

In spite of the Paris Agreement and the European Union's 2030 greenhouse gas emissions reduction target, Polish state-owned and private companies are pushing on with plans to develop a string of new open-pit lignite mines.

And while local communities on the front line of these potentially destructive projects continue to resist them, many well-known banking names - including some which have recently made encouraging, if belated, moves towards the coal finance exit doors - remain anchored in the Polish coal sector, and appear more than willing to prop up an industry which now appears to be on its last legs.

This guest blog from Kuba Gogolewski of the Polish NGO "Development YES Open-Pit Mines NO" provides the latest lowdown in the wake of Poland's largest power company's recent admission that it is facing a 'challenging 2016' as a result of its coal interests.

Two companies - Zespół Elektrowni Pątnów-Adamów-Konin (ZE PAK) and Polska Grupa Energetyczna (PGE) - dominate the Polish lignite mining market and are currently embarking on securing concessions that could result in the extraction of 7.7 billion tonnes of lignite. This staggering amount is more than has ever been extracted and burned in Poland's history.

With 64 million tonnes of coal - the dirtiest of fossil fuels - mined in Poland in 2014, and as if the nine mines involved were not enough, ZE PAK and PGE have their eyes on opening a further eight or nine mine installations which contain more lignite reserves than in all those mines currently operating. How these dirty aspirations fit with the cuts of 186 million tonnes of CO<sub>2</sub> Poland is expected to make in order to reduce its carbon emissions by 2030 is not clear to anyone.

Moreover, amidst consistent and growing bad news for the coal industry globally, the biggest energy utility in Poland - the state-owned PGE - has just released its financial results for 2015. Due to a one-off lignite assets write-off (the massive Bełchatów and Turów lignite power plant units) of close to PLN 9 billion (EUR 2 billion), PGE registered a net loss of over PLN 3 billion (EUR 680 million) last year. It is now preparing for the worst and forecasting that 2016 will be a tough year given declining wholesale electricity prices and an increase in the amount of CO<sub>2</sub> emission allowances the company needs to buy on the market.

At the same time, the wholesale electricity price in Poland remains 40% higher than in the Czech Republic, Germany or the Scandinavian market. Yet Polish prices are expected to drop as a result of the integration of the EU electricity market alongside pressure from domestic industry, which is at the moment at a disadvantage compared to its competitors in western and northern Europe.

PGE will, however, continue to receive over 19 million CO<sub>2</sub> emission allowances (albeit a drop of 6 million from 2015) in exchange for the modernisations and upgrades the company will have to carry out in order to survive on the market while at the same time falling into line with the EU's environmental and climate legislation. Yet the ongoing uncertainty over the price of CO<sub>2</sub>, combined with the increasing amount of CO<sub>2</sub> that will need to be bought every year up to 2020, increases the negative outlook for the company in the mid- to long-term.

In light of this, it might be reasonable to expect to see a drastic change of course from PGE in order to avoid a fate similar to that experienced by RWE and EON, both of which have suffered major profit squeezes in recent years. Yet, in 2015, PGE ploughed up to PLN 3.05 billion (EUR 693 million), out of its total PLN 9.5 billion (EUR 2.16 billion) CAPEX, into the construction of two new hard coal units at the Opole power plant (each 900 MW) and a new 450 MW lignite unit at the Turów power plant.

At Opole, PGE needs to splash out at least PLN 7.7 billion (EUR 1.75 billion) overall, out of which PLN 3.5 billion (EUR 795 million) CAPEX is planned for 2016 alone, until the units are completed. Meanwhile the shadow of the company's production expansion plans continues to hang over local communities in the Lubuskie Voivodship on the border with Germany, as it pushes on with plans to open up the Gubin-Brody lignite deposit which holds over two billion tonnes of lignite reserves - more than all of the combined reserves of currently operating lignite mines in Poland.

What's more, recent media reports indicate that PGE is planning to develop two further lignite fields in the next ten years. And almost PLN 3.5 billion has been deployed to keep the company's hard coal and lignite units in line with EU legislation. Such hugely expensive measures are only, however, in line with the requirements of the EU's Industrial Emissions Directive, and not with Best Available Technology requirements which will involve an additional modernisation effort in the years to come.

The fightback against the status quo

Energy news from Poland tends to be grimly repetitive - a veto to some climate-related document here, a bitter fight to secure a derogation protection for the national coal industry there. False solutions such as a way out of coal dependence via the development of unconventional fossil fuels development (read fracking) also abound, and of course there are the inevitable - and regular - protests and indignation which accompany every attempt by Brussels or the rest of the member states to bring the European economy in line with what must be done to minimise the destructive impacts of climate change.

Of course PGE is also heavily engaged in lobbying the EU institutions and the Council, both

directly and via the Polish government's unstinting efforts to extend derogations for the Polish energy system and to keep handing out free CO2 emissions allowances beyond 2020. No surprise for a company which generated 57% of its revenues from conventional energy sources in 2015, while producing 70% of its electricity direct from the most emissions-intensive of fossil fuels - lignite (38.98 TWh in 2015) - and 90% of its electricity on the basis of coal and lignite combined.

Nevertheless, this is only part of the story as more and more communities, local authorities and regions in Poland are undertaking various kinds of action to keep the geological lignite reserves permanently in the ground.

As recently as January 25 this year, the regional parliament of Wielkopolska (Greater Poland) Voivodship adopted a resolution to prevent over five billion tonnes of lignite close to Poznan - the Wielkopolska capital of 550,000 inhabitants - and southern Wielkopolska from being extracted. The reasons for this were many, including that the extraction of these reserves would cut off the fresh water delivered to over 70% of Poznan's citizens, not to mention that there is a strong and organised opposition to the plans to resettle thousands and destroy one of the most fertile agricultural lands in Poland simply to satisfy the greed of a small private company such as ZE PAK.

In fact Wielkopolska was not the first region to reject the possibility of extracting short-term profit from what the Polish government is trying to sell as black gold, although it nonetheless leaves behind huge longer-term costs. In February 2013, the Dolnośląskie (Lower Silesia) Voivodship voted in favour of a regional spatial development plan that prohibits the development of lignite with open-pit mining. This followed on from as many as eight 'gminas' (the lowest level of administrative division in Poland) rejecting new open-pit mines in legally binding referenda in 2009. Just last June, the Babiak gmina in Wielkopolska raised the number to nine, and more are likely to follow in the coming years.

International finance still fanning the flames

Meanwhile, there are readily discernible signs that the financial sector is getting the message, finally, about the impact which multi-billion dollar investments can have on the climate. Last year, most notably, the Norwegian Sovereign Wealth Fund took the decision to divest from the most carbon-dependent companies and has already sold all its shares in ZE PAK. Allianz Polska, which manages one of the ten biggest pension funds in Poland in terms of assets, will have fully divested from ZE PAK by the end of May 2016 (it presently holds 2.47% of the company's shares) while ING Bank Śląski Energy sector managing director, Kazimierz Rajczyk, recently announced that project finance for new coal projects in Poland makes no financial sense for any financial institution.

However, as of the end of December last year, the NN OFE pension fund (which is owned by the Dutch insurance giant Nationale-Nederlanden, and is the biggest by far in Poland), was still holding 9.97% of ZE PAK shares and 3.06% of PGE shares. Pension funds are the biggest players on the Warsaw Stock Exchange and have a major influence in determining the direction of the market.

What is really keeping PGE and ZE PAK running, though, are loans, as well as other forms of financial support, from some of the biggest European banks.

Commerzbank's Polish subsidiaries mBank and BRE bank, the Banco Santander subsidiary BZ WBK, Banco Comercial Portugues subsidiary Millenium and the UniCredit subsidiary Bank Pekao S.A. are among the biggest lenders to ZE PAK. However, as of autumn last year, the company remarkably had only a PLN 23 million (EUR 5.2 million) buffer between its short-term loan obligations and cashflow, making it very vulnerable to any unexpected event (for example, the loss of a court case or having to cover a mining related claim from affected parties).

So, not what one could call a secure bet for trusting that the company will manage to resettle thousands of people and recultivate thousands of hectares of land. It should also be noted that the deposit involved in granting the concession for the Tomisławice open-pit mine, which is due to operate until 2030, is PLN 4 million (EUR 0.9 million), barely enough to cover any substantial damages or claims, not to mention the costs of filling the lake which has to cover the pit after the mine closes - indeed, this same lake would need to be filled with water for 23 years.

For PGE, a giant compared to ZE PAK, the situation is very different as the company owns a subsidiary which produces renewable energy and an electricity distribution company which both have no problems in obtaining loans. The European Bank for Reconstruction and Development, the publicly owned multilateral development bank, is currently considering providing PLN 500 million (EUR 113.63 million) for a distribution subsidiary investment program, while another major European public lender, the European Investment Bank, has provided almost PLN 2 billion (EUR 475 million) as recently as October 2015, with a maturity of 2033 or later.

Furthermore, a Nordic Investment Bank investment loan of PLN 597 million (EUR 135.7 million) to finance the construction of the 858 MW power unit at the Bełchatów power plant, and an investment facility of PLN 162 million (EUR 36.8 million) from Nordic Investment Bank and UBS Investment Bank to finance the modernisation of power blocks no. 1-6 at Turów power plant, are both being repaid.

In addition, PGE's distribution subsidiary obtained PLN 76 million (EUR 17.3 million) in the

EU-supported Infrastructure and Environment Operational Programme for the 2007-2013 period. PGE also obtained an investment facility from state-owned Bank Gospodarstwa Krajowego worth PLN 1 billion (EUR 237.5 million) in December 2014, with a maturity date of 31 December 2027, and used PLN 500 million (EUR 113.63 million) of this in 2015. Also, in December last year, PGE concluded a PLN 500 million (EUR 113.6 million) loan agreement with Bank Gospodarstwa Krajowego, with a maturity date of December 31, 2028. As PGE's CEO Marek Woszczyk has boasted, the company obtained PLN 8 billion (EUR 1.8 billion) in new loans in 2015 alone.

And, where the public banks go, of course, private banks follow - en masse.

In September last year, PGE concluded a long-term loan agreement - a term loan facility of up to PLN 3,630 million (EUR 825 million) and a revolving loan facility of up to PLN 1.87 billion (EUR 425 million) - with a syndicate of banks composed of: BNP Paribas, Société Générale, Bank Handlowy w Warszawie (owned by Citi Bank), ING Bank Śląski, Bank Zachodni WBK. (owned by Banco Santander), mBank (owned by Commerzbank), Powszechna Kasa Oszczędności Bank Polski (owned by UniCredit) and Bank Polska Kasa Opieki. The final repayment date of the revolving loan facility falls on April 30, 2019 and the final repayment date of the term loan facility falls on September 30, 2023.

Deeper, under the surface financial support

It's not only through lending that PGE is enjoying significant assistance from the banks - the company's issuing of bonds is also being facilitated by some big names, including ING Bank Śląski S.A. (as Lead Arranger and Issue Agent) as well as ING Bank N.V. (as Programme Underwriter) for a PLN 5 billion (EUR 1.13 billion) bond issue program aimed at Polish capital market investors. The first issue was in June 2013 for PLN 1 billion (EUR 229 million), and the maturity of the bonds is June 27, 2018.

PGE Capital Group, via its 100% owned Swedish subsidiary, has also launched a eurobond programme from which it has recouped EUR 638 million. The total amount underwritten by the arranging banks is for up to EUR 2 billion, with the programme due to end in 2019. The bond issue managers for different issues were BNP Paribas, Bank Pekao (owned by UniCredit), ING Bank Śląski and PKO BP, with bookrunners Bank Pekao and ING Bank Śląski, Citigroup and Société Générale. The maturity of these bonds is 2029.

Big banks need to stop digging themselves deeper holes in Poland

Companies such as PGE or ZE PAK, so deeply tied to hard coal and lignite, and seemingly determined to become only more so, are now a litmus test for major international banks with any pretensions of becoming climate champions.

Project finance for lignite projects already makes no financial sense - and it is now time for

banks such as those mentioned above, who remain very active in the Polish coal sector, to wake up to the fact that providing money in the form of purchasing the corporate bonds of companies which are pursuing new lignite mines, as well as building new coal and/or lignite power plants via, for example, the banks' asset management branches, not only fuels climate change but is also putting short-term profit above long-term fiduciary duty.

The kind of major bank financing for fossil fuel dependent clients in Poland outlined above is squeezing other sectors of the economy which are striving to drive forward and realise a cleaner, more competitive and healthier future. Moreover, the asset management branches of the banks concerned should now be divesting from companies such as PGE and ZE PAK within the next year, stating clearly to the companies why they are doing so and, equally, notifying them that until such time as their investment plans are washed clean of new lignite and hard coal no more loans, no more underwriting, equity investments or any other form of financial assistance or advice will be forthcoming.

Failure to realise and act on the negative climate, environmental and health realities which coal extraction and burning necessarily entails will most likely result in an increasing public outcry aimed at politicians as well as at the banks and fossil fuel companies. Local protests are sprouting all around Poland, and wider trans-European and global anti-coal movements such as Ende Gelände and Break Free are only going to increase the risks and losses for both lignite-dependent companies and banks financially supporting them. And the banks, as they often like to insist, have far more clean investment options than the likes of PGE and ZE PAK do.

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