

14 July 2016

## ACTIVITY UPDATE

Dear Shareholder

### Introduction

Following completion of the 2016 financial year and ahead of the release of Pacific Energy's financial results, I am pleased to provide you with an update on the Company's activities. There has been a lot happening and in this update I discuss our performance in fiscal year 2016 ("FY16"), growth initiatives, the outlook for fiscal year 2017 ("FY17") and the state of our financial health.

### FY16 Performance

I am pleased to report that Pacific Energy has had an excellent year on the back of solid capital investment into the business and much hard work in the field.

During the year we upgraded our forecast Earnings Before Interest Tax and Depreciation ("EBITDA") to \$35 million. This expectation highlights Pacific Energy as a stand out performer in its sector at a time when many companies are experiencing deteriorating financial performance and an uncertain future. It also demonstrates the resilience of the business and the dependability of our earnings, underpinned by:

- annuity style income;
- long term contracted revenues;
- take or pay structure of electricity supply contracts;
- ongoing reliance on power by producing mines; and
- stable and diversified customer base.

During the year our KPS subsidiary secured several new power station contracts, as well as contract renewals and expansions at existing sites.

The majority of work on new and expanded power stations was conducted and completed in the second half and contributed to increasing results during the period. In the new financial year, the full year earnings impact from these newly commissioned projects will flow through to our earnings and as a result we expect further growth to be recorded in FY17.

We are most fortunate to have a highly talented and dedicated team of professionals who have worked exceptionally hard to meet the demands of these new installations, as well as maintaining our existing power stations to a benchmark standard.

It is important for Shareholders to appreciate that the work performed in the field is often conducted in very harsh climatic conditions, with long hours and family absences also involved. The dedication of our team to deliver a first class result for our customers in tight time frames is exceptional in this regard.

It is also pleasing to know that our staff participate in the Company's employee share scheme and therefore receive additional reward for their efforts through increased equity ownership in Pacific Energy.

## **Cash Flow and Capex**

Pacific Energy's operating cash flow (before capex) has consistently been above \$20m in recent years. Continuing the theme of reliability, in FY16 we expect to report another solid full year of operating cash flow.

The growth path put in place during the year did require significant investment in new assets and refurbishments of existing assets, as well as new supporting plant and equipment. This led to a high level of capital expenditure ("capex") for the year, which we expect to report at around \$35 million. Of course the benefits from this capex will be realised over the duration of the underlying contracts.

## **Outlook and Growth Initiatives**

As mentioned above, the full year benefit from work performed in FY16 will flow through to FY17 and subsequent years under the multi-year contracts we have in place. As a result, we expect to see another record year in FY17 and we are focussed on having annual EBITDA exceed the \$40 million level for the first time in the Company's history.

We are also busy tendering various projects and submitting proposals and expressions of interest on others. Whilst it is fair to say that there is not as much potential new work around as there has been in previous years, the level of enquiry still remains healthy and we are hopeful of securing further contracts during the course of the year.

### *Solar Alliance*

One of the Company's existing customers, Sandfire Resources Ltd, announced in June the successful completion of a \$40m solar power project at its DeGrussa mine site in Western Australia.

The 10.8MW solar facility, which includes 6MW of lithium-ion battery storage and covers an area of 20 hectares, has been fully integrated with KPS's 19 MW diesel station - which continues to generate and distribute baseload power to the site. The result is the largest hybrid power facility in Australia and reportedly one of the largest in the world.

KPS played a key role in the success of this project, which required working closely with the solar developer, juwi Renewable Energy ("juwi"), to integrate the solar facility with KPS's power station utilising sophisticated control systems.

Following from the success of this innovative project and after working closely with juwi for over nine months, KPS and juwi have recently entered into a formal strategic alliance (the "Alliance").

The Alliance will focus on off-grid projects where customers wish to supplement baseload diesel or gas fuelled power with integrated solar and battery power, bringing together the capabilities, technology and resources of two market leaders in their respective fields – KPS in thermal power and juwi in solar power.

German based juwi Group is one of the world's leading renewable energy companies and the alliance with them provides KPS with access to solar and battery storage capabilities. The two companies have successfully developed the know-how behind integrating and operating a large hybrid system in the challenging and changing conditions encountered in mine site environments.

Whilst thermal power stations of the kind operated by KPS continue to provide baseload power to mines, having capabilities in off-grid hybrid power at a time when there is an increasing global focus on renewable energy is an important value-add for the Company.

### *Africa*

Last month we announced the incorporation of a subsidiary company in the Republic of South Africa and the appointment of an experienced executive to focus on remote power opportunities on the African continent.

Africa produces more than 60 metal and mineral products and has over 30% of the world's total known mineral reserves. With many mining regions being without access to grid power due to their remote locations, and those that are connected to the grid often not having reliability, we believe there is a sound opportunity to introduce the KPS style of business.

There are approximately 190 ASX listed companies with almost 600 mining projects across 38 countries in Africa. There are also a large number of projects owned by Canadian, UK, South African and multinational companies.

These factors, together with KPS's proven and successful remote power capabilities are indicative of the potential for the Company to build a sizeable portfolio of power generating assets in Africa in the years to come and make a significant contribution to the earnings of the group.

Of interest to Shareholders is that we are already working on an opportunity where the customer is particularly interested in a hybrid solution for their new mining operation and KPS and juwi are currently in discussions to progress this.

### *Other Strategic Pursuits*

With our three subsidiary businesses in place – Pacific Energy Hydro, KPS Australia and KPS Africa – we will pursue organic growth opportunities as well as acquisition opportunities that fit strategically with each operation.

A key theme for Pacific Energy is growth in recurring revenue from energy related assets. In addition to operating the above three businesses, we are focussed on identifying investment and acquisition opportunities that fit with this theme. Several such opportunities have been pursued over the past year, however, to date none have reached the stage where a transaction has been recommended.

A number of new opportunities are currently under review and Shareholders will be advised if anything materialises.

### **Financial Health**

Looking at our balance sheet, we have seen gearing levels move up in line with the large capex required for the new projects in FY16, however, the Company's gearing level nevertheless remains conservative. This is especially so given the long term nature of our contracts and the financially strong client base who are counterparties to those contracts.

The Company's balance sheet is able to support further growth with these conservative gearing levels and we also have considerable headroom within our banking facilities.

## **Dividends**

Despite the well-publicised mining downturn, Pacific Energy has maintained payment of an annual 2.5 cent per share fully franked dividend from its stable earnings base. Our objective is to maintain a steady and reliable dividend stream for Shareholders in addition to providing capital growth prospects as we build our portfolio of long term income generating assets.

## **In Closing**

The Company has proven to be a dependable performer in recent years and should report an excellent result for FY16, underpinned by some outstanding work in the field by our talented and dedicated staff. This will extend to stronger results in FY17 and beyond, subject to retaining existing customers and securing contract renewals.

We have commenced some new initiatives and continue to review acquisition and investment opportunities to build the Company's scale and profitability.

As we develop these initiatives it is important that we remain in good financial health and are able to capitalise on opportunities that arise. With solid operating cash flows, reliable long-term income streams and a healthy balance sheet we certainly are in a strong position and are able to properly maintain our business whilst at the same time pursue growth opportunities.

I look forward to finalising our FY16 results and reporting back to Shareholders more fully in our Annual Report.

Yours sincerely,



Jamie Cullen  
Managing Director