

Strategy, goals and performance management system

Strategy

Market conditions and structures

Market conditions in the energy sector have been undergoing a period of profound change for a number of years. The desire to achieve autonomy and generate energy in a decentralised manner, as well as falling energy consumption due to improved energy efficiency, are leading to new patterns of demand amongst customers and new patterns of consumption. An increase in price and cost awareness and a continued strong focus on sustainability support this development. Cities and communities are also playing a role in this change.

The trend towards decentralisation is benefiting from regulatory funding mechanisms and from technological advances that have led to a sharp decline in the costs associated with decentralised energy generation, particularly with regard to photovoltaic power plants, but also in the area of wind power plants and combined heat and power plants. The role of centralised electricity generation is fundamentally changing as a result and is leading to considerably fewer operating hours in power plants. Nuclear power generation will be phased out by 2022, with plants being successively and safely decommissioned and dismantled.

As a consequence, energy supply companies require new business models and the revitalisation of their corporate cultures (p. 13f.). For the provision of services, dialogue-oriented communication, digitalisation and increased cooperation with partners are, for example, becoming key areas of focus for energy supply companies.

According to our long-term assessment of the individual market sectors, the total comprehensive income of the energy industry in Germany will increase slightly in nominal terms up to 2020. However, the aforementioned trends will result in significant shifts in earnings between the individual stages of the value chain. The contribution to earnings of all thermal generation in Germany will fall considerably up to 2020. The growth in earnings from renewable energies (especially onshore/offshore wind and photovoltaic) and grids – particularly as a result of the major expansion of the transmission grids – will offset this development. The sales business for standard products is under pressure, which is particularly due to the continued increase in own energy generation and energy efficiency. However, the overall sales market is anticipated to grow slightly up to 2020 due to the increasing importance of new and digital business models, as well as new market opportunities – such as in the area of electromobility.

Strategy process

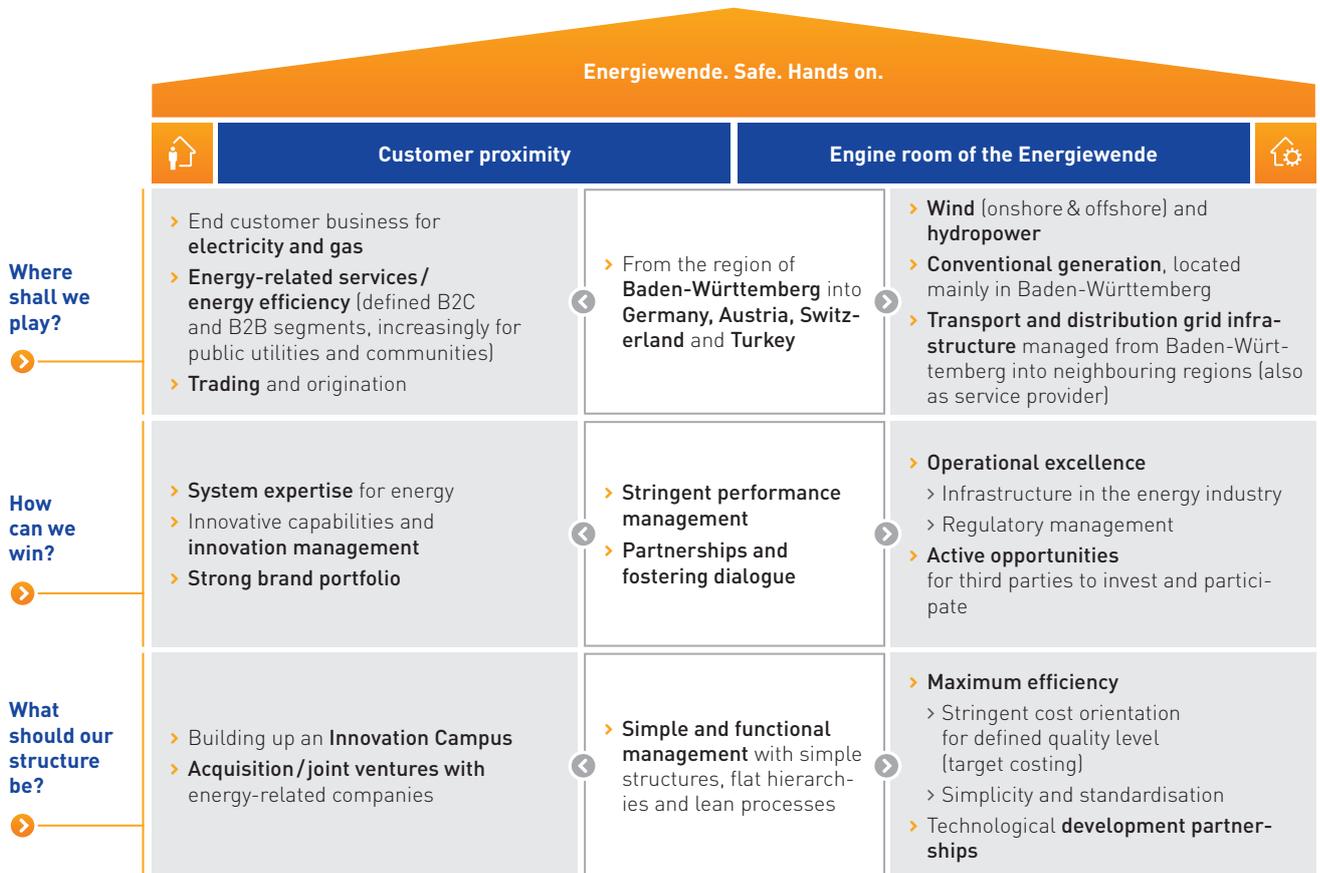
The development of strategy at EnBW is governed by a uniform and structured process. This begins with our vision which is guided by the principle “Energiewende. Safe. Hands on.” to describe our long-term objective. The Group strategy describes our strategic positioning and how we differentiate ourselves from our competitors. Sustainability is also an integral component of our Group strategy so that we can guarantee the creation of economic, ecological and social value for our stakeholders. We shape the composition and strategic development of our business portfolio through our portfolio strategy. Our strategic goals are then defined and operationalised in a final step through the design of our business, investment and functional strategies.

Strategy process



Guiding principle and Group strategy

EnBW 2020 strategy



The EnBW Group strategy developed in accordance with our guiding principle encompasses two operative and complementary models encapsulated in the EnBW Strategy House:

Customer proximity: The EnBW 2020 strategy places the focus on customers to an even greater degree. Targeted innovation management and short development times for new products and services will become key components. Cooperation with municipal utilities and local authorities should be expanded, primarily on the basis of partnership cooperation models. EnBW aims to gain an advantage over its competitors through the development of system and complete solutions for specific customer segments and a strong brand portfolio. An Innovation Campus supports the rapid development of forward-looking products. It is characterised by its focus on market proximity, bringing together the necessary expertise from the areas of research and development right through to sales and also by its entrepreneurial thinking. In the area of energy-related services, in particular, selective company acquisitions will complement existing expertise and round off the range of products and services offered (p. 39 ff.).

Engine room of the Energiewende: Safety, simplicity and flexibility are crucial when it comes to operating system-relevant infrastructure. EnBW relies on operational excellence and a strict focus on efficiency and cost-orientation to achieve defined

standards and levels of quality. Partnerships formed in the area of technological development serve to minimise costs and risks. In addition, EnBW actively offers the opportunity to invest in grids and power plants, especially to local authorities. In the “Engine room of the Energiewende”, EnBW uses its expertise to guarantee a reliable supply of energy – which also needs to be ensured during the transformation of the energy landscape.

Portfolio strategy

Restructuring the business portfolio

EnBW aims to more than double the share of its generation capacity accounted for by renewable energies from 19% (based on the reference year of 2012) to more than 40% in 2020. The capacities of our onshore wind farms will be increased significantly in the target markets of Germany and Turkey. Offshore wind power represents a further opportunity for growth. By investing extensively in grid expansion, we will be making a substantial contribution to the infrastructure required by the energy system and thus to the security of supply.

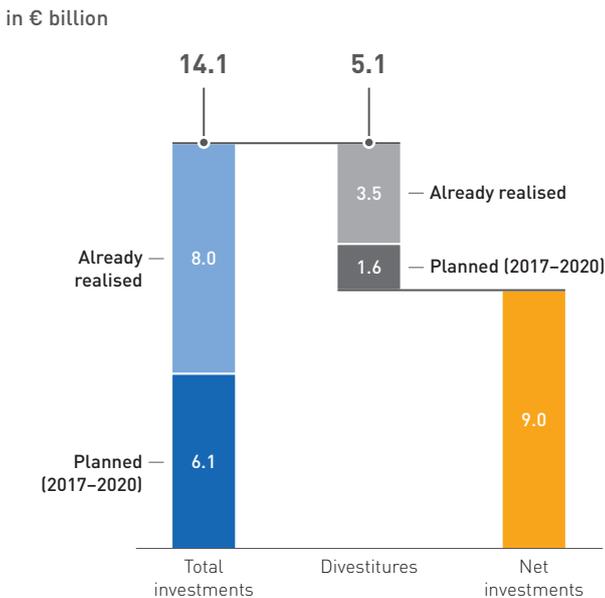
Innovative products and services will form another important pillar of the company’s business. By 2020, a significant share of our earnings – the target value for adjusted EBITDA is between €2.3 and €2.5 billion – is to be generated through strategic initiatives. At the same time, the overall share of

adjusted EBITDA accounted for by the regulated grid business and renewable energies will increase from around 40% (based on the reference year of 2012) to around 70% in 2020. This will improve the risk-return profile of EnBW.

Extensive investments and divestitures

EnBW intends to invest €14.1 billion in total by 2020 (based on the reference year of 2012). In this context, the focus will be placed on expanding renewable energies on an industrial scale. Moreover, we will also concentrate on the expansion and upgrading of our transmission and distribution grids right through to so-called  smart grids. Beyond our core market of Baden-Württemberg, we will be focusing our investment activities on Germany, Switzerland, the Czech Republic and Turkey. In order to obtain the financial headroom required for such extensive investments, we have significantly extended our divestiture programme – involving conventional divestitures, cash inflow from participation models, the disposal of assets and subsidies – with our EnBW 2020 strategy to around €5.1 billion (based on the reference year of 2012).

Investments and divestitures as part of the expansion of the portfolio



You can find further information on this subject in the “Forecast” on  page 76.

Corporate strategy outlook

Expansion of the gas business

As part of the restructuring of shareholdings with EWE Aktiengesellschaft, Oldenburg, EnBW divested itself of a 20% shareholding in EWE in 2016. EWE-Verband has also undertaken to acquire the remaining 6% of EWE’s stock from EnBW by 2019. In return, EnBW acquired a 74.21% shareholding in VNG-Verbundnetz Gas Aktiengesellschaft, Leipzig, in 2016. Following the planned full consolidation of VNG during the course of 2017, EnBW will double its gas business and become the third-largest gas supplier on the German market. The

acquisition of VNG represents an important step in the restructuring and further development of EnBW, both strategically and economically.

EnBW 2020 is well on track

As an integrated energy supply company, EnBW is rigorously and confidently implementing its 2020 strategy. The following is clear at the half way stage of the strategy period 2013 to 2020: The improvements in efficiency and the growth initiatives designed to place the company on new foundations ready for the future have been implemented to a significant extent or are well on track. If there is no new and unexpected massive deterioration in the general conditions, EnBW will achieve its goals for 2020 and thus reach one of the most important milestones in the history of the company.

Next phase of the Energiewende

The climate conferences in Paris and Marrakesh have set clear goals for global decarbonisation. The Energiewende has become an irreversible global process. Digitalisation and decentralisation are becoming the decisive drivers of the further development of the energy markets. In this phase of the Energiewende, it is the market, customers and technology that are leading the way. The pace of change on the market is increasing significantly, while new competitors are offering inexpensive and creative solutions and products. In addition, there are trends such as urbanisation, digitalisation and networking. At the same time, customers are becoming more demanding, expect individual solutions and are themselves becoming electricity producers to an ever greater extent. Moreover, their requirements for reliability and safety remain high. Solar technology is being increasingly combined with storage technologies in private households. Digital intelligence is networking the supply of electricity, gas and heat right through to charging solutions for electric cars to create an autonomous supply of energy. Electricity and gas consumers are becoming independent energy producers and energy managers. Private households are forming communities that generate, exchange and trade energy, and are thus becoming virtual power plants. Whole sectors of the economy are becoming networked together. Previously separate and individual systems and infrastructures are converging through digitalisation to form one interactive complete system. The most important prerequisite is a reliable, safe, sustainable and user-friendly operation of the infrastructure. This is where EnBW sees its future role.

An infrastructure partner with digital system competence

The digital convergence of individual energy systems and infrastructure requires the ability to safely control, operate and further develop these systems both individually and as a whole. Energy companies will become competent and reliable partners who handle these tasks for customers, citizens and local authorities. As a result of its decades of core expertise, EnBW has good prospects for assuming a central role as an infrastructure partner in the future energy world. After 2020, EnBW will focus on growth and innovations for the markets of the future, set its sights on new markets and set new priorities.

Goals and performance management system

We will safeguard the implementation of our 2020 strategy by means of a holistic goal and performance management system. This system reflects the overall performance of the company and strengthens integrated thinking within EnBW. At the same time, it underpins the comprehensive and transparent focus on performance and stakeholders within our company.

Performance management system

Since 2013, corporate management has been continually expanded through the addition of non-financial and strategic goals to now also encompass the strategy, customers and society, employees and environment dimensions as well as the finance goal dimension. The centrepiece of this integrated corporate management is the performance management system (PMS). As of 2015, the PMS incorporates all tools used in strategic and operational management. The financial and non-financial Group goals have been broken down into consistent target agreements at all management levels since 2015. The quarterly performance reviews conducted at a Board of Management level introduced in 2013 were revised in 2015 and have since included operative performance indicators that will promote the achievement of targets for the financial and non-financial key performance indicators. In 2016, this concept was fully implemented. In terms of external communication, the PMS feeds into the integrated reporting of the financial and non-financial performance of EnBW based on the reporting framework of the International Integrated Reporting Council (IIRC). This Integrated Annual Report 2016 incorporates the financial and non-financial aspects of our business activities.

TOP Further development of the key performance indicators

EnBW has up to now managed to retain its “A” ratings using the **E** dynamic leverage ratio, measured as the ratio of adjusted **E** net debt to **E** adjusted EBITDA with a target in 2020 of < 3.3 years. As a result of a non-cash-relevant increase in the pension and nuclear provisions – due primarily to the current low interest rate – and also the impact for the law of reorganising responsibility for nuclear waste management, net debt has increased by several billion euros since 2011. These effects demonstrate that the dynamic leverage ratio is only suitable as a controlling indicator to a limited extent in the current market environment. The planned restructuring of the Group should be implemented independently of non-cash-relevant fluctuations in long-term provisions.

Therefore, EnBW will utilise the **E** internal financing capability in future as a key performance indicator. This describes the ratio between **E** retained cash flow and cash-relevant **E** net investment. This new control mechanism will enable EnBW to retain its financial discipline independently of interest rate-related volatility. The goal is a solid **E** investment-grade rating.

The successful growth of the business as an energy company not only requires a strong market position and a broad customer base but, above all, in view of the radical changes to the energy landscape, also social acceptance. EnBW has thus expanded its previously reported key performance indicator Brand Attractiveness Index from the 2016 reporting period into a Reputation Index. This index reaches above and beyond the customers goal dimension and reflects a diverse range of other activities, influencing factors and assessments from a variety of stakeholder groups. Accordingly, the customers goal dimension is also being broadened to become the customers and society goal dimension. To ensure comparability in the reporting, we will also continue to publish the Brand Attractiveness Index for the core brands of EnBW and Yello in future as an additional performance indicator (**L** p. 64).

EnBW already clearly committed itself to the Energiewende in 2013 with the 2020 strategy. The central focus here in the medium and long-term is low CO₂ or zero emission electricity generation. The EnBW business model is aligned to the national and international goals for climate protection, such as those defined in the Paris Agreement (**L** p. 44). Alongside a focus on increasing the proportion of renewable energies, which has already been a key performance indicator in the environment goal dimension for managing the company for many years, the inclusion of the new key performance indicator **E** CO₂ intensity reflects the special importance of climate change as a social, political and also economic challenge.

TOP Target values for the key performance indicators

The key performance indicators enable us to measure the degree to which goals are achieved and to manage our company. Through the realignment of EnBW (**L** p. 13f.) towards increased renewable energies, the grid business and business focussing on “Customer proximity” – with clearly defined and quantitative targets for 2020 (based on the reference year of 2012) – we will become the first point of contact for energy issues and ensure the continued competitiveness of EnBW through convincing products, a return to an increasingly advantageous risk-return profile and even stronger regional anchoring.

TOP Financial and non-financial key performance indicators and targets

Goal	Key performance indicator	2016	Target in 2020	
Finance goal dimension				
Secure profitability	Adjusted EBITDA in € billion	1.9	2.3–2.5	The operating result is to return to the average level achieved before the Energiewende. The total regulated business (Grids and Renewable Energies segments) together contributes around 70% to this result.
High level of financial discipline	Internal financing capability in %	72.1	≥ 100	The level of net financial liabilities is controlled by limiting net investment to the level of retained cash flow. The Group can thus finance its own restructuring internally.
Raise the value of the Group	ROCE in %	7.8	8.5–11	Return on capital employed (ROCE) is higher than the cost of capital. EnBW is creating value for its stakeholders.
 Financial key performance indicators > pages 52 and 58 ff.  Expected trends in financial key performance indicators > page 77  Report on opportunities and risks > page 80 ff.				
Strategy goal dimension¹				
Share of result from "Customer proximity"/Sales	Share of overall adjusted EBITDA in € billion/in %	0.2/13	0.4/15	The operating result for the Sales segment doubles from €0.2 billion (reference year: 2012) to €0.4 billion in 2020 and represents around 15% of the Group operating result. Innovations make this possible.
Share of result from Grids	Share of overall adjusted EBITDA in € billion/in %	1.0/52	1.0/40	The operating result for the Grids segment increases by 25% from €0.8 billion (reference year: 2012) to €1.0 billion in 2020 and represents around 40% of the Group operating result. The share accounted for by the stable and regulated business is expanding.
Share of result from Renewable Energies	Share of overall adjusted EBITDA in € billion/in %	0.3/15	0.7/30	The operating result for the Renewable Energies segment increases by 250% from €0.2 billion (reference year: 2012) to €0.7 billion in 2020 and represents around 30% of the Group operating result. EnBW is more sustainable.
Share of result from Generation and Trading	Share of overall adjusted EBITDA in € billion/in %	0.3/17	0.3/15	The operating result for the Generation and Trading segment falls by 80% from €1.2 billion (reference year: 2012) to €0.3 billion in 2020 due to changed framework conditions and only represents around 15% of the Group operating result.
 Strategic key performance indicators > page 52  Expected trends in strategic key performance indicators > page 77  Report on opportunities and risks > page 80 ff.				

Goal	Key performance indicator	2016	Target in 2020	
Customers and society goal dimension				
Reputation	Reputation Index	50.0	55.4	In parallel with the restructuring of the business model, EnBW aims to continuously improve its reputation.
Customer proximity	EnBW/Yello Customer Satisfaction Index	132/150	> 136/ > 159	EnBW and Yello customers are satisfied customers with a high level of customer loyalty. EnBW and Yello are organisations strongly oriented towards customers and meet the needs and wishes of their customers through tailored solutions and products.
Supply reliability	SAIDI (electricity) in min/year	16	< 25	EnBW regards the maintenance of supply quality to its customers as its chief priority. The high degree of supply reliability in the grid area operated by EnBW is based on comprehensive investment in grids and plants and our abundant system expertise.
 Non-financial key performance indicators > page 63 f.		Expected trends in the customers and society goal dimension > page 78		Report on opportunities and risks > page 80 ff.
Employees goal dimension				
Employee commitment	Employee Commitment Index (ECI) ²	59	65	The commitment of our employees to EnBW is very strong and there is faith in the future viability of the company.
Occupational safety	LTIF ²	3.9	≤ previous year	The number of accidents at work and the resulting days of absence remains stable or is falling.
 Key non-financial performance indicators > page 64 ff.		Expected trends in the employees goal dimension > page 78 f.		Report on opportunities and risks > page 80 ff.
Environment goal dimension				
Expand Renewable Energies (RE)	Installed output of RE in GW and the share of the generation capacity accounted for by RE in %	3.1/23.1	5.0/ > 40	The share of the generation capacity accounted for by renewable energies has doubled compared with 2012. Onshore and offshore wind power and hydropower are at the forefront of this development.
Climate protection	CO ₂ intensity in g/kWh	577	-15% to -20%	EnBW actively contributes to climate protection by successively reducing the CO ₂ intensity of its own generation of electricity (excluding nuclear power) by 15 to 20% by 2020 compared to 606 g/kWh in the reference year 2015.
 Key non-financial performance indicators > page 67 ff.		Expected trends in the environment goal dimension > page 79		Report on opportunities and risks > page 80 ff.

¹ Other/Consolidation accounts for €0.1 billion/+3% of the overall adjusted EBITDA.

² Variations in the group of consolidated companies; see also the definition of key performance indicators on page 28.

TOP Definition of key performance indicators

The financial and strategic key performance indicators within the PMS are the **adjusted EBITDA**, the share of the adjusted EBITDA accounted for by each business segment, the **internal financing capability** and **ROCE**.

The **adjusted EBITDA** refers to the earnings adjusted for non-operating effects before the investment and financial results, income taxes and the expenses for depreciation and amortisation (p. 51 and 77). Adjusted EBITDA is a key performance indicator for the finance goal dimension. The key performance indicators for the strategy goal dimension, which refer to the share of adjusted EBITDA accounted for by each business segment, are derived directly from it. The key performance indicator **internal financing capability** is defined as the **retained cash flow** in relation to the cash-relevant **net investment** and represents the most significant performance indicator for the Group's ability to finance its activities internally (p. 58f. and 78). The retained cash flow (after covering ongoing costs and dividend payments) is available to the Group for net investment without the need to raise additional outside capital. The **ROCE** (return on capital employed) is the ratio of **adjusted EBIT** including the adjusted investment result to the average capital employed and forms the basis for determining the value added, reflecting the development of the company's value from a financial point of view (p. 62f. and 78).

In addition to the financial key performance indicators, the PMS also includes non-financial key performance indicators.

The customers and society goal dimension comprises the Reputation Index, the Customer Satisfaction Index and the SAIDI (System Average Interruption Duration Index) (p. 63 and 78).

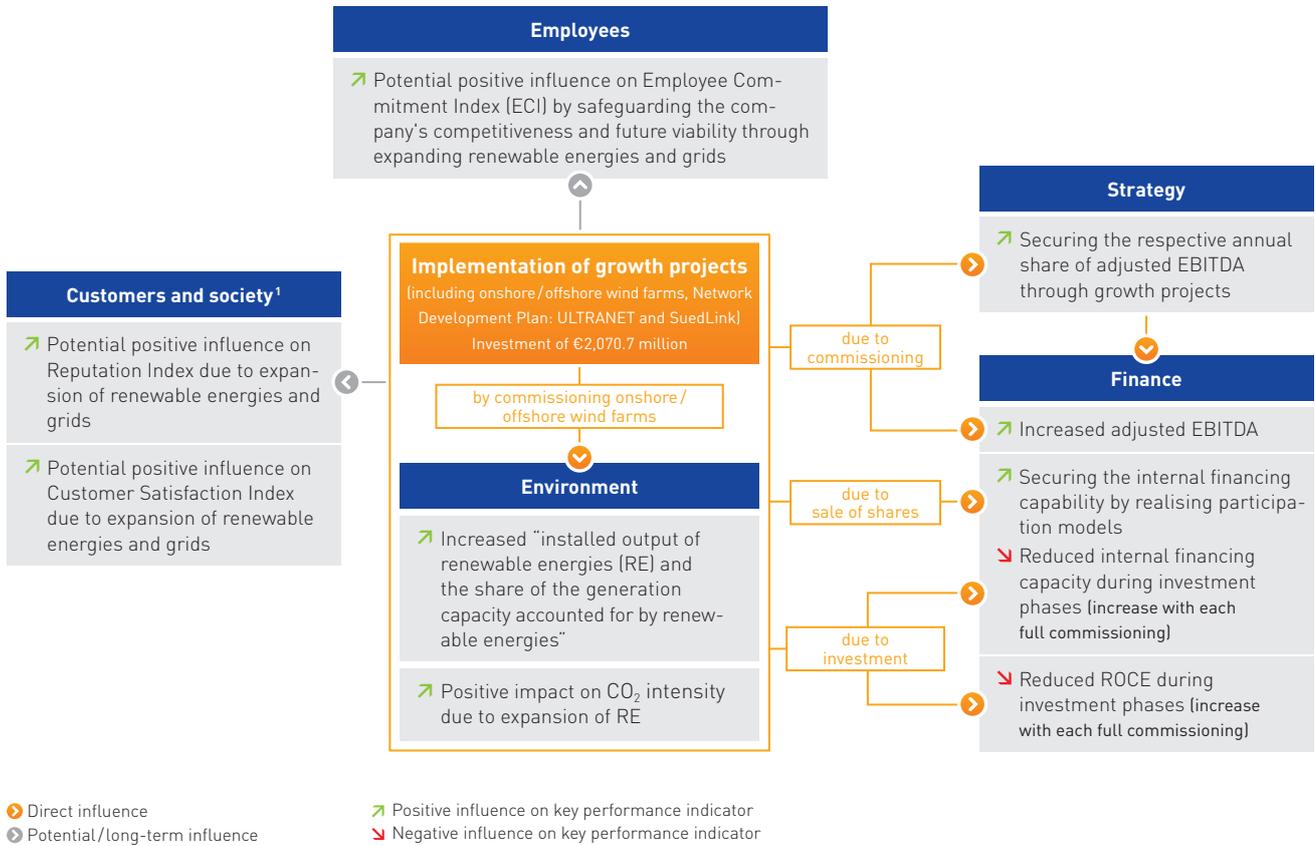
In order to calculate the **Reputation Index**, a total of around 5,000 people – from the stakeholder groups relevant for the EnBW brand of customers, the wider public, industrial companies, opinion leaders and investors – were asked about their attitudes to the EnBW brand by an external market research institute. Results were collected for each stakeholder group about the distinctiveness of the brand and the assessment of the competence of and emotional attitude towards the EnBW brand. These are merged together to form a Reputation Index. The individual reputation indices for each stakeholder group are weighted equally to form a consolidated and reported Reputation Index. The key performance indicator **Customer Satisfaction Index** comprises an integrated analysis of the average satisfaction of private end consumers of electricity over the year, which is directly linked to customer loyalty. It is compiled and derived from customer surveys carried out by an external provider. This key indicator

is compiled for the Group's two core brands of EnBW and Yello. **SAIDI** serves as the key performance indicator of supply reliability. It expresses the average length of supply interruption in the electricity distribution grid experienced annually by each connected customer. SAIDI includes all unscheduled downtimes with interruptions to supply lasting more than three minutes for end consumers. The calculation methodology is based on regulations issued by the VDE (German Association for Electrical, Electronic & Information Technologies) for reporting supply interruptions in electricity grids.

The Employee Commitment Index (ECI) and LTIF (Lost Time Injury Frequency) are utilised as performance indicators in the employees goal dimension (p. 64f. and 78 f.). The **ECI** expresses the degree to which employees are committed to EnBW. It is compiled using employee surveys and is based on standardised questions that address the degree to which employees identify with their company, including: satisfaction with their employer-employee relationship, attractiveness of the employer, identification with the company, motivational climate, competitiveness and future viability. The ECI is compiled every two to three years for those companies controlled by the Group (except ITOs) as part of a full employee survey – as was also the case in 2016. Representative random sample surveys are completed in the periods between the full surveys. The **LTIF** is calculated on the basis of LTI (Lost Time Injuries) which denotes the number of accidents during working hours which have occurred exclusively because of a work assignment from the company and result in at least one day of absence. LTIF indicates how many LTIs have occurred per one million working hours performed. This key indicator takes all employees at those companies controlled by the Group into account, except external agency workers and contractors.

The key performance indicators in the environment goal dimension of **installed output of renewable energies (RE)** and **the share of the generation capacity accounted for by RE** have now been supplemented by **CO₂ intensity** (p. 67f. and 79). The first are measures of the expansion of renewable energies and refer to the installed output of the power plants and not to their weather-dependent contribution to electricity generation. The calculation basis for the key performance indicator CO₂ intensity is the emissions of CO₂ from own generation of electricity for the Group, as well as the volume of electricity generated by the Group without the contribution made by the nuclear power plants. This performance indicator is calculated as the ratio between the emissions and the generated volume of electricity and thus specifically describes the amount of CO₂ released per kilowatt hour. By discounting the electricity generated by nuclear power plants, the performance indicator will not be influenced by the phasing out of nuclear energy in the coming years.

Interdependencies between key performance indicators using the implementation of growth projects as an example



¹ Especially in relation to the construction of onshore wind farms, we also anticipate a potential negative influence on the Reputation Index due to the risk of the rejection of individual projects in the local vicinity. However, this type of localised risk is more than compensated for by the overall potential positive influence on the Reputation Index.

Interdependencies between key performance indicators using efficiency measures as an example

