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"Third Quarter 2018 Financial Results" Conference Call

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Conductors:

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& Mr. Vasilis Tsaitas Investor Relations Officer

Conference Call Conducted by Chorus Call Hellas

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OPERATOR: Ladies and Gentlemen, thank you for standing by. I am Konstantinos your Chorus Call operator.

Welcome and thank you for joining the Hellenic Petroleum conference call to present and discuss the Third Quarter 2018 Financial Results with the management of the company.

At this time, I would like to turn the conference over to Mr. Andreas Shiamishis, Deputy CEO & CFO and Mr. Vasilis Tsaitas Investor Relations Officer.

Gentlemen, you may proceed.

SHIAMISIS A: Thank you very much. Good afternoon. Thank you for joining this call for the Third Quarter 2018 Results. Without further ado, I will go through the presentation and give you brief overview of our performance over the last few months.

So in terms of the key highlights, we have a very strong quarter… one of the best quarters ever in terms of adjusted results. Our EBITDA at €237 million which is up from the respective third quarter in 2017 and adjusted net income at €111 million, again up from last year's respective quarter.

This is particularly positive for us because this performance has been delivered against the background of weaker refining margins versus the same quarter last year which is clearly an indication of the strong performance of the company. We've had higher production which is also partly to the fact that we are comparing against last year's quarter when Elefsina was down for a few weeks, but still we are almost 20% up in terms of production, higher sales and as you will see later on, record high exports.

In terms of the actual performance, we have been able to optimize even further the crude supply and the running of the refineries which have resulted in a historical high over performance versus benchmark. This is effectively an indication that we use versus a fairly standard benchmark being the Urals crude benchmark for refining margins, which includes the benefit of different and better crude supply, better yields and of course, commercial premium.

At the same time our reported results are also exceptionally strong, it's the best third quarter in terms of reported results, and I think the second best in the history of the Group with almost €260 million of reported EBITDA and a net income of 135. Clearly this is partly attributed not only to the strong operating results, but also to the inventory effect, given that prices continue to increase in the third quarter of 2018.

Our contribution from associates being DEPA, DESFA and Elpedison mainly, has been pretty much the same as last year, and we are continuing to include DESFA as an associated as part of the DEPA Group. That's clearly going to change at the end of the year where without any surprises we expect the transaction to be completed.

Another positive sign is the further reduction of the financial expenses in this quarter by about 11%. That followed a completion of the 2018 refinancing plan which has allowed us to reduce even further the interest cost of the Group.

In terms of cash flow and balance sheet, we've had a very strong cash flow over €200 million for the quarter. And that has allowed us to not only improve our balance sheet in terms of working capital, but to proceed with deleveraging and reach a gearing of 40%, which is the lowest in the last few years.

On the basis of performance, very strong balance sheet and credit capacity and a positive outlook. The board approved today the payment of an interim dividend of $0.25 per share which will be paid before the end of this year.

In terms of other business developments, as you know we have the privatization process ongoing with the two main shareholders selling 50.1% of HELPE shared capital. We have two qualified bidders and they are in the process of due diligence. We expect that this process will be continued for the next few weeks, so that both of the qualified bidders are in a position to formulate a view for the Group and submit their binding offer.

DESFA spin-off is in progress. As you may know, the transaction with DESFA involves the reduction of the share capital in DEPA and the…, if you will, distribution of the DESFA shares…as a distribution in kind to the two shareholders being ourselves and the Hellenic Republic Asset Development Funds. And the minute we get that, we will be able to close the transaction with the winning consortium, sell the shares for DESFA and collect the proceeds.

As we have indicated in the past, a significant part of that proceeds, which is just short of €300 million will go against debt reduction, so it will improve even further our balance sheet. We are already pretty close to our long term target, so this is going to accelerate that process, and a part of that proceeds will be used, as a possible extraordinary distribution to the shareholders.

As far as DEPA is concerned, it is going…restructuring itself with two transactions which are at the final competition authorities' approval stage being the acquisition of the remaining 49% of the Attiki business being the commercial and the infrastructure business and also the sale of the Thessaloniki commercial business to ENI.

On E&P, we have competitive negotiation for two of the offshore areas in Crete. There we are part of a JV with TOTAL, Exxon and ourselves, as well as the offshore area of Kyparissiakos, which we are pursuing on our own. All of these lease agreements have been negotiated in initials and we are waiting for the formal signing and parliamentary approval.

Moving on to Page 4, as you can see it's a very strong set of numbers. The main driver is clearly the Refining, Supply & Trading business which is delivering 25% up from last year, and you can see that the adjusted EBITDA short of €240 million is up 15%.

In terms of finance cost, what I mentioned earlier, you can see that we are moving towards our medium term target of getting our finance cost down to €100 million per year. We are half way there given where we started at €211 million a couple of years ago. We are expecting to be at around €140 million, €150 million for the end of the year and hopefully in the next 12 to 18 months be able to get to the €100 million. In terms of our net debt, we are just shy of €1.8 billion which gives us the…if you will, the lowest for some time net debt-to-capital employed ratio.

Moving on to Page 6, in terms of the market environment, we have seen a further increase of crude oil prices in the third quarter and we've seen a strengthening of the euro/dollar for us at 1.16, which is beneficial for our business. In terms of crude differentials, it's a proxy if you will, for the ability to deliver more dollars per barrel for our complex refineries.

The Brent WTI differential continues to be relatively high which is clearly something which benefits U.S. Refineries and may have some negative implications for European Refineries. And the Brent-Urals spread has become tighter on the reduced supply on the constraints for sour crude supply into the East Med following the snapback of the U.S. sanctions on Iran.

In terms of refining margins, we see a weakening of product cracks with the notable exception of diesel or ULSD, where we have the benefit of having a refinery which produces a significant amount of its feedstock as diesel. So the Elefsina Refinery has been able to deliver pretty much a constant benchmark refinery margin of 5.6, whereas Aspropyrgos and Thessaloniki which is not shown here have suffered a biggest decline.

Having said that, I think it's important to have a reality check here, because we are saying that the margins are lower than last year, however, these are healthy level of margins and as you can see they have allowed us to deliver a very strong clean performance which at the nine months' stage is over €0.5 billion as clean EBITDA.

Moving on to the domestic market environment which accounts for about 45% of our sales, so it's a totally different profile than what it used to be a few years ago. We see that gasoline consumption has further reduced; it's a trend that we have seen in the last few quarters, whereas diesel has moved up by a percentage point.

Clearly the diesel market has become more critical for the auto fuels in the Greek market, and we are seeing that fuel efficiency drive from the car manufacturers, as well as, lower domestic consumption because we clearly have the tourism to account for a sizable part of that consumption. So if we isolate the domestic part of the consumption, it is moving down on the back of the economic situation in Greece.

Aviation and bunkers is proving to be strong. We had a very good third quarter particularly on aviation which helps our business with EKO

Moving onto Page 10, we have the… the high level view of how this quarter compares to last year's similar quarter. As you can see, we have a worse… a weaker environment which is the refining margins, the benchmark margins taking away about €40 million from our clean EBITDA. The emissions provision is also beginning to sort of eat into our operating results. As you know, the CO_2 emission costs have gone up over the last year or so. So, it's becoming a more important number.

On the positive side, the performance of the units has been quite positive, quite strong and you can see that asset utilization, supply optimization and better refinery production has allowed us to deliver a very strong performance for the quarter.

On the balance sheet side, we have very good developments on all fronts; the maturity profile is very balanced. The 2018 maturity was repaid last month in October. However, that facility has been renewed and is in place which means that not only we have a very reasonable maturity profile but we also have ample capacity for the Group. And you can see that financial costs are actually moving down as well.

Moving onto Page 13 and 14, we have the refining supply and trading business in Greece. Again the key point is high utilization rates and normalized operations especially in Elefsina. But, given that do run the three refineries as a system, any utilization is within one of the 3 refineries it's bound to have a knock-on effect on the other 2 as well.

So, we like refineries that work normally without any problems as it allows us to optimize the crude slate and the production in a much better way. So, a very good performance for the domestic refining supply and trading business.

You can see on Page 14, it's quite evident that the utilization of Elefsina has more than doubled from 680 in the respective quarter of 2017 to 1.5 million tons, which is effectively what we have been saying about the down time last year.

In terms of crudes and feedstock sourcing, the key point to note is the replacement of Iranian crudes from other crudes. We have a very small quantity, which is effectively some of the late deliveries in June of Iranian crude which found their way into the feedstock in July. But other than that we have been able to successfully replace those crudes with similar, with similar types of crudes without any financial burden to the Group.

In terms of production, the refinery yield for 2018 3Q is a very healthy one, because not only it shows that we have about 73% in middle distillates and gasoline, but we have only 10% in fuel oil production mainly coming from the Aspropyrgos refinery. Elefsina is a zero fuel oil producer and Thessaloniki is producing feedstock for the other refineries mainly.

So, it puts us in a very good situation for the next 2 to 3 years given the IMO, which is something that a lot of other refineries in the region will have to deal with. We will have to deal with as well, but clearly, at 10% of production, yields around 10 to 12% max. I think we are in a very good spot with respect to the IMO upcoming regulations.

In terms of sales on Page 15, you can see that we have been able to source almost 100% of the domestic market sales from our own production, up from 89% last year. And you can see that the exports market is growing for this quarter as well compared to last year simply because our production has gone up.

At the same time on Page 16, you can see that the over-performance which is effectively our definition of the difference between the net realized margins per barrel of crude compared to the benchmark using Urals as a benchmark as feedstock, has reached the highest ever value which is about \$7, \$7.3 per barrel. So, a very healthy position especially when you consider that this quarter the contribution of export sales is even higher, which means that the benefit of domestic market premia is actually having a negative impact on this over-performance.

Moving on to petrochemicals, a very stable performance. For the last 2 to 3 years, petrochemicals, have been delivering about €100 million of EBITDA per year and a very close number for cash flow given that they don't have a lot of CAPEX, which again is moving on a slightly different cycle from the refining business and allows us to have a baseline which is not entirely driven by the refining margins.

Clearly, a big part of this contribution is coming from the Aspropyrgos propylene splitter. So the vertical integration of our production chain allows us to extract this value.

In terms of marketing, domestic market is continuing to suffer in terms of demand, and also in terms of profitability. We have a relatively strong quarter in the third quarter. That is traditionally the case because of tourists and aviation. Aviation has proven to be a very strong performance in this quarter.

However, it would be a mistake not to recognize that the domestic market is going through a very difficult process. And that's actually the case for most retail businesses in Greece. On the international business, we have a slight deterioration compared to last year, which is mainly because of weaker retail margins in most markets. As we've seen, one of the reasons for the very high reported result has been the continuing increase of crude oil prices and product prices.

Unfortunately, when you see the end of chain, it's sometimes difficult to pass on these increased costs, which is loaded with taxes in most countries as well, to the end consumer. So whenever you have a rapidly increasing world price environment, it tends to create pressure on the retail end of the business.

On power and gas, we have an improved performance coming out of Elpedison. However, it's still very low. We have a low contribution at an EBITDA level and if you go at the EBIT level, we see the negative and that is because we are having problems with the market framework. And unfortunately, it is something that has not changed in the last few years.

Independent power producers are asked to cover the supply shortage in the market. They are often asked to step in to cover other producers' problems in meeting market demand, but at the same time, they are penalized in that they are not offered the proper remuneration. So it is something which needs to be taken seriously by the framework service and hopefully resulting in something better. This is particularly is the case with when the country and EU is making aspirational declarations about moving away from lignite and coal production into Nat gas and renewables. So with economics like that, it's a bit difficult to achieve this aspiration, which we have to by the way.

The lower gas fired production is actually taken its toll on DEPA as well. We have a lower contribution coming from DEPA. But the key messages here are, first of all, the DEPA privatization which after a good few years is coming to an end hopefully before the end of the year. And that will allow us to release capital, as I said earlier, and redeploy that in a more meaningful way for us. And at the same time it will allow DESFA to embark on a new chapter, if you will, and be able to strategically develop into the future.

DEPA is in the process of being reviewed and restructured with the retail business and the low pressure networks being acquired. So again, this is an area where we expect to have some developments in the next 6 to 12 months.

That brings us to the end of the discussion for the Group. So I will stop here and open the floor for any questions you may have. Thank you.

Q&A

OPERATOR: The first question comes from the line of Patricot Henri with UBS. Please go ahead.

PATRICOT H: This is Henri, and thank you for the presentation. I have three questions for you. The first one is on the fuel oil sharing the mix down to 10% this quarter, which is the level that you haven't achieved very often. So just wanted to know to what extent this is driven by the change in the crude slate. It appears to be slightly sweeter than usual or the tweaks that you have been doing to your refining system?

And then secondly, I wanted to ask about the waivers from the U.S. given to Greece earlier this week, and what it means for you if you are going to resume importing even in crude, after this news?

And finally, if you can give us some sort of guidance on how we should think about the full year dividend actually, in terms of… some of sort of payout ratio net debt level or any other metric we should have in mind? Thank you.

SHIAMISHIS A: Thanks very much, Henri. Let me start off with the third and the second question, and then I will pass on to Dinos Panas, who will talk a little bit about the fuel oil mix and the crude slate. Now, on the dividend, we set a pattern of paying around €0.45 per share a few years ago, and then we went into the crisis and the big credit crash for Greece where we sort of curtailed and in 2 years we actually didn't make any payments at all.

I think that the intention is to at least get to that level for the full year dividend. So that is if you will also portray it by the fact that our interim dividend is higher than what it has been in the past. And as I said, we need to sort of consider not only the full year results but also the DESFA proceeds payout where we have part of that close to €300 million being a candidate for distribution to the shareholders.

On the Iranian transaction waivers for Greece and another 6 countries, if I recall 7-8 countries, I think the only other European is Italy, I am afraid we know, as much as, you do at this point in time. We have seen the announcements. We have seen the press releases.

There is a lot of noise around that, but at this point in time there is nothing which is formal that we have received. We expect that something will be coming out pretty soon. Once we know what exactly we can and we cannot do, we will assess that and act accordingly. So I am afraid we don't have a lot more information to share at this point in time.

Now when the fuel oil yields, I will ask Dinos...

PANAS D: Hello, good afternoon. Yes, it is exactly a lighter slate. Our ELPE optimizer loved lighter slate during the quarter, and this you can see in Page 14. The CPC was something like 27% versus 14% in the previous quarter. So it is…this is the reason for the lowest fuel oil yield.

PATRICOT H: Understood. Thank you.

OPERATOR: The next question comes from the line of Bahl Sanjeev with Edison Investment Research. Please go ahead.

BAHL S: Two questions from me. Can you hear me?

SHIAMISHIS A: Yes, we can hear you.

BAHL S: Apologies. Two questions, the first was on refining capacity additions, over the course of 2019. I think the expectations about 2 billion barrels a day of additional capacity coming on stream from the Middle east and China. I was just wondering whether you have taken a view on potential impact that will have on Hellenic over the course of the next 12 months to 18 months.

And the second question was just looking at CO_2 allowance cost, they seem to be… they seem to have peaked and started to fall, I was just wondering whether you had an internal view on where those could head over the course of next 12 months as well?

PANAS D: Well… Yes, we see the refinery additions all over the world and in Turkey of course, and we have a demand…a global demand that is a little bit lower than this. So we are concerned, but we have a view that the margins over the next few months are going to be defined mostly by the IMO situation. And as all of you have already forecasted, we are expecting a very, very good cracks on the diesels, and since we are…have a production that is geared towards diesel.

We think that we are well-placed to take advantage of any opportunities that exist. So that was the first question and the second one was which one…?

BAHL S : CO_2.

PANAS D: We do not have a real view on the prices. What we are trying to do is, trying to cover our deficits gradually and follow the market.

BAHL S: Thanks for the answers.

OPERATOR: The next question comes from the line of Koskoletos Nikos with Eurobank Equities. Please go ahead.

KOSKOLETOS N: Yes, hi, good afternoon, Gentlemen. Just a quick…I think it is more of a clarity issue. Andreas, you mentioned €0.45 as a number that used to have in mind and most likely could be going towards that level for this year for 2018. But then you had also mentioned that the DESFA proceeds could be part of at least to be distributed as an extraordinary dividend.

Should we consider that whatever payment to be over and above the €0.45 or does the €0.45 target include whatever extra from DESFA?

SHIAMISHIS A: Good afternoon, Nikos. No I think you should include that as an additional to the €0.45 or whatever the final dividend is going to be.

KOSKOLETOS N: Okay. So when we say extra or it would be over and above…

SHIAMISHIS A: Correct.

KOSKOLETOS N: The operating so "Dividend."

SHIAMISHIS A: Correct. So the €0.45 is a benchmark if you will, I'm not saying it's going to be €0.45, it's…

KOSKOLETOS N: No. I understand.

SHIAMISHIS A: I am just indicating what it used to be, that for a full-year dividend and then we have the special distribution which may take place out of the DESFA proceeds.

KOSKOLETOS N: Perfect, clear. Thank you.

OPERATOR: Ladies and Gentlemen. There are no further questions at this time. You may proceed with your closing statements. Thank you.

SHIAMISHIS A: Once again, Ladies and Gentlemen, thank you very much for attending this call. It has been an easy one, given that we have a very good set of numbers. We expect that this year is going to be again a very strong year in terms of financial performance. Hellenic Petroleum has moved on over the last few years in terms of the size and the importance of this company.

And we believe that we are well-positioned. All of the investments that have taken place over the last few years, and specifically the Elefsina upgrade have put this company, this group in a unique strong position which with the IMO coming up in a year and a half from now… a year and three months, we will be able to enjoy a decent refining margin.

We know that it's a volatile business, it is a cyclical business, but at least we have done whatever we could to make sure that this company is well-positioned to take the benefit… to capture the benefit of these cycles.

We expect that over the next few months we will see the privatization process, conversion to its completion which is again a good thing because it will be provide clarity for the company in the markets and it would allow the full value potential of this Group to be demonstrated in terms of the market cap that we have.

Thank you and we look forward to renewing this call in three months' time.