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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, everyone. Welcome to this conference call. As usual I am joined by Rodrigo Costa, our CEO; João Conceição, our COO; and Gonçalo Morais Soares, our CFO. Rodrigo will say a few words and then Goncalo will go through the presentation that we made public yesterday. We welcome your questions afterwards. Rodrigo?

Rodrigo Costa
Thank you, Ana. Good afternoon all. This time we have some more events going on and we expect that our call will go beyond the quarter results that we just released. In general and again we had a good quarter and results were in line with analyst forecasts. Although at the financial level we did better than expected.
EBITDA reached EUR124 million, a small increase over last year's numbers, and mostly explained by the high sovereign bond yields. I also want to mention a new fact; this is the first quarter accounting for Electrogas contribution to our results.
Operationally, things are going according to plan. OpEx was necessarily higher due to the first phase of Electrogas and other than that there is nothing extraordinary to report besides the business development activity that we will speak about later.
During the quarter, we kept our focus on being as efficient as usual.
We had good progress on the average cost of debt, benefiting from the bond tenders executed in May 2016 and the other two bonds issued also done in the last year. Net income naturally benefited from better financial results but we kept being negatively impacted by the energy levy.
These are the main topics regarding the past quarter. Yesterday we also had our annual shareholder meeting. Every Board proposal has been approved by over 99% of the voting shareholders. The meeting agenda included the 2016 accounts report approvals plus the usual recurrent Board proposals.
A key topic was the capital raise for the acquisition of EDP Gas that was approved. All went super well with great support from the shareholders.
And now we move to Goncalo who, as usual, will go through the results presentation and in the end we will be available to answer any questions.
Thank you.

Gonçalo Morais Soares
Okay, good afternoon to you all. Welcome today. So I think we presented a very solid set of results for our first quarter. As Rodrigo mentioned, our EBITDA amounted to almost EUR124 million, an increase of 2%, 2.1% to be exact over the last year on the back mainly of the evolution of the electricity rate of return and we will come to that.
And also our net profit rose from EUR7.4 million to EUR13.5 million being boosted not only by these strong operational results, but also by the good performance, which has come in line with previous quarters of our financial cost and the declining average cost of debt which has come down to 2.6%. Even executing extraordinary effect our recurring net profit would have increased quite a bit.
Net debt grew a little bit but was basically due to the Electrogas acquisition. If it was not because of this net debt actually would have fallen in the quarter by a large amount. As in recent years and we've said we continue to have the energy levy in place and that accounted for EUR25.8 million.
And as you know, we already account for the full amount in the first quarter in our account. It's basically -- actually it's EUR100,000 below what we had last year basically driven by the evolution of the assets.

CapEx and transfers are basically increasing but in line with expectations very early. And we will talk a little bit more about -- if you need then about both the Electrogas but also about the EDPG transaction which we covered before, but we can give you additional -- a little bit additional color in the Q&A if you want.
So moving into slide number 3, slide number 2 is just KPIs and I will move over that slide. In slide number 3 you can see that there has been a slight increase in the bond yields in the last few months, which in our case has been translating into an increase in the rate of return. And this is, as you know, the name of the game in the regulated space.
And in this case this has translated into the fact that our base rates of return for electricity and gas have gone up from 6% to 6.5% in the case of electricity and from -- and have come down from 7.4% to 6.4% in the case of gas. Mind you that in the case of gas there was a change in terms of the regulatory period and the rules last year.

Moving to slide number 4, you can see that CapEx is growing and the transfers to RAB are also growing. But to be honest this is now still meaningless in the sense that it's very early in the year. We are actually going over also the CapEx plans, even our recent acquisitions or the planned acquisition that is to be closed of EDPG.

And so, but this is completely in line I would say with our own internal targets and there is I'd say nothing to add or to stress at this stage – which in slide number 5 you can see translates saying the normal [root] composition of the asset base, which is a decrease on the electricity without premium and an increase in the electricity with premium.
It is also on a year-on-year basis translating that decrease on the gas, which is normally already what you had seen at the end of last year and because of the fact that we have invested mainly in 2015 by buying [Dos Caverns] and now there is a decrease on the asset base as we have no major investments to do on that business unit.

Then slide number 6, you can see how that translates into RAB remuneration. So you see that that's an expected good increase on RAB remuneration on the electricity side and this is basically driven by the fact that we are now at a blended rate of return of 7.22% versus 6.78% that we were in the assets with premium before. And on the natural gas part it's basically driven because of that change in the regulatory period. But I would say also it will be higher than our expectations in terms of rates of return.

Moving to slide number 7 and in terms of cost you see a slight increase in the beginning. This is mainly driven because of transaction costs that are incurred in this first quarter. So there is nothing I'd say alarming in the cost structure that is driven by the acquisition of Electrogas, namely had some one-off cost that have caused the external supplies and services. I would say that personnel costs continue to be on their normal trend. And the other O&M and normal costs that we have in Portugal also continue to be on their normal trend.
The other cost that I would (inaudible) to have some additional cost in our terminal that this is also driven by the fact that we have been using the terminal at full capacity. So actually this is beginning of the year we normally -- the normal year would be to use more of the gas from the pipeline than the terminal; we are using more of the terminal than gas from the pipeline. It's a high gas consumption year here in Portugal and so that has driven both results and cost at the terminal, but so it is not a cost that is incurred without revenue on the other side.
So that's what translates into debt increasing core OpEx. You also see that in the noncore OpEx there's some increases namely in the ITC mechanism because of the export of electricity, but those are completely passed through. That's in slide number 8.

So moving to slide number 9, you can see that EBITDA, as I saw, and this is just summing up it's growing 2.1% basically driven by the evolution of the rate and also a little bit already by the impact of Electrogas. It's still not material at this point, but already accounting for something at this stage.
Looking below EBITDA, what I can say is that depreciations, as usual, are pretty much in line with expectations and the evolution of the asset life, so nothing very new there. Tax is already also very much in line with our expectation, so effective tax rate is around the 27%, 28% that we are always at. And the financial results, you see that good evolution. So there's a strong decrease versus the first quarter of last year.

And we can look also at slide number 11 where you see the evolution of net debt. So basically what you can see here is that on one side you have net debt going up by around EUR66 million. Given the fact that the Electrogas acquisition was actually EUR168 million you see that there was other positive impacts. There is nothing very strange. The fact is that we have incurred in previous years some tariff deviations and now we receive them.
So it's I would say the normal business.
As you know, this creates some fluctuations on the working capital, and so we are actually receiving some of this money that was [owned] to us.
And now in the first quarter, and we have a little bit less expenditures also on the CapEx front that we had made at the end of the year, and that explains this good performance in terms of evolution of net debt.
In terms of the average cost of the debt and who already give you a little bit of visibility. This is mainly driven by the renegotiation that we did and the refinancing last year, specifically the one related to the retail bonds. You did not see that fully on the cost last year, so on those 3.2% that you have last year, but you see that fully now reflected on this 2.6% comparing. And so that's basically what explains apart from other smaller issues. So it is not expected that you will see a big improvement, so I think that this is the cost that the main impact is something from last year. So this is in line with what we would expect. And then we will see how the refinancing goes in the next few months driven by the acquisition that is being concluded.

So looking at slide number 12 and summing up, you have positive impact from EBITDA, positive impact below EBITDA. So it translates -- given the low net income because of the full accounting of the levy in this quarter, it translates into a very large improvement. Of course this year-on-year improvement is not to be replicated for the next quarters, but I think it indicates a good strength for the full year.
So in conclusion, and just to mention to you very briefly, the only thing that we can add at this stage, but then you can ask away on the EDPG transaction, is that all of the regulatory and legal approvals are underway, both the ones that were pushed by REN and the ones that were pushed by the seller, by EDP, so they are all underway. We still do not have visibility when they will be concluded because it is not possible to do so.
So you can ask us a little bit more about that, but we will not be able to give you any definite date. Everything is going according to plan, so I would say that there is no concern. But we are still waiting for what comes out of it.
We have been setting up everything for the capital increase that was duly approved yesterday, but we are working hard on all of those fronts, namely in preparing the operation itself and talking to investors and preparing the prospectus. So everything I'd say is on schedule on that front.
So let's wait to hear from these approvals to then give you a little bit more information which we don't have as of now.
I would only [add], if you don't know, that both Moody's and Fitch have already reaffirmed our investment grade rating. It was not still the timing for S&P as they do their review normally at a later stage. We do not expect any bad news on that front, but I think that we managed very proactively all the rating agencies but, we are still waiting for that one.
Finally, just to reaffirm -- as you saw, we approved also the payment of the EUR0.171 per share of dividends for this year, which gives a very nice dividend [on yields] of around 6%. So that concludes our presentation and I would open and welcome any questions that you would have. Thank you.

Q&A

Sara Piccinini - Mediobanca - Analyst
Hello, good afternoon and thank you for taking my questions. I have a few. First one is on the contribution from Electrogas, should we account for Electrogas at the EBITDA level rather than at the equity line? And how much is the contribution that you expect by year-end since it is now EUR1.7 million should be in the region of EUR5 million let's say is the first question?
Second question is where do you see the cost of debt by year-end? Is there any out-performance in the cost of debt reduction for this quarter?
Finally, I know that you can't give timing on the authorization, so just to have an idea how many authorizations are you waiting for? And if we can assume that after the competition authorities most of the tough part is done? Thank you.

Gonçalo Morais Soares
Hi, thank you, Sara, for your question. So the first one, yes, you should expect seeing it also at the EBITDA. As you know, we are doing it accounting wise through the equity method but presentation wise and at the EBITDA level. Because, as you know, EBITDA is an indicator which for the auditors is something which they care a little bit less about. But at the EBITDA level you will also see us in our presentation putting at debt level. So this is what you should expect is to continue to see this being presented in terms of results as it is being now.
So secondly you asked about the cost of debt. So yes, we are expecting, as I told you, that this cost that you see now is basically already reflecting the full impact of the refinancing of last year. So we have a little bit of refinancing being done this year.
So depending on the timing of that refinancing, and this is mainly tied to the acquisition that is being approved, you can have a little bit more, a little bit less. But I would not think that it would deviate from what we are having now. So if you want to take a number take the number that you have for the first quarter; I would assume that it's going to be pretty close to that.

Rodrigo Costa
On the last question regarding the authorizations -- well, I think we are disclosing as much as we can at the moment. I would say all the process should be quite simple, but regulators are the regulators and it's not -- it doesn't really benefit the process if we put too much pressure. For sure we are doing all we can. I think we presented our cases quite well.
We discussed this beforehand. We are not expecting any surprise, but the timing for the regulators, it's something they manage. And it can always be a little bit slower or a little bit faster. I would just say that we are expecting to close the operation until the end of the third quarter of this year and this is all we can say at the moment. We are not expecting any big issue because we really did our homework before moving into the deal.

Sara Piccinini - Mediobanca - Analyst
Thank you.

Catarina Afonso - Intermoney - Analyst
Hi, good afternoon. I would like to ask if possible for you to repeat the explanation of the operating cash flow, because it's a big number compared with one year ago. I heard it was relative to tariff deviations, but this only explains around EUR60 million of this big number. Thank you.

Gonçalo Morais Soares

That's exactly right. So additionally to, I would say, that impact that you see, so if you compute back you would have an impact of EUR100 million that it will be going down. Of that decrease around 60% is driven by tariff deviations and the rest is by I would say normal evolution of working capital.
So sometimes we try and anticipate a little bit more CapEx at the end of one quarter versus the other. Sometimes we receive some money from our main customers, and I'm talking about EDP or Galp and it varies according to some quarters. And so sometimes things converge on a single quarter.
So everything I would say on the longer term, apart from the deviation, should be very flattish or you shouldn't really see a lot of working capital.
Unfortunately this tariff deviation mechanism creates both here on the [debt] level and also on the interest received [in place] at the P&L a little bit of fluctuation. This is the mechanism that we have and we've been having them for a very long time and so that is the explanation.

Catarina Afonso - Intermoney - Analyst
Okay, many thanks.

Sara Piccinini - Mediobanca - Analyst
Yes, thank you, sorry. If there are no questions I will add one more maybe. On the regulatory view for the electricity, is there any update with the regulatory? Should we expect a consultation document before the summer or should we speak to the date of October? Thank you.

Gonçalo Morais Soares
Yes, Sarah, that's exactly right. So I think that, as I said, we have in place. So João, that is here, and this team is going to start to engage with the regulator now in a few weeks in the normal fashion. And then in October 15 we will have the draft. And then in December 15 we will have the final decision. I don't know, João, do you want to add something?

João Conceição
Just to add that typically the regulator sets a public consultation on the new regulations, which we are expecting to happen before the summer, I would say mid-June, beginning of July. But this is a date that it's completely flexible and the regulator has no formal date. The only one that he has to comply with is the effects of really what Goncalo has just said, which is October 15.

Sara Piccinini - Mediobanca - Analyst
Many thanks.

Catarina Afonso - Intermoney - Analyst
Hi, hello again, sorry. I just have a question regarding Electrogas. What type of dividends should we expect on an early basis? Thank you.

Gonçalo Morais Soares
The impact in terms of net income, let me check; I want to give you the exact value of the full-year impact, but it was around EUR3 million, EUR4 million. I can give you the -- around EUR4 million in terms of net income full-year. But I can give you -- let me give you the exact number. So net income should be around those EUR4 million I would say.
So we have a little bit more dividends coming from the Company that we have a little bit of financial cost being paid also at the hold debt financial company. So at the end of the day, but at the EBITDA level that's it. But on the net income it's around EUR3 million to EUR4 million.

Gonçalo Morais Soares
Let me just add one issue that Ana was pointing to me out here in relation to Electrogas. That EUR3 million to EUR4 million impact to net income has in there a one-off, which is the cost relating [EUR1.1 million] something relating to the transactions which are one-off. So on our run rate we would -- from the operations we would actually have a EUR4 million to EUR5 million kind of impact on the accounts, okay? I hope that helps clarify the issue that you asked. Thank you.

Rodrigo Costa
Well, I believe we have no further questions and, to be honest, we were expecting a few questions today. But in fact we have been communicating
also a lot and we always have Ana providing a lot of information and we are always available. And thank you and we will keep in touch.