



## SABESP 4Q19 EARNINGS CONFERENCE CALL

**OPERATOR:** Good afternoon, ladies and gentlemen. At this time, we'd like to welcome everyone to Sabesp's Conference Call to discuss its results for the year 2019. The audio for this conference is being broadcast simultaneously through the internet on the website <https://www.sabesp.com.br>, where you can also find the slideshow presentation available for download. We inform that all participants will only be able to listen to the conference during the Company's presentation. After the Company's remarks are over, there will be a Q&A period. At that time, further instructions will be given.

Should any participant need assistance during this conference, please press \* then 0 for an operator.

Before proceeding, let me mention that forward-looking statements are being made under the Safe Harbor of the Securities Litigation Reform Act of 1996. Forward-looking statements are based on the beliefs and assumptions of Sabesp's management and on information currently available to the Company. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions, because they relate to future events and therefore, depend on circumstances that may or may not occur in the future. Investors should understand that general economic conditions, industry conditions and other operating factors, could also affect the future results of Sabesp, and could cause results to differ materially from those expressed in such forward-looking statements.

Today with us we have Benedito Braga, Chief Executive Officer; Rui Affonso, Chief Financial Officer and Investor Relations Officer, Mario Arruda Sampaio, Head of Capital Markets and Investor Relations; Sílvia Xavier, Head of Costs & Tariffs; and Marcelo Miyagi, Head of Accounting. Now, I will turn the conference over to Mr. Braga. Sir, you may begin the conference call.

**MR. BENEDITO:** Thank you. Thank you very much. Good morning, good afternoon or good evening to all of you around the world. We are very happy to present to you today the excellent results, the excellent economic and financial results of our Company during the year 2019. Unfortunately, we are in a situation today in Brazil and all around the world, with the coronavirus pandemic, that is frightening people and impacting different sectors of the economy, as well, and health and the lives of people.

Sabesp is, as you will see, very strong at the beginning of this pandemic in São Paulo state and in Brazil. Our Company is prepared to help the authorities in solving the problem of the pandemic, because more and more people at the highest level of decision-making are understanding the relationship between sanitation and health. We have been speaking about sanitation and health for decades. And this time is when everybody understands even more clearly this very close relationship, because without water security, clean water, safe water security for drinking purposes and for cleaning purposes that is essential during this pandemic and for cleaning the streets, hospitals and all these important elements facing this pandemic, it becomes more and more apparent.



And with this, I would like to stress some of the good positions we have today in order to help the government of São Paulo and Brazil to improve this very difficult situation in the health sector. We, in the last year, had a very important profit of the Company. We managed to bring in important municipality services in our business, namely Santo André with water and in Guarulhos with the sewage contract in the Company. This has improved our EBITDA margin as you will see with the presentation of Mario Sampaio in a moment.

I would like, as CEO of this Company, to stress to you that we are prepared to face this new crisis the same way we faced the water crisis that abated over us in 2014 and 2015. Sabesp has already a record of facing important crisis situations and this one is not going to be different from the previous one. We're going to face it and we are going to win. And with this, I would like to pass the floor to Mario Sampaio, to present to you the excellent results and you will appreciate how prepared we are to help the pandemic in the state of São Paulo.

**MR. MARIO:** Thank you, Mr. Braga. Let's start on Slide 3. Here we will present the evolution of the billed volume. So, the total volume billed in 2019, disregarding the volumes of the municipality of Guarulhos and Santo André, grew by 2.7%, 2.4% in water and 3.1% in sewage. When we include Guarulhos and Santo André, the volume billed shows a total growth of 3.5% with 0.2% in water and 7.7% in sewage. This is reflecting the migration of this municipality situation in which our company supplied water in the wholesale for the situation whether we directly today provide water, both water and sewage service, as I said, on a direct basis.

In retail, excluding the effects of Guarulhos and Santo André, the greatest relative growth was observed in the public category, with an increase of 4.6%, followed by the 2.7% increase in the residential category, 2.4% in the commercial category and 1.7% at the industrial category.

Let's move to Slide 4, we will here comment on our financial results. In 2019, our net income reached BRL 3.4 billion compared to a net income of BRL 2.8 billion in 18. This is an increase in our bottom line of 18.8%. This variation results from several factors, the most significant being the recognition of an extraordinary revenue resulting from the signing of the contract with the municipality of Santo André of BRL1.3 billion and the financial result that varied positively by BRL 230.6 million.

Net operating was BRL 18 billion compared to BRL 16.1 billion in 18, representing an increase of 11.9%. If we disregard the effect of Santo André in 2019 and Guarulhos in 18, net operating revenue was BRL 16.7 billion in 19 and BRL 15.2 billion in 18, which shows an increase of 9.8%. Regarding cost, administrative and commercial expenses and construction costs, there was an increase of 12%, mainly in services, electricity, general expenses and depreciation and amortization.

Adjusted EBITDA for 19 reached BRL 7.5 billion, an increase in 14.8%, or BRL 970 million in relation to BRL 6.5 billion presented in 2018.

The adjusted EBITDA margin in the year was 41.8% compared to 40.7% in the previous year. If we disregard the effects of revenue and construction costs, the EBITDA margin was 49.5% this year compared to 48.8% last year.



Let's go to Slide 5. Here, we will highlight the main events that impacted the result in 2019. Let's start with the signing of a contract with the municipality of Santo André, which was undoubtedly the highest highlight event for the results presented this year of '19. Company signed an agreement with the municipality in July, starting operations in August. In the year, the net non-recurring effect of this agreement, as we mentioned, was BRL 1.3 billion in revenue.

The operation in the municipality is still recent, it needs adjustment and investment, but it already shows a consistent perspective. So far, the transition has been successful and indicates that the results tend to be less impacted by adequacy costs that we observed in Guarulhos. In 19, there was a retail revenue of BRL 140 million.

After a full year of effective operations in Guarulhos, even those circumstances were more challenging than initially expected, with approximately one million people affected by the water rotation and not eight hundred thousand as initially forecast, Guarulhos positively impacted the 2019 net results in BRL 230.7 million, with BRL 424.6 million in operating revenue and BRL 192.9 million in costs and expenses.

In the period, there was also the adaptation to the legislation in force with the formalization of contracts with the municipalities of São Bernardo do Campo and Guarujá, extending the provision of service for a period of 40 and 30 years respectively. However, this fact led to the closing of lawsuits, which had an impact of BRL 85.4 million in the Company expenses.

We also can highlight the first full year of operation of the São Lourenço water protection system, generating an additional expense of BRL 137.9 million compared to 2018, when the system did not operate the entire year, actually as of midyear on.

Another highlight was the reversal of the provision of the retired TAC in the amount of BRL 173 million in the salaries, charges and benefits to the social security obligation. This is due to the filing of the TAC for the retirees. On October 11, 2019, the prosecutor responsible for this TAC recognized that its object was fully complied with and filed it.

Let's go to Slide 6. We highlight here the main variations that impacted cost and expenses in 19. As already mentioned on the previous slides, compared to the same period last year costs, administrative, commercial and construction costs, increased by BRL 1.3 billion or 12%. If we disregard construction costs, administrative and selling expenses increased by BRL 1.2 billion or 14.3%. The main variations were BRL 387 million or 27.8% with depreciation and amortization, BRL 333.7 million or 22.6% with services, BRL 213.8 million or 22.2% with general expenses and BRL 183.5 million or 19% in electricity.

In services, several factors contributed to the increase in expenses, such as maintenance of water and sewage networks and connection expenses with employees assigned by the city of Guarulhos and Santo André, plus water metering and delivery of bill.

General expenses increased by 22% or BRL 213 million, this mainly due to the increase in the provision for lawsuits, the termination of legal proceedings resulting from the signing with the municipality of São Bernardo do Campo and Guarujá and the greater provision for transfers



to Municipal Sanitation Funds. We also observed an increase in electricity expenses, with emphasis on the entry into operations of the Jaguari-Atibainha Interconnection and of the São Lourenço water system, plus the start of operations in the Municipality of Guarulhos.

On the other hand, it's worth mentioning the reversion of the retired TAC, which we mentioned prior with BRL 173 million, positively affecting the accounts of salary charges, benefits and social security obligations. Also, the decrease in expenses with estimated losses on settlement credits for doubtful accounts by 23.3%, from 166 million in 18 to BRL 128 million in 19. For the further breakdown of these and other changes in costs, please refer to our release.

Let's move on to Slide 7. Here we summarize the variations that affected the Company's net income in 2019 compared to 18. Net income, as already mentioned, was BRL 3.4 billion; net operating revenue increased BRL 1.9 billion; cost and expenses, including construction costs, increased by BRL 1.3 billion; other operating income and expenses, including equity income, had a negative variation of BRL 50.2 million; financial results varied positively by BRL 230 million; and finally, income tax and social contribution, which grew by BRL 233 million, due to the higher taxable income presented in 2019.

So, in the next three slides we'd like to share with you a brief analysis of three management performance indicators, which are more specifically that of the gross revenue per cubic meter, operating expenses per cubic meter and EBITDA per cubic meter billed. For this analysis, we use the historical theory since 2014 of quarterly accounting data released by the Company. Additionally, we made some adjustments to isolate some extraordinary and relevant events that would distort the result.

Additionally, in order to look at the performance in the period on the same basis, we have brought all figures at average prices for the fourth quarter of 2019 updated by the IPCA, which is our inflation index.

Our objective with this approach is to look at the Company's performance through indicators over time and on the same price basis and not in nominal values, which quarter-by-quarter, where specific events may lead to comparison basis, as well impose difficulties in analyzing the Company's evolution and performance over time.

As you can see in the graph, gross revenue shows a consistent favorable evolution. In relation to operating expenses, it's clear that it evolves in a controlled manner and it's compatible with expenditure of our business in the period as a result certainly of disciplined cost management. Finally, as a result in large part of the behavior of gross revenue and operating expenses, we see a very consistent growth in EBITDA per cubic meter.

Let's go to Slide 11. We'd like to briefly highlight some points that we considered positive in 2019 and comment on how the Company is facing the crisis generated by the Covid-19 pandemic and its impacts on activity, economic activity, and certainly complementing Mr. Braga's speech at the beginning of the call.

So first, we highlight net income of BRL 33.4 billion in fiscal year 19, which complemented by BRL 2.1 billion in new financing supported investments of approximately BRL 5.1 billion.



The Company's performance in 19 was also marked by the significant expansion of its market. About 2.5 million people were added to the population served directly, when we add the populations of Santo André, Guarulhos and population growth.

The incorporation of these municipalities last year, as well as São Bernardo do Campo and Diadema in the past, represents a historic change in delinquency of wholesale and with wholesale customers. In 2019, the Company also regularized and added new contracts to its operated base. The number of contracts increased from 307 to 324, and its share in total revenue increased from 84.8 to 92.2, which brings more strength to our cash flow.

Moving on to Slide 12, the Company's achievements in recent years, with the implementation of new water production systems and expansion of connections between both water sources that serve the metro region of São Paulo, consolidated in 20 a more favorable water situation to face the pandemic crisis, compared to the existing conditions when facing the 2014 and 15 water crisis.

Our current water production capacity in the metro region of São Paulo is 12% higher, due to the addition of the São Lourenço Production System, with a production capacity of 6.4 cubic meters per second of water and sufficient to meet 10% of the current water demand in the region. Transfers between water sources increased 163% and between distribution systems over 300%, further increasing the water security in the region.

At the same time, water storage capacity grew by 8% and this does not include the Cantareira technical reserve. At the same time, the supply resilience in the metro region of São Paulo has increased. Production demand fell from 69.1 cubic meters in 2013 to 62.6 cubic meters in December 19, but currently we work with an average production level of 65 cubic meters, still below what we saw in 13.

On the availability side, we also improved. In October 13, the volume of reservoirs in the metro region of São Paulo amounted to 52%, against 77% today. In other words, the Company is better positioned to meet greater demand arising from the pandemic caused by the Covid-19.

On the financial side, the 2019 results also puts us in a better position to face the situation of the first quarter of 20, marked by the very high uncertainty and volatility of the economy.

We ended 2013 with EBITDA margin of 44.6% compared to 52.2% in December 19. The total debt over EBITDA and the net debt over EBITDA covenants before the water crisis were 2.32 times and 1.91 times respectively, against 1.7 times and 1.45 times in December 19. This is also respectively.

As for foreign exchange exposure, at the end of 2013 it was 39.1% against 48% December last year. Despite that the dollar value of the external debt remained at the same level, that is, in 2013 it was equivalent to BRL 1.579 billion and now, in 19, it is BRL 1.78 billion. Yet, the dollar estimated to exceed the total debt to EBITDA covenant in 13 was 5 in December with a dollar of 2, while in 2019, the breaking dollar would be 13 with a dollar in December of 4.03.





The actions aimed at reducing the foreign exchange exposure defined last year and commented in our third quarter call remain a priority of the Company in 2020, despite the effects of the Covid-19 pandemic on the volatility of the economy and exchange rates.

Moving to Slide 13, our last slide, the economic recession caused by the pandemic should not significantly affect the Company's revenues, even the low elasticity of demand in the face of changes in GDP. Probably residential consumption today, 82% of the billed volume, will be maintained or will increase slightly, while the demand for commercial and industrial categories today is 10% of the billed volume, maybe lower. due to the reduction in the activity of companies in these sectors.

To conclude, as disclosed in the material fact yesterday and considering that treated water is an essential asset in facing the pandemic of Covid-19, the Board of Directors approved the exemption for 90 days, that's out April 1st, the statements of the bills for customers registered in the residential, social and the residential favela categories, what reaches a population of more than two million people with very low income, exactly the population that is in the situation of greater fragility to face the public health and economic crisis.

The exemption for this period will be mitigated by reducing cost and expenses. That's not affecting the Company's economic and financial situation, which is something fundamental to maintain investments in regular water supplies, which collection and treatment. In addition to this initiative, we started to produce reused water with a higher concentration of chlorine to be used for cleaning streets and sidewalks in the vicinities of hospitals and others institutions dedicated to healthcare.

To finalize, the role that a sanitation company plays in fighting the pandemic is absolutely essential. The interruption of water supply may simply compromise the guidance given by the World Health Organization for everyone to maintain good hygiene habits, especially washing their hands frequently and correctly. For this reason, so that operation capacity must be preserved, and the Company must count on the active support of public authorities.

Well this ends our presentation or speech and initial speech, then we now turn back to questions and answers. Thank you.

### **Question-and-Answer Session**

**OPERATOR:** Ok, thank you, sir. Again, we will now start the Q&A session. At this time, I'd like to remind everyone, in order to ask a question please press \*1 on your telephone keypad at this time. If at any time the question may have been answered, you may withdraw your question by pressing \*2.

Again it's \*1 to ask a question. At this time, we will just pause momentarily to assemble our roster.

And our first question will come from Lilyanna Yang of HSBC. Please go ahead.

**MRS. LILYANNA:** Hi, thank you for taking my question. So, I see your revenues are growing a lot, your costs are coming down, but you have two events on the tariff, right? First is this May



of 2020. So when can we expect to hear more about the level type hike that it could get this year, if it should be pushing closer to inflation?

And maybe more importantly the second question is about your rate review of May next year. So, do you consider your current level of returns as reasonable or how can we see the price outcome for next year?

And how confident are you that the assets that you just acquired in Guarulhos and Santo André they're going to be reflected in the rate review? Or if you could give any color where you see the highest risks in the rate review process, if it is on the RAB, if it is on the OpEx level or if it is on the WACC level? Thank you.

**MR. RUI:** Lily, could you... you said two events on the tariff. I got the one on the rate review outcome, but what was the first?

**MRS. LILYANNA:** The first was on the tariff adjustment for this year, May 2020, if you think it's coming without risks in line maybe with inflation or about debt?

**MR. RUI:** Ok, Mr. Braga, would you like to comment on the first, on the tariff adjustment for this year? Hello, well, let me convey...

**MR. BENEDITO:** Hello, yes, I'm here.

**MR. RUI:** Ok.

**MR. BENEDITO:** Thank you, Lily. It's very important and very good questions. There is no indication at this point in time that we will not have tariffs adjustments. Yes, we should have tariff adjustments and now in April is the time when this adjustment will take place, but the only thing we must have in mind is that we are in the middle of a health war. The government of São Paulo is giving daily reports on the development of the pandemic in the state of São Paulo.

And, of course, we are expecting the adjustments at the middle of April, but we are following what are the developments of the pandemic daily. But at this point in time, we do not foresee any problem with the readjustment of the tariffs. Mario, please.

**MR. RUI:** Mario, can I add...

**MR. BENEDITO:** Yes, Rui.

**MR. RUI:** Braga, Lily, it's just one comment. As Mr. Braga said, we don't have any indication till now concerning the tariffs readjustment, but we cannot close our eyes that the facts, and I believe that behind your concerns some agencies, electricity agencies like ANEEL, ANASA are already postponing some readjustment of tariffs in the electricity and water, due to these huge epidemic and economic crises.

So if something like this happened to us, what we can't say, it's like in the past, like in the hydrological crisis, the Board of Processes and the Board of Directors of Sabesp will readily indicate that we will call for rate reviews on our tariffs. Remember in 2015, we asked, and we had the extraordinary tariff review in 2015. And if that is the case, for sure the Company will



ask for a rate review so that we can preserve our financials and economic indicators and sustainability management.

**MR. BENEDITO:** OK, Rui, thank you so very much. So, Lily, this is absolutely important what our CFO, very careful CFO, is informing you is that in the event of a postponement of the adjustment, we certainly will be compensated, and no economic or financial impact will occur in the Company.

**MR. LILYANNA:** Thank you, that's clarifying.

**MR BENEDITO:** Mario, would you like to address the second question?

**MR. MARIO:** Yes. Lilly, could you formulate it again, provided that we're talking here, I think, we covered, and Braga covered the tariff adjustments and the rate review. So, I believe the other relates to costs.

**MRS. LILYANNA:** Yes, the other question was more on the rate review of next year, because other works start already today for an outcome one year from now. So, I wonder where you see your biggest concerns or where we could see the highest risks to the rate review, if it is on the regulatory asset base, for instance, the incorporation of Santo André and Guarulhos in the RAP?

If you think it is more a work discussion or there is going to be like more than 8.5 or is it going to be more on the 7% level like electricity distribution companies, or if you think that the controversy might be in the OpEx level, because this was a big deal in the second rate review. So, it's just a little bit more color of what more or less is at stake here and what are the biggest priorities and concerns here? Thank you.

**MR. BENEDITO:** Ok, just make sure that...Rui, do you want to comment?

**MR RUI:** Ok. Lily, we're really just starting the real conversation, the discussion with CESPE, making our points and discussing the methodology of the most what are the most important steps. But when all of us were crossed by this epidemic and economic crisis that, more than others, it isolates everybody and puts the recent discussions in its hold only mode. So, at the point that we are at right now, I cannot see a measure, a big risk. As I told in our Portuguese conference, there is still a year ahead of us to the new tariff review. One.

Second, and hopefully we have past experience in a shorter time than this, a shorter period of time, I can see certain vantages and certain better points of view from the regulatory body at the beginning of this discussion, especially concerning the asset basics. Remember that we agreed to discuss these through the methodology of accounting numbers, rather than replacement value, that from our point of view is very good.

The challenge, as you mentioned, of course, remains on the new acquisitions, because in this case we have to go to the ground and to make the sales and it's time costly. But at the same time, I think the agents will take in consideration that go to the ground and test their assets in the middle of isolation that we are all together would be more difficult. So, we have to take in consideration in the final results of the tariff review.





In the other point, in the other side, remember that we have been discussing both on this, I believe that the agency disclosed this with you, investors, the possibilities to discuss and discuss it close finally these remaining 6 billion, it was 7 billion and then we're applying the corrections and retention and everything and still have 6 billion out of our tariffs, our RAB. So, this is a good news. The mere fact that after so many years, we start discussing this from our point of view it's good. We're looking to recover part at least of this asset base, so it's good news.

The only concern I have is time. Not time just because of the tariff review, but time in general, as we are isolated as all of these things, the timeframe, all of these things becomes slow, slowly and slowly, that's the point. But conceptually, I believe that they have more grounds to be more optimistic than in the past. We'll have to deal with these two major issues, but my belief is that the huge discussion will be in the RAB and in the treatment we have to make in the case of the big acquisitions Santo André and Guarulhos.

**MRS. LILLYANA:** That's very helpful, thank you so much.

**MR. BENEDITO:** Thank you, Lilly.

**OPERATOR:** This will be the final announcement. In order to ask a question, please press \*1 on your telephone keypad. Again, that is \*1 to ask a question. Again, we will just pause momentarily.

It looks like we do have a follow-up from Lilyanna Yang, HSBC. Please go ahead.

**MRS. LILYANNA:** Hi, thank you for the opportunity, nobody is signed up yet. So, one other question is regarding your foreign exchange debt exposure, and I understand from the call in Portuguese that you are already acting to negotiate a change in contract with the government agencies, mainly, to change your exposure from dollar or yen or maybe to something like local.

Would you give us an indication of what could be your cost of debt for funding in local currency? I know it's difficult to say now, maybe you cannot use data points that you might find helpful for us. Thank you.

**MR. BENEDITO:** Thank you, Lily. It's a very critical question. Well, I think that before Rui will answer very specifically on this one, that the decision of the Board of Directors and the Board of the Company on avoiding loans in foreign currency and making sure that we could find ways of exploring existing contracts loans into local currency. It's now very clearly stated, and it's not related to Covid-19, coronavirus. This was something we decided before this situation, but I'm sure that Rui has the details to explain it to you. Please, Rui.

**MR. RUI:** Hi, Lily. It's Rui again, well we are under discussion with these two major big financiers. They are the RDB and IDB, banks that together represent the stock of effects that around US\$ 600 million, so it's a lot. We are discussing so I cannot display the costs. Remember that the union, the federal government and the state governments, especially the federal are a part of these, because they are counter guarantee, they provide us the counter guarantee for those sovereign fundings.



So, we are currently in discussions with the World Bank and the IDB. What we can say to you is that we start the process to discuss and to reduce our exposures in the foreign currency exactly in those cases that we have long-term, low cost fundings and, as they are multilateral sovereign banks, funded by sovereign treasures and countries, so, it's easier, it should be easier to do that at a lower cost and in short that's the strategy. So, we are in need, the sooner we conclude at least part of these changes, we inform to you all the details you wanted and also, we wanted to have. That's it.

**MRS. LILYANA:** That's great news, thanks. For your bonds that are dollar denominated, how expensive would it be to hedge or is it not worth it at this point in time? And I assume that you have not hedged any of those since December 2019, right, correct?

**MR. RUI:** Right, correct. We don't have any of those, but they have the under clauses, the contract, the possibility to change. We see less costly costs rather than in the private capital markets. That's the important thing and as the volatility starts to be present, an important issue in our macroeconomic scenario last year.

Many, many months before the coronavirus appeared on the recession, the world recession appeared, we started to make these strategies. It's a long-term strategy, it's not just a one-movement strategy, but it's important, it's important. We believe that we choose the lower truths to catch and I believe there are lower, but they are big and important truths.

**MRS. LILYANA:** Great. Many thanks. I wish you all well.

**MR. RUI:** Thank you very much.

**OPERATOR:** It appears that we have no further questions. Now, I'll turn the conference back over to the Sabesp team for their final remarks.

**MR. BENEDITO:** Ok. Well, thank you for your participation in our call. Be assured that SABESP will continue to work very efficiently, very carefully regarding being prudent in all the movements that we make during this important health event that we're going through.

Be assured also that we have water security in the area, our sanitation sector is being preserved by the government as an important asset to solve the corona crisis. So, we are part of the solution and not part of the problem. With the good results of 2019, we are very sure that we will face the challenge and we will win the battles and finally the war.

Thank you so very much. I don't know if Rui would like to say some words before we close.

**MR. RUI:** Just to say thank you very much and our CEO in a clever way closes this call with optimistic or resilient message to all of you. Thank you very much.

**MR. BENEDITO:** Thank you all. Thank you. Bye, bye.

**OPERATOR:** We thank you also to the management team. Again, we thank you all for attending today's presentation. At this time, you may disconnect your lines. Thank you again, everyone, take care and have a wonderful day.