

Combined management report as at December 31, 2014

This management report is a combined report on STEAG GmbH and the STEAG Group (STEAG GmbH and its subsidiaries). Business development at STEAG GmbH is reported in a separate chapter. The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) as applicable in the EU, while the individual financial statements have been drawn up in accordance with the provisions of the German Commercial Code (HGB).

Basic information on the STEAG Group

Business activities and corporate structure

Business activities

The STEAG Group operates internationally, providing integrated solutions for its customers in the areas of power and heat generation, and technical services. Its core competencies include the planning, construction and operation of large power plants and distributed facilities, and asset-based power trading. The Group's power and heat generating capacities are based on special fuels, fossil fuels and, increasingly, renewable energy sources.

Conventional energy generation

As one of Germany's largest electricity producers, the STEAG Group has a total installed capacity of 10,150 megawatts (MW), including 8,200 MW in Germany.

In Germany, it operates power plants at ten sites and has more than 200 distributed facilities to generate energy from renewable resources and to serve industry and supply heat.

Outside of Germany, the Group has its own power plants and also works closely with local partners.

The STEAG Group operates power plants in Colombia, the Philippines and Turkey. The power plant in Iskenderun (Turkey) is the Group's largest foreign investment with a capacity of 1,320 MW.

Renewable energies

Renewable energy sources are increasingly important in the STEAG Group's portfolio.

The Ullersdorf wind farm in Germany came into service in November with an installed capacity of 43.2 MW. The Group is also becoming established as a renewable energy provider outside Germany: In 2014 it started operation of the Crucea North wind farm in Romania with an installed capacity of 108 MW.

A competent trading partner

Based on many years of experience in the trading of power, coal and CO₂, the STEAG Group has a broad portfolio of products and services, and extensive expertise in trading. Today, the STEAG Group is one of Germany's leaders in the import and marketing of hard coal. It imports hard coal from the major producing nations for supply to STEAG power plants and third parties.

A wide range of services

Over the years the STEAG Group has accrued great expertise in modernizing power plants and is now regarded as one of the leading providers of solutions for customized energy supply that is both environment-friendly and profitable.

As well as being a pioneer in efficient technologies for power generation from hard coal, which contribute to the conservation of resources, it is a specialist in optimization of the entire value chain associated with power plants. The STEAG Group also has a strong position in the re-use of waste materials from hard coal power plants.

In addition, in Germany the STEAG Group is a leader in the generation of electricity and heat from mine gas and heat from geothermal energy. It is also one of the largest suppliers of district heating and a contractor and operator of biomass heating plants in Germany.

Its competencies include professional engineering and operating solutions for every type of power generation. The engineers at its subsidiary STEAG Energy Services GmbH operate internationally, for example, in Brazil, Botswana, Romania, Turkey, Switzerland, the USA, and India. STEAG Energy Services (India) Pvt. Ltd. in India has over 1,000 employees, making it the foreign subsidiary with the largest workforce.

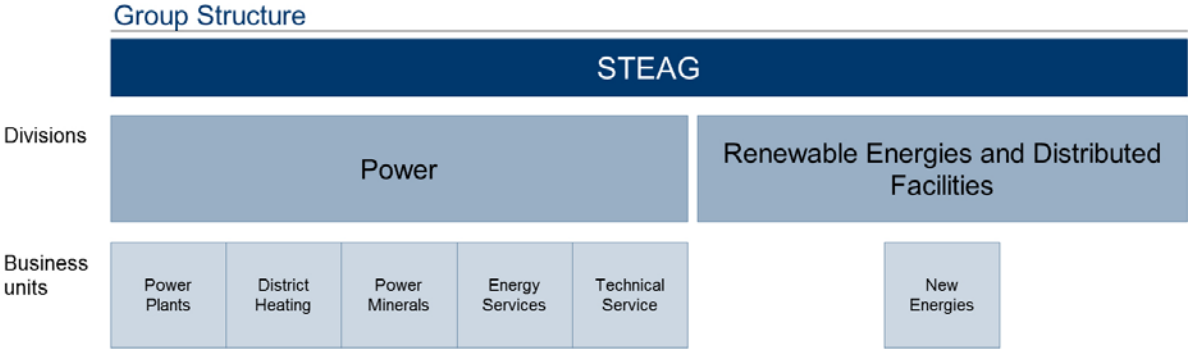
Ownership structure

As at December 31, 2014, STEAG GmbH was wholly owned by KSBG Kommunale Beteiligungsgesellschaft GmbH & Co. KG (KSBG KG).

At the start of 2014, KSBG KG held a 51.0 percent interest in STEAG GmbH. It acquired the remaining 49.0 percent stake in STEAG GmbH from RBV Verwaltungs-GmbH (RBV, a wholly owned subsidiary of Evonik Industries AG) effective September 5, 2014.

Integrated business model

STEAG GmbH, which is headquartered in Essen (Germany), is the parent company of the STEAG Group. It holds the shares in the Group's subsidiaries, either directly or indirectly. STEAG GmbH is responsible for strategic and operational management of the Group's divisions, i.e. the Power division (comprising the Power Plant, District Heating, Power Minerals, Energy Services and Technical Service business units), and the Renewable Energies and Distributed Facilities division (New Energies business unit). The structure reflects the STEAG Group's integrated business model.



In the Power division, national and international projects are the basis for high-quality technical solutions for power plants. In the Power Plant business unit, the Procurement & Optimization (P&O) department is responsible for marketing, while the Generation department is responsible for operating power plants.

In Germany, power generation is complemented by the activities of the District Heating business unit, which successfully markets the heat produced by co-generation plants.

The Power Minerals business unit markets waste materials from power plants profitably, primarily to the construction industry.

For decades, the engineers in STEAG's Energy Services business unit have been developing concepts for plants for conventional and renewable fuels. They design and build the plants and offer international services and IT solutions to optimize power plants.

The Technical Service business unit pools the service expertise gained over decades, especially in power plant maintenance and services for electricity grids.

The second division, Renewable Energies and Distributed Facilities, will become more important in the future. Activities associated with distributed energy generation (based on renewable energy sources and industrial and/or municipal supply concepts) are bundled in this division.

Organizational changes

In view of the increasing economic importance of energy policy decisions for the company, STEAG decided to establish an office in Berlin.

This was opened in March 2014. In the months since then it has improved the exchange of views and information with representatives of those responsible for federal policy, especially during the talks with the Federal Ministry for Economic Affairs and Energy (BMWi) on issues relating to the framework for the operating periods of coal-fired power plants.

In addition, the STEAG Group is continuously examining administrative workflows and processes. As a first step, the Group's planning process was optimized and restructured in 2014.

Significant contracts

STEAG GmbH and EnBW Energie Baden-Württemberg AG (EnBW) held constructive talks on the perspectives and interests of both companies at the Bexbach site. As a result, it was decided that STEAG GmbH would acquire EnBW's stake in the Bexbach power plant and all shares in Kraftwerk Bexbach Verwaltungsgesellschaft mbH. On January 1, 2015 STEAG GmbH acquired EnBW's shares in the Bexbach power plant in the Saarland region, which the two companies jointly commissioned in 1983.

This power plant is now wholly owned by the STEAG Group, which is therefore responsible for operating the plant, marketing the 780 MW installed capacity and procuring coal.

With effect from January 1, 2014, STEAG Energy Services GmbH took over the management of the 600 MW Morupule B hard coal power plant in Botswana . The state-owned energy utility Botswana Power Corporation (BPC) had only approached the STEAG Group with this request at the end of November 2013. Despite the short period, STEAG Energy Services GmbH realized the plant management concept on schedule, thereby making a substantial contribution to stabilizing energy supply in Botswana.

The Morupule power plant is located about 280 km north-east of the capital Gaborone and is of key significance for the country's power supply. In future, over 90 percent of BPC's power will be generated at the Moropule site. In the long term, operation of this power plant makes Botswana less dependent on power imports from South Africa.

Strategy

Strategic development

The STEAG Group stands for efficient and reliable energy generation - in Germany and abroad. Based on this, the strategy of the STEAG Group has three main objectives:

1. Place the business in Germany on a basis that is viable for the future
2. Realize profitable growth outside Germany
3. Significantly increase the proportion of renewable energies.

The STEAG Group's operating units and subsidiaries drive forward these objectives through five different focal areas and initiatives.

The first focal area, "optimizing existing power plants", principally aims to meet the objective of placing the business in Germany on a viable basis for the future. To achieve this, the STEAG Group focuses on continuous optimization of power plant processes and on increasing the technical and organizational flexibility of power plants to make its sites more profitable and extend their service life. In recent years, the Group has leveraged considerable technical scope for optimization, for example by reducing minimum loads, optimizing start-up and expanding the range of coals that can be used in the power plants. In parallel with the technical optimization, STEAG Technischer Service GmbH was set up to bundle maintenance expertise for internal and, increasingly, external customers.

To supplement the goal of maintaining existing business in Germany, the next initiative is "selective growth in Germany". The trend towards distributed energy generating facilities offers opportunities to expand business with municipal utilities and local authority partners, which have a strong local presence.

This also involves stepping up the use of renewable energy sources, especially onshore wind energy. Further development of co-generation and district heating, especially through the Rhine-Ruhr district heating line that is currently under development, is a very important part of this initiative. In addition, where relevant the STEAG Group will examine opportunities in the area of conventional power generation, which will be used for selective development of its domestic business if the overall assessment is positive.

The third focal area is "ongoing development of trading". The aims here are on the one hand to stabilize and drive forward business in Germany, and on the other hand to make progress in international growth. To achieve this, P&O will be stepping up marketing of renewable energies and distributed facilities. In this context, the STEAG Group's virtual power plant is an important milestone in ongoing development of the business in Germany. Further, internationalization of this unit should be successively extended, for example through cross-border trading. In this way, expertise in international energy markets can be strengthened and can provide key support for the development of international growth projects.

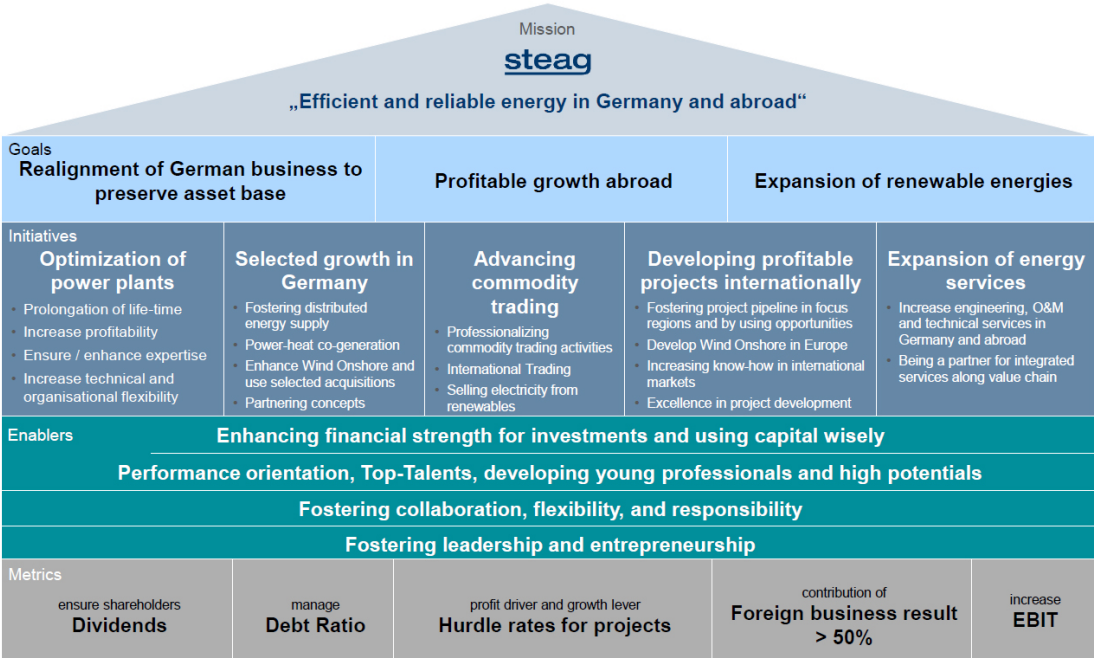
"Realizing profitable foreign projects as an independent power producer (IPP)" is the first focal area geared to foreign growth. This involves developing and realizing projects in countries such as Turkey and Indonesia and utilizing opportunities in other emerging markets. These countries have undergone substantial economic growth in recent years, accompanied by a significant rise in living standards. Both factors together increase the demand for energy. However, in most emerging markets the energy supply infrastructure is still inadequate. Smart, efficient and reliable energy supply concepts are therefore required. In the past, the STEAG Group has repeatedly proven that it is able to successfully implement this type of solution (examples being the projects in Colombia, Turkey and the Philippines). As well as developing conventional power plants, the STEAG Group is systematically extending its onshore wind portfolio in Europe, so international growth is accompanied by further diversification of its generating portfolio.

The last of the five initiatives relating to implementation of the strategic objective can be summarized as "extending services".

The STEAG Group understands this as extending its services in Germany and abroad, mainly through STEAG Energy Services GmbH, STEAG Technischer Service GmbH and STEAG Power Minerals GmbH. Other elements are extending municipal and industrial services through STEAG New Energies GmbH and strengthening internal services within the Group.

The STEAG Strategy House provides a clear and compact overview of the Group's strategy and focus.

The STEAG Strategy House



Research and development

Focus of research

The STEAG Group does not engage in basic research. Its research and development activities focus on technologies that it can use directly in its business. The main areas of interest are optimizing the operation of conventional power plants and wind energy installations. Great importance is attached to making existing power plants more flexible.

That includes lowering minimum loads and finding alternatives for the supply of start-up heat. Making conventional power plants more flexible is also the objective of two joint projects: the Competitive Load Following Power Plant (CoLoF-PP) and the "partner steam power plants" project.

Extending power storage technology is an important basis for the success of Germany's new energy policy. In recent years, the STEAG Group was successfully involved in "Lessy", a joint project at the power plant site in Fenne (Germany). Germany's first lithium-ion storage battery in this configuration was approved for use in grid stabilization by the operator of the transmission grid at the start of 2014. Storage systems of all types will gain in importance in the future. Further tests have therefore been carried out on them as part of the STEAG Group's research and development. Small-scale storage capacity of this type could be used both in conjunction with power plants and on a distributed basis. Depending on the site selected, a range of synergies could be utilized to optimize grid usage.

The STEAG Group will continue its research and development into storage technologies as an integrated energy producer that is open to new technologies. The Group is therefore driving forward the investigation of carbon capture technologies at its Herne and Lünen sites in Germany. In connection with this, a new power-to-fuel research project has been set up at the Lünen site to look at the conversion of carbon dioxide emissions into fuel. The goal is to develop options so that CO₂ can be used as a starting product in the chemical industry, for example, as a storage medium, thus obviating the need to store it separately.

Turning fly ash into a product optimized for use by the cement industry saves landfill capacity and reduces CO₂ emissions. Potential applications are therefore constantly being refined. One example is Photoment®: catalytic construction materials which, when applied to large areas, reduce pollutants through direct contact with their surface. Photoment® can also be used to improve air quality in polluted cities and ensure that surfaces remain clean and maintain their color for longer.

Biomass will also be a significant renewable source of energy in the future. As part of our research and development activities, we are looking into how small hybrid solutions and torrefaction plants can be driven forward.

We keep a constant eye on developments in the broad spectrum of "smart city issues" and pursue them where relevant.

Economic report

Economic background

General economic development

Global economic growth slowed significantly in summer 2014. As a result of the clear cooling down of economic momentum in the Eurozone and Japan, global industrial output only grew half as fast in the second and third quarters of 2014 as in the preceding two quarters. Growth rates remained robust, especially in the USA and UK, while in the emerging markets economic output actually gained pace. However, this could not offset the decline in the industrialized countries. Growth in gross domestic product (GDP) therefore slowed further to 2.7 percent in 2014 (2013: 3.3 percent)

China is still the main force driving global economic development. The Chinese economy grew by 7.4 percent in 2014, compared with 7.7 percent in 2013. Although the overall growth rate in the emerging markets has dropped (2014: 4.6 percent vs. 2013: 5.2 percent), it is still far higher than in the industrialized countries. In the industrialized countries, growth was relatively strong (2014: 1.7 percent vs. 2013: 1.3 percent). However, this was partly due to the easing of financial policy restrictions in most major industrialized countries.

The present low oil price will be an important support for cyclical trends over the coming year and will be countered by numerous structural problems in both the advanced economies and some major emerging markets such as Brazil and Argentina.

The German economy cooled down in the summer half-year but subsequently picked up considerably. The slowdown was mainly caused by the corporate sector's reluctance to invest in capital goods. This was compounded by the economic risks in the world and the Eurozone and by the German government's costly reform programs, which held back employment. Even favorable financing conditions could not generate any real impetus. However, real consumer spending increased and foreign trade also supported the overall economic performance. Further, it may be assumed that the sharp drop in the price of crude oil will continue to boost the overall economic development and strengthen purchasing power, especially of private households. Compared with the prior year, it can currently be assumed that economic growth rose considerably in Germany despite the weaker second half of the year (2014: 1.5 percent vs. 2013: 0.1 percent).

Energy consumption and energy generation¹

As a result of mild weather, energy consumption in Germany was 4.8 percent lower than in 2013 and therefore at the lowest level since German reunification. Consumption of renewable energies increased by 1.4 percent, so the proportion of renewables in the primary energy mix was 11.1 percent (prior year: 10.4 percent). Renewables accounted for 27.3 percent of gross power consumption, a year-on-year rise of 1.9 percentage points. By contrast, there was a considerable reduction in primary energy consumption of natural gas (down 14 percent), hard coal (down 7.9 percent), lignite (down 2.3 percent), mineral oil (down 1.3 percent) and nuclear power (down 0.4 percent). This had a positive effect on expected energy-related CO₂ emissions, which it is assumed declined by around 5 percent.

Power consumption

Overall consumption of electricity was around 3.8 percent lower in 2014 than in 2013. Power generation also declined slightly (2014: 610 TWh vs. 2013: 633 TWh). By contrast, the export surplus was almost constant year-on-year at minus 34.1 TWh (2013: minus 33.8 TWh).

Renewable energies accounted for around 157 TWh of total energy generated in Germany in 2014. That was 25.8 percent of power generated. Overall, renewable energies therefore accounted for a higher proportion of total energy generation in 2014 than in 2013. Moreover, for the first time they accounted for the highest proportion of total energy generated.

¹ All data on energy generation and consumption are provisional data from AG Energiebilanzen e.V. and the German water and energy industry association (BDEW).

By contrast, there was a further sharp drop in the use of natural gas to generate power (down 13 percent at 58.5 TWh). The reasons for this were increasing use of renewable energy sources and the continued discrepancy between coal and gas prices. Energy generation from hard coal declined by around 10 percent to approx. 110 TWh. As a result, the proportion of total energy generated from hard coal declined slightly to around 18 percent. Lignite accounted for 25.6 percent in 2014, making it the second largest source of energy by a narrow margin, although it was almost constant year-on-year at 156 TWh (down 4.9 TWh). Nuclear power generation remained relatively constant, dropping by only 0.4 percent to 96.9 TWh, and accounted for 15.9 percent of the total.

Development of energy prices

Prices on the international commodity markets were pushed down by the continued weakness of the global economy, which affected demand for energy, and by "unconventional" oil and gas production in the USA, the resumption of oil production in politically unstable countries such as Libya, Iran and Iraq, and the uncertainty relating to the development of demand in China, the USA and the principal countries affected by the European debt crisis. In addition, the strength of the US dollar led to lower oil and commodity prices. This, in turn, resulted in relatively low demand but high supply. Oil production in the USA was very high and the OPEC countries did not cut oil production to counter the market price trend.

The price of crude oil declined in 2014, especially in the second half of the year. North Sea Brent crude peaked at US\$ 115.0 per barrel (bbl) on June 19, 2014. By December 30, 2014 the price had halved to an all-time low of US\$ 57.51 per bbl. The average price of Brent crude was US\$ 99.68 per bbl in 2014, around US\$ 9 per bbl lower than in 2013. The downward trend in the price of hard coal observed in the previous year continued in 2014.

The API#2, which is a relevant spot price index for hard coal in Europe, registered an annual average of US\$ 75.25 per metric ton, and dropped to a low for the year in December, when the monthly average was US\$ 70.96 per metric ton. Overall, there is an oversupply of coal on the global market. The production of oil and gas from unconventional sources in the USA and slower growth in China are also holding back demand.

Backloading was introduced in 2014. This comprises the temporary withholding of 900 million CO₂ allowances in the third trading period. Overall, 400 million allowances were taken off the market in 2014.

Despite this, the absolute price of CO₂ allowances was only slightly higher than in 2013 and the sharp rise in the price of allowances predicted by experts has not yet materialized. Although there was temporarily a relatively sharp rise of around 35 percent in the average price in 2014, the absolute price remained comparatively low at €5.91 per metric ton.

The previous year's downward trend in power prices continued in 2014. The base price on the EEX power exchange was €32.78 per MWh in 2014, around 13 percent lower than in 2013 (€37.62 per MWh). The peak contract dropped by around 16 percent (average €41.00 per MWh in 2014 vs. €48.74 per MWh in 2013). As in the prior year, the continued expansion of renewable energies was responsible for the decline in electricity prices in 2014. Low prices for commodities and CO₂ allowances also had an impact.

Earnings position

Performance in 2014

As a result of the higher volume of energy traded by the Power division in 2014, sales were about 14 percent above the level predicted for the year. In 2014, overall earnings were considerably lower than in 2013, mainly due to one-off effects in 2014, which are outlined below.

Income statement for the STEAG Group

in €million	2014	2013
Sales	3,129.0	2,936.4
Change in inventories of finished goods	2.9	0.1
Other own work capitalized	1.6	4.5
Other operating income	302.8	346.3
Cost of materials	-2,242.9	-2,038.9
Personnel expenses	-405.6	-411.2
Depreciation, amortization and impairment losses	-204.1	-110.4
Other operating expenses	-408.2	-422.7
Income before the financial result and income taxes	175.5	304.1
Interest income	10.4	25.5
Interest expenses	-102.9	-64.0
Result from investments recognized at equity	-8.7	10.6
Other financial income	14.2	2.7
Financial result	-87.0	-25.2
Income before income taxes	88.5	278.9
Income taxes	-55.0	-80.0
Income after taxes	33.5	198.9
thereof attributable to		
Non-controlling interests	61.4	88.5
Shareholders of STEAG GmbH (net income)	-27.9	110.4

External sales by division

in €million	2014	2013	Change in %
Power	2,914.6	2,692.3	8.3
Renewable Energies and Distributed Facilities	214.4	244.1	-12.2
STEAG Group	3,129.0	2,936.4	6.6

Sales rose 6.6 percent to €3,129.0 million (prior year: €2,936.4 million), driven mainly by higher sales of energy following commercial start-up of the Walsum 10 power plant in December 2013, and by power trading.

Depreciation, amortization and impairment losses totaled €204.1 million (prior year: €110.4 million) and included depreciation and amortization of property, plant and equipment, intangible assets and investment property amounting to €139.1 million (prior year: €99.6 million).

The other operating expenses of €408.2 million (prior year: €422.7 million) include expenses from the valuation of derivatives (€161.1 million; prior year: €146.3 million), and exchange losses from the valuation of foreign currency items (€34.2 million; prior year: €17.6 million). These expenses are countered by income from the valuation of derivatives (€181.5 million; prior year: €159.2 million), and exchange losses from the valuation of foreign currency items (€19.2 million; prior year: €13.9 million).

Income before the financial result and income taxes decreased by €128.6 million to €175.5 million (prior year: €304.1 million). The interest result was minus €92.5 million, which was below the prior-year level of minus €38.5 million. Income before income taxes decreased from €278.9 million to €88.5 million. Income tax expense was €55.0 million (prior year: €80.0 million). Income after taxes was €33.5 million, which was below the prior-year level of €198.9 million.

The decline of €19.04 million in income before taxes was mainly caused by one-off factors in the reporting period.

Other operating income contained a write-up of €46.7 million (prior year: €91.9 million) on the Walsum 10 power plant project. Further, the prior-year figure included one-off income of €30.2 million from arbitration proceedings in Colombia. Personnel expenses were influenced principally by restructuring expenses of €29.9 million (prior year: €52.7 million). Depreciation, amortization and impairment losses contain several factors. Alongside impairment losses of €54.7 million on projects in Brazil and Spain, depreciation of €46.3 million for the Walsum 10 power plant was recognized for the first time for a full fiscal year (prior year: €4.4 million).

The reduction in the financial result was mainly due to a loss reported by a company in Spain in 2014 which is included at equity (loss of €15.2 million). The prior year figure contained one-off interest income from arbitration proceedings in Colombia (€13.1 million). In addition, following commissioning of the Walsum 10 power plant in December 2013, it was no longer possible to capitalize interest relating to the construction phase of this project (prior year: €21.4 million).

EBITDA and EBIT are used for internal management purposes and as indicators of the sustained earning power of the Group.

EBITDA (earnings before interest, taxes, depreciation and amortization) and EBIT (earnings before interest and taxes) are both earnings parameters after adjustment for extraordinary effects.

The 6.6 percent year-on-year improvement in EBITDA was principally attributable to improved earnings from the Power division. The EBITDA margin was level with the prior year at 12.5 percent.

EBIT was € 244.2 million, which was below the prior year figure of € 262.8 million. There was a slight drop of 1.1. percentage points in the EBIT margin to 7.8 percent.

STEAG Group: EBITDA and EBIT

in €million	2014	2013	Change in %
Sales	3,129.0	2,936.4	6.6
EBITDA	390.3	366.1	6.6
EBIT	244.2	262.8	-7.1
EBITDA margin in %	12.5%	12.5%	
EBIT margin in %	7.8%	8.9%	

Volume sales of energy

Total volume sales of energy from the Group's own facilities and those operated on behalf of its customers rose by 12.3 percent year-on-year to 58,464 GWh_e² (prior year: 52,083 GWh_e). Volume sales of heat by the Renewable Energies and Distributed Facilities division decreased by 6.7 percent to 1,963 GWh_{th} (prior year: 2,104 GWh_{th}), while the volume of power increased by 15.1 percent to 1,843 GWh_{el} (prior year: 1,600 GWh_{el}).

Full load operation hours were 5,034 h_{el} (prior year: 5.172 h_{el}) in the Power division and 4,305 h_{el} (prior year: 4.675 h_{el}) in the Renewable Energies and Distributed Facilities division.

² Energy sales in GWh_e comprise both electric and thermal energy; thermal energy has been converted into the equivalent amount of electric power.

Financial position

Financial risk management

The central objectives of STEAG's financial management are to safeguard the financial independence of the STEAG Group and limit refinancing risks.

STEAG GmbH manages borrowing, guarantees and sureties for Group companies centrally. It has flexible means of meeting capital requirements for day-to-day business, investment and the repayment of financial debt.

Another important objective is ensuring that the covenants relating to the bonded loans taken out by STEAG GmbH are met. The main covenants set out in the loan agreements comprise financial indicators to be calculated on the basis of the consolidated financial statements of STEAG GmbH, specifically the net debt ratio, which is the ratio of net debt to adjusted EBTIDA³.

Financing policy

STEAG GmbH provides funding for the companies in the STEAG Group and manages surplus liquidity on their behalf on market terms. To a limited extent, companies in the STEAG Group also borrow funds directly from banks and invest surplus liquidity with banks. In these cases, borrowing is secured by STEAG GmbH. The project companies' liability is secured through their cash flows and assets. No recourse to the parent company STEAG GmbH is possible. For example, non-recourse project financing has been agreed for the three foreign power plants in Iskenderun, Mindanao and Termopaipa.

In Germany, cash pooling is managed by STEAG GmbH. To minimize external borrowing, surplus liquidity in a cash pool at Group level is used to cover financing requirements at other companies in the Group.

Financing structure

As at December 31, 2014, STEAG had financial liabilities of €1,875.0 million (prior year: €1,219.0 million) and cash and cash equivalents of €686.9 million (prior year: €576.4 million).

³ As defined in the agreements on the bonded loans.

The main components of non-current financial liabilities are liabilities to banks, principally for the new bonded loans, the Walsum 10 power plant and the foreign power plant companies.

€ 86.0 million of the € 501.5 million (prior year: € 96.0 million of the € 400.2 million) in current financial liabilities relate to the liability to KSBG KG under the profit and loss transfer agreement, including the corresponding share of taxes.

The main components of financial assets are receivables from finance leases totaling € 599.7 million (prior year: € 654.9 million), including current receivables of € 150.8 million (prior year: € 119.2 million).

The STEAG Group has no further, off-balance-sheet financing instruments that could have a material impact on its present or future earnings, financial position, liquidity or other balance sheet items.

Liabilities are dominated for the first time by bonded loans amounting to € 400.0 million taken out by STEAG GmbH. The terms reflect the company's good credit standing. STEAG GmbH has also arranged other credit facilities with banks to increase the available liquidity. These currently exceed needs. Here too, positive creditworthiness ratings by the banks enabled the Group to obtain corresponding terms.

The STEAG Group's liquidity is secure.

Capital expenditure

The STEAG Group uses selective investment projects to maintain its good competitive position and expand into business activities and markets where it sees potential for sustained profitable growth and opportunities to generate appropriate returns. Every project undergoes detailed strategic and economic analyses, including sensitivity analyses and scenario analyses to reflect major risks.

Projects have to meet business-specific, risk-adjusted minimum return requirements, which include covering the cost of central functions.

Capital expenditure and financial investments

in €million	2014	2013	Change in %
Power	60.8	225.1	-73.0
Renewable Energies and Distributed Facilities	263.9	134.8	95.8
Other	156.1	3.9	3,902.6
STEAG Group	480.8	363.8	32.2

Capital expenditure totaled €480.8 million (prior year: €363.8 million), well above depreciation, which amounted to €139.1 million (prior year: €99.6 million). In 2014 capital expenditure for property, plant and equipment declined negligibly by 3.3 percent to €314.1 million (prior year: €324.9 million).

The lion's share of capital expenditure for property, plant and equipment (79.8 percent) was allocated to the Renewable Energies and Distributed Facilities division (€250.7 million; prior year: €108.2 million). The expenditure mainly related to the wind farms in Turkey, Romania, Germany and Poland. The biggest single project was the construction of the Crucea North wind farm in Romania. A further 18.6 percent of capital expenditure for property, plant and equipment was allocated to the Power division (€58.3 million; prior year: €212.9 million). Construction of the 790 MW hard coal power plant in Duisburg-Walsum (Germany) was completed in 2013. Regionally, the focus of capital expenditure in the STEAG Group was Germany, which accounted for 41.7 percent of the total (€131.0 million; prior year: €246.4 million).

The main financial investment in 2014 was the €150.0 million upstream loan to KSBG KG to finance the purchase price for the 49.0 percent stake in STEAG GmbH.

Cash flow

Cash flow statement for the STEAG Group (condensed version)

in €million	2014	2013
Cash flow from operating activities	392.7	472.2
Cash flow from investing activities	-579.1	-237.4
Cash flow from financing activities	272.2	-193.0
Changes in exchange rates and other changes in the value of cash and cash equivalents	24.7	-9.5
Cash and cash equivalents as of December 31	686.9	576.4

The cash flow from operating activities was €392.7 million, down from the prior-year level of €472.2 million. In 2013, the cash flow from operating activities was boosted mainly by an inflow of cash and cash equivalents from the utilization of a performance guarantee in connection with the Walsum 10 power plant project. A final decision on the underlying claim is still subject to arbitration proceedings.

The cash outflow for investing activities was €579.1 million, which was above the prior-year outflow of €237.4 million, mainly due to the higher cash outflows for property, plant and equipment and the upstream loan to KSBG KG. There was a cash inflow from financing activities of €272.2 million, an improvement compared with the outflow of €193.0 million in the prior year. This was principally due to higher borrowing, especially the bonded loans totaling €400.0 million taken out by STEAG GmbH.

Asset structure

Structure of the balance sheet

STEAG Group: Structure of the balance sheet

in € million	2014*	2013*	2014*	2013*	
Non-current assets	3.112,9 (58,1%)	2.800,0 (61,4%)	978,3 (18,3%)	1.256,3 (27,6%)	Equity
			2.930,6 (54,7%)	2.087,8 (45,8%)	Non-current liabilities
Current assets	2.244,4 (41,9%)	1.758,5 (38,6%)	1.448,4 (27,0%)	1.214,4 (26,6%)	Current liabilities
Balance sheet total	5.357,3	4.558,5	5.357,3	4.558,5	

* as at 31 December

Total assets increased by €798.8 million from €4,558.5 million as at December 31, 2013 to €5,357.3 million. Non-current assets increased by €312.9 million to €3,112.9 million (prior year: €2,800.0 million). This mainly resulted from capital expenditure for property, plant and equipment totaling €314.1 million (prior year: €324.9 million) and write-ups of €46.7 million (prior year: €91.9 million). This compared to depreciation and amortization of intangible assets, property, plant and equipment and financial investments totaling €139.1 million (prior year: €99.6 million) and impairment losses of €1.5 million (prior year: €2.5 million). Non-current assets accounted for 58.1 percent of total assets (prior year: 61.4 percent). Coverage of non-current assets by non-current capital was 125.6 percent (prior year: 119.4 percent). Current assets totaled €2,244.4 million (prior year: €1,758.5 million), an increase of €485.9 million compared with year-end 2013. Current assets exceeded current liabilities by 55.0 percent (prior year: 44.8 percent).

Equity contracted by €278.0 million to €978.3 million (prior year: €1,256.3 million).

The equity ratio declined from 27.6 percent to 18.3 percent, partly due to the increase in total assets. Non-current liabilities increased by € 842.8 million or 40.4 percent to € 2,930.6 million (prior year: € 2,087.8 million). This was attributable to a rise of € 469.0 million in liabilities to banks to € 1,145.6 million (prior year: € 676.6 million) and to an increase in provisions. Provisions for pensions rose by € 259.6 million to € 1,085.6 million (prior year: € 826.0 million), principally because the interest rate used to value pension provisions was lower than in the previous year. The € 34.7 million increase in other provisions to € 286.8 million (prior year: € 252.1 million) was mainly due to an increase of € 23.8 million in provisions for dismantling obligations and a rise of € 13.9 million in restructuring provisions. Current liabilities decreased by € 234.0 million to € 1,448.4 million (prior year: € 1,214.4 million). This was mainly because trade accounts payable increased by € 79.2 million to € 357.2 million (prior year: € 278.0 million). Further, current liabilities for derivatives increased by € 48.9 million to € 180.2 million (prior year: € 131.3 million). Similarly, liabilities to banks increased by € 52.7 million to € 200.6 million (prior year: € 147.9 million).

Despite the one-off effects outlined above, the STEAG Group posted a clearly positive performance. Selective investments have strengthened the Group's future earnings power, and financing and liquidity will remain on a stable basis in fiscal 2015.

Performance of STEAG GmbH

STEAG GmbH, which is headquartered in Essen (Germany), is the parent company of the STEAG Group. It holds the shares in the Group's subsidiaries, either directly or indirectly. STEAG GmbH is responsible for strategic and operational management of the Group's business activities. In addition, it is the largest single company in the Group with sales of €2,241.9 million and total assets of €3,142.9 million. The main subsidiaries in Germany are linked to it through control and profit and loss transfer agreements.

The annual financial statements of STEAG GmbH have been prepared in accordance with the accounting principles set out in the German Commercial Code (HGB).

Income statement for STEAG GmbH

in € million	2014	2013
Sales	2.241,9	2.141,9
Change in inventories, own work capitalized	-28,8	3,2
Other operating income	47,6	65,3
Cost of materials	-1.986,4	-1.880,5
Personnel expenses	-147,7	-165,1
Depreciation, amortization and write-downs	-18,1	-24,8
Other operating expenses	-143,6	-155,0
Financial result	106,0	124,2
Result of ordinary business activities	70,9	109,2
Extraordinary result	19,5	40,3
Taxes	-12,5	-17,5
Profit transfer	-77,9	-89,0
Net income/loss	0,0	43,0
Allocations to profit reserves	-	-43,0
Net profit	0,0	0,0

In 2014, STEAG GmbH's sales increased by € 100.0 million year-on-year to € 2,241.9 million (prior year: € 2,141.9 million). This was mainly due to a rise in the supply of energy and other media, while sales from coal trading declined.

In 2014 sales mainly comprised €1,461.9 million (prior year: €1,270.3 million) from the supply of energy, €573.8 million (prior year: €714.6 million) from the supply of coal and €93.6 million (prior year: €128.2 million) from operating and management fees. Revenues were generated with customers in Germany, other European countries, North America and Latin America.

Other operating income of €47.6 million (prior year: €65.3 million) mainly comprised income from the allocation of charges in the Group and reimbursement of costs, and income from the reversal of provisions.

The cost of materials increased year-on-year, mainly in line with the rise in sales revenues from energy supply and the volume and price-driven rise in the use of emission allowances.

The reduction in personnel expenses compared with the previous fiscal year was principally attributable to lower expenses for restructuring (€17.8 million; prior year: €30.1 million).

Other operating expenses were around the prior-year level at €143.6 million (prior year: €155.0 million). They mainly comprised transport costs and other administrative and selling expenses. Further they contained legal and consultancy fees, rental and lease payments and insurance premiums.

The financial result was €106.0 million in the reporting period (prior year: €124.2 million). This was mainly a result of income of €120.5 million from investments (prior year: €106.9 million) and net income from profit transfers of €32.4 million (prior year: €54.6 million). This was countered by net interest expense of €54.4 million (prior year: net expense of €36.5 million), mainly due to the interest on pension obligations and other non-current provisions and interest expense for non-current loans.

In the prior year, the extraordinary result was due to income effects relating to the Walsum 10 project, comprising income from the revaluation of financial assets and, as a counter-item, the increase in provisions for impending losses from the marketing of power. Risk provisioning was re-assessed in the reporting period, resulting in extraordinary income of €36.7 million.

Income from the write-up of the investment in STEAG Fernwärme GmbH amounting to €18.5 million increased the extraordinary result. The extraordinary result also includes write-downs of €10.0 million on STEAG Power Saar GmbH and €22 million on investments and current loans in connection with the withdrawal from the project in Brazil. Further, expenses for the adjustment of pension provisions included €3.7 million relating to revaluations in connection with the German Accounting Law Modernization Act (BilMoG). The remaining difference will be added to pension provisions in annual installments up to December 31, 2024 at the latest.

Tax expenses mainly comprised income taxes of €11.6 million (prior year: €16.4 million). The decline was due to a drop in corporation tax to €0.3 million (prior year: €4.4 million). In addition, the income taxes paid to KSBG as the main company in the fiscal entity included trade tax of €8.1 million (prior year: €7.0 million).

Income after taxes of €77.9 million for the reporting period was transferred to KSBG under the profit and loss transfer agreement.

Balance sheet for STEAG GmbH

Assets

in € million	Dec. 31, 2014	Dec. 31, 2013
Intangible assets	9,6	3,9
Property, plant and equipment	156,3	160,3
Financial assets	1.562,7	1.254,3
Non-current assets	1.728,6	1.418,5
Inventories	143,2	152,9
Receivables and other assets	742,1	643,7
Securities	19,9	51,6
Cash and cash equivalents	504,1	252,1
Current assets	1.409,3	1.100,3
Deferred items	5,0	2,2
Total assets	3.142,9	2.521,0

Equity and liabilities

in € million	Dec. 31, 2014	Dec. 31, 2013
Issued capital	128,0	128,0
Capital reserve	77,5	77,5
Profit reserves	272,8	272,8
Equity	478,3	478,3
Special items with reserve allowance	10,9	11,5
Special items for investment subsidies for property, plant and equipment	0,6	0,8
Provisions	796,7	794,2
Liabilities	1.849,7	1.228,7
Deferred items	6,7	7,5
Total equity and liabilities	3.142,9	2.521,0

Total assets of STEAG GmbH increased by €621.9 million to €3,142.9 million. Non-current assets increased by €310.1 million to €1,728.6 million (prior year: €1,418.5 million). Capital expenditure for property, plant and equipment and intangible assets was €19.9 million (prior year: €28.4 million). Capital expenditure thus exceeded depreciation and amortization, which came to €16.4 million. Additions to property, plant and equipment in 2014 mainly resulted from investments at power plant sites (€14.4 million; prior year: €24.5 million), which were basically completed by the reporting date. The principal reason for the increase in intangible assets was the introduction of an up-to-date version of SAP. The ratio of depreciation and amortization on property, plant and equipment and intangible assets (cumulative depreciation and amortization relative to the historical cost of acquisition or production) was 90.8 percent (prior year: 90.4 percent).

Changes in the capital reserve and the loss carryforward at STEAG Walsum 10 Kraftwerksbeteiligungsgesellschaft mbH resulted in a corresponding rise of €49.8 million in the carrying amount of this investment in the financial assets of STEAG GmbH. The other main capital measures were a capital contribution of €7.6 million to Steag 1. Beteiligungs-GmbH for the Arenales solar heating project in Spain and a capital contribution of €4.5 million to STEAG Rüzgar Süloglu Enerji Yaterim Üretim ve Ticaret A.S. (Turkey). As a result of a positive revaluation in connection with commissioning of the Walsum 10 power plant, a write-up of €19.3 million was recognized on the carrying amount of STEAG Walsum 10 Kraftwerksbeteiligungsgesellschaft mbH in 2014. In addition, the carrying amount of STEAG Fernwärme GmbH was written up by €18.5 million because the reason for the previous write-down no longer applied. The carrying amount of STEAG Power Saar GmbH was written down by a further €10.0 million. The shares in Canto do Buriti Bioeletricidade S.A. and Brasil Campo Grande Participacoes S.A. were derecognized in 2014, having been fully written off in the reporting period. The main changes in loans recognized under financial assets comprised the granting of a €150.0 million upstream loan to KSBG KG and a €70.2 million credit facility drawn by the subsidiary Crucea Wind Farm S.A. (Romania).

Working capital increased by €309.0 million to €1,409.3 million (prior year: €1,100.3 million). Inventories were around the prior-year level at €143.2 million (prior year: €152.9 million). The price and volume-driven increase of €23.5 million in emission allowances was more than offset by income of €28.9 million from support payments in connection with work in progress relating to the Walsum 10 project. Inventories therefore made up 4.6 percent of total assets (prior year: 6.1 percent). Receivables and other assets increased by €98.4 million to €742.1 million (prior year: €643.7 million).

This rise mainly resulted from a €38.3 million increase in receivables from profit and loss agreements with associates (€96.4 million; prior year: €58.1 million) and a sales-related increase of €41.9 million in trade accounts receivable (€192.7 million; prior year: €150.8 million). At the same time, cash and cash equivalents increased by €252.0 million in the reporting period (€504.1 million; prior year: €252.1 million), partly as a result of the bonded loans taken out.

There was no change in equity compared with the prior year. The equity ratio (excluding special items with a reserve allowance) is now 15.2 percent (prior year: 19.0 percent). Equity coverage of non-current assets is 27.7 percent (prior year: 33.37 percent).

Provisions were around the prior-year level at €796.7 million (prior year: €794.2 million). Provisions for pensions and other post-employment obligations increased by €24.0 million to €457.8 million (prior year: €433.8 million), mainly because of higher interest accruals. Pension provisions accounted for 57.5 percent of provisions (prior year: 54.6 percent). Other provisions to cover impending losses from the marketing of power from the Walsum 10 project in the future declined by €21.7 million to €107.2 million (prior year: €128.9 million). This includes a reversal to income of €17.4 million. A further decline in other provisions resulted from a change in the presentation of power purchased from third parties for which invoices had not been received. Contrary to the previous year, they are recognized in trade accounts payable and not in other provisions. Provisions for the obligation to surrender emission allowances and provisions for restructuring increased by €17.8 million to a total of €70.9 million (prior year: €58.9 million), mainly due to further additions.

Liabilities increased by €621.0 million to €1,849.7 million (prior year: €1,228.7 million). This was mainly because the company took out bonded loans totaling €400.0 million. In addition, liabilities to associates rose by €89.9 million to €1,063.3 million (prior year: €973.4 million), principally as a consequence of obligations to make capital contributions. Trade accounts payable increased by €85.6 million to €205.8 million (prior year: €120.2 million), mainly because of the change in presentation outlined above. In accordance with the profit and loss transfer agreement, a liability (including tax allocations) from KSBG KG of €86.0 million (prior year: €96.0 million) was recognized.

Non-financial performance indicators

Employees

Headcount

At the end of 2014, the STEAG Group had 6,419 employees, 11 percent of whom were female. The average age of the members of the worldwide workforce was 42. Almost 43 percent were employed outside Germany. The number of employees increased by nearly 400 year-on-year due to the following changes: The headcount at Energy Services increased as a result of the first-time consolidation of STEAG Energy Services Solar SLU (Spain) (+52) and STEAG Energy Services (Botswana) (pty) Limited (Botswana) (+247), and the expansion of business at STEAG Energy Services (India) Pvt. Ltd. (India) for the Vedanta project (+118). In the Renewable Energies and Distributed Facilities division, the headcount increased thanks to the addition of EC Gorlice Sp.z.o.o. (Poland) (+44). The increase in the number of administrative employees was mainly attributable to the transfer of commercial and technical apprentices (+105) and the Environment, Permits, Products unit (+12) from the Generating unit. There was a corresponding reduction in headcount in the Generating unit. The remaining change of 29 employees in administration was chiefly due to a reduction in the number of employees in connection with optimization of these functions.

Employees by division	Dec. 31, 2014	Dec. 31, 2013
Power	5,177	4,928
Renewable Energies and Distributed Facilities	820	772
Administration	422	334
STEAG Group	6,419	6,034

Apprenticeships

Apprenticeships at STEAG remain popular, as the constantly high number of applicants demonstrates. In December 2014, 256 apprentices were being trained in various occupations, giving a training ratio of 4.2 percent for the STEAG Group and 8.3 percent for STEAG GmbH. For years, the STEAG Group has attached great importance to attractive and high-quality training programs. In this way it assumes social responsibility and also secures skilled employees for the future.

Personnel development

The STEAG Group introduced a new personnel development program for upcoming managers at the end of 2014. There are programs for potentials and high potentials, depending on focus and experience.

High potentials are employees with a number of years work experience who have already gained some disciplinary or functional management experience. The "Executive Development Group" (EDG) offers them an opportunity to extend their networks, deepen their knowledge of the STEAG Group, and address the demands of a potential future management role in the Group.

Potentials normally have between three and five years' experience since completion of their vocational training or studies. The company enables them to broaden their competencies and establish networks within the Group through a "General Management Program" (GMP). They are supported by experienced in-house managers who act as mentors.

Alongside building and strengthening competencies, networking is also a focus for participants in the "Energy Development Program" (EDP). In 2014 a total of 43 employees from various departments in the STEAG Group completed the EDP. A further 16 embarked on this in-house development program for young and new STEAG employees in September 2014.

At STEAG Energy Services GmbH, the first international group completed the "Emotion" in-house development program in summer 2014. Emotion stands for "Energy in Motion" and has been a central element of employee development at STEAG Energy Services GmbH since 2006. Central aspects of this program include a focus on internationalization of project structures and networking across all companies at STEAG Energy Services GmbH.

Occupational health and safety and environmental protection

The number of accidents in the workplace increased by 8.9 percent from 45 to 49, while the number of commuting accidents dropped by 36.8 percent from 19 to 12. Special mention should be made of the Mindanao power plant, where there has not been an accident for eight years. Compania Electrica de Sochagota S.A.E.S.P. in Colombia has not had an accident for two years, and the RKB refinery power plant and Weiher power plant in Germany have both operated without any accidents for more than a year.

The introduction of certified occupational health and safety management systems that comply with the OHSAS 18001:2007 standard in Germany starting in 2008 has brought an improvement in all units. Successful recertification by the employer's liability insurance association at all sites and companies in recent years reflects the very high standard of occupational health and safety. To improve occupational safety, workplace safety measures at STEAG Technischer Service GmbH will be driven forward systematically in 2015 under the motto "Vision ZERO". Our coal-fired power plant companies outside Germany also achieved the same high, certified standard of occupational health and safety in 2014 and are audited regularly.

Our environmental protection management system and observance of the associated regulations were audited by the authorities in eleven site inspections in accordance with the Industrial Emissions Directive (IED). No shortcomings were identified at the power plants and heating power plants inspected.

Workplace health management

In light of demographic trends, workplace health management is a strategic basis for human resources work in the STEAG Group and will be a keystone of the upcoming change processes in the Group.

Various action areas for the sites have been identified on the basis of analyses and the results of a health survey. The findings will be used in systematic and targeted site-specific activities to secure the employability of staff at individual sites. A participatory approach involving employees and management development is the central element for a "healthy STEAG" from both a business and a human resources viewpoint.

In future, health issues will form an integral part of management development. As a first step, managers will learn how to better recognize situations of stress and overwork. As well as benefiting the health of the individual, this should avoid risks and secure the quality of work in the company.

Company suggestion program

In 2014, the STEAG Group was honored twice by the German Association for Business Administration. First place in the energy and energy supply sector went to the company suggestion program at STEAG GmbH. Second place was awarded to the ideas management system at STEAG Power Saar GmbH / STEAG New Energies GmbH. The STEAG Group has therefore been positioned among the leaders in this area for years, highlighting the fact that it is a learning organization.

The suggestions implemented in 2014 brought a measurable net benefit of €5.5 million for the STEAG Group. Employees received bonuses totaling €0.7 billion for their suggestions.

Corporate governance

Corporate governance comprises the principles that should be used to run a company and the rules and measures that are used to structure these principles and put them into practice. The principles are set out in the German Corporate Governance Code, which forms the basis for the conduct of the Board of Management and Supervisory Board of STEAG GmbH and is an integral part of STEAG's corporate culture.

For the STEAG Group, good corporate governance does not simply mean acting lawfully in all respects in compliance with statutory obligations; it also means acting in a responsible and value-oriented manner, which includes voluntary measures. Good and transparent corporate governance paves the way for lasting success.

To implement these principles, employees are guided by STEAG's Code of Conduct, more detailed guidelines and Group-wide compliance management system, which are continuously driven forward.

As in previous years, the principal focus of compliance in 2014 was on avoiding risks and preventing compliance violations. More than 1,000 employees throughout the Group received personal training through routine and target group-specific face-to-face training sessions on fighting corruption and economic crime. These included active dialogs and discussing "dilemma situations". Local compliance officers provided valuable support for this process, especially at subsidiaries. Training in Germany was complemented by training in other European countries, including Poland. Foreign business activities are becoming increasingly significant for the STEAG Group so providing preventive information on risks will be stepped up in the future.

In addition to face-to-face training, the Compliance and HR and Organization Development departments jointly developed an e-learning tool on the STEAG Code of Conduct to give new employees, those subject to regular training cycles, and other interested members of staff permanent access to STEAG's corporate governance principles.

In addition, the corporate governance principles are consistently included in the STEAG Group's contracts and voluntary commitments.

The STEAG Group has been a member of the UN Global Compact for four years and supports compliance with its ten principles in the areas of human rights, labor standards, environmental protection and fighting corruption. In addition to these principles, STEAG applies the International Labor Standards of the International Labor Organization (ILO) and acts in accordance with the OECD Guidelines for Multinational Enterprises.

These principles are also integrated into agreements with business partners, both individually and through the General Business Conditions. The STEAG Group therefore implements the principles of a sustainable supply chain and regards itself as part of this. Together with the Procurement department, Compliance has introduced a self-assessment for focus suppliers covering governance and sustainability issues and their implementation. Further, the STEAG Group continuously reports on its corporate responsibility activities in Germany and abroad, most of which strengthen site-related infrastructure at local companies and support social objectives. Further significance comes from the rising number of information portals in the internet that enable customers, shareholders and financial partners an insight into the measurable activities of the STEAG Group, especially in the areas of environmental protection and human resources.

Events after the reporting period

There have not been any changes in conditions in the sector since the start of 2015, nor have there been any significant developments that could have a material impact on the situation of the STEAG Group.

Opportunity and risk report and forecast

Risk report

Risk strategy

Opportunities and risks constantly arise for the STEAG Group in the course of its business activity. Risk management forms a central element in the management of the company and is geared specifically to securing present and future potential for success and avoiding, preventing, countering and minimizing risk. Early identification and utilization of opportunities can heighten the success of the Group.

Due to its fields of activity, the STEAG Group is exposed to constantly changing political, social, demographic, legal and economic operating conditions. The resultant risks are addressed by monitoring and analyzing the entire operating environment and anticipating the associated market developments. The findings are used to systematically develop STEAG's portfolio in accordance with the strategy for the Group.

Structure and organization of risk management

STEAG has a Group-wide internal risk management system. Alongside organizational measures and internal control systems, risk management is supported by the Audit department as a process-unrelated controlling and consulting body.

The risk management system is organized on a decentralized basis in line with STEAG's organizational structure. The organizational units bear prime responsibility for the early identification of risks, estimating their implications, introducing suitable preventive and control measures and for the related internal communication of opportunities and risks. Risk officers in the organizational units are responsible for coordinating the relevant risk management activities.

The Corporate Controlling department coordinates and oversees the processes and systems in the STEAG Group. It is the contact for all risk officers and is responsible for information, documentation and coordination at Group level. Further responsibilities include ongoing development of the methodology used by the risk management system.

Risk management is a central element in STEAG's controlling processes at all levels, and covers strategic and operational planning, preparations for investment decisions, monthly reporting and projections, and, from a certain level, immediate reporting of risks. The organizational units conduct an extensive annual inventory of opportunities and risks in connection with the mid-term planning process. All relevant factors are systematically identified and documented and the probability of the risks occurring and the potential damage are evaluated. All organizational units are required to provide details of action to be taken with regard to the opportunities and risks identified in the risk inventory and their implementation is monitored. The inventory, which looks at opportunities and risks over a short-term period of one year and a mid-term period of at least five years, is supplemented by monthly reports on changes in opportunities and risk factors previously identified, and newly identified opportunities and risks relating to the current year.

Overall risk assessment

Taking into account measures that are planned and have been implemented, no risks have been identified that — either individually or in aggregate — could undermine the position of the STEAG Group as a going concern.

Risks are subdivided into strategic, operational, financial and other risks.

Strategic risks

Changes in the present regulatory framework could have a significant impact on planned investments and the earnings position of the STEAG Group.

The Group's business activities are exposed to strong and dynamic competition which increases volume and price risks.

At present, it seems that the altered market conditions in Germany could result in a decline in domestic power generating capacity on economic grounds. This would be driven first and foremost by the promotion of renewable energies, which is unrelated to demand, and the priority given to feeding it into the grid. This preferential treatment is likely to drive out both power plants that stabilize the system and highly efficient co-generation plants, thereby holding back the systems and market integration of renewable energies. Unless the present energy policy is modified, STEAG will be forced to scale back its present power plant capacity in Germany in the medium term and will not be able to invest in conventional energy generating facilities in this country as the present market model does not give it any incentive to do so.

Political risks in the countries where STEAG operates its foreign power plants are secured through investment guarantees from the Federal Republic of Germany and credit insurance from the states that have granted export credits. This means that loss of the STEAG Group's capital investment is essentially excluded.

Operational risks

In view of the long-term nature of the power plant business, preventive risk management is particularly important. Central elements are careful analysis of the market conditions and the general business framework, careful management of the relevant risks through a balanced and systematic risk policy, the use of high-quality technology, and acceptance of the facilities by the local community. The quality of communication with customers, suppliers and local inhabitants and operation of the plants in conformance with the highest environmental standards form the basis for long-term success.

Policies that are agreed internally provide a framework for managing financial risks relating to trading prices (commodity prices, exchange rates) and the related counterparty default and liquidity risks. Corresponding indicators such as position limits, loss limits and value-at-risk are used to remain within the limits set.

While price risks relating to the use of derivatives can be managed with the aid of appropriate mathematical models, with regard to counterparty default risk the focus is on careful examination of the creditworthiness of contractual partners, the appropriateness of the underlying master agreements, and continuous monitoring of the associated credit lines. In the trading business, compliance with all relevant indicators is monitored by the trading back office.

Risk factors for the STEAG Group arise from the regulatory framework for the operation of power plants. The environmental protection requirements for the operation of power plants are met in full. Further risks arise from the energy policy framework, which could affect the Group's business performance. These include, in particular, future regulatory measures to further reduce CO₂ emissions. The STEAG Group therefore has a clear focus on work geared to reducing the specific CO₂ emissions of its power plants by increasing efficiency further and using innovative technologies. In view of their long-term nature and the large amount of capital involved, investment decisions involve complex and wide-ranging risks. The STEAG Group has defined structured responsibilities and approval procedures for the preparation, implementation and monitoring of such decisions.

Regulatory intervention in the market for renewable energy certificates by the Romanian government and the related oversupply of such certificates indicate a risk of reduced revenues from the Romanian wind farms. Oversupply and the associated negative implications for their marketability could mean that not all certificates can be sold.

Financial risks

Foreign currency risks mainly relate to the procurement and pricing of fuel requirements. They are hedged using suitable financial instruments.

For details of risk reporting on the use of financial instruments, please refer to the relevant section in the notes to the consolidated financial statements.

Planned dividend payments by the Group's foreign companies outside the Eurozone are hedged against fluctuations in exchange rates. In addition, at Compania Electrica de Sochagota S.A.E.S.P. (Colombia), costs in Colombian pesos are hedged against fluctuations in the exchange rate of the US dollar. By contrast, the risks arising from translation of the annual financial statements of foreign subsidiaries into euros at actual exchange rates compared with budgeted exchange rates (translation risks) are not hedged.

Other risks

The STEAG Group is exposed to normal legal risks arising in the course of business from contractual relationships with customers and business partners, and technical risks relating to the operation of plants, especially large-scale plants. Adequate provisions are recognized in the event of legal disputes with contractual partners, in consultation with the relevant specialist departments.

During construction of the Walsum 10 power plant, it was necessary to replace boiler components, which put construction work behind the original schedule. This led to risks in the form of additional expenditures, delayed earnings resulting from late start-up and the need for bridge financing. Since the annual financial statements for 2011, these have been taken into account by means of a thorough valuation. Commercial operation started in December 2013. The legal dispute with the consortium of general contractors, comprising Hitachi Ltd. and Hitachi Power Europe GmbH, started with the initiation of arbitration proceedings. In return, this consortium has filed a claim for recourse against STEAG GmbH with the regional court in Essen.

Risks relating to STEAG GmbH

As the parent company and head of the STEAG Group, STEAG GmbH, which is based in Essen (Germany), has control and profit and loss transfer agreements with most subsidiaries in Germany. It therefore manages most of the Group's risks in Germany. At the same time, it is the largest single company in the Group. The risks outlined for the STEAG Group therefore essentially apply to STEAG GmbH as well.

Opportunity report

Projects to cut costs, optimize processes and structures, broaden marketing and develop new business activities have been undertaken as part of optimization programs. Rapid and successful implementation of the measures associated with these projects should improve earnings.

There are good opportunities for further successful development of the business in STEAG's target markets. In Germany, the STEAG Group now has a strong position in the areas of renewable energies and distributed facilities, which are to be extended further. The STEAG Group's international focus is to be driven forward in the next few years. The focus in past years on gaining a foothold in high-growth markets and attractive regions is paying off.

Growth in selected international markets

The STEAG Group focuses on developing projects in countries where it already has long-standing business experience.

The Turkish energy market offers further potential for the STEAG Group. Construction of a wind farm in north-west Turkey (66 MW) commenced at the end of 2014 and commercial operation is expected to start in the fourth quarter of 2015.

The Asia-Pacific region also offers considerable growth potential for the STEAG Group. In particular, there are very good opportunities in services in India, where the Group has had a successful presence for years. This is an area where it can offer its special expertise in planning, building and operating hard coal power plants. Further business opportunities are emerging in Southeast Asia, where STEAG is currently working on several project concepts in the area of geothermal energy, primarily in Indonesia. Resources for a geothermal power plant in Indonesia are currently being explored.

Extending trading

The Market unit is currently extending its trading activities. These comprise national trading in renewable energies and the introduction of trading in power requirements with fixed supply profiles. At the same time it is developing foreign business, for example, the introduction of cross-border power trading and expansion of marketing activities in conjunction with foreign projects of STEAG GmbH and its subsidiaries that are already in existence or currently being realized.

Municipal partnerships and renewable energies in Germany

The STEAG Group supports municipal partners in Germany by making its expertise in power generation available to them. It has worked successfully with local authorities for many decades, either through joint ventures or under contract to administration unions. Through its ownership structure, these links have been strengthened since 2011. For example, the ownership structure offers opportunities for growth in renewable energies.

In Germany, municipal utilities account for more than half of power sales although they only have a few utilities of their own. The STEAG Group offers them access to its generating capacity and is planning to realize new energy generation projects in collaboration with municipal utilities.

To provide long-term support for sustained growth, there are plans to establish a partnership with municipal utilities through a joint company to finance, build and operate renewable energy projects and take stakes in project companies for this purpose. The STEAG Group will hold 51.0 percent of the joint company, which will form the starting point for future collaboration on selected projects from STEAG's pipeline in the biogas and wind energy sectors.

The number of municipal utilities that are customers for energy trading is also rising. Preparations are also under way for cooperation and service agreements, especially for municipal utilities' trading activities.

Opportunities for STEAG GmbH

As the parent company of the STEAG Group, STEAG GmbH manages most of the Group's business opportunities. The main opportunities correspond to those outlined for the Group.

Outlook

General economic development

Germany's central bank, the Bundesbank, is forecasting a slight rise of 1.0 percent in German GDP in 2015. According to its forecast, the main factors supporting this slight rise will be the fact that the German economy is still in good shape, with low gearing and balanced price/cost ratios in the corporate sector, and low interest rates.

This will have a positive impact on the domestic economy and will also increase the exploitation of opportunities on foreign markets. Increased opportunities for growth in the coming year should once again come from foreign markets, especially if the economic recovery in the Eurozone strengthens and global trade also flourishes.

The sharp drop in the price of crude oil in recent months should have a further positive influence on economic growth. The Bundesbank anticipates that German GDP could rise by an additional 0.1-0.2 percentage points if the price of crude oil remains at the present level for a prolonged period.

Threats to economic development are still the heightened geopolitical tension and the risk of abrupt correction processes triggered by the financial markets, which would adversely affect emerging markets.

Development of the energy sector

Continued rapid expansion of energy generation from renewable resources will result in a further reduction in conventional power generation in Germany and have a perceptible impact on electricity prices. Analysts and traders assume that the prices on the electricity exchanges will be low in the medium term. At the same time, the prices charged to consumers will rise as they also include costs for distribution, expansion of the grid, taxes and levies. In view of the German government's goal of reducing primary energy consumption, the Federal Ministry for the Economic Affairs and Energy (BMWi) assumes that, despite the good economic outlook, gross electricity consumption in Germany will stagnate or decline slightly in the next few years.

Strategic and operational challenges

The STEAG Group faces special challenges in the coming years. The shift in German energy policy has significantly altered the framework for power plant operators.

The preferential treatment of energy from renewable sources under the Renewable Energies Act (EEG) is putting pressure on the earnings of operators of fossil fuel power plants. In view of the altered operating conditions for hard coal-fired power plants in Germany, the STEAG Group is optimizing cost and revenue structures at its power plants. In addition, it is continuing to review and where necessary adjust administrative structures and processes. These measures should bring considerable savings in the coming years.

The STEAG Group also aims to adapt to the rising requirements in the marketing of generating capacity and power. Here, it is taking action so that it can respond flexibly to changing market conditions. That includes expanding its service portfolio and making preparations for the shutdown of power plants, which appears to be necessary from the present viewpoint. The Group is therefore concentrating on ensuring that its present power plant capacity can be operated for as long as possible. The aim is to take decisions on the timing of shutdowns as late as possible.

The STEAG Group is an established partner for the operation of power plants for third parties in Germany and abroad. It also provides external partners with operatives with a wide range of qualifications, either for the operation of power stations or for assignments in related sectors.

Following the successful commissioning of the Walsum 10 power plant, providing support for the arbitration proceedings initiated against the consortium of general contractors, comprising Hitachi Ltd. and Hitachi Power Europe GmbH, remains an important task. The claims asserted relate to delays in completion of the Walsum 10 power plant for which the consortium was responsible.

In addition, the STEAG Group has filed an arbitration case against the Spanish state with the International Centre for Settlement of Investment Disputes (ICSID) in connection with the Arenales solar heating project. At the end of 2012, the Spanish state adopted a royal decree which has brought various changes to the remuneration system for renewable energies, including solar heating. This has led to a sustained impairment of the cost-effectiveness of this project. In STEAG's view, the statutory changes infringe the principle of fair and equitable treatment set out in the energy charter and also constitute intervention comparable with expropriation.

Other challenges are operating the Crucea North wind farm in Romania in altered market conditions and bringing the Süloglu wind farm in Turkey into commercial service.

Turning to the STEAG Group's strategic alignment, one focal area of planned growth will be renewable energies in order to further diversify the generating portfolio. Growth should be both national and international. A stable financial basis is vital for this. To realize its growth strategy, the STEAG Group will be focusing on onshore wind projects. Two major projects, the wind farm in Ullersdorf (Germany) and the Crucea North wind farm in Romania, came into service in 2014. In addition, the foreign activities in the area of geothermal energy are to be stepped up.

The strategic focus and the possible use of synergies between STEAG GmbH, the company's sole owner KSBG KG and the companies in the KSBG consortium offer opportunities to improve the STEAG Group's market presence. We also expect this collaboration to provide impetus for the district heating and energy services operations.

Operating performance

We expect the Group to generate considerably higher sales of €3.9 billion in 2015, principally as a result of the planned expansion of trading activity, higher sourcing and increased power supply from integrated power plants (acquisition of the Bexbach power plant and marketing of power from the Bergkamen power plant). In 2015, EBIT is expected to be 10 percent lower than in 2014. An anticipated drop in earnings from domestic power plants will not be fully offset by the expected earnings from new renewable energies projects.

Contrary to the forecast made in the prior year, EBIT declined slightly in 2014.

The reasons included an unplanned deterioration in earnings from the District Heating business unit, mainly due to the weather, and unplanned valuation effects, while positive effects were reported by the Renewable Energies and Distributed Facilities division.

Compared with the forecast, sales rose by around 14 percent. This was mainly due to an unplanned rise in the volume of traded power on the domestic power market.

The future development of the Group will be influenced principally by the planned investments. Investment of nearly €550 million is scheduled for 2015 and will focus on building up new business activities. Around €470 million has been earmarked for investment in new construction projects. Within the established business, selective investments will be channeled into raising the operating efficiency of power plants.

General information on expected developments

The STEAG Group assumes that the opportunities arising from its strategic focus and, in particular, the planned investment in growth areas will help it maintain its good position in the energy market and expand into key segments in the future.

Expected development of STEAG GmbH

The operating result is expected to be lower in 2015 than in 2014, partly due to lower margins at the domestic power plants as a result of the challenging market environment. A major overhaul is only scheduled for the Herne site.

Essen, March 13, 2015

STEAG GmbH

Board of Management

Rumstadt

Baumgärtner

Dr. Cieslik

Geißler

This report contains forward-looking statements based on the present expectations, assumptions and forecasts made by the Board of Management and the information available to it. These forward-looking statements do not constitute a guarantee of future developments and earnings expectations. Future performance and developments depend on a wide variety of factors which contain a number of risks and unforeseeable factors and are based on assumptions that may prove incorrect.