

Q1 2014 Earnings Call

Company Participants

- Antonio Sergio Guetter, Chief Financial Officer and Investor Relations Officer
- Unidentified Speaker

Other Participants

- Unidentified Participant

Presentation

Operator

Good afternoon and thank you for standing by. Welcome to the First Quarter 2014 Earnings Conference Call of Companhia Paranaense de Energia COPEL for investors and analysts. We inform that all participants will be in a listen-only mode during the company's presentation. And then there will be a question-and-answer session when further instructions will be given. (Operator Instructions)

Before proceeding let me mention that forward-looking statements that might be made during this conference call regarding COPEL's business perspectives, projections and operating and financial goals, other than the beliefs and assumptions of the COPEL's management as well as the information currently available to the company.

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

This conference call is attended by Mr. Antonio Sergio Guetter, CFO and Investor Relations Officer. The presentation will be made by COPEL's management can be followed at the company's website at www.copel.com.br/ir.

Now, I would like to turn the conference over to Mr. Antonio Sergio Guetter, CFO and IRO.

Antonio Sergio Guetter {BIO 18681355 <GO>}

Good afternoon everyone and welcome to COPEL's conference call to discuss the first quarter 2014 results. I would like to join thanking you for participating on this conference call and stress that it is always a pleasure to speak with you. The Brazilian power sector

had a somewhat rough (inaudible) beginning in 2013. The unusual drought for the time of the year caused the worst weather is a worst (inaudible) concerning levels.

And the above average heat that we are experiencing in Brazil and particularly in the South, a record heat that's a very record electricity consumption result. Despite it is concerned particularly related to the cost of energy in the short-term that this quarter of COPEL was very positive.

Please go to slide three. As you can see our net income was R\$583 million up 46% compared to the same period of 2013. Our revenue grew 28% and surpassed the mark of R\$3 billion. It is the first time ever that we hit the mark while the EBITDA grew 29% and ended in the first quarter 2013 as we can see totaling 859 million.

This good result is explained by the performance of our generation company especially by the sale of energy in the short-term market influenced by the high prices in the spot market in the period. And by the sale of energy produced specifically by our thermal power plant Araucaria which as you know when facts been operated by the Araucaria gas plant is used to be lead to the PETROBRAS. Now Araucaria gas plant is a subsidiary of COPEL. On the distribution side however the result was negative. Turning again from higher energy costs primarily related to thermal contracts and contract entered into in January as a result of the A minus one auction held at the very end of last year 2013. So talking about this fiscal we received around 884 million in the first month of CDE funds and the regulated market account ACR to offer cost incurred mainly due to the involuntary exposure to the spot market in the first quarter 2014 January, February and March.

Next slide talking about involuntary exposure. We acquired in the A zero auction few days ago 388 average megawatt which zeroed our exposure in 2014. I would like to remind that this agreement entered in 2000 at the beginning of May. Given the highlights of COPEL Distribution or Copel Distribuicao we have to point out the significant 8.3% growth at the grid market compared with the first quarter 2013 same income [ph] as compared to -- and the good performance that commonly in the state of Parana in the period which includes consumption.

As we're cutting down cost more necessarily at the distribution company. We reduced by 6% our personnel expenses a fact which is keeping with our target set for 2014 and 2015 which we will firmly pursued. Last but not least everyone (inaudible) electric transmission line projects in an auction which will add around R\$50 million in rep annual available rep to COPEL generation and transmission. Well this was the main highlights for the first quarter. However I would like to do more deep analysis specifically about the Araucaria thermal power plant and about the compensation for energy purchase costs.

If we go to slide four. We can see a significant part of our results coming from the operation of the Araucaria thermal power plant. As you can see on slide four the lease agreement for the Araucaria TPP entered into between Araucaria gas plant, UEGA and PETROBRAS expired on January 31, 2014 and the contracts was not been used. So since February 1st, 2014 the operation of the plant has been under the reasonability of Araucaria TPP. The company consulted [ph] consoled by COPEL which has an 80% stake in

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the business the remaining 20% is held by PETROBRAS. The Araucaria TPP does not have availability excuse me in the Araucaria TPP does not have availability agreement and operate under a merchant in which revenue depends on the operation of the plant and energy when produced is sold in the short-term market.

In the first quarter for the consolidated net revenues of Araucaria TPP totaled R\$474 million is the first line in the table. In the same period net income stood at 134 million and EBITDA was R\$167 million. It is worth highlighting that this plant continues to operate in the second quarter which allows us to conclude with COPEL's result will continue to be positively impacted by the thermal power plant good performance. After the recovery of cost related to the purchase of energy, it also influenced our results. We are on slide five now where we'll give you more detail on the amount received.

As you know Copel Distribuicao had to purchase energy in the spot market due to the involuntary exposure caused by the lack of auction to offset a sufficient amount. The energy whose contracts ended in the end of 2013. This problem in addition I'm going to highlight that it is not impacted only COPEL, it impacted the electric system and the electric sector as a whole. All this problem was aggravated by the hydrological conclusion which drove the energy spot market price up to maximum level of R\$852 per megawatt hour to offset between the energy cost.

The Brazilian government amended issued decree number 8203 amending decree 7945 of 2013 and on the transfer of CDE funds, the energy development account to cover only for the cost increase due to the involuntary exposure of distributors in the month of January 2014. With the high electricity price and the lack of funds in the CDE. The government created the regulated market account the so-called ACR account which ended up being ratified in April of 2014 by decree number 8221. The ACR account will cover expenses resulting from the involuntary exposure to this spot market and from the thermal plants dispatched between February and December 2014. We have new lease account in the months of February and March. Regarding values we posted R\$832 million in compensation for the electricity costs. However 884 million were transferred relative to the first quarter although we had 832, but 884 million we transferred.

Of which 115 million refers to January, 447 million to February they can only relate, but they are relative to February and R\$322 million relative to March. This R\$52 million different between the amount estimated by the company and the amount transferred will be adjusted in the next quarter.

Please go to slide six. As for COPEL's consolidated results. If you saw on slide six that the net operating revenue grew 28% in the first quarter 2013 surpassing the mark of R\$3 billion. The main reason (inaudible) of this revenue increase. We're going to talk about revenues from electricity sales to final customers and the distributors. Well it was a 20% increase in revenue from electricity sales to final customers due mainly to the 9.65 service increase of Copel Distribuicao as of June 21st, 2013.

And secondly the 6.6% upturn in sales volume in this period. Also regarding electricity sales to distributors it was a 53% growth mainly standing from higher revenue in CCEE

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from energy sales due to the Araucaria thermal power plant sales in the short-term market as of February of this year and higher prices resulting as I said in the period. The use of the main distribution and transmission grid which is made up of TUSD and TUST revenues posted an 8.8% upturn rate due to the 8.3% expansion of the grid market of COPEL's distribution resulting from (inaudible) Parana commonly.

Total revenues which encompass construction, telecom, gas and other revenues had a 25% upturn and reached of R\$453 million driven exactly by two factors. One increased the construction revenue which reached around R\$300 million and the booking of investments in distribution and transmission infrastructure. And number two about 20% growth in telecom revenues in the quarter which totaled R\$40 million in the period. Please go to slide seven where we detailed our operating expenses in the first quarter 2014 which increased 28% compared to the same period of last year. Sales can be explained mainly by the 17% increase in the cost of electricity purchased for retail which totaled R\$982 million.

I would like to remind you that this amount already considered the R\$832 million of (inaudible) by the transfer from CDE and from the ACR account that were accounted for in the period. Charges for the use of the main distribution and transmission grid was down 14% in the period due to a cost reduction in system service charges. Following the lower dispatch of thermal power plant outside the merit order in the period.

The first quarter results also -- by higher expenses with gas purchases resulting from the end of the lease agreement of the Araucaria TPP which since February it has been binding gas from Comgas which on its turn is buying more gas from PETROBRAS to meet its additional demand. While talking about personnel costs including pension benefit sales dropped 6%.

On the top right hand corner of the slide. The personnel costs charge detailed on the next slide. So we also inform our manageable cost. As you can observe on the trade, personnel costs and third-party services costs dropped 4% effect which compared to IGP-M ratio of 7.3% represent a drop of more than 11% in manageable costs inverting and funding or (inaudible) cost which come to show how we are putting a lot of effort in reducing costs in the company. The greatest contribution for this reduction comes from lower expenses with compensation and charges resulting mainly from a reduction in our headcount in 2013. In the last quarter we also reduced our headcount even further. We currently have 8,600 employees currently which represent a 9% reduction vis-a-vis the previous year. I would like to highlight that analyzing adjusted numbers of COPEL's distribution reduction in manageable costs was R\$29 million which is intriguing with the expected and according to the target offsetting a R\$100 million in 2014. Perhaps the company comply with the regulatory framework which we expect to achieve in 2016.

On the next slide, slide nine. We breakdown expenses related to electricity purchase for resale which as previously mentioned grew 17% and totaled around 982 million in the first quarter of '14. The electricity purchase in the regulated market it grew mainly because of new thermal and hydro power contract and the contracting of 511 megawatt in auction A-1 in the end of 2013. The electricity sales are distributed in February and January of this

year. Also impacting was the higher cost of the thermal plant taken to account this plant dispatch in the monetary replacement of the contract.

In addition to this the discount with regulated market contracts the cost with the purchase of energy in the CCEE grew because of the high PLD. While the cost of ITAIPU grew motivated mainly by depreciation of the dollars in relation to the first quarter of the previous year.

Again talking about the company's results we are now on slide 10. Still it is possible to look at the EBITDA, consolidated EBITDA grew by 29% in the first quarter of 2014, totaling 859 million and a 28% margin over the operating revenue. Increasing this volume stock in the same period of last year. Cash generation of COPEL generation and transmission accounted for 75% of the consolidated EBITDA. While COPEL telecom accounted for 3% [ph] and the other companies that the Group accounted for 22% influenced by the result of the Araucaria TPP. COPEL distribution showed a negative EBITDA of 21 million again due to higher costs with energy cost of sales that's shown. EBITDA margin of COPEL generation and transmission reached meaningful 76%. And this is on the bottom left hand corner of the slide 10 and COPEL telecom posted a 56% EBITDA margin.

Please go to slide 11. Here we have COPEL's consolidated net income which was R\$583 million in the first quarter of 2014, 46% up compared to the same period of 2013. Net margin reached 19% and it was higher than what we achieved in the same period of last year. When announcing the results of the subsidiaries we see that COPEL's generation and transmission ended the period with a profit of 432 billion, 6% up vis-a-vis in the first quarter of 2014 and with a net margin of 51%.

COPEL telecom had a profit of 14 million which corresponds to a 23% growth year-on-year. COPEL distribution understand from today loss of R\$15 million. A little bit less than 15 million. Well these were the main highlights of COPEL's results.

However, before we close, I would like to again to talk about our success in the last transmission auction which happened about a week ago. As we can update on slide 12 we won three new lot which for an operation of more at around R\$60 million to our rep of COPEL generation and transmission. We are very happy with the results obtained which is one more example of our commitment to financial disciplined and the sustainable growth of the company.

And two out of three lots that we won this compensate with the three new projects altogether we have 17 projects of the ability [ph]. We total about 2,800 kilometers of transmission lines and an additional revenue of 355 million in this segment (inaudible) are very small. In a nutshell these were the highlights of COPEL's results for the first quarter 2014.

I would now like to begin the question-and-answer session. And I would like to thank all of you for your participation.

Questions And Answers

Operator

Thank you. We will now begin the Q&A session. (Operator Instructions) Our first question comes from (inaudible) Credit Suisse. (inaudible) you may proceed.

Q - Unidentified Participant

Good afternoon, Guetter. Thank you. Guetter, I have a couple of questions. I'm trying to do the calculation for Araucaria particularly the cost modeling we believe that the results was quite strong. I would like to have an idea of the cost of operating Araucaria in terms of megawatt hour in the invest calculation. We see that the numbers closer to 400. Could you elaborate about your cash cost and is my calculation right for Araucaria. This is the first question?

My second question is can you give a sense of how much was allocated in this quarter of energy of COPEL GeT. And my last question is about CDA. I have some questions regarding the reconciliation of the cost compensation more than 200 million for more than one quarter?

There are other components that is commonly mentioned here. Could you please point out the tariffs what are the fact that tariffs demand increase last year. But it continues to be high. So is there anything that you could mention about this that is worth highlighting? Thank you.

A - Antonio Sergio Guetter {BIO 18681355 <GO>}

Hello. Pedro [ph] it's a pleasure to have you on board again. Philippe [ph] is going to provide some additional information.

A - Unidentified Speaker

Hello. This is Philippe. Pedro about the period of Araucaria TPP that the cost is relatively small [ph]. Whatever the points we are going to dispatch for four months and when we look at the cost, the cost is diluted over the 12 months of the year and that is why we have the difference between what it was (inaudible). And what we estimated in the tariff for the thermal plant. And for COPEL GeT we disclosed this. The amount of energy sold by COPEL GeT in the first quarter was about 500 gigawatt hour. And we have to see what would be average allocation vis-a-vis available to us and as for CDA because given why (inaudible) some questions, but it is important to highlight that when we do an estimates of CVA again this is a calculation done by estimates and in this quarter specifically, when we are going through a moment where the BLD. That is a very high. So in the estimate here even if the gap is very small it ends up accounting for a lot in monetary trends. We have very big difference. It is a little bit higher than what we should have, but suppose when we talk about CVA that value considers we estimated thermal dispatch and we estimated cost for dispatch in February and March was ended up being offset by the ACR accounts.

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The differing of the tariff which is 68 million and in the next year it will be another 68 million and there is still 15 million balance in the CVA from last year. So, we have these adjustments that happened quite recently not only in COPEL and basically it need to happen, basically because this is very difficult to estimate based on the evolution and estimation [ph]. So it end up being released a lot later. So a number of sectors that implements the accounting and which is always done by estimate in this case. So these are the comments about CVA.

Q - Unidentified Participant

Thank you. And for Araucaria the cost for the four months you said three or four months then we will have to diluted by 12 months. If this is the math about it, okay. What is the cost or I have another calculation here. But when you established the cost of 695 we got the whole cost along 2014 updating cost (inaudible) when the plant is not operational. And the cost recovery was concentrated in the four months. It was estimated for the plants to be operated. So any of the cost now is kind of difficult in monetary terms.

But this is explained by tariff. The tariff considers that we are going to recover all of your operating cost, including personnel, maintenance, monthly maintenance, etcetera, that all of the cost would be recovered in the first four months when the thermal plant is operational even if it's not operating it's still into cost throughout 12 months. So the cash cost is lower. You finally mentioned that we expected to contribute constant over the years. Can I work with this kind of level in the EBITDA per megawatt hour would be more or less the same for the coming quarters in your expectation. Is this the fair statement?

A - Antonio Sergio Guetter {BIO 18681355 <GO>}

Yes. This is our expectation but it really depends on priority sometimes.

Q - Unidentified Participant

Okay. Thank you very much.

Operator

(Operator Instructions) Since there are no more questions from participants. So we will turn the conference over to Mr. Guetter.

A - Antonio Sergio Guetter {BIO 18681355 <GO>}

Well before closing I would like to thank all of you for participating. I am very happy with the results we achieved. We reaffirm our commitment with controlling our cost which as I mentioned should be even lower in the coming quarters. I stress that, we will maintain our focus on creating value to our shareholders seeking greater operating efficiency and maintaining our financial discipline when evaluating new business opportunities.

Again I would like to thank you for your participation and I would like to say that our Investor Relations department is at your disposal. Thank you very much and have a good day.

Operator

Ladies and gentlemen this does concludes COPEL's 2014 first quarter earnings conference call. We would like to thank all of you for participating and enjoy the day.

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