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As a major transmission and dispatching operator, we invest in skills, technology and innovation to ensure that we are well equipped to plan, develop and maintain the grid (Transmission Operator), and guarantee an electricity service that is balanced, secure and high quality (System Operator). Italy and Terna are at the centre of a system that includes 25 interconnections with neighbouring countries: this gives us a leading role to play in energy integration in Europe and the Mediterranean area. This know-how is, naturally, also applied in our Non-regulated and International activities. ”

+2.9%

EBITDA IN 2018

+5.5%

CAPEX IN 2018

+2.5%

TERNA'S SHARE PRICE  
IN 2018



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Performance

# Financial review 2018

## Introduction

The Annual Report for 2018 has been prepared in accordance with the requirements of art. 154-ter of Legislative Decree 58/98 introduced by Legislative Decree 195 of 6 November 2007 (the “Transparency Decree”), as amended by Legislative Decree 27 of 27 January 2010.

As required by Legislative Decree 38 of 28 February 2005 and EEC Regulation 1606/2002, the financial statements of the parent company Terna S.p.A. and the consolidated financial statements of the Terna Group for the year ended 31 December 2018 were prepared in compliance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission (hereinafter “EU-IFRS”).

In compliance with the provisions of art. 2364 of the Italian Civil Code and art. 9.2 of the Company’s Articles of Association, the Board of Directors, has decided to call an Annual General Meeting of shareholders within 180 days of the end of the annual reporting period, given that Terna S.p.A. is a company required to prepare consolidated financial statements.

## Basis of presentation

The measurement and recognition criteria applied in this Annual Report are consistent with those adopted in the consolidated financial statements for the year ended 31 December 2017, with the exception of the application of the new accounting standards, *IFRS 9 - Financial Instruments* and *IFRS 15 - Revenue from Contracts with Customers*, effective from 1 January 2018. These standards have been applied retrospectively, recognising the immaterial cumulative effect of initial application as an adjustment to the opening balance of retained earnings.

In order to present the performance of the Terna Group and Terna S.p.A. and to analyse the financial positions, separate reclassified statements have been prepared. These differ from the statements required by the EU-IFRS adopted and described in the consolidated and separate financial statements for the year ended 31 December 2018.

These reclassified statements contain alternative performance indicators, which differ from those resulting directly from the separate and consolidated financial statements. Management considers these indicators to be useful in assessing the performances of the Group and of Terna S.p.A. and representative of the business’s operating results and financial position. In line with the guidance provided by ESMA/2015/1415, the criteria used in constructing these indicators are described in specific notes, reconciling them with the amounts presented in the consolidated and separate financial statements. The notes are contained in an annex to this Integrated Report.

In addition, a number of comparative amounts in the income statement have been reclassified in order to improve presentation, without changing the comparative result. These amounts include those relating to the margin earned on overseas concessions, recognised in International revenue, and the classification of revenue from construction services performed under concession in Italy in Regulated Activities in Italy.

# The Terna Group

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## Scope of consolidation

The following changes in the structure of the Group have taken place with respect to 31 December 2017:

- part of the process of identifying and acting on new commercial opportunities for the provision of energy efficiency services and projects, on 15 February 2018, the acquisition of a 70% interest in **Avvenia The Energy Innovator S.r.l.** was completed;
- **Resia Interconnector S.r.l.** was established on 16 July 2018 in relation to the construction of the private Italy-Austria interconnection, for which the authorisation process regarding the Passo Resia-Glorenza cable section is in progress and is expected to be completed in 2019;
- The partial demerger of Terna Plus S.r.l. (a wholly-owned subsidiary of the parent, Terna S.p.A.), and the transfer of the demerged assets to a newly-established company named **Terna Energy Solutions S.r.l.**, became effective on 2 August 2018. The demerged business is focused on Non-regulated Activities and on the energy solutions activities already carried out by Terna Plus. Following the demerger, the latter company has assumed responsibility for the activities in South America. The demerger also resulted in the transfer, to Terna Energy Solutions, of the investments in companies that carry out Non-regulated Activities in Italy: Tamini Trasformatori S.r.l., Rete Verde 17 S.r.l., Rete Verde 18 S.r.l., Rete Verde 19 S.r.l., Rete Verde 20 S.r.l. and Avvenia The Energy Innovator S.r.l. (acquired on 15 February 2018).

## The Group's reclassified income statement

The Terna Group's operating results for the year ended 31 December 2018, compared with those for the previous year, are summarised in the following reclassified income statement, obtained by reclassifying amounts in the statutory consolidated income statement.

	(€m)			
	2018	2017	CHANGE	% CHANGE
<b>TOTAL REVENUE</b>	<b>2,197.0</b>	<b>2,162.8</b>	<b>34.2</b>	<b>1.6</b>
- Regulated revenue in Italy	1,989.6	1,967.2	22.4	1.1
<i>of which Revenue from construction services performed under concession</i>	25.5	21.1	4.4	20.9
- Non-Regulated revenue	194.9	189.1	5.8	3.1
- International revenue*	12.5	6.5	6.0	92.3
<b>TOTAL OPERATING COSTS</b>	<b>546.4</b>	<b>558.9</b>	<b>(12.5)</b>	<b>(2.2)</b>
- Personnel expenses	238.8	252.6	(13.8)	(5.5)
- Cost of services, leases and rentals	176.5	170.4	6.1	3.6
- Materials	77.9	69.4	8.5	12.2
- Other costs	22.6	34.9	(12.3)	(35.2)
- Quality of service	5.1	10.5	(5.4)	(51.4)
- Cost of construction services performed under concession	25.5	21.1	4.4	20.9
<b>GROSS OPERATING PROFIT (EBITDA)</b>	<b>1,650.6</b>	<b>1,603.9</b>	<b>46.7</b>	<b>2.9</b>
- Amortisation, depreciation and impairment losses	554.1	526.5	27.6	5.2
<b>OPERATING PROFIT (EBIT)</b>	<b>1,096.5</b>	<b>1,077.4</b>	<b>19.1</b>	<b>1.8</b>
- Net financial income/(expenses)	(88.8)	(88.8)	-	-
<b>PROFIT/(LOSS) BEFORE TAX</b>	<b>1,007.7</b>	<b>988.6</b>	<b>19.1</b>	<b>1.9</b>
- Income tax expense for the period	296.1	294.4	1.7	0.6
<b>PROFIT FOR THE YEAR</b>	<b>711.6</b>	<b>694.2</b>	<b>17.4</b>	<b>2.5</b>
Profit/(Loss) attributable to non-controlling interests	5.0	5.9	(0.9)	(15.3)
<b>PROFIT FOR THE PERIOD ATTRIBUTABLE TO OWNERS OF THE PARENT</b>	<b>706.6</b>	<b>688.3</b>	<b>18.3</b>	<b>2.7</b>

	(€m)		
EBITDA BY OPERATING SEGMENT	2018	2017	CHANGE
Regulated Activities in Italy	1,586.5	1,541.7	44.8
Non-regulated Activities	60.5	62.4	(1.9)
International Activities	3.6	(0.2)	3.8
<b>EBITDA</b>	<b>1,650.6</b>	<b>1,603.9</b>	<b>46.7</b>

**Gross operating profit (EBITDA)** for the year amounts to **€1,650.6 million**, up €46.7 million compared with the €1,603.9 million of 2017. This primarily reflects the improved result from Regulated Activities in Italy.

### Revenue

	(€m)		
REGULATED ACTIVITIES IN ITALY	2018	2017	CHANGE
<b>Tariff revenue</b>	<b>1,932.2</b>	<b>1,915.5</b>	<b>16.7</b>
Other regulated revenue	31.9	30.6	1.3
<b>Revenue from construction services performed under concession in Italy</b>	<b>25.5</b>	<b>21.1</b>	<b>4.4</b>
<b>TOTAL</b>	<b>1,989.6</b>	<b>1,967.2</b>	<b>22.4</b>

**Regulated revenue** in Italy is up €22.4 million, primarily due to ARERA's recognition of certain expenses not covered by the dispatching charge after revision of the transmission charge, reflecting the different performances of revenue from work in progress, including the impact of the revised contribution from international interconnections.

(€m)

NON-REGULATED ACTIVITIES	2018	2017	CHANGE
Tamini	103.4	92.6	10.8
Services for third parties (telecommunications, energy solutions, other)	82.5	80.5	2.0
Italy-France interconnector	9.0	16.0	(7.0)
<b>TOTAL</b>	<b>194.9</b>	<b>189.1</b>	<b>5.8</b>

The increase in **Non-Regulated revenue**, totalling €5.8 million, reflects revenue growth at the **Tamini Group**, after a reduction in revenue linked to the **private Italy-France interconnector** project (reflecting one-off proceeds booked in 2017).

(€m)

INTERNATIONAL ACTIVITIES	2018	2017	CHANGE
Latin America	10.9	4.0	6.9
Other	1.6	2.5	(0.9)
<b>TOTAL</b>	<b>12.5</b>	<b>6.5</b>	<b>6.0</b>

**International revenue** is up €6 million, reflecting revenue generated by investment in assets held under concession in **Brazil** (up €12.4 million), after the loss recognised on the contract for construction of the power line in **Uruguay** (down €5.4 million).

## Costs

**Operating costs** are down €12.5 million compared with the previous year. Without taking into account the increase in the cost of work carried out under concession, this reflects the following:

- **Personnel expenses:** down €13.8 million, primarily due to net provisions for the early retirement scheme launched in 2017 (down €19.6 million), after the significant increase in the average workforce as a result of the launch of the new initiatives envisaged in the Strategic Plan;
- **Services, leases and rentals:** up €6.1 million, primarily due to revised right-of-way fees in certain regions of Italy and external services, after the reduction in external costs on contract work;
- **Materials:** up €8.5 million, primarily due to an increase in contract work at Tamini and Avvenia;
- **Quality of service:** down €5.4 million, primarily due to the higher costs incurred in 2017 in relation to certain major events in central and southern Italy, with respect to outages in 2018 essentially due to events in northern Italy in October;
- **Other operating costs:** down €12.3 million, broadly due to the adjustment to the Group's provisions for risks and charges.

**Amortisation, depreciation and impairment losses** for the year amount to €554.1 million, up €27.6 million compared with 2017, primarily due to the entry into service of new plant.

Operating profit (**EBIT**), after amortisation, depreciation and impairment losses, amounts to **€1,096.5 million**, compared with €1,077.4 million for 2017 (up 1.8%).

**Net financial expenses** for the year total €88.8 million, primarily attributable to the Parent Company (€84.0 million), and are in line with the previous year.

After net financial expenses, **profit before tax** amounts to **€1,007.7 million**, up €19.1 million compared with the previous year (up 1.9%).

**Income tax expense for the year** totals €296.1 million, an increase of €1.7 million (0.6%) compared with the previous year, essentially due to the improved profit before tax. The tax rate for the year is 29.4%, broadly in line with the 29.8% of 2017.

**Profit for the year** amounts to **€711.6 million**, an increase of €17.4 million (2.5%) compared with the €694.2 million of 2017.

**Profit for the year attributable to owners of the Parent** (after excluding the share attributable to non-controlling interests) amounts to **€706.6 million**, up €18.3 million (2.7%) compared with the €688.3 million of 2017.

## Cash flow

The above performance, combined with non-cash items and other cash flows from and for operating activities, has resulted in a cash inflow of €1,474.5 million, enabling the Group to finance a large part of its investing activities (€1,091.1 million) and provide a return on equity (€486.4 million, including €451.1 million in the form of dividends paid to shareholders). The balance is financed by net debt, which totals €7,899.4 million, compared with €7,796.4 million at the end of 2017 (up €103 million).

	(€m)	
	CASH FLOW 2018	CASH FLOW 2017
- Profit for the year	711.6	694.2
- Amortisation, depreciation and impairment losses	554.1	526.5
- Net change in provisions	(48.3)	(28.8)
- Net losses/(gains) on sale of assets	(3.5)	(2.1)
<b>Operating cash flow</b>	<b>1,213.9</b>	<b>1,189.8</b>
- Change in net working capital	336.6	408.3
- Other changes in property, plant and equipment and intangible assets	36.0	137.5
- Change in investments	1.7	(2.7)
- Change in financial assets	(113.7)	(98.7)
<b>Cash flow from operating activities</b>	<b>1,474.5</b>	<b>1,634.2</b>
- Total capital expenditure	(1,091.1)	(1,033.9)
<b>Free cash flow</b>	<b>383.4</b>	<b>600.3</b>
- Dividends paid to the Parent Company's shareholders	(451.1)	(418.4)
- Cash flow hedge reserve after taxation and other movements in equity attributable to owners of the Parent	(39.6)	(2.0)
- Other movements in equity attributable to non-controlling interests	4.3	-
<b>Change in net debt</b>	<b>(103.0)</b>	<b>179.9</b>

## The Group's reclassified statement of financial position

The Terna Group's financial position at 31 December 2018 and 31 December 2017 is summarised below in the reclassified statement of financial position, obtained by reclassifying amounts in the statutory consolidated statement of financial position.

	(€m)		
	AT 31 DECEMBER 2018	AT 31 DECEMBER 2017	CHANGE
<b>Total net non-current assets</b>	<b>14,083.6</b>	<b>13,466.4</b>	<b>617.2</b>
- Intangible assets and goodwill	519.4	505.7	13.7
- Property, plant and equipment	13,244.3	12,752.8	491.5
- Financial assets	319.9	207.9	112.0
<b>Total net working capital</b>	<b>(1,822.5)</b>	<b>(1,485.2)</b>	<b>(337.3)</b>
- Net energy-related pass-through payables	(777.6)	(852.7)	75.1
- Net receivables resulting from Regulated Activities	313.9	335.1	(21.2)
- Net trade payables	(860.7)	(714.4)	(146.3)
- Net tax assets	50.9	105.9	(55.0)
- Other net liabilities	(549.0)	(359.1)	(189.9)
<b>Gross invested capital</b>	<b>12,261.1</b>	<b>11,981.2</b>	<b>279.9</b>
Sundry provisions	(307.5)	(355.8)	48.3
<b>NET INVESTED CAPITAL</b>	<b>11,953.6</b>	<b>11,625.4</b>	<b>328.2</b>
<b>Equity attributable to owners of the Parent</b>	<b>4,019.2</b>	<b>3,803.3</b>	<b>215.9</b>
<b>Equity attributable to non-controlling interests</b>	<b>35.0</b>	<b>25.7</b>	<b>9.3</b>
<b>Net debt</b>	<b>7,899.4</b>	<b>7,796.4</b>	<b>103.0</b>
<b>TOTAL</b>	<b>11,953.6</b>	<b>11,625.4</b>	<b>328.2</b>

The €617.2 million increase in **net non-current assets** compared with 31 December 2017 primarily reflects a combination of the following:

- an increase of €112.0 million in financial assets, mainly due to construction services performed under concession in Brazil during the period (up €94.3 million) and an increase in the Interconnector Guarantee Fund, set up to fund investment in interconnections by art. 32 of Law 99/09 (up €18.9 million);
- total capital expenditure of €1,091.1 million, as described below;
- amortisation and depreciation for the year, totalling €540.0 million;
- other movements during the year, resulting in a reduction of €41.3 million, including grants related to assets (primarily in relation to projects financed by the Ministry for Economic Development and the EU and to the re-routing of power lines at the request of third parties); disposals and impairment losses, resulting in a reduction of €22.6 million.

The change during the period also reflects the contribution from the acquisition of Avvenia the Energy Innovator S.r.l. (€17.6 million, primarily reflecting the company's order book).

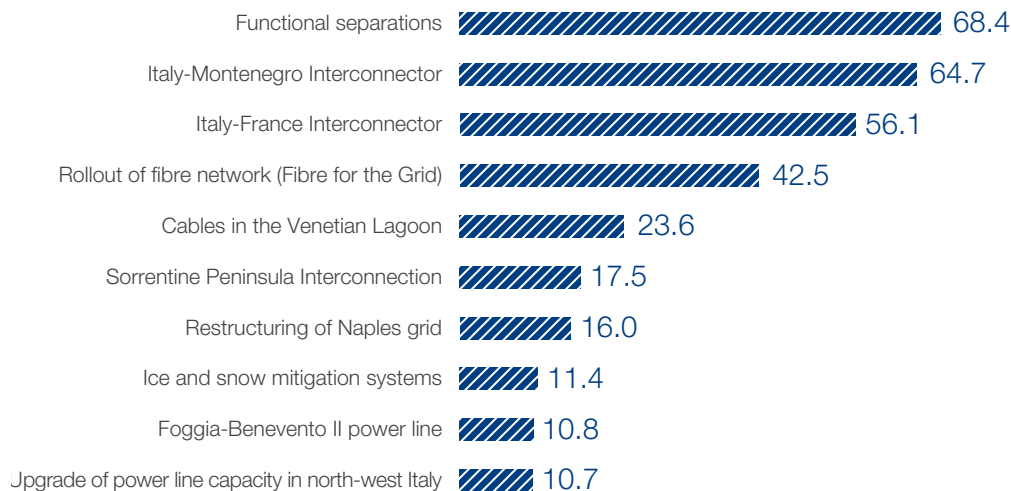
The Group's **capital expenditure** totalled **€1,091.1 million** in 2018, up **5.5%** on the €1,033.9 million of 2017. Of this amount, investment incentives amounted to **€99.5 million**, compared with €122.8 million in 2017.

Investment in non-regulated assets, amounting to €87.4 million, primarily regards the private part of the Italy-France interconnector.



The following chart shows key capital expenditure on the NTG RTN in 2018:

**KEY CAPITAL EXPENDITURE\*** (€m)



\* Amounts include financial expenses.

**A total of 159 km of power lines** entered service in 2018 (Bono-Buddusò, Villanova-Cepagatti, Benevento II-Benevento III, Messina-Riviera-Villafranca, Ciminna-Casuzze, Sacca Fisola-Fusina and the connections between the San Salvo, the Main Naples and the Naples Levante substations), alongside the San Severo, Quartu-Quartucciu, Santa Teresa, San Salvo, Portella Pero, Siculiana, Ravenna Industrial Park and Canino substations.

**Net working capital (net current liabilities)** of €1,822.5 million generated cash of €337.3 million during the year compared with 2017. This reflects the combined effect of:

*Cash inflows*

- an increase of €146.3 million in **net trade payables**, largely due to the increase in capital expenditure towards the end of the year;
- a reduction of €21.2 million in **net energy-related pass-through receivables**, primarily reflecting payment by the Fund for Energy and Environmental Services (*Cassa per i Servizi Energetici e Ambientali-CSEA*) of the RENS bonus for the quality of service provided in 2016 (€25.6 million);
- an increase of €189.9 million in **other net liabilities**, primarily due to increases in payments on account received from the entities financing the Italy-France Interconnector (up €106.1 million), in the provision for the Interconnector Guarantee Fund set up by Terna S.p.A. following the issue of the 2016 Stability Law (up €21.9 million) and in government grants received during the year (€61.6 million, primarily from the Ministry for Economic Development).

## Cash outflows

- an increase in **net energy-related pass-through payables** of €75.1 million, primarily reflecting the combined effect of:
  - a reduction in net payables resulting from transactions on the Dispatching Services Market (€24.4 million) and from imbalances (€99.7 million); these changes in DSM and imbalance costs are reflected in the amount receivable for procuring resources on the Dispatching Services Market (the uplift), which is down €68.9 million compared with the end of 2017;
  - a reduction in net payables linked to plants that are essential for the security of the electricity system - *UESS* (€127.2 million), reflecting increased payments approved by ARERA compared with the previous year;
  - an increase in amounts due from the Fund for Energy and Environmental Services (*Cassa per i Servizi Energetici e Ambientali* - CSEA) linked to the interruptibility service (€10.6 million);
  - an increase in payables relating to capacity payments (€125.4 million), resulting from items collected after payments made in 2018;
- a reduction in **net tax assets** of €55 million, primarily reflecting a decrease in the Group's refundable VAT (down €32.7 million), due to higher payments on account in the previous year as a result of the Ministerial Decree of 27 June 2017, after refundable VAT accruing on the increased volume of purchases made by subsidiaries towards the end of the year. The change also reflects a reduction in net income tax assets (down €22.7 million), essentially due to higher payments on account made in the previous year (determined on the basis of a higher rate of IRES applied in 2016) and an increase in tax payable for the period (essentially due to the increase in pre-tax profit).

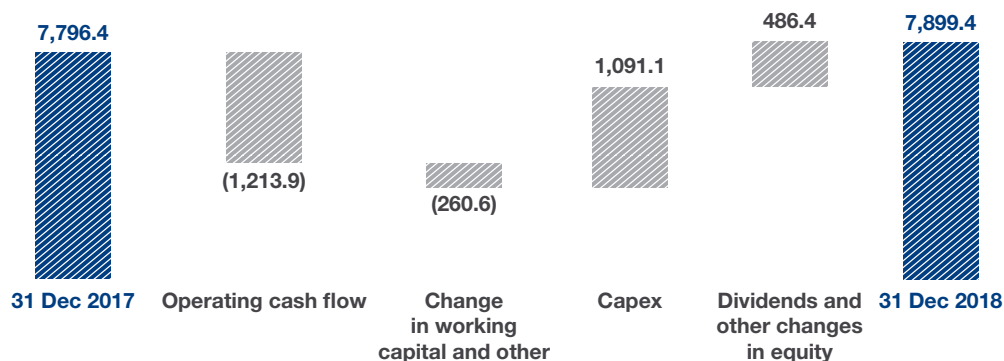
**Gross invested capital** thus amounts to €12,261.1 million, marking an increase of €279.9 million compared with the end of the previous year.

**Sundry provisions** are down €48.3 million, primarily due to:

- the adjustment to provisions for employee benefits (down €11.3 million), with particular regard to agreements relating to the energy discounts granted to pensioners), uses during the year in relation to the existing plan for generational turnover (down €9.6 million), the higher value of provisions made in the previous year for urban and environmental redevelopment schemes (down €7.3 million), favourable outcomes to a number of disputes arising in previous years (down €4.9 million) and the payment, by ARERA, of expenses not covered by the transmission and dispatching charges (down €6.6 million);
- provisions for net deferred tax liabilities (down €11.9 million), primarily due to the effect on taxation of amortisation and depreciation and uses of provisions for risks and charges.

**Net invested capital** of €11,953.6 million is up €328.2 million compared with 31 December 2017 and is financed by equity attributable to owners of the Parent, totalling €4,019.2 million (compared with €3,803.3 million at 31 December 2017), equity attributable to non-controlling interests of €35 million (€25.7 million at 31 December 2017) and net debt of €7,899.4 million (up €103 million compared with the €7,796.4 million of 31 December 2017).

### CHANGE IN NET DEBT (€m)

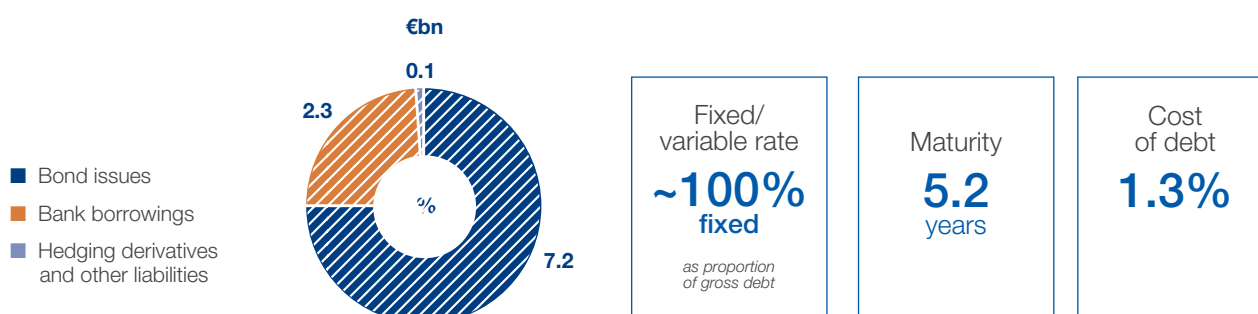


## Debt

### The Group's financial policy and gross debt

The key aspects of the Group's financial policy are diversification of the sources of funding, a balance between short- and medium/long-term forms of debt and the proactive management of debt.

**Gross debt** at 31 December 2018 amounts to approximately **€9.6 billion**, consisting of €7.2 billion in the form of bond issues and €2.3 billion in bank borrowings. The average term to maturity of debt, which is almost all fixed rate, is approximately 5.2 years.



Bonds have been issued in the form of both public and private placements under the €8 billion Euro Medium Term Notes (EMTN) Programme (in which a large number of Italian and overseas banks participate), in addition to a stand-alone issue of €800 million dating back to 2004. Focused specifically on qualified investors and listed on the Luxembourg Stock Exchange, Terna's bonds have a very diverse investor base, in terms of both sector and geographical profile.

The main provider of Terna's bank loans is the European Investment Bank (EIB). Total borrowings from the EIB at 31 December 2018 amount to almost €2.2 billion (including €46 million yet to be drawn on). Thanks to its strong credit ratings, Terna is able to obtain financing from banks on extremely good terms, as shown by the refinancing of the Revolving Credit Facility expiring in 2019 with a new revolving facility of €900 million, obtained in September and increased by a further €250 million in November. The Group currently has three committed, revolving credit facilities, amounting to €2.5 billion.

## Net debt

The Group's net debt at 31 December 2018 amounts to €7,899.4 million, an increase of €103 million compared with 31 December 2017.

	(€m)		
NET DEBT (BY TERM TO MATURITY)	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
<b>Total medium/long-term debt</b>	<b>8,286.8</b>	<b>8,677.8</b>	<b>(391.0)</b>
- Bond issues	6,563.2	6,541.9	21.3
- Borrowings*	1,664.4	2,125.4	(461.0)
- Derivative financial instruments	59.2	10.5	48.7
<b>Total short-term debt/ (funds)</b>	<b>(387.4)</b>	<b>(881.4)</b>	<b>494.0</b>
- Bond issues (current portions)	616.7	749.9	(133.2)
- Short-term borrowings	25.0	118.0	(93.0)
- Borrowings (current portions)	616.7	134.4	479.5
- Other current financial liabilities, net	89.8	105.5	(15.7)
- Financial assets	(403.9)	-	(403.9)
- Cash and cash equivalents	(1,328.9)	(1,989.2)	660.3
<b>Total net debt</b>	<b>7,899.4</b>	<b>7,796.4</b>	<b>103.0</b>
<b>NET DEBT (BY TYPE OF INSTRUMENT)</b>			
- Bond issues	7,179.9	7,291.8	(111.9)
- Borrowings*	2,278.3	2,259.8	18.5
- Short-term borrowings	25.0	118.0	(93.0)
- Derivative financial instruments	59.2	10.5	48.7
- Other financial liabilities	89.8	105.5	(15.7)
<b>GROSS DEBT</b>	<b>9,632.2</b>	<b>9,785.6</b>	<b>(153.4)</b>
- Financial assets	(403.9)	-	(403.9)
- Cash and cash equivalents	(1,328.9)	(1,989.2)	660.3
<b>Total net debt</b>	<b>7,899.4</b>	<b>7,796.4</b>	<b>103.0</b>

\* This item includes fees on credit facilities.

Changes in the **Group's net debt** are as follows:

- reduction in bond issues (down €111.9 million), resulting from repayment, in February, of bonds issued in 2012, totalling €750.0 million, the green bond issue of 23 July 2018 (€750 million) and the adjustment to these instruments to reflect their amortised cost;
- an increase in borrowings (up €18.5 million), primarily due to new borrowings €154.2 million, after repayments during the period (down €134.5 million);
- a decrease in short-term borrowings and other financial liabilities (down €108.7 million), primarily due to the Parent Company's repayment of short-term credit facilities and the settlement of interest on borrowings and the related hedges;
- an increase in derivative financial instruments (up €48.7 million), primarily due to the movement in market interest rates and the change in the notional value of the derivatives portfolio;
- an increase in financial assets (up €403.9 million) following the purchase of government securities maturing in December 2019 and having a notional value of €400 million;
- a reduction in cash and cash equivalents (€660.3 million). Cash amounts to €1,328.9 million at 31 December 2018, including €751.5 million invested in short-term, readily convertible deposits and €577.2 million deposited in bank current accounts.

## Reconciliation of the Group's profit for the year and equity with the corresponding amounts for the Parent Company

The reconciliation of consolidated equity and consolidated profit for the year and the corresponding amounts for the Parent Company is shown below.

(€m)

	PROFIT FOR FY 2018	EQUITY AT 31 DECEMBER 2018
<b>Parent Company's financial statements</b>	<b>661.3</b>	<b>3,850.9</b>
Profit and equity contributed by Group companies:		
- Group companies - Regulated Activities	62.4	116.4
- Group companies - Non-Regulated Activities	(9.5)	70.5
- Group companies - International Activities	(4.1)	(15.3)
Companies accounted for using the equity method	1.5	31.7
<b>Total consolidated financial statements</b>	<b>711.6</b>	<b>4,054.2</b>
Share attributable to non-controlling interests - Non-Regulated Activities	5.0	35.0
<b>Terna Group's consolidated financial statements</b>	<b>706.6</b>	<b>4,019.2</b>



# Terna's shares

**+191%**  
the capital gain  
since the date  
of the IPO

## Terna and the financial markets

Terna S.p.A. has been listed on Borsa Italiana's screen-based trading system (*Mercato Telematico Azionario*) since 23 June 2004. **From the date of floatation to the end of 2018, the share price has risen 191% (a capital gain)**, providing a Total Shareholder Return (TSR<sup>23</sup>) of 559%, ahead of both the Italian market (FTSE Mib +28%) and the relevant European sector index (DJ Stoxx Utilities), which is up 154%.

Europe's leading stock markets recorded negative performances in 2018, held back by fears of a global economic slowdown. Milan lost 16.1% over the year, with Frankfurt and Paris losing 20.6% and 11%, respectively, and London down 12.5% and Madrid off 15%.

## Performance of Terna's shares

Terna's shares, in contrast, ended 2018 in positive territory after an annual increase of 2.25% to €4.953 per share, outperforming the Company's principal peers and the relevant sector index for Europe (the DJ Stoxx Utilities was down 2.1%). The average daily volume traded during the year amounted to approximately 6.6 million shares per day. The ex-dividend date for the interim dividend for 2018, amounting to 7.87 euro cents per share, was 19 November.

### KEY INDICATORS PER SHARE

	2018	2017	2016	2015	2014	2013
Number of shares (in millions)	2,010	2,010	2,010	2,010	2,010	2,010
Price at year end (€ per share)	4.95	4.84	4.35	4.76	3.76	3.63
Market capitalisation* (€m)	9.507	9.668	9.367	8.482	7.718	6.713
Average price for year (€ per share)	4.73	4.81	4.66	4.22	3.84	3.34
Earnings per share (€)	0.352	0.339	0.315	0.296	0.271	0.256
Dividend per share (€)	0.233	0.220	0.206	0.200	0.200	0.200
Payout ratio	70.88%	66.63%	77.32%	76.30%	89.30%	88.40%
Dividend yield**	4.7%	4.5%	4.7%	4.2%	5.3%	5.5%
Total shareholder return	7.3%	15.90%	-4.3%	32.5%	8.9%	27.6%

\* Based on the average price for the year.

\*\* Dividend per share for the year as a percentage of the share price at year end.

WEIGHTING OF TERNA'S SHARES	2018	2017
> on the FTSE MIB	2.42%	1.94%

Source: Borsa Italiana.

<sup>23</sup> Total Shareholder Return (TSR): total return on an equity investment, calculated as the sum of:

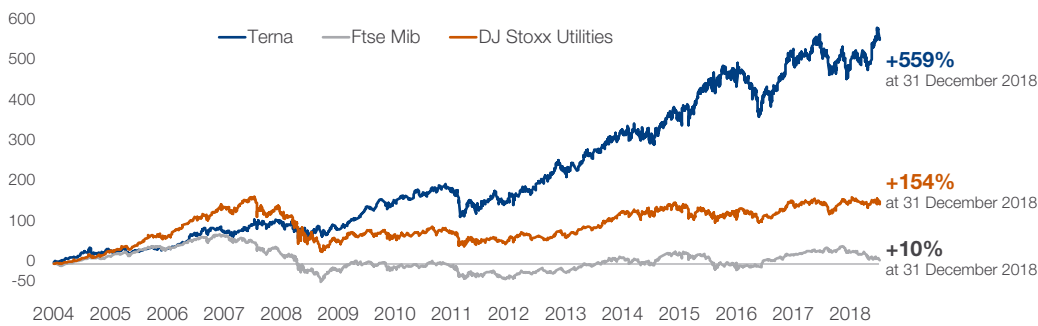
- I. the capital gain: the change in the share price (difference between the price at the end and at the beginning of the relevant period) as a percentage of the price at the beginning of the period;
- II. reinvested dividends: the ratio between dividends per share paid out during the period and the share price at the beginning of the period. Dividends are assumed to have been reinvested in the shares.

**PERFORMANCE OF TERNA'S SHARES - Price (2018)**



Source: Bloomberg

**PERFORMANCE OF TERNA'S SHARES – Total Shareholder Return** (from their floatation to the end of 2018) (%)



Source: Bloomberg

**Inclusion in stock exchange sustainability indices**

Terna's commitment to measuring and improving its ESG (Environmental, Social and Governance) performance is reflected positively in the sustainability ratings.

Terna's inclusion in all the leading international stock exchange sustainability indices was confirmed in 2018. In September, on the occasion of the annual review conducted by the Swiss sustainability rating agency, RobecoSAM, Terna's presence in the Dow Jones Sustainability Index (World and Europe) was confirmed, and the Company was named **Industry Leader in the Electric Utilities sector**.

INDEX	TERNA
BLOOMBERG GENDER EQUALITY INDEX	Included since January 2019
DOW JONES SUSTAINABILITY INDEX	Included since 2009
ECPI	Included since 2007
ETHIBEL SUSTAINABILITY INDEX (ESI)	Included since 2009
EURONEXT VIGEO	Included in the World 120, Eurozone 120 and Europe 120 baskets since 2012
FTSE ECPI	Included since 2010
FTSE4Good	Included in the index (Global and Europe baskets) every year since 2005
MSCI GLOBAL SUSTAINABILITY	Included regularly in the index since 2007
STOXX® ESG	Included in the index since 2011
STOXX® LOW CARBON	Included in the index since February 2016, the date the index was launched
UNITED NATIONS GLOBAL COMPACT ("GC100")	Included in the index since 2013

In recognition of its ranking as "Industry Leader", Terna was included in the Gold Class in RobecoSAM's "Sustainability Yearbook 2019", published in January 2019.



# Terna S.p.A.

A review of the operating performance and financial position of the Parent Company, Terna S.p.A., is provided below.

## Terna S.p.A.'s reclassified income statement

Terna S.p.A.'s operating results for the years 2018 and 2017 are summarised in the following reclassified income statement, obtained by reclassifying amounts in the statutory income statement.

	2018	2017	CHANGE
<b>TOTAL REVENUE</b>	<b>1,967.6</b>	<b>1,951.5</b>	<b>16.1</b>
- Tariff revenue	1,800.6	1,786.4	14.2
<i>of which transmission revenue</i>	1,657.5	1,674.5	(17.0)
<i>of which dispatching, metering and other revenue</i>	143.1	111.9	31.2
- Other operating income	141.5	144.0	(2.5)
- Revenue from construction services performed under concession*	25.5	21.1	4.4
<b>TOTAL OPERATING COSTS</b>	<b>452.0</b>	<b>464.9</b>	<b>(12.9)</b>
- Personnel expenses	63.6	65.7	(2.1)
- Cost of services, leases and rentals	343.8	332.1	11.7
- Materials	0.9	7.0	(6.1)
- Other costs	13.1	28.5	(15.4)
- Quality of service	5.1	10.5	(5.4)
- Cost of construction services performed under concession*	25.5	21.1	4.4
<b>GROSS OPERATING PROFIT (EBITDA)</b>	<b>1,515.6</b>	<b>1,486.6</b>	<b>29.0</b>
- Amortisation, depreciation and impairment losses	517.9	495.2	22.7
<b>OPERATING PROFIT/(LOSS) (EBIT)</b>	<b>997.7</b>	<b>991.4</b>	<b>6.3</b>
- Net financial income/(expenses)	(78.5)	(89.8)	11.3
<b>PROFIT/(LOSS) BEFORE TAX</b>	<b>919.2</b>	<b>901.6</b>	<b>17.6</b>
- Income tax expense	257.9	261.6	(3.7)
<b>PROFIT FOR THE YEAR</b>	<b>661.3</b>	<b>640.0</b>	<b>21.3</b>

**Gross operating profit (EBITDA)** for 2018 amounts to €1,515.6 million, an increase of €29.0 million compared with the previous year. This primarily reflects the overall increase in tariff revenue and a reduction in costs as a result of the favourable outcomes to a number of disputes arising in previous years.



The increase in **revenue** (equal to €16.1 million) primarily reflects growth in dispatching, metering and other revenue (up €31.2 million), above all due to the recognition of certain expenses<sup>24</sup> not covered by the dispatching charge. This was partially offset by the reduction in the transmission charge (down €17.0 million), following a revision of the related tariff to reflect completion, in 2017, of revenue from work in progress and a reduction in the volume of energy transported, offset by an increase in the portion of the NTG owned by Terna. The balance also includes the estimated impact of the revised contribution from international interconnections.

**Operating costs** are down €12.9 million, primarily due to reductions in other operating costs (down €15.4 million), broadly reflecting the favourable outcomes to a number of disputes arising in previous years, in the cost of materials (down €6.1 million, mainly in relation to the telecommunications business) and in costs incurred for the quality of service (down €5.4 million). These reductions were partially offset by increases in service costs and lease expense (up €11.7 million), primarily relating to intercompany services rendered under specific intercompany contracts and revised right-of-way fees in certain regions of Italy.

**Amortisation, depreciation and impairment losses** for the year amount to €517.9 million, up €22.7 million compared with 2017, primarily due to the entry into service of new plant.

Operating profit (**EBIT**) thus amounts to €997.7 million, up €6.3 million on the figure for 2017.

**Net financial expenses** for the year total €78.5 million, a reduction of €11.3 million compared with the €89.8 million of 2017. This primarily reflects an increase in interest income due to an increase in liquidity invested during the year and the improved return on that liquidity, as well as an increase in capitalised financial expenses linked to an increase in the Company's capital expenditure during the year.

**Income tax expense** for the year amounts to €257.9 million, a reduction of €3.7 million compared with the previous year, essentially due to non-recurring items.

**Profit for the year** thus amounts to €661.3 million, up €21.3 million on the profit for 2017.

<sup>24</sup> The regulator, ARERA has decided to allow the recovery of expenses through the uplift mechanism provided for in art.44 of Resolution 111/2006. These expenses regard receivables that are no longer recoverable and relating to the period 2006-2015 (ref. Resolution 218/2018) and increased payments made to fund the regulator for the years 2013-2017.

## Cash flow

Cash flows in 2018 and pro forma 2017<sup>25</sup> are shown below.

The above performance, combined with non-cash items and other cash flows from and for operating activities, has resulted in a cash inflow of €1,316.5 million, enabling the Parent Company to finance a large part of its investing activities (€886.1 million) and provide a return on equity (€485.7 million, including €451.1 million in the form of dividends paid to shareholders). The balance is financed by net debt, which totals €8,101.8 million, compared with €8,046.5 million at the end of 2017 (up €55.3 million).

	(€m)	
	CASH FLOW FY 2018	CASH FLOW FY 2017 PRO FORMA
- Profit for the year	661.3	640.0
- Amortisation, depreciation and impairment losses	517.9	495.2
- Net change in provisions	(66.1)	(18.5)
- Net losses/(gains) on sale of assets	(3.0)	(1.7)
<b>Operating cash flow</b>	<b>1.110.1</b>	<b>1.115.0</b>
- Change in net working capital	243.0	287.3
- Change in investments	(55.7)	(30.0)
- Other movements in property, plant and equipment and intangible assets	38.7	120.1
- Change in financial assets	(19.6)	(24.8)
<b>Cash flow from operating activities</b>	<b>1.316.5</b>	<b>1.467.6</b>
- Total capital expenditure	(886.1)	(851.9)
<b>Free cash flow</b>	<b>430.4</b>	<b>615.7</b>
- Dividends paid to shareholders	(451.1)	(418.4)
- Cash flow hedge reserve after taxation and other movements in equity	(34.6)	5.9
<b>Change in net debt</b>	<b>(55.3)</b>	<b>203.2</b>

<sup>25</sup> The comparative "2017 pro forma" column, previously published last year, takes into account the impact of the merger with and into Terna S.p.A. of the wholly owned subsidiaries of Terna Storage S.r.l. and Terna Rete Italia S.r.l. in the previous year. The merger was effective for accounting and tax purposes from 1 January 2017.

## Terna S.p.A.'s reclassified statement of financial position

Terna S.p.A.'s financial position at 31 December 2018 and 2017 is summarised in the following statement, obtained by reclassifying amounts in the statutory statement of financial position.

	(€m)		
	AT 31 DECEMBER 2018	AT 31 DECEMBER 2017	CHANGE
<b>Total net non-current assets</b>	<b>13,548.1</b>	<b>13,139.6</b>	<b>408.5</b>
- Intangible assets and goodwill	427.7	424.3	3.4
- Property, plant and equipment	12,035.0	11,705.2	329.8
- Financial assets	1,085.4	1,010.1	75.3
<b>Total net current liabilities</b>	<b>(1,388.0)</b>	<b>(1,144.3)</b>	<b>(243.7)</b>
- Net energy-related pass-through payables	(799.7)	(874.4)	74.7
- Net receivables resulting from regulated activities	313.9	335.1	(21.2)
- Net trade payables	(537.6)	(424.5)	(113.1)
- Net tax assets	(14.2)	106.8	(121.0)
- Other liabilities, net	(350.4)	(287.3)	(63.1)
<b>Gross invested capital</b>	<b>12,160.1</b>	<b>11,995.3</b>	<b>164.8</b>
Sundry provisions	(207.4)	(273.5)	66.1
<b>NET INVESTED CAPITAL</b>	<b>11,952.7</b>	<b>11,721.8</b>	<b>230.9</b>
<b>Equity</b>	<b>3,850.9</b>	<b>3,675.3</b>	<b>175.6</b>
<b>Net debt</b>	<b>8,101.8</b>	<b>8,046.5</b>	<b>55.3</b>
<b>TOTAL</b>	<b>11,952.7</b>	<b>11,721.8</b>	<b>230.9</b>

The principal changes with respect to 31 December 2017 are described below.

**Net invested capital** amounts to €11,952.7 million at 31 December 2018, an increase of €230.9 million compared with the previous year. This reflects an increase in **net non-current assets** (€408.5 million), the cash generated by **net working capital** (down €243.7 million) and a reduction in sundry provisions (€66.1 million).

The change in **net working capital**, represented by a reduction of €243.7 million, is primarily due to an increase in amounts payable to the subsidiary, Terna Rete Italia S.p.A., as a result of the greater volume of capital expenditure carried out towards the end of the year, compared with the same period of 2017, an increase in VAT and income tax payable and an increase in prepayments from third parties (primarily the Ministry for Economic Development) and from the Interconnector Guarantee Fund.

**Net non-current assets** are up €408.5 million, primarily due to capital expenditure during the year (€886.1 million), after grants deducted directly from the carrying amount of the related assets (€40.5 million, primarily in relation to projects financed by the Ministry for Economic Development), amortisation and depreciation for the year (€503.8 million) and disposals and impairment losses (€15.2 million). The change also reflects the subscription for newly issued shares in the subsidiary, Terna Crna Gora d.o.o. (€59.0 million) and the Interconnector Guarantee Fund, set up by art. 32 of Law 99/09 to fund investment in interconnections (up €18.9 million).

**Sundry provisions** are down €66.1 million, primarily due to provisions for net deferred tax liabilities (down €35.5 million), mainly due to the effect on taxation of amortisation and depreciation and movements in provisions for risks and charges, uses during the year in relation to the existing plan for generational turnover (down €9.6 million), the higher value of provisions made in the previous year for urban and environmental redevelopment schemes (down €7.3 million), favourable outcomes to a number of disputes arising in previous years (down €5.1 million) and the payment, by ARERA, of expenses not covered by the transmission and dispatching charges (down €6.6 million).

**Net debt** of €8,101.8 million is up €55.3 million.

	(€m)		
NET DEBT (BY TYPE OF INSTRUMENT)	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
- Bond issues	7,179.9	7,291.8	(111.9)
- Borrowings*	2,221.8	2,227.5	(5.7)
- Short-term borrowings and other financial liabilities	89.5	195.5	(106.0)
- Derivative financial instruments	59.1	9.9	49.2
<b>Gross debt</b>	<b>9,550.3</b>	<b>9,724.7</b>	<b>(174.4)</b>
- Long- and short-term loans to subsidiaries	(99.5)	-	(99.5)
- Financial assets	(403.9)	-	(403.9)
- Cash and cash equivalents (including the net balance on intercompany current accounts)	(945.1)	(1,678.2)	733.1
<b>Total net debt</b>	<b>8,101.8</b>	<b>8,046.5</b>	<b>55.3</b>

\* This item includes fees on credit facilities.

In addition to the information provided above, the increase in net debt also reflects the loans granted in 2018 to the Latin American subsidiaries (up e€99.5 million).

# Proposal

for the Annual General Meeting regarding the distribution of Terna S.p.A.'s profit for the year

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## Proposal for appropriation of profit for the year

Terna S.p.A.'s Board of Directors proposes to pay a total dividend of €468,730,134.40 for 2018, equal to €0.2332 per share, of which €0.0787 per share was declared in the form of an interim dividend on 9 November 2018.

The Board of Directors thus proposes to appropriate Terna S.p.A.'s profit for 2018, amounting to €661,291,201.83, as follows:

- €158,186,370.40 to cover payment of the interim dividend payable from 21 November 2018;
- €310,543,764.00 to pay a final dividend of €0.1545 to the holders of each of the 2,009,992,000 ordinary shares outstanding at the date of this Board of Directors' meeting. The final dividend will be payable on 26 June 2019, with an ex-dividend date for coupon 30 of 24 June 2019 and a record date (as defined by art.83-terdecies of Legislative Decree 58 of 24 February 1998, the Consolidated Law on Finance of 25 June 2019);
- €192,561,067.43 to be taken to retained earnings.