SARAS

Second Quarter 2009 Results
7 August 2009

Welcome

Massimo Vacca

Head of Investor Relations

Ladies and gentlemen, good evening, welcome to Saras conference call on the second quarter 2009 results. Today we have the usual agenda. We will start with Mr Dario Scaffardi, General Manager, who will give a market overview and discuss the highlights of the quarter. We will then move to Mr Corrado Costanzo, CFO who will go in a detailed review of the various segments and subsequently discuss the group financials. Afterwards we go back to Mr Scaffardi for the outlook and strategy and finally we will take your questions. Dario, please you may start.

Dario Scaffardi

General Manager, SARAS

I. Highlights

Thanks you Massimo. I would like to start the call by remembering Daniele Melis, Bruno Muntoni and Luigi Solinas who tragically lost their lives on May 26th while they were performing routine maintenance on one of our conversion units. Safety has always been a top priority for Saras and this very, very sad event has hit us unexpectedly but it will push us to further focus on safety and further invest in this field, which is absolutely a top priority for us.

The highlights of the quarter are basically a very sharp rise in the crude oil price, sluggish oil product demand. All this has equated into relatively thin base margins, which in the case of Saras has been further compounded by the fact that in Q2 we have performed a large upgrading and maintenance programme on our units.

We will go towards the end of the call into more detail on what exactly has been done and the impact both negative and positive of this on our accounts. Overall the net results are that we have some relatively modest group results on a comparable basis.

Market Overview

1. Diesel and Gasoline Crack Spreads

The market is, in a way, surprising. We have had relatively strong gasoline cracks compared to last year when they were actually negative. In this quarter they hovered around 10 dollars per barrel and instead we've had some very negative cracks on diesel basically due to the fact that diesel is the first product effected in an economic recession since it most closely reflects the economy. Runs have been lowered therefore there has been comparably less gasoline available on the market, which has contributed to the relative strength of gasoline compared to diesel. Another negative factor has been the very high price of fuel oil compared to diesel, which has negatively affected conversion margins, which are paramount to the system, like Saras, which is closely linked to the conversion spread.

2. Refining and Power Margin

These overall affects both of the market and of our scheduled maintenance have had a negative impact on our margins, as you can see in the Q2 results where our overall margin has been 1.4 dollars per barrel compared to an EMC benchmark of 1, adding only 40 cents on top of this. Whilst considering the market, if we had all the plans available we would have been able to add something in the range of 2.5 to 3 dollars per barrel so overall we would have had a margin in the quarter of something in the range of 3 to 4 dollars which compares to more than 11 dollars in the same quarter of last year. The Delta between this is all attributable to the market. I would like to hand on to Corrado who will go into detail on the various sectors.

Corrado Costanzo

CFO, SARAS

I. Segment Reviews

I. Refining

Thank you Dario. Let's start, as usual, with the refining sector. As you can see crude runs were sharply lower, down 28% vis-à-vis the same quarter of last year. This again is attributable to this major upgrade and maintenance programme that was carried out during the quarter. We estimate that the loss of conversion capacity was basically worth at least $40m and there was also a certain impact coming from the tragic incident that involved the three contractor workers. So, overall, a negative EBITDA, which could be expected given the market scenario and the maintenance programme. The exchange rate was higher than last year during the second quarter but didn't really add much to our results for obvious reasons.

Production

Let's take a look at product yields for the quarter. They're clearly completely out of the usual range and it's probably not even worth going into any detail, because again everybody can understand that these product yields and, to an extent, the crude oil slate were strictly linked to this exceptional period for us. So we will go back to normal starting from Q3.

Fixed and Variable Costs

A quick look at Fixed and Variable costs. Fixed costs are broadly in line, a little bit better if anything, with our guidance. The reason being that a substantial part of the costs incurred in connection with this turnaround and maintenance programme are capitalised. They're either straightforward investments or long-term maintenance, which for accounting and tax purposes have to be capitalised. So, overall in line.

Variable costs might look a little bit surprising at first. Given the lower runs, the dollar per barrel variable costs were sharply higher which is also due to the fact that some key units, like the expander, which produces electricity and CO boiler, which produces steam were down in connection with the turnaround maintenance of the capital in the cracking units. For this reason we had to go out and purchase more utilities than usual to support the remaining production levels. At the same time we spent several millions on catalysts, again on the same units, and these catalysts are an expense and not capitalised which therefore added to variable costs. Next quarter we believe things will be back in line with usual levels.

II. Power Generation

Power generation in the IGCC performance was basically uneventful which is good news because production was in line with expectations. We lost the "incentive" component of the CIP/6 tariff as anticipated around mid April when the 8-year incentive component expired. Therefore the overall tariff was a mix of the old incentive tariff and the base tariff during the quarter and we will continue for another 12 years to enjoy the CIP/6 status and therefore the base tariff will be still linked to the fuel component, oil prices and other components which are indexed to inflation. CIP/6 is also important because it affords priority of dispatching which is key for the performance of this unit in connection with the refinery.

Fixed and variable costs

If we look again at Fixed and Variable costs I would draw your attention to Variable costs. Down in Eur/MWh terms vis-à-vis the first half of last year and this is due to lower costs for non-TAR feed stocks. Virgin Naphtha, Nitrogen and LCO were used to a lesser extent and this explains why in Eur/MWh variable costs went down. Again we believe that this performance can be maintained for the long term.

III. Marketing

Changing subject: Marketing. Marketing posted a very strong performance, probably stronger than we anticipated. In spite of the obvious lack lustre demand, sales in Italy in Q2 were strong, + 11%, and also margins were underpinned by the fact that since the beginning of the year we were selling directly in Sardinia because an agency contract expired and therefore margin levels will stay at a substantially higher level for Italy and particularly in Sardinia. Spain was less satisfactory but we still managed to support sales levels, at only 2% less, and also margins because we sold more to supermarket chains and unbranded service stations and less to competing commercial operators.

One word on bio-diesel. The bio-diesel plant started commercial operation in June with positive results and it's headed towards full production. Clearly margins in that sector are very volatile but the first results are encouraging being supported by the absence of excess taxes on bio-diesel and by the absence of quotas in the Spanish market.

IV. Wind

Wind was disappointing in terms of production because of variable wind levels but clearly this is a sector that needs to be looked at over a longer period of time than 3 months. If we look at the forecast for this year, comparable EBITDA, we have 12 million vis-à-vis 9.5 million for last year so overall productions levels are in line for 6 months. Tariffs are broadly in line because a lower market price for electricity has been counter balanced by higher green certificate prices. So broadly in line for the tariff. The difference between the two halves is explained by the fact that during the first half of last year we had to book some losses related to old CVs, on the contrary this year we posted 1.3 million euros worth of gains on old CVs which were sold in Q2. So overall the base sustainable results are line year on year. Other sectors as usual have completely different numbers but basically are around breakeven.

V. Financial Overview

1. Key Income Statement Figures

Going into the Key Income Statement figures I would like to draw your attention to the very significant difference between EBITDA and Comparable EBITDA figures for the quarter. 148 million IFRS EBITDA vis-à-vis 24 million Comparable. This happens every time there are major changes in the price of crude oil and oil products. If we go back to the last quarter of last year we have the opposite situation – minus 275 million in terms of IFRS EBITDA and plus 169 million in term of Comparable EBITDA. We're all going to have to live with that and major differences, quarter on quarter, are more usual that we expected.

2. Key Cashflow Figures

One final word on Cashflow. Our net financial position changed from net debt of 223 million to net debt of € 472 million. Clearly during Q2 we paid dividends and therefore 158 million of this difference was attributable exactly to that. Also quite sustained investment, as you might imagine again for same reason, the major turnaround. And finally, the usual movement in working capital. If you look at how working capital moves in relation to prices, in Q2 of last year we had more or less the same effect. There was a sharp rise in oil prices so we had to fund an additional 183 million working capital, mainly inventories and this year 142 million again. So this is relatively easy to explain. The CAPEX, 122 million, was also influenced by the fact that we started to close on part of the service stations we bought from ERG Petroleos in Spain (26 million expenditure). The balance will be closed in Q3 so the final CAPEX will be a little over 40 million. Refining by the end of the year will be broadly in line with our guidance and we don't anticipate any major changes. This is it for the financial review.

Outlook and Strategy

Dario Scaffardi

I. Outlook/1 Short Term Outlook

1. Refining

Thank you Corrado. I think it worthwhile to go into a little more detail on our 2009 maintenance schedule since a lot of things have happened in this quarter and will happen in the current quarter. We, as I've mentioned before, have carried out a very important maintenance and investment cycle of which I will give a little more detail. All this work has been delayed due to the tragic incidence of May 26th so there's a little bit of carry over in Q3 and we're giving some guidance on this on our further loss of EBITDA in the quarter of something in the range of 10-15 million dollars due to this delay in carry over of our losses. Also there has been a loss in runs, of course, and the overall import for the first half of the year is 72 million dollars. The work we have undertaken as we explained last year in our original investment plan was supposed to improve energy efficiency and conversion and last year we gave a guidance of an improvement of something in the range of 60-80 cents per barrel. Of course today the situation is totally different. The market scenario is an entirely different picture and so this number in today's market would be different. Our colleagues in Investor Relations in September will be a little bit more precise, in the guidance we can give, on the impact that these works have given. In particular what we have done is revamp our FCC unit, which is one of the largest in operation in Europe, we have revamped our Alkylation unit, which is closely linked to the FCC and we have revamped one of our Topping plants. The end result without getting into too much technical detail of this is that we will be able to run heavier crudes in our FCC so we will be able to benefit directly from the fact that we will be able to use cheaper feedstocks, upgrading to gasoline and diesel. We have an entirely new plant that will offer a higher degree of dependability. We have made significant investments in energy efficiency. We have (revamped entirely) built from scratch a new boiler and there's also some other parts that will give an overall benefit of something in the range of 30-40 thousand tonnes equivalent of fuel per year. Our Alkylation plant has moved from about 900 tonnes to about 1.1/1.2 tons. Of course these plants have just restarted so we have to wait a while in order to consolidate these numbers but the first results are extremely encouraging. And we have built an entirely new furnace for one of our topping units that will be able to provide total time between overalls in the range of about 5 years. Added to this there will be a significant improvement in energy efficiency.

If we look at the outlook in the short-term period we expect to close the year being able to achieve about 14 million tons of runs. We have a difficult autumn in front of us. At the moment there is no concrete sign of significant improvement in diesel consumption in Europe although there are some encouraging signs coming from non-OECD countries, which might show some improvement towards the end of the year. But the near term, of course, remains challenging.

In the meantime our bio-diesel plant is in operation is Cartagena in Spain and today margins for production of bio-diesel are extremely interesting. There's a difference in price between the market price of bio-diesel and the most efficient vegetable oils in the range of 200-250 $/ton so there is a good gross margin. And also in Spain we have completed during the month of June the hand over of almost all the retail stations, which we purchased from ERG last year.

II. Outlook/3

1. Guidance for Refining Margins

Refining margins, of course, are tough. We have the usual guidance here and today's current differential between fuel oil and diesel in the range of 170-180 dollars we expect to be able to achieve between 2.5-3.5 dollars premium over the EMC benchmark, which should be further enhanced by the completion of the investments we have just made but we will be more precise on this in the next months. During the rest of the year we don't really have any major maintenance schedule apart from a slowdown of one of the reforming units and a standard slowdown on one of the gasifiers.

III. Strategy Overview

1. Growth Strategy Highlights and Implementation

In terms of strategy there is no change to what we outlined previously. We are concentrating on and focussing on increasing conversion capacity in order to achieve higher operational flexibility, enhancing energy efficiency and reducing cost, so that we can improve performance. Our CAPEX schedule for the year is unchanged from what we have already outlined on previous occasions so we expect something in the range between 260-280 million euros. The programme for the next year is in the range of about 150 million euros and, of course, we continue to monitor the situation, in which up to now there has been really no change, to see when we can resume our investment programme.

2. Buy-Back Plan and Dividends

We have temporarily suspended our buy-back programme and as Corrado mentioned before we have paid out 158 million euros of dividends in May. Thank you very much. We will be pleased to answer any questions you might have.

Questions and Answers

Anish Kapadia, UBS

I was just asking, in terms of your exports from your refinery, I was just wondering if you could give a percentage of your production that you export and excluding out of that exports to Spain that go to your own marketing system? And related to that for those exports, I was wondering if you are seeing significant competition come in from new refining players in the market, I suppose Reliance is the most noticeable one. And the second question was related to the dividends for 2009. I was just wondering how you are thinking about your 2009 dividend policy, given the very weak earnings seen so far and probably expected for the rest of the year?

Dario Scaffardi

Thank you, Anish. In terms of products the majority of our products remain in the Mediterranean. So the two main markets, which we have, are Spain and Italy, actually Italy is a little bit more important than Spain but similar quantities. Massimo will be able to provide you with more details. The majority of our products actually remain in the Mediterranean area. In terms of competition I would say that the majority of the competition is actually coming from the contango plays. So what is depressing and one of the factors that is depressing the diesel market is the fact that there has been a huge amount of storage of diesel, millions and millions of tons; tens of millions of tons of diesel which have been sitting in the Mediterranean and in North West Europe which have been purchased in the past month and get dumped at discounts into the spot market depressing the spot market, which is part of the reason why diesel crack spreads are so low. Whenever you have market situations with strong contango this happens every time. So there's somebody who's making money out of the contango play and unfortunately someone like us who can take limited advantage of the situation since we produce diesel every day and cannot really produce diesel thinking of storing it. We have to sell it of course. This affects us negatively. The diesel we are seeing in storage is coming probably also from Germany but I have really no idea. The sources are generally the Far East where refineries run, instead of being shut down, to make specifically diesel targets for these plays. In terms of dividend policy we have our policy stated between 40-60% of adjusted net income and that would be reviewed if necessary by the AGM next year so it's really premature to talk about it.

Massimo Vacca

Anish. In any case, to get back to you, on details of the export excluding Spain. It obviously does depend on the quarter however in Q2 2008 approximately 35% of our production was exported, excluding Spain, where in Q2 2009 it's come down to 25%.

James Hubbard, Morgan Stanley

Good afternoon. Just two questions please. The first is that we've seen a lot of pessimism because of the narrowing in the light/heavy spread and the understanding that complex refiners made abnormal or high profits in the past from the widening that spread and now the opposite is true. So could you just describe how you see your exposure to the light/heavy spread compared to other complex peers that are out there and how much you are suffering relative to those guys? Secondly is there any ongoing impact, we should be aware of, about the incident occurred in Q2 or has that investigation now completed and there's no further operational aspect to think of?

Dario Scaffardi

Thank you James. Let me answer the second question first. There is an investigation on the part of the magistrates on the accident but we expect to have no further impact. The plant was arrested for about 15 days, roughly, if I remember correctly, it's been totally freed. And we will wait and see what the outcome of the investigation will be but we expect it to have no strong impact on the company. We are confident that we have done what was in our power to have all the operational safe guards in place but of course we will wait for the outcome from the magistrates. And it's something, of course, we cannot comment on.

In terms of the light/heavy spread. Today we face the usual paradox because we've seen it already in the past when you have a situation in which you have crude oil production which is limited by outside factors, namely OPEC cutting four million barrels from their production. They're cutting this on heavy barrels basically. Therefore the price of fuel oil has been artificially pushed up. There's very little real demand for fuel oil but of course having much less heavy crude available in the market has meant there is a premium for what demand is left of fuel oil. We are in this situation. We expect this sort of situation to last until we start seeing pick up demand in crude once again therefore the taps will open up for, basically, the heavy crudes and the discounts of the heavy crudes will become more normal. The fact that in the past months we have seen situations such as marge blend or Maya that's actually been at a premium to WTI are clearly illogical, from a certain point of view, but explained by the dynamics of supply and demand.

James Hubbard, Morgan Stanley

Is it possible to ask a follow up question? Just given those dynamics I'm just wondering if it's possible for you to make any comment as to what you perceive your exposure is to a narrowing light/heavy spread compared to a typical complex refiner. Are you worse positioned or do you think you're less exposed to that negative development?

Dario Scaffardi

We are actually less exposed due to the fact that we have a high degree of flexibility. As we have explained in other circumstances we are much less committed to just one type of crude. We have 3 lines in our refinery and can run a variety of crudes. We can run a very big quota of heavy crudes and we can also reduce this quota to an absolute minimum, which is what we are doing today. We are using the minimum amount of heavy crude which is necessary to maintain certain plants, namely the gasification plant, so we are minimising the crude and also we are actually trying to choose crudes that have a very high residue so that we can free up topping capacity for lighter crudes which have higher margins. So I would imagine that we are less affected than others. As you can see also in our presentations we've actually increased the runs of light crudes compared to heavy crudes.

Lydia Rainforth, Barclays Capital

Gentlemen, good afternoon, I have three questions if I could please. First one is just on the Cash flow statement I notice that you haven't actually paid the tax, the cash hasn't gone out for the first half of the year. Just explain to me why that hasn't gone out and when you actually expect that payment to go? Secondly, just on the contango trades, you mentioned that haven't really taken much advantage of that. Is that you haven't taken advantage of that at all and explain and go into a little more detail for me? And do you have a 2010 maintenance schedule to give to us?

Corrado Costanzo

First of all taxes are paid in several instalment in Italy. One instalment came up in July and another will come up in November. This is the same for everybody. I hope this answers your question.

Dario Scaffardi

Lydia, regarding contango plays and 2010 maintenance. 2010 maintenance: we have not published the schedule yet; we'll probably do so presumably in the next call. In terms of the contango plays we haven't been able to take particular advantage of the situation due to the fact of the maintenance in Q3 since we had to stock products to fulfil our commitments with clients and with our subsidiaries in Spain and Italy. So we really did not have much storage available for commercial plays. In any case it is not very much the policy our company to do these plays. We tend to run always at minimum possible technical inventory and we are reluctant to raise inventory even if in certain moments of course it can make economic sense by storing products someplace and then selling them into the contango market.

Ryan Kauppila, Nomura Bank

Good afternoon. In any given quarter when all the units are operating at full capacity to what extend would you say you can alter your yield slate specifically between light and middle distillates?

Dario Scaffardi

We don't have huge flexibility in being able to alter our yield structure. What is the advantage that we have is the fact that we are more capable at varying the input. So we can change, what we actually act upon, is more in terms of what types of crude and feedstocks we put into the refinery rather than adjusting the plant. Our plants are big, sophisticated which means that once they are set in a certain way you can't really switch from light distillates to middle distillates. This is something that no refinery can really do. Let's say that if I can give you a rough figure probably we can switch, like anybody else, maybe something in the range of 2% could be switched from diesel to gasoline and vice versa roughly. The plants to produce gas are different from plants that produce diesel so there's not much you can about it. What is a strong advantage that we believe that we have is the fact that we can vary having a large crude storage and 3 topping units we can change and vary the type of input and that is an important advantage. And we are further gaining flexibility in this respect with the work we have performed on our FCC which already was a very sophisticated unit, one of the biggest in operation in Europe and today it's still in that league, it's brand new and it has a much increased level of feed stocks that it can run.

Corrado Costanzo

One more thing about Tax payments. There has been a tax payment in July but we were running at the end of June a sizable VAT tax credit. Therefore the payment in July was largely offset but the expiration of this VAT credit during Q3.

Lydia Rainforth, Barclays Capital

Just a very quick follow up. On terms of the bio-diesel plant. Can you actually give us the contribution for the quarter and how you're seeing that running at the moment?

Corrado Costanzo

The contribution for the quarter was nominal, in terms of EBITDA less than 1 million euros. It was in full commercial operation for about a month and clearly you're still talking about the first month of production. Overall the contribution depends heavily on margins, which are clearly volatile although there is an advantage embedded in the fact that we are located in Spain. Spain has no quotas. It's also easy to use the most advantageous feedstocks and we're not tied to any particular agricultural area or anything like that. We are fairly confident that we will be able to draw something between 5-10 million euros of EBITDA once full production and full-scale sales are ongoing.

Kim Fustier, J P Morgan

Hi, good afternoon gentlemen, just two questions if I could. You might have already answered these questions but I missed the first part of the call. Firstly can you explain why your crude slate was heavier in the second quarter this year than Q1 or Q2 of last year? It seems counter intuitive because this quarter there was a lot of maintenance, obviously restricted supply of heavy crudes as well. Secondly I'm not sure I understand why you've reduced your guidance on crude runs for the second half of this year if all you are doing is effectively pushing maintenance forward from Q4 to Q3?

Dario Scaffardi

I understand that it can be counter intuitive but the fact that our crude oil slate has been slightly heavier in Q2 is explained by the fact that the topping unit and the FCC are users of the lighter parts of the barrel. So we have proportionately decreased a bit the runs of light crude and increased the runs of heavier crude. It's just an operational aspect there is nothing particularly significant about this, it's just that the topping unit, when we entirely redid the furnaces, is the one that we generally devote to the light sweet crudes so the quotas of those has diminished. Excuse me, your other question?

Kim Fustier, J P Morgan

I just wonder why you have reduced your guidance on throughputs in the second half of this year? Previously you were guiding to 7.7 million tons and now you're guiding to about 7.5, if I'm not mistaken.

Dario Scaffardi

The shutdown of the plant has been delayed because of the accident that we had so basically the plant was supposed to restart at the beginning of July instead it started in the third week of July so we added about 15-20 days so there's been a loss of runs in that respect. The impact is already computed in those numbers that have been shown in the maintenance schedule.

Domenico Ghilotti, EquitaSim

Good afternoon. I have a question on power generation. You mentioned a lower variable cost that could be sustainable over time. Could you repeat the reason for this lower variable costs going forward?

Corrado Costanzo

In the first half of last year we used more non-Tar fuels and there's been a lot of work done in order to optimise the use of non-tar fuels particularly in light of the fact that with the expiration of the 'incentive' component those fuels really only make sense for very tight and specific technical reasons.

Domenico Ghilotti, Equita Sim

OK, thank you.

Closing Comments

Massimo Vacca

OK then, if there are no further questions, I would like to thank everyone tonight for joining us for this call and we give you appointment for the next call where we will talk about our Q3 results. All the details will be on our website. Thank you very much and good evening.