

## Q1 2017 Earnings Call

### Company Participants

- André Dorf, Chief Executive Officer
- Gustavo Estrella, Chief Financial & Investor Relations Officer

## MANAGEMENT DISCUSSION SECTION

### Operator

Good morning and thank you for waiting. Welcome to the CPFL Energia First Quarter 2017 Finance Conference Call. Today we have here with us Mr. André Dorf, CEO of CPFL Energia; Gustavo Estrella, CFO of CPFL Energia and IR Officer; and other officers of the company.

This call is being broadcast simultaneously via Internet on the website, [www.cpfl.com.br/ir](http://www.cpfl.com.br/ir). In that address you can also find the presentation for download. We inform that all participants are in listen-only mode during the company's presentation. After that, we will start a Q&A session and further instructions will be given. It is important to mention that this teleconference is being recorded.

Before proceeding, I'd 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 management and on information currently available to the company. Forward-looking statements are no guarantee of performance. They involve risks, uncertainties and assumptions because 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 could also affect the future results of CPFL Energia, and could cause results to differ materially from those expressed in such forward-looking statements.

Now, I will turn the floor to Mr. André Dorf. Please, Mr. Dorf, the floor is yours.

### André Dorf

Thank you very much. Good morning, everyone. Welcome to another call for our results. We're going to be talking about the first quarter of 2017. As usual, we will give you a brief introduction and then we will have the team available for a Q&A session.

So I would like to start on slide number 3 with the highlights for the first quarter of 2017, where we have a stable load in our concession areas of minus 0.4%. You will see ahead that we had a chunk drop in the captive market and a growth in the free market. In addition to that, we were able to maintain our contracted demand for high voltage clients,

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rather stable of minus 0.6% off peak and minus 0.2% in peak comparing March against March. Also, there was an increase of almost 28% of our net operating revenue and 15.6% of our EBITDA.

And the main growth driver in the announced revenue was the distribution segment in the quarter. Also, we invested a lot, almost BRL 700 million in the quarter. And at the end of the presentation, we will see our CapEx projection for the next year. We have ended this quarter with a net debt of BRL 13.8 billion and leverage of 3.3 times net debt over EBITDA. And this year also we have tariff adjustment for CPFL Paulista and RGE Sul in April, with a tax perceived by consumers as negative for CPFL consumers, and we do not have any negative impact in Portion B for CPFL.

About the transaction of controlled sale of the company, the appraisal report for the unified tender offer is being prepared. We have approved in an AGM the bank that is going to work on that appraisal report, which is going to be pretty soon. And so it is being worked on.

Also, there was an interesting event in the next few weeks. We launched Envo, energy for you, and the main focus here are the solutions in distributed solar power generation mainly to residential clients and small businesses. This is an interesting focus that we have had in the last few weeks. And we disclosed in April our 2016 Annual Report, and it is available on the Internet.

Now turning to the next slide, we have the EBITDA breakdown in the quarter according to the different segments. Starting to our left, we have a pizza pie showing that out of our total of almost BRL 1.2 billion EBITDA, 52% came from distribution segment and 44% from generation.

(05:48) renewable and conventional generation and 4% from our businesses such as commercialization, services and other businesses that are grown in the company.

We have a chart starting to our right in the top, it shows the evolution segment by segment here. In the distribution segment, we have an increase of almost 6%, very much driven by the consolidation of RGE Sul. So the first quarter already shows a consolidated RGE Sul vis-à-vis the same period in the last year where we did not have that consolidation.

In the conventional generations, we had a significant increase basically thanks to price adjustment in the contracts. For renewable generation, also a relevant increase because of new capacity that came in to operation, as well as because of seasonality that happened in the first quarter of 2017. The seasonality were different between quarters, therefore we had an increase in our EBITDA in the first quarter of 2017. And in the bottom left of the chart, we also had a significant increase for commercialization, services and others, and this was thanks to the margin gain of the CPFL Brazil.

Now turning to the next slide, number 5, where we have our distribution market. According on the chart, we have seen increase in sales in the concession area of 18%, and

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this figure is positively impacted by the consolidation of RGE Sul that has added 2,549 gigawatt hours in sales. And so net of RGE Sul, so that we can have comparable figures, the load in our concession area was stable, 0.4%, so we can see that to our right and top chart, once again a significant growth in the free markets, the free clients, and a drop in the captive market.

Sales also remained stable in 0.1%. You can see that in the middle chart on the bottom of the slide, so 0.1%, the same behavior between free clients and captive clients all contracted demand and that is a good news as well. It was stable and that ensures remuneration for that segment in CPFL and losses. And so this is something that we pay a lot of attention to. We've had a slight increase of 9.08% in the fourth quarter of last year, therefore in final quarter, and now 9.14% in the quarter.

So it's still a slight increment, but we are paying attention to that. And that was because of the change in the market mix. We now have more residential clients and less industrial clients. In that residential segment, the losses are a little bit higher. And also because of the economic downturn, that increases the number of disconnections.

And as a negative consequence, it increases commercial losses in the commercial segment. We should highlight as well to our right bottom chart the behavior of the different consumption segments without RGE Sul. Unfortunately, we have the same news from prior quarters, which shows that the industrial segment is still in a drop behavior (09:53) here. Just like the same happened this year. So unfortunately, this is the negative highlights in this consumption segment.

Next page, number 6. We have delinquency data and also the behavior for positions for ADA. On the top chart, we have the evolution of our ADA that is around 0.7% of our gross revenue vis-à-vis of an all-time average of 0.59%. So we see some stabilization but at a level that is a little bit higher of our all-time levels.

To our left bottom chart, we see the total overdue bills, as well the provisions above 90 days as a percentage of revenues. And we also see a stabilization in around 1.20%. So it's much higher than what we have in the first quarter of 2015. Here, we are comparing two years ago. And collection actions that have been (11:08). We have done around 341,000 disconnections in the quarter. This is a significant volume, much higher than what we used to have.

Very well, on page 7, we have generation, and then we start highlighting to our top left chart the spot price for the Southeast and Midwest markets showing the volatility of our spot price. So if we go back to April of 2016, we have BRL 49. We peaked BRL 200 in October, went back to BRL 120 in January, and we were at BRL 371 in April of this year, so this is a great level - high volatility. Actually, that is a reflection of the hydrological profile we have had in Brazil.

Talking about hydrology, the two bottom charts show hydrology represented by the reservoir levels first for the National Integrated Power Systems to our left. At May 10, we had 39% of reservoir levels and our average was 70%, much lower. But the main concern

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is on the Northeast, as you can see, in the bottom right chart. We have had in May 10, 21% of reservoir depository (12:48) against an average of 70%, and a flow in the market of around 30% of the long-term average. Therefore, we are very much below, and this is one of the main focus of attention that we have now the Northeast market.

To the top right chart, we have seen an increment of 4.2% in our installed capacity here represented by an increase in CPFL Renováveis.

On page 8, we talk about the results and then I will turn the floor to Mr. Gustavo Estrella, our CFO.

### **Gustavo Estrella** {BIO 18109709 <GO>}

So these are the highlights of the first quarter 2017. Here, we have IFRS, and we also make remarks excluding RGE Sul for comparative purposes. In the past, we were not consolidating these results. And now in the first quarter, we already have consolidation as the total of the company, RGE Sul, in the results of the group.

In this chart, the variation of total revenue, here we have the explanation, the effect of RGE Sul consolidation, 27.7%, BRL 1.2 billion on top of the revenue in 2016; EBITDA variation of 15.6% or BRL 161 million. Excluding RGE Sul, a growth of 4.2% or BRL 44 million. Next, the variation of income minus 0.1% or BRL 0.3 million compared to RGE Sul and minus 11.5% or BRL 27 million lower in 2017 compared to 2016.

A couple of words on results now broken down by business segment. For distribution, our total variation is BRL 35 million. The main variation is the effect of the consolidation of RGE Sul contributing with BRL 117 million, and also a positive market effect of BRL 14 million, which is basically owing to stability in the market compared to 2016, a variation of 0.1% in 2017, but also the positive effect of the mix. We have a positive growth in residential consumer with a positive margin to the group.

The concession financial asset, once again, we are also posting as of 2017. And we're classifying 2016 the collection of the concession financial asset. So these are collected according to IPCA. So BRL 47 million is basically a lower level of IPCA in 2017 vis-à-vis in 2016. So now we have an accounting non-cash effect of BRL 47 million in the asset.

And also, manageable PMSO adjusted basis, which is the transfer - a high transfer of inflation that happened over 2016. Inflation close to 10% over 2016, but also the maintenance and also strengthening collection action in the companies of the group.

As to renewable generation, there is (16:40) that André has talked about. Seasonality, one of the first factors, BRL 35 million, the difference in seasonality 2017 vis-à-vis 2016. This difference tends to be diluted over the year due to the adjustment of monthly seasonality. One difference from one year to the next, the other variation, the perennial (16:54) result of the group. This is the start-up of wind farms sold in the free market. And then you have in addition in the result of the group of BRL 32 million in 2017.

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With our conventional generation, now basically we have the reflex or an effect of additional capacity basically coming from an increase of transfer price adjustments based on inflation with a positive effect of BRL 41 million in the total amount, out of which BRL 24 million are price adjustments.

For commercialization, we also have an impact of exposure of the company in the free market through the commercialization company. We also see a positive impact in margins and volumes, with an additional BRL 25 million in 2017 vis-à-vis 2016. Net income, that explains the valuation and the drop in results. Net income is basically an update of financial assets, moving from a financial liability with an impact on result of BRL 73 million. And also an impact concerning RGE Sul financial results due to the company's debt of BRL 28 million, and also our mark-to-market. Now, accounting effect of BRL 19 million. So basically, these are the major highlights and valuations of the group comparing 2017 and 2016.

Now, on slide number 9, a couple of words on indebtedness. This was the first quarter of 2017 with an average of 3.3 times according to the measurement of the covenants of the group. The same goes for all companies with a net of gross debt of BRL 13.8 billion. Expectation is positive in terms of leverage. So we're already seeing some kind of stability in our leverage at lower levels. And actually, this is our trend. It is our expectation to maintain and lower our leverage over the next quarters and years.

What about costs? Now we can see a slight reduction in the nominal cost of the debt of the company. Our exposure is very high, the average cost for the last 12 months. So the benefits of reduction of the basic interest rate in Brazil gives you (19:39) through this indicator. It is a moving average for 12 months, so that will also happen in future months. And now in the short-term results is the positive impact on the reduction of the group's financial cost. Growth, this is explained by a lower inflation rate in Brazil. Renewal rates will possibly be higher.

Now on slide 10. It is an important disclosure that we always like to share. It is the company's liquidity. We closed the cash balance in March 2017 at BRL 4.8 billion. So once again, based on our strategy to recommend - anticipate and recommend for the company's groups, our status is very comfortable when it comes to liquidity. Our cash position covers the company's payment for the next 12 months.

Now on slide 11, basically we have the two major growth projects in the group, both in generation and renewable, CPFL Renováveis. (21:02) complex is Pedra Cheirosa wind farm expected to start up in 2018, and we expect it to close in 2018; and Boa Vista SHPP in 2020. So these are both growth projects in the group.

Now on slide 12, André made a brief comment (21:26) related on the second - our new company with Envo. It is a company focused on the sale of energy for the non-regulated segment. So basically to be present in the distribution business and also for low voltage residential commercial customers and a couple of companies. So it is a new line of business, obviously, and we assume and we understand it will be very promising. And we expect to grow very significantly in this business segment for years to come.

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On slide 13, now we show our CapEx forecast up to 2021. These numbers have been approved in our last board meeting. Expected growth in CapEx of the group for 2017 vis-à-vis 2016, basically here we have first the inclusion of CapEx of RGE Sul an increase in CapEx close to BRL 300 million, and naturally an addition of some investments made by other distribution companies. We preserve - we keep this higher level of investments for years to come by 2020-2021. In generation, basically we have the two projects that I mentioned before. The project of ACL, wind farms and also our SHPP, and we have a concentration of investments for 2017 and 2018.

Last but not the least, our transaction with State Grid. Like André has said we are guiding the process to have the tender offer of CPFL Energia. We already have Credit Suisse hired for the evaluation or appraisal report. And now we are drafting and building this appraisal report so we can move forward where the regular proceedings of a tender offer under the terms of our Brazilian (23:56).

So with that, we close our presentation session. And now I give the floor back for the operator, so we can start the question-and-answer session.

## Q&A

### Operator

Ladies and gentlemen, we will now start the Q&A session.

We end now the Q&A session. I would like to turn the floor back to Mr. André Dorf for his final remarks.

### A - André Dorf

I'd like to thank you for your participation on this call. The company is very much motivated with the development of the energy sector. We are also following up the news about the development, the next steps about the segment and we are very much aspiring. And also with (26:12) there's no change. We're bringing those a lot of opportunities and we will follow on with our strategy to grow the company.

Once again, thank you very much and we are available for any future questions you might have. Have a nice day.

### Operator

The conference call of CPFL Energia has concluded. Thank you all for your participation and have a nice day.

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