

INVESTMENT THESIS, THE TARGET

We have reviewed The Target and we assess the attractiveness of this investment as medium-to-high compared to other business opportunities in the CHP sector in Romania. The Target is one the largest CHP generators in Romania. The firm is 100% owned by the county council.

The Target is an attractive investment opportunity because:

- It owns and operates medium-to-large electricity (200MW and 2,100t/h installed capacity) and heat generation assets
- It has easy access to big energy-intensive local industry with potentially growing demand for energy
- The local heat market has a decent local household reference price
- You can trade electricity on a fairly liquid market (day-ahead market) administered by OPCOM
- In addition to revenues from electricity and heat trading, you receive a bonus for CHP output (EUR 26.4/MWh, average gas fired CHP bonus for the next 11 years)
- Since the region has a good biomass potential from forestry, you may have access to support mechanisms for renewable energy if you convert the existing generation assets into a biomass fired CHP plant. The current regulation awards one green certificate (GC) per MWh produced from biomass that can be sold on a fairly liquid OPCOM's GC market for EUR 42 (GC price for September 2008). However, legislation gives three GCs per MWh to biomass power generators, which will boost revenues from GC trading. This legislation was passed in the parliament and is expected to be signed by the president in the next month or so
- Overall, we estimate that the investor could earn around EUR 16,630 for every 100MWh and 100Gcal from power sold on day-ahead market and heat delivered to households. The calculation includes bonus scheme for CHP. Liberalised contracts with local industry and new renewable legislation would further increase the total revenues for the investor
- Romania is currently implementing a friendly investment regulation in the CHP sector, awarding a bonus for each MWh generated in CHP plants. The total installed capacity nation-wide which will benefit of the CHP bonus aid scheme is capped at 4,000MW

We estimate that the main risks of this investment opportunity are:

- A smaller household market (around 30,000 apartments connected) compared to other mid and large sized cities in Romania
- Potential financing difficulties of some local industry players can decrease the demand for heat and power in short to medium term
- Energy efficiency driven by privatisation of local state industry (a chemical plant mainly) may slow down the demand for heat in long term

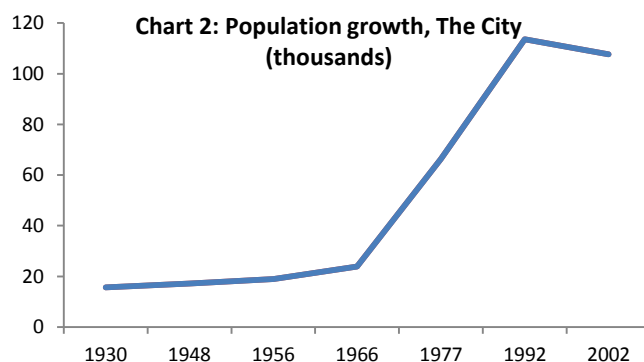
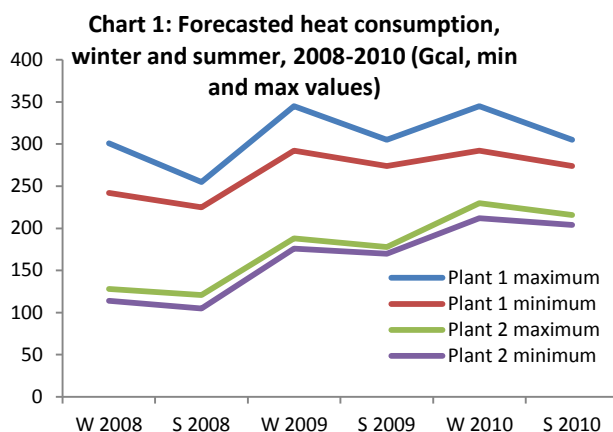
DESCRIPTION OF INVESTMENT OPPORTUNITY

<i>Opportunity</i>	The Target seeks investors/partners to invest in modernisation of its CHP power plant).
<i>Investment value</i>	EUR 218mn (VAT excluded) of which EUR 78mn (VAT excluded) are minimum emergency investment.
<i>Type of investment</i>	Unknown. The Target has not defined yet whether it will be a competitive tender or proprietary deal. The Target has not decided about the form of partnership yet.
<i>About the target</i>	The Target is one of the largest CHP generators in Romania. Its electricity market share was 0.9% of total power delivered to the grid between January – July 2008. It is 100% owned by the county council.
<i>Business model</i>	<ul style="list-style-type: none"> ▪ Electricity generator. The power is taken into the grid through 110KV voltage wires ▪ Heat generator for industry located in the south of the city (115,000 habitants). Among largest industrial consumers are: <ul style="list-style-type: none"> ▪ Chemical plant: manufacturer of organic basic chemicals. ▪ Chemical plant: manufacturer of inorganic basic chemicals. ▪ Equipment producer for chemical and energy sectors. ▪ Manufacturer of cotton-type fibres. ▪ Supplies heat and hot water to the city (107,726 habitants) ▪ Supplies heat and hot water to the town (8,633habitants) (geothermal) ▪ Supplies heat and hot water to the town (4,610 habitants)

Market Opportunities

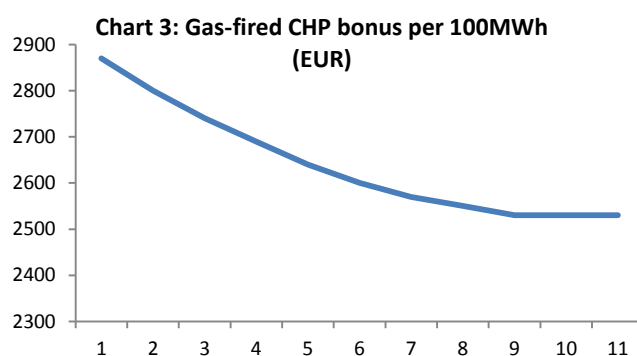
LOCAL MARKET:

- Increasing forecasted heat consumption of local industry (see Chart 1).
- Access to mid-sized household market (See Chart 2. Population in 2002: 107,726, CAGR: 31.7% for period between 1930-2002).
- Stable household market for district heating. Disconnection rate: 10.6% (around 3,500 out of 35,000 total apartments). According to data published by district heating regulator (ANRSC), no disconnection occurred in 2008.
- For each 100Gcals sold to the local distribution firm, you receive minimum EUR 7,750 (100Gcal * EUR 77.5/Gcal regulated local heat price for gas-fired plants, VAT included) from households. There is an indirect subsidy paid by the government to local administration to cover 45% of the fuel price.
- Good biomass potential from forestry in the region that can grant you access to the bonus (GC) for renewables (EUR 42/MWh in September 2008) which can secure EUR 4,200 for every 100MWh delivered to the grid. After legislation approved by the parliament is enacted by the president, the figure will be three times higher (3GCs/MWh produced in biomass-fuelled power plants).



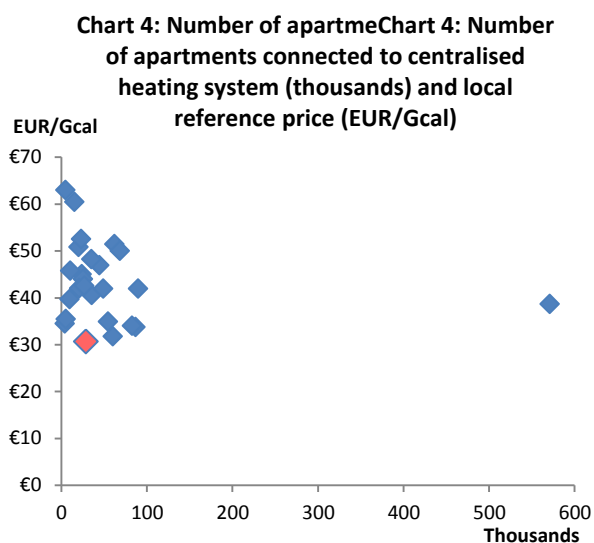
NATIONAL MARKET

- Priority grid access for electricity produced in cogeneration
- CHP bonus per MWh produced in cogeneration and delivered to the grid (see Chart 3). Average bonus for gas-fired CHP plant will be EUR 26.4/MWh over the next 11 years
- Over the next 11 years, you may receive on average EUR 8,880 for each 100MWh delivered to the grid [100MWh * EUR 26.4/MWh bonus + 100MWh * EUR 62.4/MWh average price on day-ahead market in September 2008 = EUR 8,880]
- Overall, you may receive around EUR 16,630 for an output of 100MWh and 100Gcals (liberalised contracts with industry excluded).



Investment risks

- Small household heat market and low local reference price for heating compared to other cities in Romania (see Chart 4; The City is red coloured). Botosani and Vaslui (east of Romania) have the local reference prices two times higher than The City, but have fewer apartments connected to centralised heat system. Braila, Buzau and Tg. Mures (cities comparable to The City in terms of number of apartments connected to centralised system – around 25,000) have higher local reference prices (EUR 50, 53 and 43, respectively)
- The main industry firms, Plant 1 and Plant 2, have registered very small or negative gross profits in the last three years. Plant 1 registered a loss of RON 96mn in 2007. Plant 2 posted a gross loss of RON 69.3mn in 2007
- The liquidity ratios are well below 100%, suggesting that the two firms have problems securing capital for current debts (see Annex 1). Plant 1 has a negative trend but Plant 2 succeeded to increase the liquidity ratio from 30% to almost 70% in the last three years
- Energy efficiency investments of local industry (Plant 1 particularly, if privatised) could lead to stagnant local demand for heat



CANDOLE’S OVERALL INVESTMENT ATTRACTIVENESS RANKING: MEDIUM-TO-HIGH

We estimate that the attractiveness of this investment opportunity is above average compared to other opportunities in CHP sector for the following reasons:

Cogeneration is promoted. Romania is currently implementing an investment friendly CHP regulation (priority grid access, bonus per MWh). You can trade the electricity output on a fairly liquid market (day-ahead market) at OPCOM or sign bilateral contracts with the local industry.

RES potential. The existing CHP plant can be converted into a biomass fired CHP plant which will grant you access to support mechanisms for renewable energy and will decrease the costs of CO₂ allowances. This will allow you to apply for state-aid funding for investments in renewable energy, which may cover up to 50% of eligible costs.

Demand bound to increase. Local demand for electricity and heating will increase over the next 3-5 years given the high industry potential of the region. The likely privatisation of Plant 1 by the privatisation agency (AVAS) will boost the demand for power and heat in medium future.

Among negative factors, we highlight the small household market and financial troubles of the two biggest local industrial players, Plant 1 and Plant 2, in the last three years.

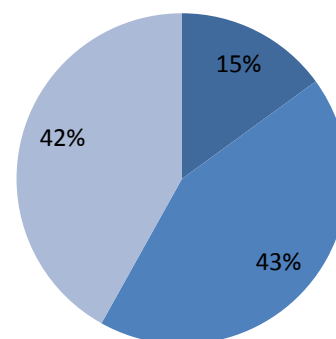
Existing assets

- Two C4 Vulcan boilers of 420t/h each, on gas or oil, PIF years: 1973 and 1976, both modernised
- Three CR 1244 boilers of 420t/h each, on lignite, gas or oil, PIF years: 1986, 1987 and 1993
- Two condensing DSL-50 turbines of 50MW each
- Two counter-pressure DKUL-50 turbines of 50MW each

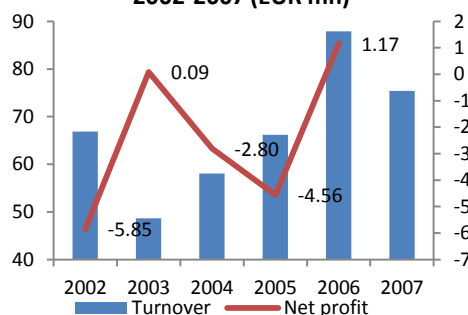
Financial information

- EUR 75.4mn total turnover in 2007
- Main customers:
 - Electrica: EUR 31.6mn from power sales
 - Plant 1: EUR 22.2mn from steam sales
 - Plant 2: EUR 9.6mn from steam sales
 - The city: EUR 11.3mn from hot water sales

The Target revenues, 2007 (EUR mn)



Financial results, 2002-2007 (EUR mn)



Power grid connections

- 3 electric wires of 110kV, with individual capacity of 133MVA, connecting The Target to the transmission grid
- 1 air wire and 7 underground wires of 110kV, with total capacity of 381MVA, connecting The Target to the Plant 1
- 2 underground electric wires of 35kV, connecting The Target to the Plant 1.
- Underground electric wires of 6kV, connecting The Target to transmission power grid system, as back-up system for internal use of the CHP plant.
- Electric wire of 6kV to power Priza Olt pump station

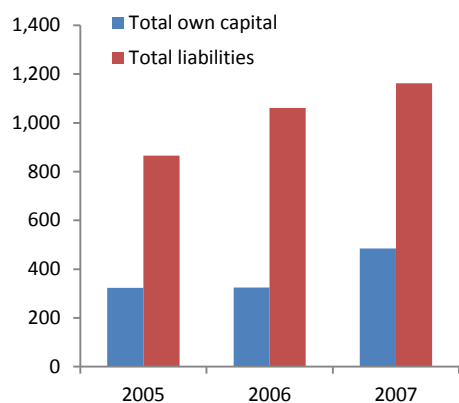
Heat pipes connections

- 5 steam transmission pipes of 28,13 and 6 bar to supply the Plant 2.
- 5 steam transmission pipes of 35, 13 and 6 bar to supply the Plant 2.
- Steam transmission pipes of 13 bar to supply the Company 1 and the Company 2.
- Hot water generation, transmission and distribution systems with maximum capacity of 2,723 t/h at maximum 150°C
- Direct water connection to The River.

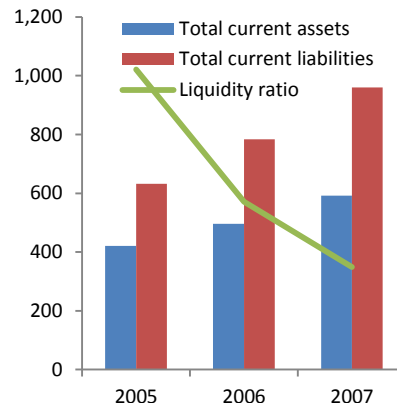
ANNEX 1: FINANCIAL INFORMATION, INDUSTRY MARKET

Plant 1:

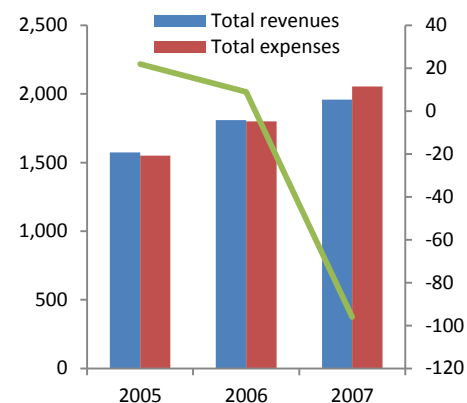
Total own capital vs. total liabilities (RON mn)



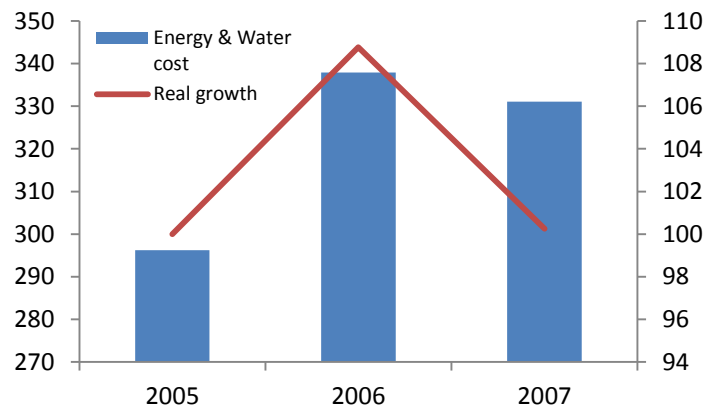
General liquidity ratios, 2005-2007 (RON mn)



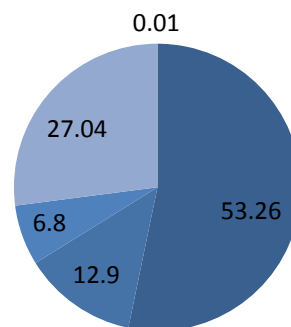
Financial results, 2005-2007 (RON mn)



Energy and water costs, absolute and relative (PCI indexed) growth (RON mn)



Shareholders' structure (%)

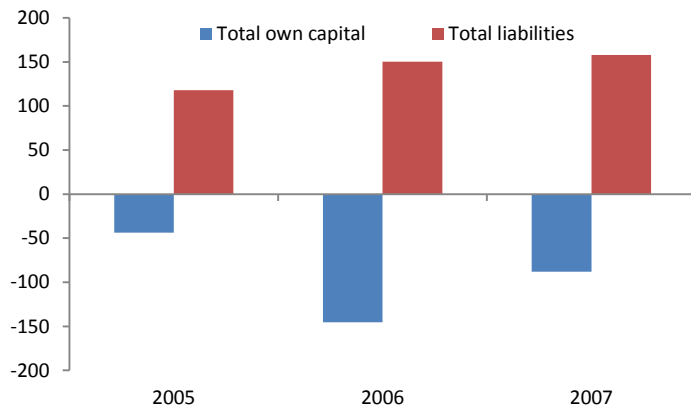


Source: Bucharest Stock Exchange and financial statements, 2005-2007

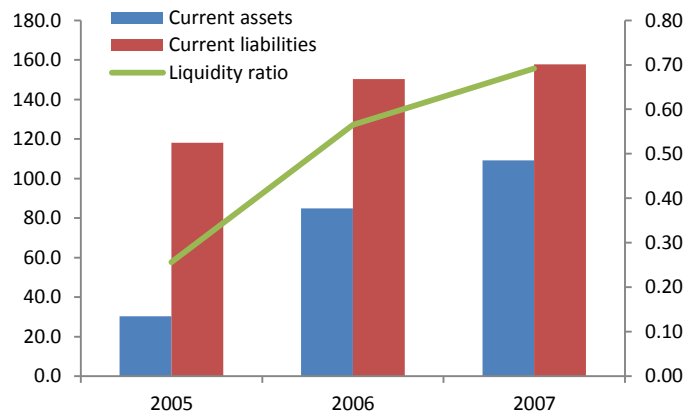
CANDOLE PARTNERS

Plant 2:

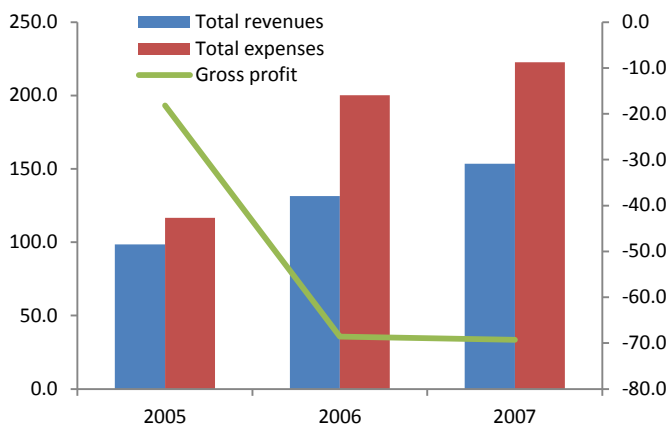
Total own capital vs. total liabilities (RON mn)



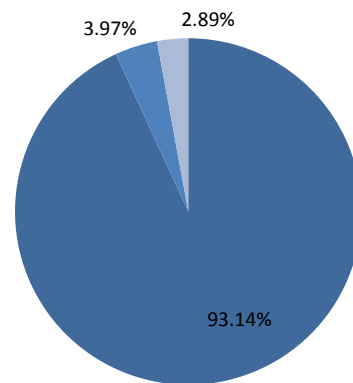
General liquidity ratios (RON mn)



Financial results, 2005-2007 (RON mn)



Shareholders' structure (%)



Source: Bucharest Stock Exchange and financial statements, 2005-2007

ANNEX 2: FORECASTED INDUSTRIAL STEAM CONSUMPTION

Industrial steam forecasted consumption, Plant 2 (84% forecasted rise of consumption)															
Pressure level	Winter 2008		Summer 2008		2008	Winter 2009		Summer 2009		2009	Winter 2010		Summer 2010		2010
	bar	Max	Min	Max		Min	Avg.	Max	Min		Max	Min	Avg.	Max	
35	77	72	75	71	74	77	72	75	71	74	77	72	75	71	74
13	144	110	120	104	120	154	120	130	114	130	154	120	130	114	130
6	80	60	60	50	65	114	100	100	89	100	114	100	100	89	100
Total	301	242	255	225	259	345	292	305	274	304	345	292	305	274	304

Source: The Target

Industrial steam forecasted consumption, Plant 2 (84% forecasted rise of consumption)															
Pressure level	Winter 2008		Summer 2008		2008	Winter 2009		Summer 2009		2009	Winter 2010		Summer 2010		2010
	bar	Max	Min	Max		Min	Avg.	Max	Min		Max	Min	Avg.	Max	
35	50	44	47	40	45	98	94	96	90	94	120	110	114	108	113
13	78	70	74	65	72	90	82	82	80	84	110	102	102	96	102
Total	128	114	121	105	117	188	176	178	170	178	230	212	216	204	215

Source: The Target

ANNEX 3: INVESTMENT COSTS OF MODERNISATION AND DEVELOPMENT OF THE TARGET

Investment costs for modernisation and development of The Target			
Project	Total cost (EUR mn)	Investment type	
		Efficiency improvement	Environmental compliance
Modernisation of boilers	21.0	18.0	3.0
Electro-filters and desulphurisation	66.0		66.0
Collecting, use and deposit ash	40.2		40.2
Modernisation of high/medium voltage power stations and networks	13.1	13.1	
Installing new turbines	25.3	25.3	
Modernisation of existing turbines	13.1	13.1	
Technological cooling system	10.1	10.1	
Replacement of hot water transmission pipes	8.3	8.3	
Modernisation of hot water generation system	8.6	8.6	
Modernisation of steam pipes & dispatch management system	4.7	4.7	
Modernisation of pipes and pumping systems	4.9	4.9	
Other costs (consultancy, project management)	3.0		
TOTAL	~218.4	~106.1	~110

Source: The Target

ANNEX 4: MINIMUM EMERGENCY INVESTMENTS

Minimum emergency investments (to be covered by state and county budgets)													
Project/investment [thousand euro]		Total	Year										
			2008	2009	2010	2011	2012	2013	2014	2015	2008-2011	2013-2015	
1	Finalising collecting dry ash, storage, moistening	1,900	1,900									1,900	0
2	Finalising PIF TA8-DKT 6,8 ,TA9-TKR 4,2	1,000	1,000									1,000	0
3	Replacement of hot water transmission pipe	8,300	900				1,400	2,000	2,000	2,000		900	6,000
4	Pumping system and transport of dense ash slurry	9,000	900		7,500	600						9,000	0
5	Turbine TA10 DKT 6,8 140/35 bar, 80 t/h 6,5 MW	5,600		3,200	2,400							5,600	0
6	Expanding dense ash slurry depot	9,600		1,500	1,500	1,900	2,400	2,300				4,900	2,300
7	Dry evacuation of slug	500		500								500	0
8	Electro-filters for boiler C7	4,000			2,000	2,000						4,000	0
9	Desulphurisation boiler C7	18,000			8,000	5,500	4,500					13,500	0
10	Rehabilitation of boiler C7	7,000			7,000							7,000	0
11	Modernisation of internal heat system	8,600						7,000	1,600			0	8,600
12	Modernisation of water supply systems (EPA)	4,920			1,640	1,640	1,640					3,280	0
Total Investment		78,420	4,700	5,200	30,040	11,640	9,940	11,300	3,600	2,000		51,580	16,900
Financed though state budget 60%		47,052	2,820	3,120	18,024	6,984	5,964	6,780	2,160	1,200		30,948	10,140
Financed through county council's budget 40%		31,368	1,880	2,080	12,016	4,656	3,976	4,520	1,440	800		20,632	6,760

Source: The Target

ANNEX 5: CO₂ EMISSION ALLOWANCES SHORTAGE (2008-2012)

Total CO ₂ allowances allocated	7,250,000 tonnes (1,425,000 t/year)	
Forecasted annual emissions	1,800,000 t/year	
Forecasted CO ₂ allowances deficit	425,000 tonnes	
Measures to cover CO ₂ allowances deficit	Year 2008	<ul style="list-style-type: none"> ▪ Reduction of condensing power by 160,000 MWh. CO₂ reduction: 235,000 tonnes. ▪ Mixing 40,000 tonnes of biomass with coal. CO₂ reduction: 65,000 tonnes. ▪ Allocation of CO₂ allowances for new entries (2 turbines). CO₂ equivalent: 60,000 tonnes. <p>Total CO₂ deficit: 65,000 tonnes</p>
	Year 2009-2010	<ul style="list-style-type: none"> ▪ Mixing 60,000 tonnes biomass with coal. CO₂ reduction: 100,000 tonnes. <p>Total CO₂ deficit: 30,000 tonnes</p>
	Year 2011	<ul style="list-style-type: none"> ▪ Building a biomass-fired power plant, 10MWe, 20MWt ▪ CO₂ reduction in 2011 and 2012: 85,000/year
Supplementary pollution allowances 2008-2012	55,000 tonnes CO ₂	

Source: The Target

ANNEX 6: DEADLINES OF ENVIRONMENTAL COMPLIANCE INVESTMENTS

Environmental objectives	Deadline for implementing
Evacuation, use and ecological storage of ash, slag and desulphurisation products	Dec. 2011
Obtaining CO ₂ allowance during 2008 – 2012	Dec. 2012
Reduction of polluting emissions (powders) bellow 50 mg/Nmc	IMA 2 – Dec 2011 IMA3 – Dec 2010
Reduction of SO ₂ emissions bellow 400 mg/Nmc	IMA 2 – Dec 2013 IMA3 – Dec 2011
Reduction of NO _x emissions bellow 400 mg/Nmc	IMA 2 – Dec 2013 IMA3 – Dec 2011
Reduction of water pollution	Permanent
Waste management	Permanent

Source: The Target