



ERG S.p.A
“First Quarter 2010 Results”
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Operator:

Good afternoon. This is the Chorus Call Conference Operator. Welcome and thank you for joining the ERG First Quarter 2010 Results conference call. After the presentation there will be an opportunity to ask questions.

At this time, I would like to turn the conference over to Mr. Alessandro Garrone, Chief Executive Officer of ERG. Please go ahead, sir.

Alessandro Garrone:

Good afternoon everybody and welcome. I am here with Luca Bettonte, our General Manager and Paolo Merli, our Head of Corporate Finance and Investor Relations.

Let me start with the highlights for the Q1 financial figures. The Q1 adjusted EBITDA at replacement costs came in at €50 million, 4 times up, if compared to the €12 million over the same period last year. These figures include €28 million of insurance reimbursement for the ISAB Energy incident, the same amount booked during Q1 last year. The year-on-year growth has been mainly driven by a solid performance of the energy business, along with improvements, compared to the same period last year, of coastal refining and renewables businesses in particular.

The replacement cost net profit had a loss of €16 million compared to a loss of €20 million in Q1 '09. At bottom line, the improvement at EBITDA level is mainly offset by higher depreciation, financial charges and minorities.

If we look now at our balance sheet, the net financial position closed at €756 million at March end compared to €662 million at 2009 year end and versus €321 million on March 2009. The net financial position adjusted for the 51% cash in ISAB balance sheet is at €685 million. The leverage increased from 14% at end of March 2009 and 26% at year-end of 2009 to 28% at the end of March 2010. The increase is the result of both weak operating cash flows, following challenging international scenarios, as well as important investments in power and renewables assets. Those effects were partly compensated by the insurance reimbursement for a total amount of €250 million, that of course we received in 2009.

So, now over to Luca, for the Q1 results in more details, thank you.

Luca Bettonte:

Good afternoon everybody. Thanks for coming as usual. Going through our figures, replacement cost EBITDA adjusted at €50 million of this quarter is better than the Q1 '09 (€12 million) and also better than the fourth quarter of last year (€21 million). Power and Gas has reported strong results, as a result of higher volumes and prices for both ISAB Energy and ERG power, which benefited by the contribution of the first train of the new CCGT plant.

Renewables: the EBITDA more than doubled compared to the first quarter of last year, thanks to an increased production following the capacity additions we had in 2009.

On the other side, coastal refining is still in red, even if a little better than last year when we had the shutdown of the ISAB refinery in January and in February.

Integrated downstream stays in line with Q1 '09 figures, as a result of stronger marketing (which benefited by the contribution of Restiani during this quarter) and weaker inland refining performance.

In terms of EBIT pattern, adjusted EBIT at replacement cost is plus 2 versus minus 30 of last year. As usual, in this chart I think it's worth commenting our performance in terms of financial income and expenses. The other item just lets you go forward and backward with reference to the replacement costs versus reported results.

Net financial income and expenses at minus 10 this quarter compared to plus 5 of the same quarter of last year. This performance seems to be negative but it is not really so, because last year we benefited by two items: €11 million exchange (Forex: positive outcome so exchange rate euros versus dollars at positive posted by €11 million) as well as €6 million represented by financial income associated with the transaction with Lukoil. If you deducted this €17 million to the plus 5, you land at the minus 12: so this it just to say that the minus 10 is a better result compared to the last year on a like-for-like basis, simply thanks to lower interest rates, while we had approximately the same level of gross indebtedness.

At the end of this chart, net profit at replacement cost is a minus 16 versus minus 20: of course, this 20 is affected by the same impact at financial charges level that I've just commented.

Going ahead, let's see the coastal refining key figures: adjusted replacement cost EBITDA is minus 16 versus minus 24 of last year. Some pressure on our margins during the quarter is of course the result of the challenging trading environment. On year-on-year basis we had a slight improvement in terms of replacement cost EBITDA, due also to the negative impact we had in Q1 '09, stemming from the general turnaround of the refinery. At the same time during this quarter margins were mainly driven by weakness of the middle distillate crack spreads and also a weakness of US dollars against the euro.

Talking now about refining margin at replacement cost: 1.57 US dollar per barrel this quarter versus 1.52 last year, and the volumes processed in kilo tons this quarter have been higher than the first quarter of last year. So unit refining margins in the first quarter this year came out slightly higher than the same quarter last year. We had two opposite factors: on the positive side last year we had the refinery shutdown for general maintenance in January and in February in a period of good margins. On the negative side, the refining scenario was very challenging in this quarter. As I mentioned before, stronger euro was also giving us more negative impact on margins, while higher volumes are easily explained with the general shutdown we had last year. In this context, the premium compared to EMC benchmark came in at 1.25 barrel per dollar over this quarter, still penalized by the scenario.

Talking about integrated downstream, replacement cost EBITDA is in line, if you consider that we posted the €15 million this quarter versus €16 million in the first quarter of last year. Marketing reported plus 20 versus plus 15, whilst inland refining logistics is at minus 4 versus 2. Overall EBITDA is a bit stronger than in the first quarter of last year, mainly for the contribution of Restiani with reference to marketing, while deducting Restiani, the performance has been in line with the previous year. Higher quantities at a bit lower margins, while inland refining and logistics EBITDA is worse, due to the negative refining scenario.

In terms of quantity sold, retail sales are higher than in the same quarter of last year while on the wholesale side sales are almost in line. In any case, it is important to underline again that our retail performance has been better than the industry trend. Let me remember you that domestic industry has shown in the first quarter of this year overall consumptions slightly lower than in the first quarter of last year: minus 1.5% driven mainly by gasoline, while diesel has been a bit positive. In this context, ERG volumes have been higher than in Q1' 09, so we increased our market share. Talking about wholesale, domestic industry was down minus 9.3% in the first quarter 2010, whilst we kept selling the same quantity of last year: as a result, our market share increased in the quarter.

Inland refining: as I mentioned before, we were affected by the unfavorable refining scenario in terms of refining margin at replacement cost during this quarter, namely 2.09 U.S. dollar per barrel versus 2.68, due simply to the negative scenario, while the volumes processed has been pretty in line with Q1' 09 values.

Moving from oil to power, let's have a look now at ISAB Energy figures. Sales in terms of gigawatt hours have been higher than the first quarter of last year (507 versus 471); replacement cost EBITDA is €39 million versus €25 million. CIP6 tariff: €97 per megawatt hour versus €89 of the same quarter last year. Higher production is a result of higher load factor (45% versus 41%) and of the higher tariffs of around 10%. Of course, it's important to underline that - upon the final commissioning of the new train - the plant is expected to be back on stream by the end of this month, so one month ahead of the original schedule.

Looking now at that Power and Gas, we note a big increase in electricity production: 543 gigawatt hours compared to 120 of the previous year. As a result, replacement cost EBITDA is 10 million positive versus 3 negative. Of course, the production was much higher as it has been positively affected by the first train of CCGT, which was in commercial operations throughout the entire quarter. During March 2010, also the second train of the CCGT was commissioned and entered in commercial operation on the 1st of April. So for us the completion of this plant is a great achievement. Let me remember that everything has been already financed just through a project finance of €330 million in twelve years.

Renewables: as far as electricity production is concerned, again we reported a larger amount compared to the same quarter of last year (109 gigawatt hours versus 85), with the replacement cost EBITDA at 11 million versus 5 million. The net income is not reported, let me remember anyway that the net income was positive, higher than €1 million. It's an important result for us after several quarters with the negative red number bottom line. Let me just remember what has been already shared with you two days ago: the reason for this positive outcome is mainly linked to the higher production, both in France and in Italy. We had the full contribution of the new wind farms of Vicari and Faeto and we also benefited by the decrease of the Terna grid limitations on some wind farms.

Investments: €78 million this quarter, versus €62 million the same quarter of last year. We have two main investment lines: firstly the investment in power sector, mainly related to the reconstruction of the train damaged in October 2008. Of course, I am referring to ISAB Energy and the completion of construction of the new CCGT that entered into commercial operation on the 1st of April, this year.

The second investment line is in the renewables sector: we keep investing in order to meet the deadlines listed in our industrial plan. We are on time on budget: the increase of investments is mainly related to Ginestra and Fossa del Lupo wind farms, while Plogastel in France (9 megawatt) has been completed and is now in the commissioning phase.

Finally, cash flow statement: we started with €662 million net indebtedness and a leverage of 26% at the beginning of the period, and landed at €756 million, with a leverage of 28% at the end of this period. If we deduct the €72 million cash, pertaining to the group but in ISAB, we should have €685 million net indebtedness on adjusted basis. The negative operating cash flow we had is due to a bottom line negative result in this quarter by €70 million, and to the investment program we are carrying on for €67 million. At the end, in any case let me underline still a solid financial structure for the Group. And now I give back the line to the Chief Executive Officer.

Alessandro Garrone:

Thanks a lot. Let me now comment on the last two slides about the economic guidance for 2010, and some strategy for the future.

On the economic guidance for 2010: compared to the previous year and looking up at coastal refining, we are slightly positive for two reasons. We have no general shutdowns planned for 2010 and we see a slight recovery in margins, even if the environment is still challenging. As far as integrated downstream is concerned, and considering just the existing perimeter (so without any guidance on the TotalERG joint venture) we see a stable situation, which means an increase in sales and market share, but with margins a little bit lower, if compared to 2009. Then lower costs, due to ERG Mobile project: as you remember, we had a cost of roughly €14 million in 2009, and we have few millions in 2010. But the scenario of inland refinery is still tough: so stable results, as far as integrated downstream is concerned.

Also on the Thermolectric, we are positive for two reasons: one is the full contribution of the CCGT plants, as of the beginning of Q2, 2010. If you remember, the first train came on stream already at the end of 2009, and the second train came on stream on the 1st of April this year: so we have almost a full contribution of this plant in 2010. The second reason is the full contribution of ISAB Energy plant as of June 2010, when the second train of ISAB energy will be on stream. We expect to have the plants fully operational by the end of this month, therefore June will be a month of full production. So the guidance is to have a total production of 6 terawatt hour, of which 3 in ISAB Energy and 3 for the CCGT plant.

We are positive also in renewables, mainly for one reason: because of the rise of electricity production compared to the previous year and because of the new installed capacity coming from Faeto and Vicari that will be fully operating. We finished those plants last year, so for 2010 they will be all 100% on stream. Moreover in 2010 we will add the production coming from the Plogastel power plant in France, and by the end of this year from Fossa del Lupo and Ginestra. So, due to production reasons, results of renewables will be better. Finally, we still have some constraints in terms of throughput and selling the electricity coming from renewables due to the maintenance work on the national grid.

And then the last slide, about the strategy and final remarks: just to sum up, we display six moves we made or we are making to have a better strategic positioning for the year to come. As far as TotalERG is concerned, we expect the Antitrust clearance very soon. Since then we will work together to define what we think is a strong industrial fit between the two complimentary realities in Italy. So, as I already said when we announced the Joint Venture, we expect this to bring very good costs and revenues synergies: we forecast roughly €20 million of synergies in the forthcoming years, as ERG share of the total synergies.

The second move is the Group re-structuring. It is going on, we announced internally at the beginning of May the new organization, and now we have two business units: the Oil business unit and the Power business unit, plus of course the renewables company, ERG Renew. We expect these to bring savings in terms of cost of around €5 million when we will be at regime and the other reason, of course is to speed up the decision process in the Group.

Third step: the new 480 megawatt CCGT is - as I said - now fully up and running, and this is our great achievement for the Group. For this plant we closed the project financing of €330 million, and also this is a very good financial result.

For ISAB Energy, we are already in the ramp-up phase: as I said before, we will be fully on stream by the end of May, which means roughly one month ahead of the schedule. This is a very good result in terms of the team works on this project, and we are also within our budget of investments.

As far as Gas is concerned, the local authority “*Conferenza dei Servizi*” has given its technical green light for Ionio Gas project: we expect the final authorization by end of the first half of this year. Of course we are working on analyzing the product in order to take the final investment decision together with our partners.

Last but not least, of course, the renewables business: we are on track to meet our target to add 430 megawatt installed by 2013, but on top of that we sat up a task force with the top management of the Group in order to define an expansion strategy, to try to achieve a strategic plan, to reach a well balanced and geographically diversified portfolio. Of course, this is also in order to mitigate the regulatory risks on this business.

Thank you for your attention, and now we are ready to take your questions.

Questions & Answers

Operator:

Here is the Chorus Call conference operator. We will now begin the question and answer session. The first question is from Mr. Paolo Citi of Intermonte. Please go ahead, sir.

Paolo Citi:

Hello, good afternoon everyone: just two questions, if I may. The first one is on the Nuce Nord plant: the plant is gaining very attractive margins, if I am correct, roughly €18 per megawatt hour EBITDA margin in the quarter. So in order to better understand, first of all the plant should have an advantage in terms of selling prices in Sicily. Is it possible to have an idea regarding this value? Secondly, regarding these prices in Sicily, do we expect these prices to remain at this level for how many years? Because I think there will be a connection from Terna that should reduce prices in the next few years in the region. And the second question is related to the coastal refining business: if my calculation is correct, you should have reduced the fixed costs for the refinery by roughly €10 million in the quarter, assuming 100% of the refinery. Is it correct? And could this reduction be considered also for the coming quarters? Thanks.

Alessandro Garrone:

Yes, good afternoon. On the IGCC plant, the figure we gave is an estimate of EBITDA on a full-year basis of €50 million or €60 million per year, which is a good number. I agree with you: of course Sicily has a zonal premium, a zonal price higher than the national price, because of the situation of the region in terms of production and demand. Of course we are following the plan of Terna in order to increase the capacity of export (from Sicily to the continent), the power connection should be roughly in 2013; and, of course we have already now in our plans, in our scenario, the reduction of this premium in Sicily which is logical of course. So it's in our figures, it's in our plan in order to calculate the return on this investment. In terms of coastal refining, yes we had lower fixed costs in Q1. This was due to results of the action we are taking in that area

together with LUKOIL: we have a very important project - the name is Sprint - in order to reduce fixed costs in the refinery. At the end of this project (which takes a couple of years) we expect to reach all the savings, to save roughly 10% of fixed costs in the refinery; but we are already seeing some results. Of course, those €10 million are not all related with savings: there are also some carryovers for that, so we will see some of those €10 million coming up in the next quarters. It's difficult to give you an exact figure, but some of those €10 million are real savings.

Paolo Citi:

Thank you

Operator:

The next question is for Mr. Alex Marie of Exane BNP Paribas. Please go ahead, sir.

Alex Marie:

Hi, good afternoon everyone. A few questions please. First of all on your Ionio Gas plant: can you just tell us what are the remaining steps, first in terms of authorization and then what is your schedule for the investment decision and potentially the start-up of the plant? And can you also update us on the CapEx for the plant? If I remember well, it was supposed to be about €100 million, do your share? Secondly on ISAB Energy: did you expect any maintenance shutdowns? When is the next maintenance shutdown basically, once you have re-started the plants? Finally, could you give us also a quick update on 2010 CapEx for the Group? Thank you.

Alessandro Garrone:

Yes. About the Ionio Gas: as I said, we had the technical green light coming from the "Conferenza dei Servizi" which is the step before the *Autorizzazione Unica*. We consider the *Autorizzazione Unica* the big last step on the authorization phase: after that, there will be some other authorizations, but the *Autorizzazione Unica* is the last big step. In parallel of course we are elaborating the industrial turnover of Ionio Gas, considering also that the scenario in the gas market has changed because of the crisis. So, we are working on the plan together with Shell, and we think we will reach the final investment decision by the beginning of 2011. We have also to work on some recommendations that we suppose will arrive from the *Autorizzazione Unica*. We will have to put those recommendations in the investment plan, because normally the recommendations refer to environment, investment *et cetera*. So I think that - due also to the scenario - some more time is required for that.

In term of CapEx, it's difficult today to give you an exact figure. I think the figure you gave is just the equity CapEx on our side, which depends of course on how we will finance the plant. About the cost of the plants: again it could be not easy to say, but on a large range it could be between €600 million and €800 million-900 million. Of course then we have to decide how to finance the plant, and at the end which will be our equity CapEx on the plant.

As far as ISAB Energy is concerned, the next general shutdown will be scheduled for 2012, so it means this year and next year we will have no shutdown in ISAB Energy plants.

To answer your last question about the CapEx: for 2010 we expect CapEx to be about €325 million, 20% lower compared to the 2009 CapEx. We are now working on the four-year business plan, which we will present by the end of this year/beginning of next year. Of course, in order to have a well defined business plan we need to work also on the TotalERG business plan, the new joint venture with Total. But we have still to start on that, because we are waiting for the Antitrust clearance for this agreement.

Alex Marie:

Okay, thank you.

Operator:

As a reminder, if you wish to register for a question please press "*" and "1" on your touchtone telephone. The next question is from Mr. Domenico Ghilotti of Equita. Please go ahead, sir.

Domenico Ghilotti:

Good afternoon, I have three questions. The first is related to ISAB Energy: can you quantify the contribution of the green certificate reimbursement you had in Q1? The second question is a clarification just on the adjusted net profit: it seems to me that you have included let's say a cut of €11 million tax provision in your adjusted net profit, is that right? And the last question is on Nuce Nord: you gave a projection of €50 million to €60 million EBITDA, but you had already around €10 million in Q1, running at half capacity, so I try to understand if you see lower tariffs going forward or any other weaker element to be factored in?

Alessandro Garrone:

Okay, I start from the last question.

Yes, in Q1 we had a good contribution of Nuce Nord: of course the price were quite good, considering also the zonal price in Sicily, and we ran one train of the plant at full capacity because we are now also in a regime where we don't need to have a flexible production. We can use all the capacity of the plants selling the electricity at the full price. So this gave us an advantage for the first quarter compared to the remaining quarters of the plan. So our €50 million-€60 million EBITDA are on an average scenario, on an average basis; of course we had a very good quarter in terms of price.

Paolo Merli:

Domenico, Paolo speaking. Just coming to your first and second question. The green certificates reimbursement during the quarter for ISAB Energy is more or less €4 million. And the second question was related to taxes during the quarter: the 11 you mentioned related mainly to gain on inventories, because of the prices going up. If you look at the replacement cost P&L, the taxes are even much, much lower, of course: just a few millions of euro, mainly related to IRAP.

Domenico Ghilotti:

Okay, thank you.

Paolo Merli:

Thank you.

Operator:

The next question is from Ms. Lydia Rainforth of Barclays Capital. Please go ahead, madam.

Lydia Rainforth:

Thank you, gentlemen. Just a question going back to your safety policies. I think one year ago you did talk about this, enforcements of safety and therefore of the amounts that you were embarking on a safety training program. So have you sort of seen any benefit from that, in terms of how that process has worked? That will be great.

Alessandro Garrone:

I am sorry. I think we have problems with the line: could you repeat again your question a little bit slower?

Lydia Rainforth:

Yeah, thank you. Just one year ago you set out for the plans about focusing on safety issues and sort of doing more training. I was just wondering in terms of the benefits that you have seen from that, and how that plan on safety process is progressing?

Alessandro Garrone:

Now I got your question, thank you. Yes, the safety program is going ahead: we already started with all the action mainly in terms of training people and working on the culture in general of the people. Of course the results take time, but I can say that we had already a very good performance in terms of safety problems in our plan: we had no incident, no injuries in the last two or three quarters, which is already a good result of our safety program.

Lydia Rainforth:

Right. Thank you very much.

Alessandro Garrone:

Thank you.

Operator:

The next question is from Mr. Thomas Adolff of UBS. Please go ahead, sir.

Thomas Adolff:

Good afternoon gentlemen. Just two questions please. Firstly on Plogastel: I understand that it has been kind of completed earlier than expected. When do you expect that to be

fully operational? The second question is in general on the Italian refining market: do you see any closure likely to happen any time soon, or generally how difficult is it to shutdown refineries in Italy? Thank you.

Alessandro Garrone:

Yes, the Plogastel plant is already fully operational since last April this year. In terms of refining closures, or capacity reduction, not looking only at Italy but speaking in general at the OECD zone, we have seen already during the crisis closures of roughly 800,000 barrel a day capacity already shutdown, and there is an estimate (not only in our estimate but also of course in that from EMC etc.) of another 600,000 barrel a day in the next months or years. So this is already a reaction coming from the crisis in the sector. Of course, there are other closures - maybe temporary closures - that could amount at 1,400,000 barrel a day of capacity also during Q2 or Q3 2010. This is already a reaction to the situation. As far as Italy is concerned, there are some weak refineries: we have seen a temporary closure of Cremona Refinery, the one owned by Tamoil. Moreover in Italy we expect closures, or temporary shutdowns, also in the future; it's not easy - not only in Italy - to close definitively a refinery, but I think that in some cases something will happen also in Italy (in some situation also with the help of the government). We have a direct experience as ERG: we closed a refinery some years ago at the end of 80s, and we closed quite a big refinery in Genoa, so we can say we have an experience to close refineries. We don't have any big trouble, but of course now the problem is the occupation: if you close a refinery the main problem is that you have to replace in some way the people working in the refinery. I hope that if the economy start-up again, there will be also opportunity for other jobs.

Thomas Adolff:

Alright, thank you very much.

Alessandro Garrone:

Thank you.

Operator:

Mr. Garrone, there are no more questions registered at this time sir.

Alessandro Garrone:

Okay, so thank you everybody for your attention; we will be in touch for the second quarter results. Goodbye.