

Integrated Report február / 2017

- Comfort for homes
- Sustainability for the future
- Competitiveness for companies
- Innovation for infrastructure

Our goal is to offer a reliable, high-quality, and environmentally-friendly energy supply, in order to:

- Improve the well-being of people.
- Drive the economic and social development of the communities in which we are present.
- Create sustainable value for our shareholders, employees, customers, suppliers, and society in general.

Mission

We create value in a sustainable way and we are committed to social dividend.

Vision

We want to be a global energy leader and create a better future for people with the support of our human team.

Values

The twelve values inspire and guide the Group's strategy and all of its actions.

Whitelee wind farm,
Scotland / UK
© Chris James

Utility of the future



Iberdrola's Public Information

Iberdrola makes all of its public information available to our shareholders, employees, customers, suppliers, and society in general to provide reliable and relevant information regarding the Company's performance and its strategic lines for the coming years.

Annual information

Integrated Report

Prepared based on the recommendations of the International Integrated Reporting Council (IIRC).

Financial Report

Prepared according to international financial reporting standards and externally audited.

Corporate Governance Report

Prepared according to the form provided by the National Securities Market Commission of Spain.

Sustainability Report

Prepared according to the Global Reporting Initiative (GRI) guidelines and externally assured.

Activities Report of the Board of Directors and of the Committees thereof

Prepared according to Iberdrola internal standards.

Director Remuneration Report

Prepared according to the form provided by the National Securities Market Commission of Spain.

Report on Compliance with Legal Provisions on the Separation of Regulated Activities

Prepared according to Iberdrola internal standards.

Report on Related-Party Transactions with Directors and Significant Shareholders

Prepared according to Iberdrola internal standards.

Report on the Application of the Shareholder Engagement Policy and the Policy regarding Communication and Contacts with Shareholders, Institutional Investors, and Proxy Advisors.

Prepared according to Iberdrola internal standards.

Report on the Independence of the Auditor in relation to the audit report for financial year 2016.

Prepared according to Iberdrola internal standards.

Additional information

Quarterly Results Report

IBE Watch Fact Sheet

Quarterly Shareholder Bulletin

Innovation Report

Environmental Footprint Report

Biodiversity Report

Greenhouse Gas Report

Information on the corporate website www.iberdrola.com

About Us

Corporate Governance

Sustainability

Shareholders and Investors

Suppliers

People and Talent

Press Room



Access the annual reports for financial year 2016 and supplementary documentation regarding the Iberdrola Group by scanning the corresponding QR code using your smart phone or tablet:

© This icon refers to related information. It also gives information on other specific reports where more information of interest can be accessed.

Integrated Report

February 2017

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Notes:

- The company Iberdrola, S.A., parent company of the Iberdrola Group, is referred to as "Iberdrola" or the "Company" in this report. Iberdrola (as parent company) and the group of subsidiaries over which Iberdrola has the power of control or joint control is also referred to as the "Iberdrola Group" or the "Group".
- The figures included in this translation follow the customary English convention, with figures in thousands separated by a comma (,) and decimals indicated by a full stop (.).
- €M: millions of euros; \$M: millions of dollars.

Letter from the Chairman & CEO

Ignacio S. Galán
Chairman & CEO of Iberdrola
© Adrián Ruiz



“In the coming years, Iberdrola will intensify its wager on the solutions required by the energy transition and which have made the company the utility of the future”.

I am pleased to present to you Iberdrola's Integrated Report, in which you can find extensive and detailed information regarding the Group's performance, the strategic foundations on which the company addresses its future, and the most significant aspects of its performance.

In the energy scenario within which Iberdrola will be acting in the coming years, notable progress has been made towards the achievement of a more sustainable energy model following the entry into force of the Paris Climate Summit Agreement on 4 November, only eleven months after it was signed. This swiftness of action, which stands in contrast with the almost eight years that the Kyoto Protocol took to come to fruition, reveals the firm commitment of the international community to reduce the emissions causing climate change and to limit the increase in temperature to less than 2 degrees by the end of the century as compared to the levels of the pre-industrial era, leaving the door open for an improvement of this goal to 1.5 degrees.

This commitment was ratified at the latest Climate Summit, held in Marrakesh, through the establishment of the agenda and the instruments needed to implement the Paris Agreement over the next two years and the preparation of working programmes on key issues in order to facilitate compliance therewith.

Meanwhile, the European Commission has affirmed its goal of a 40% reduction in CO₂ emissions by 2030 and its intention for the European Union to lead the energy transition through its “Clean Energy for All Europeans” package of proposals.

In this context, and given the technological potential of our industry to contribute to decarbonisation thanks to renewable energy, increased electrification of the economy is indispensable to honour the international commitments concerning emissions and at the same time respond to the strong growth in global energy demand.

In the coming years, Iberdrola will intensify its firm wager on the solutions required by the energy transition and which have made the company the utility of the future: more renewable energies, increased storage capacity, more and smarter grids, and growing digitisation to offer new and better services to our customers.

2016-2020: accelerating growth

In February 2017, Iberdrola updated its *Outlook 2016-2020*, which was presented a year ago, following its decision to increase investments to 25,000 million euros during the period in view of the company's financial strength to take advantage of new

opportunities for growth, primarily for the development of renewable energy projects in the United States.

Following its unique model, which combines geographic diversification with a focus on activities linked to the energy transition, the Company will allocate 91% of investment to the expansion and digitisation of networks, renewable energy, and regulated generation, which areas will contribute 81% of the Group's Ebitda. By currency, the investments will be split amongst dollars (48%), pounds (29%), euros (20%), and other (3%), and will go mainly to countries with an A rating.

Iberdrola will add 8,200 MW of new capacity to its generation pool through 2020, such that the Group's overall capacity will exceed 50,000 MW (with more than 29,000 MW of renewable energy), growing 12% from year-end 2015.

During the 2016-2020 period, the Company expects to obtain annual average growth in after-tax profits of approximately 7.5% (which will come mainly from countries with an A rating), up to approximately 3,500 million euros.

At the same time, we will continue to maintain financial strength, increase the return on investments, and improve operational efficiency thanks to advances in automation and digitisation in all businesses and processes.

Iberdrola will thus offer its shareholders growing remuneration in line with its results, with a pay-out of between 65% and 75%, such that a range of between 0.37 and 0.40 euro per share could be reached by 2020, with a floor of 0.31 euro per share in any case. We will also maintain the flexible dividend formula, and the current number of outstanding shares will remain stable.

Impact on society

The expansion of this strategic coverage will allow us to continue generating a positive economic and social impact on all of the regions in which we have a presence, contributing to their progress and to the well-being of their citizens. According to a study by PwC,⁽¹⁾ for each euro obtained in profits, Iberdrola contributes 11.1 euros to the GDP of the countries in which it does business.

We will thus continue to act as a major driving force through procurement contracts (which came to more than 9,800 million euros in 2016, thus exceeding the record figure for the prior year) and through our commitment to maintaining and creating stable and quality jobs, as shown by the addition of more than 2,600 people to our workforce only last year. Overall, Iberdrola provides direct, indirect, and induced employment to 288,000 people throughout the world, thanks to its investments and operations.⁽¹⁾

"The expansion of our strategic coverage will allow us to continue generating a positive economic and social impact on all of the regions in which we have a presence".

Our unwavering commitment to the training of the company's personnel (we currently provide three times more hours of training per employee per year than the average of European companies⁽¹⁾) will be boosted by the activities of the Iberdrola Campus in Madrid, which, with a built-up area of 45,000 square metres and 540 seats in classrooms and workshops, has already become a leading centre for corporate training. We will also continue to improve the management of our human resources by promoting the reconciliation of working and family life, gender equality, and job security.

Iberdrola will also strengthen its commitment to clean energies and to protection of the environment, by increasing its production capacity with renewable technologies over the next years and by reaffirming its goal to reach a 50% reduction in emissions by 2030 as compared to 2007 levels.

The development of our sustainable business model will allow us to remain at the top of the main indices in this field, such as the Dow Jones Sustainability Index (on which we are the only European electric utility to have been included for seventeen years), FTSE4Good, and CDP Climate Change.

Furthermore, our efforts in the area of R&D (to which we allocated 211 million euros in 2016) will be focused on sustainability, the promotion of renewable energy, and the exploitation of the opportunities offered by digitisation and automation for the development of new products and services. We thus expect to continue to be at the forefront among the most innovating electric utilities, Iberdrola now being the fourth largest electric company in the world by volume of investment.⁽¹⁾

As part of our commitment to society, the Foundations of the Iberdrola Group will continue with their programmes in the areas of training and research (primarily through the International Scholarship Programme), the protection of biodiversity and the promotion of art and culture, and cooperation and solidarity with the most vulnerable groups.

In the coming years, we will also move forward with the "Electricity for All" programme, which in 2016 already reached more than two and a half million beneficiaries in emerging or developing countries who have been given access to electric power, the aim being to reach four million beneficiaries by 2020. In parallel with all of the foregoing, Iberdrola will continue to develop its Corporate Governance System, based on ethical principles, transparency, and leadership in the application of the best international practices on good governance, an area in which the company has become an international leader.

⁽¹⁾ PwC study "Iberdrola's economic, social, and environmental impact on the world" (based on 2015 data).

Wikinger marine wind farm -
Baltic Sea / Germany

© David López Navarro





Iberdrola Today

1.1 Iberdrola Today

Our activities

- Production of electricity from renewable and conventional sources.
- Purchase/sale of electricity and gas on wholesale markets.
- Transmission and distribution of electricity.
- Supply of electricity, gas, and related energy services.
- Other activities, mainly linked to the energy sector.

Presence focused on the Atlantic area

Iberdrola carries out its activities mainly in the five countries of the Atlantic area: Spain, the United Kingdom, the United States, Mexico, and Brazil.

What we are

The process of internationalisation carried out in recent years has led Iberdrola to be one of the leading electric companies, and among the largest utilities in the world by stock market capitalisation. The corporate and governance structure is described in chapter 5.1 of this report and consists of:

- Iberdrola, as a holding company.
- Country subholding companies in the 5 main geographic areas of activity.
- Head of business companies reporting to the country subholding companies.

Iberdrola is one of the leading electric companies in the world.

2016 Data Iberdrola Group

46,925

MW
Installed capacity⁽¹⁾

142,453

GWh
Net output⁽¹⁾

229,816

GWh
Electric power distributed⁽¹⁾

9,884

€M
Procurement awarded

27,723

MW
Renewable installed capacity⁽¹⁾

34.5

Million
users⁽¹⁾

5,750

€M
Direct tax contribution

30,591

People
Direct employment

288,000

People
Direct, indirect, and induced employment⁽²⁾

4,264

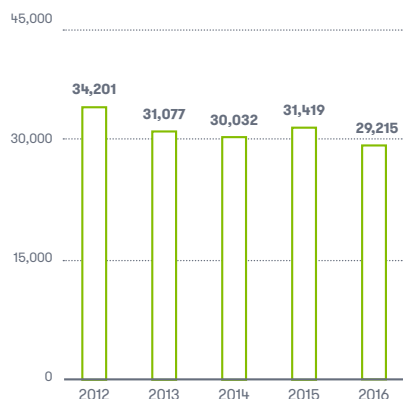
€M
Investments

(1) Managed magnitudes including 100% Neoenergia.

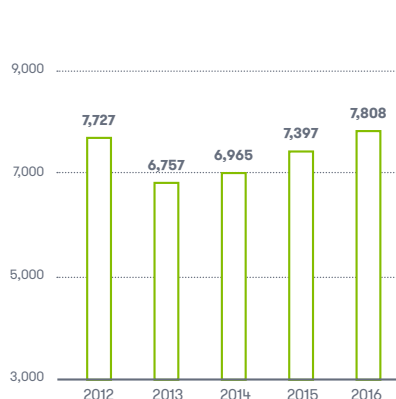
(2) Data from a Study of Iberdrola's Impact, prepared by PwC, based on 2015 figures.

1.2 Company Performance

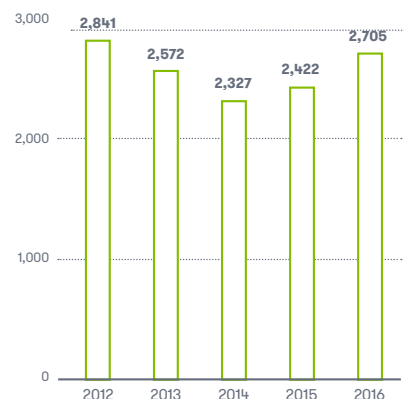
Revenues (€M)



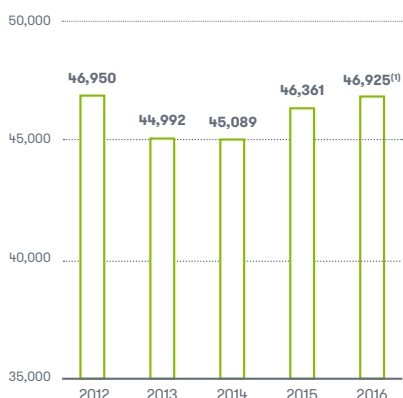
Ebitda (€M)



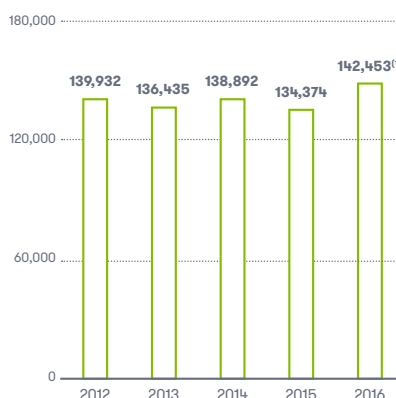
Net Profit (€M)



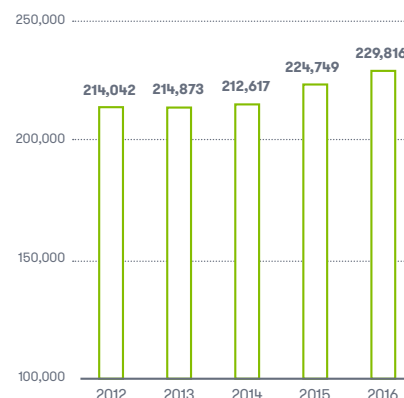
Installed capacity (MW)



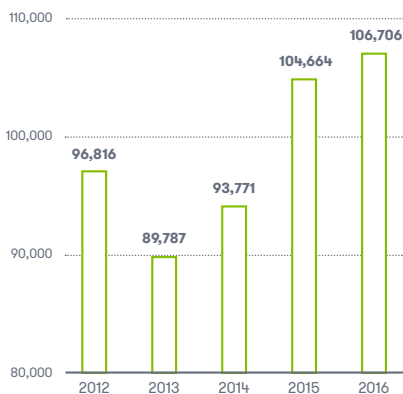
Net output (GWh)



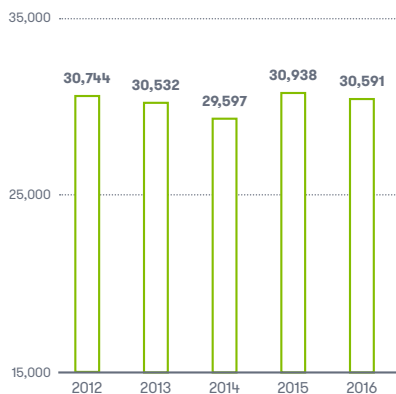
Energy distributed (GWh)⁽¹⁾



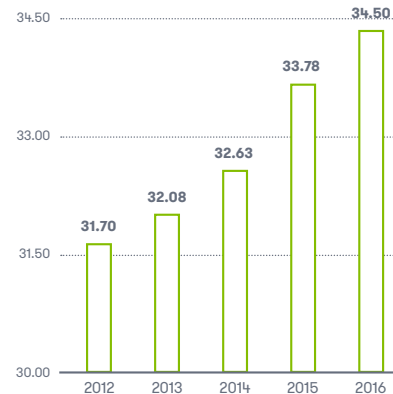
Assets (€M)



Employees



Users (millions)



(1) Managed magnitudes including 100% Neoenergia.

* Note: Due to legal requirements, Iberdrola has applied International Financial Reporting Standard IFRS-11 to the financial information for the financial years 2013 to 2016, which aspect should be taken into account in evaluating the historical performance of the Company.

1.3 Key Figures

| Financial performance (€M) | 2012 | 2013 | 2014 | 2015 | 2016 | Δ annual average 2012-16 | Δ 2015-2016 |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|--------------------------|---------------|
| Revenues | 34,201.2 | 31,077.1 | 30,032.3 | 31,418.7 | 29,215.4 | -3.9% | -7.0% |
| Consolidated Gross Margin | 12,578.1 | 11,781.9 | 12,179.5 | 12,842.7 | 12,916.2 | 0.7% | 0.6% |
| Consolidated Ebitda | 7,726.6 | 6,756.9 | 6,964.5 | 7,397.4 | 7,807.7 | 0.3% | 5.5% |
| Ebitda - Networks (Regulated) | 3,773.7 | 3,346.5 | 3,534.7 | 3,628.0 | 4,081.7 | 2.0% | 12.5% |
| Spain | 1,348.3 | 1,450.3 | 1,438.5 | 1,456.8 | 1,603.1 | 4.4% | 10.0% |
| United Kingdom | 937.3 | 939.0 | 1,024.8 | 1,138.0 | 976.2 | 1.0% | -14.2% |
| United States | 660.2 | 718.2 | 772.0 | 780.5 | 1,269.6 | 17.8% | 62.7% |
| Brazil | 827.9 | 239.0 | 299.4 | 252.7 | 232.8 | -27.2% | -7.9% |
| Ebitda - Wholesale and Retail (Liberalised) | 2,355.2 | 1,986.6 | 2,292.2 | 2,323.1 | 2,253.3 | -1.1% | -3.0% |
| Spain | 1,605.4 | 1,341.2 | 1,517.6 | 1,504.6 | 1,520.5 | -1.3% | 1.1% |
| United Kingdom | 360.6 | 320.4 | 456.6 | 421.7 | 293.6 | -5.0% | -30.4% |
| United States | 9.1 | -22.6 | -32.0 | -58.4 | 6.1 | -9.5% | - |
| Mexico and Brazil ⁽¹⁾ | 380.1 | 347.6 | 350.0 | 455.2 | 433.1 | 3.3% | -4.9% |
| Ebitda - Renewables | 1,620.3 | 1,501.1 | 1,326.0 | 1,647.2 | 1,500.2 | -1.9% | -8.9% |
| Spain | 804.3 | 668.4 | 420.6 | 473.2 | 497.4 | -11.3% | 5.1% |
| United Kingdom | 168.1 | 231.8 | 265.2 | 438.1 | 267.0 | 12.3% | -39.1% |
| United States | 412.2 | 448.0 | 495.3 | 570.9 | 563.6 | 8.1% | -1.3% |
| Mexico | 37.2 | 34.1 | 38.2 | 43.1 | 52.0 | 8.7% | 20.6% |
| Brazil | 11.3 | 9.1 | 33.0 | 26.9 | 24.9 | 21.8% | -7.4% |
| Rest of World | 187.2 | 109.7 | 73.7 | 95.0 | 95.3 | -15.5% | 0.3% |
| Ebitda - other businesses | 44.3 | 0.5 | -17.0 | -10.5 | -111.3 | - | - |
| Ebitda - Corporation and adjustments | -66.9 | -77.8 | -171.4 | -190.4 | 83.8 | - | - |
| Amortisation charge, provisions, and other | -3,349.7 | -4,537.5 | -3,023.6 | -3,568.1 | -3,253.7 | 0.7% | 8.8% |
| Operating profit (EBIT) | 4,376.9 | 2,219.5 | 3,940.9 | 3,829.3 | 4,554.0 | 1.0% | 18.9% |
| Financial result | -1,100.3 | -1,277.9 | -1,122.4 | -1,023.1 | -903.4 | 4.8% | 11.7% |
| Results from companies accounted for using the equity method | -187.5 | 205.0 | 135.4 | 55.3 | 48.7 | - | -11.9% |
| Gains on non-current assets | -13.9 | -10.4 | 247.9 | 125.1 | 48.2 | - | -61.5% |
| Profit before Tax (PBT) | 3,075.1 | 1,136.1 | 3,201.8 | 2,986.6 | 3,747.5 | 5.1% | 25.5% |
| Corporate tax | -206.5 | 1,466.7 | -837.1 | -527.1 | -904.6 | -44.7% | -71.6% |
| Non-controlling interests | -27.9 | -31.0 | -38.2 | -38.0 | -137.9 | -49.1% | -262.9% |
| Net attributable profit | 2,840.7 | 2,571.8 | 2,326.5 | 2,421.6 | 2,705.0 | -1.2% | 11.7% |
| Total assets | 96,816.4 | 89,786.8 | 93,771.4 | 104,664.1 | 106,706.2 | 2.5% | 2.0% |
| Equity | 34,084.8 | 35,288.6 | 35,790.5 | 40,956.1 | 40,687.4 | 4.5% | -0.7% |
| Net investments | 3,259.0 | 3,053.0 | 2,848.0 | 3,223.0 | 4,264.3 | 7.0% | 32.3% |
| Funds from operations (FFO) | 6,196.0 | 5,619.0 | 5,459.0 | 5,906.7 | 6,310.8 | 0.5% | 6.8% |
| Net financial debt | 30,324.4 | 26,836.3 | 25,618.4 | 28,067.1 | 29,414.0 | -0.8% | 4.8% |

| Financial ratios | 2012 | 2013 | 2014 | 2015 | 2016 | Δ annual average 2012-16 | Δ 2015-2016 |
|---|-------------|-------------|-------------|-------------|-------------|--------------------------|--------------|
| Ebitda - outside eurozone (%) | 51.0 | 49.5 | 54.0 | 56.0 | 54.0 | 1.4% | -3.6% |
| Ebitda margin (Ebitda/revenue) (%) | 22.6 | 21.7 | 23.2 | 23.5 | 26.7 | 4.3% | 13.5% |
| Net profit margin (Net profit/Revenues) (%) | 8.3 | 8.3 | 7.7 | 7.7 | 9.3 | 2.8% | 20.1% |
| NOE/Gross margin (%) | 30.1 | 29.4 | 29.8 | 29.8 | 27.7 | -2.1% | -7.3% |
| Net financial debt/ebitda (multiple) | 3.92 | 3.97 | 3.68 | 3.79 | 3.77 | -1.0% | -0.6% |
| Financial leverage (%) | 47.1 | 43.2 | 41.7 | 40.7 | 42.0 | -2.8% | 3.2% |
| Funds from operations (FFO)/Net financial debt (NFD) | 20.4 | 20.8 | 21.3 | 21.0 | 21.5 | 1.3% | 1.9% |
| Retained cash flow (RCF/NFD) (%) | 17.2 | 17.5 | 17.4 | 18.7 | 19.1 | 2.6% | 2.0% |
| Return on equity (ROE) (%) | 8.3 | 7.5 | 6.7 | 6.3 | 7.3 | -3.2% | 15.9% |

| Stock market performance | 2012 | 2013 | 2014 | 2015 | 2016 | Δ annual average 2012-16 | Δ 2015-2016 |
|--|---------------|---------------|---------------|---------------|---------------|--------------------------|---------------|
| Stock market capitalisation (€M) | 25,753 | 28,922 | 35,756 | 41,506 | 39,661 | 11.4% | -4.4% |
| Number of shares at year-end (millions) | 6,139 | 6,240 | 6,388 | 6,337 | 6,362 | 0.9% | 0.4% |
| Share price (€) | 4.20 | 4.63 | 5.60 | 6.55 | 6.23 | 10.4% | -4.8% |
| Earnings per share (EPS) | 0.45 | 0.41 | 0.36 | 0.37 | 0.42 | -1.7% | 14.4% |
| Dividend per share (DPS) | 0.340 | 0.310 | 0.275 | 0.276 | 0.286 | -4.2% | 3.6% |
| Dividend yield (%) | 8.13 | 6.65 | 4.91 | 4.21 | 4.59 | -13.3% | 9.0% |
| Total dividend (including payment in kind) (€M) | 2,093 | 1,922 | 1,716 | 1,732 | 1,966 | -1.6% | 13.5% |
| Payout ratio (%) | 65.4 | 65.5 | 73.8 | 71.5 | 72.7 | 2.7% | 1.7% |
| Price/net earnings per share (PER) | 9.31 | 11.25 | 15.37 | 17.17 | 14.66 | 12.0% | -14.6% |

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(1) These figures only include Mexico until 2015. The 2015 and 2016 figures include the value for Mexico and Brazil.

* Note: Due to legal requirements, Iberdrola has applied International Financial Reporting Standard IFRS-11 to the financial information for financial years 2013 to 2016, which aspect should be taken into account in evaluating the historical performance of the Company.

| Operating performance | 2012 | 2013 | 2014 | 2015 | 2016 | Δ annual average 2012-16 | Δ 2015-2016 |
|---|---------|---------|---------|---------|------------------------|--------------------------|-------------|
| Installed capacity (MW) | 46,950 | 44,992 | 45,089 | 46,361 | 46,925 ⁽¹⁾ | -0.9% | -2.4% |
| Net output (GWh) | 139,932 | 136,435 | 138,892 | 134,374 | 142,453 ⁽¹⁾ | -0.5% | 2.2% |
| Electric power distributed (GWh) ⁽¹⁾ | 214,042 | 214,873 | 212,617 | 224,749 | 229,816 | 1.8% | 2.3% |

| Environmental performance | 2012 | 2013 | 2014 | 2015 | 2016 | Δ annual average 2012-16 | Δ 2015-2016 |
|--|---------|---------|---------|---------|---------|--------------------------|-------------|
| Emission-free installed capacity (%) | 59.4 | 61.2 | 61.9 | 63.0 | 65.9 | 2.6% | 4.6% |
| Emission-free production (%) | 51.9 | 54.6 | 56.8 | 52.5 | 57.1 | 2.4% | 8.8% |
| Specific CO ₂ emissions (t/GWh) | 264 | 226 | 212 | 225 | 176 | -9.6% | -21.8% |
| Fuel consumption (M Tep) | 19,236 | 18,968 | 18,849 | 19,001 | 17,734 | -2.0% | -6.7% |
| Environmental investments (€M) | 1,062.4 | 1,015.7 | 1,100.9 | 1,014.2 | 2,262.2 | 20.8% | 123.1% |
| Environmental expenses (€M) | 723.3 | 686.4 | 635.7 | 669.2 | 527.1 | -7.6% | -21.2% |
| Energy produced under certified environmental management systems (%) | 85.2 | 84.4 | 87.0 | 84.2 | 84.0 | -0.4% | -0.2% |
| Water use/overall production (m ³ /GWh) | 699 | 976 | 509 | 533 | 586 | -4.3% | 9.9% |
| Direct CO ₂ emissions. Scope 1 (kt) | 35,461 | 31,846 | 30,217 | 31,752 | 25,194 | -8.2% | -20.7% |
| Indirect CO ₂ emissions. Scope 2 (kt) | 2,122 | 997 | 1,544 | 963 | 817 | -21.2% | -15.2% |
| CO ₂ avoided due to efficiency initiatives (kt) | 24,014 | 18,480 | 21,459 | 19,269 | 16,461 | -9.0% | 14.6% |
| SO ₂ emissions (t/GWh) | 0.366 | 0.217 | 0.154 | 0.125 | 0.051 | -38.9% | -59.2% |
| NO _x emissions (t/GWh) | 0.334 | 0.262 | 0.236 | 0.230 | 0.144 | -19.0% | -37.4% |

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| Social performance | 2012 | 2013 | 2014 | 2015 | 2016 | Δ annual average 2012-16 | Δ 2015-2016 |
|---|--------|--------|--------|--------|--------|--------------------------|-------------|
| Users (millions) | 31.7 | 32.1 | 32.6 | 33.8 | 34.5 | 2.1% | 2.0% |
| Electrical power | 28.1 | 28.5 | 29.0 | 29.7 | 30.4 | 2.0% | 2.4% |
| Spain | 10.9 | 10.9 | 10.9 | 10.9 | 11.0 | 0.1% | 0.5% |
| United Kingdom | 3.5 | 3.5 | 3.5 | 3.5 | 3.5 | 0.1% | 0.6% |
| United States | 1.8 | 1.8 | 1.8 | 2.2 | 2.5 | 8.5% | 13.2% |
| Latin America | 11.9 | 12.4 | 12.8 | 13.1 | 13.4 | 3.0% | 2.3% |
| Gas | 3.6 | 3.6 | 3.6 | 4.1 | 4.1 | 3.3% | -0.2% |
| Spain | 0.8 | 0.8 | 0.8 | 0.9 | 0.9 | 4.1% | 5.6% |
| United Kingdom | 2.2 | 2.2 | 2.2 | 2.2 | 2.1 | -0.8% | -2.7% |
| United States | 0.6 | 0.6 | 0.6 | 1.0 | 1.0 | 13.6% | 0.0% |
| Number of employees | 30,744 | 30,532 | 29,597 | 30,938 | 30,591 | -0.1% | -1.1% |
| Permanent contracts (%) | 98.0 | 98.5 | 98.5 | 98.4 | 98.7 | 0.2% | 0.3% |
| Employees with collective bargaining agreement (%) | 79.8 | 79.4 | 79.0 | 76.6 | 76.9 | -0.9% | 0.4% |
| Employee turnover (%) | 10.6 | 6.6 | 8.6 | 7.0 | 7.3 | -8.9% | 4.3% |
| Diversity (men/women) | 76/24 | 76/24 | 77/23 | 76/24 | 76/24 | - | - |
| Ratio between basic entry level wage and local minimum wage (%) | 151 | 154 | 161 | 153 | 154 | 0.6% | 0.9% |
| Injury rate (IR) | 0.34 | 0.46 | 0.39 | 0.28 | 0.35 | 0.7% | 25.0% |
| Hours of training (millions of hours) | 1.12 | 1.2 | 1.0 | 0.9 | 1.3 | 3.8% | 44.4% |
| Hours of training per employee (h) | 44.2 | 44.7 | 38.7 | 38.6 | 46.0 | 1.0% | 19.2% |
| Funds for social development (€M) | 51.7 | 91.7 | 65.0 | 46.0 | 61.5 | 4.4% | 33.7% |
| Contributions to society (€M) | 37.7 | 31.6 | 34.0 | 38.0 | 43.7 | 3.8% | 15.0% |
| Rural electrification programmes (€M) | 14 | 60 | 31 | 8 | 17.8 | 6.2% | 122.5% |
| Investments in R&D (€M) | 145 | 159 | 170 | 200 | 211 | 9.8% | 5.5% |
| General procurement (€M invoiced) ⁽²⁾ | 4,830 | 4,359 | 4,599 | 5,093 | 6,415 | 7.4% | 26.0% |
| Procurement from qualified suppliers (%) | 84 | 87 | 92 | 94 | 89 | 1.5% | -5.3% |
| Number of suppliers with social responsibility standards | 1,233 | 1,202 | 1,326 | 1,536 | 1,667 | 7.8% | 8.5% |
| Procurement in sensitive countries per ILO (%) | 8.9 | 12.0 | 10.7 | 10.8 | 8.2 | -2.1% | -24.2% |
| Procurement from local suppliers (%) | 90 | 86 | 87 | 85 | 84 | -1.7% | -1.2% |

(1) Managed magnitudes including 100% Neoenergia.

(2) Supplies in the amount of 9,884 million euros were awarded during 2016.

1.4 Presence by Areas of Activity

Iberdrola in Spain

Largest energy company

Δ 2016 / 2015

GDP +3.0%

Electricity demand +0.7%

Primary brands



**IBERDROLA
ESPAÑA**

Spain subholding company



**IBERDROLA
ESPAÑA**
Renovables

Renewables business



**IBERDROLA
ESPAÑA**
Redes

Networks business



**IBERDROLA
DISTRIBUCIÓN
ELÉCTRICA**



**IBERDROLA
ESPAÑA**
Generación

Wholesale and retail business



IBERDROLA



IBERDROLA
Inmobiliaria

Real Estate



IBERDROLA
Ingeniería y Construcción

Engineering



Fundación
**IBERDROLA
ESPAÑA**

Foundation

2016 data

26,162

MW
Installed capacity

15,819

MW
Renewable installed capacity

62,784

GWh
Net output

267,576

Km
Power lines

92,308

GWh
Electric power distributed

11.8

Million users

10,395

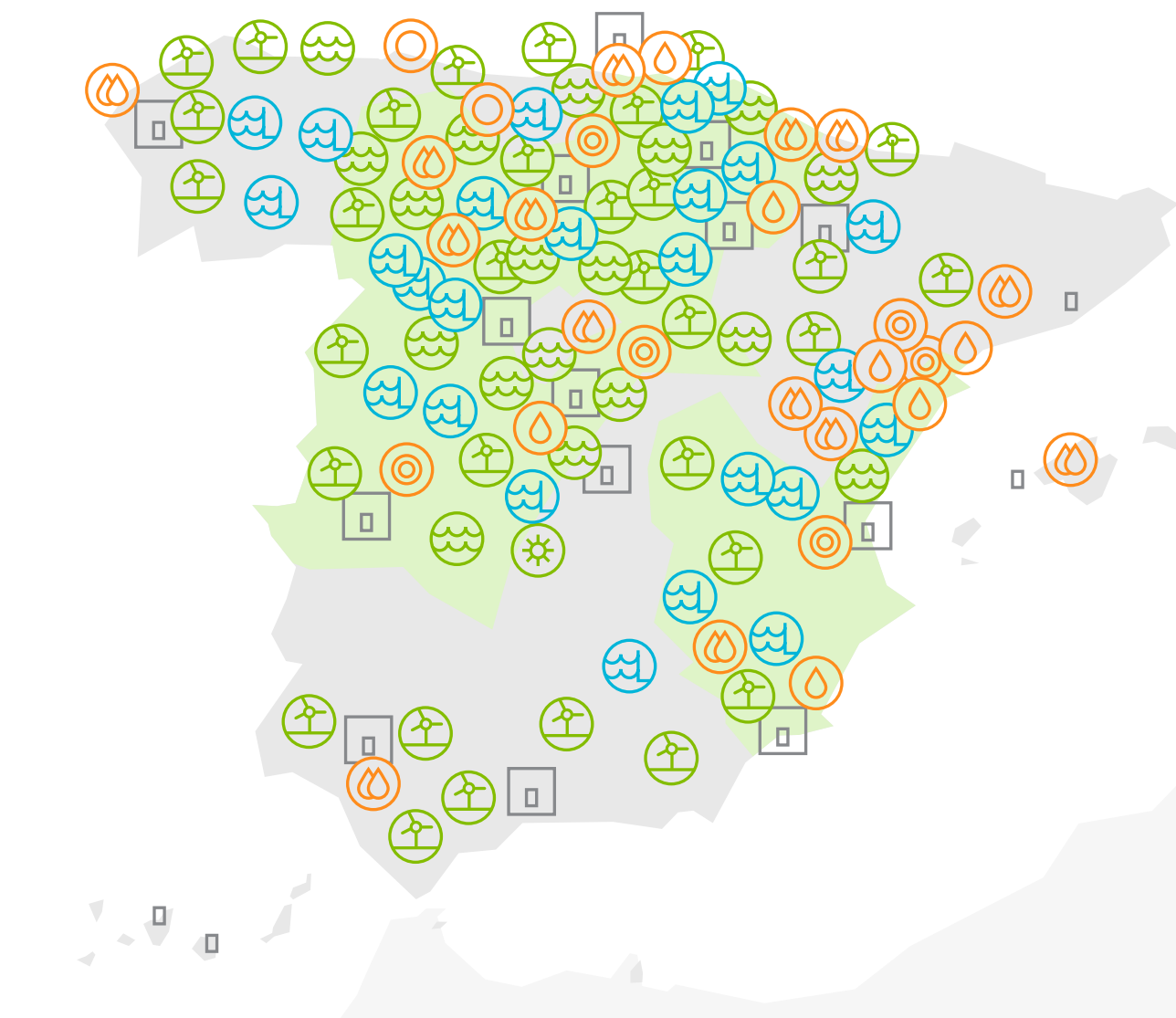
Employees

649

€M
Investments

3,454

€M
Direct tax contribution



Primary facilities

195



Windfarms
5,751 MW

89



Minihydro power plants
303 MW

1



Solar thermal plant
50 MW

8



Combined cycle gas plants
5,695 MW

20



Cogeneration plants
364 MW

6



Nuclear plants
3,410 MW

2



Thermal plants
874 MW

79



Hydro power plants
9,715 MW



Offices

Area
of influence

Electricity
distribution

Iberdrola in the United Kingdom

Largest wind producer

3rd-largest network company

Δ 2016 / 2015

GDP +1.8%

Electricity demand -1.3%

Primary brands



SCOTTISHPOWER

United Kingdom subholding company



**SCOTTISHPOWER
RENEWABLES**

Renewables businesses



**SP ENERGY
NETWORKS**

Networks business



SCOTTISH OWE
Generati



SCOTTISHPOWER

Wholesale and retail business



IBERDROLA
Engi ing & Constructi

Engineering



Foundation
SCOTTISHPOWER

Foundation

2016 data

4,537

MW

Installed capacity

2,568

MW

Renewable installed capacity

13,748

GWh

Net output

108,818

Km

Power lines

35,704

GWh

Electric power distributed

5.6

Million users

6,373

Employees

1,740

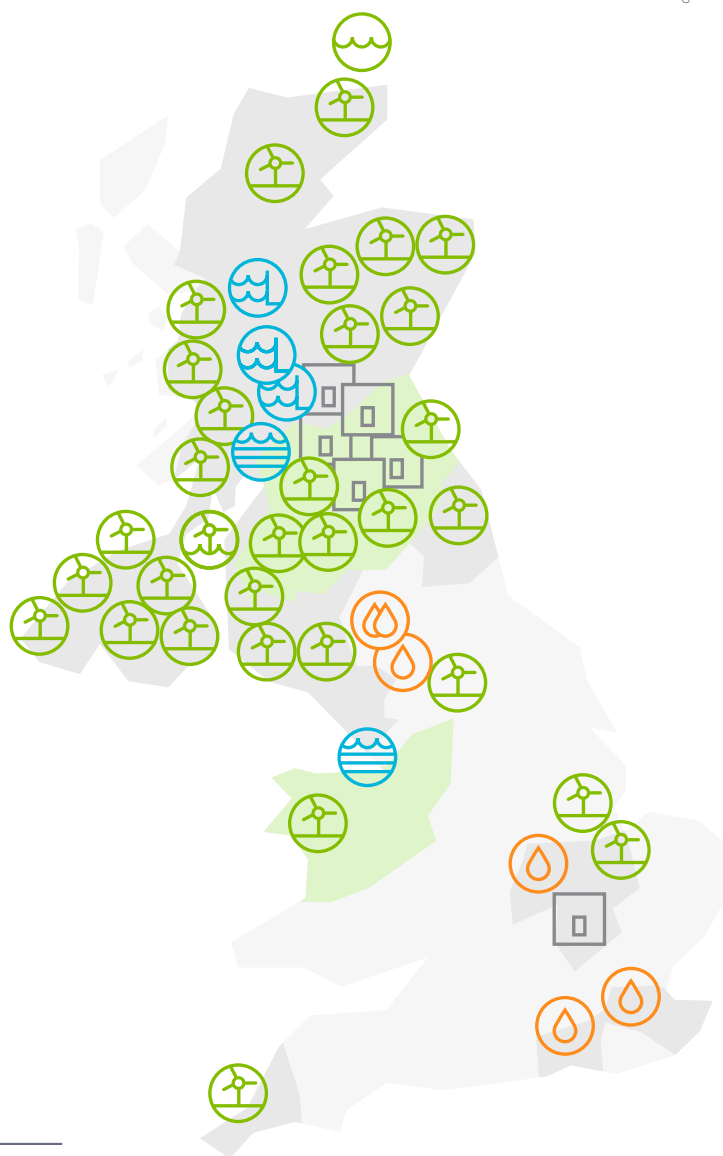
€M

Investments

536

€M

Direct tax contribution



Primary facilities

32

Windfarms
1,811 MW

1

Offshore windfarm
194 MW

1

Cogeneration plant
1 MW

4

Combined cycle gas plants
1,967 MW

3

Hydro power plants
563 MW

1

Underwater power line
425 Km



Offices

Area
of influence

Electricity
distribution

Iberdrola in the United States

Second-largest wind producer

Electricity and gas distributor in New York, Maine, Connecticut, and Massachusetts

Δ 2016 / 2015

GDP +1.9%

Electricity demand -1.3%

Primary brands



AVANGRID

United States subholding company



AVANGRID RENEWABLES

Renewables business



IBERDROLA Energy Projects

Engineering



AVANGRID Networks



CENTRAL MAINE POWER



MAINE NATURAL GAS



NYSEG



RG&E



UI



SCG



CNG



BERKSHIRE GAS

Regulated networks business and sale of electricity and gas



Foundation AVANGRID

Foundation

2016 data

6,875

MW

Installed capacity

6,033

MW

Renewable installed capacity

17,912

GWh

Net output

130,791

Km

Power lines

39,079

GWh

Electric power distributed

3.5

Million users

6,849

Employees

1,492

€M

Investments

864

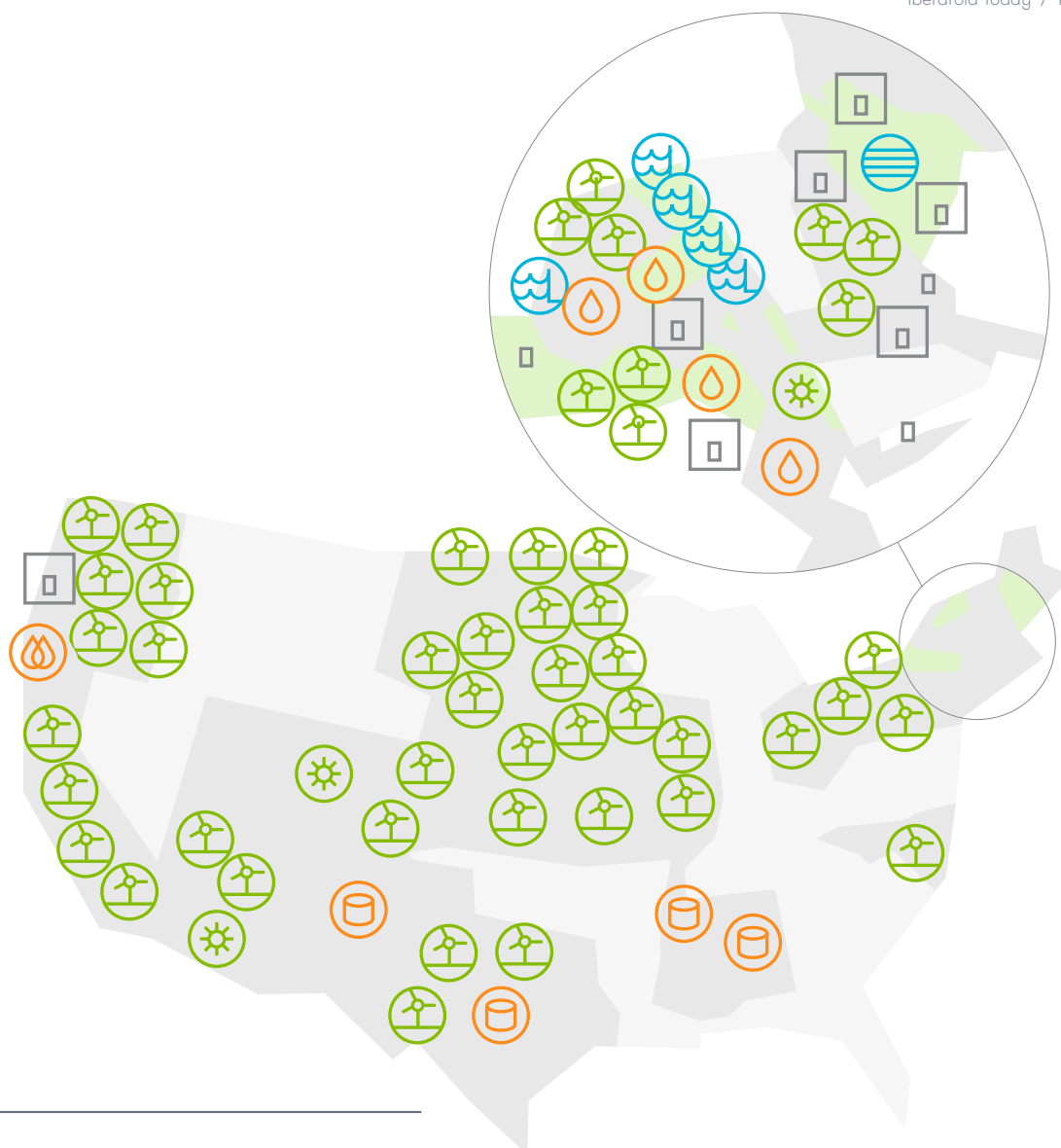
€M

Direct tax contribution


2.4

BCM

Gas storage capacity



Primary facilities

55 
Windfarms
5,855 MW

2 
Photovoltaic energy
50 MW

1 
Cogeneration plant
636 MW

4 
Gas storage
facilities

4 
Combined cycle gas plants
209 MW

9 
Hydro power plants
118 MW

1 
Power transmission line
United States-Canada / 708 Km



Offices

Area
of influence

Electricity
distribution

Iberdrola in Mexico

Largest private electricity producer

Δ 2016 / 2015

GDP +2.3%

Electricity demand +3.2%

Primary brands



**IBERDROLA
MÉXICO**

Mexico subholding
company



**IBERDROLA
MÉXICO**
Renovables

Renewables business



**IBERDROLA
MÉXICO**
Generación

Wholesale generation
business



IBERDROLA
Ingeniería y Construcción

Engineering

2016 data

5,804

MW
Installed capacity

367

MW
Renewable installed capacity

37,569

GWh
Net output

874

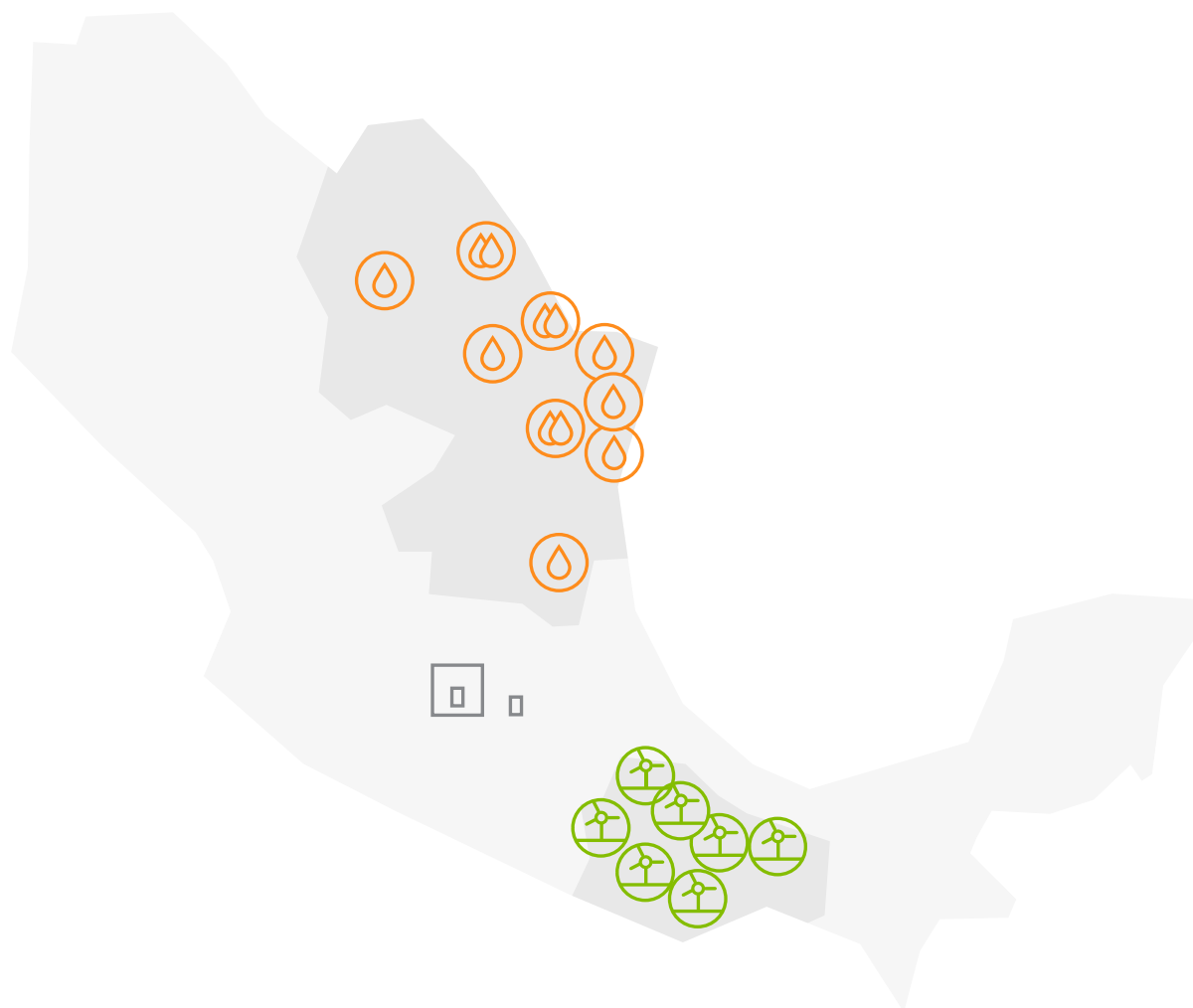
Employees

358

€M
Investments

209

€M
Direct tax contribution



Primary facilities

7



Windfarms
367 MW

3



Cogeneration plants
237 MW

6



Combined cycle gas plants
5,200 MW



Offices

Area
of influence

Iberdrola in Brazil

Largest distributor in Brazil by number of customers

Δ 2016 / 2015

GDP -3.5%

Electricity demand -0.9%

Primary brands



ELEKTRO

Brazil subholding
company



Instituto

ELEKTRO



IBERDROLA

Ingeniería y Construcción
Engineering

2016 data

2,926

MW
Installed capacity⁽¹⁾

2,315

MW
Renewable installed capacity⁽¹⁾

9,003

GWh
Net output⁽¹⁾

592,717

Km
Power lines⁽¹⁾

62,726

GWh
Electric power distributed⁽¹⁾

13.4

Million users⁽¹⁾

3,742

Employees

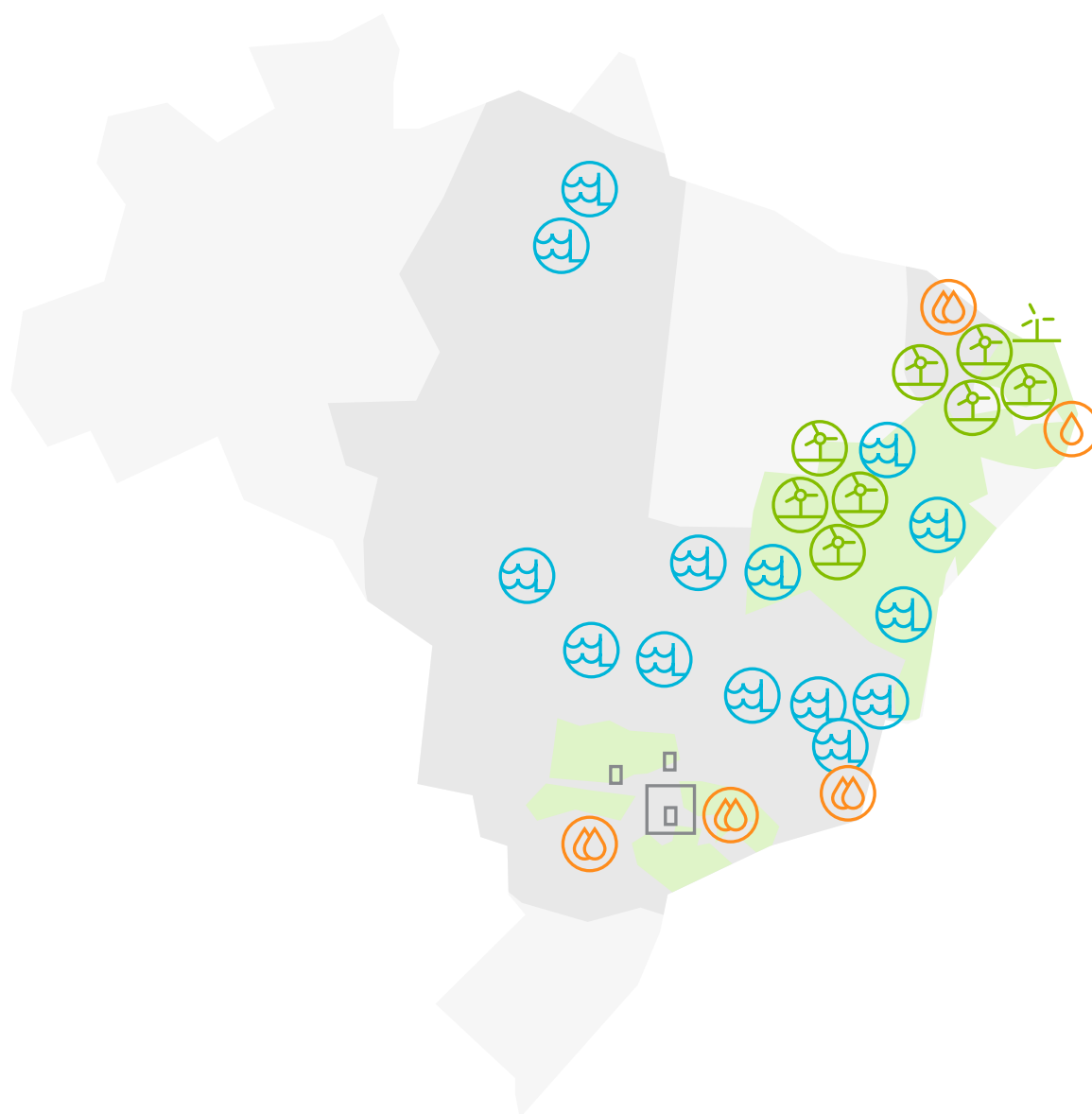
81

€M
Investments

593

€M
Direct tax contribution

⁽¹⁾ Managed magnitudes including 100% Neoenergia.



Primary facilities

11 

Windfarms
337 MW

4 

Cogeneration plants
78 MW

1 

Combined cycle gas plant
533 MW

14 

Hydro power plants
1,978 MW



Offices

Area
of influence

Electricity
distribution

Aledeadóvila Hydroelectric
plant, Salamanca
/ España
© Iberdrola, S.A.



2.

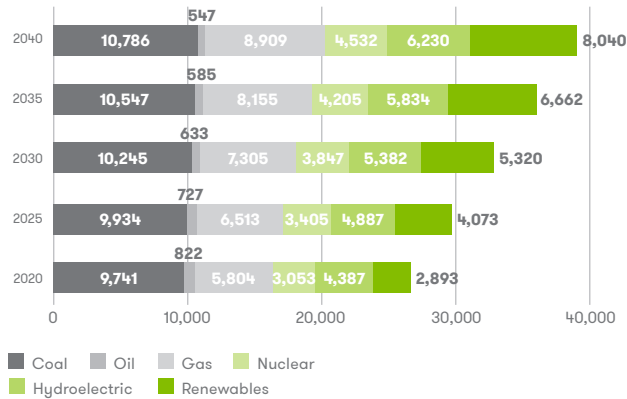
Business Model and Strategy

2.1 The Future of Energy

Opportunities for continued growth

The energy sector presents strong opportunities for growth over the long term.

Electricity production by type of source (TWh)



Source: World Energy Outlook 2016 - International Energy Agency

“Meeting the emissions targets will only be possible by massively electrifying the economy, through more clean energies, especially hydroelectric, wind and solar power, more storage capacity, and more and smarter distribution networks”

Ignacio Galán, at the WORLD ECONOMIC FORUM 2017

The electric industry, according to World Energy Outlook 2016

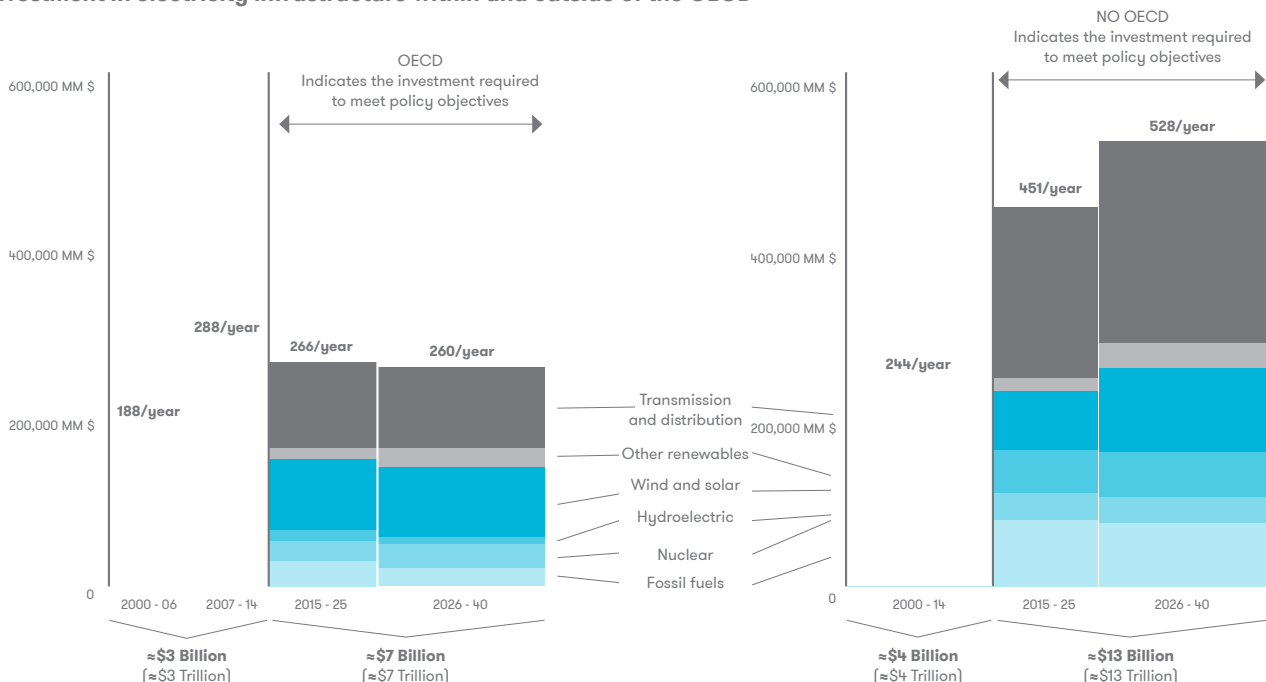
The Paris Agreement on climate change (COP21) will transform the global energy system in the coming decades.

The electricity sector is the focus of many of the Paris commitments. Almost 60% of all new electric generation capacity to be installed through 2040 will come from renewable sources. It is also estimated that by 2040 most renewable generation will be competitive without needing any kind of subsidy.

Another important factor in the near future will be the strengthening of the electric distribution grids, to facilitate better integration of renewable technologies, and ensuring the availability of sufficient backup capacity.

It will also be interesting to have the ability to store energy and to improve energy efficiency in all industries and energy-using processes.

Investment in electricity infrastructure within and outside of the OECD



Source: The Future of Electricity Report, World Economic Forum 2016

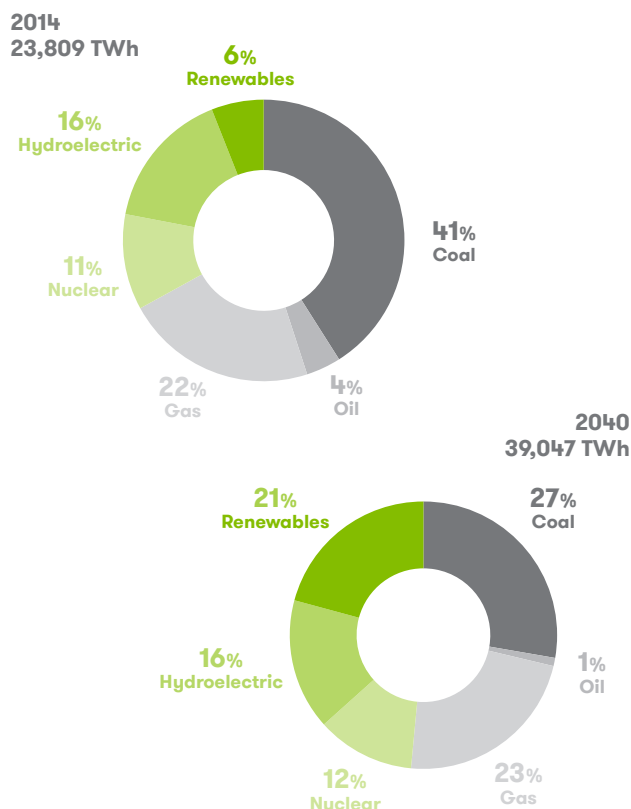
Evolution of demand^{(1), (2)}

The prospects set out in *International Energy Outlook 2016* regarding the use of energy continue to show an increase in energy demand over the next three decades, driven mainly by non-OECD countries, whose strong long-term economic growth translates into a growing demand for energy.

The EU Roadmap forecasts that electricity will at least double its share in final energy demand to 36-39% in 2050, which would contribute to a reduction in carbon emissions in heating systems and in the transport sector.

The energy sector is launching measures to reduce CO₂ emissions, showing its commitment to reach the goals set out in the Paris Agreement on climate change.

Growth in global electricity production (TWh)⁽³⁾



Sources: [1] *World Energy Outlook 2016* - IEA; [2] *Energy Roadmap 2050* of the European Parliament; [3] *World Energy Outlook 2016* - IEA

Trends in production and use of electricity

Sectoral^{(4), (5), (6)}

- The European Union has a significant challenge in meeting its commitments on climate and energy established for 2020, 2030, and 2050. The energy sector knows that supplying energy with lower CO₂ emissions is not an option, but rather a necessity.
- Rapid development of electricity output with renewable sources will mean lower manufacturing costs: an additional reduction in the average cost of photovoltaic solar energy and onshore wind energy is expected from now through 2040.
- Unsustainable pressure on natural resources. A world economy four times larger than today is projected to use 80% more energy in 2050.

Technological^{(4), (5), (7)}

- Rapid implementation of technologies with low variable costs, like most renewable energies, increases the possibility of sustainable periods of low wholesale electricity prices.
- Intelligent technologies applied to networks and remote management will allow for more active participation of demand and thus strengthen the role of the consumer in the energy market.
- Urban/technological lifestyles require more electricity. The growing middle class, the increase in income, and the larger amount of electric appliances will contribute to a doubling of electricity demand through 2060.
- Electricity storage, as a still-embryonic technological possibility, can open up new vistas for the operation and management of power systems.

Consumption^{(4), (6)}

- 1.2 billion people, or 17% of the global population, currently lack access to electricity, and 2.7 billion people, or 38% of the global population, put their health at risk by resorting to the traditional use of solid biomass for cooking.
- Over the next 25 years, it will be necessary to reduce emissions by almost half in order to halt climate change, with the difficulty that if consumption stays on its current pace, it will have increased by approximately 45%. "To solve this equation, we will need a huge energy transformation that can increase efficiency and substantially alter the energy mix with a higher contribution of low carbon sources" (Ignacio Galán).
- The development of new uses and applications for electricity may result in new markets and opportunities.

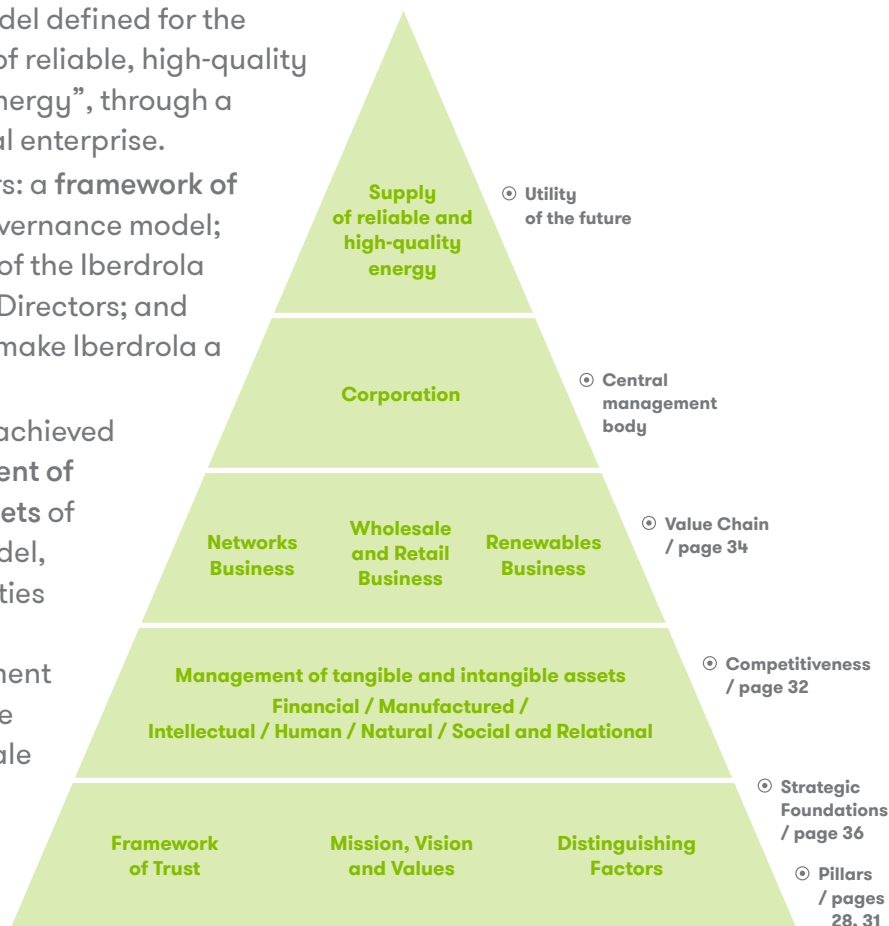
Sources: [4] *World Energy Outlook 2016* - IEA; [5] *Energy today in Spain, 15 key issues for the next legislature* - Club Español de la Energía; [6] *World Energy Outlook 2014* - IEA; [7] *World Energy Scenarios 2016* - World Energy Council

2.2 Business Model

The purpose of the business model defined for the Iberdrola Group is the “supply of reliable, high-quality and environmentally-friendly energy”, through a sustainable, long-term industrial enterprise.

The model is built on three pillars: a framework of trust based on an advanced governance model; the Mission, Vision, and Values of the Iberdrola Group defined by the Board of Directors; and the distinguishing factors that make Iberdrola a different company.

The model’s competitiveness is achieved through responsible management of the tangible and intangible assets of the Company. To apply this model, Iberdrola has defined the activities in which it seeks to be an active player, structuring its management into three global businesses: The Networks Business, the Wholesale and Retail Business, and the Renewables Business, with a Corporation as the Group’s central management unit.



Framework of trust

To ensure the sustainability of its business model, Iberdrola has implemented:

- A Corporate Governance System consistent with best international practices.
- Corporate ethics, internalised by the management units and the organisation as a whole.
- Social responsibility policies, with a view to meeting the expectations of Stakeholders.
- An advanced risk control system, to maintain an optimal “risk/opportunity” balance, taking advantage of opportunities and mitigating risks.

⊙ Corporate Governance Model
/ page 78

Mission, Vision, and Values

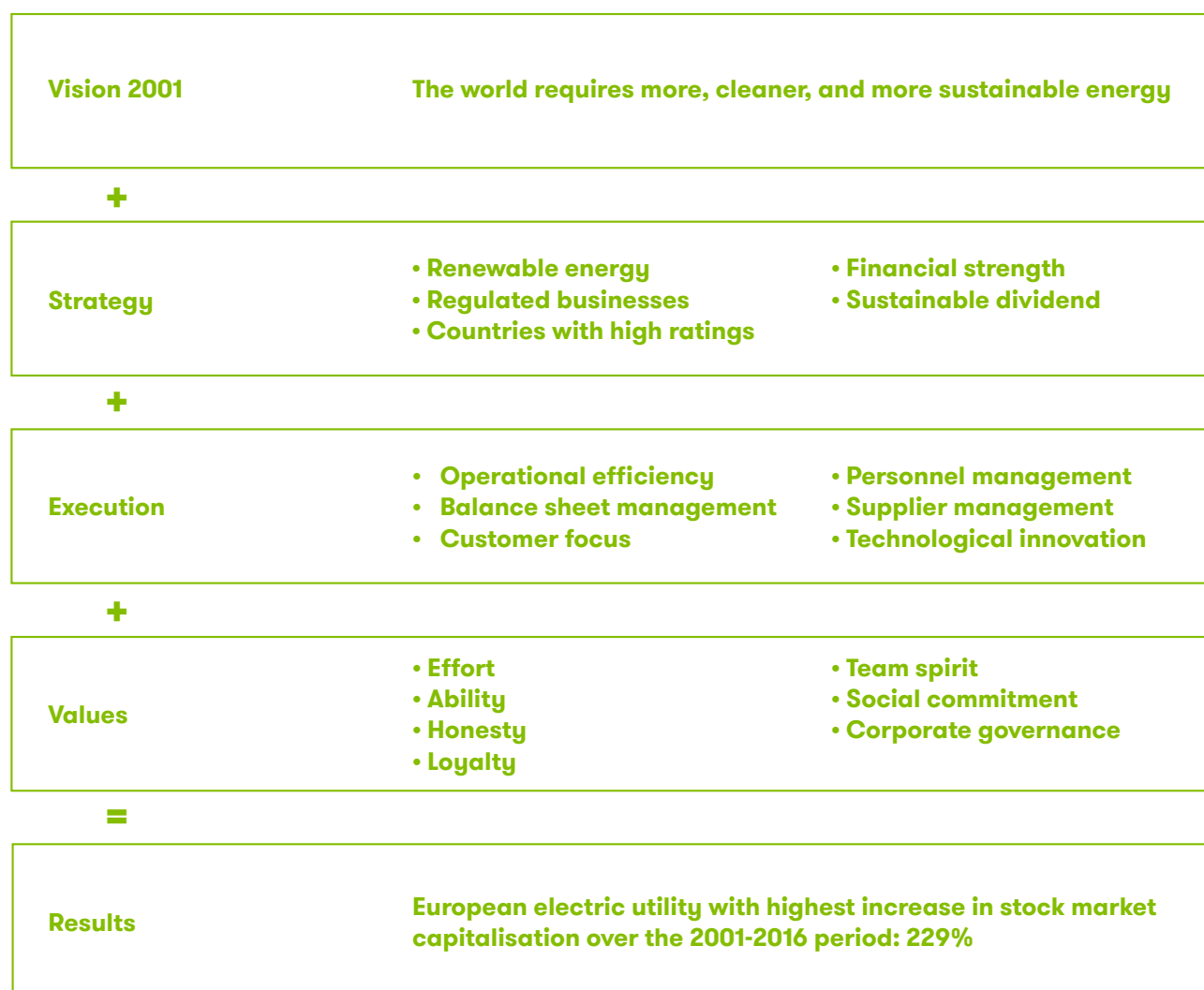
“We want to be the leading multinational group in the energy sector at the forefront of a better future, sustainably creating value with a quality service for people...”.

This Vision is based on twelve Values:

- Sustainable creation of value
- Ethical principles
- Good corporate governance and transparency
- Development of our workforce
- Social commitment
- Sense of belonging
- Safety and reliability
- Quality
- Innovation
- Respect for the environment
- Customer focus
- Institutional loyalty

⊙ Ethics and Social Responsibility
/ page 90

Iberdrola wants to be a responsible and sustainable company, serving society and people
The Company has been leading with a history of growth and foresight...



... with a very positive impact on society

Iberdrola generates a number of very significant economic, social, and environmental impacts on the countries in which it does business. The most significant are⁽¹⁾:

- Annual generation of more than €27,000 million in Gross Domestic Product (GDP) in the countries in which it operates.
- Annual contribution of more than €4,400 million in investments, for the capital formation of the world economy.
- Investment of more than €2,300 million in “green generation” (2013-15), entailing:
 - Installed green capacity (hydroelectric and renewable) constituting 55% of all of Iberdrola’s installed capacity.
 - Avoidance of the emission of more than 57 million tonnes of CO₂.
- Creation of close to 300,000 jobs throughout the world (direct, indirect, and induced employment).
- Investments of more than €100 million in rural electrification programmes in Brazil (2013-15), and facilitating access to electricity for more than 1.4 million people in developing countries (2014-15).

⁽¹⁾ Data from a Study of Iberdrola’s Impact, prepared by PwC, based on 2015 figures.


Iberdrola's strategy is perfectly aligned with the Sustainable Development Goals (SDGs)


Iberdrola is fully committed to the Sustainable Development Goals defined by the United Nations for the 2015-2030 period. There are 17 global goals intended to transform our world, ending poverty, fighting against inequality and injustice, and confronting climate change. They affect both developing and developed countries, and also all types of organisations and institutions, including companies.

Iberdrola has incorporated the Sustainable Development Goals (SDGs) into its business strategy and its *Sustainability Policy*.

The Company has prioritised the various SDGs based on type of activity, defining 3 levels of contribution:

Main focus

| | | | | | | |
|---|-------------------------|--|------------------|--|--|--|
|  | Goal | | 2020 | | | |
| | ▲ Access to electricity | | 4 million people | | | |

| | | | | | |
|--|-------------------|--|------|------|---------|
|  | Goal | | 2020 | 2030 | 2050 |
| | ▼ CO ₂ | | 30% | 50% | Neutral |

Direct contribution



Indirect contribution



Iberdrola has set ambitious challenges relating to the Goals selected as its principal Focus:

- **Goal 13 Climate action:** Achieve a 30% reduction in the intensity of CO₂ emissions by 2020 compared to those in 2007; a 50% reduction in emissions intensity by 2030; and be carbon neutral by 2050.

At year-end 2016, Iberdrola's emissions intensity was 34% lower than the European average, and 66% of its installed capacity is emission-free.

- **Goal 7 Affordable and clean energy:** By 2020, bring electricity to 4 million people who today lack access to this energy source.

By year-end 2016, we had contributed to 2.5 million people benefiting from access to electricity through projects carried out in various countries of Latin America and Africa.

2.3 Iberdrola, a Different Company

⊙ Iberdrola's Primary Businesses
/ page 43

Focus on basic and regulated businesses

Approximately 75% of Ebitda comes from regulated businesses or long-term contracts.

Operational efficiency

An energy model based on clean energy, networks, and digitisation has allowed our Company to be 30% more efficient than the average for the industry in Europe.

⊙ Iberdrola's Primary Businesses
/ page 43

⊙ Presence by Areas of Activity
/ page 14

International diversification

Approximately 55% of earnings are generated outside of Spain.

Financial strength and solidity of the Group

- Strengthening of the balance sheet due to growth in Ebitda and FFO, which allows for continued strength in solvency ratio levels.
- Liquidity position that covers financial needs for more than 18 months under a stress scenario.

⊙ Financial capital
/ page 62

⊙ Natural Capital
/ page 70

Commitment to clean and competitive energies

- Generation and production of largely emissions-free electricity.
- Large portfolio of offshore wind generation projects and wave and tidal power projects.
- Clear goals for reducing emissions.

Global, committed, and qualified workforce

- Stable and high-quality jobs, with high level of training.
- Health and safety as values: "accident reduction" goal.
- The companies of the Group have been recognised: In Spain for their Reputation (Merco) and in Brazil as the best company to work for in Latin America (Great Place to Work).

⊙ Human Capital
/ page 68

2.4 Management of Tangible and Intangible Assets

| | ⓘ Financial capital / page 62 | ⓘ Manufactured Capital / page 64 | ⓘ Intellectual Capital / page 66 |
|---------------------|---|--|--|
| | Financial capital | Manufactured capital | Intellectual capital |
| What is it? | Financial resources that the Company already has or obtains through financing. | Tangible assets or goods used by the Company to carry out its business activities. | Intangible, knowledge-based assets. |
| Management Approach | Create value for shareholders through sustainable growth. | Offer a competitive supply of energy in a safe and reliable environment. | Consider innovation as a strategic element of the Company. |
| Significant aspects | <ul style="list-style-type: none"> • Balanced growth. • Sound financial structure. • Operational efficiency. • Sustainable results and dividends. | <ul style="list-style-type: none"> • Power generation assets. • Power transmission and distribution assets. • Other assets. | <ul style="list-style-type: none"> • Promotion of R&D. • Efficiency and new products and services. • Disruptive technology and business models. |

The Iberdrola Group holds valuable assets for the development of its business model. The strategy defined by the Company transforms these assets to create value for all its Stakeholders.

| <p>⊙ Human Capital / page 68</p> | <p>⊙ Natural Capital / page 70</p> | <p>⊙ Social and Relational Capital / page 72</p> |
|--|--|--|
| Human capital | Natural capital | Social and relationship capital |
| Employee knowledge, skills, experience and motivation. | Natural resources affected by the Company's activities. | Ability to share, relate, and collaborate with its Stakeholders, promoting community development and well-being. |
| Guarantee the availability of a committed and qualified workforce. | Ensure sustainable use of natural resources and contribute to combating climate change. | Promote relations of trust with Stakeholders, improving the quality of life of people in areas where the Group has a presence. |
| <ul style="list-style-type: none"> • Global human resources management. • Goal of "accident reduction". • Talent management. • Diversity, equal opportunity, and reconciliation. | <ul style="list-style-type: none"> • Environmental management. • Preservation of biodiversity. • Prevention of pollution. • Operating excellence and energy efficiency. • Waste management. | <ul style="list-style-type: none"> • Stakeholder relations. • Community support and electricity access programmes. • Foundations of the Iberdrola Group. • Corporate reputation. • Brand management. • Informational transparency. |

2.5 Value Chain

Power generation

Electricity production through the construction, operation, and maintenance of generating plants, and purchase/sale of energy on wholesale markets.

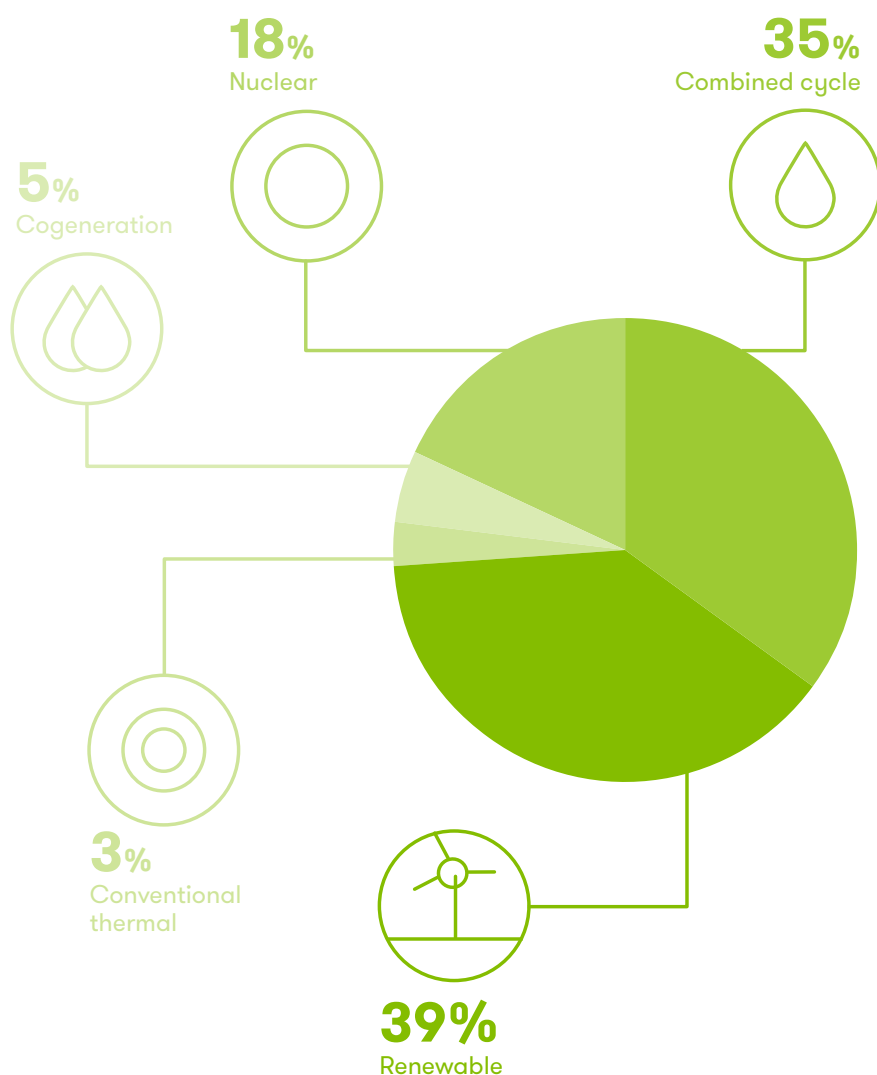


Power transmission and distribution

Construction, operation, and maintenance of electrical lines, substations, transformer centres, and other infrastructure, to transfer electrical power from production centres to the end user.

Generating plants*

* % of 2016 net output



Electric grids*

* At 31 December 2016

Overhead lines



4,000

High and medium voltage transformer substations

30,491 km
of transmission lines

875,140 km
of distribution lines



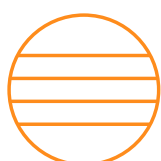
Retail sale of energy

Supply to end users of energy and additional products and services.

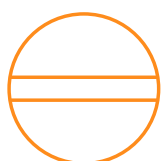
Underground lines



1.4 million
Medium to low
voltage distribution
transformers



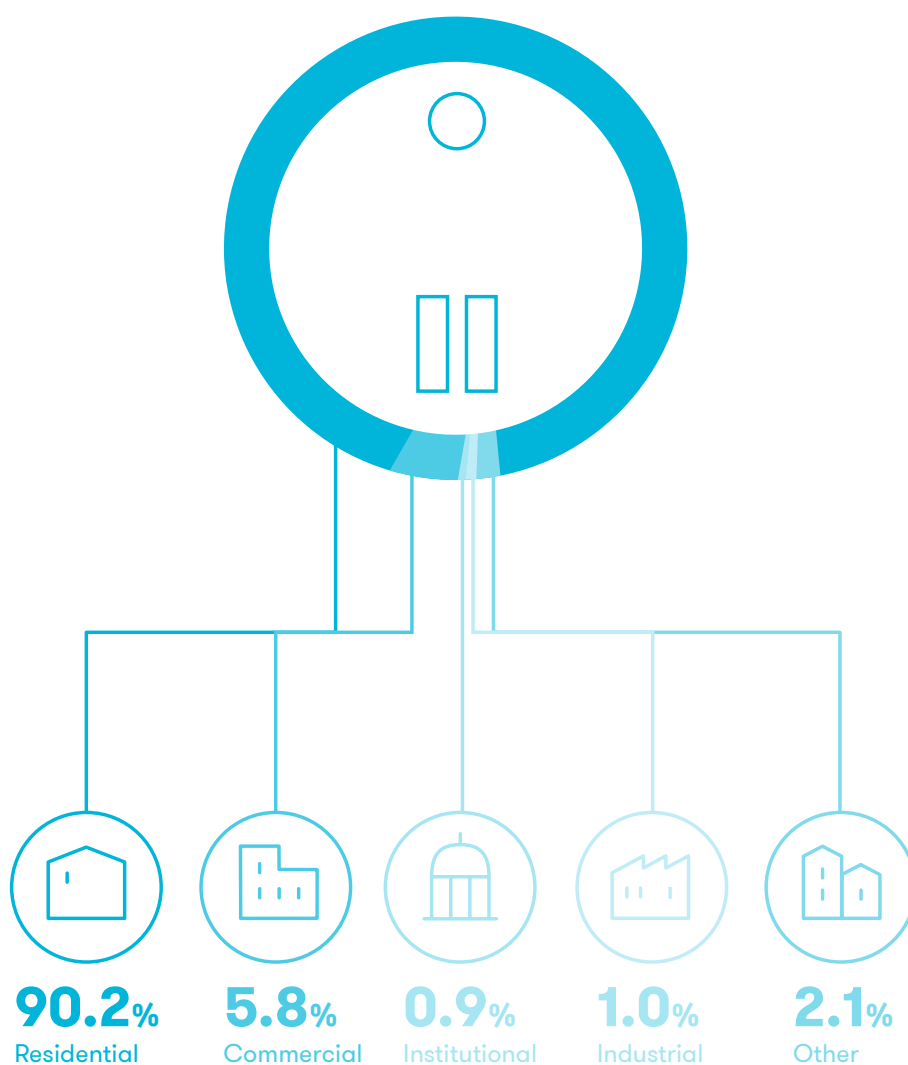
986 km
of transmission lines



193.285 km
of distribution lines

Users*

* % by sector at 31 December 2016



2.6 Strategic Foundations

for 2016-2020

Market conditions

The global energy markets are showing a certain amount of volatility, which is a reflection of geopolitical factors affecting the oil- and gas-producing countries. Our update of the scenario for the 2016-2020 period compared to prior forecasts is maintenance of prices in Spain and an increase in electricity prices in the United Kingdom, explained by an increase in the price of gas. We expect a relatively flat scenario over the full period. The diversification of businesses and countries will allow the Company to develop a strategy of growth and value creation that conforms to this environment.

Challenges and opportunities

Challenges

- Decarbonisation in the energy sector. Demand for cleaner and more sustainable energy.
- Management of a scenario of constant prices for energy in the medium term.
- Attainment of higher efficiency levels in all businesses.
- Regulatory management in all businesses, with special emphasis on transmission and distribution businesses, and in the development of the single market in Europe.
- Implementation of an investment plan focused on growth in the businesses of regulated networks, renewables, and long-term contracted generation.

Opportunities

- Balanced business model focused on regulated activities and renewable generation.
- Significant experience in the development and construction of network and emission-free generation projects.
- International diversification with a presence in countries with stable and predictable regulatory frameworks that require investment in the electricity and gas sectors.
- High quality of assets.
- Proven management capacity, culture of efficiency, and results.
- Culture of innovation to implement digitisation in relation to customers and the development of new products and services.

Growth vectors 2016-2020

Investments

- United States: the Company, through Avangrid, will continue with new onshore wind developments, taking advantage of the extension of tax credits to 2020. It is also facing growth in the area of distribution networks as well as in transmission.
- Mexico: it will consolidate its position as the largest private power generator in Mexico, through new plants under long-term contract with the Federal Electricity Commission (*Comisión Federal de Electricidad*) (CFE), and also taking advantage of the opportunities arising from the liberalisation of the sector.
- United Kingdom: Iberdrola continues with its growth phase in the power transmission and distribution businesses and with the start-up of onshore and offshore renewable energy projects. Offshore wind will gain significance beginning in 2018.
- Brazil: strengthened growth in renewables, maintaining its position as largest electricity distributor by number of customers.
- Spain: maintenance and improvement of facilities. Growth in smart grids.

Operational efficiency

- In all areas of activity, with a plan to save €1,300 million over the period.

.... expanding the geographic diversification of the Company in countries with an A rating, and increasing its presence in regulated businesses with low risk and the generation of recurring cash flows.

Strategic pillars

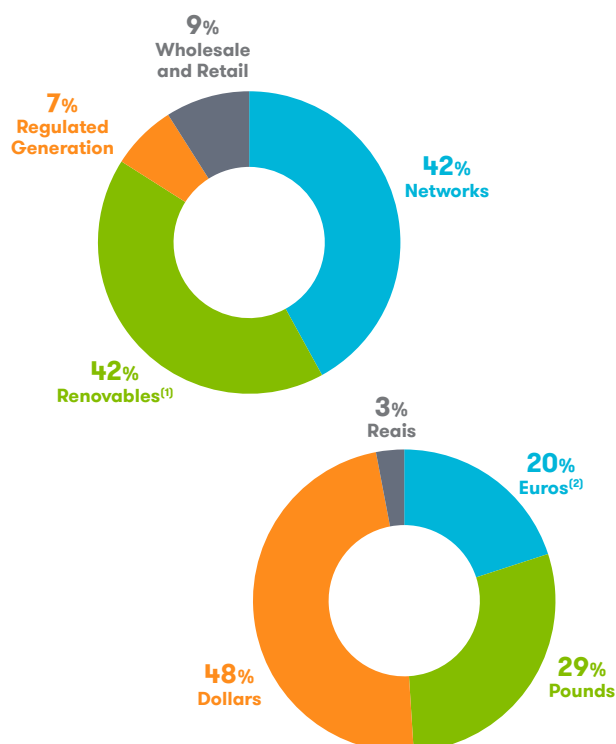
Iberdrola's strategy for 2016-2020 will remain focused on balanced growth, ensuring its financial strength and the sustainability of its dividend policy, the growth of which will be linked to growth in results.

New investments will be concentrated in countries with high credit ratings (A rating), and in businesses that are preferably regulated or under long-term contract, thus improving the profile of the Company.

1. Balanced growth

- Investments focused on businesses and countries with stable and predictable regulatory frameworks, 71% in countries with a credit rating of A.
- Net investment increases €1,000 million over the plan presented in 2016, to €25,000 million, due to higher growth in renewable generation in the United States.
- Of total investments during the period, 75% are focused on growth and the rest on maintenance.
- Electric power transmission and distribution networks will account for 42% of net investments. Of the overall amount, 42% will be dedicated to renewable energy and 7% to regulated wholesale generation. 9% of the total will be invested in the Wholesale and Retail business.
- The regulated businesses (networks, renewables, and regulated generation) will account for 90% of all planned investments.
- Geographically, Iberdrola will concentrate the bulk of its growth in the international area. By currency, 48% will be invested in dollars, 29% in pounds Sterling, 20%⁽²⁾ in the Euro zone, and 3% in Brazilian reais.

Investment by business and currency 2016-2020



(1) Includes hydroelectric

(2) Includes offshore windfarm in Germany: Wikinger

2. Financial strength

The Company obtained solid results in financial year 2016, thanks to the good performance of the businesses and a reduction in costs. Ebitda reached €7,808 million, increasing 5.5%, although it would have grown 8.2% excluding the exchange rate effect (depreciation of the pound). Net profit grew 11.7% to €2,705 million. The efficient operation of operating assets, together with the above-described investment plan, will lead to sustainable growth in the Company's results, with an estimated average annual increase of approximately 7.5% over the 2016-2020 period.

The profile of the Company's businesses, together with a balanced investment plan, will allow for sustained growth in Ebitda and Net profit of approximately 6% and 7.5%, respectively...

- Average annual funds from operations (FFO) in the amount of €7,100 million will amply exceed investments, which will reach an annual average of €5,100 million. By business, cash flow generation from Wholesale and Retail and from Networks will be significantly greater than investments, while Renewables will invest a number somewhat higher than its cash flow generation.
- Maintenance of the current financial model to provide subsidiaries with an optimal

capital structure giving appropriate financial signals and which is consistent with an investment grade rating, while respecting current guidelines for structural subordination.

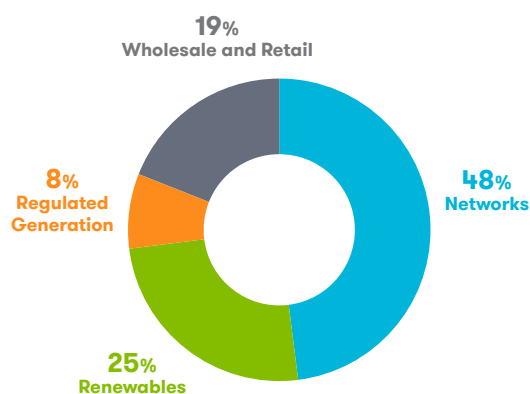
- Optimisation of liquidity position (around €8,000 - 9,000 million) to current market conditions in order to improve financial costs, maintaining 18 months of coverage even during stress scenarios.
- Maintenance of the strong 2016 solvency ratios through 2018, after which they will substantially improve, thanks to increase in Ebitda and FFO.

...resulting in the Company proposing a sustainable shareholder remuneration policy linked to the growth in results.

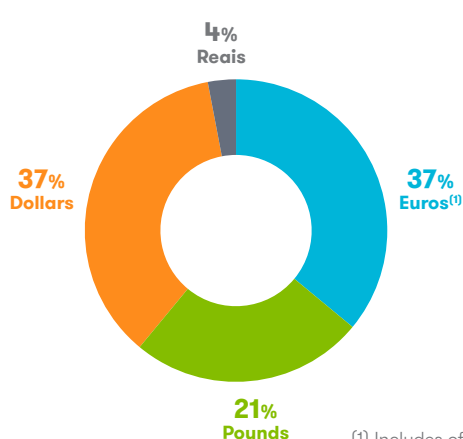
3. Sustainable dividend

- Thanks to the strength of the results obtained, the Company has announced a proposal to immediately increase the annual dividend to 0.31 euro per share with a charge to financial year 2016. This amount is also set as the minimum dividend for future years.
- In the coming years, shareholder remuneration will grow in line with the increase in results, converging towards a payout ratio between 65% and 75%. Taking into account this range and the forecast growth in net profit, the dividend would be between 0.37 and 0.40 euro per share by 2020.

Ebitda by business (forecast to 2020)



Ebitda by currency (forecast to 2020)



(1) Includes offshore windfarm in Germany: Wikinger

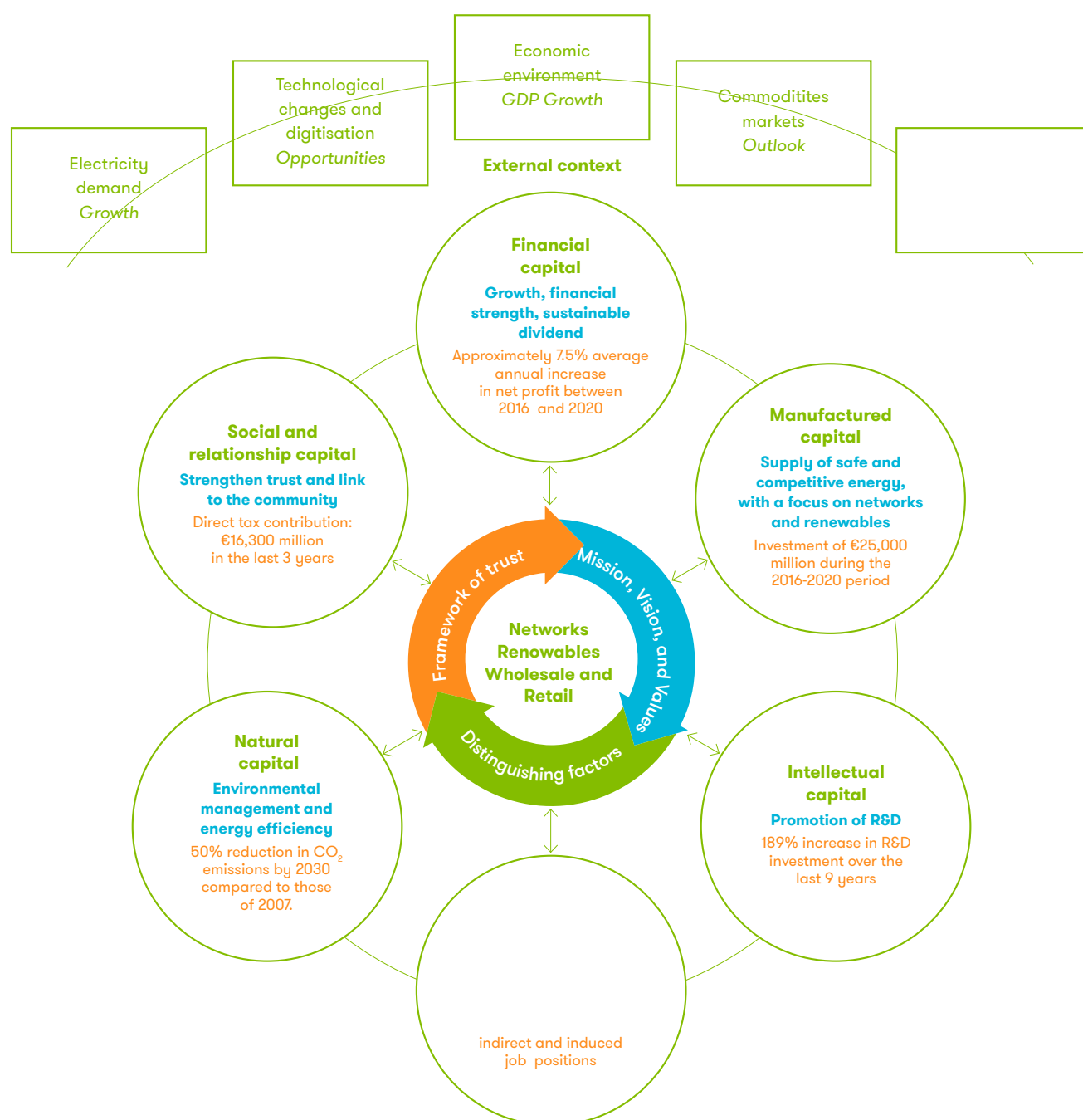
2.7. Capital/Business

Relationship

The value created by the business strategy and model of Iberdrola over time translates into an increase in its capital, which in turn feeds back into a cycle of value creation, efficiently inter-relating the operations of the businesses and the capital of the Company. The chart below shows for each Chapter its strategic focus and quantifies an aspiration

or achievement of the Company in this area.

This process creates shared value for both Iberdrola and for its Stakeholders, and constitutes a main vector for achieving the Company's goal to offer a reliable, high-quality, and environmentally-friendly energy supply.



2.8 Comparative Results

and Awards

Comparative analysis*

Comparative economic/financial variables 2016

Growth in Ebitda

| ACGR (%) | Average comparables | Iberdrola |
|-------------------------|---------------------|-----------|
| 31-Dec.-06 / 31-Dec.-16 | 1.3%** | 7.2% |

Growth in capitalisation

| Total growth (%) | Average comparables | Iberdrola |
|-------------------------|---------------------|-----------|
| 31-Dec.-06 / 31-Dec.-16 | -54.2% | 32.8% |

Iberdrola held 5th place among comparable companies in terms of stock market capitalisation for the last 10 years. It is now in second place.

Share price

| Total growth (%) | Average comparables | Eurostoxx Utilities | Iberdrola |
|-------------------------|---------------------|---------------------|-----------|
| 31-Dec.-06 / 31-Dec.-16 | -70.1% | -52.4% | -24.7% |

* Comparable companies analysed: Engie, EDF, E.On, Enel, RWE. ACGR: Annual Compound Growth Rate, i.e. weighted average annual growth.

** For Engie, Enel, E.ON, and RWE, the 2016 Ebitda figures are the estimates published by Bloomberg, due to the lack of final closing figures on the date of preparation of this document. In addition, for Engie, the 2006 figure is for GDF (prior to the merger of GDF and Suez SA).

Comparative performance of total shareholder return

| Profitability (%) | Average comparables | Eurostoxx Utilities | Iberdrola |
|-------------------------|---------------------|---------------------|-----------|
| 31-Dec.-06 / 31-Dec.-16 | -37.0% | -16.6% | 11.3% |

Iberdrola's performance

Over the last 10 years, Iberdrola has more than tripled its assets, tripled its revenues, doubled its Ebitda and increased its net profit by 60% and shareholder remuneration by 30%, while maintaining its financial strength.

| Iberdrola | 31-Dec.-06 | 31-Dec.-16 | Multiple |
|------------------------------------|------------|------------|----------|
| Assets (€M) | 33,061 | 106,706 | 3.2x |
| Revenues (€M) | 11,017 | 29,215 | 2.7x |
| Ebitda (€M) | 3,890 | 7,808 | 2.0x |
| Net Profit (€M) | 1,660 | 2,705 | 1.6x |
| Dividends ⁽¹⁾ (€/share) | 0.22 | 0.28 | 1.3x |
| Net Debt/Ebitda | 3.7 | 3.8 | 1.0x |

(1) Not including the bonus for attending the General Shareholders' Meeting.



Ignacio Galán at the offices
of the Iberdrola Tower
/ Bilbao

External awards

For the Company:

- Best Corporate Governance in Spain (World Finance): 2015, 2014, and 2012.
- Best Corporate Governance among European Utilities (Ethical Boardroom): 2016, 2015, and 2014.
- World's Most Ethical Company Index (Ethisphere Institute): 2016, 2015, and 2014.
- Leading Ibex 35 company in the tax transparency ranking 2015, from *Fundación Compromiso y Transparencia*.

© Other Awards
/ page 91

For the chairman & CEO:

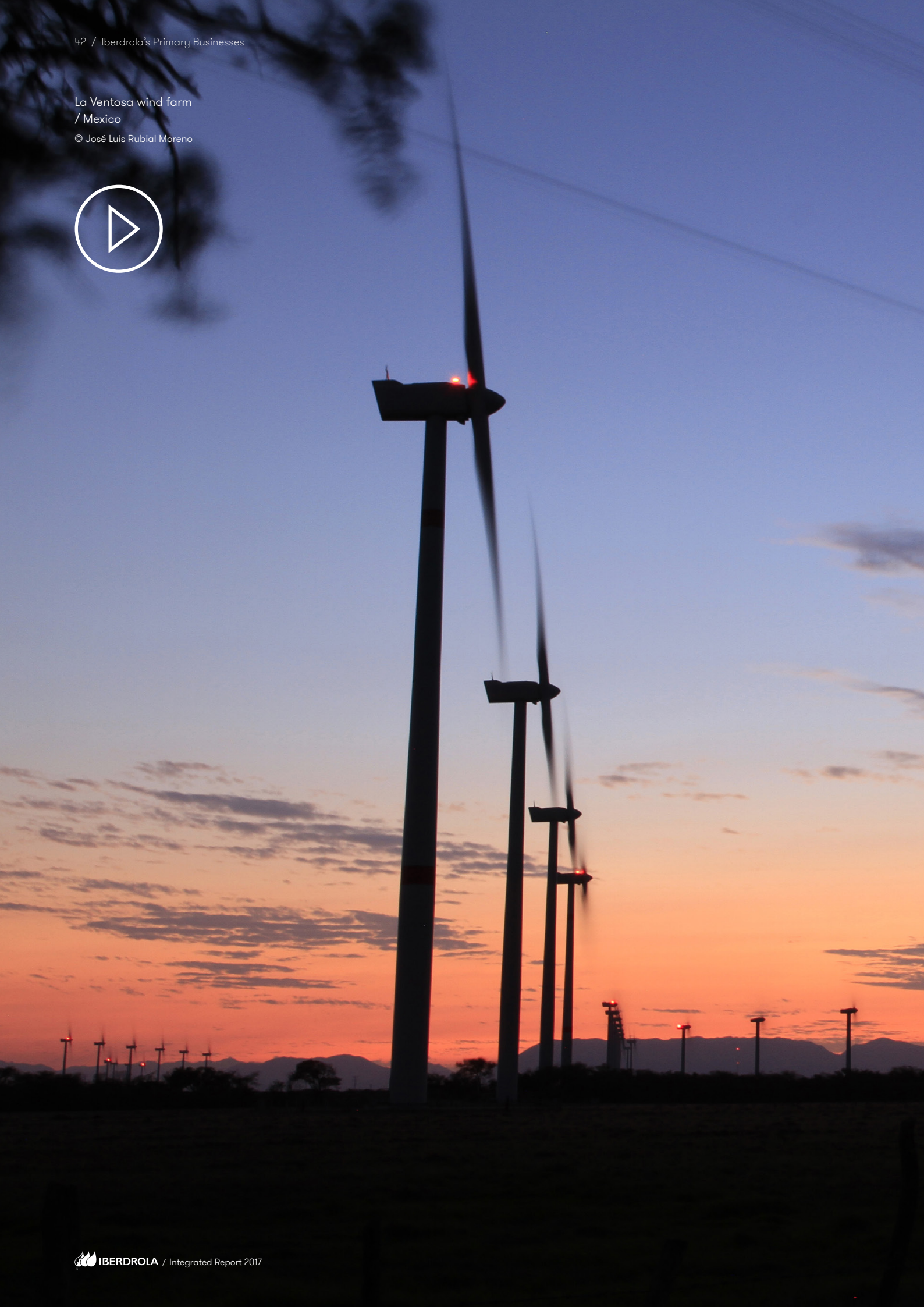
- Best European Utility CEO (Institutional Investor Research): 2016, 2015, 2014, 2013, and 2011.
- Commander of the Most Excellent Order of the British Empire: 2014.
- Honorary Doctorate from the Universities of Salamanca (2011), Strathclyde (2013), and Edinburgh (2011).

For other members of the Company:

- Best European Utility CFO (Institutional Investor Research): 2016, 2015, 2014, and 2012.
- Best European Utility Investor Relations (Institutional Investor Research): 2016, 2015, 2014, 2013, 2012, and 2011.

La Ventosa wind farm
/ Mexico

© José Luis Rubial Moreno





Iberdrola's Primary Businesses

Regulation is a key factor in the sustainability of Iberdrola's activities.

Energy policies must set clear and predictable goals in order to attract the investment needed to guarantee a safe, competitive, and sustainable supply, developing to the maximum its potential as a source of growth and employment.

3.1 Regulatory Environment

European Union

- The Climate Change Conference (COP21) agreements reached during the Paris Summit in 2015 were ratified in 2016, before the commencement of the Marrakesh Summit. These agreements entail a multilateral commitment to implement measures to reduce emissions in order to limit the increase in temperature to a maximum of 2°C. These measures will foster investment and must be supported by signals incentivising low-carbon technologies. In addition, these costs must be paid in accordance with the “polluting party pays” principle.
 - In November 2016, the European Commission (EC) published the “Clean Energy for All Europeans” package (also known as the “Winter Package”), the legislative proposals of which, in the words of the EC, have three main goals: putting energy efficiency first, achieving global leadership in renewable energy, and providing a fair deal for consumers. Among the more far-reaching measures included in the proposed Directives and Regulations are those concerning the market design reform and the safety of supply framework. Proposals have also been submitted to modify the frameworks for renewables and for energy efficiency, in line with the 2030 goals.
 - During 2017, there will be continued steps in connection with the Emissions Market Directive, and preparation of the regulations and directives contained in the “Winter Package” will begin.
-

Spain

- After the strong tariff deficit during the 2005-2013 period and a slight surplus in 2014 and 2015, the system has reached financial balance. A Ministry Order freezing electricity and gas usage charges for 2017 was published in December 2016.
 - The Supreme Court has rendered judgements holding that the funding system for the subsidised rate (*bono social*) is invalid on the grounds that it is discriminatory. The companies funding these amounts (up to now, the parent companies of vertically integrated groups) must be reimbursed for the amounts contributed between 2014 and 2016, with interest.
-

United Kingdom

- On 23 June 2016, the United Kingdom voted to leave the European Union. Future trade agreements have not yet been determined, but significant changes are expected in the energy regulatory environment in the short term.
 - After the referendum, David Cameron resigned and Theresa May was elected Prime Minister; her government stated that the protection of consumer interests is a priority and reiterated its commitment to decarbonising the economy.
 - The Competition and Markets Authority (CMA) completed its investigation into the industry in June, and the proposed orders were implemented at the end of 2016. The CMA largely disregarded the concerns about the wholesale market and vertical integration, but recommended Ofgem or the Government adopt remedies in the retail market, such as a temporary limit on prepayment tariffs, a data base to help disconnected customers, and reforms in the SME market.
-

United States and Canada

- On 8 November 2016 Donald Trump won the elections and Republicans gained control of Congress and the Senate. The states will continue establishing a large part of the regulations affecting Avangrid.
- In 2016 litigation continued forward to determine whether the Environmental Protection Agency (EPA) can implement the *Clean Power Plan* (CPP). Trump has vowed to revoke it. There are various possible scenarios depending on the decision of the U.S. Court of Appeals for the D.C. Circuit regarding the CPP.
- It is expected that PTCs (Production Tax Credits) will be maintained during the Trump administration, as they have the support of Congress. Current laws already provide for their gradual phase-out, and a change therein would have an impact on regulatory security.
- The methodology to replace net metering in the State of New York is now being debated. An order of the Commission is expected in January 2017.

Mexico

- The energy reform encourages private investment in the generation, sale, and supply of electric power. The networks continue to be under state ownership but are open to contracts with private persons. In this context, the first auction of transmission lines is expected to take place in the first half of 2017. The share of clean energy is forecast to increase up to 35% by 2024 with the creation of a clean energy certification system that will determine certain supply obligations.
- The Real-Time and Day-Ahead Markets began to operate in 2016. Two Long-term Auctions were also held, which will add almost 5 GW of new clean generation capacity.

Brazil

- The regulator has launched a Strategic Plan for the improvement of the Brazilian energy industry in order to carry out a revision of the sector, make improvements, and mitigate the risks facing the players involved. This project will continue until the first quarter of 2018.
- Due to the decrease in demand and the migration of customers to the free market, distributors have found themselves to have contracted for an oversupply of energy. The regulatory agency and the ministry have approved various regulations to minimise the effects of the 2016 oversupply.
- A two-part tariff was approved in 2016 with a view to modernising the tariff system.
- The Government has announced a plan to privatise six state-owned distribution companies belonging to Eletrobras; the plan should be completed before the end of 2017. The wave of privatisations began in 2016 with the auction sale of the distributor CELG.
- 2016 saw a modification in the model defining the maximum contract income by public auction for concessions of transmission lines. The main change was the method for calculation of the WACC,⁽¹⁾ which has been set at 9.67%. This measure increases the profitability of transmission concessions and makes auctions more appealing.

(1) WACC: Weighted Average Cost of Capital.

Work on distribution line
/ Spain
© Iberdrola, S.A.



3.2 Networks

Regulatory environment of the business

Spain

- After the approval of unit costs in December 2015, 2016 was the first year of the first regulatory period, which will end in December 2019.
- The remuneration of Iberdrola Distribución Eléctrica for 2016 was set at €1,664 million. This remuneration will increase each year based on the investments made.

United States

- The new tariff conditions for the NYSEG and RG&E (New York) gas and electricity businesses came into effect in July 2016. They will be in force for three years.
- A new three-year tariff agreement will come into effect for the electricity distribution company UI (Connecticut) in January 2017.
- In Maine, a 10-year tariff agreement for the gas distributor MNG came into effect, and the agreement for the electricity distributor CMP was extended for an additional year.
- The tariff conditions for the gas distributors CNG and SCG (Connecticut) and BCG (Massachusetts) will remain the same in 2017.

United Kingdom

- Ofgem has revised the investment scenario contemplated for the mid-period RIIO-T1, with no impact on the transmission projects of ScottishPower Transmission Ltd. (SPT) agreed in 2013 and which will end in 2021.
- Distributors ScottishPower Distribution Ltd. (SPD) and ScottishPower Manweb plc (SPM) carry out their activities during the first regulatory period RIIO-ED1, which will extend through March 2023.

Brazil

- The new tariff agreement for Celpe will come into force in April 2017 and will be in effect for five years.
- The tariff agreements for Coelba and Cosern will remain in effect until April 2018, and that for Elektro until 2019.
- The remuneration for the distribution activities of Elektro, Coelba, Cosern, and Celpe has been adjusted based on inflation in Brazil.

New tariff conditions for UI enter into effect in the State of Connecticut (USA) in 2017.

Objectives, risks, and principal activities

Objectives

- Zero accidents.
- Offer our customers excellent service based on the quality of supply and information regarding the network.
- Maximise efficiency in system operations through operational excellence and the digitisation of our assets.
- Lead the transformation towards more efficient integration of renewable and distributed energy.

Significant risks

- Safety of individuals due to risk of accidents.
- Assuring supply in the face of meteorological effects.
- Technological and cybersecurity risks affecting the security of the facilities and service to our customers.

Principal activities 2016

- Spain: continuation of the network digitisation and automation project, with

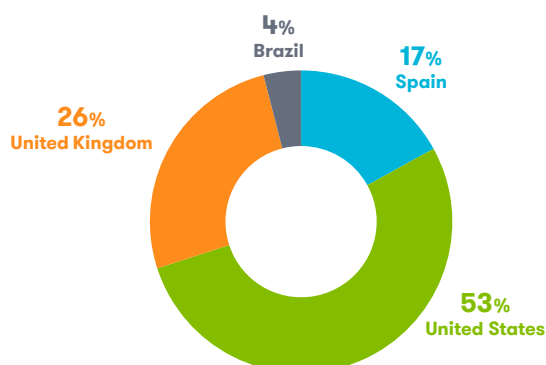
the installation of more than 8.8 million meters (83.5%) and digitisation of 55,500 transformer centres (66%).

- United Kingdom: developing the investment plans contained in RIIO-T1 and RIIO-ED1. Continuation of the Western Link HVDC project, which is expected to be completed in 2017.
- United States: developing the plan for integrating UIL's distributors within Avangrid. All regulatory quality levels have been met. Submission of filing with the regulator to launch smart meters, and creation of a platform for the integration of distributed generation within New York. Launch of Energy Smart Community project in Ithaca.
- Brazil: strengthening the position of Coelba and Celpe in Brazil's quality ranking thanks to Neoenergia's efficiency and supply quality improvement plan. At Elektro, development of facilities to meet demand and connect new customers.

Outlook 2016-2020

- Increased regulatory visibility in all countries, with investments of €10,300 million. 15% increase in RAV* since 2015, which would increase to 22% taking into account 100% of Neoenergia.
- Increase in efficiency: improvement in NOE/MB* by 2 percentage points, with a 41% in Ebitda/Employee.
- Growth in digitisation of the network (€2,600 million in investments during the 2017-2020 period), to increase efficiency and the quality of supply, and to offer new services to customers.
- Opportunities for selective growth in transmission.

Net Investment of €10,300 million between 2016 and 2020, mainly in the United States and the United Kingdom



2016-2020 cash flow generation to finance investments (€ thousands of millions)



* RAV: Regulatory Asset Value; NOE: Net Operating Expenditure; GM: Gross Margin.

Key figures of the Networks Business

| Item | Unit | Spain | | United Kingdom | | United States ⁽¹⁾ | | Brazil | | | | Total | |
|----------------------------|---------------|--------|--------|----------------|--------|------------------------------|--------|---------|--------|---------------------------|--------|---------|---------|
| | | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | Elektro | | Neoenergia ⁽²⁾ | | 2015 | 2016 |
| | | | | | | | | 2015 | 2016 | 2015 | 2016 | | |
| Gross margin | €M | 1,952 | 2,029 | 1,472 | 1,267 | 1,698 | 2,537 | 390 | 328 | | | 5,512 | 6,160 |
| Ebitda | €M | 1,457 | 1,603 | 1,138 | 976 | 781 | 1,270 | 253 | 233 | | | 3,628 | 4,082 |
| Electric power distributed | GWh | 92,685 | 92,308 | 36,253 | 35,704 | 33,697 | 39,079 | 17,448 | 17,425 | 44,673 | 45,301 | 224,749 | 229,816 |
| Users (Electricity) | Millions | 10.9 | 11.0 | 3.5 | 3.5 | 2.2 | 2.5 | 2.5 | 2.6 | 10.6 | 10.8 | 29.7 | 30.4 |
| Gas supply | GWh | | | | | 36,196 | 59,544 | | | | | 36,196 | 59,544 |
| Users (gas) | Millions | | | | | 1.0 | 1.0 | | | | | 1.0 | 1.0 |
| Investments | €M | 346 | 389 | 847 | 628 | 429 | 752 | 71 | 76 | | | 1,693 | 1,845 |
| Workforce | No. of people | 3,981 | 3,887 | 2,934 | 2,819 | 5,795 | 5,734 | 3,713 | 3,708 | 5,101 | 5,403 | 21,524 | 21,548 |

International Financial Reporting Standard (IFRS) 11 has been applied to the financial information.

1 UIL included in users and workforce in 2015. Not included in energy supplied.

2 Operational information is deemed to be 100% from Neoenergia.

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Customer service, operational efficiency, and digitisation of networks are the strategic pillars of the Networks Business upon which the business rests.

Customer service

- Investment in expansion, renewal of network, and investments in operation and maintenance to improve service quality for our customers.
- Met service quality targets, despite poor meteorological conditions during the last quarter of 2016.
- Implementation of transmission and distribution projects to improve service quality for customers.
- Development of digital customer service channels: improvements in website, apps, social media, etc.

Efficiency

- Increase in operating expenses contained despite strong increase in activity.
- Implementation of best practices throughout the networks companies, mainly in the areas of asset management, processes and technology, control systems, digitisation and automation, and customer service.
- Emphasis on the fight against electricity fraud in Brazil and Spain.
- Containment of increase in late payments in Brazil due to the country's economic crisis.

Digitisation of the network

- Projects to increase the automation of the MV network.
- Expand visibility of the LV network in Spain.
- Deployment of smart meters in Spain and the United States.
- Focus on maximising operational efficiency and improving service quality and providing useful information to customers.
- Improve customer service using new technologies.
- Strengthened measures to protect against cybersecurity risks associated with new grid management technologies.

Dulces Nombres II Combined Cycle
gas plant / Mexico

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3.3 Wholesale and Retail

Regulatory environment of the business

Spain

- Royal Decree 469/2016 was approved in November 2016, establishing the methodology for calculation of voluntary prices for small consumers of electric power and the legal rules governing contracting therefor.
- Ministry Order ETU/1948/2016 was approved in December 2016, establishing specific values for the supply costs of leading supply companies to be included in the calculation of the voluntary price for small consumers during the 2014-2018 period. A fixed amount is set in €/kW and per year and a variable amount is set in €/kWh.
- Royal Decree-Law 7/2016 was published in December 2016, governing the mechanism for financing the cost of the subsidised rate (*bono social*) and establishing other measures for the protection of vulnerable consumers of electric power. This Decree-Law provides that the costs of the subsidised rate shall be borne by the parent companies of the groups engaged in the supply of electric power, or by the supplier companies themselves if they are not part of a group, and expands the protection of groups of vulnerable customers by extending the periods before interruption of supply in the event of non-payment and by including new categories of severely vulnerable customers, who will be considered essential supply customers.
- The availability service of the generation facilities has been extended in 2017.

United Kingdom

- The capacity auction 2020/2021 took place in December 2016, with the participation of both existing plants and new projects. A total of 52.4 GW was awarded at a price of £22.50/kW, of which 48.4 GW correspond to existing capacity (generation and interconnections) and 4 GW to new capacity, mainly diesel engines and batteries.
- Based on the plan for implementation of the measures recommended by the CMA⁽¹⁾ in June 2016, Ofgem⁽²⁾ has proposed limiting the charges for the installation of prepayment meters by court order and prohibiting the billing of more vulnerable customers for the installation. Such limit will be in effect as from April 2017.

Mexico

- There were two long-term auctions in 2016 awarding the proceeds from Power, Capacity and Clean Energy Certificates (*Certificados de Energías Limpias*) (CELs).
- In April 2016, Iberdrola was awarded the Noroeste 887 MW combined cycle plant located in the state of Sinaloa.
- As from August 2016, consumers with demand greater than 1 MW can acquire their energy on the market.

⁽¹⁾ CMA: Competition and Markets Authority

⁽²⁾ Ofgem: Government regulator for gas and electricity markets

Objectives, risks, and principal activities

Objectives

- Competitive supply and excellence in service to customers.
- Operating excellence, safety, and respect for the environment.
- Risk identification and minimisation.
- Safety and continuous improvement in operating efficiency.
- Analysis of growth opportunities.

Significant risks

- Regulatory uncertainty in the countries in which it operates.
- Operating risks: downtime of facilities and incidents with environmental impact.
- Market risk: uncertainty regarding fuel prices and revenues from the sale of electricity and gas.
- Credit, exchange-rate, and interest-rate risks.
- Technological and cybersecurity risks affecting the security of the facilities or the information of our customers.

Principal activities 2016

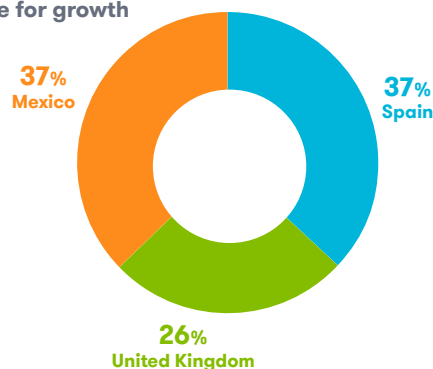
- Spain: ongoing development of products and services adapted to the needs of customers (Customised Plans, Smart Solar, Iberdrola Smart Home, ...).

- United Kingdom: final shut down of the Longannet Coal Plant took place in the month of April. The decrease in variable rates for domestic gas customers (-5.4%) became effective in March 2016. 180,000 smart meters were installed during 2016.
- Mexico: installation of 409 MW (5th unit of Monterrey CCGT (300 MW), Ramos Arizpe cogeneration (53 MW, and repowerings (56 MW)), in addition to 308 MW from the Baja California III CCGT, which entered into operation at the beginning of 2017. 2,761 MW of thermal capacity under construction.
- Brazil: work continues on the construction of the Baixo Iguazu and Belo Monte hydroelectric plants, of which 245 MW and 1,123 MW belong to Iberdrola through Neoenergia, a company in which Iberdrola holds a stake.
- Portugal: continued construction of the Tamega hydro complex, which will have 1,158 MW. As to Customers, there has been a strengthening of the offer to mass segments with the inclusion of gas and new products and services.

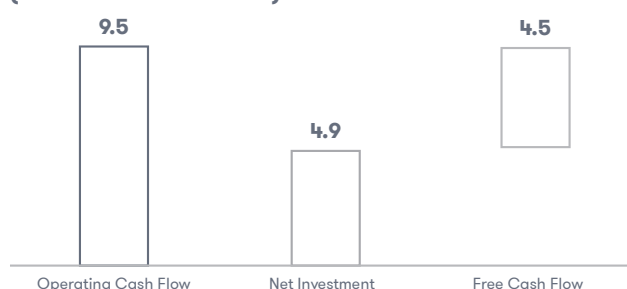
Outlook 2016-2020

- Investments of €4,900 million, mainly to increase installed capacity and to deploy 5.3 million smart meters in the United Kingdom.
- During the period, entry into service of 3,600 MW in Mexico, of which more than 700 MW have already entered into operation and almost 2,800 are under construction.
- In Retail, commitment to digitisation, multiple channels, personalisation of products adapted to the needs of our customers, and service excellence.
- Continuing improvement of operational processes and practices to increase efficiency.

Investment of €4,900 million during the period, of which €3,600 million are for growth



2016-2020 cash flow generation to finance investments (€ thousands of millions)



Key figures of the Wholesale and Retail Business

| Item | Unit | Spain | | United Kingdom | | United States and Canada | | Mexico | | Total | |
|-----------------------------------|------------|--------|--------|----------------|--------|--------------------------|------|--------|--------|--------|--------|
| | | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 |
| Gross margin | €M | 2,971 | 3,072 | 1,306 | 1,000 | -19 | 48 | 583 | 509 | 4,842 | 4,629 |
| Ebitda | €M | 1,505 | 1,521 | 421 | 294 | -58 | 6 | 455 | 436 | 2,323 | 2,253 |
| Installed capacity | MW | 20,081 | 20,058 | 4,835 | 2,531 | N/A | N/A | 4,976 | 5,437 | 29,892 | 28,026 |
| Net output (excluding renewables) | GWh | 43,616 | 50,790 | 14,925 | 10,650 | N/A | N/A | 38,128 | 36,449 | 96,669 | 97,889 |
| Electricity contracts | Millions | 10.3 | 10.3 | 3.3 | 3.2 | N/A | N/A | N/A | N/A | 13.6 | 13.5 |
| Gas contracts | Millions | 0.9 | 0.9 | 2.2 | 2.1 | N/A | N/A | N/A | N/A | 3.1 | 3.0 |
| Products and services contracts | Millions | 4.9 | 5.0 | 0.1 | 0.1 | N/A | N/A | N/A | N/A | 5.0 | 5.1 |
| Total retail contracts | Millions | 16.2 | 16.3 | 5.5 | 5.4 | N/A | N/A | N/A | N/A | 21.7 | 21.7 |
| Investments | €M | 188 | 215 | 94 | 134 | 5 | 6 | 353 | 353 | 640 | 708 |
| Workforce | No. people | 3,395 | 3,375 | 2,491 | 2,254 | 108 | 110 | 489 | 582 | 6,483 | 6,321 |

International Financial Reporting Standard (IFRS) 11 has been applied to the financial information.

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The Wholesale and Retail Business is focused on the safety of operations, the loyalty of customers, and growth in Mexico, which will allow for the stability of results and ensure the generation of funds for the Group.

Efficiency

- Optimisation of thermal production.
- Facilitating operations in complementary markets.
- Operating improvements and increase in availability and energetic yield of the thermal facilities in Mexico and Spain.

Prices

- Minimisation of risks through appropriate hedging of all generation, including renewable generation.

Growth

- Mexico: Almost 2,800 MW under development by 2020:
Escobedo I CCGT (857 MW).
Noroeste CCGT (887 MW).
El Carmen CCGT (866 MW).
Bajío Cogeneration (50 MW).
Altamira Cogeneration (57 MW).
Repowering improvements (44 MW).
- United Kingdom: Continued widespread deployment of smart meters that began in 2016, to reach 100% of customers by 2020.

Customers

- Loyalty-building and development of new products and personalised services adapted to the needs of customers.
- Retail development in Mexico pursuant to changes in legal provisions on energy reform.
- In Portugal, leadership in industrial customers, and strong growth in SMEs and residential customers.

Harestanes wind farm,
Scotland / UK

© Chris James



3.4 Renewables

Regulatory environment of the business

Spain

- A proposed Ministry Order was published in December, whereby the specific remuneration for renewables and cogeneration is revised as from 1 January 2017, following the established schedule. In the case of the wind power sector, this will entail increasing the return on investment (ROI) by €212 million, in order to offset the lower existing and expected market prices. It is expected that the final Ministry Order will be published in the first quarter of 2017.
- In 2016 the first auction of renewable capacity took place in Spain, at which 500 MW were awarded in wind-powered capacity and 200 MW in biomass. A new auction of 3,000 MW has been announced to take place in 2017, which will be technologically neutral and subject to controls in order to verify the credibility of the winning projects.

United Kingdom

- In November 2016, the new Government of Theresa May announced the second auction of Contracts for Differences, which is expected to begin in April 2017. Eligible for this auction, with an annual budget of £290 million, will be the less mature technologies: offshore wind, biomass, tidal, and wave, with start-up dates of 2021-22 and 2022-23. The starting price for offshore wind technology is £105/MWh.

The business will engage in sustainable growth, mainly based on onshore and offshore wind investments in the countries most important to the Group.

United States

- Donald Trump's victory in the presidential elections might entail a shift in the policies expected from the White House for the promotion of renewable energy. However, the main federal support comes in the form of tax credits (PTCs), which have already been approved for the coming years.
- The state support systems are stable and independent of the federal system, and it is expected that such stability will be preserved.

Mexico

- Two long-term auctions took place in 2016 for the sale of 20-year Clean Energy Certificates. The contracts deriving from such auctions included the sale of the energy and capacity associated with the projects awarded.
- According to the schedule, a new auction is slated to take place in April 2017.

Brazil

- The macroeconomic situation has entailed a certain change in planning.
- No wind or photovoltaic MW were awarded in 2016, as the December auction was cancelled due to overextension in the sector.
- It is expected that less volume than usual will be awarded in 2017.

Objectives, risks, and principal activities

Objectives

- Safety in operations.
- Efficiency in operations to maximise the profitability of the assets.
- Efficiency in construction costs, with a particular emphasis on offshore wind projects.
- Profitable growth in onshore and offshore wind investments in the countries that are strategic for the Group.

Significant risks

- Competitive auction processes in the markets in which it operates.
- Operational and technological risk.
- Risk of access to evacuation networks and limits on production due to technical restrictions of the networks.
- Open market energy prices.
- Cybersecurity risks with an impact on operations centres of the facilities.

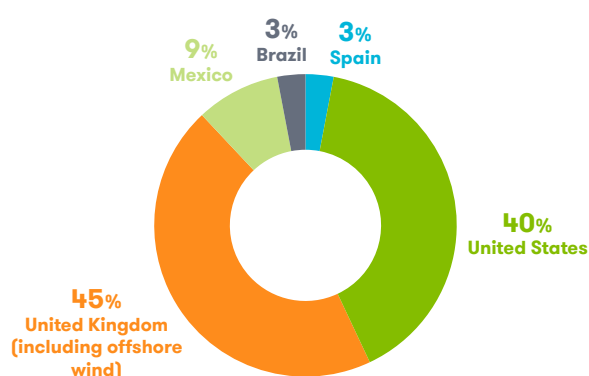
Principal activities 2016

- The year ended with 467 MW of additional capacity: 200 MW in the United States, 183 MW in the United Kingdom, and 84 MW in Brazil.
- There has been a start-up or continued construction of 1,487 MW of onshore wind capacity: 744 MW in the United States, 291 MW in the United Kingdom, 95 MW in Brazil, 32 MW in Spain, and 325 MW in Mexico.
- Construction of photovoltaic solar capacity has commenced in the United States (66 MW) and Mexico (270 MW).
- In offshore wind, there is continued progress on the construction of the 350 MW Wikingen project in the Baltic Sea (Germany). Construction has also commenced on the 714 MW East Anglia I project in the United Kingdom, after being awarded in the 2015 auction.

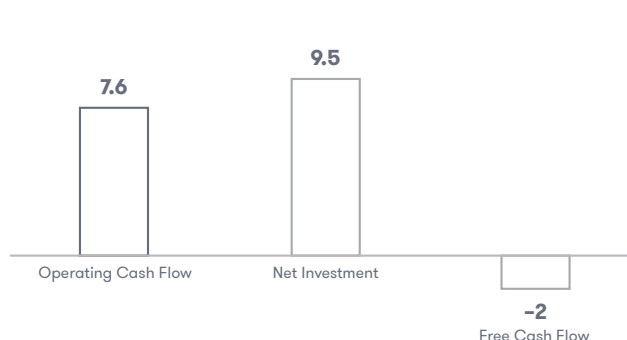
Outlook 2016-2020

- Investments of €9,500 million, mainly to increase installed capacity in the United States, the United Kingdom, and Brazil during the period.
- Start-up of 4,600 MW, of which 467 MW has already been placed into service in 2016 and more than 3,000 MW is already under construction, including two offshore windfarms: Wikingen (350 MW) and East Anglia I (714 MW).
- Continuing operational improvement, with cost savings, optimisation of useful life of the assets, and improvement in the capacity curve.

Investment plan of €9,500 million over the period, of which €8,800 million are for growth



2016-2020 cash flow generation to finance investments (€ thousands of millions)



Key figures of the Renewables Business

| Item | Unit | Spain | | United Kingdom | | United States | | Mexico | | Brazil | | Rest of World | | Total | |
|--------------------|------|--------|--------|----------------|-------|---------------|--------|--------|-------|--------|------|---------------|-------|--------|---------|
| | | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 |
| Gross margin | €M | 751 | 764 | 572 | 385 | 822 | 802 | 57 | 69 | 36 | 37 | 123 | 123 | 2,361 | 2,180 |
| Ebitda | €M | 473 | 497 | 438 | 267 | 571 | 564 | 43 | 52 | 27 | 25 | 95 | 95 | 1,647 | 1,500 |
| Installed capacity | MW | 5,861 | 5,859 | 1,615 | 1,991 | 5,534 | 5,742 | 367 | 367 | 187 | 187 | 621 | 621 | 14,186 | 14,768 |
| Output | GWh | 11,463 | 11,554 | 3,694 | 3,075 | 13,868 | 14,552 | 738 | 1,119 | 441 | 639 | 1,371 | 1,366 | 31,576 | 32,305 |
| Load factor | % | 22.3 | 22.4 | 26.2 | 21.0 | 28.8 | 29.9 | 31.5 | 34.7 | 39.1 | 38.8 | 25.2 | 25.0 | 25.7 | 25.8 |
| Investments | €M | 9.9 | 19.8 | 488.8 | 950.6 | 69.6 | 735.4 | 124.7 | 4.9 | 38.4 | 4.8 | 3.4 | -57.5 | 734.8 | 1,658.0 |

Notes:

- The figures for the United Kingdom include those of the offshore wind division.
- International Financial Reporting Standard (IFRS) 11 has been applied in the preparation of this table.

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The business will focus on the safety of operations and on sustainable growth, mainly based on onshore and offshore wind investments in the countries most important to the Group. Efficiency is a key factor for business sustainability in the medium and long terms. Iberdrola will take technological advances into account and will act on the supply chain to allow for improvement in the coming years.

Load factor

Maximising the load factor of facilities, while minimising down time through operating and maintenance measures, as well as other external factors.

Operation and maintenance costs

Continuous improvement in efficiency through global standardisation and systematisation processes.

Project Portfolio

Development of the portfolio of onshore wind projects in the United Kingdom, the United States, Mexico, and Brazil, and the East Anglia 3 (United Kingdom) and St Brieuc (France) offshore wind projects.

3.5 The Cost of Supply,

the Main Factor in the Political and Social Agenda

The cost of electricity supply is taking on a greater role in the political and social agenda. The principal challenge is to reconcile safe and environmentally-friendly supply with the use of renewable energy at prices that are competitive and can be afforded by society as a whole.

In the European Union

- The Agency for the Cooperation of Energy Regulators and the European Commission, in studies on electricity prices published in 2016, confirmed that taxes and components associated with energy and environmental policies have grown the most, reaching half of the bill in countries like Spain, due to the significant renewables effort made by the electric sector. A competitive electricity supply requires the elimination of cost components outside of the service itself, and paying for these costs through general taxes or taxes on all polluting energies.
- The strategy of the Energy Union that commenced in 2015 and that was specified in legislative proposals like the *Clean Energy for All Europeans* (2016) “package” responds to the need to comply with the 2030 environmental agenda (40% reduction in GHG⁽¹⁾ emissions, 27% increase in renewables, and 30% improvement in energy efficiency), monitoring the safety of supply and the competitiveness of the European industry, and allowing prices that are accessible for European citizens.

⁽¹⁾ GHGs: Greenhouse gases

In Spain

- The price of electricity supply in Spain is less than the European average. Less than half the costs of supply are directly related to providing the service. The rest derive from the pursuit of energy policy goals (aid for renewable energy and cogeneration) and social goals (subsidies for electricity in non- mainland territories, recovery of tariff deficits from previous years).
- Iberdrola has established a protocol to ensure energy supply for customers in vulnerable situations, defined as those entitled to subsidised rates (*bono social*) due to being pensioners or all members of a family unit being unemployed, as well as disadvantaged persons identified by the social services. Iberdrola has been collaborating with public authorities and with various institutions and NGOs for this purpose since 2015, signing agreements in order to identify these economically disadvantaged persons. 98.8% of the domestic customers of Iberdrola reside in an area protected by an agreement.

In the United Kingdom

- After the CMA⁽¹⁾ investigation, the debate on prices has focused on higher standard variable tariffs (SVTs): reducing the number of people with SVTs and the disadvantages thereof. Iberdrola has the lowest proportion of SVTs amongst the large suppliers.
- Although the government continues to focus on minimising the costs that it controls, it has maintained capacity auctions, the minimum price of CO₂, and has announced the next auction of Contracts for Difference.

In the United States

- Tariff revisions reflect pressure by regulators to limit returns on capital, while maintaining the investments required to improve the network infrastructure.
- The closure of coal plants and the new regulation developed by the Environmental Protection Agency (EPA) may increase pressure on gas and electricity prices. Shale production might limit this impact.
- Restrictions on transporting natural gas by pipeline in the Northeast could lead to volatility in electricity market prices during periods of extreme weather.
- The development of smart grids, the rapid replenishment of supplies in the face of extreme weather conditions, new EPA regulations, and the integration of new energy sources require major investments, which sometimes conflicts with the goal of reducing final tariffs.
- In 2017, President Trump and the Congress want to focus on comprehensive tax reform, including support for infrastructure and repealing environmental regulations. Trump promised to support oil, gas, and coal, questioned climate science, argued for withdrawing from the Paris Agreement, and opposed a carbon tax. This could affect electricity markets and prices.

⁽¹⁾ CMA: Competition and Markets Authority

In Mexico

- Energy reforms were launched in 2014, with one of the key goals being to improve competition and lower electricity prices for end users.
- With the opening of electrical energy generation to private investment, renewable generation objectives and other measures, such as auctions for the purchase of clean energy certificates, the reform is incentivising competition in order to diversify the energy mix and reduce the costs of generation.

In Brazil

- 2016 was marked by a position of energy overcontracting by the distributors, caused by the reduction in consumption deriving from the economic crisis, consumer migration to the free market without distributors being able to reduce the contracts, and assignment of contracts for a higher-than-necessary amount. The regulatory bodies and government have approved a set of measures to resolve this distributor risk.
- The hydrological situation improved in 2016 in comparison with the previous year, allowing a “green tariff band” structure from April to October, which entails the end customer not paying additional costs for the production of energy.

Iberdrola will support frameworks that expand market deregulation and transparency and that provide incentives for required investments and efficient operations, through tariff structures that give efficient signals to consumers and do not penalise them with costs unrelated to the supply of electricity.

Worker at the Marquesado
wind farm, Granada
/ Spain
© Iberdrola





Our Assets

Iberdrola's assets are the basis for the creation of value by the Company, which carries out its activities through the sound management thereof.

In this report, Iberdrola's assets are identified in accordance with the IIRC classification system:

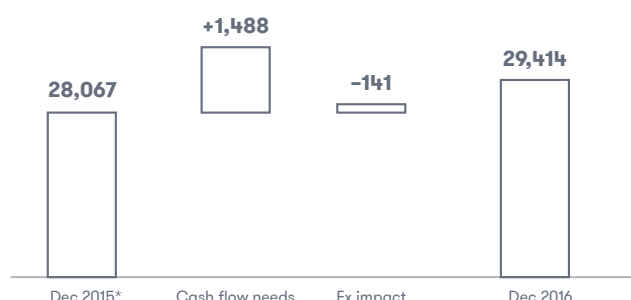
- **Financial capital**
- **Manufactured capital**
- **Intellectual capital**
- **Human capital**
- **Natural capital**
- **Social and relationship capital**

4.1 Financial Capital

| | Management approach | Results 2016 | Outlook |
|--|---|--|---|
| Balanced growth | <p>The Company has an investment policy consistent with its strategic vision and financial policy. The main goals are:</p> <ul style="list-style-type: none"> • Ensure a return on capital through projects and investments preferably in regulated businesses, renewable assets, or long-term contracts. • Increase geographic diversification, further balancing the contribution of the countries in which it does business. • Tailor investment levels to the actual needs of each market. | <ul style="list-style-type: none"> • Total investment of €4,264 million, with almost 90% channelled into regulated businesses. • The United Kingdom was the country absorbing the highest volume of investments, with 46% of the total, followed by Spain with 20%, the United States with 16%, and Mexico with 15% of the amount invested. | <ul style="list-style-type: none"> • Strict investment criteria based on earnings security, project profitability, and strategic fit. • Selection of businesses and countries with predictable and stable regulation and which have an A credit rating. • Net investment of more than €25,000 million over the 2016-2020 period, of which approximately 90% will be dedicated to regulated businesses, renewables, or long-term contracts. • The United States will be the area with the highest volume of investments, with 38% of the total, followed by the United Kingdom with 34%, Spain with 15%, Mexico with 10%, and Brazil with 3%. |
| Solid financial structure | <ul style="list-style-type: none"> • Iberdrola considers financial strength to be one of the strategic cornerstones that allows it to successfully face potential turbulence in the markets and to be in a position to exploit growth opportunities in the countries in which it does business. • The financial policy seeks stabilisation and subsequent improvement in solvency ratios, balancing an increase in debt with the generation of additional cash flow from new investments. • The debt structure is in line with the profile of the business, which is mostly regulated, and the composition thereof reflects the results obtained in the relevant currencies. | <ul style="list-style-type: none"> • Gross margin of €12,916 million, growing by 0.6%. • Net profit of €2,705 million, an 11.7% increase over the prior year. Recurring net profit was €2,532 million (+12%), as a result of the favourable performance of the businesses. • Cash flow of €6,311 million (+6.8%). • Net financial debt was €29,414 million, increasing €1,347 million since 2015 as a result of early investments in renewable energy, mainly offshore wind, and various extraordinary events (taxes in Spain, Safe Harbor in United States...) • Liquidity of €8,666 million, which covers more than 24 months of financing needs. | <ul style="list-style-type: none"> • Average annual Ebitda and net profit growth of approximately 6% and 7.5%, respectively, during the 2016-2020 period. • Average annual net investments of approximately €5,100 million, compared to average annual cash flow generation (FFO) of €7,100 million. • As a result of the investment process, increase in net debt to approximately €32,500 million in 2019 and subsequent decrease to €32,200 million by 2020. • With the current investment plan, solvency ratios in 2017 and 2018 are in line with 2016, and will strengthen in 2019 and 2020. • Optimisation of the liquidity position to cover financing needs for 18 months. |
| Operational efficiency | <ul style="list-style-type: none"> • The current macroeconomic and regulatory environment requires an additional effort to keep operating costs under control. | <ul style="list-style-type: none"> • Net operating expenses decrease 4.5% due to cost controls and the closing of the Longannet plant. Excluding the contribution from UIL and the exchange rate effect, the decrease in NOE would have been 6.9%. | <ul style="list-style-type: none"> • Progressive absorption of the increase in expenses, which will grow less than gross margin during the 2016-2020 period, maintaining an industry-leading position of leadership in cost efficiency. |
| Sustainable results and dividends | <ul style="list-style-type: none"> • Iberdrola offers its shareholders an industrial enterprise for the long-term creation of value. The confidence of its shareholders enables Iberdrola to secure the resources needed to move its enterprise forward. | <ul style="list-style-type: none"> • Shareholder remuneration of 0.286 euro per share, equal to a dividend yield of 4.59%. • Flexible dividend offering tax benefits. | <ul style="list-style-type: none"> • Increase of dividend to 0.31 euro per share, with a charge to 2016 profits. This amount is established as the minimum figure for future financial years. • Maintenance of the flexible dividend programme. • Target of maintaining the number of shares at 6,240 million, neutralising the capital increases associated with implementation of the flexible dividend programme. • Growing shareholder remuneration, in line with the increase in results, converging on a payout ratio of between 65% and 75%. Taking into account results forecasts, the dividend will be between 0.37 and 0.40 euro per share by 2020. |

Create value for the shareholder with sustainable growth

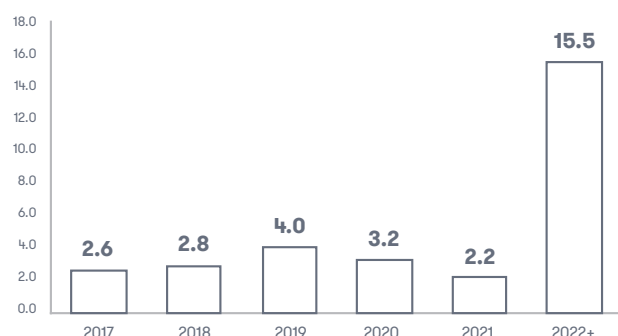
Net Debt (€M)



* Pro-forma including UIL.

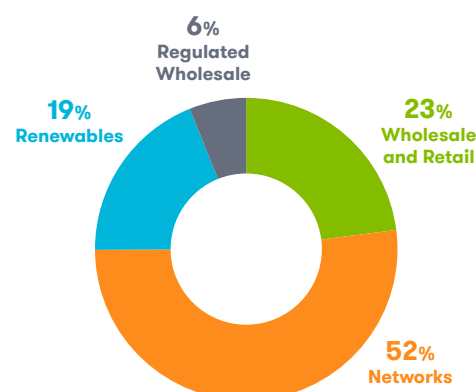
Adjusted net financial debt at 31 December 2016 increased by €1,347 million to €29,414 million, compared to €28,067 million at 31 December 2015, as a result of €720 million of non-recurring taxes in Spain arising from RDL 2/2016 on measures for reducing the public deficit in Spain and other matters, and due to early investments in renewables and the Safe Harbor in the United States (€328 million), among other reasons.

Maturity of financial debt (€M)

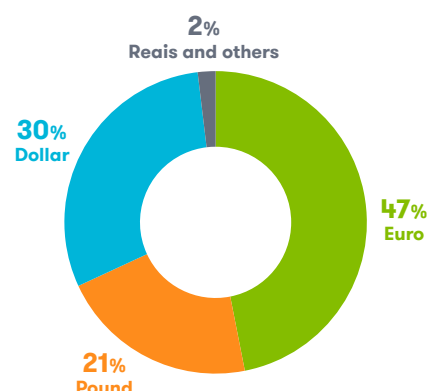


Comfortable maturity profile.

Ebitda by business 2016

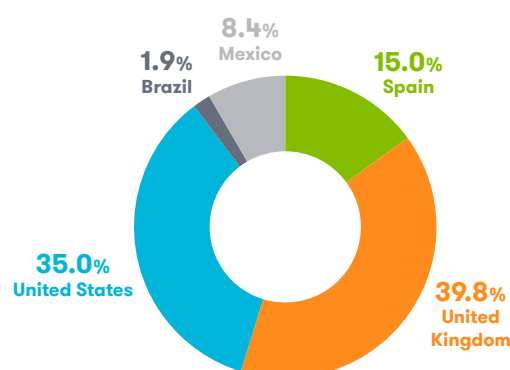


Debt structure by currency in 2016



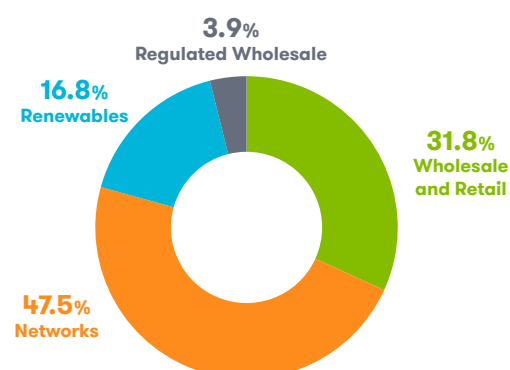
Debt structured by origin of cash flow earned in each currency. Includes derivatives to hedge net investment.

Investment by geographic area 2016



Diversification of investments, with a heavy concentration outside of the euro zone.

Gross margin by business 2016

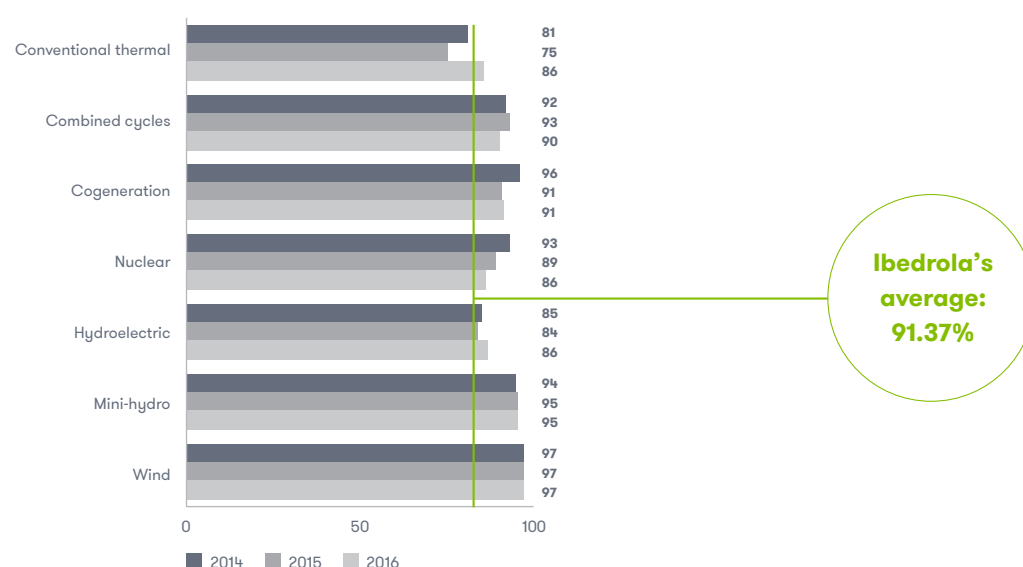


4.2 Manufactured Capital

| | Size | Principal activities 2016 | Outlook |
|---|---|---|--|
| Electric power generation assets | <ul style="list-style-type: none"> Iberdrola's generation assets comprise nearly 300 windfarms, almost 90 hydroelectric power plants (in addition to the mini- hydro plants), 36 thermal power stations using various technologies, 5 of which are nuclear, and other facilities built and operated according to the best available practices. | <ul style="list-style-type: none"> ISO 9000 certification has been attained for the operation of windfarms in Spain and the United Kingdom. | <ul style="list-style-type: none"> Construction continues on almost 1,700 MW of onshore wind, 336 MW of photovoltaic, and 1,064 MW of offshore wind. In Mexico, construction will continue on almost 2,700 MW in combined cycle and 100 MW in cogeneration. In Portugal, there is continued construction of the Tamega hydroelectric complex, with 1,158 MW. In Brazil, work continues on the construction of the Baixo Iguaçu (350 MW total) and Belo Monte (11,233 MW total) hydroelectric plants, through Neoenergia. |
| Power transmission and distribution assets | <ul style="list-style-type: none"> Iberdrola's electricity transmission and distribution networks comprise over 30,000 km of transmission lines, over 1 million km of distribution lines, roughly 4,000 substations and over 1.4 million transformers, built and operated to supply a high-quality, reliable service. | <ul style="list-style-type: none"> In Spain, more than 8.8 million smart meters have been installed (83.5%) and 55,500 transformer centres have been digitised (66%). In the United Kingdom, work has advanced on the Western Link project (completion expected in 2017). SPEN received the Customer Care Award for its customer service and the Scottish Green Energy Award for innovation. Elektro was awarded the National Quality and Iberoamerican Quality awards in 2016. In the United States, Avangrid began the Smart Grid Community Project in Ithaca (NY). | <ul style="list-style-type: none"> Significant proposed transmission projects in Maine and New York to permit the connection of renewable generation projects expected by 2020. Installation of 1.8 million smart meters in New York and automation of the network, putting Avangrid at the forefront of the REV initiative. Investments in the United Kingdom transmission network, to improve the reliability and quality of supply. Progress with the digitisation of the network to lead the transformation towards a Distribution System Operator. |
| Other assets | <ul style="list-style-type: none"> Iberdrola manages approximately 690,000 m² of offices and work centres throughout the world, with a total of 770 properties, of which 358 are located in Spain, 45 in the United Kingdom, 117 in the United States, 231 in Brazil, and 19 in the rest of the world. These properties, which follow the same corporate criteria in the interior spaces, are designed, built, and operated in accordance with the strictest sustainability and efficiency standards. | <ul style="list-style-type: none"> ScottishPower's new corporate headquarters in Glasgow. This is a property with more than 20,000 square meters of offices for more than 1,600 employees. Start-up and the first transfer occurred during the month of December. Phase I of the Iberdrola Campus began in the month of September. Located in San Agustín de Guadalix, this infrastructure is intended to become the backbone of knowledge and training for the employees of the Group. | <ul style="list-style-type: none"> As a culmination to the process of integrating Avangrid, the infrastructure holding its corporate headquarters, located at 180 Marsh Hill Road, Orange, CT, will commence operations during 2017. During the first half of 2017, it is expected that more than 1,600 employees will be transferred to the Glasgow headquarters, as well as the closing of surplus buildings. Construction will begin during 2017 on phase II of the Iberdrola Campus, which will include an expansion of training infrastructures and an office complex. Completion is expected during the first half of 2019. |

Offer a secure supply of energy that is competitive in price and quality

Average availability factor of Iberdrola's generation facilities



Quality of electricity supply

Average power outage duration

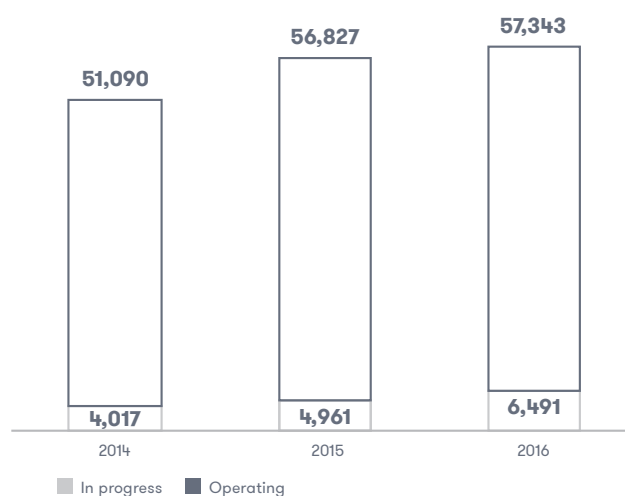
| | | 2015 | 2016 |
|----------------|-----------|-------|-------|
| Spain | TIEPI (m) | 61.9 | 54.0 |
| United Kingdom | CML (m) | 34.8 | 33.5 |
| United States | CAIDI (h) | 1.89 | 1.91 |
| Brazil | DEC (h) | 18.81 | 17.23 |

Power outage frequency

| | | 2015 | 2016 |
|----------------|-----------------|------|------|
| Spain | NIEPI (number) | 1.20 | 1.04 |
| United Kingdom | CI (ratio) | 40.1 | 42.6 |
| United States | SAIFI (index) | 1.21 | 1.15 |
| Brazil | FEC (frequency) | 7.22 | 7.46 |

TIEPI: Installed Capacity Equivalent Interrupt Time.
 CML: Customer Minutes Lost Per Connected Customer.
 CAIDI: Customer Average Interruption Duration Index.
 DEC: Equivalent Duration of Interruption by Consumer Unit.
 NIEPI: Installed Capacity Equivalent Interrupt Number.
 CI: Customer Interruptions Per 100 Connected Customers.
 SAIFI: System Average Interruptions Frequency Index.
 FEC: Equivalent Frequency of Interruption by Consumer Unit.

Property, plant, and equipment (€M)



4.3 Intellectual Capital

| | Management Approach | Principal activities 2016 | Outlook |
|--|--|---|--|
| Promotion of R&D | <ul style="list-style-type: none"> In anticipation of the energy transition towards a more sustainable model, Iberdrola has made an advance wager on innovative solutions that require greater electrification of the economy: more clean energy, more storage capacity, more and smarter grids, and more digitisation. | <ul style="list-style-type: none"> Significant increase in R&D investment: More than €211 million in 2016, a 6% increase over 2015. Being recognised as the most innovative utility in Spain and the third most innovative in Europe, according to the European Commission. Launch of “Iberdrola Universitas”, an initiative that will gather together all of Iberdrola’s activities with the academic world. The goals are to promote a university-company transfer of knowledge, the attraction of talent, and contribution to the “social dividend”. | <ul style="list-style-type: none"> Progress on the R&D Plan 2015-2017. R&D will continue to be a key factor to successfully achieve a new growth phase of our Company, making it the <i>utility of the future</i>, founded on sustainable development, the promotion of renewable energy, and emerging technologies, as engines for the creation of value and social contribution. |
| Efficiency and new products and services | <ul style="list-style-type: none"> Continuous optimisation of our operations, management of the lifecycle of facilities and equipment, reduction in operating and maintenance costs, and decreasing environmental impact. Development of new and competitive products and services that adapt to an increasingly global market, the main goal of which is to meet the needs of customers. | <ul style="list-style-type: none"> New initiatives to improve the customer experience: personalisation of content and offers, delivery of proactive real-time communications, online self-service, Optimum Rate, and Energy Advisor. New Smart Home products: Consumption Monitor, an electric meter capable of breaking down the consumption of main domestic appliances, and Smart Lamps, smart LED bulbs that can be controlled from a mobile device. | <ul style="list-style-type: none"> Our commitment to innovation will continue to be a priority in order to keep Iberdrola at the forefront of developing the new products, services, and business models that are transforming the industry. Finally, we will continue making efforts to offer our customers better and more efficient service and to contribute to sustainable development with our innovative activities. |
| Disruptive technology and business models | <p>Through the Iberdrola Ventures- Perseo corporate venture capital programme, there has been more than €50 million invested since 2008 in technologies and new disruptive businesses, which ensure the sustainability of the energy model. Lines of activity:</p> <ul style="list-style-type: none"> Customer focused solutions: energy efficiency, demand management, digital solutions, etc. Distributed energy resources: innovative generation and distributed storage solutions. Renewable energy: technologies related to renewable generation (solar, wind, offshore wind). New technologies applied to the operation and maintenance of energy infrastructures: robots, sensors, software, drones, etc. | <ul style="list-style-type: none"> Positioning of the company Silicon Valley Stem as the market leader in distributed storage. This start-up offers savings to commercial and industrial customers through a solution behind a meter that includes software (big data and cloud) and batteries. Stem reached 200 installations of distributed storage during 2016. Growth and development of the Salamancan company Arbórea Intellbird, jointly owned by Perseo and CDTI, which sells drone inspection services for all kinds of energy infrastructure. During 2016, it has inspected more than 600 of the Company’s wind turbine blades, preventively detecting anomalies and permitting a reduction in the cost of repairs and improved planning of corrective maintenance. | <ul style="list-style-type: none"> Ensure Iberdrola’s access to the energy technologies of the future. Foster entrepreneurship and the development of an innovative entrepreneurial fabric within the energy sector: investment in initiatives with a high social and job creation component. Establish alliances with key technology providers for Iberdrola (Open Innovation Ventures). |

Highlight the value of the Company's intangible assets

Main R&D research projects

Renewable energy

- Projects to improve the efficiency of assets and models for the design of windfarms. Monitoring of the main equipment for early detection of failures or reduced production using artificial intelligence/big data. The area of energy resources includes the *HPC4E* (High Performance Computing for Energy) project, which plans to use computational fluid dynamics (CFD) models in future exascale supercomputers.
- The area of offshore wind includes the installation of jacket piling and foundations at the Wikingen offshore windfarm, as well as innovative substation design based on a 6-legged jacket foundation design built in two separate blocks to simplify transport to the site.
- Renewable energy integration projects include the exceptional *ESS2Wind* project, which aims to analyse the possible application of battery storage systems associated with windfarms to provide auxiliary services to the system.

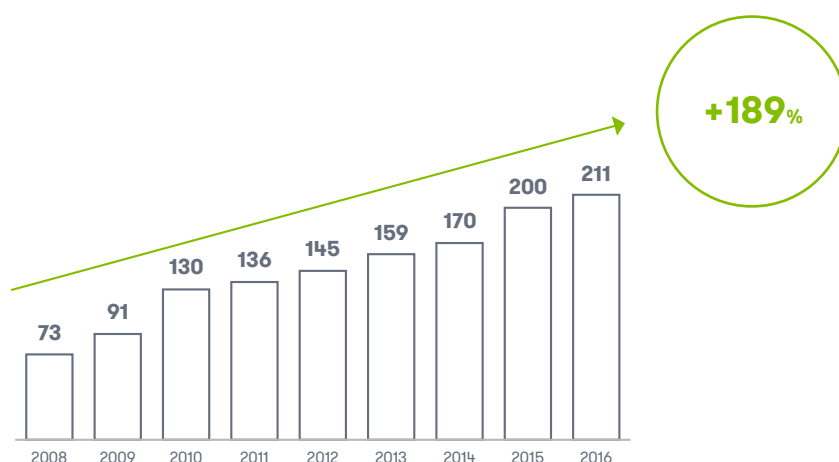
Smart grids

- The *iGreenGrid* project for developing specific methods for integrating renewable energy into the electric distribution grids and the *Discern* project for comparing different smart grid solutions to discover the ideal arrangement of architectures were successfully completed.
- In the United Kingdom, work continues on the *Visor*, *Angle* and *Fitness* projects to improve the transmission and distribution network, strengthening smart grids.

Clean generation

- The *CO₂Formare* project, the goal of which is to avoid macrofouling in a sustainable manner, reducing environmental impact. The first tests for injecting CO₂ into water have been performed, the results have been satisfactory, and the previously developed CO₂ capture modules will soon be installed at the plant.
- The *Prexes* project, which focuses on developing a model for predicting expansion in concrete hydraulic structures.

Investments in R&D (€M)



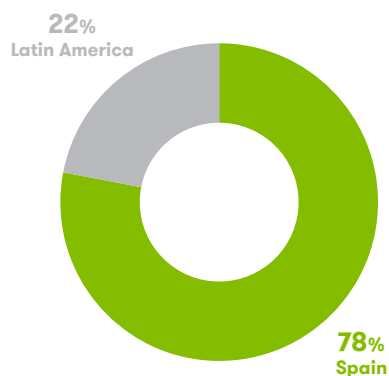
4.4 Human Capital

| | Management approach | Principal activities 2016 | Outlook |
|---|--|---|--|
| Global human resources management | <ul style="list-style-type: none"> • Achieve the goals of competitiveness and business efficiency in a climate of social peace, fostering stable, high- quality employment. • Harmonise human resources processes and make inroads with implementing the Iberdrola culture in all countries, respecting specific local conditions. | <ul style="list-style-type: none"> • Finalisation of the project for integration of the Human Resources Model [OneHR project] at Avangrid. • Management of an appropriate labour relations framework that can be adapted to suit business and social requirements. | <ul style="list-style-type: none"> • Consolidate the Human Resources function at Avangrid, extending and unifying best practices. • Strengthen the commitment to social responsibility, fostering ethical and responsible behaviour. • Maintain team pride, workforce satisfaction, job commitment, and productivity. |
| Goal of "accident reduction" | <ul style="list-style-type: none"> • Prioritise the safety of individuals at the Group's facilities and within its sphere of influence, fostering a progressive reduction in incident rates and improving health and safety conditions. • Replicate throughout the Group the best practices identified in the area of occupational health and safety, fostering a culture of excellence in management and coordinating global preventive activities. | <ul style="list-style-type: none"> • Attainment and/or maintenance of the OHSAS 18001 certification, and approval of a system of global prevention standards in accordance with the Group's policy. Assessment of level of conformance to global standards. • Monitoring of proactive and reactive indicators among the Group's companies for the global scorecard. • Establishment of goals for the management of occupational health and safety at subcontractors. • Identification and application of best safety practices. Exchange of lessons learnt. Creation of groups to promote safe behaviour. | <ul style="list-style-type: none"> • Define the global occupational health and safety strategy for the coming years. • Continue with assessment of level of conformance to global standards and the implementation of improvement groups to promote safe behaviour. • Continue developing certifications of the Group in accordance with OHSAS 18001. • Analysis of accident rate and establishment of goals for Group and subcontractor employees. • Global campaigns to raise awareness on certain types of common accidents. |
| Talent management | <ul style="list-style-type: none"> • Drive staff qualifications, preparing employees to work in a multicultural environment and making continual efforts to improve their employability. • Develop alternatives to compensate for factors stemming from the ageing of the workforce. • Maintain a team of competent, committed, and motivated professionals, which is key for the sustained success of the business. | <ul style="list-style-type: none"> • Promotion of job and international mobility within multicultural teams in a global context. • Launch of new Management School programmes. • Expansion of the professional training and development model to all countries. • Identification of the group of high-potential professionals to provide the organisation with professionals will lead the Iberdrola of the future. • Expansion of the process of publishing internal vacancies at the global level. | <ul style="list-style-type: none"> • Strengthen the talent and leadership development management model at the international level. • Define and implement the Global Development Roadmap for the Iberdrola Group. • Attract the best talent, strengthening excellence in our selection processes. • Integrated talent management of the Company in order to train future leaders, preparing them now to assume larger responsibilities. • Development of the second phase of the Campus project. |
| Diversity, equal opportunity, and reconciliation | <ul style="list-style-type: none"> • Guarantee a social model committed to professional excellence and the quality of life of our employees. • Development of labour relations based on equal opportunity, non- discrimination, and respect for diversity. • Create a high-quality labour environment by committing to reconciliation, and promote a position of leadership in these areas in the countries in which it does business similar to that enjoyed in Spain. • Align the Corporate Volunteering Programme with the Sustainable Development Goals defined by the United Nations. | <ul style="list-style-type: none"> • International cultural exchange programmes. • Corporate Volunteerism Activities focused on improving the quality of life and the integration of vulnerable groups, including the <i>International Volunteering Day</i>, the <i>Involve</i> international volunteering programme, and the project for improving the electricity situation of several refugee camps in Ethiopia. • Launch of the volunteer project regarding the fight against climate change. Sustainable Development Goals 4 (Quality education) and 13 (Climate action). | <ul style="list-style-type: none"> • Continue to foster improvements in the quality of people's lives through social-welfare activities in all of the countries in which the Iberdrola Group has a presence, creating a global volunteer community. • Promote the internationalisation of social programmes and strengthen ties among the employees of the Group at the global level. • Contribute to achieving the Sustainable Development Goals defined by the United Nations for the 2015-2030 horizon. |

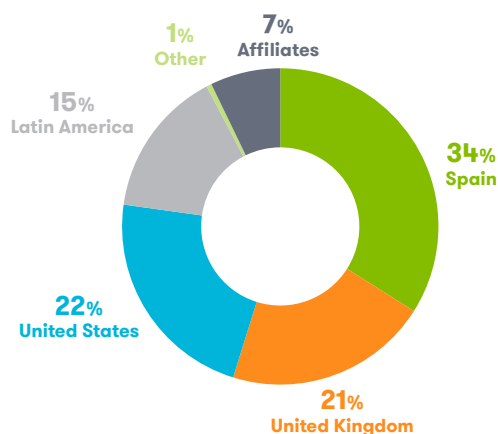
Ensure the availability of a committed, qualified workforce in a safe and stable environment

Growth and geographic diversification of the workforce

2006: 16,155 employees



2016: 30,591 employees



© Key Figures / page 12

Social commitment



© José Ramón Ladra

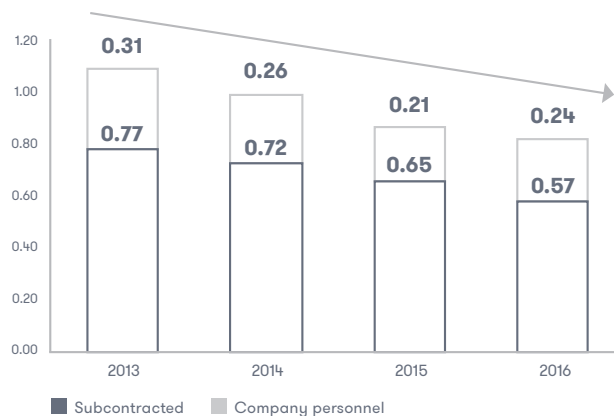
Visit by their Majesties the King and Queen of Spain to Iberdrola's headquarters in Madrid for the tenth anniversary of the international Corporate Volunteering programme and the delivery of the Iberdrola Scholarships 2016.

Iberdrola Campus: Finalisation of first phase



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Accident rate (2013-2016): progressive reduction



■ Subcontracted ■ Company personnel

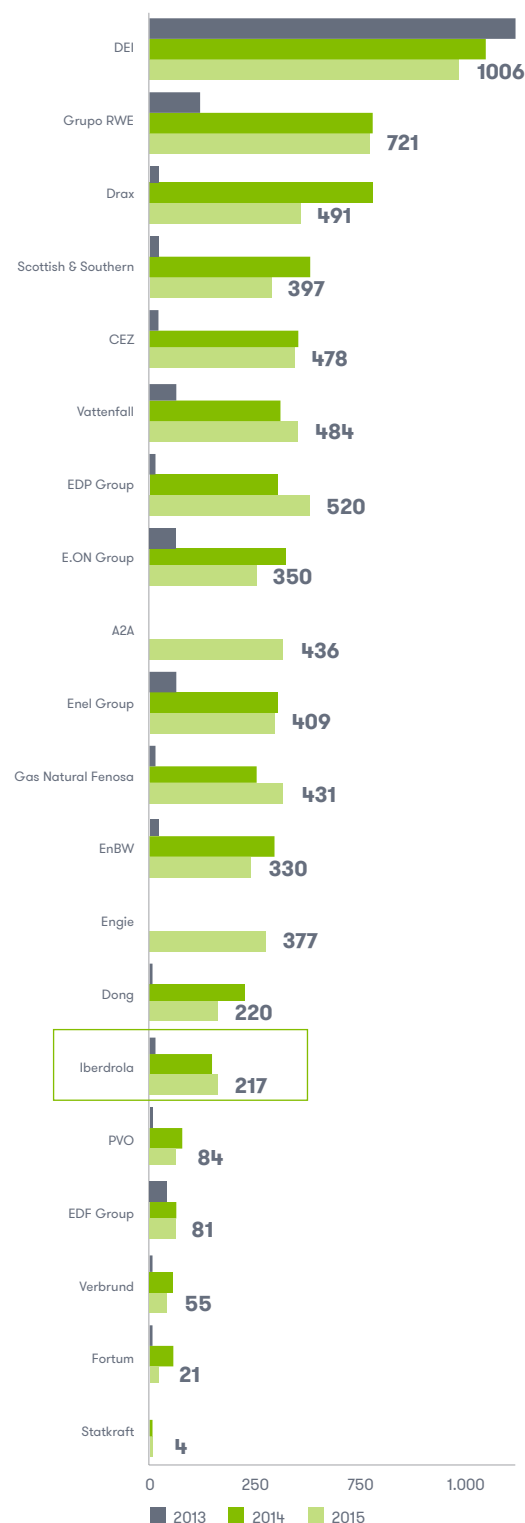
26% in subcontracted personnel and 23% in Company personnel.

4.5 Natural Capital

| | Management Approach | Principal activities 2016 | Outlook |
|---|---|---|---|
| Environmental management and biodiversity | <ul style="list-style-type: none"> Integrate standards for conserving biodiversity when engaging in new projects. Reduce environmental risks in the operation of existing facilities. Promote the protection of ecosystems in the surroundings of the facilities. Strengthen transparent dialogue with Stakeholders in seeking solutions to environmental problems. Manage environmental compliance by suppliers. Transparently report on environmental results and activities. | <ul style="list-style-type: none"> Sustainable General Shareholders' Meeting 2016: <ul style="list-style-type: none"> ISO 20121 certification. Erronka Garbia Environmental certification. ISO-TS 14072 Certificate for Corporate Environmental Footprint (CEF) 2015. Development of Environmental Product Declaration (EPD) for the Kilgallioch windfarm under construction in Scotland. Energy efficiency project for the facilities of Iberdrola España (conformance to RD 56-2016). Climate Change Adaptation Report for activities in Spain. | <ul style="list-style-type: none"> Adaptation to ISO 14001 2015 standard. Development of EDP for an offshore windfarm. Development of a strategic plan for Climate Change Adaptation. CEF by region. Environmental Guidelines linked to impacts of the CEF. Restoration, recovery, improvement, and maintenance of surroundings and habitats. |
| Prevention of pollution | <ul style="list-style-type: none"> Prevent pollution and the emission of greenhouse gases (GHGs) through practices that reduce or eliminate the production of pollutants at source. Reduce the emissions of non-GHGs into the air. Gradually replace equipment using substances that reduce the ozone layer. Promotion of awareness-raising campaigns regarding air quality. New GHG emissions-free facilities (renewable, wind, hydroelectric, etc.). | <ul style="list-style-type: none"> 42% reduction in intensity of CO₂ emissions per kWh produced since 2007. Thermal emission factor has decreased from 460 g/thermal kWh generated in 2015 to 391 g/kWh generated in 2016. Increase in emission-free installed capacity to 65.9%. Closure of Lonnganet coal plant in the United Kingdom. New commitment to reduce emissions, and active participation in the Marrakesh Climate Conference (Morocco). Sustainable mobility plan, electric car. | <ul style="list-style-type: none"> Achieve a 50% reduction in emissions intensity by the year 2030 in comparison to 2007. Carbon neutral by 2050. Develop innovation projects geared towards reducing pollution. Actively participate in achieving the Sustainable Development Goals approved in September 2015 (goals 6, 7, and 13). |
| Operating excellence and energy efficiency | <ul style="list-style-type: none"> Continuous improvement in operational performance, increase in energy efficiency, increase in energy savings, reduction in consumption of natural resources, etc., all while promoting the use of environmentally-friendly resources. | <ul style="list-style-type: none"> Innovative activities in environmental management and control. Assurance of quality in environmental management. Efficient management of water consumption. | <ul style="list-style-type: none"> Development and promotion of ecodesign initiatives. Life-cycle and green purchasing analysis. |
| Waste management | <ul style="list-style-type: none"> Improve control and management of waste (hazardous and non-hazardous) generated. Minimise the generation of waste at source. Maximise the reuse, recycling, and recovery of waste. | <ul style="list-style-type: none"> Reuse of waste from thermal coal plants. Carry out waste minimisation plans, recycling plans, and awareness campaigns aimed at employees. | <ul style="list-style-type: none"> Make progress in the optimisation of waste management: circular economy. Draw up economic/financial analyses of the best waste management strategies. |

The environmental dimension is a key factor in the concept of sustainability

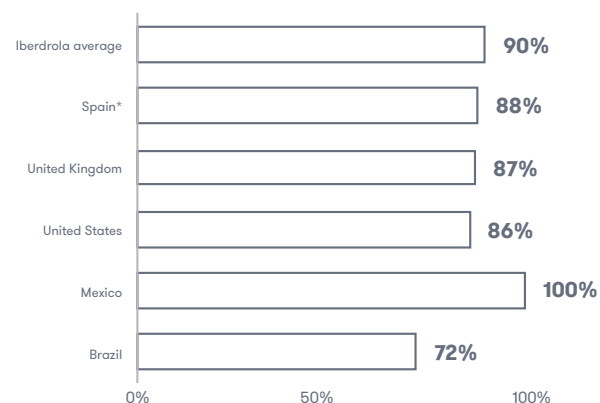
CO₂ emissions at companies in the sector (Carbon factor in kg of CO₂/MWh)



European carbon factor 2015: 311 kg CO₂/MWh.

Source: "Facteur carbone européen Comparaison des émissions de CO₂ des principaux électriciens européens" PwC France. Nov 2016.

Production of Iberdrola plants using local energy sources in the countries in which it operates

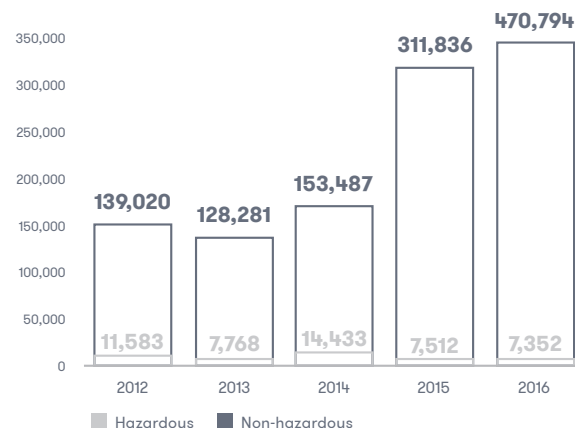


* Nuclear fuel acquired from the Spanish company Enusa is considered a local source.

Intensity of emissions at the thermal plants of the Group (CO₂/MWh)



Volume of recovered, reused, or recycled waste (t)



© Key Figures / page 12

4.6 Social and Relationship Capital

Stakeholder relations

Iberdrola wants to engage its Stakeholders in all of its activities and businesses, participating in an ongoing and constructive dialogue with them in order to know their expectations, build strong ties, and thus generate confidence and forge a sense of belonging to an excellent company, of which they feel they are a part.

Management approach

Iberdrola's strategic approach sets great store by its relations with Stakeholders, giving importance to the dual facets of this relationship:

- In terms of social responsibility, meeting their expectations and needs.
- In terms of reputation, managing Stakeholders' perception of the Company.

Principal activities 2016 and Outlook

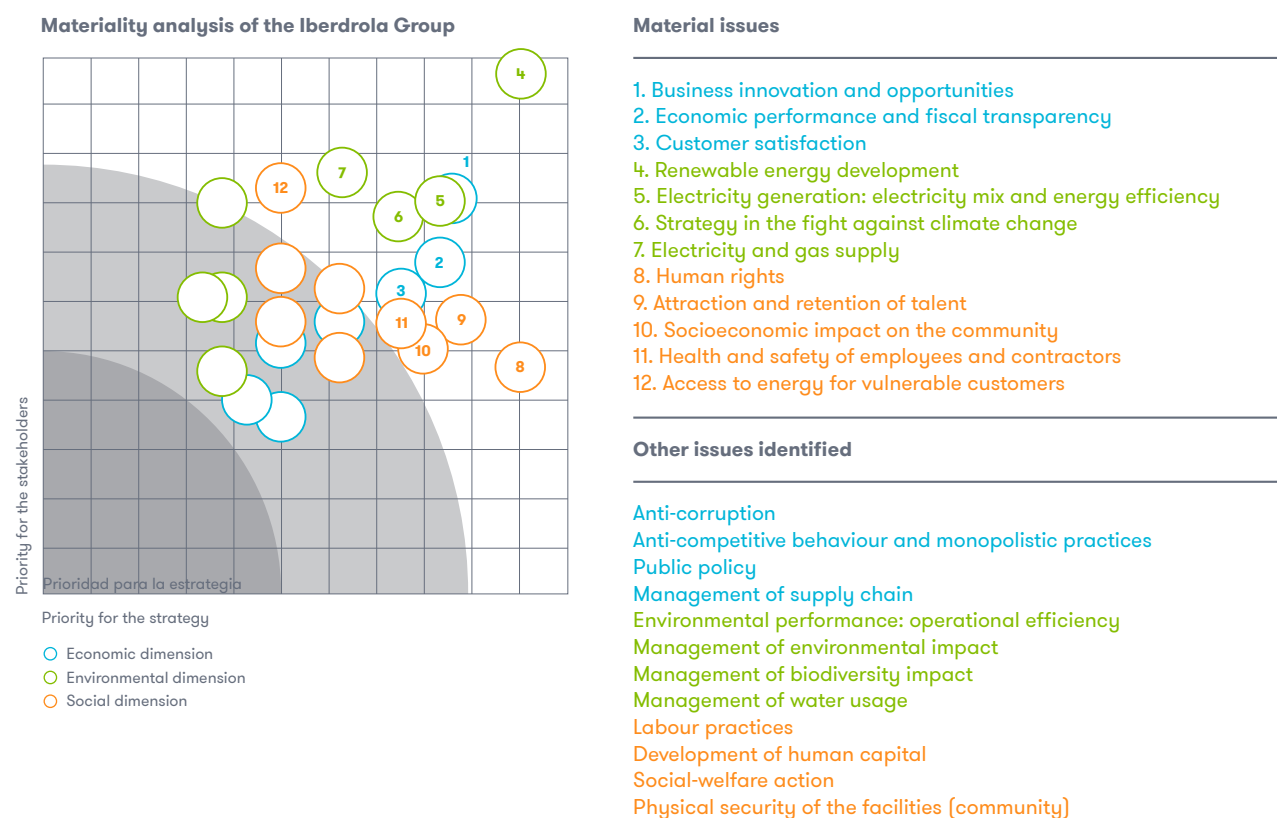
- Approval of a new *Stakeholder Relations Model*, the goals of which are:
 - To further develop the *Stakeholder Relations Policy* approved by the Board of Directors in 2015.
 - To systematise Stakeholder relations throughout the Iberdrola Group.

- To create a business culture with respect to the significance of dialogue with the Stakeholders.
- Monitoring of the AA1000 standard, in accordance with the principles of inclusiveness, materiality, and responsiveness:
 - Update of the channels of communication with the Stakeholders.
 - Identification of the most significant matters.
 - Balanced and reasonable response thereto.
- New microsite on the Employee Portal (Intranet) to internally disseminate the importance of the dialogue and of the relations with Stakeholders.
- In 2017, implementation of the new *Stakeholder Relations Model* throughout the Iberdrola Group.

A materiality analysis allows for prioritisation of the issues most important to the Company's Stakeholders.

Materiality

A Materiality Study allows for prioritisation of the issues most important to the Iberdrola's Stakeholders. In the *Sustainability Report 2016*, Iberdrola explains the management approaches taken by the Company in regard to these significant issues and the results achieved. The following graph summarises the main issues.



Community support and electricity access programmes

Primary programmes

Activities 2016

- Contribution of €44 million to the community in the countries in which Iberdrola operates, measured according to the London Benchmarking Group (LBG) international standard.
- International corporate volunteering programme, offering various volunteering opportunities to employees in Spain, the United Kingdom, the United States, Mexico, and Brazil.
- Entrepreneurial support: over €46 million of procurement from companies in operation for less than 5 years, and €70 million in venture capital for new initiatives with high technological value.
- Programmes and pricing to aid vulnerable groups in Spain, the United Kingdom, the United States, and Brazil.
- Rural electrification programmes in Brazil, to which €18 million has been allocated on a consolidated basis.
- Programmes implemented by the foundations created by Iberdrola in the principal countries in which it operates.
- Development of the *Electricity for All Programme*.

Electricity for Everyone

- The Sustainable Development Goals (SDGs) 2015-2030, approved at the UN Sustainable Development Summit in New York (September 2015), entail the recognition of energy as an engine of sustainable growth.
- The *Electricity for All* programme is Iberdrola's response to this demand to extend universal access to modern forms of energy, with environmentally sustainable, financially affordable, and socially inclusive models. This initiative is focused on sustainable electrification activities in emerging and developing countries.
- Iberdrola has set itself the goal of reaching 4 million beneficiaries of this programme by 2020. At year-end 2016, the programme had reached 2.5 million users.

Economic value distributed (€M)

| Item | 2015 | 2016 |
|--|-------|-------|
| Procurement from suppliers | 5,093 | 6,415 |
| Payments to providers of capital | 1,646 | 2,692 |
| Payments to government administrations | 2,746 | 2,740 |
| Employee remuneration | 2,187 | 2,260 |

© Sustainability Report

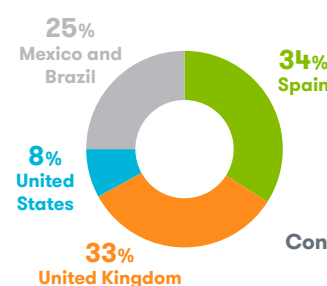
Foundations of the Iberdrola Group

Activities 2016

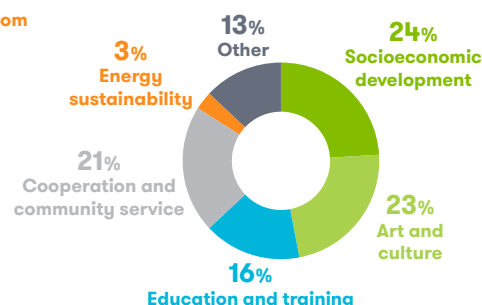
- Iberdrola has strengthened the operation of its foundation activities in Spain, the United Kingdom, the United States, Mexico, and Brazil through the actions of the Foundations Committee, as the body coordinating all of their activities and of the corresponding Boards of Trustees in each country.
- Contributions and amounts dedicated to activities have increased in all countries, including the United States, where the Avangrid Foundation has integrated a large portion of the social welfare actions carried out by UIL and its foundations.
- As regards the activities themselves, the four areas of the Master Plan (Training and Research, Art and Culture, Sustainability and Biodiversity, and Cooperation and Solidarity) have been promoted in all of the countries.
- In the training area, Iberdrola's *Scholarships and Research Assistance Programme* gave a total of 130 scholarships for students in the five aforementioned countries in 2016.
- The area of art and culture includes illumination projects like that for the *Municipality of San Sebastián*, support for exhibitions like the new *Energise Area of the National Museum of Scotland*, and projects supporting music like the *Eastman School of Music* in Rochester.
- In the area of sustainability and biodiversity, there have been multiple collaboration projects with educational and environmental centres in these five countries.
- In the area of cooperation and solidarity, there has been a strengthening of the *Social Assistance* programme in Spain and the many collaborations in the United States and the United Kingdom.

Programme results 2016

Contribution by region (%)



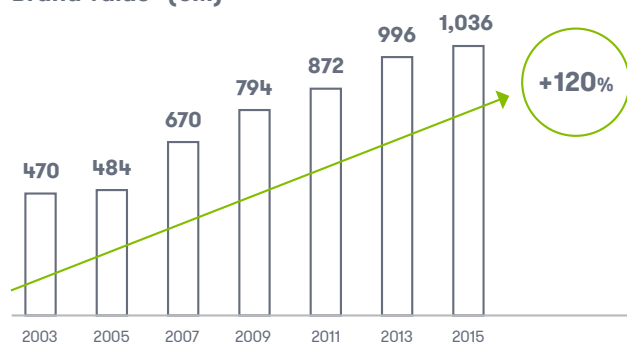
Contribution by programme (%)



Soundness and strength of the brand

- Management of the brand in such a way that it transmits the principles set out in the *Mission, Vision, and Values of the Iberdrola Group* and reflects the Company's strategy of commitment to the environment.
- Consolidation of an international brand, strengthening communication and alignment under a single brand positioning strategy in the countries in which the Company operates.

Brand value* (€M)



Source: Ranking of Best Spanish Brands by Interbrand.

Evolution of the digital ecosystem

- Offer of useful and dynamic information, with messages adapted to each stakeholder.
- Facilitate direct interaction with our stakeholders, overcoming barriers and making use of existing synergies.

Iberdrola on social media and the Internet:



Brand and reputation intelligence

- At Iberdrola, the establishment and attainment of goals allows for the conquering of challenges and sustainable growth. Thanks to the alignment between these goals and the expectations of the Stakeholders, both internal and external recognition is achieved and relations of trust are strengthened, thus increasing reputation.
- In 2016, the creation of a Brand and Reputation Intelligence Unit has allowed for progress down the path of acquiring an awareness and analysis of the brand and management of the corporate reputation as elements to take into account in short-, medium-, and long-term strategic decision-making.
- Good corporate governance is the great driver for identifying and evaluating reputation risks through policies, while the value of the brand and the value of the Company are the major beneficiaries of the implementation of an intelligence system that protects the Company from negative impacts on its reputation and risks. This is reflected in the following chart on the value creation process using brand and reputation analysis and intelligence tools:



Figure 1.
Brand and reputation intelligence value creation process

- Within this context, one of the greatest challenges on which progress has been made this year was the identification of reputational risk factors as well as the implementation of initiatives that raise the Company's awareness to confront and overcome them. Being aware of the opinion of the Stakeholders, their expectations, and what they think of the business is a vital issue for overcoming this challenge and maximising the success of the Company within a competitive marketplace and in the financial markets. Along these lines, a worldwide employee opinion survey was carried out in 2016. This has provided an awareness of the opinion of the employees regarding Iberdrola's reputation and the local brands through which it acts in the following countries: Spain, United Kingdom, United States, Mexico, and Brazil.
- Finally, good reputation shows that good governance is aligned not only with shareholders and the financial community but also with customers, employees, and each and everyone of the Stakeholders, for which reason management plans are being implemented with each of them.

International Volunteer
Day in Scotland
/ UK

© Chris James



Iberdrola Tower, Bilbao
/ Spain

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A Framework of Trust

5.1 Corporate Governance Model

Foundations of Iberdrola's corporate governance model

A. Corporate Governance System

Iberdrola is a leading multinational Group in the energy industry that seeks to create value in a sustainable manner for society, citizens, customers, and shareholders; which innovates and uses environmentally-friendly energy sources and considers its employees to be a strategic asset; committed to social return through all its business activities, generating employment and wealth in its environment, all within a strategy of social responsibility and compliance with tax regulations.

Iberdrola has adopted a Corporate Governance System made up of the *Mission, Vision, and Values* of the Group, *By-Laws, Corporate Policies, Internal Corporate Governance Rules*, and other internal codes and procedures, all available at www.iberdrola.com.

The content thereof is inspired by and based on a commitment to best corporate governance practices, business ethics, and social responsibility in all of its areas of activity.

| Position | Director | Status | Date of last appointment | Ending date |
|----------------|--|----------------|--------------------------|-------------|
| Chairman & CEO | José Ignacio Sánchez Galán [Salamanca, Spain, 1950] | Executive | 27-03-2015 | 27-03-2019 |
| Director | Íñigo Víctor de Oriol Ibarra [Madrid, Spain, 1962] | Other external | 08-04-2016 | 08-04-2020 |
| Director | Inés Macho Stadler ⁽¹⁾ [Bilbao, Spain, 1959] | Independent | 08-04-2016 | 08-04-2020 |
| Director | Braulio Medel Cámara [Marchena, Seville, Spain, 1947] | Independent | 08-04-2016 | 08-04-2020 |
| Director | Samantha Barber [Dunfermline, Fife, Scotland, United Kingdom, 1969] | Independent | 08-04-2016 | 08-04-2020 |
| Director | María Helena Antolín Raybaud [Toulon, France, 1966] | Independent | 27-03-2015 | 27-03-2019 |
| Director | Santiago Martínez Lage [Betanzos, A Coruña, Spain, 1946] | Independent | 27-03-2015 | 27-03-2019 |
| Director | José Luis San Pedro Guerenabarrena [Bilbao, Spain, 1946] | Other external | 27-03-2015 | 27-03-2019 |
| Director | Ángel Acebes Paniagua [Ávila, Spain, 1958] | Independent | 27-03-2015 | 27-03-2019 |
| Director | Georgina Kessel Martínez [Mexico City, Mexico, 1950] | Independent | 28-03-2014 | 28-03-2018 |
| Director | Denise Mary Holt [Vienna, Austria, 1949] | Independent | 27-03-2015 | 27-03-2019 |
| Director | José W. Fernández [Cienfuegos, Cuba, 1955] | Independent | 27-03-2015 | 27-03-2019 |
| Director | Manuel Moreu Munaiz [Pontevedra, Spain, 1953] | Independent | 27-03-2015 | 27-03-2019 |
| Director | Xabier Sagredo Ormaza [Portugalete, Spain, 1972] | Other external | 08-04-2016 | 08-04-2020 |

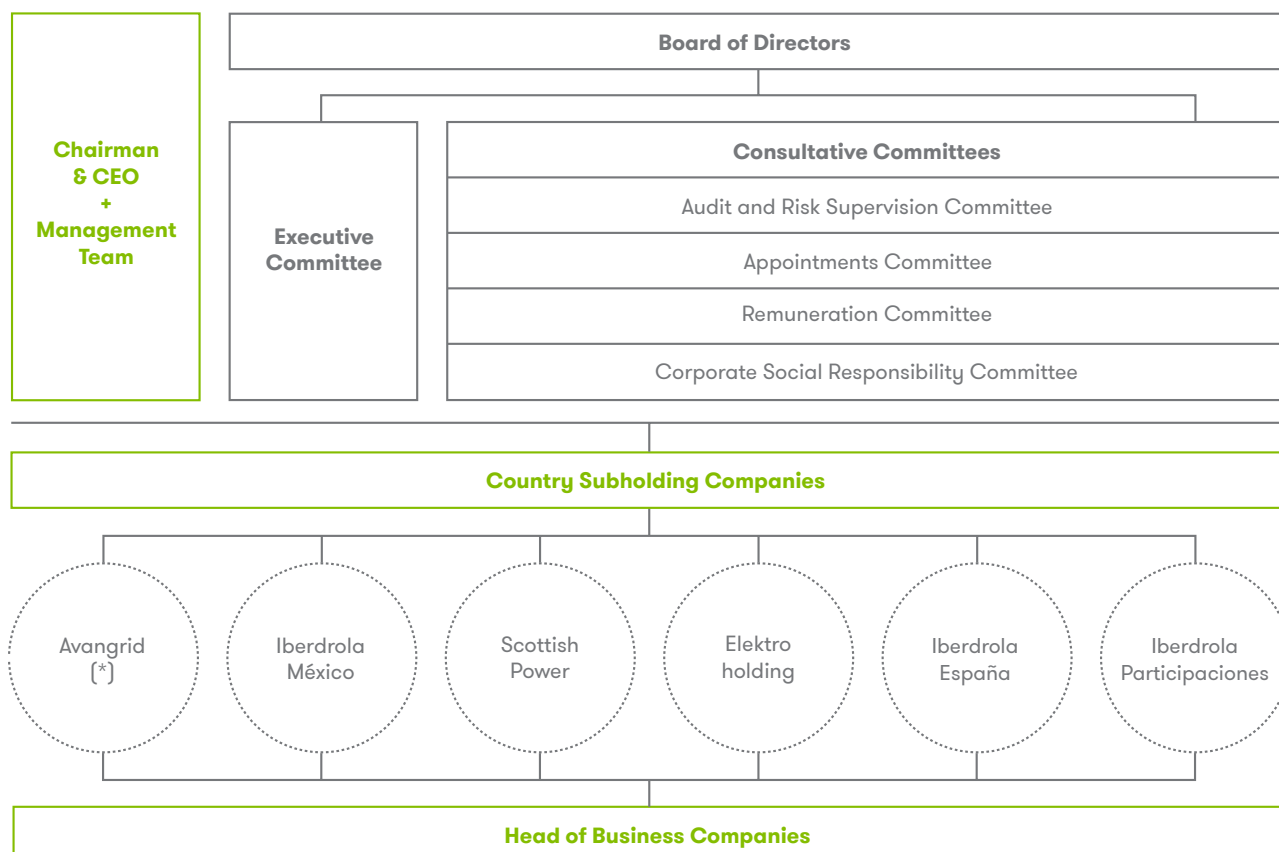
⁽¹⁾ Inés Macho Stadler is the lead independent director (*consejera coordinadora*).

B. Governance model

Appropriate differentiation between the duties of strategy and supervision and those of guidance and management:

- The Board of Directors of Iberdrola, S.A., made up of a large majority of independent directors, focuses its activity on the determination, supervision, and monitoring of the strategies and general guidelines that must be followed by the Group.
- The chairman of the Board of Directors & chief executive officer and the rest of the management team are responsible for the organisation and strategic coordination of the Group, through the dissemination, implementation, and monitoring of the overall strategy and basic guidelines.
- In all of the countries in which the Group operates, organisation and strategic coordination is implemented through country subholding companies, which group together equity stakes in the energy head of business companies carrying out their activities in the respective country and centralise the provision of services common to such companies. In addition, the Group has a country subholding company that groups together the non-energy businesses. Country subholding companies have Boards of Directors, including independent directors and their own Audit and Compliance Committees, Internal Audit divisions or units, or Compliance divisions.
- The head of business companies are in charge of the day-to-day administration and effective management of each business. They also have Boards of Directors, which include independent directors and specific management teams. This structure, which operates together with the Group's Business Model, allows for an overall integration of the businesses (Networks, Wholesale and Retail, and Renewables) and focuses on maximising the operational efficiency thereof through the implementation of best market practices.

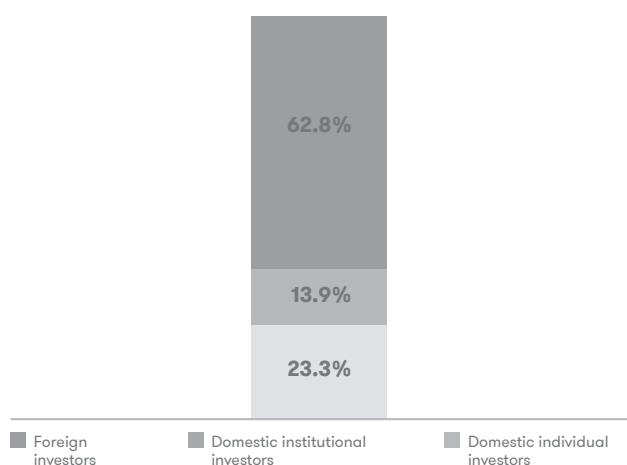
Corporate and governance structure of Iberdrola, S.A



(*) Company listed on the New York Stock Exchange.

C. Equity structure

Iberdrola has more than 600,000 shareholders throughout the world, and none of them has a controlling interest.



Foreign institutional shareholders account for 62.8% of the capital.

© External corporate governance awards / page 39

With Shareholder Week, which culminates with the holding of the General Shareholders' Meeting, Iberdrola brings the Company closer to and promotes interaction with its shareholders to give form to its corporate governance and social responsibility strategy, sharing events and initiatives regarding social-welfare, cultural, technological innovation, and digital transformation actions.

Iberdrola's response to the corporate governance challenge

A. Continuous Improvement of its corporate governance rules and practices

On corporate governance matters, the Company looks to the Good Governance Code of Listed Companies published by the CNMV and generally accepted recommendations in the international markets.

71.4% of the directors are independent.

| | |
|--|--|
| Remuneration policy | Executive directors' variable remuneration tied to objectives. |
| | Transparency. |
| | Provision for revision and reimbursement of deferred variable remuneration. |
| Operation of the Board | 71.4% of directors are independent. |
| | System of checks and balances, including a lead independent director (<i>consejera coordinadora</i>). |
| | All consultative committees have 100% or a majority of independent directors. |
| | Gender diversity: 5 women on the Board. All consultative committees are chaired by women. |
| | Cultural diversity: directors from 6 countries of origin. |
| | Rationale for proposed appointments. |
| Social responsibility and corporate reputation | External evaluation of governance bodies. |
| | Specific Corporate Social Responsibility Committee. |
| | Social Responsibility Policies. |
| | Company social action strategy through foundations related to the Iberdrola Group in Spain, United Kingdom, Brazil, United States, and Mexico. |

© Ethics and Social Responsibility / page 90

B. Commitment to shareholders and investors

- The strength of the Group's industrial and financial model will us to continue on a path of increased profits and shareholder remuneration thanks to balanced growth focused on the regulated networks businesses, renewables, and long-term contracted assets.
- Engagement: shareholders are the key players within the Corporate Governance System, which includes good governance practices beyond those required by applicable law. The *Shareholder Engagement Policy* is implemented through various channels of participation intended to build a continuous dialogue beyond the General Shareholders' Meeting.
- Boost shareholders' participation at the General Shareholders' Meeting through the payment of an attendance bonus. Since its implementation in 2007, the quorum in attendance at the General Shareholders' Meeting has exceeded 75%, and has exceeded 77% during the last three years.

The quorum in attendance at the 2016 General Shareholders' Meeting was 77.91%.



C. Alignment between corporate governance and strategy

- Director remuneration aligned with strategic objectives and shareholder return. The remuneration model for directors is based primarily on three components:

Remuneration model for the Board

| Type of remuneration | External (non- executive) directors | Executive directors |
|----------------------|-------------------------------------|--|
| Fixed | According to their duties | On market terms. |
| Short-term variable | Not applicable | Tied to annual targets. |
| Long-term variable | Not applicable | Tied to multi-annual targets and paid in shares (3-year accrual period and payment deferred over 3 years following accrual). |

There were only 2.16% votes against the *Annual Director Remuneration Report 2015*.

Parameters to which the annual variable remuneration of executive directors is tied in 2017

| | |
|-----------------------|--|
| Financial | Results. Shareholder return. |
| Social responsibility | Presence on international indices. Level of consensus received for the proposals of the Board at the General Shareholders' Meeting. Growing female presence in management positions. Labour climate. Professional training. |

Parameters to which the multi-annual variable remuneration of executive directors is tied (2017-2019)

| |
|---|
| Net profit. |
| Total shareholder return. |
| Financial strength. |
| Reduction in CO ₂ emissions. |

Principal activities of the Board of Directors

Key issues in 2016

Iberdrola's Board of Directors has focused its activities on approving the strategic goals of the Group, on defining its organisational model, and on supervising the implementation and further development thereof.

| Strategy | | |
|--------------------------|---|--|
| Growth | The Board of Directors approves the strategic goals and determines the focus of the Group's most significant investments, ensuring that they are made in the businesses identified as priority, regulated, and renewable businesses, as well as in countries with a high credit rating. | <p>Approval and update of the Outlook 2016-2020 and of the strategic pillars.</p> <p>Approval of the strategy and budgets for financial year 2017.</p> |
| Financial strength | The Board of Directors determines the financial strategy during a growth phase of the Company. | Approval of a set of diversified financing sources . |
| Sustainable remuneration | The Board of Directors ensures that shareholder remuneration is aligned with growth in the Group's results. | <p>Validation of the objective of growth in shareholder remuneration in line with the increase in results.</p> <p>Approval of an approximately 11% increase in shareholder remuneration with a charge to 2016.</p> |

Noteworthy milestones: Outlook 2016-2020.

Increase of close to 11% in shareholder remuneration with a charge to 2016.

| Supervision | | |
|-------------|---|---|
| Supervision | The Board of Directors, with the support of the Executive Committee, supervises on an ongoing basis the implementation of the Group's strategy and the development of the Group's organisational model. | <p>Detailed study of priority markets.</p> <p>Analysis of the performance and expectations for the future of the Businesses.</p> <p>Monitoring the integration of Avangrid.</p> <p>Regular supervision of key financial indicators.</p> <p>Monitoring of the impact that the merger between Siemens and Gamesa will have on Iberdrola.</p> |

Noteworthy milestone: Monitoring the integration of Avangrid and the merger between Siemens and Gamesa

Iberdrola's Board of Directors has also devoted a significant portion of its time to dealing with other strategic issues relating to the management of the Group:

Risk supervision and control

The Board of Directors is deeply involved in the supervision of the Group's risks: it monitors the level of risk by means of periodic tracking of the most significant threats.

Identification and analysis of the main risks facing the Group.

Ongoing monitoring of risks with a possible impact on financial year 2016.

Annual revision of the Risk Policies.

Update of the guidelines on risk limits.

Approval of the *Report on Risk Control and Management Systems*.

Noteworthy milestone: Risk Analysis 2016-2020

Director and senior officer remuneration

The Board of Directors has supervised the remuneration model in order to verify that it is consistent with the Company's performance and with shareholder return, thus ensuring the maximisation of long-term value.

Comparative analysis of director remuneration.

Freezing of non-executive director remuneration since 2008.

Establishment of the limit on variable remuneration as well as the targets to which it is linked.

Approval of the fixed and variable remuneration of senior officers for financial year 2016.

Noteworthy milestone: Comparative analysis of director remuneration and supervision of the consistency of the Group's remuneration model.

Corporate governance

Ongoing efforts to identify and implement best corporate governance practices are key pillars for the creation of sustainable value.

Formalisation of the *Mission, Vision, and Values* of the Iberdrola Group as an integral norm of the Corporate Governance System.

Making various improvements designed to encourage shareholder participation in the General Shareholders' Meeting.

Successive amendments to the Corporate Governance System and approval of an *Anti-Corruption and Anti-Fraud Policy*.

Coordination and supervision of the process of evaluation of the Board of Directors.

Review of contacts made by the chairman and the management team with key market players.

Noteworthy milestone: Ongoing improvement of the Corporate Governance System and inclusion of the *Mission, Vision, and Values* of the Iberdrola Group within the Company's set of rules

Social responsibility and sustainability

The Board is committed to maintaining leadership in the fight against climate change, the development of clean energy, and respect for the environment, as well as in the maximisation of the social dividend.

Amendment of various social responsibility and sustainability policies and formalisation of the commitment adopted by Iberdrola in the fight against climate change.

Introduction of new measures to promote gender equality and the reconciliation between professional and personal life.

Approval of incentives to strengthen the Group's commitment to innovation and to a healthier and more egalitarian and just society.

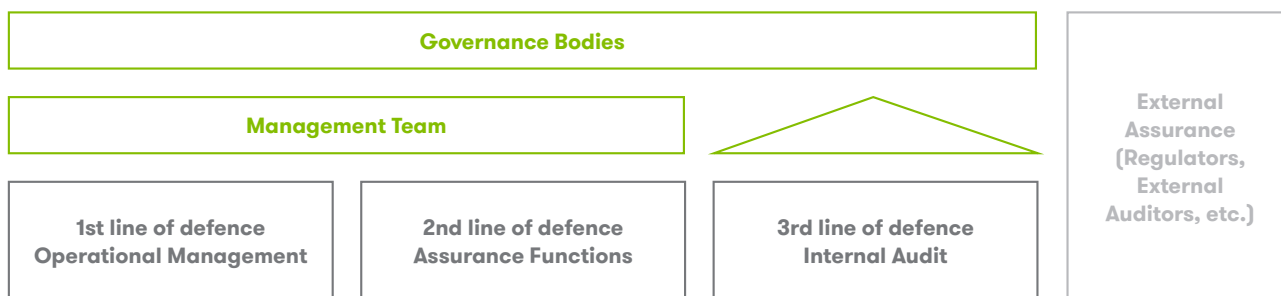
Monitoring the Group's activities in the area of sustainability and the alignment thereof with the main reference bodies.

Noteworthy milestone: Formalisation of commitments relating to the fight against climate change.

5.2 Three Lines of Defence

Three lines of defence model

The Internal Control System of Iberdrola and the companies of its Group is configured by reference to international best practices. It is based on a guarantee combined around three lines of defence, providing a comprehensive view of how the different parts of the organisation interact in an effective and coordinated manner, increasing the efficiency of the processes for management and internal control of the entity's significant risks.



Based on the document "Guidance on the 8th EU Company Law Directive, article 41" ECIIA/FERMA, September 2010.

1st line of defence Operational Management

As the first line of defence, the management team and the professionals of Iberdrola and its Group are the direct managers of the risks of the entity. Thus, the Management of the Company is responsible for maintaining effective control and implementing procedures to control risks on a continuous basis.

Internal Control Objectives (COSO. May 2013)

Operations objectives- Pertain to the effectiveness and efficiency of the entity's operations, including operational and financial performance goals, and safeguarding assets against loss.

Reporting objectives- Pertain to internal and external financial and non-financial reporting and may encompass reliability, timeliness, transparency, or other terms as set forth by regulators, recognised standard setters, or the entity's policies.

Compliance objectives- Pertain to adherence to laws and regulations to which the entity is subject.

© Significant Risks Facing Iberdrola's Primary Businesses
/ pages 48, 52, 56

2nd line of defence Assurance Functions

As the second line of defence, certain functions provide the foundation for the entity's internal control system, proposing guidelines to the Board of Directors and monitoring how the first line of defence implements them.

The primary assurance functions within Iberdrola, within their respective areas of responsibility, are: (i) the Group's Risk Division, within the framework of its functions within the Comprehensive Risk Control and Management System; (ii) the Compliance Unit, which is responsible for the Compliance System; and (iii) the Internal Control Division, which is part of the Administration and Control Division, within its duties relating to the internal control and risk management systems in relation to the preparation of financial information (ICFRS).

Iberdrola adopts the three lines of defence model to ensure effective and integrated management of its Internal Control System.

© Comprehensive Risk Control and Management System
/ page 86

© Compliance Unit
/ page 90

3rd line of defence

Internal Audit

The Internal Audit function, as the third line of defence, proactively ensures the proper functioning of the internal control, risk management, and governance systems, systematically auditing the first and second lines in the performance of their respective duties of management and control.

To ensure its independence, the director of the Internal Audit Area reports hierarchically to the chairman of the Board of Directors and functionally to the Audit and Risk Supervision Committee. The Internal Audit divisions of the various country subholding companies have this same positioning, and are coordinated under the framework of the *Basic Internal Audit Regulations of Iberdrola, S.A. and its Group*.

The 2016 annual activities plans of the Internal Audit Area Division of Iberdrola, S.A. and of the Internal Audit divisions of the Group, with a risk-based focus looking to support the achievement of the Company's goals, responded to the requirements established by the Audit and Risk Supervision Committee of Iberdrola, S.A. and the respective Audit and Compliance Committees of the country subholding companies, and included work for the senior management and the rest of the organisation, including:

- Annual audits of compliance with the *Code of Ethics* at Iberdrola, S.A. and at each of the country subholding companies.
- Audits of the process for determining and monitoring the limits and indicators of the Risk Policies of the Group's businesses.
- Half-yearly reviews of the operation of the most critical controls of the Internal Control Over Financial Reporting (ICFR) System, as well as reviews of the various cycles of preparation of the financial information of Iberdrola, S.A. and the various companies of the Group, within the framework of the general goal of reviewing the entire ICFR over a period of 3 years.

Continuing with the commitment made in 2005, Internal Audit submits to an exhaustive review every five years of compliance with professional internal audit rules (called a Quality Assurance Review) by the Global Institute of Internal Auditors. During the last review in 2015, the certification of Iberdrola, S.A. and of ScottishPower was renewed and the scope of the certification was expanded to include Iberdrola España and Avangrid.

Furthermore, since Internal Audit obtained ISO 9001 certification in 1999, it has continued to renew it through the current version ISO 9001-2008, which is expected to be updated to version ISO 9001-2015 in 2017. This ensures that all of the Group's internal auditors perform duties under the same framework and that such framework is aligned with the international professional rules of the function.

Basic Internal Audit Regulations of Iberdrola, S.A. and its Group

Approved by the Board of Directors of Iberdrola, S.A. upon a proposal of its Audit and Risk Supervision Committee (updated on 15-Dec-2015).

Defines the nature, as an independent internal unit, and establishes the regulation, competencies, powers, and duties of Internal Audit, among other things.

Establishes the framework of relations with: i) the Board of Directors, its Chairman and Committees; ii) the Internal Audit divisions of the other companies of the Group; and iii) the rest of the organisation.

Disseminates the knowledge of the Internal Audit function among the professionals of the Group.

Serves as a reference for the management model and the quality system of the Internal Audit Area of the Company and the Internal Audit divisions of the other companies of the Group.

External assurance

Regulatory bodies and other entities external to the organisation play a significant role in the general structure of governance, internal control, and risks of Iberdrola, especially in the regulated businesses. The regulators establish requirements intended to strengthen the controls of an organisation and perform a function of independent and separate monitoring, and the auditors provide assurance regarding the true and fair view of the entity's financial information. In this regard, the powers of the Audit and Risk Supervision Committee of Iberdrola, S.A. and the Audit and Compliance Committees of the country subholding companies include ensuring the preservation of the independence of the auditors in the performance of their duties.

© Regulatory Environment
/ page 44

© Audit Report on the Consolidated
Financial Statements

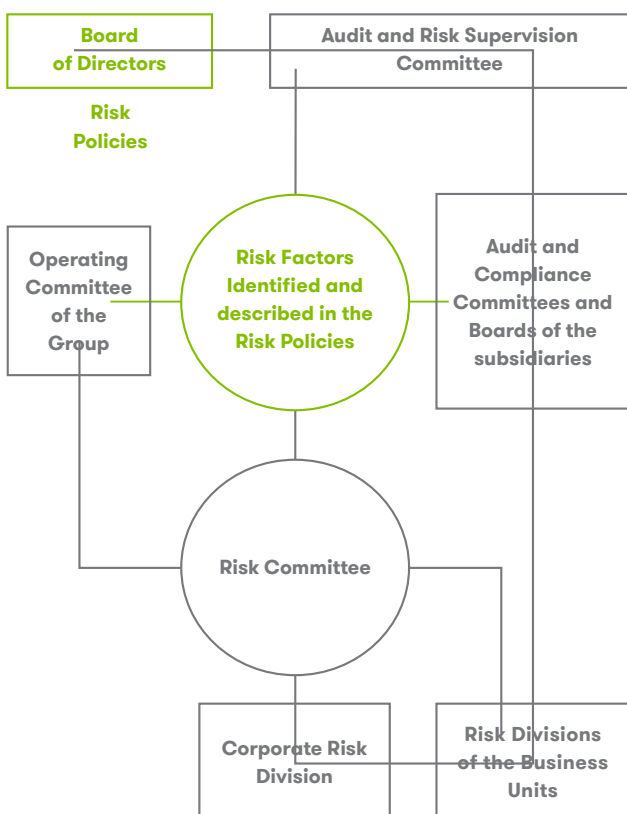
5.3 Risks

The essential elements of proper risk management are foresight, independence, and commitment to the business objectives of the Group.

Commitment of the Board of Directors and of senior management

Iberdrola's Board of Directors and senior management is strongly committed to and engaged in the management of the Group's risks:

- **Ex-ante:** acceptable levels of risk tolerance are reviewed and approved on an annual basis through risk policies and limits that establish the qualitative and quantitative risk appetite at the Group level and at each of the main businesses.
- **Ex-post:** periodic monitoring of significant risks and threats and the various exposures of the Group, as well as of compliance with the approved risk policies, limits, and indicators.



Comprehensive Risk Control and Management System

The *General Risk Control and Management Policy* of the Group approved by the Board of Directors establishes the mechanisms and basic principles for appropriate management of the risk/opportunity ratio, at a risk level that makes it possible to:

- Attain strategic goals with controlled volatility.
- Provide the maximum level of assurance.
- Protect the results and reputation of the Group.
- Defend the interests of the Stakeholders and guarantee the business stability and financial strength of the Group.

At the operational level, the Comprehensive Risk Control and Management System is structured around a Risk Committee and an independent specialised Risk Division that analyses and quantifies the risks within the main businesses of the Group.

Duties of the Risk Division

Centralised Approach – Active Management

Credit risk. Approval of counterparties and limits and/or establishment of admission criteria in order to minimise credit losses within the Group.

Market risk. Approval of detailed limits in order to delimit the effects of volatility in the markets in which the Group operates.

ERM* Approach – Integrated Vision

Ensure that the Group's significant risks are adequately identified, measured, managed, and controlled and that they are periodically reported to the various committees.

- Instruments and reports:
- Risk policies and risk limits and indicators.
 - Quarterly report on key risks.

Operational risk is managed through insurance and participation in the Group's information technology governance and cybersecurity committees.

(*) ERM: Enterprise Risk Management.

Risk policies and limits of the Iberdrola Group

The Group's Risk Policies are approved by the Board of Directors on an annual basis.

The country subholding companies of the various countries develop and approve their own policies through their Boards of Directors.

General Risk Control and Management Policy.

Specific risk policies for the various businesses of the Group:

- Risk Policy for the Liberalised Businesses of the Iberdrola Group.
- Risk Policy for the Renewable Energy Businesses of the Iberdrola Group.
- Risk Policy for the Networks Businesses of the Iberdrola Group.
- Risk Policies for the Engineering and Construction Businesses.
- Risk Policies for the Real Estate Businesses.

Corporate risk policies:

- Corporate Credit Risk Policy.
- Corporate Market Risk Policy.
- Operational Risk in Market Transactions Policy.
- Insurance Policy.
- Investment Policy.
- Financing and Financial Risk Policy.
- Treasury Share Policy.
- Risk Policy for Equity Interests in Listed Companies.
- Reputational Risk Framework Policy.
- Procurement Policy.
- Information Technologies Policy.
- Cybersecurity Risk Policy.



ERM management system

- Strategic positioning towards risk.
- Responsibilities to manage risk.
- Proactive and preventive actions.
- Quantitative and qualitative limits.
- Quarterly report on risk limits.

Principal risk factors of the Iberdrola Group

The Group is exposed to various risks inherent in the different countries, industries, and markets in which it operates, and which may prevent it from achieving its objectives and implementing its strategies. These risks, which are set out in the risk policies, are:

Credit risks: possibility of contractual breach by a counterparty, causing economic or financial losses.

Market risks: exposure to volatility in variables like prices of electricity and other energy commodities, exchange rate, interest rate, etc.

Business risks: deriving from the uncertainty of the behaviour of variables intrinsic to the business, characteristics of demand, climatology, etc.

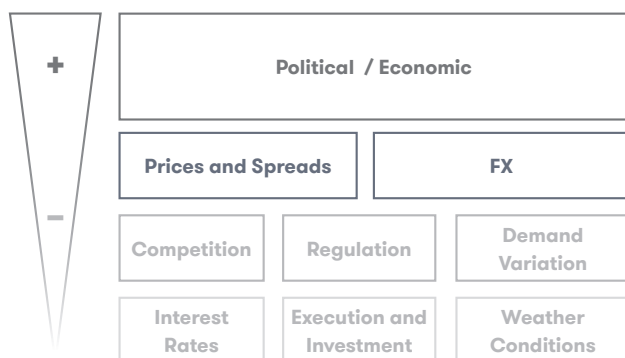
Operational, Technological, Environmental, Social, and Legal Risks: economic losses resulting from inadequate internal procedures, technical failures, human errors, etc.

Political and regulatory risks: coming from regulatory changes made by the regulators that can affect remuneration of the regulated businesses, environmental or tax provisions, etc.

Reputational risks: potential negative impacts on the Company arising from performance below the expectations of its Stakeholders.

Corporate governance risks: those that endanger the corporate interest and strategy of the Company.

Integrated Risk Analysis - Plan 2016-2020



Main sources of risk

The political/economic uncertainty of the countries in which the Iberdrola Group maintains a presence, which is difficult to quantify, represents the main source of risk due to its impact on key variables such as exchange rate, interest rate, regulatory changes, etc.

The prices of commodities and their impact on electricity prices represent the second source of risk for the Group.

Impact on Ebitda by business

| Average annual EBITDA share '17-'20 | Risk as % of annual EBITDA '17-'20 |
|-------------------------------------|---|
| 20% | Wholesale and Retail Business 4.5% - 5.5% |
| 23% | Renewables Business 1.0% - 1.5% |
| 57% | Regulated Business* 1.0% - 1.5% |

(*) Networks & Mexico

Due to its intrinsic nature, despite representing only 20% of Ebitda, the Wholesale and Retail Business holds the greatest proportion of at-risk Ebitda for the period 2017 – 2020, amounting to between 4.5 and 5.5%. The various risk profiles of the businesses are as follows:

Wholesale and Retail Business: The main variable that affects the Group's results is the price of electricity, which is closely correlated to the price of the fuel used to produce it. These risks are mitigated by offsetting at-risk positions between wholesale and retail activities, by diversifying purchase/sale agreements and the specific clauses thereof, and by trading in derivatives.

Renewables Business: Risks deriving from the Renewables Business, mainly the uncertainty of wind resources and the established remuneration systems, are mitigated via:

- The wide geographical spread of the large number of available windfarms.
- The various regulatory frameworks aimed at fostering the development of renewable energy, based on formulas that can include premiums, green certificates, tax deductions, or regulatory tariffs that allow investors to obtain an appropriate and reasonable return.

Regulated Businesses: The regulation applicable to the Networks Businesses of each of the countries in which the Group operates establishes periodically updated frameworks that ensure a reasonable and predictable return. These frameworks provide incentives and penalties for efficiency, quality of service, and potentially for management of bad debts, with a minor and insignificant overall impact.

In Mexico, the Iberdrola Group sells most of its electricity production through long-term, fixed-price contracts to the Federal Electricity Commission (*Comisión Federal de Electricidad*) (CFE), and the rest of its production to private customers at prices indexed to the CFE rate.

Risk factors and mitigation measures

Greater detail is offered below regarding the main risk factors for the income statement of a specific financial year and the main measures of mitigation to address them.

The activities carried out by the Group are subject to various market, business, credit, operational and regulatory risks, arising out of the uncertainty of the main variables that affect them, including: changes in the price of commodities; changes in hydroelectric and wind production (both internal and external); change in demand for electricity and gas; and availability of the plants.

| | | | |
|---|---|--|--|
| Changes in the price of electricity | The main variable affecting the results of the Group's Wholesale and Retail Businesses and Renewables Businesses as regards market prices is the price of electricity, which bears a close correlation to the price of fuel and applicable emission rights, required to produce such electricity. | | |
| Changes in the prices of energy commodities | Offsetting at-risk positions between wholesale and retail activities allows for a large reduction in the Group's market risk; the remaining risk is mitigated via diversification of purchase/sale agreements and the specific clauses thereof, and by trading in derivatives. | | |
| Profit margin | The Group's Renewables Businesses preferentially sell their energy at: i) regulated tariff; or ii) fixed price via long-term power purchase agreements (PPAs). The remaining market exposure of the Spain and United Kingdom Renewables Businesses is transferred to the Wholesale and Retail Business of such countries. | | |
| | Possible impact of a 5% change in the price of electricity and/or of energy commodities and CO ₂ | Wholesale and Retail Business - Spain - United Kingdom - Mexico United States Renewables Business | ● Includes the exposure of the Spain Renewables Business (windfarms prior to 2014) ● Includes the exposure of United Kingdom Renewables Business (component of energy farms subject to ROCs). ● Long-term agreements with the CFE ⁽¹⁾ have no market risk ● Includes 33% risk for windfarms without long-term sales agreements |
| Change in hydroelectric resources Spain | In the long term, wet years compensate for dry years. In the short-to-medium term, the storage capacity of hyperannual reservoirs and the Group's portfolio of power plants mitigate the level of volatility of the annual results. | Possible impact of lower hydroelectric production ^(*) <i>(*) Corresponding to dry year, followed by two dry or semi-dry years.</i> | ● Spain Wholesale and Retail Business |
| Change in wind resources of the Group | The geographical spread of the Iberdrola Group's windfarms mitigates the annual volatility of wind production at the Group level and its possible impact on results for a specific year. | Possible impact of lower wind production | ● Group Renewables Business |
| Change in demand | Higher or lower growth in annual demand has a moderate short-term impact on the Group's results, given the characteristics of the Group's generation facilities and the structure of the long-term power purchase agreements (PPAs). | Possible impact of 1% reduction in demand | ● Spain Wholesale and Retail Business ● United Kingdom Wholesale and Retail Business |
| Change in interest rate | In order to mitigate this risk, the Iberdrola Group maintains a fixed-rate and variable-rate debt structure, based on the structure of its revenues and the sensitivity thereof to changes in interest rates. | Possible impact on financial cost of +25 basis point increase | ● Group financial cost |
| Change in exchange rate | The Group mitigates this risk by taking on debt and carrying out all its financial flows in the functional currency corresponding to each company, whenever possible and economically efficient, managing its open positions with financial derivatives. The risk associated with the translation of expected results from subsidiaries in a currency other than the euro is closed out annually. | Possible impact on financial cost of 5% increase in currency | ● Group financial cost |
| Credit risk | This risk is appropriately managed and limited based on the type of transaction and the credit standing of the counterparties. As regards credit risk corresponding to accounts receivable for retail activity, late payments/defaults have been kept to moderate levels, close to 1% of the total invoicing for this activity. | | |
| Operational risk | These risks are mitigated by making the necessary investments, applying operation and maintenance procedures and programmes (supported by quality systems), planning appropriate training and skills development for staff, and finally by obtaining appropriate casualty and civil liability insurance. | | |
| Regulatory and political risk | The Group is subject to laws and regulations on tariffs and other regulatory aspects of its activities in the countries in which it does business. The introduction of new laws/regulations or amendments to existing ones could adversely affect operations, annual results and the financial value of the businesses of the Group. | | |

(1) CFE: Federal Electricity Commission (Comisión Federal de Electricidad)

● <15 M€ ● 15-50 M€ ● >50M€

5.4 Ethics and Social Responsibility

Compliance Unit

Iberdrola has a Compliance Unit, as a collective, internal, and permanent body linked to the Corporate Social Responsibility Committee of the Board of Directors.

There are also Audit and Compliance Committees at the level of each country subholding company and/or head of business company. Their duties including promoting a culture of ethical behaviour and zero tolerance for the commission of unlawful acts or fraud. Iberdrola's Compliance System is made up of the substantive rules, formal procedures, and major activities within the Group to encourage the organisation to act in accordance with applicable ethical principles and legal provisions, through a set of procedures and actions designed to prevent, detect, and react to irregular actions, fraud, or actions contrary to the Iberdrola Group's Code of Ethics or applicable laws and regulations.

Main activities in the area of ethics and compliance

Various programmes and control mechanisms for different regulatory environments are implemented at the Group within the framework of the Compliance System.

These include the crime prevention programmes, which are implemented within the framework of the process of reviewing and adapting the duties imposed by the Spanish Criminal Code, without prejudice to the legal provisions applicable in any other jurisdiction in which the Company does business, as well as the programme for compliance with the *Code of Ethics*, which includes specific training and communication plans for all professionals of the Group, among other things.

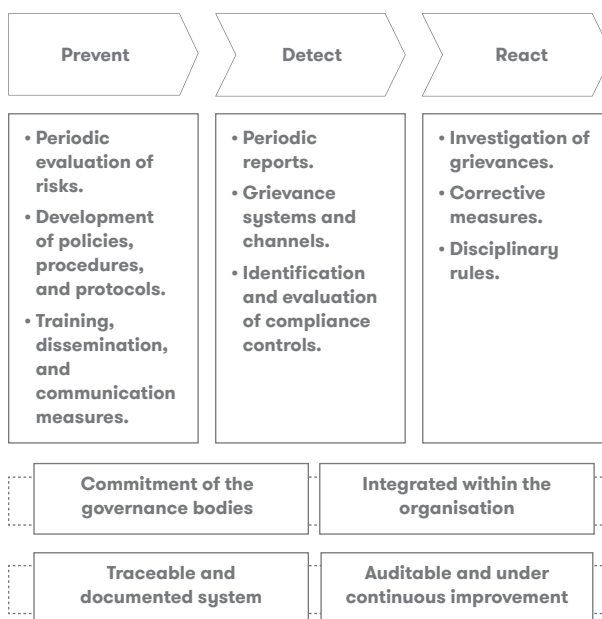
Iberdrola also has a Compliance Unit Office (the "Office"), managed by the Compliance Director and made up of members representing the various areas that form the

Compliance System. All functions that are entrusted with powers relating to compliance are coordinated through the Office, which ensures the effective functioning of the Compliance System as a whole.

Powers of the Unit

The Compliance Unit has powers related to the *Code of Ethics*, the *Anti-Corruption and Anti-Fraud Policy*, the *Crime Prevention Policy*, the *Internal Regulations for Conduct in the Securities Markets*, legal provisions regarding the separation of activities, and all other powers that may be entrusted thereto by the Corporate Social Responsibility Committee or the Board of Directors of the Company or that are established in Iberdrola's Corporate Governance System.

The Iberdrola Group's compliance system



Principal awards

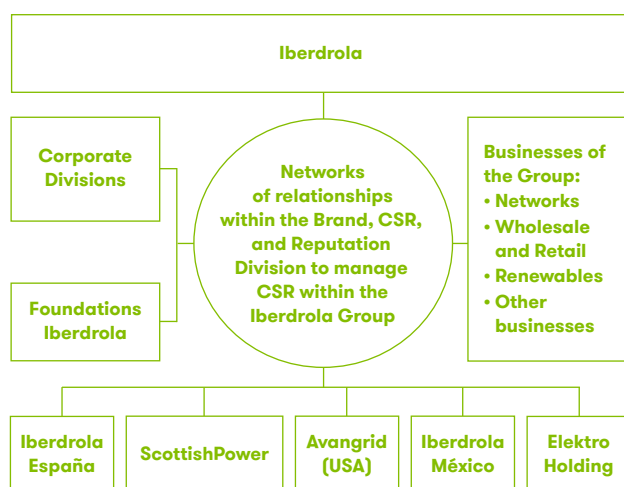
Iberdrola has been chosen for the fourth consecutive year as one of the most ethical companies in the world, according to the *World's Most Ethical Companies* ranking prepared by the *Ethisphere Institute*. This

Iberdrola considers its corporate values to include ethical principles, good corporate governance and transparency, and social commitment.

ranking recognises organisations that are committed to ethical leadership and behaviour at the corporate level.

NYSE Governance Services, together with the Ethisphere Institute, also awarded the “Compliance leader verification” certification to Iberdrola in 2015.

Organisation of social responsibility within the Group



The Iberdrola Group has an organisational structure designed to promote and manage responsible actions with its Stakeholders. The Corporate Social Responsibility and Reputation Committee and the CSR and Reputation Committees of the country subholding companies coordinate the balanced development of social responsibility within the Iberdrola Group. The CSR Committee of the Board of Directors performs the duties of supervision within its purview.

CSR plans of the Group

2015 saw the approval of the *CSR 2015-2017 Plan* for the Iberdrola Group, covering five areas of activity (dialogue with local communities, measurement tools, etc.), with a focus based on the various Stakeholders.

The CSR Plan is made up of various programmes, projects, and monitoring indicators, both cross-sectional for all involved organisations of Iberdrola as well as specific

for each business or corporate area of the Company.

Monitoring of the Plan is analysed on a half-yearly basis by the Corporate CSR and Reputation Committee and by the CSR Committee of the Board of Directors.

External awards

2016 world leader in utilities sector, with 91 points. Selected in all prior years.



Selected in 2017. Only Spanish electric company among the 100 most sustainable companies in the world.



First utility with nuclear assets to meet standards, selected for 6 years in a row.



A-list, the highest category.



Iberdrola a sponsor.



Iberdrola selected AAA.



Iberdrola selected.



Qualified as “Gold Class” in the electricity sector.



First Spanish utility and fifth worldwide.



Leader among Spanish utilities: electricity, gas, and water.



Iberdrola selected



Iberdrola among top 25 scoring companies.



Iberdrola shareholders during
a virtual reality demonstration
at Iberdrola Tower

© Antonio Triviño





About this Report

This report, which Iberdrola directs to both its shareholders and investors and all of its Stakeholders, has been prepared under the innovative “integrated report” concept, and constitutes one more example of the Group’s desire to be innovative in the area of transparency.

6.1 About this Report

Integrated report

- This report has been prepared in accordance with the reporting framework published by the International Integrated Reporting Council (IIRC) and in accordance with the recommendations thereof, taking into consideration the individual and consolidated financial statements of the Company formulated by the Board of Directors, audited and pending approval by the shareholders at the General Shareholders' Meeting of Iberdrola.
- A multi-disciplinary team made up of corporate businesses and areas of the Group was created in order to provide a complete view of the Company, its business model, the challenges and risks it faces, and its social, environmental, financial, and governance performance. The participating organisations guarantee the completeness of the information included.
- This content of this document has been reviewed by the Company's Operating Committee. It has also been reported on favourably by the Corporate Social Responsibility Committee, which has submitted the report to the Board of Directors for its final consideration. Based on all of the foregoing, the Board of Directors has approved this *Integrated Report February 2017* at its meeting of 21 February 2017.

Information boundaries

- The information submitted covers Iberdrola and its subsidiaries and affiliates. The information boundaries are defined in the Group's consolidated annual financial statements and *Sustainability Report*.
- The Group's performance in recent years is connected to external corporate transactions and internal management decisions, which the reader should take into account in order to properly interpret this report. These transactions and activities are described in the Group's public information, the following being particularly noteworthy:
 The application of IFRS 11 to the 2013 to 2016 figures, which mainly affects Brazil.
 The integration of UIL Holdings Corporation into Iberdrola USA (December 2015), which is now called Avangrid, a company listed on the New York Stock Exchange and the country subholding company of the Group in the United States.

This report has been prepared in accordance with the reporting framework published by the International Integrated Reporting Council (IIRC).

Material aspects identified

- Iberdrola has channels of communication and dialogue with its Stakeholders, developed in accordance with the principles of the AA1000 Assurance Standard, as described in detail in the *Stakeholder Relations Policy* and in the *Sustainability Report*.
- The Company also performs materiality analyses that help identify matters of significance to its Stakeholders, bringing to light particularly sensitive financial, environmental, or social issues related to the business in the various communities and geographic areas in which the Group operates.
- The contents of this report have been selected by taking into account the existing channels for dialogue as well as the materiality analyses and the framework defined by the IIRC for this kind of information.

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Internal and external verification

- This report has been subject to a process of internal verification, by means of a limited review performed by the Management of the Internal Audit Division of Iberdrola.
- Although it has not been subject to a process of independent external verification, a significant portion of the information contained herein relating to financial year 2016 and to previous years comes from annual financial reports and sustainability reports, all of which have been the subject of an external audit or verification for which the respective certificates are available. The remaining information comes mainly from other reports or public presentations made by the Company.

