

Transcript of Q&A session Energa Group conference – 14.03.2019

Paweł Puchalski, Santander: Let's start with a slide, which is not here in the presentation. We lack a slide with 2019 Outlook. It seems to be more necessary here. Could I ask for the guidance among the sectors in 2019? And secondly - there is no information about the planned CAPEX of PLN 800 million in the generation. As it is quite a big amount, I would like to ask you to divide it on the separate expenditures. Because some of the investments were mentioned there, however I would like to know exactly what are you planning to finance with those PLN 800 million.

Jacek Kościelniak, CFO: Ladies and Gentlemen, please let me answer. Mr. Pawel, as I said before, as a rule we do not publish our financial forecasts. Thus it is difficult to present detailed information on the 2019 results, EBITDA, revenue. So ladies and gentlemen we do not publish them it is our code of conduct. If we publish them we are afraid of misleading the stakeholders, because we are looking optimistically into 2019. And obviously we have our forecast, we are closing it, we lack one element for the moment, and we are verifying our investment enterprises. Regarding CAPEX in Generation, maybe Mariusz would say something.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Regarding the planned CAPEX in generation, I haven't heard what the amount was....

Paweł Puchalski, Santander: I have found somewhere the amount of PLN 800 million in 2019. Please deny if ...

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: No, regarding CAPEX in the Business Line Generation, this a misunderstanding. In that case about the separate Business Line in Generation

Jacek Kościelniak, CFO: Ladies and Gentlemen, Mr. Pawel, Energa published, somewhere around December 2016, the investment strategy program, and all of the activities are within the investment program. The only matter is to place the events on the timeline. Regarding 2019 we will divide it on quarters. In the next years it is the matter of annual plans divided by exact investments, both the decarbonization and RES. All of that results from the strategy. And the strategy is a general document and I do not know where have you taken it from?

Paweł Puchalski, Santander: So what range of CAPEX in 2019 could we talk about? Totally in the Energa Group?

Jacek Kościelniak, CFO: Mr. Pawel, We are talking about the whole program, it consists of PLN 20 million, as it's written there and we have informed you. So please, as I said, we do not publish the forecasts. When we have more detailed CAPEX for the quarter or half-year, we will inform you.

Paweł Puchalski, Santander: Good, if I may check the segments. Distribution segment ... I see here strong cost pressure. Is it possible that (similar as with PGE) not all of the costs, not the whole increase of costs will be transferred, and as a consequence EBITDA 2019

will be under pressure, so it might potentially decrease in Distribution in 2019 versus 2018?

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: This is also the matter of forecasting, Mr. Pawel

Paweł Puchalski, Santander: But we're also here to discuss the current business. I am asking about... Ok, maybe somebody else has any questions.

Robert Maj, Ipopema: I would like to ask about the provision, which appeared in Q4, PLN 136 million in the Sales segment. Is there any calculation of the amount PLN 136 million which you could present us?

Jacek Kościelniak, CFO: One moment ladies and gentlemen, we will give the floor to the Mr. President Staśkiewicz. But regarding the creation of the provision, I have to say, that we conducted dynamic discussion with our auditor, we shared the opinions and discussed with the so called „technical level”, and that is why we calculated PLN 136 million, although we had serious doubts, we as Energa, we as accountants whether we should reveal such technical provision in our books at all. Yesterday we discussed it with our Supervisory Board. We have doubts to application of IAS 20, which mostly concerns subsidies, subventions government aids. Based on standards and legal regulations as well as general principles of financial reporting standards, we believe that there is no public aid and we do not expect it. We will be entitled to the compensation probably the same as to the other utilities. It will cover so-called losses. However it appeared that the team of auditors, which examined not only us. I would like to thank the auditors for the discussion and exchange of views, however the other auditors, acting in the broader area of utilities sector, somehow treated this subject too cautiously. As we said we treat the provision as a technical element, bookkeeping, reversible in the 1Q or 2Q. If Mr. Roman could complement my statement, he is more than welcome.

Roman Staśkiewicz, acting CEO of Energa Obrot: Literally in a few sentences Mr. president. We actually had stormy discussions with the auditor. I would like to emphasize that I am lawyer by education and lawyers have often problems in communication w accountants. We perceive different phenomenon differently....

Jacek Kościelniak, CFO: Excuse me, Mr. President, how should I understand you?

Roman Staśkiewicz, acting CEO of Energa Obrot: I get on well with you, Mr. President. I hope that vice-versa. But coming back to the matter, you are asking about. From our perspective referring to IFRS 37, which concerns losses on contracts, has no grounds. I don't treat temporary reduction of revenue as a loss. This mechanism, which could be compared to part of deferred payment: part of the payment for the electricity we receive now, based on the invoices we issue, and the missing part of price will be received from the compensation manager later. There is no loss. I would like to emphasize, that the so-called electricity bill says that the difference in the prices will be compensated to the utilities. It does not say there will be partial compensation of the difference in the price, which the legislator will pass, it will be as stated and we will receive the compensation. This is the first element that raised doubts in relation with the auditor. Second is the auditor's reference to IFRS 20, which concerns government subsidies and similar benefits.

We do not treat the compensation again as a subsidy. This is the equalization of the price difference, nothing more. If the compensation manager were to give us more than we deserved, then it would be possible to talk about subsidies, subvention or other similar instruments. However, in our opinion this is not the category, but accountants have their own logic ... Lawyers also. There is even such a subject of logic for lawyers as if it was a special logic. The accountants have their logic, of course our auditor too, we agreed with it and we accepted his suggestions for prudential reasons. We finally agreed with the auditor that the creation of the reserve, including it in the statement and presenting to you, will be the most transparent and possibly most accurate way of reflecting the financial situation of Energa Obrot and the whole group.

Robert Maj, Ipopema: Two more questions from my side. Ostrołęka C – could you provide some update, what is happening in terms of closing the financing. Earlier it was mentioned 28 of January, now we have half of March and how does it look like here? Second question about the unit in Grudziadz, about which it has recently appeared the information there will be a public tender. What's the budget of the unit and do you see gentlemen if the unit is profitable or not based on the today's assumptions of gas and electricity prices? Thank you.

Jacek Kościelniak, CFO: Ladies and gentlemen, regarding Ostroleka project – we proceed according the schedule, as planned. We are in constant dialogue with the general contractor, we have appropriate declarations on his part and we take an active part in the work of the steering community. Ladies and gentlemen, we need only one piece, which is calculation of compensation volumes for the closure and this is all in general. As for the implementation of biogas unit in Elblag, here the president Mariusz Gajda, but I would like to tell you, that today regarding Grudziadz we are on the very early stage, we are inviting potential contractors to a competitive dialogue. Then, as a result of the dialogue, we will create the specification and define the CAPEX of the investment, so we can say we are on the initial path. I think that Mr. Mariusz will add something more.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Thank you very much. Regarding the CCGT power plant in Grudziadz as you know there was a public tender announced leading to the choice of a general contractor. This project (regarding all of the administrative approvals, decisions) fully ready for the implementation, there is NTP, the construction has begun. This is a gas-fired 600MW unit, performing mostly as a peak block, but we consider also part-time cogeneration, to provide heat at least for Grudziadz. Regarding the terms of gas connections we are on the implementation stage. As for the contracts with Transmission System Operator (PSE) we are also on the implementation stage, so the project is ready to implement and in theory it could be built within few years. Regarding CAPEX, budget is estimated at PLN 1,8 billion and that's all information, thank you very much.

Paweł Puchalski, Santander: So maybe me again, if I may. The question about the generation. Your competitor suggests, that the coal prices will rise about 20% in 2019. Is it a good benchmark for you? This is the first question about the generation. Second without any guidance and so on. Please tell me if your generation margin (what do you expect?) rises in 2019 vs. 2018 or decreases? Margin - sales minus CO2, minus coal.

Jacek Kościelniak, CFO: Mr president Gajda will comment the statement. Thus, if you could tell us exactly whom do you mean, regarding the competition and the increase in coal prices about 20%? Ladies and gentlemen we have emphasized many times that we have good contracts for the coal supply and annually we negotiate them and we have a good cooperation with the coal sector. Coal supplies, we talk now about Ostroleka B, they are diversified and we see no serious problem here. Perhaps when somebody carelessly talks about the coal price increase, talks about the market of non-professional recipients. It's hard to comment.

Paweł Puchalski, Santander: I'm talking about your neighbour from across the Mysia street. PGE announced yesterday their projections and one of them was 20% hikes of the coal price. So this is not any secret and no marginal player. It seems that.. good PGE stated.

Jacek Kościelniak, CFO: So again Mr president Gajda will comment it, please.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Regarding the coal prices for Ostroleka B, we have contracts signed for many years with Energa Kogeneracja Elbląg, which stipulate little increases, up to 3% of the coal price, so we do not have the risk here.

Paweł Puchalski, Santander: If I may go back, if you say about the contracts stipulating 3% of coal price increase.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Up to 3%

Paweł Puchalski, Santander: So I look at the unit costs PLN/t in 2018 vs 2017 it increased about 15%.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: It looked like that, but now it is different. Now have negotiated decent prices. Regarding the margin let me say it this way. This margin will not decrease in Ostroleka B, it performs mostly in must-run production, which means that there is almost full coverage of production cost of energy, and CO2 emission.

Jacek Kościelniak, CFO: Besides, Mr Pawel, we have presented on one of the slides cases connected with limiting the number of entities in Energa Group and implementing effectiveness plans, that is why we register savings as a group and meanwhile the power plant Ostroleka B will save money and so-called non-personal fixed costs should be lower, however taking into consideration the fact of the scale, centralization of purchases and those contracts, which we have had already negotiated - we believe that generation margin will not fall, on the contrary it will be even higher and this is our management goal.

Paweł Puchalski, Santander: I understand, that you suggest that your coal price in 2019 vs 2018 will increase about few percent? This is what I assume, that's what I've heard.

Jacek Kościelniak, CFO: We assume that it won't increase more than few percent. As the president Gajda has presented here, the contracts stipulate the increase of coal prices up to 3%. I would like to say, we have good relations with the miners and we can negotiate some things with them.

Paweł Puchalski, Santander: Second questions – what dividend for 2018 will you recommend at the General Meeting

Jacek Kościelniak, CFO: Energa Group is a dividend company, we would like to pay out dividends, all depends on our investment process, which of the so-called decarbonization investments will expand. As you can see we have begun Grudziadz project in the moment, and we want to go back to the dividend pay-outs, still it is hard to tell how we are going to share the profit of 2018.

Grzegorz Witkowski, Insignis: I have a question regarding distribution segment, you are not willing to present the forecasts, however my question concerns the current reward system. Yesterday during the PGE's conference appeared the suggestion, that the model prevents from transferring all of the costs in the tariff in the current form. How could you comment it?

Jacek Kościelniak, CFO: Sure, we would like to ask for the expert's assist – gentlemen from distribution, the CFO Marek Krasicki, Mr Marek could you please? I would like to ask for the microphone too.

Marek Kasicki, CFO, Energa Operator: As a rule the cost are transferred in the justified tariff. Every year we perform everything in order to keep them within the stagnation costs, as the distribution margin would reflect the real increase of amortization equity. Obviously there are one-time events, some strategies, they can adjust. But there are elements, which neutralise possible fluctuations of for example volumes, which can be higher, sales law. And I want to mention, the revenues on the growth of distribution.

Grzegorz Witkowski, Insignis: If I understand your speech properly this is a specific situation regarding PGE, which doesn't concern you in that particular moment.

Marek Kasicki, CFO, Energa Operator: We don't know the PGE's budget situation from the backstage, every distribution system operator (even though the activity is the same) has its own nature. We have to remember, that the history matters here, shaping of the history, strategy approved by each companies in terms of network's operation, modernization costs, because they might differ in different years, they are reflected in OPEX.

Grzegorz Witkowski, Insignis: So literally speaking, you are not afraid of failure in transferring the significant part of the costs?

Marek Kasicki, CFO, Energa Operator: No, not so much.

Jacek Kościelniak, CFO: I would like to add, that we work on the optimization of our modernization processes and taking into consideration the effects of scale, we've got a special purpose vehicle. We hope that we would be able by analogy, centralize modernisation management, but we are on the beginning of the path, I forgot about one small piece like appointing one man in the group – he will manage the cost – so-called cost manager. But please ladies and gentlemen, there's certain idea to optimize the modernization and we see no problems with transferring the cost of the tariff.

Krzysztof Brymora, BDM: I have a question regarding the CAPEX I would dig into the topic, because the amount PLN 800 million, which Pawel raised, this is the amount from the financial statement page no. 35. There is PLN 800 million in the generation, this a huge amount. If you could try to divide the amount, how much is there for BAT, how much for

the new projects would be spend in 2019? This is one question. Page no. 35 in the Management Board Report, there's for sure PLN 0,8 billion.

Jacek Kościelniak, CFO: I have to admit sincerely, I don't remember exactly this figure, but I think we could comment it in writing and send by e-mail, ok?

Krystian Brymora, BDM: Ok, because actually the amount looks bigger than it should result from the strategy, which you mentioned.

Jacek Kościelniak, CFO: Ladies and gentlemen the strategy was approved by the board of the Energa Group in December 2016, we don't deny that we verify it somehow and transfer some accents of investment implementation. Ladies and Gentlemen, today we are not talking about the gas project, we are talking about the project Wisla, although we are engaged as an expert, project will be implemented by completely other entity and we are also talking about wind farms and other connected with RES, so please these are some specifications of the description included in the financial statement.

Krystian Brymora, BDM: Second question about Grudziadz. Are you going to make it possible to participate in the capacity market this year?

Jacek Kościelniak, CFO: We took the action in order to start in the general certification, which is going to take place in the Autumn this year, December I guess.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: We would like to make it till.... In order to participate in the capacity market, of course not every activity depends on us, in order not to delay.

Krystian Brymora, BDM: I understand such support for the unit stands at around PLN 80 million, right? So in the scale of the investment PLN 1,8 billion it seems to be relative small part, so there's a key question – how much time should such a unit operate annually to be simply profitable and have positive BV.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: You know... I won't tell you now how many hours a year....

Krystian Brymora, BDM: You said it would be peak operation

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Yes, indeed peak, but we consider also the possibility of cogeneration, we are still analysing those topics. It depends on the operator (PSE), agreements with PSE. Still it's difficult to say, I won't tell you right now, how many hours annually, however regarding the capacity market I don't know if you calculated properly. How much did you say? On the capacity market?

Krystian Brymora, BDM: 600 times ... 120

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Excuse me?

Krystian Brymora, BDM: PLN 120 million, right? Something around.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Something around this figure, PLN 120 million

Krystian Brymora, BDM: I calculated.

Mariusz Gajda, Vice CEO, Energa Wytwarzanie: Plus of course intervention work on...

Krystian Brymora, BDM: And the last question, short. Ostroleka C. As we see the units in Kozienice or Jaworzno, comparable units, Their construction processes lasted more than 60 months, so you will not make it till the end of 2023 when you have the obligation from the capacity market, so does your NPV calculations consist of penalties due to the failure of power supply and what is the amount?

Jacek Kościelniak, CFO: Mr Brymora, I would like to emphasize, that you ask the question with a thesis. I said few moments earlier that we are in a good dialogue with the general contractor and I would like to end on that. There is the contract, which stipulates the construction of the units within 56 months and we see no threat for the moment of prolonging the process and maybe even shorter than the contracted schedule. Thank you very much.

Krystian Brymora, BDM: Thank you

Jacek Kościelniak, CFO: Olek, do we have any question from the internet users?

Aleksander Korsak, IR director: From the internet users we have the questions regarding Ostroleka, but we have already answered them. Question to the president Dorawa – when can we expect the transfer of projects that president Koscielniak mentioned, innovative projects to the production phase. So when would we expect the real effects for the distribution?

Piotr Dorawa, CEO, Energa Operator: Project SmartGrid is scheduled to be completed by 2023. Certainly, the installation of radio-controlled disconnectors and switchgears are in motion. There is a schedule for the installation, so partial effects will be visible in the nearest future. The scheduled completion of the project's implementation is the year 2023. This is the most tangible project that will simply show a specific effect. As for the projects that were mentioned there, example UpGrid - it is a pilot project. That took place in Gdynia, on one of the estates there was a small, low-voltage network, also the SKADA system operates there at these voltage levels. The project is over, we draw conclusions. The previously mentioned SmartGrid also assumes low-voltage SKADA so we will transfer the experience from the UpGrid project to the SmartGrid project. The NEDO project, which was also mentioned. At the moment I do not remember the schedule of implementation. Our task as the operator is to connect the national system ... the national PSE power disposition with our central power dispatch. We will provide regulatory capacity for wind farms in our area. Generally, our contribution is smaller in this project. However not less important. Also this is I think the answer to the question of the Internet users.