

2.6 Strategic Foundations

for 2018-2022

Market conditions

Compared to prior forecasts, the current scenario for the energy markets during the 2018-2022 period calls for slightly higher electricity prices in Spain and the United Kingdom during the first two years of the period, explained by an increase in fuel prices. Over the longer term, the forecasts are for continued stability in prices.

The energy policies of the countries in which the Group does business continue to encourage investment in generation technologies based on renewable sources as well as the expansion, modernisation and digitisation of networks for the integration of elements of distributed generation and new renewable generation capacity.

Within this context, the diversification of businesses and countries will allow the company to develop its strategy of growth and value creation.

Challenges and opportunities

Challenges

- Decarbonisation in the energy sector. Demand for cleaner and more sustainable energy.
- Management of a scenario of constant prices for energy in the medium term.
- Attainment of higher efficiency levels in all businesses, applying innovation and digitisation in operations.
- Regulatory management in all businesses, with special emphasis on transmission and distribution businesses, and in the development of the single market in Europe.
- Implementation of an investment plan focused on growth in the businesses of regulated networks, renewables and long-term contracted generation.

Opportunities

- Balanced business model focused on regulated activities and renewable generation.
- Significant experience in the development and construction of network and emission-free generation projects.
- International diversification with a presence in countries with stable and predictable regulatory frameworks that require investment in the electricity and gas sectors.
- High quality of assets.
- Proven management capacity, culture of efficiency and results.
- Culture of innovation to implement digitisation in relation to customers and the development of new products and services.

Growth vectors 2018-2022

Investments

- United States: The company, through Avangrid, will continue with new onshore wind developments, taking advantage of the extension of tax credits to 2020, and is developing a significant portfolio of offshore wind projects. It is also facing growth in the area of distribution networks as well as in transmission.
- Mexico: It will consolidate its position as the largest private power generator in Mexico, through new plants under long-term contract with the Federal Electricity Commission (*Comisión Federal de Electricidad*) (CFE), and also taking advantage of the opportunities arising from the liberalisation of the sector.

- United Kingdom: Iberdrola continues with its growth phase in the power transmission and distribution businesses and with the start-up of onshore and offshore renewable energy projects. Offshore wind will gain significance beginning in 2019.
- Brazil: Strengthened growth in renewables, maintaining its position as largest electricity distributor by number of customers.
- Spain: Maintenance and improvement of facilities. Growth in smart grids.

Operational efficiency

- In all areas of activity, with a plan to save €1,300 million over the period.

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Strategic pillars

Iberdrola’s proposed creation of value for the 2018-2022 period is supported by five strategic pillars: investment in projects with long-term profitable growth, operational excellence, a customer-focused business model, optimisation of capital invested, and finally, innovation and digitisation to optimise costs and create new opportunities within all of the businesses.

1. Balanced growth

The company will undertake a number of initiatives to develop this strategy, as described below:

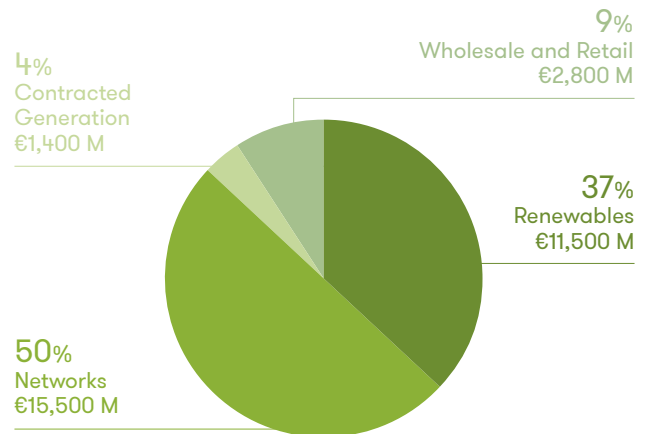
- Decarbonisation policies and technological change play an important role, as they will encourage significant investments in renewable generation and networks, supporting the growth of these businesses and contributing to improvements in efficiency.
- Within this context, net investment will reach €32,000 million, an increase of €2,000 million compared to the prior plan, excluding Neoenergia. Investments in Brazil reach a total of €5,000 million, which will be one of the engines for growth.
- The investments are focused on business and countries with stable and predictable regulatory frameworks; 90% of which will be dedicated to regulated activities or long-term contracts.
- Of the €32,000 million in planned investments, 75% are for projects secured as of today’s date or that are highly likely to be executed.
- Electric power transmission and distribution networks will absorb 50% of net investments, €15,500 million. Of the overall amount, 37% and 4%, respectively, will be dedicated to renewable energy and long-term contracted generation. 9% of the total will be invested in the Wholesale and Retail business.
- Geographically, Iberdrola will concentrate the bulk of its growth in the international area. By currency, 38% will be invested in dollars, 19% in pounds Sterling, 25% in the Euro zone and 18% in Brazilian reais.

Investments continue to be concentrated on regulated activities and long-term contracts, which represent 90% of the total investment. By business, Networks will absorb 50%, €15,500 million.

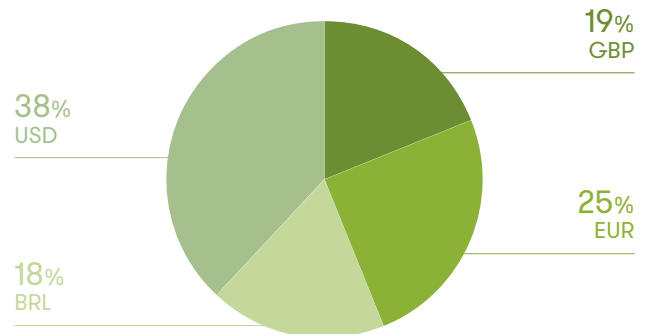
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Investment by business and currency 2018-2022

Investments of the Businesses⁽¹⁾



Investment by Currency



(1) Excluding Investments of the Corporation.
 (2) Including hydroelectric.

2. Financial strength

Net Profit reached 2,804 million euros in 2017, with growth of 3.7% thanks to the group's business model, in a year that was strongly affected by poor hydraulic conditions and the situation in the United Kingdom wholesale and retail markets.

The positive impact of the United States tax reform, together with the gain from the Gamesa-Siemens merger, were mainly allocated to provisions and to adjust the value of certain assets. This will allow us to improve the group's future results.

Consolidated EBITDA decreased by 7.8% to €7,318.7 million, with a good showing by the Networks business thanks to the United States and Brazil (positively affected by the inclusion of Neoenergia) and contracted generation in Mexico, which was overcome by the impacts explained above.

This reported EBITDA includes €203 million of provisions for the efficiency plan 2018; adjusted EBITDA is thus €7,522 million.

During the 2018-2022 plan, the company will continue to grow and increase in profitability, reaching EBITDA of between €11,500 million and €12,000 million by 2022, and net profit of between €3,500 million and €3,700 million based on currently estimated exchange rates.

80% of EBITDA will come from regulated activities or long-term contracts, 35% in euros, 29% in dollars, 20% in pounds and 16% in Brazilian reais.

The profile of the company's businesses, together with a balanced investment plan, will allow for sustained growth in EBITDA and Net Profit.

- Funds from operations (FFO) will grow 34% compared to the prior Plan, to €4,200 million for the 2018-2022 period, amply exceeding the investments of all of the businesses, which will reach a total of €32,000 million.
- Maintenance of the current financial model to provide subsidiaries with an optimal capital structure giving appropriate financial signals and which is consistent with an investment grade rating, while respecting current guidelines for structural subordination.
- Optimisation of liquidity position (around €8,000 - €10,000 million, with a margin to increase it if necessary) to current market conditions in order to improve financial costs, maintaining 18 months of coverage even during stress scenarios. Neoenergia has its own liquidity policy covering 12 months of financial requirements.

- Strengthening of solvency ratios, affected in 2017 by the lower hydroelectric activity, the consolidation of Neoenergia and the growing investments, thanks to the increase in EBITDA and FFO. Based on the foregoing, it is estimated that the FFO/Net Debt ratio will reach 24% by 2022.

...resulting in the company proposing a sustainable shareholder remuneration policy linked to the growth in results.

3. Sustainable dividend

- Thanks to the strength of the results obtained, the company has announced a proposal to immediately increase the annual dividend to 0.323 euro per share with a charge to financial year 2017.
- Shareholder remuneration will continue to grow in line with results, maintaining a pay-out ratio between 65% and 75%, which would mean reaching a dividend per share of approximately 0.40 euro per share by 2022.

EBITDA by business (forecast to 2022)



(1) Including hydroelectric.

EBITDA by currency (forecast to 2022)

