National Grid

Full Year Results Webcast

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National Grid

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Introduction

Nicholas Ashworth, Director of Investor Relations (Interim)
Thank you, Felicia. Good morning and welcome to our Full Year Results presentation. Thank you for joining us remotely, I hope you're all safe and well.

Firstly, I would just like to draw your attention to the Cautionary Statement that you'll find at the front of the presentation.

Secondly, after the presentation as usual the IR team will be available by phone to help if you have any further questions. So with that, I'd like to hand it over to our CEO, John Pettigrew. John.

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Key Highlights

John Pettigrew, Chief Executive
Thank you Nic, and good morning everyone. Welcome to our Full Year Results call. As usual I'm joined today by Andy Agg, our CFO.

We have plenty of time for calls today, so Andy and I will be able to answer any questions you may have after the presentations.

Clearly, everyone's safety and wellbeing are at the forefront of our minds at this time. Whilst dealing with the disruption that COVID-19 is causing, National Grid's greatest priority has been our people as well as the safety and wellbeing of our customers and communities.

Before we return to our results for 19/20, I want to start today's presentation by taking you through how we've been reacting to COVID-19 and how well our business continues to deliver despite this major new challenge.

At the end of March as the crisis unfolded, we successfully implemented our business continuity plans. Although COVID has had a profound impact on demand levels and on the way in which we work, I'm proud to say that we've maintained excellent levels of reliability across the networks and we continue to deliver on our significant capital programme.

As the crisis evolved, we took action to change working practices quickly and safely. In particular, we've risk assessed all our operational and construction projects, issued new working guidance to our field force and collaborated across the industry, sharing best practices and finding innovative new ways of working. And despite these changes we've continued to deliver strong operational performance.

A great example of this was our team's rapid restoration of power to 142,000 customers following a significant storm in Massachusetts on 13th April. We were able to restore power within 29 hours to 95% of impacted customers.

Away from the field, our dedicated control room staff have been working tirelessly, sequestered away from their families to ensure they're protected and can maintain our real-time operation systems.

So as you can see, we've adapted extremely well to the challenges, and I'm proud of how our employees have responded.

Turning now to our customers, our focus has been not only to keep the electricity and gas flowing, but also to help those customers who may be in financial difficulty.

In the US recognising the economic environment, we've not pursued debt collections or disconnecting customers at the present time. And as you're aware, we've also deferred proposed rate increases in New York.

We're also helping customers ascertain whether they're eligible for a discount on their bill, if they qualify for home energy assistance grants or if we can offer them flexible payment plans.

In the UK we'll continue to work with other network companies and Ofgem to help suppliers address financial challenges that COVID has brought without imposing additional burden on consumers.

A good example is the deferral of network charges for eligible suppliers. This will help the most vulnerable suppliers with a regulatory mechanism which allows us to recover these charges within our financial year.

We're also working with Ofgem to see how we can help our customers bear the increased balancing costs associated with managing the system through COVID.

In addition, we're supporting our communities. There are many examples from across the business, including financial donations to help the most vulnerable, support by individual employees in their local communities and direct actions taken by our businesses. For example, our Gas teams in the US upgraded supplies in record time to help turn a college gym into a 1,000 bed hospital on Long Island.

I won't go into detail on other examples of this here, but I can say that National Grid is acting in a responsible way and living our value of doing the right thing.

Of course, as well as ensuring the support of our staff, customers and the communities, we also need to manage the financial impact of COVID. Andy will provide more details shortly but to summarise, we expect to see a £400m impact on underlying operating profit in 2021 primarily driven by higher costs and lower revenues in the US.

However, with the regulatory mechanisms and precedents, we expect to recover these over the medium term, and we are also maintaining our focus on efficiency plans. So whilst we see a financial impact in the near term, we currently don't expect to see a significant economic impact on the business longer term.

So having provided that context, I'd now like to turn to the strong results we've delivered in the past year.

On an underlying basis that is excluding the impact of timing, major storms and exceptional items, operating profit of £3.5bn was broadly in line with the prior year. This reflects the expected increase in revenues from new rate cases in the US and lower operating costs as our efficiency programmes have started to deliver but offset by the impact of an additional provision for US bad debts. Consequently, underlying earnings per share was down slightly by 1% to 58.3p.

Underpinning this performance was a record year of investment in critical infrastructure with capex up 19% to £5.4bn. This was driven predominantly by increased spend in our UK Electricity Transmission business as we progressed major projects like Hinkley. Higher US capex, much of it mandated on safety spend and higher capex in National Grid Ventures from continued interconnector investment as well as the acquisition of Geronimo. This delivered organic asset growth of 9% above our stated target of 5% to 7%.

We achieved a Group return on equity of 11.7% in line with the prior year, delivering ongoing sustainable returns to our shareholders. And in accordance with our policy, the Board has proposed a final dividend of 32p per share. This takes the total dividend for the year to 48.57p per share, an increase of 2.6% in line with UK inflation. So as you can see, it's been a strong year for financial performance across the Group.

As you know, our safety and reliability performance remain the key to our success. On safety our UK and National Grid Ventures businesses have delivered good performance with their lost time injury frequency rates falling to record low levels.

In the US we've seen an increase in the number of safety incidents. However, we've conducted a thorough review of all our working practices and in the coming year we'll be implementing programmes to further reinforce positive safety behaviours.

Turning to reliability, performance has remained excellent across our UK and US regulated networks, as well as our interconnectors. As you know, on 9th August we experienced a rare power outage event in the UK that caused huge disruption to many people.

In early January, reports into the incident from the Energy Emergencies Executive Committee and Ofgem found no link between National Grid's actions and the power cut. Since the reports were published, we've worked with the industry, Ofgem and BEIS and all the actions proposed are progressing to time.

And in the US despite another year with a significant number of storms, we've delivered excellent reliability in line with levels from the prior year.

I'll now turn to the progress on our operational priorities last year. Starting with the US, I'm delighted that the Board's confirmed that Badar Khan is the new President of our US business. Badar's been with the Group for three years and takes over a business that's seen strong operational performance.

During the year, we achieved a return on equity of 9.3%, an increase of 50 basis points, representing 99% of our allowed return. We achieved strong rate-based growth of 12%, up from 9.2% last year as we invested over $4bn in critical infrastructure, and as a number of projects under construction were added to the rate base.

This investment was mainly driven by mandated spend to maintain the safety and reliability of our networks. An example of this is the 458 miles of leak-prone pipe we replaced across our jurisdictions. This brings the total we've replaced to date to more than 10,500 miles and means we're now halfway through the long term replacement programme.

We've also made good progress on the regulatory front. In October we agreed new rates for Massachusetts Electric with a five-year agreement that gives us long term visibility for our investment, greater protection across cost pressures and more incentives to innovate and create value for our customers. And we've made good progress on our cost-efficiency programme where we met our target to deliver $30m of savings this year and remain on course to deliver $50m in 2021.

However, as you're aware we also experienced some challenges with gas constraints in Downstate New York. Addressing this has been a major priority of mine this year. As you know, in November we agreed to lift the moratorium on all new connections until September 2021.

Since then, and in line with the terms of the agreement with the State, we filed a report outlining options for meeting long-term customer demand. This was followed by a series of public and virtual meetings that were attended by over 800 people.

From these meetings feedback was included in a supplementary report that was filed with the regulator. We're continuing to work proactively with New York State, the regulator and our customers to find a long-term solution and anticipate an outcome this summer.

Turning now to the UK. It's been an important year as we head towards the end of RIIO-T1. Operationally both our Electricity and Gas Transmission businesses continued to deliver good levels of performance. Let me talk you through a few of the key highlights.

During the year we achieved a return on equity of 12.4% within our target range of 200 to 300 basis points of our performance. And we continued our capital programme with investment of £1.3bn, which was up 5% on the prior year giving asset growth of 3.8%. This takes our total investment in RIIO 1 to $11bn, delivering world-class reliability, enabling the connection of 4.6 gigawatts of renewable energy and generating over £700m of savings for customers.

During the year we've made progress across a number of our large projects including completing the Feeder 9 tunnel into the Humber, our largest Gas project in over a decade, and driving forward the second phase of our London Power Tunnels project.

We've also made good progress on our investment at Hinkley and we welcome Ofgem's decision on allowances and the use of strategic wider works as the delivery model for this project.

And of course we've made significant focus on RIIO-T2 with draft business plans submitted in December. Our plans cover a crucial period when rapid change is expected in the energy system to reduce carbon emissions and help reduce the UKs environmental goals.

In delivering the plans we've engaged with over 25,000 stakeholders, and we're the first company to set up the independent stakeholder user groups.

And finally during the year, we remained focused on our efficiency programmes and exceeded our savings target of £50m. This achievement has been driven by cost and process improvements such as the overhaul of our IT contracts and optimisation of control and field teams.

Driving cost efficiencies whilst keeping our workforce engaged will be the key to delivering continued benefits to our customers as we move into the RIIO-T2 period.

Moving now to National Grid Ventures and our other businesses, with Badar's appointment in the US, in April we announced that Jon Butterworth would step-up to be the new Managing Director of National Grid Ventures.

Jon has spent many years at National Grid and brings a wealth of experience to the role. And it's been another year of significant progress. Investment was up substantially to £850m, mainly driven by higher interconnector spend together with our investment in Geronimo.

Progress on our new interconnectors remains on track. On IFA2 the subsea cable connection has been completed and successfully tested, and commissioning the link is on course for the end of the year.

On our North Sea Link and Viking interconnectors we've managed the disruption caused by COVID and commissioning remains on track.

And last year we completed the acquisition of Geronimo Energy and have since announced the start of commercial operations of our 200MW windfarm in South Dakota.

Finally, in another busy year in our Property business where we continued to sell sites into the St William joint venture. And I'm pleased to say that it was also the first year where the joint venture contributed net profit through the sale of homes from customers.

So in summary, I'm pleased to report that '19/'20 was a strong year for National Grid and good strategic progress was made despite the challenging backdrop at the year end.

And I've been incredibly proud to see some of the amazing things our people have done to help our customers and communities get through this COVID crisis.

I'll review shortly our priorities for the coming year, but first let me hand over to Andy to discuss our financial performance in more detail.

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Financial Review

Andy Agg, Chief Financial Officer
Thank you, John and good morning, everybody. I'll start with reviewing our financial performance over the last year before covering the impact of COVID on our business in detail.

Overall the Group delivered a strong financial performance last year. As John has mentioned, underlying operating profit was £3.5bn, mainly reflecting the impact of revenue increases in the US driven by new rate cases, lower controllable costs across both the UK and US businesses, higher UK profit with the non-recurrence of the return of Avonmouth revenues in UK Gas transmission, which together were offset by the expectation of additional COVID-related bad debts, higher levels of US depreciation on increasing levels of capex spend and the impact of lower profits from the non-recurrence of the Fulham sale and the legal settlements last year.

EPS was down 1%, at 58.2p, reflecting improved regulated business performance offset by a 2.5p impact of the COVID-related bad debt provision, an increase in finance costs, increased share count and a slightly higher effective tax rate.

Our robust operational performance was also reflected in the 11.7% group return on equity. And our value added per share was 58.9p, down slightly compared to last year. But our asset base grew strongly by 9%, reflecting significantly higher capital investment at £5.4bn including over £200m of investment in Geronimo. The full year dividend at 48.5p per share is up 2.6% in line with our policy.

Let's look at the performance of each of our segments. UK Electricity Transmission delivered another year of strong operational performance achieving a 13.5% return on equity, 330 basis points above the allowed.

Totex incentives contributed over 250 basis points from efficiency savings across our asset hold programmes and high-performing load related schemes.

This outperformance was driven by process improvement and contract management savings. Additional allowances contributed at 70 basis points, slightly above last year.

Underlying operating profit of £1.2bn was up 8%, largely due to lower operating costs and depreciation.

The UK efficiency programme that we launched in FY'19 delivered £54m of savings for the year.

Capital investment at £1bn was 13% higher than last year, primarily due to spend on the second phase of the London Power Tunnels project and the Hinkley Seabank project.

This investment along with the inflation linked growth in the RAV increased year-end regulated asset value by 4.4% to £14.1bn.

UK Gas Transmission delivered a return on equity of 9.8%, 30 basis points higher than last year but marginally lower than the allowed level. This slight underperformance reflects the higher cost of delivering key compressor projects and our new data centres. Other incentives performance at 110 basis points was strong, resulting from improved customer satisfaction and constraint management.

Underlying operating profit of £402m was up £61m or 18% compared to FY19. This is primarily due to the non-recurrence of the return of Avonmouth allowances, transitional revenue for cyber security following the reopen as agreed in 2018.

Our UK cost efficiency programme delivered £19m of savings and together with the £54m of Electricity Transmission savings we exceeded the total UK target of £50m announced last year.

Capital investment was £249m, £59m lower than last year due to the lower spend on Feeder 9 and our compressor projects. And including inflation the regulated asset value grew by 2.3% to £6.3bn.

Turning now to our US business where the return on equity was 9.3%, 99% of the allowed. Underlying operating profit increased 1% to £1.6bn at constant currency.

Net revenues were up £257m reflecting rate increases. Controllable costs decreased due to the non-recurrence of last year's Rhode Island Gas interruption, and we also exceeded our target of $30m of savings from the first year of our cost efficiency programme.

Bad debts increased £83m reflecting the additional COVID-related provision of £117m, partly offset by a lower receivables balance.

Depreciation increased due to growth in the rate base and other costs increased largely due to deferrable storm costs.

We've increased investment in our US networks to £3.2bn or $4.2bn. This, together with a $380m increase in construction work in progress coming into service drove strong rate base growth at 12% to $25.6bn.

Assets outside rate base were $2.7bn and these largely relate to capital work in progress.

National Grid Ventures contributed £336m. This is an increase of 6% on last year, including a full year's operation of Nemo links to Belgium.

Grain LNG and Interconnector profits were consistent with last year, and metering profits were broadly flat, reflecting a more gradual decline than expected in our legacy meter population as the mandated Smart Meter rollout continues.

Capital investment increased significantly to £815m, mainly driven by the acquisition with Geronimo and higher investment in our North Sea Link, Viking and IFA2 interconnector projects.

Our other activities had a small net charge of £27m, reflecting the non-recurrence of the Fulham property sale, higher insurance costs and the non-recurrence of the US legal settlements. We sold another two sites into the St William joint venture and we've also exchanged on a further four sites which will transfer in due course.

Our venture capital business, National Grid Partners, invested £61m in FY'20 and continues to make investments in innovative technology start-ups such as Copperleaf and Smart Wires.

Financing costs increased by 6% to £1bn, primarily due to higher net debt in our US business and hybrid buyback costs partly offset by lower UK RPI. The effective interest rates decreased from 4.3% to 4.1%.

The underlying effective tax rate was 19.9%, 30 basis points higher than FY'19, primarily as a result of lower value property sales in FY'20.

Underlying earnings were broadly flat at £2bn, and underlying earnings per share decreased 1% to 58.2p.

Operating cash flow was £4.9bn, £450m higher than last year. This was driven by higher regulated business income, lower year end weather-related US receivables, lower US pension costs and reduced exceptional cash costs.

During the year we raised £2.9bn of senior debt and refinanced £1.1bn of our hybrid debt.

Closing net debt was £28.6bn, an underlying increase of £2.7bn after allowing for an £800m adverse movement in exchange rates, the impact of adopting IFRS 16 and receipt of the final Cadent proceeds.

Turning to our credit metrics where Moody's RCF debt ratio was 9.2% and S&Ps FFO to debt metric was at 12.3%. These both reflect higher tax and pension costs and adverse timing, partly offset by lower exceptional cash payments and, in the case of the RCF ratio, a higher scrip uptake.

We've also guided previously for our regulatory gearing levels to remain around 65%. At the year end this stood at 63%, which remains consistent with the Group's credit rating.

During the year, we've further reduced the level of the balance sheet hedge of our US assets to around 70%. This followed our periodic review of its effectiveness, and we now see that the slightly lower hedge range will give a greater stability for our credit metrics. As a result our US dollar denominated debt balance now stands at $20bn compared to $21bn last year.

Group capital investment in FY'20 was £5.4bn. Of this, approximately £4.5bn relates to our investment in critical infrastructure across our regulated UK and US businesses with a large proportion focused on meeting mandated safety and reliability targets.

A further £500m was invested in our interconnector programme. With IFA2 set to commission this year, we have now passed the peak investment for this overall programme.

Finally, we also invested over £200m in the acquisition of our large scale Renewable Energy business, Geronimo, during the year.

Our ongoing funding for the Group investment programme remains robust with strong internal cash generation supported by the scrip dividend which we continue to utilise giving current high levels of investment as we have said previously.

And I'm proud to have used our green financing framework to issue our inaugural green bond in January and for an ECA-backed loan to fund our Viking interconnector. Together with regular bond issuance at attractive rates this highlights global debt investor confidence in National Grid.

Having reviewed last year's performance, I'd like to spend a few minutes walking you through the impact COVID is having on the business.

Like all companies, National Grid is not immune to COVID. However, as a regulated utility for the most part there are either mechanisms in place or regulatory precedents for recovering additional costs arising from COVID. In addition to regulatory recovery, we’re also maintaining our focus on cost efficiency to help offset additional costs wherever we can.

Whilst this means that we do not expect a material economic impact on the Group in the medium term, we will see an earnings and cash flow impact in the near term. So for FY'21, working with our assumption of a gradual easing of lockdown, we current forecast the impact of COVID on underlying operating profit to be around £400m.

Whilst we’d expect to see some additional costs arising in the UK and a limited impact in our National Grid Ventures business, the majority of the £400m impact is forecast to come from our US business driven by three broadly similar impacts, the deferral of rate increases across New York, incremental COVID-related costs and higher bad debt charges.

Taking these in turn, firstly we currently expect rates to be held broadly flat across our New York businesses this year as we've deferred rate increases in our Niagara Mohawk business, and with rates held flat in our KEDNY and KEDLI businesses as we discussed in the new rate agreement. As is normal, we’ll work with our regulators to agree the appropriate frameworks for recovery.

Secondly, we’re also seeing higher levels of COVID-related costs such as sequestering critical staff on site, increased IT costs as well as higher opex from the lower capitalisation of our own workforce costs given changes to our capital programmes. Again, we’re working with our regulators on ways of recovering these incremental costs.

With a weak economic backdrop we’re likely to see levels of bad debt increase. As you’ll have seen this morning for FY'20 we've taken an additional £117m provision for bad debts over and above our normal run rate against our receivables balance as at year end.

Looking forward to FY'21, we would again expect to see a similar elevated level of bad debt expense, although the final bad debt level will ultimately depend on how each of the states, we operate in exits the COVID crisis.

As is usual practice, we would anticipate recovering bad debts above our regulatory allowances through future rate plans.

Turning to cash flow overall we currently estimate the impact of COVID to be up to £1bn. This will ultimately depend on levels of demand across our networks, cash collection from our US customers and timely collections of network charges and system costs in the UK.

This will therefore also have an impact on net debt. Taking into account these assumed cash flow impacts of COVID and excluding the impact of foreign exchange, net debt is expected to increase from £28.6bn to around £31.5bn.

Together these headwinds will impact our credit metrics in the near term, but we expect this impact to unwind as we recover these costs through our regulatory mechanisms.

With this context in mind, I’d like to discuss our outlook for FY'21.

In the US we expect to see net revenue increases more than offset by bad debts and higher COVID-related costs as described previously.

We forecast depreciation to be around £100m higher, given higher levels of investment in rate base.

In the UK additional COVID-related costs will lead to a small year-on-year reduction in underlying operating profit expectations for Electricity Transmission. In Gas Transmission with limited COVID costs, we still expect to see an increase in underlying operating profit.

National Grid Ventures operating profits are expected to decrease by around 5% year on year due to lower interconnector arbitrage. And the contribution from other activities will also be lower due to lower property profits.

Our profits from St William are also expected to decrease given macroeconomic headwinds for our joint venture property sales.

Our interest charge is expected to be a little below FY'20, reflecting lower RPI and lower interest rates. We expect a tax rate of around 22%.

Overall, Group capital investment is expected to be around £5bn leading to asset growth within our 5% to 7% target range.

Whilst COVID will bring near-term earnings and cash flow headwinds, the underlying operations of the company remain strong. This has enabled the Board to confirm the dividend policy. And as previously announced, due to the current levels of investment we do not expect to buyback the scrip issues during FY'21.

To summarise, we've delivered a strong returns performance in FY'20. We have delivered a record £5.4bn of investment in critical infrastructure. The balance sheet remains robust enabling the funding of attractive asset growth in the medium term. And whilst COVID will have a near-term financial impact, we expect the majority of these additional costs to be recoverable, limiting the longer-term economic impact on the Group.

Now, John will take you through the priorities and outlook for the coming year.

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Priorities and Outlook

John Pettigrew, Chief Executive
Thank you, Andy. So let me now turn to our longer-term objectives and priorities for the year ahead.

National Grid has a critical role to play in enabling the Energy Transition, which is why our vision is to be at the heart of a clean, fair and affordable energy future.

Supporting that vision, our four strategic priorities are to enable the energy transition for all, to deliver for our customers efficiently, to grow our organisational capabilities and to empower our people for great performance. And these strategic priorities will underpin where we focus this year.

In the US we have two focus areas, to ensure we have the right rate plans in place for a post-COVID world and the efficient delivery of our significant investment programme.

In the UK, our two focus areas will be to agree the RIIO-T2 regulatory framework and to drive innovation and efficiencies to our customers.

And in our National Grid Ventures business we'll continue to focus on our interconnector programme and delivering our Geronimo investment pipeline.

Let me talk you through each of these in more detail before I come back to our clean energy ambitions.

I'll start with our US rate plans. Whilst the long-term investment requirements across our jurisdictions have not changed, the current backdrop means we'll have to adjust our short-term priorities.

As Andy has set out, we'll see revenue and impact costs from COVID in the near term. This means that our immediate focus will be on working with our regulators to agree the appropriate rate plans for the medium term and to achieve a timely recovery of increased costs.

These must recognise both the need for critical infrastructure investment and the economic environment that we're likely to be operating within.

So with that context in mind, let me now take you through our rate filing plans for the rest of the year.

Let me start with our Downstate New York Gas businesses, KEDNY and KEDLI, where we filed the new rates in April 2019. At the beginning of this month we resumed settlement negotiations with the PSC in the interests of agreeing a multi-year rate plan that will achieve four things, to mitigate bill impact to our customers, allow us to maintain safe and reliable service, advance our clean energy goals and earn a reasonable return.

Whether we agree a one year or a multi-year deal this summer, we expect rates to remain flat for our customers this year. And at the same time in Downstate New York as I mentioned earlier, we'll continue to work on delivering the solutions required to address Gas supply constraints.

In our Upstate business, Niagara Mohawk, we were due to file for new rates this spring for the period starting April 2021. However, we've delayed the filing and are exploring options including an extension of the current rate plan or rate case filing later this summer.

With regards to Massachusetts Gas, our current intention is to file towards the end of the year. As with previous filings, our aim will be to ensure that rates are increasingly forward looking, incentive based and multi-year. This will give us good visibility on the funding of our investment plan and allow for annual inflationary cost increases offset by efficiency savings.

Our second area of focus is efficient investment. The vast majority of our work is needed to improve the safety, reliability and resilience of our networks. Our top priority will be delivering this work efficiently, and this is particularly true in the context of COVID. This includes finding new streamline processes and digital solutions.

For example, in our Gas business we're rolling out our Gas business enablement programme, which will help firstly to standardise and simplify our operational processes. Secondly, to consolidate our support tools onto a modern digital platform. And, finally, to enable the efficient scheduling and optimisation of our field force.

And, on digitalisation, we've recently launched a new system that automated our dispatch processes for our Electricity Distribution workforce. These examples, together with others, will help us to deliver investment plans efficiently whilst minimising bill impacts for customers.

Turning to the UK, I'll start with regulation. As you know, at the end of the last calendar year, we submitted our final business plans for Electricity and Gas businesses that reflected the wealth of stakeholder engagement we've undertaken. Simply put, we're proposing investments to maintain reliable and resilient networks that can support a changing energy system whilst keeping bills as low as possible.

In the past few months, we've been engaging construction with Ofgem to address the points raised by the Challenge Group, which will be published in January. I was pleased that our greater level of stakeholder engagement was recognised by the Challenge Group, but I also recognise that we've got work to do to provide more evidence around our asset health investment plans.

The next key milestones in the process will be Ofgem's draft determination, expected in early July, and final determination, which is expected at the end of this calendar year.

As we progress through the year, we'll continue to work constructively with Ofgem to agree a framework that puts customers at the centre of the price control, enables the energy networks of the future and provides a financial package that allows a fair return for our investors.

On delivering innovation and efficiency for our customers, we're on track to meet our cost reduction target of £100m for 2021.

This year, our efficiency focus will be on three key areas; streamlining our maintenance operating procedures, further digital innovations to increase the productivity of our field force, and making step change improvements in our back office processes.

And we're innovating for our customers. As an example, we've recently launched, and are continuing to develop, two new digital platforms. These will help customers connect to our network more efficiently by giving them access to the right data, standardising connection design and providing a smoothly, easier customer journey. Not only will this help customers with reduced connection costs, but it will also reduce the time it takes to connect to our network.

We recognise that more efficient outcomes and improved customer relationships will be critical as we head into the new price control period.

Finally, on National Grid Ventures, the major focus will be the continued investment in the three new interconnectors; North Sea Link, IFA2 and Viking. So, by the end of this year, we'll have completed IFA2, be 85% through our construction programme of North Sea Link and be one third of the way through delivering Viking.

With investment of just over £1bn to date, we have around £1bn left to invest through to 2023. And, when all online, we expect these interconnectors, together with Nemo, to contribute £250m of EBITDA from the mid-2020s.

With regards to our US Renewable business, it has been a successful first year after our acquisition of Geronimo Energy. And, looking forward, our pipeline of future investment opportunities continues to strengthen.

In recent months, we signed power purchase agreements that will underpin nearly 500 megawatts of solar projects. Spanning across South Dakota, Illinois and Kentucky, these projects will commence operations between 2021 and 2023, and we expect further announcements like these in the months ahead.

I'll now return to our clean energy ambition which sits at the heart of our vision for National Grid. Whilst, like all companies, we're working through the impacts of COVID, we need to ensure we keep one eye on the future, which is why today we're strengthening the commitment we made in November to reach net zero for our own emissions by 2050 by setting ourselves a more ambitious interim target. That target is to achieve 80% carbon reduction on our 1990 baseline by 2030, and 90% reduction by 2040.

In the UK, in our RIIO-T2 business plans, we've committed to replace over 50% of our internal fleet with alternative fuel vehicles by 2026. And we're continuing to lead in developing alternatives to the insulating gas, SF-6, so that, from 2026, we'll no longer install any new equipment that uses this greenhouse gas.

And, in the US, we've also made commitments to decarbonise our internal fleet, and we continue to reduce emissions by replacing leak-prone pipes.

And we're also pleased to announce that we'll be hosting an investor event in October on our environmental, social and governance objectives. The event will take place on the afternoon of 5th October in London, most likely by video conference, which will enable those in the US to attend at the same time. The event will allow us to talk in more detail about how we'll achieve our own targets but also, perhaps most importantly, how we're playing a key role in enabling the wider transition to a low carbon future.

To give you just two examples on power in the UK, we're working to enable the Government's target of 40 gigawatts of offshore wind by 2030. We recently took part in BEIS first coordination stakeholder meeting, looking at the potential east coast connections needed to unlock the increased offshore capacity.

Given our capabilities and understanding complex transmission networks, both onshore and offshore, we believe we're well-placed to be part of this infrastructure build-out, and our engineers are working hard in developing options and proposals.

And on transport in the US, we're working across all our jurisdictions to deliver a number of initiatives around EVs. These will include customised support for fleet operators, educational programmes to provide customers with information to alleviate their concerns, as well as a number of pilot projects, such as municipal partnerships to deploy electric school buses.

We'll be following up from these initiatives with more substantive filings across all our jurisdictions. For example, next year, we propose comprehensive filings in New York and

Massachusetts to include funding for over 30,000 new charging ports as well as targeted residential fleet and transit programmes.

These are just two examples of the many ways that we're working to drive forward the Energy Transition, and I look forward to sharing our progress with you in more detail in October.

So, in summary, National Grid has had a strong year, and I'm pleased with the progress that we've made across all our businesses. We've managed the challenge that the COVID has brought, and helped our most vulnerable customers whilst maintaining network reliability.

We'll see higher costs in the near-term due to COVID, but, given our regulatory mechanisms, we currently don't expect to see significant economic impact in the longer term.

In the coming year, we'll continue to focus on our up-and-coming regulatory negotiations in both the US and the UK, and our interconnector delivery in National Grid Ventures whilst looking to advance the energy transition.

We expect another strong year of capital deployment, investing around £5bn in critical infrastructure, which will help to continue to grow our asset base within our 5 to 7 target range.

I believe our disciplined approach, coupled with our focus on delivering efficiently for our customers, will enable us to continue to create long-term value for our shareholders.

So, thank you for listening, ladies and gentlemen. Andy and I will be happy to take any questions you may have.

. . . .

Telephone Operator
Ladies and gentlemen, please press '*' followed '1' on your telephone keypad to ask any questions.

The first question comes from Martin Young from Investec. Please go ahead, Martin, your line is open.

. . . .

Martin Young, Investec
Thank you, and good morning to everybody. Just a few quick questions hopefully. And the first one relates to the ESO. Obviously, they've done and absolutely fantastic job adjusting to the current demand and supply balance that we have in the country at the moment. That's got a considerably higher proportion of non-programmable renewables in the mix, and you could argue that we are currently in a sort of generation mix situation that we didn't expect for a number of years.

Now, given what you've learnt from that, do you think the ESO should be more vociferous around what the longer term generation mix in this country should be? And, if so, should we be thinking about moving away from new nuclear build and making sure that we add more responsive generation that can provide flexibility and inertia services in that mix?

But the second relates to the £1bn cash flow impact from COVID-19. Obviously, we've got the £400m underlying operating impact you've talked about. I guess there's probably about £100m or so on volume timing differences in the UK. Is the balance coming from the possibility of deferring to TNUoS and BSUoS charges beyond the year end?

And then my third question, you've alluded to, you know, the fact that there's a regulatory precedent in terms of recovering, you know, these costs. That's a lot different from actually getting it over the line. What's your sort of best estimate on recovery in the US of the cost and revenue impact that you are, undoubtedly, going to experience in FY'21? Thank you.

. . . .

John Pettigrew, Chief Executive
Okay. Thank you, Martin. Look, why don't I take the first, and I'll Andy to do the second, and then I'll do the third.

So, in terms of our system operator, I mean, you're absolutely right, it's been, you know, a unique set of circumstances this summer. We've seen demand levels at 17% to 20% below what you typically expect during the summer. And, as a result of that, the system operators have to take significant action to be able to be able to balance the network.

I have you say, you know, we're incredibly proud of the way that they've responded to that. They've developed new tools, which you would have seen, including a contract with Sizewell B, but also developed new contracts for downward flexibility with about 3.5 gigawatts of providers who typically wouldn't be providing those services to the electricity system operator.

So, in terms of your forward-looking part of the question, you would have seen, hopefully, recently, the system operators set out an ambition to be able to operate the system on the basis of zero carbon generation by 2025. So, we've seen some of the challenges that will give rise to during this COVID crisis, but, actually, we have a very clear plan in place to be able to be in a position to do that by 2025.

So, ultimately, we feel very comfortable that we can develop those tools.

Whatever the make-up is, I think, you know, fundamentally, there are capacity auctions that run on a regular basis that are facilitated by the Government, and who bids into those capability auctions is, ultimately, a matter for the market. From our perspective, we need to ensure that we have the tools to be able to balance the system, you know, minute-by-minute, second-by-second, and we're comfortable we have them today, and we're comfortable we can develop them going to forward for 2025.

I'll ask Andy just to pick up on the second question around the cash aspect.

. . . .

Andy Agg, Chief Financial Officer

Sure. Thanks, John.

So, Martin, as you said at the start, so if you stand back a moment, so within the £400m, you've got the three broad buckets in the US that I described in my presentation. And, obviously, we do see a smaller impact in the UK within that as well.

So, that is then part of, as we build up towards the £1bn, and, you know, been clear we've guided up to £1bn, and I think that reflects that there is some uncertainty ultimately in the make-up of that.

I think you touched on some of the key elements, so, yes, so we see, you know, demand impacts on both sides of the Atlantic. So, referring to normal timing mechanisms, as you know, we under-collect, allowed revenues in any period, that will feed straight through into the normal mechanisms and gets collected again one to two years out.

There's also elements of, while we've recorded the bad debt expense within the £400m, the underlying cash impacts and working capital impacts of the delays in collecting those US receivables and estimating what will still be on the balance sheet as at 31st March '21, so there's a bigger cash impact at the £1bn, even though the bad debt impact is included within the £400m.

And then, finally, as you said, there remains some uncertainty about the final sort of industry support schemes that you referenced in the UK around both network charges to, you know, also the balancing costs as well where we're very much still waiting for Ofgem's final conclusion on that consultation.

So, those are, absolutely, the elements that build up towards the £1bn.

. . . .

John Pettigrew, Chief Executive
And, in terms of your final question, Martin, you know, historically, there have been circumstances in the past where there have been issues around higher bad debt against the allowances that have been allowed through rate filings, and other costs as well, and, typically, there are processes in place for either recovering those costs directly or recovering them through our rate filings.

So, each of the States, in the last few weeks, has already raised an order to understand what those costs are associated with COVID, and that will be an on-going discussion about how, exactly, they will be recovered going forward. Some of them will be through the rate filings, and the timing of that will then be influenced by when we're due to do another rate filing, and the recovery of those costs will also be influenced by the duration of any rate agreement we have with each of the individual states.

But there is plenty of precedent and mechanisms in place which give us the confidence to articulate why we think it's a short-term impact and not a long-term economic impact for National Grid.

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Martin Young, Investec
Thank you.

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John Pettigrew, Chief Executive
I've got a list in front of me. Shall we take Rob from Morgan Stanley next?

. . . .

Telephone Operator
Rob, your line is open. Please go ahead.

. . . .

Rob Pulleyn, Morgan Stanley
Thank you, gentlemen. I think Martin beat me to the first two questions there, so I will ask a couple of different ones.

The first one is do you have any views on the future US storm risk? Do you see it increasing? And, therefore, do you expect there will be a change in mechanisms for recovery as this becomes, sort of, more regular and more dramatic?

The second question, if I may, is just on the scrip buyback. I notice, obviously, you mentioned that you won't be buying back a scrip dilution this year. Can we assume that that will resume the year after or is this an ongoing situation that you wouldn't be buying it back? Thank you very much.

. . . .

John Pettigrew, Chief Executive
Okay, thanks, Rob. Let me do the first and I'll ask Andy to do the second.

So, in terms of storm cost recovery, I mean, we have different mechanisms for different states. Quite a few of our regulatory rate cases allow for the recovery of some costs on an on-going basis, and then, quite often, there's a logging up mechanism for any excess costs.

It is something that we discuss with the regulators on a regular basis when we do rate filings, and I do anticipate it will form part of that discussion going forward to make sure we've got the right allowances up-front but then we've got the right recovery mechanisms going forward.

So, as we've seen more storms over recent years, it is part of the discussion that we have with each of our regulators. But, again, the economics of it are pretty straight, is we either get up-front recovery or we're able to log it up and then get recovery as part of a future rate filing.

Andy.

. . . .

Andy Agg, Chief Financial Officer
Yeah, so, Rob, just on the scrip point, you may remember that a year ago we guided to not looking to buy back the scrip, so FY'20 and FY'21, we're reaffirmed that message for the remainder of FY'21.

We haven't guided beyond that, and, you know, we'll continue to look at that as part of our normal annual review, and that will depend on, as we've always said, you know, the levels of growth, the levels of performance across the business, and we'll guide further at that point.

. . . .

Rob Pulleyn, Morgan Stanley
Marvellous. Thank you very much.

And, if I can just ask one quick extra one just on the RAV growth, obviously noting the step down year-over-year but still a very impressive rate, can you just maybe talk about the visibility on the US side? Does RAV growth, you know, is there, you know, sort of, very simply, is it a capital constraint issue or an opportunity constraint? It seems like it's a high quality problem to have but just seeing sort of how long this RAV growth in the US do you think could continue? Thank you.

. . . .

John Pettigrew, Chief Executive
Yeah, thanks, Rob. I mean, you know, over the last few years, what we've been, you know, focused on doing is making sure that we've got rate cases in place to support the capital investment.

The three drivers of the capital investment, fundamentally, are on the electricity side it is all around resilience and asset health. On the gas side, it's predominately around safety with our leak-prone pipe programme, and then, of course, there is incremental investment needed as we move into the Energy Transition with decarbonisation and supporting that.

Those fundamentals aren't changing, and, therefore, it is driving the capex that you've seen over the last few years, and the rate base growth with it.

We're expecting, in the coming year, to see similar levels of capex that we've seen this year in the US. It might be slightly off, and that's because we are seeing some impact on COVID, particularly with the interface with our customers where you can't get access, obviously, with social separation.

But, fundamentally, we're expecting - I think we had $3.2bn this year for capex for the US, and it's going to be of similar magnitude next year. But the fundamentals aren't changing, so we can continue to expect to see strong growth going forward.

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Rob Pulleyn, Morgan Stanley
Excellent. Thank you. I will turn it over.

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John Pettigrew, Chief Executive
Okay. Thank you. I can see John Musk has got a question. Shall we go to John?

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Telephone Operator
John, your line is open.

. . . .

John Musk, RBC
Thank you, everyone. Probably three questions from me as well, actually.

I just want to come back to the £400m and the timing of the recovery, probably an impossible question, but how quickly would you expect to see that coming back? Are we talking one, two, three, four years? Roughly, what sort of timeframe should we think about for those three buckets?

Secondly, on the balance sheet, with the guidance on the £31.5bn, with lower earnings and lower cash flow, as you indicated, that's going to put further pressure on the credit metrics. I haven't done the sums, but I assume you may well drop below the 9% threshold on the RCF to net debt. You know, how much of a worry is that for you, particularly as we're coming to a RIIO-2 reset, which could also see a further fall in cash flows?

And then, finally, slightly separate, on the legacy gas meters, can you just remind me how many meters you still manage there, and how long you expect that tail to continue to be delivering a sizable EBIT number?

. . . .

John Pettigrew, Chief Executive
Okay, thanks, John. I'll do the first and third and then I'll hand over to Andy to do the second on the balance sheet.

So, in terms of the time in recovery, I think it's fair to say it is a difficult question to answer at this point because it will be unique to each state and potentially you need to know what the timing of the rate filings are.

So, what we have seen, as I said, is seen each of our states put an order out to make sure that that they can capture what those costs are. So, that is the start of the dialogue that we will have with the regulators. But then, ultimately, it could be a separate mechanism for recovery or it could be part of the rate filings.

So, it is likely to be different in each state, and it may be over a year or two, or a bit longer if we've got a long outstanding rate filing rate case. So, it is a difficult one to answer. As I said, what we do have is those precedents and those mechanisms to be able to have those discussions with the regulator.

In terms of the latest gas meters, we have 8.9 million meters at the current time at the end of the last fiscal year. In term of the roll-outs, as you're aware, the most recent announcement in terms of the roll-out of smart meters was that 85% of all customers should have a smart meter by 2024.

So, we're expecting that the sort of displacement of our meters will be over that time period, which is a much longer period than, of course, originally anticipated when - I think the original target was 2020.

Andy.

. . . .

Andy Agg, Chief Financial Officer
Yeah, thanks.

So, on the net debt/credit metrics question, John, so, as you say, guided to £31.5bn. That includes, you know, obviously the £1bn that I referred to in the previous question.

And, yes, in the coming year, given the sort of the reduced underlying profits and higher cash short-term impact, we would expect reported metrics to fall below the threshold.

I think the critical thing, though, is, as always, and we're in regular dialogue with all three agencies, we would expect the agencies to take a long-term view, as they usually do, on issues like this, and understand the route to recovery, as John's just mentioned, rather than sort of taking a one-off view of any particular point in time.

I think I'd also say that, just in terms of the reported metrics, you know, we report those all in. So, the 9.2 and 12.3, if you add that to the some of the adverse timing that we've seen and some of the other exceptionals and the bad debt, you know, sort of RCF is in the 10.5 range. So, I think, you know, as we go into the COVID situation, we're in a robust place too.

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John Pettigrew, Chief Executive
Thanks, John.

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John Musk, RBC
Okay. Thank you.

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John Pettigrew, Chief Executive
I can see that Dominic has got a question from Barclays.

. . . .

Dominic Nash, Barclays
Yeah. Good morning. Two questions from me, please.

The first one, ROEs in the US, and I think, going to page 58 of your presentation, you come up with a US GAAP net income, which is up 18% year-on-year, which is obviously impressive, but what expectations have you got for the growth, or not, of that next year as you start to move into the COVID world? And I presume that the £400m COVID operating profit is not going to be in that. And where do you think the ROE, we should sort of like model that one in our numbers going forward?

And, secondly, on your energy strategy, you talk about the Energy Transition, or your power, heat and transport, but what are your thoughts on your gas business overall on what the threats or opportunities are we going to see? Is it going to be a move to a hydrogen or are we going to move more to liquidification, or biogas or even CCS? Where do you see, particularly your gas transmission, opportunities there in the UK, please?

. . . .

John Pettigrew, Chief Executive
Yeah, so, if I start with the second then I'll ask Andy to talk about the ROEs.

So, I think in terms of gas, I think everybody recognises that decarbonisation of gas, and heat in particular, is probably the most challenging element of the net zero targets by 2050.

Clearly, you know, if you look at the UK, then over 80% of all heat comes from natural gas. And, if you look at what the Committee on Climate Change said recently, they're still expecting around 68% of the current gas volumes to persist, even in a net zero world, with an expectation of probably less gas going into buildings but more being used for things like hydrogen.

I think, at this point, Dominic, we're of the view that, you know, the solution to decarbonisation of gas is likely to be mosaic solutions. So, there is the potential for increased biogas that could, potentially, provide up to 10% or 15% of the UK needs, for example. But, clearly, things like hydrogen have a role to play, as does CCUS.

So, you will have seen that National Grid is partnering with Drax and Equinor, looking at the development of a zero carbon cluster in Humberside, which is effectively taking natural gas, taking the C02 out of it, using it for industry and, potentially, generation, and then taking that carbon emission back into oil caverns in the North Sea.

And, similarly, we are exploring working with the industry on a number a projects, looking at the role of a gas transmission network could be with hydrogen. So, we're looking at options with 20% blending 40%, and up to 100%, and what impact that will have on the network.

So, we're currently developing a piece of work to use on transmission pipelines, to test that, to see what the impact would be, and then, ultimately, to link that to some of the work that's going on in the North West, with the distribution gas companies, to test out hydrogen from beach to meter.

So, that's work that's going to go on over the next few years, you know, ultimately, to try and develop what that roadmap will look like, but we remain very positive that gas has got a really important role to play in the transition to net zero over the next few years.

Andy.

. . . .

Andy Agg, Chief Financial Officer
Yeah. So, Dominic, on US ROEs, as you know, this year 9.3%, 99% of allowed, and if you relate that through to the 18% increase in US net income, as you referenced, that's really driven by the 12% increase in rate base and 50 basis points improvement in achieved return, with a combination of those two gets you, you know, to around the 18% increase in US net income, or US GAAP net income.

I think, as I look forward, as you say, we haven't guided specifically. We're indicated, and, as John's mentioned just in the answer to a couple of previous questions, you know, as we work through the recovery mechanisms and the timing of those, obviously, that will feed through. And, also, you know, particularly in New York, with the Downstate rate cases still under discussion, you know, obviously, that will be a driver of the outturn in terms of ROE as well.

I think what I would say though is, having delivered 99% of the allowed this year, we see no reason why we shouldn't be able to deliver a strong performance on an underlying basis against whatever that allowed return is next year.

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John Pettigrew, Chief Executive
Thanks, Andy.

. . . .

Andy Agg, Chief Financial Officer
Thanks, Dominic.

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John Pettigrew, Chief Executive
I can see that Deepa's got a question.

. . . .

Deepa Venkateswaran, Bernstein
Hi. Thank you.

I have three questions. First, starting with what are your expectations from Ofgem for the July 9th draft determination. I think, in the past, you've said that the 4.3% cost of equity was low, and then you have proposed 6.5% in your business plan. So just your thoughts, particularly given the acceleration of investments needed for net zero, and then also the impact of COVID and the uncertainty that's created in the capital markets? So, that's my first question.

I think the second one, just on the balance sheet, just wanted to check, if things got tight, would you be open to, for instance, looking at divestments of some of your interconnectors? I mean, that build-out programme is now quite advanced, so would you be looking - I mean, if it came to it, would you be open to looking at, you know, some changes in the portfolio, maybe minority stakes, etc, if it came to it?

And, lastly, just a clarification to your previous answer to Dominic's question, on the US GAAP numbers, could you clarify whether you included the bad debt adjustment in that or is that pre bad debts that you've booked on those US GAAP earnings? Thank you.

. . . .

John Pettigrew, Chief Executive
Okay. Let me take the first and then I'll ask Andy to pick up the second and third.

So, in terms of expectations for the draft determination, I mean, we remain hopeful that Ofgem will recognise some of the arguments that we've made, Deepa, in terms of the overall financial package.

As you know, in our draft business plans, we set out a proposal, including a return on equity of 6.5%. Ofgem, in their initial view, was at 4.3% to 4.8%. So, we've continued the dialogue with Ofgem on that, and we're hopeful that we will see some progress to get to what, we believe, is a reasonable return.

As I've said several times, as you know, you know, fundamentally, it's the overall financial package that's going to be really important. So, returns clearly are important but we also wanted to see what the overall package looks like, including what incentives there are going to be to innovate and to drive efficiency, and how that's going to be shared between customers and ourselves going forward.

I actually think that, you know, the implications of COVID and the impact it's having on the economy, align to the fact that there is a real opportunity, I think, to use the green agenda and green investment to really stimulate the economy, but that is something that I hope Ofgem will be bearing in mind as they think about the draft determination. National Grid did report earlier in the year - you may have seen it - that showed that investments, to meet net zero, could potentially create 400,000 jobs in the UK and 100,000 in the next decade.

So, I think there is a real opportunity to think about, post-COVID, how you stimulate the economy and what does that mean for investment towards net zero. And I would be hopeful that Ofgem are thinking about that as part of their draft determination.

Clearly, once we get through that, there's still a fair way to go. Obviously, there's some important milestones, including the water companies have got their initial outcome from the CNA in September, and I'm sure Ofgem will be mindful of that as well, and then, ultimately, the final decision in December. But I think, you know, we're hopeful that some of the opportunities that I think the green agenda presents will be reflected in the draft determination.

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Andy Agg, Chief Financial Officer
So Deepa, on the two points - I mean in terms of the balance sheet and I think this was alluded to in one of the earlier questions, you know as I look forward, very much seeing COVID as a timing issue with the sort of regulatory recovery route that we have we don't see it as a significant sort of economic impact.

And I think then, you know, we will always therefore focus on the breadth of our regulatory arranagments, the diversification of those, the performance that we're than able to drive against those, which we've done consistently. And as you've probably heard us say as we look at the RIIO-2 outcome in particular, looking for the broader financial package and not just the headline return that's been referenced.

Clearly, as we've said consistently, you know we always look at our portfolio, we always look at the relative contribution of all elements of the portfolio, we'll continue to do that. But you know we don't have anything in mind.

The third point sorry, on the bad debts, so the 9.3 that we're reporting that does assume recovery ultimately of the bad debt charge, yes.

. . . .

Deepa Venkateswaran, Bernstein
Okay, so it excludes basically the bad debts both in the US GAAP earnings and the 9.3, yeah?

. . . .

Andy Agg, Chief Financial Officer
Well, it assumes recovery of it, yes.

. . . .

Deepa Venkateswaran, Bernstein
Okay.

. . . .

John Pettigrew, Chief Executive
Thanks Deepa, I can see Fraser from Bank of America is on. So Fraser?

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Fraser McLaren, Bank of America
Three questions from me as well please. So back in April I recall you were worried about not being able to recovery additional costs and lost revenues in the US and that I think was part of your remarks around the dividend. What has changed to make you feel happier about recovery now?

Number two is on inflation - do you see pressure on the UK business in the event of a period of low inflation and do you plan to move the asset base growth targets and the actual dividend benchmarks to CPIH at some point?

And then lastly on interconnectors, how dependent is that £250m EBITDA on the outcome of the UK's deliberations on the carbon price, particularly the £18 per tonne tax? Thanks.

. . . .

John Pettigrew, Chief Executive
I'll let Andy do the first two and then I'll do the interconnectors. Andy?

. . . .

Andy Agg, Chief Financial Officer
Yeah so Fraser, I think you're referring to on the first one back to our pre-close statement where, you know, understandably right at the end of March, beginning of April we - I think we said actually at the time that it was appropriate the Board would take into account everything including its normal considerations, the business performance, regulatory arrangements, but particularly the impact of COVID. And at that point, you know, a lot of uncertainty around the impacts of COVID-19.

As you'll have seen this morning I think we've got a lot more clarity of where and how that's impacting us. And as John said, you know the regulatory arrangements that we expect to be able to pursue recovery through. So you know that's why we're able to, you know, give the messages we have this morning.

In terms of inflation, just a quick reminder, so the 5 to 7, which has been our medium term growth guidance. That is always assuming 3% indexation, or RPI in the UK, so obviously as RPI does move around it will move the actual growth rate, but that 5 to 7 is driven by the long term assumption.

I think in terms of you know the broader risks around inflation, yes of course with still half our Group linked to RPI, or potentially CPI obviously under T2, but remember that today we have around a quarter of our debt book, which is index linked providing you know still a very good natural hedge for us. So you know like every utility you know many years or sustained levels of negative inflation would be something we would look carefully at, but at the moment we don't see it as a significant risk in the short term.

. . . .

John Pettigrew, Chief Executive
Yeah and in terms of the interconnectors, I mean we've taken a central view in terms of the 250 EBITDA, so both in terms of expectations in terms of carbon pricing and how that might evolve, you know whether we have a hard exit from Brexit or not. But also how we see the market developing, both in the UK and in Mainland Europe and what we see as the potential sort of view on the arbitrage between the two markets. So you know it's a central view that we're reasonably comfortable with.

Okay thanks Fraser. I'm going to move on because we've got quite a few questions to still get through. Olivier.

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Olivier Van Doosselaere, Exane BNP Paribas
Good morning. Thank you for taking my questions this morning. I just have three also follow up questions if I may, can you hear me?

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John Pettigrew, Chief Executive
Yes.

. . . .

Olivier Van Doosselaere, Exane BNP Paribas
Okay perfect, sorry. One is a follow up question on hydrogen actually; you already touched on that one. I assume that you're working at a fairly early stage now, I'm thinking of what the possibility might be for hydrogen for your business, but we are clearly seeing some political momentum rising quite a lot at the European level and potentially also at the UK level on the topic of hydrogen. I was just wandering if you could already give us a feel in terms of how hydrogen your gas network is for the UK and maybe also for the US? Should the ambition be over the long run to switch fully to 100% hydrogen networks would you require a lot of replacement or would your pipeline be essentially able to run and capture that?

The second one is on the discussions around KEDNY and KEDLI rate case in New York, I think in the press release you mentioned that potentially this may take actually more legal - in the courts, I just wonder if you could give us a bit more colour on effectively I guess the mood of discussions between you and local authorities and to what extent do you think you will get an agreement this year, or it is has to be through the courts do you have any possibilities to see how long this might actually take before an outcome has been reached?

And then the final question is on the tax rate, you guided to 22% tax rate for the coming year, in the last couple of years we were more around 20%, I wonder if you could give us an indication on what you think the more medium term tax rate is likely to be for your company? Thank you.

. . . .

John Pettigrew, Chief Executive
Thank you, so I'll take the first two and then I'll Andy to talk about the tax rate.

So in terms of hydrogen I mean there is a huge amount of work going on across the industry, much of it coordinated by either States in the US or by the government in the UK to make sure that the industry is exploring the potential for hydrogen in a sort of coordinated way.

I mean at this point it is unclear what exactly will be required by the existing network in order to modify it, or whether it needs to be modified at all to be able to support hydrogen. That is exactly the pilot projects that are being developed and are being run at the moment is to really understand what it would take to either increase the amount of hydrogen that sits within a blended solution in the network, or actually potentially moving to clusters of full hydrogen network.

So that's the work that is going to go on over the next few years, both in the work that we're doing in the US and in the UK to really understand what the roadmap will look like and what the investment around it will be.

In terms of KEDLI and KEDNY, so we - you know generally in New York there are two mechanisms by which you agree a rate filing, one is through litigation where you ultimately end up with a one year rate case and the other is through settlement. And through settlement there is always the opportunity to do a multiyear settlement.

I was quite pleased that actually the PSC reinitiated discussions with National Grid at the beginning of this month to see if we could find a settlement for KEDLI and KEDNY. They have extended the period by which we can have those discussions by 90 days. So we will know the outcome in the next quarter.

In the event that you can't agree a settlement then the natural default is to litigate for one year, in the event that we do that we would probably put another filing in relative quickly to cover the fact that it's only a one year rate case. But we remain hopeful that we can find a settlement over the next 90 days.

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Andy Agg, Chief Financial Officer
And just on your third question on the tax rate, as you say 19.9% this year, we're guiding to around 22% next. Over the last couple of years we've had the benefits of some one offs and a couple of settlements across our jurisdictions, so I think 22% probably reflects a more normal rate based on the profit mix. But obviously as US and UK profits vary in the years ahead they will be subject to that change as well. But that's the driver for the increase next year.

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Olivier Van Doosselaere, Exane BNP Paribas
Okay thank you very much.

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John Pettigrew, Chief Executive
Should we go to James from Deutsche?

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James Brand, Deutsche Bank
Hi, I had two questions the first is on the dividend and you've obviously come out with quite a clear reiteration of your dividend policy and that although it's reviewed from time to time this is a policy you think is sustainable over the medium term. Should we judge from that as you see the dividend sustainable through the RIIO-2 regulatory review in the UK under, obviously not necessarily all scenarios, but under most scenarios? That's question number one.

And then the second question is just two - it's a two part one, but just to check on a couple of areas of recovery. You booked about a 400m increase in environmental provisions including a new provision related to gas legacy - kind of gas plant facilities. Can I just check whether you think that will be recoverable under - I'm not sure if it's UK or the US, I guess it's probably the UK, whether that's recoverable or not?

And secondly, you've on slide 18 highlighted that you've moved US IT investment into the regulated segment, which I think you said is 90m last year. Can I check whether that is recoverable? Thanks.

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John Pettigrew, Chief Executive
Okay, so starting with the dividend policy, so yes today we reaffirmed our dividend, so the dividend policy has been in place since 2013, which is to - you know we aim to

increase the dividend by at least UK inflation for the foreseeable future. And quite rightly James as you said that's something that as you'd expect the Board reviews on a regular basis, taking into account business performance as well as regulatory outcomes.

So we understand the importance of sustainability of dividend to our shareholders and that dividend policy of course is underpinned by sensible regulatory outcomes. Today what we talked about is COVID, which as you've seen has got an impact in the short term, but actually it doesn’t change the fundamental economics of the business in the medium term.

And whilst we're still in discussions with regards to RIIO-T2, and we're still hopeful that we can get to a sensible regulatory outcome on that, so that is why the Board has reaffirmed the policy today.

In terms of the environmental charge that you saw, it predominantly relates to the US and a canal called the Gowanus Canal in Brooklyn. This is the cost of a clean-up operation on that canal which goes back actually over 100 years. But we are one of several companies who are the legacy companies that are responsible for the clean-up operation. Those costs are typically recovered as part of our rate filings with the PSC in New York, they have been done historically and our expectation is they will continue to be recovered.

And similarly with regards to IT investment, IT investment is no different to any other investment that we make on the network and therefore it is part of our rate filings and is recovered through our rate cases.

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James Brand, Deutsche Bank
Great, thank you.

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John Pettigrew, Chief Executive
Thanks James, should we go to Mark, Mark Freshney, Credit?

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Mark Freshney, Credit Suisse
Hello can you hear me?

. . . .

John Pettigrew, Chief Executive
We can Mark.

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Mark Freshney, Credit Suisse
Perfect. So I have three questions, firstly a question for Andy on taking off some of the US dollar swaps, you know, I think the strategy a couple of years ago under your previous finance director was for us to only take the goodwill off now we do [audio

jumping] I think you've only got the US 70% hedged. So I was just wondering what's behind that and basically closing out US dollar swaps at the bottom?

My second question is [gap in audio] …

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John Pettigrew, Chief Executive
Mark we've lost you.

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Mark Freshney, Credit Suisse
My second question was on EV [audio jumps] and the policy that you've got there, or the government policy - whether you see much movement and whether you'd be able to get your super chargers by the motorway?

And just thirdly can we expect you to reaffirm the dividend policy or layout a new dividend policy post the RIIO 2 outcome which should hopefully come early next year?

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John Pettigrew, Chief Executive
Okay so let me deal with the second and third and I'll ask Andy to deal with the dollar swap. You broke up slightly Mark but I think the question was around EV charging and our proposal that we've been discussing with the industry and government around an ultrafast charging network.

So I think at the highest level we were pleased to see the announcement in the budget that the government has set aside £500m to actually start to build out that ultrafast charging network. At the current time that task was put to OLEV to work out how exactly that would be used.

My understanding is their aspiration is to have around 650 kilowatt fast chargers at each of the strategic service stations by 2025, increasing to a total I think of around 6,000 ultrafast chargers by 2035. So at the moment we are working with OLEV and with others in the industry about exactly how that £500m will be used to support the connections that are going to be needed and the connection infrastructure investment that's going to be needed to put the capacity into those strategic service stations.

In terms of the dividend policy, as I said Mark, you know the dividend policy remains the same, you know it remains the same as it has been since 2013. And as I said earlier it is underpinned by sensible regulatory outcomes and the Board reviews it on a regular basis, taking into account things like business performance and regulatory developments.

But as of today the dividend policy remains exactly the same.

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Andy Agg, Chief Financial Officer

Yeah and Mark on the US hedge question, it's actually something we've looked at each year and we do that periodically anyway, so we've probably been moving it quite regularly for the last few years.

But the shift this year was again - we look at it against its impact on all of our metrics, not just from a total asset perspective, but impact on earnings, but particularly the impact on cash and credit as part of that. And the view was that bringing it down more closely matched dollar cash flows and provides you know a closer hedge for us in terms of the impact on credit metrics in particularly.

And I think you'll see that if you look at our overall FX impact this year with the dollar rate moving from 1.30 to around 1.24 at close, the net impact on our earnings was around $11m - sorry £11m sorry.

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John Pettigrew, Chief Executive
Thanks Mark. I can see the Verity from HSBC has got a question.

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Verity Mitchell, HSBC
Hi everybody, I've just got a couple of questions. I think the first one is on the pension deficit which has gone up quite a bit in the current year, which is a slightly different story from say some of the UK Water companies that said they benefitted from very favourable discount rates on the 31st of March, perhaps you can remind us when your next triennial valuation is?

And then just secondly a question on CWiP actually, you've had a bit rate - well a 1% rate base increase because of the transfer of assets, can you just talk us through how that profile continues for the next couple of years, in terms of the regulatory in the US?

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Andy Agg, Chief Financial Officer
So thanks Verity, I'll take pensions first, so it's very much a UK/US split this time. So as you compared us to other UK utilities and on our UK schemes we have actually seen a small improvement. It's not as large as some. You may remember earlier in the year we executed the two buy ins, partial buy ins for our gas scheme, which has held back the improvement. But otherwise we have actually seen a slightly larger pension asset under IFRS.

The downside is in the US where because of a big drop in the nominal discount rate we have increased the US pension and healthcare liability by about a billion year on year. So that is why we are seeing a net worsening across the Group.

The important thing is those are IFRS numbers, as always we look at the underlying fundamental valuations, the triennial was as of March 2019, we're just in the final stages of that, but you know we expect that to continue to show very good levels of funding for the UK schemes.

And apologies the second question?

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John Pettigrew, Chief Executive
CWiP.

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Andy Agg, Chief Financial Officer
Sorry CWiP yes. So yes so you've seen this morning this year we have seen $380m move from CWiP into rate base. There is a variety of projects that go through CWiP and it's hard to forecast precisely because of the different longevities, different scales, I suspect next year we wouldn't expect to see such a large movement from CWiP through to rate base. But that's encompassed in our sort of overall guidance - that overall asset growth will be back with the 5 to 7% range this year.

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Verity Mitchell, HSBC
Thank you.

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John Pettigrew, Chief Executive
Thanks Verity. Gus I can see you've got a question.

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Gus Hochschlid, Dept. for Business, Energy & Industrial Strategy (BEIS)
John and Andy a great many thanks, one question if I may and that is with regards to the potential impact of COVID on the current year. And my question really revolves around the potential disparity between such an impact on the UK versus the US. Now clearly I understand the factors - the three factors you alluded to, but I would have thought two of those factors should more or less equally apply to both jurisdictions, so therefore is the forecast a greater impact to the US principally as a result of the absence of new filings in New York? Thank you.

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John Pettigrew, Chief Executive
Thanks Gus, I mean I think the vast majority of the £400m is in the US and predominantly it's because in the US as well as being the network provider we are the supplier as well and therefore we face the bad debts directly that consumers can't pay. And that's why that's in there.

Let's add to that the direct costs associated with COVID, again we do see some of those in the UK, but in the UK we are a B2B business and therefore we have relatively less people in the UK than we do in the US and therefore the costs of things like providing an appropriate working place to be able to deliver capital and operational projects has a lower impact in the UK than in the US.

And of course we are a distribution company in the US as well so we are much more directly linked to where people are living and therefore we have to isolate in a different way. So it's more about the differences in the business than anything else.

The one thing that is common at the headline is that we are seeing lower demands in the US and we are seeing lower demands in the UK and that does impact on the headline figure and on the cash implication. So in the UK we would expect to see potentially lower revenue recovery this year because the demands are lower than we typically would expect when we set the tariffs.

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Gus Hochschlid, Dept. for Business, Energy & Industrial Strategy (BEIS)
Great, a great many thanks.

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John Pettigrew, Chief Executive
Thanks Gus. We have got a couple of more questions to go and we've got a couple more minutes. So Sam from UBS.

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Sam Arie, UBS
Hi good morning John, Andy and everyone, thank you for the presentation today and all your answers so far.

As you said I'm kind of way down the batting order today and I think a lot of the topics that we want to speak about have been touched on already. But do you mind if I try and ask you a sort of high level question that may give you a chance to bring a few of these different points together?

And I think what I want to ask is you know how do we square this exciting, I think confident, very positive view of the business that you give and you talked a lot about the potential contribution to the Energy Transition and so on, with the outlook for earnings, which you know if you look at consensus before today is already sort of flattish for the next few years and probably now maybe nudges down slightly after your guidance today?

And I think if I ask that question I'd sort of break it into two parts. I think the first part is, is there anything you can do to sort of cheer up the earnings outlook this year and next or are we basically stuck with that view for two years?

I mean I know we've got this mini budget from the Chancellor in July and that's set to include a massive infrastructure plan and the US infrastructure plan that's in the pipe. And I'm certainly very interested in your thoughts on both of those. But I assume that they wouldn't really impact earnings of capex you know straight away or in the next couple of years?

So then the second part of the question is sort of coming back to the portfolio and I know Deepa asked the question about disposals earlier and I think Andy you said you don't have anything in mind right now, but SSE yesterday announced a new round of disposal plans, including power networks, they basically said they wouldn't mind running a payout ratio that was more than 100%, they wouldn't mind taking a credit downgrade and even selling stakes in those power networks as long as they can keep paying out and growing the dividend.

So I guess some of those thoughts must have been crossing your minds as well and you've disposed gas distribution in the past and you've still got £6bn of RAV in the gas transmission business. And I'm just interested in generally you think disposals are going to be a feature of things going forward, or do you think it's a good time for disposals, how would you feel about the kind of strategy where you're basically disposing stakes and paying a dividend out of proceeds? Those are my two parts, a bit of a long questions but I'm really interested if you could tie that together for us.

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John Pettigrew, Chief Executive
I'll try and keep it relatively succinct because they are quite big questions, I'll ask Andy to pick up on the second. In terms of the first I do think we are in an exciting time for National Grid and in the energy sector. So in the UK you would have seen that we've submitted our draft business plan that sets out the investment that we believe is necessary over the next five years. And in the US we have continued to submit rate filings on a regular drum beat to support the capital investment that's needed.

You know ultimately those investments; through those regulatory mechanisms will drive earnings. And we have seen that in our US business most recently over the last few years as we've invested more you would have seen the earnings on a GAAP basis increase in line with that asset growth.

In the short term as we set out today we are expecting a short term impact as a result of COVID. But as we've also set out we don't see that having any long term economic impact on the business.

So you know it is an opportunity for us in terms of both maintaining the networks that we have in terms of asset health and resilience, but also in involving ourselves in the opportunities for the green agenda and decarbonisation. And ultimately as long as you get the regulatory mechanisms right the earnings will flow through from those investments.

In terms of the overall portfolio and the sort of credit and so on, Andy?

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Andy Agg, Chief Financial Officer
Yeah so Sam thanks for the question. I guess firstly, you know I'm not going to comment on what SSE said or why they may have said it, but I will give you our view and how I think about the balance sheet and credit and the dividend.

And I think as we have said consistently why the 5 to 7% is a growth rate that we believe sits well with our balance sheet strength the A minus credit rating across the Group and also we are continuing to underpin the progressive dividend policy, you know, at least in line with UK RPI.

So I think that your question sort of implied why haven't we - don't we need to go and do other things to do that and you know at the moment we'd be very much viewing the impact of COVID, as we said today, as a short term timing challenge for us, we're not having significant economy impact in the medium to long term, as John has described a few times. So you know we're comfortable and I'm comfortable with where the balance sheet is, where the ratings are and you know the medium term robustness of the Group.

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John Pettigrew, Chief Executive
Thanks Sam, I've got two questions left and I've got two minutes to go. So why don't we take Ahmed from Jefferies.

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Ahmed Farman, Jefferies
Yes, hi and thank you and thanks for taking my question and thank you for the presentation. Just a few from my side mainly follow up questions. I was hoping that you could provide us a little bit of context for bad debt, if possible, both in terms of absolute numbers and maybe percentage of revenue. So what has been the typical historical run rate, what have you seen in the fiscal year that you just reported? And then what are you sort of - as you put that in the context of what's viewed in the £400m?

And then the second question is - I mean it does seem obviously you're quite sort of confident about recovery most or all of the parts of the 400m impact that you highlighted. Could you maybe provide us some context as to how long such a recovery period was after the sort of financial crisis, I know it's very different, but I thought maybe that sort of context could be helpful for us?

And just my final questions is the difference between the 400m and 1bn, I think you mentioned a couple of buckets there, I was hoping you could give us more granularity around how significant each of those effects are, I think you mention timing differences related to volume and then differences between bill deferrals and bad debts? Thank you.

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John Pettigrew, Chief Executive
Thank you, I'll go first and I'll hand over to Andy to do the last one. So in terms of bad debt I mean typically I think across our business bad debts will run at about 1 to 1.5% of our total revenues. So our total revenue in the US is probably about $13bn. So the additional provision that we took in '19/'20 of 117m is nearly probably a doubling of what that is.

And then as you heard today with regards to the 400m, we'd expect to be taking another charge of a similar magnitude to what we took if not slightly higher than what we took at the end of '19/'20. So hopefully that gives you a sense of the impact that we're considering as part of bad debts relative to the sort of normal run rate.

In terms of recovery, as I said earlier on I mean it is very difficult to determine because it is directly influenced by how the States want to approach it, whether they want to do a separate order, whether they want to do the rate filings and where you are in your rate filing cycle, if it is chosen to go down a rate filing. So it's difficult to say but you know typically it would be over two or three years I guess if I look back historically. But it will depend on when you're doing your rate filings and how the state wants to approach it.

And with regards to the third question Andy?

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Andy Agg, Chief Financial Officer
Yes, so I'm probably going to refer to some of the answers I gave earlier on on this point, which is if you understand the buckets with the 400m, which is what will flow through underlying earnings, you've really got the three extra areas, which will be cash and potentially headline earnings. But because of the mechanisms we have from a timing perspective, so one is demand where we expect lower demand on both sides of the Atlantic to flow through some of our collections and where we collect less than our allowed revenue in a year. That goes through our headline earnings and we automatically get to recover that either the following year or the subsequent year to that.

It's very hard to be precise about the scale of these buckets because you know demand is clearly something that's very hard to forecast, particularly when those peaks and troughs are.

The second element of the billion is US customer collections, so the amount that ultimately we make an assessment of what will finally be uncollectable, which feeds into the bad debts. But assuming that as of 31st of March next year we will still have higher levels of receivables, it doesn't necessarily mean that all those receivables won't be ultimately collectable. And that's how we made our bad debt assessment.

And then the third one is we mentioned right at the start as we work with the industry, particularly in the UK, around extending credit and whether some of that may ultimately fall outside of collection this year as well once those schemes are fully in place.

So again it's very hard to be specific but those are the three broad buckets.

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Ahmed Farman, Jefferies
Thank you.

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John Pettigrew, Chief Executive
Thanks Ahmed. Last but no means least thanks for your patience E…. from Bloomberg, if you take the last question.

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Elchin Mammadov, Bloomberg
Hello everyone, I have a couple of questions, the first one is on demand, I know it's very - a lot of uncertainty and hard to predict, but how long do you reckon it's going to take for the demand to recover to pre-COVID levels, both in Britain and in the US?

And the second questions is on cost recovery, again, very hard to predict but I have to apply a haircut, how confident are you getting I don't know getting 80% or 90% of the recoverable COVID related costs and bad debt and what not? So that's all from me. Thank you.

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John Pettigrew, Chief Executive
Okay I'll take the first and give Andy the second. So in terms of demand - certainly it's an incredibly difficult question to answer. There are two factors that are really influencing you know the rate at which we'll see demand recovery back to normal levels. One is just the depth of the economic impact that COVID will have. And that will in itself vary between States and between the UK and US I'm sure.

And the other is the speed of which each of the individuals States and the UK lifts restrictions. Those two things directly will impact on the levels of demand that we see on our network.

What we have seen in COVID if I use the UK as an example is demands as low as 17% lower than we would have typically expected during this time of year. I would also say that we are just seeing perhaps the early signs of demand recovery as we're seeing some of the restrictions in terms of movement lifting. It is still very early but demands are not quite as low as they were in the early days of COVID. So we are starting to see that recovery. But exactly when it will get back to normal, you know it's very difficult to forecast.

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Andy Agg, Chief Financial Officer
Yes and I think as we've said a couple of times the routes to recovering these extra costs are varies and they vary by State in terms of existing mechanisms, future filings and using precedent in terms of other sort of crisis where we've had significant spend.

So you know we're confident as we said several times this morning that we expect to get the vast majority back, but we're not able at this point to be precise about it - exactly at percentage of that. But we remain confident that it won't have a significant impact on is.

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Elchin Mammadov, Bloomberg
Thanks a lot.

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John Pettigrew, Chief Executive
So let me just close by saying thank you ladies and gentlemen for all your questions. What you've heard this morning is that the performance in '19/'20, although performance was very strong there was a small impact of COVID at the back end. The business continues to deliver despite that new challenge. We are seeing a short term impact as a result of COVID, but we expect there not to be a significant economic impact on the business longer term. And we remain well placed to continue to create long term value for our shareholders and to meet the needs of our customers.

So thank you everybody for joining the call and I hope to see you all very soon in more normal circumstances.

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