

## Iberdrola – Decarbonization pioneer contributing to the path to net zero

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### **Jean-Hugues de Lamaze:**

Welcome to another edition of TortoiseEcofin's ongoing series about the global energy evolution. I'm Jean-Hugues de Lamaze, Managing Director and Senior Portfolio Manager of Ecofin in London. And I'm glad today to be joined by José Sainz Armada, Chief Financial Officer of the Iberdrola Group, one of the largest utility companies in Europe and in the world. Iberdrola, as most of you know, is one of the world leaders in power and renewable energy with dominant positions in Europe, the UK, but also in the U.S. and LATAM, including Mexico and Brazil.

In the U.S., the group is present through its listed subsidiary Avangrid, the third largest wind energy producer in the United States and a distributor of electricity and gas in several Northeastern States. Avangrid just announced a few days ago a strategic merger with New Mexico-based, PNM Resources. The transaction clearly illustrates Iberdrola's ambition to be at the forefront of the global energy transition. So Pepe, thank you for being with us today and I'll kick off with a pretty broad question. How do you see Iberdrola playing a role in the global energy transition and the path to net zero emissions over the next few years?

### **José Sainz Armada (“Pepe”):**

Okay. Hello and thank you Jean-Hugues and TortoiseEcofin for giving me the opportunity to chat with you. I will try to answer as best as I can all your question. I think that, as you know, Iberdrola has been one of the pioneers in decarbonizing. We were investing in renewables when none of the large utilities had started to invest. This was almost 20 years ago. I think that time has proved us right. Right now we have also expanded our footprint not only in Spain, but in other geographies like the U.S., as you have mentioned, other countries in Europe, etc.

I think that times now give us a great opportunity to continue investing in renewables and in networks because obviously you need to connect all these renewable sources. You need to improve the network system to provide more information, to provide more services to clients and to absorb the volatility of the renewable energy. So, I think that today as politicians, as countries want to accelerate the decarbonization role, we've been one of the largest players in this area worldwide. I think that we can take advantage in the different geographies in the U.S. and in Europe. We have just recently also gotten a position in the Asia Pacific, in Australia.

So, I think that we can play this role in the global transition by investing as we have been doing in the last years in renewables and in networks. And accelerating this investment in the countries where we are present, as more and more incentives will be done by politicians for these investments and as the renewable technologies become cheaper and more competitive compared to other technologies.

### **Jean-Hugues de Lamaze:**

Yeah. Thank you Pepe. So, how does the strategic merger with PNM Resources that you announced a few days ago fit into those plans? What does it bring to your group?

### **José Sainz Armada (“Pepe”):**

I think that first it increases our diversification in the U.S. We have been trying to grow in the U.S. We have never hidden that we were also open to doing corporate transactions. It gives us a footprint in an area we know well because Texas is the largest or the second largest state for us in renewables. So, we have around 1,300 megawatts in New Mexico. Also, we have

a renewables development in addition to a good connection with New Mexico for many years as we chair one of the scholarships in the University in New Mexico.

There are also states with top high growth potential for us, where investments are needed, where more renewables are going to be developed. That gives us an additional footprint there. And I think that for us, it is a way to continue growing in the U.S. in another geographical area that is a very good area for renewable investments and is an area where traditionally the GDP has been growing fast and where there are needs for further investments in this area.

**Jean-Hugues de Lamaze:**

So, how would you describe the U.S. utility landscape overall? Can you expect further consolidation going forward? How do you see the prospects there?

**José Sainz Armada (“Pepe”):**

Yeah, I think that the U.S. utilities traditionally have been relatively small. I think that a lot of them, due to the lack of size, with situations in which you could improve best practices, in which you could improve through purchasing models that are centralized. They don't have enough resources to do big investments. I think that the U.S., as in other countries, need big investments in the utility sector, probably in the U.S. more than in Europe, at least in the east part due to the situation of the grid.

I think that if you have relatively small companies, it's going to be difficult for them to do what they have to do. So, in principle, what we are seeing is a consolidation. We are already seeing a consolidation in this market of companies getting together to have more access to technology, to have more access to best practices, to have more access to capital, so that they can invest in, this global transition that is happening across the world and in the U.S., I think that the utility system in the U.S. will continue to consolidate.

**Jean-Hugues de Lamaze:**

Okay. That's interesting. So, when I look at Iberdrola obviously, historically your group has been present across all parts of the utility value chain, but, over the recent years, your capital allocation has been focused to a very significant extent on renewables and networks. Do you still see value in thermal power generation and also in the downstream part of the utility value chain? Do you think infrastructure is or could be the key going forward?

**José Sainz Armada (“Pepe”):**

Well, first of all, what is going to happen is that the traditional power is going to become renewable. So, in the end, what we are doing is just moving from one generation of technologies that were creating CO<sub>2</sub> emissions and were responsible for the heating of the planet to other technologies that will allow people to have energy, but without emitting CO<sub>2</sub>.

We think that it is important, to have a client base because first, you can't sell the electricity to your clients without having to go through the spot markets or through very competitive auctions. So, I think it makes a lot of sense to try to have clients for your own electricity consumption. In addition, as the economy electrifies, you will be offering to each client more prototype services. You will be offering them mobility. You will be offering them heating. You will be offering them efficiency, etc. So, in that sense, what we see is that having clients improve substantially in the long term the economics of having renewable generation, because you have a final client to whom you can sell energy and you can sell other products and services and improve the returns.

**Jean-Hugues de Lamaze:**

Okay. Thank you. Talking about the renewable technologies, clearly Iberdrola is one of the largest producers of wind power in the world. And you seem to have an edge in offshore wind. What do you see is your main competitive advantage there?

**José Sainz Armada (“Pepe”):**

Well up to now, we have been doing offshore in countries where we have an established presence. But also the fact that we are one of the largest utilities and we are buyers, not only of offshore platforms or offshore turbines, but also onshore and transmission and distribution cables, etc., gives us a strong, competitive advantage in terms of the purchasing, in terms of the costs of building offshore. In addition, offshore is like oil technologies, you need to learn how to do it. As you do more, you get more economies of scale. As you have more experience, you'll have the teams that are prepared, and you'll have access to the suppliers. So, that gives you an edge over those that are starting. I think that we have that edge.

The second is being a very large company. This allows us to bring talent from the rest of the group. So right now we have in London, more than 300 people only dedicated to offshore from 20 nationalities. That gives us a big, important position in terms of designing, in terms of the project management, etc.

Finally offshore, versus others, have a problem in which normally the time to cast is relatively long. Afterwards it is very profitable and creates a lot of EBITDA but you have to invest more. As a company that has a strong balance sheet and is able to finance these investments without major problems, that means also that we have access to relatively cheap financing versus others, and allows us to absorb this time lag between when we start the projects until we finalize them. And obviously suppliers, etc., are comfortable in working with us as we are a company that has a very strong, profile. So, I think that we have a lot of competitive advantages and that is what is allowing us to continue doing this business and increasing profitability.

**Jean-Hugues de Lamaze:**

And recently you've been also increasing your presence in solar. Is that also an area where you'd like to go further? Is the idea to have a pretty diversified mix of technologies? What are your views on the solar market in that sense?

**José Sainz Armada (“Pepe”):**

Well, you have answered with your question. Solar is another technology that we need. It is a technology that has its advantages, it is cheap, it always works more or less at the same time. So it is a compliment to other technologies. When you have hydro, when you have pumping, when you have onshore, when you have offshore, solar is another element. It's something which is a part of the business mix and it makes sense. In addition to that, if you, for example, have pumping you can use solar when prices are down. And because there is too much energy produced by solar you use it to pump water, or you can use solar also to produce green hydrogen.

So, it has not only, its use as another technology, but it is complimentary if you have a diversified portfolio of renewables and also it can be used for industrial processes. Solar is a cheap technology. So, it looks like you are doing a lot of megawatts of solar, but in terms of investment, probably we're going to invest more in offshore than in solar, because the production is not that large. You have to do a lot of megawatts to have a decent size in solar. While it is very dangerous to have solar as a standalone product because either you'll go through auctions or you sell the electricity to very large clients, or if not, you cannot provide electricity 24 hours a day, seven days a week to your clients. You need to have a diversified energy production to offer that to clients.

**Jean-Hugues de Lamaze:**

Okay. Do you see the equivalent potential for renewables development in the U.S. compared to Europe? Obviously in Europe, we hear a lot of the political debates around a tightening of the 2030 decarbonization targets, which is bound to fuel growth in the region. It's more debated or less clear in the U.S. as it stands. Do you still see equivalent growth potential?

**José Sainz Armada (“Pepe”):**

In the short term the push of the EU for this decarbonization, etc. is much bigger than what you are seeing in the U.S. In terms of the long term, the U.S. probably has better conditions because it has a lot of space, something that Europe doesn't have. It has a lot of capacity, not only in solar, if you have a good transmission network in the U.S. because most of the people in the U.S. live on the coast. So there is a lot of space. One of the problems that Europe is going to have is that it is too heavily populated to deploy all these renewables.

The U.S. has also huge potential in offshore, in both coasts, probably in the west coast they will have to wait until there is that floating offshore, but that is going to come. So, I think that in general the U.S. has a big competitive advantage to produce a lot of renewables. Probably in the short term, this push of Europe is going to give us more visibility in Europe. But I think that you will see in the plan that U.S. is going to be the market where we're going to be investing more in the next years.

**Jean-Hugues de Lamaze:**

Yeah, it's interesting. I was reading yesterday, an interview from your chairman that you did eight acquisitions so far this year in 2020, and obviously your two largest as you referred to earlier were in Australia and the U.S. So I assume that gives a signal about where the group is aiming to grow. Do you have an ideal geographical allocation projected for your group?

**José Sainz Armada (“Pepe”):**

Most of our investments are still going to be in the countries where we have a strong presence, in Europe and in the U.S. in high rated countries. So in that sense, that will be the same. Australia gives us a good platform to see what's happening in the Asia Pacific area, especially in offshore. But I think that most of the investments are going to be in the areas where we have a presence. Probably most of the investments are going to be in Europe and in the U.S.

**Jean-Hugues de Lamaze:**

The traditional acquisition size of Iberdrola, it's more small- to mid-size. Do you see the current market as a market which pushes for larger scale transactions? Do you expect your M&A activity to be on larger deals than before or not necessarily?

**José Sainz Armada (“Pepe”):**

Well in our plan, we are not contemplating more M&A. Another thing is that obviously, if some small M&A, as you have pointed out helps us to increase our pipeline in renewables etc., I think that is something which I wouldn't call M&A. For example, the deal that we did in France in the end was acquiring a portfolio of renewable pipeline plus some renewable already in operation. These sorts of things, yes. In the U.S. I think before doing something, or even thinking of doing something, we have to get the authorization from the authorities that will take a year. And then make the integration between Avangrid and PNM. The last time that we did that in the U.S. was back in 2015. We don't have any plans to do more M&A for the time being except these relatively small acquisitions that help us to develop more renewables together with our organic pipeline.

**Jean-Hugues de Lamaze:**

And do you see it as a concern that several of the oil majors have stated recently significant ambitions to grow further in the green energy universe? Do you expect it to make this a much more competitive context for you to grow?

**José Sainz Armada (“Pepe”):**

In the long term, no. Because what is going to happen is that there is going to be a much larger area or a much larger place where we all invest. Taking into account that as the economy electrifies, there will be more opportunities to invest and to do things. So in that sense, it is true that they have said that they are going to enter into the electricity market, but also it is true that this market is becoming bigger and bigger and their market is going to become smaller and smaller. So in the end, I suppose that they need to jump into the electricity world to try to defend their assets, their clients and their business. On the other side I think that as always you need the experience, you need knowledge, you need to develop pipelines and all these sorts of things.

And they are coming with very aggressive targets in terms of renewable developments or clients, but in the end up to now, they haven't done much meaning that if they don't start working on developing pipelines or buying clients on a large scale or these sorts of things in the end they are not going to be able to do what they are saying. It is not easy to, for example, in offshore, you need to have the lease areas. You need to have your process of authorizations, etc. They can go and buy and pay a very high price for some areas, but in the end that makes them less competitive because in the cost of the analysis of course, they have to take into account how much the lease, or the area has cost them.

So in that sense, I think that we still have strong competitive advantage compared to them to continue doing our job. There will be more competition in some specific moments. There might be, but there are also going to be much larger opportunities. And the U.S. wants to increase their offshore. The UK wants to increase their offshore. Europe wants to increase their offshore, so everybody wants to do more renewables. So being a bigger cake, we can maintain our part or even increase it as we are trying.

**Jean-Hugues de Lamaze:**

That's interesting. And Pepe, I'd like to ask you a last question on a topic which is discussed across the globe, and you've only alluded to, which is hydrogen. So what's your view on the technology? How do you see Iberdrola playing a role in the segment and its growth potential going forward?

**José Sainz Armada (“Pepe”):**

We want to be one of the early adopters or one of the early movers in this technology. Actually, we are already with some projects that we are presenting to the European Union, but not only to produce hydrogen as a way to store electricity, but also hydrogen electricity is a very important element in a lot of industrial processes. They could have done that only by replacing green hydrogen what today is grey hydrogen, which is the one that is produced by gas. It's equivalent to the annual European demand of electricity.

So there could be more uses for hydrogen as technology evolves. So in that sense, the market for hydrogen is huge. It will take some time. It will need some support because today green hydrogen is not as competitive as grey hydrogen, but I think that the same way it was done with solar and with wind at some point it will become more competitive. And I think to fuel industrial processes within green hydrogen would be a massive opportunity.

**Jean-Hugues de Lamaze:**

That's really interesting, fascinating. Congratulations for all the work to transform Iberdrola, into a world leading group present in all the segments of the global energy transition. Thank you Pepe, all the best for the future.

**José Sainz Armada (“Pepe”):**

Thank you Jean-Hugues.

**Jean-Hugues de Lamaze:**

And thank you on behalf of the TortoiseEcofin group. All the best.

**José Sainz Armada (“Pepe”):**

Thank you to you and the TortoiseEcofin group. Thank you very much.

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