

**KHD Humboldt Wedag
International AG, Cologne**



**Separate Non-Financial Group Report
in accordance with Section 315b Paragraph 3
of the German Commercial Code (HGB)
for the 2018 Financial Year**

SEPARATE NON-FINANCIAL GROUP REPORT

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SEPARATE NON-FINANCIAL GROUP REPORT

GENERAL INFORMATION

To implement guidelines in line with European requirements, the German legislature issued regulations in 2017 to strengthen non-financial reporting for companies. The CSR Directive Implementation Act concerning corporate social responsibility (“CSR”), which governs the reporting of non-financial information for certain capital market-oriented companies, became effective on April 19, 2017. KHD Humboldt Wedag International AG (“KHD AG”) must provide this non-financial report for the KHD Group in accordance with Section 315b Paragraph 1 of the German Commercial Code (“HGB”). For this reason, unless otherwise indicated, this information applies to the Group associated with KHD AG (“KHD Group” or “KHD”), i.e. the global activities of the KHD Group.

The Management Board of KHD AG is responsible for the preparation of this non-financial report. In accordance with the specifications of Section 315b Paragraph 3 HGB, the Management Board decided not to integrate the non-financial report for the 2018 financial year into the Group Management Report, but instead to create a separate, independent report that is published on the KHD website.

In accordance with the specifications of Section 171 Paragraph 1 of the German Stock Corporation Act (“AktG”), the Management Board presented the non-financial report to the Supervisory Board for audit before publication. The Supervisory Board audited the separate non-financial Group report in accordance with the legal requirements.

SUSTAINABILITY CONCEPT

Principles

For the KHD Group, acting in line with the principles of sustainability has been and remains a central business precept as this is vitally important for both the reputation and the long-term economic success and continuation of the Group. Therefore, sustainability matters play an important role in decision-making processes in various areas, and they are also incorporated into the operational processes throughout the KHD companies.

KHD currently does not use a specific reporting framework to prepare the non-financial report; instead, as in the previous year as well, it is based on the legal requirements of

Section 315 et seq. HGB. Although the use of an established reporting framework in accordance with Section 315c in connection with Section 289d HGB is recommended, German law does not specify a mandatory form. In the context of this recommendation, KHD has assessed the national and international reporting frameworks. Because the reporting frameworks currently in existence are heterogeneous in nature and so many are available, choosing a specific reporting framework does not seem useful at present. Instead, KHD will continue to monitor the development of non-financial reporting in Germany in order to determine the extent to which a standard will prevail in the future.

This non-financial report for 2018 was prepared in the initial months of the 2019 financial year taking into consideration the legal specifications and the mandatory formalized reporting with regard to non-financial matters. In accordance with the legal requirements for non-financial reporting, the report includes an introductory description of the business model in addition to significant and / or necessary information for understanding business development, business performance, the position of the KHD Group, and the effects that KHD activities have on the specific non-financial matters. The matters discussed in this report include:

- Environmental matters,
- Employee matters,
- Social matters,
- Respect for human rights,
- Anti-corruption and anti-bribery matters,
- Sustainability matters in the supply chain.

The process for determining the significant non-financial matters was implemented in the year 2018 in the context of an internal project that included consultation with internal experts from a variety of competent departments, such as Human Resources, Sales, Procurement, Controlling, Quality, and Research and Development, among others. The entire process was managed by a project team under the responsibility of the Chief Financial Officer of KHD AG. A review and update were conducted in the current year, 2019. There were no significant changes with regard to the non-financial matters in comparison with the previous year.

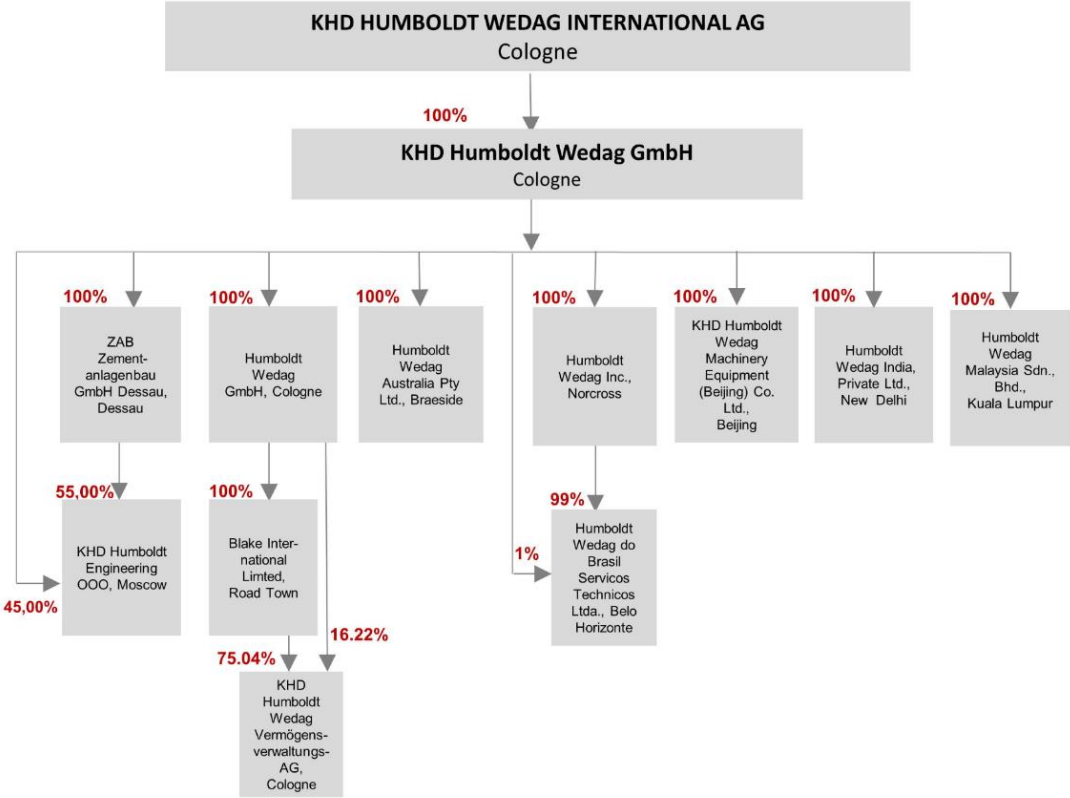
Organization und Business Model

With its subsidiaries in Europe, the Americas, Asia, and Australia, KHD AG, based in Cologne, Germany, ranks as one of the world's top equipment suppliers and service

companies for the cement industry. The scope of services encompasses process know-how and design, engineering, project management, the supply of technology and equipment as well as supervising the erection and commissioning of cement plants and related equipment. It also includes customer services such as supplying spare parts, optimizing, maintaining and repairing cement plants (e.g. with our mobile welding system for maintaining roller presses), and training plant personnel. The KHD Group focuses mainly on knowledge-intensive areas. The manufacturing of plant equipment is predominantly outsourced to quality-certified, external manufacturers who work in accordance with KHD’s specifications. KHD successfully concluded the expansion of its own production capacities in India in the 2018 financial year. Selected products will now also be manufactured increasingly with the Group’s own production capacities.

In its capacity as the ultimate holding company of the Group, KHD AG holds a 100% investment in KHD Humboldt Wedag GmbH ("KHD GmbH"), Cologne, Germany, which functions as a holding company with no operating business activities. The twelve KHD Group companies focus on the business segment of industrial plant engineering as well as related services.

Group Structure



KHD's customer base is made up of cement producers from around the world. Maintaining close contact with this target group is one of the keys to the success of the Group's business activities. Through our targeted sales, we ensure that our customers are served in accordance with their individual needs. We ensure direct customer care through our KHD subsidiaries in the respective sales territories.

Business Model

The range of KHD Group products and services is divided into the areas of Project Business (Capex) and Plant Services.

Capex (Project Business)

The scope in the Capex business unit encompasses the process technology, design, engineering, project management, and the supply of technology and equipment (grinding, pyro process, system automation). The supervision of the erection and commissioning of cement plants and related equipment (also called Field Services) that is directly connected with the project business is also classified under this segment. The KHD Group also organizes training for cement plant personnel. For this purpose, KHD draws on its own e-learning program, SIMULEX[®], with which all processes in a cement plant can be simulated and controlled by the course participants. In this way, the Capex segment comprises essential deliveries and services directly connected with a plant engineering project.

The core product range supplied by the KHD Group includes equipment for grinding and pyro processing, which are essential elements of every cement plant. Our grinding technology is utilized in raw material, clinker, and clinker substitute grinding, and comprises crushing, grinding, and separation equipment as well as fans. KHD Group's pyro processing equipment covers all of the key components of the kiln line, such as preheaters, calciner systems, burners, process fans, rotary kilns, and clinker coolers. With the PYROROTOR[®], an enhanced development of traditional calciner technology, KHD also provides technological solutions with which very coarse and poorly prepared secondary fuels can be used to manufacture cement. With the initial installation of a PYROREDOX[®] gasification reactor, KHD has reached another milestone in reducing emissions for cement plants. With this innovation, which does not require extensive catalytic technology or the use of ammonia, KHD offers an option for meeting the increasing requirements in terms of a significant reduction of nitrogen oxide emissions, even

in the future. With the PYROREDOX[®] gasification reaction, KHD customers can realize reductions in both investment and operating costs. Moreover, the KHD Group has developed a number of system automation products which are used together with process control systems to optimize plant performance.

Our products are characterized by their relatively low energy consumption, low maintenance costs, reduced vibrations, and noise emissions as well as minimal wear.

Plant Services

KHD's services include the supply of spare and wear parts as well as various plant services. These include maintenance services such as refurbishing roller presses, technical inspections, and audits as well as consulting and assistance services. In this respect, consulting on energy efficiency as well as emissions reduction and reduction of operating costs (e.g. fuel substitution by alternative fuels) when modernizing plants are important subjects.

Objectives and Strategy

The KHD Group is a full service provider for cement plants and can offer the essential, material key components of a cement plant or grinding facility with its own products.

Since its establishment more than 160 years ago, KHD has set itself apart with machines and plants developed in Germany and with leading technology. In product development, KHD focuses strongly on energy efficiency, clean plants with minimal polluting emissions, long service life, and very easy maintenance.

With our lean, quick organization, we have flexibility in dealing with individual customer requirements and can create efficient solutions.

SUSTAINABILITY MATTERS

The KHD Group has introduced a Code of Conduct as a central document that is mandatory for all employees. The Code of Conduct outlines explicit regulations or requirements to be observed with regard to non-financial matters. A Code of Ethics has been introduced for the top management level at KHG AG and KHD companies as well. It governs obligations that are above and beyond those in the Code of Conduct. For example, top management is

required to promote ethical conduct actively and to report known violations of the Code of Conduct and the Code of Ethics proactively to the Supervisory Board of KHD AG.

KHD has identified the following sustainability issues as significant. Information is provided about the conceptual strategy and the key goals with respect to these issues. Explanations regarding how KHD ensures that the respective targets are actually met are also provided. Due diligence processes are described to the extent that they are important to the identification, prevention, and mitigation of negative effects.

In addition to the results (i.e. achievement of targets, implementation of measures) of the concepts pursued in the 2018 financial year, explanations are provided regarding the significant risks in connection with the reported non-financial matters associated with our own business activities, business relationships, and our products and services. In the information about the significant risks, the KHD Group takes a net approach, i.e. the significant risks specified are those that remain after considering the risk mitigation or risk limitation measures.

If non-financial performance indicators exist for the respective sustainability matter, these are explained. Significant non-financial performance indicators are those communicated to the Management Board internally for the purposes of Group management (the so-called management approach).

Environmental Matters

One of the principles in the Code of Conduct emphasizes that KHD feels a responsibility towards the environment. Particularly in the area of enhanced product development, environmental matters play a central role at KHD.

Energy-efficient plants for reducing operating costs, using alternative fuels and, increasingly, limiting CO₂ emissions are highly important for customers of KHD. With the roller press, KHD not only has the most energy-efficient grinding technology, but also the most efficient solution for grinding slag. As our customers use slag and other clinker substitutes, KHD indirectly contributes to a considerable reduction in CO₂ emissions because the CO₂ emissions that

would otherwise occur during the pyro process related to the use of limestone are prevented. Another advantage of the KHD grinding technology with the roller press is that it uses significantly less process water in comparison with other technologies. For this reason, product development within KHD is focused on critical environmental matters such as these. The emphasis here is on the evolutionary, ongoing development and optimization of the existing product portfolio. The focus on the energy and emissions efficiency in the advanced development of our own products is an important way for KHD to differentiate itself from competitors from countries with low cost structures. In this respect, dealing successfully with these matters is highly significant to the commercial success of KHD as well.

The targeted advanced development of KHD products is carried out systematically and regularly with reference to specific customer projects. The key controlling instrument for these activities is the annual budget for research and development. In addition to the amount of the budget for product development, specific development targets are defined. The total expenses for research and development in the 2018 financial year amounted to € 1.9 million (previous year: € 2.3 million). Of this amount, € 1.0 million (previous year: € 1.3 million) was used for developments with a direct connection to energy and emissions efficiency.

The use of natural resources is not a key subject in KHD companies because the manufacturing of KHD products is predominantly outsourced to certified suppliers. However, due to the long lifetime and the comparatively low need for repair and maintenance, KHD does indirectly contribute to using natural resources mindfully.

In contrast to production companies, our own consumption of energy and resources is not a significant aspect for KHD. An energy audit in accordance with Sections 8 - 8d of the Law on Energy Services and other Energy Use Efficiency Measures was carried out in the 2015 financial year. An update of the energy audit shall be implemented in the current 2019 financial year. The energy audit is an important instrument for determining measures for increasing energy efficiency and reducing energy costs. In addition, by determining how much energy is consumed where in the company, areas where potential energy savings exist can be identified. In KHD companies, the most significant amount of energy consumption is related to the leased office buildings.

There are no significant risks associated with our own business activities or business relationships or KHD products and services that are highly likely to have serious, negative effects on environmental matters. Indirect risks are associated with the business activities

and products of KHD, i.e. if KHD is not able to develop particularly beneficial products with regard to energy efficiency, climate-relevant emissions and resource consumption, or to sell these products to customers, this will probably have negative results with regard to environmental aspects. One way that KHD manages these risks is to market the products not only with respect to price, but also, and very consciously, with respect to their environmental advantages.

For KHD, environmental matters are not a non-financial performance indicator used for controlling the Group even if they play an important role in product development and sales, for example. However, environmental matters are indirectly related to the management and controlling of KHD Group because the predominant share of revenue is earned with energy-efficient and environmentally conscious products.

Employee Matters

In addition to complying with all of the legal requirements with respect to employee matters, the KHD Group addresses the following matters, among others, in the mandatory Code of Conduct:

- The KHD Group trusts in the loyalty of its employees.
- KHD treats employees fairly, courteously, and respectfully.
- KHD is committed to equal treatment and equal and fair opportunities for all employees.
- We disavow any type of discrimination or harassment.

At KHD, compliance with the rights of trade unions is ensured in accordance with legal provisions. The inclusion and participation of employees with respect to important company matters is ensured due to our employee suggestion system, but also through the works council and the economic committee that are established at the level of Humboldt Wedag GmbH.

For KHD, as a specialized supplier of equipment and services for the cement industry, the personal dedication and the professional expertise of each individual as well as the effective

and efficient cooperation in teams are key success factors for the overall financial performance of the KHD Group. For this reason, an important task for KHD is to guarantee a working atmosphere and working conditions at the respective locations in which employees can fully realize their performance potential in a positive manner.

The basic prerequisites for a working atmosphere and working conditions that promote performance include an open, fair management culture and equal opportunities along with possibilities for flexible rules related to work time, encouragement and development of employees, and fair, performance-related compensation. The aspects important to KHD here are:

- Flexibility in organizing work time has become considerably more important in recent years for long-term employee retention. KHD ensures increasing flexibility with regard to work time by setting up work time accounts and part time work schemes.
- With regard to the compensation structure, we acknowledge competitive conditions for remuneration, taking the respective applicable local legal framework and the local salary structure into consideration.
- In KHD companies, employee development is customized and integrated into the annual feedback process carried out by the directly responsible manager with the respective employee. In these discussions, specific internal and external measures for further development in the coming year are defined. In the 2018 financial year, external expenses for training and employee development in the KHD Group amounted to € 123 thousand (previous year: € 166 thousand). Part of this employee development also includes seminars for members of the extended management team.
- Timely succession planning is also an important employee matter. In this regard, passing on the respective professional expertise in a structured and complete manner is very important. The KHD Management Board is directly involved in succession planning – particularly for management positions and knowledge-intensive expert positions.

There are no significant risks associated with our own business activities or business relationships or KHD products and services that are highly likely to have serious, negative effects on employee matters.

For KHD, employee matters are not a non-financial performance indicator used for controlling the Group even if they play an important role with regard to company success.

Social Matters

Dialog at the community and regional levels is taken seriously by KHD companies, e.g. donations made have a regional connection. With respect to social matters, KHD has very consciously decided to focus on India. The KHD entity in India supports the “Prime Minister National Relief Fund”. This fund supports people affected by natural and human-caused disasters. The fund also supports medical treatment for cancer, kidney transplantation, and heart surgery in India.

The target is to donate at least 2% of the average net profit of the KHD entity in India over the last three years for activities in the area of corporate social responsibility. After currency translation, € 132 thousand (previous year: € 122 thousand) was donated in the 2018 financial year. Thus, the donation target was achieved.

There are no significant risks associated with our own business activities or business relationships or KHD products and services that are highly likely to have serious, negative effects on social matters.

For the KHD Group, social matters are not a non-financial performance indicator used for controlling the Group. However, there is a clearly defined target for the KHD entity in India for activities in the area of corporate social responsibility, and compliance with this target is monitored by management.

Respect for Human Rights

KHD confirms its unlimited commitment with regard to respecting human rights. This includes preventing child labor, forced labor, and any form of exploitation as well as complying with prohibitions on discrimination. In Europe, the observation of human rights is primarily ensured in national and European legislation in most countries, where compliance is strictly monitored. However, KHD is also active in countries in which human rights are not legally or effectively protected to the same extent as they are in western, industrialized nations. Compliance with human rights in these regions as well is important to KHD and is ensured

for KHD companies by the Code of Conduct. Matters that relate to compliance with human rights in suppliers' organizations are described in the sections titled "Employee Matters", "Social Matters" and "Sustainability Matters in the Supply Chain".

There are no significant risks associated with our own business activities or business relationships or KHD products and services that are highly likely to have serious, negative effects on respect for human rights.

For KHD, respect for human rights is not a non-financial performance indicator used for controlling the Group even though respect for human rights is very important to KHD.

Anti-Corruption and Anti-Bribery Matters

Impeccable ethical conduct is a fundamental principle at KHD and is defined in the Code of Conduct. The Code of Conduct is a preventative measure in which KHD has very consciously established internal company rules in addition to compliance with laws and guidelines. The KHD Group is active worldwide, including in countries where adhering to compliance principles is not as pronounced as in western, industrialized nations. For this reason, it is important to raise awareness, especially among those employees with external contacts, with regard to the principles of the Code of Conduct. All KHD employees are instructed to make sure that there are no violations of the Code of Conduct in their respective area of responsibility.

The mandatory KHD Code of Conduct governs the following matters, among others:

- The Code of Conduct specifies rules for ethical behavior.
- The Code of Conduct represents a guideline for appropriate behavior in a series of sensitive areas that is expected of all KHD employees in all locations around the world.
- Management is expected to provide an example; a high level of social and ethical competency is expected from them.
- The trust of our business partners, customers and shareholders, the authorities, and the public in the conscientious conduct of all KHD employees is crucial for the reputation and success of our company.

- The KHD Group encourages employees to request advice and support from the respective supervisor or department if they have questions regarding their own conduct or in case of questionable incidents in their area of activity.

All employees as well as the managing directors and members of the Management Board receive a copy of the Code of Conduct; it is a mandatory attachment to the employment contract or service contract. Every year, KHD requires that all employees in senior management and all employees in departments with increased risk with regard to irregularities, corruption, and bribery (e.g. Sales, Procurement, Accounting), group wide, at all KHD companies, provide a written confirmation that they comply with the Code of Conduct. The top management level at KHG AG and KHD companies provides annual confirmation of compliance with not only the Code of Conduct, but also the Code of Ethics.

A whistleblower policy has been implemented at the KHD Group as an important element of the compliance management system. The whistleblower policy enables employees – also anonymously, if desired – to report concerns related to possible violations of the Code of Conduct, questionable actions, questionable internal accounting practices, or inadequate controls or auditing matters.

All of the employees addressed in writing in the 2018 financial year confirmed their compliance with the Code of Conduct in writing. All members of the top management level confirmed their compliance with both the Code of Conduct and the Code of Ethics. Moreover, no reports were received through the existing whistleblower system.

In addition, during the tendering process, it is required that an estimation of risks related to corruption and bribery is prepared for each project. If certain risk indicators are identified or specified risk values are exceeded, a mandatory risk mitigation strategy has to be developed. In the risk register related to the respective project, the identified risks with regard to corruption and bribery are updated and monitored throughout the entire project life cycle.

The (strategic) risk register for the KHD Group also explicitly monitors fraud risks, which also include risks with regard to corruption and bribery. These risks are addressed with clearly defined measures for preventing and fighting against fraud. This risk register is made available and explained in detail to the Supervisory Board of KHD AG twice a year in order to enable the Supervisory Board to assess the effectiveness of the risk management system.

There are no significant risks associated with our own business activities or business relationships or KHD products and services that are highly likely to have serious, negative effects on anti-corruption and anti-bribery matters.

For KHD, fighting against corruption and bribery is not a non-financial performance indicator used for controlling the Group even though the effective implementation of measures for prevention and detection of corruption and bribery is important to KHD. The risk assessment for individual projects is also presented to company management for approval based on specifically defined limits before providing a binding proposal. The (strategic) risk register for the KHD Group is updated quarterly and reported to the Management Board of KHD AG.

Sustainability Matters in the Supply Chain

The KHD Group supplies equipment and provides services for the cement industry. With the exception of a workshop in India, KHD companies do not have production capacities of their own.

The KHD Group uses specialized and certified external production facilities to manufacture products and plant equipment. Due to the high requirements for suppliers in terms of quality and technical ability, the suppliers are audited by internal specialists based on specifically defined inspection and assessment procedures before the initial placement of any purchase order. In addition, existing suppliers are subject to regular and incident-related supplier assessment certifications.

KHD employees with the respective qualifications visit new, potential suppliers and existing suppliers, evaluate the organizational structures and the workflow, and look at the specific

production conditions in the production facilities. Even though the non-financial aspects described in this report are not explicitly included in the internal checklists for supplier certification, these aspects are taken into account. If, for example, unacceptable working conditions, gross disregard for environmental matters, or indications of child labor or forced labor are determined, the supplier is disqualified.

Large, globally active cement producers are among KHD's important customers. Some of these customers have introduced comprehensive systems to address the subjects of corporate social responsibility and sustainability, which also include important suppliers. In every case in which KHD was included as an important supplier or supplier of key technology in the assessment of corporate social responsibility and sustainability, the required information was provided in full. KHD was subsequently informed that the stipulations according to the assessment criteria of the respective customer were met by KHD.

There are no significant risks associated with our own business activities or business relationships or KHD products and services that are highly likely to have serious, negative effects on sustainability matters in the supply chain.

Cologne, Germany, April 30, 2019

The Management Board

(s) Yizhen Zhu

(s) Jürgen Luckas

(s) Dian Xie

(s) Tao Xing