

Ørsted A/S

Transcript :: Q1 2018 results :: 26 April 2018

Welcome to this call for Ørsted Q1 2018 results call. I will now hand over the word to CEO Henrik Poulsen. Please go ahead.

0.00.09

Henrik Poulsen

Thank you and good morning everyone. Welcome to this Q1 presentation. I am here with our group CFO, Marianne Wiinholt.

Let's dive straight into it and turn page 3 in the presentation. 2018 is off to a very satisfactory start. Our strong operational and financial performance continued in this first quarter and we reached a number of important business development milestones.

We reached an EBITDA of DKK 5.5 billion, which is up 68% on the first quarter last year. The results were mainly driven by higher generation from our offshore wind farms in operation and also higher income from partnerships. In bioenergy and thermal power, we improved the spreads and higher heat generation as well as the bioconversion of Skærbæk Power Station which was inaugurated late last year. All contributed to the positive development. Along with a positive arbitration outcome regarding the renegotiation of a gas purchase contract in Distribution & Customer Solutions.

On the back of this arbitration outcome and the strong operational start to the year, we have increased our EBITDA guidance for 2018 by DKK 0.5 billion compared to the guidance in the Annual Report for 2017. EBITDA excluding new partnership agreements is now expected to amount to between DKK 12.5 and 13.5 billion.

Following the bioconversion of the Skærbæk Power Station and the continued ramp-up of our offshore wind capacity, the green share of our heat and power generation increased substantially from 56% in Q1 2017 to 68% in Q1 2018.

In April, we participated in the second transitional auction in Germany and we expect to receive the results within the next few days or next few weeks.

We also submitted a bid in the auction in Connecticut competing for roughly 200MW. We expect to receive the results from this auction later in the second quarter this year.

In late March, we submitted a bid for capacity in the first Taiwanese grid allocation. We expect to get the result of the 3.5GW grid allocation by the end of April, in other words within the next few days.

In Taiwan, we have also just taken a final investment decision on phase 2 of the Formosa 1 project where we expect to start constructing the 120MW offshore wind farm next year. This will further build on our local capability in Taiwan.

As we have previously communicated, we have seen leading edge erosion to varying degrees on the blades of the 3.6MW Siemens wind turbines. We are currently planning the individual repair and upgrade campaigns together with SiemensGamesa and specific agreements have been made for the Danish Anholt asset and for the UK London Array wind farm. These agreements build on earlier agreed guiding principles on a portfolio basis. Further agreements, which we expect to follow similar principles, are expected in the month to come. SiemensGamesa has commenced work at Anholt and during the campaign, SiemensGamesa will dismantle the blades, apply a protective shell and also install an aerodynamic improvement kit to increase the yield. Because of the increased production and partly as a result of warranty claims, the repairs will expectedly have little to no impact on our financials.

Lastly, we took another step in developing our storage business by entering into an agreement to buy the project rights for a 20MW storage project near Liverpool in the UK. We will build and operate the battery and expect it to be in operation by the end of this year. The storage solution will be used to provide services to the UK's national grid to help manage grid stability during changes between peak power demand and low power demand. Furthermore, the 2MW battery solution at the Burbo Bank offshore wind farm is also progressing according to plan. We expect it to be operational within the next few weeks. It will be the first time an offshore wind farm is integrated with a battery system to deliver frequency response to the grid.

On slides 4 and 5, I will provide an update on the market development and offshore wind opportunities across the US, Taiwan and Europe.

In February, we obtained approval from the Taiwanese Environmental Protection Administration for the EIAs for our four Greater Changhua projects with a total capacity of 2.4GW. With these approvals, we have secured exclusivity over the development of these sites. In late March, we submitted a bid for capacity in the Taiwanese grid allocation and the government, as I mentioned, will allocate a total of 5.5GW grid capacity for the period until 2025. The result of the 3.5GW grid allocation is expected within the next week and the outcome of the ensuing 2.0GW price-based auction could be announced as early as June.

In the US, offshore wind continues to build momentum along the East Coast. As you know, we submitted a bid at the first large-scale offshore wind auction in Massachusetts in December last year. The selection of the preferred bidder or bidders in the Massachusetts Auction originally scheduled for April 23 has been delayed by a month and we now expect an announcement on May 23.

The US government has also proposed a competitive price auction for two additional commercial wind lease areas in federally owned waters south of Massachusetts asking potential bidders to express their interest or reaffirm their interest within the next month.

In the state of New York, the expectation is that a competitive offshore wind auction will take place towards the end of this year or beginning of next year. In addition, the US government has requested investors to submit expressions of interest for commercial offshore wind energy development opportunities in four so-called "call areas" facing Long Island. Lease auctions could expectedly take place late next year.

Building on the momentum in the US, we have decided to open an office in Atlantic City, New Jersey during the month of May. The expectation is that New Jersey will have its first solicitation late this year or early next year.

In an address yesterday, marking his first 100 days in office, New Jersey governor Murphy emphasised the state's offshore wind ambitions and by the way also mentioned Ørsted's decision to set up office in Atlantic City.

As I mentioned in the beginning of the call, we submitted a bid in the 200MW auction in Connecticut and expect to receive the results later during this second quarter.

Rhode Island has established a target of 1GW renewable energy to be installed by the end of 2020 and currently has a mandate to procure up to 400MW of renewable energy by the end of this summer.

Moving on to Europe, in the UK the government is seeking 10GW of new capacity towards 2030 where offshore wind is competing with other less established technologies for a total pot of money of £ 557 million allocated for future CfD auctions. The third CfD auction is expected to take place during the spring of next year.

As we have previously communicated, the consenting phase is still ongoing at our Hornsea 3 project and we expect to have key consenting in place during the autumn of 2019, which would make the project eligible to participate in an expected fourth CfD auction at a later point in time.

Following the second transitional auction in Germany, we expect the German authorities to host the first centralised tender for an expected 7-800MW offshore wind farm in 2021.

A climate protection strategy and action programme is currently being discussed by the German government coalition partners. We remain hopeful that Germany will make a strong commitment to the Paris Climate Agreement and expedient phase-out of coal capacity and the restructuring of carbon pricing.

As you know, the Dutch government has published a firm roadmap for 11.5GW of offshore wind to be constructed by 2030 compared to the previous target of 4.5GW by 2023. This is supplemented by a commitment to a complete phase-out of coal by 2030 and the introduction of a carbon price floor from 2020.

The next tender in the Netherlands will be Holland Coast South 3 and 4 which is expected to take place in Q4 this year.

In Denmark, the government has just recently stated a very significant focus on offshore wind in order to reach its 50% renewables target by 2030. The new energy agreement covering the period post-2020 is under development and is expected to be finalised this year. The agreement could, subject to coming political negotiations, open up for an additional number of large-scale offshore wind farms to be constructed between 2024 and 2030.

The Belgian government has just announced plans to double the area of its North Sea waters made available to offshore wind parks after 2020 as part of its exit strategy from nuclear power. Belgium has currently 0.9GW of offshore wind capacity and wants to increase that capacity to 4GW by 2030. Tendering could come as early as next year, assuming draft plans pass into legislation at the end of 2018 or early 2019.

Turning to slide 6 for an update on the key construction projects in progress around the company where I am glad to see that construction and preparations are generally progressing according to plan. At Walney Extension, the installation of all 87 turbines has been completed. The project has

been performing ahead of original schedule recently. We now expect Walney Extension to be fully commissioned in the third quarter this year compared to the previously communicated second half of this year.

At Borkum Riffgrund 2, the installation of foundations has started and we have installed 15 out of 56 foundations by now and we expect the installation of turbines to commence within the next couple of months.

At Hornsea 1, we continue to see good progress and we have installed 23 out of the 174 foundations while the installation of the offshore export cable is ongoing.

At Borssele 1 and 2, procurement is currently our main focus. The Turbine Supply Agreement was signed last year and the remaining key contracts will be finalised during this year.

For Hornsea 2, which will be, as you know, the world's biggest offshore wind farm when operational in 2022, we have selected SiemensGamesa as the exclusive supplier of wind turbines. We expect to deploy their 8MW wind turbines. Furthermore, we have commenced construction of the onshore substation at Hornsea 2.

In Bioenergy & Thermal Power, we are well underway with the bioconversion of the Asnæs Power Station which is progressing according plan with expected commissioning by the end of 2019. The construction of our first commercial Renaissance plant in Northwich in the UK has been completed.

As you know, the Renaissance plant in Northwich is the first of its kind and there are a number of mechanical issues that are being addressed while we gradually ramp up the plant. We are making progress but testing and fine tuning of the machinery is still ongoing. We still expect the plant to be commissioned before the end of Q2 2018.

At the end of March, we had 301,000 smart meters up and running at Radius' power distribution customers. Thus, we are well on track to install approximately 1 million smart meters by the end of 2020.

All in all, we are quite pleased about our operational and financial performance in Q1 and continued strong strategic progress. On that note, I will hand over the word to Marianne.

0.14.15

Marianne Wiinholt

Thank you, Henrik, and good morning from me also.

If we start on slide 7, I will dive into the financials of Q1 2018.

As Henrik said, we realised an EBITDA of DKK 5.5 billion, an increase of DKK 2.2 billion compared to Q2 2017.

This increase was primarily driven by higher earnings from operating wind farms and partnership agreements. In Bioenergy & Thermal Power, EBITDA doubled to DKK 0.4 billion, which was driven by improved spreads, higher heat generation due to colder weather and the bioconversion of the Skærbæk Power Plant in Q4 2017.

Distribution & Customer Solutions was flat on a very strong Q1 2017 due to a positive arbitration outcome regarding the renegotiation of the gas purchase contract in 2018.

Net profit totalled DKK 3 billion, an increase of DKK 1.8 billion driven by the higher EBITDA. The free cash flow from continuing operations for Q1 2018 came in at a negative DKK 1.6 billion, which was in line with the free cash flow of the first quarter last year. The higher EBITDA and the receipt of the deferred proceeds from the farm down of 50% of Walney Extension of DKK 0.8 billion was offset by tax payments of DKK 3.1 billion.

We decided to pay the payments that we would normally do in November in March and in Q1 2017 we did not have any tax payment at all. We also paid residual taxes relating to 2017 which totalled DKK 0.6 billion.

We also had an increase in funds tied up in working capital of DKK 0.6 billion compared to Q1 2017.

If we then turn to slide 8 and our net debt and financial ratios. Our net debt ended at DKK 4.3 billion, mainly driven by the early on-account tax payments I just described as well as the distribution of DKK 3.8 billion of dividends to our shareholders.

Our key credit metric FFO/adjusted net debt stood at 46% at Q1 2018, once again above our target level of around 30%. We were pleased to see that yesterday S&P reaffirmed their BBB+ rating with a stable outlook.

Return on Capital Employed (ROCE) came in at 27%, an increase of 10%-point and was significantly impacted by the farm down gains on Walney Extension and Borkum Riffgrund 2 at the end of 2017.

On slide 9, I will describe our framework for interest rate and inflation risk management with a focus on asset and liability management principles.

The overall framework for our risk management consists of four risk categories of asset and debt allocation which Ørsted's assets are divided into. Based on the nature of inflation and interest rate exposure.

Simple risk metrics are used to match assets with the appropriate debt within each category. There are three main objectives of the interest rate and inflation risk management. First of all, the long-term real value of equity and hence the shareholder value is protected by offsetting the interest and inflation risk exposure embedded in Ørsted's income streams by allocating debt with similar but opposite risk exposure.

Secondly, the cost of funding is minimised by allowing flexibility to take advantage of attractive market opportunities, for example obtaining long-term funding at the current very attractive funding rates.

And lastly, the cost of hedging is minimised by using the natural portfolio synergies between the assets allowing matching of up to 100% of asset value with the appropriate debt. The latter is particularly utilised to prioritise the assignment of fixed-rate debt for up to 100% of estimated asset value of our continental EU offshore wind farms, which is offshore wind farms in Denmark, Germany and the Netherlands and also potentially new wind farms in the US and Taiwan where the subsidies and the PPAs are fixed in nominal terms.

Conceptually, these fixed nominal income streams are matched with Ørsted's fixed nominal debt obligations and we thereby eliminate the inflation risk embedded in the fixed nominal income streams.

This approach leaves the inflation indexed revenue primarily from the UK offshore wind farms to service the shareholder returns thereby protecting the real value of equity against fluctuations in inflation rates.

Let's then move to the quarterly results of the business units, starting with Wind Power on slide 10. Power generation increased by 43% relative to Q1 2017 primarily due to the ramp up of generation from Burbo Bank Extension, Race Bank and Walney Extension. But higher wind speeds and higher availability also contributed positively.

EBITDA amounted to DKK 4 billion, an increase of DKK 1.8 billion. The earnings from the operating wind farms increased 51% on the back of higher power generation. The earnings from partnership agreements were up by DKK 0.8 billion due to a high level of activity related to the construction of Walney Extension and Borkum Riffgrund 2 for partners. The free cash flow totalled a negative of DKK 0.2 billion. The higher EBITDA and receipt of the deferred proceeds of DKK 0.8 billion in Q1 from the farm down of 50% of Walney Extension were partly offset by the previously mentioned early on-account tax payment and payment of residual taxes regarding 2017. Return on capital employed for wind power stood at 30%.

If we then go to the results for Bioenergy & Thermal Power on slide 11, here we saw that EBITDA more than doubled and amounted to DKK 0.4 billion. The increase of 0.2 billion was due to the improved spread, higher heat generation and the bioconversion of the Skærbæk Power Plant. The free cash flow amounted to DKK 0.4 billion and here the increase was primarily due to the higher EBITDA.

If we then turn to page 12 covering the results in Distribution & Customer Solutions. Here we saw that EBITDA in Q1 was flat on a strong Q1 2017, which was due to a positive arbitration outcome regarding the gas purchase contract we described before. But in addition, we had higher earnings from our route to market for physical power and gas in Q1 2018. In 2017, Q1, we had extraordinary high earnings from the trading of our financial energy exposures.

The free cash flow amounted to a negative DKK 0.2 billion. The decrease of DKK 1.7 billion was due to more funds tied up in receivables driven by higher sales including higher sale of ROCs, receivables from ROCs, and higher prices as well as receivables from the one-off arbitration I just mentioned.

And then finally, we turn to the financial guidance and policies on slide 13.

As Henrik mentioned, we have raised our EBITDA guidance excluding new partnership agreements by DKK 0.5 billion to DKK 12.5 to 13.5 billion due to the strong operational start to the year and the positive arbitration outcome. As a further result of the positive arbitration outcome, we have also changed the directional guidance for Distribution & Customer Solutions relative to 2017 from significantly lower to lower.

We maintain the remaining guidance and targets as we have previously stated. We believe that we will carry out the divestment of Hornsea 1 in the second half of 2018 or in 2019.

On that note, we will now open up for Q&A. Operator, please.

0.24.16

Operator

Thank you. Ladies and gentlemen. If you have a question for the speakers, please press 01 on your telephone keypad and you will enter a queue. You will have to limit yourself to one question at a time and then re-enter the queue if you have further questions. Please be aware that this call will end no later than 11:30. Once again, please press 01 on your telephone keypad to enter the queue.

Our first question comes from the line of Kristian Johansen from Danske Bank. Please go ahead, your line is open.

0.24.48

Kristian Johansen

Yes, thank you. So, my question is around this arbitration case and then whether you can quantify the exact impact and also how many other similar arbitration cases do you have ongoing? In other words, I mean, is there a possibility for further one-offs to be booked in the coming quarters? Thank you.

0.25.10

Marianne Wiinholt

Unfortunately, we cannot say – mention the amount. We are bound by confidentiality. This is the last arbitration so you cannot expect further arbitration gains from renegotiations going forward in the next quarters.

0.25.29

Kristian Johansen

Thank you.

0.25.32

Operator

Our next question comes from the line of Sam Arie from UBS. Please go ahead.

0.25.38

Sam Arie

Hi everybody, good morning and thanks for the presentation and congratulations again on an excellent set of results and I admit I am smiling as I say that because I think I have said that to you every time now. And looking forward it is always, you know, the calendar is packed with catalysts that could be very positive. My question is and I apologise for asking this but just to keep us all

honest, can you spend a minute to talk about the downside so you know all the companies in the sector have issues you know problems in the in-tray that keep management up at night. What are the biggest negatives that you are dealing with at the minute. What are you worried about and where, if anywhere, should we be cautious at this point?

0.26.23

Henrik Poulsen

Thank you, Sam, and you know it is obvious that it is a broad question. I would say I sleep quite well at night also at the moment. There is no doubt that we're obviously all, as probably are many of you, you know, waiting for the outcome of the auctions that are currently in progress. Obviously, we are looking forward to getting the outcome in Germany which should arrive hopefully within days or at least within the next few weeks. In Taiwan, we will probably get an outcome from the grid allocation where the hearings take place tomorrow and on Saturday. We would expect to get an announcement shortly after that so probably no later than next week and then not least also of course outcomes in Massachusetts and Connecticut so it is not something that keeps me up at night but we are obviously very excited about getting to the outcomes of these quite competitive auctions. In terms of things that constitute the downside, you know, being or doing what we do I'd always say that building these very large assets far from shore we should always keep an eye on our construction. We have almost come to take it for granted that we deliver all of these offshore wind farms on time and budget and we have a strong track record in that area but I would certainly, you know, never take anything for granted. These are very complex projects but they are - as I mentioned earlier - they are in really good progress. Other than that, I mean clearly the competitive intensity in offshore wind has intensified over the past couple of years. These auctions and tenders that we participate in, there is obviously a keen interest to win these projects and there is no doubt that we also have a need to continue to sharpen our sword and continue to drive down the cost of electricity by constantly innovating on our side and that is also, I believe, a key focus to make sure we can sustain good value creation in a competitive environment. So, I think I will leave it at that for now but please feel free to ask more specific questions if you have any particular concerns.

0.28.43

Sam Arie

Well, now that is very helpful, thank you. I'll put my next question back in the queue. Thank you.

0.28.51

Operator

Our next question comes from the line of Casper Blom from ABG Sundal Collier. Please go ahead, you line is open.

0.28.59

Casper Blom

Thanks a lot and also congrats from my side on the strong numbers here again. I was hoping that maybe you could share a little more light over the Taiwaness process. As you mentioned Henrik, we should expect news within the next week. But what exactly, how can you say, step in the process is it that we are getting now, when will we get sort of exact news on a PPA, and when would you expect to be able to take a final investment decision in Taiwan, please?

0.29.30

Henrik Poulsen

Yearh so – as I said, the hearings will take place tomorrow and Saturday where all projects that are bidding or applying for grid allocation will get a chance to present themselves to the evaluation panel. We will then expect them to come forward with a grid allocation, probably within the next week. We expect that grid allocation to essentially allocate the 3.5GW and part of that will go to an early allocation that should be build within the next couple of years and then we will see the remaining 3GW being allocated, most likely as we understand the framework, to the top 4 applicants where the number one will get 1.2GW of grid allocation, the 2nd will get 900MW, then 600 and 300MW for number 2, 3 and 4 in that ranking. If you get grid allocated you can then essentially move into a PPA process with TaiPower and once that has been settled during second half of this year we will expect you continuing with the permitting process seeking both offshore and onshore permits to eventually commence construction. And once we have visibility on that we should be in a position to FID a potential project during 2019. So, that's the overall process on the grid allocation. And then as you know there will be a price based auction. We currently expect there to be a deadline for the price based auction for an additional 2GW. The deadline would expectedly be in June and we would expect to get an outcome from that auction fairly quickly that should be a relatively straight forward allocation mechanism so we would expect the outcome also during the month of June.

0.31.33

Casper Blom

Great. If I just may follow up, because on the PPA discussion with TaiPower there has been a lot of numbers mentioned the last year or so. And I think the last one I heard was around a 160 EUR/MWh. Is that still sort of the level that you are thinking?

0.31.50

Henrik Poulsen

That is the most recent feed-in tariff that has been made public by TaiPower and the Taiwanese government. There is a 20 year tariff slightly above a 160 EUR. There could be an alternative tariff structure where you go for higher tariff during the first 10 years and a lower tariff during the last 10 years. And again, its all going to be subject to the final PPA negotiations with TaiPower. But that is the current tariff level.

0.32.24

Casper Blom

That's very clear. Thanks a lot Henrik.

0.32.27

Operator

Our next question comes from the line of John Musk from Royal Bank of Canada. Please go ahead.

0.32.32

John Musk

Good morning everyone. We have obviously had a few upgrades to guidance over the past few quarters and just looking at the quantum of the upgrades you have given today, I just wanted to get some sense of is this enough or do you think you are being conservative here because the result in Distribution & Customer Solutions and the increased guidance there plus the strong Q1 we have seen in Wind Power would suggest that potentially you have left a little bit in the bag here. Would you be willing to comment on that?

0.33.14

Henrik Poulsen

Thank you, John. I am obviously, I don't want to start modifying the guidance here. We generally do believe that 12.5-13.5 is the right guidance for the full year. To the point you make, we have had a very strong operational first quarter with very strong availability and wind speeds driving up our load factor to 55 which is a record load factor and then we have had that arbitration outcome and the two in combination drive that half a billion, so to speak. So we do feel that this is sort of the prudent guidance to provide.

0.33.53

John Musk

Okay, thank you.

0.33.55

Operator

Our next question comes from the line of Gurpreet Gujral from Macquarie. Please go ahead.

0.34.02

Gurpreet Gujral

Hi guys, just a question from me on the CAPEX plans that you have in the non-offshore wind business within renewables. I just wanted to get a guide on what you expect to invest in other projects in the battery space or the solar PV space this year and potentially next year? Thank you.

0.34.22

Henrik Poulsen

Yes, we are, as we have mentioned earlier and most explicitly back in February, looking into ways into other renewable technologies. We at that point also communicated that if you take sort of a 5-6-7-year view on the future, we would expect 85-90% of our total CAPEX to be allocated to offshore wind and between nothing and 10% of all of our CAPEX spend to go into these new renewable technologies and we are obviously maintaining a strict capital allocation discipline in looking at these new opportunities, which means that they are all going to be filtered against very strict value creation criteria. We are looking, as we mentioned earlier, into storage. We have, as we also referred to, made the first investment decision into a standard loan utility scale storage solution in the UK. These are relatively small projects in CAPEX terms, we are talking a few million Euro so they are not significant compared to what we will be putting into offshore wind. We also continue to look at opportunities to potentially engage in onshore wind and solar PV. There, we have not yet found the right opportunities and again, if we are to move into those areas, we will only do so if we find the exact right investment opportunities. All in all, we stand by the CAPEX allocation guidance that we provided back in February. We would expect between 0-10% of our total CAPEX for the next 5-6-7 years to go into these new technologies.

0.36.14

Gurpreet Gujral

Okay, thank you.

0.36.17

Operator

Our next question comes from the line of Kristian Godiksen from SEB. Please go ahead.

0.36.22

Kristian Godiksen

Yeah, thank you, Kristian here. Just one follow-up on Taiwan, a follow-up on the PPA which is subject to negotiations. Is there a risk that the feed-in tariff could come out lower as the level sounds very lucrative and especially obviously if the Tai government sees the level in hindsight what else has been settled for in Europe? Thank you.

0.36.44

Henrik Poulsen

It is not something that I can start guessing about, Kristian, as you would imagine. I mean, the current tariff level is between 160-170 Euro for 20 years. We clearly expect that feed-in tariff regime for 20 years to remain in place. What the exact final feed-in tariff will be, again, we are going to have to wait and see what the outcome will be of the process with Tai Power but we obviously remain convinced that this is going to be solid projects if we were to get awarded some grid or win in the price-based auction.

0.37.20

Kristian Godiksen

Okay, thanks a lot.

0.37.23

Operator

Our next question comes from the line of Mark Freshney from Credit Suisse. Please go ahead, your line is open.

0.37.30

Mark Freshney

Hi, good morning. Can you talk about the potential for further cost savings for the projects under construction? If I recall, at the end of last year I think there was an acknowledgement that you had completed some of the wind farms a little bit cheaper than you had expected. Can I ask given that Walney seems to be a little bit earlier in the time frame, it is normal if projects are completed earlier for them to cost less, is there any scope for you to further out-perform on the costs on the construction contracts?

0.38.09

Henrik Poulsen

Thank you, Mark. I mean, we are obviously hard at work every day to see if we can deliver these projects better than the original FID budget and as you refer to, we have previously announced that what we refer to as the IPO portfolio of construction projects, specifically six projects in the UK and Germany, that we now expect to deliver them at around 20 million per MW capacity rather than 22-24 that we announced at the time of the IPO and we obviously continue to look for opportunities. When we deliver a project like Walney ahead of schedule, it would typically entail certain savings compared to the original FID case and also it would also mean that we reach the CfD milestone earlier than expected which will mean that we start generating subsidised income earlier than we had originally expected. So, we constantly chase these opportunities. I would rather not start sort of predicting what the forward-looking potential is but I can reassure you that we are constantly chasing these opportunities and I would say we have a track record of generally delivering these projects on budget or slightly better.

0.39.31

Mark Freshney

Thank you.

0.39.35

Operator

Our next question comes from the line of Jørgen Bruaset from Nordea Markets. Please go ahead.

0.39.40

Jørgen Bruaset

Thank you. So, Henrik, you mentioned that you are looking at solar PV and onshore wind as potential investment cases. I was just wondering, when you look at these opportunities, are you only looking at projects to develop organically or would you be willing to do sort of corporate acquisitions, do you acquire portfolios or setups where you see that you could add something to the table? Thank you.

0.40.02

Henrik Poulsen

Thanks, Jørgen. We are looking at both organic and acquisitive growth opportunities. Again, we have moved into storage and so far that has been purely organic by buying individual projects or building projects related to our own existing asset base. When you look at solar PV and onshore wind, moving into those areas, I would expect us to acquire a platform including a development portfolio if we were to step into those areas and again, we would be looking for a development portfolio where we can bring some value creation through our existing skill base and through our balance sheet and we do believe there might be such opportunities out in the market but so far we have not been able to get to something that we found to be sufficiently interesting. So, I hope that answers the question, Jørgen.

0.41.06

Jørgen Bruaset

That is perfect. Thank you so much.

0.41.08

Operator

Our next question comes from the line of Deepa Venkateswaran from Bernstein. Please go ahead, your line is open.

0.41.16

Deepa Venkateswaran

Thank you. I had a question on Taiwan as well. So, obviously, it is almost a once in a lifetime opportunity to get allocated both in the beauty contest and in the competitive auction. Do you foresee any, if you are successful in both rounds, do you foresee any issue because the project is too huge to be able to double up your empire to 0.4GW if you are successful or would you say that actually, you know, we can only build up to 1.2 for whatever logistical reasons or risk reasons or otherwise? I just wanted to understand do you see any limits, obviously subjected to your site size in Taiwan? Thank you.

0.42.00

Henrik Poulsen

Thanks, Deepa. I mean, you know, the big price obviously in the grid allocation is the top rank which would give you 1.2GW of grid allocation which in our case would cover half of the Greater Changhua portfolio, you would still be looking for additional allocation, obviously, in the price-based auction, which is just adding on top of whatever you would get in the grid allocation. So, where that leaves us, obviously it is hard to predict. Again, we are anxiously awaiting the outcome but we will certainly have an ambition that over time, we do develop the entire Greater Changhua portfolio to 2.4GW. Again, whether you can get that done within the current allocation of 5.5, that is probably a bit of a stretch, frankly. But over time, I wouldn't be surprised if the Taiwanese government would want to expand offshore wind also beyond the currently announced 5.5GW. So, over time, clearly, we would have an ambition to develop the entire area.

0.43.03

Deepa Venkateswaran

Okay, thank you.

0.43.06

Operator

Our next question comes from the line of Marcus Bellander from Carnegie. Please go ahead, your line is open.

0.43.10

Marcus Bellander

Thank you, good morning. You mentioned that wind speeds were more or less normal in the quarter but I think you also state somewhere in the report that wind speeds were higher in the UK and lower in Germany and Denmark. I am just curious about how big a difference does that make from sort of a mix perspective? And I am thinking both on your average power price but also on your load factor.

0.43.42

Marianne Wiinholt

It is definitely positive that we see very strong wind speeds in the UK and therefore we see that the revenue is benefiting from that and also the load factor because it is in the UK that we have the wind farms with the highest wind speeds and thereby the best load factors. So yes, that has impacted the strong Q1.

0.44.06

Marcus Bellander

And is it possible to quantify that effect in Q1?

0.44.09

Marianne Wiinholt

No, not really.

0.44.13

Henrik Poulsen

But there is a positive mix queue, no doubt, I mean, if you want high speeds, we want them in the UK.

0.44.19

Marianne Wiinholt

Yes.

0.44.21

Marcus Bellander

Okay, thank you.

0.44.25

Operator

Our next question comes from the line of Pinaki Das from Bank of America Merrill Lynch. Please go ahead.

0.44.30

Pinaki Das

Hi, good morning, thank you so much for taking my questions. I have got a couple of questions, one for you, Henrik. Just on Europe you have a slide, slide number 5 where you stated the different countries and the targets. I just wanted to get some insight into your thought process here because three of those countries, Germany, Netherlands and Denmark, maybe not Denmark but Germany and Netherlands could be sort of zero subsidy and also you mention Belgium could also be zero subsidy. How has your thought process evolved in terms of how you look at the zero subsidy projects and are they still effective, carbon pressures have gone up, you know, what is your thought process behind Europe in general where you see the zero subsidy regimes?

And the second question is for Marianne, just on your segment of information which is in your report, slide number 26. I just wanted to understand, I mean, you have almost 4 billion of EBITDA in the Wind Power division. The cash flow from operating activities is 75. Just wanted to understand what that difference is, is it the tax elements that you mentioned or working capital? It is quite a big difference, over 3 billion, so I just wanted to understand that. Thank you.

0.45.50

Henrik Poulsen

Thank you. On the zero subsidy projects in continental Europe, we still clearly consider the project that we won in Germany last year to be an attractive project. If anything I would say our confidence in the project has only gone up since we won it last year and I do certainly believe as you look further into the 2020s, sort of beyond 2025, that there is a potential which is also commercially attractive for us. We constantly monitor all of the underlying assumptions that we put into the bid case last year and compared to those assumptions we have clearly seen a positive development, not least in the power price but also in the outlook on CO2 pricing. We have used fairly conservative long-term estimates of CO2 prices in Europe in our cases and right now, what we are seeing in the market is that the market is actually well ahead of what we assumed back then and that is one of the key drivers of the long-term power price level. So, I would say, generally speaking, we remain quite positive on the value creation opportunity in the one zero subsidy project that we have taken so far.

0.47.16

Pinaki Das

Maybe just a follow-up on that. You know, would it be still similar in terms of financing this project with the market risk?

0.47.24

Henrik Poulsen

On a project like the one in Germany, we would clearly be in the market to look for corporate PPAs to put a price floor into the project over time. We do see the European corporate PPA market beginning to sort of develop and gain some momentum and in Germany, you actually need a zero subsidy project to be entitled to go out and sell in market the green certificates coming from the zero subsidised wind farm and therefore you could say the supply of green certificates in the German corporate PPA market is very limited at the moment, given that there are very few zero subsidy projects out there. So, over the coming year or two we would certainly be looking to start selling

some of that production volume into 10 and 10+ years corporate PPA contracts, which we believe will help build a fairly robust revenue structure into the project.

0.48.26

Pinaki Das

Thank you.

0.48.27

Marianne Wiinholt

Yes and then to your question on the operating cash flow in Wind Power. Yes, you are right, we have an EBITDA of 4 billion and we end up with an operating cash flow of only close to 700. The main difference is the tax, a significant part of this 3.1 billion tax payment, that relates to Wind Power so that is why you have the big difference.

0.48.51

Pinaki Das

Okay. Great. Thank you so much.

0.48.55

Operator

Our next question comes from the line of Elchin Mammadov from Bloomberg Intelligence. Please go ahead, your line is open.

0.49.02

Elchin Mammadov

Hi there. Your power business was unprofitable last year but this time this year it is at least near zero. I was just wondering, given the improved margins in the power prices in Europe, isn't it a good time to be looking at possibly selling this non-core asset or do you still want to hang onto it? Thank you.

0.49.23

Henrik Poulsen

No, we are very happy about the performance of the heat and power business in Q1 obviously, we have had fairly good weather conditions during Q1 this year. We have no active plans of going out trying to sell the asset, we are in the middle of converting it to biomass and we see significant value being added to the business right now so we are in no way active or in any hurry to go out and try to put this into the market. We still have value to add to this business.

0.49.57

Elchin Mammadov

Thank you.

0.50.00

Operator

I remind you that if you want to ask a question, you will have to press 01 on your telephone keypad to enter the queue.

Our next question comes from the line of Kristian Johansen from Danske Bank. Please go ahead.

0.50.13

Kristian Johansen

Yes, thank you, just a follow-up regarding the load factor as well. So, I obviously appreciate that the load factor will vary over quarters but I am just curious in terms of the guidance you gave on the IPO of these 48-50% now that you have actually ramped up most of these IPO wind farms. Is it still this range which is valid or have you discovered a bit of upside on the load factors of these wind farms?

0.50.44

Henrik Poulsen

It is a good question, Kristian. We would maintain the original guidance again. We have had a very strong quarter. It is the most windy quarter of the year so 55 is still, you need to look at it in a full-year perspective and there we would maintain the 48-50 but at least we do believe that we have strong support for the guidance we provided at the time of the IPO. But we will leave it at that guidance for now.

0.51.17

Kristian Johansen

Okay, thank you.

0.51.20

Operator

Our next question comes from the line of Sam Arie from UBS. Please go ahead.

0.51.25

Sam Arie

Hi again, so I sort of come back with another question and again thinking about the questions where the market is sometimes worried and I think there is a point about cost reduction in offshore wind happening so fast that eventually everything in offshore wind gets to the point where it doesn't need subsidies anymore. So, my sort of two questions for you on that sort of longer-term question. First, what sort of time frame do we need to think about for that outcome? And in that context, there was industry report in the UK, I think it was just a week or two ago, suggesting that actually in the UK, offshore wind would still need subsidies at some level, at least through to 2030, so I am interested if you would agree with that point of view.

And then secondly, once we do get to a zero subsidy level for offshore wind cost, do you think the industry goes to a merchant model there or do you think that there is some other kind of regulatory model that becomes standard such as zero subsidy contract for difference?

0.52.35

Henrik Poulsen

Thank you. First of all, it is important to again mention that we will continue to see subsidised contracts for years to come, again depending on the individual market regime and the individual regulatory framework and one key driver obviously being whether it is a full-scope project including the transmission asset or not. Where you include the transmission asset, I believe we are still some way away from reaching a zero subsidy level. That will take a number of years before we reach that point in my view and I would also say that we talk about zero subsidy in continental Europe but the matter of fact is it is zero subsidy because the state finances the transmission asset in a separate bucket and we would claim that if they were to include that transmission asset in a full-scope auction and expose it to competition, we would be able to build those wind farms at a lower total cost to the individual state. So, again there are a lot of nuances when we talk about zero subsidy. Overall, there is no doubt the costs are coming down rapidly. We have seen the 60% cost reduction in just four years, cost will continue to come down as we introduce new generations of turbines and continue to innovate the balance of plant. And of course as cost comes down over the next 5-10 years, we will gradually begin to approach zero subsidy models as we already began to see last year and that is kind of, in my view that is good news. It means that offshore wind is becoming very competitive vis-à-vis fossil fuels, vis-à-vis other renewables. That is going to drive very significant global demand for offshore wind and you need obviously to push the cost down and accept that that over time may increase your merchant exposure in order for the technology to have a really strong future. So, we can't have it both ways. We can't on one hand sit and say that we are worried about being subsidised and then the next moment we say we are worried about not being subsidised, you know. It is a transition, it is a natural evolution of a new industry and a new technology. I think this industry is doing a remarkable job in transforming itself and I am quite confident we can continue to create value also over the next 5-10 years as we continue to gradually progress towards lower and lower subsidies or even to zero subsidies. Of course, that will lead to a certain amount of merchant exposure but I believe there are different ways of beginning to also mitigate that risk. I mentioned earlier that for the German Cluster 1 project, we are working on corporate PPAs to go in and put a price floor structure into the project and that is one model. There could be other models, you refer to certain regulatory models that you could envisage where the state goes in and at least shares the downside risk with the bidders, which might actually be meaningful for the state to do in terms of getting to the best risk return equation also from their point of view. So, we are not as concerned about what that future will look like. We do believe that the industry has a very strong outlook. As we move towards lower subsidies, you also have to bear in mind we will see stronger and

stronger global volumes, stronger growth, stronger demand. We will continue to see cost coming down and in that total equation between supply and demand on a global level and the continued cost-out, I am quite convinced we can continue to generate fairly good value for our shareholders. A long answer to a pretty complex question but I will leave it at that.

0.56.42

Sam Arie

Very helpful, thank you.

0.56.45

Operator

Our next question comes from the line of Casper Blom from ABG. Please go ahead.

0.56.50

Casper Blom

Yes, thanks a lot. Just a subject that we also talked about a couple of years ago in connection with the IPO which would be the potential reverse changes to old subsidy levels. We have seen some news in France recently that the government wanted to renegotiate or potentially re-tender auctions that were actually done some years ago as they have been seeing cost coming down. Do you see any kind of risk of that happening to some of your old projects that sort of governments coming back to change conditions? And what is your sort of whole thinking about that debate? Thank you.

0.57.27

Henrik Poulsen

Thank you. We see no risk to our contract portfolio. When you look at the French situation, it is a particular situation as I see it. These are contracts that were awarded five years ago or more than five years ago and that means they were at around the 200 Euro per MWh level and during that exact time frame, we have seen this 60+% cost reduction for the technology, so you could say it is really a result of the French projects not really moving forward for a fairly long period of time while the industry has seen cost coming down significantly and that combination, when you look at it from the point of view of the French state, obviously means that now they are trying to rejuvenate the projects and actually move them into action. I don't think it is completely unreasonable that they kind of look at that 200 Euro level and ask themselves whether that is still the right subsidy level. You have to bear in mind that these are projects that have never reached an FID so I think it is a pretty particular situation and I don't think there is any cross-read to any of our projects. These are projects that are all FIDs and in construction or have been constructed. I am quite confident that the Danish, German and UK governments would never go back on a contract that has been allocated and acted upon through an FID or through construction.

0.59.00

Casper Blom

That is very clear. Thank you.

0.59.05

Operator

Our next question comes from the line of Kristian Godiksen from SEB. Please go ahead.

0.59.09

Kristian Godiksen

Thank you. I was just wondering what we have changed to make you participate in the upcoming tenders in the Netherlands which I guess should also be subsidy-free and where you didn't see value in participating in the one just finalised. Thank you.

0.59.24

Henrik Poulsen

Thanks Kristian. I mean, we would obviously take, you know, these Dutch tenders they are not that different in terms of their fundamental characteristics so the site characteristics so we would of course take a fresh look at all of the other key assumptions going into a bid case so that would be whether we have changed our view on the OPEX and CAPEX input parameters, the long-term power price parameters etc. so we would always update our view on these assumptions to see if we believe there is a robust value creation case or not.

1.00.06

Kristian Godiksen

And what about.. two things. What about required rate of return and then also on some of these, do you see that in your investment case decision that you had maybe too conservative assumptions now that you see that a number of your competitors did see value in participating in the tender?

1.00.25

Henrik Poulsen

We haven't really changed our view on the evaluation we did on the most recent Dutch tender. We stand by the conclusion that we reached. In terms of our return requirements, we do demand a certain spread on top of our cost of capital to make sure that we do create value and that we maintain a disciplined capital allocation and we are not going to change that.

1.00.54

Kristian Godiksen

Okay. Thank you.

1.00.56

Operator

Our next question comes from the line of Deepa Venkateswaran from Bernstein. Please go ahead.

1.01.02

Deepa Venkateswaran

Thank you. I have a follow-up question on the US market. So, you did talk about developments in New York for instance. Now, you don't really have a site there so I was wondering what your game plan is for the states where you don't have levers. Can you use the sites in other states to participate or do you anticipate essentially being able to win some levers later? Thank you.

1.02.28

Henrik Poulsen

Thanks, Deepa. I mean, it could be both, frankly. We could see ourselves participating in the state of New York from sites in neighbouring states and/or we would of course also be interested if there was an opportunity to buy sites in the area along Long Island which would probably be the opportunity that might come up. So it could be a combination of the two.

1.02.00

Deepa Venkateswaran

Okay. So you can use your New Jersey site for instance in New York maybe?

1.02.02

Henrik Poulsen

That is our expectation that we could use our New Jersey and/or Massachusetts sites.

1.02.10

Deepa Venkateswaran

Okay. Thank you.

1.02.15

Operator

As a final reminder, if you would like to ask a question, you will have to press 01 on your telephone keypad now.

Our next question comes from the line of Marcus Bellander from Carnegie. Please go ahead, your line is open.

1.02.26

Marcus Bellander

Thank you. I just wanted to follow up on the question regarding whether your guidance is conservative or not and it does look a little conservative to me as well and I am just trying to understand if there is anything in there, any one-offs that we might be missing, for example the repair of the wings on Anholt and London Array, will that in any way affect 2018 earnings negatively?

1.02.54

Marianne Wiinholt

I can definitely say no to the last question, Marcus, that will not have a significant impact. But what you need to take into account is that we also have quite a strong construction gain in the first quarter due to the good progress on Walney Extension so you will not see a similar construction gain in the remaining quarters. So it is a bit front-end loaded on that account and then of course you have the wind speed and the cold weather impacting. And the renegotiation lump sum.

1.03.32

Marcus Bellander

Okay, understood, that's great, thank you.

1.03.36

Operator

Our next question comes from the line of Kristian Godiksen from SEB. Please go ahead.

1.03.41

Kristian Godiksen

Thank you. Last question from me. So, you have still not found any attractive investments within solar and onshore wind but do you have the capacity to invest within all three areas at the same

time and then secondly, could you confirm that you are actively looking at potential acquisition targets within offshore wind in the US? Thank you.

1.04.04

Henrik Poulsen

I could see us potentially having the capacity, that doesn't mean we would necessarily do that but we could have the capacity within that 0-10% CAPEX allocation that I referred to earlier for the next years through 2023, there could potentially be room, of course that would depend on the size of the investments that we are looking at. I am not going to comment on anything specifically in terms of where we are looking for acquisitions.

1.04.36

Kristian Godiksen

Okay. But on the 0-10%, I guess, that would be on top of a potential acquisition of a company which both has some of the development competences but also the whole platform?

1.04.49

Henrik Poulsen

The 0-10% would both include the acquisition money as well as any subsequent development CAPEX.

1.05.00

Kristian Godiksen

Okay, very clear. Thanks.

1.05.03

Operator

There are no further questions at this time, so please go ahead, speakers.

1.05.09

Henrik Poulsen

All right. If no further questions, thank you all very much for joining this call and have a continued good day. Thank you.