

## Q2 2012 Earnings Call

### Company Participants

- Mario Arruda Sampaio, Head of Capital Market and Investor Relations

### Presentation

#### Operator

Good afternoon, ladies and gentlemen. At this time, we would like to welcome everyone to SABESP's Conference Call to discuss its Results for the Second Quarter of 2012.

The audio for this conference is being broadcast simultaneously through the Internet at the website [www.sabesp.com.br](http://www.sabesp.com.br). At that same address, you can also find a slideshow presentation available for download.

We'd like to inform you that all participants will only be able to listen to the conference during the company's presentation. After the company's remarks are over, there will be a question-and-answer session. At that time further instructions will be given. [Operator Instructions].

Before proceeding, let me 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 SABESP's management and on information currently available to the company. forward-looking statements are not guarantees 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 in the future.

Investors should understand that general economic conditions, industry conditions and other operating factors could also affect the future results of SABESP and could cause results to differ materially from those expressed in such forward-looking statements.

Today with us we have Mr. Rui Affonso, Chief Financial Officer and Investor Relations Officer, Mr. Mario Arruda Sampaio, Head of Capital Market Investor Relations and Ms. Nara Maria Marcondes França, Head of Accounting.

Now I'll turn the conference over to Mr. Arruda Sampaio. Sir, you may begin your conference.

### Mario Arruda Sampaio

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Okay. Good morning. Actually good afternoon everybody. Thank you for attending one more earnings conference call. We will run through a brief eight slide presentation to discuss the main events during the period. And after that as usual, we will move on to the question-and-answer session when we will all be available for further clarifications.

Let's start on slide three, we have the company's billed water and sewage volumes showing 1.4% above the same period in 2011.

Let me start by commenting that in 2012 we concluded the implementation of what we call TACE, its External Commercial Service Technician. In fact, this is a in-location electronic reading system. This was implemented throughout the company already. These services allows greater billing speed and reduced water bill reception time.

The TACE began to be utilized in the Sao Paulo city and metro region of Sao Paulo longer time ago. And was then extended to the municipalities in the interior region of Sao Paulo as of 2010. The intense implementation phase in the interior region occurred mostly in 2011. And as we implement, there is a change to the metering schedule covering a higher number of consumption days which led to a greater billing volume in that period, in that past period.

This event somewhat justifies the lower consumption reported in the second quarter of 2012, compared to the same period last year as the number of billed days was higher in the prior quarter and that is in the second quarter of 2011.

Now looking quickly to the loss ratio, you can see that we have maintained somewhat into 26% level. We understand that with the beginning of the contracting of works financed by JICA the Japan International Cooperation Agency scheduled for early 2013, we will have a more substantial decline for this indicator effect. This is when additional intense work will commence. So we should see that coming down stable and coming down throughout the year in the beginning of throughout next year.

Let's move to slide four. Here we will comment on the financial results. Net revenue was positively affected by the 6.83% tariff increase. As of September 2011 and the 1.4% growth in billed volume as we commented in the previous slide.

However, the 5.8% rise over the same quarter in 2011 was below our expectation, mostly due to the TACE implementation which we just again just commented. In fact, the conclusion of implementation of TACE in the interior region, there was also a decline as we went through it, the implementation, in fact right now there was a decline in the number of days that unbilled supply is estimated what we call here the revenue estimate.

As a result, there was less days to be counted, billing reflected sales growth and the tariff increase, but also impacted, was impacted by the unbilled revenue estimates which also is part of the operating revenue which was lower than the estimates for previous periods. But please note that this was a non-recurring event for the upcoming quarters and it in fact had no cash impact or effect.

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If we exclude the effect of this difference on the revenue -- of the revenue estimate of 90 million and that was the impact.

Gross operating revenue would have grown by 7.8%, net income totaled 346.7 million and EBITDA margin would be 34.4.

Looking at cost and expenses, as you can see declined by 6.5% in the period. Cost and expenses as a percentage of net operating revenue slightly increased 74.3% in second quarter 2011 to 74.8% in second quarter 2012. If we exclude the revenue estimate adjustment we just mentioned above, cost and expenses would have come down actually to 72.45% of net revenue.

The last line let's talk is, no, second to last is EBITDA, increased from 775.5 million to 798.4 million in second quarter 2012.

The EBITDA margin came to 32.3 versus 33.1 in second quarter 2011. And again, this was due to the non-recurring adjustments of the revenue estimates we have been mentioning currently. As for the EBIT it moved up by 3.7% from 599.3 million to 621.4 million in second quarter 2012.

Last on this slide, net income declined from 479.6 million to 292.8 million in second quarter 2012 due to the strong impact of the exchange rate variation. In fact, this non-cash effect was due to the respective 10.9% and 14.6% depreciation of the dollar and the yen against the real.

Note that in the same period in '11 the dollar and the yen had depreciated by 4.2% and 1.12% respectively against the real. On the other hand, if we exclude our exchange ratio variation on both quarter, net income would come to 430.6 million. That would be then an increase of above where we are today 11.2%.

Let's go to slide five. Here we will discuss the variations in cost in relation to the same period of the previous years. In comparison to the second quarter of 2011 the increase as we mentioned before was 6.5%. The main factors behind this expansion were the increase of 42.8% in treatment supply, 24.9% in supply, 8.6% in services and 7.6% in payroll and benefit.

Let's look at them closely. So let's start with expenses with treatment supplies which increased 15.4 million, as mentioned 42.8%, over the last quarter from 36 million total to 51.4 million. This was due to the 7.4 million upturn from higher activated carbon consumption due to weather and water source conditions and the proliferation of algae in the reservoir that serve the Guarapiranga and Cantareira water production systems.

Another impact came from 3.3 million due to the greater use of quicklime utilized in the sludge treatment. And this also element had a price increase of approximately 23.8%. We'd also like to highlight the 2.9 million increase due to couple of reasons.

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First, the greater hydrogen peroxide consumption in the sewage pumping station in the Baixada Santista region, the Southern Coastline region as a result of the proliferation of algae. And this together with the beginning of new operations in the Guarujá region of pumping stations, all this added also by price adjustment of about 12% for this material.

So, in summary, we had water quality issues, increasing capacity issues, all this together with price above inflation increases. Expenses with, now the next point will be expenses with supply, which moved 8.6 million or 24.9% over the same period last year totaling 34.6 million to 43.2 million. This was mostly due to water and sewage system preventive and corrective maintenance, which amounted to 2.2 million and the reincorporation to the stockroom of surplus material that was not used in the maintenance of water and sewage connection and networks totaling 3.6 million in the second quarter of 2011, in fact, it is a reversal back to our inventory.

Excluding this reversal let's call reincorporation of this material to the stockroom inventory, the increases have been 13.1% and not or 9%, in effect, it's only 13.1%.

Other point is service. As we mentioned it grew by 8.6%, a total increase of 20 million from 232.6 million to 252.6 million, for the most part due to 11.9 million upturn related to social and environmental initiatives performed under the partnership with the city of Sao Paulo government. The 6.4 million increase in the fleet renewal program undertaken through fleet rentals we're renting now and this increases our service expenses.

A 5.7 million rise with service payment for the public and private partnership agreements of the Alto Tiete production system, and this is due to the startup of the additional 5 cubic meters per second water capacity which was the object of the expansion of the service. Also 5 million were spent in addition to the regular in paving and basement replacing services related to the water loss reduction program.

Last on the slide but not least, payroll and benefits increased 31.5 million, were 7.6% from 412 million to 443 million due to salary increases of 8% as of May 2011 and 6.17% as of May of this year 2012, with an impact of approximately 21 million on the total payroll. And also in addition to that an R\$11.4 million increase in actuarial liabilities related to the GO pension plan.

Let's now move to slide six. Let's go quickly through the items that affected our net income and talk about the main variations. Net operating revenue moved up by 135.2 million or 5.8% over the same period in 2011. This is due to the upturn in billed volume, tariff adjustments and increasing construction revenue, this last following high investments undertaken during the period.

Cost and expenses grew 113 million or 6.5% as already discussed in the previous slides for the reasons we have reviewed them in detail already.

Other operating revenue and expenses grew -- fell sorry, 29.8 million, mostly due to the 36.3 million agreement for the exclusivity rights for the salary deposits of SABESP

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employees from March 2007 to June 2011 along with the Banco Nossa Caixa and later with Banco do Brazil.

Financial revenues and expenses that is net financials are shown in the chart, had a 337 million negative effect on the net income in the period. This was in great part due to the exchange rate effect of 282 million in consequence of the appreciation of the dollar and the yen against the real as already detailed in the previous slide.

Specifically, regarding financial expenses, there was a decline of 12.8 million in lawsuit financial expenses due to the lower need for provision. And approximately 5.8 million in domestic loans and financing interest payments over 2011 due to the amortization of the eighth and the ninth debenture issuance in June and October last year. So the base for charge was interest was smaller.

As for financial revenues, the second quarter 2012 number came in at 37.7 million, below second quarter 2011. This was mostly due to the gradual reduction in the interest rate from financial investments and also lower cash and cash equivalents observed between the periods and during the periods.

Finally, income tax and social contribution recorded a positive variation about 197.7 million, justified mostly by the impact of the exchange rate variation during the period and also the tax gain obtained by the interest on own capital or part of the interest on own capital that we booked after the dividend approval by the Annual Shareholder Meeting. So, we deferred it two times, so we captured the benefits this quarter.

Let's move now to the last, sorry, the second last slide, talk about debt. In July, the company contracted and signed 22 credit operations with Caixa Econômica Federal. Caixa is our social bank, you know well BNDES, the development bank. This is the social bank. The amounts totaled a 160 million which will be allocated to water supply and sewage works and services in municipalities with population of less than 50,000 people. The funds came from the FGTS which is the sanitation and also the sanitation for all program. And we obtained through a selection process undertaking by the Ministry of Cities.

Financial charges are basically interest rate of 6% per annum, a risk rate of 0.3% and management fee, administration fee of 1.4%, which means in all in 7.7%. It is, there is a index, it's the TR rate. The TR rate has been running very low at around 0.5. This financing has a 24 year term being four years for amortization and 20 years for, sorry, four years of grace period and 20 years for amortization.

Let's go to the last slide, talk about tariff adjustments. We would again like to inform that on August 11, the Sao Paulo State Sanitation and Energy Regulatory Agency, ARSESP, authorized a tariff adjustment of 5.15%. That is 0.05% below inflation in the period. It is to be applied on the linear basis to all categories of water and sewage consumers, as of September 11, 2012.

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As you can see on the slide, this tariff adjustment is one of the lowest to be applied in Brazil Sanitation companies this year, which just holds the idea that greater than inflation increases are possible as you can see in other companies.

We would like to remind you that tariff adjustments have been below inflation since 2008. This is due to the company's successful initiative launched in 2007 to cut costs through a corporate water loss and energy cost reduction program without the possibility. But on the flip side giving the formula without the possibility of incorporating these gains by the company and again because the formula does not provide for a productivity component.

We expect that this, as you can see, the situation remained throughout the 2012, which is this increase. But we do expect that the new tariff methodology to be implemented by the end of this year will allow the incorporation of productivity gains.

In fact, according the regulator, he has already said that the productivity gain for the period as a suggestion will be 2% for the entire four year period. Well, so we're already now pretty much what's ahead of us.

Well, that concludes our initial remarks and we are open for questions right now.

## Questions And Answers

### Operator

Thank you. We will now begin our question-and-answer session. [Operator Instructions]. It appears that we have no questions at this time. And I'll turn the conference back to SABESP for their final remarks.

### A - Mario Arruda Sampaio

Well, everybody, thank you for your time. And if you don't have the question now, but if you have it later, feel free to call myself, Angela, the entire IR team. Thank you for your time and see you next quarter. Bye.

### Operator

The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.

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