Eesti Energia Unaudited Financial Results for Q3 2019

31 October 2019
Transcription

Andri Avila

Dear investors and partners, my name is Andri Avila, CFO of Eesti Energia. I am glad to welcome you to our regular conference call to discuss Eesti Energia's third quarter 2019 financial results. I hope you have had a chance to download the quarterly report and the investor presentation from our web site.

We start from slide number 3 with Eesti Energia's sales revenues that increased by 3% in the third quarter of 2019 reaching nearly 206 million euros. EBITDA in the same period fell by 28% to 42 million euros. EBITDA decline can be tracked down to our oil shale electricity production unit where there were two major root causes. First, our newest oil shale power plant, Auvere, was in guarantee maintenance for the most of the quarter. Secondly, due to high CO2 prices there were one-off expenses in the Large Scale Energy Production unit as a result of restructuring operations carried out during the quarter. Compared to last year operating cash flow during the quarter was down by 48 million euros. The Group's capital expenditure in the third quarter amounted to 34 million euros which was nearly 44% lower than a year ago. We will be reviewing the financials in more detail in the upcoming slides, but before that let's take a closer look at the developments on our main commodity markets.

Turning to slide number 4, it can be seen that third quarter 2019 electricity prices were lower than a year ago. Last year's electricity prices benefited from low hydro levels, and also there were maintenance works of the NordBalt interconnector and Nordic nuclear power plants. In this year's third quarter the average price of Nord Pool Estonia was 48.9 euros per MWh which was 8.5% lower than last year's figure. Electricity price spread between Estonia and Finland in the third quarter of this year increased to 1.4 euros per MWh resulting in higher electricity prices for Estonian consumers. The price difference between Estonia and Finland came down from 5.2 euros per MWh difference seen in the second quarter of this year where the congestion of Finnish-Estonian connections played its role. The electricity price in Latvia was basically on the same level as in Estonia, just 0.1 euros per MWh higher.

The Clean Dark Spread, a metric we use to show the margin available to Eesti Energia's Narva Power Plants after oil shale and CO2 costs, decreased to 1.5 euros per MWh, declining by roughly 90% from last year's third quarter levels. On a yearly comparison basis, most of the impact, specifically 6 euros per MWh, came from higher CO2 prices. Electricity price component decreased by 4.6 euros per MWh and the impact from the cost of oil shale was 3.1

euros per MWh totalling at a decline of 13.6 euros per MWh. Despite the low Clean Dark Spread, we are still able to produce electricity as our Narva Power Plants target electricity production at peak hours where electricity prices are higher than NordPool quarterly average electricity prices.

Continuing to slide number 5, we will now go over the oil market developments. During the third quarter oil prices decreased compared to the levels we saw a year ago. The average price of Brent crude oil fell 18%, while the price of 1% Sulphur content fuel oil, which is the main reference product for our oil products, dropped by 7% to 339 euros per ton. These movements can be explained by talks of slowing global economic growth, and also bigger oil inventories in the USA. Nevertheless, we see good opportunities for shale oil export as the tighter marine fuel sulphur cap kicks in from 2020 which according to our expectation should support European fuel oil market.

Moving to the next slide, slide number 6, let's start the review of Eesti Energia's financial results in more detail. Compared to the third quarter of last year, this year we saw mixed performance of our segments. While shale oil and other activities managed to show increasing revenues and EBITDA growth, our electricity and distribution segments saw both declines. We will now cover the different segments in more detail.

Let's turn the page to number 8 to look at the results of the electricity segment. Eesti Energia's average electricity sales price increased by 5% in the third quarter reaching 54.7 euros per MWh, while the NordPool Estonia average electricity price decreased by 8.5% to 48.9 euros per MWh. The widening difference between our average electricity sales price and NordPool Estonia average electricity price comes from two factors. First, the bigger share of retail sales in the sold electricity sales volume implies higher average electricity sales price because the average sales price of retail contracts is higher than electricity market price on the wholesale markets. Secondly, electricity production at our Narva Power Plants takes place more during peak hours where the electricity prices are higher than NordPool average. Despite favourable dynamics of peak hour prices, Eesti Energia's electricity generation fell more than a half from last year's third quarter levels to 1 TWh due to higher CO2 market price and maintenances of three power units. From the three maintenances, our newest production unit, Auvere, was under unanticipated extended guarantee repairs and will be back operational in November this year. The other two maintenances, regarding the 5^{th} and the 11^{th} unit, took place according to the maintenance schedule. Despite higher average electricity sales prices, sales volume and sales revenue declined by 12.7 and 6 per cent respectively. Wholesale sales volume decreased due to lower electricity generation quantities, while retail sales volume quantities got support from increased sales activity on the Lithuanian and Polish markets. During previous two quarters we have pointed out the production of electricity from renewable and alternative sources which was 25% in Q1 this year, and 33% in Q2. In the third quarter electricity produced from renewable and alternative sources amounted to 41% of total production.

Turning to slide number 9, the EBITDA of the electricity segment fell by 66% from last year's 30 million euros to 10.5 million euros this year. Although during the quarter we benefitted from higher sales price, the effect of which was ca 7 million euros, we also had 24 million euros of higher costs related to electricity purchase costs. The reason here is behind lower production quantities at our Narva Power Plants which meant that we had to buy more electricity from the market for our retail clients leading to higher electricity purchasing costs. Impact from lower energy production quantities, which relate mostly to Narva Power Plants, are covered separately under the factor of volume impact in the amount -8 million euros. On the positive side we saw lower fixed costs at our oil shale related Large Scale Energy Production units, while costs at the renewables and customer services units rose. The renewable unit saw its costs go higher on a yearly basis due to the acquisition of Nelja Energia which took place in last year's fourth quarter, while customer services costs have gone up due to expansion activities in Swedish, Finnish and Polish markets.

Next let's take a look at the results of the distribution segment, which start on slide 11. Distribution volumes during the third quarter of this year were basically on the same level as last year, increasing by 0.8%. Sales revenue of the distribution operations fell by 7% on a yearly basis to 48.5 million euros. As in the first six months of this year, the reason here is the distribution tariff cut which took place in the beginning of this year. The average duration of unplanned interruptions came down by nearly half an hour to 20.8 minutes as this year's third quarter was relatively quiet compared to last year where the month of September was especially stormy.

Turning to the next slide, the EBITDA of the distribution segment declined by 8.7% to 22.5 million euros due to the already mentioned tariff cuts. Slightly higher distributed volumes and lower payroll costs helped to ease the negative impact of lower tariffs.

On slide 14 we continue the overview of the shale oil segment. Eesti Energia's average shale oil sales price, excluding the impact of hedges, declined by 7.8% on a year-over-year comparison to 339 euros per tonne, following the market price movements of 1% heavy fuel oil. Including hedges, the averages sales price increased by 7.1% to nearly 279 euros per tonne as older hedges made at lower price levels are maturing. Sales volume of shale oil increased by 27% to 101 thousand tons on the back of increased sales. Shale oil production was 9% higher than a year ago amounting to 113 thousand tons. Year to date oil production numbers are record high, we have produced 331 thousand tons of oil in the first 9 months this year, up by 11% from last year's figures. These record volumes have been made possible by our Enefit 280 oil production facility which has managed to exceed its projected capacity on a regular basis this year.

Turning to the shale oil's EBITDA on the next slide, we saw a 40% improvement as the EBITDA of shale oil operations amounted to 10.2 million euros. Main contributing factors during this quarter were bigger oil sales volumes, and gain on derivatives, whereas as the margin impact on the back of decreased average sales price without hedges and fixed costs had negative effects. Fixed costs rose due to rise in inventory levels and higher payroll costs attributable to oil operations.

On slide 16, let's cover the contribution of other products and services of Eesti Energia Group. Sales revenue of other products and services grew 87% from last year to 20 million euros in the third quarter. As in previous quarters, the main factor here is the sale of pellets, an operation that we acquired together with Nelja Energia in November last year. During the third quarter gas sales increased by 2.1 million euros as natural gas sales volumes doubled. Coming to the EBITDA impact of other services, the major effect compared to last year comes from Auvere liquidated damages as a year ago in the third quarter the accounting of liquidated damages had a negative impact, whereas this year there have been no such factors. Other changes in EBITDA, which were 0.8 million euros lower than a year ago, are made up mostly from operations of Enefit Solutions, pellet operations, mining products, RnD costs, and gas sales.

Moving on to slide 17, we show the development of Eesti Energia's third quarter operating cash flows from EBITDA. The Group's EBITDA was 42 million euros in the third quarter, while operating cash flows were 37 million euros lower. The largest difference between EBITDA and operating cash flows were caused by changes in working capital where the major contributing factor was the increase in accounts receivables. There are quite a few factors to point out. Firstly, the end of the quarter there occurred shale oil sales with payment dates in the fourth quarter. Secondly, the seasonality of retail sales started to have its effect in the third quarter as the electricity consumption starts to go slightly higher and higher resulting in higher electricity bills for electricity consumers, therefore also increasing our accounts receivables. In addition, there were some larger than usual gas related deals during the quarter as the LNG pricing in our region is attractive, but the impact of the gas deals is in the range of a couple of million euros. On the other hand, CO2 impacts was positive during the quarter as it is mainly related to the non-monetary provisions made in the income statement during the quarter to match the emissions cost of our CO2 emitting energy production. Cash flows related to electricity, oil and gas hedges had a slightly negative impact during the quarter as the collateral requirements for our hedges rose. Interest paid in the third quarter is the largest throughout the year compared to other quarters. This is because of our 500 million Eurobond with maturity date in 2023 that has its annual coupon payment date in September in the amount of nearly 12 million euros. In addition, during the third quarter there were some other scheduled debt repayments.

Next let's continue to slide 18 where we compare the operating cash flows in the third quarter of this year to last year's cash flows. Operating cash flows in the third quarter were nearly 48 million euros lower from last year's levels, from which lower EBITDA's effect was nearly a third. Working capital changes were affected by increase in accounts receivables as we have expanded our retail sales to new markets in Sweden, Finland, Poland, but also in Lithuania, resulting in higher accounts receivables compared to last year's levels. Coming to the CO2 impact, last year during the third quarter we received large market-to-market settlements for our CO2 positions, whereas this year our CO2 forward positions are lower, and the price of CO2 has been more stable – therefore the negative comparison compared to last year. Derivative instruments had a negative effect as our electricity, oil and gas related collaterals have increased compared to levels at the end of third quarter last year. However, interest paid during third quarter of this year was lower as last year in September we redeemed the remaining outstanding part of 2018 Eurobond in the amount of 152 million euros and this bond carried a coupon of 4.25%.

On slide 19 we have provided an overview of capital expenditure during the third quarter of this year. Capex fell by 43.9% on a yearly basis, amounting to 34 million euros. The major factors in the decreased capex are Auvere power plant related payments which were made last year, but not anymore. Investments into electricity networks were basically on the same level, whereas maintenance capex, which is mainly related to Large Scale Energy Production, decreased by half due to lower electricity production from oil shale. During the quarter we invested 3.4 million euros to renewable energy projects, up by 1.1 million euros a year ago.

Turning to slide 20 we have provided an overview of the group's liquidity position. During the third quarter Eesti Energia made scheduled loan principal payments in the amount of 21.7 million euros. The net cash flows during the quarter were negative as the cash balance of the group declined by 51.2 million euros from the second quarter to 41.9 million euros. In addition, we have access to revolving credit facilities with two regional banks in the amount of 300 million euros.

On slide 21 let's go over the group's leverage ratios and debt maturity profile. As a result of the high CO2 price and its effects on the oil shale electricity segment, Eesti Energia's net debt to EBITDA ratio has climbed back to levels we saw at the end of 2018, 3.7 times to be exact. This is above Eesti Energia's long term financial policy target of 3.5 times net debt EBITDA. The management of the company has outlined measures to get back to the financial policy metric. In August this year rating agency Standard & Poor's downgraded Eesti Energia's credit rating from BBB flat to BBB- with a stable outlook. Part of Eesti Energia's financial policy is to maintain an investment grade credit rating from international credit rating agencies.

On slide number 22, we will provide you with the updated outlook of Eesti Energia for the remaining 2019. Compared to the second quarter of this year, there are no changes in the expectations of sales revenues, while the management's expectation regarding the EBITDA and investments have changed. In the second quarter we expected the EBITDA for full 2019 to be stable and investments to grow. The latest expectation is that EBITDA and investments will both decline compared to 2018. EBITDA decrease comes from higher CO2 prices and longer unplanned maintenance period of Auvere power plant. Investments will decline mostly due to smaller Large Scale Energy Production related investments, and also some renewable energy investments have been postponed.

Finally, with slide 23 we will conclude today's presentation. In the third quarter of 2019 we saw substantially lower electricity production quantities from our oil shale based assets due to high CO2 prices and unplanned maintenance works of our Auvere power plant, which resulted in decreased electricity sales revenues and EBITDA. High CO2 prices meant that we also had to carry out restructuring activities in our Large Scale Energy Production which resulted in one-off costs. On the good side, our shale oil operations saw growth in revenues and EBITDA. As a result, our third quarter EBITDA was 42.1 million euros, a 27.9% decrease from last year's figure. 12.5 million euros of the EBITDA decline is attributable to longer than expected maintenance works of Auvere power plant and one-offs related to Large Scale Energy Production restructurings. The quarter ended with a net loss of 9.5 million euros mainly due to lower EBITDA, but also amortisation and financial costs were slightly higher compared to last year. That is all from our side regarding the third quarter results. We are now ready to take your questions.

Thank you for listening and we will introduce our annual results for 2019 at the end of February. Thank you.