

WEG S.A.

Conference Call - Earnings Results 2nd Quarter 2022

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Transcript of the simultaneous translation from Portuguese into English



CORPORATE PARTICIPANTS

Mr. André Luís Rodrigues – Chief Financial Officer

Mr. André Salgueiro – Finance Director and Investor Relations Officer

Mr. Wilson Watzko – Controller Officer

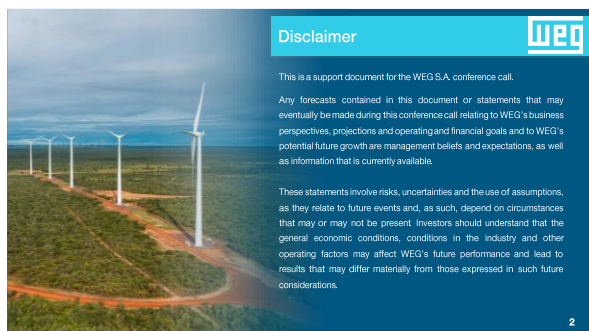
Mr. Felipe Scopel Hoffman – IR Manager

PRESENTATION

Operator: Good morning and welcome to WEG's conference call on the results of 2Q22.



We inform you that we are transmitting this conference call accompanied by the slides in our investor relations website at the web address ri.weg.net and after it finishes the audio will be available in our investor relations website. Should you need any assistance during this call please request the help of the operator by typing star zero (*0).



Any forward-looking statements contained in this document or statements that might be made during this conference call about future events, business prospects, operational and financial projections and goals and to the potential of future growth of WEG, are mere beliefs and assumptions of the Company's Management because they are based on information currently available. Forward-looking statements involve

risks and uncertainties and therefore dependent circumstances that may or may not occur.

Investors should understand that overall economic conditions, industry economic conditions and other operational factors may affect the future performance of WEG and may lead to results that will be materially different from those expressed in such forward-looking statements. Now we would like to remind you that this conference call is being conducted in Portuguese and you are listening to the simultaneous interpretation into English.

Today with us in Jaraguá do Sul we have Mr. André Luis Rodrigues, CEO and CFO; André Meneguetti Salgueiro, CFO and IRO; Wilson Watzko, Controller and Felipe Scopel Hoffman, Investor Relations Manager.

Please Mr. Rodrigues, you may start.

Mr. André Luís Rodrigues – Chief Financial Officer

Good morning everyone. It is a pleasure to be with you once again to announce the results of WEG on this conference call.

2Q22 Highlights



* Adjusted for the exclusion of ICMS from the PS and CPVMS calculation basis

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We start with the highlights of the quarter, where the operating revenue grew 25% compared to 2Q 21. We have maintained a good performance in the main markets where we operate, reinforcing our strategic direction of developing products and solutions of greater added value to our customers. We had a strong performance in the domestic market with good demand for our business of low-voltage electric motors, reducers, automation and especially businesses related to the generation of renewable energy and energy transmission and distribution.

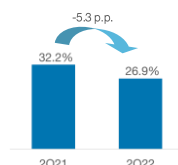
In the foreign market demand for industrial businesses is still very busy, with a growth of 23.7% in local currencies as compared to the same period a year earlier.

The adjusted EBITDA was 1.3 billion BRL, up 14.5% compared to the adjusted EBITDA in 2Q 21. The adjusted EBITDA margin ended the quarter at 17.4,



down 1.6 p.p. from last year's adjusted margin. Throughout the presentation André Salgueiro will provide more details about this performance.

Return on Invested Capital



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Lastly, ROIC fell as expected in this quarter, as we are going to see on the next slide. It dropped 5.3 p.p. as compared to 2Q 21 reaching 26.9%.

An important point that we should highlight is the that from this quarter on ROIC will suffer a greater effect of the impact of the booking of nonrecurring ICMS credit on the PIS and COFINS calculation basis since 2Q 21. The operating income after taxes of the last 12 months no longer has the great benefit of these credits, which were booked in 2Q 21; but on the other hand our invested capital still considers most of the adjustment, since the amounts of taxes to be recovered are still booked in our balance sheet.

In addition to this effect, the growth of invested capital is explained especially by the greater need of working capital and higher CapEx, which also contributed to reduction of the ROIC, despite the growth of the operating profit after taxes over the last 12 months.

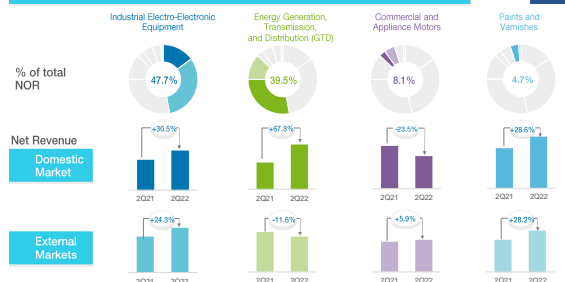
Now I would like to turn it over to André Salgueiro to continue.

Mr. André Salgueiro – Finance Director and Investor Relations Officer

Thank you André, good morning everyone. On slide 5 you can see the evolution of our business areas in the markets where we are operating, starting with Brazil where the performance of industrial electronic equipment continued positive this quarter.

The good demand was heavily pulverized in short-life equipment. This is equipment such as electric engines, reducers and serial automation products with the highlight on agribusiness, pulp and paper and mining segments.

2Q22 Business Area Performance



In the GTD area we had a relevant delivery volume of wind turbines, as well as an increase in demand for distributed solar generation.

T&D business was another highlight, with good volume of revenues driven by large transformers and substations for projects related to transmission auctions, along with transformer sales for distribution networks and industries.

In commercial engines and appliances there was a reduction which we already expected in the domestic market, after strong sales volume in the same period of last year. It is worth mentioning that we noted a gradual reduction in sales volumes at the end of the quarter, especially in engines for home appliances.

Lastly, the demand for paint and varnish products maintained the high-level of sales with emphasis on sanitation, mining and metals structures.

In the foreign market, the continuity of the industrial investment observed in recent quarters was an important factor for the performance of the industrial equipment area, despite the uncertainties of the macroeconomic scenario. Sales of short-life equipment showed significant increases in revenue, especially low-voltage electric engines, whose demand is very pulverized among different industrial segments.

In GTD revenues showed typical fluctuations of long-life businesses, mainly after deliveries of significant T&D projects in Colombia and South Africa and steam turbines in Europe throughout 2021.

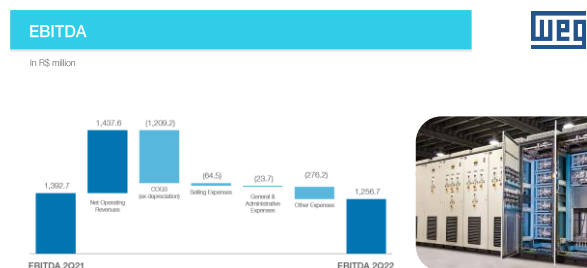
In North America, our main region of operation in this business area, we continue the process of increasing the capacity utilization of the new transformer plant in the US, taking advantage of the opportunities present in this market to build a robust portfolio for coming quarters.

In commercial engines and appliances, the positive sales volume is explained mainly by the good economic activity and market share gains in countries such as Mexico and China.

And in paint and varnishes Brazil's exports to Latin American countries and sales of other operations



abroad, both in Mexico and in Argentina, have contributed to the growth in this quarter.

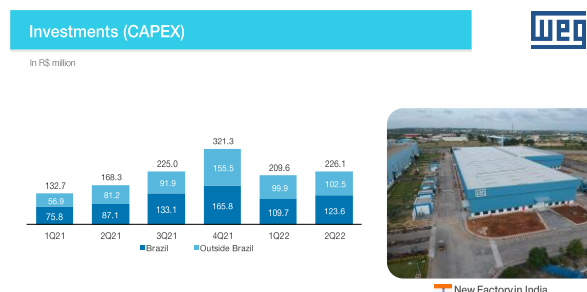


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On slide 6 shows the EBITDA performance in 2022, with a reported EBITDA showing a 9.8 reduction over the same period in the year before. The EBITDA margin ended the quarter at 17.5%.

It is important to highlight that in 2Q 21 we booked nonrecurring credits related to the exclusion of ICMS from the PIS and COFINS calculation basis. Adjusted for this effect the EBITDA grew 14.5% compared to the same period of last year, with EBITDA margin 1.6 p.p. lower.

The challenges in the global supply chain and the consequent increase in raw material costs, together with a change in the product mix and the increase in energy and freight costs, still bring pressure to the company's operating margins.



New Factory in India

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Finally, on slide number 7 we show the evolution of our investments. In 2Q 22 we invested 226.1 million BRL in modernization and expansion of manufacturing capacity, in machinery and equipment and software-use licenses, 55% of which were meant for production units in Brazil and 45% meant for industrial complexes abroad. Now I end my part and turn it back over to André.

Mr. André Luís Rodrigues – Chief Financial Officer

Before moving to Q&A, I would like to talk about some of our latest accomplishments and comment on our

prospects for the remainder of the year.



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With regards to achievements I would like to highlight the following events: in June our company was the highlight in the Broadcast Empresas Award given by Agência Estado in partnership with Getúlio Vargas Foundation. We were the number one company out of 204 companies with shares traded in B3 that generated the most value to shareholders. We also received special awards in the categories of Sustainability and New Market.

Recently we announced the beginning of the development of the new wind turbine platform with the power of 7 MW and rotors that will be 172 m wide, which would be the largest machine under development in the Brazilian market.

And this week we formalized the creation of WEG Algeria, a joint venture focused on commercial engines and appliances to serve Algeria and North Africa.

Finally, the outlook for the remainder of the year. Number one, we must not forget the macroeconomic scenario is more challenging for the rest of the year. Global inflation at high levels and the consequent increase in interest rates in major markets can interfere with the level of growth of the global economy and consequently of our businesses, especially short-life ones.

On the other hand, we understand that our competitive advantages help us a lot with that regard. We believe our business model based on verticalization, long-term vision and especially diversification of products and solutions, with different exposures to economic cycles, helps us not only expand our range of opportunities; but also mitigate risks and uncertainties in times of turbulence, like these that we are experiencing.

Therefore, despite the challenges presented in the macroeconomic scenario we expect to deliver another year of revenue growth and profitability, within the company's expectations and historical track record.



Now I end my presentation and we may move to our Q&A session.

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For more information, visit our results center:
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Q&A SESSION

Operator

Ladies and gentlemen, we now may move to our Q&A session. If you want to ask a question please press *1. To take your question from the list please press *2.

Our first question comes from Lucas Lague from XP Investments.

Mr. Lucas Lague - XP Investimentos

Good morning André Rodrigues and Salgueiro, congratulations on your performance. I would like to discuss two things with you in terms of renewable. First I am going to talk about solar and then wind.

So starting in solar, could you give us an idea about the mix in this segment of distributed generation, especially thinking of larger projects, or smaller projects such as in homes, small and middle-sized businesses?

And how do you see the growth prospects for the different subsegments in 2023, which will be a year with higher inflation and interest rates as we saw before, and the new regulation in terms of distributed generation?

So I would like to understand the positioning of the company and the growth prospects for the different subsegments in distributed segments. And then I will ask about wind, thank you.

Mr. André Salgueiro – Finance Director and Investor Relations Officer

Hi Lucas, this is Mr. Salgueiro answering your question. And in solar first, we break down solar distributed generation and centralized generation. So WEG works

on both fronts offering products for the two types of segment.

So the segment of distributed generation; but centralized generation has been growing, especially because of more recent projects that we have announced, and the most important is the one at Vale, Sun of the Cerrado. We are providing transformers and substations. So the breakdown today is more or less 90% going to GD and a little bit less than 5% goes to centralized generation.

If I understand your question, it is more specific about the breakdown in GD. In GD WEG has a bigger share in three-phase projects, which are the projects where the customer perceives a value, so there is an engineering company with know-how and knowledge. Today most of our GD is sold via three-phase and then we have some exposure in mono-phase, which is at home - but it is kind of small as a share of the whole. I do not have the exact numbers to give you now; but the vast majority are related to three-phase projects.

We have mini power plants. It is slightly bigger in industry, large commercial projects. So the dynamics of growth looking into the future is overall, we believe, and we are confident that solar generation will continue to grow in Brazil. Of course macroeconomic conditions such as inflation, maybe the FX rate might have an impact in the cost of commodities and solar plates.

But here in Brazil, and we have a combination of good solar radiation and slightly higher energy costs. So solar power makes sense, regardless of what happens, and what might happen is that it might grow slightly slower, more slowly or faster.

So the mini power plants, which are the projects that are related to remote generation, they are likely to have a smaller growth and even accommodation of revenue after this year; but other segments in GD, high consumption and retail and even small customers should continue growing in the midterm.

Mr. Lucas Lague - XP Investimentos

Well great, well this is exactly what I wanted to know. I wanted to know the breakdown in GD.

Now as to wind power I would like to understand the timing when profitability will come back in WEG. So I can in some contracts that you closed in the past and with many players are having difficulties, and my question is when are we going to see the resumption of profitability of WEG's wind turbines, considering that the products are reflecting the lowest equation between higher costs in the chain. So are there products to be delivered this year in 2022 that already are related to



this equation or is this more into the future? Your contract with Eletrosul that should be delivered in 2023 would have this normal profitability?

And the last point how are you using capacity today in terms of wind in WEG? And can we think of improved margins at the consolidated level just because of the lower share of wind, because other segments will grow more along the year? So these are the points thinking about wind in the company.

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Well, thank you very much for your question. Wind in practice is the business with the longest cycle in the company. So we have a contract, which was the first that we announced with the new machine of 4.2 with Aliança. It has just been delivered and we announced it in early 2019. So the timing is kind of long and as time went by and new contracts were signed the cost structure changed, and then we adjusted prices.

So naturally as time goes by and we deliver our next project, what we see is that there is a catch up of profitability.

Now when we look at the informations that were announced related to Aliança contract and Eletrosul we can have this perception, and as months go by our expectation is that in our portfolio today it is starting 2023 for the whole year, and 2024 from today until the end of next year and the beginning of 2024, we should see this regularization - but it is not going to be anything abrupt; it is going to be gradual. So this is more or less the dynamic.

So overall speaking, considering everything that is going on, projects today have a margin that is lower than our track record because of the cost structure. Once we catch up it will take a while. Wind even when the scenario is normal is still a business with a lower margin than the average margin, and if other businesses grow or grow more than wind we are likely to improve the margin if we consider just that effect.

In terms of capacity, today we have a plant with capacity to produce 8 turbines per month more or less, and we have this capacity until the end of next year, 2024. We are not expecting to increase capacity. If we have conditions and if market demand grows a lot, we may reconsider this and increase our capacity over the next few years.

Mr. Luca Lague - XP Investimentos

Okay thank you very much for your answers.

Operator

Our next question comes from Lucas Marchiori from BTG.

Mr. Luca Marchiori - BTG Pactual

Hello good morning. I have two questions to ask, thank you very much for the call. Number one, I would like to ask about the backlog of products and contracted products, especially US and Europe, if you are seeing an increase in demand or increase in backlog because of higher energy prices, especially in Europe because of the gas thing that is going on there.

So for example in Turkey, how could the Turkey plant help become more competitive in order to gain market share? I would like to know more about the scenario in new markets.

And the other question which is slightly simpler: could you talk to us about the working capital, inventory and your basing? Thank you very much.

Mr. André Luís Rodrigues – Chief Financial Officer

Hi Lucas, thank you very much for your question. So first I will talk about the backlog and the long-cycle dynamic, first starting with electrical electronic equipment, the industrial ones. So the orders are being placed as in the last quarters overseas, the highlight is oil and gas, mining, pulp and paper and projects related to that. The portfolio is healthy for future months, and we have good prospects to build a positive portfolio until the end of 2023.

When we go to generation, transmission and distribution, the portfolio of orders is still robust with deliveries being programmed for 2023 and early 2024, as Salgueiro talked about the wind turbines and it is very positive, especially for T&D in North America and Central America.

Now short-life is more limited to more or less three months into the future. So what we see today is that in 2H TY its performance was very positive. Some countries have some fluctuation; but even so above average as compared to the year before. So in short-cycle or short-life we are talking about slightly shorter time spans.



As WEG continues it is one of the avenues of growth, which is to go international, and as you said having a plant in the future, so it is going to be an assembly line -and might become a full factory in Turkey - will help us to go into new markets as in our industrial strategy in Mexico, always creating additional opportunities.

And another example is the low-voltage engines manufacturing plant in India that is going to help us in this process.

So the message is we are not seeing, long-cycle is doing very well. Short-cycle we are still at a better level than we were last year - and we are doing our homework to continue the process of going international and seek new opportunities.

As to working capital, we have not had any major changes as compared to what we have been reporting over the next quarters. We were very fortunate in increasing our inventory levels as a strategy to ensure the continuity of our businesses. We have always been reporting that no, none of WEG's customers had any shortages of our products because we have this verticalization, which is a competitive advantage; but there is a penalty in terms of inventory levels. Along 2H TY we are going to see a reduction.

And other performance indication both in terms of accounts payable and accounts receivable, everything is business as usual. So the increase in working capital yes, it is concentrated in inventories.

Mr. Lucas Marchiori - BTG Pactual

Thank you very much for your answers, André. Now a follow-up: this increase in energy costs, especially in mature markets - I am talking about Europe - how long does it usually take until it is reflected in your backlog to be converted into orders? Or when you see a commercial do you see an increase in demand? So just so that we can have a feel about the energy market in Europe.

Mr. André Luís Rodrigues – Chief Financial Officer

Well, in terms of energy and new opportunities for energy generation in Europe, we do not have a significant exposure. It is very small in Europe. We have gas turbines which might generate good opportunities; but this is not WEG's main or core business. We may have some opportunities in generation; but it is not immediate. Things will start to happen from now on.

Mr. Lucas Marchiori - BTG Pactual

Thank you very much, have a good day.

Operator

Our next question comes from Victor Mizusaki from Bradesco BBI.

Mr. Victor Mizusaki - Bradesco BBI

I have two questions, first one this is similar to Lucas' in terms of inventory of raw materials. How long is the impact of raw materials reflecting in WEG's margin? In 2Q are inventory levels higher in terms of providing products to customers? But there is this time mismatch between spot prices that dropped. So what should we expect in terms of fluctuations in WEG margins in the future?

And the second question is related to the 7 MW wind turbine. How does it impact WEG's competitiveness, both in Brazil and in other markets such as the US market?

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Hi Victor, this is Salgueiro, thank you for your question. As to inventory you should remember that we do have the inventory issue, and as André said in his last question they have, they are slightly higher considering the global supply chain; but another factor that we should mention is that for some raw materials, especially copper; so in order not to have the impacts of fluctuation that is so significant on spot prices directly in our inventory so that we have predictability.

So to have accurate timing, so if we consider inventory levels that we have plus production structures and pricing, I think it will be something like six months or a little bit more for us to see this transition or changes in raw material costs so that this is somehow reflected in our results.

Mr. André Luís Rodrigues – Chief Financial Officer

As to the wind turbine, we have recently announced the development of our 7 MW wind turbine. We should mention that this is the biggest machine ever



developed for the Brazilian market, and I think that thinking of prices and profitability, so in absolute terms it will be necessarily bigger than the 4.2 MW; however, relative prices in terms of BRL/MW will provide a gain for each equipment user.

So we are expecting higher profitability than we are practicing today. So yes, the expectation is that this is a new product with new technology that will provide better profitability than the current machine.

Mr. Victor Mizusaki - Bradesco BBI

Just one point: would this allow you to take this wind turbine (the 7 MW wind turbine) to India and have a slightly faster ramp-up of your operation, also in the US? And we see WEG with a very strong presence in transmission and in transformers. Does it open this market for WEG in the US?

Mr. André Luís Rodrigues – Chief Financial Officer

Well, specifically talking about India we are certifying the 4.2 machine and today it is, as far as we know it is the biggest machine available in that country. So I think that now we have many, many opportunities to explore with the 4.2 machine before we think of the new machine and trying to find opportunity for it.

So focus today is much more in Brazil. So one thing that we may try to find in other markets in the future is that the new product has a modular configuration with components, separate components that make transportation easier, and then if we have the opportunity we can try and find new markets, and as you said the US.

Mr. Victor Mizusaki - Bradesco BBI

Thank you.

Operator

Our next question comes from André Mazini from Citibank.

Mr. André Mazini - Citibank

Hello, thank you for the call. I have a question about electric mobility line. How is the certification of electric cars going in Europe, which is the next market after you focus on Lat Am? So Europe will be starting the production of new electric cars in 2025 and will increase demand. So we have a partnership with Volkswagen. Should we expect other partnerships? We know that BYD is here in Brazil, it has three plants with new models. We have more partnerships and even considering batteries? Thank you very much.

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Hi Mazini, thank you for your question. As to electric chargers or recharge stations, we have, our main focus is Brazil. So at first we want to address Brazil. We think that Brazil has a big opportunity for growth. It is always good to reinforce, WEG is the only company that has developed and manufactures this product here in Brazil, and this is a market that we know really well. So we already have a network of distributors and integrators that can help us in this business, and this is being reflected in the partnerships that we have been announcing with chief OEMs.

So major OEMs of electric vehicles, especially light vehicles, whenever they announce light electric vehicles they approve WEG as a partner in terms of chargers. We already work in Argentina and we have a focus in some other countries in Latin America.

In any way we can imagine that this product, even though we are starting it here in Brazil it can have more exposure than just Latin America. We sent some recharge stations especially to our affiliates in Europe; but there is still a certification process that has not finished yet, and the commercial effort at first is very much concentrated in Brazil and in Latin America. So I think that Europe and other regions will be left to the future.

As to the powertrain, it is always good to stress that in our case at least for now the focus is powertrain for heavy vehicles, whether trucks, buses and some other kinds of vehicles; but this overall vehicle on heavy vehicles, the main partnership is with MAN Volkswagen. We are recurring deliveries taking place.

But we have some other partnerships that have been announced: we have a bus with Volkswagen, we have a partnership with Marco Polo that is developing an electric-powered bus developing it with WEG's powertrain.

And if we have the opportunity of having new partnerships and continue developing this market, we



are paying attention in everything and will continue to discuss with potential customers. So this is the major focus of our commercial team to seek these partnerships and to develop this market here in Brazil.

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Mr. André Mazini - Citibank

Very clear, thank you very much for your answer, have a good day.

Operator

Our next question comes from Gabriel Rezende from Itaú BBA.

Mr. Gabriel Rezende - Itaú BBA

Hello, good morning for the space. I have two questions to ask, number one relates to your CapEx budget that you announced in the beginning of the year. It looks like that the level in 1Q and 2Q is going to be 1 billion, to get to the 5 billion that you are expecting for 2022.

How are you thinking about this amount? Is it going to be lower or in a scenario with considering the commodity prices, a scenario that might be more favorable to your budget, are you going to deliver the same CapEx with a more controlled budget?

Number two regarding transmission lines. A few weeks ago we had the auction that was very interesting of 15 billion BRL in investments to be made over the next few years. How much of that could be addressed to WEG? How much is coming from the auction? Is it going to benefit you? By how much?

Mr. André Luís Rodrigues – Chief Financial Officer

Hi Gabriel, thank you very much for your questions. As to the CapEx it was 1.5 billion BRL, bigger than the last few years because of the delay of projects that were carried over from 21 that we did not implement, and also to support our current levels of growth of our company. Slightly before I answer the question in terms of the outlook, as a reminder of this capital budget about 55% are meant for Brazil and 45% for overseas operations.

Even with 1.5 if we realize 500 million, something like that in 1Q, we expect to be in 1.2 more or less. This is how much we will be able to execute - but not because of delay or cancellation of projects; this is more related, so we approve the budget and then projects evolve, and it is natural that a few things are left for the next year.

Considering our visibility today, this number would be much closer to 1.2 billion for the year, and of course the delta of that amount will be carried over to next year.

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Gabriel, as to the last transmission auction the main piece of news is that once again we had a significant auction. In 2020, 2021 auctions were much below average, especially because of the pandemic - and now we are back, and we had an auction of 15.3 billion in terms of estimated investment, which is very good for the industry as a whole.

In terms of expectation, nothing has been contracted or signed in terms of the projects that have been awarded in the auction. They will be discussed over the next few quarters in terms of its commercial terms; but there are some players that have won some slots of the auction, which historically have a close relationship with our company. Nothing has been effectively contracted; but considering the volume of investment expected for the next few years and considering that this auction has a higher amount in terms of investment, this is positive news for us and good prospect for our T&D businesses in the future.

Operator

Our next question comes from Jonathan Koutras from J.P. Morgan.

Mr. Jonathan Koutras - J.P. Morgan

Good morning everyone, congratulations on your results. First about margins, you have been saying for a few quarters that there is a mix in wind and its impact, and there is an EBITDA margin which is at about 7.5, 18%, and copper has slowed down recently.

So I would like to ask about G&D in the international market. Could you give us some more color on that? And in the release you mentioned that important units were delivered in the year. Could you disclose that to us? Thank you very much.



Mr. André Luís Rodrigues – Chief Financial Officer

Hi Jonathan, thank you very much. In terms of margin for the future, in terms of what we have announced earlier this year, so in 2021, the margin should be within the expectations. We have no indications that there will be any additional reduction as shown in LQ 21. So it should not be below 17.2 and should not exceed 18%, it would be in between.

So I think that is what happened in 1Q - I am talking about the recurring margin - and in 2Q it is in line with our expectations. We should always say that even though margins are lower, slightly lower than what we had in the last two years, I think that the level of 17 something is a level where we still deal with pressures in terms of seeking raw materials in 2Q, this disturbance in the global supply chain and the increase on the revenue of businesses that usually have lower margins such as renewable energy, such as solar and the wind turbines, I think that this is a very healthy and good margin for the company.

You talked about the trends of copper prices. Yes, we are seeing a trend of stabilization, in some cases reduction of our raw materials such as copper. It seems that this is a more structural movement; but it is good to remember that it takes a while to be reflected in our cost structure.

So I think that this effect - if it is in fact structural and really takes place - we should see its effects more in the future, not immediately because this is inventory that we bought at the prices that we had before.

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Jonathan, as to international GTD this is a business area that has grown a lot in the last few years, especially after the acquisition of our transformer business in the US. So this has been the main highlight in growth.

And specifically this year what happened is that we reported this last year. There were some very important projects going on in South Africa, in Colombia and also some deliveries of important projects in steam turbines in Europe, which ended up creating a relatively strong comparison basis in 2021.

Now in the first quarters of 22 we can see that T&D businesses as a whole are growing especially in North

America; but because of other regions when we see the total consolidated number we can see a drop in revenue.

In any way the outlook is positive. In September last year we opened our third factory in the US, now we are investing to increase T&D capacity in Mexico and the second one in the US.

And at the portfolio, as they said considering previous answers it is positive, especially considering our businesses in North America. So we have positive prospects and the external market is going to grow over the next few quarters, and we look at the comparison basis comparing 2Q compared to 1Q, so we are going to continue from now on.

Mr. Jonathan Koutras - J.P. Morgan

Very clear, thank you very much.

Mr. Marcelo Motta - J.P. Morgan

Perfect, thank you very much.

Operator

Our next question comes from Andressa Varotto from UBS.

Ms. Andressa Varotto - UBS

Hi, good morning for taking my question. So I would like to ask about electro-electronic equipment in Brazil. Could you give us more detail about long-cycle versus short-cycle in the domestic market? Thank you.

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Hi Andressa, thank you for your question. Well, actually in industrial electro-electronic equipment both in Brazil and overseas we still see quite positive demand from the industrial standpoint. Even when we analyze the details we see that demand is very pulverized in all industrial segments, which confirms the fact that industrial demand is positive.

So here in Brazil we see segments such as agribusiness and mining doing very well; but somehow what we can say is that demand is positive for all products, especially industrial engines, reducers and automation. Some new



businesses that are being developed are part of industrial electro-electronic equipment, for example digital businesses. So when we add up all the businesses with the good dynamics of the manufacturing market as a whole, we have this growth performance both compared to last year; but also compared to 1Q TY.

Ms. Andressa Varotto – UBS

Thank you very much.

Operator

Our next question comes from Régis Cardoso from Credit Suisse.

Mr. Régis Cardoso - Credit Suisse

Hello, good morning Mr. Rodrigues and Salgueiro. There are two topics I would like to touch on, number one more general about this risk of recession. Are you thinking of slowing down your investments? So considering the risk of recession I could understand the timing for capacity ramp up both in India, China and now Algeria; so how much of that capacity depends on a faster pace of economic activity? This is one question.

The second question is about margin and there has been a drop in sequence, and my question is this reduction in margin and how much of it is explained because of inventory turnover? And how much of it can be explained by the FX rate because the BRL was higher before? And also, or how much of it is explained by the mix as we mentioned about the wind turbines? And ultimately whether this is commercial issue and margin pressure in the competitive environment.

Mr. André Luís Rodrigues – Chief Financial Officer

Hi Régis, thank you for your questions. Number one, we are not seeing any need to change our pace or our investment strategy because of a possible recession very soon or in the long-term.

Number one, the company has a long-term vision in having a strategic plan, and we are very disciplined in executing our strategic plan. Quite the opposite, these new fronts that we are opening help us to have share in a market where we are not present today, where we

have a low presence that help mitigate an unfavorable economic condition.

As to timing, our plant in India is ready. It is just, we are just waiting about the local issue of installing the electrical, wiring aspect locally. We are finalizing almost all civil works in China. Number one, it will be in assembly-line, components will be manufactured in China and Brazil and made available to the local market for the assembly so that WEG can start participating not just in the Turkish market but in other countries around, and this will happen over the next few weeks.

And Algeria as we ended the JV, as we announced this week we are expecting to start production in 4Q TY.

So everything that these three projects it is a matter of a few weeks, or some weeks or a few months to start contributing and adding growth opportunities for the company.

As to margin, once again we consider that margin is within expected levels. If we look at the adjusted margin in 1Q (17.7, 17.4) it is just what we were expecting, it contributed to this short drop in margin. So the FX rates for sure if we consider the FX in 1Q is 5.3, now 4.92, there was a 6% reduction; and then if I bought raw material at a high FX rate at 5.23 and I am going to export at a lower FX rate, there is an impact on margin.

There is also an impact of the issue of growth on the renewable energy, so wind and solar that are businesses. Wind is that a production capacity of 1Q was the same as in 2Q; but solar, and solar and wind are businesses with lower margins that may have an impact; but we are not seeing any impact, the commercial issues having any impact on margins.

So once again, so within the macroeconomic scenario we are dealing with all operational difficulties. So this is a diagnosis of the margins in 2Q.

Mr. Régis Cardoso - Credit Suisse

I understand. Thank you very much, congratulations on your performance.

Operator

Our next question comes from Bruno Amorim from Goldman Sachs.

Mr. Bruno Amorim - Goldman Sachs



Hello good morning everyone, thank you for taking my question. Number one is about operational leverage. So in the last few quarters most of that idle capacity that was created in the last crisis of 2015, 2016 was being used.

Can you give us an update per product type and geography? Where do you have any capacity for operational leverage? Where are you planning investments to continue growing?

And the second question is a follow-up regarding distributed generation in terms of GTD, and you mentioned especially that there was a lot of prebuy because of expected changes in regulation next year, and I would like to understand whether this limits the growth next year or if there is a very difficult comparison basis. Is it still possible to grow? That was my question, thank you.

Mr. André Meneguetti Salgueiro – Finance Director and Investor Relations Officer

Hi Bruno, thank you for your questions. As to the utilization capacity, in fact we have grown a lot in recent years. We have grown in operations here in Brazil and in operations, in overseas operations.

So on the whole I would like to give you a vision in terms of our capacity, and it is never going to be 100%. We can say this is completely full, all operations in terms of engines and automation, also including WEG Power. This is where we have middle voltage and also T&D operations.

So these operations are going on today and we are investing. André has just answered about CapEx, and the biggest CapEx this year is for that. So that we grow on those operations we are expediting our investment program.

We still have some capacity in some long-cycle operations especially outside Brazil, especially in terms of generation, hydro, thermal and medium-voltage engines.

Now we have some capacity in commercial engines and appliances here in Brazil because of this dynamic, and we still have some space in paint and varnishes, where we could have some growth without demanding much increase in capacity, in terms of qualifying the business unit.

As to GD prebuy, even the word prebuy we have been hearing a lot about that in 2019 when regulation was supposed to change, and then it took a little bit longer; but the fact is that for 2023 the regulation has not changed, so it is right to say that 2022 is a positive year.

And part of that is definitely projects that people are trying to advance to make them fit into the older rules, and in some cases even along the first months of next year because there is an issue of the request for connection of the project, and then you can still work for a few months to complete the project.

But there is some effect along this year, and this is bringing a higher demand and obviously this is going to create a comparison basis that is strong next year.

Now to talk about the expectation for next year it is still kind of early. So we are talking about GD. It is a short-cycle business, so we have a portfolio. Our portfolio is usually three, four months that we have of visibility.

We imagine that part of GD and then power plants are likely to feel slightly higher impact, and then this part of the businesses historically was not so relevant; but it started becoming more relevant in 2022 because these projects are being advanced along the year; and the rest of GD involving high consumption and retail in theory should continue to be developed.

So it is hard to imagine what will be the performance next year; but the fact is that we have a stronger comparison basis this year and the challenge in order to have a growth, especially the robust growth that we have had along the last few years will definitely not be possible next year.

Now to imagine what will be the effect and how this market is going to develop next year, we are only going to have a better visibility once we get closer to the end of the year.

Ms. Bruno Amorim - Goldman Sachs

Thank you very much.

Operator

Ladies and gentlemen, we are now ending our question-and-answer session. I would like to turn the conference over to Mr. Rodrigues for his closing remarks. Please Mr. Rodrigues, the floor is yours.

Mr. André Luís Rodrigues – Chief Financial Officer

So once again thank you all very much for your attendance and see you in our next call.

Operator

WEG S.A.

Conference Call - Earnings Results 2nd Quarter 2022

July 21, 2022 – 11:00 a.m. São Paulo (BRT)

Transcript of the simultaneous translation from Portuguese into English



WEG's conference call has now ended. We thank you
very much for your attendance, have a good day.
