

Conference Call Codensa and Emgesa FY2018

February 26, 2019

Operator: Welcome to the full year 2018 Emgesa and Codensa results conference call. My name is Sylvia and I will be your operator for today's call. At this time, all participants are in a listen-only mode.

Later, we will conduct a question and answer session. During the question and answer session, if you have a question please press * and then 1 on your touch tone phone. Please note that this conference is being recorded.

I will now turn the call over to Michele Di Murro. Mr. Di Murro, you may begin.

Michele Di Murro: Yes. Thank you, Sylvia. Good morning and thank you everybody for joining us today in our investor conference call. As Sylvia said, my name is Michele di Murro and I am the Chief Financial Officer of the company. Today I will present you the financial operating results for 2018.

As always, at the end of this presentation we will have a Q&A session where all the questions will be possible either in English or Spanish and will be answered by any of our team members that are currently available for this meeting here with me. You will also be able to download this presentation from our website.

I will start and we can move to slide number 2, where we have the highlights of the period. We can start from the first one, where we can see our Enel group companies in Colombia reached positive results over 2018, supported mainly by a successful commercial strategy on the generation business.

Emgesa and Codensa generated a total net income of COP \$1.6 trillion, equivalent to around 8% increase compared to last year, 2017.

In the next slide, we will see the drivers that have allowed these results. Let me also highlight that during 2018 Emgesa has achieved to overcome COP \$1.3 trillion net income, becoming the largest generation company in Colombia by net installed capacity.

Moving to the second point, total Capex for the companies reached COP \$1.2 trillion, showing a 14% increase during 2018. More than 70% of these investments were executed in the distribution business, supporting the strategic plan that seeks to improve quality of service, for example through the implementation of "telecontrol", while allowing the expansion of over 50 networks through new connections.

Furthermore, in order to take advantage of the positioning and awareness of the Enel brand worldwide, the companies underwent a rebranding process, evolving from Emgesa and Codensa to Enel-Emgesa and Enel-Codensa.

Finally, moving to the fourth point, we highlight the strong and reliable operation of the companies. This is reflected in the confirmation of the highest possible credit rating in Colombia, while Emgesa keeps maintaining its international rating.

Let's move to slide number three, to a regulation update. As you know, the electric regulatory agenda in 2018 was marked by the Hidroituango emergency. As you know, this led the government and regulators to issue documents to ensure energy supply in Colombia for the upcoming years, with for example the "subasta" that will take place in two days.

In this sense, we have highlighted three important regulatory updates. First of all, the resolutions regarding the first long-term auction which is taking place today. This is in order to encourage the contraction of non-conventional renewable generation projects. At the auction, traders and generators will participate for bilateral contracts for 12 years. Results will come out in this auction.

Secondly, the second important regulation this year, is the resolution regarding the reliability charge auction, which was mentioned before. This is in order to ensure energy supply for the 2022-2023 period, according to the deficit that could be registered without Hidroituango. The auction will take place next Thursday February 28th.

If we move to the distribution business, during 2018 the most important item was the publication of the final remuneration methodology and WACC for the next five years. Let me also highlight that the WACC was reviewed last week in accordance with the budget that was approved last December.

Currently, the regulator is in process of evaluation and approval of the tariff of the distribution companies. Codensa was the first one to give this tariff to distribution and we expect the new methodology to take effect starting from May 2019.

It's important to highlight that this new regulatory framework will completely change the value creation drivers of Codensa and of the distribution business in general in Colombia.

As you probably know, network investments will be remunerated with a regulated WACC, the one I was mentioning before, plus incentives based mostly on improvements in quality.

We can then move to highlight our operating results in slide number four. Here we have on the upper part of the slide generation and at the bottom the distribution business.

Starting from the generation business, we can see our net installed capacity at the end of 2018 reached 3.5 GW, presenting an increase of 1% compared to December 2017. This is explained by the increase in the capacity of the Tequendama plant to 57 MW. Therefore, after this currently Emgesa is the largest generation company in terms of installed capacity in Colombia.

We can see in production how we registered a reduction in the company's generation. This is due to the strategy considering the upcoming El Niño phenomenon that is going on right now. At the same time, during 2018 we decided to increase energy purchases, taking advantage of a low crisis scenario. In this direction, hydrogeneration was reduced by around 6% year-over-year, while thermal generation

increased by 68%. This was explained mainly by higher restrictions in the Caribbean region, which implied higher generation of Termocartagena and also higher generation of Termozipa during the last months of the year. These were the first effects of El Niño phenomenon starting to appear.

Moving to the distribution business, energy distributed by Colombia during 2018 reached 14.9 TW/h, growing 1.2% in annual terms. This can be explained by a 1.7% increase in regulated demand, driven by residential and commercial segment consumption.

It is important to remark that also demand through tolls have increased 0.6%, growing for the first time in the last two years.

Finally, currently Codensa holds a 21.5% market share in the country, positioning the company as the second largest distributor at the end of 2018.

Total customers of Codensa reached 3.4 million, showing a 3% growth in the year, equivalent to almost 100,000 new connections this year.

We can now move to slide number five to see how these operating results translated into finances. Here we start from Emgesa, where as you can see, gross margin has reached COP \$2.3 trillion during 2018, increasing more than 2% compared to last year. This result is explained by a 9% growth on operating revenues and this is due to an increase in energy prices on long-term contracts with non-regulated clients, mainly due to the PPI indexation, and a higher volume of sales in the stock market, compensated in margin by higher purchases due to the strategy of low generation previously explained.

In the same way, reported Ebitda increased 2.4% in annual terms, driven by the positive results in gross margin and a reduction of 2% on fixed costs. This has been mainly due to the elimination of the wealth tax in 2018 in comparison with 2017.

If we move to the bottom of the slide, as you can see, the net income increase is much higher, reaching a 15% growth. This was due to a reduction in financial expenses due to lower debt and a better cost of debt due to lower CPI levels, an indicator to which 68% of the debt is indexed, but we will discuss this afterwards when we talk about financial expenses.

Also, as you know, there was a lower tax rate compared to the previous year, following the tax reform of 2016 and a positive one-off effect on deferred taxes coming from the recent budget law that will reduce the tax rate by 30% in 2022.

Finally, as you can see, net debt decreased relevantly by around 15% to COP \$2.9 trillion, as cash from operations was more than sufficient to fully cover investments and dividends, leaving further cash to reduce debt.

This is a snapshot of Emgesa. Let us now move to slide six to see what happened in Codensa. As you can see, gross margin in Codensa rose 1.6% in the year and this was thanks to a growth in energy demand in our operation and an increase in the regulated business tariff due to the indexation to PPI and CPI, so these are the drivers that moved gross margin this year. As I told you before, in 2018 the key drivers

of the distribution business changed, for example, will not be more exposed to demand and will be a regulatory framework that will be based on a remuneration of investments, considering the investments that we will put in place, and that was recognized on these investments.

Getting back to the results of 2018, these positive impacts explained, have been offset by a one-off effect due to the pass through mechanism of generation costs in the tariff.

These costs are included in the tariff with a two-month delay involving a temporary impact on margins in case of increase in energy purchases cost.

This is exactly what happened in 2018, due to contracts loss during the last El Niño phenomenon, which resulted in higher energy costs in the year, reflected in the tariff with a two-month delay, implying a negative one-off effect of around COP \$50 billion in margin. This has impacted our results this year. If in the next years, the prices will go back to the level of the beginning of 2018, obviously we will have a positive one-off effect of COP \$50 billion.

Moving to business costs, they increased by 5.9% mainly due to an increase in personnel costs associated to higher costs for the execution of new projects and the tapping of the new Enel business line.

The second point that impacted fixed costs was the launch of a crash energy losses program that allows the company to reduce losses by the end of the year. In this case, we have been able to reduce losses from 7.84% to 7.74%.

As a result of the above, reported Ebitda reached a total of COP \$1.6 trillion in the period, with a slight increase from 2017. However, net income decreased by 2.4%, despite the positive Ebitda performance due to three main effects: an increase in depreciation after the relevant Capex executed during the last two years, the resulting increase in net financial expenses due to the higher debt needed to fund this investment plan, and a one-off effect considering the accounting change of the Rionegro generation plant, which is now for sale, affecting provisions during the year.

It is important to highlight that without the one-off effect explained before, net income would have increased by around 5% over the analyzed period, showing a continuous industrial growth of the company during the year.

Finally, moving to net debt, net debt in Codensa increased by 24% compared to December 2017, explained mainly by higher Capex and dividends paid.

Let's now move to slide number seven, where we have a simple summary of the results explained before in terms of profit loss with an overall view for the accounts in Colombia.

Ebitda increased 1.6%, supported by the performance of the generation business, which increased in Codensa for the reasons explained before.

As we will better see afterwards, financial expenses decreased by 9%, while for taxes, as already said, the reduction is given by the nominal tax reduction in 2018 and the positive one-off effect due to the improvement of the deferred taxes coming from the recent budget law.

After all of this, net income in Colombia reached COP \$1.63 trillion during 2018, growing almost 8% compared to the previous year.

Let me remark that without the negative one-off effect explained before, group net income would have increased by more than 10%.

We can now move to slide number eight, to take a look at our cash flow generation. We start here again with Emgesa, where we can see how our company keeps maintaining a very positive cash flow generation profile.

- The Ebitda reached COP \$2 trillion
- Net working capital improved by almost COP \$200 billion thanks to our continuous efforts in improving our cash conversion cycle
- As a result, funds from operation reached COP \$1.4 trillion, fully covering gross Capex, that amounted to more than COP \$300 billion, out of which around 50% was aimed at growth projects such as the extension project from Terkozipa.

Finally, after dividend payment, net free cash flow was positive by COP \$530 billion, supporting the net debt reduction already described.

Moving to Codensa, on slide number nine, we can see how the situation in terms of net free cash flow is different, but if we focus on operative cash flow, we see how our operative cash flow generation remains strong, overcoming COP \$1 trillion, but with a very relevant Capex plan reaching a new record of COP \$55 billion.

As already said, the company had an important investment plan for the improvement of quarter indicators and modernization of the network, which was reflected in better quality and profit indicators at the end of 2017, already moving up in a good position towards the new regulatory period that will start this year.

In conclusion, after payment of dividends, net cash flow showed a negative result of COP \$260 billion, involving a net debt increase at the end of the year.

Moving to slide number ten, we can review our overall debt position, once again, in generation and distribution.

As of December 31st of 2018, Emgesa's gross debt amounted to COP \$3.7 trillion, decreasing by 9% compared to December 2017.

Throughout 2018, Emgesa paid several financial obligations with cash on hand as follows:

- COP \$100 billion for a bank loan maturity in February
- COP \$218 billion for a bond maturity in July, and
- COP \$94 billion related to bank loan amortization.

The average cost of debt in Emgesa has decreased from 8.4% to 7.9% in 2018, mainly explained by lower CPI levels.

As of December 2018, 68% of the company's outstanding debt was indexed to CPI and 4% to the inter-bank rate.

As for the distribution business, Codensa's gross debt reached COP \$2.1 trillion at the end of 2018, with a 19% increase compared to December 17, as we already explained before.

As already communicated in April, the company issued a bond in the local market for COP \$360 billion with the following conditions:

- a 7-year of 6.74% and
- a 12-year tenor at the CPI plus 3.59% coupon with a 3.3 times over subscription.

While in October we issued the five-year tenor local bond for COP \$195 billion at CPI plus 2.8%, getting a 1.7 times over subscription.

Thanks to this, Codensa's cost of debt in the period decreased from 8.2% to 7.4%.

In Codensa, as of December 2018, 34% of the debt was indexed to CPI, and 2% to DTF (deposits rates).

Please also note that all of our debt is in Colombian pesos, considering that the company's margin leaves to almost no exposure to foreign companies and therefore our decision has always been to finance all our debt in Colombian pesos.

Total liquidity available reached COP \$6.3 trillion, including cash financing committed and non-committed credit lines with local and international banks.

Before moving to the last slide and closing remarks, let me highlight that the numbers presented in this slide are a further proof of the recognized financial solidity business.

Moving to slide 11 and closing remarks, we can say that as you've seen, the operation for Enel group in Colombia has shown positive results in 2018 both in P&L and cash flow, with generation business showing exceptional results thanks to an effective commercial strategy together with an important reduction in net financial expenses.

The distribution business reported a decrease in net income, but without the one-off effect explained, Codensa would report a 5% growth as well. It is also worth highlighting that the group has executed an aggregated Capex of COP \$1.2 trillion, focused on the distribution business, especially on the improvement of quality of service, modernization of our network, and new connections.

Basically, this is our presentation for today. Thank you very much for your attention and do not hesitate to contact me or the Investor Relation team at any time if you need any further information.

We will now open the Q&A session. We have here some representatives from various areas from the company, from regulation and finances as well, that will support me in this Q&A session. The transcript of the conference will be available in our webpages in the following days.

Operator: Thank you. We will now begin the question and answer session. If you have any question, please press * and then 1 on your touch-tone phone. If you wish to be removed from the queue, please press the # key. If you are using a speaker phone, you may need to pick up the handset first before pressing the numbers.

Once again, if you have any question, please press * and then 1 on your touch-tone phone.

The first question comes from Diego Buitrago, from Bancolombia.

Diego Buitrago: Good morning, thank you for the presentation. Could you please tell us if Emgesa is going to participate in the auctions that will be held this week? Thank you.

Michele Di Murro: Yes. Let me answer this question in this way. As you probably know, today we have this long-term energy auction and we will participate not only with Emgesa but also with Codensa as buyers. We will buy obviously only on conditions that we consider convenient.

Emgesa will obviously also participate in the capacity payment tender of next Thursday with all the existing plants that will be set in the capacity payment tender will be applied to all the existing plants starting from 2022-2023, so obviously, we are very pending and we keep monitoring this important event that we consider very important for the long-term development of the sector in the generation business.

Diego Buitrago: Thank you.

Operator: Once again, if you have any question, please press * and then 1 on your touch-tone phone. At this time, we have no further questions.

Michele Di Murro: Ok, so if there are no further questions, we thank you for your attention and we underline again that we will be available for any questions directly to me or to our Investor Relation team. Thank you everybody and have a good day.

Operator: Thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating. You may now disconnect.