

**MASTER OF SCIENCE IN
FINANCE**

**MASTERS FINAL WORK
PROJECT**

**EQUITY RESEARCH GALP ENERGIA SGPS SA:
USING THE EXPECTED CASH FLOW APPROACH**

ARTHUR PINHEIRO QUITES

NOVEMBER 2020

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ARTHUR PINHEIRO QUITES

**SUPERVISOR:
VICTOR MAURÍLIO SILVA BARROS**

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Abstract

The present document consists of an award-winning report of an Equity Research on GALP S.G.P.S., SA. This document was used in the CFA Institute Research Challenge 2020, obtaining a 1st place at the Local level and a 2nd place at Regional level. The report follows the CFA Institute format and only public information until 18/10/2020 was considered.

In addition to the standard format chosen, this report has one additional chapter, that all together form the Master Final Work. The said chapter explores further on how to define the price target, by using the **expected cash flow approach**. Between using sensitivity analysis and different price scenarios together with a mathematical methodology to define probabilities, another piece of information is provided to help investors make an investment decision.

GALP is the leading Portuguese integrated oil company. It operates throughout the whole fossil fuel value chain, from extracting fossil fuel, to transporting and refining it and finally commercializing the different by-products. GALP is a relevant player in the upstream and market leader in the downstream, in the markets the company operates.

The company was valued with a Sum-of-the-Parts approach, where a FCFF DCF was made to each business unit, reflecting all the idiosyncrasies of each BU. The result was them summed up, the adjustments were made to the resulting sum, yielding a final price target of 12.1€/sh. To support this valuation, other methods were also used, such as a FCFF DCF (for the company as a whole), FCFE DCF, the APV and the DDM. The valuation was subject to stress tests and sensitivity analysis in order to address risk. In addition, the risks the company is subject to is thoroughly explained in the report.

It is also important to mention that the report was finalized on January 15th, 2020. However, an updated research snapshot was made, to include new information, reflecting the impacts of the COVID-19 pandemic. This update reflects information from March 2020.

JEL classification: G10, G32, G34

Keywords: Equity Research, Valuation, DCF, APV, DDM, FCFF, FCFE, WACC, Excel Modelling, Oil, Gas, Fossil Fuel, Renewables, Mergers & Acquisitions.

Resumo

O presente documento consiste num relatório premiado de um Equity Research sobre a GALP S.G.P.S., SA. Este documento foi utilizado no *CFA Institute Research Challenge 2020*, obtendo um 1º lugar a nível Local e um 2º lugar a nível Regional. O relatório segue o formato do *CFA Institute* e apenas foram consideradas informações públicas até 18/10/2020.

Além do formato padrão escolhido, este relatório possui um capítulo adicional, que juntos consistem num Trabalho Final de Mestrado. O capítulo em causa explora em maior detalhe como definir o preço-alvo, usando a abordagem do ***expected cash flow***. Entre a utilização de análises de sensibilidade e diferentes cenários de preços, em conjunto com uma metodologia matemática para definir probabilidades, este capítulo fornece mais um conjunto de informações para auxiliar os investidores na decisão de investimento.

A GALP é a principal empresa petrolífera integrada portuguesa. Atua em toda a cadeia de valor dos combustíveis fósseis, desde a extração de combustível fóssil, ao seu transporte e refinamento e, finalmente, a comercialização dos diversos subprodutos. A GALP é um *player* relevante no *upstream* e líder de mercado no *downstream*, nos mercados onde a empresa está presente.

A empresa foi avaliada com uma de soma de partes, onde um *FCFF DCF* foi feito para cada unidade de negócios, refletindo todas as idiosincrasias de cada unidade. O resultado é somado, e os ajustamentos foram feitos à soma, resultando num preço-alvo final de 12,1€ por ação. Para apoiar esta avaliação, outros métodos também foram utilizados, como o *FCFF DCF* (para a empresa como um todo), o *FCFE DCF*, o *APV* e o *DDM*. A avaliação foi sujeita a testes de *stress* e a análises de sensibilidade, de modo a abordar o risco. Além disso, os riscos aos quais a empresa está exposta são detalhadamente explicados no relatório.

Também é importante mencionar que o relatório foi finalizado em 15 de janeiro de 2020. No entanto, foi criado um *research snapshot* atualizado para incluir novas informações, refletindo os impactos da pandemia COVID-19. Esta atualização reflete informações de março de 2020.

Classificação JEL: G10, G32, G34

Palavras-Chave: Equity Research; Avaliação de Empresas; Fusões e Aquisições, Renováveis.

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I wish to express my most sincere thank you to Prof. Victor Barros, CFA, for all the support, guidance, availability, help, coffee, chocolate, nights, conversations, everything. And mostly for never giving up on us and believing in us every single day. Without you, this amazing run would have never been possible. Thank you so much, Victor.

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To my friends since ever, thank you. At least it feels like since ever.

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Finally, to my mother. My inspiration. You taught me to always fight for my dreams. You taught me that with hard work, anything can be achieved. You taught me that sacrifices are needed to achieve my goals. You prepared me to face anything. You made this possible. So, this achievement is for you. It is for us. Thank you so much, for everything.

Disclosures

A significant portion of this report was submitted by a group of students from ISEG, including the candidate, for the 2020 CFA Institute Research Challenge Portuguese Local Final. Upon winning the local final, the same report advanced as the representative report for CFA Society Portugal in the 2020 EMEA Regional Final, which this year happened online due to the pandemic.

This report is published for educational purposes by Master students at ISEG and is not an investment recommendation. This report must be read with the Disclosures and Disclaimer at the end of this report. Appendices that support this report may be obtained from the author upon request.

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Date: January 2nd, 2020
 Ticker: GALP.LS (Reuters)

Current Price: EUR 14.98
 EUR 1.000: USD 1.121

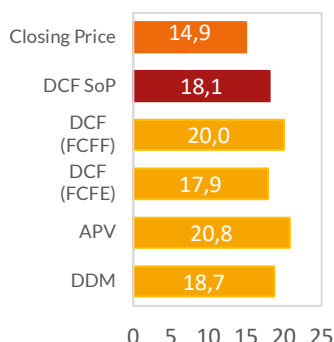
Recommendation: **BUY** (21% Upside) High-Risk
 Price Target: **EUR 18.1** (USD 20.3) 2020YE

Table 1: GALP's Market Data

Market Profile	
Closing Price (January 2nd, 2020)	14.98
52w Price Range	12.4 - 15.4
52w Daily Volume	1.5M
Shares Outstanding	829.3M
Market Capitalization (January 2nd, 2020)	12.4B
Free Float	59.2%
Dividend Yield ^{2020YE}	4.4%
ROE ^{2020YE}	16.6%
D/E ^{2020YE} (Mkt Value)	0.7
P/BV ^{2020YE}	2.5
P/E ^{2020YE}	39.8

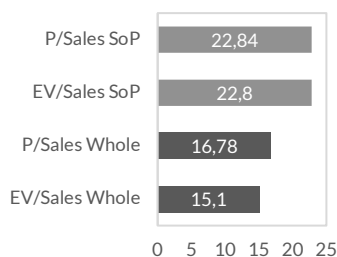
Source: Thomson Reuters, Team Estimates

Figure 1: GALP's Price Target (€)



Source: Team estimates

Figure 2: GALP's Price Target with Multiples

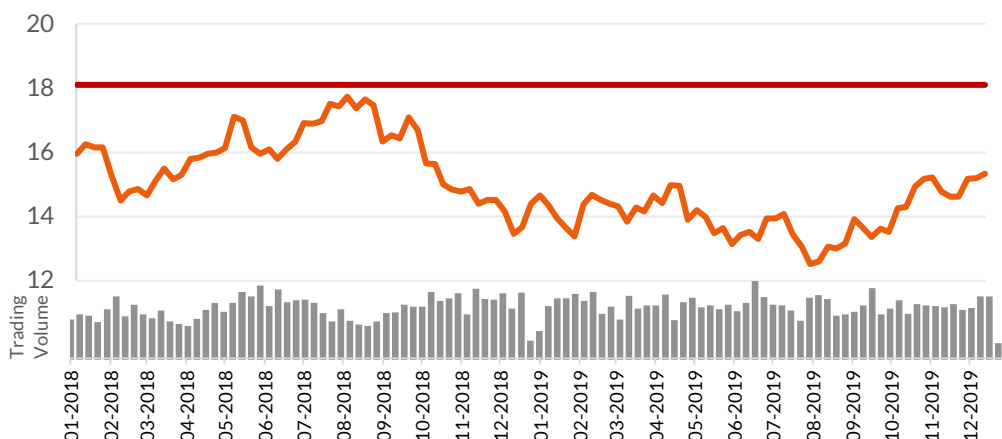


Source: Team estimates

Table 2: Industry's Abbreviations

Abbreviations	
bbl	Barrel of Oil
kb/d	Thousand bbl per Day
mb/d	Million bbl per Day
boe	Barrel of Oil Equivalent
mboe	Million boe
kboe/d	Thousand boe per Day
mton	Million Tonnes
mta	Million Tonnes per Annum
IOC	Integrated Oil Company
NOC	National Oil Company
WIP	Working Interest Production
FPSO	Floating Production Storage and Offloading

GALP: Strong, Strategic and Sustainable Using the Expected Cash Flow Approach



BUY is our recommendation for Galp Energia S.G.P.S., S.A. (GALP) with a price target of €18.1/sh for 2020YE using a DCF model, implying a 21% upside potential from the January 2nd, 2020 closing price of €14.98/sh, but we assess it as high-risk. GALP is an Integrated Oil Company (IOC) operating mainly in 6 countries across all Oil & Gas segments. We see a leading company in Portugal, with a solid market share of above 40% in the downstream; competing fiercely in the Iberian market, with 20% of the refining capacity; and partnering up globally for oil and gas exploration – being present in several and profitable projects. With a stable 2020F cash flow yield around 7%, the company will keep growing robust driven by its increasing production, supported by the oil and gas demand outlook. We see GALP as a buy stock because it is Strong, Strategic and Sustainable.

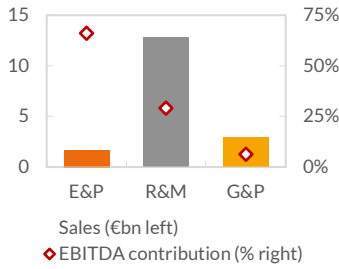
Strong, due to its cash flow generation from all segments, but mostly from the Upstream business. Sales from this segment grew strong +22.5% CAGR from 2015 to 2019E and are expected to grow further +7.0% until 2025, fueled by its E&P projects. Also, the company has a low portfolio breakeven of \$25/bbl, below its main competitors. Projects in the Brazilian pre-salt region drive the value. In the downstream, GALP is the benchmark in Portugal and a relevant player in Spain. By being an IOC, there is a natural hedging effect that partially protects the firm's strong cash flow generation.

Strategic, as GALP shows how they operate businesses by having stakes in some of the most profitable exploration projects in the world. The Lula field in the Brazilian pre-salt is an example, with very low production costs for GALP and impressive current production of 125 kb/d. The company is the 3rd biggest producer in the region, with room to improve. Also, there is the Rovuma block in Mozambique. It is one of the largest gas reserves ever discovered and a key development for GALP's lower carbon strategy. It has a 10% stake and should start producing in 2025. Our conservative view accounts for €1.05/sh of our price target. The company is highly dependent on oil, being the primary cash flow driver. Yet, the doubling of the CAPEX allocation for the G&P segment is a step towards a more sustainable portfolio.

Sustainable, as the company is very focused on ESG and has won several international awards. GALP is in the pole position in the Dow Jones Sustainability Index between its peers, ranking 1st in the DJSI Europe for Oil & Gas (3rd place at global level). Furthermore, the company is also financially sustainable. Operationally, GALP has a strong financial discipline, setting a max of 2.0x for Net Debt/EBITDA, currently at 0.9x 2019E, giving room to embrace new projects. We expect expansion CAPEX to keep the steady growth, yet sustainable for shareholders with an attractive dividend policy. Investing in GALP today should secure a dividend yield of 7-8% by 2025F.

Expected cash flow approach. Our base case price target is 100% from our DFC model. However, there are other ways to define the price target. There is no "best option" on how to do that, since each analyst can have different opinions. In the additional chapter to this award-winning report, I explore a mathematical approach to define a different price target. By using sensitivity analysis, three scenarios are created, and with a Monte Carlo simulation I define the probability of each scenario. By doing a weighted sum of the cases, I reached an expected price target of 12.74€/sh, further supporting our valuation.

Figure 3: Sales & EBITDA 2018



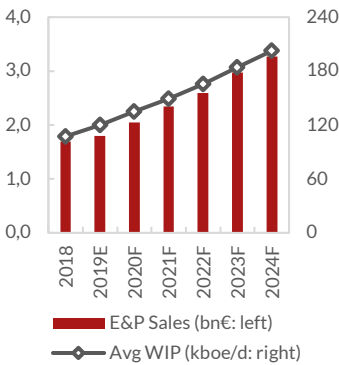
Source: GALP

Figure 4: GALP's Main Upstream Locations



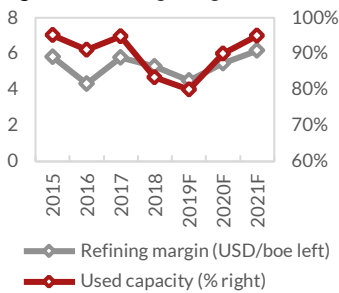
Source: GALP, Team Analysis

Figure 5: E&P Sales vs WIP



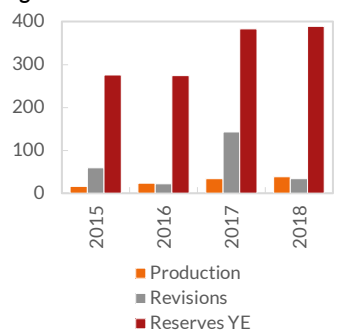
Source: Galp & Team Estimates

Figure 6: Refining Margin and % Used



Source: GALP

Figure 7: Revisions and Production



Source: GALP (kboe)

Business description

Galp Energia S.G.P.S., S.A. (GALP) is a leading Portuguese IOC. The company operates within the oil and gas value chain, both in Upstream, by searching, recovering and producing crude oil and natural gas (NG), and in Downstream, with refining and commercialization. The Upstream (Exploration & Production or E&P) is GALP's value driver with €1.7 bn 2018 sales, representing 11% of total sales, and EBITDA of €1.4bn, contributing 70% to company's 2018 EBITDA. The Downstream has two segments: the Refining & Marketing (or R&M) segment, with €12.8bn sales, accounting for 73% 2018 sales; and the Gas & Power (or G&P) segment, that recorded sales of €2.9bn, only contributing 5% to the company's EBITDA. GALP's 2018YE revenue of €17.2bn places the company among the top 15 largest oil and gas players in Europe.

History of the company

GALP's history goes back to 1976 when the merger of the four largest Portuguese players in the oil sector originated Petrogal, the leader in the R&M sector. Its position as the leading player in Portugal was consolidated in 1999, by the aggregation of Petrogal and GdP (Gás de Portugal), establishing Galp Energia. In 1982, the company entered the E&P segment with the acquisition of a stake in block 1/82 in Angola. GALP started its strong development in the E&P business in 2007, with the largest ultra-deepwater oil discovery of the last 30 years in block BM-S-11 Lula/Iracema in Brazil. From there onward, the company has been highly focused on growing this segment. The E&P's sales growth skyrocketed at +23.1% CAGR, from €140 million to €1.69 billion 2006-2018, making the segment the main contributor of GALP's EBITDA. In recent years, the company entered a B2C business in the electricity sector.

Operational segments

E&P | GALP's E&P sales are fueled by the average daily production (WIP of 107 kboe/d 2018YE). In 2018, with a \$15/boe increase in GALP's oil and gas average selling price and the preservation of production costs, the segment registered a positive YoY change in its EBITDA of 70% to €1.44 bn.

Currently, E&P sales come mostly from projects in Brazil, with GALP's operations in Angola showing a temporary slowdown, with blocks 14/14k in production decline and block 32 in ramp-up. The segment's value driver is the Lula-Iracema project, with a production of 98 kboe/d 2018YE (91% of total WIP). This project alone accounts for 8% (€1.42bn) of GALP's total sales. The next big project is expected to be Mozambique's Rovuma Liquefied Natural Gas (LNG). This new project signals GALP's aim in reducing the dependency of its operations in oil production, and, consequently, increasing the stability of the energy mix. It will be mainly through Rovuma LNG that GALP will achieve its 25-30% target for NG contribution in the company's WIP 2030F.

R&M | GALP's R&M sales increased in 2018 (1.6% YoY), mainly explained by higher Iberian energy demand. Nonetheless, maintenance operations in the refineries, accompanied by higher oil prices, led to a decrease in the company's refining margin by \$0.8/boe YoY to \$5.0/boe. Subsequently, the margins were profoundly affected, which resulted in a 17% YoY decrease in the R&M EBITDA to €0.6bn.

GALP is responsible for 20% of the Iberian Peninsula refining capacity, presenting a combined installed capacity of 330 kb/d. GALP is the leading player in the retail network in Portugal (c.40% market share), and a significant one in the Iberian market (9% market share). In Portugal, GALP possesses the total refining capacity through its refineries in Sines and Matosinhos. GALP's marketing segment is responsible for the commercialization of refined products. It sold 16.8 mton of oil products in 2018YE (-7.6% YoY), explained by the decrease in refineries' used capacity from 95% to 83%. Direct sales account for 51% of marketing sales in 2018YE, 61% of which correspond to wholesale operations (+2% YoY). Exports are the runner-up with a c.29% of marketing sales in 2018YE.

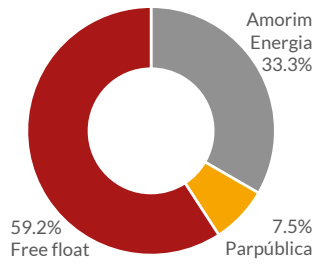
G&P | GALP's G&P sales increased 11% YoY 2018YE to € 2.9bn, mainly explained by the +8% YoY in NG sales to direct clients and the +7% YoY change in electricity sold to clients. The amount of electricity sold to the grid decreased by 14%, but the effect on sales was greatly offset by the previously mentioned increases in sales. There was a small impact on its EBITDA, increasing only 4% YoY.

Most of the sourcing of NG comes from long-term contracts in Algeria (Sonatrach) and Nigeria (Nigeria LNG). However, GALP expects to sign a contract in 2022 with a US company, to diversify its portfolio through an increase in trading activity. GALP leads the supply to industrial and large consumers in 3Portugal with 61% of total NG sales. Regarding Power, a significant part of the electricity sold to the grid comes from cogeneration units in the refineries. Nonetheless, aligned with its low carbon strategy, the company is actively working on the development of solar and wind power generation projects.

Key drivers of profitability

Oil and gas prices | GALP is highly exposed to commodity prices, as a variation of \$5/bbl reflects a ΔEBITDA of around €200m. The upstream segment is more sensitive than the downstream. However, with a portfolio breakeven of \$25/bbl due to investments in the most profitable projects in the pre-salt region, the company has a reasonable margin against oil prices decrease. This low value is mostly achieved by the high profitability of Lula-Iracema projects, driven mainly by low production costs. 2018YE oil prices of \$62.6/bbl (+31.5% YoY) and expectations for 2025F at \$65-70/bbl show good promise for GALP'S future.

Figure 8: Shareholder Structure



Source: GALP

Table 3: Executive Committee

Executive Committee	
Carlos Gomes da Silva	Vice-Chairman, CEO
Filipe Crisóstomo Silva	CFO
Thore E. Kristiansen	COO (Upstream)
Carlos Costa Pina	COO (Infrastructure)
José Carlos Silva	COO (Midstream)
Sofia Tenreiro	COO (Comercial)
Susana Quintana Plaza	COO (Renewables and New Business)

Source: GALP

Table 4: Non-Executive Directors

List of Non-Executive Directors		
Paula Amorim	Amorim Group	Chairwoman, NED
Miguel A. Marques	LID	Vice-chairman, NED
Marta Amorim	Amorim Group	NED
Francisco T. Rêgo	Amorim Group	NED
Carlos Pinto	Sonangol E.P.	NED
Luís Todo Bom	Independent	NED
Jorge S. de Freitas	Amorim Group	NED
Diogo M. Tavares	Amorim Group	NED
Rui P. Gonçalves	Amorim Group	NED
Edmar de Almeida	Independent	NED
Cristina N. Fonseca	Independent	NED
Adolfo M. Nunes	Independent	NED

Source: GALP

Notes: LID – Lead Independent Director

Figure 9: Governance Structure



Source: GALP

WIP and reserve levels | GALP's upstream sales are also dependent on reserves and the ability to turn them into WIP. The company must simultaneously maintain a reasonable level of reserves that will assure the sustainability of the E&P segment. GALP's reserves have been increasing mostly via revisions of project's estimates. WIP has been in an upward trend, with a +24% CAGR 2014-2018. The average WIP should reach 223 kboe/d by 2025F, higher by 115 kboe/d (+ 11% CAGR) 2018YE.

Company Strategies

Upstream and Downstream: different focus | GALP's strategy in the upstream is to develop its current portfolio. The company targets highly profitable and low-risk projects levered by competitive advantages in its current geographies.

In the downstream, the focus is to increase the efficiency of the refining system and to optimize the distribution of oil products in Iberia and Africa. GALP also aims to take advantage of existing opportunities in the global energy markets and grow as a gas supplier.

Energy Transition | GALP has already started the shift towards sustainable energy sources by focusing on NG and power generation through electricity (G&P segment). Also, measures are being taken to reduce the carbon intensity of its assets despite the focus of strategies on oil and NG. GALP aims to allocate 5-15% of its CAPEX to increase its market share in the G&P segment, develop new solutions and explore business projects supported by low-carbon energy (currently focusing on solar).

Financial Discipline | GALP's Net Debt/EBITDA 2018YE is 0.8x, with a maximum for this ratio set at 2x. This financial discipline allows the company to keep its focus on current objectives and decide upon new projects, not jeopardizing the future. Nowadays, GALP has room to undertake new projects as they come and to sustain the attractive dividends, even in a lower-profits scenario.

Dividend policy | The company has a strong commitment to its dividend policy aiming to increase the DPS around 10% per year, with its distribution depending on the capital structure, the cash flow generation and value-adding investments. GALP's DPS in 2018 was €0.6325 (15% increase YoY), to be paid semiannually. The total cash paid reached €525m, representing a payout ratio of 74% and an attractive 5% dividend yield.

Shareholder structure

GALP has 92.5% shares quoted in the market and the remaining 7.5% indirectly held by the Portuguese state through Parpública. Its largest shareholder is Amorim Energia B.V. with 33% of shares. The remaining shares account for 59%, mostly held by institutional investors from around the world. Individual investors account for 2% of GALP's share capital. Currently, GALP does not hold treasury shares. However, until October 2020, the BoD may proceed to an acquisition of up to 10% of GALP's capital, following a General Meeting decision from 2019Q2. Major shareholders may be allowed to divest through this mechanism.

Governance

Ms. Paula Amorim is GALP's chairwoman since 2016, after succeeding her father in the role. Before, she was the vice-chair and has been in the company's Board since 2012. She is also part of the family that owns Amorim Energia B.V. Since 2015, GALP's CEO is Mr. Carlos Gomes da Silva, a 52-year-old engineer with an MBA from ESADE, with over 30 years of experience, mostly in the energy sector. Throughout the years he took different roles in several divisions of GALP and most recently acted as COO in two distinct business units before being appointed CEO. The remaining 6 executive members have a similar academic background and relevant tenure in the company (Appendix 24).

Board Structure and Remuneration Policy

The Board of Directors (BoD) is composed of 19 members, including 12 Non-Executive Directors (NED), 5 of whom are independent (Table 4). In compliance with the By-laws, the Remuneration Committee is controlled by 3 shareholders not belonging to the Board. The remuneration policy is mixed. A fixed amount is paid to NED, while executive members get a fixed component plus a variable, based on the annual and three-year performance levels (Appendix 24). The former accounts for half, being 65% based on yearly value-added, total shareholder return and EBITDA, while the remaining 35% are of qualitative nature. Additionally, there is a retirement savings plan, equaling 25% of the fixed part.

The board turnover in 2019 was positive for gender equality. Women on Board increased from 2 to 5, with 2 of them being appointed to the executive committee, which was previously wholly composed by men. GALP's diversity policy is set from top to bottom.

Governance Model and Shareholders

GALP's governance model separates powers between different corporate bodies to ensure the transparency and effectiveness of governance. The Anglo-Saxon model is followed, and members are elected for a 4-year term. The Corporate Governance Code (CGC) of the Portuguese Institute of Corporate Governance (IPCG) is the benchmark in the country, to which GALP adopts 49 of the 60 recommendations. This represents 82%, which is close to 84% of average adoption from companies in the PSI20.

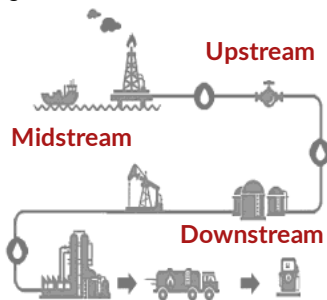
The By-laws of the company foresees a one-share-one-vote principle, without limiting voting rights. With an average 77% of the capital attending the Shareholder Meeting, Amorim Energia B.V. may exert relevant controlling voting power. Furthermore, most shareholders' resolutions only require a simple

Table 5: Key ESG Metrics

Governance Metrics	
Metric	GALP
Shareholder Meeting Attendance (3-year average)	77%
Independent Directors	26%
CGC Compliance	82%
Average Tenure (years)	5.8
DSJI Europe	1st
DSJI World	3rd
ESG Score	67th
Environmental Pillar Score	A+
Social Pillar Score	A-
Governance Pillar Score	C

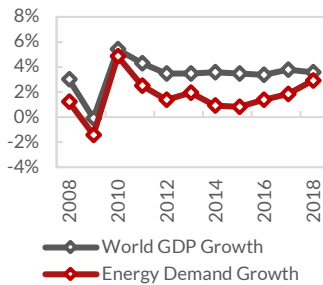
Source: GALP, Thomson Reuters

Figure 10: Oil Value Chain



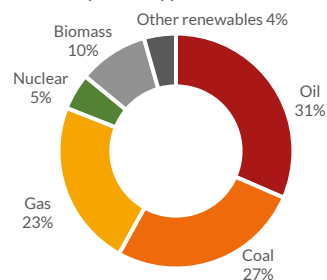
Source: Allied Consultants

Figure 11: Global GDP & Energy Demand Growth



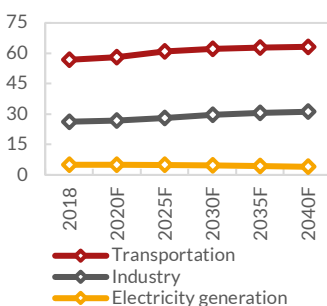
Source: IMF, BP & Team Estimates

Figure 12: 2018 World Energy Demand by Fuel Type



Source: OPEC

Figure 13: Sectors in Oil Consumption



Source: OPEC (mb/d)

majority (exception relates to the company's Management; amendments to By-laws; and company transformation/mergers). Additionally, the chairwoman and 5 NED have links to Amorim's business, increasing, even more, the influence of this company over GALP. The second-largest shareholder is the state-owned holding Parpública, and it is not directly represented in the BoD, despite the 7.5% stake.

The evident influence that Amorim Energia B.V. has over the BoD may increase the apparent absence of protection that minority shareholders have over the group's decisions. The Amorim family has shown a commitment for a stable and robust dividend policy in companies other than GALP (e.g., Corticeira Amorim SGPS SA), thus mitigating potential value extraction effects, not expected to put growth opportunities at risk. Still, we believe that the current governance structure of GALP does not jeopardize our buy recommendation.

(Going) Sustainable and (being) Socially Responsible

In the Dow Jones Sustainability Indices (DJSI), GALP ranks 1st in the DJSI Europe for Oil & Gas (3rd place at a global level). Awards for sustainability are recurring and GALP's Thomson Reuters ESG score of 44.8 (Table 5), in line with Oil & Gas companies (median of 41.7). The score is timid, yet the company is the only one that received an A and A- classification from CDP in the categories of water security and climate change, respectively.

Social responsibility is also in the company's DNA. In 2009, the Galp Foundation was born. Governed by the Chairwoman, CEO and CFO, with a total budget of €19.4m in 2018, the Foundation targets project in areas such as Social Development, Energy and Environment and Education and Culture, operating in Portugal, Guinea-Bissau and Mozambique. Currently, the leading project is "Energiza" which aims to install a photovoltaic system to provide access to energy in Mozambique. The location of this project signals a clear concern with the communities where the company operates. GALP is at the forefront regarding sustainability and social responsibility, yet new challenges such as the energy transition will put the company to the test.

Industry Overview and Competitive Positioning

The Oil & Gas industry operates around the value chain of fossil fuels. It starts in the Upstream sector (E&P), covering all activities of searching, recovering, and producing crude oil and NG. Entering this segment requires participating in each producer country's bidding rounds, which is extremely capital intensive (Appendix 21). On the opposite side of the chain, the Downstream sector (R&M and G&P) includes refining the crude oil, processing the raw NG, and covering marketing and distribution of their by-products, along with the production and commercialization of electricity. Both segments are supported by the Midstream, acting as the bridge between them, yet GALP is not intensively operating in this middle part. The Oil & Gas industry is the world's most profitable industry, according to Forbes. Aggregated profits increased YoY by 36% in 2018. Currently, global E&P alone represents 3% of the worldwide economy.

World population, GDP Growth and Energy Demand | The Oil & Gas industry will keep robust, as current levels of energy sources will be insufficient to meet increases in global energy demand. Increasing world population and expected economic growth are to blame. World population will increase by 21% until 2040, with this growth coming mostly from developing countries. Yet, growth rates will be decelerating. The global GDP growth is slowing down and is expected to be at 3.2% in 2019. With the stabilization of trade problems in the most developed countries by 2024, expected by OECD, the world's GDP growth should increase to 3.4% going forward. As in Figure 10, GDP growth and energy demand are tied together. Supply has a role to play.

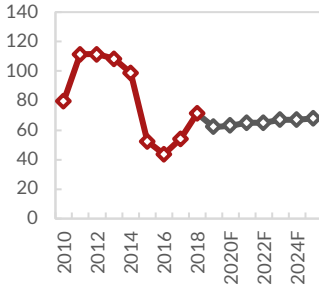
International Outlook: GALP's Upstream Outlook

There is a common misconception about the looming energy transition – the focus will shift entirely to low carbon alternatives and renewable energy. However, fossil fuels are responsible for more than 50% of the world primary energy demand. Despite the transition, fossil fuels are expected to maintain its dominant share in the decades to come.

Energy Demand Growth | According to the International Energy Agency, world energy consumption was 286 mboe/d 2018YE, with oil, coal and NG representing 32%, 27% and 23%, respectively. Energy demand is expected at 358 mboe/d by 2040, representing +1% CAGR, mainly driven by the upward trend in urbanization and population growth in developing countries. But the global energy mix will change over this period. Even with oil demand continuously increasing, its contribution to the world's primary energy demand is expected to decrease by around 3%. Still, the fuel will keep leading the energy mix (28%). The predicted increase in NG demand will turn it the world's second most consumed source (25% 2040F), surpassing coal. Renewable sources will also climb in the mix because of declining production costs. It will make renewables more competitive than ever. Over the next decade, they will register the fastest percentage growth whereas NG will grow the most in volumetric terms.

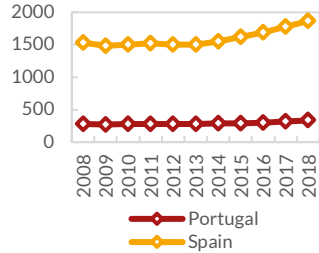
Oil Demand Drivers | Oil demand was 99 mb/d 2018YE, and it is expected to reach 111 mb/d by 2040 (+0.5% CAGR). The decelerated growth over the next years is mainly due to lower global GDP growth, improved energy efficiency and continued substitution of oil. Yet, none of the issues above should reverse the outlook for energy demand. The sectors with the biggest footprint on demand are transportation, industry (mainly petrochemicals) and electricity generation. All transportation types take the largest portion of current global oil demand, accounting for about 58%. This share is expected to remain stable until 2040. The electricity generation is the one that should offset oil demand trends, decreasing by 1 mb/d by 2040.

Figure 14: Brent Price (\$)



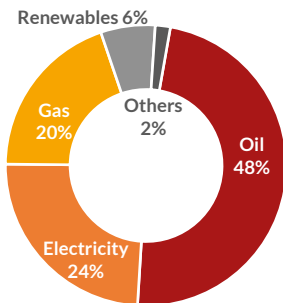
Source: Reuters, Deloitte

Figure 15: Iberian Energy Demand



Source: BP (mboe)

Figure 16: Iberian Energy Mix in 2020F (outside) vs 2025F (inside)



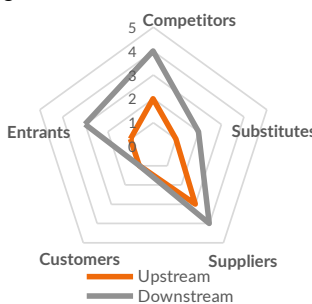
Source: European Commission

Figure 17: Refineries in Iberia



Source: INE, Team Analysis

Figure 18: Porter's Five Forces



Source: Team Analysis

OPEC | The cartel is composed of 14 of the world's largest oil-exporting nations. Together they are responsible for around 42% of total world oil production and 80% of the global proved oil reserves. They exert power in the sector. OPEC can change production to influence the global supply and thus oil prices. Current tensions in the middle east yield volatility to the sector, but we foresee that cartel's share will keep robust.

World Liquids Supply | World liquids supply is expected to reach 105.0 mb/d in 2024, growing at +1.0% CAGR. It includes crude oil, natural gas liquids, biofuels and other liquid. Non-OPEC liquid supply represents about 63% of the total supply and is expected to fall to 60% by 2040. This decrease will take place after the expected non-OPEC supply peak around 2026, followed by the US supply, both reaching peaks by the same time. After that, OPEC expects that Brazil will lead the supply growth among non-OPEC members, with 1.9 mb/d.

Oil Prices | Crude oil prices are extremely volatile and heavily affected by exogenous variables (Figure 14). Forecasting is not easy. Currently, the US shale oil production, the US crude oil stocks, and the OPEC oil supply are the main elements weighting price expectations - these are controlling forces of the global oil supply. Fluctuations in oil prices may occur for several reasons. Historically, the major price crashes occurred following either OPEC or US oversupply. Therefore, a healthy demand growth aligned with OPEC maintaining discipline over its production levels is expected to result in average prices of \$65-70/bbl 2021E.

Oil in Brazil | Brazil's total production was 2.6 mb/d 2018YE and expectations from ANP point to a total output of 7.5 mb/d by 2030. The country is expected to be within the Top 8 world's oil producers by 2040, fueled by its offshore potential. Lula and Iracema, located in the pre-salt Santos basin, are considered one of the most significant and most productive deep-water oil discoveries in the world for decades. It currently has 9 FPSOs producing at plateau level, accounting for 1.5 mboe/d, more than half of Brazil's total output. GALP has a stake of 10% in Iracema area whereas for Lula the share decreased to 9.2%, after the approval of the unitization process in 2019 (a unitisation process was required as the Lula discoveries extended outside the area first licensed, towards the adjacent areas of South of Tupi, a Transfer of Rights area and an open area. The agreement determined the new stakes attributable to each party (Petrobras, Shell and GALP)). Through its Brazilian subsidiary, Petrogal Brasil, GALP is the 3rd largest producer in the country.

NG in Mozambique | Mozambique's current NG production of 0.2 tcf is expected to grow at +13.7% CAGR to 2.8 tcf by 2040. This will represent the world's sharpest growth rate, nearly 10x higher than the world's average of 1.4%. By 2030, Mozambique is expected to become the largest gas producer in sub-Saharan Africa, surpassing Nigeria. Mozambique's current NG proven reserves are of 2.6 tcf. Due to the discovery of over 180 tcf of NG proven reserves, the Rovuma basin will constitute the world's 4th largest offshore gas project, becoming a major exporter by 2023. This project will be focused on LNG, which consists of NG that is converted to a liquid state to facilitate transportation. GALP is part of the consortium operating in Area 4 with a 10% stake. The block (Area 4) will comprise the offshore Coral South, with production expected to start in 2022, and the onshore Rovuma LNG, which will fuel the increase in NG in GALP's portfolio by 2030.

Domestic Outlook: GALP's Downstream Outlook

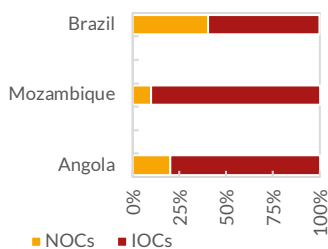
An increase in the demand for primary energy sources results from an increase in demand for by-products. The main measure of profitability in the downstream segment is the refining margin, defined as the difference between the price realized for the products to be sold and the cost of the crude delivered to the refinery.

Iberian GDP Growth | Both Portugal and Spain have been recovering from the financial crisis and subsequent sovereign debt crisis. Portugal's GDP is already reaching pre-crisis figures, while Spain is still on its path to a full recovery. In 2018, both countries grew similarly - GDP growth of 2.4% for Portugal and 2.6% for Spain. Yet, both rates are likely to decrease around 100 bps by 2024. A contraction in fixed investment and a decrease in net external demand should be the main slowdown drivers.

Iberian Energy Demand | Energy consumption in the Iberian market is mainly sourced by oil, accounting c.50% of the total. It is explained by the weight of manufacturing and transportation (c.65%). Both countries expect a drop in oil and oil by-products consumption by 203, because oil demand should decrease by 0.4% CAGR. However, oil will still lead the energy mix for this region (45% and 51% for Spain and Portugal, respectively). Electricity will continue to be the second most consumed energy for both countries, with its demand increasing 0.5% CAGR until 2030. The energy mix will be reshaped. The transportation sector is highly dependent on oil products, but Iberian countries also rely deeply on them <for heating or electricity generation. The consumption of NG products has been increasing significantly over the last years in Iberia. Authorities in both countries are encouraging the shift for cleaner energy sources with Portugal aiming an energy mix coal-free by 2030.

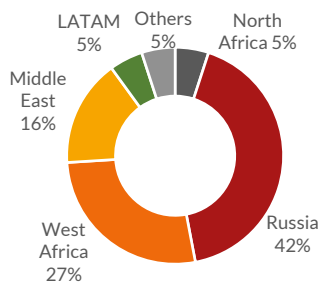
Iberian Refining Capacity, Utilization and Margin | There are 10 refineries in the Iberian Peninsula - 2 in Portugal, held by GALP, and 8 in Spain owned by Repsol, CEPSA and BP (Figure 17). In 2018, the total refining capacity was 1894 kb/d and average utilization rate 85%. GALP's refining capacity of 330 kb/d accounts for 20% of the Iberian total and average utilization rate was 83% 2015-2018. In 2018 and 2019, this rate was negatively affected by maintenance operations in both GALP refineries, reducing the refining margin. Now, GALP is fully operational. GALP's 2018 refining margin was \$5.0 per barrel, below Iberian average of \$6.2 per barrel. But the company targets a 2020 refining margin around \$6.0.

Figure 19: %NOC vs IOC in projects



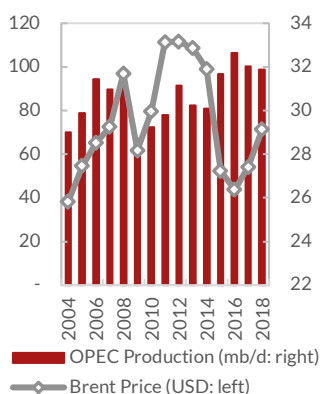
Source: Team Estimates

Figure 20: Downstream Suppliers



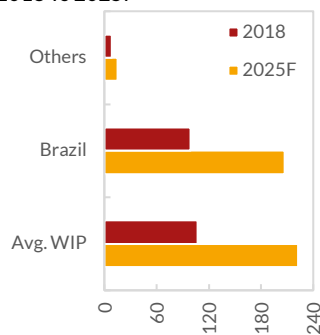
Source: GALP, Team Estimates

Figure 21: OPEC Oil Production vs Brent Price



Source: Team Estimates

Figure 22: GALP's Average WIP 2018 vs 2025F



Source: GALP, Team Estimates

Competitive Positioning

The market for oil and gas is best described as oligopolistic. However, the upstream and downstream idiosyncrasies will influence the positioning of GALP. In the upstream, the company is a relatively small but very profitable player. In the downstream, the company is market leader in the retail segment. Prices in Portugal will be significantly defined by the crude price but also by the taxation imposed by the government. Product differentiation will be relatively similar in both ends of the value chain.

Rivalry Among Existing Competitors | In the Upstream, competitors' partner up with each other. CAPEX is massive and so, risk sharing is key. Companies share the control over blocks, as agreed in the bidding rounds, where they compete for a share on the projects. The rivalry between competitors is more significant in the Downstream. GALP faces fierce competition in a perfect competition Marketing segment in Iberia. The homogeneity of the oil derived products leads to stiff competition in attracting and retaining customers. Yet, the Refining segment is monopolistic in Portugal and oligopolistic in Spain (Figure 16). Only four companies have refining capacity in Iberia.

Threat of Substitute Products | Oil and Gas are expected to keep increasing demand, keeping the fitness of GALP's portfolio. As a Downstream player, GALP will be exposed to the new dynamics in the secondary energy sources as its operations are connected to oil by-products and electricity. GALP's portfolio is mainly focused on oil by-products, but the presence in the electricity segment ensures some protection.

Bargaining Power of Customers | The main customers of the Upstream are the players in the Downstream. Usually, IOCs sell to other IOCs. GALP does not fuel the downstream with the oil produced in the upstream, as it is a financially IOC. Other players work similarly, so they have to resort to the open market. Either way, customers will have small influence setting prices. Regarding the Downstream, end consumers are highly dependent on oil and gas by-products and, consequently, have no relevant pricing power.

Bargaining Power of Suppliers | Governments can influence the bidding rounds related to reserves in their country. Usually, the preferred conditions and a higher percentage of the projects are attributed to their NOCs. As governments influence the share each company controls in the blocks, they also affect the companies' amount of crude oil for the E&P. In the Downstream, we find suppliers in two parts of the value chain. First, the Upstream players which supply oil to refineries. GALP is exposed to their power because the company buys oil in the open market. Yet, this exposition will be naturally hedged at group level by their Upstream operations. Second, the refineries that supply by-products to the marketing segment. In this case, GALP runs the two existent refineries in Portugal, being the leading supplier. Therefore, we expect suppliers to exert medium-high bargaining power.

Threat of New Entrants | Operating in the Upstream segment requires know-how and investment capacity. New joiners are unlikely because knowledge is critical, while the high CAPEX needs may benefit from economies of scale. The uncertainty around E&P projects also makes it difficult for new companies to justify high licensing fees, resulting in a low threat of new entrants. In the Downstream segment, the risk coming from new entrants is dissimilar. In the Marketing segment, it is high, while low for the Refining. The investment needed to build a Refinery is massively higher than running service stations. Yet, GALP's reputation is an asset.

Investment Summary

Our recommendation for GALP stands at BUY, with a 2020YE target price of €18.1/sh, representing a 21% upside potential to the company's stock price of €14.98/sh at January 2nd, 2020, but with high-risk. The mispricing is expected because of current uncertainties. GALP is trading at a discount against our target price because of concerns around oil prices volatility. The high potential of growth for the WIP in the Upstream (+10% CAGR 2019-2025), combined with the leading position in Portugal in the Downstream (>40% market share), and the recovery in the R&M (\$6.3/boe 2020F refining margin) should drive GALP's price up during the year. Value from the upcoming project for NG in Mozambique accounts for €0.90/sh in our estimations, but cash will only flow starting in 2025.

Key-Value Drivers

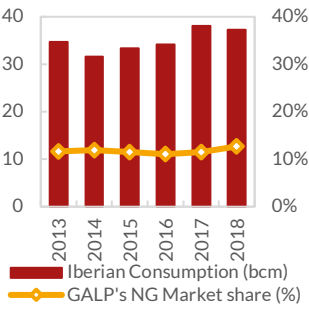
Strategic Management of the E&P Portfolio: There is risk, yet diversification is strategical to the company. GALP's E&P portfolio, with a breakeven of \$25/boe, gives the company a safety net against oil prices fluctuations. The presence in the Brazilian pre-salt, considered the benchmark worldwide, drives most of the company's E&P production and economic profit.

The accelerated production growth in ongoing projects (+24% CAGR 2015-2018) placed the company as the 3rd largest producer in the region. We forecast that GALP will maintain its strong position. The historical growth comes from the addition of 2 FPSOs during 2017-2019. The 9 FPSOs can easily increase up to 11 until 2025F because GALP and their partners in the area plan to increase the recovery rate of discovered resources from 37% to 40%. We expect an increase in production in the Lula-Iracema projects (130 kboe/d 2020F), keeping the lead of GALP's WIP and sustaining the attractive breakeven.

The projects in Mozambique will enter capital intensive phases in the new NG explorations. The Coral South FLNG and Rovuma LNG will add to the company's sustainability. Recent acquisitions in the area lead us to believe that GALP's stake in the Rovuma LNG could value up to €1.1bn in run rate.

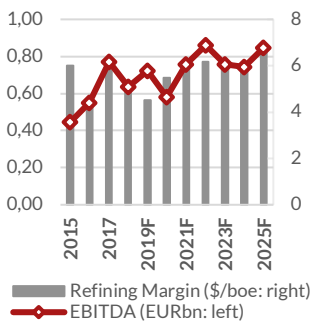
Strong Synergies in the R&M Segment: GALP is the undisputed Portuguese market leader in refining and marketing. The dominant position should be maintained, growing steadily as the demand in the Iberian

Figure 23: Iberian NG Consumption V: GALP's NG market share



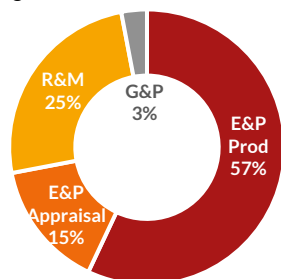
Source: BP, GALP, Team Estimates
bcm: billion cubic meters

Figure 24: Refining Margin vs. R&M EBITDA



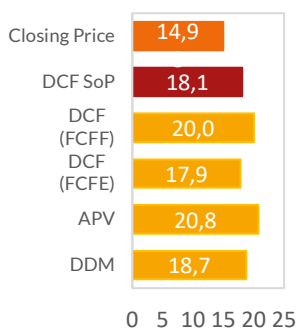
Source: GALP, Team Estimates

Figure 25: CAPEX Allocation 2025F



Source: Team Estimates

Figure 26: GALP's Price Target (€)



Source: Team Estimates

market increases. Margins in 2019 dropped due to maintenance operations. Now GALP is ready to pick up the refining margin from \$4.5/bbl 2019E to about \$6.2/bbl by 2022F.

Refining Sales depend on the used capacity of the 2 refineries, with the estimated average rate 2019E-2025F converging to a historical top of 91% (2015-2018). The marketing segment should benefit from the Refining unit improvements as the result of synergies that come from the operational vertical integration. This unit is expected to grow steadily to match energy demand (1.7% GAGR 2018-2025F), averaging 3% EBITDA margin 2019E-2025F.

Growing Sustainability through G&P | GALP is an IOC but is making efforts to become an Integrated Energy Company. CAPEX will play a role in the efforts. The company will grow its share in electricity generation and gas supply to bring more sustainable sources to the portfolio. Renewables, mainly solar, will be key for the company. We expect increases in sales of electricity to the grid, powered by energy generation in refineries and investment in renewable sources (1.7% CAGR 2018-2025F). We also expect stable growth from the supply, as GALP's 12% market share in Portugal is here to stay. The trading activities are expected to significantly increase in 2021F, because a new NG contract will increase the tradeable NG by 30%. The segment's cash flow generation is timid compared to other segments but is the more stable and sustainable.

Strong financial position: short, medium- and long-term focus | GALP's strong cash-flow generation from operations leads us to believe that GALP is in an interesting position. Economies of scale allow the company to increase its production levels and decrease OPEX, even in the absence of new projects. Yet, this fact is not stopping the company to keep searching for new investments: the new LNG projects in Mozambique brings a new energy source, a new location and adds to the sustainability of the portfolio. We believe that GALP will keep searching for new opportunities in this segment, with at least 12% of the CAPEX of the company being allocated in Exploration and Appraisal. Moreover, the G&P segment has a role to play in the long run for the company. Our analysis considers increases in energy demand from renewables in Iberia. GALP is investing now to prepare for the future, more than doubling their CAPEX for this segment.

The strategic management of the company, along with the strong synergies and strong financial position, we believe that GALP is a buy stock, despite the relevant risks. Also, investing in GALP today should secure a dividend yield of 7-8% 2025F.

Valuation methods

We used a DCF model based on a SoP FCFF by segments to achieve a price target of €18.1/sh. To complement our analysis, we run alternative valuation methods (Figure 26), all of them yielding price targets with upside. First, a DCF based on a global FCFF, reading €19.5/sh. Second, an FCFE approach with upside to €17.9/sh. Also, the DDM because of the company's focus on the dividend policy. The dividend approach points to a price target of €18.7/sh. The constant debt level led us to forecast GALP's target price using the APV approach, yielding €18.2/sh. Lastly, multiples. However, approaches of multiples per segment or considering GALP as a whole point to unreliable figures. Different risks in the segments make it difficult to assess the company through peers. The market has been trading GALP with a premium to its peers. All targets include an additional €0.9/sh from the new projects in Mozambique starting in 2025, although based on conservative transaction multiples.

Risks to achieve the price target

Investors must be aware of the impact of commodity prices, as GALP's biggest driver to E&P's value. Sales are directly linked to oil and gas prices. Increasing importance and reliance on Brazilian operations (98% of WIP 2020E) entail the risk of impacting profitability as a result of regional misbalances, although some comfort comes from the LNG production starting soon in Mozambique. Additionally, FX should be taken into account, as the industry operates in USD, but GALP consolidates EUR. Our recommendation is set with a long run Brent price of about \$68/bbl.

Valuation

Free Cash Flow to the Firm: A Sum-of-the-Parts Approach (SoP)

We value GALP using a Discounted Cash Flow (DCF) method. The unique characteristics of GALP's segments allow us to value them separately and follow a FCFF (SoP) approach. Additional approaches are used to complement our base model (overall FCFF, FCFE, APV, DDM and Multiples). Our SoP approach yields a 2020YE price target of €18.1/sh (Appendix 15). This price target includes an additional € 1.05/sh that accounts for a conservative approach on the valuation of the Rovuma LNG project.

We follow the same valuation technique for each operational segment, applying a two-stage growth model that considers detailed annual FCFF forecasts for the 2019-2025F period and assuming a constant growth rate for the perpetual period. The main assumptions inherent to our FCFF valuation relates to forecasting sales and costs for each segment are below.

Upstream: Main cash-flow driver

WIP and oil prices drive the sales. We forecast that GALP's WIP will grow at a 10.8% CAGR 2019-2025F, reaching 223 kboe/d, doubling the WIP of 2018. Growth is high, but reasonable. Production in Brazil is the main contributor, yet operations in Africa are also expected to grow until the end of the decade.

Table 6: GALP's SoP Price Target

Segment	Model	g	%	EUR
E&P	FCFF	2.75%	66.3%	13 440.67
R&M	FCFF	1.70%	23.3%	4 731.62
G&P	FCFF	1.70%	10.3%	2 093.92
Adjustments				6 123.42
Equity Value				14 142.79
Shares Outstanding				829.25
Price Target 2020YE without Mz				17.05
Mozambique				1.05
Price Target 2020YE with Mz				18.1

Source: GALP, Team Estimates

Table 7: WACC E&P, R&M and G&P

E&P	2020E	Terminal Value
Equity (Market Values)	79.93%	80.00%
Debt (Market Values)	20.07%	20.00%
WACC	9.78%	9.82%

R&M	2020E	Terminal Value
Equity (Market Values)	79.93%	80.00%
Debt (Market Values)	20.07%	20.00%
WACC	6.56%	6.51%

G&P	2020E	Terminal Value
Equity (Market Values)	79.93%	80.00%
Debt (Market Values)	20.07%	20.00%
WACC	4.64%	4.64%

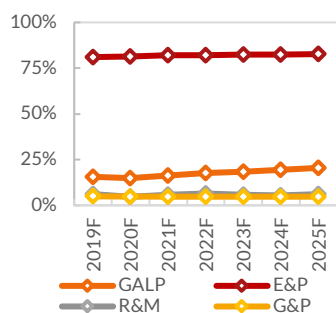
Source: Team Estimates

Table 8: Rovuma LNG

Mozambique		
Acquisition	Exxon	Total
Area	Area 4 Rovuma	Area 1 MZ LNG
Capacity (mta)	15.2	12.9
Stake bought	25.0%	26.5%
Price paid (mUSD)	2 800	3 900
P/mta (mEUR)	614.4	1 015.4
Galp ownership in mta		1.5
Galp Stake in mEUR	933.9	1 543.3
Galp MZ value (mEUR)		1 238.6
Value per share (EUR/sh)		1.49
Uncertainty factor		30%
Addition to price target (EUR/sh)		1.05

Source: GALP, Team Estimates

Figure 27: Forecasted EBITDA Margin



Source: Team Estimates

The Average Selling Price (ASP) will likely increase, as most forecasts indicate an increase in the Brent price (\$68/boe 2025F), with sales reaching €3.6bn by 2025F, yielding a 12.3% CAGR 2019-2025F. Since most of the production will still come from Brazil, it is expected that the production costs and royalties will be relatively stable throughout the forecast. Thus, we expect EBITDA margin to follow the historical trend, averaging 81% 2020-2025F.

Brazil | This location will keep being GALP's biggest value driver, with an increasing number of FPSO's in its current projects. Most of the projected growth of the WIP comes from the Brazilian pre-salt, that also benefits from low costs (the breakeven from this region is around \$30/bbl). At least 3 new blocks will start production until 2023F, but the main contributor to the company's WIP will come from the Lula-Iracema block. If all the FPSOs installed in Brazil by 2025F would be in plateau the WIP could reach 231 kboe/d by 2025F. Although, decreases in the capacity of older FPSOs are expected, so we estimate that Brazil operations will contribute with 207 kboe/d (93% of the WIP).

Angola | Blocks 14 and 14k in Angola are declining, whereas a new block is now in production - Block 32. This block will keep the contribution from Angola relatively stable. GALP expects Angola's production to represent around 1% of total WIP by 2025.

Mozambique | Gas reserves in the Rovuma Basin are among the biggest ever found. Here Galp has two projects: Coral FLNG, that starts production in 2022 and Rovuma LNG that starts in 2025. These projects will add up to the company energy mix, but we consider that the target of 70% oil and 30% gas mix will only be achieved later in this decade. For our forecast we consider gas to account for 12% in the mix.

To properly capture the potential of Rovuma project, we decided to value GALP's stake separately based on recent transactions. There are the two transactions we deemed considerable: one from Exxon and one from TOTAL. Although this second is in a different block, it is in a surrounding area. This valuation yielded an additional € 1.05 to the price target (Table 8 - Appendix 18).

Downstream: One part leading, one part growing

GALP operates in a mature market with a rather stable growth. Sales growth are forecasted to follow Portugal's economy. Different assumptions were used for the two segments. GALP's strong position in both segments lead us to a less conservative approach.

R&M | GALP is market leader in this segment where competition is fierce. In the refining business unit (BU) GALP's installed capacity gives them an advantage over their rivals, with the ASP expected to increase due to the increase in Brent Price. We forecast that the Refining Margin will increase when compared with historical values, averaging \$5.8/boe for 2020-2025. The sales from the marketing BU will be linked to the demand in the Iberian market. Knowing that the energy demand is linked with the GDP growth, we expect that sales will increase in average 1.7% in 2019-2025F. The operational improvements in the segment will lead to a 6.4% CAGR 2019-2025F of the EBITDA. More detailed information about Refining and Marketing can be found in Appendix 9.

G&P | GALP's two main BUs in this segment are the Supply & Trade of NG and the supply of Power. The Supply & Trade of NG sales will be linked to the increase in demand of NG in Portugal and the amount of tradeable NG that GALP has available. The NG demand in Portugal is expected to be 1.8% per year and the tradeable NG will increase significantly in 2022F. The power demand in Portugal is expected to increase 1.41% but GALP power unit is likely going to grow above it based on its investments in the renewables sector. This segment will represent the smallest contribution for the companies' cash flow generation, but the low capital needs and the relatively high stability of the segment will turn the segment into a valuable asset for the company, with its significance expected to grow throughout the decade. More detailed information about the Gas and Power can be found in Appendix 10.

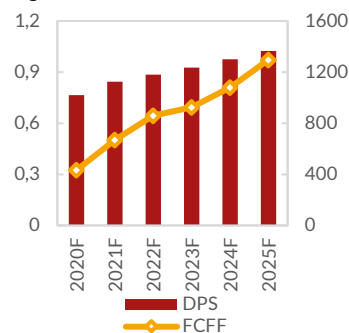
Capex and D&A

Considering the historical investment and the company's targets for CAPEX, we see an increase for all segments, all for different reasons, always above € 1bn, even reaching almost 1,2 in 2023F. Includes IFRS 16 effects. E&P CAPEX is the most demanding, consuming around 70% of the total. R&M segment will have a significant decrease in their CAPEX since historically most of its expenditures come from maintenance operations. No further operations are expected to happen throughout the forecast horizon. D&A rates for each segment are obtained via historical percentages, but differently for all segments, as some also consider production. More detailed information about the Upstream can be found in Appendix 11.

Weighted Average Cost of Capital

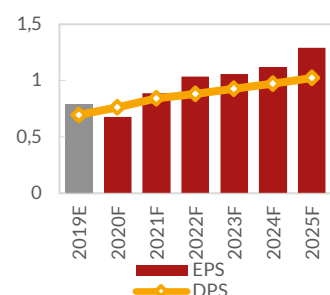
To discount FCFF we used four different WACC rates in order to account for different risks in operations and countries. We followed the CAPM approach for the computation of the **Cost of Equity**. As a proxy for the RFR we used a 10-year normalized 10Y German Government Bond Yield and added a CRP for Portugal and Brazil. Betas for the segments were estimated by computing unlevered betas for all segment peers and adjust them for GALP's capital structure and tax rate. Cost of equity ranges between 5.2% and 10.5%. To compute GALP's **Cost of Debt** we considered, again, the 10-year normalized 10Y German Government Bond Yield as the RFR, added the CRPR and, although GALP is not rated by rating agencies, we decided to add a spread of 75b.p. - according to a synthetic rating of AAA. Adjusting for taxes, we reached an after-tax cost of debt of 2.3%. Both cost of equity and cost of debt are expected to remain constant for the duration of the forecasted period, meaning that changes in WACC will only arise from changes in the capital structure.

Figure 28: Dividend vs FCFF



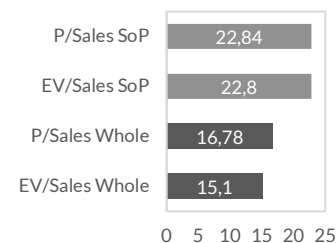
Source: Team Estimates

Figure 29: Dividend Policy



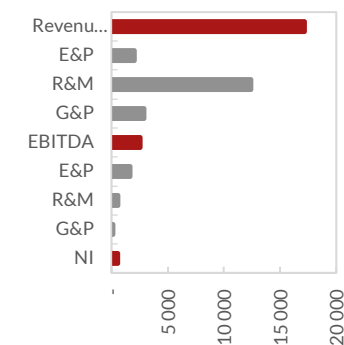
Source: Team Estimates

Figure 30: Multiples Valuation



Source: Team Estimates

Figure 31: P&L Breakdown 2020YE



Source: Team Estimates

FCFE and DDM

These complementary approaches are an interesting proxy to our price target of €18.1/sh. In the case of FCFE, it is supported by the stable capital structure the company has maintained and is expected to maintain. The use of the DDM is justified with the stable dividend payment of the company.

Dividend Policy

GALP aims at a 10% YoY dividend growth from 2019 to 2021. We deem this increase until 2021F feasible, reaching almost € 0,85/sh. From 2021 onwards, we set a 5% YoY growth that will reach a bit above €1 in 2025, representing a 6,6% CAGR 2019-2025F. In Figure 29, we can see a sustainable Payout ratio.

Peer's Selection

For GALP's peer group selection, 2 approaches were followed, consistently with our perspective so far: one group through a SoP and another looking at the company as a whole. For both approaches, we first narrowed the comparable companies based on their geographical location and then considering the similarity of various key financial results. We reached 7 peer companies for the company as a whole and never less than 4 per segment, considering the SoP (Appendix 19).

Relative Valuation

We used Relative Valuation Multiples as a complementary valuation method to the DCF, considering EV/Sales and P/Sales multiples. GALP is trading at a premium based on both multiples, EV/Sales (which is mainly explained by its potential to grow as a consequence of its high profitability E&P projects.

Using EV/Sales we reach a price target of € 15.10/sh whereas the P/Sales yields a price of € 16.78/sh, which sustains our buy recommendation using DCF approach (Appendix 20).

Financial Analysis

Strong Cash Flow Generation | Despite the general public idea, we believe that oil and gas companies will stay for good. Due to GALP's ability to generate strong CF from operations, its FCFE will increase in the 2019-2025F period (+25% CAGR). The company also presents high liquidity, mostly due to the significant levels of cash holdings. GALP should pay attractive dividends, keeping debt at low levels and still managing the working capital efficiently to present a current ratio of 1.7x to 1.8x in the upcoming years. Cash from operations will also be enough to offset demanding CAPEX requirements of up to €1.2 bn/year.

Mature industry, stable financials | Pricier R&M will affect performance. Net increase in R&M deteriorates inventory turnover, although the cash conversion cycle will stabilize around 75 days. The mature nature of the business, both in the Upstream and Downstream segments, does not require relevant working capital adjustments. Also, efficiency levels will keep stable. Asset turnover of around 1.2x is within the historical range and above peers.

Debt management | GALP's debt level is below the industry average. This does not come with a surprise, as the company is among the more profitable IOC players and has proved itself to generate stable cash flows. Book D/E is around 0.71x, while peers set the level below at 0.49x. Again, we believe that future investments are not at risk because the company can easily fund new projects with outside capital. The EBITDA margin, along with low leverage, put the debt coverage above 10x with room to improve to 16x by 2025F. Net Debt/EBITDA is comparable across the industry and GALP shows a ratio that is very close to its peers, despite the higher leverage. The ratio of 0.9x contrasts with peers 1.0x. Figures do not lie when it comes to showing how GALP is sustainably managing debt.

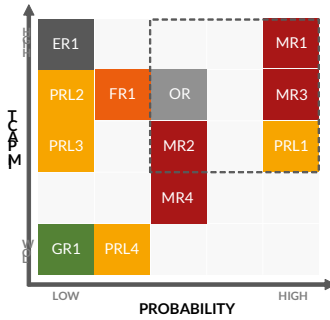
Profitability | E&P revenues are fueled by 2P Reserves (755 mboe 2018YE) and average WIP (107 kboe/d). In 2018, with a \$15/boe increase in GALP's oil and gas average selling price and the preservation of production costs, the company registered a positive YoY EBITDA margin to c.70% or €1.44 bn. In the coming years, the margin in the segment is expected to evolve positively to 83% 2025F.

Regarding revenues of the R&M segment, they increased in 2018, mainly due to higher ASP (c.27% YoY). This factor, aligned with higher maintenance operations in the refineries, led to a decrease in the company's refining margin of \$0.8/boe YoY to \$5.0/boe 2018YE. Consequently, margins were heavily affected in that year, resulting in a 17% YoY decrease in the R&M EBITDA to EUR 637mn, with margin of 5%. We take a conservative approach and forecast margins to be stable at 6% going forward.

G&P revenues increased 11% YoY to €2.9 bn 2018, mainly explained by the +8% YoY in NG sales to direct clients and the +6.7% YoY change in electricity sold to clients. The amount of electricity sold to the grid decreased by 14%, but the previously mentioned increases in sales offset much of its effects on the revenues. These changes had a small impact in the segment's EBITDA, increasing only 3.8% YoY and setting the margin at 5% 2025F.

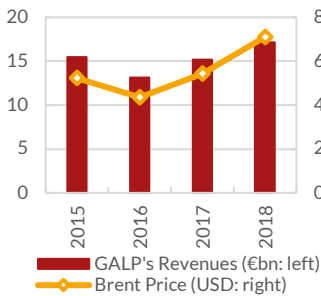
All segments make a positive whole. GALP's overall profitability is showing an upward trend since 2015. EBITDA is expected to continue evolving at +8.5% CAGR 2019-2025F, exceeding the 4% CAGR for sales. Figures are already accounting for IFRS 16 effects starting in 2019. Operational profit will grow 9.5% CAGR, regardless of operational costs increases over the years, due to augmented production and sales. The growth and later stability in generating profits will allow growing dividends distribution.

Figure 32: Risk Matrix



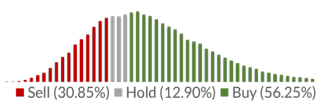
Source: Team estimates

Figure 33: GALP's Rev. vs Brent Price



Source: GALP, Thomson Reuters

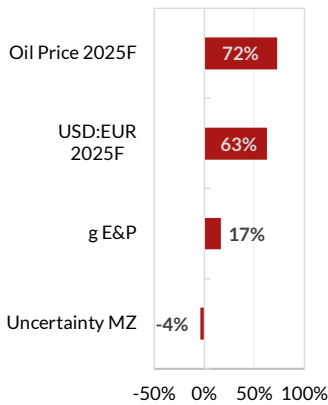
Figure 34: Monte Carlo Simulation



Mean: 18.45; Median: 18.01

Source: Team Estimates

Figure 35: Monte Carlo variables



Source: Team Estimates

ROE at unusual levels | All drivers above will set GALP's ROE averaging 18% 2019-2025F. Yet, shareholders' value in the company will also reflect the dividend distribution. Shareholders can also assess value creation through the average EVA[®] of about €1.0 bn 2019-2025F. Peer's average ROE 2019F of 11.5% show GALP's strategic way of operating businesses. The main driver for a better outlook for GALP is the operations in the Lula-Iracema region that are among the most profitable blocks worldwide, and with room to grow.

Investment Risks

Market Risk | Commodity Prices (MR1)

Commodity prices are unavoidable risks for Oil and Gas companies. GALP is highly exposed to both oil and NG prices, as any change in these variables directly affects the company's sales for both Upstream (selling price of extracted products) and Downstream (buying prices of raw material plus its effect on the by-products). Prices are mostly affected by market dynamics which GALP cannot influence.

By being an IOC, there is a natural hedging effect that works as a risk mitigating factor. Simultaneously, the risk will be softened by the use of derivatives.

Market Risk | Exchange Rates (MR2)

GALP operates in several locations. It is mostly exposed to USD, the standard currency for the Oil & Gas industry, but also to BRL, as GALP's Brazilian subsidiary (Petrogal Brasil) reports in its domestic currency. Both Upstream and Downstream sales are sensitive to FX because GALP consolidates in EUR. The exposition to USD is unquestionably significant. We estimate a ΔEBITDA of €110-120m from a +0.05 (500 pips) variation in EUR: USD. The natural hedge that comes from the presence in the Upstream and Downstream will decrease the impact of the risk. GALP also manages to mitigate it at a corporate level, mainly through derivatives.

Market Risk | Energy Transition (MR3)

The worldwide economy is highly dependent on fossil fuels, but the expectation is for this dependence to decrease in the following decades. This decrease will come from the growth of renewable sources of energy generation and the substitution of fossil fuels for electricity, mostly in terms of transportation. The electrification of other industries is also unavoidable (e.g. construction). The other big shift in the energy segment will be the surpassing of coal by NG as the second most used fossil fuel. This is aligned with the expected evolution in GALP's WIP, where the current mix of oil and gas is 90% and 10%, respectively, and the expected mix is 70% and 30%. The company is trying to follow the trend of electrification to mitigate energy transition risks through investments in the renewable energies' segment (10 to 15% of CAPEX).

Operational Risk | E&P Uncertainty (OR)

The selection of E&P projects is fundamental for IOCs, but this process encompasses a relevant uncertainty to predict the economic value. If the company manages to efficiently select its projects, it still has to overcome the possible problems that will arise with their execution, development and operation. Too many projects without commercially recoverable reserves might weight heavily on the balance sheet and jeopardize the whole group. This risk is highly diminished by the strategic choices of the company, with most of the projects being explored in locations where the company and their partners are already experienced (i.e. ultra-deep waters). The use of new technologies, e.g. AI, to diminish the uncertainty risk has become the norm in the industry. GALP is following suit, working with IBM to enhance seismic interpretation.

Political, Regulatory and Legal Risks | IMO 2020 and Paris Agreement (PRL1)

High-sulfur fuel was very common for marine bunkers, and this type of fuel leads to both CO₂ emissions and high sulfur dioxides emissions. The latter is linked to acid rain and lung cancer. IMO 2020 will limit the global bunker fuel to 0.5% sulfur content, lowering it from the current 3.5%. In 2018YE, marine bunkers represented 21% of the company's R&M wholesale unit. To comply with IMO 2020, GALP has already implemented the required changes in its refining processes. In the past years, GALP has also been adjusting its operations to reduce the GHG emissions as required by the Paris Agreement. In the case of new regulations, further changes will need to be made. These changes will lead to periods of maintenance and adaptation, negatively impacting usage capacity and refining margins, and, consequently, the profitability of the R&M segment. GALP is actively working to gradually diversify their portfolio, reducing the operational impact that more strict regulations would have.

Table 9: Combined Sensitivity Analysis

Price target	Oil Price 2025F											
	18.10	65.00	65.50	66.00	66.50	67.00	67.50	68.00	68.50	69.00	69.50	70.00
0.85	14.43	14.87	15.12	15.37	15.42	15.88	16.15	16.41	16.68	16.96	17.23	17.23
0.86	15.10	15.35	15.60	15.85	16.11	16.37	16.64	16.91	17.18	17.46	17.74	17.74
0.87	15.57	15.82	16.08	16.33	16.59	16.86	17.13	17.40	17.68	17.96	18.24	18.24
0.88	16.04	16.29	16.55	16.81	17.07	17.34	17.61	17.89	18.17	18.45	18.74	18.74
0.89	16.51	16.76	17.02	17.29	17.55	17.83	18.10	18.38	18.66	18.95	19.24	19.24
0.90	16.97	17.23	17.50	17.76	18.03	18.31	18.59	18.87	19.15	19.44	19.74	19.74
0.91	17.44	17.70	17.97	18.24	18.51	18.79	19.07	19.35	19.64	19.94	20.23	20.23
0.92	17.90	18.17	18.44	18.71	18.98	19.27	19.55	19.84	20.13	20.43	20.73	20.73
0.93	18.36	18.63	18.90	19.18	19.46	19.74	20.03	20.32	20.62	20.92	21.22	21.22

Source: Team Estimates

Table 10: Sensitivity Analysis on terminal growth rate

Change in g	-0.75%	-0.50%	-0.25%	0%	0.25%	0.50%	0.75%
Price Target	17.00	17.32	17.69	18.10	18.57	19.12	19.75
Upside/Downside	13.5%	15.6%	18.1%	20.8%	24.0%	27.6%	31.9%
Recommendation	Hold	Hold	Buy	Buy	Buy	Strong	Strong

Source: Team Estimates

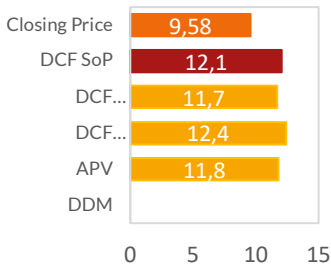
Date: March 9th, 2020
 Ticker: GALP.LS (Reuters)

Current Price: EUR 9.58
 EUR 1.000: USD 1.145

Recommendation: **BUY (26% Upside)** High-Risk
 Price Target: **EUR 12.06 (USD 13.8)** 2020YE

COVID-19 UPDATED SNAPSHOT

Figure 36: GALP's Price Target (€)



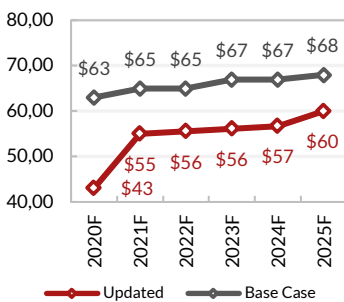
Source: Team estimates

GALP: Still Strong, Strategic and Sustainable

We issue a **BUY** recommendation in our updated equity research for Galp Energia S.G.P.S., S.A. (GALP), with a price target of €12.1/sh for 2020YE using a DCF model, implying a 26% upside potential from the March 9th, 2020 closing price of €9.58/sh, but we assess it as high-risk. Our additional valuation methods still support our updated valuation, with the exception of the DDM, with this method becoming an outlier, given GALP's dividend growth profile.

The first version of this report was finished on January 15th, 2020. Since then, the world has changed. The COVID-19 pandemic changed everything in our daily lives, and it also impacted the world economy like never before. Most of the global industries were negatively impacted by the pandemic, and the Oil & Gas industry was not an exception.

Figure 37: Oil Prices Forecast (\$/boe)



Source: Team estimates

Firstly, all of the energy sector was negatively affected by the decrease in demand of all types of energy. Most countries applied some sort of lockdown, leading to a major crash in demand. Specifically, the oil industry suffered from all fronts. The decrease in demand for the final consumer, either households or businesses, made the need for refined oil products to decrease. The decrease in the use of installed refining capacity all over the industry impacted negatively the need for the acquisition of oil, leading to a snowball effect that made the oil price reach historically low prices. Even though the problems between OPEC's Saudi Arabia and Russia were resolved, this settlement wasn't enough to offset the major impact that the pandemic had in the oil prices.

Due to the major impacts caused by the pandemic, the team made a new update in March, reflecting the new reality. We reviewed our whole forecast to understand what the impacts on GALP's operations are. With that in mind, adjustments needed to be done. As seen in Figure 37, our oil price forecast was adjusted in order to capture the new reality. Our average Brent price for our forecast period went from \$65.67 to \$54.50, with the 2020F being the one with the biggest adjustment, going from \$63.00 to \$43.00. There is an expectation that, with the combination of the new agreement that the OPEC with the possible return to normal in the next couple of years, the oil price will eventually recover to previous values. However, we decided that would be prudent to have a conservative approach, and in the terminal period our forecasted Brent Price registered a decrease of \$8.00, being fixated now at \$60.

Table 11: Industry's Abbreviations

Abbreviations	
bbbl	Barrel of Oil
kb/d	Thousand bbl per Day
mb/d	Million bbl per Day
boe	Barrel of Oil Equivalent
mboe	Million boe
kboe/d	Thousand boe per Day
mton	Million Tonnes
mta	Million Tonnes per Annum
IOC	Integrated Oil Company
NOC	National Oil Company
WIP	Working Interest Production
FPSO	Floating Production Storage and Offloading

Source: Team estimates

Operationally, just a few adjustments were made. We strongly believe that the company has the capacity to quickly recover to previous operational levels, and so we forecasted that the main impact would be felt during this year. Accordingly, we made an adjustment for the growth in production in 2020 for the E&P segment (from 12% to 7%) but maintained the growth that we forecasted for the rest of the years. We expect the R&M segment to be able to maintain its production levels, being mainly affected by the decrease in their refining margin, mainly explained by the decrease in the ASP. This decrease made the average Refining Margin for the forecasted period to go from \$6.08/boe to \$4.53/boe. Dividends were adjusted for 2020, as we truly believe GALP will strategically adjust their financial decisions to the current moment. GALP's partnerships are important in a normal scenario, and even more important in crisis. By working together, all companies can assure that operations continue as planned.

Even with all the necessary adjustments that were made in order to capture new reality in which the company operates, we still see GALP as a strong, strategic and sustainable company. Due to a strong production portfolio that's able to add value even in situations of low oil prices, the company is strategically positioned to keep growing in the years to come, driven by its increasing production and investments in new BUs aligned with the upcoming Energy Transition, either in solar power with ACS or natural gas with Mozambique. That sets the base for a sustainable growth, both financial and environmentally, in the medium and long term.

The Expected Cash Flow approach

Different scenarios with different probabilities: what is the expected value of the valuation?

When forecasting all financial statements and computing some key figures (such as the WACC), several assumptions must be made. These assumptions range from a variety of topics. Some are more general, such as the economic growth rate for the upcoming years, or any given exchange rate between two currencies the company operates. Other assumptions are more industry-specific and will change from company to company. In GALP's case, we can talk about oil price (in this case, the Brent oil price), the company's hydrocarbon production or the amount invested in renewable energy sources.

Obviously, these assumptions are made based on material public information, such as official documents and trusted sources (Table 12), as well from different analysis made by the analyst. However, it is possible that not all forecasted figures hit exactly as expected. To fight this, analysts tend to present a set of scenarios where different sets of assumptions are combined, yielding different final values for the valuation. Normally, a base case is built showing the most probable scenario, given the analyst expectations. In addition, blue sky scenario (or bull case) is built, where more favorable assumptions impact the valuation positively, compared to the base case. In contrast with the previous, a grey sky scenario (or bear case) is made having less favorable assumptions, leading to a negative impact on the valuation, compared to the base case.

Usually, these cases are presented as separate values, that are left to the consideration of the investor. However, there is a way to consider all options, together. In the late 90's, the Financial Accounting Standards Board (FASB) presented a new method to calculate the value of an asset or liability, for balance sheet recognition: the expected cash flow approach (FASB, 2008). It is possible to use this approach for valuation as well.

Incorporating probabilities into the valuation

The expected cash flow approach tells accountants to consider the different possible cash-flows together with the probability of each cash-flow. And the way to do so is to utilize the concept of expected value. In Statistics, the expected value, denoted as $E[X]$, where X is a random variable, consists in a weighted average of the different options of the variable, where the weights are the probability of occurring. The FASB presents the following example: "a cash flow might be \$100, \$200, or \$300 with probabilities of 10 percent, 60 percent, and 30 percent, respectively. The expected cash flow is \$220", resulting from this calculation: $(\$100 \times .1) + (\$200 \times .6) + (\$300 \times .3) = \220 (FASB, 2008, pg. 13). The same concept can be applied to present value.

The main purpose of this additional chapter is to use the expected cash flow approach together with a base case, a blue scenario and a grey sky scenario. One can argue that the sole existence of these scenarios plus the sensitivity analysis performed would be enough. Indeed, the result is similar, but definitely not the same. The separated scenarios and the sensitivity analysis serve to show different combinations of assumptions, and the investor is left to pick the one believes the most. With the suggested approach, I aim to provide a single price target that has all the different scenarios incorporated in that number. This is something common in the industry. Several times we see that analysts give price target that are a combination of different valuations, or different scenarios. Something like "50% DCF and 50% Multiples", or "55% base case and 45% bear case". I want to do something similar, by having a single price target that will be the sum of probability-weighted present values, i.e., the price target of each scenario. To use the expected cash-flow approach it is necessary to define the scenarios and the probability of happening of each scenario.

Scenarios

The base case was built on top of several assumptions, all laid out in this report (Appendices 6, 7, 8, 9, 10, 11, 13 and 14). To that base case we performed some sensitivity analysis to the oil price (Table 13), showing how the price target changes with the 2025F Brent price changes. In addition, two scenarios were built from the base case. I decided to alter four variables and see how the price target would change:

Brent price for year 2025 and Terminal value
FX rate for year 2025 and Terminal value
E&P Production growth for 2025 and Terminal value
Uncertainty factor for the Rovuma LNG project

These specific variables were chosen due to the fact that the team considers them to be the ones more susceptible to higher changes, since all of them are heavily exposed to either the changes in the global market or geopolitical impacts. Please note that the below scenarios were already adjusted to reflect the COVID-19 impacts.

Base case scenario | Oil price 60\$; EUR/USD 0.89; Prod growth 10%; MZ uncertainty factor 30%

The base case considers a 2025 and Terminal period oil price of 60\$/bbl (after the COVID adjustment). Similarly, for the same period the EUR/USD FX rate was adjusted to 0.89. The E&P production growth for the 2025 is 10%, affecting the and Terminal period. Finally, the uncertainty factor is 30%, showing our conservative approach.

Price target: 12.1€ per share

Grey sky scenario | Oil price 50\$; EUR/USD 0.87; Prod growth 8.5%; MZ uncertainty factor 50%

In the grey sky scenario, we considered a set of bad market conditions that will drive down our valuation. Oil price and the FX rate for 2025 and TV were reduced to 50\$/bbl and 0.87 respectively. In addition, to really picture a disaster scenario, we lowered future production levels, yielding now an 8.5% production

Table 12: Example of source, from the US Energy Information Administration

Prices	2018	2019	2020	2021
WTI Crude Oil ^a (dollars per barrel)	65.07	56.99	38.76	44.72
Brent Crude Oil (dollars per barrel)	71.21	64.34	41.19	47.07
Gasoline ^b (dollars testper gallon)	2.73	2.60	2.15	2.23
Diesel ^c (dollars per gallon)	3.18	3.06	2.54	2.55
Heating Oil ^d (dollars per gallon)	3.01	3.00	2.44	2.46
Natural Gas ^d (dollars per thousand cubic feet)	10.46	10.46	10.48	10.87
Electricity ^d (cents per kilowatthour)	12.87	13.04	13.09	13.22
Coal ^e (dollars per million Btu)	2.06	2.02	1.96	2.04

^aWest Texas Intermediate.
^bAverage regular pump price.
^cOn-highway retail.
^dU. S. Residential average.
^eElectric power generation fuel cost.

Source: EIA

Table 13: Base case sensitivity analysis to the 2025 and Terminal value Brent price

Oil Price 2025F	Price Target
30.00	4.11
35.00	4.16
40.00	4.70
45.00	5.76
50.00	7.35
55.00	9.45
60.00	12.06
65.00	15.17
70.00	18.79
75.00	22.90
80.00	27.50
85.00	32.60
90.00	38.18

Source: Team estimates

growth for 2025, limiting the impact of TV. Finally, the uncertainty factor of Mozambique was increased to 50%, truly showing a 50/50 odds of the project happening.

Price target: 5.89€/sh

Blue sky scenario | Oil price 65\$; EUR/USD 0.91; Prod growth 11.5%; MZ uncertainty factor 15%

In the blue sky scenario, we considered the inverse of the previous situation. Here a set of great market conditions will drive up our valuation. Oil price and the FX rate were increased to 65\$/bbl and 0.91 respectively. In addition to a great financial landscape, we also jacked up production levels to an amazing 11.5% production for 2025, leading to a really good TV impact. Finally, the uncertainty factor of Mozambique was reduced to 15%, showing a very good expectation on operational level, but still accounting for geopolitical risks.

Price target: 18.67€/sh

Now that the scenarios are set, it is necessary to understand what are the odds of each one.

Defining the probability of each scenario

The biggest challenge of this proposed approach is defining the probability of occurring of each scenario. The oil market has been quite volatile in 2020YTD. Between the increase in offer in the beginning of the year, and the decrease in demand fueled by the pandemic, oil prices dipped and have been slowly rising again. At this point the market expects an overall increase in oil for the upcoming years, but it is hard to tell exactly how prices will evolve.

Going back to the source of our expected cash flow approach, when defining the probabilities, the FASB talks about different ways to do so. For instance, one can opt for a more naïve choice by just making an average of the three scenarios, where all probabilities are equal, i.e., 33%. Or we might opt to attribute different probabilities, like 50% for base case, and 25% for each of the remaining cases. Or a different set of probabilities based on experience, research and expectation. However, this would not differ that much from just analyzing a sensitivity analysis. The purpose is to use a mathematical method, to add value on what was made until now. With that, the investor can compare the result to the sensitivity analysis.

In order to obtain the probabilities, we used a Monte Carlo simulation. The idea was to run a simulation with 100 000 trials and understand which price targets appear more with different random combinations of the assumptions. With the distribution of results, we can obtain the probabilities of having the grey sky price target or less, the probability of having the blue sky price target or more. The remaining of the distribution is used for the probability of obtaining our base case price target, or close to it.

To run the simulation, it is needed to define each assumption and the type of distribution that best fits the type of data. For the *Brent price for year 2025 and Terminal value* assumption, a lognormal distribution with mean 60 USD/bbl was chosen (Figure 38). This option aims to follow the same conservative approach that is followed throughout the report, as the positive skewness of this distribution will allocate higher frequency to lower values, which is something that has been characteristic of oil price in 2020. In addition, for the FX rate and the MZ uncertainty factor, a normal distribution was chosen, and, finally, for production growth, a triangular distribution was chosen. The resulting simulation is visible in Figure 39.

From our simulation we were able to define that the probability of the base case, grey sky and blue sky scenarios are 68.89%, 10.99% and 20.12%, respectively (Table 15).

It seems that the base case might be overweighted, which could lead to us say that GALP is not that sensitive to changes. However, that is not a conclusion I would jump to. It is important to have in mind that the updated base case, when compared to the original one, already shows a rather large decrease. Which means that the updated base case is already the picture of unfavorable conditions. This means that the updated grey sky scenario is something like the “worst of a bad situation”. This goes in line with the probabilities obtained with the simulation. By interpreting them, the most probable scenario is the share price walk towards the base case, with the market conditions slowly recovering from the pandemic initial impacts. Also, there is a larger probability of a very good outcome (blue sky) then a bad one, since there is more potential to grow, then to sunk even further.

Final result: the expected cash flow approach price target is 12.74€/sh

By having the three scenarios prices and the probability of each scenario, I can present a 12.74€/sh price target, which represents a single figure that comprises all different scenarios within it (Table 16).

$$(12.1 * 0.6889) + (5.89 * 0.1099) + (18.67 * 0.201) = 12.74$$

It is interesting to compare with our base case price target. We can see that it is not far away for it. The expected cash flow approach price target is 0.64€/sh higher, which makes sense due to the higher weight of the blue sky, compared to the grey sky.

It could be further discussed which approach is more accurate. If to have a mathematically set price target or if to leave it at the experience of the investor to choose which scenario they would believe more in. However, I believe that such discussion might not be relevant, as different investors have different profiles. A more experienced investor might opt to go by a “gut feeling”, whereas a less experienced investor might rely more on a mathematical approach.

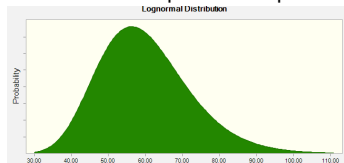
By adding the expected cash flow approach, I believe to have provided the investor with yet another piece of information to help in the investment decision. It is important to note that this approach yields a similar result to our SoP DCF, further supporting the initial buy recommendation.

Table 14: Price target scenarios

Price Target	Grey sky	Base case	Blue sky
Oil price	50	60	65
EUR/USD	0.87	0.89	0.91
E&P Prod	8.5%	10%	11.5%
MZ	50%	30%	15%

Source: Team estimates

Figure 38: Lognormal distribution chosen for Brent price assumption



Source: Team estimates, Oracle (2020)

Figure 39: Monte Carlo simulation for the expected cash flow approach



Source: Team estimates

Table 15: Probability of each scenario

Scenario	Probability from Monte Carlo
Grey sky	10.99%
Blue sky	20.12%
Base case	68.89%

Source: Monte Carlo simulation, team estimates

Table 16: Expected cash flow approach price target

Scenario	Probability	Price target
Grey sky	10.99%	5.87 €
Blue sky	20.12%	18.89 €
Base case	68.89%	12.1 €
Expected cash flow price target		12.74 €

Source: Team estimates

Appendices

Appendix 1: Income Statement (GALP)

Income Statement (mEUR)	2017	2018	2019E	2020F	2021F	2022F	2023F	2024F	2025F	CAGR 19-25F
Operating Income										
Sales and service rendered	15,201.0	17,182.0	16,206.5	17,177.4	18,349.0	18,959.4	19,339.7	19,716.5	20,726.3	4.2%
Exploration & Production	1,044.0	1,687.0	1,795.0	2,042.8	2,339.5	2,596.9	2,971.2	3,268.3	3,648.8	12.6%
Refining & Marketing	11,722.0	12,780.0	11,768.9	12,411.4	13,279.4	13,295.8	13,260.1	13,340.0	13,974.9	2.9%
Gas & Power	2,593.0	2,885.0	2,816.0	2,900.1	2,910.6	3,250.8	3,296.1	3,299.8	3,298.0	2.7%
Other	134.0	142.0	144.4	146.9	149.4	151.9	154.5	157.1	159.8	1.7%
Eliminations	-292.0	-312.0	-317.8	-323.8	-329.8	-336.0	-342.3	-348.7	-355.2	1.9%
Other operating income	105.0	141.0	143.4	145.8	148.3	150.8	153.4	156.0	158.7	1.7%
Total operating income	15,307.0	17,322.0	16,349.9	17,323.2	18,497.3	19,110.3	19,493.1	19,872.6	20,885.0	4.2%
Operating costs										
Cost of sales & Production costs	13,524.0	15,077.0	13,808.7	14,764.4	15,489.7	15,764.2	15,922.9	16,066.2	16,638.4	3.2%
Exploration & Production	194.0	247.0	340.1	381.0	423.1	469.8	521.7	574.0	631.7	10.9%
Refining & Marketing	10,951.0	12,143.0	11,044.4	11,829.0	12,523.2	12,435.0	12,504.4	12,596.5	13,129.4	2.9%
Gas & Power	2,461.0	2,748.0	2,677.7	2,760.1	2,768.8	3,093.2	3,136.0	3,139.6	3,137.8	2.7%
Other	104.0	116.0	116.6	117.7	120.1	123.2	125.0	127.2	129.7	1.8%
Eliminations	292.0	317.0	305.2	323.4	345.5	357.0	364.2	371.3	390.3	4.2%
RCA Effect	116.0	-65.0	-65.0	-65.0	-65.0	-65.0	-65.0	-65.0	-65.0	0.0%
EBITDA IFRS	1,899.0	2,180.0	2,541.3	2,558.8	3,007.6	3,346.1	3,570.2	3,806.4	4,246.6	8.9%
Exploration & Production	850.0	1,440.0	1,454.9	1,661.8	1,916.4	2,127.1	2,449.6	2,694.3	3,017.2	12.9%
Refining & Marketing	771.0	637.0	724.5	582.4	756.2	860.8	755.8	743.4	845.5	2.6%
Gas & Power	132.0	137.0	138.3	140.0	141.7	157.6	160.1	160.1	160.1	2.5%
Other	30.0	26.0	27.8	29.2	29.3	28.7	29.5	29.9	30.1	1.3%
Eliminations	0.0	5.0	-12.7	-0.3	15.7	21.0	21.9	22.6	35.1	-
D&A, Provisions & Impairments	784.0	682.0	774.1	840.9	894.4	938.8	988.8	1,032.0	1,093.7	5.9%
Exploration & Production	383	329	465.702	500.1	535.9	576.4	621.9	668.3	719.3	7.5%
Refining & Marketing	357	337	235.453	258.3	269.4	268.6	256.0	255.7	267.4	2.1%
Gas & Power	18	21	43.9934	45.1	58.6	61.6	77.6	76.0	74.5	9.2%
Other	4.0	4.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0%
Eliminations	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0%
Provisions (including CESE)	22	-9	29	37.3	30.4	32.3	33.3	32.0	32.5	1.9%
Total operating costs	14,308.0	15,759.0	14,582.8	15,605.3	16,384.1	16,702.9	16,911.7	17,098.2	17,732.1	3.3%
EBIT IFRS	1,115.0	1,498.0	1,767.1	1,717.9	2,113.2	2,407.3	2,581.4	2,774.4	3,152.9	10.1%
Exploration & Production	467.0	1,111.0	989.2	1,161.7	1,380.5	1,550.7	1,827.7	2,026.0	2,297.8	15.1%
Refining & Marketing	414.0	300.0	489.0	324.0	486.8	592.2	499.8	487.7	578.1	2.8%
Gas & Power	114.0	116.0	94.3	94.9	83.1	96.0	82.6	84.1	85.7	-1.6%
Other	26.0	22.0	27.8	29.2	29.3	28.7	29.5	29.9	30.1	1.3%
Eliminations	0.0	5.0	-12.7	-0.3	15.7	21.0	21.9	22.6	35.1	-
Net financial expenses	-14.0	-12.0	-82.1	-95.9	-101.6	-106.1	-111.5	-116.9	-122.2	6.8%
Exchange gains/losses & derivatives	-18.0	-59.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0%
Operating leases interest (IFRS 16)	0.0	0.0	-92.2	-86.0	-80.6	-76.4	-73.2	-70.9	-68.9	-4.7%
Results from financial investments	163.0	129.0	129.0	129.0	129.0	129.0	129.0	129.0	129.0	0.0%
Financial result	131.0	58.0	-45.3	-52.9	-53.2	-53.5	-55.7	-58.8	-62.0	5.4%
Profit before taxes	1,246.0	1,556.0	1,721.8	1,665.1	2,060.1	2,353.8	2,525.7	2,715.5	3,090.9	10.2%
Income taxes	-496.0	-736.0	-542.4	-524.5	-648.9	-741.5	-795.6	-855.4	-973.6	10.2%
SPT&IRP	0.0	0.0	-296.8	-348.5	-414.1	-465.2	-548.3	-607.8	-689.4	15.1%
Energy sector extraordinary contribution (CESE)	-64.0	-60.0	-64.8	-64.2	-63.2	-63.0	-63.8	-63.6	-63.4	-0.3%
Net Income	686.0	760.0	817.9	727.9	933.8	1,084.1	1,118.0	1,188.8	1,364.5	8.9%
Non-controlling interests	-88.0	-151.0	-158.8	-163.8	-195.7	-226.2	-240.8	-259.7	-294.6	10.9%
Net income to common shareholders	598.0	609.0	659.1	564.1	738.1	857.9	877.2	929.0	1,069.8	8.4%
Shares outstanding (million)	829.3	829.3	829.3	829.3	829.3	829.3	829.3	829.3	829.3	0.0%
Basic and diluted EPS	0.72	0.73	0.79	0.68	0.89	1.03	1.06	1.12	1.29	8.4%
DPS	0.00	0.63	0.70	0.77	0.84	0.88	0.93	0.97	1.02	6.6%
Dividend (€m)	0.0	524.5	577.0	634.6	698.1	733.0	769.7	808.2	848.6	6.6%
Payout	0.00	0.69	0.71	0.87	0.75	0.68	0.69	0.68	0.62	-2.1%

Appendix 2: Common-size Income Statement (GALP)

Income Statement - Common-size	2017	2018	2019E	2020F	2021F	2022F	2023F	2024F	2025F
Operating Income									
Sales and service rendered	99.31%	99.19%	99.12%	99.16%	99.20%	99.21%	99.21%	99.21%	99.24%
Exploration & Production	6.82%	9.74%	10.98%	11.79%	12.65%	13.59%	15.24%	16.45%	17.47%
Refining & Marketing	76.58%	73.78%	71.98%	71.65%	71.79%	69.57%	68.02%	67.13%	66.91%
Gas & Power	16.94%	16.66%	17.22%	16.74%	15.73%	17.01%	16.91%	16.60%	15.79%
Other	0.88%	0.82%	0.88%	0.85%	0.81%	0.79%	0.79%	0.79%	0.77%
Eliminations	-1.91%	-1.80%	-1.94%	-1.87%	-1.78%	-1.76%	-1.76%	-1.75%	-1.70%
Other operating income	0.69%	0.81%	0.88%	0.84%	0.80%	0.79%	0.79%	0.79%	0.76%
Total operating income	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%	100.00%
Operating costs									
Cost of sales & Production costs	88.35%	87.04%	84.46%	85.23%	83.74%	82.49%	81.68%	80.85%	79.67%
Exploration & Production	1.27%	1.43%	2.08%	2.20%	2.29%	2.46%	2.68%	2.89%	3.02%
Refining & Marketing	71.54%	70.10%	67.55%	68.28%	67.70%	65.07%	64.15%	63.39%	62.87%
Gas & Power	16.08%	15.86%	16.38%	15.93%	14.97%	16.19%	16.09%	15.80%	15.02%
Other	0.68%	0.67%	0.71%	0.68%	0.65%	0.64%	0.64%	0.64%	0.62%
Eliminations	1.91%	1.83%	1.87%	1.87%	1.87%	1.87%	1.87%	1.87%	1.87%
RCA Effect	0.76%	-0.38%	-0.40%	-0.38%	-0.35%	-0.34%	-0.33%	-0.33%	-0.31%
EBITDA IFRS	12.41%	12.59%	15.54%	14.77%	16.26%	17.51%	18.32%	19.15%	20.33%
Exploration & Production	5.55%	8.31%	8.90%	9.59%	10.36%	11.13%	12.57%	13.56%	14.45%
Refining & Marketing	5.04%	3.68%	4.43%	3.36%	4.09%	4.50%	3.88%	3.74%	4.05%
Gas & Power	0.86%	0.79%	0.85%	0.81%	0.77%	0.82%	0.82%	0.81%	0.77%
Other	0.20%	0.15%	0.17%	0.17%	0.16%	0.15%	0.15%	0.15%	0.14%
Eliminations	0.00%	0.03%	-0.08%	0.00%	0.08%	0.11%	0.11%	0.11%	0.17%
D&A, Provisions & Impairments	5.12%	3.94%	4.73%	4.85%	4.84%	4.91%	5.07%	5.19%	5.24%
Exploration & Production	2.50%	1.90%	2.85%	2.89%	2.90%	3.02%	3.19%	3.36%	3.44%
Refining & Marketing	2.33%	1.95%	1.44%	1.49%	1.46%	1.41%	1.31%	1.29%	1.28%
Gas & Power	0.12%	0.12%	0.27%	0.26%	0.32%	0.32%	0.40%	0.38%	0.36%
Other	0.03%	0.02%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Eliminations	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Provisions (including CESE)	0.14%	-0.05%	0.18%	0.22%	0.16%	0.17%	0.17%	0.16%	0.16%
Total operating costs	93.47%	90.98%	89.19%	90.08%	88.58%	87.40%	86.76%	86.04%	84.90%
EBIT IFRS	7.28%	8.65%	10.81%	9.92%	11.42%	12.60%	13.24%	13.96%	15.10%
Exploration & Production	3.05%	6.41%	6.05%	6.71%	7.46%	8.11%	9.38%	10.19%	11.00%
Refining & Marketing	2.70%	1.73%	2.99%	1.87%	2.63%	3.10%	2.56%	2.45%	2.77%
Gas & Power	0.74%	0.67%	0.58%	0.55%	0.45%	0.50%	0.42%	0.42%	0.41%
Other	0.17%	0.13%	0.17%	0.17%	0.16%	0.15%	0.15%	0.15%	0.14%
Eliminations	0.00%	0.03%	-0.08%	0.00%	0.08%	0.11%	0.11%	0.11%	0.17%
Net financial expenses	-0.09%	-0.07%	-0.50%	-0.55%	-0.55%	-0.56%	-0.57%	-0.59%	-0.58%
Exchange gains/losses & derivatives	-0.12%	-0.34%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Operating leases interest (IFRS 16)	0.00%	0.00%	-0.56%	-0.50%	-0.44%	-0.40%	-0.38%	-0.36%	-0.33%
Results from financial investments	1.06%	0.74%	0.79%	0.74%	0.70%	0.68%	0.66%	0.65%	0.62%
Financial result	0.86%	0.33%	-0.28%	-0.31%	-0.29%	-0.28%	-0.29%	-0.30%	-0.30%
Profit before taxes	8.14%	8.98%	10.53%	9.61%	11.14%	12.32%	12.96%	13.66%	14.80%
Income taxes	-3.24%	-4.25%	-3.32%	-3.03%	-3.51%	-3.88%	-4.08%	-4.30%	-4.66%
SPT&IRP	0.00%	0.00%	-1.82%	-2.01%	-2.24%	-2.43%	-2.81%	-3.06%	-3.30%
Energy sector extraordinary contribution (CESE)	-0.42%	-0.35%	-0.40%	-0.37%	-0.34%	-0.33%	-0.33%	-0.32%	-0.30%
Net Income	4.48%	4.39%	5.00%	4.20%	5.05%	5.67%	5.74%	5.98%	6.53%
Non-controlling interests	-0.57%	-0.87%	-0.97%	-0.95%	-1.06%	-1.18%	-1.24%	-1.31%	-1.41%
Net income to common shareholders	3.91%	3.52%	4.03%	3.26%	3.99%	4.49%	4.50%	4.67%	5.12%

Appendix 3: Statement of Financial Position (GALP)

Balance Sheet (m€)	2017	2018	2019E	2020F	2021F	2022F	2023F	2024F	2025F	CAGR 19-25F
Non-current assets	7,806.0	7,960.0	9,571.4	9,940.2	10,292.7	10,647.9	11,006.9	11,297.7	11,513.5	3.1%
Tangibles assets	5,193.0	5,333.0	5,508.9	5,693.9	5,853.6	6,016.7	6,180.4	6,288.2	6,324.5	2.3%
Rights of Use (IFRS 16)	0.0	1,282.0	1,245.8	1,215.5	1,192.0	1,175.8	1,166.4	1,155.7	1,144.0	-1.4%
Goodwill	84.0	85.0	85.0	85.0	85.0	85.0	85.0	85.0	85.0	0.0%
Intangible assets	407.0	547.0	666.0	736.7	806.6	876.9	947.1	1,006.1	1,053.5	7.9%
Investments in associates and joint ventures	1,483.0	1,295.0	1,424.0	1,553.0	1,682.0	1,811.0	1,940.0	2,069.0	2,198.0	7.5%
Deferred tax assets	350.0	369.0	369.0	369.0	369.0	369.0	369.0	369.0	369.0	0.0%
Other receivables	254.0	298.0	239.7	254.1	271.4	280.4	286.1	291.6	306.6	4.2%
Other financial assets	35.0	33.0	33.0	33.0	33.0	33.0	33.0	33.0	33.0	0.0%
Current assets	4,245.0	4,726.0	4,998.9	5,025.7	5,196.4	5,466.7	5,715.8	6,061.5	6,675.5	4.9%
Inventory	970.0	1,171.0	1,029.8	1,122.0	1,199.9	1,245.3	1,283.2	1,321.4	1,397.1	5.2%
Other financial investments	66.0	200.0	200.0	200.0	200.0	200.0	200.0	200.0	200.0	0.0%
Trade receivables	1,018.0	1,032.0	1,296.5	1,417.1	1,559.7	1,658.9	1,740.6	1,823.8	1,969.0	7.2%
Other receivables	535.0	640.0	595.8	631.5	674.5	697.0	710.9	724.8	761.9	4.2%
Other receivables - Sinopec	459.0	176.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0%
Cash and cash equivalents	1,197.0	1,508.0	1,876.8	1,655.1	1,562.3	1,665.5	1,781.0	1,991.5	2,347.4	3.8%
Assets	12,051.0	12,687.0	14,570.3	14,965.9	15,489.1	16,114.6	16,722.6	17,359.2	18,189.0	3.8%
Equity	5,779.0	6,047.0	6,287.0	6,380.2	6,615.9	6,967.0	7,315.3	7,696.0	8,211.9	4.6%
Share capital and share premium	911.0	911.0	911.0	911.0	911.0	911.0	911.0	911.0	911.0	0.0%
Reserves & Retained earnings	3,433.0	3,675.0	3,757.2	3,686.6	3,726.6	3,851.5	3,959.1	4,080.0	4,301.2	2.3%
Total equity attributable to shareholders	4,344.0	4,586.0	4,668.2	4,597.6	4,637.6	4,762.5	4,870.1	4,991.0	5,212.2	1.9%
Non-controlling interests	1,435.0	1,460.0	1,618.8	1,782.6	1,978.2	2,204.5	2,445.2	2,705.0	2,999.6	10.8%
Liabilities	6,272.0	6,640.0	8,283.3	8,585.7	8,873.3	9,147.6	9,407.3	9,663.2	9,977.1	3.1%
Non-current liabilities	3,842.0	4,006.0	5,529.4	5,658.7	5,741.0	5,863.4	5,986.2	6,093.4	6,174.3	1.9%
Debt	2,532.0	2,686.0	3,167.2	3,321.7	3,422.7	3,549.5	3,664.7	3,763.8	3,834.5	3.2%
Operating Leases (IFRS 16)	0.0	1,089.0	1,012.2	949.6	900.5	863.9	838.1	814.2	791.8	-4.0%
Other payables	286.0	126.0	126.0	126.0	126.0	126.0	126.0	126.0	126.0	0.0%
Post-employment liabilities	326.0	304.0	304.0	304.0	304.0	304.0	304.0	304.0	304.0	0.0%
Deferred tax liabilities	76.0	196.0	196.0	196.0	196.0	196.0	196.0	196.0	196.0	0.0%
Other financial instruments	3.0	37.0	37.0	37.0	37.0	37.0	37.0	37.0	37.0	0.0%
Provisions (including CESE)	619.0	658.0	687.0	724.3	754.8	787.0	820.4	852.4	884.9	4.3%
CESE	272.0	297.0	326.0	363.3	393.8	426.0	459.4	491.4	523.9	8.2%
Others	347.0	361.0	361.0	361.0	361.0	361.0	361.0	361.0	361.0	0.0%
Current liabilities	2,430.0	2,634.0	2,753.9	2,927.0	3,132.3	3,284.2	3,421.1	3,569.8	3,802.9	5.5%
Debt	551.0	559.0	622.4	693.0	771.7	859.2	956.7	1,065.2	1,186.1	11.3%
Operating Leases (IFRS 16)	0.0	113.0	108.9	101.2	95.0	90.0	86.4	83.8	81.4	-4.7%
Trade payables & Other payables	1,743.0	1,891.0	1,838.6	1,948.8	2,081.7	2,150.9	2,194.1	2,236.8	2,351.4	4.2%
Other financial instruments	21.0	102.0	102.0	102.0	102.0	102.0	102.0	102.0	102.0	0.0%
Current income tax payable	115.0	82.0	82.0	82.0	82.0	82.0	82.0	82.0	82.0	0.0%
Equity and Liabilities	12,051.0	12,687.0	14,570.3	14,965.9	15,489.1	16,114.6	16,722.6	17,359.2	18,189.0	3.8%

Balance sheet - Common-Size	2017	2018	2019E	2020F	2021F	2022F	2023F	2024F	2025F
Non-current assets	64.8%	62.7%	65.7%	66.4%	66.5%	66.1%	65.8%	65.1%	63.3%
Tangibles assets	43.1%	42.0%	37.8%	38.0%	37.8%	37.3%	37.0%	36.2%	34.8%
Rights of Use (IFRS 16)	0.0%	10.1%	8.6%	8.1%	7.7%	7.3%	7.0%	6.7%	6.3%
Goodwill	0.7%	0.7%	0.6%	0.6%	0.5%	0.5%	0.5%	0.5%	0.5%
Intangible assets	3.4%	4.3%	4.6%	4.9%	5.2%	5.4%	5.7%	5.8%	5.8%
Investments in associates and joint ventures	12.3%	10.2%	9.8%	10.4%	10.9%	11.2%	11.6%	11.9%	12.1%
Deferred tax assets	2.9%	2.9%	2.5%	2.5%	2.4%	2.3%	2.2%	2.1%	2.0%
Other receivables	2.1%	2.3%	1.6%	1.7%	1.8%	1.7%	1.7%	1.7%	1.7%
Other financial assets	0.3%	0.3%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Current assets	35.2%	37.3%	34.3%	33.6%	33.5%	33.9%	34.2%	34.9%	36.7%
Inventory	8.0%	9.2%	7.1%	7.5%	7.7%	7.7%	7.7%	7.6%	7.7%
Other financial investments	0.5%	1.6%	1.4%	1.3%	1.3%	1.2%	1.2%	1.2%	1.1%
Trade receivables	8.4%	8.1%	8.9%	9.5%	10.1%	10.3%	10.4%	10.5%	10.8%
Other receivables	4.4%	5.0%	4.1%	4.2%	4.4%	4.3%	4.3%	4.2%	4.2%
Other receivables - Sinopec	3.8%	1.4%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Cash and cash equivalents	9.9%	11.9%	12.9%	11.1%	10.1%	10.3%	10.7%	11.5%	12.9%
Assets	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
Equity	48.0%	47.7%	43.1%	42.6%	42.7%	43.2%	43.7%	44.3%	45.1%
Share capital and share premium	7.6%	7.2%	6.3%	6.1%	5.9%	5.7%	5.4%	5.2%	5.0%
Reserves & Retained earnings	28.5%	29.0%	25.8%	24.6%	24.1%	23.9%	23.7%	23.5%	23.6%
Total equity attributable to shareholders	36.0%	36.1%	32.0%	30.7%	29.9%	29.6%	29.1%	28.8%	28.7%
Non-controlling interests	11.9%	11.5%	11.1%	11.9%	12.8%	13.7%	14.6%	15.6%	16.5%
Liabilities	52.0%	52.3%	56.9%	57.4%	57.3%	56.8%	56.3%	55.7%	54.9%
Non-current liabilities	31.9%	31.6%	37.9%	37.8%	37.1%	36.4%	35.8%	35.1%	33.9%
Debt	21.0%	21.2%	21.7%	22.2%	22.1%	22.0%	21.9%	21.7%	21.1%
Operating Leases (IFRS 16)	0.0%	8.6%	6.9%	6.3%	5.8%	5.4%	5.0%	4.7%	4.4%
Other payables	2.4%	1.0%	0.9%	0.8%	0.8%	0.8%	0.8%	0.7%	0.7%
Post-employment liabilities	2.7%	2.4%	2.1%	2.0%	2.0%	1.9%	1.8%	1.8%	1.7%
Deferred tax liabilities	0.6%	1.5%	1.3%	1.3%	1.3%	1.2%	1.2%	1.1%	1.1%
Other financial instruments	0.0%	0.3%	0.3%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%
Provisions (including CESE)	5.1%	5.2%	4.7%	4.8%	4.9%	4.9%	4.9%	4.9%	4.9%
CESE	2.3%	2.3%	2.2%	2.4%	2.5%	2.6%	2.7%	2.8%	2.9%
Others	2.9%	2.8%	2.5%	2.4%	2.3%	2.2%	2.2%	2.1%	2.0%
Current liabilities	20.2%	20.8%	18.9%	19.6%	20.2%	20.4%	20.5%	20.6%	20.9%
Debt	4.6%	4.4%	4.3%	4.6%	5.0%	5.3%	5.7%	6.1%	6.5%
Operating Leases (IFRS 16)	0.0%	0.9%	0.7%	0.7%	0.6%	0.6%	0.5%	0.5%	0.4%
Trade payables & Other payables	14.5%	14.9%	12.6%	13.0%	13.4%	13.3%	13.1%	12.9%	12.9%
Other financial instruments	0.2%	0.8%	0.7%	0.7%	0.7%	0.6%	0.6%	0.6%	0.6%

Current income tax payable	1.0%	0.6%	0.6%	0.5%	0.5%	0.5%	0.5%	0.5%	0.5%
Equity and Liabilities	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Appendix 4: Cash-Flow Statement and Common-size (GALP)

Cash Flow Statement (mEUR)	2019E	2020F	2021F	2022F	2023F	2024F	2025F	CAGR 19-25F
OPERATING ACTIVITIES	1,392.1	1,468.9	1,733.4	1,969.5	2,066.6	2,181.6	2,361.7	9.2%
EBIT IFRS	1,767.1	1,717.9	2,113.2	2,407.3	2,581.4	2,774.4	3,152.9	10.1%
Non-Cash Charges	774.1	840.9	894.4	938.8	988.8	1,032.0	1,093.7	5.9%
Corporate Income Taxes and oil and gas production taxes	-903.9	-937.2	-1,126.3	-1,269.7	-1,407.7	-1,526.8	-1,726.4	11.4%
-DNWC	-245.2	-152.7	-147.9	-106.9	-96.0	-98.1	-158.5	-7.0%
INVESTMENT ACTIVITIES	-643.9	-934.7	-972.1	-1,020.7	-1,071.7	-1,050.3	-1,029.3	8.1%
CAPEX for tangible and intangible assets	-911.9	-1,029.0	-1,070.1	-1,123.6	-1,179.8	-1,156.2	-1,133.1	3.7%
CAPEX for Oper. Leases (IFRS 16)	92.0	94.3	98.1	103.0	108.1	106.0	103.8	2.0%
Other receivables - Sinopec	176.0	0.0	0.0	0.0	0.0	0.0	0.0	-
FINANCING ACTIVITIES	-379.5	-756.0	-854.1	-845.6	-879.3	-920.8	-976.6	17.1%
Financial Result	-82.1	-95.9	-101.6	-106.1	-111.5	-116.9	-122.2	6.8%
Dividends paid	-577.0	-634.6	-698.1	-733.0	-769.7	-808.2	-848.6	6.6%
Debt issuances/repayments	544.6	225.1	179.6	214.3	212.6	207.7	191.6	-16.0%
Interest relating to leasing	-92.2	-86.0	-80.6	-76.4	-73.2	-70.9	-68.9	-4.7%
Payments relating to leaseings (IFRS 16)	-172.9	-164.6	-153.4	-144.5	-137.6	-132.5	-128.6	-4.8%
Change in cash & cash equivalents	368.8	-221.7	-92.8	103.2	115.6	210.5	355.9	-0.6%
Beginning cash	1,508.0	1,876.8	1,655.1	1,562.3	1,665.5	1,781.0	1,991.5	4.7%
Ending cash	1,876.8	1,655.1	1,562.3	1,665.5	1,781.0	1,991.5	2,347.4	3.8%

Cash Flow Statement - Common-size	2019E	2020F	2021F	2022F	2023F	2024F	2025F
OPERATING ACTIVITIES	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
EBIT IFRS	126.9%	117.0%	121.9%	122.2%	124.9%	127.2%	133.5%
Non-Cash Charges	55.6%	57.2%	51.6%	47.7%	47.8%	47.3%	46.3%
Corporate Income Taxes and oil and gas production taxes	-64.9%	-63.8%	-65.0%	-64.5%	-68.1%	-70.0%	-73.1%
-DNWC	-17.6%	-10.4%	-8.5%	-5.4%	-4.6%	-4.5%	-6.7%
INVESTMENT ACTIVITIES	-46.3%	-63.6%	-56.1%	-51.8%	-51.9%	-48.1%	-43.6%
CAPEX for tangible and intangible assets	-65.5%	-70.0%	-61.7%	-57.1%	-57.1%	-53.0%	-48.0%
CAPEX for Oper. Leases (IFRS 16)	6.6%	6.4%	5.7%	5.2%	5.2%	4.9%	4.4%
Other receivables - Sinopec	12.6%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
FINANCING ACTIVITIES	-27.3%	-51.5%	-49.3%	-42.9%	-42.5%	-42.2%	-41.4%
Financial Result	-5.9%	-6.5%	-5.9%	-5.4%	-5.4%	-5.4%	-5.2%
Dividends paid	-41.4%	-43.2%	-40.3%	-37.2%	-37.2%	-37.0%	-35.9%
Debt issuances/repayments	39.1%	15.3%	10.4%	10.9%	10.3%	9.5%	8.1%
Interest relating to leasing	-6.6%	-5.9%	-4.6%	-3.9%	-3.5%	-3.3%	-2.9%
Payments relating to leaseings (IFRS 16)	-12.4%	-11.2%	-8.9%	-7.3%	-6.7%	-6.1%	-5.4%
Change in cash & cash equivalents	26.5%	-15.1%	-5.4%	5.2%	5.6%	9.6%	15.1%
Beginning cash	108.3%	127.8%	95.5%	79.3%	80.6%	81.6%	84.3%
Ending cash	134.8%	112.7%	90.1%	84.6%	86.2%	91.3%	99.4%

Appendix 5: Key Financial Ratios

Key Financial Ratios	2015	2016	2017	2018	2019F	2020F	2021F	2022F	2023F	2024F	2025F
Efficiency Ratios											
Fixed Assets Turnover (x)	1.97	1.70	2.12	2.01	1.81	1.85	1.91	1.90	1.87	1.86	1.92
Total Assets Turnover (x)	1.21	1.05	1.26	1.35	1.11	1.15	1.18	1.18	1.16	1.14	1.14
Receivables Turnover (x)	11.22	8.21	9.79	10.28	8.56	8.38	8.21	8.05	7.89	7.74	7.59
Collection Period (DSO) (days)	32.54	44.44	37.29	35.52	42.62	43.53	44.44	45.36	46.27	47.18	48.09
Inventory Turnover (x)	16.41	13.50	13.94	12.88	13.41	13.16	12.91	12.66	12.41	12.16	11.91
Days in Inventory (DIO) (days)	22.24	27.04	26.18	28.35	27.22	27.74	28.28	28.83	29.41	30.02	30.65
Payables Turnover (x)	9.55	6.76	7.76	7.97	7.51	7.58	7.44	7.33	7.26	7.18	7.08
Payables Period (DPO) (days)	38.21	54.01	47.04	45.78	48.60	48.18	49.05	49.80	50.29	50.82	51.58
Net Operating Cycle or Cash Cycle (days)	16.56	17.46	16.43	18.09	21.24	23.09	23.67	24.39	25.39	26.38	27.16
Operating Cycle	54.77	71.47	63.47	63.87	69.84	71.27	72.72	74.19	75.68	77.20	78.74
Solvency Ratios											
Long and short-term Debt Ratio (%)	27.77%	23.38%	25.58%	25.58%	26.01%	26.83%	27.08%	27.36%	27.64%	27.82%	27.60%
Long-term Debt Ratio (%)	23.91%	20.73%	21.01%	21.17%	21.74%	22.20%	22.10%	22.03%	21.91%	21.68%	21.08%
Debt to Equity Ratio (x)	0.74	0.58	0.71	0.71	0.81	0.87	0.90	0.93	0.95	0.97	0.96
Equity Multiplier (x)	2.07	1.90	2.09	2.10	2.32	2.35	2.34	2.31	2.29	2.26	2.21
Debt Ratio	0.52	0.47	0.52	0.52	0.57	0.57	0.57	0.57	0.56	0.56	0.55
Net Debt to EBITDA (x)	2.06	1.35	0.99	0.80	0.75	0.92	0.88	0.82	0.80	0.75	0.63
Interest Coverage Ratio (x)	8.83	16.39	79.64	124.83	10.14	9.45	11.60	13.19	13.98	14.77	16.50
Liquidity Ratios											
Current Ratio (x)	2.02	1.91	1.75	1.79	1.82	1.72	1.66	1.66	1.67	1.70	1.76
Quick Ratio (x)	1.24	1.22	1.13	1.21	1.37	1.27	1.21	1.22	1.24	1.27	1.34
Cash Ratio (x)	0.56	0.48	0.49	0.57	0.68	0.57	0.50	0.51	0.52	0.56	0.62
Profitability Ratios											
EBITDA Margin (%)	7.58%	10.57%	12.49%	12.69%	15.68%	14.90%	16.39%	17.65%	18.46%	19.31%	20.49%
EBIT Margin (%)	2.73%	4.12%	7.34%	8.72%	10.90%	10.00%	11.52%	12.70%	13.35%	14.07%	15.21%
Net Profit Margin (%)	1.44%	2.27%	3.93%	3.54%	4.07%	3.28%	4.02%	4.53%	4.54%	4.71%	5.16%
ROA (%)	1.74%	2.40%	4.96%	4.80%	4.52%	3.77%	4.77%	5.32%	5.25%	5.35%	5.88%
ROIC (%)	5.84%	5.25%	11.97%	12.89%	14.36%	13.22%	15.63%	17.12%	17.75%	18.60%	20.79%
NOPAT	288.6	368.3	759.0	1019.8	1203.0	1169.5	1438.6	1638.8	1757.3	1888.7	2146.4
Invested Capital	4939.0	7011.0	6339.0	7912.0	8375.7	8846.3	9205.3	9570.3	9901.5	153.7	323.7
ROCE (%)	3.94%	5.26%	11.59%	14.90%	14.95%	14.27%	17.10%	18.76%	19.41%	20.12%	21.92%
Capital Employed	10761.0	10281.0	9621.0	10053.0	11816.4	12038.9	12356.8	12830.4	13301.5	13789.3	14386.2
ROE (%)	4.67%	5.98%	13.77%	13.28%	14.12%	12.27%	15.92%	18.01%	18.01%	18.61%	20.53%
ROE (%) - DuPont Approach	4.67%	5.98%	13.77%	13.28%	14.12%	12.27%	15.92%	18.01%	18.01%	18.61%	20.53%
NI / S	1.44%	2.27%	3.93%	3.54%	4.07%	3.28%	4.02%	4.53%	4.54%	4.71%	5.16%
S / A	1.21	1.05	1.26	1.35	1.11	1.15	1.18	1.18	1.16	1.14	1.14
A / E	2.68	2.50	2.77	2.77	3.12	3.26	3.34	3.38	3.43	3.48	3.49
Value Creation and Cash Flow Ratios											
Economic Value Added (EVA) (M€)					599.0	530.0	774.5	948.3	1042.8	1156.1	1401.9
Debt Coverage (%)					17.39%	14.05%	17.60%	19.46%	18.98%	19.24%	21.31%
Cash to Income					0.79	0.86	0.82	0.82	0.80	0.79	0.75
Earnings Quality					0.91	1.05	1.06	1.12	1.14	1.14	1.08

Appendix 6: Income Statement Assumptions

Assumption	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F	Notes
Portuguese GDP growth	YoY	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	Data from European Comission.
Sales and service rendered	mEUR	Sum of segments							
Exploration & Production	mEUR	1,795.0	2,042.8	2,339.5	2,596.9	2,971.2	3,268.3	3,648.8	See Appedix 7.
Refining & Marketing	mEUR	11,768.9	12,411.4	13,279.4	13,295.8	13,260.1	13,340.0	13,974.9	See Appedix 8.
Gas & Power	mEUR	2,816.0	2,900.1	2,910.6	3,250.8	3,296.1	3,299.8	3,298.0	See Appedix 9.
Other	YoY	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	Not a business unit, it is expected to follow the economy. Grows at Portugal GDP growth.
Eliminations	% Sales	1.87%	1.87%	1.87%	1.87%	1.87%	1.87%	1.87%	Sales between segments are eliminated. Historical average.
Other operating income	YoY	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	1.70%	Company does not disclose much information about it, so we expect it to grow with the economy. Grows at Portugal's GDP.
Cost of sales & Production costs	mEUR	Sum of segments							
Exploration & Production	% Sales	18.95%	18.65%	18.08%	18.09%	17.56%	17.56%	17.31%	See Appedix 7.
Refining & Marketing	% Sales	93.84%	95.31%	94.31%	93.53%	94.30%	94.43%	93.95%	See Appedix 8.
Gas & Power	% Sales	95.09%	95.17%	95.13%	95.15%	95.14%	95.15%	95.14%	See Appedix 9.
Other	% Sales	80.8%	80.1%	80.4%	81.1%	80.9%	81.0%	81.2%	4Y Moving Average.
Eliminations	% Sales	1.88%	1.88%	1.88%	1.88%	1.88%	1.88%	1.88%	2Y Average over Sales.
RCA Effect	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	RCA adjustment was added back to treat the data based on IFRS standard. We forecast no change in this value since it is too difficult to do so without a high level of uncertainty.
EBITDA	mEUR	Sum of segments							
Exploration & Production	% Sales	81.1%	81.3%	81.9%	81.9%	82.4%	82.4%	82.7%	See Appedix 7.
Refining & Marketing	% Sales	6.2%	4.7%	5.7%	6.5%	5.7%	5.6%	6.1%	See Appedix 8.
Gas & Power	% Sales	4.9%	4.8%	4.9%	4.8%	4.9%	4.9%	4.9%	See Appedix 9.
Other	% Sales	19%	20%	20%	19%	19%	19%	19%	4Y Moving Average.
Eliminations	% Sales	4%	0%	-5%	-6%	-6%	-6%	-10%	2Y Average over Sales.
D&A, Provisions & Impairments	mEUR	Sum of segments							
Exploration & Production	mEUR	573.1	641.9	712.5	790.9	877.9	731.5	146.3	See Appendix 10 for detailed forecast
Refining & Marketing	mEUR	279.6	314.6	332.1	332.1	314.6	91.2	1,283.6	See Appendix 10 for detailed forecast
Gas & Power	mEUR	45.5	48.3	64.5	69.7	91.2	1,283.6	0.0	See Appendix 10 for detailed forecast
Other	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	No historical values.
Eliminations	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	No historical values.
Provisions	YoY	12%	12%	11%	11%	11%	10%	10%	Decommissioning/Environmental Matters Costs represent half of the value. With the increase in production/drills, it's expected to increase over time based on the increase in WIP. The Increase is based on the WIP CAGR
Net financial expenses	%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	2.5%	Average cost of financial debt reported in 2018. Will be multiplied by the debt from t-1.
Exchange gains/losses & derivatives	%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	No change YoY. Mostly related to Hedging Instruments, of which there's not enough data available to correctly predict its value
Operating leases interest (IFRS 16)	%	7.7%	7.7%	7.7%	7.7%	7.7%	7.7%	7.7%	% over Operating Leases Liabilities. Gathered from historical information
Results from financial investments	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	No change YoY. Mostly related to ventures connected to the operational segments, of which there's not enough data available to correctly predict its value
Income taxes	% EBT	31.5%	31.5%	31.5%	31.5%	31.5%	31.5%	31.5%	Both taxes were calculated through the historical data made available by the company in the income statement and the note regarding the effective tax rate
SPT&IRP	% EBIT	30.0%	30.0%	30.0%	30.0%	30.0%	30.0%	30.0%	
Energy sector extraordinary contribution (CESE)	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	2Y Moving Average. Related to the operations in the R&M and G&P.
Non-controlling interests	% EBIT	9.0%	9.5%	9.3%	9.4%	9.3%	9.4%	9.3%	2Y Moving Average over Operating result.
Dividends	YoY	10.0%	10.0%	10.0%	5.0%	5.0%	5.0%	5.0%	The company aims a dividend increase YoY of 10% until 2021, to which we deem sustainable, however from there on we assumed a 5,0% YoY growth, reaching EUR 1,02 in 2025, which represents a c.50% growth from 2018 values.

Appendix 7: Statement of Financial Position Assumptions

Assumption	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F	Notes
Non-current assets									
Tangibles assets	% of Assets	37.8%	38.0%	37.8%	37.3%	37.0%	36.2%	34.8%	Tangible assets t = Tangible t-1 + CAPEX (for tangible assets) t - D&A (for tangible assets) t. Appendix 10
Rights of use	% of Assets	8.6%	8.1%	7.7%	7.3%	7.0%	6.7%	6.3%	Rights of use t = Tangible t-1 + CAPEX (for op. leases) t - D&A (for op. leases) t. Appendix 10
Goodwill	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Goodwill is subject to Impairment Testing and assumed to remain constant over the period.
Intangible assets	% of Assets	4%	5%	5%	5%	5%	6%	6%	Intangible assets t = Intangible t-1 + CAPEX (for intangible assets) t - D&A (for intangible assets) t. Appendix 10
Investments in associates and joint ventures	%	8.6%	8.2%	8.9%	9.1%	9.4%	9.8%	10.3%	Value from t-1 + Result from financial investments / Most companies related to these joint ventures are related to E&P operations, which means that the value of these companies should increase as the sales increase over time, driven mostly due to increasing operations
Deferred tax assets	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Equal to the 2018 nominal value, offset effect with deferred tax liabilities
Other receivables	% Sales	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	1.5%	4y average of % over sales. Mainly from related to receivables from E&P partners
Other financial assets	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Hedging; keep same value. Too difficult to predict.
Current assets									
Inventory	Inventory Turnover	13.4	13.2	12.9	12.7	12.4	12.2	11.9	To do based on inventory days and inventory turnover, with the 2019E from a 2y average used. Will slightly decrease over time since there will be an increase in production.
Rights of use	%	0.10	0.10	0.10	0.10	0.10	0.10	0.10	Over Non-Current Rights of Use t-1
Other financial investments	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Hedging; keep same value. Too difficult to predict.
Trade receivables	% Sales	8.0%	8.3%	8.5%	8.8%	9.0%	9.3%	9.5%	Trade receivables have historically increased, thus we increased 0,25% every year.
Other receivables	% Sales	3.7%	3.7%	3.7%	3.7%	3.7%	3.7%	3.7%	4y average. Mainly from related to receivables from E&P partners
Loans to Sinopec	% Assets	100.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Ended in 2019
Non-current liabilities									
Debt	%	33%	33%	33%	33%	33%	33%	33%	Capital structure is expected to be the same, so a 2Y moving average is used to define the debt levels.
Other payables	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Value to be kept constant since there is not much information disclosed by the company.
Post-employment liabilities	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Assets are relatively stable through the years, with the same happening with the expected payments to the pension plan fund.
Deferred tax liabilities	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Equal to the 2018 nominal value and assumed to remain constant, as there is an offset effect with deferred tax assets.
Other financial instruments	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Hedging costs, we assume this value will be constant.
Provisions	mEUR	29.0	37.3	30.4	32.3	33.3	32.0	32.5	Provisions include decommissioning costs and CESE values. These are hard to predict, so a 3y moving average was used to obtain the contribution for CESE.
Current liabilities									
Debt	YoY	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	Expected to follow the increase registered in the Non-Current Liabilities. The increase will be higher as there will be non-current debt with maturity during the forecast horizon.
Trade payables & Other payables	% Sales	11%	11%	11%	11%	11%	11%	11%	Percentage obtained with a 4Y average from TP/Sales.
Other financial instruments	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	Hedging costs, we assume this value will be constant.
Current income tax payable	YoY	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	We assume this value will be constant, as estimation of uncertain tax positions might be too uncertain.
Payments relating to leasing	%	5.50%	5.50%	5.50%	5.50%	5.50%	5.50%	5.50%	Related to IFRS 16, based on historical values (only quarterly reports of 2019 are available).

Appendix 8: Sales & EBITDA breakdown for E&P

E&P key figures	Unit	2019E	2020F	2021F	2022F	2023F	2024F	2025F
Avg WIP	kboe/d	120.2	134.6	149.4	165.8	184.1	202.5	222.7
WI oil #	kboe/d	106	118	131	146	162	178	196
WI gas #	kboe/d	15	16	18	20	22	25	27
Oil Discount on Brent	%	80%	80%	80%	80%	80%	80%	80%
Gas Discount on Brent	%	30%	30%	30%	30%	30%	30%	30%
Brent price	USD/bbl	62	63	65	65	67	67	68
E&P Sales	mEUR	1795	2043	2340	2597	2971	3268	3649
Production costs	mEUR	192	215	239	266	295	325	358
Royalties	mEUR	148	166	184	204	226	249	274
EBITDA	mEUR	1455	1662	1916	2127	2450	2694	3017
EBITDA Margin	%	81%	81%	82%	82%	82%	82%	83%

E&P Assumptions	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F	Note
WIP	YoY	12%	12%	11%	11%	11%	10%	10%	GALP presented their expectations for the WIP growth: 12% CAGR from 2018 to 2019, 12-16% CAGR from 2018 to 2020, and a >10% CAGR up to 2030. For our forecast we projected the WIP close to the minimum value given, with a 10,8% CAGR.
Oil price	USD/bbl	62	63	65	65	67	67	68	Brent oil price forecast is extremely hard due to its volatility, so based on our research we decided to keep the price steadily increasing over time.
Oil ASP over Brent	%	80%							Computed based on information given by GALP
Gas ASP over Brent	%	30%							Computed based on information given by GALP.
USD/EUR	x€//\$	0.89							Foreign exchange forecast is extremely hard due to its volatility, so we decided to use an external source for FX (IMF)
Royalties	USD/bbl	3							Computed based on information given by GALP
E&P prod cost	USD/bbl	3.9	3.9025	3.905	3.9075	3.91	3.9125	3.915	We assume rather constant production costs due to economies of scale and several production units in plateau. Takes into account IFRS 16.

Sales from E&P

Sales from the E&P segment comes from the production that the company achieves (average WIP times 365 days) and the Brent price. It will also be influenced by the discount at which GALP sells their oil and gas production and that oil and gas will have in the WIP of the company. The production is expected to grow considerably for 2019-2025F, with a 10.8% CAGR. This increase in production will mainly come from the increase in the number of FPSOs in the Lula-Iracema projects, the new projects that will enter production in Brazil and Angola, and finally the start of the Coral FLNG project. This CAGR is way below the historical figure, but we decided to follow GALP's expectations. The Brent price forecast predicts a slow increase of the Brent price, achieving \$67/boe by 2023F. This expected increase in Brent Price will positively affect the company's sales. For the discount over Brent for oil and gas we follow the company lead of attributing 30% of Brent spot price for Gas, and, through comparisons with the historical ASP, 80% of the Brent Spot price for Oil. Finally, the production mix is expected to maintain the same weight for oil and gas since the increase in Gas is only expected to happen when the Coral South FLNG and Rovuma LNG start to operate at plateau. Overall, the sales are expected to significantly increase, yielding a 12% 2019-2025F CAGR.

EBITDA from E&P

For the E&P segment we will have two main operational costs: production costs and royalties. Productions are set at \$3.9/boe for 2019F, based on historical information. This value is expected to have a small upward trend, but it will still average 3.9\$ for 2019-2025F. This can be explained by the stable weight of production that will come from Brazil, therefore maintaining the small production costs that the company will incur. There could be a variation in the production costs based on the increase in projects that will come from outside the BM-S-11 block, but the increase in production in the BM-S-11 may lead to economies of scale and a slight decrease in costs in those projects. The royalties are also expected to be maintained around the historical value, standing at \$3.3/boe for 2019-2025F. The forecasted evolution of the operational costs will lead to a stable EBITDA Margin for the segment. Therefore, the increase in sales of the segment will lead to stable increase in segment's EBITDA.

Appendix 9: Sales & EBITDA breakdown for R&M

R&M	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F
Used Capacity	%	80%	90%	95%	95%	90%	90%	95%
Raw material processed	kboe	96,360.0	108,405.0	114,427.5	114,427.5	108,405.0	108,405.0	114,427.5
ASP	USD/boe	70.2	71.3	73.6	73.6	75.8	75.8	77.0
Brent	USD/boe	62.0	63.0	65.0	65.0	67.0	67.0	68.0
Refining Cost	USD/boe	3.7	2.8	2.4	2.4	2.8	2.8	2.4
Refining Margin	USD/boe	4.5	5.5	6.2	6.2	6.0	6.0	6.6
Refining ASP (Eur/boe)	EUR/boe	62.5	63.5	65.5	65.5	67.5	67.5	68.5
Refining Sales	mEUR	6,019.2	6,880.8	7,493.7	7,493.7	7,317.7	7,317.7	7,839.5
Refining Cost (Eur/Boe)	EUR/boe	58.5	58.6	60.0	60.0	62.2	62.2	62.7
Refining Cost	mEUR	5,632.7	6,352.3	6,866.1	6,866.1	6,738.2	6,738.2	7,171.6
Refining EBITDA	mEUR	386.5	528.6	627.6	627.6	579.5	579.5	667.9
Total oil products	mton	17.1	17.4	17.7	18.0	18.3	18.6	18.9
Marketing ASP	EUR/mton	336.5	318.3	327.4	322.8	325.1	324.0	324.6
Marketing Cost	EUR/mton	316.7	315.2	320.1	309.9	315.5	315.2	315.2
Marketing Sales	mEUR	5,749.7	5,530.5	5,785.7	5,802.1	5,942.4	6,022.3	6,135.4
Marketing Cost	mEUR	5,411.7	5,476.7	5,657.1	5,568.9	5,766.2	5,858.3	5,957.8
Marketing EBITDA	mEUR	338.0	53.8	128.6	233.2	176.3	163.9	177.6
Sales	mEUR	11,768.9	12,411.4	13,279.4	13,295.8	13,260.1	13,340.0	13,974.9
Total cost	mEUR	11,044.4	11,829.0	12,523.2	12,435.0	12,504.4	12,596.5	13,129.4
EBITDA	mEUR	724.5	582.4	756.2	860.8	755.8	743.4	845.5

R&M Assumptions	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F	Note
Used Capacity	%	80%	90%	95%	95%	90%	90%	95%	Percentage of the installed capacity that is used in the refinery. After the maintenance operations, we expected the company to recover to historical maximum, which is above 90%.
Refining Margin	USD/bbl	4.51	5.48	6.16	6.16	6.01	6.01	6.56	Amount of USD/bbl GALP realizes on each barrel of oil that is refined. Similar to usage capacity, after the maintenance operations, we expect the refining margin to recover.
Refining Cost	USD/bbl	3.68	2.84	2.42	2.42	2.84	2.84	2.42	Cost to refine 1 barrel of oil. Expected to decrease due to an increase in efficiency (maintenance operations).
Refining ASP	USD/bbl	70.19	71.32	73.58	73.58	75.85	75.85	76.98	Average selling price of the by-products from the refining of one barrel of oil.
Total Oil Sales (Quantity)	mton	17.09	17.38	17.67	17.97	18.28	18.59	18.90	Amount of oil by-products sold by the Marketing BU. The growth will follow the Portugal GDP YoY.
Marketing ASP	USD/mton	336.52	318.29	327.40	322.84	325.12	323.98	324.55	Average selling price of by-products. 2Y moving average.
Marketing Costs	USD/mton	316.74	315.19	320.13	309.87	315.48	315.17	315.16	Operational costs. 4Y moving average.

Sales from Refining

The sales from the Refining Business Unit are accessed through the multiplication of the Average Selling Price per kboe and the amount of Raw Material Processed (kboe) from the Refining system of the company. The quantity of Raw Material Processed will come from the multiplication of the Used Capacity with the installed Refining Capacity (a constant 330 kboe/d or 120450 kboe per annum).

The Average Selling Price was obtained as function of the Brent Price, with the value throughout the forecast being the 4Y historical average of the ASP over Brent times the value of the Brent for each period. With an expected increase in the Brent Price in the forecast horizon, the ASP will consequently register. The Used Capacity of the Refining system is expected to register a slight decline in 2019E because of maintenance operations. Afterwards, we predict an increase based on historical values and operational improvements from the maintenance operations.

EBITDA from Refining

In the Refining BU the main benchmark of the operational efficiency will be the Refining Margin. The Refining Margin will come from the difference between the value obtained through the sales of the refined products and the operational costs (Brent price plus the production costs). The production costs will be dependent of the efficiency of the refineries and the economies of scale that will come from higher degrees of Used Capacity. In our forecast the production costs are expected to decrease when compared with historical values, as a result of the increase in efficiency. As stated previously, the Brent price is expected to increase over the years. The result of the decrease in production costs, the increase in Brent price and ASP will yield an average \$5.8/boe Refining Margin. Consequently, the EBITDA of this BU will increase throughout the years, reaching a maximum value in 2025F where we have a \$67/boe Brent price and a 95% Used Capacity.

Sales from Marketing

The sales from the Marketing BU will come from the multiplication of the Total Sales of Oil Products (mton) and the Average Selling Price per mton. The historical ASP for the BU was obtained as the division of the sales from the BU (difference between R&M sales and the Refining BU Sales) with the Total Sales oil products. The Average Selling Price was obtained as a 2Y moving average. The Total Sales of Oil Products are predicted to grow along the lines of the growth of the GDP of Portugal (GALP's main market), as a growth in the demand of energy is associated with the growth of the economy. This will lead to an increase in sales throughout the years, reaching the maximum value in 2025F.

EBITDA from Marketing

The operational costs from the BU where achieved through a 4Y moving average. This can be justified by the fact that the company is the current market leader in Portugal and will therefore be able to maintain their current level of costs. Over the 2019-2025F the EBITDA Margin will have an average value of 3.1%, 1% increase over the 4Y historical average.

Appendix 10: Sales & EBITDA breakdown for G&P

G&P	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F
Sales	M€	2,816.0	2,900.1	2,910.6	3,250.8	3,296.1	3,299.8	3,298.0
Cost of sales & Production costs	M€	2,677.7	2,760.2	2,768.8	3,093.2	3,136.0	3,139.6	3,137.8
RCA Ebitda	M€	138.3	140.0	141.7	157.6	160.1	160.1	160.1
Supply & Trading	M€	92.2	93.0	93.9	108.8	109.8	110.8	111.8
Power	M€	46.2	46.9	47.9	48.8	50.4	52.0	53.6

G&P Assumptions	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F	Note
Gas Demand CAGR	%	1.8	1.8	1.8	1.8	1.8	1.8	1.8	European comission
Trading Increase	%	0.0	0.0	0.0	30.0	0.0	0.0	0.0	From GALP's financial statements. Contract that will provide 1 mta of NG from 2022 onward, for trading only.
Electricity Demand CAGR	%	1.4	1.4	1.4	1.4	1.4	1.4	1.4	European comission
Electricity sold to grid	%	2.0	2.0	2.5	2.5	5.0	5.0	5.0	Electricity sold to the grid is expected to rise due to increases in CAPEX, as GALP is focused in increasing low-carbon solutions in its portfolio. This decision is one more step into the energy transition.

Sales from G&P

The sales from the G&P segment where calculated through as a function of the EBITDA of the segment. They will come from the sum of the EBITDA from the Supply & Trade BU and the Power BU. As the EBITDA Margin of the segment was forecasted as a 2Y Moving Average, it will present a relatively stable value throughout the years. With the expected increase of the EBITDA between 2019-2025F, it's expected that the segment sales will increase over the years.

EBITDA from Supply & Trade

The Supply and Trade BU EBITDA for each YE is retrieved as a function of the previous year value, the increase in NG demand in Portugal and the expected growth of the trading activity. The increase in the demand of the NG in the Iberian Peninsula can be applied to the company since the company presents a stable market share of 12%. The increase in trading activity is considered to be zero over the years, with the exception of 2022F where the LNG contract will increase significantly the trading activity of GALP.

EBITDA from Power

For the Power BU EBITDA of each YE, the value is achieved as a function of the value from the previous year, the growth in energy demand in Portugal and the growth in electricity sold to the grid. The growth in energy demand in Portugal is expected to be followed by the company since the company can easily follow it by increasing the amount of electricity bought from the grid and sold to end clients. The growth in electricity sold to the grid is expected to grow over the years at different rates since it will mainly be explained by the increase in CAPEX of the segment, since this CAPEX will be mainly applied to renewable energy generation facilities.

Appendix 11: GALP's CAPEX & DD&A

CAPEX (with IFRS 16, M€)	2018	2019E	2020F	2021F	2022F	2023F	2024F	2025F	CAGR 19-25F
Exploration and Production	404.4	453.4	558.2	575.7	655.5	682.9	669.3	655.9	6.35%
Exploration and Appraisal	215.7	182.4	140.2	145.8	153.1	160.8	157.5	154.4	-2.74%
Total E&P (includes leasing)	620.0	635.8	698.4	721.5	808.6	843.7	826.8	810.3	4.12%
R&M (includes leasing)	260.6	349.8	311.8	324.3	289.5	304.0	297.9	291.9	-2.97%
G&P	9.0	18.2	18.7	24.3	25.5	32.2	31.5	30.9	9.17%
Total	889.6	1,003.9	1,029.0	1,070.1	1,123.6	1,179.8	1,156.2	1,133.1	2.04%

CAPEX Assumptions	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F	Note
CAPEX growth	YoY	2.5%	2.5%	4.0%	5.0%	5.0%	-2.0%	-2.0%	We assume that CAPEX evolves YoY, following the data given by the company.
CAPEX (without Operating Leases)	M€	911.9	934.7	972.1	1,020.7	1,071.7	1,050.3	1,029.3	Value in M€. Previous year CAPEX times (1+growth).
E&P Prod	%	43.0%	53.0%	52.5%	57.5%	57.0%	57.0%	57.0%	% of total CAPEX. Calculated based on historical values and expected investments.
E&P Appraisal	%	20.0%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%	% of total CAPEX. Calculated based on historical values and expected investments.
Exploration & Production	%	63.0%	68.0%	67.5%	72.5%	72.0%	72.0%	72.0%	% of total CAPEX. Calculated based on historical values and expected investments.
Refining & Marketing	%	35.0%	30.0%	30.0%	25.0%	25.0%	25.0%	25.0%	% of total CAPEX. Calculated based on historical values and expected investments.
Gas & Power	%	2.0%	2.0%	2.5%	2.5%	3.0%	3.0%	3.0%	% of total CAPEX. Calculated based on historical values and expected investments.
CAPEX linked to operating leases	%				10.1%				% CAPEX w/o Operating leases.
Total	M€	92.0	94.3	98.1	103.0	108.1	106.0	103.8	Value in M€.
Exploration & Production	%	67%	67%	67%	67%	67%	67%	67%	2/3 of total based on historical weights of the leases of each segment.
Refining & Marketing	%	33%	33%	33%	33%	33%	33%	33%	1/3 of total based on historical weights of the leases of each segment.

Taking into account the historical investment and the company's targets for CAPEX, we see an increase for all segments, all for different reasons, always above € 1bn, even reaching almost 1,2 in 2023F. E&P CAPEX is the most demanding, as it is divided in sub-sectors: Production and Appraisal; this is linked to increases in production (e.g. more production units) and in continuous efforts to make viable production in current non-producing blocks or further increase their portfolio through acquisition of concessions in bidding rounds. R&M segment will have a significant decrease in their CAPEX since most of its historical CAPEX comes from maintenance operations that happened between 2017 and 2019, with no further operations expected to happen throughout the forecast horizon.

D&A (with IFRS 16, M€)	2018	2019E	2020F	2021F	2022F	2023F	2024F	2025F	CAGR 19-25F
Exploration and Production	289.4	402.3	430.6	460.1	493.5	531.3	569.9	612.3	7.25%
Exploration and Appraisal	57.9	63.4	69.5	75.8	82.8	90.6	98.4	107.1	9.13%
Total E&P (includes leasing)	347.3	465.7	500.1	535.9	576.4	621.9	668.3	719.3	7.52%
R&M (includes leasing)	337.2	235.5	258.3	269.4	268.6	256.0	255.7	267.4	2.14%
G&P	5.3	44.0	45.1	58.6	61.6	77.6	76.0	74.5	9.17%
Other	4.0	4.0	4.0	4.0	4.0	4.0	4.0	4.0	0.00%
Total	689.8	749.1	807.6	867.9	910.5	959.5	1,004.0	1,065.2	6.04%

D&A Assumptions	Unit	2019F	2020F	2021F	2022F	2023F	2024F	2025F	Note
D&A	mEUR	620.9	683.0	746.4	791.3	841.9	887.4	949.6	
EP Total	%	61.2%	61.1%	60.9%	62.8%	64.6%	66.6%	67.6%	Based on historical values, and adapted to capture the UoP method that is applied to some of the assets
EP Prod	%	51.0%	50.9%	50.8%	52.3%	53.8%	55.5%	56.4%	84% of total E&P, based on 4Y average
EP Appraisal	%	10.2%	10.2%	10.2%	10.5%	10.8%	11.1%	11.3%	16% of total E&P, based on 4Y average
Refining & Marketing	%	31.0%	31.7%	30.7%	28.9%	25.8%	24.4%	24.1%	Based on historical values, and adapted to capture the UoP method that is applied to some of the assets
Gas & Power	%	7.1%	6.6%	7.9%	7.8%	9.2%	8.6%	7.8%	Based on the 2Y historical average of D&A/CAPEX
Other	%	0.6%	0.6%	0.5%	0.5%	0.5%	0.5%	0.4%	Fixed value, based on historical figures
D&A for Operating Leases	%				10.0%				% D&A w/o Operating leases
Total	mEUR	128.2	124.6	121.6	119.2	117.6	116.6	115.6	Value in €m
E&P	%	67%	67%	67%	67%	67%	67%	67%	2/3 of total based on historical weights of the leases of each segment
R&M	%	33%	33%	33%	33%	33%	33%	33%	1/3 of total based on historical weights of the leases of each segment

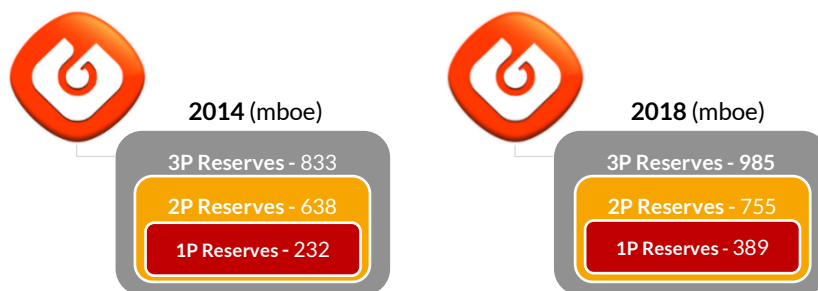
D&A rates for each segment are obtained via historical percentages, but differently for all segments, as some also consider production. For the latter one, our calculations focus in capturing the existing straight-line D&A and also the one linked to UoP.

Appendix 12: GALP's Reserves

Resources and reserves are key for Oil and Gas companies operating in the E&P as they constitute one of the drivers of profitability for the segment. This way, it is important to understand the difference between the two, considering that only the latter are in fact considered assets and incorporated in the companies' balance sheet.

Resources are classified as being contingent or prospective. The latter include quantities of oil and NG that companies estimate to recover from unknown deposits of their future projects. Contingent resources are those quantities estimated from known deposits that are not yet considered as commercially recoverable.

Reserves constitute the quantities of oil and NG expected to be commercially recoverable from known deposits. According to the probability of being recovered, reserves are classified as 1P (Proved Reserves), 2P (Proved and Probable) and 3P (Proved, Probable and Possible). Oil and Gas companies' total amount of reserves will correspond to the volume of their 3P reserves, which are the quantities with an associated probability of at least 10%. Then, 2P reserves will include those with an above 50% probability of being recovered. Finally, 1P reserves will correspond to 90% probability.



GALP's level of reserves has been increasing, mostly explained by the company's presence in projects with high levels of production, such as the ones in Block BM-S-11, in Brazil.

Appendix 13: WACC Assumptions

Four WACC rates were computed. One for each of the company's sectors – E&P, R&M and G&P – and one for the company as a whole. These rates differ as risk free rate, leveraged beta and the Market Risk Premium change to account for country and industry specific realities. WACC rates will change YOY reflecting small changes in GALP's capital structure. We considered the company's target capital structure to be composed of 80% equity and 20% debt.

Cost of Equity

In order to compute the cost of equity we used the CAPM model ($CAPM = R_e = RFR + \beta * MRP$).

GALP		
Risk Free Rate (RFR)	1.10%	10Y Government Bond yields for Germany as of 7th of January 2020. See point 1.
Country Risk Premium	1.50%	CRP (over German risk-free rate) for Portugal. See point 2.
Beta (β)	0.92	Monthly adjusted levered Betas for GALP's (as a whole) peers, which were unlevered considering each peers capital structure and effective tax rate. An average of those unlevered betas was, then, leveraged using GALP's 2019 capital structure. See point 4.
Market Risk Premium (MRP)	6.30%	Excess Market Premium for Portugal. See point 3.
Terminal Growth Rate (g)	2.00%	Appendix 14

Exploration and Production		
Risk Free Rate (RFR)	1.10%	10Y Government Bond yields for Germany as of 7th of January 2020. See point 1.
Country Risk Premium	6.10%	CRP (over German risk-free rate) for Brazil. See point 2.
Beta (β)	0.73	Monthly adjusted levered Betas for GALP's E&P peers, which were unlevered considering each peers capital structure and effective tax rate. An average of those unlevered betas was, then, leveraged using GALP's 2019 capital structure. See point 4.
Market Risk Premium (MRP)	4.50%	Excess Market Premium for Brazil. See point 3.
Terminal Growth Rate (g)	2.50%	Appendix 14

Refining and Marketing		
Risk Free Rate (RFR)	1.10%	10Y Government Bond yields for Germany as of 7th of January 2020. See point 1.
Country Risk Premium	1.50%	CRP (over German risk-free rate) for Portugal. See point 2.
Beta (β)	0.66	Monthly adjusted levered Betas for GALP's R&M peers, which were unlevered considering each peers capital structure and effective tax rate. An average of those unlevered betas was, then, leveraged using GALP's 2019 capital structure. See point 4.
Market Risk Premium (MRP)	6.30%	Excess Market Premium for Portugal (Fernandez). See point 3.
Terminal Growth Rate (g)	2.00%	Appendix 14

Gas and Power		
Risk Free Rate (RFR)	1.10%	10Y Government Bond yields for Germany as of 7th of January 2020. See point 1.
Country Risk Premium	1.50%	CRP (over German risk-free rate) for Portugal. See point 2.
Beta (β)	0.42	Monthly adjusted levered Betas for GALP's G&P peers, which were unlevered considering each peers capital structure and effective tax rate. An average of those unlevered betas was, then, leveraged using GALP's 2019 capital structure. See point 4.
Market Risk Premium (MRP)	6.30%	Excess Market Premium for Portugal. See point 3.
Terminal Growth Rate (g)	2.00%	Appendix 14

1. As the benchmark for the **risk-free rate (RFR)** we used the normalized 10Y German Bond Yield, as of 7th January 2020.
2. A **country risk premium (CRP)** was added to the risk-free rate in order to account for each country's specific risks. CRP was computed as the difference from Portugal's (or Brazil's) RFR and the German RFR. These rates were retrieved from "Market Risk Premium and Risk-Free Rate used for 69 countries in 2019: a survey" (Fernandez)
3. **Market risk premium (MRP)** is lower for Brazil than for Portugal, reflecting the higher RFR in this country.
4. We decided to compute **Betas** for the company as a whole, as well as for each of the company segments. This way, and using the pure-play method, we were able to better estimate the risk associated to each segment and region. The levered betas of GALP peers presented are the average of 2015-2019 adjusted betas, with monthly data.

	D/E (market values)	Tax Rate
Galp Energia SGPS SA	0.25	31.5%

GALP (as a whole)	Levered Beta	D/E	Unlevered Beta
Repsol SA	1.01	0.38	0.83
OMV AG	1.05	0.51	0.81
Eni SpA	0.73	0.51	0.61
Equinor ASA	1.36	0.60	1.10
MOL Magyar Olajes Gazipari Nyrt	1.16	0.35	0.88
Gazprom Neft' PAO	0.64	0.44	0.47
Total SA	0.94	0.45	0.73
	Weighted Average		0.77
GALP	0.90		

E&P	Levered Beta	D/E	Unlevered Beta
GeoPark Ltd	0.55	3.13	0.22
Enauta Participações SA	0.92	0.09	0.86
Petroleo Brasileiro SA Petrobras	1.36	1.18	0.79
Petro Rio SA	1.86	0.28	1.51
	Weighted Average		0.84
GALP	0.99		

R&M	Levered Beta	D/E	Unlevered Beta
Neste Oyj	0.84	0.66	0.54
Rubis SCA	0.57	0.25	0.48
DCC PLC	0.86	0.74	0.53
Polski Koncern Naftowy Orlen SA	1.35	0.28	1.10
	Weighted Average		0.66
GALP	0.77		

G&P	Levered Beta	D/E	Unlevered Beta
Ren Redes Energeticas Nacionais SGPS SA	0.74	1.83	0.32
EDP Energias de Portugal SA	0.94	1.84	0.35
Endesa SA	0.58	0.67	0.38
Iberdrola SA	0.58	1.03	0.32
Naturgy Energy Group SA	0.72	1.52	0.33
	Weighted Average		0.34
GALP	0.40		

Cost of Debt

Cost of Debt will be the same for all three segments of GALP as the company finances itself in Portugal.

$$\text{Cost of Debt} = \text{RFR} + \text{CRP} + \text{Spread (AAA)}$$

We used the 10-year normalized 10Y German Bond Yield (1.1%) as a proxy for the RFR and added a CRP (1.5%) to account for Portugal specific realities and risks. Finally, we added a spread of 75b.p., reaching a pre-tax cost of debt of 3.35%. Adjusting for taxes, GALP's cost of debt is 2.30%.

GALP is not rated by rating agencies. So, in order to reach the spread over the RFR we estimated a synthetic rating for the company. With a market capitalization over 12 billion euros and an interest coverage ratio of 9.45x, GALP has a synthetic rating AAA correspondent to a spread of 75b.p.

Appendix 14: Terminal Growth Rate

E&P Stable Growth Model		R&M Stable Growth Model		G&P Stable Growth Model		GALP Stable Growth Model	
CAPEX	4,709.40	CAPEX	1,614.98	CAPEX	163.05	CAPEX	6,487.43
D&A	3,621.96	D&A	1,575.37	D&A	393.31	D&A	5,590.64
Changes NWC	109.50	Changes NWC	526.21	Changes NWC	124.34	Changes NWC	760.05
EBIT	10,244.35	EBIT	2,968.69	EBIT	526.42	EBIT	13,739.46
Tax Rate	31.5%	Tax Rate	31.5%	Tax Rate	31.5%	Tax Rate	31.5%
Reinvestment Rate	17.1%	Reinvestment Rate	27.8%	Reinvestment Rate	-29.4%	Reinvestment Rate	17.6%
ROE	14.1%	ROE	14.1%	ROE	14.1%	ROE	14.1%
g	2.4%	g	3.9%	g	-4.1%	g	2.5%

In the terminal period we assumed a going concern approach with cash flows growing perpetually at a continuous rate. We followed two approaches to reach the Terminal Growth Rate – Stable Growth Model and Dividend Sustainable Growth. The first one may be applied for each segment individually, while the latter can only be applied to the company as a whole. For the Stable Growth Model, we used the sum of values of 2019-2025F, except for the value for the ROE which was computed as the average between 2015-2025F. In the Dividend Sustainable Growth Model, the values used came from 2015-2025F. In the case of the Stable Growth Model the only value that was immediately rejected came from the G&P. The E&P value was considered too low if we consider the potential growth of the segment, the R&M we considered that it was overly estimated. The value of the GALP as whole was deemed unfit, as it was too high. Thus, we applied the forecasted GDP growth on the R&M and G&P segments based on the strong relationship between the demand of the segments and the GDP growth. For the E&P we applied a premium based on the potential for growth of the segment. In the company as a whole, we based our choice in the values that the segments presented individually.

Dividend Sustainable Growth		Terminal Growth Rate	
Net Income	9,262.98	E&P	2.8%
Dividends	6,777.10	R&M	1.7%
Sales	191,479.89	G&P	1.7%
Total Assets	163,380.75	GALP	2.0%
Shareholder's Equity	52,421.24		
(NI-D)/NI	26.8%		
ROE	17.7%		
NI/S	4.8%		
S/A	117.2%		
A/E	311.7%		
g	4.7%		

Appendix 15: FCF Valuation

Regarding the FCF model, several adjustments were carried out for the transition from Enterprise Value to Equity Value. The adjustments were carried out in order to consider non-operational assets and financial liabilities. Other financial assets were added and Other Financial Instruments were subtracted. The Post-Employment Fund of the company is presented as a liability and will therefore be subtracted. The Provisions (mostly connected to Decommissioning costs and CESE) were subtracted, as they will negatively affect the company's value if they were effectively incurred. Lastly, Non-controlling interests were subtracted.

FCFF Valuation SOTP		WACC				
E&P	10 506	Risk Free Rate (RFR)	1.10%	1.10%	1.10%	1.10%
R&M	3 022	Country Risk Premium (CRP)	1.50%	6.10%	1.50%	1.50%
G&P	1 924	Beta (β)	0.90	0.99	0.77	0.40
Enterprise Value	15 451	Market Risk Premium (MRP)	6.50%	4.50%	6.50%	6.50%
Mozambique	867	Cost of Equity	8.47%	11.66%	7.64%	5.23%
Net Debt	-3 695	Cost of Debt	3.35%	3.35%	3.35%	3.35%
Other financial assets	200	Effective Tax Rate	31.50%	31.50%	31.50%	31.50%
Other financial instruments	-102	After-tax Cost of Debt	2.30%	2.30%	2.30%	2.30%
Post-employment liabilities	-304					
Provisions (including CESE)	-724					
Non-controlling interests	-1 688					
Adjustments	-5 447					
Equity Value	10 004					
Shares Outstanding	829					
Price Target	12,06 €					

GALP (whole)

	2020E	2021F	2022F	2023F	2024F	2025F	Terminal Value
Weight of equity (Market Values)	79.93%	79.15%	79.20%	79.27%	79.17%	78.99%	80.00%
Weight of debt (Market Values)	20.07%	20.85%	20.80%	20.73%	20.83%	21.01%	20.00%
WACC	7.23%	7.21%	7.22%	7.22%	7.22%	7.21%	7.23%

Exploration & Production

	2020E	2021F	2022F	2023F	2024F	2025F	Terminal Value
Weight of equity (Market Values)	79.93%	79.15%	79.20%	79.27%	79.17%	78.99%	80.00%
Weight of debt (Market Values)	20.07%	20.85%	20.80%	20.73%	20.83%	21.01%	20.00%
WACC	9.78%	9.73%	9.73%	9.74%	9.73%	9.72%	9.82%

Refining & Marketing

	2020E	2021F	2022F	2023F	2024F	2025F	Terminal Value
Weight of equity (Market Values)	79.93%	79.15%	79.20%	79.27%	79.17%	78.99%	80.00%
Weight of debt (Market Values)	20.07%	20.85%	20.80%	20.73%	20.83%	21.01%	20.00%
WACC	6.56%	6.55%	6.55%	6.55%	6.55%	6.55%	6.51%

Gas & Power

	2020E	2021F	2022F	2023F	2024F	2025F	Terminal Value
Weight of equity (Market Values)	79.93%	79.15%	79.20%	79.27%	79.17%	78.99%	80.00%
Weight of debt (Market Values)	20.07%	20.85%	20.80%	20.73%	20.83%	21.01%	20.00%
WACC	4.63%	4.64%	4.63%	4.63%	4.63%	4.63%	4.63%

Exploration & Production	2020F	2021F	2022F	2023F	2024F	2025F	Terminal Value
EBIT	1 162	1 380	1 551	1 828	2 026	2 298	2 606
Tax Rate	31,50%	31,50%	31,50%	31,50%	31,50%	31,50%	31,50%
SPT&IRP	30,00%	30,00%	30,00%	30,00%	30,00%	30,00%	30,00%
ESEC	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Unlevered Net Income	557,0	661,9	743,6	876,4	971,5	1 101,8	1 249,6
Non Cash Charges and Other Adjustments	500,1	535,9	576,4	621,9	668,3	719,3	774,2
D&A, Provisions & Impairments	500,1	535,9	576,4	621,9	668,3	719,3	774,2
Changes in Net Working Capital	-18,0	-18,7	-14,5	-14,6	-16,1	-27,6	-17,6
Capital Expenditures	-698,4	-721,5	-808,6	-843,7	-826,8	-810,3	-774,2
Free Cash Flow to the Firm (FCFF)	340,7	457,7	496,8	640,0	796,8	983,2	1 232,0
PV of FCFF	2 481,5	2 723,0	2 485,8	2 182,7	1 692,9	983,2	
PV of Terminal Value	10 959,1	12 025,5	13 196,1	14 481,2	15 890,5	17 435,3	
Enterprise Value	13 440,7	g = 2.75%					

Refining & Marketing	2020F	2021F	2022F	2023F	2024F	2025F	Terminal Value
EBIT	324,0	486,8	592,2	499,8	487,7	578,1	
Tax Rate	31,5%	31,5%	31,5%	31,5%	31,5%	31,5%	
ESEC	-52,5	-53,1	-52,0	-51,9	-51,9	-52,4	
Unlevered Net Income	169,5	280,3	353,7	290,5	282,2	343,6	
Non Cash Charges and Other Adjustments	258,3	269,4	268,6	256,0	255,7	267,4	
D&A, Provisions & Impairments	258,3	269,4	268,6	256,0	255,7	267,4	
Negative Changes in Net Working Capital	-109,2	-106,0	-74,2	-65,2	-65,7	-105,9	
Capital Expenditures	-280,4	-291,6	-255,2	-267,9	-262,6	-257,3	
Free Cash Flow to the Firm (FCFF)	38,2	152,1	292,8	213,4	209,6	247,8	252,0
PV of FCFF	920,1	980,4	882,6	628,4	442,2	247,8	
PV of Terminal Value	3 811,5	4 061,2	4 327,2	4 610,8	4 912,9	5 234,6	
Enterprise Value	4 731,6	g = 1.70%					

Gas & Power	2020F	2021F	2022F	2023F	2024F	2025F	Terminal Value
EBIT	94,9	83,1	96,0	82,6	84,1	85,7	
Tax Rate	31,5%	31,5%	31,5%	31,5%	31,5%	31,5%	
ESEC	-12,2	-11,4	-12,4	-12,7	-12,6	-12,1	
Unlevered Net Income	52,8	45,6	53,4	43,9	45,0	46,6	
Non Cash Charges and Other Adjustments	45,1	58,6	61,6	77,6	76,0	74,5	
D&A, Provisions & Impairments	45,1	58,6	61,6	77,6	76,0	74,5	
Changes in Net Working Capital	-25,5	-23,2	-18,2	-16,2	-16,3	-25,0	
Capital Expenditures	-18,7	-24,3	-25,5	-32,2	-31,5	-30,9	
Free Cash Flow to the Firm (FCFF)	53,7	56,6	71,3	73,1	73,3	65,2	66,3
PV of FCFF	296,2	309,9	265,0	202,7	135,6	65,2	
PV of Terminal Value	1 797,8	1 881,0	1 968,2	2 059,4	2 154,8	2 254,5	
Enterprise Value	2 093,9	g =1.70%					

Appendix 16: FCFE Valuation

The Equity Value in the FCFE was adjusted to discount the non-controlling interests. The net borrowings were equal to the changes in debt in the forecasted year, with adjustments being made in the terminal period. In that period, net borrowings correspond to the amount invested in net CAPEX and NWC that will be financed through debt to maintain the capital structure as 20% D/EV:

$$Net\ Borrowings_{Terminal} = \frac{D}{EV} \times (CAPEX - D\&A + \Delta NWC)$$

FCFE	2020F	2021F	2022F	2023F	2024F	2025F	Terminal Value
Net income to common shareholders	564.1	738.1	857.9	877.2	929.0	1,069.8	1,091.2
Tax Rate	31.5%	31.5%	31.5%	31.5%	31.5%	31.5%	
Non Cash Charges and Other Adjustments	803.6	863.9	906.5	955.5	1,000.0	1,061.2	1,082.4
Target D/EV	20.0%	20.0%	20.0%	20.0%	20.0%	20.0%	0.2
Capital Expenditures	-997.5	-1,037.4	-1,089.3	-1,143.8	-1,120.9	-1,098.5	-1,120.5
Negative Changes in Net Working Capital	-152.7	-147.9	-106.9	-96.0	-98.1	-158.5	-183.5
Net Borrowing (target D/EV approach)	69.3	64.3	57.9	56.9	43.8	39.2	44.3
Free Cash Flow to Equity (FCFE)	286.8	480.9	626.2	649.8	753.9	913.2	914.0
PV of FCFE	2,634.5	2,858.7	2,580.1	2,120.1	1,595.4	913.2	
PV of Terminal Value	11,118.9	12,065.2	13,091.7	14,205.0	15,413.7	16,726.8	
Equity Value	13,753.5	g = 3.0%					

Price per share	
Equity Value	13,940.9
Shares Outstanding	829.3
Price per share	16.8

Appendix 17: Dividend Discount Model (DDM)

Regarding the DDM, we applied a two-stage model together with a H-model for the terminal period. In the H-model we considered a short-term growth rate of 8% that reflects the converging dividend growth YoY from 2020F to 2025F. This rate will gradually decrease until it reaches a constant value of 3% in the terminal period from 2029 onwards, which corresponds to the perpetual growth rate for the FCFE. Despite the growing dividends, payout ratio will average 71.4% in the period 2020-2025.

DDM Price Target	
Dividend 2025	848.6
H	4
Long-term Growth	3.0%
Short-term Growth	8.0%
Terminal Cost of Equity	8.5%
PV Dividends	3,015.4
PV Terminal Value	11,664.9
Equity Value	14,680.3
Shares outstanding	829.3
Equity Value per share	17.70

	2020F	2021F	2022F	2023F	2024F	2025F
EPS	0.68	0.89	1.03	1.06	1.12	1.29
YoY	-14.4%	30.8%	16.2%	2.2%	5.9%	15.2%
DPS	0.77	0.84	0.88	0.93	0.97	1.02
YoY	10.0%	10.0%	5.0%	5.0%	5.0%	5.0%

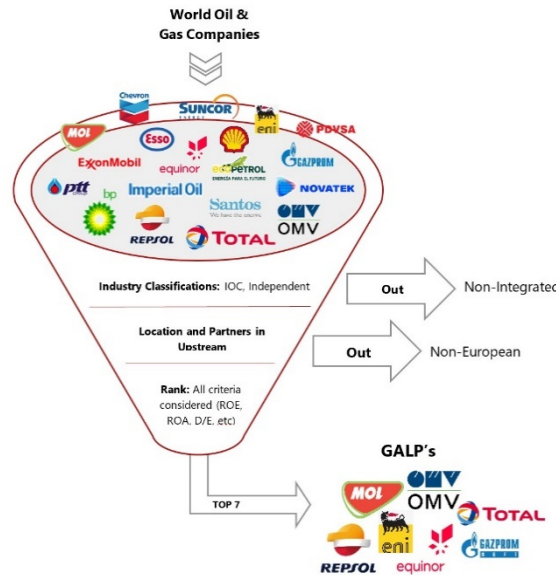
Appendix 18: Mozambique LNG

Rovuma is currently seen as one of the most promising gas discoveries in the world. Gas has a 10% stake in the project, working together with their partners in the development it. This benchmark project will play a decisive role into GALP's goal of moving into a low carbon strategy.

To properly capture the potential of Rovuma project, we decided to value GALP's stake separately based on recent transactions. There are two transactions we deemed considerable: one from Exxon and one from TOTAL. Exxon acquired a 25% stake in Mozambique's Area 4 (Rovuma LNG and South Coral FLNG) for \$2.8bn. When adjusting for the exchange rate of the period, the acquisition will be valued in €0.6bn per mta. The Total transaction occurred in 2019, with the acquisition of a 26.5% stake in Area 1 (Mozambique LNG) being valued in \$3.9bn. When doing the same adjustment that was previously done to the Exxon transaction, we will achieve a €1.0bn per mta. We then applied an average of the valuation and multiplied it by the GALP's stake in the Rovuma LNG project (1.5 mta). This will return us a value of €1.5/share. We applied an uncertainty factor of 30% over this valuation, since E&P projects always have a certain degree of uncertainty over their economic value. This valuation yielded an additional € 0.90 to the price target.

Appendix 19: Peers

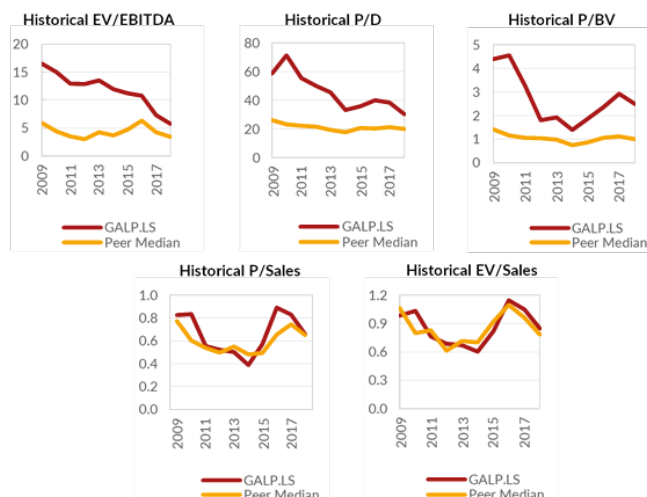
To perform a valuation with multiples, the definition of a peer group is required to more accurately benchmark the relative measures selected. The information related to the peers was taken from Thomson Reuters. The first approach considered was to find peers for each GALP's segment, Upstream and Downstream. For the Upstream, the most appropriate players would be E&P firms from Africa and LATAM, and for the Downstream, European R&M companies. However, due to the lack of comparable companies for the E&P, this approach proved to be ineffective. Since GALP is an IOC with a global presence, we decided to follow another approach where only IOCs were the possible choice for the peer group. Additionally, we narrowed the possible companies by region, only considering European companies or companies operating with GALP in its Upstream projects, either in LATAM or Africa. From the companies we reached with this selection, we eliminated those with extremely higher or lower market capitalization, sales, and assets. As the number of possible companies was still considerably high and in order to reach the peer group as close as possible to GALP's values, a ranking was constructed for a number of financial drivers chosen by our team, including Return on Equity, Return on Assets, EBITDA Margin, Net Debt to EBITDA, etc. The final peer group is represented in the figure below.



Source: Team Analysis

Appendix 20: Valuation through Multiples

The multiples applied were computed for 2020F. GALP's values were based on team estimates whereas peer multiples were extracted from Reuters' Forecast Multiples. Our team chose to first analyze several GALP's historical multiples to compare with the peers and this way understand GALP's position. GALP is trading at a premium when comparing to its peers mainly because it still has capacity to grow. What we can gather from the evolution of the ratios is that the market seems to be reviewing GALP's growth potential since its ratios are getting closer to the values of the other companies. This may be because the potential of growth of the company is getting smaller, as the company as considerably increased their WIP levels. Nonetheless, the market still seems to be evaluating GALP with a premium over their peers.



Appendix 21: Other information regarding Oil and Gas industry

We should begin by differentiating between an Operationally IOC and a Financially IOC. The first is a company operating in all segments of the Oil & Gas industry and supplying its Downstream with its Upstream production whereas the second, even operating in all segments, the Upstream and Downstream function independently, with oil from the E&P being sold to the open market and the oil for refining also bought from the open market.

Upstream segment | Upstream investments occur several years prior to the beginning of production. Consequently, projects undergo several steps until reaching the production phase. The exploration stage initiates when companies acquire the right to explore the areas through a concession deal granted by the country's government. Exploration is focused on studying the structure of the earth in depth, the geological history of the area and to measure the probability of hydrocarbon occurrence. If the studies confirm economic viability of an oil field, then the first well is drilled, known as "wildcat" well. The Development stage precedes the Production and it is relevant as resources start being accounted as reserves. Finally, Production phase starts as the first marketable hydrocarbons come to the surface. First, the projects go through a ramp-up period. After a given interval of time, which will differ depending on the projects, they reach plateau, meaning they will be producing at full capacity, and then they enter in decline.



Specifically, GALP's Upstream portfolio comprises around 50 projects, in 6 different locations (Brazil, Angola, Mozambique, Namibia, S. Tomé and Príncipe and East Timor) and in distinct stages of exploration, development, and production.

GALP's Locations	Nb Blocks	In Exploration	In Development	In Production
Brazil	16	11	2	3
Angola	3	-	-	3
Mozambique	1	-	1	-
Namibia	2	2	-	-
S. Tomé and Príncipe	4	4	-	-
East Timor	1	1	-	-
Total	27	18	3	6

In E&P Brazil, and due to the finding of high potential exploration areas, a new regime was established, meaning that currently 3 types of contracts apply to the pre-salt area. 2 examples are the Concession Contract (CC) and the Production Sharing Contract (PSA). The latter, also the most recently established and only applicable to the pre-salt polygon, occurs when exploration of oil and NG is made through a sharing contract between Petrobras (NOC) and a company or group of companies. The consortium must pay royalties to the government. The obligation of Petrobras acting as the operator and hold a minimum stake of 30% is no longer mandatory, though the company is still given preference. In the concession model, the company or companies within the consortium operate in an area granted by the State. Royalties along with Special Participation taxes must be paid. Special Participation only apply to the projects with high levels of production.

It is relevant to mention that the concession model applies to the projects within the areas contracted prior the establishment of the PSA defined to the pre-salt. In both regimes CNPE decides whether Petrobras is directly hired or if bidding rounds will take place. The participation of external companies is only recently permitted in Brazil. Companies authorized to participate in the auctions will try to get a stake in bidding rounds, where Petrobras continues to be given preference as operator. Companies offering the largest profit to the Brazilian State are the ones winning.

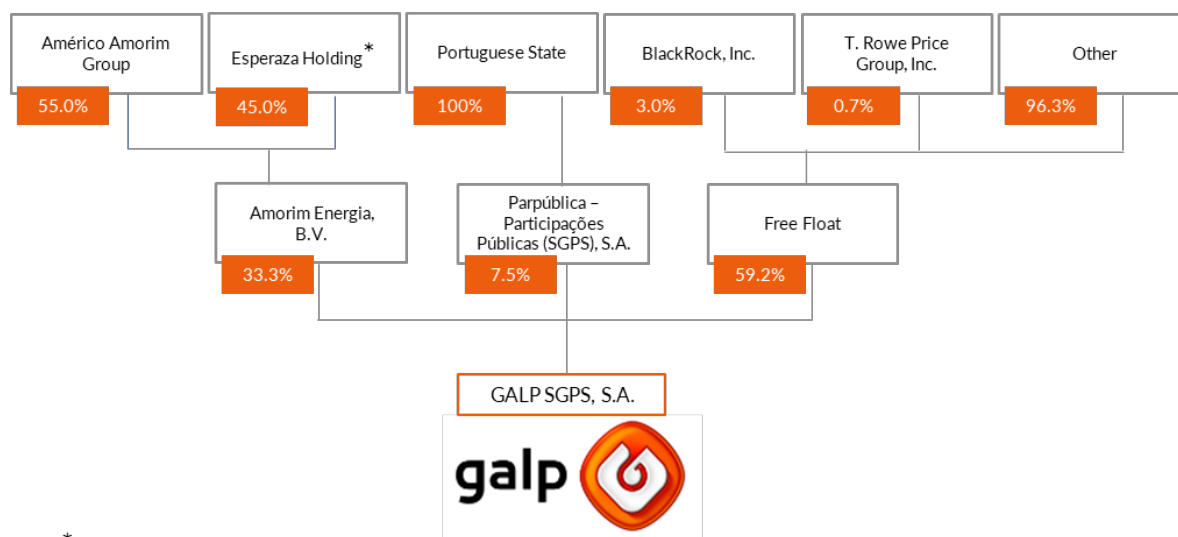
Midstream segment | Refers to the processing, transportation and storage of crude oil and NG. Reserves usually are not in the same geographical location as refineries and final consumers. As so, transportation is the main activity and includes using pipelines, rail cars, tanker ships and trucking fleets. Galp does not operate in this segment, since it is a financially IOC.

Downstream segment | R&M: A variety of products reach consumers in the marketing phase of this segment. Gasoline, gasoil, heating oil, asphalt, jet fuel, kerosene, NG, LPG, as well as many petrochemicals, are some examples. The major consumers of downstream products are airlines, trucking fleets, utilities and petrochemicals, municipalities, and industrial manufacturers. The companies involved in this segment consist mostly of refineries, natural gas and petroleum distributors, and retail outlets. A key factor that determine the success or failure in this industry is related to how companies can reduce the costs associated with the resource's purchase and refining process, in order to increase their refining margins.

The refining process is a global, extremely cyclical and margin business, where profitability is very sensitive to marginal changes in oil products supply and demand. The main measure of profitability is the margin, defined as the difference between the price realized for the products to be sold and the cost of the crude delivered to the refinery. Margins tend to diminish when crude prices increase and tend to hold or grow when crude prices drop, because the marketplace adjusts more slowly to lower crude prices than to higher ones. Margins tend to be similar for refineries that operate in the same region and market.

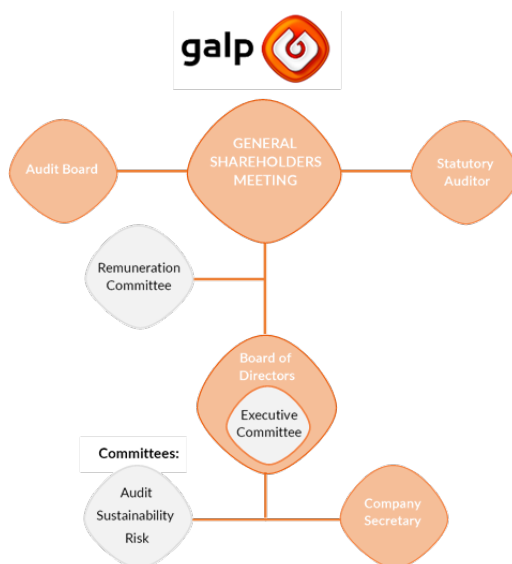
Even though Galp does not possess any refinery in Spain, it still has an extensive distribution network of oil products there. The company currently has a total of 1,460 service stations, maintaining its leadership position in the retail market in Portugal, where it has 710 service stations and 340 convenience stores, out of a total of about 3,000. It is also a relevant player in Spain, since it has over 570 service stations and 380 convenience stores, of a total of around 8,856.

Appendix 22: Shareholder Structure



* Held by Sonangol and Isabel dos Santos

Appendix 23: Governance Model



Appendix 24: Remuneration Policy

As of 31/12/2018

Director	Age	Independent	Position	Compensation (2018)	Term
Paula Amorim	48	No	Chairman	- €	2018
Miguel Athayde Marques	64	Yes	Vice-Chairman and LID	84 000,00 €	2018
Carlos Gomes da Silva	52	No	Vice-Chairman	1 755 769,00 €	2018
Filipe Crisóstomo Silva	55	No	Member	705 000,00 €	2018
Thore E. Kristiansen	58	No	Member	920 387,00 €	2018
Sérgio Gabrielli de Azevedo	70	No	Member	84 000,00 €	2018
Abdul Magid Osman	75	Yes	Member	84 000,00 €	2018
Marta Amorim	47	No	Member	42 000,00 €	2018
Raquel Vunge	53	No	Member	42 000,00 €	2018
Carlos Costa Pina	49	No	Member	705 000,00 €	2018
Francisco Teixeira Rêgo	47	No	Member	42 000,00 €	2018
Jorge Seabra de Freitas	59	No	Member	42 000,00 €	2018
José Carlos Silva	57	No	Member	887 082,00 €	2018
Pedro Ricardo	55	No	Member	693 083,00 €	2018
Tiago Câmara Pestana	55	No	Member	693 083,00 €	2018
Rui Paulo Gonçalves	52	No	Member	42 000,00 €	2018
Luís Todo Bom	71	Yes	Member	42 000,00 €	2018
Diogo Tavares	74	No	Member	42 000,00 €	2018
Joaquim Borges Gouveia	70	Yes	Member	42 000,00 €	2018
Total				6 947 404,00 €	

The BoD presented above is the one effective until December 31st, 2018. Since it has changed in 2019 and no information has yet been released regarding the remuneration of the new BoD, we decided to present the remunerations of 2018. Below, we present the current constitution of the BoD.

As of 31/12/2018

Director	Age	Independent	Position	Term
Paula Amorim	48	No	Chairman	2022
Miguel Athayde Marques	64	Yes	Vice-Chairman and LID	2022
Carlos Gomes da Silva	52	No	Vice-Chairman	2022
Filipe Crisóstomo Silva	55	No	Member	2022
Thore E. Kristiansen	58	No	Member	2022
Carlos Costa Pina	49	No	Member	2022
José Carlos Silva	57	No	Member	2022
Sofia Tenreiro	44	No	Member	2022
Susana Quintana	45	No	Member	2022
Marta Amorim	47	No	Member	2022
Francisco Teixeira Rêgo	47	No	Member	2022
Carlos Pinto	41	No	Member	2022
Luis Todo Bom	71	Yes	Member	2022
Jorge Seabra de Freitas	59	No	Member	2022
Diogo Tavares	74	No	Member	2022
Rui Paulo Gonçalves	52	No	Member	2022
Edmar de Almeida	50	Yes	Member	2022
Cristina Neves Fonseca	31	Yes	Member	2022
Adolfo Mesquita Nunes	42	Yes	Member	2022

		Fixed		
Remuneration	Variable (potential maximum of 60% based on the total annual fixed remuneration)	Annual (50%)	Quantitative Performance (65%)	GALP Value Added (33.3%)
				Total Shareholder Return (TSR) (33.3%)
				EBITDA RC (33.3%)
		3-years (50%)	Qualitative Performance (35%)	Collective performance assessment, including environmental, sustainability and energy efficiency
			Quantitative Performance (65%)	Total Shareholder Return (TSR) (50%)
				EBITDA RC (50%)
Qualitative Performance (35%)	Collective performance assessment, including environmental, sustainability and energy efficiency			

Appendix 25: Awards

Throughout the years, GALP has been recognized for its good practices. Below, we present GALP's acknowledgments and awards for 2019 with a brief explanation for each.

Ethibel EXCELLENCE / AAA Rating, by MSCI ESG Ratings / "Prime" Company, by ISS ESG / Top 3 of World's Most Sustainable Companies / "Gold" Company, by EcoVadis / Bloomberg's 2019 Gender-Equality Index / Silver Class Sustainability Yearbook Award 2019

Appendix 26: Risk Matrix

Interest Rates (MR4)

Debt is entirely in EUR, making the company exposed to ECB's monetary policies. Low-interest rates have been beneficial to the company; however, these are expected to eventually increase after 2019. Additionally, most of the debt is raised in Portugal, leaving the company financials also exposed to the Portuguese economy. Historically, the company's average interest rate spread over the long-term government bond yield has been 65 b.p.

Political Stability (PRL2)

Most of the company's Upstream projects are in countries with relevant political and economic risk. Civil disruption, expropriation and nationalization of goods or significant increases in taxes and royalties could all arise from this risk, mostly in Brazil, Angola and, eventually, in Mozambique.

Fuel Taxation (PRL3)

In Portugal, taxes account for c.52% and 43% of the price of gasoline and diesel, respectively. GALP's ability of adaptation to oil price changes is heavily affected by governmental decisions. If these taxes become even more burdensome to the company, it can become an issue for the R&M segment.

CESE – Extraordinary Contribution for the Energy Sector (PRL4)

Following the law and tax regulations, GALP is properly accounted for the legal obligation from CESE, although this obligation is currently subject to legal dispute. The company is accurately provisioned for this and, in a scenario where a payment will be necessary, it should not be a problem in the short run. The decision is in the hands of the Constitutional Court.

Amorim Energia (GR1)

Amorim Energia B.V. position in the shareholder structure (c.33%) gives it a high influence on all shareholders matters (e.g. the ability to block major changes in the company). Although this shareholder has other positive examples where they are the largest holder (like Corticeira Amorim), it is important to understand that their influence is high within GALP, and should they wish to exert that, they are able to. For example, one of the changes that need a qualified majority is the acquisition of the company, and GALP's current structure greatly decreases its desirability as a target, working as a pre-takeover defense mechanism.

Dividend Policy Maintenance (FR1)

The maintenance of a stable dividend policy is part of GALP's strategy. Despite the stability on its core business, in an unexpected event that might lower the cash-flow generation, sustaining the dividends can be difficult. This might be a sensitive topic due to the clientele effect, since some shareholders would not happily accept a dividend decrease or stoppage. Yet, the DPS is expected to remain stable in the period 2019F-2023F.

Natural Disasters (ER1)

Upstream operations are developed in extremely fragile environments (ultra-deep waters), where there is an exposure to the risk of natural disasters. A natural disaster in the Lula-Iracema FPSOs would be disruptive to the operations of GALP, heavily affecting its value creation capacity. It is also important to account for the possibility of environmental damage due to operational failures (e.g. oil spill), that can heavily damage the company's reputation and generate costs associated with damage control.

Appendix 27: Porter's Five Forces

-Rivalry Among Existing Competitors

Upstream | Low (2)

In this segment, competitors are also partners. This is because most exploration activities operate through production share agreement (PSA) deals. In these, different companies share blocks with different percentages of control, depending on the results of the auction for that specific project. Usually, National Oil Companies (NOC) are the ones awarded with the right of preference to control the blocks. All other players have to go through bidding rounds to gain the interest still available. Brazil's NOC, Petrobras, is the main player of E&P in the country, with c.74% 2018YE of the total oil production. GALP is the 3rd biggest producer in Brazil with c.3% of production, right after Shell with c.13%. As so, companies are both competitors in the auctions, as they are partners in the blocks where they have shares. For these reasons, rivalry among competitors is considered to be low in the Upstream.

Downstream | Significant (4)

There are 11,860 stations (including service stations and convenience stores) in Portugal and Spain operating in the Marketing segment. GALP has 17% of these. As so, the high number of Downstream competitors turn the rivalry quite significant. Moreover, the homogeneity of the products leads to an increase in competition since companies have the need to differentiate themselves from similar ones.

-Threat of Substitute Products

Upstream | Insignificant (1)

With the energy transition, renewable energies and NG will increase its share in the energy mix, with NG becoming the 2nd most used source of energy. These can become substitute products for oil. Nonetheless, oil demand will keep increasing in the following years and so is its E&P. For this reason, and as GALP is already producing electricity and NG in the Upstream, intending to increase production in the following years, accompanying the market trends, this force does not represent a threat for GALP.

Downstream | Low (2)

The same logic is also applied to the Downstream segment, because of the demand of by-products. However, as GALP is already present in the refining and marketing of NG and electricity, the threat of substitute products is low.

-Bargaining Power of Customers

Upstream | Insignificant (1)

Consumers are also suppliers. The customers of the Upstream are the downstream players. As so, these do not have almost any bargaining power over the price at which they will buy it.

Downstream | Insignificant (1)

In the downstream, consumers have small influence on the price since they are highly dependent on the products.

-Bargaining Power of Suppliers

Upstream | Moderate (3)

Governments own reserves inside borders, so they have power over exploration rights of their reserves. Frequently, these countries will treat favorably their NOCs, giving them preferred rights and more advantageous conditions in the bidding rounds. Otherwise, political issues may well arise. For this reason, suppliers have some control over which upstream companies get stakes in the blocks.

Downstream | Significant (4)

GALP buys oil in the market for its refining process. As so, it is exposed to the supplier's influence on the prices. However, as GALP also operates in the Upstream segment and it sells the oil produced in the open market, so it has an influence over prices as a supplier. This creates a natural hedge since the company sells and buys oil in the market, allowing it to adjust the prices in the Upstream segment.

-Threat of New Entrants

Upstream | Moderate (1)

New entrants are highly unlikely in the Upstream segment. This is mostly due to the high capital investments required to acquire the basic assets for the E&P. Recently, GALP paid over 106 million euros for a 20% stake for the C-M-791 block located in the Campos Basin in an auction realized in 2018. They already operate in the industry and can afford uncertainty around E&P projects because the current portfolio is sustainable and profitable. However, new players don't have the knowledge to invest in projects that have high uncertainty associated.

Downstream | Significant (3)

The low costs associated with opening and operating a service station or convenience store make the threat of new entrants much higher than in the Upstream segment. On the other hand, costs needed to build and run a refinery are substantially higher, what lowers the probability of new entrants. Overall, this force represents a significant threat for GALP.

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