

# **Eesti Energia Audited Financial Results for 2018**

**28 February 2019**

**Transcription**

Andri Avila Dear investors and partners, you are welcome to our regular conference call introducing Eesti Energia's financial results. We will be discussing the group's audited 2018 full year financials. Today's presentation can be downloaded at Eesti Energia's web site.

Eesti Energia's sales revenues increased by 16% in 2018 and reached 875 million euros. Group EBITDA increased by 7% to 283 million euros. The growth in revenues and EBITDA was driven by good performance of the electricity and oil segments. Operating cash flow amounted to 166 million euros, down by 38%, partly affected by an exceptionally strong result in 2017. The Group's capital expenditure totalled 215 million euros which is a 49% increase compared to a year ago. We will be reviewing the financials in detail in the upcoming slides.

Before we move to the financial results of the business segments, let's cover the developments at our main commodity markets. On slide 4 it can be seen that 2018 was characterised by favourable electricity prices. Electricity prices increased due to the higher price of carbon emission allowances and low Nordic hydro levels. The average price of Nord Pool Estonia equalled 47,1 euros per MWh in 2018, a 42% increase compared to 2017. The price spreads between the different countries in our region also increased. The prices are higher when we move from north to south in our region. Latvia and Lithuania produce less electricity than is required for their consumption. Price spreads were affected in 2018 by the outage of the Nordbalt cable between Sweden and Lithuania which lasted from August until October and reduced the access of lower priced Swedish electricity to the Latvian and Lithuanian market. The market is also affected by Russian electricity imports which has been favoured by the Lithuanian TSO when allocating transmission rights and which limited the access of Estonian and Finnish electricity to the southern countries. Eesti Energia's clean dark spread increased

about one third in 2018, to 12 euros per MWh. The increase in electricity price was more than enough to cover the impact of higher CO2 allowances.

Oil markets were also generally favourable in 2018, despite a drop in oil price in the fourth quarter. The average price of Brent crude oil equalled 72 dollars per barrel last year, up by 31% compared to 2017. The average price of 1% sulphur content fuel oil equalled 341 euros per tonne, 26% higher than in the previous financial year. The performance in fuel oil price was relatively weak compared to the Brent price in the first half of 2018 as export opportunities to Asia were limited. However, fuel oil price recovered in the second half of the year, as demand for fuel oil was high in Europe and also export to Asia were strong.

On slide 6 let's start the review of Eesti Energia's financial results in more detail. It can be seen that strong results of the electricity and shale oil segment translated into 16% growth in overall Group sales revenues and 7% growth in Group EBITDA. The distribution segment showed declining revenues and profits which was due to tariff cuts in the second half of 2017. It should also be noted that Eesti Energia's EBITDA in 2017 was supported by the financial close of the Jordan project as well as higher payments of liquidated damages from General Electric which were recorded in the „other“ segment.

On slides 8 and 9, let's look at the results of the electricity segment in more detail. Alongside generally growing market prices, Eesti Energia's average electricity sales price also increased in 2018. The price was affected by hedge positions which had been entered into on lower levels compared to prevailing market prices. The group's average electricity sales price equalled 47.4 euros per MWh, excluding the impact from derivatives. Derivatives deducted 0.7 EUR from the sales price so the sales price including the gain on derivatives equalled 46.7 euros per MWh. Eesti Energia's electricity generation amounted

to 9.1 TWh, down by 6% year-on-year, due to more extensive maintenance works in the power plants, seasonal closure of three older power units and higher carbon emission prices. Electricity sales volume totalled 9.2 TWh, down by 1%. Retail sales increased by 7% while wholesale declined by 18%. Retail sales were growing on the back of new markets such as Poland and also Latvia and Lithuania. All in all, revenues from the electricity segment grew by 25%. We have indicated the quantity and prices of hedge positions for 2019 and 2020 on this slide as well. For 2019, we have hedged 4.4 TWh of electricity with an average price of 44.8 euros per MWh. For 2020, the hedge position is 0.5 TWh.

Similarly to revenue growth, EBITDA from the electricity segment also grew in 2018 and reached 131 million euros. The segment's result also includes about 6 million euros from Nelja Energia, the recently acquired renewables company. Despite growing costs of CO2 emissions and higher electricity purchasing costs, electricity margins improved and this was the largest contributor to the electricity segment's EBITDA growth. Higher volumes also had a positive impact. Gain on derivatives had a negative impact on EBITDA, as did higher fixed costs. About 5 million of the growth in fixed costs is due to the acceptance of Auvere power plant. The income and costs related to Auvere are now fully part of EBITDA and are no longer capitalised. The remainder of the increase in fixed costs is due to more maintenance works and consolidating the costs of the acquired company Nelja Energia starting from November last year.

Next let's look at the results of the distribution segment, which start on slide 11. Distribution volumes grew by 3% in 2018 and reached 6.9 TWh. The growth in volume partly compensated for the decline in distribution tariffs which were implemented in the second half of 2017. There was another cut in tariffs introduced from January this year. The average distribution sales price

declined by 5% in 2018. In total, revenue from the distribution segment declined by 3% and amounted to 241 million euros. Network losses declined compared to 2017 and remained at a low level of 4.3%. The duration of unplanned interruptions grew because of storms in the second half of the year.

On slide 12 it can be seen that EBITDA of the distribution segment was also affected by the tariff cuts and declined by 7% to 100 million euros. Higher volume improved the segment's result but were not sufficient to prevent EBITDA decline. Fixed costs remained at a stable level compared to the year before, despite the maintenance works related to the storms.

On slide 14 we continue the discussion with the shale oil segment. In line with global oil prices, Eesti Energia's average shale oil sales price, excluding the impact of hedges, increased by 27% in 2018. Hedge positions mitigated the price increase to a certain extent as they had been entered into at lower levels than the realised market price. Oil production reached a record high of 411 thousand tonnes, an increase of 4% due to improved operational reliability of the oil plants. Sales volume increased by 6%. In total, the sales revenue of the shale oil segment increased by 31%, boosted by both volumes and prices. Looking at the current year and at 2020, a substantial share of shale oil sales has been hedged. The hedge position for 2019 amounts to 324 thousand tonnes at an average price of 273 euros per tonne. The hedge position for 2020 equals 172 thousand tonnes.

On slide 15 let's continue with the discussion of the profitability of the shale oil segment. The majority of the growth in shale oil EBITDA was due to higher market prices of oil. However, greater sales volume also had a positive impact. Gain on derivatives wiped away about 6 million euros of the market price movement. Another negative factor was fixed costs, particularly payroll costs. The majority of the increase in fixed costs was related to the mining unit and it was due to higher volumes of oil shale used for

oil production. It could be said that essentially these payroll costs are variable from the perspective of the oil segment, as they relate to higher production volumes, despite being shown under fixed costs in line with the Group perspective.

Finally on slide 16, let's cover the contribution of other products and services of Eesti Energia's Group. Sales of such other products and services reached 84 million euros in 2018, an increase of 21%. The growth was driven by increased sale of mining products, mainly oil shale, to third parties. Additionally, sales of pellets is now reflected in this segment which is a business that was acquired together with the rest of Nelja Energia. Sales revenues of the R&D unit also contributed to the segment's sales growth. EBITDA from other products and services totalled 9 million euros, down from 35 million euros in 2017. The decline is due to the smaller amount of liquidated damages related to Auvere power plant (now that the plant has been completed) and the comparative effect of the financial close of the Jordan project which occurred in 2017. Positive contribution came from Enefit Solutions, R&D unit, mining products and sale of gas.

Next let's look at the development of Eesti Energia's cash flow in 2018. On slide 17 there is a graph which shows the steps from EBITDA to operating cash flow. The Group's EBITDA was 283 million euros last year. Increase in working capital amounted to 43 million euros which had a negative impact on cash flow. Working capital movements include a 15 million increase in client receivables due to higher retail sales volumes and higher power price. Additionally, inventories increased by 17 million euros, out of which more than half related to oil shale inventories. Also collateral payments to clearing houses and trading counterparties related to the Group's electricity and oil hedges had a negative impact of 21 million euros and these are also included under working capital. The collaterals relate to higher hedge positions

and market movements which have resulted in higher margin payments. Moving on, the impact from CO2 related items was broadly neutral, as the cost of CO2 recorded in the income statement matched the cash outflow for purchasing the allowances. Additional cash flow adjustments relating to derivative instruments amounted to a negative of 21 million euros. Interest payments and income tax amounted to 31 million and 12 million euros in 2018, respectively. In total, the group earned 166 million euros in operating cash flow last year.

Next let's continue to slide 18 where operating cash flow in 2018 is compared to 2017. It can be seen that the group's operating cash flow declined by 38% compared to the year before. In line with the previous slide, working capital movements were more negative in 2018 compared to 2017. The factors behind the change in working capital include increase in client receivables in the retail business and oil sales; increase of inventories such as oil shale; and an increase in collateral payments provided to trading counterparties. The next component in cash flow comparison relates to Auvere liquidated damages. GE was paying down a large balance of receivables of liquidated damages related to the Auvere power plant in 2017 which affects cash flow in annual comparison. The cash flow impact from CO2 related items was relatively more positive in 2018 as we paid less cash for purchasing CO2 allowances in relation to the expense of CO2 emissions, when compared to 2017. Derivative instruments had a large positive impact on cash flow in 2017 but a negative effect in 2018 and the total difference is 50 million. Higher EBITDA had a positive impact of 19 million. In 2017, there was no income tax paid while the tax amount equalled 12 million euros in 2018. In conclusion, operating cash flow declined compared to 2017.

Moving on to slide 19, let's also look at Eesti Energia's investment cash flow last year. The group's capex reached 215 million euros in 2018, up by almost one half compared to 2017. The largest

component in the total capex included the distribution network with around 82 million euros. Maintenance investments to the rest of the business amounted to 62 million euros, up from 34 million euros in 2017. The growth came from the mining unit which purchased new mining equipment. In terms of developments, 34 million euros is made up by Auvere power plant, which was finally accepted from GE in 2018. Other notable developments include a number of smaller solar projects and the expansion of the capability to use oil shale gas as fuel in one of the power units. In addition to investments in fixed assets, the Group also completed the acquisition of 100% of the shares of Nelja Energia, the Baltic renewables company, in 2018.

On slide 20 we have provided an overview of the group's liquidity position. It can be seen that total investments including capex and the acquisition of Nelja Energia exceeded the Group's operating cash flow in 2018. However, the group's cash needs including repayment of debt were covered by a strong cash balance at the beginning of the year and by credit facilities. As at the end of 2018, Eesti Energia's cash balance amounted to 61 million euros of cash and 220 million euros of undrawn liquidity facilities were also available. In addition, the group's renewable subsidiary Enefit Green had undrawn term loans of 260 million euros available and these are targeted for refinancing the debt that came along with the acquisition of Nelja Energia. The refinancing is expected to be completed in the first quarter of 2019.

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On slide 21 let's have a look at the group's leverage ratios and repayment profile. As a result of the renewable acquisition which closed in November last year, Eesti Energia's net debt EBITDA ratio increased to 3.7 times by the end of the year. This level is lower than expected in the first half of the year when we planned the acquisition, but currently still exceeds the group's long term financial policy target of 3.5 times net debt to EBITDA. The Group has outlined measures to get back to the financial policy metric. The debt maturity profile outlined in this slide shows repayment of loans that the group had as at the end of 2018. The profile will somewhat change once the refinancing of the debt from the acquired company has been completed.

Finally on slide 22, let's discuss the outlook of Eesti Energia for the current year. It is the management's expectation that the group's sales revenues and investments are likely to grow in 2019 while EBITDA will remain stable compared to 2018. The Group's electricity sales revenue and EBITDA should be supported by relatively high electricity prices but higher cost of carbon emission allowances will have an adverse effect on the Group. Investments are forecast to grow primarily due to investments in renewable energy projects. Dividends are expected at a level of 57 million euros in 2019 on top of which there will be income tax of 14 million euros.

To conclude today's presentation, in 2018 we witnessed increasing electricity and CO2 prices. The group's sales revenues from electricity and shale oil segments performed well while the distribution segment posted declines in revenues and EBITDA due to tariff cuts. Investments grew mainly due to final payments

relating to the Auvere power plant and procurement of new machinery for the mining unit. We are now ready to take your questions.

Operator Thank you. 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.

Operator There are no questions at this time. I hand back to the presenter for closing comments.

Andri Avila Thank you for listening our presentation for 2018 results. And we will be back presenting Q1 results in couple of months. Thank you.