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Corporate participants

- **Rodrigo Costa** – Chairman and CEO
- **Gonçalo Morais Soares** – CFO & Executive Director
- **João Faria Conceição** – COO & Executive Director
- **Madalena Garrido –** Head of Investor Relations

Participants

- **Tomás Reis Vaz** – Analyst; CaixaBank BPI
- **Javier Garrido** - Analyst; JPMorgan Chase & Co
- **Enrico Bartoli** – Analyst; MedioBanca
- **Ignacio Domenech** – Analyst; JB Capital Markets

Madalena Garrido

Thank you all on the lines for your time and availability this morning to join our First Half 2023 Results Conference Call. As usual, we have here our executive team, Rodrigo Costa, our CEO; Gonçalo Morais Soares, our CFO and João Conceição, our COO. Rodrigo will start with his opening remarks, and then João and Gonçalo will guide you through the main operational and financial highlights. We will then move to a Q&A session on which we will be taking your questions. I will now pass the word to Rodrigo.

Rodrigo Costa

Thank you, Madalena. Good morning, as you can understand, we have been very busy, and we will keep being very busy for the time being. The energy transition will keep all TSOs and there a lot of pressure for a long, long time. The range of projects, we are actually addressing it's very diverse from new dams, solar, onshore and offshore wind, new power lines, new substations and upgrade of existing infrastructure. It's a full array of new developments that we have to address. And I think we are dealing with all these projects at the same time. We are facing a reasonable amount of further challenges. Inflation, the topic of the war, workforce ability, the availability of equipment also, the licensing processes. I think we are also -- all the TSOs who are facing these same type of problems and challenges everywhere.

The good news is that we are committed to deliver, and we believe we will make it happen. We have a solid team with good experience and we have been able to attract new talent for the company. The government just published their 2030 energy objectives. Of course, they will be reviewed by the European Commission, and later on the year, we will understand exactly what's going to happen. The plans are very ambitious, as you know, because the documents are public. And I'm sure we will do our part. Again, we know what we do, and the team is professional, and we work with a lot of transparency and everybody can follow what we're doing.

And with that, I think we should move to the presentation. And then like Madalena said, we will be here for to take all your questions

Gonçalo Morais Soares

Thank you, Rodrigo. So good morning to you all. So I think that the first half results were strong results. We came a little bit ahead of expectations in consensus. And this is mainly driven on the financial side and domestically by one side, the increase on the rate of return and also by a decrease of the electricity cost on OpEx. These are the 2 main, I say, drivers. Internationally, we also had a strong performance. There is a bit of -- although it's an operational impact. It's a nonrecurring impact that I will go into to explain you exactly what it is. That also pushed Chile's results slightly higher.

So we do expect this growth rate to normalize in the second half. We are not expecting the same time of performance, but we are expecting growth. I think this is clearly a sign that we have been sustaining growth path for the last quarter. And so we still expect that both international and the rates of return will continue to have a positive impact in the next quarters. Net debt is normalizing. It's normalized a little bit faster than we anticipated is driven by the tariff deviation. I'll also go into that detail, but I'd say nothing out of the ordinary or worrying in that respect.

On the CapEx side, it's a little bit early, but -- and I'll also go into detail, but to give you a note that we are -- I'd say, slightly below expectation in the sense that there are delays. João's teams are being confronted by a lot of permitting issues, and those are delaying the ability both to execute CapEx and to transfer items to RAB. We are still expecting a growth this year on this line, but it's going to be material growth, but it's going to be slightly below what we were aiming for. That thing said, I'll pass it to João to talk about the operational side. João?

João Faria Conceição

Thanks, Gonçalo, and good morning to you all. On the operational side, I will highlight 3 issues. The first one and starting by the end of Slide #5. In the last -- the 1st of June, ERSE published the final set of the parameters for the new regulatory period and gas starting in the beginning of next year 2024. Basically, they made some slight adjustments to the proposal original proposal. You are probably aware of the most important parameters. On the same side, the Portuguese government has recently published the first version on the National Plan for Energy and Climate Plan. This is still a draft. What we can see from there is in line with the overall European energy policy, a big push on renewables, especially solar and the introduction of the wind offshore as well as some extra effort on hydrogen. Focusing on what happened on the first half of this year in terms of the national Portuguese system for electricity and gas, we saw a recovery of the hydro production versus the same period of last year.

And as a consequence of that, the share of renewables within the electricity system increased to the normal levels, and it reached the 60%, around 60% of the all electricity consumed in Portugal. The flip kind of debt was the consumption of natural gas, which had almost a 21% decrease mainly justified by the fact that the electricity generation with combined cycle plants decrease, and therefore, it decreased the consumption on natural gas.

In terms of quality of service, we maintain our levels of quality of service with a slight increase in the interruption time on electricity and full availability of our natural gas operation. Moving to Slide #7. You have the sum up of the major highlights in terms of operation. I would delight the fact that electricity consumption almost didn't change versus the same period of last year. This is partially justified by the fact that progressively, the self-consumption is picking up also in Portugal. And therefore, this type of energy is not accounts in terms of the overall national consumption. As I mentioned, in natural gas, the consumption decreased, transmission consumption, 21%. And on our Portgás distribution operation, it decreased around 10%, slightly higher than the overall value of the conventional, what we consider national conventional consumption, which includes the industrial consumers as well as the households. The national variation was around 5%. Portgás operation decreased about 10%. With that, Gonçalo, I give back to you.

Gonçalo Morais Soares

Okay. Thank you, João. So I mean, on Slide #8, it's just the main key highlights. I will go into this in the next slide. So I'll just jump this slide and going to the consolidated view to give you an idea of where we are. So basically, what you see here of this 11% growth on EBITDA is driven by the -- on all the elements, the first one, assets and OpEx remuneration. This is basically RoR both on OpEx and on gas assets. So these are all being driven by this increase in rates. The other revenues, they are mostly an increase in our own work. So as you have more personnel costs, you also have more capitalized personnel costs. So actually, the increase that you see in OpEx is not the net increase in personnel cost and cost because part of them are capitalized. And also, as you have higher interest costs, you also have more financial loan work. So all of this increases a little bit in the other revenue.

Core OpEx, it's a mix of an increase in personnel costs and a decrease in electricity costs. We'll see that. And International segment is being driven by the good performance and by that nonrecurring impact that I will go into detail in a few more slides. This sums up to the international now already accounting around 6% in this quarter. So I would say that it's in the trends that we've seen in the past quarter.

In terms of Slide #10, it's the trend that you know, rates went up. They are now more stabilized versus what they've been in the past few months. But that versus 2022 made the RoR go up in all segments. So from 4.7% to 5.3% in electricity and around 70 basis points also in both gas transportation and gas distribution. And that is what is pushing remuneration. In terms of investments, as I said, it's a little bit early to give you a full picture. As I said also, we are expecting growth to levels that were probably at the level of 2021 or even a little bit above, but we are expecting still I'd say, strong growth of CapEx versus last year. That being said, and to give you that note also and to be fully transparent, it's a little bit below our expectations and what our operating teams were aiming for.

We have been the delays -- there has been some delays in this. As I said, it's not supply chain issues or cost it's issue of more of permitting. There has been a very strong cooperation between us and the government is also pushing on this matter because it's the energy policy hinges on us being able to deliver on this. But in some cases, there are some delays. There is, for instance, I can give you and João can go into a little bit more detail. A project that is worth EUR 54 million, and that we'll probably won't be able to put into RAB this year and only next year because there's a few permitting delays. They have been sold, but now João is going to start to build it, and it won't probably ready. In the TOTEX model, it's not that it makes that much difference if it's RAB in December or in February, but it delays the numbers of the year. So it's not a major worry, but it's something that we wanted to tell you that we are working on.

And so that makes -- in Slide #12, you see the evolution of RAB. It's normal in the middle of the year. We are still waiting for most of the construction to be completed and put into RAB. The ones from last year, there's also some delays. So it's normal at this stage, you see this negative evolution. If you look at the evolution of returns other than the TOTEX, what you see is that it's mostly driven in gas by RoR.
So you have a negative impact of asset base in gas transmission. That is actually compensated by the increase in asset based on electricity GGS. Part -- which is a part that is not on TOTEX model. But you basically have an impact of positive impact of RoR in both gas transmission and gas distribution.

Moving to Slide #14 and moving to OpEx. So this decrease you see is a mix of those 2 elements that we have there. So on one side, we are increasing personnel costs. There is part of this that is a compensation for inflation, so people were also being increased. But there is also
a big part that is more people. So we are increasing the headcount. And this is good news, although it's more cost, it's good news because it's driven by the activity that we have that is increasing. We need these people. We're actually also reinforcing resilience in some operating and IT areas. So this is good news, but it drives a little bit higher the cost.

On the other side, we have electricity costs that have been able to compensate for inflation in other costs like legal or IT, but the drop in electricity, the one that we suffered last year was bad news this year on a year-on-year trend. It's good news, and this has been compensating and it's been normalizing to where we feel. We still feel that this has some way to go, but at least it has normalized quite a bit. So we do expect still to have a decent performance in OpEx for full year, but part of this impact will normalize and attenuate a little bit as we move along the year.

Relating to Chile. And so in talking about the contribution this contribution that we have to EBITDA has grown quite a bit. In Transemel, as I said, Transemel has been also an evolving as expecting and well, we are starting now to deploy the CapEx in the project that we won last year. We are actually looking at also at new options that they are doing, but we are now starting to deploy that CapEx. But the most important thing to comment here in Transemel is that we have a EUR 4 million impact in revenue, and that is impacting both revenues and EBITDA and this relates to -- and it was a very good job done by the team there. This relates to an addition of revenues that the regulator granted. They do these reviews of assets and revenues periodically, and this was relating to 2020, 2021 and 2022. Review the assets. We presented the case. It's a normal procedure in Chile. And in our case, it resulted in EUR 4 million more. So these were revenues that we were owe, but were not in the accounts in the previous year. So it is a real, I'd say, a real revenue, but it is not a revenue that we should count as repeating itself on a quarterly basis. So you have to adjust this. You can add it to the previous years a little bit, but you cannot and you have to expect it to have a comparable basis for Transemel. Electrogas is still performing well. So gas volumes are still increasing. So we're still going up.

So although we are not expecting that on a full year basis, Chile would grow 70% as it is now. We are still expecting that it will show a very material increase as EBITDA contribution to REN as a whole. In below EBITDA and in Slide #16, so depreciation, nothing to comment, is just the evolution. On the taxes side, what you see is, I would say, nothing abnormal. And the only comment I would make now and I'll leave perhaps for the Q&A for (inaudible) a little bit is that. So we have a mixed message on the levy. So on the first quarter, we had a positive new flow that there was a first case in favor of this for complaining. Now there was a news that there were new court proceedings that were again deemed as legal by the Supreme Court. So there's a little bit of a confusion. So we are not back to square one, but it's a little bit more uncertain how this will pan out again. So we can try and give you a little bit more color, but this is basically what we know.

On financial results and the evolution of this. And so apart from the evolution of net debt, and I'll comment that in a couple of slides. The average cost of debt has been increasing in line with what we expected. So it's now at 2.4%. We are expecting this on the full year to actually go slightly higher because the [arrivers] also went higher. This is also why we are having a little bit more of returns on the RoR side. So we expect -- you don't have it, but on our budget, we'll be a little bit above on that remuneration and slightly higher on the financial expenses because of this reason. So that kind of compensate. So I'd say this is trending in the direction that we anticipated. As I said, it is slightly higher increase in arrivers. We have a little bit more also of financial income, and this is driven also because we are getting more interest on our own deposits. We had a slight increase on the dividend from Mozambique. And we have some favorable exchange rate impact from Chile. Sometimes they are positive, sometimes they are negative. So it's a little bit hard to completely anticipate the direction that they are not material. I say that the trend is that the average cost of debt will still increase a little bit until the end of the year.

So on Slide #17 and as a result, you see all of these impacts. So driven by this EBITDA, which is also has a little bit of nonrecurrent. You see this very, let's say, positive impact in net income. It is, I would say, something that at the end of the year, you will not see we are not expecting net income to grow 37%. So we do expect that this -- we expect it to grow but at a more normalized level and not at the level that we are having now in this second half.

In terms of Slide #18 net debt. So a couple of comments. This is basically the evolution of that being pushed by the issue of tariff deviations. They have increased tariff deviations EUR 554 million since the end of the year, so this is the correction of what we had, which was abnormal. To be honest with you, it was a little bit faster than we thought. It's not that it's an issue, but it proceeded in a way a little bit faster than we anticipated. We are not expecting this to continue to generate these kinds of deviations, and this is mainly a trend trading level. So it's -- those deviations because -- and you might not have noticed, it's public, but the regulator published a revision of the prices that we make the deviations on now in June, exactly to address this. So they were expecting and they were also waiting to see that the deviation would be corrected to put the price in that wood. And this was actually already predicted by them at the end of the year last year, but it puts a different pricing. So that is the deviations now would still not be created at this level. So we are expecting that this will normalize at the level that it is more or less or at the level that we normally have them. So we normally have around EUR 100 million of deviation holds to us, and we believe that, that is, I'd say, the stable level that it normally is. If you take that out, you see that net debt came actually quite [EBIT] and this is driven by strong cash flow performance, a little bit of the (inaudible) CapEx, but overall strong cash flow performance.

A couple of comments. So very high liquidity, very good funding position. The FFO/net debt is now close to 18%. The average maturity, if I take into the use and non-news lines, which many times the non-used lines have higher maturity, if I use those, the maturity will be close to 5 years so 4.7 years. So we are comfortable with the profile of debt with the amount of liquidity. So I think that we are, let's say, in a good place regarding that.

Slide #19, is just the evolution of share price. Nothing to comment to follow this every day. So in the next -- we were more or less aligned.

So now we are slightly below the market. But I think this is -- we cannot look at this on a monthly or a quarterly basis, it's normal trend.

And just to give you a very quick highlights on ESG, we continue and we are happy. We don't put all of the details here, but we are happy then to engage with any shareholder or analysts can give you more detail on this. And we are proceeding with many initiatives relating to ESG mainly, as you can see, our greenhouse gas emissions versus last semester of last year, Scope 1 and 2 are coming out 19%. We are doing a lot of initiatives, namely we are now building in several of our operating facility, gas, electricity and data centers. We are building small solar parks for our own self consumption, so that we can reduce our footprint. We continue to be inclusive in the Bloomberg Gender-Equality. It's something that we continue to strive here. In governance, we continue to invest a lot in cybersecurity and other matters. So this is something that we we've put in the business plan. We'll continue to pursue in a dedicated way. And it's not that it's because of the ratings, but you can see then the reflect and it's also good to see that reflection from somebody on the outside that you see a positive trend in almost all of the ESG rating agencies. So this is not for us the aim, but it's good that it is reflected by other people.
And so we are happy that we can be going in the right direction and that the investments that we are making is being recognized.

Okay. So in terms of closing remarks and in Slide #23, so strong EBITDA net performance, EBITDA and net profit performance in this quarter. As I said, we expect the year to be a growth year, but without this level of growth. And on the net debt, we think that it will still grow a little bit until the end of the year, but we are, I'd say, very pleased with how it is and we are not suffered there. So with this slide, I conclude the presentation, and we can open up the floor to any questions that you may have.

Q&A

Tomás Reis Vaz

I have 3. The first one is related to the financial income, which excluding the dividends, has increased substantially in the quarter from EUR 0.3 million, I believe, last year to EUR 4.8 million this quarter. Could you remind us if there was a one-off or something of the sort last year to justify this difference. Then another question would be about the EBITDA guidance for the full year and whether you're expecting any changes on that and the consensus is currently at EUR 500 million for the year. Are you comfortable with that? Do you see any upside given this semester's performance? And then lastly, I'd like to ask you about the difference between the financial results that you present on the Slide #28 of the report, the EUR 16.7 million, I think. And then on the Slide #42, EUR 18.9 million. Why is there such a big difference here? You usually have a slight adjustment between the 2 but it's much smaller, and that's all.

Gonçalo Morais Soares

Okay. Financial income, I think I kind of explain, but I can give you. So basically, one is the revenues from interest that we are all for money applied in the bank. So as rates increase, we also get more money here. So this has increased versus last year. EUR 2.5 million or EUR 2.6 million. So it is increasing a little bit in the second part without the dividend is the difference in the exchange rates from Chile, which is around EUR 1 million. So that kind of explains the bulk. The first one is more structural, okay? The client is there. So rates are higher, we get more. The exchange rate is more kind of -- sometimes it's EUR 1 million positive, sometimes it's EUR 1 million negative it's what it is. And the second thing I can say is that although we don't give guidance, we are confident with the consensus, okay? And so you can take your own conclusions from there.

The third -- the question you asked is a little bit technical, and we can actually explain that, but this is -- it's in the detail of the report of the annual accounts of the semester accounts is a reclassification of costs. It's a regulated cost that is on management accounting one part on the other accounts. It's not in EBITDA. It's really a detail, but we can give you a little bit more color to explain to you, and we'll send you a detailed explanation of it, but it's basically it's just a reclassification of costs from one item to another.

Enrico Bartoli

The first one is regarding some comments that you may have on the impact on your CapEx plan going forward from the National Energy Plan that has been presented by the government. As you mentioned, there was a significant increase in the targets for renewable capacity by 2030. I was wondering if you have any discussions with the government in order how to implement those targets in terms of support from the -- mainly the electricity transmission network.

Second question is related to the sales to the special tax. As you mentioned, there were some, let's say, different decisions by the constitutional court in the past few months. What is your take there? It seems from the first one that there would be some, let's say, positive outlook for a possible cancellation. What is your feeling what's going to happen and the next steps that you expect on this side?

The third one is related to if you can give us some indication of the evolution of RAB by the end of the year. Actually, it was a bit down compared to the end of 2022. What do you expect for end '23? And also, you mentioned the evolution of CapEx this year. If I remember well, you indicated that at least the EUR 250 million would be a reasonable figure for '23. Actually, if you can update us or provide some details considering that you mentioned that you had some delays in some projects.

João Conceição

Well, we'll start by the first question, the impact on these Energy and Climate National Plan. It's a strong push. As you know, it's a strong push on renewables, especially versus the previous plan, an extra push on solar as well as the introduction of hydrogen and the wind offshore. We are, of course, articulated with the Portuguese government, and we are going to reflect these -- these pushes on our 10-year national plans. On one hand, we have already presented the one for gas as you can see there, the impact on hydrogen is already reflected there. By October, we will have to present our 10-year electricity plan, and it will also be reflecting this goals that Portuguese national energy policy is stepping right now as well as other goals like the reinforcement of some sites, industrial sites like (inaudible) where there is a very high demand for connections for -- on the consumer perspective. Additionally to that, we are also incorporating the impact on this new effort on the wind offshore, which in our case is a significant impact on CapEx, although we are forecasting that for the end of the current decade.

Rodrigo Costa

On the sales, something we learned or some of us who have been around for many years. We should never anticipate a judge decision.
And this is the case where you have a process. We commented on our previous call on the first quarter that what happened. We believe -- we still believe this will have a positive impact in terms of the future of sales. But for the moment, we are still waiting for the constitutional court basically to decide what will be their final views on this case.

And I think we just -- this is where we are. You have some courts to decide one judge to decide one way. You have other judges who decide a different way. And now they will -- at some point, they will announce a final decision regarding those precise cases and that we need to wait for their decision. It's been almost 10 years. And that's the only thing we were sure. It was going to take a lot of time.

Gonçalo Morais Soares

So on your question on CapEx and the EUR 250 million. I think, yes, we are at this base would be the I'd say, our central number also. So we are happy with that number that I've given you, although there has been some delays. So I think that is the number around that, that I think you could safely expect. And as I said, some of the other projects, namely some that contributed to (inaudible) so you should expect a slight decrease in RAB this year also driven by the normal trend in gas that are pushing RAB down. So RAB will go down 1%, something like that. But at the end be mindful that in electricity, now the evolution of RAB is less, I'd say, significant than it was because as I said previously, is RoR now is not as much concerned of the construction being done on the 31st of December or the 5th of January. So we would like to make them in line with what our plans are, as the system needs them, but 1 or 2 more months is of delay is what really pushes us.

Javier Garrido

I have a couple of questions on the regulatory framework. First, now that we've been 1.5 years into the TOTEX model, what are your conclusions so far about this model? What are the pitfalls? And what are the advantages of this model? And how do you think it can evolve going forward?

And second, a question on the gas regulation. Why do you think the regulator has taken a different approach to the electricity regulation and whether you think that at some point when you start to face a higher CapEx bill linked to hydrogen you will be seeing, let's say, harmonization of regulatory frameworks.

João Conceição

Well, starting by the first one on the TOTEX model and the pitfalls and advantage. Clearly, the big advantage -- the biggest advantage is the one that Gonçalo mentioned is the fact that we are not binded by the CapEx execution by the 31st of December versus the 1st of January, and we have much more flexibility to adjust our CapEx execution because we will have to comply with a 4-year period instead of putting all the X on the 31st of December each year. I would say that's the biggest advantage.

The second advantage is related to a better management in what is the development CapEx versus what is the maintenance CapEx and the operational costs. We bundle everything, and even from our operation and our procurement strategy, we can adjust our partners and suppliers in an overall perspective of the total costs in not only the CapEx cost versus the OpEx costs.

On your second question on the gas regulation, the different approach. Our point of view is basically due to the fact that the different sectors are at a different stage of development and the CapEx profile is different. I would say that in electricity, it's more like a continuous trend and a continuous base CapEx, whereas in gas, it's a discrete CapEx. Once you do a project, you have a strong push on your asset base, then you stay for a couple of years without having big projects and then you come with the next big project and you have that binary increase on CapEx. And that probably puts a higher difficulty for the regulator to adjust the TOTEX variables. That's our point of view. But of course, this is a question that, ultimately, it's the regulator is the best entity to explain you why that prefers to adopt a different strategy.

Ignacio Domenech

The first question is coming back to the CapEx plan. I was wondering in terms of the offshore wind opportunity in Portugal on the plan to develop 10 gigawatts of offshore wind capacity. If you could give us a sense of the level of investment that this opportunity could represent for REN?

And then my second question is related with the 2021, '24 business plan targets that you have, we've seen in 2022, but also this year, how you are (inaudible) to exceed the targets that you had. I was wondering if you were planning on to give us a new update anytime this year on these targets.

João Conceição

Thanks for your question. I will start by the wind offshore. It will -- it's -- as you can imagine, in a significant amount, the figures that -- the preliminary figures that we have are not public. And we are not going to disclose them because it will depend on one decision that is still pending which is which model is will be selected by the Portuguese government for building up the network -- the offshore network to connect this offshore wind farms. If it's a responsibility of the TSO or if it's the responsibility of the developers and the connection point is onshore. We will present some preliminary figures by October when we will do the disclosure of our 10-year development plan, which obviously will have to include the goal that the government set for this 2 gigawatts of wind offshore by

2030.

Gonçalo Morais Soares

So relating to the target. Next year, we are going to be presenting a new business plan. you can expect next year to have, I'd say, a full overhaul of the target that you have until. So we are not going to formally revise any targets, but what you can see and expect and given the numbers that I gave you as CapEx. So this year is that on average, we are going to be clearly ahead of the CapEx. The domestic CapEx is clearly higher than we have anticipated in the business plan.

You are going to see the Chile CapEx growth were higher than we had anticipated in the plan, planning by those actions that we won. So -- but we are not going -- we gave you this kind of number for you to guide yourself this year, but we are not going to revise any targets. We will do so next year as (inaudible).

Madalena Garrido

Thank you very much for everyone on the line. We will close the conference call here, but please, we do remain available to answer any additional questions or provide any additional details offline.
Thank you very much for your availability and have a good day.

Gonçalo Morais Soares

And if we don't talk before have a good vacation for those that are right to have a good vacation. I hope you have a good rest and a good vacation.