REPORT OF THE MANAGEMENT

INHOUSE BANKING

Key events

Record profits thanks to strong growth for the Würth Group

Bolstered by the central banks' continued expansionary monetary policy, the Würth Group's markets grew more than expected in 2017. The Würth Group made successful use of this economic tailwind and, with organic sales growth of 8.2%, achieved the highest value in seven years. Better capacity utilisation enabled a significant improvement in profitability. The increased need for funds from organic growth, from capital expenditure and from the acquisition of five companies could be financed to a large extent by the cash flow generated.

In the Inhouse Banking Division, therefore, client-based transaction volume increased significantly in all areas of business and capacity utilisation was correspondingly high, whereas the volume of net lendings stagnated during the year. Investing liquidity reserves was a challenge for Inhouse Banking despite support from long-standing partner banks and the various measures to optimise cash flows. It was not possible to avoid negative interest entirely. Nonetheless, the surprisingly strong volume growth enabled a record operating result of EUR 40.0 million[1] to be achieved.

Protecting Group financing from the risks of interest rate hikes and from any rise in liquidity requirements

Companies are operating at full capacity in North America and increasingly in European countries, which means that the central banks may begin normalising monetary policy. Thus, a possible trend towards rising interest rates should not come as a surprise. The Central Managing Board of the Würth Group therefore decided at a Finance Committee meeting in the summer of 2017 to use forward-start interest rate swaps to hedge a financing volume of EUR 250 million against rising interest rates, irrespective of the precise point in time of any new capital market financing. This was put in place by Würth Finance International B.V. with three partner banks.

In parallel, the Würth Group, acting through Würth Finance International B.V., arranged an early one-year extension to 2022 of the existing syndicated credit line and increased the total by EUR 200 million to EUR 400 million. The credit line, which has never been utilised in past years, serves as a back-up facility to ensure sufficient liquidity for the Würth Group.

Varying degrees of progress in digitalisation projects

As in many other parts of the economy, a steady and lively stream of new technological options and services for corporate treasury organisations is currently appearing on the market under the banner of digitalisation. The management of Inhouse Banking is observing this trend very carefully, is maintaining a close dialogue with fellow treasurers, specialised advisors, software firms and financial service providers, is involved in treasury associations and user groups, and is making use of the new solutions to improve the division's own client services and to optimise its processes. In 2017 the main projects in strategic areas of action were unchanged: the establishment and expansion of Omnichannel Payment Gateway services and the renewal of the IT infrastructure for handling international payments (GPS Payment & Factoring project) for the Würth Finance Group.

Würth Omnichannel Payment Gateway (WOPG) services

B2B customers of the Würth Group, especially in the branches and in e-commerce, expect various payment options that they have long been using as private consumers, such as credit cards, PayPal and other payment instruments. Würth is therefore setting up the corresponding infrastructure worldwide, based mainly on the WOPG platform of the Würth Finance Group. By 31 December 2017 around 500 POS terminals of the Würth Finance Group were in operation at Würth Line companies in Germany and the Netherlands, including payment handling via the WOPG platform. The same applies to the e-commerce solutions in the United Kingdom. The new technology will also be introduced shortly in China and at other Group companies. A variety of projects are in the pipeline.

GPS Payment & Factoring project

Release 1.0 of the GPS project went live at the beginning of April 2017 with account management functions. The subsequent rectification work required was more extensive than expected, resulting in delays in the development and establishment of test libraries for release 2.0 for handling international payments and the factoring processes. The system is expected to go live by the end of 2018 after comprehensive testing and parallel operations lasting several months. In order to prevent further delays, the project resources for the next project phases will be selectively increased.

[1] Not included in these figures are the effects impacting profit and loss in the IFRS accounts from a) the marking-to-market valuation of outstanding interest rate derivatives to hedge interest rate risks with an effect of EUR –4.4 million (previous year: EUR –4.3 million) and b) a one-time reduction of pension plan liabilities amounting to EUR 0.5 million by the amendment of the benefit plan for the employees in Switzerland.

"Giving up-and-coming talents opportunities to have an impact and help shape things is the best investment in the effectiveness and future success of the Würth Finance Group. I am guided by this conviction."

Roman Fust
Managing Director, Würth Finance International B.V.

Business performance

Inhouse Banking recorded a good result for 2017, reflecting healthy growth at the Würth Group. The volumes handled by the central settlement of payments to suppliers and in intercompany factoring activities increased at a double-digit percentage pace and led to corresponding income growth. Revenue reached EUR 59.7 million[1] in the year under review (previous year: EUR 55.4 million). An even stronger increase was prevented by stagnating net interest income and lower year-on-year revenues from the IBB participation and securities investments.

Operating expenses rose by just under 2% to EUR 19.7 million[2]. This increase was mainly attributable to higher expenses for the GPS project and personnel costs. The average headcount rose in the course of 2017 to 61 employees (previous year: 60 employees).

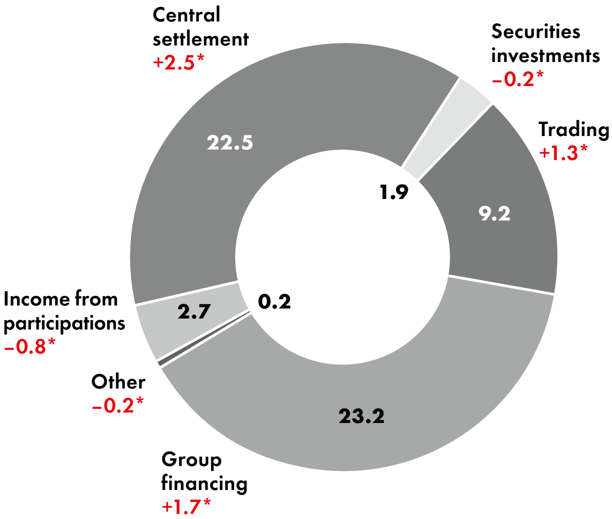
The pre-tax operating result increased by 11.4% to EUR 40.0 million.[1,2] The productivity of the Inhouse Banking Division, based on the cost-income ratio, improved from 35.2% to 33.1%.

Group financing

The Würth Group's net debt remained stable in the first half of 2017 and stepped up in the second half due to an increase of inventories. Gross cash flow of EUR 1,048 million (previous year: EUR 900 million) was almost sufficient to finance capital investment and acquisitions totalling EUR 567 million (previous year: EUR 546 million), an increase in net working capital of EUR 389 million (previous year: EUR 112 million) and net dividends to shareholders of EUR 101 million (unchanged).

Income Distribution

in million EUR



*Change vis-à-vis 2016

[1] Not included in these figures are the effects impacting profit and loss in the IFRS accounts from the marking-to-market valuation of outstanding interest rate derivatives to hedge interest rate risks with an effect of EUR −4.4 million (previous year: EUR −4.3 million)
[2] Not included in these figures are the effects impacting profit and loss in the IFRS accounts from a one-time reduction of pension plan liabilities amounting to EUR 0.5 million by the amendment of the benefit plan for the employees in Switzerland.

Accordingly, the credit metrics of the Würth Group improved. For example, the ratio of net debt to EBITDA compared to December 2016 declined slightly to 0.93×.

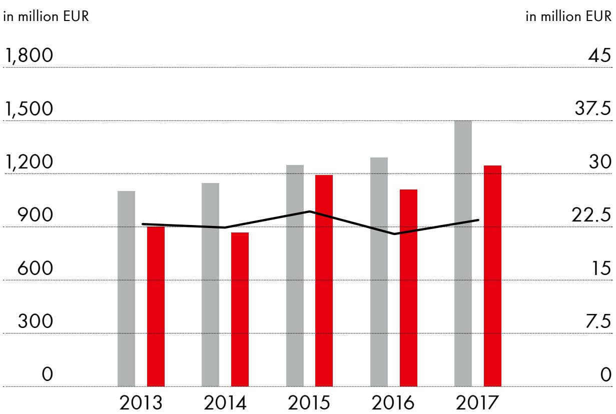
Intra-group net lending by the Würth Finance Group stagnated in the course of the year at around EUR 1,150 million. Short-term loans were preferred, resulting in a growing proportion of lendings with terms of less than one year. Liquid assets fluctuated on average between EUR 570 million and 670 million, around 100 million more than the 2016 values. The balance sheet total of the Würth Finance Group remained relatively stable over the course of financial year 2017 and as at 31 December 2017 totalled EUR 2,535 million (31 December 2016: EUR 2,457 million).

The sensitivity of shareholders' equity to interest rate changes was reduced only slightly from 9.2% to 7.7% as at 31 December 2017 due to the arrangement of new interest rate hedging for future capital market financing.

The Würth Group's strategy of progressive centralisation of procurement led to an above-average rise in intra-group sales of almost 13% in the financial year. The factoring volume handled through the Würth Finance Group increased by 13.4%.

Net interest income increased by EUR 1.7 million to EUR 23.2 million for financial year 2017. These figures do not include the effects from the valuation of interest rate derivatives used to actively manage interest rate risk. The lower euro yield curve compared to the previous year led to valuation losses amounting to EUR 4.4 million, which are reported in the IFRS accounts.

Group Financing: Volume and Revenue from Intra-Group Lendings



Factoring volume
Net lending as at 31.12.2017
— Net interest income (right-hand scale)

Würth Omnichannel Payment Gateway (WOPG) services

The success of the Würth Group is based on selling through multiple channels. Besides direct selling, customer contact through e-commerce and in the branches are gaining in importance. Würth is therefore setting up the corresponding infrastructure worldwide, based mainly on the WOPG platform at the Würth Finance Group.

Digitalisation is swiftly transforming the payments environment, with new providers appearing on the market and procedures being accelerated and simplified. The aim is to ensure that the shopping experience at Würth is not hampered by the payment process. Customers must be able to choose from the payment options that have long been available to them as private consumers, such as credit cards, PayPal and local payment instruments.

By establishing the central yet flexible WOPG platform solution for all Würth companies, resources can be saved and economies of scale can be achieved. Furthermore, a high standard of security and quality in terms of technical and organisational implementation can be ensured.

Another advantage of centralisation is in the processing and analysis of data: Inhouse Banking can set up the interfaces with providers, use the existing online communication platform and analyse data for the entire Würth Group, while adhering to international data protection legislation.

Services

Implementation: advice, project support, integration

Operation: support, data analysis

Payment Gateway: payment processing

POS terminals

"The services and solutions of the Würth Finance Group help our clients to deal with financial risks. This will be particularly pertinent if the economy fails to meet the high expectations in 2018."

Björn van Odijk
Managing Director, Würth Finance International B. V.

Income from participations

In order to strengthen the core capital of Internationales Bankhaus Bodensee AG (IBB), the Würth Finance Group committed a total of EUR 44.5 million (2016: EUR 54.5 million) in the form of a silent participation and a capital relinquishment. This participation contributed income of EUR 2.7 million in financial year 2017 (2016: EUR 3.5 million). The plan is to reduce this commitment continuously. Information on the business performance and financial position of IBB may be found on the website www.ibb-ag.com.

Central settlement of payments to suppliers

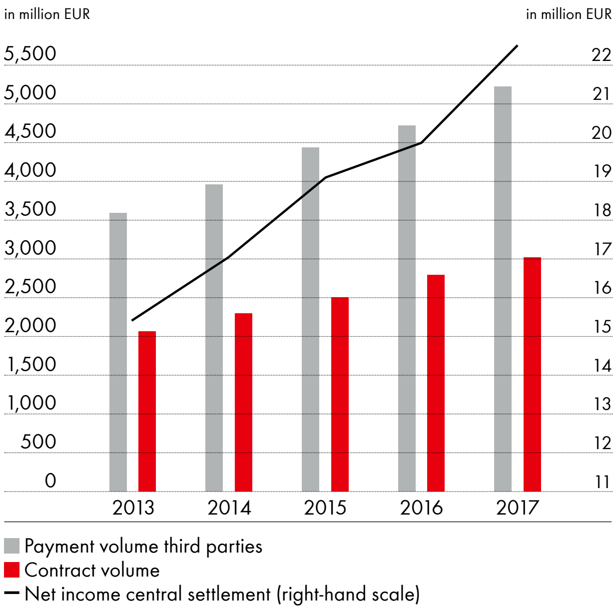
In parallel with sales Group purchasing volumes rose in the year under review, which in turn affected the central settlement of payments made by the Würth Finance Group. The total volume of 450,000 payments to suppliers processed through Inhouse Banking rose compared to 2016 by 9.7% to EUR 5,226 million.

The Würth Group constantly strives to improve business relations with its suppliers. This includes integrating all suppliers into the central settlement facility managed by the Würth Finance Group. As at end-2017, more than 7,600 contractual suppliers with sales of EUR 3,000 million had entrusted the processing of payments to Inhouse Banking. Thus, central settlement income improved by EUR 2.5 million to EUR 22.5 million.

Securities investments

The volume of securities investments was progressively increased over the course of the financial year as planned, rising from EUR 80 million to EUR 100 million. No change was made to the conservative investment strategy: more than 70% of funds were invested in investment grade corporate bonds with a relatively short duration. The share of equities was kept below 10% throughout the year. The fluctuation of the portfolio value was correspondingly low.

Central Settlement: Payment Volume/Revenue



The net performance of the securities portfolio was EUR 1.8 million (previous year: EUR 2.1 million). This equates to a return of 2.1% and exceeds the benchmark (three-month money market deposit plus 200 basis points). With the financial markets doing extremely well in the last financial year, investments in bonds and – with double-digit returns on the capital invested – equities and real estate contributed to this excellent result.

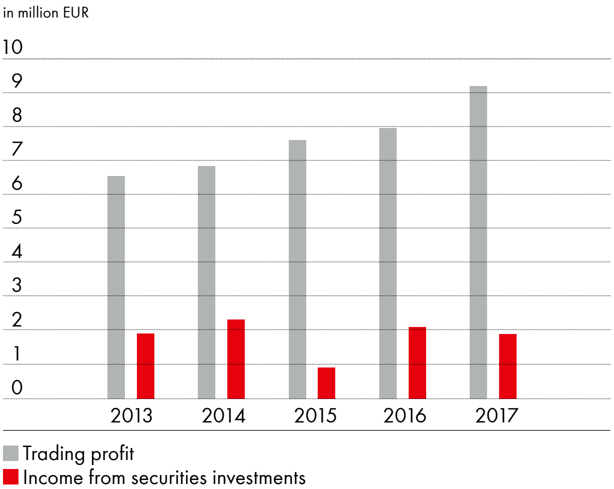
Currency hedging and trading with financial instruments

The euro and the US dollar are by far the most important currencies for the Würth Group. While the euro appreciated significantly in 2017 on a trade-weighted basis, the US dollar steadily lost value as the year progressed. Many Group companies obtain goods from suppliers in the Eurozone, so the strength of the euro towards the end of the year put pressure on their margins, at least for a time.

Würth companies selectively hedge their currency risk with Inhouse Banking in order to smooth out the effects of short-term fluctuations on their results. The volumes traded in foreign currency transactions increased by 21% to EUR 1.7 billion.

These foreign currency flows represent the basis for the trading activities of the Würth Finance Group. While adhering to the limits required by internal regulations, the traders constantly monitor and control positions by concluding countertrades with the trading units of the company's banking partners. There are also smaller trading limits for positions on the bond, equity and commodity markets. In 2017 income of EUR 9.2 million was generated through trading activities, 16% more than in the previous year.

Trading/Securities Investments: Income Development



Outlook for 2018

Overall, conditions for growth at the Würth Group and thus the prospects for the Inhouse Banking Division of the Würth Finance Group remain positive. The Management expects the operating result in 2018 will be above the previous year. The aim is to grow revenues from central settlement and intercompany factoring activities at a mid-single-digit percentage pace. The redemption of the EUR 500 million 2011–2018 bond will reduce interest expense in the second half of the year, even if new funds are obtained from the capital markets in the course of the year.

With regard to expenses, high costs will continue to be incurred for the GPS project in 2018. Thus, no notable relief for the operating result is anticipated. The new payments infrastructure is expected to be available in the course of the year, enabling efficiency gains. Another project is the renewal of the electronic communication platform to improve benefits to clients. At the same time, the company must initiate appropriate organisational and technical measures to take account of the increasing risk from cyberattacks – and the associated considerable potential for financial loss – and of the current tightening of regulatory requirements applying to data protection.

In addition, resources will continue to be devoted to developing and fostering staff so that Inhouse Banking at the Würth Finance Group can continue to fulfil its role as the central treasury competence centre for the Würth Group.

MANAGEMENT WÜRTH FINANCE INTERNATIONAL B.V.
from left to right: **Jorre van Schipstal** | **Roman Fust** | **Daniel Ochsner** | **Patrik Imholz** | **Björn van Odijk**

INHOUSE BANKING AT A GLANCE

Core business

The Inhouse Banking Division of the Würth Finance Group monitors the financial risks incurred by the Würth Group and takes the necessary measures to retain the financial stability of the Group.

In close collaboration with Group Management and the operational Group companies, the Inhouse Banking Division ensures that the necessary liquid funds are available to the Würth Group at all times and employs the Group's funds in an optimal manner. The division consists of the legal entities Würth Finance International B.V. and Würth Invest AG.

Facts and figures (at 31 December 2017)

68 employees (59.3 FTE) at the offices in Den Bosch, the Netherlands, and Rorschach, Switzerland

450,000 payment transactions with a volume of EUR 5,226 million in the year under review

Outstanding capital market funding as at 31.12.2017: three transactions with a total volume of EUR 1,500 million

Account relationships with over 400 Würth Group companies

2,960 foreign exchange transactions with 240 Group companies and a hedging volume totalling EUR 832 million

5,390 treasury transactions with external counterparties (banks)

Services

Central settlement of payments to suppliers

- Service provider for the central settlement of payments to beneficiaries worldwide
- Collection of outstanding invoices on behalf of over 7,000 Würth Group suppliers vis-à-vis all Group companies and, to a certain extent, insurance of default risk

Group financing and risk management

- Financing of the Würth Group on the capital market, principally by means of bond issues
- Competence centre and interface for banks, investors, financial market regulators, rating agencies and credit analysts
- Provision of comprehensive advice and a wide range of treasury products to Group companies
- Central management of bank accounts and financial risk management for the Würth Group

Cash and securities investments

- Securing of strategic freedom to act by managing the cash reserves of the Würth Group
- Central management of financial investments in the conflicting areas of security, liquidity and return