



Villeroy & Boch

1748

Sustainability Report 2017

Note

We are still working on the final layout of the Sustainability Report 2017 and expect to make it available to download at www.villeroyboch-group.com/en/investor-relations/publications/sustainability-reports in early March 2018.

IN FOCUS: THE “METTLACH 2.0” SITE DEVELOPMENT PROJECT

The Alte Abtei (Old Abbey) in Mettlach has been Villeroy & Boch's headquarters for more than 200 years. In 1809, Jean-François Boch purchased the former Benedictine abbey, which had been extensively damaged during the War of the First Coalition between 1792 and 1797, and restored it. With the company's success leading to a need for increased production facilities, a dense network of buildings soon arose on the site. Ever since, a region that was once characterised solely by agriculture and forestry has developed into an internationally renowned hotspot for ceramics. The entire area around Mettlach has benefited both economically and in terms of its infrastructure. Since the early 1980s, tourism has established itself as a second pillar of the economy in the region near the famous bend in the Saar River.

Our successful history as a company is inextricably linked with the Mettlach region. Our considerable social responsibility results not only from our role as a major regional employer, but also from our desire to actively contribute to the attractiveness of the location in order to sustainably improve the regional economy and quality of life. One flagship project in this respect is the “Mettlach 2.0” site development project, which we initiated in 2015 in cooperation with Mettlach municipality. The aim of the public-private partnership is to modernise the face of the region, make Mettlach a more attractive destination for various kinds of tourism, e.g. shopping and industrial heritage, and create modern working environments for Villeroy & Boch's employees. The buildings on the Alte Abtei site are being modernised, old factory halls are being dismantled to create additional open spaces, and the outside grounds are being redesigned. In future, the 60,000 square metre site will feature a new discovery centre for tourists and fans of the Villeroy & Boch brand. This will be home to our own Experience Centre - comprising Keravision, the museum of ceramics and extensive exhibition space for Tableware and Bathroom and Wellness products - as well as a Villeroy & Boch outlet centre for crockery, glass, cutlery and more. The site will also feature additional retail space.

We have budgeted a low eight-figure amount for realising the “Mettlach 2.0” project, with additional funding provided by the municipality and the state and federal governments. We expect the project to be completed in 2021.



Illustration: Open space planning by MESS Laport, architectural planning by bochem.schmidt architekten and Villeroy & Boch, illustration by KULLE Art Direction

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1 STRATEGY AND INTEGRITY

1.1 Villeroy & Boch at a glance

The Villeroy & Boch Group, headquartered in Mettlach in the German federal state of Saarland, is a leading international ceramics manufacturer with a total of 8,099 employees (as of 31 December 2017). As a full-range supplier for the bathroom and the laid table, our operating business is broken down into the Bathroom and Wellness Division and the Tableware Division. We sell our products in more than 125 countries. In addition to our main brand, Villeroy & Boch, we also use local markets such as Gustavsberg for sanitary ware products in Scandinavia and secondary brands for certain sales channels in the Tableware Division. When it comes to manufacturing our products, we currently have 14 production and assembly sites, comprising two for the Tableware Division (both in Germany) and twelve for the Bathroom and Wellness Division: two in Germany, two in Sweden and one each in the Netherlands, Belgium, France, Austria, Romania, Hungary, Thailand and Mexico.

In the 2017 financial year, we increased our consolidated revenue by 2.0 % year-on-year to € 836.5 million. Our operating earnings before interest and taxes (EBIT) improved by 8.5 % to € 49.8 million. The return on net operating assets amounted to 17.7 % compared with 15.7 % at 31 December 2016.

Our product range in the Bathroom and Wellness Division encompasses ceramic bathroom collections, bathroom furniture, shower, bath and whirlpool systems, tap fittings, ceramic kitchen sinks and accessories. These products typically find their way to consumers or project customers via a two-stage or three-stage sales channel. Our core target groups are dealers, craftsmen, architects, interior designers and planning specialists. Our Bathroom and Wellness products are exhibited at more than 10,500 showrooms around the world.

In the Tableware Division, our product range encompasses high-quality crockery, glasses, cutlery and corresponding accessories, kitchen and table textiles and giftware. We reach end consumers through specialist retailers and our own retail activities, which include more than 100 Villeroy & Boch stores, around 510 points of sale in department stores, and dedicated online shops in more than 20 countries. All in all, our products are available at around 4,750 points of sale worldwide. In addition, our project business addresses hotel and restaurant operators.

Our product range also features licence-based products from the “living” segment, particularly lighting, bathroom accessories, garden furniture and flooring.

1.2 Strategy and measures

For us, achieving our goals as a company is closely linked to various aspects of sustainable activity. It is important that all our employees have a common understanding of how we intend to achieve these goals. In particular, the instruments we use to communicate our approach include the Code of Conduct, the corporate guidelines and our management principles. We endeavour to provide our

employees with a great deal of scope and the best possible support when it comes to achieving their own goals. As long-term business success is possible only with creative and motivated employees, we are committed to the principles of respectful treatment, fair pay, targeted training and active diversity.

Our customers place their confidence in the high quality of our products with a stylish design, extremely high durability and maximum product safety. We intend to keep this confidence in future with technically superior products and sustainable value creation. This is why the requirements we make of our suppliers and our in-house production are so stringent. Alongside compliance with the law and labour and environmental standards, our aim is to achieve our outstanding product quality with a high degree of resource and energy efficiency. The use of management systems and standardised processes helps us to achieve this.

At an operational level, we have pursued specific targets in the areas of the environment, employees, the supply chain, product responsibility and compliance for a number of years. Examples include reducing the specific energy consumption of ceramic products in the manufacturing process, the successive implementation of environmental and energy management systems, and transparency in the supply chain.

In the 2017 financial year, we increased the transparency of our non-financial performance with the introduction of regular Group reporting. Data from areas such as environmental performance, procurement, employees and compliance are collected on a quarterly basis in order to allow us to measure the success of defined actions, including on a short-term and medium-term basis, and make adjustments as necessary.

As a company with a long tradition dating back to 1748, we have also been active in our social and cultural environment for many generations. Our aim is to be a strong and reliable regional partner at our various locations by supporting charitable organisations and initiatives on a targeted basis. Examples include donating products for fitting out facilities such as schools or in emergency situations, such as natural disasters or refugee aid in Germany in 2016.

1.3 Stakeholder dialogue and materiality analysis

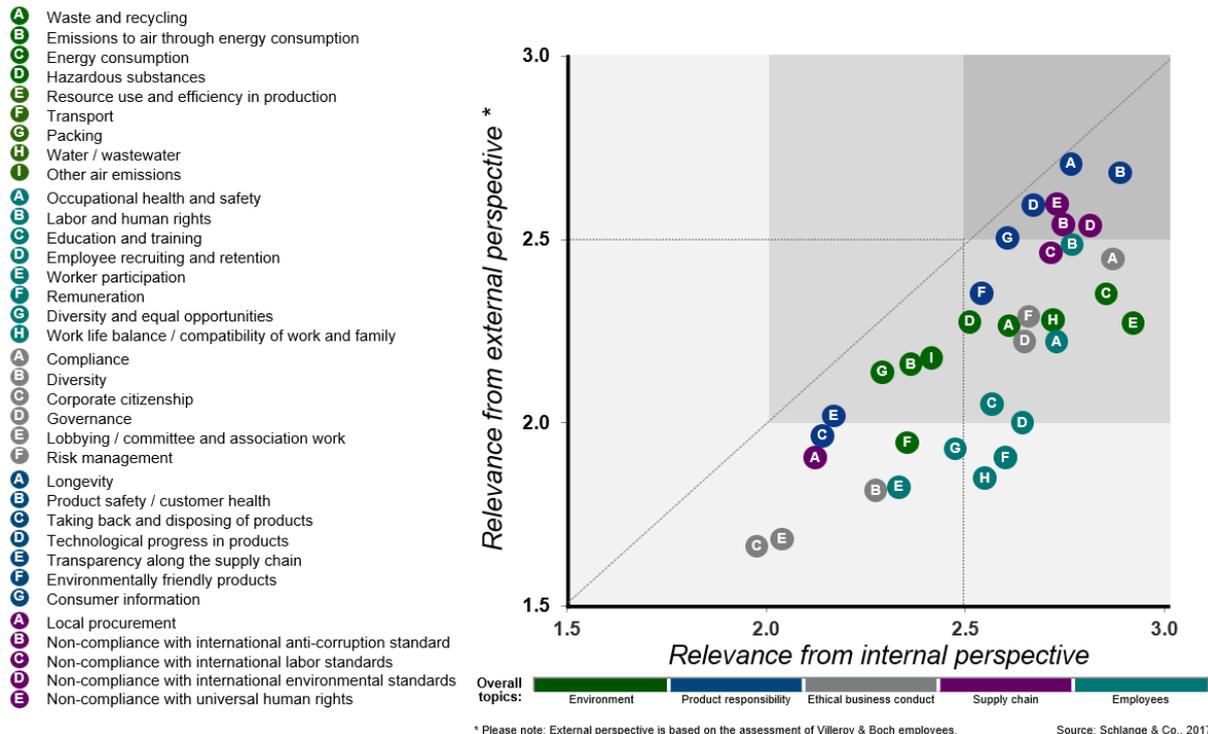
As a globally active company, we engage in a regular dialogue with a wide range of different stakeholder groups. This ensures that the varied demands, interests and expectations made of Villeroy & Boch are recorded and taken into account in our business decisions. Our most important partners in this dialogue are customers and suppliers, employees, the Works Council and union representatives, shareholders, lenders, supervisory bodies, interested members of the public, researchers and scientists, and authorities and politicians.

As the basis for our first report on Villeroy & Boch's non-financial performance and a starting point for the development of a sustainability strategy, we conducted a materiality analysis for the first time in the 2017 financial year with the support of a management consultancy specialising in CSR. The aim was to identify the most important sustainability issues for our industry in general and our

company in particular. We invited 116 selected employees from Germany and abroad to participate in an online survey. The response rate was around 75 %.

All of the participants were asked to rank the relevance of 35 pre-defined topics concerning the environment, employees, the supply chain, product responsibility and sustainable corporate governance. Employees gave their responses from an internal perspective as well as from the perspective of the respective stakeholders with whom they are in regular contact. For example, a sales employee also responded from the perspective of a customer, while an employee from the HR department was also able to assess the relevance of the topics from the perspective of a job applicant. We actively accepted the slight lack of clarity that can result from including a third-party perspective in order to keep the costs of the project reasonable. We intend to expand the materiality analysis to include interviews with external stakeholders in future years.

The materiality analysis showed that all 35 topics are relevant for our industry from both an internal and an external perspective. The area with the most highly relevant topics is product responsibility, with product safety/customer health identified as the most important individual topic. From a purely internal perspective, the participants identified resource consumption/efficiency in production as the most important topic. A full overview of all 35 individual topics can be seen in the following materiality matrix.



The materiality analysis was prepared and evaluated by a cross-functional project team consisting primarily of representatives from human resources, procurement, sales, environment, production and compliance.

1.4 Corporate governance and compliance

Sustainability is closely linked to responsible company management. Accordingly, good and transparent corporate governance is extremely important for Villeroy & Boch's long-term business success. It fosters the confidence of shareholders, customers, employees, business partners and interested members of the public.

The Management Board and the Supervisory Board of Villeroy & Boch AG have undertaken to uphold the principles of modern corporate governance. The company complies with the main requirements of the German Corporate Governance Code (GCGC) and issues an annual declaration of compliance (see: www.villeroyboch-group.com/en/investor-relations/corporate-governance/declaration-of-compliance). A detailed presentation of the tasks and responsibilities of the committees can be found in the 2017 Annual Report.

For Villeroy & Boch, acting with integrity and in compliance with the law is a fundamental element of good corporate governance in order to achieve economic success in the long term. Compliance with statutory and official provisions and internal guidelines and directives, especially our Group-wide Code of Conduct, is ensured by means of a Group-wide compliance management system.

We also expect our business partners to sign up to our Code of Conduct or demonstrate their compliance with an equivalent code of conduct (see section 4. "Supply chain") with the aim of upholding human rights and precluding the use of child labour and forced labour.

As a member of around 60 associations with anti-trust relevance, we also require that an anti-trust compliance programme is established and actively pursued within the respective organisations. Employees who represent us in these associations are given special training on the potential compliance risks of this activity.

Integrated compliance organisation

Villeroy & Boch's compliance organisation is integrated at all levels of the Group, from the Management Board of Villeroy & Boch AG to the central functions and both divisions including all local Group companies. The Chief Compliance Officer and the central Compliance department are supported by 43 functional compliance officers and local compliance managers at 55 operating Group companies.

Compliance management system

The objective of our compliance management system is to minimise compliance risks (prevention), identify and investigate potential compliance breaches (detection) and initiate appropriate countermeasures (response).

Villeroy & Boch's compliance management system covers the topics of business ethics, anti-trust law, combating corruption, fraud, money laundering prevention and sanction list screening. The central Compliance department also supports the specialist departments when it comes to overarching topics such as ensuring compliance in the context of our product responsibility (product com-

pliance), upholding social standards in the supply chain (social compliance) and foreign trade issues (trade compliance).

Our company also focuses on data protection and data security. We apply clearly defined processes to ensure that personal data is used for legitimate purposes only and in accordance with the law. We ensure that our data is secured against hacking by conducting system tests, including simulated attacks.

We work to permanently improve our compliance management system through external audits and internal reviews of our compliance processes. In 2016, an external auditor confirmed the effectiveness of our compliance management system in the areas of anti-trust law and combating corruption in Germany in accordance with audit standard IDW PS 980.

Identifying risks – structuring legally watertight processes

Our compliance management is risk-oriented. The scope and intensity of the compliance activities are determined on the basis of a Group-wide compliance risk analysis that we review regularly and modify as required. In the 2017 financial year, we conducted a risk analysis of selected core processes at Group level. The aims of this analysis included the identification of compliance risks in processes and the digitalisation of compliance-relevant security and control mechanisms. We intend to use this to integrate our guideline-based compliance management in the operating business processes along the value chain and make it more process-oriented.

The objective of regular reporting is to recognise and evaluate potential compliance risks in our business model.

Compliance training

Information and communication are a key instrument for preventing compliance breaches. We use classroom-based and online training to ensure that our employees have a common understanding of compliance. Employees and managers who are exposed to risk – particularly those from the areas of sales, marketing and procurement – are given high priority when it comes to training.

Classroom-based training allows us to adapt the contents to the needs of the respective target group and take account of any country-specific requirements. At the reporting date, 1,023 active employees worldwide had been given anti-trust training and 1,635 active employees had been given anti-corruption training.

This classroom-based offering is supplemented by online training in order to give our employees greater flexibility in terms of timing. At the reporting date, a total of 1,166 active employees had taken the online anti-trust training via our e-learning portal, while 1,258 active employees had taken the online anti-corruption training. In addition, around 800 store employees around the world completed the “Compliance” module via our International Sales Academy.

Investigating breaches

Our whistleblower system allows employees, business partners, suppliers, customers and other third parties to report potential breaches to the Compliance organisation confidentially and, if desired,

anonymously. Among other things, a reporting system has been established on the company's intranet and an external ombudsman is available as an independent confidant and mediator (by e-mail to whistleblowing@villeroy-boch.com or by post to Villeroy & Boch AG, Compliance Department, Saaruferstr. 1-3, 66693 Mettlach, Germany).

Our Compliance organisation carefully investigates all reports and takes the necessary disciplinary action. Based on the relevant reports of potential compliance breaches received within the Group, two internal investigations were required in the 2017 financial year (previous year: four); these did not result in disciplinary action.

1.5 Risk management

The long-term achievement of the company's targets is supported by Group-wide risk management in order to safeguard the company's continued existence. As ecological and social aspects are also important for the realisation of economic success, our risk management takes these areas into account. Relevant risks are systematically recorded and evaluated in the annual Group-wide risk inventory.

In the 2017 financial year, there were no significant risks within the meaning of section 289c (3) no. 3 and 4 of the German Commercial Code (HGB), i.e. risks relating to the business activities, business relations and products of the Villeroy & Boch Group that are extremely likely to occur and that could have a serious negative impact on sustainability-related aspects of this report. Details of our assessment of the individual risks can be found in the risk report in our Group management report for 2017.

2 PRODUCT RESPONSIBILITY

The future viability of Villeroy & Boch relies on innovative strength and product quality. Activities in the areas of research, development and innovation serve to strengthen our competitiveness and form the basis for the long-term business success and continued existence of the company. We invested € 15.9 million in research and development projects in the 2017 financial year (previous year: € 15.2 million), of which € 12.2 million (previous year: € 11.7 million) related to the Bathroom and Wellness Division. Activities in the period under review included the advancement of ceramic materials, surfaces and production technologies. In these areas, we regularly cooperate with external partners such as the Luxembourg Institute of Science and Technology (LIST), the German Federal Ministry for Education and Research and the Fraunhofer institutes.

2.1 Technical progress in products

While product development in the Tableware Division focuses on product design and the functionality of the respective crockery, glass and cutlery, technological development gives us an important competitive edge when it comes to Bathroom and Wellness products. The most prominent example is our range of rimless WCs, DirectFlush. Because they feature an open rim skirt, they can be cleaned quickly and thoroughly compared with traditional toilets, where debris typically collected in the old-fashioned flush rim. This comfort feature, which also means lower consumption of cleaning products, is appreciated by public facilities, hospitals and private households in equal measure. Our product range currently encompasses 25 WC models with DirectFlush functions.

In order to meet even more stringent hygiene requirements in the bathroom, particularly in healthcare facilities, we have developed AntiBac. This surface technology, which is safe for the environment and for health, has been proven to reduce bacterial growth by more than 99.9 %.

2.2 Durability of ceramic products

One of the main characteristics of ceramic products is their extreme durability. Toilets and washbasins are designed to be capable of standing up to many years of use. The load requirements for our products – e.g. 400 kilograms of static loading capacity for a properly installed toilet – are defined by quality management and tested in the product development process using a stage-gate model. Products are approved only once these requirements are met. This is how we lay the foundations for our extremely high level of customer satisfaction.

Product development in the Tableware Division focuses on sustainable product quality. In particular, porcelain products must be dishwasher-resistant. To prevent the gradual quality degradation of decorated products in particular, the development process involves subjecting them to 2,000 cycles in a household dishwasher.

2.3 Quality management as the basis for product safety, customer health and consumer information

We offer products for our customers' everyday lives, from washbasins and toilets for the bathroom through to plates, cups and cutlery. We are proud that our products are an integral part of the daily routine for millions of people and are aware of our responsibility to ensure products that can be used safely, comfortably and healthily.

In the Tableware Division, the properties of a product are optimised during the development process in order to prevent potential usage risks. A close dialogue takes place between product development and quality management to this extent. Following product approval, the resulting pre-production prototypes are manufactured under mass production conditions as a pilot series. In this status, extensive tests are then conducted to ensure that the product is not hazardous or harmful to the user's health. The requirements are becoming increasingly complex due to the growing combination of different materials and regional variations in the strict guidelines for products that come into direct contact with food or the skin.

For purchased items, such as glasses, cutlery and accessories and some seasonal porcelain items, samples are initially examined by our quality management department. Chemical analysis and sensory laboratory tests are conducted externally in order to ensure that products developed in-house and purchased items demonstrate exemplary product safety and comply with all of the relevant guidelines and regulations. A total of 193 new products were examined externally in the 2017 financial year. Items that are assessed negatively are analysed in order to establish whether the defects – e.g. incorrect product labelling or threshold exceedance – can be resolved. As a general rule, no product reaches the market without being approved by Villeroy & Boch's quality management.

Once an item has successfully completed the development and quality process and has been launched on the market, it is retested at a frequency of between 12 and 24 months in order to ensure ongoing product quality and safety. Conformity with all of the applicable guidelines and regulations, which are changed regularly, is also confirmed. In the period under review, a total of 307 items from our existing product range were tested at external laboratories. For documentation purposes, all of the test reports and their current validity are stored in a database. We also work in close cooperation with the Saarland State Office for Consumer Protection, which takes ten items from our warehouse every month and inspects their suitability for the marketplace. For purchased items, pre-dispatch inspections and incoming goods inspections at the central warehouse in Merzig are key elements of quality management. In the 2017 financial year, 503,635 units were inspected across a total of 9,021 delivery items. 395 delivery items were barred from distribution – usually temporarily – in order to analyse the reasons for irregularities, e.g. in terms of product damage or incorrect packaging, and to allow for the measures required to remediate these irregularities to be initiated in consultation with the supplier.

Quality management in the Bathroom and Wellness Division is based on the ISO 9001 quality management system. We have been certified without interruption since the system was introduced in 1995. The effectiveness of the system is examined in the form of annual audits. Quality man-

agement is integrated into the product development process in order to comply with all international (washing and rinsing) standards and ensure the required product load capacity.

To prevent a risk to customer health as a result of systematic product faults, every single ceramic product manufactured by Villeroy & Boch is visually inspected by a qualified member of staff following the firing process. In addition, central quality management has developed a catalogue of tests that requires each model to be subjected to regular, systematic load tests and functional checks. New product models are tested more frequently in the first year of production. The requirements at each production site include the inspection of all fired ceramics and an additional inspection of goods marked as error-free based on statistical sampling prior to their addition to the warehouse. All test results are documented using a defined template and stored for ten years. Internal product audits, which are conducted twice a year for each plant by central quality management, also help to maintain and improve product quality.

Product and quality management in both divisions also work in close cooperation when it comes to preparing consumer information. A packaging insert informs consumers on how to use and look after their product. Where necessary, we also include the legally required warnings for safe usage.

The concepts applied are intended to ensure that our products are used safely and enjoy a high degree of customer satisfaction in all phases of the product lifecycle. In the unlikely event that non-compliant products make their way into our warehouse or even as far as our customers, there is a guideline setting out how to inform the recipients using various stages of escalation or, in extreme circumstances, how to conduct a recall from stores or consumers.

3 SUPPLY CHAIN

The Villeroy & Boch brand has always stood for ceramics expertise. The vast majority of our toilets, washbasins, kitchen sinks, plates and cups are manufactured at nine ceramic production sites. The most important raw materials used in ceramic production are kaolin, quartz, feldspar and clay. We also possess product expertise for bathroom furniture, plastic-based wellness products such as bathtubs, and tap fittings and installation accessories using brass as the main material. In addition to raw materials for in-house production, we purchase merchandise from suppliers. In the Tableware Division, this relates primarily to glasses and cutlery. In the Bathroom and Wellness Division, we purchase items such as toilet seats, bathroom mirrors and outdoor whirlpools in order to round off our product range.

As a matter of principle, we prefer to source raw materials for in-house production from local suppliers. This typically means rapid availability and short transportation routes, which is also positive for the environment. In some cases, we are unable to use local suppliers due to limited resources, substantial quality fluctuations, uncompetitive prices, or the need for standardisation across our sites.

The total procurement volume in the Villeroy & Boch Group in the 2017 financial year was € 558.1 million. Goods and services purchased from suppliers in Germany accounted for 37.2 % of this figure.

The overarching aim of our procurement strategy is to select reliable suppliers that can provide the required materials and services in the required quality and volume at the right time and at the right price. We firmly believe that long-term relationships with suppliers in a spirit of mutual trust are an important factor in the success of our procurement organisation. We continuously refine our cooperation through regular feedback discussions and evaluations using a standardised catalogue of criteria including an assessment of environmental performance as well as quality, service and cost aspects. Our top priority is to prevent or minimize potential risks such as inadequate quality, supplier insolvency, interruptions of supply, or single sourcing. As part of our risk management, we permanently monitor the procurement markets and the financial position of key suppliers.

Responsibility in the supply chain

We are committed to upholding high standards when it comes to employment rights, human rights, health and safety, environmental protection and the fulfilment of statutory requirements. We examine and ensure compliance with these standards at our own production sites every single day. The demands we make of our suppliers are similarly high. This requires effective supply chain management.

Our Supplier Code of Conduct, which was extensively revised in the 2017 financial year, sets out our minimum requirements for business partners. The aim is to ensure that as many suppliers as possible sign up to this Code of Conduct or demonstrate the application of their own equivalent code of conduct. Our primary focus is on suppliers with a direct connection to our products or our value chain. A procurement volume of more than € 10,000 is applied as the materiality threshold. As at 31 December 2017, these criteria were met by 1,381 suppliers accounting for a total procurement volume of € 332.8 million. In the period under review, we significantly increased the extent to which this procurement volume is covered by a signed Code of Conduct or evidence of an equivalent code of conduct. Our aim is to improve this figure to at least 80 % by the end of the 2018 financial year by addressing existing suppliers in a targeted manner and adopting an even more systematic approach to new business partners.

Since 2017, all key suppliers have also been divided into four different risk classes on the basis of the Corruption Perception Index (CPI) published by Transparency International. For low-risk suppliers (e.g. from Germany), signing the Code of Conduct is considered to represent sufficient due diligence. In future, medium-risk and high-risk suppliers will also be required to self-disclose information on the basis of a standardised catalogue of questions and be assessed by our employees using a standardised visit report. Questions on employment rights, human rights, health and safety and environmental protections are key elements of these instruments. In addition, some suppliers

with the highest potential risk will be audited by external auditors every year. We seek to avoid dealing with suppliers from blacklisted nations.

4 ENVIRONMENT

We operate a total of 14 production and assembly sites in Europe, Asia and the Americas, nine of which are used to manufacture ceramic products. We are aware that this goes hand in hand with responsibility for the environment and climate protection. We are continuously improving our production processes in order to reduce production-related energy, raw material and water consumption, CO₂ emissions and non-recyclable waste, thereby cutting costs and improving our environmental and energy footprint.

Acting responsibly with regard to our ecosystem and the available resources forms part of our corporate culture. In the same way as our products are world leaders when it comes to quality and design, we want to achieve a leading position within our industry in terms of energy and the environment. This is based on structured environmental and energy management headed by our Group-wide Environment, Energy, Health and Safety (EEHS) department. At our production sites, we also employ specialists who develop and implement measures together with the respective plant managers and track target attainment. We use internationally recognised management systems in order to establish cross-site standards and enable comparability. At the reporting date, ten production sites were certified in accordance with the internationally recognised environmental management standard ISO 14001 and the energy management standard ISO 50001. Implementation at additional locations is planned or currently in preparation. Four locations also fulfil the even stricter requirements of EMAS III, a voluntary instrument instituted by the European Union for the continuous improvement of environmental performance.

In addition to the external audits conducted at regular intervals to confirm ISO certifications and EMAS validations, we have established a pool of internal auditors in recent years with responsibility for examining the environmental and energy management systems at local sites. The audit approach requires an annual audit of all production sites certified in accordance with ISO 14001, ISO 50001, or EMAS III. The audit programme and the aspects to be audited are prescribed by central environmental and energy management. Nine audits were conducted in the 2017 financial year.

Across all production sites, we have adopted the target of reducing specific gas and electricity consumption expressed in kilowatt hours per tonne of saleable goods by a low double-digit percentage by 2024 at the latest. The strategic objectives at our ceramic sanitary ware plants also include a pronounced increase in glaze recovery and a reduction in specific glaze and slip consumption by a low to medium single-digit percentage by 2019. Target attainment is regularly reviewed.

Considerable potential for improving raw material and energy efficiency is presented by a further reduction in reject rates. Digitisation can help in the form of statistical fault analysis and the stabilisation of process parameters. The basis for leveraging the resulting potential is provided by recording and collecting all of the relevant data for a product within the manufacturing process. Meas-

urement stations have been installed at all sanitary ware factories for this purpose. The aim is to combine data in such a way as to identify influences, critical ranges and interactions between the parameters in order to enable reliable predictions about the risk of a faulty product (predictive analytics). If the probability of error in a threshold-controlled process exceeds a defined level, the product is rejected as quickly as possible in order to prevent unnecessary material and energy consumption in the thermal processes. The successive improvement of these systems is expected to lead to a relevant increase in efficiency and earnings in the long term.

In addition, we are working on projects for heat recovery at our energy-intensive ceramic factories. In cooperation with renowned research institutions, we are also working on ideas for optimising and digitalising the firing process. Furthermore, we are evaluating the use of combined heat and power plants, like the one that was installed at the Mettlach site in 2014, and renewable energies in order to strengthen decentralised energy supply within our production network. We seek to improve energy efficiency when renovating existing building structures.

Although the EEHS department primarily focuses on environmental and energy management in production, energy management was also professionalised at several of our European sales companies in 2016. The starting point for this initiative was the EU Energy Efficiency Directive (EED). Eight national and management companies – including Finland, France, the United Kingdom and Spain – now have an energy management system certified in accordance with ISO 50001. The key objectives and measures at these units include making employees aware of the importance of energy efficiency and monitoring consumption data, as well as replacing old lighting elements with LEDs and generating electricity internally. Certification has allowed us to strengthen the continuous improvement process. An example: A solar power system was installed on the roof of our sales office in Helsinki (Finland) in 2017. This will almost entirely cover the energy requirements for the space used by us.

4.1 Energy consumption and emissions

The ceramic industry is traditionally energy-intensive. From the preparation of raw materials to the finished product, it involves products that require a high level of energy consumption. The sub-processes with the largest energy consumption are firing and – depending on the production technology used – casting and drying.

Accordingly, our reporting on energy consumption and CO₂ emissions focuses on our production locations. The most important form of energy in the 2017 financial year was gas, with total consumption of 496.7 million kilowatt hours (previous year: 487.0 million kWh). The gas-intensive firing process meant that 99.8 % of this figure was attributable to the ceramic factories in both divisions around the world. Electricity consumption in production amounted to 101.8 million kilowatt hours (previous year: 98.1 million kWh). Our ceramic production sites accounted for 86.2 % of this figure. The higher level of consumption compared with the previous year was attributable primarily to the 4.8 % increase in the net production volume at the sanitary ceramic ware plants.

CO₂ emissions can be calculated on the basis of our electricity, gas and oil consumption data and the CO₂ coefficients published by the respective utility companies. Emissions in the 2017 financial year totalled 148,646 tonnes (previous year: 141,858 tonnes), thereby increasing in line with the growth in the production volume.

Efficiency improvement measures

We permanently work on measures to improve the energy footprint of our production sites. High priority is given to the modernisation of existing plant and equipment, such as drying chambers and kilns, and the acquisition of new plant and equipment. Energy efficiency is a key factor when deciding on these investments, as this can allow us to reduce gas consumption, emissions and costs. In the 2017 financial year, for example, a new tunnel kiln was commissioned for our sanitary ware factory in Ramos (Mexico). This will significantly reduce gas consumption at the location.

Heat recovery has been used successfully at the Tableware sites in Merzig and Torgau for a number of years. In Merzig, ceramic pipes are used to dissipate the radiant heat generated by the firing process in order to pre-heat other products and heat the surrounding buildings. At the sister plant in Torgau, waste heat from the kiln is used for glazing and to heat production and storage rooms. New concepts are also being implemented in Mettlach and Hungary (using waste heat from the combined power plant and the kilns for the dryers) and in Romania (heat recovery at the air compressor station).

One big success in recent years has been the continuous reduction in energy consumption for the generation of compressed air. This has been achieved by investing in new compressors and systematically eliminating leakage.

In terms of building technology, lighting at several locations has been successively converted to energy-efficient LEDs. As part of the Mettlach 2.0 site development project, work on the completion of the central office and conference building continued in the period under review. The new building meets all modern heat protection requirements, uses well water for cooling and innovative CO₂-controlled air exchange.

In 2014, the cross-site energy management meeting was established as a new platform for intensifying the exchange of information on best practice solutions and future projects. The annual event is attended by the energy management officers from all of the ISO 50001-certified production sites and several members of the Management Board.

4.2 Resource efficiency in production

Manufacturing ceramic products – particularly in the Bathroom and Wellness Division – involves a high degree of process complexity. Drying and firing reduces the size of a toilet or washbasin by around 15 %. Handling natural materials and their inherent quality fluctuations, as well as factors such as process speed, product size and air humidity and temperature, lead to considerable complexity in the manufacturing process and can result in high reject rates.

Our aim is to minimise the use of ceramic slip and glaze. In the 2017 financial year, we prepared and used a total of 120,827 tonnes of ceramic slip and 12,698 tonnes of glaze across all of our sanitary ware plants in both divisions (previous year: 117,338 tonnes of ceramic slip and 12,312 tonnes of glaze). This increase reflected the higher production volume at our sanitary ceramic ware plants.

The figures also include materials collected and reused within the production process. In the case of ceramic slip, this means the excess slip from the casting process as well as so-called “green breakage”, i.e. parts that are rejected in the various quality controls prior to firing and subsequently recycled. For glaze recovery, the Mettlach sanitary ware factory uses a microfiltration system that gathers solids and re-adds them to the glaze preparation.

4.3 Water and waste water

The resource of water is also extremely important to the ceramic production process. As a matter of principle, we strive to reduce our freshwater consumption by using recycled water and – at the Mettlach site – ground water from our own well. In some cases, however, the technological requirements of the water-relevant processes are so high that we are required to use freshwater.

Our water consumption also requires responsible waste water management. To this end, we have installed a waste water treatment system at all of our ceramic production sites in order to filter ceramic and glaze residues from the waste water and recycle or dispose of them separately. The waste water is then fed into the municipal sewerage system in accordance with the respective local provisions. In the year under review, a new waste water treatment plant with state-of-the-art technology and higher capacity was installed at our sanitary ware factory in Hungary.

As a result of the increased production volume, our production sites used a total of 1,139,788 m³ of freshwater (previous year: 1,042,812 m³) and 232,231 m³ of recycled water (previous year: 211,955 m³) in the 2017 financial year.

4.4 Waste

The best kind of waste is no waste at all. To this end, increasing material efficiency and reducing the reject rate are the biggest levers for lowering the volume of waste generated. However, no manufacturing company will ever be able to avoid waste altogether. This is why we systematically seek out ways of recycling and reusing waste. In addition to reusing unfired breakage in ceramic production, we use wood scraps at our bathroom furniture production site in Mondsee (Austria) for heat generation, for example. A heating system fuelled by wood chips provides the majority of the location's heat requirements during the colder months. A similar concept is also used at our bathroom furniture factory in Treuchtlingen.

All waste that cannot be immediately recycled at the respective site is disposed of in accordance with the European or country-specific waste regulations. We comply with our post-disposal obligations at locations where we formerly operated landfill sites.

In the 2017 financial year, our production sites generated a total of 43,553 tonnes of waste (previous year: 41,373 tonnes). Here, too, the year-on-year increase was attributable to the higher net production volume at our ceramic sanitary ware factories.

5 EMPLOYEES

The Villeroy & Boch Group had a total of 8,099 employees worldwide as at 31 December 2017. This represented a year-on-year increase of 138 employees (previous year: 7,961) or 1.7 %. 33.6 % of the total workforce was employed in Germany (previous year: 34.1 %). There were 5,241 employees in the Bathroom and Wellness Division (previous year: 4,995) and 2,302 employees in the Tableware Division (previous year: 2,405). 556 employees (previous year: 561) were employed in central functions.

Production accounts for the largest proportion of our workforce – particularly at our international locations – at 49.8 %, followed by our sales and distribution employees at 27.8 %.

As a modern, responsible employer, we seek to provide our employees with interesting and challenging tasks and a varied, safe working environment so that they can make an active contribution. We see this as the basis for retaining our well-qualified, skilled and motivated employees and attracting qualified specialists and managers at all locations. The Human Resources (HR) department develops corresponding standards and seeks to ensure that the Group-wide processes are designed transparently and efficiently. The main activities are structured on the basis of the following strategic focal points:

- **Attractiveness as an employer:** We present employment at Villeroy & Boch as attractive and future-oriented for long-standing employees and new talents alike.
- **Long-term employee development:** We support the vocational training of young people and the further training of our workforce. Our comprehensive qualification programme helps to secure new talents and knowledge for the company.
- **Diversity and equality of opportunity:** We see the diversity of our employees as a key factor in our success and actively promote equality of opportunity.
- **Occupational health and safety:** We create a safe and healthy working environment with comprehensive standards and measures in the area of health management.

5.1 Attractiveness as an employer

“Opportunities for go-getters and goal-setters” – true to this motto, we are always on the hunt for people for every area of our company who want to join us in actively shaping the future of Villeroy & Boch. We are helped in this by our status as a strong employer brand, as illustrated by our performance in a national employer study conducted by Wirtschaftswoche. At the same time, we want to retain our employees for the long term, as sustainable business success can be achieved only with experienced, satisfied and committed employees. This includes conducting annual appraisal interviews with all commercial employees in order to assess their performance and potential

together with their line manager. In 2017, our employees had been with the Group for 13.07 years on average.

Fair working conditions and remuneration

Villeroy & Boch is committed to dealing with all employees respectfully and responsibly as a matter of principle. In our Code of Ethics and Code of Conduct, we undertake to uphold and protect human rights and to ensure employment that is compliant with all of the relevant laws and standards. We are also committed to a respectful and constructive dialogue with the corresponding employee representatives (Works Council), unions and other relevant bodies.

Fair working conditions also mean a fair and transparent remuneration system. This is based on clearly documented job profiles in conjunction with an internationally recognised grading system. We remunerate our employees in line with the market and irrespective of their gender, taking into account all statutory minimum wage provisions and industry-specific collective wage agreements at the individual locations. To help them to maintain their standard of living in old age, we offer our employees various options for participating in occupational and collectively agreed pension provision, the specifics of which vary from country to country.

Personnel expenses at the Villeroy & Boch Group amounted to € 286.1 million in the 2017 financial year (previous year: € 280.7 million).

Work-life balance

In terms of working hours, our employees have different preferences depending on their stage of life and how they structure their time. This is why we offer a range of flexible elements for individually structuring their work in terms of time and place so that they can achieve an optimal work-life balance. This includes flexible working hours for salaried employees and flexible shift systems, as well as part-time and partial retirement models. As at 31 December 2017, 14.8 % of the Group's workforce (previous year: 14.7 %) was employed on a part-time basis. A family-friendly HR policy naturally also includes offering the statutory maternity and paternity leave, care time and family care time in the respective countries with optimal conditions for our employees.

At Villeroy & Boch, flexible work models are also supported by digital solutions such as cloud-based applications, which are allowing us to increasingly give our employees the opportunity to work while on the move.

5.2 Long-term employee development

Our future business success depends on securing specialists and new talents for the company in a targeted, forward-looking manner. We actively address school pupils and students at an early stage with offers such as career days, internships and cooperative mentoring for degree theses. We also offer a broad range of skilled trades and dual study programmes in cooperation with regional, national and international training institutions and universities. In addition to our main training loca-

tions in Mettlach and Merzig, the Group uses smaller locations and organisational units for the development of talented young employees. At 31 December 2017, we employed a total of 190 young people throughout the Group in vocational training or as part of dual study programmes (previous year: 185). Of this figure, 88 (previous year: 70) were employed at our international locations.

We also offer a 30-month or 36-month trainee programme in order to inspire graduates with commercial and technical degrees to consider a career at Villeroy & Boch. At the reporting date, 58 talented young employees – including 12 at our international locations – were being prepared to assume specialist and management functions in various departments.

To facilitate even closer contact with universities and students, we have been a project partner of the renowned international student network Enactus since 2017. As well as providing financial support for the initiative, we want to act as a sparring partner for members of Enactus who get involved in social projects all around the world. The aim is to establish permanent project partnerships in which Villeroy & Boch employees can act as business advisors, assisting students with their experience and expertise.

Further and advanced training

Continuous development – both individually and collectively – is a fundamental requirement for successfully mastering the challenges of a business environment characterised by rapid change and remaining competitive in the long term.

First of all, this is achieved by enabling our employees to learn as part of their day-to-day work and in projects and by ensuring they have varied areas of activity with opportunities to take on new tasks at home and abroad. Modern digital communication channels are used to facilitate the internal exchange of information.

Secondly, the continuous development of all Group employees is achieved by offering them corresponding further and advanced training measures, particularly from our in-house Global Academy. Its portfolio includes a wide range of management and personality training programmes in the form of classroom-based events or digital learning formats (interactive e-learning, videos, webinars) aimed at improving employee skills and competencies. We also make use of relevant seminar offerings from external providers on a subject-specific basis as required.

A total of 1,704 employees at our German locations participated in training measures in the 2017 financial year (previous year: 1,460).

5.3 Diversity and equality of opportunity

The strength and innovation of Villeroy & Boch depends on diversity among our employees and the individual characteristics and perspectives they bring to their work. Accordingly, diversity and the corresponding equality of opportunity are a fixed element of our HR strategy and are firmly anchored within our Code of Ethics and our Code of Conduct. We do not tolerate any form of dis-

crimination against employees on the basis of their origin, gender, religion or belief, disability, age, or sexual identity.

With employees from 85 different nations, cultural diversity is a part of everyday life at the Villeroy & Boch Group. Our German locations alone had employees with 50 different nationalities at the reporting date. The number of foreign employees in Germany increased from 314 at the end of 2016 to 329 as at 31 December 2017.

The advancement of women, particularly in management positions, is a Group-wide strategic objective. At the reporting date, 35.4 % of employees throughout the Group as a whole were female. At the parent company Villeroy & Boch AG, the proportion of women at the two management levels below the Management Board was 36 %. Our long-term target remains 40 %.

When it comes to HR management, we see demographic change as a challenge and an opportunity in equal measure. In terms of the age diversity of our workforce, we seek to use the strengths of different age groups in a targeted manner and ensure adequate preparation for age-related departures as part of strategic succession planning. Within the Group, 30- to 50-year-olds are the largest group at 50.3 %, followed by the over 50s at 31.7 % and the under 30s at 18.0 %.

At Villeroy & Boch, we also promote an integrative corporate culture in which people with disabilities are appreciated for their skills and individual talents and fully integrated into the working environment. As at 31 December 2017, the proportion of employees with disabilities in Germany increased from 4.1 % to 4.3 %, corresponding to 117 people (previous year: 111).

5.4 Occupational health and safety

The health of our employees and their safety in the workplace are also fundamental elements of the Villeroy & Boch Group's sustainable HR strategy. In a continuous process, we develop our active safety culture in compliance with the respective statutory requirements and beyond. The Group-wide point of contact with responsibility for standards in the area of occupational health and safety is the Environmental, Energy, Health and Safety (EEHS) organisational unit. It manages the relevant projects and defines, coordinates and monitors improvement measures within the Group. The successful operational implementation of these topics is also ensured by local EEHS officers at the individual regional locations.

Work safety within the company and along the value chain enjoys maximum priority at Villeroy & Boch. This is reflected in our permanent "zero accident philosophy". To achieve this, we have implemented safety standards and processes that are subject to strict criteria and that we continuously enhance and monitor by way of internal audits. Our Belgian wellness production site in Roeselare was certified in accordance with the OHSAS 18001 (Occupational Health and Safety Assessment Series) standard as part of a pilot project. For our other Group locations, we will endeavour to obtain certification in accordance with the future global standard ISO 45001, which is expected to be published in 2018. It will define the requirements for occupational health and safety

management systems as part of an integrated approach for the first time and provide instructions on implementation.

A high degree of safety awareness and individual responsibility on the part of our employees is a basic prerequisite for identifying and removing accident risks and other potential dangers in our working environment. To this end, we provide our local employees with regular training and qualification in the form of relevant information events, workshops and training sessions.

All workstations within our organisation are subject to systematic evaluation in terms of health and safety risks, including compliance with ergonomic standards. Together with the continuous evaluation and analysis of measurable indicators such as the number of accidents and near misses in the workplace, potential areas for improvement are identified in order to enable us to respond as preventively as possible by taking organisational, technical or medical measures. Examples include equipping our sanitary ware plants with a new kind of plaster work booth or using state-of-the-art lifting aids for the manual movement of sanitary ware parts (e.g. from the kiln car to the sorting belts), the introduction of which has significantly reduced the physical burden on employees in terms of lifting and carrying.

Our production and logistics locations are the main areas of relevance when it comes to reporting quantitative accident data as they are subject to a higher risk of workplace accidents, e.g. due to the forklift trucks in circulation and the machines being operated. We have also integrated employee accident data at our head office in Mettlach into our reporting. All in all, we therefore report accident data covering 4,703 employees.

In the 2017 financial year, there were a total of 90 reportable workplace and work-related road traffic accidents within the defined scope resulting in the employees affected being unable to work for more than three days. This resulted in a total absence of 16,729 working hours. The accident rate - expressed as the number of workplace and work-related road traffic accidents per 10,000 working hours - amounted to 0.12.

Above and beyond occupational safety, we aim to look after and promote the health of our employees at all locations on a holistic basis. Our wide-ranging healthcare offering is aimed at improving both physical and mental vitality in order to ensure an agile, high-performance organisation even at an advanced age. We regularly conduct various local health campaigns, such as medical screenings and check-ups, subject-specific information events and workshops as part of our health days, as well as offering a wide range of preventive measures such as vaccinations. These services have met with an extremely positive response among our employees. The end result is a sickness rate that has been low for many years. In the 2017 reporting period, the Group-wide sickness rate remained unchanged year-on-year at 3.6 %.

ABOUT THE REPORT

This is the Villeroy & Boch Group's first sustainability report. It covers the period from 1 January 2017 to 31 December 2017. Future editions of the sustainability report will be published annually. The latest version is available to download from the company's website at www.villeroyboch-group.com/en/investor-relations/publications/sustainability-reports.

The report also constitutes the separate non-financial Group report within the meaning of section 315b of the German Commercial Code (HGB), with which Villeroy & Boch AG is alternatively meeting the obligation set out in section 315b (1) HGB. This Group report is combined with the separate non-financial report of Villeroy & Boch AG. Unless otherwise stated, the information shown relates to the Villeroy & Boch Group. The Group companies included in the report are the same as the consolidated group in the 2017 consolidated financial statements. The report has been approved by the Management Board of Villeroy & Boch AG. Its content has not been reviewed externally.

As an international group, we applied the GRI G4 guidelines in identifying the key areas within the materiality analysis. In terms of the report itself, we opted to deviate from the provisions of the GRI G4 guidelines in selected cases. We thereby waive the right to include the note "GRI-compliant".

This sustainability report contains forward-looking statements based on management estimates of future developments at the time at which the report is prepared. These statements are subject to risks and uncertainties that Villeroy & Boch is largely unable to influence or precisely estimate. This includes the future economic and legal conditions and the behaviour of other market participants. If this or other uncertainties occur or the assumptions on which the forward-looking statements are based prove to be incorrect, the actual results could deviate from the expected results described in this report.

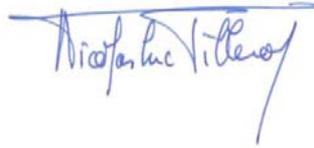
For improved readability, we have generally avoided using both genders. This does not constitute a value judgement. All statements should be considered gender-neutral.

Further information can be found at www.villeroyboch-group.com and in the 2017 Annual Report. The next sustainability report is expected to be published in spring 2019.

Mettlach, 31 January 2018



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