



**ERG S.p.A.**  
**“Second Quarter 2011 Results”**  
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**MODERATORS:**

**ALESSANDRO GARRONE, GROUP CEO**

**PAOLO MERLI, CORPORATE FINANCE, CONTROL & INVESTOR RELATIONS**

**Operator:**

Good afternoon. This is the Chorus Call Conference operator. Welcome, and thank you for joining the ERG Second Quarter 2011 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, CEO of ERG. Please go ahead, sir.

**Alessandro Garrone:**

Thank you, and good afternoon ladies and gentlemen. Welcome to this ERG second quarter and first half 2011 results. I am here with Paolo Merli, Head of Corporate Finance, Control and Investor Relations.

I remind you that, in line with the past quarters, the adjusted results include our stake in ISAB S.r.l, the refinery in Sicily - 51% in Q1 and 40% in Q2, after the exercise of the put - and include also the 51% of TotalERG, which became effective on October the 1<sup>st</sup>, last year.

Let me start with the key financials for Q2 and first half 2011. The Q2 adjusted EBITDA at replacement cost came in at €60 million, compared to the €84 million over the same period last year. The year-on-year reduction was the result of a lower contribution of the Refining & Marketing business and also of the power business, partly offset by stronger results from renewables. As far as Refining & Marketing results are concerned, they were negatively affected by a still very tough trading environment, exacerbated by the persistency of the Libyan crisis.

Results from power - although benefiting from the full contribution of the CCGT and ISAB Energy plants - were penalized by some electricity grid limitations in Sicily and by a worse (but still positive) pricing scenario in the area. Whilst renewables figures were sustained by the contribution of new assets acquired in July 2010 (IVPC Power 5) and by the gradual start-up of Fossa del Lupo wind park.

It's worth to remember that the second quarter 2010 results of power benefited from 18 million insurance reimbursement related to ISAB Energy accident occurred in 2008 (for the first half 2010, the reimbursement was €45 million). As far as bottom line, Q2 closed with a net loss of 8 million versus a positive result of €17 million in Q2, 2010.

Looking at our balance sheet, the adjusted net financial position closed at €1,025 million at June-end, compared to the €1,082 million at year-end 2010. The leverage decreased from 36% in 2010 to 35% at the end of June. The slightly reduction of net debt during the first half was mainly driven by the cash-in deriving from the exercise of the 11% of the put, partly compensated by the dividend payment and the CapEx in the period coupled with a slightly negative dynamic of working capital trend. More details will be given later on.

The first half 2011 EBITDA was at €108 million versus the €135 million in the first half 2010. The main driver of the worse results was the oil business, because of the weak refining scenario and of the general turnaround at our ISAB Refinery in Q1, 2011.

The adjusted net profit for the first half 2011 was negative to the tune of €40 million versus a positive €2 million last year. I remind that the first half 2010 results included fiscal benefits related to the so-called "Tremonti-ter".

Before going through the Q2 2011 results, I'd like to highlight some issues like the refining environment, the new wind acquisition and the TotalERG refinancing. Talking about the refining scenario, this is really still very tough (especially in the Mediterranean area), and this is still affecting our economic results and operations. In the first half, oil prices made a steep rise to \$111 per barrel, up 44% year-on-year with lower Ural Brent differential (because of the reduction of import from Black Sea) and higher Azeri Light differentials, mainly reflecting the rise in mid distillates prices coupled with lower availability of Libyan oil, thus affecting the profitability of Med refiners.

EMC margins in the first half 2011 remained negative to the tune of -\$2 per barrel on average and -\$3.2 per barrel in Q2 2011, strongly affected by weak gasoline crack spreads and distillate value not able to compensate higher oil price.

ERG is further affected by the increase in the crude price since there is a time lag in feedstock price - the feedstock for ISAB Energy - which enlarges the margin squeeze temporarily.

Looking at the new wind acquisition, as you remember, on June 2011 ERG announced the signing for the acquisition of IVPC Power 3, which owns five wind park in operations as of 2008 for a total installed capacity of 112 megawatt. The closing of the operation is expected to take place shortly.

In terms of enterprise value, the price paid - based on financial data at the end of June 2011 - was about €2 million per megawatt, and we believe this valuation reflects the very good quality of the assets (the productivity of those assets is above 2,100 equivalent hours, well above the national average) and the recent start of operation (which is also a characteristic of those wind farms), thus giving ERG the possibility to benefit from a safe incentive scheme for the remaining 12 years, because those are young power plants.

The total cash-out for the acquisition will be €133 million, out of which €100 million of equity value and €33 million as a reimbursement of an infragroup debt. All those wind parks are financed partly with a project financing and partly with a financing under the Law 488, which gives favorable financing conditions. This acquisition represents a further step after the acquisition of the 102 megawatt made last year, in the consolidation of the Italian wind sector. ERG is now a first tier operator in the Italian wind sector, being the third wind player in Italy.

In fact after the acquisition of IVPC Power 3, the completion of Fossa del Lupo (which already started producing electricity and will be fully on stream in the third quarter), and Ginestra wind park to be on stream in the second part of the year, ERG will reach 495 megawatt of installed capacity in Italy, becoming the third operator after International Power and Enel Green Power.

I have to say that the data you can see in the graph about our competitors refer to the end of 2010, whilst our figures are the forecast at the end of this year. IVPC Power 3 acquisition represents a further step towards the consolidation of our presence in the Italian wind market, and a key pillar in our recent history: from roughly 200 megawatt installed in 2009 (out of which 145 in Italy) to 310 megawatt in 2010, mainly as a result of the acquisition of IVPC Power 5 and the entry into operation of Plogastel wind park in France. In 2011 our total installed capacity will reach, as I said, 559 megawatt obtained throughout a balanced mix between Buy & Make: 112 megawatts deriving from the acquisition of IVPC Power 3, and 138 megawatt from the entry into operation of Ginestra and Fossa del Lupo.

As far as Fossa del Lupo is concerned, the final installed capacity will be 97.5 megawatt rather than 90 megawatt as previously announced in the 2010-2013 ERG Renew business plan. ERG has now a solid base in terms of wind installed capacity in Italy, and aims at maintaining the actual market share in the coming years.

And now, I'd like to comment about the financing of TotalERG recently announced. On the 4th of August, TotalERG signed a five-year multicurrency loan for €900 million to finance its medium-long term growth. The loan consists in a term loan for €400 million and in a revolving credit facility for €500 million, and lenders are a pool of Italian and international financial entities. An important issue to highlight is that loan is senior, unsecured and without recourse to TotalERG shareholders. Financing conditions and duration are very good, and the loan itself confirms that lending market is confident on TotalERG growth potential.

Just to give you an idea, the cost of debt is about 200 basis point above Euribor on average over the period, which we consider favorable in light of really tough current condition of the lending market.

I'll now hand over to Paolo who will take you through the Q2 results. Thank you.

**Paolo Merli:**

Thanks Alessandro and good afternoon everybody. As usual, I am going to focus my comments on the second quarter, on the right side of the slide. Group EBITDA was €60 million in the quarter against €84 million last year. The decline reflects a lower contribution of both refining & marketing and power & gas, only partly offset by better results in renewables. Year-on-year increasing corporate costs reflect mainly one-offs. As far as Refining & Marketing is concerned, the year-on-year reduction is mainly attributable to severe scenario of Refining business both coastal and inland, while marketing results were more or less in line.

As far as power & gas is concerned, main effects of decline were the high electricity constraints in Sicily for general maintenance on the national grid which affected both plants, but particularly ISAB Energy. This coupled with a worse (but still positive) pricing scenario for CCGT in Sicily. I would remind that results in 2010 over the second quarter included €18 million of insurance reimbursement related to the accident of ISAB Energy

in 2008. It is worth to say that power results were negatively affected by €6 million of credit write-offs during the quarter against €12 million in the same period last year. Those credit write-offs both in Q2 2011 and Q2 2010 were mainly related to a single credit towards AgrigGas, a Swiss gas company which went bankrupt.

Renewable business had an EBITDA of €12 million, more than doubled compared to last year, and benefited from the consolidation of 102 megawatts acquired last year, the gradual entry into operation of Fossa del Lupo wind park, and lower electricity limitations in Southern Italy. These positives were only partly offset by a slowdown in production at our French wind parks.

Let's now comment the pro-forma profit and loss accounts, which includes line by line ERG stakes in our JVs: ISAB with LUKOIL, and TotalERG with Total. Going below EBITDA, depreciation at €57 million (up from 53 last year) is mostly related to the investments and to the entries into operation in power and renewables, partly offset by the lowest stake in ISAB Refinery, from 51% to 40%.

Net financial expenses came in at €4 million, lower year-on-year despite higher net financial position and the interest rates. This is a result of better ForEx exchange differences and some positives from hedgings. Taxes were negative for 3 million, notwithstanding a negative pre-tax result, mainly as a consequence of the regional tax called IRAP. I would remind that in second quarter last year, ERG benefited from the "Tremonti-ter" for about €15 million. This can explain the huge difference.

Minorities were minus €4 million, lower compared to last year, mainly as a result of the lower contribution of ISAB Energy in the period. All these items together led to a net profit of -€8 million in the quarter, against €17 million last year.

On a reported basis, which includes gain on inventory for €12mn and capital gain on the sale of 11% of ISAB Refinery, net profit in second quarter was €107 million, compared to 35 last year. Adjusted net income for first half was negative at €40 million versus a positive figure in 2010 which, as I said, benefited from some fiscal benefits. Reported net income was €110 million in the half year, compared to 41 last year.

Let's now comment business by business, starting from coastal refining. EBITDA during the quarter was broadly in line year-on-year notwithstanding a much worse refining scenario in the Med after the Libya crisis. This is mainly due to a mix of effects which offset - from an economic standpoint - the deterioration of fundamentals.

First of all, positive incomes for about €16 million related to structural inventory destocking following the sale of 11% of ISAB Refinery to LUKOIL, better plants performance following the general turnaround in Q1, lower fixed costs as efficiency program keeps delivering results. It's also worth to notice that variable costs increased less than oil price as a result again of efficiency program underway.

I remind that results over the first half reflected also the 45 days of general turnaround in Q1 on top of course of negative business trends. Investments in Q2 were down year-on-

year partly structural, partly as a result of our lowest stake in the Refinery. They were anyway oriented to efficiency and safety improvements of the Refinery.

Slide 13 shows ISAB Refinery unitary margins versus benchmark. Here I like to draw your attention on EMC, which was negative for more than \$3 per barrel during the quarter. This is a great evidence of the dramatic trading conditions in the period. Our margin was positive for \$4.6 per barrel, thus leading to a premium of almost \$8 per barrel in the period. The reasons behind this large premium are practically the same I just commented.

Lower volumes in the quarter reflects the fact that as of April 1<sup>st</sup>, ERG owns 40% of ISAB Refinery, whilst in the first quarter it was 51%.

Let's now see integrated downstream, which I remind includes 51% of TotalERG and 100% of ERG Oil Sicilia. Marketing came in at €28 million, practically in line with last year notwithstanding lower volumes for industry, with a general decline. This was offset by better retail margins, contribution from specialties (which was inherited from Total) which of course we expect to become much more material as from next year.

Market share of TotalERG was 11.8%, stable quarter-on-quarter. There is here no comparison year-on-year, being there little meaning following the change and scope of consolidation.

I am now at slide 15 with margins and volumes for Inland Refining. In Italy, margins during the period were negative minus 0.74, as a results of strong deterioration in fundamentals since the Libya crisis and turmoil in North Africa. Again in terms of operating data, we are not providing here year-on-year comparison, which wouldn't be much meaningful.

Let's move now to power, starting from ISAB Energy. Production in the quarter was higher year-on-year due to the full operation of both trains, while I remind that last year, the first quarter was running at half capacity.

During the quarter, the plant was affected by some restrictions and also some slowdown associated to those restrictions. EBITDA was €27 million, lower than same period last year, notwithstanding higher volumes. These was due to two factors: as already said, last year there was an item of €18 million related to the insurance reimbursements. And as I said, ISAB Energy performance during the quarter was negatively affected in terms of efficiency by several stop and go during slowdowns.

Looking at the first half results, we are more or less in line year-on-year. I remind you that Italian GAAP EBITDA is lower because of the phase-out of the incentive.

Let's move now to power. Production in the quarter was down year-on-year due to the electricity limitation in May and June, as a results of the general maintenance performed by the grid manager in Sicily. Anyway results remains solid, even though considerably lower than last year as a result, as I said, of lower volumes, and a worse (but still

positive) pricing scenario. I've already said that results include 6 millions of credit write-offs compared to 12 million last year.

Let's move now to renewables. As I said, EBITDA (€12 million) was more than double compared to last year. The positive trend was driven substantially by the contribution of 102 megawatts acquired in July 2010, the partial start-up of Fossa del Lupo since May (whose production was 13 gigawatt hour during the quarter), higher production also for the remaining wind parks in Italy, mainly as a result of lower electricity constraints in the period. Those items were partly offset by lower production for France wind parks.

Prices of power sold remained pretty flat, while green certificates were slightly down as a result of the new decree which set the green certificates price at 78% of the difference between 180 and the price of electricity.

Let's now move to investments, which were €51 million during the quarter (-28% vs 71 last year): 41% of investment in the period were in the Refining & Marketing, of which 50% associated to ISAB Refinery maintenance and 50% to our TotalERG and ERG Oil Sicilia, mainly related to some developments in retail business.

Power accounted for 12%, mainly related to the construction of a minor ancillary plant, while 45% of investments were in the renewables. Let me just give you a quick update about investments in renewables. They were mainly associated to construction works for Fossa del Lupo, which are now completed: all the capacity is already installed and is in service for about 65 megawatt. As Alessandro said, the total capacity of the plant is 98 megawatts against the 90 previously announced, as we finally implemented a different layout for the park.

As far as Ginestra is concerned, construction works are practically finalized. We still have to complete the grid connection which for the time being is still provisional. The park has already started producing in July, and we expect it to come at full speed by the end of the year.

Let's see now cash flow over the period. Net financial position decreased from €1,226 million to €1,025 million, more or less a decline of €200 million. The main effects were the sale of 11% of ISAB Refinery, which determined a cash-in of €241 million, a better working capital for €78 million, which includes the sale of green certificates for about €30 million. Cash flow from operation for €40 million, which is still weak as a result of trends already commented. These positives were partly offset by distribution of dividends for about €62 million, taxes and other liabilities for €51 million, and investments of €45 million in the period.

Leverage went down accordingly from 39% to 35%, adjusting net debt for our JVs. We come to a net debt reported of €706 million, with a leverage of 27%.

Thank you very much. And now back to Alessandro.

**Alessandro Garrone:**

Yeah, thank you, Paolo. I will comment just the last slide about the 2011 economic guidance. As far as our Refining & Marketing is concerned, we still see a very weak refining environment as the Libyan crisis is not finished. So this will impact a lot on the refining margins in the Med area. The marketing is benefiting from the TotalERG synergies, so this is a better result compared to last year. We will see lower volumes, and that as a result of ISAB shutdown in first quarter and of course of the exercise of 11% put.

For the power & gas business, we see similar results a little bit lower compared to last year. The contribution of the CCGT Plant will be for the full year, but with lower margins expected: as we said before, the tough scenario for the CCGT will be partly offset by the geographical positioning, and so the premium on the Sicilian price - even if lower than last year - will help the results of this business.

The ISAB Energy production is expected at 3.7 terawatt hour, because we will have a maintenance shutdown in the second half of this year.

As far as renewables are concerned, we see much better results compared to last year. First of all, for the contribution of new assets, the 102 megawatt acquired last year plus the 112 megawatt as - and I can announce it in real time - we have just signed the closing for the acquisition of IVPC Power 3. So starting from tomorrow the production of IVPC Power 3 will be in our account.

Then during 2011 - as Paolo said - we have the start-up of Fossa del Lupo, and of course of Ginestra a little bit later, and those two wind farms were not running last year.

A negative point for renewables is that we still have some constrains due to maintenance work on the national grid by Terna, but also those are reducing compared to previous year.

So, thank you for your attention, now we are ready to answer your questions. Thanks.

## Questions & Answers

**Operator:**

Excuse me. This is the Chorus Call conference operator. We will now begin the questions and answers session. The first question is from Lydia Rainforth of Barclays Capital. Please go ahead.

**Lydia Rainforth:**

Thank you, and good afternoon gentlemen. Two or three questions, if I could. Firstly, you mentioned the efficiency program for the Coastal Refinery, I was just wondering if you could give us more details of what sort of things you've actually undertaken and how

much more you feel that has to do? And then secondly, are you able at this stage to give us an idea of what synergies are available through the TotalERG joint venture? And then finally, I just ask in terms of the Refining situation: does that change the way you look at the option you have to sell the rest of the business to LUKOIL? I know it is going to be a next year issue, but I am just wondering, how do you feel from that evolving whether they are determined by what your outlook for the market is? Thank you.

**Paolo Merli:**

Lydia hi, Paolo speaking. About the efficiency in the ISAB Refinery over the first half of the year, the reduction in fixed costs was for about a couple of million of Euro, of course if adjusted for the sale of our 11%. This doesn't seem a very big number, but you have to consider that last year fixed costs were reduced considerably. So I think it is a great achievement to have offset inflation here. We are now working on variable costs: in fact, if you look at them, they have increased, but much less than they were supposed to in the current trading environment, thanks to the efficiency program which keeps delivering results.

**Alessandro Garrone:**

Yes, about the second question on the synergies in TotalERG, that it's a little bit early to quantify exactly the synergy, but I can say that the integration is growing very well. As you probably remember, we made last year provision for €32 million in Q4 last year, and we spent in the first half 2011 €2.6 million out of those provisions for the actions to be taken for delivery the synergies in the future. So, as far as we can see now, I can just confirm that we expect total synergies of about €40 million for the 100% of TotalERG, which means €20 million on our shares. And really we see that the integration is growing very well. We have seen a little bit of decrease in volumes, but also because we are really concentrated in the re-integration, rationalization of the retail in order to get the best synergies in the future. Coming to your third question - and I expected that - I should answer always in the same way: as you said, we have time, we can exercise the put starting from February next year. So of course we are working on that, considering the tough scenario today, looking at the evolution of the scenario. The final decision will be taken by the end of this year, and of course we really need to understand in the best way the short and the long-term scenario in this business. And I still confirm we have the experience and the skills to manage such a business, but of course we have also to see the value creation for our shareholders. So it's really an item that we have on the table everyday.

**Lydia Rainforth:**

Okay, that's great. Thank you very much for your help gentlemen.

**Alessandro Garrone:**

Thank you.

**Operator:**

The next question is from Roberto Ranieri of Banca IMI. Please go ahead.

**Roberto Ranieri:**

Yes good afternoon gentlemen. Three questions, please. The first one is just a clarification about the TotalERG synergies and the investments probably you are doing: this recent financing scheme you had for €900 million I understand that it is for the rehabilitation or investments on re-brand of gas stations or are there also some other options you are looking at for increasing market share, or increasing the number of gas stations, the efficiency or something like that. At the end of the day, my question is if those investments have given you in the medium and long term additional synergies about the target you have over €40 million and additional EBITDA: that's my first question. And the second question shortly is about the power price in Sicily so this premium of the power prices in Sicily, do you think that this is reducing and this is the trend we are going to expect in the medium and long term, so from 2011 and onwards, or do you think that it will recover in a few months? Third question is about the upgrade investments you had in the Coastal Refinery: which was the effect in the second quarter and can you give us also an estimate of the effect of this upgrade investments and in terms of additional Euro million of EBITDA from 2011 and onwards? Thank you very much.

**Alessandro Garrone:**

Yes, Roberto. About TotalERG financing, €900 million is the maximum need estimated for TotalERG to manage the business as it is, and of course we had some investments in re-branding *et cetera*, but in those €900 million it is not included any extraordinary investment. Of course we look at TotalERG as a vehicle to take opportunities in Italy in that market in the future, but this will be a decision that has to be made by the shareholders, and they will of course put extra equity if there is any opportunity in Italy. But those €900 million are just for normal operations in need of working capital, investments *et cetera*. So without adding any further EBITDA to what we announced, I mean more than the one that was expected when we have made the deal. On the Sicilian price in the power this differential is going up and down: it depends on the situation of the production in Sicily, the maintenance of the power plants *et cetera*. So for instance in second quarter 2011, this premium was €30 per megawatt; last year it was 35, so it was lower, but not so lower. In the first half it was 22, compared to 33 last year, but really it depends on the situation of the production in the island. If you look at long term, we expect Terna should start the important investments to increase the transmission capacity between Calabria and Sicily. When these investments will be completed, we expect of course that the Sicilian price will be aligned with the national average prices. But that will be in 2013 or later.

**Paolo Merli:**

To talk about investments, really we will not have major investments in the ISAB Refinery which can change materially our EBITDA. So the investments we made over the first half of the year were mainly related to maintenance and some minor efficiency program to improve, as I said, fixed and variable costs, but I wouldn't be fair at saying that we should expect major impact in terms of EBITDA from those investments.

**Roberto Ranieri:**

Okay, thank you very much.

**Operator:**

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

**Domenico Ghilotti:**

Good afternoon. I have few questions, the first is related to the Refinery performance: I would like to understand or have a clarification on the 16 million benefit you had on inventory: it is structured, but not sustainable, is it correct? And the second question still on refining is on the throughput: you are running well below the 300,000 barrel per day. So I would like to understand: will you continue to run lower runs and as long as the margins are so weak? Then I have a question on integrated downstream: is there any update on the Rome Refinery? And the third question is on power generation: I would like to understand if the constraints in ISAB and ERG Power production have being solved or not, so shall we have to expect some constraints also in the second part of the year?

**Alessandro Garrone:**

Yes, about destocking effect we had a destocking with the main impact on Q2 of €16 million. We had the same effect last year in the same quarter, that was €9.4 million. And in first half 2011, the destocking effect was as we said €23 million. This benefit is not only because of the oil price arises, but it's also a consequence of the exercise of the put. So of course we reduced our stocks, because our throughput in the refinery is lower. So it's a one-off effect positive fortunately because the prices went up.

**Domenico Ghilotti:**

Okay.

**Alessandro Garrone:**

About the throughput, we had lower throughput mainly because of course we tried to program the refinery looking at the scenario and the prices and the margins. So when the scenario is not good, we tend to reduce the throughput and especially to use heavy residues instead of crude oil, in order to reduce the topping, the primary distillation used, and to fuel the conversion capacity plants. So that is just a question of programming the refinery and trying to get all the positive economies from that, no other reasons, no main other reasons. The third question was....

**Domenico Ghilotti:**

About refineries, is there any update?

**Alessandro Garrone:**

No update on that, and the answer is the same as before: together with Total we are working on the future plans of these assets in order to find the best solution to extract value from those assets. Of course at the moment the refinery has a very low margin even if it is located in a very good position.

**Domenico Ghilotti:**

And the last question was on the constraints for ERG Power and ISAB.

**Paolo Merli:**

Yeah, I confirm that over the first half of the year we had several constrictions by Terna, which was performing a general maintenance on the national grid in Sicily. This was particularly in May and June, both for ISAB Energy and ERG Power plant. This was one of the reason driving up the zonal premium during the second quarter. As we already said, over the second half of the year we just expect to have the general shutdown for 35 days for ISAB Energy, but minor Terna limitations, anyway in the same period of our general turnaround.

**Domenico Ghilotti:**

Okay. And just a follow up on the financing for TotalERG: have you swapped part of your debt into fixed, or is it fully variable?

**Paolo Merli:**

Yeah, just few parts but they are not material. So the financing is €400 million term loan and €500 million as a revolving credit facilities, but we do not have a swap material part on fixed.

**Domenico Ghilotti:**

Okay, thank you.

**Operator:**

Gentlemen, there are no more questions registered at this time.

**Alessandro Garrone:**

Okay. So I think we can close the conference call. Thank you everybody for the attention. The next webcast will be in November for the third quarter results. I hope to have better news on the refining situation and I wish you if it's possible a good summer to everybody. Bye-bye.

**Paolo Merli:**

Bye.