

Integrated Management Report 2020

Leading today's  
energy into our

*future*

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# Strategic framework



## 2.1.

## How we plan the future

After a particularly unpredictable year, we all realise that in the complex system in which we live, the future should never be taken for granted. Some trends saw a clear acceleration, such as digitalisation and the energy transition, while others, which seemed obvious, such as globalisation, were called into question.

In order to ensure that we are prepared for a wide range of possible futures, namely their impact on the energy value chain in different geographies, Galp includes in its strategic planning a process of critical reflection on the future. This encompasses, among other aspects, the conception of scenarios that we consider to be credible depending on the possible evolution of a group of uncertainties.

In order to ensure that Galp is part of the solution to face today's and tomorrow's challenges and to guarantee the resilience of our strategy, we have developed two alternative and contrasting scenarios. These scenarios are based on the premise that technological development is and will continue to advance and contribute positively to less carbon intensive energy solutions. However, uncertainty related to the global agreement on carbon emissions reduction and its potential impact on global trade agreements should play a key role in unlocking future technologies and accelerating the decarbonisation of the energy sector on a global scale.

## 2.1. How we plan the future

### Our scenarios

#### Fragmented

In a **less globalised world**, with **scattered policies** and **trade barriers**, **disjointed regulation** is unable to unlock the full technological potential, **preventing an adequate energy transition**



**Not all clean technologies become competitive** – some of them will have to be heavily supported (e.g., H<sub>2</sub> and efuels)

**Gas and CCS** play a big role in transition



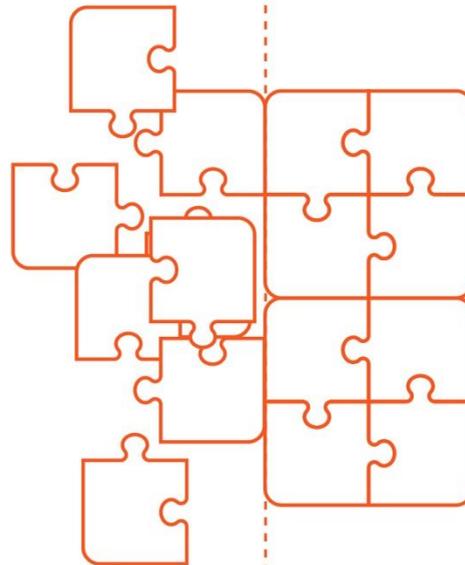
Lower global GDP growth due to deglobalisation, higher taxes and tariffs

**EU** keeps targets to **become carbon neutral by 2050** but loses competitiveness



**Energy transition at different paces** across regions

Lack of trust promotes **carbon trade wars** between **EU, US, China** and other relevant Asian markets



#### Committed

A renewed **alignment** amongst major geopolitical blocks promotes **commercial trade** and develops an **adequate political framework** for decarbonisation, **reducing global emissions to promote a 1.5°C-compliant course**

**Most zero-carbon technologies become cheaper than fossil fuels**



**Renewables, H<sub>2</sub> and synthetic fuels** are the backbone of a new energy ecosystem

**Global GDP accelerated** by new technologies



**EU reaches carbon neutrality by 2050** and promotes a virtuous **decarbonisation** cycle, pushing others to **accelerate transition**

Most light-duty vehicles become electric and autonomous



H<sub>2</sub> and synthetic fuels allow **decarbonisation of hard to abate segments**

## 2.1. How we plan the future

### Fragmented scenario

In a less globalised world, the various geographical blocs implement dispersed policies and trade barriers, resulting in unbalanced regulation incapable of unlocking the full technological potential, and preventing an adequate and effective energy transition in the combat against climate change.

International agreements and institutions lose relevance due to their inability to deal with a fast and volatile world where major economies focus exclusively on themselves. Economic protectionism is increasing, which also leads to increased political tension between the main geopolitical blocs. The uncertain economic and regulatory environment, together with the strong trade barriers, makes financing for large investments increasingly difficult to obtain. This context causes a slowdown in the economic growth, heavily impacted by tax increases and the strong state control over the economy. Not all green technologies become competitive, which means some of them need to be subsidised.

In a reality where there is a lack of coordination between the various blocs, each region adopts its own decarbonisation strategy, prioritising national energy security and its endogenous resources, which hinders the achievement of the climate goals of the Paris Agreement. Even so, some regions like the European Union continue to use carbon neutrality as their flagship by fostering this goal through regulation, using carbon tariffs to maintain their competitiveness against imports and exports.

Urban centres turn into clusters of neighbourhoods, where all the necessary services are within a maximum distance of 15 minutes, with internal combustion engine vehicles gradually being removed from cities, and public transport serving as means of transport in the centres. Companies and schools are responsible for the mobility of their employees/students, promoting proximity policies and remote work.

While mobility patterns change in more densely populated cities, currently with more shared and decarbonised mobility, longer distance transport remains quite similar to what we know today. Technological development has not been enough to change heavy and long-distance transport, which is still based on fossil fuels, although with a significant increase in the inclusion of low-carbon fuels. Industry's transition also did not have the impact initially expected, and most factories continue to rely on an energy matrix similar to the current one.

Different regions have quite different views on carbon capture and utilisation technologies, as well as on emissions allowances and offset credits. On the one hand we see a European Union focused on developing emission control areas and promoting emissions reduction, on the other hand, we see regions promoting decarbonisation exclusively through capture and utilisation technologies and, in more extreme cases, emissions offsetting systems.

## 2.1. How we plan the future

### Committed scenario

A new global agreement amongst the main geopolitical blocs promotes free trade and develops an appropriate economic, political, and regulatory framework for decarbonisation, reducing global emissions at a pace compatible with the 1.5°C goal.

The main geopolitical blocs reach a consensus on their positions on environmental, economic and social issues in major global organisations such as the United Nations, the World Trade Organisation and the World Bank. Global value chains quickly adapt and become more resilient, with digitalisation allowing for increased transparency and cost reduction. Regulatory stability and transparency of operations promote increased long-term investment, accelerating the energy transition while economic development remaining solid, even with a slower population increase, as developing countries are able to improve their living standards. The growth of world GDP is accelerated by the global consensus and the development of new technologies, specifically the so-called green technologies. Clean technologies become cheaper than fossil fuels.

The global agreement to reduce emissions is periodically ratified and reviewed, demonstrating the growing ambition of political leaders worldwide, as well as of large companies and the financial sector, which joined the agreement as a way to accelerate emission reduction through corporate action. The European Union is setting neutral by 2050, a commitment that was initially pioneering, but ultimately influences the rest of the world to implement similar measures to promote energy transition and emission reduction.

Globalisation is thriving and trade between different regions of the globe is intensifying, while the development of new energy and technological solutions means that less energy is needed to carry out this trade. Mobility is changing, in relation to what we know today, popularising mobility as an autonomous, decarbonised and shared service.

The reduction of mobility costs, along with remote work and education, leads many families to move to larger houses in the suburbs, changing the urban landscape as we know it today. Power generation also becomes much more decentralised, often going beyond self-consumption, and promoting micro-generation communities that support the balance of the electrical grid.

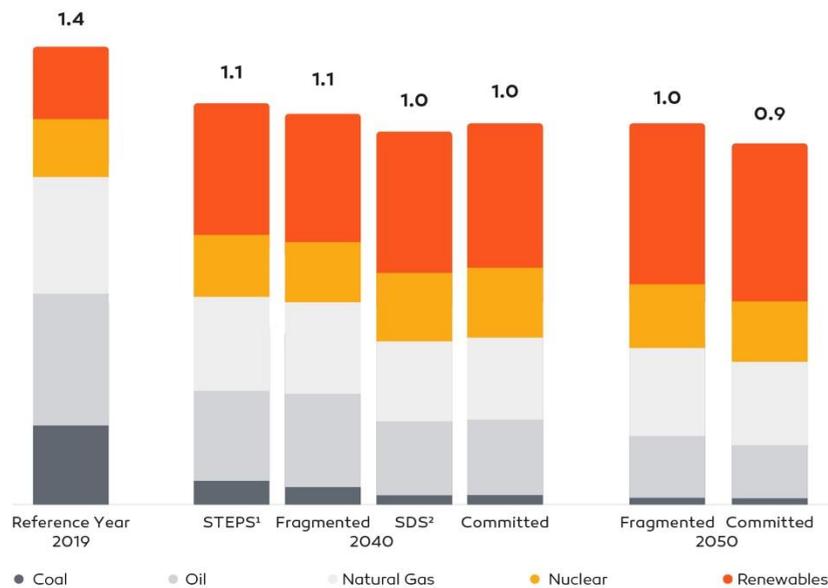
The decarbonisation of the most emission intensive sectors, such as industry and heavy-duty vehicles, is supported by the development of new technologies that enable the continuous increase of their activity, but for the first time without increasing the aggregate emissions.

Markets for trading of emissions allowances and offset credits have a global framework and now exist in several countries. The increased transparency associated with these markets contributes to their growth and to the reduction of global emissions.

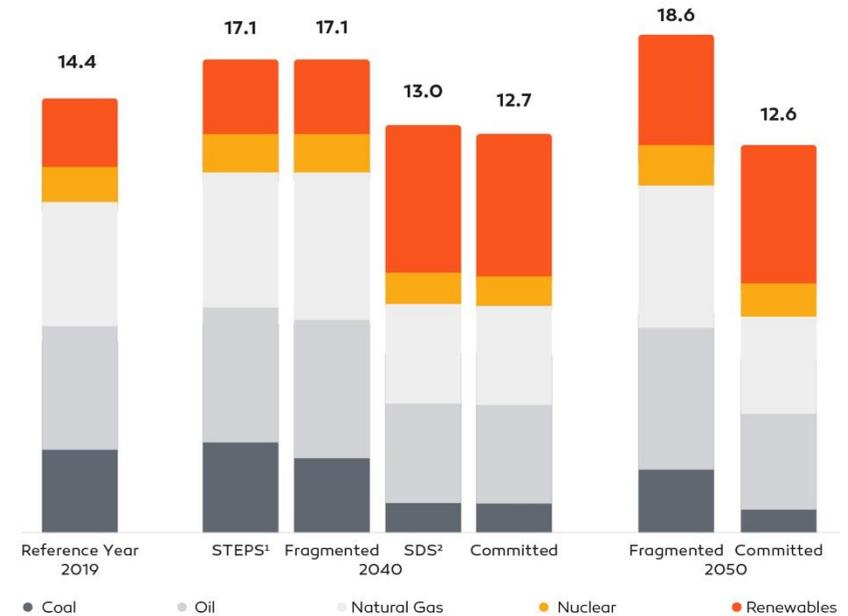
2.2.

# Our strategy

European Union Primary Energy Demand (Gtoe)



Global Primary Energy Demand (Gtoe)



<sup>1</sup> Stated Policies Scenario  
<sup>2</sup> Sustainable Development Scenario

We aim to energise the lives of our customers on a daily basis with the most sustainable solutions. We seek to create a strategy that tackles the current and future context of energy and mobility, ensuring Galp's resilience and agility in an increasingly complex, fast and ever-changing world. As an integrated energy Company we are focused on the development of sustainable businesses that generate value, through a diversified portfolio of energy generation, ranging from oil and natural

gas production to renewable energies, with an industrial background geared towards the new market needs, through the adaptation, efficiency and continuous transformation of its processes, and with more innovative commercial solutions that promote the energy transition of our customers and consumers. The organisation, skills and business that we have developed to date are the basis that allow us to put this strategy into practice. Successful partnerships in key projects and Galp's

## 2.2. Our strategy

international presence and cultural ties in many countries show our ability to develop strong partnerships and a cross-cutting vision of our activity. The energy transition will require transforming the way our customers consume (and produce) that energy, catalysing the adaptation to new commercial value pools. Galp's flexible and close asset base, particularly in Iberia, is the ideal starting point for this transformation, keeping Galp a constant presence in the lives of its customers, both today and in the future.

The way energy is transformed will also be different in the future, requiring an adaptation of existing industrial assets. The progressive decarbonisation and digitalisation will lead to these assets being converted into industrial energy hubs. Galp is preparing to make use of its industrial skills and experience to ensure the technological transformation and fair transition of its refining.

As in any transition, better prepared companies will have an advantage over the competition. We believe that our skills and resources ensure that we have the agility to enter new markets and differentiating businesses effectively, with a clear focus on value generation.

Based on this strategic vision, we have established an integrated view to support the development of the various businesses, according to their stage of maturity, the sustainable generation of value and the growth of the Company.

### Upstream

Galp is focused on the growth of its Upstream business, based on assets oriented to value creation, even in adverse macro conditions. We seek to extract maximum value from our assets by optimising key positions and dynamic portfolio management, creating investment and divestment options that ensure business resilience.

Aligning the Upstream business with the energy transition is part of our business strategy. Galp promotes an active participation in its partnerships, aiming at the development of its main assets, through its constant optimisation and operational excellence, contributing for the reduction of its activity's carbon intensity.

### Refining & midstream

The transformation of industrial assets and other midstream activities is crucial, with the goal of progressively adapting them to the evolving needs of the market, through the reduction of associated emissions and greater optimisation and integration, which ensure maximum value extraction from these assets.

Galp will continue to follow a strategy of adapting its refining system to European Union goals in the field of decarbonisation, circular economy and energy transition. The increased efficiency and flexibility of our assets will be complemented by greater integration with trading activities, with a view to optimising the integrated margin.

These activities also include other products, such as natural gas, where we want to maximise opportunities in the global market, developing new opportunities to increase the value generation of the portfolio.

## 2.2. Our strategy

### Commercial

We want to strengthen our commitment to positioning the client at the centre of all our actions and act as an enabler for people, companies, and cities. The response to changes in consumption patterns is made on a daily basis and is only possible through Galp's support and constant presence in its customers' lives, both through a physical platform, with the convenience and proximity of our network, and through a digital platform, accompanying our customers throughout their daily journey.

The joint management of these platforms puts us in an advantageous position to provide the energy of today, but also that of tomorrow, to explore new mobility trends, together with the communities where we operate, and to provide the convenience necessary for the life and business of our customers. Through an integrated approach and offer, as a one Galp, capable of delivering the products and services for the present and for the future, we support our clients' journey towards the decarbonisation and digitalisation of their consumption.

### Renewables & new businesses

The need for society's decarbonisation has brought challenges to all economic sectors, especially in the energy field, which is responsible for a significant part of global emissions. Nowadays, it is clear that the way we generate, transform and consume energy will change, and with it, something that will be shaped and followed by the strategy of companies in different geographies. Galp intends to play an active role in the energy transition that society is facing, seeking to anticipate trends, develop a portfolio in line with future needs, establishing synergies with

its current business whenever possible, and progressively reduce the carbon intensity of its activity and its customers.

Contributing to the decarbonisation of the economy, Galp will continue to invest in its renewable energy generation, based on proven technologies and differentiating projects, aspiring to increase its renewable generation installed capacity. Galp's current portfolio is based on c.3.8 GW of renewable capacity to be installed up to 2024, focused on Iberia, an advantageous market for Galp due to synergies with the electricity commercial activity. We will expand our portfolio based on investment opportunities and exploring our competitive advantages.

In a complementary way, Galp promotes the energy transition to its clients through the investment in decentralised renewable energy solutions.

As a Company that aspires to play an active role in the energy transition, we intend to continue the development of a differentiated portfolio of renewable energy generation and new at scale businesses, associated with the market trends, with an innovative approach.

The Group's capital allocation will thus be in line with the strategic pillars described above, and will be supported by the implementation of an active portfolio management aimed at covering investment needs, ensuring the existence of a solid capital structure and maximising the value of Galp's portfolio businesses. This allows for a competitive and balanced shareholder distribution in line with the Company profile.

2.3.

## How we manage risk

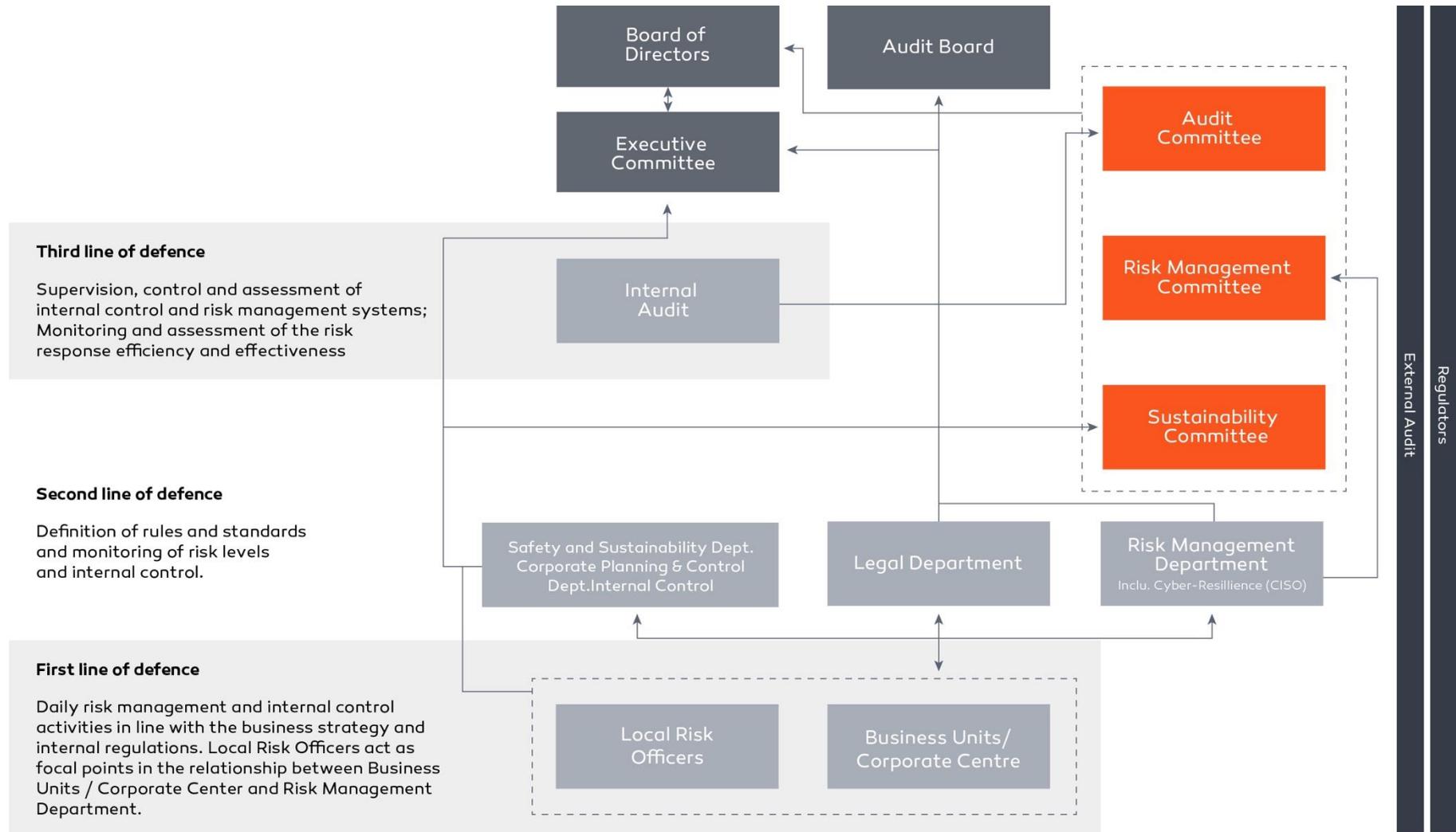
As an integrated energy Company, Galp is exposed to risks that may have a negative impact on its operational and financial performance, reputation and market capitalization.

The management of these risks is based on a Risk Management Model, implemented through an integrated, continuous and dynamic process that involves the business units and Galp's corporate areas, and which is

supported by the Risk Management Policy, the Risk Management Governance Model and the Internal Control Manual, approved by the Board of Directors.

The governance structure and organisation of risk management at Galp follows the COSO (Committee of Sponsoring Organizations of the Treadway Commission) methodology and are structured according to the organisational model of the three lines of defence, in cooperation with the supervisory bodies, as represented in the image below:

## 2.3. How we manage risk



## 2.3. How we manage risk

The risks are grouped into categories according to their nature. Galp's main risk categories are presented in greater detail in Part II of this report - Corporate Governance Report, and are summarised in the table below.

Risk Categories	
Price	Galp's assets and results are dependent on several market factors, including the price of oil products, natural gas, Liquefied Natural Gas (LNG), electricity, as well as exchange and interest rates.
IT & Cybersecurity	A breach of Galp's digital security or failure of its digital infrastructure could hinder its operations, increase costs and affect its reputation. It is critical to ensure Galp's cyber and digital integrity and readiness.
Portfolio	The execution of Galp's strategy and its sustainability may be affected if the Company is unable to develop, maintain or efficiently manage a high-value asset portfolio.
Innovation	Failure to properly anticipate market changes and customer expectations can compromise Galp's long-term competitiveness and financial sustainability.
Market	In an environment highly conditioned by the dynamics of demand and supply, Galp's ability to adapt to new paradigms and react to competition is crucial to ensure good financial performance and achieve the strategic goals.
Project Execution	Galp's organic growth and results depend on the execution of its main investment projects.
Geopolitics	Exposure to political developments and consequent changes in the operating environment can undermine the operations and adversely affect the value of Galp's assets and results.
Business Continuity	Failure to effectively respond to crisis situations or disruptions may jeopardize the continuity of operations and damage Galp's reputation and shareholder value.
Credit	Exposure to credit risk may significant and adversely affect Galp's operational results and financial condition.
Legal	Legal and regulatory changes may alter the business context in which Galp operates, impacting its profitability.

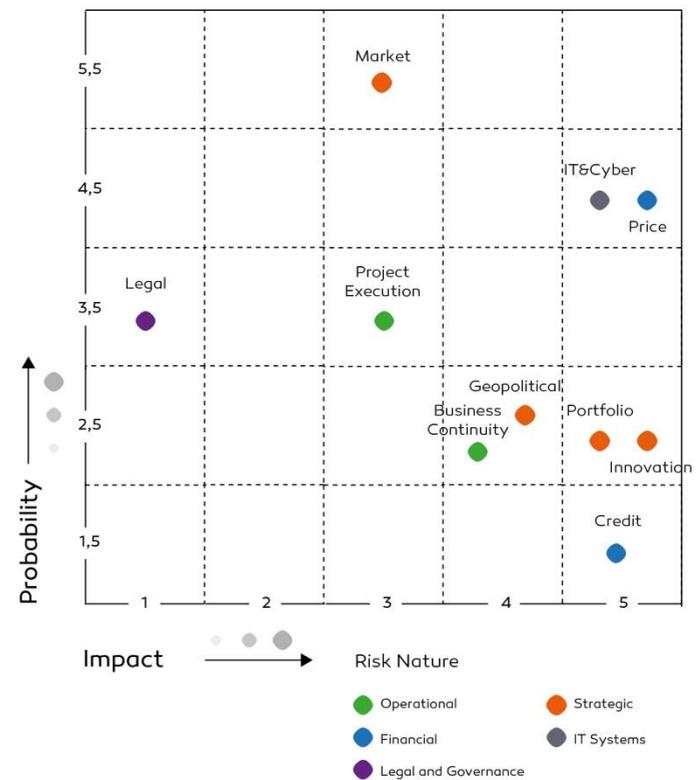
## 2.3. How we manage risk

Some of these risks are sensitive to climate change challenges and the transition scenarios for a low carbon economy, particularly those associated with regulation ("Legal"), future demand trends and potential increased competition ("Market"), fluctuations in hydrocarbon and other commodity prices ("Price"), and changes in the business model ("Portfolio").

Given the emerging nature of the risks and opportunities associated with the transition to a low carbon economy, and whereas its commitments, Galp has broadened the scope of its risk analysis, incorporating and regularly monitoring them.

The Risk Management Department performs a recurrent assessment of Galp's main risks and opportunities and monitors its risk profile. The severity of risks is assessed according to their probability of occurrence and level of impact, and risks are organised into "probability x impact" matrices.

Top 10 Risk Classes



## Cautionary Statement

This document may include forward-looking statements, including, without limitation, regarding future results, namely cash flows, dividends, and shareholder returns; liquidity; capital and operating expenditures; performance levels, operational or environmental goals, targets or commitments and project plans, timing, and outcomes; production rates; developments of Galp's markets; and impacts of the COVID-19 pandemic on Galp's businesses and results; any of which may significantly differ depending on a number of factors, including supply and demand for oil, gas, petroleum products, power and other market factors affecting them; the outcome of government policies and actions, including actions taken to address COVID-19 and to maintain the functioning of national and international economies and markets; the impacts of the COVID-19 pandemic on people and economies; the impact of Galp's actions to protect the health and safety of its employees, customers, suppliers and communities; actions of Galp's competitors and commercial counterparties; the ability to access short- and long-term debt markets on a timely and affordable basis; the actions of consumers; other legal and political factors, including changes in law and regulations and obtaining necessary permits; unexpected operating events or technical difficulties; the outcome of commercial negotiations, including negotiations with governments and private entities; and other factors discussed in Galp's Management Report & Accounts filed with the Portuguese Securities Market Commission (CMVM) for the year ended December 31, 2019 and available on our website at galp.com. This document may also contain statements regarding the perspectives, objectives, and goals of Galp, including with respect to energy transition, carbon intensity reduction or carbon neutrality. An ambition expresses an outcome desired or intended by Galp, it being specified that the means to be deployed may not depend solely on Galp. All statements other than statements of historical facts are, or may be deemed to be, forward-looking statements. Forward-looking statements express future expectations that are based on management's expectations and assumptions as of the date they are disclosed and involve known and unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in such those statements. Forward-looking statements include, among other things, statements concerning the potential exposure of Galp to market risks and statements expressing management's expectations, beliefs, estimates, forecasts, projections, and assumptions. These forward-looking statements may generally be identified by the use of the future or conditional tense or the use of

terms and phrases such as "aim", "ambition", "anticipate", "believe", "consider", "could", "envision", "estimate", "expect", "goals", "intend", "may", "objectives", "outlook", "plan", "probably", "project", "risks", "schedule", "seek", "should", "target", "think", "will" or the negative of these terms and similar terminology.

Financial information by business segment is reported in accordance with the Galp's management reporting policies and shows internal segment information that is used to manage and measure the Group's performance. In addition to IFRS measures, certain alternative performance measures are presented, such as performance measures adjusted for special items (adjusted earnings before interest, taxes, depreciation and amortisation, adjusted earnings before interest and taxes, and adjusted net income), return on equity (ROE), return on average capital employed (ROACE), gearing ratio, cash flow from operations and free cash flow. These indicators are meant to facilitate the analysis of the financial performance of Galp and comparison of results and cash flow among periods. In addition, the results are also measured in accordance with the replacement cost method, adjusted for special items. This method is used to assess the performance of each business segment and facilitate the comparability of the segments' performance with those of its competitors. This document also contains non-financial performance indicators, including a carbon intensity indicator for energy products sold by Galp, that measures the amount of greenhouse gas emissions of those products, from their production to their end use, per unit of energy delivered. This indicator covers the direct GHG emissions of production and processing facilities (scope 1) and their indirect emissions associated with energy purchased (scope 2), as well as the emissions associated with the use of products by Galp's costumers (scope 3). The same emissions are considered for products purchased from third parties and sold or transformed by Galp. For a complete definition of scopes 1, 2 and 3 and the methodology used by Galp for this indicator please refer to Galp's website at galp.com.

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