



**RED ELÉCTRICA DE ESPAÑA**

**Analyst Presentation**

**May 29, 2003**



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# **A New Red Eléctrica**



## Achieved Main Goals since IPO

### 1999

- **Fragmented ownership of Spanish Transmission assets**
- **Average estimated Capex of €104 mn per year ('99-'04)**
- **Dividend pay-out policy: 65%-75%**
- **Underleveraged financial structure**



### Current Status

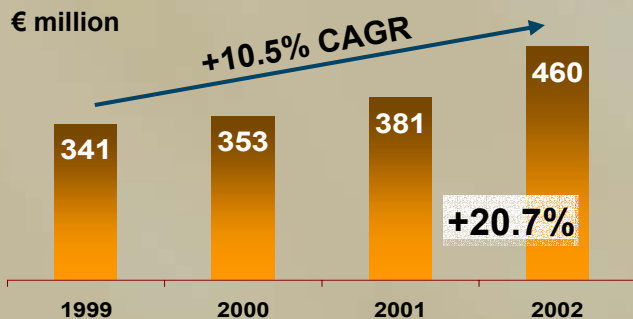
- **Set the basis to become Spanish TSO**
- **Average invested Capex of €112 mn per year ('99-'02)**
- **Dividend pay-out ('99-'02): from 66% to 68%**
- **Optimised capital structure with strong credit rating**





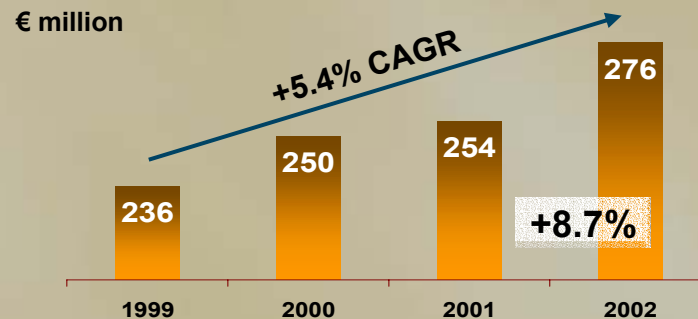
# With a Solid Story of Growth and Profitability

## Adjusted Turnover\*

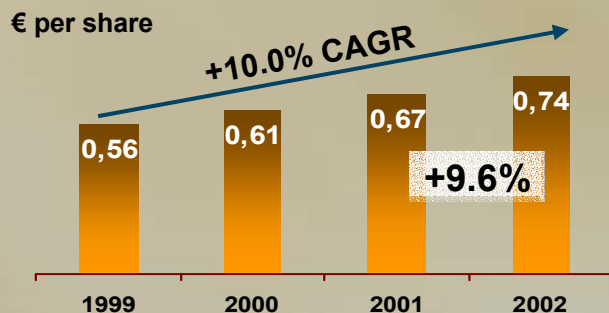


\*Net of energy purchases

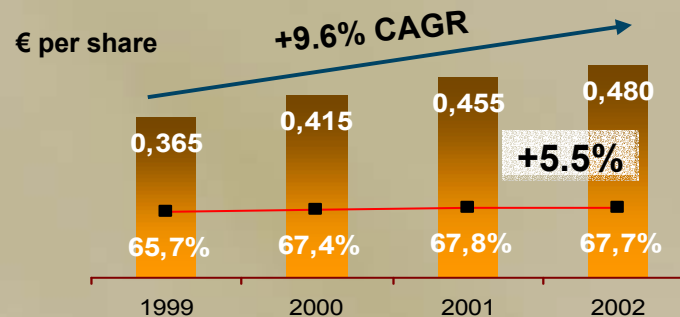
## EBITDA



## EPS

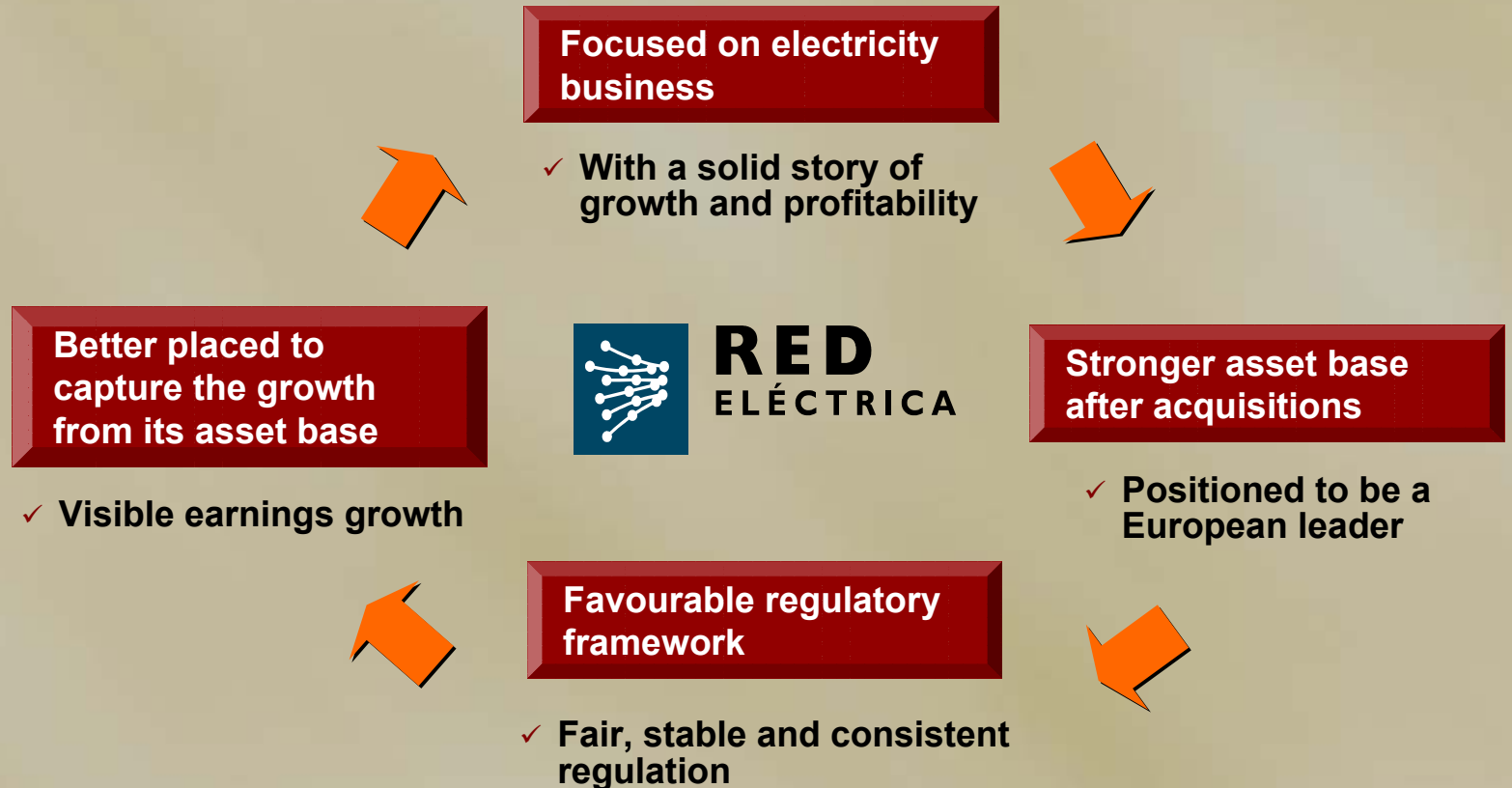


## DPS / Payout





## Positioned to Create Value: a New REE in the Market

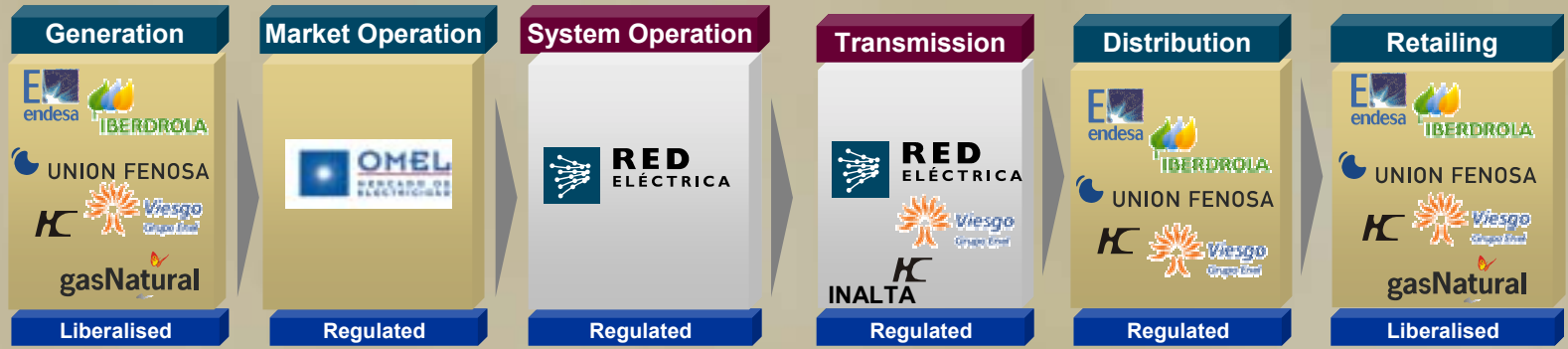


# **Core Electricity Business**

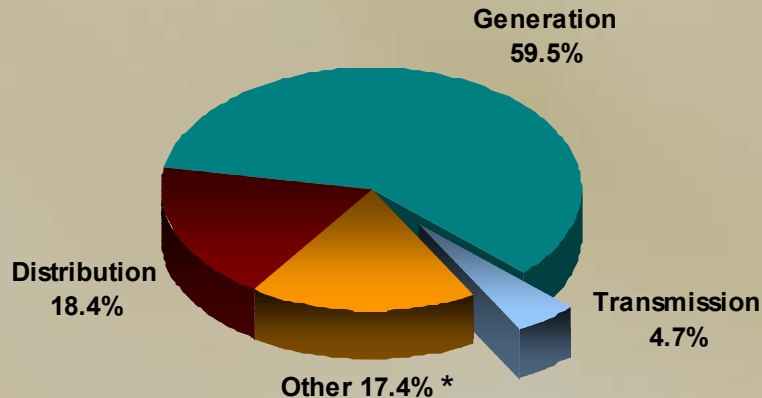




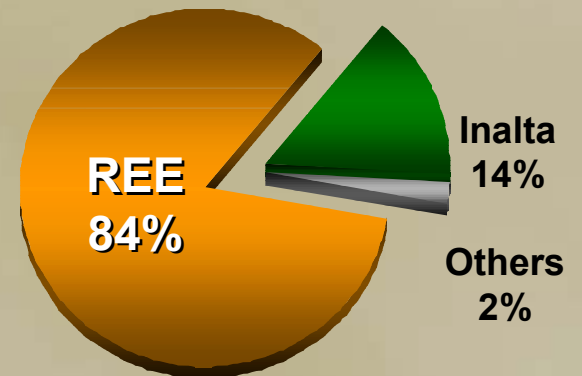
# REE in the Spanish Electricity Sector



## 2003 Tariff calculation: €14,951mn



## Allocation of transmission revenues 2003

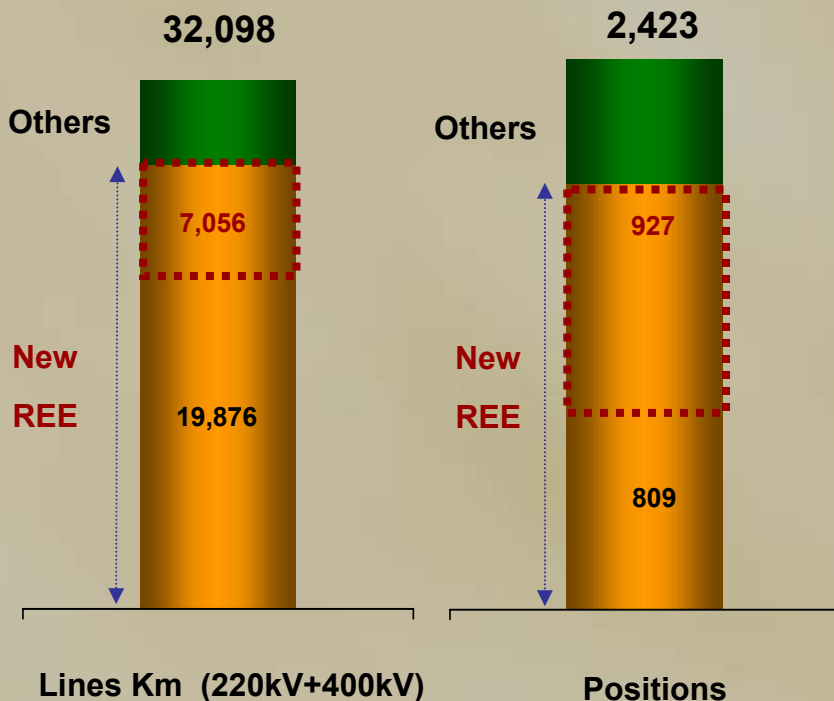


\* Including total island revenues

Source: Ministry of Economy and CNE

## Positioned to become Spanish TSO

### Total Spanish Transmission Asset Base\*



- New REE has full ownership of:
  - 84% of Spain's transmissions lines
  - 72% of Spain's positions
  
- New REE has a 25% interest in Inalta, the vehicle that owns Iberdrola's former transmission assets. Call option to acquire the rest in the medium term



## Other Activities in Core Business

### **Grid Manager and System Operator**

- Proposes planning of grid
- Manages ancillary services market
- Participates with Market Operator in electricity settlement process
- Guarantees supply quality and continuity

### **International electricity exchanges**

- Contracts signed prior to 1997 Electricity Sector Act (with EDF until 2010)
- Short term exchanges to maintain quality and reliability of supply



## Core Business Adjusted Turnover

- 96% of 2002 Adjusted Consolidated Turnover

### Core business adjusted turnover 2002 breakdown

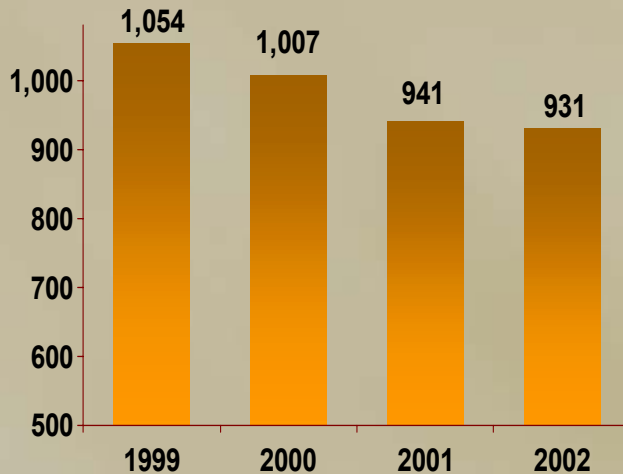


\*Includes engineering and construction projects carried out to third parties



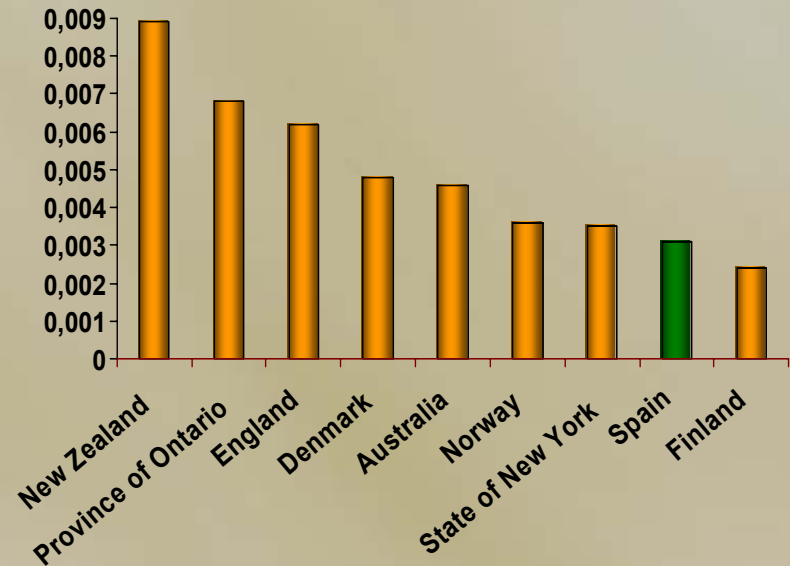
## REE Maintains one of the Lowest Transmission Costs

### Average workforce evolution



Source: REE

### Transmission costs €/kWh

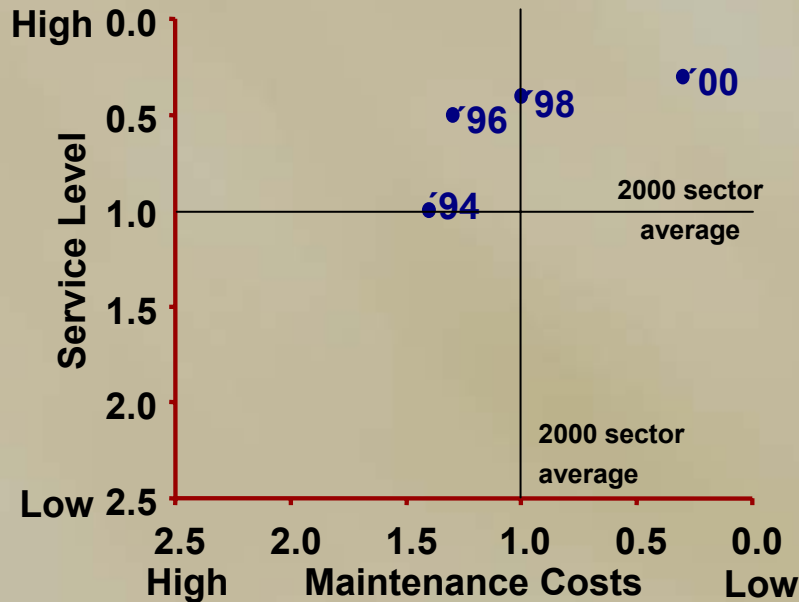


Source: Consulfirma



# Providing High Quality Service

## REE Trend from the International Benchmarking Standpoint



Source: UMS Group benchmarking report

## Average Interruption Time (Min)



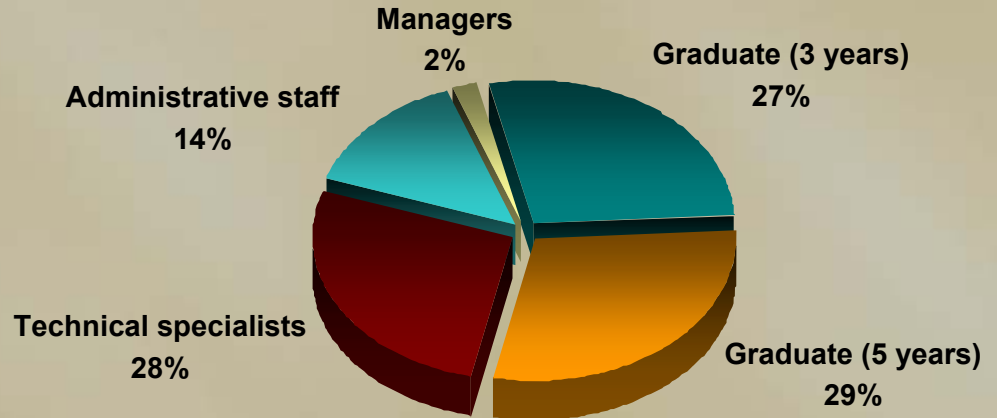
European companies: Italy, U.K., Portugal, Sweden and France

Source: REE and Company reports



## Driven by Qualified Human Capital

**High professional qualification**



**Employee Training & Development**

- 3% of personnel expenses
- 84% employee participation
- 35 hours on average per employee

Source: REE's 2002 Social Report

## **Stronger Asset Base after Acquisitions**





## European Transmission Sector Trends

**TSO Model Expected to Become Dominant in Medium Term**



■ TSO    ■ Without TSO

**Resulting European Trends**

**Creation of Regional Players**

- Integration of E&W / Scotland Network
- Nord Pool
- Iberian Electricity Market on track

**Transmission Unbundling in Eastern Europe**

- Most EU candidates towards TSO model
- External expertise and financial clout may be key for TSO model



## Asset Acquisition

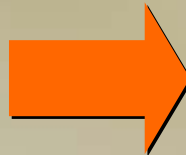
### Positions REE to become Spanish TSO

**Endesa's and Unión Fenosa's transmission assets**



- #### Impact of acquisitions
- Total Price: €1,345 mn (including €30 mn of work in progress)
  - 100% debt financing
  - Accretive from day 1
  - No goodwill
  - No transfer of personnel
  - 4 year O&M contracts

**25% stake in vehicle that owns Iberdrola's former transmission assets**



- Price: €14.9 mn
- Option to provide O&M after the 3rd year
- Call option for the remainder after 5 years



## **Expected Efficiency Improvements**

- **Minimum impact on overhead costs**
- **Efficiencies in procurement**
- **Ability to apply O&M best practices**
- **Installations / equipment standardisation**
- **Technological intensity / Scale in R&D**
- **Efficiencies in engineering and construction**



- **Only 20% expected increase in domestic workforce assumed to take on the increased regulated assets**

**Expected increase in EBITDA margin when integrated**



## Actions to Integrate Acquired Assets

TASK	2002		2003				2004				2005				2006			
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2		
Analysis of acquired assets			██████████															
Analysis of work in progress			██████████															
Closing date*			◆ 27/3															
Documentation			██████████															
Contracts, authorisations and licenses			██████████															
Drafting of integration process			██████████															
Redesign of maintenance zones			██████████															
Renewal and improvement plan			██████████															
Renewal and improvement works			██████████															
Telecontrol adaptation studies			██████████				██████████											
Transfer of full operational control to REE			██████████				██████████				██████████							
Refurbishment of control centres. New control system			██████████				██████████											
Hiring and training of new personnel			██████████															

\* With effect as of January 1, 2003 for accounting purposes

# **Spanish Transmission Regulatory Framework**



## Main Laws & Regulations in REE's History

**Law  
49/1984**

- Provides for unified management of Spain's transmission network
- REE created through RD 91/1985
- First step away from traditional regional integrated utilities

**Law  
40/1994**

- Transmission defined as  $\geq 220$  kV, to homogenize remuneration
- First step into liberalisation for Spain

**Law  
54/1997**

- Electricity Sector Law, implementing EU Directive 96/92, that set definitive liberalisation course
- REE defined as System Operator, approximating TSO status
- REE becomes non-public entity; 10% ownership limit, except for SEPI

**RD  
2819/1998**

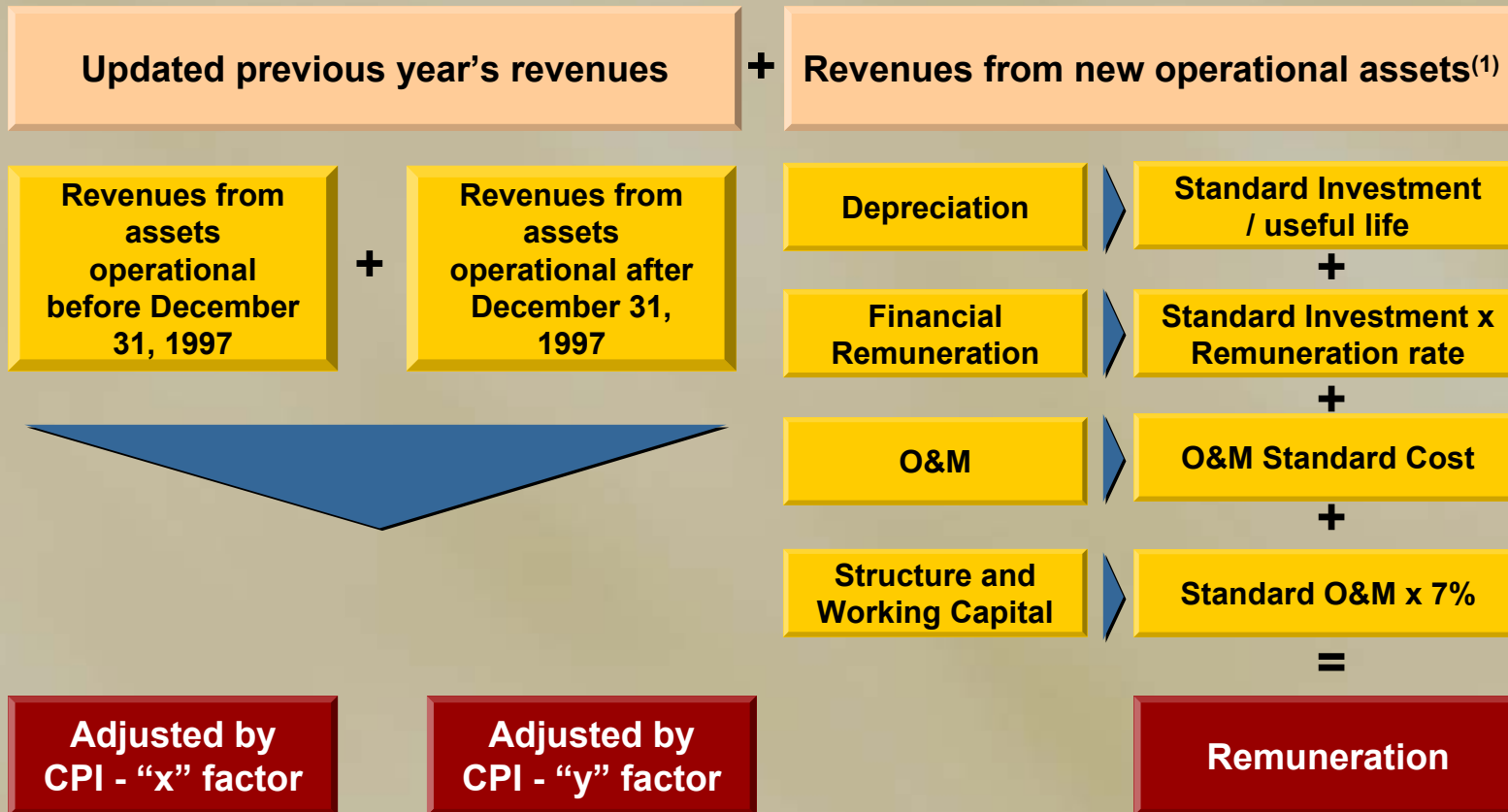
- Sets up formulas and unit standards to calculate transmission activity remuneration
- 1998 revenues set up by the Regulator
- Annual updates and new investments based on new regulation

**Law  
53/2002**

- No shareholder, other than SEPI, can hold a stake or voting rights of more than 3% of REE
- Right of first refusal over the Spanish transmission assets



## Transmission Activity Remuneration Method



(1) Only valid for directly awarded facilities. In case of facilities awarded by public tender (not yet used), the tender terms will provide for details



## Improved 2003-2006 Parameters

- The Regulator has approved the review of the remuneration parameters, valid until 2006, hence providing stability and minimising regulatory risk
- Within the same framework, the new parameters significantly improve the remuneration

	1999-2002	2003-2006
<b>Remuneration rate</b>	3m Euribor + 100 bps	10 yr Spanish Treasury Bond + 150 bps
<b>“x” &amp; “y” Efficiency Factors</b>	1.00%	0.60%
<b>System Operation*</b>	2002: € 12.9 mn	2003: € 15.5 mn

\* According to 2002 and 2003 Tariff calculation





## Positive Regulation Framework

**A fair,  
stable and  
consistent  
framework...**

- Equivalent to a gross RAB regulation
- Stable & growing revenue stream, independent of actual electricity demand
- Current regulation was approved in 1998 and has just gone through its first review with better terms for REE

**...that  
rewards  
efficiency**

- Incentive for REE to retain the benefit of outperforming the standards by means of both investment and operational efficiency

**Settlement**

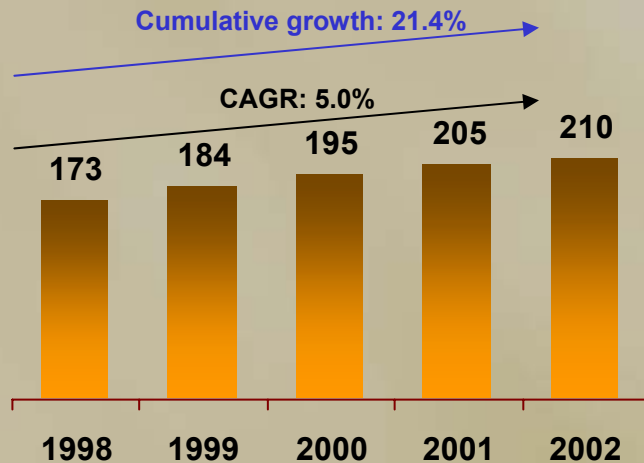
- Process administered by CNE
- Priority to regulated activities

# **Solid Investment Cycle**



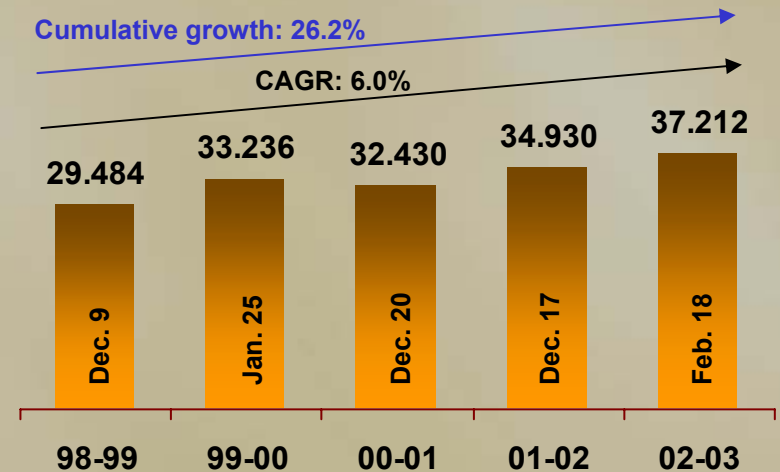
# Continuous Growth of Electricity Demand in Spain (Mainland)

### Demand (TWh)



Source: Ministry of Industry / Economy

### Winter peak demand (MW)



Source: Ministry of Industry / Economy

## ■ 2002 - 2011 forecasts:

- Electricity demand to grow CAGR 3.3%<sup>(1)</sup>
- Peak of demand in winter to grow 2.7%<sup>(1)</sup> CAGR vs. 3.3%<sup>(1)</sup> CAGR in summer

(1) Source: "Spanish Energy Infrastructure Plan 2002-2011" (Sept. 13, 2002). Base Case. Ministry of Economy



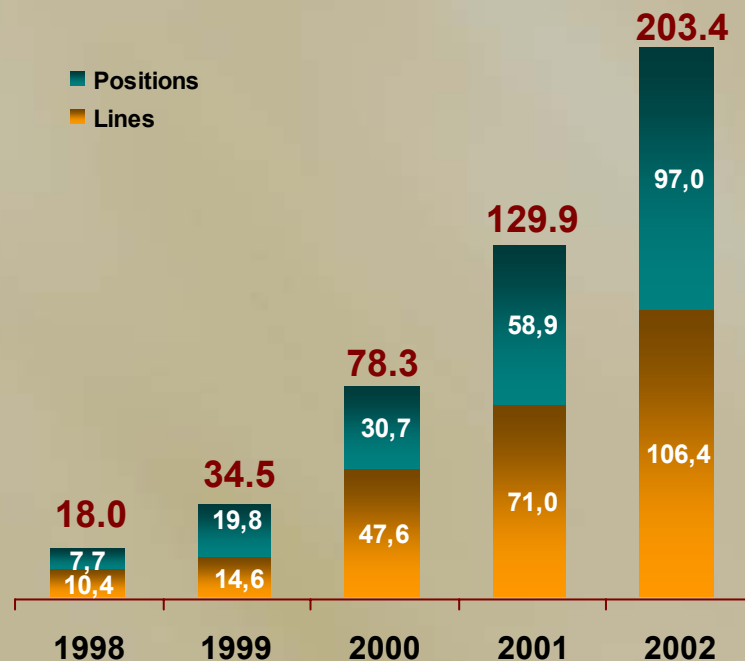
# Required to Launch a New Investment Cycle

## REE's Assets Commissioned

		1998	1999	2000	2001	2002
Lines (km)	400kV	295	0	380	181	702
	220kV	4	0	0	47	8
Positions (units)	400kV	44	21	37	78	
	220kV	15	5	8	10	

Source: REE

## REE's Transmission Network Investments (€ mn)



Source: REE



## Strong Investment Effort will Continue in the Future

### Spanish Energy Infrastructure Plan (2002-2011)

#### Approval Process

Jun 2001	CNE	Planning process initiated
Feb 2002	Ministry	Draft 2002-2011 Energy Planning
Sep 2002	Parliament	Final 2002-2011 Energy Planning

€ 2,720 mn

### REE's Transmission Investment Plan (2003-2007)

#### Main Drivers for Increase in Plan

- Larger investment needs associated with acquired assets vs. initial expectation
- Increased likelihood of certain projects
- Increase in suburban laying works
- New international interconnection with Morocco

€ 1,500 mn



## Capex Plan is Likely and Low Risk to REE

### Likely Plan

- €2.7 bn standard values estimate in Energy Infrastructure Plan is a weighted average of all proposals based on probability
- Less likely projects given a 0% weighting
- REE's capex estimates in line with the Plan

### Low Risk to REE

- Layout of REE's network expansion plans known in advance by generation developers
- REE invests in lines/substations related to new generation projects when they are clearly moving forward
- Even so, if a generation project is cancelled REE would recover its approved accumulated investments as new regulated revenue

# Diversification



## Good Fit of Diversification with Core Business

- **REE has leveraged its capabilities through diversification**
  - **Asset base: Transmission fiber optic network in Albura**
  - **Know-how: Ownership and O&M in LatAm**
  
- **Focus is on a low-risk strategy that pays-off long term**
  - **Flexible and scalable investments**
  - **Minimise uncertainties**
  - **New equity in subsidiaries need to be authorised by CNE**

**Creating Value from its Existing Assets and Know-how**

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## Overview of Albura



- Over 10,000 Km of state-of-the art optic fibre
- 175 access points
- Coverage of 75% population and 90% business areas
- Deployment DWDHM/SDH technology
- Main business lines: data capacity and transport, ADSL wholesale and IP services
- Communication services for telecom operators, ISPs, ASPs and major firms
- Role available for a strong second player given high market share of incumbent



## Albura Strategy

### Market Framework

- Commercial business plan adapted to the new market environment
- Expect to participate in capacity and data services auctions in 2003/2004
- Operators' financial constraints represent an opportunity
- Market difficulties benefit REE via reduced equipment prices
- Telecom regulator determined to improve market competition

### Investment Strategy

- Flexible and scalable business plan based on customer needs
  - Investment plan reduced by 71% from original 2001 plan
  - €150 mn invested until 2002
  - Capex plan is €150 mn\* for 2003-2007

### Alternative Infrastructure Provider

- To create value being the alternative infrastructure provider in the Spanish market
- Ensure customers' growth in their core business by acting as consolidator of transport infrastructure

\* Including possible acquisitions under study



## International Strategy Context

### Regulatory Framework

- €60 mn equity investment already made in Red Eléctrica Internacional is the maximum authorised by the Regulator

### Investment Strategy

- Financing structure without recourse to REE
- Target equity return at least 2% above project's calculated equity cost of capital
- No new investment opportunities are expected at this moment

### Specialised Consulting Services

- On-going specialised consulting projects (Eastern Europe, Maghreb, Middle East and South America))



**TDE**  
**(Bolivia)**

- In June 2002 REE completed acquisition of 99.94% of TDE for US\$88.3mn
- TDE owns the high-voltage electricity network in Bolivia with 2,000 km of lines and 19 substations
- TDE has been fully consolidated in REE financial accounts from July 1, 2002
- Results in 2002 (US\$mn):
  - Net Sales: 21.1
  - EBITDA: 13.8
- Potential growth driven by new capacity needs, financed against TDE balance sheet and cash-flows

**REDESUR**  
**(Peru)**

- 30% stake in 32 year concession awarded in 1997
- Financial performance above initial plan

**Solid performance to date credits REE's selective approach**

# Financials



## Consolidated P&L – Full Year

€ mn	FY02 <sup>(1)</sup>	FY01	Change Δ(02/01)	FY00	Change Δ(01/00)
<b>Adjusted Turnover<sup>(2)</sup></b>	<b>459.9</b>	381.0	20.7%	353.1	7.9%
<b>EBITDA</b>	<b>276.4</b>	254.2	8.7%	249.2	2.0%
<b>EBIT</b>	<b>157.0</b>	147.4	6.5%	147.5	-0.1%
<b>PBT</b>	<b>145.5</b>	139.1	4.6%	126.0	10.4%
<b>Net Income</b>	<b>99.9</b>	91.1	9.6%	83.1	9.5%

(1) Includes 2H02 results of TDE (fully consolidated)

(2) Net of energy purchases

Note: Data from 2001 onwards is consolidated



## Consolidated P&L – 1st Quarter 2003

€ mn	1Q03 <sup>(1)</sup>	1Q02	Change Δ(03/02)
Adjusted Turnover <sup>(2)</sup>	165.3	102.0	61.9%
EBITDA	108.2	71.9	50.4%
EBIT	62.2	44.0	41.4%
PBT	47.8	41.9	14.1%
Net Income	31.2	27.5	13.6%

(1) Includes impact of Endesa's and U. Fenosa's transmission assets

(2) Net of energy purchases

**Maintenance and renewal moved forward in 1Q2003**



## Balance Sheet Analysis

€ mn	Sep. 30 2002	Dec. 31 2002	Mar. 31 2003
<b>Fixed Assets</b>	<b>1,696</b>	<b>2,533</b>	<b>3,041</b>
<b>Net Debt</b>	<b>718</b>	<b>1,520</b>	<b>2,210</b>

- No unfunded pensions
- €151 mn in Spanish work in progress capex (remunerated when commissioned)
- Temporary financing via bridge loan

**€1,345 mn of Asset Acquisitions paid**





## Optimised Capital Structure

### Increased Leverage

	Sep. 30 2002	Mar. 31 2003
<b>Net debt</b>	€718 mn	€2,210 mn
<b>Net debt / (Net debt+Equity)</b>	47%	72%

- Plan to refinance bridge loan during 2003 via:
  - Syndicated loan
  - Long-term Bond

### Adjustments to 1Q03 Net Debt

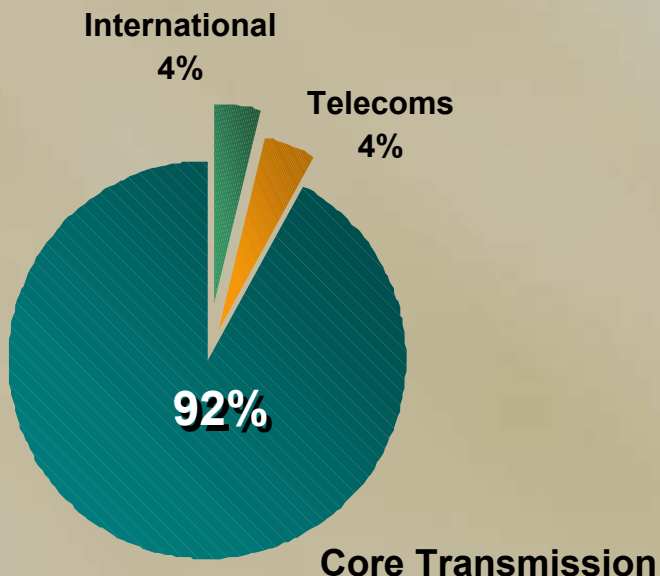
€2,210 mn	1Q03 Net Debt
(€80 mn)	Advanced for annual EDF supply
(€42 mn)	1Q03 ELE/UNF regulated revenues
(€34 mn)	Mar03 REE regulated revenues received post-closing

**Reduced WACC due to higher gearing.  
Strong credit rating (Moody's: A2, S&P: AA-)**



## Improving Quality of Earnings

### Objective medium term earnings split



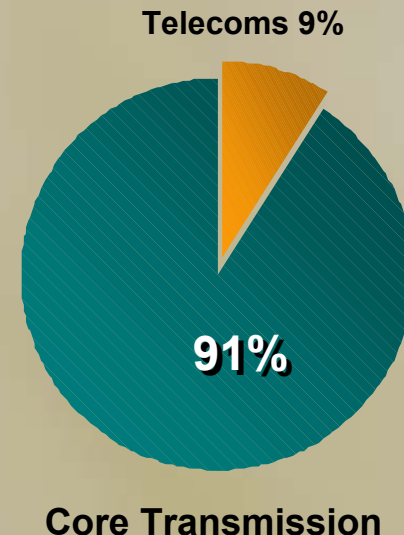
- Objectives for 'Core Business'
  - Larger exposure to core via asset acquisition
  - Synergies on acquired assets
- International accretive throughout period
- Telecoms becomes earnings positive



## Large Capex Programme Focused on Core Business

- 2003-2007 Estimated Transmission Capex: €1,500 mn
- 2003-2007 Estimated Telecoms Capex: €150 mn
- No further international investments likely

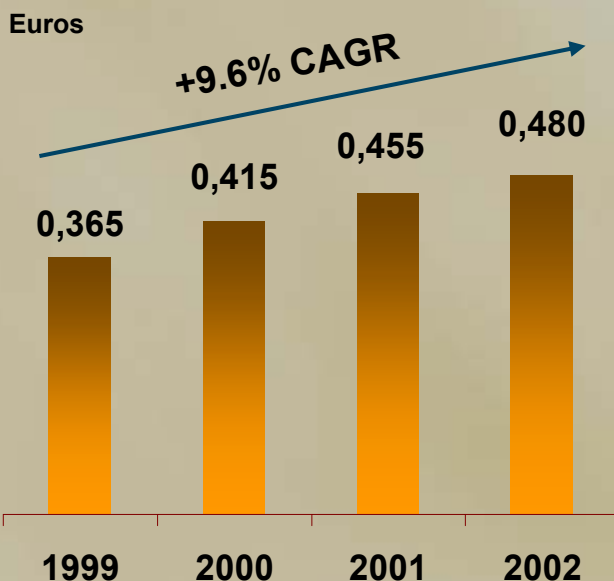
2003-2007 Estimated Capex:  
€1.65 bn



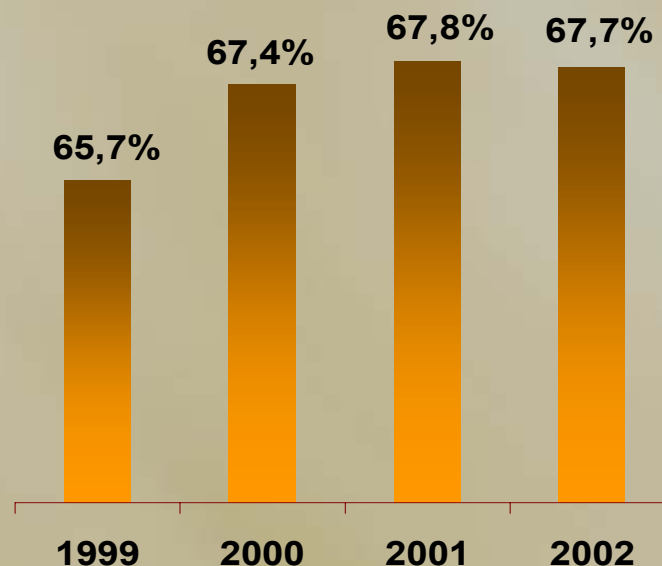


## Attractive Dividend Policy

### Dividend per Share



### Pay-out

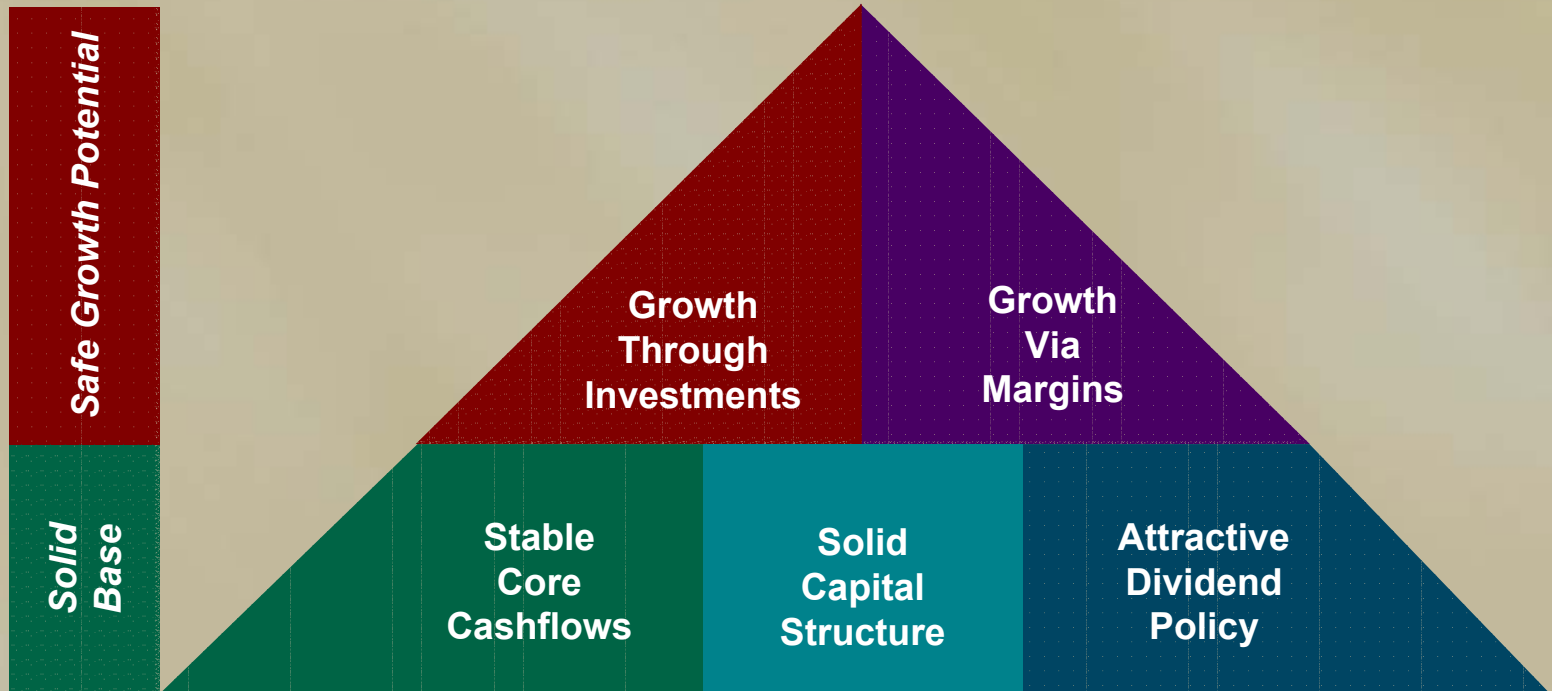


Note: Announced €0.29 per share supplementary 2002 dividend will be paid from July 1, 2003 to shareholders on June 30, 2003

# **Value Proposition**

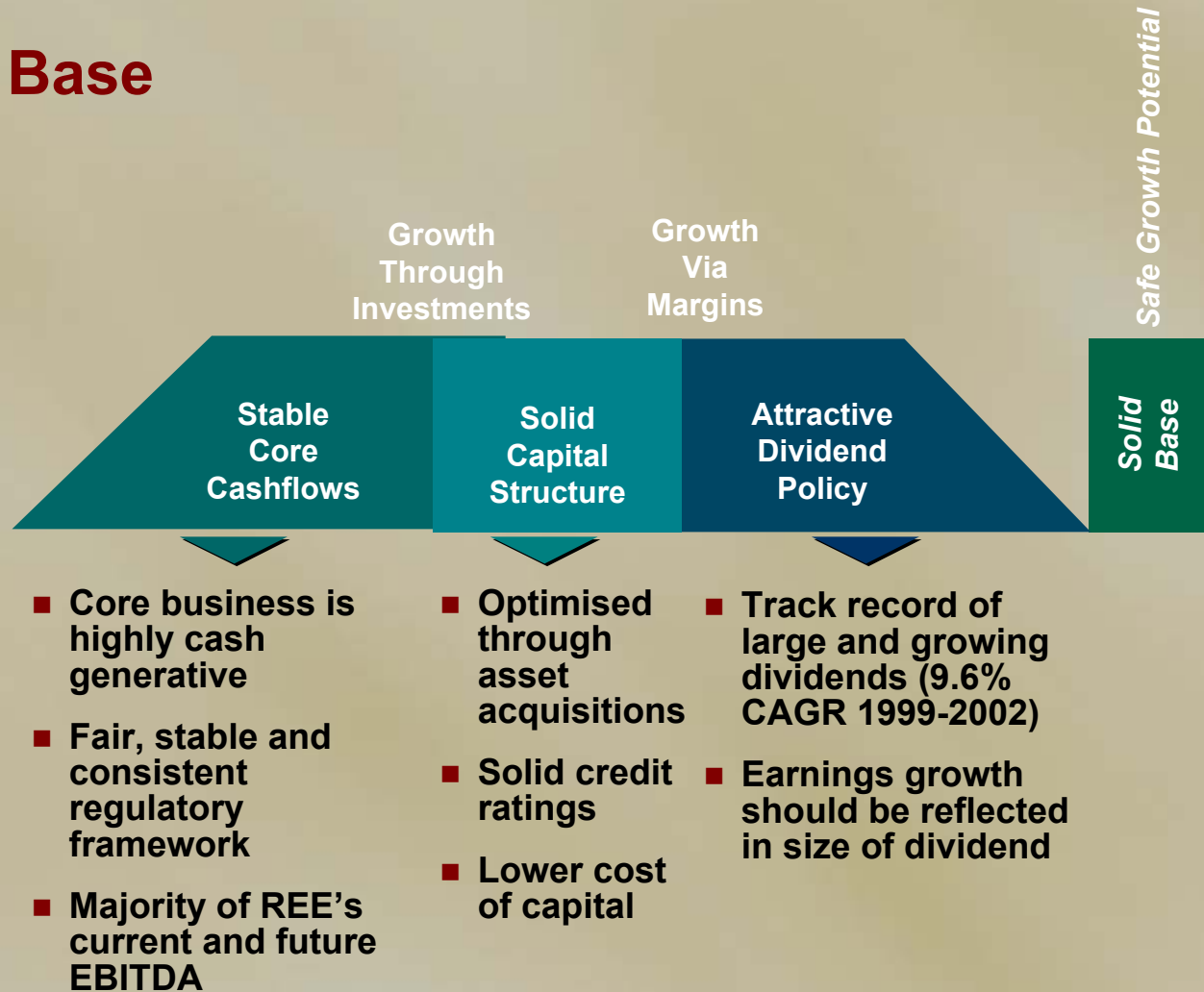


## Clear Path to Value Creation





# Solid Base



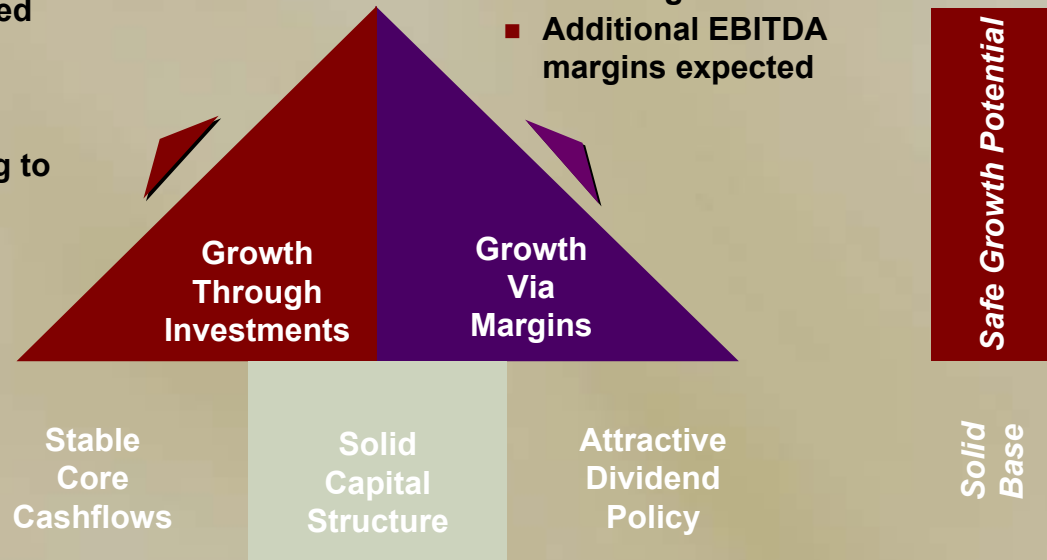
**Low risk, low downside**



## Safe Growth Potential

- Infrastructure Energy Plan forecast €2.7 bn in 2002-2011 at standard values
- REE expects to undertake the vast majority of the required investments
- Transmission investments are all in growth capex, leading to new remuneration
- Improved 2003-2006 regulation increases revenues from investment plan

- REE incentivised to outperform standard O&M expenses
- Integration of O&M contracts in 3-4 years will bring efficiencies
- Additional EBITDA margins expected



**Visible earnings growth**





RED ELÉCTRICA DE ESPAÑA

