



ERG S.p.A.
“3Q 2021 Results”
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MODERATORS:
PAOLO MERLI, GROUP CEO
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Operator:

This is the Chorus Call conference operator. Welcome, and thank you for joining the ERG 3Q and 9M 2021 Results Conference Call. After the presentation, there will be an opportunity to ask questions. At this time, I would like to turn the conference over to Mr. Paolo Merli, CEO of ERG. Please go ahead, Sir.

Paolo Merli:

Good afternoon everybody and welcome to our Webcast.

Here with me is Michele Pedemonte, our CFO, who will take you through the results in more detail after my opening remarks.

The key message I would like to convey today is the following: still a very strong quarter, up significantly YoY at operating level and - even more so - at bottom line, which reflects the amazing job done on both Capital Structure and non-cash costs, resulting in lower financial and depreciation charges respectively: the first as a consequence of the liability management programs on the debt side, and the latter as a consequence of the extended useful life of the Asset Base following our Life-Time-Extension programs.

So, you will see in a moment that - thanks to this very solid set of results and a fairly strong price environment out there - we are ready to revise our FY guidance up once again.

But on top of the economic results, which are definitely good, what I am most proud of is the excellent execution achieved YtD towards our 2021-2025 BP targets: execution turned out to be quicker and more effective than expected.

As a premise, let me finally point out the unprecedented price environment we are in, especially since August-September, as a consequence of the gas and CO2 price trends: to me this simply means that the energy transition is not just crucial but increasingly urgent. This very unique situation has two immediate consequences on our figures: on one hand, it is boosting our Operating Results (as a portion of production is still merchant, as you know), while on the other hand it is inflating our NFP, given the MtM of derivatives against future delivery... I mean, delivery beyond 2021.

In a nutshell, that is the premise I would like to give you, and what this document is about.

So, let us now start commenting on results. I am going to **page no. 4**: Ebitda is up 10% and 20% YoY over 9M and Q3 respectively. As I said, satisfactory results, but let me here focus on the Third Quarter.

So, in the third quarter Wind closed with an Ebitda of €57mn, 36% up YoY. Despite the lack of wind all over Europe especially in September, we managed to increase our Ebitda significantly YoY, thanks to the increased installed capacity and to the stronger price scenario, both for merchant and incentive price. And this was particularly true in Italy.

Solar was at €24mn of Ebitda, slightly up YoY and very solid over time.

Hydro was once again the outperformer of the period, with Ebitda almost doubled in Q3, but we have seen the same trend we have seen over the 9M, driven finally by heavy rain in 2021 against a dry year in 2020, and this coupled with the utilization of reservoirs, which were filled with water at the beginning of the year.

As far as our CCGT is concerned, here we experienced the opposite situation, with Ebitda of €8mn during the quarter, less than half the result over the same period in 2020. We knew it: 2021 is a particular year for the CCGT, because we are carrying on the investments to revamp the plant. But coming back to the results and the comparison with last year, this drop mainly reflects the phase-out of white certificates (which accounts for €5mn in the comparison), and then the extraordinary negative spark spread we have seen over the period, with those spikes in gas and CO2 prices resulting in a squeeze in generation margins. Adm all this happened in a quarter when we started the general shutdown of the plant at the end of August (and it is still going on), through which we are going to revamp the steam turbine of the Module 1, and - once the plant gets back on stream – it will be eligible to receive White Certificates.

The positive news is that the maintenance works for the refurbishment of the plant are going on well, so we expect all these works to be completed by mid-November, and then the plant to be back on stream at the end of the month with its eligibility for White Certificates. That means that as of 2022 the plant should recover its normal level of profitability.

Let me now comment on Net Profit, which was €30mn in the quarter, up three times YoY: quite an impressive number, driven up by all the work done over the last few years to minimize our cost of debt and non-cash costs, as I already said respectively through Liability Management and Life Time Extension programs.

It is quite important to say something about Net Financial Position, which ended the period at 1.829€bn, roughly €400mn higher than at the end of 2020. Of course, it reflects the dividend paid, the huge investments made over the first nine months of the year, but also – a already said - the negative MtM of futures derivatives on energy prices. This is something that is not worrying us: it is just a momentary effect, and we expect this to have a reversal effect either through the sale of the Hydro assets, or through those derivatives arriving at the delivery time.

So, let us move onto **page no. 5**, where I would like to spend few minutes on the very important achievements we obtained over the last three months, since we met in our last webcast in August.

You know that a few days after that webcast, on August 2, we signed an important agreement with ENEL to dispose of our hydro asset. So here today I would like to inform you that in the meantime - just few days ago - we received all clearance needed from the Antitrust, so we can confirm that the closing will take place in the first days of 2022.

This for us is a very important step towards the further transformation into a pure Wind & Solar operator, to be completed with the sale of our Thermo assets. In this respect I expect we will be able to announce an agreement in the forthcoming weeks.

Here you have the main financial figures around the hydro transaction: €1bn of Enterprise Value, then there is the perimeter of derivatives which are included in the transaction, with a fair value positive for us, as in term of adjustment in price we expect €130mn, and this is the number based on the value registered at the end of September. This amount basically is already discounted in our NFP, because in the cash we anticipate the clearing out, but this amount will be received by the company at the closing for the hydro assets disposal, if the conditions will remain basically the same.

Let us move on... on one hand we moved on in the asset rotation, on the other hand we moved on in expanding our portfolio of RES activities. On October 1 we announced an acquisition which is very much representative of what we are seeking in order to reinvest our proceeds coming from the asset rotation. This acquisition is about 152MW of Wind and Solar assets in France and Germany, for a total consideration of roughly €200mn. We expect this portfolio to contribute roughly €20mn – or slightly less than that, going forward – and we are going to consolidate these assets as of October 1, 2021. So, what I think is perceived as a good piece of news is that the transformation is moving on and faster than expected in our 2021-2025 Business Plan.

Moving to **page no. 7**, here I have a list of important recent achievements: the last three months have been a quite busy period. Let me summarize like this.

We continued to work on securing revenues, in line with our strategy to target (at least) 80% of quasi-regulated revenues.

We signed a 5Y PPA in France with Engie, covering some plants exiting their incentive scheme by the end of the year, for a total amount of 55MW

Then you already knew that we participated with 144MW into the last auction, and in September we had the official feedback from GSE that all those megawatts were awarded a tariff for 20 years at cap in the area of 60-61€/MWh

In September and October – this is another positive piece of news - we managed to obtain two *Autorizzazioni Uniche* (i.e. full authorizations) for two further projects in Italy: one is Repowering project that was in our Business Plan (50MW in absolute terms, and 30MW in differential terms). The other project is totally an upside compared to our Business Plan, because it is a Greenfield of roughly 47-48MW. The two projects took part into the last auction, which was held in October 2021: we are still waiting for the results of the auction, but we are quite positive about the outcome

Then we have several achievements in the ESG area, which is at the core of our strategy, where we obtained 3 important recognitions, which honestly surprised ourselves: we were ranked first out of 80-90 electric utilizes around the world by ISS, SBT approved our 2021-2025 emission reduction targets, and finally, - last but absolutely not least - ERG

has been included in the MIB ESG Index, which means we are ranked in the first 40 corporates listed in Italy and most exposed to the ESG world.

So far so good: we are right on track with our Business Plan.

Last achievement, a quite important one: in September we issued our third Green Bond. A €500mn Green Bond with a 10-year duration, the longest duration so far for us. The issuance was once again a great success, with demand exceeding 6 times the offer, and in the end all this brought to a Yield-to-Maturity of below 1%, which is a very satisfactory level.

And now over to Michele for his comments on Q3 Results.

Michele Pedemonte:

Good afternoon and thank you for the attention.

I am on **page no. 10**.

Power demand in Italy was up 3% YoY: mainly due to the fact that 3Q 2020 was still negatively impacted by the pandemic situation. You see here that the only technology which contributed positively to demand was wind (+9%), whilst there was a decline in all the other technologies, and namely solar (-2%), hydro (-2%) and thermo (-6%). Looking at ERG, our wind productions in Italy were up 8% (pretty much in line vs. country average), while hydro was up 44%, higher than national level, due to its location in central Italy, which benefited from good hydro volumes, coupled with the use of reservoirs in the period.

As far as electricity prices in Italy, in 3Q 2021 there was an unprecedented rise in electricity prices, with the national price at €124, tripled YoY. The all-in price, from €141 to €234, benefited from the rise of electricity prices coupled with the rise in incentive - which you know is calculated on the basis of last year's average national electricity price - that recorded very low levels due to the COVID 19 lockdown. The trend in electricity prices, as you know, mainly reflects the strong rise in gas prices and in CO2 prices.

As a consequence, our CCGT's Clean Spark spread declined to 3€/MWh, with rising gas and CO2 prices only partially offset by a recovery of prices in Sicily. These numbers reflect a Sicilian premium vs the national price of 11.8€/MWh vs. 13.5€/MWh last year.

At the bottom-right of the chart you can see the average reference selling prices for our productions, country by country. Even abroad, it is worth noting the generalized rise in prices in Q3, in particular in countries where we have green certificate-type mechanisms, such as in Romania.

I am now on **page no. 11**: here as usual a picture of the main drivers per business of the Ebitda evolution in Q3.

As we have said before, Wind in Italy was up €12mn due mainly to better electricity price and a higher value of incentive, coupled with rising volumes. Wind abroad was up €3mn mainly due to a slight decline in production, offset by the contribution as of July of the recent acquisition in France.

Solar was almost in line YoY with slightly lower volumes, partly offset by better prices in the period and by the contribution of Joran in France.

Hydro up €16mn, thanks mainly to a rise in volumes (+44%), driven by the exploitation of reservoirs. Energy available in lakes is 16GWh (-98GWh vs. end of 2020).

CCGT was down €13mn, as already commented, mainly due to the white certificates phase-out and the squeezing of spark spreads in the period. Let me also add that in September we started the maintenance works for the refurbishment of the plant, which is expected to return to its normal level of profitability as of 2022.

I am on **page no. 12**, on Wind results.

Ebitda in Q3 was €57mn, up 36% YoY. Ebitda was up in Italy (+44%) and abroad (+18%). Productions in Italy were up YoY (+8%).

As far as prices, in Italy the average unitary revenues were 140€/MWh, higher than 122€/MWh last year. Abroad the average is 102 €/MWh.

So, in the end the rise here is related to a stronger scenario, both in Italy and abroad, coupled with a rise in production in Italy and with M&A acquisition in France.

Let us move on, to Solar results at **page no. 13**.

Ebitda increased slightly at €24mn (+3%), for the following items:

- higher Unitary Revenues (in Italy) at 346€/MWh versus 321€/MWh last year, as a result of the higher merchant price, and
- contribution of France acquisition since July 2021.

Moving on, I am on **page no. 14**. I am going to comment on Hydro results.

Ebitda was €34mn (+93%), up YoY mainly as a result of higher volumes, coupled with a better price scenario and a higher value of incentives.

As such, unitary revenues were 135€/MWh.

The main takeaway here is still the same: strong hydro availability in 3Q 2021 thanks to the use of the reservoirs vis-a-vis particularly dry season in 3Q 2020.

Moving onto **page no. 15**. I am going to comment on Thermo results.

Ebitda in 3Q 2021 was €8mn, significantly down 63% YoY, which of course is a direct consequence of the end in 2020 of the first 10 years of validity of White Certificates (-€5mn) and a negative scenario (-€8mn).

Let us move onto **page no. 16**, for a brief overview of investments in the period. Here it is worth focusing on 9M: we invested €367mn versus €110mn over the same period of last year.

During the 9M 2021, Capex are composed as follows:

- about €188mn of M&A in Wind and Solar abroad: I am speaking about an acquisition of a RTB project in Sweden for €41mn, and the recent acquisition of Wind and Solar installed capacity in France for €147mn. I remind that the economic effect of the latter started as of 2H 2021, while the plant in Sweden is under construction
- about €155mn related to organic Capex in Wind, referred to construction activities mainly in UK, France, Poland and in Sweden. This figure includes also the Capex for the repowering and reblading done in the period.
- about €8mn related to the refurbishment of Module 1 of the CCGT plant, in order to renew its eligibility for another 10-years period of White Certificates, and finally
- about €15mn of maintenance Capex, spread across all of our technologies.

Moving on to Financials (on **page no. 18**), commenting on P&L on a recurring basis.

I have already commented on Ebitda. So, going down the P&L and looking at the 3Q of the year, I am going to comment on depreciation, Net Financial Position and taxes.

Lower depreciation (-€5mn) reflects:

- the reduction in depreciation of some Wind assets due to the end of amortization period, coupled with a review in depreciation plan of some intangibles wind assets, due to a Life Time Extension project of our assets, and
- the reduction in depreciation in the consolidated accounts of the Hydro assets, due to an increase of the amortization period, without any tax effect.

Net Financial expenses at €7mn, vs. €13mn in 3Q 2020, thanks to a lower cost of gross debt (1.7% vs. 2.3% in previous year), mainly following the issuance of our second Green Bond in September 2020

Tax rate in the quarter was 26% against 22% in 3Q 2020. Taxation in the quarter benefited from ACE in the area of €2.7mn.

As a result of all this, adjusted Net Profit amounted to €30mn in 3Q 2021 vs €9mn in 3Q 2020, and €130mn in 9M 2021.

Now I am on **page no. 19**: let us take a look at the Cash Flow Statement and the Net Financial Position for the 9M 2021.

Net Financial Debt closed at €1.829bn, up by €390mn from the end of 2020.

Starting from the left, we have our Ebitda (€400mn), the Investments made over the period (€367mn), change in Working Capital, Financial charges, dividends of €113mn and a change in MTM hedging future derivatives (€254mn), that reflects the strong increase of future commodity prices.

So, all these effects led to a Net Debt of €1.829bn.

Please note that about €130mn of MTM of future derivatives are connected to the Hydro business, and it will be subject to a positive price adjustment in the sale agreement with the Hydro buyer.

I think that I have touched on all the relevant items. Thank you for your attention, I will now hand over to Paolo for his final remarks.

Paolo Merli:

Thanks Michele. Here we are with the guidance for 2021.

We have already commented the 9M results, but thanks to this solid set of results YtD, the further installed capacity that came within our scope as of 1 October (contributing as of the first quarter), and also to the unprecedented price scenario (which anyway is boosting our results), we are now in the position to revise our guidance for the full year upwards with just one quarter missing. In order:

- Ebitda: central-case up by €20mn, of which roughly €5mn will be coming from the newly acquired capacity in France and Germany.
- Capex: once again we revised up the central case by roughly €200mn, which – it is not a coincidence -is exactly what we are going to pay for the latest acquisitions in France and Germany.
- As a result of all this, and of the dynamics of MtM that I explained in my opening remarks and then Michele explained even better in his speech, the NFP guidance is increased by some €350mn – so €200mn for investments and the remaining mainly related to the dynamics of the MtM. But please consider that this is just a temporary effect, because it will have a full reversal effect in 2022, as most of this amount is related to the Hydro and CCGT perimeter.

Thank you very much for listening. We are now ready to take your questions.

Questions & Answers

Operator:

Excuse me. This is the Chorus Call conference operator. We will now begin the question and answer session. Anyone who wishes to ask a question may press "*" and "1" on their touchtone telephone, to remove yourself from the question queue, please press "*" and "2." We kindly ask you to use handsets when asking questions. Anyone who has a question may press "*" and "1" at this time.

The first question is from Sara Piccinini with Mediobanca. Please go ahead.

Sara Piccinini:

Hi, good afternoon everybody, and thank you very much for taking my questions. I have three questions, and then maybe I can follow up later with others. The first question is on hedging: can you please provide an indication on the level of price that you expect for 2022 and 2023, and also the level of hedging in terms of percentage of production?

The second part of the question is more related to the impact of the higher prices on the actual value of the Green Certificate for next year. So, if this year we have such a high price, this could significantly reduce the level of Green Certificates for 2022, so this should have a meaningful impact on results. Can you please explain us what your expectation is on that, and also if there is any limit on the value of the Green Certificates related to the hedging contracts? Okay, sorry this was the first question: so, the level of hedging and also the impact for next year on Green Certificates.

The second question is on Capex cost inflation: we are seeing a lot of debate on cost inflation and implications that this could have on future Capex. What is your position on that, and how much of your Capex is already secured? And in terms of supply chain disruption, do you see anything going on?

And then the third question is just a clarification on the guidance of net debt: I know that you already explained it very well, but just to be sure I understood correctly. So, the €1.9-2.0bn that you are giving as a guidance for net financial position should be adjusted for the €130mn that ENEL should give you as a price adjustment, correct? And could you quantify the level of these derivatives on the debt that you expect by year end, and that should be then reabsorbed, going forward? Thank you very much... I am sorry for the long questions.

Paolo Merli:

Okay Sarah, your questions are very clear, thanks. So, on the first one on the hedging, I give you a rounded number but the production hedging in 2022 is in the region of 75%, slightly higher than that, and the price is more or less in the region of 65€/MWh. And for 2023 the coverage of production is in the region of 50%, and more or less the price is very similar. So: a price which is higher than what we expected at the time of announcing the Business Plan.

About the value of the incentive for 2022, you are perfectly right. It is a mathematical formula: €180 less the price for 2021 (the price for 2021 is going to be something between €100-€110). That means – it is just a mathematical effect - the incentive next year should be in the region of €50, or something like that, more or less: more than half the level we are having in 2021. Of course, in our preliminary projections this effect should be more or less offset by the fact that we still have a portion of energy which is

merchant, so the two effects should be surely balanced. Consider that also outside Italy, part of the asset base is going to enjoy higher scenarios. So, for instance - let me give you this detail - the tariffs in Germany are a one-way CFD: so, with the price that is higher than the tariff -and that is the case in 2022, at least according to the forward market - you are going to get the merchant price.

In Poland as well – because, you know, the mechanism is merchant plus Origins certificates - part of the production in Poland is covered, but part is merchant. So all-in-all, we think the two effects should be at least balanced, but this is just a preliminary projection we are building these days ahead of next year.

About Capex, you are definitely right: I think it is not a secret that there is a strong inflation all over the sector. For sure, the wind turbine providers have reported data over the last few weeks, and they announced profit warning, because this cost inflation is squeezing their margins. Fortunately, in our case we have been good, but maybe also a little bit lucky, because we signed just last year a couple of framework agreements with a 3-year duration with Vestas and Enercon, which provide us with - let me say - almost full coverage for our Business Plan.

There is some indexation to iron, but it is not very material: so far, we are very near, or we are just experiencing a near increase, by which I mean few percentage points compared to what we inserted in the Business Plan. So, there is not a major impact because we are covered by this framework agreement. Let me just give you an example to be even clearer. During the webcast I said that we obtained two *Autorizzazioni Uniche* for two projects. One was already in the Business Plan, so it was covered by the framework agreement with Vestas, and then the Capex per megawatt is exactly in line with what we announced: €1mn per megawatt.

The other one is a Greenfield: it is a very good wind farm, so the return is still amazing. But in that case, that project was not in the Business Plan, it was not covered by the framework agreement, and here we are experiencing a higher Capex per megawatt, at least 10% higher than that. So, your point is correct. I hope the legislator - in particular the Ministry of the Energy Transition - when looking at the next auctions, will take into consideration the fact that this inflation is going to probably reverse the LCOE trend, which was expected to go down forever. But this is not an issue for ERG: it is an issue for the entire sector and probably other industries. But in our case, you know, auctions are the main tool through which players are going to secure revenues. So, we all hope that legislators around Europe - as we are in Europe - are thinking about this, and for instance, connecting and linking the tariff price to inflation, at least. In Italy there is no inflation: the price, the tariff is nominal for 20 years. I hope I answered this question.

And the third one: yes, let me try to explain even better. So, our net financial position - €1,829mn at the end of September - includes €277mn, so almost €300mn, associated to the hedging, the futures we have signed over time to cover 2022, 2023 and 2024 productions, and also the remaining part of 2021. Part of this amount is linked to the hydro, and the exact number is €130mn as at 30 September. What is going on with this amount? If the market remains exactly the same - which is a strong assumption – as the one we had at 30 September, at the end of the year we will still have this number in our net financial position. But just few days after – let us assume, I do not know, the closing with Enel will be on January 2, let me say, just to guess a day - that day Enel will pay us €1bn plus €130mn, so our net financial position will be recovering in the first quarter of 2022. This is just the amount of the Hydro. And then there is a very similar situation for the CCGT, but there we have not yet closed the sale, so let me wait. Sara, I hope, I explained everything well.

Sara Piccinini:

Yes, it was very, very clear. Many thanks. Just a very quick clarification: the price for the level of hedging that you are indicating is excluding hydro, is it?

Paolo Merli:

Yes, it is for our Wind and Solar production.

Sara Piccinini:

Okay. And the very last question: can you also give 2021 levels? Many thanks.

Paolo Merli:

The coverage in 2021 was slightly below €60 because the coverage has been built during August 2020, when the prices were at that level: €55, the exact number is €55.

Sara Piccinini:

Very clear. Many thanks.

Paolo Merli:

Thanks to you, Sara.

Operator:

The next question is from Roberto Letizia with Equita SIM. Please go ahead.

Roberto Letizia:

Yes, thanks for taking my questions. I have a follow up on Sara's questions on the hedging, because just every time this makes me confused when it is re-explained again. But just to be clear, you do not hedge the Italian production covered by Green

Certificates, because these are naturally hedged. So, when you say the hedging, you say it as a mix of the Italian production covered by the Green Certificate (which are naturally hedged) plus the productions that are covered by financial contracts: is that correct? This is the first question.

The second one relates to the disposal procedure. I wonder if you can now give us a figure of how much of net income is going to be deconsolidated next year, in order to allow us to have a better forecast of the 2021 profit and loss. I was just wondering whether the sale of the CCGT - if it is going to happen by the end of the year or beginning next year, or whenever it is going to happen - will trigger significant changes in the ESG index participation of ERG, as far as you know of course, because this is not a very predictable matter. But maybe you are already accounted for by the fact that in some of the major global indexes you may have an additional re-rating by the fact that your ESG position probably increases. Thanks a lot.

Paolo Merli:

Thanks to you, Roberto. Let me elaborate a little bit more on our hedging policy. No: when I say we have covered roughly 70% of production, I mean all the renewable production. It is true that we have this mechanism for the incentive, but you know, yes: the natural hedging is there but it is partial because it covers multi-years, because the coverage assured by the formula is going to be the year after and consider that not far away in time our incentives are going to expire. So, in our policy we tend to protect the budget here. So, we have hedging ratio based on the entire renewable production. I hope it is now clear.

Let me then answer first your last question. I must say we expect to have the sale of CCGT for sure by the end of the year, but the announcement - I hope - will be coming in the very next few weeks. And yes, you are right: once the CCGT will be disposed of, we are landing on a zero-carbon world, because that is the only plant we have in our portfolio that emits CO₂. And yes, we have some idea of the impact of this on, for instance, the Standard & Poor Energy Index or other indexes, other ratings. We are already very top-ranked in all the ESG ratings. But for sure, in the equity indexes, we should make a quite important step forward, once the CCGT is out of our portfolio. But honestly that is behind our strategy, that is why we are disposing this plant, because this plant is a fantastic one, as it has always generated cash flow, we are now finalizing the general shutdown, and at the end of November we expect the new steam turbine and the new steam system to be on stream and eligible, once again, for another shot of White Certificates for the next 10 years.

And you ask me the impact of net profit: it is in the region of €50mn, some €50 to €60mn can be the impact on net profit coming from the Hydro and Thermo, more or less.

Roberto Letizia:

So, for both of them? So that include both the consolidations: €50-60mn. Alright, thanks a lot.

Paolo Merli:

Combined, thank you Roberto. I covered all your questions, did I?

Roberto Letizia:

Yes, you did. Thanks.

Paolo Merli:

Thanks to you.

Operator:

Mr. Merli, there are no more questions registered at this time.

Paolo Merli:

So, thank you very much, and we will be in touch, let us say, early January or maybe before through our press release. So, thank you very much for listening, and have a good afternoon.