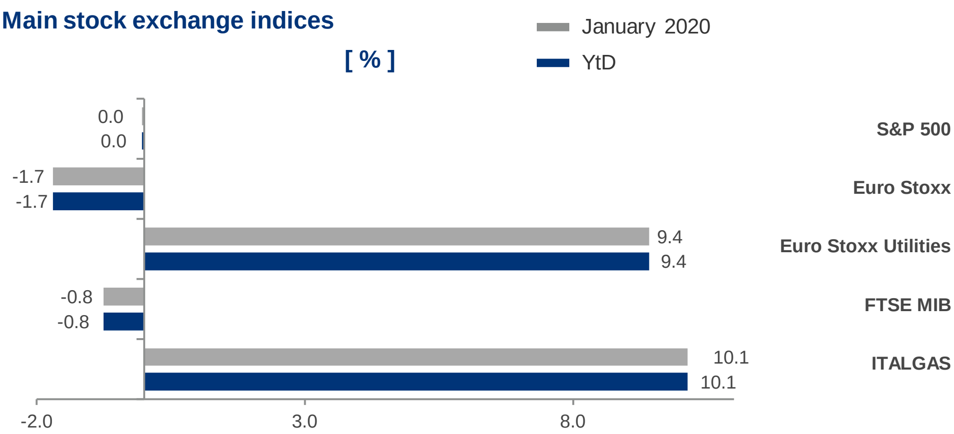
January 2020

Financial Markets Review

After reaching new highs in the period, the eurozone equity retreated on fears of spreading coronavirus. Core yields down sharply with risk-off; spreads keep contracting with election results

Financial Markets

The European market indexes declined in Janaury, on the back of exponential growth of coronavirus contagions in China. The drop also reflected some profit taking after the indexes touched 12 years highs in December led by the risk-on phase which reflected the finalization of the US / China trade agreement and the conservatives winning the early UK elections, opening the doors to Brexit by January and avoiding nationalization risks, as well as de-escalation of geopolitical tensions following the US attack on Iranian targets.
The Euro Stoxx and the FTSE Mib closed down between 1% and 2%, in moderate underperformance vs S&P500 (unchanged, at historical highs) reflecting fears that the US administration could again consider restrictive measures against European imports, in particular motor vehicles (among worst performers) if European governments had not supported the US in introducing new sanctions against Iran. After moving back in line with the previous historical lows of 07/2016 and adjusted by the maturity benchmark extension, the Bund yield decreased by 29 bps to -0.44%



Source: Italgas elaboration on Bloomberg data

(vs -41 bps for the UST at 1.51%) reflecting fears of spreading virus. The spread between 3m and 10 yrs US yields turned negative, a clear sign of economic slowdown fears. Adjusted for the aforementioned change in benchmark maturity for the Bund, the BTP-Bund spread fell 19 bps to 137 bps as a result of the regional elections in Emilia Romagna, which reduced the risks of government crisis.

EUR / USD -1.1% at 1.11 due to the inverse relationship between the dollar and oil prices and expectations of an upward revision of the ECB inflation target to allow more space in terms of accommodative monetary policies. EUR / GBP -0.7% at 0.84 based on the ECB expectations, better than expected UK macro data and BoE unexpected decision to leave the reference rate unchanged at 0.75%.

The oil market

After reaching new highs since April in view of the output cuts made by OPEC + and despite the ongoing production interruptions in Libya caused by the civil conflict, crude oil prices fell by 15% (Brent to 56 USD / b). This was due to fears of the virus spreading, which could lead to to reduction in global mobility, as well as IEA estimating excess world supply of 1 mbd in H1 2020, and Kuwait announcing the restart of a 0.5 mbd capacity oil field stopped for almost 5 years due to legal dispute with Saudi Arabia. The dynamic was mitigated by the intention by OPEC + to convene an extraordinary meeting in February to launch further 0.5 mbd production cuts to compensate for the decline in demand.

Performance by sector

Sector dynamics favour defensives with risk-off; cyclicals worst performers

The risk-off phase that occurred in the final part of the month penalized cyclicals, with the automotive, oil&gas and mining-steel industries falling 8-10%. The auto sector, in particular, was negatively affected by (i) fears of possible introduction of new restrictive measures in the USA against European imports in case of lack of support of sanctions against Iran; and (ii) Daimler's results (-15%) below expectations. Also noteworthy was the 7% drop of the travel & leisure as a result of global mobility restrictions to combat virus expansion. On the opposite side, utilities and real estate outperformed due to their bond-proxy profile. Financial services were among the best performers on the back of M&A (acquisition by Amundi of Sabadell asset management) and fund inflows at the end of 2019.

Main sectors performance, January 2020

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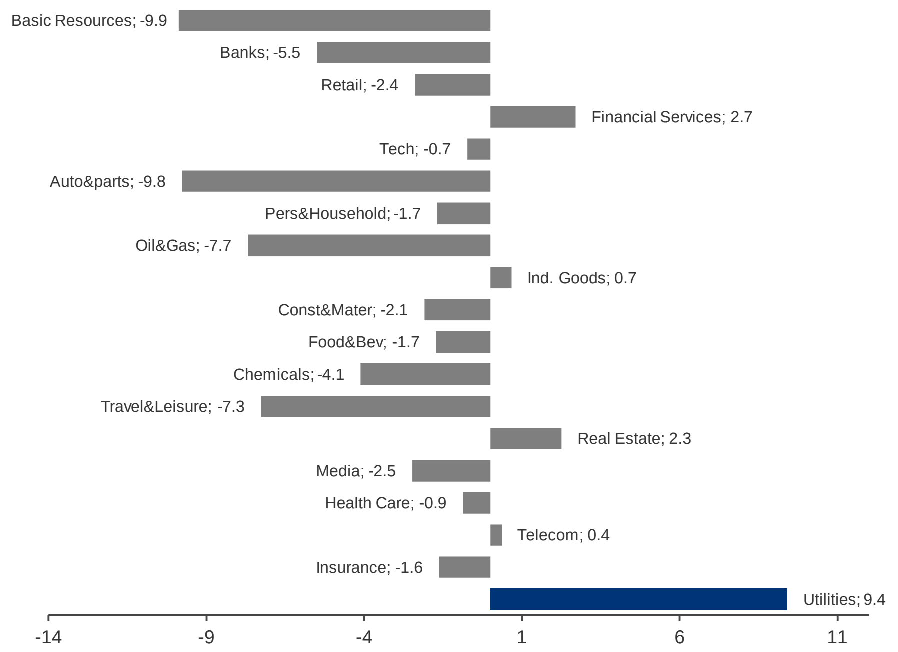

Source: Italgas elaboration on Bloomberg data

Utilities best performers thanks to their defensive profile and EU decarbonisation plan

Utilities sector performance

The utilities sector (+ 9%) was by far the best performer. The contraction in core yields was supportive. The sector was also led by electricity producers with exposure to renewables, on the back of EU Parliament approval of 1 tn euro investment plan to support the complete decarbonisation by 2050 (intermediate target for the reduction of CO_2 emissions by 2030 increased from 40% to 55%). Better than expected outcome of the coal phase-out helped German operators (RWE + 15%). Veolia and Suez were also among the best performers (up respectively 13% and 10%) supported by growing attention to water and environmental issues, and upgrades by some brokers.

January 2020 – Trend of the sector and subsectors

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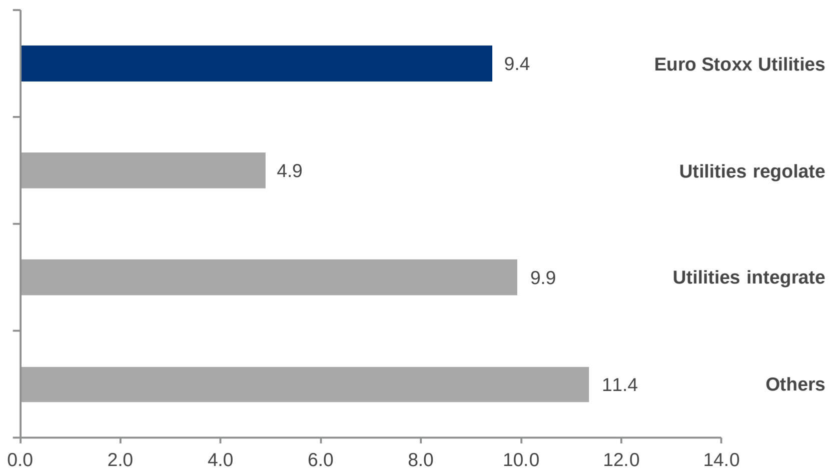
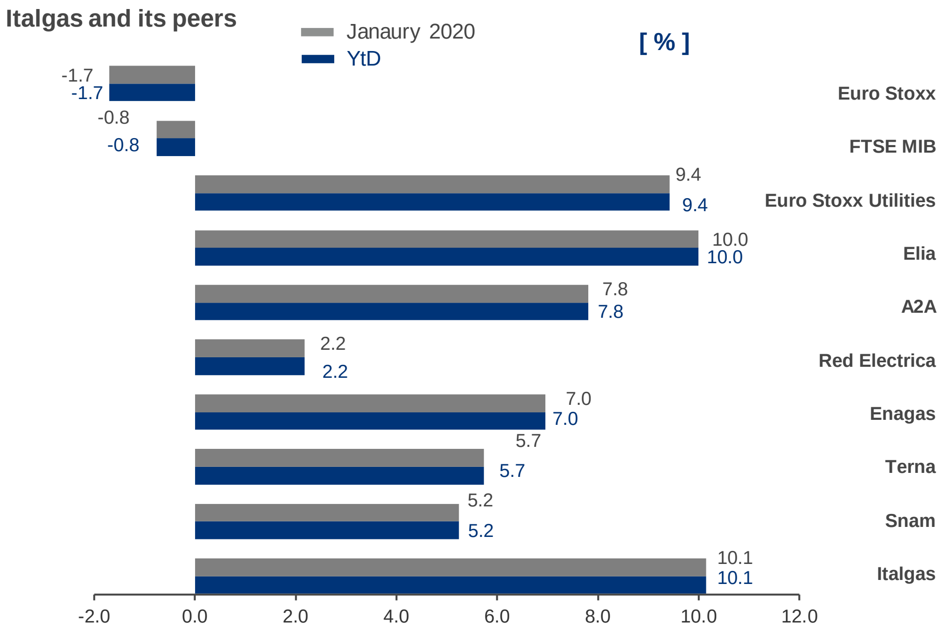


Source: Italgas elaboration on Bloomberg data

Italgas and its peers

Italgas (+ 10%) best performer recovering the H2 2019 drop as prices already anticipated the tariff review outcome

Strong rebound for Italgas (+ 10% to 5,996 euros). Alongside Elia, Italgas was the best performer in the sector in the month. Supported by the decrease in core yields and spreads, as well as by the upgrades by BofA and Kepler-Cheuvreux, Italgas partially recovered the underperformance accrued in the second half of 2019 as the share price was already anticipating an overall negative outcome from the regulatory review (resolution 570 / 19). The Belgian TSO Elia reached new highs, supported by the contraction in core yields, the extended regulatory visibility, with the electricity transmission tariff periods defined until 2023 in Belgium and Germany. It should be noted that all peers moved up in January.



Source: Italgas elaboration on Bloomberg data

Agenda

Corporate events

11 March	Board meeting Q4/FY; dividend proposal 2019
11 March	Press release and conference call

Corporate News

Italgas is awarded the "Valle D'Aosta" district

The Aosta contracting station has officially awarded Italgas the tender for the management of the natural gas distribution service in the “Valle d'Aosta” district for the next 12 years. The area consists of 20K end users and a RAB of over 40 mn euros. In the offer presented, Italgas has planned investments of approximately 100 mn euro, that will generate a strong stimulus for the local economy, with positive fall out also in terms of employment. “After the Turin 2 Area - commented Italgas' CEO Paolo Gallo - we have further confirmation in a territory with strong and historical roots for Italgas such as the Aosta Valley. A result that testifies the goodness of the work carried out and that allows us not only to give continuity to the management of the service in the territory, but also to carry out the important investment programs planned to develop the service also in those areas not yet reached by natural gas”.

Italgas-A2A agreement finalized

On January 31st Italgas and A2A have concluded an agreement for the reciprocal transfer of some assets in order to strengthen their respective core businesses. The transaction, announced on 8 October 2019, was finalized following the occurrence of the conditions precedent provided for.
In particular, Italgas Reti (Italgas Group) sold to A2A Calore & Servizi (A2A Group) all the district heating activities currently managed in the municipality of Cologno Monzese (Milan); at the same time, Unareti (A2A Group) will sell to Italgas the natural gas distribution activities managed in seven municipalities in the ATEM Alessandria 4.

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