
HRVATSKA ELEKTROPRIVREDA d.d.

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Presenter:
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OPERATOR: This is Conference #_____.

Operator: Good afternoon, and welcome to today's 2017 Financial Results Investor Call. If you wish to ask a question during today's call, you will need to press star and 1 on your keypad. I must advise you that this conference is being recorded today on Thursday, the 14th of June, 2018.

I will now hand over to Ivan to introduce your call. Please go ahead, Ivan.

Ivan Dodig:

Thank you. Ladies and gentlemen, it is a pleasure to welcome you all to HEP's 2017 audited financial results presentation. Today, our Head of Investor Relations, Ms Sučić Funko will take you through the highlights of our business and financial performance in 2017 using presentation materials. As we informed you in our Investor Call Invitation, the presentation materials are available on our corporate website under „investor relations“ section both in English and Croatian, and we hope you managed to access it. We estimate that presentation would last around 30 minutes. We will reserve some time for Q&A session at the end of the presentation, when you are welcome to ask questions you might have.

Before we start, let me draw your attention to the harbour statement on [slide 3](#) of our presentation. Now, allow me to introduce Ms Sučić Funko, Head of Investor Relations who will outline company's performance in the period ending December 31st 2017.

Ivana Sučić Funko:

Hello, everyone. Thank you for joining us today. It is a pleasure to be here with you this afternoon together with my colleagues from Finance Department to inform you about our 2017 performance.

I would like to start the presentation from **slide number 4** by mentioning key highlights of 2017. In 2017 HEP Group fulfilled its mission of safe, quality and reliable electricity supply to customers holding stable market share of 85% in Croatia and continuing further regional expansion in the neighbouring countries: in Bosnia and Herzegovina, Serbia, Kosovo, Slovenia. HEP's acquired 12,5% electricity market share in commercial sale in Slovenia.

Active and prudent liquidity management was acknowledged by Standard and Poor's rating agency which in 2017 confirmed the upgrade of HEP's stand-alone credit rating of bb as well as HEP's all-in credit rating of BB by which it has been equalled to credit rating of the Republic of Croatia. In March 2017. Moody's confirmed HEP's long-term credit rating (Ba2) as well as change the rating outlook from negative to stable.

As of April 2017, HEP continued to provide the role of the wholesale gas market supplier as a public service under regulated conditions until the appointment of the wholesale gas market supplier based on a public invitation and tender procedure that would apply for the period starting on 1st August 2018 until 31st March 2021, all according to Act on Amendments to the Gas Market Act.

During 2017, 50 ELEN public electric vehicle chargers were opened as a part of eMobility project that is being strongly supported by the Company.

Last year, pursuant to the decision adopted by the General Assembly, HEP paid into the State Budget dividend in the amount of HRK 794,3 (seven hundred ninety four point three million Kuna) for the profit earned from business operations in 2016.

In December 2017, the Collective Agreement has been signed with trade unions representatives which reflects a continuous good relationship with Company's social partners.

Moving to slide 5, you can see key facts of our financial performance in 2017. HEP Group has achieved the good result fourth year in a row with consolidated net profit of 1,3 billion Kuna (that is approximately around 180 million euros). This represents a 36% decrease of net profit compared to year before mainly due to increased costs of electricity procured (around 30%) and increased cost of energy fuel (around 23%). In 2017, the Company retained its strong liquidity with a cash position of more than 2 billion Kuna which is 33% lower than year before. Never the less, due to HRK 980 million for repayments of loans and bonds, HEP's net debt remained the same: 2.2 billion Kuna.

In 2017, the total of 2.4 billion Kuna in CAPEX were invested mostly into the reconstruction and revitalisation of existing energy facilities, construction and preparation of the construction of new energy facilities as well as into connecting customers. All investments were financed by the cash flow from operations.

At the end of 2017, the Group employed a total of some 11,9 thousand workers.

Moving to next slide 6, let me address a couple of key figures related to performance in natural figures: electricity generation in 2017 was 4% lower compared to the year before, mainly due to unfavourable hydrology and 18% lower hydro power plants generation.

Due to a relatively mild winter, heat sales were 1% lower. The sale of gas to retail customers in 2017 was 1.4 TWh which represents a 7% increase compared to 2016. Gas wholesale, which HEP operates since April 2014, was 2% lower than the year before.

Starting from slide 8, we'll discuss the 2017 financial performance in more details.

As you can see in 2017, operating income amounted to almost 15 billion Kuna, which was an increase of 4% or 569 million Kuna compared to the year before. The revenue from electricity sales increased by 662 million Kuna which is around 6%. This was a result of 3 factors. Firstly, the increase in domestic market revenue of 366 million Kuna. Secondly, foreign market revenue grew by 106 million Kuna. And finally we have had an increase in revenue from HEP's producers in the incentive system of generation from renewable energy sources by 162 million Kuna.

The revenue from thermal power sales decreased by 16 million Kuna. This represents a 2.3% decrease compared to the year before due to a 1.3% lower consumption.

The revenue from the distribution and sales of gas to retail customers decreased by 25 million Kuna (around 7.6%). This was due to a 13.5% lower average sales price. However the volume of sales has gone up by 7%.

The revenue from the sale of gas on the wholesale market has fallen by 139 million Kuna which is around 13%, when compared to 2016. We account for this by 1.7% reduction in sales volume and 9.4% reduction in sales price.

All other operating income was increased by 87 million Kuna approximately 6% compared to 2016, mainly due to circa 200 million Kuna of income from reversal of provisions for impairment of fixed assets and increased income of border capacities sale in the amount of 70 million kuna.

Let's now turn to slide 9, in the top left hand corner, you can see that in 2017 operating expenses amounting to 12.7 billion Kuna, were 9% higher compared to previous year. This was a result of: increase of electricity purchases for supply of customers in the region and the increase of electricity sales to domestic customers. As you are aware there has been a significant increase of electricity prices on the market in the reporting period. The electricity purchase price was 17.7% higher. Because of that total expenses rose by 4%.

Now turn your attention to the top right hand corner. Two figures stand out: the 355 million rise in fuel costs which is an effect of increased generation in thermal power plants. We have opted to operate gas-fired power plants more frequently instead of coal-fired power plants. This decision is a

result of higher coal prices. To get back what I was saying earlier the other figure that stands out is 638 million of electricity purchase cost which is a result of already mentioned 17.7% higher electricity procurement price.

In 2017 the structure of revenues remained relatively stable compared to the previous year, whereas in the structure of expenses electricity purchase cost in 2017 had a relatively higher share in total operation expenses when compared to 2016.

This brings us to slide 10. As we have already mentioned, the liquidity position in 2017 remained strong and stable with cash position at the year end of 2 billion Kuna. This is almost 260 million euros. Additionally we have a liquidity reserve in undrawn bank lines under short term financing sources in the total value of 1.4 billion Kuna.

Let us move on the slide 11, in the top left hand corner chart, you can see that the Company continuous to be relatively low leveraged with net debt to EBITDA ratio of 0.5 at the end of period.

Although debt currency structure presents 100% of debt exposed to EUR, by Croatian National Bank providing foreign exchange policy where HRK is strongly related to EUR, the actual risk is relatively limited.

In 2017, 980 million Kuna was used for repayments of the loans, remaining amortising domestic bond and full repayment of the 2012 Eurobonds.

Moving to slide 12, as it is known, HEP has been the first company in Croatia that requested credit rating from Standard & Poor's and Moody's, way back in 1997. Since then, Standard & Poor's has revised HEP's credit rating every year while the relationship with Moody's was resumed in 2011.

In 2017, Standard & Poor's confirmed the upgrade of HEP's stand- alone credit rating of bb as well as HEP's all-in credit rating of BB. This means that our credit rating is the same as credit rating of the Republic of Croatia.

In March 2017 Moody's confirmed HEP's long-term credit rating (Ba2) and changed the rating outlook from negative to stable.

This bring us to Operations results section.

On the slide 14, in the top right hand corner chart you can see the geographical position of power plants HEP operates across the Republic of Croatia. The upper left hand side chart shows generation performance of power plants with a higher generation of thermal and hydro power plants as well as nuclear power plant Krško (which is co-owned with Slovenian GenE). Due to a relatively mild winter, generation of heat energy was at the same level as the year before.

As you can see from the chart in the bottom left hand side, HEP in 2017 operated a large and diversified generation mix with 3.353 MWe of installed capacities. Generation is largely based on hydro and nuclear power with limited CO₂ footprint and a reduced exposure to commodity prices. Even though subject to weather conditions, the production of electricity from hydro power plants represents a cost efficient and renewable source of energy.

Moving to slide 15, you can see that hydrology in 2017 was 18% lower than the year before, and 9% below average hydrology.

Since hydro power plants account for 50% of installed capacity, there is a certain hydrological dependence which Company takes effort to mitigate by prudent energy balancing and system optimizing. As it is seen from the bottom left hand side chart, certain improvements have been made. Comparing 2011 and 2012- extremely low hydrology was reflected in lowered EBITDA whereas in 2017, for similar hydrology as in 2012, achieved EBITDA was almost doubled.

80% of total hydro installed capacities derive from the accumulation HPPs which gives certain possibilities of using the water energy balance during whole year compared to the run-of river hydro power plants where there is no possibilities of storing water in accumulation.

On the next slide 16, you can see that thermal power plants generation in 2017 was 11% higher compared to year before. Although, as you can see from the upper right hand side chart, 5% of thermal installed capacities in 2017 are those that run on crude oil, when optimising generation portfolio balance, thermal power plants generating electricity, were those that run on gas and hard coal. Crude oil-fired capacities serve only as reserve capacities due to uncompetitive prices. Thermal power plants fired by hard coal provide a stable base load source of electricity, while gas-fired power plants are all CCGT capacities producing heat as well and used for thermal and heat supply, which is seen from the bottom left hand side chart.

Moving to slide 17, the upper right hand side chart shows the Croatian transmission system which is one of the 5 best connected transmission system operators in Europe. Through continuous long-term investments into the transmission network, i.e. cross-border transmission lines, TSO (HOPS) accomplished great and almost infinite capacities (from the perspective of needs and use of the same capacities/power) towards the interface with the CEE region (Hungary and Slovenia) that represents the major part of total cross-border transmission capacities at the Croatian borders (66.61%).

Furthermore, when we talk about transmission network losses, they are below very competitive 2%. They do vary during the season due to a series of factors, such as: system load, temperature, hydrology, topology of the network itself etc., but overall they are at competitive levels compared to surrounding transmission systems.

Also, HEP TSO is 50% owner of the Croatian Power Exchange- CROPEX, together with HROTE. Croatian Power Exchange acts as Central Counter Party between sellers and buyers of electricity and takes the risks of buying and selling electricity for all day-ahead and intraday trades concluded on the trading platform.

Moving to slide 18. HEP DSO is a sole distributor of electricity in Croatia- regulated monopoly activity, performing after November 2016 role of distribution system operator.

Distribution network losses are decreasing over time due to investments into modernisation and reconstruction of distribution network. A couple of years ago, distribution network losses were higher than 10% and as you can see from the upper left hand side chart, total network losses were around

8%, similar to year before. Total network losses comprise technical and commercial losses where technical losses are related to network performance and commercial losses derive from unauthorised usage and inefficiency of network management.

HEP DSO with 7.5 thousands employees is the largest subsidiary of HEP, in 2017 continued its process of restructuring, expecting significant savings in operational expenses and improvements through more efficient organisation.

On the slide 19, in the top left hand corner chart, you can see that HEP's electricity market share is 85% in 2017. The customer outflow that HEP was facing during 2014 was stabilised and has remained at these levels since 2015. HEP Elektra supplies customers under public service obligation (universal service and guaranteed supply) while HEP Supply supplies all other customers opting for a market supplier.

When talking about market suppliers, HEP Supply is the largest market supplier in Croatia among 16 others, having supplied 74% of commercial customers in Croatian market.

In 2017, HEP continued its regional presence, especially in Slovenia where HEP holds 12.5% market share in commercial sale, by this compensating loss of market share in Croatia.

Coming to slide 20, you can see that in the electricity market in Croatia, electricity demand in 2017 was by 4% higher compared to the year before. Furthermore, in 2017, HEP's electricity needs were 12% higher due to 3.5% higher electricity sale, compared to 2016.

Moving to slide 21, let us say a few words on gas business. HEP Group provides activities of gas distribution and gas supply on retail market through its subsidiary HEP Gas and until 1st of August it acts as a sole wholesale gas supplier under regulated terms to public service suppliers for household customers providing reliable and safe gas supply in Croatia. At this moment Croatian regulatory energy agency conducts public tender for new wholesale gas supplier. Besides the 60% of Standard bundled units of the Underground Gas Storage allocated to HEP Group until April 1, 2022 it is worth mentioning that around 50% of total gas delivered in Croatia is from HEP Group.

On the other hand, HEP Gas is the second largest gas supplier out of 54 gas suppliers in Croatia by volume sold to end-customers and in the same time the second largest gas distributor out of 35 gas distributors in Croatia.

On the slide 22, in the lower right hand corner chart you can see the geographical footprint of district heating systems across Croatia where red dots represent HEP's district heating systems being the largest distributor of heat covering approximately 81% of the total market by the number of customers in Croatia. Looking at the chart at the bottom left hand side chart, you can see that in 2017, HEP's sale of heat energy was accounting for 5% of revenue share of the overall Group's revenue.

Before moving to Capital Expenditures, on **the slide 24**, let us say few words on other HEP's operations. In 2003, HEP established subsidiary HEP ESCO as implementing company for energy efficiency

programs providing activities of development, implementation and financing of ESCO (energy service company) projects that are repaid from savings, where customers find additional value added. Providing this additional service to the customers, HEP ESCO represents a cross-selling channel for improving customer relations and developing the benefit program with electricity, gas and heat supply.

An important role of optimisation of power plants operations is carried out by HEP Trade, subsidiary performing trading activities on markets in the region as well as via bilateral trading in countries across the region. Except from electricity trading (including reservation of cross border transmission capacities), HEP Trade is trading emission units, green certificates, gas sale and reservation of the transport system capacity. Spot and futures trading is performed on European energy Exchanges (BSP Southpool, HUPX, EPEX, EEX, CROPEX, SEEPEX, CEGH) and broker platforms (TFS, Spectron).

HEP Group is present on wholesale electricity markets from Germany to Kosovo, directly in EU members' states or through HEP-Trade's daughter companies in Bosnia and Herzegovina, Serbia, and Kosovo. HEP Group is also active on the retail markets of Slovenia, Serbia and Bosnia and Herzegovina (electricity supply).

In 2017 HEP Trade traded 9.3 TWh of electricity in Croatia whereas in Bosnia and Herzegovina volume traded was 0.2 TWh. Also, in 2017, volume traded with Slovenia was 1.2 TWh and with Serbia 0.1 TWh.

Moving to slide 25, brings us to capital expenditures. In the last few years Company provided on average 2 – 2.5 billion Kuna in CAPEX per year. In 2017, total investments amounted to 2.4 billion Kuna which is a 6% decrease compared to 2016, including 1.5 billion Kuna for transmission and distribution network renovation, as well as 600 million Kuna into power plants facilities.

As to future investments, the revitalisation plan for hydro power plants is ongoing expecting 140 MW of additional capacities. As for the thermal power plants, plans are aimed in line with low CO₂ emissions where a two phase tender for the EPC Contract for the reconstruction of EL-TO Zagreb CCPP is undergoing.

With this I would like to thank you very much for your time and attention and would move to Q&A session of this conference call.

Ivan Dodig: Ms Sučić Funko, thank you very much. May I please kindly ask the operator to open call for questions?

Q&A's session:

Operator: Thank you. And as a reminder, if you do wish to ask a question, you can press star and 1 on your keypad and wait for your name to be announced. Star and 1 on your keypad for any question.

We've got no questions on the phone lines. Please continue.

Ivan Dodig:

If there are no further questions, I would like to once again, thank all participants for your attention and wish everybody a nice day.

We will now end this conference call, and would like to instruct you to refer to our web site where you'll find contact details for any further inquiries.

On behalf of HEP Team, best regards from Zagreb!