

ENSE

Issuer	Issue Rating	Outlook
Entidade Nacional para o Setor Energético, E. P. E.	BBB- Medium and Long Term	Stable

RATING DATE
9 September 2019

NEXT REVIEW DATE
9 September 2020

INITIAL RATING
2 June 2008

LAST REVIEW
7 September 2018

PERIOD OF ANALYSIS
Historic: 2014 to 1Q 2019
Forecast: 2019 and 2020

INFORMATION ANALYSED
ENSE Reports and Accounts
ENSE Interim Accounts
ENSE 2019 and 2020 Budget
Details on ENSE's Reserves
World Bank's Commodity
Markets Outlook
Peers Reports and Accounts

METHODOLOGY APPLIED
ARC Ratings' Corporate Entities
Rating Methodology available at
www.arcratings.com

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RATING RATIONALE

ARC Ratings, S.A. (ARC Ratings) has upgraded to "BBB-", with Stable outlook, from 'BB+', with Positive outlook, the rating accorded to the EUR 360.0 million bond issued by Entidade Nacional para o Setor Energético, E. P. E. (ENSE), on 6 August 2008. This rating action is based on the sovereign rating upgrade in May 2019, in the context of a decrease of the company's net financial debt, recovery of oil prices in 2019 that is expected to be sustainable according to general forecasts, and, consequently, the recovery of the coverage of net financial debt by the reserves at market value. In addition, being a "State corporate entity", ARC Ratings assumes that if ENSE's monitoring activity of all energy sectors is not self-sustaining, it will benefit from Portuguese Government financing.

COMPANY PROFILE

ENSE, formerly designated ENMC - Entidade Nacional para o Mercado de Combustíveis, E.P.E. and before that EGREP - Entidade Gestora de Reservas Estratégicas de Produtos Petrolíferos, E.P.E., was founded in 2004 and headquartered in Portugal, remains a State-owned entity and was assigned by law with the duty of being the Portuguese central stockholding entity in the acquisition and maintenance of the strategic portion of national emergency reserves of oil and oil products (its main activity).

In August 2018, within the reorganization of public entities with responsibilities in the energy sector in Portugal, the company's duty of supervision was enlarged to cover all energy sectors (including electricity and natural gas). ENSE still manages and monitors the storage activities for crude oil and its derivatives throughout the national territory, in order to guarantee and supply of crude oil and petroleum products, depending on consumption needs.

ENSE'S KEY RATING DRIVERS INCLUDE:

- Government ownership** – ENSE's share capital is wholly owned by the Portuguese Government and the bond has an ownership clause regarding the maintenance of this sole ownership by the Portuguese Government. Consequently, its rating is indirectly linked to the ratings of the Portuguese Republic (BBB / Stable / A-2), however there is no obligation of timely support, but the Portuguese Government, as is established in law, is ultimately responsible for ENSE's liabilities ("in the case of dissolution of ENSE, the State assumes any losses arising from the liquidation of assets, as well as the residual responsibilities").

- Favourable debt profile– ENSE’s debt levels remain largely unchanged, still comprising solely the bond that is rated in an amount of EUR 360 million, maturing in 2028. Above all, ENSE’s expenses (including bond interests) have been totally covered by revenues, mainly originated from the oil market operators. The investments in Portuguese Government issued debt securities increased and the cash position remained positive, allowing to decrease the company’s net financial debt.
- Stable, long-term relationships with key customers – The entity has developed strong, mutually beneficial relationships with the main distributors of oil products in Portugal: Galp Energia, SGPS, S.A. (Galp Energia), Repsol, S.A. (Repsol), BP p.l.c. (BP) and Compañía Española de Petróleos S.A. (CEPSA).

THE KEY CONSTRAINTS ON ENSE’S CREDIT RATING ARE:

- Oil price volatility and the coverage of the loan by reserves – The nature of ENSE’s operations and concentration of its assets render its financial performance heavily exposed to oil price fluctuations. In fact, the oil price drop trend in the last two months of 2018, reaching the minimum price at the end of 2018, led the coverage of financial debt by reserves to decrease to 0.91 times (from 1.12 times at the end of 2017). However, the recovery of the oil price allowed this to improve coverage to 1.23 times at the end of March 2019 (the highest coverage achieved since 2014). The coverage of net financial debt by reserves was still above 1 times (1.07 times) at the end of 2018 and increased to 1.46 times at the end of March 2019 (compared with 1.31 times at the end of 2017).
- Concentration of customer base – Despite some decrease over 2018, compared to 2017, the majority of ENSE’s revenue derived from five companies: Galp Energia (that represented 26% of ENSE’s revenues in 2018), Repsol (24.2%), BP (close to 20%), Prio Supply, S.A. (10.5%) and CEPSA (9.5%).

SHAREHOLDER AND CORPORATE GOVERNANCE

ENSE’s share capital is wholly owned by the Portuguese Government, being a “State corporate entity” with administrative, financial and patrimonial autonomy.

ENSE was assigned by law, since its foundation, with the duty of being the Portuguese central stockholding entity in the acquisition and maintenance of the strategic portion of national emergency reserves of oil and petroleum products. The company is responsible for maintaining a continuously updated record of emergency reserves containing the information necessary for its respective control. Until 1st September of 2018 the company’s additional responsibilities included the supervision of the National Petroleum System, monitoring the markets for crude oil, oil products, liquefied petroleum gas (LPG), biofuels, promotion of technical safety and fuel quality, as well as prospecting, research, development and exploitation of oil resources.

Within the reorganization of public entities with responsibilities in the energy sector in Portugal, by the Decree-Law 69/2018 (published on 27 August 2018 and in force since 1st September of 2018), ENSE also became responsible for monitoring electricity and natural gas sectors. Therefore, in addition to its main activity, ENSE was also assigned with the duty of supervision and prevention of compliance with legislation regulating the exercise of economic activities in the energy sector. On the other hand, ENSE is still managing and monitoring the storage activities of crude oil and its derivatives throughout the national territory, in order to guarantee and supply of crude oil and petroleum products, depending on consumption needs.

National emergency reserves of oil and petroleum products comprise ninety days of the nation's average daily net imports of crude oil and oil products from the preceding year and its acquisition and maintenance are an obligation of oil market operators, distributed according to each market share. The share of reserves to be held by ENSE (strategic reserves), in substitution of market operators, corresponds to "one-third of the reserves which the bound operators are obliged to maintain", i.e. 30 days of the nation's average daily net imports of crude oil and oil products from the preceding year.

According to the terms of the law, the following continues to apply for ENSE:

- In the case of dissolution of the company, the State assumes any losses arising from the liquidation of assets, as well as the residual responsibilities.
- The expenses associated with the build-up and maintenance of strategic reserves by the company are fully supported by operators obliged to build-up of emergency reserves.
- ENSE is obliged to create a provision fund (recorded in equity) by annual increases, aiming to achieve at least an amount corresponding to 25% of the oil reserves' acquisition cost (at the end of March 2019 the provision fund corresponded to 11.2% of oil reserves' acquisition cost, a percentage that has been increasing since the end of 2014).
- In the case of an energy crisis or severe supply disruption, if ENSE sells strategic reserves of oil products in a situation where proceeds obtained are insufficient to cover the average acquisition cost of product, less the amount resulting from the proportional use of the provision fund, the State assumes the corresponding loss by making an extraordinary contribution to the fund.

On 13 August 2019 ARC Ratings met with senior management of ENSE to carry out the onsite review as part of the analytical rating review process.

CASH FLOW GENERATING CAPACITY AND RECENT DEVELOPMENTS

The total volume of oil products introduced for consumption in Portugal increased 2.3% in 2018, to 8.25 million tonnes (Mton), compared with an 2.9% increase in 2017. As occurred in 2017, increases in B (diesel) and D (liquefied petroleum gases – LPG) more than offset decreases registered in A (gasoline) and C (fuel oil) categories. The volume mix of oil products introduced for consumption in Portugal did not change materially, with the B category representing 78.5% and the A category 12.7%, while the D category accounted for 6.2% and the C only for 2.6%. In the context of the increase in the total volume of oil products introduced for consumption in Portugal, the required nation's minimum emergency reserves (90 days) and ENSE's strategic reserves (30 days) also increased 2.3% in aggregate in 2018, to 2,034.2 thousand tonnes (tton) and 678.1 tton, respectively.

ENSE slightly increased its own reserves to 938.6 tton at the end of 2018, while its reserves contracted under CSO Tickets (Compulsory Stockholding Obligation) slightly decreased to 301.5 tton, from respectively 938.1 tton and 303.5 tton at the end of 2017. Nevertheless, ENSE continued to present substantial headroom between its mentioned own reserves and the legally required strategic reserves (678.1 tton), with significant headroom in all categories, allowing ENSE to continue replacing part of the operators' own obligation. Therefore, globally in all categories, at the end of 2018 ENSE held 51.6 days of the total volume of oil products introduced for consumption in Portugal in 2018 (instead of the required minimum of 30 days). CSO Tickets are contracted according to market demand for ENSE to replace the market operators.

The analysis of the composition of the reserves held by ENSE at the end of 2018 shows that: ENSE continues to own the majority of the reserves (75.7%), with the remainder being contracted under CSO Tickets; the totality of ENSE's own reserves were stored in Portugal, while the 24.3% of reserves contracted under CSO tickets were stored outside Portugal; and finished products represented 36.7% of the total stocks (compared with one third required by law and 44.3% at the end of 2017).

The storage of ENSE's own reserves in Portugal continued to be carried out under agreements with Galp Energia (mostly stored near Galp Energia's oil refineries in Matosinhos, near Porto in the North of Portugal, and Sines, in the South of Portugal), and with the Portuguese Government (for the POL NATO deposits near Lisbon). ENSE is studying storage alternatives, namely the possibility of future storage in caverns in Portugal, which presents some advantages due to their underground location.

ENSE'S RESERVES OF CRUDE OIL AND OIL PRODUCTS (IN TONNES AT END OF THE PERIOD)

	2014	2015	2016	2017	2018
OWN RESERVES	948,325	938,273	938,192	938,018	938,603
CRUDE OIL	548,081	538,082	538,082	538,082	538,082
GASOLINE	51,400	51,400	51,400	51,400	51,400
DIESEL	297,844	297,791	297,710	297,536	298,122
FUEL OIL	45,000	45,000	45,000	45,000	45,000
LPG	6,000	6,000	6,000	6,000	6,000
UNDER CSO TICKETS	396,401	140,000	249,000	303,500	301,500
CRUDE OIL	324,501	110,000	149,000	153,500	246,500
GASOLINE	0	10,000	0	0	0
DIESEL	31,900	20,000	100,000	0	55,000
FUEL OIL	40,000	0	0	150,000	0
LPG	0	0	0	0	0
TOTAL ENSE'S RESERVES	1,344,726	1,078,273	1,187,192	1,241,518	1,240,103
CRUDE OIL	872,582	648,082	687,082	691,582	784,582
GASOLINE	51,400	61,400	51,400	51,400	51,400
DIESEL	329,744	317,791	397,710	297,536	353,122
FUEL OIL	85,000	45,000	45,000	195,000	45,000
LPG	6,000	6,000	6,000	6,000	6,000
TOTAL ENSE'S RESERVES IN DAYS OF CONSUMPTION					
GASOLINE	60	51	50	45	48
DIESEL	64	50	47	45	50
OTHER	170	75	43	112	54

Source:
ENSE.

The use of the POL NATO deposits by ENSE is done under an agreement dated 1 July 2016 for a 25 years period. Under this agreement, ENSE pay an annual fee of EUR 1.1 million (annually updated by the inflation rate of previous year) that can be reduced, with a low of EUR 0.4 million, if the difference is spent by ENSE in the management and improvement of the infrastructure. This was an important agreement for ENSE due to the lack of historical investments made by the Portuguese Government in the infrastructure. Under this agreement ENSE has the obligation to make additional investments, initiated in 2017, and was EUR 0.6 million in 2018. According to ENSE's 2019 forecasts, dated December 2018, this investment amount was moderate and could reach EUR 1.6 million in

2019, EUR 1.1 million in 2020 and EUR 1.9 million in 2021. The realization of this priority investment plan will allow significant improvements in the conditions of those strategic facilities and aim to provide them with greater operational, maintenance and mobilization capacity where part of the strategic reserves are located. ENSE plans to finance these investments with its own funds (its short-term financial assets – cash, deposits and short-term investments in debt securities issued by the Portuguese Government – were EUR 45 million at the end of March 2019 and are expected to stabilise at this level).

ENSE's revenues from the main activity (holding and managing reserves of crude oil and oil products), corresponds to the recovery of its expenses on this activity from oil market operators, aiming to have a net profit in this activity tending to zero (except for gains or losses in the valuation or in the sale of reserves), and the amounts to be received are calculated every year based on the expenses forecasted by ENSE. Occasionally ENSE may sell oil reserves, as occurred in 2013 and 2014. Until now, expenses with the other activities (much lower) needs to be covered by these activities' revenues.

Hence, ENSE's turnover continues to be mainly originated from the main distributors of oil products in Portugal, namely:

- Galp Energia (28% of ENSE's revenues), the market leader; Galp Energia is not rated; Galp Energia is also ENSE's main supplier of reserves storage;
- Repsol (in 2018 represented 24.2% of ENSE's revenues), which is not rated by ARC (BBB / Positive / A-2 by Standard & Poor's Financial Services LLC (S&P); Baa1 / Stable by Moody's Investors Service, Inc. (Moody's); and BBB / Positive / F2 by Fitch Ratings, Inc. (Fitch));
- BP (close to 20%), which is not rated by ARC (A- / Positive / A-2 by S&P; A1 / Stable by Moody's; and A / Stable by Fitch);
- Prio Supply, S.A. (10.5%), a Portuguese company not rated; and
- CEPESA (9.5%), which is not rated by ARC (BBB- / Stable / A-3 by S&P; Baa3 / Stable by Moody's; BBB- / Positive by Fitch).

Regarding the 2018 ENSE's operational expenses, it should be noted the increase of subcontractors' costs related to the acquisition of CSO Tickets to EUR 4.6 million. This represent a deviation of EUR 0.9 million compared with the forecast, due to higher acquisitions and higher average price and of EUR 3.1 million compared to the 2017 figure. The largest CSO purchase in 2018 aimed at taking advantage of a good moment for oil prices (when futures were already rising). On the other hand, the longer the ticket contracting period, the better the trading conditions. Therefore, through this instrument ENSE aims to improve its storage costs.

Regarding ENSE's 2018 operational expenses, it is also worth mentioning the absence of rotation of diesel stocks in the POL NATO infrastructure (as occurred in 2017) which represented a cost savings of EUR 1.5 million against the forecast.

As mentioned, ENSE's financial statements are impacted by the oil price volatility (an external factor) in the book value of its oil reserves. In 2018, despite the average oil price increasing by 29% against the 2017 figure, according to World Bank report dated April 2019, the oil price volatility had a negative impact due to the oil price drop trend in the last two months of 2018. The minimum oil price reached at the end of 2018 led the company to record an impairment loss of EUR 26.1 million, given that its oil reserves were recorded by the lower of its market value or

acquisition cost. Conversely, in 2017 the company recorded a reversal of impairment loss of EUR 5.3 million (related to part of the significant impairment losses recorded in 2015, EUR 85.3 million, and in 2014, EUR 54.3 million).

ENSE - FINANCIALS AND RATIOS (THOUSAND EUROS)

	2014	2015	2016	2017	2018	2018 Jan to Mar	2019 Jan to Mar	2019 (F)	2020 (F)
TURNOVER	79,747	24,562	24,331	25,398	24,266	5,988	6,345	25,310	26,150
EBITDA	32,839	8,519	6,857	7,722	2,958	935	1,332	424	945
EBIT	(21,927)	(76,845)	114,371	12,744	(23,684)	855	1,221	(158)	214
FINANCIAL RESULT	(859)	(41)	625	659	647	169	169	611	611
NON-CURRENT RESULTS	(4,067)	(7,802)	(7,518)	(7,931)	(20)	(1,005)	(566)	2,235	(2,256)
NET PROFIT	(26,869)	(84,707)	107,477	5,460	(23,386)	19	824	2,688	(1,432)
OPERATING CASH FLOW (OCF)	7,208	9,425	9,825	11,912	3,219	3,260	1,721	730	1,236
FREE CASH FLOW	(12,736)	14,335	9,053	11,785	2,690	3,089	1,593	(691)	15
RESERVES' BOOK VALUE	321,091	235,750	343,337	348,590	322,727	348,590	322,727	355,903	355,903
RESERVES' MARKET VALUE	333,087	237,087	385,418	403,831	327,926	399,233	443,257	387,496	387,496
TOTAL ASSETS	350,867	270,790	387,783	404,310	381,729	406,915	383,279	414,385	415,231
NET WORKING CAPITAL (NWC)	335,221	256,289	370,532	383,543	364,383	384,436	365,587	397,133	397,181
NET WORKING CAP. REQUIREMENTS (NWCR)	321,212	234,817	343,341	348,233	323,095	346,385	323,039	356,005	355,963
NET CASH POSITION (NCP)	14,009	21,473	27,191	35,310	41,288	38,050	42,548	41,129	41,218
FINANCIAL DEBT	360,013	359,676	359,539	359,583	359,632	359,583	359,632	359,670	359,714
NET FINANCIAL DEBT*	343,971	329,298	320,098	308,357	305,716	305,100	303,945	307,761	307,790
RESERVES' MARKET VALUE / FINANCIAL DEBT	0.93	0.66	1.07	1.12	0.91	1.11	1.23	1.08	1.08
RESERVES' MARKET VALUE / NET FINANCIAL DEBT	0.97	0.72	1.20	1.31	1.07	1.31	1.46	1.26	1.26
Contribution Margin (%)	41.8%	35.7%	31.4%	34.3%	18.5%	20.8%	26.4%	1.4%	12.1%
EBITDA Margin (%)	41.2%	34.7%	28.2%	30.4%	12.2%	15.6%	21.0%	1.7%	3.6%
Operating Return on Turnover (%)	(27.5%)	(312.9%)	470.1%	50.2%	(97.6%)	14.3%	19.2%	-0.6%	0.8%
Operating Return on Assets (%)	(6.2%)	(28.4%)	29.5%	3.2%	(6.2%)	0.8%	1.3%	(0.0%)	0.1%
Gross Cost of Borrowed Funds (%)	0.4%	0.2%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net Return on Turnover (%)	(33.7%)	(344.9%)	441.7%	21.5%	(96.4%)	0.3%	13.0%	10.6%	(5.5%)
Payout Ratio (%)	0%	0%	0%	0%	0%	0%	0%	0%	0%
Coverage of Interest Costs by EBITDA (x)	20.7	11.6	80.3	206.3	79.0	-	-	-	-
Coverage of Net Interest Costs by EBITDA (x)	38.2	209.8	-	-	-	-	-	-	-
CASH FLOW Coverage of Net Interest Paid (x)	(11.0)	27.2	-	-	-	-	-	-	-
Financial Debt / EBITDA (x)	11.0	42.2	52.4	46.6	121.6	96.2	67.5	848.1	380.6
Net Financial Debt/ EBITDA (x)	10.5	38.7	46.7	39.9	103.4	81.6	57.0	725.7	325.6
CASH FLOW Coverage of Net Financial Debt (%)	(3.7%)	4.4%	2.9%	3.9%	1.1%	n.av.	n.av.	n.av.	n.av.
Equity / Assets (%)	(4.7%)	(34.4%)	5.6%	8.7%	4.3%	8.9%	4.6%	12.1%	12.3%
NET GEARING (Net Debt to Equity) (x)	(21.0)	(3.5)	14.7	8.8	18.8	8.4	17.2	6.1	6.0

Notes:

Figures rounded.

Accounts adjusted by ARC Ratings for analysis purposes.

2014 annual accounts audited by Caiano Pereira, António e José Reimão, S.R.O.C.. 2015 - 2017 period annual accounts audited by Moore Stephens & Associados, S.R.O.

2018 annual accounts audited by Vitor Almeida & Associados, S.R.O.C., S.A..

*Financial debt net from cash and deposits and also from investments in debt securities issued by the Portuguese Government.

**Assumed by oil operators, not ENSE.

Sources:

ENSE.

In the context of negative 6-months Euribor, interest costs, which are allocated to the activity of managing oil reserves (the financial debt was contracted to finance the acquisition of oil reserves), were not significant in 2018. ENSE has not paid interest in 2018, as occurred in 2017. In these conditions, the company continued to present positive financial result, mainly reflecting interest gains from the investments in debt securities issued by the

Portuguese Government. Thus, the coverage of interest costs by EBITDA remained high, at 79.0 times (compared with 206.3 times in 2017 and 80.3 times in 2016).

In 2018 ENSE made an increase in the provision fund in the amount of EUR 4.5 million (a EUR 0.5 million positive deviation compared to the forecast). In 2017, in the context of favourable conditions, the increase in the provision fund was EUR 7.9 million, compensating for the lower increases made in previous years (including none in 2014) and in order to present a pre-tax result of nil before recording the impairment loss reversal on inventory. For all periods analysed, ARC Ratings considered the costs with the provision fund as non-current, not affecting EBITDA and EBIT.

In addition, in 2018 ARC Ratings also considered as non-current EUR 4.5 million of guarantees enforced. This value was received in 2017 but only recognised as a gain in 2018, given that the company was awaiting confirmation regarding which entity should recognize it.

ENSE recorded a loss of EUR 23.4 million in 2018, mainly due to the impairment loss, which is crucial for the company's results. Therefore, in the context of reversal of impairment loss, in 2017 and in 2016 ENSE presented net profit of EUR 5.5 million and EUR 107.5 million in 2016, respectively.

Since 2016, by the Law 7-A/2016, ENSE's profits on the activity of managing strategic reserves of oil products became exempt from corporate taxes.

The 2018 auditor's report was issued without qualifications, as in previous years.

In the first quarter 2019, i.e. the first period with the new responsibilities of ENSE, the company showed EUR 0.8 million of net profit, in the context of EUR 1.3 million of EBITDA, positive financial result, EUR 0.6 million increase in the provision fund and no change on the book value of strategic reserves of oil products. The company only calculate the impairment of loss or the reversal of this impairment at end of December. Thus, the impact of the recovery of oil prices in the first quarter of 2019 not was reflected in the financial statements, as usual.

FINANCIAL POLICY

At the end of 2018 ENSE's assets totalled EUR 381.7 million, which represents a decrease of EUR 22.6 million, equivalent to -5.6%, comparing to the end of 2017. The company's oil reserves, after the mentioned impairment loss of EUR 26.1 million, accounted for EUR 322.7 million, which was EUR 5.2 million below its market value at the closing of 2018. The total amount of cash and deposits and short-term investments in debt securities issued by the Portuguese Government increased by EUR 2.7 million, to EUR 43.4 million at the end of 2018, while the amount invested in medium and long-term debt securities issued by the Portuguese Government was maintained at EUR 10.1 million.

In the first quarter of 2019 ENSE's assets slightly increased to EUR 383.3 million, reflecting the increase in the total amount of cash and deposits, short-term investments and medium and long-term investments in debt securities issued by the Portuguese Government to EUR 55.7 million (a EUR 1.8 million increase against the end of 2018).

ENSE made investments in fixed assets in the total amount of EUR 0.8 million in 2018 (EUR 0.4 million in 2017), mainly including EUR 0.6 million of investments in the POL NATO and EUR 0.1 million in IT systems and help desk. In the first quarter of 2019 the amount of investments carried out in fixed assets was EUR 0.2 million.

ENSE's equity dropped to EUR 16.3 million at the end of 2018 (from EUR 35.1 million at the end of 2017) mainly due to the company's loss in 2018, in part offset by the increase of the provision fund. At the end of March 2019,

the company's equity increased to EUR 17.7 million, benefiting from its net profit and the increase of the provision fund in the first quarter of 2019. The provision fund increased from EUR 37 million at the end of 2017 to EUR 42.1 million at the end of March 2019. At that date the provision fund corresponded to 11.2% of reserves' acquisition cost (compared with 9.9% at the end of 2017) and was totally covered (122.6%) by a portfolio of debt securities issued by the Portuguese Government (the medium and long-term debt securities covered 25.3% of the provision fund).

The equity / assets ratio of ENSE remains positive, despite decreasing from 8.9% at the end of March 2018 to 4.3% at the end of 2018 and slightly recovering to 4.6% at the end of March 2019.

Notwithstanding the decrease of the company's net financial debt in 2018 and in the first quarter 2019, the net gearing ratio increased to 18.8 times at the end of 2018 and somewhat improved to 17.2 times at the end of March 2019, compared with 8.4 times at the end of March 2018. The increase of the net gearing ratio was determined by the significant decline in the company's equity, mentioned above. The recovery of oil prices in the first quarter of 2019 was not recognized in the company's financial statements.

At the end of March 2019, ENSE's borrowed funds correspond to the book value of the EUR 360 million bond being rated and that matures in 2028. As above-mentioned, this loan was contracted to finance the investment in oil reserves and, thus, the respective interest costs are recovered from oil market operators.

The oil price drop trend in the last two months of 2018, reaching the minimum price at the end of the 2018, led the coverage of financial debt by reserves to decrease to 0.91 times (from 1.12 times at the end of 2017). However, the recovery of oil price allowed coverage to improve to 1.23 times at the end of March 2019 (the highest coverage achieved since 2014). The coverage of net financial debt by reserves was still above 1 times (1.07 times) at the end of 2018 and increased to 1.46 times at the end of March 2019 (compared with 1.31 times at the end of 2017).

To provide additional insight and enable useful comparison, the coverage ratios of two of ENSE's European peers were also evaluated. The Spanish entity, Corporación de Reservas Estratégicas de Productos Petrolíferos (CORES), had a coverage ratio of 1.57 times at the end of 2018 (1.62 times considering the net financial debt, compared with 1.84 at the end of 2017). CORES is not rated by ARC, being rated A- / Positive / A-2 by S&P (the same level assigned to the sovereign), and A- / Stable / F1 by Fitch (also the same level assigned to the sovereign). The French entity, Société Anonyme de Gestion de Stocks de Sécurité (SAGESS), had a coverage ratio of 1.35 times at the end of 2018 considering the financial debt (1.36 times considering the net financial debt, compared with 1.45 times at the end of 2017). SAGESS is also not rated by ARC, being rated AA / Stable / A-1+ by S&P (the same level assigned to the sovereign).

Reflecting the long-term maturity of the bond (due on 6 August 2028) and representing the only financial debt of ENSE, and the significant amount of cash and deposits and short-term investments in debt securities issued by the Portuguese Government, ENSE's liquidity risk is virtually nil. On the other hand, the indicator of interest rate risk is 100% reflecting the fact that all financial debt (bond) bears interest indexed to 6-months Euribor and presently ENSE has no coverage contracts in force. However, as mentioned the interest costs with the bond are recovered from oil market operators and, thus, this risk is not assumed by ENSE. In addition, due to the negative values for Euribor, ENSE has not paid interest costs since February 2016.

The prevailing legal framework requires the reserves held by ENSE to be protected by insurance. Oil products owned by ENSE and stored in the POL NATO deposits are adequately covered by a multiple risks policy provided by AIG. Due to the high seismic risk in the areas where its stocks of oil products are stored (POL NATO deposits),

ENSE has also contracted with AIG an insurance to protect against the environmental risks facing these stocks. The insurance coverage of oil products owned by ENSE that are stored with Galp Energia is contracted by Galp Energia and the respective cost included in the storage costs paid by ENSE. ENSE also maintains insurance policies covering its exploration civil liability and environmental liability. The company aims to strengthen the mentioned insurance coverage of these risks, namely related to the POL NATO infrastructures, expecting to launch a new international public tender up to the end of 2019.

FORECASTS

In December 2018 ENSE prepared its updated 2019 forecasts and its 2020/2021 forecasts according to its current roles. In fact, the 2019 forecasts analysed by ARC Ratings in the Rating Report - Review dated 7 September 2018 were prepared by the company prior to the publication of the Decree-Law 69/2018, therefore considered its roles until the end of August 2018.

ENSE updated its 2019 forecasts (2019 forecasts from now on) based on its 2018 estimates. Given the proximity of the end of the year, ENSE, exceptionally, considered the book value of the oil reserves taking into account the oil prices at 23 November 2018, which led to the estimate of a reversal of the impairment of loss of EUR 7.3 million in 2018 and to a book value of oil reserves of EUR 355.9 million (which would be EUR 31.6 million below its market value as at 23 November 2018).

Regarding the main activity, ENSE assumed the maintenance of the 2018 estimate value of inventories (EUR 355.9 million) at the end of 2019 (as well as at the end of 2020). Thus, without including any impact from changes in the market value of oil reserves, considering no significant interest costs and increase of EUR 2.3 million in 2019 and in 2020 in the provision fund, ENSE estimates a net profit close to nil for its main activity in 2019 (as provided by law). From the monitoring activity of all energy sectors ENSE estimates a net profit of EUR 2.7 million in 2019. For this net profit determination point in time there was a EUR 4.5 million gain related to guarantees enforced. Without this gain this activity would present a loss of EUR 1.8 million.

For 2020, ENSE expect a global loss of EUR 1.4 million. This expected loss will come from the monitoring activity of all energy sectors. The company assumes that the potential loss from this activity will be financed by the Portuguese Government in the future, to the extent the expected revenues do not cover all operational costs. ARC Ratings continues to assume this assumption, as ENSE is a "State corporate entity" with the Portuguese Government its sole shareholder and ultimately responsible for its liabilities.

As referred above, ENSE plans to invest EUR 4.6 million in the POL NATO infrastructure over the 2019 – 2021 period (in an annual amount between EUR 1-2 million), to improve their operating conditions and ensuring compliance with the industry's most stringent safety, monitoring and operation standards. In addition, it should be highlighted the investment to be made in the IT area in an amount of EUR 1.3 million in the 2019-2020 period. These investments are planned to be financed by cash and deposits and short-term investments in debt securities issued by the Portuguese Government.

The assumptions made by the company (in the base scenario) led to improvements in the equity / assets ratio, to the 12% band, and in the net gearing ratio, to 6 times, at the end of 2019/2020. However, these ratios could assume different values given that the company's equity at the end of 2018 was EUR 29 million lower than the estimates and already included the impact of a non-current EUR 4.5 million gain forecasted for 2019.

For the end of 2019/2020 ENSE expect cash and deposits and investments in debt securities issued by the Portuguese Government of EUR 51.9 million. This value was already exceeded by EUR 3.8 million at the end of March 2019. Based on that assumption and considering stabilisation of the oil prices, compared to 23 November 2018, the company's forecasts point to a coverage of net financial debt by reserves, at market value, of 1.26 times at the end of 2019/2020. It should be noted that this coverage was 1.46 times at the end of March 2019.

Oil prices (Brent crude) have recovered since the low of 27.88 USD/bbl at the end of 20 January 2016, breached the 60 USD/bbl level in the last quarter of 2017 and has been fluctuating in the 70 and 80 USD/bbl band since April 2018, reaching 84.16 USD/bbl on 5 October 2018. After that date, according to the World Bank report issued on April 2019, a backdrop of global growth concerns, rising oil production by Organization of the Petroleum Exporting Countries (OPEC), and U.S. waivers on sanctions on Iran had triggered a plunge in Brent crude oil prices to 52.2 USD/bbl on 28 December 2018. Since then, oil prices have recouped most of these losses on subsequent production cuts by OPEC and its partners. In fact, oil prices recovered to 60 USD/bbl band in the first quarter 2019 and to 70 USD/bbl band in April 2019. Since mid-May 2019 oil prices returned to the 60 USD/bbl band, quoting 58.64 USD/bbl at 16 August 2019.

World Bank expected that average crude oil prices evolve to \$66/bbl in 2019 (a modest decrease compared with \$68/bbl in 2018) and to \$65/bbl in 2020, with balanced risks primarily related to policy outcomes.

Also relevant for the valuation of ENSE's oil reserves is the EUR/USD exchange rate. The appreciation trend of the EUR against the USD since the beginning of 2017, with a negative impact in the EUR denominated value of ENSE's oil reserves, reversed since May 2018. The average USD/EUR exchange rate was 1.18 in full 2018, compared with 1.13 USD/EUR in full 2017 year. In the first half of 2019 the average USD/EUR exchange rate was again 1.13. In the 2019 / 2020 forecasts, ENSE assumed 1.135 USD/EUR.

SENSITIVITY ANALYSIS

ENSE's credit quality is mainly dependent on the Portuguese Government's credit quality, given its sole ownership of ENSE and its ultimate responsibility for ENSE's liabilities defined by law, and on the oil market prices that would determine the revenue from the possible sale of oil reserves to repay the financial debt in a timely manner (in a hypothetical scenario of ENSE not being able to contract new financial debt to repay the bond and maintain the oil reserves). However, it should be noted that no formal guarantee is in place.

ARC Ratings considered an alternative scenario in 2019 and in 2020, built on the base scenario. In the alternative scenario ARC Ratings considered a possible 10% decrease in the market value of oil reserves at the end of 2019 compared with the end of May 2019 (the most recent valuation available), equivalent to EUR -42.5 million. It was also considered an additional 10% decrease in the market value of oil reserves at the end of 2020 compared with the end of 2019, equivalent to EUR -38.3 million.

The possible impact on ENSE's equity at the end of 2019 would be EUR -11 million, given that in the base scenario the book value of oil reserves at the end of 2019 is EUR 31.6 million below its market value. The impact on the ENSE's equity would increase to EUR -49.2 million at the end of 2020. Therefore, the company would present an equity / assets ratio of 9.7% at the end of 2019 and of 0.5% at the end of 2020 (compared with 12% band in the base scenario). As above mentioned, the company's equity at the end of 2018 was lowest than the estimates, therefore the equity / assets ratio in 2019 and in 2020 may be lower. However, ARC Ratings does not expect this to impact the company's ability to meet its debt service.

In this alternative scenario the coverage of financial debt by oil reserves would be 1.06 times in 2019 and 0.96 times in 2020 (compared with 1.08 times in the base scenario). The coverage of net financial debt by oil reserves would be, respectively, 1.24 times and 1.12 times (compared with 1.26 times in the base scenario).

ISSUANCE CONDITIONALITY

The rating assigned applies specifically to the EUR 360.0 million bond issued by ENSE (under its previous name of EGREP - Entidade Gestora de Reservas Estratégicas de Produtos Petrolíferos, E.P.E.) on 6 August 2008, with these main terms:

- A 20-years maturity with full repayment of principal at maturity, which will occur on 6 August 2028.
- The possibility of full but not partial early redemption at issuer initiative, on 7 August 2023, or: “in the event the following circumstances occur cumulatively:
 - change, after the issue date, of tax regulations applicable in Portugal, or change in the official application or interpretation of such regulations, that impose upon the issuer the obligation to pay additional sums other than foreseen in the contractual documentation;
 - the issuer is unable to avoid the referred imposition by taking measures available to it for the purpose, within reasonable criteria”.
- Early redemption, among others, in the following cases:
 - if the Portuguese Government ceases to hold, directly or indirectly, the entire share capital and voting rights of the issuer, or if the issuer ceases to have the legal status of an “entidade pública empresarial” (State corporate entity);
 - if any change in issuer's legal framework eliminates or restricts the Portuguese Government's current obligation to assume losses arising from the liquidation of assets as well as the residual responsibilities;
 - non performance of pari passu or negative pledge clauses;
 - change in the 0% weighting attributed by the Bank of Portugal to the liabilities of credit institutions to the issuer for the purpose of calculating the solvency ratio and the limits to major exposures.

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This Review Report should be read together with initial Rating Report and with the subsequent Review reports.

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Ratings do not constitute a recommendation to buy or sell, but only one of the factors to be weighted by investors.

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