In terms of environmental protection, the Lufthansa Group invests continuously in the renewal of its fleet and in operating measures aimed at reducing the specific fuel consumption and the resulting CO_2 emissions per passenger-kilometre. In addition, the Lufthansa Group offsets the CO_2 emissions of all its employees' business flights worldwide and has set a target of becoming carbon neutral in its ground operations in Germany, Switzerland and Austria by 2030. The Lufthansa Group is also committed to noise abatement and reducing the amount of in-flight waste.

Above and beyond its actual business activities, the Lufthansa Group continues to assume responsibility in addressing today's social challenges. The central pillar of its global social engagement for disadvantaged people is the help alliance, which celebrated its 20th anniversary in 2019. The help alliance supports educational projects that are largely initiated by employees. Furthermore, the Lufthansa Group provides fast, professional emergency aid in humanitarian crises and natural disasters.

To reflect the growing importance of corporate responsibility for the Lufthansa Group, all activities in this area now report to the new Executive Board function Customer & Corporate Responsibility.

FINANCIAL STRATEGY AND VALUE-BASED MANAGEMENT

C07 FINANCIAL STRATEGY

Sustainable increase of Company value

	Improve profitability	Focus capital allocation	Maintain financial stability
Focus	– Sustainable value generation – Continuous unit cost reductions	– Profitable capital expenditure – Working capital management – Shareholder participation in the Company's success	– Maintain investment grade rating – Hedging of financial risks – Access to different forms of funding and maintaining appropriate liquidity
Target	– Adjusted ROCE – Adjusted EBIT margin	– Adjusted free cash flow – Dividend	– Adjusted net debt/Adjusted EBITDA

Financial strategy aims to increase Company value
The financial strategy of the Lufthansa Group seeks to increase its Company value in a sustainable manner. It will concentrate on three dimensions: improving profitability, focussing capital allocation and maintaining financial stability.

Improving profitability

Sustainable value generation in the Company
The Lufthansa Group applies a value-based system of management. At its centre is the profitability of the Company. This is measured by reference to Adjusted EBIT. In order to hardwire profitability into all decision-making processes, the management's variable remuneration is linked to the Company's economic performance as well as to non-financial factors such as specific CO_2 emissions. ↗ **Remuneration report, p. 115ff.** Adjusted EBIT came to EUR 2,026m in 2019 and was thus 29% below the previous year. Specific CO_2 emissions per passenger-kilometre were 92.2 grammes in 2019, on par with the previous year. Positive effects from greater fuel efficiency due to the fleet renewal and a higher passenger load factor were offset by a lower proportion of freight in the total payload.

The adjusted return on capital employed (Adjusted ROCE) is measured for the Lufthansa Group and the individual companies. If Adjusted ROCE exceeds the weighted average cost of capital (WACC), the Company is creating value. In 2019, the Lufthansa Group had an Adjusted ROCE after tax of 6.6%. This was 4.0 percentage points down on the previous year and higher than the WACC, which was just 4.2% and unchanged from the previous year. The Company therefore added value again in 2019.

T009 CALCULATION OF ADJUSTED ROCE AND COST OF CAPITAL

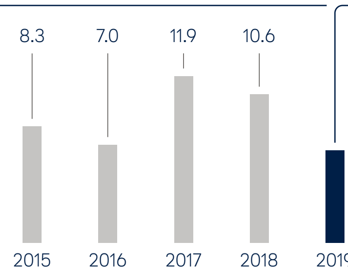
in €m	2019	2018	Change in %
Revenue	36,424	35,542	2
Other operating income	2,574	2,349	10
Operating income	**38,998**	**37,891**	**3**
Operating expenses	37,309	35,091	6
Result from equity investments	168	174	-3
EBIT	**1,857**	**2,974**	**-38**
Adjusted EBIT	**2,026**	**2,836**	**-29**
Interest on liquidity	79	68	16
Taxes (assumption 25% of EBIT + Interest on liquidity)	-484	-761	36
Cost of capital[1]	-1,007	-860	-17
EACC	**445**	**1,422**	**-69**
ROCE[2] in %	**6.1**	**11.1**	**-5.0 pts**
Adjusted ROCE[3] in %	**6.6**	**10.6**	**-4.0 pts**
Balance sheet total	42,659	38,213	12
Non-interest bearing liabilities			
of which liabilities from unused flight documents	4,071	3,969	3
of which trade payables, other financial liabilities, other provisions	5,868	6,306	-7
of which advance payments, deferred income, other non-financial liabilities	3,089	2,830	9
of which others	4,575	4,099	12
Capital employed	25,056	21,009	19
Average capital employed[4]	**23,982**	**20,502**	**17**
WACC in %	4.2	4.2	–

[1] WACC x Average capital employed.
[2] (EBIT + Interest on liquidity – 25% taxes)/Average capital employed.
[3] (Adjusted EBIT + Interest on liquidity – 25% taxes)/Average capital employed.
[4] Average capital employed in 2019 including IFRS 16 right-of-use assets as of 1 January 2019.

C08 DEVELOPMENT OF ADJUSTED ROCE (AFTER TAXES)

in %

2019
6.6



Continuous cost management contributes to structural increase in profitability

Continuous reductions in unit costs, increasing process simplification and productivity improvements are intended to lift structural profitability. Unit costs at the passenger airlines, adjusted for fuel costs and exchange rates, are to be reduced by 1% to 2% per year. Cost-cutting measures are also implemented on a continuous basis in Aviation Services.

Focussing capital allocation

Balanced investment to modernise the fleet

A balanced level of investment is very important for the Lufthansa Group. Investments are directed to projects with the highest expected returns. Going forward, the Lufthansa Group will continue to invest steadily in the renewal of its fleet, in-flight and ground products and infrastructure. The aircraft ordered for the period until 2025 serve mainly to replace older, less efficient models. Growth opportunities arising in the short and medium term can nonetheless be exploited by activating reserve aircraft or procuring used aircraft. The allocation of new aircraft to the different airlines and bases is constantly optimised according to value-based criteria. This makes the investment profile more balanced and increases focus on the deployment of capital. It also increasingly creates greater room for manoeuvre regarding any further consolidation activity. Capital expenditure should be financed from the company's own cash flow. Adjusted free cash flow is planned to exceed EUR 1bn again in the medium term. ↗ C14 **Primary, secondary and financial investments, p. 38.**

Gross capital expenditure (without expenditure on equity investments) fell by 5% to EUR 3,559m in 2019 and was mainly on down payments and final payments for aircraft, aircraft components, and aircraft and engine overhauls.

Dividend policy adjusted and aims for continuous distributions

Shareholders should participate directly in the Company's success. The Executive Board of the Lufthansa Group decided in 2019 to in future distribute 20% to 40% of the Group's net profit, adjusted for non-recurring gains and losses. The previous dividend policy provided for a dividend of 10% to 25% of consolidated EBIT. With this adjustment to its dividend policy, the Group has committed to the aim of generating an attractive return for its shareholders. The new distribution range gives the Group greater flexibility to enable continuous dividend payments than the previous policy. The new dividend policy also allows for shareholders to participate in a particularly positive performance of the Company by means of a special dividend or share buy-back.

In view of the impact of the coronavirus crisis on the course of business and to further strengthen the balance sheet, the Executive Board and Supervisory Board will table a proposal at the Annual General Meeting on 5 May 2020 not to pay a dividend for financial year 2019. ↗ **Dividend, p. 38.**

Maintaining financial stability

Investment grade ratings secure financial room for manoeuvre

Investment grade ratings for the Company's debt ensure low funding costs and financial flexibility as a result. For this reason, Deutsche Lufthansa AG would like to safeguard its current investment grade rating for the long term. Standard & Poor's and Scope Ratings raised the Group's rating in 2019. Standard & Poor's now gives Deutsche Lufthansa AG a rating of BBB (stable outlook), while Moody's gives it a rating of Baa3 (stable outlook) and Scope Ratings gives it a rating of BBB (stable outlook).

T010 DEVELOPMENT OF RATINGS

Rating/outlook	**2019**	2018	2017	2016	2015
Standard & Poor's	BBB/ stable	BBB-/ positive	BBB-/ stable	BBB-/ negative	BBB-/ stable
Moody's	Baa3/ stable	Baa3/ stable	Baa3/ stable	Ba1/ stable	Ba1/ positive
Scope Ratings	BBB/ stable	BBB-/ positive	BBB-/ positive	BBB-/ stable	

T011 LUFTHANSA'S CREDIT RATINGS

Standard & Poor's (April 2019)[1]	Long-term: BBB Short-term: A-2 Outlook: Stable	**Moody's Investors Service** (August 2019)[1]	Long-term: Baa3 Short-term: N/A Outlook: Stable	**Scope Ratings** (September 2019)[1]	Long-term: BBB Short-term: S-2 Outlook: Stable
Strengths		**Strengths**		**Strengths**	
⊕ One of the leading global network carriers with an excellent competitive position and one of the largest route network world-wide; strong market position at hubs in Frankfurt, Munich, Zurich and Vienna		⊕ One of the largest airlines in the world and a leading position in the European airline sector with a strong diversified route network		⊕ Global network coverage, diversified route network, member of the global airline alliance Star Alliance and a high share of business travellers with a strong market position at hubs in Frankfurt, Munich, Zurich and Vienna	
⊕ Balanced exposure to high-yielding, premium and long-haul traffic across its route portfolio; leading domestic market position in Germany; regional brands are well established		⊕ Robust business profile with diversified business segments reduces its exposure to volatility in passenger and cargo business		⊕ Leading position in home market of Germany; competitive advantage in premium market for long-haul traffic	
⊕ Besides the passenger airline business well diversified business profile with leading market positions in maintenance, repair and overhaul (MRO) services as well as airline catering adds stability to Lufthansa Group earnings		⊕ Diversity of business segments; maintenance, repair and overhaul (MRO) and airline catering business segments deliver stable profit contribution		⊕ Diversified operations (maintenance, repair and overhaul (MRO) and airline catering) with strong market positions mitigating cyclicality risks in passenger and cargo traffic	
⊕ Strong liquidity position		⊕ Good liquidity position; conservative financial strategy		⊕ Solid liquidity position	
Weaknesses		**Weaknesses**		**Weaknesses**	
⊖ Cost position as a competitive disadvantage		⊖ Profitability of the Airline Group depends on external factors including fuel prices and economic development in Europe		⊖ Cyclicality of the airline industry; Lufthansa Group's profitability below its peers	
⊖ High capital intense business model		⊖ Restructuring and turnaround plan for Eurowings is likely to take time		⊖ Cost advantages could erode by competitive pressure	

[1] Latest report.

Adjusted net debt/Adjusted EBITDA serves as an indicator of the Company's ability to service its debts

The ratio of Adjusted net debt/Adjusted EBITDA is used to measure the Group's ability to service its debts. With Adjusted net debt, the indicator takes into account not only traditional net debt but also pension provisions and the financial obligations arising from Group leases (including for property and aircraft).

At the end of 2019, the ratio was 2.8. This was 1.0 point higher than the previous year, mainly due to the first-time application of IFRS 16 and an interest rate-related increase in pension obligations, but still within the target range for gearing of 3.5. ↗ **Net assets, p. 41f.**

T012 **ADJUSTED NET DEBT/ADJUSTED EBITDA**

	2019 in €m	2018 in €m	Change in %
Net indebtedness[1]	6,415	3,242	98
Pension provisions	6,659	5,865	14
Adjusted net debt	**13,074**	**9,107**	**44**
Adjusted EBIT	2,026	2,836	-29
Depreciation and amortisation	2,692	2,180	23
Adjusted EBITDA	**4,718**	**5,016**	**-6**
Adjusted net debt/ Adjusted EBITDA	**2.8**	**1.8**	**56**

[1] In order to calculate net indebtedness, here 50% of the hybrid bond issued in 2015 (EUR 247m) has been discounted. Calculation of net indebtedness ↗ **p. 42.**

Structured risk management minimises finance risks

Integrated risk management, particularly by hedging fuel, exchange rate and interest rate risks, minimises the short-term financial risks for the Lufthansa Group. The hedges smooth price fluctuations by means of rule-based processes. ↗ **Opportunities and risk report, p. 65ff.; Notes to the consolidated financial statements, Note 43, p. 200ff.**

Diverse forms of funding ensure liquidity

Optimising the funding mix reduces financing costs, maintains a balanced maturity profile and diversifies the Lufthansa Group's portfolio of creditors. The majority of the fleet should remain unencumbered and wholly owned by the Lufthansa Group in order to maintain its great financial and operational flexibility.

The main financing instruments are aircraft financing and unsecured financing arrangements such as borrower's note loans and publicly traded bonds. Furthermore, the Lufthansa Group has bilateral credit lines with a large number of banks, which serve as an additional liquidity reserve. As of 31 December 2019, these credit lines came to EUR 774m (previous year: EUR 849m) and had not been used. The Group aims to maintain liquidity of at least EUR 2.3bn at all times, in order to continually manage liquidity and refinancing risks for the Lufthansa Group, especially at times of volatile demand and financial markets.

A total of 19 Japanese operating lease (JOLCO) transactions were concluded in 2019. This enabled funds amounting to a total of EUR 1,159m to be raised on favourable terms. These JOLCO deals are repaid continuously over the approximately eleven-year term of the respective contracts.

In financial year 2019, the Lufthansa Group placed a borrower's note loan for over EUR 800m with investors. The borrower's note loan has different maturities, as well as fixed and floating-rate tranches. In addition, the Lufthansa Group issued several short-term borrower's note loans for some EUR 600m, which served to refinance floating-rate tranches that were repaid early.

The EMTN programme (Euro Medium Term Note Programme or Debt Issuance Programme) was renewed in July 2019. The programme enables the Group to issue bonds on the capital market at very short notice. It is listed on the Luxembourg stock exchange.

In September 2019, the Lufthansa Group used the favourable conditions on capital markets to issue a five-year bond for EUR 500m under its existing EMTN programme. The bond matures on 6 September 2024 and pays interest of 0.250% per annum. The issue was oversubscribed by more than six times. The terms of the bond underline the great confidence enjoyed by the Lufthansa Group, also as a borrower.

Several unsecured loans with a volume of EUR 100m and a maturity of seven years were arranged with a Japanese lender on attractive terms.

There were no significant off-balance sheet financing activities last year.