

Y 2018 Earnings Call

Company Participants

- Gustavo Estrella, 'Chief Executive Officer'
- YueHui Pan, 'Chief Financial and Investor Relations Officer'

Other Participants

- Analyst
- Bruno Varella

Presentation

Operator

Good morning and thank you for waiting. Welcome to CPFL Energia's Fourth Quarter 2018 Earnings Conference Call. Today with us, are Mr.Gustavo Estrella,CEO of CPFL Energia; Mr.Pan, CFO and Investor Relations Officer of CPFL Energia, and other Officers of the company. The presentation will be available for download at CPFL Energia's Investor Relations website www.cpfl.com.

br/ir. We would like to inform that all participants will be in listen-only mode during the company's presentation. After the company's remarks there will be a Q&A session when further instructions will be given. (Operator Instructions) I would like to remind you that this call is being recorded.

The conference will be held in Portuguese by Mr.Gustavo Estrella, with Simultaneous Interpretation into English, and we will have the participation of Mr.Pan who will be addressing all listeners in English. Before proceeding, we would like to mention that forward-looking statements are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of CPFL Energia's management and information currently available to the company. Forward-looking statements are not guarantees of performance, they involve risks, uncertainties and assumptions as they relate 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 operating factors may also affect the future results of CPFL Energia and may cause results to differ materially from those expressed in such forward-looking statements. Now we would like to turn the conference over to Mr.Estrella. You may proceed.

Gustavo Estrella {BIO 18109709 <GO>}

Good morning everyone and thank you for participating in our conference about the fourth quarter 2018 Result and the full-year of 2018.

Let's go to Slide number 3, with some highlights of 2018 and the first one is the increasing of the consumption of energy in the loaded our concession area 2.7% increased, very much concentrate into the residential and industrial classes, it's important to highlight that this is the second year that we have over 2% increase after negative years. 2015-2016 with 3% to 4% markets drops in 2017, we had this recovery of higher than 2%. I would like to highlight the growth of the EBITDA, 15.9% EBITDA and net income 74.2% a record net income of the company and as well as record EBITDA net debt, so that BRL16.3 billion, leverage reaching 3.05 net debt EBITDA ratio with the drop vis-a-vis 2017. And 2017 the leverage was 3.20 and now we have 3.05 another important highlight in relation of investment that the fourth quarter of '18 investments and the BRL693 million.

And for the year over BRL2 billion closing at BRL2,066 million. We would like to mention the tariff reviews, especially to CPFL Paulista and RGE Sul, and RGE that occurred during the year of '18. By the end of the year on December 31, we grew the concession of RGE and RGE Sul in January 1, 2019 now we have only one concession in the state of Rio Grande do Sul, will the assets of RGE and RGE self-combined. Regarding those are the participation of the company and auctions the renewables auction, we won two projects, the first one is SHPP Cherobim with 28 megawatt installed and then also the Gameleira Wind farm with 69.3 megawatt capacity.

And another important landmark is the start-up of the Boa Vista SHPP that should be started at the beginning of 2020 and we brought it forward over 1 year. So, which start-up in December '18, another important highlight is a participation in the transmission options we had 2 last year. And we won 1 lot in, see new CapEx a BRL102 million and 2 lots in December '18. The first one is June '18, and the CapEx was BRL366 million the first one, and the second BRL349 million.

Together the project start from renewable energy part of volume of transmission, we were talking about an additional CapEx for BRL1.4 billion and at the end of November, we also had the auction four CPFL Renovaveis. contribute [ph] only 99.94% of the shares take rate now holds 99.94% of the shares CPFL Renovaveis. Now going to Slide no 4, we see that besides the highlights of the EBITDA record, EBITDA as I said BRL5.6 billion, and reshaped the distribution per segment of the EBITDA in distribution distribution continues to be the main one with 53% share renovation [ph] 23% and renewable 21%. And lastly, the commercialization services and others with 3%, here we have a highlight of our results, and afterwards Pan will be talking about our results more in detail, we see an important evolution in the distribution segment.

Our EBITDA growing up by 8.7% in the fourth quarter and 34.5% in the full-year of 2018 accumulated comparing to '17, it's important to highlight. The group of the market, that directly affects the evolution of our EBITDA (inaudible) conclusion of tariff review in our distribution companies as well. In the Conventional Generation Segment, here we see basically the 13.4 in the quarter, 6.1 in the year have to do with a long-term contract that we have because here we don't have any new project in the renewable energy we see an effect in the fourth quarter of '18, due to the right of assets of 47 million this is a non-

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recurring defect with impact only on this quarter, so because of that we have a drop of 15.8% to the year we see a drop of 1.1% and we'll be talking in detail but the main reasons for that, is the reduction in volume of wins in commercialization services and others in the market is more general the nature of the commercialization segment, we have here a drop-in margin and the at least should be EBITDA drop in the fourth quarter as well as on the year 75% for the quarter and 26.9% on the full-year. Moving on to Slide 5, we have here a little bit more detail, in the increase of energy consumption and the concession area in the fourth quarter of 2018 specifically the total sales in concession, we have an increase of 1.2%.

And 0.4% in the captive market and 2.8% and a free market. We still have bit of a reflection of that migration from the captive market to the free market. Now looking here, when we breakdown per segment, the increase in the residential segment is 2.2% followed by industry that 0.9% commercial 0.7% and others basically in the others of 0.6%. In the comparison by region and our concessions at where our concessions are located.

We compare CPFL with Brazil, where we see a growth of 1.2% comparing the Brazilian market that increased 1%, in the Southeast CPFL increased 0.6% compared to 1% of the regional -- region as a whole and in the south region 2.6% for CPFL, 2% for the region. Now on the next slide, it is the same information but focusing on the year 2018. So, we can see sales in the concession area of 2.5% even with the effect of the for the same effects of the fourth quarter was here the increase of the captive market of 0.5. And the increase on the free market of 7%, so that's basically due to the migration of clients from the captive market to the free market.

Some of the highlights. Is the increasing the Residential Segment of 2.6% with an impact over the year, that was positive in the consumption due to temperature. Especially in the RGE region with the growth of 3.7%. In the industrial class on the average of the year, we have an increase of 2.8%.

And the highlights our Piratininga with a 4% increased RGE at 3.1% and CPFL Santa Cruz at 7.6%. So for this year, the main highlights of the consumption segment that we have in our concession areas, as we see is the motor vehicle metallurgy and chemical segments being the main classes contributing to this growth in 2018. The comparison by region, we see higher growth in all of them when compared to the country's growth and the comparison with the Southeast and with the Southern region. Now on Slide 7, we have the hydrology scenario and we can see a significant recovery in the reservoir levels throughout the month of March.

With a more pessimistic expectation in the beginning of the year with a decreasing the need level of reservoir. But an important recovery on the average in the month where we historically have a lot of rainfall. This is an important piece of data so this recovery of the reservoir during the month of March and April. We started April, a little bit more pessimistic in terms of rainfall.

So, it's a slightly below average but still at a good level and month of April so bring more recovery in the reservoir levels. So we should close that around between 48% to 49% by

the end of the month. We see here in the (inaudible) PLD, which is connected to the expectation of rainfall increase in the month of March. After the peak in February, where the expectation was a out much less rainfall but, we come now, to these levels.

And 17 to see a curve that is, suffering from an impact with the industry agents, now secondary and power in the beginning of the year, but with an expectation of higher levels in the second half of 2019. Moving on to the next Slide. I will turn over to Mr.Pan and he will talk a little bit about the details of the company. I would now like to turn over to Mr.Pan, and he will give his presentation in English.

YueHui Pan {BIO 20609514 <GO>}

Good morning, and My name is Pan and just here to present the following slide The first one is about revenue and today's earning fourth quarter of 2018, our revenue BRL6.7 billion which is 10% lower than last year and in terms of EBITDA as of fourth quarter of 2018 we have BRL1.3 billion which around BRL700 [ph] million in last year and in terms of net income our fourth quarter income in last year, is BRL673 [ph] million which is BRL323 [ph] million higher than last year that is 35%[ph] as (inaudible) have revenue of a very recent [ph] EBITDA , first about the distribution contribute at around BRL68 million of increase in terms of the marketing tariff we have one of the BRL186 million of increase that we have adjustments is BRL63 million lower than last year and in terms of PMSO, we stay at BRL38 million of the increased amount its PMSO, we have legal and judicial expenses increased by BRL40 million and in terms of the ADA, around BRL40 million. The second part is about the conventional generation, we have benefited BRL7 million increase in compared to the fourth quarter last year, on an average (inaudible) 77 [ph] million, we have price adjustment that will contract contribute to BRL23 million, and I have to have a conventional until BRL17 [ph] million in amortization [ph] its contributed BRL30 million. And the GSF compensation agreement BAESA its BRL11 million contribution and we have kind of a physical Guarantee reduction that's not decreased the our EBITDA by BRL9 million. Turning to the third-party is the conventional and service areas, which (inaudible) BRL62 [ph] million of decrease mainly because of the margin in the commercial like business side BRL140 [ph] million.

And in terms of renewable generation we see I think BRL6 [ph] million that is because of the right path of asset, which is BRL47 [ph] million and also we have lower running in time as par partially offset by the lowest TUSD tax (inaudible) and that is around BRL10 million. And in terms about the net income we see 74% increase compared to last the fourth quarter of 2017, that mainly because we have a decrease in BBI, and from 7% to 6.5% and that contribute around BRL25 million, And now let's turn to Slide 9. This is full year number in terms of the revenue 2018, we have 5.2% increase compared to this 2017, and in EBITDA our 2018 number is BRL5.6 million [ph] which is a historical high and that is the around of 16% [ph] increase compared to 2017 that is BRL773 million. And, net income 2018 we have BRL2.2 billion of net income also the historical high which represents 74% increased around amount of the BRL923 million compared to 2017.

Also In terms of the variation of EBITDA I would like to follow the first distribution slide, we have the for the variation of BRL770 million, that BRL770 million around BRL641 million come from the market at tariff revision we had last year and in the financial (inaudible) the

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side we have the adjustment of BRL141 million, and second part of our conventional generation we have BRL73 million increase compared to 2017. The price adjustment of contracts contribute BRL44 million, and to (inaudible) compensation adjustment BRL44 million. And to the IFRS [ph] confidently and account contribute BRL40 [ph] million and have the reduction as an estimate wind up in the activities slide contribute next to the BRL45 million. In terms of a commercialization of service sector we have around 56 units (ph) that we have 74 million [ph] comes from the commercialization side with margin lost in the service sector we have margin (inaudible) of BRL8 [ph] million And lets got to renewable generation we still next to the BRL70 [ph] million generation compared to 2017 particularly disposal of (inaudible) of statistics and the compensation mechanism and (inaudible) and also the (inaudible) we have around net to effective BRL3 [ph] million.

And have their energy next year BRL30 [ph] million We have a positive of BRL51 million of the increase come from higher prior generation. And in the net income side we have an increase of BRL385 million comes from the financial results that is the reduction of the interest rate CDI contribute BRL360 [ph] million. At our next slide, slide 10. We have a list of the whole group it has have full year fourth quarter of last year we have a historic (inaudible) because of the very low net income over EBITDA we will ensure that the BRL0.03 [ph] (inaudible) and our adjusted EBITDA that in the last (inaudible) not now is BRL5.3 billion and in terms of the gross profit cost is 7.5% in nominal is expected inflation of 2.6% and the breakdown of the gross (inaudible) it has 54% in CDI lease and CDI the PMDF 24% and inflation impact of 7% and a we have the drop of the (inaudible) interest rate financing is 5%.

Gustavo Estrella {BIO 18109709 <GO>}

So I come back on Slide 11. of the Boa Vista SHPP which is new as I said what commercials tied up in the end of last year with an installed capacity of 29.9 megawatt 100% already operational now. Now on slide 12. receive the two projects that we won in the last auction and a minus A-6 of 2018, the first one is the shuttle Cherobim SHPP with an installed capacity of 28 megawatt the projects that we will initiate construction same thing for the Gameleira Wind Complex, 69.3 megawatt of installed capacity, with the project should be structured to begin the construction and the financing.

On Slide 13 we see a transmission auction there were two auctions throughout the year, one in June 28th where we won Lot 9 and the State of Ceara with a contractor RAP of BRL7.9 million and the investment estimated BRL102.2 million. In the December auction we won two lots one in Santa Catarina, with a wrap of BRL26.4 million and then investment estimated in BRL360 [ph] million, and the second lot, lot 11 and (inaudible) RAP of BRL33.9 million and investment estimated of BRL348.9. On Slide 14, we have our CapEx program for 2019 to till 2023. What we have here for the 5 years.

CapEx in the total close to BRL12 billion is a BRL11.938 million , and concentrated in the distribution segment with slightly above BRL10 billion with investment close to BRL2 billion per year in the distribution segment, and since last year we have additional investments in generation over the renewables projects, but also in the transmission segment with the two auctions that we won last year. And here finally on the last Slide just to give you a highlight of the grouping of RGE and RGE Sul, as we were saying and set a program at the

Su, we have a new concession will be RGE The one concession with closer to 3 million clients 2.9, in 381 municipalities, and the capacity for synergies is a lot greater when we have one single concession. This concludes our presentation, and we would like myself and Pan to make us up available for the Q&A session. Thank you.

(Question And Answer)

Operator

Ladies and gentlemen, we will have the Q&A session now, which will be in Portuguese with translation into English. (Operator Instructions) Juliana (inaudible) from (inaudible) Investments

Analyst

hello -this net income over BRL2 million was beyond even the most optimistic analyst I have two questions in fact Mr.Estrella, State grid that they acquired cheaper sell it was BRL25 and at the time they, it was about 24 times high, 2019 it would be close to 12 times high. You believe there is a possibility of a follow-on for instance be below the price that they paid for and this is my first question, and the second question is it (inaudible) let's suppose you do a follow on having a primary offering, how much of the tons of the primary author would be invested. Do you believe this could happen over 2019 what the gains would be and what would be the destination of these funds the other funds?

Gustavo Estrella {BIO 18109709 <GO>}

Thank you for your question.

first regarding the price. We see an important evolution in net income in 2016 we announced the acquisition and it was concluded in 2017 in 2016 and I think some of the company was 102, and now it's almost BRL2.2 billion infact it's a major recovery of our results this affect the price. So if we have a follow-on process of the company. of course this is a talk that is just starting they don't be perspectives and the results of the company the company obtained today in our 2016.

In this case it would be a follow-on issue based on the perspectives of the company obtained today, and not on 2016 we have a very different scenario today compared to 2016. And if we choose a follow-on path we will be telling the story of CPFL today and not 2016. So the scenario is completely different and we are just talking about that and regarded the primary offering and the secondary offer in the case of a follow-on and in the case of a primary offer, we have many different alternatives ahead of us, one of them would be the acquisition of the participation of State Grid in RGE Sul, and the expectation of synergies with the interpreters apologize. However, the sound that we are receiving here in the interpretation booth is totally impossible to translate, we are trying we are doing our best.

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So we have a pipeline of CapEx of BRL24 billion is left. Based on the expectation of a recovery of consumption for the whole of Brazil in general, in generation this opens opportunities for additional investments and we have also the expectation of distribution as well in the sense, passive that could be financed by our possible follow on. if we choose this back. So let me take this opportunity and ask you another question.

The decision about the follow-on when this could happen and do you believe it could be done by the end of May, which would be the 18 months, we could make a very fast decision, and this is on the table this is being discussed today. Between CPFL and State Grid. And so we expect to have a very quick decision about this subject and regarding the deadline we're almost in April already to any of the two alternatives. They will be done or they will be carried out within this framework.

Thank you very much.

Operator

Our next question is from Bruno Varella from Solana Capital.

Bruno Varella

Good morning Estrella, I have two questions the first and Which was Juliana's question. How much time did you have we are in the beginning of April, how long would you estimate for each of the processes those in the MTO or VIPO and what you would have to meet in terms of discussing with us stock exchange in terms of timer that line.

And the second question in this last quarter in particular there have been some increases in the working capital accounts very relevant and ahead considered cash generation of a just around 1.5 and it came to 1.4 and if you consider the basic accounts of EBITDA, CapEx, interest and tax-rates, you get to those numbers. And this includes (inaudible) and negative receivables account and providers, you can invert this 1.5 billion positive to 1.4 negative CDI is clear enough. But I would like to understand the dynamics of the receivables from providers in your working capital.

Gustavo Estrella {BIO 18109709 <GO>}

So first in terms of the deadline.

It's a challenge for us to estimate. Of course in an NPO process this is not 100% controlled by the company, so this process may be longer as we receive questions or discussions, about the process on the table. So if it's a process without any surprises it would be something around two or three months for its conclusion, but this could be much longer depending on how the discussions develop in the market. As for the follow one.

It also depends on a number of factors. So, if we have an expectation that there is an open window, with a regular term that would be the until mid-July for example, for our

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results. We could try to access that window but the market is developing and the window is open and close, very rapidly. So if we chose the path of the follow one, we would be paying attention to that, of course we would not go to market without definition that is very clear that there is a window that allows us to go to market for that operation.

So without being too clear, but there are many factors involved and we and they will be discussed at some point and any of these processes will be addressed with serenity and following all the proper procedures for us to have the best operation possible. As for the working capital. An important point here, the company raised funds in December and at the end of the year, we have made use of the cash available to anticipate some payments so advance some payments that would usually be done in the beginning of the year we made in the month of December, just making use of the cash available at the table. We can't see that affect yes but the month of January.

The payments that would have been made, had been made and with starting or that under working capital in January. So there's no structural change in the working capital flow, that were basically us making the most of an opportunity in the payments that had to be made. Thank you.

Bruno Varela

And as following up on the BMTO [ph] or the re IPO question.

At what stage do you think this decision is at state grid, is this still at the state grid international level or has it been forwarded to the controlling shareholder in China

Gustavo Estrella {BIO 18109709 <GO>}

Considering how close the final deadline is. This subject is a top priority not only for us, but for them as well. So we're at the last stages to have this decision shortly.

Bruno Varela

Excellent.

Thank you.

Operator

(inaudible) with Sharon [ph]

Analyst

Good morning, Estrella. So my questions have mostly been answered already because, they were included in Bruno and Juliana's questions. I would like to ask a question about CapEx.

that about the wind farms, the options that you want, are you going to bring forward the CapEx are you going to bring it forward? To have a more short term return.

Gustavo Estrella {BIO 18109709 <GO>}

This was a very recent fact I didn't say that auctions that we want. We are evaluating this possibility, and of course we are looking at this as an alternative this is to be started depends on many factors the execution of the project and the grid connection. It's a little bit too early for us to say anything about this and of course we will be analyzing this over the next few months to check if this is a real possibility or not thank you very much.

Operator

Our next question will be in English, from Roger (inaudible)

Analyst

(inaudible) thank you. I have two questions the first one its related to be page it's like and what's are the major component of the assets, that were we cannot. Second one is also other things like, what is near major reason for the reduction interest rates, thank you.

Gustavo Estrella {BIO 18109709 <GO>}

Could you please repeat your question?

Analyst

I'm sure.

The first question once are the major components of the assets that were written off in the renewable generation. And the second one, on what is the major reason for the reduction of integrate. Thank you. people again overall if you can speak Chinese you can also, understand Chinese Mandarin.

Okay, I can speak English. So I can use English to ask my over to my question first and then I will repeat my question in Chinese language. My first question is related to the CapEx that was written-off. What are the major component of that asset last year recent loss.

And the second one and its related to the reduction of interest rates. Are what is the major reason for the reduction of interest rates and now I'm use Chinese to repeat my question (Non- English)

Gustavo Estrella {BIO 18109709 <GO>}

About on Slide 8. We have mentioned that write-off of assets, actually and this BRL47 million of write-off assets. Is the we have some no project.

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How to power plant in progress, in (inaudible) level and even and we found out these ask that is not you know little value to continue for the development and according to the company rule. We found very kind of impairment facilities its over the write-off and name of the product is (inaudible) number by negative 3 to this is a project really write-off and in terms of the second question about the decrease of the interest rate. Actually the book rate of interest rate is there So for certain loan of the certain interest rates CDI, which is that this situation in Brazil it's different from (inaudible) 3.5% this is that from the Central Bank of Brazil and because, most of our financing actually 54% [ph] of our financing is CDI so we have this kind of work you have become a decrease of interest rates if you have this kind of damages interest expenses. I'm not sure you heard it it's not really it's (inaudible) coming in Mandarin.

Analyst

Yes, it's clear. It's clear, thank you.

YueHui Pan {BIO 20609514 <GO>}

Thank you very much.

Operator

We would like to conclude the question and answer sessions.

I will turn over to Mr.Gustavo Estrella, for his final considerations.

Gustavo Estrella {BIO 18109709 <GO>}

Once again thank you all for your presence and participation in our results conference call. It's an important moment for the company with record results, and net income of the company's EBITDA and as important as the results, we also have a significant reduction in our indicators, in our improvement, in our quality levels with also broken records in with a decrease of 17.8% compared to 2017. So it's a record results with excellent quality indicators and an aggressive expansion plan for CapEx as we can see was closer to BRL12 [ph] billion of investments.

With a very good results of (inaudible) throughout the last year. So we have asset based that has quality, efficiency, generating results and receive the possibility to bring future growth, so that's our scenario with very positive perspective and outlook for 2019 and the coming years. So once again, thank you. Have a great day.

Operator

CPFL energy is conference call is now over. We thank you all for your participation. Have a good day.

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