 5. It's also important to mention the movements of the inflation indices that corrected the financial assets. I would like to remind here that in order of asset correction, we use the inflation with a lagging of one month. The graphs here that you have on this slideshow the evolution of the inflation indices accumulated along the quarter. It's interesting to mention that exactly one year ago, we were explaining why the monetary risk statement revenue dropped so much in comparison to the Second Quarter 2017 against Second Quarter 2016. At that time, indices of the inflation had a reduction, a sudden reduction, mainly in the IGP-M, which reached its lowest level in the last two years with a deflation of 2%, as you can see in the first comparison. And in this period the monetary restatement (recipe) reduced -- were cut short by BRL 172 million, after the second Q '17, IGP-M to which our assets are exposed, much exposed, reported indices in continuous growth.

Consequently, the monetary restatement received also started to show a consistent increase quarter-after-quarter, reporting in this second Q '18 BRL 104.6 million cash, which is quite an impressive increase of BRL 192 million, again, the breakthrough of 2017. Also recovering the level of revenue that we had two years ago in 2016. It's important to mention, the large exposition of our concessions at IGP-M since most of them is category 2.

This exposition is driven by the correlation of the graph that you have here on IGP-M and also the ones in the lower part of the monetary restatement of the financial assets.

And lastly, as was mentioned in the beginning, in this current scenario of macroeconomic increase, we were able to distribute a higher result to our shareholders. Therefore, the year-over-year graph shows a revenue of monetary restatement of totaling BRL 173.2 million, an increase of almost BRL 200 million. And the year-over-year totaled BRL 210 million in the dividends distribution and grew by BRL 170 million in the same period.

In the Second Quarter of '18, our cost show total BRL 81.4 million, 46.8% when compared to the same period last year. In this graph, slide 6, you can see that the increases do lend it to the cost of construction, that as we said mentioned in the slide with revenues, is due to Miracema and Mariana holdings, as well as to higher costs with reinforcements and improvements at Novatrans and (GSM). The cost with personnel also increased 15.1% in

the current -- in the year-over-year mainly due to the salary readjustments of workers, due to the collective bargaining and also the systemic (error) in provisioning all these amounts.

The cost of service without sourcing services increased by 10.6%, due to higher administrative expenses related to provisioning for contingencies. In the line of other expenses, we had a reduction of 22.1% resulting in a written negotiation with the supplied insurance supplier, generating OpEx gains to the company.

Slide seven now, please, we will (flip) construction costs because they are compensated by the construction income. And it doesn't impact the IFRS of the company. So we see the ONM construction costs. And in a year-over-year increase we have reached 9%, totaling BRL 52.6 million in the quarter. When we exclude even more the (punctual effects) of the (systemic error), in the personnel line, looking down here at the slide. And this is -- was around BRL 2 million. As we mentioned in our last quarter teleconference, OpEx reached an increase of only 4.7% in annual comparison. And the personnel line in this case grew by 7.8%, basically due to the salary readjustments due to collective bargaining and hiring new headcount for the new concessions.

Slide eight now, we speak about the results of equity income IFRS, with a growth of BRL 70.9 million in annual comparison. This is mainly due to the result of TBE, due to its large representation in our stakes. And since Taesa, the (inaudible) impact was the high in IGP-M which affected positively the monetary restatement revenue, BRL 92 million. And besides the net financial expenses, were 38% lower than what we reported in second Q '17 due to the paying out of the second issuance of the ventures of (EAT) and (XA) in October 2017 and due to the drop in the inter-bank deposit during the period.

Another impact in the equivalent is the direct participation of Taesa in (Transmineiras) since its acquisition November 2017. By saying that, the results of this subsidiary also impacted the performance of the equity income line when comparing the two periods.

Now slide nine is the financial consolidation income. The consolidated (tie) as the financial link, on both this BRL 54.7 million in the quarter with an increase by 3.1% against BRL 53.1 million last year. Like Marcos mentioned earlier, the lower volume in that and the higher CDI compared, were compensated but the increase of IPCA associated to a higher debt index to this inflation index.

Now slide 10. We go to net profit according to IFRS, which are the highlights. Here, we reported (rate) of almost 260% in the annual comparison, which means BRL 190 million higher than the same period 2017. And as you can see in the graph, the strong positive performance of profits was basically due to an improvement in net revenues and the growth in the line of equity income, both impacted by the increase in IGP-M.

Now the regulatory net revenue -- the operating net revenue consolidated at Taesa closed the Second Quarter of the year at BRL 413.9 million, a reduction of 4.5% when compared to the same period 2017. If we consider the stakes in all the invested companies together. And the affiliates, the total of the net revenue was BRL 526.7 million in the quarter. The reduction of 4.5% explained mainly by just allowed annual cut in TSN,

which attained the 16th year of operations in the cycle 2017-18 and also due to the risk reaction in the drop of this annual allowance at ETEO in the previous cycle.

Another cost was the reduction in the net revenue, was the increase of the variable portion in the quarter.

Now the regulatory EBITDA, which is the best proof of the cash operating of the company, demonstrates the operating capacity of our cash flow. In second Q '18, EBITDA, consolidated EBITDA, was at BRL 361.3 million, showing a reduction of 6.1% in annual comparison. And an EBITDA of 87.3%. If we consider the stakes as invested companies together and the affiliated EBITDA was BRL 462.1 million, with a margin of 87.7%.

So in short, the (rough cut) of concessions TSN and ETEO, the increase in the variable portion due to unforeseen advance. And the correction of the system of provisioning of its amounts, a system which (thankfully) impacted the cost in personnel around BRL 2 million. It is important to mention that in regulatory accounting, differently from IFRS, we have the investments that are accounted for as part of this demonstration and therefore the answer is operating expenses.

Our debt, the gross debt, closed the quarter in BRL 3.1 billion with an average term of 3.1 years, being 85% of the total long-term maturity. 78% of the debt is currently indexed by IPCA and the remainder practically by the (interventive) (inaudible) (certificate). Our average cost of debt currently is (BRL 4.5).

As a consequence, net debt of the company reached BRL 2.3 billion in the second Q '18. With that, the ratio of net debt over EBITDA was 1.4 times.

And now before we close the presentation, we would like to give the floor to our Director for Implementation and Development of Business, Jose Alois Ragone, to tell us about the whereabouts of our projects in construction.

JosÃ© Aloise Ragone Filho

Thank you, Cristiano. We will now share with you eight projects that are being implemented, three of them which are integral participation of Taesa, Miracema -- Miracema Janauba and a partnership with (UNIPAR) and the three (Amara), Aimores and Paraguacu, in partnership with CTEEP.

About Miracema. And the (BTE), it's important to mention that we already have the possibility because Miracema has (five from three) different substations, in a stretch of 300-330 in (SKZ) and all of them have been staffed already. And the operations foreseen for EDTE are consistently being ready to be re-initiated in the last quarter of this year. It's important to state that this term was calculated, it was based in a schedule that I oriented. And I would like to mention that all the schedule involving projects, licensing, acquisition and contracting equipment and the manpower. And all of them have an initial definite project. We now have (CFT), Janauba, Aimores and Paraguacu. We are about to receive the license and the license for implementation. And this gives us the conditions to start

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working under the situation and start discussing the situation to be able to start operations in (RTS), Janauba, Aimores and Paraguacu, representatively before the term contracted by (ANEL). So we are working with these four concessions, with a very strong position in startup of operations.

And last, (IGI) which is our (inaudible) investment effort because we have the conditions already implemented. And we are in a very calm situation consistently thinking of starting operations six months before the contracted term, which was August '22.

And to close my brief presentation, I want to say that the eight projects are in line with the physical schedule. And they are in very favorable conditions to start operations. And as I said, five of them with a very consistent forecast to anticipate (stock-up) of operations and mostly the anticipation of acquiring additional allowed annual revenue for the project.

And it was up to me to conclude our presentation. And therefore we close the presentation of results of Taesa's Second Q 2018 and we now open the floor for the Q&A session. Thank you very much for your attention.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from Thiago Silva, Santander Bank.

Q - Thiago Silva {BIO 19419043 <GO>}

My question relates to the growth strategy of the company in the last few years. How do you intend to grow more concentrating in brownfield, or not? Due to what we have seen in the last auctions, there is such a high competition. So we want to know how does the company seek growth, maintaining the capital level it has shown so far?

A - Unidentified Speaker

First, I would like to reinforce the fact that our discipline and our strategy of adding value to the company and to our shareholders, this is our guidance. And therefore this gives us our (now historic) growth. Naturally, due to market conditions which you know very well, companies that said the market today have different positions from what they had in the past, in the recent past. Therefore yes, we did focus and will focus in our plans despite having lower opportunities than in the past. But we will spare no opportunity and with our dedication and our struggle, we will participate in all these auctions successfully. We have noticed higher participation in recent auctions. But recently we think that very few players will change our positioning, defining growth as number 1. And financial structure and value adding, this will not be abandoned, by no means, or placed in second place. For us, this is our higher degree decision.

Operator

Our next question comes from Maria Carolina from Credit Suisse.

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Q - Maria Carolina Carneiro {BIO 16342681 <GO>}

I have two questions. The first, if you could go back to the issue of the variable portion, in order to better understand, in the beginning you said that you were applying at ONS to revert the negative impact of the two advance that were unforeseen. And in order to understand the process, also to understand what -- how recurrently we would see this variable portion in the next quarter or half of a year? Second question, going back to (NMA) you mentioned in the call and the media published the positive expectation of the company to implement the auction of participation in the U.S. auctions, where you already have a participation. We would like to understand what -- I know it couldn't be marked in -- that's for September. But I would like to know how feasible it is, your participation in September, or if you believe that this would be left for year-end mostly.

A - Cristiano Prado Grangeiro {BIO 20213891 <GO>}

This is Cristiano. I will start with Ragone who speak about the auction situation. Then, our colleague here will explain better. In terms of Eletrobras, I think that the most important, (Carol), is that we are prepared very well-positioned. And out of the 11 participations that were offered, we already participate in five of them. And due to the shareholders' agreement, we have the right of preference. And we participate in a lot of concessions. But however, we will analyze very carefully what is being offered. And we understand that yes, it is viable. And by the end of September, we will see. And we have very positive expectations of (ties) in this auction. This participation will address the answers to the first question.

A - JosÃ© Aloise Ragone Filho

In the two occurrences mentioned, the most relevant refers to the line going to Sao Joao du Piaui. The automatic shutoff coincided with a period of truck drivers' strike. And everything was very harmed due to the strike, with the oil and all that we lived through. And therefore this reconsideration of the variable portion due to this situation.

Operator

Our next question comes from Marcelo Sa from UBS.

Q - Marcelo SÃ;

I have some questions. First, I would like to hear in more detail how are the discussions regarding the project you are building, your construction? We saw no financing from BNP. I would like to know what's happening, indeed and what would be the potential amount for financing that you want to get in this cheaper credit line? And also in infrastructure, what are the new projects with BNDS, another infrastructure project? Please, if you could give us more details on the launches? And the last question regards the last auction. Did you have any situation or information that you could share with us on what would be an excellent return? Something you had in mind in order to give us an idea of what you want to get in this last auction?

A - Marcus Pereira AucÃ©lio

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I will answer the first question. And the second question will be answered by Ragone. In these projects, we have Mariana and Miracema. And we also issued a debenture some time ago from equity. We also raised IPCA+441. The other part of financing, as to the other part, we also have the board's approval and also (the NDS) approval. And both projects are in the phase of hiring, contracting, at Miracema. In terms of the project of BNP, we have the opportunity of Janauba, Aimores and Paraguacu. And Janauba is already well-advanced. And as soon as we have the previous license, the previous license which is promised for last month, we will certainly sign the contract next month already. Aimores and Paraguacu also will have its previous license by the end of August. And we also are pursuing the efforts to get financing at BNB. We will close the contract, Aimores and Paraguacu in September, Janauba in August. And what we have got so far in Janauba and Paraguacu is the following. Paraguacu is 100% in (SUDENE's) area and the two projects, for the two projects we were able to get 70% of financing at BNB and plus 5% in debentures as part of the project by sharing guarantees with BNB. In terms of this debenture, we just issued an infrastructure debenture for Janauba, Aimores and Paraguacu. So in terms of financing, the project is quite decided, defined.

Q - Marcelo SÃi

Sorry to interrupt you. But I want to know, Janauba, Aimores and Paraguacu, 70% with BNB? And you would have any IPCA+4 costs during construction, which will drop if you don't have to put a guarantee or something? Is it along this line that you are thinking?

A - Marcus Pereira Auc lio

Yes. In terms -- this should be IPCA plus around 2. And in the middle of the construction (we would have it) but afterwards we would not. But the cost will be around IPCA+2. And one, this is the name of (IVAI) which will be ERB1. We are also (pleading at Benedea) (BNDS). And we are talking with some institutions. And we will be able to raise the funds with long term with quite attractive rates. Since in these projects we would have a higher leverage, with a rate of 82% to 85% and also an amortization structure for the debentures in these projects, which will be a more customized line of debentures. So we are having all these market conditions that add more value than BNDS so we are analyzing this currently.

Q - Marcelo SÃi

I just want to understand, (BNDS) would be for a line of debt around 7?

A - Marcus Pereira Auc lio

No. We are analyzing too, Marcelo. IPCA also and (CLP). So IPCA plus CLP today. This could be scaled up to five years' time. So CLP today is more advantageous than IPCA. And the question on the last auction, I'll give the floor to Ragone.

A - Jos  Aloise Ragone Filho

Marcelo, this is Ragone. Our focus is growth. And we try to reach it as best as possible. Therefore, it's natural that after the auctions, we step back and carry out our analysis. And this is part of the game. And this has enabled Taesa in the last two years to participate quite effectively in the auctions. 2016-17 we had a very outstanding participation. We also conquered in a very positive form for all the results with the new concessions. And this

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gave us some lessons. So after the last auctions, we analyzed the situation and this analysis enables us to improve our raising. So after every auction, we become more and more competent in adding value and in market participation. But we already considered that when I do not depend on third parties' actions. And when this is technically viable, I am (at a state) that today I am not depending on third parties. Today, Taesa works with a CapEx license which is much higher than before. And our structure enables us to anticipatedly contract important input for (cables towers) implementation. So answering now after my comments, which I think are important, I showed you what motivates us to participate in the coming auctions and I can tell you that in the way we work, we went to our maximum. We had watched one with the result above 50%. But our player was labeled to deal with a higher discount. But this, after all of our efforts to competently and with discipline, participate with discipline, we wouldn't repeat this. But when we consider the discount of our competitor. And our situation, our money, (inaudible) (complete) for our growth strategy doesn't make any sense and of course, we would provide the lower returns to our shareholders.

Operator

Our next question comes from Mr. Dias from Banco do Brasil.

Q - Rafael Bezerra Dias {BIO 19216212 <GO>}

I had two simple questions. First, the confirmation on the RAP error due to labor charges, if it was solved or something was left for the next quarter? Second question, what you recently declared the payout rate was 64%, which is slightly lower than historically carried by the company. Since June's (IGPMs) were quite different from last year, I would like to know if with this higher, stronger results -- if this stronger results, will we have a stronger dividend distribution and the payout rate as well.

A - Marcus Pereira Auc lio

Answering your first question as to provisioning, yes. These causes that are known -- these are ad hoc causes. Some of our situations were civil, others were labor charges. And due to these judicial processes, we could have never new causes and new values. And we will not make a forecast of trends. In terms of the second question, what the company has been doing is the following. We have been distributing as much dividends as we can. In the net profit we gear 5% to legal reserves and also the fiscal incentive reserve which we have with SUDAM and SUDENE. As to payout, it varies as a function of interest on equity. And what we have in the First Quarter, we paid basically result through dividends less interest on equity. And this call does to provide higher distribution in the First Quarter for reserves and fiscal incentives. As of the first half of the year, when we once more have higher interest on equity, the payout throughout the year will get close to what we distribute normally, which is around 90%. It was much more the payout as a function of the fact that we distributed less interest on equity in the first half of the year. And this influenced the high rate of payout. But the company is trying to pay as much dividends as it can.

Operator

As we have no more questions, I would like to give the floor back to Mr. Marcus Aucelio for his final consideration.

A - Marcus Pereira Aucelio

I would like to thank on behalf of our board and Taesa's team to all who participated in this teleconference. I would also thank Taesa's team for the excellent work they have been carrying out towards building a sustainable and strong company. This dedication and efforts have been reflected in our results. Thank you very much. And have a nice day.

Operator

Thank you. The teleconference of Second Q '18 of Taesa is closed. Please disconnect your line. Good afternoon.

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