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Dear Paolo,

Thank you for your thoughtful letter dated 1st September.

We genuinely appreciate your kind remarks about the constructive nature of our dialogue as well as the open minded way you and your colleagues have been ready to discuss even some of the more radical ideas we have brought to you for delivering shareholder value. While shareholder value ranks highly amongst our priorities, we recognise that no change is likely to take place unless the public interest is also served and in this context we are just as mindful as to the consequences of our proposals on employment, energy prices, security of supply and the Italian public sector deficit, *inter alia*. As committed shareholders of Eni, we would like to continue with these discussions – in a similar constructive vein – taking into account the objections mentioned in your letter where these are relevant, as well as the public interest.

There are two key issues raised by your letter that we would like to explore further: the valuation of Eni and the synergies associated with keeping certain parts of the Group together. As you know, we believe that Eni's valuation is severely handicapped by the Group's conglomerate structure and that more than € 50 billion of value could be released by spinning off to the shareholders (including the Italian Treasury) the Group's large and very valuable downstream business.

The conglomerate nature of the Group also creates an inefficient structure from a financial point of view, as it does not allow Eni to obtain full access to the untapped borrowing capacity that resides in its infrastructure utility. This financial constraint has unnecessarily

resulted in the dividend being cut and, more important still, may also hold back future growth in the E&P division which has increasing capital expenditure requirements[1].

In your letter you recognise that the structure of the Group may have an associated cost but you go on to argue that the benefits of a "single group" structure outweigh the costs. We note, however, that the benefits you allude to relate mainly to synergies between upstream E&P operations and gas marketing (or supply) – not to any synergies with the gas infrastructure businesses which are mostly regulated – and you do not address the issue of Eni's financial constraints.

Valuation

Let us start with the observation that Eni is undervalued, both in relative terms (i.e., compared to its peers) and in absolute terms, a view that we can confidently say is shared by many of your largest institutional shareholders around the world and, it seems, by the Italian Government[2].

In terms of EV/ DACF, which is the multiple most often used by oil sector analysts, Eni trades at a discount to its peers: for 2009E it trades at 5.9x compared to the average of its peers of 7.5x (the range being from 5.9x to 9.5x); for 2010E, Eni trades at 5.3x compared to the industry average of 6.1x (range 4.6x to 8.6x).[3] In terms of P/E, Eni also trades at a discount: for 2009E it trades at 10.9x versus 13.8x for the sector (range 10.9x to 17.6x), and for 2010E Eni trades at 8.3x versus 9.9x for the sector (range 8.3x to 12.9x). This is all the more surprising given that Eni is the only one of the oil majors to own a substantial utility and that utilities (in particular infrastructure utilities) generally trade at much higher multiples than oil companies. For example, in terms of 2009E EV/ DACF, Snam Rete Gas trades at 12.1x (after adjustments for a full year consolidation of Stogit and Italgas). If the market believed that there were significant synergies resulting from the Group's unique structure, then one would expect Eni to trade at a premium to both the oil sector and the utilities sector, instead of a discount to both sectors.

You will no doubt already have seen the valuation of Eni that we published on 30th September, a copy of which we sent to you prior to its release (see Appendix A). The key elements are summarised in the following table.

[1] "*Zubair is one of the most important oil fields in the world. It is one of the very few that is capable of producing more than 1m barrels a day. Because we are going to Iraq, it means that we will not be doing other things …*" Paolo Scaroni quoted in the Financial Times, 13th October 2009.

[2] "*Buy the shares of Eni and Enel because they are undervalued. These are companies that continue to be profitable and, as such, sooner or later the price of their shares will go back to reflecting their true value ...*" President Silvio Berlusconi quoted in Finanza & Mercati, 11th October 2008.

[3] Prices as of 4th September, 2009 and consensus estimates; averages exclude Eni. Peer group includes Exxon, Shell, BP, Total, Chevron, Statoil and BG. Conoco excluded since we view this as a special case.

	Valuation (€ million)				Valuation per Share (€)		
	Low		High		Low		High
Snam Rete Gas	20,467		21,604		5.65		5.96
International Transport	4,978		5,255		1.37		1.45
Supply and Marketing	8,070		9,684		2.23		2.67
Distrigas	3,822		3,822		1.06		1.06
Gas-related equity stakes (including UFG, GVS, AES Torino, stakes in TAG, TMPC, TENP, Transitgas)	3,138		3,610		0.87		1.00
Gas & Power (s/total)	**40,474**		**43,974**		**11.17**		**12.14**
Exploration & Production	64,610		75,379		17.84		20.81
Refining & Marketing	3,538		4,082		0.98		1.13
Petrochemicals	786		943		0.22		0.26
Oil Services & Engineering (including Saipem)	9,664		11,151		2.67		3.08
Oil-related equity stakes (including Galp, Nigeria LNG)	10,616		10,799		2.93		2.98
Other Activities	(1,300)		(1,517)		(0.36)		(0.42)
Corporate & Financial	(464)		(541)		(0.13)		(0.15)
Less:							
Net financial debt	(18,144)		(18,144)		(5.01)		(5.01)
Snam Rete Gas minorities	(5,126)		(5,665)		(1.41)		(1.56)
Saipem minorities	(3,912)		(4,753)		(1.08)		(1.31)
Equity Value	**100,743**		**115,708**		**27.81**		**31.94**

Further to your suggestion that most analysts use a "sum-of-the-parts" valuation methodology when considering how to value Eni, we have examined a number of these valuations in detail and have found that the two areas where we arrive at higher numbers are (i) the gas and power division and (ii) the value of the equity stakes/ associates, which many analysts simply ignore (see Appendix B).

With respect to the gas and power division, which appears to be valued by many oil industry analysts almost as an afterthought, we find that the quality of analysis is often very poor. This is graphically illustrated in the way brokers value Snam Rete Gas, a quoted company (see Appendix C) – the utility analysts valuing it in a very tight band at € 19 to 21 billion (that is to say in line with its market value and RAB) and the oil and gas analysts valuing it at € 10 to 16 billion, that is to say as if it were an oil company!

Some analysts argue that all oil companies trade at a discount to their sum-of-the parts valuation and that a "conglomerate discount" needs also to be applied to Eni. Having examined this point carefully we find that the conglomerate discounts applied by the analysts when fixing their target prices range from as little as 2% to almost 40% (see Appendix B) whereas their target prices are closely bunched. This strongly suggests that what the analysts are really doing is converging on some other metric – such as EV/DACF – and valuing Eni's utility on oil company multiples. In any case, we continue to believe that a sum-of-the-parts methodology is entirely appropriate in this case as we are valuing Eni on a restructured basis (i.e. assuming it is restructured in such a way as to eliminate the conglomerate discount).

Turning now to the E&P division, if one were to deduct the value we place on the gas and power, refining, oil services and petrochemicals divisions, as well as the equity stakes, we see that the implied 2008 EV/DACF multiple being placed on Eni's upstream businesses is just 1.6x[4] compared with 5.6x for Total on a comparable basis (the equivalent numbers using 2009E data being 2.2x for Eni's upstream business and 7.0x for Total).

2008 multiples	**Eni**		**Total**	
	Enterprise Value	**EV/ DACF**	**Enterprise Value**	**EV/ DACF**
Group	**88,514**	**4.6x**	**108,001**	**6.5x**
less:				
Gas & Power	40,474		2,173	
Refining & Marketing	3,538		16,224	
Oil Services	9,664		–	
Petrochemicals	786		2,760	
Equity stakes	10,616		17,166	
Corporate	(464)		(1,876)	
E&P (implied)	**23,900**	**1.6x**	**71,553**	**5.6x**

The discount on which Eni's upstream assets trade relative to Total is not an aberration: we have done similar calculations for Shell, BP, BG, Exxon and Repsol and the implied 2008 EV/ DACF multiples for their E&P assets are all in the range of 5x to 7x. In each case the market is valuing the E&P assets at 3 to 5 times as much as Eni's (or, conversely, the market is ascribing no value at all to Eni's downstream assets).

When considering whether it is reasonable to value Eni's upstream assets relative to Total's (or those of its other peers) like this, one should remember that Eni's upstream portfolio is very similar and in some cases identical to some of these. Appendix D shows that 90% of Eni's 2P reserves are located in the same 14 countries as 70% of Total's – the main areas where there is no overlap being Canada's oil sands and Abu Dhabi (where Total is present) and Egypt (where Eni is present) – so the political risk is not dissimilar. Furthermore, Appendix D also shows that 25-30% of each company's 2P reserves are actually located in the same fields. Clearly, were one to bring BG into the picture, the overlap would include some of these other geographies or assets (cf., for example, BG's positions in Egypt and Karachaganak, its joint venture with Eni and the Kazakh national oil company).

We value Eni's upstream business at a 2009E EV/ DACF multiple of 6x to 7x on a standalone basis (i.e. at a discount or in line with Total), or €65 – 75 billion. As you can see from Appendix B this is very much in line with most analysts' valuations of Eni's upstream business.

[4] Based on Eni's share price of €16.62 on 4th September 2009.

We would like to comment briefly on the discounted cash flow (DCF) methodology for valuing upstream assets which you also refer to in your letter. In our view, the financial markets are on very soft ground when it comes to valuing upstream assets on this basis, mainly because there is insufficient information in the public domain to conduct a robust, field by field analysis using appropriate risk-adjusted discount rates. Nevertheless, for the purposes of completeness, we have tested our upstream valuation with a reserve-based valuation of these assets using $ 65-70 oil prices (sourced from Wood MacKenzie). This gives us a similar value for the upstream assets and a valuation of € 31 per Eni share, which is very close to our own valuation.

Finally, before leaving the comparison between Eni and Total, we are aware of the fact that some market commentators attribute Eni's discount to the fact that the State has a 30% shareholding. This rather naïve point of view fails to take into account that all "national champions" are controlled, directly or indirectly, by their respective Governments. We have no doubt that the French Government, for example, which has no direct shareholding in Total, would take a very close interest in any takeover or restructuring proposal involving Total, just as it did in the case of Suez – where it engineered the merger with State controlled Gaz de France when Enel expressed interest in acquiring it.

Synergies and the public interest

As we see it, Eni's downstream business is comprised of (i) gas pipeline and other infrastructure businesses, both in Italy and leading into Italy, (ii) gas marketing or supply in Italy and Belgium (Distrigas), and (iii) a number of associates and minority equity stakes, such as Union Fenosa Gas and the international pipeline stakes, which are not consolidated. We fully accept that there may be some synergies between these various activities and Eni's E&P business, but it is obvious from the fact that Eni trades at a discount to both the oil sector as well as the utilities sector that the market puts no value on these synergies. Instead, the market identifies a cost to which is attributable to the structure of the Group.

If the market is to place any value on the synergies that may exist between Eni's businesses and weigh these properly against the benefits of restructuring, then the market needs to have more detailed financial information on the synergies in order to reach its own view as to their value.

We discuss below our thoughts on the synergies you discuss in your letter.

(i) Synergies between Eni's upstream and gas marketing (supply) businesses

You argue that the main reason for keeping the gas marketing assets within Eni is that these activities are fundamentally linked to Eni's upstream oil and gas business, delivering significant competitive advantage to the Group as a whole. As an example, you cite Eni's access to Gazprom's Russian upstream assets that are a consequence, you say, of the

"reciprocal set of benefits" that are bundled into Eni's long-term gas supply contract with Gazprom.

The advantages accruing to Eni's upstream business from its partnership with Gazprom are difficult to see since BP, Total and Shell, to mention but three examples, were each able to secure upstream positions in Russia despite their not having comparable downstream businesses like Eni's to offer in exchange.

In any case, from a shareholder's perspective, we question whether Eni should be as keen on Russian upstream assets as it appears to be. It is obvious that if an investor wants exposure to Russian upstream assets the best way of doing so is to buy shares in Gazprom itself since Gazprom offers investors an opportunity to own Russian upstream assets on an implied upstream EV/ DACF multiple of under 2x. Russian upstream assets owned by foreign companies ought, in our view, to be valued at a discount to that figure (given their less advantageous position in the country).

One could perhaps argue that the benefits of Eni's partnership with Gazprom accrue more to Eni's gas marketing business but these long-term supply contracts do not appear to have brought Eni (or its customers, for that matter) much advantage – either in terms of price[5] or in terms of security of supply[6]. It is hard for us to place a value on these synergies since the terms of your contracts with Gazprom are not in the public domain. We would point out, however, that the financial value of these synergies cannot be significant to Eni as a whole since the entire Italian gas marketing business is only worth € 2.50 per share.

(ii) Synergies between Eni's upstream and gas infrastructure businesses

With respect to synergies between your E&P and midstream assets, you cite another example: the strategic relationship that Eni has developed with Algeria, Libya and Egypt (that represent 40% of Eni's upstream production and a significant portion of its gas marketing activities), based on taking an integrated approach to development.

This seems logical: being able to offer access to final customers by pipeline almost certainly provided some competitive advantage to Eni when the North African contracts were initially being set up. But is this a sustainable advantage that can or should be capitalised? We would make the following three observations: (1) given the regulatory environment, the advantage should exist independently of who owns the pipeline, (2) the advantage is

[5] *"We have always said that we pay more for our energy than our competitors and this one of the reasons for our economy's poor competiveness and the low growth in the last 10 years. The data released by the OECD are but the latest confirmation of a fact that is well known to our companies and citizens, which is that they pay more for their energy than the French or Germans …"* Minister Claudio Scajola quoted in Libero, 23rd September 2009.

[6] *"Italy was heavily impacted by the January 2009 gas crisis as there was no alternative for gas in Italy … Western European gas supply is highly diversified -- and was plentiful in January 2009. The main issue is the lack of cross-border capacity and dependency on Russian gas. [Italian] security of supply will come from a well-functioning, competitive, integrated EU gas market …"* Dr Pierre Noël of the Cambridge EPRG at the Knight Vinke conference 'Eni and the structure of the Italian Energy Market', 30th September 2009 in Milan

probably limited to these countries, and may not be repeatable or indeed sustainable, and (3) in other, more remote countries, Eni's true advantage may reside more in its ownership of Saipem than in its minority stakes in the international pipelines that lead into Italy.

We note that no mention is made in your letter of synergies between Eni's E&P and Italian gas infrastructure businesses – for obvious reasons, given the regulatory framework within which the latter operate – but have on occasion heard suggestions that there is an advantage for Eni in owning these businesses as their steady cash flow can be re-invested by the E&P business. This line of thinking is financially absurd and can only destroy value: there can be no sense in taking cash flows which the market is valuing at 12.1x (i.e., SRG) to re-invest in a business which the market is valuing at 2.2x (2009E EV/DACF in each case, see above).

To summarise, while we accept that there could be some synergies between upstream and marketing, it is difficult for the market to give any value to these in the absence of hard evidence as to their financial value. We see no present or future synergies at all between upstream and infrastructure, either in Italy or elsewhere. In order to demonstrate significant competitive advantage, Eni needs to be able to demonstrate that its unusual structure gives it something of great value that its upstream peers (with little or no access to gas customers or infrastructure) were not able to secure and that this advantage is sustainable. The value of the synergies needs to be quantified and the burden of proof is on Eni.

Knight Vinke's proposed restructuring and alternatives

Proposal A: Spinning off OilCo or GasCo (or both)

The initial proposal which we have tabled (see Appendix E) consists of splitting Eni into two specialist companies by means of a spinoff of one or the other to Eni's shareholders: one ("GasCo") comprised of Eni's large and very valuable utility, the other ("OilCo") encompassing all of the Group's upstream and other activities. GasCo consists of Eni's gas and power division – as it is currently configured, including its 51% stake in SRG – *plus the cash flow from some of Eni's most mature/ legacy assets*. The latter are transferred from OilCo to GasCo by means of contracts for difference or swaps (i.e., ownership of these assets continues to reside within OilCo). The value of these "legacy" assets that are to be transferred amounts to approximately € 15 billion and covers approximately 10-15% of Eni's total 2P reserves. Given that half of Eni's € 18 billion of consolidated debt already sits within SRG, OilCo would therefore be completely debt free (and in fact would have net cash) after the transfer of these legacy assets.

While it is true that some utilities, such as GDF-Suez, E.ON or Centrica, have shown an interest in acquiring upstream assets, this is primarily for the purpose of hedging their oil price exposure. These companies tend, therefore, to be interested in the more mature, slow growing or declining assets that are generally no longer attractive to oil companies and their investors. The transfer of Eni's economic interest in the Group's slowest growing (or

declining) assets from OilCo to GasCo has two major advantages: it gives GasCo the commodity hedge that all utilities seek while also giving OilCo a production profile that is no longer burdened by these legacy assets. We estimate that OilCo's organic production growth rate would amount to approximately 11% p.a. over the next five years – compared to 1-2% for Eni today – and that as one of the fastest growing oil majors with no debt, OilCo would almost certainly be given a higher rating by the stock market than Eni has today.

Utilities (and in particular infrastructure utilities) can sustain much higher levels of debt – for any given credit rating – than oil companies. Although Eni clearly does benefit somewhat from the utility that sits within its structure (see Appendix F), the rating agencies have made it clear that Eni's financial leverage has gone as far as they will permit (given the Group's AA credit rating) and this appears to have precipitated the cut in Eni's dividend earlier this year[7]. Without questioning the fact that Eni is not alone in facing financial constraints of this nature, Eni is unique in having untapped borrowing capacity within its utility business that can be unlocked without placing its credit ratings at risk.

It has been argued by some observers that Eni needs to remain large so as to be able to negotiate from a position of strength with gas suppliers such as Gazprom and Sonatrach. This is certainly true, but GasCo, as we have described it, would be a <u>very</u> large company – larger even than E.ON – and what matters most to these gas suppliers is access to a large market, which is something that would not change as a result of the proposed restructuring of Eni. With respect to OilCo, size is also of importance, but once again, Eni is not as "large" or as strong as a debt free/ cash rich OilCo would be, particularly given the financial constraints that Eni faces today as a result of its inefficient structure. Furthermore, having highly rated shares as a currency for acquisitions may give OilCo the scope to make far bolder acquisitions or mergers than Eni is able or willing to contemplate today.

It should be obvious that the Italian Treasury would remain a 30% shareholder in both OilCo and GasCo as a result of the proposed spinoff, but the option remains for Eni to spin off 70% of <u>each</u> of OilCo and GasCo – to its existing institutional and retail shareholders – leaving the Treasury as the sole shareholder of Eni. Eni would thus become a pure State holding company with a 30% interest in two companies each worth approximately as much as all of Eni is worth today.

As a final thought, going back to the subject of synergies, it seems to us that there could be true advantage to be gained from combining OilCo with a major upstream player with contiguous or shared joint venture assets. This goes far beyond what we are proposing, but there would undoubtedly be huge additional value to be created from combining Eni's stakes in Kazakhstan, Nigeria, Algeria, Egypt, Congo etc. with those belonging to BG, Shell or

[7] "*Eni's financial policy is moderate rather than conservative … the group's debt policy is moderate too, with gearing (defined as net financial debt to equity) below 40% (38% at end-2008); under our current oil price assumptions, maintaining leverage at the 40% level could result in rating pressure …*" S&P, 31st July 2009.

Total, say, to create a much larger European oil major. This would require that the Treasury be prepared to accept some dilution of its interest in OilCo, but having a 30% shareholding is not the only way of maintaining control (as demonstrated by the example of France, mentioned above).

Alternative B: Spinning off Netco

As we have pointed out, although Eni's gas marketing business in Italy is very significant, its value is small within the context of Eni as a whole – approximately € 2.50 per share – and is likely to become even smaller if the Competition Authorities in Brussels (and the Autorità) are successful in imposing the structural remedies they are seeking which will increase competition.

We believe that an alternative solution to the one we initially proposed would be for SRG to acquire from Eni (for approximately € 6 to 7 billion in cash) all of Eni's remaining infrastructure assets and stakes, thereby creating a much larger pure infrastructure company ("Netco"). Eni would then spin off to its shareholders (including the Italian Treasury) all of its interest in Netco, thereby deconsolidating the debt that resided within SRG (€ 9 billion) and leaving Eni with almost no net debt (€ 9 billion remaining less the € 6 to 7 billion in cash received from Netco). As a mostly regulated low-risk utility, we believe that Netco would be able to sustain this level of debt while maintaining an investment grade credit rating.

We believe that this solution would deliver to Eni's shareholders a large part of the 100% upside that we see in the stock while resolving, but to a lesser degree, the financial constraints that indirectly burden the E&P business. This solution would also allow Eni to retain the synergies that it sees from keeping gas marketing and E&P under one roof. It would not, however, remove the slow growing legacy assets from Eni's E&P division and the latter would continue to remain under pressure from the market to make acquisitions so as to match its better performing peers in terms of production growth.

As you know, we have almost a third of our funds under management invested in Eni and care deeply about the Company and its ability to deliver sustainable value for all its stakeholders. We also reaffirm the high regard that we have for Eni's senior management team.

With kind regards

Eric Knight   Glen Suarez

cc: Mr Giulio Tremonti, Minister of Economy and Finance