

Q1 2013 Earnings Call

Company Participants

- Antonio Previtali, IR Manager
- Elio Wolff, Market Relations Manager of GDF SUEZ Energy Latin America
- Manoel Zaroni Torres, CEO
- Unidentified Speaker, Unknown

Other Participants

- Carolina Carneiro, Analyst
- Felipe Leal, Analyst
- Gabriel Lyra, Analyst
- Sandra Boente, Analyst
- Vanessa Knowles, Analyst
- Vinicius Canheu, Analyst

Presentation

Operator

Good morning. This is Tractebel Energia conference call. All participants are connected in a listen-only mode. Later we'll open a Q&A session when further information will be given, will be provided to you. (Operator Instructions). We would like to remind you that this teleconference is being recorded.

I'll now turn the floor to Mr. Antonio Previtali, Tractebel's Investor Relations Manager. Please, Mr. Previtali, go ahead.

Antonio Previtali

Good morning, ladies and gentlemen. Welcome to Tractebel Energia's conference call where we'll discuss the results for the First Quarter of 2013. This conference call together with the slides will be simultaneously broadcast via www.tractebelenergia.com.br at the Investor section where you will also find the earnings release and presentation.

Before proceeding, I would like to clarify that statements that may be made during this teleconference regarding business outlook of the Company should be treated as forecasts. They depend on the Company's macroeconomic conditions, performance and regulation of the electric industry in addition to other variables and therefore they are subject to change.

We have today together with us Manoel Zaroni Torres, Chief Executive Officer, who will talk about the performance of the First Quarter 2013; and Elio Wolff, Market Relations Manager of GDF SUEZ Latin America who will talk about Jirau hydropower plant.

Right after the presentation they will be here to answer any questions that may be asked. I now turn the floor to Mr. Zaroni. Please go ahead.

Manoel Zaroni Torres {BIO 20231580 <GO>}

Good morning, everybody. Let's go straight to the highlights for the First Quarter, slide number 4, where we have the most important financial and operational highlights. Our net revenue from sales, when we compare the First Quarter of 2013 to the First Quarter of 2012, we see an increase of 20.6% attributable to -- explain why we have traded more energy and also we have followed a strategy of energy allocation.

As you remember, in the past we were short in the first half of the year and this year we are selling. So we are long. This owes itself to CTE [ph] EBITDA increase 22.2%, the margin EBITDA NRS 62%. The net income was BRL424.9 million, almost BRL425 million. It increased 29.8%.

Energy sold increased by 7%, the average price of energy contracts increased 5.2% basically due to contract adjustments and the average position also increased because of the firing up of thermal powers in addition to the hydraulic. So it's because of MRE, but it grew 11% in terms of production.

As highlights we would like to say that the Company beat its own instantaneous generation record. So we produced 7,757 megawatts in the last instance. On March 21st, we started operating at full capacity at 1,087 megawatts in HPP Estreito, where we have 40.07% share of the production. So the eight units have started operations in March.

The Board of Directors has approved the acquisition of CLWP Brasil (inaudible), which is the holding company, the specific purpose company, to develop seven wind generation projects in Campo Largo in the southern part of Bahia and we have already approved a project for 206 megawatts and we can expand it further to another 150. The projects are located in the state of Bahia and we are going to start the projects when we have auctions or when we have the opportunity to sell to special customers.

On April 25th, Fitch Ratings reaffirmed our international rating. So in BBB and the Long Term National Scale Rating it has reaffirmed with a AAA Brazilian with a stable perspective.

Slide number 6 shows our shareholder strategy or structure. The only relevant information is that Mayeza [ph] is no longer here. Mayeza was -- we had a consortium, Tractebel and Mayeza. And Mayeza has different partners in addition to Tractebel; (inaudible) and other companies. So Mayeza was dissolved and now the consortium is a consortium among the partners of (inaudible), the only highlight of this slide.

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Slide number 7. Here you have our diversified portfolio and its growth. Let me remind you that we have 17% of thermal plants in our portfolio. So in these stages of high cost price it may make a difference in the results, the end results for the Company.

Slide number 9 shows that we're reaching our target. We wanted to have 50% sold in the regulated market and 50% in the farther free market, and we're reaching there. 2013, our projects are here 50% for the regulated market, 8% for the trading companies and 41% in the free market. It is something we have been focusing on.

Slide number 10, here you have our portfolio from the buyer side. We reached 1,710 average megawatts. That's something we have never reached before. Actually we are selling a lot of energy and getting ready to the moment when Jirau is transferred to us and we'll have a phase where rather we're going to have a large customer base.

If you can see here, distribution is quite well distributed in the whole market thus mitigating the risk of consumption variations from the industrial side and also mitigating the risk of default. So in our credit analysis we have managed to have no defaults (inaudible).

Slide number 12, energy market outlook. If you look at the right-hand side chart, the ratio between supply and demand for this year and for the next year has gone down due to the delay in the transmission lines and even generation, the calling off of some projects and the delay in Jirau and some other assets. So we have undergone some problems here.

On the right hand side, you see the price hikes this year due to the -- here you have only until the December. But as you know, the First Quarter has also seen very high spot prices due to the rainfall levels and low hydrology aspects. So we see here a conversation with the thermal generation.

As of May, we already have in the model Super K [ph] represented here in this model and also contributes to the increase. So in the long term, this is good news for the trancos [ph], but it's not pleasant to have a change in regulations after the game has started.

Slide number 14, our strategy to always sell regardless of price, the stock prices. Of course, we try to get our best possible conditions. But we try to be always present in the market, always selling. We are practically 100% contracted until 2015. We only have 10% less at 2015. And on the right-hand side, we see that each year our long term contract increase. So the amount of non-contracted energy lowers in a sort of reverse ladder as if you were climbing down the stairs.

Slide number 15, here you see our energy balance in detail? We have our own resources showing a slight increase. So this is basically due to the last (inaudible). I'm sorry, I'm showing 2013 and '14. So we have average 2006 by 549. Usually it goes down and this is the way it should be. We're buying also. We also have regulated contracts as you already know with the prices updated until March 31st, on the right-hand side. This is a very relevant portfolio.

2015, these contracts of three times BRL115 will finish. We expect better prices here for future contracts bilateral sales, 2,458 average megawatts. Also the traders (inaudible) industry and something remaining for the RGE. We also have bilateral prior to this model. Total sales, 4,118 with the 670 megawatts in 2013. Average sales price 137, buying 124 relative to the 549 megawatts.

Let me now turn to Elio who is going to talk about Jirau project update. He's going to give you an update on the project.

Elio Wolff {BIO 17147591 <GO>}

Thank you very much. Good morning, to all. Once again we're going to talk about the Jirau project and I'm going to give you an update. On slide 17, we have some basic characteristics of the project. The capacity you all know, 6,750 megawatts. 2,185 average megawatt of assured energy of which 73% have been contracted for 30 years with the distributors.

Contracts are indexed by PPA by inflation. The first PPA starts in the Second Quarter and this will probably be linked with the start up of the plant, and the second PPA starts in March 2014 with an updated price of a 112 megawatt hour.

As you all know, the balance of energy available with the SCE [ph] has been contracted by the shareholders and 60% of the energy is going to GDF Suez. You can see that on the right lower graph this volume will be 323 megawatt hour for GDF Suez. As regards to CapEx, until March 2013, BRL16.3 billion, and if we look at December amongst with high inflation, change of scope and increase of prices, so CapEx will effectively be BRL16.3 billion to March 2013. That was a clean development mechanism.

We have won the second process and the analysis at the UNFCCC. We expect to complete that at the end of the Second Quarter and as of then we will be able to sell net carbon credit. We already have a revenue forecast for 2014, and when we achieve full capacity, it should give us 6 million tons.

We also have options to create additional value, additional assured energy. We are still discussing that. Now tax incentives in the region and also the Ministry of Mines and Energy recently approved Jirau as a priority project for the purpose of issuing infrastructure debentures. This is being assessed by the shareholders and by the SCE, and as we have an update, we are going to bring it to you.

On slide 18, we have some additional updates on the projects, some pictures. We started the filling of the reservoir on the left bank for starting the commercial operation. This is expected to begin at the second of the -- at the Second Quarter of 2013. We have begun commissioning. You see the electrical gallery. This is practically ready. We also have the control center and also the spillway. We see how the project is progressing when you look at the pictures.

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As regards to financing, BRL9.5 billion linked to the long-term interest rate plus spread and the amortization in 20 years. On slide 19, we see some pictures of the project; the collecting substation on generating unit 29, one of the first who will begin to operate. We also have the runner chamber closed, and on the lower part you see the power house on the right margin and also all the views upstream and downstream to start operations in the Second Quarter.

Also on the picture of the left bank powerhouse, you see that we have begun the filling already. It's almost done. We expect we can announce very soon the start up of the commercial operation. I'll turn the floor back to Zaroni.

Manoel Zaroni Torres {BIO 20231580 <GO>}

Thank you very much, Elio. We are going to see on slide 20 updates about the thriving wind complex. We have four wind farms with a total of 115.4 megawatts of installed capacity. It's renewable energy and we expect to start operating in the First Quarter of 2013. We're going to make comments about that. The commercial capacity is 62.4 average megawatts and the investment is BRL419 million.

The supplier of the turbines will be Siemens. There was a small -- a short delay on our part. Some of the towers have been assembled already and by yearend we are going to finish the wind farm. The problem is connecting to the basic grid as this is running late, but we expect that in the second semester we will have part of these projects operating. The CapEx is within budget. There were no surprises there.

Let's talk about the financial performance. On slide 22, we compare the net revenue, which I think growing year-on-year, a CAGR of 9.5% relative to the First Quarter of 2012, it went to BRL1.391 billion, a 20.6% CAGR for the quarter. As regards EBITDA it grew 22.2% in the quarter. EBITDA has been growing as well with a CAGR of 9% and it went from BRL712 million to BRL871 million in this quarter as a result of the differences.

I never advice you to compare quarter-on-quarter. You know that energy allocation is made on an annual base and you might have a quarter when you were short and others when you were long. So there might be a variation there. The net income was for BRL425 million in the quarter, 30% increase relative to the First Quarter of 2012 when we posted BRL327 net income. Don't multiply BRL425 million by 4 because this could be misleading.

In slide 23, we have the net revenue from sales. And on the top graph you have the revenue per quarter to show you that there are differences. And in the case of this year, if you compare with 2008, we had 28% in the First Quarter and then 23% in 2010, and in 2013, we will have an amount higher than 23%. So we cannot compare quarter-on-quarter.

As regards the net revenue from BRL1.153 billion to BRL1.391 billion, BRL105 million came from the CCEE, the average sales drive through by BRL66 million, the sales volume grew by BRL57 million and other amounts for BRL10 million and this gave us this 20.6% growth.

EBITDA is linked to the revenue and we segregated the growth in the CCEE, 82% impact and other operations which include higher volume, higher selling price that accounts for BRL77 million and we went from BRL720 million to BRL871 million. And as regards the net income, it went from BRL327 million. We had the positive impact of the CCEE of operations and also the financial result, which was a little bit lower than in the previous quarter. We had net income of BRL425 million in the First Quarter of 2013.

As regard the Company's debt, on slide 26 you can see the indebtedness of the Company is low. Relative to our EBITDA, it is at 1.5 times the EBITDA of the last 12 months. 6% is denominated in foreign currency, and our cash generation is 0.74 of our operation relative to our debt. If we exclude the cash position in March the 21st -- the 31st, our net debt is BRL2.815 billion.

Net debt EBITDA for 12 months is 1.1, which is a very low amount if you would consider that as a covenant. As regards the changes in net debt, we went from BRL2.355 billion. We paid dividends and interest on extra capital. We also paid income tax in the First Quarter. We paid in January BRL401 million.

Then working capital changes accounts for a positive impact of a BRL165 million, BRL145 million of investments in Estreito and in our wind farm, accrued interest BRL54 million and the rest are the minor amounts plus our operational activities, which account for a negative impact of BRL887 million, which took our debt to BRL2.815 billion.

As regards the composition of the debt, it's always the same. I think you all are familiar with that. It's basically denominated in reais at the cost of the TJLP plus spread, 72% plus the spread. The debt profile is very confirmed. In terms of payment, we have to pay BRL400 million and then another amount and then another amount in 2014, and we might have that if we make any acquisitions.

In the investment plan, on slide 29, we estimated for 2013, but we are going to continue to invest a BRL153 million in Trairi Complex and BRL543 million includes BRL237 of O&M, BRL66 to Estreito. And under those BRL218, we have our equity in Trairi and BRL20 million is for Campo Largo in Bahia. That's for 2013.

For 2014, we took BRL511 million for the Jirau transfer because this is going to happen only in 2014. So this is kind of a reserve so to speak and the rest excluding BRL70 million for Estreito; BRL238 million, which is our equity is for O&M operations.

Regards to dividend policy, we have showed this when we showed the results for 2012. We paid 2.37 per share, a 100% of payout and the dividend yield was 7.1%. And on May the 14th, we are going to begin the payment of interest on the equity capital relative to 2012 or BRL276 million, BRL0.423 per share.

So I'd like to wrap up here and I'm available for questions, any questions you may have.

Questions And Answers

Operator

Ladies and gentlemen, we will now start the Q&A session. (Operator Instructions). Felipe Leal, Merrill Lynch.

Q - Felipe Leal {BIO 2015017 <GO>}

I would like to know what the Company sees in terms of the ratio of ISS? Will you have to bear this cost or will you pass it on to the regulations or to the allocation market?

A - Unidentified Speaker

We are sure that this is not due. It's done in order to avoid price increases to the consumers and the generators are paying for it, putting the bill, but this is a regulation, regulatory decision, we are going to try and protect ourselves not to be exposed, especially in terms of the stock market and we are going to ask especially in the regulated contracts, we are going to ask for an update on the price of energy sold. Thank you.

Operator

Vanessa Knowles, Credit Suisse.

Q - Vanessa Knowles {BIO 18903103 <GO>}

In terms of what Felipe asked, you said that you intend to protect yourself especially in terms of delta spot price or PLD, how much could this lead to cost? How much could it represent, I mean, the ISS allocation and the delta spot price so that we have an idea of the potential impact if this is not passed on or if the resolutions remains as it is today?

A - Unidentified Speaker

It's a very tough situation and may, for example, they have introduced the Super K which in crisis is sales [ph] to the spot price. So you are buying thermals from all prices, you increase the spot price, you decrease the delta because the cutting point for those that are dispatching due to merit does not modify.

So last week the spot price was BRL128 or BRL148 and the delta was BRL150. This week it's BRL277 and the delta PLD [ph] is BRL100. So you are changing the cutting point and it depends on the exposure you have. It's hard to assess the exposure.

So we are quoting in weekly basis. So there is some exposures we had not projected, for example, at the end or out of the end and since we generate flat when the load is reduced. So it reduces the hydro generation. So your contract had a certain capacity, you are exposed, and you have no way to protect yourself against that.

So it's sort of an arbitrage that is really leading to a number of difficulties to us especially in terms of protecting ourselves. But I can assure you that we have taken all the measures and we are going to try and protect ourselves as much as we can. But due to the fact that those we sell receive PLD and those that pay, wholesale pay PLD plus delta. The market

adjusts itself very quickly and the tendencies for delta PLD to go to zero. I mean, it won't be zero because of the distributors, but it will be very low. And this goes to the general pro rata distribution, which is like 7% of the market, half of it is Degenco [ph] 3.5. In a total of BRL600 billion; BRL800 billion, this is what we have, this is our share of the bill, BRL20 billion or BRL30 billion.

Operator

(Operator Instructions). Vinicius Canheu, Credit Suisse.

Q - Vinicius Canheu {BIO 6300903 <GO>}

Let me take the chance to ask another question. In terms of the reservoir scenario, hydrology, I know it's not easy to project for the future to know what's going to happen, but what's the scenario that you think most likely to occur for the rest of the year? I mean, due to allocations, GSC was very low in January, but then February and March it was close to 1 again. So thinking about the exposure the Company will have in CTE along the year, could you tell us about the GSS along the year according to the allocations we've already seen?

A - Unidentified Speaker

Listen, Vinicius, it's very hard to really know what's going to happen because we don't know what the hydrology is going to be. So you can project, but you don't know. Last year at this point hydrology was fine. Up to August everything was excellent. PLD was low and then we had that huge hike that was unexpected, So we really don't know. We did see an improvement, a very remarkable improvement in April and now we've seen a worsening. But it's so hard to tell why because this month we had introduction of Super K, which also has led to an increase in prices. So as far as see, the trend finds to a drop in spot price, the PLD by the end of the year because we are going to have the plans for a data, which will start operating and contribute with more energy in the market, especially during the summer. This is what we project. But thermo generation GSC have lead to very bad symptoms. It's almost -- I'm sorry, if you have very high thermal firing, thermal generation and you have secondary energy, this is another very favorable situation because it's contributing on lowering the reservoir. So ideally we should be the threshold for the next month.

Operator

Carolina Carneiro, Santander.

Q - Carolina Carneiro

I would like you to comment about the auctions expected for this year and what your expectations are in terms of the competition amongst companies and if you have any particular interest in the auctions especially for thermal energy.

A - Unidentified Speaker

We are always interested in auctions and I think that we can go for better prices. This will make us more competitive. And for reserve energy, as I said, we acquired some projects for wind farms and we are certainly going to take part in the auctions with this project. Whether we are going to be successful or not, it will depend very much on the price.

As for thermal energy, we are a large producer of energy based on coal in the south and we believe we will be able to participate in the next auction. I don't know if in this year, but we have experience, we have the knowledge, our Group has the knowledge, to participate in this auction and we are interested in participating. We have significant cash generation and the guidance of the Group is towards growing in the country.

Operator

Felipe Leal, Merrill Lynch.

Q - Felipe Leal {BIO 2015017 <GO>}

Just one more question. It seems Elio is here today with us. Speaking of auctions for contracting the 27% of Jirau, are you interested in participating in the A minus O auction?

A - Elio Wolff {BIO 17147591 <GO>}

At this point, what we think is essential and this is what we have been pursuing is to start up the commercial operation of the plant. I think it would be premature to think about selling this energy given that we might have to make some adjustments in the schedule. So today what we are focusing on is to achieve commercial operation. This should take place in the Second Quarter. This is where we are giving our efforts to. Of course, the market conditions now are favorable in a sense, but we prefer to focus on meeting the schedules. And as regards the auction, everything depends on the price on the conditions, on the timing and on the prices for purchasing energy in the auction.

Operator

Sandra Boente, HSBC.

Q - Sandra Boente {BIO 1511861 <GO>}

I have two questions; one has to do with the auction, if you are interested in purchasing any of the plants that will go out of (inaudible) or any one which will be spin off from (inaudible). Then what is your due relative to long-term prices 2015 specifically? What is your take on the contracts market? What is the demand for the contract market with free customers? Is there any interesting terms in -- longer than one year? How do you see the situation for the longer term?

A - Unidentified Speaker

Auctions for the plants, which are going to sell close, we know something about it, but I would say that our operation is very efficient, our maintenance is very efficient but you no longer produce the commodity megawatt hour something that is regulated and you

become a service provider and the regulation for that is more restricted than for transmission companies and distributors. So I think it is early for us we will have to assess further whether we want to participate or not. As regards the prices for longer term contracts it is difficult because they are psychologically affected by the short price at the time but we have to look at the technologies and at the sites which are going to be auctioned we are working on BRL115 and BRL130 for 2015.

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Q - Sandra Boente {BIO 1511861 <GO>}

BRL115 and BRL120, one of the issues on the table where you saw the contract and the average price of sale, the average price of purchase, your purchase average sale for 2015 is at BRL137 per megawatt hour which is more or less in line with your selling price. Do you think you will be able to change that situation with a positive trend or do you think that in truth prices will remain at that level, a BRL115 and BRL120, with a negative spread as you see today, or even at bigger negative spread?

A - Unidentified Speaker

Sometimes we have to do this to compose the product for the longer terms but this BRL136 is our purchasing price is for a smaller number of megawatts. So in terms of volume, in terms of amount it is not significant.

Operator

Gabriel Lyra, Itau BBA.

Q - Gabriel Lyra

I just want to clarify something. I was looking at the share balance sheet which will have the figures for the consortium and we have BRL13.7 billion in fixed assets under formation or already formed with the debt of 9.7%, 9.1% and equity of BRL4.7 billion. We multiply that by 60% in terms of the equity, it is BRL2.8 billion. What are the alternatives for incorporating these assets?

A - Unidentified Speaker

BRL2.8 billion is a bit expensive in terms of what you see in the reserves of Tractebel to pay for that. I can't understand the math underlying your question but the cost of the project today is BRL16.3 billion. So that is the cost at the end of the work. And most of these investments has been made already.

We are now in the final stages of commissioning, assembling. So if we start with this BRL16 billion and we work on 60%, this is the stake that will be transferred to Tractebel probably in 2014, and we might have to get more information from Saloni [ph] but Tractebel has a low level of leverage.

So there are some ways that we can do this transaction. We are considering how we are going to do it. We could do it via debt. There are many alternatives. But Tractebel today has the flexibility to make the right decision on how to make this acquisition.

Gabriel, let's suppose that this is going to be an acquisition, a real acquisition. If I'm to be a odd book [ph] this would be BRL2.8 billion. As you have calculated, BRL2.8 billion, and if I do this with the debt, it will be twice as much. But even that my ratio total debt EBITDA will reach two-something. I mean it won't impact my covenant?

Q - Gabriel Lyra

No, no this is not my question, not to have an impact on covenant. I would like to know how this fits with your plans to participate in further auction or even thinking in terms of your (inaudible) an cooperation with a third party if it could make it more digestible from the perspective of the balance sheet and also new projects.

A - Unidentified Speaker

You're right. I mean, everything as it's done. We are going suddenly to find the best possible solution to create value to Tractebel. I mean, if it is going to be what equity was set or if we are going to look for partner, I don't know. We will find something.

Q - Gabriel Lyra

One last question. From the BRL4.7 billion of invested equity, you won't have any more investment. The rest will be the NTF [ph] and --

A - Unidentified Speaker

No, no, no. I think it is going to be a mix of debts and own equities.

A - Antonio Previtali

I'll bring to an end our Q&A session. I will now give the floor to Manoel Zaroni Torres for his final consideration. You may gone on, Mr. Zaroni.

A - Manoel Zaroni Torres {BIO 20231580 <GO>}

Thank you very much. I would like to thank everybody who asked questions because this gives us the opportunity to clarify some questions, some points. I myself, the IR people, Sattamini, Gabriel, we are all available for any other questions you may have in the future. And let me once more state my concern with the regulations that are being enacted in the regulatory systems in terms of interference and changing the rules in the middle of the game. So this is what I wanted to tell you. Thank you very much.

Operator

Tractebel's audio conference now comes to an end. We thank you all for your participation. Have a nice afternoon and thank you for using Chorus Call.

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