Results' Presentation

Otelo Ruivo, Head of IR

Good morning to you all and welcome to Galp 1Q21 results presentation. I hope that you are all in good health.

This should be a shorter than usual call, focused on quarter results only. A broader update will be made during our upcoming Capital Markets Day, to be virtually hosted by late May or June. Dates and details will be circulated soon.

Today, we will have Filipe and Thore to take us through the quarter results and Q&A.

As usual, I would like to remind you that will be making forward looking statements that refer to estimates and actual results may differ to factors included in the cautionary statement at the beginning of our presentation, which we advise you to read.

I will now hand over to Filipe.

Filipe Silva, CFO

Thank you, Otelo and good morning everyone.

Strong quarter in otherwise difficult circumstances, but let me jump straight to the key drivers of that.

Q1 Ebitda was really an upstream story, as downstream in Iberia was still struggling its way out of the Covid-19 restrictions. Upstream production was marginally up QoQ to 125 kbpd. This was still impacted by the operational and logistic restrictions. Ebitda of €438 m, was up 37%. This is QoQ with the higher brand prices.

Commercial Ebitda of €69 m was actually quite resilient in the circumstances. Portugal was under full lockdown during most of the quarter, so it's no surprise that commercial volumes were down another 20% YoY, with jet alone down by three quarters. Happy to say that things are looking much better, now in April, with the end of the lockdowns.

On refining, margins improved slightly, averaging $2.0/boe in the quarter, supported by improved gasoline cracks. Still, this barely covers our cash costs and Matosinhos is considered as a discontinued operation, so this is Sines only.

Although middle distillate cracks remained under pressure, capped by weak demand, we are seeing improving market conditions with our refining margin currently above $3/boe.

On Midstream, the contribution was rather neutral, impacted by some headwinds this quarter. With the rapid increase in commodity prices, we had negative swing from the lag in pricing formulas. We also had gas sourcing restrictions from Algeria into Iberia, which forced gas purchases on the expensive spot market, so this squeezed our otherwise more supportive margins in the quarter. We also had extra costs to access the regasification terminal in Portugal, which we had flagged before, impacting results this year to the tune of around €10 m per quarter.

Renewables, they're not consolidated in our financials as the operations are mostly developed through JVs, so this shows under the Associates line.

However, to enhance visibility and highlight the value of this business, we are starting to also provide a proforma Ebitda for this business as if it was consolidated through the equity method, i.e., our equity stake. So, this renewable proforma Ebitda was just €1 m in Q1. This is a seasonally weak quarter for solar, of course, and this quarter in particular, we had the restrictions with transformers we had flagged before. Happy to say this is behind us and it's all operating at full capacity.

Now on the P&L, with Ebitda RCA of €0.5 bn. That's up 22% QoQ and driven entirely by upstream.

Associates of zero reflects the sale of GGND and the phasing out of Tupi BV, as all its equipment is booked in the Brazilian entity. Other than that, the international pipelines contribution was offset by the negative net income from renewables, which is still in the early stage of development.

On the financial results, we are now booking as special items the mark-to-market swings on client driven derivative and FX hedges. This removes unhelpful volatility in our RCA net income line. These are client-related hedges with little relevance to measure the underlying performance of the business.

P&L taxes were €181 m in the quarter, considering the effect of the strong upstream mix on production and income taxes. So, this quarter we had effectively no contribution on earnings before tax from the lower-taxed downstream activities.

RCA net income was €26 m and IFRS net income was €161 m and the difference comes mostly from positive inventory effects from the rising commodity prices.

On the cash flow, we have now added an adjusted operating cash flow indicator. This provides a good proxy of our clean operating performance, so this excludes volatile inventory effects, working capital variations and the special items. And under this metric, we delivered €445 m in the quarter, and that's up 46% YoY.

This quarter, we had €48 m in dividends from Tupi BV as we unwind this unconsolidated vehicle. CFFO was €377 m, considering a positive inventory effect, which was more than offset by a working capital build.

FCF generation was resilient at €175 m, or €514 m if you consider the proceeds from the sale of GGND. The GGND sale price was €368 m. We have another €25 m to be received now in this second quarter.

You will have noticed that we are now booking the reimbursement of principle on IFRS 16 leases below the free cash flow line. This is in line with what our peers do, so this is now considered as a reduction of debt, whilst before we had it as a free cash flow outlay.

Net debt was down by €513 m. And with the cash that we generated in Q1 we amortised a €0.5 bn Eurobond in the quarter. Our net debt to Ebitda now stands at 1.1 times with the last 12 months Ebitda capturing entirely the difficult Covid-impacted period.

Now, the Ebitda denominator is expected to start rising meaningfully from April onwards, also with commercial and refining contributions, whilst the net debt nominator should rise this quarter with the dividend payments and the last payment for the BMS-8, the Carcara acquisition, a disbursement of about €80 m. And liquidity remains very strong at €3 bn at the end of the quarter.

So, this is all from my side. Thore and I will now take your questions. Thank you.

Questions & Answers Session

Oswald Clint – Bernstein

Thank you, Filipe. I'll keep it just related to the quarter. First question was just on the Matosinhos refinery. I think last year you spoke about it saving €90 to 100 m of costs. Is that proving to be accurate so far after the first quarter? And I see some decommissioning costs for that refinery in the quarter. Can you tell us how big those should be ultimately?

And then secondly, we're just talking about gas and some of the sourcing restrictions you have, but I was more interested in what happens with something like Venture Global. It looks like they're looking to start that up in the second half, so I think you guys are taking 1 mtpa of that. Or are you expecting to take some of that this year? And what happens? It comes into Portugal and then you're going to be selling at some of the pretty high gas prices that we see today? Is that how that contract is going to work? Or perhaps you could add some colour please? Thank you.

Filipe Silva, CFO

Good morning, Oswald. On Matosinhos, the €90 to 100 m that we have provided you with is an historical number, and that's what it should have been under normal circumstances. So, we have about €60 m of opex and €30 m of recurring run rate capex numbers in that number.

So, we have no indication at this stage that the numbers would be different, so we are stopping some of the units. Actually, the units should be all stopped by the end of this month and we are starting the decommissioning phase. Decontamination will come much later, so from a cash outlay perspective, this will take a long time, but no difference from previous guidance.

On the Venture contract, this is first gas in 2023. We have a number of contracts, such as with Nigeria and Algeria. Those also mature over time, so the destination of the molecules will be whatever and wherever we can capture more value. So, it could come into Iberia. This is an Henry Hub indexed formula, we could divert some volumes from Nigeria to other places and bring those ones into Iberia and we can consider that for trading. So too early to tell exactly what the risk management will be around those molecules, but we will be short gas over the next few years if we don't renew the Nigerian contracts. Thank you.

Mehdi Ennebati – Bank of America

Thanks for taking my question. So, two questions, please, if I may. First question regarding your production. Can you please update us on your production at the end of April and are you confident that you will be able to grow the production from the current level in the coming month, or, on the contrary, would you say that the uncertainty remains currently quite high due to the pandemic situation in Brazil, which remains according to the news, out of control.

And second question regarding your capex guidance, please. I just wanted to know if there is a portion of your capex guidance this year which is related to Mamba project in Mozambique and if yes, would you say that the amount is substantial or not? Thank you.

Thore E. Kristiansen, Upstream COO

Thank you, Mehdi, for your question. I'll take the first and then Filipe will take the second question regarding Rovuma.

Two messages. One, we are reconfirming the guidance for the year of between 125 and 135 kboepd. Production in April has been ramping up according to our expectation, so in April we were running around 130 kboepd, so that's where we are and further guidance we will not do at this stage. Thank you.

Filipe Silva, CFO

Hi, Mehdi. So, most of Mozambique's capex we have on the plan and within the guidance we've provided you €500-700 m is mostly related to Coral, so Coral is advancing very nicely and according to plan. We are expecting a low burn rate on Mamba, given the circumstances. Thank you.

Joshua Stone - Barclays

Thanks, and good afternoon. Just two questions, please. One on refining margins, if you just give us an update of how margins have been trending in April and any views there.

Secondly, the upstream operating costs to barrel were quite low and impressive in the quarter. Is there anything to note there and the sustainability of that for this year? Thank you.

Filipe Silva, CFO

Morning, Josh. We are comfortably above $3/boe, month to date in April, so it looks better. Then we see also jet coming back, so middle distillates are less pressured in Iberia. Thore will take the opex question. Thank you.

Thore E. Kristiansen, Upstream COO

Thank you, Filipe and Joshua. With respect to opex, yes, it was low in the quarter at $1.8/boe. However, this is the flipside of Covid. Due to Covid and the restrictions that it imposes on us, we have a POB on board that is on average at around 70%, so that's actually the main reason. Plus, there was some adjustments for some past costs in Block 14. We are still comfortable guiding you that it will be below $3/boe. Hope far below. Will depend very much on what Covid will let us do of activities on the installation. Thank you.

Thomas Adolff - Credit Suisse

So, two questions for me please, as well. Just on the cash flow statement, the dividends paid to non-controlling interests, essentially Sinopec. It was zero in 1Q21, it was more than €100 m in 1Q last year. Can you just say kind of the timing for the payment of the dividend to Sinopec if any, and the amount of it?

Secondly, just on the lease payments. So, if you look at the IFRS 16 interests and the principal leases. The aggregate of that, if you deconstruct the €54 m, I think €19 m is related to IFRS 16 and then we have to reimbursement of €27 m in each quarter. So, is roughly €150 to 200 m the annual run rate going forward?

Filipe Silva, CFO

Good morning, Thomas. So, the dividend to our Chinese partner in Brazil is related to the fiscal year of 2020. This should be played out in Q2. We're guiding, and it's related to a relatively weak performance, of course, in 2020 in Brazil, to €100-150 m to be paid out this quarter.

The lease amounts. So, we've got about €150 to 200 m of interest plus principal every year and we have deconstructed that within what is real interest and amortisation of the principle as a debt reduction.

Michele Della Vigna - Goldman Sachs

Filipe, congratulations on this strong free cash generation in the quarter and two questions actually relating to cash flow. The first one is the dividend from the associates of €48 m in the quarter. My understanding is that we're unlikely to see more dividends from associates in the coming quarters but let me know if it that's not correct. And secondly, on the tax. The cash tax was much lower than the P&L tax in the quarter. I believe most of it was due to delayed timing in terms of oil pricing for the taxes in Brazil. How do you expect that to evolve in the coming quarter? Thank you.

Filipe Silva, CFO

Good morning, Michele. So, in the cost structure that the consortium had, the equipment was booked under the BVs, which was charging the consortium in Brazil with a cost-plus margin basis over time. As we unwind that vehicle, we are distributing the amounts that were captured over time through that margin. So, it is distributed out to the Galp perimeter, which you never saw that because Tupi BV was deconsolidated. There's still more to come, not significant amounts, but there's still more to come over the next two or three quarters, but immaterial amounts.

Cash tax versus P&L tax. So, we have a phasing effect in that, in Q1 we paid for the SPT tax in Brazil related to Q4 last year, when Brent was materially lower. So, if you assume Brent prices to remain flat for the rest of the year, that will gradually be captured over the next few quarters.

Please mind as well that when you look at the cash at the P&L tax line, this is an RCA tax calculation, whilst we are taxed effectively on the cash basis based on IFRS numbers, and taxed locally in every jurisdiction based on different tax incentives that we have, such as accelerated depreciations, etc. So, over time and as per previous guidance, we should expect to see a 40% cash basis and 50% P&L basis throughout the next few years. Thank you.

Michael Alsford - Citi

Thanks. Good morning, all. A couple of questions from me. On Commercial, clearly in the 1Q the volumes were all weak given the lockdowns across Iberia. I was wondering whether you could talk a little bit more about the trends that you're seeing now as some of the lockdowns have started to ease a little bit in 2Q. The second question I have is on the Upstream's DD&A. It was a bit lighter, I think, than some was expected, and I just wondered if you talked about how you see the trends there through the course of the rest of the year. Thank you.

Filipe Silva, CFO

Thank you, Michael. If we look out of the window, we see for the first time in many, many quarters, traffic and traffic jams. So yes, there's a very different environment since the end of the lockdowns. Jet fuel is going up, but it's still significantly below pre Covid levels. So, hopefully, we're way past the difficult period of Covid, but we remain cautious until we see it continuing on a sustainable basis. But it's looking much, much better now.

DD&A in upstream. Now we have lower production in Angola, so hence, unit of production metrics also changed, so we spread out depreciation based on unit of production. So that is the driver.

Matt Lofting – JP Morgan

Hi, thanks for taking the questions. Two brief ones. First, coming back to Thore's earlier points on production in April, sort of working a bit higher. I wonder, with the Covid backdrop etc. in the region, if you could just elaborate a bit on Brazil's offshore operating conditions, the extent to which you're sort of still seeing logistical restrictions relative to sort of the previous two or three quarters.

And then second, Galp talked in Q4 last year about submitting with the consortium on Lula-Iracema development plan this year, including a potential, I think, field life extension request. I just wondered if you could update us on the status of that. Thank you.

Thore E. Kristiansen, Upstream COO

Thank you, Matt. Let me first address your questions regarding production and Covid. As I said, as we are running right now with a POB that is on average around 70% of the normal population and that is due to minimising the level of people that are exposed to the pandemic. That has an impact on what we can do of maintenance. Of course, operationally critical maintenance is not sacrificed. But when it comes to connecting new wells and doing other maintenance, preventive maintenance, we are behind schedule. That is maintained for the time being with the current situation, in particular in Brazil.

And when it comes to Tupi-Iracema the work in the partnership goes really well. Very good meetings in the partnership with the view and the plans to developing a new plan for operation and development. And the target remains to submit this by the end of this year, and then it will most likely also include a request for field life extension, so it works. So far, so good. Thank you.

Jorge Guimarães – JB Capital

Good morning. Two quick ones. Firstly, is it possible to elaborate on the evolution of supply margins in gas and electricity in Portugal on the Commercial division? And the second, do you have any view on today's announcement by Total that it is declaring force majeure in the Mozambique project? Thank you very much.

Filipe Silva, CFO

Thank you, Jorge. I'll take the first one. So, on gas supply margins, it really depends on the different sources that we have, be it Algeria, Nigeria, or spot purchases. So, the market is more generous, I would say, in April then it was in Q1, so gas prices are going up. The issues that we have, despite better margins, is we have higher regasification costs in in Iberia, so that has depressed our 2021 numbers, so we expect this to continue until the end of this year.

Thore E. Kristiansen, Upstream COO

Thank you for the question, Jorge. So, we acknowledge what Total has announced today. The situation in Cabo Delgado is really severe, so it is understandable that this situation needs to be controlled first in order to make sure that the proper safety can be ensured for the people working on the activities. On our side, it doesn't directly impact us because the work for Area 4 continues to be optimise and improve that product in order to move it forward in the value chain. Thank you.

Biraj Borkhataria - RBC

Hi. Just two quick ones, please. The first one is: what proportion of your gasoline sales went to the to the US in the first quarter? And the second one: you might have mentioned this already, but my line was cutting out. Are there any Carcara payments due through the unit, if you could just outline what you're expecting there. Thank you.

Filipe Silva, CFO

Good morning, Biraj. On Cárcara we have about €80 m equivalent for payment of the acquisition of the additional stake in BM-S-8. And we are likely to take FID on the overall Carcara project, and so we will have Capex. Within our guidance of Capex, we have the FID taken, so that's built into the €0.5 bn to €0.7 bn.

Gasoline sales into the US is about 20% of the total volume exported. That's about 300 ktons or so. Thank you.

Otelo Ruivo, Head of IR

Thank you, this concludes our call today. Thank you for all your questions. Please contact our IR team if you need any additional clarification from our side. Our next event will be our Capital Markets Day. As we said at the beginning, we will announce soon the date and details for the Webcasts. We will look forward to having you all there participating at the event. Have a great week, enjoy the rest of the earnings season. And keep safe.