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"Second Quarter 2020 Financial Results" Conference Call

Thursday, 27th August 2020

18:00 (GR Time)

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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 Second Quarter 2020 Financial Results with the Management of the Company.

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

Gentlemen, you may now proceed.

SHIAMISHIS A: Thank you very much for this introduction and good afternoon to everybody participating. We will spend the next half an hour or so going through a discussion on the Second Quarter results, which clearly dominated by the events of recent months and the pandemic that we are all experiencing in Greece, and of course, throughout the world.

So, going through the first page, we thought that it's appropriate to set the scene for the operational environment that we've had to deal with. So, in terms of health issues, the COVID-19 situation in Greece was handled very well. The lockdown started fairly early in the process, as early as mid March, and in terms of the company as we have discussed a few months ago, we started even earlier addressing the issue. The result is that we've had no personnel health issues, minor instances and very isolated cases which did not affect the operation of the company.

We had 100% uninterrupted operation and of course we maintained 100% of the supply in the domestic market and in other critical markets of the supply.

Unfortunately, this was not the case with demand. We did not manage to do a lot about demand which collapsed in the process. As you know, the crude oil demand overshot supply and we had about 26 to 30 million barrels of drop per day at the beginning of the crisis. The OPEC and friends' decision helped to address part of that issue, but not before the end of April. So we witnessed a significant drop in the oil price and of course, we had quite a challenging period in the Second Quarter, given that when the crude oil price dropped, there was a stickiness on the product pricing, unfortunately, which helped report decent refining margins for April, but then when crude oil started picking up, we witnessed exactly the opposite because crude oil price went up, product prices went down and we had record low refining margin.

Even so we managed to maintain a positive operating cash flow. We engaged in contango trades which is effectively taking advantage of the balance sheet, the tankage, the trading expertise of Dinos and his team to trade around the forward curve being able to first of all, utilize part of the production which had no customers to go to, and make some money in the process.

Now as you can see, we put some statistics on this page just to signify the magnitude of the challenge that we had to face. 80% reduction in air traffic. I think we had days when there was not even a single flight coming into the main Athens airport and 80% drop in tourist arrivals in the country. Again, we managed to, if you will, optimize the situation through the storage management. We didn't have to close down any of the refineries with the contango trades again and some basic cost management for the obvious costs.

So, in terms of the key highlights, we've discussed the environment due to COVID-19, and we will be going through the basic drivers of the environment with Dinos in a while. The performance in terms of operations was positive. We maintained the supply at a very high level.

We've used our tankage to divert either crudes or products that were uneconomical to sell at the spot markets into contango trades. We managed to take advantage of the flexibility of the refineries in crude selection for the 3 refineries and delivered a significant over performance compared to the benchmarks that you will see in a minute.

And of course, in other businesses where we had the impact of COVID-19 and the repercussions, we tried to mitigate the negative effect as much as possible. Clearly, it is not possible to offset all of these effects, but at least to the extent that we could, we reduced the negative impact.

As a result, we have a positive quarter at €63 million, roughly 50% down compared to last year, and the reported EBITDA a bit higher than that, given that inventory gains were effectively reported in the quarter, covering part of the loss ground in the previous quarter.

In terms of net debt, we see a normalization at €1.8 billion as working capital which was used for contango trades was partly released. And we have ample of credit capacity in the system.

In terms of our CSR, we take pride in being one of the most important participants in this fight from a private company point of view in this fight for COVID-19, as we have been quite quick to support the government with a number of equipment and consumables by primarily by supplying a number of testing machines and about 10% of the tests that have been performed in this...in Greece during this period.

In terms of strategic and operational developments, we see an outlook...we see a weak market. Clearly, it's a period when everybody is a bit pessimistic and gloomy as the tourist season ends, which actually never started in full force. And people are coming back to the base city. We see a spike in the number of incidents. This clearly affects economic activity. So, we will have to manage in the next few months, a prolonged period of uncertainty until there is a positive development on the health pandemic front.

A key priority for us is the Aspropyrgos Refinery full turnaround, which is effectively starting tomorrow. It's on its own a very challenging task, because it's the biggest shutdown and maintenance schedule that we have undertaken in a single turnaround around of refinery. We have in excess of €130 million of maintenance and capital expenditure work to take place.

And that is on its own quite a task. We have more than 2,000 people visiting the refinery on a daily basis for the next two months. So, we have taken extra precautions for safety reasons and of course for COVID-19 protection of our staff and the contracted employees.

We haven't been standing still. Yes, we have lost some time at the beginning of the crisis. But in terms of strategic initiatives, we have moved forward on a number of fronts. The renewables transition is being…the energy transition is being pursued through the renewables project. The Kozani landmark project is expected to break ground in the next few weeks. We have a number of developments there and Georgios Alexopoulos will explain a little more about it.

The DEPA subgroup projects which involve the privatization of the infrastructure and the commercial business are being progressed, as well as the DEPA international business case which has been divested from. And we also have some developments there, which again, Georgios will explain when we cover the natural gas.

From a performance point of view, we have formally launched a 3-year digital transformation program, which is expected to deliver a significant benefit on an annual basis to the business. And that benefit is coming mainly from competitiveness improvement and from cost reduction. We've tested these numbers over the last year and it seems that we will be able to achieve at least as much as €50 million of improvements year-on-year.

In terms of results, you can see the numbers on Page 5. The big driver is the COVID crisis and the macros as a result of that, with the heavy demand drop in the Second Quarter. And we have effectively limited contribution from the associates in terms of the results and positive news on the financing which is gradually moving to the €100 million per year target which is what we said a few years ago.

Now, we will move on to the industry environment which Dinos will walk us through and effectively explain a little bit better the main drivers of the business.

PANAS D: Okay. Thank you, Andreas. Good afternoon to all. So on Page 7, according to the International Energy Association, the global demand fell by 16.4 million barrels in the retail in the Second Quarter of the year. These lockdowns were imposed to combat the COVID-19 pandemic. And of course, as a result of the collapse in the demand, we saw collapse in prices, and we heard the Brent crude price printing at its lowest quarter in level since 2003 at $29.6 per barrel.

We saw WTI settling at minus $37 per barrel on the 20th of April, with Naphtha flat price in the med at just $10 per metric ton, a week later. The WTI and Brent converging during the winter, while the Brent Urals differential inverted on reduced sour grades availability, following OPEC++ resolution.

Now, this Brent Urals inversion made other crude slates price on Brent like Basra, Azeri, Saharan and CPC, cheaper and more profitable for us to run than URALS, a fact that we managed to take advantage of during the quarter, as you will see later on during this presentation. The U.S., dollar maintained it is strength against the euro, as you can see.

Now, on Page 8, in this quarter we had the lowest quarterly benchmark barely positive just $0.5 per barrel, for FCCs and just $0.1 per barrel for hydrocracking and coking. We also have the longest trend of record low margins in the history, the gasoline and the diesel cracks during the quarter were very low, but the Jet cracks were negative.

As I said we witnessed HSFO cracks recovering from its lows that we saw in the previous two quarters, the First Quarter of 2020 and the Fourth Quarter 2019.

Finally, on Page 9 and on the domestic consumption, we had the gasoline consumption in Greece down by 30% in the second quarter, diesel down by 18% and LPG down by 17%. On the other hand, we had heating gas oil but…by more than 400% due to colder weather than 2019, more people working or just staying at home, very low prices and an extended tax derogation in May. The combination of these brought the overall domestic consumption at 1.56 million tons, the same as in 2019…second quarter 2019.

Now, the jet consumption was down during the quarter by 94%, the marine gasoil down by 33% and bunkers fuel oil down by 44%. This was also the case globally; we had the most severe drop in consumption in April, when we had in place the strictest social distancing rules for the quarter.

Following, April we had a steady partial recovery of the consumption, with a news…good news being that in July, the consumption of gasoline was down by just 6% and diesel by just 9.8%. Now, we're getting into single-digits reduction in the main products here in July.

And with this, I will pass you to Christian to comment on the group results.

CHRISTIAN TH: Good afternoon from me as well. We are on Page 11 now. So here like every quarter we present this page to you in a simplified version, just to see how results have been affected separately by the environment, and by our own performance.

As was mentioned earlier, you can see that although the impact of the environment has been quite negative, mostly due to the collapse of the benchmarking margins, and the lost sales contribution due to the pandemic. At the same time, we managed to regain back approximately half of that loss through our strong assets' availability and utilization. Our correct crude selections and, of course, the effect of the new IMO model. In total, resulting in a decrease in our adjusted EBITDA, Second Quarter on Second Quarter from 130 to 63.

Just turning to Page 12, on this page, you can see the maturity profile of our committed facilities. Overall, you can see that we've got enough capacity as was mentioned before, and a quiet phasing of maturities. At 30th of June, we were standing on an available headroom of €300 million, which was extended by another €100 million in the Third Quarter.

We are in the process right now refinancing our bank facilities, which are maturing in the next 9 to 12 months.

And while, you can also see the spike of the 2024 Eurobond yield in April, which has now normalized back through 2.26 %, as of few days ago. And just as mentioned by Andreas before you can see the finance costs approximately standing now at €100 million per annum, which is significantly lower from prior year.

I'll handover to Vasilis, who is going to take you through some further figures.

TSAITAS V: Thank you, Christian. Good afternoon to all of us listening. We'll go through the performance of the business, starting from refining, supply, and trading. On Page 14, and in the very difficult and challenging environment with record low benchmark margins, the lowest on average for the quarter that we've seen on our time series up to at least a couple of decades back, and the declining margins globally, regionally, and in Greece.

Adjusted EBITDA came in at €38 million, 43% lower. I guess, the main highlight was being able to sustain utilization of our refineries above 100%, so production being at the same levels of last year. Taking advantage of the crude spreads, especially in May and June that Dinos mentioned before, and utilizing our storage capacity and entering into the contango trades that will unwind in the Third and the Fourth Quarter with positive benefits on our financials.

Moving on Page 15, a closer look on our operations. We can see all refineries attained very high utilization levels and aggregate production. 2% lower year-on-year. On the crude sourcing, the main differentiation versus last year reflects the new IMO model for Aspropyrgos refinery. So, crudes for… from Azerbaijan, Algeria, and U.S. increasing their participation on our crude slate.

Also, the new model evident in the yield of our products with diesel and gasoline at… higher levels, if you compare with previous years. And HSFO at the minimum of 3%, that's the lowest we've seen with the new IMO fuel oil at 5%, while retaining the flexibility to switch depending on market conditions.

Moving on, on, on Page 16, sales were just over 10% lower year-on-year, evident…that you can see the decline on aviation and bunkering sales, given that this was effectively that showed the largest decline. Also, if you look at production, you also have around 250,000 tons of products that were set aside and entered into the storage/contango trades if you compare versus last year.

On Page 17, you can see the over-performance was retained at the very high level between $5.5 to $6 per barrel. That was due to the ability to take advantage of the crude spreads in May and June, as well as, the high heating gasoil sales in the domestic ground fuels market, which offset the decline on auto-fuels marketing in Greece, which was just over 25%.

We just mentioned before about the Aspropyrgos full turnaround, that's the most important project for this year. It's the largest ever turnaround that was undertaken in the Group after a 5-year run. Health and safety is obviously top priority, COVID-19 plays an additional challenge. As a result of that we are extending the turnaround duration by two weeks versus what would be the normal.

In terms of budget, €130 million CAPEX, around half of that is earmarked for upgrade projects, which are mostly focused on health and safety, including a large project that will bring down particulate matters emissions at the refinery by 6%. The lost output out of the turnaround will be around 800,000 tons in terms of lost production that will spread between the Third and the Fourth quarter.

And in terms of key targets, we'll address end of run performance with creep utilization and improve specs. And as I mentioned before, we have a lot of improvements in terms of safe and better operations, as well as emission reduction.

Moving on our Petrochemicals business on Page 16. Global macro had an impact on industrial production in the region and knock-on effect on our polypropylene benchmark margins, which were among the lowest, which we've seen. As a result, profitability was lower by just over 40% to at €16 million of adjusted EBITDA. Again, an important highlight is that we're able to place our products in the market and the impact on sales was relatively small.

Moving on our Fuels Marketing business, on Page 22. For those of us that have been following in the last few years, as you can recall that our domestic marketing business is a seasonal business with the Third…with the Second and the Third quarter being traditionally the stronger, as air traffic, tourism and coastal marine, are the main drivers for profitability.

During these periods, all those were activities that were most heavily impacted by the lockdown and the mobility restrictions of the Second Quarter, as a result of that profitability was also impacted. With the positive impact, again of heating gasoil sales that partially offset the negative impact.

On Page 23, our international marketing business. All of our…all of the countries that we operate were also equally affected by the mobility restriction measures. So, this is evident on the volumes, profitability further bit better compared to other business just 30% lower versus last year at €10 million adjusted EBITDA.

At this point, I will hand you over to Georgios Alexopoulos, who's looking after our renewables and power and gas business.

ALEXOPOULOS G: Thank you, Vasilis. On the renewables front, as Andreas already mentioned, we are approaching closing of the Kozani Landmark project in the next few weeks. We have already selected the optimal technical solution. We will be installing bifacial panels, and the project configuration is currently being finalized. Funding discussions are at… in advanced stage and based on the current schedule, we are expecting commercial operation in early 2022.

On other developments, we had a PV project securing reference price of €53 per megawatt hour in the recent RAE tender. At the same time, projects of approximately 50 megawatts reached the final stage of development, and in the context of the new licensing process that RAE has instituted, we have resubmitted all our recent production license applications under the new electronic permitting scheme. We are also currently looking at several opportunities in the market…in the renewables market.

Regarding power and gas, we are pleased to report a very strong quarter for Elpedison, €11 million EBITDA, €4 million EBIT on the back of higher availability of the Thisvi plant increased natural gas participation in the country energy mix and most importantly low cost raw material supply given the ample availability of cheap LNG in the market.

On the DEPA front, we are progressing on all the privatization fronts. More specifically, we have issued together with the privatization fund TAIPED, the request for binding offers for the DEPA infrastructure business that was issued in early August. Due diligence has commenced as you may recall there are five participating in the process and we expect binding offers in January.

On the DEPA commercial privatization where we participate together with EDISON**,** we expect to receive the request for binding offers in the next few days. Moreover, as Andreas mentioned, we are considering the divestment of the DEPA international projects business.

This is the third company created through a restructuring out of the original DEPA Group. There again, we own 35%, and we expect to be divesting this stake to the Hellenic Republic.

And with this, I think the presentation on gas and power is completed, and I will turn it over to Andreas.

SHIAMISHIS A: Thank you very much George. I guess, this concludes the discussion on the presentation part. As I said, it has been a very challenging… few months. We believe that we have managed to achieve decent results despite the challenges, clearly much weaker than what we would have been able to do otherwise, but at least we have been able to maintain positive performance and progress on specific fronts.

At this point, I believe that we are opening the call for any questions you may have.

Q&A

OPERATOR: First question is from the line of Patricot Henri with UBS. Please go ahead.

PATRICOT H: Yes, hello, everyone. Thank you for the presentation. I have three questions, please, the first one is on results of the Second
Quarter and the contango trade. I think you mentioned that these will contribute mostly in the Third and Fourth quarter of the year. So, there is not much of an impact from this contango trades in the Second Quarter.

And second, if you can also comment around the working capital movement and what drove the decrease in the Second Quarter, and I think it will change over the rest of the year. And then finally, if you can comment on the market condition and performance this summer in July and August, it looks like quite a challenging environment still, have you able to keep the utilization rate quite high. Any comment there would be helpful? Thank you.

SHIAMISHIS A: Dino, contango…

PANAS D: Okay. The first question on the contango and how much we expect to make in the contango and during what period, if I understand correctly. So, the contango we are expecting in total to make more than $50 million and most of this will come during the Third Quarter of the year. So, most of this, a majority of this is coming during the Third Quarter of the year, and some parts in the Fourth Quarter of the year and a small part in Second Quarter of the year.

What else, the market condition is now as I told you we see a recovery of the demand in Greece, July figures I mentioned before…official July figures, we see similar numbers from our sales in August. We had also replaced the products in the markets, in the international markets. So, but of course now we are having less quantities before we have the shutdown that we will have in a couple of weeks and will bring the production down.

So, we seem okay from this end, and the most of the contango's were improved. So, extraordinary we have built big inventories and products that we will not be able to send to the market. So, this is more or less what I can comment on this situation.

SHIAMISHIS A: Vasilis on the working capital.

TSAITAS V: Hi, Henri, on the working capital, as you remember, there was a working capital build in the First Quarter, that was due to the turmoil with the crisis that we saw in March and we mentioned in the last conference call that should gradually...that should gradually reverse so what you see in the Second Quarter is a partial reversal of that as the market in terms of prices at least crude oil prices start normalizing.

PATRICOT H: Great, okay.

OPERATOR: Ladies and Gentlemen, there are no more questions registered at this time. You may now proceed with your closing statements. Thank you.

SHIAMISHIS A: Thank you very much for attending this call. As I said at the beginning, these are very peculiar times to say the least. We have been through a very difficult period over the last few months on a global basis. All economies have been tested. Greece has done very well in terms of COVID. However, the impact on tourism has been more severe than in other countries because of the relative weight in participation and contribution in the economy.

This means that we will suffer as well, and we have suffered as well in the Second Quarter. And we believe that's going to be the case in the Third Quarter as well, given that Greece traditionally has a tourist... a tourism season which extends to the end of September.

So, we are bracing for a difficult quarter in Q3, but in terms of looking forward, once we get the Aspropyrgos maintenance out of the way, which will improve the performance, because we are experiencing end of run issues on the performance of the units. So, that's going to be resolved. We have progressed on strategic initiatives and we expect that over the next few quarters, we will be seeing a gradual recovery of the industry environment, and of course, we will be seeing the effect of our own actions on the results of the Group.

Thank you very much. And we look forward to having you on the call for the Third Quarter results.