



AB AMBER GRID STRATEGY

2017–2022

CONDENSED VERSION

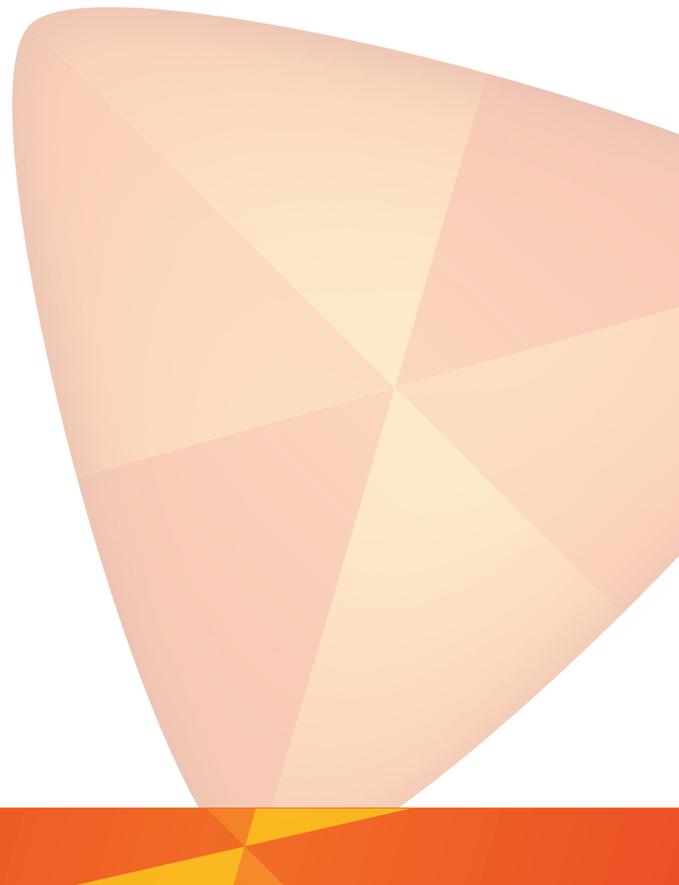


TABLE OF CONTENTS

	SUMMARY	3
1.	DESCRIPTION OF ACTIVITIES	4
	1.1. Company Activities	4
	1.2. The Company's Shareholder Structure	4
	1.3. The Company's Services and Clients	5
2.	ANALYSIS OF ENVIRONMENTAL FACTORS	8
	2.1. Analysis of the Company's Internal Environment	9
	2.2. Analysis of the Company's External Environment	10
	2.2.1. An Overview of the Most Important Events in the Region	11
	2.2.2. Political, Economic, Social, Technological, Environmental and Legal Impact Factors	12
	2.2.3. Strengths, Weaknesses, Opportunities and Threats (SWOT) Analysis	14
3.	STRATEGY OF AB AMBER GRID	14
	3.1. Mission, Vision, Strategic Directions and Values	14
	3.2. Strategic Objectives and Performance Measurement Indicators	16
4.	RISKS AND RISK MANAGEMENT	17
5.	IMPLEMENTATION OF THE STRATEGY	18

SUMMARY

The aim of this document is to outline AB Amber Grid’s (hereinafter referred to as Amber Grid or the Company) strategic directions, objectives, tasks and actions / programmes for the period spanning 2017–2022, as well as to develop specific performance measurement indicators based on which the Company will evaluate its performance both in the short and long term. Having started operating as an independent transmission system operator on 1 August 2013, a long-term strategy of the Company was approved in 2015. The present strategy paper for 2017–2022 presents updated data, forecasts, objective assessment of the business environment developments and changes in the market situation, which affects the Company’s long-term strategy.

Amber Grid’s strategy is based on the integration into a single regional natural gas market, efficiency, modernisation, fostering of infrastructure, and development of an advanced organization. These elements are essential in terms of the pursuit of the strategic and financial objectives set by the shareholder.

AMBER GRID’S MISSION

We provide effective and reliable gas transmission, we create favourable conditions for competition in the gas market and for the development of renewable energy sources.

Amber Grid is Lithuania’s gas transmission system operator. The Company owns, operates and

develops natural gas infrastructure – Lithuania’s gas transmission pipelines and ancillary facilities – and secures safe and reliable gas transportation. The Company’s main tasks are to connect gas systems, to grant a non-discriminatory access to the system, to create conditions for competition on the gas market and the development of renewable energy sources, and to contribute to the process of making gas, as an energy resource, to help the economy grow.

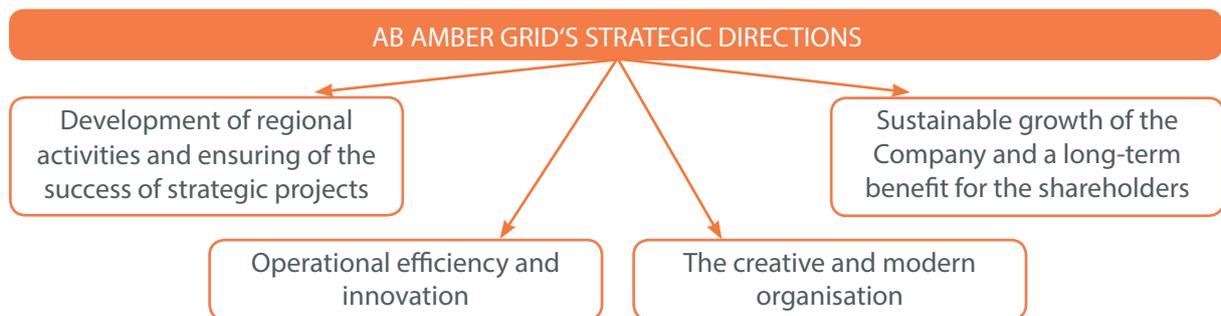
AMBER GRID’S VISION

Innovative energy company in the integrated European gas network.

In the perspective of 2017-2022, Amber Grid sees the gas markets of the four countries of the Eastern Baltic Region (Lithuania, Latvia, Estonia and Finland) as a single gas market, i.e. a market operating according to harmonised rules, having a single area in terms of gas trading, balancing and entry-exit points. Upon the completion of the construction of the gas system interconnector linking the transmission pipelines of Amber Grid and GAZ-SYSTEM SA (i.e. upon the implementation of the Gas Interconnection Poland-Lithuania Project (hereinafter – the GIPL Project), the region’s gas market will be interconnected with the gas market of the European Union (hereinafter – the EU).

In pursuit of the Company’s vision and the strategic objectives set by the state and the shareholder – to increase the corporate value and ensure the implementation of strategic interests of the country in the gas sector – AB Amber Grid will mainly focus on the following four strategic directions:

- ▲ development of regional activities and ensuring of the success of strategic projects;



- ▲ sustainable growth of the Company and a long-term benefit for the shareholders;
- ▲ operational efficiency and innovation;
- ▲ the creative and modern organisation.

Seeking for a clearer linking of the strategies of UAB EPSO-G (hereinafter – EPSO-G) Group companies in the implementation of the strategic directions, a decision was made to unify them across all companies of the Group.

In order to implement the strategic directions, Amber Grid works on the development of an appropriate organisational culture based on shared values of UAB EPSO-G Group. Amber Grid's values form the basis for corporate behaviour, corporate activities and organisation culture.

The Company follows three core values:

- ▲ professionalism;
- ▲ cooperation;
- ▲ progress.

Strategic goals, objectives and measures with the pursued outcome and deadlines has been prepared for each of the strategic directions of the Company.

Specific measurable indicators have been set for the strategic goals of the Company, based on which the Company will evaluate its performance both in the short and long term.

The present long-term strategy paper also analyses the current situation, presents the results of the analysis of the Company's internal and external impact factors, the analysis of its strengths, weaknesses, opportunities and threats (SWOT), and a description of the risk and risk management measures, financial targets and indicators, principles of the strategy evaluation, improvement and maintenance.

1. DESCRIPTION OF ACTIVITIES

1.1. Activities of the Company

Amber Grid is Lithuania's natural gas transmission system operator responsible for the transmission

of natural gas (transportation via high-pressure pipelines) to system users, also for the operation, maintenance and development of the natural gas infrastructure. Amber Grid was registered on 25 June 2013 following the spin-off of the natural gas transmission activity (including the assets, rights and obligation attributed to this activity) from AB Lietuvos Dujos. The Company has been in operation since 1 August 2013 with the entering into force of an interim natural gas transmission licence issued to the Company by the National Commission for Energy Control and Prices (hereinafter – the NCC).

The new legal entity was established in the implementation of the requirements of the third energy package of the EU and of the Law on Natural Gas of the Republic of Lithuania. The incorporation of Amber Grid marked the implementation of the legal, functional and organisational unbundling of the natural gas transmission activity.

When on 21 May 2014, E.ON Ruhrgas International GmbH and on 19 June 2014, OAO Gazprom transferred the Company's shares to UAB EPSO-G controlled by the Ministry of Energy of the Republic of Lithuania, and after the composition of the Board of Directors of the Company was changed by respective decisions of the Extraordinary General Meeting of Shareholders on 30 June 2014, Amber Grid's activities and ownership control was unbundled from natural gas companies engaged in gas production and supply activities. On 10 April 2015, the NCC issued to the Company an open-ended transmission system operator's license, and thus the Company was designated a certified transmission system operator in accordance with the applicable EU requirements.

Amber Grid owns 100 % of shares of UAB GET Baltic. UAB GET Baltic administers an electronic trading platform for trading short-term and long-term natural gas products at various trading sites located in Lithuania, Latvia and Estonia.

Since 1 November 2015, Amber Grid has been a member of the European Network of Transmission System Operators for Gas (ENTSOG).

1.2. Structure of the Company's shareholders

According to the data of 30 June 2018, more than 2 200 natural and legal persons from Lithuania

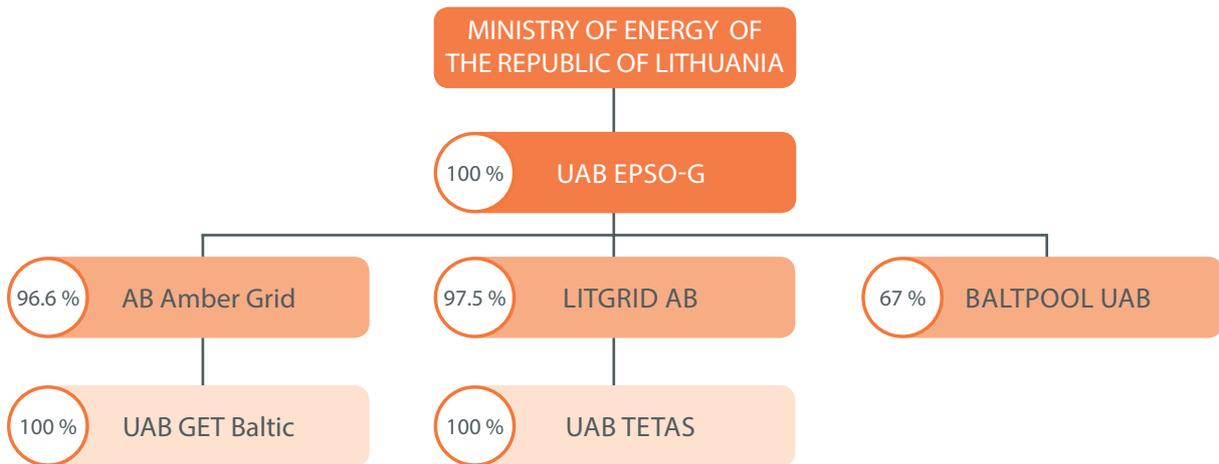


Figure 1. UAB EPSO-G Group

and abroad were shareholders of the Company, of which one shareholder, namely, UAB EPSO-G, had a controlling (96.58%) stake in the Company. The remainder of the Company’s shares (3.42%) is quoted on the Stock Exchange NASDAQ Vilnius Baltic Secondary List (the acronym of the Company at the Exchange is AMG1L).

The main shareholder of the Company, UAB EPSO-G, is 100%-owned by the Ministry of Energy of the Republic of Lithuania. UAB EPSO-G also has the controlling interest in the Lithuania’s electricity transmission system operator Litgrid AB and other companies. Figure 1 illustrates the governance structure of the parent company.

1.3. Services provided by the Company and its customers

As a natural gas transmission system operator, the Company provides system users, other operators and natural gas market participants with the following services:

- ▲ transmission of natural gas in the territory of Lithuania;
- ▲ balancing of natural gas flows in the transmission system;
- ▲ administration of funds intended to compensate costs of the construction and operation of the liquefied natural gas (hereinafter – LNG) terminal, its infrastructure and interconnection.

Customers of the Company are large producers of electricity and district heating, industrial companies and medium-sized Lithuanian businesses, also natural gas supply companies, which are provided with natural gas transmission services. Figure 2 illustrates the structure of the natural gas transmission system users in terms of the transmitted volume of natural gas.

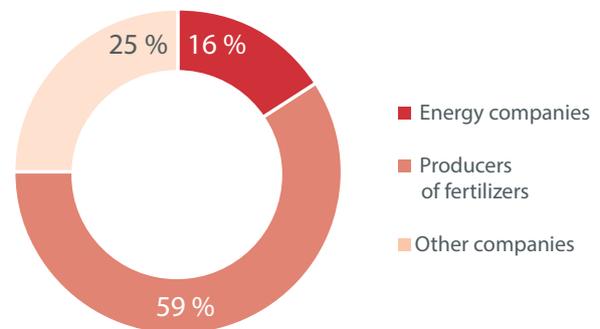


Figure 2. Structure of natural gas transmission volume by system users, 2017, %.

Currently, the Lithuania’s natural gas transmission system comprises:

- ▲ 2,115 km of gas transmission pipelines;
- ▲ 68 points of connection with distribution systems and system users;
- ▲ 2 cross-border gas metering stations;
- ▲ 2 gas compressor stations.

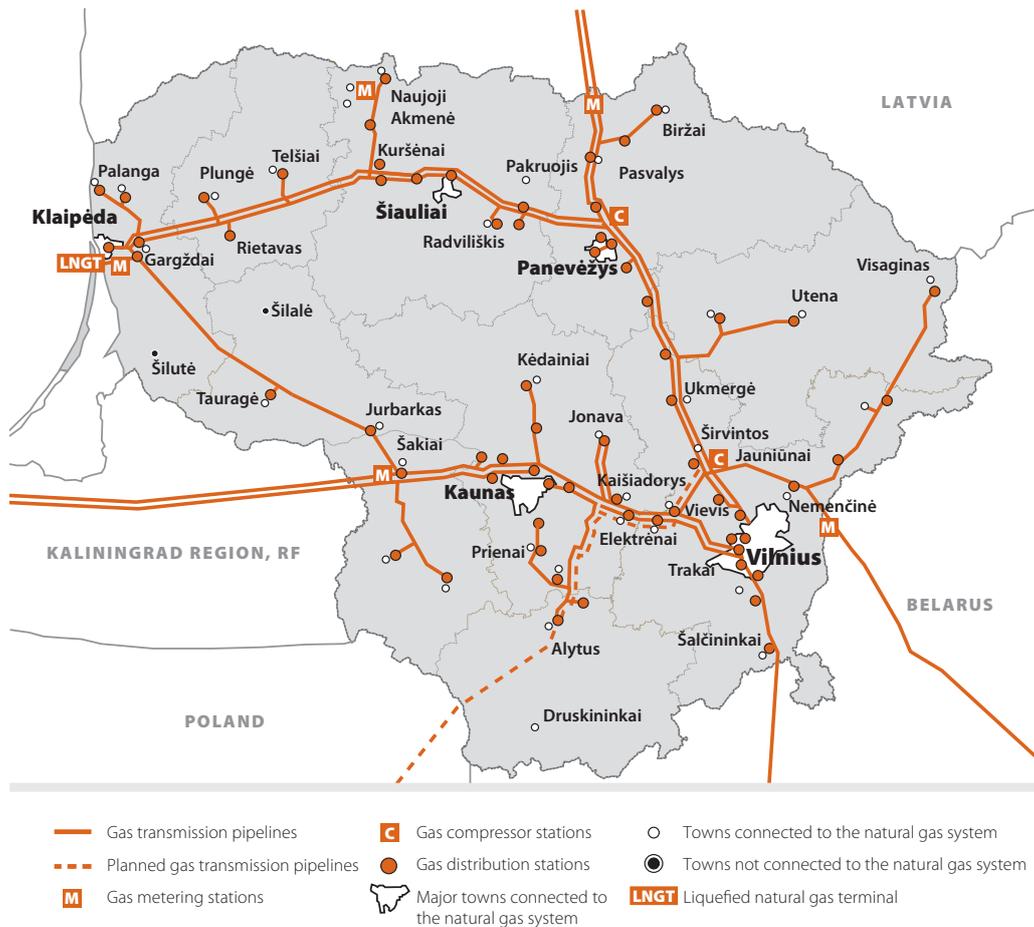


Figure 3. Map of Lithuania’s natural gas transmission system

A map featuring Lithuania’s natural gas transmission system and highlighting the main infrastructure facilities operated by Amber Grid is presented below (Figure 3).

Pricing of the natural gas transmission activity

The NCC regulates the prices of natural gas transmission and balancing services provided by Amber Grid. The NCC also sets the additional natural gas supply security price component designated for compensating costs of the construction and operation of the LNG terminal, its infrastructure and interconnection, as well as for administering these funds. In October 2018, the NCC set for the Company a natural gas transmission price cap for the total volume of natural gas planned to be transported via the transmission system (including transit and transport in the EU states) of EUR 0.88 / MWh to take effect as from 1 January 2019, which is

subject to annual adjustments in accordance with the procedure established by law (price caps set for the Company in October 2017 for each individual natural gas transmission system entry-exit point per unit of long-term capacity booked applied in 2018). The core income of the Company currently comes from natural gas transmission services, with transmission services provided to Lithuanian natural gas users accounting for the major share thereof.

Figure 4 illustrates price¹ dynamics for the needs of Lithuanian users in 2010–2019.

More significant changes that occurred in price dynamics in 2015–2016:

- ▲ In the implementation of the requirements of EU legislation, at the beginning of 2015, Lithuania introduced a model for allocation of capacities

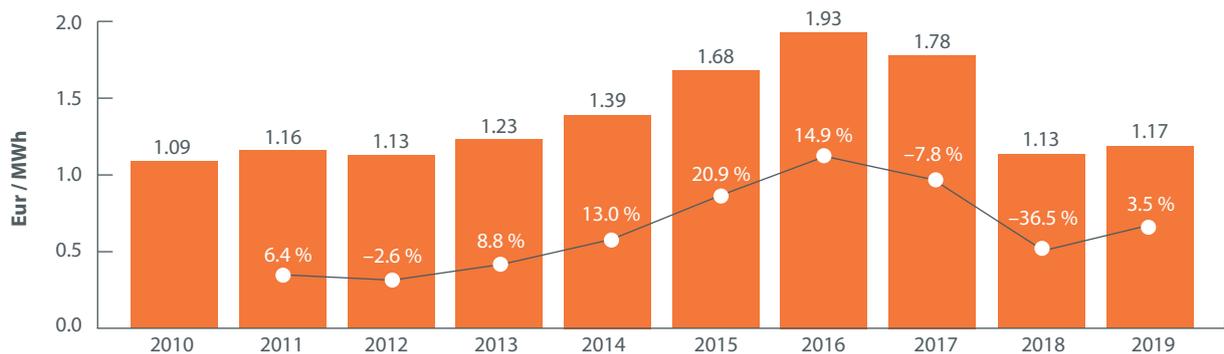


Figure 4. Dynamics of average natural gas transmission service prices in 2010–2019

of the natural gas transmission system entry-exit points and their pricing, which replaced the principle of “postage stamp” formerly used to set gas transmission service prices (associating prices with a specific route);

- ▲ In order to increase the correlation between gas transmission service costs, profits and payment for the services, at the end of 2015, the NCC amended the Methodology for Setting State-regulated Prices in the Natural Gas Sector, allowing to apply a three-component gas transmission service price, also setting the price for consumption capacity². A trinary price has applied at the internal transmission system exit point since 2016: the price for gas transmission capacity booked; the price for the set consumption capacity and the price for transmitted volume. The covering of a part of costs of the transmission system through the application of the price for consumption capacity allows forming a rational behaviour of natural gas transmission system users, promoting efficient use of the transmission capacity that they need and thus reducing costs of using transmission infrastructure, which in turn allows optimizing investments in the transmission system.

Processes that occurred/ have been lasting since 2017 and the planned changes in pricing:

- ▲ Commission Regulation establishing a network code on harmonised transmission tariff structures for gas (2017/460) was introduced in the European Union on 6 April 2017, with a part of its provisions (related to the price publication requirements) taking effect as from 1 October 2017 and a part (related to the applicable methodology for setting transmission prices, pricing of transmission capacity products and harmonization of the permissible income level) – as from 31 May 2009; taking into consideration the fact that provisions of Regulation 2017/460 will apply in full as from 31 May 2019, the Company’s transmission service prices will also depend on the requirements of the Regulation 2017/460 as from 2020;
- ▲ Given the fact that in recent years, gas flows have not had any nature of seasonality at certain points, and in order to stimulate the development of the natural gas market of Lithuania and the entire Eastern Baltic region, as from 2018, prices of short-term (quarterly,

¹ Average gas transmission prices (exclusive of indicators attributed to the service of gas transportation to/from a third country) for 2015–2019, exclusive of indicators attributed to gas transmission through the cross-border Kiemėnai Gas Metering Station entry/exit point; i.e. the prices cover average prices for the needs of Lithuania’s domestic consumers). For the years 2010–2019, the average prices that are comprised of the price component for gas transmission capacities (from 2016 onwards not only for the capacities booked, but also for consumption capacities) and the price for gas transmission volumes are expressed in units of energy (MWh) (gas pricing in units of energy was introduced from 2015 only; till then, prices were set per volume unit (per thousand m³)). According to the price cap set by the NCC for 2019, the average price to meet the needs of Lithuanian consumers could increase in 2019 compared to the price of 2018; however, solutions applied by the Company in order to reduce transmission service prices ensured that the average price to meet the needs of Lithuanian consumers increased only slightly in 2019.

² Natural gas consumption capacity means the maximum daily natural gas volume needed by natural gas system users and/or consumers to meet their maximum natural gas consumption needs at each natural gas delivery point. Consumer capacities are calculated and set according to the procedure set by the Government, which also provides for a mechanism to encourage consumers / system users not to exceed their declared consumption capacity level or the level that has been set for them when booking transmission capacities.

monthly, daily) transmission capacity were set in all entry points and at the point of exit to the Republic of Latvia (Kiemėnai) no longer applying seasonal factors (i.e. eliminating price differences in different seasons). Such pricing will have an incentive effect on cross-border gas flows;

- ▲ A new 5-year regulatory period (from 1 January 2019 to 31 December 2023) will start in 2019 and, having also taken into account provisions of Regulation 2017/460, a transition from the regulatory mode, in accordance with which price caps are set for the Company, to the regulatory mode setting the permissible income level of the Company will be made. Accordingly, amendments to the Methodology for Setting State-regulated Natural Gas Transmission Income and Prices of the NCC (approved in October 2018) are planned at the end of 2018/ beginning of 2019 (having set the permissible income level of the Company for 2019 and calculating the price cap based thereon, the Commission plans to set in the nearest future the permissible income level of the Company only, having taken provisions of Regulation 2017/460 into account);
- ▲ Having assessed methodological amendments to the setting of prices according to the Methodology for Setting State-regulated Natural Gas Transmission Income and Prices of the NCC (approved in October 2018) – unifying the principles for the setting of gas transmission prices in the EU states, the principle of “postage stamp” applied when setting the prices of natural gas transmission services;
- ▲ On 7 September 2017, national regulatory authorities (NRA) of Lithuania, Latvia, Estonia and Finland reached a principled agreement on methodological guidelines for the regional natural gas market in the Eastern Baltic region (hereinafter – the Guidelines) aimed at harmonizing the transmission service pricing in the Eastern Baltic region;
- ▲ Taking the Guidelines into consideration, the Company has been actively working with Latvian, Estonian and Finnish transmission system operators aiming to develop a common entry and exit point zone in the Eastern Baltic region in order to harmonize transmission service prices at entry points into the region (with possible discounts under Regulation

2017/460 at the points of entry from the LNG terminal in Klaipėda and from the infrastructure created to eliminate the separation of the transmission systems of the Member States). To achieve this goal, the Company and the Latvian, Estonian and Finnish transmission system operators seek to establish a mechanism for cost reimbursement between transmission system operators (Inter-TSO Compensation (ITC) mechanism).

More detailed information on natural gas transmission service prices, pricing and information under the Regulation 2017/460 is available on the Company’s website www.ambergrid.lt (in the section “Prices and Taxes” under the heading “Transmission Services”).

2. ANALYSIS OF ENVIRONMENTAL FACTORS

Further this paper analyses the internal and external factors with the greatest impact on the Company’s activities. According to the Strategic Planning and Strategic Management Guidelines issued by the Ministry of Economy of the Republic of Lithuania, Amber Grid’s operating strategy sees the environmental impact as a combination of external environmental factors (political, economic, social, legal, environmental and technological), internal strengths and weaknesses, and opportunities and threats arising from the outside. All this affects the strategic directions selected by the Company. The Figure below shows the key internal and external impact factors affecting the business of Amber Grid.

In the beginning of 2016, the Company conducted an exhaustive analysis assessing the natural gas transmission activity prospects for the period until 2035. This analysis is updated annually. The analysis served as a basis for carrying out the analysis of Amber Grid’s environmental factors in 2018, as well as for the formation of the strategic objectives and tasks of the Company.

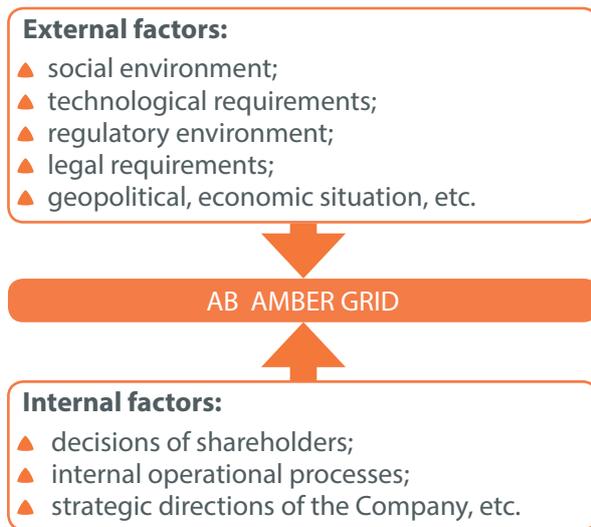


Figure 5. Matrix of internal and external factors of Amber Grid

The business environment in which Amber Grid operates is constantly affected by:

- ▲ changing legal frameworks of the EU and of Lithuania;
- ▲ energy and environmental policy;
- ▲ changes in the regulatory environment;
- ▲ development of technologies in the energy sector.

For these seasons, the Company’s development and strategic directions are in part based on assumption. Even though the Company cannot control external factors further analysed in the strategy, any such factors are subject continuous evaluation and monitoring. In light of changing circumstances, the Company aims to predict any pending risks, to avoid threats and to take advantage of any growth and business development opportunities available in a timely manner.

The assessment of the said circumstances allows determining the specific direction that Amber Grid should choose and predict the results it can achieve during the strategy’s implementation period with a sufficient degree of objectivity.

2.1. Analysis of the Company’s internal environment

Amber Grid was established through the spin-off of natural gas transmission activity of

AB Lietuvos Dujos, the natural gas transmission system infrastructure, other assets, as well as human and other resources related to this activity. The Company, which was formed as a result of the spin off, engages in a single core activity – the transmission system operator’s activity – has functions that are clearly defined and is not engaged in any activities that are unrelated to its core business. One of the keys to carrying out natural gas transmission activity in an effective manner is management of internal processes, their efficiency and expediency.

The Company has sufficient technological, managerial and financial capacity to carry out its core activity.

The total length of the transmission system pipes is more than 2.1 thousand km in the territory of Lithuania. The natural gas infrastructure used in the Company’s activities has been developed since 1961. More than 50% of all the gas pipelines were built more than 25 years ago.

The Company operates 65 gas distribution stations (GDS), 3 gas metering stations (GMS) and 2 gas compressor stations (CS).

The Company’s moderate and balanced investment policy allows maintaining the infrastructure in an adequate condition, ensuring its reliability. Before 2015, the infrastructure was adapted for transmitting natural gas from a single source. Since the end of 2014, having built the LNG terminal in Klaipėda, gas has been imported from two sources. The LNG terminal allowed market participants to import gas from global markets. The construction of the Klaipėda-Kuršėnai gas transmission pipeline in late 2015 opened up the possibility to fully exploit the capacities of the LNG import terminal and to transport gas both in Lithuania and in the direction of other Baltic States. The LNG terminal can meet about 90% of the demand of the three Baltic States, it ensures diversification and security of natural gas supply. Works of the implementation of the gas interconnection Poland-Lithuania (the GIPL) project have been carried out as planned. The completion of the GIPL construction project is planned in 2021. A feasibility study and cost-benefit analysis of increasing the capacities of the pipeline interconnection between Latvia and Lithuania

was carried out in 2018 together with the Latvian transmission system operator Conexus Baltic Grid. The implementation of this project is planned by the end of 2023.

Since 2015, the Company’s information systems have been adapted to changes related to natural gas supply diversification, sale of transportation capacities and changes in units of measurement of gas volume. The information systems used by the Company have been harmonised with information systems of other gas transmission system operators operating in the region used in the fields of transmission capacity management, gas flow balancing and gas trade. The introduction of an Assets Management System and a Pipeline Integrity Management System (PIMS) is planned for the control of internal processes of the Company.

The Company started operating as a separate legal business unit on 1 August 2013, having successfully taken over most of the internal management processes from AB Lietuvos Dujos. Due to the specifics of activities of Amber Grid, the Company has to implement and review a number of its internal processes: its motivation systems, IT systems integration, project management, etc. They have been included in the Company’s business plans and started to be implemented.

The Company is in good and stable financial condition. The business nature and the regulation allow the Company to generate revenues covering the necessary costs and the regulated returns on investment. The Company’s leverage ratio enables efficient execution of its investment and development projects.

Amber Grid’s structure and governance principles

After amendments to the Law on Companies of the Republic of Lithuania took effect in 2018, the Board of AB Amber Grid has been strengthened conferring thereto supervisory functions. Having complemented the responsibility of the Board, the composition of the Company’s Board changed as well in 2018. In order to continue to comply with good governance practice, representatives of the Company’s administration carrying out the

executive function can no longer be elected to the Board consisting of five members and carrying out the supervisory function. The Articles of Association of the Company establish that the Board of the Company shall consist of 5 (five) members elected for a term of office of four years. The Board of the Company consists of two independent members and three employees of the parent company UAB EPSO-G.

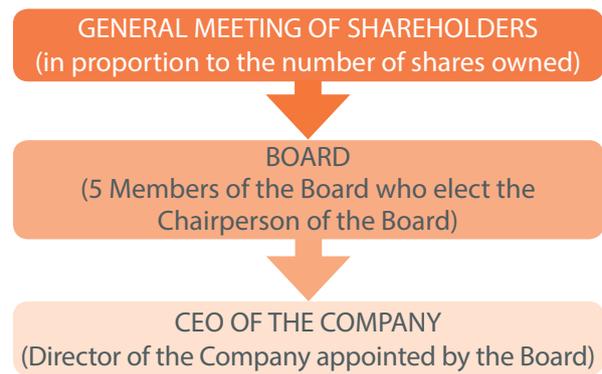


Figure 6. Amber Grid’s governance principles

In 2014, Amber Grid became a part of UAB EPSO-G Group and, consequently, a company indirectly owned by the state. The Company’s governance structure is essentially consistent with the applicable regulations on state policies established in respect of state-owned enterprises.

The Company’s corporate governance implements the good governance principles and corporate governance policies of state-owned enterprises.

2.2. Analysis of the Company’s external environment

The gas transmission activity is subject to licensing. The license grants exclusive rights to provide gas transmission services throughout the entire territory of the Republic of Lithuania. The Company operates in a strictly regulated environment that is constantly changing and is dependent on provisions of legal acts of the EU and national Lithuania’s legislation, policies regulating the natural gas transmission sector as well as actions of authorities implementing these policies.

2.2.1. Overview of the most important developments in the region

In the past few years, natural gas demand in the Eastern Baltic Region, which includes Finland, Estonia, Latvia and Lithuania, has been declining. From 2013 to 2017, it shrank by nearly 17%. The main causes include the conversion of fuel in the heat production sector, moving to energy production from renewable energy sources, the possibility to import cheap electricity, which makes local electricity production uncompetitive, and the decline in consumption by industrial companies, e.g. in the shrinking paper production sector in Finland. Finland consumes the most of natural gas in the region (28.9 TWh). Lithuania uses the most of natural gas among the three Baltic States – 24.3 TWh, i.e. almost two times more than Latvia (13.8 TWh) and over four times more than Estonia (5.2 TWh). According to forecasts, natural gas consumption will stabilise at this level.

The European Natural Gas Sector has been rapidly changed by the implementation of the third energy package of the EU. This legislative package is aimed at the liberalisation of the natural gas market, promoting competition among different natural gas suppliers. Legislation relevant to the gas sector includes:

Directive:

- ▲ DIRECTIVE 2009/73/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC

Regulations:

- ▲ REGULATION (EC) No 715/2009 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 13 July 2009 on conditions for access to the natural gas transmission networks (715/2009);
- ▲ REGULATION (EC) No 713/2009 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 13 July 2009 establishing an Agency for the Cooperation of Energy Regulators (713/2009).

Pursuant to package regulations and directives, European states have been unbundling their natural gas transmission activities from the gas supply and

distribution businesses in their vertically integrated natural gas companies. The aim is to create an integrated natural gas market of European states, thus creating preconditions for greater market liquidity, competitive pricing, more efficient use of infrastructure and improved security of supply.

The most important current developments in the Eastern Baltic Sea Region are related to activities of natural gas transmission system operators, in particular, to the unbundling of gas companies' activities and transfer of their shares to new legal entities, also cooperation of gas sector representatives in the development of a liberal and integrated gas market.

Lithuania and Estonia have already established their separate companies engaged exclusively in gas transmission activity, namely, Amber Grid and Elering AS. The latter company is also engaged in electricity transmission activity. Since the beginning of 2017, AS Conexus Baltic Grid has been Latvia's natural gas transmission system and gas storage system operator established having unbundled the activity of gas transmission via gas transmission pipelines from AS Latvijas Gaze. Preparations for the unbundling of the gas transmission activity from the gas distribution and supply business are also underway in Finland. A newly established gas transmission system operator is planned to start operating in 2020, also opening the wholesale and retail gas markets to foreign companies.

A well-functioning regional market of the Eastern Baltic countries requires harmonisation of the legislation and regulations throughout the region as well as an adequate infrastructure.

To coordinate the development of the regional market, at the beginning of 2015, a special working group was set up, consisting of representatives of the Eastern Baltic Region's transmission system operators, ministries in charge of the energy sector and national regulatory authorities. In March of 2016, the consulting firm Frontier Economics prepared an Eastern Baltic Regional Market Development Study at the order of transmission system operators. It was funded by the Baltic Sea Region Energy Cooperation Organisation (BASREC). The study advised that the most appropriate markets integration model would be to combine the Lithuanian, Latvian, Estonian

and Finnish gas markets into a single market area, with a single entry-exit points system for the four countries and with a single virtual trading point and one balancing zone. On the basis of this study, the working group drafted an Eastern Baltic Regional Gas Market Development Action Plan, which was approved by prime ministers of the Baltic States in December of 2016. Since 2016, the working group has been working on the implementation of the Action Plan aiming to create a single gas market by the end of 2019.

On 1 July 2017, the Company, together with Latvian and Estonian transmission system operators, started using the implicit capacity allocation model at cross-border interconnection points in the Baltic States for the allocation of the capacities of the upcoming day. It is an instrument for the integration of gas markets of the Baltic States used in the transitional period in order to increase the competitiveness of gas market and promote cross-border trade in gas. According to the plans, the regional gas market should start operating in 2020. The application of the implicit capacity allocation model was expanded on 2 July 2018 having also started allocating capacities of the current day.

Together with other members of the Group, the Company prepared the principles of the management of transmission capacities in a single Baltic States' market, alternatives for the establishment of a market operator and concepts of a single balancing area in 2017. The conducted analysis was used in drafting balancing rules and the rules of transportation in the single area in 2018.

Also, investments in the integration of the region's natural gas transmission systems have been planned.

The plan is to integrate the region with the European natural gas market through the construction of the gas interconnector Poland-Lithuania (GIPL). In October of 2015, an agreement was concluded among Amber Grid, GAZ-SYSTEM A.S. and the EU Innovation and Networks Executive Agency, whereby the GIPL project was granted EU financial support covering 60% of the eligible project costs. In 2017, amendments to EU financial assistance contracts were signed. The amendments were initiated after the Polish

transmission system operator GAZ-SYSTEM S.A. faced problems during the preparation of the GIPL project and proposed to alter the pipelines' route in the territory of Poland, leading to the changed scope of the GIPL project in the territory of the Republic of Poland and its implementation deadlines. The planned total project value is about EUR 510 million. The project implementation deadline was extended until 31 December 2021. In May 2018, a cost allocation agreement was signed by Polish, Lithuanian, Latvian and Estonian transmission system operators establishing the procedure of allocation of GIPL project costs among the countries. Also, in May 2018, Amber Grid and GAZ-SYSTEM S.A. signed a network interconnection agreement confirming the final decision to invest in the GIPL project.

In August 2016, the European Commission decided to grant support of EUR 188 million for the project of the construction of the Balticconnector gas pipeline and the expansion of capacities of the cross-border connection between Estonia and Latvia. According to estimates, project costs total EUR 250 million. The Balticconnector gas pipeline will interconnect Estonia's and Finland's gas transmission systems and will create preconditions for Finland's integration into the Region's gas market. The transmission system operators are also considering investment in the expansion of the cross-border interconnection between Latvia and Lithuania and in the Incukalna Underground Gas Storage Facility in Latvia enhancing its capacity to supply gas in the winter season. Services of Klaipėda LNG Terminal have been developed in the development of LNG bunkering services intended to supply ships with fuel and to deliver LNG to smaller terminals, as well as through the construction of an over-ground LNG distribution station, which would supply areas outside the reach of the gas transmission system with gas with the help of vehicle transporters.

2.2.2. Political, economic, social, technological, environmental and legal factors

Decisions of national authorities on national strategic directions for energy and priorities

of development of individual energy sectors, decisions related to the promotion and development of biofuel and other energy resources, improved energy consumption efficiency, implementation of provisions of the Network Codes as adopted by the EU regarding gas pipeline safety, reliability, interoperability and access terms and conditions, trade, pricing and other fields will have the greatest impact on the Company's plans.

On 21 June 2018, the Seimas of the Republic of Lithuania approved the updated National Energy Independence Strategy. The National Energy Independence Strategy establishes that the extent of natural gas consumption in industry, transport and households will depend on the competitiveness of natural gas as an energy resource. Increasing natural gas consumption in industry and transport in the short and medium term is planned to partially offset the decline in natural gas consumption in energy production, and the extent of consumption of natural gas in the long term will depend on the consumption of natural gas for non-energy use in industry and transport.

The legal environment, which has a significant impact on the Company's business decisions, especially in the fields of the national energy policy and the EU assistance policy, is highly dependent on political developments and manifests in frequent amendments to legislation regulating the gas transmission sector, which may have an adverse impact on sustainability of the Company's long-term strategic decisions.

The most important economic factors affecting the natural gas transmission sector include the promotion and development of the use of biofuel and other renewable resources in the energy sector as well as a more efficient use of energy and energy resources. Due to large subsidies granted in various forms, namely, through incentive energy buy-up tariffs, direct grants or the incentive economic regulation regime, unequal competitive conditions are being created leading to a rapid growth in the use of biofuel both in the electricity and heating sectors, which reduces the demand for natural gas and undermine its competitiveness in the market, and, with infrastructure costs being largely stable, causes an increase in gas transmission and distribution service prices and the LNG Terminal

maintenance costs (the additional natural gas supply security price component) for market participants. Moreover, decisions to invest in the use of alternative fuels in the production of heat and electricity have so far been made in state-regulated energy fields, whose investments are subject to approval by regulatory authorities, without having carried out a comprehensive socio-economic assessment, which promotes re-investment and creates a risk of implementation of economically unfeasible investment projects.

Other important economic factors that can affect the Company's business decisions are the Company's customer structure, which determines a strong dependence of the Company's operating income on a few large gas system users (10 of the largest system users generate about 90% of the Company's revenue) and the availability of EU support funds for the development and modernisation of the gas transmission system.

Technological factors affecting the Company's operating decisions are related to the keeping of the natural gas infrastructure facilities used in the Company's operations in good working order. It is necessary to consider that 57% of gas pipelines were constructed more than 25 years ago. The condition of the operated gas pipelines is being inspected using various advanced techniques, such as the intelligent pigging, the external diagnostics based on electromagnetic field measurements, aerial pipeline inspection with the help of a helicopter carrying a laser-based highly sensitive gas leak detection equipment, etc. The findings of the inspections serve as a basis for carrying out essential repairs of individual sections of the Company's gas transmission pipelines, thus ensuring security and reliability of the transmission system.

Social factors that determine consumers' behaviour, for example, inciting them to choose a different type of fuel instead also have an indirect impact on the gas transmission business. These include a relatively low purchasing power of Lithuania's population, high emigration rate and negative demographic trends, even though, in the course of the past few years, gas prices decreased significantly and gas quality parameters improved (there was a significant improvement in the gas

supply security and the possibility to choose gas suppliers or to acquire gas at the natural gas exchange). An increasing shortage of skilled workforce and increasing wages will also have an adverse impact on the development of the sector and consumption.

The Company's operations are also affected by environmental policies of the EU – the ever stricter environmental requirements may result in the need for additional investments; moreover, in the implementation of environmental requirements, a priority is given to renewable energy development policies, which all have a significant impact on the decline in the consumption of natural gas.

2.2.3. Strengths, weaknesses, opportunities and threats (SWOT) analysis

In the view of the Strategic Planning and Strategic Management Guidelines prepared by the Ministry of Economy, in order to summarise the analysis of the environmental factors, an analysis of strengths, weaknesses, opportunities and threats (hereinafter – SWOT) was carried out. The analysis identified Amber Grid's strengths and weaknesses that depend on the Company's internal factors, also identifying the opportunities and threats – the external factors that are beyond the Company's control.

The internal and external environment analysis identified the essential strengths and weaknesses of AB Amber Grid and allowed determining the most significant external threats and opportunities.

The results of the SWOT analysis constitute a basis for developing operational scenarios, strategic directions and targets. The results of the analysis must be taken into account when setting strategic objectives or drawing up action plans, which are used to achieve the Company's strategic objectives. The following sections describe the strategic directions and objectives, specify in detail the strategic tasks and programmes, which have been developed in light of the findings of the conducted SWOT analysis.

3. AMBER GRID'S STRATEGY

3.1. Mission, vision, strategic directions and values

The transmission system operator's activity carried out by AB Amber Grid is regulated in detail by EU law and the national law of the Republic of Lithuania. Therefore, the fundamental points of the Company's strategy stem from the legislation governing the activity in question – the third energy package of the EU, the Law on Natural Gas of the Republic of Lithuania and its implementing legislation, and the National Energy Independence Strategy. The Company's strategy is impacted by the EU and national energy policy and the regulatory policies implemented by the regulatory authorities of the EU and Lithuania. The regulatory policies implemented by regulatory authorities directly affect the Company's strategic plans in terms of financial prospects. The Natural Gas Transmission System Operator's Ten-Year Network Development Plan drawn up by Amber Grid is subject to the NCC's approval. The Company's strategy is also affected by the fact that the Company's activity is essentially related to activities of transmission system operators of other countries and on its strategy. Moreover, the Company belongs to a Group owned by the state of Lithuania, which in turn is impacted by the policies of state-owned enterprises set by the state of Lithuania, which indirectly establish the expected rate of return, the strategic planning guidelines and governance principles.

In 2015, the European Commission introduced an ambitious Energy Union Package covering the dimensions of the security of supply, the creation of a single energy market, energy efficiency, research, innovation and pollution mitigation. Over the next decade, the most important task of the energy sector will be to ensure a high level of use of the existing infrastructure for the national development, transparency, and strengthening of regional cooperation. Amber Grid associates its contribution to the implementation of the European energy policy with the creation of a single natural gas market of the Baltic Region as

well as the construction and expansion of inter-system links.

AMBER GRID'S MISSION

We provide effective and reliable gas transmission, we create favourable conditions for competition in the gas market and for the development of renewable energy sources.

- ▲ EFFECTIVELY – we pursue the best results working efficiently and optimizing our operating processes.
- ▲ RELIABLY – we transport gas to our customers safely and without any unplanned interruptions.
- ▲ CONDITIONS FAVOURABLE FOR COMPETITION – we work for the conditions of the use of the transmission system and the services provided to be flexible and convenient for the existing and new gas market players, allowing to easily obtain gas from various sources.
- ▲ DEVELOPMENT OF RENEWABLE ENERGY SOURCES – by administering the register of “green” gas guarantees of origin and with other initiatives, we seek for the development of production and trade of gas from renewable energy sources.

AMBER GRID'S VISION

Innovative energy company in the integrated European gas network.

- ▲ INNOVATIVE – applying advanced methods and techniques, which allow working faster, more efficiently, offering innovative solutions to customers and partners.
- ▲ Integrated European gas network – when the Baltic and the European gas markets both having access to the global LNG market are interconnected by physical infrastructure as well as well-functioning market and

infrastructure rules, enabling easy and flexible gas transportation and trade.

Strategic directions

Seeking for a clearer linking of the strategies of UAB EPSO-G Group companies in the implementation of the strategic directions, a decision was made to unify them across all companies of the Group.

Amber Grid's strategic directions will contribute to the achievement of the objective of the National Energy Independence Strategy for the natural gas sector - to ensure technically reliable and diversified supply of natural gas to domestic consumers at competitive prices and costs based on the principle of efficiency and cost-effectiveness.

Amber Grid's strategy is based on the integration into a single regional natural gas market, efficiency, modernisation, fostering of infrastructure, and development of an advanced organization. These elements are essential in the pursuit of the strategic and financial objectives set by the shareholder. The diagram below summarises the strategy of Amber Grid.

In pursuit of the Company's vision and strategic goals set by the state and the shareholder – to increase the value of the Company and to ensure the implementation of national strategic interests in the gas sector – Amber Grid will focus on four strategic directions:

- ▲ development of regional activities and ensuring of the success of strategic projects;
- ▲ sustainable growth of the Company and a long-term benefit for the shareholders;
- ▲ operational efficiency and innovation;
- ▲ the creative and modern organisation.

Strategic objectives, tasks and measures with the desired outcomes and deadlines have been prepared for each of the strategic directions of the Company.

Values

With a view to the implementation of the strategic directions, Amber Grid has been developing an appropriate organisational culture based on the Company's values.



Figure 7. Amber Grid's strategy fact sheet

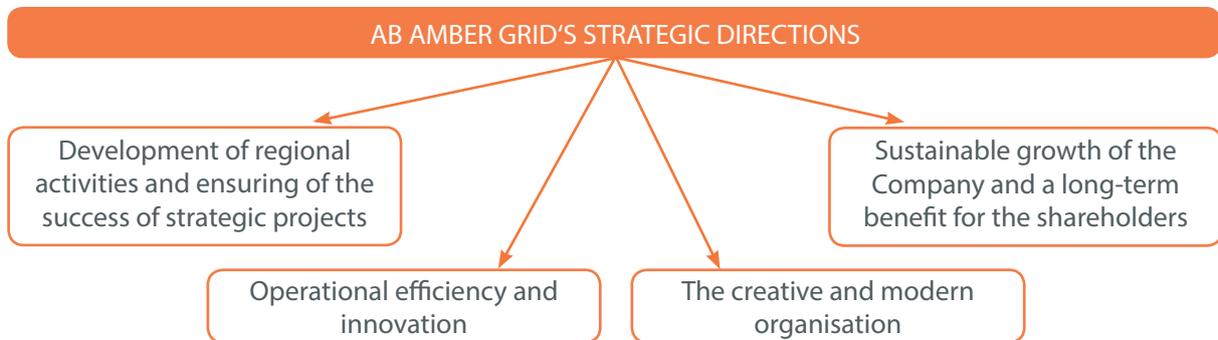


Figure 8. Amber Grid's strategic directions

Amber Grid is guided by common human, national and professional values. Amber Grid's values form the basis for the Company's behaviour, activities and organizational culture. Amber Grid distinguishes three core values: professionalism, cooperation and progress.

3.2. Strategic objectives and their measurement indicators

Specific measurement indicators were formed for some of the Company's strategic objectives, which it will use as a basis to evaluate its performance in the short and long term.

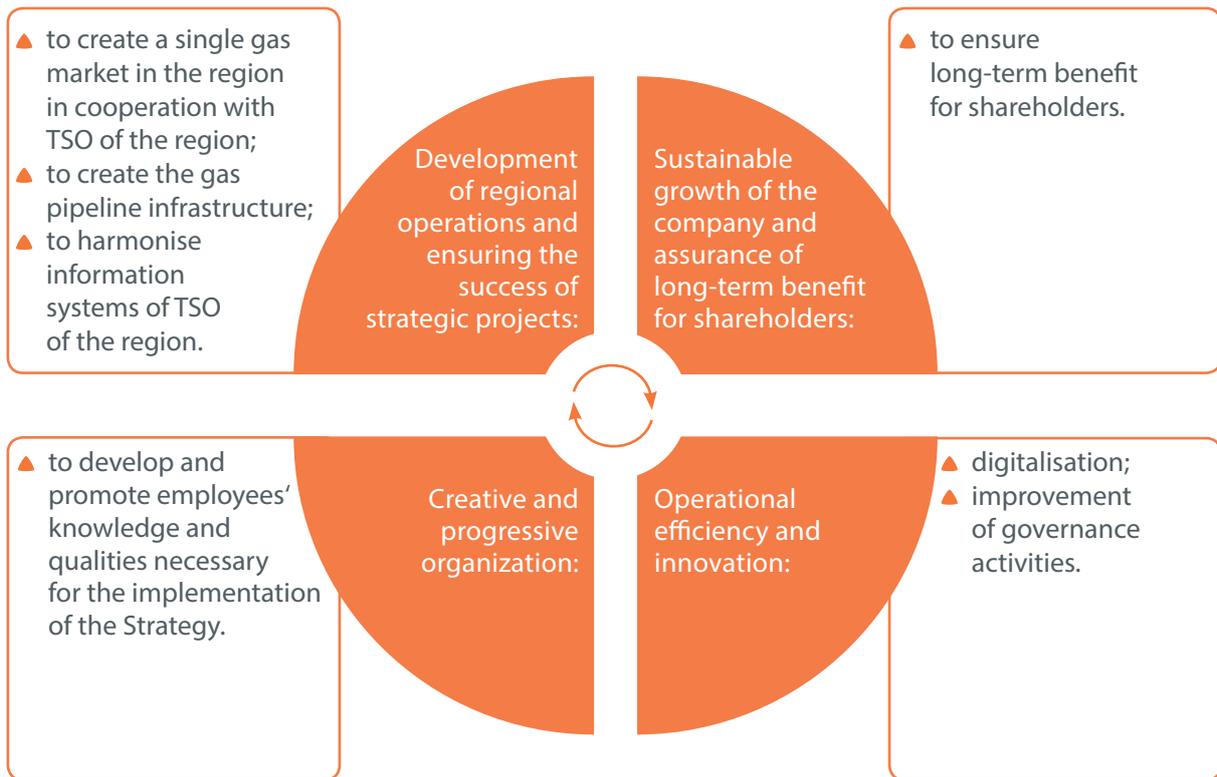


Figure 9. Relation between Amber Grid's strategic directions and objectives

4. RISK AND RISK MANAGEMENT

Risk is the likelihood of unplanned events that may have both a negative and a positive effect on the pursuit of the strategy or business goals. Risk may have one or several consequences. No organization is protected against risk, thus a proactive (taking action to put risk under control before it manifests) and integrated approach to risk management is necessary in order to achieve the goals set.

Risk management is an integral part of the Company's activities, and it pursues the following objectives in managing risks:

- ▲ to increase the likelihood of achieving the Company's performance objectives;

- ▲ to increase operational efficiency;
- ▲ to raise confidence of the society and the state in the Company;
- ▲ to pre-plan and coordinate the implementation of the actions, which would reduce adverse effect of potential events or the likelihood of their occurrence;
- ▲ to improve safety of employees, third persons and the environment;
- ▲ to improve the prevention and management of unforeseen events;
- ▲ to determine the responsibility of employees involved in the risk management process for specific risks;
- ▲ to ensure effective risk management process in the Company.

The risk management methodology was developed in accordance with the provisions of the international standard COSO ERM (edition of June 2017), the Risk Management Methodology of EPSO-D and internal documents of Amber Grid.

5. IMPLEMENTATION OF THE STRATEGY

In order to carry out the programmes outlined in the strategy, to achieve the objectives set and thus advance in the implementation of the Company's vision and mission, AB Amber Grid continuously assesses and control the progress made in the strategy implementation process. Problem areas of the Company's activities calling for improvement are identified on the basis of the collected information. If new external factors are identified in the assessment process or economic, political, social environment or essential strategy assumptions change, the Company's strategy may be subject to improvement, adjusting the pursued indicator values.

Representative indicators defined for each strategic objective and/or task are used in the

assessment of the implementation of the strategy.

The monitoring of the achieved indicators is performed periodically. In case of any discrepancies, the Company's activities, say, the Company's organisational structure, processes or actions are improved, or new employees are recruited. Where necessary, indicator values are adjusted. Adjustments are made in Company's medium-term plans and, where necessary, in the long-term strategy—the Company seeks to be ambitious, while simultaneously making an objective assessment of changes in its business environment and the market situation.

The monitoring of the strategy is carried out on a systematic and regular basis, and information on monitoring results is used in the Company's management or presented to other stakeholders.