Report of the management

# INHOUSE BANKING

## Alternative Performance Measures (APMs)

In presenting and discussing the Würth Finance Group's financial position, operating results and net profit, management uses certain alternative performance measures not defined by IFRS. These alternative performance measures (APMs) should not be viewed in isolation as alternatives to the equivalent IFRS measures and should be used as supplementary information in conjunction with the most directly comparable IFRS measures. Alternative Performance Measures do not have standardised meaning under IFRS, and therefore may not be comparable to similar measures presented by other companies.

To afford a better overview of the development of the Inhouse Banking activities and their added value for the Würth Group, APM adjustments are made that impact the operating income and the net profit of the Inhouse Banking Division, which can be specified as follows:

| in TEUR | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|---|
| Hedge accounting effect management accounting | 8,438 | 4,297 | 4,353 | 3,742 | 2,993 |
| Impact of adoption of IFRS 9 | 0 | 0 | 0 | 3,698 | -739 |

- Hedge accounting effect management accounting refers to the effect of the market valuation of interest rate derivatives to hedge the interest rate risk where historically no hedge accounting was applied. As of the implementation of IFRS 9 Hedge Accounting, new hedge relations will be presented as such.
- Impact of adoption of IFRS 9 refers only to related party losses and therefore does not apply to the Würth Group.

## 2019

| in TEUR | Inhouse banking | Hedge accounting effect management accounting | Impact of adoption of IFRS 9 | Segment inhouse banking |
|---|---|---|---|---|
| **Income distribution** | | | | |
| Group financing | 36,157 | –3,062 | 1,005 | 34,100 |
| Credit loss (expenses)/recovery | 0 | 0 | 1,005 | 1,005 |
| Income from factoring activities | 16,419 | 0 | 0 | 16,419 |
| Interest income | 16,872 | –3,062 | 0 | 13,810 |
| Other ordinary income | 2,866 | 0 | 0 | 2,866 |
| Other | 1,513 | 0 | 0 | 1,513 |
| Income from participations | 1,353 | 0 | 0 | 1,353 |
| Central settlement | 25,220 | 0 | 0 | 25,220 |
| Income from trading activities and financial instruments | 15,174 | 69 | –266 | 14,977 |
| Securities investments | 4,447 | 0 | 0 | 4,447 |
| Trading | 10,727 | 69 | –266 | 10,530 |
| **Total income** | **76,551** | **–2,993** | **739** | **74,297** |
| **Total expenses** | **–22,018** | | | **–22,018** |
| **Profit Inhouse Banking** | **54,533** | **–2,993** | **739** | **52,279** |

| | Inhouse banking | External financial services | Eliminations | Total |
|---|---|---|---|---|
| **Segment profit before taxes (adjusted)** | 52,279 | 385 | 128 | 52,792 |

## 2018

| in TEUR | Inhouse banking | Hedge accounting effect management accounting | Impact of adoption of IFRS 9 | Segment inhouse banking |
|---|---|---|---|---|
| **Income distribution** | | | | |
| Group financing | 32,283 | –3,956 | –3,698 | 24,629 |
| Credit loss (expenses)/recovery | 0 | 0 | –3,698 | –3,698 |
| Income from factoring activities | 16,018 | 0 | 0 | 16,018 |
| Interest income | 12,977 | –3,956 | 0 | 9,021 |
| Other ordinary income | 3,288 | 0 | 0 | 3,288 |
| Other | 1,285 | 0 | 0 | 1,285 |
| Income from participations | 2,003 | 0 | 0 | 2,003 |
| Central settlement | 25,515 | 0 | 0 | 25,515 |
| Income from trading activities and financial instruments | 7,711 | 214 | | 7,925 |
| Securities investments | –2,366 | 0 | 0 | –2,366 |
| Trading | 10,077 | 214 | 0 | 10,291 |
| **Total income** | **65,509** | **–3,742** | **–3,698** | **58,069** |
| **Total expenses** | **–20,133** | | | **–20,133** |
| **Profit Inhouse Banking** | **45,376** | **–3,742** | **–3,698** | **37,936** |

| | Inhouse banking | External financial services | Eliminations | Total |
|---|---|---|---|---|
| **Segment profit before taxes (adjusted)** | 37,936 | 483 | 97 | 38,516 |

The Inhouse Banking Division and more precisely Würth Finance International B.V. is recognised as a central treasury competence centre. To keep it that way, the strategic fields of action with regard to the offered services and performance are geared towards the relevant drivers: the growth plans of the Würth Group for the next five years, the ongoing digital transformation of the financial and banking business and the development of the world economy and financial markets.

Derived from the resulting opportunities and risks, management focuses on ensuring the necessary technical and organisational capacities, the targeted promotion and further development of employees, the strengthening of ICT management skills (including cyber risk management) and the active management of banking policy and financial risk management.

With regard to the further development of the service range, the focus is on process optimisation and ancillary services for the Würth Group companies. Performance in Inhouse Banking is all about the ability to manage data: the efficient and secure flow of data between different systems, the availability and user-friendly preparation of the relevant information and the quality of the data management.

Pleasant progress was made in 2019 in this regard, but not all goals were achieved in full or just with a delay. Towards the end of the year, preparations for the extensive migration of intercompany transactions to a customised electronic trading platform were in full swing.

## Key events

**Record profit**

The stars were aligned for the Inhouse Banking Division in financial year 2019. The record set in 2018 was again significantly exceeded, with an adjusted pre-tax operating result of EUR 54.5 million, representing a year-on-year increase of 20%, or EUR 9.2 million. This is all the more encouraging given that this improved result was achieved while our parent group experienced slowing momentum. The Würth Group was hampered by the gloomy global economic outlook, with its revenue growth falling short of expectations.

The new record result in the Inhouse Banking Division was achieved mainly thanks to booming equity markets and an active interest rate risk management, benefiting from the ultra-low interest rates in the euro area. In particular, around two-thirds of the sharp improvement in results was attributable to securities investments. By contrast, the business units that have a strong correlation with the Würth Group's core business (e.g. intercompany financing and central settlement of supplier payments) recorded lacklustre performance. In summary, the success in 2019 was mainly attributable to three factors:

1.) Active securities portfolio management

2.) Reduction of bond financing costs (including receiver interest rate swaps)

3.) Targeted use of opportunities for short-term refinancing at negative interest rates

"Strong commitment combined with mental resilience, diverse and complementary skills, and mutual trust – including the support of the Management and the Board of Directors – were the keys to the GPS project's success. Everyone involved should be proud."

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

**Economic conditions**
The defining themes of the year, including Brexit, trade disputes and the economic slowdown, had already become apparent by the end of 2018. There were very few positive surprises. Hopes of a swift resolution to the trade disputes, major structural reforms or effective influence from the World Trade Organization dissipated during the year. Overall, the long-standing economic upswing lost considerable momentum, and economic forecasts, including the OECD's, were repeatedly downgraded.

However, things were not all bad: unlike the industrial sector (especially the automotive industry), private consumption proved reasonably resilient to market conditions, doubtless bolstered by the still positive employment environment.

But the most significant stimulus came from central banks, which again bailed out market participants by further easing their ultra-expansionary monetary policy. These institutions showed that they still have monetary policy ammunition by again cutting interest rates and reviving asset purchase programmes. As this became apparent, the financial markets relaxed, enabling the stock markets to reach new highs.

Stock market indices subsequently performed very strongly (MSCI World: +26%), reflecting the hope that the worst was over and the fact that, given the negative interest rate environment, there was an absence of available alternatives. Overall, the impression grew that the markets are becoming increasingly political.

**Successful implementation of the new Global Payment System (GPS)**
After going live in May 2019, the GPS system was subsequently stabilised and its unlimited effectiveness was demonstrated, meaning that the project was successfully completed in autumn 2019. The replacement of the IT infrastructure for processing around 700,000 international payments a year – with several million individual items in over 30 currencies and a volume of around EUR 7,500 million – has been the largest and most difficult corporate project in the 40-year history of Würth Finance International B.V. The successful implementation pays testament to the excellent work by the whole project team.

## Business performance

### Securities investments

The sharp decrease in interest rates, which began in the autumn of 2018, dominated the 2019 investment year. Interest rates were on an almost unbroken downward trajectory until late summer, when a slight recovery set in. With regard to medium to long-term liquidity management, this meant that it was virtually impossible to find government or corporate bonds with an acceptable risk/return profile. With negative yields to maturity, attractive alternatives were scarce, which led to a significant reduction in bond holdings. At the start of 2019, the investment volume was EUR 81 million, compared with just EUR 63 million at the end of the year.

Although the equity allocation was kept quite low in 2019, with an exposure of between EUR 3.5 million and EUR 10.6 million (average: EUR 6.1 million), it accounted for around half of the securities portfolio's return. The remainder was attributable to bonds and, to a lesser extent, commodities. With net earnings of EUR 4.5 million total performance was 5.6%, beating the expectations by far.

### Group Financing

Also in 2019 the Würth Group followed its well-balanced growth path, based on a solid financing structure: while it invested a new record amount of EUR 710 million in capital expenditure, net working capital increased below average compared to sales growth.

While the Würth Group's shareholders' equity rose by over EUR 300 million to EUR 5,500 million, net debt went up just EUR 140 million to EUR 1,400 million. To finance this additional funding need, Würth Finance International B.V. issued commercial papers at negative interest rates.

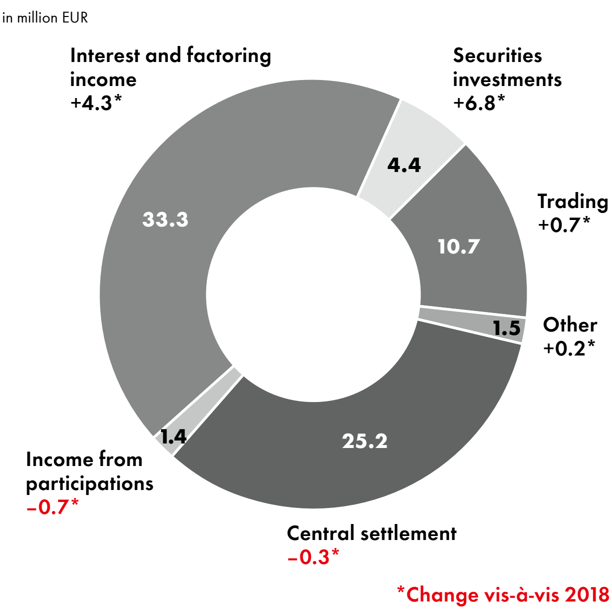
As at 31 December 2019 the Würth Group's liquidity reserves amounted to an adequate amount of EUR 850 million, consisting of liquid assets of EUR 450 million and an unused committed revolving credit facility of EUR 400 million.

The Inhouse Banking Division's income from Group Financing benefited from the above-mentioned commercial paper issuance. Another major positive impact came from the 2018 bond issue with a coupon rate of 1.0%, which for the first time affected the full financial year. In 2019 the interest rate sensitivity of the Würth Finance Group was continuously reduced from 4.8% to 3.1%. This was achieved by refinancing new and extended intercompany loans to Würth Group companies with shorter durations.

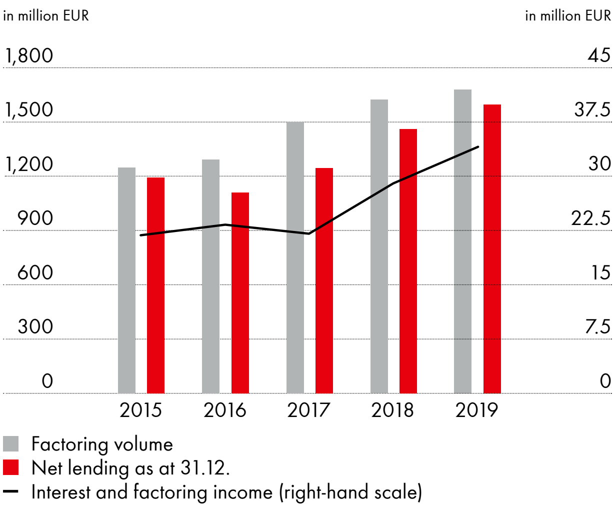
Group Financing also includes the pre-financing of intercompany receivables (factoring). Volumes and income in this area grew slightly by 2.7%.

All these effects resulted in a substantial increase of the adjusted income from interest and factoring income by EUR 4.3 million (+15%) to EUR 33.3 million.

Income distribution




Group financing: volume and revenue from intra-group lendings



“In this world of continuous innovation, we closely track fintech developments and use only proven financial products that add value for our clients.”

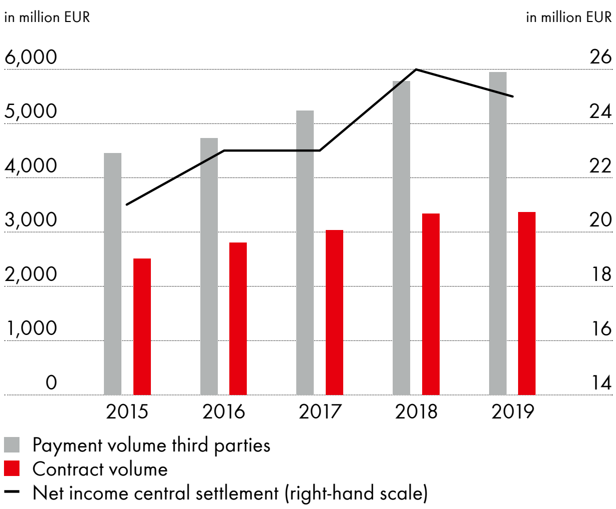
**Björn van Odijk**
Managing Director, Würth Finance International B. V.

**Central settlement of payments to suppliers**
In a trading conglomerate such as the Würth Group, negotiating payment terms and conditions with suppliers and the subsequent settlement of payments represent core competencies. Würth Finance International B.V. centralises these functions and thus enhances efficiency within the decentralised network of group companies. Payment conditions are contractually agreed with the suppliers and are applicable to all transactions with the Würth Group companies.

In recent years, alongside efficiency, guarding against cybercrime has grown in importance. Consequently, the bulk of the Inhouse Banking Division’s IT budget is invested in this area. In the course of 2019 and with reference to the implementation of the new GPS system, employees in this specialist area had to familiarise themselves with the new payment system in their day-to-day activities, following exhaustive testing rounds. Another key project in this area was the further centralisation of supplier data held on Würth Group suppliers. The Central Settlement team of Würth Finance International B.V. has taken on greater responsibility for the Würth Group in this regard since autumn 2019.

The core “central settlement of payments to suppliers” services are well established and are developing roughly in line with the Group’s purchasing volume. Outliers are only apparent in the case of major acquisitions, if notable suppliers are lost or if there are other internal changes. In the reporting year the payment volume increased by 2.6% to just under EUR 6 billion. On the other side revenue remained more or less unchanged year on year, at EUR 25.2 million. This discrepancy is attributable to the strategic replacement of a few major suppliers and the fact that there was a shift from purchasing to in-house production in one of the strategic business units of the Würth Group.

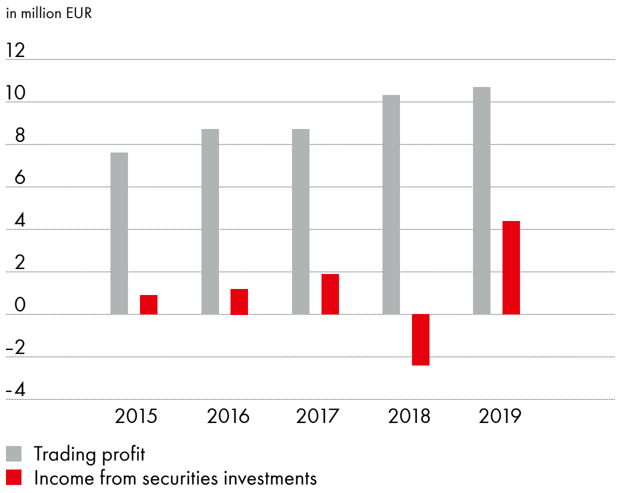
Central settlement: payment volume/revenue



**Currency hedging and trading with financial instruments**
The expertise of the Group's currency experts was again in high demand in the reporting year. Political events kept the markets on their toes, so foreign currency hedging was a persistent theme among the finance colleagues in the Würth Group companies. Spot transactions, forwards, non-deliverable forwards and currency options were used as protection against negative currency effects and to provide reliability of planning. Overall, the settled volume remained at the previous year's level. In addition and in line with the exposure limits agreed by the Board of Directors, a couple of trading positions were successfully taken. This contribution supported the increase of the adjusted trading income by 6.8% to EUR 11 million in financial year 2019.

**Income from participations**
As planned the silent participation in Internationales Bankhaus Bodensee AG was transferred to another Würth Group company with effect from 1 August 2019. This meant that income from participations at Würth Finance International B.V. was also reduced, decreasing from EUR 2 million to EUR 1.35 million.

Trading/securities investments: income development




## Outlook for 2020

Coronavirus (COVID-19) has spread rapidly throughout the world and is significantly affecting global healthcare systems, people's behaviour, the capital markets and hence economies and day-to-day lives. The economic and financial scale and end-point of these impacts are hard to predict. There is a high probability of a global recession lasting several quarters. At best, the Würth Group's core business will stabilise in the second half of the year.

Our top priority is the health of our employees. We are adhering to the corresponding instructions and recommendations from the health authorities, and most of the Inhouse Banking Division's employees are currently working from home. Access to systems is guaranteed, and we continue to operate as normal. There are no restrictions to client services.

Weak investment markets and declining payment volumes at the payment factory, along with a potential increase in lending volumes, have a direct and partially compensatory effect on the revenue and operating result of the Inhouse Banking Division. However, the extent of this effect cannot be reliably estimated at present. No relief is expected in terms of expenditure and the need for continued investment in the ICT infrastructure and the digitalisation of the Inhouse Banking Division's business. A double-digit drop in profits is entirely conceivable, however.

The EUR 500 million bond maturing in May 2020 is to be refinanced by raising long-term funds in the amount of EUR 750 million or possibly up to EUR 1,000 million. A consortium of banks is providing bridge financing of EUR 750 million with a term of one year (subject to a resolution of the bank directors). This can be used if a capital market transaction is not possible in May 2020 due to the capital markets still being closed.

MANAGEMENT WÜRTH FINANCE INTERNATIONAL B.V. AND WÜRTH INVEST AG
from left to right: **Alejandro Muñoz** | **Roman Fust** | **Björn van Odijk** | **Philip Guzinski** | **Jorre van Schipstal** | **Patrik Imholz** (Würth Invest AG) | **Daniel Ochsner**

# 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 its financial stability.

In close collaboration with the Central Managing Board 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 2019)

65 employees at the offices in Den Bosch, the Netherlands, and Rorschach, Switzerland

484,000 payment transactions with a volume of EUR 6,000 million in the year under review

Outstanding capital market funding with a total volume of EUR 1,500 million

Account relationships with over 400 Würth group companies

2,900 foreign exchange transactions with 280 group companies and a hedging volume totalling EUR 970 million

10,083 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 9,000 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