Q3 2013 Snam SpA Earnings Conference Call

Transcript

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Presentation

Operator [1]

Good day, and welcome to the Snam third-quarter results conference call. Today's conference is being recorded. At this time I would like to turn the conference over to Carlo Malacarne. Please, go ahead, sir.

Carlo Malacarne, Snam SpA - CEO [2]

Thank you. Good afternoon, ladies and gentlemen, and welcome to Snam 2013 third-quarter results presentation. Today's agenda will be structured in two parts. First I will start by outlining the main highlights of the 9 months and some recent development, and Antonio will then focus on the financial results for the first 9 months in more detail. At the end of the presentation we will be pleased to answer any question you may have.

Let me begin with the main highlights from the first 9 months as well as giving you an update on the businesses. For the first 9 months of 2013 I'm pleased to report a solid set of results consistent with our track record of delivery despite the tough environment.

Snam's sound operating performance over the period is reflected by the EUR2,633 million of revenues and EUR2,083 million of EBITDA, up 3.8% and 2.5% respectively versus the same period of 2012. The increase in consolidated EBITDA was achieved due to the growth in regulated revenues across all our businesses and our continued focus on the control of operating cost.

EBIT reached EUR1,516 million, almost in line with the same period of 2012. From a business segment perspective the positive contribution of both the storage businesses, in which EBIT increased by 14.4%, EUR30 million, and transport business, in which EBIT increased by 3.2%, EUR28 million, despite the reduction of gas volume transported was almost offset by the result in the distribution business which include the negative effect of higher depreciation.

Net income reached EUR674 million, up around 31% on like-for-like basis. This remarkable increase is related to our continued focus on financial efficiency as well as the one-off effect of the unwinding of some interest rate swap contracts as part of the full repayment of the financing provided by Eni which occurred in the third quarter 2012.

As a consequence, the comparison with the adjusted net income of the same period of 2012 shows a decline of 7% on like-for-like basis as result of higher net financial charges mainly due to higher outstanding debt. Antonio will discuss this in more detail later on.

In the first 9 months of 2013 cash flow for operation of around EUR1.5 billion allowed us to fully finance both domestic CapEx and the acquisition of the 45% stake in TIGF, totaling EUR1,456 million of net investment in the period.

This underlines the soundness of our growth strategy and our commitment to maintaining a solid and efficient capital structure. As of the end of September 2013 Snam's net debt was around EUR12.9 billion.

Let me now provide you with a quick overview of the gas demand trend in Italy. In the first nine months of 2013 gas consumption totaled 49.9 bcm, down 8.2% or 4.5 bcm year on year. This decrease was mainly driven by the reduction in gas consumption in the power generation sector.

In particular, the thermoelectric sector experienced a decrease of around 21%, driven by the reduction of 3.7% in the electricity demand, 9 terawatt hour, mainly due to the negative market economic trend; the remarkable recovery in hydroelectric production, 9 terawatt hour, driven by higher levels of rainfall, particularly during the first part of the year; the significant increase in electricity production from renewable sources, 5 terawatt hour, in particular solar energy.

These negative elements were partially offset by reduced usage of coal and oil products in the thermoelectric production.

Gas demand in the industrial sector decreased by around 3.8%, 0.4 bcm on like-for-like basis as a consequence of the declining trend in industrial production in Italy throughout the period. Gas consumption in the residential and commercial sector increased by 1.1%, 0.2 bcm. This was mainly due to the higher usage of gas versus other sources, in particular oil for household heating.

Finally, gas injected into the network for the first 9 months of 2013 decreased by 12.4%. The difference between gas injected into the network and the gas demand trend is related to the storage flow. In particular, the higher withdrawal from the storage site and the lower injection activity versus the same period of 2012 result in a negative balance of around 2.7 bcm.

For the full year 2013 our current forecast envisages a slight improved gas consumption trend than the one registered in the first 9 months, thus accounting a decrease in the range of 6% to 7%.

With regard to gas volume transported, we expect a recovery in the full year compared to the trend registered in the first 9 months as a result of the increase in gas demand forecasted by year and a neutral impact from storage activity.

That's all from me. I will now hand you over to Antonio, who will discuss our third-quarter consolidated result in greater detail.

Antonio Paccioretti, Snam SpA - CFO [3]

Thank you, Carlo, and good afternoon everyone. Looking at the consolidated income statement of the first 9 months 2013, EBITDA registered an increase of EUR51 million, up 2.5%. EBIT rose by EUR4 million, 0.3%, driven by the structural revenue growth as noted by the increase in deprecation.

Net profit for the period amounting to EUR674 million increased by about 31.4% compared to the same period of 2012 when registered one-off financial cost related to the unbundling process from ENI. Adjusting 2012 results by this effect, net profit declined by around 7%.

Total revenues increased by EUR97 million, 3.8%, compared to the first 9 months of 2012. The growth in regulated revenues net of pass-through components was driven by the following elements. Transport revenues grew by EUR38 million despite being negatively affected by the current decline in gas consumption trend. The positive contribution from the investments carried out in 2011, equal to EUR76 million, was partially offset by the annual tariff adjustment of EUR15 million and by the effect of the decrease of gas injected into the network of EUR23 million.

The increase in pass-through revenues was mainly due to the overall gas transport system balancing service.

Storage revenues grew by EUR40 million, a remarkable increase of about 13.5%, mainly due to the contribution from investments carried out in 2011. Distribution revenues increased by EUR8 million, mainly benefiting from the annual tariff adjustment.

Moving to the operating expenses, total cost increased by EUR46 million, mainly related to pass-through elements, concentrated among variable and other regulated costs. Controllable fixed cost in the first 9 month of 2013 were substantially flat. This result confirms our guideline for flat controllable fixed cost in real terms of a full-year basis.

Other costs, net of pass-through components, increased by EUR3 million because of the growth in concession fees for the distribution activity. Non-regulated costs amounted to EUR25 million, almost in line with the same period of last year.

Consolidated EBITDA amounted to EUR2,083 million, up 2.5%. Depreciation and amortization amounted to EUR567 million, an increase of EUR47 million compared to the same period of the previous year, mainly due to the new assets beginning operation and to the higher depreciation in the distribution business related to depreciation of the net consideration accounted for the new concessions.

Consolidated EBIT amounted to EUR1,560 million with an increase of EUR4 million.

Looking at each business segment contribution I would like to highlight the very strong performance by Stogit, which registered EBIT growth of EUR30 million, up 14.4%, driven by the increase in regulated revenues and the positive performance of Snam Rete Gas despite the negative effect of lower volumes. Italgas was however negatively impacted mainly by the increase in depreciation accounted in the period, while Snam's EBIT decline was a result of corporate not-regulated activities.

All in all, these results confirm the resilience of our business even in a challenging gas market environment in the first 9 months of 2013.

Net profit for the period was EUR674 million, up 31.4%, compared to the first 9 month of 2012. We have to consider the non-recurring effect of the unwinding of the interest rate swap accounted in 2012 equal to EUR213 million net of fiscal effects.

In addition to the aforementioned EBIT growth, the other factors impacting net profit were, firstly, the increase in interest expenses by EUR66 million, of which around EUR31 million of upfront fees paid last year related to the term loan financing subscribed in 2012 for an original tenure of 5 years and repaid in advance last April. Net of this effect, the increase of EUR35 million, was primarily due to the growth in our outstanding average debt over the period.

Secondly, the decrease in the net income from associates by EUR11 million, which was impacted by a non-recurring accounting item of EUR29 million related to the [pro-quota] tax burden paid by the French [bid co] for the acquisition of TIGF.

It is important to underline that this component was included in the total consideration of EUR597 million in Snam and was already priced in the total target return assumed for the acquisition. The tax rate was around 43%, almost in line with the previous period.

And now let's move on the results of the 2013 debt optimization exercise we highlighted at our mid-March strategy presentation. Today we are proud to confirm that most of the job has been done, achieving material benefit for our financial structure and cost of debt. Regarding our financial structure, we would like to highlight that today we have a significant liquidity buffer represented by around EUR3 billion of undrawn committed credit facilities net of the outstanding debt of around EUR1 billion of uncommitted facilities.

We will not need to carry out any major refinancing exercise until 2015. The average maturity of our outstanding medium- to long-term debt is around 5 years.

As for the latter, the contribution for these institutional lenders at the end of September amounts to around EUR1 billion, which include around EUR300 million of EIB -- European Investment Bank financing obtained in August. In addition, the same European Investment Bank granted a further EUR400 million -- around EUR400 million in October, which allows us to reach around EUR1.4 billion of financing from institutional lenders at the year-end.

It's worth reiterating the actions already completed. April bond issuance and term loan repayment for EUR1.5 in April. Dual tranche TAP in early September for EUR750 million with an average tenure of 6 years. One private placement in early September for EUR70 million at 5 years. Two private placement in October for around EUR400 million, including floating rate notes of around EUR300 million at variable rate at medium and long-term. Pool banking and bilateral facilities and renegotiation of margins and commitment fees for a total amount of facilities of over EUR5.3 billion mainly in the first part of the year. Cancellation of a portion of certain relatively expensive credit facilities maintaining at the same time strong liquidity profile.

These actions led to savings in net financial expenses that can be estimated in excess of EUR60 million on a full-year basis. These factors make us confident that we can achieve an average cost of debt of 3.7% in 2013, well below our March guidance of around 4% before the aforementioned actions.

In addition to the reduction in our cost of debt, we have also improved the quality of our financing days and the soundness of our debt structure by reducing the risks related to the interest rate exposure. Increasing fixed rate from 49% at 2012 year-end to 65% at the end of September and extending the duration of the same fixed rate debt to 5 years, thanks in particular to April and September bond issuances.

In this regard let me stress that given the timing of the execution, the impact of our optimization exercise in 2013 will be fully visible in 2014 when we expect further year-on-year improvement assuming an unchanged interest rate environment.

Turning to cash flow, in the first 9 months of 2013 the Group achieved a remarkable cash flow from operations of EUR1.480 billion, which enabled the Company to generate a positive free cash flow of EUR24 million, even after financing both technical investments and the acquisition of TIGF. Therefore, the increase of net debt in the period was limited to EUR479 million after the distribution of the 2012 final dividend.

Compared to the first 9 months of 2012, cash flow from operations more than doubled, in part thanks to the net working capital optimization. The main components of the increase are related to lower tax payment, which last year included the Robin Hood tax payment for 2 years, 2011 and 2012, and the effect of receivables not paid at the due date in relation to balancing activities accounted by the third quarter 2012 of about EUR400 million.

Looking at the cash flow -- cash component of the working capital in the first 9 month of 2013, the cash generation was EUR261 million, mainly due to the increase of tax payable accrued in connection with the profit of the period. Taking into consideration the expected dynamics of working capital for the last quarter of the year, we expect the level of working capital at the end of 2013 to be in line with year-end 2012.

I will now discuss CapEx in more detail, in the first 9 months of 2013 consolidated CapEx gross of subsidies was EUR775 million, down 3.1% compared to the same period in 2012. Under the current regulatory framework around 70% of the total CapEx is expected to receive a premium over the base return. CapEx for the transport and regasification businesses was around EUR398 million, approximately 50% of total CapEx. This was highlighting that 76% of the total amount is incentivized.

In particular, around 37% of the transport CapEx was deployed on the expansion of projects and new entry points with an extra premium of 3%. Investments in the storage business in the first 9 month of 2013 amounted to EUR155 million, representing around 20% of consolidated Group investments. Around 90% of storage CapEx received a 4% extra remuneration for 8 or 15 years.

Moving to the distribution business, CapEx amounted to EUR221 million. Around 16% of Italgas CapEx was related to cast iron replacement, while 24% was related to metering. For the full year 2013 we confirm the previously announced level of Group consolidated CapEx of around EUR1.3 billion.

Let's now move to the balance sheet. Fixed capital increased by EUR807 million compared to year-end 2012, mainly thanks to their -- the acquisition of the interest in TIGF, which drove the increase of EUR550 million in the equity-accounted and other investments. In addition, new CapEx for EUR775 million and the reduction of CapEx payable of EUR161 million were partially offset by depreciation of EUR567 million and subsidies of around EUR52 million.

Total net financial debt amounted to EUR12.877 billion, up EUR479 million compared to the year-end 2012.

Thank you very much for your attention. We are now pleased to answer any questions you may have.

Questions and Answers

Operator [1]

(Operator Instructions)

Javier Suarez, Mediobanca.

Javier Suarez - Mediobanca - Analyst [2]

I just have three questions on the Company. The first one is on the ongoing and regulatory review. Two questions on that front. One is your latest estimate for the timing of this regulatory review for transmission and distribution and also your reading or your takeaways from the document that the regulator has published for LNG terminal. I'm particularly interested on your view on the CPI that the regulator has used and any other cross-reading that this document could offer for the ongoing regulatory review for transmission and distribution?

Second point is on the, we have seen on the local press several articles related to the difficulties to develop a new LNG terminal. The difficulty that Gas Natural is having trying to get the approval for each facility, et cetera, et cetera. And I just wanted to have your update on how this whole situation of difficulties to develop new LNG terminal could be affecting the business plan of Snam. And related to that, I just wanted to have an update on your -- on the development of that and your potential interest on the that?

And the final question is on the extra financing that you have got from the EBC. The question is if you can give us a sense of how competitive is this extra financing that you have got, and related to that, which is your latest estimate or guidance in the cost of debt for the year 2014? Many thanks.

Carlo Malacarne - Snam SpA - CEO [3]

For the first question, Javier, the time -- we expect by the middle of November, during the month of November the final resolution by the regulators for the transmission regulatory review.

I think the question was the decision about the inflation, the CPI. I think that considering, for example, the regulatory framework of the regasification, the authority did not highlight the inflation rate utilized in the calculation of the work for LNG business, for example. Therefore, we cannot comment on an official data.

Anyway, let me remind you that it's clear that the regulatory body stated several times that the figure utilized by the government represents an important guideline to be used in citing the inflation rate. But they can't also take into account an analysis carried out by the independent bodies. So we, I cannot say today the number will be set and defined by the regulator.

For the second question, it's true that in terms of authorization today there is no decision, so final resolution about the LNG, the timing of LNG construction. What I can comment, I can say that anyway if you consider the rules, the policy set in the strategic energy plan by the government is one LNG is set source by the government to maintain the security of supply and efficiency supply in Italy.

I think that we have one LNG in south of Italy, the LNG by Enel in Sicily, which have today all the authorization, all the environmental authorization and the construction authorizations. At the same time, there is today some discussion about the definition, the resolution for the Gas Natural LNG in north of Italy, as you know, on the Adriatic Sea. And the approach today is that the Gas Natural can provide some comment, some new -- some update of the project set before to have the possibility to change the previous decision, a new way to speed the final decision. Only to say that it's clear there is no today a final investment decision, but my opinion is that I think during next year, 2014, it's possible to have some final investment decision for one LNG.

For TAP, we are following and we are discussing with the TAP consortium the connection with the pipe with Italy, and all our investment we have to provide to -- for the new 8 bcm supply. Today there is no interest of Snam to take part or to become shareholder in TAP. You know it's completely different, the strategy of the business. We are ready to set and to discuss with the regulator the rules for the booking capacity of TAP to speed all the criteria which will be set in the next year by the regulators to accommodate the new supply of TAP.

What I can say is that the new, if you can speak about new, of TAP is of that last September, as you may recall, some agreements have been signed with several international players, in particular Gaz de France, E.ON, Gas Natural and Axpo and the Italian ones and [Nera] for the potential new supply.

So it's a new signal, let me say. It's a new -- it's -- anyway the approach by the supplier is very positive, and I think the possibility of the final investment decision of TAP is very close. So in terms of our future investment CapEx is a positive news.

Antonio Paccioretti - Snam SpA – Planning, Administration, Finance and Control [4]

As far as the last question, Javier, between August and October we signed with the European Investment Bank new loans for a total amount of around EUR700 million. The tenure of those loans were up to 20 years for an average cost in terms of spread of around 80 basis point.

The effect is clear, that the effect of this recent funding is already considered in the guidance we gave you for 2013, which is an average cost of debt of around 3.7%.

Javier Suarez - Mediobanca - Analyst [5]

Thank you.

Operator [6]

Alberto Gandolfi, UBS.

Alberto Gandolfi - UBS - Analyst [7]

I also have three questions, the first one relates to CapEx. And can you please elaborate on where you see CapEx going next year in Italy, if the previous guidance is confirmed or if you're revising your plans? And can you talk a little bit more about your commitment to international growth and how would you fund it? And can you rule out big deals that may impact your capital structure, meaning, like equity, just for instance, or having to change your divided policy?

Second question, we have seen in the stability law there was no mention of the Robin Hood tax, can you -- do you have any insights to share with us about that? But it looks like, as things stand, the previous law applies and so it will be declining as of next year?

And lastly, I'm curious to see what's your bigger picture view on gas demand in Italy and Europe as a whole given energy efficiency and given in Italy particularly all these incentives to restructure housing and insulate houses. What do you think demand is going to be besides the normalization of gas utilization rate once the hydro level is normalized? But where do you see structurally gas demand in the next 5 years in Italy and in Europe? Thank you.

Carlo Malacarne - Snam SpA - CEO [8]

Thanks, Alberto. For the first question I confirm our CapEx plan by end of 2013 of EUR1,300 million and our previous commitment in 2014 of EUR1.4 million.

With regard, as regard our action and our activity outside Italy, today, frankly speaking, our approach is to define inside the agreement we have with FluxSwiss all the rules and criteria to be ready starting from the next spring, in April or May, to sign the first reserve flow contract.

So the activity is to work together. There is no, let me say, acquisition on the table. There is no -- there is only the commitment for the investment in Italy to provide the reserve flow, the commitment by FluxSwiss to provide the investment outside Italy, in Switzerland, in Germany, to have the possibility by 2015 to start with the reserve flow contract.

And I remind you that the reserve flow contract is not a question of increase of the gas demand but is the need by the supplier to increase the gas exchange to increase the arbitration to the European and Italian hub. And at the same time we have to consider that the overcapacity of gas in Europe, but in this moment in Italy, automatically need some activity by the supplier to accommodate, to bring some capacity from the take-or-pay contract outside Italy. So the reason why all the activity we are doing today is to be ready with the new contract of reserve flow.

We are analyzing today the impact of TAG. Our strategy at European level is to have the possibility to manage or, let me say, to control the development of the activity in the corridor north-south and east-west. The reason why I said a lot of time the TAG fit perfectly with our strategy. But today it's only an analysis and discussion. I don't have news today about the new pipe.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [9]

As far as the second question, I mean the growth, the possibility of growth abroad and the possible financial structure, the evolution on that, as you know, as you probably know this point was deeply elaborated in our last meeting with the investor and the analyst we had in the UK very recently. I shall try to summarize the main outcome.

As you know, first of all, it must be clear that any further international initiative that we could have must be current with our industrial strategy, which you know is aimed at implementing the south-north and east-west gas corridor. So the focus is, our interest is concentrated on that corridors, not elsewhere.

Needless to say that these -- that they must, that such a project must also provide the opportunity to create value for our shareholders.

What does it imply? This implies that should an additional opportunity arise we will evaluate it as our usual ways of taking into consideration, first of all, the industrial fit and using our strict financial discipline and, for going to the point, analyzing what could be the best financing in order to preserve the solid balance sheet we have and optimizing our cost of capital.

We have experienced the appetite of infrastructural fund, and in general I would say fund, sovereign fund in this kind of asset for TIGF, for TIGF we shared the commitment, the financial commitment with the financial operators with trust in our industrial expertise. And so we catch the point for the acquisition and the same time maintaining our balance sheet.

It is clear that we will evaluate this opportunity time to time for the future having in mind that the priority are, first of all, maintaining the balance sheet as strong as it is today, and, secondly, maintaining the shareholder return at the level we have.

Carlo Malacarne - Snam SpA - CEO [10]

The next question for the Robin Hood, I don't have, I do not have a specific comment. I can say that in our business plan we have considered for the future the existing law which set the tax of Robin Hood of 6.5% starting from January 2014. This is the base of which we will take -- we will carry out our program.

For the last question of the gas demand, I think it's very complex today to set some strategy in the gas demand evolution. And our expectation is that the gas demand will remain flat. By 2025 at European level we consider a CAGR of around 0.9%, in Italy around 1%, could be 1% is very conservative. We have to consider that in Italy in terms of strategic energy plan we have to reconsider to rethinking completely the strategy of the energy consumption in Italy.

We are not in the condition of some other countries at European level as, for example, Germany. In 2013 the reductions of the gas demand is due to the power generation. But at the same time we have in Italy in 2013, for example, a reduction in the coal consumption and oil consumption.

So the fuel for the power generation has been hydroelectric and renewable, a reduction in the electricity demand. That is the reason why the consequence, I think, in the next 5, 10 years is that renewable and gas will remain the main sources. And with this type of perspective, I think that is crucial to redefine the impact of the renewable in the possibility of power generation. So it's quite -- I think it's impossible that in the next 10 years the load factor in the combined cycle will remain 1,500 terawatt hour per year. So that is the reason why I think that it's true that there is a reduction of the gas demand. There is an efficiency in the gas consumption, but the gas will remain the main sources, anyway, if the renewable will increase. That is the reason why we consider in our plan a flat result of the gas demand in the next 3, 4 years.

We have at the same time to take into account that the reduction in the gas demand is due in part for roughly 1, 2 bcm from the industrial sector. So the other point is that I don't think that the industrial production will remain completely, let me say, out of the possibility of restart in the next 2 or 3 years. This is the reason why 0.9%, 1% CAGR in the next 3, 4 year in Italy is a reasonable expectation which we can do.

Operator [11]

Olivier Van Doosselaere, Exane.

Olivier Van Doosselaere - Exane - Analyst [12]

A couple of questions on my side, firstly, we have seen lately some press speculation about the government thinking about potentially selling some of its stake in its networks. I was wondering if you have any insight on that.

And then, secondly, with a cost of debt that is now at 3.7% gathered for 2014, given that it's actually an ongoing decrease, would it be fair to assume that for next year you will be probably closer to 3.5%?

And then a final question, maybe just some numbers, if you could give us a guidance on where you expect the calendar RAB to be at end of 2013 and 2014 and maybe also where you expect the net debt to be at the end of this year that would be great. Thank you.

Carlo Malacarne - Snam SpA - CEO [13]

Frankly speaking, I'm not used to comment the decision by our shareholder. Anyway, the only answer I can do is that the rumors in the press, anyway, have not impact in our shareholder structure. But I cannot comment the decision by the shareholder.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [14]

As far as the other two points, first of all in terms of cost of debt, I think that your estimation is reasonable, 3.5% could be used as a reference for next year. As far as the RAB evolution, the RAB at the end of this -- the guideline we gave in July as far as the calendar RAB at the end of 2013 is between EUR23.5 billion, EUR23.6 billion which with an increase of the previous year of around EUR600 million, EUR700 million. We think that ceteris paribus. Therefore, I'm assuming the same amount of investment, such a growth could be a reference for the next year.

Olivier Van Doosselaere - Exane - Analyst [15]

Thank you.

Operator [16]

Monica Girardi, Barclays.

Monica Girardi - Barclays - Analyst [17]

I just have one last question, and is on the what you define to be as an efficient capital structure. Antonio, I think, if I understood correctly, you mentioned at the end of the 9 months you had 65% of the debt that's fixed. I was wondering if this structure is, can be taken as a reference also for next year, so for the new regulatory period. Thanks.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [18]

First of all, I have to complete my previous question -- my previous answer. I missed to give the guideline for our debt at the end of this year, which remain the one we gave in July, around EUR13.6 million -- sorry, EUR13.6 billion.

As far as the, what we mean as a solid and efficient capital structure, it is what we think is the best tradeoff between solidity and cost. We want to maintain the capital structure permitting us to maintain this rating and therefore this cost of debt in terms of spread because I mean we cannot speculate on the future.

What we had decided in the last 12 month is to invest in security and to reduce the risk for our shareholders in terms of floating rates and increasing our fixed rate to 60% and so investing in duration. Our fixed rate has a duration of 5 years. The aim is to have an alignment between the duration of the regulatory periods and the duration of our fixed rate.

In terms of mix, I think that two-third -- 65% is a good reference for the future in terms of fixed floating -- fixed to total debt.

Operator [19]

Sarah Laitung, JPMorgan.

Sarah Laitung - JPMorgan – Analyst [20]

I have two questions. Firstly, could you give some insight into how you achieved the strong working capital management during the third quarter?

And the second question is, following the regulatory review for regasification, given that the volume linkage has been removed and so that reduces risk and also expansion CapEx will get a 2% premium, could you consider reviving the project to expand the capacity of the Panigaglia terminal, and if so how much could this add to your CapEx plan?

Carlo Malacarne - Snam SpA - CEO [21]

I'll start with the last question. In the regulatory, we have to highlight that it is clear in the document of the regulator that the regulatory review for the regasifications is for the existing plan in Panigaglia. We have today for the new plant or, let me say, the expansion will change completely the potentiality, completely the capacity, the regasification capacity of the plant. The regulators will take into account the specific plant or the specific, let me say, new plant with new rules.

That is the reason why the return of investment set is for the existing CapEx plan we have in Panigaglia. And you know we don't have in the 4 years CapEx plan the expansion of the regasification, is outside, is beyond 2017. So it's the CapEx plan presented to the regulator to define the existing regulatory regime. Only to say that I think that for the new regasification, anyway, and other regasification in Italy or big expansion with double capacity as Panigaglia we have to discuss the specific regulatory regime, the new specific regulatory regime with the regulators.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [22]

As far the net working capital dynamics, in the presentation we tried to confirm that as -- from a financial point of view the net working capital for this year has to be -- can be -- is expected to be considered, let me say, substantially neutral and so we expect a stock for working capital at the end of the year more or less in line with the beginning of 2013.

Looking at the cash component in particular or the working capital in the first 9 month which we closed with a cash generation of EUR260 million, I have to say that this is mainly due -- it is due to several elements, but among them I would like to underline first of all the increase of tax payable, which is in the -- around EUR250 million, which is clearly related to the increase of profit before tax. We have to pay tax in November, and therefore at the end of September it is ordinary dynamic having a fund from this element.

Let me remind you that the net working capital of the first 9 month is affected by the payment of about EUR140 million of -- for the -- which was the residual payment for the unwinding of the interest rate swap we paid to Eni, and therefore, with the other drivers we were able to mitigate the effect of this negative element.

Operator [23]

Jose Ruiz, Macquarie.

Jose Ruiz - Macquarie - Analyst [24]

Just two questions, one refers to Midcat. The EU has considered the project as strategic. After the Capital Day we had, does it change any way your expectations in terms of timing of this project?

And my second question, I was trying to calculate the impact or the consolidation, equity consolidation of TIGF. Removing the EUR29 million one-off, what would be the contribution in terms of earnings from the consolidation in just 2 months? Thank you.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [25]

If I understand well, as far as the impact on our accounts, please, first of all, it must be clear that TIGF is not consolidated, so we are talking about the impact on the net income from subsidies -- subsidiaries, sorry.

As far as the negative impact that we accounted, as was already said, is -- were in the estimation we made at the moment of the bid. It is something -- it was a tax that the bid co had to pay. It is a property tax actually due in France for this kind of transaction. It is something around EUR29 million for this year, which is the net between the tax -- the gross tax, which is EUR35 million pro-quota for us. And mitigated by the contribution on our income, which is for the period August and September because TIGF contributes only for

August and September in our accounts of EUR6 million and EUR7 million. So you have also all the elements for calculating the rest.

Carlo Malacarne - Snam SpA - CEO [26]

For the first question, for the Midcat, in the plan of TIGF it doesn't change the strategy today because anyway we considered the Midcat strategic and the decision by the European community is only a confirmation that it's a strategic pipe.

But in terms of business plan, TIGF was -- is not -- doesn't change, let me say, the number, the investment or the value of investment because it's today the new pipe outside the present CapEx plan set by TIGF. But is the new CapEx plan will be set by TIGF in the future will consider the investment of the Midcat.

Jose Ruiz - Macquarie - Analyst [27]

Thank you very much. Very clear.

Operator [28]

Alberto Ponti, Societe Generale.

Alberto Ponti - Societe Generale - Analyst [29]

I have two questions. The first is Standard & Poor have said that they want to review some of their criteria for assigning ratings, and in particular they may want to adjust the definition of gross cash flow. I haven't spoken to them about this. Does it have any impact?

And the second thing, the second question is more general. I remember if you go back few years ago, the rationale for convergence of electricity and gas regulation was that they have the same risks and therefore they should be remunerated with the same formula, same return. Obviously we have seen quite the opposite, that gas is riskier than electricity. There was the first risk of the introduction of nuclear in Italy, which didn't came to -- didn't come to fruition. And now we see renewables that have caused a substantial reduction in volumes.

So why do you think the regulator keeps stubbornly talking about convergence of returns when it's clear that transmission of gas is riskier than electricity? Thank you.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [30]

As far as the first question, Alberto, the -- we, as you probably can imagine, we are closely monitoring the evolution of these methodologies. We are part of these tables. I would say that the element you underlined is one of the element which is under discussion. But it's not the only one. All in all, we expect that the impact, the total impact of the possible new methodologies to be applied in our case, at least in our case will be substantially neutral.

Carlo Malacarne - Snam SpA - CEO [31]

For the second question, this type of discussion is a long discussion with the regulator we started 3, 4 years ago. And it's clear, it's true, I completely agree with you. What we have done in the last -- in this consultation, we provide to the regulator all the comments, the document to demonstrate and to, let me say, to provide all the technical data and the strategic evolution at European level which confirm the riskier aspect of the gas in respect of the electricity.

The regulator today has all the element, which is management element, strategic element, the possibility of share of the different fuel in Italy. But I'm not so sure that the previous decision to align the two business will be changed with the new regulatory regime.

I hope that we try in with all our possibility to demonstrate the difference. But I'm not so -- I'm not confident, let me say, that we reached the objective for the new regulatory regime.

Alberto Ponti - Societe Generale - Analyst [32]

It's very clear. Thank you.

Operator [33]

Roberto Ranieri, Banca IMI.

Roberto Ranieri - Banca IMI - Analyst [34]

Just one question, a very quick question on the CapEx portion with the higher remuneration, if I'm not wrong, from the presentation you basically -- your CapEx with the highest remuneration of 3% is decreasing, I'm wondering, just wondering if this -- in 9 month 2013

I'm just wondering if this trend will have a rebound on a more favorable trend for the rest of the year and for 2014? Thank you very much.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [35]

No, I would say that it is clear that the mix at the end of September in terms of incentivized or not investment is just the result of the different phasing of the different investments. Let me say that the guidance we gave in the past are confirmed.

Roberto Ranieri - Banca IMI - Analyst [36]

Thank you very much.

Operator [37]

Antonella Bianchessi, Citi.

Antonella Bianchessi - Citi - Analyst [38]

Just two questions, the first one is on the working capital. You recovered in the first 9 month, but you're saying that is going to be compensated in the last quarter. Why this is happening? You had outstanding receivable for unpaid balancing of gas you're not able to recover -- what is going in the fourth quarter?

The second question is really to go back on the CapEx. I mean, your CapEx plan have always been in the region of 6.4, 6.3. But if I cumulate the historical CapEx you have made, you never -- of the 4 year before, you never get to this number. So with your -- with this year CapEx and next year CapEx would imply that 2015 and 2016 CapEx will go up to 1.8 to meet your target of EUR6.2 billion in 4 year. Is this happening? And if this is happening, can you clearly explain which projects are -- you are delivering in that, in 2015 and 2016? Thank you.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [39]

I will start from the easier -- for the easier answer. Antonella, among the liabilities we have in the working capital, at the end of September we have, first of all, the tax that we have to pay. And so we have to pay in the second -- in November and therefore it is an outflow, in significant outflows.

The other important outflows is the dividend that we paid few days ago and which at the end of September was a part of the liabilities in the working capital. So those are the main reason for having a negative impact on the working capital in the last quarters.

Antonella Bianchessi - Citi - Analyst [40]

And just to be more precise, basically last year the working capital was particularly high because of the EUR400 million. And if it doesn't improve this year means that you don't expect this issue to be recovered or there is something else. This was really my question.

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [41]

I had to remember that the EUR400 million which you are mentioning at the end of this -- at the end of 2012 were for Tarvisio, so it is -- it was not a matter of working capital.

Antonella Bianchessi - Citi - Analyst [42]

Okay.

Carlo Malacarne - Snam SpA - CEO [43

For the second question, Antonella, we confirm today the CapEx of 2013 -- 1.4 2014. And it's true that we will have a peak of investment in 2015 and 2016. But we have to consider -- I think the question is we have to consider that the commitment of our existing project, so the reserve flow project, the Adriatic Sea connection with TAP and LNG will provide the total investment link to the project of EUR10 billion to complete the investment.

If you consider that the construction phase will last usually for 3, 4 years, it's true we have some delay, for example, in the first part of the Adriatic Sea. That is the reason why it's possible that there is -- there will be some tuning, but the total investment are EUR10 billion.

That is the reason why we expect a peak in the last year of -- in 2015 and 2016, only because when we start with the construction phase it's clear that we will have the peak of investment, which I think you have to take into account is the commitment for this project.

This project, the reserve flow, is under construction and we have an increase of the second part of the investment end of 2014, starting from 2015. For the Adriatic Sea, we start with the investment not only when we have the construction authorization, environmental authorization, but we start when we be sure that we have the transmission contract in place.

That is the reason why we are in the discussion. We are awaiting for the open season for TAP for LNG. And when we are ready to start, but we are waiting to be sure that we have all the transmission contract. There is no interest to increase the tariff with investment without the commitment.

So our approach is to finalize all the authorization process, if you need 2, 3 years. We know that in 3, 4 years -- 3, 4 years is the time for the construction. And the conclusion is that it's true, that could be that 2015, 2016, 2017 could be some peak of investments due to this type of approach.

Antonella Bianchessi - Citi - Analyst [44]

Okay, thank you.

Operator [45]

Stefano Gamberini, Equita.

Stefano Gamberini - Equita - Analyst [46]

Just a quick clarification about the RAB you expect at the end of the year, EUR23.5 billion, EUR23.6 billion. Is this calculated with a 2% inflation? And if you can elaborate what is the actual inflation you expect right now, because, if I'm not wrong, in the first part of the year it was in the region of 0.5%?

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [47]

In the guideline -- first of all, in the guideline we gave, we assumed an inflation of 1% for 2013.

Stefano Gamberini - Equita - Analyst [48]

Okay. So you confirm the guidance even with a lower inflation compared the initial one?

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [49]

No, actually I have to say that in July, if I don't remember -- if I remember well, the guideline was between 20 -- was -- the upper range was EUR23.6 billion assuming a higher inflation. I will say that EUR23.5 billion with 1% is a reasonable guideline.

Stefano Gamberini - Equita - Analyst [50]

Many thanks.

Operator [51]

Enrico Bartoli, MainFirst.

Enrico Bartoli - MainFirst - Analyst [52]

Just one question left, I was wondering if you can give us the feeling about your discussions about, with the rating agencies about your financial parameters, because after the acquisition of TIGF I guess that financial parameters in terms of net debt on EBITDA or net debt on RAB went up?

So do you have the feeling that the rating agencies are happy with this increase or it is consistent with the current level of rating? Or you think that in the future also considering that your CapEx is going to ramp up very significantly over the next few years, there would be some pressure to lower them or to change the rating? Thank you.

Antonio Paccioretti - Snam SpA – Planning, Administration, Finance and Control [53]

First of all, as you know, the relation with the two rating agencies is day-by-day relations in which we discuss everything. In particular there is a series of meetings in May, June in our case for discussing the business plan, for discussing the evolution of our financials.

I have to say that also in the last June so with all the financials rising from the TIGF deal we have received the confirmation that today we are, I would say, with reasonable buffer of security within all the metrics that they consider in -- for setting their evaluation. The same is for the future, we don't see any risk that -- any event today that could put at risk our rating.

Operator [54]

Anna Maria Scaglia, Morgan Stanley.

Anna Maria Scaglia - Morgan Stanley - Analyst [55]

Sir, two very quick questions and a clarification. The first one is on -- you said that you expect the transmission regulation to be published during the month of November. I guess the same is valid for distribution, if you can confirm.

And the second question, according to the regulator website you had a meeting with them early last week. I was wondering, is part of the discussion also a potential revision of allowed OpEx and allowed D&A? So there is room, in your view, of an improvement there? Thank you.

Carlo Malacarne - Snam SpA - CEO [56]

Can you -- the second -- the first question is clear, we expect by middle of November the transmission regulator. I don't know if it will be in the same time distribution and transmission. But anyway it could be that there is some delay from transmission and distribution. But anyway by the middle of November the transmission is -- will be in place.

I don't -- the second question, I think Antonio --

Antonio Paccioretti - Snam SpA –
Planning, Administration, Finance and Control [57]

Sorry, could you repeat? Not better elaborate, but elaborate once again for better understanding from our side the second part. So you mentioned depreciation, amortization and our expectation on that?

Anna Maria Scaglia - Morgan Stanley – Analyst [58]

Yes. Well, what I meant is what at the end -- people will tend to focus on the allowed return, but what at the end matters is the overall allowed revenue. And in the past both in your case or in Terna case we have been -- we have seen changes in allowed D&A and allowed OpEx, which were quite important. So I'm wondering besides the discussion on the allowed return if we could be surprised on allowed OpEx and allowed D&A, or no, or you think it is too premature?

Carlo Malacarne - Snam SpA - CEO [59]

In the discussion with the regulator it is clear that our approach is not only to discuss the beta level and or to understand the [VAC], but is, in general our approach is to define all the criteria which could increase or maintain our allowed revenue. So there is not only the cost but there is other technicality inside the regulatory regime which we try to manage and to discuss with the regulator to recover all the possibility advantage in our business.

It's very technical, let me say, discussion. But frankly speaking, I cannot say today our approach give us the possibility to increase independent of the (inaudible) our revenue. It is clear that there are, frankly speaking, some points today under evaluation by the regulator. For example, I can say, for example, the cost for the unbundling, so the cost we have sustained in the 2 years for the unbundling, the cost which we had by law, let me say, considering the unbundling law and the need to refinance the debt. So all this type of discussion were very in detail with the regulator. I'm confident that some positive effect will -- could -- let me say, we can receive some positive effect at the end of the new document.

Anna Maria Scaglia - Morgan Stanley - Analyst [60]

Thank you.

Operator [61]

As there are no further questions at this time I would like to hand the call back to the speakers for any additional or closing remarks.

Unidentified Company Representative [62]

Okay. Thank you everybody for participating in the conference call. If you need any further detail please contact the IR department. Thank you everybody.

Carlo Malacarne - Snam SpA - CEO [63]

Thank you. Bye.

Operator [64]

That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect.

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