

EPM Group Conference Call Transcript- 4Q2019 Earnings Release

Operator: Good afternoon. My name is Anna and I will be your conference operator today. At this time, I would like to welcome everyone to the fourth quarter and full year 2019 consolidated financial results conference call - EPM Group.

All lines have been placed on mute to prevent background noise. After the speaker's remarks, there will be a question and answer session. Thank you for your attention.

Mr. Jorge Tabares, Executive Vice President of Finance and Investments of EPM Group, will be the host and speaker today. Mr. Tabares, you may begin your conference.

Jorge Tabares: Thanks Anna and welcome everyone. I appreciate your interest in participating in our conference call.

I'm going to go over the prepared slides that are published and then we'll go, as mentioned, to a Q&A.

After the agenda, I'll make a few remarks on what has happened recently. Then I'll go typically to the energy market, an update on Ituango, the financial results, the investment plan, and the liquidity and investments and financing strategy.

On page three I highlight which is a very unique feature of this group. The amount of infrastructure investments we made last year, 3.5 billion COP. This is a reference point. This is 3.5 billion COP to be divided by 4,000 to give you a US dollar amount, so this figure is equivalent to almost 900 million dollars, the 3.5 billion.

We transferred to the municipality last year 1.5 billion dollars in dividends or in transfers to the municipality and that represented 25% of the total revenue from all sources that the city had last year so we are very important to the city, which is the second city in the country.

In terms of asset sales, we undertook a very significant divestment program. Let me recall that this was defined back in July of 2018, when we had much more uncertainty on Ituango, and the fact that the Ituango situation evolved positively in terms of the damages were controlled, and that we did not have any major implication in terms of third-party damages. Of course, nobody has been hurt throughout this contingency, so at the end we did not have to sell the two major assets that we needed to. Because the contingency evolved favorably, we only had a real need to sell one of the assets. As I am going to say, we ended up deleveraging the company via a combination of actions that effectively more than compensated the need to sale the two big assets so we ended up selling 729,000 million COP, which is a fraction of what we originally thought we would need to sell, figuring the main objective all along was to deleverage the company, and I am going to give you the leverage position in a few minutes.

We maintained then about 8% of ISA. That's not for sale anymore. We had an authority to sell those shares until the end of 2019 and that expired, and we have people interested in acquiring Aguas de Antofagasta. That divestment is currently on hold. It is not required to deleverage the company, and it's now a matter of either a possible—I'm not saying a likely,

but a possible kind of portfolio. We're shuffling strategy. Or, if we let a few months, or more than a few months pass by, it could be a possibility if the Covid impact is too strong. So we retained the two biggest assets we had on sale in our portfolio.

Moving to page four, we entered this Covid situation with very recent rating, so back in March Moody's ratified our rating in their annual review. [no audio] 15, Fitch ratified also our ratings, so this is good because those were the annual reviews. In both cases, they incorporated the acquisition of CaribeMar, the north coast electricity distribution operation [inaudible] electricity distribution operation. They maintained the outlook and the main rationale is what should be happening in Ituango, which we're fairly confident about the control and the technical evolution, and the risks in the project. We have yet to persuade the rating agencies to improve their understanding of the situation in order to remove the ratings. I'm going to show you some stuff on the timeline.

I'm going to stop here, operator. The screen we are seeing looks like corrupted. It is not very clear. How can we check if everybody is seeing the same bad screen that we are seeing?

Ok, for those who are not watching a properly displayed presentation, I encourage you to download it from our website. It was sent on the link in one of the emails or the invite that you received. This is not a major issue because I'm explaining the stuff very clearly. Maybe when there is more information is more relevant, so I'm going to continue and we'll check if the technical issue could be resolved, so remain in page four for those of you who have the proper page opened.

We did have a change of major of the city starting on January 1st and one of the key decisions that the new major needs to make is the EPM board. The message here is a message of continuity. Five of the nine board members remained in the board, and he appointed three people besides himself, who is the chairman, which complement fairly well the rest and with very good experience that allow the composition of the board in terms of disciplines to remain intact. Jesus Aristizabal was a long-term EPM employee that retired a few years ago, and he's now back on the board. Then Luis Fernando Alvarez is a very prominent attorney in Colombia that was the head of one of the high courts a few years ago, and he brings a lot of expertise that is now very positive for us, as we are facing some legal issues associated with the Ituango contingency, and then Oswaldo Leon Gomez has very solid financial experience and is an entrepreneur, so he should be contributing significantly, so is a message of continuity and positive experience.

On page five, a little bit of detail. That page is displaying almost properly on the bottom part, not in the top part. The CEO, the incoming CEO, made some changes in the structure. This may be seen as a detail but I think it signals very important topics or focus areas for him. The first thing is that he created a Vice President of Strategy and Planning. He added the planning. Strategy was part of another vice presidency before. He created a brand new Risk Vice Presidency, recognizing the additional complexity that the business would have under this scope of the group. That was positively welcomed also. He created a general secretary to, again, reinforce the defense on all the legal issues that are happening to the company. And then he created this new Business, Innovation and Technology Executive Vice Presidency

that now includes technology that in our group before was part of the human talent, of the HR group.

And that's pretty much a focus area of his tenure, it's pointing to us becoming more digital and taking advantage of more digital businesses. So, again, very constructive changes to the structure of the company, and one that signals better planning, better risk management, and accelerated the technology agenda for the company.

Moving to page six, on the Ituango project there were—one event here that is a major event, which is associated with the environmental license. Since June 2018, the ANLA, which is the EPA in Colombia, issued resolution 820, and that had some requirements of information to ANLA. It precluded some activities that were not associated on the contingency. ANLA made it very clear in an official document that we could continue to finish the project as needed, in order to be able to dissipate the water in the reservoir. That's the risk left fast forward, and that recognition is something that is important for us in order to ensure that the project is not stopped by the environmental agency, and also it has embedded another message, which is by issuing this clarification, ANLA also recognizes that we are in full compliance of the major material elements of the environmental license. We have been operating throughout the contingency based on resolution 820, which incorporates extensive reporting to ANLA and visits by the ANLA team to the project, so we are in good shape in terms of the understanding of how we can move forward with the project and ANLA on March 2 of this year made it very clear to the open community.

The second point here on page seven is, as I mentioned, the acquisition of CaribeMar. CaribeMar is a house of the operation of the north of the country. These are the four states that are in green. This page is -- The technical problem remains but the broad messages could be read. Bolivar, Cesar, Cordoba and Sucre, the four states. This is above 1.5 million people, and a very unique opportunity for us, one that we are undertaking with a long-term view. All the modeling we run, all the technical plans we put in place, call for a multiyear, almost a decade effort moving forward to get this company to the level of all of other electricity distribution operations in the country or in other three countries in which we have the operation. So, with this, we will be operating in nine different states in Colombia. The current operation is about a quarter of the total market, and this adds 10% so with that we will be covering 19 million people in Colombia with electricity distribution.

We are very confident that our capabilities and long-term orientation will improve the lives of all these citizens that have suffered due to very deteriorated electricity distribution service. To give you an example, they have more than ten times the blackouts, the non-planned interruptions of service per year for our other operations, so the opportunity here is huge to improve the quality of life with this people there.

On page eight, it's the timeline of the transaction so we expect to take over this operation in around September. We signed the document at the end of March. I highlight that we signed this well within the Covid contingency, so in the purchase and sale agreement we have some provisions that cover us for extreme implications of Covid.

The government was the seller of this operation and they recognize that if there is a material negative impact from Covid, we will not be taking that risk. We will be compensated for that. And on the far right is the core of what we are planning to do, so we are going to invest very heavily. We have--Based on all the technical analysis, ours and external, there is a lot of work to be done on the investment side, so we are going to undertake those investments, and that should bring quality of service. We need to apply our standards to relationships with clients. Every study we run and every survey we did in the area called for a very significant distrust of the citizens with the company. This is not the case in the rest of our operations. In our operations, people trust us and they have a very high regard for how the company behaves as a corporate citizen, so we are just going to apply our DNA in that operation, and we think we can improve the relationships with customers, and the fact that we are going to invest very heavily is just translating [inaudible], the government, or the energy regulator set up a unique tariff regime for this whole operation, again, in recognition that the investments we are going to undertake are completely unprecedented, so the rates and the bills should be handled differently than in the rest of the country, so we are very happy.

Basically, the transaction was for a nominal amount. It's not a matter of acquiring an asset by paying money to the previous owner. It's mostly related to the commitment to invest and I'm going to give you more details on a minute.

We have got a lot of questions on page nine about the Covid impact. I'll qualify in three areas. One is maintaining operations, so we have very significant challenges ensuring that our people are safe and that the service continues. So far we have not had any disruption in our operation. Ituango had very, very minor impact for a few days, and then has continued or ramped up very, very quickly after we better set up the protocols to be able to operate under these conditions. So we have extensive protocols in place to make sure that people are properly taken care of and that the operation can continue and we ensure that to all the citizens.

In the Ituango case, I will point that, perhaps not being very fair with the project, is relatively easier because you can really isolate the place. We stop any non-essential visitor to the project, and even when we have a change of shift, in which typically people go back to their towns, and some towns may be far away from the project place, they decided to stay in the project, they feel safer in the project, so what that means is that we have less possibility of contagion, because less people is going in and out of the project. So the fact that the project is relatively isolated is easier. That's the impact on the operation.

So the second impact--We had at some point 4,200 people working from home, the technology worked out very nicely, we all learned how to work under these conditions. As of this week, some people again, only the essential people, started coming to the office. I'm currently speaking from the office, but the office probably had about 5% of the total population and we have around 300 people here or less. Only by exception people come here and given the importance of this call we decided to make sure that technology was—the company's technology and not our home technology.

The second impact was a reduction in consumption, so energy consumption in Colombia for the peak months of April reduced by about 15%. Our demand did not reduce by that amount because the first capacity that comes out is the expensive capacity in our thermal plants, so our impact is lower than that. And then gas, which is a smaller business we have, overall, the demand was reduced by more, by about 25%. As of last week, the country started reopening the economy, and yesterday it was announced that initially there were two sectors, the construction and the manufacturing, and now there are like 48 different sectors that are going to get back to work next Monday. So you see activity and demand improvement.

And then the third, and perhaps the most uncertain impact, is our clients' ability to pay. Initially in April, I think it's dangerous to extrapolate what happened in April. We did see some reduction in energy. We saw a reduction in the collections of about 5% so we collected about 95% of what we collected the previous year. But it's premature to really assess how big that impact is going to be in most of our countries of operation, Colombia which is the biggest by far, and then Panama and Guatemala, the other one being El Salvador on the electricity distribution business, then we put plans in place to actually finance the clients, a recognition that family or personal economies are not too solid and when people are at home they don't get revenue, they don't get payments, so we put financing conditions in place. That means that it's going to require some working capital from us, and of course depending on how deep and how long the impact is, we're going to have bigger or less cash needs in order to accommodate for that reality, which is a weakened consumer. Not only the individuals, but also the medium or small companies, family companies, that do not have a lot of standing power for maintaining their payrolls and business going.

On page ten, this is the typical page that we have. I'll just point here that the most significant operations in which we are present had growth. Colombia had a very solid energy consumption, power consumption demand in 2019 of 4.1% increase. Panama always grows faster than the rest of Latam. It grew at 4.7 and then Guatemala had a solid 3% growth. We basically maintained our market share in Salvador, Guatemala and Panama. We reduced our market share in Colombia by about 2 percentage points. As you can see in the EPM graph on the bottom left, there was a reduction of 7.5% in our commercialization of energy. This is big clients, this is not the recurrent base business. And pretty much this is the least profitable part of the client base, so the results are quite positive as I'm going to show you and they do not reflect this 4.1% variation in the electricity commercialization in the country.

Overall, we sold 26,000 GWh during the year. That's 2% lower than the previous year again, but we lost the less profitable business. In this particular case, the main client is an oil company which runs auctions that are extremely competitive and do not add a lot of value.

On page 11, we have the behavior of the spot price. Most significantly, Colombia. Colombia had a great year last year, and the average spot price increased by 80% during the year. I can say that in 2020 we have seen the same behavior. Very dry conditions. Reservoirs are currently at about a 32% level, which is low for this period of the year. We sold altogether, we generated altogether 15,000 GWh, again lower than the previous year, but financially we more than compensated by the regular margin of the rest of the business and by the spot price

increase. We basically generate in Colombia. We have very minor generation capacity in Panama.

On page 12, this is an updated chart, one that is easier to read and what it looks like. So this is on April 30th, so we keep track of the areas in the project that we have already stabilized, and the areas that we have not been able to fully access, and the ones in the process of stabilization, and the ones that are inaccessible. So the black ones are inaccessible and are never going to be accessible. We do not need to access those. They were going to be always underwater, and they are underwater now.

The green is the areas that we have stabilized and repaired already, and I'll give you more detail in a minute. And the yellow ones are areas in process of stabilization. So basically, three major areas of process of stabilization.

The first one is the intakes five to eight so the yellow ones in the middle. That's the area which we call the south part of the cavern complexes. We have yet to fully identify what the damage is. The second piece is the powerhouse, some areas that have yet to be stabilized, the middle one, that big block there. And then the third one is the auxiliary system, the bottom tunnel that is yellow.

Having said that, we have not experienced any surprise, any movements, any cause of concern in all those yellow areas, not in the purple areas, for more than a year. This color coding corresponds to a final and full technical stabilization and solution, but it is not a cause of concern as we speak. And you can see that the phase one of the project, which are intakes one to four, you can see the numbers very little, basically below all of the project title. If you go down the O, you are going to see "one, two, three, four." That's phase one. 1.2 GW.

We have already contracted, and we have a very clear schedule and cost for that phase one, the first 1.2 GW. Where we have some uncertainties is the second phase of the project, the second 1.2 GW. Those are less impactful from the financial perspective because the project is never going to generate at full capacity for 12 months. Just a few peak months of hydrology is when the full project is going to be operating. So clear path to phase one, phase two, a little bit of uncertainty, but we have not observed in any of the underground complexes or intakes any signals of distress, any surprises, so we claim that the risk continues to be lower as we move forward.

Going to page 13-- We can see the page properly now. Thank you.

Adding a few notes on the dam and spillway. It's basically operational. We are monitoring it. We have two channels and we can handle the water from one to the other. The second area is the intake tunnels. Very importantly, we just finished filling the cavity between tunnels one and two. This was a major operation, one that required a lot of creativity and innovation from the engineering perspective because we have to pour concrete that was going to drop 70 meters into the cavity, so for those of you civil engineers, the segregation of concrete when you dump it from such height is something that is a huge technical challenge. Finding the right mix and the right concrete and cement was critical. We accomplished that. That's

checked. Very important because this cavity was big. 75 meters tall, 45 meters wide, and about 40 meters in the other direction, and it was in the intakes one and two, so very close to the reservoir. That's checked. And a very important de-risking activity in the project.

Then we will be between next quarter and the following, but mostly in terms of the plugging of the two tunnels, we will be plugging the next quarter and at the beginning of 3Q. We are almost done in the slope zone and rock mass stabilization at 89-90% in the work there, and finally in the powerhouse we think we will finalize the stabilization next quarter, so three or four months from now. And we will also finalize the removal of the equipment we had installed there. This is a major demolition activity because this equipment is very embedded in concrete. That's going to take a while, but this is a fairly straightforward exercise, if you will.

I'll highlight on the bottom of that page that we have a world-class monitoring system in the project. We have ramped up instrumentation more than tenfold. We have online monitoring of hundreds of areas in the project with multiple types of measurement points and instrumentation, so everything that is going on in the project has a lot of visibility and we take action very, very quickly. We have not observed any surprises that could cause any concern to us.

As I said initially, we got some slowdown in the project but now it's fully ramped up, so it was just a few weeks of kind of lower pace. We feel confident that using the protocols we have we will be able to continue the schedule of the project.

On page 14, basically not much new here in terms of the total cost of the project. As I said, we may have in that 15.268 of the total cost some pressure on phase two. That is going to be further out. It's not going to be something that is going to happen soon. This is money to be spent perhaps '22, '23. On the bottom, we have invested, since the contingency, 1.5 billion, so above 400 million dollars in the project, in the contingency.

And in terms of money to be paid because of the contingency, it's the table in the middle. As you can see, we have been relatively conservative in the estimates and the accrual that we have in our books, so about 120 million dollars overall, 509,000 million COP. From that, most of it has been identified and spent, except for the payment to the transmitter. This is a payment to ISA, who is building the four transmission lines. We know we're going to have to pay that number. It's going to be a monthly payment starting at the end of this year, so it's not an immediate cash flow pressure, which is the bigger number in the picture.

But most importantly, the affected care and compensation to the impacted people on one side, and then the contingency and the environmental sanctions. We were very initially conservative in assessing the biggest fine we could be imposed, and we could add in our books back in 2018. That has not materialized. We have had some minor fines for very non-material lack of compliance points. This is normal under the Colombian environmental law on such a major project, and one that suffered a very significant impact or contingency as we suffered.

So, we are confident that these numbers will not escalate and we keep fully committed to compensate the people we affected, the people who were directly impacted in their homes. We have been paying them all along and we plan to continue to do so but most of the people are back in their homes and back in their normal life. That's very important. And this happened only after the government estimated that it was safe for them to go back to their homes, which happened almost a year ago.

Moving to page 15, which is properly displayed also, the numbers for the year. Revenues went up by 12%. The costs were up by 5%, which allowed the Ebitda to grow by 17%, with 1.5 billion dollars of Ebitda. We're very proud of the growth because this reflects two things. One is the healthy business environment in which we operate. We have more clients, the consumption is growing, and because of our investment in infrastructure, the regulatory asset base increases, and we picked up a little bit of tariff also with a very virtuous circle that also is positive because we are setting up or deploying infrastructure that will allow us to provide a good quality service overtime for many years to come.

Then, on the bottom left we have the figures for the first quarter. The first quarter was positive also. 1.5 billion of Ebitda. This is 5% higher than the previous quarter of 2019, again, growing healthily. The margin was reduced from the 33.4 we ended up the year. That's because we are now selling some of the Ituango electricity that we had to—when the contingency happened, we had sold some electricity from Ituango, so we are selling that basically at low margin, so it weighted down on our total margin.

This is the higher Ebitda margin, 33.4 in five years. We maintained very strong discipline on expenditures and cost control, and that is being reflected in the figures.

Going to page 16, since the portfolio has been organic, we have not incorporated any acquisition, this is relatively stable. The international revenue increased from 32 to 36% so it increased a little bit from the previous year but the composition between Guatemala and Panama is relatively stable and when you look at the Ebitda, as we are going to see, you realize that the 8% revenue share of Chile becomes 23%, and that's because that operation is highly—Aguas de Antofagasta, one of the highest Ebitda margins in our portfolio.

I'll say from the Ebitda perspective about more than 85% of our Ebitda is stable and that's not the only 15% remaining. It's the one that has linkage to the hydrology and the spot prices of energy.

On page 17, very stable from previous times, just for the sake of time because I'm spending too much time and I want to allow time for questions.

On page 18, a very healthy portfolio. Adasa had a slight reduction in Ebitda. This is because of two non-recurring issues, one associated with the sea bringing more algae. It's called red tide and this is something that has only occurred once in the five years that we have had the company. It also happened that the winter in the desert was strong last year and that caused some damage to our operations. Again, this is relatively infrequent in the magnitude it

happened last year. So that's Adasa, which is one of the big balls—the size of the circle is the Ebitda size.

And then in Guatemala with Deca we managed to improve the variation of Ebitda so if you may recall last year the Ebitda decreased by around 10% due to a regulatory update, a tariff update with two cash-ins. We know are more efficient and on path to better profitability in Guatemala.

And then in Ticsa, which is a small business project [inaudible] and the construction business, and the construction business was impacted because of delay in projects, so that's why it decreased. Ensa, so Ensa in Panama improved its growth rate.

Page 19 is a key page to understand EPM and this is the one that confirms that basically all businesses are doing well. The cash businesses, the smallest business we have had a slight reduction in Ebitda. Distribution contributed big time. This is the most diversified business we have. And by the way, this is the same one we are entering to Electricaribe.

Look at the 10.5 CAGR of the last four years of our Ebitda. This is a very strong reflection of our business performance and the focus throughout the company is to maintain that growth and that discipline to continue growing.

Page 20. As I was pointing before, this is very important. Our net debt to Ebitda at the end of '19 was 3.1. This is what we were selling assets for, to deleverage the company. We didn't have to sell everything, and we managed to get to the level we wanted. We ended up the year with 2.3 billion COP, which is about 550 million dollars of cash at hand. Today we have 850 million dollars of cash in the bank and again, the asset base, which is [inaudible] assets infrastructure. The CAGR is at 6.3% over the last four years.

Finally, on the maturity profile not much changes here from what we have been reporting in the last couple of quarters. We have a very moderate profile over the next couple of years. This next year about a billion pesos, say 250 million dollars, again, based on a 1.5 billion Ebitda is very manageable. And by '22 – '23 increases, we should have Ituango generating cash for us. The average term of the maturity is 6.8 years. This is one year more than we had last year, and you see here the big green blocks in '27 and '29. '29 was the bond operation we issued in July of 2019 and part of the 2027 was a [inaudible] we did also.

Here on page 22 I just have a detail on—Colombia had a significant depreciation of the currency. 25% this year. And what that meant is that that 3.5% debt to Ebitda became 3.8 without any significant increase on the actual debt disbursed. Just a re-expression of the debt.

And then on page 23, as I mentioned before, we are a very heavy investor. We are the biggest investor in Colombia in infrastructure. Period. And that's very significant for the employment and the economic impact of those investments. Last year we invested 3.2, from which about a third is Ituango. The rest of it is hardcore infrastructure assets for our operation. In the first quarter we have invested about 150 million dollars already in our portfolio, and we are coming down from a peak investment. From the previous four years, '16 to '19, we invested 13.9 billion COP and in next page, 24, is the investment profile, the Capex profile for the

next four years so the 13.9 becomes 10.4, which is very positive. And here we have estimated preliminary figures for CaribeMar and the next couple of years those investments account for about 12% of our total Capex, so the CaribeMar is a very moderate financial bet by the company. It nevertheless had a huge impact on the social benefits to these communities that have very poor-quality service.

Finally, on page 25, when we entered the Covid situation we had two credit lines, one with international banks and they disbursed on April 2nd, and we have a facility left by IDB Invest for 150 million dollars left to be disbursed. We are working with the IDB and lenders in order to see if we can have disbursed within 3Q 2020. We have this note that I made on resolution 820. Still have some issues pending there. Then we basically think we have all credit possibilities open. We plan not to tap on the local market. As we are too big for Colombia, we don't want to kind of crowd out other companies to generate lack of liquidity, so international funding is what we are preferring to at this time, much bigger markets and one that we think are going to price us very positively.

So that's what I have prepared. I'll now go back to operator to answer any questions.

Operator: At this time, I would like to remind everyone, in order to ask a question simply press * then 1 on your touchtone phone. If you'd like to withdraw your question, please press the # key. We'll pause for just a moment to compile the Q&A roster. At this time, we are going to require the questions first from the audio conference and then questions from the web.

Once again, as a reminder, if you would like to ask a question press * then 1 on your telephone keypad.

And I have no audio questions at this time. Do we have any web questions?

And there are no questions at this time. Mr. Tabares, do you have any closing remarks?

Jorge Tabares: No. We thank you the attendance. We remain open to any questions that may arise. We're more than happy to provide those answers. We have been asked by a few investors about how are we getting money, the payment of the invoices that we are sending to clients. I think it's premature because April, which was the approved confinement month, perhaps is not the best month to judge what may happen in the near future because it's not the full assessment of the economies of people and families and small companies cannot be assessed yet.

I'm very hopeful of the reactivation of the economy and Colombia from the death perspective of Covid is a very moderate country. The government took very early actions, very strong actions, and for that reason very manageable situation so far despite not having a very strong hospital and medical care unit system. So a lot of uncertainty. We are in the path of getting liquidity, making sure that we have cash in order to ensure that our operation can continue, and the clients are going to be well served. We are very vital to the economy and we just are going to have an extra little bit of liquidity just to be prepared for a longer isolation or the economy downturn.

Thank you very much and we remain open through our Investor Relations contact.

Operator: This concludes today's conference call. You may now disconnect.