ARC Ratings affirms ENMC's "BB+" rating, with Negative outlook

ISSUER

ENMC - Entidade Nacional para o Mercado de Combustíveis, E.P.E.

ISSUE RATING

BB+ Medium and Long Term (BB+, with negative outlook)

RATING DATE

15 September 2016

ARC Ratings, S.A. (ARC Ratings) has affirmed the "BB+" rating accorded to the EUR 360.0 million bond loan issued by ENMC - Entidade Nacional para o Mercado de Combustíveis, E.P.E. (ENMC), on 6 August 2008. Despite the partial recovery and stabilization of oil prices and oil product prices and, thus, the recovery of the financial debt's coverage by the oil reserves (at market value), the rating outlook continues to be Negative reflecting the Negative outlook recently accorded to the rating of the Portuguese Republic that is the sole shareholder of ENMC and has ultimate indirect responsibility for ENMC's liabilities.

COMPANY PROFILE

ENMC, founded in 2001 and headquartered in Portugal, is a State-owned entity and was assigned by law with the duty of being the Portuguese central stockholding entity in the constitution and maintenance of the strategic portion of national emergency reserves of oil and oil products. Additional responsibilities include the supervision of the National Petroleum System, monitoring the markets for crude oil, oil products, liquefied petroleum gas, biofuels, promotion of technical safety and fuel quality, as well as prospection, research, development and exploitation of oil resources.

RATING RATIONALE

The key rating drivers for ENMC's bond loan rating are:

- Government ownership – ENMC's share capital is wholly owned by the Portuguese Government. Consequently, its rating is indirectly linked to the ratings of the Portuguese Republic (BBB- / Negative / A-3), however there is no implicit timely support, but the Portuguese Government is ultimately responsible for ENMC's liabilities, as is established in law ("in the case of dissolution of the ENMC, the State assumes any losses arising from the liquidation of assets, as well as the residual responsibilities").
- Financial stability and favourable debt profile – Despite losses incurred due to the impairment in inventories (due to adverse oil price fluctuations, in part already reversed), and the consequent negative equity, ENMC's expenses (including bond loan interests) have been totally covered by revenues, mainly from the oil market operators. In addition, the entity's debt levels remain largely unchanged, still comprising the bond loan that is rated (EUR 360 million, repayable in 2028), and also maintain a positive cash position.
- 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 ENMC's bond loan rating are:

- Oil price volatility and the coverage of loan by reserves – The nature of ENMC's operations and concentration of its assets render its financial performance heavily exposed to oil price fluctuations. After a strong decrease from 1.4 times at the end of 2013 to 0.66 times at the end of 2015 and to 0.62 times at the end of January 2016, the coverage of financial debt by reserves recovered in the last months to 0.7 times at the end of March 2016 and to 0.89 times at the end of June 2016. Please note that ENMC also held a significant amount of cash and deposits and investments in debt securities issued by the Portuguese Government, thus the coverage of net financial debt by reserves was 0.77 times at the end of March 2016.
- Concentration of customer base – The majority of ENMC's revenue derives from just four companies: Galp Energia (represented 31% of ENMC's revenues in 2015), Repsol (26%), BP (16%) and CEPSA (14%).

RECENT DEVELOPMENTS AND OUTLOOK

In 2015, the total volume of oil products introduced for consumption in Portugal increased 2.6%, to 7.7 million tonnes, reverting the decline tendency (in 2014 it stabilized). Increases in the B (diesel) and C (fuel oil) categories compensated for decreases registered in A (gasoline) and D (liquefied petroleum gases – LPG) categories. Thus national's emergency reserves required (90 days) and ENMC' strategic reserves required (30 days) also increased 2.6%, in aggregate, to 1 904.5 thousand tonnes (tton) and 634.8 tton, respectively.

ENMC still maintained at the end of 2015 a large headroom between its own reserves (938.3 tton) and the legally required strategic reserves (634.8 tton), with significant headroom in all categories, allowing ENMC to continue replacing in part the operators' own obligation. All ENMC's own reserves are currently stored in Portugal, under agreements with Galp Energia and the Portuguese Government (for the POL NATO deposits near Lisbon).

ENMC's financial performance in 2015 was heavily affected by the significant oil price decline (as occurred already in 2014), with the entity recording an impairment loss of EUR 84.0 million (EUR 54.3 million in 2014). In the first quarter of 2016 the impairment was partially reverted (adjustment made by ARC), at the amount of EUR 14.3 million. At the end of June 2016 the impairment reversal would be EUR 83.3 million.

ENMC - FINANCIALS AND RATIOS (THOUSAND EUROS)

	2011	2012	2013	2014	2015	2015 Jan to Mar	2016 Jan to Mar	2016 (F)
TURNOVER	31,089	37,922	219,427	79,747	24,562	5,927	8,154	23,998
EBITDA	8,273	16,240	126,816	32,839	8,519	2,159	4,240	2,371
NET PROFIT FOR THE PERIOD	158	27	(11,894)	(26,869)	(83,370)	1,517	18,128	85,885
OPERATING CASH FLOW (OCF)	10,470	13,495	127,852	7,208	9,425	2,761	4,039	4,455
RESERVES' BOOK VALUE	348,914	349,601	279,692	321,091	237,087	321,091	251,401	320,371
RESERVES' MARKET VALUE	710,964	725,834	505,098	333,087	237,087	-	251,401	320,371
TOTAL ASSETS	386,856	390,912	387,140	350,867	272,127	349,795	290,053	357,012
FINANCIAL DEBT	362,945	366,567	360,019	360,013	359,676	359,572	359,504	359,568
NET FINANCIAL DEBT*	330,957	333,689	331,239	343,971	329,298	342,537	326,047	328,830
RESERVES' MARKET VALUE / FINANCIAL DEBT	1.96	1.98	1.40	0.93	0.66	-	0.70	0.89
RESERVES' MARKET VALUE / NET FINANCIAL DEBT	2.15	2.18	1.52	0.97	0.72	-	0.77	0.97
EQUITY / ASSETS (%)	5.4%	5.4%	2.7%	(4.7%)	(33.8%)	(4.1%)	(25.3%)	(2.2%)

Notes:
Figures rounded.
Accounts adjusted by ARC Ratings for analisys purposes.
2011 to 2014 annual accounts audited by Caiano Pereira, António e José Reimão, S.R.O.C.. 2015 accounts not audited yet.
****Financial debt net from cash and deposits and also from investments in debt securities issued by the Portuguese Government.***

Sources:
ENMC.

Thus, ENMC recorded a net loss of EUR 83.4 million in 2015 and a net profit of EUR 18.1 million in the first quarter of 2016. Without considering the impairment costs and gains, ENMC recorded a net profit of EUR 0.6 million in 2015 and a net profit of EUR 3.8 million in the first quarter of 2016.

In 2015 ENMC registered significant operational and financial expenses reductions in the management of oil reserves comparing to 2014 and to forecasts, allowing it to make an extraordinary increase in the provision fund in the amount of EUR 7.8 million.

The coverage of interest costs by EBITDA was 11.6 times in 2015 and the coverage of net interest costs by EBITDA was 209.8 times.

Reflecting the referred net loss registered in 2015, ENMC's equity decreased to EUR -91.9 million at the end of 2015 from EUR -16.3 million at the end of 2014 (reverted in a small part in the first quarter of 2016 to EUR -73.3million). The provision fund, included in equity, increased from EUR 13.8 million at the end of 2014 to EUR 21.6 million at the end of 2015 and to EUR 22.1 million at the end of March 2016 (corresponding to 5.9% of reserves' acquisition cost, compared with 3.7% at the end of 2014). At the end of March 2016 the provision fund was totally covered (127.6%) by investment assets in debt securities issued by the Portuguese Government.

At the end of March 2016 ENMC's borrowed funds consisted almost entirely of its financial debt (EUR 359.5 million), corresponding to the book value of the EUR 360 million bond loan being rated and that matures in 2028. The coverage of financial debt by the market value of oil reserves owned by ENMC decreased from 0.93 times at the end of 2014 to 0.66 times at the end of 2015 and recovered to 0.7 times at the end of March 2016 and to 0.89 times at the end of June 2016.

Without including any impact from changes in the market value of oil reserves, ENMC forecasts for the completed year of 2016 a net profit lower than EUR 0.1 million, considering the recovery from oil market operators of the forecasted costs in the activity of managing oil reserves, including the interest costs with the bond loan (net from interest gains in financial investments), and also the equilibrium in the total remaining activities (total forecasted operating costs in these activities amounts to EUR 1.7 million).

Considering the impairment recorded at the end of 2015 and the market value of ENMC's reserves at 30 June 2016, ARC Ratings included an impairment reversal in 2016 of EUR 85.8 million, leading to a net profit in 2016 of EUR 85.9 million. With ENMC's forecasts and ARC Ratings assumptions, ENMC would record at the end of 2016 an equity / assets ratio of -2.2% (compared with -33.8% at the end of 2015) and a coverage of net financial debt by reserves (at market value) of 0.97 times (compared with 0.72 times at the end of 2015).

THIS DISCLOSURE IS FOR INFORMATION PURPOSES ONLY AND SHOULD BE READ IN CONJUNCTION WITH THE RESPECTIVE RATING REPORT.

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