

Q2 2021 Earnings Call

Company Participants

- Alexandre Nogueira Ferreira, Regulatory Affairs and Strategy Officer
- Mauricio Perez Botelho, Chief Financial Officer
- Ricardo Perez Botelho, Chief Executive Officer
- Unidentified Speaker

Other Participants

- Andre Sampaio, Analyst
- Carolina Carneiro, Analyst
- Marcelo Sa, Analyst
- Unidentified Participant

Presentation

Operator

Good afternoon, ladies and gentlemen, and thank you for waiting. Welcome to Energisa's Conference Call to discuss the Results of the Second Quarter 2021. We would like to inform you that this event is being recorded (Operator Instructions). Both audio and slide show for this presentation are being broadcast simultaneously via webcast and may be accessed through the website ri.energisa.com.br.

Before proceeding, let me mention that forward-looking statements that may be made during this conference call regarding the company's business prospects, operating and financial projections and goals are based on beliefs and assumptions of Energisa's management as well as information currently available to the company. Forward-looking statements are not guarantee of performance, they involve risks, uncertainties and assumptions as they relate to future events and therefore depend on circumstances that may or not occur, general economic conditions, industry conditions and other operating factors may affect the company's future results and may lead to results that differ materially from those expressed in such forward-looking statements.

Now, I would like to turn over to Mr. Ricardo Botelho. Please Mr. Botelho, you may proceed.

Ricardo Perez Botelho {BIO 2105867 <GO>}

Thank you, operator. Good afternoon, everyone. We start another important teleconference for the results of the second quarter of 2021. Here with us today, we have Mauricio Botelho, IR and Financial Vice President; Gioreli De Sousa, Vice President of Distribution; Alexandre Ferreira, Vice President of Regulations; Daniele Salomao, Vice

President of Human Resources; Antonio Carlos Tovar, Director of Corporate Finance; Newton Santos, Director of Revenue Protection; Roberto Godoy, Vice President of Energy Solutions; and finally our Investor Relations team.

To kick off our presentation today, first of all, I'd like to kindly ask you to look at Slide number 2. It should be read carefully before we make any decisions on investment by the company. And then on Slide number 3, I would like to present the highlights for the meeting today. They include the performance in the energy market, energy losses, quality indicators, DEC and FEC, delinquency rate, collection rate, net RAB evolution and Parcel B evolution with the tariffs for this year. Special highlight throughout our presentation today will be on one important factor we have observed in Acre and Rondonia in terms of operational efficiency, improvement for client services and financial results. We expect to overcome the internal goals for the transformation plan and will celebrate with you. And then after that, Mauricio Botelho will present the financial highlights, investments and advances in the transmission segment, and finally, we are going to open for Q&A.

On Slide 4, we have the operational highlights of the Group and the performance in the energy market, which had the highest growth in nine years for the second quarter, with an increase of 7.9% when compared to the same period last year. Even though the market in 2020 was impacted by the COVID crisis, this recovery demonstrates that we're going back to track with our -- in full power growing even when compared to pre-pandemic levels. Actually, we are present in a large part of Brazil and our 11 concessions were benefited by the recovery of the economic activities this year with a growth in the consumption of energy in this quarter, especially those located in the Southeast of the country.

Also in the consumption classes, all of them had an excessive growth. Industrial consumption was an increase of 14.4% has guided the positive results for this quarter, which was leveraged mainly by the cement production sector, textile, food, vehicle parts, mining with the resumption of the consumption market for these products. For the residential class, which is the most important one for the Group and represents 40% of the total was also a highlight improving 4.7% in face of the energy increase recovered with a good performance of losses that we will demonstrate immediately after.

I would also like to highlight that the growth higher than two-digits in the business class are in the order of 13.1%, which was harmed in 2020 with the parallelization of the activities in business and services since the COVID first wave. All of our 11 distributors have benefited from this growth and it has been possible because of the advance of vaccination and social distancing relaxation [ph], however, and the plants is still below the pre-pandemic level. The rural class has had a relevance in the growth of consumption, with an increase of 4.0%, and this was leveraged by the production of egg, soy, rice, cattle raising, especially in the Mato Grosso do Sul concessions, Tocantins and inner Sao Paulo state because of the higher irrigation services in Paraiba and Sergipe.

In Slide 5, we can see that the average consumption of energy is 200 bps higher than the national average in the last 10 years, and I would like to highlight that in the last quarter, our performance was lower than the average in Brazil, but this is perfectly explained by

the facts that happened in 2020 in the peak of the pandemic as it can be clearly shown in the graph. With this, the comparison basis was harmed.

And now in Slide 6 and 7, we can see the losses with a highlight for Rondonia and Acre since December 2019. In this quarter, the 12-month curve, the indicator of total loss were in the order of 13% and 11% with an excessive reduction of 0.66 percentage points when compared to March, and it is the highest value for this area and I would like to reinforce that the consolidated losses of the Group for this quarter were below the regulatory limit for the first time since the fourth quarter of 2018 when started recording the losses for Rondonia and Acre. This performance is explained by the consistent improvement in the electrical system, also the use of technology and analytics intelligence and capacity building of all of our employees.

All of these measures have led us to reduce the loss indicator in all 11 distributors when we compare March 2021 and June 2021. The Mato Grosso and Paraiba distributors have had descending loss curves with levels that are closed to the regulatory limits. Paraiba has produced its best results since September 2019, and the losses in the second quarter of 2020 in the peak of the first wave of the pandemic were explained by the restrictions in our field team.

I would also like to highlight our Rondonia and Acre concession, where in Slide 7, I present since 2019 the trajectory of losses with improvements of 5.8% and 7.3%, respectively. And then when we compare this to March this year, we can see that in June and March 2021, these reductions are even more relevant. With that for Rondonia, we have decreased the distance between this indicator and it's regulatory limit in 2.5 percentage point when compared to a distance of 4 percentage points presented in March 2021. The Acre concession has performed below the regulatory limit since December 2019 with a relevant increase in performance in March and June 2021, with reductions of 2.4 and 3.3 percentage points, respectively. In both companies, the loss reduction was accelerated by the implementation of analytical tools and management tools of the processes that are used in all of the companies of the group and the system migration took place in December 2020 and March '21.

In Slide 8 and 9, we can see the performance of the DEC and FEC quality indicators of our 11 distributors with excellent results in both indicators. This quarter, the companies had their historical minimum index, where Energisa continues with the reduction of 2.9 hours or 14.7% when compared to June 2020 overcome its historical minimum in the previous quarter and Energisa Paraiba with a reduction of 1 hour in the interruptions.

Once again, I would like to highlight the good progression in Rondonia and Acre, and Slide 9 shows a trend hours decreased since December 2019 with a reduction in the duration of interruptions of 17 hours and 8.4 hours, respectively. Rondonia remains above its regulatory limit with a difference of only 4.37 hours, and we are working to have the connection of the nine isolated system in the state take place this year.

Regarding the FEC indicator, all of the 11 distributors remained below their regulatory limits with a highlight once again to Rondonia and Acre, who have their historical minimum

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in this second quarter. These two companies also have presented a decreasing trend for this indicator of frequency of interruptions with a reduction which is 10 times and 9.5 times, respectively since December 2019.

And in slide 10, we can see the results for the Group of distributors with an improvement of 0.7 percentage points, and this is still impacted by the COVID pandemic. The actions that have been implemented have allowed a gradual recovery and the results confirm the expectation of sustained improvement. We have also had a decrease of \$142.6 million when compared to the second quarter in 2020 in the delinquency. And even with this improvement, the scenario is challenging. However, it is more optimistic if compared to last year when the indicator reached record levels.

Our collection actions with more flexible payment offers and access to digital media has contributed for a better performance in this indicator, and in the graph below, we can see the performance for the quarter in Rondonia and Acre, which have reverted their provisions for PPECLD continuously.

In Slide 11 and 12, we can see the progression based on the liquid payments of payment B in the distributors Borborema, Minas Gerais, Nova Friburgo, which had their reviews performed by June '21 and the Southeast distributor with a review in July this year and Paraiba. And then we can see the graph with an increase in the net base for the fifth cycle. When compared to the last two quarters, these results reflect investments and the good asset management which has been done consistently in these companies with a highlight to Energisa Southeast and Paraiba.

With this progression, I'd like to show you in the next slide where we have had improvements in the payment of Parcel B. In other words, we were able to guarantee an increase in four of the distributors in the Southeast and Paraiba, which together have an actual increase of Parcel B of approximately BRL72 billion [ph] when compared to the previous quarter. And we can also see that this performance once again shows the company's discipline, what the main leverage we have, whereas we provide improvements in our services to all of our clients.

And now, I turn over to Mr. Mauricio Botelho, who will present the financial highlights for the quarter.

Mauricio Perez Botelho {BIO 2105889 <GO>}

Thank you very much, Ricardo, and now let's move onto Slide number 14. Here we're going to highlight the controllable expenses, which were reduced 11.9% in the semester and 4.6% in the quarter. We have PMSO, which grew 5.3% and the semester and is below the IPCA inflation of 8.3% and IGPM of 35.8%. And then in this quarter, we can see a total BRL662.7 million, an increase of BRL110.2 million when compared to the second quarter of 2020.

It's important to highlight that in the second quarter last year, it was the first wave of the pandemic where we adopted severe contingency measures forecasts and service delays

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in addition to the benefits that were granted at the time by means of a decrease in labor payments based on provisional measure 960. And then for PMSO in the first quarter of 2020, which is before the pandemic, it was BRL648.4 million and so we had in fact a nominal increment of only 2.4% in phase of this normalized expense level.

I highlight in the second quarter, an increment of BRL27.1 million and expenses with materials and this results from a combination of factors such as increase in the price of commodities and the resumption of activities when compared to the same period last year, and this is the result of a higher expenses such as vehicle parts and accessories and in the service line we had an increase ranging in the order of BRL23.8 million in the quarter due especially to the resumption of the activities with a higher volume of services.

On Slide 15, we have the EBITDA for the second quarter with an increase of 90.5% or BRL658 million when compared to the second quarter in 2020. In the accrued for the year, the increase was 70.8% or BRL1.1 billion and this performance is explained especially by the increment in Parcel B of the distributors, which totaled BRL602.7 million in the quarter and was impacted by the reviews and readjustments in the tariffs. In addition to that, we also had a contribution from the regulatory EBITDA of the transmission without the O&M revenue. The EBITDA without non-recurring effects and non-cash effects between quarters had a growth of 109.8% and reached the level of BRL1.25 billion.

And then moving onto Slide 16, we're going to talk about the adjusted EBITDA in the last 12 months. In this graph, we can see that the volatility is removed as well as the seasonability and we had an increase of adjusted EBITDA on annual basis of BRL695 million when compared to the first quarter this year and it is BRL1.7 billion higher than when compared to the last 12 months. And PMSO also went down from BRL2.82 billion in the second quarter of 2020 to BRL2.65 billion this quarter. And the PMSO ratio for EBITDA went down from 74.9% in the second quarter last year to 48.2% in this last quarter.

And we are now going to the next slide. We're going to talk a little bit about Acre and Rondonia. Ricardo had already mentioned this, we had an excellent recovering in these two areas. We have demonstrated the PMSO and adjusted EBITDA progression in these companies, and as you can see in the 12-month graph that we have had continued flow reduction in PMSO in the two companies since the first quarter of 2020 and an increase was recorded only now in the second quarter, and this was impacted in large part by the factors that were mentioned previously. We can also see the adjusted EBITDA, which resulted in a joint variation for the two companies of BRL52.7 million, when comparing the second quarter of '21 to the first quarter of '21. This growth is even higher, it is of BRL611 million when compared to the performance of these companies.

When we compare the performance with that of the first quarter of 2019, in Slide 18, we highlight the progression of the two last acquisitions, and please note that after the initial period of consolidation of the two former state-owned companies, we have already operated with over performance of 54.4%, when compared to the regulatory EBITDA.

And Energisa Rondonia went from a negative EBITDA and now we are in positive, however, it is still lower than the regulatory level. In Acre since last year, we have

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overcome, we are above the regulatory EBITDA and there is still a lot more to do, but we can see that these companies are gradually being transformed into efficient companies.

In Slide 19, we're going to talk about our net profit. In the quarter, we recorded BRL749 million when compared to losses of BRL88 million in the second quarter of 2020. And here we have some exclusions, we have excluded non-cash and non-recurring effects in addition to other effects and the growth in profit is still relevant. The profit was BRL355.3 million between quarters or an increase of 397.1% or the equivalent of BRL218.9 million, and it's important to mention that Energisa maintained its tradition of paying for dividends every semester and decided to pay BRL0.65 per unit of dividends equivalent to 35% of the net profit in the semester representing BRL235.3 million. And then on August 18, 2020 the shares are going to be negotiated ex dividends and payments will be made on September 29th.

And then on Slide 20, we're going to talk a little bit about our debts, and it was BRL13.9 billion, representing a decrease of BRL314 million when compared to the debt in March 2021. And in the second quarter of this year, we performed 15 operations including expansion of deadlines, rollout which totaled BRL1.5 billion with a capitalization of BRL3.1 billion in the year and we have concluded the quarter with a robust cash position of BRL5 billion. And the average time of our growth that is 4.1 year and the average cost is 7.08% in the year when compared to 5.15 in March 2021.

CDI is our main index and it is a 64.9% of our debt. The leverage indicator, the net debt according to the adjusted EBITDA closed in June at 2.5 times when compared to three times in March 2021 and when compared to the second quarter of 2020, we represent an expressive reduction of 1.2 times. The covenant limit of the net debt by EBITDA for the 2021 year is 4 times, in other words, a more comfortable situation in this indicator.

And then moving onto the next slide, we can see our investments in this quarter, which were in the order of BRL909.2 million, an increase of 35.4% when compared to BRL771.5 million in the second quarter of 2020 and this increase was observed for electric and our non-electric asset values, and taking into account the electric assets, there was a growth in investments in the order of 41.3% or BRL226.3 million. And as of the total investments in this period, 78.6% were directed to the distributors and 13.5% to the transmissions that are being constructed. In regards to these investments and distributed generation, we have 11 ongoing projects, of which four have been inaugurated this semester with investments of BRL48 million and a capacity of BRL12.7 MWp.

And the investment for the second quarter this year, for the projects under constructions, we have a total of BRL125 million in Minas Gerais and Rio de Janeiro. And in 2021, we have record investments that totaled BRL3.8 billion. In the distributors we're going to have BRL2.8 billion invested in the transmitters. And in Rondonia, the expected investments are of BRL747 million, of which BRL314 million in electric assets and BRL410 million from special liabilities, including the interconnection of nine isolated systems in the second semester. And the concessions of Mato Grosso, Mato Grosso do Sul together represent about BRL1 billion in investments.

And then in the next slide, we're going to talk about transmission. We can see our enterprises transmission, which represent BRL283.1 million for the 2021 cycle, and we signed a concession contract on March 30 of Energisa Transmissora Amazonas with a payment of BRL239 million to Amazonas Geracao, and this refers to the acquisition of the existing assets in this concession. We have also received a 30% of the RAP in the month of May this year and this is retroactive to April. We expect an average anticipation between 12 and 18 months including retaliation of the existing assets. In the last month of June, we had a victory in the ANEEL auction, and this includes the acquisition of a new yard of 138-KV of Gurupi Substation in synergism with Energisa Tocantins Transmissora. And I finalize my presentation with very good piece of news, we had the approval of the VMDS and Basa [ph] for the funding of our transmission project in Tocantins and the amounts are BRL166 million and BRL327 million, respectively, totaling BRL493 million or about 75% of the estimated CapEx.

I thank you for your attention. We're now going to open for Q&A. Operator, please.

Questions And Answers

Operator

Thank you. (Operator Instructions) Our first question is from Carolina Carneiro from Credit Suisse.

Q - Carolina Carneiro

Hello. Good afternoon, everyone. Thank you for the call. I have two questions. The first one, in this semester, you had a very good performance in terms of default and this was before the most recent facts. I would like you to comment whether you expect to have any changes in this level because of the increases in the tariffs or if you haven't seen that yet and perhaps you have already worked or are trying to mitigate the impact?

And then the second topic, if you can comment, you have been very active in IGD and this week we've seen a new project to discuss EGD, which will probably be voted next week. And so could you please comment a little bit about your expectations of what it's being negotiated? Thank you very much.

A - Unidentified Speaker

Well, we're going to divide this answer. About the role of tariffs in the default, we have seen the results in the residential area and we did have an impact. We have had increases in default payments.

Now your second question. I'm going to turn over to Alexandre and Ricardo so that they can both answer this question.

Well thank you Carolina for your question. So you would like to know what our impression is about the project and what is the impact on our companies. The agreement has not been voted by the Congress, and this is how this will have to be solved. This is not

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beneficial for anybody, not for the distributed generation factor among others. And we have a 12-month period after the law has been approved. And for those who come in between month three and 18, the old rule will be applied until 2031 and those who come in after month 19, we will have gradual increases and Parcel B will have to be paid totally to the distributor. And so based on the view of the distributor and the difference between the payments of the whole parcel, and this payment in different steps is something that will probably lead to increases for the consumers. This is well known, we have been discussing this for a while.

There is a specific rule for shared cases after month 18 and 19, the parcel will be paid and then 40% of the transmission parcel and 100% of the tariffs. So I believe that we will have enough time to adjust to the rules and the assets will be managed in the long run. This is our opinion about PLD and its impact on the business.

Q - Carolina Carneiro

Thank you very much.

Operator

Our next question is from Andre Sampaio from Santander.

Q - Andre Sampaio {BIO 19422379 <GO>}

Good afternoon. I'd like to ask a quick question about Parcel B, I know that there is reasonable possibility that we will have an impact of inflation on the tariffs in addition to water shortage. So what do you see this for next year? Thank you very much.

A - Unidentified Speaker

Can you please wait a minute.

A - Alexandre Nogueira Ferreira {BIO 19917568 <GO>}

Hello, good afternoon. This is Alexandre. Regarding the prospective for Parcel B next year, what we see, in a welcome example, it's what happened this year, we are trying to do something with the government so that we can comply next year. We've seen this happen in early this year when we're trying to find solutions. We have had a winning solution. This is being dealt with ahead of time with more time than what we did last year. So, I do not see any problems for next year.

Q - Andre Sampaio {BIO 19422379 <GO>}

Thank you very much. That's perfect.

Operator

Our next question is from Marcelo Sa of Itau.

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Q - Marcelo Sa {BIO 16454581 <GO>}

Hello everybody. Well, actually there is a question by Andre, in the beginning of the year, Energisa carried out a study and it showed that if we did not control tariff increases, we would have an increase of 18% and then with all of the measures that were taken, we would have an increase in average of 10%. And then we have same in of Parcel B and other measures that were taken and ended up being successful. But I know that if we have a stock, which was not taken into account for next year and we have very high levels of EGES [ph] at high levels and I know that there is a lot of pressure and part of it somehow is already being taken into account. But we still have some amount left. And when we look at all of these factors next year, we're probably going to have another year with some tariff pressure. So, why do you think that the impact is not going to be as relevant for next year?

A - Ricardo Perez Botelho {BIO 2105867 <GO>}

Alexandre?

A - Alexandre Nogueira Ferreira {BIO 19917568 <GO>}

Okay, I'm going to answer it. Marcelo, good afternoon. Yes, you did mention a series of factors related to the tariffs and a large part of them will be minimized by the increases in tariff. We already had an increase in July and we will probably have another one next month after our public consultation so that we can have a reaction during this critical period of time.

And in addition to that, there are other actions that we can take. For example, ICMS, recently we learned that the actions in Acre and Mato Grosso were considered relevant, so we're trying to obtain the credits of these (inaudible). And there are other actions that are being evaluated. It's important to say that we do have alternatives as I answered in the previous question and it's important for us not to have this potential readjustments. We have different actions being taken into account and we do not think that there will be an impact.

Q - Marcelo Sa {BIO 16454581 <GO>}

Okay, great. And also talking about the water crisis, the government announced incentives for large consumers so that they change their consumption profile and I've seen different reports and consumer reports. And the way it was proposed, it does not seem that we will have a lot of a vision and it won't be very effective. The government also mentioned that it will announce a series of measures to encourage consumption reduction by residential and commercial consumers. Do you have any idea of what these measures are and whether there are any financial incentives? And if so, who will pay the bill? Will it be paid by the consumer thereon? Or how do you think that this is going to be implemented.

A - Unidentified Speaker

Well, this is just a comment. And perhaps I have the same level of information that you do. We are using our branches, our association to try to understand how this will work in terms of consumption. We're trying to better understand how these mechanisms are discussed, but we still do not know what they will be like. So it's very difficult for us to come to

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conclusions without more concrete information or information that have not been disseminated yet and that's not available to us.

Perhaps, we should look at past experiences of the previous water crisis and analyze what measures would be applicable today. So I don't really know how this will take place. We have had discussions with NIL, with the ministry. But the agents have not been involved in this discussion. We have requested our branches, our association for support. And we expect that in the near future, we will have more information on how this will be done. We understand that the water situation is complicated, it is critical. And we have different measures by the government regarding the management of the reservoirs, but we know that we will also have to have measures based on the demand and on consumption.

Q - Marcelo Sa {BIO 16454581 <GO>}

Okay, thank you very much. It is very clear. And now if you allow me to ask a last question regarding the tax reform, which is being discussed and the tax that changes all the time. But if we think that we will have some reduction in taxes, I would like to know how you see the impact of distribution? According to our understanding, a distributor that base 34% of tax income, this effect should be neutral that will be also included in the tariffs, but you have, for example, Sudan [ph] incident which have a negative impact because the tax reduction that you have will be minor because it will be calculated based on lower values. I don't know whether that's your understanding. We have discussed with our clients and perhaps NIL should review the regulatory framework. I would like to know if you have considered these possibilities and whether they make sense?

A - Unidentified Speaker

Marcelo, as you well mentioned, this reform comes and goes, there are different operations that are being conducted, but taxes of dividend and the reduction of the corporate amount, so the advantage you have in one region will be decreased because -- you will have advantage, but in terms of changes or regulatory changes, it would be a bit too early for us to say anything right now.

Q - Marcelo Sa {BIO 16454581 <GO>}

Excellent. Thank you very much.

Operator

Our next question is via webcast from Carolina Gazes [ph].

Q - Unidentified Participant

Good afternoon. I have two questions. First, what are the projects of the company for the long run? Can you invest in something outside of the energy sector? Also the market is more and more competitive, do you see any possibilities?

A - Unidentified Speaker

Bloomberg Transcript

Carolina Gazes, regarding the deadlines review projects, we have confirmed activities. We have tried switching your portfolio for distributed generation, renewable generation and also we're looking at other aspects. Right now, we do not see anything outside the market. And we do not intend to go into, for example, the sanitation market. We have to evaluate opportunities very carefully. The resources are a bit more stringent in other segments.

Operator

(Operator Instructions) Thank you. The Q&A session is now over. And I would like to turn over to Mr. Mauricio Botelho for his final considerations. Mr. Mauricio, please move on to your final considerations.

A - Mauricio Perez Botelho {BIO 2105889 <GO>}

Well, I'd like to thank you all for your presence in this conference call. We understand that the results were superior this quarter. They were quite sustainable throughout the year (Foreign Language) with assets that will generate higher returns reinforcing our business platform.

Operator

I would like to conclude our session today and I thank you for your participation. Thank you very much. The tele conference of Energisa is now over and we thank you all for your participation and wish you a good day.

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