

Q2 2019 Earnings Call

Company Participants

- Daniel Isaza Bonnet, 'Member of Management, Human Resource, Auditing, Financial and New Business Committee'
- Marcus Pereira Aucelio, 'CFO, Investor Relations Officer Member of Executive Board'
- Raul Lycurgo Leite, 'CEO, Chief Legal Regulatory Officer and Member of Executive Board'
- TAE, ''

Other Participants

- Catalina McCartney
- Rafael Dias

Presentation

Operator

Ladies and gentlemen, thanks for standing by and welcome to the conference call of Taesa. We would like to inform you that all participants will be in a listen-only mode during the company's presentation, (Operator Instructions). I would now like to turn the call over to Mr.Raul Lycurgo Leite, Taesa CEO.

Raul Lycurgo Leite {BIO 19066621 <GO>}

Good morning everyone, we would like to thank you for attending this conference call.

Here with me are the Director Mr.Marcus Aucelio, Director of -- Financial Director and IRO; Marco Faria, Technical director and Jose Ragone, our Business Director. Before Beginning our presentation of results, I would like to mention some important deliveries of the period in a very brief manner in the month of May and April, we completed the acquisition of the shares of Eletrobras in EtAU, Brasnorte and Transmineiras that we acquired in the first auction of Eletrobras that was held in September last year. With this we started to have the important shares in those assets, adding more than BPL 50 million of RAP in our asset bases and BRL 9.8 million to the result of the company in view of the advantageous purchase of those assets. In the Greenfield project that are under construction, in this quarter, we were granted the installation premits for our major undertaking, Janauba, Paraguacu, Aimores and some facilities in Ivai.

And therefore we are now with all projects with their work target. At the end of the presentation, we will provide details of the progress of each of them. From the regulatory viewpoint and new published in June, the Homologation 2565 of 2019 that establishes

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that of its concessions of transmission for the cycle 2019, 2020 beginning in July 1, 2019 and being valid up to the third quarter 2019. Without going too far, we are going to complete the reduction of the cycles, relevant of RAP in view of the concession agreements of category two and as of December this year, we will see an increase in our regulatory income in view of this concept of the new project under construction.

In addition, completing all the conditions based on the acquisition of the four assets, we are going to increase our, RAP in an additional BRL130 million. We'd like to stress that Taesa has been working to continue its growth process always based on the pillars of financial discipline, return, operating efficiency and value generation to our shareholders. Another relevant point is our commitment with sustainability. It's levels of governance, social responsibility and environment.

In this regard, I'd like to stress our issue of green debentures with a matured period of 25 years that was completed last May, reinforcing our commitment with all society and our stake holders. Before turning the floor to the next speaker I would like to remind you that we launched the new RI site, fully reformulated with a direct and simple communication and an interactive and innovative experience that is responsive to all types of -- to investor in the investments. This is a proof of our commitment with transparency, an important pillar of our corporate governance. We've enjoyed this rich source of information about the company and the transition sector.

I turn the floor over to our Financial Director and our IRO, Marcus Aucelio, who will present the results of this second quarter.

Marcus Pereira Aucelio {BIO 19965152 <GO>}

Thank you Raul, good morning everyone. We are going to start our presentation from slide three with the highlights of the second quarter and with the results in IFRS in this quarter, the income profit reached BRL307.4 million, an increase of 11.3% were higher when compared to the second quarter of 2018, the next factors that impacted in a positive way, the net income of the second quarter 2019 for the following, the first one was the increase of inflation rates both for IGP-M and for IPCA with an impact in the line of the monetary correction line as well as the equity method with a growth of BRL10.2 million and BRL19.9 million respectively, with a higher operating income and maintenance income at BRL6.5 million. This is the results of the adjustments of the 2018 2019 cycle.

We also had an improvement in our variable parcel of BRL8.2 million in the annual comparison due to the major events that took place in 2018, we had the reduction of BRL3.8 million in cost and expenses of operations excluding construction costs and OEM costs. In addition, the company had a gain of BRL26.5 million in relation to the acquisition of the shares of Branorte, Transleste and Transudeste companies that had recorded a fair value of asset higher than the paid value, accounting for considering the three acquisitions is specifically an advantageous purchase. On the other hand, due to the acquisition of the control of Brasnorte, we have to remeasure the value of this assets in the balance of the company based on the fair value of this acquisition with this, there was a loss related to these new measurements at BRL16.7 million in the net results. The company recorded a gain in the acquisitions of BRL9.8 million in the result of the second quarter 2019 in IFRS,

Lastly, the company has the financial expense of 71.6 million, net 16.9 million higher than that of the second quarter 2018 and this was due to the funds that were raised and the sixth emission of debentures of Taesa in May of BRL1.06 billion and the first emission of debentures that we held related to the project of Janauba in February, 2019 in the amount of 224 million.

We'd like to mention that the good performance of our investment, that was above 106% of the CDL in the first quarter 2019, together with the cash position, which was high contributed to the financial revenues, reducing the impact of the financial expenses for the quarter. And it's important to mention, the net, the gross profit in comparison to the previous quarter as we had already mentioned in the conference call of, the first quarter, the highest levels of inflation that's recorded in April and May were signed that we would have better results in the second quarter and this was confirmed with a growth of 92.6% of our profits. In other words, BRL 150 million in comparison to the first quarter 2019. As it's important to mention that the company in order not to adversely affect the cash and its leverage levels have been excluding the effect of having adopted the CPC 47 for purposes of dividend payout because there's no cash effect in the results.

Therefore, the adjusted net income in the first quarter 2019 amounted to BRL 384.9 million. After the allocation of the legal reserve and the fiscal incentive, the payout distributed on this result added to BRL 345.5 million in other words, BRL 1 per unit and a payout of 89.8%, as we had already mentioned before, and we had already paid BRL 96.7 million between dividends and equity -- return. Return on equity, board approved the maximum distribution of net income distributor -- which is distributable in the amount of BRL 248.7 million. Payment related to this distribution will happen on August 19 based on the share holding position of August 8, 2019.

We are now going to move on to slide four, where we will discuss the regulatory results and this results continues to be very solid. When we look at our, liquidity position, the company started the quarter with BRL 2.2 billion, that means an increase of 82.8% in relation to those first quarter 2019, due especially to the sudden raise with a sixth emission of debentures that happened in may 2019. The net debt was nearly BRL 2.5 billion, an increase of 5.3% in comparison to the first quarter 2019, and this was driven by the payment of that happened in last quarter but was partially offset by the operating cash generation. The ratio, net debt and EBITDA closed the quarter at 1.8 times slightly above what was recorded in the first quarter 2019 that was 1.7 times.

I would like to draw your attention to the excellence results of our funds raised, raising when related to the sixth emission of debentures of Taesa the amount of BRL 1,016 billion for cash reinforcements, in order to pay for the projects, that are underway as well as the recent operations related to the acquisitions we are carrying out, the first series with institutional debenture in the amount of BRL 180 million was rate at 108% CDA -- CDI with A maturity to period of seven years and there's also a demand of nearly three times book of the offer that led to closing the rates at 250 bps from 110.5% to 108% of the CDI. The 2nd series was something really positive because we captured the venture, incentive debenture the amount of EUR 210 million to pay for our projects in Mariana, Miracema and Sant Ana at the cost of --, the six plus 5.50% with the certification of green title reinforcing our social responsibility and the commitment of Taesa has had for social environmental

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topics. We would like to highlight that this emission of debentures was the longest ever recorded in Brazil. The net income of the second quarter 2019 amounted to EUR 360.2 million with an annual drop of 13% which was driven especially by the cuts of the 50% of the RAP of some concessions.

But this is well known by everyone, considering the nature of this concession agreement. The operating costs and expenses stood at 50.8 million, a reduction of 3.5% in the annual comparison, this variation is driven especially by a reduction of expenses with the personnel BRL 2 million due to the change in the capitalization of costs with the personnel in the projects of construction, after the implementation of SAP four/Hana in the second quarter, 2019 and also the correction in the second quarter 2018. Related to the provisioning of funds and the charges for personnel expenses this are all non-recurring events which has a reduction of BRL 1 million with expenses with the sponsorship which was partially offset by an increase of cost with third parties of \$1.2 million to the service of the property around the project. Our EBITDA regulatory stood at BRL309.4 million.

Even with a cut of RAP, our EBITDA margins stood at 85.9%, showing resilience and the operating consistency in a period of drop of income related to these concessions of category 2. It's important to report that even with a EBITDA dropping, which was expected and known the company keeps its financial solidity with the financial rates, which are quite robust and a solid cash position that has allowed us to maintain, the maximum tradition of pay out to our shareholders. The availability rate of our transmission lines stood at 99.89% and the variable portion in the first semester of 2019, amounted to \$2.3 million with a reduction of 84.6% in relation to the same period of 2018. Our focus is to continue searching a level of excellence in the operation and maintenance of lines to deliver a quality service.

And thus contributing to the interconnected system in Brazil. In relation to the progress of Brownfield and Greenfield project, Raul has already mentioned the topics. I would only like to add that the acquisition of the share of Brasnorte as of May 31, when we started to hold the total share of 88.4% of the assets. The company started to consolidate the full result of this concession and it no longer counts for in the equity method, line and share is included in non-controlling of Brasnorte in the net income of Taesa, this amount is not distributable to our shareholders.

On slide five, where we show the macro impact of our results, it's important to mention that the impact of macroeconomic rate of Taesa are very relevant because any percentage point of inflation would significantly impact the revenue of the monetary correction of our contracted assets. At present, the company has 20 concessions, which are indexed to IGPM and 16 concession which are linked to our IPCA Out of which nine considering those 16 concessions that I mentioned are projects under construction and there is a major correlation of our revenues with those rates, but especially IGP-M, as, we can observe on the slide, the three month of that impacted the result of the second quarter '19, the IGP-M The IGPM had an inflation of 2.65%, when compared to the inflation rate recorded of 2.6%, in the second quarter 2019. On the other hand, IPCA for the second quarter 2019, stood at 1.46% in comparison to 0.71% in the second quarter 2018. So the impact of those rates in the monetary correction revenues was positive by \$114.1

million in comparison to BRL 100.7 million positive in the second quarter 2018, an increase of \$13.5 million in the monetary correction revenue in the contractual asset.

I also draw your attention to significant recovery of the correction -- monetary correction in the comparison with an increase of BRL 116.5 million against the first quarter 2019. As I mentioned before, we said that this recovery would actually happen in the previous conference call. Considering the inflation rate that has been recorded in the last two months. It's very clear that the correction of IGP-M and the monetary correction of revenues of Taesa had a very important impact on our results.

Moving on to Slide 6, about the net income in IFRS, we can see on this Slide clearly, as I had mentioned before, the main impacts that influenced the increase in net income in IFRS, in the annual comparisons were the inflation rate both in the monetary correction and in the equity method. An improvement in the variable portion is BRL 8.2 million. And net gain with the acquisition of the shares of Brasnorte, Transleste and Transudeste in the amount of the BRL 9.8 million. And this is my part of the presentation.

I now turn the call over to our Director of New Businesses and Share Management, Jose Ragone, who will discuss our projects from Slide 7.

Daniel Isaza Bonnet {BIO 20691361 <GO>}

From Slide seven. Good morning everyone additionally in summary Raul mentioned before in relation to the nine projects that we have underway, I'm going to share with you the main highlights about the evolution and how they sense. At the end, I will make some comments about this important project, which was not acquired in an auction, but it's an important reinforcement our business that is part of this portfolio.

Now nine -- amounting to nine that were acquired in auction. Mariana is the first one I would like to discuss and in August, we started the last stage of implementation of the undertaking that comprehends the launch of conductors, so the undertaking is in line. It's going to start operation in December this year. Miracema is a concession held 100% via Taesa in the state of Tocantins has a second circuit, the second interconnection of Lajeado to the interconnected Brazilian system.

And this connection of the capital of Palmas in the interconnected system. Physically, from the electrical viewpoint, we have two blocks in this concession and the interconnection of 500 kV in Miracema and the double trip circuit of 230 from Lajeado to Palmas. We are about to end, the launch of cables in 230. And the completion considering the installation of accessories of in the of the 230 line.

For the first fortnight of the this month of August and the completion of the launch of conductors of 500 kV for the end of August. In summary, we are going to complete the delivery of this undertaking according to the agreement with our regulator that was signed in November. So the schedule is very tranquil, it's very comfortable, so that we can deliver all the agreements within the agreed deadline. So the condition is that all the commissioning part has been done with our team from the Technical management.

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So that it will start and operating and our operation and maintenance teams will be operating in a very comfortable way and with total control of this asset that is going to be explored. And in Bahia, we have a project in partnership with Alupar. And we have major headways with the launch of cables, which is the last phase of the project. All the structure has already been completed and we have been working according to the schedule of -- for the stations.

And this will make us very comfortable to understand that we are going to start operating in December, the three, first concession, Maricana, Miracema and EDTE, will start operation according to schedule. And we move on to ESTE, which is also a project with Alupar 500 kV substation, two substations in Espirito Santo. We are going to be granted, the permits that will allow us to start our works this year. We are preparing with our suppliers for the project to structure all the work sites, so that we expect to have the permit granted in the fourth quarter of this year Aimores, Paraguacu, and Janauba, we hold 100% and Aimores and Paraguacu we have a partnership with Citi, and the three confessions comprehended the new interconnection, the new level of the interconnection of North, South East and these are concessions so that we can operate closely with this interconnected system and connect all the regions in the country.

I would say that the three undertakings have been obtained in the same auction. The installation permit were obtained in the same period and the works have started nearly together in the three concessions. It's important to mention that, considering the three concession, we have a concrete prospect of negotiation with the suppliers. So that we are likely to start operating beforehand.

So we are negotiating with the suppliers, already at this time involving all the materials and all the contractors, so that we will start operating before plan. And Ivai is concession in the state of Parana with a partnership also with Citi. As Raul has already mentioned, we have partial permit that will allow us to start. The construction of this undertaking, we expect to implement it with a lot of care, because of the region requires that and this is an undertaking which is in our pipeline and we are sure that we are going to start operating according to schedule.

Sant'Ana was acquired in the last transmission auction in December last year, and I would also like to add to what Raul has already been said, when he talked about the how successful the funds were raised. He said that part of the funds were -- is going to be allocated to Sant' Ana. It's important to mention this, because we have lots of activities, which were focused on the authorities, on the permitting processes, which have been carried out together with Rio Grande do Sul authorities. And we expect that the start of the project will be this year, the beginning of the constructions.

And we have this concrete project to have this, the permit still this year, and family and construction will start in January, according to our plans, a very positive consistent plan and our IR team is going to report to you, when this actually happens. And lastly, we have a project which is quite significant, very important to the company. And also to the transition factor which is the new power of the new concession, which is Novatrans. It's a reinforcement, which is significant considering its technical challenge, in relation to the management and CapEx, we have this commitment.

We require two authorizations by the regulator that is planned to materialize in October this year and also in December this year. We have already completed the most important, the most critical phases of this project, which includes the bypass of the equipment, which are being replaced. So these initiatives that were granted and they were executed in July. So the equipment are out of service and they are being replaced by the new pieces of equipment.

So the schedule is updated and we already have requested the proper agency to start operating again using those new pieces of equipment and one according to schedule and one bringing forward three months considering the authorization. So this reinforce will add an additional RAP of BRL40 million to the company. So generally speaking these were the comments I'd like to make and now, we will start the Q&A session. And if you need any additional information, please contact us, me and our team.

(Question And Answer)

Operator

Thank you. We are now going to start the Q&A session. (Operator Instructions). Catalina McCartney from Credit Suisse, would like to ask a question.

Catalina McCartney

Good morning everyone. Thank you very much for the call. I would like to make some comments on potential assets, that you can consider, we hear a lot about some companies looking for or trying to dispose of some assets in the market. And recently, Eletribras announced, that it will start the process of selling some assets and project.

I would like to know, if the company would be interested in those types of assets and what are other assets that you would consider to add to your portfolio in the future?
Thank you.

Raul Lycurgo Leite {BIO 19066621 <GO>}

Carolina this is Raul. Answering thank you for your question, as we have already mentioned in the past. The Taesa is always interested in some assets provided that it maintains our of financial discipline, return and the addition of value.

When Eletrobras started this process of divestment, we were one of the first companies to say that we would take part in this process provided that it would make sense. In relation to our value generation, when we talk about the M&A, Taesa is always ready, always on the lookout and I would like to mention our IR website. That I mentioned that has been remodeled recently and by the way I would like you to have a look so that you would provide us with a feedback in relation to this new format of the website. So if you look at the website, you are going to see that the footprint and the map is very comprehensive and asset, which is there if anybody would like to observe this asset this would make sense to Taesa.

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So we see 82 players give or take medium and small player that hold BRL 1.4 billion of operational RAP and BRL 4 billion under construction BRL 5.5 million, BRL 5.6 million of Reps divided by 83 players, an average of BRL 68 million for each one of those players. So it's higher ground for an M&A process. So, at all the time, considering the 82 players, so what time during possibility have an M&A So Taesa considering over we have in terms of assets today we have 36. But if we can see the plus 4, we would reach 40 asset.

So it doesn't matter the location where it stands in Brazil, there's always an asset, which is in our frontier. So yes, it does make sense. We are also prepared to a future auction. We can see that the auction that will be held in December is a bit smaller and of course when we compare it to the previous two auctions that were held and were very significant today we are talking about 13 months, but we are ready to grow in Greenfield and in new auctions.

Catalina McCartney

Okay, thank you very much.

Operator

Mr.Rafael from Banco do Brazil, would like to ask a question.

Rafael Dias {BIO 19216212 <GO>}

Good morning. I would like some clarification related to this new power of another trail.

How much has been invested and how much more into December, until you finish this process.

TAE {BIO 2217689 <GO>}

Hafeil, this is -- speaking. We have been authorized by ANEEL, and this two resolution to a CapEx of BRL200 million. Okay, of course we work with a negotiation efficiency and the CapEx related to all those resolution and the new power involves BRL 200 million.

Okay. Thank you.

Operator

(Operator Instructions). We close the Q&A session now, I would like to turn the call over to Mr.Raul Lycurgo for his final considerations.

Raul Lycurgo Leite {BIO 19066621 <GO>}

I would like to thank you all for attending this conference call. If you have any questions, our team is at your service. Thank you all, have a good day you all thank you.

Operator

Taes'a conference call is complete, we thank you for your attendance, and have a good day.

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