

Company Name: Hera
Company Ticker: HER IM
Date: 2019-03-27
Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
Current PX: 3.24
YTD Change(\$): +.578
YTD Change(%): +21.713

Bloomberg Estimates - EPS
Current Quarter: N.A.
Current Year: 0.190
Bloomberg Estimates - Sales
Current Quarter: N.A.
Current Year: 6138.000

Q4 2018 Earnings Call

Company Participants

- Tomaso Tommasi di Vignano
- Stefano Venier
- Luca Moroni

Other Participants

- Javier Suarez
- Roberto Letizia
- Emanuele Oggioni

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon. This is the Chorus Call operator. Welcome to the 2018 Financial Results Presentation of Hera Group. All participants are in listen-only mode. Following the initial presentation, there will be a Q&A session. [Operator Instructions]

And I'd like to give the floor to Mr. Tomaso Tommasi di Vignano, Executive Chairman of Hera Group. You have the floor.

Tomaso Tommasi di Vignano

Good afternoon, everybody. We are a little tired after a long board meeting, but here we are ready to present our group's results for 2018. The fundamental points that we would like to highlight in our introduction refer to the very many things done during the year. We concluded a few M&A transactions, which for the most part were focused on the energy sector. But also in the market region, we also completed a merger with a company, which owned a good portion of the gas networks in the Pesaro province. All of this happened in Q1. In Q2, we continued to work with our usual commitments with a specific focus on the position that we are gaining on the topic of sustainability with a view to expanding within our company, a special focus on sustainability in various sectors which also allowed us to receive international recognitions of a significant kind. And also as far as obtaining credit is concerned, we were able to work on the innovative initiatives, which were also then implemented by other players.

Q3 and Q4 were marked by a number of opportunities, especially as far as partnerships are concerned. One such partnership was with Eni to manage the use of vegetable oil collected through sorted collection. The second partnership is with the Bio-on company to launch and then produce bio-plastic. A third topic, which is entirely different in those same quarters was a contender we were awarded in the Waste sector to clean up the Chioggia port in the province of Venice, which is certainly a very important operation. And then, as far as the tenders are concerned, both for the gas market and the electricity market, we reconfirmed our position in these client segments because for the third time, we were awarded the

Salvaguardia & Default markets, allowing us to hold on to a sizeable presence in these sectors. Also, as far as the tenders are concerned, this goes to show that if we look to the past, we weren't very used to competition at these types of transactions. But with the liberalization of markets, we were able to promote a certain kind of a culture which was

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

then also followed by some of our colleagues. And therefore, in some sectors in which we used to have difficulties, we have now been able to achieve positive results. Such as, for instance, in the public lighting sector where, as you know, we are the second largest Italian player after Enel. And even this year, in fact, we were able to increase the number of our public clients.

And finally, I'd like to mention the fact that also in Q3 and Q4, the very first biomethane plant was started, a plant that we built so close to Bologna with a fairly important size. And then at the end of the year, as is usual for our company, we focused on drafting and then launching our new Business Plan to 2022, which we then presented to the market during the month of January and early February. And we are quite satisfied that we were able to continue with a very important tradition of ours. The roadshow was very important, also given the number of investors we met and we met over 100 investors during the period. And I'd also like to mention the fact that as an award when we returned home, we finally were able to enter the main segment of the Italian Stock Exchange FTSE MIB index. From that moment on also given the increase in the volumes of trades, we were finally able to obtain these important results, which is extremely gratifying even in the more recent days given the way our stock has been performing.

Moving on to our operational results. As you can see on page 2 of the presentation, we posted a good performance from a number of different profiles. And you can see the comparison with the previous two years. As you can see in terms of EBITDA, our growth was equal to 4.7%, allowing us to reach a formal target, which is important which we are proud of because, as promised, we were able to achieve €1 billion in EBITDA. In fact, we even went above our forecast for the end of the year, which we had talked about at the beginning of the roadshow.

Moving on to our net profit even here we are even more satisfied since our growth was equal to 12.1%, closing the year with a net profit equal to €282 million.

The third element I'd like to refer to which is equally important is the net debt to EBITDA ratio performance – something that as you know we pay close attention to which once again allowed us to improve our performance in 2018 compared to 2017. We stand at 2.5 times at the end of 2018.

And finally in terms of guaranteeing transparency vis-à-vis what we had announced during the business plan presentation, today the board has confirmed the forecast included in the business plan according to which for 2018, we will be paying €0.10 per share with a growth which therefore had already been illustrated the previous year.

Now, these good results are based on a very good operational performance, first of all, which has an impact on our P&L all the way down to the bottom line with a very good growth in our net profit. And as far as the latter is concerned, we also counted on the good tax and financial optimization. And as far as taxes are concerned, the government's actions contributed to this result allowing us to achieve these figures as far as the earnings per share are concerned, it grows at – by €0.192, which is also significant. Our cash flow was able to fully cover our investments and dividend payments, whereas the developments for the – or the investments for the development of plants and M&A despite it being limited as far as the financial impact is concerned over the period that brought about a total increase equal to €63 million, which means that our financial soundness has improved based on the ratio I mentioned. And also the other items were covered with a very limited growth in debt. We presented the figures to our board today and as I already mentioned, we also approved the increase in our dividend as I mentioned earlier.

Moving on to a topic which we always try to cover during our presentations. In other words, how we stand today when we are drawing the final figures for 2018 compared to the business plan covering the years to 2018 which was drafted in 2014. And just as a way of offering a form of continuity to our work and also as a way of underlining our ability to forecast things and to show how closely we are to our forecast and our execution. If you turn to page 3 in the presentation, you have a comparison of the results which – and all of the graphs you can see here are in-line or above the forecast we had included and the business plan which ended in 2018 and which was drafted in 2014, which goes to show how reliable our forecasts are and it can certainly be a way of guiding us in our future activities.

As far as EBITDA is concerned as you can see, we were targeting a result at year-end 2018 equal to €1.02 billion. We now stand at €1.031 billion, which is very much in-line with our forecast. The results were even better in terms of net profit. We also performed well in terms of having a satisfactory net debt to EBITDA ratio.

Company Name: Hera
Company Ticker: HER IM
Date: 2019-03-27
Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
Current PX: 3.24
YTD Change(\$): +.578
YTD Change(%): +21.713

Bloomberg Estimates - EPS
Current Quarter: N.A.
Current Year: 0.190
Bloomberg Estimates - Sales
Current Quarter: N.A.
Current Year: 6138.000

And, finally, as far as dividends are concerned, we made the choice which was confronted by the board given the fact that we have all the necessary elements to continue increasing our dividend policy as a form of remuneration for our shareholders. These are the more significant elements on page 3.

And I'll let you briefly move onto a summary of the elements which brought about our EBITDA growth, which between 2017 and 2018 was marked very much by the Networks performance with a €40 million growth. This was certainly due to an increased concentration, but in our structure as you know this is a sector in which we concentrated most of our investments on, therefore it would be negative where this kind of result not to be achieved.

As far as Waste is concerned, despite having some difficulties especially in terms of the availability of landfills which were a part of our traditional array of assets you're all familiar with, we did have some difficulties because two of the landfills included in their regional wasteland due to a number of reasons encountered more difficulties than expected in terms of obtaining the necessary authorizations. This is a complex process which was completed for one of the two landfills mentioned, whereas for the second one we hope to be able to count on a ruling that can allow the landfill to be up and running again.

In any case, the results of the Waste sector, also taking into account the increase in prices which continued for special waste. Throughout 2018, as you can see despite the negative elements, we were still able to post a positive result as far as growth is concerned.

Moving on to the market, even here we were certainly able to maintain our position. As far as the Salvaguardia & Default tenders are concerned, which I already mentioned, we increased the number of our customers significantly. We now stand at 2.5 million customers which is what we had programmed in the business plan, which means that even here all of the elements we are looking at are comforting vis-à-vis our forecasts.

And due to the reasons I mentioned earlier, we also had a good performance in public lighting. And then the TLC sector, despite it being a smaller sector, a smaller business for us, it did contribute nonetheless to the column marked as Other which is worth €7 million. The only negative elements in all of this scenario is due to some negative factors in the electricity generation sector in which, per se, as you know isn't an especially relevant part of our portfolio. Plus throughout 2018, there was a concentration of periods during which the service was suspended, which we have not overcome but it did have an impact on production throughout the year.

I think this is the only thing which in fact had a negative impact on our results, whereas everything else is very satisfactory which again confirms the importance of the regulated businesses but which was also marked by positive performances in the liberalized businesses in Waste and in Sales & Trading.

Finally, a point of view we'd like to share with you on the topic I just mentioned namely organic growth which was a major part of the results posted. As you can see here, we tried to breakdown the various components within organic growth to further clarify the way in which we were able to achieve the major growth we posted at the end of the year.

You can see three spots here, which show that €12.4 million in our EBITDA equal to 27% of what we were able to post, stemmed from the intensity of our investments, from the tariffs which were especially positive in the Waste sector and also due to the premiums we were awarded for the very first time in terms of the quality of service which was a major recognition.

The second diagram refers to the market tenders I mentioned earlier and the growth of our customer base. The growth of our customer base was very important throughout 2018, because as you have seen in our new business plan, we are now targeting 3 million customers, a figure we hope to achieve as soon as possible in the various components which have allowed us so far to allow these figures to grow constantly.

The third item, which is also something that we are very familiar with is our ability to obtain efficiencies which was further enriched by the component which used to be less visible in the past. This is a general term and I'm referring to innovation – being able to innovate and the types of businesses that we have always focused on by joining forces and by continuing to rationalize our strengths is something that we have always focused on, whereas now we are also focusing on technological innovation, all the more so compared to the past as you know, which makes the entity of

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

efficiencies even more interesting, efficiencies which are no longer based on our organizational efforts. They are now very much linked to technological innovation per se. I think these are the ingredients which justify an almost €50 million growth organically, which we are always very pleased with.

And I'll give the floor to you Stefano now.

Stefano Venier

Good afternoon, everybody. Let's go into the various business areas, page 6. I think the very first element I'd like to focus on is the balancing between our businesses. We had a higher amount of regulated activities, as a consequence of a very good performance the Chairman was commenting on especially concerning our Networks performance, and all of those businesses which are a fully regulated, the largest of which is water followed by gas distribution. The Networks which as you can see moving on to the right have improved their performance to €464 million, a €40 million more compared to the previous year with a growth equal to 9.6%. And then we will be going into the specifics, if you go into the reasons why we have seen this increase which is maybe surprising given the fact that last year was stable compared to 2016.

Moving on to Waste. You will notice that for the third year in a row, we are continuing with a significant growth, marked by roughly €6 million. You may remember that in 2017, we also had an increase in perimeter with the Aliplast transaction which has contributed to our growth. In 2018, we didn't have any sizeable increases in our size, which means that the contribution to growth was entirely organic and as what we're seeing it stems from the industrial waste or special waste sector.

Moving on to the Energy sector, the result was equal to €286 million, slightly lower compared to the previous year. As we already mentioned, the reason for that is due to the lower performance we had in our production and generation activities which is a small portion but which does contribute to the end result and that motivates the €7 million decrease which is a part of the contraction. Part of the contraction was also offset by the development of our commercial activities. But moving – or looking back to two years ago, we did have an increase equal to €46 million compared to 2016 which means that we are still able to achieve an important result in a linear fashion.

Moving on to the business-by-business breakdown and let's begin with the most important sector, Networks which covers almost 50% of our total EBITDA. You'll notice that half of the growth was brought about by water due to three main reasons: First of all, there was an increase in recognized revenues, which also includes the part stemming from our commercial quality, which in 2018 was equal to some €3 million. The second item refers to efficiencies. Earlier, we were mentioning how, all-in-all, our efficiencies contributed to €15 million growth; half of that growth came about from the Networks sector roughly €8 million. And finally, this refers to a one-off component. We have some €6 million we were able to recover from previously standing situations recognized by Authority during the 2018 year, which we were able to recover [ph] of over – (00:24:16) to previous years.

Moving on to the gas sector, even here we have been able to mark a significant growth worth some €10 million, allowing the gas distribution final results to be equal to €261 million out of a total of €464 million. These further €10 million once again stem from the following ways: €2 million from recognized revenues; in this case due to the investments we made in the previous period; further €4 million came about through efficiencies bringing the grand total of efficiencies to €12 million in the Networks sector, plus a number of other items, white certificates and others.

Furthermore, in electricity distribution, we had a €5 million growth. Even in this case, 50% of that growth was due to recognized revenues and further €2.5 million due to efficiencies and other items. All-in-all, the Networks sector contributed to efficiencies with almost €15 million.

Finally, district heating. The thermal season was a good one. We were able to promote certain efficiencies and innovation initiatives, allowing us to improve the optimization of the systems we manage and their performance, allowing us to improve the results by €6 million, so that the grand total EBITDA in district heating is equal to €16 million within the €464 million at €1 million total.

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

Other important things to note as far as these businesses are concerned we have the RAB value of the three businesses we are considering, equal to €3.1 billion with a slight growth compared to the previous year. As far as the gas tenders are concerned, as you know and as we mentioned during the business plan presentation, the tender in Udine 2 is happening within our territory. This is a very first field test that we are dealing with as far as the tenders are concerned.

Initially, the offers had to be sent in by February. This deadline has been postponed to May and we'll be seeing how that goes. Finally, as I mentioned and commenting the various business areas, a part of these results came about by the premiums we received and the quality of service I mentioned – the one for water because it is good news for 2018. But even the two other businesses, gas distribution and electricity distribution, received a positive contribution which is also the combined total of premiums and reduction [ph] and indemnization (00:27:25). Two years ago, we gave ourselves a target equal [indiscernible] (00:27:31) and we are now close to that – achieving that goal which also brought about an improvement in the overall profitability of these businesses.

Moving on to the Waste sector. First of all, at this time we wanted to underline the contribution of Aliplast equal to €1 million. The overall profitability of the business was equal to €18 million. We expect something more in 2019 because in Q4 of the year, towards the end of the year therefore we created a new [indiscernible] (00:28:21), this was in Q4 of 2018 and this will allow us to increase that site's ability to perform with obvious positive repercussions on the company's performance. But we have €11 million in organic growth. This is the sum of a number of different components, among which we have the contribution stemming from the marketplaces which grew on average by 10% throughout the year, although we had a piece which were well above that up to 20% or 30%. This contribution was strengthened by the profitability on the production of renewable electricity, which benefited from the price dynamics we had in 2018. Although its positive effect was eroded by the lower volumes we were able to manage due to a limitation on the ability to dispose of waste and that was equal to some 100,000 tons over the year. This is, of course, removed a potential business, although compared to the previous year we were still able to post – we posted a slight contraction. Special waste were equal to 2.155 million tons compared to the 2.2 million tons roughly of the previous year whereas urban waste were 2.35 million tons with a plus 48,000 tons compared to the previous year, with an overall total of 4.5 million tons which were treated on the market.

As far as our plants are concerned, we already started our biomethane plant. Let me just give you some information on the waste collection sector. In this sector, we no longer manage waste collection in the Forlì city. That municipality has a micro in-house company. This is minus €3.5 million for us which eroded our growth which otherwise would have been equal to plus €10 million.

Despite all of this, we continue to evolve in terms of waste collection and sorted waste collection specifically. We now stand at 62.5% of recycling, with excellent examples such as the city of Ferrara which stands at 85% and other areas which are lagging behind especially in the mountain regions were in very specific context. We had a good performance as far as our waste energy plants are concerned. Even last year, they were able to treat 1.3 million tons like in the previous year.

Moving on to the Energy sector. I already mentioned everything, I think. Three dynamics in this sector marked a slight contraction, but not as far as our core businesses are concerned. From that point of view, we increased by €10 million given the broader perimeter on the default market in the last quarter of the year, but also due to the almost 150,000 further customers we added throughout the year; of which 70,000 came from acquisitions, the remaining customers came about through our commercial activities as we did in previous years. I already mentioned the negatives. Therefore, I will not go into further details.

We also had good performances in terms of managing our CRM. We were very effective in terms of managing our credits with an unpaid ratio, which like last year stands at around 1%, excellent efficiencies on our cost to serve, allowing us to be a part of the first quartile in the more efficient players on the market.

If we then have a look at the lines below EBITDA, page 10, we further improved our financial management thanks to a better profiling of our net debt, thanks to our further optimization on tax rates and also thanks to the good performances we had in terms of interest on delayed payments.

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

As far as the tax rate is concerned, we had a significant improvement that we'd like to illustrate in a homogeneous way here. In fact last year, we had a tax rate equal to 29.8% in our P&L, although there were some one-off extraordinary maneuvers. The real figure was 30.9%. This year, we closed the year at 29.1%, which was over 1.5% of further optimization, which means that we're looking to further improve that. This is a result that we are especially pleased with, but due to the fact that it also is the outcome of certain investment policies we made as a way of focusing on investments on innovation, which last year were well above €60 million.

The EPS, which stems from all of this, grew by €0.02 per share up to €0.192. And the ROI and ROE indicators also performed well since we improved the already excellent performance we had in 2017 by almost 0.5%.

And let me conclude my presentation with a brief focus on one of the topics that we have been focusing on over the past three years, which is that of offering a full transparency concerning the €1.03 billion, and the way in which it ties into our strategies concerning sustainable development. With the promotion of smart use of energy and efficient use of resources and innovation and development of territorial social ecosystems, and we're very pleased to say that this part of the margin is now up to €375 million. It now covers 36% of our total EBITDA. It is [ph] fairly (00:35:22) in-line with the 40% target we have given ourselves to 2022, and with a major growth compared to the results posted in 2017.

This was due to our daily activities and a number of initiatives the Chairman also mentioned such as our ability to recover vegetable oil – used vegetable oil to produce biodiesel which we didn't use to fuel our waste collection trucks. This is just an example of course, plus some careful choices we made on investments which in 2018 are equal to €186 million, out of a total of €460 million which account for 40% of our investments devoted to these areas, which means that the result we were able to post on shared value is also the consequence of our policies. It is also the consequence of some milestone results we were able to achieve that were very important and we're quite pleased to say that over a four-year period, we were able to reduce our energy consumption by 4.4% and we are now in a reach of the 5% target. We have reduced our carbon footprint compared to 2015 by 16%, and we've already reached this year another result referring to the directive on the EU Circular Economy, which means that after the [ph] run of the use of (00:36:52) landfills and this year we have a lower percentage compared to the previous year equal to 5%, the recycling rate of our packaging which is now up to 70%, which is the target defined for 2030. And I could continue but you could find all of this information on our sustainability budget presentation.

Let me give the floor to Luca for some financial information.

Luca Moroni

Thank you. Good afternoon. We had an excellent performance on our operational level, over €700 million allowing us to cover and operational investments worth almost €400 million. The operational cash flow was equal to €200 million, thanks to the excellent work done, both in terms of our financial management and also in terms of taxes as it was already mentioned, especially as far as the tax rate is concerned. You may remember that we're able to extract the most value possible by taking full advantage of the rules of the past two years' financial laws, especially on the topic of Industry 4.0.

We were certainly one of the companies to take the most advantage from this opportunity. The networking capital was equal to some €70 million, which was what we had communicated at the end of the year. And €70 million were used to pay the dividends and to invest on development CapEx. Buyback was worth €26 million and then we also used up €22 million for the M&A transactions we mentioned. These investments implied a slight increase of our net financial position equal to some €60 million so that the [indiscernible] (00:39:08) was equal to [ph] €2.185 billion (00:39:12) with a net debt to EBITDA ratio, which is still improving and that's under 2.5 times as you can see on page 13 with with an FFO to net debt ratio [indiscernible] (00:39:30) 27%, which allows us to be in the best position in our discussions with the rating agencies and with a financial profile which is always very cautious, given the fact that our average duration for our debt stands at around seven years, with a fixed interest rate equal to 85% of the total.

At the end of the year 2018, we signed credit lines committed, [indiscernible] (00:40:11) €350 million, allowing us to hedge ourselves with the volatility we saw in those few months. Also, given the fact in 2019, we do have the expiry of

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

a bond worth roughly €400 million, which means that we're closing the year with an excellent financial profile and with an excellent cash flow generation.

I think we can conclude our presentation, and we can open the floor to your questions. We are certainly satisfied with our closing figures for 2018. We're very proud it is a solid result marked by constant activities and constant efforts. With a forecast as to our net debt to EBITDA ratio, which is very comforting. And it allows us to consider any possible future opportunities as we mentioned during the roadshow for any possible M&A transactions.

We can now open up the floor to some Q&A.

Q&A

Operator

The Q&A session can now begin. [Operator Instructions] The first question is from the Italian conference call, Javier Suarez, Mediobanca.

<Q - Javier Suarez>: Good afternoon, everybody; and thank you for your time. The first question refers to the EBITDA [indiscernible] (00:42:26) divisions for 2019. I'd like to know if you can help us understand the dynamics for 2019, given the major growth in 2018. Which dynamics do you have in your main divisions, beginning with Networks, slide number 7.

The €464 million EBITDA, you mentioned there is a €6 million one-off, and you also mentioned the premiums. And I was wondering how much of this should be considered as one-off? Do you think, this figure, the €464 million will continue to grow in 2019, and if so, why?

The second question is on the waste management business. In this case, organic growth was significant, slide number 8, €11 million. There's a strong growth in prices, of course. In this case there is no valuation perimeter. And next year, you will have the new plant online, which should also bring about significant growth. Will this growth in Waste accelerate due to your larger capacity? And will the prices continue to increase? [indiscernible] (00:43:46) one-offs involved here. Is my interpretation correct?

And as far as the Energy business is concerned, slide number 9, this year was marked by a slight decline due to the reasons you've explained. What are the dynamics for 2019? What are the more significant elements? Is this figure flat? Do you expect growth or a further decline?

And the final question is the contribution to EBITDA per activities. I noticed a €28 million growth, a significant growth compared to last year. Is this figure sustainable for 2019? And which growth dynamics do you expect for 2018 compared to 2017?

<A>: Can you please repeat your last question on the €28 million?

<Q - Javier Suarez>: The €28 million you were mentioning should be the contribution of other activities to EBITDA, not waste, not water, not gas, not electricity. That growth implies a growth compared to the 2017 figures. Are these €28 million sustainable in 2019? Are there any other one-off opportunities we have to consider?

<A>: Let me begin by commenting the regulated businesses. There have been some extraordinary operations or one-off opportunities, but as usual, we do not consider a contraction in 2019. In other words, we see elements, which allow us to consider that our performance will be better compared to the €464 million. Let me explain why.

In the water sector for instance, we were having further contribution from tariff contributions. Given the fact that we are abiding with the quality technical quality, we expect to achieve a further €3 million to €4 million on top of the commercial quality we already obtained. And we will continue with our efficiencies activities.

As far as the gas and electricity sector, there, the results are a little bit more stable. All-in-all, we're looking at a result, which will be better than the €464 million, which means that the growth there will be equal to €5 million to €10

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

million.

As far as waste is concerned, it is true that prices are holding, we don't see any dips in prices. Although the revenues will be slightly lower on electricity, because as you know, the market prices have dropped, so that may have a negative impact worth a couple of million euros. And then, we'll also be having the contribution of the biomethane plant, which we expect will contribute a further €5 million to €6 million on a yearly basis. And all of this, therefore, we just expect a further improvement in the results and the €252 million we posted this year.

As far as our sales are concerned, this is a little bit more complex. As you know, compared to 2018, this year, there was a special contract in the Salvaguardia market. The new two-year period has begun with conditions that are less favorable compared to the previous ones. As we mentioned during [ph] business time (00:47:50) presentation, the effect of the Salvaguardia market will be marked by a €40 million contraction in EBITDA that we have obviously equipped ourselves to try to offset that decline. And therefore, the goal we have given ourselves internally is to reabsorb that figure entirely. In general terms, if we look at the various businesses, therefore, in 2019 we expect a result, which will be above the €1.03 billion we achieved in 2018.

And then, a final comment on the other activities you mentioned, district heating and TLC. Yes, the result is sustainable, and actually, in both of these businesses we are, in fact, seeing excellent results even in 2019. Last but not least, just to give you an example, the offers for the [indiscernible] (00:48:58) public lighting tender were opened. And we were the best both technically and economically, which means that this will be a further building block in further developing the public lighting sector, which is becoming an important business for us. Also, because it represents one of the essential elements in terms of developing the smart city solutions, which are now a part of an offer that an innovative utility has to have. That's interesting.

<Q - Javier Suarez>: And just as a follow-up question, I noticed the contraction in taxation from 29%. If I remember correctly, in the recent Business Plan, you were indicating 30% for the Business Plan years. The 29% that you were able to obtain as taxation in 2018, is that sustainable going forward, or is it a one-off?

<A>: Well, we tried to take advantage beforehand, as Mr. Moroni was saying, of the Industry 4.0 options, which means that we will be able to sterilize the 4.0 program review, which is being made with the current government. But this year, we count on defending 29.5% or 29.7% tax rate. Moving forward, unfortunately, starting in 2020, we will be paying slightly more, going back to the 30% we indicated in the business plan, since the government reduced the incentive mechanisms on the Industry 4.0 program, which will allow the tax rate to increase by 0.3% or 0.4%.

Operator

The next question is from Enrico Bartoli, MainFirst.

<Q - Javier Suarez>: Good afternoon. I have some questions for you. The first refers to the trends in Q4, especially in the gas and electricity businesses. It seems to me that there was a reversal in the trends compared to the first nine months, especially in gas. The growth equaled to [ph] €10 million (00:51:28), whereas EBITDA dropped in Q4. And there was a contraction in first nine months in electricity, whereas there was a major recovery in Q4.

Can you help us with some further details as to the drivers in these two inverted trends? Especially in gas, it seems to me that there was a positive effect stemming from the default market, which is something that I believe you quantified as equal to €5 million. Can you confirm that figure, its contribution to EBITDA in Q4?

Second question on Energy, and on electricity, specifically. This year's indication was that the €40 million of reduction from the Salvaguardia market will be recovered elsewhere. What will be the drivers behind the recovery? I imagine an increase in your customer base or in volumes, but what about in terms of sales margins? Do you expect an improvement throughout 2019?

And then, a final question on the water sector. Can you give us some insight or what your expectations are on the dagga law, and how it is doing in Parliament? I think the Emilia-Romagna regional government took a firm stance against this

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

bill. Do you think the fact that the industry is speaking out against this proposal can bring about significant changes in the initial bill?

And one final question, can you refer to the cost of debt for 2018, and what you expect for 2019?

<A>: Beginning with your question on gas, in fact, the thermal season was quite good in Q4 2018, especially. Nevertheless, "we had a reduction in profitability" and due to the fact that in 2017 we had received a sum at the end of the year, which was a one-off contribution equal to some €10 million, which explains the difference you see on a quarter-by-quarter basis." There are no other reasons. That one-off was an amount of money, plus a fair value effect for the end of the year, which means that we had very good results in Q4 2017, whereas Q4 2018 was more organic, so to speak.

As far as electricity and the Salvaguardia effects are concerned, well, I mentioned that our ambition – or our target is something you may be taking for granted in terms of our duty to reabsorb everything. We certainly want to reabsorb most of these effects. Of course, we would be more than pleased to reabsorb the entire figure.

And how can we achieve this? Well, first of all, from the volumes delta, because on the liberalized market, at the end of the campaign, we were able to increase our customer base and volumes. We were also awarded some [indiscernible] (00:54:55) tenders nationally, which was also – increase our presence in that business. We will also be benefiting from the continuation of the development of our customer base.

And then, in the gas sector, the sector will help us to compensate from the electricity sector. And then gas, we will have some further margins. Therefore, in the energy sector in general, we will be able to pretty much offset things. But let me just be clear, I was referring to the energy sector in general and its ability to reabsorb the Salvaguardia effect. I wasn't referring to electricity sales alone.

Then you also had a question on the cost of debt. Net-net, it was worth €3.7 million, which is a figure we expect to have moving forward. And then, there was a question on the dagga bill. Well, what can we say? As you may have read in the news, originally the bill should have been submitted to Parliament on March 25. That has not been postponed to a future date to be confirmed due to the fact that the President of the Commission had asked the [indiscernible] (00:56:29) for some technical reports, as a way of assessing the sustainability of this bill. And these reports still haven't been drafted.

Of course, the most important technical report is the one drafted by the Ministry for the Economy and Finance (sic) [Ministry of Economy and Finance] (00:56:43), which as you know, the effects of this bill will have major financial implications. This has also stopped the discussion of various amendments to the bill for the time being. The ones which have been submitted are significant, and many of which were also submitted by the league parties, which is the [indiscernible] (00:57:09) government.

And then, concerning the various opinions, or the way in which stakeholders or the industry has spoken out, including [indiscernible] (00:57:29), but not only. As we already commented in the past, all stakeholders agree on a negative opinion or a complete refusal, as we saw in some cases, but not so much the Emilia- Romagna regional government. Governor Bonaccini was working as the President of the state regions conference, which meaning he spoke on behalf of all Italian regions.

And in fact, during the audition in the commission, the Governor of another region had attended, not Mr. Bonaccini, as a way of showing that their opinion was shared by all of the Italian regional governments, regardless of their political party belonging, which means that so far, we have been seeing some doubts and the not very positive opinions on this bill among all stakeholders. And this of course, is slowing down the bill's presentation to parliament and its possible discussion and vote.

And in fact, even the honorable [ph] dagga (00:58:59) is starting to understand that, that the bill, as it is, cannot be sustainable. So, much so that even she said last week that she was submitting a bill that she had proposed 8 to 10 years ago. And she said, in the meantime a number of things have been changed and therefore she, too, feels that the bill has to be reviewed. I think that is a major admission on her part.

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

Operator

The next question is by Roberto Letizia, Equita SIM.

<Q - Roberto Letizia>: Good afternoon, and thank you for your time. I'd like to go into the Waste business. I seem to understand that in this first part of the year, you aren't seeing any further significant increases in the price for waste treatment, do you think this is a transition of sorts? And do you think there can be a potential worsening of the imbalance in that treatment capacity, and therefore, an increase in prices, or do you think we have now reached a stable level?

And then, do you expect any possible EU decisions as a way of having a positive impact on pricing investments and the treatment capacity of the waste sector? And can you also remind us of how much benefit you can reap from the PET cleaning plant in Aliplast? And what other possible options Aliplast has on the market? Are you looking at building further biomethane plants in the upcoming years?

The final aspect as far as Waste is concerned, the DCO, the consultation document presented at the end of last year, not that you've been able to read through it, but do you have any comments on the document? Do you see any possible risks on the RAB assessment for treatment for instance, which may potentially have an impact on a decline in the RAB over the years?

[indiscernible] (01:01:19) is pretty different from distribution. There may be a significant decrease in RAB due to amortization. Is this a possible risk when it comes to defining the regulation? And then, I have a couple of other questions if possible. As far as the weather is concerned, is Q1 having an impact on consumption, especially as far as gas and heating is concerned? And a final more technical question. Can you give us some insight as to the impact of the new [ph] REFS (01:01:53) on the group's P&L this year?

<A>: Let me begin with your last question, which is the easiest to answer. The impact we will be having on the [ph] EFRS (01:02:08) concerning the leasing contracts and the operational contract, et cetera, will bring about an impact on the [ph] PSN equal to €90 million (01:02:20), and an impact on EBITDA equal to €13 million. These are the two effects we'll be seeing on the 2019 figures.

As far as the impact of weather is concerned, of course, we are seeing an impact. There has been a contraction in volumes. And you can read this statistics on the Energia daily. January was a good month. It was even colder compared to January 2018, which means we sold something more compared to the previous year, as February and March were a lot warmer. And this of course will have an impact.

But of course, once we measure things, as far as our company is concerned, in terms of volumes sold, we will be seeing the effects of the larger presence in the four markets, which we did not have in 2018. And that will help us offset part of these lower volumes. I still don't have updated figures till yesterday. The most recent figures I have referred to, late February. At the end of February, we had reabsorbed the weather effects, whereas in March, it will be a little bit more complicated, but nothing too dramatic.

As far as the waste prices are concerned – well, as far as prices are concerned, we don't see any criticalities. And it's difficult to see any possible problems in a country such as Italy, which doesn't have the amount of waste treatment plants it needs. We had good results over the past two years. Apparently, the prices haven't declined. I don't know whether or not, if this phase will continue to improve further. But of course, the reasons which brought about this increase in prices still exist, because no plants have been built and their quality hasn't been improved either.

And just to give you a further element, we are negotiating for a plant to add to our landfills, which I mentioned earlier, which means that we hope to be able to increase that number, which will be in line with the figures included in the regional waste plant that will be in the waste regional program. This will be our contribution, but of course as our Governor says, we have to look to our own business. We should stop looking at other regions, who still haven't built their own assets. That's my point of view.

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

As far as new biomethane plants are concerned and the regulatory risks – as far as biomethane is concerned in our Business Plan, the one you're familiar with, we had already included the intention to build the second biomethane plant throughout the Business Plan years, besides the one that we are already running currently. That refers to the Business Plan. But then of course, as we do have this opportunity opened to 2022, we're seeing, we don't know if there can't be other further possible opportunities for third-parties.

As far as the TCO is concerned, we are currently reading through it. As far as the way in which the RAB will be evaluated. If I understood correctly, I don't really share your concerns. Treatment plant have a technical leverage, which is fairly long, therefore I'm not expecting a dip or a consistent – or major dip in their value. Plus, these plants can be technologically upgraded as a way of improving the quality of the outgoing product, allowing us to hold onto the value of the plant itself.

Think of the selection of plants and of the new optical and AI systems to identify the types of materials, or think of the organic treatment sector and the new biomethane wave, which can in fact be an upgrade compared to the traditional biodigesters that we had built to produce renewable energy. These are the two main examples of the types of assets we have in the treatment part of the business. And I hope I understood your question correctly.

<Q - Roberto Letizia>: Thank you.

Operator

The next question is by Emanuele Oggioni, Banca Akros.

<Q - Emanuele Oggioni>: Good afternoon, and thank you for your time. My first question is, can you give us a breakdown of the RAB for 2018 and the remunerated investments you made? I noticed apart from water, but [indiscernible] (01:08:24) split for gas and electricity. And then, how much will they grow? How much will the remunerated investments growing to be in 2019?

And as far as the liberalization of the electricity market – [indiscernible] (01:08:41) market is concerned, do you expect, as in the UK, a cap on margins; or how's the discussion going; or is this still too early to have an idea?

<A>: We're currently in the discussion at how the liberalization of the [indiscernible] (01:09:17) market will happen in December of 2020. I don't think the topic is essential for the time being. It's not a core element of the political debate. We have had some select meetings, but I don't have any elements to give you some technical insight on top of the things we've already said.

Regarding investments, last year, our net investments were worth €432 million, which include €130 million invested in the water sector, which will be accounted as RAB; €115 million in gas will be accounted as RAB; €123 million in electricity, which will again be accounted for as RAB. The RAB breakdown begins – can certainly give you the detailed figures, but we're looking at 1.5% in water; 1.1% in gas; and the remaining parts for electricity, for a grand total of 3.1%. And then, I'm not sure about the specific figures, but Jens can certainly provide those figures to you.

<Q - Emanuele Oggioni>: What about your growth in regulated investments for 2019? Well, our policy is to grow progressively. Our policy is to grow progressively in the regulated invested capital, which means that our current investment budget is slightly above the one we had in 2018, roughly €450 million all in all. The portion pertaining to the regulated side of the business is similar to the one we have this year. Thank you.

Operator

[Operator Instructions] Next question is a follow up by Javier Suarez, Mediobanca.

<Q - Javier Suarez>: I have a follow question on page 15, with the detail on the P&L. I'd like to hear the details between depreciation and provisions. What are the provisions you've included in your P&L? And what figures you're looking for 2019, if the figures for 2018 can be a good proxy for 2019?

Company Name: Hera
 Company Ticker: HER IM
 Date: 2019-03-27
 Event Description: Q4 2018 Earnings Call

Market Cap: 4,826.11
 Current PX: 3.24
 YTD Change(\$): +.578
 YTD Change(%): +21.713

Bloomberg Estimates - EPS
 Current Quarter: N.A.
 Current Year: 0.190
 Bloomberg Estimates - Sales
 Current Quarter: N.A.
 Current Year: 6138.000

And then on the cash flow statements on page 12. Can you help us understand the cash flow for 2019? If you could give us a snapshot on the €70 million net working capital? Where will they stand next year? Are the €70 million something structural for next year, or will they be a reabsorption, and the €50 million provision utilization. These two items in other words, what are you looking at for 2019?

And a follow-up question on share buyback worth €26 million. What was the rationale behind the buyback, and will you continue with your buyback programs?

<A>: The breakdown for the €521 million and depreciation, amortization, et cetera. €391 million are equal to amortization, €40 million provisions, and €90 million refer to the credit devaluation fund. Out of that, there won't be any major changes. As far as provisions are concerned, that is a pretty physiological level, but is also in line with the €50 million provisions you see. Of course, it's difficult to give you the exact provisions for the end of the year, but I don't think it will be any major changes.

As far as the working capital is concerned, no, we will not have any reabsorption in 2019. Also given the fact that we are still completing the realignment of all of our suppliers to a 60-day payment, which reduces our commercial debts, and as I already mentioned, on other occasions, we made a choice. As far as gas procurement is concerned, it is more internal, which means that we have moved from payment terms which used to be [ph] n+2, and they are now n+1 (01:14:26), which had an impact on working capital.

Last but not least, of course, were we to broaden the scope of the business and the default market, and were we to broaden our scope [indiscernible] (01:14:41) markets and then the supply side, we will be needing some more working capital, which means that we don't have expectations this year in terms of contracting the net working capital, which we have posted so far, which brought us around €28 million or €29 million in 2017 to the roughly €100 million at the end of 2018, which are very limited numbers in fact.

Well, the buyback is a choice that we have made. As an opportunity, we will be we remaking this proposal during the shareholders' assembly. We will be using part of this in the CMV transaction we completed last year. And as part of the trading we work on especially given that small possible opportunities we see. Thank you very much.

Operator

Mr. Tomaso Vignano, gentlemen for the time being, there are no further questions.

Tomaso Tommasi di Vignano

Thank you very much. Have a nice evening. Talk to you soon.

This transcript may not be 100 percent accurate and may contain misspellings and other inaccuracies. This transcript is provided "as is", without express or implied warranties of any kind. Bloomberg retains all rights to this transcript and provides it solely for your personal, non-commercial use. Bloomberg, its suppliers and third-party agents shall have no liability for errors in this transcript or for lost profits, losses, or direct, indirect, incidental, consequential, special or punitive damages in connection with the furnishing, performance or use of such transcript. Neither the information nor any opinion expressed in this transcript constitutes a solicitation of the purchase or sale of securities or commodities. Any opinion expressed in the transcript does not necessarily reflect the views of Bloomberg LP.

© COPYRIGHT 2019, BLOOMBERG LP. All rights reserved. Any reproduction, redistribution or retransmission is expressly prohibited.