



SESSA conference "Perspectives and Challenges
of EU Electricity-Enlargement"

**Topic: Activities of Investors in and of Accession
Countries**

Berlin, 8. - 10. December, 2004

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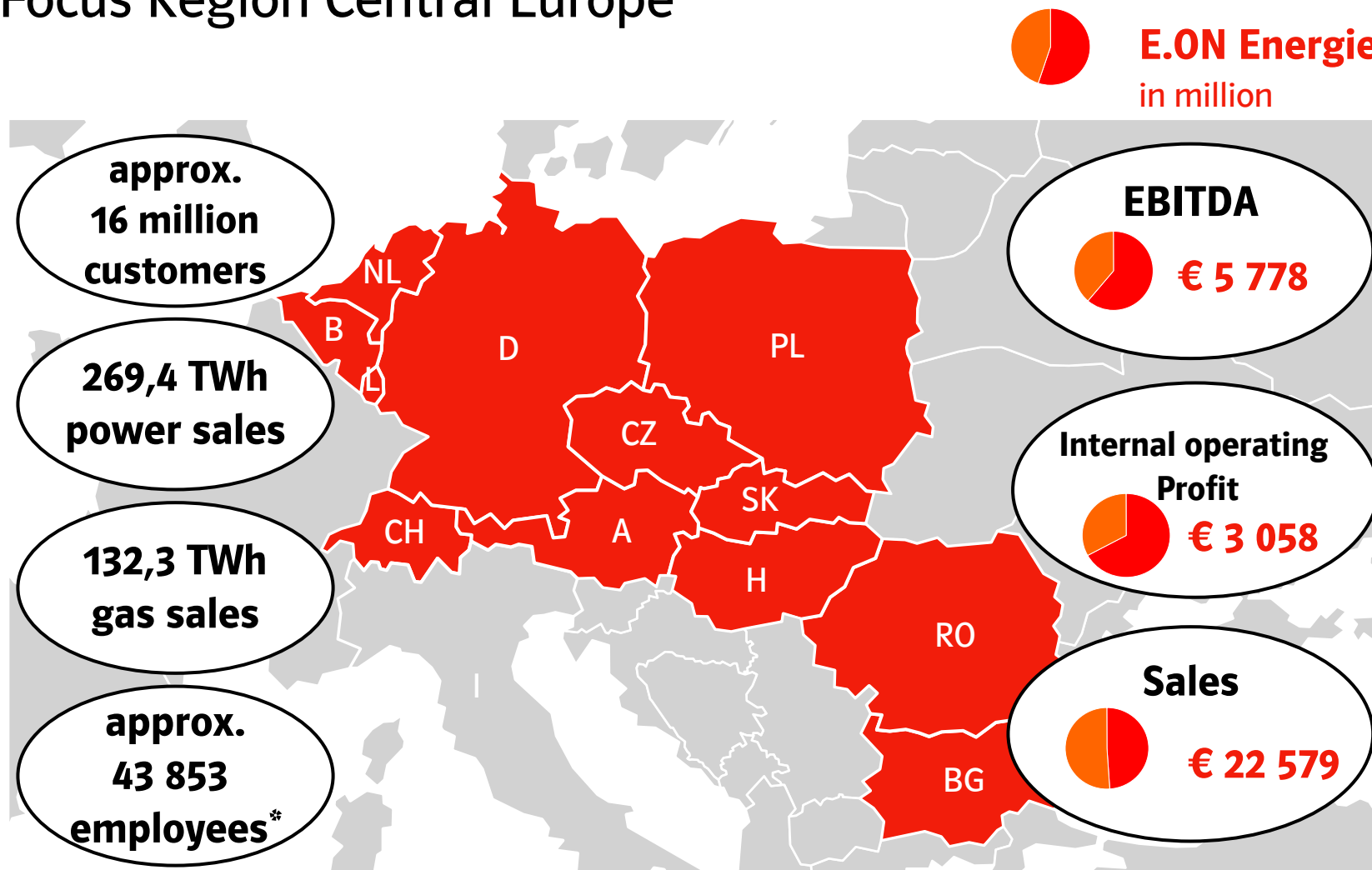
Agenda

- **E.ON Energie – Central Europe**
- **Growth potential in SEE**
- **Envisaged future development**
- **Strategy and success factors of E.ON Energie**
- **Electricity market development in EU**
- **Financial investors**
- **Summary and conclusion**

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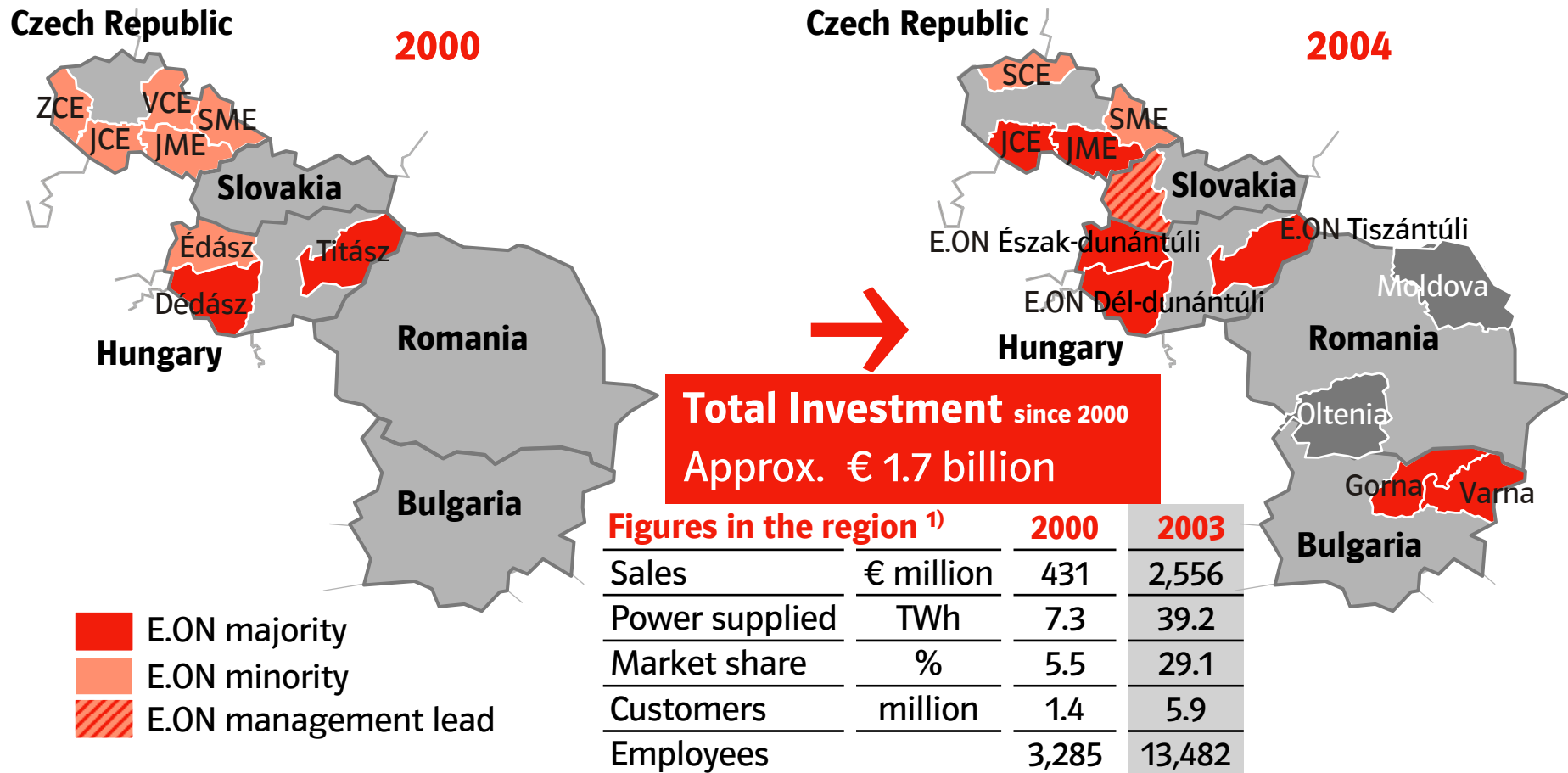
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Focus Region Central Europe



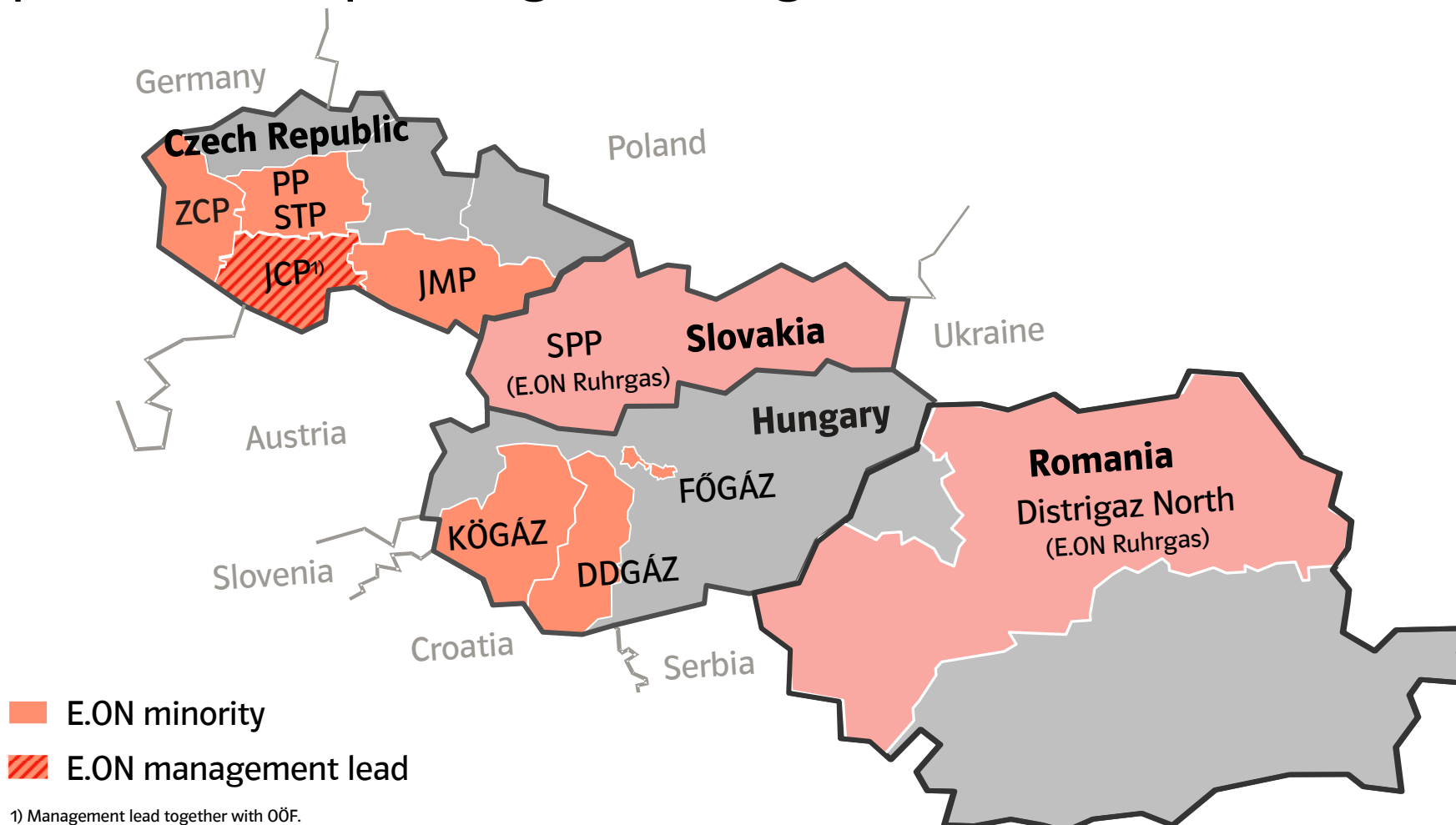
*32% outside Germany
Annual report 2003

Electricity: Through acquisitions and swaps E.ON Energie has achieved a significant consolidated market share in the region



1) Shareholdings with E.ON Energie management lead. Region: CZ, SK, HU, BG

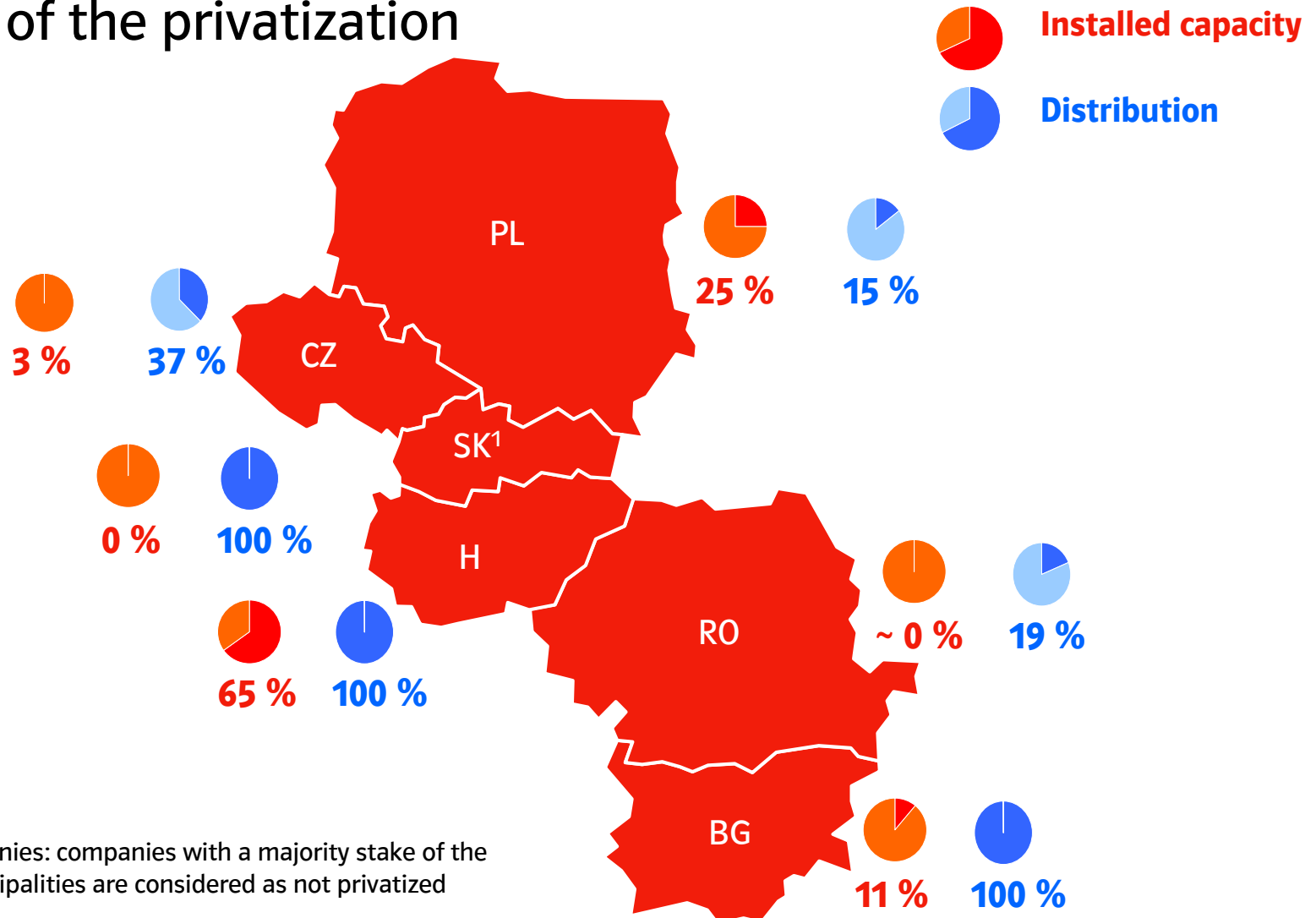
Gas: E.ON Energie well positioned to achieve majority positions and power-gas convergence



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Status of the privatization

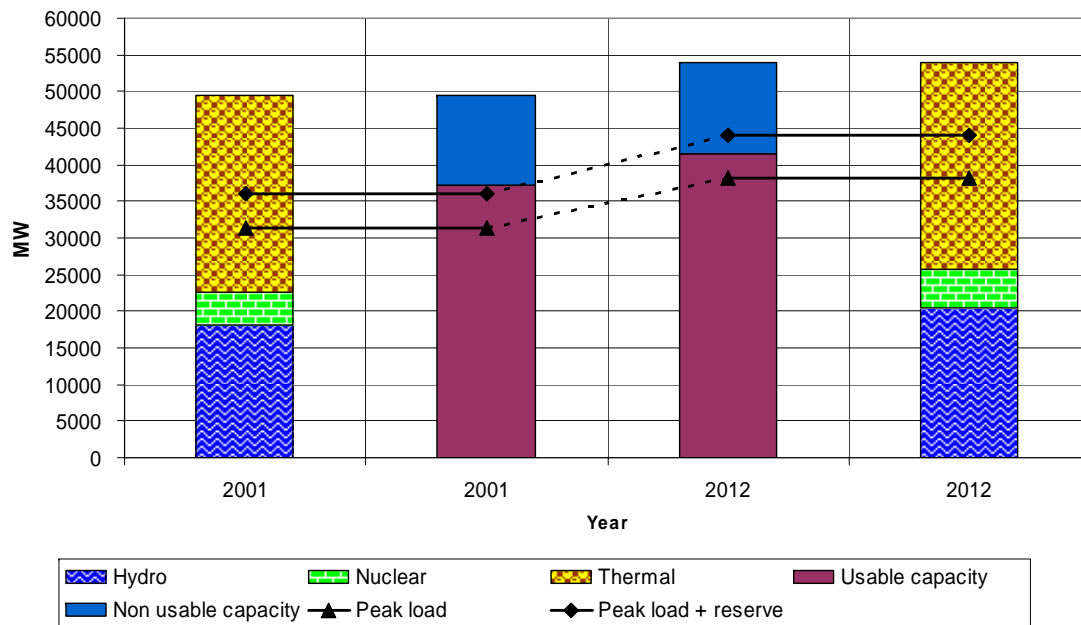


Private companies: companies with a majority stake of the state or municipalities are considered as not privatized

¹ Privatisation in process

High investment need in SEE according the World Bank *

SEE: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Macedonia, Romania, Serbia and Montenegro



- **Around 4500 MW (additional generating capacity) will be required over the next ten years, together with the substantial rehabilitation of existing plants (about 2.500 MW)**
- **The associated financing requirement would be well in excess of 5 bn USD**
- **Additionally also large investment in transmission and distribution is necessary to meet security of supply as well as environmental standards**
- **In 2005, according to the „Bank Austria Creditanstalt“ the foreign direct investments in SEE will be amounted 8,4 bn €**

* World Bank-Study, Review of Electricity Supply and Demand in Southeast Europe, Copyright 2004

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Concentration on focus regions triggers optimization of acquisition capital

Synergies and advantages of scale

- Physical and economic synergies in adjacent regions
- Interconnection advantages and risk limitation through integration of value chain in the regions

Terms and conditions of the market

- Comparable political and regulatory terms and conditions in the regions

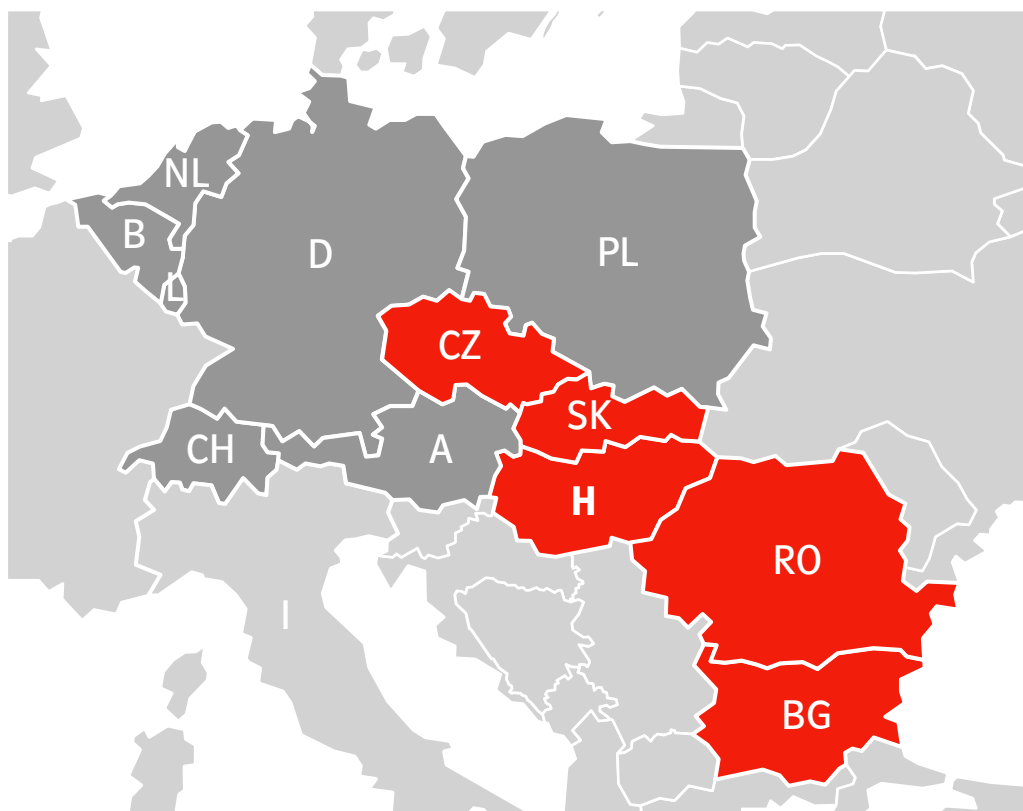
Leading position

- Leadership as sole strategic investor
- Significant market share
- Entrepreneurial freedom for restructuring of assets

Balanced portfolio

- Balanced mix between developed and transforming markets
-

E.ON Energie is considering the creation of power generation capacity as an asset-backing measure for existing distribution and sales activities



Opportunities

- Privatization (Bulgaria / Romania)
- New development in generation (HU, CZ, SK, RO, BU) gas and coal

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Criteria for the selection of projects

Strategic Criteria

- Market attractiveness
(returns, growth, regulation)
 - Political and economic stability
 - Target attractiveness
(asset quality, market position,
management quality)
 - Value creation potential
(cost reduction, integration benefits,
transfer of best practice)
-

Financial Criteria

- Earnings enhancing in the first full year
after acquisition
 - Returns exceeding cost of capital three
years after acquisition
in general
 - Not endanger Group performance
targets
-

E.ON Energie's success factors also applicable in Central Europe East

PAI – Process

- Conception during M&A process
- Creating transparency in Controlling
- Integration into E.ON's overall strategy

Integration

Best Practice

- Knowledge exchange between subsidiaries
- Efficiency gains through best practice processes
- Setting high standards for all Group members

Cost leadership

Decentralized Structure

- Autonomous subsidiaries
- Own Board of Management for subsidiaries
- Close contact to the local market

Corporate governance

Consequent integration and restructuring is key success factor in Central East Europe

Integration of acquired business units - Example ZSE

- Restructuring of state-run distributor to competitive market player
 - Core competence „professionell managing of PAI-Projects“
 - Organisational and financial targets delivered within 12 months
-

Merger and restructuring project - Example Czech.ON

- Merger of power distributors JME and JCE with power trader MEAS
 - Pilot project concerning fulfillment of „unbundling“ - requirements
-

Transnational Synergies - Example ZEUS

- Process optimization involving distributors in Hungaria, Slovakia and Czech Republic
 - Integration of region following „OneE.ON“ - identity
-

Best-Practice Projects - Example e.on@future in Central Europe East

- Adopting German best-practice processes to CEE environment
 - Integration into group-wide solutions, such as IT or procurement
-

Complete Integration into group - wide E.ON Energie - risk management

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The electricity costs (excluding all kinds of public issues) in the medium- and long-term in all EU-Countries will be comparable

Reasons

- Comparable environmental standards
- Same fuel suppliers
- Labor costs have marginal relevance
- New generation capacity needed
- Improvement of the efficiency and continuing growth of appropriate cross board transmission lines
- Cross board trading development according ETSO-Directive

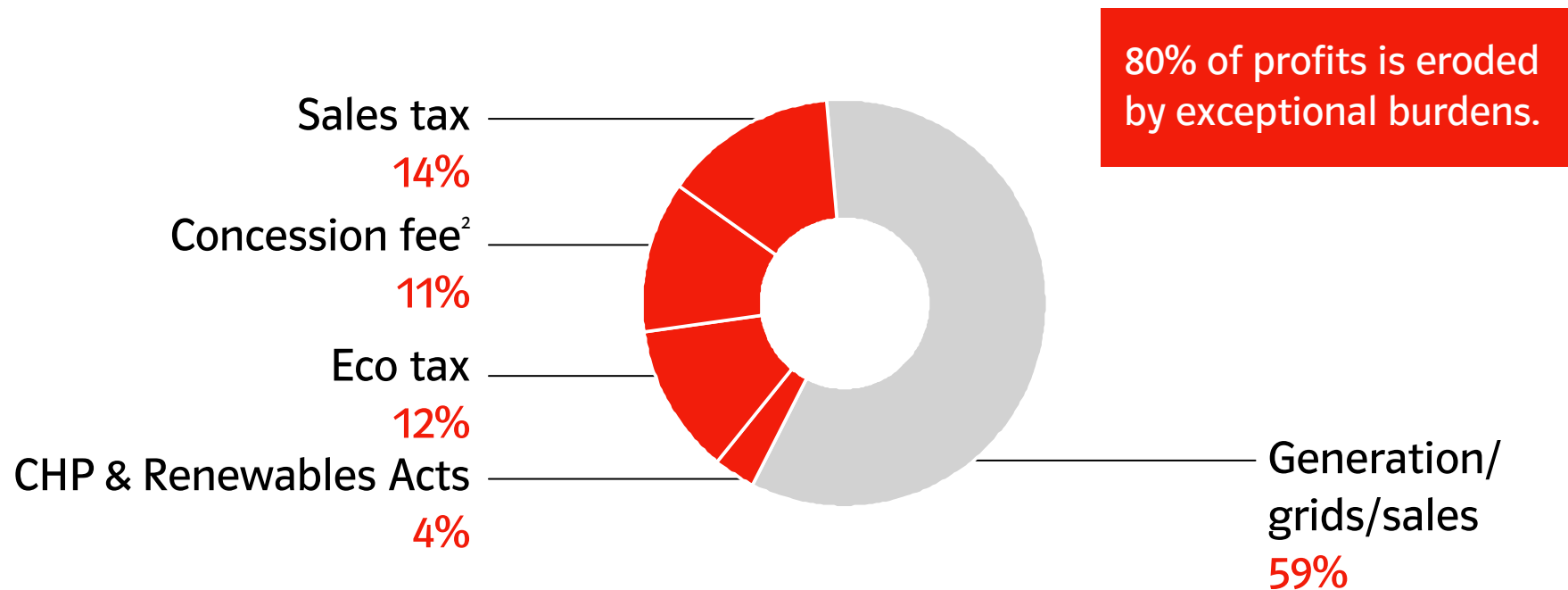
Exception

- Hydropower has advantages but without a high practical relevance, due to limited expansion potential
- Lignite in selected locations
- As the case may be nuclear energy (due to state intervention)
- Free allocation of emission certificates
- Other state burdens or subventions

Increasing convergence of the wholesale prices
(without UK/Nordic Countries)

Electricity Price in 2003: State Accounts for 41%

**Average price for private customers¹ :
17.12 ct/kWh**



Source: German Energy Industry Association (VDEW).

¹Electricity supplied to households; annual sales volume: 3,500 kWh.

²Concession fee in cities with between 100,000 and 500,000 residents.

Increase of cross board transmission capacity

Pro's

- Minimum size and number of market players needed to create functioning market
- Artificial generation location (subsidized wind power) create necessity for more transmission capacity e.g. German, the Netherlands

Con's

- The transport of electricity is unprofitable for distances greater than 250 km as a result of grid loss¹⁾
- UCTE: More interconnectors mean more artificial trade which pressurizes the system. This can lead to power cuts such as that in Italy last year". The UCTE believes expanding interconnectors endangers rather than protects supplies

Erection of new generation capacity will reduce long distance transport foster the development of liquid markets

??? How to incentive and steer additional cross board capacity in a regulated market ???

Competition for assets (privatization, acquisitions)

Western utilities

- Know how (experience) in liberalization process and transformation markets
- Financial capabilities
- Track record experience from the deal development via the acquisition until the integration process

Eastern utilities

- Lack of financial and transaction experience
- CEZ is the only exception on the acquisition market
- Privatization in some countries slowed down due to increased own financial capabilities (e.g. Slovenia) and increasing knowledge and self-confidence (Poland)

Western utilities dominate as acquirer of East European utilities in privatizations and sales

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Financial Investors

All that glistens is not gold

- Financial investors sometimes offers the highest price
- Their target is normally a short term optimization
- Some are not interested in the long term sustainable development of the company and sector
- They often cash-out the target company and/or sell essential parts of the company

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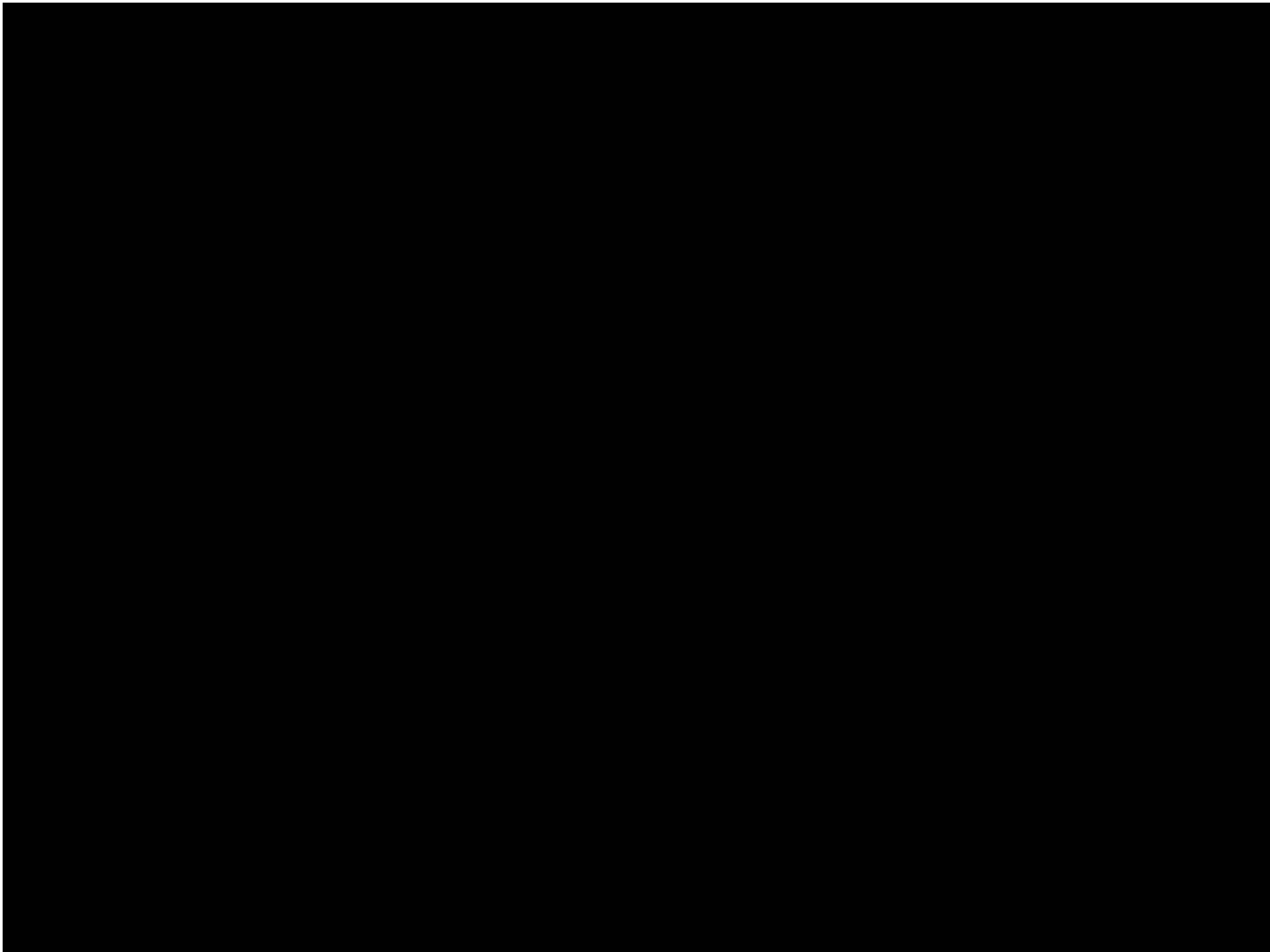
Summary

Large investment needs in Central Europe East

- Ongoing privatization, liberalization and integration of electricity and gas markets
- Rehabilitation and environmental requirements
- Necessity of additional generation capacity (medium term)

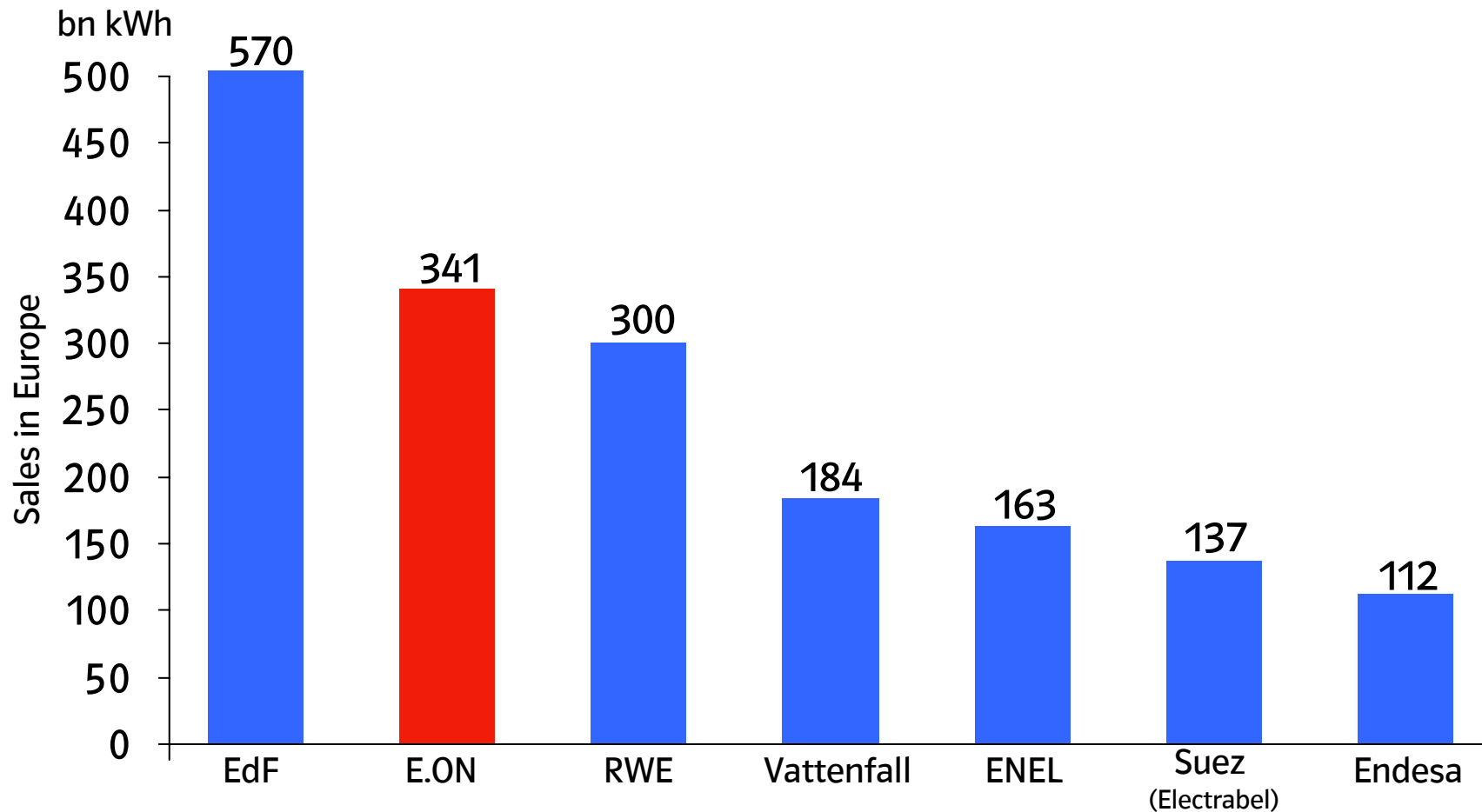
E.ON Energie

- Extensively involved in Central and Central Europe East
- Experienced in transformation and privatization processes
- A long term, reliable, private experienced, cash rich, strong strategic investor
- Respecting local politics and interests, sociopolitical responsibility, good responsible employer



Backup

E.ON Group: Electricity Sales of Leading European Utilities

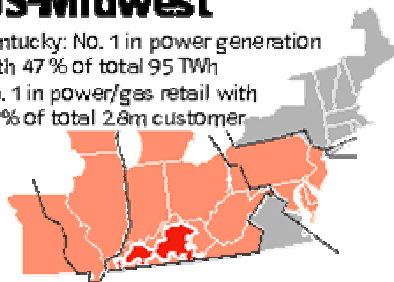


E.ON has strong positions in five target markets

Market positions – power and gas

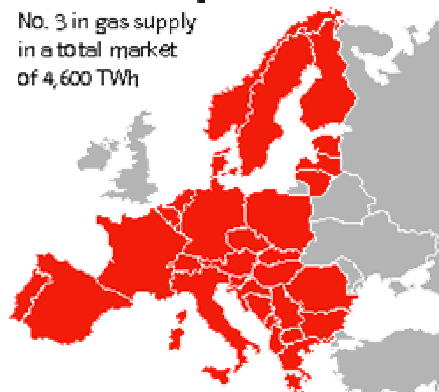
US-Midwest

Kentucky: No. 1 in power generation with 47 % of total 95 TWh
 No. 1 in power/gas retail with 42% of total 2.8m customer



Pan-European Gas

No. 3 in gas supply in a total market of 4,600 TWh



Source: E.ON New Energy - Powering Performance 2003/8

Nordic

No. 4 in power generation with 9 % of total 390 TWh
 No. 3 in power/gas retail with 7 % ³⁾ of total 14m cust.

UK

No. 2 in power generation with 17% of total 350 TWh
 No. 2 in power/gas retail with 18 % of total 49m cust.

Central Europe

No. 2 in power generation with 13 % of total 1,050 TWh^{1),2)}
 No.1 in power/gas retail with 20 % of total ~ 130m cust^{1),2)}

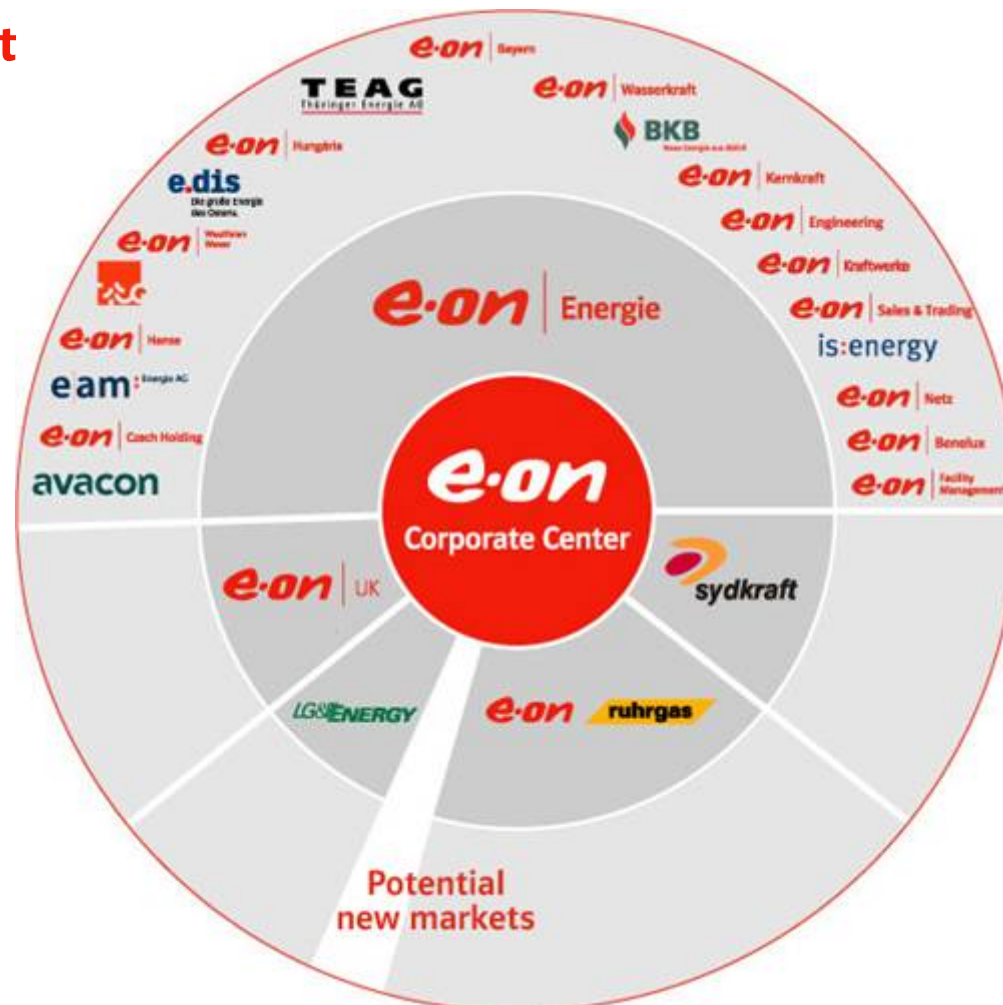
¹⁾ includes Germany, Netherlands, Austria, Switzerland, Hungary, Slovakia, Czech Republic, Poland
²⁾ includes minorities ≥ 20 %
³⁾ Preconsolidation of Orange

Our vision and mission

The success of the on-top project

E.ON will

- provide competitive solutions for its customers, their lives and businesses
 - stay on top by being an integrated power and gas company
 - combine international strength with local focus
 - apply the best ideas from across the Group
- **Be the world's leading power and gas company**



End of Backup