

CELG-T Acquisition Webinar – Transcript – October 14,2021

00:00 – Marília Nogueira

Good evening everyone. We are going to start now the webinar talking about the auction for the CELG-T acquisition. The presentation is going to be made by João Marques da Cruz, our company CEO and also Henrique Freire, our CFO. Together with us today, in addition to myself Marília, the Company's IRO, we have Luiz Felipe Falcone and Daniel Sarmento as well as the vice president of Generation and Transmission.

This webcast is being on our IR website, on the internet only, and later on we are going to make available the recording. Any questions can be asked on the webcast platform. Before starting I would like to let you know that any statement that may be made during this presentation are based on the Company's estimate and are subject to macroeconomic assumptions that may occur or not.

I will now turn the call over to Marques da Cruz to start the presentation.

01:17 - João Marques da Cruz

Good afternoon everyone. It is a pleasure to be with you today to talk about the acquisition of CELG-T. An acquisition that we tried and we succeeded. As you can see on the next page, this is a Company based as you can see in the map of Brazil, mostly in the state of Goiás. There is a bit of Mato Grosso do Sul state but mostly in the state of Goiás. That is a state, as we all know, in which energy consumption is increasing substantially. In fact, we have an increase of 3.7 times the average of the whole of Brazil. So, this is a state as you know, of agribusiness and this is relevant because we understand that we bought a platform for expansion.

It is true, this is a Company that has 756 km of line length as you can see on screen, a main asset that represents 744 out of the 756. The other two assets are very small as you can see, but we are buying and I think this is the first message. We are buying more than the set of existing assets. We are buying greenfield. And we are buying greenfield in the state of Goiás and also in adjoining states but mostly in the state of Goiás. So, that is the first message. This is a platform for expansion.

Second message, this is a concession of 23 years. That is, the remaining concession is 23 years and today over 50% of assets are with advanced depreciation. Which means that in addition to expansion that demand is going to call for, we will have to make replacement investments. So, once again, more than 14 substations and 756 km, more than the contracted RAP of 223 million, more than it all, we are talking about expansion.

Let's go on to the next page in which we can show you basically the ideas that justify the amount that we offered for this asset. An amount that was very much thought of, following the metrics that we used in prior auctions and acquisitions. And in private auctions we were not able to win, as CEEE-T. But this time we did. Some players, our competitors, decided not to take part of this privatization process but I am not here to talk about that. But they were the same metrics of financial discipline that we applied in the past, and that we applied for this asset. And fortunately, we were able to win the bid with an asset that in our point of view, enables us to have a shareholder's profitability that is real, and it is two digits. I said that in the press conference, in fact I said that twice. In the press conference right after we won the bid of B3 and I repeat it here today. And why? Because this is a fact. This is the truth. We do not share a profitability as is obvious but I would like to say that this asset has real shareholders profitability

at two digits. And that because, and I am going to one of the notes that is on the screen that you can see now, it is in English, it talks about Financial Structure Optimization. Which is, we are able to have a level of leverage and Henrique, our CFO of course is going to give you more color about the negotiation as is obvious, but that really enables us to have this relevant shareholder profitability.

Anyway, going back to the first of the six points. There is a high potential for reinforcement and upgrades. Pre-approved investments of 260 million. We are not considering the 260 million alone precisely because of what I mentioned. The great relevance of the state, which is central in Brazil, especially for expansion, agribusiness and therefore we do believe in the capacity to grow.

And also, we talked about the regulatory framework which is a type 1 model. As you know, and to be quite precise, the 756 km, there are 744 that are type 1 and then there are some kilometers that are type 3. That we have in our transmission lines. It's obvious that type 1 as we all know, and that's inarguable is more favorable to investors. I am not going into details but I'm certain that our CFO is going to talk about that. I haven't finished here but it's clear that I want to talk about our expertise, our know how and we do believe in operational gains. We do have an agenda of synergies that have already been mapped out. Of course, we are going to do things in respect of people and the state but we do have a clear agenda of synergies that we are going to put into practice and unleash value with the synergic movements that are going to be made. We are specialists in transmission, and you know, it makes no sense for us not to integrate this structure with a company that we have the stock close to 100%.

Also, I would like to point out the limited liabilities. Contingencies and liabilities that are limited. It's important to say here, that our prudence that made us lose CEEE-T in Rio Grande do Sul, that we know it is a fantastic company. We wanted to win the auction of course but this is a company that stayed on, it has actuarial contingencies that are significant. Not the case with this company. And as we are very sensitive to contingencies, I would say that this allowed us to be more aggressive in this bid.

Well, these were the key points of our acquisition strategy so now I will turn over to our CFO Henrique Freire to cover the next pages. Thank you.

09:54 - Henrique Freire

Hello. Good afternoon everyone. I think that we should go on to slide 4 of the presentation. I think that João has already given you an overview of the levers that support the assessment of this asset. So, I would like to go a bit more in to detail for each one of them for you to understand the rationale of this acquisition.

First, to talk about potential growth. And to talk about potential growth we have to talk about reinforcement and upgrades which have to do with two things. One, the replacement of depreciated assets, as assets depreciate they are going to be replaced for us to keep the parameters of quality. And here you have to remember that we have a set of assets that are already advanced in depreciation. A set of assets that were built you know, a long time, so in this 23 year of concession we do have a profile that is highly depreciated. Which creates a potential of investments and on the other hand, we have what we can consider an expansion which is the reinforcement of lines, transmissions, to cater to the needs of the demands that are placed.

And so, we have this estimate, and we already have 260 million, 254 million on the reference base of the auction. So, 254 million, now 260 million and this is the amount that is going to be spent on 2021/2022. Then 2023 is going to be a lower year and as of 2024 we understand that we are going to get to a certain level of stability. Just as a reminder, the Company invested in the last 10 years about 5.4 % of the asset base in reinforcement and upgrades. So, this is something that has been consistent.

And therefore we understand that the asset base is going to positively evolve and of course the creation of value of this investment has to do with how we are going to execute the Capex because you know, it is based on ANEEL regulation and therefore our capacity of execution is very important. And I think that our capacity of execution is well shown by what we did in recent years in our transmission process. So, we are very comfortable with this kind of project. We know them well, and we can execute them in a very consistent manner without setbacks and we can always advance times. And also, I would like to say that CELG also had you know, a very good result in the last cycle of investments that it made. And we are not working with averages, this is not something that we are going to project for the future, but it was based on a very important due diligence process that we conducted before the acquisition.

I think that we can go back to the presentation, please. It's slide number 4, ok? In just a second, we are going to replace the presentation and upload it again. Just bear with us a second. The presentation was in English. It could be kept in English but anyway we are going to turn to Portuguese. Could you please go to the previous slide? Yes, thank you very much. So, anyway just one more point before we move on to the next one.

As João already talked about the regulatory models, so I think we can go the slide number 5. On slide 5 we talk about the regulatory model. So, I think that the regulatory model is different from what we have, and it is common in auctions today. In auctions you generally have type 3 or APs. So you'll have the auction, you'll have the maximum allowed revenue and then it is updated by inflation and then you have the cost of debt of the market so basically it is a variable that is always in these auctions. But here, is slightly different. You have a component, that if you go to the box to your right, you will have first what we call the financial RBSE which is an indemnity that is paid and should be continued until 2028 and also the economic RBSE that is a steady base and is reviewed every five years until the end of concession that is 2042. And the average financial base is about 65 million.

Then we have our RAP that is associated to O&M. This is based on a benchmarking that is performed on the reviews that take place every five years. This is almost close to the real economic value that we are more used to, that is more usual in our other network structures. So, it is a RAP based on efficiency. And this is a relevant amount, almost 25% of the total RAP amount so it is important to be considered.

And then we have the RBNI. Which is the RAP that is connected to new assets or investments, and that can grow depending on the new investments. And new investments since 2013, so it carries over the investments that were made as of 2013 until today and it will continue from now on. So, you know that there are two lots, F and K, that have the conventional RAPs of the auctions of 2015/2016 and they are type 3. So, basically these are our RAP conditions.

Now we are going to go to the next slide. And here we talk a bit about efficiency against operating the asset. Here, we bring first a comparison which is a PMSO cost per kilometers of power line. With the different players, and this is a calculation made by ourselves and our consultants. And so, when you take a look at this RAP you see the efficiency of our operations

which is basically the same efficiency of CELG-T which is in the model. And again, that depends a lot on the line concessions which is a universal RAP but it directional of what we can do in terms of efficiency.

So, we are going to converge to an efficiency that is closer to ours in a time of two to three years. We are going to have an initial period which whilst in the RAP, talking about the conditions for the next twelve months, the tender documents, PDVs are slightly above the market which I think is suitable so there is an expectation that they are going to be quite well accepted.

And obviously, we as a company, have all respect towards the company and its people but we want to move towards a more efficient structure compared to what we see on this chart. And again, with corporate synergy potential gains of scale in a plan that is going to be developed in the due time. Again, in respect with the company that we are acquiring and considering all additional costs that we are going to have in the beginning, and that will be necessary for implementation. But again, we are quite comfortable. This is not a turnaround process you generally see in a privatization process. This is a company with several levels of efficiency and we believe that we are going to have a quite comfortable process along the way.

Going to the next slide. Here, I would like to talk a bit about our funding structure and contingencies. First about the funding structure, we have EDP Brasil that is a company with low leverage. You know that our net debt corporate EBIDTA is two times. If you consider the adjusted EBIDTA, that is when you discount RFRS of the distribution and etc. as we report, the number goes to 2.8 times.

And we are in the peak of leverage because we are closing, finalizing our main transmission lot so we are still carrying the debt. So, Capex investments made and still we don't have the benefits of the EBIDTA. So, this is a point that shows that we have more than room of accommodating this concession. Albeit on the other hand of the structure itself, we are going to do that with a vehicle, a company that is going to have in a space of amortization of 24 months so, it's going to be a bridge that will correspond to about 90% of the acquisition price.

And then, thinking of any turmoil of the financial market in the next year. We should leverage the company at a corporate level of net debt EBIDTA of four times which we believe is compatible to the asset and to the debt that we have issued. And in terms of cost, you know our presence in the capital market, so at a cost that is quite suitable.

In terms of contingencies, we have remote, possible and probable contingencies. We are talking about anything that is below 15 million Reais. And again, it is a situation that is very different from other auctions that we took place. This is a very clean company, in a way that is not carrying too much contingency. And of course, we have an exhausted due diligence process and we even track contingencies that are not material, but we consider that we can go up to 20 million Reais. With land related and labor related issues which are typical with this kind of asset. But again, not saying completely irrelevant, that have to do with the profile of the assets that we are talking about.

And here, I will finalize my part and now I am going to turn back to João to close the presentation.

23:30 - João Marques da Cruz

Thank you, Henrique. I would please refer to slide number 8 which is an illustration of the four avenues of value that we believe that this asset can yield. With these four forms of creating value, and without them we wouldn't offer the prices that we offered. Which are they? New

investments that we talked about, and in addition to additional investments, we also have sourcing optimization. That is, to buy better than the reference amount that the seller had, and in fact, the Company is already doing that and will do this even better. Also, constructions ahead of schedule which is a rule of thumb for our transmission business.

Operational efficiency. I already talked about synergies. I have no doubts that we are going to have the synergies, we are going to find them, with respect to the people because these are our people now and we should always treat them right. But treating people right does not mean being efficient. We have to have efficiency and we have to have gains of synergy with centralized O&M activities. Obviously, we are going to have ZBP program as we have in all our assets, and then certainly we are going to adjust contracts.

Financial optimization. Basically, this is something that Henrique already talked about but obviously we are also going to have synergies here and also access to you know, other credit structures and leverage the capital structure. We are not going to disclose numbers, but you know, the bars give you an idea of magnitude and how we are going to add value to this acquisition.

Going to the last slide and then we are going to open for your questions. But in a nutshell, we bought basically the whole of the company, 99.9. You have preemptive rights of minority shareholders but you are talking about 0.1, 0.07 from Eletrobras and other shareholders, 0.03. So, if they do exercise their preemptive rights it really does not make a difference to us. To your left you see, according to the rules today we had the public auction session, until December 20th the minority shareholders have to speak up, most important the controlled execution between January 3rd and 28th, and then closing a settlement between February and March. And of course, before that you have the submission of documents to ANEEL and CADE. And here you have the five companies that were our partners and helped us out in the process, and I would like to thank them in public.

So, Marília, I think that we can go to our Q&A.

27:43 - Marília Nogueira

Thank you very much, Marques da Cruz. We have a first question from André Sampaio from Santander. The question is, what is the level of annual investment as of 2024? Is there a rationale behind using the PCH vehicle for the acquisition? What is the EBIDTA margin expected for the asset? And the 16 million, is it a reflex of the CAPEX of 260 million or is it an additional RAP?

28:19 - João Marques da Cruz

Henrique, you are on mute.

28:26 - Henrique Freire

I'm sorry. Ok, let's start with the acquisition. The vehicle is a company that we had, and it was used in the past. We had a project that did not develop, it was a hydric project and that's why its name. But it is a leverage structure which is usual in this kind of transaction. It makes you know, the channeling of resources easier so it is usual and typical. Other transactions are already made this way. Then you talked about the EBIDTA margin. Well, the EBIDTA margin should be about 90% which is, or somewhat close to this number, which is going to be a natural conversion. And once again it is not you know, a direct application of the RAP that I mentioned but is just directional so to answer your question, 90%. The 16 million, this is something that I think is very

interesting, this is not a RAP. The 16 is an annualized RAP and the annualized RAP considering the cycles 2021 and 2022 should be 223 million. And on the same reference date that is June 21st, it should go up to 245 million with the update. With the RSBC and the RAP referenced to that. Just to make the numbers clear. I hope I have helped.

30:32 - Marilia Nogueira

Our next question comes from Pedro Manfredini from Goldman Sachs. Hello, I would like to explore the financial engineering. Henrique said that you are going to leverage 90 points of the acquisition in another vehicle. Is it going to be operational? Are you going to have to have a tax shield? And 24 months later you are going to transfer the debt to CELG-T and then the remainder of 90 points is equal to 1.8 billion minus 1 billion that is 800 million. Is it going to be kept, this million, as an asset or are you going to use another operational vehicle?

31:27 - Henrique Freire

Ok. I'm going to go straight to your answer. We always keep our interest in having the efficient management of our debt which in general means to place the debt where it is going to be more efficient. And as a group, this is how we operate. So, initially the vehicle is not operational, it was a vehicle that was just organized for that, and that it may include an operational structure to include this asset. But not in the beginning. And then that that would be prepaid and refunded perhaps at the level of the asset. So that's the point. We can advance that if there is a merger process or something. So, we can advance this process, but these are our typical processes, so we are not, it's a very plain vanilla structure so to speak in terms of transaction. So, if I place that in one distribution company, this is not you know, to pay dividends and the other is to reinvest in transmission. It is a global management and what I can say is that we generally try to allocate our debt and capture the tax shield whenever possible. I hope I have answered your question.

33:15 - Marilia Nogueira

Still Pedro Manfredini. Do you believe that the return adjusted by the risk of the asset was more appealing than the new auctions?

33:27 - João Marques da Cruz

I am going to answer that. Yes. Undoubtedly it is more appealing. It is more appealing for us than the new auctions. I mean, I have no questions about that. In addition to the risk itself. Obviously in auctions, the lots are not bid and, in some cases, in many cases there are several issues that are related to the lot. So certainly, we like auctions. So we like bidding but the level of competitiveness and of risk or perhaps the competitiveness/risk ratio is more favorable in this case than in an auction because we continue to be interested in taking a look at other auctions and to know if we are going to take part or not.

34:38 - Marilia Nogueira

Our next question comes from Sara. She would like to know if we are going to give her any indication on EBIDTA or multiples in this acquisition.

34:58 - Henrique Freire

Well the structure, the multiples, is basically a summarized assessment exercise. I would say the structure, based on what I said on the RAP, it's not very easy to capture everything in the multiple and it's not up to us to do the math. I think that whatever calculation you make, you

are going to find out that the multiple is quite good. We have to remember that the company is in very good shape and therefore we have an equity value that can be a bit confused with the enterprise value. And the enterprise value is slightly lower if you do the math. And in terms of the EBITDA margins, I think that we have to think of what we can converge. I think that information is available for you to have your own calculations. But you have to make into consideration that this is not just a regular transmission auction, it has a network structure, more than a single power line, and that brings more interest in compensation structure. So, it is you know, a bit more complicated in terms of calculation, that whatever parameters that you choose you are going to see that it is quite appealing. Remember, this is a performed, built asset with high levels of availability that can be improved but that has high level of availability, so it is with a limited turnaround complexity. And I think with all that, I think it answers your question. It is at a suitable risk level.

36:54 - Marilia Nogueira

Well, since there are no further questions, we are going to close this webinar on the acquisition of CELG-T. All the material is available on our IR website and we thank you very much for joining us today. Thank you very much.