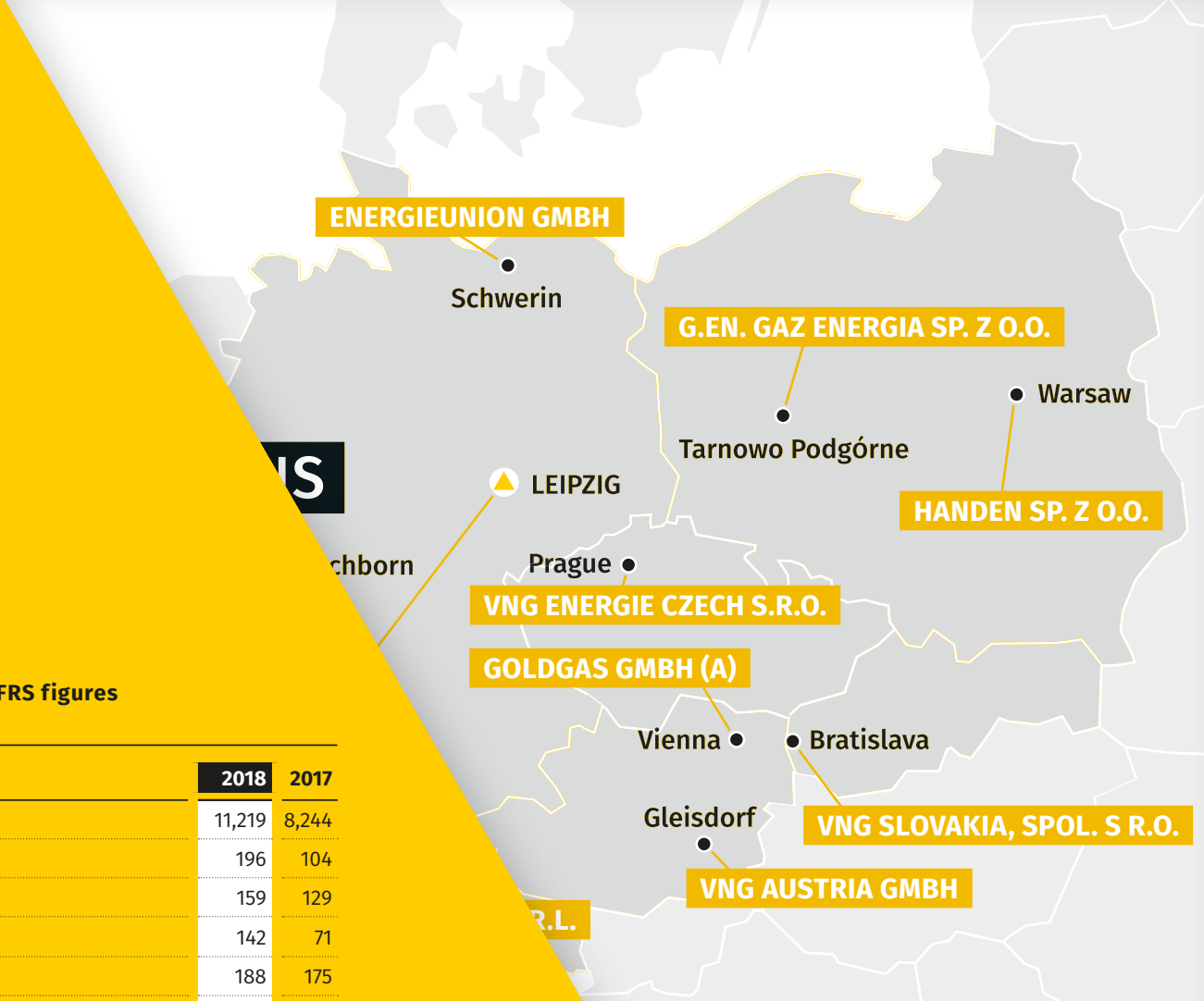
VNG

STRONG TOGETHER – UNITY IN DIVERSITY

Annual Report 2018



VNG's key IFRS figures at a glance

in € million	2018	2017
Revenue	11,219	8,244
EBIT	196	104
adj. EBIT*	159	129
Net income	142	71
FFO**	188	175
Net cash investments	–62	145
Non-current net liabilities***	301	456
Equity ratio (%)	22	27

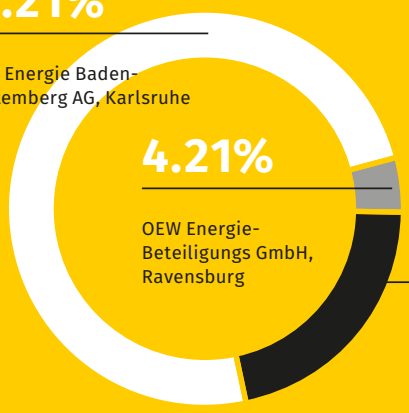
* EBIT adjusted for extraordinary and non-recurring income items
** Funds from operations, i.e. consolidated earnings adjusted for non-cash income and expenses as well as gains/losses from the disposal of fixed assets
*** Net financial liabilities plus provisions for pensions and decommissioning less inventories that can be liquidated at short notice

VNG key performance data

		2018
Number of employees at year end*		1,101
Group companies and holdings		62
Number of European countries with VNG holdings		6
Gas send-out	in billion kWh	500
High-pressure pipeline system	in km	7,000
Storage capacity	in billion m³	2.2

* Total employees of all fully consolidated companies; as at 31 December 2018

Shareholders of VNG AG



* Trustee for eight municipal utilities and municipal companies (Annaberg-Buchholz, Chemnitz, Dresden, Hoyerswerda, Leipzig, Lutherstadt Wittenberg, Neubrandenburg, Rostock); as at 31 December 2018

strong group
f companies
for gas and
structure

NATURAL GAS CAN DO MORE. WE CAN TOO.

WE ARE CONVINCED THAT GAS CAN DO MORE.

Gas is the nucleus of our business activities and an energy source with great future potential. Be it the use of natural gas as a bridging technology for rapidly advancing decarbonisation or renewable gases as a sustainable solution in the energy mix of tomorrow – we play our part in enabling and advancing a secure, cost-effective and environmentally friendly supply of gas.

VNG IS A RENOWNED GAS SPECIALIST.

We unite profound expertise along the entire gas value chain with the highest quality in our products and services. We take advantage of new opportunities in the energy market to create value for our customers and partners. By making numerous strategic and operational decisions and launching a new brand that combines all our companies' competencies under a single umbrella, in 2018 we systematically and sustainably positioned ourselves to play a major role as we journey towards a new energy system.

Learn more on pages 10 – 27

VNG

BALANCE VNG BIOENERGIE GMBH
ENERGIEUNION
GDMcom
GEN GAZ ENERGIE
GEOMAGIC
goldgas
goldgas
HANDEN
infracon Infrastruktur Service
MGMTree
MoviaTec
ontras
SPI GAS
VNG Austria
VNG Energie Czech
VNG Gasspeicher
VNG Handel & Vertrieb
VNG Innovation
VNG Italia
VNG Slovakia
VNG ViertelEnergie

OUR LOCATIONS

A strong group of companies for gas and infrastructure

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FOREWORD BY THE EXECUTIVE BOARD

The executive board (from left to right)

Hans-Joachim Polk/Chief Infrastructure & Technology Officer
Bodo Rodestock/Chief Financial & Human Resources Officer
Ulf Heitmüller/Chief Executive Officer

Dear Shareholders and business partners, dear friends of the company,

It is with great pleasure that we present our successful results for the 2018 financial year, which was simultaneously the company's 60th anniversary.

In this context, success to us means that we were able to generate excellent results across the board that exceeded our expectations. In the second year since the adoption of our VNG 2030+ strategy, we succeeded in resolutely pushing ahead with the transformation of our company initiated in 2017, while at the same time maintaining a systematic focus on costs and achieving strong operating performance. Initial achievements in the implementation of our strategy combined with positive non-recurring items intensified our company's strong growth and give us strength for the future.

Expressed in figures, this means: With an adjusted EBIT of € 159 million, we were able to increase earnings by 23 percent compared to the previous year. Considering consolidated net income, the figure actually doubled to € 142 million.

This outstanding performance in the past year was achieved on the basis of the excellent cooperation between all of VNG Group's business areas. At the beginning of the third regulatory period, the Transport business area once again made a significant contribution to consolidated earnings, while the Storage business area – with its strict focus on earnings – was able to almost break even in an environment that remained difficult. In the Trading & Sales business area, the wholesale segment particularly exploited its opportunities through active portfolio management, integrated physical sales and a strong purchasing position. Due to regulatory requirements, the wholesale business was retroactively spun off into VNG Handel & Vertrieb GmbH, a wholly-owned subsidiary of VNG AG, at the end of March 2018 with effect from 1 January 2018. In this context, nothing has changed for our customers and partners except for the name. As VNG, however, we were able to take advantage of this spin-off to reposition our trading and sales activities on the market.

Since the end of September 2018, with financial effect from 1 January 2018, the Exploration & Production business no longer forms part of the group. The decision to sell was not an easy one for us to make – just as entering the E&P business in 2006 was correct and important, the exit was just as logical in view of the realignment of our company within the framework of VNG 2030+.
By selling VNG Norge AS, we generated positive non-recurring earnings that contributed to the successful financial year and opened up additional opportunities for us to further restructure our business portfolio. In addition, we will be able to benefit in many ways from the expertise that we have developed over twelve years in the E&P business to establish new areas of business in the future.

In the current year, we will continue to focus on implementing our strategy. In this context, reducing CO_2 emissions – the keyword here being the decarbonisation of the energy industry – is one of our main drivers. It is spurring us on to make our core product, natural gas, even more climate-friendly – an objective that we are pursuing partly with the growth achieved in the biogas segment in 2018 and with forward-looking concepts for green gases.

However, other megatrends such as increasing decentralisation, steadily advancing digitisation in all areas of social and economic life and demographic change also have a direct impact on our strategic direction and thus on our business activities. This is reflected not only in the adjustments we have made in the traditional business areas of Trading & Sales, Transport and Storage, but also in our new business areas and ideas for district development and digital infrastructure. In this way, we are confronting new challenges and gradually diversifying VNG's earnings base.

But another thing is clear: In light of constantly shifting challenges, we will continuously review our strategy and adjust it where necessary. In addition, we are systematically improving our innovation management, cooperating with promising start-ups and promoting cultural and mental change within the company. The result is that, today we are already much more agile, digitally savvy and efficient.
We are cultivating a new form of collaboration that creates substantially more room for proactive action and fresh ideas. And we don't want to let up here. Another important issue for us remains the safety and health of our employees at their workplaces (health, safety, and environment).

The same thing applies today and tomorrow: We want to play a key role in shaping a green, digital, and gas-based future. After all, even though we operate in a fiercely competitive market, we still view natural gas as a source of energy as a great opportunity to protect the climate and successfully restructure our energy supply. With our products and solutions around natural gas, we offer answers to important questions that arise in the context of the energy transition: How can we make rapid, effective and affordable progress towards reducing CO_2 emissions in order to protect the climate? Why should the energy transition just be an »electricity transition«? In the context of integrated energy, what is the best way for gaseous fuels of the future to be combined with renewable energies? How do we guarantee supply security in an increasingly volatile system of energy generation from renewable energies? In all this, we are convinced that with natural gas and its ability to itself become more

green as well as the existing infrastructure, we have the right solutions at our disposal to further shape the energy supply of the future.

Furthermore, 30 years after the Peaceful Revolution and the fall of the Berlin Wall in the autumn of 1989, we would like to emphasize that our origins and deep roots in our home region are important to us. VNG has continuously evolved over the past 60 years; in our business activities, our focus on regional value creation and our social commitment, we have always believed in the idea of »from the region, for the region« – and have been and will remain a close partner to the region.

Dear readers, we cordially invite you to discover (or rediscover) VNG within the pages of this annual report. With our new brand identity, we are showing the outside world what has changed in and around the company. VNG stands for a strong alliance that draws its strength from the diversity of the competencies of its more than 20 companies. However, it also stands for a strong bond with its customers, partners and the region.

Finally, we would like to thank our shareholders, our Supervisory Board, our customers and our partners for their continued trust in our services and the future viability of our strategy during the 2018 financial year. In addition, we would like to particularly thank our employees, whose hard work and dedication played a key role in making the prior financial year so successful.

The Executive Board

Ulf Heitmüller
Chief Executive Officer

Hans-Joachim Polk
Chief Infrastructure & Technology Officer

Bodo Rodestock
Chief Financial & HR Officer

Further information can be found in the »Interview with the Executive Board« section on pages

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Learn more about the members of the executive board at

www.vng.de

REPORT OF THE SUPERVISORY BOARD

The Executive Board regularly, comprehensively and promptly informed the Supervisory Board, both orally and in writing, as to the development and the position of the Company as well as regarding significant business transactions. On the basis of these reports, extensive consultations and the information provided, the Supervisory Board monitored the Executive Board and, in particular, considered the development of the business areas, the Company's financial position, questions around financial, investment and personnel planning as well as all measures which, pursuant to the Articles of Association, require the approval of the Supervisory Board.

In the 2018 financial year, the Supervisory Board held a total of five meetings including an extraordinary meeting. Among other things, the meetings focussed on:

- *the Company's results of operations,*
- *the strategy review VNG 2030+,*
- *the revised version of the Articles of Association of VNG AG as well as the rules of procedure for the Supervisory Board and the Executive Board,*
- *the implementation of the unbundling requirements of Section 10b (3) of the Law on the Energy Industry [Energiewirtschaftsgesetz, EnWG] by spinning off the business area Trade,*
- *the sale of 100% of the shares of VNG Norge AS,*
- *the taking on of loans and agreements with respect to lines of credit and*
- *capital expenditures in new business areas, in particular Biogas.*

The Supervisory Board extensively addressed the results as well as the status of the implementation of the Company's strategic realignment as presented by the Executive Board.

Within the scope of its consulting and monitoring function the Supervisory Board addressed VNG's gas trading activities, in particular the management of gas trading contracts and the conclusion of gas procurement contracts, the developments in the business area gas storage as well as gas transport projects. Furthermore, it dealt in detail with the Company's other investments, including restructuring under company law and funding.

On the basis of these discussions and also the reports and information provided by the Executive Board, the Supervisory Board has satisfied itself as to the propriety of the Executive Board.

KPMG AG Wirtschaftsprüfungsgesellschaft, Leipzig has audited VNG AG's annual financial statements as at 31 December 2018 as well as the management report for financial year 2018 prepared by the Executive Board, including the accounting records, as well as compliance with the accounting regulations pursuant to Section 6b (3) of the EnWG, and has issued an unqualified auditor's report. Furthermore, the consolidated financial information which was electively prepared on the basis of IFRS, including the Group management report was audited. The auditor also issued an unqualified auditor's report with respect hereto. The audit report and the audit opinions were distributed to all members of the Supervisory Board. The Supervisory Board has noted and approved the results of these audits.

The Supervisory Board has examined the annual financial statements of VNG AG and the management report as well as the consolidated financial information along with the Group management report. This examination did not lead to the identification of any objections. The auditor attended the meeting of the Supervisory Board at which the financial statements were discussed and reported to the Supervisory Board on the most significant results of its audit. The Supervisory Board approved the annual financial statements as at 31 December 2018 prepared by the Executive Board. The annual financial statements are thereby approved. In addition, the Supervisory Board approved the consolidated financial information of VNG AG as at 31 December 2018 including the Group management report.

Thomas Kusterer, Chairperson

The Supervisory Board concurs with the recommendation of the Executive Board with respect to the use of the balance sheet profit.

The report pursuant to Section 312 of the German Stock Corporation Act (AktG), which the Executive Board must prepare with respect to relationships with affiliated companies of VNG AG has been provided. The financial statement auditor has audited this report and has provided the following unqualified auditor's report pursuant to Section 313 (3) of the AktG:

»On the basis of our dutiful examination and judgement we confirm that

1. the actual disclosures in the report are accurate,
2. for the legal transactions presented in the report, the consideration given by the Company was not inappropriately high.«

On the basis of its own assessment, the Supervisory Board concurs with this auditor's opinion.

Upon completion of its examination, the Supervisory Board does not have any objections to the statements of the Executive Board at the end of the report with respect to the relationships with affiliated companies.

On 16 May 2018 respectively 12 July 2018, Dr. Reinhard Richter and Prof. Dr. Norbert Menke, the latter as 1st Vice Chairperson for the Supervisory Board, left the Supervisory Board. Correspondingly, by resolutions of the extraordinary shareholders' meeting on 17 May 2018, Dr. Frank Brinkmann and from 13 July 2018, Michael M. Theis as well as Volkmar Müller (as replacement member for Michael M. Theis) were appointed as members of the Supervisory Board with immediate effect. With effect from 13 July 2018, Hans-Joachim Herrmann and Christina Ledong took over the seats of 1st Vice Chairperson respectively 2nd Vice Chairperson of the Supervisory Board. Furthermore, with effect from the conclusion of 12 July 2018, Peter Leisebein resigned from his position as 2nd Vice Chairperson for the Chairperson of the Supervisory Board.

In accordance with the changes in the rules of procedure of the Supervisory Board, the Supervisory Board committees were established and elected in the Supervisory Board meeting on 17 May 2018. In each case, the number of members of the Committees was increased from three to five. Furthermore, Christina Ledong and Dr. Reinhard Richter gave up their positions in the Finance and Audit Committee and Prof. Dr. Norbert Menke as well as Peter Leisebein gave up their positions in the Personnel Committee with effect from the conclusion of 12 July 2018. They were replaced by Dr. Frank Brinkmann and Josefine Bormann in the Finance and Audit Committee as well as Hans-Joachim Herrmann and Christina Ledong in the Personnel Committee. In addition, Markus Baumgärtner and Michael Raida were appointed to the Finance and Audit Committee, Markus Baumgärtner and Dr. Bernd-Michael Zinow were appointed to the Personnel Committee and Markus Baumgärtner as well as Michael Raida were appointed to the Exploration and Production Committee.

As a result of the sale of all of the shares in VNG Norge AS at the end of September 2018, VNG AG completely pulled out of the business area Exploration and Production. As such, the Exploration and Production Committee within the Supervisory Board was no longer required and, correspondingly, in its meeting on 29 November 2018, the Supervisory Board resolved to dissolve this with immediate effect.

The Supervisory Board expresses its appreciation to the members of the Supervisory Board who have stepped down for their cooperation in an atmosphere of mutual trust as well as for their tremendous commitment. The Supervisory Board acknowledges and thanks the Executive Board as well as all employees for the work done in financial year 2018.

Leipzig, 11 April 2019
The Supervisory Board

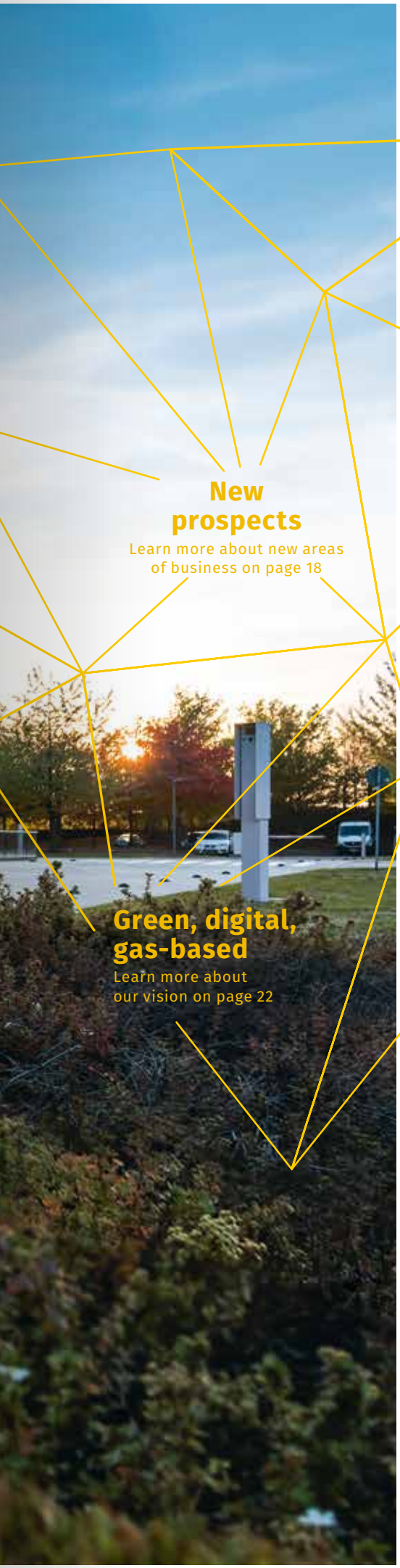
Thomas Kusterer
Chairperson

STRONG TOGETHER – UNITY IN DIVERSITY

Driving innovation

Learn more about innovation at VNG on page 20

VNG stands for concentrated gas expertise and gas infrastructure, but at the same time encompasses much more. The following pages will provide a look at our company's activities and the trends surrounding a promising energy source that is cost-effective, environmentally friendly and technologically advanced.



Engine of the energy transition

Learn more about natural gas' climate-saving potential on page 23

New prospects

Learn more about new areas of business on page 18

Green, digital, gas-based

Learn more about our vision on page 22

VNG companies have locations in

6

European countries

1,101

employees (total of all fully consolidated companies)

VNG 2030+

Learn more about our strategic direction on page 15

62

group companies and holdings

If a company wants to compete in the highly complex energy sector, it must have a solid foundation – this is true today more than ever before. As a group of companies active throughout Europe with strong regional roots and over 60 years of experience, we at VNG combine more than 20 companies with wide-ranging competencies under a single umbrella. In this context, we primarily focus on the areas of Trading & Sales, Transport and Storage as well as the development of new, promising areas of business. ▶

60 YEARS VNG

Founded in

1958

as »Technische Leitung Ferngas«

Our business areas at a glance

Trading & Sales:
Trading natural gas is one of our core activities. We also offer our customers gas, electricity and energy-related services. Our portfolio ranges from full supply to individual and highly flexible supply concepts. In 2018, we spun off our wholesale business in Germany into VNG Handel & Vertrieb GmbH as a result of regulatory requirements. We took advantage of this opportunity to position the company in a more modern way. This is also reflected in all other trading companies operating in Germany, Poland, the Czech Republic, Slovakia, Italy and Austria.

Transport:
Through the distribution of gas and the provision of pipeline-related services, our Transport business area guarantees supply security in Germany. As an independent transmission system operator, ONTRAS Gastransport GmbH guarantees non-discriminatory access to the network and, together with its subsidiaries, contributes to a functioning European gas market. ONTRAS is also a pioneer for green energy within the German gas network. The focus here is on developing future options for sustainable, green use of the gas infrastructure with renewable natural gas.

Storage:
As the third-largest storage operator in Germany, VNG Gasspeicher GmbH ensures the reliable, safe and efficient storage of gas at all times, and has been doing so since the 1970s. Today, our storage facilities are an important part of the gas infrastructure. They will remain an integral part of our future energy supply as storage facilities for volatile renewable energies. In the field of underground gas storage, we have comprehensive expertise ranging from operation and maintenance to marketing storage capacities. We also offer our customers intelligent and flexible storage products as well as special engineering services. ▶

TRADING & SALES

We supply power plants, industrial companies, municipal utilities and regional distributors as well as end customers in Germany and abroad through VNG Handel & Vertrieb GmbH and its subsidiaries.

VNG Handel & Vertrieb

500 billion kWh
in gas send-out

TRANSPORT

As an independent transmission system operator, ONTRAS Gastransport GmbH operates and markets a pipeline network that is 7,000 km long.

ontras

STORAGE

Through VNG Gasspeicher GmbH and a marketable storage volume of more than 2.2 billion m³, we are one of the largest storage operators in Germany and provide capacities in facilities at several locations in northern and central Germany.

VNG Gasspeicher

4
underground storage facilities

2.2 billion m³
working gas volume

7,000 km
of high-pressure pipeline

450
pipeline interconnects

»Gas is and will remain at the core of our business.«

Partner to the gas industry of the future

Today we can say that thanks to the variety of products and services we bring together in our group, we are a reliable partner for natural gas and supply security. We not only cover the traditional range of products and services, but are also systematically positioning ourselves to meet the requirements of the future natural gas and energy industry with new business ideas for biogas and green gases, digital infrastructures and district solutions. ▶

60 YEARS VNG

1958–2018: FROM GAS PIONEER TO CREATOR OF A GAS-BASED FUTURE

On 29 June 2018, we celebrated our 60th anniversary. We used this occasion to look back over the history of our company across very different stages and in different economic systems. Important milestones in this process included the development of the East German interconnected gas network, the transition to a market economy and the »natural gasification« of the East German gas network in the 1990s, growth and internationalisation in the 2000s, and, since 2017, an increasing focus on decarbonisation and a renewable world of energy for the future. Our expertise and experience from 60 years of VNG and successfully dealing with change are our guiding principles for successfully shaping the present and the future: Green. Digital. With gas.

VNG 2030⁺ – OUR PATH INTO THE FUTURE

It is no longer enough to look ten years into the future to understand and help shape the fundamental change that is currently looming in the energy sector. Consequently, we are also focusing on the world of natural gas in the far future: For example, whilst what are known as green gases currently account for less than one percent of total natural gas consumption today, this ratio will be reversed within a few decades – with considerable effects on our business and the entire energy sector.

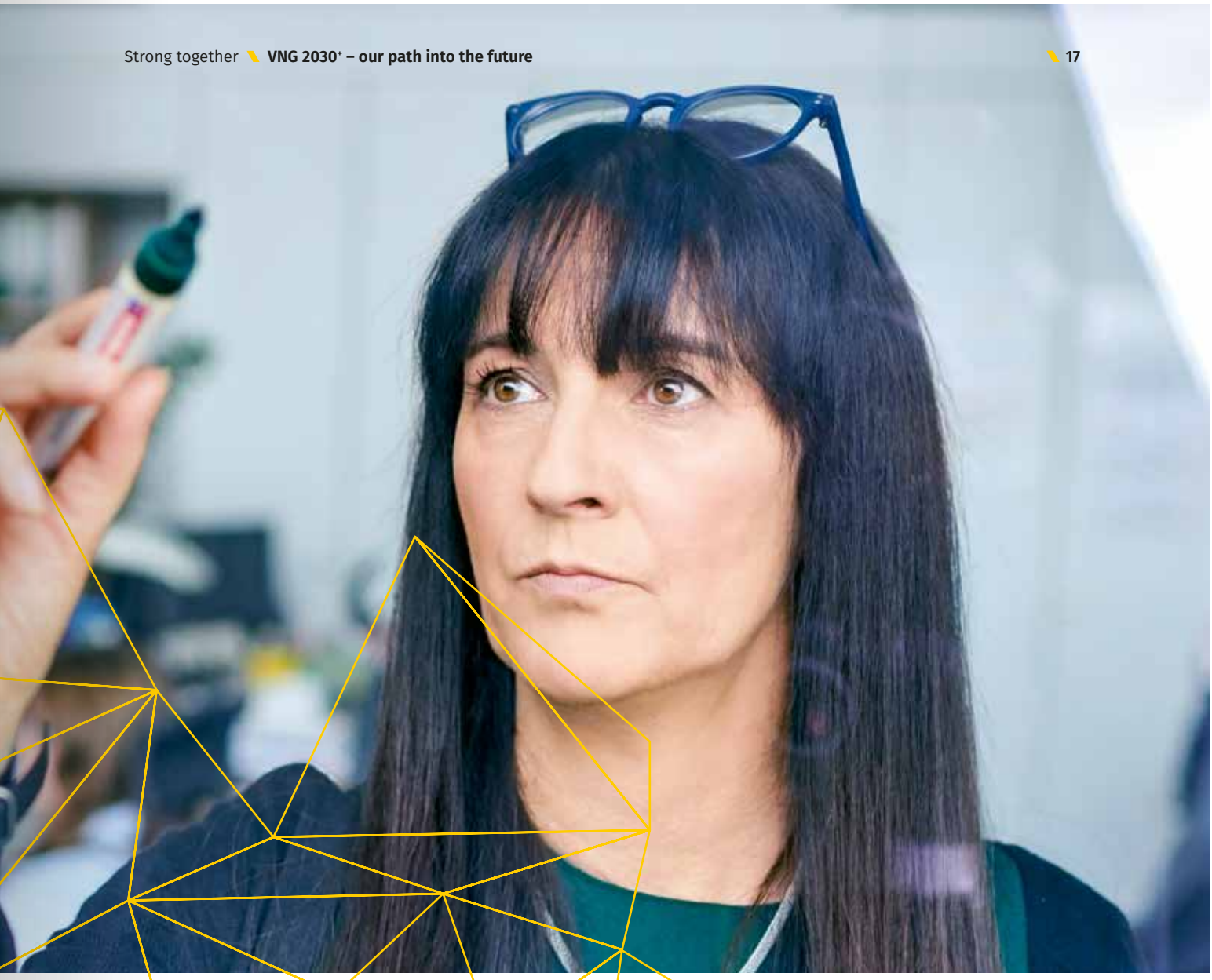
On the other hand, natural gas can and will continue to play a crucial role in reducing CO_2 emissions in all areas of society and achieving European climate change objectives. At the same time, an interconnected mindset and method of operating will become a key competence across all areas and sectors. Our proactive approach to these and other megatrends is reflected in our VNG 2030⁺ strategy. This is the key to our future growth – and to a functioning energy system in the future.

»2018 was primarily dedicated to our VNG 2030+ strategy.«

The goal in sight

There is no question that even in an increasingly complex energy market, we want to offer our partners and customers the right gas and energy services and products. This is why we initiated a group-wide strategy process in 2017 entitled VNG 2030+. In so doing, we have developed a strategic outlook for VNG that is geared not only to financial requirements but also, and in particular, to challenging energy policy and social requirements. This is how we intend to hold our own in the face of intense competition with evolving challenges while leveraging earnings potential.

Within the scope of our realignment, we are taking a two-pronged approach: In our established Trading & Sales, Transport and Storage areas of business, our focus is on further optimising our operational performance. In addition, we are continuously identifying growth opportunities in adjacent business areas. The year 2018 was dominated by this objective and saw us achieve the initial positive results. A major initial milestone was the sale of our exploration and production business. In conjunction with the conclusion of a syndicated loan agreement, we thus created further financial freedom for the implementation of our strategy in the coming years.



ENERGY WITH A NEW LOOK

After countless internal and external changes, it was finally time to completely revamp our corporate brand in the year of our 60th anniversary – and in September we were able to present our updated brand identity to the public. It symbolizes the fact that we view ourselves as players in an overarching environment characterised by dynamic change – and that at the same time, we as a group are moving closer together. In the process, we have, however, remained true to our values and our corporate culture.

VNG

As part of the brand relaunch, the »Verbundnetz Gas AG« and »VNG Group« brands were merged to form the new »VNG« brand. VNG now serves as the brand for VNG AG and at the same time as the umbrella brand for the entire VNG Group.

Introducing a new brand identity in 2018 was no accident – it complements the implementation of the VNG 2030+ strategy, which initiated a fundamental transformation of our corporate group.

New prospects for VNG

We are systematically diversifying our activities by developing adjacent and new business areas. In this process, we are focusing on issues that also have a significant impact on the energy policy environment and are important keys to mitigating climate change, enhancing supply security and making headway in the field of integrated energy.

As a competence-based field of growth, green gases are particularly important to us: they can be used and stored flexibly and can make a major contribution to reducing CO_2 emissions in the heating market, in the transport sector and in industrial manufacturing. This is what makes them an important part of the renewable energy mix.

As part of the VNG 2030+ strategy, we have set a goal of growing in this area – which we also achieved in 2018 with BALANCE VNG Bioenergie GmbH. The company focuses on investing and making advances in biogas and renewable natural gas system concepts.

In addition, we are increasingly focusing on projects and our own pilot projects around hydrogen.

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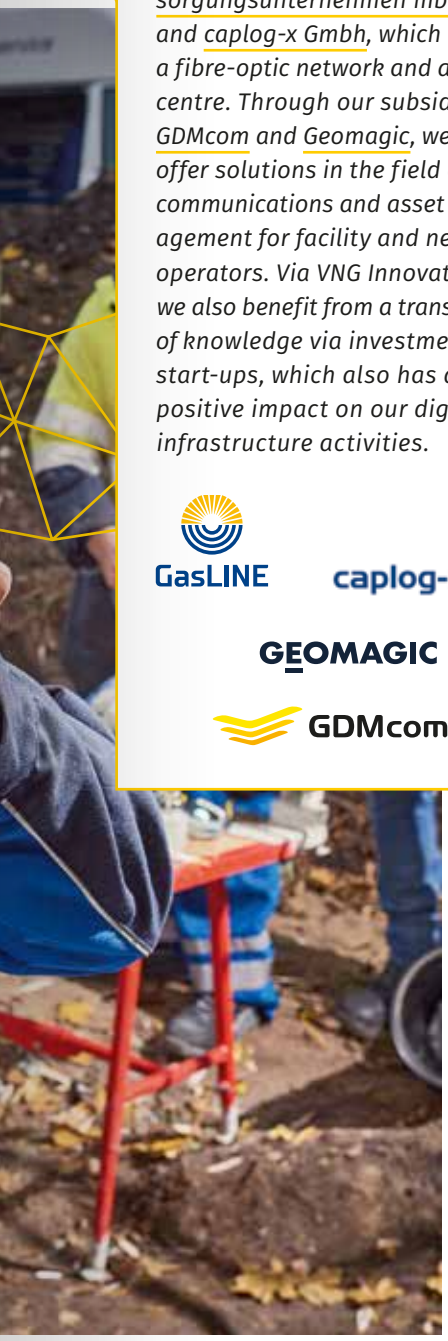
CONSOLIDATING DIGITAL EXPERTISE

We have been operating gas distribution systems and storage facilities for over 60 years – infrastructures with sophisticated technical requirements. As part of our VNG 2030+ strategy, we are leveraging these competencies to operate other system-critical and especially digital infrastructures. In our digital cluster, we already cover the entire value chain today. Examples include our investments in GasLINE Telekommunikations-gesellschaft deutscher Gasver-sorgungsunternehmen mbH & Co. and caplog-x Gmbh, which operate a fibre-optic network and a data centre. Through our subsidiaries GDMcom and Geomagic, we also offer solutions in the field of tele-communications and asset man-agement for facility and network operators. Via VNG Innovation, we also benefit from a transfer of knowledge via investments in start-ups, which also has a positive impact on our digital infrastructure activities.



When it comes to digitisation, we not only examine our internal processes, but also potential new areas of business. As such, we have identified digital infrastructures as a growth area. The advantage here is that our core competencies in the reliable operation of critical infrastructure such as transport networks and storage facilities can also be applied to the transport and storage of data. We invest in the expansion and operation of digital infrastructure via our shareholdings. On the basis of this approach, we are striving to become one of the leading indepen-dent providers of infrastructure-based secure data services.

Holistic thinking is particularly important in the planning, imple-mentation and operation of demand-driven district solutions – from generating heat to power, mobility, telecommunications and energy efficiency. Our subsidiary VNG ViertelEnergie GmbH has specialised in this area and, together with its Leipzig-based partner Tilia GmbH, supports local municipalities in developing and implementing forward-looking solutions. ▶

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Driving innovation

As a group with many decades of tradition, we want to remain true to our roots. At the same time, we also embrace fresh ideas and innovation. One example of this is the »Lateral Thinker« initiative, an ideas workshop launched by our employees. Furthermore, we want to continue gradually enhancing our innovation management. Last year, for example, we established a new IT platform for the group-wide generation and development of ideas and launched various innovation campaigns.

Through our subsidiary VNG Innovation GmbH and its investments in up-and-coming companies, we maintain close ties with young thought leaders in the industry. And through our partnership with Leipzig-based SpinLab – The HHL Accelerator, we are systematically positioning ourselves as a strategic partner for start-ups within the framework of the Smart Infrastructure Hub. ▶

SPINLAB THE HHL ACCELERATOR

»We create lasting shareholder value through innovation.«

VNG INNOVATION: COMMITTED TO START-UPS

VNG Innovation

Our capacity to innovate is an integral part of the VNG 2030+ strategy. In this context, VNG Innovation GmbH sees itself both as a driving force behind and an accelerator of new ideas and value creation. This company was once again active as a strategic investor in 2018:

In April 2018, it entered into a partnership with the Leipzig-based start-up Rhebo GmbH, thus supporting anomaly detection in the field of industrial network security.

By acquiring a stake in the Dresden-based start-up Infrasolid GmbH, it has been supporting the mass production of innovative infrared radiation sources since September 2018 together with the Saxony Technology Start-up Fund. These are used in gas detection and gas analysis systems, among other applications.

VNG Innovation also increased its stake in akvola Technologies GmbH. The Berlin-based start-up is successfully focused on technological solutions to clean hard-to-treat industrial waste water.

VNG Innovation also supports Cloud&Heat Technologies GmbH, a company that manufactures and operates cost-efficient and energy-saving data centres. What makes its approach special is that the waste heat is used to heat buildings, as well as for other purposes. In early 2019, Cloud & Heat was named the most innovative of the 50 fastest-growing European start-ups.

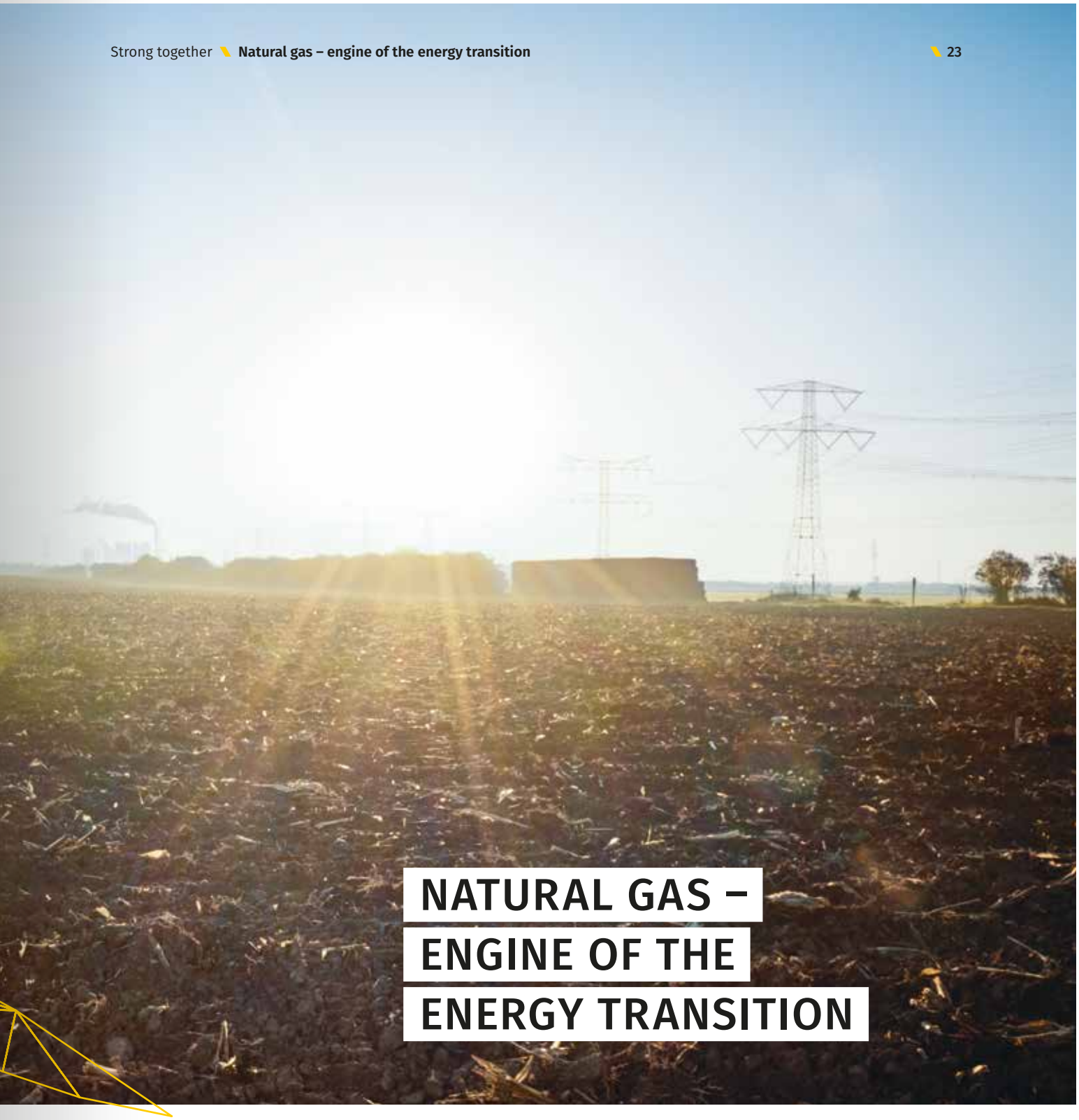
A strategic investment in Eigenheim Manager GmbH rounds off the portfolio. Thanks to its integrated mobile meter reading system, the company, which was founded in 2016, can continuously monitor consumption and supports documentation. »Eigenheim Manager« was launched by software and real estate experts from Leipzig.

Rhebo Industrial Network Continuity INFRASOLID akvola TECHNOLOGIES CLOUD & HEAT EIGENHEIM MANAGER

GREEN, DIGITAL, GAS-BASED

We view ourselves as a company proactively shaping the energy transition. In this context, our vision is to make VNG green, digital, and gas-based:

- *Green, because a modern energy system must be sustainable and renewable, green gases will be an important partner for renewable energies.*
- *Digital, because smart processes play a key role in integrated energy and in establishing and co-ordinating infrastructures.*
- *Gas-based, because gas is particularly climate-efficient, encompasses numerous technologies for the future and is an energy source that can be turned green.*



NATURAL GAS – ENGINE OF THE ENERGY TRANSITION

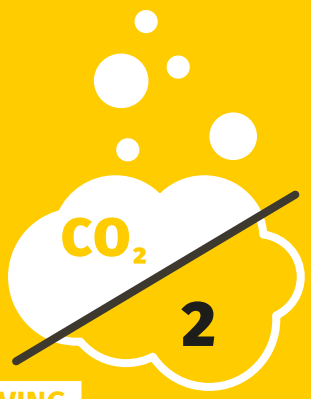
The energy transition represents a major opportunity for VNG. After all, our natural gas product harbours significant and cross-sector CO_2 savings potential – and where natural gas flows today, renewable gases can also provide the same benefits in the future. Biogas and RNG are already renewable, controllable and storable today. This will make it possible to achieve short-term objectives as well as further steps towards a low-carbon society – and we will do our utmost to achieve this in the future.

Gas can do it all

Since the UN climate conference in Paris, decarbonisation has been one of the key concepts of our time. In light of this, we believe that our company with gas as its nucleus offers a solution for the energy transition. The fact is that the energy transition can only succeed if we demonstrably reduce greenhouse gas emissions. An important option here is to make greater use of gas as an energy source.

For example, replacing outdated heating systems offers enormous potential – innovative gas-based systems can cut CO_2 emissions by up to 40 percent compared to old heating systems. When it comes to power generation, gas-fired power plants also offer major advantages: they halve emissions compared to coal and optimally supplement volatile renewable energies thanks to their ability to be managed flexibly. And in passenger, freight and ship transport, natural gas as a fuel in compressed (CNG) or liquefied (LNG) form can help to significantly reduce both CO_2 and particulate emissions. Natural gas thus stands for rapid and effective climate protection.

Climate-saving potential



HALVING

CO_2 EMISSIONS

when gas rather than coal is used to generate power.

Up to

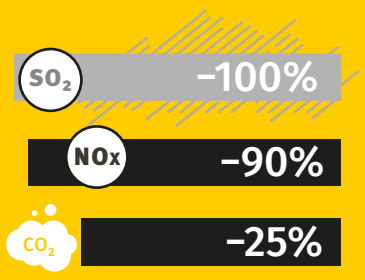
40% CO_2 SAVINGS

can be achieved by installing a new gas condensing boiler compared to an old heating system.

LNG offers an efficient

SOLUTION FOR ENVIRONMENTALLY FRIENDLY HEAVY-DUTY TRANSPORT

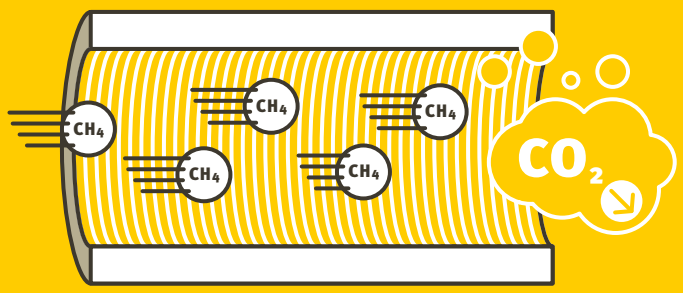
on the road and at sea.



Increasing the admixture

OF HYDROGEN AND SYNTHETIC GASES

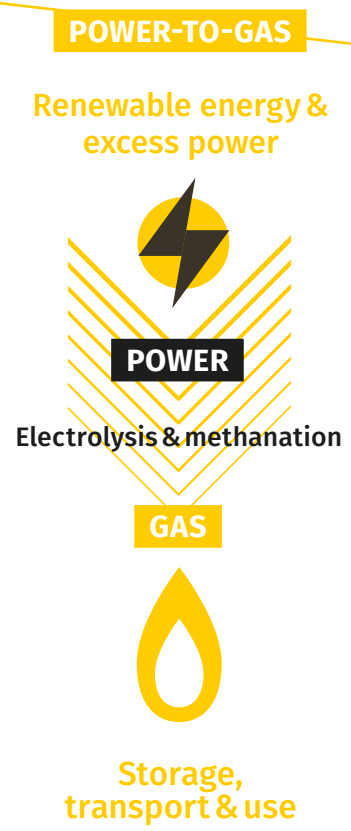
can further significantly reduce CO_2 emissions.



Rethinking energy

In the energy world of tomorrow, our gas will guarantee supply security. But not all gases are equal: as new technological possibilities emerge, gaseous energy sources are becoming increasingly climate-friendly. Thanks to the admixture of green gases – such as renewable natural gas or hydrogen – the carbon footprint will improve even further.

Gas will also play a key role in the progressive integration of the power, heat, mobility and industrial sectors as well as in the overall optimisation of the energy system. This means that a well-developed gas infrastructure also benefits renewables. As part of the power-to-gas concept, gas even becomes a solid partner: in this process, excess energy is converted into hydrogen or synthetic gas, which can be stored, transported and used in the long term. This means that as an element of integrated energy, gas is becoming renewable – and an integral part of a climate-neutral future.



VNG VIERTELENERGIE: GREEN IDEAS FOR THE DISTRICT

In cooperation with Tilia GmbH, VNG ViertelEnergie GmbH supports municipalities in implementing holistic district development solutions. The focus is on a wide range of areas – from heat, power and electric mobility to telecommunications, energy efficiency and local use of resources.

In early 2019, VNG ViertelEnergie won over the jury of an ideas competition for climate-friendly buildings. The »RE:Frame Energy Efficiency Award« was presented jointly by both the German Federal Ministry for the Environment and the Federal Ministry of the Interior, Building and Community. The focus of the »green neighbourhoods, happy citizens« is creating green spaces in buildings renovated for energy efficiency.

The aim is to step up climate protection measures and make them visible. The idea not only impressed the jury because of its impact, but also because of its feasibility and suitability for the target audiences.

VNG ViertelEnergie

BALANCE CONTINUES TO GROW WITH BIOGAS

In 2018, our subsidiary BALANCE VNG Bioenergie GmbH took an important step towards our aim of growing with biogas. The company has already consolidated VNG's activities in the field of alternative energies since 2006. Underpinned by the VNG 2030+ strategy, it has steadily added new biogas plants to its portfolio since 2017. In addition to the acquisition of seven individual plants, the company acquired a plant portfolio in December 2018 consisting of a total of five biogas plants at locations in the German states of Saxony-Anhalt and Lower Saxony. With this groundbreaking acquisition, BALANCE complemented its portfolio and doubled its installed capacity – giving the strategic growth area of sustainable gases a major boost.

BALANCE VNG BIOENERGIE GMBH

»Gas will pave the way for the energy transition.«

INTERVIEW WITH THE EXECUTIVE BOARD

Ulf Heitmüller,
Chief Executive Officer

WITH A NEW STRATEGIC ALIGNMENT, VNG HAS UNDERGONE BOTH AN INTERNAL AND EXTERNAL TRANSFORMATION SINCE 2017. IN LIGHT OF THIS, HOW SATISFIED ARE YOU WITH THE COMPANY'S PERFORMANCE IN THE 2018 FINANCIAL YEAR?

ULF HEITMÜLLER: Overall, I am extremely satisfied. We have noticeably focused VNG and successfully begun the further optimisation and restructuring of our business portfolio. The sale of the E&P business and the encouraging growth in the number of plants owned by our biogas subsidiary BALANCE were major steps forward for us. These acquisitions have considerably enhanced our position in this area. The spin-off of our wholesale business into VNG Handel & Vertrieb GmbH was also an important step. In general, we have accomplished a great deal – in terms of the company's organisational structure, processes and external communication with the relaunch of our brand.

BODO RODESTOCK: 2018 was an exceptionally good year. The figures speak for themselves: adjusted EBIT rose by 23 percent and consolidated earnings doubled. We recorded solid operating performance in all areas and also benefited from non-recurring items and achieved the first important milestones in our strategy. We have worked hard to achieve this, whilst never losing sight of costs and efficiency. We have good reason to be a bit proud of ourselves – and we owe a great deal to the tireless efforts of our employees throughout the VNG Group.

SPEAKING OF EMPLOYEES, WHAT IS YOUR ASSESSMENT OF 2018 AS CHIEF HUMAN RESOURCES OFFICER?

MR RODESTOCK: We have a highly motivated team. That was and is crucial to the success of the company. We are now working together in a completely different manner than was the case just a few years ago, we are focusing on greater participation and more transparent information processes. We continue to develop our culture of collaboration through agile and increasingly digital working methods.

»We are active in the region and for the region with a high degree of vertical integration.«

VNG HAS ADOPTED THE SLOGAN »STRONG TOGETHER – UNITY IN DIVERSITY« . WHAT DOES THIS MEAN?

HANS-JOACHIM POLK: This refers to the close bond between VNG's individual subsidiaries, business areas and departments, as well as the partnership with local and regional partners and our shareholders. Together is the only way that we will be able to master the challenges ahead. I can say from experience that ideas are generated especially when different points of view and competencies come together. And that's what we need, because VNG encompasses a wide variety of issues that we want and need to address. This approach is also reflected in our VNG 2030+ strategy.

TO WHAT EXTENT HAS THE VNG 2030+ STRATEGY ALREADY BEEN IMPLEMENTED INTERNALLY?

MR HEITMÜLLER: We are on the right track and are seeing a very high level of acceptance among the workforce. This is only possible because we have formulated and developed a common growth story with our employees. We are constantly improving and becoming more efficient – I am quite pleased that the strategy has had such an impact internally. This is a great example of the momentum that can develop when you embrace something new, and I'm referring in particular to our approach to strategy development across companies and hierarchies.

Hans-Joachim Polk
Chief Infrastructure & Technology Officer

WHAT IS THE ESSENCE OF THIS STRATEGY?

MR POLK: In addition to the many operational and strategic aspects within VNG's traditional business, the main goal is to position gas as a partner to renewable energies. To achieve this, we must convince our customers and politicians that together we can gradually make our core product, natural gas, greener. We can cut CO_2 emissions even further by using biogas, synthetically produced gases or hydrogen – which in turn will help us achieve the major undertaking of the energy transition. In addition, we want to develop new areas of business and expand our business portfolio on the basis of our competencies from the core gas business.

In this process, workplace safety is always a top priority. Our results in this area were again very good and we continue to work hard on the topic of HSE, because it is by no means an obstacle to efficient work – on the contrary. Everyone should go home as healthy as they were when they came to VNG. And this should be the case every single day.

VNG IS REGARDED AS ONE OF THE REGION'S MOST ATTRACTIVE EMPLOYERS. HOW HAVE YOU ACHIEVED THIS?

MR RODESTOCK: Our employees are the key to our success – and we operate accordingly. At VNG, this is reflected in flat hierarchies, an excellent work-life balance and flexible working hours, for example. The news magazine Focus recently ranked us as one of the top 10 employers in the German energy sector; across all sectors, we even ranked second in Saxony. This really made my day. But it also motivates us to continue in this direction and to become even better.

In general, VNG has very strong regional roots. We are active in the community, support many charitable initiatives, participate in regional business initiatives focusing on Central and Eastern Germany and are intensifying our collaborations with universities. This allows us to enter into partnerships that benefit both sides when it comes to the complex issues of our time. In short, we come from the region and are committed to the region.

Bodo Rodestock,
Chief Financial & HR Officer

»The benefits of natural gas are obvious. Reducing CO_2 emissions is what drives us.«

VNG CELEBRATED ITS 60TH ANNIVERSARY IN 2018, AND 2019 WILL MARK THE 30TH ANNIVERSARY OF THE PEACEFUL REVOLUTION AND THE FALL OF THE BERLIN WALL IN 1989. WHAT'S THE SIGNIFICANCE OF THIS FOR VNG?

MR RODESTOCK: It's extremely significant. As a Leipzig-based company with such a long tradition and experience in various political and economic systems, we have a very special connection to the Peaceful Revolution and the fall of the Berlin Wall 30 years ago, as it was this fundamental transformation that allowed VNG to evolve into the company it is today. The company's employees at the time viewed this as a major opportunity. This has paid off – and this mindset in dealing with major changes around us is what I continue to want for VNG, and is what underpins our new strategy and commitment to the use of gas.

VNG IS ALSO A VOCAL PROPONENT OF GAS AT THE NATIONAL AND INTERNATIONAL LEVEL. CAN YOU EXPLAIN THIS POSITION?

MR HEITMÜLLER: VNG is synonymous with gas expertise within the EnBW Group, in which we feel very comfortable. Of course we want to do justice to this role – which we also view as a responsibility – regionally, but also nationally and at the European level. We are active in various associations and initiatives in Berlin and Brussels. We participate in energy studies, conferences and events.

My impression is that in recent years we have been very successful in positioning gas as an energy source with excellent prospects for the future in the political arena and in the public eye. But we can't let up now.

THE TRANSITION TO A SUSTAINABLE ENERGY SUPPLY REPRESENTS A MAJOR TRANSFORMATION. WHAT CONTRIBUTION CAN VNG MAKE TO THE SUCCESS OF THE ENERGY TRANSITION?

MR HEITMÜLLER: We make a distinction between a first and a second energy transition. As VNG, we gained extensive experience with the first energy transition, which involved the transition of large parts of the East German energy supply systems to natural gas after German reunification. On the other hand, the current situation is much more complex than in the 1990s. We face regulatory, political and societal challenges. Natural gas and gaseous energy sources will, however, play an important role in the decarbonisation of the energy supply over the short, medium and long term. This is exactly where VNG comes in – our infrastructure for gas is extremely well developed. And in conjunction with renewable energy sources, we do not have to completely convert them, but can gradually transform the energy system by taking small technological steps.

WHERE DO YOU SEE THE GREATEST POTENTIAL FOR NATURAL GAS?

MR POLK: In the heating market and for power generation in particular, as well as in mobility, especially in commercial freight and heavy goods transport. Liquefied natural gas (LNG) will also be unstoppable in shipping. Steel mills will increasingly consider replacing coal or coke. In other words, there are many compelling reasons to increasingly use natural gas across all sectors.

But gas, especially green gas, can do more. With its ability to itself become more green as well as with the existing infrastructure of networks and storage facilities, gas is shaping its own future. To this end, we at VNG already launched a number of initiatives in 2018 to make our own contributions. We are absolutely certain that green gas, in its many forms, will be part of a completely renewable system for the long term.

CLIMATE PROTECTION INITIATIVES AND ENERGY POLICY PROCESSES ARE BECOMING MORE RELEVANT. WHAT TRENDS PARTICULARLY STOOD OUT TO YOU IN 2018?

MR HEITMÜLLER: We are currently following the »Gas Dialogue Process 2030« launched in 2018 by Germany's Federal Ministry for Economic Affairs and Energy with great interest, and there have also been numerous initiatives at the European level that focus on gas, such as the preparation of the »Gas Package 2020« as part of the Madrid Forum. This shows just how much we still need to discuss. It is now a matter of using the momentum to further promote gas – after all, the gas industry can not only contribute to a secure and affordable energy supply, but also actively help protect the climate today. With our gas infrastructure and the ability to make gas greener, we still have great potential. Now we just need to tap it.

WHAT ARE THE FUTURE CHALLENGES FOR VNG?

MR HEITMÜLLER: In an environment that remains challenging, we would do well to vigorously pursue our strategic initiatives. A key challenge will be to achieve further leaps in growth, for example in the area of green gases and biogas, and to integrate the new business. To me, I think a more long-term project will be defining who we are and want to be as a company: What role will VNG play when it comes to balancing a regional focus with global trends? What is our overarching contribution to society? What is it that makes us unique beyond our strategy? These questions will keep us busy for some time. But as my colleague Mr Rodestock said: So far, VNG has always embraced major changes as an opportunity. I'm certain this isn't going to change in the future.

GROUP MANAGEMENT REPORT

for the financial year 2018

STRONG TOGETHER – UNITY IN DIVERSITY


CLEVERTOUCH

GROUP MANAGEMENT REPORT

for the financial year 2018

A. Further on course with a fresh wind of change

In a challenging economic and energy policy environment, the VNG Group's (VNG) expectations with respect to financial year 2018 were substantially exceeded. The positive business development, which already became evident in the second half of the year, was confirmed with an adjusted EBIT of € 159 million and consolidated results of € 142 million. As such, the results also improved in comparison with the prior year in which adjusted EBIT realised totalled € 129 million and Group results of € 71 million were achieved.

All operating areas within VNG contributed to this successful business development. The business area Transport again made a substantial positive contribution to Group results. The business area Trading and Sales utilised its opportunities in terms of results in particular with respect to wholesale trade on the basis of successful portfolio management, an integrated physical sales approach and a strong procurement position. The end-user business remained an important pillar with respect to results. On the back of measures to improve results, the business area Storage was able to, in part, compensate the negative effects from the sustained difficult market environment. However, after twelve years, the business area Exploration & Production (E&P) no longer forms part of the Group. As a result of the sale of VNG Norge AS, positive non-recurring effects were realised in 2018, as a result of which the unadjusted EBIT of € 196 million is significantly more positive than the adjusted EBIT. Finally, the programme initiated in 2015 to increase VNG's profitability also positively impacted business development. The additional earnings targeted in 2020 were already realised in the financial year just ended.

2018 was an anniversary year for VNG as the parent company, VNG AG, became 60 years old. Not only the energy sector fundamentally changed over the course of the last 60 years. VNG transitioned from a state-owned entity to a modern and future oriented group of companies. In 2017 with the "VNG 2030+" strategy, VNG defined its future path on the basis of which the established business areas will profitably and sustainably be further developed and whereby substantial investments will be made in related growth areas. Initial significant results of the implementation of the strategy became evident in 2018. Future topics including power-to-gas, "green" hydrogen and sector linking are increasingly in VNG's focus.

On the basis of its business decisions and development, VNG is making itself fit for the future. The modernised brand profile demonstrates this new self-perception and externally clarifies that which is currently being completed internally: the transformation of the old Verbundnetz Gas into the new VNG.

B. An overview of VNG

1. Business model and implementation of "VNG 2030+" strategy

In the "VNG 2030+" strategy, the Group's goals into the year 2030 and beyond were described and consequentially further developed in financial year 2018. The goal of the strategy is, on the basis of own strengths and the competencies around the energy source (natural) gas, to be a designer of a greener, digital and gas-based future. The established business areas are to be profitably and sustainably further developed. Alongside this, the substantive development of new business areas such as digital infrastructure, biogas and district solutions is envisaged. The sale of VNG Norge AS strengthened the capital base, in

STRONG TOGETHER UNITY IN DIVERSITY

order to consequentially implement the strategic transformation process. VNG's core focus is on the following **business areas and fields**:

Transport: ONTRAS Gastransport GmbH (ONTRAS) operates Germany's second largest long-distance gas grid with a pipeline covering more than 7,000 kilometres and approximately 450 network interconnection points. The infrastructure is an integral component of the European long-distance gas grid. By virtue of the participation in the European gas transport pipeline link EUGAL, ONTRAS is further expanding upon its gas infrastructure. In addition to the transport business, ONTRAS' subsidiaries provide numerous network related services in the unregulated segment.

Storage: VNG Gasspeicher GmbH (VGS) builds, operates and markets underground storage in its facilities in central and northern Germany and had a saleable working gas volume of approximately 2.2 billion m³ at its disposal. Further income is generated via the provision of services. In addition, VGS has a holding in Erdgasspeicher Peissen GmbH (EPG), which operates and is further expanding upon on underground storage "Katharina" near Bernburg (Saxony Anhalt).

Trading & Sales: Due to regulatory requirements, VNG AG's domestic and foreign wholesale trading activities were spun-off into the subsidiary VNG Handel & Vertrieb GmbH (VNG H&V) with effect from 1 January 2018. VNG H&V supplies natural gas to foreign and domestic trading companies, distributors, municipal utilities and other large customers while also offering services around the product natural gas. Alongside the German market, VNG H&V and its foreign trading companies also serve customers in Italy, Austria, Poland and the Slovak Republic. ENERGIEUNION GmbH supplements the activities in Germany with access to the German electricity trading market and its offering with respect to comprehensive portfolio management and settlement services. The domestic and foreign retail business with gas and electricity is organised in additional subsidiaries such as the German goldgas GmbH (goldgas).

Biogas: The Group strategy calls for substantial growth in the biogas area. At the end of 2018, a subsidiary of BALANCE VNG Bioenergie GmbH (BALANCE) acquired a portfolio of five biogas plants in Saxony Anhalt and Lower Saxony. At the same time, the personnel required for the operational management were taken over. The Federal Anti-Trust Authority [Bundeskartellamt] must still agree to the acquisition. On the basis of the new plants, BALANCE supplemented its portfolio of currently eight plants, doubling the installed power to the then approximately 70 MW_{FWL}. Other potential plants are currently being assessed.

Digital infrastructure: VNG's core competence of reliably operating critical infrastructure can also be conferred to the transportation and storage to date. On the basis of various shareholdings, VNG is investing in the expansion and operation of digital infrastructure. As such, GasLINE Telekommunikationsnetzgesellschaft deutscher Gasversorgungsunternehmen mbH & Co. KG is further expanding upon its approximately 12,000 km fibre optic network. GDMcom Gesellschaft für Dokumentation und Telekommunikation mbH provides services in the areas documentation, telecommunication and software. GEOMAGIC GmbH focuses on modern IT solutions and well as energy consulting services. caplog-x GmbH is a specialist for energy related IT services, cloud services, application and data management as well as for computer centres involving critical infrastructure.

Innovation: VNG Innovation GmbH is a strategic partner of now five start-up companies in the energy sector. The focal point of the investments, which were also further advanced in 2018, was in the areas energy efficiency, energy storage, energy conversion, digitalisation, mobility as well as sustainability. In 2018, VNG Innovation Consult GmbH was established to provide consulting services and to further expand the cooperation with the Leipzig SpinLab – The HHL Accelerator.

District solutions: Together with a Leipzig based partner company, VNG ViertelEnergie GmbH supports municipalities in the implementation of holistic solutions with respect to the development of districts. With respect hereto, topics such as the generation of heat, electricity, mobility, telecommunication infrastructure or energy efficiency for spatially separate residential and industrial areas are assessed. Collaboration with real estate project developers was also stepped up. The initial projects will be implemented in 2019. The subsidiary received an energy efficiency prize

from the German Federal Ministry for Environment [Bundesumweltministerium] and from the Federal Ministry of Construction [Bundesbauministerium] for an idea with respect to climate friendly construction and refurbishment of buildings.

2. Financial performance indicators and goals

The strategic realignment of the VNG Group is underpinned by key economic performance indicators and is consistent with the financial strategy. It is geared to sustainable business practices, provides transparent financial guiding principles and reassesses the viability of the strategic direction. In retrospect, in the past, this made it possible to act based on sound judgement which, despite all of the challenges, has provided the Group with a very solid financial starting base. The conclusion of a € 700 million syndicated loan agreement in the financial year just ended did more than just improve the capital base and provide flexibility for action. The successful refinancing also demonstrates the confidence of the financial partners in the future viability of the strategic direction and VNG's good creditworthiness.

VNG's financial strategy is based on the following core goals: appropriate dividends for the shareholders; avoiding risks, which pose a threat to the company; generating positive cash flows; as well as an appropriate rate of return. The Group is primarily managed based on adjusted EBIT. One-time unplannable impacts on results are not considered. Additional financial goals include the cash flow figure, funds from operations (FFO) as well as the amount of the long-term net debt, the equity ratio and capital expenditures. The focus of controlling, monitoring of the quality of the outlook as well as reporting to management, the Supervisory Board as well as the shareholders, is on information with respect to the Group. These figures are compiled on the basis of the regulations of the International Financial Reporting Standards (IFRS).

3. Non-financial performance indicators and goals

In addition to adhering to safety, environmental and quality standards, as well as maintaining the confidence of customers and business partners, the satisfaction of employees is a significant foundation for economic success. This is regularly fostered and assessed by measures to improve the work environment, working hours, the compensation system, health protection and reconciling the interests of family and career. As such, a survey conducted during the financial year indicated that the degree of commitment shown by employees to the company and the Group is well developed and that this has noticeably improved in comparison with the prior year. This commitment is specifically linked to the satisfaction with the employment relationship, the attractiveness of the employer, the level of identification with the company, the motivational environment as well as the competitive and future sustainability.

A further important indicator is work place safety. In 2018 the Group had only one work related accident classified as LTI (Lost Time Injury). Nonetheless, an external assessment identified measures as to how the high level in work protection and health protection can be maintained in Leipzig as well as in the infrastructure areas and how the safety awareness of the employees can be sustainably further improved.

The guiding principles of VNG encompass the common values partnership, openness, entrepreneurship and responsibility. This is intended to provide for confidence and stability. As a regionally positioned company, the VNG Group also supports selected projects and initiatives to strengthen the common good. As such, the VNG Foundation supports projects and initiatives in the areas of science and education, arts and culture as well as philanthropic engagements. For in excess of 17 years, the VNG initiative, "Verbundnetz der Wärme", supported by the VNG Foundation, particularly acknowledges the work and service of volunteers. During the financial year, VNG further increased its financial support for the VNG Foundation in order to more intensively support projects in the region focussed on the environment and social issues. The cooperation

with research and scientific institutions with respect to topics such as the energy sector and climate and structural change are to be concentrated in the Foundation so as to be thematically and regionally expanded. Within the scope of the sponsorship project "ONTRAS.Stadtbekannt [ONTRAS known all over town]", ONTRAS supports specific charitable projects of associations and initiatives and has participated in the foundation for volunteers and civic involvement in Mecklenburg-Western Pomerania.

4. Personnel and organisation development

Personnel and organisational changes: As at 31 December 2018, VNG had a total of 1,101 employees in the Group and thereby continues to be an important employer in the region. As such, the business magazine Focus selected VNG as one of the three best employers in Saxony and one of the ten best in the energy sector in Germany.

In comparison with the prior year (1,154 employees) the change in personnel is primarily attributable to the sale of VNG Norge AS. Simultaneously, in conjunction with the implementation of the "VNG 2030+" strategy, VNG has increased headcount. In addition, due to their growing strategic importance, the companies in the biogas sector were, for the first time, fully consolidated. Within the Group, the employees in VNG AG's wholesale trade area transferred to VNG H&V. As a result of the spin-off of this significant area and in conjunction with the further implementation of the "VNG 2030+" strategy, the cooperation between the controlling, operating and service areas of VNG were further refined. As reflected in the noticeable improvement in employee satisfaction, the personnel and organisational changes introduced within the Group in prior years showed positive effects in the financial year just ended.

In the current process of change, the employees provide important impulses for the future. As such, the workforce developed various initiatives and platforms for innovative ideas for important future topics as well as for the establishment of creative and open working and thinking in everyday operations. The strategic realignment is thereby accompanied by cultural change within the organisation. Employees are thereby intensively addressing digitalisation in an integrated approach, comprising technology as well as the processes, business areas and culture. The Group companies are closely cooperating in this process. In steps, new projects with Group-wide and strategic relevance are being advanced and positive learning experiences are being accumulated. One focal point is on the automation of administrative processes.

Personnel development: One of the focal points with respect to personnel development in the financial year just ended was on the leadership days organised Group-wide for all employees. The focus was on issues of leadership, agile working as well as consequences of digitalisation. Important impulses for discussion were provided by the 180-degree feedback process carried out in 2017 and 2018. Against the background of the changes in the energy sector and demographic change, VNG is pursuing sustainable human resource policies, whereby in addition to supporting the skills and personal competencies of the individual employees, strategic personnel planning is a focal point. The flexibility and willingness of employees to take on new changed tasks as well as the active use of the Group's internal job market is just as important in this process as the needs-based selection of qualified recruits. In this process, VNG is closely cooperating with universities and other scientific institutions in the region. As such, VNG employed three students in 2018 who enrolled in a dual course of study in economics at the Berufsakademie Leipzig.

5. Research and development

A wide range of research and development work is carried out in the subsidiaries ONTRAS and VGS with respect to the modernisation of their technical plants as well as for the development of new innovative, efficient and environmentally friendly technologies. On this basis ONTRAS was, for example, able to substantially reduce gas lost in the course of maintenance by utilising mobile compressors.

Together with partners, the infrastructure entities also assess the technological and economic feasibility of means of utilising the transport and storage equipment for renewable energy. In this manner the linking of the electricity and gas infrastructures via the innovative technology power-to-gas is an important future option for the sustainable, flexible provision of energy. With respect hereto, the Group is also pursuing a number of activities in the areas production, transport, storage and application of hydrogen.

In the upcoming years the focal point of the development of BALANCE will be on the process engineering optimisation of production of biogenic fertiliser on the basis of fermenting substances. In the short-term, in particular the potential to reduce costs by relieving the final storage capacities is to be achieved. By refining the nutrients and thereby improving the regional marketing in the agricultural environment, additional mid- to long-term earnings potential can be realised.

C. Economic report

1. Market environment

Overall economic development: Economic growth in Germany slowed in 2018. The gross domestic product only increased by 1.4 percent in comparison with the prior year. The German federal government expects the economic development to weaken further in 2019.

Development of the energy sector: The use of energy declined by approximately five percent. This was attributable to the mild weather conditions beginning in the second quarter, the increase in raw material prices and efficiency measures. While the share of renewable energy to total energy needs increased further, the demand for conventional energy sources declined. Despite this development, natural gas by far continues to be the most important and most popular energy source in the heating market.

Price development: VNG is subject to a wide range of market-related factors such as the development of raw material prices, exchange rates and the level of interest rates. These factors can have an impact on the development of the business as well as on the valuation of significant assets. At the Dutch trading point TTF, the **gas prices** in 2018 averaged 23 €/MWh and were thereby substantially higher than the prior year level of 17 €/MWh. As a result of the cold spell and the planned disruptions in supply in February/March, the peak gas prices rose to in excess of 100 €/MWh. The storage levels in Europe declined to a very low level. The filling of the storage, higher prices for oil, lignite and emission certificates as well as a reduction of the LNG available in Europe also led to a continuous increase in gas prices in the summer to up to 30 €/MWh. This development only began to tamper off at the start of the fourth quarter. The average **price for Brent** in 2018 amounted to 72 US dollars/barrel, substantially exceeding the 55 US dollar/barrel average level of 2017.

As a result of the gas price development, the **summer-winter spread**, important for the management and measurement of the storage capacities, remained at a historically low level throughout the year. In the cold spell in the middle of March, the spread between the summer and winter of 2018 only amounted to 0.50 EUR/MWh. The **level of interest** also remained very low. The euro, as compared with the **Norwegian krone** as well as the **US dollar**, appreciated. On average, in 2018, the exchange rate amounted to USD 1.18/€, (in the prior year: USD 1.13/€). In 2018 the exchange rate for the Norwegian krone averaged NOK 9.60/€ (in the prior year: NOK 9.33/€).

2. Energy policy framework

At the **national level**, the design of the federal government's coalition agreement as well as the work of the "Commission for growth, structural change and employment", in conjunction with the politically desired withdrawal from coal dominated the energy policy debate. At the end of January 2019, the Commission presented its final report. This encompasses concrete recommendations for an exodus from lignite by the year 2038 as well as for the design and financing of

the structural change in the affected regions. In the Commission's report, the role of natural gas and the gas infrastructure to safeguard the provision of energy is, in principle, positively presented. In concrete terms, the Commission recommends strengthening the role of gas in the generation of electricity, the further development of technologies such as power-to-gas as storage and transportation options and strengthening the links between the sectors heat, mobility, industry and electricity. Special significance could be given to the use of synthetic gas or green hydrogen. In the Commission's final report topics in which VNG is engaged such as digital infrastructure, district solutions and mobility are addressed.

In its own metastudy with respect to the linking of sectors, VNG engaged in the public debates in 2018. In this study, ten current studies by associations, consulting and research organisations were analysed so as to identify robust conclusions and plausible arguments for political decision makers with respect to different strategies in terms of sector linking. The conclusion is a wide consensus that a combination of natural gas and increasingly green gas in conjunction with the gas infrastructure can make an important contribution to the energy transition. VNG controls the required assets, in particular also in the lignite regions affected by the structural change – Lusatia and central Germany – and can thereby be active in this market over the mid- to long-term.

On the **European level** VNG was actively involved in the preparation of a comprehensive legislative package with respect to the design of the European gas market. There is the opportunity to firmly entrench gas with its infrastructure and application opportunities over the long-term in the energy system of the future.

At the **11th German-Russian raw material conference**, VNG again discussed the sustainable use of raw materials giving consideration to the energy transition with representatives from politics, science and business. In the interim, VNG can reflect on a successful energy partnership with Russia which has spanned 45 years.

D. Business development in VNG's business areas

1. Transport

Economic development: Again in 2018 ONTRAS and its subsidiaries were able to make a substantial positive contribution to Group results. As an independent pipeline network operator, ONTRAS has been subject to incentive regulation since 2010. As was the case in the first and second regulatory periods, the Federal Network Agency [Bundesnetzagentur] also confirmed an energy efficiency level of 100 percent to ONTRAS for the periods from 2018 to 2022. The revenue ceiling is slightly higher than the prior year level however the general sector productivity factor of 0.49 percent is below the previous fixed level of 1.5 percent. In addition to the results from the transport business, ONTRAS generated further revenues via its subsidiaries in the unregulated network-related services.

Development and expansion of the network: ONTRAS is currently investing in various regions in eastern Germany in the new construction of individual pipeline sections so as to provide for secure and efficient transport which is viable for the future. In addition, ONTRAS, in conjunction with other German transmission system operators, has committed to regularly provide a joint network development plan for gas to provide for the reliable supply and expansion of the gas infrastructure as needed. With the construction of EUGAL and the associated establishment of pipeline connections to ONTRAS' network, initial expansionary measures result for ONTRAS within the scope of a network development plan. ONTRAS has a 16.5 percent participation in the project and the future leadership of EUGAL, which is currently being built with substantial investments between the Baltic Sea and southern Saxony.

Projects for the climate friendly provision of gas: In 2018 ONTRAS was active in numerous projects to utilise its infrastructure for the transport of green gases and hydrogen. Currently 22 biogas plants, which feed-in up to 180 million m³ of biomethane per year, are connected to the ONTRAS network. As such, ONTRAS transports the highest volume of biomethane of all of Germany's transmission system operators. Two connected power-to-gas plants convert electricity generated on the basis of wind to hydrogen such that this can be fed into the ONTRAS network. A further plant is being planned. ONTRAS would like to advance this technology beyond the pilot phase and to establish this in the market.

2. Storage

Economic development: The seasonal difference between the summer and winter prices for natural gas as a significant indicator for the value of storage capacities remained at a historically low level in 2018. The virtually complete use of stored amounts in the cold spell in the first quarter further intensified the negative development of the summer-winter spread, in particular in the Gaspool market area and thereby the prices and revenues in the storage business year 2018/2019. As a result of the substantial increase in marketing of day ahead capacities in February and March, additional revenues could be generated thereby partially compensating the negative effect. VGS reacted to this development by more rigorously controlling costs, marketing new products and implementing a service business. In 2018 initial positive contributions to results could be realised in the services business.

Development of storage capacities: With its underground storage in locations in central and northern Germany, VGS had a marketable working gas volume of approximately 2.2 billion m³ in 2018. The underground storage was fully utilised in the storage year. Investing activities continued to be characterised by focussed and reduced investments in property, plant and equipment in existing installations as well as by the completion of already contractually committed expansionary plans. VGS is hereby concentrating on its most economical and productive core assets. In Buchholz the dismantling and decommissioning process, which is to be completed in 2022, is on schedule. In 2018 the general engineering work was awarded. Currently, detailed planning and the EU-wide tendering phase are in process. As a result of an economic assessment, the immediate and final decommissioning of the storage in Kirchheilingen was resolved. After removal of the remaining gas quantities, the concept for the dismantling process is currently being developed. The arbitration proceedings initiated in 2014 in connection with a storage project have, in the meantime, been concluded. The results from these procedures, already provided for in prior years, were reflected in the accounts. In 2018, additional caverns were commissioned in EPG's underground gas storage, "Katharina". The underground development work is scheduled to continue through 2024.

3. Trading & Sales

Economic development: The operating business in the business area Trading and Sales substantially improved in 2018. Primarily the **wholesaling** of VNG H&V contributed to this development. In addition to the realisation of classic sales margins, the volatility of the market was, in turn, used to realise additional contributions to results within the scope of active portfolio optimisation. The focus was thereby again on the management of flexible procurement contracts as well as storage and transport capacities, hedging to protect sales margins and using short-term arbitrage opportunities. VNG H&V thereby utilises all opportunities from the cooperation between trade and sales so as to generate successes in the continuing low margin classic sales. Simultaneously, the market situation remains very challenging. Additional income could be realised from the provision of services, primarily for the balancing group management for customers, as well as non-recurring income from the settlement with a customer in price adjustments.

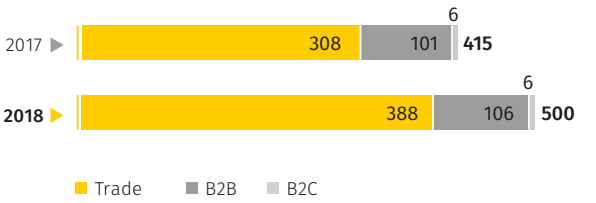
In addition to wholesaling, the **retail business** is an important pillar for results. This portion of the business area is primarily accounted for by goldgas along with the foreign trading companies, which currently supply approximately 98,000 gas customers as well as approximately 94,000 electricity customers in Germany.

In a tight competitive environment with low margins and a high willingness on the part of the customers to change providers, the ultimate supplier achieved positive results. In a ranking by Focus-Money in 2018, goldgas was recognised as one of the fairest gas suppliers in Germany.

Particularly in Poland and Austria, the expansion of the **retail and business customer sales** of electricity and gas **abroad** was below expectations in terms of results. This was primarily attributable to increasing procurement prices. Nonetheless, the customer base could be substantially expanded. The results from the Polish gas distribution network as well as from the Italian Trading and Sales business were, for the most part, stable at the prior year level. The planned expansion of the Italian retail customer portfolio stagnated in 2018 due to the reform of the political environment in Italy.

Development of send-out and procurement quantities: In 2018 VNG's **gas send-out** again exceeded the prior year level (approximately 415 billion kWH) totalling approximately 500 billion kWh.

VNG gas send-out billion kWh*



* Without short-term arbitrage amounts

Despite substantially milder temperatures, sales in the retail customer business (B2C) remained stable. In B2B sales, the send-out in comparison with the prior year could, primarily in Germany, be increased by securing new industrial customers as well as exploiting additional sales channels. VNG's primary sales areas abroad continue to lie in Italy, Luxembourg, Austria and Poland. Gas send-out in the trading area primarily increased as a result of a further increase in hedging and optimisation transactions in a volatile price environment.

VNG's gas **procurement amounted** to approximately 506 billion kWh (in the prior year: approximately 412 billion kWh). The quantities procured from Russian partners within the scope of long-term supply agreements increased by just under 10 percent to approximately 67 billion kWh as compared with the prior year (61 billion kWh). The quantities procured from Norway also increased slightly (2018: approx. 11 billion kWh; in the prior year: approx. 10 billion kWh). The procurement of the remaining gas quantities was completed via bilateral short and mid-term supply contracts as well as within the framework of trading activities in the European spot and futures markets. The mid- to long-term procurement primarily serves to cover the demand of sales customer portfolios. The excess quantities as compared with the total sales quantities were fed into gas storage.

E. Results of operations, financial position and net assets

1. Overall assessment

The goals in terms of results of operations and financial position for financial year 2018 were substantially exceeded. VNG's operating results again substantially improved in comparison with the prior year. An **adjusted EBIT** of € 159 million (in the prior year € 129 million) and consolidated results of € 142 million (in the prior year € 71 million) underline this positive development, which was also supported by the measures already implemented in the programme to increase earnings power. The 2018 unadjusted EBIT of € 196 million is even more clearly positive than the adjusted EBIT and, in particular, also includes the one-time effects attributable to the sale of the E&P business. The effects on earnings from E&P, the business area given up, are separately presented within the income statement. As such, comparability with the prior year is provided for.

Corresponding with the earnings development, **FFO**, which just as clearly demonstrates the operating performance, also improved. By virtue, of the sale of the E&P business, the cash effective divestments, which were not planned in this magnitude, predominate. A more substantial portion of the long-term **net debt** than planned could be repaid thereby strengthening the capital base. In principle, the positive development of results strengthened VNG's equity even though the substantial increase in short-term debt within the scope of the portfolio management reduced the **equity ratio** in comparison with the prior year and the budget due to the balance sheet date.

VNG's **key figures** developed as follows:

€ million	**2018**	2017
Adjusted EBIT*	159	129
Group results	142	71
FFO**	188	175
Cash effective net investments	–62	145
Long-term net debt***	301	456
Equity ratio (%)	22	27

* EBIT adjusted for extraordinary and non-recurring effects on results
** Funds from operations, i.e. consolidated results adjusted for non-cash expenses and income as well as profits/losses from the disposal of fixed assets
*** Net financial liabilities plus pension and dismantling provisions less inventories saleable in the short-term

2. Results of operations

In financial year 2018, VNG's **revenues** of approximately € 11.2 billion were substantially higher than in the prior year (€ 8.2 billion). As was the case in the past, a substantial portion is attributable to the sale of gas and electricity in the business area Trading and Sales. The increase in revenues as well as the **cost of materials** in comparison with the prior year period was attributable to higher prices as well as sale and procurement quantities in the wholesale area. Income and expenses from short-term arbitrage transactions were netted.

The higher **other operating income** (€ 110 million) in comparison with the prior year (€ 57 million) primarily results from the release of provisions as well as from the market valuation of sale and procurement contracts. In the prior year period, this measurement led to expenses, as a result of which the **other operating expenses** (€ 134 million) decreased in comparison with 2017 (€ 158 million). The results of the contract measurement are off-set by realised contributions to earnings in the physical trading business.

Personnel costs (€ 86 million) slightly exceed the prior year amount (€ 84 million).

Amortisation and depreciation (€ 64 million) results primarily from fixed assets in the transport and storage areas. The higher amortisation and depreciation in the prior year (€ 100 million) resulted primarily from extraordinary depreciation of individual storage assets (€ 32 million).

The **investment result** (€ 15 million) deteriorated substantially in comparison with the prior year period (€ 46 million). This change is explained by lower income from investments which are not fully consolidated (decrease of € 11 million) as well as measurement adjustments to the carrying amount of the investments (€ 14 million). In the prior year a reversal of the write-down of an investment (€ 6 million) positively impacted the investment result.

The improvement in the **financial result** (€ –9 million; in the prior year: € –15 million) primarily resulted from lower financing costs due to the lower use made of loans and an improvement in conditions. In contrast, the expenses in conjunction with the unwinding of discounting of provisions remained virtually unchanged.

The **tax expenses** (€ 31 million) comprise ongoing tax expenses of € 14 million and expenses attributable to deferred taxes of € 17 million. The substantial change in the total tax expense in comparison with the prior year (€ 9 million) primarily resulted from additional expenses for deferred taxes as a result of the measurement of derivative financial instruments.

In total, the profits from continuing operations totalled € 84 million (in the prior year: € 46 million). Giving consideration to the profit from the discontinued E&P business operations totalling € 58 million (in the prior year: € 25 million), consolidated net income amounted to € 142 million (in the prior year: € 71 million).

3. Financial position

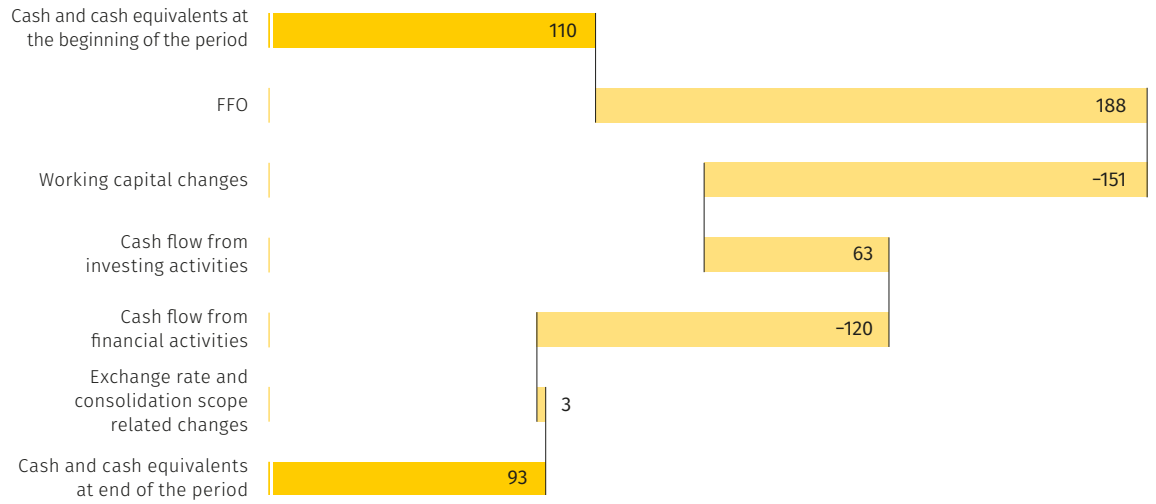
Corresponding with the development of results, the **FFO** (€ 188 million) improved in comparison with the prior year. Off-setting this, the **substantial change in working capital** (€ –151 million) negatively impacted cash flow. In particular, the increase in inventories led to high cash outflows.

Within the scope of the **investing activities** divestments, in particular from the sale of the E&P business, led to cash inflows totalling € 296 million. They overcompensate the substantial disbursements for investments of € 274 million. They primarily relate to the transport network, the acquisition of biogas plants as well as exploration assets up to the point of the final sale of the E&P business. In addition, financing was contributed to EPG for the establishment of the underground storage "Katharina". Within the cash flows from investing activities, cash effective dividends collected (€ 35 million) as well as interest received (€ 6 million) are presented.

With the proceeds from the divestment as well as from the operating activities, financial liabilities to external financing partners of approximately € 64 million were repaid within the scope of the **financing activities**. Interest payments of € 21 million were made. In 2018 a dividend payment for 2017 totalling € 35 million was made.

Giving consideration to exchange rate changes as well as changes in the scope of consolidation (€ 3 million), **cash and cash equivalents** declined from € 110 million to € 93 million. The companies included in the VNG Group were, at all times, able to make payments due.

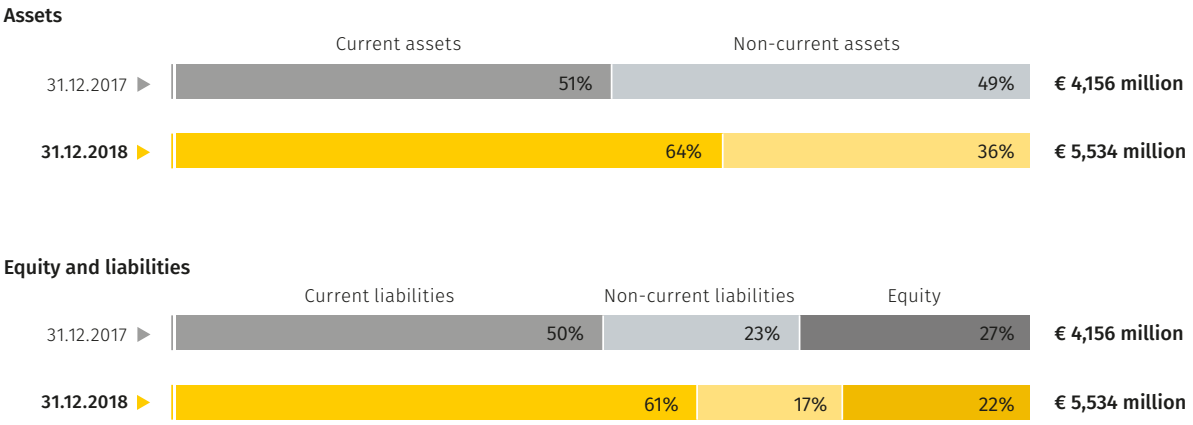
Cash flow from the operating activities of VNG in 2018 € million



4. Net assets

In comparison with the prior year, VNG's **balance sheet structure** developed as follows:

Balance sheet structure



In comparison with the prior year balance sheet date, the **balance sheet total** increased by € 1,378 million respectively 33 percent to € 5,534 million. This substantial change is attributable to a number of, in part, off-setting effects. The **non-current assets** declined due in particular to the divestment from the sale of the E&P assets. In contrast, the **current assets and liabilities** increased as a result of the price development, the increase in inventories, the increase in short-term arbitrage transactions as well as the higher market value of procurement and sales contracts as a result of which the share of current assets and liabilities to the balance sheet total increased substantially in comparison with the prior year.

The total **non-current liabilities** remained virtually unchanged. The decline in non-current provisions – in particular for the dismantling of the E&P assets – is off-set by higher market values of trade contracts. The substantially higher **current liabilities** led to a substantial increase in the balance sheet total and a change in the capital structure. As such, the **equity ratio** declined from 27 percent in the prior year to 22 percent, even though in absolute terms the **equity** was strengthened by the positive Group results.

F. Opportunities and risks report

1. Risk management system

VNG has a comprehensive risk management system, which includes all business areas and Group companies, to continuously ensure that a well-balanced relationship is maintained between opportunities and risks. In addition to the operational measurement and monitoring of risks, a comprehensive inventory is completed twice each year, in which the opportunities and risks of all Group companies are systematically recorded in terms of a deviation from the corresponding budgeted results and are assessed. In addition to the regular risk assessment reporting methods, there is also an ad-hoc reporting system on the basis of defined benchmarks which provides for the early identification of deviations from budget and thereby changes with respect to the opportunities/risks portfolio.

2. Operational opportunities and risks

VNG has established a wide base in its core business areas around the product natural gas thereby providing for new potential beyond natural gas within the scope of the "VNG 2030+" strategy. This positioning provides for the diversification of risks while simultaneously allowing the opportunities in the dynamic market environment to be utilised. Based on the budgeted results, the opportunities and risks profile is also virtually even for 2019. In comparison with the prior year, the sale of VNG Norge AS reduces VNG's overall risk profile. The significant opportunities and risks are market price driven. Above all, this pertains to the development of the summer-winter spread in the Storage area and the price volatility with respect to the raw materials markets in the Trading area. The risks in the infrastructure areas in 2019 are primarily limited to risks associated with operating the technical equipment. For the most part these are, however, covered by insurance.

Other than the general business risks, there are currently no identifiable risks which could have a sustainable substantial impact on VNG's net assets, financial position and results of operations.

Business area Transport: The economic development of ONTRAS is heavily dependent on the regulatory framework and the resulting permissible revenue caps. ONTRAS continues to take advantage of the opportunities provided by the regulated transport market. With its participation in EUGAL, ONTRAS can diversify the sale of its capacities and can reduce the age of its own asset structure. As a result of its holding in EUGAL, ONTRAS has risk exposure as this project is functionally dependent on the project Nord Stream 2. There are also typical project risks such as possible construction delays or a budget increase. As such, ONTRAS has implemented measures to minimise these risks to the extent possible. Likewise, ONTRAS is attentively monitoring the current sanctions by the USA with respect to infrastructure projects in the European energy sector. However, at present, ONTRAS has not identified a higher risk potential.

ONTRAS utilises every opportunity to provide services in the unregulated energy infrastructure area. With a view to the energy policy challenges of a CO_2 neutral energy future, there is a long-term opportunity for the further use of the German gas infrastructure in the step by step conversion from natural gas to renewable gases. By linking the sectors electricity, heating market, mobility and industry, it may be possible to develop an economically useful and cost-efficient solution utilising the gas infrastructure. All activities for the CO_2 neutral provision of gas by 2050 are being bundled under "ONTRAS, going green". ONTRAS continuously carries out required refurbishment and modernisation on the technical equipment so as to achieve the highest possible reliability in the network thereby providing for the gas supply as contractually specified to the downstream networks and end users. The technical safety and availability of the transmission system with the associated equipment was also provided for at all times in financial year 2018. The risks in 2019 are primarily limited to operating the technical equipment.

Business area Storage: The intensity of competition has, among others, led to an increasing share of short-term storage bookings. The volatile and simultaneously declining market price developments lead to uncertainty with respect to the future sale of storage capacities and the revenues attainable from these capacities. With respect to 2019, these risks are, however, low as a substantial portion of the storage capacities have already been sold. VGS is addressing market developments with product innovations, demand-oriented investment decisions, decommissioning storage facilities, which are not efficient or economically viable such as those in Buchholz and in Kirchheilingen, as well as measures to improve efficiency. As a reaction to the demand situation, cost structures are being further optimised and the organisation is being structured more in line with market requirements and additional revenues are being generated from the service business. In addition, there are opportunities to utilise the existing infrastructure as storage for renewable energy. As is the case in the business area Transport, in 2019 risks from the operation of the technical equipment account for the bulk of the risk profile. For the most part, these are, however, insured. Furthermore, the ongoing maintenance

and monitoring of the underground gas storage on the basis of technical as well as internal regulations along with the regular assessment of the condition of all underground and surface equipment, provide for a high technological safety standard consistent with mining law. VGS' high quality standards are provided for on the basis of annual training plans designed to provide for the ongoing qualification of the workforce and service providers as well as regular internal and external audits.

Business area Trading & Sales: Opportunities and risks in VNG H&V's trading business are primarily attributable to price volatility with respect to the raw material markets. Along with changes in the market price level, price differences between the European gas trading hubs and price spreads between seasonal forward products are important risk factors. In addition, temperature developments – in particular in the winter period – can have an impact on trading results. The positions in procurement and sales contracts are pooled in a complete portfolio, continuously monitored and managed. In addition to natural hedging effects within the portfolio, specific hedging strategies are used to limit negative developments with respect to results. These take account of the respective risk factors and may include derivative financial instruments. The activities in the business area Trading are carried out giving consideration to a concrete risk and loss limiting framework for operating activities. On the basis of the budgeted results, the proportion of opportunities and risks in 2019 is virtually even. With respect to the specified risk factors, maximum deviations from budgeted earnings could be at the lower double-digit million-euro level.

VNG H&V has a structurally diversified procurement portfolio closely aligned to the market. The existing contracts primarily serve to cover the sales position. On the sales side, VNG H&V continuously develops new products and develops additional distribution channels in the traditional wholesale business. In addition, H&V consistently and continuously utilises the market opportunities as well as those in the spot and future markets to optimise the overall portfolio.

The most significant credit risks result from natural gas supply and trading contracts with national and international business partners. Credit risks also result from financial instruments concluded to hedge exchange rate risk as well as raw material price risk positions. Assessments as to the creditworthiness of business partners (customers and suppliers, trading partners as well as financial institutions) are made within the scope of established credit risk management on the basis of available information using processes customary in the market. They are also continuously monitored. Credit risks are managed using common safeguarding instruments (e.g., guarantees). In addition, the customer portfolio is covered by a credit risk insurance policy.

VNG is subject to energy and financial market regulation. The effectiveness and appropriateness of the systems to satisfy the requirements pursuant to EMIR (European Market Infrastructure Regulation) are annually certified by an independent accounting firm. Appropriate IT systems have been installed to satisfy the requirements of MiFiD II (Markets in Financial Instruments Directive), MAR (Market Abuse Regulation) and REMIT (Regulation on Energy Market Integrity and Transparency).

The retail customer supplier, goldgas, operates in a challenging competitive environment with low margins and high customer churn rates. This can have a negative impact on the customer base as well as sales. Simultaneously, goldgas considers there to be opportunities in new sales channels, in the continuous optimisation of processes as well as in energy related services. As a result, the establishment of innovation management and systematic product development is being pursued.

Further development of IT systems: The Group's operating business and the continuous changes in the framework conditions result in substantial requirements in terms of stability, reliability and adaptability of the business processes. On the basis of continuous monitoring of processes and the further development of business IT systems, the Group provides for a high degree of process reliability and is constantly working on further improvements.

3. Compliance management system

The Group companies are integrated in the Group-wide compliance management system (CMS). This system seeks to ensure that all employees conduct themselves in compliance with all legal requirements so as not to pose a risk to confidence from the perspective of customers, business partners, shareholders and the general public. In addition to organisational precautions and regulations, there is also an extensive reporting system as well as targeted training for employees. The effectiveness and appropriateness of the CMS was assessed and certified by an independent auditing company. Pursuant hereto, the regulations and measures of the CMS are deemed suitable, to provide reasonable assurance that risks with respect to significant violations of laws and internal regulations in the areas corruption prevention, cartel law and trade regulation within the Group are identified in a timely manner as well as to prevent such violations of regulations.

4. Financial risk management

VNG is, in particular, exposed to risks from changes in raw material prices, exchange rates and interest rates as well as credit risks. The fundamentally conservative orientation is reflected in systematic financial risk management. Market and follow-up functions such as financial risk management are organisationally segregated.

The sole purpose of the standard derivative financial instruments used as part of financial risk management is to hedge existing risks in underlying transactions. Commodity futures of the trading companies are used to manage price risks arising from gas procurement and sales contracts. Statistical risk measures are utilised for the daily measurement and monitoring of these risks and to limit potential changes in the present value of the trading portfolio. To the extent possible, all of the Group's foreign currency exposure is concentrated and completely hedged within the parent company. Contracts with Group companies outside the Eurozone are, in principle, concluded in the local currency of these companies. Foreign currency future contracts and natural portfolio hedging are the primary hedging instruments. VNG has an active interest rate risk management in which all interest risks are regularly assessed. Derivative financial instruments are also used for management purposes. As a result of adequate liquidity reserves in the form of committed credit lines as well as by optimising the allocation of liquidity within the Group, solvency is provided for at all times. The core financing elements are a sound line of credit and promissory note loans with various financing partners. The multi-year rolling liquidity plan regularly determines the future peak financing requirements, which, as of the balance sheet date, even under risk scenarios, were covered by adequate financing sources.

G. Outlook

VNG is resolutely continuing on its path: VNG believes it has an important role in the transformation process of the German gas sector. Simultaneously, it is VNG's task to commercially successfully carry out its operating business and to further develop this. To remain on course, the new strategy will consequentially also be implemented in 2019. For this reason, the investing activities will focus on the core business in the gas sector as well as on the establishment of new business areas such as biogas, digital infrastructure and district solutions. The long-term goal is to develop VNG to a more diversified, green, digital Group with a strong gas sector core.

The implementation of the strategy includes ambitious investing policies with the target sustainable operations. The active management of opportunities and risks is intended to provide for VNG's financial stability. The sale of VNG Norge AS led to a reduction of VNG's overall risk and to an improvement of the capital base for the implementation of the strategy. In addition, transparent financial guidelines allow for the continuous assessment of the sustainability of the strategic direction.

For 2019 VNG has budgeted a slightly lower adjusted EBIT in the lower three-digit million euro range as well as consolidated results in the mid double digit million-euro range. Stable results are again expected in the business area Transport in 2019. In the business area Storage, slightly higher summer-winter spreads lead to an improvement in the results of operations. Opportunities lie in structural market changes. This also applies in the business area Trading and Sales, in which the sales market remains extremely competitive. As demonstrated in the financial year just ended, the wholesale markets provide opportunities which must, however, be newly utilised each year. The retail business remains an important pillar for earnings in the target markets Germany, Poland, Austria and Italy.

Strong financial base for the further strategic implementation: Due to the increasing investing activities in the business areas Transport and Biogas in particular, a justifiable increase in the debt level is to be expected in 2019. As was the case in the past, the development and measurement of working capital levels in the trading business due to the balance sheet date may be subject to substantial volatility and will continue to have a decisive influence on Group debt, the balance sheet total and thereby also on the equity ratio. As per the budget, the ratio is again expected to increase slightly. In comparison with 2018, the FFO will decline analogous to the development of results.

Fundamental political decisions as well as elections in Germany and the EU: At the federal level, the design of a climate protection law will significantly determine the energy policy agenda in 2019. For the first time, binding climate protection goals will be established for the sectors electricity, heat, commerce, industry, and agriculture and measures will be established to achieve these goals. In addition, the upcoming state elections in Saxony, Brandenburg and Thuringia as well as the associated topics around the exodus from lignite and the design of the structural change will impact the political discussions in the affected regions and, last but not least, in eastern Germany. In the elections at the European level in 2019, the course will be set in terms of topics and the further development of the European Union in the upcoming five years. The energy policy agenda of the then newly constituted EU institutions will include, among other things, the format and enactment of a comprehensive legislative package with respect to the future European gas market design. As was the case in prior years, VNG will intensively participate in the discussions with respect to energy policy as well as climate policy issues at all political levels thereby emphasising, on the basis of documentable facts, the advantages of gas and the gas infrastructure to guarantee the reliability of supply, climate friendliness as well as economic efficiency.

In 2019, a look back at the past is, however, also warranted. 30 years ago, the people in Leipzig and other cities in the German Democratic Republic took to the streets for a reunified Germany. On 9 November 1989 the Wall fell. The years of upheaval in 1989 and 1990 also characterised VNG. In the course of the reunification of Germany, the state-owned enterprise VNG – Verbundnetz Gas AG (today's VNG AG) was established, the first completely privatised company in eastern Germany. This established the foundation for the development to today's VNG. In the future, VNG will also benefit from its experiences over the last three decades.

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEET OF THE VNG GROUP

as at 31 December 2018

Assets

€ million	Notes	31.12.2018	31.12.2017
Non-current assets		**1,978.1**	**2,024.3**
Intangible assets	1	9.5	44.9
Property, plant and equipment	2	1,362.1	1,423.6
Entities accounted for using the equity method		188.5	188.3
Other financial assets	3	190.8	224.6
Derivative financial instruments		182.6	84.3
Other non-current assets		37.0	2.8
Deferred taxes		7.6	55.8
Current assets		**3,556.0**	**2,131.3**
Inventories	4	423.0	250.8
Financial assets		0.5	0.3
Trade receivables	5	2,100.2	1,366.2
Income tax receivables		17.4	21.3
Derivative financial instruments		850.0	325.6
Other current assets	6	71.6	56.8
Cash and cash equivalents		93.3	110.3
Total assets		**5,534.1**	**4,155.6**

Equity and liabilities

€ million	Notes	31.12.2018	31.12.2017
Equity		**1,223.2**	**1,106.0**
Subscribed capital		328.0	328.0
Revenue reserves		753.6	705.5
Group net income attributable to the controlling interest		142.0	70.6
Cumulative changes not affecting income		−6.0	−4.4
Non-controlling interests		5.6	6.3
Non-current liabilities		**940.6**	**948.9**
Provisions	7	454.2	558.8
Deferred taxes		33.5	15.0
Financial liabilities		216.5	224.9
Trade payables	8	0.3	0.2
Derivative financial instruments		221.7	133.3
Other liabilities and subsidies	9	14.4	16.7
Current liabilities		**3,370.3**	**2,100.7**
Provisions	7	89.4	116.3
Financial liabilities		88.9	137.0
Trade payables	8	2,164.3	1,357.0
Income tax liabilities		49.9	37.3
Derivative financial instruments		869.3	351.5
Other liabilities and subsidies	9	108.5	101.6
Total equity and liabilities		**5,534.1**	**4,155.6**

CONSOLIDATED INCOME STATEMENT OF THE VNG GROUP

for the period from 1 January to 31 December 2018

€ million	Notes	01.01. to 31.12.2018	Adjusted*: 01.01. to 31.12.2017	Reported: 01.01. to 31.12.2017
Revenue	10	11,219.1	8,243.6	10,324.4
Change in inventories		1.3	0.4	0.4
Other own work capitalised		2.5	2.4	2.4
Other operating income		110.4	56.6	93.4
Cost of materials	11	–10,941.7	–7,937.6	–9,975.4
Personnel expenses	12	–85.5	–83.9	–89.7
Other operating expenses		–133.9	–157.6	–164.5
Amortisation and depreciation	13	–63.6	–99.8	–133.6
Investment result	14	15.0	46.0	46.0
Financial result	15	–8.9	–14.6	–7.9
Income taxes	16	–30.9	–9.3	–24.5
Income from continuing operations		**83.8**	**46.2**	**–**
After tax earnings from discontinued operations		**58.5**	**24.8**	**–**
Group net income		**142.3**	**71.0**	**71.0**
a) of which results attributable to non-controling interests		*0.3*	*0.4*	*0.4*
b) of which results attributable to the shareholders of VNG AG		*142.0*	*70.6*	*70.6*

* Adjustment comprises the separate presentation of the results of the E&P business as discontinued operations as well as the netting of income and expenses from arbitrage transactions

BASIS OF PREPARATION AND EXPLANATIONS ON THE CONSOLIDATED FINANCIAL INFORMATION OF THE VNG GROUP

I. General principles

The VNG Group (hereafter: "VNG") is a group of companies with activities throughout Europe which has a wide sustainable service portfolio in gas and infrastructure. Along the gas value-added chain, VNG concentrates on three business areas – Transport, Storage as well as Trading and Sales. From this core competency in gas, VNG is increasingly focusing on new business areas with the "VNG 2030+" strategy. Among others, this includes biogas, digital infrastructure and district solutions. VNG AG (until 29 March 2018: VNG – Verbundnetz Gas Aktiengesellschaft), as parent company, is registered in the Leipzig Commercial Register under number HRB 444. The Company is domiciled in Leipzig, Germany. The address is VNG AG, 04347 Leipzig, Braunstraße 7.

Other than with the following exceptions, this consolidated financial information was prepared in accordance with the International Financial Reporting Standards (IFRS) as they are required to be applied in the European Union (EU) as at the balance sheet date as well as by giving consideration to the Interpretations as published by the IFRS Interpretations Committee (IFRS IC). Other than the exceptions presented, the consolidated financial information thereby corresponds with the IFRS and Interpretations as published by the International Accounting Standards Board (IASB) to the extent these have been taken over into EU law.

The deviations to IFRS are described below:

- This consolidated financial information solely consists of the consolidated balance sheet and the consolidated income statement. As a supplement hereto, these disclosures and explanations were prepared, comprehensively describing the basis of preparation of the consolidated financial information.
- This consolidated financial information thereby does not comprise complete consolidated financial statements with all of the financial statement components and disclosures as required by IFRS.
- In the measurement of gas delivery contracts with flexibility in terms of quantities, which were concluded with customers without direct market access, the determination of the fair value of the contracts is based on the expected delivery quantities as determined by the customers' projected physical demand. Had the flexibility in terms of quantities not been applied, the consolidated results would have been approximately € 1.4 million lower.

In the course of the compilation of the consolidated financial information, discretionary decisions and estimates must be made in the application of accounting policies and measurement methods. These could affect the presentation and measurement of reported amounts for the assets and liabilities, the expenses and income as well as contingent liabilities. These comprise complex and subjective assessments as well as the application of assumptions which are, by nature, subject to uncertainty as well as change with the passage of time.

The consolidated financial information was prepared applying the **going concern** assumption. Amounts are presented in € million. Amounts were rounded in accordance with standard commercial practice; this may lead to rounding differences.

To improve transparency, line items on the consolidated balance sheet and the consolidated income statement are presented in a summarised manner. The consolidated income statement was prepared in the total cost format.

In financial year 2018, VNG AG sold its shareholding in VNG Norge AS and has thereby discontinued its operations in the business area Exploration & Production. In the consolidated income statement, the after-tax results of the discontinued business area are presented separately. The prior year amounts in the consolidated income statement were presented as if the business area Exploration & Production had been discontinued from the start of the comparable prior year period.

To present the development of the business more appropriately, income and expenses from arbitrage transactions are presented net within revenues. This led to the off-setting of revenues and costs of materials totalling € 6,329 million. The prior year amounts were, correspondingly, adjusted. The effect of the netting in the prior year totalled € 2,016 million. As such, the prior year adjusted revenues total € 8,244 million and the adjusted costs of materials total € 7,938 million.

The consolidated income statement was extended by one column with the adjusted prior year amounts.

The consolidated financial information is prepared on the balance sheet date of the financial statements of VNG AG. VNG AG's financial year is the calendar year.

II. Information on the consolidated financial information

1. New accounting regulations

The application of new standards/interpretations respectively modifications has as a prerequisite that they are approved by the EU in the course of IFRS endorsement procedures. These standards and interpretations are only applied by VNG at such point when their application is required and the endorsement by the European Commission has taken place.

In July 2014, the IASB published IFRS 9 "Financial Instruments", which is to be applied for financial years starting after 1 January 2018. Pursuant to the transition regulations of IFRS 9, adjustment of prior year figures is not required. The regulations of the standard include a new model for the classification of financial assets and financial liabilities. The incurred loss model previously in effect has been replaced by the more future oriented expected credit loss model. The conversion effects which result from the initial application were recorded in equity without an impact on profit and loss. Furthermore, the risk provisioning resulting from the expected credit loss model has increased.

In financial year 2018, VNG initially applied IFRS 15 "Revenue from contracts with customers". With respect to the initial application in the consolidated financial information, the modified retrospective approach was applied whereby the standard is only applied to the most recent reporting period presented within the financial information. The comparative period 2017 is presented on the basis of the regulations of IAS 18. The initial application did not have a significant effect on the components of the consolidated income statement.

2. Consolidation

2.1 Principles of consolidation

The financial statements of the domestic and foreign subsidiaries included in the consolidation were prepared in a uniform manner in accordance with the accounting policies which are applicable at VNG. These are presented in Section 3.

Receivables, liabilities and provisions between consolidated companies are netted. Intercompany income is off-set against the corresponding expenses. Intercompany profits and losses are eliminated unless they are of minor importance.

In accordance with the full consolidation method, all subsidiaries directly or indirectly under the control of VNG AG are included. VNG AG controls an associate if it is exposed to risks or has rights to variable returns as a result of its involvement in the associate and the Group can exercise its control over the associate in a manner that affects the level of the returns from the associate. In the full consolidation process, the assets and liabilities of a subsidiary are, in their entirety, included in the consolidated financial information.

The equity method is applied when there is a joint arrangement in the form of a joint venture or when a significant influence may be exercised over the business policies of the associate, but the entity does not qualify as a subsidiary. At the time of acquisition, it is recorded at acquisition costs and in subsequent periods at the amortised prorated net assets. The carrying amounts are increased or decreased each year reflecting the prorated results, dividends distributed and other changes to equity. This means that when shareholdings are measured, only the company's proportional equity, rather than its assets and liabilities, is presented in the consolidated financial information. Any goodwill is included in the stated value of the shareholding. Negative differences are recognised in profit or loss in the investment result.

Holdings in subsidiaries, joint ventures or associates which, from the Group's perspective, are of minor significance for the net assets, financial position and results of operations, are not consolidated or included on the basis of the equity method. Revenues and results are used as indicators for determining the significance of such companies.

2.2 Scope of consolidation

A total of 18 companies (in the prior year: 15) are included in VNG's consolidated financial information as **fully consolidated companies**.

An overview of the fully consolidated companies is presented below:

Shareholding in %	Name and registered office of the company
Holding	
100.00	VNG AG, Leipzig
Transport	
100.00	ONTRAS Gastransport GmbH, Leipzig
Storage	
100.00	VNG Gasspeicher GmbH, Leipzig
Trade	
100.00	VNG Handel & Vertrieb GmbH, Leipzig
100.00	ENERGIEUNION GmbH, Schwerin
100.00	G.EN. Gaz Energia Sp. z o.o., Tarnowo Podgórne, Republic of Poland
100.00	goldgas GmbH, Eschborn
100.00	goldgas GmbH, Vienna, Austria
100.00	HANDEN Sp. z o.o., Warsaw, Republic of Poland
80.00	SPIGAS S.r.l., Milan, Italy
100.00	VNG Austria GmbH, Gleisdorf, Austria
100.00	VNG Energie Czech s.r.o., Prague, Czech Republic
100.00	VNG-Erdgascommerz GmbH, Leipzig
100.00	VNG Italia S.r.l., Bologna, Italy

Shareholding in %	Name and registered office of the company
Biogas	
100.00	BALANCE VNG Bioenergie GmbH, Leipzig
100.00	BALANCE Erneuerbare Energien GmbH, Leipzig
100.00	Leipziger Biogasgesellschaft mbH, Leipzig
100.00	MBG Mitteldeutsche Biogasgesellschaft mbH, Leipzig

In the reporting period there were the following changes in the scope of consolidation:

VNG Norge AS was sold in financial year 2018. In conjunction with the completion of the transaction as at 28 September 2018, the entirety of the shareholding in VNG Norge AS and thereby also the shareholding in the subsidiary, VNG Danmark ApS, transferred to the purchaser. VNG Norge AS and VNG Danmark ApS were, correspondingly, deconsolidated upon completion.

With economic effect as at 1 January 2018, VNG AG spun-off the entirety of the business area "Wholesale" transferring all associated assets and liabilities as well as all employment relationships, subsidiaries and other holdings in companies to VNG Handel & Vertrieb GmbH (VNG H&V). As a result of the full consolidation of VNG H&V from 1 January 2018, there was no impact on the comparability of the consolidated financial information with that of the prior year as a result of the spin-off.

In conjunction with the expansion of the biogas activities within the scope of the "VNG 2030+" strategy, the biogas companies were, for the first time, included in VNG's consolidated financial information due to their growth in strategic importance. Within the scope of the initial inclusion, as at 1 January 2018, five companies in the Biogas segment were fully consolidated.

One of the companies was merged into BALANCE Erneuerbare Energien GmbH in 2018. The initial consolidation did not lead to any significant effects in VNG's consolidated financial information.

14 affiliated companies (in the prior year: 17) are not included in this consolidated financial information as a result of their being of minor significance.

Associated companies

Entities in which VNG holds voting interests of at least 20 percent and a maximum of 50 percent or in which management and supervisory functions can substantially be influenced, are included on the basis of the equity method. As was the case in the prior year, four associated companies are included on the basis of the equity method.

An overview of the entities included on the basis of the equity method is presented below:

Shareholding in %	Name and registered office of the company
25.10	EMB Energie Mark Brandenburg GmbH, Potsdam
50.00	Erdgasspeicher Peissen GmbH, Halle (Saale)
23.39	GasLINE Telekommunikationsnetzgesellschaft deutscher Gasversorgungsunternehmen mbH & Co. Kommanditgesellschaft, Straelen
24.60	MITGAS Mitteldeutsche Gasversorgung GmbH, Halle (Saale)

In comparison, 14 (in the prior year: 13) other associated companies were not included in the consolidated financial information as they are of minor significance for the presentation of a true and fair view of the net assets, financial position and results of operations.

2.3 Acquisition accounting

Business combinations are accounted for applying the acquisition method. The acquisition costs of an acquired entity are measured based on the fair value of the assets transferred and liabilities assumed or entered into as of the acquisition date. Non-controlling interests are measured at the proportionate fair value of the identifiable assets and the liabilities assumed. Incidental acquisition costs are expensed when they are incurred. In a business combination achieved in stages, the acquisition-date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to the fair value on the date control is obtained by the acquirer and the resulting gain or loss is recognised in profit or loss. Any excess of the acquisition cost of the business combination plus the amount of any non-controlling interests in the acquiree over the acquired identifiable assets, assumed liabilities and contingent liabilities is reported as goodwill if positive or, if negative, is reassessed and recognised through profit and loss.

A change in the ownership interest in an entity which continues to be fully consolidated is accounted for as an equity transaction. All remaining interests are remeasured at fair value upon loss of control.

2.4 Foreign currency translation

In the stand-alone financial statements, the companies account for transactions in foreign currencies using the exchange rate in effect on the date of the transaction. On the balance sheet date, non-monetary items are measured at the rate prevailing when they were first recorded. Monetary items are translated at the closing rate as of the balance sheet date. Exchange differences from monetary items allocable to operating activities are recognised through profit or loss in other operating income or other operating expenses. Translation differences from financing activities are disclosed in the financial result.

VNG's reporting currency, which is also the functional currency, is the euro. Currency translation is performed in accordance with IAS 21 "The Effects of Changes in Foreign Exchange Rates" using the modified closing rate method. Under this method, the assets and liabilities of entities that do not report in euro are translated at the mean rate prevailing on the balance sheet date, while expenses and income are translated at the average annual rate. The companies impacted are economically independent foreign subunits. Differences arising from the foreign currency translation of assets and liabilities compared to the translation of the previous year, as well as exchange differences between the income statement and the balance sheet, are recognised directly in equity within other comprehensive income with no impact on profit and loss.

The following exchange rates served as the basis for the foreign currency translation:

	Rate on the balance sheet date		Average rate	
1 €	**31.12.2018**	31.12.2017	**2018**	2017
Danish krone	n/a	7.44	7.45*	7.44
Norwegian krone	n/a	9.84	9.59*	9.33
Polish złoty	4.30	4.18	4.26	4.26
Czech koruna	25.72	25.54	25.64	26.33
US dollar	1.14	1.20	1.18	1.13

* Average exchange rate from 1 January to 28 September 2018

2.5 Discontinued operations and assets held for sale

Discontinued operations are to be presented as soon as a portion of the business is classified as held for sale. VNG presents assets and liabilities as one or more disposal group(s) when these are to be sold or surrendered in a transaction or in another manner. In the case of the discontinuation of a business area, the results of discontinued activities are separately presented in the consolidated income statement, separate from income and expenses of continuing activities.

3. Significant accounting policies and measurement methods

3.1 Intangible assets

Intangible assets acquired for consideration (excluding goodwill) are carried at amortised cost respectively production costs and are amortised using the straight-line method based on their individual economic useful life.

As at the reporting date, there was no goodwill acquired for consideration nor were there internally developed intangible assets.

The useful lives and amortisation methods are regularly reviewed.

3.2 Property, plant and equipment

Property, plant and equipment is measured at amortised cost respectively at production costs. Acquisition respectively production costs comprise all direct costs incurred to render the asset operational.

Property, plant and equipment subject to wear and tear are depreciated using the straight-line method over the expected useful life of the individual components. Depreciation is recorded pro rata temporis in the year of the addition.

Repair and maintenance costs are recorded as expenses. Renewal and maintenance expenses which lead to future economic benefits of an asset are capitalised.

Investment subsidies are not deducted from the acquisition respectively production costs of the corresponding assets, but rather are deferred on the equity and liabilities side of the balance sheet within the line item other liabilities and subsidies.

Corresponding with the net present value of decommissioning or disposal obligations, the so-called decommissioning assets are capitalised and subsequently depreciated on the straight-line basis in future periods.

The scheduled depreciation of major items of property, plant and equipment is calculated using the following uniform Group-wide useful lives:

Balance sheet line item	Useful life in years
Buildings	25 – 100
High pressure pipelines	55
Caverns for gas storage	40
Gas distribution equipment	10 – 55
Production equipment	Dependent on production
Other equipment as well as operating and office equipment	4 – 14

Useful lives and depreciation methods are regularly reviewed.

Property, plant and equipment are either derecognised upon disposal or when no further economic benefits are expected from their continued use or sale. The gain or loss arising on derecognition of the asset (calculated as the difference between net

disposal proceeds and the carrying amount of the asset) is included in profit and loss in the income statement in the period in which the asset is derecognised.

3.3 Borrowing costs

If it takes a substantial period of time (more than twelve months) to acquire or produce a qualifying asset and to get it ready for its intended use, the directly attributable borrowing costs incurred until such time as the asset is ready for its intended use are capitalised. Where there are specific debt financing arrangements, the respective borrowing costs incurred are used.

3.4 Leases

A lease is an agreement whereby the lessor conveys to the lessee the right to use a specific asset for an agreed fixed period of time in return for a payment or a series of payments. This also applies for agreements that do not explicitly describe the conveyance of such a right. Leases are classified either as finance leases or as operating leases.

Leases where VNG as **lessee** has substantially all of the risks and rewards of ownership of the leased asset are classified as finance leases. The leased asset is recognised at the lower of the fair value and the present value of the minimum lease payments. A liability is recorded for the same amount.

The recognised leased asset is subject to scheduled depreciation over the shorter of its economic useful life and the lease term. The liability is repaid and carried forward in subsequent periods using the effective interest method.

All other leasing relationships in which VNG is lessee are classified as operating leases. Lease payments respectively rental payments for operating leases are directly recognised as an expense in the income statement.

Leases in which VNG is **lessor** only exist in the form of operating leases. The leased asset remains in the consolidated balance sheet and is subject to scheduled depreciation. The payments made by the lessee are recognised as income on the straight-line basis over the term of the lease.

3.5 Impairments

The carrying amounts of intangible assets as well as property, plant and equipment are tested for indications of impairment at each balance sheet date. If there is any indication that the asset may be impaired, the recoverable amount of the asset is determined within the scope of the impairment test. The recoverable amount is the higher of the fair value less costs to sell and the value in use.

The fair value is determined on the basis of a business valuation model and reflects the best possible estimate of the amount at which an independent third party would acquire the asset. The value in use corresponds with the present value of the future cash flows on the basis of the earnings and financial planning. This is the value which is expected to be derived from an asset or cash-generating unit. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows which are largely independent of the cash inflows from other assets or groups of assets.

If it is not possible to determine the recoverable amount for an individual asset, the recoverable amount is determined for the cash-generating unit to which the asset can be allocated.

If the recoverable amount of an asset falls short of its carrying amount, an impairment loss is immediately recognised in profit and loss.

If the reason for a previously recognised impairment loss no longer exists at a later date, the impairment loss is reversed through profit and loss. The upper limit is the carrying amount that would have been determined had no impairment loss been recognised in the past (amortised acquisition respectively production costs).

In addition to technical progress and damage – in particular for natural gas storage – changes in expectations as to short-term, mid-term and long-term summer-winter spreads as well as changes in the expected decommissioning costs could lead to impairments respectively reversals of impairments.

3.6 Non-current financial assets

Investments in non-consolidated affiliated entities as well as those in associates not accounted for using the equity method are measured at amortised cost. If there is a permanent or significant impairment as at the balance sheet date, the adjustments to the market value are recognised in profit and loss.

Other investments are recorded at their fair value. These assets primarily comprise other investments, which are not traded on an active market.

Investments in associated companies are recorded at acquisition costs at the time of acquisition and subsequently recognised according to the amortised prorated net assets. The carrying amounts are increased or decreased on an annual basis reflecting the prorated results, dividends distributed or other changes in equity.

Loans are accounted for at amortised acquisition cost after deducting any required impairment charges as determined giving consideration to actual risk of default. Loans subject to market interest rates are recognised at their nominal value.

3.7 Inventories

The predominant portion of the inventories are acquired for trading purposes and are measured at their fair value less costs to sell. This relates to the gas inventories intended for trading purposes. The spot price as at the balance sheet date is used in the determination of the fair value.

The other inventory is recorded at acquisition respectively production costs. As a rule, it is measured at average prices. Where necessary, the lower of the net realisable value and the carrying amount is recorded. Reversals of impairment losses on inventories are deducted from the cost of materials.

3.8 Energy efficiency certificates

Energy efficiency certificates acquired for own use and for trading purposes are presented within inventories at acquisition costs. As at the balance sheet date, the energy efficiency certificates are either recorded at acquisition costs or, if necessary, at their lower net sales proceeds.

Pollutant emission rights obtained free of charge are included within inventories at a notional value.

3.9 Trade receivables and other assets

Trade receivables and other assets are accounted for at acquisition cost less any required bad debt allowances, based on the actual risk of default. The amount of the bad debt allowance is hereby based on estimates and assessments of individual receivables, based on the maturity structures of the receivable balances, the creditworthiness of the customers, experience with respect to write-offs of receivables in the past and changes in payment conditions. The trade receivables all have short remaining terms. As such, as at the balance sheet date, their carrying amounts approximate their fair values.

The receivables include a contingent sales price payment from the sale of shares in VNG Norge AS. This sales price payment is dependent on the occurrence of defined conditions which are primarily associated with the timely development of resources in field developments. As at the balance sheet date, the present value of the expected amount was recorded. The discounting was based on an interest rate appropriate for the term.

3.10 Provisions for pensions and similar obligations

For defined benefit plans, provisions for pensions and similar obligations are determined using the projected unit credit method in accordance with IAS 19. In addition to the known pensions and entitlements as at the balance sheet date, this method also considers future anticipated salary and pension increases. Actuarial gains and losses are recorded in their entirety in the financial year in which they arise. They are reported outside of the income statement as part of the cumulative changes not impacting profit and loss and are directly recorded in equity. They do not impact profit and loss in future periods. The service cost is disclosed in personnel costs, while the net interest portion of additions to the provision is recorded in the financial result.

Provisions for semi-retirement obligations, comprising other long-term services to employees, were also considered and primarily reflect the top-up amounts to be paid.

3.11 Other provisions

The other provisions take account of all legal or constructive obligations to another party resulting from past events that are identifiable as at the balance sheet date, to the extent that it is probable that they will lead to an outflow of resources in the future and their amount can be reliably estimated. The provisions are recognised at their settlement amount. They are measured at the estimated future amount respectively at the amount deemed most likely to be incurred.

Provisions for onerous contracts are recorded when the unavoidable costs to settle the contractual commitments exceed the expected economic benefits.

The non-current provisions are presented at their discounted settlement amount as at the balance sheet date. This does not apply to provisions for pensions and similar obligations. They are subject to special regulations pursuant to IAS 19.

3.12 Deferred taxes

Deferred taxes are recorded in accordance with the temporary concept (IAS 12) on all timing differences between the tax balance sheet and the IFRS balance sheet of the individual entities. Deferred taxes from consolidation entries are recognised separately. Deferred tax assets are recognised on deductible temporary differences and unused tax losses carried forward if it is reasonably certain that they will be recovered.

Deferred taxes are calculated on the basis of the tax rates that apply or that are expected to apply in the individual countries at the time of utilisation. For domestic Group companies, a tax rate of 31 percent was applied (in the prior year: 31 percent). Tax assets and tax liabilities are netted to the extent that the prerequisites for this have been met.

A substantial amount of management judgement is required in the determination of the amount of the deferred tax claims which can be capitalised in terms of the expected time of occurrence as well as the amount of the future taxable income and the future tax planning strategies.

3.13 Financial liabilities

Financial liabilities are recorded at their fair value upon initial recognition. After initial recognition they are measured at amortised cost. Liabilities from finance leases are measured at the lower of the fair value and the present value of the minimum lease payments at the date the leased asset is recognised.

3.14 Trade payables and other liabilities

Trade payables and other liabilities are recognised at the amount repayable. Trade payables primarily have short remaining terms to maturity. Investment subsidies are released over the depreciation period of the subsidised fixed asset. The release is openly off-set from the depreciation.

3.15 Derivatives

The derivatives include transactions within the gas trading portfolio as well as foreign currency and hedging transactions. Derivatives are measured at fair value pursuant to IFRS 9, whereby prices in active markets, for example stock exchanges, are given preference. Where such prices are not available, the fair values are determined by reference to generally accepted valuation techniques. If available, quoted prices in active markets are used as input parameters. If this is also not possible, entity-specific planning assumptions are considered in the valuation. Default risks with respect to a counterparty are, to a great extent, covered by appropriate commercial credit insurance.

Changes in fair value are recorded through profit and loss in the income statement to the extent that hedge accounting is not applied.

For derivatives for which cash flow hedge accounting is applied, the effective changes in the fair values used to off-set future cash flow risks arising from existing underlying transactions or highly probable forecast transactions are initially recognised directly in equity (cumulative changes not impacting profit and loss). Amounts are reclassified to the income statement when the hedged underlying transaction impacts profit or loss. An ineffective portion identified in the course of the continuous measurement of the effectiveness is directly recorded within other operating results.

Contracts concluded for the purpose of receiving or delivering non-financial items pursuant to the expected procurement, sale or use which are still intended for own use are not recorded as derivatives pursuant to IFRS 9, but rather as pending transactions pursuant to IAS 37.

3.16 Contingent liabilities

Contingent liabilities are possible obligations to third parties or present obligations where the probability of an outflow of resources is remote or the amount cannot be reliably determined. Contingent liabilities are not recognised.

3.17 Revenue recognition

Revenue is generally recognised when control of the goods or services transfers to the customer and the customer has the ability to determine the use of the goods or services transferred and, for the most part, has the ability to determine the remaining use. The basis for the measurement of revenue for goods or services is the transaction price. Revenue is recognised net of any sales deductions such as price discounts and rebates and without value added tax, as well as after elimination of intercompany sales. We refer to Section I with respect to the netting of revenues and costs of materials resulting from arbitrage transactions.

Interest income is recognised pro rata temporis using the effective interest method. Dividend income is recognised when the right to receive payment is established.

III. Disclosures on the consolidated balance sheet

(1) Intangible assets

€ million	31.12.2018	31.12.2017
Software	5.5	9.8
Concessions/industrial property rights	1.3	4.9
Prepayments made	2.7	2.8
Capitalised exploration costs	0.0	27.4
Total	**9.5**	**44.9**

(2) Property, plant and equipment

€ million	31.12.2018	31.12.2017
Land and buildings	49.9	47.3
Technical equipment	1,008.7	1,173.7
Operating and office equipment	5.9	7.0
Prepayments made/construction in progress	297.6	195.6
Total	**1,362.1**	**1,423.6**

(3) Other non-current financial assets

€ million	31.12.2018	31.12.2017
Shares in affiliated entities	11.4	25.0
Loans to affiliated companies	0.0	12.2
Other investments	73.9	81.4
Loans to other investments	105.5	106.0
Total	**190.8**	**224.6**

(4) Inventories

€ million	31.12.2018	31.12.2017
Raw materials, consumables and supplies	30.8	29.6
Work in progress	1.9	0.5
Finished goods and merchandise	388.9	220.7
Prepayments made for inventory	1.4	0.0
Total	**423.0**	**250.8**

(5) Trade receivables

€ million	31.12.2018	31.12.2017
Receivables from third parties	1,997.1	1,344.0
Receivables from affiliated companies	92.0	12.8
Receivables from companies measured at equity	6.5	4.4
Receivables from other investments	4.6	5.0
Total	**2,100.2**	**1,366.2**

(6) Other current assets

€ million	31.12.2018	31.12.2017
Other assets	32.5	26.3
Other receivables from affiliated companies and investments	3.1	2.6
Tax receivables	36.0	27.9
Total	**71.6**	**56.8**

(7) Provisions

€ million	Current	Non-current	31.12.2018 Total	Current	Non-current	31.12.2017 Total
Pension provisions	1.5	39.0	40.5	1.9	36.1	38.0
Tax provisions	0.0	0.0	0.0	5.5	0.0	5.5
Other provisions	87.9	415.2	503.1	108.9	522.7	631.6
Total	**89.4**	**454.2**	**543.6**	**116.3**	**558.8**	**675.1**

The **other non-current provisions** primarily comprise obligations for the decommissioning of underground storage and pipelines as well as onerous contracts. **Other current provisions** were recorded for risks associated with the gas business and for other uncertain liabilities.

(8) Trade payables

€ million	Current	Non-current	31.12.2018 Total	Current	Non-current	31.12.2017 Total
Third party payables	2,047.0	0.3	2,047.3	1,339.2	0.2	1,339.4
Liabilities to affiliated companies	113.6	0.0	113.6	15.8	0.0	15.8
Liabilities to companies measured at equity	0.8	0.0	0.8	0.8	0.0	0.8
Liabilities to other investments	2.9	0.0	2.9	1.2	0.0	1.2
Total	**2,164.3**	**0.3**	**2,164.6**	**1,357.0**	**0.2**	**1,357.2**

(9) Other liabilities and subsidies

€ million	Current	Non-current	31.12.2018 Total	Current	Non-current	31.12.2017 Total
Other liabilities	31.2	13.3	44.5	36.5	8.9	45.4
Other liabilities to affiliated companies and investments	11.3	0.0	11.3	14.1	6.8	20.9
Subsidies provided by governmental sources	0.0	1.1	1.1	0.0	1.0	1.0
Other taxes payable	66.0	0.0	66.0	51.0	0.0	51.0
Total	**108.5**	**14.4**	**122.9**	**101.6**	**16.7**	**118.3**

IV. Explanations on the consolidated income statement

(10) Revenue

Revenues primarily comprise sales to redistributors, industrial customers and on wholesale markets. In addition to the revenues from the gas business, this line item primarily includes revenue from the transportation of gas and storage revenues. We refer to Section I with respect to the effect from the netting of revenues and costs of material from arbitrage trading.

(11) Cost of materials

€ million	2018	2017 Adjusted	2017 Reported
Cost of raw materials, consumables and supplies and of purchased merchandise	10,642.9	7,620.4	9,655.9
Cost of purchased services	298.8	317.2	317.2
Exploration costs	0.0	0.0	2.3
Total	**10,941.7**	**7,937.6**	**9,975.4**

(12) Personnel expenses

€ million	2018	2017 Adjusted	2017 Reported
Compensation	71.9	70.0	70.3
Social security, pension and other benefit costs	13.6	13.9	19.4
of which for retirement	*1.7*	*2.0*	*4.6*
Total	**85.5**	**83.9**	**89.7**

(13) Amortisation and depreciation

€ million	2018	2017 Adjusted	2017 Reported
Scheduled amortisation and depreciation	63.4	66.1	98.8
Impairment losses	0.2	33.7	34.8
Total	**63.6**	**99.8**	**133.6**

(14) Investment result

€ million	2018	2017 Adjusted	2017 Reported
Results of companies measured at equity	21.1	27.5	27.5
Income from other investments	7.0	10.4	10.4
Income from profit/loss transfer agreements	1.0	2.0	2.0
Write-ups of other investments	0.0	6.1	6.1
Impairments of other investments and shareholdings in affiliated companies	–14.1	0.0	0.0
Total	**15.0**	**46.0**	**46.0**

(15) Financial result

€ million	2018	2017 Adjusted	2017 Reported
Interest income	3.3	3.1	3.1
Other financial income	2.4	1.2	13.7
Interest and similar income from discontinued business areas	6.2	9.2	0.0
Total interest and other income	**11.9**	**13.5**	**16.8**
Interest expense on loan financing	12.1	16.1	15.5
Interest expense from the unwinding of discounting of provisions	4.1	4.1	6.5
Interest expense from finance leases	2.7	2.7	2.7
Total interest and similar expenses	**18.9**	**22.9**	**24.7**
Income/expense from foreign currency translation	5.8	–17.4	0.0
Income/expense from FX derivatives	–7.7	12.2	0.0
Foreign currency expenses from discontinued business areas	–1.9	–5.2	0.0
Financial results (+ income/ – expenses)	**–8.9**	**–14.6**	**–7.9**

(16) Income taxes

€ million	2018	2017 Adjusted	2017 Reported
Taxes on income – corporate income tax	8.9	17.8	17.9
Taxes on income – trade tax	5.3	11.4	11.4
Tax income from tax refund	0.0	0.0	–11.0
Expenses attributable to deferred taxes	16.7	–19.9	6.2
Total	**30.9**	**9.3**	**24.5**

V. Other disclosures

Composition of VNG AG's Executive Board

Ulf Heitmüller	Chief Executive Officer
Hans-Joachim Polk	Chief Infrastructure & Technology Officer
Bodo Rodestock	Chief Financial & Human Resources Officer

Composition of VNG AG's Supervisory Board

Thomas Kusterer	**Chairperson** Member of the Executive Board of EnBW Energie Baden-Württemberg AG
Hans-Joachim Herrmann	**1st Vice Chairperson (from 13 July 2018)** Managing Director of Stadtwerke Lutherstadt Wittenberg GmbH
Christina Ledong	**2nd Vice Chairperson (from 13 July 2018)** Chairperson of the Works Council of VNG AG, ONTRAS Gastransport GmbH, VNG Gasspeicher GmbH and VNG Handel & Vertrieb GmbH
Markus Baumgärtner	Head of Value Chain Natural Gas of EnBW Energie Baden-Württemberg AG
Josefine Bormann	Main Consultant of Business Regulation of ONTRAS Gastransport GmbH
Dr. Frank Brinkmann	**(from 17 May 2018)** Managing Director of DREWAG – Stadtwerke Dresden GmbH
Barbara Endriss	Managing Director of OEW Energie-Beteiligungs GmbH
Christina Fenin	Head of Cooperations of VNG Gasspeicher GmbH
Dr. Martin Fleckenstein	Independent Consultant
Hans-Peter Floren	Entrepreneur
Monty Heßler	System Technology Office of GDMcom Gesellschaft für Dokumentation und Telekommunikation mbH

Dr. Martin Konermann	Managing Director Technology of Netze BW GmbH
Peter Leisebein	Deputy Chairperson of the Works Council of VNG AG, ONTRAS Gastransport GmbH, VNG Gasspeicher GmbH and VNG Handel & Vertrieb GmbH (until 12 July 2018 2nd Vice Chairperson)
Michael Raida	Management Consultant
Dr. Jörg Reichert	Member of Management of Energiedienst Holding AG
Gunda Röstel	Managing Director of Stadtentwässerung Dresden GmbH
Dr. Benno Seebach	Head of Capacity Planning at ONTRAS Gastransport GmbH
Michael M. Theis	**(from 13 July 2018)** Chairperson of the Managing Directors of LVV Leipziger Versorgungs- und Verkehrsgesellschaft mbH
Stefanie Thiele	Project Manager at ONTRAS Gastransport GmbH
Dr. Jochen Weise	Senior Advisor of Allianz Capital Partners GmbH
Dr. Bernd-Michael Zinow	Head of Function Unit Legal, Audit, Compliance and Regulatory of EnBW Energie Baden-Württemberg AG

Former members of the Supervisory Board

Prof. Dr. Norbert Menke	**(1st Deputy Chairperson and member of the Supervisory Board until 12 July 2018)** Former Managing Director of LVV Leipziger Versorgungs- und Verkehrsgesellschaft mbH
Dr. Reinhard Richter	**(until 16 May 2018)** Former Managing Director of DREWAG – Stadtwerke Dresden GmbH

Significant events subsequent to the balance sheet date

In conjunction with the acquisition of a biogas portfolio comprising five biogas plants by BALANCE Erneuerbare Energie GmbH, merger control procedures were initiated at the Bundeskartellamt [Federal Cartel Office] at the start of the new financial year. It is currently not expected that the cartel authorities will prohibit the merger. BALANCE Erneuerbare Energie GmbH intends to complete the transaction in financial year 2019.

There were no other significant events subsequent to the conclusion of the financial year.

Consolidated financial statements

EnBW Energie Baden-Württemberg AG, Karlsruhe (EnBW), prepares the consolidated financial statements for the most extensive group of companies as well as for the smallest group of companies applying the International Financial Reporting Standards (IFRS) as they are to be applied in the EU and a group management report. VNG AG is included in these consolidated financial statements as a fully consolidated entity. EnBW's consolidated financial statements and group management report are electronically submitted to the operator of the (German) Federal Gazette [Bundesanzeiger] and are available via the company register (www.unternehmensregister.de).

Pursuant to Section 291 of the HGB, VNG AG is exempted from the requirement to compile consolidated financial statements and a Group management report.

Leipzig, 26 February 2019

VNG AG

The Executive Board

Heitmüller **Polk** **Rodestock**

IMPRINT

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EDITORIAL DEADLINE
11 April 2019

DESIGN, EDITING, LAYOUT AND PRODUCTION
IR-ONE AG & Co. KG, Hamburg
www.ir-one.de

REPRODUCTION
MWW Medien GmbH, Hamburg
www.mww-medien.de

PRINTING
Sepio GmbH, Leipzig
www.sepio-media.de

PHOTOS
Torsten Proß, Jeibmann Photografik

With the exception of:
EnBW AG (page 9)
Eric Kemnitz (page 10, 12)
Peter Eichler (page 12, 14/15)

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