Interim Management Report

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

After a relatively optimistic start, the economic situation in the current business year 2014/15 was marked by an increasingly sober mood from the summer months onward. Of the major global economies, only North America remained firmly on its growth path throughout the course of the year. China is struggling more and more to maintain its economic growth, Brazil continues to be plagued by structural problems, Russia is being increasingly tested by Western sanctions, and in Europe, the recovery anticipated for 2014 had to be postponed by (at least) a year.

Once again, the beginning of the current business year was marked by economic optimism in the European Union, however, by mid-year, it was clear that 2014 would be yet another year when the actual economic momentum would not come close to the high expectations in the early part of the year. In addition to the "old," unsolved structural problems primarily—but not solely—in Southern Europe, the main reason for the disappointing development was a somewhat weaker economic trend in Germany and its neighboring countries during the summer months, caused mainly by political tensions resulting from the Russia-Ukraine conflict. However, the latest signals from the German economy are again pointing to a certain economic revival. For some time, the economic situation in England, Poland, and most recently in Spain as well has been moving in a positive direction, although in the latter country, movement began at an extremely low point. The next months will show whether these incipient developments will—supported by measures to stimulate the economy taken by the new EU Commission and the European Central Bank—create more than a temporary easing of the economic situation.

In contrast to Europe, in North America growth forecasts were raised after the summer months, driven by positive trends from both consumers and investors. In addition to the sustained upward trend of various macroeconomic early indicators, such as the Purchasing Manager Index (PMI), which reached its highest level in several years toward the end of 2014, it is primarily the enormous number of newly created jobs and the resulting dramatic reduction of unemployment, which boost confidence in the economic recovery and which will probably result in an adjustment of the interest rate by the US Federal Reserve in the course of the year.

In China, anxiety about a more broad-based economic slowdown became more pronounced in the course of the current business year. Triggered by a correction in the real estate sector, the early indicator PMI fell below the critical 50-point mark for the first time in some time. The central government reacted to this situation by adopting a more expansive money market policy on one hand and, on the other, by implementing a comprehensive economic stimulus program of around EUR 1.3 trillion, of which the lion's share of around EUR 900 billion will go to infrastructure projects, in order to guarantee annual minimum growth of 7%.

Just how dramatic the economic situation is in Russia is made abundantly clear by the inflation rate, which reached around 9% toward the end of the year and an interest rate in December 2014 of around 17%. The concurrent massive decline of the ruble highlights the magnitude of the recessive development.

While Brazil shifted from a recession to "mere" economic stagnation in the summer of 2014, the deterioration of the price of oil and other raw materials in conjunction with very negligible political reform momentum makes a rapid return to the growth rates of an emerging economy unlikely.

The voestalpine Group continued to hold its ground successfully in this uneven and inconsistent economic environment due to its broad-based positioning and sophisticated portfolio; in a year-to-year comparison, it again recorded stable revenues and improvements in all reporting categories.

In the first three quarters of the current business year, the Steel Division, (up to now still) mainly focused on the European market, faced a differentiated economic scenario insofar as the quite satisfactory level of demand was contrasted with a price environment that continued to be difficult. Despite deflationary framework conditions—falling raw materials and steel prices—the division maintained its revenue at a stable level and reported considerably higher earnings.

The Special Steel Division profited from its broad-based geographic positioning and substantially grew both revenue and earnings. In the past three quarters, the North American and Asian markets for tool steel and special materials made a particularly significant contribution to the division's performance; viewed overall, after a rather volatile phase during the summer months, conditions on the European market most recently became more favorable.

The Metal Engineering Division once again reported outstanding results although they did not quite match the previous year's level with its highly profitable railway infrastructure project business. Overall, the railway infrastructure segment is continuing unabated at a high level, and the other business segments Wire, Seamless Tube, and Welding Technology are enjoying a stable and positive level of demand.

The earnings of the Metal Forming Division performed unusually well during the business year 2014/15 thus far, due primarily to non-recurring effects resulting from portfolio streamlining. At the operational level, performance of the Automotive Parts and Components business segment continues to experience strong demand. Performance of the Tubes & Sections business segment differed widely depending on region, while the Precision Strip business segment was under increasing pressure from the competition. The Warehouse & Rack Solutions business segment continued its very satisfactory performance.

Report on the financial key performance indicators of the voestalpine Group

In the first nine months of the current business year, at EUR 8,254.9 million, the revenue of the voestalpine Group remained at a stable level compared to the previous year (EUR 8,268.8 million). Revenue losses suffered by the Metal Engineering Division as a result of the closure of the standard rail production in Duisburg as of the end of the 2013 calendar year was compensated by larger delivery volumes in the Special Steel Division. In a year-to-year comparison, revenue in both the Metal Forming Division and the Steel Division remained constant.

The voestalpine Group's operating result (EBITDA) improved during the first three quarters of 2014/15 by 8.8% compared to the previous year, going from EUR 999.6 million to EUR 1,087.2 million. It should be noted in this context that in the second quarter of 2014/15, non-recurring effects in the amount of EUR 66.5 million were recorded as a result of the sale of the Flamco Group in August 2014, the agreement at the end of 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 Metal Forming Division companies located in the Netherlands. Excluding these non-recurring effects, EBITDA rose by 2.1% to EUR 1,020.7 million. The EBITDA margin therefore rose from 12.1% in the previous year to 13.2% in the current year. Excluding non-recurring effects, the EBITDA margin for the current year is still 12.4%. During the same period, profit from operations (EBIT) improved compared to the previous year by 10.2%, going from EUR 569.3 million to EUR 627.4 million. Adjusted by the non-recurring effect of EUR 45.2 million resulting from the aforementioned extraordinary income, EBIT rose by 2.3% to EUR 582.2 million. The adjusted EBIT margin thus increased to 7.1% compared to 6.9% in the previous year. With the exception of the Metal Engineering Division, which nevertheless remained the Group's most profitable division despite the slight decline in the operating result, all other divisions improved their profitability in the first three quarters of 2014/15 in a year-to-year comparison.

Although the voestalpine Group's gross financial debt increased as of December 31, 2014, net interest charges, which had amounted to EUR 125.0 million as of the end of December 2013, fell as of the same reporting date in 2014 by 22.6% to EUR 96.8 million. The increase in gross financial debt resulted primarily from the refinancing of hybrid bond 2007 (volume: EUR 500 million), which was redeemed as of the end of October 2014, by the issue of corporate bond 2014 (issue on: October 14, 2014, volume: EUR 400 million). While the hybrid bond was recognized in equity, corporate bond 2014 is recognized as part of borrowed capital. As interest rates fell in the past quarters, interest expenditure decreased significantly; as a result, profit before tax rose substantially in a year-to-year comparison by 19.4%, going from EUR 444.3 million to EUR 530.6 million. Even after deduction of the non-recurring effects amounting to EUR 45.2 million, profit before tax in the first three quarters of 2014/15 improved by 9.3% to EUR 485.4 million.

The fact that profit for the period increased even more than profit before tax is due to the lower tax rate in the current business year. Thus, profit for the period rose by 26.6% from EUR 349.7 million to EUR 442.8 million. Adjusted by the non-recurring effects (EUR 43.4 million), profit for the period in the first three quarters of 2014/15 was EUR 399.4 million, corresponding to an increase compared to the previous year of 14.2%. Earnings per share in the current business year are EUR 2.28, more than one third higher than the figure of EUR 1.69 in the previous year. After deducting the non-recurring effects, earnings per share are EUR 2.03, still an increase of 20.1%.

Equity fell by 2.0%, from EUR 5,117.4 million as of December 31, 2013 to EUR 5,013.4 million as of December 31, 2014. Compared to the reporting date of March 31, 2014 (EUR 5,261.0 million), equity decreased by 4.7%. As previously stated, the reduction in equity is due to the refinancing of hybrid bond 2007, which is recognized in equity, by corporate bond 2014, which is reported as part of borrowed capital. This measure naturally had a impact on net financial debt, which increased in a year-to-year comparison by 19.4% from EUR 2,584.1 million (adjusted retroactively) to EUR 3,086.6 million. The increase corresponds precisely to the volume of the hybrid bond of EUR 500 million. Compared to the reporting date of March 31, 2014 (EUR 2,421.4 million, adjusted retroactively), net financial debt rose by 27.5%. Due to these changes in the Group's financing structure, the gearing ratio (net financial debt in percent of equity) rose in the first nine months of the business year 2014/15 from 46.0% (adjusted retroactively) to 61.6%.

As of December 31, 2014, the voestalpine Group had 46,461 employees (FTE), almost exactly the same figure as in the previous year (46,460 employees, adjusted retroactively).

Comparison of the quarterly and nine-month figures of the voestalpine Group

In millions of euros				Q1–Q3		
	Q 1 2014/15 04/01–06/30/2014	Q 2 2014/15 07/01–09/30/2014	Q 3 2014/15 10/01–12/31/2014	2014/15 04/01–12/31/2014	2013/14[1] 04/01–12/31/2013	Change in %
Revenue	2,826.7	2,734.4	2,693.8	8,254.9	8,268.8	–0.2
EBITDA	363.7	393.2	330.3	1,087.2	999.6	8.8
EBITDA margin	12.9%	14.4%	12.3%	13.2%	12.1%	
EBIT	218.4	226.3	182.7	627.4	569.3	10.2
EBIT margin	7.7%	8.3%	6.8%	7.6%	6.9%	
Profit before tax	192.9	198.8	138.9	530.6	444.3	19.4
Profit for the period[2]	154.4	169.6	118.8	442.8	349.7	26.6
Employees (full-time equivalent)	47,463	47,379	46,461	46,461	46,460	0.0

[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.

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 be able to fulfill the pioneering role in technology, which it has established in recent years, even more comprehensively in the future and to sustain its commitment to extremely sophisticated products, investment in the voestalpine Group in the first three quarters of 2014/15 was again increased compared to the same period in the previous year, going from EUR 657.5 million to EUR 747.1 million, an uptick of 13.6%. Relatively speaking, the Metal Engineering Division saw the greatest boost in investment at 65.6%; however, this figure also includes the acquisitions undertaken by the division in the third quarter of 2014/15 (see also the "Acquisitions" section). At EUR 349.7 million, investments by the Steel Division in the first nine months of 2014/15 were only slightly higher than in the previous year (EUR 343.7 million). Besides necessary replacement of legacy equipment, investments by this division were focused on cost, product, and technology optimization measures. Current priority projects are the construction of a direct reduction plant in Texas (completion scheduled for late 2015/early 2016), installation of coal injection systems on all three blast furnaces in Linz (in the completion stage), construction of secondary metallurgy system 4 (commissioning slated for the fall of 2015), construction of a new heavy plate rolling mill (commissioning slated for the fall of 2015) as well as construction of continuous casting facility 8 (construction recently contracted).

Investment in the Special Steel Division in the first three quarters of 2014/15 amounted to a total of EUR 99.1 million, a decline of 8.8% compared to the previous year's figure of EUR 108.7 million. The main focus of investment activity was on the Value-Added Services segment. As of the beginning of the current business year, a coating service center was established in Shanghai, China, and a coating facility in Taiwan began operations as of the beginning of the third quarter. Significant expansion has also been undertaken in strategic markets in the tool steel hardening segment, which is upstream of the coating segment. For example, the new sales center near Istanbul, Turkey, is now a one-stop provider of both sophisticated tool steel and high quality heat and surface treatment processes and in mid-January 2015, a sales company that also provides pre-processing facilities was opened in Puebla, Mexico.

In the first three quarters of 2014/15, investment, including acquisitions, in the Metal Engineering Division was at EUR 165.1 million, around two thirds higher than last year's figure of EUR 99.7 million. The division's strategically most significant project is the construction of a new wire rod mill (including a walking beam furnace) in Donawitz, Austria. which has extremely sophisticated technology. To enable continuing technological improvement of innovative rail grades, the Rail business segment is also erecting a new walking beam furnace.

In the first nine months of the business year 2014/15, the Metal Forming Division invested a total of EUR 126.9 million, an increase of 28.2% compared to the previous year's level (EUR 99.0 million). Investments, which were part of the comprehensive expansion and internationalization strategy, were focused primarily on the press-hardened steel segment ("phs-ultraform"), which is based on new technology. In the third quarter, two new "phs" lines in Schmölln and Schwäbisch Gmünd, Germany, were put into operation; they will complement production sites belonging to the Automotive Body Parts business segment in the USA, South Africa, and China. In addition, at the beginning of the current business year, production of special sections for construction and agricultural machinery started up in Suzhou, China.

Acquisitions

In the course of the business year 2014/15 thus far, the Metal Engineering Division made two acquisitions, one in the Wire business segment and the other in the Turnout Systems business segment. The Italian manufacturer of special wire Trafilerie Industriali S.p.A., which is headquartered in Nervesa della Battaglia (Treviso), was acquired in the third quarter. The company specializes in the production of drawn wire. It has 80 employees and in 2013, it generated annual revenue of EUR 43.8 million with an annual production of around 50,000 tons. For voestalpine, this acquisition means an additional enhancement of the product portfolio in the segment of drawn wire for the automotive industry and another customer-specific extension of the value chain in the premium quality segment; it also strengthens voestalpine's market position in Italy. The business segment Turnout Systems further expanded its leading market position in Australia in the third quarter by acquiring the Australian company Bathurst Rail Fabrication Center (BRFC). This specialist for high-quality welded rails, turnouts, and track components has a staff of around 60 employees and generated annual revenue of around EUR 34 million last year. With its turnout and rail welding plant, BRFC is the key railway competence center for Sydney Trains, which operates a major part of the railway network in the Australian state of New South Wales. With this acquisition, the Turnout Systems business segment has expanded its local presence in Australia considerably; paired with the voestalpine Group's expertise, this creates the potential for future mass transit projects in Australia as well as in the important heavy-haul sector. The acquisition is set to close in the early part of the business year 2015/16.

Employees

As of the reporting date December 31, 2014, the voestalpine Group had 46,461 employees (FTE, full time equivalent) worldwide; the number of employees remained practically unchanged compared to the previous year's reporting date (46,460).
The number of temporary staff was 3,993 persons, an increase of 5.1% compared to the third quarter of the business year 2013/14 (3,798).
As of the reporting date December 31, 2014, 1,666 apprentices were being trained Group-wide, 3.7% or 59 young people more than as of December 31, 2013 (1,607).

Research and development

The current focus of the Research & Development sector at voestalpine is on accelerating the process of synergistically combining the expertise that is internationally available within the Group in order to develop new process and product solutions that are tailored to specific customer needs and requirements. The long-term objective is to develop innovative complete solutions in the individual sectors with the goal of generating optimum customer benefit while reducing life cycle costs, and to achieve the best performance possible along all the value chains.

One of the measures taken in this respect was a cross-divisional project that critically examined the chain from tool steel to tool user. As the Group has all of the expertise necessary, for example, production of tool steel, heat treatment, and coating, and also not only manufactures tools but uses them as well, an intensive collaborative process resulted in significantly improved productivity and, at the same time, considerable cost savings.
A completely different research project was recently put into actual practice under the name "Möllerradar" (batch radar). With the help of this measuring equipment, topography and temperature distribution on the batch surface are mapped at a blast furnace at the Linz site during production in real time. This enables optimized process management, which in turn results in decreased consumption of reducing agents in the blast furnace process.
The topic of this year's eighth annual R&D Synergy Platform, which took place in early October 2014 in Kapfenberg, Styria, was "Tools/dies and tool/die materials," in other words, tools and forming tools and the materials necessary for the process. The conference provided the roughly 100 attendees from various Group companies with an excellent overview into this technically very sophisticated niche segment through lectures by experts from all the divisions as well as additional input and fresh aspects from lectures by external speakers.

Environment

Energy and climate policy 2030 in the European Union

It currently appears that the European Union wants to retain its quantitative "2030 objectives," after which point in time it plans to introduce mechanisms to continue to increase the CO_2 price. This would result in yet another massive disadvantage of the energy-intensive manufacturing industries not only vis-à-vis the energy sector but especially vis-à-vis overseas competitors. The next step in the spring of 2015 will be the vote on the proposal for a "market stability reserve for emissions trading," which will provide the first indications about the further development and which will in all likelihood result in a revision of the Emissions Trading Directive. Concurrently, discussions will continue at the European level regarding how emissions trading will be organized in the long term, including the basic technological criteria.

Global level

After the Lima Climate Change Conference in December 2014, the UN Climate Change Conference will meet in Paris in late 2015 to decide on a follow-up agreement to the Kyoto Protocol that will expire in 2020. As a preliminary step, there are plans to define national reduction commitments in the coming months. The scope and, in particular, the degree of comparability and transparency of the reduction of greenhouse gases in the individual nations and regions will be a major indicator for the seriousness of global climate protection efforts.
In particular the ambitions of those nations, which have not ratified the Kyoto Protocol thus far (e.g., USA), and of the emerging economies, which have joined the treaty but have nevertheless increased their emissions, notably China and India, are of crucial importance for the industry in the European Union.
From the vantage point of the voestalpine Group, which operates globally, preference should be given to a climate protection agreement based on uniform principles that is mandatory worldwide as opposed to varying regional solutions.

Outlook

In the development of the global economic trends, the beginning of 2015 does not bring much that is new: continuing strong economic data from the USA and a stable development in China are contrasted by a stagnating economy in Brazil and Japan. Under the current political and economic circumstances, Russia will continue to face a significant recession for some time to come. The noticeable atmosphere of renewal resulting from the change in the political landscape in India should provide opportunities for increased growth in 2015.
And Europe? After the economically disappointing second half of 2014, the EU Commission and the European Central Bank have recently proposed ambitious packages of measures, on one hand at the investment end (investment package amounting to EUR 315 billion) and, on the other, in the area of quantitative easing (government bond-buying program amounting to EUR 1,140 billion), thus taking clear aim at a revitalization of the economy. However, it is still up in the air to what extent it, together with more investments in infrastructure in a number of countries, as well as the first signs of progress in Spain and Portugal will enable a return to at least modest growth during the course of the year. What will be crucial is less the future development in Greece, which is of secondary importance economically measured against Europe as a whole, but rather the development in France and Italy and the course that the Russia-Ukraine conflict will take.
Supporting factors for a recovery in Europe could be the continued strong economic activity in the automobile industry, a certain uptrend in the mechanical engineering sector, and the expected revival in the construction and construction supply industries resulting from accelerated implementation of infrastructure projects—the latter being already visible in the railway infrastructure sector. The decline of the oil price and the associated postponement of exploration and pipeline projects brings pressure on the corresponding industry segments; however, on the other side of the coin, it results in significant benefits for the consumers with corresponding positive effects on their buying habits.
A positive effect for an economic recovery in Europe is also the significantly lower rate of exchange of the euro, especially vis-à-vis the US dollar, as this improves the export possibilities for European companies.
Despite this proliferation of positive economic signals, it would be premature to assume that this equals a beginning recovery in Europe; the political and economic uncertainties are still too great. But there is a chance that in the course of the second half of 2015 Europe will see at least a slight economic recovery.
Against this backdrop and assuming stable capacity utilization in all of the most important business segments, the outlook for the voestalpine Group is unchanged. For the business year 2014/15, the Group can expect an operating result (EBITDA) and profit from operations (EBIT) that are slightly above the level of the past business year (even without taking positive non-recurring effects into consideration).