

## TRANSELEC AND SUBSIDIARY

Detailed Analysis of the Consolidated Financial Statements  
(Figures in thousands of Chilean pesos)

March 31, 2008 and 2007

(Translation of financial statements originally issued in Spanish)

### **A) SUMMARY**

As of March 31, 2008, Transelec S.A. and its Subsidiary Transelec Norte S.A. recorded a net income of ThCh\$12,041,331, 56.22% higher than in 2007. This net income arises from a positive operating income of ThCh\$25,835,646, from a negative non operating income of ThCh\$9,589,833, a first category and deferred income tax charge of ThCh\$4,204,442 and by the minority interest result of ThCh\$40. As of March 31<sup>st</sup>, 2007, net income of ThCh\$7,707,690 was recorded which is explained mainly by a positive operating income of ThCh\$20,819,220, negative non-operating activities for an amount of ThCh\$10,501,440, a first category and deferred income tax charge of ThCh\$2,609,018, and by the minority interest result of ThCh\$1,072.

During this period revenues reached ThCh\$39,714,461 (ThCh\$34,524,882 in 2007). These revenues come mainly from the commercialization of the transmission capacity of the facilities, revenues include the reassessment of the tolls of the Trunk Transmission System corresponding to year 2007, according to the Decree N°207 of the *Ministerio de Economía Fomento y Reconstrucción* published on January 15<sup>th</sup>, 2008 and the Toll Report of year 2007 published by the CDEC-SIC in March 2008 (ThCh\$5,450,000). In addition, some services related to the activity were sold.

Operating costs amounted to ThCh\$12,404,871 (ThCh\$12,582,962 in 2007), of which 66.23% is explained by depreciation of property, plant and equipment (63.07% in 2007), 11.31% corresponds to personnel costs (12.00% in 2007), 15.03% are associated with contracted services, supplies and contracted works (17.80% in 2007) and 7.43% are due to amortization of the rights of way (7.13% in 2007).

Administrative and selling expenses amounted to ThCh\$1,473,944 (ThCh\$1,122,700 in 2007), distributed as 45.87% in personnel expenses (40.83% in 2007); 46.72% in works, supplies and contracted services (51.62% in 2007) and 7.41% in depreciation (7.55% in 2007).

Non-operating income amounted to a loss of ThCh\$9,589,833 (ThCh\$10,501,440 in 2007), mainly due to financial expenses for a total of ThCh\$8,073,780 (ThCh\$13,299,652 in 2007), goodwill amortization of ThCh\$1,803,880 (ThCh\$3,369,845 in 2007). Other important items that affected the non-operating income during this period were the financial incomes for ThCh\$1,576,863 (ThCh\$5,542,803 in 2007), the negative exchange rate impact for ThCh\$37,129 (positive ThCh\$243,089 in 2007), price-level restatement for a negative amount of ThCh\$1,189,721 (a negative amount of ThCh\$148,802 in 2007) and other negative non-operating results amounted to ThCh\$62,186 (positive ThCh\$530,967 in 2007).

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### **B) INCOME STATEMENT**

Items	As of March 31, 2007	As of March 31, 2008	Variation March 2008/2007	Variation March 2008-2007
	ThCh\$	ThCh\$	%	ThCh\$
Operating Revenues	34,524,882	39,714,461	15.03%	5,189,579
Toll sales	33,969,210	39,090,797	15.08%	5,121,587
Work and services	555,672	623,664	12.24%	67,992
Operating costs	-12,582,962	-12,404,871	-1.42%	178,091
Fixed costs	-3,749,858	-3,267,410	-12.87%	482,448
Depreciation	-7,935,564	-8,216,195	3.54%	-280,631
Amortization of Intangibles	-897,540	-921,266	2.64%	-23,726
Administration and sales expenses	-1,122,700	-1,473,944	31.29%	-351,244
<b>Operating Income</b>	<b>20,819,220</b>	<b>25,835,646</b>	<b>24.10%</b>	<b>5,016,426</b>
<b>Non-Operating Income</b>	<b>-10,501,440</b>	<b>-9,589,833</b>	<b>-8.68%</b>	<b>911,607</b>
Income tax	-2,609,018	-4,204,442	61.15%	-1,595,424
Minority Interest	-1,072	-40	-96.27%	1,032
<b>Net Income</b>	<b>7,707,690</b>	<b>12,041,331</b>	<b>56.22%</b>	<b>4,333,641</b>
R.A.I.I.D.A.I.E.	30,362,390	33,793,243	11.30%	3,430,853

### **PROFITABILITY**

RATIOS	As of March 31, 2007	As of March 31, 2008	Variation March 2008/2007
Shareholders' Equity profitability	0.94%	1.48%	57.45%
Assets profitability	0.46%	0.71%	54.35%
Operating assets profitability	1.76%	2.26%	28.41%
Earnings per share (\$)	7,707.69	12,041.33	56.22%

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#### **C) BALANCE SHEET ANALYSIS**

	As of March 31, 2007	As of March 31, 2008	Variation March 2008/2007	Variation March 2008-2007
	ThCh\$	ThCh\$	%	ThCh\$
Current assets	115,359,288	131,347,867	13.86%	15,988,579
Fixed assets	1,035,096,459	1,002,027,867	-3.19%	-33,068,592
Other assets	514,356,156	557,412,583	8.37%	43,056,427
<b>Total Assets</b>	<b>1,664,811,903</b>	<b>1,690,788,317</b>	<b>1.56%</b>	<b>25,976,414</b>
Current liabilities	44,198,332	141,684,624	220.57%	97,486,292
Long-term liabilities	804,699,122	733,962,738	-8.79%	-70,736,384
Minority interest	108,055	3,829	-96.46%	-104,226
Shareholders' Equity	815,806,394	815,137,126	-0.08%	-669,268
<b>Total Liabilities &amp; Equity</b>	<b>1,664,811,903</b>	<b>1,690,788,317</b>	<b>1.56%</b>	<b>25,976,414</b>

#### **VALUE OF THE MAIN FIXED OPERATING ASSETS**

	As of March 31, 2007	As of March 31, 2008	Variation March 2008/2007	Variation March 2008-2007
<b>ASSETS</b>	ThCh\$	ThCh\$	%	ThCh\$
Land	16,436,957	16,300,553	-0.83%	-136,404
Building, infrastructure, works in progress	746,148,955	738,801,993	-0.98%	-7,346,962
Machinery and equipment	294,891,564	301,578,172	2.27%	6,686,608
Other fixed assets	1,530,226	1,444,279	-5.62%	-85,947
Depreciation (less)	-23,911,243	-56,097,130	134.61%	-32,185,887
<b>Total</b>	<b>1,035,096,459</b>	<b>1,002,027,867</b>	<b>-3.19%</b>	<b>-33,068,592</b>

As of March 31<sup>st</sup>, 2008 and 2007, the fixed assets are composed mainly by lands, buildings, infrastructure works and machinery and equipments.

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The assets of the Company and its subsidiary are valued according to General Accepted Chilean Accounting Principles.

### **DIFFERENCES BETWEEN BOOK VALUE AND ECONOMIC VALUE AND/OR MARKET VALUE OF PRINCIPAL ASSETS**

Considering that the assets of the Company and its Subsidiary Transelec Norte S.A were valued at market value as of June 2006 accordingly to Technical Bulletin N° 72 of the Chilean Institute of Accountants A.G., for consolidation effects, it is estimated that the book value in the affiliated Transelec Norte is 35.2% lower than the economic value and/or market value.

### **LIQUIDITY AND INDEBTEDNESS**

<b>RATIOS</b>	<b>As of March 31, 2007</b>	<b>As of March 31, 2008</b>	<b>Variation March 2008/2007</b>
Current Ratio	3.27	0.93	-71.56%
Acid-Test Ratio	1.69	0.18	-89.35%
Debt to Equity	1.04	1.07	2.88%
% Short term debt	5.21	16.18	210.77%
% Log term debt	94.79	83.82	-11.58%
Financial expenses coverage	2.28	4.17	83.26%

### **D) MOST IMPORTANT CHANGES IN THE MARKET IN WHICH THE COMPANY PARTICIPATES**

Transelec S.A. develops its activities in the market of the electricity, which has been categorized in three different sectors: the sector of generation, the sector of transmission and the sector of distribution. The electric power generation sector include the businesses that are dedicated to the generation of electricity, whether that energy and electric power stem from hydroelectric power plants, coal, petroleum, gas, aeolian, or another form of power plants. It is important to emphasize that that sector is dedicated to the production of electricity, the one that subsequently will be used along the country by the final consumers. The distribution sector has as mission to carry the electricity to the physical place where each one of the final consumers will make use of

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that electricity. Then, the distribution companies have nettings or electric networks that allow the flow of that electricity from the "points of entrance" to their networks, to the residence of each one of their final consumers. Finally, the transmission sector has as basic objective the transportation of the electricity generated from the place of its production (the power plants), and the "points of entrance" to the networks of the distribution companies.

Transec's business focuses mainly on commercialization of the electricity transmission and transformation capacity of its facilities, according to established quality standards. Transec's transmission system, which spans 2900 kilometers between the city of Arica, and the Island of Chiloé, includes most of the lines and substations of trunk electricity transmission of the two major interconnected systems in Chile: the Central Interconnected System (SIC in Spanish), and the Northern Interconnected System (SING in Spanish). These transmission systems transport the electricity that reaches areas inhabited by approximately 99% of the Chilean population. The Company owns 100% of the 500 kV lines, 51.1% of the 220 kV lines and 94.5% of the 154 kV lines.

The electric transmission business in Chile is regulated by the General Law for Electric Services of 1982 (DFL(M) No. 1/82) and its subsequent amendments, which includes Law 19,940 ("Short Law"), enacted on March 13, 2004. These rules are complemented by a By-Law enacted in 1997 (Supreme Decree No.327/97 of the Ministry of Mining) and its respective amendments, as well as the Technical Rules for Reliability and Quality of Service (R.M.EXTA No.40 enacted on May 16, 2005) and its subsequent amendments.

Law 19,940, also known as the "Short Law" (Ley Corta), modified the General Law for Electricity Services of 1982 in matters referring to electricity transmission and established a subdivision of the transmission network into three types of systems: trunk transmission, subtransmission and additional transmission. Additionally, Law 19,940 establishes that the transmission of electricity through either trunk transmission or subtransmission facilities constitutes a public service and is thus subject to the regulation of rates.

Finally, Law 19,940 contemplates a transitory period starting March 13, 2004 that will remain in force until the first pricing lists for the trunk transmission system are published. Thus, during 2007, the collection and payment of transmission facilities continued to be governed, as they were in 2004, 2005 and 2006, by the legal and regulatory rules that were in force prior to the publication of the Short Law. Any remuneration collected by the trunk transmission systems is considered provisional and will be subject to recalculation, according to the terms and conditions established in the Decree N°207 of the *Ministerio de Economía, Fomento y Reconstrucción*, published on January 15<sup>th</sup>, 2008.

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### **E) RISK FACTORS**

Both because of the characteristics of the electricity market and the rules that regulate this sector, Transelec S.A. is not exposed to significant risks as a result of the development of its main line of business. However, it is appropriate to mention and consider the following risk factors:

#### **Regulatory Framework**

The legal rules that govern electricity transmission in Chile were modified recently by the enactment of Law 19,940, called Short Law I, published on March 13, 2004. Although the enactment of the Short Law implies matters to be defined in the electricity regulations, which have still not been drawn up, the most relevant methodological aspects that allow to establish the Trunk Transmission Tolls that each company must pay, the payment and reassessment mechanisms are included in the Decree N° 207 published in the Official Gazette on January 15<sup>th</sup>, 2008. In the case of the subtransmission, the Decree establishing the rates and their respective indexation formulas is still pending.

#### **Concentration of income in only one client**

Approximately 72.6% Transelec's income comes from one sole client, Empresa Nacional de Electricidad S.A. (ENDESA) and its affiliate generating companies. The toll agreements entered into with Endesa and its affiliates Pangué and Pehuenche will generate a large part of Transelec's future cash flow, and any substantial change in their property, financial position or operating results could affect Transelec.

#### **Operating Risks**

Although the management considers that Transelec maintains adequate risk coverage in line with industry practices, it is not possible to guarantee that the insurance will be sufficient to cover certain operating risks to which Transelec is exposed, including risks of nature, damage to transmission installations, labor accidents and failure of equipment. Any of these events could affect the company's business.

#### **Application of environmental rules and/or policies**

Transelec is also subject to environmental regulations which, among other things, require it to conduct environmental impact studies in connection with future projects and obtain the relevant statutory permits. It is not possible to guarantee that the environmental impact studies will be approved by the government authorities, that public opposition will not give rise to delays or modifications of the proposed projects, or that laws and regulations will not change or be construed in a sense that could affect the company's operations and plans negatively.

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### Delays in the construction of new transmission installations

The success of the Expansions and New Works program of the transmission network will depend on numerous factors, including costs and funding availability. Although Transelec is experienced in large-scale construction projects, the building of new facilities could be affected negatively by factors that are commonly associated with projects, such as: delays in obtaining the statutory permits; scarcity of equipment, materials or labor, or changes in their price; adverse weather conditions; natural catastrophes and unforeseen circumstances, and difficulties in obtaining funding at reasonable rates. Any of these factors could cause delays in the partial or total conclusion of the capital investment program, and could also increase the costs of the contemplated projects.

### Technological Changes

The return on investments in electric transmission facilities developed by Transelec is obtained through the annuity of the valuation of existing facilities. In the event of major technological advancements in the equipment used at Transelec's facilities, such valuation could diminish, potentially hindering the total recovery of the investments made.

## **F) EXCHANGE RATE & INTEREST RATE RISKS**

### **Exchange Rate Risk**

Depending on market conditions and other considerations, Transelec has engaged, when necessary, in certain hedging activities such as cross currency swaps and currency forward contracts in order to cover the risk of fluctuations in the UF-dollar relationship for its dollar-denominated bonds. The fact that Transelec maintains these coverage contracts does not, however, guarantee that it will be adequately protected against exchange risks. Moreover, cross-currency swaps and currency forwards are exposed to counterparty credit risk, cash requirements on maturity dates and other associated risks.

As of March 31, 2008, part of the Company's debt is denominated in US dollars due to the placement of bonds abroad in the amount of US\$500,191,940 (includes accrued interest), likewise is the recognition of the payment to be done during April 2008 to HQ related to the VI adjustment (US\$160,807,900) and other liabilities in the amount of US\$46,753,168. On the other hand, intercompany loans to Transelec Holdings Rentas Limitada for the amount of US\$71,858,404 (includes accrued interests), short-term investment in the market for US\$22,364,721 (includes accrued interests), a provision for the goodwill increase due to the VI adjustment amounted to US\$160,807,900, swap contracts in the amount of US\$236,559,715 (includes accrued interests), fixed assets and write-of ways for US\$196,632,403, forward contracts in the amount of US\$ 12,400,000 and other current assets for US\$2,265,374 are the

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assets owned by the company denominated in US\$, which are lower than the respective liability by US\$2,792,745.

As of March 31, 2007, the Company and its subsidiary had part of their debt at fair value denominated in US dollars due to the placement of bonds abroad in the amount of US\$546,953,174 (includes accrued interest), as well as other liabilities in the amount of US\$44,748,169. The US dollars assets include a mercantile credit to Transelec Holding Rentas Limitada amounted to US\$53,914,384 (includes accrued interest), short-term investments in the financial market in the amount of US\$76,072,258 (includes interest earned), swap contracts at fair value in the amount of US\$227,995,312, fixed assets and writ-of ways in the amount of US\$207,057,275 and forward contracts in the amount of US\$17,400,000, and other current assets for US\$2,317,388 which decrease the respective liability denominated in US dollars by US\$ 4,795,002.

Exposure to the exchange rate variation is partially mitigated by the fact that the incomes from the tolls are expressed in US dollars and indexed biannually using indexation formulas that are partly linked to the US dollar.

Toll contracts are denominated in US dollars, but monthly invoices are expressed in the equivalent Chilean pesos, using the average monthly exchange rate for the observed dollar for approximately 92.9% of the contracts and the exchange rate for the observed dollar on the last day of the month for 5.2% of the contracts. The corresponding exchange rates are as follows:

#### EXCHANGE RATE

	<u>Average</u>	<u>Last day</u>	<u>Average</u>	<u>Last day</u>
	<b>2008</b>	<b>2008</b>	<b>2007</b>	<b>2007</b>
January	480.90	465.30	540.51	545.18
February	467.22	458.02	542.27	538.42
March	442.94	439.09	538.49	539.37
<b>Average for the Period</b>	<b>463.69</b>	<b>454.14</b>	<b>540.42</b>	<b>540.99</b>

The indexation formulas applied semiannually incorporated to the toll contracts reflect the variations in the value of the installations and in the operating, maintenance and administrative costs. In general, these indexation formulas use the variations in the international prices of equipment and in the prices of national labor and materials. For the period, the indexation effect increased the value of tolls in average 6.98% compared to period 2007.



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### **Interest Rate Risk**

The company presents debts that contemplate fixed interest rates. In fact, the debt denominated in US dollars contemplates a fixed interest rate equal to 7.875% annual. On the other hand, all the debts denominated in UF were placed with fixed interest rates that vary between 4.25% and 6.2%, depending on each bond. Likewise, the Company maintains a mercantile account with related companies, which is denominated in Chilean pesos, UF and U.S. dollars, and that also contemplates a fixed interest rate. In this manner, it is estimated that the Company does not present a risk that could affect its results due to a change in the interest rates in the market.

### **G) MAIN CASH FLOWS DURING THE PERIOD**

During January 01, 2008 and March 31, 2008, negative net cash flows amounted to ThCh\$6,161,711 were generated, from which ThCh\$16,063,480 come from operating activities, compensated by ThCh\$632,526 used in financing activities, and ThCh\$21,592,665 used in investment activities. During January 01, 2008 and March 31, 2008, positive net cash flows of ThCh\$4,340,585 were generated, from which ThCh\$9,182,815 comes from operating activities, compensated by US\$2,489,527 used in financing activities and ThCh\$2,352,703 used in investment activities.

During this period activities related to financing generated a negative cash flows of ThCh\$632,526, mainly due to a payment of bonds. In the period 2007, activities related to financing generated a negative cash flows of ThCh\$632,526, mainly due to a) the payment of the total capital of Series A Bonds in March 2007 for an amount of ThCh\$119,234,408, which was compensated by the placement of a new UF bonds (Series C) in the same month, for an amount of ThCh\$116,744,881.

In the present period, investment activities generated a negative cash flow for an amount of ThCh\$21,592,665 derived mainly from the acquisition of fixed assets valued at ThCh\$3,236,929 and from negative flows from related companies for ThCh\$18,099,449. In the same period 2007, the negative cash flow from investment activities was ThCh\$2,352,703 mainly due to additional fixed assets by ThCh\$2,141,385.

In the present period, the effect of inflation on cash and cash equivalents was negative and amounted to ThCh\$1,200,215. In the same period of 2007 the abovementioned effect was positive and amounted to ThCh\$541,446.

The final cash balance, as of March 31<sup>st</sup>, 2008, was ThCh\$25,454,520, while the opening balance was ThCh\$ 32,816,446. In the comparison period of 2007 the final cash balance was ThCh\$74,695,892, while the opening balance was ThCh\$69,813,861..