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Corporate participants

- **Rodrigo Costa** – Chief Executive Officer
- **Gonçalo Soares** – Chief Financial Officer
- **João Conceição** – Chief Operational Officer
- **Ana Fernandes –** Head of Investor Relations

Conference participants

- **Javier Fernandez Garrido -** JP Morgan Chase & Co
- **Sara Piccinini - Mediobanca -** Banca di credito finanziario S.p.A.

Presentation

Ana Fernandes
Hello, everybody. Happy Friday. Thank you, and welcome to our conference call. It's the usual thing, we're joined by Rodrigo, Gonçalo and João, the executive team of REN. And we'll follow the procedure of the last results conference calls. So I'll pass the floor to Rodrigo. Rodrigo?

Rodrigo Costa
Thank you, Ana. Good afternoon all, and thank you for joining us for the annual results conference call. Ana sent me the comments some of you had made so far and it seems that results are aligned with the average market expectations. After my introduction, Gonçalo will go through the financial highlights and then together with João Conceição we'll be able to answer any question you may have.
I have some brief comments about the results. Overall, we had a positive year. We did very well in all our operational items from service, security, efficiency targets, plan execution, new business integration, all things that depend on our management capacity went quite well without any negative surprise, and that's super important for our team.
From a financial results perspective, it's obvious that a lower net profit is always something we would rather not have, but still we believe that under the circumstances, all in all, we have had a good set of results since we went through a year where we had higher amortizations and some tax increases that we will go over at a later point, and I'm sure we'll talk about our tax challenges.

In that regard, progress is 0 so far regarding sales, as you know. But it seems that at least we see the light at the end of the tunnel.
According to the government, with the decline of the social tariff deficit, the sales tax will come down and eventually will go away in 2, 3 or maybe 4 years, but that's at the most. We keep our court disputes, but you all know that it will take time. There is a couple of matters that I also would like to talk about, and I think they are positive signs for the future.
Both Electrogas and Portgás projects are going well and aligned with our best expectations. These 2 projects were and are a key contribution to offset expected lack of domestic investments we had over the past 4 years. For the first time, we have seen our investment plans approved by the government. This is totally new, and a positive important step towards the new energy transition plans introduced by the Portuguese government. The new plan will also have a positive impact on the investment outlook, not massive impact, but a relevant impact.
The plan approval is also providing a good guidance regarding the next 5 years in terms of investment. This is something that before we always had trouble to disclose. Our EBITDA remained stable. Our financials are robust, and we had a decrease in the level of debt. In this regard, the news were also good. On the results themselves, now Gonçalo will give you a more detailed overview and after that we will go through any other matter you may want to cover. Gonçalo?

Gonçalo Morais Soares
Thanks, Rodrigo. Hello, good afternoon to you all. So let me start right away on Slide #2 with the highlights. So I think '18 was another very stable year, very much as we expected year. I think that we are very happy that we were able to deliver on the plan that we presented to you earlier on 2018, and we delivered both on the numbers that we told you then, and we delivered on the integration of Portgás.
I think we will keep, as Rodrigo said, focusing on Portugal. We keep our electricity story simple and we keep basing ourselves on safe and regulated assets, which is what we like.
In terms of numbers, EBITDA is growing around 1% to EUR 492 million. Net income, as expected, was down around 8% to EUR 116 million. CapEx was actually a little bit higher than expected at EUR 122 million, which made cash flow particularly strong, and we were expecting this that this allowed for us to decrease net debt more than EUR 100 million in the year of 2018.

We want to skip Slide #3, which is just the main key numbers, and we go directly to Slide #4.
I think we continue to see this, I would say, extraordinary interest rate environment, rates continue to come down at a very low level. This is good news for Portugal, and this is, of course, some pressure on our own regulated returns. And but we have, for some time been managing this on the financial side, on the funding side, and we have in debt area, been managing both a scenario of increasing rates and at the same time also a possible scenario of low rates for a longer period.
At this time, electricity returns then came down from 6.3% to 5.2%. And actually at the rates that we are now, which is with PGB's 10-year bonds at around 1.1%, 1.2%, we are very close to the floor in electricity, and we are already at the floor on the gas returns.

If next moving on to Slide #5, and talking a little bit about CapEx. So this is the first point where we deliver on what we told you early in '18. We said that CapEx will be between EUR 120 million and EUR 145 million. We actually told you

that in '18, we would be below that interval because it was the lowest year in the business plan, but we actually were able to be inside with EUR 122 million. And secondly, and as Rodrigo said, we think that the approval of our long-term investment plan is very positive and gives us full certainty of all the CapEx that we have included in the business plan. It is actually a little bit above what we had in the business plan, not in a material way.
And that's not even considering the new measures and the new [Connect] 2030 plan that the government has issued. And to be very clear with you, we don't really have any new estimates or figures to give you now of what the impacts could be, we are still working on that. But even if they're small, it's good news. I think that it's more investment in the sector.
In terms of forecast, let me just make a remark that don't forget that the number that you see in 2017 there is only relating to 3 months of the company. So the EUR 25 million in '18 -- EUR 24.9 million relating to the 12 months and the other are not. So there is an increase because CapEx increase in Portgas and will go to debt, but it's not such a big increase.

Moving on to Slide #6, we can see that RAB evolution then is no surprise, and this is exactly because of this decrease that we see here that we anticipated and that we invested both in Chile and particularly in Portgás in 2017. So what you can see is that Portgás really does have a lot of asset base in the last few years. And relative to Portgás, let me tell you that the unit has been delivering on the plan, CapEx of close to EUR 25 million, up from EUR 21.5 million the year before. And we are investing and continue to invest in the networks. We connected more than 13,000 new clients. We built close to 220 kilometers, so we have been executing on the company and on the growth that we told you that the company has.

And on Slide #7, we come to RAB remuneration and this, as expected, has dropped. And the reason mainly by the decrease of rates, but also, as I told you, by the decrease in the asset base. And I think -- let me just tell you already some information because you're probably going to ask us about the new regulatory period for gas in the coming times. Just to alert you that some of the rates are a little bit different. So because in sales they have been more or less anticipated both around 2 weeks, so we will have the first idea of numbers in 1st of April and then the final ones in the 1st of June. So João will then go into a little bit more detail. I think we are not expecting any major changes in the framework, he has been discussing this with us in the recent weeks. So I would say that overall you should expect more or less the same thing.
One thing also which is a little bit different is that now it's going to be implemented in sync with the period for electricity, so it will only start in 1st of January of next year and not the 1st of July of this year as it usually is, which I think is good news given that the rates are going down a little bit.

So going for the next slide and talking a little bit about OpEx. OpEx this year is a little bit confusing to analyze because not only of Portgás, but also because some costs went from passthrough to be in the revenue cap. That being said, what can I tell, what can I tell. So in terms of personnel costs, they grew by around EUR 700,000, but in the transmission business, part of this forecast that came from the distribution business because of our centralizing function, and part of this was because there was a little bit of a one-off in 2017 relating to pension rules that have more or less a EUR 0.5 million impact. So I'd say that without those kinds of effects, it would be more or less

flat. Headcount decreased slightly. What you would see if you saw the detail, is that you would see people moving from gas distribution that were in the support functions back -- or back not but into our shared services centralized functions, that was the main move that happened. Overall, the decrease of 2 people.
And talking about Portgás, just to tell you that the migration is going as expected with no hiccup. It's going really well and most of the support functions is mostly done and the support functions systems are basically done. Also, now we are only migrating some things up until June, July where everything will be finally migrated and the agreement of transition when the sale with EDP will be concluded. That being said, I can also tell you that the [cost of Portgás whether] will be decrease this year as we expected in our business plan.

Going for Slide #9 and talking a little bit about core OpEx. This is where I told you that it's a little bit confusing because of these costs, that some of them are now in the revenue cap. The forest cleaning is the main one. So what you cannot see that you see EUR 3.8 million more but at the same time you also have EUR 3.4 million in the cap in terms of revenues. You have some costs that are related to electricity in the LNG Terminal that you do not see but also have corresponding revenues. You have certain costs that were incurred because of Hurricane Leslie that have also corresponding impact because of insurance payments. So at the end of the day, what you would see was mainly you have a little bit more of cost because we issued debt as we didn't do the previous year. We have a little bit of cost because of the business plan that we did, a little bit more of maintenance cost and that was more or less balanced by the fact that we didn't have any M&A costs. So at the end of the day, it would be more or less flat in the year. And I would say that's more or less the trend also for next year, will be more or less to be flat or have a small decline within, I'd say, what the regulator usually asks us to be deficient.

Moving on to Slide #10 and in terms of EBITDA. So what you can see is a result of this. So you have a plus on the forecast side and a minus on the normal decrease on rates of return. You have this I'd say one-off impact of the LPG sale which was, in our opinion, a good proceeding, it was a nonstrategic asset for us, and we sold it well.
And in terms of Electrogas, I haven't said anything, but it's basically in line with the plan. It's basically in line with the numbers that we have when we bought the company. And there is a small decrease last year in terms of revenues, very small because of some of the revenues, which are interruptible as I say, so it's not the firm contracts, but the other ones. But actually, in terms of EBITDA contribution, it increased a little bit because the previous year we had a lot of transaction costs, which you don't have this year. So it had an impact of around EUR 6.5 million in EBITDA this year. So this is another objective that we achieved. We said that we would be between EUR 475 million and EUR 500 million in terms of EBITDA, and we are at EUR 492 million. So another one that we delivered on.
Moving to Slide #11 and looking at below EBITDA. So depreciation is basically the impact of business as usual and Portgás. Portgás has to have rate increases. And the second thing I wanted to touch upon is taxes. So there was -- there is a slightly higher effective tax rate.
So there's several things at play here. One, which was expected is because the corporate rate for a company of our size increased slightly last year. So the tax was a little bit more in all of the companies above a certain amount, we're taxed a little bit more, so this was already in the budget, it was announced.
The second thing is that because this year we generated a little bit more deviations in REN Trading, the company that manages those 2 PPAs, that translates into a tax -- deferred tax liability, which actually adds a little bit to the tax rate. This happens every year, perhaps this year it's a little bit more visible, but so it's something that happens every year, sometimes it's in one side, sometimes it's in the other.

Since REN is trading normally, is more on one side, the deviations are normally to one side, it normally has this kind of an effect, but that's it. So there is nothing very abnormal. I think that the only thing which is abnormal is that we are still paying the special levy, but that's a story that we -- you all know. As Rodrigo said, there's no news on that front. I would say that if you wanted to look at the normalized tax rate, I would go for something around 28% that would be more or less this. And in terms of financial results. I think we are keeping with the tradition. We are still continuing to decrease, but at the floor, right, so we came from 2.5% to 2.2%. And that joined with the fact that the average gross debt actually increased during the year made the costs only go down by around 6%, so EUR 3.5 million. And as I told you, we have been careful to manage for both interest rate scenarios in this period. So our first objective is clearly to protect net income. Our second one is to optimize the cost of net debt, but as has been proven, it's not good to place everything in one scenario. This low rate scenario has been staying perhaps longer than many others expected. I think we were prudent and wise to be managing for both these scenarios. So we are now renegotiating some loans, which will extend a little bit more the maturities that we have. But we do not foresee any bond issuance in the short term.

Now moving for Slide # 12. I think this is an important slide also because we were able to have an important decrease in net debt. This is also very important for us. It's just normal cash flow, nothing very out of the ordinary. This has strengthened really the FFO net debt figures, I think we are in a good position, this is another objective that we actually more than fulfilled versus what we said in terms of our business plan and much closer to 13% and not the 11%, 12% that we said. So I think this is an area where the prudent management of cash flow has paid off. Of course, in the future, we don't expect to resist debt every year around EUR 100 million, but I would assume that it would continue to go down in the coming year.

Moving for the next slide and looking at net profit. So it's down, but it's already also not only down, but above our target. So it's the normal EBITDA, went up a little bit, but at the same time depreciation because of Portgás went up more. We have a little bit more effects, slightly lower interest cost, but everything together made I think it come down this 8%. But I have to tell you that this EUR 115.7 million, so basically EUR 116 million is above, again, it's another goal achieved, it's above the range that we had told you. So we had told you that net income would be between EUR 110 million and EUR 115 million, and so we are again above or more than -- we think we are above the range that we had told you, and fulfilled the target with investors.

So as final remarks. And as I told you, so this was a very stable year. Portgás [revealed] was an important acquisition. It was an important year to be able to digest and integrate well. So this is I would say already business as usual here under the direction of our COO, who manages also this division and it's going pretty well. And financials are improving as expected. And unfortunately the levy is still there, but it didn't -- this was not enough for us, not to be upgraded by S&P recently, and I think we are maintaining a very strong investment grade profile. And as there was also published, the Board of Directors is going to propose to the general assembly the dividend that we set out in the dividend policy in our business plan of 17.1 cents. So I'd say another thing which is completely as was expected. So with this, I conclude my presentation. And we open up the floor for any questions that you may have. Thank you.

Q&A

Javier Fernandez Garrido

I have a couple of questions. First one is on the evolution of your net debt. We look beyond operating cash flow items, both in CapEx and in tax payments, the payments were significantly above the accrued figures. Should we expect to see more similar number of payments versus accruals in the next couple of years, or should we expect to see the still incremental payments versus a good figure? The second question is on the outlook for CapEx. You have described that it's positive to see approval of your long-term plans by the government, but how -- let's say, sustainable is that CapEx level, because if Portugal is going to deliver on the aggressive targets of renewable capacity additions and is going to shut down coal capacity radically by 2025, shouldn't your CapEx requirements increase relatively soon, what is your view about that? And then the third question is on the interconnection with Morocco. Spain has signed a memorandum of understanding with Morocco for a third interconnection. Is this the end of the plan to build a direct connection between Portugal and Morocco, or is there room for both players?

Gonçalo Morais Soares

On the first question, [cash flow] now, I mean, sometimes you have a little bit above, sometimes a little bit below. If you take the longer term, it should be more or less the same. And if you want to simplify in your model that's what I would do. Of course, in some years, you have a little bit more, in others a little bit less. That should not change the fact that you'd have in the coming years still positive cash flow in every year, excluding any nonorganic investment that you do, so you'll have -- when we did the business plan we said that debt would come down by around EUR 200 million or EUR 300 million if there wasn't anything like that, so I'd say that we did EUR 100 million in the first year. You can expect, I'd say, EUR 150 million of decrease in the next 3 years. So something like if -- but of course, that could vary a little bit, okay? João will answer the second.

João Conceição

First of all, good afternoon. Regarding your second question, I would say on the first point, like Gonçalo has already mentioned, that the approval of our electricity transmission plan already includes a couple of projects that the purpose are precisely to accommodate these efforts of higher renewable penetration. That's why we are quite happy that -- due to the fact that we need approval on the very short-term, say in the next 2, 3 years, we will have the necessary approvals of the projects that we included in the business plan. Having said that, as it was mentioned also before, we are, at the moment, assessing the consequences for the grid regarding the energy plans or the energy transition plans that the government put forward. We do agree with you that they're quite aggressive ambition into increase renewable targets. These, of course, will have an impact on the grid. These, of course, will mean that the grid will have to adjust to accommodate this new renewable capacity and that's exactly what we are doing at the moment in order to present our new CapEx plans to the government. João?

Gonçalo Moprais Soares

Regarding the last one on the Morocco project, this is something we are not really including in our plans for the moment. We always said that this is going to be subject to a government decision. We believe -- to your question if we think there is room for these projects – we think so, we believe that both for Portugal and Morocco, it's important to have this interconnection. It would make sense. This is something that has been studied for many, many years and it always creates more redundancy between the systems, and I think it's even good for Europe and also even for Spain. This is something that makes sense. Now there was a study that has been commissioned through a specialized company. And these studies should be ready in a couple of months, and then the governments will be able to make a decision. I'm sure that they will consult the DSOs, both the one from Morocco Energy and us. And hopefully, this will be -- we will have a positive outcome. I also like always to remember this is a very long term project. These type of projects, they take a number of years to be prepared. You have a design phase, a licensing phase, and then you have the construction, then we think again, we think it's a good thing that would help both systems, the Portuguese energy system and the Morocco energy system, creates redundancy, creates competition. And the Portuguese energy system and the Moroccan energy system, they are very complementary, in the sense that when they have extra energy, we don't and when we have extra energy, they don't. And then I think it would even in life of the new plan, the new transition plans, I think, this would make a lot of sense. But -- and we will keep updating you as soon as we have more news. And I think also both governments will have to deal with the decision.

Sara Piccinini

I have four. The first one is on EDP Gás, the EBITDA of this business is actually showing a decrease versus last year. Is this fully attributable to the lower returns due to the Portuguese bond and can you see any synergies going forward that can improve the EBITDA?
Or in other words, if this EUR 35 million can be seen as a normalized EBITDA for EDP Gás going forward? So your expectation on EBITDA in EDP Gás is the first question. The second is on consolidation opportunities, if you can please remind us which consolidation opportunities for external growth are you considering and if you have any update from the renewable of some electricity distribution concessions in Portugal? The third question is on the working capital in the cash flow. If you can provide us a figure of the net working capital in the evolution of the debt from EUR 17 million to EUR 18 million, I missed the and that you say that figure is. Is this a positive working capital effect? And final question is, if you can repeat the process of the review of the gas -- regulatory review of the gas business. So you said on the 1st of April, there should be this first draft and then this new WAC should be applied from 1st January, 2020, correct?

Gonçalo Morais Soares

So on forecast, it's no longer EDP Gás, but, yes, I heard your question. So we didn't see the -- so we actually don't see the EBITDA come down. It's so that there is an impact of around EUR 4 million of the LPG business, which is, I'd say, a one-off. But on the other side, we also saw the RAB remuneration come down, being more than compensated by the OpEx contribution. So we contextually see the EBITDA come down. I think Ana can give you a little bit more of the details. But even excluding this EUR 4 million, you'd still see it go up by a
little bit, okay? So that's not the case. Of course, looking forward, when you implement the new regulatory regime that João will explain in a minute, of course, you will see rates go down, and then you'll probably see more of an impact on the rate of return, but as of now, we don't see that, okay?

João Conceição

I'll take the second and then I will go -- we'll go back to the results. On the consolidation opportunity, just to say that, we have nothing new to report. We do not have anything that we can talk about at the moment. We keep our strategies to one we presented last year, and I think you know well. In Portugal itself, we don't believe there is really opportunities at the moment. We never know, but we are not expecting really anything to show up that soon. And regarding our research outside, we keep doing our research. We always repeat our objective and somehow also -- Gonçalo already spoke about it. We like the businesses that are regulated and/or are very close to be regulated. We only like geographies where we have a very stable outlook and we always play on the safe side. What we did before is exactly what we will be doing in the future if the right opportunity show up. With that said, we know how important it is to find the right opportunity because what we had in the past couple of years is, the effect of investing in Electrogas and Portgás was good, and it compensates a more mature market that we have here in Portugal. Of course, in light also of these new transition -- new energy transition plants that all the governments are doing and Portugal is no exception, we think there will be some more opportunities that we will take advantage for sure.

Gonçalo Morais Soares

Just to comment on forecasting to João, on the issue of working capital. So there isn't a lot, so there's only a couple of things. What you can see is that we have CapEx of EUR 122 million and CapEx payments of EUR 144 million, I'd say that's completely normal within what happens normally in our business. And the other thing that you have more or less in terms of working capital is the fact that tariff deviations increased by EUR 6 million, but they are basically stable. So you'd have, even, I'd say, a bigger decrease in terms of net debt if they stayed exactly the same. But apart from debt, there isn't any. And these are 2, which are very, I'd say, common, and even small vthings in terms of working capital. So I'd say, it's not very material in terms of the evolution or the combination of the evolution of the net debt in a period. João?

João Conceição

Thanks, Gonçalo. Regarding your question about the process, basically, what impacts on us are 3 things. The first 2 are minor. It's just that previously as we do the first proposal by the 15th of April, and now it will do it by the 1st of April, and the final proposal was set by the 15th of June, and now it's supposed to be set by the 1st of June. But the biggest change is that, contrary to the past where the regulatory period was starting on the 1st of July, now the regulatory period is postponed, and these new parameters and all these new rules will only apply from the 1st of January 2020 onwards. So these are basically the 3 changes on the process that the regulator is proposing.

Ana Fernandes

Okay. So if there are no further questions, I wish you all a great weekend. If it's sunny where you are as it is here in Portugal, it's going to be great. And if you have any questions that you want to ask me later, I'll be available. Thank you. Have a nice day.

Rodrigo Costa

Thank you.