Special Steel Division

Market environment and business development

As was the case throughout the entire Group, growing regional political instability, economic embargos, often drastic declines in raw materials prices, and significant currency fluctuations dampened the Special Steel Division's economic environment in the past business year. The oil price that remained low reduced oil and natural gas exploration and the associated use of special steel in this important customer industry, leading to a substantial decrease in incoming orders from this sector. The division's sales in the mechanical engineering sector were adversely impacted by diminished demand, particularly from China, while in contrast, the trend in the aerospace sector continued to be positive. Demand in the tool steel segment also remained healthy, primarily due to a high level of incoming orders from the automotive industry.

Viewed regionally, the picture during the business year just ended varied widely from region to region. Despite a stable trend in the automotive and consumer goods industries and the continuing positive outlook in the aerospace sector, Europe otherwise remained a market with little growth momentum. Energy engineering (power plants), a sector which has been weak for years, did not demonstrate any noticeable trend toward recovery, and the mechanical engineering sector also remained below expectations. The low level of investment activity in the oil and natural gas industries worldwide has also had a considerable negative effect on the European suppliers of global oil field equipment manufacturers. The direct impact of the political conflict between Russia and Ukraine remained minimal, however, certain indirect effects, primarily in the mechanical engineering sector and in the agricultural industry were noticeable.

In the USA, business volume with Europe grew substantially in 2015/16, especially after the devaluation of the euro vis-à-vis the dollar. This applies particularly to the competitive position of the Special Steel Division vis-à-vis its North American competitors in the aerospace sector. Although business with the oil and natural gas industries has been marked by a dramatic slump since the summer of 2015, the oil and natural gas service center in Houston, Texas, USA, which was opened last year, demonstrated its competence as a flexible partner to cover requirements that arise on short notice, showing that a business expansion is possible even in times of crisis. Furthermore, as production capacity in the automotive sector, particularly in Mexico, was expanded, demand for tool steel was on a positive trajectory.

In South America, especially in Brazil, the economic climate in the past business year has continued to worsen. Industry, especially the entire automotive sector, again faced declining sales. Rising unemployment, falling income, and, not least, corruption scandals have depressed investment activity in all major industrial segments. The sole positive aspect of the economic trend in Brazil was the significantly lower rate of exchange of the Brazilian real, which improved its international competitiveness, especially with regard to exports to North America. In Asia, particularly in India and China, the division benefited from the favorable economic trend in the customer industries important for its products so that business activities in this region were expanded compared to previous years.

In the business year 2015/16, the High Performance Metals (production) business segment

Key figures of the Special Steel Division[1]

In millions of euros	2014/15	2015/16	Change in %
Revenue	2,777.4	2,650.9	–4.6
EBITDA	406.9	364.1	–10.5
EBITDA margin	14.6%	13.7%	
EBIT	253.6	227.2	–10.4
EBIT margin	9.1%	8.6%	
Employees (full-time equivalent)	13,490	13,470	–0.2

[1] Business year 2014/15, Q1 2015/16 and Q2 2015/16 retroactively adjusted.
Further details are given in the Notes to the consolidated financial statements 2015/16 "B. Summary of accounting policies".

faced not only less demand but also had to contend with customers' high inventory levels. As a result, temporary capacity adjustments had to be made at individual locations. Nevertheless, sales of premium products, e.g., remelted and powder-metallurgical steel, increased even further. The market situation for products for the heavy mechanical engineering industry and the energy engineering industry remained challenging. In contrast, demand for special steel for the aerospace industry continued to be very satisfactory. The restructuring process at the Buderus Edelstahl production site in Wetzlar, Germany, continued systematically. The focus remains on a drastic reduction in costs and a partial strategic reorientation toward tool steel products.

In the Value-Added Services business segment, service offerings were increased on a broad basis in the past business year by expanding existing sites and establishing and acquiring new ones (see Chapters "Investments" and "Acquisitions"). By investing in this business segment with its already existing 160 service centers, the division is continuing to expand its leading position as a premium service provider for toolmaking worldwide. Despite challenging market conditions, this resulted in an increase of delivery volume with relatively minor price fluctuation.

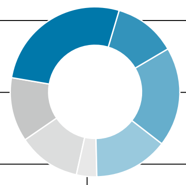
Financial key performance indicators

Low demand from the oil and natural gas industries in the business year 2015/16 resulted largely in a reduction of the division's delivery volume. Premium steel, however, was the exception, with deliveries increasing. At the same time, passing on declining costs for alloy metals to customers resulted in falling prices, although the weaker euro vis-à-vis the US dollar had positive revenue and earnings effects for deliveries to US dollar regions. Nevertheless, revenue fell by 4.6% overall from EUR 2,777.4 million in 2014/15 to EUR 2,650.9 million in 2015/16. The declining raw materials prices affected not only the price level but also required value adjustments of inventory that had commensurate negative effects on earnings. The continuation of comprehensive cost optimization programs compensated this trend in part, however, the operating result (EBITDA) dropped by 10.5% from EUR 406.9 million to EUR 364.1 million. As a result, at 13.7%, the EBITDA margin in the business year 2015/16 was also lower than the previous year's figure of 14.6%. In the same time period, EBIT fell by 10.4% from EUR 253.6 million to EUR 227.2 million, while the EBIT margin went down from 9.1% to 8.6%.

A direct quarter-to-quarter comparison between the third and the fourth quarter of 2015/16 showed a significant increase of the key figures, primarily a result of seasonal effects. Overall, revenue increased due to a higher delivery volume in the fourth quarter by 8.1% from EUR 616.0 million to EUR 666.1 million. Concurrently, EBITDA rose by 41.2% from EUR 73.8 million (margin: 12.0%) to EUR 104.2 million (margin: 15.6%). EBIT escalated sharply by 70.4%, going from EUR 40.5 million in the third quarter of 2015/16 to EUR 69.0 million in the fourth quarter of 2015/16, with the EBIT margin increasing in a direct quarter-to-quarter comparison from 6.6% to 10.4%.
As of March 31, 2016, the Special Steel Division had 13,470 employees (FTE). This is 0.2% less than on the previous year's reporting date (13,490 FTE), although the division made acquisitions in the business year 2015/16.

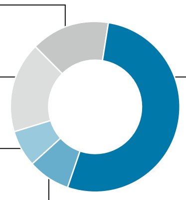
Customers of the Special Steel Division

As percentage of divisional revenue
Business year 2015/16



Markets of the Special Steel Division

As percentage of divisional revenue
Business year 2015/16



Quarterly development of the Special Steel Division[1]

In millions of euros	1st quarter 2015/16	2nd quarter 2015/16	3rd quarter 2015/16	4th quarter 2015/16	BY 2015/16
Revenue	709.0	659.8	616.0	666.1	2,650.9
EBITDA	99.9	86.2	73.8	104.2	364.1
EBITDA margin	14.1%	13.1%	12.0%	15.6%	13.7%
EBIT	65.2	52.5	40.5	69.0	227.2
EBIT margin	9.2%	8.0%	6.6%	10.4%	8.6%
Employees (full-time equivalent)	13,411	13,434	13,301	13,470	13,470

[1] Business year 2014/15, Q 1 2015/16 and Q2 2015/16 retroactively adjusted.
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