

Q2 2020 Earnings Call

Company Participants

- Fabio Antunes Fernandes, Chief Financial Officer, Investor Relations Director
- Marco Antonio Resende Faria, Technical Officer & Member of Executive Board
- Marcus Vinicius do Nascimento, Director of Business & Management of Holdings, Director of Implementation and Member of Executive Board

Other Participants

- Carolina Carneiro

Presentation

Operator

(Call Started Abruptly) -- that will lead to results that will differ materially.

Now I would like to turn over to Mr.Faria, CEO and Technical Director of Taesa. Please, Mr.Marco proceed.

Marco Antonio Resende Faria {BIO 16679297 <GO>}

Thank you. Good morning. I would like to thank you all for your presence in this conference on the results for the second quarter 2020 of Taesa. I have here with me the CFO, Fabio Fernandes; the Business Director, Participation Management and Implementation, Marcus Vinicius.

Before I start my presentation, I would like to make some comments that I consider to be important on how we have acted during this crisis. This unprecedented crisis.

Moving on to Slide number 2. I'd like to highlight how Taesa has tried to minimize the impact of the pandemic. In the second quarter of 2020, we had a lot of challenges because of the increasing expansion of the pandemic of COVID-19. As a golden rule for the company, we remain committed with the health and safety of our employees and our assets that are connected at a national level. We have intensified the care that was initially implemented because of the expansion of the pandemic.

We have kept social distancing using home office, and we've been doing so for 5 months now. We have hired specialized medical consultancy to help us implement the safety protocols from the very beginning of the pandemic. We're also very carefully starting and doing so according to all of the safety protocols to have a gradual return to our activities. But once again, I would like to reinforce that we are following the guidelines established

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by each one of the different municipalities and above all, respecting the specific characteristics of each one of our employees.

We have performed adjustments to home office and are providing the required support so that our collaborators and family members can take care of the physical health, mental care. We monitor our team. We monitor the implementation of the protocols and follow up everyone's health status. And as I mentioned before, all of our employees are monitored and the cases that are suspected to be positive are being carefully watched.

From the point of view of the continuation of our operations, we have adopted even more restrictive measures in our operation activities. We have intensified our contingency plans. And furthermore, we have started a confinement regimen of the operators who worked in Taesa's control center. They are essential for the operation of the national electric system. I'd like to remind you that in certain cities, we have seen that these measures have been not followed strictly, and we see an increase of the contamination by that disease.

We have been very careful and responsible. That's why our activities supported by -- and our operations have allowed us to keep the same level of productivity with operational excellence. We never stopped quite the other way around. We are applying the best maintenance practice to guarantee the stability and maintenance of our electric system. Our lines are available. And the rate of availability has been very high with 99.96% of availability with a variable of 1.6%.

Furthermore, we have had important advancements in the projects under construction. And in the total for the year, we have accumulated almost a BRL700 million in CapEx -- BRL700 million. And I will talk more about this later on. Because of the extension of the pandemics and also the regulations of different municipalities, which have imposed even more paralyzation, we have had a slowdown in our constructions, but the company has been dedicated to try to meet our schedules and deadlines.

In the third pillar, about the financial health of the company, we have closed the first half of the year with a solid liquidity position in adequate leverage level. In April, we captured BRL900 million to reinforce our cash position. We do not think we have to raise anymore until early next year. We have consistent operating cash generation, maintaining the company's low historical default levels. In other words, even with all of the difficulties, the companies in the electric sector have honored their commitment and made payments to the transmission sector, and this is very positive. It is positive in the face of the dimension of this crisis.

I would like to highlight that the recent regulation of COVID to support the distributors, which were the ones that suffered the most impact from demand and default point of view, it was essential to allow us to avoid potential systemic risk, which was until then the greatest threat to the sector and the country. The joint activity of the Ministry of Mines and Energy, ANEEL and other agencies in the sector was essential for us to find a quick solution to this issue. However, we will continue monitoring closely the default levels to guarantee adequate liquidity and operational activities of Taesa. So whenever we talk

about this topic, I'd like to highlight that Taesa is always concerned with its different stakeholders and has advanced in the communication and practices related to environmental and social issues and governance, and we have discussed this with investors in the local market, which pursue sustainability in their investments, going well beyond the financial gains, trying to think of generating value and the purpose of the company.

So moving on to Slide 3. The company has created initiatives and identified opportunities for a clear communication of the social-environmental activities and governance activities, which are in force at Taesa, and that in addition to the pursuit for continuous advancement in best ESG practices. In this regard, we reinforced the sustainability project last year, which pursues improvement or continues improvement in sustainable actions among the improvements that were implemented. I'd like to highlight the annual report of social-environmental responsibility in phase of the global reporting initiative methodology.

The global pact of the UN is a voluntary initiative that promotes a communication among companies, corporations in different UN agencies on social and environmental responsibility policies. Today, the pact is the largest sustain -- corporate sustainability initiative worldwide with over 13,000 members scattered over 160 countries. The idea is to foment the social dimension of globalization, aimed at aligning our strategies and operations to the ten universal principles in the area of human rights, labor, environment and anticorruption, developing actions that may contribute to face the challenges in society.

With that commitment, Taesa hopes to contribute with the reach of the sustainability global agenda, whose main pillar are the 17 objectives of sustainable development. I'd like to highlight important advancement in our annual report of social-environmental responsibility of 2019, which was disseminated in June -- last June. It was based on the ESG aspects and report Taesa's actions in consonance with the global pact of the UN and the objectives of sustainable development.

I would also like to highlight some important initiatives and awards that demonstrate the company's position. We performed four large mission of green titles in the capital market last year. We also have social-environmental responsibility projects and social communication and environmental education campaigns in the communities that are impacted by their alliance, in addition to carrying out environmental impact reduction program in our enterprises to compensate the environment and recover degraded areas, for example. Also, I'd like to highlight Taesa's environmental management guidelines and the health policy also for the environment and safety.

Among the awards, I would like to highlight the Great Place to Work certificate and also the award for the -- as a best company in the segment of energy in the area of safety, health and work by ANIMASEG. Both were obtained last year. These awards demonstrate Taesa's commitment with well-being.

And I now turn over to Fabio Fernandes, our CFO, and IR Director, to present our results.

Fabio Antunes Fernandes {BIO 21749197 <GO>}

Thank you, Marco. Good morning, everyone. I will try to be brief during my presentation so that we have more time for Q&A, which will be more productive and interesting for us.

So I'm going to start with Slide 4, highlights for the second quarter of 2020. Our first highlight was the performance of our IFRS net income, which totaled BRL437.8 million, and in the next slides, I will provide you further detail.

As a second highlight, we observed that this was the first quarter -- the second quarter this year was the first one that we had a positive impact of the consolidation of results. And I would like to remind you that we delivered Midas CMIBT [ph] and Novatrans reinforcements. And in the first part of this year, we concluded Sao Joao, Sao Pedro and Lagoa Nova acquisitions.

I would also like to highlight that in the comparison with the second quarter of 2019, the acquisitions of participations in ETAU, Brasnorte and Transmineiras in Eletrobras auction also had a positive impact on the results of the second quarter of 2020.

I would also like to highlight that even in a scenario of adversities, we have successfully concluded the integration of the new assets obtained in the primary and secondary market. And these achievements show the commitment and total dedication of our teams in such a difficult moment.

The third highlight was the improvement in the financial results in over 60% in the annual comparison. This effect is due basically to the deflation accumulated of 0.43% in the second quarter of 2020. And that combined to a higher volume of IPCA debt substantially decreased the financial decreases in the quarter. Even with lower financial revenue, we had an improvement in our financial result of BRL43 million so when compared to the same period in 2019.

Regarding the distribution of -- to our shareholders, we have monitored closely potential impacts of the crisis on Taesa's business, and we'll continue evaluating the distribution of dividends. Because this part, we have not observed significant impacts on the business and cash flow and financial health of the company, we are carefully and in a disciplined manner distributing for the second quarter of 2020. And therefore, our Board has approved the distribution of BRL279.3 million, which represents BRL0.81 per unit, including interest rates on our own capital and dividends based on the financial demonstrations of June 30, 2020. With that, we have a payout this far of 65%. But if we consider the adjusted net profit, which does not take into account the CPC 47, we have a payout greater than 90%.

The last highlights in the slide talk about the maintenance of a solid position and liquidity and continuity of investments in the businesses. I would also like to highlight that we will continue working based on the pillars of financial discipline, always monitoring the current crisis closely and also the impacts on our business.

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Moving on to Slide number 5. We have the net income under IFRS. And as you can see on the graph on the left, the main factors that explain this performance of the net income under the IFRS were the implementation of infrastructure margin, that increased due to higher investments in projects under construction, which are 100% Taesa, and therefore are consolidated and have a positive impact on Taesa's implementation.

The equity method improved because of the concessions. There was an increase of implementation margin also in our participations. We have observed a reduction in financial expenses mainly due to the accumulated deflation of IPCA in this quarter.

Finally, it's important to highlight the consolidation of the results of the new brownfield and greenfield assets, 9 in total, which have added approximately BRL25 million to the IFRS net income.

In Corona, we had the following negative effects on IFRS. The reduction of BRL39.8 million in monetary adjustment because of the lower macroeconomic levels recorded in these periods, an increase of BRL18 million in PMSO due to higher operating expenses and implementation, especially because of the beginning of the operations and the new concessions.

We also had some recurring effects, which I will better explain later on. We also had increased taxes because of the profit before taxes. The tax benefit of interest on our own capital was reduced, and therefore, it increased the quota for the quarter. It's important to highlight that the adjusted net profit had an increase of 16.3% in the comparison between the quarters as can be seen on the graph to the right.

We now move on to Slide 6, and we'll talk about the macroeconomic impact on IFRS revenues. I'd like to show you the strong correlation with IGP-M, as you can see in the graphs on the top and on the bottom. I'm not going to get into details. The correction -- monetary correction was not a highlight, but even with a negative IPCA accumulated in the quarter, the adjustment was of almost BRL75 million in this period, especially because of a high -- of the high levels recorded by IGP-M, which was 2.34%. I'd like to remind you that our IGP-M exposure has to do with our assets that have to do with Category II concessions.

Right now moving on to Slide 7, where we will talk about the regulatory results. The regulatory revenue for the second quarter of 2020 closed at 375 -- BRL385.7 million with a growth of 7.1% when compared to the same period of 2019. After 2 years of recurring decreases, having -- we had the first increase, and we can see that, that added to the inflationary readjustment is greater than the effects of some Category II concessions. As you can see, in the revenue graph, Sao Joao, Sao Pedro, Lagoa Nova, and the conclusion of Miracema, Mariana, and the capacitors had a positive impact on our net revenue of BRL68.9 million. There was a positive effect of BRL24 million. These effects when combined were higher than the negative effect of BRL63.7 million, regarding the decrease we had in some, Category II concessions that occurred in 2019-2020.

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On the lower graph, with the regulatory costs, we can see the investments in operation, and there was an increase of BRL7.4 million in PMSO. We also had some nonrecurring events totaling BRL5.3 million, which pressured our costs, including contingency prognosis, strategic consultancy, hired, among others. If we exclude these costs, PMSO would have increased because of the new assets, but that also had a positive impact on our net revenue. When we look at these assets, we have a consolidated EBITDA margin of 67%. In other words, the inclusion of the new -- these new assets generates value, which is very positive for us.

Another very important aspect to be observed in this slide is that when we exclude the RAF, we would have had an increase of 24.8%. This demonstrates that we have tried to be very diligent with costs and our results are due to the growth of the company.

I now turn over to Marcus Vinicius, who will conclude the presentation with a brief summary of our projects under construction.

Marcus Vinicius do Nascimento {BIO 21749203 <GO>}

Thank you, Fabio. Good morning, everyone.

In Slide number 8, I show you the status of the projects under construction at Taesa. So in addition to Mariana, which was delivered last May, we have Miracema and NDTE [ph], which were delivered at the end of 2019 and early this year, as mentioned by Marco and Fabio. But we currently have investments under construction. We reached almost BRL700 million in the accumulated of the year. We will work to be able to deliver them according to our schedule. However, as mentioned, we have had a deacceleration in the constructions in some sites. We are working carefully to minimize the potential impact in our schedule, trying to meet the delivery deadlines that was hired with the different companies.

Our vendor management committee is trying to readjust everything, informing ANEEL on a continued basis about the construction, and we also demand to receive updated information on the status of the construction from our contracted constructors.

Considering the current scenario, this is all very positive. We have obtained environmental licensing. And as you can see in the slide, we have advanced in all different projects.

So this is what I had to share with you. We conclude our presentation and now open for Q&A. Thank you very much. We remain available.

Questions And Answers

Operator

(Question And Answer)

(Operator Instructions)

A - Marco Antonio Resende Faria {BIO 16679297 <GO>}

Good morning, everyone. We have received a question via webcast from Casu. Thank you for your question Casu. The question is, what is Taesa's perspective regarding the activity at the end of the year. I'm going to turn over for this question.

Casu, you asked the question. We are evaluating the 11 lots of the next auction, which is scheduled for December 17. Of course, Taesa will participate. We have studied all of the lots that are available. And we will concentrate ourselves on those that make better sense in terms of competitiveness, keeping our financial discipline and always trying to pursue adequate returns to our business.

And our appetite for these lots will depend on some factors, including CapEx payments, which will be close to the operational activities. And we should also consider some partnerships, some of them, we have already been working with, and others are being analyzed.

There's an item here regarding -- that was published by ANEEL regarding RAF and CapEx, and these studies are detailed and more in depth.

In addition, because they cannot sell the lots under construction, we believe that competition will remain tight with a lower number of lots.

This is our position right now. And we are available to discuss other aspects. I thank you for the opportunity.

Operator

(Operator Instructions)

A - Marco Antonio Resende Faria {BIO 16679297 <GO>}

Good morning. We have received another question. A question from Leonardo Aguiar. Thank you for the question, Leonardo. If there is a cap for the net debt? Fabio will answer your question.

A - Fabio Antunes Fernandes {BIO 21749197 <GO>}

Thank you, Leonardo, for your question. If we take into account the net debt for the companies that are controlled at the end of the first quarter 2020, we still had a ratio of 3.3x, which is a little bit higher than what was recorded in the first quarter of 2019, which was 3.0. However, I'd like to remind you that the company does not have debt coverage. Our reference is the maintenance of our AAA rate in the 3 rate agencies. Within this context, our expectation is that by the end of the year, probably because of the CapEx payments for Santa Angela [ph] investments, this will be higher. This index will be higher. But as of 2021, when the projects start operating, we will have a quick deacceleration of

this index, which will lead to a reduction in our leverage. This is what we see for this index here at Taesa. However, emissions do not have debt coverage. We always operate based on a quick deleveraging because of our capacity to generate cash.

Operator

(Operator Instructions)

A - Marco Antonio Resende Faria {BIO 16679297 <GO>}

Good morning. We have received another question via webcast from Bruno Lima. Do you believe that even with RAF reduction, the payment of dividends will be capped at the same rate as in previous years?

I will turn over to Dr.Fabio for his answer.

A - Fabio Antunes Fernandes {BIO 21749197 <GO>}

Good morning, Bruno. Thank you for your question. Regarding the RAP reduction, we have reductions of smaller companies ahead of us. So they are not very significant when we consider the total RAP and that will be diluted in the next cycle. So what we see is that this reduction, which will be observed in the upcoming cycles will be compensated by the adjustment of inflation in the -- when compared to the RAP of the other companies and also because of the new projects, which will have a positive impact as of 2021. So within this context, where we see that this reduction will be absorbed by these two factors basically. We understand that the capacity to pay dividends of the company would not be directly affected by this reduction.

Operator

The next question is from Carolina Carneiro, Credit Suisse.

Q - Carolina Carneiro

Hello everyone. Good morning. Thank you for the call. I would like to ask you to share a little bit about the growth perspectives via M&A. You announced some new acquisitions, but I would like to have an idea of what the market is like after COVID? What the market is like for this kind of asset, the secondary asset? Do you think that anything has changed in terms of multiple for the acquisition of these assets because of our current scenario and perhaps even more intense competition of other players, which participate in this M&A market with you.

A - Marcus Vinicius do Nascimento {BIO 21749203 <GO>}

Carol, Marcus Vinicius here. We have seen that the market has presented opportunities. We are evaluating all of the opportunities for the company. We are exactly doing this internal exercise. We are evaluating a few cases. We have a package of actions, and of course, we are analyzing which one would add value. And of course, that this position we have today will -- is based on doing what will add value. Regarding the position of the

company, we think that some investors might change. We are careful. We are watching. We are already evaluating some projects. And in the near future, we will have news to the market about this as soon as possible, hopefully.

Q - Carolina Carneiro

Thank you very much.

Operator

(Operator Instructions)

A - Marco Antonio Resende Faria {BIO 16679297 <GO>}

We have received another question via webcast. Adamir asked us to explain the risks of default that were mentioned during the presentation. I'm going to turn over to Fabio.

A - Fabio Antunes Fernandes {BIO 21749197 <GO>}

Good morning, Adamir. Thank you for your question. For the transmission sector, the highest risk during pandemic was on the distribution issue. Because of the COVID account, the government turned -- or the government neutralized this risk, so that from the beginning of the pandemic until now we have not observed any impact on our default levels resulting from COVID.

We have the same historical default levels in the company in the average of 0.5%. And we are monitoring this on a daily basis, so that if anything happens that will affect this historical average we will take the required actions. But so far, we have not identified anything that might have an impact on our default levels. We have robust contracts, and they guarantee payment in a satisfactory manner.

Operator

(Operator Instructions) Since we have no more questions, we turn over for the final considerations.

A - Marco Antonio Resende Faria {BIO 16679297 <GO>}

This is Marco Faria. I'd like to thank everyone for the participation in our teleconference. I thank you very much, and wish you all a good day.

Operator

Taesa's teleconference is now over. Have a good day.

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