

With successful business, rescheduling of the loans, rationalization of the costs and record production, the costs are reduced for almost 21 billion RSD- The objective is that EPS become more organized and efficient company- Consumed electricity must be paid Measures taken during the autumn of last year and this year have resulted in the improvement of the operations of “Electric Power Industry of Serbia”. Form the company, which in February this year was faced with the very difficult finance situation, more precisely very dramatic, half-year results show signs of improvement and the effects of implemented measures.

Alexandar Obradović, Acting General Director of EPS, says that the situation he found on September 6<sup>th</sup> 2013, when he was appointed by the Government of Serbia as Acting General Director, was a disaster. Back then EPS had 10 billion RSD of outstanding liabilities - debts and obligations for current repairs, investments and expropriations, and the expected loss at the end of 2012 was 33 billion RSD. It lacked 40 billion RSD in cash flow.

The initial Annual business plan of EPS, which was adopted in February by Government of Serbia, anticipated the shortage of funds of almost 50 billion RSD. For the first time in the history, EPS was faced with the possible bankruptcy. Why was it so and what has changed in the meantime?

The financial situation was alarming and deeply disturbing, and then it was, that for the first time in the history of EPS, that someone came out and said: “This is the real situation - the emperor is naked!” Apart from catastrophic financial indicators, EPS failed to meet its legal obligations last year. According to the Energy Law, we are obliged to, from the 1<sup>st</sup> October last year, have the separate operator of the distribution system and firm which will deal with the public supply. Why is that important? According to our Energy Law, and in accordance with the European Union Directives and signed Energy Community Treaty for South-East Europe, we are obliged to open the electricity market for competition and to establish market approach. As the monopolies in other sectors were breaking, power sector is also an area where the monopoly has to be broken. EPS did not meet the basic legal provisions to separate the infrastructure - part of the distribution network, which will deal only with the distribution of electricity from the part that deals with supply.

Why was it important to separate the business?

That is the point of liberalization and breaking the monopoly. The aim is non-interference of everything, but one company to be engaged in distribution. And that company will have to have the same attitude and treatment for EPS and other participants in the market. Other competitors will be eligible to use the distribution network and to offer their supply services to the end costumers. EPS did not do that, and therefore the liberalization of the market was threatened because there were no preconditions to start with the opening of the market. However, with the appointment of the new team, new management and with a superhuman effort of the colleagues in EPS and in subsidiary companies, we have succeeded to reverse

the situation totally in less than a year.

What has been done?

We managed to solve the financial problem. EPS is now liquid and meets all obligations on time. I would like to thank all the employees, colleagues in EPS for commitment and hard work to achieve the better results. It was planned that the loss in 2013 to be approximately 22 billion RSD, but we expected it to be 800 million RSD. That means that, with successful business, rescheduling of the loan, rationalization of the costs and record production, we have reduce the loss for almost 21 billion RSD. The obligation under the loan of 21 billion RSD was rescheduled, out of which about 15 billion should reach in 2013, which would adversely affect the liquidity. We have improved our cash flow - from the insolvency and minuses of almost 49.2 billion RSD, the results were improved for 42.8 billion RSD. The cash flow is the lifeblood of the company. If there are the liabilities and incomes that cannot meet their needs, than you cannot pay the salaries, pay the suppliers, taxes and other expenses.

When will EPS finally operate with the avail?

Serbia and EPS strive for an open, liberalized market and that market only knows the market price. There are supply and demand, and successful companies will make a profit because they will be able to meet the market at the certain price. The companies that are unsuccessful, inefficient will withdraw from the market, lose the consumers and, at some point, will go bankrupt. However, on the other hand, EPS, that is our new daughter company "EPS Supply", apart from the consumers supply at the open market, it has received the license for public supply. "EPS Supply" supplies all the tariff customers at the price we call "reasonable price". This is the price that will enable us to maintain this system and stable electricity supply for the citizens and economy, which will, however, take into account the general economic situation. Since the market at high voltage was opened from 1<sup>st</sup> January 2013, it is now easy to see what the market price is. If we would apply the market price on public supply, that is if the current supply market price would be factored into the Energy Agency for pricing the electricity price, the price would have to be raised for 38 percent, instead for 10.9 percent, as it was increased from 1<sup>st</sup> August. However, EPS is aware of its social function and the burden of the market price cannot be, in this economic situation, switched on tariff customers. Therefore, we have reduced the resources for investment, maintenance and overhauling, in order to obtain the current price.

But the recent increase of price did not cover the cost of inflation. What to do?

It is true that the electricity price has not been changed for two years and four months, and the inflation in this period was 14.1 percent. We did not even cover the inflation, and if take into account the market price in the past eight years, we would get the information that EPS has given six billion euros to the economy and citizens. Those six billion euros was not included in investments, in new production capacities, and the current capacities with its

lifespan, are no longer reliable as when they were new. The question is how to reconcile the social aspect and coping with the real situation, because what if there is unfavorable climate situation and some thermo block “drops”? this indicates that social politics, which should exit, but in short term, when lasts for too long, eats the core of the company. It is true that the price is not the only, but it is the key factor. Because, when you are forced to sell far below the market price, it is not good from the start.

What are the other factors?

The goal is that EPS becomes the more organized and efficient company. In November last year, the Serbian Government adopted the Starting points for reorganization of EPS through which the company should become profitable and successful. One of the first tasks is opening and participation in the open market, because, since 1<sup>st</sup> January this year, EPS is no longer equal to the entire electric power system of Serbia. Now, we are just one of the participants in the market and we have to behave market. As the market opens, no one can guarantee us that we will keep the consumers.

And how much have we moved forward in the application of the Starting Points for reorganization?

The Ministry of Energy has agreed and Serbian Government, in November 2012, has adopted the direction in which EPS has to go to become more efficient and profitable. The key for improvement the parameters of the EPS business is reorganization through corporatization. Today, EPS is the parent company with 13 affiliated companies which operate quite independently. The idea is to make some savings precisely in corporatization and centralization of various functions - legal, finance, IT, human resources. Because we do not need to do some things 13 times in all companies, but let's do that central. The Starting Points states clearly that one supplier and operator of distribution system should be established, and not to have 5, 10 or 20 of them and still to create new companies with new directors. But, out of these Starting Points we have fulfilled the part related to the establishment of “EPS Supply”. There have been a lot of obstructions within the system and on the side, because a lot of interests were threaten, ranging from local politics. There even were the obstructions from the previous Board of Directors, who persistently refused to allow the establishment of “EPS Supply”, and thus worked against the interests of EPS. If we had not set up the “EPS Supply”, we could not have asked for the price increase. Creating an ambient for the fulfillment of the Starting Points is not in power of management because the corporative management requires a change in a statute and change in the incorporation charter documents, even a change of legal form of EPS. And these changes are the responsibility of the founders, that is Government. This management is trying to look at EPS as a company which has to make a profit for its owner which is the state. Each year, the market is more open, in 2013 the high voltage is liberalized, and from 1<sup>st</sup> January 2014 the medium voltage is going to be opened, and this means that over 4,000 new firms will

enter the market. Every year, according to the Law on Energy, practically every customer will have a right to choose their supplier from 2015.

The market for customers on high voltage is open. Are you satisfied with the results?

One of the main successes, for which I am particular proud of the new management, colleagues in EPS, is that we were able to keep 97 percent of market at the high voltage. And with the improved market price we have achieved the revenues of 2.3 billion RSD. On the one hand, we were able to increase the revenue and to keep 97 percent of the market. We only lost one customer, German company "Messer", which has opted for a new supplier. That one customer has repeated that he was not satisfied with the price of EPS. How is it possible that Slovenian company offers the more favorable price than EPS?

Customer does not see the manufacturer, but only the supplier, because, according to market rules, the function of electricity production and supply two different things.

Electricity can be bought on open market and re-sold or to be self-produced, but that the customer did not see nor know about it. All the manufacturing facilities in EPS will sell the electricity or "EPS Supply" or "Electrical network of Serbia. But it should be clear that no one will be able to buy the electricity directly from TPPNT or "Kostolac". This is how all the companies function - RWE, CEZ, they have their companies for supply. And everything is allowed on the market. It could be worked out with smaller margin or even a loss, but in order to take a part of the market. I still believe that we will try to win the "Messer" back, which we have lost, because EPS is strong and stable partner. Together, our production, distribution and supply capacities can offer the most to our customers.

At the market opening there were complaints that EPS went too far with increasing the prices. Is that true?

That is not true, if we have in mind that almost for a decade all of today's buyers on high voltage benefited from the social cost of electricity and none of them complained about purchasing electricity at much lower-than-regular prices. They saved hundreds of millions of euros that way. In the last eight years, they've had option to buy the power on the open market, but they rather opted for EPS as the most favorable. And, if you have on the one side the tariff price for which you are eligible and on the other side market price that is much higher, of course no one will go where it is more expensive, but will choose the tariff price. Now, if a vendor offers cheaper electricity, it does not mean that EPS should be criticized for its sticking to higher rate in spite of being the producing company. The question is when the vendor arranged that purchase - its purchase price may be lower than our production price. The fact that we are a producer does not mean that we have the cheapest electricity in every moment, and insurance is always expensive. To be secured for the following winter, EPS needs to buy the power in advance and at a fixed price in order to enter the winter season without problems. But how do you know what the price will be?

What happens if you now purchase something at much higher price than it will be later, and

then in February one says “Why did you buy at the price of 55 instead of the current 45?” Or it could be vice versa, so we make a great profit. That’s why I do not understand when someone asks “Why did you buy electricity a year in advance instead of waiting for a lower price?” Price is a dynamic category that depends on many factors, and no one can predict it. How has the decision, that the state institutions and firms must pay their debts within 45 business days and business people within 60 days, affected liquidity of EPS?

That decision has harmed us by adding more pressure on our obligations to pay on time. However, on 31<sup>st</sup> December 2012 payables amounted to RSD 24.6 billion, while on 30<sup>th</sup> June 2013 they were RSD 16 billion, which means that the amount of RSD 8.5 billion was paid in six months and it entered the economy. We have, however, a big problem because many consumers owe us money that they do not pay.

How to solve it?

We have initiated several activities related to the rescheduling of debts, because we wanted to do a favor to both businesses and citizens. In agreement with the relevant ministry, currently we have the final agreement on debts rescheduling.

Regular payers are not very happy because of that!?

Electricity consumption has to be paid. The fact that the previous governments and the managements of EPS tolerated waste of state assets through non-payment of electricity is not an excuse to continue with that practice in the future. Actually, the purpose of this rescheduling is to settle outstanding liabilities. On the other hand, the court proceedings are expensive and we are trying to save money both for EPS and the state by avoiding those proceedings. All those who fail to pay for the electricity are going to be cut from the power network. In the future, we will be more dedicated to regular payers and will be more investing in relationships with them.

We have been waiting for the construction of a new capacity for more than two decades. Is there a step forward?

The projects that the EPS began in 2013 include inter alia the purchase of mining equipment for MB “Kolubara”, worth 181 million euros, and the revitalization of HPP “Zvornik”, worth 70 million euros. It is very important that the strategic directions of EPS and project management that is in accordance with the best practices of reputable electric companies, were created for the period until 2025/2030. It was also defined the basis for the selection of investment projects in a way that ensures profitability of the company. EPS will meet the obligations under the previously signed memorandums and protocols. Whatever projects are selected, the main criterion and our strategic goal will be profitability. The preparation of a feasibility study for the project of reversible HPP “Bistrica” is under way, and current projects include TENT B3, “Kolubara B”, “Kostolac B3” and combined gas-steam power plant “Novi Sad”. The activities in progress also include preparation of feasibility studies for all the projects, which is expected to be completed by the end of the



year.

Market response

Incentive tariffs for renewable energy sources attract investors. When are we going to attract investors for building the thermal or gas power plant?

Electricity production is a market activity, and everyone has the right to build a production capacity. The good question is why this does not happen. The answer lies in the fact that the market conditions have to be created in order for anyone to wish to invest. The opening of the market should be a move forward also in this field.

We must reduce the costs

Do the employees have a reason for fear, because we hear from year to year that there is a labor surplus in EPS, and especially in the administration?

We must reduce the costs in order to be more efficient. Currently we work on the comprehensive systematization analysis of the employees work position, because we do not see EPS or each PLC as a separated company, we treat EPS now as a whole instead.

In some fields, we have a lack of labor, especially in the difficult occupations, i.e. assembler, miner, plant engineer, but on the other side, we have surplus in unproductive administration. When we have many unproductive people in the system, we have to hire other firms for these productive units, what means double costs, and workers who are not enough familiar with the operation process; the result is, we must buy all we need at the market. However, we cannot relocate people just like that; the preconditions must be created first. The goals for the reorganization of EPS have to be fulfilled, and the corporatization established. The age structure is also the problem because the average is 45 years. We do not have generation that could take over all these operating units, but the first thing to do is to train the young people by working together with the old ones. Therefore, we cannot afford waiting for somebody to be retired to hire the new one. Who is going to train them?

Peak production, good sale

What are the six-month production results?

The „Electric Power Industry” produced about 19 billion kWh in the first six months this year, which is the peak production for this period. It is expected that the production will be even 37 milliard kWh by the end of the year. Comparing to the Electricity production plan, the production is higher by 0,8 percent, and comparing it with the same period last year by 6,4 percent. Not for a moment, there was a problem during the operation of PE EPS Power Plants. Comparing to the plan, the total production is higher by 154 million kWh, and in the first half of the year 2013, the production was higher by 1,137 billion kWh than the last year. In the six month period EPS sold 1,66 billion kWh, worth € 67,35 million, i.e. 33,4 percent more than planned. The sold electricity value will exceed 100 million euros by the end of the year.

Procurement according law

The Public Procurements were often referred to as one of the key problems in the system. What has been done in this field?"

For the first time the consolidation of the Procurement Plans in EPS and its PLCs was done. The plan value of these PLCs is about 250 billion dinars. By the Public Procurement centralization we achieved, the economic expenses, more efficient usage of means, more enabled bidders and favorable offers and unified technical specifications. The conditions and requirements in tenders are defined which provides quality, competition and more favorable terms to the company, secured integrity of the process by the implementing of the Procurement control and transparency of Procurement process according to the Public Procurement Law. One of the examples of the saving is pooled Procurement of licenses and maintenance services of "Microsoft" software products, because we have the best financial conditions and discount of 33 percent. That is saving of 1,7 million dollars.

Source; EPS Kwh