



Investor's guide to Eurosibenergo (ESE)

Our concerns:

Eurosibenergo(ESE) and Yangtze Power establish joint venture “Yes Energo” to build dams at unnamed locations in Eastern Russia. While they have not disclosed the locations of the proposed projects but hydropower construction in Eastern Russia is high risk. Rivers without Borders is not aware of any environmentally and socially acceptable sites for large hydropower plants close to Sino-Russian border.

Members of Rivers without Boundaries Coalition are concerned with the following:

- increasing threats to lake Baikal
- loss of large free-flowing river ecosystems and surrounding primeval forests;
- negative impacts on indigenous peoples' cultures and livelihoods;
- impacts on rich fish stocks in Eastern Russia on which local residents depend;
- lack of necessary environmental and social safeguards in hydropower planning process: EIA, public hearings, proper protection of historical relics, etc;
- decreasing opportunities for sustainable development for local communities.

We advise IPO Managers that investing in Eurosibenergo is too environmentally, socially and politically risky – and that these hydropower projects must be dropped.

We would like investors to consider the high risks listed below and many uncertainties and not to invest into Eurosibenergo and YesEnergo until companies change their unacceptable environmental and social policies and provide clear and transparent plans for the future which guarantees for proper public involvement.

We also believe that large hydro in Siberia and Fareast is by no means an “sustainable alternative renewable energy source” and in Russia there are many possible yet untapped alternatives in the field of truly green energy: solar, wind, tidal ,etc. We hope that they soon could draw attention of international investors.

IPO background:

Russian oligarch Oleg Deripaska's electricity supplier Eurosibenergo for the second time postponed launch of its US\$1.2 billion Hong Kong initial public offering on Feb 24. The company has been targeting Middle Eastern government funds after lack of enthusiastic response from Chinese investors, though mainland utilities company China Yangtze Power has agreed to buy up toUS\$168 million worth of shares. China Three Gorges

Corporation is the controlling shareholder of China Yangtze Company. Investor confidence has been also affected by Russian Prime Minister Vladimir Putin's call to limit electricity price hikes to 15% annually and cut state investments in hydropower. (Source: [South China Morning Post](#)). Bank of China International, Deutsche Bank AG and Bank VTB OAO have been assigned as global coordinators for the sale. Credit Suisse, Merrill Lynch, RBC, Renaissance Capital were among bookrunners. "EuroSibEnergO" and the "China Yangtze International" (Hong Kong subsidiary company of the "China Yangtze Power") have signed an agreement to form a joint power venture in Russia's Siberia. EuroSibEnergO In the first stage of the new venture –“YES EnergO” will examine two un-named hydropower projects and one thermal project in Ust-Kut (Irkutsk Region) with a total installed capacity of over 3 GW, the said in a statement, adding that the joint venture is aiming at building up to 10 GW of new capacity to feed domestic demand and to create additional capacity for power exports from eastern Russia to China. ESE is wholly owned by EN+ Group, which in turn is part of Basic Element, a conglomerate controlled by Deripaska. Domestically and all over the world Deripaska runs wide-scale propaganda campaign on how to solve China's environmental and Russia's economic development problems through electricity exports.

Meanwhile "EuroSibEnergO" and its parent companies are known for unwillingness and inability to solve serious environmental, social and management problems they are facing.

Key risks:

1. Risks related to EuroSibenergo (ESE) that controls 4 hydropower plants in Siberia having detrimental environmental impacts on internationally recognized and protected freshwater ecosystems of the world:

1.1. According to the [GEF-World Bank](#) Project on Strategy for Lake Baikal Biodiversity Conservation the ESE's Irkutsk Hydro Power Plant (HPP) has had most profound negative effect on Lake Baikal (World Heritage Site) by using it as reservoir with unnatural water regime¹. This has led to increase in erosion, losses in endemic and economically important fish, degradation of unique coastal ecosystems and historic relics, damage to coastal property of local people, conflicts with the Government of Buriatia Republic that receives most of negative impacts. Limits on unnatural water level change is imposed by government and reflected in [State Reports on Baikal Lake](#).

1.2. ESE has undertaken continuous attempts to lobby for greater oscillation of Baikal lake water level oscillation in order to generate more energy at the expense of integrity the world heritage site. (see [Letter of O.Deripaska to the prime minister](#) dated 2009-09-20) Such proposals were presented by company at Baikal Economic Forum in 2008, advocated in newspapers by top managers in 2010, as well as implanted into draft water management plan for Angara River.

1.3. Disastrous ecological condition of Bratsk and Ust-Ilimsk reservoirs formed by EuroSibenergo's plants on Angara River: water polluted by decaying wood (including

¹ Also see monograph. **Hydroelectric power industry and the condition of Lake Baikal's ecosystem**/ A. A. Atutov, N. M. Pronin, A. K. Tulokhonov et al. — Novosibirsk: Publishing House of the SB Russian Academy of Science, 1999. — 280 p.

emission of methane and other greenhouse gases) and wastes of surrounding industry. Downstream of these three dams managing water from the purest lake in the world the water has [very poor quality](#).

1.4. We also see that contribution of large hydropower dams to greenhouse gas emission from reservoirs and other effects leading to climate change are not considered in ESE proposals. Abovementioned hydropower projects have had profound cumulative impacts on climatic features of the Arctic due to changing hydrological and thermal regime of Angara -Yenisey River basin. Biotic exchange between Lake Baikal ecosystem and Arctic Ocean has been also blocked by 3 ESE dams.

1.5. Known impacts of Krasnoyarskaya and other HPPs on local climate, human health and safety in the area. In winter the unnatural iceless stretch of Yenisey River below the dam extends 400 kilometers downstream, causing increase in respiratory deceases in Krasnoyarsk City and deterioration of aquatic and riparian communities.

1.7. Low cost of electricity production at old hydropower stations cited by ESE does not take into account expenditures on solving abovementioned problems and mitigating environmental impacts. Due to new Russian legislation and introduction of international standards these costs may constitute substantial part of hydropower projects.

1.6. EuroSibenergo and Yangtze Power consistently do not disclose at which specific sites they consider to build 10 GW of hydropower plants, which likely indicates very high risks, especially given social and environmental record of two companies and huge risk known at facilities they operate now. We do not know environmentally and socially acceptable sites for large hydropower plants close to Sino-Russian border. For example, in 2010 after two-year campaign by environmental NGOs and indigenous people Rushydro effectively removed from its development plan [Evenkiiskaya HPP](#), which was designed for long-distance transmission of electricity from Yenisey River tributary. Altogether in 1992-2005 altogether more than 30 large hydropower projects in Siberia were frozen and dismissed due to environmental, social and economic reasons. Two power plants being built now are dams, construction of which started in 1970s-80s and thus exempt from many modern requirements.

Disclosure of information on what specific river stretches are considered for future development is necessary prior to any IPO to judge the degree of associated risks and expenditures.

2. EN+Group has a terrible environmental and social track record, which includes RusAl aluminum company, a company that only survives due to cheap electricity generated by ESE.

2.1. Boguchanskaya hydropower dam on Angara River is being built now without Environmental Impact Assessment, not meeting international standards. EBRD initially planned to support this project in its 2006 country strategy, but later never dared to do so due to poor performance of the project. In February 2011 Russian environmental enforcement agency (Rosprirodnadzor) acknowledged that [dam is being built without proper State Assessment and EIA](#).

2.2. Negative effects of growing cascade on Angara River on Lake Baikal World Heritage Site and Angara River ecosystem. The greater is the chain of downstream dams - the stronger is [demand for alteration](#) of Baikal Lake water level. Each new reservoir adds to deterioration of Angara River ecosystems and water quality.

2.3. Boguchanskaya HPP project also known for improper handling of resettlement issues, neglect to preservation and salvation of historic relics, use of prisoners in “partial cleaning of Boguchansky reservoir bottom”, as well as constant feud with major partner “Rushydro” trying to shift to each other major [social and environmental responsibilities](#).

2.4. [Frequent environmental accidents](#) on RusAl facilities, like the one on [Nikolaevsk \(Ukraine\)](#) bauxite processing plant on February 11-26, 2011, where drying red mud pulp generated red dust spreading on many settlements and river valleys. Or on March 1 2011 [environmental ministry of Guinea](#) had threatened to stop operations of Rusal’s aluminum refinery due to chronic heavy pollution.

2.5. Greatest contribution to air pollution and greenhouse gas [emissions by aluminum plants](#) and other production facilities in Siberia. According to 2009 State environmental report all locations of Rusal facilities are on the list of 15 dirtiest cities of Siberia. According to [Green Patrol](#) NGO Rusal is also #1 air polluting company in Russia.

3. The worst environmental and social record belongs to the Basel Group uniting all holdings of Oleg Deripaska:

3.1. Baikalsk pulp and paper plant - the symbol of [destruction of the Baikal Lake](#). In 2011 researchers from [Russian Academy of Science](#) again found most dangerous pollutants - dioxins in bottom sediments adjacent to the plant. Under Basel Group management Baikalsk pulp and paper plant committed many violations of the [environmental norms](#). This evoked country-[wide public protests](#): there have been 20+ [rallies](#) in 10+ [cities all over Russia](#) just within past year with [demands to close](#) Baikalsk pulp and paper plant and punish owners.

3.2. Multiple management failures under Basel leading to bringing the plant to a brink of collapse. Initially Basel was offered substantial international assistance to switch to closed water cycles, but failed to secure it from WB, etc. All retrofitting efforts failed, plant is on the brink of technological collapse (several serious accidents since Jan.2010 including leak of chlorine in 2011), huge debt burden, external management imposed.

3.3. Huge burden of environmental fees and fines are unavoidable due to systemic failure in basic environmental management and CSR([Credit Suisse 2010](#)).

3.4. Extremely poor treatment of workers at Baikalsk mill and other Basel plants in general (massive lay-offs, housing issues, social benefits issues, low salaries, etc). Demonstrations and hunger strikes by workers and laid-off employees like guards of Baikalsky PPP in 2010.

3.5. Extremely [controversial image](#) of Deripaska as manager and policy figure. He has been denied a visa to the U.S. because of State Department concerns about his possible [connections](#) to organized criminal groups. He was declared ‘enemy of Siberia’ by popular on-line vote, publicly punished by the prime-minister for not caring for workers at Pikalevo, etc.

3.6. Last year [Clariden Leu AG](#) advised not to buy Rusal shares due to extremely low environmental responsibility of the Basel as parent to Rusal.

4. Investors risk reputational damage due to poor communication with local communities and public:

4.1. Basel structures are closed for dialogue with civil society. For example, in April 2010 delegation of Chinese NGOs tried to meet with IrkutskEnergo and Baikalsk PPP

and in both cases were denied by Basel managers. This creates extremely negative attitude towards Basel among most active parts of society -NGOs, journalists, politicians, local [businessmen](#).

4.2. [Provocateurs arrested by police](#) at environmental rally in Irkutsk in 2010 were reported to be Basel staff. Also reportedly Basel tried to send [plant workers](#) to confront green activists. This shows poor corporate social responsibility (CSR) and is greatly harming public relations of Basel and all its subsidiaries.

4.3. In 2008-2010 standoff of Rusal and people of Guinea over [environmental](#) and justice issues resulted in [deaths of local](#) protesters, [disruption of operations](#) due to attacks on Rusal facilities, [activist demonstrations](#) in Conakry and Moscow, ever worsening image of Basel-Rusal in Africa and elsewhere as “new colonialist” power.

4.4. Poorly designed propaganda campaign “save world from Chinese climate impacts by producing hydropower in Russia” will result in further public and political opposition to Deripaska activities in Russia, because it neglects real needs of local population of Eastern Russia and is also perceived as colonialism.

5. Investors should be briefed on operational problems and technical risks

5.1. Krasnoyarskaya dam is linked in a cascade with Sayano-Shushesky HPP of Rushydro, where major accident occurred in 2009, which leads to further problems in flood management and limits electricity production. Deep erosion of river bottom occurs immediately below the Krasnoyarskaya dam, etc.

5.2. Highly [questionable tandem of RusAl and ESE](#) (both parts of En+), where ESE has to provide the cheapest possible energy to its aluminum sister-enterprize and therefore ESE often has profits [much lower](#) than its rival Rushydro. Thus in February 2011 Federal anti-monopoly [service \(FAS\)](#) “[established](#) that in 2009 - 2010 the aluminum plants of RUSAL Group used a joint strategy for price bidding which could bring the electricity price being below the production costs of electric power generated by most producers of electric power.”

5.3. Assessment by Bank of China last year notes obvious fact that in foreseeable future there are no technical means to export energy from Angara -Enisey River to China: 1100 km just to Manzhouli at the border ([South China Morning Post](#)). Besides there is competition with Rushydro\ InterRao that uses Bureya and Zeya HPP for such export now.

5.4. Low level of technology and outdated equipment at many facilities (Baikalsk paper mill - prime example). [High accident rate](#) and high risks associated with related fines and payments at many Basel facilities.

6. Governance Problems and Political Risks

6.1. Constant conflict with various state agencies accusing Basel [of financial frauds](#) and other violations (illegality of tolling schemes, unfulfilling obligations to pay for new generation facilities, massive tax evasion, etc)

6.2. Constant wars with business partners and minority share holders (Boguchansky, etc) (this is noted in investment guides in Russia as great risk of Basel-owned companies)

6.3. Lack of state support for liberalization of market prices for electricity. Analyst at brokerage Troika Dialog says “One potential problem is the regulatory uncertainty we still have in the Russian electricity sector.” ([South China Morning Post](#)).

6.4. Due to presently non-transparent and corrupt administrative system of Russia it may seem that many violations go unchecked for years due to inconsistent and biased law implementation. However environmentally destructive projects, such as Sakhalin II and many others, have been challenged in court, and have faced long delays and cost overruns and sometimes even semi-forced change in property ownership.

6.5. Large companies, which as Basel disregard environmental and social welfare in the regions where they work, provoke build-up of protest movements among local people. Personnel and assets of foreign partners of their joint companies would be the first to feel the victim of unleashed anger of local people, since local governments and businesses would like to channel public discontents towards “harmful foreigners”. This tendency already presents the single most obvious obstacle to development of constructive Sino Russian cooperation in Siberia and Far East.

We believe that Eurosibenergo(ESE) and its parents En+ and Basel Group are least likely actors to achieve economic social and environmental benefits they claim in this IPO campaign due to their historical record of inefficiency, low responsibility and poor environmental and social record of participating companies. We want you to consider that risks listed above are significant and that Eurosibenergo has not adequately disclosed all risk to investors.

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