METAL ENGINEERING DIVISION

MARKET ENVIRONMENT AND BUSINESS DEVELOPMENT

As a leading quality supplier to the rail and turnout technology, wire, seamless tubes, and welding consumables sectors, during the business year 2016/17 the Metal Engineering Division succeeded in performing well in the consistently challenging market environment which characterizes these segments. This was in no small part due to rigorously implementing the strategy of offering its customers innovative products as well as tailor-made logistics solutions and services. The focus on customer-specific research projects, as well as investments in new and technologically-sophisticated facilities, and the ongoing exchange of know-how between the individual business segments, contribute to further differentiating the division from its competitors.

Following the predominantly attractive market environment of the past years which prevailed in Europe's railway infrastructure sector (the core market for the Rail Technology business segment), these conditions deteriorated during the second half of the business year 2016/17. The positive market development in Europe in 2014 and 2015 was primarily due to the backlog in maintenance investments, and less the result of laying new lines. Over the course of the calendar year 2016 the level of maintenance activities in the European rail network once more returned to a much more moderate level. In the oil-financed Gulf States and the mining countries of Brazil, Australia, and South Africa, investments in railway infrastructure also fell below that of previous years, due, among other factors, to low oil and raw materials prices. In Brazil, however, the order situation improved slightly towards the end of the business year with the securing of contracts for several individual projects.

As a globally-active division with over 40 production and sales sites, the Turnout Systems business segment was largely able to compensate for the weakness in the European market. Demand for high-speed lines in China in particular was at a very attractive level during the past business year. In contrast, demand for turnouts in the US heavy-haul transport market fell significantly, due to comparatively low freight transport volumes in 2016. Bureaucratic hurdles in India in 2015/16 resulted in project delays, whereas an increased number of contracts were recorded in 2016/17.

For the Wire Technology business segment, which manufactures high quality rod wire, drawn wire, flat and shaped wire, as well as ultra-high-tensile fine wire, the business year 2016/17 marked a turning point; commissioning of the new wire rod mill is almost complete so that the world's most modern facility of its type will be fully operational during the business year 2017/18. In terms of demand, the mood in the automotive industry remained positive during the business year 2016/17. In addition, there was a slight market upswing in special wires for the oil and natural gas industries during the second half of the business year.

There was also a significant uptick in orders from this sector for the Seamless Tubes business segment, leading to an improved performance in the second half of the business year. As well as

KEY FIGURES OF THE METAL ENGINEERING DIVISION

In millions of euros	2015/16	2016/17	Change in %
Revenue	2,850.4	2,684.6	–5.8
EBITDA	510.9	360.8	–29.4
EBITDA margin	17.9%	13.4%	
EBIT	314.9	200.8	–36.2
EBIT margin	11.0%	7.5%	
Employees (full-time equivalent)	12,675	13,157	3.8

KEY FIGURES OF THE METAL ENGINEERING DIVISION, ADJUSTED

In millions of euros	2015/16	2016/17	Change in %
Revenue	2,850.4	2,684.6	–5.8
EBITDA	384.4	360.8	–6.1
EBITDA margin	13.5%	13.4%	
EBIT	251.5	217.4	–13.6
EBIT margin	8.8%	8.1%	
Employees (full-time equivalent)	12,675	13,157	3.8

increased oil shale mining activity in the oil and gas industry in the USA, the implementation of new and innovative product solutions designed to optimize the exploration process was a significant factor in the growing upwards trend. However, improved capacity utilization in the industry was initially reflected only in an increase in volumes, not a rise in prices; it was only toward the end of the business year that the rising costs of iron ore and coke could be gradually reflected in higher prices. The measures the US government plans to protect its national steel sector are not yet clear, but continue to entail significant volatility for the US business.

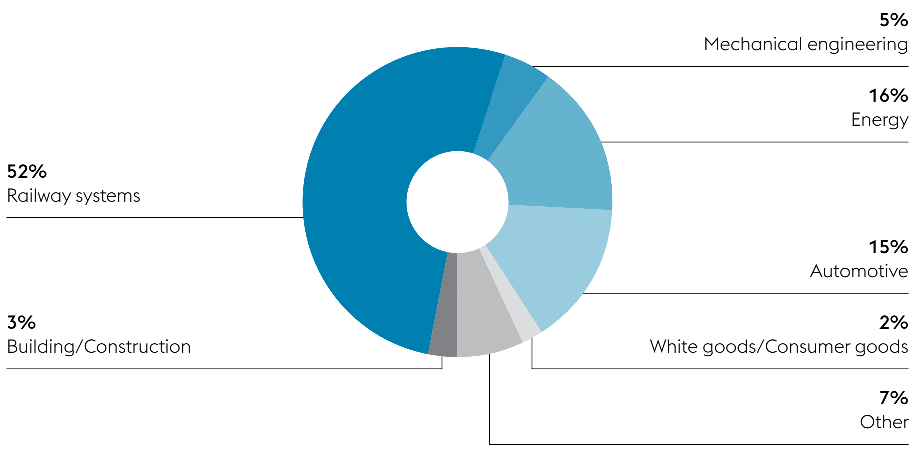
The market environment faced by the Welding Consumables business segment continued to be challenging during the past business year. It was primarily the energy sector which suffered continuing market weakness. It terms of the key sales regions, market conditions in Asia, and especially China, were significantly more attractive than in Europe and the USA; in contrast, no notable revival of demand is expected in South America for the time being. Conversely, the program of restructuring and diversification introduced and partly implemented in past years has already contributed to a significant improvement in earnings.

FINANCIAL KEY PERFORMANCE INDICATORS

Revenue and earnings in the Metal Engineering Division were lower in the business year just ended than in the previous year. This is primarily due to the massive economic downturn in the oil and gas sector as well as falling volumes of rail deliveries over the course of the year, themselves the consequence of reduced infrastructure activities particularly in the European railway systems customer segment. During the fourth quarter of 2016/17 the division was able to trigger a reversal of this trend after stabilizing the key figures in the first three quarters of the past business year, although at a level significantly lower than in the previous year. This was supported both by the upswing in the oil and gas sector, as well as the restructuring measures undertaken in the Welding Consumables business segment which have had a noticeably positive impact. In a year-over-year comparison, the division's revenue decreased by 5.8%, from EUR 2,850.4 million in 2015/16 to EUR 2,684.6 million in the business year just ended. Earnings performance during the past business year was positively influenced by non-recurring effects amounting to EUR 126.5 million recorded in EBITDA and EUR 63.4 million recorded in EBIT due to the acquisition of the controlling interest in the companies voestalpine Tubulars GmbH & Co KG, voestalpine Tubulars GmbH (both belonging to the Seamless Tubes business segment), as well as CNTT Chinese New Turnout Technologies Co., Ltd. (Turnout Systems business segment) which were fully consolidated for the first time. As a result of reassessments based on fair value less depreciation of hidden reserves which are also included in the non-recurring effects of the previous year, EBIT declined by a total of EUR 16.6 million in the business year 2016/17.

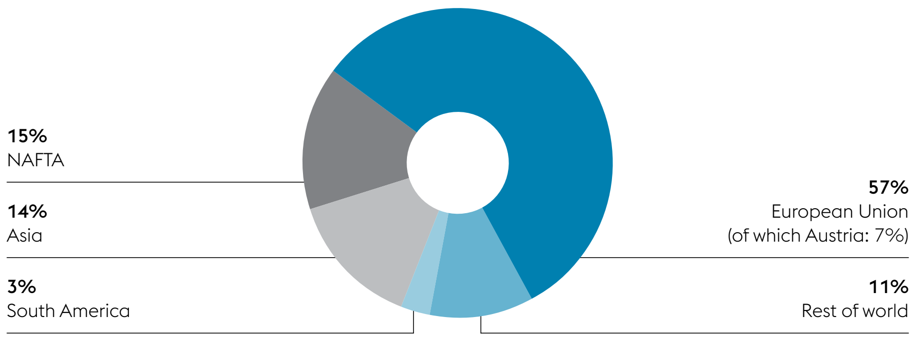
CUSTOMERS OF THE METAL ENGINEERING DIVISION

As percentage of divisional revenue, business year 2016/17



MARKETS OF THE METAL ENGINEERING DIVISION

As percentage of divisional revenue, business year 2016/17



Against this backdrop, in a year-to-year comparison the earnings figures published in accordance with International Financial Reporting Standards (IFRS) declined by around a third, with EBITDA falling from EUR 510.9 million to EUR 360.8 million, and EBIT from EUR 314.9 million to EUR 200.8 million. Disregarding these non-recurring effects, the adjusted operating result (EBITDA) for the division only declined by 6.1%, from EUR 384.4 million in the previous year, to EUR 360.8 million in 2016/17. Adjusted for non-recurring effects, during the same period profit from operations (EBIT) declined by 13.6%, from EUR 251.5 million to EUR 217.4 million. As a result of lower revenue, in a twelve-month comparison the adjusted EBITDA margin remained stable at 13.4% (previous year 13.5%), while the adjusted EBIT margin dropped from 8.8% in the previous year to its current level of 8.1%.

A comparison of the fourth quarter of 2016/17 with the quarter immediately preceding highlights the positive trend visible toward the end of the business year. This rise is mainly contributable to the Wire Technology, Seamless Tubes, and Welding Consumables business segments which are the segments particularly active in the energy sector. Against this backdrop, compared to the quarter immediately preceding, revenue in the division rose by 4.1%, from EUR 662.4 million to EUR 689.7 million. The improvement in the earnings figures was far more significant. EBITDA rose by 28.6%, from EUR 82.6 million in the third quarter to EUR 106.2 million in the fourth quarter. EBIT increased by 36.6%, from EUR 44.5 million to EUR 60.8 million, and EBIT adjusted for non-recurring effects gained 38.3%, rising from EUR 48.0 million to EUR 66.4 million. As a result of this positive development, the adjusted EBITDA margin rose from 12.5% in the third quarter to 15.4% in the fourth quarter, while the EBIT margin adjusted for non-recurring effects grew from 7.2% to 9.6%.

As of March 31, 2017, the Metal Engineering Division had 13,157 employees (FTE), an increase of 3.8% compared to the same reporting date in the past business year (12,675). This primary reason for this rise since the start of the business year is the improved level of orders from the oil and gas industry; personnel capacities in the Seamless Tubes business segment have been adjusted to reflect this improved market environment.

QUARTERLY DEVELOPMENT OF THE METAL ENGINEERING DIVISION

In millions of euros	1st quarter 2016/17	2nd quarter 2016/17	3rd quarter 2016/17	4th quarter 2016/17	BY 2016/17
Revenue	680.4	652.1	662.4	689.7	2,684.6
EBITDA	87.6	84.4	82.6	106.2	360.8
EBITDA margin	12.9%	12.9%	12.5%	15.4%	13.4%
EBIT	49.7	45.8	44.5	60.8	200.8
EBIT margin	7.3%	7.0%	6.7%	8.8%	7.5%
Employees (full-time equivalent)	12,606	12,709	12,822	13,157	13,157

QUARTERLY DEVELOPMENT OF THE METAL ENGINEERING DIVISION, ADJUSTED

In millions of euros	1st quarter 2016/17	2nd quarter 2016/17	3rd quarter 2016/17	4th quarter 2016/17	BY 2016/17
Revenue	680.4	652.1	662.4	689.7	2,684.6
EBITDA	87.6	84.4	82.6	106.2	360.8
EBITDA margin	12.9%	12.9%	12.5%	15.4%	13.4%
EBIT	53.6	49.4	48.0	66.4	217.4
EBIT margin	7.9%	7.6%	7.2%	9.6%	8.1%
Employees (full-time equivalent)	12,606	12,709	12,822	13,157	13,157