Conference Call Transcription
Results of 2T21
Aeris Energy (AERI3 BZ)
August 12, 2021

Operator

Good afternoon everyone and thank you for waiting. Welcome to Aeris Energy's 2T21 results conference call. Today with us we have Mr. Bruno Vilela, CEO of Aeris Energy and Mr. Bruno Lolli, Director of Investor Relations Planning.

Please be advised that this event is being recorded and that all attendees will only be listening to the conference call during the presentation, and when further instructions are provided we will start the Q&A session. If any of you need any assistance during the conference call, please request the assistance of an operator by typing asterisk zero.

This event is also being broadcast simultaneously over the Internet via webcast and can be accessed at the address https://www.ri.aerisenergy.com.br/en/ where the respective presentation is available.

The slides selection will be controlled by you. The replay of this event will be available soon after its closing. We remind you that webcast participants will be able to register questions for Aeris Energy via website, and those will be answered by the IR team after the conference ends.

Before proceeding, we would like to clarify that any statements that may be made during this conference call regarding Aeris Energy's business prospects, projections, operating and financial goals constitute the beliefs and assumptions of the company's management, as well as information currently available to Aeris Energy.

Future considerations are not performance guarantees and involve risks and uncertainties, and assumptions as they refer to future events, and therefore depend on circumstances that may or may not occur. Investors and analysts should understand that general conditions, industry conditions and other operating factors could affect Aeris Energy's future results and lead to results that differ materially from those expressed in such forward-looking statements.

I would now like to hand the floor over to Mr. Bruno Vilela, who will start the presentation, please Mr. Vilela, you might proceed.

Bruno Vilela

Good afternoon everyone, before we talk about our market results and also a little about the company perspective, you must have followed in the media that recently the UN report came out talking about the global warming program, and that the planet has already warmed a degree and that this is almost irreversible.

So, even with all governments having aggressive plans to reduce carbon dioxide emissions, this impact is still worrying. What are we going to see? We will see governments even more aggressive with emission reductions. What we can say is that we are already seeing in practice in the market.

We always talk about what matters most to us. A few billion dollars went to the ports to adapt to the American offshore market. So, the United States is getting ready to receive the offshore market, in terms of regulation we have already commented that it is now resolved, and that there is investment in infrastructure, another billions of dollars for the transmission line, which will greatly help the onshore market .

In the United States, unlike Brazil, the system is not interconnected, so there are several sites that have wind potential that do not have power generation because they do not have transmission lines. And finally, it is very relevant to us that a few billion dollars will be invested in gas stations for electric cars. This will accelerate the energy transition that we have been talking about and this is already a reality.

In Europe, there is an innovation law for this program, which speaks of reducing carbon gas emissions by up to fifty-five percent by 2030, that is, Europe also has very aggressive plans to reduce carbon gas emissions. Wind energy will stand out in Brazil, in the short and medium term, due to the crisis we are experiencing, a water crisis that generated a significant increase in the cost of energy, and we are already feeling the impact on our inflation.

Today, the biggest reason for the inflation increase that has impacted us the most, is the increase in the energy cost. And when we talk about a short-term perspective, you can ask that we are talking about medium and long term, but what if in relation to the short term, what is happening?

What is happening, it can be said that it is a little of the pandemic unfolding and it generates a certain uncertainty in the investors who build the wind farms. What are these uncertainties? What will be the world growth and what will be the inflation level, and why? Because current inflation has caused wind components to increase their price a lot. So, these investors are waiting to understand what the economy will be like in the future to actually make these investments.

We know that it is a repressed demand, and it is increasingly aggressive. Also, it is not happening in short term due to the problem of the price increase in both raw material and component.

This is the pandemic unfolding, we see and feel this in practice, most of us are able to pass it on to customers. Another part of us has to work to mitigate the risk of raw material price increases, but there is also a logistical risk.

We just got the news that the port in China has been closed due to covid cases. The pandemic diminished, but even so, it continues to have an impact on the production chain, not just wind power, but any type of industry that has exports and imports.

And to finish with Aeris' perspective, we are already producing the three molds of Siemens Gamesa, our new customer, for which only Aeris manufactures in the West, besides themselves. It is a client that we started a relationship with, now there are three models. This model will be very important for us, the ramp up that is this learning curve will be very important in relation to the prospects for the following year's results.

Moving on to slide number three, talking a little about the results, we see that our net income in this quarter was R$18.7 million, reaching R$113.8 million in the last twelve months.

The medium ROIC in the last twelve months was 13.9%, still negatively impacted by the high share of capital allocated to operational and non-mature lines. Investment of R$68.8 million this quarter and we are coming very close to ending the investment cycle this year.

So, every investment we had planned is being executed. Net revenue was R$590.9 million this quarter, reaching more than R$2.7 billion. EBITA reach R$55 million in this quarter accumulating R$255 million in the last twelve months. This is just a highlight of our numbers. I will now pass the word to Lolli who will continue the presentation.

Bruno Lolli

Thank you Vilela, I will start with slide four. Good afternoon everyone. I am demonstrating here the company absenteeism, in the evolution of the last two and a half years. We know that blade manufacturing is very labor dependent, very labor intensive. Consequently, our results depend on the engagement level, the specialization degree of the workforce and the higher the absenteeism, the more entropy we have in our operations.

If compared to 2019, which is this gray line, we have absenteeism ranging between 1.2% and 1.6%. When we analyze 2020, in the red line, we can see that in the first pandemic wave we had a peak in May of almost 10% and in the second wave, which started closer to the end of last year, especially here in Ceará, we climbed again in this second quarter, and we had an average of almost 7% in absenteeism.

This contributes to having costs above the those naturally planned. One of the strategies we adopted for not getting the production plan right was to hire in advance part of the staff that will be allocated to the Siemens Gamesa project, and now we are running with the decision to have a cost above normalized, so that the other above normal levels do not affect the production plan.

I think it is important to highlight that we maintain all actions to take care of the physical and mental health of the people who are here with us, this is a priority, it will always be a priority. Last July, we saw a reduction in these absenteeism levels and the expectation for this third quarter, we already have a much-improved situation, with the way we are progressing satisfactorily in vaccination here in the state of Ceará.

Moving on to slide five. This is another topic that I would like to highlight about the pandemic impacts, and also with something that is natural to happen in the beginning of operations, that is having working capital requirement levels slightly above normalized levels. Here I'm splitting the company's inventory position into revenue days since the end of 2019.

The main changes that we see in relation to the previous quarter is an increase in the average production period of the products, which is quite common, a product that is at the beginning of the manufacturing cycle is produced in thirty days. We are going to reduce this manufacturing cycle, until we have something around ten to twelve days of average manufacturing term.

Another account that we see increasing in the scenario is the advance of raw material suppliers, since we have a new customer, it is natural that, in the beginning of our relationship, we have suppliers that we had no relationship with until then.

The first purchases are usually paid in advance and as the relationship develops, we start to have credit limits and have longer deadlines. The current inventory position is around R$200 million above the levels we ended the first quarter, which are already above normal levels as a pandemic result.

At the end of last year we made the decision to increase safety stocks, which will only be felt towards the end of the third quarter, beginning of the fourth, considering that our material transit cycle is reasonably long. Going to number six, this is a slide that we are already used to see in our results. On the left scale, on the bars, we have the average invested capital for each period and on the right the line that shows the accumulated of the last twelve months.

We reached R$211.5 million in the last twelve months of NOPAT, it's a growth of more than 9% compared to the end of 2020, but the growth of NOPAT does not keep up with the investment growth. First we invested and then we went through the ramp-up period, so that from there we could take full advantage of the investment that was made.

Then, the Average Investing Capital grew more than 60% compared to the end of last year and we will only take advantage of the results arising from this investment more intensely in 2022. Moving on to slide seven, we can better understand this dynamic evolution of investments and returns. Separately, we can see that around 45% of the company's invested capital is still allocated to pre-operational and non-mature lines.

Combining lines of no negative return and these lines as they mature, and are installed in the case of pre-operational lines and mature in the case of non-mature lines, they naturally evolve towards the mature lines results.

We can actually expect a very representative growth in returns from mid-2022. In this period, mature lines are reaching 22.4% ROIC.

I commented on the pandemic and that comes in general. I will comment further on the net slide, that it has been consuming around two hundred bases of EBITDA margin in the company, mainly to the mature lines. A lot of emphasis on slide seven was about our return in the services division.

As the pandemic in the United States is now more under control, we had a damming of services in wind farms that was somehow released in this second quarter. The revenue grew significantly, especially in the United States and it is a division that has been delivering results and returns at around 50% per year, remembering that a good part of this contract is much longer than in the blades manufacturing.

On the net revenue we noticed a note of expressive growth in the first half of 2021 compared to the first half of 2020, but a drop in the last quarter, and this drop, as we can see here, is more intense in manufacturing for the domestic market , but it was around three hundred and fifty megawatts compared to what we had originally designed. We are passing this volume on to next year.

One of our clients asked for a postponement of volumes due to a restriction in the supply of one of the inputs. I must remember that the negotiation between our customers and our suppliers is made between them.

Aeris participates by executing these commercial agreements that our customers sign with our suppliers, and they decided to communicate Aeris later that the volumes we would receive of these inputs would be reduced this year and that next year we will return to volumes very close to 100% of the capacity occupation for this customer.

This lost volume in 2021 is fully transferred to 2022, and this does not affect the project's return in any way, but separately for this quarter we have a lower fixed cost dilution capacity, since this postponement was made with a notice much shorter than usual.

Moving on to slide nine, we have the results evolution. Even with this lower ability to reduce fixed costs, we managed to improve the margin in this period, from 9.2% to 9.3%. I think it's important to highlight that the margin that brings non-mature lines was around 7.5% this quarter, while for the mature lines, the margin reached 11% this quarter.

So, that comment I made in the 200 bases previous slide, the expectation for these mature lines this quarter would be 13% margin if we had not suffered all these effects related to the pandemic, mainly and also the non-full dilution of fixed costs, as we had projected.

As mentioned earlier, on slide ten we can see that the investment cycle is coming much closer to the end, it is not an expense at all. With the lack of R$300 million, there is still some uncertainty about this number, as a result of some contractual negotiations that we have been carrying out with some clients, that could lead to the lines transition within this year of 2021.

For 2022, we already expect investment levels much closer to what we call maintenance. The expectation for 2022 is that the investment will be between R$50 and R$70 million reais. We can see on slide eleven that the distribution center that is part of the large assets built with the resources, is already in preliminary operation, and we will reach full DC occupation at the end of September this year. It has more than thirty-five thousand square meters of built area.

Moving on to slide twelve, we can see the industrial expansion, it's basically a new site. Internally, we call it Pecém III, it is a continuation of the company's headquarters and the definition of a master plan to build another 50,000 square meters on this land, if we have enough demand in the future to make this expansion and this contract. According to what we are seeing here, it already allows us to fully comply with the current contract with Siemens Gamesa.

Going to slide thirteen, we show the amortization flow for the company's debt, the cash position at the end of the second quarter was R$478 million and what we see in the bars in red are the operations that were carried out in the 1T and in 2021 . These operations have an average cost much lower than the company's historical average cost, and the orange bars show the debts raised until the end of 2020.

This August we are doing this second debentures emission, which will be the company's events, with this second issue that will be in the amount of R$700 million. We have paid in advance all these debts that we see here in the orange chart, they add up to R$380 million and the cost difference from the second debenture mission to the average of these debts of R$380 million exceeds 370 bases.

We are talking about something around R$15 million of financial expenses reduction per year as a result of this new operation. And the volume of this operation also allows us to have a much more comfortable cash position through the year of 2022. We naturally know that it is an election year, and it won't be as quiet an election as in history.

Not that the record has been smooth. It is an election that generates a lot of uncertainty, so we prefer to have a more comfortable cash position for 2022.

On slide fourteen, we show the orders evolution covered by long-term contracts, we went from 11.7 gigawatts in the first quarter to 11.5 gigawatts in the second quarter. This is the combination of the 700 megawatts produced volume and the contractual obligations addition on the part of one of the customers and the order of 500 megawatts with the confirmation of an additional production line.

These contracts potential revenue, considering the exchange rate at the end of the second quarter is R$8.1 billion and the average power of the zero generators already reaches 4.7 average megawatts. Slide 15 shows each of the lines contractual evolution, considering their maturity stage, what we have in relation to the previous quarter here is the closure postponement of one of the lines, so we were planning to decommission three lines in this current quarter.

In the third quarter of 2021, one of these three lines will be decommissioned, but only at the end of the year. We also had an extension, by one of the customers, of a line installation, this last bar that we see here in the graph. It was originally planned to happen at the end of this year, it will pass the second quarter of next year and the changes for this quarter is one of the lines that were in immature stage and that has been moved to the mature stage.

And as Vilela commented, we started to execute the contract with Siemens Gamesa, so one of the lines was already operational at the end of the quarter, and we converted it from this pre-operational phase to a non-mature phase. I pass the floor back to the operator.

Operator

Thank you. Ladies and gentlemen, we will now start the Q&A session, if you have any questions press asterisk one on your phone. If at any time your question is answered, press asterisk two to remove yourself from the line. Questions will be answered as they are received.

Please take the phone off the hook when asking the question, so that you will be able to enjoy optimal sound quality. Our first question comes from Lucas of XP Investimentos, please Lucas, you can proceed.

Lucas of XP

Good afternoon Vilela, good afternoon Lolli, thanks for the space. A question here is in relation to this globally generalized pressure that we have been saying in relation to raw material funds. We have seen it also Siemens Gamesa, Vestas and TPI on the competitive side. I would like to hear from you how are these conversations with manufacturers, and also in relation to this issue that they are managing to pass on 100%. Leave an existing contact person or if there is any room for renegotiation with customers given this atypical scenario.

And also, thinking about new additions of lines, given the departure of these three lines planned for this year. How is the conversation going in the negotiations of many customers to add these new production lines in this space that will end? If you are eventually seeing any pressure on pricing given this scenario of increased cost.
Increase that may impact the company's ROIC level in the medium term, possibly below historical levels.

I think it's more about this issue, you gave a good idea, but think a little more in detail here, in relation to this rectification trend with new contracts, less existing contracts. Thank you.

Good afternoon Lucas, it's Vilela talking. First, we would like to apologize because we saw here that the transmission is failing a bit. Even Lucas' question failed to us a little too, but I think I understand your question, Lucas, we are not only executives, we are partners in the company, so we always try to mitigate the issue of risk in our contracts and look its own ROIC with the design vision.
Our contracts differ from TPI's contracts that the first time disclosed the contact structure a little. It was in the results disclosure that in our contracts the price increase of raw material is past through. There are contracts that are daily, others that are weekly, and others that are no daily contracts because it is very difficult to be in the matter of exchange rate variation, which is really daily.

Regarding the fear of raw material prices, it will be charged monthly or in the next quarter. So we didn't suffer any financial loss due to this raw material price increase.

What we are seeing, talking to suppliers, is that this situation is actually generating the increase, generated by the economy uncertainties and also the increase in logistical costs, but it is a one-off thing that tends to return to normal levels as soon as things calm down in relation to the pandemic. We say that the pandemic is over, but that ends up being a pandemic result for all the reasons we have already mentioned.

Very high liquidity in the world generated inflation, logistical complications, but we do not believe that these prices will be maintained. So, in short, prices will return, we are convinced of it, and Lolli will give more details about it.

Bruno Lolli

Good afternoon Lucas, about ROIC, which Vilela has already commented well, the increase in input costs is passed on to customers, so the biggest effect we have here is not on the ability to have results, but on the need of working capital. In this period, and not only because of the costs increase, but also because of the logistical cycle increase.

When we price contracts, we obviously assume a degree of conservatism in the average materials transit time, but current times are above what we assumed.

So, it's natural that until we have a normalized performance in the global logistics cycle,
we have a need for working capital a little above normalized levels and, consequently, more invested capital and less ROIC than we priced. We are very confident that the situation towards the end of this year to the beginning of next year will already be much closer to the indicators that we have priced.

Lucas of XP

Perfect, thanks and good afternoon to you.

Operator

Our next question comes from Rodrigo's webcast from BRL Capital The question is, analyzing the Aeris sustainability report I noticed that the energy consumption per produced blade is much lower than that of TPI, to what do you attribute this? Thank you.

Bruno Lolli

Good afternoon Rodrigo, this is Lolli speaking, thank you for the question, I think you read the sustainability report very carefully, TPI also recently released its report, and when we compare energy consumption that we actually have, I think it's around 40% less energy consumption per produced blade when compared to TPI. I think a good part of this, in addition to the efficiency of resource management in general, is something that is part of Aeris' DNA.

I think the fact that we have a large factory, mainly because it is located in Ceará, contributes a lot to that. We have a very low thermal amplitude in Ceará and a good part of what we have in terms of energy consumption is associated with air conditioning. The production process, so that it has a level of control required by both us and our customers, needs to be acclimatized.

Then, in our ability to consume less energy to keep the buildings within the parameters of the quality requirements, we consume less energy to do that, and naturally it's more efficient for air production in relation to the use of that resource. I think even more important than this is when we look at energy consumption as a whole percent of energy from renewable sources.

And when we look at our competitors, if I'm not mistaken, the TPI, for example, it doesn't even reach 20% in this indicator, so it's one more commitment of Aeris to maintain and improve our ability to contribute. By being productive and ensuring that this production is of low impact It also contributes to this process that Vilela commented very well at the presentation beginning and is becoming more and more fundamental.

Climate change is something that our generation is already paying the price for and if we don't do something faster, the next generations will be even more affected.

Operator

Thank you. Remembering that to ask a question just press asterisk one. Please wait while we collect questions.

Our next question is also from the *webcast*, it comes from Anderson, who asks: I noticed that the volume of services has been growing, what is the perspective for this department? Thank you.

Bruno Vilela

Good afternoon Anderson, the service sector has really been growing and the reason it has been growing is little, it wasn't there in the annuals, the fleet that needs to receive service provision increases annually. There are few companies in the world that have the capacity to repair wind turbines and other few companies have an engineering body like Aeris to repair wind blades.

We've stopped fighting for price in relation to service a while ago, we don't find this competition interesting, so some clients we already rejected, but other clients have already seen that cheap is expensive, so they are coming back to us.

We have an organic growth, both in Brazil and in the United States, in Brazil we are already consolidated, and in the United States the operation started in 2019, so it is in its second year. We can say it is stabilized and we are experiencing very strong growth there and, and it is clear that Aeris company behind it helps a lot, in financial and mainly in engineering capacity.

This is an industry where knowledge is very relevant.

Operator

Thank you. Our next question is also from *webcast,* it comes from Vitor Rampazo with [32:20]. Good morning, I would like to know what happens when an Aeris customer reduces the contracted capacity; the production is delayed or not even carried out? In addition, I would like to better understand what was the input that generated this impact in the production. Thank you.

Bruno Lolli

Good afternoon Vitor, the client has this contractual flexibility. All of our contracts provide that the customer can order less than 100% of the capacity we dedicate to it. In these cases, the natural thing is that the price increases, this is already foreseen in the contract. In this specific case, we do not practice the price increase now because this reduction was not a full reduction, it was in fact a postponement, and it guarantees us an additional volume next year, so we also do not give the discount associated with that.

In 2022 we will recover what we stopped producing in that period with a slightly better average price. About the input that affected this period, being quite transparent, it was another fact that pultruded carbon fiber is one of the main structural components of the blade and one of our client's suppliers had a supply restriction.So, reduce the volume in this period does not affect us in the medium term, so we agreed with this postponement now, to ensure more results for the following year.

Operator

Thank you, our next question is also from *webcast,* it comes from Lucas Vandercem of Gerval company; Could you comment on today's value-linked report on Aeris' product diversification possibilities? Thank you.

Bruno Lolli

Good afternoon Lucas, we obviously cannot give much more details about this without being relevant when in fact we understand that the subject deserves this emphasis. So, being less specific but still answering your question, we have been continuously discussing with some players, not necessarily in the energy sector, manufacturing some components in composite material.

These businesses cases are being prepared by the board and will be submitted for evaluation when we concluded. They are businesses always associated with the energy transition process, we understand that there is a lot of opportunity both in civil construction and in the transport sector to manufacture components that have resistance and are lighter than other materials.

The great advantage of composite material is that it achieves mechanical properties with less weight. For example, when we talk about vehicles, for example, we either increase the pay load that this vehicle carries or increase the range it can do before refueling.

It is very advantageous for the transport sector to migrate to the use of composite material, especially when we are talking about a more electric vehicle fleet. So, we continue to evaluate these business cases, it is nothing that is so relevant at the moment, but we understand that gaining maturity could be a good opportunity for the company diversification.

Operator

Thank you, and since there are no other questions, we are now closing the Q&A session. I would like to hand the word over to Mr. Vilela, for his final remarks. Please, go ahead.

Bruno Vilela

Good afternoon. And again, I am sorry for the communication failure, we are at the factory today, so there may have been some quality drop in the Internet, but next time it will be resolved. Thank you for your patience and for your availability. We know that everyone has little time and it's important for us to pass on our vision.

It remains very optimistic, in fact, increasingly optimistic, not only for market perspectives, but because of our relationship with our customers and the improvements we are seeing here in our daily operations.

We continue to work hard to improve short, medium and long term results and there is nothing better than this projects and legislation good news to regulate the wind energy market, whether offshore or in the energy transition, and we are very well positioned to capture this pent-up demand. Why are so well positioned?

Because this year we finish all the planned ramp-ups and next year will be a year of stabilized production, in which the margins are much better. But I'm not talking about the margin now, I'm talking more about the team's dedication .

When we have a new product launch, we demand a great dedication from the NPI team and the engineering team. As we know, this demand is repressed, there will be a demand boom next year and that is why we are very well positioned to capture this it, whether in financial liquidity to make investments (if necessary) or in relation to the engineering team.

So that's it, thanks again for everyone's availability and patience and we are at your disposal for any questions. Have a good day and good Thursday.

Operator

Aeris Energy's conference call is closed. We appreciate your participation, have a good day and you can disconnect now.