National Grid

Full Year Results Presentation 2020/21
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National Grid

Nick Ashworth, Director of Investor Relations

John Pettigrew, Chief Executive Officer

Andy Agg, Chief Financial Officer

Questions

Dominic Nash, Barclays

Chris Laybutt, Morgan Stanley

Jenny Ping, Citi

Mark Freshney, Credit Suisse

John Musk, RBC

Ajay Patel, Goldman Sachs

Sam Arie, UBS

Martin Young, Investec

Deepa Venkateswaran, Bernstein

Ahmed Farman, Jefferies

Elchin Mammadov, Bloomberg

Bartek Kubicki, Societe Generale

Nick Ashworth, Director of Investor Relations
Good morning everyone and welcome to the National Grid Full Year Results Presentation.

I'm Nick Ashworth, Director of Investor Relations, and I'm here with our Chief Executive John Pettigrew, and CFO Andy Agg.

I'm pleased that we're able to join you this morning by video, and that we'll also be able to see you ask questions by video. Instructions are on your webcast screen.

So, before we start, I'd just like to draw your attention to the Cautionary Statement that you'll find at the front of the presentation.

And, after the presentation, as usual, the IR team will be available by phone to help if you have any further questions.

And so with that I'll to hand over to our CEO John Pettigrew. John.

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Key Highlights

John Pettigrew, Chief Executive Officer
Thank you, Nick, and good morning everyone and welcome to the call.

As usual I'm joined by Andy Agg, our CFO, and following the presentation, we'll both be happy to take your questions.

A lot has happened over the past year. We've performed strongly during the pandemic and delivered solid financial performance, testament to the resilience of our businesses and commitment of our people.

It's from this position of strength that we announced our acquisition of WPD in March. This is a transformational development for National Grid, increasing our focus on electricity, putting us firmly at the heart of the energy transition and enhancing the long-term growth profile of the Group.

This transaction alongside our decision to sell a majority stake in our UK Gas Transmission business, combined with a greater level of regulatory certainty, underpins the new 5-year outlook that we're announcing today.

But first, let me start with the financial performance for the year.

On an underlying basis, that is excluding the impact of timing, major storms and exceptional items. Operating profit of £3.3bn was 3% below last year at constant currency, driven by the financial impact of COVID.

Consequently, underlying earnings per share was down 7% to 54.2 pence. And Group return on equity was 10.6%.

Excluding the increase in costs due to COVID, financial performance across our regulated businesses was in line with last year.

Andy will cover the impact of COVID in more detail shortly, but as I've said previously, we expect to recover the majority of these costs over the medium term.

And despite the challenges brought about by COVID, we've delivered another strong year of investment in critical infrastructure.

Capital expenditure was in line with guidance at £5bn, similar to the prior year at constant currency, and adjusting for the Geronimo acquisition. This has driven Group asset growth of 6%.

In line with our policy, the Board has proposed a final dividend of 32.16 pence per share. This takes the total dividend for the year to 49.16 pence, an increase of 1.21%, in line with UK RPI.

Looking forward and reflecting the move from RPI to CPIH in our UK regulated businesses, the Board announced in March, our aim to grow the annual dividend per share, in line with UK CPIH.

Turning next to our safety and reliability performance. Safety is at the heart of performance across our businesses. FY'21 saw our lost time injury frequency rates reduce, with the UK delivering its best ever year of safety.

In the US we also saw a fall in our lost time injury frequency rates. Whilst in National Grid Ventures, we've seen a small rise in minor incidents, and are redoubling our efforts to reverse this trend.

Turning to reliability, performance has remained excellent across our UK and US regulated networks. In particular, I'm really pleased with how the teams have adapted to the changing demand patterns we've seen, over the past 12 months.

In the UK, the Electricity System Operator developed new innovative services, to manage periods of very low levels of demand, coupled with high levels of renewable generation.

And we implemented learnings from the storms in 2018, to manage the highest gas demand seen in a decade, without incident or disruption to our customers.

In the US, electricity network reliability remained excellent at over 99.9%. However, the significant number of severe storms we experienced throughout the year, particularly in Massachusetts, led us to incur, a service quality penalty, of $14m.

We're continuing to take action to improve performance during storms, as well as to re-align our regulatory frameworks, which I'll talk about shortly.

Overall, I'm pleased to say, we delivered another good year for safety and reliability, against a challenging backdrop. And this outcome underpinned our resilient operational performance, which I'll cover now.

So Starting with the US, where we've made good operational progress against our targets. Our financial performance has been impacted by the additional costs of COVID, and a greater number of storms, with our achieved return on equity, decreasing by 210 basis points to 7.2%.

Adjusting for these headwinds, and the impact of rate case delays, shows our return on equity at 8.6%, or 92% of our allowed return.

As we highlighted at our half year results, and as the slide shows, we've seen a greater number of storms across our regions in the past year. However, we've made strong progress to minimise their impact, through upgrading our infrastructure, undertaking weather impact studies, as well as introducing new digital technologies in areas such as vegetation management.

Our success at reducing their impact, means more storms are being categorised as minor, which do not qualify for cost deferral and recovery. We're therefore developing new mechanisms for future rate cases, that will both incentivise improved storm performance, and provide for a greater level of upfront cost recovery.

During the year, we increased investment in critical infrastructure by $200m to $4.3bn, with our single largest area of investment continuing to be our gas pipe replacement programme.

Despite challenges due to COVID, we managed to deliver over 350 miles of mains replacement, exceeding our initial target of 300 miles. This means, we're now well over halfway through, the 20 thousand miles we've identified that we need to replace. This enabled us to continue to deliver strong rate base growth, at 8% in FY'21.

On the regulatory front, we've made significant progress this year. We've reached a joint proposal with the New York Public Service Commission staff for KEDNY/KEDLI in Downstate New York. The 3-year settlement, which includes an allowable ROE of 8.8%, will see us invest $3.3bn to modernise gas infrastructure and enhance network safety; and supports a sustainable and affordable path towards a low-carbon energy future.

In Upstate New York, the new filings for our Niagara Mohawk business are in settlement discussions, and we expect an outcome sometime this summer.

And in November we filed a 5-year rate plan for our Massachusetts Gas business. Hearings are underway, and we expect the new rates to be effective from October this year.

Finally, it's also been a good year for our electricity transmission business. With increasing focus on delivering greater levels of renewable energy, the New York Power Authority has selected National Grid as a partner, in the Northern New York Priority Transmission Project. This project will see us invest an estimated $500m over four years, to rebuild a 100-mile transmission line, supporting the state in meeting its clean energy goals.

So moving to the UK, where FY'21 marked the end of a very successful RIIO-T1 period. Through the 8 years, our total investment reached over £12.5bn and generated over £850m of savings for customers.

In our last year of T1 we achieved a return on equity of 12.6%, within our target range of 200 to 300 basis points of outperformance.

And I'm really pleased to say, that this year in both our Electricity and Gas Transmission businesses, we saw our highest customer and stakeholder satisfaction scores, of the T1 period.

We continued our capital programme with £1.2bn of investment, leading to 2.2% asset growth. Spend was driven by significant progress on the Hinkley Seabank connection, and the second phase of our London Power Tunnels project. This was partly offset by lower spend in Gas Transmission, following the completion of the Feeder 9 project.

We're also investing in new technology, that's helping to support connecting increasing levels of renewable generation on our electricity transmission system. Working with a Californian company called Smart Wires, we're installing smart power flow control devices, that increase our network capacity, without the need to build new lines.

This is the first time this solution has been used at transmission voltages and we've already commissioned three circuits with a further two expected this summer.

On the gas side, we've made significant advances with hydrogen. For example, our ambitious Future Grid project, which is the largest of its kind in the world, will test the options for repurposing the existing transmission network to hydrogen.

Finally, our focus in the UK over the last 12 months, has very much been on reaching a successful outcome for RIIO-T2. Over the 5-year price control, we expect substantially higher investment levels than in RIIO-T1, particularly in Electricity Transmission, where we expect to spend around £8bn on asset health, system reinforcement to connect offshore renewable generation, and other new onshore system connections.

However, whilst we were pleased with the improved package around investment levels in the final determination, we still believe there are strong technical arguments for a higher overall cost of equity and view the outperformance wedge as conceptually flawed.

The CMA has recently granted permission for our appeal, and we'll work closely with them, as this process moves forward through the summer.

Looking now at National Grid Ventures and our Other businesses. Investment of £576m was primarily focused on delivery of our interconnectors. IFA2 was commissioned in January, and the North Sea Link with Norway, and the Viking Link with Denmark, are on track to come on line in 2021 and 2024.

Working in collaboration with Elia and TenneT, we're continuing to assess the feasibility of offshore multi-purpose interconnectors, and believe they can play a key role, in enabling the UK government's ambition for 40 gigawatts of offshore wind.

We've been successful in our Humber Carbon Capture project, receiving a contribution of £56m from Government, to develop a system to capture, transport and store carbon emissions from industries in the Humber and Teesside areas, in partnership with a number of oil and gas majors.

Moving to the US, our onshore renewables business continues to grow, following the completion of our acquisition of Geronimo last year, now renamed National Grid Renewables.

The business operates over 400 megawatts of renewable generation, with another 600 megawatts currently under construction, including Noble, our solar and battery project in Texas, which we expect to begin operations in the first half of 2022.

With regards our other businesses, year-on-year profitability was lower, as a result of fewer land development sales, in our Property division.

So to summarise, we've delivered strong performance across our operations in a very challenging year, and with our announced transactions in March, we've further strengthened the resilience of our business as we look to the future.

So, having spent some time reviewing the year just gone, and before moving on to talk about our new 5-year outlook, I'd like to spend a moment talking about why, I think our portfolio mix is the right one.

National Grid is one of a handful of FTSE 100 companies to have consistently grown its dividend for over 20 years, helped by the balance between different regulatory regimes in the US and the UK, and the ebb and flow of capex requirements as we've seen growth rise and fall at different times in different jurisdictions.

The geographic and regulatory diversity has been key to delivering strong returns, with an annualised total shareholder return of nearly 10% over the past 10 years, versus the FTSE-100 delivering just under 6%.

And, following the completion of our transactions, I'm confident that this diversity, will continue to underpin our performance in the years ahead, given the exciting opportunities we see, including the connection of offshore wind, the infrastructure requirements for EV charging, the critical investment in safety and clean gas growth, and in our National Grid Ventures business, the opportunities with interconnectors and renewables.

As you can see, our portfolio places us firmly at the heart of the energy transition.

And so it's against this backdrop that today, for the first time, we're setting out our longer-term expectations for the Group.

The next 5 years will see us increase our capex to between £30bn and £35bn, the highest ever level of investment for National Grid.

And as we finalise the purchase of WPD, and crystalise our planned asset sales, together with this higher level of investment, we expect this to deliver Group asset growth of 6% to 8% per annum on average to 2026.

We'll deliver this growth whilst maintaining a strong balance sheet, with comfortable headroom at our current credit rating level throughout the period.

Growth in our assets, drives growth in our earnings with Group underlying EPS expected to grow by 5% to 7% per annum on average through to 2026, and to be at, or above the top end of our range, in the early years of this period.

And this will continue to support our policy, of growing the dividend in line with CPIH.

So with that, I'll now hand over to Andy, to go through our full year results, as well as providing a little more detail on our five-year plan.

I'll then come back and talk about our priorities and outlook for the coming year.

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Financial Review

Andy Agg, Chief Financial Officer
Thank you, John, and good morning everyone.

Before covering the Group's full year performance, I'd like to provide the details of the COVID financial impacts we've experienced during this year.

Firstly, I'd like to start by saying that I'm really pleased with the performance we've delivered. Our teams have done a great job in mitigating direct COVID costs, against a tough operating backdrop, whilst continuing to deliver the service our customers expect.

Against our guidance of a £400m underlying operating profit impact from COVID, we've seen an impact of £355m.

Additionally, in the past few weeks, we've recognised £59m revenue recovery in FY'21 for the commodity portion of some of our COVID bad debts. Therefore, our year end underlying operating profit impact from COVID is £296m.

This is made up of, a residual bad debt cost of £120m, a shortfall of revenue under existing rate plans of £78m, net direct COVID costs of £28m, and a £70m impact from delays to new rates being approved in KEDNY and KEDLI.

We also guided to a cash flow impact from COVID of up to £1bn for the full year, with our final cash impact being around £600m, with some elements ultimately being smaller than initially estimated.

As our regions emerge from COVID during FY'22, we continue to expect an impact to be felt from weaker demand and reduced cash collection from our US customers.

But as I've said before, in the US we remain confident that we'll be able to recover the majority of these COVID related costs, either through the usual regulatory mechanisms or through separate filings.

Turning now to the overall Group performance for the year, which was resilient in the face of COVID, delivering a solid financial performance.

As John has mentioned, underlying operating profit was £3.3bn, down 3% at constant currency versus last year mainly reflecting the impact of favourable net income from rate case increases across our US regulated businesses, lower controllable costs in our UK regulated businesses which all together were more than offset by, higher depreciation in UK electricity transmission and, the impact of COVID, including the bad debts in our US business

EPS was down 7% at 54.2 pence, reflecting COVID related costs, a weaker US dollar and lower property sales, all partly offset by lower financing costs.

Our resilient operational performance was also reflected in the 10.6% Group return on equity and our value added per share was 51.3 pence.

Our asset base grew by 5.6%, reflecting capital investment of £5bn, in line with our guidance.

The full year dividend of 49.16 pence per share is up 1.2%, in line with our policy and the Board has recommended a final dividend of 32.16 pence.

Now, looking at the performance of each of our segments in detail.

UK Electricity Transmission delivered another year of strong operational performance, achieving a 13.9% return on equity, 370 basis points above the allowed.

Totex incentives contributed 240 basis points from our streamlined capital delivery processes in load and non-load projects and further opex efficiency savings.

Other incentives and legacy allowances contributed 130 basis points, 50 basis points above last year.

Underlying operating profit of £1.1bn was down 4%, largely due to the impact of COVID and higher depreciation.

The UK efficiency programme continued to deliver savings, with a further £34m reduction in controllable costs compared to the prior year, in total exceeding the £100m overall UK efficiency savings target we set two years ago.

Capital investment at £1.1bn was 3% higher than last year, primarily due to continued 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 our year-end regulated asset value by 3.1% to £14.6bn.

UK Gas Transmission delivered a return on equity of 9.6%, reflecting the higher capital costs of key compressor and data centre projects.

Other incentive performance at 90 basis points, was below last year due to lower shrinkage performance.

Underlying operating profit of £438m was up £36m, or 9%, compared to FY'20. This is primarily due to higher revenues, year on year RPI uplift and lower controllable costs.

Capital investment was £176m, £73m lower than last year, due to the completion of several large projects and lower spend on compressor projects and IT infrastructure.

And including inflation, the regulated asset value was flat year on year at £6.3bn.

Turning now to our US business.

The return on equity, excluding COVID, higher levels of non-deferrable storm costs and impact of rate case delays that John mentioned, was 8.6%, 92% of the allowed level.

After taking account of storms and incremental COVID costs the return on equity was 7.2%.

Underlying operating profit was £1.5bn, driven by an increase in net revenues of £216m at constant currency, reflecting rate increases and capital trackers, more than offset by an increase in controllable costs due to higher IT costs and inflation, higher depreciation due to growth in the rate base, and a year-on-year increase in COVID costs.

We've increased investment in our US networks, to $4.3bn, driving strong rate base growth of 8% to $27.6bn.

Assets outside rate base, excluding working capital, grew year on year to $3.2bn reflecting our investment in several multiyear projects we expect to be coming into service in future years.

National Grid Ventures contributed £354m, an increase of 5% on last year, including the first period of operation for IFA2, our second interconnector to France.

Grain LNG profits were higher than last year due to the extension of asset lives in line with our new contracts, and metering profits fell less than expected, reflecting a slower decline in our legacy meter population.

Capital investment decreased significantly to £509m, mainly driven by the non-recurrence of the acquisition of Geronimo and lower investment in our interconnector projects as they progress towards completion.

Our Other activities had a net charge of £61m, £34m higher than prior year reflecting fewer property sales and slightly higher insurance costs.

Our venture capital business, National Grid Partners, invested £38m, £21m lower than FY'20 at constant currency due to reduced activity at the start of the year in the early months of COVID.

Financing costs decreased by 8% at constant currency, to £942m, mostly due to lower RPI and favourable borrowing rates. The effective interest rate for the year decreased from 4.1% to 3.2%.

The underlying effective tax rate was 21.2%, 130 basis points higher than FY'20, primarily as a result of a smaller impact from tax credits relating to prior years.

Underlying earnings were down 5% at £1.9bn and underlying earnings per share decreased 7% to 54.2 pence.

Operating cash flow was £4.6bn, £300m lower than last year driven by increased storm costs, lower US customer collections, and reduced UK revenues.

During the year, we raised £5.6bn of senior debt and the year-end closing net debt was £29.7bn, including a £1.6bn favourable movement from exchange rates.

After adjusting for Rhode Island as an asset held for sale, the revised closing net debt was £28.6bn.

Our regulatory gearing for the year was at 65% and the RCF to debt and FFO debt metrics were 6.6% and 11.7% respectively. These both reflect lower revenues and COVID costs and, as we have previously said, the credit agencies have signalled they are willing to look through any short term COVID related weakness.

Going forward we expect to be comfortably positioned in our new rating band and this rating position, coupled with our regulatory frameworks, means we're well placed as we look to the future.

So, turning to our guidance, and starting with the current year. As usual, business by business detail is given in our forward guidance section in the results statement.

This forward guidance is based on our existing businesses for the entire year. Given this scenario, we expect FY'22 underlying EPS growth, to be towards, or above, the top end of the 5% to7% growth range, as set out in our 5-year guidance.

Our earnings outlook will change as the transactions move forward through the course of the year.

We expect to provide guidance on WPD by half year results, and WPD's earnings will be included in Group results from the point of deal completion.

We expect to commence the sale process for a majority stake in Gas Transmission in the second half of this financial year, and therefore under accounting rules, we expect this business to be classified as a discontinued operation. This means we'll have to remove all of its contribution to the Group results when this change in disclosure is made.

For Rhode Island, we would expect to include it earnings in our FY'22 results up to the point-of-sale completion.

So, putting this together we still expect to deliver FY'22 underlying EPS towards, or above, the top end of the 5% to 7% growth range, as set out in our 5-year guidance.

Turning now to that longer term guidance. As you'll have seen earlier, our five-year financial framework is presented based on WPD being a full member of our Group, the sale of Rhode Island completing by the end of the financial year and the sale of a majority stake of Gas Transmission completing during FY'23.

We're confident in the visibility that the £30bn to £35bn Group investment levels to FY'26 gives us and I'd like to give a little more detail about this.

In the UK we expect investment levels of around £8bn in Electricity Transmission will be needed during the RIIO-T2 period. As we explained when we accepted the majority of the T2 package, this will cover asset health, anticipatory and system reinforcement to facilitate offshore generation and other new onshore system connections.

We expect the WPD networks to be investing £4bn to £5bn over the next 5 years in asset maintenance, facilitating the infrastructure for electric vehicles and directly connected generation.

In our US businesses we expect investment of around £17bn over the years to FY'26. And as we've explained previously, this includes safety related projects in our gas networks, storm hardening and other net zero investments in our electricity distribution networks, as well as incremental investment in electricity transmission projects.

Lastly, we expect that National Grid ventures will invest £2bn to £3bn over 5 years, focusing on our interconnector programme and continued investment in US renewable generation.

As we complete the WPD purchase, subsequent asset sales, and deliver the capital investment programme, whilst taking in to account the broad economic protection our businesses have against rising macro variables such as inflation, Group asset growth is expected to be 6% to 8% per year on average to FY'26.

I've said previously that while we settle the WPD, Rhode Island and gas transmission transactions, Group gearing levels will be above current levels. Over the 5 years to FY'26, under our central assumption of CPI at 2%, we expect regulatory gearing to increase through the transactions, and then to settle above 70% once all three transactions are completed.

However, throughout the period, we expect our long run gearing levels, and the other standard metrics we monitor, to sit comfortably within our current BBB+, Baa1 corporate rating band from S&P and Moodys, and as a result we do not expect any further rating action at a Group level.

The changing mix of the Group, coupled with the strong growth opportunities we see across our businesses in the coming years is expected to deliver compound annual growth rate in underlying earnings per share in the 5% to 7% range, through to FY'26, including our long run scrip take up assumption of 25% per annum.

As we work through the transactions, together with recovery from the impact of COVID, we would expect earnings growth to be at, or above the top end of our range, in the early years. This will continue to underpin our sustainable dividend policy into the future.

So, to summarise, we've performed strongly in mitigating the direct costs of COVID and continue to work with regulators on cost recovery mechanisms, we've delivered £5bn investment in critical infrastructure and achieved a solid underlying financial performance. The recent acquisitions have enhanced the long-term growth profile of the Group, and our confidence is reflected in the new 5-year financial framework we have set out today.

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 Officer
Thank you, Andy. So, hopefully you can appreciate from what Andy and I have covered this morning, it's been a very busy year for the Group, and I'm pleased with the significant progress that we've made.

Within the 5-year framework we've outlined today, in the coming year our priorities are to complete our proposed transactions, maintain our regulatory progress, build momentum through stakeholder engagement, and continue to lead the debate, on climate action.

Turning first to our transactions. Our first priority will be to complete the WPD purchase this summer, and then file, the final business plan for RIIO-ED2 by the end of the year.

Preparations for the sale of our Gas Transmission business are well underway, and we still expect to launch the process in the second half of this year.

And regulatory clearances regarding our Rhode Island business are also anticipated by the end of our financial year.

Our intention is to host a capital markets event in Q4, where we'll provide more detail on our longer-term plans, and the growth opportunities we see across our businesses.

Alongside this, we'll continue to progress our regulatory agenda. In the UK, with regards to our RIIO-T2 appeal to the CMA, we expect a final determination at the end of October. And whilst not a direct read-across, we were encouraged by the CMA's recent decision on the Water PR19 review, and continue to believe, our strong technical arguments should lead to a higher level of return.

In the US, in our Upstate New York filings, we're working on agreeing a multi-year settlement, which will include investment to support decarbonised heat, whilst maintaining a focus on managing customer affordability. New rates are expected to become effective in July 2021.

And in Massachusetts Gas, the distribution filing we made in June, it proposed a new performance-based rate mechanism, that will link annual revenue increases to inflation. It also proposes funding for projects to decarbonise the gas network, including hydrogen, renewable natural gas, and demand side measures. We expect new rates to become effective from October 2021.

Whilst working with regulators on these filings, we're also excited to see greater levels of political and stakeholder engagement across all aspects of the energy transition.

In New York, we've recently published a joint report with Con Edison, and the Mayor's office, on Pathways to a Carbon-Neutral New York City. This study highlights, the critical need for continued investment in gas networks, to maintain system safety, reliability, and affordability, as we continue the energy transition.

In Massachusetts, the regulator is also consulting on the Future of Heat, as it looks to develop roadmaps with the gas distribution companies, that will help the state to achieve its 2050 net zero target.

We'll use our experience of developing scenarios for the energy transition in the UK, as well as our recent study in New York, to develop pathways, that can meet these targets, in an efficient way for our customers.

2021 will also be a very busy year with UK political engagement. We're expecting to see a transport decarbonisation plan, the publication of the UK's hydrogen strategy, BEIS's consultation on net zero governance, and further thoughts on the offshore transmission review. And we'll be engaging across all of these topics and more.

And as you've heard me say many times, our ambition is to enable the energy transition for all, and we'll continue to lead the debate on this.

This November's UN COP26 conference in Glasgow, provides us with a perfect platform to do just that, and I'm proud that National Grid is a Principal Partner of this event.

The Responsible Business Charter we laid out last year sets out our climate change strategy, including how we'll support transitioning to a cleaner energy system, a system that is vital to meet the ambitious net zero targets set by governments, regulators, and businesses.

This summer, we'll see the first publication of our Responsible Business Report, alongside our Annual report. This will showcase the priorities we've set, and actions we're taking, in delivering our climate and responsible business goals. It'll enable people to track our progress, bringing all our sustainability reporting into one place.

And I'm pleased to announce that this report will include our new Scope 3 reduction emissions target, aligned to the Science Based Target initiative, to reduce carbon emissions by 37.5% by 2034 from our 2019 baseline.

In the years ahead, we'll invest to accelerate the energy transition for all our customers, in regulated electricity and gas networks, and adjacent infrastructure that supports the goals of energy decarbonisation.

So to summarise, this is shaping up to be a defining year ahead, as we make a significant strategic pivot towards electricity, with the integration of WPD, reach an outcome on the CMA appeal on RIIO-T2, and agree new rates for upstate New York and Massachusetts Gas, work on defining net zero roadmaps, across both the UK and US, whilst also using our voice to influence climate change action, in the run up to COP26. And we're in a strong position to enact this change.

Our geographic and regulatory diversification will continue to underpin the stability of the business, as it's done over the course of the past 20 years, and it provides the platform to build on the huge number of opportunities that we see ahead.

This attractive asset growth will drive sustainable long-term earnings growth, maintaining and underpinning our dividend policy.

I'm very excited about delivering the ambitious 5 year plans we've set out, and the increasingly important role that National Grid is playing in the energy transition.

Now, before we come to questions, I'd just like to take a moment to thank Nicola Shaw who is stepping down from her role later this year. Nicola has helped to drive the UK business forward in her 5 years with the company and we wish her well for the future.

And, after over 9 years as Chairman, Sir Peter Gershon will be retiring from the Board at the end of the month. Sir Peter has made an outstanding contribution to National Grid during his tenure. National Grid is a very different and much better positioned Group to the one he joined.

I would personally like to thank him for the support and advice he has given to me, during that time.

With that, I'll thank you for listening and Andy and I will be happy to take your questions.

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Questions and Answers

Nick Ashworth, Director of Investor Relations
Thanks John. Now it's time for our Q&A. As a reminder, the instructions to ask a question are on your webcast screen and on the Q&A slide that you can see in front of you.

I'm going to hand back over to John now who will start with the video questions. John, over to you.

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John Pettigrew, Chief Executive Officer
Okay, thanks Nick. So I can see there's lots of hands up, so should we start with Dominic and then go to Chris Laybutt. So Dominic.

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Dominic Nash, Barclays
Hi, everyone, hopefully you can hear me okay. Two questions from me please.

The first question is on the capex number in the guidance you've given us of £30bn to £35bn. Within that you've obviously given us quite a tight range for ED, Electricity Distribution. The draft - can you just give us a little bit of colour there, is the draft business plan being submitted before completion of WPD? And how involved have you been on developing that plan? And do you think Ofgem will adopt a number of scenarios similar to the RIIO 2 transmission programme.

So basically the question I'm leading into is how much scope for uncertainty is there around that £4bn to £5bn?

And the second question I've got, I'm intrigued by the JV that was announced this morning with RWE on US offshore wind. Can you provide some details on this, like what size project are you lining up and is this an enduring JV, or is this a JV just for a one-off project in the US? Thank you.

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John Pettigrew, Chief Executive Officer
Thanks Dominic. So let me just pick up on the capex question first. So as you heard today what we tried to set out is a range of £30bn to £35bn, I think to reflect the confidence that we have in the transparency of the regulatory frameworks that we now see. So as you know in Electricity Transmission, we accepted the vast majority of the RIIO T2 price control and therefore we've got good visibility of what we expect the investment to be.

Similarly, you would have seen recently that we've just agreed KEDLI and KEDNY, $3.3bn over the next three years, with a potential extension for a fourth year.

With regards to WPD, obviously they have submitted their first draft business plan, they received feedback from their stakeholders. They are about to submit their second draft business plan at the end of July. That will go through the usual iteration that you'd expect during these types of price controls. And they will make a final business plan submission in December.

We've set out in our outlook that we expect it to be £4bn to £5bn. I think we are reasonably confident with that level of investment. Ofgem, usually, will look at various scenarios, but when we look at the fundamentals in terms of asset replacement, connections for distributed generation and new customers, and then supporting EVs, I think the range that we've set out for the Group of £30bn to £35bn looks very sensible and we're very comfortable with that.

With regards to RWE and the announcement on that, so as you know over the last few years, we've always looked to use the capabilities that we have in National Grid to look to adjacent markets. Most recently, over the last three of four years, that has been in our interconnectors business, as well as onshore solar in renewables with the acquisition of Geronimo, which is now National Grid Renewables.

So over the last few years we've build up a fantastic capability of being able to develop these offshore cables. Add to that the local knowledge we have in the North East and the RWE JV just looks like a national extension.

So, as always, we take a very disciplined approach to any investments that we take. We are not expecting there to be significant capex in the short term. As you know the development of offshore wind has a long lead time, both in terms of the seabed lease process and then ultimately the construction. So modest capex in the next three to four years, but we do see it as a natural extension of our National Grid Ventures business.

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Dominic Nash, Barclays
Following on from that, is it a JV that covers RWE for all offshore in North America, or is it just that single project?

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John Pettigrew, Chief Executive Officer
It's focusing on the developments as we see them today in the North East and we'll see how we take that forward on it. So it's not just a single project, it is a relationship for offshore wind in the North East of the US.

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Dominic Nash, Barclays
Thank you.

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John Pettigrew, Chief Executive Officer
Okay, should we take Chris's question and then turn to Jenny.

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Chris Laybutt, Morgan Stanley
Good morning, thank you very much. And I guess a thank you from me also for providing five-year guidance at EPS, that's very useful for us. In terms of that guidance, our immediate thoughts this morning went to the impact of COVID on '21, which was 6 to 7 pence at EPS on our calculations. Reflecting on your recent experience with the PSC, do you think that might be a little bit more challenging than previously thought to recover that amount? And how long do you think that might take to recover that lost ground?

And then secondly, just on storms, it looks like non-deferrable storm costs have increased fairly significantly in the period. Do you think that's a trend which will be ongoing and if so, how long do you think it will take for your proposed mechanisms to be in place to recover these costs? Are they in specific areas under the mandate of specific regulators, or is it quite widespread? Just some more detail would be very helpful. Thank you.

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John Pettigrew, Chief Executive Officer
Thanks Chris. Why don't I take the second then Andy, if you want to pick up the first?

So in terms of the non-deferrable storms, I mean what we actually saw in the last 12 months Chris is probably a doubling of the level of storms that we normally see at this time of year. And at one level we're sort of a victim of our success, which is the storms, when they do happen, are having a lower impact on our customer base and therefore rather than being classed as major storms, which we can then defer and get recovery on, they're being captured as minor storms.

So we've recognised that issue in terms of our improved performance when we have storms and we've started to engage with regulators in Massachusetts Rhode Island and New York, about how we can ensure that the rate filings that we do going forwards capture fairly the actual cost of minor storms as they come along.

I think it's too early to assume that we're actually seeing more storms every year going forward. We are doing some work look at the weather and whether there is an impact that's more sort of permanent. But at the moment we're engaging with our regulators to make sure that when we go our rate filings, we get some upfront recovery, as well as being incentivised on the performance of storms. Andy.

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Andy Agg, Chief Financial Officer

Thanks John. So in terms of the recovery, I think as we've said previously the recovery of the COVID costs, particularly the bad debts that we've incurred to date, we still expect to recovery the majority of those, but as we've previously said, we expect that to be over a period of time, so into the medium term, you know, years rather than months.

The element that we reported today, the £59m of commodity recovery is if you like the first instalment. But we expect that to come back in over a period of time.

I think in terms of FY'22, absolutely we expect a much smaller impact of COVID, as we mentioned this morning, some ongoing minor impacts in terms of US collections and bad debts. But in terms of the overall guidance for FY'22, as well as COVID, you obviously need to look at the impacts of the Electricity Transmission business moving into T2 and also the higher interest costs that we guided to this morning as well.

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Chris Laybutt, Morgan Stanley
So Andy, in terms of that COVID impact, which gets a little bit, I guess - you're paring in back in '22, but do we assume that by the end of the five years you've recovered all of that lost ground and so that sort of 6 to 7 pence, comes back to you in the form of earnings, is that the assumption underpinning the guidance?

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Andy Agg, Chief Financial Officer
I mean it's hard to be precise until we've agreed all of those specific mechanisms, but I think it's fair to say that over the period of five years we would anticipate recovering the majority of it. But we'll be able to firm that up once we get the specific mechanisms in place.

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Chris Laybutt, Morgan Stanley
Thank you.

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John Pettigrew, Chief Executive Officer
Thanks Chris. Should we go to Jenny and then to Mark Freshney?

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Jenny Ping, Citi
Hi, thanks. A couple of questions please. If I can just follow on from Dominic's question in terms of the RWE JV. Is this a venture for Geronimo that's specifically focused on the North East of the US, or are you thinking of going offshore wind more globally, so really making grounds in entering that market? That’s the first question.

And then secondly, just on your Ventures business, you talk about a capex of £2bn to £3bn, predominantly linked to the interconnectors, as well as the US Renewables business. Can you talk a little bit more about multipurpose interconnectors, the £23bn to £29bn that the UK Government is talking about to connect the 30 gigawatts? And more specifically, you know, because the £2bn to £3bn capex that you've highlighted what is the potential scope and also timelines of when we can hear from the Government on this?

And then linked to that I guess is - you're talking about a 70% debt to RAV already post transactions. So if the MPIs were to come along and further growth in Ventures, does that mean you need to raise additional equity, or is - the hybrids possibility will cover that? Thanks.

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John Pettigrew, Chief Executive Officer
Okay, thanks Jenny, there's quite a lot of questions there, so I'll just work through all of that. So in terms of the JV with RWE and our thinking about involvement in offshore wind, this is very much around the North East of the US. So as I've said previously, we look for opportunities where we've got capabilities and that we can create value for our shareholders.

We have fantastic expertise in offshore cables, and we have fantastic expertise in understanding onshore transmission and distribution in the North East. So that capabilities means that we're a strong partner with RWE in that region. But we're not looking to expand beyond that. We will focus on the regions that we know best.

In terms of the National Grid Ventures and the £2bn to £3bn, so we have a great pipeline of investment opportunities. As Andy and I have said many times we'll be disciplined around that. so those opportunities include potentially things like MPIs, as well as onshore solar and wind in the US.

With regards to the MPIs, at the moment it's a relatively early concept, we think that it has potential in terms of mitigating some of the cost impacts of connecting offshore wind, whilst take advantage of connecting the UK with the rest of Europe. So hence why we're working with TenneT and Elia to think through that.

In terms of the broader sort of capex to connect the 30 gigawatts of offshore wind, I think the current review that's going on with BEIS on the Offshore Transmission Review is incredibly important. I think everybody recognises that the concept of every single individual offshore wind farm connecting to the East Coast is going to be problematic from a planning perspective and therefore a degree of coordination is needed. From our perspective, clearly when we understand exactly the timing of that investment then we'll be able to have a better understanding of how much investment is needed onshore.

One of the things that National Grid has been advocating for and others in the industry are, is to have a clearer blueprint of what the networks look like, both offshore and onshore by 2030. And we'll continue to advocate that. And I know that Ofgem have recently started to engage in this issue to try and get a better understanding of what infrastructure investment is needed.

Andy, do you want to pick up the second point?

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Andy Agg, Chief Financial Officer
Yeah, so Jenny in terms of I guess your point about the funding of those potential additional investments, I think as John said, the timescales may be slightly further out, given the elements that need to be worked through. So we are comfortable in terms of funding the range of investments we put out.

And as we've always said, you know, to make disciplined decisions about investing in additional projects we want to make sure we have the right regulatory or other frameworks to ensure appropriate funding for those and recovery of those investments as well. So we'd made those decisions down the track. But at this point we're very comfortable with the framework we've set out this morning.

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Jenny Ping, Citi
Thank you.

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John Pettigrew, Chief Executive Officer
Okay, thanks. Should we take Mark, and then should we go to John Musk after that?

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Mark Freshney, Credit Suisse
Hello, thank you for taking my questions. I have two major questions. The first one is on the Ofgem report on System Operator Independence that they have sent to BEIS. We've heard very little on that since then. When you meet with BEIS ministers, you know, what are they saying and how likely is it that you may be forced to look at independent ownership there?

And just secondly on the Gas Transmission business, returns - we know the RIIO 1 price control was just inappropriate for that business eight years ago, we know that, and you know in the final year of RIIO 1 the ROEs were almost unacceptable, the outperformance was almost unacceptable. But in terms of RIIO 2 how is that review looking for that business? And what steps have you and Nicola and the MD of that business made to turnaround performance ahead of sale?

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John Pettigrew, Chief Executive Officer
Thank you, Mark. In terms of the Electricity System Operator, you're quite right, so that last sort of key piece of news was Ofgem's consultation that looked at its thoughts on the future role of the ESO.

Since then things haven't hugely progressed, the next step in the process is the BEIS are due to issue a broader consultation around the institutional arrangements that will support the energy transition to net zero to the UK.

National Grid's position hasn't changed either, in that we continue to work with Ofgem and BEIS. We believe it is important to look at the institutional arrangements and inevitably as part of that you get into the role of the ESO. Until you do that broader piece looking right across the industry it's difficult to decide whether it's right that the ESO should be further separated from National Grid.

So we're participating in that, the exact timing for BEIS to do their consultation, I think it's slightly unclear, I know it's due this year but whether it's before the summer recess or after I'm not yet clear, Mark. But we continue to participate in that discussion as we said at the half year results.

In terms of Gas Transmission, so in terms of - as you know as part of the price control for RIIO T2 we accepted the vast majority of the price control, both for Electricity Transmission and Gas Transmission. You'll recall that when we had the session on that we talked about £10bn of investment across the UK, £8bn of that related to the Electricity Transmission and just under £2bn of it to Gas Transmission.

So there is a step up in the level of investment that's been agreed as part of RIIO T2, compared to T1 for Gas Transmission. And we were comfortable that that base level of capex, together with the uncertainty mechanisms that were put in place to deal with things like compressor replacement for environmental issues was sufficient for us to be able to agree to those levels.

So given that we remain confident that we've got the right levels of capex to support the business going forwards.

In terms of the sale process itself, we're still in the early stages of that. So as we said back in March, we're intending to launch the process in the second half of this year. We believe it will be a competitive process. you know the Gas Transmission business is a strong business, it's got a great reputation and with the clarity of regulation that we now have we expect that that will be a competitive process.

Thanks Mark. Should we go to John and then we'll go to Ajay after that?

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John Musk, RBC
Morning, two questions from me. Firstly on the CMA process, I just wanted to understand what sort of input you've had into that since that's ticked off, what discussions there may have been between them and you, or is it very much that you've submitted your files and you're just waiting to hear back?

And then secondly, I did have a question on ESO as well, but Mark took that. But can you just give the numbers of the System Operator this year, or sorry in FY'21, what did that contribute at EBIT and what is it as a share of RCV or a number for the RCV?

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John Pettigrew, Chief Executive Officer
Thanks John, I'll let Andy pick up the numbers on the ESO. I mean in terms of the CMA process, so as you know our application was - in terms of the challenge around the cost of equity and the outperformance wedge was agreed. Actually this week there were clarification sessions with the Commission, so Nicola Shaw and the team were actually in front of the Commission this week. But it was very much around clarification and understanding of the submission that we'd made.

The next steps are there will be sessions around cost of equity, outperformance wedge, and for the other networks of course they refer to other aspects. And the timing is I think August for draft decision and then a final decision in October. So we are engaged with the Commission and this week really has been the first step when we've been in front of the commission to be able to make some points. Andy.

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Andy Agg, Chief Financial Officer
Yeah, John, just in terms of the ESO so its operating profit for FY'21 was £70m, so that's significantly down on last year because we had some specific one-off recovery amounts last year around some of the data centre work in particular. So £70m this year and I think that's consistent with what we've said for many years, which is it's a very small part of the overall organisation, around 2% of the total business.

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John Pettigrew, Chief Executive Officer
Thanks John, should we take Ajay and then go to Sam after that?

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Ajay Patel, Goldman Sachs
Good morning and thank you very much for the presentation. So I have two questions. Firstly, the one on the earnings growth over the next five years, is there any chance we could unpack that a little bit. So you know what proportion is - is there synergies in there from the WPD deal or is that not yet included, or any sort of broad proportion of the growth that comes from synergies?

What are you assuming for the sort of outcome of the reviews - are you assuming returns that are equivalent to what you've just received in Transmission or you assuming maybe with the CMA, would that be an uplift for example?

Then on the US, maybe another way of looking at it is what sort of cumulative bill increases do you think you need over the five years to attain that earnings target? To give us a sense of what may be required in the rate cases.

And then sort of more strategically - there has been a sizable change here away from gas and towards electricity as a function of that announced deals that you've made. And I was just wondering is the journey finished, or why is this the right split for the company? Maybe some thoughts there would be really, really helpful. Thank you very much.

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John Pettigrew, Chief Executive Officer
Okay, well why don't I pick up on the strategic question and then let Andy pick up on the financial questions. In terms of the strategic position - you know as we set out in March the opportunity for us to participate at scale in the UK came along with the WPD transaction. It did allow us to shift the overall Group to around about 70% electric and 30% gas and we feel that gives us the right sort of geographic and regulatory diversity that actually has delivered the sustainable returns that I talked about in my remarks this morning.

So if you look over the last ten years, we've been able to deliver total shareholder returns of just under 10% against the FTSE of 6%. And over the 20 years we've been able to deliver sustainable increases in the dividend.

So I think when we look at the overall shape of the Group, in terms of diversity and regulation we feel very comfortable.

And then added to that it really reflects I think a sort of broader view we have about how we see the energy transition. So there is no doubt we're going to see significant growth in electricity demand, but there is also no doubt that we're going to see gas play a significantly important role in this energy transition. So when we put all that today I think we're very comfortable that the shape we've got in the Group is the right one. Andy.

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Andy Agg, Chief Financial Officer
Thanks John. So Ajay, just in relation to the five-year guidance, as you can imagine a group of this size over a period of that time there's many different parameters involved in that. And what we've set out this morning is a range that we're very comfortable with in terms of the set of balanced assumptions allowing for the fact that some of those will change. You called out a few in terms of both cost efficiency, regulatory outcomes potentially from the CMA and so forth.

I think what I'd say is we're comfortable that we've made a sensible set of assumptions, based on the regulatory frameworks that we have and that it converts into a sensible bill profile. As you've seen just in the KEDLI/KEDNY joint proposal this week we've been very focused on that with our regulators in New York, for example agreeing the zero and then two and two for the outer years. And we're comfortable - you know we are focused on driving cost efficiency as we always do, that that is something that we can convert through to the appropriate level of earnings growth.

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Ajay Patel, Goldman Sachs
And I just follow up on that Andy. I just want to check that that guidance does include synergy benefits from this deal and the base level returns on the reviews at least, so that we know that these are incremental to come, or is some quantity already in the numbers? It's just so that we have a reference point to start with.

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Andy Agg, Chief Financial Officer
Again, we're not going to get drawn into specifics. I think, as we said back in March when we announced the transactions, you know, when we think about the opportunities going forward, we're confident there are opportunities to continue to deliver value for us customers through the WPD transaction and for all our stakeholders. And I think that's part of what we'll be working through as we go ahead, but, you know, we will have to continue to work on those.

I think I'd say again, you know, we're confident we've set out the right range to allow for, you know, many different outcomes in those parameters in this point.

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Ajay Patel, Goldman Sachs
Okay, all right, fair enough. Thank you very much.

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John Pettigrew, Chief Executive Officer
Okay. Shall we go to Sam and then go to Martin after that?

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Sam Arie, UBS
Hi.

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John Pettigrew, Chief Executive Officer
Thanks, Sam.

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Sam Arie, UBS
Thank you. Good morning, everybody. I have a question for Andy on the guidance and then maybe a bigger picture one for you, John.

But, Andy, let me start with the guidance question - I'm always a bit nervous when I'm kind of way down the line of questions and nobody's asked my question yet, which makes me worry, perhaps I misunderstand something, but it seems to me something very important changed on gas today. So can I just check, you've given us a five-year guidance now, which is working back from a '25/'26 number that includes zero contribution from gas at all. So you're confirming that, I guess, not just the 50% still but 100% of the gas is out of the result by '25/'26?

And then, if I heard your comments correctly earlier on in the voiceover, you might be taking 100% of gas out of the result from the second half of this year, so not even keeping, you know, a 49% associate holding, and yet you still think, in the early years of the five years, you'll beat the 5% to 7% EPS range? I mean, that sounds quite bullish and good to me, but can I just confirm, Andy, that I've understood that correctly?

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Andy Agg, Chief Financial Officer
So, not quite. Let me just take you through the two bits quickly. In terms of the five-year guidance, as you said, you know, the capex that we've set out, the £30bn to £35bn, you're absolutely right, that doesn't include an element in relation to Gas Transmission effectively because that is relating to how we will be reporting our capex. When we have a minority ongoing stake in that business, that will not show up, if you like, in our capex. That will be included in within our minority interests that will be reported through, you know, the dividend stream that we would expect to retain.   So, it’s not in the £30bn to £35bn, but it is included in the earnings trajectory and, ultimately, the asset growth because, obviously, our retained share in that business through to FY'26.

The point that I made this morning in my comments around the accounting rules is, you are right, that, effectively, as soon as we get to the point of the sale becoming highly probable, which we would expect to happen once we've launched the process and worked through some of the separation work that we need to step through, that, absolutely, we will have to report the whole income of Gas Transmission as discontinued through this period, even though, ultimately, we expect to retain, you know, as we said, a significant minority stake. That’s just, unfortunately, how the accounting rules require us to report it.

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Sam Arie, UBS
Okay, but can I just confirm, in the 5% to 7% EPS growth, that's including a 49% gas minority then in the '25/'26 year or it's including nothing on gas?

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Andy Agg, Chief Financial Officer
In terms of the EPS guidance we've given this morning, it continues to assume a retained minority stake, yeah.

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Sam Arie, UBS
Oh, right.

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Andy Agg, Chief Financial Officer
We haven't been specific about the size.

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Sam Arie, UBS
Okay. Well, that, kind of, triggers a follow-on question. Apologies, but I suppose, you know - and I think it was a great package that you put out today and a really good presentation, the only thing that we thought there might be questions on is the sort of, implication, you said 5% to 7% earnings growth over five years, but you might be at the top of that range or slightly above in the earlier years.

If I just look at where consensus is for this coming year, consensus is looking for nearly 62p, which is, what, 14% above what you've just announced for the year completed. So I was wondering if that difference was explained by the fact that, you know, you're not going to be including any of the gas, in a surprising way, but now I think I understand that you are still including, basically, half the gas at the bottom line. So I wonder if, maybe, that means consensus is overcooking a little bit the WPD contribution for this year or could there be some other explanation? I'm assuming, I guess, Andy, that, you know, 14% would be not within what you're saying about early years EPS growth being above the 5% to 7% range.

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Andy Agg, Chief Financial Officer
Yeah, so I think it's probably not for me now to try and, you know, interpret exactly what's in consensus across different analysts.

I think, as you set out this morning, it is a complicated story. I understand that. And, obviously, over the next few days, I'm sure the team will be very happy to help you through that.

What we've been clear on this morning is, as we said, in the early years of the five, we do expect to be at, or, you know, potentially, above the top end. We do have to take account of the discontinued operations, but we're, as I said this morning, we're comfortable with that range, even with including that accounting impact that we've set out this morning.

Beyond that, it's probably sensible that we, sort of, catch up with you offline with that.

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Sam Arie, UBS

Okay. Very good. Thanks for your help on that. And, John, if I could maybe turn to you with just my bigger picture question, but I can't resist asking because you did mention the climate conference at the end of the year, and I know you're very close to the powers that be organising that conference this year. Can you just share with us any sense that you have of what actually might be achieved at that conference? I suppose, Madrid was the last one and that was a great disappointment that nothing was actually signed. What do you think might actually happen at Glasgow?

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John Pettigrew, Chief Executive Officer
Yeah, thanks, Sam. Difficult to know exactly what will happen at Glasgow, but I think what I would say is, what we've seen over the last, sort of, six to nine months in the run-up to COP26 is increasing alignment and increasingly ambitious targets being set from various countries, including the US. So I think there is a sense of optimism that something significant can be achieved at COP26.

I know that the UK Government is very keen to be able to lay out roadmaps by sector for what net zero will look like going forward as one of their objectives, so I'm pretty optimistic. I think it's a fantastic opportunity for the UK to be able to showcase all the great work that we've done so far, and actually some of the good things that we're doing to support net zero going forward as well. So, we're very proud to be a principal partner.

I'm pretty optimistic, actually, that it could be, you know, a very significant UN conference, given what I've seen in the run-up over the last six to nine months.

Okay, thanks, Sam. I'm going to go to Martin I think, and then I'm going to go Deepa.

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Martin Young, Investec
Yeah, good morning to everybody. I've got a couple of questions if I can, please. The first relates to, sort of, the high-level thinking about returns for distribution, electricity distribution in the UK.

If we look at the CMA report and your own comments this morning, I don’t think there's any validity whatsoever to the idea of the outperformance wedge, so let's assume, you know, that goes, and transmission returns get positioned higher. But, if you step back and think about where the action really is likely to be over the next five, six, seven, eight years plus, it's going to be in electricity distribution with, you know, heat pump deployment, EV charging deployment, etc. You know, given the CMA comments around an uplift to the range, you know, for networks that require investment in resilience, etc, should we be thinking that the distribution rate of return should be higher than what, ultimately, gets awarded for transmission?

The second question gets back to the five-year guidance. I note that you've based that on an exchange rate of $1.3 to the pound. Obviously, we're above that level at this juncture. You know, if we were to mark that at $1.4, a little above $1.4, what would that do the guidance that you've set out this morning? Thanks.

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John Pettigrew, Chief Executive Officer
Okay. Thank you, Martin. I'll take the first question and I'll ask Andy to take the second.

So, in terms of distribution returns, I'll start with just reflecting on where we are with the CMA process for, you know, Gas Distribution and Electricity Transmission companies. I think we took some heart from the PR19 process in that there was an awful lot in there that, I think, reinforced our view that it was right to make the technical referral that we did. And I think, although, as I said in my remarks, you can't do a direct read-across. I think, if you, you know, just apply some of the logic that they've taken for the water companies to the energy companies, you will end up with a higher return than where Ofgem were in their final determination.

I think, added to that, I sort of concur with your thoughts in that, in terms of Electricity Distribution, clearly, over the next five years, there's going to be a significant need for investment to support EVs given the acceleration of the Government's target together with the need to continue to connect distributor generation. And, therefore, it does need to be in an environment that attracts investment.

I think Ofgem themselves, about 12 months ago, talked about the fact that they felt that electricity distribution was where the action would be over the next five years and therefore, you know, if you take that logic, you would suggest that you would want to see a higher return than for transmission.

Having said all that, it's early days, you know, WPD will be putting its draft business plan in at the end of the July, and then it will listen to its stakeholders before putting its final plan in at the end of December, but, you know, I definitely agree, there is an awful lot to be done, and we want to create the right environment if we're going to meet these targets that the Government has set. Andy?

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Andy Agg, Chief Financial Officer
Yeah, no, thanks, Martin. In terms of FX, as you'll know, we continue to run a significant hedge of our dollar balance sheet and our dollar assets, and that continues, you know, to give us a significant level of protection in terms of earnings volatility as well.

So, broadly, you know, as we've seen this year, around a 5 cent swing, and the average rate was just over half a penny, so it's that sort of range, you know, if you wanted to do something for your modelling.

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Martin Young, Investec
Thanks.

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John Pettigrew, Chief Executive Officer
Okay, thank you. I'm going to go to Deepa, and then I'm going go to Ahmed. So, Deepa?

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Deepa Venkateswaran, Bernstein
Thanks. I have a few questions. So, the first one is on the US business. So, next year, you've guided to a 100-basis point improvement in ROI, which would still only get you to 8.2%, so I was whether, you know, what is the mid-term objective? Do we still aim for 95% of the allowed ROIs, so towards that 9% number? So any guidance on that.

And then, long-term, how should we think about the EBIT trajectory of this division versus this '21 phase, given that now you've at least got more and more visibility on your KEDNY/KEDLI settlement. That's one area which is a bit unclear for me.

Second, a question just on the Gas Transmission sale process, when do you think the market will have an idea what valuation that asset will get? I mean, are we talking about Q3 of calendar '22 or will you already have some indication before that?

And just a clarification on, Andy, when you gave the guidance, when you've said that you expect it to be more than at the top end of the range for this year, if you took all these transaction impacts into account, can I just confirm that, on that one, Gas Transmission is not included at all, not even as associate, whereas, in your longer term guidance for the next five years, it is included as a minority?

So those would be my main questions. And the last one for you, John, I'm sure you read the IEA's Net Zero Pathway Report, so I was just wondering if you had any reflections, particularly on, you know, the mammoth task of four times scale-up in renewables in just ten years? And, you know, any thoughts on that would be greatly appreciated. Thanks.

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John Pettigrew, Chief Executive Officer
Thanks, Deepa. So I think I captured five questions there, so let me have a go at the first, the third and the fifth and then I'll let Andy do the second and the fourth I think he captured.

So, in terms of US returns, I think in our guidance we've set out some of the things that have pushed returns back this year which, you know, we're not assuming that are going to be repeated next. So, our position on US returns, you know, my position's always been the same, which is our aim to get as close to the allowed return as possible, and that will be the focus of the business going forward.

We're pleased that we've now got a settlement in KEDLI and KEDNY, and three-year settlement with an agreed capex, and $3.3bn and an 8.8% ROI. And, as you know, we've got a filing in Niagara Mohawk to complete this summer, and then Massachusetts Gas later on this year.

So, you know, our focus will continue to be to get the regulatory frameworks to recognise the challenges of affordability, but also the need for investment, but the team's aim is always to get as close to the allowed returns as possible.

In terms of the Gas Transmission sale, so just in terms of the process, so we are still in the position where we're likely to launch the process in the second half of this year.

As I've said previously, we've got quite a bit of work to do to separate out Gas Transmission from the UK business, but our base plan is that we will launch in the second half.

In terms of valuations, you know, if it follows a similar drumbeat of timings to the Gas Distribution sale, then it's likely to be around the turn of the year, but, you know, we will have a much clearer view, I think, after the summer than we have today. But my baseline assumption would be around about then.

And, in terms of the report you mentioned, I think, from our perspective, you know, we believe a lot of the targets that have been set are achievable but hugely ambitious. What we've said consistently is that we need to get the right policies and the right regulation in place. But really 2021 and 2022 needs to be the year when we start to really execution if we're going to deliver the levels of renewables and the levels of decarbonisation that have been set out in, you know, lots of reports over the last six months or so. Andy?

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Andy Agg, Chief Financial Officer
Yeah, thanks. So, Deepa, on the two, I think the first one was around how does the sort of, returns and expectations in the US flow through into earnings and operating profit of that business. And I think, as we said previously, you know, on the basis that we are continuing to target maintaining and delivering a good returns performance, over time, we would anticipate that the capex growth, and the asset growth that we're driving, will then, you know, effectively, get delivered through the earnings trajectory for that business as well.

As we've seen in, you know, the most recent rate cases we talked about this morning with KEDNY and KEDLI, in the short-term, clearly, there's a focus on customer bills, but, again, we've maintained a balanced set of assumptions looking forward and, with that, we would expect the earnings and the operating profits of the US business to go on an upwards trajectory in line with the asset growth.

In terms of GT, yes, I think is the short answer. So, as we said, for next year, the discontinue treatment means that we, effectively, have to report the whole earnings of Gas Transmission out of our FY'22 numbers. That's what we've mentioned in terms of the next year with the flow-through of the transactions in FY'22. But you're right then, in FY'26, the five-year frame continues to assume that we earn our share from the retained minority interest in that business going forward.

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John Pettigrew, Chief Executive Officer
Okay. Thanks, Andy. Shall we go to Ahmed and then go to Elchin? So, Ahmed.

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Ahmed Farman, Jefferies
Yes, morning. Thank you for taking my questions. A few from my side.

I think, when you originally provided us the guidance for March '21, you talked about a £1bn cash impact on various, sort of, COVID-related issues, and you've, sort of, come in at £600m, so I just wanted to understand a little bit better the variation there.

And then, if you could also just talk a little bit about cash collection trends in the US and, you know, what, at your end, you can do to, sort of, improve those, that would be helpful.

And then, just finally, on the transaction effects that you outline on Page 21, and I'm just, sort of, really thinking here about the EPS bridge between '21 and '22, are you able to, sort of, give us a little bit of granularity as to what these means at the EPS level on a net basis, year-on-year impact? That would very helpful. Thank you.

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John Pettigrew, Chief Executive Officer
Thanks. Andy?

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Andy Agg, Chief Financial Officer
Okay, yeah, sure. So, on the first one, I think a few points in terms of what's driving that. I think, clearly, you know, in terms of the original guidance, we were, you know, deliberately, at the time, estimating how, you know, significant it could be. And, what we've seen, as we've gone through the year, is there's a number of elements for that which have actually come in slightly inside our expectations, so, the impact, for example, on UK demand flowing through into the revenues for the Transmission business, also some of the volume reductions in the US business as well have been slightly less.

We've still seen, as you imagine, in terms of, you know, the bad debt impact, we've still seen some lower US customer collections and, therefore, larger outstanding receivables in the US. That’s still feeding through into that £600m. But all-in-all, just some of our estimations come in slightly inside, you know, what we were expecting when we set that guidance a year ago.

In terms of cash collections, I think a variety of things. To be clear, all the three states that we're in still have restrictions on ability to enact, you know, some of the specific measures around customer collections and, you know, termination for default, etc. A lot of that is still being pushed out because of COVID, quite rightly. But we are working very closely with our customers, a range of measures in terms of, you know, obviously there is federal support for low-income households and other measures like that which enable us to continue to get revenues, you know, across our customer base.

So, we're doing what we can, and we'd expect some of those measures to either be taken away or, potentially, extended, depending on each legislator in the three states that we operate in.

And then, in terms of FY22, obviously, you know, there's the detail in the Results Statement. I think what I'd call out in terms of the bridge from '21 to '22 is we don't expect, as we said earlier, such a significant impact from COVID next year. There's a small amount still, potentially, in US bad debts that we anticipate. So the bulk of that will come back from an earnings perspective.

We've guided to the impact of moving into T2, particularly in Electricity Transmission, and then we've also mentioned the fact here that the interest rates and the interest charge is likely to increase year-on-year.

So those are the three things I'd call out, but, as I say, the detail is set out in the Results Statement.

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John Pettigrew, Chief Executive Officer
Okay. Thank you, Andy. Shall we go to Elchin and then to Bartek?

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Elchin Mammadov, Bloomberg
Hi, everyone. I have two questions, well about two topics. The first one is on rising yields and rates. Are you expecting any upward pressure on your ROI in the US business particularly? So any benefit from that given your upcoming rate case reviews? And, similarly, are you expecting any potential negative impact on the valuation of your UK Gas business?

And the second set of questions on your ESG metrics, please. I mean, following the divestments of UK GT and Rhode Island, you mentioned that the share of gas will fall to 30% of the assets, are there any plans to divest the remaining Gas business to further improve your ESG metrics, maybe that remaining minority stake possibly?

And the second part of the ESG metrics question that is not clear to me is, on your CCUS projects that you could potentially go into, would that have any impact on your emissions reporting? I don't know how CCUS counts when it comes to emissions, so if you can give us a bit more colour on that that would be great.

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John Pettigrew, Chief Executive Officer
Yeah, so I'll go to the second question and I'll ask Andy to pick put up the first.

So, with regard to the ESG metrics, I mean, I think, you know, the key message I want to get across today is the new target that we've set for our Scope 3 emissions of 37.5% reduction.

In terms of those emissions that we see in National Grid, you know, the vast majority of our emissions in that area are through the sale of Gas to our customers in the US. We don't have any intention of further divestment for, you know, the reasons I set out earlier, which is that we're very comfortable with the overall shape of the portfolio.

We think it's important that we work with our key stakeholders to work through the energy transition, and that includes the decarbonisation of gas and heat, and we think there are some, you know, really important opportunities, both in terms of renewable natural gas as well as things like repurposing the networks for hydrogen.

So, our focus is very much on those areas in terms of the actions that we can take to help with climate change and with our ESG targets.

In terms of CCUS, CCUS is a partnership that we're working on. As I said earlier, in my remarks, we've got support from the UK Government to look at these zero carbon clusters in the North East. Our role would be to help to develop the transport of the carbon dioxide that we captured as part of that process.

So, in terms of the target itself, it's not going to impact on the targets that we've set out, but, clearly, it is an important role as we think about the broader agenda in the UK, about how we decarbonise gas. So, you know, what we're looking at there is a cluster whereby industry can, potentially, use hydrogen rather than natural gas. Generation is using hydrogen either directly, to create electricity, or that it's being captured at the back end through the carbon capture storage, and then we transport the carbon dioxide that is captured back to oil gas fields in the North Sea.

So, I think it's a really positive project, it's got significant government support, as you will have seen as part of the Prime Minister's ten-point plan, and we're working with our partners on that, on the sort of, early engineering feasibility of it. Andy?

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Andy Agg, Chief Financial Officer
Yeah. Thanks, John. So, I think, in terms of the two areas, in terms of the US ROIs, so, as you're probably aware, the methodology for setting US cost of equity is well-established, it's a very mathematical calculation and, subject to, sort of, you know, reviews through to the litigation process as well.

So, you know, there could, potentially, be upside if those rates stay high for longer. We'll have to wait and see. It's not something that we're anticipating, and it's certainly not something we've assumed in the guidance we've set out this morning, but one other thing I would say is that, actually, cost of equity has held up very resiliently when we've been through such an elongated low-rate period. But, yes, there is potential upside in the future, but we're not banking on that today.

In terms of Gas Transmission, I think two things. Obviously, the debt book within the Gas Transmission business is a long-term portfolio. It has a good proportion of both index-linked debt and also fixed rate debt as well. So, we don't have a significant exposure to short-term rate movements.

Obviously, we have the debt tracker mechanism in that business as well, which has served us well. And I think, going into T2 and beyond, obviously, we've agreed the indexation of the cost of equity as part of the new price control as well. So, with all of those, I'm comfortable that, you know, we have a lot of protection against any concerns in the macro rate environment.

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John Pettigrew, Chief Executive Officer
Thanks, Andy.

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Elchin Mammadov, Bloomberg
Thank you.

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John Pettigrew, Chief Executive Officer
Thanks. Unfortunately, we've run out of time, so I'm going to make this the last question. So, Bartek, do you want to ask your question?

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Bartek Kubicki, Societe Generale
Sure. Good morning. Thank you for this. Two questions.

Firstly, I would like to ask you about this FY'22 guidance for the UK. You are talking a 30% revenues increasing in both NGGT and NGET, but, on the other hand, there is also guidance for quite significant costs increase which could also be revenues. Consequently, I would like to ask you whether you can elaborate a little bit more, what is the key driver of those costs, apart from depreciation, of course, and whether this could be somehow compensated through regulatory mechanisms?

And, secondly, I would like to ask you about the inflation protection in the US, of course, in the UK, it's clear, everything is inflation indexed, but, if we are facing rising inflation in the US, how are you protected from the regulatory point of view and from that, and whether this would squeeze your future ROEs?

And, thirdly, if you don't mind, on WPD, it has quite a lot of high coupon bonds in its portfolio, so I just wonder, once you buy it, what are you going to do with this? Are you going to somehow refinance, or will you keep their bonds on your balance sheet? Thank you.

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John Pettigrew, Chief Executive Officer
Yeah. So, thanks, Bartek. Why don't I take the second one on inflation and I'll ask Andy to pick up the first and the third.

So, if you look across the Group for National Grid, actually, we have reasonable protection against higher inflation. So, in the UK, obviously, we get indexation of our regulated asset base and, as a consequence to that, our revenues will follow it.

In the US, we have the ability to pass through the costs in our transmission FERC-regulated businesses.

You're probably aware that, last year, we agreed a new regulatory formula in Massachusetts for Massachusetts Electric, which is effectively an RPI minus X-type form of regulation. So, again, we get indexation there. And we have, as part of our rate filing on the gas side, done exactly the same.

And, with regard with New York, then we're able to project cost increases as part of any multi-year settlement, which, of course, we would have done as part of KEDLI and KEDNY, and we will do in Niagara Mohawk.

If we see significant inflation, you've always got the ability in the US to be able to go back in and do a subsequent rate filing. So a little bit of exposure when you've got a multi-year settlement in New York, but, across the vast majority of the Group, we've got, you know, reasonable protection against higher inflation. Andy?

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Andy Agg, Chief Financial Officer
Yeah, thanks. So, in terms of the question around the UK costs, as we look into FY'22, and you mentioned depreciation, obviously, that is one of the drivers with the continued growth in the asset base.

I think, remember, that the UK also includes the System Operator. There is a significant level of investment in new technology in terms of, you know, delivering their programme of work over the next five years as part of their price control. So a lot of that is passed through. So the recovery is, you know, assured, but it does flow through our numbers as opex costs, which is one of the drivers.

And then, just secondly, across the rest of the Transmission business as we deliver our increased work programmes we've talked about this morning, stepping up towards the £10bn of investment over the five years, that clearly comes with some associated opex. But the important thing, again, those are included in the allowances that have been agreed for T2.

And then on the WPD point, you know, I think I mentioned this when we announced the transactions back in March, yes, conscious that the debt book does have some high coupon debt in it today. We don't have any immediate plans for, sort of, any focused effort on that. We would expect the debt book to churn, obviously, as we go through the next few years and we refinance. And, therefore, I'd expect some opportunities as we go through that, but nothing, sort of, specifically on that at this point.

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John Pettigrew, Chief Executive Officer
Thank you. Thank you, Andy.

So, as I said, unfortunately, we've run out of time. Can I just say thank you, everybody, for joining us on the results call today.

As you, hopefully, have got a true sense, we're very excited about what we set out in terms of our five-year plans to deliver £30bn to £35bn over the next five years, and we look forward to seeing you all where we'll share a lot more detail with you on each of the businesses at our Capital Markets event later in the year. So thank you for joining us.

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