

ENTIDADE NACIONAL PARA O SETOR ENERGÉTICO, E. P. E.

ARC Ratings, S.A. (“ARC Ratings”) has upgraded to “BBB+”, with Stable outlook, from “BBB”, with Stable outlook, the final public long-term issue rating assigned to the EUR 360.0 million bond issued by Entidade Nacional para o Setor Energético, E.P.E. (ENSE), on 6 August 2008.

ISSUER	RATING CLASS	RATING	OUTLOOK
Entidade Nacional para o Setor Energético, E. P. E.	Long-Term	BBB+	Stable

Rating Date	13 September 2022
Initial Rating	2 June 2008
Last Review	9 September 2022
Next Review Date	13 September 2023
Criteria Applied	ARC Ratings’ Non-Financial Corporate Entities Rating Methodology

This rating action is based on the recent upgrade of the Portuguese sovereign rating, which improved its implied support to the company, in a context where the improvement of the coverage of the company’s net financial debt provided by the market value of its oil reserves had already led to a recent upgrade of ENSE’s rating. ARC Ratings will monitor the determinants of the assigned rating and the possible extension of ENSE’s duties and take action as needed.

The rating was assigned by ARC Ratings, S.A. and endorsed by ARC Ratings (UK) Limited in accordance with Statutory Instrument 2019 n° 266 - The Credit Rating Agencies (Amendment etc.) (EU Exit).

Table of Contents

- Issuer Profile
- ENSE’s Key Rating Drivers
- The Key Constraints on ENSE’s Credit Rating
- Key Tipping Points
- Shareholder’s and Governance
- Cash Flow Generation Capacity
- Financial Policy
- Forecasts
- Issuance Conditionality
- Related Criteria and Research
- Period of Analysis and Information Analysed

Analytical Contacts



ISABEL FERNANDES

Senior Corporate Analyst

Lead Analyst

isabel.fernandes@arcratings.com



VÍTOR FIGUEIREDO

Sector Head – Special Projects

Back-up Analyst

vitord.figueiredo@arcratings.com



PINKY SHARMA

Head of Credit Assessments

Panel Chairperson

pinky.sharma@arcratings.com

ISSUER 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 potential 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 2004, is a State-owned entity with the following duties:

- To be 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 is 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 the supply of crude oil and petroleum products, depending on consumption needs.

ENSE'S KEY RATING DRIVERS:

- Government ownership – ENSE's share capital is wholly owned by the Portuguese Government and the bonds being rated have a continual ownership clause regarding the maintenance of this sole ownership by the Portuguese Government. Consequently, its rating is linked to the ratings of the Portuguese Republic: BBB+/Stable/A-2 by S&P Global Ratings (S&P); Baa2/Stable/P-2/ by Moody's Investors Service, Inc. (Moody's); BBB/Positive/F2 by Fitch Ratings, Inc. (Fitch) and A(Low)/Stable/ R-1 (low) by DBRS Morningstar. Note that 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 issue 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 showed an increasing trend to EUR 71.8 million in June 2022, 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 strategic role in the Portuguese oil market and of its operations leads to a very high concentration of its assets on oil and oil derivatives and renders its financial performance (in accounting terms, without cash flow impact, as the company doesn't actively trade oil or oil derivatives) heavily exposed to oil price fluctuations. The recovery in oil price in 2021 led to the improvement of the coverage of gross financial debt by reserves to 1.37 times at the end of 2021 (from 0.82 times at the end of 2020). The coverage of net financial debt by reserves also increased to 1.71 times at the end of 2021 (from 1.00 times at the end of 2020). Thanks to the significant increase in oil price in the first half of 2022 these coverage ratios further improved to 2.43 times and 3.04 times respectively at the end of June 2022. After that date we saw a smooth decrease, with some fluctuations. In the long term the oil price maybe impacted by the slow energy transition trend towards energy sources with lower environmental impact.
- Concentration of customer base – The majority of ENSE's revenues (74.4%) continues to be derived from five companies, despite a decrease in 2021 compared with 2020: BP (accounting for 21.2% of ENSE's 2021 revenues), Repsol (20.2%), Galp Energia (16.2%), CEPSA (8.5%) and PRIO (8.3%). 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 credit ratings (the other two are not rated).

KEY TIPPING POINTS

Positive Turning Points

Triggers for a potential rating upgrade would come from an upgrade of the Portuguese Sovereign rating.

Negative Turning Points

Triggers that could prompt a rating downgrade would include:

- a downgrade of the Portuguese Sovereign rating; or
- 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. A new Board of Directors is expected to be appointed at short-term.

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.

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 2022, the provision fund was equivalent to 15.9% 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, with the cost being supported by 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 17 August 2022 ARC Ratings conducted a tele-conference call with ENSE's senior management as part of the analytical review process. The recovery of the oil products quantities introduced for consumption in 2021 and 2022, the reserves and its storage, the impact from the increase of inflation, the doubtful accounts receivables, the investment carried out and to be carried out, the 2022 budget and the oil prices volatility were the main themes of discussion.

CASH FLOW GENERATION CAPACITY

OIL PRODUCTS INTRODUCED FOR CONSUMPTION AND RESERVES OF CRUDE OIL AND OIL PRODUCTS

Since March 2021, benefiting from the gradual withdrawal of the restrictive measures imposed to contain the spread of Covid-19, there was a recovery of the total volume of oil products introduced for consumption in Portugal. Thus, after a 20.9% decrease in 2020, there was a 5.1% increase in 2021, to 6.96 million tonnes (Mton), with increases close to 7% in A category (gasoline) and B category (diesel). In opposite, there was an 8.5% decrease in C category (fuel oil and liquefied petroleum gas). The recovery trend continued in the 1H2022 with a 27.6% year-on-year increase (with increases in all categories), although volumes were still 4.6% below the 1H2019 (pre-Covid). In ENSE's view, due to the conflict in Europe between Russia and Ukraine and measures being taken to control the increase of inflation the recovery of the volume of oil products introduced for consumption in Portugal may slow down in the 2H2022.

The volume mix of oil products introduced for consumption in Portugal slightly changed in 2021 and in 1H2022. The B category accounted for 77.4% of the total in 2021 (76.3% in 2020) and 78.6% in 1H2022 (76.6% in 1H2021). The A category accounted for 13.7% (13.5%) and 13.1% (13.4%), while the C category decreased to 8.8% (10.2%) and 8.4% (9.9%) respectively.

As legally defined, the increase in the total volume of oil products introduced for consumption in Portugal in 2021 only impacts the calculation of the required oil products emergency reserves level in the 2H2022 and in the 1H2023.

It should be noted that the conflict between Russia and Ukraine, had no impact, so far, on the European regulation of reserves of crude oil and oil products. In addition, up to now, there was no need to use the national emergency reserves of oil and oil products in Portugal (contrary to what happened if some other European countries). Therefore, there was no change of the physical reserves owned by the company in 2021 and in the elapsed period of 2022.

ENSE maintains a flexible model of reserves, combining a level of physical reserves owned by the company for the long term and CSO tickets (Compulsory Stockholding Obligation) - short-term contracts that the company buys in the market (usually from European peers with excess of physical reserves) - as required to achieve the necessary level of emergency reserves. The level of physical reserves covered a large part of the needs, and the company just had to adjust the level of CSO tickets.

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. Thus, the analysis of ENSE's own physical reserves in the table beside is reported as at the end of 2021.

ENSE's own physical reserves remained at 0.94 Mton at the end of 2021, while its reserves contracted under CSO Tickets decreased by 58.5% to 0.51 Mton. This decrease of CSO Tickets was related with the reduction of the emergency reserves of crude oil and oil products, because of the drop in the total volume of oil products introduced for consumption in Portugal in the Covid-19 context (this evolution is a proof of the flexibility of the physical reserves + CSO Tickets model used by the company). CSO Tickets are contracted according to market demand for ENSE to replace the oil market operators (namely small oil operators). As usual, strategically, ENSE acquired in advance CSO Tickets (currently is under negotiation the acquisition for the 1H2023). 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 to replace part of the operators' own obligation.

The analysis of the composition of the reserves held by ENSE at the end of 2021 shows that: ENSE continues to own the majority of the reserves in physical products, which increased its share of total to 86.1% (from 72.1% in 2020), while the remainder being contracted under CSO Tickets (that decreased as abovementioned); the totality of ENSE's own physical reserves continue to be stored in Portugal, according to applicable regulation, while 13.9% of reserves contracted under CSO tickets were stored outside Portugal (in European countries with highly reputed entities); and finished products, without considering the CSO Tickets, accounted for 42.7% of the total stocks (this percentage was 36.8% considering the CSO Tickets) i.e. in both cases above the one third required by law. The percentage of finished products does not represent a concern in ARC's view, given there is oil refining capacity installed in

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

	FYE Dec 2017	FYE Dec 2018	FYE Dec 2019	FYE Dec 2020	FYE Dec 2021
OWN RESERVES	938,018	938,603	938,459	938,476	938,483
CRUDE OIL	538,082	538,082	538,082	538,082	538,082
GASOLINE	51,400	51,400	51,400	51,400	51,400
DIESEL	297,536	298,122	297,978	297,994	298,001
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 (*)	303,500	301,500	356,250	363,500	151,000
CRUDE OIL	153,500	246,500	320,000	363,500	151,000
GASOLINE	0	0	30,000	0	0
DIESEL	0	55,000	0	0	0
FUEL OIL	150,000	0	6,250	0	0
LPG	0	0	0	0	0
TOTAL ENSE'S RESERVES	1,241,518	1,240,103	1,294,709	1,301,976	1,089,483
CRUDE OIL	691,582	784,582	858,082	901,582	689,082
GASOLINE	51,400	51,400	81,400	51,400	51,400
DIESEL	297,536	353,122	297,978	297,994	298,001
FUEL OIL	195,000	45,000	51,250	45,000	45,000
LPG	6,000	6,000	6,000	6,000	6,000
TOTAL ENSE'S RESERVES IN DAYS OF CONSUMPTION					
GASOLINE	45	48	60	51	53
DIESEL	45	50	49	50	54
OTHER	112	54	60	59	59

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

Source: ENSE.

Portugal. In addition, according to ENSE most reserves owned directly by oil market operators are finished products.

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 Sines, in the South of Portugal, and in Matosinhos, near Porto in the North 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 continues to study storage alternatives with the goal of further reducing the operational cost structure of storing reserves of crude oil and oil products and reduce the dependence on Portuguese refining capacity. However, this cost reduction goal will always be subordinated to the company main priorities: the safety and quality of products and conditions of use in case of need.

The maintenance of the quality of oil reserves stored under the 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 based on 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. The investment carried out in 2021 was EUR 0.7 million, an increase compared with EUR 0.1 million in 2020. This investment has been impacted by constraints arising from Covid-19, late approval of the ENSE's budgets and need of approval by the owner of the infrastructure. According to ENSE, there is an acceleration of the investment in the 2H2022 in order to prepare the POL NATO deposits for the rotation of diesel (planned for the 2H2023), thus the company expects to meet the investment target in 2022 (or surpass) of EUR 0.9 million. For 2023, it is projected EUR 3.0 million of investment with the goal of accelerating the recovery of the POL NATO installations. 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 2022).

ENSE'S OPERATIONAL PERFORMANCE

ENSE's 2021 financial statements were audited by Vitor Almeida & Associados, SROC Lda without qualifications. However, an emphasis was presented regarding the fact that it is not possible to anticipate the consequences arising from the conflict in Europe in terms of the economy and consequently of the ENSE's economic and financial structure. The company's Board of Directors considers that its continuity is not jeopardized. As usual, the interim accounts are unaudited.

ENSE's revenues decreased year-on-year by 5.1% in 2021, to EUR 27.1 million, and by 15.8% in the 1H2022, to EUR 13.0 million. ENSE's revenues primarily come from its main activity (holding and managing reserves of crude oil and oil products), which accounted for 98.5% of total revenues in 2021 and 95.7% in the 1H2022. 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). Its main revenue decreased by 5.5% in 2021 and by 20.1% in the 1H2022 primarily related to the decrease of CSO Tickets sales to the main oil market operators (at their request) due to the reduction of emergency reserves following a drop in total volumes of oil products introduced for consumption in Portugal (in the Covid-19 context). ENSE's other revenues come from its other duties, and it aims to cover its expenses with them. These revenues included EUR 0.4 million in 2021 for the issuing of biofuel tickets, a modest increase compared with EUR 0.3 million in 2020 (biofuel tickets are a mechanism to facilitate the control of the compliance with the obligation to incorporate biofuels in fuels), and other fees.

ENSE's turnover continues to be mainly originated from the leading distributors of oil products in Portugal. In 2021 the five main customers accounted for 74.4% of its total turnover (compared with 88.4% in 2020). The decrease was due to the lower need to purchase CSO Tickets, particularly by GALP, with impact on the breakdown of ENSE's total turnover by its main customers, as indicated below:

- BP p.l.c. (21.2% in 2021; 20.9% in 2020), which is not rated by ARC (A- / Stable / A-2 by S&P; A2 / Stable by Moody's; and A / Stable / F-1 by Fitch);
- Repsol (20.2%; 21.2%), which is not rated by ARC (BBB / Positive / A-2 by S&P; Baa2 / Stable / P-2 by Moody's; and BBB / Stable / F2 by Fitch);
- Galp Energia (16.2%; 26.7%), the market leader; Galp Energia is not rated; Galp Energia is also ENSE's main provider of oil reserves storage;
- CEPSA (8.5%; 9.3%), which is not rated by ARC (BBB- / Stable / A-3 by S&P; Baa3 / Stable by Moody's; BBB- / Stable by Fitch); and
- Prio Supply, S.A. (8.3%; 10.3%), a Portuguese company not rated.

ENSE's operational expenses mainly comprise supplies and services and staff costs. In 2021, supplies and services decreased by 12.8% compared with 2020, mainly thanks to the decrease of subcontractors' costs related to the acquisition of CSO Tickets (less quantity and lower price) to EUR 1.1 million (EUR 4.6 million in 2020). Staff costs were EUR 2.5 million, increasing by 53.1% compared with 2020 mainly because of staff reinforcement (with the annual average number of employees up to 48 from 33) to perform the supervision duty. The company's internal skills and resources allowed it to replace some external specialized services. In the 1H2022 both operational expenses dropped year-on-year. The supplies and services costs decreased to EUR 9.3 million (-0.9%), benefiting from the decrease of costs related to the acquisition of CSO Tickets which more than offset the increase of storage costs, whilst the staff costs exceptionally reduced to EUR 1.1 million (-5.9%).

We should note that due to the late approval of the company's 2021 budget there was an absence of rotation of diesel stocks in the POL NATO infrastructure (as occurred in 2019/2020). However, thanks to the very good storage qualities of this infrastructure, these diesel stocks still meet the quality requirements. This absence of rotation represented a cost saving of EUR 1.0 million against the forecast.

In 2021 the company recorded impairment costs, net of reversal of impairment, of EUR 0.7 million (a decrease compared with EUR 1.0 million in 2020) to fully cover doubtful customers (small market operators). In the 1H2022 was recorded a EUR 0.1 million reversal of impairment (versus any impairment/reversal in 1H2021). There were no impairments regarding its main customers.

ENSE - FINANCIALS AND RATIOS I/II (THOUSAND EUROS)

	FYE Dec 2017	FYE Dec 2018	FYE Dec 2019	FYE Dec 2020	FYE Dec 2021	1H 2021	1H 2022	2022 (F)
TURNOVER	25,398	24,266	26,116	28,514	27,064	15,477	13,031	29,424
EBITDA	7,722	2,958	4,938	6,352	6,682	4,873	2,598	3,020
EBIT	12,744	(23,684)	48,971	(69,894)	86,710	4,682	2,516	2,508
FINANCIAL RESULT	659	647	654	276	(35)	(18)	(12)	(37)
NON-CURRENT RESULTS	(7,931)	(20)	(4,745)	(5,639)	(6,543)	(1,177)	(1,226)	(2,453)
NET PROFIT	5,460	(23,386)	44,862	(75,272)	80,115	3,487	1,278	18
OPERATING CASH FLOW (OCF)	11,912	3,219	5,439	6,287	7,118	4,256	385	4,864
CASH FLOW	12,086	3,372	5,945	6,968	7,235	4,251	366	4,822
FREE CASH FLOW	11,785	2,690	5,149	16,764	6,228	4,075	161	3,332
Contribution Margin (%)	34.3%	18.5%	24.6%	27.8%	33.7%	39.0%	28.3%	18.3%
EBITDA Margin (%)	30.4%	12.2%	18.9%	22.3%	24.7%	31.5%	19.9%	10.3%
Operating Return on Turnover (%)	50.2%	(97.6%)	187.5%	(245.1%)	320.4%	30.3%	19.3%	8.5%
Net Return on Turnover (%)	21.5%	(96.4%)	171.8%	(264.0%)	296.0%	22.5%	9.8%	0.1%
Payout Ratio (%)	0%	0%	0%	0%	0%	0%	0%	0%
Coverage of Interest Costs by EBITDA (x)	206.3	79.0	131.9	169.7	178.5	260.3	208.2	80.7
Coverage of Net Interest Costs by EBITDA (x)	-	-	-	-	191.3	-	-	-

Notes: Figures rounded. Accounts adjusted by ARC Ratings for analysis purposes. 2017 annual accounts audited by Moore Stephens & Associados, S.R.O.C.. 2018 - 2021 annual accounts audited by Vitor Almeida & Associados, S.R.O.C., S.A.. The interim accounts are unaudited. F = Forecasts.

Source: 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, as the oil price at the end of 2021 was higher than the one at the end of 2020, the company recorded EUR 81.1 million reversal of impairment. On the contrary, in 2020 the company had recorded an impairment loss of EUR 74.9 million. Usually, ENSE only records an impairment loss or reversal of prior impairment losses in its inventories at the end of the year which limits the comparison between the annual and semi-annual accounts. However, in the 1H2022 this impact would not have been significant as the remaining impairment loss that could be reverted is now very small.

In 2021 ENSE increased the provision fund by EUR 6.5 million (16.0% above the 2020 figure). In the 1H2022, similar to the 1H2021, the increase in the provision fund was EUR 1.2 million. 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.

INTEREST COSTS AND COVERAGE RATIO

In 2021, 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 (equal to the 2020 figure). ENSE has not had to pay interest in 2021, only fees. The interest gains from the investments in debt securities issued by the Portuguese Government were almost nil in 2021, due to the 0% interest rate, therefore the financial result was very moderately negative (compared with EUR 0.3 million in 2020). In the 1H2022 the financial result continued very moderately negative. The coverage of interest and other associated bond costs (fees) by EBITDA remained extremely high, at 178.5 times in 2021 (compared with 169.7 times in 2020) and at 208.2 times in the 1H2022.

NET PROFIT

ENSE recorded a EUR 80.1 million net profit in 2021 (compared with EUR 75.3 million of losses in 2020) primarily due to the reversal of impairment on its reserves. The impact of the oil price volatility continued to be crucial for the level and volatility of the company's results, but the relevance of this volatility is clearly subdued by the strategic nature of its activity and the reason why it maintains oil products stockholdings for the long term. In the 1H2022 the company's net profit was EUR 1.3 million (a decrease compared with EUR 3.5 million in the 1H2021, due to lower dilution of fixed expenses). As mentioned before, the 1H results don't reflect any impact from impairment or reversal of impairment on the company's reserves.

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

ENSE - FINANCIALS AND RATIOS II/II (THOUSAND EUROS)

	FYE Dec 2017	FYE Dec 2018	FYE Dec 2019	FYE Dec 2020	FYE Dec 2021	1H 2021	1H 2022	2022 (F)
RESERVES' BOOK VALUE	348,590	322,727	368,021	293,137	374,288	293,137	374,288	293,137
RESERVES' MARKET VALUE	403,831	327,926	435,007	293,310	492,555	441,974	875,353	n.av.
TOTAL ASSETS	404,310	381,729	430,955	362,651	450,464	368,044	451,885	373,391
NET WORKING CAPITAL (NWC)	383,543	364,383	413,806	354,803	440,886	359,564	443,369	361,560
NET WORKING CAP. REQUIREMENTS (NWCR)	348,233	323,294	366,966	292,199	373,760	293,333	374,943	292,836
NET CASH POSITION (NCP)	35,310	41,089	46,840	62,603	67,126	66,231	68,426	68,724
FINANCIAL DEBT	359,583	359,632	359,675	359,716	359,758	359,736	359,773	359,789
NET FINANCIAL DEBT*	308,357	305,716	300,608	294,343	288,152	290,287	288,005	285,771
RESERVES' MARKET VALUE / FINANCIAL DEBT	1.12	0.91	1.21	0.82	1.37	1.23	2.43	n.av.
RESERVES' MARKET VALUE / NET FINANCIAL DEBT	1.31	1.07	1.45	1.00	1.71	1.52	3.04	n.av.
Operating Return on Assets (%)	3.2%	(6.2%)	11.4%	(19.3%)	19.2%	2.5%	1.1%	0.7%
Gross Cost of Borrowed Funds (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Financial Debt / EBITDA (x)	46.6	121.6	72.8	56.6	53.8	36.9	69.2	119.2
Net Financial Debt/ EBITDA (x)	39.9	103.4	60.9	46.3	43.1	29.8	55.4	94.6
CASH FLOW Coverage of Net Financial Debt (%)	3.9%	1.1%	2.0%	2.4%	2.5%	2.9%	0.3%	1.7%
Equity / Assets (%)	8.7%	4.3%	15.3%	(1.0%)	18.4%	0.2%	18.9%	1.3%
Financial Debt Struc. (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%
LIQUIDITY RISK (%)	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Interest-Rate Risk (%)**	100.0%	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. 2017 annual accounts audited by Moore Stephens & Associados, S.R.O.C.. 2018 - 2021 annual accounts audited by Vitor Almeida & Associados, S.R.O.C., S.A. The interim accounts are unaudited. *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. n.av. = Not available ; F = Forecasts.

FINANCIAL POLICY

ASSETS AND LIABILITIES

At the end of June 2022 ENSE's assets raised to EUR 451.9 million, primarily due to the increase of the book value of its reserves. Current assets accounted for 99.6% of total assets (close to 99.7% in December 2020).

The book value of its reserves increased to EUR 374.3 million in June 2022. This value is the same as in December 2021, due to the company practice of only estimating the existence of any impairment or reversal of impairment at the end of the year, comparing the acquisition cost with the oil prices at the end of December. Consequently, the value of EUR 374.3 million reflected the book value at the end of 2020 of EUR 293.1 million adjusted by the EUR 81.1 million of reversal of impairment in 2021. At the end of June 2022, the market value of the company's reserves significantly increased to EUR 875.4 million, which means that under the same practice has it does for the end of the year the 2021 the remaining impairment would have been reverted (EUR 1.2 million).

The total amount of cash and deposits and short-term investments in debt securities issued by the Portuguese Government increased to EUR 71.8 million in June 2022 (EUR 65.4 million in December 2020), being ENSE's second biggest asset. EUR 59.7million of which was for the coverage of the provision fund managed by the company, while the remainder EUR 12.0 million is free to use, namely, to finance the company's investments related to its current duties.

The outstanding amount of accounts receivable was EUR 1.7 million in June 2022. The doubtful customers of EUR 2.7 million, related to small oil market operators, were fully covered by impairments. ENSE is taking measures to recover this value, at least partially.

The company's tangible assets of EUR 1.6 million in June 2022, mainly related to equipment, only accounted for 3.6% of its total assets.

In 2021 the company carried out EUR 1.0 million of investment (EUR 0.7 million of which in the in the POL NATO infrastructure), an increase compared with EUR 0.2 million in 2020 (EUR 0.1 million of which in the POL NATO infrastructure). In the 1H2022 only EUR 0.1 million investment was carried out (similar to the 1H2021). However, in the 2H2022 there is an acceleration of investment in order to prepare the POL NATO deposits for the rotation of diesel (due in the 2H2023). Thus, the company expects to meet the investment target for 2022 of EUR 1.4 million. It is worth mentioning that 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.

FINANCING AND COVERAGE OF DEBT BY RESERVES

ENSE's debt level remains unchanged, still comprising solely the bond issuance 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 continued 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 288.0 million in June 2022 (a 2.2% decrease compared to December 2020).

The oil price volatility significantly 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 improved to 1.37 times in December 2021, from 0.82 times in December 2020. The coverage of the company's net financial debt by reserves also increased to 1.71 times, comparing with 1.0 times in December 2020. With the oil price increase in the 1H2022, these coverage ratios significantly improved to 2.43 times and 3.04 times in June 2022, the highest in the latest decade.

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 2.52 times at the end of 2021 (2.55 times the net financial debt), an improvement compared with 1.35 times at the end of 2020 (1.38 times the net financial debt). CORES is not rated by ARC, being rated A/Stable/A-1 by S&P (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 with the purpose of building up and stockpiling strategic oil reserves improved the coverage ratio to 1.71 times at the end of 2021 (1.74 times the net financial debt) from 1.01 times at the end of 2020 for both ratios. SAGESS is also not rated by ARC, being rated AA/Stable/A-1+ by S&P (the same level assigned to the sovereign).

CAPITAL STRUCTURE, LIQUIDITY, AND INTEREST RISK

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 59.7 million in June 2022, from EUR 51.9 million in December 2020. At the end of June 2022 ENSE's equity was EUR 85.4 million. The oil prices increase in the 1H2022 was not recognized in the company's equity at the end of June 2022, because, as explained before, the company only reflects the impact of the oil price changes

on the value of its reserves at the end of each year (and caps that reflection on the cost of the reserves, that is, it doesn't reflect potential gains). However, if it had been reflected the impact would have been limited to a EUR 1.2 million increase.

The equity / assets ratio of ENSE was 18.4% at the end of 2021, an improvement compared with -1% at the end of 2020, and slightly increased to 18.9% at the end of June 2022.

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. The bond bears interest indexed to 6-months Euribor, with no floor, which means that due to the negative values for EURIBOR, ENSE has not paid interest since February 2016 until August 2022. We should note that the 6-months Euribor inverted the decreasing trend since the beginning of 2022 and became positive since June 2022, in a context of interest rate increases to control the current high inflation. Thus, in the next coupon due in February 2023 the company will pay interest considering the 6-months Euribor on 6 August 2022 plus the spread (0.12%). This will have an impact on the 2022 accounts of c. EUR 1.2 million related to August-December 2022 period. However, as mentioned before, the interest costs of the bond are recovered from oil market operators and, thus, this risk is not assumed by ENSE.

INSURANCE

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., which is rated A (Insurer Financial Strength) and A- (Long-Term Issuer Default Rating), Stable outlooks, by Fitch.

ARC Ratings is not aware of any significant contingent liability of the company at the end of June 2022.

FORECASTS

ENSE's 2022 budget prepared in September 2021, based on the 2021 estimates, was not yet approved, but it has been guiding the company's activity in 2022, adjusted as required by the change of circumstances.

This budget considered a modest increase of turnover in 2022 in ENSE's main activity, to EUR 27.0 million, and the start of diesel stocks rotation stored in POL NATO infrastructure (with a EUR 1.0 million operational cost). However, the diesel stocks rotation will be postponed for 2023 because of the existing operational constraints of the infrastructure, thus the need to complete the ongoing ENSE's investments. Nevertheless, the quality of the diesel stored remains high, despite some indicators of need to be rotated at short-term. The provision fund was expected to increase by EUR 2.5 million in 2022, to reach EUR 56.8 million at the end of 2022 (level already surpassed in June). Financial results were expected to be very modestly negative, but the most recent interest rate evolution will lead to a more significant (around EUR 1.2 million) negative financial result, a deviation that the company has headroom to accommodate namely with the saving in the cost forecasted for the diesel rotation. As usual, for the main activity, the principle underlying the forecast is to register a net profit close to zero (without considering any effect of impairment/reversal of impairment in the book value of its reserves).

The company forecasted an increase of the turnover of the supervision activity in 2022, in order to achieve the balance in this activity, but the delay in the legal approval of the update of prices for issuing biodiesel tickets, its main category of revenue, should postpone the achievement of this goal. Considering the benefits of its activity in terms of providing a greater supervision activity to all economy, the company has been proposing the allocation of some form of compensation to be included in the State budget, which would further help this activity to achieve equilibrium.

ENSE's 2023 budget is still in preparation and, therefore, is not available to be incorporated in the current review report. Still, the general principles that underlie this budget are the same of the previous budgets: achieve the equilibrium between income and costs in its two activities (without considering the impact of any change in the book value of its reserves). It should be noted that, in the current context of high inflation, if the increase of the company's main activity operational costs exceeds the assumption considered in the company's 2023 budget, there is a legal possibility of establishing an extraordinary instalment to be billed to operators in 2023, so that the net profit of its main activity continues to tend to zero. ENSE will also have a possibility of reducing the extraordinary annual contribution for the provision fund to balance the URP's net profit (due to extraordinary contributions done in previous years).

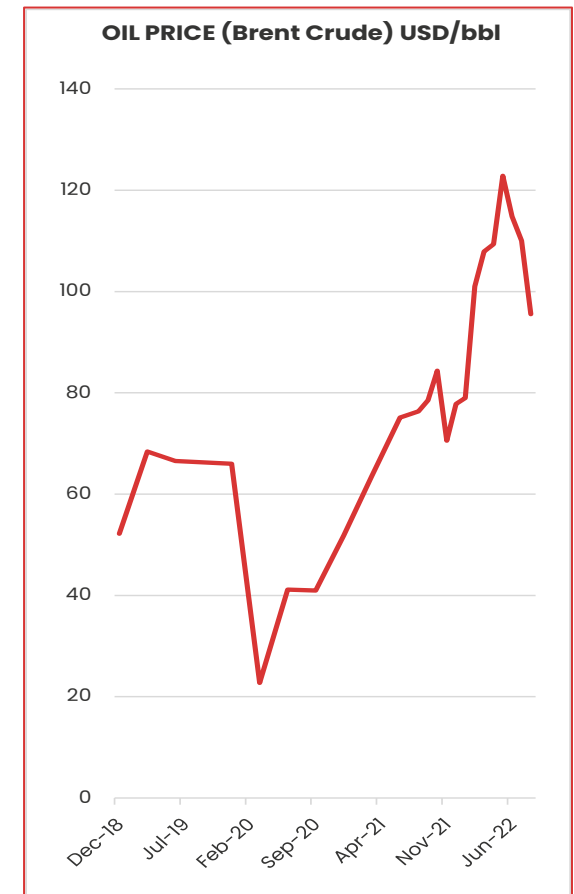
ENSE's net profit and the coverage of the company's net financial debt by the market value of its reserves depends on two key external factors: oil price and the EUR/USD exchange rate.

According to the World Bank Commodities Price Data, the average oil price (Brent crude) registered a 66.4% recovery in 2021, to 70.4 USD/bbl, with the increase of total world consumption (after the economic recession due to Covid-19) surpassing the growth of total world production. The increase trend continued in the 1H2022 and was exacerbated by the consequences of the conflict between Russia and Ukraine. Per the U.S. Energy Information Administration's forecasts, the average Brent crude price in 2022 is expected to be c. 48% above the 2021 figure, while for 2023 it is expected some decrease (c. 9%), but the current geopolitical situation and the economic impact of the measures that are being taken to curb inflation make these forecasts particularly uncertain.

The EUR/USD exchange rate showed a decreasing trend, with fluctuations, in 2021 (to 1.13 on 31 December 2021, from 1.23 on 31 December 2020) and in 2022 to the 1.0 since July, increasing even more the impact of the oil price increase in USD on the market value of ENSE's oil reserves recorded in euros.

While not expected in the short-term, the possible significant unfavourable evolution of the market value of reserves in euros would have a negative accounting impact on the company's equity, and related ratios, but no impact on its cash flow, given that it does not trade in oil products. Although trading in oil products is not part of the company's activities, oil reserves may need to be partially sold to respond to any strategical need, namely in the context of the European conflict, or, in the long term, as a result of lower consumption of oil products due to the energy transition trend. 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, as well as the strategic goal the company has in the Portuguese oil market, a role assigned by the government. However, it should be noted that no formal guarantee is in place.

The current context of conflict in Europe raised the need to implement a scheme of strategic reserves to be applied to gas, in addition to the existing emergency reserves (owned and managed by the incumbent operator of the country's gas transport, storage and regasification - Redes Energéticas Nacionais, SGPS, S.A.). This is being studied in Portugal and there are expectations for this study to be concluded in the short term. The final model to be adopted will depend on a political decision, but, given the current role of competences and the experience of ENSE, there is a good possibility that the solution to be adopted is the extension of ENSE's duties to also cover the acquisition and maintenance of strategic gas reserves. In ENSE's view, this potential duty is expected to follow the model of the acquisition and maintenance of the strategic portion of national emergency reserves of oil and oil products, i.e. the entity with that duty will get a long term financing to acquire the reserves and then pass all costs of maintaining those reserves to the market operators, with net profit of that activity tending to be null. ARC will monitor the possible extension of ENSE's duties.



Source: Bloomberg.

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 + 0.12% until 7 August 2023. This spread will slightly increase to 0.14% until the maturity.
- 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:
 - o 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;
 - o 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:
 - o 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);
 - o 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;
 - o non-performance of pari passu and/or negative pledge clauses;
 - o 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.

RELATED CRITERIA AND RESEARCH

ARC Ratings' Non-Financial Corporate Entities Rating Methodology

Entidade Nacional para o Setor Energético, E. P. E. Initial Rating Report (2 June 2008)

Entidade Nacional para o Setor Energético, E. P. E. Previous Rating Report (9 Sep 2022)

PERIOD OF ANALYSIS AND INFORMATION ANALYSED

PERIOD OF ANALYSIS

Historic: 2017 to 1H 2022

Forecast: 2022

INFORMATION ANALYSED

Entidade Nacional para o Setor Energético, E.P.E. Annual Reports and Audited Accounts – 2017 to 2021

Entidade Nacional para o Setor Energético, E.P.E. 1H2021 and 1H2022 Interim Accounts

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

Details on Entidade Nacional para o Setor Energético, E.P.E.'s Reserves

World Bank's Commodity Markets Outlook

DISCLAIMERS

ARC Ratings only provides a rating of the rated securities or of the issuer and neither recommends nor will recommend how an issuer can or should achieve a particular rating outcome. A rating does not cover a potential change in laws and is not and cannot be regarded as an audit. Moreover, ARC Ratings is not a party to any transaction documents of the instrument/transaction it is rating. Users of our ratings should familiarise themselves with the transaction documents. ARC Ratings does not act as a legal, tax, financial, investment or other advisor and users should seek professional advice from appropriate third parties where necessary.

ARC Ratings, S.A. is registered as a Credit Rating Agency with the European Securities and Markets Authority (ESMA), within the scope of the Regulation (EC) N° 1060/2009 of the European Parliament and of the Council, of 16 September, and recognised as External Credit Assessment Institution (ECAI).

ARC Ratings (UK) Limited is registered as a Credit Rating Agency with the United Kingdom Financial Conduct Authority, within the scope of the Statutory Instrument N° 266/2019, of 13 February, and recognised as ECAI.

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

Credit Ratings assigned by ARC Ratings are independent and forward looking opinions of the relative credit risks of financial obligations issued by various entities. The credit risk is the risk that an entity may not meet its financial obligations as they come due i.e. the capacity and willingness of an entity/issuer to make all required interest and principal payments on a given obligation in a timely manner in accordance with its terms. Credit ratings express risk in relative rank order – they are an ordinal measure of credit risk whose probability of default or loss may vary through the credit cycle. They are issued using an established and defined ranking system of rating categories (rating scale). ARC's credit ratings are determined using ARC's published rating criteria.

The rating(s) assigned by ARC Ratings in this report was/were sought by the entity whose financial commitments are being rated.

Prior to the assignment or revision of a rating ARC Ratings provides to the entity whose financial commitments are being rated the documents that substantiate the rating to be attributed. This entity is thus given the opportunity to clarify or correct factual details. The comments made by the entity whose financial commitments are being rated are taken into account by ARC Ratings in the assignment of its ratings. ARC Ratings also grants the issuer the possibility of appealing a rating accorded by ARC as long as this appeal is supported on additional information that has not been taken into account in the original rating.

ARC Ratings, S.A. historical default rates are published in the European Securities and Markets Authority Central Repository (CEREP) which can be accessed on the website ceres.esma.europa.eu/cerep-web/. It should be highlighted that ARC Ratings' rating portfolio can be characterized as a "very low default portfolio" and therefore the agency's historical defaults are not statistically significant. Default is the lack of full and timely payment of capital or interest or of the occurrence of any event that explicitly indicates that the future full and timely payment of those commitments will not occur (e.g., in case of insolvency).

Ratings do not constitute a recommendation or offer or solicitation to buy, sell or hold any investments that may be mentioned, and are only one of the factors that investors may wish to consider. The use of any rating is entirely at the user's own risk.

Throughout the entire period during which ratings are valid, ARC Ratings monitors the issuer's performance via public sources and information provided by the issuer/sponsor and, if a material development occurs, ARC Ratings may bring forward the date of the review unless stated to be a point in time rating. The updated list of public ratings is available on the website www.arcratings.com.

ARC Ratings' ratings are assigned based on information, which may include confidential information, collected from a wide variety of sources which ARC Ratings believes to be reliable including from the entity being rated or whose financial commitments are subject to rating. ARC Ratings has adopted and implements measures aiming to ensure that, to the extent available in the circumstances, it has obtained reasonable verification of the information it uses in assigning a rating and that such information is from reliable sources. Notwithstanding the foregoing, if ARC Ratings is not satisfied with the quality of the information it receives it will decline to assign the rating. The according of a rating should not be viewed as a guarantee of the accuracy, completeness, or timeliness of the information relied on in connection with the rating or the results obtained from the use of such information.

In the rating process, ARC Ratings adopts procedures and methodologies aimed at ensuring transparency, credibility and independence, and also that rating classifications are not influenced by conflicts of interest.

CONTACT DETAILS

ARC Ratings (UK) Limited

30 Churchill Place, Canary Wharf
London E14 5RE - UNITED KINGDOM
+44 203 927 8600
arcratings_uk@arcratings.com

Rhonda Moore
Business Development Director
rhonda.moore@arcratings.com

ARC Ratings, S.A.

Rua de São José. 35 – 1º B
1150-321 Lisbon - PORTUGAL
+351 21 304 11 10
arcratings_eu@arcratings.com



www.arcratings.com