Quick overview

In line with the “Lifting profitability and Driving sustainability” agenda Hydro is committed to two overarching long-term targets: 1) Lifting RoaCE > 10 percent over-the-cycle; and 2) Reducing Hydro’s total CO2 emissions by 30 percent by 2030. In response to the Covid-19 outbreak in 2020, Hydro launched decisive immediate cash-preservation measures, while at the same time strengthening longer-term measures to improve cash generation from current operations. Hydro also focused on positioning the company for the future and defined the most attractive growth areas, where the megatrends match Hydro’s capabilities.

Hydro’s financial priorities are to create long-term shareholder value by generating capital returns above the cost of capital over-the-cycle supported with clear priorities for capital allocation, while at the same time maintaining a strong balance sheet and ensuring a robust shareholder payout. In the shorter-term, Hydro aims to lift cash flows towards 2025 by supporting earnings with the improvement ambition and commercial initiatives, while also optimizing capex and net operating capital. Finally, in order to reduce risk and lift value potential, Hydro aims to diversify its portfolio and pursue profitable growth opportunities within recycling, renewable energy and batteries.

Our future profitability depends on our ability to operate sustainably. We have quantified a set of ambitions towards 2030 to improve our performance on climate, environment and social responsibility. By reducing risk, emphasizing safety in our operations, improving relations with stakeholders and neighbours, increasing resource efficiency, reducing our own emissions and developing new markets, Hydro’s business will be more robust. Complying with laws, regulations, Hydro’s steering documents and respecting human rights, is fundamental to Hydro’s way of working and are considered key elements to the company’s license to operate.

On March 5, 2021, Hydro entered into an agreement to sell its Rolling business. The sales transaction will impact Hydro’s targets and ambitions such as the improvement program, commercial ambitions, recycling growth targets and sustainability goals and targets. Targets included in this report include the Rolling business area and will be adjusted during 2021.
Lifting profitability, driving sustainability

Hydro’s financial ambition is to lift cash flows and generate capital and shareholder returns through a combination of longer-term financial priorities supported by near-term financial targets. At the same time, Hydro aims to differentiate through its strong sustainability position and to develop businesses where megatrends match Hydro’s capabilities.

Supported by an increasing interest from the regulators, customers and financial markets, Hydro firmly believes that leading in sustainability is a strong foundation for long-term license to operate and a key driver for long-term profitability. By emphasizing climate, environment, integrity and social responsibility, as well as by developing greener business and product offerings, Hydro will reduce risks and create new profitable opportunities for the future.

In 2020, the Covid-19 pandemic created significant social, operational and market challenges. The company responded with a number of cash-preservation actions in the short-term and a set of stronger improvement measures until 2025. Despite the challenges in 2020, Hydro has focused on positioning the company for the future reflected in the revised strategy to differentiate with greener products and diversify the business portfolio beyond aluminium. Furthermore, Hydro conducted a review of its key financial metrics and has prioritized those metrics that are most aligned with the financial and strategic agenda. The first chapter describes the 2020 progress on the existing targets and then introduces the revised financial goals towards 2025 and beyond. The second chapter gives an introduction to Hydro’s sustainability agenda, ambitions, targets and performance.

On March 5, 2021, Hydro entered into an agreement to sell its Rolling business. The sales transaction will impact Hydro’s targets and ambitions such as the improvement program, commercial ambitions, recycling growth targets and sustainability goals and targets. Targets included in this report include the Rolling business area and will be adjusted during 2021.

Lifting profitability

Description and progress in 2020

Financial priorities

Hydro has developed a framework that establishes clear priorities for uses of cash in order to help guide the company’s capital allocation decisions. The Covid-19 outbreak in 2020 has put Hydro’s financial framework and its agility to a test. The pandemic introduced significant uncertainty regarding the financial outlook for the company with potential negative implications for Hydro’s investment grade credit rating. Hydro responded with a set of cash-preservation measures in order to mitigate the downside scenario. The balance sheet strength was prioritized, with dividends temporarily suspended and capex reduced by 20 percent compared to plan. Net operating capital optimization, portfolio review and restructuring as well as additional cost reductions were all used as additional sources of cash. The implemented measures illustrate the flexibility of Hydro’s financial framework allowing the company to act according to the established financial priorities in an unprecedented situation.

Financial strength and flexibility

Hydro is committed to maintaining a robust balance sheet, strong liquidity and an investment grade credit rating. Hydro considers this crucial in order to navigate the industry cycles and to be able to invest also during cyclical downturns. Up until 2020, two financial ratios were used as indicators of the balance sheet strength: Funds from operations to average Adjusted net cash (debt), with a target to stay above 40 percent over the cycle, and Adjusted net cash (debt) to Equity, with a target to stay below 55 percent over the cycle. Following a review of the key financial metrics used for performance follow-up and managing capital, these two metrics will be replaced by average Adjusted net cash (debt) to underlying EBITDA going forward (see later in this chapter).

Currently, Hydro has a BBB rating with S&P Global and a Baa3 rating with Moody’s, both with a stable outlook. The average Funds from operations to Adjusted net cash (debt) ratio was 39 percent in 2020, close to the over-the-cycle target of 40 percent, and an improvement from 27 percent in 2019. The negative impact from the Covid-19 pandemic was partly offset by higher production in Alunorte, improved smelter margins, and a strong cost response throughout the company. The Adjusted net cash (debt) to Equity ratio was 36 percent, within the over-the-cycle ambition to stay below 55 percent. For further details, see Note 7.1 Capital management to the consolidated financial statements.
In order to ensure strong liquidity, Hydro has a NOK 1.6 billion undrawn revolving credit facility that expires in 2025. The margin on the facility is linked to Hydro’s CO2 emission reduction target, thereby linking financing costs to the progress on Hydro’s main climate target and highlighting the important connection between sustainability and profitability. As a measure to secure funds during the covid-19 situation, Hydro issued bonds amounting to NOK 7 billion in May 2020.

**Robust shareholder payout**

Hydro aims to offer its shareholders a predictable dividend and a satisfactory yield. Up until 2020, Hydro’s ambition was to pay out 40 percent of reported net income to majority shareholders over the cycle, and a dividend floor of NOK 1.25 per share. In response to high uncertainty on the back of the unprecedented covid-19 pandemic, the 2019 dividend was suspended in May 2020. However, the dividend was distributed later, in November 2020, based on the improved financial position and positive outlook for the company.

Hydro’s Board of Directors proposed an annual dividend of 1.25 NOK per share. The new policy reflects Hydro’s ambition to lift performance and cash returns to shareholders over the cycle. Hydro may evaluate share buybacks and additional dividends with due consideration given to the alternative investment opportunities, financial situation and earnings outlook.

**Clear principles for capital allocation**

Hydro has established clear priorities and guidelines for capital allocation. This is critical in order to deliver on the company’s strategic direction and may be an important differentiator for the long-term financial performance. The strategy is to allocate more growth and return-seeking capital to the areas with higher value generation potential, both from a profitability and sustainability perspective. Historic returns on investments, earnings volatility, differentiation potential, and improved sustainability position play a key role in the allocation process. All the business areas have been grouped into different strategic modes. The focus in Bauxite & Alumina and Aluminium Metal is to sustain and improve the current asset base, Extrusions and Energy are in selective growth mode. Rolling was put under restructuring and strategic review in 2019, which was concluded in March 2021 with a sale of the Hydro Rolling business to KPS Capital Partners. Recycling across the portfolio, renewables and batteries have been identified as the strategic growth areas.

---

9 Pending approval from the AGM on May 6, 2021.

10 The transaction is subject to customary approvals from competition authorities and is expected to be completed during second half of 2021.
Roadmap to profitability targets

Hydro has a target to achieve an underlying return on average capital employed (RoaCE) of 10 percent over the cycle compared to the group long-term nominal cost of capital of 9 percent. Both the cost of capital and the corresponding return requirements are differentiated for each business area with the ambition to achieve an underlying return on average capital employed above the respective cost of capital. Nominal long-term cost of capital for business areas reflects the risk and volatility of earnings and cash flows. For more cyclical upstream divisions – Bauxite & Alumina and Aluminium Metal – it is set to 10-11 percent, for the downstream divisions with more stable earnings profiles – Extrusions, Rolling and Metal Markets, including recycling – it is 7-8 percent, while in Energy it is 6-7 percent reflecting a relatively low risk and low earnings volatility.

In 2020, underlying return on average capital employed was 3.7 percent, significantly below the ambition to deliver 10 percent over the cycle, mainly as a result of weak macroeconomic conditions due to the Covid-19 pandemic. This, however, was an improvement from 1.3 percent in 2019 affected by the Alunorte embargo as well as the cyber attack. For more information on the returns on average capital employed, see the Alternative performance measures (APMs) section in the Appendices to the Board of Directors’ report.

<table>
<thead>
<tr>
<th>Business areas1)</th>
<th>2020</th>
<th>2019</th>
<th>2020</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hydro</td>
<td>7.5 %</td>
<td>(0.9) %</td>
<td>3.7 %</td>
<td>1.3 %</td>
</tr>
<tr>
<td>Bauxite &amp; Alumina</td>
<td>5.4 %</td>
<td>1.9 %</td>
<td>5.9 %</td>
<td>2.5 %</td>
</tr>
<tr>
<td>Aluminium Metal</td>
<td>1.9 %</td>
<td>(3.9) %</td>
<td>2.9 %</td>
<td>(2.6) %</td>
</tr>
<tr>
<td>Metal Markets</td>
<td>22.5 %</td>
<td>20.7 %</td>
<td>21.4 %</td>
<td>27.3 %</td>
</tr>
<tr>
<td>Rolling2)</td>
<td>(12.1) %</td>
<td>(5.0) %</td>
<td>0.4 %</td>
<td>2.4 %</td>
</tr>
<tr>
<td>Extrusions</td>
<td>1.3 %</td>
<td>3.8 %</td>
<td>6.2 %</td>
<td>5.7 %</td>
</tr>
<tr>
<td>Energy3)</td>
<td>249.5 %</td>
<td>13.4 %</td>
<td>8.7 %</td>
<td>12.9 %</td>
</tr>
</tbody>
</table>

1) Hydro group RoaCE calculated as EBIT last 4 quarters less Income tax expense adjusted for tax on financial items/Average capital employed last 4 quarters. RoaCE at business area level is calculated using 25% tax rate, and 80% tax rate for Energy (also see footnote 2) below.

2) Reported RoaCE for Rolling in 2020 was affected by an impairment loss of NOK 1.9 billion related to the sale of the Rolling business to KPS Capital Partners.

3) Reported RoaCE for Energy in 2020 was affected by a recognized gain of NOK 5.3 billion related to the Lyse Kraft DA transaction (excluded from underlying results). A tax rate of 25% was applied to calculate Energy reported RoaCE in 2020. Energy reported RoaCE 2019 restated to 13.4% from 14.7%, as disclosed in the Annual report 2019, due to change in tax rate in the calculation.

In the medium- to long-term Hydro’s strategic direction is to diversify earnings and portfolio in order to reduce exposure to the volatile upstream markets, and to grow in the areas that promise attractive returns on capital employed. Hydro will also differentiate from its competitors with its strong sustainability position that is supported with the megatrends and the current regulatory developments. Further, Hydro will continuously review its portfolio in order to identify and manage non-performing and/or non-strategic assets to foster reallocation of capital. These initiatives are expected to provide an upside to the RoaCE potential from the existing asset base visualized on the graph above.

Financial targets

Hydro’s performance in the recent years has been affected by the Alunorte embargo in 2018-2019, cyber-attack in 2019, as well as the weakening market outlook further exacerbated by the global pandemic in 2020. The 2023 targets launched in 2019 had been impacted by the Covid-19 situation and were revised early in 2020. To support group cash generation, Hydro has strengthened focus on optimizing the capex profile and managing net operating capital and has extended its improvement efforts towards 2025. This chapter reviews the 2020 status on the targets established in 2019, while the revised goals are described in the next chapter.

Improvement program

Hydro started the year with an accumulated 2020 improvement target of 4.1 BNOK out of the total ambition of 7.3 BNOK by 2023, of which 1 BNOK was realized in 2019. The program consisted of various improvement levers including volume ramp-up in Brazil following the Alunorte embargo, cost, efficiency and procurement initiatives across the business areas and staffs, commercial activities to drive volumes and margins mainly downstream as well as growth ambitions such as HUSNES smelter restart in Aluminium.
Metal, customer-driven growth in Extrusions and energy-storage investments in Energy. About a quarter of the program was based on commercial and growth initiatives that rely on the market support.

The Covid-19 pandemic and the related macroeconomic slow-down with a sudden demand drop as well as a series of lockdowns imposed by the authorities to reduce the spread of the virus significantly impacted the progress on many improvement initiatives exposed to the market. The net EBIT ambition in Extrusions suffered as a result of shrinking demand, and so did portfolio high-grading activities in Rolling. Aluminium Metal adjusted its product and project portfolio in response to the weak demand by postponing the planned Husnes restart, partially curtailing Slovalco and disconnecting electrolysis cells in several Norwegian smelters. Growth initiatives in Energy, in particular Corvus, were also affected by the market situation. Furthermore, performance and ramp-up in Brazil were affected by some operational issues unrelated to covid-19, including extended pipeline maintenance in the Paragominas mine and a fire incident in the Albras smelter. As a result, the realized improvements in 2020 lagged far behind the initial target of 4.1 BNOK for the year.

In response to the challenges, Hydro has revised the improvement program definition in order to exclude market-driven initiatives affected by covid-19 and to visualize the progress on the initiatives within Hydro’s control. This allowed the organization to set realistic targets thereby lifting motivation and created a strong incentive to look for further improvements across Hydro. As a result, Hydro exceeded the re-focused target of 4.1 BNOK accumulated for 2020 and realized 4.2 BNOK in improvements, of which NOK 0.5 billion came from various initiatives in Rolling. The re-focused definition has replaced the previous 7.3 BNOK target by 2023 with a new target of 8.5 BNOK by 2025 in cost and efficiency initiatives. Commercial and growth ambitions will come in addition. The new improvement definitions and targets are described in the next chapter.

Completion of Hydro Rolling strategic review
On March 5, 2021, Hydro entered into an agreement to sell its Rolling business to KPS Capital Partners. The sale of Rolling will enable Hydro to deliver on the 2025 strategy, strengthening our position in low-carbon aluminium, while exploring new growth in areas where our capabilities match global megatrends. The sales transaction will impact Hydro’s targets and ambitions such as the improvement program, commercial ambitions, recycling growth targets and sustainability goals and targets. Targets included in this report include the Rolling business area and will be adjusted during 2021.

Optimizing capital allocation
Ensuring disciplined capital allocation is key to deliver on return requirements, with growth projects to be aligned with strategic priorities, and sustaining capex to be maintained at competitive and affordable levels. At the beginning of the year, Hydro guided for a capex level of 9.5-10 BNOK in 2020, of which 6.5-7 BNOK in sustaining investments. However, as described above, capex was reduced by 20% in the midst of the covid-19 situation in order to preserve cash and prepare for a potential severe downside scenario. This resulted in an updated 2020 guidance of 7.5-8 BNOK, of which 5.5 BNOK in sustaining capex.

Total capex in 2020 ended up at NOK 6.4 billion, excluding lease and excluding periodization effects of NOK (0.1) billion, a further reduction of about 15 percent compared to the already reduced frame. Some projects have been postponed to 2021, while others have been re-prioritized or delayed. Some customer-driven investments, especially in Extrusions, did not materialize in 2020 due to the market situation. In addition, positive currency development, in particular weakening of the BRL vs the NOK, has also contributed to the reduction beyond the targeted levels.

The capex reduction compared to the year-end estimate of NOK 7 billion communicated at the Capital Markets Day in December 2020 is largely due to a capex carry-over into the next year and is reflected in the updated 2021 capex guidance.

Projects prioritized in 2020 include critical maintenance activities needed to safeguard Hydro’s production assets in every business area. Examples include smelter relining in Aluminium Metal, power plant rehabilitation and upgrades in Energy, various upgrades of presses in Extrusions, rolling mills in Rolling and recyclers in Metal Markets. In addition to those, Bauxite & Alumina accounted for a large share of sustaining investments in 2020. These were mainly related to the bauxite pipeline maintenance, the tailings dry backfill project in Paragominas as well as several investments to improve energy efficiency of the boilers and calciners in the Alunorte refinery.

Growth and return-seeking capex was significantly reduced in 2020 as many growth and customer-driven investments were paused and postponed. The main spend in this category was related to the Husnes smelter upgrade and restart resumed in November and ongoing customer-driven investments in Extrusions.
Strengthen working capital management

Reflecting the strong focus on cash generation, maintaining an efficient level of working capital is a top priority. The main initiatives include high focus on inventory reduction in all business areas, optimizing material flow from raw materials to finished goods, establishing benchmarking tools and regular follow-up procedures, and tight collaboration between sales and metal purchasing.

Hydro released NOK 2.4 billion of cash-effective net operating capital in 2020, in addition to NOK 5.6 billion released in 2019. On top of a general reduction in net operating capital due to the weak market conditions, the largest contributor were inventory reductions in Rolling and Extrusions, partly offset by higher levels of safety stocks. Average net operating capital in days of revenue (NOC-days) was 59 in 2020, slightly down from 60 days in 2019.

The dashboard below summarizes the 2020 achievement on the key financial priorities and targets.

---

### 2020 Status and targets

**Lifting profitability**

- **Capital returns**
  - URoaCE: 3.7%<sup>1)\</sup>
  - 10% target over the cycle

- **Balance sheet**
  - FFO/aND: >40%<sup>2)\</sup>
  - 40% target over the cycle

- **Free cash flow**
  - 7.7 BNOK<sup>3)\</sup>

**Improvement program**

- **Cash effective change in net operating capital**
  - 2.4 BNOK release

- **Capex**
  - 6.4 BNOK<sup>5)\</sup>

- **Shareholder payout**
  - 1.25 NOK/share<sup>6)\</sup>

---

1) URoaCE Hydro (Annual definition) calculated as underlying EBIT last 4 quarters less income tax expense adjusted for tax on financial items/ Average capital employed last 4 quarters.
2) Funds from operation LTM/Average LTM adjusted net debt. From 2021, Hydro will replace this measure with a goal of net debt excluding equity accounted investments over uEBITDA < 2x.
4) The original improvement program definition was revised in 2020 with effect from 2019, now focused on cost and efficiency initiatives and excluding market driven initiatives.
5) 2020 capex excluding lease and excluding periodization effects of NOK (0.1) billion. 2021 target including capex carry-over from 2020.
6) Pending approval from the AGM on May 6, 2021. From 2021 onwards, the policy has been revised to a minimum of 50% payout ratio of underlying net income over the cycle with the dividend floor maintained at 1.25 NOK per share.

* Targets to be revised following the sale of the Rolling business area.
Performance targets 2021-2025

In addition to the immediate measures implemented in 2020 in response to the covid-19 situation, Hydro has focused on positioning the company for the future, which resulted in a streamlined strategic direction and further stretched financial ambitions towards 2025. To support the revised agenda, Hydro has also reviewed its key financial measures and has prioritized the ones most aligned with the new ambitions. This chapter describes the updated financial goals towards 2025 and beyond.

Review of key financial metrics

During 2020, Hydro reviewed the key financial metrics used for performance follow-up and managing capital. The goals were to achieve clear communication aligned with industry and peer practice, simplify where possible, and through that support a correct valuation of the Hydro share and debt. This process resulted in Hydro focusing on EBITDA as the main performance measure. Hydro considers EBITDA, in combination with cash effective change in net operating capital and capital expenditures (capex), to be a better support to Hydro’s focus on cash generation than EBIT, which also includes consumption of historic investments. EBITDA is also more commonly used among peers and preferred by Hydro’s investors and analysts. The review also included the key financial solidity ratios used. Management has decided to replace Adjusted net cash (debt) to Equity and Funds from operations to average Adjusted net cash (debt) with average Adjusted net cash (debt) to underlying EBITDA, which is a more broadly used metric in the industry as well as consistent with the increased focus on EBITDA. Note that Adjusted net cash (debt) will focus on Hydro’s debt only, excluding the previously included adjustments for debt in equity accounted investments. Hydro targets, over the business cycle, a ratio of average Adjusted net cash (debt) to underlying EBITDA below 2x. See Note 7.1 Capital management for further information.

Updated financial priorities and targets

Financial priorities

The four financial priorities described earlier in this chapter remain in place, however with some changes. Hydro maintains its capital return target of 10 percent underlying RoaCE over-the-cycle and will continue to actively use the capital allocation framework. Strong balance sheet and liquidity continue to be the top priority, with a target of maintaining average Adjusted net cash (debt) to underlying EBITDA below 2x over the business cycle. For comparison, this ratio was 1.93 and 2.27 in 2020 and 2019, respectively. During 2020, Hydro has performed a review of risk management strategy, and intends to utilize derivative and non-derivative measures to manage price exposure over slightly longer period than the practice in recent years. Finally, Hydro’s goal is to create long-term value for its shareholders and to offer robust and predictable payout annually. In addition, Hydro aims to lift performance and cash returns to shareholders over the cycle. To emphasize this commitment, the Board of Directors has increased the dividend payout ratio from 40 percent of Net Income to a minimum of 50 percent of underlying Net Income over the cycle with effect from 2021 onwards.

Financial targets

In order to succeed with its longer-term financial ambitions, Hydro has established a set of targets within the 2025 horizon. The main goal is to lift cash flow generation from current operations and to establish a solid foundation for future cash generation potential through growth. The focus areas include 1) Improvement program and commercial ambitions; 2) New strategic growth initiatives; 3) Capex optimization; 4) Net operating capital optimization.

Targets and ambitions described in this report include the Rolling business area. The sales transaction of Hydro Rolling to KPS Capital Partners announced in March 2021 will impact Hydro’s targets and ambitions such as the improvement program, commercial ambitions, recycling growth targets and sustainability goals. These will be reviewed during 2021.

Three levers driving Hydro value creation potential to 2025

- BNOK 8.5 Improvement program
  - Maximizing value-creation from current assets/operations
    - Operational excellence
    - Commercial excellence in daily operations
    - Raw material efficiency, procurement
    - Volume creep and capacity utilization
    - Fixed cost optimization
  - Initiatives focused on influenceable parameters and continuous improvement

- BNOK 2.0 Commercial ambitions
  - Pursuing market and customer-driven growth opportunities
    - Pricing and share of the wallet
    - Upgrading and developing product portfolio
    - Customer-driven incremental growth
  - Initiatives within the current business portfolio, dependent on market conditions

- Larger changes in business portfolio and/or strategic direction
  - Recycling: more than doubling post-consumer scrap utilization, creating EBITDA uplift of BNOK 1.0 to 1.5 by 2025
  - Renewable Growth: investing into more than 1GW of renewable power projects in 2021
  - Battery: Generating pro-rata EBITDA of MNOK 600 - 700

* Targets and ambitions to be revised following the sale of the Rolling business.
The full value creation potential

In order to reflect the full value potential in Hydro, a new framework has been introduced with targets extended until 2025 (as described on figure below)\(^\text{12}\). It includes three levers: 1) improvement program focused on the controllable parameters, such as costs and operational excellence; 2) commercial initiatives that cover largely customer-driven initiatives within the current asset portfolio and are dependent on the market support; and lastly 3) strategic and growth initiatives that currently include ambitions within Recycling, Renewable Growth and Batteries. While equally important, these three categories differ in the extent they can be influenced by Hydro, cyclacity and reliance on the market conditions, time horizon, as well as relevant measurements and targets.

Improvement program

Operational excellence is key when it comes to maximizing value creation from current assets; and relies on the culture of continuous improvement and good control over the influenceable parameters. These initiatives are developed consistently throughout the cycle regardless of the macro and market situation. The total EBITDA improvement potential in the period 2019-2025\(^\text{13}\) amounts to NOK 8.5 billion, reflecting the sum of potentials in all the business areas as well as staff functions and procurement. The program is front-loaded and around 70 percent — NOK 6.0 billion — of the total improvements expected to be delivered by end-2021.

<table>
<thead>
<tr>
<th>2025 accumulated improvement potential by year</th>
</tr>
</thead>
<tbody>
<tr>
<td>In NOK billion</td>
</tr>
<tr>
<td>2.7 NOK billion</td>
</tr>
<tr>
<td>3.0 NOK billion</td>
</tr>
<tr>
<td>5.8 NOK billion</td>
</tr>
<tr>
<td>0.6 NOK billion</td>
</tr>
<tr>
<td>0.2 NOK billion</td>
</tr>
</tbody>
</table>

The main improvement levers include volume, fixed costs optimization, raw material cost and efficiency, and process and commercial excellence in daily operations.

The Bauxite & Alumina improvement program mainly focuses on ramping-up production at Alunorte and Paragominas to full capacity. This accounts for NOK 2.7 billion out of the total Hydro improvement target by 2025. In 2020, capacity utilization in the refinery averaged 87 percent and is expected to reach the nameplate capacity of 6.3 million tons of alumina in 2021. Other elements include optimization of the energy mix and consumption as well as fixed costs reduction.

Aluminium Metal target improvements across many categories, including restart of the Husnes smelter and volume ramp-up at Albras in Brazil, debottlenecking, fixed cost reduction including overhead costs, as well as digitalization of processes through soft sensor technology, advanced analytics, and automation.

Improvements in Rolling are to be achieved through organizational right-sizing and de-manning mainly resulting from closure of two foil lines in Grevenbroich, Germany; improving raw material cost with metal cost optimization such as increased use of scrap; and procurement improvements. Restructuring initiatives have delivered above expectations, with NOK 500 million of NOK 1.1 billion improvement program delivered by end 2020. At the same time, Hydro launched a strategic review and restructing of Rolling in 2019 aiming to evaluate the optimal ownership set up for the business area. The review was concluded with a 100 percent sale of Hydro Rolling to KPS Capital Partners, announced on March 5, 2021. The transaction will enable Hydro to deliver on the 2025 strategy, strengthen our balance sheet and position in low-carbon aluminium, while exploring new growth in areas where our capabilities match global megatrends. See Board of Directors Report for more information on the transaction.

Extrusions have launched an extensive cost improvement program that includes SG&A cost reduction, portfolio review and restructuring as well as procurement initiatives.

Improvements in Energy include commercial and operational handling in Energy’s daily operations and realizing synergies related to the Lyse Kraft DA transaction.

Improvements in all business areas include savings related to increased efficiency within staff and support functions, with Global Business Services (GBS) contributing the most. A sizeable share of improvements comes from the Hydro-wide procurement initiative addressing measures within supplier management, demand and specification management and process management across the company.

\(^{12}\) Targets and ambitions to be revised following the sale of the Hydro Rolling business.
\(^{13}\) The programs use 2018 as the baseline year for, e.g., operational parameters and production. As market conditions and prices in 2018 were heavily influenced by the Alunorte situation, LME, PAX, raw materials and exchange rates have been based on a 3-year average (2016 – 1H-2018).
By end-2020, NOK 4.2 billion was realized compared to the re-focused improvement target of NOK 4.1 billion. The main contributors were Bauxite & Alumina with the continued volume ramp-up and Extrusions with aggressive cost optimization initiatives, including procurement and restructuring. Aluminium Metal and Rolling have also delivered significant cost savings. However, performance in the upstream divisions was behind plan due to several operational issues in Brazil. This was offset with higher than expected cost improvements in both downstream divisions – Extrusions and Rolling.

Commercial initiatives
Commercial initiatives are about pursuing market and customer-driven growth opportunities within the current business portfolio. They drive topline growth and represent an important part of mid to long-term value-creation, especially in the downstream divisions. Execution and success of these initiatives rely on the market support and customer demand, and therefore are less certain. The total EBITDA potential from commercial activities adds up to NOK 2 billion in the period from 2019-2025. This includes new product development in Aluminium Metal, such as growing greener products offering; portfolio high-grading initiatives towards market segments with higher growth and margins, such as automotive, beverage can and battery foil in Rolling; and various efforts, such as plant specialization, to gain market share in dedicated segments and lift margins in new customer projects in Extrusions.

In 2021, commercial initiatives are expected to contribute positively in line with the projected partial recovery following the cyber-attack in 2019 and the covid-19 pandemic in 2020. However, the progress will depend on the market development and customer demand, and full return to the 2018 levels is not expected until 2022-2023.

Growth and strategic initiatives
Growth and strategic initiatives represent larger changes in the business portfolio and/or significant strategic moves within the current portfolio and are key drivers of long-term shareholder value creation. Hydro’s strategy is to diversify and grow in recycling, renewable energy and storage solutions – areas, which are supported by the current megatrends and where Hydro can leverage the company’s core industrial expertise and footprint to generate returns.

The potential is to more than double post-consumer scrap utilization across Hydro with EBITDA uplift of NOK 1.0 to 1.5 billion by 2025; and to generate pro-rata EBITDA of NOK 600 – 700 million by 2025 through investments in batteries. In addition, Hydro’s expertise within Energy combined with significant power consumption in production processes make Hydro an attractive partner in renewable projects. Already in 2021, Hydro targets to invest in more than 1GW of renewable power projects on a 100 percent basis together with its partners.

In order to lay a strong foundation for successful growth, Hydro’s first priority is to build a solid pipeline of attractive and profitable investment opportunities in recycling, renewables, and batteries. The progress will depend on business cases and access to funding, among other factors.

Capex optimization
Following the capex cut to a level of 6.4 BNOK in 2020 in response to the Covid-19 situation, Hydro is guiding for the total capex of NOK 9.5-10 billion in 2021, which includes a capex carry-over from 2020 due to the project timing and delays. Sustaining capex in 2021 accounts for NOK 6.5-7 billion out of the total. For the period of 2022-2025, current investment plans add up to an average of NOK 9-9.5 billion per year, of which NOK 6.5-7 billion in sustaining capex, including Rolling. In the long-term, sustaining capex needs are estimated to NOK 6-6.5 billion per annum, with the continuous efforts ongoing to ensure long-term competitive sustaining capex level. A certain level of investments in Extrusions, currently classified as return-seeking, is necessary in order to replace completed customer projects and maintain a stable earnings level. These will come on top of the indicated long-term sustaining capex guidance. The main projects requiring sustaining capex in the period 2021-2025 include investments in Alunorte robustness, opening of a new mining area in Paragominas, pipeline replacement in Bauxite & Alumina, and smelter reining and asset integrity in Aluminium Metal.

Growth and return-seeking guidance reflects NOK 2 to 3 billion that Hydro intends to invest annually through 2025 in order to achieve its cost improvement and commercial ambitions within our current portfolio. The main projects include selected customer-driven growth in Extrusions, recycling and metal cost optimization across Hydro, and the fuel switch project in Bauxite & Alumina.

Capex guidance

Larger organic and inorganic investments needed to enable strategic growth in recycling, renewables and batteries are not included in the guidance. In order to achieve the targeted EBITDA uplift in recycling, Hydro estimates additional investments of between NOK 2.5 and 3 billion within 2025 to handle more scrap, implement advanced sorting technology, and upgrade existing recycling and recasting capabilities. To achieve the targeted value uplift within batteries, Hydro and the battery partners intend to invest in attractive areas of the value chain requiring about NOK 2.5-3 billion capex from Hydro’s ownership share. The Renewable Growth projects

14 - Targets and ambitions to be revised following the sale of the Hydro Rolling business area.
will be financed through a partnership model with Hydro as an industrial minority partner in funded Special Purpose Vehicles (SPVs) established for each site.

**Net operating capital optimization**

In order to maximize cash generation and minimize tied-up capital, while giving due consideration to managing supply chain and production risks, Hydro will continue optimizing net operating capital levels both in absolute terms and in days of revenue. Development going forward may be affected by underlying market conditions, changes in prices and exchange rates, as well as shifts in the portfolio mix.

**Driving sustainability**

Sustainability is an integrated part of lifting Hydro’s long-term profitability and the basis for our future positioning. By reducing our footprint, improving relations with stakeholders and neighbors, managing impacts, increasing resource efficiency and developing new markets, Hydro will reduce risk and create new opportunities.

In developing a more holistic approach to sustainability we have quantified a set of ambitions towards 2030 that will improve our performance on climate, environment, business ethics, and social responsibility. We have ambitions to reduce our own environmental impacts and emissions in production, develop greener products, help our customers design more sustainable solutions and continue with our ambition to make a positive difference by strengthening local communities and our business partners. The sales transaction of Hydro Rolling to KPS Capital Partners announced in March 2021 will impact Hydro’s targets and ambitions, and these will be reviewed during 2021.

The overarching goal of our climate strategy is to reduce the impact our operations have on the global climate. The climate strategy – “30 by 2030” – calls for a 30 percent reduction of own greenhouse gas emissions throughout the aluminium value chain by 2030. We will do this through greener sourcing and greener production, that will reduce the carbon footprint of the products we deliver to our customers. We have initiated a significant R&D program towards 2030 to look into different alternatives to achieve CO2-free processes. We will explore different paths such as carbon capture and storage, biomass anodes and carbon-free processes. By 2030 we expect to have a clearer view on a path to further significant GHG emission reductions by 2050.

In 2020, we expected no GHG emission reductions due to higher expected production. However, total GHG emissions were reduced by 9.1 percent compared to the climate strategy’s baseline. About half of the reduction were due to improved performance, especially at the Alunorte refinery. The remaining reduction was due to significant reduced production across Hydro because of the Covid-19 pandemic.

The environment strategy for 2030 addresses the industry’s key environmental challenges. Our goal is to mitigate emissions to land, water and air, conserve and restore biodiversity and reduce waste production. To achieve this, we strive to identify, monitor and reduce environmental risk throughout the lifetime of our operational sites. The emphasis of the 2030 environmental strategy is continued rehabilitation at our bauxite mine in Pará, Brazil, reducing our tailings and bauxite residue footprints, recycling our spent pot lining and halving our non-greenhouse gas emissions (SO2, NOx and particulate matter) to air.

Hydro Bauxite & Alumina has developed and tested of the “Tailings Dry Backfill” methodology at the Paragominas mine, addressing one of the industry’s key challenges. This is an approach to minimize the volume of tailings stored, by excavating dried tailings from the storage facility and returning it to the mined areas before they are rehabilitated. The methodology eliminates the need for continuous construction or upgrade of new permanent tailings facilities. The application of this approach in Paragominas represents the end of construction of new facilities for storage of bauxite tailings. The operating license to implement this new approach was received in December 2020, and it has now been fully adopted into operations at the mine.

We recognize that we can only succeed if communities and partners around us succeed. With our social responsibility strategy we aim to make a positive difference by strengthening our business partners and the local communities where we operate. To deliver on this, we will target the fundamental drivers of long-term development and will contribute to education and capacity building for 500,000 people by end of 2030. Community dialogue and stakeholder engagement is the foundation of our work.

Social responsibility programs, initiatives and dialogue with local communities surrounding our operations continued in 2020. Due to Covid-19, all activities have adapted new measures. Where possible, activities have been moved to digital platforms, and infection prevention protocols are strictly followed for physical activities. During 2020, Hydro has approved and started implementing a revised Human Rights Policy and Supplier Code of Conduct, based on prioritized human rights risks to people.

In Hydro, we see diversity as a as a source of competitive advantage, as it encourages innovation, learning and better customer understanding. Through diversity and inclusion, we want all employees to know they are valued for their differences and that they contribute to the success of our business strategy. Hydro has established an ambition to increase the share of women employees to 25 percent by 2025, the share of women employees was 18 percent in 2020.

Our ambition is to prevent all injuries and ill health to avoid human suffering and we will work continually to avoid damage to property and loss of production. We continue to see high-risk incidents with a potential for fatality or permanent injuries or ill health, but at a lower level than previous years. We consider this the main leading indicator for our safety performanceFrom 2020, our emphasis has also been on the closing rate of actions related to high-risk incidents in our operations in 30 days. For 2020 we achieved a rate above 90 percent. We consider this one of the main leading indicators for our safety performance. The high-risk incident rate improved in 2020.

The number of total recordable injuries and associated rates improved over 2019 levels to a total recordable injury rate of 2.7 from 3.0.
There were no life-threatening injuries during the year; however, there was one life changing injury at one of our North American facilities where a worker’s right foot was surgically amputated after his foot was crushed when a heavy load fell from the forks of a forklift truck.

Complying with laws, regulations, and Hydro’s governing documents, and respecting human rights, is fundamental to Hydro’s way of working and are considered key elements to the company’s license to operate.

Hydro’s certified product brands CIRCAL and REDUXA, set a new standard for low-carbon and recycled aluminium, and commercialize the company’s sustainability position. Customer feedback and order intake underline the potential for these types of products that represent exciting opportunities moving forward. Hydro is a founding member of the Aluminium Stewardship Initiative (ASI) and has currently certified 61 sites according to the ASI Performance Standards, covering the value chain from bauxite mining to finished products. ASI sets standards for responsible production throughout the aluminium value chain and covers issues like climate change, biodiversity, human rights etc. Most of the sites are also certified according to the ASI Chain of Custody standard which allows Hydro’s sites to sell ASI certified material to our customers. Hydro is currently the aluminium company with most certifications globally, and has certified all fully owned production sites in Europe according to the ASI Performance Standard and the ASI Chain of Custody standard.

For a description of Hydro’s policies, commitments, goals and targets, responsibilities, resources, grievance mechanisms related to sustainability, see Viability Performance and Viability Performance Statements. Hydro reports according to the GRI Standards, and the reporting is based on a materiality analysis.

### 2020 Status and targets

<table>
<thead>
<tr>
<th>Safety</th>
<th>Social responsibility</th>
<th>Biodiversity</th>
</tr>
</thead>
<tbody>
<tr>
<td>TRI rate 2.7 FY 2020</td>
<td></td>
<td>On track 2020</td>
</tr>
</tbody>
</table>

- **Ambition:** Zero fatalities and injury free work environment
- **2030 target:** Contribute to education and skills for 500,000 people
- **Target:** rehabilitate available mined areas within two hydrological cycles

<table>
<thead>
<tr>
<th>Climate</th>
<th>Business integrity</th>
<th>Greener products</th>
<th>Environment</th>
</tr>
</thead>
<tbody>
<tr>
<td>GHG emissions -9% compared to strategy baseline</td>
<td>76% Integrity culture index</td>
<td>16.000 mt CIRCAL produced FY 2020</td>
<td>Tailings dry backfill methodology developed and tested</td>
</tr>
</tbody>
</table>

| | 2030 target: 30% reduction in GHG emissions | Ambition: high employee perception of a culture of business integrity | combined 2020/21 target: 65,000 mt in total | 2030 target: addressing the industry’s key environmental challenges |

---

1) This is known as the 1:1 target
2) Baseline emissions 13.3 million metric tonnes CO₂ equivalents and includes direct and indirect emissions (scope 1 and 2).
3) About half of the reduction were due to improved performance, especially at the Alunorte refinery. The remaining reduction was due to significant reduced production across Hydro because of the Covid-19 pandemic.

* Targets may be subject to revision following the Hydro Rolling transaction.