



**Q1 2016 SNAM SPA
Earnings Call
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Corporate Participants

- [Antonio Paccioretti](#)
Snam S.p.A. - CFO
- [Marco Porro](#)
Snam S.p.A. - IR

Conference Call Participants

- [Harry Wyburd](#)
BofA Merrill Lynch - Analyst
- [Cosma Panzacchi](#)
Bernstein - Analyst
- [Oliver Salvesan](#)
Jefferies LLC - Analyst
- [Antonella Bianchessi](#)
Citigroup - Analyst
- [Javier Suarez](#)
Mediobanca - Analyst
- [Stefano Gamberini](#)
Equita SIM - Analyst
- [James Brand](#)
Deutsche Bank - Analyst
- [Olivier Van Doosselaere](#)
Exane BNP Paribas - Analyst
- [Maurice Choy](#)
RBC Capital Markets - Analyst
- [Rui Dias](#)
UBS - Analyst



Presentation

Operator

Good day and welcome to the Snam 2016 first-quarter results conference call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Mr. Antonio Paccioretti, CFO. Please go ahead.

Antonio Paccioretti , Snam SpA - CFO [1]

Good afternoon, ladies and gentlemen, and welcome to Snam 2016 first-quarter results presentation. As we go through the financial results for the first quarter and at the end of the presentation, I will be pleased to answer any questions you may have.

Let me start outlining the main business and financial highlights. In the first quarter, Italian gas market adjusted for weather condition increased by 1.2% compared to the last year. Following the recovery of gas consumption in the thermoelectric sector, where the volume of gas injected into the network was up 3.2% versus the same period as a consequence of lower gas storage withdrawals.

Looking at the financial performance, our results, well in line with the expectation, were impacted by the regulatory review that led to work reductions. The performance realized allows us to confirm the resilience of our business model, taking also into account our continuous focus on operational and financial efficiency.

With reference to our growth path, investment aimed to increase the flexibility, liquidity, and security of both the Italian and the European gas system, enhancing gas flows, and the interconnectivity of market across the EU. In the first quarter of this year, we deployed total CapEx of EUR231 million, fully financed by the operating cash flow. All these mentioned effects led to a solid balance sheet with a net financial debt of around EUR13.5 billion, down more than EUR200 million compared to 2015 year-end level.

I am now going to focus on our earnings results. EBIT amounted to EUR429 million, recording a reduction of about 16% or EUR81 million compared to the first quarter 2015. This decrease mainly reflects the reduction of regulated revenues following the lower



remuneration due to the regulatory review and increasing depreciation due to assets entered into operation.

Net profit decreased to EUR266 million. EBIT reduction was partially mitigated by the positive contribution of lower cost of debt following the continuous optimization of our financial structure.

Regulated revenues, net of pass-through items, showed a reduction of EUR52 million, down 6.1%, mainly due to the already mentioned work reduction in transport from 6.3% to 5.4%, worth EUR33 million in the period. And distribution business from 6.9% to 6.1%, worth EUR11 million as the positive contribution of new investments was counterbalanced by the effect of depreciation and the tariff adjustments.

Storage-regulated revenues recorded a reduction of EUR7 million due to some temporary tariff effects that would be recovered by the year end when we expect to see the full deposit contribution of the regulatory work increase in the storage segment from 6% to 6.5%. Finally, the reduction of other revenues was related to a lower disposal of nonoperating cash inventories in the transport business, down EUR20 million with no impact on margins.

Moving on to operating expenses, total costs in the first quarter amounted to EUR209 million, with a decrease of EUR3 million compared to last year. Controllable fixed costs decreased by EUR3 million in spite of the expansion of our business activities, mainly as a consequence of our continuous attention to efficiency gains and of a slight increase of internal capitalized costs.

Variable costs rose by EUR6 million and were related to balancing activities in transport business and energy efficiency certificates in the distribution segment. The increase of EUR21 million in other costs was mainly due to higher risk on provisions, EUR10 million net reversal in 2015 versus EUR10 million net provision in 2016. Cost of nonregulatory activities totaled EUR4 million, with a decrease of EUR19 million due to the already mentioned lower disposal of nonoperating gas inventories.

Consolidated EBIT amounted to EUR429 million with a decrease of EUR81 million compared to the first quarter 2015. This was the result of EUR52 million decrease in regulated revenues, the positive effects of the reduction in controllable fixed costs of EUR3 million, EUR7 million increase in depreciation, primarily as an effect of a significant asset capitalization in transport and storage businesses, and EUR25 million decrease of other components, mainly related to the already mentioned net change of risk on provision.



Turning to net profit performance, first quarter 2016 recorded a 18% reduction to EUR266 million. The decrease was mainly driven by the previously commented reduction of EBIT, partially offset by lower net interest expense of EUR4 million. The positive impact of a lower average cost of debt, EUR12 million, has been mitigated by higher non-cash item of EUR8 million, mainly due to lower interest during construction following the already mentioned significant asset capitalization.

Non-consolidated assets contributed to first-quarter 2015 results for EUR31 million. The reduction of EUR10 million is essentially due to a different timing profile of quarter results, mainly related to TAG, that we expect will be recovered by the end of this year.

Now let me give you an overview of Snam's debt structure. As regards debt breakdown, the fixed rate portion is 65%, in line with our plan to have around two-third of our debt at fixed rate. The maturity profile is well spread over time, avoiding major concentration issues and going forward, with an average maturity of our medium- to long-term debt of around five years.

As regard our strong liquidity profile, our buffer is represented by around EUR4 billion of undrawn committed credit facilities covering 18-month maturities. Also thanks to the full effect of the optimization measures carried out in the second half of last year, and in particular the liability management exercise carried out on November, made it possible to achieve an average cost of debt in the first three month of 2016 of around 2.6%.

Turning to the cash flow, funds from operations amounted to EUR572 million with a positive contribution of working capital for EUR121 million, mainly related to tax payables accrued in the period. The positive contribution of net trade payables in the distribution business, mainly due to revenues' seasonality, has been entirely counterbalanced by the reduction of net trade payables in the transport business, mainly related to balancing activities.

The cash flow from operations fully financed net CapEx of EUR321 million, resulting in a positive cash flow of EUR251 million. Thanks to the contribution of the cash flow, net debt at the end of the first quarter 2016 amounted to EUR13.5 billion, recording a reduction of more than EUR200 million compared with 2015 year end.

Thank you very much for your attention. I am now pleased to ask for any question you may have.



Questions and Answers

Operator [1]

(Operator Instructions)

Marco Porro - Snam S.p.A. - IR [2]

Good afternoon, everyone. This is Marco Porro speaking. Before we start the Q&A session, we would greatly appreciate if you could focus your question just on the first-quarter results.

Forward-looking statements, both strategic and financial, will be provided during the strategic review early this summer. And on the same date, we will also comment in detail on the results of our ongoing feasibility study for the merger of Italgas. Thank you in advance for your cooperation.

Operator [3]

Harry Wyburd, Merrill Lynch

Harry Wyburd - BofA Merrill Lynch - Analyst [4]

So unfortunately, you knocked out most of my questions there. So I will focus on the first-quarter results, then. In your increase in other costs, you talked about the provisions for risks and charges. And in the press release, there's a mention of some increases in provisions for storage remediation.

So could you give us a bit more detail on that? And let us know whether there will be further provisions for storage remediation or any other type of remediation later in the year? That's my only question, actually. Thanks.



Antonio Paccioretti - Snam S.p.A. - CFO [5]

In relation to the provision, risk on provision, the higher cost is the result of -- they are a cost of EUR20 million, say around EUR20 million as a result of a positive utilization of the risk on provision of last quarter or the first quarter 2015 for EUR10 million. And the provision for this quarter, for the first quarter 2016, of EUR10 million. The final result therefore is a cost of EUR20 million.

In relation to the storages, revenues for storages, the reduction of the revenues in first quarter versus first quarter is just the result of a different distribution of revenues, which characterized the previous regulatory period that expired at the end of the first quarter 2015.

All in all, we expect this -- the evolution of revenues at the end of this year will result in the increase of revenues we expect for -- resulting from the increase of work. So we are talking about an expectation of higher revenues of around EUR20 million.

Harry Wyburd - BofA Merrill Lynch - Analyst [6]

Okay. So in the [press release], you mentioned something about provisions, recent charges on an adjustment for dismantling and restoration for storage sites. So has that provision in particular impacted earnings in the quarter or not?

Antonio Paccioretti - Snam S.p.A. - CFO [7]

No, the risk provision I was mentioning before is not due to the restoration of any -- on any site or storage site. It just referred -- must be referred to risk on provisions, legal proceedings, and so on, distributed among the different business segments we have.

Harry Wyburd - BofA Merrill Lynch - Analyst [8]

Thank you.

Operator [9]

Cosma Panzacchi, Bernstein.



Cosma Panzacchi - Bernstein - Analyst [10]

Thank you for taking my questions. I have two on gas distribution. Basically in this first quarter, we have seen that you have a field against the gas distribution tender in Venice. And the administrative tribunal is expected to rule on the appeal today.

So is there a risk that a ruling in your favor may put the gas distribution standard process entirely on hold? And if yes, could this effect the potential growth of Italgas? And finally, more in general, what is your view at this point on the current status of the gas distribution tender process in Italy? Thank you.

Antonio Paccioretti - Snam S.p.A. - CFO [11]

So we are starting from the situation in Venice. The recourse refers to the fact that -- first of all, it refers to the fact that the tender we believe was not current with the applicable low-end regulation. And therefore, we believe it do not allow the operators to submit a full and competitively binding offer.

The objective -- the target of the recourse is to obtain the issue of a new tender that is compliant with the law that allows to all the operators to bid in a transparent and competitive way. We do not have any information for giving you the possible effect of this decision on the calendar or the schedule for the entire schedule for the concessions. What we can say is that Italgas is ready for the start of the concession tender process and we believe the first concession could start in the second half of the year.

More in general term, we believe that a certain number of concession will start by the end of this year. However, we still -- second part of this year, with the wording, not before the end of 2017. However, we still expect the total length of the process to last around four to five years.

Cosma Panzacchi - Bernstein - Analyst [12]

Thank you.

Operator [13]

Oliver Salvesan, Jefferies.



Oliver Salvesan - Jefferies LLC - Analyst [14]

Just one quick question. Would you be able to go into any more detail on the move in equity consolidated income in the first quarter? And could you give us an indication of what you expect for the full year from this line? Thank you.

Antonio Paccioretti - Snam S.p.A. - CFO [15]

In the first quarter, net income from SOCs amounted to around EUR30 million -- EUR31 million, exactly. And it was due to the contribution of the international activities, EUR26 million, and the contribution of the Italian distribution associates, which is Tuscan Energia, totaling EUR5 million.

For the international activities, the total of EUR26 million related to target for EUR18 million, TIGF for EUR7 million, UK, the interconnected, for EUR2 million, and TAP, which -- for TAP, we have a negative result of EUR1 million, which is the per-quarter -- the amount of -- the per-quarter amount of the cost of the company, which are not capitalized. You know the company is in a startup phase.

The amount of it are almost fully capitalized. There is a marginal number, which constitutes for us -- has for us a negative impact. For this quarter, it is something around EUR1 million.

Let me say -- let me underline that the reduction of income from the participation in TAG this quarter we had a contribution lower than the first quarter 2015 is a consequence of the temporary accounting affects related to the PPA in the first quarter of 2015 that we believe will be recovered within the year. So on a yearly basis, TAG income is expected to be substantially in line with 2015 results.

Oliver Salvesan - Jefferies LLC - Analyst [16]

All right, thank you very much.

Operator [17]

Antonella Bianchessi, Citigroup.



Antonella Bianchessi - Citigroup - Analyst [18]

Just a quick question on your OpEx in Q1. Yesterday, you mentioned the provisions, changes, and [such]. But can you just give us a dynamic clean of that? Because we are seeing also that the pass-through revenues are going down. So I would suppose that those are the pass-through costs that of going down.

So if you could give us a clean trend of this and what you expect on a full-year basis. And which are the measure that the Company can still put in place in order to control the OpEx.

The second question is when looking at your EBIT, EUR429 million, I remember Mr. Malacarne anticipated a target for EBIT in 2016 of EUR1.8 billion. So can you elaborate if you think that after this quarter, you are still on track on the EBIT and which type of EBITDA this would imply. And yes, this is pretty much all my questions. Thank you.

Antonio Paccioretti - Snam S.p.A. - CFO [19]

I will start from the expectation we have in terms of OpEx for the full year. I would reiterate the guideline we gave in the past, which is that in terms of controllable fixed costs, we expect to have a base -- an expectation of around EUR500 million. In our business model, a controllable fixed cost represent -- usually represent around 70% of the total cost.

In focusing on the first quarter, I believe -- I think that all in all, if I don't remember well, the comparison shows a slight increase of around EUR5 million. The important number for me is the evolution of the controllable fixed cost, so a reduction of EUR3 million that we -- you know, represent for us the measure on which we commit our capacity to maintain -- to deliver our efficiencies.

For the last question, which is the -- all in all, the possible guideline we can give you in terms of EBIT. I think that considering the reduction of revenues, which are characterized due to the work reduction, which characterized this year, together with the increase of depreciation that we expect for the important amount of investment entered into operation last year, the increase of depreciation we have in mind -- we expect for the full year is a number between EUR40 million and EUR45 million. We believe that the most appropriate guideline for EBIT is something up to the mid-range EUR1.7 billion, EUR1.8 billion.



Antonella Bianchessi - Citigroup - Analyst [20]

Thank you.

Operator [21]

Javier Suarez, Mediobanca.

Javier Suarez - Mediobanca - Analyst [22]

Just one question remaining. It is on the cash flow statement. On one of the slides, you are showing a positive working capital effect of EUR121 million. If you can kindly review to us and explain us the reason for that positive impact on working capital for EUR121 million?

And then on the strategy presentation, obviously without entering into details, what is your latest expectation on the timing for that presentation? On the press release that in which you communicated you were starting the potential spinoff of Italgas, you were mentioning something like before end July. Can you elaborate a little bit on your latest thought on the timing for that presentation? Many thanks.

Antonio Paccioretti - Snam S.p.A. - CFO [23]

Starting from the second question, our calendar provides for the -- for one Board at the end of July. We are working for having the presentation -- a strategy presentation with the result of our feasibility study in relation to Italgas before, I will say, end of June.

In relation to the dynamics of the working capital, as you know, Soviet dynamic in the first quarter is the ordinary one. We do not pay tax; we -- on the net income we create in this quarter because the [rev] on tax are paid in May. So the EUR120 million of decrease in working capital, so increasing the cash flow, is related to this effect. There are other effects that at the end they mitigate -- they neutralize each other.



Javier Suarez - Mediobanca - Analyst [24]

Thank you.

Operator [25]

Stefano Gamberini, Equita SIM.

Stefano Gamberini - Equita SIM - Analyst [26]

Just two question. The first regarding the cost of debt. You spent 2.6% for the first quarter. Could we have the same guidance also for the full year? And regarding the lower capitalization of EUR8 million in the first quarter, if we have to multiply for four in order to have the capitalization -- the lower capitalization for the full year.

And the second -- just regarding your guidance of [EBITDA] between EUR1.7 billion, EUR1.8 billion. So you said that the position will be up EUR40 million, EUR45 million, so quite a limited range as well as regarding the OpEx -- the visibility is quite high. So could you share with us what are your thoughts regarding the revenues that could change by EUR100 million in order to have such a wide range of EBIT. Many thanks.

Antonio Paccioretti - Snam S.p.A. - CFO [27]

Stefano, starting from the first question, if I understood well, in the first quarter, we have a cost of debt of around 2.6% and this is still the guidance for the full year. We had a reduction in the first quarter, reduction of -- in terms of financial charges of around EUR4 million, which actually was the compensation of a reduction in the financial -- cash financial charges paid of EUR12 million, and the increase of non-cash item around EUR8 million, out of which -- of which 50% -- around 50% are lower [entering] during construction.

And the other 50% is the accounting effects, the non-cash accounting affect of the calculation of the current value of the long-term liabilities. I'm talking about this monthly fund, which is due to the lower interest rational.



So trying to answer to your question, the increase -- sorry, the decrease of entering during construction for four is not to multiply by four for the full year. I would say that the original guideline for this lower entering during construction for the full 2016 is something around EUR10 million.

The other question was related to the guiding of our EBIT. I would say that the guidance is just what we have discussed yesterday. And the Board is based on the most recent expectation that the Board has elaborated yesterday. And we will see in the second part -- in the [receivable], three quarter of the year, which will be the evolution. For sure, the results. This is an all-in-all guidelines, which also include the expectation we have in OpEx -- in operating costs.

Stefano Gamberini - Equita SIM - Analyst [28]

Thanks.

Operator [29]

James Brand, Deutsche Bank.

James Brand - Deutsche Bank - Analyst [30]

Just one question left, if I may. Just wanted to ask around the mid-period gas distribution review, whether you see the shift to a totex regime as being an opportunity for you. Thanks.

Antonio Paccioretti - Snam S.p.A. - CFO [31]

If I don't make a mistake, it is a consultation document that is just -- for the distribution has just issued. It's just a matter of some days -- the beginning of this month. So let me -- let us evaluate in details in depth the documents.

All in all -- in general terms, let us say that the introduction -- the possible introduction of this methodology for a company -- efficient company like Italgas are to be considered an opportunity of value creation. As we did -- as Italgas also did in terms of efficiency gains in relation to OpEx could be also done in relation to the other -- to CapEx. And therefore the totex is something that could be an opportunity for us.



James Brand - Deutsche Bank - Analyst [32]

Thanks.

Operator [33]

Olivier Van Doosselaere, Exane.

Olivier Van Doosselaere - Exane BNP Paribas - Analyst [34]

Thank you very much for taking my question. I only had one left, if we focus just on the Q1s. You said that there was some temporary effects that affected the associates in the first quarter. I was wondering if you could give us the guidance of where you expect associates to be for the full year 2016. Thank you.

Antonio Paccioretti - Snam S.p.A. - CFO [35]

Last year, we have a contribution from our -- in terms of full year. Our affiliates of around EUR135 million, out of which EUR10 million was the nonrecurring accounting items due to the revaluation of certain asset -- [Accam], Accam in particular -- following the acquisition -- the consolidation of debt. I would say that EUR125 million also for this year could represent a reasonable guideline.

Olivier Van Doosselaere - Exane BNP Paribas - Analyst [36]

Thank you very much.

Operator [37]

Maurice Choy, Royal Bank of Canada.

Maurice Choy - RBC Capital Markets - Analyst [38]

Thank you for taking my call. Just one question from me and it's more about I guess the strategy for your debt moving forward. Obviously at Q1, your mix between fixed and floating are -- it's relatively similar to your year end.



I just wanted to understand whether or not you feel that it is about time to begin increasing your exposure to fixed rate debt, I guess today or within the next few months, rather than the -- in a year or two's time. Can you just help us think about that? Thank you.

Antonio Paccioretti - Snam S.p.A. - CFO [39]

I think that everyone in this interest scenario is considering the possibility to increase the fixed rate portion of debt. Anyway -- and also for us, it is something that we are evaluating. For us anyway, we have to consider the choice of the Company to maintain a proper alignment between our -- between the duration of our assets, which you know reset -- the return on which reset periodically, and the duration of our liability.

Having said that, I believe that we -- by the year end, it will be our -- it is in our program to execute part of our liability management in order to maintain the advantage we have today.

Operator [40]

Rui Dias, UBS.

Rui Dias - UBS - Analyst [41]

My question on equity investments has just been answered, so allow me to go back to your EBIT target. So as far as I understand, the guidance was an EBIT for the full year of around EUR1.8 billion. But you just mentioned a EBIT on the top half between EUR1.7 billion and EUR1.8 billion. Is this right? And apology if I missed something. Thank you.

Antonio Paccioretti - Snam S.p.A. - CFO [42]

I repeat, the guidance is an [EBITDA] in -- up to the mid-range, EUR1.7 billion, EUR1.8 billion.

Rui Dias - UBS - Analyst [43]

Thank you very much.



Operator [44]

Antonella Bianchessi, Citigroup.

Antonella Bianchessi - Citigroup - Analyst [45]

Sorry to insist on the full-year guidance on EBIT, but the CEO just mentioned EUR1.8 billion three weeks ago. Now he thinks that the guidance is a little bit lower. Can you elaborate on which are the reason for being more cautious into 2016?

Secondly, is it correct that if we add up like 870, 880 of the provision, we will get to overall guidance in terms of EBITDA below EUR2.7 billion?

Antonio Paccioretti - Snam S.p.A. - CFO [46]

Antonella, I believe that I have been very clear about our guidance. Those are the results of the discussion that the Board has yesterday. I believe that I cannot add anything that can contribute to your concern.

Antonella Bianchessi - Citigroup - Analyst [47]

Thank you.

Operator [48]

It appears there no further questions at this time. I would now like to turn the conference back over to today's speaker for additional or closing remarks.

Marco Porro - Snam S.p.A. - IR [49]

So if there are no more questions, thank you, everybody. And if you need any additional follow-up or information, please contact the IR department. Thank you, everybody.

Operator [4]

That will conclude today's conference. Thank you for your participation and have a good day.



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