

NO. 13-434/11.04.2019

TO,

**SNGN ROMGAZ SA MEDIAS
GENERAL MEETING OF SHAREHOLDERS**

**SUBSTANTIATION NOTE
OF THE
INDIVIDUAL INCOME AND EXPENDITURE BUDGET FOR 2019**

I. Substantiation of the 2019 Income and Expenditure Budget draft and of the 2020 - 2021 forecast was based on the laws concerning:

- ~ implementation of International Financial Reporting Standards by the companies whose securities are traded on a regulated market;
- ~ strengthening of the financial discipline and establishing the expenses for salaries and wages in the 2019 budget, at the level of economic operators where the state or administrative territorial units are sole or majority shareholders or hold directly or indirectly a majority participation;
- ~ profit distribution by the national companies and trade companies fully or majority state owned, as subsequently amended and supplemented;
- ~ implementation of the Fiscal Code;
- ~ layout and structure of the income and expenditure budget, as well as its related substantiation annexes;
- ~ setting up fiscal-budgetary measures, amendment and supplementation of certain laws and extension of terms.

II. The assumptions for drafting the income and expenditure budget proposal comply with "The Projection of the Main Macroeconomic Indicators 2018-2022" - the Winter Forecast - 2019, published by the National Prognosis Commission, are as follows:

	2019	2020	2021
Index of consumption prices - annual average	2.8%	2.6%	2.4%
Exchange rate RON/Euro - annual average	4.67	4.62	4.60
Exchange rate RON/USD - annual average	4.03	3.98	3.97

**) according to the National Strategy and Prognosis Commission "The Projection of the Main Macroeconomic Indicators 2018-2022" - the Winter Forecast - 2019*

III. Outline and substantiation of the indicators included in Romgaz 2019 Income and Expenditure Budget draft

1. Substantiation of Income

The substantiation of the main income categories of the income and expenditure budget is based on the forecasted evolutions of the gas demand and delivery price, the production programs, storage program of own gas, import gas acquisition and delivery. The gas delivery price is limited between May 1, 2019 – February 28, 2022 for "the gas quantities used to cover the consumption of households and thermal energy producers, only for the gas quantity used to produce thermal energy in cogeneration plants and in thermal power plants for the consumption of the population" according to GEO no. 19/2019, that amends and supplements GEO no.114/2018.

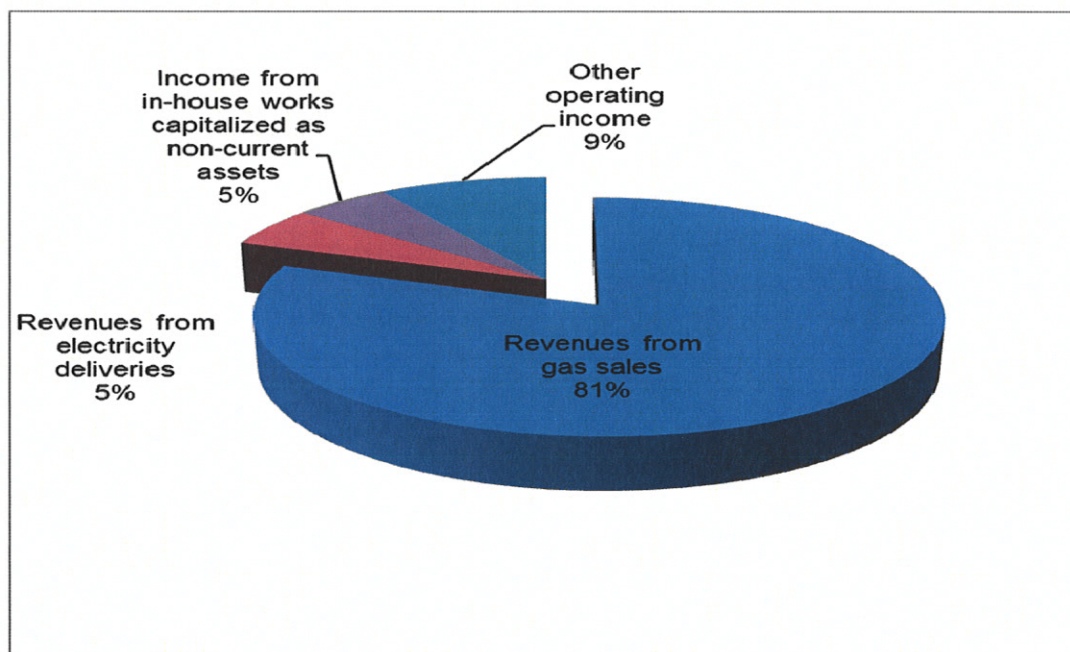
Revenues of the Electricity Production Branch (SPEE Iernut) are generated from the electricity production and delivery as well as from other field related services.

Besides the main revenue categories, revenue is also recorded from other activities such as: service provision for third parties (transportation, gas dehydration and compression, rental of goods, chemical analyses, sale of condensate, and sale of goods).

Operating Income

Operating income is estimated to be **RON 5,002,165 thousand**.

The structure of operating income for 2019 is shown in the figure below:



Operating income is detailed in the table below:

Item no.	RON thousand	Achieved 2018	Proposal 2019	Ratio 2019/2018 %
1	Revenues from Romgaz gas sales delivered from own production (excluding joint ventures, and gas for electricity production)	3 852 335	3 861 722	100.24%
2	Revenues from joint ventures	132 607	94 226	71.06%
3	Revenues from import gas deliveries	205 912	69 649	33.82%
4	Revenues from electricity deliveries	288 341	270 717	93.89%
5	Revenues from storage services*)	115 328		0.00%
6	Income from in-house works capitalized as non-current assets	208 507	258 232	123.85%
7	Other income from sold production (transmission, distribution, storage, subsidiary rent, goods and variation)	362 365	447 619	123.52%
	Total operating income	5 165 406	5 002 165	96.84%

*) in Q1 2018 revenues from natural gas storage activities include the revenues from the storage activity taken over as of April 1, 2018 by the subsidiary

Revenues from Romgaz gas delivered from own production (excluding gas from joint ventures and gas for electricity production) were determined based on the gas quantities estimated to be delivered to clients in 2019 and on the average delivery price of gas from current production and withdrawn from UGSs; taking into account the effective laws on gas delivery prices, namely GEO no.114/2018, amended and supplemented by GEO no.19/2019.

Revenues from joint ventures represent the value of natural gas delivered under joint-ventures and which correspond to Romgaz participating interest.

Revenues from import gas deliveries represent the value of natural gas purchased from import and resold by Romgaz to clients.

Revenues from delivered electricity were determined based on the quantities of delivered electricity and on the estimated average delivery prices.

Revenues from underground gas storage services are generated from services supplied for gas injection and withdrawal into/from UGSs and for capacity booking and changes in inventories.

Income from in-house works capitalized as non-current assets represents the value of works performed in-house.

Other income represents income from gas distribution, rentals, condensate deliveries, transmission and storage services (can be found also at expenses).

Financial income of **RON 21.289 thousand** is generated by the interest received from banks for the company's cash placed in bank deposits and state bonds.

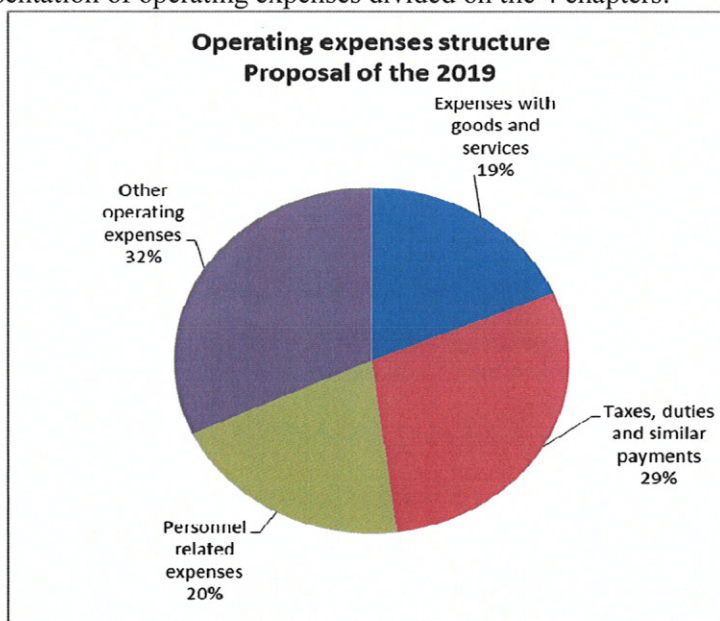
2. Substantiation of expenditures

Operating expenses are classified in the following main chapters:

- A. Expenses with goods and services;
- B. Expenses with taxes, duties and similar payments;
- C. Personnel related expenses;
- D. Other operating expenses.

RON thousand	Achieved 2018	Proposals 2019	Ratios (%)
	2	3	4=3/2
A. Expenses with goods and services, out of which:	858 882	719 843	83.81%
A1.Expenses with inventories	435 003	320 222	73.61%
A2.Expenses with services supplied by third parties	22 512	25 300	112.38%
A3.Expenses with other services supplied by third parties	401 366	374 321	93.26%
B Expenses with taxes, duties and similar payments	995 540	1 133 393	113.85%
C. Personnel related expenses	696 133	778 163	111.78%
D. Other operating expenses	1 017 314	1 235 564	121.45%
Total Operating Expenses	3 567 870	3 866 963	108.38%

Graphic representation of operating expenses divided on the 4 chapters:



A. Expenses for Goods and Services:

For this expense category (A) of RON 719,843 thousand we estimate a decrease of 16.2% as compared to the expenses of 2018, mainly influenced by the decrease of import gas quantities purchased for resale estimated for 2019.

Expenses for materials, spare parts, fuel, inventory as well as services for maintenance and repairs, services provided by third parties are mainly generated by the increase of the scheduled work volume such like in-house works capitalised as non-current assets, maintenance and repair works, renew work and protection equipment. Actions, activities, operations that were not fulfilled in 2018 in this chapter, influenced the increases forecasted in 2019 due to the necessity to fulfil these for performing the current activities of the company.

The increase of the gross gas production in 2019 as compared to 2018 (by 0.3%) reflects the efforts undertaken by the company to mitigate the natural decline of the gross physical production and this generates increased consumption of materials, spare parts, technological consumption, inventories and fuel consumption.

A large share of the expenses with goods and services is represented by pipes, tubing, christmas trees for the gas wells, foam agent, cement, spare parts for maintenance of compression and dehydration stations.

Expenses with services performed by third parties will increase by 12.4% compared to 2018 and are forecasted at the level for necessary continuing activities under safety conditions. The largest share is allocated to expenses for maintenance and repairs of the equipment specific for the gas production activity. These expenses include recompletion operations, buildings, constructions, equipment, compressor manifold, total or partial replacement of elements or parts thereof.

Expenses with other services supplied by third parties consist of expenses with partners, commissions, fees, legal services, protocol, advertisement and publicity, sponsorship, transportation, employee transportation and relocation, security, organization restructure design, employee training and record a slight decrease as compared to the previous year (6.7%).

B. Expenses for Taxes, Duties and Similar Payments

These expenses include royalty calculated as percentage from the physical production, from condensate (RON 489.5 million), windfall tax (RON 557.9 million), 2% contribution according to GEO no. 114/2018 (RON 77.2 million) as well as land and building taxes, total permitting, licencing and environment taxes (RON 8.8 million).

C. Personnel-related Expenses:

Personnel-related expenses were estimated based on:

~ **Government Emergency Ordinance no. 26/2013** on strengthening the financial discipline at the level of economic operators where the state or administrative territorial units are sole or majority shareholders or hold, directly or indirectly, a majority share, as subsequently amended and supplemented;

~ **Law no. 227/2015** - Fiscal Code as subsequently amended and supplemented;

~ **Law no. 50/15.03.2019** on the State Budget for year 2019;

~ **Labour Code;**

~ **Collective Labour Agreement.**

Law no. 50/2019 of the State Budget for 2019 provides at Chapter III “Final Dispositions” art. 62, para (1)-(6) the government’s policy coordinates on the salary policy for 2019.

The provisions on applying the index of growth in labour productivity, on the increase of salaries related expenses apply to the operators that “exceeded the level of overdue payments planned for the end of 2018”, pursuant to letter a) paragraph (1) of Article 62; these provisions do not apply to SNGN Romgaz SA.

The State Budget Law for 2019 does not include limitations as regards the increase of salaries related expenses for the operators that do not record overdue payments.

The fact that in 2019 the provisions of the state budget law are not applied when preparing the personnel related expenses is an opportunity to analyse the possibility to increase salaries in order to incentivize and to maintain the professional employees.

Personnel related expenses are by 11.8% higher than the expenses of 2018, the increase is generated by applying the inflation index on the average wage of the previous year and by the increase of the average employee number.

The number of employees forecasted for the end of 2019 is 5.943, and the average number is 5.812 employees.

D. Other operating expenses

This chapter records an increase of expenses estimated for 2019 (by 21.5%) generated mainly by the level of depreciation expenses.

The chapter includes expenses with non-current assets, other expenses not included in the previous chapters, tangible and intangible assets depreciation, adjustments and provisions.

IV. 2019 Profit Distribution Proposal

Profit distribution was made in the 2019 budget proposal in compliance with the provisions of *GO no. 64/2001 on profit distribution at fully or majority state owned national companies, trade companies*, as subsequently amended and supplemented. The net profit distribution rate to shareholders is 50%, and the undistributed difference is allocated to own development sources.

V. Level of overdue receivables estimated for the end of 2019 is of RON 1,202,046 thousand.

VI. Level of Arrears is estimated to RON 0.

VII. Investment Program of RON 1,245,000 thousand is completely self-financed.

The priorities of Romgaz 2019 Investment Program are focused on projects aiming to compensate the natural decline of the gas production, by way of:

- continuing geological research works through new exploratory drillings and geological and geophysical surveys to discover new natural gas reserves;
- development of the production potential by ensuring new capacities for the already existent facilities (drilling production wells, surface facilities, compressor and dehydration stations, booster compressors), improving the performances of the existing facilities and equipment,

- in order to increase the operational safety, reduce energy consumptions and enhance efficiency of gas reservoir production;
- develop the electricity generation potential by building a new thermal power plant with combined gas cycle at CET Iernut;
 - modernization and refurbishment of workover rig equipment and installations as well as procurement of high performance equipment and installations specific for the main activity;
 - specific machinery acquisition to ensure technological transportation and maintenance of the main activity, as well as maintaining optimum conditions of road infrastructure in gas fields.

VIII. Summary of Main Indicators

	RON million	Achieved 2018	Proposal 2019	Ratios 2019/2018 %	Estimations 2020	Estimations 2021
1	Total income	5 222.5	5 023.5	96.2%	5 022.6	5 085.1
2	Total expenses	3 643.7	3 898.8	107.0%	4 000.8	4 120.9
3	Gross result	1 578.9	1 124.7	71.2%	1 021.8	964.2

IX. Indicator Forecast for 2020 - 2021

The forecast for 2020 – 2021 rests on those assumptions underlying the substantiation of the 2019 budget, the market demand and conditions, current legislation on natural gas delivery prices.

We would like to emphasize that the indicators forecasted for 2020 and 2021 are indicative only and are not the final indicators of the company's performance for the respective years; they are going to be updated in accordance with the law in force when preparing the income and expenditure budgets for each of the respective years.

ROMGAZ Board of Directors endorsed the Income and Expenditure Budget Proposal for 2019 and the forecast for 2020 – 2021 in the meeting of April 11, 2019.

In accordance with Article 4 paragraph (1) letter d) of Government Ordinance no. 26/2013, we hereby request the Ordinary General Meeting of Shareholders to approve SNGN Romgaz SA Medias Individual Income and Expenditure Budget for 2019.

The following annexes are part of the Income and Expenditure Budget:

- Annex 1: 2019 Income and Expenditure Budget (including estimations for 2020 – 2021); we publish only Annex 1 with the column for the current year, in accordance with O.M.F.P. no. 3145/2017.
- Annex 2: Detailed information on the economic-financial indicators included in the income and expenditure budget and their quarterly distribution;
- Annex 3: Total Income Stage of Completion;
- Annex 4: Investment Program, Equipment and Financing Sources;
- Annex 5: Measures to Improve Gross Result and Reduction of Outstanding Payments.

The data for years 2020 -2021 from Annex 1 and Annex 2-5 are not public. These may be reviewed only by Romgaz shareholders at the headquarters, daily between 10 am – 2 pm; the shareholders may address questions in compliance with the procedure described in the Convening Notice of the Ordinary General Meeting of Shareholders (OGMS) on *day 17, 2019.*

**CHAIRMAN
OF THE BOARD OF DIRECTORS
Dorin-Liviu NISTORAN**



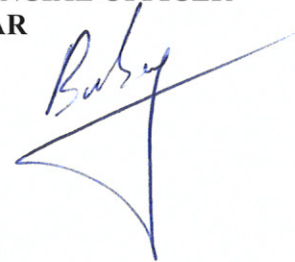
ENDORSED,

**CHIEF EXECUTIVE OFFICER
Adrian Constantin VOLINTIRU**

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**CHIEF FINANCIAL OFFICER
Andrei BOBAR**



2019 INCOME AND EXPENDITURE BUDGET - INDIVIDUAL

RON thousand

		INDICATORS	Row no.	2019 Budget proposal
0	1	2	3	4
I.		TOTAL INCOME (Row1=Row2+Row5+Row6)	1	5 023 454
	1	Total operating income out of which:	2	5 002 165
		a) subsidies, according to legal provisions in force	3	
		b) transfers, according to legal provisions in force	4	
	2	Financial income	5	21 289
	3	Extraordinary income	6	
II		TOTAL EXPENSES (Row7=Row8+Row20+Row21)	7	3 898 761
	1	Operating expenses, out of which:	8	3 866 963
	A.	expenses for goods and services	9	719 843
	B.	expenses for taxes, duties and similar payments	10	1 133 393
	C.	personnel-related expenses, out of which:	11	778 163
	C0	expenses for salaries and wages (Row 13+ Row14)	12	718 283
	C1	expenses for salaries	13	638 166
	C2	expenses for bonuses	14	80 117
	C3	other personnel expenses, out of which:	15	13 666
		expenses with termination benefits	16	12 458
	C4	expenses for the mandate contract and for other management and control bodies, committees and commissions	17	2 923
	C5	expenses with contributions owed by the employer	18	43 291
	D.	other operating expenses	19	1 235 564
	2	Financial expenses	20	31 798
	3	Extraordinary expenses	21	
III		GROSS RESULT (profit/loss)	22	1 124 694
IV		PROFIT TAX	23	225 571
V		PROFIT AFTER DEDUCTION OF PROFIT TAX, out of which:	24	899 122
	1	Legal reserve	25	
	2	Other reserves representing fiscal facilities provided by law	26	
	3	Coverage of accounting loss from previous years	27	
	4	Establishing equity finance for projects co-financed from foreign loans, and establishing sources for reimbursement of installments, payment of interest rates, charges and other costs related to such loans.	28	
	5	Other distributions provided by law	29	
	6	Accounting profit after deduction of the amounts provided at Rws. 25, 26, 27, 28 and 29.	30	899 122

RON thousand

		INDICATORS	Row no.	2019 Budget proposal
0	1	2	3	4
	7	Profit share payable to employees within the limit of 10% of the net profit, but not more than one monthly average base salary paid by the economic operator during the reference financial year	31	28 829
	8	Minimum 50% payments to the state budget or local budget in case of autonomous companies, or as dividends paid to shareholders in case of national companies and companies which are fully state-owned or where the state is the major shareholder, out of which:	32	463 975
	a)	- dividends to the state budget	33	324 783
	b)	- dividends to the local budget	33 a	
	c)	- dividends to other shareholders	34	139 193
	9	Profit not allocated to rows 31-32 is allocated to other reserves and represents the company's own equity finance	35	435 147
VI		INCOME FROM EUROPEAN FUNDS	36	
VII		ELIGIBLE EXPENSES FROM EUROPEAN FUNDS, out of which:	37	
	a)	expenses for materials	38	
	b)	expenses for salaries	39	
	c)	expenses for services	40	
	d)	expenses for promotion and advertising	41	
	e)	other expenses	42	
VIII		INVESTMENT FINANCING SOURCES, out of which:	43	1 245 000
	1	Allocations from the budget, out of which:	44	
		budget allocations related to payments of previous years commitments	45	
IX		INVESTMENTS	46	1 245 000
X		SUPPORTING DATA	47	
	1	Forecasted no. of employees at the end of the year	48	5 943
	2	Total average number of employees	49	5 812
	3	Average monthly income per employee (RON/person) determined on basis of salary-related	50	9 430
	4	Average monthly income per employee (RON/person) determined on basis of salary expenses recalculated under the Annual Law of the State Budget	51	9 211
	5	Labour productivity in financial units per total average number of employees (thousand RON/person) (Rw.2/Rw.49)	52	861
	6	Labour productivity in financial units per total average number of employees recalculated under the Annual Law of the State Budget	53	861
	7	Labour productivity in physical units per total average number of employees (thousand RON/person)	54	
	8	Total expenses related to RON 1 000 total income (Rw.7/Rw.1)x1000	55	776
	9	Outstanding payments	56	
	10	Overdue accounts receivables	57	1 202 046

CHIEF EXECUTIVE OFFICER,
ADRIAN CONSTANTIN VOLINTIRU



CHIEF FINANCIAL OFFICER,
ANDREI BOBAR