SURINAME

Corporate Financial Assessment of EBS

The objective of the report is to update the financial capacity assessment of EBS, its corporate financial information and reporting practices; the level of financial support from the government and the mechanisms to implement such support.

**Executive Summary**

The Financial Statements analysis of N.V. Energiebedrijven Suriname (EBS) electricity and gas company has been updated, up to December 31, 2013, as compared to December 31, 2012, 2011, 2010, and 2009[[1]](#footnote-1).

After including the new financial analysis information for the company, it can be concluded that the current financial situation is similar to that of previous years, as reflected in the following paragraph taken from prior reports:

**“The EBS financial situation maintains a delicate balance through various Government subsidies.”**

Nonetheless, it bears noting that in 2012, the government hired the consulting firm KPMG to analyze and report on various public companies, including EBS. Based on the firm’s results and recommendations, EBS developed a plan to adapt and improve its administrative, operational, and financial efficiency. This plan is currently being implemented, with measures to enhance the administrative structure, adjust administrative and operational processes, restructure long-term liabilities, adjust rates, etc.

As the plan has been in implementation phase for such a short period of time, the results have not yet been reflected in its financial statements. However, based on the rate adjustment announced by the government this year of US$0.07 for low-income users and US$0.26 for large consumers like casinos, hotels, shopping centers, large companies, etc., the improvement will be noticeable.

Based on the foregoing, it has been deemed most appropriate to begin the analysis with the impact government subsidies have on financial statements and, especially, financial indicators.

To streamline the terminology in the paper, direct subsidies are defined as those that stem from laws, decrees, or agreements between EBS and the government, such as the D.E.-Sector and fuel oil subsidies. Indirect subsidies are defined as payments made by the government to cover debts, materials, or services that EBS must pay, such as the repayment of loans taken out to conduct investment projects.

**Direct Subsidies for Electricity[[2]](#footnote-2).**

The direct subsidies paid out by the government had the largest impact on the EBS income statement[[3]](#footnote-3).

The table below shows the change in sales between 2009 and 2013.

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| (In thousands of SRD) | 2013 | | 2012 | | 2011 | | 2010 | | 2009 | |
|  | Quantity | SRD | Quantity | SRD | Quantity | SRD | Quantity | SRD | Quantity | SRD |
| Electricity sales (MWh) | 1,398,398 | 334,045 | 1,325,661 | 325,003 | 1,232,700 | 299,500 | 1,164,925 | 257,968 | 1,076,687 | 226,176 |
| Gas sales (X 1000 lbs) | 63,784 | 58,884 | 3,556 | 58,254 | 33,750 | 54,506 | 32,527 | 46,432 | 31,446 | 44,582 |
|  |  | 392,929 |  | 383,257 |  | 354,006 |  | 304,400 |  | 270,758 |
| Other proceeds |  |  |  |  |  |  |  | 62,918 |  | 44,411 |
|  |  | 392,929 |  | 383,257 |  | 354,006 |  | 367,318 |  | 315,169 |

As seen above, there is a significant yearly percentage increase in the volume of electricity sales in terms of quantity and revenue, which leads to the company’s improved financial outlook. But the reality is that these increases also required substantial subsidy increases, due to low electricity and gas rates.

The table below shows the variation of the percentage growth in sales, by volume and revenue:

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Increase in Sales %** | **2012-2013** | **2011-2012** | **2010-2011** | **2009-2010** |
| **Quantity** | 5.49% | 7.54% | 5.82% | 8.20% |
| **SRD** | 2.78% | 8.52% | 16.10% | 14.06% |

Growth was sustained for both volume and revenue: electricity sales rose 5.49% in 2013, resulting in a 2.78% increase in revenue.

When the behavior of direct subsidies is analyzed over this same 2012-2013 period, it can be seen that they surged 38.59%. Therefore, although on the surface, EBS’s financial situation appears to have improved due to increased sales, the government actually had to significantly boost its share through subsidies to preserve the company’s equilibrium.

The following tables show the figures and percentages for the abovementioned subsidies.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Total Subsidy | 2013 | 2012 | 2011 | 2010 | 2009 |
|  | **474,362** | **342,266** | **213,773** | **174,491** | **82,238** |

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | 2012-2013 | 2011-2012 | 2010-2011 | 2009-2010 |
| Subsidy Increase % | **38.59%** | **60.11%** | **22.51%** | **112.18%** |

As noted, this situation arises from the low average sales price of energy, compounded by the elevated use of thermal power plants to generate power, whose cost is directly influenced by oil prices. The significant fluctuations in generating costs are not offset by higher sales; on the contrary, they heighten the need to use subsidies to close the gap created by greater demand, as rates are not adjusted according to cost variations.

It is important to point out that, since 2013, the oil company of Suriname (Staatsolie) is expanding its refinery, which is expected to double the capacity to 15,000 barrels per day. The expansion has contributed to the increase of capital goods and service imports, and it has brought Suriname to a negative situation in the international position, despite of Suriname being an oil producer country.

Suriname has been deemed eligible for access and is a participant of the PetroCaribe agreement, but in any case PetroCaribe is not reflected in the public financial statements of the country. The country has recently entered into the PetroCaribe agreement and had been finalising its implementation arrangements even up until 2013. As of the end of 2013, the authorities were finalizing a mechanism for the implementation of a PetroCaribe arrangement, but it has not yet been used. As a result, there is no related documented PetroCaribe debt, interest payments, or projected disbursements that would imply any fiscal tightening for the central government. This information is confirmed by the databases of the Central Bank of Suriname, Annual Financial Notes from the Ministry of Finance, and IMF.

If the projected finishing date for the refinery works is accomplished and the execution of the agreement with Petrocaribe starts, it could reduce the oil prices for EBS in the future, thus also decreasing the use of direct subsidies.

Based on the foregoing and the information in the adjusted income statements provided in the Annexes, the following analysis was performed.

**Search for the financial and operating breakeven points**

If it is established that these subsidies substitute higher revenue for sales, because rates are low, it can be seen that EBS’s total revenue would be SRD 876.29 million and SRD 725.52 million for 2013 and 2012, respectively, with the share of the subsidies accounting for 55% of 2013 total revenue and 47% of 2012 total revenue. The following table shows the algorithms used.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Electricity Operations | 2013 | 2012 | 2011 | 2010 |
| (In thousands of SRD) | **SRD** | **SRD** | **SRD** | **SRD** |
| Sales | **392,929** | **383,257** | **299,485** | **257,968** |
| Government contribution, D.E.-Operations |  |  | **103,606** | **90,171** |
| Fuel Subsidy |  |  | **110,167** | **84,320** |
| Total Subsidy | **474,362** | **342,266** | **213,773** | **174,491** |
| Sales + Total Subsidy | **867,291** | **725,523** | **513,258** | **432,459** |
| % Sales | **45%** | **53%** | **58%** | **60%** |
| % Subsidy | **55%** | **47%** | **42%** | **40%** |

If the financial and operating breakeven points are to be maintained without government subsidies, this subsidies revenue must be obtained through sales revenue. To this end, the income statements have been modified by eliminating the subsidies and amortization and the new sales revenue has been calculated to obtain a neutral or zero outcome[[4]](#footnote-4).

By applying this criterion, it is concluded that for 2010, 2011, 2012, and 2013, the rates would have had to have increased 98%, 66.22%, 130%, and 151%, respectively.

The table below shows these algorithms, with figures on the sales revenue that would have been necessary to preserve the financial and operating breakeven points (without investments) and the respective percentages for actual sales revenue.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | 2013 | 2012 | 2011 | 2010 |
| (In thousands of SRD) | **SRD** | **SRD** | **SRD** | **SRD** |
| Sales, no subsidy | 841,451 | 747,290 | 497,811 | 512,691 |
| Sales, with subsidy | 334,045 | 325,003 | 299,485 | 257,968 |
|  | 151% | 130% | 66.22% | 98% |

Based on this, it can be deduced that, if the average rate per kW is approximately 7.3 US cents, it should be adjusted upward to at least 18.5 US cents. If a 10% rate of return is added, the rate would need to be set at around 20 US cents.

It bears noting that the previous analysis determined a financial and operating breakeven rate that did not include hedging investments.

**Indirect Subsidies**

The main indirect subsidies EBS receives stem from loans the government takes out and repays, and which are used for company investment projects.

This situation is not reflected in the income statement, rather in EBS current and non-current liabilities, as each new payment made by the government increases EBS debt.

Below is a list of government loans, according to Note 12 of the financial statements for the fiscal year ending December 31, 2013:

|  |  |  |
| --- | --- | --- |
| Government Loans | 2013 | 2012 |
| 2004 Loan for generators (USD 13.7 million) | 45,965 | 45,965 |
| 2005 Loan for 161kV transmission lines (USD 12.9 million) | 43,403 | 43,403 |
| 2007 Loan for distribution materials (€4.8 million) | 21,140 | 21,140 |
| 2008 Loan for distribution materials (€7.5 million) | 33,120 | 33,120 |
| 2012 Loan for repaying RBC Royal Bank loan  (USD 14.2 million) | 47,515 | 47,515 |
| 2012 Loan (USD 46.4 million) | 155,561 | - |
| 2013 Loan for generators and power (SRD 64.6 million) | 48,473 | - |
| Total | **397,646** | **191,143** |
|  |  |  |
| Government loans, Classification |  |  |
| Short term | 7,778 |  |
| Long term | 389,868 | 191,143 |
| Total | **397,646** | **191,143** |

Past loans are not repaid.

Interest to be paid is included in current liabilities.

In 2012, the RBC Royal Bank loan was paid by the government on behalf of EBS.

At the time of the financial statement preparation, the terms of the loans had still not been agreed.

The interest rate is estimated at 6%.

On December 6, 2012, the Ministry of Finance took out a USD 46.4 million loan (completed in 2013), with a two-year grace period, later extended to 10 years, starting November 30, 2014. This loan is earmarked for financing the power plant construction.

On March 6, 2013, the Ministry of Finance took out a SRD 64,631,145 loan to finance the purchase of three generators and additional work related to the power plant construction. The grace period was set at two years, after which the loan term was set at 15 years, starting April 30, 2015.

Currently, all new EBS investment projects must be financed through such mechanisms, in which the government is responsible for directly repaying the loans used for financing investments. The reason for this is that rates do not cover operating costs, let alone investment costs.

Furthermore, the way this mechanism calls for financial statements to present their items, and therefore their indicators, is not recommendable. For example, equity capital is negative and, at a glance, the company is being financed through long-term liabilities. While this is true, any analyst would think that this is through suppliers or other mechanisms common in the course of business. But in this case, the liabilities reflect debt held with the government for the non-fixed term loans they directly repay.

This has been compounded by the fact that fixed assets have not been revaluated since 1994, to avoid higher depreciation in the financial statements, thereby increasing losses recorded over the years. Consequently, equity is also undervalued.

**Conclusion:**

EBS maintains a delicate balance in its financial situation, preserved through the use of various types of Government subsidies. This situation can be maintained over time, propped up by fiscal resources, as has been the case to date.

Nonetheless, it bears noting that in 2012, the government hired the consulting firm KPMG to analyze and report on various public companies, including EBS. Based on the firm’s results and recommendations, EBS developed a plan to adapt and improve its administrative, operational, and financial efficiency. This plan is currently being implemented, with measures to enhance the administrative structure, adjust administrative and operational processes, restructure long-term liabilities, adjust rates, etc.

As the plan has been in implementation phase for such a short period of time, the results have not yet been reflected in its financial statements. However, based on the rate adjustment announced by the government this year of US$0.07 for low-income users and US$0.26 for large consumers like casinos, hotels, shopping centers, large companies, etc., the improvement will be noticeable.

1. Financial Statements audited up to December 31, 2013, 2012, 2011, 2010 and 2009. [↑](#footnote-ref-1)
2. The financial analysis has focused on the impact that subsidies have on EBS on electricity, as it has a much larger impact on results than gas subsidies. [↑](#footnote-ref-2)
3. For a clearer understanding of the outlook, a new Income Statement has been developed, adjusting for the following items:

   1. Operating income, taking into account direct government subsidies.
   2. The price of fuel oil has been adjusted and presented it as the cost value, deducting the subsidy received.
   3. The amount resulting from adjusted liabilities (due to the extraordinary update of the Pension Fund) was deducted from personnel expenses and presented as extraordinary expenses.
   4. The resulting adjustment of the revalued foreign-currency denominated liabilities was deducted from the financial costs item and presented as extraordinary losses.
   5. Depreciation of assets is presented separately to get the EBITDA and EBIT indexes.

   [↑](#footnote-ref-3)
4. ANNEX Income Statement for the Operating Breakeven Point. [↑](#footnote-ref-4)