

ANNUAL
REPORT

2019





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This annual report includes the management report and the most relevant tables of the annual accounts of the consolidated Ercros Group, corresponding to the year ended on 31 December 2019, which were approved unanimously by the board of directors on 21 February 2020, following a favourable report from the audit committee meeting on the same day.

Contents

1	Letter from the Chairman	3
2	Group position	5
3	Business evolution and results	10
4	Liquidity and capital resources	18
5	Main risks and uncertainties	23
6	Subsequent events	32
7	Foreseeable evolution	33
8	R&D activities	34
9	Acquisition and disposal of treasury shares	36
10	Other relevant information	37
11	Corporate governance report	43
12	Non-financial information statement	43
13	Consolidated financial statements of the Ercros Group	45
13.1	Consolidated statement of financial position	46
13.2	Consolidated statement of comprehensive income	48
13.3	Consolidated statement of changes in total equity	49
13.4	Consolidated cash flow statement	50
14	Historical data series	51
14.1	Consolidated statement of financial position	52
14.2	Consolidated statement of comprehensive income	53

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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.

Dear Shareholders,

In 2019 the Ercros Group's ebitda stood at EUR 61 million and its profit amounted to EUR 31 million. Both results are lower than those of the previous year; however, it should be borne in mind that the Group's activity was affected by the continuation of the downward phase of the chemical cycle, which began in the second half of 2018 resulting from the slowdown in industrial activity in the developed world.

One consequence of this slowdown was that the prices of most raw materials began to drop, which in turn effected the price of the final products, which were already under pressure from weak demand and abundant supply. Despite this, our Group managed to close the year with moderate growth in income, thanks to the 14.4% increase in the volume of products sold, following the start-up of new production capacity in the chlorine-caustic soda plants and other products with growing demand, such as tablets for treating swimming pool water, polyols and some active pharmaceutical ingredients.

With these investments, we have practically completed all the actions envisaged in the 2016-2020 Act Plan, with an outlay in the order of EUR 100 million. Initially, this plan was designed to deal with the technological change resulting from the European ban on producing chlorine-caustic soda with mercury technology; however, it was subsequently expanded with actions to modernise and improve the energy efficiency of our industrial facilities and to increase the manufacturing capacity of the aforementioned products.

Another relevant fact regarding 2019 that is important to note is that, despite the lower results and the increase in expenditure on investments and provisions, we managed to significantly increase the free cash flow, which amounted to EUR 28 million compared to EUR 7 million in 2018. This increase was mainly possible thanks to the high ebitda obtained and the management of working capital. The generation of these resources allowed us to reduce net financial debt by more than EUR 16 million and to remunerate shareholders with EUR 11 million.

The results for 2019 were very stable throughout the year and from the third quarter exceeded those of 2018. On the other hand, ebitda in the second half of 2019 was also EUR 1.5 million higher than in the first half. This is exceptional since, traditionally, for seasonal reasons, results tend to be lower in the second half of the year than in the first half.

Thanks to the improvement experienced in the second half of last year, the Group met the conditions established for shareholder remuneration. Therefore, if approved by the general meeting, we will pay a dividend of EUR 0.05 per share. Similarly, we have launched a new programme to repurchase shares to be retired, with the aim of meeting the commitment to allocate 45% of the profit for 2019 to shareholder remuneration.

The Ercros' board continues to have a gender balance. In fact, we stand out among Spanish listed companies in terms of the presence and role of women on our board. However, women represent 16.5% of the Group's workforce, which is insufficient. Although it is increasing steadily each year, it is doing so too slowly. To drive the process and achieve the gender equality objectives in the medium term, we are carrying out informational and awareness-raising activities.

In relation to sustainability, we continue working towards our goal of achieving CO₂ neutrality by 2050 and contributing to the fight against climate change. As a first step, we have set targets for 2030 that, with respect to 2015, entail reducing direct and indirect emissions by 25%, energy consumption by 20% and water consumption by 30%. Likewise, we want 1% of energy consumption to be produced from renewable sources within our own facilities, 70% of electrical energy consumed to come from renewable sources and 90% of consumption to be energy certified.

It is also worth noting the results achieved during the year in relation to prevention and occupational safety, specifically a 36% reduction in accidents among internal and external staff, the lowest in the last 10 years. However, absenteeism due to common illness increased by 13% year-on-year, a fact that concerns us and that we are working on.

The forecast for this year is becoming very complicated by the major uncertainty caused by the spread of covid-19 and its impact on the world economy. To prepare our staff and help stop the spread of the virus, we at the Ercros Group are taking the appropriate measures, in accordance with the recommendations of health and industry authorities.

Without considering the potential effects of this crisis, it is our expectation that our business's performance in 2020 will not vary significantly from that of 2019. All the forecasts of the specialist publications indicate that the prices of final products will remain at levels similar to those of last year. In view of the difficulty of obtaining better prices, we are focusing our commercial strategy on maintaining the sales volume and concentrating our activity on the applications and countries with the best return.

On the expenditure side, a very significant reduction in the price of electricity and oil has been observed so far this year, which is an indicator that our suppliers will have difficulty increasing the price of raw materials. To the contrary, we believe that such prices are likely to fall. This should potentially improve margins over the course of 2020 and have a positive impact on the income statement.

Antonio Zabalza Martí
Chairman and CEO of Ercros

Barcelona, 21 February 2020

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) General meeting of shareholders

On June 14, 2019 the Company held its shareholders' 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 approval of the non-financial information statement pursuant to Law 11/2018 of December 28. The non-financial information statement extends the corporate social responsibility report that Ercros included as an informative point in the agenda of the shareholders' meeting and that was not put to the vote [see chapter 12].
- The approval of the renewal of the directors' remuneration policy for the 2020-2022 period, as the old policy, approved by the meeting in 2016 for the 2017-2019 period, expired. The current policy maintains the same structure and criteria as the old one.
- A payment of dividends amounting to EUR 6,473 thousand, equal to EUR 0.06 gross per share, which means a payout of 14.5% of the Ercros Group's 2018 consolidated profit [see chapter 10.1 b) (ii)].
- A capital decrease amounting to EUR 888,240, through the redemption of the 2,961 thousand treasury shares that the Company held, which represent 2.7% of share capital, and which were acquired in the framework of the treasury share repurchase program, with an acquisition cost of EUR 11,477 thousand, which accounts for a payout equal to 25.7% of the consolidated profit obtained in 2018 [see chapters 9 and 10.2 a)].

The shareholders in the ordinary general meeting approved all the proposals for agreements included in the agenda. In attendance at the meeting were 7,315 shareholders of 78,974 thousand shares, representing 73.2% of the subscribed voting capital, of which 20.4% was present and the remaining 52.8% was represented.

The Company paid a premium of EUR 0.005 per share to the shareholders that attended said meeting.

b) The board of directors

The composition of Ercros's board of directors has not changed over 2019 and it consists of the following members:

- Chairman and executive director: Antonio Zabalza Martí.
- Independent directors: Lourdes Vega Fernández and Carme Moragues Josa.
- Board members classified as "Other external directors": Laureano Roldán Aguilar and Eduardo Sánchez Morrondo.

The non-board member secretary is Mr. Daniel Ripley Soria.

In 2019 the board held six meetings that were personally attended by all the directors.

At the meeting held on December 19, 2019, the board of directors evaluated the quality and efficiency of the functioning of the board, the audit committee and the appointments and remuneration committee, as well as the performance of the Company's CEO and board members. Also at that meeting, the board approved the criminal risk prevention handbook and the criminal compliance policy.

(i) The audit committee

The composition of the audit committee, which has not changed over 2019, is as follows:

- Chairwoman: Carme Moragues Josa, independent director.
- Board members: Lourdes Vega Fernández, independent director, and Laureano Roldán Aguilar, a director belonging to the "Other external directors" category.

The secretary of the audit committee is Mr. Josep Rovira Pujals, who is also the administration director of Ercros.

Over 2019 the audit committee held six meetings, five of which were attended by all its members, and in the other one one director was absent.

On February 22, 2019 the audit committee regulations were approved in accordance with technical guide 3/2017 on audit committees of public interest entities approved by the CNMV on June 27, 2017.

The internal audit department, which is led by Xavier Álvarez García, and the compliance committee, which is composed of Xavier 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 2019, which is composed of:

- Chairwoman: Lourdes Vega Fernández, independent director.
- Board members: Carme Moragues Josa, independent director, and Eduardo Sánchez Morrondo, a director belonging to the "Other external directors" category.

The secretary of this committee is Mr. Joaquín Sanmartín Muñiz, who is also the human resources director of Ercros.

In 2019 the committee held two meetings attended by all its members.

On April 25, 2019 the appointments and remuneration committee regulations were approved in accordance with technical guide 1/2019 on appointments and remuneration committees approved by the CNMV on February 20, 2019.

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 general manager of the business, the CFO and the manager of the General Secretariat. This body meets once a fortnight and when the situation requires so.

No changes in Ecofin occurred over 2019.

d) The management committee

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

It consists of the CEO, two 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, such as the sales directors of the main activities.

No changes occurred in the management committee in 2019 and it met 11 times.

Composition of the board of directors at 12-31-19

Board member	Position	Category	Committees	Latest appointment
Antonio Zabalza Martí	Chairman and CEO	Executive	–	6-10-16
Carme Moragues Josa	Coordinating director	Independent	Audit and Appointments and Remuneration	3-21-17
Lourdes Vega Fernández	Proxy coordinating director	Independent	Audit and Appointments and Remuneration	6-10-16
Laureano Roldán Aguilar	Board member	Other external board members	Audit	6-10-16
Eduardo Sánchez Morrondo	Board member	Other external board members	Appointments and Remuneration	6-10-16
Daniel Ripley Soria	Secretary, non-board member			

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, 2019, the Group had 10 production centres, all of them located in Spain. In the current year, there were no significant changes to the Group's industrial structure.

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 EDC Hydrochloric acid PVC Sodium chlorate Sodium chlorite Sodium hypochlorite TCCA VCM	Chemical industry Industry in general Derivatives manufacturing VCM manufacturing Industry in general Construction Paper pulp bleaching Water treatment Water treatment Swimming-pool water PVC manufacturing
Intermediate chemicals	Almussafes, Cerdanyola and Tortosa	Glues and resins Formaldehyde Moulding compounds Paraformaldehyde Pentaerythritol Sodium formate	Wood industry Derivatives manufacturing Sanitary equipment and electrical material Resins Paints Tanning industry
Pharmaceuticals	Aranjuez	Erythromycin Fusidic acid Phosphomycin	Antibiotics Skin infections Antibiotics

2.3. Operation

a) Mission and principles

The general purpose of the Ercros Group is to consolidated as a solid and long-lasting industrial group that contributes in a sustainable manner 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 four core principles: (i) maximum security for its employees, neighbours and installations; (ii) sustainability; (iii) satisfying the needs of its customers; and (iv) 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, sustainable and environmentally 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.

c) Industrial upgrade plan and extension of production capacity

In 2019 the Group has continued upgrading and extending its facilities in accordance with Plan Act.

Plan Act was initially designed to deal with the technological change derived from the EU prohibition to produce chlorine using mercury-based technology. It was subsequently extended and measures were adopted to upgrade and improve the energy efficiency of the Group's industrial park and to increase the manufacturing capacity of the most in-demand and best-selling products. After the implementation of these measures, the plan will entail investment of around EUR 100,000 thousand in the 2016-2020 period. This plan is currently at a very advanced stage of completion and goes according to schedule.

The following capacity extensions became operational during 2019:

- The process for launching the capacity extension of polyol production plants (pentaerythritol, dipentaerythritol and sodium formate) in the Tortosa factory. The overall capacity of the first two plants (pentaerythritol, dipentaerythritol) has increased by 5,000 t/year up to a total capacity of 35,000 t/year, whereas in the sodium formate plant capacity has increased by 3,000 t/year up to 23,000 t/year.
- The third capacity extension of the chlorine and caustic soda production plant at Vila-seca I factory was completed in October with the start-up of the new 26,000 t/year electrolyzer, which places Ercros' total chlorine production capacity at 217,000 t/year (172,000 t/year at Vila-seca I factory and 45,000 t/year at Sabiñánigo factory). This has allowed the Group to reach an actual chlorine and caustic soda production similar to the 2017 levels, which was the last year that the production plants using mercury-based technology were operational.
- The extension of 6,000 t/year in the TCCA plant at Sabiñánigo factory became operational in December. As a result of this extension, the Group's TCCA nominal production capacity will reach 28,000 t/year.
- The construction of the new finished products warehouse at Aranjuez factory, with a capacity of around 150,000 kg, was also completed in December.

The higher volume of products available after the aforementioned extensions has consolidated the Group's present in the markets in which it operates, has improved its market share therein and has also allowed it to open new markets. Additionally, these measures entail technological developments in the production processes and greater energy efficiency, thus improving the Group's competitive position.

d) 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 fixed relation of 1 ton of chlorine per 1.12 tons 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 profitability from the different chlorine applications; and (ii) in the cost side, on the one hand, by the price of energy power at any given time, which accounts for around 45% of ECU production costs and, on the other, by the cost of the raw materials consumed in the production of chlorine derivatives. In 2019 approximately 60% of the chlorine produced by the Group has been 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 a customer.

The challenge for the chlorine derivatives division in the short term is to optimize the capacity extension of electrolysis plants by increasing the sales volume of caustic soda and chlorine derivatives; all this within a context of higher supply in the market and weakened demand from the main application sectors and, consequently, general decrease in prices. In the medium term, the challenge is how to deal with the end of the chlorine customer contract without it affecting the business profitability. And in the long term, the challenge is to assume the costs derived from the objectives of the decarbonisation of industry and to increase the weight of higher added value products and expanding markets.

Formaldehyde is the key product of the intermediate chemical division, and methanol its main raw material. This consumable accounts for around 30% of the division's variable expenses. 79% of formaldehyde produced by the Group is used in the manufacture of liquid as well as solid derivatives. These (paraformaldehyde, polyol, moulding compounds), which account for 67% of the business's revenue, have greater added value than the liquids and its market is global.

The challenge for this business for 2020, in an adverse economic environment, is to improve product margins and consolidate its position in certain geographical areas. In the medium term, the challenge for the intermediate chemicals division is to consolidate the launch of new resin range (ErcrosGreen+ and Ercros Tech) with better environmental and technological features. And in the long term, the challenge for 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.

The pharmaceuticals division focuses on the production of raw materials and APIs ("Active Pharmaceutical Ingredients"), generic products, mainly from the family of antibiotics. The division also specializes in the production of active and intermediate principles for third parties, specially tailored for the customers. The main value of this business is its global leadership, in terms of both its command of fermentation and its capacity to obtain sterile products. The importance of external markets in the business causes both its sales volumes and margins to be influenced by the dollar/euro exchange rate.

The challenge for this business in the short term is to make the higher production capacity of sterile products profitable by incorporating new products and opening new markets for sterile phosphomycin and to achieve a better use of the fermentation capacity installed by increasing the volume of sales of fusidic acid, within a context of pressure on margins due to the increase in the prices of key raw materials. In the medium and long terms, the strategy is to increase the portfolio of new products; meet the quality demands from customers and regulatory agencies, and face competition from China and India.

3.1. Analysis of the business evolution and results

a) Production

The optimal operation of the extensions in production capacity in 2019, carried out within the framework of Plan Act [see chapter 2.3 above], has resulted in a 10% increase in the Group's production over the prior year. Thus, the Group produced 1,488 thousand tons of product last year, that is, 1,353 tons more than in 2018.

The most significant increase was in the chlorine derivatives division, whose production increased by 13%. In 2019 the production of chlorine and caustic soda, which was significantly reduced due to the close-down of the mercury-based technology electrolysis plants at the end of 2017, has marked an important step forward towards the recovery of former production levels: the volumes of chlorine and caustic soda produced have increased by 26% and 32%, respectively, over 2018.

The greater availability of chlorine has allowed the Group to increase the production volume of certain chlorine derivatives. For this same reason, the production of EDC has tripled, which has resulted in a decreased purchase of third-party EDC, which is the chlorine derivative that the Group has to buy to meet its current chlorine needs (EDC is the product that starts the PVC chain and consists of chlorine and ethylene; when there are enough levels of chlorine, the Group produces its own EDC).

In 2019 the annual production of TCCA and chlorite, but especially PVC, has reached all-time highs.

The intermediate chemicals division was the least hit in 2018 by the general drop in the production volume and after this one-off setback, has returned to the trend shown in the last few years, with an annual moderate but gradual growth of around 3%. In this business, the production of polyol -whose capacity was extended at the beginning of the year- has increased by 21%.

The pharmaceuticals division has been the Group's counterpoint in terms of production, as it has decreased by 4%. However, in this case it is interesting to observe how the mix of product families has evolved, since the ones with lesser added value are the ones that have decreased more, whereas the production volumes of sterile phosphomycin and fusidic acid -which offer the highest profitability in the business- have increased by 24% and 10%, respectively.

b) Income

Revenue from products has remained virtually stable in 2019 despite the higher volume of products sold (+14.4%). This is due to the general drop in prices after the maximum highs registered by the middle of 2018, except for active pharmaceutical ingredients, which have continued to increase.

Revenue from products amounted to EUR 638,737 thousand, that is, 0.1% lower than in the prior year, when it amounted to EUR 639,543 thousand.

The chlorine derivatives division was the hardest hit by the significant drop in the prices of its main products (caustic soda and PVC); the income from this business decreased by 0.7% to EUR 391,635 thousand (EUR 394,388 thousand in 2018).

The intermediate chemicals division's revenue has also decreased (2.3%). This division's revenue decreased from EUR 193,992 thousand in 2018 to EUR 189,587 thousand in 2019. Although the appreciation of the US dollar -the currency in which 26.2% of the business sales are carried out- has contributed EUR 2,609 thousand to sales, the lower revenue was due to the fact that reduction in the cost of the main raw materials (methanol and melamine) was passed on to the price of final outputs. However, the transfer was only partial, which allowed the Group to improve the business margins.

On the contrary, the pharmaceuticals division's revenue has shown positive evolution, despite the 4% drop in the production volume. Sales increased from EUR 51,163 thousand in 2018 to EUR 57,515 thousand in 2019, that is, a 12.4% increase. The start-up at full operation of the production capacity extensions carried out in the fermentation, synthesis and sterile products plants has allowed the Group to have a higher volume of products to meet an upward market demand. Additionally, the robustness of demand has made it possible for the prices of all the products of this business to increase comfortably in line with the rise in the price of intermediate raw materials. Also, the effect of the US dollar has improved revenue by EUR 1,288 thousand in comparison with 2018. The best-performing product family has been phosphomycin, whose revenue increased by 32%.

In addition to the pharmaceuticals division products -in the chlorine derivatives division- and chlorine and sodium chlorite, and polyol -in the intermediate chemicals division were good performing products in 2019.

However, the year was not good for the two products that contribute the most to the Group's revenue (PVC and caustic soda), which together account for 35% of consolidated revenue.

PVC had to reduce its price because of the pressure put on it by the weakened demand and the drop in the price of its raw material (ethylene). Although the higher volume of product sold allowed revenue to show positive evolution, it was not enough to make up for the loss in unit margin, as explained in subsection c) below.

In the case of caustic soda, the drop in price was the response of a contracting market to an excess supply after a shortage in recent year made prices reach all-time highs. The increase in the Group's sales volume in 2019 was not enough to make up for the effect of the drop in price and prevent revenue from showing a downward trend. In profitability terms, the decrease in revenue was somehow mitigated because the greater availability of own caustic soda allowed the Group to reduce the proportion of third-party caustic soda marketed, whose margin is significantly lower. The variance in the selling price of caustic soda is usually the one with higher impact on the Group's results.

No customer accounts for more than 10% of the Group's sales individually, although there is one customer that purchases 40% of the chlorine produced.

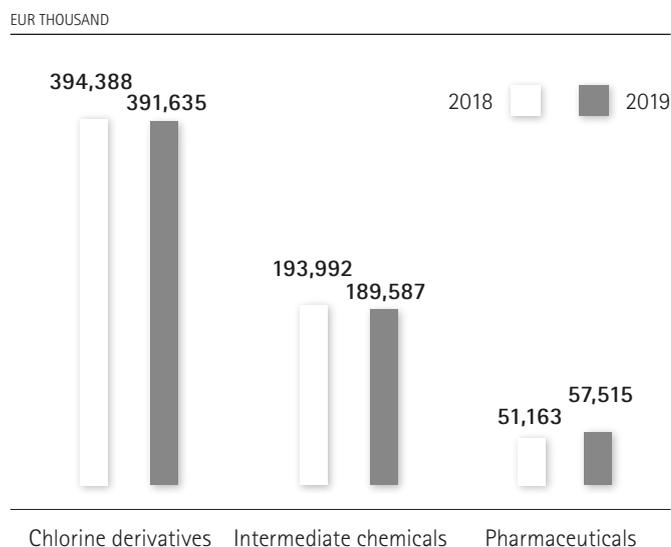
In 2019 the Group's turnover was also affected by reduction of EUR 1,352 thousand in income from the rendering of services (-4.2%). Almost all of this reduction is due to the lower remuneration for the interruptibility service of electricity paid by Red Eléctrica Española ("REE"), has been gradually decreasing year after year. Between 2018 and 2019 it dropped by 27.8% (45.8% between 2017 and 2018).

On the contrary, "Other operating income" increased by EUR 5,102 thousand, largely because of the increase in the grants received to compensate for indirect CO₂ emissions.

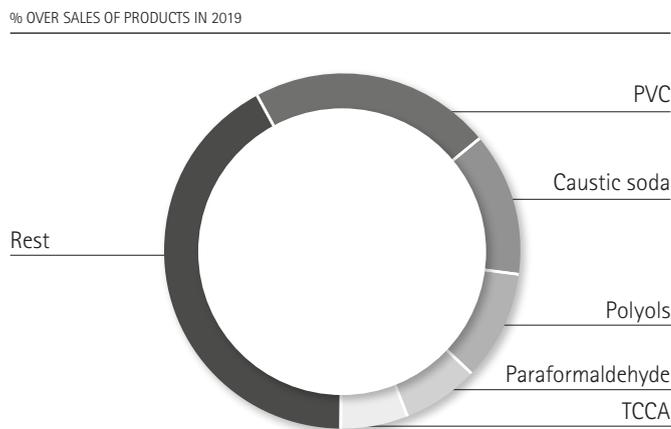
The non-operating gains of EUR 3,148 thousand generated by the sale of a plot of land and the non-recurring income of EUR 2,233 obtained mostly from the sale of scrap iron from the dismantled mercury-based technology plants should also be highlighted.

The overall result of these items meant an increase in revenue of EUR 4,271 thousand, from EUR 684,802 thousand in 2018 to EUR 689,073 thousand in 2019.

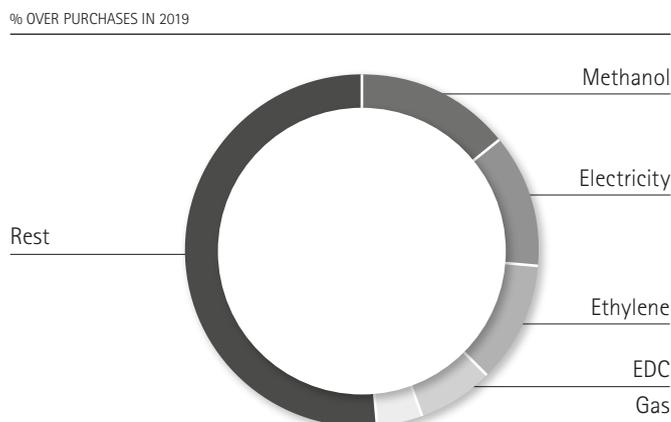
Sales by division



Top five products



Top five consumables and utilities



c) Expenses

Expenses in 2019 amounted to EUR 628,169 thousand and were 2.4% higher than in 2018, when they amounted to EUR 613,690 thousand. All items composing this chapter showed an upward trend between 2018 and 2019, with consumables and utilities registering more moderate increases than the rest.

In 2019 the bill for consumables and utilities increased by 0.4% even though the price of the main components continued to show the downward trend started at the end of 2018, pushing in turn a cut in the selling prices of final outputs, as indicated in subsection b) above.

Given that the prices went down, the slight increase in purchases was due to the volume effect. In this case, the higher amount of raw materials purchased –as a result of the increase in production [see subsection a) above]– made up for reduced purchases of third-party EDC and caustic soda, which decreased by 18% and 54%, respectively, since own production increased, as explained in subsection b) above.

As a result of this small increase in purchases and the maintenance of revenue from products, there was a slight increase in the ratio of consumables and utilities over the Group's sales, which has gone up from 68.5% in 2018 to 68.8% in 2019.

In 2019 consumables amounted to EUR 343,573 thousand (2018: EUR 341,780 thousand). The drop in the price of methanol stood out (-21%). This is the basic raw material of the intermediate chemicals division, whose profitability even increased, as the decrease in this variable cost was only partially passed on to the price of final outputs.

Electricity is the main supply of the chlorine derivatives division, which purchases it to the two main suppliers in Spain and France. The contracts with these companies are signed on an annual basis. They are renewed upon expiry and its price is linked to a pool.

Not the same happened with ethylene, which is an important raw material in the PVC chain. Its price fell less than its equivalent in the final output, with the corresponding margin loss. In the case of the PVC produced using third-party EDC (which already includes some ethylene and chlorine), the loss was even more significant since the price of this raw material increased notably (+18%), especially during the first half of 2019. Luckily, the greater availability of chlorine has allowed the Group to increase the production of PVC from own EDC instead of third-party EDC. Whereas in 2018 92% of EDC needed in the PVC chain was purchased from third parties, this percentage has dropped by 83% in 2019.

Additionally, sodium chloride did not show the same downward trend in prices and went up by 10% as a result of the mix of consumption and better quality of consumed product. This product is a raw material for the production of chlorine and caustic soda, although its weight over the cost of these products is not as significant as over the cost of electricity.

The utilities bill amounted to EUR 96,171 thousand, almost the same amount as in the prior year (EUR 96,027 thousand), performing differently from the main products of this caption. On the one hand, the electric bill was 1% lower because of the cheaper unit price of electricity and despite the increase in the amount purchased, in line with greater production. The drop of this cost prevented the profitability of chlorine, caustic soda and its derivatives from worsening. On the other hand, the cost of natural gas increased by 4%, which had a negative effect on the margins of the intermediate chemicals business and PVC.

Methanol, electricity and ethylene are the most significant raw materials in the Group's costs. These three products account for 39% of total consolidated purchases, and exceed 40% of the total costs of the manufacturing processes of formaldehyde, chlorine-caustic soda and PVC, respectively.

The expenses chapter also includes personnel expenses, which amounted to EUR 83,127 thousand, that is, a 4.1% increase. The reason for this increase is the rise in Social Security contributions, because of an increase in the bases, and pay raises. In 2019 the average headcount of Ercros Group was 1,297 employees, seven more than in 2018.

Other operating expenses amounted to EUR 97,461 thousand (2018: EUR 89,659 thousand), EUR 7,802 thousand more. This caption includes, as its main items, maintenance expenses, which decreased by 5.5%; transport expenses, which increased by 10.6% and lease expenses for logistic facilities, which increased by 36.3%.

Charges to provisions increased by EUR 1,483 thousand compared to 2018 (23.3%) as a result of the reassessment of the cost of soil remediation work. In 2019 provisions were charge for an amount of EUR 7,837 thousand (2018: EUR 6,354 thousand).

d) Results

(i) Consolidated results

In 2019 the activity of the Ercros Group has been affected by the ongoing downward trend in the derivative chemicals cycle in the European industrial sector. After four years of uninterrupted rise, in the second half of 2018 the price of most raw materials started to fall and, as a result, the price of final outputs, which were pushed by the weakness of demand and excess supply in the market. This situation has been slightly corrected during the year and ebitda for the first half of the year is EUR 1,488 thousand higher than ebitda for the first half. This is important because the second half of the year traditionally shows lower activity due to seasonal reasons.

This effect can also be observed when comparing 2019 ebitda with prior years, since although ebitda is lower than in 2018, the most significant change occurred in the first half of the year.

The evolution of income and expenses between 2018 and 2019 has given rise to ebitda decreasing by 14.4% and amounting to EUR 60,904 thousand (2018: EUR 71,112 thousand). Additionally, decreased ebitda has caused a reduction in the margin of ordinary ebitda¹ over sales, which has decreased from 11.3% in 2018 to 9.5% in 2019.

In the prior year, two items of opposite nature, not related to ordinary activities, that did not have any balancing entry in 2018 were recorded: the sale of a plot of land, which generated gains of EUR 3,148 thousand, and impairment of investment properties amounting to EUR 5,615 thousand.

Additionally, depreciation and amortization, amounting to EUR 26,576 thousand, were slightly higher than in 2018 (0.8%); however, impairment of assets arisen has caused ebit to decrease by 35.8% between 2018 and 2019, from EUR 44,747 thousand to EUR 28,713 thousand.

Finance costs –amounting to EUR 6,502 thousand– decreased by 20.3% due to the lower average cost of debt, the lower impact of currency translation differences and the effect of the cancellation of the debt of the non-controlling interest of Ufefys, S.L.

In 2019 the Group has recorded an income of EUR 414 thousand (EUR 1,132 thousand in 2018) from associates and an income of EUR 8,418 thousand from the aforementioned income tax (EUR 6,876 thousand in 2018). At December 31, 2019 the Group still has unrecognized deferred tax assets amounting to EUR 65,051 thousand (EUR 76,397 thousand at prior year end).

As a result of all this, profit amounting to EUR 31,043 thousand has been obtained, which is 30.4% lower than 2018 profit, when it amounted to EUR 44,594 thousand.

This reduction in profit but also, though in a lesser proportion, in the number of shares composing share capital have caused earnings per share ("EPS") to decrease from EUR 0.408 in 2018 to EUR 0.2924 in 2019 [see chapter 10.1 a)].

Income statement

EUR THOUSAND			
	2019	2018 ²	Change (%)
Income	689,073	684,802	0.6
Sales of goods	638,737	639,543	-0.1
Rendering of services	31,045	32,397	-4.2
Other operating income	13,466	8,364	61.0
Reversal of provisions and other non-recurring income	2,233	1,821	22.6
Changes in inventories	444	2,677	-83.4
Gains on disposals of investment properties	3,148	0	–
Expenses	-628,169	-613,690	2.4
Supplies	-343,573	-341,780	0.5
Utilities	-96,171	-96,027	0.1
Employee benefits expense	-83,127	-79,870	4.1
Other operating expenses	-97,461	-89,659	8.7
Charge of provisions and other non-recurring income	-7,837	-6,354	23.3
Ebitda	60,904	71,112	-14.4
Depreciation and amortization	-26,576	-26,365	0.8
Impairment of investment properties	-5,615	0	–
Ebit	28,713	44,747	-35.8
Finance costs and exchange gains (losses)	-6,502	-8,161	-20.3
Share in the profit of associated companies	414	1,132	-63.4
Profit before tax	22,625	37,718	-40.0
Income tax	8,418	6,876	22.4
Profit for the year	31,043	44,594	-30.4
Earnings per share (EUR)	0.2924	0.4085	-28.4

¹ Ebitda from ordinary activities: It is obtained by subtracting non-recurring items from ebitda (EUR 63,360 in 2019 and EUR 75,645 in 2018).

² The 2018 income statement has been restated to include the application of IFRS 16 and make it comparable to the 2019 income statement.

Results by business segment¹

EUR THOUSAND

	Chlorine derivatives division			Intermediate chemicals division			Pharmaceuticals division		
	Year 2019	Year 2018	Variation (%)	Year 2019	Year 2018	Variation (%)	Year 2019	Year 2018	Variation (%)
Income	435,334	432,560	0.6	191,427	197,199	-2.9	56,931	53,222	7.0
Sales of goods	391,635	394,388	-0.7	189,587	193,992	-2.3	57,515	51,163	12.4
Rendering of services	31,005	32,262	-3.9	40	48	-16.7	0	87	—
Other income	9,123	6,721	35.7	3,825	1,479	—	518	164	—
Changes in inventories	3,571	-811	—	-2,025	1,680	—	-1,102	1,808	—
Expenses	-397,390	-377,657	5.2	-176,719	-184,503	-4.2	-46,223	-45,176	2.3
Supplies	-208,912	-195,063	7.1	-116,007	-127,538	-9.0	-18,654	-19,179	-2.7
Utilities	-77,912	-77,955	-0.1	-14,405	-13,974	3.1	-3,854	-4,098	-6.0
Employee benefits expense	-48,786	-46,838	4.2	-21,373	-20,921	2.2	-12,968	-12,111	7.1
Other expenses	-61,780	-57,801	6.9	-24,934	-22,070	13.0	-10,747	-9,788	9.8
Ordinary ebitda	37,944	54,903	-30.9	14,708	12,696	15.8	10,708	8,046	33.1
Depreciation and amortization	-16,169	-16,122	0.3	-7,296	-7,108	2.6	-3,111	-3,135	-0.8
Operating profit	21,775	38,781	-43.9	7,412	5,588	32.6	7,597	4,911	54.7
Assets	289,893	296,436	-2.2	146,492	158,740	-7.7	55,773	52,731	5.8
Liabilities	82,372	93,204	-11.6	32,949	33,720	-2.3	9,261	9,738	-4.9
Investments in non-current assets	25,250	20,662	22.2	2,835	7,314	-61.2	5,487	3,609	52.0

¹ The sum of the captions of the divisions does not equal the total of the captions in the consolidated financial statements as certain items have not been allocated to any division.

(ii) Profit from the chlorine derivatives division

As explained in the subsections above, 2019 was not as good a year as the previous two for the chlorine derivatives business; the drop in the prices of raw materials, especially caustic soda and PVC, affected it severely causing a significant impairment of margins.

The drop in margins has been mitigated due to the decrease in costs, especially in the case of electricity, the main raw material, and the increase in the volume sold, as a result of the entry in some Spanish market areas that until now were taken by other competitors.

In this context, the business's ebitda, which amounted to EUR 37,944 thousand, was reduced by 30.9% in comparison with 2018. Thus, the ebitda over sales margin reached 9.7% compared to 13.9% in 2018 and keeps close to the 10% objective.

After discounting depreciation and amortization, for an amount of EUR 16,169 thousand, the business's operating profit amounts to EUR 21,775 thousand, 43.9% lower than in 2018.

(iii) Profit from the intermediate chemicals division

The intermediate chemicals division showed gradual improvement over the year, and the business's operating profit ended up increasing significantly (+32.6%). The year was particularly favourable for the polyol product family, with an increase in its production capacity that resulted in a greater volume sold of 19%.

This business has dealt with a scenario of strong demand from the markets and drop in prices. This combination, as said in subsection c) above, made that the decrease in consumables was only partially passed on to the prices of final outputs. This is the reason why ebitda increased by EUR 2,012 thousand (15.8%) despite the reduction in revenue. The appreciation of the US dollar against the euro also had a positive influence which help exports without it damaging purchases. The impact of the exchange rate on ebitda, compared to 2018, has been EUR 2,609 thousand.

In line with the margin improvement, the ebitda over sales ratio has gone up from 6.5% in 2018 to 7.8% in 2019, which brings it closer to the usual values of this business.

After depreciation and amortization –which have increased by 2.6%– the business's operating profit amounts to EUR 7,412 thousand compared to EUR 5,588 thousand in the prior year.

(iv) Profit from the pharmaceuticals division

The pharmaceuticals division continues to show the upward trend started in recent years. Almost all parameters were favourable to this business in the current year.

The robustness of the market allowed for a general increase in the prices of final outputs but, most importantly, the volume sold, especially in the case of higher added-value products. Additionally, it was positively impacted by the average US dollar exchange rate, and this currency accounts for 43.2% of its sales. The only negative point was the increase in the cost of intermediate raw materials (+13.7%), although even this could be partially offset by the significant drop in the costs of energies (-6%).

From the concurrence of the aforementioned factors, ebitda increases by 33.1% compared to the prior year: from EUR 8,046 thousand in 2018 to EUR 10,708 thousand in 2019, a rise of EUR 2,662 thousand.

This significant improvement has made it possible for the ebitda over sales margin to increase substantially up to 18.6% (15.7% in 2018).

Finally, after subtracting depreciation and amortization amounting to EUR 3,111 thousand, the business's operating profit amounted to EUR 7,597 thousand compared to EUR 4,911 thousand in 2018, an increase of 54.7%.

e) Geographical markets

Unlike in the prior year, in 2019 the foreign market performed better than the domestic market, partially due to the favourable average US dollar exchange rate, which push exports towards the countries operating with this currency. Thus, the slight decrease in the Group's sales (-0.1%) is due to the 2.0% increase in exports and the 2.1% reduction in domestic sales.

The domestic market accounted for 52% of sales and amounted to EUR 329,914 thousand (EUR 336,876 thousand in 2018). The remaining 48% of sales were made abroad and amounted to EUR 308,823 thousand (2018: EUR 302,668 thousand).

66% of the chlorine derivatives division's turnover was recorded in Spain. In this business, sales to the Spanish market decreased by 2.1% and exports increased by 2.2%.

In the intermediate chemicals division the reduction in turnover has affected both markets but has hit the foreign market harder, with sales decreasing by 2.4%, than the domestic market (2.1%). This business exports 65% of its turnover.

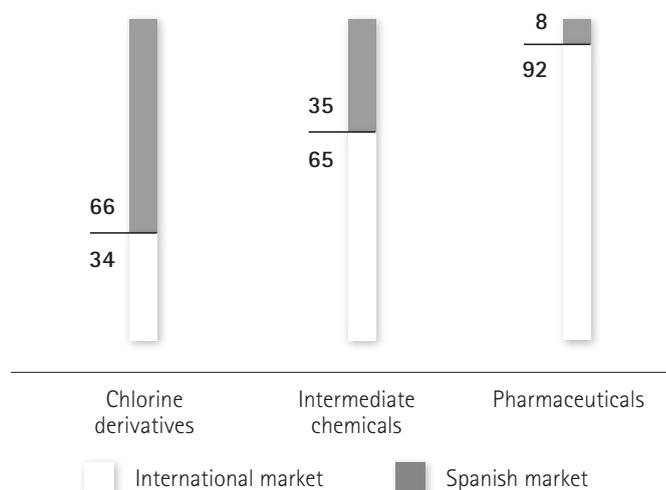
The pharmaceuticals division carries out 92% of its sales outside of Spain, increasing by 13.5% in comparison with 2018. The increase in sales in our country has been more moderate (0.9%).

The European Union ("EU") is the main destination of the Group's exports and accounts for 28% of consolidated sales; turnover in the EU remained stable (1%) compared to 2018. However, the sales to OECD countries recorded significant growth of 14%, pushed by the sales to the USA; this geographical area accounts for 9% of the Group's sales. The area that showed poorer performance, for the second year in a row, was the rest of the world, which accounts for 11% of consolidated turnover and saw a decrease in sales of 5% between 2018 and 2019.

The sales to France, Italy and Portugal, which are traditionally the three main destination of the Group's exports, have decreased, whereas they have increased notably to the USA and Germany.

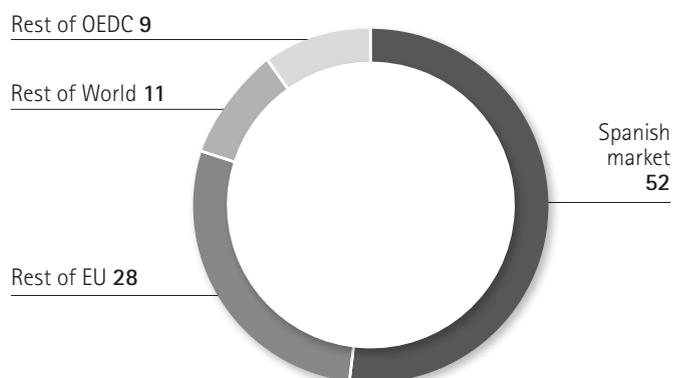
Business markets

% OVER TOTAL SALES OF EACH BUSINESS IN 2019



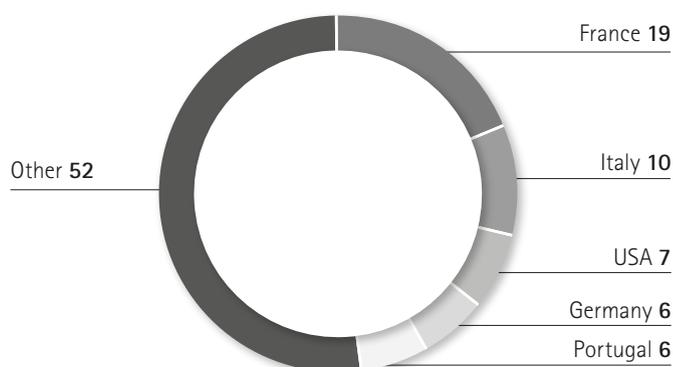
Sales by geographical areas

% OVER TOTAL SALES IN 2019



Top five destinations

% OVER EXPORTS IN 2019



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 2019 the average exchange rate of the US dollar appreciated against the euro. In the case of the Group's consolidated sales, the average exchange rate decreased from 1.181 US dollar/euro in 2018 to 1.118 US dollar/euro in 2019 (a -5.3% difference).

The fact that the US dollar has appreciated against the euro has a positive effect on the Group, since the competitive position of the products it markets improves, which explains the increase in sales in this currency in 2019 compared to 2018, and improves the return in euros on the sales in dollars, which increases profitability.

An average exchange rate of 1.150 has been estimated for 2020. Thus, if this forecast finally proves good, the profitability of the Group's products may be reduced, although not significantly.

In 2019 the sales in US dollars amounted to EUR 105,394 thousand whereas they amounted to 101,677 in 2018, which means a 3.7% increase. The sales in this currency accounted for 14.8% of total consolidated sales (13.5% in the prior year).

On the contrary, the appreciation of the US dollar against the euro cause the price of Group purchases in US dollars to rise. Consequently, the Group decided to reduce them as much as possible: from 63,889 thousand to 48,978 thousand. This 23.3% reduction could be possible, among other measures, by reducing the volume of third-party EDC, a consumable that is paid with this currency. In 2019, purchases in US dollars accounted for 9.9% of total consumables and utilities paid for by the Group (12.4% in the prior year).

The strong decrease in purchases made in US dollars –and to a lesser extent, the increase in sales made in this currency– resulted in a higher net exposure of the Group to US dollar, which amounted to 56,416 thousand dollars in 2019 compared to 37,788 thousand dollars in 2018. The effect of the dollar appreciation over the Group's ebitda –calculated based on 2018 net exposure– was EUR 2,794 thousand.

3.2. Financial, operating and stock market indicators

Indicators ¹	Year 2019	Year 2018 ²
Financial		
Leverage ratio (< 0.5) ³	0.38	0.46
Solvency ratio (< 2) ³	1.74	1.67
Liquidity	1.03	0.99
Funding of assets	1.02	0.99
ROCE (%)	6.76	10.19
Average collection period (days)	61.00	62.00
Average payment period (days)	53.74	55.16
Operating		
Production (thousands of tons)	1,488	1,353
Added value (EUR thousand)	144,031	150,982
Productivity (EUR/person)	111,049	117,040
Gross margin/revenue (%)	50.14	50.09
Ordinary ebitda/sales margin (%)	9.46	11.26
Stock market		
Quoted market value (EUR /share)	2.56	3.11
Capital value (EUR thousand)	268,585	335,496
EPS (EUR) ³	0.2924	0.4085
CFS (EUR)	0.57	0.45
PER	8.65	7.52
P/BV	0.92	1.23

² The 2018 income statement has been restated to include the application of IFRS 16 and make it comparable to the 2019 income statement.

³ Conditions for the payment of dividends.

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: operating profit/loss ÷ resources used.
- Purpose: measure the level of return obtained by the Group in its 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 + personnel costs.
- 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 – consumables) ÷ 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 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 are 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 – = subtracted × = 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 December 31, 2018 and 2019, the most striking thing in the balance sheet is the reduction of EUR 16,370 thousand (-12.9%) in net financial debt ("NFD"), from EUR 126,541 thousand to EUR 110,171 thousand. This reduction has been possible thanks to the generation of free cash flows, as disclosed in the cash flow statement.

The high volume of investments made in 2019 [see section 4.3 b) below] has affected the evolution of non-current assets, which have increased by EUR 12,479 thousand (3.6% in comparison with 2018 year-end) and amount to EUR 359,713 thousand.

Working capital has been significantly reduced mainly due to the decrease in inventories and trade receivables. At 2018 year end working capital amounted to EUR 91,865 thousand whereas at 2019 year end working capital has decreased by EUR 26,995 thousand (-29.4%) to EUR 64,870 thousand.

The Group's total equity –amounting to EUR 292,083 thousand– has increased by EUR 19,827 thousand (+7.3%). This variation is lower than the profit obtained during the year, due to the funds allocated to shareholder remuneration for the year, which resulted in a decrease in total equity of EUR 11,216 thousand (EUR 4,545 thousand due to the acquisition of treasury shares; EUR 6,295 thousand due to dividends paid; and EUR 376 thousand due to the payment of the general meeting attendance bonus) [see chapter 10.1 b) (ii)].

Provisions and other debts have decreased by EUR 17,973 thousand due to the exceptionally high payments made during the year, amounting to EUR 25,001 thousand, among others, the historical liability corresponding to the decontamination of the Flix reservoir, amounting to EUR 11,332 thousand, and the contribution to the Tesoro Público related to the 2013 labour force adjustment plan, amounting to EUR 3,065 thousand.

Economic analysis of the balance sheet

EUR THOUSAND

	12-31-19	12-31-18 ¹	Change (%)
Non-current assets	359,713	347,234	3.6
Working capital	64,870	91,865	-29.4
Current assets	184,470	217,044	-15.0
Current liabilities	-119,600	-125,179	-4.5
Applied funds	424,583	439,099	-3.3
Equity	292,083	272,256	7.3
NFD²	110,171	126,541	-12.9
Provisions and other borrowings	22,329	40,302	-44.6
Origin of funds	424,583	439,099	-3.3

¹The 2018 balance sheet has been restated to include the application of IFRS 16 and make it comparable to the 2019 balance sheet.

²All financial debts with non-bank entities, as well as lease payables, are included in net financial debt (EUR 13,378 thousand in 2019, and EUR 19,234 thousand in 2018). Additionally, apart from cash and cash equivalents, those deposits that guarantee debt commitments have been recognized as a decrease in the financial debt EUR 11,247 thousand in 2019, and EUR 9,078 thousand in 2018).

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 2019.

The significant increase in the resources generated by the Group's businesses in 2019 has provided the necessary liquidity to meet its obligations in a timely manner (payment on investments and shareholder remuneration) and to reduce the net financial debt [see section 4.1 above]. Forecasts for 2020 suggest that the level of free cash flow will remain stable as almost all the investments planned for the 2016-2020 period have been completed. Consequently, it is not expected that the Group will be exposed to a liquidity risk in its transactions. In addition, at 2019 year end the Group's liquidity amounts to EUR 61,117 thousand.

a) Major financing sources

In 2019 the Group has used the following financing sources:

(i) External

- The factoring facility in euros, which allows the Group to finance working capital up to a limit of EUR 102,146 thousand. At December 31, 2019, the drawdown balance of this facility amounts to EUR 51,105 thousand (EUR 41,780 thousand in the prior year).
- The revolving credit agreement, with an overall limit of EUR 30,000 thousand. At December 31, 2019 EUR 30,000 thousand have been drawn down (EUR 20,000 thousand in 2018).
- The ICO loan, amounting to EUR 18,000 thousand. At December 31, 2019, the balance of this loan amounts to EUR 17,730 thousand (EUR 2,000 thousand in the prior year).

- The loans granted by the Department of Industry, Tourism and Trade, which are secured by deposits on a portion of the principal. At December 31, 2019, said deposits amount to EUR 2,956 thousand (2018: EUR 1,875 thousand).
- In May 2019 Ercros cancelled its financing facility at maturity through the securitization of accounts receivable arranged with Finacity Corporation for an amount of USD 12,000 thousand.

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

- In 2019 the Group's activity and the sale of a non-operating land, classified as an investment property, have generated a high volume of funds. Free cash flows amounted to EUR 28,079 thousand (EUR 6,099 thousand in 2018) and the sale of the land meant a cash inflow of EUR 5,748 thousand.

The funds available have been allocated: (i) to pay investments amounting to EUR 31,352 thousand; (ii) to remunerate the shareholders for an amount of EUR 11,216 thousand; and (iii) to reduce NFD, by EUR 16,370 thousand.

Thanks to the cash flow generation, the Group has also strengthened its liquidity and solvency position, increasing cash and cash equivalents by EUR 45,272 thousand.

- At December 31, 2019 the Group had cash amounting to EUR 61,117 thousand (EUR 15,845 thousand at 2018 year-end) and additional funding amounting to EUR 8,406 thousand (EUR 32,733 thousand at 2018 year-end).
- At the beginning of 2020, the refund of the 2018 income tax, amounting to EUR 7,724 thousand, was received.

The Group has faith that, as it has happened until now, if new investment opportunities and needs arise in some production facilities to meet its growth expectations, other supplementary mechanisms could be used to obtain one-off liquidity, such as the partial and selective sale of non-operating items or the issue of bonds in the short and medium terms in organized markets.

b) Grants and public aid

In 2019 Ercros has received the following grants from public entities:

Entity	Item	Factories	Amount (EUR thousand)
Ministry of Industry, Trade and Tourism	Offset of cost related to 2016 indirect CO ₂ emission allowances ¹	Flix, Sabiñánigo, Tortosa and Vila-seca II	1,445
Ministry of Industry, Trade and Tourism	Offset of cost related to 2017 indirect CO ₂ emission allowances ¹	Almussafes, Flix, Sabiñánigo, Tortosa, Vila-seca I and Vila-seca II	198
Ministry of Industry, Trade and Tourism	Offset of cost related to 2018 indirect CO ₂ emission allowances ²	Almussafes, Flix, Sabiñánigo, Tortosa, Vila-seca I and Vila-seca II	4,413
IDAE ³	Investment in caustic soda concentration technology	Vila-seca I	472
Acció ⁴	R&D on ErcrosBio PLA 3D premium	Chlorine derivatives division	60
CDTI ⁵	R&D on new materials produced with PVC	Chlorine derivatives division	58
Total			6,646

¹ Granted in 2018.

² Granted in 2019.

³ The Institute for Diversification and Saving of Energy ("IDAE") is a public company affiliated to the Ministry for Ecological Transition and Demographic Challenge that grants aid to improve energy efficiency and implement renewable energies.

⁴ Acció is an agency for business competitiveness affiliated to the Department of Business and Knowledge of the Regional Government of Catalonia.

⁵ The Centre for the Development of Industrial Technology ("CDTI") is an entity depending on the Ministry of Science and Innovation that grants aid for innovation and technological development projects.

Additionally, the Group has been granted aids by IDAE, for an amount of EUR 7,386 thousand, which are pending receipt while the investments that have generated them are justified and reviewed.

Additionally, in 2019 the Group was granted the following public aid:

- The Ministry of Industry, Trade and Tourism granted the Group free assignment of emission allowances for an amount equal to EUR 4,936 thousand (EUR 1,746 thousand in 2018).
- The State Foundation for Training in Employment ("Fundae") reimbursed a portion of the training expenses incurred, EUR 195 thousand, which is deducted from the contributions to the Social Security paid by the Group (EUR 186 thousand in 2018).

c) 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 EUR /share.
- That the solvency ratio (DFN / ordinary ebitda) is less than or equal to 2.
- That the leverage ratio (DFN / total equity) is less than or equal to 0.5 [see chapter 10.1].

d) Level of indebtedness

As indicated in section 4.1 above, the NFD has been reduced by EUR 16,370 thousand. At December 31, 2019, the NFD amounts to EUR 110,171 thousand in comparison with EUR 126,541 thousand at 2018 year end.

As said in subsection c) 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, which has always been met in these past years (2016, 2017, 2018 and 2019) and is expected to be met in 2020.

e) Payment period to suppliers

The average payment period to suppliers at 2019 year end was 53.7 days (55.2 days at 2018 year-end), which means a reduction of 1.5 days between both years, in line with recent years' trend.

At December 31, 2019, the payments that exceeded 60 days accounted for 34% of all payments made (40% in 2018). The Group forecasts that it will continue reducing the percentage of payments exceeding 60 days, in line with the two past years.

In the prior year the average collection period was 61 days (2018: 62 days).

4.3 Capital resources

The Group has 10 industrial premises located in several Spanish autonomous regions and supplies products to customers in 88 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, gas), have considerable relevance to the Group's costs. Consequently, the cyclical fluctuations in prices also causes fluctuations in the company'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 requirements.

The volume of capital is established based on the existing risks and the corresponding capital adjustments are made based on changes in economic conditions and the risks associated with the activity.

The Group manages capital considering the characteristics of its business and is not subject to externally imposed capital requirements. In order to manage its share capital, the Group uses the leverage and solvency ratios set forth in the shareholder remuneration policy [see chapter 10.1 a)].

The Group periodically measures and analyses these ratios and makes future estimates of them, being the key factor when determining its investment policy, divestments to reduce debt, payment of dividends, capital returns to its partners or the issuance of new shares.

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].

Between December 31, 2018 and 2019 total equity has increased by EUR 19,827 thousand (+7.3%) from EUR 272,256 thousand to EUR 292,083 thousand. This increase is due to the profit for the year after discounting the resources allocated to shareholder remuneration amounting to EUR 11,216 thousand (EUR 19,699 thousand in 2018).

a) Firm commitments to obtain capital resources

There are no firm commitments to obtain new capital resources.

b) Investment commitments or obligations

In 2019 the measures set forth in the investment plan for the 2016-2020 period, which amounted to EUR 100,000 thousand, were almost completed [see chapter 2.3 c)].

Thus, over the prior year, investments amounting to EUR 33,572 thousand (EUR 31,585 thousand in 2018) were made, of which EUR 16,228 thousand (EUR 23,718 thousand in 2018) corresponded to actions for extending the production capacity and the other EUR 17,344 thousand correspond to other investments (EUR 7,867 thousand in 2018).

At December 31, 2019 there were investment commitments amounting to EUR 20,816 thousand (EUR 28,319 thousand in 2018). 20% of said amount, corresponds to investments allocated to increase the production capacity of several plants (60% of the amount committed in 2018).

Given that the entire plan for the 2016-2020 period is currently almost completed, the Group plans to invest around EUR 30,000 thousand in 2020. This is the annual capex level considered normal, provided that no new regulations requiring exceptional investments are introduced.

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 year 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, quantify and monitor the potential risks it is exposed to. This alert system is triggered whenever a risk that might affect the Group is identified.

Additionally, there is a compliance committee that provides assistance to the audit committee –to which it reports– on criminal risk prevention. On October 31, 2019 the board of directors approved, following a favourable report by the audit committee, the criminal risk prevention handbook and the criminal compliance policy. Additionally, the Group has a (i) code of ethics; (ii) an ethical channel procedure; (iii) an anti-corruption and crime prevention policy; and (iv) a conflict of interest procedure in place.

Likewise, 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.

5.2. Main risks for the Group

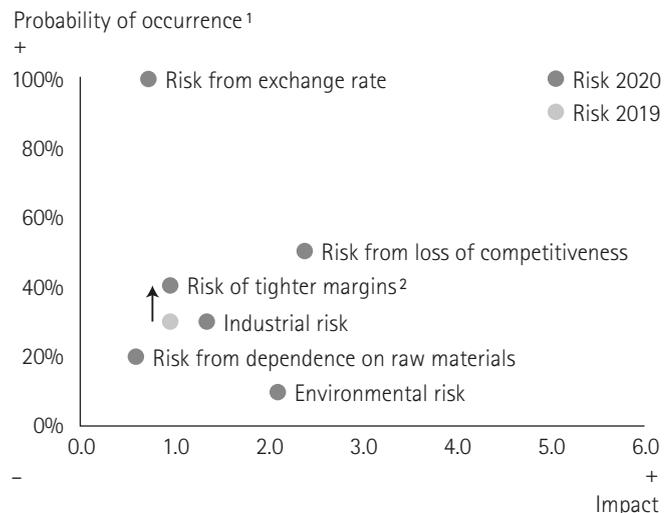
The Ercros Group's activity involves several kinds of risks, classified under the criteria that the Group considers most appropriate to manage them efficiently. In this regard, not all businesses entail the same risks, although sometimes they may share some of them. In general, the Ercros Group is exposed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

On December 19, 2019 the business directors presented to the board of directors the risk maps for each business identifying the most relevant risks for 2020 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.

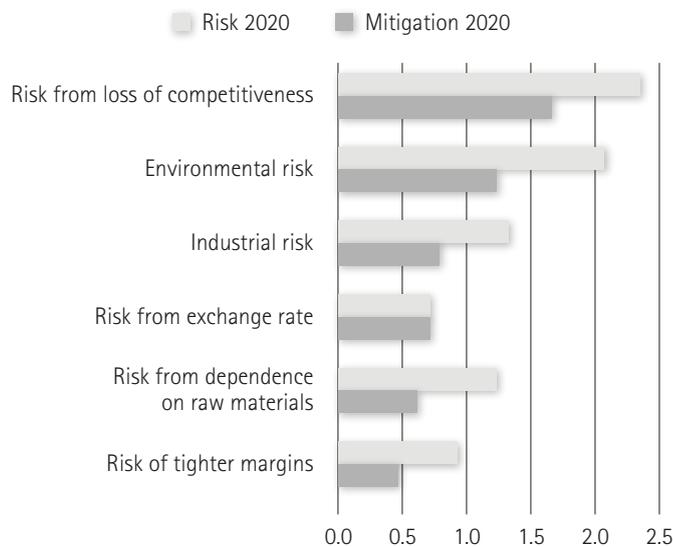
The graph below shows the relevant risks to the Group for 2020 based on the probability of occurrence and impact, and their evolution in comparison with 2019 according to the risk map prepared:



¹ To prepare this graph, in the risks shared by two or more businesses, the highest probability of occurrence percentage has been used.

² Risk that may worsen in 2020.

The graph below shows the same relevant risks after applying mitigating measures:



The risk map does not include risks related to corruption, bribery and money laundering because these types of risks have not been identified as relevant to the Group. In 2019 the work plan of the external auditor, Ernst & Young, focused on analysing the following significant issues: net sales and accounts receivable, provisions, contingencies and obligations, and deferred tax assets, without any significant incidents being detected.

The main risks that may affect the Group, classified by type, are described below:

a) Operating risks

The Ercros Group is an industrial conglomerate with 10 production facilities that carry out its production activities within the framework of its commitment to the safety of its facilities and the health of its staff, respect for the environment, the quality of its products and dialogue and transparency in relation to society.

During the course of carrying on its business activity, the Group is exposed to the following operating risks:

(i) Risk of loss of competitiveness (relevant)

The Ercros Group engages in its business in a global environment that new competitors are continually entering, competitors that have benefited from looser regulations in their countries of origin, fewer environmental requirements compared to the European market, lower wages and energy costs and measures in support of development. The

cost differential in these countries becomes a key competitive factor when setting the final price of products. This situation is exacerbated by the fact that the Group's main products are commodities that are subject to stiff competition from emerging markets, such as India and China. Competition from these countries is one of the main risk factors of the intermediate chemicals and pharmaceuticals divisions.

The main raw material used by the chlorine derivatives division is electricity, which currently accounts for approximately 44% of the production cost of the electrolysis plants. Although the caustic soda market is a global market, the electricity costs for production are specific to the Iberian market and, therefore, electricity is a component that affects the Group's competitiveness.

The downward trend in the price of electricity in 2019 affected all European producers, although the slightly larger drop in Spain made it possible to reduce the differential with the main producer countries, resulting in a slight improvement in competitiveness. In addition, the technological updating of the production processes undertaken by the Group resulted in greater energy efficiency and a higher utilisation ratio, which improved the profitability of its products.

On the other hand, over the last 10 years, the Group has been receiving remuneration for the interruptibility service of the electricity supply to the chlorine and caustic soda plants it provides Red Eléctrica Española ("REE"), which is set through auctions. In 2019 the amount was set through two auctions. The first auction was for the period from 1 January to 31 June and the second was for the period from 1 July to 31 December. The price paid for the interruptibility service has been gradually reduced. Thus, in 2019 the amount received by the Group for this service was five times less than that obtained in 2009. At 2019 year end, an auction was held for the first half of 2020. For the first time, the Group did not award a batch because of the low remuneration. The Group expects to offset part of the remuneration it had been receiving through greater modulation of consumption, the decrease in the price of the electricity pool and the improvements to be established by the future energy-intensive consumer statute.

Likewise, the government enacted Royal Decree Law 20/2018, of 7 December, on urgent measures to foster economic competitiveness in the industrial and commerce sector in Spain, including measures to promote the fair transition of energy-intensive industries, including the approval of the energy-intensive consumer statute. On 11 February 2020, the government published a draft Royal Decree regulating the energy-intensive consumer statute, the aim of which is to reduce the cost of electricity for energy-intensive industries through measures such as: (i) a reduction of up to 85% for some system costs; (ii) compensation for the indirect costs of CO₂ emissions; and (iii) incentives to contract energy from renewable sources in the long term. These measures would replace the remuneration for interruptibility and would also make it possible to reduce the gap between Spanish producers and their European competitors in relation to electricity costs.

A relevant risk for the Group's competitiveness is the regulatory changes in the labour market announced by the government that, if confirmed, could significantly increase the cost of subcontracted services.

Another factor that has traditionally affected the Group's competitiveness is the euro to dollar exchange rate, particularly in the case of products from countries that use this currency in their commercial transactions –mainly emerging economies. In 2019 the average dollar exchange rate appreciated against the euro by 5.3%, which improved the competitiveness of the Group's products. The forecast that in 2020 the dollar may again depreciate somewhat against the euro would worsen the competitive position [see section c) (i) Foreign exchange risk].

(ii) Industrial risk (relevant)

The production activity carried out by the Ercros Group involves the execution of operations that are dangerous and require diligent action on the part of the staff performing them. In addition, industrial facilities in the chemical industry have intrinsic potential risks arising from the use (handling, storage and processing) of substances –some of which are dangerous– that they use or manufacture; from human failure due to the improper use of the products or processes; and from the maintenance or restructuring of these facilities.

The safety of people and facilities is a priority for the Ercros Group and, therefore: (i) it carries out its activities within a framework of maximum safety and compliance with legislation; (ii) its facilities are certified with internationally approved standards and are subject to operability studies (HAZOP method) and to periodic inspections; (iii) each factory has a preventive maintenance plan for its industrial facilities; and (iv) internal and external employees receive training on preventive matters adapted to their job. In addition, the Group investigates all accidents and incidents, analyses their causes and establishes, where appropriate, the corrective actions necessary to prevent their recurrence.

The Group carries out programmed shutdowns of its production plants for maintenance, repair or modernisation, although on occasions there are also unplanned shutdowns. The start-up of a production plant can sometimes take longer than expected, which prevents the production plans from being fulfilled. In other instances, plants have to slow down or even stop production because of problems with key raw material suppliers or important customers of the final product. The Group has taken out insurance to cover the loss of earnings arising from these contingencies.

(iii) Risk of tightening margins (relevant)

In the chemical industry, due to the high volume of products manufactured worldwide and the unequal growth of supply and demand, it is customary for two to five-year periods in which the supply and demand are balanced and the product profitability is adequate to alternate with other periods where the supply increases inordinately with respect to demand, or demand falls, in both cases causing an imbalance, ultimately eroding margins. From 2016 to the first half of 2018, the cycle maintained an upward trend, in a context of demand pressure, supply shortages and high prices; however, after the first half of 2018, the trend shifted, marked by oversupply, falling prices and, in general, the weakening of global markets, entering a recessive chemical cycle that is expected to last until 2021.

In the Ercros Group, PVC and caustic soda are the products that weigh most heavily in consolidated billings (in 2019, their combined share was 35%) and that suffer most from these tensions in the margins, a situation that increases the Group's sensitivity to them.

In the case of caustic soda, in 2019 the slight global increase in production capacity and the higher rate of use of this capacity generated excess supply in the global markets that, together with the contraction in demand resulting from the worsening of economic activity, drove prices down. This drop was greater than the drop in the price of electricity, its main input, with the consequent deterioration of the margin of the final product. During the year, the Group tried to mitigate this effect by increasing the total volume of caustic soda sales and, in particular, own caustic soda, the margin of which is significantly higher.

Over the past year, the loss of profitability of PVC was caused both by the rise in the price of external EDC –the product that starts the PVC chain– and by the loss of profitability of PVC compared to the other important raw material, ethylene. The price of PVC was the result of weak demand in Europe and the entrance of product from the US at a more competitive price, although in a more moderate manner than in 2018.

The following table shows the analysis of the sensitivity of the Group's ebitda to possible variations, all other things being equal, in the price of caustic soda and PVC:

	Price Variation	Effect on ebitda (EUR thousand)
Caustic soda	± EUR 50/t	± 6,430
PVC	± EUR 50/t	± 8,800

(iv) Risk of dependence on raw materials (relevant)

As seen in point (iii) above, the Group is heavily dependent upon the main raw materials it uses in its industrial processes, the prices of which are subject to cyclical variations, and on occasions, may not be available in the quantities required or within the desired time.

The Group aims to mitigate the risk of dependence on raw materials by applying a strategy in relation to key suppliers that seeks: (i) the stable supply of the most volatile raw materials with long-term supply agreements although, in view of the current downward trend in the price of supplies, the Group has decided to prioritise, to the extent possible, short-term agreements to take better advantage of this situation; (ii) to negotiate supply agreements in which the sales prices of the main products are indexed to the cost of their raw materials; and (iii) the diversification of strategic supply sources. In addition, to reduce the impact on the business of the volatility of the prices of raw materials, the Group efficiently manages stocks.

The Group's three main inputs are methanol, electricity and ethylene, which represent 39% of the total amount of consolidated purchases and more than 40% of the total cost of the chlorine, formaldehyde, and PVC manufacturing processes, respectively.

As mentioned above, the Ercros Group always tries to pass on the variations in its variable costs to the price of its products; however, sometimes, depending on the demand situation, it cannot do so in full or even in part, or when it does, it does so with a certain time lag, which can lead to the loss of profitability of the product in question. In 2019 the weakness of the markets prevented, in certain instances, the increase in some raw materials from being passed on to the price of the end product or, as in the case of PVC, the price of the end product fell more than that of ethylene, causing a narrowing of margins as described in point (i) above.

Electricity is the primary supply of the chlorine derivatives division. The Group purchases its electricity from two of the main distributors in Spain and France. The agreements with these companies are annual and are renewed upon termination.

The price of the MWh consumed in the electrolysis plants is determined by the daily electricity reviews, which are significantly influenced by the electricity generation structure at any given time. Therefore, the price drops when electricity generation using renewable sources (wind and hydraulic energy) increases and rises when it is generated using fossil fuels. The regulated costs of the system must be added to the price.

In 2019 the unit production cost for electricity consumption reduced thanks to the greater energy efficiency of electrolytic plants that manufacture with membrane technology—which is 30% more efficient in terms of electricity consumption than the previous ones with mercury technology—and a lower electricity

pool price in Spain due to lower demand from industry (2019 closed with a very significant decline in industrial electricity consumption), the increased weight that renewable energy is acquiring as a supply source and the near disappearance of energy generated in coal plants. By 2020 the lack of remuneration received by the Group for the interruptibility service is expected to be offset by a continued drop in the cost of electricity and greater modulation in consumption.

The Group is also exploring bilateral long-term renewable energy purchase agreements, known as PPAs (Power Purchase Agreements), and the possibility of installing solar panels on land owned by Ercros that is not currently used for any industrial activity. It also continues to implement operational measures aimed at making its processes more energy efficient. With these measures, the Group's strategy is to reduce energy consumption and the future cost of this supply, and to ensure that it comes from renewable sources to be in a position to meet the decarbonisation goal set out in the draft Spanish National Integrated Energy and Climate Plan and reinforce the recent Government Declaration on the climate and environmental emergency, in keeping with the targets set by the European Commission in the Green Pact.

In addition to electricity, the raw material in the production process of chlorine and caustic soda is sodium chloride. Membrane electrolysis plants require sodium chloride with very high purity. Although sodium chloride is an abundant raw material, currently, there are a limited number of manufacturers in Europe that can provide the quality required. To ensure the availability of this product, the Group has signed long-term agreements.

In 2019 the drop in oil prices pushed down the cost of methanol (-14%) and ethylene (-8%), key raw materials for the intermediate chemicals and PVC divisions, respectively.

Methanol is the main raw material of the intermediate chemicals division and is produced from natural gas. The Group has signed supply agreements with various international suppliers from different areas and with different intervals to avoid supplier concentration risk and prevent agreements from renewing at the same time. In 2019 the EU maintained the suspension of the 5.5% tariff on methanol imports, otherwise it would have harmed the Group by making imports of this raw material more expensive.

In 2019 the reduction in the price of ethylene and, above all, the greater availability of chlorine allowed the Group to increase the production of its own EDC—the product that starts the PVC chain—at the cost of reducing the purchase of external EDC (which already incorporates chlorine and part of the ethylene, and the price of which has risen by 18%). This has reduced the Group's dependence on this raw material and prevented further deterioration of the PVC margin. The Group also tries to minimise the risk of price volatility of external EDC by bolstering purchases of this product from shale gas rather than oil.

The following table shows the analysis of the sensitivity of the Group's ebitda to possible variations, all other things being equal, in the price of electricity, ethylene and external EDC:

	Price Variation	Effect on ebitda (EUR thousand)
Electricity	±10 EUR/MWh	±8,060
Ethylene	±100 EUR/t	±5,430
External EDC	±50 EUR/t	±5,370

(v) Risk of product concentration

56% of the Group's activity revolves around the production of chlorine, caustic soda and its derivatives. Chlorine and caustic soda are produced in the same process; however, while chlorine –for safety and efficiency reasons– is consumed practically in full in the production facility during the manufacture of chlorine derivatives, caustic soda is sold worldwide.

The most significant product manufactured from chlorine is PVC, the performance of which is tied to the performance of the construction industry. This fact lends an element of volatility to the price of caustic soda (a chlorine co-product) that must be taken into account in the Group's projected results. As explained in section a) (iii), PVC and caustic soda account for more than one third of the Group's billings.

(vi) Risk of the cyclical nature of products

In general terms, the markets in which the Group operates are more active during the second and third quarters of the year, except for August. In recent years, the trend among customers of reducing orders at the end of the year as a result of Christmas holidays and the general desire to reduce their warehouse stocks at the end of the year has become more pronounced, causing activity to drop in December.

The products with the most notable seasonal shifts are those used for treating and disinfecting water for human use –sodium hypochlorite, sodium chlorite and trichloroisocyanuric acid–, use of which peaks in the summer, and PVC, consumption that is slower in the cold months of the year due to the stoppage in construction. Demand for other products is steady throughout the year, except in August and December.

As explained in point (iii) above, the chemical industry in which the Group carries out its activity is characterised by its cyclical nature. Therefore, the Group is not immune to the market uncertainties generated by changes in supply and demand, whose repercussions on the margins of the products it sells can affect their profitability and, on occasion, earlier and with greater intensity than in other sectors given that its products are commodities.

(vii) Risk of customer concentration

Although no customer represents more than 10% of the Ercros Group's billings, it is worth highlighting the importance of the main chlorine customer, which currently consumes nearly 40% of the chlorine produced by the Group.

At the end of 2017, this customer announced that it would be building its own chlorine plant to meet the needs of its factory. The start-up of the aforementioned plant, which was scheduled for the end of 2020, is delayed. Therefore, in 2019 the Ercros Group renewed the chlorine supply agreement with this customer until 31 December 2021. If supplies to this customer were not to continue after 2022, the Group would rearrange the distribution of the chlorine available for the manufacture of its own EDC that would mean increasing ethylene purchases, ceasing to purchase external EDC and, foreseeably, ceasing production of dicalcium phosphate, which could affect the Group's overall profitability.

In 2019 the Group signed a new long-term formaldehyde supply agreement with its main customer for the 2021-2030 period.

(viii) Market risk due to geopolitical tensions

The Group exports 48% of its sales to 88 countries. Given its exposure to foreign markets, the Group may sometimes be influenced by political or geostrategic conflicts that generate tension in the markets where it markets its products.

The uncertainty generated by the social and financial crisis in Turkey last year led to a lack of liquidity in dollars in the Turkish market –where 5% of the Group's exports– are directed. The Group has minimised exposure to risk in this market by marketing its products mainly through a multinational distribution company with headquarters in other countries.

In 2019 the intensification of the trade war between the US and China altered the global flows of certain products. The situation has caused some of the PVC sold by the US in China to be redirected to the European market. However, India's elimination of anti-dumping duties on American PVC (India is the largest importer of this product) led to less American PVC reaching Europe in 2019 than in 2018. The market forecasts that the signing of the first phase of the trade agreement between China and the US in 2020 and the liberalisation measure adopted by India will confirm the reduction of the inflow of American PVC into Europe and restore the global flows of the products concerned.

On the other hand, an increase in tensions between the US and Iran could lead to a shortage of oil and an increase in the price of this product could be transferred to gas, ethylene, methanol and EDC –important inputs for the Group.

In view of the confirmation of the UK's departure from the EU, in 2019 the Ercros Group: (i) conducted a study on the possible direct

impact that a hard Brexit could have on its ebitda; (ii) initiated the registration process for the products it sells in this market (polyols, sodium chlorite and trichloroisocyanuric acid); and (iii) sought alternative suppliers of raw materials and auxiliary chemicals to those it buys in this market. The conclusions of this study revealed that, even under the most adverse scenario, the impact would not be significant since the UK is not a relevant market. Following the country's departure from the EU on 31 January 2020, uncertainty remains as to whether a trade agreement can be reached in time to avoid a hard Brexit.

The current socio-political instability in Chile and Venezuela has no impact on the Group's income statement since it does not sell a significant volume of product in these markets.

At the end of January 2020, the declaration by the WHO of the covid-19 outbreak as an international health emergency increased the uncertainty regarding the future of this market and its impact on the rest of the world. The Group obtains its supplies of certain raw materials from China, which is also a destination market for the Group's products. The Group has a contingency plan to minimise the potential lack of availability of these raw materials as a result of the restrictions on industrial activity in China, should such restrictions be extended.

(ix) Technological and cybersecurity risk

The Group is exposed to cyber risk that could lead to an interruption of its business processes, which would temporarily compromise the Group's normal operations.

To minimise the risk of the discontinuation of operations –arising from failures or incidents in the computer systems– the Group has a specific protection plan for its technological infrastructure within the framework of an operating security plan.

The aforementioned plan addresses security against accidental or intentional internal and external cyber threats. The Group continuously has the means necessary to attempt to prevent, detect and, where applicable, eliminate the cause of this type of threat.

As a preventive measure, specialised external consultants periodically carry out a penetration test, which allows continuous improvements to be applied to its security system.

In the event of an incident that partially or totally interrupts the normal functioning of its business processes, the Group has a disaster recovery plan that would allow the operations of its critical processes to be resumed within a reasonable period of time.

b) Non-financial risks

(i) Environmental risk (relevant)

All Ercros Group factories have environmental management systems in place to minimise the potential impact of the industrial activity on the environment. Even so, in the course of their activity, these centres are subject to risks that may cause environmental harm, such as accidental emissions of harmful substances or fires.

The Group (i) performs the official monitoring of its environmental performance; (ii) conducts external verifications of its sustainability management system; and (iii) carries on its activity in accordance with the emission limits set forth in the applicable laws, relevant licences and based on the voluntary agreements it has signed. Furthermore, it has implemented indices to evaluate its overall emissions into the water and the atmosphere and waste generation, enabling it to verify the performance of its environmental management. The Group periodically reports on the reduction of emissions achieved in its industrial activity.

In 2019 all Ercros Group centres conducted their environmental risk analysis, with the exception of Monzón. This centre is considered a low-risk centre and, therefore, in accordance with the Spanish Environmental Responsibility Act (Ley de responsabilidad ambiental) it is not required to perform such an analysis; however, in 2020 whether such an analysis should be carried out will be assessed.

(ii) Risks related to changes in regulations

In recent years legal requirements in relation to environmental matters have become increasingly demanding and have given rise to significant changes in the chemical industry, in Europe, Spain and at the autonomous community level. The Ercros Group makes a significant effort to adapt to this new legal framework and performs the activities and actions necessary to comply with the requirements set forth in the various regulations. Specifically, legislation related to the safety of facilities and people, occupational health, environmental protection and the transport, packaging and handling of dangerous goods.

Certain of the rules, restrictions and procedures that affect the Group are in the process of being implemented and may change in the future. If this occurs, the Group will adapt to the new requirements.

As regards changes in the energy market, the Group's main risk is the uncertainty arising from the absence of a stable legal framework and the impossibility of knowing at medium term the amount of remuneration and administrative exemptions for energy-intensive companies. This prevents the Group from making predictions about the price of this supply, the weight of which is very significant in its variable costs. To mitigate the impact of this

risk, the Group carries out actions to improve energy efficiency and encourages modulated consumption and the use of renewable energy to reduce the price and environmental impact.

The serious accident that occurred on 14 January 2020 at the factory of a chemical company in Tarragona, in which three people died and seven people were injured, in addition to there being significant material damage to industrial facilities, has called into question the safety and warning measures of factories in the chemical industry. The regional and local authorities have reacted by supporting the demands of local residents, which could translate into even stricter regulations for the entire sector. It is also foreseeable that government licenses and permits will be tightened, which could affect industrial activity.

By 2020, as a result of IMO 2020 coming into force, which requires that ships use very low-sulphur fuel or install scrubbers (exhaust gas cleaning systems), a significant rise in maritime transport costs is expected. The Ercros Group has negotiated new shipping agreements to minimise the impact on freight rates as much as possible.

(iii) Claims risk due to soil remediation

The Ercros Group has a long history of industrial activity and, although it has always complied with and applied the law as it stands at any given time, legal requirements introduced in recent years and their application, some of them retroactively, have raised the risk of claims of pecuniary liability to assume the costs of cleaning-up or remediating affected soils and sites.

The Ercros Group has submitted soil control and remediation and landscape regeneration projects to the competent authorities for all land that has been identified as affected.

The Group estimates the value of the remediation obligations each year and makes the corresponding provisions for remediation.

(iv) Risk of employee claims

Occasionally, the Ercros Group must face claims from former employees, or their heirs, related to compensation for damages arising from asbestos exposure and public benefit surcharges for a lack of safety measures for exposure to asbestos.

These types of liabilities are not attributable to the Group's current management, nor do they relate to damage caused to current, active employees, rather, they are liabilities claimed of the Group as the universal successor of companies that have been defunct for many years and are not related in any way to current activities.

In this connection, in 2019, two new proceedings were commenced and are pending a decision from the courts. In addition, a new

proceeding for public benefit surcharges related to mercury exposure has come to light. To mitigate this risk, the Group has recognised provisions for the amounts it expects could be claimable in the legal proceedings that are still pending resolution.

(v) Human resources risk

The Ercros Group analyses the risks arising from human resource management, including the risk of low productivity due to the high rate of staff absenteeism (4.4% in 2019), which in some workplaces can make it difficult to cover all production shifts. To mitigate the impact of this risk, multidisciplinary working groups have been created to analyse the specific causes and propose concrete solutions.

The Group is also subject to talent risk as a result of the departure of key employees. To mitigate this risk, the Group: (i) makes it easier for its staff to perform their work by implementing social measures and measures to promote a work-family life balance, flexible working hours, etc.; (ii) facilitates personal and professional growth with training plans, payment for master's and postgraduate degrees, and prioritises internal promotion to fill vacant positions; and (iii) encourages loyalty to the Group through long-service bonuses, pension plans and life and health insurance. Given that the level of staff turnover is very low (average service of 19 years in 2019), the Group does not feel it is necessary to implement talent management programmes.

c) Financial risks

In the normal course of its operations, the Group is exposed to credit risk, market risk (interest rate risk and foreign exchange risk) and liquidity risk.

The Group's main financial instruments, other than derivatives, include the syndicated factoring facility, the revolving credit facility, loans from public financial institutions, bank loans, credit facilities, finance leases, cash and short-term deposits.

The Group has no derivatives to hedge interest rates or foreign exchange risk.

In recent years, it has been the Group's policy not to trade with financial instruments.

The Group notes that the financial risk remains within parameters that can be assumed by a cyclical company. The solvency ratio (consolidated net financial debt/consolidated ordinary ebitda) was 1.74 in 2019, under the maximum limit that has been set at 2.

In 2019 the Group maintained the investment pace set out in the 2016-2020 Act Plan, which will involve investments of around EUR 100,000 thousand.

The implementation of the Act Plan is almost complete and, thus, the resources allocated to investments included in the plan in 2019 were significantly lower than in the previous year (-32%). In 2020, the allocation of such resources is expected to decline further.

In addition, at 2019 year end, the financial solvency conditions for shareholder remuneration were met, as provided for in the policy for remunerating shareholders out of the profits from the 2017-2020 period.

(i) Foreign exchange risk (relevant)

The only assets and liabilities exposed to foreign exchange risk are those from the purchases and sales related to the Group's ordinary business. The Group does not have any other assets on its balance sheet that are exposed to foreign exchange risk.

The dollar is –by far– the main currency to which the Group is exposed and it has not arranged any derivatives to hedge this risk.

In 2019 the average dollar-euro exchange rate appreciated by 5.3% to USD 1.118/EUR, which had a positive effect of EUR 2,794 thousand on the Group's ebitda. Net exposure amounted to EUR 50,499 thousand.

An average change of 1.150 has been estimated for 2020. If the dollar loses some of its value against the euro, it could have a negative effect on the Group by worsening the competitive position of the products it sells. Therefore, if this forecast holds true, the Group could see an immaterial reduction in the profitability of its products.

The following table shows a sensitivity analysis to reasonable potential changes in the average dollar exchange rate due to its net exposure to this currency according to 2019 figures, keeping all other variables constant:

Dollar/euro ratio	Effect on ebitda (EUR thousand)
1.25	-5,366
1.20	-3,485
1.15	-1,441
1.12	–
1.10	788
1.05	3,230
1.00	5,916

(ii) Interest rate risk

External financing is based on the syndicated factoring facility, the revolving credit facility and loans from government agencies. The financing accrues interest at variable rates normally tied to Euribor. In this regard, given that interest rates are currently very low, potential increases in the Euribor would entail an increase in the Group's finance costs.

The following table shows a sensitivity analysis to reasonable potential changes in interest rates, keeping all other variables constant:

Increase/decrease in basis points of the cost of the debt	Effect on financial result (EUR thousand)
200	-2,716
100	-1,358
-100	1,358
-200	2,716

(iii) Credit risk

The Group has implemented a customer credit management policy and the exposure to default risk is managed in the normal course of its business. Solvency assessments are carried out on all customers who require a limit greater than a certain amount. Likewise, in certain sales, the Group requires the customer to deliver a letter of credit or a bank guarantee.

The Group's customer portfolio does not have a high concentration.

With respect to the Group's other financial assets, such as cash and cash equivalents, credits, available-for-sale financial assets, the maximum exposure to credit risk is equivalent to the carrying amount of these assets at year end.

(iv) Liquidity risk

The Group manages its liquidity risk by using financial planning techniques. These techniques take into account the cash inflows and outflows from ordinary activities, investments and financing. The Group's objective is to maintain a balance between the flexibility, term, and conditions of the source of financing contracted based on the expected requirements at short, medium and long term.

It should be noted that the significant increase in resources generated by the Group's businesses in 2019 provided the necessary liquidity to meet its obligations on time (payment of investments and shareholder remuneration) and to reduce net financial debt. The Group expects the situation to remain the same in 2020 and, therefore, does not anticipate being exposed to liquidity risk in its transactions.

To extend its available financing lines, until the end of 2022, the Group has a syndicated factoring facility amounting to EUR 102,146 thousand; a revolving line of credit for an overall limit of EUR 30,000 thousand; and a credit with the Instituto de Crédito Oficial ("ICO") amounting to EUR 18,000 thousand maturing in 2026. In addition, if the need arises, the Group believes that it could use other complementary mechanisms to obtain one-off liquidity, such as the partial and selective disposal of assets not used in operations or the issue of short- or medium-term bonds in organised markets.

(v) Tax risk

The group tries to minimise the tax risk arising from its activities. To that end, it strives to comply meticulously with its tax obligations, and avoids taking decisions based on aggressive or controversial interpretations of tax regulations. Nor does it attempt to plan its operations so as to minimise its tax charge through companies located outside of Spain. The Ercros Group receives advisory services from external tax experts to comply with tax regulations and not to assume risks in the interpretation of the regulations.

Practically all the Group's operations are carried out at the parent company, Ercros, S.A., which has its registered office in Spain and pays taxes in full in Spain. Only its marketing subsidiary in France is taxed in that country.

However, occasionally, the tax authorities use criteria to interpret the regulations applicable to the activities carried out by the Group that give rise to discrepancies with the criteria used by the Group itself.

In this connection, in 2017, Ercros submitted a statement of defence to the Central Economic-Administrative Tribunal contesting the definitive tax assessment issued by the tax authorities after their review of the Aranjuez factory due to the exemption applied on the consumption of ethyl alcohol used to manufacture medicine in 2011 and 2012 amounting to EUR 5,300 thousand, of which EUR 4,488 thousand relates to the tax rate and EUR 812 thousand to late-payment interest. On 5 February 2020, the Central Economic-Administrative Tribunal dismissed that appeal and Ercros is now preparing an appeal before the Administrative Division of the National Court of Appeals. The Company has guaranteed, by means of credit insurance, payment of the amount resulting from this assessment, although it has not made any provision as it believes that its claims will be upheld by the National Court of Appeals.

The Company's directors and its legal advisers consider that a tax audit would not give rise to any tax contingencies of a material amount in the event of discrepancies in the interpretation of the tax legislation applicable to the Group's operations.

In 2019 the Group adhered to the Spanish Code of Good Tax Practices.

5.3. Risks materialized during the year

Risk presented in the year	Causes	Functioning of the control systems
Industrial risk	Start-up of production plants.	The Group schedules these implementations to minimize impact on production.
Risk of tighter margins	Weakened demand and excess supply in the caustic soda market.	The Group reaches supply agreements to ensure the sales volume, focusing commercialization on the domestic market with higher profitability and increasing the proportion of own caustic soda sales to the detriment of third-party caustic soda, with has a lower margin.

6.1 Special tax on alcohol

On February 5, 2020 the Central Economic Administrative Court ("TEAC") rejected Ercros's defence allegations against the final tax assessment derived from the inspection carried out by the IRS's technical department on the exemption applied to the use of anhydrous ethanol for the manufacture of drugs, during 2011 and 2012. Ercros Management, supported by its advisors, expects that its defence allegations will be accepted by the chamber for contentious administrative proceedings of the Spanish High Court to which the corresponding appeal will be lodged within two months from the TEAC's resolution.

6.2 Purchase of treasury shares

On February 10, 2020 the board of directors approved the fifth treasury share repurchase program, which will consist of a maximum monetary amount of EUR 18,000 thousand and in no case the number of treasury shares to be purchased can exceed 7% of the Company's current share capital, which consists of 104,916 thousand shares (equal to 7,350 thousand shares). The program will be in force until June 30, 2021. Until February 20, prior to the authorization of the financial statements for issue by the board of directors, the Company has purchased 548,390 treasury shares, for an amount of EUR 1,500 thousand within the framework of said program.

6.3 Ongoing investigation

On February 12, 2020 the Group's headquarters and the Vila-seca I and Vila-seca II factories were searched by order of the court of instruction no. 2 of Tarragona. Said investigation is *sub judice*.

In accordance with the good governance practices established by the Group, the audit committee has started an internal investigation that will also include a forensic analysis carried out by an independent external company.

According to the available information at the date these consolidated financial statements were authorized for issue, no matters that may cause significant impacts have been identified as the investigation is still at an initial stage and is not possible to objectively assess the consequences and impact that may arise from it, if any.

In line with the forecasts suggesting a slowdown of growth in most developed economy, and in particular in Europe, the Group estimates that in 2020 the performance of its businesses will not vary significantly from 2019. The scenario is more optimistic for the intermediate chemicals and pharmaceuticals businesses, whose market show greater robustness, than for the chlorine derivatives business, because of its strong link with the European industrial sector.

All forecasts from specialized sources indicate that in 2020, in line with expected demand, the prices of final outputs will tend to remain at the levels of 2019 year end. Due to the difficulty of obtaining better prices, to defend turnover, the Group has decided to shift its sales strategy to the maintenance of the sales volume and focus its activity on the applications and countries with better returns. One positive aspect of these forecasts is that it is expected that the prices of utilities and consumables will remain stable, which should result in the maintenance of margins.

No significant change in the price of variable expenses is expected, either, or less so, a sudden increase that further damages margins. At the beginning of 2020, the price of the three main utilities -methanol, electricity and ethylene- has continued to decrease and the tipping point cannot be seen. To maintain profitability in a very highly pressured environment, the Group's strategy is to reduce the contractual term of the utility if possible to take full advantage of the present situation of prices.

In the case of electricity, a reduction in the final price of the utility is expected due to the decrease in the electricity wholesale market price and the approval of the electro-intensive consumer bylaws, which will help, if confirmed, to reduce the costs differential with the rest of European countries, enhancing the competitiveness of affected companies, including the Ercros Group. For 2020 the Group also expects that improved energy efficiency and higher operation ratio of the new electrolysis plants allow it to further reduce the production unit cost. It trusts that the aforementioned measures, plus greater modulation of consumption adapted to the hours with lower energy cost, allow it to offset the lesser retribution it currently received for the interruptibility service of power supply.

As for the exchange rate, the forecast for 2020 is that the US dollars depreciates slightly against the euro, which would cause some damage to Ercros's profitability, although the US dollar has appreciated against the euro during the current year so far.

As for fixed costs, the Group's personnel benefits expense will increase for the third year in a row as a result of the 2.5% raise established in the industry agreement.

In the medium term, the Group's challenge is to incorporate new products or specialties to the company's portfolio; open new markets and consolidate its position in certain geographical areas; and increase production of own products to replace third-party products commercialized and thus increase margin.

As a result of all this, the Ercros Group is moderately optimistic about a possible improvement in margins over 2020, which should be achieved through an increase in revenue, higher volume of products sold, maintenance of low prices of the main raw materials and reduction in the cost of energies.

8.1. R&D activities

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. In 2019 innovation costs and investments incurred amounted to EUR 6,099 thousand (EUR 5,983 thousand in 2018).

Ercros has 16 patents and two new applications in progress, on both products and manufacturing processes.

The Group's R&D activities in 2019 have mainly focused on three projects that are carried out in cooperation with the Centre for the Development of Industrial Technology ("CDTI"): (i) the development of the new range of ErcrosGreen+ resins; (ii) the process for obtaining magnesium hydroxide and potassium nitrate; (iii) the process for extracting multiproduct for the active ingredients obtained through biological fermentation.

Within the ErcrosBio project, the Group has continued to work on improving the mechanical and thermal properties of PLA and PHA and on expanding their fields of application.

8.2. Development of products

Below are described the most relevant projects in 2019 regarding the development of new products and the expansion of applications and features of already existing products.

a) In the chlorine derivatives division:

- Formulation of TCCA tablets with several additives that introduce new fragrances and colours.
- Application of PVC and its compounds and copolymers in 3D printing, as well as reprocessing of recycled PVC.
- New materials of the ErcrosBio family with improved properties for packaging, 3D printing and high added value applications.

b) In the intermediate chemicals division:

- Development of a new range of technical polymers as cross-linking agents used as coating in the construction, automotive, food-packaging industries, etc.
- Research for obtaining a new organic compound oriented towards increasing the portfolio of the division with sustainable final outputs.

c) In the pharmaceuticals division:

- Development of new antibiotic active ingredients obtained through fermentation.
- Definition of standard conditions for extractive processes for both new and existing active ingredients.

8.3. Process improvement

These are the most relevant measures taken to improve processes:

- Program in the pilot plant for obtaining chlorine and caustic potash through the zero-gap membrane-based technology, which is more energy-efficient.
- Optimization of the cracker operation conditions at the VCM plant in order to reduce combustion emissions.
- Decrease in the production costs for the PVC polymerization process by simplifying suspension agents and changing auxiliary products.
- Development of new moulding compounds specialties with the expansion of high-density products, which have better features.
- Development of an extraction process for fusidic acid that reduces the use of solvent.

8.4. Collaboration with research centres

In 2019 the Group has developed research lines in cooperation with several reference research centres, including:

- Collaboration programmes with the Centre for Technological and Industrial Development Centro para el Desarrollo Tecnológico Industrial ("CDTI") for the development of a new system for the combined manufacture of magnesium hydroxide and potassium nitrate from common extraction methods in API fermentation processes.
- The ErcrosBio PLA Premium collaboration programme for the development of bioplastic formulations for 3D printing, together with the technological centre Leartiker from Vizcaya and the Catalan Plastic Centre of the Polytechnic University of Catalonia.
- The agreement signed with Leartiker for the development of standard PVC for 3D printing formulations for the Monzón composite factory.
- Agreements for the development of research projects with the Instituto de Tecnología Química de la Universidad Politécnica de Valencia (ITQ-UPV-CSIC) to optimize the polyol production process.
- Agreement with the Centre Tecnològic de Catalunya ("Eurecat") and the Universitat Rovira i Virgili ("URV") for a project for developing and characterizing new resins.
- Agreement, through the Oficina de Transferencia de Resultados de Investigación ("OTRI") of Universidad de Zaragoza, for studying the possibility of using alternative solvents in the production of hydrogen peroxide.
- Agreement with Instituto Químico de Sarriá ("IQS") for doing research on the development of industrial processes for generic drugs and thermal stabilization of copolymers.
- Sponsorship of the UAM-Ercros chair of Universidad Autónoma de Madrid ("UAM") for the promotion of research and teaching activities in the pharmaceutical chemistry area.
- Cooperation in the PhD dissertation 'New bioplastic materials with a barrier effect' by José Ignacio Valero, a chemical engineer who works at the Group's R&D&Ei department. The dissertation is the result of the cooperation agreement signed between the Ercros Group and UPC.

The Group also cooperates with the Consejo Superior de Investigaciones Científicas ("CSIC"); the Citius program from Universidad Autónoma de Barcelona ("UAB"); the Eurecat; and the Instituto Polymat from Universidad del País Vasco.

Over 2019 the Company paid 4,545 thousand shares to purchase 1,369 thousand treasury shares, which means an average price of 3.3 EUR /share. These treasury shares were purchased for redemption purposes, in compliance with the shareholder remuneration policy [see chapter 10.1 b) (ii)].

These 1,369 thousand treasury shares acquired in 2019, together with the 1,592 thousand treasury shares that had been purchased in 2018 (2,961 thousand treasury shares in total) were redeemed through a capital decrease of EUR 888,240, which was filed on August 23, 2019 with the Barcelona Mercantile Registry.

These 2,961 thousand treasury shares were bought within the third and fourth repurchase programs, following the authorization granted by the shareholders at the meeting held on June 23, 2017. The conditions regarding price and volume were in accordance with those 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 was Solventis A.V., S.A.

After the end of the fourth repurchase program, on February 10, 2020, the board of directors approved the fifth program, also following the authorization from the shareholders in June 2017. The maximum amount of this new program is EUR 18,000 thousand and in no case can the number of treasury shares to be acquired exceed 7% of share capita after the approval (this is equal to 7,350 thousand shares). The program will remain effective until June 30, 2021. The conditions regarding price and volume are the ones legally established. The company designated as the main manager in the fifth program is Banco de Sabadell, S.A.

The four programs carried out from the end of 2016 to date, within the shareholder remuneration policy framework, have meant the purchase of 9,17 million treasury shares, whose redemption has resulted in a capital decrease of EUR 2.75 million, that is a 8.03% reduction in initial share capital.

The table below shows the programs already completed and the fifth program that is currently being carried out:

Program	Resolution by the shareholders' meeting	Approval by the board of directors	Start date	End date	No. of shares acquired (thousands)	Total amount (EUR thousand)	Nominal amount (EUR thousand)	Share capital (%)	Average price (euros/share)
First	6-10-16	6-10-16	1-20-17	3-27-17	3,107	9,000	0.932	2.7	2.897
Second	6-23-17	7-26-17	10-04-17	3-09-18	2,117	6,030	0.635	1.9	2.849
Third	6-23-17	2-23-18	3-12-18	7-09-18	1,440	5,970	0.432	1.3	4.147
Fourth	6-23-17	6-15-18	7-09-18	6-30-19	2,508	9,502	0.752	2.3	3.789
Fifth	6-23-17	2-10-20	2-12-20	6-30-21	548 ¹	1,500 ¹	0.165 ¹	0.5 ¹	2.735 ¹

¹ Up to February 20, 2020.

10.1. Shareholder remuneration

a) Shareholder remuneration policy

Ercros's 2017-2020 shareholder remuneration policy was ratified by the shareholders at the ordinary general meeting held on June 23, 2017.

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 2019 these conditions were met since EPS were EUR0.292 (EUR 0.408 in 2018), the solvency ratio was 1.74 (1.67 in 2018) and the leverage ratio was 0.38 (0.46 in 2018) [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 2019

(i) Against 2019 profit

As indicated in subsection a) above, in 2019 the requirements established in the shareholder remuneration policy were met. Consequently, the board of directors –at the meeting held on February 21, 2020– resolved to propose the shareholders in general meeting the payment of a dividend of EUR 0.05 gross per share, which will mean EUR 5,246 thousand s and a 16.9% payout over the consolidated profit obtained by the Group in 2019. This percentage exceeds the minimum established for that year in the shareholder remuneration policy, which is 16%.

Considering the payout involved in the payment of the dividend and given that, in accordance with the shareholder remuneration policy for 2019, the overall payout amounts to 45% of 2019 consolidated profit, the payout to purchase treasury shares will be 28.1% of said profit, which means an amount of EUR 8,735 thousand.

The repurchase of these treasury shares will take place in 2020, under the fifth repurchase program that was approved by the board of directors on February 10, 2020. Until February 20, prior to the authorization of this report for issue by the board of directors, the Company has purchased 548,390 treasury shares, for an amount of EUR 1,500 thousand.

In 2019 the Company paid EUR 11,216 thousand to remunerate the shareholders. Of this amount, EUR 4,545 thousand were allocated to the acquisition of treasury shares against 2018; EUR 6,295 thousand to the dividend payout also against 2018; and EUR 376 thousand to the payment of the 2019 general meeting attendance bonus.

(ii) Against 2018 profit

On June 25, 2019 the Company proposed a dividend distribution of EUR 0.06 gross per share, against 2018 consolidated profit. This means an amount of EUR 6,473 thousand and accounts for a payout of 14.5% of 2018 profit. The 2,961 thousand treasury shares held by the Company were excluded from the receipt of dividends, which meant an effective payout of EUR 6,295 thousand.

Also against 2018 consolidated profit, the Company acquired treasury shares for redemption for an amount of EUR 11,477 (of which EUR 6,932 were paid in 2018 and EUR 4,545 in 2019), which accounts for a 25.7% payout of 2018 profit, thus completing the payout estimated in the shareholder remuneration policy for the current year (40.3%).

In 2018 the Company paid EUR 19,699 thousand to remunerate the shareholders. Of this amount, EUR 7,024 thousand were allocated to the acquisition of treasury shares against 2017; EUR 6,932 thousand to the acquisition of treasury shares against 2018; EUR 5,372 thousand to the 2017 dividend payout; and EUR 371 thousand to the payment of the 2018 general meeting attendance bonus.

The table below shows the amounts paid and proposed in 2019 and 2018 for the payment of dividends and the payout made for the repurchase of treasury shares:

EUR thousand	Year 2019	Year 2018
Paid dividends	6,295	5,372
Against 2017 (0.05 euros/share)		5,372
Against 2018 (0.06 euros/share)	6,295	
Proposed dividends	5,246	6,473
Against 2018 (0.06 euros/share)		6,473
Against 2019 (0.05 euros/share)	5,246	
Payment for the purchase of treasury shares	4,545	13,956
Against 2017		7,024
Against 2018	4,545	6,932
Against 2019	0	

10.2. Stock market information**a) Share capital**

On August 23, 2019 the Barcelona Mercantile Registry filed a capital decrease in Ercros amounting to EUR 888,240, corresponding to the nominal amount of the 2,961 thousand treasury shares that the Company had purchased between May 21, 2018 and April 27, 2019 for redeeming them within the framework of the shareholder remuneration policy. The redemption of these shares reduced the number of shares by 2.7% and meant a payout of EUR 11,477 thousand for the Company.

After this transaction and until the moment this CMR was approved –February 21, 2020–, Ercros's share capital amounts to EUR 31,475 thousand and is represented by 104,916 thousand ordinary shares with a nominal value of EUR 0.30 each.

The table below shows the evolution of Ercros's share capital between 2018 and 2019:

	Share capital (EUR)	Number of shares
At 12-31-18	32,362,986.30	107,876,621
Capital reduction	-888,240.00	-2,960,800
At 12-31-19	31,474,746.30	104,915,821

Main share-related parameters

	12-31-19	12-31-18	12-31-17	12-31-16	12-31-15
Shares on the stock market	104,915,821 ¹	107,876,621 ²	110,979,611 ³	114,086,471	114,086,471 ⁴
Market capitalization (EUR)	268,584,501	335,496,291	317,401,687	209,919,106	70,277,266
Traded shares:					
In the course of the year	88,224,937	128,748,505	186,848,681	130,902,035	92,905,410
Highest in one day	2,413,214	3,814,986	3,618,126	4,700,641	5,918,106
Lowest in one day	84,469	92,124	111,569	24,004	16,737
Daily average	345,980	504,896	732,739	509,346	362,911
Traded volume (EUR):					
In the course of the year	220,569,600	526,361,941	536,068,883	187,864,193	55,992,629
Daily average	864,979	2,064,165	2,102,231	730,990	218,721
Share price (EUR):					
Highest	3.95	5.57	3.63	2.41	0.86
Lowest	1.56	2.66	1.83	0.44	0.39
Average	2.50	4.09	2.87	1.44	0.60
Last	2.56	3.11	2.86	1.84	0.62
Frequency rate (%)	100	100	100	100	100
Liquidity rate (%)	84.09	119.35	168.36	114.74	81.43

¹ Yearly average 2019= 105,824,340 shares.

² Yearly average 2018= 109,610,895 shares.

³ Yearly average 2017= 112,801,167 shares.

⁴ Yearly average 2015= 113,987,683 shares.

b) Share evolution

Despite the recovery of the share's quoted price as from the middle of August, 2019 has not been a good year for Ercros shares, which has shown lower figures than in 2018 in all parameters (quoted price, traded shares and traded cash).

Ercros closed 2019 with a market capitalization of EUR 268,585 thousand (EUR 335,928 thousand in 2018). At December 31, Ercros share's quoted price was EUR 2.56 (2018: EUR 3.11).

Ercros share reached the highest quoted price on February 19 (EUR 3.95). In 2019 the average quoted price was EUR 2.5 (2018: EUR 4.1).

The overall volume of traded cash amounted to EUR 220,570 thousand (EUR 526,362 thousand in 2018) since the number of traded shares amounted to 88,225 thousand (126,749 thousand in 2018).

The day on which the highest number of securities was traded was November 26, 2019 2,413 miles. The yearly average purchase was 345,980 securities.

c) Key stock market ratios

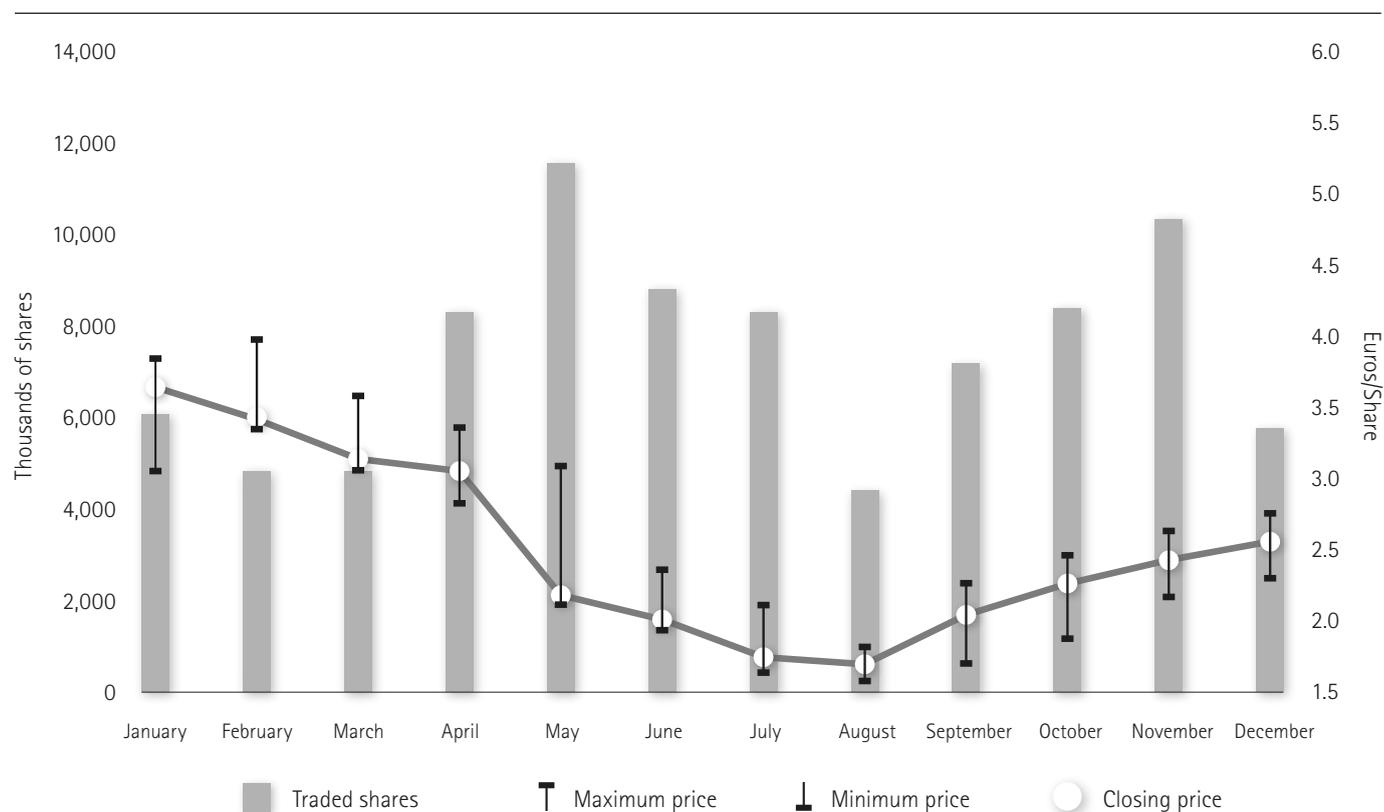
Between 2018 and 2019 CFA –calculated as the operating cash flow divided by the number of shares– has significantly improved from 0.45 to 0.56. This increase is related to the high volume of funds generated in the prior year. CFA is a ratio that allows the Group to measure the generated cash flow corresponding to each share.

The decrease in quoted price and the reduction in the number of shares in share capital has damaged EPS, which has gone down from 0.408 euros/share in 2018 to 0.293 euros/share in 2019. This ratio is the profit for the year divided by the weighted average price of outstanding shares considering the redemption of 2,961 thousand treasury shares and is used to measure earnings per share.

In 2019 PER –calculated by the number of times that market capitalization is included in profit for the year– has been slightly reduced compared to 2018 PER: from 7.52 times to 8.65.

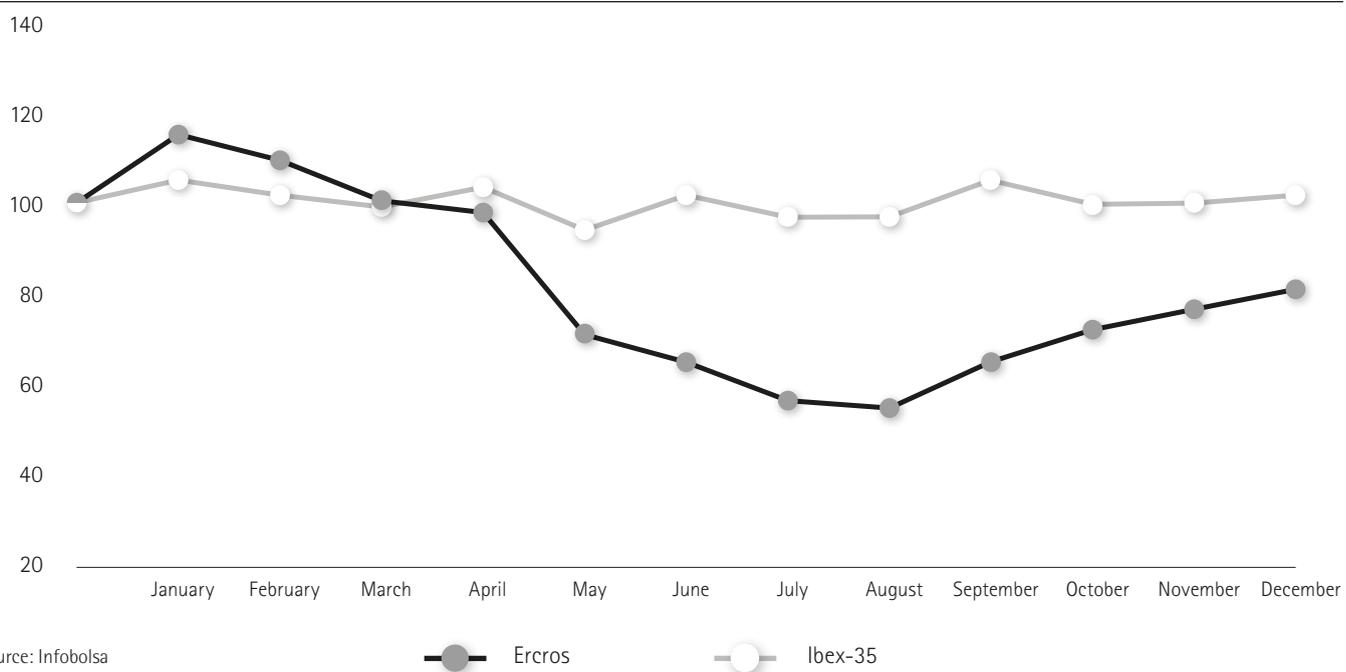
In the reference period P/BV –market capitalization divided by total equity and relates the Company share's value in the stock exchange to its underlying net carrying amount– decreased from 1.23 in 2018 to 0.92 in 2019.

Evolution of share and traded volume in 2019



Comparison between Ercros and Ibex-35 in 2019

BASE 100= 12-31-18



Source: Infobolsa

d) Significant shareholders

On September 13, 2019 the shareholder Joan Casas reported an increase in his ownership interest of up to 5.1%, as a result of the capital reduction carried out by Company on August 23, 2019. The other significant shareholders have kept their number of shares, although their interests in share capital have increased by 2.7% as a result of said reduction.

According to the shareholder communications to the Spanish National Securities Market Commission ("CNMV" by its acronym in Spanish), at December 31, 2019 the shareholders that hold significant ownership interest own directly or indirectly 17,865 thousand shares in Ercros's share capital, which account for 17.1% therein, according to the following detail:

Name or corporate name of shareholder	No. of direct shares (thousands)	No. of indirect shares (thousands)	Interest in share capital (%) ¹
Dimensional Fund Advisors	–	5,557 ²	5.3
Joan Casas Galofré	5,357	–	5.1
Victor Manuel Rodríguez Martín	3,634	–	3.5
Montserrat García Pruns	3,317	–	3.2

¹ The percentages are calculated over the number of shares that make up the share capital at December 31, 2019.

² It includes the direct ownership interest of its subsidiary, DFA International Small Cap Value Portfolio, for 3,330 thousand shares, and thus, it is also a significant shareholder of Ercros.

The Company's free float at December 31, 2019 is estimated at 82.9%.

Between December 31, 2018 and 2019, 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 increased from 0.093% to 0.095%.

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 b) above.

d) Ordinary shareholders' meeting

See chapter 2.1 a).

e) Approval of the criminal risk prevention handbook and the compliance policy

See chapter 2.1 b).

f) Approval of the audit committee and the appointments and remuneration committee regulations

See chapter 2.1 b) (i) and (ii).

g) Capacity extensions in production

See chapter 2.3 c).

h) Renewal of the formaldehyde and chlorine supply agreements

At the end of 2017, the main chlorine customer, whose consumption currently accounts for 40% of the chlorine produced by the Group, announced that it would build its own chlorine plant to cover the needs of its factory. The start-up of the plant, which was expected by the end of 2020, is falling behind schedule. Consequently, the Ercros Group renewed the chlorine supply agreement with this customer until December 31, 2021.

In 2019 the Group signed a new long-term formaldehyde supply agreement with its main customer for the 2021-2030 period.

The Ercros Group publishes an annual corporate governance report ("ACGR") in compliance with article 540 of the Spanish Corporate Enterprises Act ("CEA"). The ACGR is part of this CMR 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 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, 2019 is available on Ercros's (www.ercros.es) and CNMV's (www.cnmv.es) websites.

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 CMR 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, 2019 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	46
13.2. Consolidated statement of comprehensive income	48
13.3. Consolidated statement of changes in total equity	49
13.4. Consolidated cash flow statement	50

EUR THOUSAND

Assets	12-31-19	12-31-18 restated	01-01-18 restated
Non-current assets	405,035	387,735	373,239
Property, plant and equipment	296,937	281,689	269,388
Investment property	30,456	37,588	37,588
Intangible assets	6,795	4,226	4,097
Right-of-use lease assets ¹	12,933	18,821	22,793
Investments accounted for using the equity method	6,654	6,840	6,428
Financial assets	10,997	6,871	7,014
Deferred tax assets	40,263	31,700	25,931
Current assets	251,380	237,657	248,727
Inventories	82,244	97,675	79,739
Trade and other receivables	86,595	98,656	123,040
Other current assets	11,051	13,138	20,297
Current income tax assets	10,373	12,343	2,908
Cash and cash equivalents	61,117	15,845	22,743
Total assets	656,415	625,392	621,966

¹ The amounts at December 31, 2018 and at January 1, 2018 for this caption have been restated as a result of the first-time application in 2019 of IFRS 16.

EUR THOUSAND

Equity and liabilities	12-31-19	12-31-18 restated	01-01-18 restated
Total equity attributable to owners of the controlling entity¹	292,083	272,256	247,361
Total liabilities	364,332	353,136	374,605
Non-current liabilities	120,937	112,191	124,149
Loans	65,984	48,393	46,258
Lease payables ¹	6,760	12,189	16,535
Deferred tax liabilities	24,114	25,678	25,763
Provisions for environmental remediation	9,286	12,533	19,527
Other provisions	2,010	2,819	7,273
Commitments to active staff	1,965	1,798	1,302
Other liabilities	—	137	266
Accrued income and grants	10,818	8,644	7,225
Current liabilities	243,395	240,945	250,456
Loans	92,864	73,979	67,797
Current portion of non-current loans	10,309	9,858	11,823
Lease payables ¹	6,618	7,045	6,389
Trade payables	101,226	107,655	118,654
Provisions for environmental remediation	6,208	16,580	12,993
Other provisions	7,796	8,304	9,767
Other liabilities	18,374	17,524	23,033
Total equity and liabilities	656,415	625,392	621,966

¹ The amounts corresponding to December 31, 2018 and at January 1, 2018 for these captions have been restated as a result of the first-time application in 2019 of IFRS 16.

13.2

Consolidated statement of comprehensive income

EUR THOUSAND

	Year 2019	Year 2018 restated
Income	689,073	684,802
Sale of finished products	638,737	639,543
Rendering of services	31,045	32,397
Other income	13,466	8,364
Reversal of provisions and other non-recurring income	2,233	1,821
Increase in inventory of finished products and work in progress	444	2,677
Gains/(losses) on disposals of investment properties	3,148	—
Expenses	-628,169	-613,690
Consumption of raw material and secondary materials	-343,573	-341,780
Utilities	-96,171	-96,027
Employee benefits expense	-83,127	-79,870
Other expenses ¹	-97,461	-89,659
Charge of provisions and other non-recurring income	-7,837	-6,354
Gross operating profit ("ebitda")	60,904	71,112
Depreciation and amortization expense ¹	-26,576	-26,365
Impairment of assets	-5,615	—
Operating profit ("ebit")	28,713	44,747
Finance income	1,109	142
Finance costs ¹	-7,159	-7,081
Losses on disposal of financial assets at amortized cost	-281	—
Impairment losses on financial assets	-97	-701
Exchange gains	-74	-521
Share in the profit of associated companies	414	1,132
Finance cost	-6,088	-7,029
Profit before tax	22,625	37,718
Income tax income	8,418	6,876
Profit for the year attributable to owners of the parent	31,043	44,594
Profit per basic and diluted share (euros)	0.2924	0.4085

¹ The amounts corresponding to December 31, 2018 and at January 1, 2018 for these captions have been restated as a result of the first-time application in 2019 of IFRS 16.

13.3

Consolidated statement of changes in total equity

EUR THOUSAND

	Share capital	Other reserves	Treasury shares acquired	Profit for the year	Equity
Balance at 01-01-18	33,294	172,707	-3,001	44,492	247,492
Adjustments to balances ¹	–	-131	–	–	-131
Restated balance at 01-01-18 ¹	33,294	172,576	-3,001	44,492	247,361
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 ¹	32,363	202,231	-6,932	44,876	272,538
Adjustments to balances ¹	–	–	–	-282	-282
Restated balance at 12-31-18 ¹	32,363	202,231	-6,932	44,594	272,256
Transfer of 2018 retained earnings	–	38,299	–	-38,299	–
Dividends	–	–	–	-6,295	-6,295
2019 comprehensive income	–	–	–	31,043	31,043
Transactions with shareholders and owners:					
Meeting attendance bonus	–	-376	–	–	-376
Purchase of treasury shares	–	–	-4,545	–	-4,545
Redemption of treasury shares	-888	-10,589	11,477	–	–
Balance at 12-31-19	31,475	229,565	–	31,043	292,083

¹ The amounts corresponding to December 31, 2018 and at January 1, 2018 for these captions have been restated as a result of the first-time application in 2019 of IFRS 16.

13.4

Consolidated cash flow statement

EUR THOUSAND

	2019	2018 ¹
A) Cash flows from operating activities	59,431	48,210
Customer collections	761,775	769,315
Proceeds from the net variation in the non-recourse tranche of the factoring facility	3,145	7,255
Payments to suppliers ¹	-599,280	-623,125
Proceeds from/payments on VAT returns	1,231	1,367
Payments to and on account of ordinary employees	-80,597	-76,294
Payments to and on account of retired employees on the payroll and collective dismissal	-1,618	-5,107
Payments against provisions for environmental remediation	-20,281	-7,727
Payments against other provisions	-3,102	-1,633
Other operating proceeds/payments	-443	-823
Grants received related to indirect CO ₂ emissions	6,056	1,390
Other grants received	472	311
Interest paid	-5,065	-4,838
Interest received	111	131
Payments on / proceeds from net exchange gains (losses)	-111	-541
Dividends received	600	720
Proceeds from prior years' income tax refund	4,618	–
Payment on account of the income tax for the year	-4,172	-8,306
Payments of local and other taxes	-3,908	-3,885
B) Cash flows from investing activities	-31,352	-42,111
Acquisition of intangible assets	–	-540
Purchase of property, plant, and equipment:		
Investments in capacity extension	-21,469	-32,330
Other investments	-15,631	-9,241
Disposal of investment property	5,748	–
Free cash flows (A+B)	28,079	6,099
C) Shareholder remuneration	-11,216	-19,699
Purchase of treasury shares	-4,545	-13,956
Payment of meeting attendance bonus	-376	-371
Dividends paid	-6,295	-5,372
D) Cash flows from financing activities	28,301	6,593
Amounts drawn down on non-current loans	27,257	10,815
Repayment and redemption of non-current loans	-12,218	-10,868
Net variation of current revolving lines	21,287	5,536
New finance lease arrangements ¹	1,189	2,699
Finance lease payables ¹	-7,045	-6,389
Cancellation of deposits	789	5,457
Constitution of deposits	-2,958	-657
E) Net increase/decrease in cash and cash equivalents (A+B+C+D)	45,164	-7,007
Cash and cash equivalents at the beginning of the period	15,845	22,743
Effect of foreign exchange rate	108	109
Cash and cash equivalents at the end of the period	61,117	15,845

¹ The amounts corresponding to 2018 fiscal year for these captions have been restated as a result of the first-time application in 2019 of IFRS 16.



14

HISTORICAL DATA SERIES

- 14.1. Consolidated statement of financial position 52
- 14.2. Consolidated statement of comprehensive income 53

14.1

Consolidated statement of financial position

EUR THOUSAND

Assets	12-31-19	12-31-18 ¹	12-31-17 ¹	12-31-16	12-31-15
Non-current assets	405,035	387,735	373,239	305,620	284,711
Property, plant and equipment	296,937	281,689	269,388	249,231	235,296
Other non-current assets	108,098	106,046	103,851	56,389	49,415
Current assets	251,380	237,657	248,727	254,561	226,956
Inventories	82,244	97,675	79,739	72,009	57,854
Trade and other receivable	86,595	98,656	123,040	102,135	113,496
Other current assets and cash	82,541	41,326	45,948	80,417	55,606
Non-current assets held for sale	—	—	—	—	—
Total assets	656,415	625,392	621,966	560,181	511,667
Equity and liabilities					
Equity	292,083	272,256	247,361	219,826	175,878
Non-current liabilities	120,937	112,191	124,149	124,298	104,496
Long-term loans	65,984	48,393	46,258	58,811	42,772
Long-term provisions	13,261	17,150	28,102	35,080	30,789
Deferred tax liabilities and other non-current liabilities	41,692	46,648	49,789	30,407	30,935
Current liabilities	243,395	240,945	250,456	216,057	231,293
Short-term loans	103,173	83,837	79,620	89,341	98,375
Trade accounts payable and other accounts payable	101,226	107,655	118,654	106,855	115,548
Provisions and other current liabilities	38,996	49,453	52,182	19,861	17,370
Equity and total liabilities	656,415	625,392	621,966	560,181	511,667

¹ Some amounts do not correspond to those reflected in the consolidated financial statements for the years 2018 and 2017 as they have been restated by application of IFRS 16.

14.2

Consolidated statement of comprehensive income

EUR THOUSAND

	Year 2019	Year 2018 ¹	Year 2017 ¹	Year 2016	Year 2015
Income	689,073	684,802	694,037	619,589	627,213
Turnover	669,782	671,940	681,470	602,543	618,275
Other operating income and variation in inventories	19,291	12,862	12,567	17,046	8,938
Expenses	-628,169	-613,690	-619,726	-561,159	-594,589
Supplies	-343,573	-341,780	-316,581	-270,215	-301,213
Staff	-83,127	-79,870	-83,387	-81,822	-79,863
Other operating expenses	-201,469	-192,040	-219,758	-209,122	-213,513
Gross operating income ("ebitda")	60,904	71,112	74,311	58,430	32,624
Depreciation	-26,576	-26,365	-18,252	-19,371	-19,874
Profit/loss from impairment of assets	-5,615	–	–	11,990	–
Costs for abandoning mercury technology	–	–	-21,732	–	–
Operating profit ("ebit")	28,713	44,747	34,327	51,049	12,750
Financial result	-6,088	-7,029	-5,644	-5,727	-6,001
Earnings before taxes	22,625	37,718	28,683	45,322	6,749
Result of interrupted activities	–	–	–	–	–
Income taxes and non-controlling interests	8,418	6,876	15,899	-157	478
Another comprehensive result	–	–	-90	–	–
Profit of the year	31,043	44,594	44,492	45,165	7,227

¹ Some amounts do not correspond to those reflected in the consolidated financial statements for the years 2018 and 2017 as they have been restated by application of IFRS 16.

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