2016-23: New regulatory period for electricity distribution in Italy

January, 21st 2016

New regulatory period for electricity distribution in Italy
Highlights

Overall framework
Stable and supportive of network investment plan

2016 tariff revenues
Estimated reduction by 5% from 4.81 €bn in 2015 to 4.55 €bn in 2016
WACC revision from 6.4% to 5.6%

2016 regulated asset base
Estimated at ~21 €bn

Overall in line with expected regulatory scenario in November plan

New regulatory period for electricity distribution in Italy
Summary of the regulatory decisions

Resolutions

Published

- **654/2015 -** Tariff general framework
- **583/2015 -** WACC
- **646/2015 -** Quality of service and output based regulation

To be published

- Final allowed revenues
- Smart meters regulation

Main changes	Longer regulatory periods
	New WACC methodology
	Regulatory lag reduction
	Gradual approach to the extension of asset life
Key confirmations	Allowed opex
	No exposure to energy volumes
	Quality of service
Pillars for the future	New framework for innovative investments
	Smart meters regulation draft
	Totex regulation starting from 2020

New regulatory period for electricity distribution in Italy
Main changes: longer regulatory periods

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Previous regulation (2012-15)	New regulation (2016-23)
Tariff /WACC regulatory period: 4 years	**Tariff regulatory period: 8 years**
2012 – 2014 – 2015	2016 – 2020 – 2023
WACC mid term review only for risk free rate	*Tariff mid term review Start of TOTEX regulation*
	WACC regulatory period: 6 years
	2016 – 2019 – 2021
	WACC mid term review already defined for all main parameters

Greater stability thanks to longer regulatory periods

Main changes: new WACC methodology (1/2)

New methodology to stabilize fluctuations in interest rates and inflation

2016-18	Real pre-tax WACC set at 5.6% vs. 6.4%
2019-21 Future updates	New methodology defined for all main parameters

A new approach to manage the new macro-economic scenario

New regulatory period for electricity distribution in Italy
Main changes: new WACC methodology (2/2)

	2016-18	Update rules (2019-21)
Real risk-free rate	0.5%	October 2017- September 2018 high rating Countries risk free rate – 0.5% floor
Country risk premium	1%	Based on Italy-Germany 10 year bond spreads change in 2018 vs. 2015
Equity risk premium	5.5%	Based on the new Risk Free Rate and on a fixed 6% Total Market Return
β unlevered	0.39	Potential update in 2019 within tariff regulatory period
Debt spread	0.5%	No interim update
Gearing = D/(D+E)	0.44	Alignment to European benchmark - cap 0.5
Tax shield	27.5%	To be updated at the end of 2018
Tax rate	34.4%	To be updated at the end of 2018
Inflation rate	1.5%	European Central Bank forecast at the end of 2018
"F" Factor	0.5%	Resulting from the update of Tax rate, Tax shield and Inflation
WACC real pre-tax	**5.6%**	

New regulatory period for electricity distribution in Italy
Main changes: regulatory lag reduction

	Previous regulation 2012-15	New regulation 2016-23
Remuneration on RAB	▪ Year *t-2* capex included in year *t* RAB ▪ +1% WACC for new investments	▪ Year t-1 capex included in year t RAB ▪ +1% WACC premium on 2012-14 capex replaced by a RAB uplift
Allowed depreciation	▪ Year t-2 capex included in year t Depreciation	▪ Year t-2 capex included in year t Depreciation

Lag reduction to 1 year with neutral NPV and positive effects on cash flow

New regulatory period for electricity distribution in Italy
Main changes: extension of asset life

Life for MV and LV lines built after 2007 extended from 30 to 35 years

Further possible revision with the introduction of Totex mechanism in 2020

Gradual reduction of allowed depreciation

New regulatory period for electricity distribution in Italy
Key confirmations: allowed opex (1/2)

Allowed opex composition

50% of 4th regulatory period extra efficiencies
Residual value of 3rd regulatory period extra efficiencies
2014 opex

- Allowed opex calculated on 2014 costs
- 50/50 profit sharing for the 4th regulatory period extra-efficiencies
- Residual value of 3rd regulatory period and 50% of 4th regulatory period extra efficiencies to be returned to consumers by 2019 via the X-factor

Allowed opex regulation broadly confirmed

New regulatory period for electricity distribution in Italy
Key confirmations: allowed opex (2/2)

	Previous regulation 2012-15		New regulation 2016-23	
Distribution	2.8%	X-factor set to return to consumers the 2nd and 3rd regulatory period extra-efficiencies (by 2015 and 2019 respectively)	1.9%	X-factor set to return to consumers the 3rd and 4th regulatory period extra-efficiencies (both by 2019)
Metering	7.1%		1%	
Weighted average	3.1%		1.8%	

X-factors set only to return previous periods extra-efficiencies by 2019

New regulatory period for electricity distribution in Italy

Key confirmations: no exposure to energy volumes

Allowed revenues will continue to be based on the average number of customers

Allowed revenues to be guaranteed by an equalization mechanism

No exposure to energy volumes

New regulatory period for electricity distribution in Italy

Key confirmations: quality of service

Stable incentive mechanisms on frequency and duration of interruptions

Frequency: four year extension supportive of structural network investments

Duration: premium maintained to sustain the high quality levels already achieved

Quality of service regulation broadly confirmed

Pillars for the future: new framework for innovative investments

New regulatory mechanism "Output based"
replacing extra WACC remuneration

New bonus mechanisms based on a benefit sharing
between the distributor and the system

First two main innovative functionalities on MV grid
RES observability systems and advanced voltage regulation to increase RES hosting capacity

New regulatory framework as fundamental enabler
for the future smart grid development

New regulatory period for electricity distribution in Italy

Pillars for the future: 2nd generation digital meters

New meter functional requirements definition ongoing

Cost benefit analysis process in line with European guidelines

Potential first TOTEX application on the second generation meter investment

Smart meters regulation to be finalized by first half 2016

New regulatory period for electricity distribution in Italy
Estimated revenues and RAB

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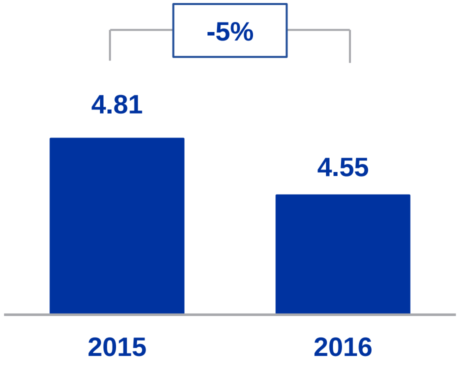
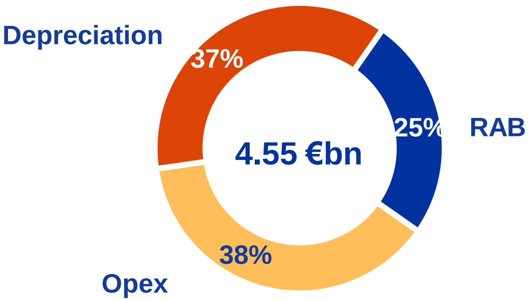
Allowed revenues[1] (€bn)



2016 revenues breakdown



Estimated Tariff RAB[2]	~21 €bn

Estimated 2016 revenues in line with November plan assumptions

1. Enel estimates based on criteria foreseen by the resolution and on tariffs applied to customers; final allowed revenues will be published in April - July
2. Including estimated NPV of depreciation of electromechanical meters as per Resolution n. 654

New regulatory period for electricity distribution in Italy
Closing remarks

A new regulatory framework to face the current macroeconomic scenario and system needs

2016 estimated results in line with November business plan figures

A positive context to encourage investment in networks and innovation

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Contact us

Investor Relations Team (investor.relations@enel.com)

Tel. +39 06 8305 7975

Visit our website at:

www.enel.com (Investor Relations)