



Saras

Q1 2018 Results

Welcome

Francesca Pezzoli
Head of Investor and Media Relations, Saras

Good afternoon ladies and gentlemen, and thank you for joining us today for this conference call on Saras' First Quarter 2018 Results. The analyst presentation, has been already distributed with the usual channels, and is available on our website.

Our agenda today will be the usual one. Mr Dario Scaffardi, Chief Executive Officer and General Manager of the Saras Group will start with the highlights of the period, followed by a detailed review of the results of each business segment. Afterward, Mr Franco Balsamo, Chief Financial Officer, will discuss the key financial figures of the Group, and then back to Mr Scaffardi for the outlook and finally we will have the Q&A session.

At this time, I would like to hand over to Dario.

Dario Scaffardi
CEO & General Manager, Saras

Highlights

Thank you, Francesca. Good morning, ladies and gentlemen. Thank you for being with us here today. The first quarter of 2018, the Saras Group posted a reported EBITDA which was in line with the comparable EBITDA of about € 72 million. This is mainly due to the fact that the refinery operated in much less favourable market conditions, due to a contraction of the margins, and also because of a



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heavier maintenance in the first quarter of this year and some issues with our performance. I will be more detailed about the market in the following slide, but at this stage, I'd like to highlight that the Brent continued its rising path started at the end of 2017 after the agreement reached between the OPEC and non-OPEC countries for the production cuts all through 2018, furthermore compounded by various geopolitical issues and a very robust demand growth.

Gasoline and fuel oil cracks were also weaker in this quarter, and this affected negatively the EMC benchmark which averaged \$1.70 in the quarter.

Towards the end of the quarter, in March, things started on a path of improvement, which we'll give a little bit of detail on later. From the operational point of view, the maintenance activity was completed in a timely manner during the first quarter of the year, even those regarding the IGCC power plant. And, as announced during our full-year result the maintenance this year is front-loaded, meaning that the remaining that the remaining part of the year will have only smaller activities to be carried out. So, we count on being ready to capture the opportunities that the market will offer.

Looking at our cash position, the group reported a slightly negative position by € 1 million versus € 87 million positive at the end of 2017. This was mainly driven due to an increase, temporary, in the inventory levels, and we expect to be back in positive area, even after the payment of € 0.12 of dividend per share due for payment on May 23.

Looking at the crude oil prices, Brent continued its upward path started at the end of the year. At the beginning of the year it started at \$67.00 and it continued a strengthening phase due to a series of factors: first of all, the extension of the OPEC cuts, but also the tensions with Russia, the tensions with Venezuela, now the tensions with Iran. So, Brent surpassed \$70.00 per barrel in mid-February, notwithstanding a continued increase of production of US tight oil, as well as improvement in Canada and in Brazil. The quarter closed at \$67.30, but right in the beginning of the new quarter the market started to rise again, and as everybody knows, today we are almost in the range of \$80.00.

In January and February, the gasoline crack spread was further weakened, and hit a lower level of the last few years due to an increased accumulation of product which was due to high refinery runs due to wet weather conditions, which created an excess production of gasoline, which in the meantime has been absorbed by the market.

On the middle distillates, in Q1 2018 the crack spread of diesel remains stable, at satisfactory levels, benefiting for a strong demand for heating oil driven by the cold weather, especially in the United States and due to low level of supplies from South American refineries, due to their high level of maintenance and unplanned outages. The crack spread was around \$12.00 per barrel in the first quarter of 2018.

I will say that more significant was the crude oil differentials in this first part of the year. Crude oil differentials, if we look at the value of Ural and the Arabian heavy, it started rising towards the end of the year and reached their maximum in January and February with a strong overhang of sour barrels, which subsequently were lowered as price and were made, and the effect of more barrels on the market was more manifest after the end of the quarter.



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If we look at the recent trends in refining margins starting with the EMC benchmark, the EMC benchmark, let me remind you, represents the profitability of mid-complex costal refinery located in the Mediterranean with a feed stock made 50% of Brent and 50% of Urals, conventionally. So, in Q4 2017, the benchmark was at \$2.30 per barrel, in the context of fast-rising Brent price. In the first quarter, this declined to \$1.70 due to further weakening of the gasoline price, the fuel oil spread, and a strengthening of the crude oil price. Since then the situation has improved.

In the first quarter of 2018, the premium stood at \$2.10 per barrel, as usual, after the impact of the maintenance carrying out during the period, which weighed approximately \$1.30 per barrel. Considering that 2018 is a front-loaded maintenance year, we confirm our guidance to achieve about \$2.50 to \$3.00 premium post-maintenance on the average for the year.

Segment Reviews

1. Refining

If we now look at the various sectors, refinery crude runs in the first quarter of the year were at 23.4 million barrels, down 7% compared to the same quarter of 2017, while the crude runs of complementary feedstocks were about 260,000 tons. This is mainly the evolution of a maintenance program carried out, and of lower operating performance. The comparable EBITDA was € 9.1 million compared to almost € 70 million in the first quarter of last year.

First of all, there were less favourable market conditions. The EMC benchmark stood at \$1.70 compared to \$3.30 of 2017. So, high crude oil prices brought penalisation which is worth about € 70 million compared to the same quarter of last year, and this shows up a lot in consumption and losses.

The gasoline crack spread was weaker, and offset partially the strengthening of the diesel crack, with a net effect or an increase to the value of production of about € 5 million compared to the same quarter last year. Finally, the negative effect of the Euro-US Dollar exchange rate, which accounted for about € 15 million.

From an operational point of view, the production planning in this quarter posted a lower EBITDA of about € 5 million compared to the same period of last year, due to a less favourable mix of crude oil available. As I mentioned before, the first quarter was particularly challenging in terms of the prices of the heavy sour crudes that reached unreasonably high levels, which were subsequently corrected.

The commercial performance instead was approximately € 5 million lower than the same period of last year, mainly due to the same reasons.

If we look at crude oil and product yields in the various -- in this quarter, as we have explained many times, it's not very meaningful to look at a single quarter since each quarter can be heavily affected by temporary factors such as maintenance or strong or lighter purchase of a specific type of crude oil based on market conditions. Nonetheless, the crude oil slate was slightly lower, and this is in line with



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the fact that there is high availability of low-sulphur crude oils and their price had been relatively lower compared to those of other crudes. So, we have slightly increased the percentage of these type of crudes, which shows up in a higher yield of gasoline and slightly lower yield of distillates.

We don't usually comment in the quarter on the figures for fixed and variable costs, I would pass on to the power generation segment.

2. Power Generation

The power generation segment had the heaviest part of the annual scheduled maintenance activity, which involved one train of our gasifier combined cycle and one of the two gas washing line trains which is a very important part of the plant, which basically provides hydrogen to the refinery. So, these two effects combined show that we had a lower electricity production, which was 886 megawatts in the quarter compared to a standard quarter, which would have a number which is about 1.2. But still, 21% higher than the one of last year, which was 735 megawatts.

The power tariff was slightly higher, it was Eurocent/KWh 9.2 compared to Eurocent/KWh 8.8, of last year, mainly due to the CIP6 tariff component and also by a higher base price for electricity. Comparable EBITDA was € 53.1 million compared to €43.9 million achieved in Q1 of 2017. This difference is due to lower fixed costs, thanks to a lighter maintenance cycle compared to last year, and to an increase of 4% in the CIP6 tariff.

Sales of steam and hydrogen, which are not subject to the equalisation procedure, were essentially in line with those of last year.

3. Marketing

If we move to the marketing segment, it was overall positive both in Italy and in Spain. For the first time in a long time, in Italy there was an increase of 0.6% on the total market sale which is mainly driven by middle distillates because there was a significant decline both in gasoline and fuel oil, while jet fuel increased. The same is true in Spain, and actually in Spain, the increase in middle distillate demand was significantly more robust than in Italy, with a 3.8% increase.

So, sales in Italy were more or less in line with those of last year, roughly 500,000 tons in the quarter, while in Spain they were up 7% compared to those of last year's. Better market condition and better margins, more utilization on the various outlets and channels have given a significant improvement in this segment.

4. Wind Power

Comparable EBITDA for the wind power segment was € 4.6 million, down compared to the € 6.9 million in the first quarter of 2017. The volumes were actually much higher, 32% compared to the



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same period of last year, thanks to much better wind conditions. But, this dynamic was offset by the reduction in the electricity tariff, roughly 1 cent and a decrease in the incentive tariff of 8 cent compared to the same period of last year. In this period, the incentive period expired on approximately 60% of the volumes produced. Remember that the incentive was set for 12 years, and we have reached for 60% of production.

5. Others

In the Others segment, not much to say. I will hand over to Franco, if you have any comment on the financials?

Franco Balsamo
Chief Financial Officer, Saras

Financials

Thank you. Some comments below the EBITDA line, the financial and income expenses is very close to zero, and the combination of interest expenses for € 3.5 million, that is in line with the previous quarter of the previous year. And, there are positive € 3.4 million on the financial income, as Saras presented, for € 9.7 million is the fair value on derivatives on the CO2 certificate. And there are negative expenses for € 6.3 million represented by derivatives on commodities and on the foreign exchange.

If you look at the gap between reported EBITDA and comparable EBITDA, we have accounted negative € 20 million in term of gain and losses on the inventory, which are mainly due to the increase of the Brent over the period that moved from \$61.00 a barrel to \$67.00 a barrel. € 9.7 million, as we've seen before, is the fair value on the CO2 derivatives that is a non-recurring items.

And finally, there are realized and unrealized hedge on derivatives on foreign exchange, on the commodities for € 9.7 million, that are accounted in the comparable EBITDA. The remaining part are still included into the financial expenses in the reported account.

Finally, some comments about the group cash flow. The working capital were negative for roughly € 60 million, it is the combination of different factors. The most important is the delta in inventories, that arose for € 260 million, and as Dario said before, this amount in terms of quantity will be released by the end of June. On the opposite we had € 90 million as a positive effect of the management on the working capital as well as the positive effect on this quarter represented by the VAT. So, the combination of those three factors are the explanation of that € 60 million negative. CAPEX at € 50 million are in line with our forecast.

So, the cash flow before dividend is - € 88 million

I'd like to pass to Dario for other comments.



Dario Scaffardi
CEO & General Manager, Saras

Outlook

Thank you, Franco. So, we haven't changed our outlook for 2018, and the maintenance schedule has not been changed in a significant manner. I would just like to highlight that the heaviest part of the maintenance, annual maintenance program, has already been carried out in Q1/18 with a little bit in the earliest part of Q2. So, in 2018, we expect the electricity production to pick up and reach 4.2 terawatts, with a comparable EBITDA of around € 150 million. We expect an improvement in the overall refining scenario as the market paves the way to the IMO regulation, which we expect will have a very significant effect on our sector.

I would just like to make a mention on the Iranian situation, which of course has been a hot topic in the last couple of days and over which we have received many inquiries. Iran is one of the suppliers of Saras', one of the main sour suppliers into the Mediterranean, though not the only supplier. And of course, Saras will comply with any law and regulation which might come into effect as we have always done. We find the current situation worrying, because it affects the international commerce in the same way other sanctions do, and we are of course worried not by not having access to crude oil, but for the value of these various crude oils.

I would just like to remind that in 2015, Iran was under embargo, so at least for European-American countries, it was not possible to buy Iranian crude, and we were not buying Iranian crude. And, Saras posted its record year in 2015. So, our profitability is not directly linked to Iranian crude or any other type of crude. Our profitability is certainly linked to the overall market scenario, to the tensions, and history shows that these types of tensions are not positive. So, we are worried about the overall scenario, of course, not specifically on the capability for being able to source crude oil, which thanks to our flexibility and our knowledge of the market, is not an issue. At what price, is another issue, of course.

Thank you very much. We will be pleased to answer the questions you might have.

Questions and Answers

Alessandro Pozzi - Mediobanca

Thank you for taking my two questions. The first one is going back to Iran. I've seen that you have maintained your guidance for the premium over the benchmark to 2.50 \$/bl to 3.00 \$/bl. I was wondering, does that include



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any potential impact on the compressions on the heavy-light differentials? And, I was wondering, what is your gut feel at the moment where those differentials are going to go in the second half of the year?

And, my second question is on middle distillates. I think we are seeing a global tightness in the middle distillates, and I think with IMO regulations coming in potentially, we could see those cracks performing really well. I was wondering what is the maximum yield that your refinery could produce in terms of middle distillate? Thank you.

Dario Scaffardi

On the heavy-light differential, of course at the moment there is some temporary worry that this might come, that might move back in. Now, there have been some very, very significant moves in the last couple of months on this differential, for instance, all the sour barrels from the Arabian gulf have been discounted by almost a dollar more compared to the same period of the previous month, and we view this as a positive factor. Of course, after the situation with Iran, at the moment it's just too soon to assess what the implications might be, depending on the positions of the various governments which at the moment is totally not clear. I mean, the only position which is very clear is that of the US government, which is extremely negative to anything that involves Iran. What Europe is exactly going to do is, to us at least, is not extremely clear.

Having said that, at the moment I think there's going to be a little bit of pressure on heavy differential, because commerce with Iran is going to be a little bit more difficult. Whether the Saudis are going to compensate by pumping more on the heavy side, at the moment I just don't know, and it would probably have to be something that arises from sort of international agreement, which doesn't seem likely at the moment.

I agree with your view of the demand for middle distillates position, which is extremely robust and we're seeing it every day, -- one of the star performers has been jet fuel, which has increased significantly compared to diesel. We, depending on the crude slates, we can average something like probably 53% - 54% of middle distillates. That depends a lot on the type of crude oils that we run. As we explained many times, we don't target, necessarily, a production but we target a return. So, it's the mixture between value of the crude and the value of the products that gives our profitability. But, to make a long story short, the maximum is around 53%, 54%, maybe 55%.

Alessandro Pozzi - Mediobanca

Thank you very much. That's very clear, thank you.

Peter Low - Redburn

Thanks, two questions from me. First, just on your near-term outlook for the refining margins, demand and product inventory seem healthy but margins are soft versus last year, particularly for gasoline. Can you just walk us through what you're seeing in the market?



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And then, my second was just on power generation, and the difference between IFRS and Italian GAAP EBITDA. Can you remind me, should these two converge over time, or the cash flows from power gen be sustainably lower than the IFRS EBITDA number implies? Any colour on that would be great, thank you.

Dario Scaffardi

Well, I'll leave that gladly to Franco. On the gasoline market, basically what has happened is that there have been high refinery runs in the first part of the year, which have created an excess of inventories in gasoline, and reduced the cracks, which since have recovered in an important manner. I would say that there is just a little bit of risk of an excess production of gasoline on the back of a high production of diesel, which is in demand, but on the other side I must say that a big importer of gasoline, which is South America, has some very, very significant problems. The Venezuelan refineries are not running. We are exporting gasoline to South America since last year for the first time in our history, I would say. And, there is strong demand in North Africa, in the Middle East. So, all in all the picture doesn't look worrying.

Franco, do you want to explain how IFRS works? I gladly leave it to you.

Franco Balsamo

Complicated issues, but if we just go a quick answer -- if you look at the value term of cash flow generated by the power activity, you have to take into consideration only the Italian GAAP EBITDA, because the difference between the Italian GAAP and the International Financial Principle is represented by the fact that due to the linearization, and the linearization is not a monetary issue. So, in this quarter, the difference between the term of cash between the -- in the power segment and between Italian GAAP and International Account is negative for € 35 million.

Peter Low - Redburn

Okay, do you expect it to sustain at that level, or is it impossible to say?

Franco Balsamo

The linearization is a tax asset we have in our account for approx. € 125 million. This amount will be splitted over the duration of the concession, so up to the end of the year 2020 to the CIP6 contract. In terms of cash flow generated by the business with a plan to the operations performances of the plant. So, but the two amounts are not going to be the same, of course. So quarter-by-quarter it will be utilised up to the end of the concession.

Peter Low - Redburn

That's great, thank you.



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Massimo Bonisoli - Equita Sim

Good afternoon, and thank you for the presentation. Two questions. One on the hedging of refining margins. We discussed about the eventual hedging of forward margin over the four-quarter results conference call. Do you have any update on hedging? And the second, on the new CEO role versus the Managing Director, congratulations, Dario, for the new role. Could you give also some colour on the relevant changes for the governance of Saras?

Dario Scaffardi

Well, thank you. On the hedging, it's something that we're still looking at, and to be very honest, I would say we are lukewarm on the issue. I would say that historically anybody like me, who has been for a long time in this business, has always seen some pretty bad horror stories on long-term margin hedging. And I don't recall any positive stories. So, at the moment, we've seen that there's a window of opportunity looking forward, but just looking at the past, and by the past I mean decades, that sort of dampens any enthusiasm.

Having said that, our people, in particular financial and commercial people, are looking in closely to see if there is opportunities to catch. Refinery margin hedging is an extremely complex operation, because you cannot look at the individual cracks in isolation. Let me give an example.

If today the diesel cracks, are , about \$14.00 and the forward cracks today are \$20.00, \$21.00. So, one would think that it might be a good idea to sell some cracks forward at \$21.00. Sounds like a good idea, but if you're actually refining oil, that means that you're also exposed to gaps in the price of oil. So, if you're selling a crack of \$21.00 and the price goes from \$75.00 to \$110.00, which is not bizarre, it's not crazy, that's already happened, you would lose on both sides. So, you're actually compounding your losses, so in some way you have to be extremely careful on the management. The idea would be to hedge exactly in a mathematical manner, the refining margin which is not really possible, or it's possible partially through some very complicated operations.

So, we are looking at it. We haven't really done anything at least for now, but never say never.

And on the role, thank you for the congratulations. On the governance of the company, I would say that it hasn't changed significantly since the management team is the same that has been in place in the last couple of years, and I will say that there's a great maturity on the controlling shareholders, which have decided to create a governance which is more in line with what the market expects. So, but, we're within the framework and in line with the tradition of the company.

Massimo Bonisoli - Equita Sim

Very helpful, thank you.



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Josh Stone - Barclays

Hi, good afternoon, and thanks for the presentation. I've got two questions, please. Firstly, on the power generation business, running slightly ahead of guidance of € 190 million helped by higher tariff, are you able to say what guidance the tariff is based on, if that's still valid, and what you expect for the power tariffs for the rest of this year?

And then secondly, just coming back onto Iran, I assume you're still purchasing crude from Iran today. How do you look to diversifying that slate to other places, and maybe you can provide some more details as to where and how that's going? Thank you.

Dario Scaffardi

Well, for the time being, let's say on the immediate, nothing has changed in the supply, anyway we are of course in contact with all the crude suppliers in the world. So -- well, maybe not all of them, but a great majority of them. So, we're talking about sour crudes from the Mediterranean, we have contracts and relationships with Iraq, with Saudi Arabia. Saudi Arabian crude does not really come that much into the penetration, due to market reasons. Libya is a producer of sour barrels of course, Russia, we are waiting for more volumes of Kirkuk to come out of Seyhan. Kurdistan wasn't an important supplier of crude into the Mediterranean region until the political events of last November, would seem that we are converging through some sort of clarity there as well. And so, resumption of export of Kirkuk from Seyhan are expected in the near future.

These are the main suppliers of this type of quality. Of course, West Africa also is increasing in terms of availability of this type of crude oil. Of course, on the negative side, there's the situation in Venezuela which although it's never been an important supplier to the Med, still, it's a supplier on the market and there is a ripple effect.

So, at the moment, this is a source of concern, of course. In terms of prices and relative values, not in terms of being able to source material. So, I think this might, is the single thing that could put some pressure on the market, depending on which way it evolves.

Now, is Iran going to continue to export, and its exports are going to go mainly in certain countries? Then, those countries will start to not import the qualities that they're importing today, and things realign. It just depends on if there's going to be a net subtraction of certain types of barrels from the market or not. This, at the moment, is not known.

On the power generation, I would like --

Franco Balsamo

We have in our forecasting, we considered the production lost in the first quarter will be recovered in the coming months, so our guidelines shall remain unchanged.

Dario Scaffardi

But I think the question was on what the power tariff, what it depends on. Was that the question?



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Josh Stone - Barclays

Yes, exactly, just to get some sense -- because the power tariff was up quarter-on-quarter, just to get a sense of how --

Dario Scaffardi

The power tariff is mainly linked to gas prices.

Josh Stone - Barclays

Okay. Okay, fair enough. Great, thanks very much.

Dario Scaffardi

Not mainly, exclusively linked to gas prices.

Franco Balsamo

There is also a fixed element

Dario Scaffardi

Yes, there is -- and then there's some fixed elements. I mean, in terms of commodity, it's only linked to gas.

Josh Stone - Barclays

Good answer, then. Thank you.

Francesca Pezzoli

Okay, if there are no more questions, thank you, everyone, for listening to the conference call, and we are available for any follow-up question you might have. Thank you.

Dario Scaffardi

Thank you very much.

Franco Balsamo

'Bye.