

APPROVED

by the Order No 1K-186 of 19 June 2020 of the
Minister of Finance of the Republic of Lithuania

LETTER
ON THE OBJECTIVES PURSUED AND THE EXPECTATIONS SET BY THE STATE
THAT ARE RELATED TO THE ACTIVITIES OF UAB IGNITIS GRUPĖ GROUP OF
COMPANIES

This letter presents the expectations of the State, the shareholder of UAB Ignitis Grupė (hereinafter – the Company), which is represented by the Ministry of Finance of the Republic of Lithuania, regarding the activities, priorities, principles of activities and objectives of UAB Ignitis Grupė Group of Energy Companies (hereinafter – the Group).

Activities

The activities of the Group include electricity and gas distribution, generation and development of green energy, management of flexible electricity generation facilities, electricity and gas supply, development of energy-smart solutions, and other commercial activities. Activities of the Group which are of strategic importance to the State: management of the strategic infrastructures of the Lithuanian energy system and carrying out the projects of strategic importance according to the National energy independence strategy¹.

The general principles of corporate governance for the Group are set out in the Description of Corporate Governance Guidelines for the State-Owned Energy Group approved by the Minister of Finance of the Republic of Lithuania².

The Company, which is the Parent Company of the Group, is responsible for the transparent management and coordination of the Group activities, increasing efficiency in order to provide competitive services to the customers and in ensuring a socially responsible increase of long-term value for the State.

Priorities of the activities, principles and goals

The activities of the Group must be related to sustainable and socially responsible development by further developing a modern, international, competitive Group. The shareholder expects for a consistent and purposeful growth of the Group by modernizing the energy infrastructure and developing new energy competencies.

Given the strategic impact on the Lithuanian energy system, by its activities the Group contributes to the implementation of the goals of the National Energy Independence Strategy and integrates them by formulating its long-term and short-term priorities of the activities, and by focusing on the National Energy Independence Strategy goals which are directly related to the activities and goals of the Group:

¹ Resolution No XIII-1288 of the Seimas of the Republic of Lithuania of 21 June 2018 on the Amendment of the Resolution No XI-2133 of the Seimas of the Republic of Lithuania of 26 June 2012 on the Approval of the National energy independence strategy.

² Order No 1K-205 of the Minister of Finance of the Republic of Lithuania of 7 June 2013 on the approval of the description of the corporate governance guidelines of the state-owned energy company group (version of the Order No 1K-82 of the Minister of Finance of the Republic of Lithuania of 26 March 2020)

-development of green energy and sustainable bioenergy, and of wind farms in the Baltic Sea to increase electricity generation in Lithuania because currently only slightly more than one quarter of total Lithuanian electricity consumption demand, which increases as the gross domestic product changes, is generated;

- smart energy development by developing digital energy networks and smart meters to help save energy;
- synchronization with a reliable and continental European energy system to ensure Lithuania's energy system independence;
- development and implementation of energy innovations in the region, as well as the development of prosumers and of electric vehicles solutions, promoting sustainable energy use, etc.

The expectations of the activities of the Group are formulated taking into account the strategic importance of the assets used in the activities of the Group to ensure the stability of the Lithuanian energy system. The aim is also to implement the innovative and modern - contemporary solutions that meet the needs of the local and global market, which would ensure the integration of the global and regional energy changes into the Lithuanian energy system. In recent years, the continuity of the activities of the Group and the consistency of development were carried out: projects of generation from renewable energy sources, which contribute to reducing global greenhouse gas emissions, were developed rapidly, the new business models were created, innovative energy solutions were developed and expansion has taken place in the region.

Expectations of the Group strategic priorities

1. To ensure a reliable and flexible Lithuanian energy system and its development, by contributing to the implementation of changes in the energy sector in Lithuania and in the region.
2. To expand green generation by contributing to Lithuania's and regional commitments to increase electricity generation from renewable energy sources.
3. To develop innovative solutions and to actively seek new opportunities for profitable development of activities.
4. To ensure sustainable development of the activities of the Group:
 - to follow the principles of environmental and social responsibility as well as of good governance practical principles (including the criteria of transparency of activities of the state-owned companies);
 - to contribute to achieving the sustainable development goals of the United Nations (hereinafter - the Sustainable Development) by giving priority to the Sustainable Development goals which are most affected by the activities of the Group;
 - to consistently reduce greenhouse gas emissions;
 - to restrain from development of electricity generation capacity on the basis of coal and nuclear energy.

Expectations by priority activities

Networks

Priority is given to ensuring the resistance of the electricity and gas distribution network to externalities, efficient distribution of electricity and gas, and to implementation of changes in the energy sector, and to increasing electricity generation from renewable energy sources. Therefore, the Group must continue to invest in Lithuanian electricity and gas distribution networks in striving to modernize this asset

of strategic importance, as well as to digitize the electricity distribution network by implementing the smart meter installation program to the extent planned, and to consistently improve the quality indicators of distribution networks.

Green generation

Priority is given to the targeted, sustainable and profitable development of green generation. The Group should continue to look for ways to increase electricity generation and should invest in electricity generation from renewable energy sources both in Lithuania and abroad (both in countries where the Group already operates and in countries where changes in the energy sector are beginning to be implemented through transition to the development of renewable energy sources). The main green generation technologies in which the Group should invest include wind (including offshore wind), solar energy, biofuels and waste. In order to absorb new technologies, the Group is recommended to cooperate with partners which have experience in implementing this type of investment. The development of green generation must be carried out in accordance with the principles of financial discipline return on projects must be consistent with the risk taken, and the project debt level should be in line with the market practice applied by banks. To maximize returns on projects and to use financial resources efficiently, the asset rotation strategy, which is common in the energy sector, under which part of the projects is sold to financial investors, is recommended to be considered.

Flexible generation

Priority is given to ensuring a reliable and flexible Lithuanian energy system by providing reserve and system services. New flexible electricity generation capacities can be developed if market conditions allow to do so, and the development meets the return expectations posed, worn-out conventional electricity generation facilities must also be decommissioned and they must be dismantled The Group must contribute to successful synchronization of the Baltic energy system with the continental European electricity grid system, must carry out the necessary preparatory works in order to adapt effectively to the continuously changing market of system services.

Customers and Solutions

Priority is given to the development of innovative energy solutions that create added value and to the implementation thereof by contributing to the development of the energy sector, to electricity and gas supply and trade, and its to ensuring their development in the region. Innovative solutions should be developed together with the partners, by contributing to environmental objectives and by striving to help the consumers to become energy smart.

Financial expectations

Initial public offering

In order to implement strategic priorities and at the same time to ensure financial discipline, the Company needs to prepare for the initial public offering with the goal to execute it, subject to appropriate market conditions. The Company must prepare for the IPO by September 2020. The newly issued shares should make up at least 25 percent and not more than 33.33 percent of all shares of the Company.

Dividends

Company has to strive delivering dividends to the shareholders in line with the growth of the Group. The dividend policy of the Group has to be established in accordance with the Resolutions of the Government of the Republic of Lithuania.

Structure of the capital

The Company has to maintain a high investment credit rating (BBB and higher), and the net debt of the Group in the medium and long term should not exceed amount of 5-year annual earnings before interest, tax, depreciation and amortization (EBITDA).

Return on equity

In implementing the strategy of the Group, the Company must ensure the return on equity (ROE) set by the Government of the Republic of Lithuania, which, in the period of 2019-2021, is set not less than 6.6 percent. When investing outside Lithuania, the risks associated with the investment should be adequately assessed and an appropriate return on capital should be ensured.

Non-financial expectations

Good environmental, social responsibility and corporate governance practice

Criterion for environmental, social responsibility and good governance practice must be integrated into the long-term business objectives of the Group, the commitment to reduce net carbon emissions to zero by 2050 must be also implemented consistently, and its implementation must be monitored, and there must be contribution to the implementation of the Sustainable development goals, which are most affected by the activities of the Group.

The Group must maintain the level of maturity of corporate governance and the highest corporate governance level index which is granted subject to the evaluation by the Governance Coordination Centre. The Group must continue to follow the requirements of the Organization for Economic Co-operation and Development (OECD), and of stock exchanges on which it is listed, as well as good governance practices of international companies, thus showing an example to follow by other state-owned companies. The Group must apply in all its activities the highest standards of transparency and the principles of depoliticised activities. The Group must continue to refine the activities, to eliminate non-core activities altogether and must continue to increase efficiency of both the core functions and of the service and support functions.

Implementation of innovation and digitization program in energy

In addition to investment in electricity generation capacity and infrastructure development, which allow ensuring efficient energy activities, competitiveness of the country's economy, provision of quality energy services, the Group should continue the digitization program of the Company and investing in start-ups that develop new services in energy. The Company must also continue implementing the initiative to apply the latest technologies and innovate so that, in close cooperation with the local and international business and the scientific community, potential for the export of innovative energy products and services would be created. Implementation of the energy efficiency solutions would allow the Group to reduce customer costs of electricity and would thus increase their competitiveness in domestic and international markets.

Accountability

It is appropriate for the Supervisory Board, which is the supervisory body of the Company and of the Group, to maintain the existing practice, and to submit to the shareholders periodically, on a quarterly basis, a summary report of the Group activities

The shareholder hopes that the management and supervisory bodies of the Group will continue good corporate governance practices and will carry out once a year evaluation of their activities and will also agree on further steps to improve the functioning of these management and supervisory bodies.
