

## Q2 2014 Earnings Call

### Company Participants

- Antonio Sergio Guetter, Chief Financial Officer and Investor Relations Officer
- Lindolfo Zimmer, Chief Executive Officer
- Sergio Luiz Lamy, Chief Executive Officer
- Unidentified Speaker
- Vlademir Santo Daleffe, Chief Distribution Officer

### Other Participants

- Maria Carolina Carneiro, Analyst
- Pedro Manfredini, Analyst
- Unidentified Participant

### Presentation

#### Operator

Good afternoon and thank you for waiting. Welcome to Companhia Paranaense de Energia Copel Conference Call to present the Earnings of the Second Quarter of 2014. We would like to inform you that all participants will be in listen-only mode during the company's presentation. Afterwards, we will have a question-and-answer session, when further instructions will be given. (Operator Instructions)

Before proceeding, we would like to clarify that forward-looking statements that might be made during this call related to the business perspectives of Copel, operating and financial projections and targets are beliefs and assumptions of the company's management as well as information currently available.

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

In this call, we have Mr. Lindolfo Zimmer, CEO of the company; Mr. Antonio Sergio Guetter, CFO and Investor Relations Officer; and Mr. Sergio Luiz Lamy, President of Copel GeT, and Vlademir Daleffe, President of Copel Distribution. The presentation that will be made by Copel's management may be followed at the company's website [www.Copel.com.br](http://www.Copel.com.br).

Now, we would like to give the floor to Mr. Lindolfo Zimmer, CEO of the company.

## **Antonio Sergio Guetter** {BIO 18681355 <GO>}

Good afternoon and this is Antonio Guetter, CFO and Investor Relations Officer. First, I would like to welcome you all to the call that will be presenting the second quarter of 2014 earnings of Copel. First, I would like to thank you for your presence, for the presence of those who follow this call, and I would like to mention that it is always a great, great pleasure to talk to you. I will be speaking slowly so that the interpreter may follow the presentation.

2014 has been a year of many challenges to the electric -- Brazilian electric sector because of the below average rainfall especially in the regions with the largest reservoirs. And in fact, together with the delay in the construction of many plants it has been bringing pressure on energy prices with a direct impact on customers.

Tariff adjustment of distribution companies is one example of that with more expensive energy, ANEEL has been authorizing significant adjustments to all companies in Brazil. And in the case of Copel Distribuicao, the agency established more than 35% adjustment. However, after a request by the company, ANEEL authorized the application of an average adjustment of 24.86% and the deferral of the remaining percentage, which will be restated by the IGP-M and recovered in the next tariff adjustments.

With relation to the highlights of the third quarter -- the second quarter, as you can see on slide number three, our net income was R\$248 million in line with what we delivered in the same period last year, a minimum difference on a year-on-year basis. Consolidated revenue grew by 48% and exceeded R\$3.1 billion, whereas the EBITDA closed the quarter at 467 million with a 6% increase. And this result is once again explained by the performance of our generating company especially by the sale of energy in the spot market and also the sale of energy produced by Araucaria thermal power plant that is once again or that February of this year started again to be operated by UEG Araucaria, a subsidiary of Copel and sold about 417 average megawatt, between February and June 2014 or the equivalent to this amount in spite of the growth in revenues across, with the purchase of energy once again impacted the consolidated result and considering only the second quarter figures, they went up incredibly 77% driven by the costs related to the thermal contracts and the re-contracting of energy in the A minus one and A minus zero auctions and the price of energy in these auctions was established at higher levels.

On the positive side, the captive market of Copel Distribution had a good performance and accrued 6% increase in the first half of the year, where the consolidated payroll cost was 5% lower in the first half year in fact is in line with the objectives that we listed in the sustainability plan of the distribution companies for 2014 and '15.

Lastly, we should stress the startup of the substation Cerquilho III is a 100% Copel in the interior of Sao Paulo State and the Caiua Transmissora de Energia SPE, where Copel has a 49% stake. All together these assets represent an increase of 40 million in Copel's RAP.

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In the renewable energy segment, we acquired 49% of the Sao Miguel do Gostoso wind farm, which has a 108 megawatts of installed capacity and is located in the State of Rio Grande do Norte. And we signed a partnership with WEG to increase the Palmas farm -- wind farm in the State of Parana. Very well, these were the main highlights for the second quarter.

Nevertheless, before we talk about the financial performance, I would like to give you some more color about the Copel Distribution tariff spend also about the Araucaria thermal power plant.

Now going to slide number four, about Copel Distribution tariffs. As you can see on slide number four, we should stress here that the average adjustment defined initially by ANEEL was 39.71% according to calculation available on Technical Note 193/2014, which took into account beside the significant increase in the cost of energy. The recovery of the -- of last year's deferral nevertheless by authorizing the adjustment, the agency decided to keep the deferral and it's approving a 35% adjustment, which was 20 lower than the one that we forecast before. And as you know, we requested the suspension of the adjustment with the perspective of increase of -- or the application of a new deferral, which was authorized by ANEEL thus the tariffs of Copel Distribution suffered an average adjustment of 24.86%. The remaining percentage, which is the difference between the initial and applied adjustment is equivalent to R\$900 million of which 276 refers to the 2013 deferral and R\$622 million refers to 2014 deferral as you can see on the slide.

It is always important to stress that deferral does not hinder the financial health of the company, where the deferred amount will be adjusted by or restated by the IGP-M and recovered in the next tariff adjustment.

And lastly still on this slide, I would like to draw your attention to the cost of the energy contracted by Copel Distribution. As you can see on the state of -- on the lower part of the table, the average cost of energy went up over 35% going from R\$130 per megawatt hours in the previous tariff year to R\$176 per megawatt hour in the current tariff year. And this increase is related to the increase in the cost of the energy acquired during the auction and higher expectation of thermal dispatch over the next 12 months.

On the next slide, slide number five, we here detailed about the amount received by means of the transfer of the CDE and ACR account resources. As you can see between January and April, we received over R\$1 billion to cover costs related mainly to the involuntary exposure and also to the dispatch of thermal power plants.

I would like to remind you that in this period, Copel Distribution was obliged to acquire energy in the spot market due to the involuntary exposure caused by the lack of auctions to rebut in sufficient amount the energy that expired at the end of 2013. However by the end of April the Distribuicao acquired 388 average megawatts in A minus zero auction beginning sale to distributors in May in average price of R\$268 a megawatt hour. After acquiring this energy, Copel Dis Co is 100% contracted until the end of 2014, which decreases the need for transfers of resources from the ACR account specifically about the second quarter, we received a transfer of R\$177 million to cover the cost referring to

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improve and disclosing all the amount recorded in the period. For the settlement of May that was postponed till the end of August due to the lack of resources in the ACR account that transfer has already been defined at 90 million, an amount that was not required during the quarter and for the June settlement occurred last week, no amount was authorized for the discuss.

And before talking about the financial performance, I would like to highlight the results of the Araucaria TPP. As I said before, it was significant contribution to the company's consolidated results. As you can see on slide number six, since February 1st, 2014 the plant operation is under UEG, Araucaria's responsibility a company that is controlled by Copel and that has 80% of its capital stock and the 20% remaining they belong to Petrobras, which the Araucaria does not have an availability contract and operate under the merchant modalities in which the revenue depends on the operation of the plant and the energy when produced is sold at the spot market.

So, for the five months of operation under Copel's responsibility, the plant produced about 1,500 gigawatt hours, which brought about a revenue of over R\$1 billion and resulted into a 334 million EBITDA and 245 million net income being 111 million in the second quarter impacting directly the company's consolidated result.

The plant is being dispatched in a recurrent fashion due to the low rainfall. The plant should continue operation until the end of the year and may be requested to operate even outside the order of merit such as was the case in June, when the spot price was lower than the CVU declared for the plant, which is R\$572 per megawatt hour minimum amount for which the plant sell the energy produced.

Now regarding the consolidated results of Copel, you can see on slide number seven that the operating revenue grew by 38% during the first half of 2014 exceeding R\$6 billion. The main drivers for this revenue hike were the 18% increase in the revenue from sales to end customers due mainly to the 9.55% adjustments applied to the tariffs applied by Copel Distribution in June 2013 and also the 6% growth in the sale of energy to the captive market of Copel Distribution during the first half of 2014 on a year-on-year comparison.

Also the 113% growth in the sales to distributors account stemming mainly from the higher revenues at the CCEE due to the sale of energy of UEGA Araucaria and also the energy sold in the spot market by Copel GeT, which ultimately benefited by the high energy price in the period in the spot market. And the availability of the grid, which is made up by the TUSD and TUST revenues went up by 9% basically due to the growth of the grid market of Copel Distribution.

And the other revenues that include the revenues from constructions, from telco, from gas and others grew by 12% reaching R\$984 million driven mostly by the growth in revenues from construction, R\$626 million and it is an accounting entry of the largest investment in distribution and transmission and also the 20% growth in the telco revenues that reached 80 million in the period.

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On the next slide, slide number eight, we show you the operating costs and expenses for the six first months of 2014 with a growth of 42% on a year-on-year basis driven in great part to the 43% increase in expenses with energy brought for resale, which exceeded R\$2 billion. And I'd like to remind you that this amount already consider the compensation of R\$1 billion by means of transfers from the CDE, the energy development account and also the ACR account, which were booked between January and April because where charges for the use of the grid grew by 44% in the period basically driven by the comparison basis effect one in the second quarter of '13, there was an extraordinary transfer of resources from the CDE account amounted to R\$200 million in order to compensate the costs, which are for the services of the system related to the dispatch of thermal power plants outside the order of merit at the beginning of 2013.

The first half of the year was marked by the increase in expenses with the purchase of gas by Compagas, which buy this fuel to supply Araucaria TPP, which since February operates under Copel's responsibility. Now payroll cost including social security benefits dropped by 5% and they are detailed on the next slide, where we also detail the control of the manageable costs on slide number nine.

As you can see on this chart, consolidated costs with payroll and third-party services dropped by 3.4% in the first half of the year and it compared to the IGP-M 6.2% in the last 12 months. This represents an about 10% drop in manageable costs, which shows the extent of our cost reduction efforts by the company. And the largest contribution to this reduction come from the lower expenses with compensation and charges coming from the reduction also on headcount over 2013 and we count on 8,573 employees currently it represents an 8% reduction on a year-on-year basis regarding our headcount.

As you can also see that the reduction in our headcount continues in 2014 and 74 people have enrolled in the incentivized voluntary redundancy plan and they left the company towards the beginning of the year.

I would like to highlight that analyzing just Copel Distribution figures, the reduction in manageable costs was 55 million in the half-year, which is in line with what we expected and according to our objective of saving a 100 million in 2014 to bring the results of the distribution company closer to the regulatory benchmarks that we intend to achieve in 2015.

On slide number 10, we separate the cost with energy brought for resale because at resale grew 43% amounted to over R\$2 billion in the first half. The purchase of energy in the regulated market grew due to the contract of 511 megawatt and the A minus one auctions held in late 2013 and the sale to distributors just started in January this year and the hiring of 388 average megawatts in the A minus zero auction, the sales of distributors started in May ended both auctions of price the energy was established at high levels, as we have already referred to.

I would like to mention that the inflow of new energy contracts in order to meet the needs of the growing market and also the higher cost with the thermal power plants also had an

impact as a monetary restatement of contracts in force, which were restated by the inflation in the period besides the higher cost to the contract in the regulated market.

The cost with the purchase of energy at the CCEE grew due to the high spot price, whereas the cost at ITAIPU grew driven by the increase in the amount of energy bought and also by the depreciation of the dollar in the period.

Going back to our earnings on slide number 11, we can see that the consolidated EBITDA grew by 20% in the first half amounting R\$1.3 billion with a 22% margin on the operating revenues.

Cash generation by Copel GeT accounted for 93% of the consolidated EBITDA, whereas Copel Telecom represented 4% and the other companies and the Group only 3% impacted by the result of Copel Distribution. The group had a negative EBITDA 316 million in the half year, as a consequence of again of the higher cost with the purchase of energy, as we've already shown. EBITDA margin of Copel GeT reached 74% on expected figures, Copel Telecom, 56%.

On slide 12 we present the consolidated net income of Copel, which was 831 million in the first half year of 2014 and amounted to 28 higher than the one achieved in the same period last year. Net margin was 13% basically in line with the results of the previous years. Analyzing the results of the subsidiaries, we can see that Copel GeT ended the first half of 2014 with R\$821 million net income 48% higher on a year-on-year basis and with a net margin of 50%/ Copel Telecom posted 28 million net income corresponding to a 21% increase on a year-on-year basis. Copel Distribution in its turn posted a loss of R\$229 million in the first half of the year once again the consequence of the high cost with the purchase of energy. Very well, these were the main highlights about Copel's results. However, before finalizing, I would like to make a few remarks about the startup or transmission projects and new investments in renewable energy.

As you can see on slide number 13, at the end of July substations Cerquillo III an asset, which is a 100% Copel GeT and Umuarama, Guaira and Cascavel Oeste, Cascavel Norte transmission line were started up as well as the substation Cascavel Norte, Santa Quiteria all these belonging to Caiua Transmissora de Energia and SPC, where Copel has a 49% stake. All together the ventures are already delivering an additional rack of R\$14 million. Besides in the renewable energy segment, we acquired a 49% stake in the Sao Miguel do Gostoso wind farm located in Rio Grande do Norte State with 108 megawatts of installed capacity.

And lastly, we signed a partnership with WEG for the construction of the Palmas II wind farm in Parana. All in all these were the highlights of Copel's result.

Now we would like to invite you to participate in the APIMEC meetings that we will be holding next week. For those who are in Sao Paulo the event will be next Wednesday, August 20th and for those, who are in Rio, this meeting will be on August 21st, Thursday. You may enroll at the regional centers of APIMEC or you may contact our Investor Relations area.

Now, would like to open for questions from the audience.

## Questions And Answers

### Operator

Now we will start the Q&A session (Operator Instructions) Our first question comes from Giuliano from Itau BBA.

### Q - Unidentified Participant

Good afternoon, everyone. I have two questions. As you have raised R\$1 billion for the next tariff year. What about the impact that this had on your appetite for new investment? What about A-5? What is your expectation should you expect for the next few months?

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

Thank you for your question. I like your questions very much. You asked that we do have the same appetite for investment of course in this situation the company has to review the way and invest its resources with the limitation in resources of course we have to be careful. However this does not mean that we will not continue to participate in the market in a consistent fashion such as has been the case until now. Good opportunities will be considered.

And of course, we will be willing to participate of course we'll have to reshuffle our investments and revise our time schedule for investments and the -- obviously requires revisiting this area of investments so that we may mitigate this restriction, this limitation of almost 1 billion.

But I understand we will be surviving in a very healthy fashion through this moment because on the one hand, we have difficulties on the other ahead we have opportunities. Araucaria is bringing this balance and we are being able to keep our place. So, we will always pay very keen attention to investment opportunities and according to the guidelines that have always guided the company that is to see investments that may be healthy and be a very good investment on funds. Your other question was about the participation in the A-5, our team is prepared and it has been tackling the issues and up to now we are enthusiastic about the possibility to participate.

And of course the details and the studies and the conclusion of the studies will be fine tuned to the extent, we can increase or decrease our appetite, but in principal we will be participating.

### A - Sergio Luiz Lamy

Good afternoon. This is Sergio from Copel GeT, Sergio Luiz Lamy. Regarding GSF for the second half, 0.9 is the figure we estimate, maybe slightly lower than 0.9 now in August. And as of October, this should be growing up slowly reaching 0.94, 0.96 towards the end of the year, okay?

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## Q - Unidentified Participant

Thank you.

## Operator

Our next question comes from Mr. Gabriel from Safra Bank.

## Q - Unidentified Participant

Good afternoon. Along the same lines of our GSA, I would like to understand in generation if you intent to ask for compensation due to the impact and if it does occur if this is required to be separately made by Copel or whether you will be doing this with the other members of the association of generating companies? And what would be the possible rationale to justify this reimbursement or this compensation?

## A - Unidentified Speaker

This is Lamy from Copel Generation. We do not have a final position regarding this theme, regarding this request to be submitted to ANEEL we are debating this theme in the forum of the association Araucaria et cetera, and we have not come to a conclusion yet. But if we submit a request, of course, Copel will not be alone in that. Copel will be doing it -- this together with the associations.

And the rationale that seems to us to be relevant for this kind of request or claim is the quality of the thermal generation contracted with excessively high costs for generation. And the generation are -- they are subject to this high amount in the case of a lower generation. And the planning for expansion, there is responsibility for the expansion and there is production of this more responsibility lies in the hands of the regulators. So, our hands are tied and this is a risk that doesn't seem to be reasonable as far as we are concerned.

## Operator

Pedro Manfredini from Credit Suisse. You may proceed.

## Q - Pedro Manfredini {BIO 21633245 <GO>}

Good afternoon, everyone.

I have two quick questions. The first one is about Araucaria. We saw the success of the Araucaria endeavors. So what is your strategy regarding Araucaria? In the past it was leased to Petrobras for some time. So what is the alternative that you have for 2015 and '16? What are you planning to do with Araucaria?

The other question has to do with Colider that Colider would have to come in the next few months in the grid? And what about construction? What about the status of this project? Could you give us an update?



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## **A - Lindolfo Zimmer** {BIO 2132989 <GO>}

Pedro, this is Lindolfo. About Araucaria of course this year, we will still require Araucaria to dispatch until the end of the year until the arrival of the new rainfall season, the normal period and this would decrease the chance of Araucaria continuing to dispatch for the next year. But we do not know what the future holds maybe the situation is not as I described it maybe, it continues to be necessary. I would like to share one characteristic of Araucaria. It operates due to security reasons for the system for the center of gravity of the south region. And from the electricity viewpoint, it might be necessary to guarantee the stability of the whole system that covers our region. So, the possibility of dispatch of Araucaria is higher than the merit of keeping costs it goes beyond that.

On the other hand, we expect that with the evolution that -- of exploration that could bring gas at a lower price, this will mean opportunities for Araucaria to dispatch more frequently \$23 per Btu and it's already supplied by Petrobras and there's nothing we can do about that. We expect to get gas that is more competitive and may allow us to dispatch more. Anyway if it dispatches integrally such as is being done, Araucaria will have performed its role giving the results that were expected by us, okay?

Regarding Colider, our project is lagging behind, in fact, and we're working considering the beginning of commercial operations in the second half of 2015. And this delay in the project was driven by the fact that we are not under the responsibility of the company and that were aggravated by characteristics of the region, where it is being built.

Many construction activities, for instance the dam cannot be built in a rainy season. And in that region, you have half of the year with a lot of rainfall. And other events that are not under the responsibility of the company and because of these facts, there was a delay in the construction.

So regarding this question, Copel GeT has own energy reserves of course, because we are very cautious and we have to deserve to comply with our commitment. But undoubtedly, we will be submitting to ANEEL a claim for exclusion of responsibility in this regard so that we are not hindered by factors that are not under our control and that are not under our responsibility therefore.

## **Q - Pedro Manfredini** {BIO 21633245 <GO>}

Still regarding Colider, you said about exclusion of responsibility in your claim. So do you think the contract could be extended? If you are able to get the exclusion, can you roll it over for in another six months? Or is it just a matter of not being penalized? Do you have this facility regarding the concession extension?

## **A - Unidentified Speaker**

Yes, we are going to submit this report as well of extension of the concession terms.

## **Operator**

Carolina from Santander.

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

Good afternoon. Two questions. What about the energy balance that you always make available? I don't know I was a little bit late connecting to the call, I don't know whether you referred to that or not. But could you give me an update regarding the amount that you have available for next year without the contract and that could serve as a hydrological hedge?

And the second question, probably the regulatory agenda is rather complicated. But do you have any update regarding the concession renewal process for distribution? We know that it is only next year that we will see some movement, but you probably have talks with the regulators. So do you have an idea of the time frame and when we will have news about parameters and the announcement about the decision of ANEEL? Any additional information about this project?

## A - Sergio Luiz Lamy

This is Sergio Lamy. I will answer the first part of the question regarding the availability of energy next year. Then I will pass the microphone over to Vlademir from Copel Distribuicao that will answer your other question. Our availability of energy for next year is around 13% of our critical guarantee around 250 megawatts for instance, more or less.

## A - Vlademir Santo Daleffe

This is Vlademir. We have been maintaining frequent contact with the regulator with ANEEL. As you know that the agency is federal and they will -- the federal government will be defining this. And there are two issues involved. The main one is that the fundamentals that will be guiding this decision have already been achieved. So Copel, over the last few years has been the national benchmark.

And as you have issues involved regarding sustainability and balance, economic and financial balance, we have been able to get significant reduction, over R\$100 million last year; last half year, R\$55 million. If you consider the inflation, it will mean significant productivity gain and we have already submitted to ANEEL the fact that we would be reaching the desired sustainability level up to 2016. And our projections for 2015 already -- and as ANEEL should have manifested itself about our claim for renewal that should have (inaudible) journey that has not happened yet. What happens is that in a few months, it will not be possible to make the transfer of control so to say. So all in all, our expectation is rather bullish.

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

One last question. We have the impression that you had a positive allocation in the first half, since you had a partial tariff increase that you have deferred for next year. And practically, your results will be more pressured and maybe because there are heavier GSF in spite of the Araucaria operation. So could you please talk about your cash balance and how do you manage to maintain dividend payout policy if there will be any change in that if you will keep the same dividend payout that you had last year due to the pressure that we see from now on? So could you please tell us what you see as a possibility of dividend payout vis-a-vis last year given the current situation?

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

Carolina, this is Antonio Guetter. You've asked two questions one about the financial and economic balance. And as our CEO said at the beginning of the Q&A, we made a reassessment of our time schedule for investments and we estimated R\$2.6 billion. If this investment is -- so we reviewed our time schedule in order to keep our cash level that is totally under control.

And about the dividend policy, our idea is to maintain this policy and getting closer and closer to the average of the market. But of course, we will be assessing rather prudently and on a timely fashion the dividend payout situation. But in principle, we are favorable to maintaining the dividend payout policy that we have been maintaining at Copel in the last few years.

## Q - Unidentified Participant

Thank you very much.

## Operator

As there are no more questions from our participants, we would like to give the floor back to Mr. Lindolfo Zimmer for his closing remarks.

## A - Lindolfo Zimmer {BIO 2132989 <GO>}

Once again, I would like to thank you all for participating in this call and it was a great pleasure for us to present our results to you and talk about the perspective for the future. So, once again, thank you very much and I wish you a very good weekend and say that our Investor Relations people and our financial team are available to you, if you need any further clarification as well as the other areas of the company, generation, transmission and distribution with Vlademir, Guetter and Luiz. And thank you very much and have a good weekend.

## Operator

Ladies and gentlemen, Copel's conference call about the results of the second quarter of 2014 is closed. Thank you very much and have a good afternoon.

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