Renewable Energy and Energy Efficiency Finance Forum

27 September 2004, SAS Radisson Hotel, Budapest

Risk Management in Practice – The Case Study of Pannongreen Project

Eva Revesz
Agenda

I. OTP Bank
II. The Pannongreen Project

The Case Study of Pannongreen Project
I. OTP Bank

I.1 Market Share
I.2 Balance Sheet
I.3 Profit and Loss Account
I.4 Subsidiaries
I.5 Project Finance

The Case Study of Pannongreen Project
## I.1 Market Share

<table>
<thead>
<tr>
<th>Segment</th>
<th>Market share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retail deposits</td>
<td>36%</td>
</tr>
<tr>
<td>Retail loans</td>
<td>14%</td>
</tr>
<tr>
<td>Corporate deposits</td>
<td>14%</td>
</tr>
<tr>
<td>Corporate loans</td>
<td>12%</td>
</tr>
<tr>
<td>Municipal deposits</td>
<td>75%</td>
</tr>
<tr>
<td>Municipal loans</td>
<td>54%</td>
</tr>
</tbody>
</table>

Source: Annual Report 2003
## I.2 Balance Sheet

Balance Sheet as of 31 December 2003

<table>
<thead>
<tr>
<th></th>
<th>Million HUF</th>
<th>Million EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Assets</strong></td>
<td>2,758,606</td>
<td>10,874</td>
</tr>
<tr>
<td><strong>Current Assets</strong></td>
<td>1,128,176</td>
<td>4,513</td>
</tr>
<tr>
<td><strong>Fixed Assets</strong></td>
<td>1,590,374</td>
<td>6,361</td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
<td>2,758,606</td>
<td>10,874</td>
</tr>
<tr>
<td><strong>Short-term Liabilities</strong></td>
<td>2,326,249</td>
<td>9,305</td>
</tr>
<tr>
<td><strong>Long-term Liabilities</strong></td>
<td>116,540</td>
<td>466</td>
</tr>
<tr>
<td><strong>Subscribed Share Capital</strong></td>
<td>28,000</td>
<td>112</td>
</tr>
<tr>
<td><strong>Reserves</strong></td>
<td>233,776</td>
<td>935</td>
</tr>
</tbody>
</table>

Source: Annual Report 2003

The Case Study of Pannongreen Project
## I.3 Profit and Loss Account

<table>
<thead>
<tr>
<th>Profit and Loss Account as of 31 December 2003</th>
<th>Million HUF</th>
<th>Million EUR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Result of Ordinary Business Activity</td>
<td>86,732</td>
<td>348</td>
</tr>
<tr>
<td>Profit/Loss before Tax</td>
<td>86,701</td>
<td>347</td>
</tr>
<tr>
<td>Profit/Loss after Tax</td>
<td>71,562</td>
<td>286</td>
</tr>
<tr>
<td>General Reserves</td>
<td>-7,156</td>
<td>29</td>
</tr>
<tr>
<td>Dividends</td>
<td>16,800</td>
<td>67</td>
</tr>
<tr>
<td>Balance Sheet Profit/Loss</td>
<td>47,606</td>
<td>190</td>
</tr>
</tbody>
</table>

Source: Annual Report 2003

The Case Study of Pannongreen Project
1.4 Main Subsidiaries

<table>
<thead>
<tr>
<th>Main Subsidiaries</th>
<th>Activity</th>
</tr>
</thead>
<tbody>
<tr>
<td>as of 30 June 2004</td>
<td></td>
</tr>
<tr>
<td>OTP-Garancia Insurance Ltd.</td>
<td>Insurance</td>
</tr>
<tr>
<td>OTP Real Estate Ltd.</td>
<td>Real estate management and development</td>
</tr>
<tr>
<td>HIF Ltd. (UK)</td>
<td>Forfeiting</td>
</tr>
<tr>
<td>Markantil Bank Ltd.</td>
<td>Car purchase financing</td>
</tr>
<tr>
<td>OTP Fund Management Ltd.</td>
<td>Fund management</td>
</tr>
<tr>
<td>OTP Mortgage Bank Company Ltd.</td>
<td>Mortgage financing</td>
</tr>
<tr>
<td>OTP Banka Slovensko (Slovakia)</td>
<td>Commercial banking</td>
</tr>
<tr>
<td>DSK Bank (Bulgaria)</td>
<td>Commercial banking</td>
</tr>
<tr>
<td>Banca Comerciala RoBank (Romania)</td>
<td>Commercial banking</td>
</tr>
</tbody>
</table>
I.5 Project Finance

Projects covered:
- Energy-, energy-related
- Infrastructure
- Telecom
- Real estate
- Acquisitions
- Special projects

Portfolio as of 31 December 2003:
- Total commitment: HUF 210,000 million (= EUR 840 million)
- Outstanding: HUF 160,500 million (= EUR 642 million)
II. The Pannongreen Project

II.1 The Project
II.2 The Borrower
II.3 Regulatory Framework
II.4 Main Contracts
II.5 Risk Assessment
II.6 Financing
II.1 The Project

The Project:
- Refurbishment and transformation of a former coal-dust fired unit of Pannonpower to biomass fuelled (wood, wood-chips)
- Development and construction of wood processing and depo facilities
- Operation of the Project

- New biomass unit: 49.9 MWe and 65.0 MWth
- Largest biomass project in CEE
- Total Project Cost: HUF 6,665 million (= EUR 27 million)
- Financing: 25% equity and 75% bank loan
- Construction period: 1 year; commercial operation since August 2004
- Turn-key construction contract
- Revenues and costs are based on either long term contracts or regulatory off-take obligation
II.2 The Borrower

- Pannonpower Inc.: successor of former „Pecs Power Plant” comprising different power generation units
- Corporate restructuring: a holding company was established
- Owner and Sponsor: Pannonpower Holding Inc.
- SPV / project company founded solely for the Project: Pannongreen
II.3 Regulatory Framework

Act No. CX 2001 regulating generation, transmission, distribution, trading, and consumption of electric energy
- In full force and effect since 1 January 2003
- Deals more profoundly with energy generation based on renewable sources and offers special conditions

Decree of Ministry of Economy and Transport No. 56/2002 (XII.29.)
- In full force and effect from 1 January 2003 to 31 December 2010
- Regulates the mandatory off-take obligation in respect of – inter alia – renewable energy
- Provides regulatory and subsidized off-take prices
II.4 Main Contracts

- Turn-key construction contract with performance- and warranty bonds
- Long-term Wood Supply Agreement with Pannontrading Ltd.
  - Basis: long-term wood supply agreements between Pannontrading Ltd. and two major Hungarian sylvicultural companies
- Annual Power Purchase Agreement with the energy off-taker DEDASZ, a Hungarian energy distribution company
  - Basis: long-term heat supply agreement between Pannonpower Ltd. and district heating supplier Petav
- Long-term Operation and Maintenance Agreement with Pannonenergia Service Ltd.
- Emission Reduction Purchase Agreement with the Prototype Carbon Fund of IMF

The Case Study of Pannongreen Project
II.5 Risk Assessment

Construction risk: LOW
- EPC contractor: reputable Hungarian company with proven experience and track-record
- Fixed-price turn-key contract
- Performance bond, warranty bond
- Refurbishment and transformation as opposed to new installation

Operational risk: LOW
- Experienced personnel
- Manuals, trainings
- New technology
Market risk: MEDIUM

Fuel
- ☺ Long-term Wood Supply Agreement
- ☺ Potential other sources: other sylvicultural companies
- ☺ Alternative fuel sources: sunflower, rape, straw, corncob, agricultural and wood-like by-products
- ☹ Limited availability
- ☹ New sources are still research and development
- ☹ Increasing competition through new biomass installations

Heat
- ☺ Long-term Heat Supply Agreement
- ☺ Potential industrial off-takers
- ☹ Potential change in the district heating market – switch from district heating to gas
- ☹ Unknown industrial demand in the region
Regulational risk: MEDIUM

- EU accession in May 2004
- Supporting EU directives
- Increasing importance attached to „green” projects and renewable energy
- Hungarian legislation is likely to follow EU principles
- Recent changes in the Energy Act
- Decree ceases to be in force and effect after 31 December 2010
- Uncertain energy off-take after 2010

Legal risk: LOW

- Experienced international legal advisors on both sides
- Complicated contractual arrangements
CO2 risk: MEDIUM

😊 „Extra” revenue for the Project
😊 Prestigious deal being the largest CO2 deal so far in Hungary
😊 Good experience for the parties
😊 Unavailable limits and numbers
😊 Additional risk due to bank guarantee issuance
😊 Pay-back obligation
😊 No track-record

The Case Study of Pannongreen Project
II.6 Financing

- 25% equity, 75% long-term debt financing
- Facilities:
  - Long-term project loan
  - VAT facility
  - Working capital facility
  - Bank guarantees
- Tenor: 10 years maturing in 2013
Q & A
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