

1.1 STRATEGY AND STRUCTURE

RWE ranks among Europe's five leading electricity and gas companies. We want to strengthen this position. However, the market environment is likely to remain difficult. Competition is becoming fiercer, and the demands placed by customers on our service levels and product offerings are rising. Furthermore, regulatory intervention is changing established business models. At the same time, we are witnessing low prices on the electricity and gas wholesale markets. We are tackling these challenges by developing innovative products and services and continuing to invest in environmentally friendly energy supplies for the future.

Major challenges for power utilities. Energy supply requires a long-term business model. Investments in power plants, networks as well as oil and gas production are usually planned for decades in advance – not just for years. Therefore, our strategy builds on fundamental trends. However, Europe's energy markets are undergoing change, which requires utilities to adapt their business models. This change is characterised by:

- the European Union's ambitious goals to reduce greenhouse gas emissions, which cause CO₂-intensive generation technologies to be increasingly replaced by methods that are more gentle on the climate;
- a persistently substantial need for investment in energy infrastructure, especially to convert the generation portfolio to accommodate more renewables and the ensuing need to modernise and expand network infrastructure;
- the increasing need for flexible power plant deployment, triggered by the expansion of renewable generation and its strongly fluctuating electricity feed-ins;
- the convergence of regional markets resulting from increasing international trading and the expansion of cross-border transmission capacity;
- the mounting political influence exerted on the supply structure and price formation on energy markets and the general public's ever more frequent resistance to infrastructure projects such as the construction of power plants, networks and CO₂ storage facilities; and
- unexpected structural rifts in the markets, e.g. the decoupling witnessed since 2009 of wholesale gas prices from those established in oil-indexed gas purchasing agreements.

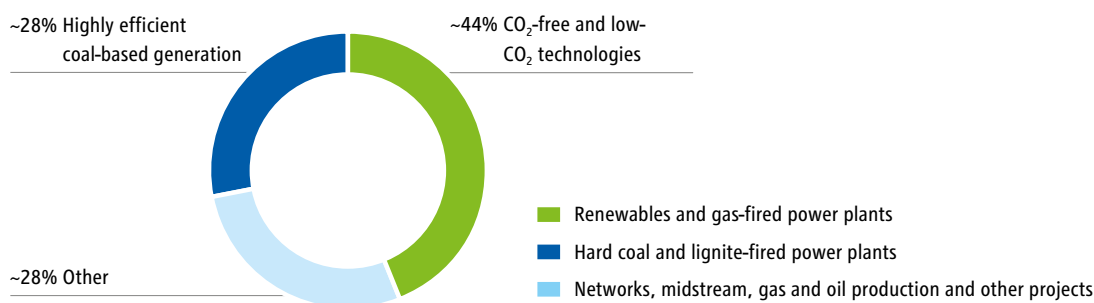
Covering all stages of the value chain creates stability. This challenging environment provides new opportunities for powerful and broadly positioned market players. We recognised the aforementioned challenges early on. The cornerstone of our current and future success is our strong, integrated business model, which adds substantial value. We cover all of the major stages of the energy value chain. In the field of electricity, we are not simply a generator, but a trader, network operator and sales company as well. We are also active at all value-creation stages in the gas sector, from the well to the end customer. Thanks to this structure, we can flexibly offset market fluctuations in individual areas.

Climate protection is the centrepiece of our strategy. We can only be successful in the long run if we manage to provide affordable, safe and environmentally friendly energy. Lowering carbon dioxide emissions is among our prime strategic targets. It provides the direction for the modernisation and expansion of our generation portfolio. Furthermore, by spending heavily on networks and pipelines, we are making a contribution to ensuring the reliable supply of electricity and gas. Another pillar of our strategy is the expansion of our gas and oil production. In addition, we want to give our activities a stronger regional diversification. The following guidelines will determine our action in the next few years:

- **Improving our CO₂ emissions balance:** Our current new-build power plant programme, which is in the last third of its implementation phase, will make a substantial contribution to reducing our carbon footprint. However, this will not be the end of the transformation of our power plant portfolio. In the long run, we are considering supplementing our generation base with additional state-of-the-art combined-cycle gas turbine power stations, as their ability to rapidly vary their load factor ideally complements renewable energy. The decision to extend the lifetimes of German nuclear power plants helps us cut down on CO₂. Our medium-term reduction target orientates itself towards the average carbon emissions per megawatt hour (MWh) of generated electricity. Our goal is to use physical and financial measures to lower our CO₂ intensity to the average level of the competition in our markets no later than 2020. Our assumption is that the customary emission factor in these markets will be roughly 0.45 metric tons of CO₂ per MWh in 2020. By comparison, RWE emitted 0.73 metric tons per MWh in the financial year that just ended (2009: 0.80 metric tons per MWh).
- **Value-added growth by expanding our renewable energy business:** RWE Innogy wants to enlarge its renewable electricity generation base substantially. The aim is to have 4.5 gigawatts (GW) under construction or in operation by 2014. Due to reductions in capital expenditure and project delays, we will not be able to achieve this goal as early as 2012, which was our original plan. The majority of the funds are earmarked for onshore and offshore wind projects. We are also investing in the production of electricity and heat from biomass and are investigating the construction of new hydroelectric power plants. In addition, we are active in the field of solar thermal power, albeit only on a small scale.
- **Strengthening of our upstream position:** We want our annual gas and oil production to reach about 70 million barrels of oil equivalent by 2016. As a result, we would produce more than twice as much gas and oil as in the financial year just ended. We had originally sought to achieve this target as early as 2015, but we are not progressing as quickly as anticipated at the outset, mainly due to reductions in capital expenditure and delays in approval procedures.
- **Stronger international diversification:** In view of mounting location-related risks, it is becoming increasingly important to give our company a large regional footprint. Over two thirds of our growth investments are already being made abroad. In 2010, the share of the operating result achieved by our activities outside Germany amounted to about a quarter. We aim to increase it significantly over the medium term.

From strategy to implementation: the largest investment programme in RWE's history. A main building block of our strategy is capital expenditure on power plants and networks. In the financial year that just ended, we commissioned two state-of-the-art gas-fired power stations, an 876 MW facility in Lingen (Germany) and a 1,650 MW plant at Staythorpe (UK). By the middle of 2014, we want to have commissioned about 12 GW in new capacity, with more than half of this being based on CO₂-free and low-CO₂ technologies. We largely finance our capital expenditure with the earnings of our generation and network activities. However, from 2011 onwards, we expect to experience substantial earnings shortfalls due to the introduction of the nuclear fuel tax in Germany. Persistently low prices of electricity and gas on the wholesale markets will also curtail our earnings. This forces us to cut spending. We originally envisaged investing a total of €28 billion in property, plant and equipment from 2010 to 2013. Now we plan to achieve a target of about €25 billion for that period, which equates to approximately €18 billion from 2011 to 2013. Nevertheless, our capital expenditure programme is still by far the biggest in RWE's history.

Some €12 billion of the €18 billion in capital expenditure on property, plant and equipment between 2011 and 2013 is earmarked for growth and replacement investments, of which:



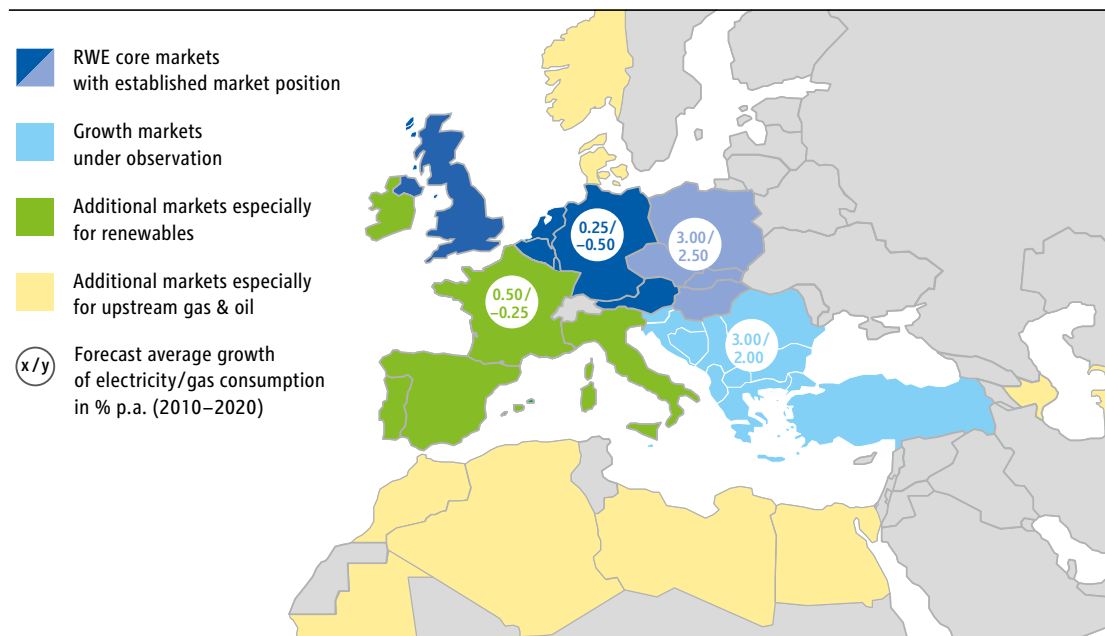
In addition to power plants and networks, our investment activity also centres on the expansion of our gas and oil production. More than €3 billion has been set aside for this for the period from 2011 to 2013. Our investment in the gas business is also earmarked for the construction of new storage and transmission pipelines. One example of this is the Nabucco pipeline, which will give European customers access to new gas sources in the Caspian region and the Middle East via a new route. We are also on course for expansion in activities relating to the transport of liquefied natural gas (LNG).

Above and beyond this, energy efficiency is becoming more important for us. Thanks to the innovative products and services of RWE Effizienz GmbH for households, corporate customers and municipal facilities, we are setting standards in this field.

Organic growth takes centre stage for us. However, this does not mean that we rule out minor acquisitions which complement our portfolio. We believe that Central Eastern and South Eastern Europe, including Turkey, provide particular opportunities.

We measure all investment projects by whether they help us achieve the aforementioned goals. The key financial yardstick is the internal rate of return (IRR), which must at least match the cost of capital, plus a return premium. The latter reflects the risk profile of the division and country in question. We increased this premium significantly in 2010. As a result, some projects no longer achieve the required return and will therefore be discontinued. Besides saving funds, this frees up room for more attractive projects.

Europe remains our market. The regional focus of our activities is and will remain Europe. Among our core markets are Germany, the United Kingdom, the Benelux countries as well as Central Eastern and South Eastern Europe. These markets are relatively stable, despite the heightened political risks. In particular, the Central Eastern European countries and Turkey distinguish themselves through good growth prospects. Due to the need of these countries to bridge the gap to the rest of Europe, their energy consumption will rise more than the European average. At the same time, there will be a substantial need for investment due to the outdated energy infrastructure. The markets of North Western Europe continue to be attractive for us, although they still harbour weak growth potential in terms of electricity and gas consumption. Energy utilities can set themselves apart in these markets by offering intelligent solutions for increased climate protection and energy efficiency as well as through tailor-made products and services. We intend to establish the prerequisites for this on the strength of our record investment programme, thus further improving our market share in the face of increasingly fierce competition.



As illustrated by the chart on page 55, our activities go beyond our core regions, particularly in our upstream business. We produce gas and oil not only in Europe, but also in North Africa. In addition, we launched an upstream project in the Caspian region and are looking into projects in other areas around the world. We have also widened our regional focus in the expansion of renewable energy. In this respect, our growth strategy includes countries such as France, Spain and Italy. It is natural for certain activities to take place outside our core markets, for instance climate protection measures within the scope of the Kyoto Clean Development Mechanism and Joint Implementation schemes. The same applies to our LNG business. In addition, energy trading is becoming increasingly global. This is a growing field of activity for us in Asia and North America.

In our core markets, we command a leading position in terms of sales volume with at least one of our main products, namely electricity and gas. This is also what we strive for when entering new markets.

Market positions of the RWE Group in terms of sales	Electricity	Gas
Germany	No. 1	No. 3
United Kingdom	No. 4	No. 4
Netherlands	No. 2	No. 1
Central Eastern and South Eastern Europe	No. 2 in Hungary No. 3 in Slovakia Presence in the Czech Republic No. 6 in Poland Presence in Turkey	Leading position in Hungary No. 2 in Slovakia No. 1 in the Czech Republic – –
Total Europe	No. 3	No. 6

Efficient structure and business management. Our organisation is the platform with which we achieve our goals, so it must adapt itself to new market conditions and strategic guidelines. We constantly work on making our Group's structure more efficient. We also set the stage in some important respects in 2010. For example, we pooled the German sales and distribution network businesses in the new RWE Deutschland AG (formerly RWE Rheinland Westfalen Netz AG). Our activities in Central Eastern Europe and Turkey were also reorganised. Our operations in that region now report to the newly established RWE East, s.r.o., headquartered in Prague (Czech Republic). The aforementioned reorganisation measures entered into force on 1 January 2011. More detailed information can be found on page 69 of this report.

Value-oriented growth: our internal control instrument. RWE's central control instrument is value added. This is how we embed our goal of adding value over the long term in the Group's and the divisions' management processes. Value added is the return on capital employed, minus the cost of capital. In addition to other individually agreed targets, this added value is also the yardstick for the performance-linked compensation of our executives and salaried staff. Details on RWE's value management are described on pages 90 et seq. and 231 et seq.