Annual Report
www.hermle.de

2017

besser fräsen


HERMLE
since 1938

01.1 Hermle at a glance

Hermle Group

€ million	2013	2014	2015	2016	2017	Change 2017/2016 in %
Sales	305.9	346.8	356.6	394.0	402.0	2.0 %
- Domestic	121.3	147.7	147.9	160.3	168.2	5.0 %
- Abroad	184.6	199.1	208.7	233.7	233.8	0.0 %
Incoming orders	352.3	332.5	360.7	364.5	433.2	18.9 %
Orders on hand	133.4	119.1	123.2	93.8	125.0	33.3 %
Capital investments	7.8	15.4	7.1	16.4	23.5	43.3 %
- Property, plant and equipment*	7.8	15.4	7.1	16.4	18.5	12.8 %
- Financial assets	–	–	–	–	5.0	–
Depreciation	6.6	6.2	6.7	7.0	7.8	11.4 %
- Property, plant and equipment*	6.6	6.2	6.7	7.0	7.8	11.4 %
- Financial assets	–	–	–	–	–	–
Earnings before taxes	62.2	79.4	80.6	100.3	99.4	-0.9 %
Net income	45.5	58.8	59.2	73.8	73.3	-0.7 %
Cash flow	51.2	64.4	65.4	80.8	81.1	0.4 %
Balance sheet total	258.2	282.7	288.4	309.6	330.7	6.8 %
Shareholders' equity	185.2	202.8	209.8	229.9	237.5	3.3 %
Employees (reporting date 12.31.)	912	964	977	1,018	1,086	6.7 %

* Property, plant and equipment and intangible assets.

For reasons of simplification, the terms employee and worker in this Business Report are used, in part, to represent the female and male form.

01
Hermle

Tool and mold making. Forging die mold.

Tool and mold making. Rib component made of tool steel for a shoe sole die mold.
5-axis simultaneous machining using a sophisticated groove cutting strategy.

Contents

Date of shareholders' meeting: Wednesday, July 4, 2018 at 11.00 a.m. at the business premises of Maschinenfabrik Berthold Hermle AG

Presented with the compliments of Maschinenfabrik Berthold Hermle AG

01.2 Company executive bodies

Supervisory Board

Dietmar Hermle
Chairman,
Entrepreneur

Lothar Hermle
Deputy Chairman,
Industrial Foreman

Dr. Sonja Leibinger Deputy Chairwoman, Attorney

Dr. Wolfgang Kuhn
Spokesman of the management board of Südwestbank AG, Stuttgart

Adolf Weber*
Works Council Chairman

Gerd Grewin* Industrial Foreman, Control Technician

Günther Leibinger
Honorary Director,
Merchant

*Elected employee representatives

Management Board

Günther Beck

Areas of responsibility:
Finances Information technology
Material Management (to 12/31/2017)

Franz-Xaver Bernhard

Areas of responsibility:
Research & development Sales

Benedikt Hermle (from 1/1/2018)

Areas of responsibility:
Material Management.
Production (from 4/1/2018).
Service (from 4/1/2018)

Alfons Betting (to 3/31/2018)

Areas of responsibility:
Production Service

Fully authorized representative

Gabriele Peyerl

Area of responsibility:
Human resources

Benedikt Hermle

Area of responsibility:
Production (7/5/2017 - 12/31/2017)

Additional Management Board and Supervisory Board positions are stated on page 80.

01.3 Company history

1938 Founding of the company, a bolt and machine screw manufacturer in the southwestern German town of Gosheim. Production of turned parts begins.

1953 Conversion of company to Maschinenfabrik Berthold Hermle KG.

1956 Centrifuge production begins.

1957 Milling machine production begins.

1972 Presentation of first Hermle universal milling machine.

1975 Production of numerically-controlled milling machines.

1978 Start of production of CNC controlled milling machines.

1984 Conversion of the company to Maschinenfabrik Berthold Hermle GmbH & Co.

1990 Conversion of company to Maschinenfabrik Berthold Hermle AG and IPO.
Company opens new sales and administration building in Gosheim.

1992 Start of comprehensive restructuring of the Hermle Group in Germany and abroad.

1995 Optimization of company as part of the 2000 Concept.

1997 Hermle + Partner Vertriebs GmbH commences operations.

1998 Founding of Hermle-Leibinger Systemtechnik as a joint venture for customer-specific automation of Hermle machines.

1999 Hermle Schweiz AG is founded in Switzerland as sales and service support center.
Opening of the new demonstration center in the Kassel-Lohfelden business park.

2000 New technology and training center opened at the company headquarters in Gosheim.

2001 US branch becomes independent entity as Hermle Machine Co. LLC.
Founding of Hermle Nederland B.V.

2003 Service and sales center commissioned in North America.

2004 Company opens a modern customer service center at the Gosheim location.
Opening of the sales branches and representative offices in China, Austria and the Czech Republic.

2005 Founding of the export business Hermle WWE AG in Switzerland and a Russian subsidiary to expand activities in Eastern Europe.

2006 Hermle Italia S.r.l. is founded to directly process the Italian market.

2007 Two additional sales centers are opened in Russia.

2009 During the grave financial crisis, the concept of the 'breathing company' proves successful, as it already had in 2002:
despite the massive drop in demand, Hermle manages to make a profit and avoid job losses.
In order to facilitate the opening up of the markets in Scandinavia and south-east Europe, new offices are established in Denmark and Bulgaria.

2011 Hermle establishes new branch in Poland.
A new warehouse and logistics center with the state-of-the-art shipping and warehousing systems commences operations at the company headquarters in Gosheim.

2013 Hermle celebrates its 75th company anniversary.

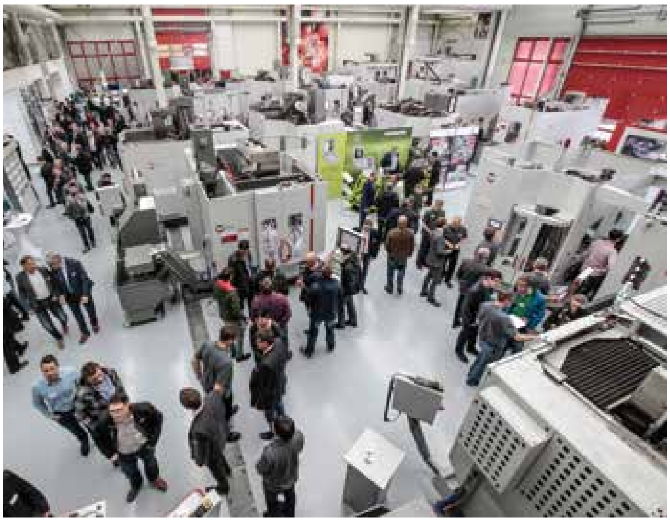
2014 At its Gosheim location the company moves into a state-of-the-art production facility for the assembly of large machines and automated plant, and opens a new restaurant for customers and visitors.

2016 Second production facility established in Zimmern ob Rottweil.

01.4
2017 highlights

April I – Hermle Open House presents latest industry trends

Despite wintry conditions, more than 2,700 visitors from 1,200 companies all over the world attend the Hermle Open House in Gosheim to find out all about the company's latest development trends in milling, milling-and-turning, and generative manufacturing. Alongside numerous Hermle machines and automation solutions, over 50 exhibitor present the latest in the fields of clamping technology, CAD/CAM, software and control engineering. There are also daily presentations, user training sessions, as well as information resources detailing Hermle's services.



April II – Innovative automation solution: HS flex handling system

Among the major new product launches in 2017 was the HS flex handling system, presented for the first time at the Hermle Open House. The compact, high-performance, attractively priced solution provides a cost-effective entry to the automation of Hermle machining centers. It is suitable for Performance and High Performance line machines.

01.4
2017 highlights

July – Start of production at the new Zimmern location

Just nine months after start of construction, mass production of mineral casting beds is launched at the new Hermle facility at Zimmern ob Rottweil. The structures, used as machine base units, were previously bought-in. By establishing in-house production, Hermle is expanding its know-how in key technologies and assuring its supply source.

August – Construction project in Gosheim completed

The construction work on the new, enlarged chip removal manufacturing facility in Gosheim is ended with the demolition of no longer needed walls and ceiling panels of the former building complex during the works vacation period. This project was designed to make the plant fit for the future, and involved building over an existing factory floor and modernizing the facility while maintaining production operations. In 2018, a new large-scale machining facility and several Hermle machines will be installed.

September I – Presentation of the C 650 at EMO

At EMO, the world's leading trade fair for metal processing, Hermle presents its new C 650 machining center. It adds a third model to the Performance line: The C 650 substantially enhances the options for cost-effective three- and five-axis machining at the top end of the range.

September II – Digital module portfolio grows

Hermle also uses EMO to launch its expanded portfolio of digitalization modules designed to help customers establish Industry 4.0 manufacturing based on Hermle machining centers. The continuously growing range of software includes Digital Production, Digital Operation and Digital Service products.

01.5
Introduction by the Management Board

DEAR SHAREHOLDERS, BUSINESS PARTNERS AND FRIENDS OF THE COMPANY,

Maschinenfabrik Berthold Hermle AG saw its business grow in an increasingly dynamic fashion in 2017. There was a marked surge in demand for our machines and automation solutions as from the second quarter, which meant that we were able to surpass our start-of-year forecasts. Incoming orders over the full year Group-wide increased by almost 19 % to € 433.2 million, while sales revenues rose slightly to a new record high of € 402.0 million – thanks primarily to growth on the domestic market. Group earnings after tax totaled € 73.3 million, almost reaching the very good level of 2016 despite the upfront costs of two future development projects, and even though the high revenues from a number of big international contracts generated the previous year were no longer contributing.

At the parent company Hermle AG, net income grew from € 64.6 million to € 69.3 million. On that basis, the Management Board and Supervisory Board will propose to the shareholders' meeting that an increased dividend be paid for the 2017 business year: € 15.05 per preference share, comprising the unchanged basic dividend of € 0.85, a stable bonus of € 12,00, plus a one-off special bonus of € 2.20.

Our successful year was founded on unexpectedly positive market conditions. We also benefited from the customer-oriented nature of our product portfolio, which we are continually expanding and enhancing. A key element of our portfolio is the High Performance line, comprising extremely high-performing, precision machines which are used primarily for very demanding applications in high-tech sectors, and represent the benchmark in five-axis machining. We also offer the Performance line for cost-effective three- to five-axis milling. Two new models have been added to it in the last two years: the C 250 for machining small workpieces launched in 2016 – already a key driver of sales in the year under review – and the top-of-the-range C 650 launched in Fall 2017, which has likewise seen strong demand. Other major factors in our growth are our automation components by which Hermle machining centers can be upgraded to fully automated manufacturing cells. In 2017 we launched a successful innovation onto the market in this segment with the HS flex handling system, and we will be presenting more new products at our 2018 Open House.

Hermle is also responding to the current hot topics of digitalization, Industry 4.0, the Smart Factory and generative manufacturing with an extensive range of products. Our steadily growing range of software provides our customers with a powerful suite of digital modules for the deployment of Hermle machining centers in Industry 4.0 and Smart Factory applications.
Our MPA (metal powder application) technique for the generative manufacture of complex components is also developing in a very promising way. In response to the high demand for this technology, which we offer our customers as a service, we are currently adapting it to additional machine models in order to expand our MPA capacities in future.

Alongside our intensive development activities, the two projects mentioned at the beginning are key to the future growth of our business. The first of them involves expanding and modernizing the chip removal manufacturing function at our corporate headquarters in Gosheim. To that end, an existing building complex was built over in a space-saving and energy-efficient way, with state-of-the-art machinery and technology being installed while production operations kept running. A new large-scale machining facility was installed and commissioned into operation in early 2018, and a number of new Hermle machines are scheduled to go online in the coming months. This strategically important project will then be completed by the end of this year.

The second project aimed at setting us on course for the future is our new facility at Zimmern in the neighboring district of Rottweil. In a first step at the location in 2017 we launched in-house state-of-the-art manufacture of machine beds, thereby enhancing our know-how in a key area. The mineral casting technology employed, and the optimization of the production facilities, will not only assure the high quality of the machine beds but will also help us to cut our energy consumption and CO_2 emissions thanks to the new location's close proximity to our corporate headquarters. The first self-produced machine base units were delivered to Gosheim in the middle of last year. We are now making machine beds for almost all Hermle models in Zimmern. The additional as yet unused areas still available to us provide us with plenty of scope for expansion in delivering new products and services.

The two major projects, and the strains on our capacities, imposed high demands on the entire Hermle team in 2017, which they met with great commitment and vigor. The Management Board would like to thank all the company's employees most sincerely for their efforts in once again achieving such very healthy results. In recognition of their important contribution, following the shareholders' dividend payment each Hermle AG employee will receive a one-off bonus of € 4,500.

All corporate divisions worked hard throughout the year to cope with the high levels of demand. Nevertheless, the backlog of orders at the end of 2017 totaled €125.0 million – around a third higher than the previous year's figure. Those orders, combined with our expanded capacities, provide Hermle with a sound foundation for further growth. For 2018 we predict growth in Group sales and in earnings in the mid to upper single-digit percentage range, provided our market conditions develop as expected. Our aim is to sustain the long-term growth of Hermle in the years ahead – to the benefit of our customers, our employees, our business partners, our shareholders, and of the people in our region.

Best regards,

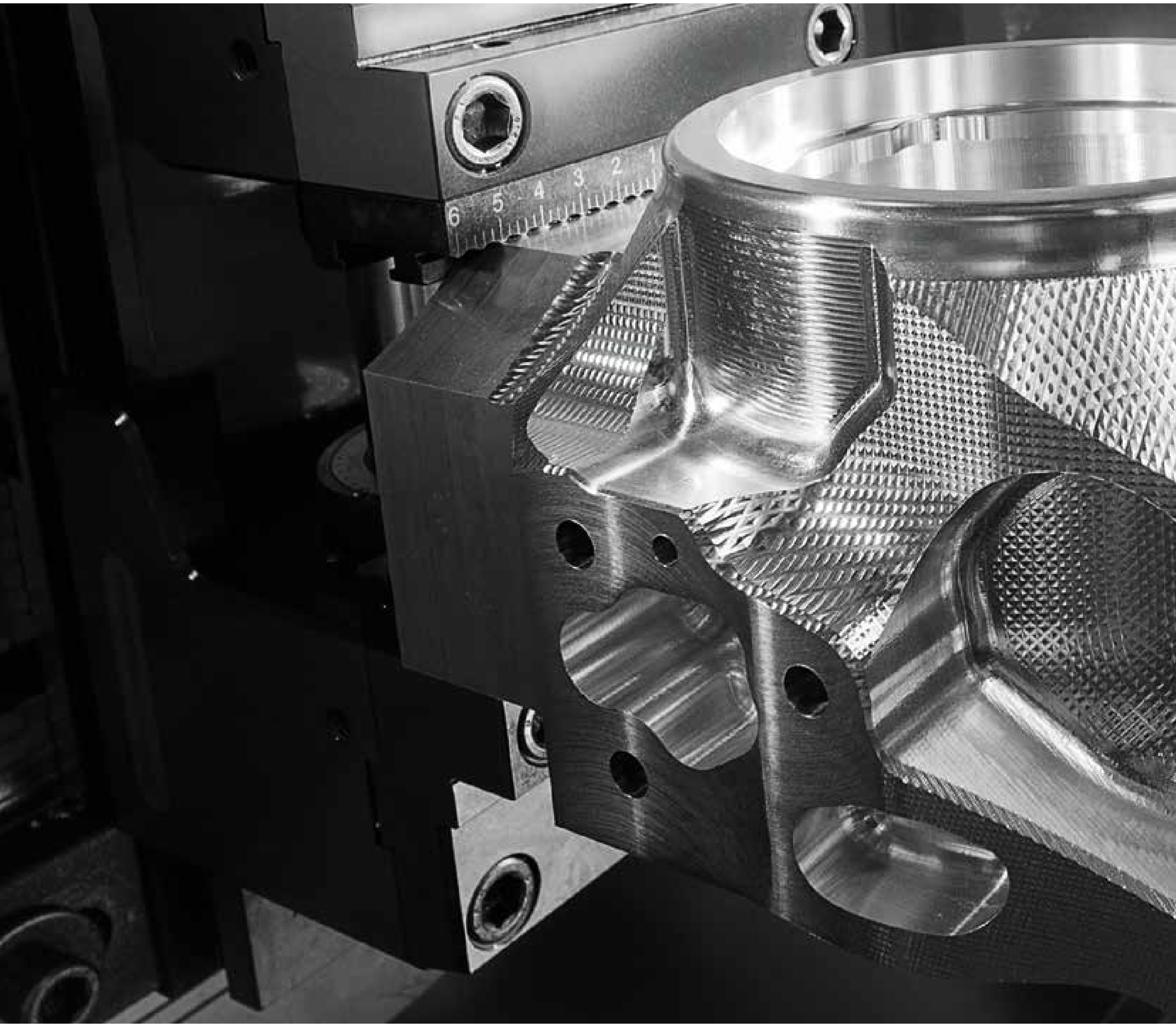
Günther Beck
Management Board

Franz-Xaver Bernhard
Management Board

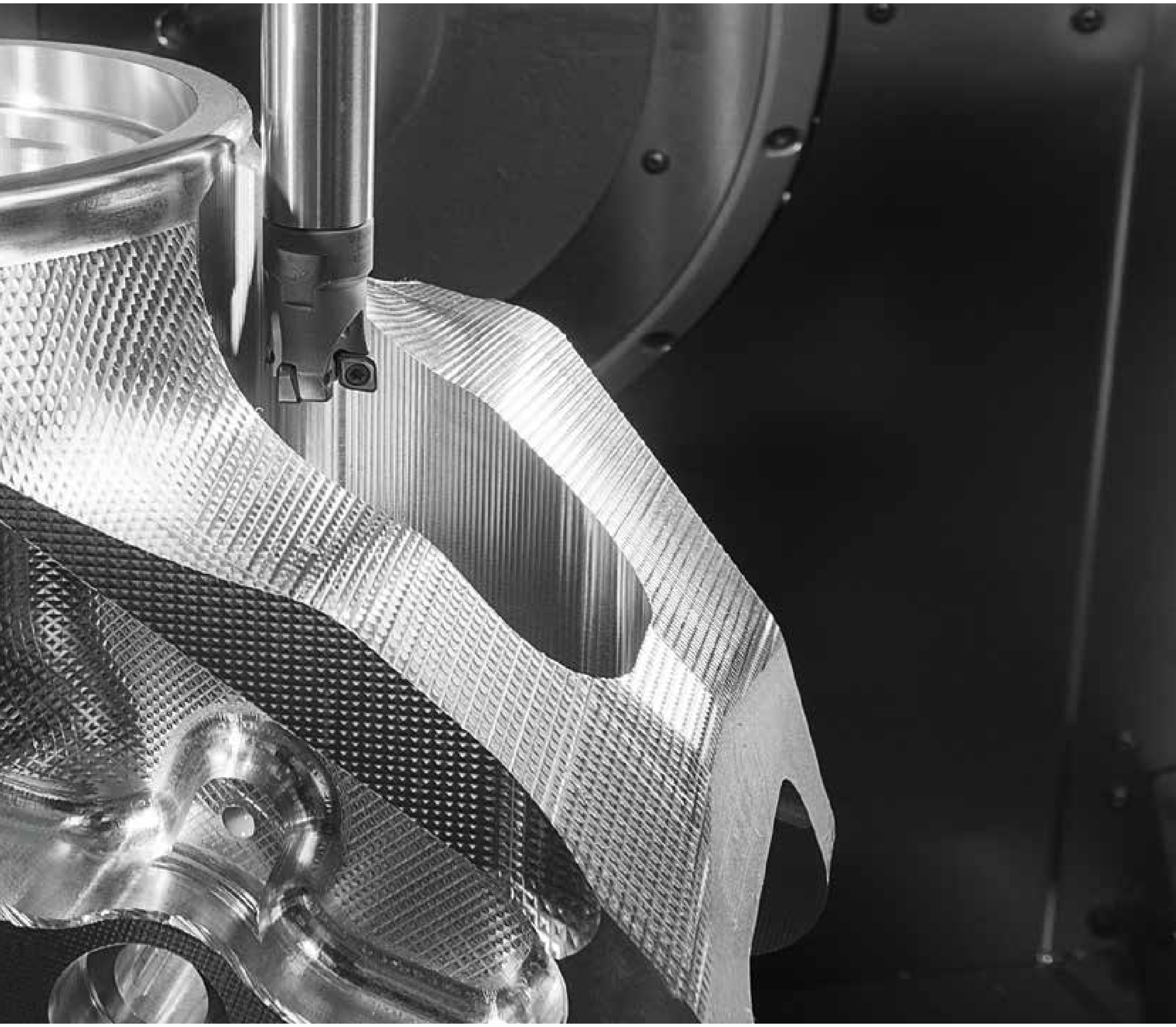
Alfons Betting
Management Board

Benedikt Hermle
Management Board

02
Reports



Automotive.
Wheel carrier.



Automotive. Lightweight wheel carrier.
Complex ultra-high-precision 5-axis simultaneous machining with top-quality surface finish.

02.1
Supervisory Board Report

LADIES AND GENTLEMEN, DEAR SHAREHOLDERS,

Maschinenfabrik Berthold Hermle AG once again enjoyed great success on its markets in the past business year, achieving a slightly rise in sales revenues and stable earnings around the previous year's level. The two major projects aimed at safeguarding the long-term future of the business at the corporate headquarters in Gosheim and at the new location in Zimmern ob Rottweil were also completed on schedule. The strains on our capacities and the construction projects imposed high demands on the entire Hermle team. In the name of the Supervisory Board, I would like to expressly thank the Management Board and all the company's employees for their hard work and great dedication.

Strong cooperation between Management Board and Supervisory Board

In the past business year the Supervisory Board performed all its tasks as specified by law and the articles of association with due diligence. We provided the Management Board with advice and support in managing the business, and monitored its work in a constructive manner. We were routinely, promptly and thoroughly informed through verbal and written reports from the management board about the current position and course of business of Hermle AG, and of the associated opportunities and risks. The Management Board provided detailed explanations of any non-conformity to planning in business developments.

At the Supervisory Board meetings, we discussed the course of business and all events of key importance to the company. We also were gave intensive consideration to the company's financial and earnings position, corporate planning – including financial, investment and personnel planning – as well as business policy and strategy. The Supervisory Board participated directly in decisions of fundamental significance to the company, and always took decisions regarding transactions subject to mandatory Supervisory Board consent on the basis of informative documentation and following detailed discussions. The Chairman of the Supervisory Board also regularly met with the Management Board between the Supervisory Board meetings in order to discuss current matters.

Supervisory Board meetings and committees

During the year under review, the Supervisory Board had five scheduled meetings: on March 22, April 26, July 6 (two meetings), and on December 6. The Supervisory Board was quorate at all meetings. On only one occasion was a member of the Board unable to attend. As in previous years, a presidential committee was formed consisting of the Chairman and his two deputies. It was not necessary for the Supervisory Board to convene at other times in 2017.

The main Supervisory Board issues in 2017

In all the Supervisory Board meetings, we spent much time considering the market situation and the course taken by Hermle AG's business, as well as that of the domestic and foreign subsidiaries. We also devoted our attentions throughout the year to the two major projects aimed at safeguarding the long-term future of the business.

At our first meeting on March 22, 2017, we additionally discussed in detail the proposed dividend payment based on the provisional figures for 2016. Other matters focused on were the situation on various international markets and the available options for expanding the Gosheim site. We also informed ourselves concerning the new Hermle website and the company's digital brand communications concept.

The meeting at which the annual financial statements were reviewed was held on April 26, 2017. In the presence of the auditor, we intensively reviewed the financial statements of the parent company Hermle AG and of the Group, which were approved and thereby adopted. Other agenda items passed were the agenda for the shareholders' meeting, the dividend proposal, and the report of the Supervisory Board.

At the two meetings on July 5, 2017, before and after the shareholders' meeting, the Management Board reported to us in detail on the completion of the new building project at the Zimmern location and the commissioning of the mineral casting facility there. Intensive consideration was also devoted to the ongoing construction works at the corporate headquarters in Gosheim as well as to other options for expanding the site. Among other resolutions, the Supervisory Board approved the installation of a new transformer substation and the acquisition of additional space for employee parking. We also discussed the potential for development of the subsidiary company Hermle Maschinenbau GmbH, which bundles our operations in the generative manufacturing of complex components, and assigned Mr. Benedikt Hermle general authority over the production function.

The Supervisory Board meeting on December 6, 2017 focused on the budget and investment planning for 2018, which was discussed in detail and subsequently approved. The Supervisory Board also considered the new bonus arrangement for employees, consented to the expansion of the US subsidiary's facility, and also agreed to the establishment of a new training and customer service center at the corporate headquarters in Gosheim as a medium-term objective. The Supervisory Board also passed a resolution on the acquisition of the remaining shares in the automation business Hermle-Leibinger Systemtechnik. We also passed the latest issue of the company's Corporate Governance Statement. This is permanently available on the Hermle website in the Stock Exchange / Information for Shareholders / Mandatory Disclosures / Code Section 161 AktG (German Stock Corporation Act) section.

Audit of the annual financial statement

On July 5, 2017, the shareholders' meeting voted in favor of commissioning the financial auditing and tax consulting company Bansbach GmbH, Stuttgart, to conduct the annual audit for the 2017 business year. In conclusion, the Supervisory Board awarded the audit commission to Bansbach GmbH. The auditors assured that they did not render any significant services to Maschinenfabrik Berthold Hermle AG in the year under review going beyond this assignment and that no circumstances apply that could jeopardize their impartiality.

Bansbach GmbH audited the financial statements of Maschinenfabrik Berthold Hermle AG drawn up in accordance with the German Commercial Code (HGB), the Group consolidated financial statements according to IFRS, and the summary management report for the 2017 business year, including the bookkeeping, and certified its unreserved confirmation of each. The auditors also reviewed the company's internal control system and confirmed it as being effective, and confirmed that the management report appropriately portrays the opportunities and risks of future developments. The audit was performed in line with the generally accepted German standards for the auditing of financial statements promulgated by the Institut der Wirtschaftsprüfer (German Institute of Auditors).

All Supervisory Board members were provided in good time with the annual financial statement of Hermle AG, the consolidated financial statement, the summary management report and the audit reports. We scrutinized the documents and discussed them together with the auditor during the accounts meeting. Our own review was also concluded without objections. The Supervisory Board concurs with the judgment of the auditors, and approves the annual financial statements and the management report. The annual financial statement of Maschinenfabrik Berthold Hermle AG is, therefore, formally approved. We also reviewed the mandatory Non-Financial Statement pursuant to sections 289b and 315b HGB, and confirmed that they comply with the legal requirements. We concur with the proposal on the appropriation of profits for the 2017 business year put forward by the Management Board entailing the distribution of a dividend of € 0.80 for each ordinary share and € 0.85 for each preference share, plus a bonus of € 12.00 for each share, plus a one-off special bonus of € 2.20 per share.

Changes in the constitution of the Management Board

At its meeting on December 6, 2017, the Supervisory Board appointed Mr. Benedikt Hermle to the Management Board of Maschinenfabrik Berthold Hermle AG with effect from January 1, 2018. With effect from January 1, 2018, he has taken on the Material Management portfolio, and with effect from April 1 has additionally taken over the post of Mr. Alfons Betting as head of Production and Service. Mr. Betting resigned from the Management Board at his own request on March 31, 2018, though he will continue to work for the company on a consultancy basis. The Supervisory Board would like to thank Mr. Betting for his many years of outstanding service. He worked for the company in a number of roles over several decades, and had been a member of the Management Board since 2011.

Hermle AG had a high backlog of orders at the end of 2017. Consequently, the prospects for growth in sales revenues and earnings in 2018 are good, though this does pose a major challenge in view of the already heavily strained capacities. The Supervisory Board wishes all employees and the Management Board every success in achieving the set goals.

Gosheim, April 2018

Dietmar Hermle
Chairman of the Supervisory Board

02.2
Management report of the AG and Group management report

This report is a summary management report covering Maschinenfabrik Berthold Hermle AG and the Group. It was prepared in line with the requirements of the German Accounting Standard (DRS) 20. As last year, the Group consolidated financial statements for 2017 comply with the International Financial Reporting Standards (IFRS), as applicable within the European Union. The requirements of the German Commercial Code (HGB) were applies to the annual financial statement of the individual company Maschinenfabrik Berthold Hermle AG. Details that refer to the individual company are denoted with the addition "Hermle AG" or "Individual Company". The mandatory Non-Financial Statement pursuant to sections 289b and 315b HGB can be viewed on the Hermle website at www.hermle.de (section heading: Investor Relations / Mandatory Disclosures / Non-Financial Statement). It set out all the key information on our sustainability-related activities.

The share capital of Maschinenfabrik Berthold Hermle AG is divided into 4 million ordinary shares and 1 million non-voting preference shares. Only the preference shares are traded on the stock exchange. Therefore, mandatory disclosure requirements do not apply pursuant to sections 289a and 315a HGB.

GROUP FUNDAMENTALS

Business model and sales markets

Maschinenfabrik Berthold Hermle AG ranks among the leading global suppliers of high-quality milling machines and machining centers. As a manufacturer with the highest standards of quality, we set the benchmarks when it comes to 5-axis machining of complex workpieces. Our customers at home and abroad include companies from high-tech sectors such as tool and mold making, medical technology, the optics industry, aviation, power engineering, the automotive industry and motor racing as well as their supplier industries.

Our product range has a modular structure that is being continuously enhanced in accordance with the requirements of the various market segments. Increasingly important factors in that ongoing development are innovative automation solutions, connected production, and additive manufacturing.

Organizational structure

The Hermle Group consists of the parent company Maschinenfabrik Berthold Hermle AG (Hermle AG) and its subsidiaries. Within the Group, Hermle AG handles most of the development and production activities, central services and logistics services, as well as commercial and administrative functions. The domestic subsidiaries are Hermle + Partner Vertriebs GmbH (HPV), the development company Hermle Maschinenbau GmbH (HMG) focusing on additive manufacturing, and the at-equity consolidated Hermle-Leibinger Systemtechnik GmbH (HLS), which specializes in custom automation solutions. The companies which have their headquarters in Germany make up the Domestic company segment.

The Foreign Sales segment comprises the companies and operating facilities outside Germany. They largely perform marketing and service activities in various regions. Independent Hermle subsidiaries are located in Italy, Netherlands, Russia, Switzerland and the USA. Operating facilities are located in Denmark, Austria, Poland, and the Czech Republic. We also operate representative offices in key sales territories, such as Bulgaria and China, which are allocated to Hermle AG.

No changes were made to the organizational structure in the year under review.

Strategy and management control

Maschinenfabrik Berthold Hermle AG pursues a strategy geared towards profitable, organic growth. We aim to produce premium grade tool machines at the location Germany relying on a strong equity base and a highly motivated and competent team of employees working for the company on a long-term basis, offer excellent service worldwide and in the process generate comfortable revenues. An increasingly key strategic development is the digitalization of our products and services and of all the processes within the business. We successfully implemented our strategy in 2017.

The Hermle Group is controlled centrally by Hermle AG. In addition to incoming orders and sales revenues, the significant key performance indicator (KPI) in that respect is earnings before interest and tax (EBIT), which corresponds to the operating result. The three-member (in first quarter 2018 temporarily four-member) Management Board of Hermle AG has overall management responsibility. The Management Board remuneration is made up of a fixed element and a variable element that is dependent on the development of the net income of the individual company.

Corporate Governance Statement

The working methods adopted by the Management Board and the Supervisory Board as well as relevant details of corporate governance practices are set out in the Corporate Governance Statement pursuant to sections 289f and 315d HGB, which is permanently available on our website www.hermle.de (under: Investor Relations / Mandatory Disclosures / Management Declaration). It also includes the legally required disclosures of female-to-male employee ratios pursuant to sections 76 and 111 of the German Stock Corporation Act (AktG).

BUSINESS REPORT

Framework conditions: Global economic upturn

The global economy grew markedly in 2017. Many countries performed better than expected, as a result of which, according to estimates by the International Monetary Fund (IMF), the global economy grew at a price-adjusted 3.7 % – up from the previous year's 3.2 %. Growth was driven primarily by the industrialized nations, where gross domestic product (GDP) increased by 2.3 % overall (previous year: 1.7 %). The Eurozone, the USA and Japan saw an upturn. Germany's GDP is predicted to have increased by 2.2 %. Emerging economies grew by 4.7 % (previous year: 4.4 %), driven by sustained high growth rates in China and India, as well as recovery in Brazil and Russia. Worldwide industrial output is predicted to have increased by 3.5 %, resulting in a significant improvement in industrial capacity utilization. The strong economic growth came as a surprise to the IMF, and resulted in repeated upward adjustments to forecasts in the course of 2017. Despite this, economists still see many risks for the global economy – including from the increasing protectionism being seen in many countries, from geopolitical tensions and humanitarian disasters, and the resultant refugee crises.

Upturn in machinery manufacturing

The German machinery manufacturing industry also profited from the global rise in demand for capital goods in 2017, increasing its order receipts by 8 % according to provisional figures from the German Engineering Federation VDMA. Domestic orders increased by 5 %, and international orders by 10 %. Manufacturing output increased by over 3 % on a price-adjusted basis. Growth in the sector resulted almost entirely from exports. German companies achieved growth primarily through sales to China, the USA and the other EU member-states. Sales of plant and machinery worldwide are predicted to have increased by around 6 %.

On the German machine tool market, machine tool manufacturers' association VDW reported a record 4 % increase in production in 2017. In that sector, too, exports were the main driver of growth, with the strongest increases being seen in sales to America and Asia. According to the VDW's estimates, Germany was the world's leading exporter in the past year, and after China the second largest producer of machine tools. Order receipts in the sector rose by 8 % overall. The increase in new orders was 10 % on the domestic market and 7 % internationally.

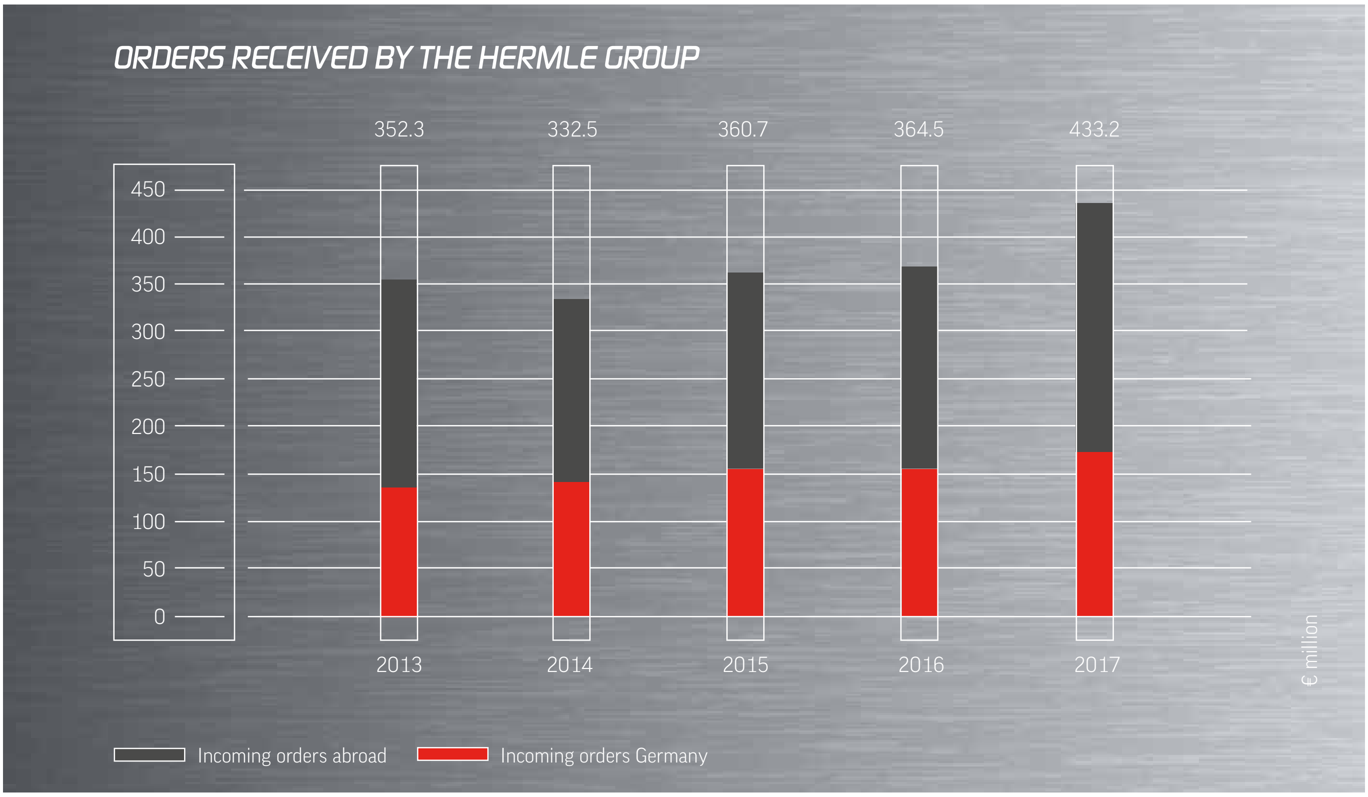
02.2
Management report of the AG and Group management report

In terms of technology, in 2017 the machine tool sector was once again driven by sustained strong demand for extremely high-performance, high-precision machines on the one hand and high-end, standardized – and so low-cost – entry-level models on the other. The increasing spread of automation and digitalization in production processes (Industry 4.0) and the trend toward generative manufacturing techniques (3D printing) was also maintained. Competitive pressures in the industry remained intense.

An overview of Hermle's business progress

As a technology leader in five-axis machining centers, Maschinenfabrik Berthold Hermle AG maintained its market share in 2017 and achieved a slight increase in Group sales revenues. Order receipts grew at an increasing pace from the second quarter onward. That was true of our high-end entry-level Performance line machines as well as our highly dynamic and precise High Performance line. Hermle's versatile automation and digitalization modules also saw high levels of demand. Consequently, our plants worked at full capacity throughout the year. Thanks to the great flexibility of our processes, we were nevertheless able to adapt our production to the rising demand. Alongside its operational business, Hermle also dealt with two major projects aimed at safeguarding the long-term future of the business at the corporate headquarters in Gosheim and at the new location in Zimmern ob Rottweil in the reporting period, both of which were completed on schedule.

19 % more new orders



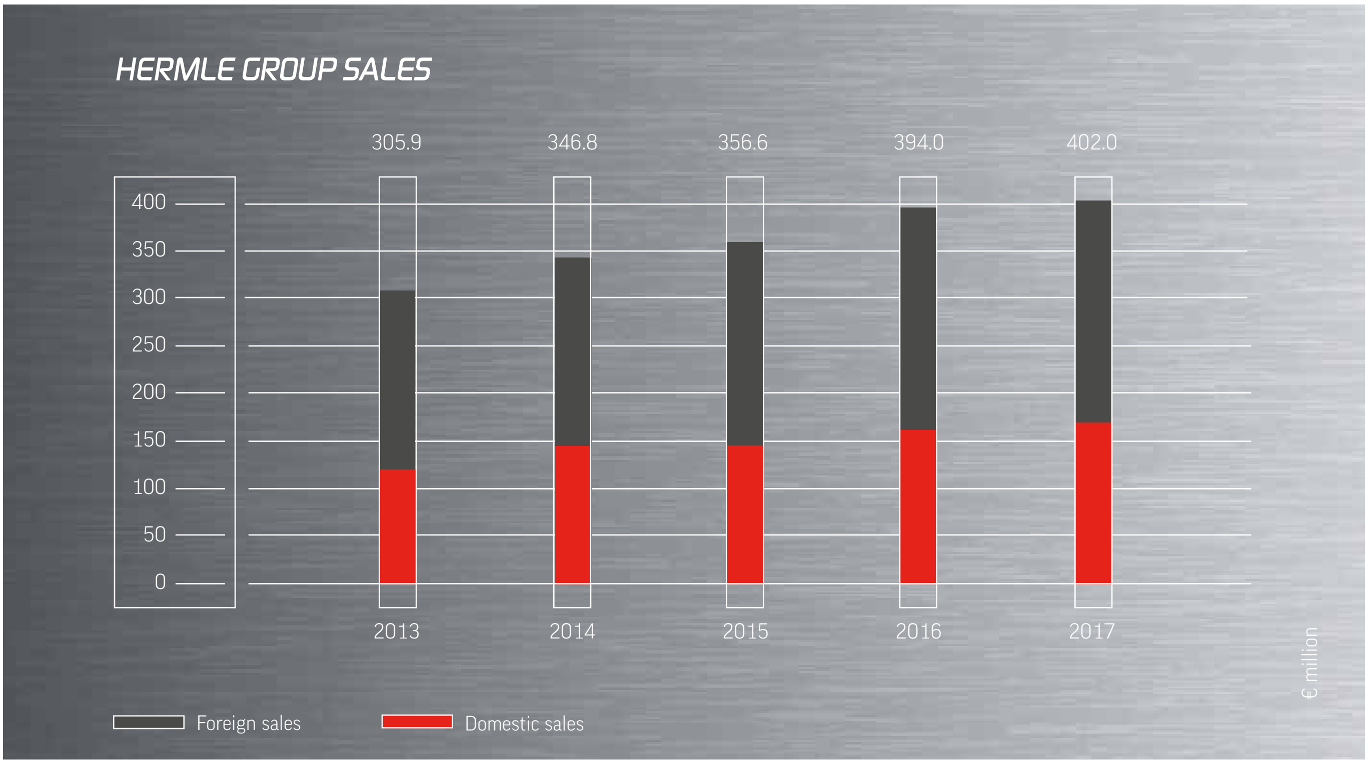
The Hermle Group's incoming orders increase by 18.9 % to € 433.2 million in 2017. The pleasing growth was driven by both the Performance and High Performance lines, and particularly by the innovations introduced in 2017. The main source of growth in regional terms was on international markets, where new orders increased by 25.9 % to € 261.5 million. Orders from Germany totaled € 171.7 million, up 9.6 % on the previous year. The backlog of orders at the Reporting date was a third higher at € 125.0 million.

Parent company Hermle AG's order receipts grew by 17.9 % to € 402.7 million. Of that total, € 172.7 million (+9.5 %) was generated in Germany and € 230.0 million (+25.1 %) on international markets. The backlog of orders at the end of 2017 reporting date was 30.0 % higher year-on-year, at € 115.8 million.

Sales reach new record total of € 402.0 million

The Hermle Group's sales revenues increased in the reporting period by 2.0 % to € 402.0 million – a new record high. Domestic sales increased by 5.0 % to € 168.2 million. International sales of € 233.8 million were up slightly on the previous year's € 233.7 million, so the export rate decreased slightly from 59.3 % to 58.2 %. We achieved growth both with new machines and with our services. The main drivers were the Performance line C 250 model launched in 2016 as well as automation components such as the new HS flex handling system.

Sales of Hermle AG increased by 4.2 % to € 376.0 million. On the domestic market we saw growth of 4.9 % to € 169.2 million, while international sales rose by 3.6 % to € 206.8 million, representing an almost steady export rate of 55.0 % (previous year: 55.3 %).



Segment development

In the Domestic Companies segment, business volumes in 2017 increased by 7.5 % to € 252.2 million. In addition to Hermle AG, the distribution company HPV and the automation solutions specialist HLS saw growth. The Foreign Sales segment, which had handled large numbers of large-scale projects in the previous year, recorded a decline in revenues in the year under review as expected, down 5.9 % to € 149.8 million. There was a stabilization of business at our companies in the USA and Italy, as well as at Swiss-based export company Hermle WWE. The remaining foreign-based subsidiaries increased their sales.

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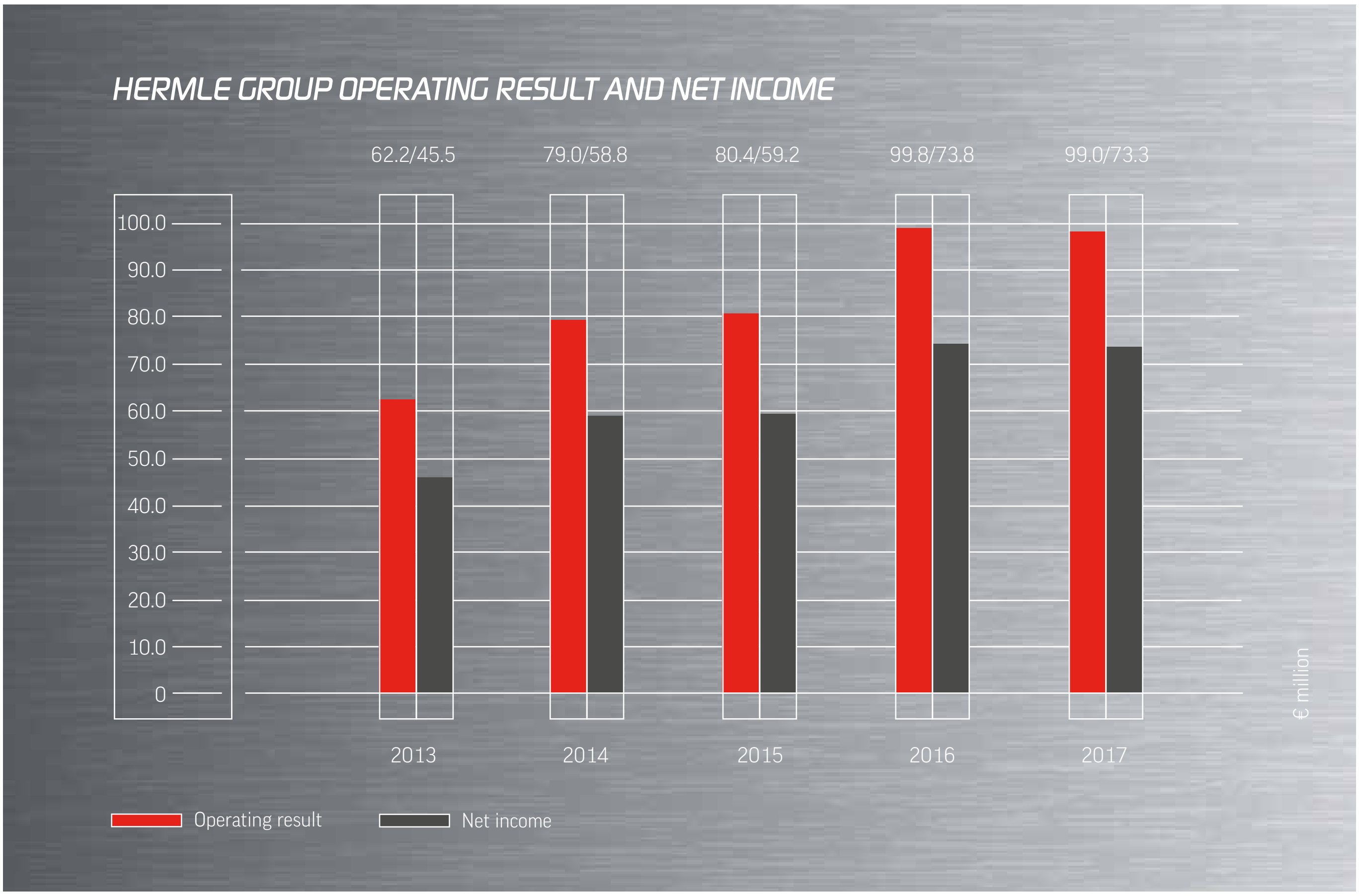
Operating result of € 99.0 million virtually at previous year's level

Based on the slight increase in business volumes and the high efficiency of our processes, growth in our operating earnings kept pace with the rise in sales revenues, though earnings were impacted by substantial upfront costs on the two future development projects as well as due to the absence of the high earnings contributions from a number of one-off large-scale international contracts which had been enjoyed the previous year. Total output Group-wide increased by 3.4 % to € 407.7 million. A notable factor in this was a greater increase in inventories, up to € 4.5 million from the previous year's zero because some invoicing was postponed to 2018 as a result of delays to machine deliveries, and because production was increased in anticipation of the increase in sales planned for 2018. Nevertheless, the 44.2 % material cost rate was only slightly above the previous year's level of 43.4 %. Moreover, the personnel cost rate as a percentage of total output rose from 20.4 % to 21.3 % as a result of the increase in the workforce undertaken in 2017 – among other reasons to handle in-house production of mineral casting beds. Depreciation rose from € 7.0 million to € 7.8 million due to the intensive capital investment activities. The net balance of other operating expenses and income was € -33.5 million (previous year: € 36.2 million).



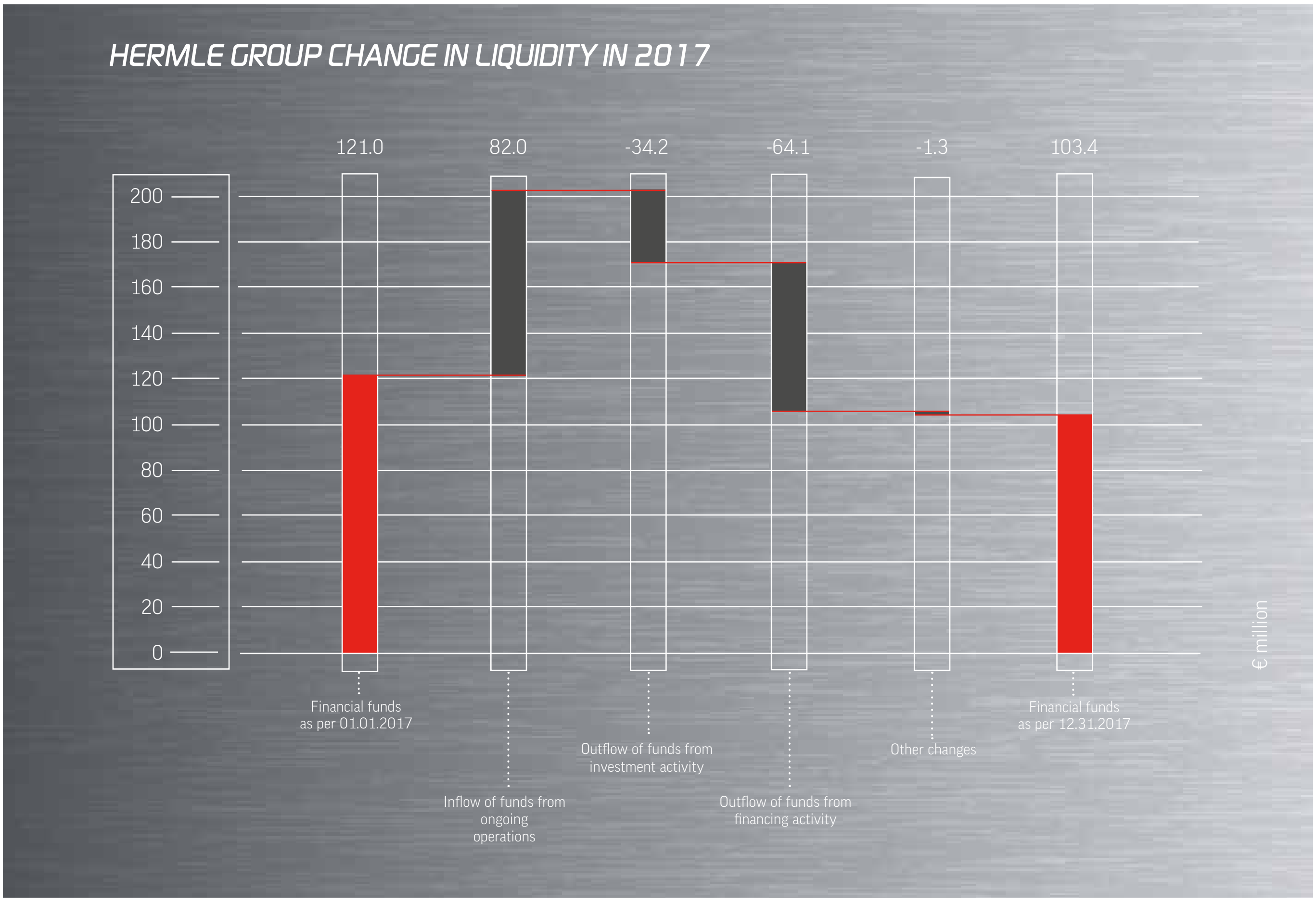
The Hermle Group's overall operating result was slightly improved in 2017 to € 99.0 million (previous year: € 99.8 million). Of that total, prior to consolidation effects, € 91.4 million (previous year: € 88.0 million) was attributable to the Domestic Companies segment and € 7.5 million (previous year: € 12.2 million) was attributable to the Foreign Sales segment in the year under review.

Taking into account the financial result of € 0.4 million (previous year: € 0.5 million), Group-wide pre-tax earnings of € 99.4 million were slightly down against the previous year comparative of € 100.3 million. This resulted in a gross sales margin for 2017 of 24.7 % (previous year: 25.4 %). Group after-tax net income totaled € 73.3 million, against € 73.8 million in 2016. Earnings per ordinary share totaled € 14.65 (previous year: € 14.76) and € 14.70 per preference share (previous year: € 14.81).

The operating result of parent company Hermle AG according to HGB increased from € 86.7 million to € 90.4 million. The net income, also including a one-off dividend of € 2.0 million from subsidiary Hermle Nederland, was € 69.3 million (previous year: € 64.6 million).

Financial management and financial position: Operating cash flow of € 81.1 million more or less stable

The financial management of Hermle AG and the Group aims to achieve largely internal financing and to safeguard our liquidity. We invest available funds exclusively on a low-risk and primarily short-term basis. We normally aim to finance both current business operations and capital investments from cash flow. This enables us to respond rapidly and flexibly to market changes relatively independently of third-party interests and uncertain capital markets. We use financing options such as leasing only in a few exceptional cases where this seems advisable.



The financial position of the Hermle Group remained sound in 2017. Backed by more or less stable earnings, cash flow before changes in working capital totaling € 81.1 million was around the previous year's level of € 80.8 million). The funds tied up in working capital in the reporting period decreased slightly against 2016, meaning that the inflow of funds from business operations increased from € 74.0 million to € 82.0 million. Notable factors in this included an increase in payments on account received on orders.

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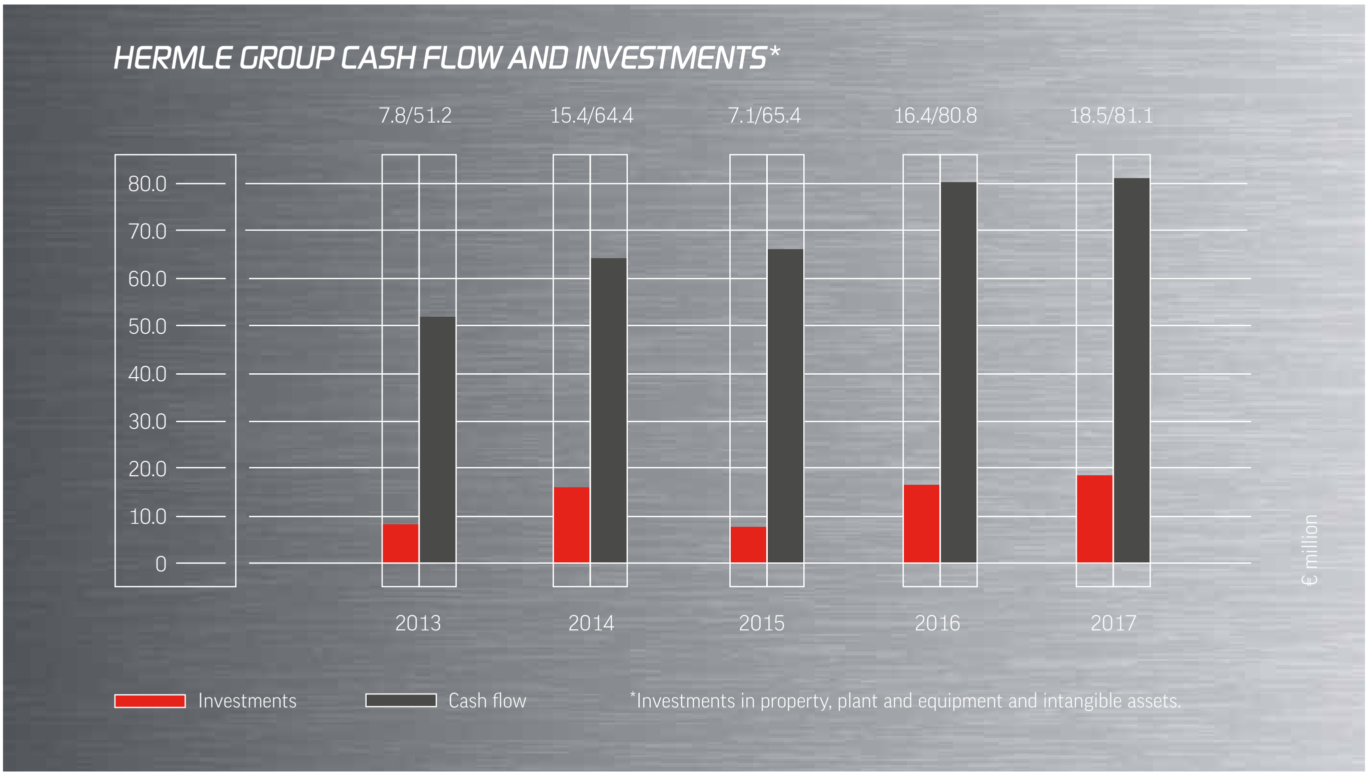
The outflow of funds for capital investment totaled € 34.2 million (previous year: € 0.3 million). In addition to the increase in investment activity, notable factors in this were the purchase of fixed-term deposits with terms of more than three months and promissory note loans similar to fixed-term deposits which according to IFRS must be stated as marketable securities. In the previous year, investment expenditures were largely balanced by income from the sale of such securities.

The outflow of funds from financing activity of € 64.1 million (previous year: € 54.1 million) was attributable to the dividend payment, as in the previous year. All in all, taking into account changes linked to exchange rates and other minor changes, liquid funds of the Hermle Group at the 2017 reporting date decreased from € 121.0 million to € 103.4 million.

Capital investments up again at € 18.5 million

Investments in property, plant and equipment and intangible asset by the Hermle Group increased once again in 2017, from € 16.4 million in the previous year to € 18.5 million. The reasons for this were the two major projects aimed at safeguarding the long-term future of the business: the modernization and expansion of chip removal manufacturing at the corporate headquarters in Gosheim and the establishment of a second production facility at Zimmern ob Rottweil. The 'Production' section contains more information on these projects.

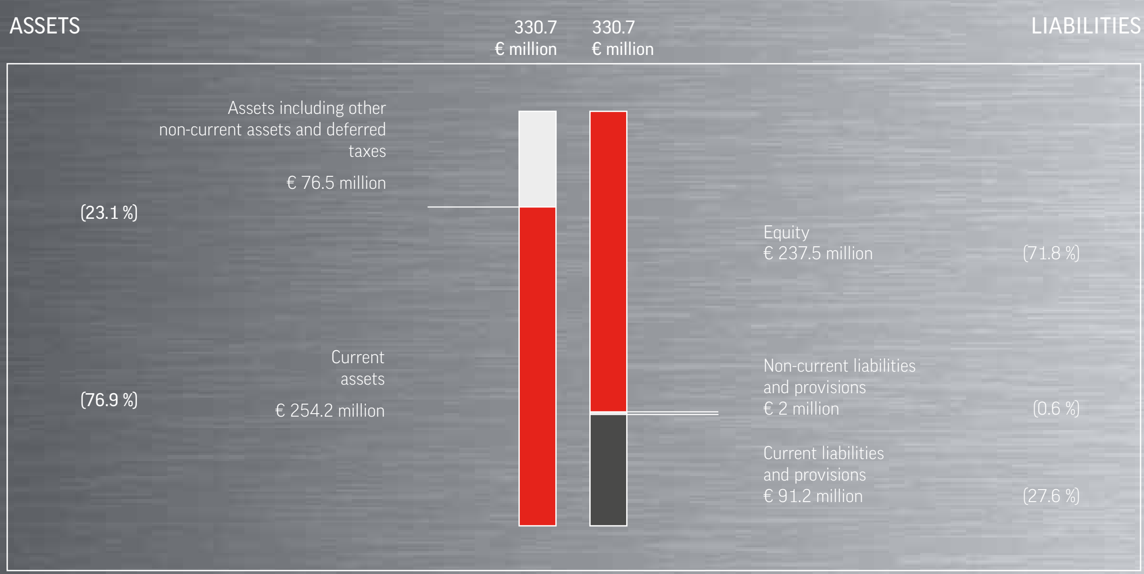
Investments by Hermle AG in 2017, with a similar focus to those of the Group as a whole, rose from € 15.1 million to € 16.3 million.



Net assets: Equity ratio still high at 72 %

The consolidated Group balance sheet of Maschinenfabrik Berthold Hermle AG at the 2017 reporting date grew by 6.8 % against the previous year to € 330.7. On the Assets side, non-current assets increased overall by 24.1 % to € 76.5 million, primarily due to the two major projects aimed at safeguarding the long-term future of the business, which resulted in an increase in property, plant and equipment assets by 17.2 % to € 66.7 million, as well as due to the long-term financial investments. Intangible assets changed insignificantly from € 1.5 million to € 1.8 million. The main factor in the 2.5 % rise in current assets to € 254.2 million was the 15.9 % increase in inventories to € 62.1 million. The reasons for that increase were the already mentioned above-average increase in factory stocks, an increase in raw materials, supplies and consumables, with the aim of improving security of supply, as well as higher advance payments on inventories. The expansion of business also led to an increase in accounts receivable from trading by 4.3 % to € 61.2 million. Securities and other assets increased from € 10.6 million to € 22.1 million. This was because we invested in fixed-term deposits with terms of more than three months and promissory note loans similar to fixed-term deposits as a result of the ECB's sustained zero interest rate policy. Conversely, cash and cash equivalents decreased from € 121.0 million to € 103.4 million.

HERMLE GROUP BALANCE SHEET STRUCTURE (12.31.2017)



The Equity and Liabilities side of the balance sheet was again characterized mainly by own funds, which increased by 3.3 % to € 237.5 million thanks to the again very healthy earnings. The equity ratio remained high, at 71.8 % (previous year: 74.3 %). The non-current liabilities and provisions increased from € 1.6 million to € 2.0 million, due – among other factors – to the rise in provisions for part-time working prior to retirement. Current liabilities and provisions increased by 16.9 % to € 91.2 million. Trade payables increased, as a result of the higher business volumes, from € 8.5 million to € 11.4 million. Personnel provisions were also topped up as a result of the increase in workforce numbers and in connection with due bonus payment as well as a rise in tax reserves, so that current provisions and tax reserves increased from € 40.3 million to € 43.6 million. The increase in advance payments received on orders also led to a rise in other current liabilities from € 29.3 million to € 36.2 million.

The balance sheet total of Hermle AG at the reporting date was up 6.6 % at € 264.2 million. 72.2 % of that total was own funds (previous year: 74.8 %).

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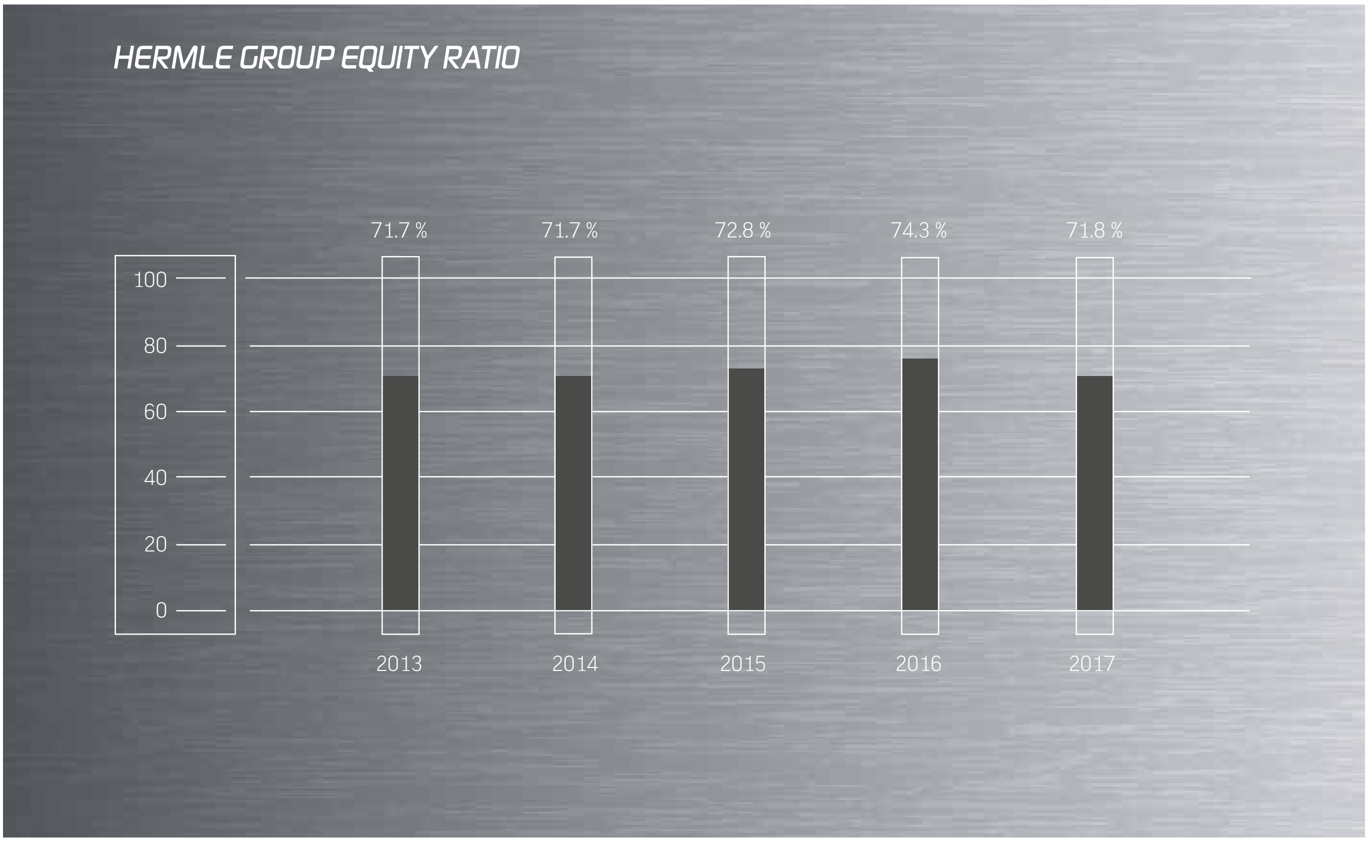

Overall assessment of the economic situation and comparison with the forecast

In 2017, Maschinenfabrik Berthold Hermle AG maintained its market position and generally performed better than expected. Despite the many still persisting economic uncertainty factors, demand for our machines and automation solutions grew at an increasing pace from the second quarter onward. As a result, on presenting our half-year interim report we were able to make an upward adjustment to our modest start-of-year forecast, which had in fact predicted a decline. Incoming orders rose by almost 19 % Group-wide to € 433.2 million. Group sales increased by 2 % to € 402.0 million, while operating earnings of € 99.0 million were virtually at the previous year's level. Consequently, the trend in our sales and earnings was within the bounds of the revised forecast, which had predicted sales volumes at or slightly above the 2016 level and earnings at or slightly below it.

Hermle's financial and asset position remained very sound. Operating cash flow totaled € 81.1 million, and the equity ratio was around 72 %. Overall, the Management Board considers the earnings, financial and asset position of Hermle AG and the Group at the time the financial statements were prepared to be still very good.

ADDITIONAL PERFORMANCE INDICATORS

Development: A new model in the Performance line

We maintained our research and development activities at a high level in 2017. The focus was again on new machines, automation solutions and digitalization modules meeting the different requirements of our customers. Among the key innovations we presented in the past year was the new C 650 machining center, which extends the top end of our Performance line for cost-effective three- and five-axis machining. As an entry-level solution for automating our machining centers, we launched the HS flex handling system, which can be adapted to both Performance and High Performance line machine models. We also expanded our suite of software solutions for Industry 4.0 applications.

And we achieved progress in generative manufacturing, which we offer to our customers as a service: In view of the strong demand for our metal powder application (MPA) technique, during the reporting period we began adapting the technology to our C 42 machining centers in order to expand the capacities of our MPA machinery portfolio with appropriate new models in future.

Production: In-house production of machine base units launched

In parallel with our operational activities during the year under review we also worked intensively on two major projects aimed at safeguarding the long-term future of the business: at the Zimmern ob Rottweil facility established in 2016, and at the corporate headquarters in Gosheim. At Zimmern, a state-of-the-art production facility incorporating all the relevant plant for the in-house production of so-called mineral casting beds, the base units of our machines, was completed in the first half of 2017. This has secured the supply of these vital components, which we had previously bought in, and has enhanced our manufacturing know-how in a strategically key area. Mass production was started in July 2017. We are now producing mineral casting beds for all our machine models, as well as various components, at the facility.

At the corporate headquarters in Gosheim, the modernization and enlargement of our chip removal manufacturing – one of our core competencies – was continued in the year under review. Following the building extension work carried out in 2016, in the first half of 2017 we completed the installation work as planned, and set up the first technical systems, all while maintaining ongoing operations. During the works vacation period in August, the old parts of the building were removed and work was started on the construction of a new large-scale machining facility, which was completed in early 2018. By expanding this area of our production, we are responding to the sustained high demand for our products and the increasing numbers of larger machines being ordered, entailing a correspondingly greater amount of space.

We have also improved the efficiency of module assembly at the Gosheim location based on optimized process flows.

Improved logistics processes and greater security of sourcing

In the logistics field, we developed a new warehouse strategy in 2017 in order to further reduce the picking effort for each machine. Thanks to innovative warehousing systems, we are also able to utilize the greater height of the new facility more effectively and so further improve the efficiency of our logistics.

By establishing our own mineral casting production facility, we have increased our in-house production rate and enhanced our security of supply of these key components. We will still be procuring some machine beds externally in future however. We generally operate on a basis of long-term collaboration and trust with our suppliers, and therefore experienced no bottlenecks in the procurement of key materials and components in the year under review.

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Intensive service and sales

In order to further enhance our acknowledged industry-leading high standards of service and rapid response capability, we again strengthened our service network in Germany and internationally in 2017. This has brought us closer to our customers, and also made our organization more decentralized.

We presented our product portfolio to the market at some 40 national and international trade fairs in the past year. Alongside the Hermle Open House, the world's leading trade show for the metalworking industry, EMO, held in Hanover in September, was of major importance for us. At those events, we introduced industry insiders to new products and features including our new C 650 machine, innovative automation solutions such as the HS flex handling system, and our growing portfolio of software modules for the digitalization of production processes.

We also once again hosted numerous workshops, in Germany and internationally, at which we informed our customers of innovations and new technologies from Hermle.

Employees: Workforce grows to 1,086 persons

The number of people employed by the Hermle Group as per the 2017 reporting date totaled 1,086 – an increase of 6.7 %, or 68 people, year-on-year. The increase in the workforce above and beyond the business volumes resulted largely from the establishment of in-house mineral casting bed production at the Zimmern location, for which purpose alone 27 additional staff were recruited. The workforce also grew – primarily in the production departments – due to the employment of apprentices following their successful completion of training and the corresponding new intake. The production workforce overall increased from 395 to 425 people. A number of new posts were additionally created in service functions in Germany and abroad. The number of people employed in customer service, supplier support and R&D increased overall from 554 to 585. The number of administrative staff increased from 69 to 76. A notable factor in this was the growing need for personnel to handle the increasing flood of regulatory requirements. Additional bureaucracy was necessitated, for example, by preparations for new data privacy laws, implementation into German national law of the CSR Directive, and the law governing transparency of pay to promote equality between men and women.

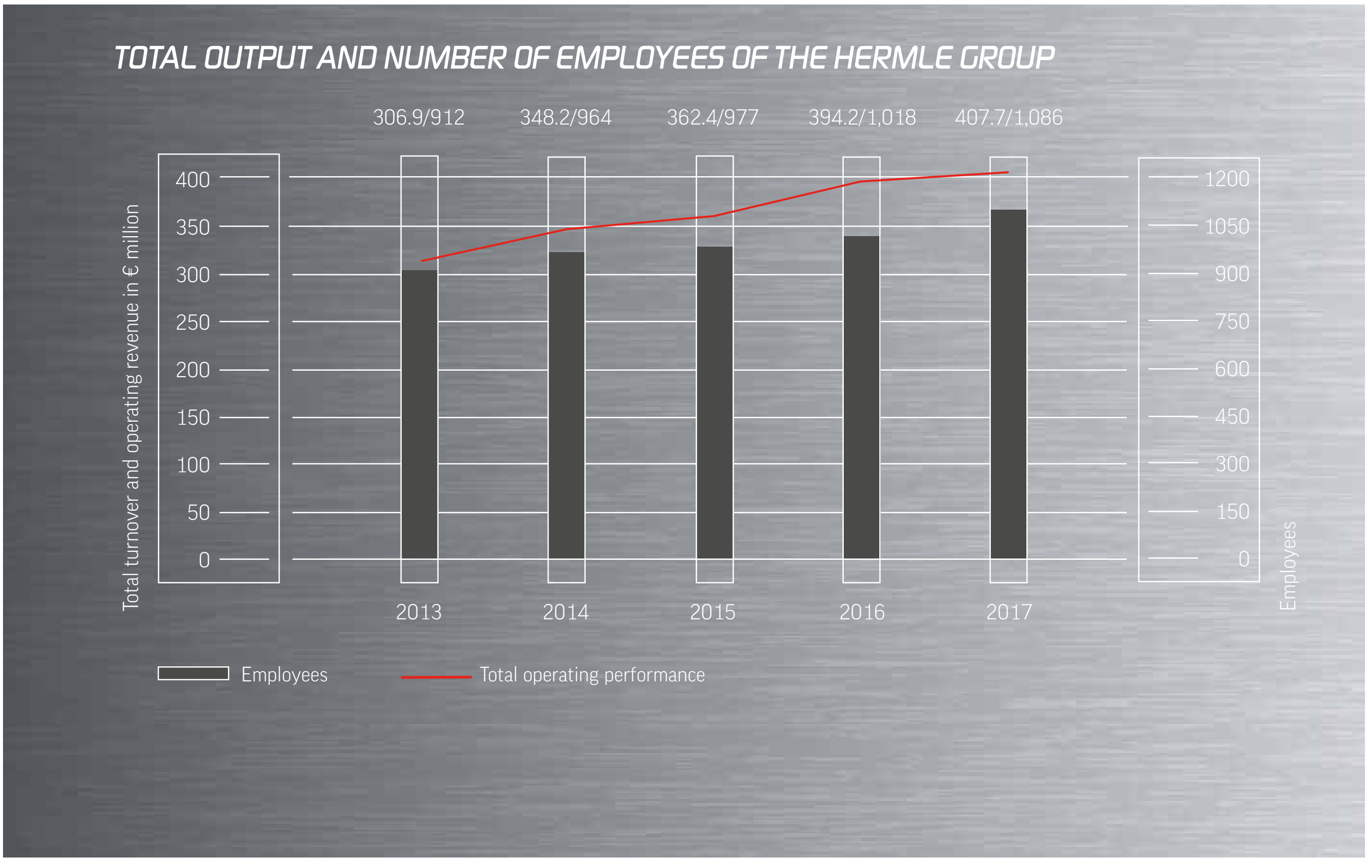
The workforce of the Hermle Group totaled 1,053 people on average in the past business year (previous year: 1,009), of which 927 people (previous year: 891) at the domestic companies in Germany and 126 (previous year: 118) in the Foreign Sales segment.

Hermle AG employed 937 people at the end of 2017 – 50 more than before the start of the year. The number of young apprentices included in that figure rose from 95 to 96. More information on our training activities is contained in the Social Affairs section of our Non-Financial Statement.

Strong performance by the Hermle team

The increase in business volumes achieved one again, and management of the parallel-running large-scale infrastructural projects, was only made possible thanks to the high levels of motivation and great know-how of our workforce. As in previous years, the employees of Hermle AG will again share in the company's success based on the healthy results achieved in 2017 and in recognition of their great efforts and commitment. A bonus will be paid to each employee following payment of the shareholders' dividend. At the suggestion of the Works Council, this previously mostly wage-linked payment has been changed to a fixed one-off amount, which for 2017 will be € 4,500.00.

Total output per employee in 2017 was €k 375.4 (previous year: €k 387.2). Our employees' flexitime accounts were well filled thanks to the high level of capacity utilization.



Diversity of the workforce

In order to recruit a wide range of skills and experience for our business, and in response to the shortage of skilled workers in Germany, we promote diversity and tolerance with regard to gender, nationality, age, and disability. To enhance diversity among our workforce, we are making efforts in particular to increase the number of women employed in commercial and technical functions. The percentage number of women in the Hermle AG workforce increased in 2017 from around 6 % to over 7 %. Well over 80 % of all jobs at Hermle, and some 90 % of the roles at the top two management levels, have a technical focus, and require a technical, engineering or trades qualification, or qualification in the so-called MINT subjects (mathematics, information technology, natural sciences and technology) – fields in which women remain underrepresented. Consequently, in our recruitment procedures for technical staff we aim to consider at least a number of women proportionate to the total number of applicants. In 2017 we succeed in appointing a woman to a master tradesperson's post in the trade skills training function. We are also specifically targeting the recruitment of young female staff through events in schools and so-called "Girls' Days". Disclosures relating to the percentage numbers of women in management positions at Hermle are contained in the Corporate Governance Statement pursuant to sections 289f and 315d HGB. Additional mandatory disclosures by the parent company in accordance with the German law governing transparency of pay to promote equality between men and women ("Entgelttransparenzgesetz") are contained in the Remuneration Report appended to the parent company management report.

The increasingly international nature of the business is creating increasing numbers of roles within the organization for employees of different nationalities. In order to strengthen our presence on key international selling markets, and intensify local customer relations, we specifically aim to recruit native-speakers from the regions in question, such as from Eastern and Southern Europe, Turkey, and Russia.

Our aim is to promote our employees' long-term loyalty to the company, so as to retain the great wealth of experience of older employees especially. We do, however, also offer older employees the possibility to switch to part-time working models prior to retirement if they are interested in so doing. The average length of service of Hermle AG employees in the past business year remained at 12 years. 19 people have celebrated 40 years of service with the company in the last 10 years. The average age of the workforce in 2017 remained unchanged at 37.

Hermle also offers attractive employment to people with disabilities. In 2017 the percentage number of disabled persons employed by Hermle AG remained around the previous year's level of 3 %.

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SUPPLEMENTARY REPORT

Following the conclusion of the 2017 business year and up until this report was signed off, there were no events that had significant effects on the net assets, financial position, results of operations and cash flows of Hermle AG or the Group. With effect from January 1, 2018, Hermle AG acquired the remaining 51 % of shares in Hermle-Leibinger Systemtechnik GmbH from its former co-shareholders. Consequently, from 2018 onward the company, in which we previously held a 49 % interest, will be fully consolidated into the Hermle Group. This will not have a material effect on the development of sales and operating results however. At the end of 2017 the Gosheim-based HLS employed 85 people. The full takeover will provide us with greater flexibility in the key field of automation in future, and will further expand our portfolio of configurable automation solutions. No changes will result for our customers.

RISK AND OPPORTUNITIES REPORT

Risk and opportunities management

As an active, medium-sized company, the Maschinenfabrik Berthold Hermle AG sees itself as being faced with a wide range of opportunities and risks regarding its activities. In that respect, it is frequently the case that opportunities can only be utilized if certain risks are accepted. For this reason, managing opportunities and risks constitutes a fundamental element of our corporate governance, and it is of great importance for Hermle's long-term positive development. We aim to take risks only if an appropriate contribution towards our value as a going concern can be expected from the associated business transaction.

The basis of our risk and opportunity management is our Group-wide planning and controlling system. This provides us with early information on important external or internal changes which might entail opportunities or risks for Hermle. The information is regularly reviewed within the company on a cross-divisional basis. As part of this open discussion, we develop suitable strategies to deal with the respective opportunities and risks.

Internal control system

In addition to our risk and opportunities management, we have put in place an internal control system (ICS). Core elements of the ICS include application of the two-person rule as a matter of principle, and the general separation of central functions into the areas and business processes of key importance to the company's overall risk situation, which are additionally secured by access controls on IT systems. We also undertake monthly analyses of order receipts, sales revenues and key expenditure items, as well as monitoring trends in individual cost categories in order to identify any discrepancies quickly. Moreover, our product and order costing procedures, service delivery, warehousing and production operations incorporate appropriate monitoring mechanisms to detect changes at an early stage. In 2017 the internal control system (ICS) was enhanced in relation to new machinery sales, service and human resources, and expanded to cover the monitoring of tax risks.

Presentation of key risks

The following sets out the key risks for Hermle, in the order of their significance:

Market and macroeconomic risks – In our view, the uncertain macroeconomic conditions, deriving from wide-ranging political and economic factors, continue to pose a high risk. Generally speaking, the already fast-moving and fluctuating cycles in our industry might be exacerbated by any downturn in economic conditions. Alongside the widening political differences within the EU and the continuing lack of clarity as to the consequences of Brexit, we regard the protectionist tendencies in the USA, the increasing difficulty of exporting to Russia as a result of the sanctions imposed, and the over-indebtedness of many countries and other economic players, as especially critical. These factors might both directly and indirectly impose burdens on Hermle. As well as these factors, the regulative pressure and bureaucratization in Germany continue to increase, and this is not conducive to a positive economic development. Hermle is able to adapt very well to normal fluctuations in the economic cycle through flexible structures and processes within the concept of the 'breathing company', particularly thanks to the further topping-up of our employees' flexitime accounts. Our healthy liquidity and high equity ratio, and our resultant high degree of independence, additionally help Hermle to withstand even major fluctuations in demand without harm.

Competition risks – Hermle responds to the strong price and competition pressure that applies to machine tool production with particularly high-quality machines, system solutions geared to customers' individual needs and a highly competent and reliable service to reinforce customer loyalty. Through our intelligently structured product range and the modular construction of our machines, we also put ourselves in a position to offer tailor-made solutions and at the same time maintain a sound cost structure. The specific tailoring of what we have to offer to meet differing market requirements also has positive effects.
We counter trends toward market consolidation on the demand side and the risk of associated dependencies through regional and industry-specific diversification and by striving to acquire new customer accounts and open up new markets. We reduce the risk of companies defaulting on payment through insolvency through intensive scrutiny of orders and comprehensive receivables management.
The risk of our products being imitated is increasing due to the growing internationalization of our sector. Hermle responds to this by bundling the R&D activities at the Gosheim location, stringent access regulations and own production to a considerable depth. The fundamentally highly complex nature of the machines also provides a degree of protection.

Innovation and product risks – We counter risks associated with innovation by regularly exchanging ideas with customers, system suppliers and other market participants. The information obtained is used to orient Hermle machines consistently towards market requirements. Also, our extensive R&D activities consolidate our role as a technological leader. Product liability risks are reduced by way of intensive testing prior to market launch as well as by suitable contractual arrangements and insurance policies.

Production risks – Careful, pro-active and comprehensive maintenance and investment measures at an early stage reduce the risk of production downtimes and keep Hermle's production plant up to date. This is augmented by our efficient organizational structures that ensure smooth production processes. Operating errors are very unlikely to occur thanks to our employees' high skill levels.

Quality risks – The high quality of our machines and service is a key factor for Hermle's competitiveness. It is guaranteed by way of systematic quality management, comprehensive testing procedures and training for our employees.

Procurement risks – To avoid procurement bottlenecks, Hermle selects suppliers carefully and cooperates with them fairly and generally on a long-term basis. The increasing degree of overheating on various procurement markets is, however, making it difficult for Hermle – as others – to achieve further production increases in some areas. Where this is considered wise, we reduce the risk of procurement shortfalls by means of a second-source strategy as well as a program of rolling demand planning. We obviate the increasing risk regarding energy supplies resulting from Germany's move away from nuclear power and its energy transition policies to some extent by operating our own combined heat and power (CHP) plants.

Personnel risks – As our employees generally train within the company and regularly take part in qualification measures, they have high levels of specialist competence. Our workforce is intrinsically highly motivated and reliable, and this is enhanced by an interesting working environment, in many cases long periods of employee service, and a philosophy that gives them a sense of personal responsibility and independence in carrying out work. We are responding to the expected increasing shortage of skilled workers in Germany resulting from current demographic trends by presenting ourselves as an attractive employer, by committing strongly to education and training, and by promoting the recruitment of women to the workforce, especially in technical functions. All in all, we consider personnel risks to be low.

IT risks – We counter IT-related risks through the use of state-of-the-art technology and redundant systems in key areas. As part of this approach, Hermle operates two mirrored computer rooms and an additional room for data backup in different parts of the building, as well as applying thorough security mechanisms to ensure maximum data protection. We assign high priority to data security, which is why we have expanded our employee training in that area.

Financial risks – Hermle is very unlikely to be exposed to financial and liquidity risks, as we finance major capital investment projects and our ongoing business operations internally on the whole, are very conservative in our balance sheet management, and maintain a high equity ratio. Currency risks are minimized by way of suitable hedge transactions, which are described in detail in the Notes to the consolidated financial statements, item 30. Additionally, tax risks might arise from routine audits.

Overall risk situation – In the view of the Management Board, the discernible risks to which Hermle is currently exposed are controllable, and continue to pose no threat to the existence of the business, either singly or in combination.

Presentation of the opportunities

Significant opportunities arise for Hermle from the strengths of the business and the environment in which it operates. They are presented below and divided into these categories:

Business environment opportunities – If the underlying macroeconomic and industry-specific conditions develop better than expected, Hermle is basically in a position to outperform its forecast business development. Thanks to our concept of the Breathing Company, allied to flexible capacity reserves and processes, we have a high supply capability, and are in a position to exploit any potential economic upturns.

The boost to our customers' business entailed by an economic upturn additionally improves the opportunities for selling our products. In periods of strong demand, our customers generally need reliable, high-performance machines such as Hermle manufactures.

Also, the trend towards digitalization and automation in manufacturing (Industry 4.0) – reinforced by the demographically driven shortage of skilled workers in Germany – provides Hermle with further expansion potential, because it demands high-quality, extremely reliable machines.

We continue to see particularly big growth opportunities abroad. We are therefore expanding our position in key markets, and are reviewing additional interesting sales regions on an ongoing basis. The increasing maturity of various international markets where Hermle is already present opens up the opportunity for us to sell greater volumes of higher quality machining centers to them.

Opportunities deriving from the strengths of the business – The high skill levels and outstanding commitment of Hermle's workforce underpin the success factors of flexibility and quality already cited in relation to the external opportunities, and so strengthen our already healthy market position. The commitment, experience and know-how of our employees also helps us to cope with fluctuations in demand and capacity utilization, and to enhance customer loyalty based on strong service.

Our good name established in the past as a reliable partner focusing on quality and service based on continuity generally enables us to gain additional customers in existing and new market segments. Also, the high reliability of our machining centers and our state-of-the-art, needs-oriented product portfolio, with ongoing innovations, also increase the chances of gaining new customers as well as opening up potential for additional applications by our existing customers. The new high-grade, standardized and therefore cost-effective, 3- and 5-axis models that now augment the machinery portfolio have also improved our prospects of opening up markets in new regions.

Thanks to our healthy liquidity and equity ratio we are financially independent, enabling us to respond rapidly to fluctuations in the economic cycle, and to withstand economic downturns for longer.

FORECAST

Global economic upturn expected to continue

The International Monetary Fund forecasts that the global economy will again pick up pace in 2018, growing at a rate of 3.9 % overall. It sees the main drivers of growth – forecast at 4.9 % – as being the emerging economies. The IMF again expects substantial increases in China and India, though it predicts that the pace of growth in China will slow further, while the Indian economy will gain momentum. It also predicts that the recovery in Russia and Brazil will be maintained. The forecast for the industrialized nations is for 2.3 % growth, as last year – at a somewhat more dynamic pace in the USA and slightly more modestly in most of the other countries. The IMF forecasts that Eurozone GDP will rise by 2.2 %. The German Federal Government forecasts that Germany's economy will grow at a rate of 2.4 %. The IMF continues to point out numerous uncertainty factors and risks for the economy. Negative effects might be felt, for example, as a result of nationalist tendencies in the USA and some European countries, the wide-ranging political crises and conflicts around the world, and the resultant refugee movements. In terms of monetary policy, upheavals are possible if expansive activities are sustained, and also in the event of shifts in exchange rates. Other factors include elections in some countries, as well as the lack of progress in Brexit negotiations.

Positive climate in the industry

The economists at the German Engineering Federation VDMA forecast that sales in the plant and machinery manufacturing sector worldwide will increase by about 4 % in 2018. Against that background, German manufacturers need to up their production by a further 3 %. The industry association considers it likely that demand in China will grow somewhat more slowly, and will decline in the UK, though exports to the USA and other EU member-states are predicted to remain stable. The VDMA hopes to see an upward trend in domestic demand.

The outlook for German machine tool manufacturers this year is likewise bright. The VDW forecasts that international machine tool consumption will increase by 3.6 % based on the dynamic rate of global economic growth. The main drivers are likely to be Europe and America, while in Asia a slowdown is predicted following the strong growth of last year. German manufacturers are forecast to be in a position to increase their production by 5 % on that basis.

Hermle predicted to increase sales and earnings in 2018

Hermle's healthy progress was sustained through the early weeks of 2018. Against the background of the high backlog of orders from last year, we forecast that full-year Group sales will rise in the mid to upper single digit percentage range. This is subject to the proviso that the framework conditions develop as forecast, and the numerous economic risks do not actually occur. The operating result is forecast to improve at a similar rate, though the trend is expected to be lower than the rise in sales. In view of the strains on procurement markets, the possibility of price increases on raw materials cannot be ruled out, and it might not be possible to pass them on in full. Other potentially impacting factors are the increase in collective pay rates and the possibly still weak US Dollar. We forecast that the rate of incoming orders will stabilize in 2018.

Financial and asset position remains very sound

The expected increase in earnings will further underpin Hermle's already sound financial and asset position in the current year. This should enable us to continue financing capital investment projects and our business operations from our own funds, and without taking on bank liabilities, in future.

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Management report of the AG and Group management report

Investments in production and logistics

The investment volume of the Hermle Group is forecast to decrease in 2018 based on current estimates, but will still be above normal levels. Following the commissioning of the large-scale machining facility planned for the first quarter of the year, in the coming months a number of Hermle machining centers will be installed in the chip removal manufacturing area, thereby making optimized use of available space. We are also going to be adding a new system to boost our warehousing and logistics capacities, so cutting down further on transportation and picking times. Other areas of focus are a transformer substation for the modernized building in order to reduce power loss, and new parking for our employees.

Workforce increased slightly

In connection with the expansion of business, the number of people employed by Hermle will also increase slightly in 2018. Recruitment is planned in areas including service and mineral casting production. We will also likely be employing apprentices following their successful completion of training and recruiting a new intake of apprentices to replace them.

Development focus on automation and digitalization

In view of the strategic importance of innovation to the success of the business, we will be maintaining intensive development activities at the same high levels in 2018. The focus will be on new automation components and additional features for our digitalization modules, aimed at helping our customers to establish Industry 4.0 standard manufacturing. Among the major new launches at this year's Open House, for example, are an innovative robot system featuring a Kanban storage system, additional components for the HS flex handling system, and new developments of software modules to match them. In the field of generative manufacturing, we are planning to complete the adaptation of our MPA technology to our C 42 machining center and start running the first prototype during the reporting period.

Overall assessment of the future development

The Management Board forecasts that the sales and earnings of Maschinenfabrik Berthold Hermle AG and the Group will grow in the mid to upper single-digit percentage range in 2018. This is based on the healthy backlog of orders from last year. The orders situation is forecast to normalize during 2018. On completing our two major projects aimed at safeguarding the long-term future of the business, we have adjusted our capacities to the sustained high levels of demand. In addition to this, there is enough space at the Zimmern location for additional activities with new products and services. Our concept of a Breathing Company, along with our very sound financial and asset position, also provides us with maximum flexibility to respond appropriately to the economic fluctuations that are common in our industry. Thanks to our portfolio of machinery tailored to differing market requirements, and the wide-ranging automation and digitalization solutions we offer, we see good opportunities for long-term positive development of the business well into the future.

Gosheim, March 2018

Maschinenfabrik Berthold Hermle AG

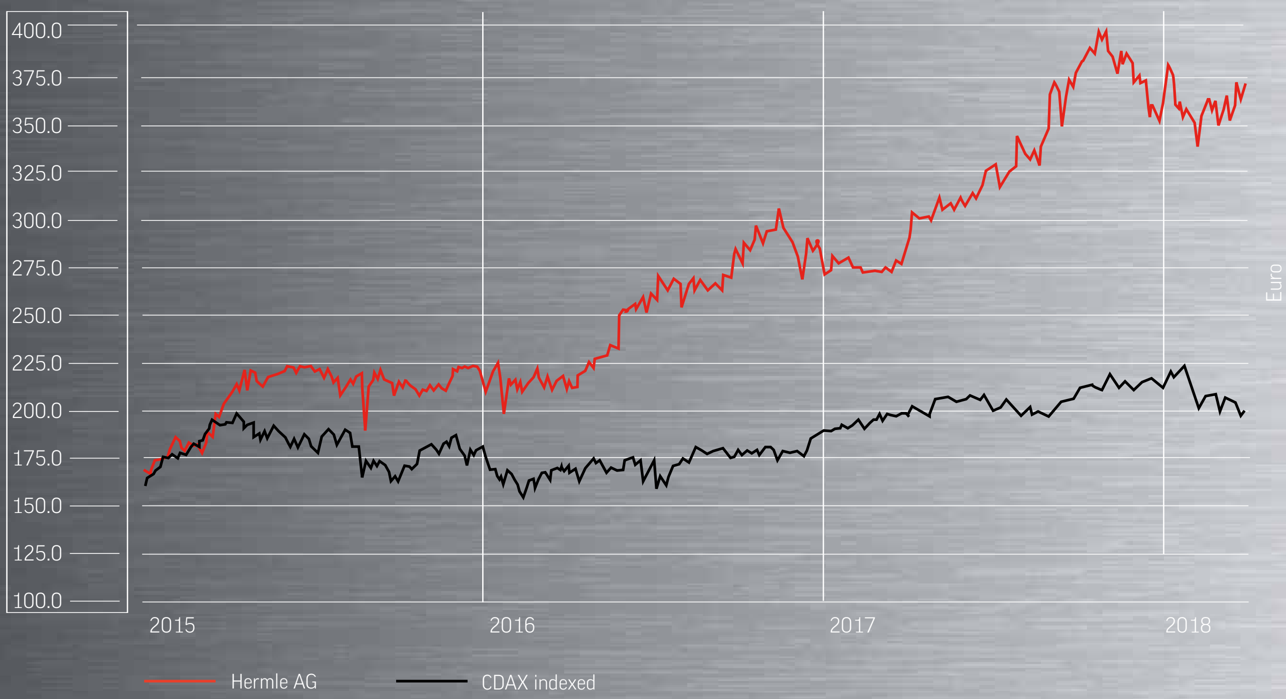
Management Board

02.3 The Hermle share

Positive mood on share markets

2017 was a good year for stock markets worldwide. Markets around the world were boosted by favorable economic data and the sustained expansive monetary policies of many central banks. Key indices in the USA recorded major gains despite the unclear course of the US government for example. Stock markets in other parts of the world also profited: Strong gains were seen in Asia and Latin America. Trends on European exchanges were somewhat more modest. Nevertheless, the Euro Stoxx 50 index recorded growth of around 6 %, while the UK's FTSE 100 ended last year 8 % up, despite the risks entailed by Brexit. Germany's DAX index was up 12.5 %. The CDAX, reflecting the development of all German stocks in the Prime and General Standard sectors, closed about 16 % up.

PRICE DEVELOPMENT OF THE HERMLE SHARE FROM JANUARY 2015 TO MARCH 2018



02.3
The Hermle share

Hermle share increases in value by almost a third

The price of the Maschinenfabrik Berthold Hermle AG preference share barely moved initially in early 2017. The year low was recorded on February 2, at € 271.00 – the same as the 2016 closing price. From the second half of March onward, the price climbed almost constantly, and by October 24 had reached its high for the year of € 398.00. It reached that level again on November 1, before falling back again in the last two months of the year. At the end of 2017 the Hermle preference share price was €359.00. It had thus gained 32.5 % in value during the reporting period.

KEY HERMLE PREFERENCE SHARE DATA (IN €)

	2013	2014	2015	2016	2017
Result per preference share[1]	9.17	11.79	11.88	14.81	14.70
Cash flow[1]	10.30	12.85	13.08	16.15	16.21
Shareholders' equity[1]	37.03	40.55	41.96	45.99	47.50
High[2]	168.00	188.45	224.00	306.15	398.00
Low[2]	93.30	144.42	160.00	198.00	271.00
Closing price[2]	150.80	161.53	214.10	271.0	359.00
Year-end profit ratio	16.44	13.72	18.02	18.30	24.42
Year-end cash flow price ratio	14.64	12.57	16.37	16.78	22.15
Dividend per preference share	0.85	0.85	0.85	0.85	0.85[3]
Bonus	7.20	10.00	10.00	12.00	12.00[3]
Special bonus					2.20[3]
Price on March 29, 2018					371.00

[1] Share basis: 5,000,000 shares
[2] Source: Stuttgart Stock Exchange
[3] Subject to approval at the annual general meeting

Earnings per share more or less stable

The Hermle Group's 2017 net income of € 73.3 million was at virtually the same high level as the previous year's € 73.8 million. The earnings per share thus barely changed, and stood at € 14.70 per preference share. At the 2017 year-end, this resulted in a price-earnings ratio of 24.42. The cash flow and equity per share each increased slightly, to € 16.21 and € 47.50 respectively.

One-off dividend increase to € 15.05 planned

The net income of the parent company Hermle AG improved in the reporting period from € 64.6 million to € 69.3 million. The balance sheet profit, including the retransfer of revenue reserves, was € 75.4 million (previous year: € 64.1 million). The Management Board and Supervisory Board will propose to the shareholders' meeting on July 4, 2018 that from that amount, as in the previous year, a basic dividend of € 0.85 per preference share and € 0.80 per ordinary share be paid, as well as a stable bonus of € 12.00 per share. In view of the prevailing low interest rates, and the changed political conditions, the payment of a one-off special bonus of € 2.20 is additionally planned. In total, this corresponds to an increase in dividend per preference share from € 12.85 to € 15.05, and a return on dividend of 4.2 % measured against the year-end closing share price.

The share capital of Maschinenfabrik Berthold Hermle AG is, without change, divided into 4 million ordinary shares and 1 million non-voting preference shares, however these have a dividend preference. The preference shares have been quoted on the stock exchange since 1990, and are traded on the regular market of the Stuttgart and Frankfurt am Main stock exchanges.

Corporate governance and transparency

Maschinenfabrik Berthold Hermle AG is committed to responsible corporate governance. Our aim is to safeguard the long-term future of the Hermle Group, enhance its value, and balance the interests of our shareholders, customers, employees, suppliers, and other partners. To that end, we apply a dedicated corporate governance concept based on legal standards and on the rules of procedure of the Management Board and Supervisory Board. Further information on this is contained in our Corporate Governance Statement, which is available on our website at www.hermle.de in the Investor Relations / Mandatory Disclosures section. Our Corporate Governance Statement pursuant to section 161 AktG can also be downloaded from the same location, and is additionally printed on page 79 of this annual report.

For Hermle, good corporate governance includes transparent and responsible communication.
We provide information to our shareholders and potential investors, the financial media and financial market players on business trends and key events in a timely manner, and based on a policy of equality. We do so primarily through our annual and half-year interim reports, interim bulletins reporting on the first and third quarters, as well as through media releases and ad-hoc reports.
Interested parties can view these publications, together with extensive background material concerning the company and its products, on the website at www.hermle.de. The Hermle web presence was redesigned in 2017. The Machining Centers section of the website now presents seven argument in favor of Hermle, listing the company's strengths: Precision, Reliability, Long-term accuracy, 5-axis benchmark, Service competence, Fairness, and Location dedication. Our shareholders are also able to find out about the company in more detail through factory tours conducted on the occasion of our annual shareholders' meeting.

02.4
New expertise

Long-term success in the machine tool manufacturing industry, as in many others, demands a readiness to respond to changing market and customer requirements and to build the essential expertise. In line with those demands, Hermle again made progress in many areas in the past year: with product innovations and with new manufacturing know-how.

Innovation expertise: C 650 machining center and automation components

Alongside the sustained high demand for dynamic, high-precision, comprehensively equipped machining centers which Hermle covers with its High Performance line models, demand for cost-effective entry-level models for 3- to 5-axis machining is also growing in the machine tool manufacturing sector. To meet that demand, Hermle developed the Performance line, which 2017 was extended at the top of its range by an additional machine: the C 650. Like the C 400 and the C 250 in the same line, it is of the tried and proven modified gantry design. The machine base unit made of mineral casting originates from our in-house production. With capacity for up to 3000 kg workpieces in the 3-axis configuration, the C 650 is particularly suitable for our tool and die making customers. In fact, the swiveling rotary table required for 5-axis machining enables high-precision machining of workpieces up to a maximum of 1500 kg in weight.

The C 650 features an integrated magazine storing 42 tools, and can be optionally equipped with two additional magazines. A pivotable control panel and other details ensure an ergonomic design. Digital modules such as the Hermle Information Monitoring Software (HIMS) or the Hermle Automation Control System (HACS) can be integrated as required. The range of applications of the C 650 can be extended further with various systems for cooling, swarf removal, extraction, and tool breakage monitoring and measurement.

Another major trend in our industry is automation. We are continually broadening our offer in that area, and at our 2018 Open House we presented more innovations. The first was the RS 2 Combi robot system featuring Kanban storage, a platform-based solution with a 6-axis industrial robot capable of transporting components up to 240 kg in weight. Customizable racks additionally provide space for grippers, additional tool storage, or pallets and workpieces on dies. Also, the HS flex handling system has been upgraded to a multi-pallet system and provided with a gripper change feature which enables the use of a wide variety of different pallet systems.

02.4
New expertise

Digital expertise: Three steps to Industry 4.0

Many manufacturing operations are currently facing the challenges of digital transformation. In order to support our customers in the digitalization and automation of their processes, we offer a comprehensive smart suite of software modules that is continually being enhanced. It comprises three steps to Industry 4.0:

- Digital Production with software solutions for transparent, connected production processes, including based on intelligent order management (HACS), machine monitoring (HIMS) and tool organization (HTMC and HOTS).

- Digital Operation for smart machine tuning (HMT) based on dynamic adaptation of controller parameters and machining settings or practical machine control with a direct link to the entire IT infrastructure (Remote Desktop).

- Digital Service with the externally operable maintenance diagnostic system WDS and our uncomplicated remote maintenance.

In 2018 we presented upgraded software solutions linked to our product innovations as well as a new Digital Operation module: the Hermle Home Screen, featuring a customizable screen view that can be combined with the HACS and HIMS software components. The Digital Modules brochure available on our website details all Hermle software options.

As part of its commitment to advancing connectivity in manufacturing generally, Hermle is an active contributor to the VDW's "Machine tool – automation interface" working group, which is concerned with the standardization of interfaces in automated manufacturing processes, and has already developed a flexible standard for the easy integration of robots and other automation components into manufacturing systems. We are also supporting the VDW's "Connectivity for Industry 4.0" initiative, aiming to create a common, manufacturer-neutral interface between machines and higher-level IT systems.

New production expertise: Mineral casting

A key factor in attaining the high quality standards of our machining centers is that we are committed to in-house production in strategically important areas. That is why in 2017 we further expanded our expertise in mineral casting technology, commissioning our own machine bed production into operation. We have thereby also enhanced our security of supply of these key components.

The new production facility is located at the Zimmern ob Rottweil site which we established in 2016 as an investment in the long-term future development of Hermle. The plant in Zimmern was commissioned into operation in mid 2017. Today it makes base units for virtually all Hermle machine models, as well as other components. We previously outsourced our machine beds, but now over 80 % of our demand is met by in-house production. We will still be procuring some base units from external suppliers in future however.

The complex production of mineral casting beds first involves preparing the individual parts of the metal mold, installing components, and assembling them. Cores are produced subsequently to create the necessary recesses and cavities. Gelcoat parting compound is then applied to the finished mold, providing good shaping characteristics and a uniform surface color of the casting. Then the mineral casting, made from components stored in silos inside the production facility, is mixed and poured cold into the mold. The part sets overnight. Our staff then remove the mold, take out installed components and cores, detach the machine bed from the mold bottom, and place it on a pallet. The final steps involve finishing and post-processing, followed by precise photo-optical measurement and inspection of the part, before it is transported to Gosheim for fine chip removal and assembly.

Our mineral casting machine beds are characterized primarily by outstanding damping, high temperature stability, and immunity to chemical contamination and mechanical stress. As additional benefits, the manufactured parts are flexible in design and can be disposed of in an environmentally friendly way.

03 Consolidated Financial Statements

Machine construction.
Gearwheel.

Machine construction. Gearwheel with worm gear external splines
and straight internal splines produced by hob peeling.

03.1 Group Balance Sheet

ASSETS	Notes to the financial statements	12.31.2017 €k	Previous year €k
A. Non-current assets			
I. Intangible assets	(7)	1,754	1,462
II. Property, plant and equipment	(7)	66,737	56,949
III. Shares in companies valued using the at equity method	(7)	1,073	1,012
IV. Other financial assets	(7)	5,006	5
V. Other non-current assets	(8)	49	61
VI. Deferred tax assets	(25)	1,911	2,155
		76,530	61,644
B. Current assets			
I. Inventories	(9)	62,083	53,547
II. Accounts receivable from trading	(10)	61,162	58,640
III. Other current assets	(10)	5,404	4,130
IV. Securities and other assets	(11)	22,118	10,610
V. Cash and cash equivalents	(12)	103,390	120,992
		254,157	247,919
TOTAL ASSETS		330,687	309,563

LIABILITIES		12.31.2017 €k	Previous year €k
A. Equity			
I. Equity of shareholders of Hermle AG	(13)	237,494	229,924
II. Minority interests	(14)	17	16
		237,511	229,940
B. Non-current liabilities and provisions			
I. Other non-current assets	(16)	0	65
II. Long-term provisions	(15)	1,523	1,351
III. Deferred tax liabilities	(25)	431	140
		1,954	1,556
C. Current liabilities and provisions			
I. Current trade payables	(16)	11,418	8,466
II. Other current liabilities	(16)	36,234	29,317
III. Tax provisions	(15)	4,464	2,842
IV. Short-term provisions	(15)	39,106	37,442
		91,222	78,067
TOTAL LIABILITIES		330,687	309,563

03.2 Consolidated Income Statement

	Notes to the financial statements	2017 €k	Previous year €k
Sales	(17)	402,009	393,950
Change in stock of finished and unfinished products		4,519	-4
Other own work capitalized		1,137	248
Total turnover and operating revenue		407,665	394,194
Other operating income	(18)	8,849	9,432
Material costs	(19)	180,349	170,927
Personnel expenses	(20)	87,004	80,297
Depreciation on intangible assets, and plant and equipment	(21)	7,810	6,974
Other operating expenses	(22)	42,366	45,627
		317,529	303,825
Operating result		98,985	99,801
Result from companies valued using the at equity method	(23)	428	331
Other financial result	(24)	-8	180
Financial result		420	511
Earnings before taxes		99,405	100,312
Taxes on income and earnings	(25)	26,079	26,463
Net income		73,326	73,849
Profit shares of other shareholders		-2	-4
Profit share of Hermle AG shareholders		73,324	73,845
Result per share in €	(26)		
Per ordinary share		14.65	14.76
Per preference share including dividend preference		14.70	14.81

03.3
Group Overall Income Statement

	2017 €k	Previous year €k
Net income pursuant to income statement	73,326	73,849
Other total income		
Items that may subsequently be reclassified to the income statement		
Exchange rate changes	-2,315	472
Changes from derivative financial instruments	830	-173
Changes from financial instruments available for sale	0	0
Income tax on other overall income		
- Tax on currency changes	0	0
- Tax on changes from derivative financial instruments	-220	46
- Tax on changes from financial instruments available for sale	0	0
Total income tax on other overall income	-220	46
Other overall income after tax	-1,705	345
Overall income	71,621	74,194
Shares of other shareholders in overall income	1	4
Shares of shareholders of Hermle AG in overall income	71,620	74,190

03.4
Group Equity Statement

	Subscribed capital Ordinary shares €k	Subscribed capital Preference shares €k	Capital reserve €k	Mandatory revenue reserves €k	Other revenue reserves €k	Group balance sheet profit €k
At 31 Dec. 2015	12,000	3,000	3,286	1,749	101,021	86,511
Dividend for previous year according to shareholders' meeting resolution						-54,050
Net income 2016						73,845
Allocations to revenue reserves as per Art. 16(3) of articles of association					1,000	-1,000
Exchange rate changes						
Cash flow hedges						
Other changes						
At 12.31.2016	12,000	3,000	3,286	1,749	102,021	105,306
Dividend for previous year according to shareholders' meeting resolution						-64,050
Net income 2017						73,324
Withdrawal from revenue reserves					-6,000	6,000
Exchange rate changes						
Cash flow hedges						
Other changes					8	-8
At 12.31.2017	12,000	3,000	3,286	1,749	96,029	120,572

Total revenue reserves €k	Cumulated other equity from foreign currency conversion €k	Cumulated other equity from derivative financial instruments €k	Cumulated other equity from financial instruments available for sale €k	Equity of the shareholders of Hermle AG €k	Shares of other shareholders in the capital €k	Interests of other shareholders in cumulated Group profit €k	Equity €k
189,281	2,367	-150	0	209,784	1	11	209,796
-54,050				-54,050			-54,050
73,845				73,845		4	73,849
	472			472			472
		-127		-127			-127
209,076	2,839	-277	0	229,924	1	15	229,940
-64,050				-64,050			-64,050
73,324				73,324		2	73,326
	-2,314			-2,314		-1	-2,315
		610		610			610
218,350	525	333	0	237,494	1	16	237,511

03.5 Group Cash Flow Statement

	2017 €k	Previous year €k
Net income	73,326	73,849
Depreciation on fixed assets	7,810	6,974
Depreciation on marketable securities	176	0
Change in long-term reserves	172	264
Profit shares in joint companies	-428	-331
Cash flow before change in working capital	81,056	80,756
Elimination of after tax result from investment disposals	-361	-171
Commitment of funds / release of funds		
Inventories	-8,536	2,202
Accounts receivable from trading	-2,522	-8,725
Other short-term receivables	-1,274	-1,198
Deferred tax assets and other non-current assets	257	324
Short-term trade accounts payable	2,952	-205
Short-term provisions	3,285	3,772
Other current liabilities	6,917	-2,691
Non-current financial liabilities	-65	65
Deferred tax liabilities	291	-132
Inflow of funds from ongoing business activity	82.000	73.997
Disbursements for investments in property, plant and equipment	-17,579	-15,545
Proceeds from the disposal of property, plant and equipment	663	474
Disbursements for investments in intangible assets	-963	-895
Proceeds from the disposal of intangible assets	0	0
Dividends received from joint ventures	368	319
Disbursements for the purchase of third-party securities and other assets	-23,988	-10,610
Proceeds from the sale of outside marketable securities and other assets	7,303	26,007
Outflow of funds from investment activity	-34,196	-250
Funds raised / funds released from		
disbursement of dividends	-64,050	-54,050
Outflow of funds from financing activity	-64,050	-54,050
Exchange rate-related value changes*	-1,966	348
Change from direct charging without affecting the operating result*	610	-127
Other changes*	0	0
Change in funds	-17,602	19,918
Financial funds as per 01.01.	120,992	101,074
Financial funds as per 12.31.	103,390	120,992

*See Group equity statement and statement of asset additions and disposals

See explanations in Notes to the financial statements (27)

03.6 Group Segment reporting

	Domestic companies	Operations abroad	Consolidation effects	Consolidated financial statement IFRS
	2017 €k	2017 €k	2017 €k	2017 €k
Sales with third parties	252,169	149,840		402,009
Operating result	91,351	7,458	176	98,985
Share in profit for the period of companies valued at equity	428			428
Net income	70,332	5,640	-2,646	73,326
Long-term segment assets	71,753	4,777		76,530
of which Book value of the companies valued using the at equity method	1,073			1,073
Short-term segment assets	197,379	74,946	-18,168	254,157
Segment assets (Total assets)	269,132	79,723	-18,168	330,687
Segment debts including provisions	67,748	42,475	-17,047	93,176
Investments	21,994	1,549		23,543
Depreciation	6,840	970		7,810
Employees annual average	927	126		1,053

	2016 €k	2016 €k	2016 €k	2016 €k
Sales with third parties	234,660	159,290		393,950
Operating result	88,004	12,179	-382	99,801
Share in profit for the period of companies valued at equity	331			331
Net income	65,736	8,889	-776	73,849
Long-term segment assets	56,697	4,947		61,644
of which Book value of the companies valued using the at equity method	1,012			1,012
Short-term segment assets	194,267	65,211	-11,559	247,919
Segment assets (Total assets)	250,964	70,158	-11,559	309,563
Segment debts including provisions	58,006	33,427	-11,810	79,623
Investments	15,177	1,263		16,440
Depreciation	5,949	1,025		6,974
Employees annual average	891	118		1,009

See explanations in Notes to the financial statements (28)

03.7 Group Statement of Asset Additions and Disposals 2017

		Acquisition and manufacturing costs				
		At 01.01.2017 €k	Additions €k	Retirements €k	Transfers to other accounts €k	Currency adjustments €k
I.	Intangible assets					
	1. Concessions, industrial property rights and similar rights and values as well as licenses for such rights and values	6,769	345	31		-4
	2. Capitalized development expenses	3,136	618			
		9,905	963	31		-4
II.	Property, plant and equipment					
	1. Land, leasehold rights and buildings including the buildings on non-owned land	55,253	7,225	535	6,701	-354
	2. Technical equipment, plant and machinery	41,086	4,729	268	1,995	-110
	3. Other plant, operating and business equipment	26,806	5,274	1,909	143	-240
	4. Advance payments on property, plant and equipment	8,845	351		-8,839	
		131,990	17,579	2,712	0	-704
III.	Financial assets					
	1. Shares in companies valued using the at-equity method	1,012	61 [1]			
	2. Other financial assets	5	5,001 [2]			
		1,017	5,062			
Total I. to III.		**142,912**	**23,604**	**2,743**	**0**	**-708**

[1] Includes the proportionate annual result (incl. changes from elimination of interim profits) less the dividend distribution of the holdings valued at equity

[1] The addition relates to fixed-term bank deposits with terms of more than 1 year

	Depreciation						Residual book value	
At 12.31.2017 €k	At 01.01.2017 €k	Additions €k	Retirements €k	Transfers to other accounts €k	Currency adjustments €k	Cumulated depreciation €k	At 01.01.2017 €k	At 12.31.2017 €k
7.079	5.485	418	31		-1	5.871	1.284	1.208
3.754	2.958	250				3.208	178	546
10,833	8,443	668	31		-1	9,079	1,462	1,754
68,290	23,696	1,758	391		-103	24,960	31,557	43,330
47,432	32,413	2,174	201		-84	34,302	8,673	13,130
30,074	18,932	3,210	1,817		-171	20,154	7,874	9,920
357							8,845	357
146,153	75,041	7,142	2,409		-358	79,416	56,949	66,737
1,073							1,012	1,073
5,006							5	5,006
6,079							1,017	6,079
163,065	**83,484**	7,810	2,440	0	-359	88,495	**59,428**	**74,570**

03.8
Group Statement of Asset Additions and Disposals 2016

	Acquisition and manufacturing costs				
	At 01.01.2016 €k	Additions €k	Retirements €k	Transfers to other accounts €k	Currency adjustments €k
I. Intangible assets					
1. Concessions, industrial property rights and similar rights and values as well as licenses for such rights and values	5,985	805	56	35	
2. Capitalized development expenses	3,117	90	71		
	9,102	895	127	35	
II. Property, plant and equipment					
1. Land, leasehold rights and buildings including the buildings on non-owned land	52,645	2,345		163	100
2. Technical equipment, plant and machinery	40,057	1,142	185	26	46
3. Other plant, operating and business equipment	25,545	3,409	2.212		64
4. Advance payments on property, plant and equipment	419	8,649		-224	1
	118,666	15,545	2,397	-35	211
III. Financial assets					
1. Shares in companies valued using the at-equity method	999	13 [1]			
2. Other financial assets	5				
	1,004	13			
Total I. to III.	128,772	16,453	2,524	0	211

[1] Includes the proportionate annual result (incl. changes from elimination of interim profits) less the dividend distribution of the holdings valued at equity

	Depreciation						Residual book value	
At 12.31.2016 €k	At 01.01.2016 €k	Additions €k	Retirements €k	Transfers to other accounts €k	Currency adjustments €k	Cumulated depreciation €k	At 01.01.2016 €k	At 12.31.2016 €k
6,769	5,196	344	55			5.485	789	1,284
3,136	2,719	310	71			2,958	398	178
9,905	7,915	654	126			8.443	1,187	1,462
55,253	22,167	1,508			21	23,696	30,478	31,557
41,086	30,628	1,867	100		18	32,413	9,429	8,673
26,806	17,933	2,945	1,995		49	18,932	7,612	7,874
8,845							419	8,845
131,990	70,728	6,320	2,095		88	75,041	47,938	56,949
1,012							999	1,012
5							5	5
1,017							1,004	1,017
142,912	**78,643**	6,974	2,221	0	88	83,484	**50,129**	**59,428**

03.9
Group Notes to the Financial Statements

(1) General principles

Maschinenfabrik Berthold Hermle AG, which has its headquarters in Gosheim, Industriestrasse 8-12, Germany, and is entered in the Stuttgart Local Court ("Amtsgericht") commercial register under HRB 460397, is the primary controlling company of the Hermle Group. Maschinenfabrik Berthold Hermle AG and its subsidiaries manufacture and sell high-end precision milling machines and machining centers.

The consolidated financial statements of Maschinenfabrik Berthold Hermle AG were prepared in accordance with the International Financial Reporting Standards (IFRS), as applicable in the European Union (EU), and in compliance with the commercial requirements pursuant to section 315e HGB. In that respect, all applicable standards, concepts and interpretations that were mandatory on the reporting date were taken into account.

The statements of the companies incorporated in the consolidated financial statement are prepared pursuant to standardized accounting and valuation principles applicable on the reporting date December 31, 2017.

To improve the clarity of the presentation, some items of the balance sheet and income statement are summarized. These are stated separately and explained in the Notes to the financial statements. The income statement was prepared pursuant to the total cost type of accounting. The Group currency is the euro. Unless otherwise stated, the figures are presented in thousands of Euro, with the standard commercial rounding up or down.

The Management Board of Maschinenfabrik Berthold Hermle AG released the consolidated financial statements on March 29, 2018 for forwarding to the Supervisory Board. The Supervisory Board's responsibility is to review the consolidated financial statements and state whether or not it approves them.

(2) New and amended standards/interpretations

The IFRS standards were taken as a basis for the 2017 business year. Their application is mandatory for business years that commence on January 1, 2017.

The following standards and interpretations were mandatory for the first time in the current business year:

IAS 7:	Disclosure initiative (amendments)
IAS 12:	Recognition of deferred tax assets for unrealized losses (amendments)
IFRS 2014-2016:	IFRS 12 (amendments)

The first-time application of these standards and interpretations did not have any effects on the consolidated financial statements, because Hermle did not need to make any amendments to the accounting and valuation principles as a result.

The following new standards and interpretations, which have already been adopted by the European Union, have yet to come into force and were not taken into account in the statement:

IFRS 9:	Financial instruments
IFRS 15:	Revenue from contracts with customers and clarifications relating to IFRS 15 (amendments)
IFRS 16:	Leasing contracts
IFRS 4:	Application of IFRS 9 financial instruments and IFRS 4 insurance contracts (amendments)
IFRS 2014-2016:	IFRS 1 and IAS 28 (amendments)
IFRS 2:	Clarifications of classification and measurement of share based payment transactions (amendments)
IAS 40:	Transfers of investment property (amendments)
IFRS 9:	Financial assets with negative prepayment penalty (amendment)

Re IFRS 9: IFRS 9 'Financial instruments' is to be used in business years that start on or after January 1, 2018. IFRS 9 replaces the former IAS 39 'Financial instruments: recognition and measurement', and includes amongst other things a unified model for the classification and determination of the evaluation method (including depreciation) of financial instruments. In addition, IFRS 9 contains regulations for a general hedge accounting model as well as additional notes on the financial instruments.

Classification

The new standard contains a new classification and measurement concept for financial assets based on the business model within which assets are held and the characteristics of their cash flows. There are three key classification categories for financial assets: valued at amortized cost; valued at fair value, with value changes in profit or loss; and valued at fair value, with value changes in 'Other profit'. The IAS 39 categories 'held to maturity', 'loans and receivables' and 'available for sale' no longer apply.

Hermle expects no material effects on the recognition of trade receivables, loans and financial assets resulting from the new classification requirements.

Impairment

The new impairment model is applicable to financial assets valued at amortized cost or at fair value with no effect on profit and loss. The model stipulates three levels determining the expected losses and the future interest income. These take account of already expected defaults on loans, as opposed to losses actually incurred as previously according to IAS 39. Expected losses in the amount of an expected 12-month loss must be recorded from the point of acquisition. If a significant increase in default risk occurs, the risk provision must be topped up in the amount of the total loss over the entire remaining term. If objective evidence of impairment occurs, the interest income must be stated on the basis of the net carrying amount (carrying amount less risk provision). Hermle will most likely utilize the simplified method, applying the concept of "life-long loan default" to all trade receivables.

Within the Hermle Group, trade receivables are mainly affected by the new impairment model. Application of the impairment model will not have any material effects on other items in the consolidated financial statements.

Accounting for hedging transactions

IFRS 9 offers more possibilities for accounting for hedging transactions, and enables companies' risk management activities to be better reflected in their financial statements. The amendments relate to the scope of potential underlying transactions and hedging transactions and to the rules on the efficacy of hedging relationships.

The hedging transactions currently designated by Hermle as effective hedging relationships also fulfill the criteria in IFRS 9 for statement as hedging transactions. As the general principles for stating effective hedging relationships are not changed by IFRS 9, application of the new rules will have no material effects on the consolidated financial statements.

Re IFRS 15: Hermle will apply IFRS 15, "Revenue from contracts with customers" for the first time in the 2018 business year. The Group intends to apply the modified retrospective method. IFRS 15 replaces the existing guidelines for the recognition of sales revenue, including IAS 18 "'Revenue', IAS 11 'Construction contracts', and IFRIC 13 'Customer Loyalty Programs'. The new standard now sets out a five-stage model for disclosing revenue, as follows: Step 1. 'Identify the contract(s)', 2. 'Identify the performance obligations in the contract', 3. 'Determine the transaction price', 4. 'Allocate the transaction price to the performance obligations in the contract' and 5. 'Recognize revenue when (or as) the entity satisfies a performance obligation'. The model is, in principle, to be used for all customer contracts.

Differences from the current statement of sales revenues may occur based on the fact that, according to the new delimitation rules, differing performance obligations arise from a contract with a customer, the remuneration for the entire transaction must be allocated to those identified performance obligations, and the performance obligations are realized at different points in time. So there might be differences in the timing of sales revenue realization.

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Group Notes to the Financial Statements

The Hermle Group's activities primarily entail the sale of goods, in particular machine tools, parts and accessories. It also provides related services, such as repairs, servicing and maintenance, and training.

Contracts with customers for the sale of goods include few ancillary services which can be classified as separate performance obligations according to the principles of IFRS 15. As such, sale contracts mostly comprise a uniform performance obligation with a single time of realization of the revenue. In these cases, the revenue is realized when power of disposition of the asset is transferred to the customer. If additional performance obligations are identifiable, they are of subordinate importance, are fulfilled at a specific point in time, and are closely linked to the other performance obligations in terms of timing. To that extent, there are no material variations from the previous realization of revenues according to IAS 18.

Country-specific statutory warranties exist in relation to the sale contracts which, following application of IFRS 15, will be taken into account through the creation of provisions as previously according to IAS 37. Hermle also offers extended warranties which must be classed as separate performance obligations, and to which a separate price can be allocated. The revenue is only realized when a claim is made under the warranty, or at the end of the warranty period. According to IFRS 15, this revenue component would be realized later than is currently the case.

Revenues relating to services have to date been recorded when the service was rendered. Hermle assumes that, according to IFRS 15, revenues from most service contracts will be realized by reference to a specific point in time on rendering of the services concerned. In the case of contracts entailing a range of different performance obligations, the allocation will be based on their respective separate prices, as the services are also offered in separate transactions. The separate prices then also correspond to the respective fair values of the service components. The volume of sales revenues which are generated in relation to a specific period over a protracted time and which would result in a major shift in sales revenues to subsequent periods is considered to be of subordinate importance.

Based on estimates to date, additional new or clarifying aspects of IFRS 15, such as the amended rules for the treatment of contract costs and financing components will fundamentally not have any material effects on the realization of revenues.

Apart from the duties of recognition, disclosure and explanation, it is assumed that the implementation of IFRS 15 will have no material effects on Hermle's consolidated financial statements.

Re IFRS 16: The Hermle Group will not be applying the new IFRS 16, "Leases" until the 2019 business year.
The standard stipulates that both finance and operating leases must be recognized on the balance sheet.

According to the unified model for the recognition of leases of more than minor value with terms of more than 12 months, the lessee's balance sheet must recognize a leasing liability in the amount of the present value of the future leasing payments and an asset in the same amount reflecting its right to use the leased item. Whereas the leasing liability will progress according to the effective interest rate method, the right of use will be written down over the term of the lease.

The new standard means that rentals and leases not previously stated on the balance sheet will in future have to be recognized in a comparable way to the current balance sheet recognition of finance leases. At December 31, 2017, future non-discounted minimum lease payments from existing property, vehicle and other rental and hire agreements total €k 602 (see item 29). An increase in the balance sheet total by this non-discounted amount would reduce the equity ratio only marginally. In view of the low volume of rentals and leasing, the EBITDA will increase only by a small amount. Consequently, the effects of IFRS 16 are not material to the Hermle Group.

It is not expected that the other standards will have any material effects on the consolidated financial statements.

Furthermore, the following new or amended standards and interpretations exist which were issued by IASB, but have yet to be recognized by the European Union. These standards and interpretations have not been applied in advance:

IFRS 14:	Regulatory adjusting items
IFRS 17:	Insurance contracts
IFRS 10, IAS 28:	Sales or contributions of assets between an investor and its associate/joint venture (amendments)
IAS 28:	Long-term investments in associates and joint ventures (amendments)
IFRIC 22:	Foreign currency transactions and advance consideration
IFRIC 23:	Uncertainty regarding treatment for income tax purposes
IFRS 2015-2017:	IFRS 3, IFRS 11, IAS 12 and IAS 23 (amendments)

It is to be expected that these standards will have significant effects on the consolidated financial statement.

(3) Group of consolidated companies

All subsidiaries and joint ventures of Maschinenfabrik Berthold Hermle AG are incorporated in the consolidated financial statement. Subsidiaries are companies that are directly controlled by Maschinenfabrik Berthold Hermle AG and are consolidated in full. Joint ventures are companies that are managed jointly with other companies and which are incorporated in the consolidated financial statement using the at equity method. The analysis as to whether or not a subsidiary or a joint venture applies is conducted in that respect on the basis of the corporate governance structures and additional contracts that may apply.

company	Type of Consolidation	Equity holding
Segment Germany		
Hermle + Partner Vertriebs GmbH, Gosheim	full	100.0 %
Hermle-Leibinger Systemtechnik GmbH, Gosheim	Equity method	49.0 %
Hermle Maschinenbau GmbH, Gosheim	full	100.0 %

company	Type of Consolidation	Equity holding
Foreign Sales Segment		
Hermle (Schweiz) AG, Neuhausen, Switzerland	full	100.0 %
Hermle WWE AG, Neuhausen, Switzerland	full	99.8 %
Hermle Vostok OOO, Moscow, Russia	full	99.8 %
Hermle Nederland B.V., Blerick, Netherlands	full	100,0 %
Hermle Italia S.r.l., Rodano, Italy	full	100.0 %
Hermle Machine Co. LLC, Franklin Wisconsin, USA	full	100.0 %
Hermle Uljanovsk OOO, Uljanovsk, Russia	full	100.0 %

The group of consolidated companies is the same as for the previous year.

(4) Consolidation principles

The capital consolidation applies pursuant to IFRS 3 (Business Combinations) using the purchase method. Accordingly, the acquisition costs of the purchased shares are offset at the proportionate market value of the purchased assets and debts of the subsidiary at the time of acquisition. A resulting positive difference is capitalized as derivative goodwill, a resulting negative difference is immediately liquidated affecting the current result. Resulting goodwill normally undergoes an impairment test at least annually.

Jointly managed companies are stated in the balance sheet pursuant to IFRS 11 according to the equity method. On each reporting date the Group reviews whether or not there are indications of the need to take into consideration impairment expenses regarding the investment in jointly managed companies.

Interim results between the fully consolidated companies are eliminated where significant. Expenses and income as well as receivables and liabilities between Group companies are offset.

Interim results between the Group and companies incorporated using the equity method are eliminated on a proportionate basis where significant.

A compensating item for interests of other shareholders has been created in the sum of their share of the equity for the interests of non-Group shareholders in the Group companies. In addition to third party holdings in capital and provisions, this amount includes the pro rata balance sheet profit.

(5) Currency conversion

The annual financial statements of consolidated companies prepared in foreign currencies were converted on the basis of the concept of the functional currency using the modified reporting date price method. In view of the fact that all companies incorporated in the consolidated financial statement operate their business transactions independently in terms of finances, management and organization, as a general rule the functional currency is identical to the respective national currency of the company. Therefore, the assets and debts are converted in the consolidated financial statements at the reporting date rate, equity items at historical rates, and expenses and income at the annual average rate. Conversion differences resulting from converting the statement are recorded in equity without an effect on the operating result up until the subsidiary leaves the Group.

As a general rule, monetary items in foreign currencies are converted in the statements of the individual Group companies at the reporting date rate. Currency gains or losses as a result are directly recorded as having an effect on the operating result. As a general rule, currency conversion differences from the conversion of balance sheet items of foreign operating facilities are recorded with an effect on the operating result.

The following exchange rates were used for converting the key foreign currency contracts:

	Reporting date rates 12.31.2017	Reporting date rates 12.31.2016	Average rates 2017	Average rates 2016
USD	1.1993	1.0541	1.1766	1.1032
CHF	1.1702	1.0739	1.1163	1.0909

(6) Accounting and valuation principles

ASSET ITEMS

Intangible assets and property, plant and equipment

Patents, software, licenses and similar rights are stated pursuant to IAS 38 less scheduled depreciation.

Even the company's own intangible assets that are highly likely to provide future benefit for the company, and the cost of which can be reliable determined, are capitalized in the manufacturing costs. In that respect the manufacturing costs record all costs that are directly attributable to the manufacturing process and reasonable parts of the associated overheads. Financing costs are not capitalized. As a general rule, research and development expenses that are not eligible for capitalization are treated as ongoing costs when they arise. The development cost of new or significantly improved products are capitalized provided the technical implementation capability and the marketing eligibility and intent are secured. Proof of the stated criteria is furnished via the technical trials of the new products at the company and the successful presentation to trial customers. Capitalized developments are depreciated using the straight-line method for an expected product life cycle of three to four years, and reviewed annually via an impairment test, and commence with the public presentation.

The property, plant and equipment item is stated on the basis of the acquisition and manufacturing costs less scheduled depreciation in line with the customary company life cycle. Scheduled depreciation applies in line with the expected consumption of the future use. The company-produced assets were stated in the balance sheet with the directly attributable costs plus pro rata overheads. Repair and maintenance costs as well as financing expenses are recorded as current expenses.

The scheduled depreciation is based on the following standardized Group useful life periods:

Commercial proprietary rights and similar rights	3 to 5 years
Development costs	3 to 4 years
Buildings	12 to 50 years
Technical equipment and fixtures	3 to 14 years
Other fixtures, fittings, tools and equipment	3 to 14 years

There are no assets with an uncertain useful life.

Impairment tests

The soundness of the fixed assets is regularly reviewed on the reporting date. Non-scheduled depreciation is applied if a likely permanent drop in value is given as a result of changed circumstances. The soundness is determined by way of a comparison of the book value of the respective asset with the achievable amount. The achievable amount corresponds with the higher value form the use or the sale of the affected asset. Non-scheduled depreciation is applied insofar as this has fallen below the book value. If the market value increases for an asset that had to date been depreciated on a non-scheduled basis, an increased valuation is applicable.

Non-current financial assets

The financial assets are largely made up of shares in companies valued using the at-equity method as well as other financial assets in the form of fixed-term deposits with terms of more than one year that are stated at amortized cost as loans and receivables issued by the company.

Other non-current assets

The other non-current assets largely contain unsecured claims that are stated as loans and receivables issued by the company with the continued acquisition costs. Value reductions within the meaning of IAS 39 are applied with an effect on the operating result as soon as objective indications arise in that respect.

Inventories

As a general rule, raw materials and merchandise are stated at average acquisition cost or the lower net sale value. Unfinished and finished goods are stated at manufacturing costs or the lower net sale value. In addition to the directly attributable costs, manufacturing costs contain the reasonable and necessary production and material overheads as well as applicable administrative costs eligible for capitalization based on normal utilization. Finished products are stated at standard costs. Adequate depreciation is applied to the lower net sale value for stocks warehoused for lengthy periods and in the case of diminished marketability or loss-free valuation. This becomes inapplicable once the reasons for depreciation no longer apply. Interest on borrowings is not taken into account.

Accounts receivable from trading and other short-term receivables

The accounts receivable from trading and other short-term receivables are stated in the balance sheet at the continued acquisition costs or the lower fair value. Potential and identifiable defaults in the case of individual receivables are taken into account by way of appropriate allowances for losses on individual bank loan accounts. In the case of all other receivables, flat-rate impairment is applied based on the duration of the average receipt of payment, the current business environment and past experience. Non-interest bearing or low-interest bearing receivables and assets with terms in excess of one year are stated at the cash value.

Financial instruments

Financial instruments are contracts that in the case of a company lead to a financial assets and in the case of the contracting party a financial obligation or an equity capital instrument. Pursuant to IAS 39, financial instruments are allocated to the following categories upon receipt:

Loans and receivables

Financial assets

- financial assets held up until final maturity
- financial assets held for commercial purposes
- financial assets available for sale

Financial liabilities that are stated at continued acquisition cost

Financial liabilities stated at the fair value with an effect on the operating result

Original financial instruments

As a general rule, financial assets that are not held for commercial purposes are stated at the continued acquisition cost less the value reductions (Loans and receivables). Value adjustments on receivables, in particular in the case of accounts receivable from trading, are created depending on the likelihood of complete or partial realizability. The value adjustments are, to a considerable extent, based on assessments and valuations of individual receivables which, in addition to the default in payment and creditworthiness of the respective customer, are based on cyclical developments and assessments of the further development. Receivables are ultimately written off as soon as they are no longer recoverable.

Financial assets held up until final maturity are stated at the continued acquisition cost. These financial instruments only apply at the Hermle Group at present in individual cases, and are not of great importance.

Financial assets held for commercial purposes are stated at the fair value. A fair value is the amount that can be achieved in business transactions between independent contracting parties under current market conditions.

Financial assets available for sale are stated in the balance sheet at the fair value. This category includes, above all, securities. Changes to the fair value are recorded in the cumulated other equity with consideration given to deferred taxes without an effect on the profits. If the fair value is permanently or significantly below the book value, the depreciation is recorded with an effect on profits. Furthermore, the fair value changes at the time of sale are recorded with an effect on the operating result.

Financial liabilities that are stated at continued acquisition cost are largely made up of trade accounts payable. Accordingly, the amount stated on the reporting date are stated at nominal value including turnover tax or at the higher fair value.

Financial liabilities that are stated with an effect on the operating result at the applicable current value currently only apply at the Hermle Group in individual cases, and therefore are not hugely significant.

IAS 39 only permits, in narrowly defined exceptional cases, reclassification between certain categories of financial instruments. Financial instruments were not reclassified, as was the case in the previous year.

In the event that the reasons for the previously applied non-scheduled depreciation no longer apply, corresponding write-ups are applied up to the amount of the original acquisition costs.

Derivative financial instruments

Hermle uses derivative financial instruments to safeguard existing or planned basic operating transactions and appertaining risks. At present, forward exchange transactions are largely used to safeguard foreign currency risks. Derivative financial instruments and forward exchange transactions are initially recognized by Hermle AG at the fair value. The market values are also relevant to the follow-up valuation. Derivative financial instruments with a positive fair value are stated in the other receivables, while those with a negative fair value are stated in the other liabilities. As part of the hedge accounting, value changes of fair value hedges used to safeguard value fluctuations of balance sheet items are, as in the case of value fluctuations of basic transactions stated in the balance sheet, recorded with an effect on profits in the income statement. Value changes of cash flow hedges are offset against the cumulated other equity by way of eliminating the ineffective part and with consideration given to deferred taxes without affecting the profit provided the hedge accounting requirements are given within the meaning of IAS 39.

LIABILITY ITEMS

Provisions and liabilities

The tax provisions and other provision take into account all legal and factual obligations and risks involving third parties that are identifiable on the reporting date that are based on past business transactions or past events and which in the future are likely to lead to an outflow of resources, and can be reliably assessed. They are created in the sum of their likely performance amount, and are not offset against potential recourse claims. Long-term provisions are stated in the balance sheet at the discounted performance amount on the reporting date provided the interest effect created from the discounting is significant.

As a general rule, financial liabilities are enter on the liabilities side at the repayment amount.

Deferred taxes

Deferred taxes are stated for all temporary differences between the amounts stated in the IFRS balance sheet and the tax balance sheet of the individual companies and for consolidation measures that have an effect on profits. Furthermore, deferred tax assets for tax reductions claims based on tax losses carried forward are also stated in the balance sheet provided the future realizability is adequately safeguarded. The tax rates used to calculate the deferred taxes are in each case the tax rates valid or expected at the realization time.

INCOME STATEMENT

Income and expenses

Sales are booked at the time at which the products are goods are delivered or the services have been rendered and the risk has passed to the customer. Trade discounts and price reductions reduce the sales revenues.

Operating expenses are recorded upon the delivery or utilization of the service. We create provisions for guarantees provided at the time at which the products are sold. Interest and similar income and expenses are recorded in line with the respective period.

EXPLANATORY NOTES ON THE BALANCE SHEET

(7) Assets

The development and apportionment of the fixed assets is set out in the statement of asset additions and disposals.

The capitalized development costs from the development of new tool machine products are stated in the intangible assets. At the end of the business year, the net amount was €k 546 (previous year: €k 178). The research and development expenses recorded directly as expenses were €k 12,677 (previous year €k 11,991).

An overview of the interests held by Maschinenfabrik Berthold Hermle AG is stated in (3).

Hermle Maschinenbau GmbH aims to develop a production-safe new procedure for the additive manufacture of complex metallic bodies. The company holds various patents in that respect.

In the capacity of a joint venture company, Hermle-Leibinger Systemtechnik GmbH renders on behalf of Maschinenfabrik Berthold Hermle AG services in conjunction with projecting and supplementing the Hermle standard machines to adjust specific customer elements such as the incorporation in production systems and appertaining correlate devices or programs in line with specific production parts.

Summarized information for joint companies that are insignificant individually:

	2017 €k	2016 €k
Share in profits from continued activities	428	331
Share in profits from discontinued activities	0	0
Share in other profit	0	0
Share in total profit	428	331
Aggregated book value as per 12.31.	1,073	1,012

In the year under review, the depreciation or value increase on the long-term financial assets was € 0 (previous year: € 0).

(8) Other non-current assets

The item very largely comprises profit participation from life insurance policies. In the previous year it also included tax refund claims arising from EK 40.

(9) Inventories

The inventories are classified as follows:

	12.31.2017 €k	12.31.2016 €k
Raw materials, supplies and consumables	26,121	22,888
Work in progress	18,300	16,926
Finished goods and merchandise	15,879	13,100
Advance payments on inventories	1,783	633
	62,083	53,547

The book value of the inventories stated at net sales prices was €k 9,181 (previous year €k 9,438). The increase in the value adjustment for inventories recorded with an effect on profits was €k 510 (previous year: €k 28). Advances paid are stated as net amounts without turnover tax.

(10) Accounts receivable from trading and other short-term receivables

	12.31.2017 €k	12.31.2016 €k
Accounts receivable from trading		
due from third parties	61,033	58,563
due from other Group companies	129	77
	61,162	58,640
Other short-term receivables		
Derivative financial instruments	730	13
Tax refund claims	2,841	1,819
Deferred charged and prepaid expenses	818	802
Remaining other assets	1,015	1,496
	5,404	4,130
Total	66,566	62,770

The accounts receivable from trading and other short-term receivables with a residual term of more than one year was €k 1,468 (previous year: €k 880). The other receivables and other assets all had remaining terms of less than one year.

Pursuant to IAS 39, the derivative financial instruments stated in the other short-term receivables are stated at fair value. They apply both to the so-called effective and ineffective part of the positive market values of currency hedge transactions as part of the statement presentation of hedging relationships pursuant to IAS 39. Insofar as they are intended for fair value hedge security purposes, the positive market values are juxtaposed with depreciation in the balance sheet items of the allocated basic transactions.

Furthermore, the remaining other assets contain as primary items short-term receivables due from suppliers from returns as well as short-term receivables due from employees.

The composition of the non-value adjusted accounts receivable from trading classified according to overdue dates is stated below:

	Book value Total	of which: neither impaired nor overdue	of which: not value adjusted and overdue in the following time bands			
			<3 Months	3-6 Months	6-12 Months	>12 Months
	€k	€k	€k	€k	€k	€k
Trade receivables 12.31.2017	61,162	38,322	6,149	0	0	0
Trade receivables 12.31.2016	58,640	28,013	6,010	1	0	0

With regard to the neither impaired nor in default or overdue amount of accounts receivable from trading, on the reporting date there are no indications of the debtors being unable to honor their payment obligations.

The following table illustrates the change in the impairment on the amount of accounts receivable from trading and other short-term receivables:

	2017 €k	2016 €k
Impairment at the start of the business year	6,064	6,130
Amount stated in income statement in the period under review	-100	66
Writing off receivables	-191	-179
Currency conversion effects	214	47
Impairment at the end of the business year	5,987	6,064

The following table illustrates the expenses for the complete writing off of accounts receivable from trading as well as income from the receipt of written-off accounts receivable from trading:

	2017 €k	2016 €k
Expenses for the complete charge off of receivables	474	225
Income from the receipt of charged off receivables	9	16

(11) Securities and other assets

In the year under review, bonds, commercial papers as well as fixed-term deposit investments with a term of more than three months in the sum of €k 22,118 (previous year: €k 10,610) are stated in this item.

(12) Cash and cash equivalent

The cash and cash equivalents largely apply to cash in banks.

	12.31.2017 €k	12.31.2016 €k
Cash in banks	103,353	120,974
Cash on hand	37	18
	103,390	120,992

(13) Equity

The share capital is unchanged compared with the previous year and is divided into 4,000,000 ordinary shares and 1,000,000 non-voting preference shares. The preference shares have a surplus dividend of € 0.05. The arithmetical nominal value of the shares is € 3.00 for each share.

The capital reserve contains allocations from the sale of treasury shares acquired in previous business years via the stock exchange.

During the business year, an amount of €k 6,000 was withdrawn from the revenue reserves of Maschinenfabrik Berthold Hermle AG in order to increase the balance sheet profit.

The annual general meeting is recommended to pay out the amount of €k 75,362 from the 2017 balance sheet profit of Maschinenfabrik Berthold Hermle AG amounting to €k 75,050 through the payment of a dividend totaling € 15.00 per ordinary share and € 15.05 per preference share, and to carry forward the remaining €k 312 to new account.

In the 2017 business year a dividend totaling € 12.80 per ordinary share and € 12.85 per preference share was paid in respect of the 2016 business year.

The differences resulting from the currency conversion contain the differences resulting from the conversion of foreign subsidiaries.

The cumulated other equity contains the effects from the evaluation of financial instruments without affecting the operating result.
In the 2017 business year income (previous year: expenses) from the market valuation of derivative financial instruments attributable to cash flow hedges were allocated to the equity without affecting profits in the sum of €k 500 (previous year: €k 410). In addition, an amount of €k 330 (previous year €k 237) was withdrawn from the equity and recorded as expenses (previous year: expenses) in the period result.

The development of equity and its elements is stated in the equity statement.

(14) Minority interests

The remaining item is attributable to the share in equity of Hermle WWE AG attributable to the other shareholders.

(15) Provisions

	At 01.01.2017 €k	Consumption €k	Resolution €k	Allocation €k	Other changes €k	At 12.31.2017 €k
Tax provisions	2,842	1,590	83	3,322	-27	4,464
Personnel provisions	14,340	13,070	144	14,930	-45	16,011
Other provisions						
in marketing and sales	23,405	12,939	1,705	15,179	-291	23,649
For other areas	1,048	774	91	795	-9	969
	24,453	13,713	1,796	15,974	-300	24,618
	41,635	28,373	2,023	34,226	-372	45,093
of which short-term provisions	40,284	28,080	2,002	33,759	-391	43,570
of which long-term provisions	1,351	293	21	467	19	1,523

The provisions in the personnel area largely apply to holiday and flexitime provisions, provisions for partial retirement commitments as well as bonus payments. The marketing and purchasing risks apply to warranties, fairness in trade and other follow-up benefits, acceptance or buy-back obligations and a raft of other purchasing and marketing risks. The other area contains other outstanding services and liabilities, which have not been identified on merit and/or in terms of their ultimate amount.

As in the previous year, the long-term provisions are personnel-related provisions, in particular relating to long-service award payments and flexitime commitments.

The other changes comprised currency and interest effects totaling €k -372 (previous year €k +91). The effects from the adding of interest and from changes to the discounting interest rate in the sum of €k 36 (previous year: €k 39) apply in an amount of €k 19 (previous year: €k 19) to personnel provisions and €k 16 (previous year: €k 20) to other provisions.

(16) **Liabilities**

The liabilities relate in particular to:

	12.31.2017 €k	12.31.2016 €k
Other non-current liabilities		
Derivative financial instruments > 1 year	0	65
Short-term trade accounts payable		
to third parties	10,690	7,625
to other Group companies in which interests are held	728	841
	11,418	8,466
Other current liabilities		
Received advance payments	23,062	15,678
Derivative financial instruments	122	632
Liabilities from taxes	5,817	7,197
Liabilities for social security	254	308
Other liabilities	6,065	4,423
Deferred charges	914	1,079
	36,234	29,317
Classification of liabilities according to residual terms		
to 1 year	47,652	37,783
1 to 5 years	0	65
more than 5 years	0	0
	47,652	37,848

The short-term trade accounts payable contain title reservations that are customary in the trade.

Pursuant to IAS 39, the derivative financial instruments stated in the other liabilities are stated at fair value. They apply both to the so-called effective and ineffective part of the negative market values of currency hedge transactions as part of the statement presentation of hedging relationships pursuant to IAS 39. Insofar as they are intended for fair value hedge security purposes, the negative market values are juxtaposed with value increases in the balance sheet items of the allocated basic transactions.

The advances paid are stated as net amounts without turnover tax.

EXPLANATIONS ON THE INCOME STATEMENT

(17) Sales

The sales proceeds are broken down by region as follows:

	2017 €k	2016 €k
Federal Republic of Germany	168,211	160,242
Other countries	233,798	233,708
	402,009	393,950

(18) Other operating income

The other operating income item applies to:

	2017 €k	2016 €k
Income from the liquidation of provisions	1,950	2.692
Income from the liquidation of value adjustments	3,007	3,775
Income from investment disposals	524	291
Currency gains form price differences and financial instruments	1,268	0
Remaining other operating income	2,100	2,674
	8,849	9,432

The remaining other operating income item contains as key elements income from letting and leasing, from the passing on of costs and compensation payments of insurers and other third parties.

(19) Cost of materials

Costs of materials apply to:

	2017 €k	2016 €k
Expenses for raw materials and supplies and procured goods	166,029	157,126
Cost of purchased services	14,320	13,801
	180,349	170,927

(20) Personnel expenses

Personnel costs include:

	2017 €k	2016 €k
Wages and salaries	74,614	68,818
Social security, pension and other benefit costs	12,390	11,479
	87,004	80,297

As in the previous year, there were no expenses for old-age pensions.

Average numbers of employees:

	2017	2016
Production employees	348	321
White-collar workers	616	596
Trainees	89	92
	1,053	1,009

In line with the resolution adopted at the shareholders' meeting on July 6, 2016, the emoluments of the Management Board are not stated individually but rather for the entire Management Board. The board members' emoluments totaled €k 2,776. Of that total, €k 693 was attributable to basic salaries including passenger car use and direct insurance policies. In addition, the item contained performance-related elements of €k 2,083. The Supervisory Board members' emoluments totaled €k 80.

(21) Depreciation

The depreciation largely applies to scheduled depreciation on intangible assets and property, plant and equipment. Non-scheduled depreciation of €k 54 (previous year: € 0) was applied in the business year.

(22) Other operating expenses

	2017 €k	2016 €k
Creation of value adjustments for receivables	3,138	3,640
Currency losses	0	303
Remaining other operating expenses	39,228	41,684
	42,366	45,627

The other operating expenses largely apply to expenditure for marketing, service and administration, rent and leasing installments as well as for maintenance expenses for buildings, fixtures and fittings. In addition, the item contains so-called taxes chargeable as expenses for road tax and land tax as well as foreign representative offices.

With regard to auditing the annual financial statement and consolidated financial statement of Maschinenfabrik Berthold Hermle AG, in 2017 auditor's fees of €k 170 (previous year €k 161) were recorded as expenses. In the 2017 business year, € 0 (previous year: € 0) were charged for tax consultancy services and €k 0 (previous year €k 5) for other services.

(23) Result from companies valued using the at equity method

The result from companies valued using the at equity method of €k 428 (previous year €k 331) applied to the proportionate profits from the holdings in Hermle-Leibinger Systemtechnik GmbH.

(24) Other financial result

The other financial result is classified as follows:

	2017 €k	2016 €k
Other interest and similar income	308	331
Depreciation of securities and other assets	-176	0
Interest and similar expenses	-140	-151
	-8	180

The depreciation of securities and other assets concerns the timing-dependent interest rate-related depreciation of fixed-interest securities acquired above nominal value.

The interest expenditure comprises external interest and the internal interest charge on current and non-current provisions, as well as interest portions from the difference between the spot and forward rates of currency hedging transactions. Such differences from spot and forward rates of currency hedging transactions are also included in the interest revenue.

(25) Taxes on income and earnings

The taxes on income and earnings apply to:

	2017 €k	2016 €k
Ongoing taxes	25,868	26,749
Deferred taxes	211	-286
	26,079	26,463

The following table illustrates the transition from the calculated or expected to the actual income tax liability, and explains the key differences in a summary:

	2017 €k	2016 €k
Result before income tax	99,405	100,312
Arithmetical income tax in %	26.50 %	26.50 %
Calculated income tax	26,342	26,583
Tax-free income	0	0
Non-deductible expenses	+64	+46
Other non-recurrent taxes	-121	-104
Amendment of tax rates	+197	+26
Differences from tax rates and currency conversion	-364	-65
Losses carried forward not taken into account	-39	-23
Total tax liability	26,079	26,463

The calculated income tax was calculated for domestic companies based on a tax rate of 26.50 % (previous year 26,50 %), while the deferred taxes were created on the basis of a tax rate of 26.50 % (previous year 26.50 %). The tax rate contains trade tax, corporation tax and the solidarity surcharge.

The stated deferred tax assets and liabilities apply to the following balance sheet items:

	12.31.2017 €k	12.31.2016 €k
Deferred tax assets		
Tax losses carried forward	0	0
Consolidation	415	446
Fixed assets	140	147
Inventories and receivables	880	912
Provisions	444	465
Liabilities	0	0
Derivative financial instruments	32	185
Other	0	0
Total	1,911	2,155
Offset against deferred tax liabilities	0	0
Total	1,911	2,155
of which items charged to equity without affecting the operating result	0	100
Deferred tax liabilities		
Fixed assets	159	62
Inventories and receivables	68	49
Securities	0	0
Provisions	11	25
Derivative financial instruments	193	4
Other	0	0
Total	431	140
Offset against deferred tax assets	0	0
Total	431	140
of which items charged to equity without affecting the operating result	120	0

The deferred tax assets are stated in the balance sheet in the non-current assets item, while the deferred tax liabilities are stated in the long-term liabilities item.

Tax losses capable of being carried forward of €k 536 (previous year €k 684) have not been stated due to the uncertain realization options. Due to changes to the corporation taxation law in 2006, corporation tax credits that have yet to be utilized from EK 40 are capitalized at a cash value of € 0 (previous year: €k 251).

(26) Result for each share

	2017 €k	2016 €k
Net income:		
According to income statement	73,326	73,849
Minority interests in result	-2	-4
Result after minority interests	73,324	73,845
Expired dividend preferences	-50	-50
Result after minorities and preference dividends	73,274	73,795
Weighted average:		
Outstanding ordinary shares	4,000,000	4,000,000
Outstanding preference shares	1,000,000	1,000,000
Total of all share types	5,000,000	5,000,000
Average weighted number of shares in items:	5,000,000	5,000,000
Undiluted result for each share in euros:		
For each ordinary share	14.65	14.76
For each preference share including dividend preference	14.70	14.81

On a cumulated basis the company holds 0 (previous year: 0) own preference shares. In other respects, too, no further changes to the equity instruments occurred. The preference shares contain a surplus dividend of € 0.05 for each share compared with the ordinary shares. This additional share in the profit is initially shortened on a standardized basis in the case of calculating the result for each share, and only added once again in the case of the result for each preference share.

(27) Cash flow statement

The development of the money flows and their effects on the funds of the cash equivalents are illustrated in the cash flow statement. In that respect a distinction is made between payment flows from the ongoing business activity and the investment and financing activity. The cash flow from the ongoing business activity is determined using the indirect method, while by contrast the cash flow from the investment and financing activity is determined on a payment-related basis. Effects from the currency conversion and amendments to the group of consolidated companies are adjusted in that respect.

The cash and cash equivalents from cash in hand and cash in banks explained in (12) make up the funds of the cash and cash equivalents.

Tax payments as well as interest payments are stated in full as fund outflows or fund inflows from the business activity. The cash flow from the ongoing business activity contained cash flows from interest and other financial income amounting to €k 316 (previous year €k 272) and cash flows from taxes of €k -26,325 (previous year €k -30,369).

(28) Segment reporting

For table see page 47

With regard to the segment reporting, Hermle follows IFRS 8 "Operating Segments", which on a mandatory basis promotes classification in segments in line with the "Management Approach". By way of this method, information is published on the operating segments based on the internal organizational and management structure. In this respect the financial reporting to the primary management committee of the company is authoritative, which is represented at Hermle by the Management Board.

In view of this, this segment reporting is geared towards the segmenting in line with the marketing activities. On the one hand, the segments are divided into homogeneous activities of the foreign marketing companies and marketing branches, which cover the function of authorized dealers and marketing branches, and on the other in the remaining domestic companies that each report their results on an ongoing basis. The companies and branches are classified in segments according to their affiliation. The following companies are allocated to the foreign marketing segment: Hermle Machine Company LLC, Hermle Nederland BV, Hermle Italia S.r.l., Hermle (Schweiz) AG, Hermle WWE AG (Schweiz), Hermle Vostok OOO (Russia) and Hermle Uljanovsk OOO (Russia) as well as the marketing branches of Hermle AG in Austria, the Czech Republic, Denmark and Poland.

In that respect, sales and services between the segments are offset using conditions that are customary in the market. Hermle measures the success of the segments primarily by way of the operating result.

Receivables and liabilities, provisions, income and expenses between the segments are eliminated in the column consolidation effects. In addition, in the column consolidation effects the items are also stated that cannot be allocated to the stated segments. As a general rule, the segment reporting is based on the same accounting and valuation methods that apply to the consolidated financial statement. As a general rule, the assets of the segments comprise all assets, whereby the segment-wide relations are stated in the column consolidations. However, apart from the assets, all shares, interests and loans to companies that are incorporated in full or in part in the consolidated financial statement are in the long-term financial assets area.

As a result of Hermle's customer structure and business structure, there was no significant concentration on individual customers or regions in the reporting years.

(29) Contingent liabilities and other financial obligations

The following contingent liabilities and other financial commitments applied on the reporting date:

	12.31.2017 €k	12.31.2016 €k
Contingent liabilities		
Liability from shares in cooperative societies	5	5
Other financial commitments:		
obligations from operating rental and leasing contracts		
due up to 1 year	334	495
due up to 5 years	268	471
due after 5 years	0	0

(30) Financial instruments

Original financial instruments

The following section contains additional, key explanations on the statement presentation of financial instruments and their effects on profits in the income statement within the meaning of IFRS 7. The following overviews illustrate the composition of the financial instruments according to balance sheet items and valuation categories, the fair value and the valuation results according to valuation categories.

The amounts stated for the financial instruments according to valuation categories are as follows:

	Book value 12.31.2017 €k	Values stated in the balance sheet pursuant to IAS 39 Updated acquisition costs €k	 Fair Value affecting profits €k	 Fair Value neutral effect on profits €k	Fair Value 12.31.2017 €k
Assets					
Non-current assets					
Other financial assets	5,006	5,001		5	5,006
Other non-current assets	49	49			49
Current assets					
Accounts receivable from trading	61,162	61,162			61,162
Other current assets	875	875			875
Derivative assets	730		277	453	730
Securities and other assets	22,118	10,002	12,116		22,118
Cash and cash equivalents	103,390	103,390			103,390
Liabilities					
Non-current liabilities					
Financial liabilities	0				0
Derivative liabilities	0				0
Current liabilities					
Trade payables	11,418	11,418			11,418
Other liabilities	6,055	6,055			6,055
Derivative liabilities	122		122		122
Of which aggregated by valuation categories as per IAS 39					
Loans and receivables	180,479				
Financial assets available for sale	5				
Financial assets held for commercial purposes	12,846				
Financial liabilities valued at updated acquisition cost	17,473				
Financial liabilities affecting the operating result valued at fair value	122				

	Book value 12.31.2016 €k	Values stated in the balance sheet pursuant to IAS 39: Updated acquisition costs €k	Fair value affecting profits €k	Fair value neutral effect on profits €k	Fair value 12.31.2016 €k
Assets					
Non-current assets					
Other financial assets	5			5	5
Other non-current assets	61	61			61
Current assets					
Trade receivables	58,640	58,640			58,640
Other current assets	1,386	1,386			1,386
Derivative assets	13		13		13
Securities and other assets	10.610		10,610		10,610
Cash and cash equivalents	120,992	120,992			120,992
Liabilities					
Non-current liabilities					
Financial liabilities	0				0
Derivative liabilities	65		24	41	65
Current liabilities					
Trade payables	8,466	8,466			8,466
Other liabilities	4,489	4,489			4,489
Derivative liabilities	632		254	378	632
Of which aggregated by valuation categories as per IAS 39					
Loans and receivables	181,079				
Financial assets available for sale	5				
Financial assets held for commercial purposes	10,623				
Financial liabilitiesvalued at updated acquisition cost	12,955				
Financial liabilities affecting the operating result valued at fair value	96				

The net results of the financial instruments according to valuation categories are as follows:

	from interest/ dividends	from follow-up valuations: to fair value	currency conver-sion	value adjust-ment	from disposal	2017	2016
	€k	€k	€k	€k	€k	€k	€k
Loans and receivables	93		1,150	-131	-617	495	-1,204
Financial assets available for sale	0					0	0
Financial assets held for commercial purposes	221	-176				45	-32
Financial liabilities valued at updated acquisition cost	-103	-36				-139	-55
Financial liabilities valued at fair value							-96
Total	211	-212	1,150	-131	-617	401	-1,387

The net profits or losses from loans and receivables largely contain changes in the value adjustments, currency conversions, income from received payments and write-ups as well as interest income.

Determining the fair value of the financial instruments set out in the above tables is geared towards a fair value hierarchy that takes into account the significance of the input data used for the valuation, and is classified as follows:

Level 1: listed on active markets (unchanged assumed prices) for identical assets and liabilities;

Level 2: for the asset value or the liability either directly (as price) or indirectly (derived from the prices) observable input data that do not constitute a listed price according to Level 1;

Level 3: drawn input data that are not based on observable market data for valuing the asset and the liability (non-observable input data).

In the business year and in the previous year, the stated fair values were determined exclusively according to Level 2 of the fair value hierarchy.

Derivative financial instruments and hedging strategies

Financial risk management

As per December 31, 2017, the Hermle Group has an above-average equity ratio in the sum of 71.8 %. On the reporting date, the amount of liquid funds and securities was €k 130,509. The liquid funds and securities apply to debtors with a good credit rating or a credit rating guaranteed by way of ‘political guarantees’ or capital contributions by the German federal government, German federal states, or regional authorities. As a result of these circumstances, the Hermle Group is not dependent on interest-bearing outside capital to finance spare parts and expansion investments and the distribution of dividends. The Hermle Group gives consideration at all times to keeping adequate financial reserves available to react at short notice to potential changes in the economic situation.

Below the financial risks are assessed insofar as these are of importance to the Hermle Group.

Risks from interest changes

Risks from interest changes arise from the investment of liquid funds in the form of variable and fixed-interest investments. Additional interest risks do not apply because there is no interest-bearing outside capital. At the end of the year, the liquid funds were invested largely with residual terms of less than one year, in part even with terms of up to three months, and therefore were practically equated with variable interest rates.

With regard to the liquid funds and marketable securities (current) held up to the end of the year, an increase in the interest rates of 0.5% during the period of one year would lead to a potential increase in the net interest income of the following year by approximately € 0.3 million (previous year: € 0.7 million). The risk from deterioration of interest rates is increased because the ECB's policies mean that negative interest rates are also possible. We have to date been only marginally affected by negative interest rates, but in 2018 increased negative interest rates might be more widely passed on to bank customers to as much as 100 % (previous year: expectation of 100 %). However, the risk may be expected to be limited to the costs incurred through the alternative of 'cash withdrawal', i.e. deposit fees and insurance premiums, specifically to € -0.5 million (previous year: € -0.5 million).

Default risks

There is no significant concentration of default risks at the Hermle Group because no more than 10 % of the Group's sales are generated with any single end customer. Furthermore, the default risks are further reduced by way of the ongoing monitoring of the payment behavior of our customers, and consistent receivables management.

Liquid funds are invested in securities or lodged with debtors with good credit ratings or credit ratings maintained by way of 'political guarantees' or capital participation by the German federal government, German federal states, municipal institutions, such that based on the information currently available default risks are not to be expected, notwithstanding latent risks resulting from the capital markets. In addition, short investment periods are currently chosen. The for us highly significant indirect risk of default of totally over-indebted countries, if it were to occur, cannot be assessed by us with regard to the likelihood of occurrence. However, during the course of the last few years it has increased, and in the case of individual countries, in particular in the euro area, it is still to be classified as 'high' or 'very high'. By way of the so-called "Stability pact" and defined new borrowing ceilings, risk-limiting counter-measures have been introduced which, however, merely restrict new debt, and so have little effect in relation to cumulative debt levels. In the case of other countries, temporary exceptions were granted on successive occasions, so that a guarantee for future compliance with the rule is questionable. The maximum default risk arises from the book value of the financial assets stated in the balance sheet.

Liquidity risks

The Hermle Group have above-average high stocks of cash and cash equivalents. Current liquidity risks have not been identified in view of this, whereby the stability of the German banking system is deemed given (see comments on default risks).

Exchange rate risks

Exchange rate risks apply, in particular, where receivables and liabilities exist in a currency other than the functional currency of the respective company or will arise in the case of scheduled business development in the form of future payment flows. Hedging exchange rate risks refers to payment flows; foreign currency risks that do not lead to payment flows are not secured. These are, for example, risks from converting the contracts of foreign subsidiaries and operating facilities in the Group reporting currency euro.

The exchange rate risks of the Hermle Group largely refer to the amount of accounts receivable from trading in foreign currencies, derivative instruments as well as the inflow of cash and cash equivalents in foreign currencies. Derivative instruments are used to hedge these currency risks. These are aimed at securing the foreign currency receivables that exist on the reporting date, which are normally hedged as a general rule, beyond this additionally the hedging of cash flows that have yet to be recorded in the balance sheet on the reporting date or pending or anticipated cash flows. Hedges for expected cash flows only are secured depending on the assessment of the price situation within a window of up to twelve months, beyond this in exceptional cases.

With regard to the presentation of market risks, IFRS 7 specifies sensitivity analyses on the effects on hypothetical changes in relevant risk variants on the year-end result and equity. As per December 31, 2017 and December 31, 2016, all key accounts receivable from trading in foreign currency had been hedged by way of forward exchange transactions that were classified as fair value hedges. Currency items concluded from these result, in each case, in compensation effects such that changes do not, insofar, occur in equity and in the annual result. However, the valuation of the cash flow hedges as well as the conversion of foreign currency contracts are sensitive in relation to changes in currency rates.

In the case of depreciation of the key foreign currencies by 5 % in 2017, an income for the 2017 business year of € 0.3 million (previous year: income of € 0.4 million) would arise; in the case of a corresponding increase in value, a loss of € 0.4 million (previous year: € 0.5 million loss). In the case of depreciation of the key foreign currencies by 5 % in 2017, the Group capital as per December 31, 2017 would decrease by € 0.4 million (previous year: decrease of € 0.1 million); in the case of a corresponding write-up of the foreign currencies, it would increase by € 0.4 million (previous year: increase of € 0.2 million).

The nominal volumes taken as a basis for the derivative financial instruments as well as their market values on the reporting date are stated in the following table:

	12.31.2017 €k	12.31.2016 €k
Forward currency sales:		
Nominal volume	15,936	18,386
of which residual term > 1 year	0	1,423
Positive market values	730	13
of which Fair value hedges < 1 year	(271)	(1)
of which Fair Value Hedges > 1 year	(0)	(0)
of which cash flow hedges < 1 year	(459)	(12)
of which cash flow hedges > 1 year	(0)	(0)
Negative market values	122	697
of which Fair value hedges < 1 year	(43)	(250)
of which Fair value hedges < 1 year	(0)	(0)
of which Cash flow hedges < 1 year	(79)	(382)
of which Cash flow hedges < 1 year	(0)	(65)

The market value corresponds with the profits and losses in the case of a notional settlement of the derivatives on the reporting date. The maximum default risk of derivative financial instruments corresponds with the total positive market values. It applies to potential assets that may arise from the failure by individual trading partners to honor contractual obligations. Derivative financial instruments are only concluded with banks that have the stated creditworthiness to avoid such a risk.

As a general rule, changes in the market values are recorded with an effect on profits. If future planned cash flows in foreign currencies are the subject matter of an effective hedge within the meaning of IAS 39, the regulations of a cash flow hedge are applied. The market values of the corresponding hedge transactions are then initially offset against the equity, without affecting profits, in the "cumulated other equity" item, and only recorded with an effect on profits at a later date in the case of realizing the basic transaction.

(31) Estimates

Estimates are incorporated in the valuation of the accounts receivable from trading, inventories as well as determining the other provisions. In the case of the accounts receivable from trading stated in the balance sheet, these largely apply to the likelihood of default for the individual debtors, and in the case of the inventories warehoused for lengthy periods or inventories with a low likelihood of being marketed the future marketability, and in the case of the stated other reserves both the likelihood of occurrence of events and assumed performance amounts which, where possible, are determined on the basis of previous empirical values. In view of the fact that the actual future development of these parameters may vary from the forecast assumptions, new valuations of the corresponding items may arise in subsequent years with an effect on profits.

(32) Events after the reporting date

No events occurred after the reporting date having material effects on the earnings, financial and asset position of the Hermle Group.

With effect from January 1, 2018, Hermle AG acquired the remaining 51 % of shares in Hermle-Leibinger Systemtechnik GmbH from its former co-shareholders. As a result the company, which was previously included in the Group's financial statements on an at-equity basis, has been fully consolidated with effect from the 2018 business year. The full takeover will provide Hermle with greater flexibility in the key field of automation in future, and will further expand our portfolio of configurable automation solutions.

The purchase price was €k 6,245.

The fair value of the previously held minimum shares at the date of acquisition was €k 6,000. The necessary €k 4,927 adjustment of the carrying amount is included in the financial result affecting net income.

The final purchase price to be allocated had not yet been determined by the time the consolidated financial statements were approved for publication, so no disclosures can be made concerning the fair-value addition to net assets, in particular concerning any unstated intangible assets, or any goodwill arising from the transaction. It is expected that hidden reserves will have to be recognized in the intangible assets, and an additional goodwill value will have to be stated. The net asset at December 31, 2017 at carrying amounts totaled €k 2,420.

The fair value of the trade receivables is €k 728; the gross amount of the trade receivables is €k 728. None of the trade receivables was impaired, and the full contractually stipulated amounts are collectable.

(33) Relations with closely affiliated companies and persons

In addition to the subsidiaries incorporated in the consolidated financial statement as the holdings not incorporated in the consolidated financial statement, as a general rule consideration here is given to members of the Management Board or Supervisory Board as well as shareholders with a considerable influence within the meaning of IAS 24 "Related Party Disclosures". The relations with this group of closely affiliated companies and groups are processed at conditions that are customary in the market.

Closely affiliated companies that are dominated by the Hermle Group or upon which the Hermle Group exerts a considerable influence are stated in the holdings list (3).

The scope of the Hermle Group business relations with closely affiliated companies is as follows:

The deliveries and services performed and rendered by the Group for companies consolidated at equity was €k 330 (previous year €k 308), while the proportionate deliveries and services procured from companies consolidated using the at equity method were €k 9,670 (previous year €k 9,228). On the reporting date, the Group receivables due from companies consolidated using the at equity method were €k 129 (previous year €k 77), while the Group liabilities due to companies consolidated using the at equity method were €k 728 (previous year €k 841).

The deliveries and services performed and rendered by the Group for other closely affiliated companies were €k 119 (previous year €k 192), while the deliveries and services purchased by the Group from other closely affiliated companies were €k 2,825 (previous year €k 2,416). On the reporting date, the Group receivables due from other closely affiliated companies were €k 15 (previous year €k 2), while the Group liabilities due to other closely affiliated companies were €k 481 (previous year €k 285).

(34) Declaration pursuant to Section 161 AktG

The Management Board and Supervisory Board stated that apart from various individual points the recommendations of the government commission's German Corporate Governance Code have not been complied with. This is justified in that Maschinenfabrik Berthold Hermle AG conducts its operations in accordance with the principles of open information policy that it has put in place to date, which were implemented as part of the rules of procedure of the Management Board and the Supervisory Board. In that respect, the mandatory requirements were complied with in full.

The Management Board and Supervisory Board hold the view there are various reasons for not implementing recommendations of the Corporate Governance Code that extend beyond this. The recommendations set out in 2.3 have not been complied with because to ordinary shares of Hermle AG with voting rights are not listed on the stock exchange. The recommendations set out in 3. and 4 will not be complied with because the valid mandatory regulations combined with the rules of procedure are considered adequate by the Management Board and Supervisory Board. In addition, the "external experts" cited in the Code have not been incorporated. Furthermore, we believe that the Code regulations in 5. are geared towards international major DAX-listed Groups but not, however, to an SME with a limited number of ordinary shareholders who, in part, are represented personally in the supervisory committees. The recommendations set out in Item 6. will not be complied with either because the mandatory regulations are adequate. In addition, various topics are provided for here that are also irrelevant to Hermle because of the composition of the group of preference shareholders. The recommendations set out in Item 7. will not be complied with because similarly irrelevant fields such as share options are provided for but these are associated with cost reasons. Overall, in view of the relative lower market capitalization of the company, the shareholder structure, the very lean and therefore efficient company organization to date as well as the additional costs associated with full implementation, Hermle has decided in favor of a merely very limited realization of the DCGK.

However, in addition to all mandatory regulations, Hermle complies with various individual recommendations of the Code, which are stated below:

3.10.: Publication of the declaration of compliance on the website for 5 years

4.2.1.: Management Board made up of several persons

7.1.1.: Disclosures to shareholders and third parties

This statement is permanently available for the general public to view on the Hermle website at https://www.hermle.de/de/investor_relations/pflichtveroeffentlichungen/kodex_161_aktg.

(35) **Details of the company's executive bodies:**

The following persons form the Management Board

Günther Beck

Franz-Xaver Bernhard
Other memberships of supervisory boards and controlling bodies:
Member of the Supervisory Board of Vollmer Werke Maschinenfabrik GmbH, Biberach, Riss

Alfons Betting, to March 31, 2018

Benedikt Hermle, from January 1, 2018

The following persons form the Supervisory Board:

Dietmar Hermle, Chairman of the Supervisory Board
Entrepreneur, former Spokesperson of the Management Board of Maschinenfabrik Berthold Hermle AG
Other memberships of supervisory boards and controlling bodies:
President of the Administrative Board of Hermle WWE (Worldwide Export) AG, Neuhausen/Switzerland

Lothar Hermle, Deputy Chairman
Production Foreman

Dr. Sonja Leibinger, Deputy Chairwoman
Attorney
Other memberships of supervisory boards and controlling bodies:
Chairman of the Supervisory Board of AdCapital AG, Tuttlingen

Dr. Wolfgang Kuhn,
Chairman of the Management Board of Südwestbank AG, Stuttgart
Other memberships of supervisory boards and controlling bodies:
Deputy Chairman of the Supervisory Board of KIWI Financial Living AG, Heidelberg
Chairman of the Supervisory Board of Tresides Asset Management GmbH, Stuttgart
Advisory Board member, SWB Treuhand GmbH, Stuttgart
Chairman of the Board of Partners, Blue Estate GmbH, Stuttgart, to July 14, 2017
Chairman of the Advisory Board of Vertiva Family Office GmbH, Stuttgart, from November 22, 2017

Adolf Weber*
Chairman of the Works Council

Gerd Grewin*
Industrial Foreman, Control Technician

Günther Leibinger, Honorary Member
Entrepreneur

* Elected employee representatives

(36) Assurance of the legal representatives (balance sheet oath):

We assure to the best of our knowledge that pursuant to the applicable accounting principles, the consolidated financial statement gives a true and fair view of the net assets, financial position, results of operations and cash flows, and in the joint management report of Maschinenfabrik Berthold Hermle AG and the Group the business development, including the business result, and the Group's position are stated such that a true and fair view of the actual circumstances is presented, and the key opportunities and risks of the likely development are described.

Gosheim, March 29, 2018
Maschinenfabrik Berthold Hermle AG

Günther Beck Franz-Xaver Bernhard Alfons Betting Benedikt Hermle

03.10
Auditor's Report

Independent auditor's report

AUDITOR'S REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS AND THE SUMMARY MANAGEMENT REPORT

Audit appraisal

We have audited the consolidated financial statements of Maschinenfabrik Berthold Hermle AG, Gosheim, and its subsidiary companies (the Group) – comprising the Group balance sheet as per December 31, 2017, the Group income statement, the overall Group income statement, the Group equity statement and the Group cash flow statement – for the business year from January 1, 2017 to December 31, 2017, as well as the Group Notes to the financial statements, including a summary of key financial reporting methods applied.

We have also audited the Group management report of Maschinenfabrik Berthold Hermle AG, which was summarized together with the company management report (in the following referred to as the summary management report), for the business year from January 1, 2017 to December 31, 2017. In accordance with German law, we have not reviewed the content of the parts of the summary management report cited in the "Other information" section of our audit report.

In our opinion, based on the findings of our audit,

- the enclosed consolidated financial statements comply in all respects with IFRS, as adopted in the EU, and with the additional requirements of section 315e (1) of the German Commercial Code (HGB), and in line with those requirements give a true and fair view of the net assets and financial position of the Group as per December 31, 2017, and of the results of its operations and cash flows for the business year from January 1, 2017 to December 31, 2017.
- The summary management report as a whole provides an accurate view of the Group's position. The summary management report is consistent with the consolidated financial statement in all material respects, complies with German law, and accurately presents the opportunities and risks of future developments. Our appraisal of the summary management report does not extend to the content of the parts of the Group management report cited in the "Other information" section.

Pursuant to section 322 (3), clause 1 HGB, we hereby declare that our audit raised no objections concerning the accuracy and propriety of the consolidated financial statements or the summary management report.

Basis of the audit appraisal

We conducted our audit of the consolidated financial statements and the summary management report in accordance with section 317 HGB and EU Regulation 537/2014 on specific requirements regarding statutory audit of public-interest entities (in the following referred to as the EU Audit Regulation), in line with the generally accepted German standards for the auditing of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Our responsibilities pursuant to the said regulations and principles is detailed in the section of our audit report headed "Responsibilities of the auditor for auditing the consolidated financial statements and the summary management report". In accordance with European law and with German commercial law and professional standards, we are independent of the Group companies, and have fulfilled our other professional duties as German auditors in line with the said requirements. Furthermore, we hereby declare in accordance with Article 10 (2) f) of the EU Audit Regulation that we have provided no prohibited non-audit services pursuant to Article 5 (1) of the EU Audit Regulation. In our view, the documentary records we requested were adequate and suitable to serve as the basis for our audit of the consolidated financial statements and the summary management report.

Key matters in auditing the consolidated financial statements

Key audit matters are matters which according to our prudent judgment were the most significant in our audit of the consolidated financial statements for the business year from January 1, 2017 to December 31, 2017. The said matters were given due consideration in the context of our audit of the consolidated financial statements as a whole and in drawing up our overall audit appraisal; we provide no separate appraisal of the said matters.

In our view, the following matters were the most significant in our audit:

1. Valuation of inventory assets
2. Recognition and valuation of other provisions

We structured our presentation of these key audit matters as follows:

a. Matter and problem at hand
b. Audit procedure and findings
c. Reference to more detailed information

In the following we set forth the key audit matters:

1. Valuation of inventory assets

a. Matter and problem at hand

The "Inventories" balance sheet item in the consolidated financial statements of Maschinenfabrik Berthold Hermle AG shows inventory assets totaling € 62.1 million. The inventory assets are valued at the lower of cost or net realizable value. The measurement of net realizable value is largely dependent on the estimates and assumptions made by the legal representatives. Since this entails a risk that the valuation of the inventory assets might not be within an appropriate range, this matter was, in our view, of particular importance to the audit.

b. Audit procedure and findings

In the course of our audit, we initially traced the method of measuring the net realizable values. We also assessed the adequacy of the key estimates and assumptions by the legal representatives based on the past.

We additionally checked to ensure that the result of the valuation of inventories was accurately recorded in the consolidated financial statements – that is to say, that the inventories were stated at the lower of cost or net realizable value.

We ascertained that the net realizable values were measured accurately, and that the estimates and assumptions made by the legal representatives were adequately documented and justified.

c. Reference to more detailed information

The company's disclosures regarding the valuation of inventory assets are set out in section (6) "Accounting and valuation methods" and in section (9) "Inventories".

2. Recognition and valuation of other provisions

a. Matter and problem at hand

The "Long-term provisions" and "Short-term provisions" balance sheet items in the consolidated financial statements of Maschinenfabrik Berthold Hermle AG show other provisions totaling € 40.6 million. In our view, this matter was of particular importance because the recognition and valuation of these items – representing substantial amounts – was largely based on estimates and assumptions made by the company's legal representatives.

b. Audit procedure and findings

Being aware that estimated values entail an increased risk of financial reporting errors, and that decisions on recognition and valuation made by the legal representatives have a direct effect on the Group's results, we assessed the adequacy of the values stated. Among others aspects, we considered the contractual bases, cost estimates, and the existence of de-facto commitments in assessing the recognition and valuation of commitments.

We ascertained that the estimates and assumptions made by the legal representatives were adequately documented and evidenced as a means of justifying the recognition and valuation of the other provisions in significant amounts.

c. Reference to more detailed information

The company's disclosures regarding the other provisions are set out in section (6) "Accounting and valuation methods" and in section (15) "Provisions".

03.10
Auditor's Report

Other information

The legal representatives are responsible for the other information given. The other information comprises the following information procured by us prior to the date of this audit report:

- The separate Non-Financial Report pursuant to section 289b subsection 3 and section 315b subsection 3 HGB contained in the first paragraph of the summary management report.
- The Corporate Governance Statement pursuant to section 289f and section 315d HGB contained in the paragraph headed "Corporate Governance Statement".
- The report pursuant to section 21 of the German law governing transparency of pay to promote equality between men and women ('Entgelttransparenzgesetz') appended to the summary management report of the parent company.
- The assurance pursuant to section 297 subsection 2, clause 4 HGB relating to the annual financial statements and the assurance pursuant to section 315 subsection 1, clause 5 HGB relating to the summary management report.

The other information also includes the remaining parts of the annual report likely to be provided to us after this date, with the exception of the audited consolidated financial statements, the audited summary management report, and our audit report.

Our audit appraisal of the consolidated financial statements and the summary management report does not extend to the other information. Accordingly, we provide no audit appraisal, nor do we present any other form of audit conclusions, on the said other information.

In connection with our audit we have a duty to read the other information, and to consider whether the other information

- contains material inaccuracies relating to the consolidated financial statements, the summary management report or our findings from the audit, or
- appears to be materially incorrectly presented in any other way.

Responsibility of the legal representatives and of the Supervisory Board for the consolidated financial statements and the summary management report

The legal representatives are responsible for compiling the consolidated financial statements in compliance with IFRS, as applicable in the EU, and with the additional German legal requirements pursuant to section 315e subsection 1 HGB in all material respects, and for ensuring that the consolidated financial statements convey a true and accurate view of the net assets, financial position, results of operations and cash flows of the Group in line with those requirements. The legal representatives are also responsible for the internal controls which they have designated as necessary in order to compile consolidated financial statements containing no – intentionally or unintentionally – materially false information.

In compiling the consolidated financial statements, the legal representatives are responsible for assessing the ability of the Group to maintain its business operations. They further have a duty to disclose any relevant matters pertinent to the maintaining of business operations. Their responsibilities also include reporting on the Group's ability to maintain business operations on the basis of financial reporting principles, unless it is intended that the Group should be liquidated or cease its business operations, or there is no realistic alternative to doing so.

The legal representatives are also responsible for compiling the summary management report, presenting an accurate overall view of the Group's position and complying in all material respects with the consolidated financial statements and with German law, and accurately presenting the opportunities and risks of future developments. The legal representatives are also responsible for implementing the precautions and measures (systems) they consider necessary in order to compile a Group management report in compliance with the applicable German laws and to provide adequate and suitable evidence supporting the statements made in the Group management report.

The Supervisory Board is responsible for overseeing the Group's financial reporting processes in compiling the consolidated financial statements and the summary management report.

Responsibilities of the auditor for auditing the consolidated financial statements and the summary management report

Our objective is to establish with adequate certainty that the consolidated financial statements as a whole contain no – intentionally or unintentionally – materially false information, and that the summary management report presents an accurate overall view of the Group's position and complies in all material respects with the consolidated financial statements, with the findings of the audit, and with German law, and accurately presents the opportunities and risks of future developments. We are required to draw up an audit report setting forth our appraisal of the consolidated financial statements and the summary management report.

'Adequate certainty' means a high degree of certainty, but does not guarantee that an audit conducted in accordance with section 317 HGB and the EU Audit Regulation, in line with the generally accepted German standards for the auditing of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW), will reveal all materially false information. False information may result from violations of regulations or from errors, and is regarded as material if it might reasonably be expected that – in isolation or overall – it will influence commercial decisions of the target readership taken on the basis of these consolidated financial statements and this summary management report.

During the audit, we exercise due diligence in making judgments and adopt a critical view. Additionally:

- We identify and assess the risks of intentionally or unintentionally materially false information presented in the consolidated financial statements and the summary management report, plan and implement audit procedures in response to the said risks, and gather evidence which is adequate and suitable to serve as the basis for our audit appraisal. The risk that materially false information will not be revealed is higher in the case of violations against regulations than it is in the event of errors being made, as violations can include fraudulent collaboration, fakery, intentional omission, presentation of misleading information or the bypassing or disabling of internal controls.
- We gain an understanding of the internal control system relevant to auditing of the consolidated financial statements and the precautions and measures relevant to auditing of the summary management report, in order to plan audit procedures which are appropriate to the given circumstances, though not with the aim of appraising the efficacy of the company systems.
- We assess the adequacy of the financial reporting methods applied by the legal representatives and the accuracy of the estimated values and related information give by the legal representatives.
- We draw conclusions as to the adequacy of the financial reporting methods applied by the legal representatives in evidencing the ability of the Group to maintain its business operations, and check on the basis of the audit evidence gathered whether there is any material uncertainty in relation to events or circumstances which might cast significant doubt on the ability of the Group to maintain its business operations. If we conclude that there is any material uncertainty, we have a duty to cite the relevant disclosures in the consolidated financial statements and the summary management report in our audit report or, if the said disclosures are inappropriate, to modify our audit appraisal. We draw our conclusions on the basis of the audit evidence gathered up to the date of our audit report. Future events or circumstances may, however, result in the Group no longer being able to maintain its business operations.
- We assess the overall view presented, and the structure and content of the consolidated financial statements, including the disclosures in it, as well as assessing whether the consolidated financial statements present the underlying transactions and events such that the consolidated financial statements in compliance with IFRS, as applicable in the EU, and with the additional German legal requirements pursuant to section 315e subsection 1 HGB convey a true and accurate view of the net assets, financial position, results of operations and cash flows of the Group.
- We gather adequate and suitable audit evidence concerning the financial reporting information on the companies or business operations within the Group in order to provide appraisals of the consolidated financial statements and the summary management report. We are responsible for guiding, supervising and conducting the audit of the consolidated financial statements. We bear sole responsibility for our audit appraisal.
- We assess the conformance of the summary management report to the consolidated financial statements, its legal compliance, and the view it provides of the Group's position.
- We implement audit procedures relating to the forward-looking information set out by the legal representatives in the summary management report. Based on adequate and suitable audit evidence, we in particular trace the significant assumptions made by the legal representatives underpinning the forward-looking information they set out, and assess the correct and proper derivation of the said forward-looking information from the said assumptions. We do not provide a separate appraisal of the forward-looking information or of the assumptions underpinning it. There is a significant unavoidable risk that future events will vary materially from the forward-looking information presented.

We consult with the staff responsible for overseeing the planned audit on matters including the scope and timing of the audit, and discuss with them significant findings from the audit, including any deficiencies in the internal control system which we identify in the course of our audit.

We provide the staff responsible for overseeing the audit with a declaration that we have complied with the relevant requirements for independence, and discuss with them all the relationships and any other matters which might reasonably give rise to the assumption that our independence could be impaired, as well as discussing with them the preventive measures implemented to prevent any such impairment.

03.10
Auditor's Report

From the matters discussed with the staff responsible for overseeing the audit, we define those matters which were most significant in auditing the consolidated financial statements for the current reporting period, and which consequently are considered to be key audit matters. We detail the said matters in our audit report, unless the law or other legally binding regulations prohibit public disclosure of the matters.

OTHER STATUTORY REQUIREMENTS

Other disclosure pursuant to Article 10 of the EU Audit Regulation

We were elected to audit the consolidated financial statements by the shareholders' meeting on July 5. 2017. We were contracted to conduct the audit by the Supervisory Board on August 24, 2017. We have been the auditors of the consolidated financial statements of Maschinenfabrik Berthold Hermle AG without interruption since the 1990 business year.

We hereby declare that the audit appraisals set forth in this audit report conform to the additional report to the Supervisory Board pursuant to Article 11 of the EU Audit Regulation (Additional report to the audit committee).

RESPONSIBLE AUDITOR

The auditor responsible for the audit is Mr. Andreas K. Wiedmann.

Stuttgart, March 29, 2018

BANSBACH GMBH
Auditors and tax consultants

(Hauser) Auditor	(Wiedmann) Auditor

04 Additional Information

Model making.
Cylinder.

Model making. Cylinder for prototyping in aluminum.
Highly dynamic 5-axis simultaneous machining for a perfect finish.

04.1 Balance Sheet

of Maschinenfabrik Berthold Hermle AG

ASSETS	12.31.2017 €k	Previous year €k
Fixed assets		
Intangible assets	1,160	1,213
Property, plant and equipment	62,584	53,155
Long-term financial assets	3,401	3,401
	67,145	57,769
Current assets		
Inventories	59,488	50,156
Trade and other receivables		
Receivables	48,622	45,454
Other assets	5,351	6,701
Marketable securities	8,128	6,305
Cash on hand and cash in banks	74,827	81,201
	196,416	189,817
Deferred charges and prepaid expenses	604	308
TOTAL ASSETS	264,165	247,894

LIABILITIES		
Shareholders' equity		
Subscribed capital	15,000	15,000
Capital reserve	2,874	2,874
Revenue reserves	97,517	103,517
Balance sheet profit	75,362	64,064
	190,753	185,455
Provisions	39,378	35,709
Liabilities		
Financial liabilities	0	0
Other liabilities	33,451	26,076
	33,451	26,076
Deferred charges and prepaid expenses	583	654
TOTAL LIABILITIES	264,165	247,894

04.2 Income Statement

of Maschinenfabrik Berthold Hermle AG

	2017 €k	Previous year €k
Sales	376,002	360,894
Change in stock of finished and unfinished products	4,452	230
Other own work capitalized	519	140
Total turnover and operating revenue	380,973	361,264
Other operating income	5,399	7,093
Material expenses	174,838	165,991
Personnel expenses	71,877	66,519
Depreciation	6,482	5,585
Other operating expenses	42,808	43,565
Operating result	90,367	86,697
Financial and operating result	3,177	801
Earnings before taxes	93,544	87,498
Taxes on income and earnings	24,040	22,708
Earnings after taxes	69,504	64,790
Other taxes	157	173
Net income	69,347	64,617
Profit carried forward	15	447
(+) Withdrawal from / (-) Allocation to revenue reserves	6,000	-1,000
Balance sheet profit	75,362	64,064

The complete annual financial statement of Maschinenfabrik Berthold Hermle AG, including the audit certificate, is published at www.hermle.de (menu item: Investor Relations/Financial reports).

04.3 Proposal for the Appropriation of Profits

Resolution on appropriation of balance sheet profit for the 2017 business year

The Management Board and Supervisory Board proposes to appropriate the balance sheet profit of the 2017 business year of € 75,361,754.90 as follows:

Distribution of a dividend of € 15.00 for each ordinary share (€ 0.80 + € 12.00 bonus + € 2.20 one-off special bonus) Security identification number 605 280 / ISIN DE0006052806 for 4,000,000 ordinary shares for the 2017 business year:	€ 60,000,000.00
Distribution of a dividend of € 15.05 for each preference share (€ 0.85 + € 12.00 bonus + € 2.20 one-off special bonus) Security identification number 605 283 / ISIN DE0006052830 for 1,000,000 preference shares for the 2017 business year:	€ 15,050,000.00
To be carried forward to new account:	€ 311,754.90
Balance sheet profit	€ 75,361,754.90

In accordance with section 58 subsection 4, clause 2 of the German Stock Corporation Act (AktG), claims to a dividend become due on the third working day following the resolution by the shareholders' meeting, i.e. on July 9, 2018. Therefore the dividend shall be paid out on July 9, 2018.

Insofar as Maschinenfabrik Berthold Hermle AG holds its treasury shares at the time at which a resolution is adopted at the shareholders' meeting, these shall not be eligible for a dividend pursuant to the German Stock Corporation Act. The partial amount attributable to individual share certificates will likewise be carried forward to a new account.

Gosheim, April 25, 2018

Maschinenfabrik Berthold Hermle AG

Günther Beck   Franz-Xaver Bernhard   Benedikt Hermle

04.4
Hermle Worldwide

Hermle + Partner Vertriebs GmbH
Gosheim, Germany
www.hermle.de

Hermle-Leibinger
Systemtechnik GmbH
Gosheim, Germany
www.hermle.de

Hermle Maschinenbau GmbH
Ottobrunn, Germany
www.hermle-generativ-fertigen.de

Hermle Austria
Vöcklabruck Branch,
Austria
www.hermle-austria.at

Hermle Česká Republika,
Organizacni slozka,
Prague Branch, Czech Republic
www.hermle.cz

Hermle Polska
Warsaw Branch, Poland
www.hermle.pl

Hermle Nordic
Odense Branch, Denmark
www.hermle-nordic.dk

Hermle Southeast Europe
Sofia, Bulgaria
www.hermle.de

Hermle (Schweiz) AG
Neuhausen am Rheinfall, Switzerland
www.hermle-schweiz.ch

Hermle Machine Company LLC
Franklin/WI, USA
www.hermlemachine.com

Hermle Nederland B.V.
Horst, Netherlands
www.hermle-nederland.nl

Hermle Belgium
Belgium
www.hermle-nederland.nl

Hermle Italia S.r.l.
Rodano, Italy
www.hermle-italia.it

Hermle WWE AG
Neuhausen am Rheinfall, Switzerland
www.hermle-vostok.ru

Hermle Vostok OOO
Moscow, Russian Federation
www.hermle-vostok.ru

Hermle China
Shanghai and Beijing
Representative Office, China
www.hermle.de

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