Q4 2016 EPM Earnings Conference Call (ENGLISH)

Corporate Speakers

- Jorge Andres Tabares; Empresas Publicas de Medellin; Executive Vice President of Corporate Finance, Risk Management, Investment

PRESENTATION

Operator: Good afternoon, my name is Richard and I ´ll be your conference operator for today at this time I would like to welcome everyone to the fourth quarter 2016 EPM consolidated financial results conference call. All lines have been placed on mute to prevent any background noise. After the speaker´s remarks there will be a question and answers session. Thank you for your attention Mr. Jorge Tabares, executive vice-president of Cope finances and investment manager of EPM group he will be the host and speaker for today. Mr. Tabares you may begin your conference.

Mr. Tabares: Thank you very much operator and welcome everybody and thank you for attending our quarterly conference call. I will present you with the fourth- II 2016 results and the full year results for the EPM Group. We do have a presentation that I am gonna show, now you can move to page 2 please. And the agenda is we are gonna talk about relevant events of the quarter and after the closing the energy market in the countries in which we operate If you are not updated on the Lituango Project and finally the financial results. Moving to page 3, after relevant events of the quarter during 2016 we pay so closes to what will be the discharge of dividends as elsewhere of 3.371 thousand Colombian pesos and during the full year 2016 we transfer 816,000 COP, for those of you who are not familiar with the exchange rate you can use 3.000 COP per dollar as a reference exchange rate for these numbers. At the end of 2016, the Board of Directors approved a budget of 12.5 billion COP for 2017 which is equivalent to almost 2 billion US, this is for the period 2017-2020.

Our investments, the group investments will total be 10.6 billion in the next 4 years from those 80% will be in Colombia and 20% in the international in bay, countries where we have investments. Looking at by segments, 73% of that investment, would be dedicated to energy, and 27% to the water service. From that amount 30% will be allocated to the Lituango Project, which is the largest country being built in the country and the largest ever in the corporative history of the group EPM. On March 14th, 6 ratings revised our international rating, moving it from negative to stable. And this is in parallel to the change in the Colombian sovereign rating. And last week Moody ratified our financial fondness but raising our international rating to BAA2 with a stable outlook that is after the active on a positive outlook that we had in place since 2014, a very relevant and positive event for the rating of EPM. Moving to page 4, we are talking about the Energy Market, here we have the total commercial demand in the countries in we which we operate and EPM shares of that in the oval in the second number below the square. The highlights of this information is that the Colombian market remains basically flat, in terms of energy demand and EPM delivers 24% of that demand during 2016. And you see better growth rate especially in Guatemala and Panama where the 2 most relevant operations are. We represented 41% of the Guatemala market delivering 4,253 years of hours to that market and 35% of the Panamian energy market. Looking at our delivery during 2016 we delivered 15,711 gigabytes hour and that’s the slightly piece of point 6 from the previous year that have noticed that part of that energy that was not delivered was due to the outage of the Guatape Plant and the revenue that was going to be provided by that energy was compensated by the insurance company that have the business interruption coverage for that outage. At the international market, we grew 0.6% delivering 9,345 gigabytes hour highlighting the benefits of the diversification of the portfolio well, the Colombian market, we decreased the international segments had a small increase in the energy deliver and from that I highlight the 3% growth in ENSA at the most relevant one. 3.7 decrease in El Salvador applies from a smaller base on those less relevant for the total results. Moving to page 5, the story about the Energy Market and the spot sites of the geographies in which we operate was negative the prices decreases significantly in all markets in which we operate 46% decrease of the prices of the stock prices in Chile being the most relevant number and in Colombia we have from the average spot prices we have a decrease of 27% moving from 132 to 96 dollars per megabyte hour. Looking at our generation business the generation decrease by 4.2% to 13.460 megabytes hour during 2016. And a smaller base we had a 20% decrease in the Cururos wind park energy generation and a 5.1 decrease in Bonji Panama. Then, here the 4% reduction in Colombia was more than compensated by the insurance company payment and if we were to account for that energy that was recognized in the insurance we will have otherwise grow by around 2% our energy duration in Colombia. Moving to page 6 most important project and where significant progress has been made during 2016.Lituango ended February of 2017 at 66.3% of completion without invested almost 6 billion dollars since the start of the project making very solid progress towards an on time and on budget delivery in November 2019. I'm sorry 2018. The dam construction is a 53%, the spillway construction is at 85%, and basically all the excavations of the powerhouse were concluded. We also have made significant progress in the generation equipment for the 2 baselines of phase I , they are all manufactured and the assembly is at 38% that's the top chart, that's a picture of one of the size of the generation cavern and from the 24 transformers 12, are already on its final location and finalizing assembly. Critical part of the construction are the two cramp bridges that would have 600 tons capacity and both are 100% manufactured and the first crane is already fully assembled. At this point, the efficiency in the progress of the project is related to installation of equipment and a serial construction as we have to do twice times, the same type of work for the first size of the transformer and 4 times the assembly of the generation unit. Looking at the total cost in page 7 set the project to finalize at 11.4 billion COP that's about 11.7 billion US and from the financing we have already financing in place for 38% of the total project cost is equivalent to 79% of the total estimated debt of the 64 structures that we have defined for the project. Those figures include a transaction which is currently under negotiation that should be executed within the next 6 months initially targeting 550 million dollars with the possibility of being increased as additional demand is found by IC and DIDB. Moving to page 8, 2016 was also a very heavy year for investments we invested a total of 3.5 billion COP that's about 1.16 US billion. Lituango is the most prominent investment for that amount about a third a 1.3 trillion COP but the investment profile is much diversified. You can see in the picture the EPM company excluding Lituango also invested 165 thousand million and from that 60% was dedicated to power mainly distribution business and in water we invested 36% on that's only the part of the company which basically covers the Metropolitan area of Medellin. The international subsidiaries we invested 629 billion COP 76% of that dedicated to power. The main investment there is the Guatemala transition line and expansion of our capacity of our infrastructures both in Panama and Guatemala and the final phase is The Aguas Claras Guatemala waste water treatment plant. Invested 37 thousand million COP and expect to finalize that project during 2017 and in the 4th Colombian Power subsidiary we invested 339 thousand Colombian COP. Moving to page 9, from the figures I quoted at the beginning 10.6 billion COP equivalent to 3.5 billion US the approved investment plan for 2017 -2020. 73% of that is power from which Lituango represents 30% but is also very diversified between the investment in the Metropolitan area and Antioquia where our headquarters is the international subsidiary with 21 % and the Colombian power subsidiaries with 18%. Also, I highlight the 6% investment dedicated to appraisal improvement that support our core strategy of gain efficiency and productivity across our operations.

This is a level of investment that is high on a relative basis compared to the historical investment rate and one that is gonna impact the future of the company given the additional asset base that we will have and that is expected to be remunerated at the regulatory remuneration rate which is value added for the group. Looking at the geographies in page 10 this is in order of relevance for our businesses from left to right, the size of the investments we have made and there you see the deceleration of the growth rate that has been experiencing in the past. Colombia, with a relatively low growth rate of 2% being the most important for the Group results. The GDP in Chile does not affect so much the ADASA operation as the water consumption is not very linked to that GDP growth, different from the energy market in which it actually had an impact and Guatemala and Panama showing although decrease low rate what would be considered healthy growth rate when you look at the global scale 3.1 and 3.9 percent are healthy growth rate when you look at the Global landscape. Moderation in the consumer price index across in the operation in the countries in which we have operations. Colombia is still on a relatively high size well above the 4% top of the target rate defined by the central bank but with clear expectations to coming on line those expectations in the next 12 to 18 months. The BPA in Colombia at 1.62 is also not worthy because it is low compared to the typical standards and the GAP between the BPA and the CPA has an impact on the 2017 results at this revenue because most of the non-regulated contracts are indexed to the PPI in our Colombian distribution operation. Also, across the South American operations and Central America the local currencies appreciated against the US dollar most relevant for us are Colombia and Chile we have a benefit of the same rates different in our net income and Mexico moved in the opposite direction mostly related to the Trump election in the US with a 20% devaluation from that already 20% had reversed during the first 3 months of 2017 putting the Mexican peso as the most appreciated currency across the globe. Moving to page 11, we show here the quarter results on the full year results and you see when we compare the 4th quarter 2016 to the 4th quarter 2016 there are significant improvements and that’s related to the fact that we are comparing Niño quarter which is 2015 with a no Niño quarter which is the 2016. The EBITDA moved from 5.95 more than double to 1 billion 227 million during the year with a 106 % increase. Most relevantly on the full year basis the revenue grew 14 % not of all is related to additional consumption or demand as I show in the previous information but related to the highest top prices that were in place in Colombia due to the impact of El Niño Phenomenon. The EBITDA grew at a healthy 12% rate probably the most important result and achievement of the group during 2016 a 12 % increase in our EBITDA putting an 4 billion 36 thousand million is about 1.33 US billion and the group comprehensive income situated at 1.8 thousand million COP with an increase of 85% and this has a significant impact due to the relative movement of the Exchange rate during 15 and 16 .If you look at the total numbers in the total group , energy sold during 2016 stands at 25 thousand Gigabytes by hour from which Colombia represents almost 16 gigabytes hour. The total water sold slightly reduced to 263 million cubic meter mainly impacted by the water saving campaigns that were put in place in Colombia related to el Niño Phenomenon and the lack of rainfall in the region, in the Colombian territory we treated 343 million cubic meters of water basically flat versus the previous year and the total gas sold increased by 4% due to the operations related to the Gas crisis and consumption associated with El Niño and the fact that we had to turn on our thermal plant in Antioquia. Also, very important in our results is that when we compared the recurrent expenses they grew below the inflation which is a reflection of the effort that the Group is being attempting to do in order to become more efficient. When we look at the full year results the EBIDTA margin grew from 26 to 27 percent in general achievement that we think is worth highlighting and reflects the effort across on the businesses and the services areas of the organization. The operational margin slightly decrease from 19 %to 18 %. Moving to page 12 this gives you a fairly good idea of the diversification of the portfolio from the total revenues we achieved 53% of those from the EMP prime company and the Colombian power subsidiaries delivered 13% of that and the international subsidiaries accounted for 32% so almost a third of the revenue during 2016 was delivered by the international businesses a reflection of the diversification of the portfolio. When we further split the 32% of the revenues in Guatemala and Panama represent the both of it with 38% and 35% respectively and when we look at the EBITDA composition I highlight that 25% of the EBITDA same from operations outside of Colombia at the ones in pesos delivered by the international portfolio. Guatemala is the majority of it with 42% but Chile is showing a healthy 25% contribution to that and this is in fact associated with the ADASA acquisition, ADASA was part of the portfolio only since June 2015. So, those 2015 figures accounted only for half year of the ADASA operation. Also, highlight the relative weight of the Chile operation in which the revenues stand it at 9% the EBITDA contributed at 25% of the group results and this is due to the fact that the Chilean operation has the much higher EBITDA margin than the rest of the international operations mainly led by the ADASA results. From the other side on the comprehensive income we have 81% of the comprehensive income being delivered by the EPM, power subsidiaries delivered 9, and the international subsidiaries delivered a relatively low 9%. Again, I highlight this proportionality in this case negative from the revenue contribution or EBITDA contribution to the net income contribution and this is related to the fact that we had to do some impairments that affected the net results in our wind power operation in Chile related to the lower energy prices in that country and also an impairment in Panama in our head subsidiary in our highest generation plant due to lower prices also in Panama. On page 13 we saw a comparison of the different assets outside of EPM, all of our investments in subsidiaries are on the horizontal axis , we show EBITDA margin for 2016 on the vertical axis we show the variation in the EBTIDA margin from 2015 to 2016 on the side of the bottom represented amount of the EBTIDA in Colombian pesos for each of the operations there I highlight 3 issues one is the ADASA, as I said before ADASA has an EBITDA margin above 55% and the EBITDA grew by 24% percent significant actually in this one is 32% when we look at the figures in Colombian pesos so, ADASA which was the most recent and the most significant acquisition that the group has made is delivering excellent results . You see the EBITDA changing negatively from 15 to 16 in the 2 businesses that I just mentioned Cururos and head Cururos in Chile and head in Panama. And finally, when you look at the very small dot on the left with a negative EBITDA at the Colombian water subsidiaries although this is not material at the group level I can say that we have made progress in the operating results of these businesses but, still have a long way to move in the results to the place in which we feel comfortable with. Moving to page 14 we have a different view of the same results showing power generation delivery in 22% and power distribution delivery 58% of the revenue. Distribution accounted for 48 % of the EBITDA and 44% of the comprehensive income this is considered very positive distribution business is not so link to rainfall patterns and the weather impact that El Niño o La Niña season may have on our portfolio. But, I also highlight here the light blue parts of the pie with the water operation delivering 9% of the revenue and 12% of the comprehensive income. This is how we combine our water operation in the metropolitan area plus the ADASA results. An important story on page 15 on the top side during the year we grow at equity by 5% this is mainly related to the net income less than the surplus that we passed to the municipality of 0.8 billion and the assets group by 2% mainly by the PPE line which is directly by infrastructures projects under construction mainly Nueva Esperanza and Lituango and during the year you may remember that we also sold the ISAGEN shares for 1.5 billion this is about 500 million US. On the left, the EBITDA ratio which is very closely monitored by us giving our commitment to having below 3.5 on a medium to long term as we have set since the 4th Q of 2015 we expected that the figure was going to be above the coming about 3.5 that was going to come on line during the first half of the year we did close 2016 with a 3.69 debt to EBITDA ratio still above the 3.5 we timely secure covenant from the 3 multilateral banks that have that covenant in place in our law agreement this is GBA and GFD and IDB and so for February the ratio already closed below 3.5 staying at 3.46 we expect for the improvements by the quarter end by one Q of 2017 that figure should still come down and when we look at the financial debt it was basically flat at 37 % and EBITDA to financial expenses moved from 498% to 479%. Finally, looking at the debt profile at the end of the year the company had 4.8 billion COP and on the right top side 29% of that is denominated in US dollars not hedge 77% is in COP and 9% is in Chilean pesos is related to the ADASA financing by local banks in Chile and the nominated currency. And the debt profile fairly miles profile cash demand for 2017 and 2018 and a peak of 3 billion dollars in 2019 associated mainly with the 2019 bond international US dollars bonds and the local banks loans to ADASA which we expect both to be roll over up at some point during the next 18 months the average term 75.67 years looking at the matrix of the portfolio debt. With that, I conclude the introduction I would like to open for questions I encourage you to make any question that you may have that could benefit not only you but maybe others in the conference call.

Operator: At this time I would like to remind everyone in order to ask a question simply press star, the number 1 on your telephone keypad if you would like to withdraw your question press the pound key or wait for just a moment to compile the Q and A roster at this time we are going to Provide 6 questions first from the audio conference and then questions from the web and we are sending by for question .Our first question on line comes from Richard from * Please Go ahead.

Richard: Hi you guys have discussed before getting to a target EBITDA above of 3 million dollars by 2025 and I just want to find out how do you think about that target now? In terms of achievability, and in addition to Lituango, what of the main drivers you know, to get EPM to that goal?

Mr. Tabares: Thank you Richard very good question and frequently asked both internally and externally. I'll start by saying that the Mega, as we called it because of the Spanish translation. The Mega is a long term vision that signals growth and the last time we run the numbers we expected that we were able to achieve basically a 3 x increase in the EBITDA figure to be delivered. At this point the key drivers to be able or not to achieve that goal are related to our investment ability we have growth coming from 4 different sources the main one coming from the efficiency and running the assets more competitively only put a lot of effort in achieving more efficiency and track operational performance across the Group in order to monitor and make sure we make improvements on that line. And the 3rd and 4th one are organic and inorganic growth. And the second one is how to innovate both in terms of incorporating new technologies or new business models that will allow us to continue growing, what this shows you in terms of the CAPEX, from 2017 to

2020 focuses on organic growth this is due to the fact that our portfolio is very robust and we see investment opportunities across businesses and across geographies. To give you an idea we have to connect around 100 thousand new clients every year and that demands investment and the remaining investment depending on the EBITDA deliver and the cash liability will be dedicated to acquiring companies we do not see any materials acquisition here in the near term because the CAPEX figure is demanding for us and we are not going to run the company on a sustain basis with a debt to EBITDA above 3.5 %. We are currently doing a study review working with a worldwide consultant to define based on the incorporation of the new technologies mainly solar generation, power generation and distributed generation in Groups in conjunction with energy storage. How these 3 new elements are gonna contribute to the EBITDA in the next 10 years of the company and so we will have an outcome of that consultancy and strategy review by the end of the year in which case we will have a better view of can we achieve that based on the technology adoption that we expect to happen in Colombia so at this point this number, the number that you could reflect and the last exercise we conducted in mainly here but we constantly reviewing what do we consider that is achievable given the energy markets , the prices and the volume that we are seeing an updating all the time combined with the adoption of the new technologies so to keep in mind and as a key conclusion and message about the growth, and the Mega and the 2025 target is that we are not going to abandon the investment rate and the conservative financial policy that we have had in place for many years now but on the other side we want to continue growing within the growth over the last 10 years which has been very healthy for the company that we have strong capabilities and know- How that could be applied in different geographies in different core businesses and we are going to pursue that growth with financial soundness maintaining our investment rate and debt to EBITDA at 3.5 .So I hope that it addresses your question

Richard: I guess, I think you already mentioned that you don't see too much MNA or new acquisitions are there other or certain countries so that you are particular interested in investing or you are deciding so, you know you see more investment focusing in there?

Mr Tabares: So, we, since 2010 we decided which ones were going to be the target countries and that's basically where do we have operations today Mexico, Guatemala, Panamá and Chile. We also think Peru maybe attractive , we used to consider Brazil as a target place but now we are kind of hold mode until we see more clarity on the governance regulatory and stability of the economy perspectives and we don't see and again just because the CAPEX portfolio is so significant we don't see as making any mayor investment over the next 18 to 24 months we do make small transactions basically in Colombia related to operations that are close to our operations and we can gain some important synergies or strategic benefits of conducting those acquisitions but none of them if they work to materialize would include a significant amount of money . Beyond that, we do expect to go back to those geographies and continue making acquisitions to support the group growth remember that in Colombia we are basically limited today in the growth due to the CAP of 25% that we have both in generation and distribution of energy so those are our main businesses today that are not allowed to grow in Colombia and the company is not doing any regulatory activity to have those CAPS removed.

Richard: Great, thank you

Operator: Thank you once again for any questions over the phone press start and 1 on your touch tone phone you maybe have a question using the Q and A on the web. We have a question on line from Roy from Bank of America. Please go ahead

Roy: All right, first I don't see the presentation available anywhere I don't know if this available on the link to the audio presentation because I can't access and I don't find it on the website I am not sure where it is I Can't find that. And the second one I am wondering, even that normalize even that margin of 25% or 26% on an annual basis and if the 4th quarter even that margin seasonably very, very low it was 50% this year and 60 % last year but, 3 years ago in 2014 it was closer to 31% So I wonder you know even if that normalizes now this current level 25% ,26% and what is the reason that 4th quarter even does so we can get it for sure the EBITDA margin ?

Mr. Tabares: Thank you, Roy so we will post the presentation soon after we finish this I would expect that some other of the callers were able to follow the presentation to the link and we have been kind of moving it along as we have made the presentation so I apologize you cannot see that. The format Roy is the same format we have typically shown. Ok, and then the second one is about the EBTIDA margin for the quarter and I am showing here 4th II 2016 of 27% compared to the 15% that is an abnormal EBITDA margin due to the fact that was impacted by El Niño in 4th II 2016 in terms of what we expect and we compare the numbers to the 2014 numbers we expect the EBITDA figures to grow higher the EBITDA margin figures to grow higher and in the following quarters and specially for the 4th quarter as you are comparing and then you asked why the fourth Q- 2016 is much slower than the 4th Q -2014 is that right?

Roy: Yes, yeah

Mr. Tabares: I have to go back to you and we can close on the line

Roy: Yeah, I'm just curious what is the normalize rate to the 4th quarter is it the 4th quarter seasonably low for some reasons that will allow us to expect a lower margin for the 4th quarter?

Mr. Tabares: No, there is no certainty What happens during 4th quarter of 2016 is that since when the Niño finished we went back to a relatively normal hydrology but at the end of the year the hydrology was very positive there was a lot of rainfall in Colombia and since that started to fill out our reservoirs we add not just hours but also the system and the energy prices went low so the spot prices of 4th Q were seasonably below and that affected our EBITDA margin we do not expect that we think that is abnormally and 29 or 30 % is a normalized number not 27% it was abnormally due to rain season during 2016 4th Q

Roy: Ok Thanks

Operator: I want to give a reminder to attendees for any questions just touch number 1 on your touch tones phone if you also want to ask any question to the presenters just press the Q and A on the internet interphase. We don't have any questions at this time. Mr. Tabares Do you have any closing remarks?

Mr. Tabares: Yes, thank we so appreciate again the attendance and I highlight that the 2016 results were very positive for the Group the 12% EBITDA growth and stating putting it at 3.81 US BILLION and that was a very positive result and achieved due to the efforts across the company including the resolution during the year the Guatape insurance claim the full and complete resolution of the claim during the year which was a significant accomplishment. Also, I highlight the 66% completion as which Lituango stated as of February and the increased certainty that we are gonna have the project delivered on time and on budget being the relevant release for the group I also highlighted with that I conclude the conference call and invite you to propose any other questions that you may post to our investor email and we will be happy to provide more information if you think more additional questions in the future Thank you.

Operator: Let's conclude today's conference call and you may now disconnect.