

Transmissao Paulista (CTEEP PN)

1Q07 Results Slightly Above Expectations Even When Excluding Non-Recurring Gains; Reiterate OW on Margin Expansion Upside - ALERT

Overweight

R\$27.46

20 April 2007

Sao Paulo-based, pure transmission utility CTREP reported strong 1Q07 net and operating results, even when adjusting for non-recurring gains that have been previously guided by the company in February. We reiterate our OW rating, based on inexpensive 2007/08E valuation (5.9-5.3x EV/EBITDA and 9.5-9.0x P/E, with ~10% yield) and expected operating and financial turnaround.

Emerging Markets Equity Research

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- **1Q07 EBITDA was R\$215 million, and still strong at R\$187 million when adjusted by a R\$28 million gain regarding the reversal of provisions regarding an out-of-court settlement with Eletropaulo on a property dispute.** Adjusted EBITDA was slightly above our R\$177 million estimate (consensus estimates were not available), mainly due to lower than expected personnel expenses, partly on the back of the company's 4Q06 voluntary dismissal program (PDV).
- **Net income of R\$227 million (R\$1.52/1,000 or US\$0.74/1,000) compared positively vs. our R\$136 million estimate.** Strong net income was mainly due to a R\$108 million after-tax gain on the Eletropaulo-CTEEP settlement on the property dispute mentioned above, booked as follows: (a) R\$55 million in financial gains (from the revaluation of the building value; and; (b) R\$70 million in non-operating gain due to reversal of provision for losses. Excluding this non-recurring gain, net income was R\$119 million (vs. our estimate of normalized net income of R\$103 million).
- **Capex in 1Q07 was R\$209 million** vs. total 2007E capex budget of R\$436 million. The relatively high capex this quarter implies, in our view, that CTREP will leverage its balance sheet for growth capex as opposed to higher dividends (we expect dividends at up to 95% of earnings).
- **Status of legal disputes remains unchanged.** As per CTREP earnings release, the disputes against (a) Eletropaulo (regarding who owns an estimated ~R\$882 million debt to Eletrobras) and (b) the Sao Paulo State Government (related to who has to pay an estimated R\$114 million in pension fund expenses regarding Law #4,618, from Sep. 2005 to Mar. 2007) remain unresolved: (a) Eletrobras continues to request the payment of the debt from Eletropaulo and Eletropaulo continues to argue Eletrobras should charge CTREP instead; and, (b) CTREP continues to

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pay part of the pension expenses (~R\$80 million/year) while it argues in the courts that the full liability belongs to the State.

- Please see Table 1 for details on 1Q07 and 1Q06 results.

Table 1: 1Q07 & 1Q06 Summary Results

R\$ millions unless otherwise specified

INCOME STATEMENT	1Q07	1Q06	Chg	Comments on 1Q07
Net Revenues	336	297	13%	slightly above our R\$327 MM estimate
Personnel	(59)	(80)	-27%	below expectations; meaning margin expansion upside from voluntary dismissal program
Material + 3rd Parties	(27)	(32)	-15%	slightly below expectations
Regulatory Charges	(33)	(19)	77%	as expected
Provisions	12	(10)	n.m.	includes R\$28 MM of net reversal of provision (out-of-court settlement with former sister Eletropaulo)
Depreciation	(43)	(42)	1%	
Other	(15)	(11)	33%	
Operating Profit (EBIT)	172	103	67%	
<i>Operating Margin</i>	<i>51.1%</i>	<i>34.6%</i>		
EBITDA, reported	215	145	48%	R\$187MM when adjusted for net reversal of provision; above our R\$177 MM estimate
<i>EBITDA Margin</i>	<i>63.8%</i>	<i>48.8%</i>		
Net Financial Result	68	26	158%	includes R\$55MM gains in asset revaluation from out-of-court agreement with Eletropaulo
Interest on Capital	0	0	n.m.	
Non-Operating Results	81	(0)	n.m.	includes R\$70 million in reversal of provisions from out-of-court agreement with Eletropaulo
EBT	322	129	149%	
Income Tax	(94)	(46)	104%	30% effective tax rate
Reversal of Int. on Cap.	0	0	n.m.	
Net Income	227	83	175%	above our R\$136 MM estimate (consensus estimates not available)
EPS (R\$/1,000)	1.52	0.55	175%	
EPS (US\$/1,000)	0.74	0.26	189%	
BALANCE SHEET	1Q07	1Q06	Chg	Comments on 1Q07
Total Assets	4,917	4,919	0%	
Shareholder's Equity	3,973	3,910	2%	
Net Debt	30	(249)	n.m.	includes pension fund debt
RATIOS	1Q07	1Q06		Comments on 1Q07
ROA, annualized	18.5%	6.7%		
ROE, annualized	22.9%	8.5%		
Current Ratio	1.8	2.7		
Interest Coverage	n.m.	n.m.		net cash position
Net Debt / Equity	0.7%	n.m.		we expect higher leverage with new controlling shareholder and 95% earnings payout
Net Debt/EBITDA	0.0	n.m.		net cash position

Source: Company; JPMorgan.

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CTEEP ON (TRPL3.SA) Price Chart



Date	Rating	Share Price (R\$)	Price Target (R\$)
08-Feb-06	N	31.39	-
13-Jun-06	UW	22.90	-

Source: Reuters and JPMorgan; price data adjusted for stock splits and dividends. Initiated coverage Feb 08, 2006. This chart shows JPMorgan's continuing coverage of this stock; the current analyst may or may not have covered it over the entire period. JPMorgan ratings: OW = Overweight, N = Neutral, UW = Underweight.

CTEEP PN (TRPL4.SA) Price Chart



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