

Q3 2014 Earnings Call

Company Participants

- Antonio Sergio de Guetter, Chief Financial Officer
- Lindolfo Zimmer, Chief Executive Officer
- Unidentified Speaker

Other Participants

- Maria Carolina Carneiro, Analyst
- Unidentified Participant

Presentation

Operator

Good afternoon and thank you for waiting. Welcome to Companhia Paranaense de Energia - Copel's Conference Call to present the Third Quarter of 2014 Earnings. We would like to inform you that all participants will be in listen-only mode during this call. And afterwards, we will have a question-and-answer session when further instructions will be given.

(Operator Instructions) Before proceeding, we would like to clarify that forward-looking statements that might be made during this call relating to the business perspectives of Copel, operating and financial targets and projections are beliefs and assumptions of the Company's management as well as information currently available to the Company.

Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions as they refer to future events, and therefore, they depend on circumstances that may or may not occur. Investors should understand that general economic conditions, industry conditions and other operating factors may affect the future performance of Copel and may lead to results that differ materially from those expressed in such forward-looking statements.

We have the participation of Mr. Lindolfo Zimmer, CEO of the Company; Mr. Antonio Sergio Guetter, CFO and Investor Relations Officer; Mr. Marcos Domakoski, Business Management Officer; and Mr. Cezar Monteiro Piraja, Assistant Director of Copel Generation and Transmission. The presentation that will be made by Copel's management may be followed at www.copel.com.br/ir.

Now, we would like to give the floor to Mr. Lindolfo Zimmer, CEO of the Company.

Lindolfo Zimmer {BIO 2132989 <GO>}

Good afternoon. Welcome to the third quarter of 2014 conference call. I would like to thank you very much for participating in this call and I would like to mention that it is always a pleasure to be able to communicate with you. I would like to start this talk, talking a little bit about Copel's anniversary on October 26. We completed 60 years of existence and the celebration came as recognition over 2014. We received many awards among which I would like to highlight the Abradee Award as the best distribution company in the country and the award by the Comision de Integracion Energetica Regional, CIER, the main entity of the electricity sector in this continent and that named Copel as the best energy company [ph] in Latin America. And these were not isolated awards in the last four years. This was the third time that we were appointed by Abradee and by CIER as the best distribution company in Brazil and Latin America, respectively. Besides this valuable recognition of our distribution company, another company of the Group Copel Telecom received the award Highlight of the Year given by Telecom 2014 Yearbook based on the financial economic performance of companies in the telco sector.

Lastly, I would like to mention that Copel ranked fourth in the ranking among the best companies in the South of the country and the rank is called 500 biggest companies in the South by the Amanha magazine and by PricewaterhouseCoopers being classified as the largest company in the state of Parana.

Before giving the floor to our CFO, who will be talking about the figures of the third quarter, I think it's important to remind you that the Brazilian electricity sector has been facing many challenges this year, mainly due to the lower-than-average rainfall in the regions where the largest reservoirs are located and this adverse hydrology had a direct impact on the reduction of the GSF and on the maintenance of the high dispatch by the thermal power plants, and these factors impacted our result which will be detailed afterwards by Guetter to whom I pass the floor now.

Antonio Sergio de Guetter

Thank you very much. And today we are receiving another award from PSU and another award. Okay, so thank you very much for your presence in this call and I would like to start by reminding you that the Board of the Company approved the early payment of R\$381 million in dividend and interest on capital, corresponding to 50% of the adjusted net income of the first half of the year and that will be paid out on the 21st of this month.

About the highlights in the period, we can see on slide number 3 that Copel posted revenues of R\$3.3 billion, 45% higher on a year-on-year basis. And this was driven by the 24.86% adjustment applied to the tariffs of the distribution company and the sale of energy produced by Araucaria gas plant that continued to operate in the third quarter, and in spite of the growth in revenue, the cost with the purchase of energy once again impacted the consolidated results of the company, and considering only the figures for the third quarter, they went up 52% due to the cost related to the thermal contract and the rig contracting of energy in the A minus one and A minus zero auctions, and the impact of the GSF in the period.

And the net income of the third quarter was R\$233 million. Because of that, whereas [ph] EBITDA closed the period at R\$496 million, with a 7% hike. Another highlight is the 5% increase in the captive market of Copel Distribution and the 2.8% reduction in the manageable costs year-to-date.

On the next slide, slide number 4, we give you details about the transfer of the CDE and the ACR account transfers. As we have already said, in other opportunities Copel Distribution is a 100% contracted since May 2014 when we bought 388 megawatts, average megawatt at R\$268 per megawatt hour during the A minus zero auction. And as you can see on slide number 4, the amount received by means of the transfer of the CDE and the ACR accounts resources amount to something around R\$1.2 billion up to September 2014.

Considering only the figures for the third quarter, we received the transfer of R\$96 million, of which R\$94 million refer to the month of May and this amount was only transferred in August. And therefore, it has not been accounted for in Q2 and the situation also affects the transfer of R\$51 million referring to September which was authorized by ANEEL in October and will only be accounted for in Q4.

On slide number 5, we present more details about Araucaria gas plant. And as you know, it has been giving a positive impact on the company's consolidated results. In Q3, it was not different in spite of remaining the two first weeks of September shut down for scheduled maintenance at thermal power plant, dispatched about 796 gigawatt hour in the quarter, giving us a revenue of R\$466 million in the period and a net income of R\$72 million, and EBITDA of R\$103 million. Since February this year, Araucaria TTP generated 2.3 gigawatt hour which gave us revenue of R\$1.5 billion and resulted into an EBITDA of R\$437 million year-to-date. The plant is being dispatched recurrently and due to the lower hydrology the plant should continue operation until the end of this year. It's important to remind you that Araucaria does not have availability contract and it operates towards [ph] the merchant modality and the revenues depend on the operation of the plant and the energy when produced so that the spot market at the spot price, which bounce back to the maximum level in the last few weeks.

On slide numbers 6, we see consolidated results of Copel. We can see that the operating revenue grew by 40% year-to-date, reaching about R\$9.5 billion and the main reasons for this growth were the 26% increase in revenues from sales to end customers because basically of the adjustments of 24.86% applied to tariff practiced by Copel Disco as of June 2014 and the 119% growth in the energy sale to other utilities because of the higher revenue at the CCEE due to the sale of energy of the Araucaria plant and also the energy sold in the spot market by Copel GeT, and that benefited from the high spot price in the period.

Also the availability of the grid, which is made up by the TUSD and TUST revenues with 11% increase due to the growth of 4.9% in the grid market and also the start-up of new assets, and also the other revenues that include revenues from construction, telco, gas and others, reaching R\$1.5 billion, a 12% growth on a year-on-year basis, driven mostly by the growth in our construction revenues which reached R\$972 million this year and the accounting record of higher investments in distribution and transmission, and also the

growth of 19% in revenues from telecommunications that reached R\$122 million in the period.

On slide number 7, we give you details about the operating expenses and costs for the first nine months of 2014 that amounted to R\$8.2 billion, 45% higher on a year-on-year basis. And the main reason for the increase in costs is the 48% hike in expenditures with electric energy bought for resale, R\$3.5 billion, already considering the compensation of R\$1.2 billion of CDE and of the ACR accounts that were accounted for in the period.

Costs with charges for the use of the grid grew by 51%, basically due to the comparison basis effect, up to September 2013 there was a transfer of resources from CDE amounting to R\$320 million to compensate costs with the charges for the system service charges or SSC related to the dispatch of TTPs outside the order of merit at the beginning of 2013. The cost with the purchase of gas rose significantly and this is a consequence of the Araucaria power plant operation because Compagas buys the fuel in order to supply to the plant.

On the other hand, personnel costs including the social security benefits dropped by 3% because of the efforts made by the company to reduce other manageable costs.

Slide number 8 shows that the consolidated EBITDA grew by 16% up to September this year, amounting to R\$1.8 billion, with a 19% margin over the operating revenue. Cash generation of Copel GeT accounted for 81% of the consolidated EBITDA and Copel Telecom represented 5% and the other companies of the Group 14%. With relation to the margin, Copel GeT reached 64% and Copel Telecom 55%. Copel Distribution delivered a negative EBITDA of R\$158 million up to September, driven once again by the higher cost with the purchase of energy as we have already explained. Nevertheless, when we consider only the third quarter, the EBITDA is positive, mainly due to the extraordinary revenues coming from the settlement of the surplus energy in the spot market.

On slide number 9, we present Copel's consolidated net income which exceeded R\$1 billion in the first nine months of 2014, 15% higher on a year-on-year comparison. Analyzing the result of our subsidiaries, we can see that Copel GeT closed the period with R\$969 million in net income, 35% higher on a year-on-year basis. Copel Telecom reached R\$43 million as net income corresponding to a 21% increase, also on a year-on-year basis. Copel Distribution posted a loss of R\$178 million up to September, driven by the high costs with the purchase of energy. However, for the same reason that has already been mentioned in the previous slide, when we analyze only the results of the third quarter, the net income is positive by R\$51 million. Very well; these were the main highlights about the results of Copel. But before closing my remarks, I would like to say a few words about the start-up of transmission assets and new investments in renewable energy that you can see on slide number 10.

The transmission segment -- in this transmission segment, we started up recently Costa Oeste and TSBE, Transmissora Sul Brasileira de Energia or TSBE project where we hold a stake of 51% and 20% respectively and that's jointly are already giving as an additional RAP of R\$17 million. With that, the total RAP of the transmission assets of Copel is R\$209

million, an amount that considered what is posted as revenue and as equity income as well.

According to the same criteria, we should add an additional R\$177 million in RAP over 2015. In the segment of renewable energies, on October 31, we participated in the 6th Energy Reserve Auction and we sold 71.2 megawatts average of energy of the Cutia complex at the ceiling price R\$144 per megawatt hour and with that we expanded our position in the wind energy segment and we already have 526 megawatts in installed capacity already being commercialized.

Overall, these were the highlights of Copel's results, but we cannot close this call without making some remarks about the concerns related to the critical situation of the reservoirs and the changes that are being discussed by these sector or for the sector about the reservoirs. In spite of the fact that we are in the south of Brazil where the situation is rather normal, we are affected by the low hydrology of the system as a whole and we have been following very closely the evolution of the reservoirs and although we are still at the beginning of the wet period, it is also possible -- already possible to say that 2015 will be very difficult such as in the case of 2014 under the viewpoint of hydro energy.

This means another year of high thermal dispatch and expensive energy. If this were not enough, we are also going through a crucial moment in the definition of very important items such as the parameters for the fourth cycle of the distribution company, the implementation of the tariff banners, the changes in the spot price, among others. In this adverse scenario, I would like to reiterate our commitment of acting in a conservative fashion, always defending the interest of the company and of shareholders. Now, we would like to open for questions.

Questions And Answers

Operator

(Operator Instructions).

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

This is Maria Carolina Carneiro from Santander. Good afternoon everyone. Can you give us an update about the energy balance that is to say the energy that you have available for sale or for hydrological hedging for 2015, 2016? Has there been any change regarding the previous quarter? This is my first question.

And my second question has to do with the cost performance. So, we see a very interesting work being done by you on your PMSO line item, I would like to know if the cost level that you reached this quarter will be recurrent or do you believe that you still have an additional potential to further reduce your PMSO mainly in distribution? Thank you.

A - Lindolfo Zimmer {BIO 2132989 <GO>}

Maria Carolina, this is Lindolfo. Thank you for participating in our call. The first part has to do with our availability for next year and for 2016. It's up [ph] about 10%. We are talking about 200 average megawatts, which is our potential or availability. In 2016, it will be slightly higher, 22%, but these are the figures that we have today.

Regarding your second question, the evolution of our cost reduction program. It's happening as planned. This plan was established to go up to 2025, R\$100 million reduction this year, last year as well. And this continues on, the costs continue to go down. And it is very clear in our minds that the endeavors by the company should be on an ongoing basis and with productivity gains, efficiency gains and this is a very important part of the company.

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

Thank you very much. If you allow me, another question. Regarding the renewal concession for Copel's discount [ph], do you have any update coming from the Ministry or from ANEEL of when this process should be resumed?

A - Lindolfo Zimmer {BIO 2132989 <GO>}

Carolina, we are not concerned with the renewal of our discounts, concessions. First, because we already have a plan that goes up to 2025 and that's fully being complied with and the plan has already been approved by ANEEL. So, there is no concern whatsoever in our minds about that. And secondly, or first, I would say the concern regarding clients and the delivery to consumers, our company has been systematically appointed as one of the best companies in the country in terms of delivering to clients. So, we have quality, we deliver quality and we also comply with the economic and financial requirements. So, we have no concern whatsoever regarding the renewal of these concessions.

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

Thank you.

Operator

Giuliano [ph] from Itau BBA.

Q - Unidentified Participant

Good afternoon, everyone. I have three questions. The first one along the same lines as Carol's question, do you believe that the renewal of this distribution company contract could have some burden, a lower WACC for instance, regulatory WACC? Secondly, how do you see the next A minus 5 auction, will you be participating, which project is the most interesting as far as you are concerned? And the third for the next rain period for 2015, you said the hydrology is very bad. And do you work with a possible scenario of rationing and how do you see the level of the reservoirs for the end of the wet period and what about the spot price?

A - Lindolfo Zimmer {BIO 2132989 <GO>}

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Giuliano, thank you for participating. Regarding the renewal, we do not believe there will be any new contingency for renewal. Of course, each company is different in relation to performance, in relation to results, but our company is very comfortable regarding this aspect. Regarding the A minus 5, the next auction we are looking at that, with all our attention we might come and participate.

We intend to be present and also recover assets that as the terms of the concessions mature, the ones that we have, we wish to replace them and mainly in terms of wind energy. And the other question has to do with rationing. I would say it's very difficult to express any viewpoint because we depend on the hydrology, we depend of rainfall on factors that fall totally outside our control.

Of course, the implementation of the tariff banner is that we will start in January, we'll bring a lot of discipline to the market and we will see the market having a reaction proportional to the penalty that will be imposed depending on the color of the banner and this will be a kind of rationalization, so to say or a more rational use of energy I would say. And one additional need besides that, that is dealt with by the banner, it will depend on the hydrology and the growth of the economy itself, the GDP and so on and so forth, because if you have a low GDP, a low development, so the needs will be lower and rationing would be a very severe measure to be taken and it ends up penalizing everybody, it penalizes society as a whole. And as a citizen, I wouldn't like to rationing.

Q - Unidentified Participant

What about the ceiling price, ceiling spot price?

A - Lindolfo Zimmer {BIO 2132989 <GO>}

This is being discussed and ANEEL will come to a conclusion next week, 388 was the ceiling defined by means of studies carried out by the regulator. I don't know whether this will prevail or not. It doesn't really matter as far as we are concerned because what we have in terms of availability is Araucaria and it's higher and it dispatches normally not based on the order of merit, but because of the energy needs of the system in the South region.

Of course, the 822 spot price brings us stronger results, but we do not believe this will hinder us.

Q - Unidentified Participant

Okay, thank you. Thank you.

Operator

(inaudible) from UBS.

Q - Unidentified Participant

Bloomberg Transcript

Good afternoon, thank you for the call. I have two questions. Is there a date for you to deliver the RBS report to ANEEL and what is the return that you intend to have from your wind energy sales?

A - Unidentified Speaker

This is Philip [ph]. About RBSE, the deadline to deliver the report and deliver the figures is March 2015, to hand this over to ANEEL. And regarding the profitability of the wind energy, I will give the floor to my colleague.

A - Lindolfo Zimmer {BIO 2132989 <GO>}

We are -- these projects regarding wind energy receive our full attention. All the wind farms that we are starting up and those that are already operating already deliver very good returns, with two digits rates, and so on and so forth. Wind energy represents a major part of our revenues already and I would say that these are the best deals that we have been doing, the generation of wind energy and the application of these assets. We are evaluating with due care the participation in wind energy and most of our projects are still in the maturation phase. Thank you.

Operator

(Operator Instructions) And there are no more questions, we would like to give the floor back to the company for closing remarks.

A - Lindolfo Zimmer {BIO 2132989 <GO>}

In order to finalize, once again, I would like to thank you very much for participating in our call. It is always a great pleasure for us to present our results and talk about the outlook for our company. Thank you very much and wish you a very good afternoon.

Operator

Copel's conference call is closed. We thank you for participating and wish you all a very good afternoon.

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