

Entidade Nacional para o Setor Energético, E.P.E.

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

RATING DATE	9 September 2020
INITIAL RATING DATE	2 June 2008
LAST REVIEW	9 September 2019
NEXT REVIEW DATE	9 September 2021

PERIOD OF ANALYSIS	Historic: 2015 to 1H2020 Forecast: 2020/2021
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INFORMATION ANALYSED	ENSE 2015-2019 Report and Accounts ENSE 1H2019 and 1H2020 Interim Accounts ENSE 2020/2021 Forecasts Details on ENSE's Reserves World Bank's Commodity Markets Outlook Peers' Report and Accounts
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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 affirmed the final public "BBB-" rating, with Stable outlook, 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 implied support of the Portuguese sovereign and the coverage of the company's net financial debt provided by the market value of its oil reserves. In the context of oil price volatility this ratio (reserves/net financial debt) decreased, notwithstanding the decline in its net financial debt. Future oil price volatility may be even greater giving the uncertainty surrounding the impact of Covid-19 on the world economy. ARC Ratings will monitor the determinants of the assigned rating and take action as needed.

COMPANY PROFILE

After the 70s oil crisis, major consuming countries agreed to assume an obligation to maintain an adequate level of oil reserves in order to mitigate the effects of future supply problems.

The founding of 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., represented Portugal's assignment of the responsibility for maintaining all or part of their emergency oil reserves to a state entity.

Therefore, ENSE, founded in 2001, is a State-owned entity with the following duties:

- Being the Portuguese central stockholding entity for the acquisition and maintenance of the strategic portion of national emergency reserves of oil and oil products (reserves) – this its main activity.
- Supervision of all energy sectors.
- Management and monitoring of the storage activities for crude oil and its derivatives throughout the national territory, to guarantee and supply crude oil and petroleum products, depending on consumption needs.

At the end of 2019, the company has 36 employees, including its Board of Directors and Fiscal Council.

ENSE'S KEY RATING DRIVERS ARE THE FOLLOWING:

- Government ownership – ENSE's share capital is wholly owned by the Portuguese Government and the bond has a continual 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 by

Standard & Poor’s Financial Services LLC (S&P); Baa3/P-3/Positive by Moody’s Investors Service, Inc. (Moody’s); BBB/Stable by Fitch Ratings, Inc. (Fitch). However, there is no obligation of timely support, but the Portuguese Government, as established in the company’s bylaws, 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 level remains unchanged, still comprising solely the bond that is rated in an amount of EUR 360.0 million, maturing in 2028. Above all, ENSE’s expenses (including bond interest) have been, as structurally intended, totally covered by revenues, mainly originated from the Portuguese oil market operators. ENSE’s cash and deposits and investments in Portuguese Government issued debt securities continued to increase to EUR 63.3 million, reducing 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), Prio Supply, S.A. (PRIO) 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 (in accounting terms, without cash flow impact) heavily exposed to oil price fluctuations. In fact, the oil price drop trend in the first half of 2020 led the coverage of gross financial debt by reserves to decrease to 0.79 times at the end of June (from 1.21 times at the end of 2019). The coverage of net financial debt by reserves also declined to close 1.0 times at the end of June 2020 (from 1.45 times at the end of 2019). The period up to the end of August 2020, saw an oil price recovery trend, albeit with some fluctuations.
- Concentration of customer base – The vast majority of ENSE’s revenues (87.6%) continue to be derived from five companies, despite some decrease in 2019 compared with 2018: Galp Energia (accounting for 26.1% of ENSE’s 2019 revenues), Repsol (21.7%), BP (20.2%), PRIO (10.5%) and CEPSA (9.1%). It should however be noted that ENSE maintains stable relationships with them and there is no risk of losing customers. ARC Ratings notes specifically that three of the aforementioned customers carry investment grade ratings.

KEY RATING TIPPING POINTS	
<p><u>Positive Turning Points</u></p> <p>Triggers for a rating upgrade would come from:</p> <ul style="list-style-type: none"> (i) an upgrade of the Portuguese sovereign rating; or (ii) a significant long-standing increase of the coverage of the net financial debt by the market value of its oil reserves. 	<p><u>Negative Turning Points</u></p> <p>Triggers that could prompt a rating downgrade would include:</p> <ul style="list-style-type: none"> (i) a downgrade of the Portuguese Sovereign rating; or (ii) a significant long-standing decrease of the coverage of the net financial debt by the market value of its oil reserves.

SHAREHOLDERS AND 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 the required level of strategic reserves and a continuously updated record of emergency reserves containing the information necessary for its respective control.

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 the electricity and natural gas sectors. Therefore, ENSE was also assigned the duty of supervision and prevention of non-compliance with legislation regulating the exercise of economic activities in the energy sector. Other than that, it is still managing and monitoring the storage activities of crude oil and its derivatives throughout the national territory, to guarantee and supply crude oil and petroleum products, depending on consumption needs. In this regard, it should be noted that, during the energy crisis in August 2019 (from 9th to 21st), caused by the road haulage (tanker fleet) operators strikes, the emergency plan implemented by ENSE to guarantee the supply of fuels, proved to be adequate (without need to resort to its reserves), ensuring the normal functioning of the country.

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 company's market share. The share of reserves to be held by ENSE (strategic reserves), in substitution of oil 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 to 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 oil market operators which are obliged to build-up emergency reserves.
- ENSE is obliged to create a provision fund (recorded in equity), funded in annual increments, aiming to achieve at least an amount corresponding to 25% of the oil reserves' acquisition cost. At the end of June 2020, the provision fund was equivalent to 12.7% of the oil reserves' acquisition cost, a percentage that has been increasing. The company intends to annually continue to reinforce this provision fund to reach at least 25% of the oil reserves' acquisition cost, at the cost of the oil market operators.
- 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 5 August 2020 ARC Ratings conducted a tele-conference call with ENSE's senior management as part of the analytical review process. In summary, the Covid-19 impact, the 2020 budget and investment plan, the oil price volatility, and the insurance policies were discussed.

COVID-19 PANDEMIC

The Covid-19 pandemic, that led to a lockdown of the Portuguese economy, has had a very limited impact on ENSE's operational activity. There was a contingency plan to ensure the continuity of ENSE's essential activities. This plan was updated to allow staff to return to the office in safe conditions.

The company, in exercise of its main role, is prepared to operate in any contingency, with a high level of functions done by remote access (via internet) and dealt well with the Covid-19 disruption. Given ENSE's strong liquidity position, the company did not resort to the available Government measures to support its treasury.

The pandemic outbreak caused a reduction in the Portuguese economic activity with a consequential reduction of oil products consumption. In this scenario of excess supply of oil products, to avoid exceeding national storage capacity, the activity of the national Sines and Matosinhos refineries were temporary suspended from mid-April to the end of June and late July respectively. Both refineries are currently fully operational.

CASH FLOW GENERATING CAPACITY AND RECENT DEVELOPMENTS

Oil products introduced for consumption and reserves of crude oil and oil products

The total volume of oil products introduced for consumption in Portugal increased by 1.4% in 2019, to 8.36 million tonnes (Mton), against a 2.3% increase in 2018. Increases in B (diesel) and in A (gasoline) categories of oil products more than offset the decrease in C (fuel oil and liquefied petroleum gas) category. The volume mix of oil products introduced for consumption in Portugal did not change materially in 2019. The B category accounted for 78.8% of the total, while the A category accounted for 12.8% and the C category accounted for 8.4%.

In 2020 in the Covid-19 context the total volume of oil products introduced for consumption in Portugal decreased year-on-year by 15.3% in March, by 51.9% in April and by 36.5% in May. Following the emergency national lockdown period (18 March to 2 May) there has been a recovery trend, particularly related to the sectors most focused on domestic consumption. However, year-on-year, the Portuguese Gross Domestic Product dropped by 16.3% in the second quarter of 2020, after a 2.3% decrease in the first quarter of 2020. Thus, in the company's view, it is expected that it will take some time before consumption is back in line with the pre-pandemic level.

It should be noted that the drop in the total volume of oil products introduced for consumption in Portugal in the first half of 2020 (1H2020) will only impact the calculation of the required oil products emergency reserves level in 2021.

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

	FYE Dec 2015	FYE Dec 2016	FYE Dec 2017	FYE Dec 2018	FYE Dec 2019
OWN RESERVES	938,273	938,192	938,018	938,603	938,459
CRUDE OIL	538,082	538,082	538,082	538,082	538,082
GASOLINE	51,400	51,400	51,400	51,400	51,400
DIESEL	297,791	297,710	297,536	298,122	297,978
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 (*)	140,000	249,000	303,500	301,500	356,250
CRUDE OIL	110,000	149,000	153,500	246,500	320,000
GASOLINE	10,000	0	0	0	30,000
DIESEL	20,000	100,000	0	55,000	0
FUEL OIL	0	0	150,000	0	6,250
LPG	0	0	0	0	0
TOTAL ENSE'S RESERVES	1,078,273	1,187,192	1,241,518	1,240,103	1,294,709
CRUDE OIL	648,082	687,082	691,582	784,582	858,082
GASOLINE	61,400	51,400	51,400	51,400	81,400
DIESEL	317,791	397,710	297,536	353,122	297,978
FUEL OIL	45,000	45,000	195,000	45,000	51,250
LPG	6,000	6,000	6,000	6,000	6,000
TOTAL ENSE'S RESERVES IN DAYS OF CONSUMPTION					
GASOLINE	51	50	45	48	60
DIESEL	50	47	45	50	49
OTHER	75	43	112	54	60

Source:

ENSE.

Notes:

(*) CSO Tickets = Compulsory Stockholding Obligation Tickets, which are international contracts for the maintenance at order of oil reserves owned by third parties.

As a rule, the calculations of the required emergency reserves are only carried out at the end of the year, although their evolution is monitored by ENSE during the year. Therefore, the analysis of ENSE's own reserves in the table above is reported as at the end of 2019.

ENSE's own reserves stabilised at 0.94 Mton at the end of 2019, while its reserves contracted under CSO Tickets (Compulsory Stockholding Obligation) increased by 18.2% to 0.36 Mton. CSO Tickets are contracted according to market demand for ENSE to replace the oil market operators (namely small oil operators). Under CSO Tickets, which are international contracts, stock is reserved by the CSO ticket seller for the benefit of the CSO ticket buyer during the reservation period and must always be physically accessible and available. In 2019, strategically, ENSE acquired CSO Tickets for part of 2019 and the full 2020, benefiting from a lower average purchase price.

ENSE continued to present substantial headroom between its own reserves and the legally required strategic reserves, with significant headroom in all categories, allowing ENSE to continue replacing part of the operators' own obligation. Considering the three oil products categories, at the end of 2019, the company had oil products reserves equivalent to 53.1 days (compared to the minimum of 30 days and 51.6 days at the end of 2018).

The analysis of the composition of the reserves held by ENSE at the end of 2019 shows that: ENSE continues to own the majority of the reserves (72.5%), with the remainder being contracted under CSO Tickets; the totality of ENSE's own reserves were stored in Portugal, while the 27.5% of reserves contracted under CSO tickets were stored outside Portugal (in European countries); and finished products accounted for 33.7% of the total stocks (marginally more than one third required by law and compared with 36.7% at the end of 2018). The percentage of finished products does not represent a concern in ARC's view, given there is oil refining capacity. Without consider CSO Tickets the percentage increase to 42.7% (the same of at the end of 2018).

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, which initially served to supply North Atlantic Treaty Organization operational assets). ENSE continue to study storage alternatives with a view to further reducing the operational cost structure of storing reserves of crude oil and oil products. However, the company continues to prioritize the safety and quality of products and conditions of use in case of need.

The maintenance of the quality of oil reserves stored under agreements with Galp Energia is ensured by this company, while the quality of diesel reserves stored in POL NATO deposits is monitored by an external entity, the Bureau Veritas - Oil & Petrochemicals Laboratory.

Storage costs, which are passed on to the oil market operators, are updated according to the inflation rate of the previous year. The annual utilisation fee paid for the POL NATO deposits can be reduced if the difference is spent by ENSE in the management and improvement of this infrastructure. Under this agreement ENSE has the obligation to make additional investments with EUR 0.4 million carried out in 2019 (EUR 0.6 million in 2018). According to ENSE's 2020 budget, dated mid-October 2019, the investment amount was moderate and could reach EUR 1.5 million per year in 2020, in 2021 and in 2022. The realization of this investment plan will allow significant improvements in the conditions of those strategic facilities and aims 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 (more than enough considering the strong liquidity position at the end of June 2020).

ENSE's profit and loss

ENSE's 2019 financial statements were audited by Vitor Almeida & Associados, SROC Lda without qualification. It should be noted that ENSE adopted the permitted exceptions provided for International Financial Reporting Standard 16 for leases (i.e. low-value or short-term), thus it had no impact on the financial statements.

ENSE's revenues increased year-on-year by 7.6% in 2019, to EUR 26.1 million, and by 7.5% in the 1H2020, to EUR 13.9 million. ENSE's revenues primarily comes from its main activity (holding and managing reserves of crude oil and oil products), which accounted for 98.8% of total revenues in 2019 and 96.9% in the 1H2020. ENSE's revenues from its main activity corresponds to the recovery of its expenses on this activity (operating and financing expenses) from oil market operators (see below for the respective ratings of these counterparties). The amounts to be received monthly are calculated every year based on the expenses forecasted by ENSE with the aim 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). The growth of its main revenue has related to the increase of CSO Tickets sold to the main oil market operators, at their

request. ENSE's other revenues come from its other duties and it aims to cover its expenses with them. These revenues included the issuing of biofuel tickets (of EUR 0.3 million in 2019, against EUR 0.1 million in 2018), a mechanism to facilitate the control of the compliance with the obligation to incorporate biofuels in fuels, and some sanctions applied in case of breaches of the legal regime (less significant).

Therefore, ENSE's turnover continues to be mainly originated from the leading distributors of oil products in Portugal. In 2019 the five main customers accounted for 87.6% of its total turnover (compared with 92.2% in 2018). The breakdown of total turnover by its main customers did not change significantly compared to 2018:

- Galp Energia (26.1% in 2019; 28% in 2018), the market leader; Galp Energia is not rated; Galp Energia is also ENSE's main provider of oil reserves storage;
- Repsol (21.7%; 24.2%), which is not rated by ARC (BBB / Stable / A-2 by S&P; Baa2 / Negative / P-2 by Moody's; and BBB / Stable / F2 by Fitch);
- BP p.l.c. (20.2%; close to 20%), which is not rated by ARC (A- / Stable / A-2 by S&P; A1 / Negative by Moody's; and A / Stable by Fitch);
- Prio Supply, S.A. (10.5% in 2019 and in 2018), a Portuguese company not rated; and
- CEPESA (9.1%; 9.5%), which is not rated by ARC (BBB- / Stable / A-3 by S&P; Baa3 / Negative by Moody's; BBB- / Stable by Fitch).

ENSE's operational expenses mainly comprise supplies and services and staff costs. In 2019, supplies and services, primarily subcontractors' costs related to storage costs and acquisition of CSO Tickets, was EUR 19.7 million, almost in line with the 2018 figure. The subcontractors' costs related to the acquisition of CSO Tickets increased by 14.7%, to EUR 5.2 million. Staff costs increased by 15.3% in 2019, to EUR 1.6 million, due to the company having hired 4 additional employees to cover the enlargement of duties. The company's internal skills and resources allowed it to replace some external specialized services. In 1H2020 supplies and services costs rose by 7.1% year-on-year, to EUR 10.3 million, while its staff costs decreased by 3.6%, to EUR 0.7 million.

Regarding ENSE's 2019 operational expenses, it is worth mentioning the absence of rotation of diesel stocks in the POL NATO infrastructure (as occurred in 2018, because it was not necessary to ensure its quality) which represented a cost saving of EUR 1.4 million against the forecast.

In 2019 the company recorded impairment costs of EUR 0.8 million to fully cover doubtful customers (small market operators), compared with EUR 0.2 million in 2018. In the 1H2019 and 1H2020 the company has not recorded any impairment costs. There were no impairments regarding its main customers.

ENSE - FINANCIALS AND RATIOS (THOUSAND EUROS)

	FYE Dec 2015	FYE Dec 2016	FYE Dec 2017	FYE Dec 2018	FYE Dec 2019	1H 2019	1H 2020	2020 (F)	2021 (F)
TURNOVER	24,562	24,331	25,398	24,266	26,116	12,901	13,874	30,183	31,358
EBITDA	8,519	6,857	7,722	2,958	4,938	2,467	2,810	3,112	3,699
EBIT	(76,845)	114,371	12,744	(23,684)	48,971	2,245	2,622	2,388	2,769
FINANCIAL RESULT	(41)	625	659	647	654	321	293	256	(55)
NON-CURRENT RESULTS	(7,802)	(7,518)	(7,931)	(20)	(4,745)	(1,133)	(1,295)	(2,589)	(2,674)
NET PROFIT	(84,707)	107,477	5,460	(23,386)	44,862	1,433	1,620	55	40
OPERATING CASH FLOW (OCF)	9,425	9,825	11,912	3,219	5,439	4,857	4,274	4,323	4,108
CASH FLOW	14,605	9,417	12,086	3,372	5,945	5,437	4,769	4,819	4,459
FREE CASH FLOW	14,335	9,053	11,785	2,690	5,149	5,045	14,750	1,350	2,490
RESERVES' BOOK VALUE	235,750	343,337	348,590	322,727	368,021	322,727	368,021	322,727	322,727
RESERVES' MARKET VALUE	237,087	385,418	403,831	327,926	435,007	n.av.	283,392	n.av.	n.av.
TOTAL ASSETS	270,790	387,783	404,310	381,729	430,955	386,043	435,969	389,444	392,417
NET WORKING CAPITAL (NWC)	256,289	370,532	383,543	364,383	413,806	367,283	427,336	369,713	371,783
NET WORKING CAP. REQUIREMENTS (NWCRC)	234,817	343,341	348,233	323,293	366,966	321,158	365,980	321,917	321,705
NET CASH POSITION (NCP)	21,473	27,191	35,310	41,090	46,840	46,125	61,355	47,796	50,078
FINANCIAL DEBT	359,676	359,539	359,583	359,632	359,675	359,648	359,692	359,712	359,756
NET FINANCIAL DEBT*	329,298	320,098	308,357	305,716	300,608	301,022	296,336	299,908	297,462
RESERVES' MARKET VALUE / FINANCIAL DEBT	0.66	1.07	1.12	0.91	1.21	n.av.	0.79	n.av.	n.av.
RESERVES' MARKET VALUE / NET FINANCIAL DEBT	0.72	1.20	1.31	1.07	1.45	n.av.	0.96	n.av.	n.av.
Contribution Margin (%)	35.7%	31.4%	34.3%	18.5%	24.6%	25.2%	25.5%	10.0%	19.6%
EBITDA Margin (%)	34.7%	28.2%	30.4%	12.2%	18.9%	19.1%	20.3%	10.3%	11.8%
Operating Return on Turnover (%)	(312.9%)	470.1%	50.2%	(97.6%)	187.5%	17.4%	18.9%	7.9%	8.8%
Operating Return on Assets (%)	(28.4%)	29.5%	3.2%	(6.2%)	11.4%	1.2%	1.2%	0.6%	0.7%
Gross Cost of Borrowed Funds (%)	0.2%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Net Return on Turnover (%)	(344.9%)	441.7%	21.5%	(96.4%)	171.8%	11.1%	11.7%	0.2%	0.1%
Payout Ratio (%)	0%	0%	0%	0%	0%	0%	0%	0%	0%
Coverage of Interest Costs by EBITDA (x)	11.6	80.3	206.3	79.0	131.9	131.8	150.1	56.2	66.8
Coverage of Net Interest Costs by EBITDA (x)	209.8	-	-	-	-	-	-	-	66.8
CASH FLOW Coverage of Net Interest Paid (x)	27.2	-	-	-	-	-	-	-	264.8
Financial Debt / EBITDA (x)	42.2	52.4	46.6	121.6	72.8	72.9	64.0	115.6	97.2
Net Financial Debt/ EBITDA (x)	38.7	46.7	39.9	103.4	60.9	61.0	52.7	96.4	80.4
CASH FLOW Coverage of Net Financial Debt (%)	4.4%	2.9%	3.9%	1.1%	2.0%	3.6%	3.2%	n.av.	n.av.
Equity / Assets (%)	(34.4%)	5.6%	8.7%	4.3%	15.3%	4.9%	15.8%	6.1%	6.7%
NET GEARING (Net Debt to Equity) (x)	(3.5)	14.7	8.8	18.8	4.6	16.0	4.3	12.7	11.3
Financial Debt Struct. (S.T. Fin. Debt as a % of Total Fin. Debt)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
LIQUIDITY RISK (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Interest-Rate Risk (%)**	99.8%	99.9%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Notes:

Figures rounded.

Accounts adjusted by ARC Ratings for analysis purposes.

2015 - 2017 period annual accounts audited by Moore Stephens & Associados, S.R.O.C..

2018 and 2019 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.

n.av. = Not available ; F = Forecasts.

Sources:

ENSE.

The oil price volatility (an external factor) impacted ENSE's financial statements due to the book value of its reserves being recorded at the lower of its market value or the acquisition cost. Therefore, based on the oil price at the end of 2019, which was higher than the one at the end of 2018, the company recorded a reversal of impairment loss recorded in previous years of EUR 45.3 million. On the contrary, in 2018, due to the minimum oil price reached at

the end of the year, it recorded an impairment loss of EUR 26.1 million. Usually, ENSE only records an impairment loss or reversal of prior impairment losses in its inventories at the end of the year.

In 2019 ENSE increased the provision fund by EUR 4.7 million, more than 5% growth over the 2018 figure. In the 1H2020 the increase in the provision fund was EUR 1.3 million, compared with EUR 1.1 million in the 1H2019. Usually, over the year the provision fund increase is equivalent to 10% of the company's operational costs, including depreciation, and financial expenses net of financial income. At the end of the year the company makes an additional increase depending on the net profit of its main activity. As aforementioned, excluding the possible impairment (or reversal of impairment) on the book value of its reserves, the net profit tends to be close to zero. ARC Ratings considers the provision fund credit positive and the costs of the provision fund as non-current, not affecting EBITDA and EBIT.

In the context of negative 6-months Euribor (noting that this is not floored), 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 2019. ENSE has not had to pay interest in 2019, as occurred in 2018. In these conditions, the company continued to present a positive financial result, mainly reflecting interest gains from the investments in debt securities issued by the Portuguese Government. This situation did not change in the 1H2020. The coverage of interest and other associated bond costs (fees) by EBITDA remained high, at 131.9 times in 2019 (compared with 79.0 times in 2018) and at 150.1 times in the 1H2020.

ENSE recorded a net profit of EUR 44.9 million in 2019, primarily due to the reversal of previous impairment losses on its reserves. The impact of the oil price volatility has been crucial for the company's results. Thus, in 2018, in the context of significant impairment loss, the company showed a loss of EUR 23.4 million. In 2018, its loss was partially offset by EUR 4.5 million of bank guarantees which were punctually enforced, which ARC Ratings considered as non-current. In the 1H2020 ENSE showed a net profit of EUR 1.6 million, a 13% increase against the 1H2019 figure.

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.

FINANCIAL POLICY

At the end of June 2020 ENSE's assets totalled EUR 436.0 million, with current assets accounting for 99.7% of total assets (97.3% at December 2018).

The book value of its reserves, of EUR 368.0 million in June 2020, was its main asset. This value is the same as in December 2019, due to the calculation of any impairment usually being performed at the end of the year, comparing the acquisition cost with the oil prices at the end of December. Thus, the value of EUR 368.0 million reflected the book value at the end of 2018 of EUR 322.7 million adjusted by the EUR 45.3 million reversal of impairment in 2019.

In mid-June 2020, one medium and long-term financial investment in debt securities issued by the Portuguese Government of EUR 10.1 million matured. This financial investment with an annual interest rate of 6.78% generated most of the company's interest gains in 2019 (as in 2018) and in the 1H2020.

The total amount of cash and deposits and short-term investments in debt securities issued by the Portuguese Government was EUR 63.3 million in June 2020, ENSE's second main asset, EUR 47.6 million of which was for the coverage of the provision fund managed by the company, while the remainder of EUR 15.7 million is free to use,

namely, to finance its investment (usually of lower value). In the current context of low interest rates the company will maintain the short-term investments in debt securities issued by the Portuguese Government.

The outstanding amount of accounts receivable was EUR 0.5 million in June 2020. The doubtful customers of EUR 1.0 million, related to small oil market operators, were fully covered by impairments.

The company's tangible assets of EUR 0.9 million in June 2020, mainly related to equipment, only accounting for 0.2% of its total assets.

ENSE carried out investments in fixed assets of EUR 1.0 million in 2019 (EUR 0.8 million in 2018), EUR 0.4 million of which were investments in the POL NATO infrastructure and EUR 0.2 million in IT systems. In the 1H2020 the investment carried out in fixed assets was not significant. In fact, its 2020 investment plan (which is part of its annual budget, prepared in mid-October 2019) was not yet approved by the public entity that oversees the company. In response to the Covid-19 pandemic, in July 2020 all State-owned entities were required to update their 2020 budgets (up to 21 September 2020). In ENSE's view, its 2020 budget (and investment plan) does not need to be updated due to the limited impact on its activity from the Covid-19 pandemic. The delay in carrying out investment does not create significant risks for the company's activity.

ENSE continued to show positive free cash flow allowing it to reinforce its cash and deposits and investments in debt securities issued by the Portuguese Government.

ENSE's debt level remains unchanged, still comprising solely the bond that is rated in an amount of EUR 360 million, maturing in 2028. As abovementioned, this loan was contracted to finance the investment in oil reserves and thus the respective interest costs are recovered from oil market operators.

Thanks to the increase of cash and deposits and investments in debt securities issued by the Portuguese Government, ENSE's net financial debt has shown a decreasing trend, to EUR 296.3 million in June 2020 (a 3.1% decrease compared to December 2018).

The oil price volatility impacted ENSE's reserves' market value and the coverage of debt and net debt by reserves. Therefore, according to information provided by the company, the coverage of its debt by reserves dropped to 0.79 times in June 2020, from 1.21 times in December 2019 (0.91 times in December 2018). The coverage of the company's net financial debt by reserves also decreased to 0.96 times at June 2020, compared with 1.45 times at December 2019 (1.07 times at December 2018).

To provide additional insight and enable useful comparison, the coverage ratios (financial debt by reserves) of two of ENSE's European peers, which have the same main strategic role and strong control from States, were also evaluated:

- The Spanish entity - Corporación de Reservas Estratégicas de Productos Petrolíferos (CORES) – which manages Spanish strategic oil reserves of petroleum products and assures oil and gas market had a coverage ratio of 2.03 times at the end of 2019 (2.06 times the net financial debt). CORES is not rated by ARC, being rated A / Stable / A-1 by S&P (being the same level assigned to the sovereign), 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) – established on the initiative of oil French operators and under the aegis of public authorities has the purpose of building up and stockpiling strategic oil reserves had a coverage ratio of 1.50 times at the end of 2019 for both net and gross financial debt

(1.36 times the net financial debt at the end of 2018). SAGESS is also not rated by ARC, being rated AA / Stable / A-1+ by S&P (being the same level assigned to the sovereign).

The oil price volatility also has an accounting impact on ENSE's equity, through the full year net profit. The provision fund, also recorded in equity, was reinforced to EUR 47.6 million in June 2020, from EUR 41.6 million in December 2018. At the end of June 2020 ENSE's equity was EUR 68.8 million. The oil prices drop in the 1H2020 was not recognized in the company's equity at the end of June 2020 (as usual). The impact of the oil price change between the end of 2019 and the end of 2020 will be recorded in December 2020.

The net gearing ratio improved from 18.8 times at the end of 2018 to 4.6 times at the end of 2019 and to 4.3 times in June 2020, benefiting from the decrease of the net debt and the equity increase.

The equity / assets ratio of ENSE improved from 4.3% at the end of 2018 to 15.3% at the end of 2019 and to 15.8% at the end of June 2020.

Considering the long-term maturity of the bond (due on 6 August 2028) and the significant value of cash and deposits and short-term investments, ENSE's liquidity risk is virtually nil. On the contrary, the bond bears interest indexed to 6-months Euribor and presently ENSE has no interest rate coverage contracts in force. However, as mentioned the interest costs of 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 and the absence of a Euribor floor at 0% for the bond, ENSE has not paid interest since February 2016.

The prevailing legal framework requires the reserves held by ENSE to be protected by suitable insurance. Oil products owned by ENSE and stored in the POL NATO deposits are adequately covered by a multiple risks policy, including environmental risks. 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 entirety of its mentioned insurance policies was provided by Fidelidade - Companhia de Seguros, S.A., the major shareholder of which (with an 85% stake) is FOSUN International Limited (BB / Negative by S&P and Ba3 / Negative by Moody's).

ARC Ratings is not aware of any significant contingent liability of the company at the end of June 2020.

FORECASTS

In mid-October 2019, based on the extrapolation to the end of 2019 of the data verified until August, ENSE prepared its 2020 budget. As mentioned, this forecast has not yet been approved by the public entity that oversees the company.

ENSE's 2021 budget is being prepared, however, it will not be available to be incorporated in the current review report. Therefore, for analysis purposes, ARC Ratings considers the 2021 forecast included in the document prepared in October 2019.

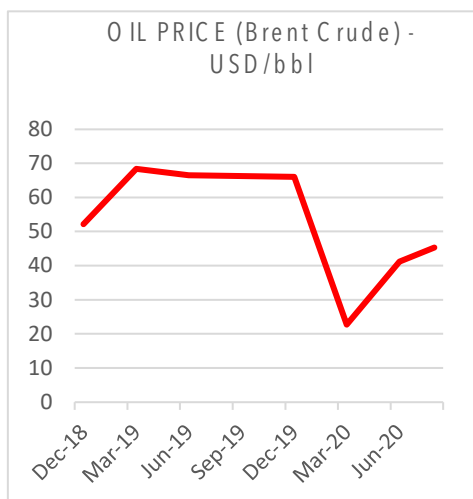
Regarding the main activity, ENSE assumed a turnover increase mainly related to the expected rise of CSO Tickets to be sold to the oil market operators and increase of operational costs. The company maintained the 2018 book value as its value assumption for its reserves (EUR 322.7 million) at the end of 2020 and at the end of 2021, thus no impairment or reversal of impairment was considered. The provision fund was expected to increase by

EUR 2.6 million in 2020 and by EUR 2.7 million in 2021, to reach EUR 46.4 million at the end of 2020 (level already achieved in June) and EUR 49.1 million at the end of 2021. The financial result was projected to be EUR 0.3 million in 2020, less than half of the 2019 figure due to the maturity of its medium long-term investment in mid-June 2020. For 2021, due to expected low interest rates, a negative, but not significant, financial result was forecasted, that will be passed on to the oil market operators. Globally, ENSE forecasted an insignificant net profit in 2020 and 2021. In the company's view, any possible negative deviation in the result from its other activities (beyond its main activity) should be covered by the oil market operators.

ENSE planned to invest EUR 2.8 million in 2020 and EUR 1.6 million in 2021. Most of this is related to the POL NATO infrastructure, of EUR 1.5 million per year, to improve their operating conditions and ensuring compliance with the industry's most stringent safety, monitoring and operational standards. In addition, it forecasted EUR 1.0 million of investment in the IT area in 2020. Given its investment plan for 2020 was not yet approved, thus not carried out, there will be a delay in completing this forecasts plan of investment. These investments are planned to be financed by cash and deposits and short-term investments.

The company forecasted a net financial debt decrease over 2020 and 2021, to EUR 297.5 million in 2021, through the increase of cash and deposits and short-term investments. It should be noted that, in the absence of investment in 1H2020, its net financial debt was already lower (at EUR 296.3 million).

It should also be noted that the coverage of the company's net financial debt by the market value of its reserves will depend also on external factors, such as oil price volatility and the EUR/USD exchange rate.



Source: Bloomberg

According to the World Bank Commodities Price Data, the average oil price (Brent crude) showed a drop of 10% in 2019, to 64 USD/bbl, after a 30.7% increase in 2018. The declining trend remained in the 1H2020, particularly in the second quarter, as per the above Chart. The minimum price was recorded on 21 April 2020 of 19.33 USD/bbl, per Bloomberg. In the following months, the Brent crude price recovered with some volatility, to 41.15 USD/bbl at the end of June 2020 and to 45.46 USD/bbl on 18 August 2020. Per the Commodity Markets Outlook of the World Bank, dated April 2020, it is expected an average of oil price of 35.0 USD/bbl in 2020 and a recovery to 42.0 USD/bbl in 2021. Nevertheless, there remains uncertainty related to the impact of Covid-19 on oil products demand, linked to the economic environment.

The EUR/USD exchange rate, with impact in the market value of the ENSE's oil reserves recorded in euros, decreased from 1.15 on 31 December 2018 to 1.12 on 31 December 2019 and on 30 June 2020, per the European Central Bank.

The possible unfavourable evolution of the market value of reserves in euros would have a negative accounting impact on the company's equity, and related ratios, however without impact on its cash flow, given that it does not trade in oil products (and does not rotate stocks). In a hypothetical scenario of ENSE not being able to contract new financial debt to repay the bond and maintain the oil reserves, oil market prices would determine the revenue from the possible sale of oil reserves to repay the financial debt in a timely manner.

Above all, 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. However, it should be noted that no formal guarantee is in place.

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.
- Variable interest rate at EURIBOR 6 months + 0.075 percent p.a.
- The possibility of full but not partial early redemption at the issuer's 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 the 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 any residual responsibilities;
 - non-performance of pari passu and/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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