
# MS Industrie AG

## EXTRACTS from the Group's Management Report 2018

NOT LEGALLY BINDING

**Important notes:**
English translation for convenience purposes only
General data format is "TEUR" (Euro thousands),
i.e. TEUR 1.000 = EUR 1.000.000 or EUR 1 million

# Foreword from the Executive Board on the 2018 Annual Financial Report

Dr. Andreas Aufschnaiter

Armin Distel

**Dear Shareholders, Employees and Business Partners of MS Industrie AG,**

In 2018, our Group once again experienced strong organic growth with revenues of around **EUR 282,8 million** overall. Compared with the revenues generated in the previous year (EUR 250,6 million), this represents an increase of around **+12,8%,** which resulted from the strong demand both in the commercial vehicles sector and the special purpose machines sector in North America and Europe. The various key earnings figures developed positively, mainly as a result of the expansion in business volumes. The Group achieved a positive profit for the year after taxes of EUR 7,1 million (previous year: EUR 7,0 million) and slightly increased its equity ratio from 37,1% to 38,2%.

We would like to highlight a few crucial milestones and developments for the readers of this Annual Report, which we consider to be significant in terms of assessing the financial year 2018 and the outlook:

- Business performance in the "Powertrain" segment (**MS Powertrain Technology Group**, also briefly **MS PTG**) reflected substantial growth in demand in the entire **NAFTA region** since the beginning of the year, while at the same time product demand for new diesel engines in **Europe** including Germany was rising continuously again, boosting revenues by around +13,2% overall. New orders were received in 2018 for series production at the Trossingen location, with production starting in the fourth quarter. The "Powertrain" segment was also successful in April 2019 in obtaining an order for series production of valve train components for a new engine platform for heavy commercial vehicles of a renowned global group. Series production is expected to commence in early 2021.

- In the "Ultrasonic Technology" segment (**MS Ultrasonic Technology Group**, also briefly **MS UTG**), the **construction of special purpose machines** for our customers in the passenger car industry grew at around +11,6% in Europe and North America. However, the order situation in 2019 must be considered as more difficult given the uncertainty and caution of car manufacturers as the debate over the merits of diesel vs electric cars is continuing.

- The new range of MS UTG’s industry 4.0-based **ultrasonic welding machinery** products for the „**MS soniTOP**" brand developed very positively, growing by +200% and attracting customers from a number of industries. Simultaneously, we stepped up our sales capacities in order to accomplish the expansion of the business planned for the coming years. The trade fair "K-Messe" in Düsseldorf in October 2019 will again provide important stimuli in this respect.

- Demand for the electric drive "ERZMO" for "last mile" transport applications, which has been further developed by **Elektromotorenwerk** in Grünhain (EMGR), was increasing in late 2018, also owing to an innovative vehicle concept developed by b&p engineering mobility GmbH, in which we hold a non-controlling interest. The integrated drive system comprises a powerful electric motor, a three-speed gearbox and an electronic control for the application in cargo bikes, e.g. for mail and parcel delivery services as well as businesses in the craft and disposal sectors.

- •The successful disposal of our 19,9% interest in **Zehnder Pumpen GmbH** to the French SFA Group in January 2019 was a first positive business transaction after the balance sheet date. Zehnder Pumpen will continue to rely on EMGR as supplier of a multitude of bespoke motors and even expand its activities at the location of Grünhain-Beierfeld under the direction of the new shareholder.

- A second event of great importance for MS Group after the balance sheet date was the **sale of the production** for the Daimler world engine at the Webberville / Michigan site to Gnutti Carlo Group (Gnutti Carlo S.p.A., Maclodio / Italy) in March/April 2019. This strategic decision means that sales of the MS Industrie Group will initially decline by around EUR 80 million per year; however, at the same time, dependency on the major global customer Daimler will decrease, which, of course, will continue to be supplied in Europe in the usual quality and reliability regarding the world engine and as well as a number of other parts and components in the powertrain segment. The MS Industrie Group will continue to be present in the US and will systematically expand its local business activities, especially in connection with the marketing of ultrasonic welding machines throughout the North American market. The space not used by the MS UTG segment at the Webberville site, which was acquired at the beginning of 2019, will be leased to Gnutti on a long-term basis.

The average **order backlog** for the MS Industrie Group overall amounted to over EUR 150 million in the first quarter of 2019, around +5% higher than at the end of 2018, and is therefore an indication of a positive development. Following the sale of the production for the Daimler world engine in the USA, the order backlog in the Group was around **EUR 107 million** as at early April 2019. Although the economy has been in a somewhat fragile state internationally and experts have downgraded their growth forecasts, we expect more stable sales markets for the MS Industrie Group in 2019.

Our strategy for the year 2019 and beyond will focus on continuing organic growth in Europe in the MS PTG segment, which is to be achieved mainly by winning new customers, adding new high-precision powertrain components and systems to our range and by increasing the level of automation in manufacturing. In the MS UTG segment, the basis for our growth will be a large number of R&D projects in varied applications and industries. At the same time, we are pushing ahead with the enlargement of our customer base and footprint on markets worldwide.

The **MS Industrie share price** unfortunately followed the general trend in the capital markets, in particular in the automotive industry, and dropped by as much as around -40% in 2018. In early 2019, however, it showed a slight recovery. Despite this difficult market environment we will continue to pursue the further strategic and operational development of our Group with vigor and take a more focused approach to capital market communication.

We are particularly grateful to all of the employees at the MS Industrie Group and for the efforts made in 2018 in jointly mastering the challenges we were facing.

Yours sincerely,

Dr. Andreas Aufschnaiter Armin Distel

Munich, 24 April 2019

ULTRASONIC TECHNOLOGY GROUP

**Production locations**

Reputed customers around the world rely on us for our innovativeness, reliability and the premium quality of our products. We maintain production locations around the globe:

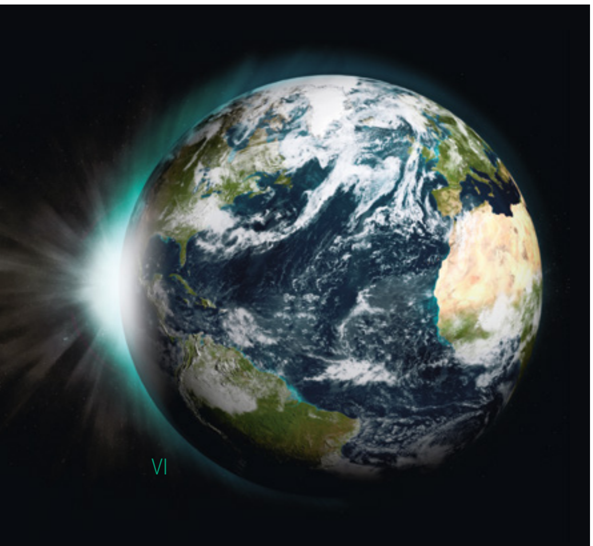
Production locations in Germany:
**MS Ultraschall Technologie GmbH**
in Spaichingen, Baden-Württemberg: 18,000 m²
**MS Powertrain Technologie GmbH**
in Trossingen-Schura, Baden-Württemberg: 16,000 m²
**MS PowerTec GmbH**
in Zittau, Saxony: 5,000 m²
**Elektromotorenwerk Grünhain GmbH**
in Grünhain-Beierfeld, Saxony: 17,000 m²

Production locations in the United States:
**MS Plastic Welders, L.L.C.** and
**MS Precision Components, L.L.C.** (until 04/2019)
in Webberville, Michigan: 16,000 m²

Production locations in Brazil:
**WTP MS Ultrasonics**
in Belo Horizonte: 900 m²

Production locations in China:
**Shanghai MS soniTEC Co., LTD.**
in Jiangyin: 4,000 m²

Production locations in Bulgaria:
**EMGR EAD**
in Gabrovo: 700 m²



**MS Ultraschall Technologie GmbH**
**MS Plastic Welders, L.L.C.**
**WTP MS Ultrasonics**
**Shanghai MS soniTEC Co., LTD.**

**Ultrasonic custom machines (MS soniMAC)**
**for the automotive industry.**

**Ultrasonic servo presses (MS soniTOP)**
**for industry-independent ultrasonic applications.**

**Ultrasonic systems (MS soniSYS)**
**for customized ultrasonic solutions.**

**Ultrasonic components (MS soniCOM)**
**for industry-independent ultrasonic applications.**

**Ultrasonic technology**

The MS Ultrasonic Technology Group operates globally and across all industries. As a leader in innovation in the area of ultrasonic technology, it provides customisable special machines, innovative servo presses, modular systems and efficient components as powerful integrated solutions in connection and processing technology for thermoplastic materials, films and textiles as well as for cutting food.

POWERTRAIN
TECHNOLOGY
GROUP

MS Powertrain Technologie GmbH
MS PowerTec GmbH
MS Precision Components, L.L.C. (until 04/2019)


**Systems**

- Complete valve trains
- Rocker arms

**Components**

- Gear box housings
- Valve bodies

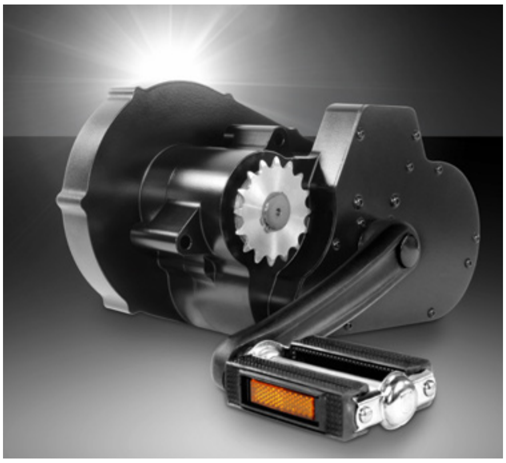
**Development**

of innovative and targeted cost-related valve control and engine braking systems.

**Machining technology and module assembly**

The MS Powertrain Technology Group has extensive knowledge for perfectly customised solutions over the entire power train. It develops, manufactures, assembles and delivers powerful systems and components for and to many well-known automobile and commercial vehicle manufacturers as well as leading engine and gear manufacturers globally. MS does this by successfully combining many years of manufacturing experience with the latest processing technologies.

Elektromotorenwerk Grünhain GmbH
EMGR EAD



**Electric motors**

- Capacitor motors
- Three phase A.C. motors
- Synchronous motors
- Rotors
- Stators
- Pedelec-drive for Cargo-e-mobility

**Electric motor production**

At our electric motor company Elektromotorenwerk Grünhain (EMGR) we offer market-leading customised drive solutions for industrial applications. Our electric motors, which are produced based on a high vertical integration, are developed in cooperation with our customers based on their specific requirements. New energy-efficient motors, drive electronics, brakes, gear elements and aluminium die-cast components are being increasingly added to our motor range.

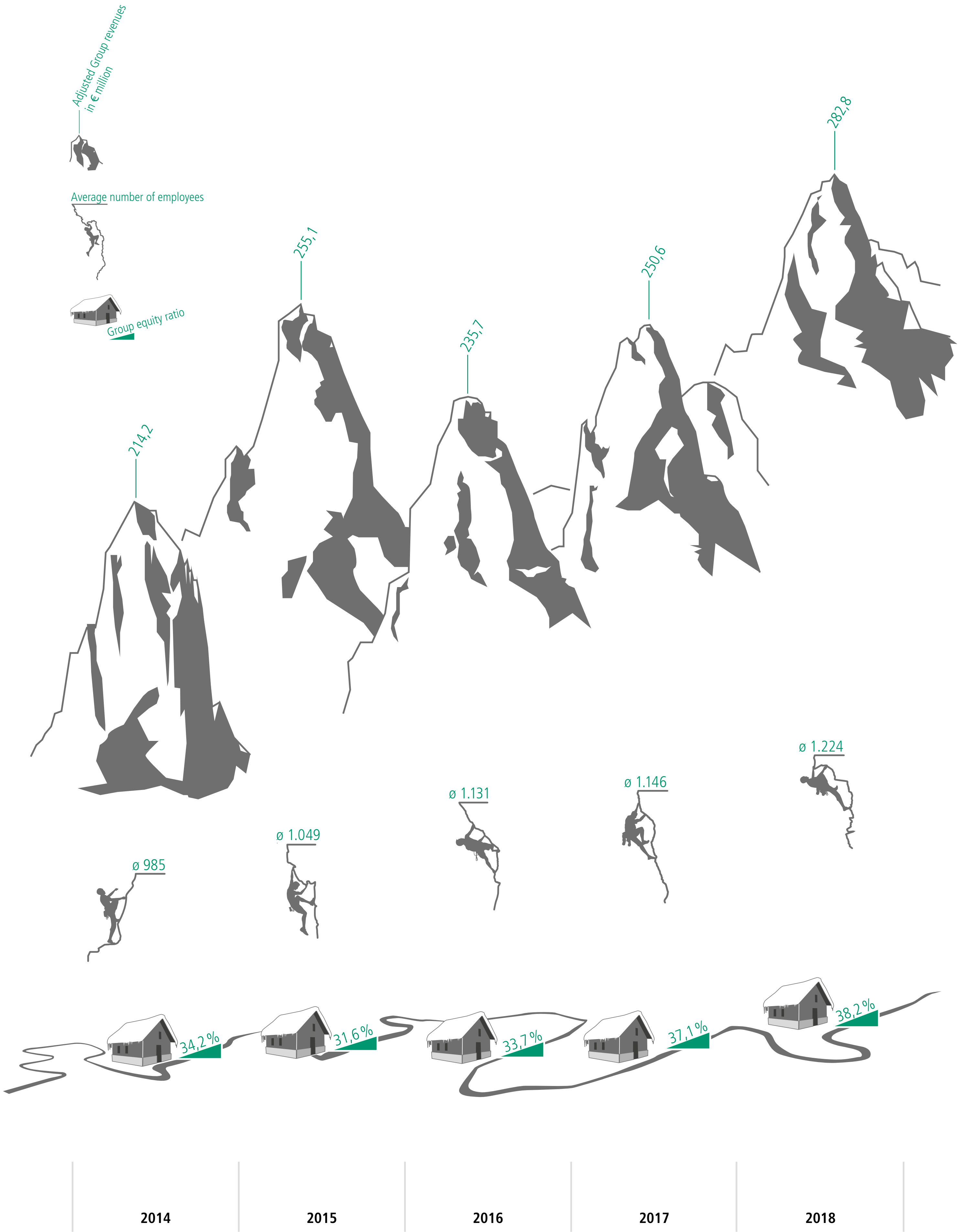
# Annual Consolidated Financial Statements 2017 - Overview of key figures

**MS Industrie Group, according to IFRS, audited, in TEUR**

| Balance sheet key figures | 31.12.2017 | 31.12.2018 |
|---|---|---|
| Total assets | 152.709 | 171.070 |
| Equity and non-controlling interests | 56.684 | 65.313 |
| Equity ratio (%) | 37,1 % | 38,2 % |
| Trade receivables | 27.506 | 44.267 |
| Liquid funds (Cash and cash equivalents ./. Current accounts) | 1.389 | -4.028 |
| Net working capital (Inventories + Trade receivab. ./. Trade payables) | 54.407 | 73.160 |

| Cashflow key figures | 2017 | 2018 |
|---|---|---|
| Net cash generated from operating activities | 5.854 | 1.132 |
| Net cash used in investing activities | -3.317 | -12.365 |
| Net cash generated from / used in financing activities | -1.676 | 5.816 |

| Income statement key figures | 2017 | 2018 |
|---|---|---|
| Revenues | 250.621 | 282.753 |
| Other operating income | 5.582 | 4.148 |
| Cost of materials (including changes in inventories) | 132.239 | 150.577 |
| Gross profit | 123.964 | 136.324 |
| Personnel expense | 63.629 | 71.083 |
| Other operating expense and IFRS 9 | 38.309 | 42.460 |
| Earnings before interest, taxes, depreciation and amortisation (EBITDA) | 22.026 | 22.781 |
| Depreciation and amortisation expense | 13.057 | 12.017 |
| Operating profit (EBIT) | 8.969 | 10.764 |
| Financial result and result from associated companies | -463 | -1.453 |
| Profit before income tax (EBT) | 8.506 | 9.311 |
| Profit for the year after non-controlling interests (EAT) | 7.022 | 7.190 |
| Consolidated earnings per share in EUR | 0,23 | 0,24 |



Adjusted Group revenues in € million
Average number of employees
Group equity ratio
214,2
255,1
235,7
250,6
282,8
ø 985
ø 1.049
ø 1.131
ø 1.146
ø 1.224
34,2 %
31,6 %
33,7 %
37,1 %
38,2 %
2014
2015
2016
2017
2018

MS Industrie AG, Munich
Consolidated income statement for the financial year 2018

| | 2018 TEUR | | 2017 TEUR |
|---|---|---|---|
| Revenues | | | |
| a) Revenues from industrial and real estate business | 282.625 | | 250.511 |
| b) Revenues from consulting and commissions | 128 | | 110 |
| | | 282.753 | 250.621 |
| Changes in inventory of work in process and finished goods | | 4.504 | 2.571 |
| Other income | | 4.148 | 5.582 |
| | | 291.405 | 258.774 |
| Cost of materials | | | |
| a) Costs of raw materials and consumables used and of goods purchased | 146.590 | | 127.231 |
| b) Costs of services | 8.491 | | 7.579 |
| | | 155.081 | 134.810 |
| Personnel expense | | 71.083 | 63.629 |
| Depreciation and amortisation expense | | | |
| a) Depreciation of property, plant and equipment | 11.990 | | 12.982 |
| b) Impairment losses | 27 | | 0 |
| c) Depreciation of investment property | 0 | | 75 |
| | | 12.017 | 13.057 |
| Impairment Loss (-) / Income (+) IFRS 9 | | 467 | 0 |
| Other expense | | 42.927 | 38.309 |
| Operating Profit | | 10.764 | 8.969 |
| Finance income | | 883 | 995 |
| Finance costs | | 2.401 | 2.065 |
| Share of profit of investments accounted for using the equity method | | 65 | 607 |
| Profit before income tax | | 9.311 | 8.506 |
| Income tax expense | | 2.163 | 1.546 |
| Profit for the year | | 7.148 | 6.960 |
| profit attributable to owners of the parent | | 7.190 | 7.022 |
| profit attributable to non-controlling interests | | -42 | -62 |
| | | 7.148 | 6.960 |
| Consolidated earnings per share, in EUR | | | |
| basic, after non-controlling interests | | 0,24 | 0,23 |
| diluted, after non-controlling interests | | 0,24 | 0,23 |
| Number of shares, average weighting | | | |
| basic | | 29.901.131 | 29.893.201 |
| diluted | | 29.901.131 | 29.893.201 |

MS Industrie AG, Munich, Consolidated statement of comprehensive income
for the financial year 2018

INDUSTRIE AG

| | 2018<br>TEUR | 2017<br>TEUR |
|---|---|---|
| Profit for the year | 7.148 | 6.960 |
| *Items that may be subsequently reclassified to profit or loss* | | |
| Change in value of available-for-sale financial assets (IAS 39) | 0 | 331 |
| Currency translation differences | 902 | -2.343 |
| | 902 | -2.012 |
| *Items that will not be reclassified to profit or loss* | | |
| Change in value of financial assets held for purpose of sale (IFRS 9) ("FVOCI") | 106 | 0 |
| Change in value of financial assets (IFRS 9) ("FVOCI") | -535 | 0 |
| Remeasurements of post employment benefit obligations | -72 | -73 |
| Actuarial gains/losses | 1 | -14 |
| Income taxes recorded in other comprehensive income | 20 | 24 |
| | -586 | -63 |
| Other comprehensive income for the year, net of tax | 422 | -2.075 |
| Total comprehensive income for the year | 7.570 | 4.885 |
| attributable to owners of the parent | 7.612 | 4.947 |
| attributable to non-controlling interests | -42 | -62 |
| | 7.570 | 4.885 |
| Consolidated earnings per share, in EUR | | |
| basic, after non-controlling interests | 0,24 | 0,23 |
| diluted, after non-controlling interests | 0,24 | 0,23 |
| Number of shares, average weighting | | |
| basic | 29.901.131 | 29.893.201 |
| diluted | 29.901.131 | 29.893.201 |

# MS Industrie AG, Munich

## Consolidated balance sheet as at December 31, 2018

| | 31.12.2018 TEUR | 31.12.2017 TEUR |
|---|---|---|
| **ASSETS** | | |
| Intangible assets | 2.817 | 3.528 |
| Property, plant and equipment | 55.247 | 51.150 |
| Investment property | 6.990 | 7.065 |
| Investments | 1.038 | 1.918 |
| Investments in associates | 3.230 | 3.192 |
| Deferred income tax assets | 208 | 86 |
| Other non-current financial assets | 4.930 | 4.734 |
| Other non-current assets | 430 | 516 |
| **Non-current assets** | **74.890** | **72.189** |
| Inventories | 41.494 | 41.847 |
| Trade receivables | 44.267 | 27.506 |
| Assets held for disposal, classified as held for sale | 1.194 | 0 |
| Cash and cash equivalents | 2.256 | 8.384 |
| Income tax assets | 118 | 512 |
| Contract assets | 4.238 | 0 |
| Other current financial assets | 896 | 548 |
| Other current assets | 1.717 | 1.723 |
| **Current assets** | **96.180** | **80.520** |
| **TOTAL ASSETS** | **171.070** | **152.709** |
| **EQUITY AND LIABILITIES** | | |
| Ordinary Shares (30.00 million shares less 91.320 treasury shares) | 29.909 | 29.894 |
| Share premium | 7.609 | 7.590 |
| Statutory reserve | 439 | 439 |
| Retained earnings | 3.946 | 3.931 |
| Other reserves | 3.106 | 1.794 |
| Group Reserves | 20.485 | 13.175 |
| Non-controlling interests | -181 | -139 |
| **Equity and non-controlling interests** | **65.313** | **56.684** |
| Non-current Borrowings | 26.962 | 17.808 |
| Provisions for pensions and similar obligations | 1.525 | 1.725 |
| Deferred income tax liabilities | 1.706 | 922 |
| Other non-current provisions and accruals | 389 | 382 |
| Other non-current financial liabilities | 12.785 | 14.010 |
| Other non-current liabilities | 693 | 947 |
| **Non-current provisions and liabilities** | **44.060** | **35.794** |
| Current Borrowings | 27.342 | 26.965 |
| Trade payables | 16.259 | 14.946 |
| Current income tax liabilities | 277 | 0 |
| Current provisions and accruals | 8.780 | 7.029 |
| Contract liabilities | 580 | 0 |
| Other current financial liabilities | 5.691 | 7.737 |
| Other current liabilities | 2.768 | 3.554 |
| **Current provisions and liabilities** | **61.697** | **60.231** |
| **TOTAL EQUITY AND LIABILITIES** | **171.070** | **152.709** |

MS Industrie AG, Munich

Consolidated cash flow statement 2018

| | 2018<br>TEUR | 2017<br>TEUR |
|---|---|---|
| Profit for the year | 7.148 | 6.960 |
| Income tax expense (recognised through profit and loss) | 2.163 | 1.546 |
| Finance income (recognised through profit and loss) | -883 | -995 |
| Finance costs (recognised through profit and loss) | 2.401 | 2.065 |
| Depreciation of property, plant and equipment and amortisation of intangible assets | 11.990 | 12.982 |
| Depreciation of investment property | 0 | 75 |
| *Material non-cash other expenses (+) or income (-):* | | |
| - Impairment losses | 27 | 0 |
| - Gains/losses on revaluation of investment property | 75 | 0 |
| Losses/gains (-) on investments accounted for using the equity method | -65 | -607 |
| Losses/gains (-) on disposal of property, plant and equipment and intangible assets | -91 | -4 |
| Losses/gains (-) on disposal of investments held for sale | -7 | -311 |
| Losses/gains (-) on deconsolidation | 0 | -1.379 |
| Increase/decrease (-) in inventories, trade receivables and other assets not assigned to investing or financing activities | -19.568 | -7.037 |
| Increase/decrease (-) in trade payables and other liabilities not assigned to investing or financing activities | 98 | -4.133 |
| Interest received | -122 | 110 |
| Interest paid | -1.197 | -1.952 |
| Income tax received | 0 | 115 |
| Income tax paid | -837 | -1.581 |
| **Net cash generated from operating activities** | **1.132** | **5.854** |
| Proceeds from sale of property, plant and equipment and intangible assets | 149 | 15 |
| Purchases of property, plant and equipment and intangible assets | -12.143 | -7.117 |
| Purchases of investment property | -63 | 0 |
| Proceeds from disposal of fully consolidated subsidaries  less cash and cash equivalents transferred under the sale | 0 | 1.246 |
| Disposal of borrowings due to deconsolidation | 0 | 0 |
| Proceeds from disposals of investments held for sale | 7 | 3.089 |
| Purchase of investments | -25 | -79 |
| Payments made for the granting of borrowings | -325 | -532 |
| Proceeds received from investments | 35 | 61 |
| **Net cash used in investing activities** | **-12.365** | **-3.317** |
| Repayments of debt-equivalent bonds | -200 | 0 |
| Proceeds from borrowings | 30.305 | 5.547 |
| Repayments of borrowings | -20.013 | -2.316 |
| Repayment mezzanine capital | -897 | 0 |
| Proceeds from finance lease transactions | 634 | 693 |
| Payments made for finance lease transactions | -4.013 | -5.600 |
| **Net cash used in financing activities** | **5.816** | **-1.676** |
| **Net increase / decrease in liquid funds** | **-5.417** | **861** |
| **Exchange gains / losses on liquid funds** | **0** | **-367** |
| Liquid funds at beginning of period | 1.389 | 895 |
| **Liquid funds at end of period** | **-4.028** | **1.389** |

MS INDUSTRIE AG

# MS Industrie AG, Munich

## EXTRACTS from the Group's management report for the financial year 2018

## Content

## 1. Report on economic situation

### 1.a. Macroeconomic and industry-related environment

The somewhat uncertain framework conditions still prevailing in the eurozone continued to adversely affect economic development and events on the financial markets over the past year. Nevertheless, the German economy once again proved to be stable overall throughout 2018 according to the report published by the Federal Statistical Office in Wiesbaden in January 2019, showing price-adjusted growth of the gross domestic product (GDP) of 1,5% (compared to 2,2% in 2017). The manufacturing sector (excluding the construction sector), which again accounted for a good quarter of the overall gross value added, also grew moderately by 1,0%. Thanks to record employment and further wage increases, consumer spending in particular provided momentum to the economy in the past year. Consumption was again higher than in the previous year, with private consumption increasing by a total of 1,0% and public consumer demand by a total of 1,1%. In total, consumer spending increased by 2,1%. Despite the uncertainty about future economic trends, businesses also felt encouraged to increase their capital spending. Expenditure on plant and machinery rose by 3,0% year-on-year, following a 2,9% increase in 2017. Once again, the German economy benefited above all from a strong domestic demand. German foreign trade also gained further momentum on an annual average in 2018: Germany exported 2,4% more goods and services on a price-adjusted basis than it did in 2017.[1]

Thus, the German economy once again proved to be able to assert itself in a challenging global economic environment, continuing its moderate growth throughout the year 2018: after price, seasonal and calendar adjustments, the gross domestic product in the fourth quarter matched the level of the previous quarter.[2] Following a boom period, the German economy thus returned to normal in 2018. Especially when comparing the optimistic expectations prevailing one year ago with the economic outlook of today, the cooling down of the economic climate is noticeable: in 2018, nearly all economic research institutes expected more than two percent growth for that year.

In the USA and Canada – together still forming one of MS Industrie AG's most important sales markets outside the EU accounting for a 38,5% (previous year: 35,2%) share in the Group's revenues for 2018 – economic development exceeded the growth rate in Germany with real GDP growth of around 2,9%.[3] This was due in part to the fact that in the USA a positive economic sentiment in the wake of the tax reform adopted in autumn 2017 and the end of the FED's zero-interest policy in particular were triggers for additional corporate investments.

In this global economic environment, the exchange rate of the US dollar to the euro fluctuated between values of 1,20 and 1,15 US dollars over the course of 2018. As at year end, the value of the euro was 1,14 US dollars, i.e. significantly lower than at the beginning of the year (1,20 US dollars).

Demand in the "Powertrain Technology" segment slightly increased, growing +3,2% overall in Germany and Europe.[4] The US commercial vehicle market, too, proved again to be much stronger than in the previous year. This applies particularly to one of our main customers in the US in 2018, Detroit Diesel Corporation ("DDC"), a supplier of engines for truck brands such as "Freightliner" and "Western Star".[5]

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[1] Source: German Federal Statistical Office, (Destatis) Subject matter series 18, series 1.1 of 15 January 2019.

[2] Source: German Federal Statistical Office, Press release No. 50 of 14 February 2019.

[3] Source: Statista, USA: Growth of real GDP, as at: 14 February 2019.

[4] Source: "ACEA", Commercial vehicle registrations, 24 January 2019.

[5] Source: Internal analyses.

MS Industrie AG is a group which, through its internationally operating subsidiaries, operates primarily in the industry sector (subgroup MS Technologie Group GmbH and Elektromotorenwerk Grünhain GmbH plus subsidiaries) as well as in the services sector and was therefore exposed to the general economic environment described above and the situation in the relevant sectors as prevailing in the financial year 2018.

### 1.b. Business development

The financial year 2018 was characterised by a marked increase in sales over the previous year, in particular at the Group's US site (in the main thanks to a pronounced recovery of truck sales owing to the positive economic development in the US). During the 2018 financial year, average order book levels in the "Powertrain" core segment were ranging clearly above the level of the previous year which still showed some signs of being affected by non-recurring effects relating to the US economy. This also applies to revenues generated by the two segments "Powertrain" and "Ultrasonic": the segments' revenues clearly outperformed the previous year and in total somewhat exceeded the originally planned values.

Since the Group is a supplier of heavy combustion engines, the demand for our products is particularly dependent on truck registration figures. In the North American market in particular, "Class 8" registrations in the financial year 2017 picked up again. Orders for heavy duty commercial vehicles ("Class 8") continued to expand in the NAFTA region in 2018, from over 20.000 units per month at the beginning of the financial year to an average of more than 25.000 units per month for the full year 2018.[6] Overall, the revenue increase in the US was complemented by additional growth in Europe and in the ultrasonic technology business throughout most of the year 2018, so that for the whole financial year 2018 total industrial revenues grew by around +13% compared to 2017.[7]

Just like in recent years, the order books of the Ultrasonic Technology Group are well filled at the beginning of the year 2019 and the order situation in the "Powertrain" core segment may be described as good. The machine park and equipment at the three German MS sites in Trossingen, Spaichingen and Zittau has been upgraded and extended considerably in the course of 2018. These positive developments have a positive impact on volumes reflected by an increase in the corresponding key figures for the financial year.

Most of the investments to support growth at the different sites of the Group have already been completed. This means that any additional requirement for capital expenditure in the coming years will be much below the average of recent years, unless any unforeseen new large-scale orders would involve increased capital spending. At the same time, we continue to expect a constant increase in capacity utilisation in the individual production areas.

We are once again entirely satisfied with the operating performance at the different earnings levels in the financial year 2018, given the positive development of sales volumes in Europe and the USA and the ongoing considerable structural adjustments in Germany with the new organisational, management and communication structure established in 2018 after the successful split-up of the former MS Spaichingen GmbH into several entities in 2016.

<u>The developments of the past financial year in detail:</u>

In 2018, the <u>MS Technologie Group (MS)</u> recorded subgroup revenues of around EUR 264 million compared to EUR 232 million in the previous year. MS operates predominantly in two market segments: "Powertrain Technology"

[6] Source: Rhein Report, January 2019, p. 26

[7] Source: Internal analyses.

(mechanical assemblies and components for the automotive industry, particularly commercial vehicles) and "Ultrasonic Technology" (special purpose machines for the automotive industry as well as ultrasonic welding and sealing systems and components, including for the packaging industry). MS is one of the few "single-source suppliers" in the automotive supply sector, especially to customers in the commercial vehicle market, and continues to maintain long-term supply agreements with its main customers.

With revenues of around EUR 19 million in the financial year 2018, and also around EUR 19 million in the financial year 2017, Elektromotorenwerk Grünhain GmbH (EMGR), including its new Bulgarian subsidiary, achieved revenues roughly on previous-year levels and an annual result according to HGB (German Commercial Code) for the past financial year before profit transfer / loss absorption of TEUR 136 (previous year: TEUR -160), despite a once again weaker economy towards the end of the year. EMGR is a successful manufacturer of customised electric motors in a variety of designs and of related products maintaining its own aluminum die-casting foundry. Besides meeting internal demands, the foundry also supplies external clients, mostly from the automotive industry but also in the field of heating systems. The production of custom-developed electric motors for applications in the bicycle and tricycle sectors commenced as planned in 2018 and production figures can be expected to rise considerably in 2019.

The financial situation of the Group continues to be in good order. Given a marked increase in total assets of 12,0%, the equity ratio improved somewhat, rising from 37,1% in the previous year to 38,2% in 2018. The main reasons for the increase in the equity ratio in 2018 over the previous year are the Group's total comprehensive income of EUR 7,6 million (previous year: EUR 4,9 million) as well as the adoption of IFRS 9 and IFRS 15 as of 1 January 2018, which has an impact of EUR 1,9 million not recognised in profit or loss, with a considerable increase in total assets.

With a marked increase in revenues, a clearly improved operating profit and a considerably weaker financial result, the earnings situation is characterised by pre- and post-tax profits on a slightly higher level than in the previous year. Income tax in the previous year was positively affected in the amount of EUR 0,8 million by deferred tax income arising in the USA as a result of the tax reform adopted there in December 2017.

In summary, we can state that we continue to be satisfied with the economic position of the MS Industrie Group as at the balance sheet date. Our confidence is bolstered by the good order situation currently reported by all the operating subsidiaries in the Group, despite the continued global economic uncertainties.

However, although sales volumes in the core segment "Powertrain" in the US continued to recover along with the general upturn in the underlying market, the previous year's projections were not met regarding the performance indicators cash flow from operating activities, cash flow from investing activities, equity ratio and net debt-to-equity ratio. In the 2017 Group management report, we projected a modest increase in the Group's industrial consolidated revenues of around 7% to around EUR 270 million. In fact, adjusted revenues rose by around 13% to around EUR 283 million in the reporting period. This means that the previous year's projection of a modest revenue increase of around 7% to around EUR 270 million was exceeded substantially. For the financial year 2018, we had anticipated a minor rise in EBITDA, a substantial improvement in the Group's key earnings figures EBIT and EBT, a slight increase in the EBIT margin, a constant gross margin as well as slightly improved earnings per share from continuing operations (excluding non-recurring items) and thus also a significant increase in Group equity. While not all of these expectations have materialised, despite the overall positive development of the market, the forecasts were still met to a substantial degree or only slightly missed (for further information on the development, see Section 2.d. Status of the Group further below). In addition, we had expected that cash flow from operating activities would again improve slightly over the previous year. Unfortunately, this expectation has not materialised. No significant changes had been anticipated for cash flow from investing activities compared to the previous year. This expectation, which was based on deliberate considerations, was not met. A number of steps had been initiated with the intention to further reduce the debt-to-equity ratio in the financial year and to significantly increase the equity ratio according to previous year's plans. Both expectations have not materialised (for further information on the development, see Section 2.d. Status of the Group further below).

In the previous year, we had anticipated for the financial year 2018 that the MS Technologie Group's revenues would slightly increase and the 2017 annual result would be stabilised. This objective was exceeded. The MS Technologie Group assumed for planning purposes that in the financial year 2018 revenues in the "Powertrain Technology" segment would be slightly ahead the previous year's level. The "Ultrasonic Technology" segment based its planning on the order backlog and anticipated a marked increase in revenues compared to 2017. Both expectations have materialised and/or have been substantially exceeded.

Despite the weaker performance of the electric motor business in the previous year, the management of Elektromotorenwerk Grünhain GmbH, Grünhain-Beierfeld (EMGR), an entity which is active in the "Powertrain - Electric" business, had anticipated a return to a more positive business development for 2018 with revenues further increasing and a positive annual result. Because of the difficult business environment in 2018, the former was only just attained.

For the development of non-financial performance indicators, the previous year's report had forecasted that the MS Industrie Group would do all it can to continue fulfilling all relevant environmental standards and to continue in its - to date successful - attempts to keep staff turnover as low as possible using staff retention programs. In view of the anticipated modest revenue growth, there were originally no plans to hire new staff in 2018, especially no specialists and managers. The Company envisaged the employment of temporary agency workers, however. As a result of the strong volume growth, which had not been projected in the annual planning for 2018, the Company increased its headcount moderately in the course of the financial year, also in order to be able to respond swiftly to further volume increases anticipated for the future. These are measures with which the Company also intends and has always intended to counteract a shortage of skilled workers and to prepare future managers for demanding tasks in a targeted manner.

Ongoing, individual job training and development continue to be regarded as a matter of great importance within the Group. The Company had also planned to maintain the existing high level of customer satisfaction as a minimum, and to further increase the already very high level of innovative strength while at the same time ensuring a constant delivery performance in all segments and product lines. All this has been implemented as planned. The Group's research and development spending was slightly up in the year under review from EUR 3,7 million to EUR 3,8 million, thus remaining at a very high level just like in previous years. The Group maintained its ability to deliver at all times and customer satisfaction continues to be very high.

## 1.c. Status of the Group

All figures are prepared in accordance with IFRS as adopted by the European Union.

### Earnings situation

The essential key figures of our Group are presented and explained in the following with a comparison with the previous year.

| | 1.1. to 31.12.2018 | | 1.1. to 31.12.2017 | | Difference | |
|---|---|---|---|---|---|---|
| | TEUR | % | TEUR | % | TEUR | % |
| **Revenues** | **282.753** | **100,0** | **250.621** | **100,0** | **32.132** | **12,8** |
| Other income | 4.148 | 1,5 | 5.582 | 2,2 | -1.434 | -25,7 |
| Cost of materials (incl. changes in inventory) | 150.577 | 53,3 | 132.239 | 52,8 | 18.338 | 13,9 |
| **Gross profit** | **136.324** | **48,2** | **123.964** | **49,5** | **12.360** | **10,0** |
| Personnel expense | 71.083 | 25,1 | 63.629 | 25,4 | 7.454 | 11,7 |
| Impairment Loss (-) / Income (+) IFRS 9 | 467 | 0,17 | | | | |
| Other expenses | 42.927 | 15,2 | 38.309 | 15,3 | 4.618 | 12,1 |
| **Earnings before interest, taxes, depreciation and amortisation (EBITDA)** | **22.781** | **8,1** | **22.026** | **8,8** | **755** | **3,4** |
| Depreciation and amortisation expense | 12.017 | 4,2 | 13.057 | 5,2 | -1.040 | -8,0 |
| **Operating profit (EBIT)** | **10.764** | **3,8** | **8.969** | **3,6** | **1.795** | **20,0** |
| Finance costs, net | -1.518 | -0,5 | -1.070 | -0,4 | -448 | 41,9 |
| Share of profit of investments accounted for using the equity method | 65 | 0,0 | 607 | 0,2 | -542 | -89,3 |
| **Consolidated profit before income tax (EBT)** | **9.311** | **3,3** | **8.506** | **3,4** | **805** | **9,5** |
| Income tax (expense) | 2.163 | 0,8 | 1.546 | 0,6 | 617 | 39,9 |
| **Consolidated profit for the year before non-controlling interests (EAT)** | **7.148** | **2,5** | **6.960** | **2,8** | **188** | **2,7** |
| Profit attributable to non-controlling interests | -42 | 0,0 | -62 | 0,0 | 20 | -32,3 |
| **Consolidated profit for the year after non-controlling interests (EAT)** | **7.190** | **2,5** | **7.022** | **2,8** | **168** | **2,4** |

Like in the previous year, no substantial non-recurring items arose in the current reporting period; therefore, no adjustments were required.

After a slight increase of around 6,3% in the previous year, external revenues rose again significantly in the reporting period by around 12,8% to around EUR 282,8 million. As a result, the previous year's forecast of a slight increase in revenues by around 7,2% to around EUR 270,0 million was clearly exceeded. The strong growth in revenues is mainly attributable to the US business of the MS Industrie Group, in particular the "Powertrain" segment, which was stronger again in line with expectations. The increase in revenues and the associated positive annual result projected in the previous year for the "Powertrain / Electric motors" sub-segment has also materialised. The revenues generated by Elektromotorenwerk Grünhain GmbH in 2018 were slightly above the previous year's level.

In geographic terms, revenues again developed quite heterogeneously: While there was only a slight increase in industrial revenues of around 7,6% in the domestic market – still the market with the highest revenues - exports to the second-strongest foreign market, the EU, rose again by around 33,6%. In the North America / Canada region, which remains the strongest foreign market with 38,5% of consolidated revenues, revenues increased by around 23,4%.

The revenues include primarily the revenues of TEUR 263.629 (previous year: TEUR 231.944) generated by the MS Technologie Group. They also include the revenues of the Elektromotorenwerk Grünhain Group of TEUR 18.990 (previous year: TEUR 18.561).

Other operating income includes in particular income from the reversal of provisions and other accruals as well as other income generated in prior periods totaling TEUR 1.112 (previous year: TEUR 1.685). Other operating income also includes exchange rate gains of TEUR 999 (previous year: TEUR 2.086) incurred by the MS Technologie Group.

The gross margin (revenues including changes in inventory plus other operating income minus cost of materials) as a percentage of revenues is 48,2% in the financial year (previous year: 49,5%).

The minor increase in the cost of materials ratio to 53,3% (previous year: 52,8%) is primarily due to the changes in the product mix of the "Powertrain Technology" segment (more material-intensive product groups).

Personnel expenses rose year-on-year by around 11,7%, i.e. more or less proportionately to revenues, with the average headcount increased by around 6,8% to 1.224 permanent employees (excluding temporary agency workers and trainees) (previous year: 1.146 employees).

As a result, earnings before interest, tax, depreciation and amortisation and impairment (EBITDA) were EUR 22,8 million (previous year: EUR 22,0 million). Thus, the previous year's forecast of a slight increase in EBITDA was met in 2018. The main reason for this is the market recovery in the USA, which had been firmly projected in the previous year and improved fixed cost allocation again.

As expected, depreciation and amortisation in the financial year 2018 slightly decreased by around 8,0% from TEUR 13.057 to TEUR 12.017.

Based on the substantial expansion in the Group's revenues and after increased personnel expenses, decreased depreciation and amortisation and significantly higher other operating expenses, earnings before interest and taxes (EBIT) were positive in the financial year 2017 at EUR 10,8 million (previous year: EUR 9,0 million). This confirms the previous year's forecast of a significant increase in EBIT in 2018.

The EBIT margin as a percentage of revenues is around 3,8% in the financial year 2018 (previous year: 3,6%). As described above, the somewhat higher EBIT margin can be explained by the fact that fixed costs did not rise proportionately with the strong growth in revenues.

The net financial result declined by around 41,9% year-on-year, mainly because of the Group's higher net financial debt. The net financial result includes financial income of TEUR 883 (previous year: TEUR 995) and finance costs of TEUR 2.401 (previous year: TEUR 2.065).

Financial income results partly, in the amount of TEUR 366 (previous year: TEUR 427), from the market valuation of financial derivatives, especially the fair value measurement of interest rate swaps.

Finance costs include EUR 1,8 million attributable to the MS Technologie Group (previous year: EUR 1,7 million).

The share of profit of investments accounted for using the equity method in the financial year 2018 amounts to TEUR 212 (previous year: TEUR 606) from the "at equity" valuation of the Beno Immobilien Group, Starnberg, and TEUR -145 (previous year: TEUR 59) from the "at equity" valuation of Shanghai MS soniTEC Co., Ltd., China and TEUR -2 (previous year: TEUR -58) from the "at equity" valuation of WTP Ultrasonic Industria e Comercio de Maquinas Ltda., Contagem City, Brazil.

At EUR 9,3 million, consolidated profit before income tax (EBT) is significantly higher than in the financial year 2017. Compared to the pre-tax profit of EUR 8,5 million in the previous year, this confirms the previous year's forecast anticipating a substantially improved pre-tax profit.

Consolidated profit for the year after non-controlling interests (EAT) is EUR 7,1 million (previous year: EUR 7,0 million). In the previous year, the strong cut in corporation tax from 35% to 21% under the tax reform in the USA had a positive impact of around EUR 0,8 million on EAT.

Rounded consolidated earnings per share rose from EUR 0,23 per share in the previous year to EUR 0,24 per share in the financial year under review. Thus, consolidated earnings per share from continuing operations have slightly improved, as projected in the previous year.

## Cash Situation

*Principles and objectives of financial management*

Ensuring financial flexibility is the highest priority in the Group's financing strategy. This flexibility is achieved through a wide selection of financial instruments and a high diversification of investors or financial institutions. The maturity profile of the Group's liabilities features a wide spread of maturities with a high proportion of medium and long-term financing. Market capacity, investor diversification, flexibility, credit requirements and the existing maturity profile are all taken into account in selecting financial instruments.

*Presentation and analysis of the financial position*

| | 2018 TEUR | 2017[8] TEUR |
|---|---|---|
| Net cash generated from operating activities | 1.132 | 5.854 |
| Net cash used in investing activities | -12.365 | -3.317 |
| Net cash used in financing activities | 5.816 | -1.676 |
| **Net decrease in cash and cash equivalents** | -5.417 | **861** |
| Exchange gains/losses on liquid funds | 0 | -367 |
| Liquid funds at beginning of period | 1.389 | 895 |
| **Liquid funds at end of period** | **-4.028** | **1.389** |

The decrease in liquid funds (liquid assets less current account liabilities) is mainly due to the anticipated negative cash flow from investing activities, which the Company was not able to compensate despite the positive cash flows from operating activities and from financing activities. The previous year's forecast of a slight improvement in cash flow from operating activities has not materialised.

The reduced cash flow from operating activities reflects the decline in cash flow from operations of MS Industrie Group in 2018 due to the expansion of working capital in the financial year. The negative cash flow from investing activities in particular reflects the expected investing activities of MS Industrie Group. Part of the capital expenditure in the financial year was realised through a finance lease (EUR 3,0 million; previous year: EUR 2,2 million) which did not affect cash flow at the time the investment was made, and through advance payments of EUR 3,5 million for two rotary indexing machines.

As at 31 December 2018, cash and cash equivalents amount to EUR 2,3 million (previous year: EUR 8,4 million). In addition, unused current account credit facilities of EUR 21,6 million are available (previous year: EUR 11,8 million), and current assets (EUR 96,2 million) exceed current liabilities (EUR 61,7 million) by EUR 34,5 million as at the balance sheet date.

Bank borrowings as at the balance sheet date are EUR 54,3 million of which EUR 35,5 million are subject to certain financial covenants. Unused credit facilities amount to EUR 21,6 million including EUR 13,5 million which were provided with financial covenants (refer to Section "Financing Risks" in Chapter 6 of the Opportunities and Risk Report).

[8] In the cash flow statement for the financial year 2017 the item "cash flow from investing activities" was reduced by EUR -4,4 million and "cash flow from financing activities" was increased by EUR + 4,4 million (adjustment according to IAS 8.49a). For further information see Note 10 in the Notes to Consolidated Financial Statements.

## Financial Situation

The essential changes to the Group's financial situation can be seen in the following illustration:

| | 31.12.2018 | | 31.12.2017 | | Difference | |
|---|---|---|---|---|---|---|
| | TEUR | % | TEUR | % | TEUR | % |
| **ASSETS** | | | | | | |
| Deferred income tax assets | 208 | 0,1 | 86 | 0,1 | 122 | >100,0 |
| Other non-current assets | 74.682 | 43,7 | 72.103 | 47,2 | 2.579 | 3,6 |
| Current assets | 96.180 | 56,2 | 80.520 | 52,7 | 15.660 | 19,4 |
| **Total assets** | **171.070** | **100,0** | **152.709** | **100,0** | **18.361** | **12,0** |

| | 31.12.2018 | | 31.12.2017 | | 31.12.2018 | |
|---|---|---|---|---|---|---|
| | TEUR | % | TEUR | % | TEUR | % |
| **EQUITY AND LIABILITIES** | | | | | | |
| Equity and non-controlling interests | 65.313 | 38,2 | 56.684 | 37,1 | 8.629 | 15,2 |
| Deferred income tax liabilities | 1.706 | 1,0 | 922 | 0,6 | 784 | 85,0 |
| Other debt | 104.051 | 60,8 | 95.103 | 62,3 | 8.948 | 9,4 |
| **Total equity and liabilities** | **171.070** | **100,0** | **152.709** | **100,0** | **18.361** | **12,0** |

Non-current assets in our Group increased by around 3,6% in the financial year 2018; they stand at around 43,7% of total assets (previous year: around 47,2%) so that the change was minor, however. The increase in non-current assets is primarily due to the planned capital expenditure in the financial year. Set against this are the scheduled amortisation of intangible assets and depreciation of plant and machinery as well as the disposal of investments no longer considered strategically important, such as the Zehnder Pumpen GmbH, Grünhain-Beierfeld.

The investment volume originally planned by the MS Technologie Group for 2018 was set at a total of around EUR 9,2 million, with EUR 6,2 million accounted for by the "Powertrain" segment, EUR 2,6 million by the "Ultrasonic" segment and EUR 0,4 million by the "Services" segment. The actual investment volume at MS Technologie Group turned out higher at a total of around EUR 14,8 million for 2018, with EUR 7,6 million spent on the "Powertrain" segment, EUR 4,0 million on the "Ultrasonic" segment and EUR 3,2 million on the "Services" segment. The deviation from projections mainly resulted from advance payments of EUR 3,5 million in total required for the purchase of two rotary indexing machines.

While current assets increased by around 19,4%, mainly due to growth of accounts receivable by around 60,9%, cash and cash equivalents decreased and inventories remained at the same high level. As a proportion of total assets, the percentage share of current assets of around 56,2% (previous year: around 52,7%) slightly increased towards the end of the financial year.

Net working capital (inventories, contract assets and trade accounts receivable minus trade accounts payable and contract liabilities) as at 31 December 2018 is EUR 73,2 million (previous year: EUR 54,4 million) and thus rose by around 34,5% year-on-year.

Compared to 31 December 2017, equity increased in absolute terms by EUR 8,6 million to EUR 65,3 million. This is primarily attributable to the Group's total comprehensive income for the year of EUR 7,6 million as well as to the adoption of IFRS 9 and IFRS 15 as of 1 January 2018, which has an impact of EUR 1,9 million (previous year: EUR 0,0 million) not recognised in profit or loss. The Group's equity ratio showed a slight increase compared to 31 December 2017: as a result of total assets expanding by 12,0%, the equity ratio is at around 38,2% as at the balance sheet date (31 December 2017: 37,1%). The main reasons for the increase in the equity ratio are also the Group's total comprehensive income as well as the adoption of IFRS 9 and IFRS 15 as of 1 January 2018, which has an impact of EUR 1,9 million (previous year: EUR 0,0 million) not recognised in profit or loss. This confirms the previous year's forecast of a slight increase in the equity ratio in the financial year 2018.

Other debt in the Group has substantially risen by around 9,4% to EUR 104,1 million. As a result, despite an increase in total assets of around 12,0%, the debt-to-equity ratio has unfortunately not remained stable as projected in the previous year's forecast.

The Group's net debt ratio (defined as net liabilities/equity) rose from 64,2% as at the end of 2017 to 79,7% as at the end of the financial year 2018. The net debt ratio is calculated by dividing the Company's liabilities, which are defined as current and non-current financial liabilities (excluding derivatives and financial guarantees) minus cash and bank balances, by its equity (the Group's entire capital and reserves).

Non-controlling interests as at 31 December 2018 are TEUR -181 (previous year: TEUR -139). As in the previous year, the non-controlling interests are completely attributable to the subsidiary of Elektromotorenwerk Grünhain GmbH.

**General statement on business performance and financial situation**

The financial year 2018 was still characterised by the Group's focus on the two business segments "Powertrain Technology" and "Ultrasonic Technology" and on further measures for the disposal of investments which are no longer strategically relevant.

The cash situation as at the end of 2018 and beginning of 2019 can still be described as sound, with significant available credit lines. All of the subsidiaries continue to be able to meet their payment obligations from ordinary activities in full.

Since the Group was able also in 2018 to generate a positive total comprehensive income, equity including non-controlling interests increased in absolute terms. The financial situation continues to be in good order, based on the slightly increased equity ratio of 38,2% (previous year: 37,1%).

Operating business in all operating subsidiaries in the first half of the financial year 2019 has developed according to plan until the date of preparation of these consolidated financial statements. Hence, the Group's financial, cash and earnings situation was also sound when these extracts from the Group's management report for 2018 were prepared.

Munich, 18 April 2019

MS Industrie AG

The Executive Board

Dr. Andreas Aufschnaiter
(Chairman)

Armin Distel

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