

August 11, 2016 – 1:00 p.m. E.T.
Valener Inc. Q3 2016 Results



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Event Date/Time: August 11, 2016 - 1:00 p.m. E.T.

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CORPORATE PARTICIPANTS

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Gaz Métro – President and Chief Executive Officer

Pierre Despars

Gaz Métro – Executive Vice President, Corporate Affairs and Chief Financial Officer

Mariem Elsayed

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CONFERENCE CALL PARTICIPANTS

Ben Pham

BMO Capital Markets – Analyst

Robert Kwan

RBC Capital Markets – Analyst

PRESENTATION

Operator

Good afternoon and welcome to Valener's Third Quarter 2016 Earnings Conference Call. At this time all participants are in a listen-only mode. Following the presentation we will conduct a question and answer session. Instructions will be provided at that time for you to queue up for questions.

If anyone has any difficulties hearing the conference, please press star followed by zero for operator assistance at any time.

Please note that this call is being recorded today, Thursday, August 11, 2016 at one o'clock Eastern Daylight Time.

I will now turn the call to Ms. Mariem Elsayed, Senior Advisor, Investor Relations. Please go ahead, Ms. Elsayed.

Mariem Elsayed, Senior Advisor, Investor Relations

Thank you, Jessa. Good afternoon and welcome to Valener's third quarter 2016 conference call. With me today from Gaz Métro are Sophie Brochu, President and Chief Executive Officer, and Pierre Despars, Executive Vice President, Corporate Affairs and Chief Financial Officer.

This call is being webcast and I encourage you to download the supporting slides, which are available in the investor section of Valener's website under events and presentations.

As always, certain subjects we will cover involve forward-looking information. Please refer to the cautionary note section, which can be found on the second page of our presentation, as well as in our quarterly MD&A, which was published earlier today and is available on our website and on SEDAR.

We may also refer to certain indicators that are non U.S. GAAP financial measures and should not be considered in isolation or as substitutes for other performance measures that are in accordance with GAAP.

I will now turn the call over to Sophie.

Sophie Brochu, President & Chief Executive Officer, Gaz Métro

Merci, Mariem. Bonjour à tous. Good afternoon, everyone.

The third quarter was a strong one for both Valener and Gaz Métro. The improved financial performance in both entities reflects the quality of our underlying assets and the value of our diversified operations.

Valener generated adjusted net income of \$1.7 million, a \$900,000 increase from the third quarter of 2015 as stronger results at Gaz Métro were only partially offset by lesser winds observed at the Seigneurie de Beaupré wind farms compared to last spring. Adjusted net income per share was \$0.04 for the third quarter of 2016 compared to \$0.02 the year before. For the first nine months of the year, adjusted net income to common shareholders was \$50.6 million, up 3 percent compared to the prior year period. Valener generated normalized operating cash flows of \$0.36 per share this quarter compared to \$0.32 in the third quarter of 2015. This increase is mainly the result of higher distributions received from Gaz Métro following Valener's subscription of almost 4.5 million Gaz Métro units in the second half of 2015, as well a \$0.01 per unit increase in Gaz Métro's quarterly distribution to unitholders in late 2015, and lastly, the timing of Seigneurie de Beaupré distributions.

Now on to Gaz Métro on slide five. Gaz Métro generated adjusted net income of \$9.8 million during the third quarter compared to a net loss of \$100,000 last year. The higher net income was driven by growth in Gaz Métro-QDA's non rate base investment and in the increased natural gas deliveries. This was partly offset by lower net income at the Seigneurie de Beaupré wind farms, which you will recall enjoyed very strong winds last year. On a per-unit basis, adjusted net income was \$0.06 for the third quarter of 2016, up \$0.06 compared to the third quarter of last year. It was \$1.35 for the first nine month of 2016, up \$0.02 compared to the equivalent 2015 period. A significant improvement given the unit issuances made in the second half of last year.

Let's now look at our major projects, turning to slide six. In Montréal, we continue to make headway on the expansion work to triple the gas liquefaction capacity of our LSR plant with the objective to commission the expansion in late 2016. During construction, we

continue to safely operate the current plant in order to supply LNG to our growing customer base.

In Vermont, the second segment of construction of the Addison project, consisting of putting an additional 49 kilometres of pipelines in the ground, is ongoing and although we are facing some challenges, we are addressing them and expect work to be finished by the end of 2016. Pierre will give you greater details in a moment.

In the Saguenay region, we began engineering work and site preparation work last May. We will be working to improve and strengthen the transmission network in order to ensure reliable gas supply to our customers over the next 10 years. This project is valued at \$80 million. We're building a new compression station in La Tuque and upgrading the existing station in Saint-Maurice. Detailed engineering work and equipment installation remain under way with end service planned for late 2017.

Green Mountain Power continues to focus on the development of its multi-megawatt solar energy project, which consists of mounting five solar parks at five different sites in Vermont. Regulatory approvals were received for four of the five parks and construction of two of the parks is almost complete. Construction of two of the three others is expected to start this month. Upon completion of all five sites, which we expect will be by the end of 2016, they will have total capacity of 22 megawatts. This represents a \$40 million U.S. investment that is in the rate base of Green Mountain Power and it will contribute to growing it even further.

We are pleased with the progress being done at all of these sites and continue to monitor every project. Upon completion, these projects will allow us to better service our customers and the various communities we are expanding into, be it in Vermont, be it in Québec.

The third quarter was also one of many exciting and innovative achievements for Gaz Métro. Let me walk you through them. Please take slide seven.

In late spring, in collaboration with our partner, the SEMER, a semi-public renewable energy company, we enhanced the Blue Road, our network of natural gas refueling stations, with a new LNG station in Rivière-du-Loup. This one marks our eighth station on the Blue Road and following the usual ramp-up period it will enable transportation companies wishing to operate with more eco-friendly fuel and those already using LNG to travel east toward Gaspésie or New Brunswick or west toward Montréal. SEMER expects to produce approximately 3.5 million diesel equivalent liters of liquefied bio-methane at its plant from which it will be drawn the amount agreed for the station. This renewable natural gas will eventually make up 100 percent of the station's supplies, making this the first of the eight stations to supply RNG. With Rivière-du-Loup, the Blue Road will expand from east of Rivière-du-Loup as far as the reach is concerned, up to the other side of Toronto and to Mississauga. It's a pretty long road.

We announced alongside the Québec Energy Ministry that we started delivering LNG to Stornoway's diamond mine, the first Canadian diamond mine with all-season road access, and it's precisely this all-year-round road access that enables the mine to use LNG as a power source instead of diesel, which in turn means lower operating cost and environmental emissions.

In June we published our 2015 sustainability report based on the global reporting initiative, which is called GRI. This report is a culmination of consultations, surveys, workshops, and discussions with our stakeholders, 86 of them external, 57 internal, to identify and address what matters most to them. This online-only report is the fruit of the efforts of intense collaboration and a rigorous process. It highlights our ambitions, our achievements, and our dedication to social responsibility, and I encourage you all to view it. It has nothing to do or not much with the financials, but it sure has to do with the social license to operate and we do believe it is our most important asset.

In Vermont, Green Mountain Power recently transformed a challenging situation into a successful first. In the face of recent storms that caused mass outages, a few customers were able to use their Tesla Powerwall home batteries, which GMP began distributing in May in order to provide backup power to their homes for the duration of the outage. They never lost power. This revolutionary battery is rapidly forcing us to change how we think of energy storage. GMP is the first utility in the United States to install the battery for its customers. Over 700 of whom have already signed up to get one and we can't wait to see where it will go from there. The eye of the rest of America is turned to our little so beautiful electricity distributor in Vermont.

More recently, in July Green Mountain Power announced an agreement with Enel Green Power North America, a leading owner and operator of renewable energy plants in North America. The deal is to acquire 14 of its power stations, mostly in the New England area, with total capacity of 17 megawatts. The agreement also calls for the purchase of the power produced at two other stations. This acquisition, subject to regulatory approvals from the VPSB and the FERC, will increase GMP's renewable energy portfolio once completed. We expect the deal to close in fiscal 2017.

So, to recap, in a nutshell, this was another solid quarter for Gaz Métro. Our results reflect our handle on operating costs, an increase in natural gas deliveries in Québec and higher LNG deliveries, which now include those destined to Stornoway's diamond mine, over a 1,000 kilometres away from Montréal. We continue to make progress on our major projects and our ongoing diversification efforts, such as the development of solar parks in Vermont and the pending acquisition of Enel's 14 power stations. All this is to prove our resolve to our guiding principle, that of creating value for both our clients and our shareholders while contributing to bettering our environment.

I will turn the call over to Pierre now, who will talk to you about segment performance. Pierre?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Thank you, Sophie.

On to slide eight. Excluding special items, Gaz Métro generated adjusted net income of \$9.8 million during the third quarter of 2016, a \$9.9 million increase compared to the third quarter of last year. For the nine-month period, Gaz Métro generated adjusted net income of \$225.6 million, a 10 percent increase over last year.

The energy distribution segment generated adjusted net income of \$7.9 million during the third quarter of fiscal 2016, up \$9.2 million from the third quarter of last year.

Natural gas distribution in Québec generated an adjusted net loss of \$3.6 million, a \$6 million improvement from the third quarter of fiscal 2015, mainly as a result of an increase in capitalized interest on non-rate-base investments, increased natural gas deliveries, and an increase in the company's share of overearnings compared to fiscal 2015. Results for the first nine months of the year exceeded our expectations, owing in part to the item I just described, as well as our handle on costs during the third quarter. As a result, we now expect to finish the year slightly above the \$123.7 million of net income prescribed for in Gaz Métro-QDA's 2016 rate case and have therefore booked our share of overearnings accordingly.

Turning to slide 10, the Vermont operations generated a combined adjusted net income of \$11.5 million during the third quarter, up \$3.2 million or 4 percent from last year. Results were positively affected by the increase in GMP's average rate base and a timing difference between revenue and cost recognition. They were partly offset by the unfavourable effect of, beginning in the second quarter of 2016, no longer capitalizing allowance for funds used during construction, or AFUDC, related to the Addison project. Following a re-evaluation of costs relating to Phase 1 of Vermont Gas's Addison project, we now expect total project costs to be closer to \$165 million, resulting mainly from horizontal drilling activities and increased rock risk. You'll recall that recovery of costs relating to this project are capped to \$134 million following an agreement reached last year with the Vermont Department of Public Service. As such, we took a \$20.6 million impairment charge during the third quarter. Despite these overruns we, and the VGS management team, remain confident that this project will provide long-term economic benefits to the State of Vermont.

The natural gas transportation segment generated adjusted net income of \$3 million during the third quarter, up \$400,000 or 15 percent compared to the same period of last year. The increase stemmed primarily from greater volumes transported by PNGTS during the quarter.

On to slide 11, in electricity generation we recorded a \$200,000 adjusted net loss during the third quarter, down \$800,000 from the year-ago period, mainly due to less favourable wind conditions, which were exceptionally strong last year.

The energy services, storage, and other segment generated adjusted net income of \$1.4 million in the third quarter compared to a net loss of \$100,000 in the same period last year. The \$1.5 million improvement was largely the result of a stark increase in the LNG shipments. As a result of new contracts we more than doubled our Q3 2015 sales volume.

On to slide 12, through the first nine months of fiscal 2016 Gaz Métro invested \$323 million in property, plant, and equipment, in line with our plan, and we remain on track to close the year around \$480 million in CapEx.

On May 24th Gaz Métro Inc. closed a \$100 million private placement of first mortgage bonds. The bonds are secured, bear interest at 1.5 percent per year, and will mature in four years. They were assigned a rating of A and A+ by DBRS and Standard & Poor's, respectively. Proceeds from the private placement were used to pay down part of Gaz Métro's credit facility and for general corporate purposes.

And, as you'll recall from our last call, Gaz Métro and Valener, along with our partner Boralex, completed the \$617.5 million refinancing of Seigneurie de Beaupré Wind Farm 2 and 3 during the third quarter, which allowed for a special distribution of \$80 million to the partner. Gaz Métro and Valener used their combined distribution of \$40 million to pay down debt.

Sophie Brochu, President & Chief Executive Officer, Gaz Métro

Merci, Pierre. Before closing the call I would like to announce that, and you've seen that, that my dear friend and business ally of 20-odd-years, after a career of how many years, Pierre?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

25.

Sophie Brochu, President & Chief Executive Officer, Gaz Métro

25 years at Gaz Métro, has elected to retire. And he has indicated that he wants to retire at the end of 2017. All of us at Gaz Métro are saddened to be losing such an outstanding and admired colleague, and an invaluable member of the team. Actually, for those of you who read Harry Potter, Pierre was something like Dumbledore.

In early 2017, Éric Lachance will be joining us from the Caisse de dépôt et de placement du Québec, where is currently running the Paris office. He is responsible for the oversight of Caisse's infrastructure portfolio in Europe. So for a full year he will be working alongside

Pierre during a transition period expected to last roughly one year. Éric will be named CFO of Gaz Métro at the end of this transition period. Now, we know Éric, Éric knows us. He is no stranger to Gaz Métro. He sat on our company's Board of Directors from 2010 to 2014.

So, like me, you will say that Pierre is much too young. That did not influence him. So we'll have the privilege to be working for a full year on that transition. This is a luxury of a company that is planning its future and its talent just like we're planning our investment.

That concluded the call, operator, and we will now open the line for questions.

QUESTION AND ANSWER SESSION

Operator

Thank you. At this time, if you would like to ask a question, please press star followed by the number one on your telephone keypad. Again, that's star followed by the number one on your telephone keypad.

Your first question comes from the line of Ben Pham from BMO. Please go ahead.

Ben Pham, BMO Capital Markets

Thanks. Good afternoon. Just my first question is on the Addison project and I'm wondering are you very comfortable about the recent cost numbers that you've put out today?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Yeah, when we take that provision in the third quarter this is our best estimate at this moment of the cost to complete the project. There was a hurdle in the process. There is a last remaining domain that, ah, hearings that occurred last week, which is the last parcel of land that we need at a right-of-way to get on that will allow us to complete the project this year. So construction is going well but we had to revisit the cost. So, as of today, this is our best estimate of the cost to complete the project.

Ben Pham, BMO Capital Markets

Okay. And can you remind me the excess above the, what you can recover, how do you plan to finance that? Is that your typical capital structure or is it all equity, all debt?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Yes, the capital structure Vermont Gas is approximately 50 percent debt, 50 percent equity. So the total investment will be funded in the same manner.

Ben Pham, BMO Capital Markets

Okay. And then I wanted to more just check the Hydro acquisition. Presumably that all rate based and you'd have to get approval for that?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Yes.

Ben Pham, BMO Capital Markets

Okay.

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Yeah, this is all rate based. As you know, generation in Vermont can be included in the rate base, so it is pending the approval by the Vermont Public Service Board. That should be obtained, I will say, in the first quarter of 2017.

Ben Pham, BMO Capital Markets

Okay. And can you clarify, I haven't looked in the state for a while, do you need to meet some sort of renewable purchasing target at the utility level?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

In Vermont, yes, there's requirement to purchase, ah, to have those renewable energy credits.

Ben Pham, BMO Capital Markets

Okay. All right. Okay. I'll just get back in the queue and wanted to congratulate you, Pierre, on your retirement. You definitely are way too young to take off but really, ah, (inaudible) my regards. I know you're going to be around for some time but I wanted to congratulate you on that.

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Thank you very much.

Operator

If there are any additional questions at this time, please press star followed by the number one on your telephone keypad.

Your next question comes from the line of Robert Kwan from RBC Capital Markets. Please go ahead.

Robert Kwan, RBC Capital Markets

Good afternoon. If I can start with Vermont Gas and just—what are you booking AFUDC on, at least right here? Are you booking on the actual amount that's been spent or is it some proportion based on how much disallowance you've got?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

No. We were booking AFUDC up until the beginning of this year and it was on the actual amount disbursed to the project. We stopped accounting for AFUDC during the second quarter of the current fiscal year. So until the end of the construction of the project and the inclusion in the rate base, so there is going to be no AFUDC account to the project.

Robert Kwan, RBC Capital Markets

So, Pierre, sorry, to be clear, in the fiscal third quarter there was no AFUDC whatsoever or there was no incremental AFUDC over what you had booked in Q2?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

There was no incremental AFUDC recorded in the third quarter.

Robert Kwan, RBC Capital Markets

Okay. But you still booked the AFUDC on the amount that had been incurred up to third quarter.

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Up to the second quarter of this year.

Robert Kwan, RBC Capital Markets

Sorry, second quarter, correct. Okay. Okay. And just, I guess, turning to QDA, can you just give an update on the GHG credit purchase strategy, where the inventory level might be and how that might be fluctuating just in terms of the balance, the value of the balance?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

We have... Let me get the exact number, and it's in the financial statements. We have approximately \$300 million of greenhouse gas credit and the strategy is to buy for a period in advance. So this is where we are at this point.

Robert Kwan, RBC Capital Markets

Okay. But, put differently, where you are right now there is no expectation... Obviously the value of the credit itself may move this around but in terms of, say, the quantity as you head into fiscal 2017, there should be no major changes here?

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

No major changes. Exactly.

Robert Kwan, RBC Capital Markets

Okay, perfect. And if I can just finish here on the Bécancour project, just the wording that you had in the MD&A, I think I know what you're getting at, but with that being tied up on Hydro-Québec side, you had mentioned or you reiterated that the project or the contract has not been cancelled but, to be clear, the contract, is it contingent though on Hydro-Québec actually getting the approval?

Sophie Brochu, President & Chief Executive Officer, Gaz Métro

Yes, it is contingent on that, and there are various ways to skin that weird cat and we're looking at them right now. And I'm not talking about HQ about the cat, I'm talking about the project. I wouldn't dream about skinning Hydro-Québec. But no, joke apart, we are trying to find a solution. There are a couple of paths going there. I will retrain myself because it involves pretty confidential discussions but we'll see. Next quarter we'll have complete visibility on this one. But we are working hard and this point of time we believe there is a solution to this one.

Robert Kwan, RBC Capital Markets

Perfect. Great. Thank you, Sophie. Thanks, Pierre. And, Pierre, congratulations on your retirement as well.

Pierre Despars, Executive Vice President, Corporate Affairs & Chief Financial Officer, Gaz Métro

Thank you. And, Robert, the exact number you asked me for is \$350 million of credit.

Operator

There are no further questions at this time. I turn the call back over to the presenters.

Sophie Brochu, President & Chief Executive Officer, Gaz Métro

We thank you very much for taking the time with us. We wish you a happy end of the summer. Thank you.

Operator

This concludes today's conference call. You may now disconnect.