



Q2 report 2004

23 August 2004

DONG A/S

Highlights

- Second quarter 2004 profit after tax of DKK 317 million versus DKK 338 million in the second quarter 2003
 - Half year profit after tax of DKK 1,162 million versus DKK 1,439 million in the same period last year
 - Full-year 2004 profit expectations adjusted upwards to DKK 1.7 billion, partly as a consequence of higher oil prices
 - Second quarter 2004 natural gas sales on a par with the second quarter 2003, despite the opening of the market. Declining sales in Denmark fully offset by increasing exports
 - DONG is pursuing its strategy of acquiring long-term gas reserves and has acquired a 20 per cent stake in the Laggan discovery west of Shetland and, on the Norwegian shelf, a further 10 per cent interest in the Marulk licences and a 15 per cent interest in the Alve discovery
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DONG Group – Financial highlights

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DKK m	Q2 2004	Q2 2003	H1 2004	H1 2003	2003
Revenue	2,881	3,052	7,276	7,821	14,247
EBITDA	1,035	965	2,746	3,195	5,547
EBIT	531	471	1,789	2,144	3,168
Group share of profit for the period	317	338	1,162	1,439	1,941
Cash flows from operating activities	796	1,253	1,180	2,608	4,469
Cash flows from investing activities	(303)	(665)	(358)	(1,070)	(2,926)
Dividend	(1,906)	(440)	(1,906)	(440)	(440)
Change in non-interest-bearing finance	(198)	(69)	105	-	-
Reduction in net interest-bearing debt	(1,611)	79	(979)	1,098	1,103
Total assets	27,282	31,010	27,282	31,010	33,010
Goodwill	74	186	74	186	130
Net interest-bearing debt (net cash)	1,384	2,249	1,384	2,449	2,389
Equity	15,334	16,324	15,334	16,324	16,794
Gross margin	23%	19%	28%	30%	27%
EBIT margin	18%	15%	25%	27%	22%
Return on average invested capital	8%	6%	13%	14%	10%
Return on equity	8%	8%	16%	18%	12%
Equity ratio (excl. recognition of undistributable reserves)	56%	53%	56%	53%	49%
Gearing (net interest-bearing debt/equity)	9%	14%	9%	15%	14%
Number of employees at end of period	1,043	904	1,043	904	1,156

Note: Ratio definitions can be seen from DONG's annual report 2003 and at www.dong.dk

Group profit and expectations for 2004

The DONG Group delivered profit after tax of DKK 319 million for the second quarter of 2004 compared with DKK 339 million for the second quarter of 2003.

The DONG Group's profit is highly sensitive to the price of oil. In the second quarter, the oil price was around USD 7 up on the same quarter last year; however, the impact of higher oil prices was not felt in full due to two factors:

- The oil price and the USD exchange rate are incorporated in DONG's natural gas purchase and sales contracts with different time lags. Oil price changes consequently impact on selling prices relatively quickly, whereas purchase prices are adjusted with a time lag effect of up to 15 months. The increasing oil prices in the first half of 2003 yielded an extraordinary gain that has not been seen to the same extent in 2004.
- A substantial part of DONG's oil and USD exchange rate exposure is hedged, as DONG's risk policy is based on active hedging of the market prices that impact on DONG's earnings. As part of its risk policy, DONG actively manages market risks up to five years ahead by concluding financial hedging contracts with a view to securing stable results and cash flows. The oil and USD exchange rate hedging had an adverse impact on profit for the second quarter as a consequence of the oil price having been hedged below the existing price level. This impact was only partially offset by the favourable effect of USD exchange rate hedging.

Group profit for the first half of 2004 was DKK 1,162 million (2003: DKK 1,439 million). The significantly better performance for the first half of 2003 was due, to a great extent, to the time lag effect referred to above, which was particularly high in the first quarter of 2003, when oil prices rose considerably due to the Iraq war.

The Group delivered revenue of DKK 2,881 million for the second quarter of 2004 compared with DKK 3,052 million for the corresponding period in 2003. The decline compared with 2003 primarily reflected the impact of hedging transactions referred to above and the fact that DONG Transmission (now: GASTRA A/S) was transferred to the Danish State on 1 January 2004 and is consequently no longer included in DONG's revenue.

DONG's equity at 30 June 2004 was about DKK 1 billion lower than at 30 June 2003, despite a net profit of about DKK 1.7 billion for the period. Besides ordinary dividend, the reduction was due to extraordinary dividend being paid in connection with the State's acquisition of DONG Transmission, and the adverse impact of hedging transactions.

DONG's assets were about DKK 3.7 billion lower than at 30 June 2003, mainly due to a reduction in property, plant and equipment in connection with the transfer of DONG Transmission to the State.

Expectations for 2004

The full-year profit expectations for 2004 are adjusted upwards, primarily as a consequence of higher oil prices and the time lag effect resulting from rising oil prices.

Overall, full-year post-tax profit of around DKK 1.7 billion is anticipated for 2004, up DKK 400 million on the DKK 1.3 billion profit forecast in the Q1 2004 announcement.

Special factors

➤ Privatisation of DONG

In June, the Danish Ministry of Finance published a study of privatisation alternatives for DONG. The study was commissioned in January 2004 and was prepared by the investment bank N M Rothschild & Sons.

The purpose of the study was to identify possible privatisation options. The study also reviews advantages and drawbacks of the various privatisation methods viewed in conjunction with the important social considerations associated with DONG's activities.

Finance Minister Thor Pedersen stated in connection with the publication of the report that "the study provides us with a good basis for deciding on the State's future ownership of DONG" and that "the Government is of the view that an IPO in connection with a sale to a broad range of owners could be an appropriate privatisation model."

DONG is preparing for such a flotation.

➤ Divestment of EnergiGruppen Jylland's grid activities and acquisition of shares in EnergiMidt A/S

In June, EnergiMidt, Herning Municipality, EnergiGruppen Jylland and DONG entered into various agreements, including the following:

- DONG will acquire an approximately 77 per cent shareholding in EnergiMidt A/S. EnergiMidt A/S is the indirect owner of a 8.86 per cent shareholding in Elsam. EnergiMidt Holding will retain the remaining 23 per cent in EnergiMidt A/S.

- EnergiMidt Holding will acquire EnergiGruppen Jylland's electricity and service activities with about 37,000 customers in the Herning area and about 67 employees.

Post-balance sheet events

➤ Signing of turnkey contract - Barrow Offshore Wind Ltd

In July, Barrow Offshore Wind Ltd (BOW), which is owned jointly with UK-based Centrica, entered into a turnkey contract for the construction of Barrow Offshore Wind Farm in the East Irish Sea off Barrow-in-Furness on the UK west coast.

The turnkey contractor is a consortium comprising the engineering company Kellogg Brown & Root and the wind turbine manufacturer Vestas. Barrow Offshore Wind Farm will consist of 30 Vestas V90 wind turbines with an installed capacity of 90 MW, sufficient to supply electricity to about 75,000 households. Construction will commence in late spring 2005 and is scheduled for completion by November 2005.

DONG, Centrica and Norwegian Statkraft acquired the shares in BOW in 2003. Statkraft has subsequently decided to sell its BOW shares to DONG and Centrica, taking DONG's ownership interest in BOW from 37.5 per cent to 50 per cent. However, Statkraft has an option to buy back the shares sold to DONG and Centrica at a later point in time, within an agreed framework.

DONG's business areas

Exploration and production activities

DONG's oil and gas exploration and production take place on the Danish, Norwegian, UK, Greenland and Faroese continental shelves. DONG E&P showed EBIT of DKK 216 million (2003: DKK 199 million) for the second quarter and profit after tax of DKK 86 million (2003: DKK 16 million). The improvement in earnings after tax was due to the fact that a relatively larger proportion of earnings came from Denmark than in the same quarter last year.

Revenue amounted to DKK 729 million versus DKK 816 million in the second quarter last year. Second quarter production was 4.7 million boe (barrels of oil equivalent), slightly up on the production in the second quarter of 2003. Danish fields accounted for around 65 per cent of production and Norwegian fields for the remaining 35 per cent. The lower revenue was due to the adverse impact of financial hedging transactions compared with the same period last year.

Total investment expenditure on exploration and production amounted to DKK 176 million in the second quarter, related mainly to development activities on the Syd Arne, Siri and Nini/Cecilie fields in the North Sea.

YTD profit after tax was DKK 227 million (2003: DKK 74 million). The earnings improvement was due to a lower level of activity on the exploration front, and the fact that a relatively larger proportion of earnings came from Denmark.

DONG and ConocoPhillips have entered into a deal under which DONG will take over ConocoPhillips' shares in the UK licences P.911, P.912 and P.967 and the Faroese licence F003. At the same time ConocoPhillips will take over part of DONG's share in the Norwegian licence PL273. The deal will give DONG a share in several gas finds, including 20 per cent of the Laggan find north-west of the Shetland Islands, where an appraisal well has just been completed. All the licences are located in an area in which DONG already has substantial interests.

On the Norwegian shelf, DONG and ExxonMobil have signed an agreement under which DONG will acquire ExxonMobil's 10 per cent stake in the Norwegian PL122 and PL122B licences with the Marulk gas find. The licences will subsequently be owned by Statoil (50 per cent), DONG (30 per cent) and the operator Eni Norge (20 per cent). Last year, DONG acquired Amerada Hess' 20 per cent share in the licences.

In addition, DONG has acquired 15 per cent of the Alve gas find from Shell, located in licence PL159 in Mid-Norway (the deal is awaiting approval by the Norwegian authorities). Furthermore, DONG has been awarded five exploration licences by the Norwegian authorities.

Natural gas trading

DONG's natural gas trading activities generated second quarter EBIT of DKK 280 million (Q2 2003: DKK 160 million) and profit after tax of DKK 204 million (Q2 2003: DKK 137 million). First half 2004 EBIT was DKK 917 million (H1 2003: DKK 1,243 million), and profit after tax was DKK 655 million (H1 2003: DKK 890 million).

The higher profit in the second quarter of 2004 compared with the same period in 2003 was primarily due to the fact that the oil price was on average USD 7/barrel higher than in the second quarter of 2003. A lower USD exchange rate had the opposite effect.

Natural gas sales in the second quarter of 2004 totalled 1,410 million m³, including 748 million m³ for export. Sales for the same period in 2003 amounted to 1,402 million m³, including 583 million m³ for export. Natural gas sales for the first half year amounted to 3,685 million m³, including 1,641¹ million m³ for export, compared with 3,908 million m³ for the first half of 2003, including 1,616 million m³ for export.

DONG's business areas

Loss of market share was the main driver behind the declining sales in the Danish market in the first half of 2004, particularly the loss of several large accounts, including the regional company Naturgas Fyn. Conversely, DONG has won around 30 per cent of the Funen market as direct end customers. Until the market opening, DONG supplied all Danish customers directly or indirectly. It is therefore natural and unavoidable for DONG to experience some loss of market share in the Danish market.

The loss of market share in Denmark is expected to be more than offset by the growth in exports. A volume decline caused by renegotiation of large contracts was more than offset by new contracts with end customers in Sweden, Germany and the Netherlands. The effect of some of these new contracts will be felt in the third quarter of 2004 as the natural gas pipeline from the Tyra field to the Dutch Nogat pipeline is completed.

Overall, DONG anticipates higher natural gas sales in 2004 than in 2003.

Distribution and Storage activities

DONG's gas distribution and gas storage activities are taken care of by the two companies DONG Distribution and DONG Lager. These companies delivered a second quarter EBIT loss of DKK 15 million (2003: DKK 1 million loss) and a profit of DKK 25 million (2003: DKK 31 million), respectively, and a post-tax loss of DKK 18 million (2003: DKK 35 million loss) and a profit of DKK 13 million (2003: DKK 6 million loss), respectively. Second quarter 2004 revenue was DKK 82 million (2003: DKK 94 million) and DKK 88 million (2003: DKK 95 million). The lower revenue generated by Distribution for the second quarter was due to a restructuring of the tariff structure that will not, however, have any impact on full-year profit.

The terms for gas storage are negotiated individually on the basis of standard storage packages, while fixed tariffs have been set for standard services in the distribution network. The Danish Energy Regulatory Authority monitors that the terms for utilisation of storage facilities and distribution are fair and non-discriminatory and are open to all.

Renewable energy activities

DONG's renewable energy activities are undertaken by DONG VE, which today has energy production in Denmark, with an installed capacity of 71 MW from wind turbines and 7 MW from geothermal sources.

DONG's renewable energy activities showed EBIT of DKK 7 million in the second quarter of 2004 (2003: DKK 1 million loss) and profit after tax of DKK 2 million (2003: DKK 1 million loss) on total revenue of DKK 28 million (2003: DKK 9 million).

Electricity activities

At the beginning of 2003, DONG acquired 65.6 per cent of EnergiGruppen Jylland. EnergiGruppen Jylland consists of six underlying operating companies. Three of these cover the supply areas electricity, water and heat, while two are production companies with production based on waste incineration and biogas, respectively, and the last one is a service company.

EnergiGruppen Jylland posted EBIT of DKK 13 million in the second quarter of 2004, matching expectations.

The Group in figures

Income statement & Balance sheet

DONG Group

Q2 report 2004

DKKm	Q2 2004	Q2 2003	H1 2004	H1 2003	2003
Income statement					
Domestic sales	1,478	1,658	4,005	4,487	8,010
Export sales	1,403	1,394	3,271	3,334	6,237
Revenue	2,881	3,052	7,276	7,821	14,247
Export share (per cent)	49	46	45	40	44
Gross profit	660	597	2,059	2,391	3,811
Sales and marketing	(41)	(15)	(87)	(44)	(240)
Management and administration	(62)	(81)	(130)	(143)	(295)
Other operating income and expenses	2	(2)	(3)	(4)	(4)
Profit before goodwill amortisation	559	499	1,845	2,200	3,280
Goodwill amortisation	(28)	(28)	(56)	(56)	(112)
Operating profit (EBIT)	531	471	1,789	2,144	3,168
Share of pre-tax profits (losses) of associates	(2)	2	5	14	24
Financial income and expenses, net	16	94	196	178	56
Profit before tax for the period	545	567	1,989	2,336	3,248
Tax on profit for the period	(226)	(228)	(756)	(896)	(1,299)
Profit for the period	319	339	1,233	1,440	1,949
Minority interests' share of profit for the period	(2)	(1)	(71)	(1)	(7)
Group share of profit for the period	317	338	1,162	1,439	1,941
Dividend	0	0	0	0	1,906

Balance sheet

Goodwill	74	186	130
Other intangible assets	290	132	259
Property, plant and equipment	17,252	21,098	22,096
Investments	3,177	1,957	2,172
Current assets	6,489	7,637	8,353
Total assets	27,282	31,010	33,010
Share capital	2,144	2,144	2,144
Revaluation reserve	1,960	5,168	5,168
Undistributable reserves in regulated companies	663	648	663
Retained earnings	10,567	8,364	6,913
Proposed dividend	0	0	1,906
Equity	15,334	16,324	16,794
Minority interests	638	591	564
Long-term liabilities including provisions	6,798	8,439	9,224
Short-term liabilities other than provisions	4,511	5,656	6,428
Total equity and liabilities	27,282	31,010	33,010

The Group in figures, continued

Notes					
DONG Group					
Q2 report 2004					
DKKm	Q2 2004	Q2 2003	H1 2004	H1 2003	2003
Statement of changes in equity					
Equity at start of year	17,218	15,813	16,794	14,655	14,655
Group share of profit for the period	317	338	1,162	1,439	1,933
Value adjustment of hedging instruments	(435)	(4)	(1,032)	167	133
Foreign exchange adjustments	2	(30)	(1)	(93)	(104)
Addition of undistributable reserves in regulated companies on acquisition	0	648	0	648	655
Transfer to undistributable reserves in regulated companies	0	0	0	0	8
Tax on equity items	131	1	310	(50)	(40)
Other adjustments	7	(2)	7	(2)	(6)
Dividends paid	(1,906)	(440)	(1,906)	(440)	(440)
Equity at end of period	15,334	16,324	15,334	16,324	16,794
Cash and cash equivalents					
Cash and cash equivalents at start of year	3,438	4,207	3,610	3,655	3,655
Cash flows from operating activities	796	1,253	1,180	2,608	4,469
Sale of subsidiaries	1,130	0	1,430	0	0
Cash flows from other investing activities	(1,433)	(665)	(1,788)	(1,070)	(2,926)
Dividends paid	(1,906)	(440)	(1,906)	(440)	(440)
Cash flows from other financing activities	(262)	(944)	(763)	(1,342)	(1,148)
Change in cash and cash equivalents	(1,675)	(796)	(1,847)	(244)	(45)
Cash and cash equivalents at end of period	1,763	3,411	1,763	3,411	3,610
Volumes					
Natural gas sales (million m³):					
Domestic	662	819	2,044	2,292	4,052
Exports	748	583	1,641	1,616	2,999
Total natural gas sales	1,410	1,402	3,685	3,908	7,051
Production of crude oil and natural gas:					
Production of crude oil and natural gas (million boe/oil equiv):	4.7	4.4	9.6	9.4	18.8