

# **Eesti Energia Unaudited Financial Results for Q2 2017**

**28 July 2017  
Transcription**

## **Speaker key**

AA	Andri Avila
OP	Operator

Andri Avila Dear investors, dear partners. My name is Andri Avila, the CFO of Eesti Energia. Welcome to our regular conference call introducing Eesti Energia's quarterly financial results. You can access the presentation of our second quarter results at Eesti Energia website.

On slide 3 we have presented a quick overview of Eesti Energia's second quarter results. You will notice that we had another quarter of improving financial results, with sales revenues growing by 19% and EBITDA by 17% to 64 million euros. The improvement was based on all of three major business segments. Additionally, we had a strong quarter in terms of operating cash flow, which increased 28% year-on-year and amounted to 65 million euros. Eesti Energia's investments were essentially flat in annual comparison at 31 million euros.

Moving to slide 4, let's have a look at the performance of our major commodity markets. The power price in Nord Pool Estonia area equalled 30.8 euros per MWh in the second quarter, representing a small 2% decrease year-on-year. The price was almost equal in Estonia and Finland. The commissioning of the NordBalt cable between Lithuania and Sweden has contributed to the convergence of power prices between Estonia and its southern neighbours Latvia and Lithuania. In the second quarter the price difference between Estonia and Latvia amounted to 3.2 euros per MWh which is somewhat higher compared to previous quarters due to maintenance works of the NordBalt cable as well as transfer restrictions between Estonia and Latvia. Our clean dark spread against Nord Pool Estonia price increased to 8 euros per MWh, mainly due to continued impact from lower cost of oil shale and lower cost of CO<sub>2</sub>.

Turning to an overview of the oil market on slide 5, you can see that the price of Brent crude oil averaged 49 dollars per barrel in the second quarter, up by 8.5% from the same period last year. The average euro price of our benchmark product 1% heavy fuel

oil increased even more, by 45% to 261 euros per tonne. Fuel oil price has performed better compared to Brent because of local supply-demand conditions on the European fuel oil market and increased arbitrage opportunities to Asia.

Starting with slide 6 we will look at the quarterly financial results in more detail by each segment. It can be seen that Eesti Energia's sales revenues grew by 19% to 177 million euros in the second quarter, supported mainly by increasing revenues from electricity as well as shale oil. EBITDA totalled 64 million euros, a 17% increase from the same period in 2016. Growth in EBITDA was also positively impacted by the electricity and shale oil segments. The negative contribution from the „other“ segment mainly reflects the one-off positive contribution of 13 million euros, which we had from the retroactive change in the resource fees and environmental taxes in the second quarter of 2016.

On slide 8 let's look at the electricity segment in more detail. Our production and sales of electricity grew substantially in the second quarter. Total sales amounted to 2.3 TWh, up by 35% due to higher wholesale volumes. Total generation volume amounted to 2.4 TWh, up 43% year-on-year. Growing volumes were caused by an improvement in the competitiveness of our power plants as cost of oil shale is lower with the flexible taxation system introduced in July last year. Eesti Energia's average electricity sales price declined by 10% in the second quarter as we generated and sold more power also during the relatively lower priced hours, but the sales price remains definitely higher than the average Nord Pool price. In combination, the changes in the volume and price translate into 82 million euros of sales revenues from power sales, a 24% increase year-on-year. We have also provided in this slide information about the hedge positions which we have entered into for the remainder of 2017 and for 2018.

On slide 9 we continue with the analysis of EBITDA from the electricity segment. Eesti Energia's EBITDA from the electricity

product amounted to 23 million euros in the second quarter. Such level represents a 49% increase year-on-year and it was mainly driven by higher sales volumes. Impact from margins was also positive because although we had a decline in the average sales per MWh our variable cost declined even more. Fixed costs increased so this had a negative impact on profits. The growth in fixed costs was primarily related to more maintenance works in Narva power plants, which was required since the power plants have generated more electricity than projected. Additionally, payroll costs in the mining subsidiary have increased owing to larger mining quantities. A remaining smaller negative effect on EBITDA includes relatively lower result from derivative positions. All in all, it was a good quarter in terms of the financial result for our electricity segment.

Moving next to distribution segment on slide 11, it can be seen that distribution volumes increased by 6% to 1.5 TWh due to colder weather and supportive economic conditions. Average sales price declined by 1.4% which implies together with higher distribution volume that sales revenue from the distribution segment grew by 4.7% to 59 million euros. Network losses remained at a low level of 4.4%. The duration of unplanned interruptions was as at a low level of 21.5 minutes which is substantially lower due to continued efforts on improving the reliability of the grid but also due to favourable weather conditions. We would also like to point out that starting from July this year, the distribution tariffs will decrease by 7% on average.

Moving next to slide 12, it can be seen that the positive effect in distribution sales revenues carries over also to EBITDA. Although the margin impact related to lower decreased average sales price was slightly negative and there was also an increase in fixed costs, higher volumes have a sufficient positive effect and quarterly EBITDA grew by 2% to 30 million euros.

On slide 14 we have presented information on the third large business segment, which is shale oil. You can see that both revenues as well as EBITDA from the oil segment grew extensively compared to the second quarter of 2016, which was a very difficult time on the oil markets and affected our results a year ago. Eesti Energia's sales and production volume grew by 53% and 87% in the second quarter, respectively. Our sales of oil totalled 104 thousand tonnes. As mentioned, oil price development has been positive and Eesti Energia's average oil sales price reflects this trend. The average sales price including the effect from hedge positions equalled 235 euros per tonne, up by 17% year-on-year. Hedge positions contributed a negative of 11 euros per tonne in the second quarter which is an expected development in a time of increasing prices where hedge positions have been entered into at somewhat lower levels. You can also see in the slide that a substantial share of Eesti Energia's oil sales have been hedged for the second half of 2017 and for 2018.

On slide 15 you can see that similarly to oil revenues, also oil EBITDA grew markedly in the previous quarter. Shale oil EBITDA amounted to 7 million euros in the second quarter, compared to -3.2 million in the same period of 2016. Primarily, the positive result from better sales prices and better margins although increase in sales volume and lower fixed costs also provided a positive impact. Gain on derivatives had a negative impact compared to the same period in 2016. Last year there was a small positive result from the hedge positions but this year the hedges had a negative result given that the hedged price was lower than current market price.

On slide 16 we summarise the rest of Eesti Energia's products and services. It can be seen that while the revenues from such other products and services remained at a level of 13 million euros, EBITDA declined by 67%. The explanation is that in the second quarter of 2016 Eesti Energia benefitted from the one off

impact related to the retroactive change in resources taxes and environmental fees which improved last year's result by 13 million euros but of course there was no such impact this year. Part of this effect was reversed by the income from General Electric that is payable as liquidated damages for the delay in the delivery of the Auvere power plant. The amount of these liquidated damages equalled 5.6 million euros in the second quarter of this year. Other changes in the segment results were already more minor. All in all, the combined EBITDA from such one-off items and other products and services totalled 4 million euros.

The following two slides cover Eesti Energia's cash flow development in the second quarter. Firstly, on slide 17 we have presented how operating cash flow builds up compared to the EBITDA of 64 million euros. Impact from CO<sub>2</sub> related items contributed a negative of 32 million euros compared to EBITDA. Usually, Eesti Energia purchases the CO<sub>2</sub> allowances that are required its annual emissions in December of a given year. In 2017 it was decided to purchase the full year's allowances earlier for the purpose of optimising working capital and liquidity. This cash outflow in the amount of 47 million euros is the primary reason why the impact from CO<sub>2</sub> related items was negative in the quarter. However, the effect is intra-year as it would have been necessary to buy the allowances by the end of the year in any case. Various changes in working capital had a large positive effect to cash flow in total amount of 40 million euros. 25 million euros of this is related to the liquidated damages that Eesti Energia receives from General Electric and which were included in EBITDA in 2016 but are only paid monthly now. The rest of the working capital items are mainly related to a reduction in receivables, some of it seasonal and some related to the timing of specific oil shipments. In total, Eesti Energia's operating cash flow amounted to 65 million euros in the second quarter.

Moving on slide 18, it can be seen how the operating cash flow changed in year-on-year comparison. Eesti Energia's operating cash flow grew by 27.5% in the second quarter compared to the same period a year ago. About 9 million euros of this change is explained by higher EBITDA. Another important positive factor is again the change in the working capital where payments in the amount of 25 million euros received from General Electric have a major role. Additional positive contribution was made to working capital by a reduction in receivables and reduction in tax prepayments. On the negative side, CO2 related items had an impact of -42 million euros. As explained in previous slide, we purchased CO2 allowances in the amount of 47 million euros in the second quarter of this year whereas there was no such purchase last year. These were the major drivers behind the increase in the operating cash flow in the previous quarter.

Looking at slide 19, it can be seen that Eesti Energia's capital expenditure was stable compared to a year ago and amounted to 31 million euros. Investments into the distribution network continued as the largest share of the capex, making up about 17 million euros of the total. Other maintenance type of investment increased to 5 million euros as large electricity generation volumes also require somewhat higher level of maintenance and repairs. Regarding Auvere power plant, General Electric continues their work on the filters which needs to be completed before final acceptance of the project and which is scheduled for the autumn of 2017. Meanwhile, the plant continues working at levels possible in order to comply with emissions requirements.

On slide 20 we have provided information on Eesti Energia's liquidity position, which remains very strong. The amount of cash and cash equivalents totalled 386 million euros as at the end of June, supported by strong operating cash flow and relatively small investments. The liquidity buffer is further boosted by revolving credit facilities and unused investment loan with EIB

which gives us a comfortable position ahead of larger debt repayments in 2018.

Moving on to slide 21, it can be seen that Eesti Energia's debt ratios have been improving over the past couple of quarters. Eesti Energia's net debt to EBITDA ratio stood at 1.5 as at the end of June, slightly further down from March. This development is created both by healthy cash flow and declining net debt but also owing to relatively solid 12 month rolling EBITDA. It should however be noted that the rolling EBITDA also includes one-off items such as Auvere contractual penalty from GE, accounted for in the fourth quarter of 2016. Eesti Energia's current ratings were confirmed by Moody's in April and S&P in July. S&P maintained their negative outlook to the BBB rating whereas the rating from Moody's is Baa3 with stable outlook. Regarding the debt maturity profile, some of the EIB loans which were originally due to be paid back in 2019 have recently been paid back in July to manage Eesti Energia's liquidity profile.

Now, let's move on to slide 22, which includes the outlook for the full year of 2017. The outlook remains unchanged compared to our communication given in April with the first quarter results. We still estimate that the sales revenues are likely to grow by less than 5%, whereas EBITDA is forecast to decline by more than 5%. If we make an adjustment for certain one-off positive items which were included in EBITDA in 2016, the result for 2017 is expected to remain at similar level. Capital expenditure is expected to grow this year mainly due to development investments. According to current plans, it is expected that the final payment for Auvere power plant will be made later this year and that the first payments related to the Tootsi wind farm could also already take place in 2017. Regarding dividends, it is currently forecast that the payment to the shareholder will amount to 47 million euros on top of which income tax will have to be paid.



Finally, to conclude our today's presentation, the latest quarter definitely had a solid financial result with all Eesti Energia's major business segments contributing to the improvement in EBITDA. Investments remained at a stable level compared to last year. Financial ratios were at reasonable levels and complied with internal financial policy targets as well as contractual covenants. Thank you for listening, we will now take any questions that you may have.

Operator Ladies and gentlemen, at this time we will begin the question and answer session. Anyone who wishes to ask a question may press \* followed by 1 on their touch-tone telephone. If you wish to remove yourself from the question queue you may press \* followed by 2. If you are using speaker equipment today, please lift the handset before making your selections. Anyone who has a question may press \* followed by 1 at this time. One moment for the first question please.

Operator There are no questions registered. I hand back to Mister Avila for closing comments.

Andri Avila Yes, thank you for listening and I would like to see you again or to be heard again after three months when we announce our third quarter results. Thank you.