

Q1 2017 Earnings Call

Company Participants

- Adriano Rudek de Moura, Chief Financial Officer
- Antonio Sérgio de Souza Guetter, Chief Executive Officer & Director
- Maximiliano Andres Orfali, Chief Executive Officer - Copel Distribuição S.A.
- Sergio Luiz Lamy, Chief Executive Officer - Copel Geração e Transmissão S.A.

Other Participants

- Arlindo Carvalho, Analyst
- Marcelo Sa, Analyst
- Pedro Manfredini, Analyst
- Thiago Silva, Analyst

MANAGEMENT DISCUSSION SECTION

Antonio Sérgio de Souza Guetter

Good morning, everyone. I thank each one of you for participating in our call. I would like to start our talk by saying a few words about the current Brazilian economy scenario, which starts to give some signs of recovery at the beginning of this year.

The electricity charge of the National Interconnected System grew by 3.5% in the first quarter of 2017, (00:38) in part by the improvement in industry confidence that went up only 3% in March 2017, exceeding 90 points, the highest level since May 2014.

These figures are driven by some factors, which seem (00:55) to encourage the economy. Industrial production and domestic consumption. Among them, we could highlight trade balance that had the highest surplus since the beginning of the historical figures, amounting to \$14 billion, vis-à-vis, \$8 billion that we saw in the same period in 2016.

Inflation, measured by the extended CPI, reached the lower level in the last 10 years. And the accumulated ratio in the last 12 months was 4.6% and also, the reduction in the (01:19) rate by 1.5 points in three months only.

In our concession area, it couldn't be different. Up to March, the industrial physical production grew by 4.6% on a year-on-year comparison, driving job generation in Paraná, which closed the quarter with a positive balance of over 16,000 positions being the third state with the highest balance of formal employment in the first quarter of 2017.

The consequence of that can be seen in consumption of the grid market of Copel Distribuição with a growth of 3.5% in the first quarter of this year. We can also see an improvement in delinquency.

We closed the first quarter with a balance of past due between 15 and 360 days, up BRL 257 million, the lowest level since November 2015 and the ratio was maintained at 1.6% slightly higher than Copel's historical levels, whereas the ADA dropped by 40% on a year-on-year comparison amounting to BRL 25 million up to March this year.

Now going to slide number 4, I would like to talk a little bit about recent decisions by Aneel about our asset base related to the RBSE. On May 9, last Tuesday, Aneel ratified the results of the inspection of the appropriation report of assets related to the RBSE and recognized the amount BRL 668 million as the net amount of assets for indemnification purposes on the base date of December 31, 2012.

Based on our best estimate, the company had already recognized in our financial statements of 2016 a historical amount of BRL 580 million and the respective remeasurement of the cash flow represented an asset of almost BRL 1.2 billion of which BRL 810 million impacted our operating revenue at the time.

And with the ratification of the appraisal report, management made the necessary adjustments in the result of the first quarter of this year with a positive impact on the operating revenue by BRL 225 million. It's important to highlight that the effective receipt of this indemnification will occur in the next few years as of July 2017.

Still talking of GET - about GET, we posted BRL 30 million in impairment of the Cutia Wind Farm assets due to the higher CapEx of projects and other assumptions utilized in the tax realized in the fourth quarter of 2016. And another relevant matter that I would like to mention is about the recent approval of dividend payout amounting to BRL 506 million related to the fiscal year of 2016, occurred during the 62nd Annual Shareholders' Meeting on April 28th.

Payments will be made in two installments and the first one will be as interest on equity up to June 30, and the second one as dividends up to 31 December, 2017. The total approved (05:05) corresponds to 50% of the payout referring to the 2016 fiscal year.

Besides during the same meeting, new members of the board and the Fiscal Council were elected for the 2017 to 2019 term, and the composition of these boards (05:21) is 100% compliant to law 13,303, the law of state-owned companies.

Now, going to slide number 5, we can see that the operating revenues increased by 7% in the first quarter of 2017 on a year-on-year comparison amounting to BRL 3.3 billion. And the main reason for this increase was the 33% growth in the revenue from the use of the power grid amounting to BRL 1.1 billion, which reflects the recognition of BRL 225 million related to the remeasurement of the cash flow of the transmission asset related to the RBSE, as I have already mentioned.

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Revenue from the sale to distributors reached BRL 724 million and had a 6% increase, reflecting mainly the higher CCEE revenues due to the higher GSF and also the higher spot market in the period.

Revenue growth was partially offset by the drop of 28% in the sale to final customers. This movement is justified (06:37) by the average reduction of 13% in tariffs in June 2016 due to the result of the 4th Tariff Review Cycle of Copel Distribuição, and also the drop of 11% in the captive market due to the migration of clients to the free market.

The other operating revenues items made up by the telco revenue, gas distribution and others grew by 4%, and reflects mainly the expansion of the client base of Copel Telecom.

On slide number 6, we show the operating costs and expenses that amounted to BRL 2.5 billion in 1Q 2017, amount (07:20) 10% lower from a year-on-year basis. And this is attributed mostly to the 10% drop in the costs with the purchase of energy, which amounted almost BRL 1.1 billion due to the lower acquisition cost of energy coming from Itaipu, and due to the lower exchange rate for the dollar in the period.

The charges for the use of the grid dropped by 36% due to the lower cost with charges for the system services due to the lower thermal dispatch outside the order of merit, and the provision and reversal line dropped by 18%, reflecting mainly the lower volume of provisions for legal claims and also, for allowance for doubtful accounts, ADA, partially offset by the closing of additional impairment, as I said, related to the Cutia Wind Farm.

The manageable costs dropped by 1% in the first quarter of this year, reflect mainly the lower costs with third party services and financial compensation for the use of hybrid resources. Due to the lower generation of hydro energy in the period, partially offset by the 11% increase in personnel, reflecting the adjustment of salaries applied as of October 2016.

Slide 7, shows the EBITDA, which was 87% higher on a year-on-year comparison, totaling BRL 1 billion in the first quarter of 2017, with a 31% margin over the operating revenue. This growth is very well explained by the remeasurement of the cash flow of the transmission assets related to the RBSE by the result of the fourth tariff review cycle of Copel Distribuição, valid as of June 24, 2016, the higher GSF and also higher spot price in the period and the growth of the grid market of Copel Distribuição.

In the first quarter of 2017, Copel GeT cash generation accounted for 71% of the consolidated EBITDA; Copel Distribuição for 19%; Copel Telecom for 3%; and other companies in the group accounted for 7%, with the fact that the main contribution came from (09:54).

On slide 8, we show the Copel consolidated income. In the first quarter, the company posted a net income of BRL 417 million, 270% higher than the BRL 136 million posted in the first quarter of 2016. Analyzing the result of subsidiaries, we can observe that Copel

GeT closed the quarter with a net income of BRL 343 million, Copel Distribuição net income of BRL 71 million, and Copel Telecom, BRL 12 million.

Before starting the question-and-answer, I would like to introduce to you our new COO (sic) [CFO] (10:48) and IRO elected yesterday by our board, Mr. Adriano Rudek de Moura is graduate of Accounting Sciences specializing controllership and finance, 34 years of experience in finances of which 20 years were at Electrolux, global leader in home appliances with the presence in over 150 countries. In the last 14 years, he has Administrative Financial and Investor Relations Officer of Electrolux Latin America.

On behalf of the whole company, I would like to welcome Mr. Moura who joined the company with the mission of helping us to maintain our excellent pace of growth, focus on maximizing value to the company and higher efficiency and austerity, and financial discipline.

Well, these were our highlights. Now, we are available to answer your questions.

Q&A

Operator

Now we would start the question-and-answer session. Mr. Thiago Silva from Santander.

Q - Thiago Silva {BIO 22071118 <GO>}

Good morning, everyone. Thank you for the call. My question has to do with the volume of the Distribuição company. Captive volume was impacted mainly by the migration of customers from captive to the free market, and I would like to know when in your view we could see a stabilization of this movement and the volume for the future?

And the second question related to cost. We see a performance of manageable cost in your release. And I would like to know if you have an internal program, an in-house program, maybe regarding personnel in this regard?

A - Antonio Sérgio de Souza Guetter

I will give the floor to the CEO of Copel Distribuição.

A - Maximiliano Andres Orfali {BIO 20897325 <GO>}

We already see a stabilization of this problem (14:04), and we already started with those process. We expect this to stabilize and maybe reduce. Regarding the cost, we have a very strong program to reduce our cost.

We have a program that should have impact by the end of this year, and we do not intend to hire new people for these jobs that have been vacant. We would like to remind you that last year, we had a reduction of about 200 employees in Distribuição, and we did not replace any of them. So, these jobs are vacant. So, this is a way of taking advantage of our

program and not replace, that is to say to take advantage of our voluntary redundancy program.

Operator

Our next question comes from Mr. Marcelo Sa from UBS. You may proceed.

Q - Marcelo Sa {BIO 16454581 <GO>}

Good morning. Thank you for the call. I would like to know if you can give us an update about your discussions about RBSE and if you have negotiated some solution with Abradee and Aneel? Also, I would like to know if you have some relevant changes in the volume of contracted energy at Copel? And also about Distribuição, the market was higher than most people expected. I would like to know if there was a specific reason this slight - the growth in volume. Do you believe that this is recurrent from now on?

Operator

Could you please repeat your second question? Company asks.

Q - Marcelo Sa {BIO 16454581 <GO>}

I would like to know in generation, if you have reduced the energy contracted amount?

A - Antonio Sérgio de Souza Guetter

Luiz, he is the CEO of GeT.

A - Sergio Luiz Lamy

Good morning. Marcelo. In relation to your question about the RBSE, there are many different things involved and all of them happening simultaneously and dealing with them, with this team, in the judicial arena Abradee is very much proactive. And Copel GeT is also part of Abradee and we're hiring two law firms. In order to track the evolution of this subject and defend (17:46) the interest of transmission company. And regarding this negotiation, this is a process underway and it's a rather interesting one. And this has been ordained by the Ministry of Mines and Energy.

In order to sit at the table and discuss and evaluate all the most important agreement related to this subject (18:25), we have already scheduled a meeting with many players with the participation of Abradee and (18:37) and the Ministry of Mines and Energy trying to find a solution that may please all the parties and we are very bullish about this possibility.

Regarding energy contracts, Copel already - at the end of 2016, had already foreseen the possibility of a low level of GSF (19:18) for this year, especially after the second half. And therefore, we had already taken precautions last year in order to leave reasonable amount of energy, about 15% of the energy contracted. In order to cope with this challenge, we had a plan and what is new is that, we had a part of energy to be delivered

in 2017, and that would be fulfilled in 2017. We're already (19:50) at the beginning of 2017. When the perspective of lower GSF started to become more real, we changed that. So, Copel is very well positioned in order to cope with this difficulty that will happen as of May of reduction of energy because of the low GSF.

And the third question was about the reasons for the strong improvement in the distribution. Maximiliano will be talking about that.

A - Maximiliano Andres Orfali {BIO 20897325 <GO>}

What we can say is that, we had no non-recurring items yet, and we were very much focused on reducing the ADAs and the very good results in the reduction of the allowance for doubtful accounts, ADA. And, we had a reduction of 200 in our head count last year. We are not replacing them. So, this is another reason. So, our personnel cost, we were almost able to absorb the adjustment of the last collective bargaining without having an increase in our payroll. I would say that these two factors ended up contributing for this result. Thank you.

Q - Antonio Sérgio de Souza Guetter

(21:30-21:37).

Good morning, everyone. Thank you for the question. I have a doubt about your debt. Could you give us a strong guidance regarding your leverage up to the end of the year? Is there a level of comfort that you have in mind in order to close the last quarter of 2017? I see that you have 2.3 times. And I would like you to give us some color regarding what could be the optimal level to be achieved?

(22:22) About our leverage, we intend to be under the limit of our 3.5 times, so our forecast is to have this up to the end of the year. And I would like now to turn the floor over to Adriano.

A - Adriano Rudek de Moura {BIO 3590957 <GO>}

Good morning. Well, this is a point of attention of the whole management of the company. We have already published our information also regarding this event and we intend to deal with that. And we have - pretty much have a efficient cost management and also a debt profile. I believe all these events together made Copel have the conditions to keep (23:24-23:33).

Q - Antonio Sérgio de Souza Guetter

But can you give me a figure, (23:35) that is to say, can you give me a number (23:37-23:44).

As I said, (23:45) we want to be below 3.5 and our objective is to stay at 3.3 (23:52).

(23:53-24:32)

(24:33-24:54) so he has a lot of knowledge in these areas and he's very experienced in funding and accounting, and I'm sure that (25:04-25:44)

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Good morning. Good morning, everybody. Adding to (25:49) regarding this year, we've carried out the test. And also, we saw a negative cash generation that's higher (26:03) to the amount that was (26:04) during the first quarter, exactly the amount that we (26:09) as CPLE was brought to our results in the first quarter.

Impairment (26:17) every single year came to the assumption (26:21) and we have to review this since this is something that we monitor on an ongoing basis within the first quarter.

It's the component of the cash (26:30) already realized in December. And that shows the recoverability of the amount of BRL 13 million, that was processed now (26:37).

Thank you.

Operator

Pedro Manfredini from Itaú BBA.

Q - Pedro Manfredini {BIO 21633245 <GO>}

Just an update regarding payments (27:04) could you give us an update about that?

Operator

The interpreter apologizes for the sound being very bad.

A - Antonio Sérgio de Souza Guetter

It's a pleasure to talk to you. Well, there is nothing new in the tranche there because the state is paying the (27:23) again.

Q - Pedro Manfredini {BIO 21633245 <GO>}

Thank you.

Operator

Arlindo Carvalho from Credit Suisse.

Q - Arlindo Carvalho

Good morning. About your investment, we saw that you have BRL 10.7 billion maturing now in the short run, and I would like to know if you intend to (27:56) over and how do you see this matter?

A - Antonio Sérgio de Souza Guetter

Good morning, Arlindo. Felipe (28:06) will answer your question.

Good morning, Arlindo. Good morning, everyone. In fact, we have a relevant amount that will be maturing in the next few months and also 2018, and we have seeing a direct contact with the banks. In fact, institutions are very comfortable in terms of the capacity of rolling over Copel GeT. So, we are very comfortable regarding this, regarding our capacity to extend the maturity, and we have all the right conditions to roll them over in the next few (28:41) months.

Q - Arlindo Carvalho

What is the level of cost that you see for that? Will it be different from (28:49) Can you give us a figure?

A - Antonio Sérgio de Souza Guetter

Well, you can see that in our financial statements because we have already published this information last night. And the most recent operation that we signed was a promissory note at 117% of the CDI.

Q - Arlindo Carvalho

Thank you.

Operator

Pedro Manfredini, Itaú BBA. You may proceed.

Q - Pedro Manfredini {BIO 21633245 <GO>}

...company intend to make a debenture issuance? The interpreter apologizes because the sound is totally distorted here in the translation booth, we apologize.

A - Antonio Sérgio de Souza Guetter

At Copel G&T, we have not issued an infrastructure debenture yet and all the projects that you mentioned (30:23) and the other wind farms et cetera, we are under the umbrella of Copel G&T, and there could be an issuance of infrastructure debentures in the future.

In the few months, when this opportunity arises, we intend to issue also a infrastructure debenture at Copel G&T. We made only one, which was in Copel Telecom, and Copel G&T has a lot of backup energy for this kind of security and we should go towards that in the next operations that we might develop.

Q - Pedro Manfredini {BIO 21633245 <GO>}

Thank you very much, Felipe (31:05).

Operator

If there are no more questions, we would like to give the floor back to Mr. Sérgio de Souza Guetter for his final remarks.

A - Antonio Sérgio de Souza Guetter

We thank you very much for your interest in our call, and I would like to say that I'm very bullish about the results of the first quarter. I believe that the market is showing very fast recovery and a major one. So, once again, I thank you very much for following our call, and I expect to see you all in our next call. Thank you very much and have a good day.

Operator

The first conference call is closed. We thank you for participating and wish you all a very good day. Thank you.

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