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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Hydro One Limited's Fourth Quarter 2022 Analyst Teleconference. (Operator Instructions) I would now like to introduce your host for today's conference, Mr. Omar Javed, Vice President, Investor Relations at Hydro One. Please go ahead.

Omar Javed ***Hydro One Limited - VP of IR***

Good morning, and thank you for joining us in Hydro One's quarterly earnings call. Joining us today are President and CEO, David Lebeter, and our Chief Financial Officer, Chris Lopez. In the call today, we will go over our quarterly and annual results and then spend most of the call answering as many of your questions as time permits. There are also several slides that illustrate some of the points we'll address in a moment. They should be up on the webcast now, or if you're dialed into the call, you can also find them on Hydro One's website in the Investor Relations section under Events and Presentations.

Today's discussions will likely touch on estimates and other forward-looking information. You should review the cautionary language in today's earnings release and our MD&A, which we filed this morning regarding the various factors, assumptions and risks that could all cause our actual results to differ as they all apply to this call. With that, I'll turn the call over to our President and CEO, David Lebeter.

David Lebeter ***Hydro One Limited - President, CEO***

Thank you, Omar. Good morning, and thank you for joining us for our fourth quarter earnings call. This morning, I will talk about our fourth quarter, our annual achievements and a look forward. Chris will then take you through the financial results in greater detail. I'm excited to take on the role of the CEO of Hydro One and to continue to work with all our employees across Ontario. As many of you know, I've been the COO at Hydro One for the past 3 years and have seen first-hand the hard work and dedication that our teams bring to our organization every day.

Together, we have achieved great success, and I'm confident that we will continue to successfully execute our strategy in the years to come. Our top priorities as CEO will be to maintain our focus on safety, meet our customers' expectations, drive operational excellence and invest in our teams to ensure we have the skills and capabilities to meet the demands of the future. In short, we will continue to focus on executing our strategy. As we move into 2023, I want to assure our employees, shareholders, partners and stakeholders that the transition from Bill Sheffield's leadership to mine is smooth and seamless. Our priority is to maintain the momentum.

I am proud of the results we have achieved. Our strategy, people, culture and values are what have made Hydro One successful. I'm committed to building upon that foundation, delivering on our promise to our customers and stakeholders. In Q4, we built on the momentum of the first 3 quarters and achieved outstanding safety results. Our focus on and commitment to protecting the well-being of our employees has truly paid off as demonstrated by a record low recordable and serious incident. I am proud of the dedication and hard work that has gone into making our workplace safer. While we have made good progress, we have much more work to do. Safety will always be a priority as we continue to make the workplace safer.

In 2022, Hydro One achieved our best safety results ever and made significant progress to preventing life-altering injuries and fatalities.

Our workplace was safer in 2022 than has ever been because we had a good plan, the safety improvement plan, which we created with our employees 2 years ago and because the entire organization was committed to that plan, the results speak for themselves. Hydro One's recordable injury of 0.616 for 200,000 hours is well below the world-class benchmark of 1.0. Hydro One saw a significant improvement in the number of high energy serious injuries over 2021, with only 1 employee to sustain the high-energy serious injury in 2022 compared to the 4 in 2021.

This equates to a high-energy serious injury and fatality or HSIF rate of 0.012 per 200,000 hours, well below our annual target of 0.066. We are well on our way to eliminating all serious injuries and fatalities by 2024. Our safety results are even more impressive when considered in relation to the adverse storms of 2022. Our crews who are committed to provide the highest level of service to our customers, restored power to nearly 760,000 customers after the Toronto storm in May and spent weeks in Maritime Canada rebuilding their system after post tropical storm Fiona and then restored power to approximately 550,000 customers during the December holiday season storm.

While these storms adversely impacted our reliability statistics, I am pleased to report there were no recordable incidents during those events. In addition, we were once again recognized by the Edison Electric Institute for our efforts following the May derecho. This is our 13th Edison Electric Institute Award. In late November, the Ontario Energy Board approved our 5-year Joint Rate Application. This is a culmination of years of work for many people and established a clear path forward. The rate application was approved because through the largest customer outreach ever, we knew what Ontarians wanted.

We demonstrated year-over-year productivity savings; we were responsive to the concerns from interveners and had built an investment plan which met the evolving needs of our customers while keeping pace at the maintenance and growth needs of the transmission and distribution system. We believe this plan will benefit all Ontarians by ensuring we are able to provide safe and reliable electricity for years to come.

I also want to recognize our regulators, the Ontario Energy Board for their constructive process. It is only because we submitted a strong investment plan into a robust regulatory process in which all participants, interveners, the Ontario Energy Board regulators and Hydro One displayed a high level of cooperation that such a complex case was settled so quickly. Now that the approval is behind us, it's all hands-on deck, executing our investment plan and delivering on our promises to our customers and stakeholders. I have no doubt that every person in Hydro One will continue to execute their work to the best of their abilities.

Once again, we met our capital investment commitments. This year, we deployed $2.132 billion of capital and in-service $2.267 billion of assets. I am pleased to say we have done this while being extremely mindful of costs. Every dollar we invest comes at a cost to our customers, which is why we are committed to spending wisely and continually improving productivity. In 2022, we achieved productivity statements of $374 million, which represents an 8.6% increase year-over-year. Total productivity savings since 2015 now amounts to almost $1.5 billion. This is a remarkable effort, especially considering inflationary pressures faced this past year.

We operate in the traditional and 3D territories of more than 100 indigenous communities. In 2022, we were proud to announce a historic partnership model, First Nations when building new transmission lines. This partnership model reflects our commitment to reconciliation, sustainable development, inclusivity and being a responsible corporate citizen. By working together, we aim to create long-lasting benefits from indigenous people, Ontarians and Hydro One. The Hydro One equity model offers First Nations a 50% equity stake in new transmission line projects with a value exceeding $100 million and will transform the benefits of infrastructure development for First Nations. We believe that this collaboration sets an example for the industry and demonstrates the power of listening, respect and seeking mutually beneficial outcomes in infrastructure development.

As part of our commitment to being a trusted partner of indigenous communities, this year, we also increased total procurement with indigenous businesses to $95.9 million, our highest spend to date. This is a significant increase from last year and has us well on our journey to purchase 5% of our materials and services from indigenous businesses by 2026. The indigenous procurement target is one of the many goals that are included in our updated sustainability report that was released in August. At Hydro One, we take our commitment to people, planet and community seriously, and we'll continue to keep you informed of our annual progress report.

Following the release of the sustainable linked pricing on our lines of credit in January 2022, we recently published our sustainability financing framework in January 2023. The framework, which is a first for a utility in Canada, allows Hydro One and its subsidiaries issue sustainable financing instruments such as sustainable and green bonds and allocate the net proceeds to investments in eligible green and social project categories. The framework was so well received that we issued Hydro One's first medium-term notes in accordance with the sustainability financing framework. This was the largest aggregate amount in issuance of sustainable bonds by a corporate issuer to date in Canada.

Looking out for our people, planet and communities is ingrained in the DNA of our organization. Hydro One employees personally raised approximately $1.6 million in the annual power to give month last September, more than doubling what was raised the year before. There's this commitment to serving others and doing the right thing that makes Hydro One such a special place to work. For the eighth consecutive year, Forbes recognized Hydro One as one of Canada's best employers. It's an honor for me to lead this committed and dynamic group of people.

Looking ahead, I see tremendous opportunities for Hydro One. Ontario and Canada are building an economy more reliant on clean electricity. The independent electricity system operator or ISO, estimates that obtaining a decarbonized electricity sector by 2050 will require a system more than double the size it is today at an estimated cost of around $400 billion. Hydro One has the unique opportunity to be a leading player in achieving that goal. As I take on the leadership role of Hydro One, my top priorities are: one, ensure our safety journey continues; 2, fill the vacancies on our executive team; and 3, remain disciplined in executing our maintenance and capital investments.

As I conclude my remarks, I want to thank Bill Sheffield, who stepped in from the Board as Interim CEO when the company needed him. Bill, I know you're listening to today's call. On behalf of the company, the executive team and myself, I want to thank you for your service to the company, its shareholders, partners, customers and stakeholders. Your leadership and dedication to ensuring a smooth transition has not been unnoticed and I'm truly grateful for your unwavering support. Your guidance has been invaluable and has set a strong foundation for my role as incoming CEO. I'm confident that your contributions will have a lasting impact on Hydro One, and I'm eager to build on the progress that you have made. With that, I'll turn it over to Chris to discuss our financial results. Over to you, Chris.

Christopher Felix Lopez ***Hydro One Limited - CFO***

Thank you, David. Good morning, everyone, and thank you for joining us today. David, I'd like to extend my sincere congratulations on your appointment as CEO. Your leadership, strategic vision and passion for excellence have been evident in your previous role, and I'm confident that you will bring that same energy to this new role. Your unwavering commitment to our mission and values will be instrumental in driving the company to new heights. I look forward to working with you and our talented team at Hydro One as together, we continue to strive towards achieving our goals and creating long-term value for our stakeholders. Once again, congratulations.

In terms of our financial results for the quarter, earnings per share was $0.30 compared to $0.27 last year. For the full year, EPS was $1.75 compared to EPS of $1.61. The main drivers of the higher earnings this year were consistent with our experience throughout the year. They were higher revenues on account of approved rates, which considered our annual investment in the grid and power system, strong electricity demand experienced throughout the year and recognition of conservation demand management or CDM revenues, a onetime item in the fourth quarter. These rises were partially offset by higher operations, maintenance and administration or M&A expenses on account of higher work program expenditures, including environmental management and line maintenance and IT initiatives.

Higher depreciation, amortization and asset removal costs due to the growth of our capital assets, partially offset by the sale of surplus property, a onetime item in the fourth quarter. Higher year-over-year financing charges due to the recognition of carrying charges for the deferred tax asset or DTA recovery amounts last year and higher interest rates on short-term notes as well as higher income tax due to increased pre-tax earnings, partially offset by higher deductible timing differences.

As a reminder, we adjusted for the amounts pertaining to the DTA implementation decision in both revenue and income tax, making them net income neutral. Similarly, we had a tax recovery relating to the capital overhead tax variance in both transmission and distribution following the joint rate application or JRAP decision which resulted in a reduction in both revenue and income tax, once again making this net income neutral.

While our costs were higher this year, I did want to echo David's comments that we continue to be highly productive. As a result of our efforts, we were pleased to give back approximately $23.5 million to our customers via the earnings sharing mechanism as both our transmission and distribution businesses performed very well this year. On the productivity front, we achieved $374 million in productivity savings in 2022, which brings our cumulative productivity gains since the initial public offering to approximately $1.5 billion. We saw meaningful increases in productivity in areas such as operations and forestry. Overall, productivity was weighted evenly between capital and OM&A. Through these achievements, we are delivering on our multiyear commitment to keep costs as low as possible.

Turning to the fourth quarter, net income to common shareholders was higher year-over-year by 11.9%. Key drivers of the quarter were: higher revenues due to approved rates, 2 onetime items, one in revenue and one in depreciation, as mentioned previously and upon which I will elaborate further during this call as well as lower taxes, which was partially offset by higher OM&A. Our fourth quarter revenue net of purchase power was higher year-over-year by 11.8%. The increase is mainly due to revenues resulting from the Ontario Energy Board or OEB approved 2022 rates as well as regulatory adjustments, including the recognition of CDM revenues following the receipt of the JRAP decision, net of earnings sharing.

For the transmission segment, revenues were higher by 14%. This increase reflected the recognition of the onetime CDM revenues arising from the JRAP decision on account of the disposition of the variance account associated with CDM revenues from 2018 and 2019. Going forward, we do not expect there to be any material amount for CDM revenues from prior years as this account is now closed. The CDM revenues were partially offset by higher earnings sharing adjustment for 2022 that is recorded in the fourth quarter. Additionally, we had higher transmission revenues due to OEB-approved rates for 2022. Year-over-year peak demand for the quarter was relatively flat, driven by marginally weaker demand in all 3 months compared to the same period last year.

For the Distribution segment, revenues net of purchased power were higher by 9.9%. The main drivers were the OEB approved rates and positive regulatory adjustments net of earnings sharing for 2022 compared to last year. Consistent with the annual analysis, both the transmission and distribution segments had net income-neutral items included in revenue resulting from the DTA implementation decision and the capital overhead (inaudible). The corresponding offsets are in tax expense, making them net income neutral.

On the cost front, operating maintenance and administration expenses were higher year-over-year by approximately 39%. This represents approximately 75% of the annual increase in M&A. M&A was higher in the transmission segment due to higher work program expenditures, which included maintenance and stations in line, higher corporate support costs and higher property taxes, which were partially offset by lower project write-offs. In the distribution segment, OM&A was higher due to higher work program expenditures that included a higher volume of emergency restoration and environmental management, higher spend on IT and customer programs as well as higher corporate support costs and project write-offs in comparison to last year. The level of OM&A expenditure is consistent with our expectations that have been outlined in previous calls as we caught up with our work programs that were deferred on accounted storms earlier in the year.

Depreciation expense for the fourth quarter was lower year-over-year by 6.5% due to a onetime gain realized on the sale of surplus property to the city of Toronto to facilitate transit. This was partially offset by higher depreciation from the increase in capital assets, which is consistent with our stated capital investment program and higher asset removal costs. On financing, we saw an increase of 4.1% in interest expense in the quarter due to a higher weighted average rate on short-term notes, partially offset by gains on interest rate swap agreements.

As I'd mentioned, on January 12, 2023, we announced our sustainable financing framework. Under this framework, we can issue green, social or sustainable bonds, loans or commercial paper for several purposes. The use of proceeds allows us to raise financing for initiatives, including the transmission and distribution of Clean Energy, smart grid technology and other uses that promote energy efficiency, facilitation of clean transportation, including EVs, biodiversity conservation, climate change adaptation, socioeconomic advancement of indigenous peoples and access to essential services like broadband.

On January 27, 2023, Hydro One Inc. issued an inaugural offering of $1.05 billion of medium-term notes under the sustainable financing framework. This consisted of $300 million maturing in 2029 with a coupon rate of 3.93%, $450 million maturing in 2033 with a coupon rate of 4.16% and $300 million maturing in 2053, with a coupon rate of 4.46%. This was the largest aggregate corporate sustainable bond issuance in Canada and a further demonstration of our strong commitment to sustainability. We continue to be pleased with the stability of our balance sheet and robust investment-grade credit rate. As we look forward, we will continue to access the debt markets opportunistically.

Income tax expense was $41 million for the quarter compared to $55 million in the same quarter last year. The decrease in income tax expense was due to higher deductible timing differences and net income neutral items that are also catching revenues. These were partially offset by taxes on higher earnings for the quarter. The effective tax rate this quarter was 18.6% versus the effective tax rate last year of 25.5%. On a full year basis, income tax expense for 2022 was $288 million compared to $178 million in 2021. The increase in income tax was primarily due to the net income neutral items discussed earlier and higher pre-tax earnings, partially offset by higher deductible timing differences.

The effective tax rate for 2022 was 21.4% versus 15.5% in 2021. This is consistent with the annual guidance we provided last year of 14% to 22% over the next 5 years. Following the approval of the joint rate application and the corresponding capital plan, we are now updating the ETR guidance to 13% to 16% over the next 5 years, with the most significant impact occurring in 2023 due to the recovery of the previously shared DTA amounts.

Moving to investing activities, capital investments for the fourth quarter were $570 million, which is a 7.1% increase from the fourth quarter in 2021. The increase came primarily from the distribution segment, which had a higher spend on storm-related asset replacements and higher volume of work on customer connections. There was a marginal increase in the transmission segment, which had a higher volume of refurbishment and replacement work on transmission stations and lines and a higher volume of work on wood poles. This was partially offset by a lower volume of work on customer connections.

For the full year 2022, capital investments were relatively flat with a 0.3% increase compared to the full year 2021. You'll also note that the future capital investment profile for both segments have been updated since our last call. The primary reason being to reflect the adjusted timing and pacing of future capital investments and reprioritization of work. The overall increase in transmission capital reflects the projects that are outside of the joint rate application.

In the fourth quarter, we placed over $1 billion of assets in service for our customers, a 38.7% increase compared to the prior year. The year-over-year increase in the transmission segment of 44.7% related to completion of large replacements for end-of-life air blast circuit breakers, higher customer connections, timing of IT initiatives and refurbishment and replacement of transmission line. In the distribution segment, the 26.8% increase was on account of the partial in-servicing of a feeder development project, storm-related asset replacements and miscellaneous assets placed in service for IT initiatives and customer connections. On a full year basis, assets placed in service were higher by 29%.

On guidance, as most of you know, we are unique in the Canadian utility sector because we provide earnings guidance along with projected rate base and targeted dividend growth estimates. This not only demonstrates the confidence we have in our ability to execute, but also the stability and predictability of our earnings in our business. As promised, we updated our only guidance to reflect our view of the next 5 years. We have also provided normalized earnings for 2022, which can be used as a waypoint for our guidance. The updated slide is available in the investor presentation that is posted on the website.

Our view of normalized basic EPS is $1.61 after adjusting for items that we view as non-recurring and for rebasing due to the new base period commencing in 2023. Starting at the 2022 reported EPS of $1.75, we made 2 adjustments for onetime items that we discussed earlier on this call. The gain on sale of surplus properties sold to the city of Toronto and the recognition of the disposition of the CDM revenues that were approved as part of a joint rate application. The resulting figure is an EPS of $1.67 that has been normalized for onetime items. This is slightly above the target of 4% to 7% EPS growth, a possibility we communicated in last quarter's call. We then normalized earnings to factor in the allowed return on equity or ROE for both segments as well as 100 basis points of potential overhead. This step is necessary to rebase for all the productivity savings, favorable demand and impact of low interest rates that will now benefit customers in the next rate period.

The rebasing is a great example of a constructive regulatory incentive rate-making model that has worked as intended to deliver positive outcomes for the long-term benefit of the customer. The resulting normalized EPS for 2022 is $1.61. With that last point in hand, we move to the future. We're updating our guidance in introducing a range of EPS for 2027 of $2.05 to $2.26. This range translates into a compound annual growth rate of 5% to 7% over the period 2022 to 2027, on normalized EPS of $1.61 in 2022.

The long-term projected rate base growth currently stands at 6%, and it could be expected that dividends with the approval of the Board of Directors, would follow this level of rate base growth. Finally, we anticipate funding this growth through internally generated cash with no need for external equity issuance. As important as it is to know the growth figures, it is equally important to know what is not included in this forecast and how we intend to update it. The EPS growth range does not factor in growth from broadband, LDC consolidation and 5 of the 6 transmission loans that have been previously awarded to us but only have preliminary estimates as well as any amounts from externally driven variance accounts. We will update guidance if there is a material change to the growth range when we have further clarity and concrete estimates on these specific initiatives.

Furthermore, we will not provide quarterly or annual reconciliations going forward, unless there are material events that impacted the guidance discussed here. We also don't expect to provide rolling guidance. Future guidance is expected to mirror the term of the rate piles. This is an exciting time for Hydro One. We have a strong culture of performance. This has proven through our historical ability to deliver on our predictable capital plan and our ability to realize significant operational efficiencies year-over-year. We have plans to grow our business through investment in our aging assets and in support of the growing Ontario economy. Lastly, we have a strong balance sheet that provides stability and underpins our growth plans. I'll stop there, and we'd be pleased to take your questions.

Omar Javed ***Hydro One Limited - VP of IR***

Thank you, David and Chris. We ask the operator to explain how they'd like to organize the Q&A polling process. In case we can't address your questions today, my team and I are always available to respond to follow-up questions. We ask that you limit your questions to one question and one follow-up. If you have any additional questions, we request you to re-join the queue. Please go ahead.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Robert Hope with Scotiabank.

Robert Hope ***Scotiabank Global Banking and Markets, Research Division - Analyst***

David, the question is for you. What has been your focus in the first few days as CEO? And as you look forward, I do appreciate kind of the priorities that you did lay out in your prepared remarks. But diving into that a little bit deeper, any areas where you want to focus on more than has been a focus in the past?

David Lebeter ***Hydro One Limited - President, CEO***

Robert, thank you for joining us on the call today. Clearly, my focus in the first few days, weeks in this role have been re-establishing the executive team, filling the vacancies that we do have and I'm very confident we're going to be able to fill them from internal. We have a strong bench strength of people coming up within the organization as was evidenced by my promotion into the CEO role.

In terms of the other priorities, there's not much more detail I'd like to actually provide. Safety continues to be a paramount focus for us. It's been a long-term goal of ours to reduce all fatalities and serious injuries and one which I indicated in my prepared remarks that we're well on our way to, and then maintaining our focus on delivering or executing on our maintenance and capital programs. That is really our priority, and that's how we live up to our promise to our shareholders, our stakeholders and our customers.

Robert Hope ***Scotiabank Global Banking and Markets, Research Division - Analyst***

And then maybe a little bit more of a detailed question. On the broadband opportunity, you spoke quite a bit about that with your last quarter results. When you take a look at the opportunity set in front of you, how are the opportunities coalescing? And when would you expect to see meaningful capital being put to work on that opportunity?

David Lebeter ***Hydro One Limited - President, CEO***

The broadband program, the intent is to have all Ontarians connected up by the end of 2025. Our role in that program is really to facilitate access to our infrastructure, so the Internet service providers can attach their equipment and connect customers. So to that extent, the program is really driven by their pace. We started to see some ramp up in the back half of 2022. We're continuing to see some increased activity right now. We expect that to accelerate through 2023 and onwards towards that completion date of 2025.

Operator

Our next question comes from the line of Linda Ezergailis with TD Securities.

Linda Ezergailis ***TD Securities Equity Research - Research Analyst***

I'm wondering if you could help us understand some of the elements or potential opportunities that are not embedded in your guidance, what could that add potentially to your earnings growth outlook? What's the magnitude?

Christopher Felix Lopez ***Hydro One Limited - CFO***

Linda, it's Chris. Thanks for that. Yes, so what we attempted to do here in the guidance is stay consistent with what we've done previously for 2019 to 2022, which is show the base growth rate, which is what we're showing you here, 5% to 7%, which really tracks the 6% in the joint rate application effectively. So that's the midpoint. Things that can force better or can help us go above that would be earnings above 100 basis point overrun, which is good for everybody if we get there by 2027 because it means that we can give more back to our customers. Savings of interest rates, for example, if we can secure rates that are lower than what was previously secured.

A good example was the reason, one we just did have some benefit on that. So we can continue to do that and time those allocations that would be useful. But I think what you're asking is what additional investments could come in. So broadband was already asked. And I think the question that Robert had was when could we expect some guidance on that number? The more insight we get into the demand program on broadband, that's where we'll have confidence in bringing that forward. I've said in the past, it could be anywhere from -- it's in the hundreds of millions, it's not in the billions. It could be $0.5 billion to $1 billion. We won't know that until we see more of this demand coming through. So that's one example.

The other one is the transmission lines. We said 5 of the 6 are not included. So the only one that's in here right now is Chatham to Lakeshore of $268 million. Again, I don't have an estimate for you today of what each transmission line is worth. You can have an assessment yourself. But again, that can be in the hundreds of millions. And then the final one is the acquisition of LDCs. And it's set out on the slide on the website. And that one there, we target $100 million to $200 million per year. So that can add another certain amount.

And I said that one in the past, for every $100 million that we acquire of rate base, it's about $0.01 accretive. So those items are not in this guidance range. But if they came through in any material way, it would cause us to reissue guidance and it would push us above that range.

Linda Ezergailis ***TD Securities Equity Research - Research Analyst***

And just as a follow-up in your core business, you've got an approved joint rate application. Clearly, some opportunities there to benefit all stakeholders as you execute and implement your plans around that. What are the priorities and the milestones of putting things in place to pivot to that new regime and where do you see the challenges in executing that?

David Lebeter ***Hydro One Limited - President, CEO***

Linda, it's David. I'll answer that question. The joint rate application is very consistent with our previous strategy. We're focusing on our investments, maintaining our assets and new builds as Chris outlined. So there's really no change and there won't be a pivot as we move forward.

Linda Ezergailis ***TD Securities Equity Research - Research Analyst***

And where do you see the biggest challenges like continued inflationary pressures or attracting and retaining the right talent to execute that?

David Lebeter ***Hydro One Limited - President, CEO***

Yes. My apologies, I forgot the second half of your question, so thank you for reminding me. The challenges are, it's actually going to be the inflationary pressure. So far, we've experienced about 6%. It is different by category. I'm really pleased that the way our team has responded to that inflationary pressure. We've looked at alternative sources of supply. We purchased long lead times ahead of purchased long lead time items. A lot of our procurement has locked in rates that are formulaically driven based on the base price of commodities underneath. So that's going to be our biggest challenge in the short term. Talent for us, we're very, very fortunate that in general, we have very low turnover, somewhere around 1%. When we do go to the market to recruit people, we have many people that apply and want to come work for us.

Now there are a few sectors that are a bit more challenging for us, IT, cybersecurity being 2 of them that come to mind. But to date, we've been very successful in filling the vacancies we have in acquiring the talent that we need to continue to deliver on our strategy.

Linda Ezergailis ***TD Securities Equity Research - Research Analyst***

Congratulations on your promotion.

Operator

Our next question comes from the line of Dariusz Lozny with Bank of America.

Dariusz Lozny ***BofA Securities, Research Division - Research Analyst***

First one is I just wanted to maybe reconcile a couple of the statements made in the opening remarks and in your presentation. So I understand that over the long term, you're targeting a 70% to 80% dividend pay-out range. And I think with the dividend update this morning, you're tracking a little bit below that. So curious if you could maybe speak to those dynamics a little bit. As far as relative growth rate of the dividend pay-outs over this 5-year time frame that you laid out the new EPS CAGR for.

Christopher Felix Lopez ***Hydro One Limited - CFO***

Thanks, Dariusz. It's Chris. You're correct. So we didn't have an increase this morning. We've traditionally done that in May and you can expect that to occur in May of this year. We have not changed the target. It is 70% to 80%. There will be an increase recommended to the Board, they'll need to approve it. But there'll be an increase recommended. And I would expect in those remarks, as I said, that the dividend increase would track our rate base growth. So in the past, it's been around 5%, and I expect it to be 6% going forward. So you can expect that in May. And I think that will get closer to your number, Dariusz, I think we're in the low 60s right now. It will take you up into that 70% range. The lower end of that, which, again, we're very pleased with our balance sheet and gives us a lot of flexibility for growth moving forward.

Dariusz Lozny ***BofA Securities, Research Division - Research Analyst***

Great. And actually, you alluded to my second question in your response there. I just wanted to ask about the specific headroom that you have on your balance sheet as far as obviously, we're talking quite a bit about upside 2 year 5% to 7% as far as LDCs, acquisitions, transmission projects, et cetera. At what point assuming that those pieces of upside materialize, would you anticipate needing additional financing, including potentially external equity throughout this 5-year plan?

Yes, so Dariusz, I said earlier, based on the joint rate application itself, no need. LDCs are interesting because we end up getting synergies of them very early on too. They're actually not dilutive to our borrowing capacity. So effectively, for the smaller ones, it's quite supportive of our debt metrics. So we would not need it for the smaller ones. Now if we had a very large capital program on transmission, for example, that's where you might need it, but it wouldn't be in these 5 years because remember, we only balance up equity and debt when we actually put the asset in service. So if new transmission lines are announced beyond the 5 of the 6 that have already been announced, it's unlikely they would go into service by 2027. So the time you would need equity would be on this 5-year period in any case. So I'm fairly confident that the requirement for equity is very low in this period. It's non-existent right now. I don't see a position where that would come in the next 5 years.

Operator

Our next question comes from the line of David Quezada with Raymond James.

David Quezada ***Raymond James Ltd., Research Division - Director & Equity Research Analyst***

Yes. Just one for me. Just curious, when you look over your coming 5 years and thinking about, I guess, things that are not in your capital plan, I know that in the province of Ontario, there's new storage capacity that's going to be integrated, potentially some additional renewables and other generation sources. So I'm just curious if you see any opportunities there incrementally over and above your current plan or guidance from integrating those new generation sources in storage.

David Lebeter ***Hydro One Limited - President, CEO***

David, it's David. There will be opportunities as we move forward and the future becomes clear. So right now, we do have some battery storage within our own joint rate application. As always, we will always connect customers, whether they be load customers or generation customers that come along. And as you can imagine, the energy transition or electrification of Ontario's economy is really just starting to pick up steam. So we're watching all this and we're paying attention to it. And we're really excited by the ISO, independent electric system operator's report on pathways to decarbonization. And that points to, as you pointed out rightly so, increased investments in batteries and renewable generation.

So we're following all that. We're in active discussions with the ISO as well as the Ontario Energy Board as well as the province of Ontario and how this plays out. So we remain an active participant and a facilitator.

Christopher Felix Lopez ***Hydro One Limited - CFO***

I think, David, just one thing to add to that would be that similar to the question we had earlier on when would those material investments come up and even in pathways, a material amount of that opportunity will be outside this 2027 period. So when we're providing guidance today to 2027, we will update that on our next application as well as we've done in the past. And that's when you could expect to see more of those kinds of opportunities come out. There's more and more discussion on them. There are more announcements being made, but it's still going to take time for those investments to be made and put into the system.

Operator

(Operator Instructions) Our next question comes from the line of Maurice Choy with RBC Capital Markets.

Maurice Choy ***RBC Capital Markets, Research Division - MD & Analyst***

Just want to follow up on the guidance range. Chris, you mentioned that the approach in designing this guidance is the same as when you put out the 2022 guidance. And in deriving this $1.61 normalized EPS of 2022, you've removed $0.06 for 100 basis points over earned. When we look at the $2.05 and $2.26 for 2027, does that include the 100 basis points over earned or put differently, any reason why we shouldn't expect you to also deliver this over the next 5 years?

Christopher Felix Lopez ***Hydro One Limited - CFO***

Maurice, thanks for the question. The 100 basis points is in both numbers. So in the guidance we put forward back in 2019, we took it out of the starting number, and we left it in the back end, and that sort of tilted the growth rate up. So in this one here, we have left a 100 basis points in the base year, and it's in the final year as well to show we may not reach it in every year, but we would expect that over 5 years, you would absolutely reach that number, and that's part of incentive rate making is that we are encouraged to do that or incentive to do it because our customers benefit from it in the future. So in short, Maurice, it's in both numbers, and we're committing to achieving that for the benefit of all stakeholders.

Maurice Choy ***RBC Capital Markets, Research Division - MD & Analyst***

Perfect. And maybe just a follow-up on the DPS question earlier on about your dividend pay-out ratio. Suppose you get into a situation where your EPS obviously outstrips your DPS growth, when you think about the next 5 years and the propensity for this to be perhaps on the lower end of your dividend pay-out ratio, what will propel you to or motivate you to consider increasing that rate or even changing your target pay-out ratio to be perhaps closer to some of your peers south of the border?

Christopher Felix Lopez ***Hydro One Limited - CFO***

Yes. So I think, Maurice, it's always a matter for the board and I guess the lucky position of recommending what we should do, that the board will approve it. My thought to this that look, it's a way of financing new growth. We don't have any restriction right now on how we're going to finance new growth. So the dividend will absolutely match our rate base growth. I could see at 6%, we have no challenge with that. At 7% that still would be okay. So I would see it tracking at that point. It's when you get up, if I think about -- David spoke about ISO pathways and so on, beyond 2027, when you start getting into much higher growth rates that are potentially there, that's when we would think about do you chase the dividend pay-out all the way up or do you use that as a form of financing.

What I would do, I've said it before Maurice is I would consult with our shareholders and all stakeholders to work out what is the best way of financing that growth for the longer term because there are shareholders that depend on the dividend pay-out. So we would look at all forms of financing but I don't see any need to change it at this point. It will be 70% to 80%. I think if rate base went up to 7%, it would chase it to 7%. And we'd look at it as and when needed. So I don't expect any change or departure from that policy in this 5-year period.

Operator

Our next question comes from the line of Mark Jarvi with CIBC.

Mark Thomas Jarvi ***CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research***

I want to come back to the pathways to decarbonization of the ISO report. In 2021, you guys were awarded or directed to advance some transmission projects. Given the sort of grander scope on the pathway to decarbonization, what do you think the process going forward? You expect them just to continue to direct projects as needed or do you think you start to become sort of longer-term planning here that--provide me a bit more visibility in terms of your transmission needs over the next decade?

David Lebeter ***Hydro One Limited - President, CEO***

Mark, this is David here. You're absolutely right. The pathways report lays out some pretty ambitious investments that we need to make for Ontario to decarbonize the electric grid by 2050. In the past, we have seen direct awards to Hydro One. We've also seen direct awards to other organizations with respect to transmission infrastructure. It's unclear at this time how the government plans to award transmission in the future. I know it's a topic they're discussing at Queens Park and what approach they're going to take. We're certainly actively involved participating recommendations but at this point, it really is in their ballpark, and we hope that they decide to award them to Hydro One. But if they were to go down the path of competitive transmission, we're quite prepared to compete with anybody else.

Mark Thomas Jarvi ***CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research***

Okay. And then Chris, coming back to you in terms of some assumptions on the EPS growth. Just can you clarify whether or not there's any change in view in terms of whether financing cost, interest expense is a drag or a net positive? And then maybe just elaborate on your comment around the most recent sustainable financing and the potential positive impact it has in terms of EPS?

Christopher Felix Lopez ***Hydro One Limited - CFO***

Yes. Thanks, Mark. So in short, we're not in this range for us to go above. We got 6% rate based growth, for us to go above 6, a way that we could do that is by achieving better all-in financing costs. So it's not included in the base number, but it's included in the range, if you like. It's a way of getting above 6% growth and into the higher end like 7%, for example. And we did quite well in the last period because rates were accommodative. We're fairly confident that opportunities will come. Again, we maintain a lot of flexibility on our balance sheet, so we can do that. So my point, Mark, about this last financing because we managed to time that at the right point. If I was to issue it today, those rates are already 30 to 40 basis points higher than where they were when we did the issuance a few weeks back now.

So capturing those moments throughout the year, if we can do that, and we were very successful in doing that in the last period, if we can do that, we actually get lower all-in rates over this period and it benefits everybody. It benefits our shareholders now because you'll get us through this rate period. And when we go back in for new rates, the rate pay gets the benefit over the longer term. So that's what I was talking about. On the last one, we did the sustainable bond itself, we've got a greenium. So it was pleasing to see that when you do all the work and your good ESG citizen, that there is a benefit to that. And it was 3 to 4 basis points. So again, not a lot, but it shows that there is some spread now for that kind of activity.

And again, all-in lower cost of financing, every time we do this, it's the gift that keeps on giving. It gives today, it gives for the next 5 years for the shareholders. And after that, it gives for the next -- in the case of the 30-year bond, another 25 years to our customers.

Operator

Thank you. And that does conclude our Q&A session for today. I'd like to turn the call back over to Omar Javed for any further remarks.

Omar Javed ***Hydro One Limited - VP of IR***

Thank you, Shannon. The management team at Hydro One thanks everyone for their time with us this morning during what is a busy period. We appreciate your interest and your ownership. If you have any questions that weren't addressed on the call, please feel free to reach out, and we'll get them answered for you. Thank you again, and enjoy the rest of your day.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program, and you may all disconnect. Everyone, have a great day.