

Window of opportunity; up to Buy

- Mispriced, so upgrade to Buy:** The bond-market-led fall in National Grid's share price at the end of 2016 (-16% since July 2016's high) has created an opportunity to buy this robust income stock. We do not believe that the current share price fairly reflects the £4bn net proceeds that National Grid expects to return to shareholders from the sale of its Gas Distribution stake starting in Q2 2017. We expect an 85p (8.9%) special dividend and the launch of a £1bn share buyback programme. The special dividend is incorporated into our £10.50 price target, which we have increased from £9.70. Beyond this event, the shares continue to hold plenty of appeal for income investors. The 4.8% yield may be a little below the sector average but the dividend comes with a promise of RPI-linked dividend growth for the foreseeable future. Our EPS forecasts are on a pre-consolidation basis although we also show what the effects of a consolidation would be.
- Special dividend from gas sale:** National Grid has negotiated a good price for its UK Gas Distribution business. It has agreed to sell a 61% stake to a consortium of long-term infrastructure investors. The £13.8bn price tag (including £1.8bn of new debt) exceeds our prior £12bn valuation and represents a 55% premium to the 2016/17E regulated asset value. The bulk of the net proceeds will be returned to shareholders in Q2 2017 via a special dividend (with accompanying share consolidation) and a share buyback. There is a possibility that the group will sell a further 14% stake to the consortium on similar terms in the future.
- Refocused portfolio offers better growth:** The stake sale also rebalances National Grid's portfolio of regulated businesses. Gas Distribution had reached maturity in terms of capex opportunities. Post-disposal, we should see stronger regulated asset base (RAB) growth, driven by both UK transmission and the group's US operations. We expect a c7% pa CAGR in regulated assets for 2017-20.
- RPI-linked dividend:** RAB growth and improving US returns support National Grid's inflation-linked dividend growth commitment. We think there is scope for dividends to grow at a marginally faster pace than RPI.
- Dollar impact:** The movement in sterling versus the dollar will have a positive translation effect on the group's US EBIT (33% of group in FY16) and increase the sterling-value of the US RAB. However, National Grid also has a large proportion of US-denominated debt, which largely offsets the benefits. US earnings should be further supplemented by RAB growth and gradually improving returns.
- The caveat:** Our economists put a 30% chance on a UK rate rise this year and make a good case as to why currency-induced inflation may be temporary. However, if investors believe that there is more to recent bond market moves than a correction and expect yields to continue to rise, then they should put National Grid on the wait-and-see pile.

Y/E 30/3., GBPm	2014	2015	2016	2017E	2018E
EBITDA	5,080	5,345	5,710	5,892	5,018
EBIT	3,664	3,863	4,096	4,205	3,564
EPS	53.50	57.60	63.50	62.19	60.92
DPS	42.03	42.25	43.16	43.76	45.51
FCF per share	15.2	40.5	37.9	21.6	75.2
Y/E net debt (net cash)	23,775	27,294	28,320	30,643	25,203
EBITDA Growth	1.6%	5.2%	6.8%	3.2%	-14.8%
EPS Growth	4.1%	7.7%	10.2%	-2.1%	-2.0%
DPS Growth	2.9%	0.5%	2.2%	1.4%	4.0%
ROCE	8.1%	8.1%	8.0%	7.9%	7.7%
EV/EBITDA	12.6x	12.2x	11.7x	11.7x	12.5x
P/E	17.7x	16.5x	14.9x	15.3x	15.6x
Dividend Yield	4.4%	4.5%	4.5%	4.6%	4.8%
FCF Yield	1.6%	4.3%	4.0%	2.3%	7.9%

Source: Company data, Berenberg

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19 January 2017

BUY

Current price GBp949
Price target GBp1,050

18/01/2017 London Close

Market cap (GBPm) 35,646
Reuters NG.L
Bloomberg NG/ LN

Changes made in this note

Rating: Buy (Hold)
Price target: GBp1,050 (970)

Estimates changes

	2016		2017E		2018E	
	old	Δ %	old	Δ %	old	Δ %
EBITD	5,622	1.6	4,643	26.9	4,902	2.4
A						
EBIT	4,064	0.8	3,312	27.0	3,499	1.8
EPS	61.02	4.1	54.40	14.3	56.65	7.5

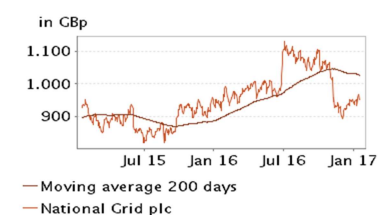
Source: Berenberg estimates

Share data

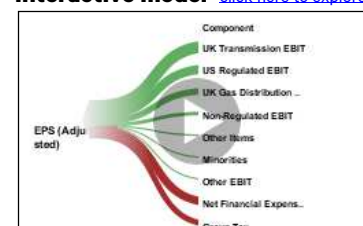
Shares outstanding (m) 3,755
Enterprise value (GBPm) 69,191
Daily trading volume 9,150,000

Key data

Net gearing 231.6%
CAGR EPS 2009-2013 107.4%



Interactive model [click here to explore](#)



* there may be a delay for the new estimates to be updated on the interactive model
[View all interactive models in Utilities](#)

BUY

19 January 2017

Current price **Price target**
GBP949 **GBP1,050**

18/01/2017 London Close

Reuters NG.L
Bloomberg NG/ LN
Market cap (GBPm) 35,646
EV (GBPm) 69,191
Trading volume 9,150,000
Free float 93%

Non-institutional shareholders

None with a holding of more than 3%.

Share performance

High 52 weeks GBP1,131
Low 52 weeks GBP892

Business description

National Grid owns and operates electricity and gas transmission and distribution networks in the UK and North America.

Performance relative to

	SXXP	SX6P
1mth	0.0%	1.4%
3mth	-18.9%	-7.5%
12mth	-10.1%	5.5%

Investment thesis

- National Grid is a fundamentally sound business and it has a few well-flagged catalysts that incrementally add to its attractions (e.g. a Gas Distribution sale and special dividend, and improvements in the US).
- We see little major change on the horizon under new CEO John Pettigrew.
- The group has sold a 61% stake in its UK Gas Distribution business, valuating the entity at an EV of £13.8bn. The majority of cash proceeds will be paid out to shareholders as a special dividend (c85p) with an accompanying share consolidation and a £1bn share buyback.
- Furthermore, we expect the group to continue to deliver on the RPI-linked dividend policy.
- New US rate filings should facilitate a recovery in ROEs, although, cautiously, we assume a pick-up of only 100bp to 8.6% by 2020 (versus 9.1% allowed). We estimate that each 100bp improvement in US ROE adds 3% to EPS.
- Our price target is based on a blend of metrics: a DCF sum-of-the-parts, a dividend discount model, and a target P/E and yield.

Profit and loss summary

GBPm	2014	2015	2016	2017E	2018E
Revenues	14,809	15,201	15,115	16,085	15,164
EBITDA	5,080	5,345	5,710	5,892	5,018
EBITA	3,664	3,863	4,096	4,205	3,564
EBIT	3,664	3,863	4,096	4,205	3,564
Associates contribution	28	46	59	72	292
Net interest	1,015	1,198	1,112	1,212	938
Tax	284	617	438	719	670
Minorities	-12	-8	3	11	11
Net income adj.	2,015	2,189	2,386	2,335	2,236
EPS reported	65.70	53.20	69.00	62.19	129.00
EPS adjusted	53.50	57.60	63.50	62.19	60.92
Year end shares	3,766	3,798	3,755	3,755	3,671
Average shares	3,766	3,798	3,755	3,755	3,671
DPS	42.03	42.25	43.16	43.76	45.51

Cash flow summary

GBPm	2014	2015	2016	2017E	2018E
Net income	2,015	2,189	2,386	2,346	4,746
Depreciation	1,416	1,482	1,614	1,686	1,454
Working capital changes	-59	301	456	24	-23
Other non-cash items	647	1,035	912	456	0
Operating cash flow	4,019	5,007	5,368	4,513	6,178
Capex	-3,445	-3,470	-3,946	-3,700	-3,417
FCFE	574	1,537	1,422	813	2,760
Acquisitions, disposals	0	0	-116	0	4,258
Other investment CF	-2,115	-1,469	-26	0	150
Dividends paid	-1,059	-1,271	-1,337	-1,621	-4,837
Buybacks, issuance	9	16	10	0	-1,065
Change in net debt	-309	-223	8	-5	967
Net debt	23,775	27,294	28,320	30,643	25,203
FCF per share	15.24	40.47	37.87	21.65	75.19

Growth and margins

	2014	2015	2016	2017E	2018E
Revenue growth	3.1%	2.6%	-0.6%	6.4%	-5.7%
EBITDA growth	1.6%	5.2%	6.8%	3.2%	-14.8%
EBIT growth	0.7%	5.4%	6.0%	2.7%	-15.3%
EPS adj growth	4.1%	7.7%	10.2%	-2.1%	-2.0%
FCF growth	1048.0%	167.8%	-7.5%	-42.8%	239.6%
EBITDA margin	34.3%	35.2%	37.8%	36.6%	33.1%
EBIT margin	24.7%	25.4%	27.1%	26.1%	23.5%
Net income margin	13.6%	14.4%	15.8%	14.5%	14.7%
FCF margin	3.9%	10.1%	9.4%	5.1%	18.2%

Key ratios

	2014	2015	2016	2017E	2018E
Net debt / equity	199.5%	227.9%	208.8%	231.6%	255.7%
Net debt / EBITDA	4.7x	5.1x	5.0x	5.2x	5.0x
Avg cost of debt	4.2%	4.7%	4.0%	4.1%	3.4%
Tax rate	22.5%	24.2%	24.0%	23.5%	23.0%
Interest cover	3.6x	3.2x	3.7x	3.5x	3.8x
Payout ratio	78.6%	73.4%	68.0%	70.4%	74.7%
ROCE	8.1%	8.1%	8.0%	7.9%	7.7%
Capex / sales	23.3%	22.8%	26.1%	23.0%	22.5%
Capex / depreciation	243.3%	234.1%	244.5%	219.4%	235.0%

Valuation metrics

	2014	2015	2016	2017E	2018E
P / adjusted EPS	17.7x	16.5x	14.9x	15.3x	15.6x
P / book value	3.0x	3.0x	2.6x	2.7x	3.5x
FCF yield	1.6%	4.3%	4.0%	2.3%	7.9%
Dividend yield	4.4%	4.5%	4.5%	4.6%	4.8%
EV / sales	4.3x	4.3x	4.4x	4.3x	4.2x
EV / EBITDA	12.6x	12.2x	11.7x	11.7x	12.5x
EV / EBIT	17.5x	16.9x	16.3x	16.5x	17.7x
EV / FCF	111.4x	42.4x	47.0x	85.1x	22.8x
EV / cap. employed	1.4x	1.4x	1.3x	1.3x	1.4x

Key risks to our investment thesis

- Political and regulatory intervention in the UK and US
- Failure to deliver on RPI-linked dividend commitment
- Rising interest rates (the adverse valuation effects offsetting any benefits from higher allowed regulatory returns)
- Wall of capex: More capex is good (it drives RAB growth) as long as it is not too concentrated, putting strains on the balance sheet. For this reason, a sharp reversal of the hiatus in UK generation investment and tightening reserve margin remains a risk.

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National Grid – investment thesis

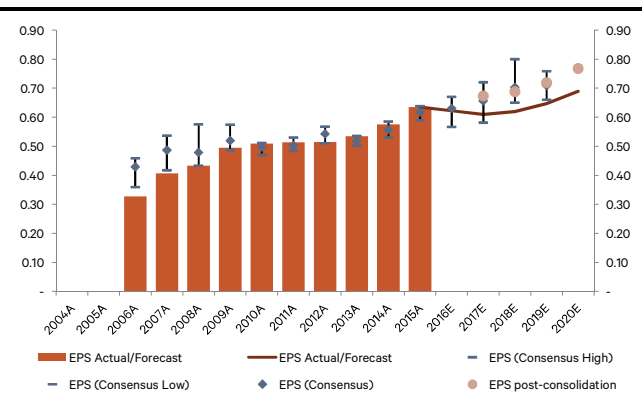
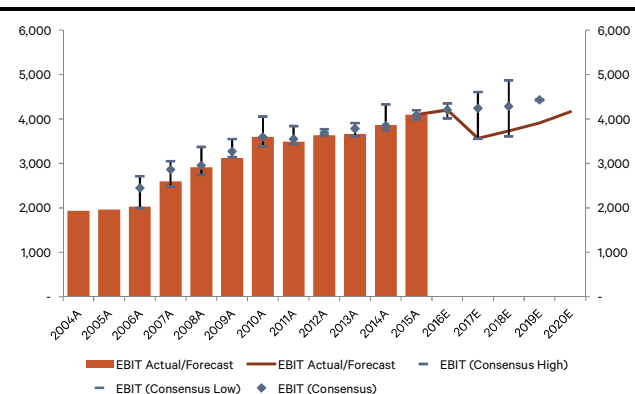
What's new: National Grid has agreed to sell a 61% stake in its Gas Distribution business. We expect a special dividend (with accompanying share consolidation) and share buyback in Q2 2017. Our EPS forecasts are on a pre-consolidation basis although we also show what the effects of a consolidation would be; consensus does not. New US filings should boost ROEs.

Key investment point one: UK Gas Distribution sale nears completion

- **Key statistic:** We expect National Grid to pay an 85p/share special dividend from the lion's share of the net proceeds from its Gas Distribution stake sale. We assume that there will be an accompanying £1bn share buyback and share consolidation, starting in Q2 2017.
- On 8 December 2016, National Grid agreed to sell a 61% stake in its UK Gas Distribution business to a consortium of long-term infrastructure investors (Macquarie Infrastructure and Real Assets, Allianz Capital Partners, Hermes Investment Management, CIC Capital Corporation, Qatar Investment Authority, Dalmore Capital and Amber Infrastructure Limited/International Public Partnerships).
- The £13.8bn enterprise valuation implied by the transaction reflects a £12bn underlying valuation (in line with our estimate), plus a £1.8bn injection from additional debt financing. This effectively values the business at a 55% premium to RAV.
- The bulk (£4bn) of the net cash proceeds (including some of the new debt) will be returned to shareholders via a special dividend (at least 75%) and a share buyback. The c85p special dividend is expected to be paid in Q2 2017. We also expect a share consolidation (10 for 11), which will smooth the impact on earnings.
- Both National Grid and the consortium have expressed an interest in the possibility of a further 14% stake sale, on broadly similar terms, in the future.
- Note, our EPS forecasts are on a pre-consolidation basis although we also show what the effects of a consolidation would be.

Berenberg EBIT estimates versus consensus (consensus does not yet appear to reflect the Gas Distribution sale)...

We show here how there would be little impact on EPS, if we include the share consolidation to accompany the disposal and special DPS (although in the near-term this would distort ratios)



Source: Company reports, Berenberg estimates, Bloomberg

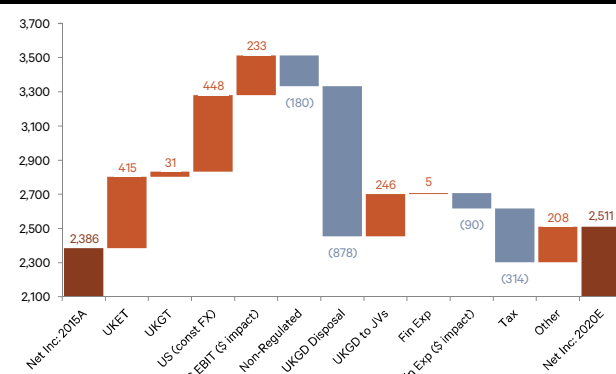
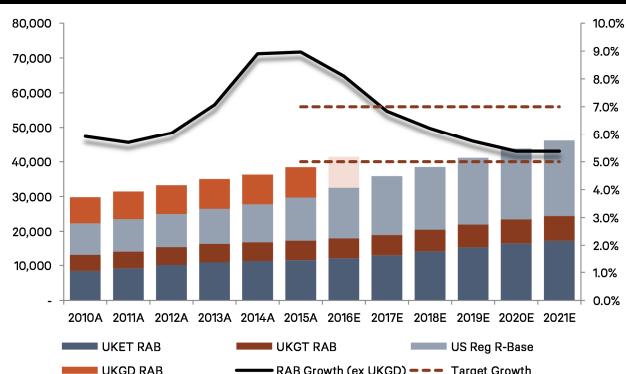
Source: Company reports, Berenberg estimates, Bloomberg

Key investment point two: a faster-growing portfolio, especially in the US

- **Key statistic:** We expect a 7% CAGR (2017-20) in total group regulated assets, with the US business leading the way. We anticipate an underlying growth rate of 7-8% pa from the US, but the RAB, in sterling terms, will receive an extra fillip from currency movements.
- Gas Distribution in the UK had matured in terms of RAB growth opportunities. Disposing of a majority stake frees up capital for management to invest in the faster-growing UK transmission businesses and the US.

We expect growth from all three remaining regulated businesses

Growth in UKET and the US, plus currency movements, drive net income growth



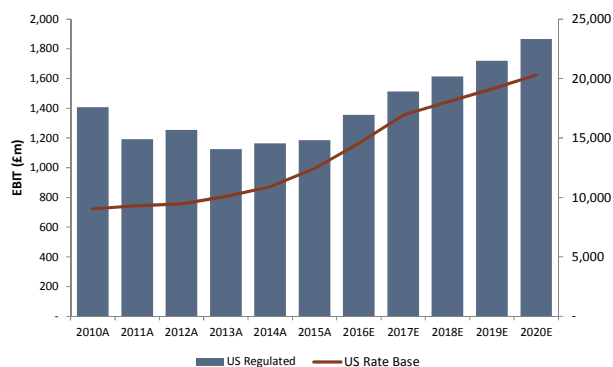
Source: Berenberg estimates

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Key investment point three: currency tailwind and US recovery

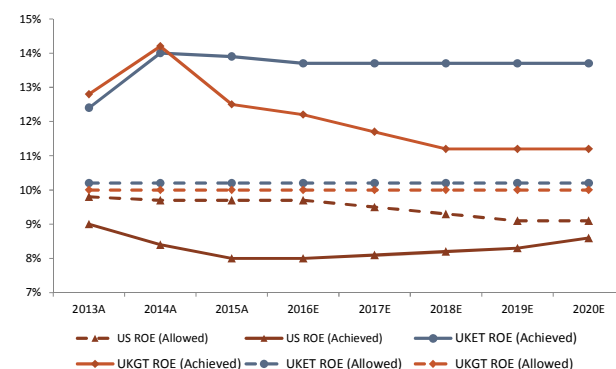
- **Key statistic:** We estimate that every additional 100bp on National Grid's average achieved US ROE is worth +3% EPS.
- A promise of a US recovery is nothing new to the National Grid story. Past achieved returns have been frustratingly low versus allowed levels, most recently due to a self-enforced hiatus in new rate filings while accounting issues were addressed.
- New filings (in Massachusetts and downstate New York) should rectify this. Cautiously, however, we assume a pick-up of only 60bp by 2020/21 versus a forecast 8.0% ROE for FY 2016/17 (ie 8.6% achieved versus 9.1% allowed). We also assume that allowed ROE's decline by 60bp over this period from the current 9.7% (see chart below). However, it is unlikely that achieved ROEs in the US will hit the allowed level due to regulatory lag.
- Sterling's weakness against the dollar will have a positive translation effect on EBIT from the US business (33% of group profit). However, investors should be aware that National Grid has the equivalent of £17bn of US-denominated debt on its balance sheet. This mitigates the currency effects via interest costs and, from a valuation point of view, the associated increase in net debt offsets any rise in the value of the North American business.
- It is too early to tell what Donald Trump's presidency means for the US utility sector as a whole, although it is important to remember that the bulk of National Grid's activities in the country are dictated by state-level regulation, rather than federal policies. It is also feasible that a leaner Trump government could lead to faster decision making on infrastructure projects. Of course, that could simply mean that it says no more quickly.

US EBIT growth driven by currency and rate base growth



Source: Company reports, Berenberg estimates

US business ROE's should recover, although they are likely to stay below a falling allowed level due to the nature of regulation

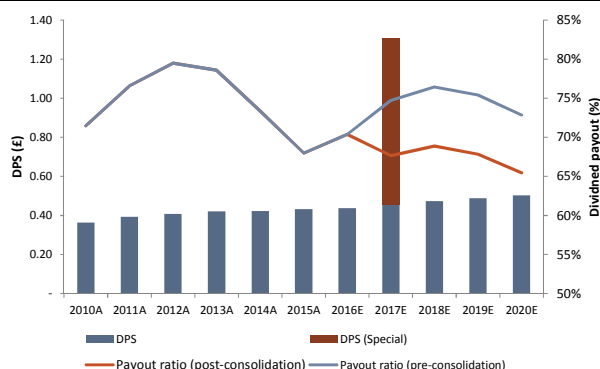


Source: Company reports, Berenberg estimates

Key investment point four: dividend sustainability

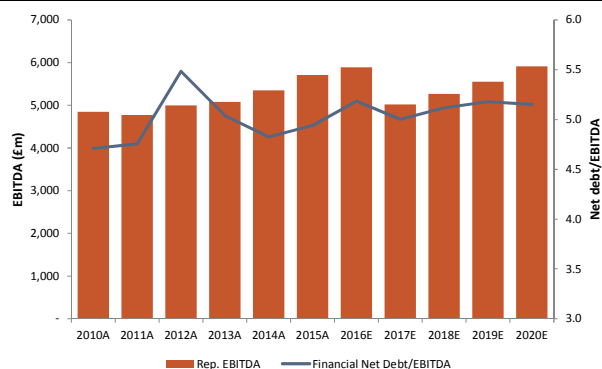
- **Key statistic:** National Grid targets annual growth in its dividend that is at least in line with inflation for the foreseeable future.
- The group's dividend commitment is appealing (certainly in the context of the dividend pitfalls seen in the broader utilities sector) and looks achievable. Of course, the payout ratio and cash cost of dividends will be helped by the share consolidation, which is expected to accompany the distribution of proceeds from the Gas Distribution stake sale.
- In fact, we think there is scope for dividends to grow at a marginally faster pace than RPI.
- A little inflation can help: National Grid's UK business is index-linked. Revenues and regulated assets are adjusted for inflation. Consequently, a little inflation as a result of sterling's fall against the dollar can (eventually) contribute to earnings and dividend growth.

We do not expect the Gas Distribution sale and distribution of proceeds to affect National Grid's underlying DPS growth promise



Source: Company reports, Berenberg estimates

The balance sheet remains robust. 5x net debt/EBITDA is about right for a highly regulated utility



Source: Company reports, Berenberg estimates

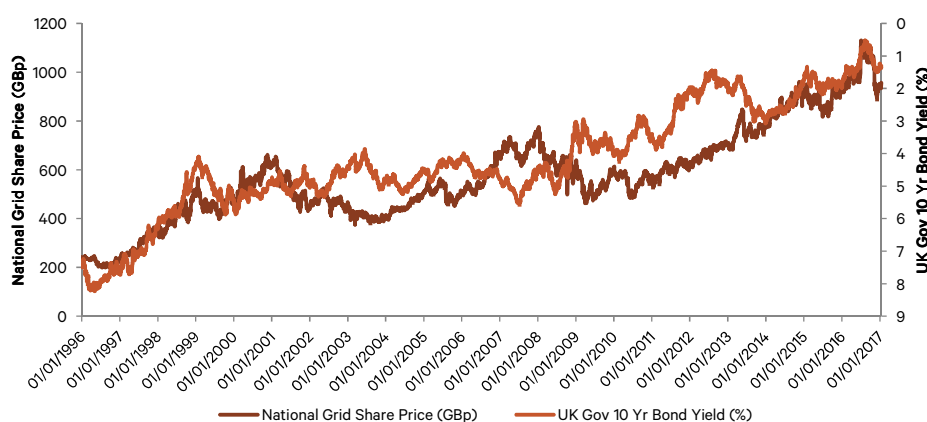
Key investment point five: the caveat – beware rising bond yields

- **Key statistic:** We estimate that a 0.25% increase in the group's post-tax, nominal WACC (of 3.8%) affects our price target by -7%.
- National Grid's share price has been closely linked to medium/long-term bond yields; ever since it was floated in 1995, in fact (see chart below).
- The recent set back in National Grid's share price (16% off its July 2016 high) appears to be largely bond-yield related. UK gilt yields rose (relatively sharply) at the end of 2016 in

anticipation of interest rate hikes, leading to a sharp correction in the valuation of National Grid and its regulated peers.

- Our in-house view is that, although UK inflation is expected to rise due to higher input costs as a consequence of sterling weakness, the effects are likely to be temporary. Our economics team sees only a 30% risk of an interest rate hike later this year. Of course, long-dated bond yields may rise to accommodate higher inflation, even if base rates remain low.
- If investors are convinced that bond yields will continue to rise, then National Grid is probably not the stock for them; it is more one to keep a watchful eye on.

National Grid share price versus UK 10-year government bond yield

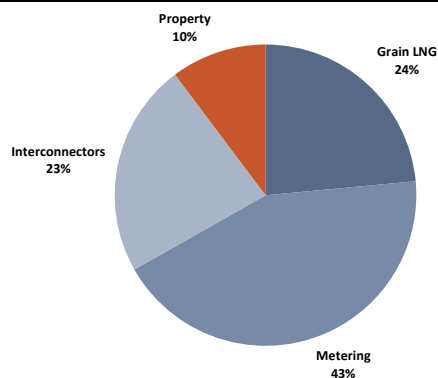


Source: Bloomberg

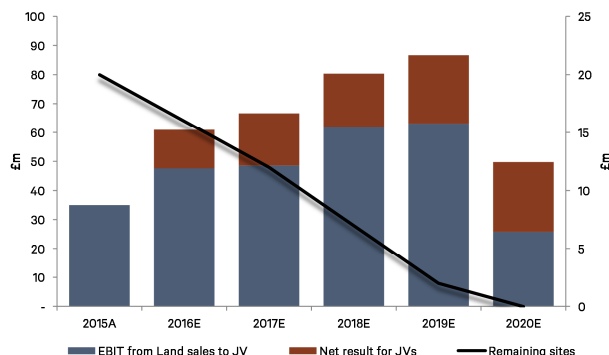
Other key investment points

- **The “Other” activities:** The group’s “Other” activities are often overlooked. They include LNG (liquefied natural gas) and metering, property, US development projects and electricity interconnectors.
 - Following the divestment of the UK Gas Distribution stake, the “Other” activities division will represent c10% of group EBITDA. Importantly, the businesses offer a relatively reliable and growing income stream. The 50/50 St William property development JV with Berkeley Group provides a vehicle for the group to unlock some value from redundant gas and electricity sites. The market-based land valuation was recorded at the time of exchange with the JV, with a 50% gain versus book value booked as EBIT; remaining EBIT will be recognised gradually as units are sold. The operating profit of the property segment (including the share of the St William JV) is expected to grow sustainably, with medium-term performance beyond 2019E reaching 2x current levels. As a consequence, the contribution of JVs will grow. We expect Property profits to tail off thereafter though as the sites are developed and sold.
 - Grain LNG is underpinned by long-term take-or-pay contracts.
 - Interconnectors should benefit from the tight supply-demand balance in the UK and, for that matter, France (while a number of nuclear units are offline). That said, the Brexit vote has cast some doubt over the likelihood of future interconnector projects to increase the links between the UK electricity market and Europe. Of course there are two interconnectors already in use. Furthermore, the UK is short of power and, irrespective of Brexit, needs more interconnection with the European mainland.
 - Metering has performed solidly over the last three years, supported by a sharp focus on efficiency and investment. National Grid is exploring participation in rolling out smart meters as a logical extension to its existing UK metering activities. It hopes to benefit from experience, financing and customer feedback, and has already started a pilot with a mid-level energy supplier.

EBITDA split of “Other” activities 2016-17E (excluding JV contribution for Property and interconnectors)



We expect Property profits to tail off by 2020E as the sites are developed and sold



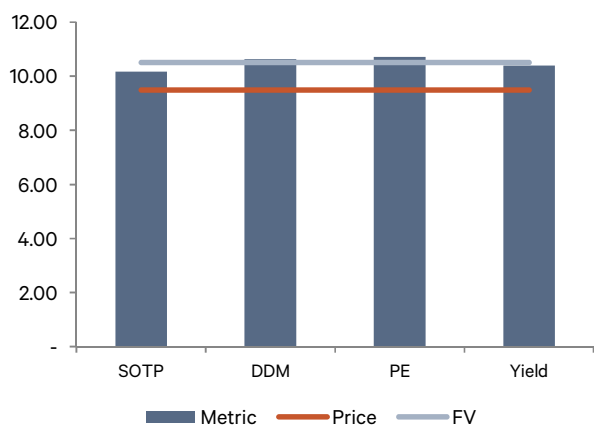
Source: Company reports, Berenberg estimates

- Compromise on Systems Operator role:** National Grid and energy regulator Ofgem have hopefully found a solution to the distracting debate over the group’s role as UK electricity system operator. In recent years, there have been calls for the group to divest this relatively small part of its business due to concerns over a perceived conflict of interest with its ownership of electricity market infrastructure (including interconnectors). The compromise is for greater separation of the activities. National Grid will move its Systems Operator activities into a new wholly owned subsidiary.

Valuation and sensitivity analysis

- We value the shares using a blend of metrics: a DCF-based sum-of-the-parts, dividend discount model, target yield and target P/E.
- Our blended price target is £10.50 per share (%11 upside). This offers a total shareholder return of +16%. Our price target includes a c85p (9%) special dividend from the sale proceeds of the UK Gas Distribution stake and is stated before the expected accompanying 10 for 11 share consolidation.
- National Grid's 2017-20 EPS growth is 4% versus the sector's 6%, while its 2017E P/E (adjusting for the share consolidation) is 15.6x, a 10% premium to the sector. However, we note that the group's highly regulated earnings stream is relatively less risky than the broader sector. In addition, the shares trade more or less in line with the regulated sub-sector. DPS CAGR 2017-20 is 3% compared to the sector's 4% although, again, the risks to the dividend are relatively lower.

Valuation metrics (£/share; pre-share consolidation)



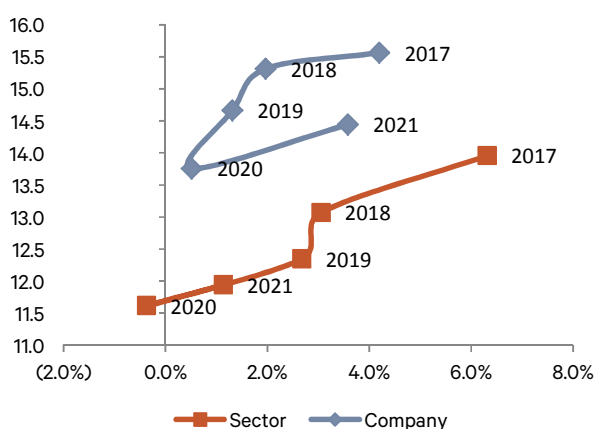
Source: Berenberg estimates

SOTP valuation (£/share; pre-share consolidation)

	Value	£/Share	2017 EV/ EBITDA	Method
UK Transmission	28,292	7.53	11.9	+57% RAV
UK Gas Distribution	-	-	-	-
US Regulated	21,413	5.70	9.9	DCF
Non-Regulated	4,726	1.26	9.5	DCF
Other	5,783	1.54	-	JV (inc GD)
Enterprise Value	60,214	16.04	12.0	
Debt	(25,097)	(6.68)	(5.0)	2017E
Provisions	(2,995)	(0.80)	(0.6)	2017E
Other	2,892	0.77	0.6	2017E
Minorities	(10)	(0.00)	(0.0)	2017E
Liabilities	(25,210)	(6.71)	(5.0)	
Equity	35,004	9.32		
NOSH	3,755			2016E
Equity per Share	9.32			
Special Dividend	0.85			
Sum of the Parts	10.17			

Source: Berenberg estimates

P/E versus EPS three-year CAGR (pre-share consolidation)



Source: Berenberg estimates using three-year forward EPS CAGR

Dividend yield versus DPS three-year CAGR (pre-share consolidation)

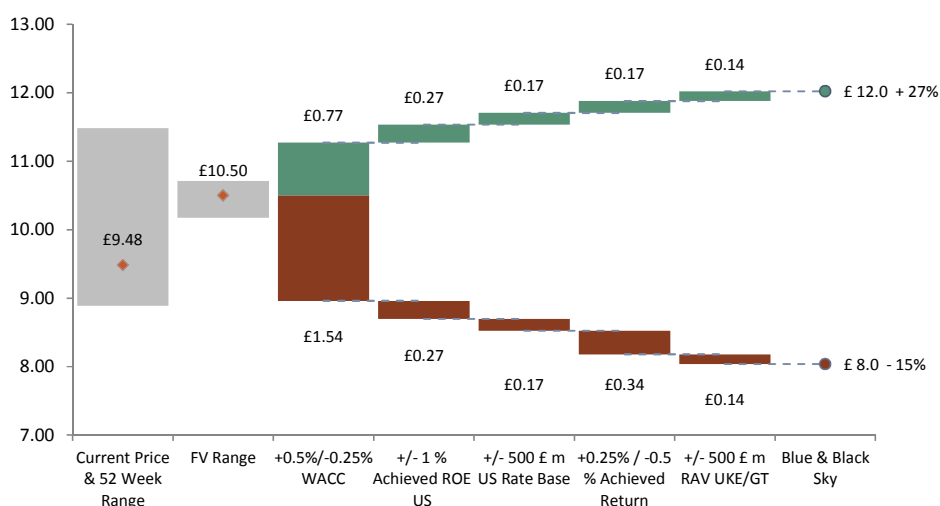


Source: Berenberg estimates using three-year forward DPS CAGR

Black-sky/blue-sky scenario

Our black-sky/blue-sky price target range is £8.0-£12.0 per share. Our blue-sky valuation gives 27% upside from current levels and our black-sky valuation gives -15% downside.

Price target black-sky/ blue-sky scenario (€/share)



Source: Berenberg estimates

Black-sky/blue-sky scenario assumptions

Driver	Bull €/share	Bear €/share	Assumptions
Base Case Valuation	10.5	10.5	
+0.5%/-0.25% WACC	0.8	(1.5)	Post-tax WACC 3.8%
+/- 1% Achieved ROE US	0.3	(0.3)	UKET 13.7%; UKGT 11.7%
+/- 500 £ m US Rate Base	0.2	(0.2)	ROE 8.2%
+0.25% / -0.5 % Achieved Return	0.2	(0.3)	Rate base £17bn
+/- 500 £ m RAV UKE/GT	0.1	(0.1)	RAV £19bn
Blue & Black Sky Valuation	12.0	8.0	
Upside/(Downside) from share price	27%	(15%)	

Source: Berenberg estimates

Changes to numbers: Berenberg versus consensus

Estimate changes

Estimate Changes	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
EBITDA (New - as reported; £ m)	5,080	5,345	5,710	5,892	5,018	5,269	5,551	5,911
EBITDA (Old - as reported; £ m)	5,080	5,345	5,622	4,643	4,902	5,173	5,487	5,899
Change	+0%	+0%	+2%	+27%	+2%	+2%	+1%	+0%
EBIT (New - as reported; £ m)	3,664	3,863	4,096	4,205	3,564	3,730	3,911	4,165
EBIT (Old - as reported; £ m)	3,664	3,863	4,064	3,312	3,499	3,693	3,913	4,225
Change	+0%	+0%	+1%	+27%	+2%	+1%	-0%	-1%
EPS (New - as reported; £)	0.54	0.58	0.64	0.62	0.61	0.62	0.65	0.69
EPS (Old - as reported; £)	0.54	0.58	0.61	0.54	0.57	0.60	0.63	0.69
Change	+0%	-1%	+4%	+14%	+8%	+4%	+2%	+0%
DPS (New - as reported; £)	0.42	0.42	0.43	0.44	0.46	0.47	0.49	0.50
DPS (Old - as reported; £)	0.42	0.43	0.43	0.44	0.45	0.47	0.48	0.49
Change	+0%	-1%	-0%	-1%	+0%	+1%	+2%	+2%

Source: Berenberg

Berenberg versus consensus

Berenberg Forecasts vs Consensus	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
EBITDA* (£ m)	5,080	5,345	5,710	5,892	5,018	5,269	5,551	5,911
Consensus (Average)	5,213	5,349	5,644	5,645	5,734	5,850	6,439	#N/A
Berenberg +/- vs Cons	-3%	-0%	+1%	+4%	-12%	-10%	-14%	#N/A
EBIT* (£ m)	3,664	3,863	4,096	4,205	3,564	3,730	3,911	4,165
Consensus (Average)	3,780	3,851	4,085	4,202	4,242	4,282	4,428	#N/A
Berenberg +/- vs Cons	-3%	+0%	+0%	+0%	-16%	-13%	-12%	#N/A
Net Income* (£ m)	2,015	2,189	2,386	2,335	2,236	2,256	2,356	2,511
Consensus (Average)	1,921	2,096	2,333	2,510	2,354	2,403	2,503	#N/A
Berenberg +/- vs Cons	+5%	+4%	+2%	-7%	-5%	-6%	-6%	#N/A
EPS* (£)	0.54	0.58	0.64	0.62	0.61	0.62	0.65	0.69
Consensus (Average)	0.52	0.56	0.62	0.63	0.66	0.70	0.71	#N/A
Berenberg +/- vs Cons	+3%	+3%	+3%	-1%	-7%	-12%	-9%	#N/A
EPS (post-consolidation)* (£)					0.67	0.69	0.72	0.77
Consensus (Average)					0.66	0.70	0.71	#N/A
Berenberg +/- vs Cons					+3%	-2%	+1%	#N/A
DPS (£)	0.42	0.42	0.43	0.44	0.46	0.47	0.49	0.50
Consensus (Average)	0.42	0.43	0.44	0.44	0.46	0.47	0.49	#N/A
Berenberg +/- vs Cons	-0%	-2%	-1%	-1%	-0%	-0%	-1%	#N/A

* Based on company's definition of metric

Source: Berenberg estimates, Bloomberg

Sensitivity analysis

Sensitivity analysis

Sensitivities	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
EBITDA Sensitivity* to								
+/- 1 % Achieved Return UKET	2.1%	2.1%	2.1%	2.1%	2.6%	2.7%	2.8%	2.8%
+/- 1 % Achieved Return UKGT	1.1%	1.0%	1.0%	1.0%	1.2%	1.2%	1.2%	1.2%
+/- 1 % Achieved Return UKGD	1.7%	1.6%	1.5%	1.5%	0.0%	0.0%	0.0%	0.0%
+/- 1 % Achieved ROE US	0.9%	1.0%	1.1%	1.2%	1.6%	1.7%	1.7%	1.7%
+/- 1000 £ m RAV UKE/GT	2.4%	2.5%	2.3%	2.2%	2.5%	2.3%	2.1%	2.0%
+/- 1000 £ m RAV UKGD	2.7%	2.4%	2.4%	0.0%	0.0%	0.0%	0.0%	0.0%
+/- 1000 £ m US Rate Base	3.0%	2.8%	2.4%	2.3%	2.5%	2.4%	2.4%	2.3%
+/- 1 % UK Growth	0.4%	0.4%	0.4%	0.4%	0.5%	0.5%	0.5%	0.5%
+/- 1 % US Growth	0.2%	0.2%	0.2%	0.2%	0.3%	0.3%	0.3%	0.3%
+/- 10 % USDGBP currency move	3.0%	3.0%	3.0%	3.3%	4.3%	4.4%	4.5%	4.6%
Net Income Sensitivity* to								
+/- 1 % Achieved Return UKET	4.1%	3.9%	3.7%	4.0%	4.4%	4.8%	4.9%	5.0%
+/- 1 % Achieved Return UKGT	2.1%	1.9%	1.8%	1.8%	2.0%	2.1%	2.1%	2.1%
+/- 1 % Achieved Return UKGD	3.2%	3.0%	2.8%	2.9%	0.0%	0.0%	0.0%	0.0%
+/- 1 % Achieved ROE US	1.8%	1.8%	1.9%	2.3%	2.8%	2.9%	3.0%	3.0%
+/- 1000 £ m RAV UKE/GT	3.2%	3.2%	3.0%	3.4%	3.4%	3.2%	3.0%	2.8%
+/- 1000 £ m RAV UKGD	3.8%	3.2%	3.2%	0.0%	0.0%	0.0%	0.0%	0.0%
+/- 1000 £ m US Rate Base	4.3%	3.8%	3.3%	3.6%	3.5%	3.5%	3.4%	3.3%
+/- 1 % UK Growth	0.7%	0.7%	0.7%	0.7%	0.8%	0.8%	0.8%	0.8%
+/- 1 % US Growth	0.3%	0.3%	0.4%	0.4%	0.5%	0.5%	0.6%	0.5%
+/- 10 % USDGBP currency move	3.9%	3.5%	3.7%	4.3%	5.7%	6.0%	6.2%	6.4%

* Ceteris Paribus; e.g. does not take account of hedged positions.

Source: Berenberg

Key assumptions

Key assumptions

Power Price Forecasts		2014A	2015A	2016E	2017E	2018E	2019E	2020E
Country	Unit							
UK (Local)	£/MWh	47.0	47.0	43.1	46.2	50.6	51.3	51.0
UK (EUR)	EUR/MWh	58.5	62.1	54.2	54.1	58.9	59.0	57.9
Germany	EUR/MWh	35.0	30.5	27.0	27.8	29.8	27.8	29.5
Nordic	EUR/MWh	33.1	32.8	22.0	27.5	25.0	23.7	23.5
Italy	EUR/MWh	52.9	46.0	40.8	41.3	45.7	45.2	45.3
Benelux	EUR/MWh	47.0	40.0	32.0	32.8	34.8	33.0	32.6
France	EUR/MWh	47.0	38.0	32.0	34.9	37.0	36.9	37.0
Spain/Portugal	EUR/MWh	47.0	47.0	43.0	44.0	45.7	42.9	43.7

Fuel Price Forecasts		2014A	2015A	2016E	2017E	2018E	2019E	2020E
Fuel	Unit							
Oil (Brent)	\$/bbl	101.9	53.5	53.5	59.7	59.1	59.1	59.1
Coal	\$/t	78.3	53.3	49.5	57.5	63.0	58.0	58.0
Gas (Europe LTC)	EUR/MWh	26.4	21.9	13.6	14.9	17.9	18.2	17.7
Gas (Italy)	EUR/MWh	23.2	20.0	12.4	13.7	16.4	16.6	16.2
Gas (UK) £	£/MWh	14.1	12.0	9.3	10.8	13.1	13.4	13.2
Carbon UK floor	£/t	14.3	20.0	22.0	22.7	23.0	23.1	23.2
US Gas Henry Hub	\$/MWh	14.7	8.7	29.6	11.9	10.0	9.7	9.9
Uranium	EUR/MWh	8.5	8.5	8.5	8.5	8.5	8.5	8.5
Carbon	EUR/t	6.0	7.8	5.5	5.5	5.9	5.9	5.9

Year end currency rates	2014A	2015A	2016E	2017E	2018E	2019E	2020E
EURGBP	0.78	0.74	0.85	0.85	0.86	0.87	0.89
EURTRY	2.83	3.17	3.70	4.16	4.68	5.23	5.85
EURSEK	9.44	9.17	9.57	9.52	9.52	9.58	9.70
EURUSD	1.21	1.09	1.05	1.06	1.09	1.12	1.15
EURRUB	73.50	80.00	64.72	68.86	74.83	80.39	86.10
EURMXN	17.84	18.75	21.81	23.17	25.07	27.12	29.29
USDBRL	2.66	4.00	3.26	3.56	3.80	4.06	4.35

Inflation	2014A	2015A	2016E	2017E	2018E	2019E	2020E
Central Europe	0.8%	0.1%	0.4%	1.6%	1.7%	1.7%	1.7%
Eastern Europe	5.8%	9.0%	6.1%	4.8%	4.6%	4.6%	4.6%
UK	1.5%	0.1%	0.6%	2.5%	2.4%	2.4%	2.4%
Nordic	0.5%	-0.2%	0.7%	1.4%	1.6%	1.6%	1.6%
Spain/Portugal	-0.2%	-0.1%	0.2%	1.2%	1.5%	1.5%	1.5%
US	1.6%	0.1%	1.3%	2.3%	2.4%	2.4%	2.4%

Source: Berenberg

Financials

Income statement

Income Statement (£ m)	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Revenue	14,809	15,201	15,115	16,085	15,164	15,772	16,429	17,301
Reported EBITDA	5,080	5,345	5,710	5,892	5,018	5,269	5,551	5,911
Change	+2%	+5%	+7%	+3%	-15%	+5%	+5%	+6%
Margin	+34%	+35%	+38%	+37%	+33%	+33%	+34%	+34%
Depreciation	(1,416)	(1,482)	(1,614)	(1,686)	(1,454)	(1,538)	(1,640)	(1,746)
Other OPEX	-	-	-	-	-	-	-	-
Reported EBIT	3,664	3,863	4,096	4,205	3,564	3,730	3,911	4,165
Change	+1%	+5%	+6%	+3%	-15%	+5%	+5%	+6%
Margin	+25%	+25%	+27%	+26%	+24%	+24%	+24%	+24%
Net Financial Expenses	(1,015)	(1,198)	(1,112)	(1,212)	(938)	(1,088)	(1,144)	(1,197)
Tax	(284)	(617)	(438)	(719)	(670)	(676)	(706)	(752)
Other	(362)	133	(157)	72	292	300	305	305
Minorities	12	8	(3)	(1)	(1)	(1)	(1)	(1)
Reported Net Income	2,015	2,189	2,386	2,335	2,236	2,256	2,356	2,511
Change	+5%	+9%	+9%	-2%	-4%	+1%	+4%	+7%
Margin	+14%	+14%	+16%	+15%	+15%	+14%	+14%	+15%
Number of Shares	3,766	3,798	3,755	3,755	3,671	3,643	3,643	3,643
Per Share:								
Basic EPS	0.66	0.53	0.69	0.62	1.29	0.62	0.65	0.69
Change	+14%	-19%	+30%	-10%	+107%	-52%	+4%	+7%
Reported EPS	0.54	0.58	0.64	0.62	0.61	0.62	0.65	0.69
Change	+4%	+8%	+10%	-2%	-2%	+2%	+4%	+7%
EPS post share consolidation					0.67	0.69	0.72	0.77
Change						+2%	+5%	+7%
DPS	0.42	0.42	0.43	0.44	0.46	0.47	0.49	0.50
Change	+3%	+1%	+2%	+1%	+4%	+4%	+3%	+3%
Payout	79%	73%	68%	70%	75%	76%	75%	73%
DPS Special	0.00	0.00	0.00	0.00	0.85	0.00	0.00	0.00

Source: Berenberg

Divisional EBITDA

UK Transmission (£ m)	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Revenue	4,328	4,776	5,024	5,281	5,377	5,583	5,845	6,262
Change	+2%	+10%	+5%	+5%	+2%	+4%	+5%	+7%
% Group	+29%	+31%	+33%	+33%	+35%	+35%	+36%	+36%
EBITDA	2,019	2,222	2,227	2,333	2,368	2,459	2,584	2,782
Change	-2%	+10%	+0%	+5%	+2%	+4%	+5%	+8%
Margin	+47%	+47%	+44%	+44%	+44%	+44%	+44%	+44%
% Group	+40%	+42%	+39%	+40%	+47%	+47%	+47%	+47%
EBIT	1,504	1,674	1,659	1,751	1,769	1,843	1,938	2,106
Change	-5%	+11%	-1%	+6%	+1%	+4%	+5%	+9%
Margin	+35%	+35%	+33%	+33%	+33%	+33%	+33%	+34%
% Group	+41%	+43%	+41%	+42%	+50%	+49%	+50%	+51%

UK Gas Distribution (£ m)	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Revenue	1,898	1,867	1,918	1,914	-	-	-	-
Change	+11%	-2%	+3%	-0%	-100%	+0%	+0%	+0%
% Group	+13%	+12%	+13%	+12%	+0%	+0%	+0%	+0%
EBITDA	1,175	1,112	1,176	1,124	-	-	-	-
Change	+11%	-5%	+6%	-4%	-100%	+0%	+0%	+0%
Margin	+62%	+60%	+61%	+59%	+0%	+0%	+0%	+0%
% Group	+23%	+21%	+21%	+19%	+0%	+0%	+0%	+0%
EBIT	904	826	878	817	-	-	-	-
Change	+14%	-9%	+6%	-7%	-100%	+0%	+0%	+0%
Margin	+48%	+44%	+46%	+43%	+0%	+0%	+0%	+0%
% Group	+25%	+21%	+21%	+19%	+0%	+0%	+0%	+0%

US Regulated (£ m)	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Revenue	8,040	7,986	7,493	8,255	9,137	9,558	9,995	10,558
Change	+2%	-1%	-6%	+10%	+11%	+5%	+5%	+6%
% Group	+54%	+53%	+50%	+51%	+60%	+61%	+61%	+61%
EBITDA	1,544	1,616	1,720	1,939	2,153	2,319	2,495	2,714
Change	-8%	+5%	+6%	+13%	+11%	+8%	+8%	+9%
Margin	+19%	+20%	+23%	+23%	+24%	+24%	+25%	+26%
% Group	+30%	+30%	+30%	+33%	+43%	+44%	+45%	+46%
EBIT	1,125	1,164	1,185	1,356	1,513	1,614	1,720	1,865
Change	-10%	+3%	+2%	+14%	+12%	+7%	+7%	+8%
Margin	+14%	+15%	+16%	+16%	+17%	+17%	+17%	+18%
% Group	+31%	+30%	+29%	+32%	+42%	+43%	+44%	+45%

Non-Regulated (£ m)	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Revenue	736	762	876	845	846	835	803	705
Change	+9%	+4%	+15%	-4%	+0%	-1%	-4%	-12%
% Group	+5%	+5%	+6%	+5%	+6%	+5%	+5%	+4%
EBITDA	342	395	587	496	497	490	472	414
Change	+78%	+15%	+49%	-15%	+0%	-1%	-4%	-12%
Margin	+46%	+52%	+67%	+59%	+59%	+59%	+59%	+59%
% Group	+7%	+7%	+10%	+8%	+10%	+9%	+8%	+7%
EBIT	131	199	374	282	281	273	253	194
Change	+1091%	+52%	+88%	-25%	-0%	-3%	-7%	-23%
Margin	+18%	+26%	+43%	+33%	+33%	+33%	+32%	+28%
% Group	+4%	+5%	+9%	+7%	+8%	+7%	+6%	+5%

Source: Berenberg

EBIT breakdown

EBIT Breakdown	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Rep. EBIT	3,664	3,863	4,096	4,205	3,564	3,730	3,911	4,165
change (%)	+1%	+5%	+6%	+3%	-15%	+5%	+5%	+6%
margin (%)	+25%	+25%	+27%	+26%	+24%	+24%	+24%	+24%
UK Transmission	1,504	1,674	1,659	1,751	1,769	1,843	1,938	2,106
Electricity	1,087	1,237	1,173	1,248	1,272	1,346	1,428	1,588
Gas	417	437	486	502	497	497	510	517
UK Gas Distribution	904	826	878	817	-	-	-	-
US Regulated	1,125	1,164	1,185	1,356	1,513	1,614	1,720	1,865
Non-Regulated	131	199	374	282	281	273	253	194

Source: Berenberg

Cash flow statement

Cash Flow (£ m)	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Net Income	2,015	2,189	2,386	2,346	4,746	2,267	2,367	2,522
Depreciation	1,416	1,482	1,614	1,686	1,454	1,538	1,640	1,746
Working Capital	(59)	301	456	24	(23)	15	16	22
Other Operating Cash Flow	647	1,035	912	456	-	-	-	-
Operating Cash Flow	4,019	5,007	5,368	4,513	6,178	3,820	4,023	4,289
CAPEX	(3,445)	(3,470)	(3,946)	(3,700)	(3,417)	(4,204)	(4,358)	(4,516)
FCF (Post CAPEX)	574	1,537	1,422	813	2,760	(384)	(335)	(227)
Acquisitions and Disposals	-	-	(116)	-	4,258	-	-	-
FCF (p. CAPEX, Aq&D)	574	1,537	1,306	813	7,018	(384)	(335)	(227)
Other Investment Cash Flow	2,115	1,469	26	-	(150)	-	-	-
Dividends	(1,059)	(1,271)	(1,337)	(1,621)	(4,837)	(1,671)	(1,724)	(1,776)
FCF (p. CAPEX, Aq&D, Divs)	1,630	1,735	(5)	(808)	2,031	(2,054)	(2,059)	(2,003)
Buybacks and Equity Issuance	9	16	10	-	(1,065)	-	-	-
Borrowings	(1,058)	(1,296)	1,830	803	-	1,088	2,059	2,003
Other Financing, Disc and FX	(890)	(678)	(1,827)	-	-	-	-	-
Net Change in Group Cash	(309)	(223)	8	(5)	967	(967)	-	-

Source: Berenberg

Balance sheet statement

Balance Sheet (£ m)	2013/14A	2014/15A	2015/16A	2016/17E	2017/18E	2018/19E	2019/20E	2020/21E
Intangible Fixed Assets	5,263	5,947	6,202	6,202	6,202	6,202	6,202	6,202
PP&E	37,179	40,723	43,364	45,378	34,199	36,865	39,582	42,353
Other Non-Current Assets	2,453	2,388	3,056	3,056	5,396	5,396	5,396	5,396
Total Non-Current Assets	44,895	49,058	52,622	54,636	45,797	48,463	51,180	53,951
Inventories and Receivables	3,123	3,176	2,909	3,096	2,918	3,035	3,162	3,330
Cash	354	119	127	119	1,086	119	119	119
Other Liquid Assets	-	-	-	-	-	-	-	-
Other Current Assets	4,012	2,736	3,276	3,276	3,276	3,276	3,276	3,276
Assets Held for Sale	-	-	-	-	-	-	-	-
Total Current Assets	7,489	6,031	6,312	6,491	7,280	6,430	6,557	6,725
Total Assets	52,384	55,089	58,934	61,126	53,077	54,893	57,737	60,675
Short-Term Debt	(3,511)	(3,028)	(3,611)	(3,608)	(3,608)	(3,608)	(3,608)	(3,608)
Payables	(3,031)	(3,292)	(3,285)	(3,496)	(3,296)	(3,428)	(3,571)	(3,760)
Provisions	(282)	(235)	(236)	(236)	(236)	(236)	(236)	(236)
o/w Nuclear Liabilities	-	-	-	-	-	-	-	-
o/w Pensions	-	-	-	-	-	-	-	-
o/w Other Provisions	(282)	(235)	(236)	(236)	(236)	(236)	(236)	(236)
Other Current Liabilities	(507)	(819)	(589)	(589)	(589)	(589)	(589)	(589)
Liabilities of Businesses Held for Sale	-	-	-	-	-	-	-	-
Total Current Liabilities	(7,331)	(7,374)	(7,721)	(7,929)	(7,729)	(7,861)	(8,004)	(8,193)
Long-Term Debt	(22,439)	(22,882)	(24,733)	(27,051)	(22,578)	(23,473)	(25,257)	(26,957)
Provisions	(3,948)	(4,879)	(4,478)	(4,478)	(4,478)	(4,478)	(4,478)	(4,478)
o/w Nuclear Liabilities	-	-	-	-	-	-	-	-
o/w Pensions	(2,585)	(3,379)	(2,995)	(2,995)	(2,995)	(2,995)	(2,995)	(2,995)
o/w Other Provisions	(1,363)	(1,500)	(1,483)	(1,483)	(1,483)	(1,483)	(1,483)	(1,483)
Other Non-Current Liabilities	(6,747)	(7,980)	(8,437)	(8,437)	(8,437)	(8,437)	(8,437)	(8,437)
Total Non-Current Liabilities	(33,134)	(35,741)	(37,648)	(39,966)	(35,493)	(36,388)	(38,172)	(39,872)
Shareholders' Equity	(11,911)	(11,962)	(13,555)	(13,222)	(9,846)	(10,634)	(11,551)	(12,601)
Minorities	(8)	(12)	(10)	(10)	(10)	(10)	(10)	(10)
Total Equity	(11,919)	(11,974)	(13,565)	(13,232)	(9,856)	(10,644)	(11,561)	(12,611)
Total Liabilities and Equity	(52,384)	(55,089)	(58,934)	(61,126)	(53,077)	(54,893)	(57,737)	(60,675)
Net Debt (As Reported)	21,190	23,915	25,325	27,648	22,208	24,070	25,854	27,554
Economic Net Debt	23,775	27,294	28,320	30,643	25,203	27,065	28,849	30,549
Net Debt / EBITDA (As Reported)	4.2	4.5	4.4	4.7	4.4	4.6	4.7	4.7
Economic Net Debt / EBITDA	4.7	5.1	5.0	5.2	5.0	5.1	5.2	5.2

Source: Berenberg

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Production of the recommendation completed: 19.01.2017, 18:03

Historical price target and rating changes for National Grid plc in the last 12 months

Date	Price target - GBP	Rating	First dissemination GMT	Initiation of coverage
<u>12 May 16</u>	<u>970.00</u>	<u>Hold</u>	<u>2016-05-13 07:04</u>	<u>06 March 12</u>
<u>19 January 17</u>	<u>1050.00</u>	<u>Buy</u>	-	

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