Ercros

ANNUAL REPORT 2018

Contents

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Bearing those cases in which the comprehension of the text requires so, all references contained in this document using the male gender will be deemed as indistinctly referring to all persons, men or women, in order to avoid reiteration of terms to facilitate the reading thereof.

1 Letter from the Chairman

Ladies and gentlemen,

In 2018 Ercros completed the transition process from mercury technology to membrane technology, just like many other European manufacturers of chlorine and caustic soda. It completed all aspects of the challenge and at the same time minimised the impact thereof in company operations. Furthermore, in this demanding situation the Company closed the year with a profit of EUR 45 million, which consolidates the historic record level achieved in the previous two years.

By way of a strategic company decision, it addressed the technology change in two stages: in 2018 the capacity to produce chlorine with membranes was 191,000 tonnes per year, and will reach a final level of 217,000 tonnes per year in the third quarter of 2019. Due to the enhanced service performance of the new technology, once final capacity is attained, production will be similar to how it was prior to the technology change.

In the meantime, in order to serve the market, Ercros replaced its minor in-house production with the marketing of external products. This enabled us to achieve sales of EUR 640 million, which is very similar to those of 2017.

Electricity remains expensive in Spain: its price has increased by 14% over the course of the year and remuneration for the interruptibility service was seven million lower than in the previous year. Fortunately, we now have a technology to produce chlorine and caustic soda much more efficiently in terms of energy use. Other important raw materials have also risen, such as methanol, the price of which increased by 13%.

Despite these difficulties, the low prices of primary products have allowed us to end the year with EUR 45 million profit. In the past three years, 2016, 2017 and 2018, Ercros' total profit has amounted to almost EUR 135 million. The profit per share, which is another way of looking at results and that also includes the effect of reduction of share capital, went from EUR 0.3958 in 2016 to EUR 0.4111 in 2018, a 4% improvement.

None of this can be achieved without significant investment effort. The 2016-2020 inversions "Act Plan" determined the initial path for this effort, particularly with respect to chlorine-caustic soda plants adapting to the use of membrane technology. This path has subsequently been supplemented by additional actions in other areas of the business, with the intention of increasing the production capacity of products with significant margins and improving the Company's energy efficiency. In total, between 2016 and 2020, Ercros will be investing around EUR 100 million.

Last year we recommitted to fulfilling the three established conditions in the shareholder remuneration policy whereby, during the shareholders meeting, the board agreed to propose a dividend distribution of EUR 0.06 per share, which increases that of 2017 by 20% and represents an outlay of 14.4% of Ercros' consolidated profit in 2018. Furthermore, throughout the year, the Company bought treasury shares to amortise and will continue to do so in 2019 until a value of EUR 11.5 million is reached in order to complete the maximum combined outlay expected in the shareholder remuneration policy for 2018, which is EUR 18 million, 40% of the profit made. In the past three years, once the remuneration as a 2018 expense has been met, Ercros will have paid out EUR 47 million to remunerate shareholders and, by the next meeting in June, will have reduced the number of its shares by around nine million.

During 2018 the board endorsed the update of the ethical code of conduct, the anti-corruption and crime prevention policy and the audit committee regulations. The audit committee, for its part, updated the ethical channel procedure and approved the procedure for conflicts of interest. As a consequence of updating the ethical code and ethical channel, the compliance committee, which reports to the audit committee, became responsible for managing the ethical channel and the guarantor to ensure the confidentiality of information transmitted through the same.

Ercros' board has a balanced gender representation. Women represent 40% of board members; 67% of supervision and control committees and 100% of independent board members. Therefore, Ercros exceeds the 30% target set in the 14th recommendation of the Good Governance Code *(Código de Buen Gobierno)* for 2030 and is placed at the head of listed Spanish companies with a greater female presence and prominence on its board. For this reason, it was deserving of the award for "Equality" in the II CSR Chemical Sector Awards, issued by the Spanish Chemical Industry Business Federation *(Federación Empresarial de la Industria Química Española)* in 2018.

In the field of sustainability, it must be emphasised there was a 30% reduction in the lost-time accident rate among our own staff and a 26% reduction in the absenteeism rate for common illness. The direct greenhouse gas emission rate also decreased by 11%. The total emissions rate increased by 51%, although such an increase is the consequence of incorporating new compounds in the calculation formula.

The consolidated and corporate management report, which forms part of this annual report, includes for the first time non-financial status information in accordance with the new Spanish Law 11/2018 of December 28. As required by this law, this report has been verified by an external certification company.

Although it is still early to make reliable forecasts, Ercros is cautiously optimistic regarding the Company's development in 2019. Only factors outside the Company's control —such as some GDP growth deceleration forecasts— are creating uncertainty. The increased production capacity will enable external production to be replaced by in-house production, which leads to greater margins. Additionally, the predicted reduction in procurement costs should also make a positive contribution to the profit and loss account.

Antonio Zabalza Martí
Chairman and CEO of Ercros

Barcelona, February 22, 2019

2.1. Organizational structure

The governing bodies of Ercros (hereinafter the "Company" or "Ercros") are the general meeting of shareholders and the board of directors and, within this: the audit committee and the appointments and remuneration committee. The operating management bodies are Ecofin and the management committee.

a) The annual general meeting

On June 15, 2018 the Company held its annual general meeting. Its agenda included, in addition to the mandatory or usual proposals —approval of the financial statements, re-election of the external auditor, advisory vote on the report on the remuneration of the directors, and delegation to the board and the secretary for executing the agreements—, the following proposals:

- The payment of a dividend of EUR 0.05 gross per share, which accounts for a 12.5% payout of the Ercros Group's consolidated profit in 2017, which amounted to EUR 44,492 thousand [see chapter 10.1 b)].

- A capital decrease amounting to EUR 930,897, through the redemption of the 3,103 thousand treasury shares that the Company held, which represent 2.8% of share capital, and which were acquired in the framework of the treasury share repurchase program, with an acquisition cost of EUR 10,025 thousand, which accounts for a payout equal to 22.5% of the consolidated profit obtained in 2017 [see chapters 9 and 10.1 b)].

The shareholders in the annual general meeting approved all the proposals for agreements included in the agenda. In attendance at the meeting were 7,526 shareholders of 78,794 thousand shares, representing 71% of the subscribed voting capital, of which 15.3% was present and the remaining 55.7% was represented.

The Company paid a gross premium of EUR 0.005 gross per share to the shareholders that attended or were represented at said meeting.

b) The board of directors

The composition of Ercros's board of directors has not changed over 2018 and it consists of the following members:

- Chairman and executive director: Antonio Zabalza Martí.

- Independent directors: Lourdes Vega Fernández and Carme Moragues Josa.

- Directors classified as "other external directors": Laureano Roldán Aguilar and Eduardo Sánchez Morrondo.

The position of non-director secretary continues to be held by Daniel Ripley Soria.

In 2018 the board met eight times: seven meetings were attended personally by the directors, and one meeting was held in writing and without the directors attending personally. Six of the meetings were attended by all the directors and in two of them the absent director delegated their vote to the coordinating director.

At the meeting held on April 19, 2018 the board of directors approved the anti-corruption and crime prevention policy. At this meeting, it also approved the update of the code of ethics for Ercros personnel.

(i) The audit committee

The composition of the audit committee has not changed over 2018, either. Its current composition is as follows:

- Chairwoman: Carme Moragues Josa, independent director.

- Audit committee members: Lourdes Vega Fernández, independent director, and Laureano Roldán Aguilar, a director belonging to the "other external directors" category.

The position of secretary of the audit committee continues to be held by Josep Rovira Pujals, who is also the administration director of Ercros.

Over 2018 the audit committee held five meetings, four of which were attended by all its members, and in the other one the absent director delegated their vote.

The internal audit department, which is led by Xavier Álvarez García, and the compliance committee, which is composed of Mr. Álvarez García and Asunción Loste Madoz, director of the legal department, answer to the audit committee.

(ii) The appointments and remuneration committee

No changes in the composition of the appointments and remuneration committee occurred in 2018, which is composed of:

- Chairwoman: Lourdes Vega Fernández, independent director.

- Appointments and remuneration committee members: Carme Moragues Josa, independent director, and Eduardo Sánchez Morrondo, a director belonging to the "other external directors" category.

The position of secretary of this committee continues to be held by Joaquín Sanmartín Muñiz, who is also the human resources director of Ercros.

In 2018 the committee held one meetings attended by all its members.

c) The Ecofin

It is the body that ensures that the agreements reached by the board of directors are put into practice and followed up, periodically monitors business evolution and approves the Group's investments and financing.

It consists of the CEO, the COO, the CFO and the secretary-general. This body meets once a fortnight and when the situation requires so.

No changes in Ecofin occurred over 2018.

d) The management committee

It is the body responsible for the monthly monitoring of the evolution of the businesses.

It consists of the CEO, the general managers, the managers of the three divisions and the managers of the general secretariat, administration, finance, sustainable development, human resources and information systems. Other managers of the Group are invited to the meetings of the management team, including the sales directors of the main activities.

No changes occurred in the management committee in 2018 and it met 11 times.

Composition of the board of directors at 12-31-18

Board member	Position	Category	Committees	Latest appointment
Antonio Zabalza Martí	Chairman and CEO	Executive	–	06-10-16
Carme Moragues Josa	Coordinating director	Independent	Audit and Appointments and remuneration	03-21-17
Lourdes Vega Fernández	Proxy coordinating director	Independent	Audit and Appointments and remuneration	06-10-16
Laureano Roldán Aguilar	Director	Other external director	Audit	06-10-16
Eduardo Sánchez Morrondo	Director	Other external director	Appointments and remuneration	06-10-16
Daniel Ripley Soria	Secretary, non-director			

2.2. Industrial structure

Ercros industrial group (hereinafter the "Group" or the "Ercros Group") is structured into three business segments: (i) the chlorine derivatives division, a business strategic unit with chlorine as the common link; (ii) the intermediate chemicals division, which focuses on the formaldehyde chemistry, which is the product from which the other products composing its portfolio are manufactured; and (iii) the pharmaceuticals division, which engages in the manufacture of active pharmaceutical ingredients ("APIs").

At December 31, 2018, the Group had ten production centres, all of them located in Spain.

a) Upgrade of the chlorine derivatives division

In 2018 the Group has continued to upgrade its chlorine and caustic soda production premises, a process that started in the prior year, after closing down the mercury-based technology plants, to this end, has increased its investment in the new chlorine-caustic soda production capacity using membrane-based technology, which is considered the best available technology ("BAT").

The purpose of these investments, which were included in the investment Act Plan, is to make the Group's actual chlorine and caustic soda production reach a similar level to the one it had in 2017. Consequently:

- On February 8 the extension —of 15,000 tonnes/year— of the production capacity in the electrolysis chlorine and caustic soda plant using membrane-based technology at the Sabiñánigo factory became operational, resulting in an increase in the chlorine production capacity of up to 45,000 tonnes/year.

- On December 13, the extension of 26,000 t/year of the chlorine and caustic soda production plant in Vila-seca I factory became operational, adding to the extension of 65,000 t/year made in December 2017.

- After this investment, a third extension of 26,000 t/year more was also launched in this Vila-seca I plant, which will become operational in the second half of 2019. Once this last extension is completed, the overall chlorine production capacity of the Group will reach 217,000 t/year (45,000 t/year at Sabiñánigo factory and 172,000 t/year at Vila-seca I).

Last year the Group also started the extension of the TCCA production plant for swimming-pool water treatment by 6,500 t/year, which is expected to become operational by the end of 2019. As a result of this extension, the Group's TCCA nominal production capacity will reach 28,000 t/year.

b) Extensions in the intermediate chemicals division

In 2018 the intermediate chemicals division has carried out significant extensions in the production capacity of the family of products with greater added value and whose premises had used up its capacity.

In the last quarter of 2018 an extension of the polyol production capacity from 5,000 t/year to 35,000 t/year was carried out at Tortosa factory. Additionally, the Group also managed to increase the energetic efficiency of this plant by introducing new internally-developed technologies.

At Cerdanyola factory, the production capacity of the moulding compounds plant was extended by 3,000 t/year up to 24,000 t/year. This investment has also allowed the Group to increase the supply of Carbaicar HD, a range of moulding compounds which is suitable for high performance standards.

Chlorine nominal production capacity

T/YEAR

		Extensions			
	Previous situation	12-17-17	12-13-18	09-30-19 [1]	Final location
Vila-seca I	55,000	+65,000	+26,000	+26,000	172,000
Sabiñánigo	30,000	+15,000			45,000
Total	**85,000**	**+80,000**	**+26,000**	**+26,000**	**217,000**

[1] Estimated date.

Centres and products

Division	Facilities	Products	Applications
Chlorine derivatives	Flix, Monzón, Tarragona, Sabiñánigo, Vila-seca I and Vila-seca II	Caustic potash Caustic soda Chlorine Chloroisocyanurates EDC Hydrochloric acid PVC Sodium chlorate Sodium chloride Sodium hypochlorite VCM	Chemical industry General Industry Derivatives manufacturing Pool water treatment VCM manufacturing General industry Construction Paper pulp bleaching Water treatment Water treatment PVC manufacturing
Intermediate chemicals	Almussafes, Cerdanyola and Tortosa	Formaldehyde Glues and resins Moulding compounds Paraformaldehyde Pentaerythritol Sodium formate	Derivatives manufacturing Wood industry Sanitary and electrical equip. Resins Paints Tanning industry
Pharmaceuticals	Aranjuez	Erythromycins Fosfomycins Fusidic acid	Antibiotics Antibiotics Skin infections

2.3. Operation

a) Mission and principles

The general purpose of the Ercros Group is to consolidate a solid and long-lasting industrial group that contributes to generate social wealth and wellbeing that gives appropriate returns to its shareholders and favours personal and professional development of its employees.

The Group's measures, aimed at increasing its value, is guided by three core principles: (i) maximum security for its employees, neighbours and installations; (ii) absolute respect for the environment, and (iii) satisfying the needs of its customers and the greatest quality of its products

b) Corporate strategy

The Ercros Group defines its business strategy according to multiannual plans that establish the measures to be adopted in order to increase productivity and efficiency in the use of its resources.

The three major long-term strategic objectives of the Group are:

— To create an efficient, healthy and profitable chemical group with international presence.

— To have modern and environment-friendly and industrially integrated productive premises of a European dimension and located at competitive sites.

— Focus on high added-value products, which present competitive advantages and offer growth expectations.

Industrial upgrade plan and extension of production capacity (Act Plan)

As indicated in section 2.2 above, an inversion Act Plan was initially designed to face the technological change derived from the EU prohibition to produce chlorine using mercury-based technology. Act Plan has been subsequently extended to upgrade its industrial park and include other measures to increase the manufacturing capacity of the most in-demand products and reach commercial success. After the implementation of these measures, the plan will entail investment of around EUR 100,000 thousand in the 2016-2020 period.

The execution of this plan is currently in an advanced phase and follows the expected timetable. Big progress has been made in 2018 thanks to the aforementioned extensions that became operational [see chapter 4.3 b)].

c) Business model and challenges

Chlorine is the common link of the chlorine derivatives division. Chlorine and caustic soda are obtained simultaneously during the same production process from sodium chloride (common salt) dissolved in water (brine) and electricity, in a proportion of 1 ton of chlorine to 1.12 tonnes of caustic soda. This assembly is known as the electrolytic unit ("ECU"). The margin of the ECU is determined: (i) in the income side, by the selling price of co-produced caustic soda and sensitivity from the different chlorine applications; and (ii) in the cost side, by the price of energy power at any given time, which accounts for around 44% of production costs. Approximately 60% of the chlorine produced by the Group is used in the production of chlorine derivative products (sodium hypochlorite, hydrochloric acid, TCCA and the EDC/VCM/PVC chain) and the rest is piped to Covestro.

The main challenge that the chlorine derivative division faces in the short term is to reach by 2020 the level of chlorine and caustic soda production it had when the mercury-based plants that were closed down in December 2017 were still operational. In the medium term, the challenge that this division faces is to increase the overall margin of each ECU for all chlorine uses, mainly PVC, in a context in which the price of electricity is very high because of the decarbonisation of industry.

Formaldehyde is the key product of the intermediate chemicals division, and methanol its main raw material. This consumable accounts for around 40% of the division's total costs. 81% of formaldehyde that is produced is used in the manufacture of liquid as well as solid derivatives. These, which account for 66% of the business's revenue, have greater added value than the liquids and its market is global.

In the short and medium terms, it is expected that the worldwide demand for the main products of the intermediate chemicals division will increase while the global production capacity is decreasing. The challenge of this business is to maintain global leadership based on qualitative differentiation with respect to the products of the competition, mainly of Asian origin, maintaining competitiveness and profitability.

The pharmaceuticals division focuses on the production of raw materials and APIs, mainly from the family of antibiotics, which are marketed as generic products. The division also specializes in the preparation of other active and intermediate principles specially tailored for the customers. The main value of this business is its global leadership in the production of certain APIs, due to its command of their manufacturing processes, through both fermentation and chemical synthesis, and also because of its sterile packaging capacity.

The main short- and medium-term challenge of this business is to make the higher packaging capacity of sterile products profitable by incorporating new products and opening new markets for sterile fosfomycin. It is also important to achieve a better use of the fermentation capacity installed. In the long term this business must meet the quality demands of the customers and regulatory agencies, develop new strains, extend the product portfolio and face competition from China and India.

3.1. Analysis of the business evolution and results

a) Production

2018 has been a year of great challenges for the Group as it has been the year in which the extensions in the membrane-based technology electrolysis plants that replaced the closed-down mercury-based technology plants became operational, coping with the inherent difficulties that these processes entail. We can now state that the challenge has been satisfactorily overcome [see chapter 2.2].

As expected, production in the electrolysis plants has decreased, as well as in other plants where capacity extensions have been carried out, as a stoppage was required during the connection works. Consequently, the Group manufactured 1,378 thousand tonnes of products, 31.1% less than in the prior year.

As a result of the aforementioned causes, the most significant drop occurred in the chlorine derivative division, where production between 2017 and 2018 was reduced by 38.3%. The close-down of the mercury-based technology electrolysis plants affected in particular the chlorine and caustic soda production.

In order to meet the market's needs, the decrease in production has been replaced with the purchase of third-party products. This circumstance, together with higher selling prices, has allowed the Group to maintain similar sales figures to last year's. As indicated in chapter 2.2, by 2020 the Group will have recovered the level of chlorine and caustic soda production it had in 2017.

During the year, improvements in the production processes and PVC and TCCA premises have also been made, which resulted in the manufacture of these products to reach annual historical highs.

However, in terms of production volume, the most relevant fact has been the closure of the Cardona factory on December 15, 2017 and, consequently, the discontinuation of the sodium chloride production. This product was used as raw material in the closed-down mercury-based technology electrolysis plants and has been replaced with a third-party product of several origins that meets the purity and quality standards required by the membrane-based technology electrolysis plants.

The reduction in the production of EDC, which is the first product used in the PVC chain, has also been significant in the chlorine derivative division. Also in this case, the lesser amount of own EDC available has been met by purchasing third-party EDC of several origins.

Finally, in 2018 the production of caustic potash stopped temporarily. This product was manufactured together with chlorine in the membrane-based technology electrolysis plant at Sabiñánigo factory. Due to the good performance of the caustic soda market, the Group decided to adapt this plant so that it could produce both chlorine-caustic soda and chlorine-potash. This has allowed the Group, for the same chlorine production, to increase caustic soda production by 30,000 t/year while maintaining the supply of potash to customers with third-party product.

The intermediate chemicals division is the business whose production has decreased the least. (4.2%). The reason for this reduction are the scheduled stoppages made in the last quarter of the year so that the new capacity extensions become operational, as well as the need for a gradual start of the new premises [see chapter 2.2 b)].

In the case of the pharmaceuticals division, production has decreased by 12.9%. This reduction is almost entirely focused on the fosfomycin family and is mainly due to the adaptation of production to the demand for fosfomycin pea salt.

b) Income

In 2018 the Group managed to maintain almost the same sales figure despite the decreased volume of own products. This was possible because of the commercialization of third-party product and the average high level reached by the prices of almost all products, despite the fact that in the second half of the year they started a slight decreasing trend. Sales amounted to EUR 639,543 thousand and were a bit below the ones obtained last year (0.4%), which amounted to EUR 641,793 thousand.

The chlorine derivative division —which as said before was the most affected by the reduction in the volume of own products available— managed to maintain its turnover, and the sales figure hardly decreased (0.5%), from EUR 396,558 thousand in 2017 to EUR 394,388 thousand in 2018. This division consolidated substantial increases in the price of several of its products, such as caustic soda, sodium hypochlorite and hydrochloric acid.

The intermediate chemicals division was the only Group's business where sales increased in 2018. The intermediate chemicals division's turnover amounted to EUR 193,992 thousand in comparison with EUR 191,259 thousand in the prior year, which means a 1.4% increase. This higher turnover is due to the increase in the price of the main raw materials (methanol, urea and melamine) as the depreciation of the average dollar exchange rate acted as an opposite effect (23.5% of this business's sales are made in US dollars). This depreciation has negatively impacted turnover by EUR 2,093 thousand.

In percentage terms, the biggest drop in sales corresponds to the pharmaceuticals division, which has decreased from EUR 53,976 thousand in 2017 to EUR 51,163 thousand in 2018 (a 5.2% reduction). In this case, the effect of the US dollar —which has taken EUR 981 thousand off sales— has partnered with a slight reduction in the volume sold.

The Group product that showed the best evolution in 2018 was sodium hypochlorite, which more than doubled its price and increased the volume sold in comparison with the prior year. The huge increase in its price is due to the decrease in supply in Spain as a result of the stoppage in several electrolysis plants producing chlorine-soda. This also explains the significant increase in the price of hydrochloric acid and caustic soda, the latter even above the high values it reached in 2017.

In order to meet the need for caustic soda of the Group's customers, within a context of decreased production, the Group increased the purchase of external product by 87.3%, which allowed it to substantially minimize the loss in the sales volume and maintain its market share.

After the PVC family, caustic soda is the second product that most contributes to the Group's turnover. This last product showed very irregular performance over the year; the first half of the year was highly favourable whereas the second half was mainly affected by the trade war between the US and China, which entailed the entry of American product in Europe, at a cheaper price. However, considering the year as a whole, PVC sales remained stable in terms of both volume and price. Caustic soda and PVC account for 37.8% of the Group's sales.

Other products that performed well in 2018 were, in the intermediate chemicals division, paraformaldehyde, glues and resins and, in the pharmaceuticals division, fusidic acid, which reached a historical sales volume.

None of the customers taken separately accounts for more than 10% of the Group's sales.

The Group's turnover has also been affected by the 18.3% reduction in income from the rendering of services (EUR 7,279 thousand). Almost this entire decrease is due to the lower remuneration for the interruptibility service of electricity, whose amount went down by 45.8% between 2017 and 2018.

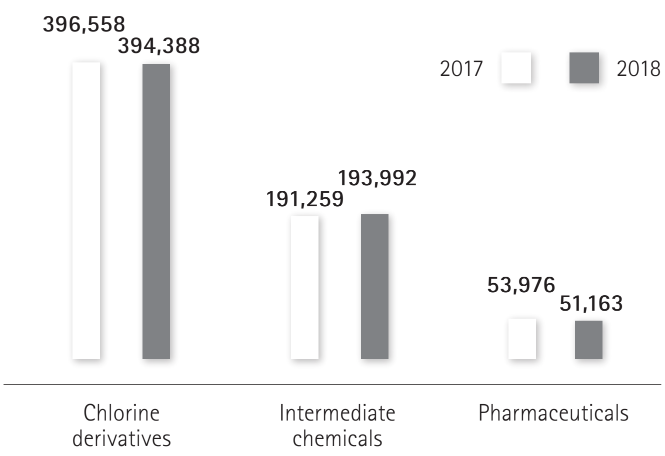
On a negative note, the lesser income from the reversal of provisions, amounting to EUR 5,121 thousand, should also be highlighted. This was due to the re-estimate made in 2017 of some provisions set aside for an amount of EUR 6,942 thousand, in comparison with EUR 1,821 thousand recorded for reversal of provisions in 2018.

On a positive note, the change in inventories of finished products and work in progress stands out, improving by EUR 4,839 thousand compared to 2017 due to the higher volume of products in stock at prior year end, which in turn was due to the increase in marketed products and the high December production rates after the new investments became operational. The "Other income" caption also performed well, increasing by EUR 577 thousand.

As a result, income amounted to EUR 684,802 thousand in comparison with EUR 694,037 thousand in 2017, a difference of EUR -9,235 thousand, that is a 1.3% decrease.

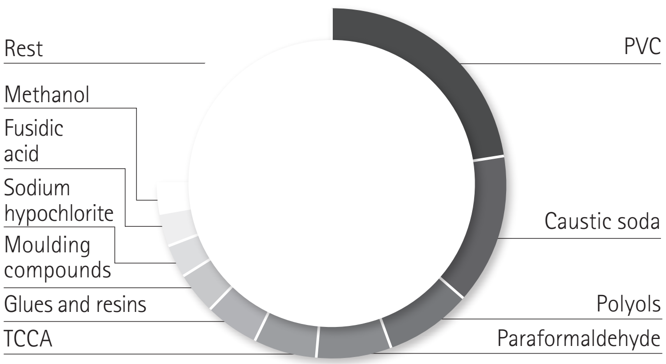
Sales by division

EUR THOUSAND



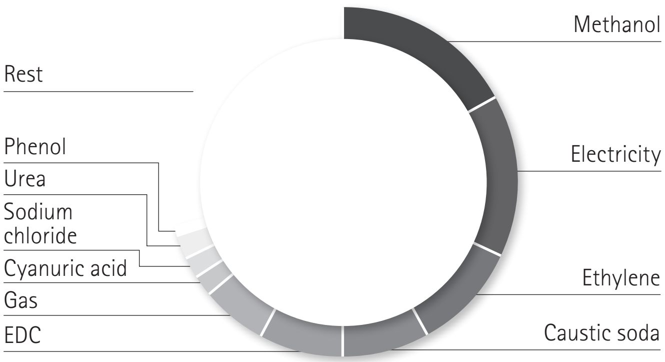
Top ten products

% OVER SALES IN 2018



Top ten procurements and utilities

% OVER PURCHASES IN 2018



c) Expenses

Expenses in 2018 amounted to EUR 621,896 thousand and were 0.4% higher than in 2017, when they amounted to EUR 619,726 thousand. This slight increase includes the significant rise in the procurement bill and the higher charge to provisions for other liabilities, which are almost entirely offset by the decrease in the other items in this chapter, such as utilities, employee benefits expense and other operating expenses.

The increase in the oil price and the global geostrategical tension have caused the prices of most of the Group's procurements and utilities —such as electricity and methanol at the forefront— to increase again over the already expensive prices they had in 2017.

The increase in costs was even higher in the second half of the year and, although it could be partially mitigated thanks to the high selling prices of end products, it meant a stop in the improvement in profitability seen in the first half of the year. In autumn last year, the prices of raw materials and electricity reached historical highs, although in the last weeks of the year they started to decrease and continued to do so in the first weeks of 2019.

As a result of the high price of raw materials, the procurements and utilities ratio over the Group's sales worsened between 2017 and 2018 from 67.1% to 68.5%.

In 2018 procurements, amounting to EUR 341,780 thousand (EUR 316,581 thousand in 2017), increased by 8%. In addition to the price factor, this increase has also been due to the higher volume of products acquired, mainly sodium chlorine, EDC and caustic soda. In the case of sodium chlorine, third-party product has been purchased to replace the production of Cardona factory, which was closed at the end of 2017. In the case of EDC, the purchase was made to cover the demand of the PVC plant within a context of lesser chlorine availability. And in the case of caustic soda, in order to keep our market share after the temporary reduction of the production of own product [see subsection a) above].

Additionally, the cost of utilities decreased to EUR 96,027 thousand in 2018 (EUR 114,389 thousand in 2017), which means a 16.1% reduction. This drop occurs despite the strong increase in the price of electricity (+14.2%) —its main component— and is due to the reduction in power consumption as a result of a better energetic efficiency in the new premises and the lower production in electrolysis plants in the current year.

As occurred with electricity, the increase in the oil price also push up significantly the cost of methanol (+12.8%), which hindered the profitability of the intermediate chemicals division because of the big impact of this raw material on its costs.

Other products whose cost has also increased as a result of the increase in the oil price were natural gas (+7.3%) —the price of this supply has a special impact on the margin of the intermediate chemicals business and PVC— and ethylene (+6.6%). However, as already happened in 2017, the bill for this last product has decreased due to the reduction in the production of own EDC, of which it is a raw material. The other side of this effect has been a higher volume of purchased third-party EDC, as commented above. Both ethylene and EDC are the most significant costs in the PVC production process.

Unlike electricity, fluctuations in the price of methanol and ethylene —if favoured by demand— can be usually passed on to the price of final products, especially in the latter case, which makes it possible to keep the margins [see subsection d) below], although this was not possible in 2018.

Methanol, electricity and ethylene are the most significant raw materials in the Group's costs. These three products account for 42% of total consolidated purchases, and exceed 40% of the total costs of the manufacturing processes of formaldehyde, chlorine and PVC, respectively.

The expenses chapter also includes a significant increase in charges to provisions for several items, for an amount of EUR 3,458 thousand. In 2018 provisions were charge for an amount of EUR 6,354 thousand (2017: EUR 2,896 thousand).

Employee benefits expense —amounting to EUR 79,870 thousand— decreased by EUR 3,517 thousand (4.2%), mainly because of the staff reduction resulting from the collective dismissal due to the close-down of the mercury-based technology electrolysis plants. In 2018 the average headcount of the Ercros Group was 1,290 people (1,372 people in 2017), that is, 82 people less, which means a 6% decrease in staff.

Other operating expenses amounted to EUR 97,865 thousand (2017: EUR 102,473 thousand). This caption includes, as its main items, maintenance expenses, which decreased by EUR 1,200 thousand; transport expenses, which decreased by EUR 3,043 thousand and lease expenses for logistic premises, which increased by EUR 1,525 thousand.

d) Results

(i) Consolidated results

As commented at the beginning of the chapter, the Group satisfactorily overcame the main challenge it had to face in 2018: the change of technology in the electrolysis plants without weakening activity.

As the year passed by —in line with the sharp slowdown experienced by the main European economies— in the income chapter, the price of end products started to slightly decrease as the amount of the services rendered dropped because of the lower remuneration of the electricity interruptibility service. In the expenses chapter, on the contrary, the price of raw materials consolidated its upward trend until reaching historical highs.

In comparison with the prior year, 2018 was damaged by the impact of charges and reversals of provisions, reducing ordinary ebitda by EUR -8,579 thousand. This figure results from the decrease in the income from the reversal of provisions —amounting to EUR 5,121 thousand— and from the increase in the expense for the charge to provision by EUR 3,458 thousand.

The evolution of income and expenses between 2017 and 2018 has given rise to a gross ordinary operating profit ("ebitda") that has decreased by 15.3% amounting to EUR 62,906 thousand in 2018 (2017: EUR 74,311 thousand). Additionally, the drop in ordinary ebitda has caused a reduction in the margin of ordinary ebitda over sales, which decreased from 11.6% in 2017 to 9.8% in 2018.

The recognition in 2017 of costs and provisions derived from the phase-out of the mercury-based technology, for an amount of EUR 21,732 thousand, cause operating profit ("ebit") to increase by 25.9% and reach EUR 43,212 thousand (EUR 34,327 thousand in 2017).

Depreciation and amortization amounted to EUR 19,694 thousand (EUR 18,252 thousand in 2017), 7.9% higher due to the new investments that became operational.

Finance costs —amounting to EUR 5,823 thousand— were reduced by EUR 124 thousand (2.1%), despite the increase in debt, because of the average cost thereof.

In 2018 the Group has recorded an income tax income of EUR 6,876 thousand which is below the EUR 15,899 thousand recorded in 2017. At December 31, 2018 the Group still has unrecognized deferred tax assets amounting to EUR 76,397 thousand (2017: EUR 91,207 thousand).

As a result, profit amounts to EUR 44,876 thousand, which is higher than prior year's (EUR 44,492 thousand) by 0.9% (EUR 384 thousand).

This slight increase in profit and the reduction in the amount of shares have resulted in a 4% improvement in earnings per share ("EPS"), which has increased from EUR 0.396 in 2017 to EUR 0.411 in 2018 [see chapter 10.2].

Income statement

EUR THOUSAND

	Year 2018	Year 2017	Change (%)
Income	**684,802**	**694,037**	**–1.3**
Sales of goods	639,543	641,793	-0.4
Rendering of services	32,397	39,677	-18.3
Other operating income	8,364	7,787	7.4
Reversal of provisions for other liabilities	1,821	6,942	-73.8
Changes in inventories	2,677	-2,162	–
Expenses	**–621,896**	**–619,726**	**0.4**
Procurements	-341,780	-316,581	8.0
Utilities	-96,027	-114,389	-16.1
Employee benefits expense	-79,870	-83,387	-4.2
Other operating expenses	-97,865	-102,473	-4.5
Charge to provisions	-6,354	-2,896	×2.2 [1]
Ebitda from ordinary activities	**62,906**	**74,311**	**–15.3**
Cost of mercury technology phase-out:			
Workforce reduction	0	-11,000	–
Dismantling and remediation	0	-10,732	–
Depreciation and amortization expenses	-19,694	-18,252	7.9
Ebit	**43,212**	**34,327**	**25.9**
Finance costs, losses and impairment	-5,823	-5,947	-2.1
Exchange gains (losses)	-521	-437	19.2
Share in the profit of associated companies	1,132	740	53.0
Profit before tax	**38,000**	**28,683**	**32.5**
Income tax	6,876	15,899	-56.8
Other comprehensive income	0	-90	–
Profit for the year	**44,876**	**44,492**	**0.9**
Earnings per share (euros)	**0.4111**	**0.3963**	**3.7**

[1] Multiplicative factor.

(ii) Profit from the chlorine derivatives division

2018 was a good year for the chlorine derivatives business if we take into account that it came from a significantly lower production capacity —derived from the discontinuation of the mercury-based technology electrolysis plants— and that during the year it had to face the issues arisen in the processes for launching the new capacity extension, as well as assuming the increase in variable costs, in particular electricity.

All these negative effects were offset by the strength of demand which, as a result of a generalized scarce supply, had to assume the proposed increases in the prices of end products, and also by the depreciation of the dollar exchange rate, which, unlike in the other two businesses, favoured this division because of the higher amount of purchases made in this currency in comparison with sales.

Additionally, this business's ebitda has decreased by 2.7% from EUR 48,016 thousand in 2017 to EUR 46,707 thousand in 2018. The main reason for this difference is the net balance of the provisions charged in both years.

This reduction in ordinary ebitda, within a context of stable sales, caused a decrease in the margin of ebitda over sales, which reached 11.8% (12.1% in 2017). Despite the reduction, the ratio in 2018 continues to be one of the highest ever reached by this business.

However, in comparison with the prior year, the division's ebit has more than doubled again as no non-recurring costs were recorded in 2018, as happened in 2017 as a result of the phase-out of the mercury-based technology. So in 2018 the business's ebit amounted to EUR 34,878 thousand in comparison with EUR 15,342 thousand in 2017, a difference of EUR 19,536 thousand.

After discounting the finance costs, which amount to EUR 3,755 thousand, the business's profit totalled EUR 31,123 thousand, which is more than 2.5 times higher than last year's (EUR 11,912 thousand).

(iii) Profit from the intermediate chemicals division

For the intermediate chemicals division, 2018 was a transition year while the effect of the extensions in production capacity made in several plants manifests, which is expected to occur in 2019.

This business's markets, in general, remained stable, especially in the case of paraformaldehyde, which could apply significant increases in price. It was also a good year for glues and resins thanks to the successful launch of the new ErcrosGreen+ range, which presents greater added value in comparison with traditional products.

The increase in the selling prices, however, did not result in improved results due to the pressure that several elements exercised against it: (i) the lower volume of available products for sale; (ii) the upward evolution of the prices of the main procurements —methanol, urea and melamine— and utilities —natural gas and electricity—; and (iii) the depreciation of the average dollar exchange rate, which worsened the business's profitability because of the significant weight (23.5%) that the American currency has on its sales.

Thus, the division's ebitda decreased substantially from EUR 16,542 thousand in 2017 to EUR 10,182 thousand in 2018. After recording depreciation and amortization and finance costs —which have barely changed in comparison with 2017— the division's profit amounted to EUR 4,124 thousand (EUR 10,358 thousand in the prior year).

(iv) Profit from the pharmaceuticals division

The pharmaceuticals division was damaged in 2018 by (i) the average dollar exchange rate (the US dollar accounts for 44.8% of its sales; (ii) the drop in sales of two of the most mature products (fosfomycin pea salt and erythromycin base); and (iii) the increase in variable costs (raw materials and energy).

On a positive note, the good performance of fusidic acid should be highlighted —the product has the highest margin in the business— and the successful conclusion of the inspections by the health authorities as a prior step to the commercialization of several products in the US and South Korea. Obtaining the certifications from said authorities in 2019 will allow the division to conduct business in these important markets.

As a result of these opposite factors, the division generated an operating profit that is EUR 1,587 thousand lower than in 2017. However, the recognition in 2018 of several non-recurring expenses, for an overall amount of EUR 2,149 thousand, of a diverse nature has had a strong impact on the division's ebitda, which has decreased from EUR 9,753 thousand in 2017 to EUR 6,017 thousand in 2018. The drop in the division's ebitda caused the ebitda over sales margin to decrease from 18.1% to 11.8%.

Lastly, profit before tax in 2018 amounted to EUR 2,753 thousand in comparison with EUR 6,413 thousand in 2017.

Results by business segment
EUR THOUSAND

	Chlorine derivatives division			Intermediate chemicals division			Pharmaceuticals division		
	Year 2018	Year 2017	Change (%)	Year 2018	Year 2017	Change (%)	Year 2018	Year 2017	Change (%)
Sales of goods	394,388	396,558	-0.5	193,992	191,259	1.4	51,163	53,976	-5.2
Ebitda from ordinary activities	**46,707**	**48,016**	**-2.7**	**10,182**	**16,542**	**-38.4**	**6,017**	**9,753**	**-38.3**
Cost of mercury technology phase-out	0	-21,732	–	0	0	–	0	0	–
Depreciation and amortization expenses	-11,829	-10,942	8.1	-4,854	-4,470	8.6	-3,011	-2,840	6.0
Ebit	**34,878**	**15,342**	**x2.3** [1]	**5,328**	**12,072**	**-55.9**	**3,006**	**6,913**	**-56.5**
Finance cost	-3,755	-3,430	20.4	-1,204	-1,714	-29.8	-253	-500	-49.2
Profit before tax	**31,123**	**11,912**	**x2.6** [1]	**4,124**	**10,358**	**-60.2**	**2,753**	**6,413**	**-57.1**
Assets	363,131	362,745	0.1	183,104	182,674	0.2	56,336	53,754	4.8
Liabilities	199,593	221,029	-9.7	93,629	91,611	2.2	40,685	39,041	4.2
Investments in non-current assets	20,662	37,252	-44.5	7,314	4,436	64.9	3,609	3,128	15.4

[1] Multiplicative factor.

e) Geographical markets

In 2018 exports in the three businesses and in all geographical areas decreased due to the strong domestic demand and the unfavourable average dollar exchange rate, which damaged exports to the areas operating in this currency. Thus, the slight decrease in the Group's sales (0.4%) is due to the 5.5% drop in foreign market sales and the 4.8% increase in domestic sales.

The domestic market accounted for 52.7% of sales and amounted to EUR 336,876 thousand (EUR 321,561 thousand in 2017). The remaining 47.3% of sales were made abroad and amounted to EUR 302,668 thousand (2017: EUR 320,232 thousand).

67% of the chlorine derivatives division's turnover was recorded in Spain. Between 2017 and 2018 in this business the Spanish market increased by 6.5% and exports decreased by 12.4%.

On the contrary, in the intermediate chemicals division, the increase in turnover was due to the growth in foreign market (+2.6%) while sales in the domestic market decreased by 0.7%. In this business exports accounted for 64.8% of sales.

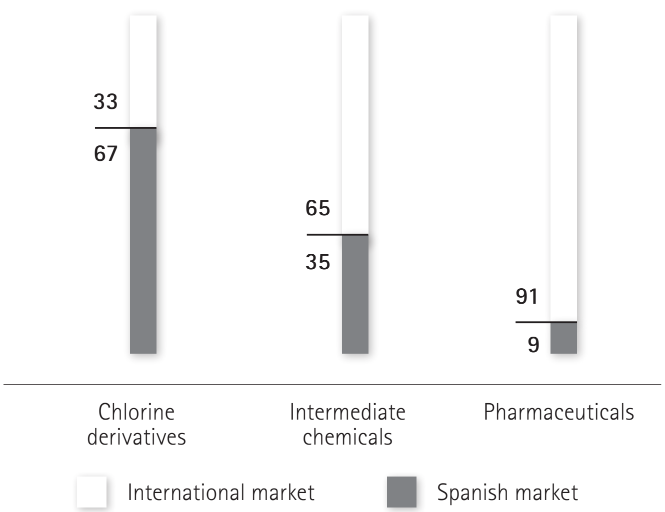
In the case of the pharmaceuticals division, the drop in sales affected both exports (-4.9%) and sales in Spain (-8.5%), although it should be noted that 91.9% of the business's turnover was generated abroad.

The EU is the main destination of the Group's exports and accounts for 28.1% of consolidated sales. Turnover in this area remained stable (-0.3%) in comparison with 2017. Sales in OECD countries, however, decreased by 8%. This geographical area accounts for 7.8% of the Group's sales. Nevertheless, the area that showed poorer performance was the rest of the world, which accounts for 11.4% of consolidated turnover and saw a decrease in sales of 14.7% between 2017 and 2018.

France, Italy, Portugal and Turkey continue to be the main destinations of the Group's exports. The first two alone account for 31.8% of consolidated sales in foreign markets.

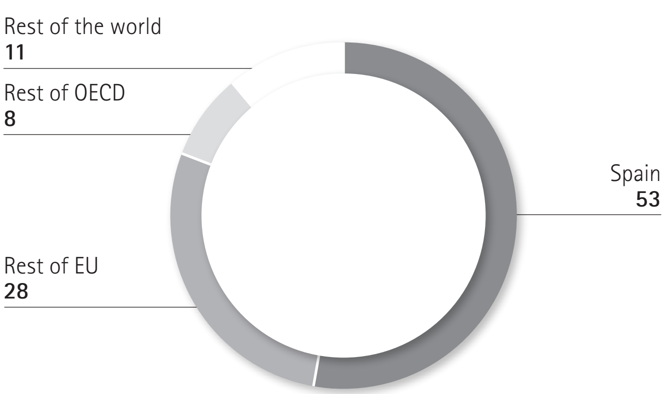
Business markets

% OVER EACH DIVISION'S SALES IN 2018



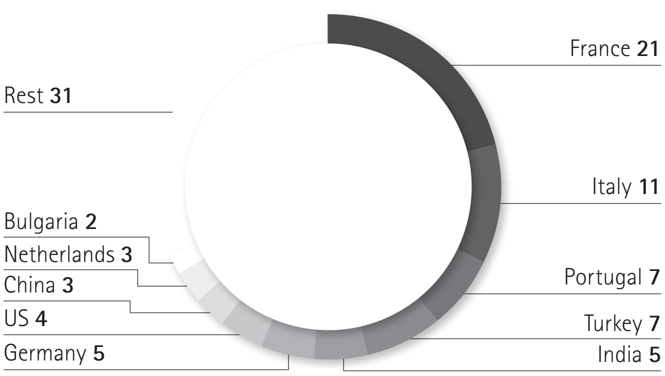
Sales by geographical areas

% OVER SALES IN 2018



Top ten destinations

% OVER EXPORTS IN 2018



f) Exchange rate

The only assets and liabilities exposed to foreign currency risk are those arisen as a result of ordinary purchases and sales. No other assets in the Group's balance sheet are exposed to foreign currency risk.

The US dollar is —by far— the main foreign currency that the Group is exposed to. No derivative instrument to hedge this risk is arranged.

In 2018 the average exchange rate of the US dollar depreciated against the euro. In the case of the Group's consolidated sales, the average exchange rate increased from 1.130 US dollar/euro in 2017 to 1.181 US dollar/euro in 2018 (a 4.5% difference). In 2019 a neutral effect of the US dollar is expected in comparison with 2018, and therefore, it is not expected that the profitability of the Group's will decrease for this reason.

The fact that the US dollar is depreciated against the euro has a negative effect on the Group, since the competitive position of the products it markets worsens, which explains the decrease in sales in this currency in 2018 compared to 2017, and damages the return in euros on the sales in dollars, which reduces profitability.

The sales in US dollars in 2018, amounting to DOL 101,677 thousand, were 4% lower than in 2017 (DOL 105,865 thousand) and accounted for 12.8% of total consolidated sales (13.6% in the prior year).

Between 2017 and 2018, however, purchases in US dollars increased substantially from DOL 42,544 thousand to DOL 63,889 thousand. This 50.2% increase is mainly due to the higher volume of purchased EDC, a product that is paid for in US dollars. In 2018 purchases in US dollars accounted for 12.4% of total procurements and utilities paid for by the Group (8.8% in the prior year).

The strong increase in purchases made in US dollars —and to a lesser extent, the decrease in sales made in this currency— resulted in a reduction of the Group's net exposure to US dollar, which amounted to DOL 7,788 thousand in 2018 compared to DOL 63,321 thousand in the prior year. Despite this, the effect of the dollar depreciation over the Group's ebitda —calculated based on 2018 net exposure— was EUR 1,521 thousand.

3.2. Financial, operating and stock market indicators

Indicators[1]	Year 2018	Year 2017
Financial		
For the payment of dividend:		
Leverage ratio (< 0.5)	0.39	0.36
Solvency ratio (< 2)	1.71	1.20
Liquidity	1.02	1.02
Funding of assets	1.02	1.01
ROCE (%)	10.30	14.19
Average collection period (days)	60.21	60.30
Average payment period (days)	55.40	49.11
Operating		
Production (thousands of tonnes)	1,378	2,010
Added value (EUR thousand)	142,776	157,698
Productivity (euros/person)	110,679	114,940
Gross margin/revenue (%)	50.09	54.39
Ordinary ebitda/sales margin (%)	9.36	10.90
Stock market		
Quoted market value (euros/share)	3.11	2.86
Capital value (EUR thousand)	335,496	317,402
EPS (euros)	0.411	0.396
CFS (euros)	0.41	0.39
PER	7.48	7.13
P/BV	1.23	1.28

[1] Calculation method and purpose of each indicator:

Leverage ratio:
- Calculation: net debt ÷ total equity.
- Purpose: evaluate the level of non-group financing over the Group's equity.

Solvency ratio:
- Calculation: net debt ÷ ordinary gross operating profit/loss.
- Purpose: evaluate the capacity to repay third-party financing in number of years.

Liquidity:
- Calculation: current assets ÷ current liabilities.
- Purpose: evaluate the capacity to meet payment commitments in the short term.

Funding of assets:
- Calculation: (equity + non-current liabilities) ÷ non-current assets.
- Purpose: evaluate to which extent non-current assets are financed with permanent resources.

ROCE:
- Calculation: ordinary operating profit/(loss) ÷ resources used.
- Purpose: measure the level of return obtained by the Group in its ordinary business over the investment made.

Average collection period:
- Calculation: (average receivables in the year ÷ sales) × 365.
- Purpose: evaluate the average of days between sales and total collections in the year.

Average payment period:
- Calculation: (average payables in the year ÷ operating costs) × 365.
- Purpose: evaluate the average of days between purchases and total payments in the year.

Production:
- Calculation: volume of produced units.
- Purpose: measure the number of physical units produced.

Added value:
- Calculation: ordinary ebitda + employee benefits expense.
- Purpose: measure the wealth generated by the Group.

Productivity:
- Calculation: added value ÷ number of employees.
- Purpose: measure each employee's contribution to the generation of the Group's added value.

Gross margin/revenue:
- Calculation: (Income – procurements) ÷ revenue.
- Purpose: evaluate the profitability of the Group's product portfolio.

Ordinary ebitda/sales margin:
- Calculation: ordinary gross operating profit/loss ÷ sales.
- Purpose: measure the profitability of sales in relation to ordinary gross operating profit obtained.

Quotation:
- Calculation: Ercros share quoted price at year end.
- Purpose: know the value given by the market to each Company share.

Market capitalization:
- Calculation: quoted price at year end × number of issued shares.
- Purpose: know the value allocated by the market to the Group's total equity.

EPS:
- Calculation: consolidated profit/(loss) for the year ÷ weighted average number of shares.
- Purpose: measure the earnings corresponding to each share.

CFS:
- Calculation: operating cash flow ÷ number of shares
- Purpose: measure the generated cash flow corresponding to each share.

PER:
- Calculation: market capitalization ÷ profit/(loss) for the year
- Purpose: know how many times earnings per share is included in the share value.

P/BV:
- Calculation: market capitalization ÷ total equity.
- Purpose: relate the Company's value in the stock exchange to its underlying net book value.

+ = added × = multiplied ÷ = divided

4.1. Economic analysis of the balance sheet

As a management tool, the Group uses the economic analysis of the balance sheet, which is obtained from certain presentation reclassifications of the consolidated statement of financial position in order to reduce the number of operating magnitudes and achieve a better analysis and comparison.

Between 2017 and 2018 year ends, non-current assets have increased by EUR 18,586 thousand mainly because of the investments made [see section 4.3 b) below]. The investment plan also explains the rise in net financial debt ("NFD"), which increased by EUR 18,050 thousand and amounted to EUR 107,307 thousand at December 31, 2018 (EUR 89,257 thousand at 2017 year-end).

Working capital has increased by EUR 17,103 thousand, mainly due to the increase in inventories as a result of the increase in commercialized products, while trade receivables have decreased.

The Group's total equity —amounting to EUR 272,669 thousand— has increased by EUR 25,177 thousand. This variation is lower than the profit obtained, due to the shareholder remuneration, that resulted in a decrease in total equity of EUR 16,826 thousand (EUR 12,001 thousand due to the purchase of treasury shares; EUR 4,439 thousand due to dividends paid; and EUR 386 thousand due to the payment of the annual general meeting attendance bonus) [see chapter 10.1].

Provisions and other debts have decreased by EUR 7,538 thousand. It should be noted that in 2017 this caption included —among other provisions—the costs from the phase-out of the mercury-based technology, amounting to EUR 21,732 thousand, of which EUR 10,117 thousand were paid in 2018 (EUR 1,121 thousand in 2017). Of these payments, EUR 5,285 thousand related to the dismantling of plants and EUR 4,832 thousand related to the collective dismissal.

Economic analysis of the balance sheet [1]

EUR THOUSAND

	12-31-18	12-31-17	Change (%)
Non-current assets	**337,093**	**318,507**	**5.8**
Working capital	**93,698**	**76,595**	**22.3**
Current assets	218,877	218,282	0.3
Current liabilities	-125,179	-141,687	-11.7
Applied funds	**430,791**	**395,102**	**9.0**
Equity	**272,669**	**247,492**	**10.2**
NFD [2]	**107,307**	**89,257**	**20.2**
Provisions and other borrowings	**50,815**	**58,353**	**-12.9**
Origin of funds	**430,791**	**395,102**	**9.0**

[1] The Company uses the economic analysis of the balance sheet, which is obtained from certain presentation reclassifications of the balance sheet in order to reduce the number of operating magnitudes and achieve a better analysis and comparison.

[2] All financial debts with non-bank entities are recognized in NFD. Additionally, apart from cash and cash equivalents, those deposits that guarantee debt commitments have been recognized as a decrease in the financial debt (in 2018: EUR 9,078 thousand, and in 2017: EUR 13,878 thousand).

4.2. Liquidity

The Group manages liquidity risk by using financial planning techniques, which take into consideration cash inflows and outflows relating to operating, investing, and financing activities.

The Group's objective is to keep a balance between the flexibility, the terms and the conditions of the financing sources registered, based on expected needs in the short, medium and long terms.

The Group's financing is subject to meeting obligations and financial ratios, which have been appropriately fulfilled in 2018.

The improvement in Europe's economic environment and greater efficiency have allowed the Ercros Group to obtain profit for four consecutive years. This profit has provided the Group with the necessary liquidity to meet its obligations. The Group's forecast for 2019 is that this situation will continue and therefore it is not expected that it will be exposed to liquidity risk in its transactions.

At December 31, 2018 the Group's available financing amounted to EUR 32,733 thousand (EUR 59,105 thousand at December 31, 2017). Additionally, if needed, the Group considers that it can use other supplementary mechanisms for obtaining occasional liquidity, such as the partial and selective disposal of assets not used in operations or the issue of short- and medium-term bonds in organized markets.

a) Major financing sources

In 2018 the Group has used the following financing sources:

(i) External

– The factoring facility in euros, which was renewed on October 27, 2017, allows the Group to fund working capital up to a limit of EUR 102,146 thousand, of which up to EUR 25,000 thousand can be non-recourse. At December 31, 2018 EUR 57,445 thousand have been drawn down from this facility (EUR 63,404 thousand in the prior year), of which EUR 15,665 thousand correspond to the non-recourse tranche (EUR 8,410 thousand in the prior year).

– The revolving credit agreement, for an overall limit of EUR 30,000 thousand, signed on December 14, 2017. At December 31, 2018, EUR 20,000 thousand have been drawn down (no amount had been drawn down yet in the prior year).

– The securitization facility whereby accounts receivable from customers are prepaid, with a limit of DOL 12,000 thousand —equal to EUR 11,380 thousand at the date it was arranged—, by virtue of the agreement reached with Finacity Corporation on May 9, 2016 for the 2016-2019 period. At December 31, 2018, EUR 5,655 thousand from this facility had been utilized (EUR 7,632 thousand in 2017).

– The three credit lines signed with the Catalan Institute of Finance ("ICF") for an overall amount of EUR 12,276 thousand in order to partially fund the change of technology in Vila-seca I factory. At December 31, 2018 these lines had been fully drawn down (EUR 10,033 thousand had been drawn down at December 31, 2017).

The Group expects that, just like it has happened until now, if new investment opportunities in production plants to meet its growth expectations arise, financing from suppliers or customers of favoured products may be available at market interest rates.

At December 31, 2018 the Group's available funding amounted to EUR 32,733 thousand.

(ii) Internal [see table in the consolidated cash flow statement in chapter 13.4]

– The free cash flow from the divisions' operating activities, which in 2018 amounted to EUR 44,520 thousand (EUR 43,813 thousand in 2017).

With the resources generated by the Group's activity, the amount released for the cancellation of deposits EUR 4,800 thousand (EUR 12,555 thousand EUR in the prior year) and the new loans taken out —for an amount of EUR 10,815 thousand (EUR 5,410 thousand in the prior year)— financial debts have been repaid and interest has been settled —for an aggregated amount of EUR 10,170 thousand (EUR 33,006 thousand in 2017)—; the investments made have been paid —for an amount of EUR 42,111 thousand (EUR 42,844 thousand in the prior year)— and shareholders have been remunerated through the payment of dividends, the meeting attendance bonus and the repurchase of treasury shares —for an amount of EUR 19,699 thousand (EUR 16,826 thousand in the prior year). As a result of the foregoing, the NFD amounts to EUR 107,307 thousand (EUR 2017: 89,257 thousand).

b) Limitations on the distribution of dividends

There are no restrictions on the distribution of dividends provided the three conditions established in the prevailing shareholder remuneration policy for the 2017-2020 period are met:

– Profit for the year/number of shares ratio is at least 0.10 euros/share.

– NFD/ordinary ebitda ratio (solvency ratio) is lower than or equal to 2.

– NFD/total equity ratio (leverage ratio) is lower than or equal to 0.5 [see chapter 10.1].

These three conditions were met at 2016, 2017 and 2018 year ends.

c) Level of indebtedness

As mentioned in chapter 3.1, NFD has increased by EUR 18,050 thousand and amounted to EUR 107,307 thousand at December 31, 2018 (EUR 89,257 thousand at 2017 year-end).

As said in subsection b) above, the shareholder remuneration policy establishes —among other conditions— limits related to the Group's level of indebtedness to be able to carry out the shareholder remuneration set for each year of the applicable period. In the case that the Group envisages the possibility of not meeting one of these ratios, the necessary measures will be adopted to reduce debt.

Considering the increasing payout established in the shareholder remuneration policy, payments derived from the provisions recorded, as well as the investments of the technological upgrade and capacity extension plan for the 2017-2020 period, the Group forecasts that the level of indebtedness will continue to increase in 2019. However, the limits imposed by the shareholder remuneration policy ratios will continue to be met.

d) Payment period to suppliers

The average payment period to suppliers was 55.4 days (49.1 days at 2017 year-end), which means an increase of 6.3 days between both years. This increase is due to the decision by the main suppliers that are paid within less than 30 days —in light of the solid financial position of the Group— to increase their payment periods, since the Group has reduced the payment period for the rest of suppliers.

At December 31, 2018, the payments that exceeded 60 days accounted for 43% of all payments made (34% in 2017). The Group forecasts that it will continue reducing the percentage of payments exceeding 60 days, in line with the two past years.

4.3. Capital resources

The Group has ten industrial premises located in several Spanish autonomous regions and supplies products to customers in 94 countries worldwide. Most of the Group's business is based on chlorine and its derivatives chemistry and is therefore subject to the usual cyclical nature of this industries, which alternate adjusted demand and supply periods (with high returns) with other periods with higher supply and/or lower demand, and therefore, lower returns, which makes it necessary to operate the plants at the highest utilization ratio possible for efficiency purposes.

Additionally, the main raw materials (methanol, ethylene, EDC) and utilities (electricity, steam) have considerable relevance to the Group's costs. Consequently, the cyclical fluctuations in prices also causes fluctuations in the Group's profitability as it is not always possible to pass on the increases, not even immediately. There are no appropriate financial instruments to cover these fluctuations.

The Group's activity is subject to regulatory changes, mainly of an environmental nature that require recurring investments to adapt to the new demands, as occurred recently with the prohibition using mercury-based technology for chlorine production.

The Group manages capital considering the characteristics of its business and is not subject to externally imposed capital requirements. The Group's objectives in capital management are:

- Follow a prudent financial policy, based on the stage and duration of the economic cycles.
- Maintain the capacity to perform transactions with a high level of solvency, in order to provide satisfactory returns to the shareholder and profit to other stakeholders, such as employees, customers, providers, etc.
- Comply with the shareholder remuneration policy [see chapter 10.1].

The Group measures and analyses these ratios periodically and estimates their projections. This is the key factor when determining the policy of investments, sale of investments to reduce debt, payment of dividends, returns of capital to its share capital and issue of new shares.

In order to manage its share capital, the Group uses the leverage and solvency ratios set forth in the shareholder remuneration policy [see section 4.2 b) above and chapter 10.1].

The Group measures and analyses these ratios periodically and estimates their projections. This is the key factor when determining the policy of investments, sale of investments to reduce debt, payment of dividends, returns of capital to its share capital and issue of new shares.

The Group is not subject to externally imposed capital requirements. The volume of capital is established based on the existing risks and make the corresponding adjustments to capital, based on the changes in economic conditions and the risks associated with the activity.

Between December 31, 2017 and 2018 total equity has increased by EUR 25,177 thousand (10.2%) from EUR 247,492 thousand to EUR 272,669 thousand. This increase is due to the profit for the year after discounting the resources allocated to shareholder remuneration amounting to EUR 19,699 thousand (EUR 16,826 thousand in 2017.

a) Firm commitments to obtain capital resources

There are no firm commitments to obtain new capital resources.

b) Investment commitments or obligations

The investment plan launched in 2016 has continued in 2018, although the most relevant actions initially included in the investment Act Plan, related to the change of technology in chlorine production, have already been carried out, as Ercros's board of directors identified the opportunity to benefit from the good performance of the caustic soda market, the chlorine derivatives and the polyols to approve the new capacity extensions. These are being carried out between 2016 and 2020, for a total forecast amount of EUR 100,000 thousand [see chapter 2.3].

Thus, over the prior year, investments amounting to EUR 31,586 thousand (EUR 52,991 thousand in 2017) were made, of which EUR 23,719 thousand (EUR 44,164 thousand in 2017) corresponded to actions for extending the production capacity and the other EUR 7,867 thousand correspond to other investments (EUR 8,827 thousand in 2017).

At December 31, 2018 there were investment commitments amounting to EUR 28,319 thousand (EUR 19,415 thousand in 2017). 60% corresponds to investments allocated to increase the production capacity of several plants (62% of the amount committed in 2017).

The Group plans to invest an annual average of EUR 40,000 thousand in the 2019-2020 period. After that, the volume of investments should be around EUR 18,000 thousand annually, provided that no new regulations are introduced that require exceptional investments.

These investments will be mainly funded with the resources generated by the Group and, also with non-current financing facilities within the framework of the industry aid programs carried out by the public administrations.

However, the local and regional administrations' requirements within the framework for the renewal of integrated environmental authorizations in the Group's factories may entail investments amounting to EUR 15,000 thousand over a five years period.

4.4. Contractual or out-of-balance obligations

The Group has not assumed any contractual or out-of-balance obligations that require significant financial resources.

5.1. Identification of risks

The Group has implemented a risk alert system called "SARE" that makes it possible to identify, monitor and quantify the potential risks it is exposed to. This alert system that is triggered whenever a risk that might affect the Group is identified.

The Group has the governance bodies necessary to supervise the development of the organization general strategy and carry out its duties with adequate efficiency, objectivity and independence. It also has procedures to identify, measure, assess, control and prioritize the risks it is exposed to, as well as management systems that define the control, follow-up and reduction or elimination of these risks.

Name of body	Description of duties
Board of directors	It establishes and supervises risk control systems in general
Audit committee	It is responsible for internal control and risk management systems
Internal audit department	It supervises the operation of internal control systems
Compliance committee	It supervises the prevention of criminal risks
Economic and financial committee	It supervises risks in general
Risk and collection committee	It is responsible for controlling trade receivables risk
IFRS [1] committee	It is responsible for the correct application of IAS [2] and IFRS [3] in the preparation of financial information and control of tax risks
ICFR [4] committee	It is responsible for the operation of ICFR
CEDES [5]	It supervises operating risks
CESR [6]	It supervises reputational risks

[1] International financial reporting standards.

[2] International accounting standards.

[3] International financial reporting standards.

[4] Internal control over financial reporting.

[5] Committee for sustainable growth.

[6] Committee for ethics and social responsibility.

5.2. Main risks for the Group

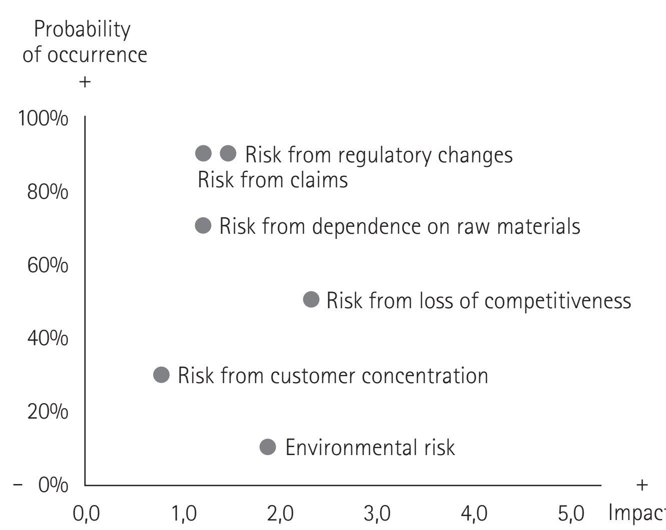
The Ercros Group's activity involves several kinds of risks, classified under the criteria that the Group considers most appropriate to manage them efficiently. In this regard, not all businesses entail the same risks, although sometimes they may share some of them. In general, the Ercros Group is exposed to financial and operating risks.

Many of these risks are inherent in the development of the activities carried out by the Group or derive from external factors. Thus, it can try to avoid them, but it is not possible to eliminate them completely.

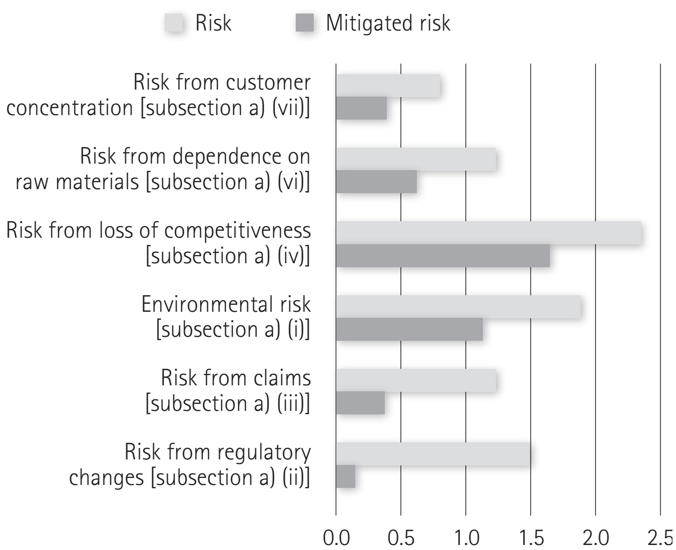
Relevant risks are those which may compromise the goals of the Group's business strategy, maintenance of financial flexibility and solvency.

The Group has prepared a risk map identifying the most relevant risks based on the probability of occurrence (on a scale of 0% to 100%) and the impact that their materialization would entail for the Group (on a scale of 0 to 6). Based on the risk map, the Group has implemented controls to mitigate the risks detected.

The following graph shows the relevant risk according to their probability of occurrence and impact, before the adoption of mitigating measures:



The graph below shows the impact of these risks after the application of mitigating factors:



Below we describe the main risks that may affect the Group by type:

a) Operational risks

In the development of its activities, the Group is exposed to the following operational risks:

(i) Environmental risk

Although all the Ercros Group factories have implemented environmental management systems to reduce the environmental impact derived from the industrial activity, these factories are subject to risks that may cause environmental damages, such as accidental emissions of harmful substances or fires.

The Ercros Group carries out official test controls on its management systems and develops its activity in line with emission limits provided in the applicable legislation, the corresponding authorizations and prevailing voluntary agreements. Additionally, the Group has implemented indexes to assess global emissions, to water and atmosphere, and generation of waste, in order to check the evolution of environmental management and periodically report on the reduction of emissions reached in its industrial activity.

In 2018 the environmental risk analysis for Tarragona and Cerdanyola factories and El Racó de la Pubilla dumpsite, in Flix, was conducted.

(ii) Risk from regulatory changes

In recent years, legal requirements have become more demanding and have caused significant changes in chemical sector in both the Europe and Spain and its autonomous communities.

The Ercros Group makes significant efforts in both human and material means to adapt to regulatory changes and carries out the necessary activities and actions to comply with legislation requirements, and in particular, with regulations on installations and people's safety, occupational health, environment protection, and transport, packaging and manipulation of dangerous goods.

Some of the standards, limits and procedures affecting the Group are currently being implemented and may be subject to future changes. The Group adapts to the new requirements within the established deadlines.

In 2018 the Group continued with the chlorine business restructuring process that was started last year as a result of the EU prohibition to use mercury in the electrolysis plants, and has completed and started new investments that supplement those already made in 2017. These investments aimed to restore the level of the Group's actual chlorine and caustic soda production to the level it had before the aforementioned plants closed down.

On November 21, 2017 the EU published the conclusions on the best available techniques ("BAT") for the large volume organic chemical industry ("LVOC") and the deadline —November 22, 2021— for making the required adaptations. In the case of the Ercros Group, the adoption of this decision will entail adaptations in the EDC and VCM production plants that are currently being studied, since the formaldehyde plants, which are also affected by these regulations, have already been adapted to the new requirements.

On June 9, 2016 the EU published the conclusions on BATs for the Common Waste Water and Waste Gas Treatment/Management Systems ("CWW"), which will entail conducting several actions, currently in progress, in all the Group's production centres, before June 10, 2020.

(iii) Risk from claims

The Ercros Group has a long history of industrial activity and it has always complied and come to terms with the legislation prevailing at any given moment. Nevertheless, the new legal requirements imposed in recent years and their strictness, which in some cases are applied retrospectively by the courts, have given rise to the risk of claims for equity liability to cover the costs of cleaning and decontamination of polluted land and environment, and compensation for professional illnesses.

The Ercros Group has submitted to the relevant authorities soil remediation and landscape regeneration projects for the plots of land affected. Provisions have been recorded for all environmental contamination claims for the amount that the Group considers that it is reasonably probable that they are administratively and legally acknowledged and, therefore, it may have to meet.

Law 5/2017 of March 28, 2017 introduces into the Catalan legislation the concept of historic contamination. For the Group, this law clarifies and determines the measures that the authorities may require for restoring the soil on which historic industrial sites are located in Catalonia.

Remediation works in progress

In connection with the Flix factory land, the actions set forth in the environmental adaptation plan submitted to the administration on February 28, 2017 have been carried out. The plan describes the measures for improving the quality of the soil and subterranean water of Flix factory, and the steps to be followed to eliminate potential mercury emissions after the close-down of the chlorine production plant on December 10, 2017. Over 2018, all the premises were emptied and cleaned up and it is expected that they will be dismantled in 2019.

Over the prior year, the Group continued with the soil characterization and decontamination works for Vila-seca I and Vila-Seca II factories. In Vila-Seca I, the works for cleaning and dismantling the cells that used mercury have started and a new deposit for storing it and subsequently transporting it to an authorized manager.

In Sabiñánigo and Monzón factories, the competent administration approved the plan for soil and subterranean water monitoring and control. Lastly, also with the approval by the administration, a pilot project was launched in Palos de la Frontera factory, which was sold in 2015. The purpose of this plan is to improve the quality of subterranean water in the land that are still owned by the Group in the premises.

On July 24, 2018, Ercros and Acuamed —following the requirement of the Provincial Court of Tarragona, section two— reached a transactional agreement that established EUR 11,331 thousand compensation to be paid by Ercros to Acuamed, in compliance with the Provincial Court of Tarragona's ruling, as the contribution to the cost for decontamination works on the Flix reservoir carried out by Acuamed. On November 2, the agreement was certified by the Provincial Court of Tarragona, declaring that Ercros's third-party liability derived from this lawsuit had extinguished and closing the legal proceedings.

In 2018 the Group continued restoring the Terrera Nova de Cardona dumpsite, whose saline waste extraction activity was discontinued in 2012, in accordance with the plan approved by the general management of Qualitat Ambiental i Canvi Climàtic ("DGQA") of Generalitat de Catalunya. The approval of the plan for the restoration of Terrera Vella submitted to the DGQA in 2017 is pending resolution.

On January 21, 2019 Ercros received two notifications from the general directorate of Environment and Mar Menor of the Region of Murcia declaring (i) the end of the proceedings for the voluntary soil remediation of El Hondón, where the old Cartagena factory was located; and (ii) the start of the proceedings for declaring this plot of land contaminated and declaring Ercros responsible in the first place for the necessary land decontamination and remediation works, as the party having caused the contamination and in the second place, the current owners of the land. If Ercros is declared the first party responsible for recovering El Hondón land for industrial use, this does not prevent Ercros from passing on these costs to the owners of the land. Therefore, based on the information available at the date this annual report was prepared —February 22, 2019—, Ercros does not consider it necessary to record any additional amount in the provisions already set aside.

Labour claims

Occasionally, the Group must face lawsuits lodged by former employees, or their heirs, related to damages for asbestos exposure and benefit surcharges due to lack of security measures in asbestos exposure. These type of liabilities are not attributable to the Group's current management, nor do they relate to damage caused to currently active employees, but they are liabilities claimed to Ercros as the universal successor of companies that became extinct many years ago and have no relation with current activity. On June 20 and September 21, 2018 Ercros reached settlement agreements in connection to three lawsuits that had been filed against it for asbestos exposure. Nine more lawsuits have been lodged for this reason that have not been settled yet. The Group has recorded provisions for the amounts that it may be liable for as a result of the lawsuits that have not been ruled on by the courts yet.

(iv) Risk from loss of competitiveness

The Ercros Group carries out its activity within a global environment that sees new competitors each year, who benefit from more lax regulations in their countries of origin, less strict environmental requirements in comparison with the European market, lower labour and energy costs and measures to encourage development. In these countries costs differential becomes a decisive competitive factor to set the products' final price. This situation is worsened by the fact that the main products of the Ercros Group are commodities, which are subject to a strong competition from the pressure of emerging markets such as India or China. These countries competition is one of the main risk factors for the intermediate chemicals and pharmaceuticals divisions.

The industrial transformation plan that China is carrying out over the 2016-2020 period for combating pollution resulted in the close-down, relocation or adaptation to the new environmental requirements of hazardous chemical product facilities in densely populated areas. This plan has temporarily improved the Group's competitiveness in this market.

The main raw material used by the chlorine derivatives division is electricity, which may account for 44% of production cost. This price is established based on the price awarded at daily electricity auctions held by Red Eléctrica de España ("REE"), to which regulated costs are added. Although the caustic soda market is of a European nature, electrical production cost is related to the Iberian market, and therefore, this is a component that affects the Group's competitiveness.

Unlike what happened until now, the increase in the cost of electricity in Spain in 2018 has occurred within a context of generalized increase in this utility in the main European countries, so the price paid by the Group and the price paid by its competitors have started to converge. This is a very relevant fact, since Europe is the natural market for the products from the electro-intensive plants.

Additionally, since 2008 the Group has been remunerated for the rendering of the interruptibility service to REE, which consist of the possibility that the latter company interrupts the power supply to the Group's electrolysis plants when there are electricity generation and demand situations that require so, among other reasons. Since 2015 the amount paid by REE for the interruptibility service had been established annually through an auction that took place prior to the start of the calendar year. In 2018 this amount was established through two auctions, one for the period comprised between January 1 and May 31, and the second one for the period comprised between June 1 and December 31. At the end of 2018 the auction for the first half of 2019 took place. In each of the auctions held, the price paid for the service has been gradually decreasing while the Group has offered lesser interruptible MWh, in line with the lower electrical consumption. Thus, between 2017 and 2018 the amount received by the Group for this service has been reduced by 45.8%.

In this environment, the Ercros Group focuses its strategy on improving productivity, reducing costs, increasing efficiency in operations, diversifying activity to include innovative products with greater added value.

Another factor that has traditionally made the Group lose competitiveness is the euro/dollar exchange rate, especially in products from the countries that operate with this currency in its trade transactions, basically the emerging economies. During 2018, the US dollar has depreciated against the euro by 4.5%, which has damaged the competitiveness of the European economy and of the products marketed by the Group, too. In 2019 a neutral effect of the US dollar is expected in comparison with 2018, and therefore, it is not expected that the profitability of the Group's will decrease for this reason.

Lastly, as a result of the phase-out of chlorine production using mercury-based technology in Europe in December 2017, the chlorine production capacity installed in Spain decreased by more than 60% and the number of local producers was reduced from seven to four. The Group had to close down two production plants but has made investments to reach by 2020 a similar level of chlorine and caustic soda production to that it had before the mercury-based technology plants were closed, extending the capacity of the plants that are already using membrane-based technology.

This has improved the competitive position of the Group in the Spanish market, which currently accounts for 62% of total chlorine production capacity installed in Spain. The Group is currently operating just through membrane-based technology plants —which have a better usage ratio, consume less electricity by chlorine production unit and have lower fixed costs— and means gaining competitiveness compared to the prior situation. However, the caustic soda market is of a European dimension and the Group hardly accounts for 2% of produced caustic soda.

(v) Risk from concentration and cyclical nature of products

Higher activity has generally been noted in the markets in which the Group operates during the second and third quarter of the year, except for the month of August. In recent years the customer's trend towards a reduction in orders at the end of the year has accentuated. This is related to the Christmas holidays and a generalized will to decrease stocks in warehouses at year end, which causes a reduction in activity in December.

The products that show a more acute seasonal trend are those used in wastewater treatment and water disinfection for human use —sodium hypochlorite, sodium chlorite and TCCA—, with a peak consumption in the summer, and PVC, which shows greater apathy in the colder months due to the halt in construction. The rest of the products show a stable demand across the year, except for the months of August and December.

61.7% of Ercros's activity hinges around the production of chlorine and its derivatives. Chlorine and caustic soda are manufactured in the same process, but whereas for safety, efficiency and application reasons all chlorine is consumed in the production centre itself in order to manufacture chlorine derivatives, caustic soda is traded at European level. The most significant product made from chlorine is PVC, the evolution of which is related to the construction sector. Consequently, the price of caustic soda (a co-product of chlorine) is volatile, complicating the projection of the Group's results.

After the availability of the chlorine and caustic soda produced by the Group decreased as a result of the close-down of the mercury-based technology electrolysis plants, and in light of the excellent evolution of the prices of caustic soda and PVC (main chlorine derivative), in 2018 in order to maintain its presence in both markets and, thus, the current level of service to customers —in particular caustic soda, sodium hypochlorite, hydrochloric acid and PVC customers—, the Group (i) has extended the chlorine production capacity of the plants using membrane-based technology; (ii) has adapted Sabiñánigo electrolysis plant so that it can produce both chlorine-caustic soda and chlorine-potash;

(iii) has increased the purchase of third-party caustic soda; (iv) has distributed the chlorine produced allocating a greater share to the most profitable uses; and (v) has increased the purchase of third-party EDC —which already incorporates chlorine and ethylene— for the production of PVC.

Thus, EDC becomes temporarily the most relevant raw material to the Group, while the importance of ethylene as raw material decreases. Additionally, the Group has increased its commercial profile since it does not produce a significant portion of the caustic soda it markets. Given that the price of some raw materials is linked to the price of the end products they are allocated, the Group reduces the cyclical nature of their margins in the PVC price in comparison with prior years, since part of the industrial margins have become trade margins, which are more stable.

(vi) Risk from dependence on raw materials

The Group has a strong foreign dependence on the raw materials it uses in its industrial processes, the prices of which are subject to cyclical variations and, on occasion, may not be available in the amounts required or in the right time frame.

The Ercros Group tries to reflect all these cost variations in the selling price of its products, but it cannot always fully achieve it or, in some cases, it needs time to do so.

The Group tries to mitigate this effect by adopting a strategy regarding suppliers that pursues: (i) stable supply of raw materials with higher volatility, and (ii) diversification of the number of suppliers of strategic procurements.

Also in order to reduce the impact on the business of the volatility in the prices of raw materials, the Group manages stock efficiently and tries to reach supply agreements with customers in which the selling prices of its main products are linked to the cost of raw materials, especially for those products in which raw materials bear significant weight.

The Group's three main procurements and utilities —methanol, electricity and ethylene— account for 42% of the total amount of consolidated purchases, and exceed 40% of total costs of the manufacturing processes of formaldehyde, chlorine and PVC, respectively.

Regarding electricity cost, the price of MWh consumed in the electrolysis plants is determined from the daily electricity auctions, which are highly influenced by the electrical generation mix at any given time, so the price decreases when the generation of electricity through renewable sources is high (wind or hydro powers) and increases when it is generated through fossil fuels. Additionally, as explained in item (iv), the Group's electro-intensive factories benefit from the interruptibility service remuneration that REE pays for interrupting power supply under certain conditions.

After the Spanish Government developed the main milestones in the energy market reform in recent years, in 2018 no new regulatory development in the energy market has taken place that has had a significant economic impact on the Group's activity, except regarding interruptibility, and certain temporary tax rebates in the electricity generation tax.

The Government published Royal Decree Law 20/2018, of December 7, establishing urgent measures for encouraging economic competitiveness in industry and trade in Spain, and implementing measures for supporting a fair transition to the electro-intensive industry, including the electro-intensive consumer bylaws which, at the date this annual report was published, was under regulatory development. The purpose of these bylaws is to implement mechanisms that make it possible to reduce energy costs for this type of consumers, among with the Group is included, and favour the decarbonisation of industry. The Group does not know the impact that this process may have on future electricity prices.

The gradual increase in the cost of electricity, commented in item (iv), is being partially mitigated by the decrease in consumption derived from the implementation of the membrane-based technology electrolysis plants —which is 30% more efficient in terms of electricity consumption— and other improvements in the polyol production process. In order to reduce the cost of this utility in the future and ensure it comes from renewable sources, the Group is currently exploring bilateral power purchase agreements for renewable energy.

In addition to electricity, the other raw material used in the chlorine and caustic soda production process is sodium chloride. Electrolysis plants using membrane-based technology require highly pure sodium chloride. Although sodium chloride is an abundant raw material, there is currently a limited number of producers in Europe that are able to supply sodium chloride that has the required electrolytic quality. In order to ensure the availability of this product, the Group has signed long-term agreements.

During 2018, the increase in the oil price has significantly pushed upwards the cost of methanol (+12.8%), which is the main raw material of the intermediate chemicals division, and the cost of natural gas (+7.3%) and ethylene (+6.6%). However, the decrease in the production of own EDC, which uses ethylene, chlorine and gas as consumables, as a result of the purchase of third-party EDC as a raw material, has allowed the Group to reduce, in addition to the bill, its level of dependence on these raw materials, although this has increased for EDC.

In general, the Ercros Group can pass on to its customers the fluctuations in methanol and ethylene prices, which are negotiated globally, which favours the maintenance of margins. It is not so in the case of local energies —mainly electricity—, and therefore, a significant rise in the price of these utilities affects the margin of final output and the Group's competitiveness and profit.

The close-down of several competitors in China, mentioned in item (iv) above, reduces the risk from loss of competitiveness of the products marketed by the Group worldwide, but it may increase the risk from dependence on raw materials in the event that the availability of the consumables that the Group purchases in this country should decrease —or price should rise.

(vii) Risk from customer concentration

Although no customer accounts for more than 10% of Ercros Group's turnover, the relevance of the company Covestro should be highlighted, as it consumes around 40% of the chlorine produced by the Group.

Ercros and Covestro signed a supply agreement for the 2017-2020 period. However, on December 11, 2017 this customer announced its intention of setting up a chlorine plant at the end of 2020 to meet the needs of its Tarragona factory. If the supply of chlorine to this customer does not continue as from 2021, the Group would reduce its external EDC purchases for production, and would increase its ethylene and own EDC purchases and, most probably, it would discontinue the production of dicalcium phosphate, which could affect the Group's profitability.

(viii) Commercial risk

The Group exports 47.3% of its sales to 93 countries. Given its exposure to the foreign market, sometimes the Group may be influenced by political and geostrategical conflict, which generates tensions in the markets where it commercializes its products.

During 2018, the worsening of the trade conflict between the USA and China has generated a change in the global flows of some products. This circumstance has damaged the Group, since some of the PVC that the USA sold to China has been diverted to the European market, which opted to purchase this product as it has a more competitive price.

Political uncertainty as a result of the social, economic and financial crisis in Turkey during the prior year resulted in a shortage of liquidity in US dollars in this market, which received 7.2% of the Company's exports. The Group has minimized risk exposure in this market by commercializing its products through distributing companies based in other destinations.

The current political instability in Venezuela has had no impact on the Group's income statement as it does not sell any products in this market.

Brexit

The Group does not expect that the UK's withdrawal from the EU will have a significant direct impact on its income statement as this is not a relevant market.

(ix) Tax risk

The Group tries to minimize the tax risk derived from its activities. For such purpose, it strives to scrupulously fulfil its tax obligations, trying not to make any decision based on aggressive or controversial interpretations of tax regulations. Nor does the Company plan its operations aimed at minimizing the tax charge through companies located outside Spain. The Ercros Group is advised by external tax experts in order to adjust to the tax regulations and take no risks due to regulatory interpretations.

Despite this, tax inspections occasionally use interpretative criteria of regulations applicable to the activities developed by the Group that give rise to discrepancies in the criteria used by it.

In this regard on July 5, 2017 Ercros submitted allegations to the Central Economic Administrative Court ("TEAC") due to disagreement with the final tax assessment derived from the inspection carried out for the exemption applied to the consumption of pure ethanol used in the production of medicines during 2011 and 2012 issued by the tax authorities, for an amount of EUR 5,300 thousand, of which EUR 4,488 thousand correspond to the tax liability and EUR 812 thousand to late payment interest. The Group has guaranteed, through the arrangement of a credit insurance, the payment derived from this assessment. Based on recent resolutions issued by TEAC and on the criterion expressed by the Directorate General of Taxation in inquiries made by the pharmaceutical industry, the Group expects a favourable ruling to the appeal lodged and, consequently, has not recorded any provision for the payable amount in relation to said inspection assessment.

Ercros has been inspected for VAT and withholdings and payments on account for the period comprised between February 2012 and December 2013, and for the income tax for the years 2011, 2012 and 2013. Additionally, the Company is open to inspection for the rest of taxes to which it is liable for the last four years. No significant liability has arisen from these inspections.

The Group's Directors and tax advisors consider that no significant tax contingencies would arise as a result of varying interpretations of the tax legislation applicable to the Group's transactions.

(x) Technological and cybersecurity risk

The Group is exposed to cybernetic risks that may cause an interruption of its business processes, which would temporarily jeopardize the normal operation of the Group.

In order to minimize the risk from discontinuity of business operations —due to failures or incidents in the IT systems— the Group has a specific protection plan in place for its technological infrastructures that is included in the operational security plan.

This plan also covers security against external and internal cybernetic threats —accidental or intended. The Group has the necessary means to prevent, detect or, where appropriate, eliminate the cause of these threats.

b) Financial risks

During the normal course of operations, the Group is under credit risk, market risk (interest rate risk and exchange rate risk) and liquidity risk.

The Group's main financial instruments, other than derivatives, include the syndicated factoring, the revolving credit agreement, the dollar receivable securitization program, loans with public financial institutions, banking loans, credit policies, financial leases, cash and short-term deposits.

The Group does not have in force any contract derived by the coverage of the interest rate risk or exchange rates.

The policy of the Group, maintained during the last years, is that of not negotiating with the financial instruments.

The Group notes that the financial risk has been reduced in the last three years due to the improvement of its operational results. The solvency ratio (net financial debt/ordinary ebitda) was 1.71 in 2018, far from the 2 that has been set as the maximum limit.

In 2018 the Group has maintained the investor plan that began in 2016 with the restructuring of the chlorine business, taking advantage of the good situation of the caustic soda markets, chlorine derivatives and polyols, in which it will invest around EUR 100,000 thousand between 2016 and 2020.

In this sense, the Group requested and obtained from the pool of banks that integrate the syndicated factoring a dispensation to be able to undertake investments above what they had initially authorized in the framework of the expansion of the productive capacity. By means of the authorization obtained, the Group could make investments up to a maximum of EUR 140,000 thousand during the period 2017-2019 and, consequently, take advantage of the opportunities of expansion of productive capacity that are presented.

The implementation of the plan of productive capacity expansion is causing, in a transitory way, an increase of the Group's indebtedness, in such a way that at the end of 2018 the net financial debt has risen to EUR 107,307 thousand (EUR 89,257 thousand in 2017), an increase of 20.2%.

Likewise, at the end of 2018, the financial solvency conditions were fulfilled to repay the shareholder provided in the shareholder remuneration policy from the benefits of the exercises 2017 until 2020 ratified by the annual general meeting held on June 23, 2017.

(i) Credit risk

The Group has established a customer credit management policy and the exposure to default risk is managed in the normal course of business. Solvency assessments are conducted in respect of relevant customers. Additionally, in certain sales the Group requires the customer to deliver a letter of credit or a bank guarantee.

The Group has arranged a credit insurance policy associated with the customers of the securitization program for accounts receivable in dollars.

The concentration of the Group’s customer portfolio is not high and shows low default rates.

For the remaining financial assets of the Group such as cash and cash equivalents, credits, and financial assets available for sale, the maximum exposure to credit risk is equivalent to the book value of these assets at year end.

(ii) Market risk

Interest rate risk

External financing is obtained through the syndicated factoring, the revolving factoring agreement, the securitization program for accounts receivable in dollars, and loans granted by public institutions. Financing accrues floating interest rates usually linked to Euribor. In this regard, since interest rates are very low —potential increases in Euribor— finance costs would be higher for the Group.

The table below shows an analysis of sensibility to possible reasonable changes in the interest rate. The remaining variables have remained stable:

	Increase/decrease in basis points of debt cost	Effect on profit/loss (EUR thousand)
2018:		
	200	-2,303
	100	-1,149
	-100	1,149
	-200	2,303
2017:		
	200	-1,963
	100	-981
	-100	981
	-200	1,963

Foreign currency risk

The only assets and liabilities exposed to exchange rate risk are those arising from purchases and sales of ordinary traffic. The Group does not have in its balance sheet other assets exposed to currency risk.

Specifically, on December 31, 2018, the Group has accounts receivable, amounting DOL 19,563 thousand; accounts payable, amounting DOL 13,698 thousand; treasury balances, amounting 2,774 thousand; and financing of accounts receivable in dollars with Finacity Corporation, amounting DOL 6,321 thousand. The net exposure, therefore, is debited on December 31, 2018 and amounts to DOL 2,318 thousand.

The dollar is, to a large extent, the main currency to which the Group is exposed, which has not contracted any derivative products to cover this risk.

In 2018 the average dollar exchange rate weakened towards the euro. In the case of the Group's consolidated sales, the average exchange rate went from 1,130 dollar/euro in 2017 to 1,181 dollar/euro in 2018 (a difference of 4.5%). The Group estimates that in 2019 the effect of the dollar will be neutral given that for the whole of the year its exchange rate will remain in line with the average of the last year.

The fact that the dollar loses value towards the euro has a negative effect for the Group in worsening the competitive position of the products it sells, which explains the decrease in sales in this currency in 2018 compared to 2017, at the same time that it damages the return to euros of sales in dollars, which goes to the detriment of profitability.

The 2018 dollar sales reached DOL 101,677 thousand (DOL 105,865 thousand a year earlier), a reduction of 4.0%. Sales in dollars in 2018 accounted for 12.8% of total consolidated sales (13.6% the previous year).

On the other hand, between 2017 and 2018, purchases in dollars increased significantly, from DOL 42,544 thousand to DOL 63,889 thousand. This increase, of 50.2%, is due, fundamentally, to the greater volume of EDC acquired, product that is paid with this currency. In 2018 purchases in dollars amounted to 12.4% of the total procurements and supplies satisfied by the Group (8.8% the previous year).

The sharp increase in purchases in dollars —and to a lesser extent lower sales in this currency— led to a reduction in the net exposure to the dollar —difference between the amount of sales and purchases made in this currency— of the Group, which reached DOL 37,788 thousand in 2018 compared to DOL 63,321 thousand in the previous year. In spite of this, the effect of the devaluation of the average exchange rate of the dollar on the Group's ebitda, calculated on the basis of the 2018 net exposure, was EUR 1,521 thousand.

The following table shows a sensitivity analysis to possible reasonable variations in the average dollar exchange rate, while maintaining all other constant variables for the net exposure to this currency according to the 2018 figures:

US dollar/euro relationship	Effect on profit/loss (EUR thousand)
1.30	-2,854
1.25	-1,691
1.20	-432
1.18	—
1.13	1,519
1.05	4,067
1.00	5,866

(iii) Liquidity risk

The strength of the main markets and the greater efficiency have allowed the Ercros Group to close four consecutive years with benefits. These benefits have contributed the liquidity necessary to meet their obligations on time. The forecast for 2019 is that this situation is maintained, so it is not expected that the Group can be exposed to a liquidity risk in its operations.

On November 27, 2017, Ercros renewed its syndicated factoring line, to the end of 2022, for the same amount it had contracted (EUR 102,146 thousand) and with an improvement in economic conditions. On December 14, 2017, he signed a revolving credit agreement, for a global limit of EUR 30,000 thousand in order to expand its available financing lines. The Company also subscribed two lines of credit with the Catalan Institute of Finance ("ICF"), for a total amount of EUR 8,000 thousand, to partially finance the change of technology in the factory of Vila-seca I.

Additionally, in the case of necessity, the Group considers that it could go to other complementary mechanisms for the precise obtaining of liquidity, such as the partial and selective sale of assets not affected by the operation or the issuance of short bonds or medium term in organized markets.

With regard to Law 15/2010, of July 5, which modifies Law 3/2004, of December 29, which establishes measures to combat delinquency in commercial operations, it is reported that on December 31, 2018, the average payment period for suppliers was 55.4 days (49.1 days at the end of 2017), which represents an increase of 6.3 days between the two years. This increase is the result of the decision of the main suppliers —in view of the sound financial situation of the Group— of extending the payment terms, since with the rest of suppliers the Group has made an effort to reduce the period of payments.

At December 31, 2018, payments exceeding 60 days accounted for 43% of all payments made (34% in 2017).

The Group expects that the cash generation from its current activity will allow 2019 to continue reducing the percentage of payments that exceed 60 days, in line with what has been achieved in the three previous years.

5.3. Risks materialized during the year

Risks materialized	Events that gave rise to them	Control systems
Risk from regulatory changes	Lawsuits for decontamination of land in El Hondón.	Measures aimed to not increase the already assumed obligations have been started.
Operational risk	Capacity extension of production plants.	The Group schedules these implementations to minimize impact on production.
Exposure to increase in raw material prices	Ongoing increase in the electricity and methanol prices.	In the case of electricity, implementation of more efficient technologies from an energetic perspective. In the case of methanol, contracts with customer that link increases in raw materials to end product.

6 Subsequent events

6.1. Purchase of treasury shares

As part of the repurchase policy for treasury shares, purchases made by the Group in 2019 —until February 22, 2019— amount to 420,344 shares.

6.2. Communications from the environmental authorities

On January 21, 2019, the Government of the Murcia Region informed Ercros the start of a declaration of contaminated soils in El Hondón (Cartagena). Ercros is not the owner of these lands but the cause of their contamination. This declaration, to prosper, means that Ercros is considered obliged in the first place to remediate these lands without prejudice to the subsequent repetition against the current owners of land.

7 Foreseeable evolution

The Group is moderately optimistic about 2019 because of the higher volume available of caustic soda and chlorine —in the chlorine derivatives division— and polyol and moulding compounds —in the intermediate chemicals division. Sales of sterile fosfomycin and trometamol to the US and South Korean markets are expected to increase in the pharmaceuticals division, after successfully completing in 2018 the inspections by the authorities and currently awaiting the corresponding certifications.

Although this increased production volume will presumably come with cheaper prices, the total contribution should be higher in 2019 than in 2018. However, close attention shall be paid to the downward trend in prices started in the second half of 2018, although they still are at historical highs, a situation that is expected to continue at least during the next two years, to the extent that economic growth continues in the Euro zone.

Additionally, the increased production of own products —which have significantly higher margins— will allow the Group to partially replace the purchases of third-party products that have been made to meet customer demand while the Group launched the new production capacities.

As for the prices of the main procurements, pressure on margins is expected to decrease, in line with the trend shown at the end of 2018 and first weeks of 2019. This reduction, however, does not apply to electricity, which in 2019 continues to register very high prices.

As for the exchange rate, the Group estimates that the dollar effect will be neutral in comparison with 2018.

However, the Group is not unaffected by the market uncertainties that generate variations in supply and demand for the products it commercializes, as well as in the cost of its main procurements, generating fluctuations in margins that may affect their sensibility cyclically and usually earlier and more intensely than in other industries because of the commodity nature of its products.

8 R&D activities

In the context of R&D in 2018 the Group completed the projects related to Generalitat de Catalunya's Nuclis aids, co-funded by the EU's European Regional Development Fund, within the 2014-2020 ERDF operational program for Catalonia, to develop the PLA premium bioplastic range under the ErcrosBio brand and study the use of new silver catalysts in the formaldehyde production process. The Centre for the Development of Industrial Technology ("CDTI") aid program for developing a bioplastic especially suitable for manufacturing packages also ended and the development of the new range of ErcrosGreen+ resins is still in progress.

In the prior year two new CDTI aids were approved, as well as one by the Institute for Diversification and Saving of Energy ("IDAE").

Thanks to the aids received it has been able to start new research lines —which are still being explored— in cooperation with several leading research centres such as Institut Català d'Investigació Química ("ICIQ"); Consejo Superior de Investigaciones Científicas ("CSIC"); the Citius program of Universitat Autònoma de Barcelona ("UAB"); Universidad Politécnica de Valencia ("UPV"); and Centre Català del Plastic ("CCP") of Universitat Politècnica de Catalunya ("UPC").

The Group has four R&D centres in Aranjuez, Monzón, Sabiñánigo and Tortosa that provide service to the pharmaceuticals, chlorine derivatives and intermediate chemicals divisions, and maintains the collaboration agreements with universities and technological centres.

Ercros has 16 patents on both products and manufacturing processes and is processing two more.

In 2018 innovation costs incurred amounted to EUR 5,983 thousand (EUR 6,036 thousand in 2017).

8.1. New products

The most relevant projects currently underway in 2017 related to the development of new products are as follows:

a) In the chlorine derivatives division:

- Micro-encapsulation tests on several additives —fragrances and colorants— in swimming-pool water treatment tablets.
- The study for obtaining several types of potassium salt and magnesium in order to give greater added value to the caustic potash production. This project has received a CDTI aid.
- The improvement in the performance of the ErcrosFlex range in some transformation parameters and the ongoing cooperation with potential customers in the soil sector.
- Tests for the use of PVC and its co-polymers in 3D printing.

b) In the intermediate chemicals division:

- The development of new resins in the ErcrosGreen+ range with emission levels that are as low as those in natural wood.
- The adaptation of almost all production of moulding compounds (90%) to the new high density quality, which offers substantial improvements in the manufacture of electrical and healthcare material.

c) In the pharmaceuticals division:

- The development in laboratory of a new active principle obtained by fermentation to create a liquid culture to design the extractive technique for the product and, thus, be able to define standard production conditions.
- The obtaining of other fermentation products of an antibiotic nature, which have passed production at laboratory and pilot plant levels, in both fermentation and extraction land.

8.2. Improvement in processes and new applications of existing products

Among the most relevant measures taken in already existing efficiency improvement processes and new product applications the following stand out:

– The program in the pilot plant to obtain chlorine and caustic soda through the zero-gap membrane-based technology has been extended to the study of the migration of the production of caustic potash to caustic soda and vice versa, and the trial of new work and operation procedures.

– The resolution of the issues in the VCM production process, which made it impossible to fully benefit from the optimization carried out in the PVC plant capacity.

– The industrial use of the new anode activations developed at the R&D level.

– The increase in the production and improvement in energetic efficiency in the process for obtaining polyols and moulding compounds.

– The development of an extraction process for fusidic acid that reduces the use of solvent. Work at laboratory and pilot plant level.

9 Acquisition and disposal of treasury shares

Over 2018 the Company paid EUR 13,956 thousand to purchase 3,576 thousand treasury shares, which means an average price of 3.9 euros/share. These treasury shares were purchased for redemption purposes, in compliance with the shareholder remuneration policy [see chapter 10.1].

Of these treasury shares acquired in 2018, 1,984 thousand shares were redeemed as part of the shareholder remuneration against 2017 profit for an amount of EUR 7,024 thousand. The remaining 1,592 shares, which were purchased on account of the shareholder remuneration against 2018 profit for an amount of EUR 6,932 thousand, are the treasury shares that the Company held at December 31, 2019 (1,119 thousand shares for an amount of EUR 3,001 thousand at 2017 year-end) and account for 1.5% of share capital (1% in 2017).

All treasury shares have been bought within the framework of several repurchase programs, at market price in accordance with the conditions regarding price and volume established in Commission Delegated Regulation (EU) No. 2016/1052 of March 8, 2016, and in the Company's internal code of conduct in the securities market. The company designated as the main manager is Solventis A.V., S.A.

Over 2018 the Company has completed the second and third repurchase programs and has started the fourth one, which on February 22, 2019, the date on which the board of directors authorized this annual report for issue, is still active. The first program was entirely developed in 2017.

The table below shows the programs carried out:

Program	Resolution by the AGM	Approval by the board of directors	Start date	End date	No. of shares acquired	Total amount (euros)	Nominal amount (euros)	Share capital (%)	Average price (euro/share)
First	06-10-16	06-10-16	01-20-17	03-27-17	3,106,860	8,999,804	932,058	2.723	2.897
Second	06-23-17	07-26-17	10-4-17	03-09-18	2,116,488	6,029,600	634,946	1.907	2.849
Third	06-23-17	02-23-18	03-12-18	07-09-18	1,439,610	5,970,403	431,883	1.309	4.147
Fourth	06-23-17	06-15-18	07-09-18	06-30-19	1,559,146 [1]	6,473,137 [1]	467,743 [1]	1.445 [1]	4.152 [1]

[1] Up to February 22, 2019.

10.1. Shareholder remuneration

a) Shareholder remuneration policy

On April 28, 2017 the board of directors approved the shareholder remuneration policy against the Group's consolidated profit for the years 2017-2020, which was subsequently ratified by the shareholders at the annual general meeting held on June 23.

Shareholder remuneration is carried out through the repurchase of treasury shares, which will subsequently be redeemed, and the payment of dividends.

According to this policy, the Company will remunerate the shareholder with a maximum payout of: 35% of 2017 consolidated profit; 40% of 2018 consolidated profit; 45% of 2019 consolidated profit; and 50% of 2020 consolidated profit.

The repurchase of shares is the preferred shareholder remuneration procedure, provided that it establishes a payment of a dividend of at least: 12% of 2017 consolidated profit; 14% of 2018 consolidated profit; 16% of 2019 consolidated profit; and 18% of consolidated 2020 profit.

This payout is conditional on (i) obtaining minimum consolidated earnings per share ("EPS") equal to 0.10 euros/share; and (ii) fulfilling the following ratios at each year end: net financial debt/ordinary ebitda ("solvency ratio") lower or equal to 2 and net financial debt/total equity ("leverage ratio") lower or equal to 0.5.

In 2018 these conditions were met since EPS were EUR 0.411 (EUR 0.396 in 2017), the solvency ratio was 1.71 (1.20 in 2017) and the leverage ratio was 0.39 (0.36 in 2017) [see section 10.2 c) below].

Ercros's dividend policy is defined within the shareholder remuneration policy. There are no restrictions on the payment of dividends other than meeting the aforementioned conditions.

b) Shareholder remuneration paid and proposed in 2018

(i) Against 2017 profit

On July 6, 2018 the Company paid a dividend of EUR 0.05 gross per share against 2017 profit. The total amount proposed —which means a 12.5% payout— amounted to EUR 5,549 thousand, although the amount finally paid, after discounting the treasury shares at that time, was EUR 5,372 thousand.

Also against 2017 the Company allocated EUR 10,025 thousand to the repurchase of treasury shares, which means a 22.5% payout.

In total, the Company paid 15,574 to remunerate the shareholders, which means a 35% payout of 2017 profit.

(ii) Against 2018 profit

As indicated in subsection a) above, since in 2018 the requirements established in the shareholder remuneration policy were met, the board of directors —at the meeting held on February 22, 2019— resolved to propose the shareholders in annual general meeting the payment of a dividend of EUR 0.06 gross per share, which means EUR 6,473 thousand and a 14.4% payout over the consolidated profit obtained by the Ercros Group in 2018. This percentage exceeds the minimum established for the distribution of the 2018 dividend in said policy (14%).

Additionally, in 2018 the Company repurchased 1,592 thousand treasury shares for redemption for an amount of EUR 6,932 thousand, which means a 15.4% payout on account. Subsequent to year end, the Company has continued to purchase treasury shares and will continue to do so for an amount of EUR 4,545 thousand, which means a total amount of EUR 11,477 thousand in order to complete a 25.6% payout and reach the overall maximum payout for 2018 set forth in the shareholder remuneration policy, which is 40%.

Additionally, in 2018 EUR 371 thousand were allocated (EUR 386 thousand in 2017) to the payment of a meeting attendance bonus to the shareholders that attended the annual general meeting.

10.2. Stock market information

a) Share capital

On July 24, 2018 the Barcelona Mercantile Registry filed a capital decrease in Ercros amounting to EUR 930,897, corresponding to the nominal amount of the 3,103 thousand treasury shares that the Company had purchased between October 4, 2017 and May 8, 2018 for redeeming them within the framework of the shareholder remuneration policy. The redemption of these shares reduced the number of shares by 2.8% and meant an overall payout of EUR 10,025 thousand for the Company [see section 10.1 b) above].

After this transaction and until the moment this annual report was approved —February 22, 2019—, Ercros's share capital amounts to EUR 32,363 thousand and is represented by 107,876 thousand ordinary shares with a nominal value of EUR 0.30 each.

The table below shows the evolution of Ercros's share capital between 2017 and 2018:

	Share capital (euros)	Number of shares
At 12-31-17	33,293,883.30	110,979,611
Capital reduction	-930,897	-3,102,990
At 12-31-18	32,362,986.30	107,876,621

b) Share evolution

2018 has been a bad year for equity securities worldwide. Despite this, Ercros has been one of the few companies in the Spanish market that was able to increase its share's quoted price (8.8%).

Ercros closed the prior year with a market capitalization of EUR 335,928 thousand (EUR 317,402 thousand in 2017). At December 31, 2018, Ercros share's quoted price rose to EUR 3.11 (2017: EUR 2.86).

Ercros share reached the highest quoted price on August 22 (EUR 5.57). The average quoted price was EUR 4.1 (2017: EUR 2.8).

Main share-related parameters

	12-31-18	12-31-17	12-31-16	12-31-15	12-31-14
Shares on the stock market	**107,876,621** [1]	**110,979,611** [2]	**114,086,471**	**114,086,471** [3]	**112,283,591** [4]
Capital value (EUR)	**335,927,797**	**317,401,687**	**209,919,106**	**70,277,266**	**44,127,451**
Traded shares:					
In the course of the year	128,748,505	186,848,681	130,902,035	92,905,410	63,727,976
Maximum in one day	3,814,986	3,618,126	4,700,641	5,918,106	1,484,483
Minimum in one day	92,124	111,569	24,004	16,737	9,790
Daily average	504,896	732,739	509,346	362,911	249,913
Traded volume (EUR):					
In the course of the year	526,361,941	536,068,883	187,864,193	55,992,629	31,356,127
Daily average	2,064,165	2,102,231	730,990	218,721	122,965
Share price (EUR):					
Highest	5.57	3.63	2.41	0.86	0.58
Lowest	2.66	1.83	0.44	0.39	0.37
Average	4.09	2.87	1.44	0.60	0.49
Last	3.11	2.86	1.84	0.62	0.39
Frequency rate (%)	**100**	**100**	**100**	**100**	**100**
Liquidity rate (%)	**119.35**	**168.36**	**114.74**	**81.43**	**56.76**

[1] Yearly average 2018= 109,610,895 shares.

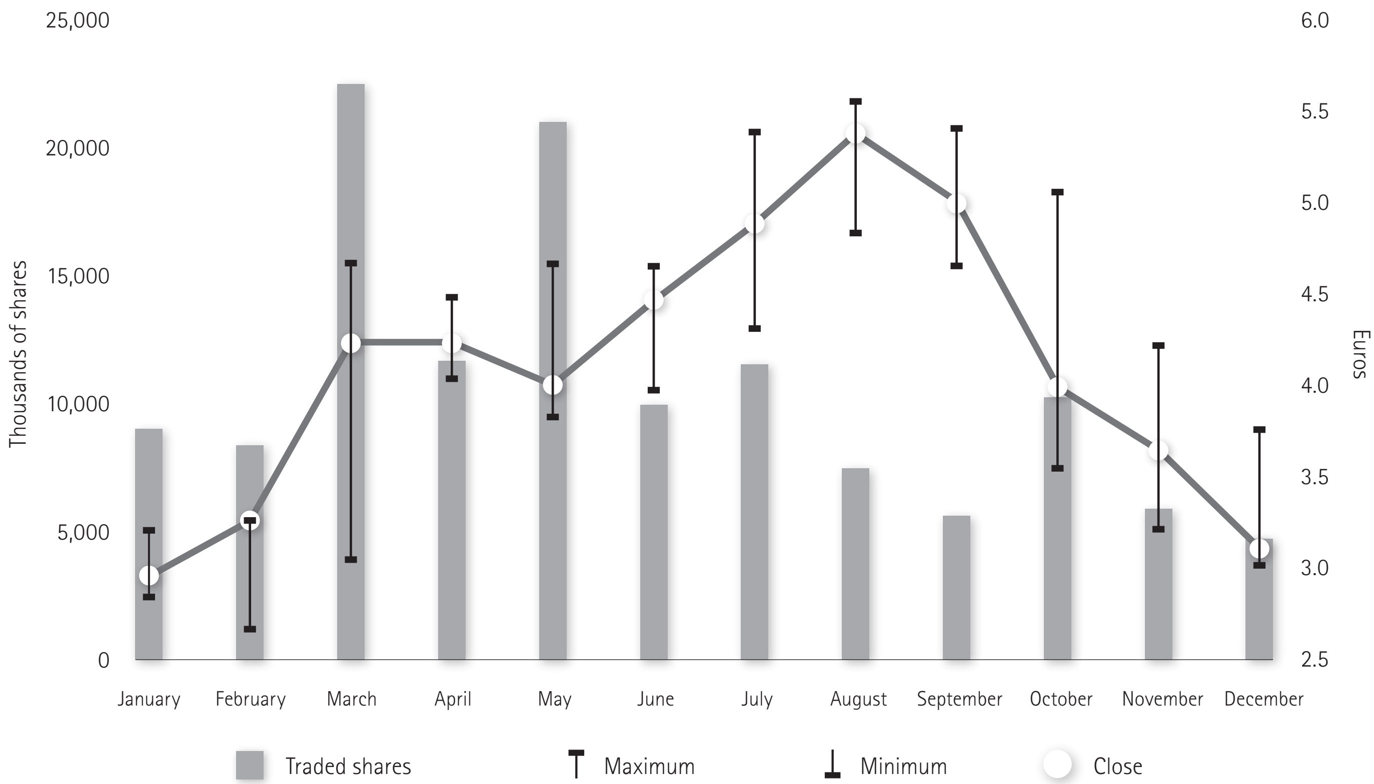
[2] Yearly average 2017= 112,801,167 shares.

[3] Yearly average 2015= 113,987,683 shares.

[4] Yearly average 2014= 110,175,394 shares.

Evolution of share and traded volume

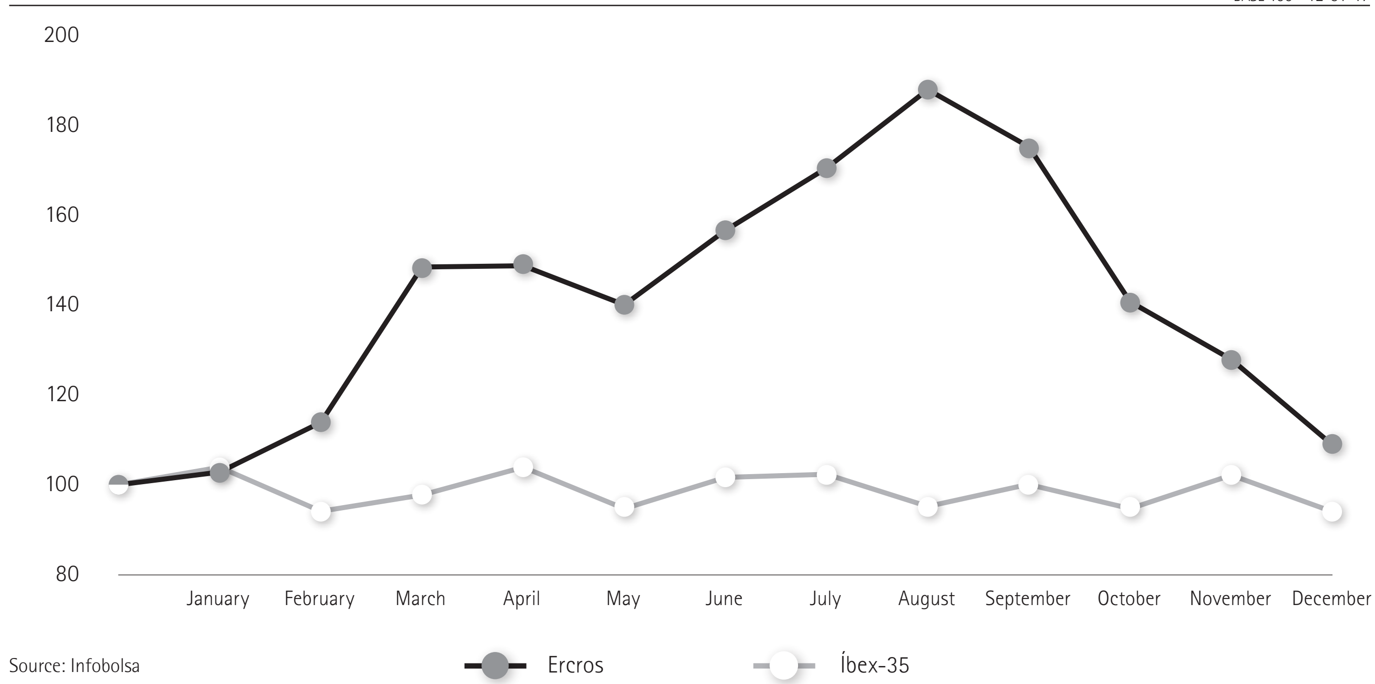
2018



Comparison between Ercros and Ibex-35

2018

BASE 100= 12-31-17



Source: Infobolsa

The overall volume of traded cash amounted to EUR 526,362 thousand (EUR 536,069 thousand in 2017) since the number of traded shares amounted to EUR 126,749 thousand (EUR 186,849 thousand in 2017), that is, 4.8 times the average number of Ercros shares available in the market in 2018.

The day on which the highest number of securities was traded was March 26, 2018 (3,814 thousand). The yearly average purchase was 504,896 securities.

In 2018 Ercros shares were the eighth most re-valued security in the Small Cap index of the continuous market of the Spanish stock exchange (the thirteenth in 2017). The upward evolution of Ercros is even more significant when compared to the drop in the main stock exchanges —Ibex-35, Madrid Stock Exchange index ("IGBM") by 15%, respectively, and Basic Industrial Materials and Construction index ("ICNS") by 8.6%.

c) Key stock market ratios

The improvement in quoted price and the reduction in the number of shares in share capital have pushed the key stock market ratios upwards [see subsections a) and b) above].

As a result of this last factor —together with the slight increase in 2018 profit—, EPS have improved from 0.396 euros/share in 2017 to 0.411 euros/share in 2018. This ratio is the profit/(loss) for the year divided by the weighted average price of outstanding shares considering the redemption of 3,103 thousand treasury shares and is used to measure earnings per share.

In 2018 PER —calculated by the number of times that market capitalization is included in profit/(loss) for the year— has remained stable compared to 2017 PER: from 7.13 times to 7.48.

Between 2017 and 2018 CFA —calculated operating cash flow divided by the number of shares— has increased from 0.39 to 0.41 (CFA is used to measure the generated cash flow corresponding to each share), whereas P/BV —market capitalization divided by total equity and relates the Company's value in the stock exchange to its underlying net carrying amount— which in 2018 was 1.28 and in 2017 was 1.23.

d) Significant shareholders

In 2018 the main development regarding Ercros significant shareholders is the increase in the ownership interest held by the American fund Dimensional Fund Advisors, LP and the entry of Montserrat García Pruns as a significant shareholder. The other shareholders have kept the same number of shares, although their interest in share capital has increased by 2.8% as a result of the reduction in share capital carried out [see subsection a) above].

According to the shareholder communications to the Spanish National Securities Market Commission ("CNMV" by its acronym in Spanish), at December 31, 2018 the shareholders that hold significant ownership interest own directly or indirectly 17,086 thousand shares in Ercros's share capital, which account for 15.84% therein, according to the following detail:

Name or corporate name of the shareholder	Number of direct voting rights	Number of indirect voting rights	% of total voting rights
Dimensional Fund Advisors	–	5,557,057 [1]	5.15
Joan Casas Galofré	4,578,000	–	4.24
Víctor Manuel Rodríguez Martín	3,633,577	–	3.37
Montserrat García Pruns	3,317,000	–	3.08

[1] It includes 3,329,569 direct voting rights of its subsidiary, DFA International Small Cap Value Portfolio, and thus, it is also a significant shareholder of Ercros.

The Company's estimated free float at December 31, 2018 is 82.69%, after discounting the treasury shares held by the Company.

Between December 31, 2017 and 2018, no change occurred in the number of Ercros shares held by the members of the board of directors, which was 100 in the case of Laureano Roldán Aguilar and 100,000 in the case of Antonio Zabalza Martí; however, due to the aforementioned capital decrease, the interest held by Mr. Zabalza Martí in the Company's share capital increased from 0.090% to 0.093%.

e) Credit rating

The Company is not aware of any credit rating for the Group.

10.3. Significant events in the current year

a) Capital reduction

See section 10.2 a) above.

b) Purchase of treasury shares

See chapter 9 and section 10.1 b) above.

c) Dividends paid

See section 10.1 above.

d) Ordinary shareholders' meeting

See chapter 2.1 a).

e) Capacity extensions in production

See chapters 2.2 a) and b).

f) Approval of the anti-corruption and crime prevention policy

See chapter 2.1 b).

11 Corporate governance report

The Ercros Group publishes an annual corporate governance report ("ACGR") in compliance with article 540 of the Spanish Corporate Enterprises Act. The ACGR is part of this annual report but is presented as a separate document as allowed by regulations.

The structure and content of this ACGR follows the model established in appendix I to Circular 5/2013 of June 12, modified by Circular 2/2018 of June 12, both issued by the Spanish National Securities Market Commission ("CNMV").

The ACGR provides information on the adopted corporate governance practices, including a description of the main characteristics of the risk management and internal control systems in place in connection with the financial reporting issuance process.

The ACGR of the Ercros Group for the year ended December 31, 2018 is available on Ercros's (www.ercros.es) and CNMV's (www.cnmv.es) websites.

12 Non-financial information statement

The Ercros Group publishes a non-financial information statement ("NFIS") in compliance with articles 44 of the Code of Commerce and 253 and 262 of the Spanish CEA. The NFIS is part of this annual report but is presented as a separate document as allowed by regulations.

The structure and content of the NFIS is in accordance with article 49 of the Code of Commerce, which has been modified by Law 11/2018 of December 28.

The NFIS is presented as part of the corporate social responsibility report ("CSRR"), which also explains the level of compliance with the 183 indicators in the guide to the application of the CSR in the chemical and life sciences industry, promoted by the Spanish Chemical Industry Federation ("Feique") in collaboration with Forética, which in turn sets out the indicators required for the certification of an ethic and socially responsible management system according to SGE 21:2008 standard.

Pursuant to article 49 of the Code of Commerce, the NFIS has been verified by the company Bureau Veritas.

The NFIS of the Ercros Group for the year ended December 31, 2018 is available on Ercros's (www.ercros.es) and CNMV's (www.cnmv.es) websites.

13

CONSOLIDATED FINANCIAL STATEMENTS OF THE ERCROS GROUP

13.1 Consolidated statement of financial position

EUR THOUSAND

Assets	12-31-18	12-31-17
Non-current assets	**367,081**	**350,446**
Property, plant and equipment	281,689	269,388
Investment property	37,588	37,588
Intangible assets	4,226	4,097
Investments accounted for using the equity method	6,840	6,428
Financial assets	5,038	7,014
Deferred tax assets	31,700	25,931
Current assets	**239,490**	**248,727**
Inventories	97,675	79,739
Trade and other receivables	98,656	123,040
Other current assets	14,971	20,297
Current income tax assets	12,343	2,908
Cash and cash equivalents	15,845	22,743
Total assets	**606,571**	**599,173**

EUR THOUSAND

Equity and liabilities	12-31-18	12-31-17
Equity	**272,669**	**247,492**
Equity attributable to owners of the controlling entity	272,669	247,492
Total liabilities	**333,902**	**351,681**
Non-current liabilities	**100,002**	**107,614**
Loans	48,393	46,258
Deferred tax liabilities	25,678	25,763
Provisions for environmental remediation	12,533	19,527
Other provisions	2,819	7,273
Employee benefits	1,798	1,302
Other liabilities	137	266
Accrued income and grants	8,644	7,225
Current liabilities	**233,900**	**244,067**
Loans	73,979	67,797
Current portion of non-current loans	9,858	11,823
Trade payables	107,655	118,654
Provisions for environmental remediation	16,580	12,993
Other provisions	8,304	9,767
Other liabilities	17,524	23,033
Total equity and liabilities	**606,571**	**599,173**

13.2 Consolidated statement of comprehensive income

EUR THOUSAND

	Year 2018	Year 2017
Income	**684,802**	**694,037**
Sale of goods	639,543	641,793
Rendering of services	32,397	39,677
Other operating income	8,364	7,787
Reversal of provisions for other liabilities	1,821	6,942
Changes in inventory of finished products and work in progress	2,677	-2,162
Expenses	**-621,896**	**-619,726**
Procurements	-341,780	-316,581
Utilities	-96,027	-114,389
Employee benefits expense	-79,870	-83,387
Other operating expenses	-97,865	-102,473
Charge to provisions for other liabilities	-6,354	-2,896
Ordinary gross operating profit ("ebitda")	**62,906**	**74,311**
Cost of mercury technology phase-out:		
Workforce reduction	–	-11,000
Dismantling and remediation	–	-10,732
Depreciation and amortization expenses	-19,694	-18,252
Operating profit ("ebit")	**43,212**	**34,327**
Finance income	142	151
Interest cost	-5,264	-5,774
Losses on disposal of financial assets at amortized cost	–	-235
Impairment losses on financial assets	-701	-89
Exchange gains (losses)	-521	-437
Share in the profit of associated companies	1,132	740
Profit before tax	**38,000**	**28,683**
Income tax	6,876	15,899
Profit for the year	**44,876**	**44,582**
Other comprehensive income (net of tax effect)	–	-90
Total comprehensive income for the year	**44,876**	**44,492**
Total comprehensive income attributable to:		
Equity holders of the parent	**44,876**	**44,492**
Profit per basic and diluted share (euros)	**0.4111**	**0.3963**

13.3 Consolidated statement of changes in total equity

EUR THOUSAND

	Share capital	Other reserves	Treasury shares acquired	Retained earnings	Equity
Balance at 12-31-16	**34,226**	**140,435**	**–**	**45,165**	**219,826**
Transfer of 2016 retained earnings	–	40,726	–	-40,726	–
Dividends	–	–	–	-4,439	-4,439
2017 comprehensive income	–	–	–	44,492	44,492
Transactions with shareholders and owners:					
Meeting attendance bonus	–	-386	–	–	-386
Purchase of treasury shares	–	–	-12,001	–	-12,001
Redemption of treasury shares	-932	-8,068	9,000	–	–
Balance at 12-31-17	**33,294**	**172,707**	**-3,001**	**44,492**	**247,492**
Transfer of 2017 retained earnings	–	39,120	–	-39,120	–
Dividends	–	–	–	-5,372	-5,372
2018 comprehensive income	–	–	–	44,876	44,876
Transactions with shareholders and owners:					
Meeting attendance bonus	–	-371	–	–	-371
Purchase of treasury shares	–	–	-13,956	–	-13,956
Redemption of treasury shares	-931	-9,094	10,025	–	–
Balance at 12-31-18	**32,363**	**202,362**	**-6,932**	**44,876**	**272,669**

13.4 Consolidated cash flow statement

EUR THOUSAND

	Year 2018	Year 2017
A) Cash flows from operating activities (1)	**44,520**	**43,813**
1. Operating activities	**44,520**	**43,813**
Customer collections	769,315	735,622
Proceeds from the net variation in the non-recourse tranche of the factoring facility	7,255	8,410
Payments to suppliers	-626,615	-606,593
Proceeds from/payments on VAT returns	1,367	7,932
Payments to and on account of ordinary employees	-76,294	-82,713
Payments to and on account of retired employees on the payroll and collective dismissal	-5,107	-3,841
Payments against provisions for environmental remediation	-7,727	-2,586
Payments against other provisions	-1,633	-761
Other operating proceeds/payments	678	311
Interest paid	-4,838	-5,607
Interest received	131	114
Payments on/proceeds from net exchange gains (losses)	-541	-229
Dividends received	720	960
Proceeds from prior years' income tax refund	–	4,400
Payment on account of the income tax for the year	-8,306	-7,915
Payments of local and other taxes	-3,885	-3,691
B) Cash flows from investing activities (2+3)	**-42,111**	**-42,275**
2. Payments on investments	**-42,111**	**-42,844**
Acquisition of intangible assets	-540	-151
Purchase of property, plant, and equipment:		
Investments in capacity extension	-32,330	-33,136
Other investments	-9,241	-9,557
3. Proceeds from disposals	**–**	**569**
Disposal of investment property	–	569
C) Cash flows from financing activities (4+5)	**-9,416**	**-26,260**
4. Proceeds from and payments on equity instruments	**-19,699**	**-16,826**
Purchase of treasury shares	-13,956	-12,001
Payment of meeting attendance bonus	-371	-386
Dividends paid	-5,372	-4,439
5. Proceeds from and payments of financial instruments	**10,283**	**-9,434**
Amounts drawn down on non-current loans	10,815	5,410
Repayment and redemption of non-current loans	-10,868	-12,491
Net variation of current revolving lines	5,536	-14,908
Cancellation of deposits	5,457	14,213
Constitution of deposits	-657	-1,658
D) Net increase/decrease in cash and cash equivalents	**-7,007**	**-24,722**
Cash and cash equivalents at the beginning of the period	22,743	48,265
Effect of foreign exchange rate	109	-800
Cash and cash equivalents at the end of the period	15,845	22,743

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HISTORICAL DATA SERIES

14.1 Consolidated statement of financial position

EUR THOUSAND

Assets	12-31-18	12-31-17	12-31-16	12-31-15	12-31-14
Non-current assets	**367,081**	**350,446**	**305,620**	**284,711**	**292,568**
Property, plant and equipment	281,689	269,388	249,231	235,296	245,695
Other non-current assets	85,392	81,058	56,389	49,415	46,873
Current assets	**239,490**	**248,727**	**254,561**	**226,956**	**228,155**
Inventories	97,675	79,739	72,009	57,854	55,529
Trade and other receivables	98,656	123,040	102,135	113,496	116,200
Other current assets and cash	43,159	45,948	80,417	55,606	54,626
Non-current assets held for sale	–	–	–	–	1,800
Total assets	**606,571**	**599,173**	**560,181**	**511,667**	**520,723**

Equity and liabilities					
Equity	**272,669**	**247,492**	**219,826**	**175,878**	**168,190**
Non-current liabilities	**100,002**	**107,614**	**124,298**	**104,496**	**100,272**
Long term loans	48,393	46,258	58,811	42,772	42,330
Long term provisions	17,150	28,102	35,080	30,789	25,920
Deferred taxes and other non-current liabilities	34,459	33,254	30,407	30,935	32,022
Current liabilities	**233,900**	**244,067**	**216,057**	**231,293**	**252,261**
Short term loans	83,837	79,620	89,341	98,375	106,350
Commercial accounts payable and other accounts payable	107,655	118,654	106,855	115,548	130,070
Provisions and other current liabilities	42,408	45,793	19,861	17,370	15,841
Total equity and liabilities	**606,571**	**599,173**	**560,181**	**511,667**	**520,723**

14.2 Consolidated statement of comprehensive income

EUR THOUSAND

Items	Year 2018	Year 2017	Year 2016	Year 2015	Year 2014
Income	**684,802**	**694,037**	**619,589**	**627,213**	**606,804**
Turnover	671,940	681,470	602,543	618,275	603,676
Other operating income and changes in inventories	12,862	12,567	17,046	8,938	3,128
Expenses	**–621,896**	**–619,726**	**–561,159**	**–594,589**	**–592,362**
Procurements	-341,780	-316,581	-270,215	-301,213	-311,038
Personnel expenses	-79,870	-83,387	-81,822	-79,863	-78,809
Other expenses	-200,246	-219,758	-209,122	-213,513	-202,515
Ebitda	**62,906**	**74,311**	**58,430**	**32,624**	**14,442**
Amortizations	-19,694	-18,252	-19,371	-19,874	-18,889
Profit/loss from asset impairment	—	—	11,990	—	-560
Cost of mercury technology phase-out	—	-21,732	—	—	—
Ebit	**43,212**	**34,327**	**51,049**	**12,750**	**–5,007**
Financial results	-5,212	-5,644	-5,727	-6,001	-7,501
Profit/loss before tax	**38,000**	**28,683**	**45,322**	**6,749**	**–12,508**
Profit/loss for the year from discontinued operations	—	—	—	—	815
Income taxes and non-controlling interests	6,876	15,899	-157	478	5,401
Other comprehensive result	—	-90	—	—	—
Profit/loss of the year	**44,876**	**44,492**	**45,165**	**7,227**	**–6,292**

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