

Creating solid earnings growth in Russia

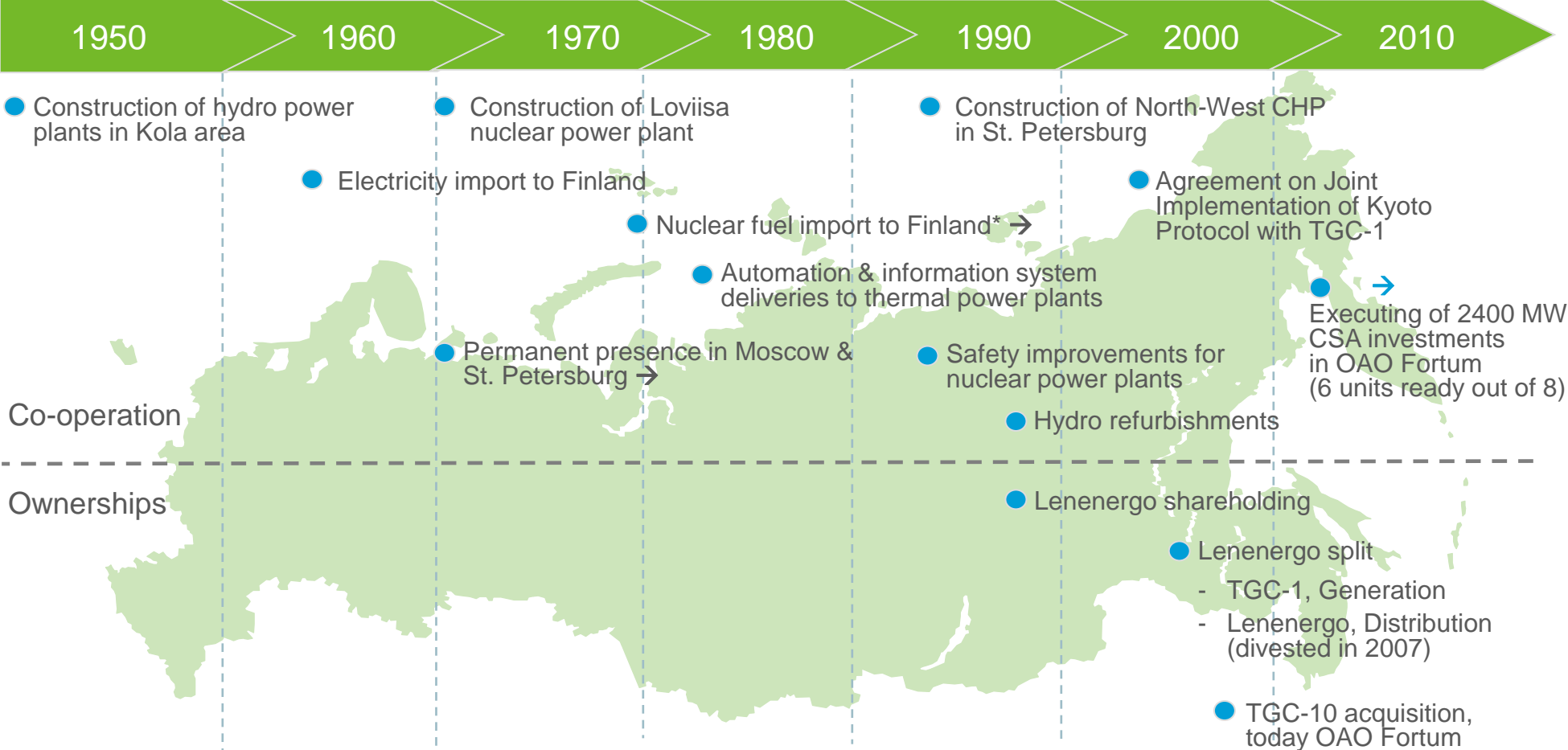
Fortum Capital Markets Day
5 November 2014

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Executive Vice President, Russia

Agenda

- Fortum in Russia
- The Russian power market reform
- Key competitive advantages of Fortum
- Update on Russian heat market reform
- Summary

Fortum has long experience of co-operation with the Soviet Union and Russia



*) Including single largest purchase agreement of uranium with TVEL

The Russian power market reform was the world's largest single power market reform and completed by the end of 2011

2003	2006	2007	2008	2010	2011	2013	Ongoing
Transitional model of electricity markets.	<p>Launch of the current electricity markets model.</p> <p>Only volumes deviating from the expected power balance were traded at market prices.</p>	Start of deregulation of the traded electricity volumes.	<p>Launch of the capacity market transitional model.</p> <p>Start of deregulation of the traded capacity volumes.</p>	<p>Adoption of the target capacity market rules.</p> <p>Launch of the system services market.</p> <p>Start of the electricity futures trading.</p>	<p>All purchased/sold volumes are supplied at unregulated prices, except for supply to households and consumers of some regions.</p> <p>Launch of the target capacity market model.</p>	Launch of RES support model	<ul style="list-style-type: none"> • Heat market reform • Cross-subsidies removal • Gas prices liberalization • Next Energy market model development • Must run generation regulation changes

Day-ahead (spot) market

Deregulation of electricity volumes				
2007	2008	2009	2010	2011
5-10%	15-25%	30-50%	60-80%	100%

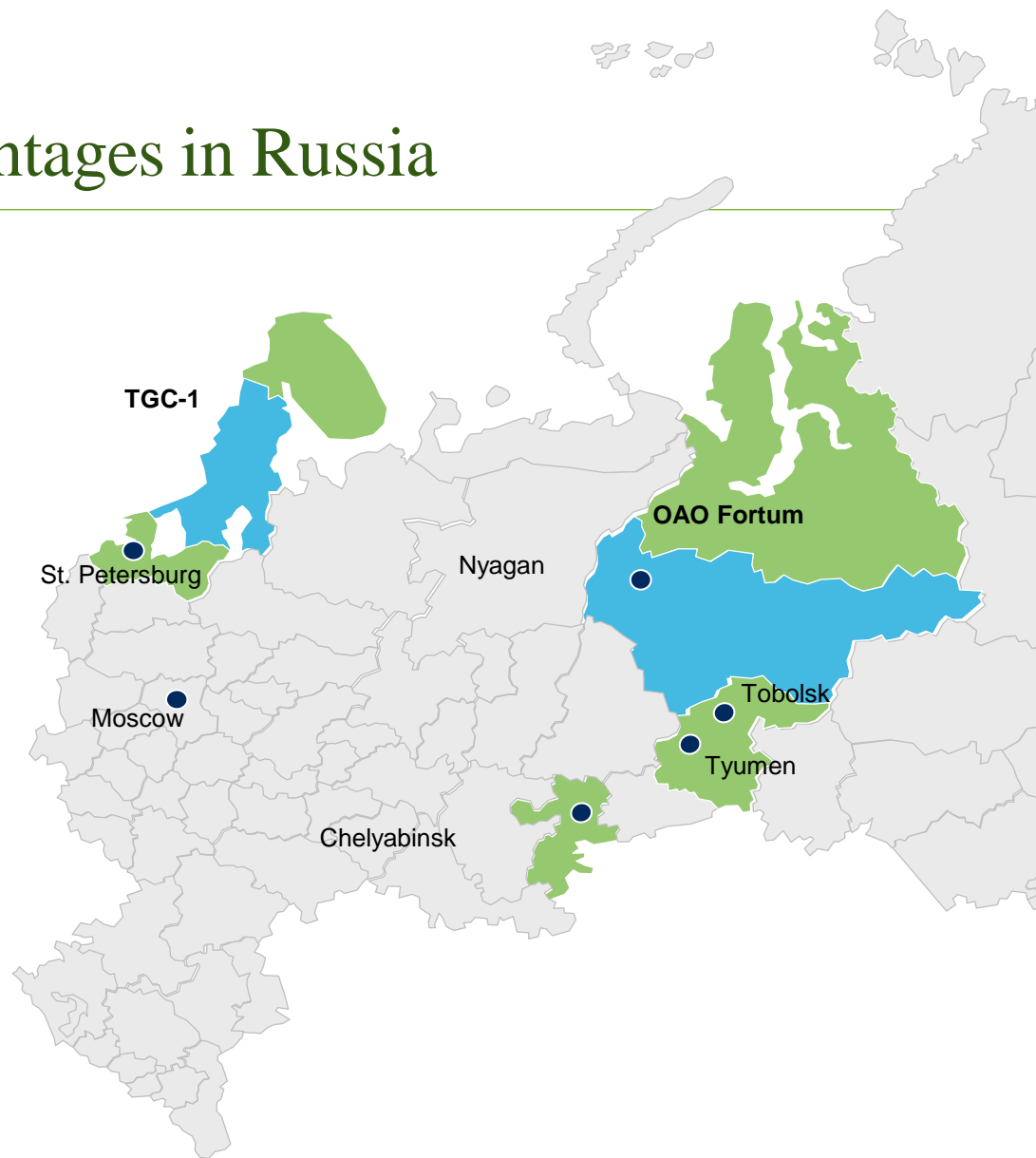
Capacity Market

Deregulation of capacity volumes

Source: Fortum Industrial Intelligence

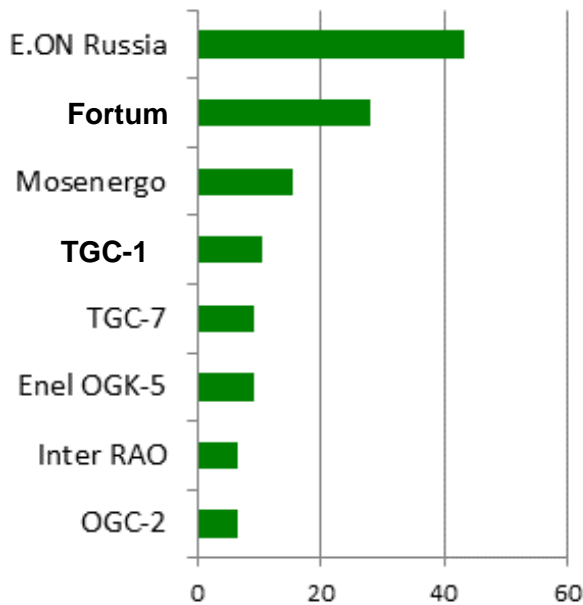
Fortum's key competitive advantages in Russia

- Newest and the most efficient fleet among competitors. Most of the fleet are CHPs
- Solid financial results, reliable, safe and environmentally friendly operations
- Good reputation among peers, authorities and regulators



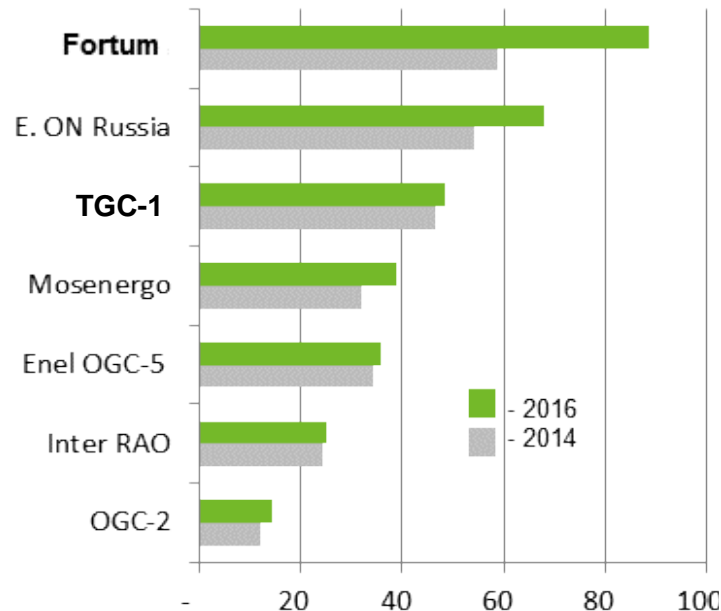
Fortum Russia is the one of most efficient company in Russian power sector

Russian utilities in 2013
(Net profit*/Installed capacity (kEUR/MWe))



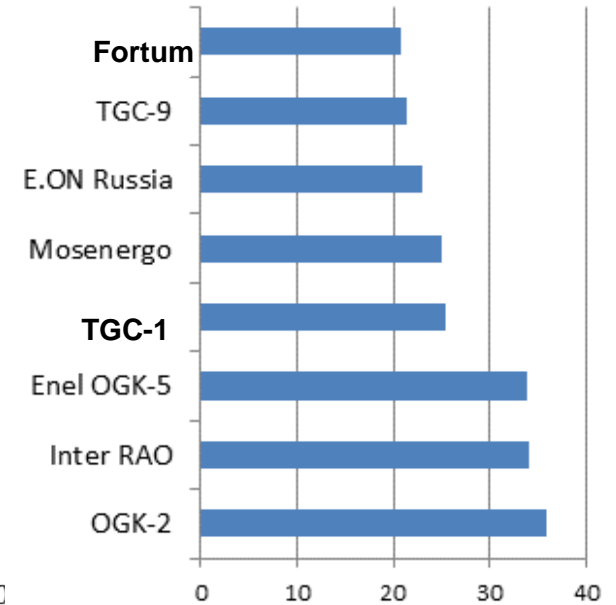
* According to Russian accounting system

Russian utilities consensus forecast
(EBITDA/Installed capacity (kEUR/MWe)**)



** Source: Bloomberg

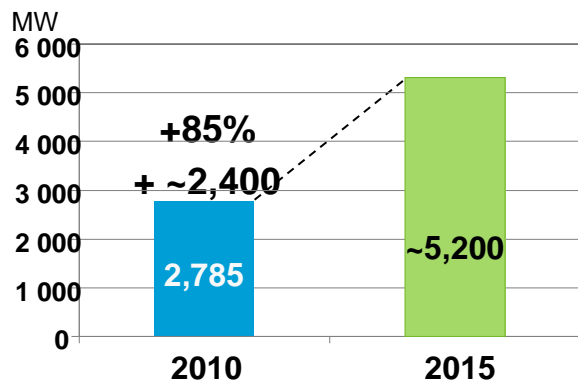
Production costs of generating companies in 2013*, EUR/MWh**



*** Whole costs of the company divided by the total energy output (electricity and heat). Based on Market Council data.

Extensive investment programme in OAO Fortum: Investment programme nearly finished – 2 units still to be commissioned

- Total amount of investments EUR 2.5 billion
 - Of which approximately EUR 0.3 billion still to be invested as of September 2014
- Increasing capacity by ~ 85% by the end of 2015
 - More than any other Russian generating company
- Five new units in commercial operation
- Nyagan 3 was commissioned in October 2014 and starts commercial operations in January 2015
- Two new units in Chelyabinsk during H1/2015

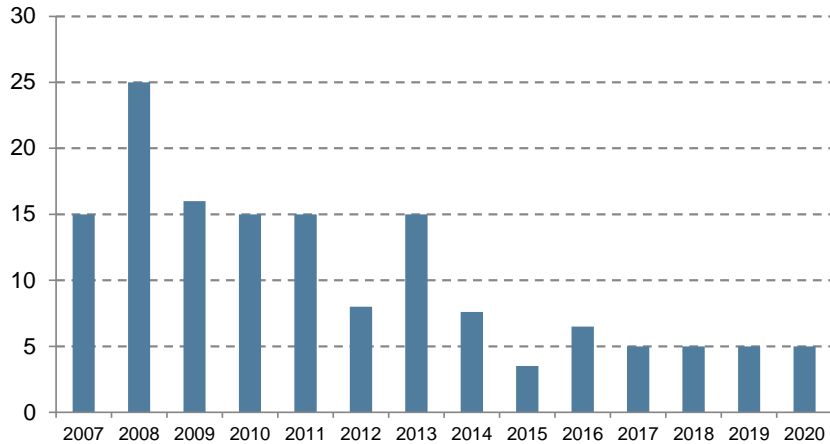


Six units commissioned

Commissioning Date	Unit Name	Capacity (MW)
Mar / Dec 2013	Nyagan 1 + 2 + 3	420 + 424 + 422 MW
Feb 2011	Tyumen	209 MW
Jun 2011	Chelyabinsk	216 MW
Oct 2011	Tobolsk	213 MW

Gas price growth and significant share of old assets create opportunity for efficient generators

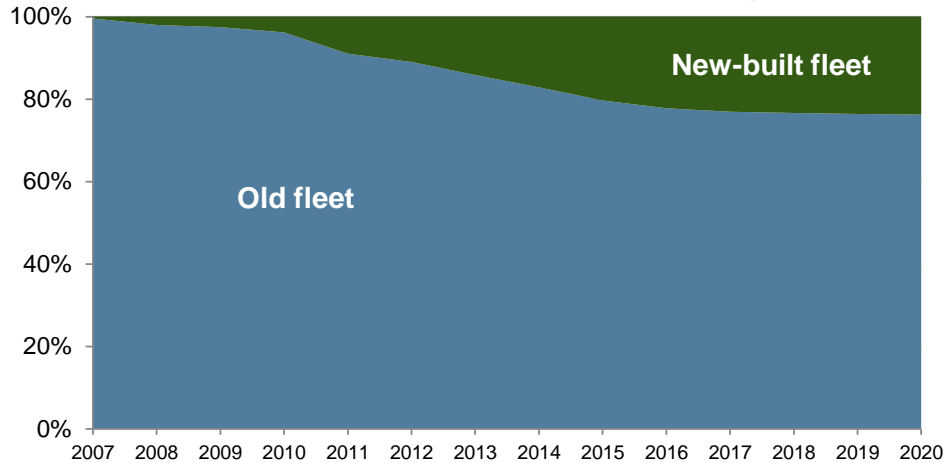
Gas price growth official forecast , %



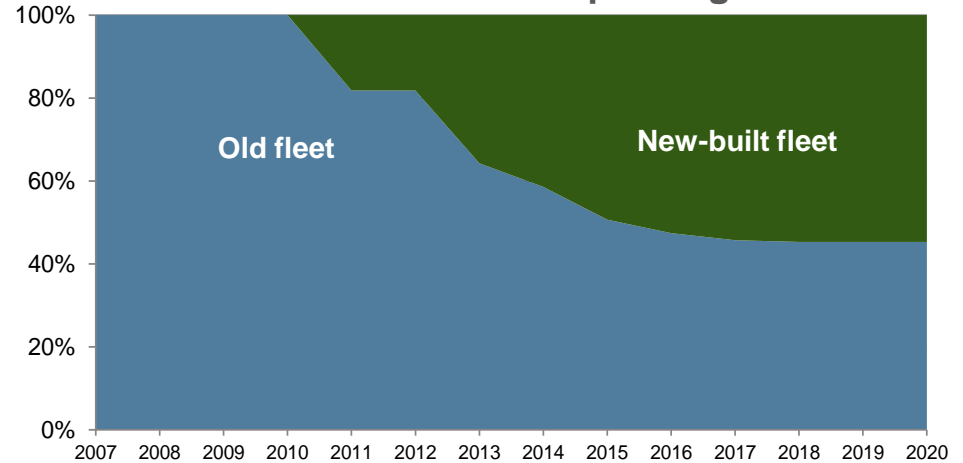
Source: Ministry of economy development

- Gas price growth was decreased significantly compare to the previous period, but won't be lower than inflation rate
- The share of inefficient old generators will stay significant until 2020. Thus the marginal electricity prices will remain on the high level
- The spark-spreads are lucrative for the efficient generators, especially for the CCGT (combined-cycle gas turbine) technology in combined mode

Market* ratio of new&old thermal power generation

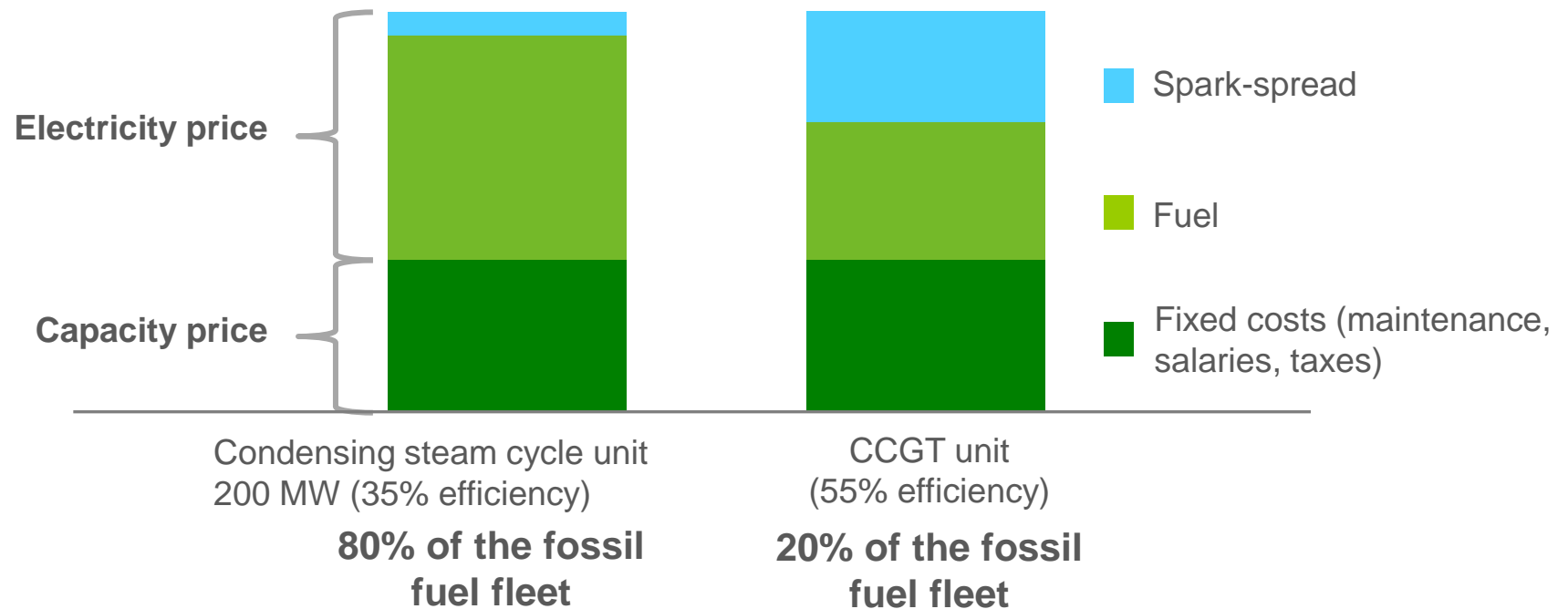


Fortum's ratio of new&old power generation



* For the First price zone

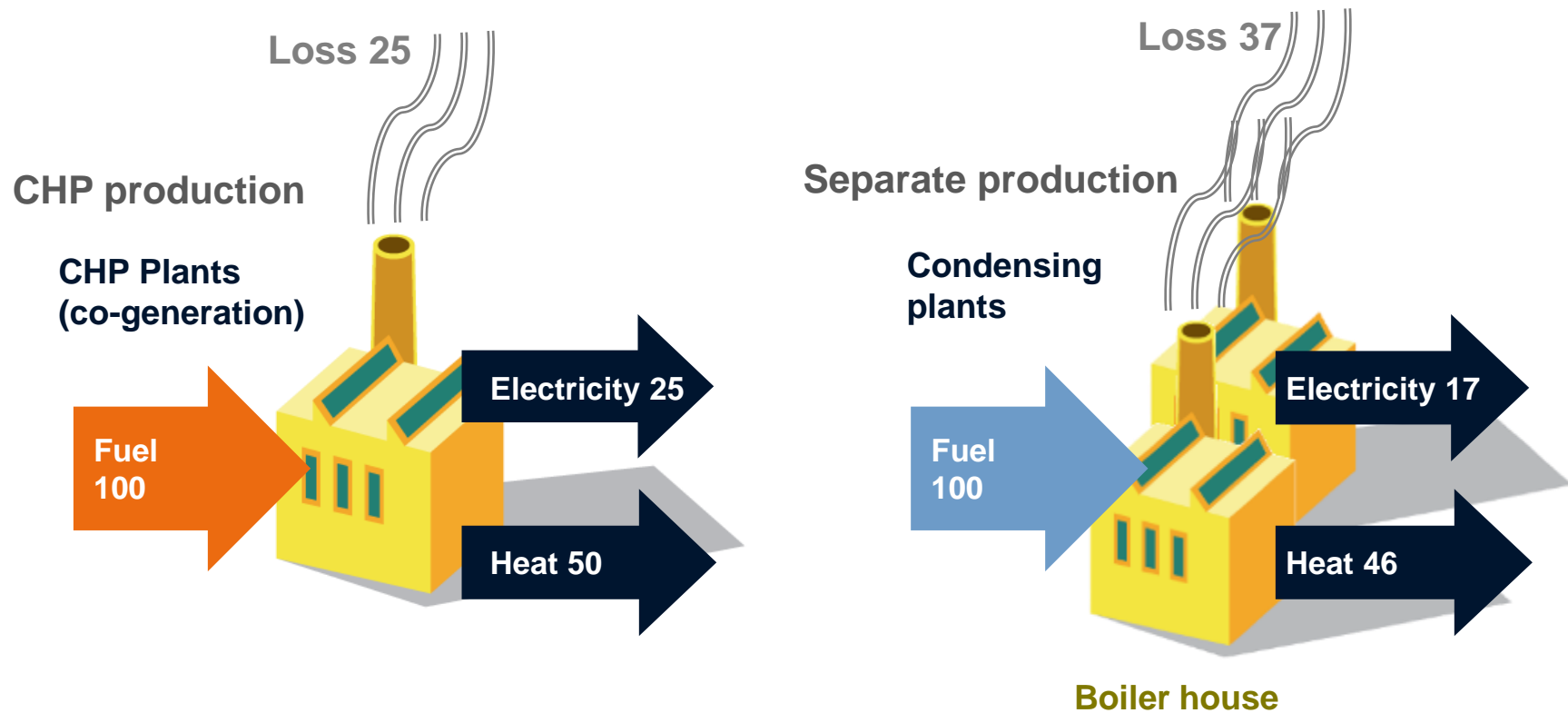
Fortum invests in the most efficient CCGT generation in Russia, using fuels more efficiently and providing additional margin for new capacity



- Major part of power plants in Russia are very obsolete and inefficient. Average efficiency of the thermal power plants is about 37%
- Investor, which builds the new efficient equipment has a better margin than the owner of the old plants

Fortum invests in efficient CHP, with clear advantages compared to condensing power production

Combined heat and power production is much more efficient than separate production



Update on Russian heat market reform

Basic principles of the proposed new heat market model

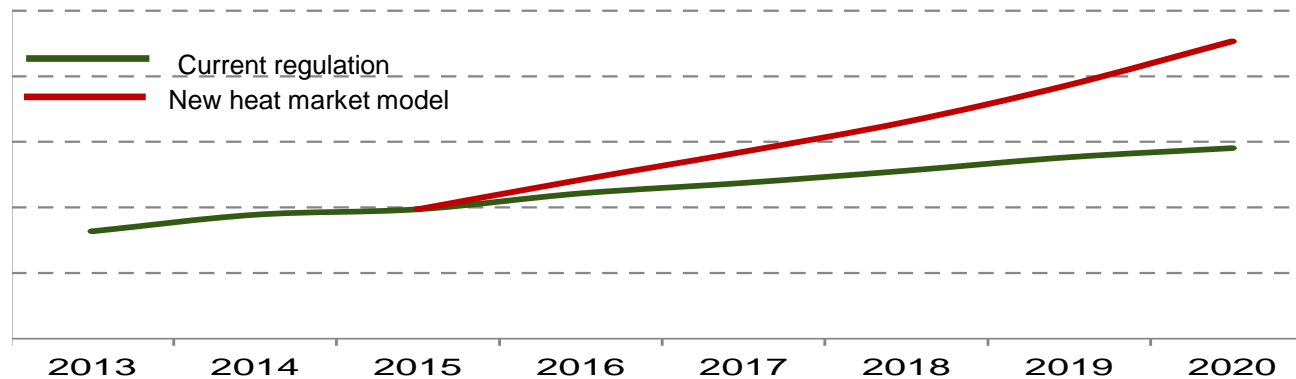
- The price-cap is to be set up at the level of the “alternative heat-only boiler”
- The heat tariffs are to be gradually transitioned to reach “alternative HOB” level within 5-8 years
- Full liberalization within the price cap at the level of “alternative HOB” of the heat prices takes place after the transitional period

Current status and further actions

- Basic principles were adopted by V. Putin in April 2014
- Heat Roadmap was signed by D. Medvedev in October 2014. The Roadmap implies price liberalization from 2020/2023
- The new regulation is to be effective from 2016

<http://publication.pravo.gov.ru/Document/View/0001201410070001?index=0&rangeSize=1>

CHP heat tariff of Fortum



Update on the Russian electricity and capacity market

Negative effects...

- **Russian GDP growth slows down** (0-0.5% in 2014 and 0.5-1.5% in 2015)
- Electricity demand for 2014 and 2015 to be decreased as well, consequently lower electricity spot prices. **Weakening exchange rate** (to RUB/EUR~50 in 2015)
- **Accelerated inflation** (to 8% in 2015)

... and positive effects which mitigate impacts

- **Growth of bond yields** which directly effect the Capacity supply agreements (CSA) rate of return*
- **Inflation growth** - compensation through the tariffs decisions (e.g. regulated sector, gas, heat)

Yield of 10-years bonds, %



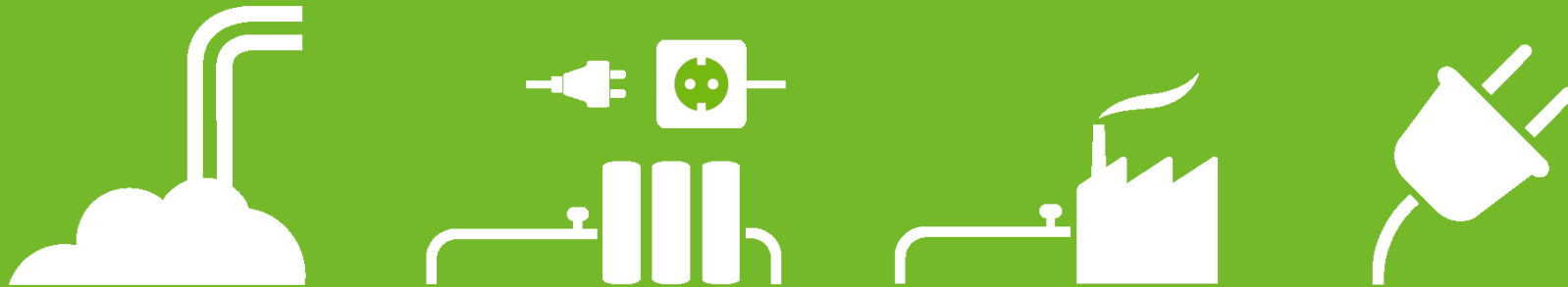
Exchange rate RUB/EUR



* According to methodology of CSA pricing, 1% growth of yield bonds increases the capacity price by 6% in average

Summary

- CSA- related Investment programme to be concluded in 2015 (2x250 MW CHP units)
- Nyagan 3 - CSA payments start as of Jan 1, 2015 (1 year ahead of the actual CSA Date)
- Efficient assets provides competitive advantages
- Capacity modernization program continues
- The financial target RUB 18.2 billion run-rate is to be reached during 2015
- Heat reform is potential upside



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