



Results as at 30th November 2016

Bologna, 9th November 2016

Speakers:

- ***Tomaso Tommasi di Vignano, Executive Chairman***
- ***Stefano Venier, Chief Executive Officer***
- ***Luca Moroni, Administration, Finance And Control***
- ***Jens Klint Hansen, Investor Relations Manager***

Chorus Call operator

Good morning. This is the Chorus Call operator. Welcome to the H1 2016 Financial Results for Hera Group. All participants are in listen-only mode, and following the initial presentation, there will be a Q&A session. (Operator Instructions).

I'd now like to give the floor to Mr. Tomaso Tommasi di Vignano, Hera Group's Executive Chairman. Mr. Tommasi di Vignano, you have the floor.

Mr. Tommasi di Vignano – Executive Chairman

Good afternoon, everyone. We are here with the usual team to illustrate the Q3 results. I also hope you have received the material and the press release. As you can see and consistently with the first six months, the effort we have made as was mandated by a year 2016, which was -- which has been a complex year. A year in which we had to recover some of the negative impact of certain regulations, and I'm referring to events such as the reduction in WACC. And we will be discussing the amounts, and to that we also have to add a number of other factors, which also has some negative effects. Despite all this, as you can see, we were able to post the growth, as you can see on the left-hand graph on the screen. They are all positive down to the net profit, which increased significantly vis-a-vis the previous year, almost by 14%. In the year's first nine months, we also want to underline the importance of the net profit, because as you can see on the right-hand graph, the growth of this figure over the past five years has been a constant growth.

And since a few years ago, this was seen as one of the criticalities in our results. I have to say that, we have been making a major come back in all of the first nine months of the past five years. The results are good as far as we're concerned, as far as P&L and the balance sheet are concerned. I was mentioning the negative impacts, the ones which as far as regulation are concerned had to do with the cut in the WACC, plus we also had the expected expiry of a number of incentives in the renewable sector and also in the waste sector, due to the fact that the incentives for a specific waste treatment plants expired, especially the ones related to the Ferrara plant and the Pozzilli plant.

All of these elements combined along with another factor, which was an almost internal one. In other words, the limited availability in the first nine months this year of our main landfills, which is a topic we'll be going back to later, and which in the waste sector of course, had an impact in the first nine months. And therefore, as we began the year, we had to recover the figure around EUR50 million and not below that as we had envisaged from the business plan. And therefore, if we take all of these elements into account, as you can see, the efforts we made especially in terms of increasing our organic growth was a sizable effort indeed.

Therefore, by using organic growth for the most parts, but with a contribution from M&A as well, you can see that through our model we can continue to post growth despite the difficulties encountered this year, which were difficulties

we had expected. As far as the financial aspects are concerned, we have been reducing our debt by EUR85 million which is a no marginal fleet[ph], since we are now at 2.56 -- or 2.567 million. What else can we say as far as our other results are concerned.

As far as the revenues are concerned, we have a number of elements which reflect all the way down to EBITDA. The biggest impact on revenues was decreased in the energy commodity prices, which along with the reduction of incentives and the lower contribution of landfills, one of which, as I was saying, has been up and running since the month of August. It is now fully operational. And the second landfill is about to begin operations once again, since we are only concluding the more administrative aspects. And therefore, we will close the year with the second of the three landfills once more available. And as you know, last year we also strengthened our position to offset the closing of landfills, we made two landfill acquisitions in the Veneto region, where we had no such assets and that helped us to overcome the problem as you can see in the waste sector of results which Mr. Venier, will be illustrating later.

The EBITDA margin was above 19%, it grew approximately 1% year-on-year. We also had an increase in depreciation links to the broadening of our perimeter, and some of these transactions are well known since they happened at the beginning of the year. And this was also compensated by reduced provisions over the first nine months. Our financial management went very well with the production in financial costs, which was also accompanied by an increase in the benefit of minorities, by increased minority stakes.

As far as the tax rate is concerned, we went down from 38.2% last year to down to 36.5% in the first nine months of this year. And an excellent result was the net profit post minorities, which grew by almost 14%, which means that we are now at EUR142 million over the first nine months of the year.

Moving on to the EBITDA growth drivers, you can see them on page three.

We have the two negative impacts, referring to the expected reductions, especially the WACC which was the more sizable reduction. Firstly, decrease in a EUR14 million of stemming from the expiry of incentives and the PUN price over the same period. As far as organic growth is concerned, where we have to take into account our overall recovery efforts we will be closer to EUR50 million, but the truth is that here we factored in the organic growth and synergies worth of EUR39 million, since these are the ones which allowed us to more than compensate -- to more than offset the two negative elements, which I've mentioned a number of times. As far as M&A is concerned, we have completed three transactions that you are familiar with early in the year, two in the waste sector, and specifically I'm referring to the waste recycling transaction in Tuscany and the two landfills in the Veneto region I mentioned. Also in the waste and liberalized activities, we also have to add the acquisition of Julia Servizi, which is an operation we completed in the first half of the year. And we are currently defining a second transaction in the same area, which will add a couple thousand customers to what we have already obtained in the initial part of the year.

So it'll be a second transaction of the same type, referring to companies which are focused on gas and electricity sales. Plus also based on our forecast, we will be completing a further transactions within the end of the year or early next year, since we're currently in the negotiation phase. Mr. Venier?

Mr. Venier – Chief Executive Officer

Good afternoon, everybody. Let's go into the business-by-business breakdown as usual. As you can see, the waste business is stable and its results for the most part compared to the first nine months last year. This figure is improving slightly compared to what we had posted at the end of the first half of the year, and this is mainly due to two factors; the first of which is linked to the price effects that we had already mentioned when we were commenting the first half results. And especially as far as a dry waste and organic waste are concerned, there has been an increase in prices ranging from EUR3 to EUR10 based on the contracts and based on the type of waste.

This of course is bringing about a positive contribution to the managed volume, as which in the first nine months is worth a couple of million euros. Then we have a further couple million euros which are linked for the most part to an increased efficiency, which is also a way to effectively respond to the dynamics we had seen over the past few quarters, which as you may remember suffers due to the decrease in electricity prices on one hand and on the end incentives on the other, which combined over the first nine months of the year has equaled minus EUR14.5 million. The Executive Chairman already mentioned our acquisitions, as you can see the results on the quarter are worth 10.5 million. And this isn't simply in line with our expectations and it even exceeds our expectations, especially as far as the waste recycling company which we made the acquisition of in Tuscany, which is integrating in a very swift and effective way into our system, but it is also further expanding its perimeter of activities especially in Tuscany.

You can see that in terms of volumes, we have posted an improvement vis-a-vis last year where it's of 270,000 tons, which is related for the most part to acquisitions. And therefore, the effect of this delta on the above is included in the EUR10.5 million in M&A, since as we were mentioning earlier, as far as infrastructure and landfills are concerned that we didn't do very well in the first nine months, except for the fact that in early August, we started the first of the three landfills that we have been working on with EUR1 million capacity located in Ravenna which began receiving waste plants beginning in early August and therefore it had an impact on Q3 in a very limited way.

Efficiency and dynamics on waste collection services were very good. And as I already mentioned, they made a positive contribution in terms of increased efficiency, but also in terms of extracting value from a sorted collection of waste, which is above 55% now in the first nine months of the year.

Moving on to our networks. The result is slightly below the results we posted last year. This is no surprise, since the tariff review happens every month as a matter of fact, and it has an impact on results of course. To this, we also have to add a number of effects which ended compared to the past. First of all inflation, which in 2016 is almost equal to zero, compared to previous years in which inflation was always at around 1% or 1.5% and that brings about a few million euros in reduced revenues due to the lack of a review in RAB. And then we also have efficiency, which was pretty positive.

And that also includes the tariff review which we already mentioned, but also and especially we also have a efficiency initiatives, which allowed us to offset the effects of tariffs. As far as our organization is concerned, as of July 1st, we've set up InRete, which is a new legal entity, which doesn't have any effects on our consolidated figures. Although it is a reorganization which is dictated by the unbundling regulations. And within this sector for the most part, where we to focus on a couple of further pieces of information concerning the business areas, which you typically ask off. Within the EUR303.5 million overall results, 174 refers to the water business, which is pretty much stable compared to the last year with EUR1 million decrease, EUR38 million refers to electricity networks and EUR84 million to gas networks. The remaining part approximately EUR8 million refers to district heating. This is the trend in a nutshell. Especially gas networks in our case, which are the more relevant ones in Q3. We're also affected by the negative effects of the dynamics we're witnessing in the white certificates market. As you know, all energy distributors have to comply with obligations concerning white certificates, and the recent interventions made by the organization which has to limit white certificates, and some of the government's guidelines have limited the offer or the supply rather.

And therefore prices have gone up considerably with a negative effect for operators at least for the part that refers to the titles we have to go out and buy in the market. This had a EUR4 million impact in the first nine months of the year, which isn't something we're pleased with of course, also because it doesn't, -- it isn't something we can control very much. And the energy sector, things are continuing well. There haven't been any signs of a slowdown in the dynamics, we had witnessed in the first six months of the year.

As you can see, organic growth was about EUR14 million, which as you can see from the lower left hand graph refers to a number of phenomena. We had a decreased performance as far as the gas supply and trading are concerned, especially gas trading given the effect of the price crunch between Central Europe and Italy, which is the consequence of a first half of the year thermally which is pretty mild it reduced to the opportunities to optimize gas both through import networks and referring to the gas stocked in the storage units. While, as far as the supply business is concerned, we are pretty stable on margins with a very slight erosion. As far as the electricity is concerned, both supply and trading posted an improvement. As far as their performances are concerned and this refers both to the liberalized market and to the (inaudible) market in which we operate.

Finally, we posted a good results in our small power generation activities, these are relatively small figures, although they did contribute in an important way to the results we're illustrating today. Out of the EUR14.7 million referring to Power gen, we have some 12 million which referred to the MSD market, whereas the rest refers to asset management, which means that the business which lost a couple of million euros last year, in the first nine months, and this year has posted a plus EUR12 million improvement with the net figure of plus 14.7 million.

As far as our customer base is concerned, we have continued to expand it not only through the acquisition we mentioned earlier, to which we'll also have to add a second transaction at the end of the year, plus we have also had the typical organic development. We now have 1.38 million customers in the gas business and 864,000 customers in the electricity sector with an overall growth of 44,000 customers, which is in line with our performance in the recent past. I'll give the floor to Luca now for a couple of remarks on the cash flow, which as we mentioned were very satisfactory.

Mr. Moroni - Administration, Finance And Control Director

Good afternoon. We had last talked to each other at the end of H1 with the free cash flow which is above 180 million. Currently our free cash flow is well above 200 million, we're at 243 million to be accurate, which means that we were able to generate very positive cash flows, which allows us to self-finance our investments. CapEx is worth 241 million, which is a plus 9% compared to the previous year. And also thanks to a continuous and the constant excellent management of the networking capital. We were also capable of reducing our debt by EUR85 million as we mentioned, bringing it below EUR2.6 billion, we're at EUR2,567 million to be specific.

The cost of debt is now at around 3.7%, and therefore we reduced a few further bps. Also thanks to the constant attention paid to the restructuring and refinancing of our debt, with yet another operation last October with a tender -- new (inaudible) transaction through which we emitted a new bond after we've recalled a part of the two already existing bonds on the market. This is a new 10-year bond with an interest rate, which is below 1%, with the credit spread equal 60 -- equal to 60 basis points with 45 basis points lower compared to the time at 10-year BTP. This is a very satisfactory operation, which also allowed us to increase the average duration of our debt, which is now closer to nine years compared to the past.

The results were very positive, which go to show the positive trends in our financial management, and as far as our presence on the markets are concerned. Well, for the most part, all of the things that we were able to achieve in the third quarter was positive as you can see, these are justified by the elements we've illustrated. We are preparing and despite the difficulties and the hysteria on the market, we are quite ready. We have a financial situation which is very positive as you've seen, which guarantees the soundness of our Company and guarantees our ambition to continue to grow.

The opportunities in the acquisitions which are no second-class citizen compared to the mergers between multi-utilities, there are simply a different way of achieving M&A. And therefore over the past few months, we have decided to focus more on acquisition specifically, because there were a number of opportunities on the liberalized market which were easier to negotiate. Whereas we were still waiting for the completion of the regulatory framework of the Madia Decree, without which as you know the new regulations are simply aren't complied with. And of course, there were no possibilities for mergers, because we are now waiting for the completion of the Decree, which are about to happen actually. And therefore, we will be facing the upcoming future with our typical desire to complete the transactions we're interested in, and we will ignore the ones that are less interesting.

I think that this is already one of the elements which we'll be characterizing, the new business plan with its effects, the business plan that we are currently completing. And the beginning of the tender phase especially in the gas sector, will also be a part of the business plan that we are almost ready for the beginning of the tender process in certain locations. Therefore, as far as growth possibilities are concerned, these will be the two more fascinating possibilities. The newest elements following a period in which the market was at a standstill. As I was mentioning, we are preparing the business plan and we will be publishing it early next year as we already mentioned, and we will be presenting the business plan to the market at the beginning in the second half of January.

That's it, as far as we're concerned, and we are ready to take some of your questions.

Q&A

Chorus Call operator

This is the Chorus Call operator, we can now begin our Q&A session. (Operator Instructions) The first question is from the Italian conference call, Javier Suarez, Mediobanca.

Mr. Suarez, Mediobanca

Good afternoon. I have a few questions for you. First of all, the first question on the gas sector, especially on slide six, which underlines the impact, the 7 million negative impact on gas supply and margins. Can you give us some details on the reasons behind this decline? And what do you see is the trend in the first month of the quarter -- can you give us some indications on the gas volumes till the end of October compared to last year?

Then I have a question on waste. You underlined the major growth you posted in volumes in special waste, can you give us some further details on the market conditions that you observed during Q3 and whether or not you feel this trend will be sustainable in the upcoming quarters.

And then a final question on slide seven, and specifically on the EUR75 million in improvement and working capital. Can you give us some details? Do you think that this level will be sustainable to -- although which is at the end of the year?

Mr. Venier – Chief Executive Officer

I'll begin by commenting page six. The EUR6.8 million reduction isn't due to an erosion on margins, and isn't due to the commercial aspects such as sales. It is more links to a lower performance in gas trading. Last year, we had some especially favorable conditions to import gas, especially the 0.5 billion cubic meter capacity on the tag pipeline which is something that we had taken advantage of very well.

This year, we didn't have those same conditions which means that the physical imports weren't possible this year. The conditions simply weren't there, and therefore this capacity remained empty and the cost of the capacity therefore had an impact on the first nine month results.

And this explains five of the EUR6.8 million shown in the graph, the large chunk thereof. Concerning the supply side in the first 40 days of the thermal season, as far as gas procurement is concerned, the conditions are similar to the thermal season we recently concluded. As far as volumes are concerned, we still haven't seen the statistics because the business review will be happening in four days or five days. But my guess is that the volume is for October, don't differ too much from the volumes last year, since October was characterized by a first week which was slightly colder than

last year, whereas the second half of the month was slightly warmer. Therefore, I don't think there will be any major changes. Plus the real result of the quarter is seen in December, and that's the month in which volumes are doubled compared to October.

As far as waste is concerned, your question refers to the 270,000 further tons in terms of volume. This stems for the most part, if not entirely from the volumes induced by the further capacity of our asset, stemming from the acquisitions that we made last year. 150,000 tons from the former Geo Nova landfill and 170,000 tons or further 150,000 tons from the waste recycling assets.

As far as prices are concerned, even in Q3 there has been a consolidation as far as the growth trend is concerned. To-date including October we haven't had any dips. A few months ago we were mentioning an improvement somewhere between EUR3 to EUR5 per ton, over the past three months we have had improvements up to EUR8 or EUR10 per ton compared to the same period last year, which means that for the time being we aren't seeing any signs of reduction in the trend, which is understandable, of course, because, this can also be seen by the events happening in certain Italian cities, some major cities of that[ph].

The landfill capacity which is -- the landfill capacity throughout the country isn't available. We're not the only ones to have problems in obtaining the authorization to broaden our landfills. We have -- we don't have a major ability of treating organic waste in Italy. And therefore, due to supply and demand mechanisms following two or three years, in which things haven't been very good for this point of view.

And this has an impact on prices, now prices aren't back to the levels we saw in 2012 or 2013. Of course, the prices are above 2014 and '15, but they're still not back to those levels we had in 2012 and '13. Therefore, I'm not concerned by the fact that prices have increased. I believe they will be increasing further to go back to the conditions we had in the past. As far as the question of working capital is concerned, I'll leave the answer to Luca. As far as working capital, efficiency was brought about by two items. First of all, month-by-month we are continuing to optimize our invoicing cycles, which we try to keep under control, something we try to monitor constantly, and they are improving on a monthly basis with an increasingly positive performance. The second item depends on all of the investments, and the efforts we've made over the past few years in terms of optimizing the entire credit management process. We began with a number of targets namely to reduce the unpaid ratio from 1.4 or 1.5 we had down to 1, which is something we were able to do, we're now about 1 to 1.1. And this is all a further positive cash flows. We also tightened the entire process and therefore, we have pretty much -- already begun the cashing in process which contributes to the positive management of the free cash flow. What is the future perspective look like? Obviously, September is a lower seasonal momentum, which means that we will be dealing with the final three months of the year, the winter months which will be absorbing some of the free cash flow. And therefore, we expect to be at a debt level, which will be above the current debt level, although it will be below the level we had last year. Therefore, we will be positioned somewhere in between the two figures.

Mr. Gamberini, Equita Sim

Good afternoon, just a couple of questions. As far as the energy breakout is concerned after the nine months, can you give us some information compared to last year? And as far as EBITDA on the whole year is concerned, do you have anything to add, although I do understand you don't offer guidances, can you help us understand what your year-end target is? Thank you.

Mr. Venier – Chief Executive Officer

As far as your question on the energy sector is concerned, the actual level of the EUR116 million we have posted in the first nine months of the year, EUR95 million are referred to the gas sector, including heating, whereas the remaining 66 million referred to electricity. This is the breakdown of the two elements within the energy sector. And as far as EBITDA is concerned, I don't know whether the Executive Chairman has anything to add.

Mr. Tommasi di Vignano - Executive Chairman

So honestly speaking, I'm not really interested in your question. We have a clear trend for the initial part of the year. The first must or the first target we had was to recover our conditions based on the reductions brought about by the regulatory framework, and we succeeded in doing that. And therefore in the first three quarters, you can see the improvement we made, and our target of course is to reach year-end in the consistent way with the trend we've had so far. Taking into account that we've already covered most of the bounce back, most of the recovery. We recovered three-fourths of the WACC recovery and so on.

Which means that we want to continue, we want to be continuous as far as the values we have illustrated today. Plus, as far as any extraordinary effects vis-a-vis a more linear trend towards the end of the year, that isn't something we expect.

And as we've already said, we're continuing to work on M&A, but in any case were the formal announcement of any possible further transaction to happen, it will probably happen at the end of the year. Therefore, in terms of the impact, in terms of the effects you were mentioning, I don't think we'll be seeing very much. The important thing will be to conclude the transactions and be able to enjoy its effects beginning next year. Therefore, there is no reason to believe that we won't be continuous in our approach.

Mr. Gamberini, Equita Sim

Just a final follow-up. The impact of the white certificates, did that impact emerge in Q3? There wasn't something which happened in the previous quarters, and what is your estimate vis-a-vis what we can expect for the entire year, and if you can compare that to the impact last year.

Mr. Venier – Chief Executive Officer

If you look at the GME website, if you can look at the competitions for the past three months on white certificates, you'll see that the growth has been almost vertical. Therefore, most of the EUR4 million impact happened in the past three months or four months. Obviously in giving this figure, I'm simply assessing the obligation I have to cover that depending on the current market price.

And as far as, what it may be at the end of the year, well, next week we'll be a meeting to understand what the trial looks like. For the time being, the market is absolutely schizophrenic, so it's difficult to say, but it will be fine if it isn't four, it won't be a 10 or 15, I think that's pretty safe to say.

Also given the levels we've reached were at above EUR150, the figures are simply unthinkable. Thank you.

Chorus Call operator

Mr. Tommasi di Vignano and gentlemen, there are no further questions for the time being.

Mr. Tommasi di Vignano – Executive Chairman

Well, thank you very much, and we will talk to you soon.