MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

June 30, 2019 and 2018

ORAZUL ENERGY PERU S.A. AND SUBSIDIARIES

US$550,000,000 – 5.625% Senior Notes due 2027

ORAZUL ENERGY PERU AND SUBSIDIARIES S.A.

About the Company

We are a Peruvian company and our business is composed of a diversified portfolio of hydropower and thermal power generation, transmission and natural gas production and processing assets. We are the only vertically integrated power company that owns and operates natural gas extraction and transmission assets in Peru.

We conduct our operations through two primary business units: Orazul, which is comprised of hydropower generation and transmission assets, and Aguaytia, which is an integrated gas-to-power complex comprised of natural gas production and processing, thermal power generation and transmission. We generate and sell electricity to regulated customers (distribution companies) and non-regulated customers under short-term and long-term power purchase agreements ("PPAs") and to the spot market. Our contracting level under PPAs is approximately 84%[1] and in 2018 we extended our PPA portfolio average life from 4 years to approximately 10 years, reducing the risk related to the fluctuation of spot market prices of electricity.

Our businesses are summarized in the following table:

	Entity	Location	Type	Overview
Orazul	Orazul	Cañon del Pato	Hydro Generation/ Run-of-river	255MW
		Carhuaquero	Hydro Generation/ Run-of-river	110MW
	Etenorte	Huallanca - Chimbote - Carhuaquero - Chiclayo	Transmission	349km
	Entity	**Location**	**Type**	**Overview**
Aguaytía	Termoselva	Aguaytía	Thermal Generation (natural gas)	192MW
	Eteselva	Aguaytía - Tingo Maria - Vizcarra - Conocoha - Paramonga	Transmission	391km
	Aguaytía Energy del Perú	Aguaytía	Hydrocarbons	45 mmscfd 1,050 bbls/day

Orazul Energy Perú S.A. ("OEP") is a subsidiary of Orazul Energia (UK) Holdings LTD. OEP was incorporated in Peru on October 10, 2016 and on December 20, 2016, acquired, from Duke Energy Corporation, 87.23% of Orazul Energy Group S.A.C. (formerly Duke Energy International Group), which owned a group of companies in Peru, Chile, Guatemala and El Salvador engaged primarily in power generation. On August 2, 2017, OEP acquired an additional 12.76% of Orazul Energy Group S.A.C. from Orazul Energía (España) Holding S.R.L. (which had previously acquired the participation from Duke Energy Corporation in 2016), increasing its share to the current 99.99%. On August 16, 2017, OEP merged by absorption with Orazul Energy Egenor S. en C. por A., one of its main subsidiaries in Peru. As part of the strategy to improve business efficiencies, a corporate restructuring was executed during 2017 and 2018, and the businesses located in Chile, Guatemala and El Salvador were carved-out.

[1] Estimated contracting level from 2019 to 2021.

OEP is indirectly owned by certain funds managed by I Squared Capital Advisors (US) LLC (the “Sponsor”). On December 31, 2017, the Sponsor through Nautilus Inkia Holdings LLC (“Inkia”), acquired substantially all the Latin American and Caribbean business held by Inkia Energy Limited, an international company focused on the electric power sector, specifically on generation and distribution, with operations in Peru and other countries in Latin America. On April 30, 2018, the Instituto Nacional de Defensa de la Competencia y de la Protección de la Propiedad Intelectual, INDECOPI, the Peruvian antitrust authority, approved the acquisition by the Sponsor. Since then, the related parties of OEP include Kallpa Generación S.A. (“Kallpa”) and Samay I S.A.. Since January 1, 2019, as part of a strategy to optimize operations and maximize benefits from having the same shareholders, Kallpa and OEP have integrated and streamlined their management teams, implementing a single management organization, with no legal mergers between the companies.

Management has extensive experience in the power generation business. Our executive officers have an average of approximately 15 years of experience in the power generation industry and have previously held senior positions in leading power generation companies, financial institutions and the Peruvian government. Our management team provides in-depth market knowledge and power industry experience, with significant experience in the Peruvian energy industry and government regulators. We believe that this overall level of experience allows our management team to lead the Company in the effective operation and maintenance of our facilities.

Our Notes

On April 25, 2017, OEP issued senior notes for an aggregate principal amount of US$550 million in the international capital markets under Rule 144A and Regulation S of the Securities Market Law of the United States of America (the “Notes”). These Notes accrue interest at a rate of 5.625% payable semi-annually and have final maturity in April 2027. The proceeds from this issuance were used to: i) prepay the outstanding senior debt incurred in connection with our acquisition under the US$450 million senior secured loan facility with Deutsche Bank AG, Banco de Crédito del Perú, Scotiabank and Banco Internacional del Perú S.A.A., as lenders, and (ii) prepay US$35 million and US$40 million, in aggregate outstanding principal amount of local corporate bonds. The Notes are rated BB by Fitch Ratings and Standard & Poor’s.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITIONS AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with our Unaudited Condensed Consolidated Interim Financial Statements as of June 30, 2019 and 2018.

For the six-month period ended June 30, 2019 and 2018

	Six months ended June 30		*% Change*
In millions of U.S. dollars	**2019**	**2018**	
Revenues of energy, capacity and transmission	70	69	*1%*
Revenues of hydrocarbons	9	14	*-36%*
Revenues	**79**	**83**	***-5%***
Cost of Sales of energy, capacity and transmission	(14)	(17)	*-18%*
Cost of Sales of hydrocarbons	(4)	(7)	*-43%*
Cost of sales (excluding depreciation)	**(18)**	**(24)**	***-25%***
Depreciation	(17)	(22)	*-23%*
Administrative expenses	(6)	(9)	*-33%*
Other income, net	1	(1)	*-200%*
Operating profit	**39**	**27**	***44%***
Finance income	1	1	*0%*
Financial cost	(20)	(23)	*-13%*
Net foreign exchange difference	-	-	-
Finance cost, net	**(19)**	**(22)**	***-14%***
Profit before income tax	**20**	**5**	***300%***
Income tax expense (benefit)	(9)	2	*-550%*
Profit from continuing operations	**11**	**7**	***57%***
Net profit for the period from discontinued operations	-	1	-
Profit for the period	**11**	**8**	***38%***

Results of Operations

The Company's net profit from continuing operations for the six-month period ended June 30, 2019 amounted to US$11 million compared to US$7 million during the same period in 2018. The Company's results were mainly explained by the following:

Revenues

Sales of energy, capacity, transmission and hydrocarbons declined by US$4 million, or 5%, to US$79 million during the first six months of 2019 from US$83 million during the same period in 2018, primarily due to:

(i) US$5 million lower liquids sales, or 36%, mainly in natural gasoline, due to 32% lower liquids production from 148,211 bbl during the six-month period ended June 30, 2019 compared to 216,784 bbl during the same period in 2018 related to the unavailability in one of our wells, and a 6% reduction in natural gasoline price, from US$60/bbl during the six-month period ended June 30, 2019 compared to US$64/bbl in the same period in 2018 related to lower international prices; and,

(ii) US$2 million lower spot energy revenues primarily due to a 33% decrease in spot prices, from US$7.3/MWh during the six-month period ended June 30, 2019 compared to US$10.9/MWh during the same period in 2018. This was partially offset by a 3% increase in net volumes, 474 GWh during the six-month period ended June 30, 2019 compared to 461 GWh in the same period in 2018.

These effects were partially offset by:

(iii) US$3 million higher capacity sales under PPAs in connection with the Take or Pay clause with regulated customers.

Cost of sales (excluding depreciation)

Cost of sales decreased by US$6 million, or 25%, to US$18 million during the first six months of 2019 from US$24 million during the same period in 2018, primarily due to (i) US$3 million lower cost of royalties, storage and transport of natural gasoline and LPG (liquefied petroleum gas) related to lower sales in connection with lower production; and, (ii) US$3 million decrease in personnel expenses due to the management integration process between Kallpa and OEP which started in January 2019.

Depreciation and amortization

Depreciation and amortization decreased by US$5 million, or 23% to US$17 million during the first six months of 2019 from US$22 million during the same period in 2018, due to the write-off and end of the useful life of certain assets.

Administrative expenses

Administrative expenses decreased by US$3 million, or 33% to US$6 million during the first six months of 2019 from US$9 million during the same period in 2018, primarily due to a decrease in personnel expenses related to the management integration process between Kallpa and OEP which started in January 2019, added to additional synergies as lower legal services and headquarter fees.

Other income, net

Other income, net amounted to US$1 million income during the first six months of 2019 compared to US$1 million expense in during same period in 2018 mainly due to services rendered by Cañon del Pato’s maintenance workshop, added to income from an insurance recovery related to a previous year incident.

Financial expenses, net

Financial expenses, net decreased by US$3 million, or 14% to US$19 million during the first six months of 2019 from US$22 million during the same period in 2018, primarily due to (i) US$2 million lower interest due to the reduction in the interest rate of our shareholder loan to zero since January 2019; and, (ii) US$1 million lower withholding taxes related to loans with related parties.

Income tax expense

Income tax expense increased by US$11 million to US$9 million during the first six months of 2019 from US$2 million income during the same period in 2018; primarily due to higher exchange gains in local currency during 2019, 2.6% local currency appreciation as of June 30,2019 compared to 0.8% devaluation in the same period in 2018.

Liquidity and Capital Resources

Our main cash requirements are primarily for the following purposes:

- Working capital requirements;
- Capital expenditures related to maintenance projects; and,
- Debt and interest service.

Our main sources of liquidity have traditionally consisted of the following:

- Cash flow from operating activities; and,
- Short-term under our US$25 million committed credit facilities and long-term borrowings.

During 2019 and 2018, cash flow generated by operations was primarily used for working capital requirements, investment activities and to service our outstanding interest and debt obligations.

As of June 30, 2019, our cash and cash equivalents amounted to US$66 million.

Cash Flows

	Six-month ended		**%**
In millions of U.S. dollars	**2019**	**2018**	
Cash from operating activities	**43**	**44**	**-2%**
Income tax paid	(2)	(7)	-71%
Net cash from operating activities	**41**	**37**	**11%**
Net cash used in investing activities	**(9)**	**(3)**	**200%**
Net cash used in financing activities	**(16)**	**(33)**	**-52%**
Net increase in cash	**16**	**1**	**1500%**
Cash and cash equivalent as of January 1	50	23	117%
Effects of variations on exchange difference on held cash	-	-	-
Cash as of June 30	**66**	**24**	**175%**

Cash Flows from Operating Activities

Our main source of operating funds corresponds to cash flow generated from our operations. Net cash provided by operating activities increased by 11% to US$41 million during the first six months of 2019 from US$37 million during the same period 2018.

The increase was primarily driven by: (i) US$6 million due to lower personnel expenses related to the management integration process between Kallpa and Orazul, (ii) US$6 million in lower third-party purchases added to improved terms in accounts payable to suppliers of goods and services, (iii) US$4 million in lower income tax payments due to application of prior year tax credit, added to higher taxable income from 2017, paid in 2018; and, (iv) US$2 million lower royalties mainly due to lower natural gasoline and LPG sales. These effects were partially offset by (i) US$8 million in lower collections from natural gasoline sales due to the lower natural gasoline and LPG sales and the higher collections in the first months of 2018 which included an outstanding balance from 2017, and; (ii) US$6 million in lower energy sales in the spot market due to a decrease in spot price.

Cash Flows Used in Investing Activities

Net cash used in investing activities increased in US$6 million to US$9 million during the first six months of 2019 from US$3 million used during the same period in 2018.

During the first six months of 2019, cash from investing activities was mainly used in payments for US$6 million related to the compensation paid to the distribution companies under the option agreements to extend certain PPAs term, and US$3 million in capital expenditures.

During the first six months of 2018, cash from investing activities was mainly used in US$4 million capital expenditures, partially offset by US$1 million dividends received from a Chilean subsidiary.

Cash Flows from Financing Activities

Net cash flows used in our financing activities decreased by 52% to US$16 million during the first six months of 2019 from US$33 million during the same period in 2018.

During the first six months of 2019, we used cash to pay US$16 million in interest related to the 2027 Senior Notes.

During the first six months of 2018, we used cash (i) in a US$17 million capital reduction; and, (ii) to pay US$16 million in interest related to the 2027 Senior Notes.

For the three-month period ended June 30, 2019 and 2018

	Three-month ended June 30		% Change
In millions of U.S. dollars	**2019**	**2018**	
Revenues of energy, capacity and transmission	35	33	*6%*
Revenues of hydrocarbons	5	8	*-38%*
Revenues	**40**	**41**	***-2%***
Cost of Sales of energy, capacity and transmission	(7)	(9)	*-22%*
Cost of Sales of hydrocarbons	(2)	(4)	*-50%*
Cost of sales (excluding depreciation)	**(9)**	**(13)**	***-31%***
Depreciation	(8)	(10)	*-20%*
Administrative expenses	(3)	(4)	*-25%*
Other income, net	-	(1)	*-100%*
Operating profit	**20**	**13**	***54%***
Finance income	1	-	-
Financial cost	(11)	(11)	*0%*
Finance cost, net	**(10)**	**(11)**	***-9%***
Profit before income tax	**10**	**2**	***400%***
Income tax expense (benefit)	(3)	3	*-200%*
Profit from continuing operations	**7**	**5**	***40%***
Net profit for the period from discontinued operations	-	-	-
Profit for the period	**7**	**5**	***40%***

Results of Operations

The Company's profit from continuing operations for the three-month period ended June 30, 2019 amounted to US$7 million compared to US$5 million during the same period in 2018. The Company's results were mainly explained by the following:

Revenues

Sales of energy, capacity, transmission and hydrocarbons declined by US$1 million, or 2%, to US$40 million during the second quarter of 2019 from US$41 million during the same period in 2018, primarily due to US$3 million lower liquids sales, mainly due to lower production, from 108,355 bbl in the second quarter of 2018 to 68,562 bbl in the same period of 2019, related to the unavailability of one of our wells. This was partially offset by an increase in spot energy sales due to higher spot prices, US$8.2/MWh during the second quarter of 2019 compared to US$7.9/MWh in the same period in 2018, coupled with slightly higher volumes.

Cost of Sales

Cost of sales decreased by US$4 million, or 31%, to US$9 million during the second quarter of 2019 from US$13 million during the same period in 2018, primarily due to (i) US$2 million lower cost of royalties, storage and transport of natural gasoline and LPG related to lower sales in connection with lower production; and, (ii) US$2 million decrease in personnel expenses due to the management integration process between Kallpa and OEP which started in January 2019.

Depreciation and amortization

Depreciation and amortization decreased by US$2 million, or 20% to US$8 million during the second quarter of 2019 from US$10 million during the same period in 2018, due to write off and the ending of the useful life of certain assets.

Administrative Expenses

Administrative expenses decreased by US$1 million, or 25% to US$3 million during the second quarter of 2019 from US$4 million during the same period in 2018, primarily due to a decrease in personnel expenses related to the management integration process between Kallpa and OEP which started in January 2019, added to additional synergies related to lower legal services and headquarter fees.

Financial expenses, net

Financial expenses, net decreased by US$1 million, or 9% to US$10 million during the second quarter of 2019 from US$11 million during the same period in 2018, primarily due to lower interest in connection with the reduction in the interest rate of our shareholder loan to zero since January 2019: coupled with higher financial income from available funds in cash accounts.

Income tax expense

Income tax expense increased by US$6 million to US$3 million during the second quarter of 2019 from US$3 million income during the same period in 2018; primarily due to higher exchange gains in local currency during 2019.

Appendixes

EBITDA & Adjusted EBITDA reconciliation

	Six months ended June 30,		Three months ended June 30,	
In millions of U.S.	**2019**	**2018**	**2019**	**2018**
Profit from continuing operations	**11**	**7**	**7**	**5**
(+) Income tax and profit sharing	9	(2)	3	(3)
(+) Financial expense, net	19	22	10	11
(+) Depreciation and amortization[2]	18	22	9	10
Total EBITDA	**57**	**49**	**29**	**23**
(+/-) Non-recurring expenses, net	-	3	-	3
Total Adjusted EBITDA	**57**	**52**	**29**	**26**

Material Indebtedness

In millions of U.S. dollars	**Outstanding Principal Amount as of June 30, 2019**	**Interest Rate**	**Final Maturity**	**Amortization**
Long-term debt:				
Unsecured:				
5.625% Notes due 2027	541	5.625%	April 2027	Principal due at maturity with semi-annual interest payments.
Total	**US$541**			

Note: *values net of transaction costs*

Subsequent events

On July 30, 2019, OEP amortized US$20 million of the shareholder loan granted by Orazul Energia Partners LLC. The outstanding amount of the loan as of the date of issuance of this report amounted to US$108 million.

[2] Includes depreciation classified as Administrative expenses in our consolidated financial statements.