REN – Redes Energéticas Nacionais
29 July 2016
3,30 pm Lisbon/ London time

Corporate participants

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

Ana Fernandes

Hello, everybody, welcome to the conference. I'm joined by Rodrigo Costa, our CEO; Gonçalo Soares, the CFO; and João Conceição, the COO. They are all ready to hear your questions once it's time for that, but today we'll do an introduction first and then Gonçalo will follow with the presentation. Rodrigo.

Rodrigo Costa

Thank you, Ana. Good afternoon. Yesterday, after the closing of the markets we released our financial report for the first half of the year. As you all know, results were very much in line with consensus and came out without any surprises.

Our overall performance remains very stable, as expected. EBITDA was slightly lower than in the first six months of 2015, but that was mainly because of the absence of extraordinary events. Last year we had the impact of sale of our Enagas shares, that was the major event.

This semester we continue our efforts to become more efficient, both operationally and financially, with OpEx in line with the budget and financial costs better than expected, helped by a lowering cost of debt. Cost of debt came down from 4.1% at the end of the year last year to 3.5% now.

Net income benefited from what I have just explained, but suffered from the maintenance on the energy levy and from the fact that last year the Company enjoyed a lower effective tax rate, due to a one-off fiscal credit. Overall, the quarter was uneventful on the operational side also.

And with that, I will turn now to Gonçalo, and as Ana said, after Gonçalo does the presentation, myself, him and Joao will be here, available to address any questions you may have. Thank you.

Gonçalo Morais Soares

Hello, good afternoon to you all. So as Rodrigo said, this was a quarter and a semester pretty much in line with expectations, as usual. So EBITDA was down 5.5% to EUR240 million, but that drop is basically due to the fact that last year we had that non-recurrent impact from Enagas.

And that is the same in net profit, you see that net profit falls, but recurrent net profit increases basically in line with that improvement in financial costs and I'll go into that. Overall CapEx is in line with our expectations and so I'll also detail a little bit more what's going on on that front.

So if you want to move directly to slide number 3 and just looking at how the bond market has been evolving in the last few months or so. It has been, I'd say, more or less stable, slightly increasing. But it has this year been on average higher in this first six months than it was last year, and that's what you see then on the base rate of return of both gas and electricity power 10 basis points higher than they were, but I'd say pretty much in line with what we had last year.

If you want to go to slide number 4, to CapEx and transfers to RAB, what you see is a big drop that is basically explained by the fact that last year we bought natural gas assets from GALP. If you exclude that, you basically see CapEx and transfers to RAB increasing.
Nevertheless, as you know, at this stage in the middle of the year this doesn't really give us any major information. It's all, I'd say, pretty recent in the investment cycle of REN, which is made basically at the end of the year.
That being said, I would also already tell you that, as we were last year, with the purchase of the caverns, above the interval that we had in the business plan, what we want to be now is below that interval. And this is by design, as we've already told you in previous occasions, so that then on average we will be inside what we had forecasted in our business plan.
If you go to slide number 5, you'll see the normal evolution of our regulated asset base. So what you see is the electricity being shifted from non-premium assets to premium assets. And what you see in natural gas is also the normal kind of evolution, given that we bought the assets last year and that this year we are only making the investments. Later on, you'll see a drop. But overall the expectation would be that over the life of the business plan, the regulated asset base would be more or less stable.

So moving on to slide number 6 and giving you a little bit more color in terms of the detail of the REN remuneration on gas and electricity, you see an increase in both. This is basically due to the fact that you have an increase in asset base in both cases, mainly in gas, and that you have an increase in the rate, which explains a little bit this positive impact in both cases.

Looking at costs, we are down versus last year, this is in slide number 7. We are continuing to reduce personnel costs and also external supplies and services. This is, I would say, the ongoing cost discipline that we have in the Company in order to be able to meet and I'd say slightly exceed the targets that are set to us by the regulator.
As you know and as we've told you before, we consider ourselves already a pretty efficient company now, that is in European terms. We are a pretty efficient TSO; and so we continue to decrease costs.
But the base is now less than it used to be. And although we meet the targets, we do not plan to exceed them by any wide margin, okay? So the impact that you see always in EBITDA flowing from costs is now lesser in terms of size, as it was already last year compared to what it was in previous years.

You can see that also in slide number 8, which is basically just evolution of the core OpEx and seeing how core OpEx evolves. And I'd say the drop is higher than it is in overall OpEx, but pretty much in line with our expectations.
We think that at the end of the year you should see some decrease, but not as high as we have now in the first half. We have some of the costs which is also typically tend to be sometimes occur later on in the year, namely in maintenance.
So overall and concluding in terms of EBITDA, basically the impact versus last year is the sale of Enagas, which accounts for EUR20 million. If it was not for that, you would actually see some increase if you try and see some kind of recurrent EBITDA, you would actually see an increase in EBITDA in this period.

If you go to slide number 10, and just to go over what we have below EBITDA, so depreciation I'd say pretty much in line with what we have on the asset side. In terms of taxes, I'd say we are pretty much in line with what we were expecting on a normal tax rate. They changed versus last year because last year we had a positive nonrecurring impact in the middle of the year of almost EUR10 million, EUR9.9 million to be precise, which doesn't occur this year. But apart from that, things are very stable. And fortunately the special levy is also very stable and it's still there, but I'd say things are very stable and nothing, let's say, out of the ordinary.

In terms of financial results -- and this is always, as we know, the flipside of the evolution of the rate of returns on the asset side -- I think that we continue to do a pretty good job. We continue to take advantage of the momentum of the market and the good credit conditions, and I think we continue to also do a good job in terms of managing our financial structure, which is resulting in, I'd say, an evolution of the cost of debt in a way which is ahead of our expectations.

In slide number 11 we detail how net debt has been evolving. Net debt is, I'd say, growing slightly. It is usual that it grows slightly in the middle of the year, mainly because of dividends. And so I'd say that apart from that, that is what explains mainly the evolution of net debt, which should tend to be, I'd say, more stable on a yearly basis than it is now.

The average cost, as I said, equates to 3.5% and the credit metrics we continue to pledge to the investment grading, so FFO net debt continues to be in a region which we consider comfortable.

So overall -- and we can go to slide number 12 -- net profit came down by 35%, but in reality recurrent net income actually went up on the back, not only of the EBITDA performance, the recurrent EBITDA performance, but also on the improvement of the financial costs.

So summing up on slide number 13, I think that we have, which is good, a non-eventful quarter and semester within expectations. I think that the bond issuance that we did cemented the trajectory in terms of the cost of debt.

We are now more than two and a half years refinanced in advance, so we are in a very comfortable position financially. We are renegotiating some of the loans that we have and so I think that you can expect this trend of the cost of debt to go down to continue.

And apart from that, I think that everything is basically in line with what we want and what is our expectation for this year.

So with that, I thank you for your attention and we will open the floor to any questions and answers that you may have.

Q&A

Nelson Bernardino - Haitong Bank - Analyst

Hi, good afternoon, everyone and thanks for taking my questions. So I just have two questions, the first one on the OpEx evolution for the coming years, asking what are you expecting. It's something around 2% decline every year, something around that.

And also, since your cost of debt has been going down fairly quick recently, what are your expectations for the cost of debt at the end of the year and for the years going forward? Thank you.

Gonçalo Morais Soares

Hi, thank you. As you know, we don't give specific guidance. I think that Ana can guide you through the model, or the more detail, but I can tell you the following.

In terms of OpEx, I think that the efficiencies that you see on the regulatory side and what the regulator is asking us for us to reduce in terms of regulated cost, gives you a good idea of how the costs should evolve. Of course, not all costs are considered within those revenue caps, but it gives you an idea and an indication of what you can expect. And so I would say that our objective is to continue to decrease costs in line with those efficiency targets set by the regulator.

In terms of the cost of debt, as I said, I will not give you specific numbers, but we are now at 3.5%. Part of an expensive debt will be refinanced in a couple of months, so that could have a slight -- although not the full impact -- a slight impact still this year on the cost of debt, if everything stays the same.

And then I'd say that you would feel the full impact of that renegotiation, because it's EUR300 million, going from 6.25% to less than 2%, so it does have a strong impact. So you would see some kind of decrease next year, but we will assume not at the same pace that you saw this year. So what you will see is that decrease, but you'll still see some decrease in the coming year, okay? Thank you.

Nelson Bernardino - Haitong Bank - Analyst

Thank you.

Sara Piccinini - Mediobanca - Analyst

Hi, good afternoon, thank you for taking my questions. I have a few, on the CapEx there has been some discussion on your CapEx plan from the regulator and also from the IMF that has borne the necessity to reduce the CapEx on the transmission networks in Portugal. How much could you eventually reduce your CapEx from the current guidance of EUR180 million and how much of this EUR180 million represents maintenance CapEx?

And the second question would be an update on the special levy, not about what we should expect for the budget that hopefully will take out or reduce the levy, but in the process that you will bring to the constitutional court, do you have any update? And when can we expect the decision?

I mean, this year, next year? And that's it, thank you.

João Conceição

I'll try that, the first question -- it's João Conceição speaking -- on the CapEx plan, what we can tell you is that it's true there has been a discussion with the regulator, it's true that there was some opinions from the IMF and other entities. But it's also true that we have concession obligations to fulfill, so the overall outcome is a mixture of all these points. So we are trying to calibrate our CapEx due to our obligations.

We have typically until now a ratio about 25% to 30% of replacement CapEx, which is a ratio obviously that depends on the overall CapEx that we have to do. We are going to take into the account the needs of the system, the obligations of the concession company and obviously for the future we're going to adjust on those needs. That's basically what we can tell you right now.

Rodrigo Costa

Okay, this is Rodrigo. Regarding the special levy, I apologize, but we don't have much to say. The process is moving on with the court. Our lawyers are working on the case. Sometimes we are waiting for information, sometimes they are waiting for our reply. Courts usually in Portugal, they are not very fast, depending of course on the type of case we are talking about.

In this specific situation, things are slow. We said that since the very, very beginning, I remember the first time I spoke about that and this is it. We need to be patient, we need to also to be smart in how we deal and that's why we have very good lawyers working with us. We believe in the merits of our complaint and we will see the results.

Regarding timeline, this is something that can take from a year to two or three years. It's just the way it works and this is a complex case.

João Conceição
Thank you.

Sara Piccinini - Mediobanca - Analyst
Many thanks.

Fraser McLaren - Bank of America Merrill Lynch - Analyst
A very good afternoon to you. Just looking please for an update on international investment plans, including the Moroccan interconnector please.
And then just secondly, just having completed a regulatory review, could you say a few words about your relationship with the regulator and to what extent that has been shaped by your experience of the review? Thank you.

Rodrigo Costa
Okay, regarding an update in terms of our international efforts, we keep working in the direction we disclosed some time ago. We have – our ambitions are very modest, but we believe we should do it.
But as you know, this is a very difficult market and we have some rules that we are not going out of those rules. We will only invest in areas where we are experts, we do not want to diversify from our core competencies. We need to find projects that have a size, a model, a guarantee that is according us with the level of risks we want to take, which are low.
And this takes time, so we are patient, we are not going to jump in the wrong project, for sure. And as you can expect, I cannot say much more.
Just sharing what are the rules, we are very committed to keep playing under those rules.
Regarding the interconnection with Morocco, this is a project that at the time what's going on is the Government of Portugal and the Government of Morocco, they launched a tender to do the studies of the implementation of these interconnections. And this is the phase where we have to wait for the results of the studies.
This is not something we are going to take part of, because our objective is to play a role at a later stage in the management and concession of this line, if we can. But it's still subject to the result of the studies, it's subject to approval of the project by both governments and then it's still a long way.
This is something we believe and we agree with the Portuguese Government and also with the Government of Morocco that this is an importante project. For the plans that the Portuguese Government is disclosing regarding generation, this makes all the sense. It could be an opportunity, we will see what are the results of the studies and that we are following very, very carefully.
On your other question regarding the regulators, this is one of the companies where there is no doubt we have to maintain all collaboration possible with the regulator. We manage two very large concessions, critical to the country.
We are very committed to our long-term mission, which is to make sure all the citizens, all the companies, all the systems work properly and that's basically our main drive in everything we do. And the regulator is a key stakeholder in this process and we work, we collaborate. It doesn't mean that we always agree, but I'm sure on both sides there is a lot of commitment to do our mission.
And with that, I would say some days it's more difficult than others, sometimes we are able to make ourselves understandable and people accept our proposals, sometimes they don't. But the world keeps moving.
And as you can see from all the indicators we have, and I would say both operationally and financially, we have been able to deliver according to the best expectations of the country in terms of companies and citizens. And at the same time, we've been able to -- we have been succeeding, delivering to the best expectations of our investors, which I think is a great combination.

Fraser McLaren - Bank of America Merrill Lynch - Analyst
Many thanks.

Ana Fernandes
Well thank you, everybody. Have good holidays, the ones who are going on holidays and we'll see each other again in September. Thank you.