Report on the Group’s business performance and the economic situation

The current business year 2014/15 began with a quite optimistic economic climate for the mature economies and mixed expectations for the emerging markets. However, in the course of the first six months of the business year, it became increasingly clear that—with the exception of North America and China—the global economic trend does not have sufficient momentum for a broad upswing.

While of the European countries, Great Britain and Poland demonstrated considerable economic strength, as the year continued, the eurozone was characterized by an increasingly difficult economic environment. The satisfactory growth trend in the early part of the year lost much of its impetus over the summer months. Especially the unexpected downturn of the German economy, primarily the perceptible decline of the construction industry, put increasing pressure on the eurozone, especially considering the recessive developments in Italy and France. While these two countries continue to suffer from a low level of business investment and weak exports, due particularly to the marginal progress in implementing structural reforms, the mood in the European economic regions, which have been more robust thus far, has soured, not least as a result of increasing geopolitical crises that have been unfolding.

Only Spain, which has stayed on its course of reform consistently, has been able to avoid the negative trend and accelerate its growth, although starting from an extremely modest level. Viewed overall, the long-term recovery in Europe continues to be inconsistent, slow, and fragile.

In North America, however, the first half of the current business year saw a continuation of robust and broad-based growth, with both private consumption and industrial investments and exports continuing to demonstrate an upward trend with concomitant welcome developments on the labor market and in the market sentiment indicators. At this time, there are no signs that this positive trend is reversing; North America has clearly undertaken the role of global economic locomotive.

Brazil, the most important economic region in South America for the voestalpine Group, on the other hand, slipped into a recession in the spring of 2014; at this time, the prospects for a return to the growth rates of an emerging economy are slim.

The situation in Russia is also increasingly difficult; a resolution of the disputes with the Ukraine is a prerequisite for a return to satisfactory growth.

In Asia, China’s economic development got underway slowly in the early part of the year, however, during the spring, it was able to continue the previous year’s trend, due mainly to significantly increasing exports. However, the efforts of the central government to entrench private consumption as a stable pillar of sustainable economic growth have not yet produced the desired result. Nevertheless, China is expected to experience economic growth of more than 7% in 2014.

In this very inconsistent macroeconomic environment, during the first half of the business year 2014/15, operational business performance of the voestalpine Group’s four divisions was largely stable.

The Steel Division, which is active mainly on the European market, profited from continuing high demand from the automotive sector and a recovery in the sector of oil and natural gas transport (pipeline projects). Demand maintained a mostly stable trajectory in the early part of the year, but it waned somewhat over the course of the summer months.
The Special Steel Division profited from the prospering markets in the USA and Asia, while the European market was generally subdued over the course of the first six months of the current business year.

The Metal Engineering Division continued its positive development. Due to its broad-based positioning and a continuing satisfactory level of demand in practically all business units in the first half of the 2014/15 year, its performance is stable at a high level.

In the Automotive Parts business segment, the Metal Forming Division continued its very good performance, however, since the early part of the business year, it has faced a subdued market in Europe for tubes and sections.

Overall, the performance of the voestalpine Group in the first half of the business year 2014/15 has been at a satisfactory level despite an increasingly challenging economic environment in Europe.

Report on the financial key performance indicators of the voestalpine Group

At −1.5%, from EUR 5,643.4 million in the first half of 2013/14 to EUR 5,561.1 million in the first six months of the business year 2014/15, the voestalpine Group’s revenue this year was down slightly. The sole reason for the dip was the closure of the standard rail production in Duisburg as of the end of 2013 and the resulting decrease in the Metal Engineering Division’s delivery volume. In contrast, all other divisions in the Group boosted their revenue. The weaker level of prices, which is due to raw materials and pre-material costs that continue to fall, had an overall negative impact on revenue in the first half of 2014/15.

At EUR 756.9 million, the operating result (EBITDA), which was markedly higher in the current business year by 11.2%, includes non-recurring effects in the Metal Forming Division totaling EUR 66.5 million due to the sale of the Flamco Group in August 2014, the agreement executed in late September 2014 to sell the automotive companies voestalpine Polynorm Van Niftrik B.V. and voestalpine Polynorm Plastics B.V., and the structural reorganization of pension obligations in individual companies in the Netherlands, which are part of the Metal Forming Division, also in the second quarter of 2014/15. Adjusted for these non-recurring effects, EBITDA rose by 1.5% from EUR 680.4 million in the previous year to EUR 690.4 million this year; as a result the (adjusted) EBITDA margin went up from 12.1% to 12.4%. The (unadjusted) profit from operations (EBIT) rose by 12.2% from EUR 396.3 million to EUR 444.7 million. Adjusted by the non-recurring effect of EUR 45.2 million due to the one-time effect detailed above and reduced by a write-down of individual assets that are not part of the core business, EBIT came to EUR 399.5 million in the first half of 2014/15, which corresponds to an increase of 0.8%. The adjusted EBIT margin was therefore at 7.2% (previous year: 7.0%). With the exception of the Metal Engineering Division, which, however, still remains the strongest division in terms of margins, all of the divisions reported a gain in both operating result and profit from operations in the first half of 2014/15.

Although gross financial debt increased as of the reporting date of September 30, 2014, due primarily to the reclassification of the hybrid bond 2007 from equity to borrowed capital, interest charges were significantly reduced. Recognition of the entire hybrid bond 2007 as part of borrowed capital became necessary as a result of the resolution adopted by the Management Board of voestalpine AG in September 2014 to call the entire issue of this bond as of the first possible call date, i.e., October 31, 2014. Interest charges declined primarily because interest rates fell considerably in a year-to-year comparison; as a result, the improvement in the profit before tax of 25.5% from EUR 312.1 million to EUR 391.7 million was very substantial. After deduction of the non-recurring effect of EUR 45.2 million due to the one-time effect detailed above and reduced by a write-down of individual assets that are not part of the core business, EBIT came to EUR 346.5 million or 11.0% above the previous year’s figure.

Profit for the period gained 35.9%, going from EUR 238.4 million to EUR 324.0 million. Without taking the non-recurring effects (EUR 43.4 million) into account, the adjusted profit for the period is EUR 280.6 million, also an improvement compared to the previous year of 17.7%. This is a result of the increase in profit before tax and a decrease of the tax rate. Thus, earnings per share were EUR 1.65 in the first six months of the current business year, a sharp rise of +43.5%
compared to the previous year’s figure of EUR 1.15. The adjusted earnings per share for the first half of 2014/15 were EUR 1.40 or 21.7% higher than last year’s figure.

As of September 30, 2014, equity fell year-to-year by 2.6%, going from EUR 5,062.3 million to EUR 4,931.5 million. Compared to the reporting date of March 31, 2014 (EUR 5,261.0 million), equity fell by 6.3%. This decline is largely due to the previously described reclassification of the hybrid bond 2007, which was called in September 2014, from equity to borrowed capital totaling EUR 500 million as of September 30, 2014 as well as dividend payments amounting EUR 170 million in the second quarter of 2014/15. As a result of the early redemption of the hybrid bond 2007, net financial debt went up year-to-year by 22.4% from EUR 2,368.3 million (adjusted retroactively) to EUR 2,898.8 million. Compared to the reporting date of March 31, 2014 (EUR 2,421.4 million, adjusted retroactively), there was an increase of 19.7%. Due to these changes in the Group’s financing structure, the gearing ratio (net financial debt in percent of equity) rose in the first six months of the business year 2014/15 from 46.0% to 58.8%.

As of September 30, 2014, the voestalpine Group had 47,379 employees (FTE); this corresponds to an increase of 0.5% compared to the figure of 47,126 employees (FTE) twelve months ago.

### Comparison of the quarterly and six-month figures of the voestalpine Group

<table>
<thead>
<tr>
<th></th>
<th>Q1 2013/14</th>
<th>Q1 2014/15</th>
<th>Q2 2013/14</th>
<th>Q2 2014/15</th>
<th>H1 2013/14</th>
<th>H1 2014/15</th>
<th>Change in %</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenue</strong></td>
<td>2,895.3</td>
<td>2,826.7</td>
<td>2,748.1</td>
<td>2,734.4</td>
<td>5,643.4</td>
<td>5,561.1</td>
<td>–1.5</td>
</tr>
<tr>
<td><strong>EBITDA</strong></td>
<td>363.5</td>
<td>363.7</td>
<td>316.9</td>
<td>393.2</td>
<td>680.4</td>
<td>756.9</td>
<td>11.2</td>
</tr>
<tr>
<td><strong>EBITDA margin</strong></td>
<td>12.6%</td>
<td>12.9%</td>
<td>11.5%</td>
<td>14.4%</td>
<td>12.1%</td>
<td>13.6%</td>
<td></td>
</tr>
<tr>
<td><strong>EBIT</strong></td>
<td>221.6</td>
<td>218.4</td>
<td>174.7</td>
<td>226.3</td>
<td>396.3</td>
<td>444.7</td>
<td>12.2</td>
</tr>
<tr>
<td><strong>EBIT margin</strong></td>
<td>7.7%</td>
<td>7.7%</td>
<td>6.4%</td>
<td>8.3%</td>
<td>7.0%</td>
<td>8.0%</td>
<td></td>
</tr>
<tr>
<td><strong>Profit before tax</strong></td>
<td>175.0</td>
<td>192.9</td>
<td>137.1</td>
<td>198.8</td>
<td>312.1</td>
<td>391.7</td>
<td>25.5</td>
</tr>
<tr>
<td><strong>Profit for the period</strong></td>
<td>137.6</td>
<td>154.4</td>
<td>100.8</td>
<td>169.6</td>
<td>238.4</td>
<td>324.0</td>
<td>35.9</td>
</tr>
<tr>
<td><strong>Employees</strong></td>
<td>46,548</td>
<td>47,463</td>
<td>47,126</td>
<td>47,379</td>
<td>47,126</td>
<td>47,379</td>
<td>0.5</td>
</tr>
</tbody>
</table>

1 Business year 2013/14 retroactively adjusted due to the application of IFRS 11 “Joint Arrangements” and due to the change in the method of disclosure for results of entities consolidated according to the equity method (formerly reported as part of financial result, from April 1, 2014 onward, reported as part of EBIT). Further details are described under “General information/Accounting policies.”

2 Before deduction of non-controlling interests and interest on hybrid capital.
EBIT was at EUR 40.1 million, 10.5% less than the immediately preceding quarter. The EBIT margin went down from 7.4% to 6.9%.

As of September 30, 2014, the Metal Forming Division had 10,921 employees (FTE). This figure is 2.4% lower than the figure on the same date of the previous business year and 4.3% less than as of the end of the last business year (11,416). The decline in headcount is primarily due to the sale of the Flamco Group in August 2014.

**Business transactions with associated companies or parties**

Information regarding business transactions with associated companies and parties is available in the Notes.

**Investments**

In order to ensure the leading position of the voestalpine Group both with regard to quality and technology and to implement its growth strategy, its investment activities in the first half of the business year 2014/15 remained at a continuously high level. At EUR 427.1 million, they matched the magnitude of last year’s investments (EUR 429.9 million) almost exactly. However, while the Steel and Special Steel Divisions (temporarily) reduced investment volume in the first six months of 2014/15, the other two divisions (Metal Engineering and Metal Forming Divisions) increased their investment expenditure in comparison to the previous year.

Investment activity in the Steel Division declined in the first half of 2014/15 by 16.3% from EUR 226.1 million to EUR 189.3 million. Current projects were focused on increasing efficiency of production processes and on continued improvement of the product portfolio. In accordance with the policy of consistent cost optimization in the liquid phase, installation of coal injection systems in all three blast furnaces in Linz, Austria, will be completed by the spring of 2015. Productivity improvement also includes the construction of the direct reduction plant in the USA, where all necessary permits and approvals have now been obtained; construction began in the early part of the second quarter. In the interest of continuing accelerated enhancement of product quality, initial measures have been taken to expand the capacity of the secondary metallurgy systems in the steel mill. The new facilities (vacuum system, ladle furnace) are expected to be ready in the fall of 2015. Construction of the new heavy plate rolling stand is already well underway; it is scheduled to start up operation in the 2015 calendar year.

In the first half of 2014/15, the Special Steel Division undertook investments totaling EUR 58.1 million, 22.3% less than in the same period of the previous year. The expertise in the high-tech coating of tools that was acquired by the takeover of the Eifeler Group in the business year 2012/13 is being gradually rolled out globally. As of the beginning of this business year, a new, coating facility that is appropriate for the operation’s needs was launched in Shanghai, China. On-site coating has now been added to the production of sophisticated special steel as well as its processing and heat treatment. Similar concepts are currently being realized at other locations (including Poland and Taiwan). In the Value-Added Services business segment, the range of service offerings was expanded during recent months as planned, thus solidifying and reinforcing the Group’s position as a global premium service provider in the toolmaking segment. For example, a new heat treatment facility in Düsseldorf, which has one of the largest blast furnaces worldwide, was put into operation. This investment enables voestalpine to provide the automotive industry with tool steel that is used for the forming of press-hardened steel plates. In Turkey, a new service center was opened in September 2014 near Istanbul; it will also provide heat treatment processes for this growth market.

The Metal Engineering Division laid out EUR 87.8 million for investments in the first half of 2014/15, which corresponds to an increase of 58.8% over the previous year’s figure of EUR 55.3 million. As far as magnitude is concerned, the largest single project is the construction of a new...
wire rod mill in Donawitz, Austria. This investment will enable the Wire business segment to differentiate itself even more significantly from its competition as far as quality is concerned. In the Rail business segment, a new walking beam furnace will be in place starting in the 2016 calendar year; it will enable both an increase of the throughput and a reduction in energy consumption. An interim repair of one of the two blast furnaces at the site in Donawitz, Austria, was performed in the spring of 2014; this work was carried out as scheduled without impacting customers (advance production and external sourcing of materials).

In the Metal Forming Division, at EUR 88.1 million, investments in the first six months of the current business year were 25.3% above the previous year’s level (EUR 70.3 million). As was the case in the past business year, focus is on consistent implementation of the internationalization strategy in the segment of automotive components made of press-hardening steel (“phs-ultraform”) based on new technology. In the Automotive Body Parts business segment, new production sites in the USA, South Africa, and China have been successfully launched. The production speed of press-hardened components in Germany was optimized by using new approaches to better supply the quantities required by automotive customers. Another project focused on “phs-ultraform” is currently being planned for Shenyang, a new location in China. In the Tubes & Sections business segment, a new plant was also put into operation in China; it is geared to producing special sections for the construction machinery and agricultural machinery industries.

**Employees**

As of the reporting date of September 30, 2014, worldwide the voestalpine Group had 47,379 employees (full-time equivalent, FTE). This is a slight rise compared to the same quarter of the last business year (47,126) by around 0.5% or 253 employees (FTE).

The number employed as temporary staff was 4,605 employees (FTE), corresponding to an increase of 100 employees (FTE) or 2.3% compared to the end of the second quarter of the business year 2013/14.

As of the reporting date of September 30, 2014, 1,646 apprentices were being trained in the Group, an uptick of 31 young people and 2% more than in the previous year (1,615).

**Research and development**

In accordance with the Group’s decentralized R&D strategy, activities in the Research & Development sector are located at various sites within the Group. Despite the fact that development centers are geographically centered in Europe, employees, particularly those working in the area of process development, are being trained for worldwide deployment in order to be able to handle country-specific customer requirements. For example, as locations in North America are currently being expanded, processing expertise is being transferred there in accordance with local requirements in the interests of further development at the individual sites.

The Group project “KW50+” is currently the subject of particular focus, where know-how and process development for the production of components made of new materials for low-carbon steam power plants are being advanced across multiple divisions. CB2, a highly temperature-resistant casting material, has now been introduced successfully on the market and the appropriate welding process qualification has already been completed. The pilot production of components made of nickel-based alloys as well as development of processes for seam welding of dissimilar metals (nickel-based alloys with steel) have been successful.

The Special Steel Division, which has R&D sites in Austria, Germany, Sweden, and Brazil, is currently focusing on the further development of high-performance tool steel, special materials for the oil and natural gas industries, energy production, and the aviation industry. In addition to pure materials development, the current R&D portfolio also includes development of groundbreaking processing technologies and the development of
new products for the aviation industry as well as innovative hard coatings for tools including the coating facilities needed for these processes. In the Metal Engineering Division, DOBAIN®, the tear-resistant, bainitic brand of rail steel, is being intensively tested in Europe on various test tracks. Due to its cold resistance, it offers additional safety when used at extremely low temperatures. A newly developed type of rail steel for the tram segment, which has improved welding and wear properties, has been introduced on the market and has already proven to be very successful.

Under “HORIZON 2020,” the new EU Framework Program for Innovation and Research, voestalpine is participating in the “SPIRE” and S2R programs. SPIRE (Sustainable Process Industry through Resource and Energy Efficiency) is an initiative of energy-intensive industries with the aim of creating new, cross-sector energy- and resource-efficient process solutions. S2R (Shift to Rail) has the objective of increasingly shifting freight transport volume from road to rail. The Metal Engineering Division is participating in this project as part of VVAC (Virtual Vehicle Austria Consortium) with new and improved products.

Environment

Climate and energy policy 2030
On October 23, the European Council in Brussels agreed on the climate and energy policy framework for the period up to 2030: energy savings (indicative) of at least 27% (instead of the originally planned 30%), an increase in the percentage of renewable energies to at least 27%, and a decrease in CO₂ emissions of at least 40%, all compared to 1990 figures. For industries covered by the emissions trading system (i.e., including the steel industry), an emissions reduction of 43% compared to 2005 was set.

The number of certificates available for auction under the emissions trading system will be reduced; an annual linear reduction of 2.2% (rather than the previously defined 1.74%), starting in 2021. In the future, there will be a reserve of pollution rights (2% of the number of certificates) for “poorer” EU nations who face particularly high modernization costs. One method of covering these costs is to auction off such “reserve certificates.” Furthermore, existing funding for innovation will be increased from 300 to 400 million certificates; in the future, business investments in low-carbon measures will also qualify for funding, rather than only receiving funding for low-carbon research as had previously been the case.

The following measures were defined to protect energy-intensive industries in the emissions trading system: the free allocation of certificates remains in effect, the benchmarks for free allocation will be reviewed periodically, taking “technological progress” into consideration in individual sectors. Taking both direct and indirect costs into account, the most efficient facilities in a sector should not be burdened by undue costs which encourage relocation of industries to other regions (“carbon leakage”). This is positive in principle, but it is questionable how the word “undue,” which can mean “excessive, inappropriate, not permitted,” will actually be interpreted. The future allocation of free certificates should also guarantee that actual production levels are better taken into account (it is currently based on historical data from 2005–2008). The European Council expressly emphasized that existing measures to protect against carbon leakage (relocation of CO₂-intensive industries) will also remain in effect after 2020, provided that there are no comparable efforts to reduce CO₂ in other significant, global economic regions. It has also explicitly committed itself to ensuring that the affected industries will be protected against loss of competitiveness.

The results of the European Council summit on energy can be summarized as follows: the Council has reiterated its commitment to ensuring “affordable” energy prices and improved pan-European integration of energy policies and infrastructure. The energy efficiency target of at
least 27% was “only” indicatively set; it will be reviewed in 2020 and the goal of 30% remains the desirable target. This means that the 2020 target of 27% could be increased to 30%. Implementation is up to the member states which can also define higher targets. The Commission will also determine the sectors to which specific requirements for greater energy efficiency apply. This offers potential for additional discussions and definitely requires more precise definition.

The Council’s most recent decisions provide a thoroughly constructive and realistic framework approach, one that defines concrete objectives and specifies measures intended to minimize the risks associated with these objectives. However, only a framework has been established; it is now up to the Commission and the member states to define it in detail and implement it. It will be critical to more closely define the still unfinished provisions, which are intended to protect the industry against one-sided burdens in the international marketplace.

In particular, the primary objective must remain to establish a tiered certificate allocation mechanism (based on 100% free allocation for the top 10% “most environmentally friendly” facilities).

**voestalpine Environmental Conference 2014**

Information, networking, and the definition of concrete steps regarding the latest environmental topics were the focus of the Environmental Conference, where the Environmental Officers from the European voestalpine companies met in Linz in September.

The challenges in the environmental sector are becoming increasingly complex and extend far beyond the individual sites. Once again, this became clear at this conference. With the participation of all environmentally sensitive European locations (Austria, Germany, Sweden, France, and Hungary) for the first time, and with the inclusion of external experts, the conference examined EU environmental and climate policy, the life cycle assessment of steel, intensification of the environmental network, and environmental communication.

**Life cycle assessment (eco-balance)**

The life cycle assessment takes a comprehensive approach to a material’s life cycle, beginning with the extraction of raw materials, transport and energy costs, to sustainability effects of the entire production and value chain through to recycling and/or reuse. Steel has undisputed advantages over all competing materials as it can be recycled back into the production process with no loss in quality.

The current challenges primarily include European developments to establish environmental product declarations (EPDs) and create ecological footprints for products and processes. In order to guarantee objective, international comparability, a technically correct, uniform approach to indicators, methods of measurement, and valuation is necessary. The difficulty lies particularly in the need to standardize pre-existing and extremely varied standards, rules and regulations, both in Europe and globally, and formulating an appropriate response to significant life cycle complexity.

voestalpine’s cross-divisional and cross-departmental Life Cycle Assessment (LCA) Team is active both in international working groups and advocacy and special interest groups, as well as in appropriate research projects in order to influence and shape the developments surrounding this topic.

**Outlook**

When the Letter to Shareholders for the first quarter of 2014/15 was published in the summer of this year, the overall economic situation seemed to indicate that a stable or even an upward trajectory could be expected for the remainder of the year, however, in the meantime, the signs of economic growth—at least in Europe—have faded. The continuing political and military destabilization in parts of the Middle East as well as the Russia-Ukraine conflict with its escalating sanction mechanisms are taking an increasing toll on the European economy. Additionally, a lack of confidence in the future as a result of an increasing recessive trend in some EU core nations and
a certain leadership vacuum surrounding the changing of the guard at the European Commission have also impacted Europe’s economic development. In any case, all of these aspects have not contributed to an improvement of sentiment.

The economic performance of the USA, however, continues to be strong, and China is succeeding in maintaining stable growth of 7% over the course of the year. In clear contrast, the negative economic development in Brazil and Russia has continued.

Regarding the current trends in the industrial sectors that are most important for the voestalpine Group, there is increasing differentiation among the various sectors. While the performance of the automobile industry worldwide is marked by continuing demand and the situation in the aviation and railway infrastructure industries is the same or at least similar, the slight uptrend in the construction, mechanical engineering, and electrical industries that persisted until the summer has not continued in the last few months, at least in Europe. The trend in the conventional energy generation industry has remained weak, while the development in the oil and natural gas sectors has continued to be very favorable worldwide despite the fact that the oil price has dropped sharply. As a result of major pipeline projects that have been recently awarded, there is an upward trend in energy transport sector as well. Performance of the consumer goods and white goods industries is stable, albeit not very remarkable and the agricultural machinery industry is trending significantly weaker.

Even though the economic framework conditions in Europe have not improved as had been hoped in the beginning of the year, it can be anticipated that in the second half of the business year 2014/15, all four of the Group’s divisions will enjoy practically full capacity utilization. Although most business sectors continue to experience strong price pressure, efficiency improvement and cost optimization programs that are in place in all the divisions and the accelerated development of markets outside of Europe should make it feasible to slightly improve profitability compared to the previous year even without taking any possible extraordinary income into account.

This means that the outlook for the current business year remains unchanged. From the current vantage point, it can be expected that the voestalpine Group will have an operating result (EBITDA) and profit from operations (EBIT) in 2014/15 that are slightly above the level of the past business year.