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SPM.MI - Q1 2017 Saipem SpA Earnings Call

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## PRESENTATION

### Operator

Good day, and welcome to Saipem's First Quarter 2017 Results Conference Call. Today's conference is being recorded. At this time, I would like to turn the call over to Mr. Stefano Cao, CEO. Please go ahead, sir.

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**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Good morning, ladies and gentlemen, and welcome to our first quarter 2007 (sic) [ 2017 ] results presentation. I'm here today with Giulio Bozzini and a number of distinguished colleagues.

I will begin our presentation today by highlighting how in the current persistently difficult environment, our company has been able to deliver a robust operational performance. We have extended for another quarter the benefits of the constant focus on execution on efficiency and organizational measures.

We closed the quarter with revenues of circa EUR 2.3 billion and adjusted EBITDA above EUR 250 million, in line with our annual guidance, underpinned by E&C Offshore good results, thanks to the contribution of progress achieved on various initiatives and lower idleness and supported by a resilient EBITDA margin on ongoing although diminishing offshore drilling operations.

Onshore E&C business delivered a positive result with a 3% adjusted EBITDA margin, continuing on a path of progressive operational recovery.

In line with expectation, as anticipated in our full year 2016 conference call, our net debt increased to EUR 1.6 billion during the quarter, mainly due to the impact of cash distribution associated to project managed in joint venture. Although above year-end levels, our net debt dynamics during the quarter have further underpinned our confidence in achieving our net debt guidance.

During the quarter, further financial deals were executed aiming at optimizing our capital structure and extending our average debt maturity to 3.8 years. Our capacity to move fast in a persisting favorable condition of the capital market allowed us to arrange and successfully place a new bond issue on March 29 for the amount of EUR 500 million and a maturity of 5 year. Demand from institutional investors was strong, more than 3x



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the amount offered, prompting an improvement in inaugural bond benchmark term. This positions us well with the strength in capital structure for the medium term to capitalized upon the expected upturn in our market.

I'm also very pleased to announce that the new export credit facility was successfully concluded on the market with the support of Atradius, the Dutch export credit agency, for an amount of approximately EUR 270 million, strengthening our liquidity position. Giulio will elaborate more on these steps during his slides.

Before leaving the floor to him, I'd like also to remind you that our bond recently approved -- our board recently approved 1 to 10 reverse stock split operation, which will shortly go before the AGM called for April 28. This will substantially reduce the number of share outstanding, following the 2016 capital increase and alleviating the higher volatility associated with stock trading at prices below EUR 1.

Giulio, over to you.

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### **Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

Thanks, Stefano, and good morning to all of you attending our presentation today. First quarter revenues are broadly in line with our expectations. The decrease versus first quarter 2016 is across all businesses and due to the following: lower activity, chiefly in Caspian and Central South America in E&C Offshore as well as in West Africa and in America in E&C Onshore, higher inactivity in offshore drilling and lower utilization in onshore drilling mainly in South America.

Turning to margins. I would like, first of all, to point out that the difference between adjusted and reported results is due to the 2017 provision for redundancies, which are related to the reorganization of the group as announced last October.

Overall adjusted EBITDA is in line with our guidance. E&C Offshore margins increased versus 2016 as a result of good operational efficiency and lower idleness. E&C Onshore margins slightly increased, benefiting from operational improvement, greater efficiencies and the conclusion of legacy contracts, fully worked out from our backlog.

Drilling Offshore margins, despite slightly decreasing, were extremely resilient, notwithstanding higher idleness, since it is still partially backed by long-term contracts negotiated in a significantly better market environment. As rates are renegotiated, they will align to current market condition.

Drilling onshore margins continue to be penalized by depressed South American activity levels. As anticipated on previous calls, first quarter 2017 net profit is characterized by a normalized tax rate, following 2016 exceptionally high tax levels.

Net debt at the end of March 2017 amounted to EUR 1.6 billion, in line with our expectations. As already anticipated both in October 2016 and in February 2017, first half 2017 net debt evolution is penalized by the distribution of cash associated to project joint venture. In particular, around EUR 250 million were distributed in the first quarter 2017. You should note that around a further EUR 50 million in residual payments were made at the beginning of April 2017.

The cash flow generated in first quarter more than offset CapEx, which continues to be strictly monitored. Working capital dynamics were in line with our expectations, also thanks to payments of some historic overdue receivables. Working capital management remains a key element in respect to our full year guidance.

In the last presentation, I mentioned that after completing our permanent financial structure, we were monitoring financial markets to possibly strengthen our financial profile. In this respect, in first quarter 2017, we made notable progress. Firstly, within the frame of our EMTN program and following our inaugural placement in September 2016, given the positive market conditions, an additional bond tranche was placed and well received by the market amounting to EUR 500 million on a 5-year term with a fixed annual coupon of 2.75%.

Secondly, we have positively negotiated an additional credit facility guaranteed by Atradius amounting to EUR 270 million and available in more tranche of 8.5-year tenor each, starting 24 months from signature. The relevant all-in costs are around 2%.



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As a result of the above, I think that Saipem's permanent financial structure has been usefully reinforced. The average debt maturity was extended to 3.8 years. We have no significant maturities in 2017, and those of 2019 are more than covered by the undrawn export facilities guaranteed by GIEK and by Atradius. Available excess cash at the end of March 2017 amounted to EUR 958 million versus EUR 900 million at the end of 2016.

We have a committed revolving credit facility of EUR 1.5 billion expiring end of 2020 as well as few uncommitted credit lines for treasury purposes.

Having said that, we will continuously monitor the financial market, and we remain alert to future options to still further strengthen our financial profile.

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### **Stefano Cao** - Saipem S.p.A. - CEO and Non Independent Director

Okay. Thanks, Giulio. Let's now move to our business update section. The relative stability of oil prices at around \$50 a barrel in the recent months has not translated yet to a change in investment approach by the upstream oil and gas players. Demand forecast for oilfield service industry is still expected to remain under pressure throughout 2017, especially in Offshore E&C, and leading to very few initiatives being sanctioned in the quarter.

Our company was not immune to this trend, with no major project awarded in the quarter. However, thanks to smaller initiatives awarded, including the Perro Negro 4 contract extension reported in our full year '16 presentation, and now included in the backlog, and variation order formalized on some ongoing projects, we were able to close in the first quarter of 2017 with a backlog of EUR 12.5 billion, compared to the EUR 14.2 billion at full year 2016.

For different reasons, those initiatives which we had expected to be already sanctioned have been delayed, such as the high-speed train project which is pending the investment and funding authorization by the Italian Ministerial Committee, and West Hub, which by decision our clients is smoothly progressing, but under work order mode.

Advanced negotiation are proceeding on the Zohr Phase 2 project. Simultaneously, we are progressing ahead of schedule with the offshore activities on the early development phase of this project.

Negotiations are also ongoing with reference to offshore drilling contract regarding Scarabeo 8 for possible extension up to the year-end, Saipem 12000 for activity in East Africa and other opportunities for Scarabeo 5. In addition, following the end of the quarter, we have been successfully concluding a contract for Saipem 12000 with Eni, on which I will comment on our drilling review slide.

In terms of yearly coverage, the residual backlog, in addition to revenues accounted in the quarter, are now providing coverage of circa 80% of our guided revenue target, in line with historical coverage at this time of the year.

Turning to our customary schedule of offshore drilling commitments, notwithstanding the persistence of poor conditions and prospects in this segment, I'm happy to highlight that those initiatives we mentioned in our full-year presentation have been recently confirmed with new commitment. As mentioned earlier, we agreed with Eni a set of opportunities on a work order basis for our 12000 drill ship, starting with 2 wells in Cyprus plus option for other possible wells to be executed while the vessel heads to the Atlantic to perform prebooked drilling operation in Portugal, originally planned for 2017 and now postponed until 2018. These initiatives bridge other long-term opportunities which we are currently negotiating in East Africa.

For Scarabeo 9, we are finalizing a comprehensive commitment for the execution of a modification program to be implemented on our semi-sub and paid by the client throughout the year, enabling the transit under the Bosphorus bridge. Once finalized, the commitment will entail the drilling on 1 well plus 1 optional well in the Black Sea. Clearly, depending on the outcome of the exploration wells, we aim at extending the commitment in this area for a longer period, possibly with other clients.

Both initiatives envisage daily rate consistent with the current market for similar vessels.



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While we are also still negotiating possible extensions for Scarabeo 8 and Scarabeo 5 and tendering Perro Negro 8 in the Middle East, there are no significant opportunities for our vessel currently stuck in stack mode. And shortly, we will take a decision about a possible new scrap in the shape of Scarabeo 6.

Onshore drilling rig weighted average utilization rate was around 57% from 64% at the end of 2016.

In Latin America, there are still no signs of a recovery. Our activity remains under pressure, especially in Venezuela and Peru, although our costs have been reduced significantly. Argentina only presents signs of improvement in the region.

The Middle East is providing stability with the new contract extension announced in January, but already included in 2016 year-end backlog.

Last February, with our full year results, we provided highlights on headline projects. And with this slide, I wish to provide you with a brief description of other ongoing initiatives, which will significantly contribute to 2017 results. The first is West Hub, a deepwater project for Eni in Angola and a PCI contract for rigid and flexible pipeline, with related SURF facility to be installed with our FDS and Norman Maximus. By decision of our client, the project is advancing on a work order mode with engineering and procuring activities ongoing and the fabrication activities to be executed in our Arbatax in Italy. The offshore company is expected to start during the second half of this year.

I also wish to highlight the status of Kaombo project for Total. The project was impacted by delays. However, we have already implemented an acceleration plan to achieve key milestones. The plan has encompassed increasing the workforce in Karimun and Sembawang yard.

The Tangguh Expansion Project for BP was an important award in 2016 with 2 separate contracts: the offshore EPCI contract is progressing according to schedule. The detailed engineering phase is well underway. All critical purchase orders have been placed, and the platform structure fabrication is planned to start soon at Saipem Karimun yard in Indonesia. The onshore EPCC contract relates to a 3.8 million ton per annum LNG train with associated utilities. Engineering and procurement activities are on schedule and site logistics and mobilization started at the end of 2016.

Another important ongoing project is the KNPC Al Zour project in Kuwait. In 2015, Saipem was awarded an EPC contract for Package 4, covering tankages and related facilities of Al Zour refinery. The engineering and procurement phase is almost completed and construction work have already started.

Finally, a few details on the Khurais expansion project for Saudi Aramco. This EPC contract was awarded in 2014. The engineering and procurement activities are at an advanced stage with Saipem and subcontractors personnel fully mobilized at the construction site.

Our next slide provides you with our customary look across the various initiatives on which we are tendering or negotiating with our clients. Our commercial department remains highly active, on a large number of projects worth in excess of EUR 34 billion. However, the downturn persists and although we show several new additions here, a number of initiatives are now estimated to be sanctioned from 2018 onwards.

In E&C Offshore, despite the challenging environment, there are indications of some opportunities, which are expected to be sanctioned sometime this year, like the second phase of the Zohr gas development, currently under negotiation with our client in order to allow a seamless continuation of offshore construction operation after early termination of Phase I. While for West Hub, which you still find listed as an opportunity, as already mentioned, operations are progressing on a work order basis.

Other tenders include Liza EPC 3 for Exxon and Burullus Phase IXB in the subsea segment. In addition, we are pursuing other opportunity in E&C Offshore, such as BP Shah Deniz IMR activities and some other packages under the LTA agreement with Saudi Aramco.

Naturally, we look to derisk our portfolio through a diversification strategy, and we actively monitor the renewable and decommissioning markets, leveraging our distinctive assets and our expertise as a capable and reliable EPC contractor.



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In onshore, we are still participating to various tenders for sizable upstream investment which we anticipate moving ahead in Oman, Saudi Arabia, the Emirates and Kuwait. We'll continue to focus our attention to LNG initiatives, although it seems that FID on several such projects may not be taken soon.

Fertilizer plants, which leverage our property and technology, remains an important segment.

In infrastructure, as I stated already, we still await a decision from the Italian government regarding the Milan-Verona high-speed train project. Green light seems now to be expected between the second and third quarter of this year.

The cost saving program is progressing as scheduled targeting EUR 750 million run rate target savings for 2017. The program is already in an advanced completion status and the focus is now on the full harvesting of ongoing initiatives to exploit additional, although not major, upsides. We are on track with the planned headcount reduction, having reduced the full-time equivalent figure to around 36,500 at the end of Q1 2017.

With regard to the new operating model and organization, as mentioned earlier, we are progressing as expected. The new organization based on 5 strongly independent division, including the new high-value services division, with all the necessary levers to drive the business, will be effective during the second quarter.

And the Fit for the Future 2.0, we are also progressing, as expected, on the 800 redundancies linked to this program, having already achieved above 20% of the planned total.

In conclusion. We believe first quarter results continue to show a strong operational performance in light of a still challenging global environment. We are on track to deliver on the commitments made to strive on competitive even more at the bottom of the cycle. The financing operations duly described, with the new bond and the additional credit facilities, have strengthened our capital structure and increased our liquidity position. In addition, our new organizational structure will be fully implemented during the second quarter with these associated cost savings.

The overall progress achieved in the quarter, altogether, position us well on the way to meeting this year's forecast guidance.

With that, I would like to open the call up for your questions. Thank you very much.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Now we come to the first question for today, and it's from Amy Wong from UBS.

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### Amy Wong - UBS Investment Bank, Research Division - Executive Director and Analyst

Amy Wong from UBS. Just 2 questions for me. The first one just comes back to your E&C opportunity page, and you remarked that there were quite a few delays going on. So could you help us understand what are the main reasons that you see a lot of your clients push back? And perhaps if you can elaborate if there's any difference in behavior between offshore opportunities versus onshore downstream opportunities, that would be helpful. And the second one just comes -- my second question relates to the offshore construction division. You commented in the press release about the year-on-year performance. Like could we also understand the evolution of the Q-on-Q kind of how we went -- Q-on-Q from the fourth quarter to the first quarter, the performance there and the reason for the margin decline there.

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**Stefano Cao** - Saipem S.p.A. - CEO and Non Independent Director

Okay. I'll address question #1. Yes, there is, I would say, a difference in terms of the behavior of our clients, onshore and offshore. But firstly, let me comment on the underlying reason which was the first part of your question. I think as I was commenting, although there seems to be a fairly stable scenario at \$50 a barrel, we do not perceive, as far as our customers, so we don't perceive a sufficient level of confidence in the level of prices remaining stable going forward. And in practical terms, we don't see the CapEx rising again. Certainly, we see a slowdown in the reduction of the CapEx, but we seem still to be at the trough of the cycle in terms of capital expenditures for our clients. I think that for a combination of consideration, one related, indeed, to the fact that there is an underlying lack of reserve replacement, but this is obviously a judgment from the outside. So that should necessarily push our clients to reopen the CapEx programs going forward. I think that will be the time when we will see an impact in terms of more projects coming to final investment decision or more projects coming to tender. As far as difference of onshore and offshore, I would say the situation remains pretty much the same as far as, on the onshore, there is indeed an area of the world which is continuing investing heavily, and this is the Middle East. In particular, Saudi Aramco rather than Kuwait and Emirates, without making reference to the potential market of the Iran, which has been characterized by a stable volume of CapEx being brought forward. Offshore is rather more related to the cycle, to the comment I was making at the first part of the answer.

**Giulio Bozzini** - Saipem S.p.A. - Chief Financial and Strategy Officer

Yes, in terms of margins for the E&C Offshore. The quarter of 2017 showed an improvement versus the first quarter of 2016, and a decrease versus the fourth quarter of 2016. The reason of the decrease versus the fourth quarter of 2016 is mainly driven by the mix of the projects and the status of those projects. We had already anticipated that, in 2017, the margins would be lower than the margins that we experienced in 2016 due to the mix of projects, and I think that the margin that we achieved in the first quarter of 2017 are somewhat indicative of the margins that we will achieve for the full year.

**Operator**

Our next question comes from Michael Alsford from Citi.

**Michael J Alsford** - Citigroup Inc, Research Division - Director

So I've got 2, actually. Maybe just following on a little bit from the first couple of questions. I just wanted to get a sense, you mentioned the fact that there's, I guess, insufficient, sort of, confidence from your customers regarding some sanctioning new projects. I'm just asking really whether that confidence has increased with the stabilization of the macro or decreased into the beginning of the year. I'm just thinking that you actually has come back more strongly than the market would have expected, and therefore do we think that the award slipped further to the right as people get more uncertain, I guess, in the direction of the macro. That was my first question. And then just secondly on Kaombo, but I just wanted to get a sense as to your increasing cost in the project, and I'm just wondering whether there is still contingency remaining within that project or whether you're up against that level of contingency already.

**Stefano Cao** - Saipem S.p.A. - CEO and Non Independent Director

As far as the market evolution, let me comment on business line by business line. Let me start from onshore drilling. Like Latin America, which seems to remain depressed, I would say the other major area of operation for us, which is Middle East, has been reasonably more buoyant. So we see there signs of opportunities picking up. In terms of offshore drilling, I think, during my presentation, I tried to give you the flavor that although in terms of rate, we are obviously still talking of bottom of the cycle rates, we see a little bit more buoyancy in terms of opportunity of employing our units. I refer particularly to the 12000, which was one of the most sophisticated units which did not provide in our backlog any contribution. We see that things are moving there, as well as things are moving for the Scarabeo 9. We will undergo the modification, which will land at the end of the year. Then obviously, the unit will be capable of entering the Black Sea, and we shall finalize a commitment for, as I said, the drilling of 1 plus 1 well. The fact that we have a unit as sophisticated as Scarabeo 9 in the Black Sea, we believe it might convince other operators to have a utilization at, I would say, lower mobilization cost, just to state the obvious. As well as we are negotiating the extension of the Scarabeo 8 up to the end of



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the year, and we're negotiating on a much shorter time span also possible extension for Scarabeo 5. This is as far as drilling are concerned. Onshore E&C, I think I already commented there is indeed this area of the world, which keeps providing opportunities. I think consistent with what we said, we have decided to maintain a level of [rigorousness] in terms of the way we participate to bids. There are opportunities, I think, at this stage. The new commercial approach is paying in terms that, obviously, we have managed to resolve the issues related to a number of legacy contracts, and we are moving towards a better return for the activity. Offshore construction. Offshore construction, I think, is the area where we have to, at this time, we have to play on opportunity-by-opportunity basis. That's the reason why I specifically referred to the Phase 2 of the [ Zohr ] development in Egypt. That's the reason why I referred to a different approach to the West Hub development, whereby, obviously, the moment you invest, let me say, a couple of hundred million of dollars then it doesn't make any sense to stop. So the logic would say that you will get to the full completion of the project, which is in the order of magnitude, overall, of EUR 0.5 billion. Then there are the ongoing LTA, and we think we should get access to this. There are other opportunities, such as Liza. Liza is the new country. Obviously, one of the most important oil company in the world, Exxon. Then there are other things, which certainly will come up in terms of our subsea capability related to Sonsub and IMR activities and particularly in projects where we have already got the development project.

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**Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

With respect to Kaombo, as Stefano mentioned earlier the project is currently on delay with respect to the original baseline. We have already identified an acceleration plan finalized to the achievement of the key milestones sail away and first oil. The plan encompass the strengthening of the workforce in Karimun and Sembawang yards as well as the general optimization of the following activities. As of today, the activities in Karimun yard are almost over. North FPSO has been terminated and South FPSO will be ended in about 4 months. The operating activities are now mainly focused in Sembawang yard in order to be ready for the sail away as per current schedule. All costs overruns related to delays and acceleration have been assessed and incorporated in the project economics. The project is now at breakeven.

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**Michael J Alford** - *Citigroup Inc, Research Division - Director*

Sorry, one quick follow-up, if you don't mind. So just I'm going to, I guess, confirm or backfill the remaining revenue that you've got obviously delivered to meet your EUR 10 billion of target. It sounds like we should be looking at that for contracts being awarded in the drilling division. And I guess, West Hub is a key component of that. Is there anything else that you think about in terms of really filling that gap?

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**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Listen, you call it a gap, but this is castaway in our industry. I mean, being at 80% of the revenues at this time of the year, it's absolutely -- if you look in retrospect, you will find that probably even a lower coverage in the past, 80% is something which makes us more than confident that we shall have no issues in achieving the other percent target.

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**Operator**

Our next question comes from Phillip Lindsay from Credit Suisse.

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**Phillip Anthony Lindsay** - *Credit Suisse AG, Research Division - Research Analyst*

I just had 2 questions. The first one really follows on from the last one, but it's more focused on 2018. Obviously, you said 2017, 80% coverage now looks comfortable. And then -- but when we look to 2018, I mean, you mentioned Zohr Phase 2, West Hub, they look very, very promising, and that should help to close some of the gap that we can all see for 2018. But at this point and given what you've said in terms of business development prospects, do you think that a flat revenue scenario for '18, which is where The Street is at, is that looking a little bit optimistic to your mind? And then the second question, you're on the wires this morning, saying that you don't intend to break Saipem up. But at the same time, there's clearly businesses within the group that you consider to be non-core. So I just want to get a sense of the board's urgency to transform Saipem into a higher





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value-add group of businesses. Is cycle timing a priority in terms of when you're trying to extract value for many of the disposals that you may wish to make?

**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Okay. As far as your question, 2018, I'm sure you agree that, especially this time of the year, we don't provide any projection on 2018. So I think what -- during the course of 2017, what is extremely important to us is the progress on seeking all available opportunities, which are consistent with our capabilities and which brings value to our company in order to create sufficient backlog so to fill this 2018. But as far as target revenue at this time, especially this time of the year, we don't provide any indication. In terms of the comment I made earlier on and to which you are referring, the question was a simple question, and the question was are you considering break up, and my answer was quite strong, no way whatsoever. I mean, personally, I'm not here to break up the company. Then if you ask me a strategic, a more strategic question, then I would say that we are moving in the direction of creating the condition for business by business so that we can fully take advantage of the recovery of the cycle when it will come. I think you must remember that I consistently said that we consider the Offshore E&C as the core business of Saipem as far as the business where we express the highest level of capabilities, both in terms of people and in terms of the equipment and vessel which we operate. We have launched a program, a number of initiatives on innovation. We strongly -- I personally strongly believe that innovation is the tool which we need to employ in order to make the Offshore E&C capabilities grow in accordance with the market, which allows Saipem to be strongly present in that market and to provide our clients with solutions helping to reduce the breakeven cost for our clients. As far as the Onshore E&C, Onshore E&C is the business which has provided reason for, I would say, major concern in the past. However, we express a degree of competencies there and project management capability in such a high level that we did view changes in the approach to the business, and with the importance associated with the licenses which we own and with possible additional license which we may add to our portfolio is still a business which can provide good satisfaction to our company going forward. Offshore drilling, we operate a few number of high sophisticated units. That is not -- I would not see that as a major problem. Obviously, we are doing consistently with the crisis of the industry, we're doing cleanup of our fleet. We are scrapping the older units, consistent with the rest of the industry. I would not consider this business as an issue going forward other than being the natural and good complement to the E&C business in terms of cash flow provision. Onshore drilling, I think consistent with what I said, is certainly a business on which we may consider some portfolio activities, which does not imply at all that it needs to be a divestment. We can consider to join force. We can consider strategic operation with our operation. Finally, not in terms of volume, but in terms of capabilities, we attached a lot of value in the new division which we have created. As far as the division operating in a phase of the cycle closer to the client, when the clients make a major decision, strategic decision in how to develop the field, it is a good way to preserve the high-quality engineers, which otherwise associate with the overall reduction in volumes, it would be idle. So the alternative would be to dispose, unfortunately, to lose such capabilities. So I think that strategically is quite an important decision. I hope I have given you a full scenario, but a bit longer than I wanted.

### Operator

From Morgan Stanley, we've got Rob Pulleyn on the line.

**Robert John Pulleyn** - *Morgan Stanley, Research Division - Analyst*

Rob Pulleyn from Morgan Stanley. May I change (inaudible) slightly and ask a different topic here. There was a newswire regarding your discussions with Gazprom regarding the South Stream project for which, of course, there is moneys outstanding, with Gazprom signing essentially a counterclaim. I was just wondering what your thoughts were around whether this affects your ability to be made whole on the moneys owed from the South Stream contract. And I'll leave it at that for the moment and ask my second question when we've addressed it.

**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Okay, about South Stream, you will read on newspaper a flow of information related to the arbitration. So we have presented our claim. The counterparty has presented a counterclaim. I think that, that is the usual progress of an arbitration. What I can say is the outcome of the arbitration is going to be in middle of 2018. And so that will be the time of the final settlement of the issue. Of course, we are strongly convinced that what



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we are thinking in terms of reimbursement is what is fairly due to a contractor when a client decide in his own right and that this is absolutely part of the game. And it's normal in the industry to discontinue a certain -- cancel a certain project. And the discussion is around the compensation, which is due to the contractor, so it's a very -- a contractor dispute. Having said that, I think it is important to say that we continue to target not only Gazprom, but the whole Russian market as a very important market. We continue looking for additional opportunities for our operation, and we remain not open, but more than willing, to settle the issue, obviously, at a level which we consider satisfactory in terms of the impact which the discontinuation of the contract has caused to our company.

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**Robert John Pulleyn** - *Morgan Stanley, Research Division - Analyst*

Okay. And just a quick follow-up in terms of the net debt guidance. Can I just check in terms of moving parts that, that's still predicated on relatively small moves in working capital across the year, i.e. the seasonal moves in the first half will be offset with the seasonal moves in the second half?

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**Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

Yes, with respect to the guidance for the full year, we expect the working capital to remain substantially stable. So without any particular either improvement or deterioration. The deterioration in the first quarter was already anticipated and is due to the distribution of cash in project-related joint ventures, and this has been already anticipated. So we knew that the first quarter and the first half of the year would have been penalized. But apart from this extraordinary factor, there is a trend of recovery which in the first quarter has been confirmed.

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**Operator**

Our next question comes from Fiona Maclean from Merrill Lynch.

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**Fiona Margaret Maclean** - *BofA Merrill Lynch, Research Division - European Oil Services Analyst*

Yes, it's Fiona Maclean from Merrill Lynch. I have a couple of questions. I'd like to look at 2018 and a little bit more and try and understand how confident you can be with the potential for revenues in that year and also the progression on margins. And can you also clarify when we should expect Saipem to declare guidance for 2018? And then one last question. I'm sorry I missed it, can you just reconfirm when the Kaombo project is going to be completed for Saipem?

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**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

You referred to Kaombo?

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**Fiona Margaret Maclean** - *BofA Merrill Lynch, Research Division - European Oil Services Analyst*

Yes.

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**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

I think you referred to Kaombo as the project?

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**Fiona Margaret Maclean** - *BofA Merrill Lynch, Research Division - European Oil Services Analyst*

In terms of when it will be complete.



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**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Okay, 2000 -- your first question was related to 2018 and the creation of a complementary backlog which we need to get during the course of 2017. I think probably the last part of the presentation was devoted to the opportunities which we see closer to becoming material. I think those are still the main target for this year in terms of acquisition. Then I could, in summary, comment that, indeed, there are a number of Offshore E&C opportunities which we keep pursuing. I refer to something which is, logically speaking, is something which we consider already part in our mind of 2018, and this is the Phase 2 of the Egyptian development. There should be then a third phase, which may come following the second. Obviously, being mobilized we would be a natural candidate also for the third phase. Then there is -- I referred to the Exxon project in Guyana, the Liza. I referred to the West Hub, which again is something which is progressing in any case. And I would say it's progressing, although you don't see reflected in the number of the backlog. And LTA is something which is coming up. Then bear in mind that we have a number of -- a large number of initiatives which they do not attract the light of a press release, which have -- and I referred earlier on to Sonsub in in subsea. Certainly, we have a number of smaller initiatives which will naturally come. I referred to the diversified business as far as the decommissioning, decommissioning, especially in the North Sea, is a potentially huge market. We have the tools in terms of lifting tools, but we have the project management capabilities, overall, to run those measures, decommissioning. Going forward, we believe that there should be a new sort of approach in terms of taking responsibility for the end of life of a field, which is due to a bid, then subsequently decommissioned. I think that, that would imply that you can organize the dismantling of operations, while you are involved in the running of the latter part of the life of that. We have the wind, we are participating. I think I already referred to in our yearly results to the project launch by EDF which we are becoming sizable. I would say a dream project, the size can be as much as EUR 0.5 billion -- the size of EUR 0.5 billion. Then we are pursuing opportunities with DONG. So I would say, overall, you probably will see less very large projects, but a lot more of smaller project in terms of size. But altogether, they're filling up the gap, which we have in the backlog at the moment.

**Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

Maybe with respect to the timing of the guidance for 2018, the guidance of 2018 in terms of revenues will clearly depend upon the order intake over the next quarter. So the guidance will be given in February 2018, coming back to the usual schedule of giving the guidance. With respect to Kaombo, I think that we have to stick to what I mentioned before.

**Fiona Margaret Maclean** - *BofA Merrill Lynch, Research Division - European Oil Services Analyst*

Okay. And just for clarity, with regard to all of the projects that you listed that you're bidding on. Are you essentially saying that you think Q1 is the bottom for the backlog and it's going to increase (inaudible) going forward?

**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Right. Quite frankly, it is difficult to -- I mean, backlog is something which comes -- addition to the backlog, there comes a lag. So it's difficult to say whether this is the bottom or not. Certainly, if you look at the history, if you measure it by quarter, you see ups and downs. I think the clear message which we are sending is that EUR 500 million was the addition for this quarter. We have a large number, a sufficient large number of opportunities with which we are in the position to make up the shortages.

**Operator**

From Kepler Cheuvreux, we got Kevin Roger on the line.



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**Kevin Roger** - *Kepler Cheuvreux, Research Division - Research Analyst*

Just one quick question, please, for the 2017 top line guidance. You say that you have a coverage of 80% in line with the historical ratio. But when I look at the Q1 revenue and the backlog, you will need EUR 2 billion of additional revenue. And when I compare it to the Q1 2016, you only secured, I can say that, EUR 1 billion at the end of the year of additional revenue. Can you please elaborate on the reason making you thinking that you will be able to reach the EUR 10 billion target with EUR 2 billion of new revenue found over the year?

**Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

Yes. First of all, as you saw in the first quarter, basically, we had no major contracts awarded. So with the addition of a small contract plus variation order of existing contracts, plus the usual activity linked to frame agreements and service contracts, we manage basically to increase the 2017 coverage by approximately EUR 500 million. So should we consider something recurrent with respect to these activities, even lower, we reach an amount which can be estimated between 90% and 95% of the total EUR 10 billion of revenues that we are providing as a guidance. Then the balance will have to come from the contracts that we expected to be awarded this year. So basically, I think that there is a reasonable certainty of these revenues. Obviously, this will be dependent, as usual, also upon the progress on the awards and the progress on the project that which we expect both in the offshore and in the onshore to increase in terms of execution to the different phases of these projects over the next quarters.

**Kevin Roger** - *Kepler Cheuvreux, Research Division - Research Analyst*

Okay, very clear. And maybe just one follow-up on the offshore drilling segments. Did you still benefited in Q1 from, I would say, old contracts in a better environment and if the EBITDA margin could decrease again in Q2, Q3 as you stop to benefit from those contracts?

**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Certainly, the resilience which we specifically referred to in terms of contribution also in the quarter, it comes from contract, long-term contract which are still running. And in particular, the long-term contract are the ones those related to the 10000, those related to the Perro Negro 7, Perro Negro 5 units. And I would say that, also, the contribution coming from the Scarabeo 7, which runs up to the middle of next year. So this is, I would say, the underlying strength of the traditional portfolio. Then going forward, I think I don't need to repeat that we are moving towards present market rates, although we see opportunity for getting more optimization, becoming a bit more buoyant and promising.

**Operator**

Our next question comes from Maria-Laura Adurno from Goldman Sachs.

**Maria-Laura Adurno** - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Actually, I have 2. So the first one is with respect to the Onshore E&C segment and the margin progression seen quarter-on-quarter. Particularly, if I look at it, it's actually been quite a substantial improvement. So I was just wondering if you could maybe run us through the underlying drivers, where also we stand on pending legacy revenue and whether we should take that 3 percentage of EBITDA margin as the run rate for the full year. The second question is around Kaombo. And you mentioned earlier in the conference call that you currently expect the project to be breakeven, and I was just wondering if this is incorporated also in your full year 2017 guidance.

**Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

Okay. With respect to the margin in the E&C Onshore. I think that the reason why there is a reasonable result this quarter is because there is nothing particular with reference to the old historic projects that penalized the results, which has happened also in 2016. So basically, this is something that, should nothing else come from the past, could be also an indication for the overall year in terms of margin. Second question was?



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**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Kaombo, Kaombo.

**Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

The second question was on Kaombo. Now on Kaombo, clearly, the project is at breakeven, has been reviewed at breakeven last year. And in the guidance for this year, it is assumed at breakeven. Obviously, when we are talking about breakeven, we are talking about operating level and there are taxes, et cetera. So basically, the project is draining cash.

**Maria-Laura Adurno** - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

So from that standpoint, the full year considers this guidance that you provided at the EBITDA level, does it still stand? I mean, is it inclusive of the fact that you have this cash drain from Kaombo?

**Giulio Bozzini** - *Saipem S.p.A. - Chief Financial and Strategy Officer*

Yes.

**Operator**

(Operator Instructions) Now we come to our next question, and we got David Farrell from Macquarie.

**David Richard Edward Farrell** - *Macquarie Research - Oil and Gas Research Analyst*

One question from me, it relates to your alliance with Aker Solutions, there's obviously been quite a bit of press speculation with regard to what happened to that subsea business. Do you have any contingency planned in case that business gets sold to someone that already has a vertically integrated offering? It would suggest that you could actually be kind of less the loan with a SURF offering but no SPS offering to the market, and it does seem as if the market's increasingly inclined to be going down the vertically integrated route.

**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Okay. As you well know, the alliance was set up in order to provide ourself the capability of offering integrated projects. The alliance has been built up on the basis of sort of reciprocal freedom of participating or not participating to bids. I think we made clear that in most of the cases, we have decided to participate through the alliance with Aker, which is quite good and is working quite well. But also in some other cases, we have devised and decided to go with other participants. Should the rumors you refer to is becoming a reality in terms of Aker being acquired, obviously, will depend on who's going to acquire it. Should that be (inaudible), this is the rumor which is commonly spread in the market, that should it be Halliburton, then, quite frankly, that will not necessarily create a limitation or a constraint for Aker to continue in the same -- along the same path. The final comment is, obviously, we are all participating to the bids coming in the integrated shape, obviously, with the aim of understanding how much this is going to become a normal approach taken by the oil company, while we certainly see a very obvious foreign dependence. And for national companies to follow the path, we see less obvious that the major oil company may decide to follow the same path. So at the moment, we are indeed participating to the best of our capabilities. We have a very good relationship with our partner. But we maintain a great attention on the evolution of the overall, I mean, the overall approach.



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### Operator

That will conclude today's Q&A session. I would like to turn the call back to Stefano Cao for any additional or closing remarks.

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**Stefano Cao** - *Saipem S.p.A. - CEO and Non Independent Director*

Okay. Thank you very much for your participation, and I look forward to talk to you next quarter. Thank you very much.

### Operator

That will conclude today's conference call. Thank you again for your participation, ladies and gentlemen. You may now disconnect.

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