

CONSOLIDATED INTERIM FINANCIAL REPORT
30 SEPTEMBER 2016
TERNA GROUP

2016

Transmitting energy



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Highlights - Performance 9M 2016

Performance of Terna stock and shareholder return

€4.59/share*

Price at
30 September 2016

€5.08/share*

Maximum share price,
reached on 30 March 2016

* Closing price

Economic, financial and equity performance

(Amounts in € millions) vs 9M2015



REVENUE

1,551.0
+2.3%



EBITDA

1,176.3
+1.3%



GROUP NET PROFIT

486.8
+7.0%



INVESTMENTS

530.2
(-24.5%)



NET FINANCIAL DEBT

7,800.9
(-2.5%)*

* comparative figure 31/12/2015

Operating performance

Commissioning of "Sorgente-Rizziconi" power line



- This represents the longest 380 kV AC undersea electrical connection in the world
- Significant reduction in the price spread between Sicily and the Southern market zone
- Savings of around € 600 million a year expected for the electricity system
- Reduction of 700,000 tonnes of CO₂ emissions into the atmosphere each year
- 114 km of old power lines dismantled and over 200 hectares benefiting from a lower environmental impact

Commissioning of "Villanova-Gissi" power line



- Increased transfer capacity for renewables of 700 MW
- Reduction of 165,000 tonnes of CO₂ emissions into the atmosphere each year
- Improvement of energy deficit in Abruzzo
- Benefits for the security and efficiency of the system, savings for families and businesses

Italy-France Interconnection



- Issue of decree of exemption by MED for the private line

Introduction

This **Consolidated Interim Financial Report of the Terna Group at 30 September 2016**, not subject to independent auditing, has been prepared voluntarily in accordance with the provisions (regarding implementation of the new EU Directive on Transparency (Directive 2013/50/EU)), of Italian Legislative Decree no. 25 of 15 February 2016 (the “Decree”), which removed the obligation to publish interim financial statements on the part of listed companies, delegating to CONSOB the task of evaluating the possible reintroduction of the obligation to publish “*additional periodic financial information*” with the limits and conditions set out in the said Decree.

Pending the application of the new comprehensive regulatory framework, Terna saw fit to publish, in keeping with past practice, this Report at 30 September 2016.

Significant events in the third quarter of 2016

Interconnections abroad

On **20 July 2016** the Ministry of Economic Development (hereinafter the MED) issued the “Decree of exemption for the private line of the interconnection power line” in favour of the company **Piemonte Savoia S.r.l.** The exemption, lasting ten years, concerns (i) the rules on the right of access of third parties, (ii) the regulations on the management of income deriving from the assignment of interconnection capacity, (iii) the tariff regulations and (iv) the regulations relating to ownership unbundling. The document was sent to the European Commission for the necessary approval.

International activities

In line with the targets of the 2016–2019 Strategic Plan, which provides for a maximum amount of € 200 million, Terna is exploring business opportunities in the area of international activities.

In Europe, in **July 2016** Terna manifested its interest in participating in the tender for privatisation of 24% of the **Greek TSO**. On **21 October 2016** Terna, in a joint venture with F2i SGR S.p.A., presented a binding purchase offer. Please see, on this point, the paragraph “Events subsequent to 30 September 2016”.

In **September 2016** Terna was been **awarded in Uruguay** the tender by UTE – a vertically integrated, state-owned company which manages the generation, transmission, distribution and sale of electricity – for the construction of three new electricity infrastructures in the country.

More specifically, Terna will create a 500 kV line, 213 km long, from Melo to Tacuarembó, to increase the efficiency and security of the national electricity grid in Uruguay, to promote energy diversification, and to support the integration of renewable production in the north of the country (wind and biomass in particular). Furthermore, another two lines will be created to connect to the pre-existing transmission system, for a combined length of 10.5 km. Once the tender results are formalised, Terna will have 24 months to construct and commission the three power lines. The total value of the contract, calculated on a thirty-year basis, is estimated by UTE at \$ 230 million.

Sustainability

Terna won the **Safety Prize awarded by Confindustria and INAIL** with the official patronage of the President of the Republic, which was consigned on **20 July 2016** in the presence of the Chairperson of Confindustria. The 4th edition of the “Companies Safety Prize”, awarded by Confindustria and INAIL with the technical collaboration of APQI (*Associazione Premio Qualità Italia* - Italy Quality Prize Association)

and Accredia (the Italian Accreditation Body) was intended to reward companies that have distinguished themselves for commitment in the field of health and safety management, as a useful example for highlighting and sharing their experiences to raise the awareness of other companies and workers on legislative, cultural, organisational and behavioural aspects. Among the most significant assessment parameters, Terna was rewarded for the degree of maturity reached in adopting the most effective best practices at the international level on the subject of safety.

On 9 September 2016 the annual review of the Swiss sustainability rating agency RobecoSAM confirmed for the eighth consecutive year the presence of **Terna among the top positions in the prestigious Dow Jones Sustainability World Index**. The inclusion is particularly significant because only 6 Italian companies are confirmed in the index. The Group scored **97/100 for the environmental component, up three points from 2015**, placing it at the top of the Electric Utilities sector. The result for the economic component is also up three points. This component evaluates the quality of management and aspects such as Risk Management, anti-corruption activities, management of the supply chain and the application of the principle of materiality, where Terna achieved the maximum possible score. The newly-introduced materiality criterion recognises the coherence of Terna's sustainability approach, from identification of the areas most closely connected to the creation of value, to their management through dedicated policies and instruments, including executive compensation.

On 21 September 2016, Terna obtained a further recognition for sustainability with **confirmation**, for the sixth consecutive year, **in the STOXX Global ESG Leaders Indices**. Terna is present in these indices created by the company STOXX Limited which, on the basis of sustainability performance, selects 345 companies among the 1,800 stocks present in the initial international basket, the STOXX Global 1800 Index. In particular, to obtain access to or confirmation in the ESG Leaders indices, a company must stand out in at least one of the three areas of analysis – environmental, social and governance – for inclusion in the related index, the STOXX Global Environmental Leaders, the STOXX Global Social Leaders or the STOXX Global ESG Governance Leaders.

Thanks to the excellent performance in all areas of analysis, Terna has been confirmed in all three indices. There are a total of 5 Italian companies, and 8 utilities at the global level that can boast the same result, and there are only 14 Italian companies, including Terna, in the STOXX Global ESG Leaders.

Finance

On 26 July 2016, Terna agreed a back-up Revolving Credit Facility, in the form of a “committed” line (the “Revolving Credit Facility” or “Facility”), for a total amount of € 500 million, with a pool of banks including Banca IMI, BNP Paribas, Bank of Tokyo - Mitsubishi, Caixa Bank and UniCredit serving as Joint Mandated Lead Arrangers and Bookrunners. The Revolving Credit Facility will have a duration of 5 years and the amount available will be usable throughout the duration of the loan with prior notification. The interest rate is linked to the EURIBOR plus a margin between 0.70% and 1.10% (based on the portion used).

Organisation and Business

The Terna Group and its mission

The main business of the Terna Group is the transmission and dispatching of electricity in Italy, playing the role of TSO (Transmission System Operator), in a monopoly position through government concession. Terna manages all its activities focusing on their possible economic, social and environmental consequences and adopts a sustainable approach to business to create, maintain and consolidate a relationship of mutual trust with its stakeholders, needed for value creation for the Company and for the stakeholders themselves.

The business lines that characterise the activities and organisation of the Terna Group are presented below:

Regulated Activities – Electricity dispatching and transmission in Italy

The Terna group owns 99.6% of the Italian National Transmission Grid.

It is the largest independent transmission system operator in Europe and among the leaders in the world in terms of kilometres of lines managed (more than 72 thousand km).

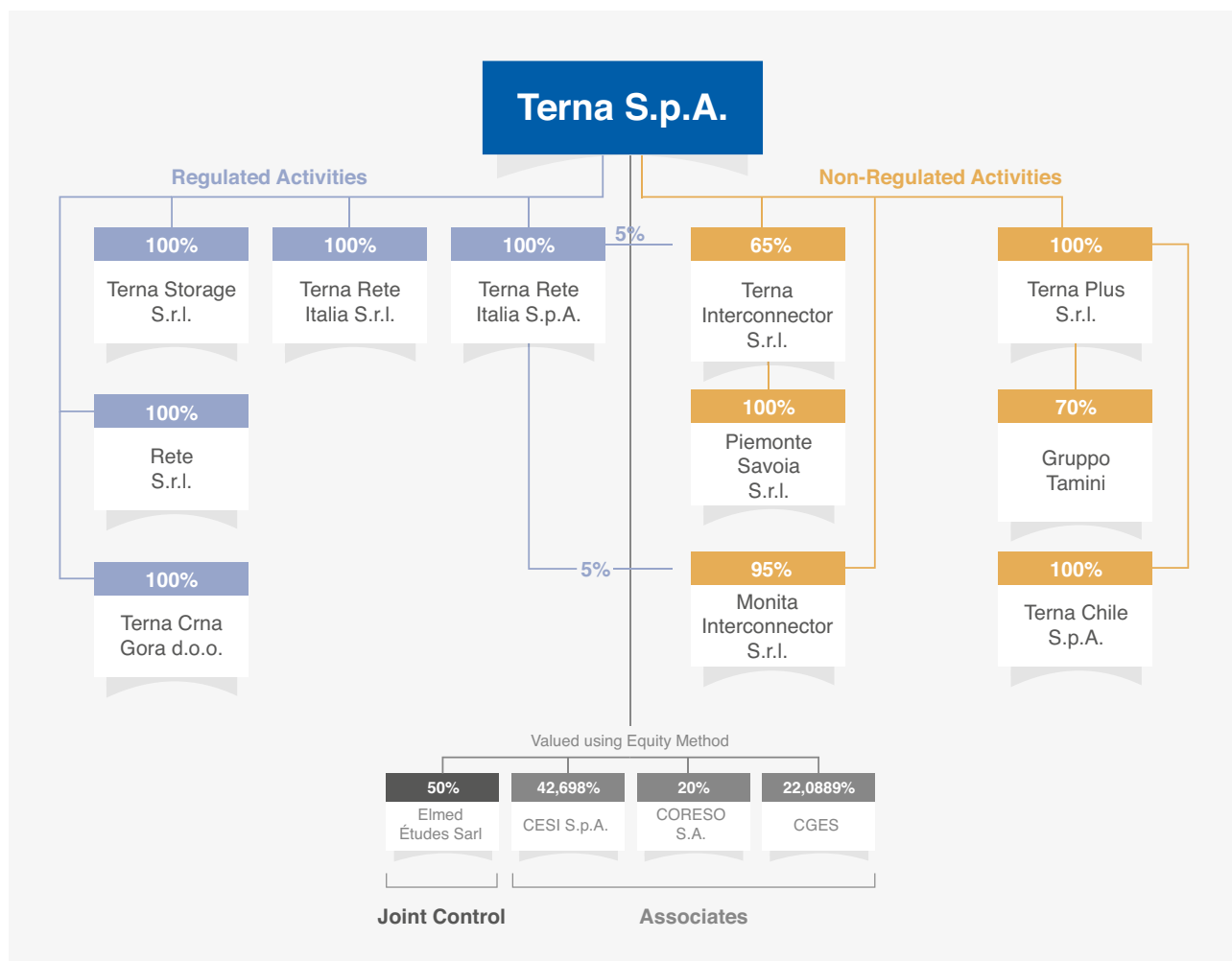
It is responsible for the transmission and management of power flows on the High-Voltage and Very-High-Voltage Grid throughout the national territory, in order to maintain the balance between demand and supply of energy (dispatching). It is also responsible for the planning, construction and maintenance of the grid. It acts as the Italian TSO in accordance with the regulations of the Italian Regulatory Authority for Electricity, Gas and Water (hereinafter AEEGSI) and the guidelines of the MED. It ensures the security, quality and cost efficiency of the national electricity system and pursues the development of the grid and its integration with the European grid. It ensures equal conditions of access for all grid users.

Non-Regulated Activities – New business opportunities in Italy and abroad

The Terna Group offers products and services linked to infrastructural activities under the national or foreign market system or under foreign regulatory authorities, pursuing new business opportunities with its experience, technical expertise and ability to innovate, all gained managing complex systems.

Corporate structure

The corporate structure of the Terna Group at 30 September 2016 is shown below.



During the first nine months of 2016, there were no events that would have had effects on the Terna Group's organisational structure, which therefore reflects the situation at 31 December 2015.

THE PARENT COMPANY

Terna S.p.A.

Holds the government concession for the transmission and dispatching of electricity and 80.13% of the NTG (considering the portions held by the subsidiaries Terna Rete Italia S.r.l. and Rete S.r.l., detailed below, the Group holds 99.6% of the NTG). Owns the infrastructures and is responsible for defining the NTG Development Plan and its Defence Plan.

SUBSIDIARIES OPERATING IN REGULATED ACTIVITIES

Company	Activity
Terna Rete Italia S.p.A.	Carries out all traditional operating activities, ordinary and extraordinary maintenance, the management and performance of work on developing the NTG.
Terna Rete Italia S.r.l.	Owner of 10.75% of the NTG infrastructures.
Rete S.r.l.	Owner of 8.71% of the NTG infrastructures; it was acquired during 2015 from Gruppo Ferrovie dello Stato Italiane (FSI Group).
Terna Storage S.r.l.	Design and creation of diffused energy storage systems.
Terna Crna Gora d.o.o.	Company founded under Montenegro law that manages the activities relating to the development and management of the Italy-Montenegro Interconnection in the territory of Montenegro.

SUBSIDIARIES OPERATING IN NON-REGULATED ACTIVITIES

Company	Activity
Terna Interconnector S.r.l.	Development and creation of the private infrastructures for interconnection between Italy and France.
Piemonte Savoia S.r.l.	Owner of the private Italy-France Interconnection under construction, to be operated under the Interconnector system, as provided for in Italian Law 99/2009.
Monita Interconnector S.r.l.	Vehicle for the development of the private Italy-Balkans Interconnection and management of the Interconnector system (Italian Law 99/2009).
Terna Plus S.r.l.	Development of new activities and business opportunities on the Italian Non-Regulated market and construction and management of High-Voltage infrastructures in Italy and abroad.
Tamini Group	The Group operates in the production and sale of industrial and power electricity transformers using six manufacturing facilities, all situated in Italy, in Legnano, Melegnano, Novara, Valdagno, Ospitaletto and Rodengo.
Terna Chile S.p.A.	Chilean-law company that manages the activities related to the planning, construction and maintenance of electrical infrastructures, including those for interconnection.

ASSOCIATES OR COMPANIES UNDER JOINT CONTROL

Company	Activity
CESI S.p.A.	Pure and applied research for progress in the electrotechnical, energy, electronic and information technology sectors.
CORESO S.A.	Belgian-law company that manages the preparation of daily forecasts and real-time analyses of energy flows in Central and Western Europe, identifying possible critical issues and duly informing the TSOs concerned in a timely manner. The shareholding structure includes Terna the operators of France (RTE), Belgium (Elia) and Great Britain (National Grid), with 20% each, and the German operator, 50Hertz Transmission, with 10%.
CGES (Crnogorsk Elektroprenosmi Sistem Ad)	TSO of the Montenegro electricity market. Investment purchased under the scope of the Italy-Balkans Interconnection project.
Elmed Etudes Sarl	Entity under joint control together with the Tunisian company STEG for the creation of studies preparatory to the construction of the works necessary for connection between the Tunisian electricity grid and the Italian one.

Reference context

Energy context

Electricity demand and production in Italy

During the first nine months of 2016, electricity demand in Italy dropped by 3.4% compared to the same period of 2015. In the period January-September 2016, in fact, demand for electricity in Italy amounted to 230,481 million kWh (provisional data), compared to the 238,669 million kWh of the comparative period.

ELECTRICITY BALANCE SHEET FOR ITALY, GWh

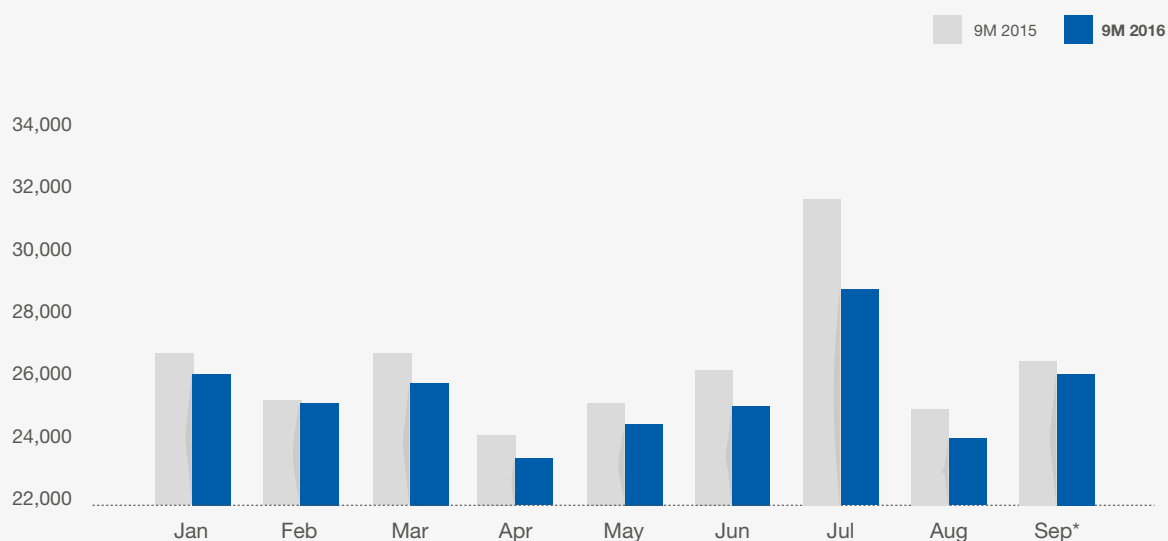
	9M 2016*	9M 2015	Δ	Δ %
Net production** (national production)	200,610	207,129	(6,519)	(3.1%)
From foreign suppliers (imports)	36,227	36,579	(352)	(1.0%)
Sold to foreign clients (exports)	(4,701)	(3,676)	1,025	27.9%
For pumping***	(1,655)	(1,363)	292	21.4%
Total demand in Italy	230,481	238,669	(8,188)	(3.4%)

* Provisional data

** Does not include the demand for energy related to services auxiliary to electricity production activity.

*** Electricity used for lifting water by pumps, for the sole purpose of being used subsequently for electricity production

MONTHLY ELECTRICITY DEMAND IN 2016, GWh



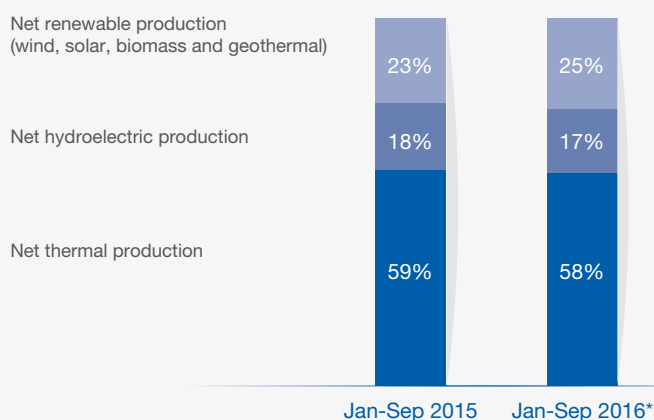
* Provisional data

The monthly trend of electricity demand in Italy in the first nine months of 2016 shows a reduction in all months of the period, compared to the same month of the previous year.

ELECTRICITY PRODUCTION ACCORDING TO TYPE OF SOURCE

In the first nine months of 2016, renewable sources covered approximately 36% of the total energy demand, substantially in line with the same period of 2015. A slight reduction was recorded in Photovoltaic production offset by an increase in wind power production. Hydroelectric production, also to be considered a Renewable source, was substantially unchanged.

ITALIAN NET PRODUCTION BY SOURCE



* Provisional data

Energy prices and Exchanges with other countries

Energy prices

The average hourly price on the Italian energy exchange (IPEX¹/SNP – Single National Price) for the first nine months of 2016 was 38 €/MWh, sharply down (-27%) compared to that recorded in the same period of 2015 (52 €/MWh). The SNP is formed on the Day Ahead Market (DAM) as the balancing price between demand and supply of electricity. A driver of the price formation is also the status of the electricity grid: the more this is developed and becomes capillary, the more it will make it possible to withdraw and transport energy at more competitive prices. It needs to be stated in addition that a sharp reduction in the price of commodities also contributed to keeping the SNP at minimum levels; this ensured that numerous traditional plants became more competitive.

We can note, in addition, that with the new Sorgente-Rizziconi connection, the spread of the electricity purchase prices between Sicily and the SOUTH market zone recorded a significant reduction compared to past years.

Exchanges with Foreign Countries

In the first nine months of 2016, foreign trade recorded net imports down by 2.6 TWh compared to the same period of the previous year (-8% YoY). This reduction is attributable to the sharp increase in Exports and more efficient management of the interconnection capacity due to ever-increasing integration of the

(1) IPEX: Italian Power Exchange.

European electricity market (for example Market Coupling).

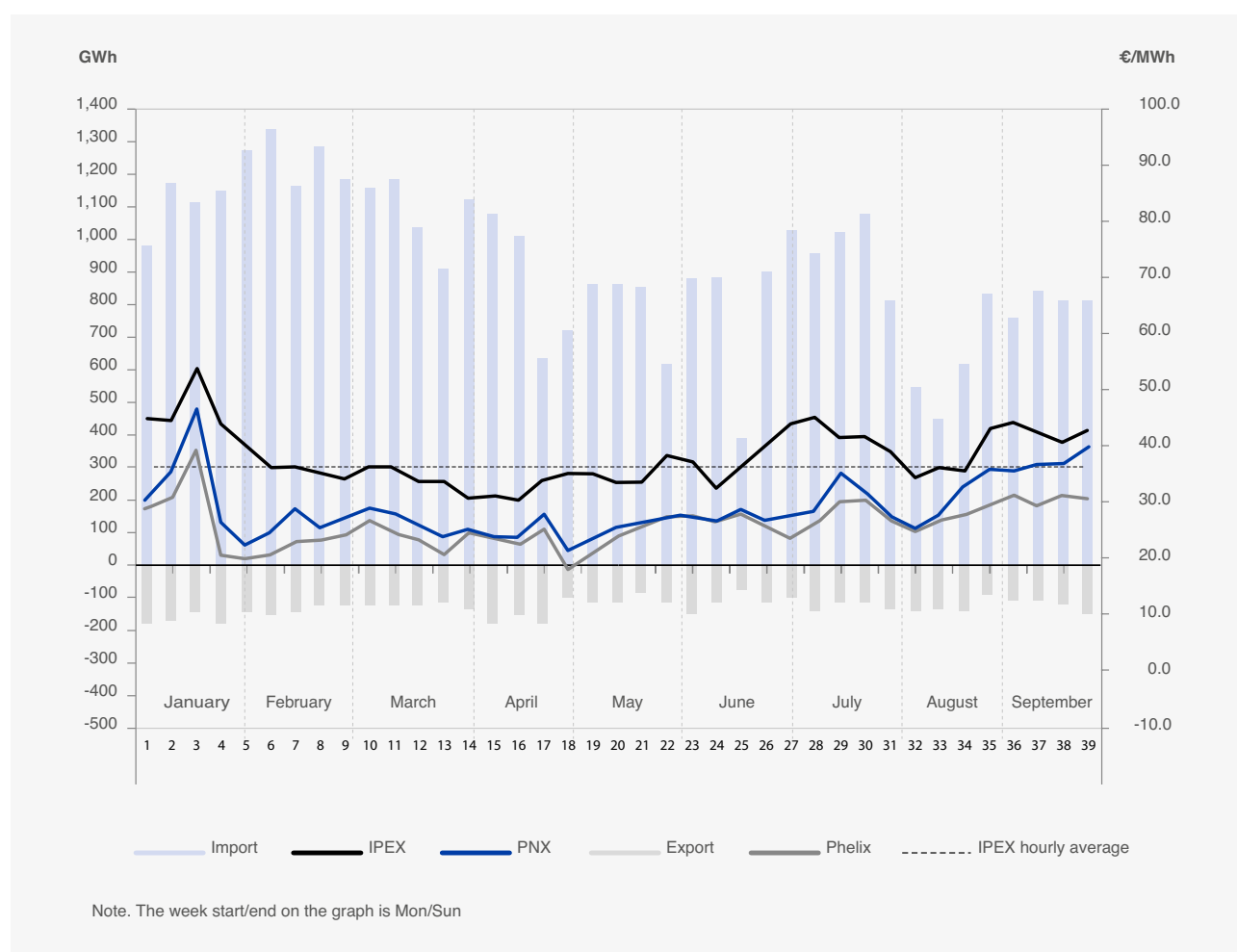
The Single National Price is still on average higher than the prices of the French (PNX) and German (EEX/ PHELIX) foreign exchanges, although the spread continues to decline owing to the gradual alignment of the SNP with the foreign securities:

- the price on the French power exchange (PNX) was € 29/MWh (-23% YoY);
- the price on the German power exchange (EEX/PHELIX) was €26/MWh (-16% yoy).

As a consequence, the spread between the IPEX/SNP and the French exchange fell by approximately 5 €/MWh, going down from 14 to 9 €/MWh, while the spread with the German exchange decreased by approximately 9 €/MWh, going down from 21 to 12 €/MWh.

The difference in price of the exchanges is justified by the different generation plants, characterised in Italy by higher production costs, hence the prevalence of import trade.

COMMERCIAL EXCHANGES AND WEEKLY AVERAGE PRICES OF ENERGY IN THE FIRST NINE MONTHS OF 2016:



Regulatory context

The Authority, with reference to multi-annual regulation periods, establishes the structure and parameters for determining the revenue, and updates the tariffs to take into account the evolution of the invested capital and the cost base. More specifically, the **price for the transmission service** accounts for most of the regulated revenue (92.4%) and is calculated as the sum of the three components below.

Component	Description
Remuneration of the investment	<p><i>Regulated Asset Base x Weighted Average Cost of Capital (WACC)</i></p> <p>The RAB (recognised invested capital) basically represents the regulatory value of Terna's assets. The recognised invested capital is subject to annual updating, primarily based on net investments, disposals, and the deflator of gross fixed investments.</p> <p>The WACC² considers the expected return on the risk-based capital component, the cost of debt and the proportion of these two components. In turn, the expected return of the risk capital component depends on the level of the risk-free rate, on the risk premium of the equity market of reference and on the specific risk level of the single service compared to that of the equity market of reference (beta).</p>
Cover of depreciation and amortisation	Depreciation and amortisation recognised on assets.
Covering of operating expenses	Operating expenses recognised.

New tariff system 2016-2023 for the Terna Group

With Resolutions no. 583/15/R/com, no. 653/15/R/eel, no. 654/15/R/eel and no. 658/15/R/eel, the AEEGSI set the tariff regulation for the 2016–2023 regulation period for electricity transmission, distribution, measurement and dispatching and the regulation regarding the quality of the transmission service, for which you are referred to the detailed description provided in the Interim Financial Report at 30 June 2016.

Social context

The most significant element of the social context, in relation to Terna's business, regards a generalised opposition with regard to the construction of new infrastructures in the territory, expressed by the populations of the areas involved and often identified by the expression "NIMBY (Not In My Backyard) syndrome". The opposition arises from people's strong sensitivity to defending their territorial – residential, rural – areas which translates, in the case of electrical infrastructures, into rejecting any work which would entail, in the opinion of the opponents, visual damage to the landscape and consequently loss of value of the properties nearby. The opposition is fuelled by certain imprecise notions on the role of Terna, whose mission of general interest is sometimes not known or is intentionally distorted by the Opposition Committees, and fears associated with the effects of electromagnetic fields on health. Finally, the purposes of security and functioning of the electrical service which Terna represents in the general interest – even if known and recognised – are not considered relevant with respect to the objective of protecting people's specific territory, owing also to

(2) For the period 2016-2018 the WACC for the transmission service is set at 5.3%.

the clash between benefits of a general nature and local impact. The role played by Terna in the electricity system is instead considered with interest by those who - like the main environmentalist associations, in their central structures - express concern over the effects of climate change, sustain the need for a rapid transition to the production of energy from renewable sources and see the development of the transmission grid and smart technology as a factor able to allow for this energy transition both in Italy and worldwide. In the same way, the production sector is normally oriented positively in relation to Terna owing to the effects of efficiency and lower cost of the electrical service related to development of the grid.

Legislative context

The regulatory environment of Terna is shown in detail in the Annexes – “Regulatory Framework” and “AEEGSI Resolutions”.

Strategy

2016-2019 Strategic Plan

On **17 February 2016**, Terna approved the Strategic Plan for 2016–2019. In light of the new regulatory framework and the evolution of the market context, the Plan concentrates on reinforcing the core business, on improving operating efficiency, on Non-Regulated Activities in Italy, and on developing internationally. More specifically, the strategic initiatives identified regard:

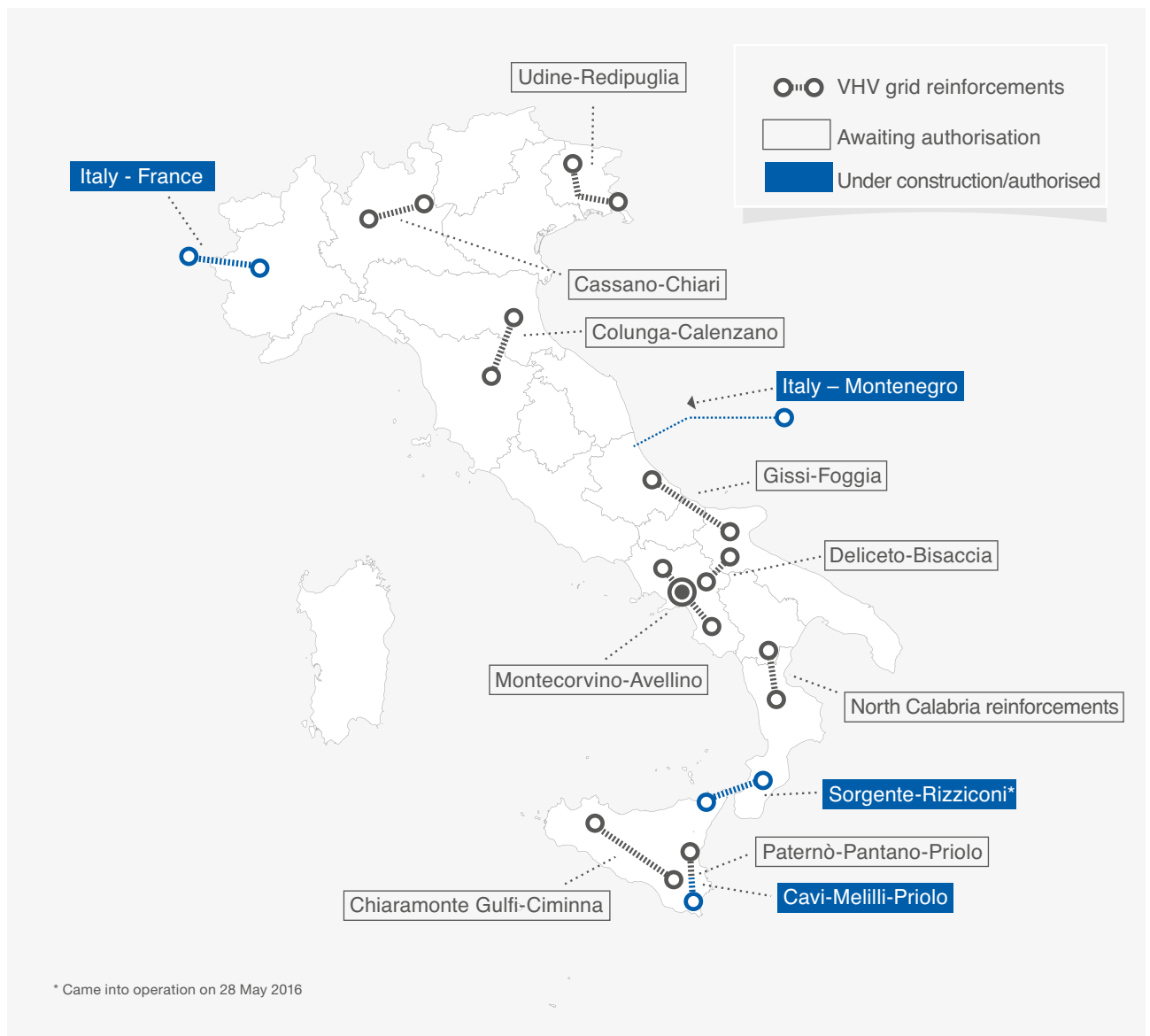
- in terms of **Regulated Activities in Italy**, the increased commitment to developing the National Electricity Grid (as described in the paragraph “2016 Development Plan” below) and the integration of the High-Voltage grid acquired from the FSI Group during 2015;
- the promotion of new business under the scope of **Non-Regulated Activities, in Italy and abroad**;
- the identification of **international opportunities in regulated areas**, coherent with the Group’s current risk profile;
- the increase in **operating efficiency**, the improvement of the processes and the rationalisation of external costs;
- **technological innovation** and supporting research for solutions in support of environmental sustainability and the development of storage systems;
- **improving the Free Cash Flow** and maintaining a solid financial structure, also with a view to the new dividend policy (+3% over the period of the Plan).

2016 Development Plan

The 2016 Development Plan includes investments for nearly € 6.6 billion, thanks to which the electricity system will be made more efficient, with further significant advantages such as:

- reduction of energy losses of 1.6 billion kilowatt-hours per year;
- reduction of CO₂ emissions of approximately 15 million tonnes/year;
- reduction of congestions for an amount of more than 5,000MW;
- greater overall foreign exchange capacity, estimated at more than 6,000 MW;
- greater power capacity generated by renewable sources of around 5,500 MW.

Implementing Directive 2009/28/EC and the National Action Plan (NAP) prepared by MED in 2010, Terna included a specific section in the National Development Plan which defines the action needed for full use of the energy deriving from the production of renewable systems. The grid analyses carried out in order to facilitate the use and development of production from renewable sources have enabled us to identify action to be taken both on the primary 380-220kV transmission grid, and on the 150-132kV High-Voltage grid. Below is a figure showing an overview of the main development work carried out on the 380 kV Very-High-Voltage grid:



Capital

In its role as the reference operator for the Italian electricity system, Terna generates significant benefits for the entire electricity sector. These objectives are pursued by transforming the capital that the Group holds into actions that focus on reaching these objectives, based on governance strategies and systems, in the context of both Regulated Activities and Non-Regulated Activities.

Capital



Infrastructural

NTG, production plants and other physical capital available (means of transport, equipment, etc.).



Financial

Funding sources that are available for use in the provision of services and goods.



Human

Skills, abilities, experience and motivation to innovate human resources.



Intellectual

Patents and intangible assets based on technical, technological and specialist knowledge and on processes.



Objectives

Continuity of the electricity service

Maximise the availability of the national electricity service

Security of the electricity service

Minimize the vulnerability of the NTG to internal or external events

Costs of the electricity service

Contribute through development of the NTG and optimisation of its management to reduce energy costs

Economic results

Produce satisfactory economic results continuously

Sustainability

Build good relations with stakeholders, minimizing the environmental footprint, ensuring adequate allocation of intangible capital over time

Infrastructural capital

The main changes in the dimensions of the Terna S.p.A. and Terna Rete Italia S.r.l. plants at 30 September 2016 are illustrated below, compared to the situation at the end of June 2016. The dimensions of Rete S.r.l. underwent no changes.

Terna S.p.A.

The dimensions of Terna S.p.A. recorded overall a decrease of 1 substation, 1 bay and 1 three-phase power line which corresponds to 38.8 km of three-phase power line, as described below:

Substations

- definitive decommissioning of the Martinetto (TO) 132 kV substation, which consisted of 4 132 kV bays;
- activation of 3 bays in the substations of Patria (NA), Castelnuovo (SA) and Melfi (PZ).

Power lines

- activation of the new 132 kV Cedegolo Sud - S. Fiorano cable power line, 1.3 km of three-phase power line;
- deactivation and/or demolition of 1.33 three-phase power lines for a total of 42.6 km, of which: 2 three-phase power lines and 17.3 km at 220 kV, 1 three-phase power line and 25.3 km at 132 kV.
- construction of variants and/or route changes with an overall increase of 2.5 km of three-phase power line, of which: + 4.4 km at 220 kV, - 1.9 km at 132 kV.

Terna Rete Italia S.r.l.

The dimensions of Terna Rete Italia S.r.l. recorded overall a decrease of 1 three-phase power line which corresponds to 4.3 km of line, as described below:

Power lines

- deactivation and/or demolition of 2 three-phase power lines for a total of 3.9 km, of which: 1 three-phase power line and 0.2 km at 60 kV, 1 three-phase power line and 3.7 km at 50 kV;
- construction of variants and/or route changes with a decrease of 0.4 km of three-phase power line at 60 kV.

Financial capital

The Group's financial policy is distinguished by its diversification of financing sources, the balance between short and medium-long term instruments to cover loans, and the proactive management of debt.

At 30 September 2016, gross financial debt³ totalled approximately € 8.7 billion, of which € 6.5 billion was made up of bonds and € 2.2 billion of bank loans. The average debt maturity is around 5 years; the proportion of net debt at fixed and floating rate to the total amounts to 85% and 15% respectively.

Bond debt consists of both public and private placement issuances in the context of the € 8 billion EMTN Bond Issue Programme (with the involvement of a number of both Italian and foreign banking and financial institutions), combined with the stand-alone issue for € 800 million dating back to 2004. Focusing on a specific bracket of qualified investors and listed on the Luxembourg Stock exchange, Terna bonds present a significantly diverse investor base, in terms of both sector and geographical profile. With regard to banking debt, Terna's main lender is the European Investment Bank (EIB); the total debt contracted with the EIB at 30 September 2016 stood at almost € 1.6 billion; all contracts entered into with the EIB are at a floating rate. Thanks to the solid nature of its credit profile, Terna is able to procure financial resources from banks at extremely favourable rates, as is testified by the three back-up revolving credit facilities in committed form for a total amount of € 2.05 billion.

The financial debt is illustrated in detail in the paragraph "Economic, Financial and Equity Performance".

(3) By gross debt is meant the sum of the items "Bonds", "Floating-rate loans" and "Short-term loans" detailed under Net Financial Debt presented in the paragraph Economic, Financial and Equity Performance, to which you are referred.

Human capital

COMPOSITION AND EVOLUTION

At 30 September 2016, the Terna Group had 3,831 employees. Details of the number of Terna Group employees at 30 September 2016 are shown below:

Change in the workforce	at 30.09.2016	at 31.12.2015	Δ
Senior executives	77	76	1
Junior executives	572	514	58
Office staff*	1,961	1,971	(10)
Blue-collar workers	1,221	1,206	15
TOTAL	3,831	3,767	64

* Includes employees of Terna Crna Gora d.o.o. with local contracts (Montenegro).

The number of personnel at the end of the third quarter of 2016 shows an increase of 64 compared to 31 December 2015 (139 joining against 75 leaving); this change is associated mainly with the following events:

- completion of the remaining portion of the plan for the recruitment of the resources necessary for the generational turnover project that the Terna Group implemented during 2015;
- launch of the process of integrating the High-Voltage assets acquired from the FSI Group and consequent implementation of the policy of recruiting resources with a view to the future management of the plants, which led to 64 new resources joining as of 30 September;
- industrial restructuring of the Tamini facility in Novara and implementation of redundancy incentive policies which involved 42 resources.

The change in personnel composition of the junior executives and office staff categories is due in particular to the merit plan implemented by the Terna Group in the first half of the year.

The breakdown, by company, of the number of employees at 30 September 2016 is illustrated in the table below:

At 30.09.2016	Terna S.p.A.	Terna Rete Italia S.p.A.	Terna Plus S.r.l.	Terna Storage S.r.l.	Tamini Group	Terna Crna Gora d.o.o.	Group Total
Senior executives	36	27	1	-	13	-	77
Junior executives	171	377	6	-	18	-	572
Office staff	259	1,542	8	-	147	5*	1,961
Blue-collar workers	-	999	-	-	222	-	1,221
TOTAL	466	2,945	15	-	400	5	3,831

* Local employees.

Training

During the third quarter of 2016, the Group continued the training activities aimed at developing the necessary skills of personnel brought in under the generational turnover project; as at 30 September 2016 a total of 130 thousand hours of instruction had been delivered in particular for the topics “Context & Business Model”, “Education” and “Training”.

Next Energy Initiative

In May 2016 Terna launched NEXT ENERGY, an initiative developed in partnership with the Cariplo Foundation to help young engineering graduates, through inclusion on corporate working groups engaged in developing innovative projects, and to support the development of innovative projects in areas related to development of the system through an entrepreneurial empowerment programme.

Intellectual capital

In all the “core” activities related to the transmission grid, the Terna Group has always pursued the highest standards, starting from the design through to the management and maintenance of assets, and without compromising on the objectives of ongoing improvements in the areas of technologies and materials. Over the years, the highest quality standards have always been guaranteed thanks to applied research, interaction with suppliers, operational experience, and the assessments made by international benchmarks. With time, this approach evolved into a consistent application of criteria as well as stable and unified projects.

More recently however, the natural and consolidated approach to research and the development of best practices has been overtaken by the need to find optimal solutions and guide the capacity to innovation towards carefully adapting to the requirements progressively imposed by the environment and surrounding world.

Terna has, in fact, been instrumental in the energy transition that is shaping the entire sector. It therefore intends to provide an effective contribution to finding ‘sustainable’ solutions, also within the context of eco-compatibility and mindful of climate change.

Attention and effort will consequently focus both on core activities, which are now faced with new prospects and a different approach, as well as on decidedly innovative sectors.

With these premises, research and development is undertaken organically and systematically, taking advantage of the in-house skills, and seeking leverage from the technical know-how and capacity also to develop opportunities beyond the regulated framework.

Operationally, the new approach makes it possible to undertake projects and initiatives with a view to “open innovation”, through the opening of new development fronts that follow two main directions:

- dynamic interactions with universities and research centres;
- collaborations with large national and international industrial players.

The first component includes significant initiatives aimed at ensuring on the one hand freshness and stimulation for the profile of **research** and **innovation** itself, on the other the premises for guiding young talents towards skills and professionalism relevant to the world of work. By way of example we can indicate the following:

- *Next Energy Project*: described in the paragraph above to which you are referred;
- *Collaboration with EnSiEL*: for the purpose of promoting and coordinating studies and research in the Energy field, contributing to the preparation of expert researchers in the sector and promoting and favouring initiatives aimed at education and training in the Energy sector, a **Memorandum of Understanding** was signed in July 2016 with the EnSiEL consortium, a non-profit research body with

which as of today 18 Italian Universities are associated. The agreement provides for collaboration between Terna and the partner Universities for the implementation of international and national research studies and projects of great scientific importance.

In the second component, that of **corporate open innovation** of an industrial kind, by way of example we can note the prestigious collaboration agreed between Terna and Tesla through a MoU on areas of absolute interest in the electrical sector, such as green islands and grid to vehicles applications, that is applications aimed at guaranteeing greater sustainability, cheapness and safety in the management of grids.

Alongside these initiatives, the increasing value of the human capital in the company is stimulated by increasingly active participation in international associations and committees of significance in the electrical and innovation sector. By way of example we can note the engagement in the EASE (European Association for Storage of Energy), of reference in the area of storage systems, testified also by the organisation of a workshop held at the Storage Lab plant in Codrongianos, in which a tangible demonstration was given of the benefits achievable from the implementation in the TSO's systems of new resources for management of the Electricity System.

In this context, the Terna Group has also begun the activities necessary to seize the opportunities of incentives in the **Research and Development** field that derive from the national legislation, such as, by way of example:

- a) rules on the subject of "Patent boxes" (subsidy introduced by Art. 1, paragraphs from 37 to 45 of Italian Law no. 190/2014);
- b) "tax credit for companies that invest in research and development activities" (subsidy introduced by Art. 1, paragraph 35 of Italian Law no. 190/2014).

Performance in the first nine months of 2016

Operating performance

International Regulated Activities

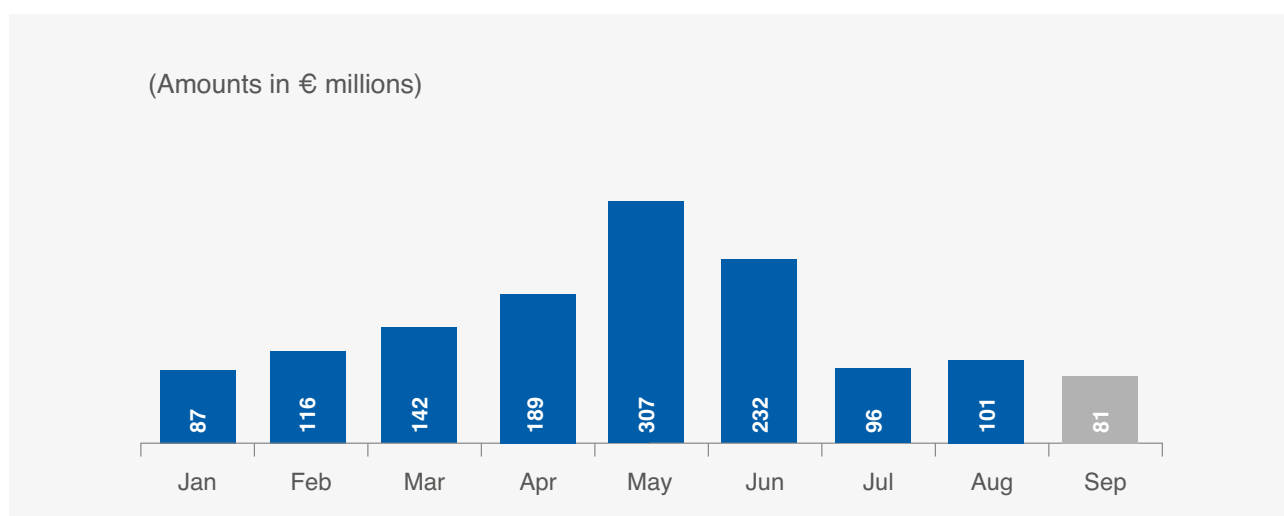
With a view to the development of regulated business opportunities at the international level, in July 2016 Terna announced its interest in acquiring a 24% stake in the share capital of the Greek transmission operator ADMIE/IPTO (Independent Power Transmission Operator S.A.), in response to the invitation to express interest proposed by the company Public Power Corporation S.A. (PPC, the current 100% parent company of ADMIE/IPTO) in virtue of the privatisation process launched by Greek Law no. 4389/2016 (subsequently amended by Law 4393/2016).

The Board of Directors of PPC admitted Terna, together with other qualified subjects, to the subsequent stage of the process, which ended with the presentations of the binding purchase offers presented on 21 October 2016. Terna participates in this initiative in a joint venture with the infrastructural fund F2i. On 31 October 2016, the Board of Directors of PPC, officialised the appointment of State Grid as Preferred Strategic Investor; this appointment will be approved by the Shareholders' Meeting called for 24 November 2016.

Dispatching Services Market

On the Dispatching Services Market (DSM), Terna procures dispatching resources to guarantee the security and adequacy of the electricity system. In the first nine months of 2016, the net expense on the DSM was € 1,352⁴ million, up compared to the corresponding period of last year (€ 891 million), owing to the increase recorded in the months from April to June (as illustrated in the next paragraph).

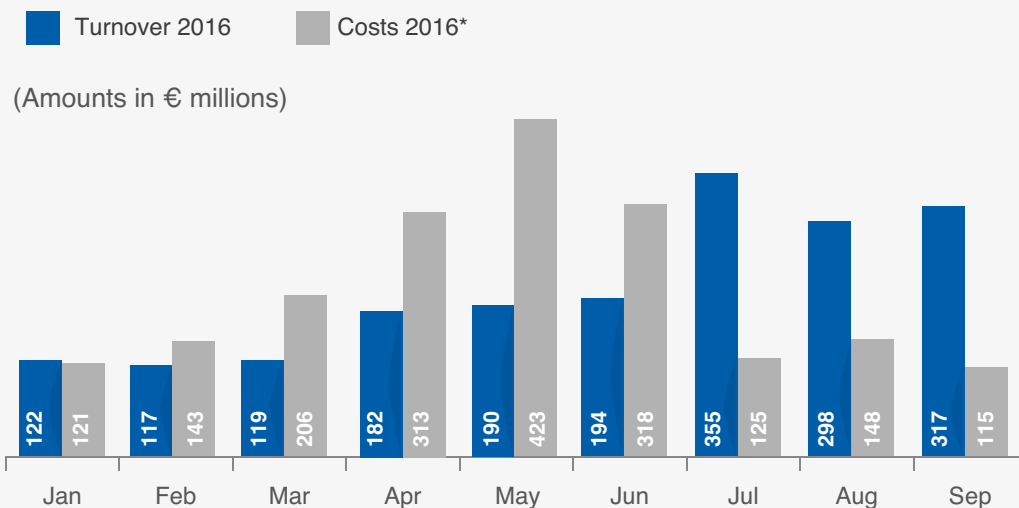
DSM 2016



(4) Provisional data for September.

Fee for procurement of resources on the DSM (uplift)

The Fee for procurement of resources on the DSM (uplift), pursuant to AEEGSI Resolution no. 111/06 Art. 44 and subsequent amendments, represents the net expense associated with the following energy-related items: purchases and sales on the DSM, spot and forward (the latter representing premiums of contracts signed as an alternative to declaration of essentiality), remuneration of plant goodwill on the DSM (goodwill and structure change token), imbalances, congestion earnings and related financial hedges, virtual interconnection service (Interconnector) and other smaller items.



* of which the DSM component is presented in detail in the previous paragraph.

This price is invoiced pro-rata to users of the dispatching on the energy withdrawn, to cover the envisaged accruing monthly cost and the prior differences.

In the first nine months of 2016, the total cost for the uplift was € 1,912 million⁵, up compared with the same period of the previous year, owing mainly to the increase in the DSM cost (commented on in the previous paragraph) and in unbalancing expenses.

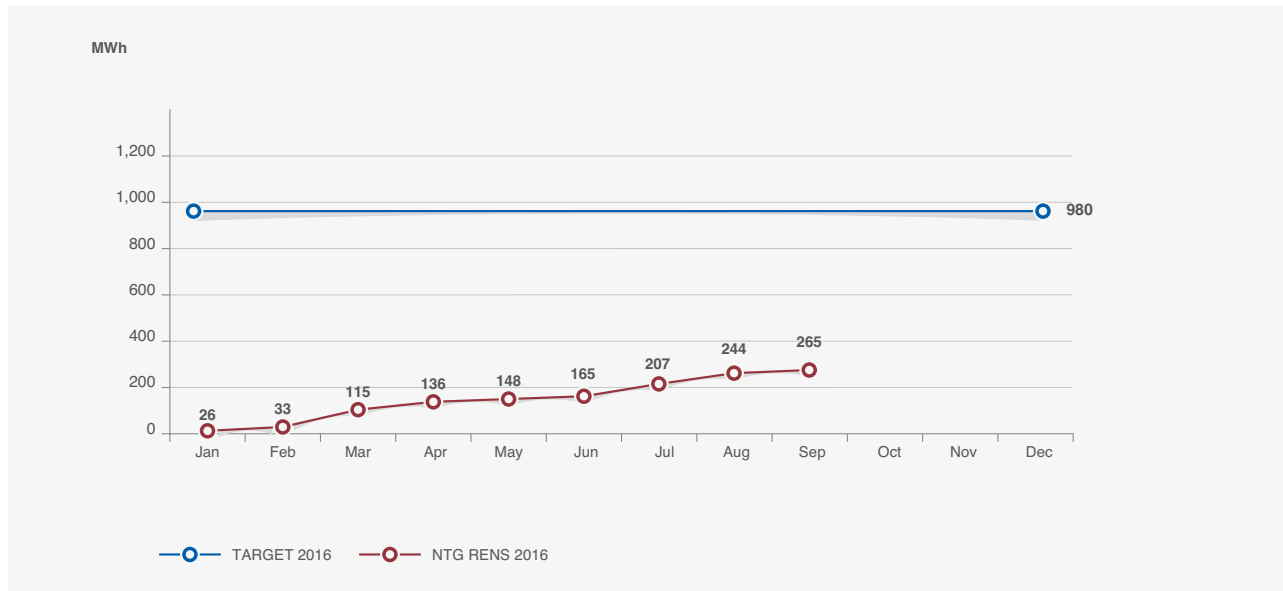
Continuity indices of the electrical service

During the first nine months of 2016 there were no events with a high impact in terms of electricity system management and service continuity.

The advancement of the “RENS - Reference Energy Not Supplied” indicator, based on preliminary operating data, with an indication of the annual target is shown below.

(5) Provisional data for September.

NTG RENS – REGULATED ENERGY NOT SUPPLIED



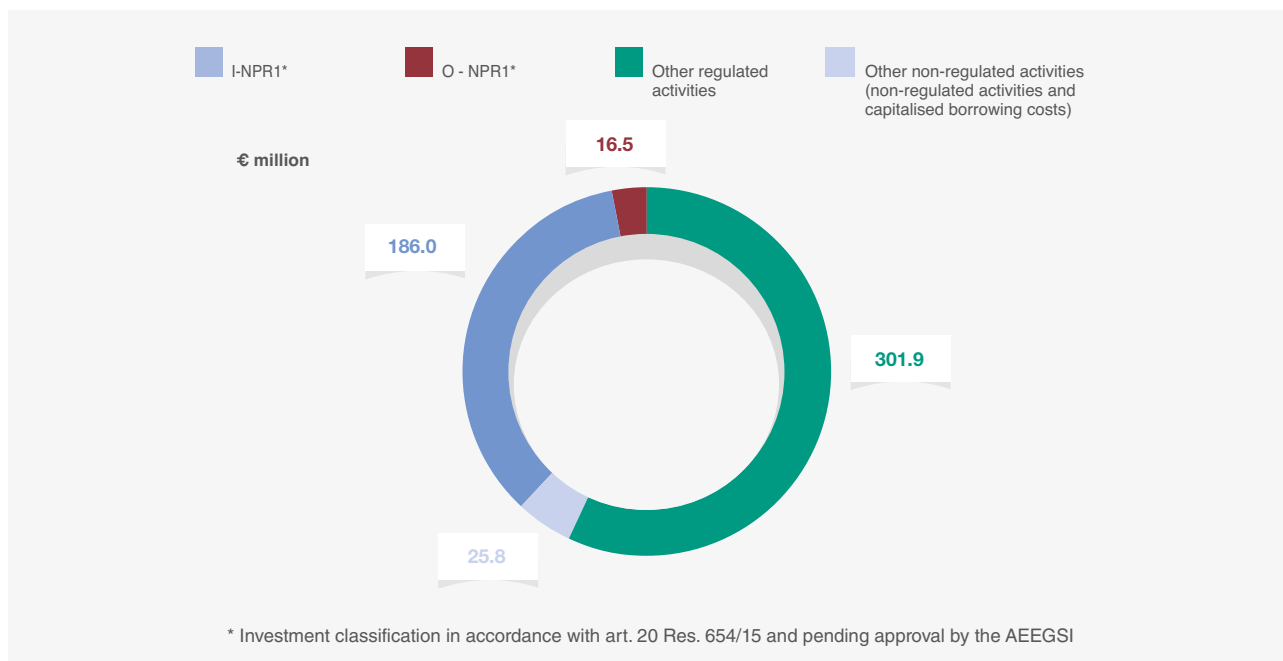
Implementation activities

The **total investments** made by the Terna Group in the first nine months of 2016 amounted to **€ 530.2 million**, of which **€ 504.4 million** in Regulated Activities and **€ 13.3 million** in Non-Regulated Activities, and the remainder refers to the related capitalised borrowing costs.

In the context of Regulated Activities incentivised **investments** (categories I-NPR1 and O-NPR1, to which AEEGSI grants an extra-remuneration of 1%) were **€ 202.5 million** and recorded a decrease of € 13.1 million compared to the corresponding period of 2015 (-6.1%).

Below is the classification of the Group's investments according to the remuneration categories identified within the new regulatory framework (5th Period).

INVESTMENTS ACCORDING TO REMUNERATION CATEGORY



- **Implementation activities - Regulated Activities**

With reference to the main projects in the period, there follows a brief comment on the stage of progress of the main works:

Italy-Montenegro interconnection (€ 102.8 million):

- Cable connection: the laying of terrestrial cables is in progress both at Kotor and at Cepagatti; the production of the undersea cables continues.
- Conversion stations: at the Cepagatti substation assembly of the prefabricated buildings has been completed; construction of the civil works of the two poles is in progress with a forecast for the start of equipment assembly by the end of the year; at the Kotor substation the foundations of the buildings are being laid.

380 kV Sorgente-Rizziconi power line (€ 71.3 million):

- The entire connection came into operation at the end of May 2016 and work is now underway on landscaping areas and restoring building sites. The work will guarantee greater security of the connection of the Sicilian electricity grid to that of the mainland, creating the conditions required to eliminate the current price spread which exists between Sicily and the rest of the country.

380 kV Foggia-Villanova power line (€ 24.0 million):

- The entire connection, about 70 km long, went into operation in January 2016; work is now underway on landscaping areas and restoring sites to their former conditions.

Melilli 380 kV substation (€ 10.1 million):

- At the Melilli substation work is in progress on the control system and the approval testing and activation of 3 bays is planned for October.
- Cable connection: the cable has been laid, the work on the terminals and joints remains to be completed.

Bari Nord 380 kV substation (€ 9.4 million):

- In the substation the electromechanical assemblies are being completed.
- Cable connection: the building sites are open and the excavation and laying of the first stretch has been completed.

Restructuring of the Palermo metropolitan area (€ 7.3 million):

- At the Casuzze substation the work on assembling the equipment and laying the cables has been completed.

Italy-France interconnection (€ 6.0 million):

- At the Piossasco substation the survey and test drilling activities have been completed and the fencing work is in progress.
- Cable connection: the civil works have begun on the connection stretch outside of the motorway, while for the other two stretches the approvals of the executive projects and the procurement activities are in progress.

The item "other" includes mainly actions to purchase and/or renovate offices (€ 5.0 million).

Investments in intangible assets (€ 22.7 million) include actions aimed at the upgrade and development of software and a residual investment reclassified in accordance with IFRIC 12 (€ 3.4 million).

• **Implementation activities - Non-Regulated Activities**

Projects under Non-Regulated Activities in Italy completed in the third quarter of 2016 are divided into the following areas:

- Interconnections;
- Services for third parties;
- Production of Transformers - Tamini Group;
- Initiatives abroad.

Interconnections

Activities went ahead in the quarter aimed at developing the Interconnector projects implementing Italian Law 99/2009. In particular, these activities regarded the projects in the most advanced stage of development related to the Italy-France interconnections.

“Italy-France” Interconnector Project

On 5 August 2016 the Decree authorising the construction variant was issued by MED. In addition, on 20 July 2016 the Ministry issued the exemption decree, which was then sent to the European Community for the necessary approval.

Services for third parties

In Italy, during the third quarter of 2016, Terna continued to perform activities for third parties in the area of engineering services (developing technical solutions and supplying innovative services), telecommunications (TLC, housing of telecommunication equipment and maintenance services involving fibre optic networks) and third-party plant management (operating and maintaining High-Voltage and Very-High-Voltage plants).

As regards services in the **Engineering** area, among the main contracts acquired we can note: the construction of a 132 kV substation for connecting to the NTG a gas cavern storage plant in Lombardy, the construction of a connection solution in HV for 5 photovoltaic fields, the construction of a mini wind farm made up of 16 plants and the upgrading of an electricity substation annexed to a production power station. It is also worth noting the Memorandum of Understanding signed with Vento di Venezia S.r.l. in the context of the project for requalification and sustainable development of the island of Certosa in Venice, through the testing of new technologies and clean energies. This project forms part of a wider Terna strategy to modernise the grid and to make the smaller islands more innovative and hi-tech.

As for **Telecommunications** activities, the company has continued to aim at developing electrical infrastructure enhancement services for offering fibre optic and housing services, with particular reference to telecommunication operators.

In particular, during the third quarter of 2016, further contracts were signed for the transfer of use rights for optical fibres and feasibility planning was begun for the issue of further offers.

In addition studies and projects were launched for the further use of pylons as supports for radio systems in rural areas and environmental monitoring networks.

As regards **Third-party plant management** activities, development work continues in the field of energy efficiency services.

Production of Transformers - Tamini Group

During the period the first Phase Shifting Transformer units were delivered; this is a complex and strategic project for Tamini which has managed to enter into this important sector on a European scale. In addition, again at the Legnano facility, the approval test was carried out successfully on the 500 MVA transformer with transformation ratio 400/220 kV for ESB; this is the largest transformer installed in Ireland, for dimensions and weight.

Sales of transformers in the first nine months of the year fell compared to the same period of the previous year (-29%).

At the end of August work began on reclaiming and making safe the Melegnano Facility, which will therefore remain out of operation for the duration of the work, expected to last around 6 months.

Initiatives abroad

In the last quarter Terna has been awarded the tender called in Uruguay by UTE – a vertically integrated, state-owned company which locally manages the generation, transmission, distribution and sale of electricity – for the construction of three new electricity infrastructures. Once the tender results are formalised, Terna will have 24 months to construct and commission the three power lines.

Scouting activities continued regarding development prospects in geographical areas with low risk profiles and high growth rates.

Economic, financial and equity performance

In order to present the performance of the Terna Group and to analyse its financial position, financial schedules have been prepared. These are not subject to independent auditing.

These reclassified tables contain alternative performance measures (hereinafter APMs, as per ESMA/2015/1415 guidelines⁽⁶⁾) which management considers useful for monitoring Group trends, and representative of the economic and financial results produced by the business.

The criteria used to construct these measures are the same used in the annual reporting; for the related details, please see the contents of the Annex “Alternative Performance Measures”.

Consolidation scope

During the first nine months of 2016, there were no events that would have had effects on the Terna Group’s consolidation scope, which therefore reflects the situation at 31 December 2015 as described in the paragraph “Corporate Structure”. We can note that the Income Statement of the first nine months of 2016 includes the contribution of Rete S.r.l. and of TES-Transformer Electro Service (controlled by Tamini S.r.l.), not included in the comparative period, since the acquisitions occurred on 23 December and 30 October 2015 respectively.

Basis of presentation

The measurement and recognition criteria applied in this consolidated interim financial report are consistent with those adopted in the consolidated financial statements at 31 December 2015. We can specify that, for the purpose of better representation of the effects of acquisition of the FSI Group grid, a number of comparative equity balances were redetermined under the terms of IFRS 3, without however modifying the economic result at 30 September 2015 and the equity at 31 December 2015.

(6) These guidelines apply to APMs distributed by issuers or by the subjects responsible for preparing the statements in the publication of regulated information or of statements starting from 3 July 2016. In particular, the references to Directive 2003/6/EC are understood as made to Regulation (EU) no. 596/2014 of the European Parliament and of the Council, of 16 April 2014, on market abuse (market abuse regulation) which abrogates Directive 2003/6/EC of the European Parliament and of the Council and Directives 2003/124/EC, 2003/125/EC and 2004/72/EC of the Commission, and must be read in accordance with the correlation table pursuant to Annex II of the said regulation.

Economic results

The results of the Terna Group for the first nine months of and for the third quarter of the years 2016 and 2015 are summarised in the following operating income statement.

3rd quarter					1 January - 30 September			
2016	2015	Δ	Δ %	€ million	2016	2015	Δ	Δ %
REVENUE								
435.0	421.7	13.3	3.2%	- Transmission Fee	1,306.1	1,261.0	45.1	3.6%
28.7	32.0	(3.3)	(10.3%)	- Dispatching Fee	83.5	94.0	(10.5)	(11.2%)
44.4	56.2	(11.8)	(21.0%)	- Other revenues and income	151.3	149.2	2.1	1.4%
7.3	1.8	5.5	305.6%	of which other revenue from Regulated Activities	23.8	11.6	12.2	105.2%
37.1	54.4	(17.3)	(31.8%)	of which other revenue from Non-Regulated Activities	127.5	137.6	(10.1)	(7.3%)
3.0	4.9	(1.9)	(38.8%)	- Revenue from construction of licensed activities*	10.1	12.6	(2.5)	(19.8%)
511.1	514.8	(3.7)	(0.7%)	TOTAL REVENUE	1,551.0	1,516.8	34.2	2.3%
OPERATING EXPENSES								
52.4	51.4	1.0	1.9%	- Personnel expenses	165.6	163.2	2.4	1.5%
37.3	31.4	5.9	18.8%	- Services, leases and rentals	121.4	97.2	24.2	24.9%
11.7	24.2	(12.5)	(51.7%)	- Materials	50.6	56.4	(5.8)	(10.3%)
5.9	8.5	(2.6)	(30.6%)	- Other expenses	21.9	23.1	(1.2)	(5.2%)
1.5	0.2	1.3	650.0%	- Service quality	5.1	3.5	1.6	45.7%
3.0	4.9	(1.9)	(38.8%)	- Costs of construction of licensed activities	10.1	12.6	(2.5)	(19.8%)
111.8	120.6	(8.8)	(7.3%)	TOTAL OPERATING EXPENSES	374.7	356.0	18.7	5.3%
399.3	394.2	5.1	1.3%	GROSS OPERATING MARGIN (EBITDA)	1,176.3	1,160.8	15.5	1.3%
136.0	118.9	17.1	14.4%	- Amortisation, depreciation and impairment	403.2	361.9	41.3	11.4%
263.3	275.3	(12.0)	(4.4%)	OPERATING PROFIT (EBIT)	773.1	798.9	(25.8)	(3.2%)
(24.2)	(53.4)	29.2	(54.7%)	- Net financial income (expense)	(60.4)	(117.1)	56.7	(48.4%)
239.1	221.9	17.2	7.8%	PROFIT BEFORE TAXES	712.7	681.8	30.9	4.5%
77.5	76.9	0.6	0.8%	- Income taxes for the period	228.2	226.9	1.3	0.6%
161.6	145.0	16.6	11.4%	NET PROFIT FOR THE PERIOD	484.5	454.9	29.6	6.5%
(0.4)	-	(0.4)	0.0%	- Share attributable to non-controlling interests	(2.3)	-	(2.3)	0.0%
162.0	145.0	17.0	11.7%	GROUP NET PROFIT FOR THE PERIOD	486.8	454.9	31.9	7.0%

* Recognised pursuant to "IFRIC 12 - Service Concession Arrangements"

In the first nine months of 2016, the Terna Group achieved **revenue of € 1,551.0 million**, referred to Regulated Activities for € 1,413.4 million and to Non-Regulated Activities for € 127.5 million. The item shows an increase of € 34.2 million compared to the same period of the previous year (+2.3%), due to the net effect of the increase in revenue from Regulated Activities, of € 46.8 million, and of the reduction in revenue related to Non-Regulated Activities, of € 10.1 million.

Revenue from investments in licensed activities⁷, of € 10.1 million, showed a decrease compared to the same period of the previous year of € 2.5 million.

(7) This item includes the recognition of revenue provided for in "IFRIC 12 - Service Concession Arrangements", with the same amount in operating expenses.

The following are details of Revenue items that make up the **Regulated Activities**⁸.

REVENUE FROM REGULATED ACTIVITIES

€ million	9M 2016	9M 2015	Δ
Transmission Fee	1,306.1	1,261.0	45.1
Dispatching Fee	83.5	94.0	(10.5)
Other revenues and income	23.8	11.6	12.2
TOTAL	1,413.4	1,366.6	46.8

The increase in revenue from Regulated Activities, of € 46.8 million compared to the first nine months of 2015, was mainly due to the combined effect of:

- increase in the **fee for transmission activity** (€ +45.1 million): particularly significant are the contribution of the inclusion in the first nine months of 2016 of the National Transmission Grid acquired at the end of 2015 from the FSI Group (€ +48.2 million, including the linearisation under the terms of IFRS 3 of the effects provided for in Resolution 517/2015/R/eel), and the one-off effect of the recognition of the strategic investments related to the 2015 incentivised work in progress defined in AEEGSI Resolution 335/2016/R/eel (€ 5.5 million), as well as the overall effects of the new 2016–2023 regulatory period (which entail a reduction in revenue referable to the revision of the WACC, partially offset by the reduction in the time-lag);
- negative change in the **fee for dispatching activity** (€ -10.5 million), which reflects the overall effects of the new 2016–2023 regulatory period;
- increase in **other operating revenue** (€ +12.2 million): of particular importance the higher revenue from sales to third parties, essentially for continuation of the so-called “Copper Plan” (€ 10.8 million), which provides for the gradual replacement of certain obsolete copper conductors with new aluminium conductors and higher revenue connected with service of connecting plants to the NTG (€ +1.4 million).

REVENUE FROM NON-REGULATED ACTIVITIES

€ million	9M 2016	9M 2015	Δ
Tamini Group	74.9	77.5	(2.6)
Tamini price adjustment	-	5.9	(5.9)
New TLC contracts	6.7	-	6.7
Order in Chile	2.2	7.3	(5.1)
Other (services and other revenue)	43.7	46.9	(3.2)
TOTAL	127.5	137.6	(10.1)

The revenue related to **Non-Regulated Activities** fell by € 10.1 million compared to the corresponding period of the previous year substantially as a result of non-recurring items recognised in the first nine months of 2015. In particular:

- lower revenue of the Tamini Group (€ -2.6 million) owing substantially to the impact of an insurance indemnity recognised in the first nine months of 2015, net of the effects of the perimeter delta attributable to the acquisition of TES (not included in the consolidation scope in the comparative period);

(8) Net of revenue from construction of licensed activities.

- recognition in the comparative period of the adjustment of the price paid for the acquisition of Tamini (€ -5.9 million);
- higher revenue recognised in the comparative period connected with an order in Chile (€ -5.1 million), in the completion stage;
- reduction of grants for variants at the request of third parties (€ -3.8 million); offset by new TLC contracts (in particular a contract for support on the Rete S.r.l. power lines of the optical fibre owned by Basicel for € +4.2 million, and the concession to third parties of usage rights on a stretch of optical fibre, for an amount of € 2.3 million, signed by the Parent Company in April 2016).

NI In the third quarter of 2016, revenue fell by € 1.8 million compared to the corresponding period of 2015, net of revenue from construction of the licensed activities (€ -1.9 million), owing essentially to the drop recorded in Non-Regulated Activities (€ -17.3 million, mainly related to the Tamini Group and to the subsidiary Terna Chile S.p.A.), in part offset by the higher revenue of Regulated Activities (€ +15.5 million) deriving from the aforementioned one-off effects of AEEGSI Resolution 335/2016/R/eel and from the change in perimeter, which more than offset the effects of the tariff review on transport and dispatching prices, and from the increase in other revenue mainly related to the “Copper Plan”.

OPERATING EXPENSES

€ million	9M 2016	9M 2015	Δ
Personnel expenses	165.6	163.2	2.4
Services, leases and rentals	121.4	97.2	24.2
Materials	50.6	56.4	(5.8)
Other expenses	21.9	23.1	(1.2)
Service quality	5.1	3.5	1.6
Costs of construction of licensed activities*	10.1	12.6	(2.5)
Total operating expenses	374.7	356.0	18.7

* Recognised pursuant to IFRIC 12

In the first nine months of 2016 **operating expenses**, of € 374.7 million, increased in comparison with the corresponding period of 2015 of € 18.7 million, mainly as a result of the expenses related to the subsidiary Rete S.r.l., not included in the comparative period.

The breakdown of the Group's operating expenses in the period, with separate evidence for the Tamini Group deviation, is shown in the following table:

€ million	9M 2016	9M 2015	Δ Total	Δ without Tamini	Δ Tamini
Personnel expenses	165.6	163.2	2.4	(1.5)	3.9
Services, leases and rentals	121.4	97.2	24.2	23.8	0.4
Materials	50.6	56.4	(5.8)	(4.1)	(1.7)
Other expenses	21.9	23.1	(1.2)	(1.9)	0.7
Service quality	5.1	3.5	1.6	1.6	-
Costs of construction of licensed activities*	10.1	12.6	(2.5)	(2.5)	-
Total operating expenses	374.7	356.0	18.7	15.4	3.3

* Recognised pursuant to IFRIC 12

Operating expenses, net of the Tamini Group's balances, recorded an increase of € 15.4 million compared to the first nine months of 2015, owing mainly to the following changes:

- “Services, leases and rentals”: € +23.8 million, relating mainly to maintenance costs incurred by the subsidiary Rete S.r.l. (€ 27 million) and related to the grid maintenance contract with the FSI Group, partially offset by efficiencies on the costs for services provided for in the plan;
- “Personnel expenses”: € -1.5 million, deriving essentially from the effect of the savings generated by the generational turnover plan implemented during 2015, taking into account the lower capitalisations of the period;
- “Materials”: € -4.1 million, related essentially to the order in Chile (€ -5.2 million), substantially completed in the period, in part offset by the higher costs for materials recognised by the subsidiary Terna Rete Italia S.p.A. (€ +1 million) for ordinary maintenance activities on the Group's plants;
- “Other expenses”: € -1.9 million, attributable mainly to the Parent Company for provisions for IMU (council tax) set aside in the comparative period (€ -5.4 million) and as a result of a number of one-off items (€ +3.5 million, attributable in particular to legal disputes).

The economic effects of the bonus/penalty mechanisms on service quality for the first nine months of 2016 showed an increase of € 1.6 million compared to the same period of the previous year, substantially as a result of grants to provisions for exceptional events (€ +1.7 million). A comparative table on service quality costs is provided below:

Electricity service quality costs

€ million	9M 2016	9M 2015	Δ
Mitigation and partnership mechanisms	2.3	2.8	(0.5)
Contributions to Exceptional Events Provision	2.4	0.7	1.7
High-voltage users compensation mechanisms	0.4	-	0.4
Total Service quality	5.1	3.5	1.6

The overall change in operating expenses also takes into account the lower costs associated with investments in infrastructures in concession (IFRIC 12, € -2.5 million).

In the third quarter of 2016, operating expenses fell by € 8.8 million compared to the corresponding period of 2015, owing essentially to the combined effect of the factor described above (owing mainly to lower costs related to the order in Chile and to the saving policy, offset by the contribution of Rete S.r.l.) besides the reduction of the operating expenses of the Tamini Group.

EBITDA (Gross Operating Margin) for the period came out at **€ 1,176.3 million**, an increase of € 15.5 million compared with the € 1,160.8 million of the first nine months of 2015.

The **EBITDA margin** went down from 76.5% in the first nine months of 2015 to 75.8% in the corresponding period of 2016, considering also the contribution of the Tamini Group.

The item **amortisation, depreciation and impairment** for the period, amounting to € 403.2 million (of which € 342.8 million of the parent company, € 36.2 million of the subsidiary Terna Rete Italia S.r.l. and € 19.1 million of the subsidiary Rete S.r.l.), grew by € 41.3 million compared with the same period in 2015 owing to the commissioning of new plants (the main impact derived from the Sorgente-Rizziconi and Villanova-Gissi power lines) and to the depreciation and amortisation related to the subsidiary Rete S.r.l., not present in the comparative period.

EBIT (Operating Profit), after deducting amortisation, depreciation and impairment, came out at **€ 773.1 million**, compared with € 798.9 million in the first nine months of 2015 (-3.2%).

The **net financial expenses** for the period, of € 60.4 million, primarily attributable to the Parent Company (€ 59.1 million), showed a reduction of € 56.7 million compared to the same period in 2015 despite the lower capitalised borrowing costs (€ -10.3 million, owing to lower investments made in the period and the reduction in market interest rates). This drop is attributable to the general decline in interest rates and to the one-off effects connected with the Liability Management operation carried out on 20 July 2015 (equal to € 28,4 million).

Profit before taxes came out at **€ 712.7 million**, up by € 30.9 million compared to the same period of the previous year (+4.5%).

Income taxes chargeable to the period were **€ 228.2 million** and, despite the higher pre-tax profit, they were substantially in line with the same period of the previous year (€ +1.3 million, or +0.6%), owing mainly to higher deductible items, also taking into account the 2016 Stability Law (Italian Law 208/2015), which therefore brought the **tax rate** of the period to 32% compared to 33.3% in the first nine months of 2015.

Net profit for the period reached **€ 484.5 million**, up € 29.6 million (+6.5%) compared with the € 454.9 million of the first nine months of 2015.

The Group's net profit for the period, finally, came out at **€ 486.8 million**, up € 31.9 million (+7.0%) compared with the € 454.9 million of the first nine months of 2015.

Results by business segment

Economic results

The breakdown of the Terna Group's results by business segment, in relation to the first nine months of 2016 and 2015, is shown in the table below⁹:

€ million	9M 2016	9M 2015	Δ	Δ %
Total revenue from Regulated Activities	1,413.4	1,366.6	46.8	3.4%
Transmission Fee	1,306.1	1,261.0	45.1	3.6%
Dispatching Fee	83.5	94.0	(10.5)	(11.2%)
Other core revenue	23.8	11.6	12.2	105.2%
Total revenue from Non-Regulated Activities	127.5	137.6	(10.1)	(7.3%)
Tamini Group revenue	74.9	77.5	(2.6)	(3.4%)
Other non-regulated revenue	52.6	60.1	(7.5)	(12.5%)
Revenue from construction of licensed activities	10.1	12.6	(2.5)	(19.8%)
Total revenue	1,551.0	1,516.8	34.2	2.3%
Total costs of Regulated Activities	265.3	244.6	20.7	8.5%
Personnel	138.3	140.7	(2.4)	(1.7%)
External resources	106.7	82.7	24.0	29.0%
Service quality	5.1	3.5	1.6	45.7%
Other expenses	15.2	17.7	(2.5)	(14.1%)
Total costs of Non-Regulated Activities	99.3	98.8	0.5	0.5%
Tamini Group costs	79.5	76.2	3.3	4.3%
Other non-regulated costs	19.8	22.6	(2.8)	(12.4%)
Costs from construction of licensed activities	10.1	12.6	(2.5)	(19.8%)
Total operating expenses	374.7	356.0	18.7	5.3%
EBITDA	1,176.3	1,160.8	15.5	1.3%
EBITDA Regulated Activities	1,148.1	1,122.0	26.1	2.3%
EBITDA Non-Regulated Activities	28.2	38.8	(10.6)	(27.3%)

The **EBITDA of Regulated Activities** amounted to € 1,148.1 million, recording an increase of € 26.1 million compared to the figure for the first nine months of 2015, owing mainly to the contribution of the subsidiary Rete S.r.l. (€ +20.7 million) commented on above.

The **EBITDA of Non-Regulated Activities** amounted to € 28.2 million and showed a reduction of € 10.6 million substantially due to the Tamini Group (€ -5.9 million) and to the impact of the price adjustment paid for the acquisition of Tamini recognised in the comparative period (€ -5.9 million).

(9) The Terna Group's business segments are in keeping with the internal management control system adopted by the Parent Company, in line with the 2016–2019 Strategic Plan.

Investments

Resolution 654/15/R/eel confirmed the effects of incentive regulations from prior regulatory periods for all investments that came into operation at 31 December 2015. For investments that will become operational as from 01 January 2016, relating both to development works approved by the AEEGSI not included among the ex-I3 investments and approved under Resolution 40/13 (O-NPR1), as well as to certain I3 investments approved under Resolution 40/2013 (I-NPR1), a 1% increase in the WACC is recognised for 12 years, subject to specific conditions set out in Annex A to Resolution 654/15/R/eel and therefore awaiting the approval of the AEEGSI.

The table below shows the breakdown of investments for the first nine months of 2016:

INVESTMENTS

€ million	9M 2016	9M 2015	Δ	Δ%
I-NPR1	186.0	178.9	7.1	4.0%
O-NPR1	16.5	36.7	(20.2)	(55.0%)
Investments with incentives*	202.5	215.6	(13.1)	(6.1%)
Other regulated activities	301.9	450.6	(148.7)	(33.0%)
Investments in Regulated Activities	504.4	666.2	(161.8)	(24.3%)
Other Non-Regulated**	25.8	35.8	(10.0)	(27.9%)
Total investments	530.2	702.0	(171.8)	(24.5%)

* Investments classified in accordance with Art. 20 of Resolution 654/15/R/eel and pending approval by the AEEGSI.

** These include "investments in Non-Regulated Activities" and capitalised borrowing costs.

During the first nine months of 2016, the Terna group invested € 530.2 million, compared to € 702.0 million in the same period of the previous year. Of this € 202.5 million are investments included in the I-NPR1 and O-NPR1 categories specified above.

"Investments in Non-Regulated Activities" regard mainly investments of the subsidiary Piemonte Savoia S.r.l..

The Group's reclassified statement of financial position

The reclassified consolidated statement of financial position at 30 September 2016 and at 31 December 2015 is summarised in the table below:

€ million	at 30.09.2016	at 31.12.2015	Δ
Net non-current assets			
- Intangible assets and goodwill	514.2	530.1	(15.9)
- Property, plant and equipment	12,224.9	12,078.7	146.2
- Financial assets	93.1	89.5	3.6
Total	12,832.2	12,698.3	133.9
Net working capital			
- Trade receivables	454.9	568.3	(113.4)
- Inventories	14.0	12.4	1.6
- Other assets	23.7	13.8	9.9
- Trade payables	(563.5)	(720.9)	157.4
- Net energy-related pass-through payables	(467.1)	(617.9)	150.8
- Net tax liabilities	(202.6)	132.5	(335.1)
- Other liabilities	(384.7)	(364.9)	(19.8)
Total	(1,125.3)	(976.7)	(148.6)
Gross invested capital	11,706.9	11,721.6	(14.7)
Sundry provisions	(358.5)	(373.1)	14.6
NET INVESTED CAPITAL	11,348.4	11,348.5	(0.1)
Equity attributable to the owners of the Parent	3,524.8	3,320.8	204.0
Equity attributable to non-controlling interests	22.7	25.0	(2.3)
Net financial debt	7,800.9	8,002.7	(201.8)
TOTAL	11,348.4	11,348.5	(0.1)

The increase in **Net non-current assets** of € 133.9 million, compared with the figure of 31 December 2015, is mainly attributable to the item **Property, plant and equipment** (€ +146.2 million) owing essentially to the ordinary changes that occurred in the period related to:

- investments for € 507.5 million;
- amortisation of € 362.8 million and other changes in the period, such as the recognition of grants for plants, disposals and impairment (€ +1.5 million).

Intangible assets and goodwill recorded a decrease of € 15.9 million compared to the previous period, attributable to ordinary changes in intangible assets owing to the combined effect of investments of € 22.7 million, net of the amortisation for the period (€ 38.6 million).

Total investments made by the Group in the first nine months of 2016 amounted to € 530.2 million, in line with the Strategic Plan, compared with € 702.0 million in the corresponding period of 2015 (-24.5%).

€ million	9M 2016	9M 2015	Δ	Δ%
Investments in Property, plant and equipment	507.5	682.0	(174.5)	(25.6%)
Investments in Intangible assets	22.7	20.0	2.7	13.5%
Total Group Investments	530.2	702.0	(171.8)	(24.5%)

Net working capital amounted to € -1,125.3 million and during the period provided liquidity of € 148.6 million, owing mainly to the combined effect of:

Liquidity absorbed

The following phenomena have been identified:

- a reduction in **net energy-related pass-through payables** of € -150.8 million (€ 467.1 million at 30 September 2016), relating to the electricity dispatching activity by the Parent Company, mainly due to the combined effect of:
 - an increase in net receivables associated with the so-called Uplift and associated items (€ +503 million) due to the higher expenses recorded for the Dispatching Services Market (DSM)¹⁰ and for unbalancing in the second quarter of 2016;
 - an increase in net payables associated with the essential units for the security of the electricity system - UESS (approximately € 357.1 million) consequent to items related to collection which more than offset the payments in favour of users of essential plants made during the period in execution of AEEGSI orders;
- a decrease in **trade payables** of € 157.4 million, mostly attributable to the greater investment activities implemented in the last period of the previous year;
- an increase in **other assets** (€ +9.9 million), substantially referable to higher prepayments (€ +8.3 million) of items liquidated in the period related to personnel, local taxes, insurance premiums and the like.

Liquidity generated

The following phenomena have been identified:

- a decrease in **trade receivables** of € -113.4 million, due mainly to the reduction in grid transmission fee receivables (€ -89.1 million), mainly attributable to the collection from Cassa per i Servizi Energetici e Ambientali (CSEA) of the receivable for the supplement to Terna S.p.A.'s grid transmission fee revenue related to 2014 (€ 80.8 million); it is also worth noting the reduction in receivables associated with Non-Regulated Activities for collections in the period referable to greater activities recognised at the end of 2015;
- an increase in **net tax liabilities** of € 335.1 million attributable mainly to the trend in the payable position to the tax authority for VAT (€ +218.0 million, compared to the credit situation at the end of financial year 2015) and to higher net payables to the tax authority for current taxes (€ +114.1 million), as a result of the recognition of income taxes of the period, net of the advances paid in the period and of the liquidation of taxes for financial year 2015;
- an increase in **other liabilities** (€ +19.8 million), mainly attributable to the interconnector guarantee fund¹¹ set up under Terna S.p.A. by the 2015 Stability Law (€ +12.4 million) and also to higher guarantee deposits (€ +3.6 million) received essentially from the electricity market operators to guarantee their contractual obligations under the dispatching contracts.

Gross invested capital, therefore, amounted to € 11,706.9 million, recording a decrease compared with the previous financial year of € 14.7 million.

Sundry provisions recorded a decrease of € 14.6 million, attributable to the change in provisions for net deferred tax liabilities (€ -33.1 million, owing mainly to the utilisation of earlier provisions for additional depreciation and amortisation with respect to the economic and technical quotas), partially offset by the trend in provisions related to employee benefits (€ +2.5 million) and by changes in provisions for risks and charges (€ +16.0 million, mainly as a result of expenses consequent to entry into operation of plants, with particular reference to the Sorgente-Rizziconi).

(10) In the first nine months of 2016, the net expense on the DSM was € 1,352 million (provisional data for September) up compared to the € 891 million of the same period of last year.

(11) We can note that on 30 September 2016 the related implementing Decree was issued by the MED, as commented on in the Annex "Legislative Framework" to which you are referred.

Net invested capital amounted to € 11,348.4 million, substantially in line with the figure recorded at 31 December 2015 (€ -0.1 million) and is financed by equity attributable to the owners of the parent for € 3,524.8 million (compared with € 3,320.8 million at 31 December 2015), by third party equity for € 22.7 million (€ 25.0 million at 31 December 2015) and by net financial debt of € 7,800.9 million (€ -201.8 million compared with the € 8,002.7 million of 31 December 2015).

Cash flows

Net financial debt

The Group's net financial debt at 30 September 2016 (€ 7,800.9 million) is broken down in the table below:

€ million	30.09.2016	31.12.2015	Δ
Net financial debt (by duration)			
A. Medium- and long-term debt			
- Bonds	5,737.6	6,406.1	(668.5)
- Floating-rate loans	1,987.4	2,110.4	(123.0)
- Derivative financial instruments	(355.9)	(680.9)	325.0
Total	7,369.1	7,835.6	(466.5)
B. Short-term debt (liquidity):			
- Bonds (current portion)	769.7	-	769.7
- Short-term loans	28.8	416.6	(387.8)
- Floating-rate loans (current portions)	134.6	122.9	11.7
- Other net current financial liabilities*	56.8	59.2	(2.4)
- Cash and cash equivalents	(558.1)	(431.6)	(126.5)
Total	431.8	167.1	264.7
Total net financial debt	7,800.9	8,002.7	(201.8)
Net financial debt (by type of instrument)			
- Bonds	6,507.3	6,406.1	101.2
- Floating-rate loans	2,122.0	2,233.3	(111.3)
- Derivative financial instruments	(355.9)	(680.9)	325.0
- Short-term loans and other financial liabilities	85.6	475.8	(390.2)
- Cash and cash equivalents	(558.1)	(431.6)	(126.5)
Total net financial debt	7,800.9	8,002.7	(201.8)

* Including interest accrued not yet collected

The structure of net financial debt, which decreased overall by € 201.8 million in the first nine months of 2016, shows the following changes:

- increase in bonds (€ +101.2 million), as a result of the bond issue on 3 March 2016 for € 80 million and the adjustment to fair value of these financial instruments (€ +21.2 million, including amortised cost) as a result of the change in forward rates as of 30 September 2016;
- decrease of floating-rate loans (€ 111.3 million) for instalments paid from outstanding loans;

- change in the mark to market of derivative financial instruments (€ +325.0 million), resulting from the simplification of the derivatives portfolio carried out during the second quarter of 2016 partially offset by the net effects on the fair value of these derivatives owing to the update of the reference interest rate curve with respect to the curve of December 2015;
- a decrease in short-term loans and other financial liabilities (€ 390.2 million) mainly as a result of repayment made by the parent company of the credit lines outstanding at 31 December 2015;
- an increase in cash and cash equivalents (€ 126.5 million). Cash and cash equivalents at 30 September 2016 amounted to € 558.1 million, of which € 258.8 million invested in time deposits and € 299.3 million deposited in bank current accounts.

Cash flow

The consolidated cash flow at 30 September 2016 and 30 September 2015 is presented in the statement below.

€ million	Cash flow 9M2016	Cash flow 9M2015
- Net Profit for the period	484.5	454.9
- Amortisation, depreciation and impairment	403.2	361.9
- Net financial expense	60.4	117.1
- Net changes in provisions	(14.6)	(42.2)
- Net Losses (Gains) on asset disposals	(5.5)	(1.3)
Self-financing (Operating Cash Flow)	928.0	890.4
- Change in net working capital	147.2	524.9
- Other changes in non-current assets	1.2	46.1
- Change in equity investments	(1.2)	(1.3)
Cash Flow from Operating Activities	1,075.2	1,460.1
- Total investments	(530.2)	(702.0)
Free Cash Flow	545.0	758.1
- Dividends paid to the owners of the Parent	(261.3)	(261.3)
- Net financial expense	(60.4)	(117.1)
- Cash flow hedge equity reserve net of the tax effect and other changes in equity	(21.5)	25.3
Change in net financial debt	201.8	405.0

The **Cash Flow from Operating Activities** in the first nine months of 2016 came out at € 1,075.2 million compared to the € 1,460.1 million of the same period of the previous year. This flow is attributable to self-financing (€ +928.0 million, compared to the € +890.4 million of the first nine months of 2015) and to the financial resources generated by net working capital (€ +147.2 million, compared to the € +524.9 million of the first nine months of 2015).

The effect on **Self-financing (Operating Cash Flow)** was that of profit for the first nine months of 2016 of € 484.5 million, amortisation, depreciation and impairment accruing of € 403.2 million and net financial expense for the period of € 60.4 million.

The change in **net working capital**, of € +147.2 million, was mainly attributable to the change in the tax position, which more than balanced the reduction in the net position of energy-related pass-through payables and the items of a commercial nature.

The Group's **total investments** made in the period amounted to € 530.2 million referable to property, plant and equipment for € 507.5 million and to intangible assets for € 22.7 million.

Therefore the **Free Cash Flow** was € 545.0 million compared to € 758.1 million in the first nine months of the previous year.

Taking into account the **remuneration of shareholders**, of € 261.3 million for payment of the 2015 final dividend, the **remuneration of third-party capital** (€ 60.4 million, compared to the € 117.1 million of the comparative period), and after the other changes in equity (in particular the change in the cash flow hedge reserve), the net financial debt fell by € 201.8 million, compared to the reduction of 405,0 million in the first nine months of 2015.

Performance of Terna stock

Terna S.p.A. has been listed on the Borsa Italiana electronic market since 23 June 2004 and is one of the leading Italian companies in terms of market capitalisation (eleventh on the FTSE MIB index). From the listing date to the end of September 2016, the shares have almost tripled in price (+170%) and the Total Shareholder Return (TSR¹²) has been 448%.

In the first nine months of 2016, Terna recorded a drop of 3.5% closing at 4.59 €/share, a better performance than the European industrial index of reference (DJ Stoxx Utilities) which fell by 5.2%. On 30 March 2016, the stock reached a new all-time high of € 5.08 per share. The average daily volume traded in the period on Terna stock stood at approximately 7 million shares daily, down compared to the same period of 2015 (8.3 million shares).

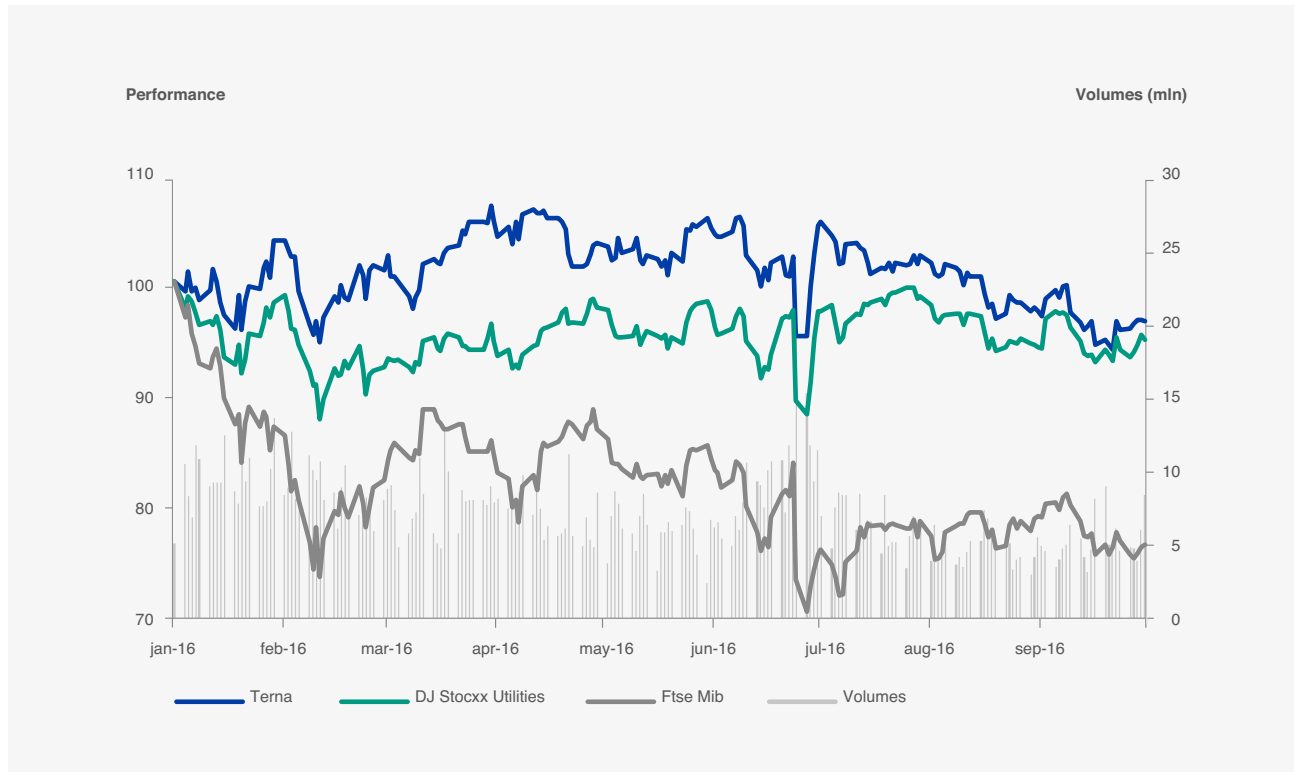
In the same period, the main European stock exchanges showed negative performance with the exception of London, which recorded a gain of 10.5%. From the beginning of the year Milan recorded a loss of 23.4%, Paris and Frankfurt closed respectively at -4.1% and -5.1% and Madrid fell by 7.9%.

The markets were negatively affected above all by the international macroeconomic scenario characterised by still weak growth data, and by the instability of the Euro Area caused by the referendum vote which was in favour of Great Britain exiting the European Union. With regard to government securities, the European Central Bank confirmed the expansive monetary policy measures, which contributed to further reducing the ten-year BTP yield, which went from 1.6% at the beginning of the year to 1.2% at the end of September 2016.

(12) Total Shareholder Return (or TSR): total return on an equity investment, calculated as the sum of:

- I. capital gain: ratio between the change in the price of the share (difference between the price recorded at the end and at the beginning of the reference period) and the price recorded at the beginning of the said period;
- II. dividends reinvested: the ratio between the dividends per share distributed in the reference period and the price of the stock at the beginning of the said period. The dividends are considered reinvested in the stock.

TREND OF TERNA STOCK AND THE FTSE MIB AND DJ STOXX UTILITIES INDICES



PERFORMANCE OF TERNA STOCK



Terna proportion on FTSE MIB and Rating

PROPORTION OF TERNA SHARES

> in the FTSE MIB index¹³ 2.55%

Source: Borsa Italiana. Data as at 30 September 2016.

	Short Term	M/L term	Outlook
Terna S.p.A.*			
Standard & Poor's	A-2	BBB	Stable
Moody's	Prime-2	Baa1	Stable
Fitch	F2	BBB+	Stable
Italian Republic*			
Standard & Poor's	A-3	BBB-	Stable
Moody's	Prime-2	Baa2	Stable
Fitch	F2	BBB+	Stable**

* Data at 30 September 2016

** On 21 October 2016 rating revised from Stable to Negative.

(13) % Total FTSE MIB

Significant events subsequent to 30 September 2016

Laying of the underground cable of the Mon.Ita. Project: the Montenegro-Italy “electrical bridge” inaugurated

On **4 October 2016** the work to lay the underground cable of the Montenegrin stretch was inaugurated in the presence of the Prime Minister of Montenegro, Milo Dukanović and the Chief Executive Officer of Terna S.p.A. Matteo Del Fante. The interconnection between Italy and Montenegro is a strategic project at the European level that represents the first “electrical bridge” between Italy and the Balkans.

The site is part of the wider project for electrical connection between Montenegro and Italy, an infrastructure in direct current for 1,000 MW of power, a total of 455 km long between Villanova (Pescara) and Kotor, with no environmental impact because it runs up to 1200 metres on the bed of the Adriatic sea and is buried for the part on land: 433 km of power line are laid under the Adriatic sea and the remaining 22 km are underground cable, of which 6 km in Montenegro and 16 km in Italy.

The work, which will be completed by the end of 2019, represents the first “electrical bridge” between Europe and the Balkans and is considered of strategic importance at the continental level: the Mon.Ita. project, in fact, has been included among the Projects of Common Interest (PCI) by the European Commission, which co-financed the feasibility studies in the framework of the programme to support the Trans-European Network (TEN) priority electrical infrastructures.

The infrastructure is a fundamental step for the European Energy Union, crucial for integrating the entire Balkan area into Europe, via Italy. Precisely Montenegro, thanks to its geographical position and through this infrastructure, can in turn become an electrical hub, performing the role of electricity exchange platform between Eastern and Western countries.

€ 750 million 12-year bond issue

On **5 October 2016** Terna finalised a bond issue in Euro, at fixed rate for a total of € 750 million as part of its Euro Medium Term Notes (EMTN) Programme of € 8,000,000,000, to which has been attributed a “BBB” rating by Standard and Poor’s, “(P)Baa1” by Moody’s and “BBB+” by Fitch.

The bonds, with a duration of 12 years and maturity on 11 October 2028, have a coupon of 1.00%, and are issued at a price of 98,882%, with a spread of 57 basis points with respect to the midswap (the “Bonds”).

The bond issue, destined for qualified investors, was placed by a syndicate of banks made up of Banca IMI, BofAML, BNPP (B&D), GSI, SG CIB, RBS and Unicredit as joint lead managers as joint bookrunners.

The operation is part of Terna’s financial optimisation programmes, to cover the needs of the Group’s Industrial Plan.

Approval of the Project for Merger by incorporation of Terna Rete Italia S.r.l. and Terna Storage S.r.l. into Terna S.p.A.

As part of the programme for corporate simplification of the Group, on **12 October 2016**, the Board of Directors of Terna S.p.A. resolved the project for the merger by incorporation into the same of two companies wholly controlled by it, Terna Rete Italia S.r.l. and Terna Storage S.r.l.

The objective of this operation is to improve the operations of the Group companies, increasing synergies, through a reorganisation aimed at simplifying the shareholding chain and at pursuing greater management efficiency and reducing administrative costs, as all the companies to be merged operate respectively in the same sector as the parent company in the management and operation of electricity lines and the further activities performed by the latter also through the subsidiaries under the terms of Art. 12.4 of the Terna S.p.A. Concession Agreement. Terna S.p.A.’s bylaws will not undergo amendments as a result of the merger, which is expected to be completed by the end of the next financial year.

Development of the website dedicated to “Open & Transparent Construction Sites”

Open & Transparent Construction Sites is the first and only online portal that allows all citizens, as well as businesses, to check on the progress of works for major infrastructure projects, as well as the economic focus, number of companies that participated in tenders, and the names of the companies that were assigned the work.

On **13 October 2016**, one year after its initial launch, *Open & Transparent Construction Sites* - the website entirely dedicated to the construction sites for electricity infrastructure in Italy - became even more interactive, dynamic and quicker. The new website includes the possibility of carrying out multiple searches by region, construction site, line, building, cable or electrical substation, with further information provided about the type and number of tenders and subcontracts and the related economic value.

This has made the details for every tender and subcontract related to over 176 Terna construction sites located throughout Italy available to all, including the names of the 353 companies working on them, which employ 4,000 workers each day. And now the information is also available on any electronic device.

Memorandum of Understanding signed with the Finance Police to promote legality, security and environmental protection in the network

On **19 October 2016** an important **Memorandum of Understanding** was signed with the Finance Police in relation to the project entitled “*Security in the network*” with the objective of strengthening further the prevention of the risk of criminal infiltration into the economic fabric and protecting legality in the creation of electrical infrastructures. The main objectives of this project are transparency in managing contracts and in procedures to award work, combating corruption, undeclared employment and unpaid contributions, new environmental rules in the context of processing of waste and of all production materials, sharing of information in all the stages of tender procedures and supervision of the correct use of raw materials and training of employees.

Terna has a task force of **professionals dedicated** to this project, a **new IT platform** and **innovative software** capable of correlating and processing the large mass of information and data collected through the **10 different data banks**, which will then be shared with the Finance Police. Thanks to this agreement, in fact, Terna will make available to the Finance Police and will report all the significant information for the prevention and repression of irregularities, frauds and all other illegal acts of an economic-financial nature. In addition, the collaboration involves a common commitment to combat unreported employment and unpaid contributions, as well as control and monitoring on the correct destination and use of raw materials and semi-finished products, with great attention to protecting the environment and the health and safety of workers: a unique **integrated approach**, with the objective of strengthening an organic vision of business on legality, transparency and the environment.

EMTN programme renewed

On **19 October 2016** Terna S.p.A. renewed its € 8,000,000,000 bond issue programme entitled “Euro Medium Term Note Programme” (EMTN) as resolved by the Board of Directors on 4 May 2016. Deutsche Bank and Citigroup were the Joint Arrangers for the programme, which obtained ratings of BBB from Standard & Poor’s, (P)Baa1 from Moody’s and BBB+ from Fitch.

The demolition of 1.6 km of power lines in the city of Vicenza begins

On **19 October 2016** the demolition of 10 pylons dating back to the 1960s began in the San Pio X district in Vicenza. This demolition is part of the rationalisation plan for the city of Vicenza which has seen a total investment by Terna of € 13 million and has been made possible thanks to the commissioning this summer of the 132 kV underground-cable power line “SE Vicenza Monteviale – CP Vicenza Viale Pace”, around 10 km long, and a short 132 kV overhead cable “SE Sandrigo – SC Fusinieri”, just 900-metres long.

The restructuring of Vicenza’s electricity grid, part of the 2011 Memorandum of Understanding between Terna, the Municipality of Vicenza and AIM, will bring increased security to the energy transmission service, aligning it with the city’s increased energy requirements, which have grown over the last 20 years by about 36%, and with electricity-service quality standards.

Binding offer presented for the acquisition of a 24% stake in the capital of ADMIE

On **21 October 2016**, the consortium formed by Terna S.p.A. and F2i SGR S.p.A. (with equal 50% stakes) which became a Qualified Participant this past 12 August 2016, presented a binding offer for the acquisition of a 24% stakes in ADMIE, a company also known as Independent Power Transmission Operator S.A. (IPTO), in keeping with the tender procedure launched on 12 July 2016 by Public Power Corporation (PPC), as the sole shareholder of ADMIE.

ADMIE is the electricity Transmission Grid Operator in Greece and owns and manages the National Electricity Transmission Grid, which has 11,529 km of lines with power of 66 – 400 kV and 310 substations.

On 31 October 2016, the Board of Directors of PPC, officialised the appointment of State Grid as Preferred Strategic Investor; this appointment will be approved by the Shareholders' Meeting called for 24 November 2016.

Further information

“Further information”, which includes indications required by specific laws or regulations governing the sector, is provided below.

Treasury shares

The Parent Company does not hold any treasury shares or shares of CDP Reti S.p.A. or Cassa Depositi e Prestiti S.p.A., nor has it acquired or sold any during the first nine months of 2016, either directly or indirectly.

Related-party transactions

For the disclosure on related parties please see the detailed contents of the Interim Financial Report at 30 June 2016.

Participation in the legislative simplification process pursuant to CONSOB Resolution no. 18079 of 20 January 2012

For the disclosure related to participation in the CONSOB simplification process please see the detailed contents of the Interim Financial Report at 30 June 2016.

Declaration by the Financial Reporting Manager in accordance with the provisions of Art. 154-bis, paragraph 2 of Italian Legislative Decree No. 58/1998

The Financial Reporting Manager, Tiziano Ceccarani, in accordance with Art. 154-bis, paragraph 2 of the Consolidated Law on Finance, declares that the accounting disclosure provided in this Consolidated Interim Financial Report at 30 September 2016 is consistent with the documents, books and accounts.

ANNEXES

Alternative Performance Measures

In line with the ESMA/2015/1415 guidelines, the Alternative Performance Measures used in the present Interim Financial Report are illustrated below.

MEASURE	DESCRIPTION
ECONOMIC RESULTS	
Gross Operating Margin - EBITDA	this is a measure of operating performance and it is calculated by combining the Operating Profit (EBIT) with Amortisation, depreciation and impairment .
Operating Profit - EBIT	this is a measure of operating performance and it is calculated by combining the Profit before taxes with Net financial income/expenses .
EBITDA MARGIN	this is a measure of operating performance and it derives from the ratio between the Gross Operating Margin (EBITDA) and Revenue .
TAX RATE	this expresses the proportion of tax with respect to the result and derives from the ratio between Income taxes for the period and the Profit before taxes .
EQUITY RESULTS	
Net working capital	this is an equity measure which expresses the company's liquidity situation and it is determined by the difference between current assets and current liabilities of a non-financial nature represented on the balance sheet.
Gross Invested Capital	this is an equity measure which expresses the total of the Group's non-current assets and derives from the sum of Net non-current assets and Net Working Capital .
Net Invested Capital	this is an equity measure which expresses the investments made by the Group net of the contribution of external capital and it is determined by the Gross Invested Capital net of Sundry provisions .
CASH FLOWS	
Net financial debt	this is a measure of the Group's financial structure and it is determined as the sum of the short- and long-term financial debts and the related derivative instruments , net of cash and cash equivalents and of financial assets .
Free Cash Flow	this is the cash flow and it is given by the difference between the cash flow from operating activities and the cash flow for investments .

With reference to the reconciliation of the APMs described above with respect to the IFRS tables, please see the criteria used and described in the context of the annual reporting.

Legislative framework

Below is a brief description of the main recent legislative measures of interest for the Parent Company issued during the third quarter of 2016 and, subsequently, up to the date of preparation of the present Report.

- **On energy**

Decree of the Ministry of Economic Development of 30 September 2016

The MED issued the decree which, implementing Article 1, paragraph 831 of the 2016 Stability Law (Italian Law no. 208 of 28 December 2015) contains the regulation of the Guarantee Fund for the creation of the Interconnectors pursuant to Art. 32 of Italian Law 99/09. The amounts paid in by the selected subjects are added to the Fund and are destined to guarantee all the Interconnectors for which the mandate contract for construction has been signed, starting from the date on which the said contract was signed.

- **On employment**

Italian Legislative Decree no. 159 of 1 August 2016, regarding “Implementation of Directive 2013/35/EU on minimum health and safety rules related to the exposure of workers to risks deriving from physical agents (electromagnetic fields) and that abrogates Directive 2004/40/EC”, published in Official Journal no. 192 of 18 August 2016.

- **On company law**

Italian Legislative Decree no. 135 of 17 July 2016, entitled “Implementation of Directive 2014/56/EU that amends Directive 2006/43/EC concerning the legal auditing of annual accounts and consolidated accounts”, published in Official Journal no. 169 of 21 July 2016.

- **On contracts and infrastructure**

Decree of the Ministry of Economy and Finance of 3 August 2016, entitled “Concession of the State guarantee on financial operations of investment platforms eligible for the European Fund for Strategic Investments (EFSI)”.

The decree, adopted implementing Article 1, paragraphs 822 at seq. of Italian Law 208/15 (2016 Stability Law), establishes the methods with which financial operations of investment platforms eligible for the European Fund for Strategic Investments (EFSI), identified by the national promotion institute (for Italy the CDP), can be assisted by a State guarantee.

- **On the subject of public administrations and public equity investments**

In implementation of the delegated powers contained in Italian Law no. 124 of 7 August 2015, on the reorganisation of public administrations, the following legislative decrees were adopted:

Italian Legislative Decree no. 127 of 30 June 2016, entitled “Measures for reordering the rules on service conferences, implementing Article 2 of Italian Law no. 124 of 7 August 2015”, published in Italian Official Journal no. 162 of 13 July 2016.

The decree reforms the institution of the service conference, an instrument which collected the consent necessary for the adoption of the decrees authorising the works of Terna’s national transmission grid. It is envisaged that normally the event will be held as a video-conference. For more complex projects or when after the video-conference discussions between administrations and proponent is considered necessary, the conference is held in simultaneous mode. In this case, the participation of the different administrations is envisaged with a single representative for each level of government.

Italian Legislative Decree no. 174 of 26 August 2016, entitled “Consolidated Law on companies with public equity investments”, published in Italian Official Journal no. 210 of 8 September 2016.

Operations which entail the purchase by a state administration of equity interests in existing companies are decided with a Prime Minister’s decree, on the proposal of the Ministry of the Economy, after being resolved by the Cabinet.

Italian Legislative Decree no. 97 of 25 May 2016, “Revision and simplification of the provisions on the prevention of corruption, on openness and transparency, amending Italian Law no. 190 of 6 November 2012 and Italian Legislative Decree no. 33 of 14 March 2013 pursuant to Article 7 of Law no. 124 of 7 August 2015, concerning the reorganisation of the public administrations”, published in Official Journal no. 132 of 8 June 2016.

AEEGSI Resolutions

Below is a short summary of the main resolutions passed by the Regulatory Authority for Electricity Gas and Water during the third quarter of 2016 extending to the date of preparation of this Report.

Resolution 342/2016/E/eel - Launch of the proceedings under Regulation (EU) no. 1227/2011 (REMIT), for the timely adoption of prescriptive measures and the assessment of potential abuse in the wholesale electricity market

With Resolution 342/2016/E/eel the Authority ordered the opening of a procedure under Regulation (EU) no. 1227/2011 (REMIT), for the timely adoption of prescriptive measures and the assessment of potential abuse in the wholesale electricity market. In launching this procedure, in addition, the Authority also:

- gave notice to any users of despatching involved in this, to cease any conduct aimed at the adoption of programming strategies that are inconsistent with the principles of diligence, prudence, skill and forethought, and any behaviour involving offers likely to alter the proper price formation process in the electricity markets, including effects on the behaviour of market participants which act according to reference prices, because such conduct may potentially be construed as market manipulation under Article 5 of the REMIT;
- mandated Terna to consider the possibility of future procurement of dispatching resources in order to minimise and stabilise dispatching charges, and to transmit the results of its considerations to the Authority.

With Resolution 459/2016/E/eel the Authority launched new proceedings under the terms of the aforementioned REMIT regulation in relation to further users of the dispatching with respect to those already identified with Resolution 342/2016/R/eel.

Resolution 353/2016/R/eel - Adjustment of the supplementary fee covering generation costs for the units essential for the security of the electricity system subject to cost coverage

With this measure the Authority modified, starting from 1 July 2016, the unit price to cover the costs of essential plants admitted to cost coverage, setting it at 0.2225 c€/kWh. This price was adjusted to the revenue needs envisaged for the year 2016, updated to take into account that the essentiality system pursuant to Italian Law Decree 91/14 will be applied for a shorter period considering the entry into operation of the Sorgente-Rizziconi.

Resolution 358/2016/R/eel - Provisions on the subject of attribution, to the Integrated Information System, of the activity to aggregate the measurements of withdrawals for settlement purposes, with reference to electricity withdrawal points treated on an hourly basis

With this measure the Authority acted to amend the Integrated Settlement Rules (ISRs) in order to transfer to the Integrated Information System (IIS), starting from the accrual month January 2017, the aggregation activity of the measurement of the withdrawal points treated on an hourly basis and of the corresponding points at public lighting plants not treated on an hourly basis, an activity currently performed by the distributor companies. The transfer of this activity to the IIS is part of the wider reform of the processes and management procedures of the electricity measurement data under the scope of the IIS.

Resolution 424/2016/R/eel - Simplification of the procedures for the technical and economic conditions for connection to the grids with obligation of connection of third parties of the electricity production units

With this measure the Authority introduced amendments to the Integrated Rules on Active Connections (IRAC), defining the methods of implementation in the GAUDÌ system of the flows related to putting into conservation, reactivation and decommissioning of production plants, which will be applied from 1 January 2017. The Authority instead put off to a subsequent resolution the changes to the IRAC relating to simplification of the procedures for connection in the case of small production plants, in consideration of the information received from the Ministry of Economic Development on the launch, by the end of 2016, of an investigation of the subject and the consequent adoption of the related measure.

Resolution 442/2016/R/eel - Methods of updating the records of Closed Distribution Systems

With this measure the Authority supplemented the regulation of closed distribution systems (CDSs) pursuant to Resolution 539/2015/R/eel (Annex A - Integrated Rules on Closed Distribution Systems- IRCDSs) in order to make it effective starting from 1 January 2017 and therefore defined the methods for updating the records of the CDSs (that is to say of internal user grids (IUGs) and other private grids), specifying what information must be made available, to what subjects and with what timing.

Resolution 444/2016/R/eel - Priority actions on the measurement of effective imbalances in the context of electricity dispatching

With this measure the Authority introduced a new system for measuring effective imbalances in the context of dispatching services with gradual application, starting from 1 August 2016, in order to provide incentives to the users of the dispatching to programme correctly the quantities of electricity on input and withdrawal. The measure, while awaiting an organic and overall reform of dispatching services, introduced, in fact, mechanisms aimed at providing a more effective incentive to plan with diligence, expertise, prudence and foresight, and to enable the Authority to detect in a systematic manner possible breaches of this obligation, also for the purposes of adopting the prescriptive and/or sanction measures.

Resolution 458/2016/R/eel - Regulation of the electricity measurement activity. Approval of the Integrated Rules for regulation of the Electricity Measurement activity (IREM)

With this measure the Authority approved the “Integrated Rules of the Authority for Electricity, Gas and Water for regulation of the Electricity Measurement activity” (IREM) with which it acted to rationalise the regulation of electricity measurement activity, integrating in a single measure the regulation of measurement of energy put in and withdrawn and of energy produced, revising the underlying definitions and responsibilities for the different operations that make up the measurement activity.

Resolution 461/2016/R/eel - Rules on the subdivision of the main grid into zones

With this measure, in order to take into account the entry into force of Regulation (EU) 2015/1222 of the Commission (CACM Regulation) and the criteria and methods provided for therein for the revision of the zonal configuration, the Authority established that the current zonal configuration of the main grid would be extended for the whole of 2017 and that Terna should send to the Authority by 31 January 2017:

- the methodology for revision of the market zones, updated to take into account the criteria pursuant to Article 33 of the CACM Regulation;
- the alternative zonal configuration proposed for the three years 2018-2020, and a technical report containing the results of the assessment of these configurations.

Resolution 462/2016/R/eel - Rules on the essential unit Ottana Biopower. Amendments and supplements to the Authority's Resolution 111/06, on essential plants for the security of the electricity system

With this measure the Authority made some changes to the remuneration systems for essential plants and determined the values of some of the significant parameters for the application of the typical systems to the essential unit Ottana Biopower.

Resolution 495/2016/E/eel - Approval of an inspection of the electricity transmission company, on the subject of service quality

With this measure the Authority approved an inspection of Terna, to be carried out by 31 December 2016, on the subject of service quality, according to the methods defined precisely in the measure. In particular, the inspection operations, completed during October, regarded the correct application of the obligations to record outages and of the calculations of energy-not-supplied indicators, communicated to the Authority during 2016, and were carried out by the Authority's personnel and by the Finance Police.

Resolution 498/2016/R/eel - Verification of conformity on the proposed amendments to the code of transmission, dispatching, development and security of the electricity grid

With this measure the Authority approved the proposed updates of the chapters and annexes of the Grid Code transmitted to Terna following the consultation (Chapters 1, 3 and 7 and Annexes A.22; A.23; A.24; A.33; A.34 and A.60), considering this documentation consistent and compliant with the provisions of Resolution 558/2015/R/eel and of the dispatching rules.

Resolution 499/2016/I/eel - Congestion income at borders: report under the terms of Article 6, paragraph 6.5, of Annex I to Regulation (EC) 714/2009

With this measure the Authority highlighted, under the terms of Annex I of Regulation (EC) 714/2009, the congestion earnings deriving from allocation of the interconnection capacity on borders of the portion due to the Italian system and of the related use. In particular, data are provided in relation to the monthly balance of the earnings and expenses deriving from the assignment procedures of the transfer capacity on the interconnection network with foreign countries for the period July 2015 – June 2016, as transmitted by Terna. The Authority also confirmed that these earnings are used by Terna in line with the purposes provided for in Article 16, paragraph 6, of Regulation (EC) 714/2009.

Resolution 519/2016/R/eel - Decisions on the request for admission to the cost coverage system in the Sardinia zone

With this measure the Authority admitted to the cost coverage system the Ottana Biopower plant for the period 1 October 2016 – 31 December 2017, established that the fixed costs are to be paid in a manner proportional to the days of admission to the system and permitted Ottana Energia to propose an alternative method on making a request for payment of the said costs. The Authority also specified the criteria for determining the unavailability rate of the plant in 2016, in take into account the admission to the system for only one quarter of the year.

Resolution 530/2016/R/eel - Approval of the rules for allocating the cross-border transport capacity valid for the year 2017

With this resolution the Authority approved the Harmonised Auction Rules (HARs) of 2017, that is to say the rules valid for allocation in 2017 of the transfer capacity on the interconnection network with other countries, which were drawn up by the Transmission System Operators, including Terna, in the context of ENTSO-E (European Network of Transmission System Operators for Electricity). These rules are adopted in the context of the voluntary and advance implementation of the rules of the European Forward Capacity Allocation Regulation (Regulation EU 2017/1719).

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00156 Rome Viale Egidio Galbani, 70
Ph. +39 06 83138111