

2017 ANNUAL
AND CORPORATE
RESPONSABILITY REPORT

RISK MAP

PERIOD 2018 - 2022



CEPSA

Cepsa Group has developed an Integrated Risk Management System (IRMS) in order to respond effectively to any potential risk event which may significantly affect the Group.

The Integrated risk management provides an identification and treatment of the main risks across the company, defining a strategy, at the level of the business unit, corporate unit, and common risk unit, with an overview on an aligned and consistent basis at Cepsa Group.

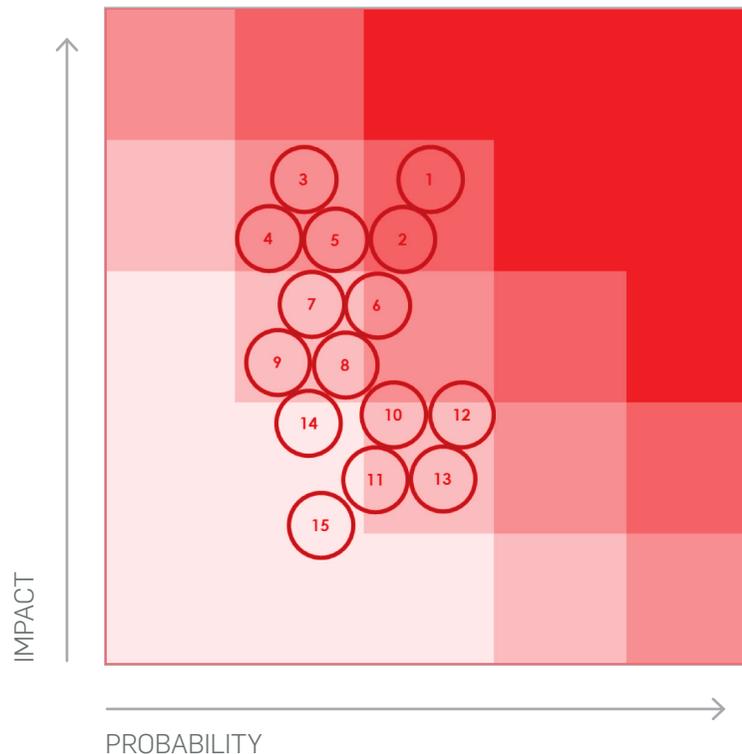
Cepsa's commitment to implementing the IRMS is reflected in the approval by the Group's Board of Directors in 2017 of a General Risk Policy which defines Cepsa Group's appetite for risk. The basic principles of the Policy are defined in the Basic Standard for Integrated Risk Management.

The management model is inspired by the international standard ISO 31000, by the methodology defined by the Committee of Sponsoring Organizations of the Treadway Commission for

enterprise risk management (COSO-ERM) and in the Three Lines Defence model.

In this context, the CEPESA GROUP strategic and budgetary planning process has estimated the impact of the potential risks in the businesses and has performed a sensitivity analysis of the main variables, in order to gain a comprehensive view of their impact.

1. Refining margin
2. Regulatory uncertainty and Compliance
3. Operational safety
4. Physical security
5. Information security
6. Large projects management
7. Production and replacement of reserves
8. Geopolitical risk
9. Local communities
10. Commodity pricing
11. Exchange rate
12. Market competition
13. Demand evolution
14. Talent management
15. Credit risk



MAXIMISATION OF VALUE

- ① ⑥ ⑦ ⑩ ⑪ ⑮

GROWTH

- ① ⑥ ⑦ ⑧ ⑩ ⑫ ⑬ ⑭

LEADERSHIP

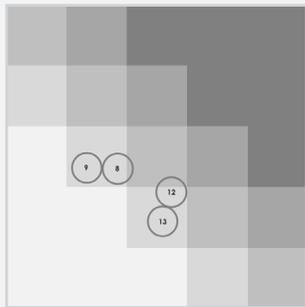
- ③ ④ ⑤ ⑨ ⑫ ⑬ ⑭

ROBUSTNESS

- ① ⑦ ⑩ ⑪ ⑫ ⑬ ⑮

STRATEGIC & PLANNING RISKS

Related to environmental factors where Cepsa Group operates, such as political, economic, socio-cultural and technological factors.



- 8. Geopolitical risk
- 9. Relationships with local communities
- 12. Market competition
- 13. Demand evolution

CONTEXT/ EXTERNAL THREATS

- The improved global economic outlook has come hand-in-hand with permanent significant risks round the central arena, which include recent increased global geopolitical tension, in addition to the uncertainty surrounding the United Kingdom's exit from the EU and economic policy in some advanced economies, which is particularly relevant in the field of the United States tax policy.
- In the current economic context where Cepsa produces and markets its products, one highlight is the favourable outlook for the Spanish economy in the medium term. The outlook is also positive for Brazil, Colombia and Peru. On the other hand, China is forecast to grow moderately after the 6.8 percent leap of 2017 and will sit at around 6.4 percent growth in 2018, according to World Bank estimates.
- Strong competition due to pressure from the markets with greatest productive advantages (access to cheaper crude oil, fewer regulatory restrictions, etc.).
- The role of renewables in the energy mix will continue to increase. It is estimated that by 2030, renewable energies will account for more than 60% of Spanish electricity demand in order to meet the global targets in this respect.

RISK

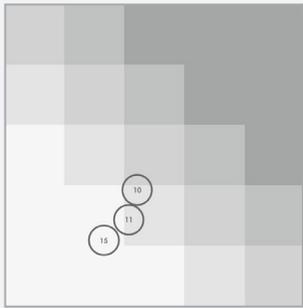
- Financial crises, political instability and social disturbance affecting operations, nationalisation or public expropriation of assets, monetary restrictions and other restrictions on the movement of capital or changes in the regulations and administrative policies of the country; these are just some examples of the geopolitical risk which CEPSA faces in performing its international activity.
- Changes in demand and market competition over time.
- Relationships with local communities.

MANAGEMENT ACTIONS

- With a view to proactively managing this risk, CEPSA monitors all countries in which it has operations, following the trend of some key **indicators** defined for a series of categories of identified sources of risk, which include: security, **political stability, effective governments, legal and regulatory environment, fiscal and macroeconomic policy.**
- **Diversification** of the portfolio of exploration and production projects: to mitigate our exposure to geopolitical risk, Cepsa strives for balance in its project portfolio by expanding its activities to different countries.
- The quest for excellence in customer service, constant monitoring of trends in an ever-more dynamic and changing market or continuous improvement as one of the main values of the Group are some of CEPSA's levers to address these risks.
- Maintaining responsible and transparent relations with the communities in which CEPSA is present is a key and integral part of our activities and operations, enabling value to be generated for society and collaborating in its economic, social and environmental development, through integration in the environment and implementing community projects.
- Creation of the Cepsa Foundation in 2016 as an example of the CEPSA Group's commitment to the host communities and locations where CEPSA performs its activity.
- In 2016, Cepsa created Voluntar, a specific corporate volunteer programme focused on caring for the environment, fostering employment and education, supporting culture, promoting sport and health and addressing basic needs.

FINANCIAL AND MARKET RISK

Derived from the volatility of commodity prices, of exchange rates, of interest rates and of hedging and trading transactions, and those relating to liquidity and solvency management, credit risk and counterparty risk management.



- 10. Commodity pricing
- 11. Exchange rate risk
- 15. Credit risk

CONTEXT/ EXTERNAL THREATS

- Positive perspectives regarding the **price of crude oil** in 2018 following the extension, at the end of November, of the agreement on production cuts by **OPEC** member countries until 2018, in an attempt by the group to end excess supply and avoid further price decline.
- Cepsa activities are generally **sensitive** to the **change in the exchange rate** of the **euro** versus the **US dollar**, the currency in which the majority of crude and petroleum and petrochemical products are priced. Thus, the recent exchange rate volatility represents a source of uncertainty which needs to be monitored in terms of potential implications for the medium term perspectives on price stability.
- In the financial arena, we cannot overlook the **current environment** which, characterised by **abundant liquidity** at low costs and very low levels of volatility in the main capital markets, may lead to abrupt adjustments in the value of some assets, with an adverse impact on the financing conditions of the agents.

RISK

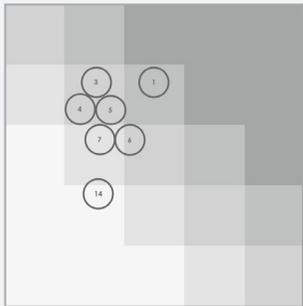
- Price risk of raw materials (commodities) due to the volatility of oil and gas prices.
- Liquidity risk, exchange rate risk and interest rate risk derived from the behaviour of financial markets.
- Credit and counterparty risk.

MANAGEMENT ACTIONS

- Investment refocus in order to fit the new situation and expectations for the Brent.
- Management of fluctuation risks by means of a **hedging** system that protects the Company from price fluctuations.
- Adjustment of **internal policies** tailored to the current scenario, enabling more adequate price risk management.
- Strategies to optimise production processes and improve efficiency enabling margins to be maximised in such a volatile context.
- **Vertical integration** of the Group enabling the economic cyclical effects and specific impact on the business units or areas to be minimised.
- Maintaining a sound equity structure equipping the Group with the **solvency** required in order to address potential changes in the economic and sectorial scenarios.
- Minimising the impact of the risk of change on commercial transactions performed (change risk is centralised and managed from the global net position of cashflows in currencies of the various Cepsa companies).
- **Centralising** the arrangement of financing sources, the investment of surplus funds, and **instruments for hedging** financial risk.
- The Cepsa Group is also exposed to changes in interest rates; hence, for the purpose of managing and mitigating that risk, the CEPSA Group, when it sees fit, obtains **fixed rate** financing or arranges **interest rate** hedging via financial derivatives.
- Keeping available an amount of credit facilities and treasury that ensures that payment obligations and any needs for funds are covered.
- Arranging insurance policies to cover the risk of bad debts of customers in some areas.
- Establishing a system of credit quality analysis of trade receivables and other client assets which are determined based on their solvency and payment performance (high, mid and low quality).

OPERATIONAL RISKS

Linked to operational effectiveness and efficiency, including the supply of products, goods and services, transport management, extraction and manufacturing processes, safety of personnel and facilities, care for the environment, human resources and information technology.



- 1. Refining margin
- 3. Operational safety
- 4. Physical security
- 5. Information security
- 6. Large projects management
- 7. Production and replacement of reserves
- 14. Talent management

CONTEXT/ EXTERNAL THREATS

- Refining margins are affected by the volatility of the markets, the accompanying high capacity of installed distillation in Europe and commissioning of new refineries in Asia – Middle East in the coming years. However margins are expected to increase substantially due to the entry into force of the MARPOL regulation in 2020.
- Upturn in M&A activity in the sector thanks to an improvement in the outlook for the price of crude oil.
- Growing concern and stricter regulation regarding environmental quality, and health and safety matters.
- Increasing vulnerability of the company in the current context of new technologies in terms of protecting its information.

RISK

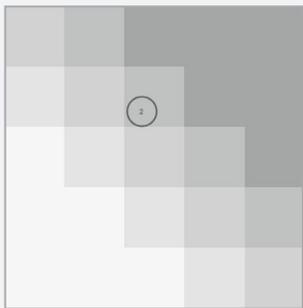
- Volatility of the refining margin.
- Industrial risks, prevention and safety which may lead to accidents and incidents at Cepsa facilities.
- Environmental risks arising from potential impact of our operations on the environment.
- Risks associated with information security.
- Management of large projects, production and replacement of reserves.
- Risks related to retaining and attracting talent related to the existing human resources' level of skills and how it fits in order to support strategic plans and growth objectives.

MANAGEMENT ACTIONS

- **Transformation** and **optimisation** projects to improve the efficiency and effectiveness of processes and operations at our industrial plants, and strengthen integration and synergies between units.
- Optimisation strategies for production processes and improved efficiency, and **research** for new product development with greater competitiveness and added value.
- Strict cost control reflecting the economic context and current prices.
- Safety integrated throughout the entire chain of command (stated in its "Basic Regulation" and in its management system based on international specification **OHSAS 18001:2007**).
- Insurance coverage for property damage risk, loss of profits arising from property damage; civil liability, and loss or damage in the transportation of crude oil, products and equipment.
- Establishing a **Policy** and **Internal Standard** for Environmental Protection and certification by independent bodies of the environmental management systems of all the major industrial Cepsa plants.
- Cybersecurity awareness, knowledge and training of employees, via training days providing a clear and pragmatic vision of cybersecurity underpinned by four key pillars: information, awareness, legal issues and technology.
- Certification of the existing Company Information Security Management by the strictest international standard (**ISO 27001**).
- Exhaustive **planning** and permanent **control** of costs and project deadlines are key maxims applied at Cepsa when executing and managing the complexity of the projects which it faces.
- Cepsa strives for **balance** in its project portfolio by expanding its activities to different countries.
- Launch of different programmes focused on development, training and attracting talent such as the **Challenging U** programme. Hiring policies and procedures (such as "Success Factors") that guarantee equal opportunities and zero discrimination.
- Development and dissemination of the initiatives carried out by the Company focused on improving the employment offer at Cepsa (**Top Employer**, certification as Responsible Family Company, Social Advantages, etc.).

REGULATORY AND COMPLIANCE RISKS

Related to the change in applicable regulations on the activities and/or sector and which may affect the structure with which the activities are performed and the results generated by operations, regulatory compliance and internal policies and procedures of the Company.



2. Regulatory uncertainty and Compliance

CONTEXT/ EXTERNAL THREATS

- The Paris Agreement (COP21) represents the first universal climate agreement. The agreement has been ratified by the immense majority of States although it must be noted that the United States is one of the exceptions.
- The EU has also set targets to progressively reduce greenhouse gas emissions by 2050. It should be noted that, within the framework of these targets, the existence of both the Package of climate and energy measures by 2020, which contains binding legislation, and the Climate and Energy Framework for 2030 aiming to reduce greenhouse gas emissions by 40%, aim at a share of at least 27% renewable energy and at least 27% improvement in energy efficiency.
- Regarding data protection, the European General Data Protection Regulation (2016/679) entered into force on 25 May 2016 and will be compulsory as of 25 May 2018.
- On 3 January 2018, the new regulatory framework on markets and financial instruments came into force, based on the MiFID II directive and the MiFIR regulation.
- The new KYC policies refer to the international fight against money laundering. The Spanish Act 10/2010 Prevention of Money-Laundering and Funding of Terrorist Activities regulates matters in this field.

RISK

- Compliance with legislation applicable to the sector's activities due to changes in that legislation.
- Misconduct or breaches of applicable internal regulations by our professionals and which may damage Cepsa's image and reputation.
- Regulatory changes due to the change in applicable legislation and tax regulations for the activities Cepsa performs or sector in which it operates.

MANAGEMENT ACTIONS

- Development of internal standards and procedures for the environment, biodiversity and health and safety and occupational risk prevention, guide our personnel's way of working in order to guarantee compliance with the applicable legal requirements, and incorporate other additional requirements in order to reach high levels of safety and environmental protection.
- In terms of corruption prevention, Cepsa has an Anti-Corruption Policy in place that establishes the procedural guidelines relating to fraud, transparency and the fight against corruption. Additionally, the Board's Audit, Compliance and Ethics Committee is tasked with overseeing the Internal Control over Financial Reporting (ICFR), which seeks to ensure a reasonable control environment in the preparation of the financial statements.
- In terms of fair competition, Cepsa has established a "Compliance Programme" tailored to the new European Commission criteria.
- Regarding the prevention of money laundering and terrorist financing, the Group's Board of Directors approved the Group Counterparty Analysis Policy in September of this year.
- Cepsa Group has implemented a comprehensive methodology to set up a Corporate Compliance Model that allows us to identify compliance risks and implement preventive and detective measures and sanction conduct that may result in company or employee liability, including commitments acquired by Cepsa under its Code of Ethics and Conduct, and their commitment to Corporate Responsibility.
- Cepsa Group has an Ethics and Compliance Channel and a Policy that describes how it works and how investigations are managed; both are available to the public via our corporate website www.cepasa.com.
- Anticipation and adaptation to regulatory changes to minimise the impact of regulations: Cepsa strives to be ahead of the market in terms of change, and adapts to new requirements as quickly as possible.