INTESA SANPAOLO

Credit

Company Note

Saipem

9 August 2021: 17:45 CET
Date and time of production

Weak 2Q21 Driven by Operational Issues

Saipem's 2Q21 results were weak with the company hit by operational issues relating to a wind farm project in the North Sea and the suspension of the Mozambique project. Saipem is guiding for a return to positive adjusted EBITDA in 2H21 and higher net debt at YE21. We see the outlook remaining challenging in 2H21 and maintain our Negative Credit View and SELL Recommendation on the bonds.

Saipem - Investment recommendations

	Sen Secured	Chg	Sen Unsec	Chg	Sub	Chg	Hybrid	Chg
Investment Grade	-	-	-	-	-	-	-	-
High Yield	-	-	SELL	c	-	-	-	-
Unrated	-	-	-	-	-	-	-	-

Note: c = confirmed; d= downgraded; u = upgraded; n = new; NA = not assigned; na = no action; U/R = under review. Source: Intesa Sanpaolo Research

Credit View, NEGATIVE

Saipem's 2Q21 results were weak and notably below consensus estimates (Bloomberg), with the group reporting a notable EBITDA loss for the period. Despite this, the group managed to preserve cash, with net debt slightly lower than 1Q21 thanks entirely to positive working capital effects. Operational issues such as the suspension of the LNG project in Mozambique and issues with a wind farm project in the North Sea were key drivers of the weak performance. Guidance points to higher net debt at YE21 and a return to positive EBITDA in 2H21, although we take the view that the outlook remains challenging. We maintain our Negative Credit View.

Investment Recommendation. SELL

We maintain our SELL Recommendation on Saipem's bonds as we take the view that Saipem's bonds could underperform in relative value terms.

Credit View

NEGATIVE

Italy/Oil Equipment & Services

Key Results

EUR M	2Q20	2Q21
Sales	1,503	1,582
EBITDA	31	-462
Margin (%)	2.1	-29.2
	31.3.21	**30.6.21**
Net debt	1,448	1,397
Leverage (x)	5.5	NA

Source: Intesa Sanpaolo research elaborations on company data

Credit Ratings

	Rating	Outlook
Moody's	Ba2	Negative
Fitch	-	-

Source: Bloomberg data

Report priced at market close on day prior to the issue (except where otherwise indicated).

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See page 14 for full disclosure and analyst certification

9 August 2021: 17:50 CET
Date and time of first circulation

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Credit View

Although sales were higher yoy in 2Q21, EBITDA turned materially negative, with figures missing Bloomberg consensus estimates. E&C offshore was the main driver of the EBITDA hit, although E&C onshore also contributed. The sharp deterioration was heavily influenced by specific operational issues, which included issues with an offshore wind farm in the North Sea, as well as the suspension of the LNG onshore project in Mozambique. The company also referred to the continuing effects of the Covid-19 health crisis on its activities. While core cash generation was negative, net debt was slightly lower than 1Q21 and the group managed to conserve cash, but this was entirely driven by materially positive working capital effects.

Saipem stated that it will be in contact with its bankers regarding the covenant on its facilities (tested at YE). We note the group is guiding for net debt of about EUR 1.6Bn for YE21, with a return to positive adjusted EBITDA in 2H21. At EUR 1.6Bn net debt, this implies at least EUR 457M of EBITDA would likely be required for FY21 (on our estimates) to avoid a covenant breach. This looks highly challenging to us given the adjusted EBITDA loss of EUR 266M at 1H21 and the reported EBITDA loss of EUR 389M. Any covenant breach could also have implications for the (currently fully available) EUR 1Bn RCF, and therefore for back-up liquidity and refinancing risk. The latter is also conditioned by the extent of available liquidity after accounting for the EUR 1.4Bn of restricted cash locked up in projects and subject to currency conditions. We do not, however, anticipate any significant issues with regard to a temporary waiver of the covenant at this point in time, particularly given the size of the current backlog. At 1H21 the backlog represented a high EUR 23.6Bn (or EUR 26.2Bn including the non-consolidated backlog), which provides reasonable visibility going forward, with EUR 4.025Bn due in 2H21 at present.

We expect 2H21 to continue to be dogged by Covid.19- related issues and uncertainty over the investment environment for the sector, as well as the issues pertaining to the Mozambique and North Sea wind farm projects. However, there is potential for a recovery to feed through from next year, in our view. We also note that the group stated that the current positive signals for (economic) recovery have only partially translated into a recovery of investments in the oil and gas sectors due to the conservative strategies of operators in the sector, which is being driven by both a desire to maintain financial solidity, as well as attempts to diversify their investment portfolios in order to respond to the growing market pressure in terms of the energy transition and CO_2 emissions reductions. In this respect we note Saipem's still heavy reliance on traditional segments of the industry, with the backlog composition at 1H21 represented by gas (67%), downstream oil (18%), upstream oil (4%), infrastructure and other non-oil (6%) and with renewables and green representing 5% of the backlog.

We maintain our Negative Credit View for the time being and our SELL Recommendation on the bonds.

Market Focus

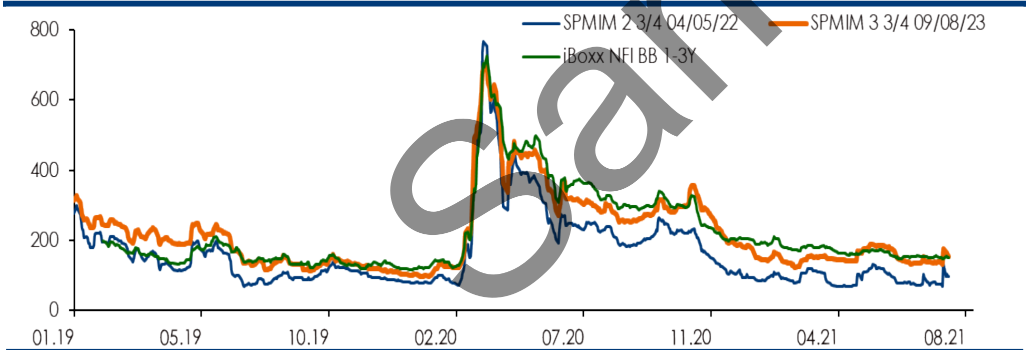
Saipem's ASWs widened materially across the board on publication of the 1H21 results, but particularly at the shorter end of the curve. ASWs have since retraced some of the lost ground. YTD the shorter-end of the curve is tighter, but wider at the longer end of the curve. With the exception of the 2022 bond, the bonds have underperformed the iBoxx NFI BB indices across the relative curves.

Saipem Finance International BV bonds/CDS (ASW, bps)

Bond	Next call and price	Type	Outst. EUR M	Price	YTM %	SPRD TYPE	SPRD	-1W (bps)	-1M (bps)	YTD (bps)	52-week range		Ratings		
							6.8.21			4.1.21	max	min	Mdy	Fitch	BBG
Saipem Finance International BV															
SPMIM 2 3/4 04/05/22	-	FX	500	101.5	0.4	ASW	94	-38	18	-2	264	68	Ba2	-	BB
SPMIM 3 3/4 09/08/23	-	FX	500	105.6	1.0	ASW	155	-22	18	-23	356	123	Ba2	-	BB
SPMIM 2 5/8 01/07/25	-	FX	500	103.1	1.7	ASW	214	-24	23	-2	409	179	Ba2	-	BB
SPMIM 3 3/8 07/15/26	04/26 100.0	FX	500	102.8	2.8	ASW	313	-14	31	27	453	246	Ba2	-	BB
SPMIM 3 1/8 03/31/28[1]	12/27 100.0	FX	500	101.3	2.9	ASW	319	-10	23	3	329	279	Ba2	-	BB
							5.8.21								
Saipem Finance International BV CDS 5Y							347	-11	19	56	485	233			
Saipem Finance International BV CDS 10Y							418	-15	10	60	562	315			

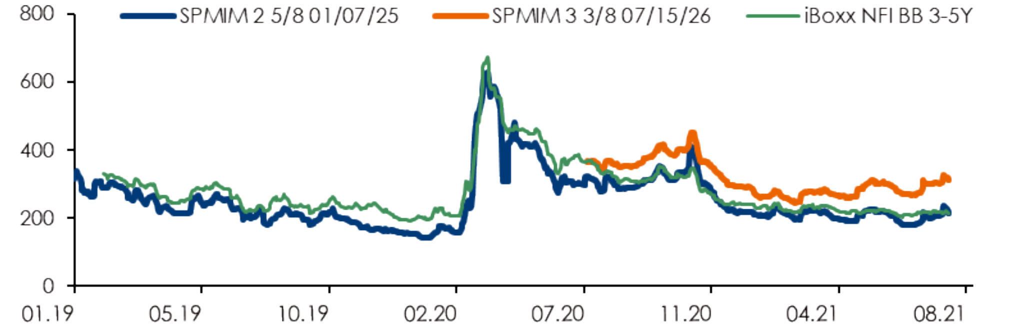
Type: FX = Fixed; FL=Floating; VR = Variable; FT = Flat Trading. YTM: yield to maturity or yield to call for callable bonds. SPRD TYPE: ASW=Asset Swap. Ratings: reported in the table refer to individual issues. Notes: 1) YTD from launch date for bonds issued in 2021. Source: Intesa Sanpaolo Research elaboration on Bloomberg data at 09:39.

Saipem Bonds ASW vs. iBoxx NFI BB 1-3Y



Source: Intesa Sanpaolo elaboration on Bloomberg data

Saipem Bonds ASW vs. iBoxx NFI BB 3-5Y



Source: Intesa Sanpaolo elaboration on Bloomberg data

Saipem Bonds ASW vs. iBoxx NFI 5-7Y

Source: Intesa Sanpaolo elaboration on Bloomberg data

We have closed our outright position on the 2023 bond which has not performed in line with our expectations (-32.9bps).

Investment Recommendation on Saipem's bonds

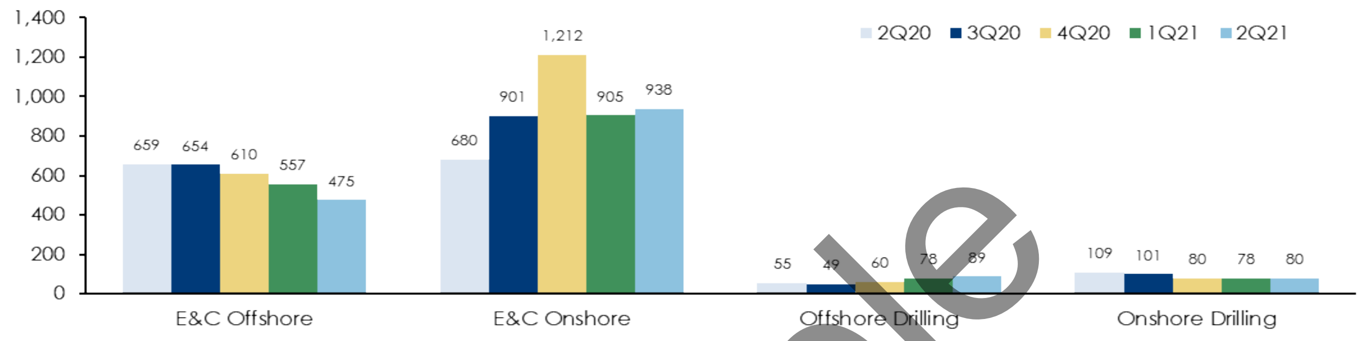
Date	Bond/CDS	Type	Sprd	Rate	Buy/ Sell	Entry level (bps)	Current level[1] (bps)	Pick-up (pbs)	Status
14.5.21	SPMIM 3 3/4 9/8/23	Sen	ASW	FX	SELL	188.6	155.7	-32.9	CLOSED 05.08.21

Source: Intesasanpaolo elaboration on Bloomberg Data at 13:00

Financial Review

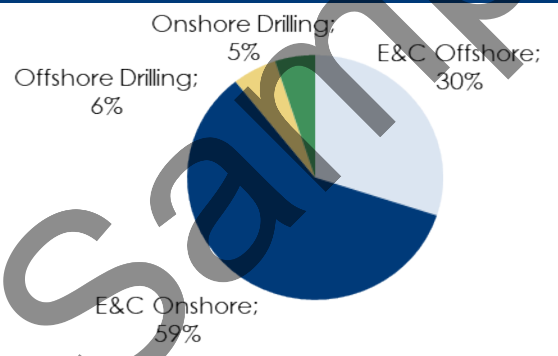
Sales were 5.3% higher yoy, at EUR 1.58Bn, which mainly reflected growth in E&C onshore (+38% yoy to EUR 938M) and, to a lesser extent, offshore drilling (+62% yoy to EUR 34M), although E&C offshore saw a sharp contraction (-28% yoy to EUR 475M) with onshore drilling declining 27% yoy to EUR 80M. The mix thus swung further to E&C onshore.

Sales Development by Quarter (EUR, M)



Source: Company data and Intesa Sanpaolo Research

1H21 Revenue Mix

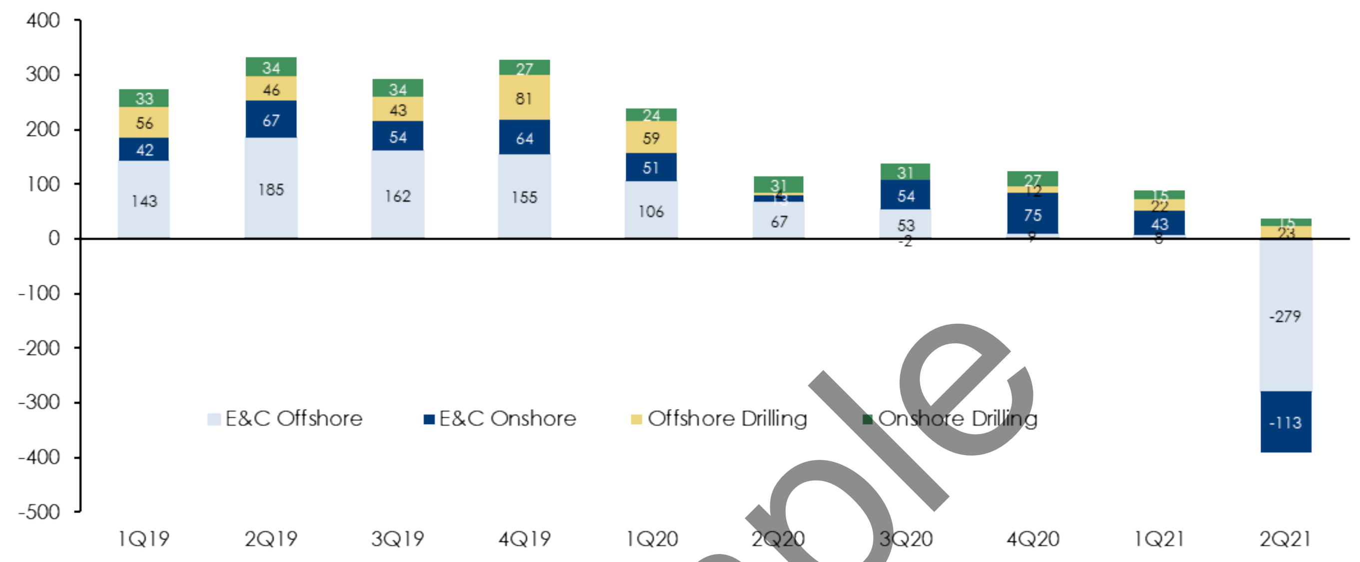


Source: Company data and Intesa Sanpaolo Research

EBITDA turned materially negative (for EUR 462M in 2Q21 compared to the positive EUR 31M at 2Q20) with the EBITDA margin sharply negative (-29% vs. +2.1% in 2Q20) reflecting a significant (+50% yoy) hike in costs yoy. Adjusted EBITDA also saw a similar yoy deterioration (-EUR 354M vs +EUR 115M in 2Q20). Only the onshore and offshore Drilling activities were EBITDA positive in 2Q21, with both E&C onshore and E&C offshore reporting sharply negative EBITDA in the quarter (-EUR 279M and -EUR 113M, respectively). The adjusted EBITDA margin was negative for 22%, dragged down by the sharply negative margins in E&C offshore (-59%) and E&C onshore (-12%) in 2Q21.

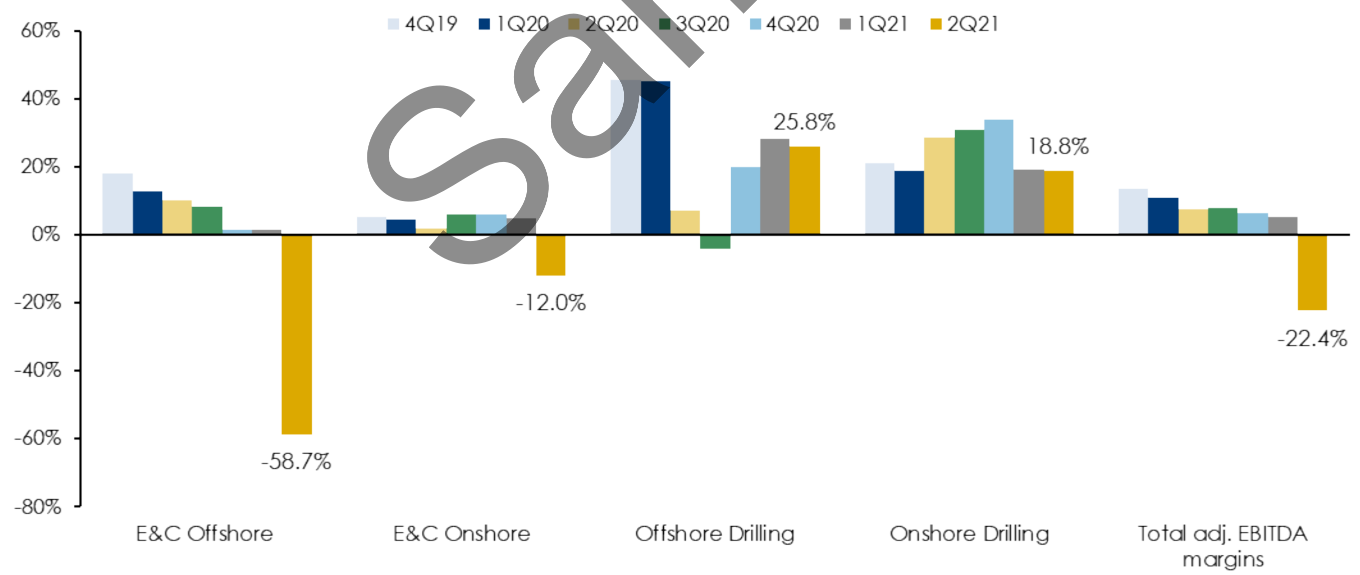
For 1H21 as a whole, the group noted that the weakness in E&C offshore derived from lower volumes in E&C offshore in the Middle East and North Africa, partially offset by Europe and the Americas. The division was also impacted by issues at a specific wind farm project and by fabrication bottlenecks in the Far East due to the pandemic, and the low volumes and high operating leverage which amplified the EBITDA loss. With regards to E&C onshore, revenue growth in Sub-Saharan Africa more than offset lower volumes in the Middle East, but margins were affected by the suspension of the Mozambique project and extra costs in the Middle East.

Adjusted EBITDA Development by Quarter and Business Unit



Source: Company data and Intesa Sanpaolo Research

Adjusted EBITDA Margin Development by Quarter and Business Segment



Source: Company data and Intesa Sanpaolo Research

The EBIT loss was 10% wider yoy for 2Q21 at EUR 589M (-37% of sales), the EBT loss 14% wider yoy at -EUR 629M, and the net loss 9% wider at -EUR 659M. We also note equity losses (EUR 25M in 2Q21) from JV projects.

Core cash generation was weak in 2Q21, with FFO negative at -EUR 269M (17% of sales), but cash flow was aided by material positive working capital cash effects (EUR 402M), leaving CFO at EUR 133M (8.4% of sales), which covered lower yoy capex (-50% yoy to EUR 68M). Working capital cash effects thus helped preserve cash and permitted a EUR 51M reduction in net debt to EUR 1.4Bn. With 1H21 LTM EBITDA negative for EUR 232M and LTM FFO at -EUR 162, leverage ratios are relatively meaningless, although we note that the net debt/equity ratio increased to 0.6x, from 0.5x at 1Q21, and net debt/CFO increased from 1.9x at 2Q20 to 5.1x at 2Q21.

Short Form Cash Flow

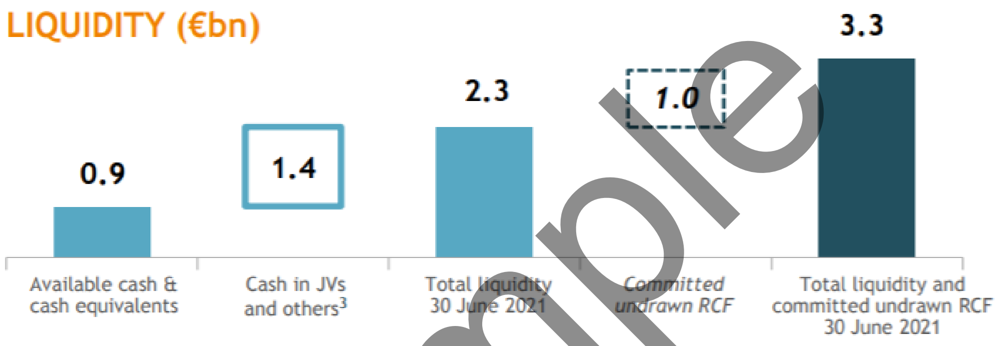
(EUR, M)	2Q20	% sales	1Q21	% sales	2Q21	% sales	1H20	% sales	1H21	% sales
Net profit loss	-616		-120		-659		-885		-779	
Non-controlling interests	13						15			
D&A and other non-monetary items	587		99		390		1,008		489	
FFO	**-16**	**-1.1%**	**-21**	**-1.3%**	**-269**	**-17.0%**	**138**	**3.8%**	**-290**	**-9.1%**
Working capital	-68		-98		402		-274		304	
Saipem CFO	**-84**	**-5.6%**	**-119**	**-7.4%**	**133**	**8.4%**	**-136**	**-3.7%**	**14**	**0.4%**
Capex	-136	9.0%	-67	4.1%	-68	4.3%	-195		-135	4.2%
FCF	**-220**	**-14.6%**	**-186**	**-11.5%**	**65**	**4.1%**	**-331**		**-121**	**-3.8%**
Investments in equity, consolidated subs.	0									
Disposals	1		2				1		2	
Saipem FCF	-219	-14.6%	-184	-11.4%	65	4.1%	-330		-119	-3.7%
Treasury shares	0						-16			
Share capital	0									
Capital and reserves	-10		-26				-10		-26	
Repayment of lease liabilities	-44		-21		-64		-78		-85	
Forex	4		2		-1		5		1	
Change in net debt before lease liabilities	-269		-229		0		-429		-229	
Change in lease liabilities	131		7		51		151		58	
Change in net debt	-138		-222		51		-278		-171	
Starting net debt	1,222		1,226		1,448		1,082		1,226	
End net debt	1,360		1,448		1,397		1,360		1,397	

Source: Company data and Intesa Sanpaolo Research

However, net debt of EUR 1.4Bn incorporates the positive impact of restricted liquidity. Saipem reported gross debt of EUR 3.4Bn and total liquidity of EUR 2.3Bn, leaving net debt at EUR 1.4Bn (or EUR 1.1Bn before accounting for the IFRS 16 impact). However, available liquidity was EUR 0.9Bn, with EUR 1.4Bn in restricted cash (mainly related to projects and local currencies). Adjusted net debt (stripping out restricted liquidity) is therefore higher at about EUR 2.8Bn. Moreover, credit facilities contain a leverage covenant of 3.5x (tested at YE21), with clear implications for the RCF should this not be satisfied at YE21. Saipem stated in the conference call it is approaching its banks with regards to the covenant.

Net Debt and Restricted Liquidity

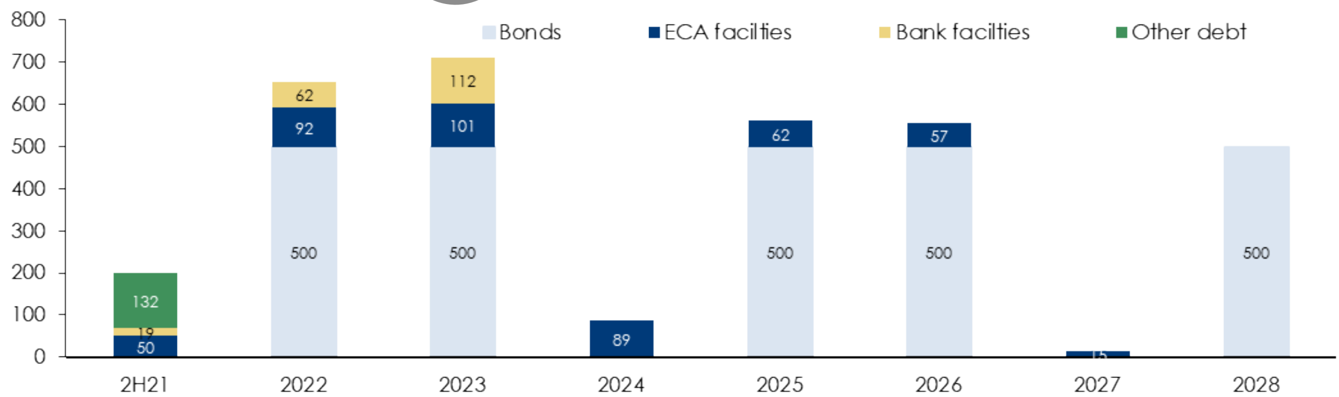
€ billion	1H 21
Gross Debt[1]	3.4
(Total liquidity)	(2.3)
Net Debt (pre IFRS 16)	**1.1**
IFRS 16	0.3
Net Debt (post IFRS 16)	**1.4**



Source: Company data and Intesa Sanpaolo Research (3) restricted liquidity mainly related to projects and local currencies

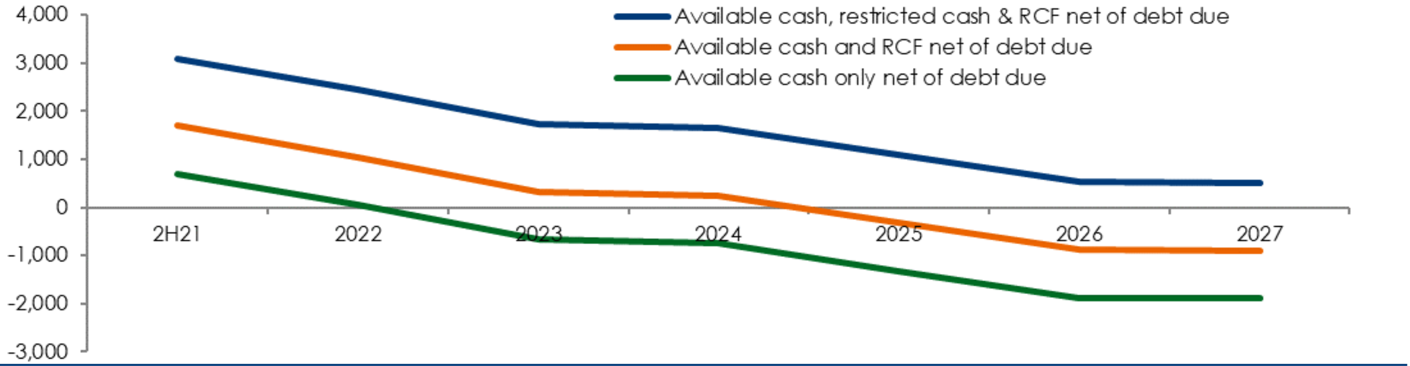
While the spate of issues over the last year has served to extend the average tenor, the company's refinancing risk is increasing given the pressure on cash flows. Consequently, while refinancing pressure (including the restricted cash and back-up liquidity in the RCF) appears negligible, adjusted for restricted cash, refinancing pressure emerges in 2025 on current data, while if stripping out the RCF, material refinancing pressure emerges in 2023.

Debt Maturity Profile (EUR, M)



Source: Company data and Intesa Sanpaolo Research

Refinancing Risk – Available Cash, Restricted Cash and the RCF

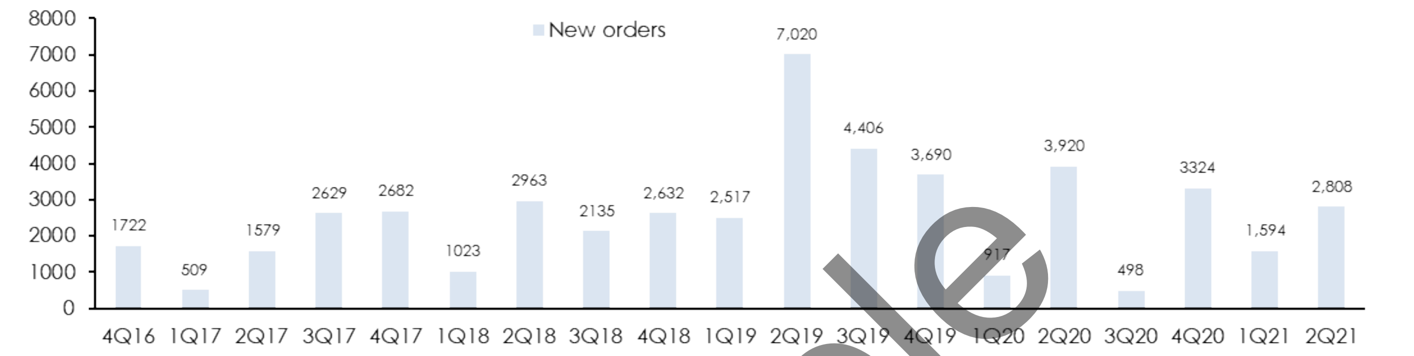


Source: Company data and Intesa Sanpaolo Research

New Orders and the Backlog Development

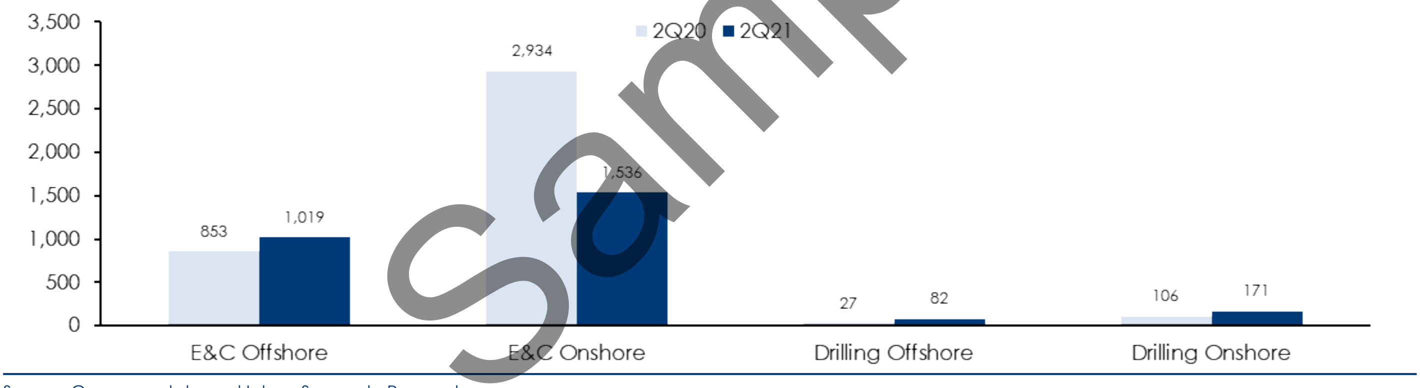
New orders were 28% lower yoy in 2Q21 at EUR 2.8Bn but 9% lower yoy for the first half at EUR 4.4Bn. The lower new orders in 2Q21 were entirely attributable to the E&C onshore division, where new orders were down 49% yoy, while new orders picked up yoy for all other business units. Nevertheless, the book-to-bill ratio was 1.8x in 2Q21 (1.4x in 1H21).

New Order Development by Quarter



Source: Company data and Intesa Sanpaolo Research

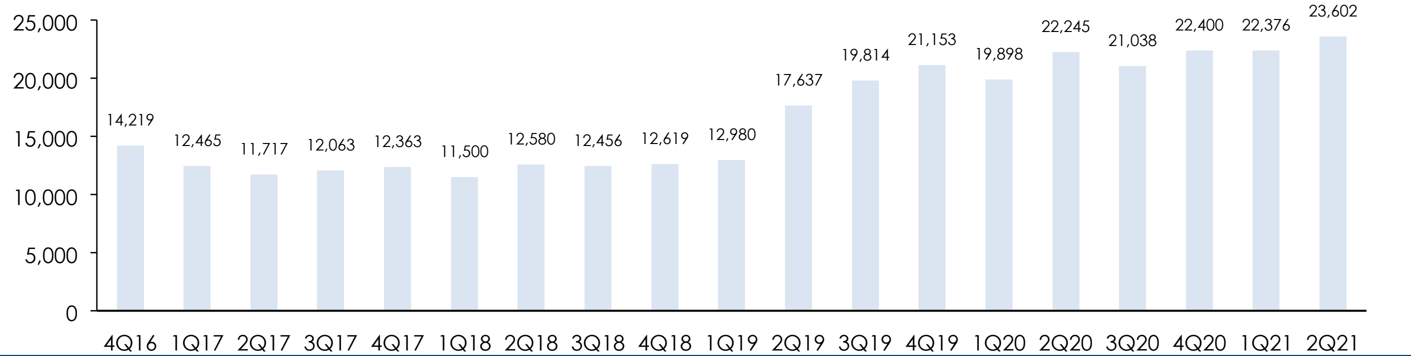
New Order Development yoy by Business Unit



Source: Company data and Intesa Sanpaolo Research

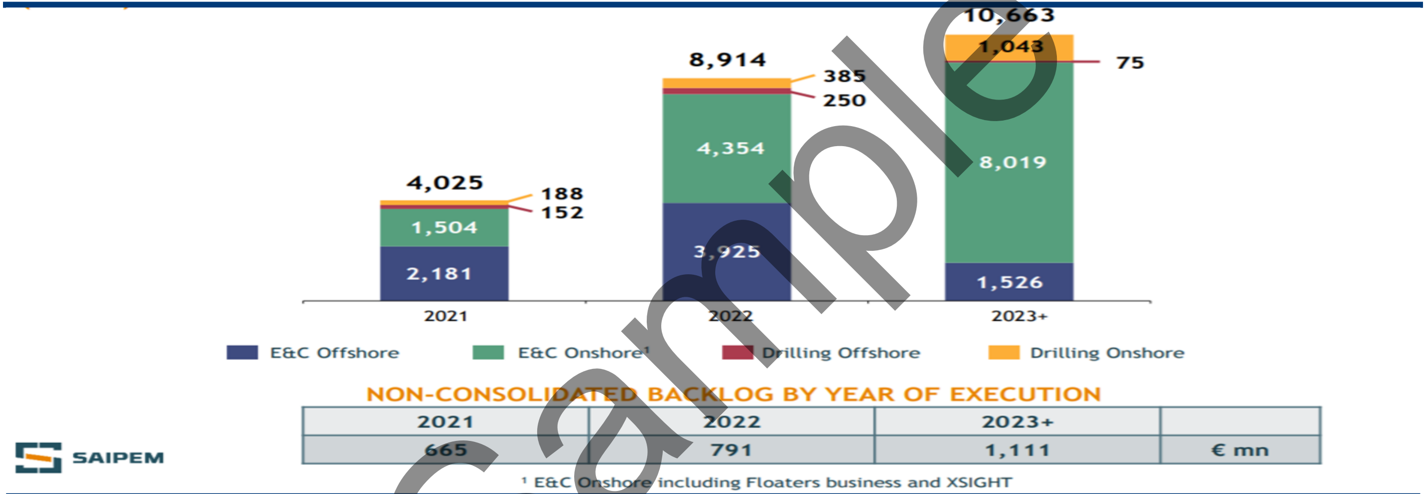
The backlog increased further in 2Q21 to a high 23.6Bn (or EUR 26.2Bn including the non-consolidated backlog). The 2H21 backlog run-off was EUR 4Bn, which would provide a minimum revenue base for 2021 of EUR 7.2Bn. The current distribution of the backlog suggests a EUR 8.9Bn run-off in 2022, compared to current consensus estimates for revenues of EUR 9.2Bn for 2022 (Bloomberg), and with EUR 10.7Bn relating to 2023 onwards.

Backlog Development by Quarter (EUR, M)



Source: Company data and Intesa Sanpaolo Research

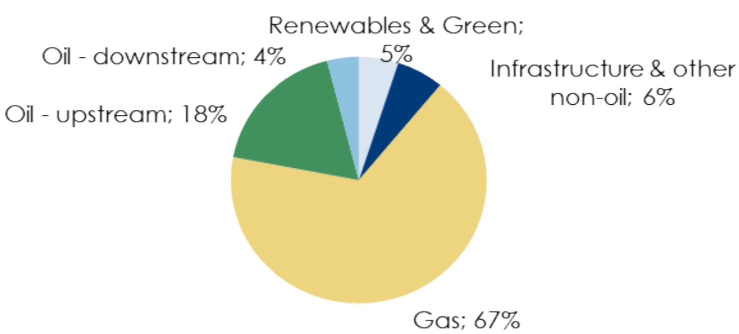
Yearly Distribution of the Backlog



Source: Company data and Intesa Sanpaolo Research

Despite the group's increasing focus on the energy transition and a reduced reliance on the traditional oil sector, we note that the group still remains heavily reliant on the gas sector, which represents 67% of the backlog, with renewables and green representing 5%, and infrastructure and other non-oil representing 6%.

Backlog Composition by Segment



Source: Company data and Intesa Sanpaolo Research

Outlook – Challenging Times and Project Issues

The business environment is still conditioned by the pandemic and characterized by certain project delays and cost overruns according to the company, with an impact on project acquisitions and with direct costs weighing on financials.

The group stated that the Mozambique project (issues were flagged in 1Q21) was suspended, with discussions ongoing on options to preserve the value of the site. The residual backlog for this project was stated to be c. EUR 3.6Bn in 2021, excluding any potential contribution from reimbursements of suspension and security risk costs. In 2H21 the revenue contribution from this project is thus expected to be related to reimbursements. In addition, Saipem announced that it also had execution problems with a specific offshore wind project that had encountered technical issues due to challenging soil conditions, which led to a project reassessment.

However, management argued that there were early signs of a recovery in drilling (in fact, onshore drilling utilisation rates rose from 36% in 1Q21 to 45% for 1H21), although these activities make modest contributions to revenues and EBITDA overall. Management also underscored the growing demand for the energy transition and renewables, which represented 14% of the tendering pipeline ahead (although a more modest 5% of the backlog at 1H21), and also made mention of possibilities from Italy's National Recovery and Resilience Plan, with planned investment in advanced infrastructure.

The group launched a strategic review of all business units to define a new plan to be presented in the autumn, as well as launching a programme to reduce operating leverage though a streamlining of operations and processes.

Updated guidance pointed to 2H21 revenues of between EUR 4.5-5Bn, which would put 2021 revenues at between EUR 7.7-8.2Bn, with adjusted EBITDA turning positive, capex of EUR 200-300M and net debt at EUR 1.6Bn (thus up c. EUR 200M on 1H21).

Outlook 2H21

Metrics	2H 2021
Revenue	€4.5-5bn
CAPEX	€200-300mn
Adjusted EBITDA	Back to positive
Net debt	~€1.6bn

Source: Company data and Intesa Sanpaolo Research

The outlook does not factor in a further and possible material macro and business deterioration.

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Credit Research Publications in Last 12M

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https://group.intesasanpaolo.com/en/research/RegulatoryDisclosures/archive-of-intesa-sanpaolo-group-s-conflicts-of-interest0

Valuation methodology

Intesa Sanpaolo's credit views are based on the expected trend of the company's fundamentals. The view reflects the sector trend and the competitive scenario, the company's financial strength, as well as its profitability outlook and competitive positioning. In our credit quality valuation, we consider management's intention and ability to meet debt obligations, the company's dividend policy and, in general, its attention to bondholders' interests. Among key financial ratios, for those sectors where relevant, we assess the company's ability to generate operating cash flow, its capacity to repay maturing debt through cash flow, its net interest coverage ratio and capital ratios.

In the case of significant events, which could determine a change in our credit view, we may place our recommendation under review. This review does not necessarily imply a change in the credit view.

Corporate credit view key

Credit rating key

Credit view	Definition
POSITIVE	We expect an improvement in fundamentals over the next six months
NEUTRAL	We expect substantially stable fundamentals over the next six months
NEGATIVE	We expect a deterioration in fundamentals or visibility on fundamentals over the next six months
SUSPENDED	The credit view and investment recommendation for this company have been suspended as there is not a sufficient fundament The previous credit view, if any, is no longer in effect for this company
NOT ASSIGNED	The company is or may be covered by the Research Department but no credit view and investment recommendation are c applicable regulations and/or firm policies in certain circumstances.

Historical Credit View and Investment Recommendation Changes

Saipem - Historical Credit View (-1Y)

Date	Credit View
14-Oct-20	NEGATIVE

Saipem - Historical Investment Recommendations (-1Y)

Date	High Yield Senior Unsecured
14-May-21	SELL

Credit View allocations

Intesa Sanpaolo Research Credit View distribution at July 2021

Number of Companies subject to credit views: 29*	Positive	Neutral	Negative
Total Credit Research coverage - last credit view** (%)	6.9	86.2	6.9
of which Intesa Sanpaolo's clients*** (%)	100	80	50

* Total number of companies covered is 33; **Last credit view refers to credit view as at end of the previous quarter; ***Companies on behalf of whom Intesa Sanpaolo and the other companies of the Intesa Sanpaolo Group have provided corporate and investment banking services in the last 12 months; percentage of clients in each rating category.

Investment recommendations

Intesa Sanpaolo's recommendations on the issuer(s) bonds or relative CDS are based on the following rating system:

Investment recommendation

Recommendation	Definition
BUY	We expect the bond or CDS subject to the recommendation to outperform the reference index, sector or benchmark in a period up to six months
HOLD	We expect the bond or CDS subject to the recommendation to perform in line with the reference index, sector or benchmark in a period up to six months
SELL	We expect the bond or CDS subject to the recommendation to underperform the reference index, sector or benchmark in a period up to six months

Company-specific disclosures

Intesa Sanpaolo S.p.A. and the other companies belonging to the Intesa Sanpaolo Banking Group (hereafter the "Intesa Sanpaolo Banking Group") have adopted written guidelines "Organisational, Management and Control Model" pursuant to Legislative Decree 8 June 2001 no. 231 (available at the Intesa Sanpaolo website, https://group.intesasanpaolo.com/en/governance/leg-decree-231-2001) setting forth practices and procedures, in accordance with applicable regulations by the competent Italian authorities and best international practice, including those known as Information Barriers, to restrict the flow of information, namely inside and/or confidential information, to prevent the misuse of such information and to prevent any conflicts of interest arising from the many activities of the Intesa Sanpaolo Banking Group, which may adversely affect the interests of the customer in accordance with current regulations.

In particular, the description of the measures taken to manage interest and conflicts of interest – related to Articles 5 and 6 of the Commission Delegated Regulation (EU) 2016/958 of 9 March 2016 supplementing Regulation (EU) No. 596/2014 of the European Parliament and of the Council with regard to regulatory technical standards for the technical arrangements for objective presentation of investment recommendations or other information recommending or suggesting an investment strategy and for disclosure of particular interests or indications of conflicts of interest as subsequently amended and supplemented, the FINRA Rule 2241, as well as the Financial Conduct Authority Conduct of Business Sourcebook rules COBS 12.4 - between the Intesa Sanpaolo Banking Group and issuers of financial instruments, and their group companies, and referred to in research products produced by analysts at Intesa Sanpaolo S.p.A. is available in the "Rules for Research " and in the extract of the "Corporate model on the management of inside information and conflicts of interest" published on the website of Intesa Sanpaolo S.p.A.

At the Intesa Sanpaolo website, webpage https://group.intesasanpaolo.com/en/research/RegulatoryDisclosures/archive-of-intesa-sanpaolo-group-s-conflicts-of-interest you can find the archive of disclosure of interests or conflicts of interest of the Intesa Sanpaolo Banking Group in compliance with the applicable laws and regulations.

Furthermore, we disclose the following information on the Intesa Sanpaolo Banking Group's conflicts of interest.

- One or more of the companies of the Intesa Sanpaolo Banking Group plan to solicit investment banking business or intends to seek compensation from Saipem Finance International BV in the next three months
- One or more of the companies of the Intesa Sanpaolo Banking Group have granted significant financing to Saipem Finance International BV and its parent and group companies
- One or more of the companies of the Intesa Sanpaolo Banking Group have been lead manager or co-lead manager over the previous 12 months of any publicly disclosed offer of financial instruments of Saipem Finance International BV
- One or more of the companies of the Intesa Sanpaolo Banking Group provide/have provided investment banking services to and/or concerning Saipem Finance International BV in the last twelve months
- One or more of the companies of the Intesa Sanpaolo Banking Group plan to solicit investment banking business or intends to seek compensation from Saipem in the next three months
- One or more of the companies of the Intesa Sanpaolo Banking Group have granted significant financing to Saipem and its parent and group companies
- One or more of the companies of the Intesa Sanpaolo Banking Group have issued financial instruments linked to Saipem

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