

## Q3 2019 Earnings Call

### Company Participants

- Andre Luis Almeida, Director of Accounting
- Henrique Freire, Vice President of Finance
- Miguel Setas, Chief Executive Officer
- Unidentified Speaker

### Other Participants

- Fernando Errazuriz, Analyst
- Maria Carolina Carneiro, Analyst

### Presentation

#### Operator

(Starting Abruptly) at the release of the Company's results.

Before continuing, EDP Energias do Brasil explains that statements during -- made during this conference call relative to the Company's business prospects, operational and financial goals and projections pertaining to its potential growth, are forecasts based on the expectations of the management regarding the future of EDP Energias do Brasil. Forward-looking statements depend on the economic scenario of the country, that the performance and regulation of the electric industry and other variables and therefore, are subject to change.

Now I would like to give the conference over to Mr. Miguel Setas, CEO and IRO of EDP Energias do Brasil, who are going to start our conference call. Please Mr. Setas, you may start.

#### Miguel Setas

Thank you very much. Good morning to everyone. So we are going to have our conference call to release the results of the third quarter of 2018 [ph] where I have Henrique Freire and other executive officers, VP who will later on be available to answer any questions you may have.

I would like to start by talking about the highlight. And then we have the presentation, and this quarter is very important for us for two main reasons. The first, because of the completion of tariff review in Sao Paulo and Espirito Santo, and these tariff review that I'm going to be showing to you, have had very good results, very significant results at the end

of this tariff cycle that has just ended on October the 23rd in Sao Paulo and in August in the case of Espirito Santo.

So the first highlight of the quarter is the completion of the tariff review. The second highlight is a significant growth in the conditions that are necessary for our investment and transmission. And I can tell you, and announced that we have all installation, licenses have already been issued, and for this reason, we have the prospect that we will be able to advance towards [ph] we have declared and as a result of our participation in auctions.

That said, we are going to go to page 3 to tell you all in a summarized way, the main impacts of the tariff review, of the two tariff review that we have completed recently. So in this period, there was an investment of BRL2 billion in -- if we bring the two companies together. And then in Sao Paulo, we had a net increase of the QRR of 23%, Espirito Santo, 28%. So on average about 36% of the bet RAB. So this is associated to an increase in the regulatory EBITDA of the two companies. So it's close to BRL1 billion for both companies, which corresponded to a 31% increase as compared to previous tariff cycles. It's also important to mention that the regulatory haircut will be reviewed. It's lower than 0.5%.

In terms of the asset that has been booked or recognized for the two reviews, in the case of Sao Paulo. 0.3% -- 0.6% for Sao Paulo. And so we are very happy with that. And because the Company has a history when these numbers used to be higher two cycles before, we had two-digit haircuts. And therefore, the implementation of zero haircut process along the past two years has provided full results. Now according to what we know to our best efforts, this is the lowest level in the Brazilian energy industry. So we are very happy to see this. And the legitimate -- the investments that the Company has made in this tariff review cycle of BRL2 million in constructions, and this optimizes the allocation of the Company's capital. Obviously, these reviews have also had some increases that are related to our performance.

So now, I would like you to turn to page 4 to see our losses. So in this case, commercial losses -- low-voltage commercial losses that the Company has had over the past few years, these curves, you can see the red curve, identifies as a trajectory of reduction of losses in distribution companies and not just lead the regulation agency in this tariff review cycle. So once again, defined trajectory, as our regulatory target that imposes a gradual reduction in losses.

So the targets are ambitious. But overall, they are compatible with what the Company aims for the next tariff cycle, and the objective is to continue to be below regulation losses. And it is perfectly acceptable and possible for the upcoming tariff review cycle. And therefore, this is a point of attention, to us versus within the level of our objectives or goals.

On page number 5, there is an overview of the market, distribution and market evolution. So the market in terms of accumulated numbers is above the average of Brazil. So our growth is 2.3% in our numbers, year-to-date numbers. So slightly more expressive considering the temperature in Espirito Santo, 4% or 5% and Sao Paulo slightly lower 1% or

2%. And therefore, we think that the trajectory of volumes for both distribution companies above the Brazilian average.

As to losses, you can see our track record. We showed losses in low voltage. So you can see here on the chart that we have a gradual reduction track record of 0.38% in Sao Paulo and 0.07% [ph] in Espirito Santo. In the case of Espirito Santo, we should mention in our current business to draw your attention that in agreement with the new accounting of losses, we are no longer including the losses of Santa Maria and its indicated that you can see on the page, if we compare the losses with the same effect, so that we may identify the trajectory with equivalent situations for both quarters, that's why we have excluded.

Now on page 6, you can see our strategy for integrated hydrological risk management. As you can see, we are 5% below in terms of the first nine months of the year in terms of margin, and this is associated to our contracts of hydro power. And therefore, in a scenario where hydrological risk is marginally negative and the mitigators that we have in terms of uncontracted energy and the commercialization, are offsetting the hydrological risk.

What I think it's important to demonstrate is that, obviously, we have an energy scenario today, which is quite different from what we had a year ago. And today, we have BRL200 per megawatt hour. Last year it was BRL400 per megawatt hour, which means that the hydrological risk is smaller than we had last year. And also the mitigators play a role that is not so relevant as they did in 2018 and 2017.

Now, going to page 7, we expect to have BRL250 -- BRL300 per megawatt hour as we have today. So in Q4, we think this is going to be more significant, so that the balance of the year is -- demonstrate the effective management that we have had over the past two years of hydrological risk. Therefore, last half of the year, I'll explain to you -- and therefore, it's very clear to us that this strategy obviously, has the objective of providing symmetry, which is the main -- and the main downside in terms of hydrological risk in our financials. And therefore, in a scenario when that downside is not so significant, we adopt this procedure.

Now on page 8, you have a better vision of transmission. As I said, two major events in this event tariff review, and the licensing of transmission companies that -- of the lots that we contracted in 2017 and 2018. So our CapEx is 37% of the total. This is the CapEx that has been executed or disbursed. For the lots with the highlights were Lot 11 and we already have 78% of the construction works complete. And this is even more optimistic than we initially regarded in the auctions when we contracted this lot.

And you can see on Lot 7, 16% of construction complete. Lot 18, we had license. Lot 21, we have the license issued yesterday -- just yesterday. We have 29% of the lot already disbursed with 43% of the construction works completed. This is just to demonstrate that our expectation in terms of execution of transmission is absolutely in line with our expectation.

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On page 9, you can see our licensing processes, that we have obtained all licenses before scheduled -- initially scheduled the regulation agency had -- that the regulation agency had defined. So this advance, part of it is recent, is already reflected here in this chart. And then we move on to the construction of the lots and this is a new phase. Obviously, as you are aware, we have announced this very frequently. And we have calendar with schedules that are even more ambitious, and then the calendars that we have established with the regulation agency for our transmission projects.

On page 10, you can see the financial results. So I'm going to turn the conference to Henrique Freire.

## **Henrique Freire** {BIO 19117781 <GO>}

Good morning, everyone. On slide 10, you see our financial numbers. So this quarter, we had a net income of BRL839 million, 12% above the previous period for the first nine months of this year. And so, we complete the tariff review cycle and on -- this cycle was slightly above the QRR. And twice QRR, which is also recognized and we are happy with the results. Our haircuts is very low, and so we have good numbers. And so -- and all of this is related to very good numbers that we have, and from now on, we will be able to execute everything.

In terms of distribution, the highlight is that tariff market as compared to last year, we had BRL48 million margin, and we also added another BRL10 million of losses. And comparing to last year, we have over-contracting of minus BRL43 million. In terms of hydro generation on this quarter, it was negative, so it's slightly above. So over-contracting was neutral in Q3, whereas last year in the third quarter, if we compare with a better contracting level, we have a gain greater than BRL40 million. So if we compare the EBITDA in the -- this quarter and the previous quarter, we have about BRL40 million.

In terms of hydro generation, we compare our SHPs, and if we compare that EBITDA, so we have BRL24 million less. In terms of hydro power generation, it was BRL143 million that is above that EBITDA. But if you compare to last year, we are below because of risk mitigation strategies.

Now talking about Pecem, so we are down by BRL64.3 million in the year-to-date numbers. If we compare 2019 to 2018, we have to remember that in 2018 we calculated the ADOMP. So we generated a final gain along the year of 2018 of about BRL100 million. Now, if we can think of the EBITDA of this cycle of 2019, we have BRL386 million which is compared to BRL370 million last year. So as you can see, there is a reduction of 43.2% in the average CVU [ph] and higher dispatch by the ONS. So if we compare quarter-on-quarter, sometimes there is some mismatch and sometimes there is a longer effect.

Now talking about marketing or trading in transmission, services and others, we had a good result. But obviously, if we compare to last year with the long position, we had a gain of BRL55 million. So in this comparison, we have a gap of BRL47 million. But obviously, this amount is not really very significant.

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Now on slide -- you can -- efficiency cost control. First of all, our PMTO showing in that first nine months an evolution build, we had a growth of 2.1%, and in the quarter of about 3%. Our vision is that this is related to the interest rate and other macroeconomic factors that affect this. What we see is a consistent drop in our provision for bad debts, a consistent drop. So we implemented many, very good and significant initiatives in order to solve this 159 Efficiency Initiatives. And every year, we have been able to renew everything and we have invested technology. We are also using robots. We have 170 robots operational, and now we are introducing new generation robots. Third-generation robots now are already being introduced and they are more sophisticated.

So lastly, we have our provision for bad debts in this -- on this page. And so, we are stricter now in terms of accounting or the provisions for bad debts. So it looks like there is a slight increase, but there is not. This is perfectly under control and we are going to close the year before our 1%.

Now talking about our debt on slide 12. The highlight here is that we have had the issuance of our debt, and we have completed our cycle of issuance. And I think that our issuance was BRL500 million. 10.3 [ph] IPCA plus 0.85% [ph] and our rates are good. In this issuance -- also, we will include an additional issuance regarding this lot. So what we intend to see here is that we have -- our estimated CapEx is BRL3.5 billion with six transmission projects and all of our lots have been delivered before time, ahead of schedule. And obviously, the return we have for these projects is well above what we had expected.

And now, I would like to turn the conference back over to Mr. Setas.

## Miguel Setas

A brief word in conclusion about the future of our business. And so on page 13, with the reference on initiatives that we started this week, we launched one of the projects that has been approved by ANEEL, our regulation agency with an incentive to support and to encourage electric mobility in Brazil.

ANEEL issued a Public Call (inaudible) BRL50 million in projects and the projects were approved demonstrating EDP's commitment to this issue. And yesterday or earlier this week, we launched here in Sao Paulo, the first state network with ultra-fast charging stations. This is the first time we do it in Brazil, and in Latin America, we want to do that too. So in the state of Sao Paulo, we are going to have about 30 ultra-fast charging stations on the main highways of the state. We want to have greater capillarity covering the whole region of the state of Sao Paulo. And this is the largest network of ultra-fast charges for electric vehicles in South America. So -- also for example, the mobility between Florianopolis and Victorio with a good network support.

So this is not closely related to our financials, but it's like I wanted to mention this, I would like to touch on this. And obviously when we look at our strategy, we have three horizons where we place our businesses -- mature businesses. So, there is strong cash generation and we have long-term contracts and a lot of growth in transmission, thermal generation,

and hydro generation. And then we have growing businesses and then we have future businesses. Like what I have just mentioned about the charges for the car, the charging stations for car, and we wanted to invest in new businesses, businesses of the future. So electric mobility is something that fits into the third wave of the future horizon that we call optionality. Optionality of future businesses and obviously, we want to be present to assure sustainability in the long term for our Company.

That said, I have finished what I had to say and we are available to answer any questions you may have. Thank you very much.

## Questions And Answers

### Operator

(Operator Instructions) Our first question comes from Ms. Carolina Carneiro from Credit Suisse.

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

Good morning, everyone and thank you very much for the conference call. I have two questions. Number one, we know that in the short term, you were not directly affected. And then if you could comment, the process of opening and for the WACC for the three segments. And some companies have publicly said, the improvement for initial WACC that has been proposed. Could you comment on WACC and what you have -- can you tell us about timing and when you expect that?

And then -- and the second question is, could you give us slightly more in detail -- and then you talked about the hydro portfolio and there are some numbers and information in the release. So if you could tell us -- it's more about the fourth quarter because in terms of seasonality and allocation, according to the slide, it looks that you were very close to Q3 and we understand the hydrology slightly bad, but -- so that we have a better idea, both in terms of your hydro generation and in the trading company, or are we going to suffer pressures as we did in the Q3?

#### A - Unidentified Speaker

Carol, thank you. I'm going to go to the two questions and then -- thank you, Carol. Good morning. On the first part about WACC, obviously, we are all doing our homework and there is space for improvement in methodology and pricing of two main items. The first one is the capital that according to our new -- they understand according to what they have said in debentures, it may get badder, because it may suffer the influence of different leverage. And when we look at the risk of the business there are different segments and basically there is -- it's slightly displaced. So we are working to develop the methodology that will differentiate for the distribution industry, as compared to other industries.

We have prepared our technical documents, we've been talking to the regulation agency, and we are waiting and we don't know what they will decide, but we can see that

considering these two pillars in terms of differentiating our businesses as compared to others, there is some space for advances of the agency. What we have also seen is that ANEEL is working, so that in early December, there will be a technical note that you have mentioned and they have basically a month or month-and-a-half to close their internal issues.

About the Q4, what we expect from the fourth quarter, especially in the third quarter, what we experienced when we look at cost curves and analyzing supply and demand, there are minor variations between BRL500 average megawatts to BRL1000 average megawatts or in that region of price ranging variation of BRL100 megawatt hour with a small variations. In the third quarter especially in August and September, it was very close to going up to BRL100 per megawatt hours. So what we will be seeing as of tomorrow, we'll see prices going even further up at the level of BRL300, because this is a very critical situation (inaudible).

So on the fourth quarter, especially in November, our spot prices are lot higher, as to our position our generation is well protected. I think that we are prepared for this cycle, and what we see is that when we analyze the historical trends of spot prices, the rise is very fast and when it goes down -- and when it goes down, it's slower. But we are prepared for this increase, for price increases. And so, the scenario is of draft, but we are prepared to deal with this situation.

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

Thank you very much. This is very clear.

**Operator**

Excuse me, our next question comes from Mr. Fernando Errazuriz from Itau.

**Q - Fernando Errazuriz** {BIO 19965523 <GO>}

Good morning. Thank you for the conference call. I would like to ask you two questions. The first one regards the Company growth. And so there is a wave of privatization in the country. Do you have any updates, anything that you could tell us (inaudible)? Have you been talking to the Government of Santa Catarina, is there anything to tell?

Second question is an update about this question of -- this dispute of (inaudible) on the sign of a new -- have you heard anything from them? Do you have any updates regarding that? Thank you very much.

**A - Unidentified Speaker**

Fernando, thank you for your questions. Well as to finance, we do not have any final decisions or announcements from the government of Santa Catarina regarding privatization. We should considering this possibility in everything that is going on in Brazil on the team. And I would like to remind you that our effort when we invested in Temasek, we wanted to have a mid and long-term calendar. In the meantime, while the privatization is not closer, so there -- we've been partners with Temasek. We are developing joint

projects. We are trying to find new business opportunities in the state of Santa Catarina, which to us is also important in terms of the increase in the amount that we have already identified in this partnership. And therefore in practice, the Company continues to the deepen our partnership with Temasek and to complement the partnership in distribution with other businesses such as transmission and other projects that we currently have together with them.

But then on the other hand, I think it's very clear that our distribution strategy is the focus of a lot of investment for us. As you have seen our investment level in Sao Paulo has increased. And this amount is almost the double today. And we are clearly betting on this business segment. I'm going to turn it to Andre, our Director of Accounting.

#### **A - Andre Luis Almeida** {BIO 20620753 <GO>}

Good morning. So an update of the last quarter. There are two important agents in terms of fiscal themes. On one hand, the revenue office and we had credit -- we will -- we were able to enable it in late September, we're going to start using it in the other provinces [ph] and we are in the hope that in fourth quarter, they will position themselves in terms of the evolution. For the time being, we don't have our final positioning, but we think that - and we will decide that issue shortly, so that we may start with the return.

#### **Q - Fernando Errazuriz** {BIO 19965523 <GO>}

This is very clear. Thank you very much.

#### **Operator**

(Operator Instructions) If there are no further questions, the conference call of the third quarter and the first nine months of 2019 of EDP Energias do Brasil has now ended. The questions that we received through the webcast will be answered afterwards by the Investor Relations team. We thank you all for your participation and wish you a very good afternoon. Thank you.

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