

COMPANY UPDATE

Sabesp (SBSP3.SA)

Buy

Equity Research

Assessing Arsesp technical note w/ preliminary tariff review figures

What's changed

On August 11, regulator Arsesp opened the Public Hearing #1/2017 to discuss the second tariff revision process and also disclosed the technical note with a proposed preliminary tariff increase of 4.365% vs. our 8.30% (real terms). Main highlights include (1) an initial net regulatory asset base (net RAB) of R\$40.3bn vs. our R\$42.5bn, (2) a regulatory WACC of 8.01% vs. our 8.26% (in real terms, after tax), and (3) a P0 (initial tariff) of R\$3.63/m³ vs. our R\$3.76/m³. These figures will be discussed in the Public hearing until September 4, with the final figures in this first stage scheduled to be published by October 3.

Implications

We have a negative assessment of the proposed preliminary tariff increase. Should these preliminary figures be confirmed, we estimate a negative impact of R\$2.2/sh for SBS' equity value (or -4.7%). Nevertheless, we have exercised a hypothetical scenario which considers (1) the revisiting of the calculation of the Beta for the regulatory WACC (based on the methodology used for Copasa's tariff review process), and (2) a higher net RAB, should the regulator incorporate the full value of the company's audited PP&E (vs. 48.85% included in the preliminary technical note). While we don't take a view on the likelihood of potential changes in the public hearing process and acknowledge a range of outcomes outside our analysis, our exercise implies a 7.06% tariff increase under both a higher WACC and RAB (details on pages 6-7). We maintain our Buy rating on Sabesp and our 12-month, DCF-based price targets of R\$44.0 (SBSP3.SA) and \$13.2/ADR (SBS).

Valuation

Sabesp currently trades at normalized EV/EBITDA and P/E multiples of 4.7x and 5.7x, implying a 27% discount vs. our Brazilian utilities coverage.

Key risks

(1) lower-than-expected water and sewage volumes in 2017-18; (2) worse final tariff review figures vs. our assumptions.

INVESTMENT LIST MEMBERSHIP

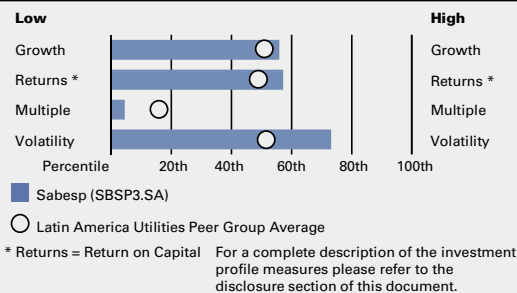
Americas Buy List

Coverage View: Attractive

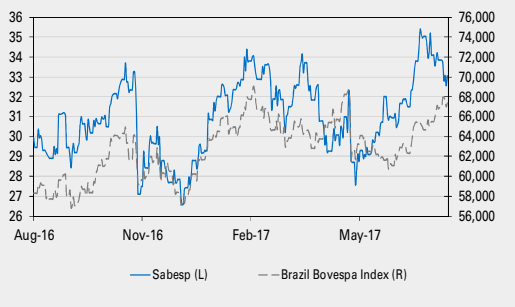
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Investment Profile

Key data	Current			
Price (R\$)	33.05			
12 month price target (R\$)	44.00			
SBS Price (\$)	10.41			
SBS 12 month price target (\$)	13.20			
Market cap (R\$ mn)	22,590.0			
Dividend yield (%)	3.2			
Net margin (%)	25.8			
Debt/total capital (%)	44.7			
	12/16	12/17E	12/18E	12/19E
EPS (R\$)	4.31	4.66	5.76	6.24
SBS EPS (R\$)	4.31	4.66	5.76	6.24
P/E (X)	6.2	7.1	5.7	5.3
SBS P/E (X)	6.2	7.1	5.7	5.3
	3/17	6/17E	9/17E	12/17E
EPS (R\$)	0.99	0.99	1.16	1.57
SBS EPS (R\$)	0.99	0.99	1.16	1.57

Price performance chart

Share price performance (%)	3 month	6 month	12 month
Absolute	10.4	0.6	10.4
Rel. to Brazil Bovespa Index	10.6	(1.3)	(4.5)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 8/11/2017 close.

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Sabesp: Summary Financials

Profit model (R\$ mn)	12/16	12/17E	12/18E	12/19E	Balance sheet (R\$ mn)	12/16	12/17E	12/18E	12/19E
Total revenue	10,365.3	12,350.9	13,889.7	14,806.2	Cash & equivalents	1,886.2	1,224.8	3,793.3	5,854.1
Cost of goods sold	(7,115.8)	(7,505.0)	(7,934.8)	(8,483.3)	Accounts receivable	1,557.5	1,888.1	2,309.5	2,459.2
SG&A	0.0	0.0	0.0	0.0	Inventory	58.0	77.0	86.3	95.2
R&D	0.0	0.0	0.0	0.0	Other current assets	321.9	578.2	634.6	675.6
Other operating profit/(expense)	0.0	0.0	0.0	0.0	Total current assets	3,823.6	3,768.2	6,823.7	9,084.1
ESO expense	0.0	0.0	0.0	0.0	Net PP&E	22,393.2	25,120.9	27,802.1	30,132.2
EBITDA	4,372.7	6,127.0	7,438.2	8,044.3	Net intangibles	0.0	0.0	0.0	0.0
Depreciation & amortization	(1,123.2)	(1,281.0)	(1,483.3)	(1,721.3)	Total investments	0.0	0.0	0.0	0.0
EBIT	3,249.5	4,845.9	5,954.9	6,322.9	Other long-term assets	10,528.2	9,348.5	8,678.8	8,250.3
Net interest income/(expense)	(270.1)	(271.4)	(247.8)	(125.6)	Total assets	36,745.0	38,237.5	43,304.6	47,466.6
Income/(loss) from associates	0.0	0.0	0.0	0.0	Accounts payable	772.0	773.6	816.0	855.3
Others	326.2	(996.4)	(1,373.6)	(1,387.2)	Short-term debt	1,246.6	1,392.1	2,602.6	2,659.5
Pretax profits	3,305.6	3,578.1	4,333.5	4,810.2	Other current liabilities	2,283.9	2,298.5	2,630.5	3,744.8
Provision for taxes	(1,182.0)	(1,249.3)	(1,504.3)	(1,666.4)	Total current liabilities	4,302.5	4,464.2	6,049.1	7,259.5
Minority interest	0.0	0.0	0.0	0.0	Long-term debt	13,982.8	12,964.9	13,597.0	14,401.7
Net income pre-preferred dividends	2,123.6	2,328.8	2,829.2	3,143.8	Other long-term liabilities	3,040.5	3,060.4	3,081.2	3,103.0
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	17,023.3	16,025.3	16,678.2	17,504.7
Net income (pre-exceptionals)	2,123.6	2,328.8	2,829.2	3,143.8	Total liabilities	21,325.8	20,489.5	22,727.4	24,764.2
Post tax exceptionals	823.5	855.8	1,104.6	1,124.3	Preferred shares	0.0	0.0	0.0	0.0
Net income (post-exceptionals)	2,947.1	3,184.6	3,933.8	4,268.1	Total common equity	15,419.2	17,748.0	20,577.2	22,702.4
EPS (basic, pre-exception) (R\$)	3.11	3.41	4.14	4.60	Minority interest	0.0	0.0	0.0	0.0
EPS (diluted, pre-exception) (R\$)	3.11	3.41	4.14	4.60	Total liabilities & equity	36,745.0	38,237.5	43,304.6	47,466.6
EPS (basic, post-exception) (R\$)	4.31	4.66	5.76	6.24	Additional financials	12/16	12/17E	12/18E	12/19E
EPS (diluted, post-exception) (R\$)	4.31	4.66	5.76	6.24	Net debt/equity (%)	86.5	74.0	60.3	49.4
Common dividends paid	(700.0)	(727.4)	(938.9)	(1,974.3)	Interest cover (X)	4.5	6.6	7.5	7.1
DPS (R\$)	1.02	1.06	1.37	2.89	Inventory days	3.1	3.3	3.8	3.9
Dividend payout ratio (%)	33.0	31.2	33.2	62.8	Receivable days	50.8	50.9	55.2	58.8
Growth & margins (%)	12/16	12/17E	12/18E	12/19E	BVPS (R\$)	22.56	25.97	30.11	33.21
Sales growth	23.8	19.2	12.5	6.6	ROA (%)	6.0	6.2	6.9	6.9
EBITDA growth	40.6	40.1	21.4	8.1	CROCI (%)	14.4	14.5	15.3	15.1
EBIT growth	59.6	49.1	22.9	6.2	Dupont ROE (%)	13.8	13.1	13.7	13.8
Net income (pre-exception) growth	449.6	9.7	21.5	11.1	Margin (%)	20.5	18.9	20.4	21.2
EPS growth	449.6	9.7	21.5	11.1	Turnover (X)	0.3	0.3	0.3	0.3
Gross margin	31.4	39.2	42.9	42.7	Leverage (X)	2.4	2.2	2.1	2.1
EBITDA margin	42.2	49.6	53.6	54.3	Free cash flow per share (R\$)	2.19	1.37	2.33	3.36
EBIT margin	31.4	39.2	42.9	42.7	Free cash flow yield (%)	8.1	4.1	7.0	10.2
Cash flow statement (R\$ mn)	12/16	12/17E	12/18E	12/19E					
Net income	2,947.1	3,184.6	3,933.8	4,268.1					
D&A add-back (incl. ESO)	1,123.2	1,281.0	1,483.3	1,721.3					
Minority interest add-back	0.0	0.0	0.0	0.0					
Net (inc)/dec working capital	143.0	(745.5)	(361.5)	(84.4)					
Other operating cash flow	0.0	0.0	0.0	0.0					
Cash flow from operations	4,213.3	3,720.1	5,055.5	5,905.0					
Capital expenditures	(2,714.5)	(2,784.1)	(3,463.5)	(3,608.2)					
Acquisitions	0.0	0.0	0.0	0.0					
Divestitures	0.0	0.0	0.0	0.0					
Others	(1,667.7)	(4.2)	(4.4)	(4.6)					
Cash flow from investing	(4,382.1)	(2,788.3)	(3,467.9)	(3,612.8)					
Dividends paid (common & pref)	(127.4)	(700.0)	(855.8)	(1,104.6)					
Inc/(dec) in debt	543.3	(893.2)	1,836.5	873.1					
Other financing cash flows	0.0	0.0	0.0	0.0					
Cash flow from financing	415.8	(1,593.2)	980.8	(231.5)					
Total cash flow	247.0	(661.4)	2,568.5	2,060.7					

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

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Assessing Arsesp's technical note with preliminary tariff review figures

We outline below the main preliminary parameters proposed by regulator Arsesp for the second tariff revision process for Sabesp for which the first stage is scheduled to conclude by October 3 and the final stage by April 10, 2018.

1. **Regulatory Asset Base (RAB):** The regulator Arsesp proposed a preliminary R\$40.3bn net RAB for Sabesp, which compares to our R\$42.5bn. It is important to highlight that the regulator acknowledges room to revisit these figures as, according to the technical note, there was a R\$3.2bn difference in the appraisal report that calculated the replacement cost of Sabesp's regulatory asset base and the company's audited net PP&E (Property, Plant and Equipment, or its net fixed assets). The regulator included 48.85% of this difference in the preliminary proposal.

Should Arsesp assume 100%, the net regulatory asset base would have come to R\$42.0bn (in line with our R\$42.5bn).

2. **Preliminary consideration of the assets that were not incorporated in the first tariff revision cycle:** Arsesp revisited the original Sabesp's claim about the assets that were not incorporated into the first cycle regulatory asset base and the regulator proposed a R\$1,047.2mn increase, as per the table below.

Exhibit 1: Regulator Arsesp proposed additional values on assets that were not included in the first tariff cycle
R\$ thousand

Revision of the Replacement Cost (VNR) for the 1st cycle pipelines (at September 2011 prices)	Sabesp's claims (R\$*000)	Arsesp's technical note #004/2014 (R\$*000) (I)	Revised values (R\$*000) (II)	Delta (R\$*000) (III) - (I)
Factory value (VF)	6,534,547	5,554,365	6,534,547	980,182
Additional equipment (EA)	233,937	166,631	196,036	29,405
Additional costs (CA)	26,645,495	16,939,491	16,939,491	0
Financial remuneration for work in progress (JOA)	1,553,817	845,236	882,894	37,658
Recalculated Replacement cost (VNR) - 1st cycle	34,967,796	23,505,723	24,552,968	1,047,245

Source: Arsesp, Goldman Sachs Global Investment Research.

3. **Regulatory WACC:** Arsesp proposed a regulatory WACC (in real terms and after tax) of 8.01% vs. our 8.26%, the 8.06% witnessed in the first tariff revision cycle (concluded in 2014) and 7.94% / 8.62% for sanitation peers Copasa and Sanepar, respectively. Main difference vs. our regulatory WACC assumption was the proposed Beta used in the WACC calculation of 0.76x vs. 0.78x for Sanepar and 0.88x for Copasa. As per Arsesp's technical note, the calculation of the unlevered Beta for Sabesp was based on US sanitation peers, and then leveraging for Sabesp's capital structure.

Should the Beta be calculated by using Sabesp's weekly returns vs the IBOVESPA index (methodology used for Copasa's tariff review process), we estimate a Beta of 0.862x, implying a regulatory WACC of 8.40% (Exhibit 2).

Exhibit 2: Regulatory WACC for Sabesp

Proposed WACC vs. our estimate, the first cycle WACC and the ones approved for Copasa and Sanepar

Regulatory WACC - Sabesp						
Tariff revision	1st cycle	2nd cycle		Comparables		Scenario
		GSe	Preliminary	Copasa	Sanepar	Adj Beta
Capital Structure						
Equity	53.0%	53.0%	58.8%	67.3%	51.3%	58.8%
Debt	47.0%	47.0%	41.2%	32.7%	48.7%	41.2%
Cost of equity (nominal)						
	14.4%	14.4%	12.5%	15.79%	13.71%	13.2%
Risk free rate	4.2%	4.2%	5.1%	7.9%	4.9%	5.1%
Financial risk premium	7.5%	7.5%	4.9%	5.3%	4.7%	5.5%
RFR premium	5.9%	5.9%	6.4%	6.0%	6.0%	6.4%
Beta	1.28	1.28	0.76	0.88	0.78	0.86
Country risk premium	2.7%	2.7%	2.6%	2.6%	4.1%	2.6%
Cost of debt (nominal)						
	9.9%	10.0%	11.2%	12.16%	12.4%	11.2%
Risk free rate	4.2%	4.2%	5.1%	7.9%	4.9%	5.1%
Country risk premium	2.7%	2.7%	2.6%	2.6%	4.1%	2.6%
Credit risk premium	3.1%	3.1%	3.5%	1.7%	3.4%	3.5%
Tax rate	34.0%	34.0%	34.0%	34.0%	34.0%	34.0%
Average US Inflation rate	2.5%	2.3%	2.2%	2.2%	2.2%	2.2%
Average Brazil Inflation rate	n.m.	n.m.	n.m.	6.2%	n.m.	n.m.
WACC after taxes	8.06%	8.26%	8.01%	7.94%	8.62%	8.40%

Source: Arsesp, Arsae-MG, Agepar, Goldman Sachs Global Investment Research.

- 4. Regulatory Opex:** Regulator Arsesp proposed an average 4.6% lower opex vs. Sabesp's 2017-20 opex estimates. It is important to highlight that in the previous 2012-2016 cycle, the regulator assumed a 9.0% lower opex vs. Sabesp's opex plan for the equivalent period.

Exhibit 3: Regulatory opex vs. Sabesp's 2017-20 opex estimates

R\$m

		2017	2018	2019	2020	TOTAL
OPEX	Sabesp's business plan	5,920.2	6,222.6	6,111.8	6,086.0	24,340.6
	Arsesp's estimates	5,431.4	5,506.3	5,588.3	5,764.0	22,290.0
Expenses related to PPP	Sabesp's business plan	63.5	131.8	131.8	131.8	459.0
	Arsesp's estimates	63.5	437.5	437.5	437.5	1,376.0
Total	Sabesp's business plan	5,983.7	6,354.4	6,243.7	6,217.8	24,799.6
	Arsesp's estimates	5,494.9	5,943.8	6,025.8	6,201.5	23,666.0
Difference (%)		-8.2%	-6.5%	-3.5%	-0.3%	-4.6%

Source: Arsesp.

- 5. Regulatory Losses curve:** The proposed regulatory water losses curve for 2017-2020 is 31.7%/31.0%/30.1%/29.3% vs. the previous regulatory targets in the 2012-2016 cycle of 32.1%/30.5%/29.3%/28.1%/27.0%.

Exhibit 4: 2017-20E proposed regulatory water losses curve

in %, compared to Sabesp's claim, the previous cycle curve and Sabesp's 2012-16A performance

Water losses	2012A	2013A	2014A	2015A	2016A	2017E	2018E	2019E	2020E
Sabesp	32.1%	31.2%	29.8%	28.5%	31.8%	31.7%	31.3%	30.6%	29.9%
regulator Arsesp	32.1%	30.5%	29.3%	28.1%	27.0%	31.7%	31.0%	30.1%	29.3%
difference	0.0%	-0.7%	-0.5%	-0.4%	-4.8%	0.0%	-0.3%	-0.5%	-0.6%

Source: Arsesp.

- 6. Regulatory delinquency rates:** Arsesp proposed a 1.15% / year regulatory delinquency rate for 2017-2020 vs. the previous regulatory targets in the 2012-2016 cycle of 2.20%/2.07%/1.94%/1.80%.

Exhibit 5: 2017-20 proposed regulatory delinquency rates

as a % of direct regulatory revenues and compared

Water losses	2013A	2014A	2015A	2016A	2017E	2018E	2019E	2020E
Sabesp	1.08%	1.55%	0.03%	0.80%	1.95%	2.10%	2.09%	2.07%
regulator Arsesp	2.20%	2.07%	1.94%	1.80%	1.15%	1.15%	1.15%	1.15%
difference	1.12%	0.52%	1.91%	1.00%	-0.80%	-0.95%	-0.94%	-0.92%

Source: Arsesp.

- 7. Regulatory EBITDA:** The 2017-20 regulatory EBITDA, as per Arsesp's technical note, implies an average EBITDA 7.4% lower vs. our estimates but 23.1% above Bloomberg consensus (exhibit 6)

Exhibit 6: 2017-20E proposed regulatory EBITDA

In R\$m; values as of YE2016

	2017	2018	2019	2020
Direct Regulatory Revenues	13,066.3	13,422.3	13,794.1	14,162.1
Indirect Revenues	203.6	208.9	214.5	220.0
Non Operating Revenues	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(881.2)	(904.9)	(929.6)	(954.1)
Total Net Revenues	12,545.4	12,883.1	13,235.7	13,584.7
(-) Regulatory OPEX	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(149.7)	(153.8)	(158.0)	(162.3)
Regulatory EBITDA	6,900.8	6,785.5	7,051.9	7,220.9
GSe EBITDA	7,117.9	7,366.4	7,695.9	8,022.5
Bloomberg Consensus	5,198.1	5,725.0	5,874.2	5,918.1
Regulatory vs. Gse	-3.0%	-7.9%	-8.4%	-10.0%
Regulatory vs. Consensus	32.8%	18.5%	20.0%	22.0%

Source: Goldman Sachs Global Investment Research, Bloomberg, Arsesp.

Based on the preliminary regulatory parameters, the regulator Arsesp proposed a 4.365% tariff increase for Sabesp, as detailed below.

Exhibit 7: Arsesp's proposed preliminary tariff increase

Breakdown of the preliminary P0 (initial tariff); prices as of YE2016

	NPV Dec 2016	2017	2018	2019	2020
p0 tariff (R\$/m3)	3.59193				
Estimated volumes ('000 m3)	12,501.6	3,637.7	3,736.8	3,840.3	3,942.7
Direct Regulatory Revenues	44,955.4	13,066.3	13,422.3	13,794.1	14,162.1
Indirect Revenues	699.4	203.6	208.9	214.5	220.0
Non Operating Revenues	519.1	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(3,030.3)	(881.2)	(904.9)	(929.6)	(954.1)
(-) Regulatory OPEX	(18,418.6)	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(1,102.4)	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(515.1)	(149.7)	(153.8)	(158.0)	(162.3)
Taxes (Income tax + Social Contribution)	(6,310.5)	(1,913.6)	(1,851.0)	(1,916.3)	(1,948.1)
Capex	(9,625.1)	(2,521.5)	(3,042.2)	(2,996.7)	(3,136.7)
Financial Remuneration for Working progress (18 months)	(578.2)	(151.5)	(182.8)	(180.0)	(188.4)
Changes in Working Capital	(334.1)	(252.4)	(66.9)	(36.7)	(18.9)
Initial Net RAB	40,328.7	-	-	-	-
Final Net RAB	34,069.0	-	-	-	46,367.6
Free Cash Flow	(40,328.7)	2,061.9	1,642.7	1,922.2	48,296.4
IRR (real terms)	8.01%				
P0 at April 2017 (R\$/m3)	3.62652				
Necessary tariff adjustment	4.365%				

Source: Arsesp.

Assessing the preliminary tariff review figures under different WACC and net RAB scenarios

Although we don't take a view on the likelihood of potential changes in the public hearing process and acknowledge a range of outcomes exist outside our analysis, for illustrative purposes we assess different regulatory WACC and RAB figures for Sabesp's final tariff review process.

Higher regulatory WACC: Should we assume a regulatory WACC of 8.40% (based on a beta of 0.862x, as detailed on pages 3-4), we estimate a tariff increase of 6.435% based on an implied preliminary P0 of R\$3.70/m3 vs. 4.365% proposed by Arsesp, all else held equal.

Exhibit 8: GS estimated implied tariff increase under a higher WACC scenario
 in R\$m; values as of YE2016

	NPV Dec 2016	2017	2018	2019	2020
p0 tariff	3.66316				
Estimated volumes ('000 m3)	12,501.6	3,637.7	3,736.8	3,840.3	3,942.7
Direct Regulatory Revenues	45,446.3	13,325.3	13,688.5	14,067.6	14,442.9
Indirect Revenues	693.3	203.6	208.9	214.5	220.0
Non Operating Revenues	514.6	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(3,061.8)	(898.2)	(922.3)	(947.6)	(972.6)
(-) Regulatory OPEX	(18,258.3)	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(1,091.2)	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(520.7)	(152.7)	(156.8)	(161.2)	(165.5)
Taxes (Income tax + Social Contribution)	(6,530.1)	(1,994.0)	(1,933.6)	(2,001.2)	(2,035.2)
Capex	(9,539.4)	(2,521.5)	(3,042.2)	(2,996.7)	(3,136.7)
Financial Remuneration for Working progress (18 months)	(573.1)	(151.5)	(182.8)	(180.0)	(188.4)
Changes in Working Capital	(332.3)	(252.4)	(66.9)	(36.7)	(18.9)
Initial Net RAB	40,328.7	-	-	-	-
Final Net RAB	33,581.3	-	-	-	46,367.643
Free Cash Flow	(40,328.71)	2,220.63	1,805.71	2,089.77	48,468.45
IRR	8.40%				
P0 at April 2017	3.698				
Necessary tariff adjustment	6.435%				

Source: Goldman Sachs Global Investment Research.

Exhibit 9: Implied regulatory EBITDA under a higher WACC scenario
 in R\$m; values as of YE2016

	2017	2018	2019	2020
Direct Regulatory Revenues	13,325.3	13,688.5	14,067.6	14,442.9
Indirect Revenues	203.6	208.9	214.5	220.0
Non Operating Revenues	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(898.2)	(922.3)	(947.6)	(972.6)
Total Net Revenues	12,787.5	13,131.8	13,491.3	13,847.1
(-) Regulatory OPEX	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(152.7)	(156.8)	(161.2)	(165.5)
Regulatory EBITDA	7,140.0	7,031.2	7,304.4	7,480.1
GSe EBITDA	7,117.9	7,366.4	7,695.9	8,022.5
Bloomberg Consensus	5,198.1	5,725.0	5,874.2	5,918.1
Regulatory vs. Gse	0.3%	-4.6%	-5.1%	-6.8%
Regulatory vs. Consensus	37.4%	22.8%	24.3%	26.4%

Source: Goldman Sachs Global Investment Research.

Higher net Regulatory Asset Base: As discussed in the technical note, should we assume the regulatory asset base implied in the company's audited net PP&E of R\$41,987.9mn, we estimate a tariff increase of 4.915% based on an implied preliminary P0 of R\$3.65/m3 vs. 4.365% proposed by Arsesp, all else held equal.

Exhibit 10: GS estimated implied tariff increase under a higher RAB scenario
 in R\$m; values as of YE2016

	NPV Dec 2016	2017	2018	2019	2020
p0 tariff	3.61084				
Estimated volumes	12,501.6	3,637.7	3,736.8	3,840.3	3,942.7
Direct Regulatory Revenues	45,192.1	13,135.0	13,493.0	13,866.7	14,236.6
Indirect Revenues	699.4	203.6	208.9	214.5	220.0
Non Operating Revenues	519.1	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(3,045.8)	(885.7)	(909.5)	(934.4)	(959.0)
(-) Regulatory OPEX	(18,418.6)	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(1,102.4)	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(517.8)	(150.5)	(154.6)	(158.9)	(163.1)
Taxes (Income tax + Social Contribution)	(5,906.9)	(1,789.8)	(1,728.6)	(1,795.2)	(1,828.3)
Capex	(9,625.1)	(2,521.5)	(3,042.2)	(2,996.7)	(3,136.7)
Financial Remuneration for Working progress (18 months)	(578.2)	(151.5)	(182.8)	(180.0)	(188.4)
Changes in Working Capital	(334.1)	(252.4)	(66.9)	(36.7)	(18.9)
Initial Net RAB	41,987.9	-	-	-	-
Final Net RAB	35,106.2	-	-	-	47,779.3
Free Cash Flow	(41,987.88)	2,249.16	1,830.26	2,110.28	49,896.70
IRR	8.01%				
P0 at April 2017	3.64561				
Necessary tariff adjustment	4.915%				

Source: Goldman Sachs Global Investment Research.

Exhibit 11: Implied regulatory EBITDA under a higher RAB scenario
 in R\$m; values as of YE2016

	2017	2018	2019	2020
Direct Regulatory Revenues	13,135.0	13,493.0	13,866.7	14,236.6
Indirect Revenues	203.6	208.9	214.5	220.0
Non Operating Revenues	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(885.7)	(909.5)	(934.4)	(959.0)
Total Net Revenues	12,609.7	12,949.1	13,303.6	13,654.4
(-) Regulatory OPEX	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(150.5)	(154.6)	(158.9)	(163.1)
Regulatory EBITDA	6,964.3	6,850.8	7,118.9	7,289.7
GSe EBITDA	7,117.9	7,366.4	7,695.9	8,022.5
Bloomberg Consensus	5,198.1	5,725.0	5,874.2	5,918.1
Regulatory vs. Gse	-2.2%	-7.0%	-7.5%	-9.1%
Regulatory vs. Consensus	34.0%	19.7%	21.2%	23.2%

Source: Goldman Sachs Global Investment Research.

Higher WACC and net Regulatory Asset Base: Finally, should we assume both the 8.40% WACC and regulatory asset base of R\$41,987.9mn, as described above, we estimate a tariff increase of 7.061% based on an implied preliminary P0 of R\$3.72/m3 vs. 4.365% proposed by Arsesp, all else held equal.

Exhibit 12: GS estimated implied tariff increase under a higher WACC and RAB scenario
 in R\$m; values as of YE2016

	NPV Dec 2016	2017	2018	2019	2020
p0 tariff	3.68472				
Estimated volumes	12,501.6	3,637.7	3,736.8	3,840.3	3,942.7
Direct Regulatory Revenues	45,713.8	13,403.8	13,769.1	14,150.4	14,527.9
Indirect Revenues	693.3	203.6	208.9	214.5	220.0
Non Operating Revenues	514.6	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(3,079.4)	(903.3)	(927.6)	(953.0)	(978.2)
(-) Regulatory OPEX	(18,258.3)	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(1,091.2)	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(523.8)	(153.6)	(157.8)	(162.1)	(166.4)
Taxes (Income tax + Social Contribution)	(6,140.2)	(1,873.3)	(1,814.3)	(1,883.3)	(1,918.6)
Capex	(9,539.4)	(2,521.5)	(3,042.2)	(2,996.7)	(3,136.7)
Financial Remuneration for Working progress (18 months)	(573.1)	(151.5)	(182.8)	(180.0)	(188.4)
Changes in Working Capital	(332.3)	(252.4)	(66.9)	(36.7)	(18.9)
Initial Net RAB	41,987.9	-	-	-	-
Final Net RAB	34,603.7	-	-	-	47,779.3
Free Cash Flow	(41,987.88)	2,413.75	1,999.39	2,284.09	50,075.15
IRR	8.40%				
P0 at April 2017	3.72020				
Necessary tariff adjustment	7.061%				

Source: Goldman Sachs Global Investment Research.

Exhibit 13: Implied regulatory EBITDA under a higher WACC and RAB scenario
 in R\$m; values as of YE2016

	2017	2018	2019	2020
Direct Regulatory Revenues	13,403.8	13,769.1	14,150.4	14,527.9
Indirect Revenues	203.6	208.9	214.5	220.0
Non Operating Revenues	156.8	156.8	156.8	156.8
(-) PIS-Cofins taxes	(903.3)	(927.6)	(953.0)	(978.2)
Total Net Revenues	12,860.8	13,207.1	13,568.7	13,926.5
(-) Regulatory OPEX	(5,431.4)	(5,506.3)	(5,588.3)	(5,764.0)
(-) Expenses related to PPP	(63.5)	(437.5)	(437.5)	(437.5)
(-)Regulatory delinquency expenses	(153.6)	(157.8)	(162.1)	(166.4)
Regulatory EBITDA	7,212.4	7,105.5	7,380.8	7,558.5
GSe EBITDA	7,117.9	7,366.4	7,695.9	8,022.5
Bloomberg Consensus	5,198.1	5,725.0	5,874.2	5,918.1
Regulatory vs. Gse	1.3%	-3.5%	-4.1%	-5.8%
Regulatory vs. Consensus	38.8%	24.1%	25.6%	27.7%

Source: Goldman Sachs Global Investment Research.

We continue to believe that monitoring the preliminary tariff review will be key for Sabesp's valuation. We will revisit our model for Sabesp after the final parameters for the first stage of its second tariff review process are published by October 3, 2017.

Disclosure Appendix

Reg AC

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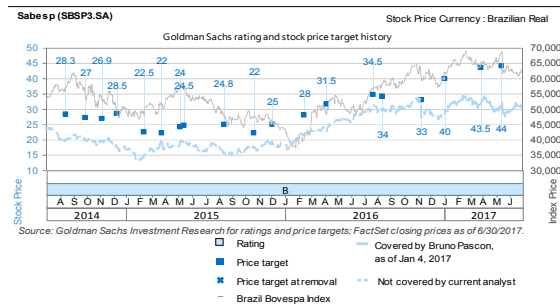
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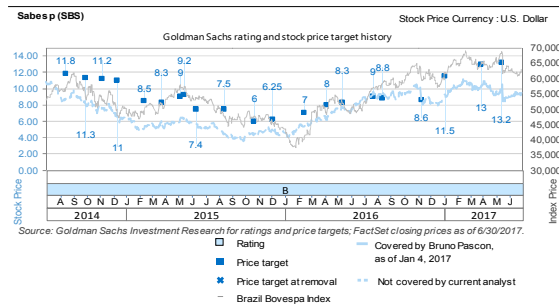
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