

Q2 2017 Earnings Call

Company Participants

- Cristiano Prado Grangeiro, Unknown
- Marco Ant nio Resende Faria, CEO, Business Development Officer, Member of Executive Board & Technical Officer
- Marcus Pereira Auc lio, CFO, Member of Executive Board & IR Officer
- Unidentified Speaker, Unknown

Other Participants

- Marcelo S , Associate Director and Analyst
- Unidentified Participant, Analyst

Presentation

Operator

Good afternoon, ladies and gentlemen. Welcome to Second Quarter 2017 results presentation conference call for Taesa. We would like to inform all the participants that the presentation is available for download at www.taesa.com.br/ri and on the platform in the IP.

(Operator Instructions)

Before proceeding, we would like to clarify that any statements that may be made during this conference call regarding the company's business prospects, projections and operational and financial targets constitute the beliefs and premises of the Board of Directors of Taesa as well as on information currently available to the company.

Forward-looking statements are not a guarantee of performance. And they involve risks, uncertainty and assumptions. These refer to future events that, therefore, depend on circumstances that may or may not occur.

Investors should understand that general economic conditions, industry conditions and other operational factors may affect the company's future results and may lead to results that differ materially from those expressed in these forward-looking statements.

I'd now like to give the floor to Marco Ant nio Resende Faria, who will begin the presentation. Sir, you can proceed.

Marco Ant nio Resende Faria {BIO 16679297 <GO>}

Good afternoon, everyone. It's a pleasure to be here with you. And thank you for participating in our teleconference for the Second Quarter of 2017.

As you can see in our presentation, Taesa has showing consistently its financial discipline and its strong operational cash generation, which positions us as an important player in the transmission sector and the player able to capture opportunities of growth in the next period -- in the next years. It's important to remember that between 2016 and the beginning of this year, we won 6 batches in auctions that will add over BRL 520 million in RAP, totaling an investment of BRL 2.0 billion.

As I have mentioned in the last conference call, we have structured ourselves to deliver all these projects in timely deadlines, low cost and high quality. We have a very well-prepared team and a seasoned team that has all the knowhow necessary for all the further stages of our development.

I'd like to highlight again that the participation and integration of all the teams and areas of Taesa is our differential. In addition, we have been diligent and very critical in the analysis of the auction. And we'll keep this discipline, aiming at offering proposals to the batches that really add value to our business.

Both in greenfield and M&A, we have identified currently the market's several opportunities, all of which will be studied carefully in the short and medium term. We have deeply studied all the cases so that, at the right time, we are able to take advantage of them, generating the value that we want for Taesa.

We are at a very good moment to capture these opportunities, considering the room that we have in our statements and our sound ability for cash generation. Therefore, this has been a major focus to achieve growth with transmission assets that add value to Taesa.

Before giving the floor to our financial director and RI (sic) (IR) officer, Marcus Auc lio, I'd like to highlight how ISA went through the block of control under Taesa, which occurred in June. We believe that with ISA's sound experience -- shareholder in energy transmission, we will consolidate our position in the sector, creating greater opportunities for growth and value generation for our shareholders.

I now give the floor to our financial and IR officer, Mr. Marcus Auc lio.

Marcus Pereira Auc lio

Thank you, Marco. Good afternoon, everyone. I will now go to Slide 3. And we have the highlights for the Second Quarter of 2017.

Looking at the IFRS results, the main impact was the drop in the macroeconomic levels of inflation, IGP-M and IPCA, which reflected in the monetary correction of the financial assets which, affected directly, net income would have dropped by 47.7% year-on-year. Therefore, even with the efforts in the rigorous control of costs, one of our main pillars.

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And with improvement of the financial results, reduction of taxes and the fall of inflation in taxes, drastically, the net income for the period was dropped by 65.2% year-on-year.

But we believe IGP-M, for example, had a significant difference in the period. In the Second Quarter of 2017, it had a 2% deflation against an accumulated inflation of 1.66% in the Second Quarter of 2016. In the regulatory results, we have presented a strong operational cash generation EBITDA. Consolidated EBITDA was at BRL 385 million for the quarter, almost 13% better than the Second Quarter of last year. And this resulted growth of 10.5% in net income and a reduction of 5.2% in cost and expenses. And with this, the EBITDA margin reached almost 89%.

In this quarter, we continue with the level of 1.7x net debt to EBITDA. And as our President mentioned before, our low leverage levels puts us in an excellent position to capture opportunities both in greenfields and in brownfields. And for this, we are prepared and looking carefully to the potential assets of the market.

I'll now give the floor to Christian Prado, our new RI (sic) (IR) Manager, who will present the results for the Second Quarter of Taesa.

Cristiano Prado Grangeiro {BIO 20213891 <GO>}

Thank you, Marcus. And good afternoon, everyone. We're now moving on to Slide 4, where we can -- we are looking at IFRS net income. It's a positive (reserve). But the main impact is the line of correction of the financial assets, which dropped BRL 572 million year-on-year. This great negative variation is explained by the significant difference in the macroeconomic indexes, IGP-M and IPCA, recorded in these growth periods.

In the Second Quarter of 2017, IGP-M presented an accumulated deflation of 2% and IPCA accumulated 0.7% of inflation. At the same period in 2016, IGP-M was 1.66% and IPCA 1.83%.

The OM revenue increased by BRL 13.2 million, 10% -- 10.7% higher year-on-year. Following closely, the readjustment of the RAP at the cycle 2016-2016 (sic) (2016-2017) and IGP-M, 11.1%; and IPCA, 9.3%.

The revenue for the financial assets reduced naturally because of the payment of the financial assets in the last 12 months. The variable (possible) reduced 11.2% because of an occurrence of last year in May. (inaudible) net income IFRS totaled BRL 169.3 million in the quarter, corresponding to a drop year-on-year 47.7%.

Going on to Slide 5, where we have the costs, the expenses, depreciation and payments. We continued with a total focus in operational efficiency and cost control.

The drop of BRL 2.9 million in the personnel line compared to the Second Quarter of 2016 was explained by the capitalization across with personnel in the projects of maintenance, reinforcement, improvements, which was offset with the collective agreement.

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We have the material line that cannibalizes O&M and building and presented a growth by BRL 2.0 million, especially in the transactions of Miracema, Janaína, Novatrans, ETEO and STE. The expenses with third-party services increased by BRL 2. million (sic) (BRL 2.5 million). And increased by 23.6% year-on-year due to expenses in cleaning and expenses with consulting firms.

In other expenses, the drop is explained by the provision of civil compensation that took place in the Second Quarter. As a result, the costs, expenses, depreciation and amortization were almost stable year-on-year, totaling BRL 55.4 million in the quarter.

On Slide 6, where you can see the financial results, we can see the impact of the drop in IPCA and CDI in the last month. Even with this drop, the financial interim of BRL 4.9 million higher, which represents a growth of 36.2% year-on-year was a result basically of an average cash volume, which was higher in this quarter.

The drop in interest rates is explained by the reduction of gross debt in addition to the drop in CDI and IPCA levels for the period, considering that they are the main indexes of our debt.

The variation registered a fall of BRL 24.5 million also because of the drop in IPCA. In other financial expenses, the increase is due mainly to the variation of the market of debt 4131. As a result, financial results improved by 46.9% year-on-year, closing the quarter at BRL 53.1 million.

Moving on to Slide 7. The results for patrimonial equivalent, which is the concession in which Taesa has participation also suffered a drop in the macroeconomic level, especially the concessions in TBE.

Lastly, considering the fall in taxes, as a result of a lower result in IFRS, the net income for the Second Quarter was BRL 72 million. Please note, by the bottom half chart that this drop in 65.2% in income is explained by the drop of the inflation indexes that affected net revenue and patrimonial equity even if we had lower cost, lower financial expenses and lower taxes.

Moving on to Slide 8. We have a sound regulatory result. The operational income -- net operational income, consolidated for Taesa, totaled 43 -- BRL 433.2 million, an increase by 10% year-on-year. If we take into account the participation of the companies invested, the total of net revenue is BRL 553.1 million.

The annual variation is due basically to the adjustments that happened yearly for RAP, which took place in July of last year. ETEO and ECTE concessions had a reduction of 50% in RAP and some reinforcements went through tariff review, which gave an annual variation of 7.4%, a percentage which is lower than the inflation indexes in the cycle, 11.1% for IGP-M and 9.3% for IPCA. These effects were offset by a drop in PV, totaling BRL 11 million, which resulted an increase by 10.5% of consolidated net income against the Second Quarter of 2016.

On Slide 9, we have the regulatory EBITDA performance, which is a key indicator to show our capacity for operational cash generation. It is possible to see on the slide the increase of net income associated to the cost and expenses led to an increase of 13% of EBITDA compared to the Second Quarter 2016 totaling BRL 385 million in this quarter. As a result, the EBITDA margin totaled almost 89%.

If we look at managerial EBITDA, which includes proportional EBITDA for the invested company, the number hits BRL 495 million in the quarter, a margin of 89.5%. The highest and biggest contribution came through the TBE group, which added BRL 103.7 million in EBITDA with a (sound) margin of 92.5%.

This performance confirms the importance that we will grow through participation. It is important to highlight here that our revenue is adjusted yearly by the IPCA and IGP-M, the latter with a greater role, reflects this mix in the collective agreement of the employees of the company. And the personnel cost represents 65% of our OpEx.

In addition, the cost with third-party services we tried to reflect this mix in the agreement were the same indexes that adjust the RAP. And that is how we can minimize the impacts of inflation in our operational margin.

Moving on to Slide #10. We have the profile of the debt. Gross debt totaled BRL 3.4 billion at the end of the Second Quarter of this year with a payout -- with an amortization profile presented on the bottom half of the slide. 71% of the debt is with long term with a period of 2.5 years.

It was mentioned that we reduced 17 (new) % of net debt year-on-year totaling BRL 2.7 billion at the end of the quarter. The relationship between net debt and EBITDA was 1.7x against 2.6x the amount recorded in the same period of last year. This reduction shows how quick the company is able to deleverage, which is an important differential for a company that looks for growth opportunities.

I'd also like to highlight that besides having BRL 900 million debt that will be payable this year, rolling out from that is less than BRL 200 million, which puts us in a very comfortable position in our obligations.

And we will now end this presentation. And we are available for questions and answers. Thank you, all.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from (inaudible) from (Banco DiversiÃ³).

Q - Unidentified Participant

Taesá has always stood out for M&A operations. In addition to what the market has been doing, are you -- can you notice any kind of movement? What's the pipeline today for the acquisition of new assets, seeing that you have new projects to develop? And maybe how can this happen and affect other auctions? In addition to carrying on with current operations, how do you see the future? Could you elaborate a little?

A - Unidentified Speaker

Thank you for your question. It was very low. But if I understood you well, you are asking if we are looking at M&A opportunities. And we are looking at all the opportunities and everything that we have available so we can study it carefully. And we can see the investments and to carry out all the possible analyses that are needed and make this available to the market as soon as we can. But what we have before us in addition to the opportunities with (natural gas) we're still waiting. We're looking for the recovery -- the digital recovery procedure that's going on and all the information that we have available. And we'll be accepting and -- in order to make their proposal give added value to Taesá, as I said, in the presentation.

Q - Unidentified Participant

In addition, of the (digital) resolution and investment in (natural gas), are there any other (sat) assets that you are looking to -- into more closely? Basically, that's my question.

A - Unidentified Speaker

As I've said on other occasions, we are always ready to assess every opportunity. And everything that comes up, we will look into. This is what I can tell you at this time.

Operator

Our next question comes from Mr. (Andrés Sampayo) from Banco (Santander.)

Q - Unidentified Participant

I'd like to know more about the tax incentives. What can you tell us about the negotiations in this area? We've seen an evolution with Patesa in this quarter. Do you have any news on the other units?

A - Marcus Pereira Auc lio

Marcus Auc lio, (Andrés), actually we have viewed it. There is a concession that has won the incentive -- that was awarded the incentive. It was (inaudible). And we are now entering with the procedure of -- to renew this at SUDAM. And our impression is that all the material that we have and that we have occurred in the past, we still have time. It's -- this is approved at SUDAM and then to take this to the Internal Revenue Service. And since we have a period to do this until April and we want to (interact) for the entire year, our expectation is that we will take advantage of the (inaudible) fiscal incentive for the 2017 fiscal year.

Operator

Our next question comes from Fernando Zorzi from UBS.

Q - Marcelo SÃ;

This is Marcelo SÃ;, actually. Can I have a question on dividends. And this calls attention, which is the drop because of the IGP-M? If we try to make a forecast for the future, can I imagine that Taesa will drop below 8% for 2017 because of the IGP-M effect?

A - Unidentified Speaker

Marcelo, inflation is much lower in this connector in this quarter and, therefore, the market in the IGP-M projections than the IPCA projections and the estimates today to -- for the end of the year are much lower. In our assessment so far, we will continue to monitor what's going on with the IPCA and IGP-M. And our policy is that as soon as we record this, we'll continue to pay out the maximum amount of dividend. For the projection of the year, things will depend on what goes on in terms of inflation. And part of our concessions are attached to the IGP-M rate and the other part to the IPCA so really have to wait and see and what actually materializes in terms of inflation for 2017.

Operator

(Operator Instructions) Since there are no further questions, I'd like to give the floor to Marco AntÃnio for his final remarks. Sir, the floor is yours.

A - Marco AntÃnio Resende Faria {BIO 16679297 <GO>}

Well I'd like to thank, again, everyone for being here. Thank you for the questions and to say that our IR team is available to all of you. Thank you. Thank you.

Operator

The Second Quarter conference call for Taesa is now closed. Please disconnect now.

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