

Business Report

www.hermle.de



2016





01.1 Hermle at a Glance

<i>Hermle Group</i>						
€ million	2012*	2013	2014	2015	2016	Change 2016/2015 in %
Sales	302.7	305.9	346.8	356.6	394.0	10.5 %
- Domestic	133.9	121.3	147.7	147.9	160.3	8.3 %
- Foreign	168.8	184.6	199.1	208.7	233.7	12.0 %
Incoming orders	306.1	352.3	332.5	360.7	364.5	1.0 %
Orders on hand	87.0	133.4	119.1	123.2	93.8	-23.9 %
Capital investments	4.3	7.8	15.4	7.1	16.4	130.7 %
- Fixed assets**	4.3	7.8	15.4	7.1	16.4	130.7 %
- Financial assets	–	–	–	–	–	–
Depreciation	7.5	6.6	6.2	6.7	7.0	3.5 %
- Fixed assets**	7.5	6.6	6.2	6.7	7.0	3.5 %
- Financial assets	–	–	–	–	–	–
Earnings before taxes	63.9	62.2	79.4	80.6	100.3	24.4 %
Net income	46.0	45.5	58.8	59.2	73.8	24.8 %
Cash flow	53.2	51.2	64.4	65.4	80.8	23.4 %
Balance sheet total	243.9	258.2	282.7	288.4	309.6	7.4 %
Shareholders' equity	175.5	185.2	202.8	209.8	229.9	9.6 %
Employees (record date 31.12.)	927	912	964	977	1018	4.2 %

* Data before conversion to at-equity consolidation including Hermle-Leibinger Systemtechnik GmbH and its employees.

** 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



Automotive Engineering. Frame section.



Automotive engineering. Frame section of an aluminum footrest support for a motorcycle. Complex 5-axis full-machining milling process – for extreme demands in racing.

Contents

01 Hermle	U1	01.1 Hermle at a glance U1 01.2 Company executive bodies 3 01.3 Company history 4 01.4 Highlights 2016 5 01.5 Introduction by the Board of Management 8
02 Reports	10	02.1 Report of the Supervisory Board 12 02.2 Parent company management report and Group report 14 02.3 The Hermle share 33 02.4 Investment projects and innovations 36
03 Consolidated financial statement	40	03.1 Group balance sheet 43 03.2 Group income statement 44 03.3 Overall Group income statement 45 03.4 Group equity statement 46 03.5 Group cash flow statement 48 03.6 Segment reporting 49 03.7 Group statement of asset additions and disposals 2016 50 03.8 Group statement of asset additions and disposals 2015 52 03.9 Group Notes to the Financial Statements 54 03.10 Auditor's report 84
04 Additional information	86	Information about Maschinenfabrik Berthold Hermle AG 04.1 Balance sheet 88 04.2 Income statement 89 04.3 Proposal for the appropriation of profits 90 04.4 Hermle worldwide 91

Date of shareholders' meeting: Wednesday, July 5, 2017 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

Joachim Weber*
Applications Technologist (until 6 July 2016)

Gerd Grewin*
Industrial Foreman, Control Technician (from 6 July 2016)

Günther Leibinger
Honorary Director,
Merchant

Management Board

Günther Beck
Areas of responsibility:
Finances Information technology
Material Management

Franz-Xaver Bernhard
Areas of responsibility:
Research & development Sales

Alfons Betting
Areas of responsibility:
Production Service

Fully authorized representative

Gabriele Peyerl
Area of responsibility:
Human resources

*Elected employee representatives

Additional Board of Management and Supervisory Board positions are stated on page 82.

01.3

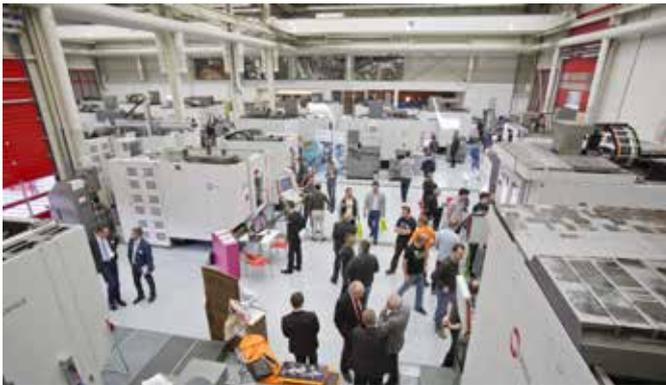
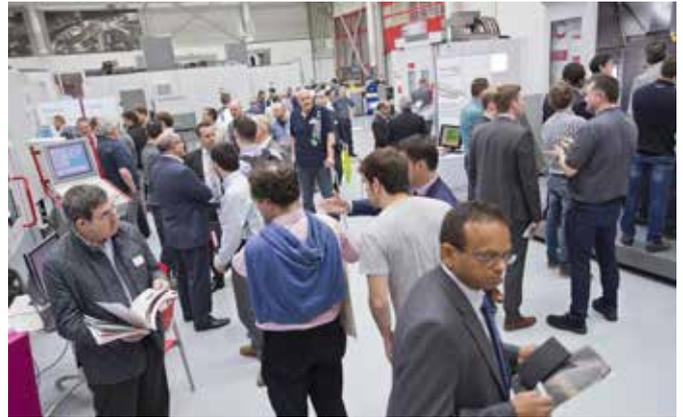
Company History

- 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.

01.4 2016 Highlights

April I – Open House with record visitor numbers

More than 2800 guests from 1200 companies find out about the latest trends in milling, turning and additive manufacturing at the Hermle Open House 2016. The popular sector meeting-place set a new visitor record. The specialists come from Germany and elsewhere in Europe, but visitors from the USA, Japan and India also come from much further afield to check out Hermle's latest innovations.



April II – Highlight C 250

Hermle's most important new product in 2016 is the C 250, a compact entry-level machine for 3-axis to 5-axis machining. Together with the larger C 400 variant, it makes up the Hermle Performance Line, characterized by high-quality, standardized equipment. Other newcomers on display at the Open House are the modified version of the C 62 large machining center from the High-Performance Line, innovative MPA technology and various software components for Hermle Industry 4.0 solutions.



01.4 2016 Highlights

May – New land for future growth

Hermle buys a plot in the Rottweil district so as to secure options for future expansion. The new location in Zimmern ob Rottweil supplements the company's head office in Gosheim and is quite close both to Gosheim as well as to the freeway. It is also located in an area specifically earmarked for industrial development, so it is not subject to serious limitations in terms of planning permission.



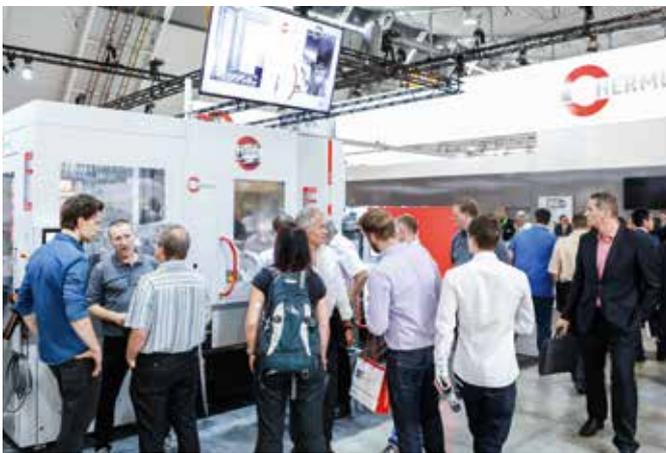
August – Expansion of metal-cutting manufacturing

Work commences on extending and modernizing the metal-cutting manufacturing facilities at the Gosheim location. In a first step, a new building shell is erected over older production halls during the 3-week vacation close-down. Over the following months, interior construction and the installation of state-of-the-art technical plant is carried out in parallel with normal operations. The complex construction project is scheduled to be completed in August 2017 with the demolition of the old buildings.



September I – Hermle at AMB and IMTS

Hermle presents itself at the two most important sector meeting places, the AMB in Stuttgart (Ausstellung für Metallbearbeitung, Exhibition for Metalworking) and the IMTS (International Manufacturing Technology Show) in Chicago, North America's largest trade fair for machining technology. The stars of Hermle's show are the Performance Line and High-Performance Line as well as various innovations in the areas of product automation and digitalization.



September II – Construction begins in Zimmern

Just four months after purchasing the plot, Hermle can begin the construction of a modern production building at the new location in Zimmern ob Rottweil. In a first step, facilities for Hermle's own production of mineral-cast machine beds are to be installed. In addition to this, there is enough space there for other activities with new products and services.



01.5

Introduction by the Board of Management

***DEAR SHAREHOLDERS, BUSINESS PARTNERS
AND FRIENDS OF THE COMPANY,***

For Maschinenfabrik Berthold Hermle AG, 2016 was an unusually successful year in which new peak levels could be achieved: The Group turnover increased by more than 10 % to 394.0 million euros, while the profits went up even more steeply, from 59.2 euros to 73.8 euros. The incoming orders also increased slightly to 364.5 million euros, whereby the demand in the second half of the year normalized noticeably and as anticipated.

The gratifying development gives the Board of Management and Supervisory Board reason to propose a higher dividend for the past business year: In addition to the unchanged base dividend of € 0.80 for each ordinary share and € 0.85 for each preference share, a bonus of € 12.00 is to be paid for each share. With this, the dividend payment per preference share increases from € 10.85 to € 12.85.

Without the great efforts and well-grounded know-how of the entire Hermle team, such excellent results for 2016 would not have been possible. Therefore we once again wish to ensure that the employees can participate in the company's success: On conclusion of the dividend distribution, all Hermle AG employees will receive a wage-related bonus and a fixed lump sum, as was the case in previous years. The Board of Management expressly thanks all employees for the outstanding performance and the tremendous motivation with which they have mastered the various tasks of the previous year.

In addition to the daily routine – demanding enough in itself – there were two major projects for securing viability in the future that needed attention in the year under review. In Gosheim, we began with the extension and modernization of the metal-cutting manufacturing facilities.

To this end, an existing building complex was built over during the vacation close-down, and then equipped with new plant and state-of-the-art technology in parallel with normal operation. The old building shell will remain in place to protect the production facilities, before being demolished in August 2017.

To supplement our head office premises and with an eye to securing long-term development options, we also bought a plot of industrial land in the neighboring district of Rottweil in May 2016. As a first step, we shall set up our own production plant for mineral-cast machine beds, and this will be followed by other activities in due course. After a brief period needed to obtain planning permission, we were able to start construction as early as September. Commissioning is planned for the second quarter of 2017.

These two projects – and it goes without saying that they take the very latest sustainability criteria into account – represent part of Hermle's strategy to keep its production capacities at the cutting edge of technological development. This includes paying close attention to the demands made by Industry 4.0. A large number of our manufacturing processes are already networked and digitalized. For this, we use the control and digitalization components that we ourselves put on the market, amongst others. This range of products was extended in the course of the year under review, putting us in a position to set up Industry 4.0 manufacturing using Hermle machines and components.

Hermle also provided new solutions for all the other important sector trends in the course of 2016: Here, the main focus is on the machining centers, of course. Our Performance Line comprising high-quality, standardized entry-level machines, was extended by the introduction of the compact C 250. We have extended the High-Performance Line of extremely precise and dynamic machines for high-tech applications into the next generation. The C 62 machining centers are the largest so far.

In addition to this, we have developed a new, high-performance generation of spindles and an innovative entry-level automation solution which was presented during the Open House 2017. As far as additive manufacturing is concerned, which Hermle addresses with its MPA technology, the accent was on new, customer-specific applications.

Alongside these technological trends, service provision for machine tool engineering is playing an increasingly important role. Our aim is to make things as straightforward for our customers as possible in view of the increasing complexity of the machines and the networked, digitalized machining processes. Therefore we have extended our service capacities on an international scale and decentralized them further in the course of the year under review.

Despite increasingly difficult boundary conditions, Hermle has made a good start in the business year 2017. The anticipated normalization of demand during the fourth quarter meant that the number of orders on hand was significantly less than for 2016. This was accompanied by a great deal of uncertainty in our operational environment that was aggravated by individual events such as the Brexit vote and the new Administration in the USA. Therefore we think it might be possible that the incoming orders and turnover might reduce by a mid-one digit percent figure in 2017. The results would then fall off disproportionately.

However, after the unusually good year 2016, we would still consider that to be a satisfactory development. Hermle remains well equipped to deal with the normal ups and downs experienced by the machine tool engineering sector. Our 'breathing company' concept that helps us to cushion the effects of fluctuations in demand remains fully viable even 15 years after it was first introduced. In combination with a high degree of financial independence, it enables our company to achieve solid results even in weak phases of the economic cycle. At the same time, our strong equity and liquidity basis enables us to make anticyclical investments. For instance, the two major capacity-extending projects that will be concluded in 2017 mean that we have already secured our options for long-term development.

Best regards,



Günther Beck
Board of Management



Franz-Xaver Bernhard
Board of Management



Alfons Betting
Board of Management

02 Reports



Tool and mold making. Smartphone holder.



Tool and mold making. Steel die form for a smartphone holder.
Complex ultra-high-precision 5-axis simultaneous machining with top-quality surface finish.

02.1

Supervisory Board Report

LADIES AND GENTLEMEN, DEAR SHAREHOLDERS,

The business year 2016 was extraordinarily successful for Maschinenfabrik Berthold Hermle AG. Compared with the record figures for the previous year, turnover and profits once more increased significantly. Both the employees and the Board of Management have made significant contributions to this gratifying development. In the name of the Supervisory Board I should like to thank the team in its entirety for these good results.

Close cooperation between the Board of Management and the Supervisory Board

In 2016, the Supervisory Board fulfilled all the tasks devolving upon it according to both legislative requirements as well as the statutes with due care and attention, while providing consultative support to and constructive supervision of the Board of Management. Throughout the year, we conducted regular detailed reviews of the situation and development of the parent company Hermle AG and of the Group as a whole, including the associated opportunities and risks. As well as the economic progress and the financial and earnings situation, we paid close attention to corporate planning, including financial, investment and human resources planning and corporate policymaking. This was on the basis of detailed verbal and written reports supplied by the Board of Management both prior to and during supervisory board meetings. All decisions involving approval were taken by the Supervisory Board on the basis of comprehensive documentation and in-depth discussion. The Supervisory Board and the Board of Management also kept up regular contact between the meetings in order to air current topics.

Supervisory Board meetings and committees

During the year under review, the Supervisory Board had five scheduled meetings: on March 17, April 27, 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 2016.

The main Supervisory Board issues in 2016

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. Other recurring topics were projects aimed at extending and modernizing capacity.

During the first meeting on March 17, 2016, the Supervisory Board approved the purchase of a plot of land in Zimmern ob Rottweil by way of supplementing the head office in Gosheim and securing options for additional capacity and future growth. The new site is located close to company headquarters in a purely industrial zone with direct access to a freeway, and no construction limitations apply. We also obtained information about the planned modernization and extension of the metal-cutting manufacturing facilities in Gosheim. This project involves building over an existing building so as to increase the usable space and provide for state-of-the-art technological capabilities. In addition, we considered the dividend proposal on the basis of the preliminary figures for the 2015 business year. Other discussion points included various development projects concerning extending the range of products, as well as the organization of the sales operations.

During the accounts meeting held on April 27, 2016, the Supervisory Board paid special attention to the year-end results of the Hermle AG and the Group for the 2015 business year, in addition to the regular topics. We discussed the results in detail, ascertained them and then approved them in the presence of the auditor. We also agreed upon the Supervisory Board's report and the dividend proposal, as well as the other points for the 2016 annual general meeting agenda.

The meetings on July 6, 2016, took place before and after the annual general meeting. During the meetings, we dealt amongst other things with the competitive situation in the international machine tool industry, the scheduled expansion measures for metal-cutting manufacturing in Gosheim and the fine points of the new construction at the new location in Zimmern. As a first step, the company is to build its own mineral casting facility. We also obtained information about developments and progress in the MPA (Metal Powder Application) additive manufacturing technology.

The Supervisory Board meeting on December 6, 2016, focused on the budget and investment planning for 2017, which was discussed in detail and subsequently approved. Our deliberations also included the fast and punctual implementation of the construction projects in Gosheim and Zimmern ob Rottweil. In addition to that, we debated strategic development options for the company headquarters and various subsidiaries. Finally, we agreed upon the corporate governance declaration. There was no change in respect of the previous year's declaration, and it is permanently available on the Hermle website under the heading Investor Relations / Pflichtveröffentlichungen / Kodex § 161 AktG.

Audit of the annual financial statement

On July 6, 2016, the annual general meeting voted in favor of commissioning the financial auditing and tax consulting company Bansbach GmbH, Stuttgart, to conduct the annual audit for the 2016 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.

The annual financial statement of the Maschinenfabrik Berthold Hermle AG was drawn up according to the requirements of the German Commercial Code (HGB), taking changes to the German Accounting Directive Implementation Act (Bilanzrichtlinie-Umsetzungsgesetz, BilRUG) into account. The consolidated financial statement was based on the IFRS standards. Bansbach GmbH audited the financial statements of Hermle AG and of the Group, as well as the summary management report for the 2016 business year, including the bookkeeping, and certified its unreserved confirmation in each case. The risk management and the internal control system were also investigated and considered effective. 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 with the annual financial statement of Hermle AG, the consolidated financial statement, the summarized management report and the audit reports in good time. We scrutinized the documents and discussed them together with the auditor during the accounts meeting. We did not encounter any discrepancies during our own scrutiny, so we concurred with the audit results. The Supervisory Board approved the financial statements and the summarized management report. The annual financial statement of Maschinenfabrik Berthold Hermle AG is therefore formally approved. We also concur with the proposal on the appropriation of profits put forward by the Board of Management 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, which bonus represents an increase from € 10.00.

Changes in the constitution of the Supervisory Board

On the occasion of the new elections of employee representatives to the Supervisory Board held on May 18, 2016, the employees elected Mr Gerd Grewin and Mr Adolf Weber to represent them with effect from the conclusion of the annual general meeting on July 6, 2016. Mr Joachim Weber retired from our Board as employee representative after the annual general meeting. The Supervisory Board expresses its thanks to him for his contribution, which was always constructive and characterized by a basis of mutual trust. The shareholder representatives on the Supervisory Board were reelected by the annual general meeting on July 6, 2016. In the course of the ensuing constitutive meeting, Mr Dietmar Hermle was reconfirmed as Chairman of the Supervisory Board, Dr Sonja Leibinger and Mr Lothar Hermle as deputy Chairpersons and Dr Wolfgang Kuhn as financial expert.

It is to be expected that Hermle's business will normalize during 2017 as a result of a significantly lower number of orders on hand. The uncertainties of the larger picture and the two large construction projects that are scheduled for completion in the current year mean that all employees and the Board of Management are faced with challenging tasks. The Supervisory Board wishes them every success here.

Gosheim, April 2017



Dietmar Hermle
Chairman of the Supervisory Board

02.2

Management Report of the AG and Group Management Report

This report is a summarized management report for 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 2016 complied with the International Financial Reporting Standards (IFRS), as applicable within the European Union. The requirements of the German Commercial Code (HGB) applied to the annual financial statement of the individual company Maschinenfabrik Berthold Hermle AG, taking changes to the German Accounting Directive Implementation Act (Bilanzrichtlinie-Umsetzungsgesetz, BilRUG) into account. Details that refer to the individual company are denoted with the addition "Hermle AG" or "Individual Company".

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 is responsible for the lion's share of the development and production activities, central services and logistics services as well as the commercial and administrative positions. 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.

All companies and production facilities outside Germany are included in the foreign marketing segment. 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. This strategy was pursued successfully in 2016.

The Hermle Group is controlled centrally by Hermle AG. In addition to the incoming orders and turnover, we use the earnings before interest and tax (EBIT) as a KPI, which corresponds to the operating result. The three-member Management Board of Hermle AG has overall management responsibility. The Board of Management 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. The working methods adopted by the Board of Management and the Supervisory Board as well as relevant details of corporate governance practices are set out in the Corporate Governance Statement pursuant to sections 289a and 315 (5) 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).

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 289 (4) and 315 (4) HGB.

BUSINESS REPORT

The boundary conditions remain restrained

In 2016, the world economy once again developed in a less-than dynamic way. The International Monetary Fund (IMF) estimates that global economic activities expanded by around 3.1 %, which is somewhat less than the previous year. The growth prospects and investment preparedness of companies was dampened by a number of factors. According to the IMF, these include the structural upheavals in China, continuing economic difficulties affecting individual EU member states, the Brexit vote and the US election, but also regional crises, the refugee problem and international terrorism.

Taken together, the industrialized countries increased their gross domestic product (GDP) by 1.6 % in 2016. Amongst these countries, the USA's GDP increased by 1.6 %, while that of the euro area by 1.7 %. In comparison, according to preliminary estimates made by the German Federal Statistics Agency, the German economy was a little more dynamic, with a growth rate of 1.9 %. The overall growth rate for the developing and newly industrialized countries was 4.1 %, a figure that has much to do with the situation in China and India: There, the growth rates are slowing, but still highly dynamic.

02.2

Management Report of the AG and Group Management Report

A sound sector environment

According to a statement issued by the Verband Deutscher Maschinen- und Anlagenbau (German Mechanical Engineering Industry Association, VDMA), a decrease in the number of incoming orders in 2016 for the German mechanical engineering sector of 2 % can mainly be attributed to the many political uncertainties that currently prevail. The number of new orders reduced within the domestic market but even more so within the market in Europe. The production volumes of the domestic manufacturers remained at the levels of the previous year. Seen from the global perspective, the VDMA anticipates stagnation in the sales of machines for the year under review. In its view, the sector experienced slight growth in China and stabilization in Europe, but in the USA and in Japan sales went down.

The domestic machine tool industry developed somewhat vigorously. According to the Verein Deutscher Werkzeugmaschinenfabriken (German Machine Tool Builders' Association, VDW), the number of incoming orders for the sector increased by 7 % in 2016, whereby the main impulses came from abroad. The sector production increased by 1 % to a new record value of 15.2 billion euros. This means that Germany ranks third behind China and Japan amongst the most important manufacturing countries.

As in previous years, demand in the machine tool sector was once more apparent for high-grade, but standardized and therefore low-cost, entry-level models. In parallel with this, there is also demand for extremely high-performance, high-precision machines. Significant technological trends could be observed in the increasing automation and digitalization of machining processes (Industry 4.0), as well as additive manufacturing processes (3D printing). The sector remains characterized by intense competition.

An overview of Hermle's business progress

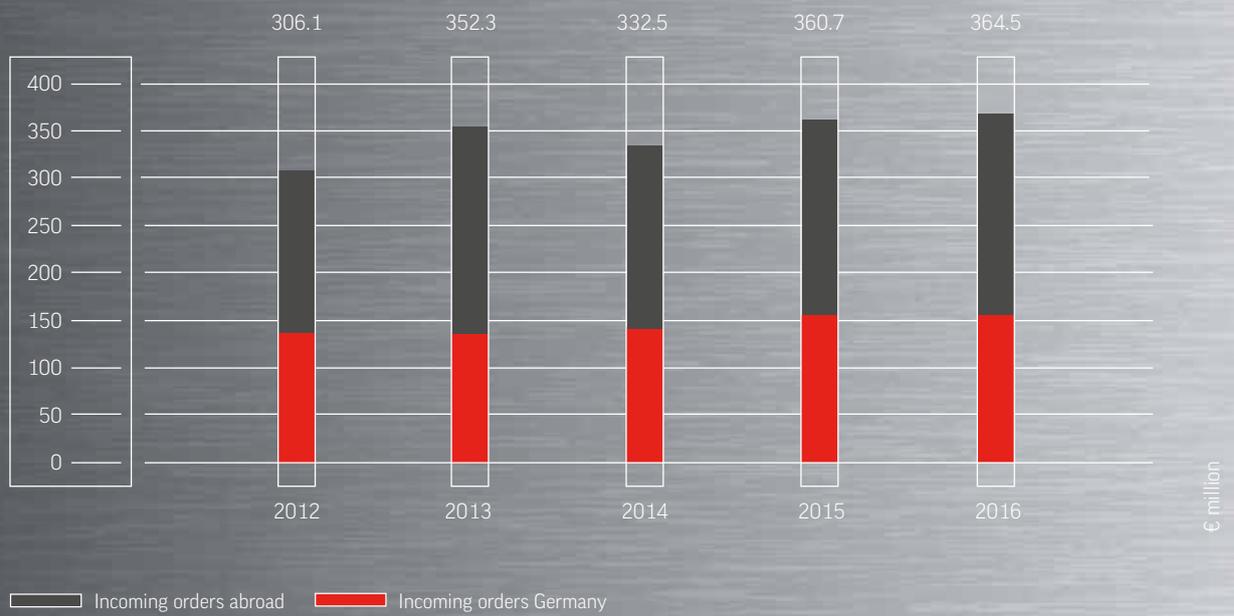
In 2016, Maschinenfabrik Berthold Hermle AG consolidated its market position as a technological leader in 5-axis machining centers. The business year saw a number of major unsettling events and yet remained unusually successful, with Group sales and results increasing significantly. Demand was high not only for our new, high-grade entry-level Performance Line machines, but also for the extremely dynamic and precise, top-of-the-range machining centers of the High-Performance Line, as well as for the multitude of automation solutions. Our plants worked at full capacity throughout the year. As anticipated, the demand settled down in the course of the year. Therefore the incoming order volume only grew by a small amount, and the orders on hand reduced noticeably in numbers.

Incoming orders increase by 1 % to € 364.5 million

New orders across the Hermle Group totaled € 364.5 million in 2016, 1.0 % more than in the previous year. In Germany, we achieved growth figures of 0.6 % to € 156.8 million, while abroad the increase was 1.4 % to € 207.7 million. According to the closing date comparison, the orders on hand at the end of 2016 were down by 23.9 % at € 93.8 million.

For the Hermle AG individual company, incoming orders increased by 3.2 % to € 341.6 million. The new orders from German customers increased by 0.7 % to € 157.8 million, while those from abroad increased by 5.5 % to € 183.8 million. The growth for the individual company have in each case been calculated according to BilRUG (German Accounting Directive Implementation Act) specifications, i.e. taking the corrected previous year figures into account as per BilRUG. On December 31, 2016, the orders on hand amounted to € 89.1 million, i.e. 17.8 % below the previous year's level.

ORDERS RECEIVED BY THE HERMLE GROUP



02.2

Management Report of the AG and Group Management Report

Sales up 10.5 % to € 394.0 million

On the basis of the large volume of orders on hand from the previous year and the continued increase in orders coming in during the first half of 2016, Hermle achieved an upturn in Group sales of 10.5 % during the reporting period, with a new peak of € 394.0 million. Positive impulses came from both the new machine business as well as service provision. New products such as the C 250 from the Performance Line also made important contributions to sales. The volume increased in both domestic and foreign business. Domestic sales went up by 8.3 % to € 160.3 million, and the foreign volume by 12.0 % to € 233.7 million. This meant that the export ratio increased a little, from 58.5 % to 59.3 %.

Sales for the Hermle AG rose by 9.1 % to € 360.9 million. In Germany, the increase was 8.4 % to € 161.3 million, while the foreign sales figure increased by 9.6 % to € 199.6 million. These values have also been calculated on a basis determined according to BilRUG.

Segment development

Classified by segment, the domestic company sales of € 234.7 million were almost the same as those of the previous year (€ 237.3 million). In addition to the Hermle AG, these companies comprise the sales company HPV, the automation solution specialist HLS and the development company HMG. Partly on account of a build-up of major projects, the volume of business in the foreign sales segment rose about by a third to € 159.3 million. The US subsidiary was especially successful, but other companies such as the Dutch and Italian subsidiaries also increased sales considerably.

Operating result grows to € 99.8 million

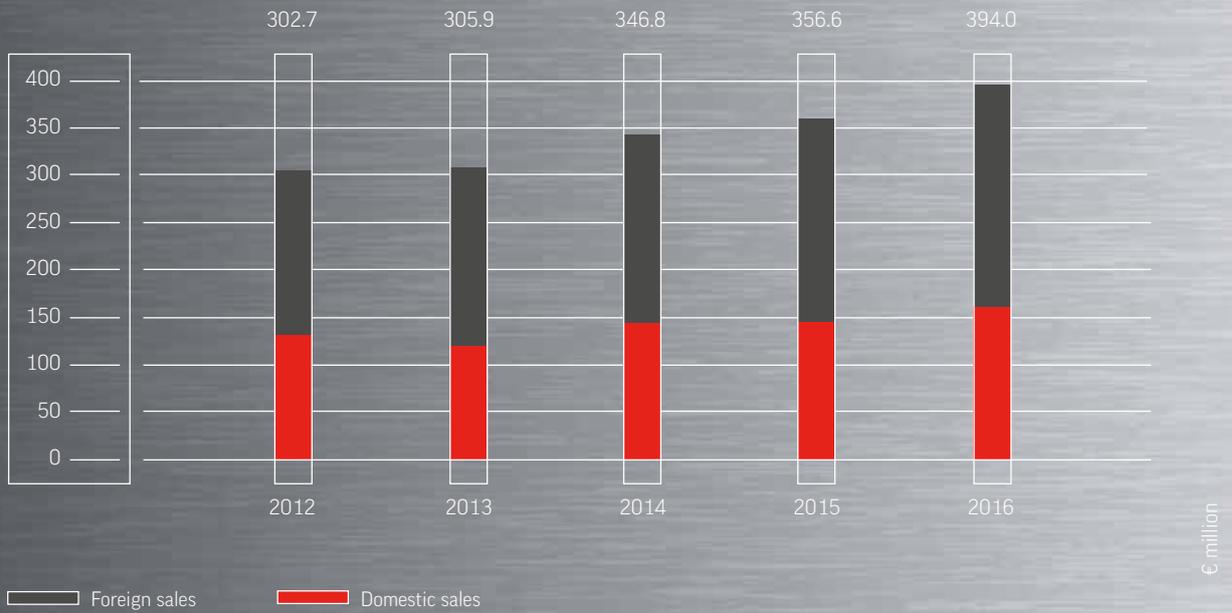
The sales growth, the high degree of capacity utilization and the continued high degree of efficiency of our processes resulted in a marked growth in earnings for 2016. The overall Group performance increased by 8.7 % to € 394.2 million, which is less than the growth in sales. In contrast to the previous year there was hardly any additional inventory build-up. Because of this, and also thanks to a stable price quality and value analysis optimizations, the cost-of-materials ratio decreased relative to the overall performance from 46.3 % to 43.4 %. Despite wage increases and a modest increase in employee numbers, the proportion of personnel expenses went down from 20.8 % to 20.4 %. Depreciation costs increased by 3.5 % to € 7.0 million. The balance from the other operating expenses and income was € -36.2 million after € -32.1 million in the previous year, because these expenses increased noticeably as a result of the business expansion.

In total, the Group-wide operating result for 2016 rose from € 80.4 million to € 99.8 million. Here it should be borne in mind that the EBIT of the previous year were affected by negative special factors from exchange rate fluctuations. Of the 2016 operating result (not taking consolidation effects into account), € 88.0 million (previous year € 74.0 million) were attributable to the domestic company segment, and € 12.2 million (previous year € 6.8 million) to foreign sales (the latter being influenced by one-off major projects.)

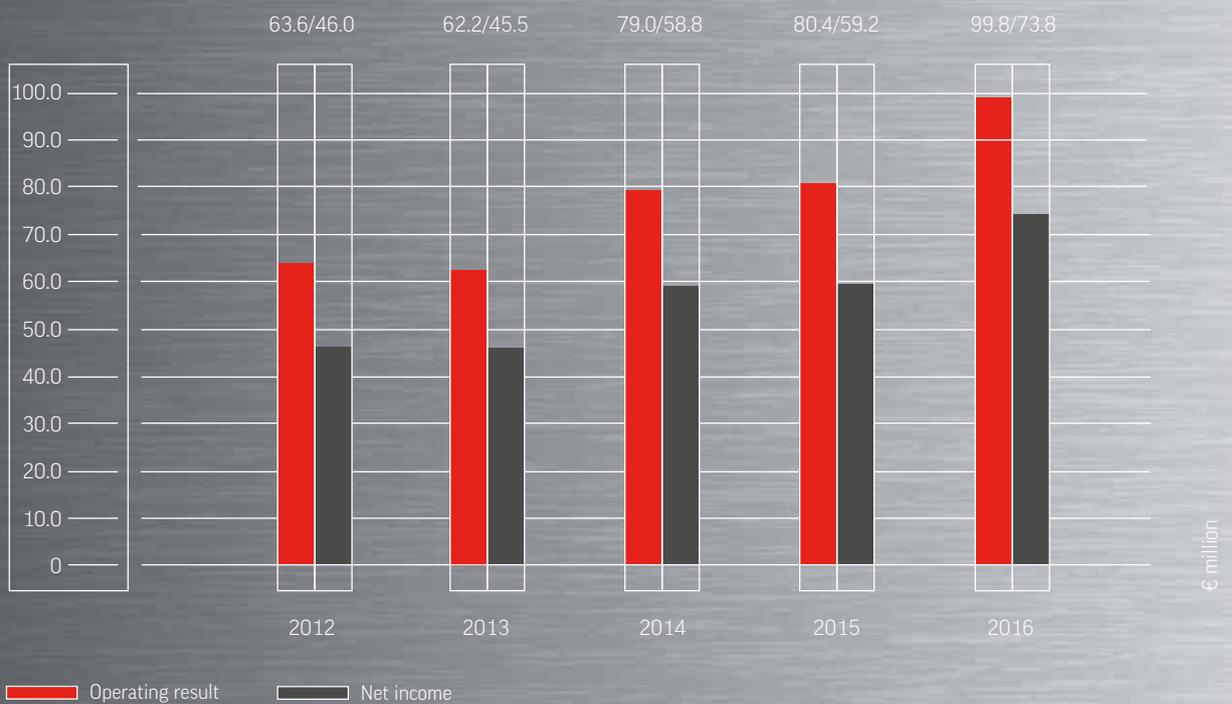
Including the financial result of € 0.5 m (previous year € 0.2 million), the Group earnings before taxes rose from € 80.6 million to € 100.3 million. This is equivalent to an improved gross sales margin of 25.4 % (previous year 22.6 %). After taxes, the Group net income was € 73.8 million, compared with € 59.2 million in the previous year. This result represents an increase per ordinary share of € 14.76 (previous year € 11.83) and per preference share of € 14.81 (previous year € 11.88).

The operating result for the individual company Hermle AG (calculated according to HGB regulations) grew from € 72.6 million to € 86.7 million, and the net income from € 54.5 million to € 64.6 million.

HERMLE GROUP SALES



HERMLE GROUP OPERATING RESULT AND NET INCOME



02.2

Management Report of the AG and Group Management Report

Financial management and financial situation: Operative cash flow greatly increased

The financial management of Hermle AG and the Group aims especially towards largely internal financing and securing our liquidity. Available funds are invested exclusively short-term and with low risk. The aim is normally to finance both the ongoing business operations and the investment projects 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 Hermle Group's robust liquidity situation improved further during the reporting period. Thanks to the large increase in profits, operating cash flow prior to the change in working capital increased from € 65.4 million to € 80.8 million. This growth was compensated by a significantly higher commitment of funds in the working capital, mainly due to higher trade accounts receivable. In the previous year, funds were released at this point. Therefore the cash flow from business activities reduced from € 76.3 million to € 74.0 million.

In the area of investments, high payments in connection with the two major construction projects that are described in the 'Production' section contrasted with funds released from short-term financial investments. These investments were in securities and fixed term deposits with terms of more than three months that according to IFRS accounting standards are to be declared as securities of the working capital. On balance, therefore, there was an outflow of only € 0.3 million (previous year € 19.4 million).

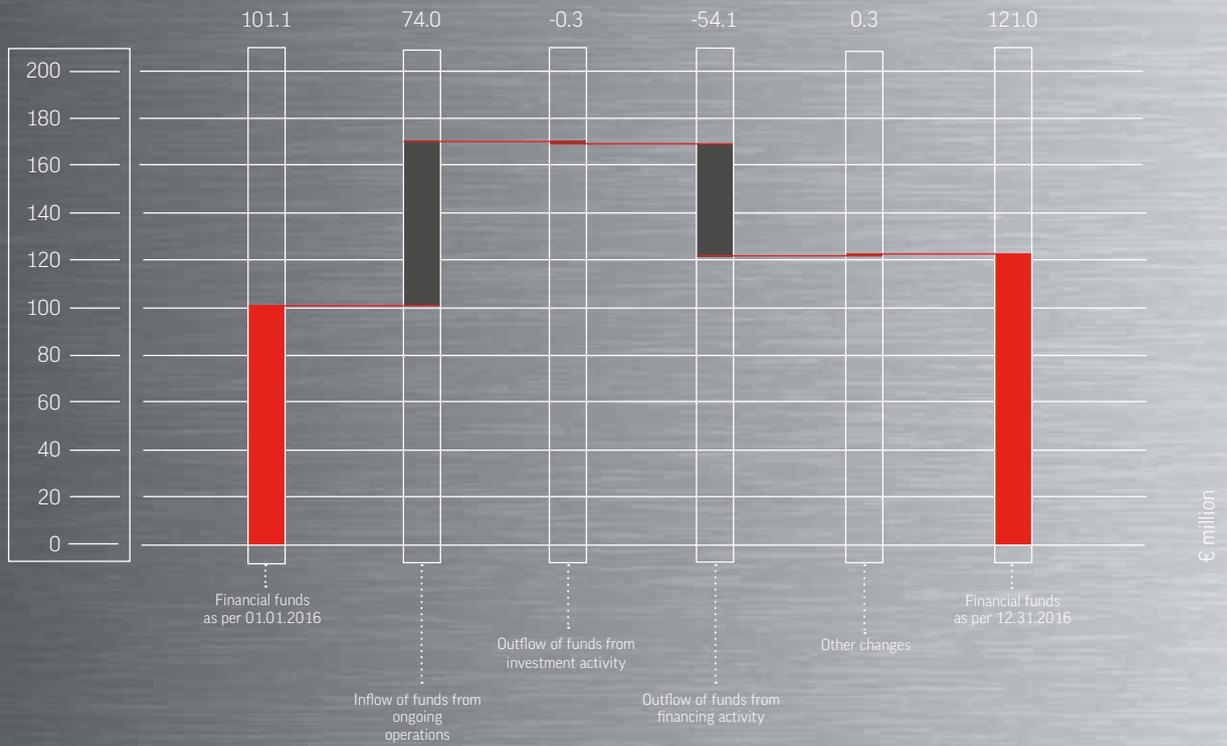
In 2016, the outflow of funds from financing activity was equal to the previous year at € 54.1 million, and involved the disbursement of the dividend. After taking into account changes linked to exchange rates and other minor changes, liquid funds at the accounting reference date increased from € 101.1 million to € 121.0 million.

Investments greatly enlarged to € 16.4 million

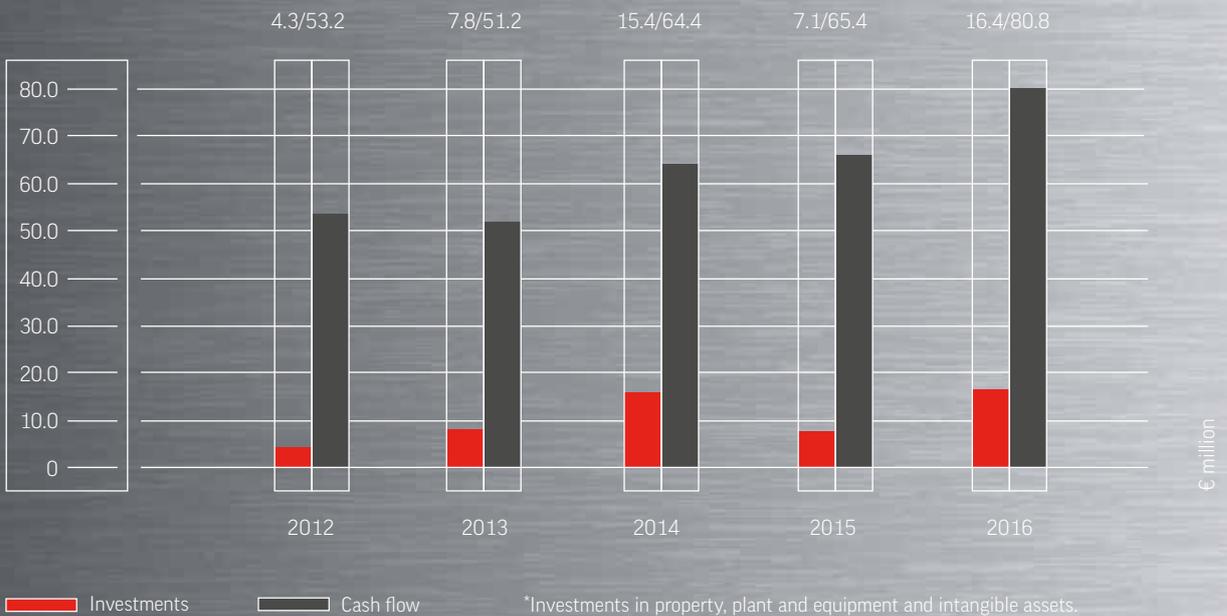
In 2016, the Hermle Group increased investments in property, plant and equipment and intangible assets from € 7.1 million to € 16.4 million. The main focus was on two major projects whose purpose is to ensure sufficient capacity for future growth. In one of the projects, at the company headquarters in Gosheim, an existing hall is being modernized and extended for metal-cutting manufacturing. The other one is being implemented at a new location in the neighboring district of Rottweil. A plot of land has been purchased and construction has begun on a new production building. The 'Production' section contains more information on these projects.

Investments made by Hermle AG increased by 154.4 % in 2016 to € 15.1 million, and these can largely be accounted for by the same projects as have been mentioned in the Group overview.

HERMLE GROUP CHANGE IN LIQUIDITY IN 2016



HERMLE GROUP CASH FLOW AND INVESTMENTS*



02.2

Management Report of the AG and Group Management Report

Net assets: Equity ratio rises to 74 %

As of December 31, 2016, the Group consolidated balance sheet of Maschinenfabrik Berthold Hermle AG extended by 7.4 % to € 309.6 million. On the assets side – specifically the long-term assets that rose by 17.0 % to € 61.7 million – the greatly increased advance payments and plant under construction in connection with the major projects made a large difference. This contributed towards the increase of 18.8 % in the fixed assets to € 56.9 million, while the intangible assets increased only a little, from € 1.2 million to € 1.5 million. The total current assets increased by 5.2 % to € 247.9 million. Because of the business expansion, the trade accounts receivable increased from € 49.9 million to € 58.6 million. In contrast, inventories dropped from € 55.7 million to € 53.5 million. The rise of the liquid funds from € 101.1 million to € 121.0 was largely offset by the reduction in fixed-term investments from € 26.0 million to € 10.6 million.

The greatest change in the liabilities was in the equity, which improved by 9.6 % to € 229.9 million thanks to the good results. This produces an equity ratio of 74.3 % (previous year: 72.8 %). At € 1.6 million, the long-term liabilities and provisions were insignificantly higher than the previous year figure of € 1.4 million. The short-term liabilities and provisions also changed only slightly, rising to € 78.1 million from € 77.2 million the year before.

Here, the business expansion meant that the short-term provisions increased from € 36.5 million to € 40.3 million, whereas the other short-term liabilities went down from € 32.0 million to € 29.3 million on account of lower advance payments for orders. At € 8.5 million, the trade accounts payable were similar to those of the year before.

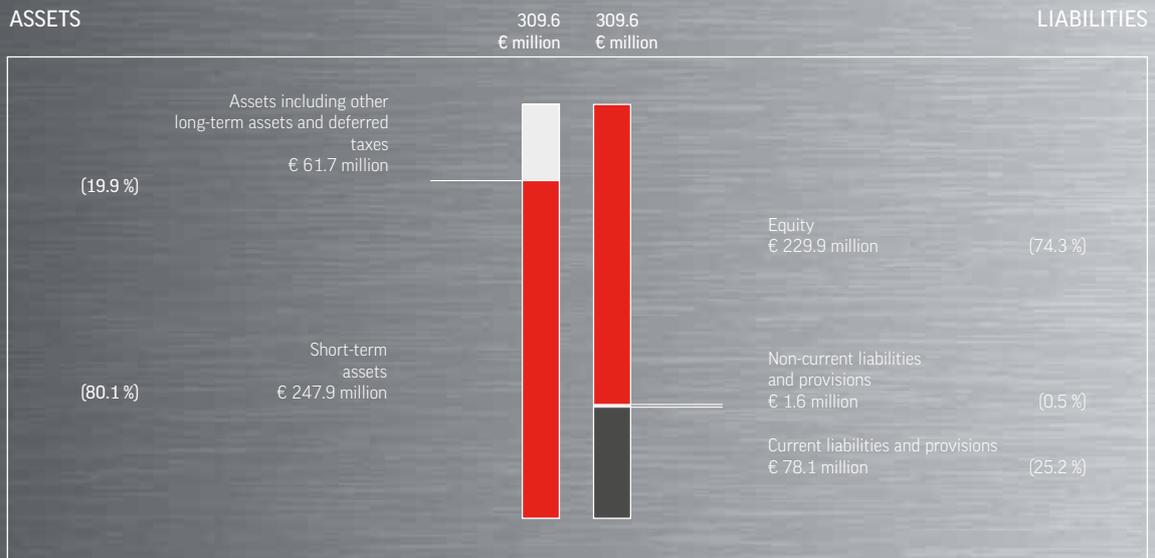
In an appointed day comparison, the balance sheet total of the individual company increased by 4.5 % to € 247.9 million (previous year € 237.1 million). Of this, 74.8 % (previous year 73,8 %) was equity capital.

Overall assessment of the economic situation and comparison with the forecast

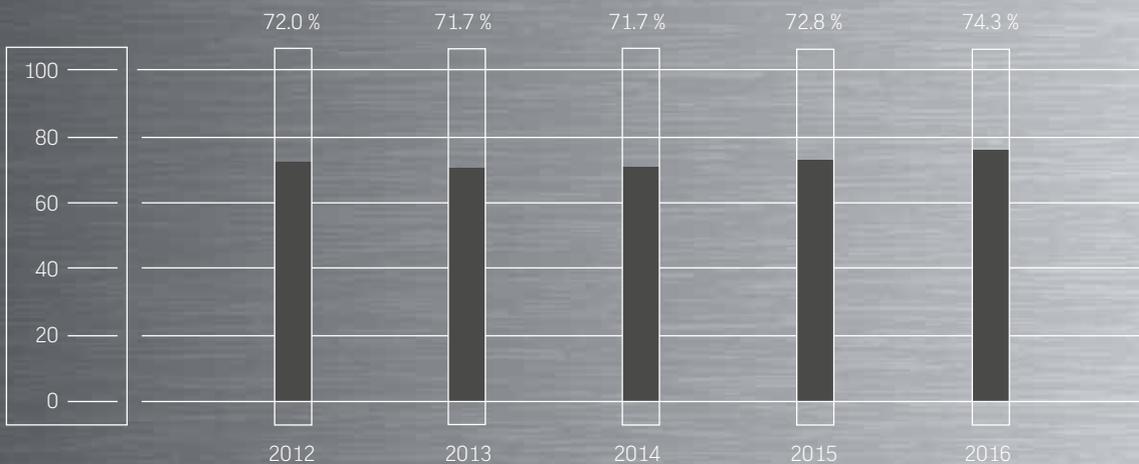
In 2016, Maschinenfabrik Berthold Hermle AG was able to defend its market position despite a still highly competitive climate, and achieved overall growth that was considerably better than expected. Over the Group as a whole, incoming orders rose by 1.0 % to € 364.5 million, although at the beginning of the year we had forecast a slight downturn. This effect was mainly influenced by recoveries on several markets, especially in southern Europe, as well as major projects that could not be anticipated. This was the basis on which both sales and the results increased more than had been predicted: The Group turnover increased by 10.5 % to 394.0 million euros, and the operating result from € 80.4 million to € 99.8 million. At the beginning of the year we reckoned with an increase in turnover in the region of 5 percent, and profits roughly at the same level as the previous year.

Thanks to the good income situation, the financial and net assets consolidated further and reached a very firm position, as anticipated. The operative cash flow increased to € 80.8 million, and the equity ratio to 74.3 %. Overall, the Board of Management considers the income situation, financial position and net assets of Hermle AG and the Group as being unusually good, this also applying at the time the statement was prepared.

HERMLE GROUP BALANCE SHEET STRUCTURE (12.31.2015)



HERMLE GROUP EQUITY RATIO



02.2

Management Report of the AG and Group Management Report

ADDITIONAL PERFORMANCE INDICATORS

Development: Machine innovations, automation and digitalization

In the course of the reporting period we pursued our intensive R&D activities further. Our focus remains on new machines, automation solutions and Industry 4.0 packages for differing market requirements. The high points of the Open House in April 2016 were the presentation of the C 62, the second generation of our largest machining center from the High-Performance Line, as well as the new C 250, a smaller version for starting up in 5-axis / 5-side machining that added to the Performance Line range. As the year progressed, the development focus shifted to innovative automation solutions such as the HS flex handling system and a new generation of spindles for machining especially hard materials such as stainless steels and tooling steels. We were also working on additional software modules for digitalizing our own manufacturing processes and those of our customers.

In the area of additive manufacturing, the development of special applications continued, such as the generation of special material properties through the combined application of different metals.

Production: Extending capacity

Hermle started on two major construction projects in the 2016 business year. On the one hand we have begun the modernization and expansion of the metal-cutting manufacturing facilities at the company headquarters in Gosheim. To this end, an existing older hall is being built over and then new technical plant will be installed during normal operation. The work began in August 2016 and is to be completed during 2017. With this undertaking, we are adjusting capacity to match the continued high level of demand, and making a firm statement in favor of the location Gosheim.

In addition, in view of the limited spatial and constructional room to maneuver at the head office location, a plot of land was purchased in the neighboring district at Zimmern ob Rottweil in May 2016 in order to keep options open for further growth. The new plot lies in an area specifically designated for industrial development, and is therefore not subject to limitations in terms of planning permission. After a brief period needed to obtain planning permission, we were able to start construction of a modern production hall as early as the fall of 2016. At first, it is planned to manufacture mineral-cast beds there, commencing in the second quarter of 2017. This will improve our position with regard to supply, and we will gain additional know-how for these strategically important components. In addition to this, there is enough space at the new location for other activities with new products and services.

Optimized logistics and supply reliability

In order to optimize our storage and logistics processes steadily and, for instance, shorten travel times, we commissioned a new high rack system in the course of the reporting period. From the procurement point of view, the main accent was on securing our high product quality standards and supply reliability. Despite the planned own production of mineral-cast machine beds, we will still obtain these components from external suppliers as well in order to guarantee sufficient supplies. We generally operate on a basis of long-term collaboration and trust with our suppliers, and therefore once again experienced no bottlenecks in the procurement of key components in the year under review.

Service and sales: Continued decentralization

To secure our position in the sector as acknowledged providers of high service quality and fast responders, we have augmented both our domestic and foreign service segments in 2016. In addition, the decentralization of service structures was pursued further.

As in the previous year, we presented our product portfolio at some 50 national and international trade fairs during the reporting period. Particularly significant were the Hermle Open House in April at the company headquarters, the IMTS (International Manufacturing Technology Show) in Chicago – the largest trade fair for machining technology in North America – and the AMB international exhibition for metalworking in Stuttgart, which both took place in September. We also organized a large number of workshops at the company headquarters in Gosheim, in our Technology and Training Center in Kassel-Lohfelden, at the US-American subsidiary as well as in the United Kingdom, in order to provide our customers with supplementary information about innovations and new technologies at Hermle.

Sustainability through a high degree of energy efficiency and resources conservation

As a member of the 'blue competence' initiative of the VDW trade association (German Machine Tool Builders' Association), Hermle has long been a champion of energy efficiency and conservation of resources, because it brings benefits both to our customers as well as to ourselves. We see both the manufacturing process as well as the products themselves as providing avenues of approach. Therefore on the one hand we employ sustainable production processes such as virtual machine development and optimization, low-energy component production, use of high-grade, long-life components, reducing transportation energy by manufacturing in a certain region, utilizing local sourcing, and practicing a very high degree of in-house fabrication. On the other hand, we also ensure that our machines are highly energy-efficient, for instance through the use of energy recovery systems, demand-tailored drive and cooling technology as well as a machine stand-by mode that lowers consumption.

Sustainability aspects also play a major role in construction and modernization measures. Thus the extension currently under construction in Gosheim not only saves space, but thanks to a new heating and air-conditioning concept as well as improved insulation it also uses less energy and noise emissions are lower. The new construction in Zimmern ob Rottweil is also being carried out according to the most recent sustainability principles.

Employees: 1,018 employees across the Group

Hermle employed 1,018 people at the end of 2016, which is 41 more than was the case at the beginning of the year. About half this increase, relatively low in relation to the business volume, was accounted for in the commercial sector. Here, many apprentices who successfully passed their final examinations were offered positions, and the vacant places were filled by new apprentices. New posts were also filled at Hermle Maschinenbau GmbH, the additive manufacturing specialist, both in the service segment and in catering. The number of people employed in production increased by 19 to 395, in administration by 5 to 69 and in the segments customer care, supplier care and R&D by 17 to 554 employees.

The yearly average number of people employed across the Group was 1009 (previous year 973), of whom 891 people (previous year 859) worked for the domestic companies and 118 (previous year 114) in foreign sales and service. This does not include the nearly 80 employees of the at-equity consolidated Hermle-Leibinger Systemtechnik GmbH.

02.2

Management Report of the AG and Group Management Report

Hermle AG offers its employees an attractive, modern working environment, entailing a high degree of personal responsibility within performance-oriented teams. We create additional incentives through an extensive range of training opportunities, primarily on specific specialist topics. This is also aimed at enhancing employee loyalty to the company. The average age of our workforce was 37 years in 2016 (previous year 36) and the average period of service at Hermle was 12.1 years (previous year 11.7).

A strongly motivated Hermle team

The high degree of motivation and technical competence of our workforce is an essential factor determining Hermle's success. In 2016, the overall performance per employee increased to €k 387.2 (previous year €k 371.0). Thanks to the high degree of capacity utilization, our employees' flexitime accounts were well filled up. This means that as a 'breathing company', Hermle can avail itself of substantial room to maneuver in future if years with less demand should lie ahead.

As in previous years, the Hermle AG employees are to participate in the company's success in 2016 by way of acknowledgment for their commitment and the good results. Therefore after the dividend has been paid out, each employee will receive a performance bonus amounting to 70 % of one month's salary, plus a fixed lump-sum payment.

More vocational training

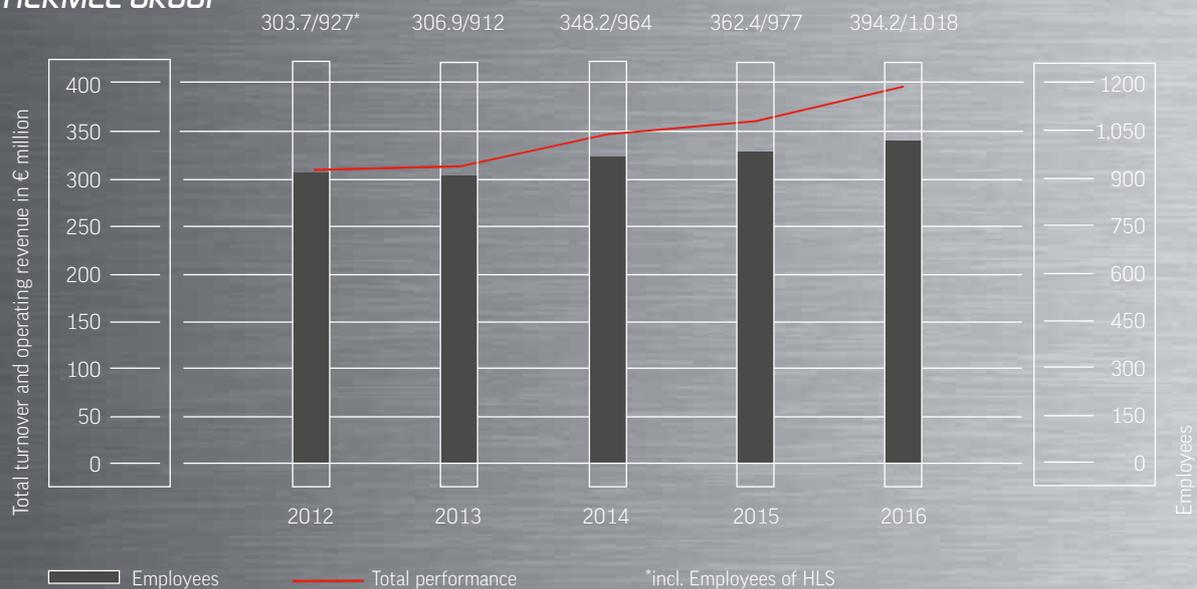
On December 31, 2016, 95 young people completed their training at Hermle (previous year 96). In relation to the whole Hermle AG workforce, which increased from 852 to 887 persons in the period under review, this represents a continuation of the high vocational training rate of 10.7 % (previous year 11.3 %).

Our trainees either embark on one of the many classical apprenticeships in modern technical and commercial vocations, or they start a dual course of study at Hermle. Right from the apprenticeship stage, they learn to work independently on selected projects within teams and to think in a holistic way about the business. In 2016, the courses offered were extended in the area of construction, amongst others, and the training workshop was upgraded with state-of-the-art technical plant such as an automated Hermle C 12 machining center and a 3D printer. We have also intensified cooperation with schools and exchanges with other companies regarding training projects.

Our outstanding commitment to training and development offers young people attractive career prospects in the region, as well as helping to safeguard the future of our business in view of the impending shortage of skilled staff.

As in previous years, we are striving to increase the number of women employed throughout the organization – particularly in technical and engineering professions, where the quota is currently around 6 %. 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). Consequently, it is our aim to consider women candidates more favorably when filling training places and recruiting new staff in technical areas, subject to their suitability for the post in question.

TOTAL TURNOVER AND OPERATING REVENUE AND STAFF NUMBERS AT THE HERMLE GROUP



SUPPLEMENTARY REPORT

Following the conclusion of the 2016 business year and until the moment when this report was signed, there were no events that had significant effects on the income situation, financial position and net assets of Hermle AG or the Group.

02.2

Management Report of the AG and Group Management Report

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. This enables Hermle to respond rapidly with countermeasures as required.

Presentation of key risks

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

Market and economic risks – In our view, the uncertain macroeconomic conditions, deriving from wide-ranging political and economic imponderables, pose a high risk that has increased in 2016. Any deterioration in the economic boundary conditions may exacerbate the already marked and fast-changing cycles in our industry. In addition to the still critical economic situation in some southern European countries, and the growing differences within the EU, we are also keeping a close eye on developments in Russia affected by political tensions, sanctions, and the general weakness of the economy. These factors might both directly and indirectly impose additional burdens on Hermle. The Brexit vote and the change in the US-American administration also carry incalculable risks. 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 limited by means of appropriate contract framing and insurance cover.

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.

Personal 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 attractive 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 therefore consider personnel risks to be low.

Procurement risks – To avoid procurement bottlenecks, Hermle selects suppliers carefully and cooperates with them fairly and generally on a long-term basis. 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 increased uncertainty regarding energy supplies resulting from Germany's move away from nuclear power and its energy transition policies by operating our own combined heat and power (CHP) plants.

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.

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 hedging operations, which are described in detail in the Group Notes to the financial statements in Item 30.

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.

02.2

Management Report of the AG and Group Management Report

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 therefore well prepared to exploit economic upturns.

An economic upturn would also boost our customers' business. That, in turn, presents greater sales opportunities for our products, because our customers would then normally require highly efficient and reliable machines such as those manufactured by Hermle.

Also, the trend towards digitalization and automation in manufacturing – Industry 4.0 – provides Hermle with further expansion potential, because only high-quality, extremely reliable machines come in to question here.

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 higher-standard machining centers to them.

Opportunities deriving from the company's strengths – The high skill levels and outstanding commitment of Hermle's workforce underpin the success factors of flexibility and quality already cited among the external opportunities, thereby consolidating 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 through credible service provision.

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. Moreover, the high reliability of our machines together with our regularly updated and demand-oriented product portfolio, incorporating continual innovations, are improving the opportunities for additional applications of our machines by existing and new customers alike. 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.

Moreover, 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

Considerable global economic uncertainty

In the opinion of the International Monetary Fund, the global economy can be expected to experience something of an upturn in 2017, growing by about 3.4 %. The main contribution to this is expected to come from the developing and newly industrialized countries. Despite a slight downturn in the Chinese economy, the IMF forecasts an overall GDP increase of around 4.5 % for them. Thanks to the recovery in raw materials prices, Brazil and Russia will probably weather the recession, and a greater degree of dynamism is also anticipated for India. The IMF forecasts an average upturn of 1.9 % for the industrialized nations, fueled mainly by resurgences in the USA and Canada. A moderate slowdown is forecast for the euro area, and this will be more pronounced for the United Kingdom. All in all, the IMF accentuates that the degree of uncertainty is generally unusually high. Especially the continued development in the USA and the United Kingdom, and the knock-on effects on other national economies, are very difficult to predict.

In the opinion of the German Council of Experts, the German gross domestic product will increase by only 1.3 % in the coming year, which will mainly be due to a calendar effect, however.

A sound sector environment

The German Mechanical Engineering Industry Association (VDMA) is relatively optimistic about the prospects for the machine and plant construction sector. In spite of many risk factors, it reckons with slight growth in the important sales region of the USA, China, Japan and Europe, so that global sales of machines can be expected to increase by 2 % in 2017. In view of this, German machine and plant manufacturing will probably expand by 1 %. From the current perspective, exports to the newly industrialized countries Brazil and Russia and to the other euro countries, as well as domestic business, will show slight positive growth. In contrast, the VDMA considers it to be very difficult to forecast the demand that will come from the United Kingdom and the USA in view of changes that may be under way.

According to the VDW, German machine tool manufacturers will increase their production by 3 % in 2017. The sector trade association bases this estimate on the probable positive progress of global demand for machine tools, as well as a respectable volume of orders on hand.

Hermle expects sales and profits to normalize

During the first weeks of 2017, Hermle's business progressed steadily and as predicted. In contrast to the extraordinarily good performance during the previous year, the results for 2017 altogether may be expected to normalize, especially in view of the significantly lower number of orders on hand at the beginning of the year. This is exacerbated by the many imponderables with which many of our customers are faced, and which may lead to a degree of investment reluctance. The uncertainties associated with Brexit and the new administration in the USA, the strained financial situation of several southern European countries, growing political differences within the EU and the later consequences of Dieselgate all make their various contributions. Our business may also be adversely affected by increased trade restrictions on exports to countries like China, Russia and Turkey. Despite the official relaxation of export restrictions to Iran, the fact that practical restrictions still remain means that genuine export opportunities are not to be expected in the short term.

In view of this, we think it is possible that incoming orders and turnover in the Hermle Group will go down to a figure in the region of 5 percent, or perhaps towards 10 percent, and the profits will decrease disproportionately, mirroring the large upturn

02.2

Management Report of the AG and Group Management Report

of the previous year. Such a development – which we would regard as being still satisfactory – is forecast on the assumption that our economic boundary conditions will be essentially as the trade associations are anticipating.

Financial and net assets position remains sound

In the coming year, Hermle's position from the financial and net assets point of view will consolidate further thanks to the clearly positive result that is to be anticipated. This means that, as far as can be forecast from the current perspective, our company can continue to finance investment projects and operative business using its own resources and without bank liabilities.

High investment volume again

In 2017, the modernization of the metal-cutting manufacturing facilities and the new machine bed production plant in Zimmern ob Rottweil will continue to account for the lion's share of investment funds. Both major projects are scheduled for completion in 2017. Looking beyond this, we are planning to extend metal-cutting manufacturing with an additional large machining center.

Modest increase in workforce

The number of people employed in the Hermle Group will probably go up a little in 2017. Much of this increase will be attributable to the new Zimmern location. As was the case in previous years, the company intends to take on apprentices who have completed their training successfully and to refill the positions as they become vacant.

Strategically important development activities

Innovation is of strategic significance for Hermle's success. Therefore our activities in the area of R&D will be pursued energetically also in 2017. The main accent is on new machine models for various market segments as well as supplementary automation and digitalization solutions. The area of additive manufacturing remains in focus as well. We shall be presenting our new products to experts at the Hermle Open House in April 2017 and at various domestic and foreign trade fairs.

Overall assessment of the future development

In the Board of Management's opinion, Maschinenfabrik Berthold Hermle AG's business and that of the Group as a whole will normalize and continue to develop steadily in 2017. In our estimation, a return to normality following the exceptionally good previous year is likely in view of the considerably lower number of orders on hand and major uncertainties in Hermle's area of activity. We anticipate Group sales to go down by around 5 % or perhaps by a figure closer to 10 %. We expect the uncertain situation to lead to reluctance on the part of our customers regarding investments. Therefore the number of incoming orders will probably go down in line with sales. Thanks to our policy of maintaining a 'breathing company', we are suitably prepared for the economic fluctuations that are common in our sector. The continuing, very stable financial and net asset situation provides a firm foundation for the planned investments connected with the two major projects. Altogether, the Board of Management considers the company to be well set up to maintain successful development in the coming years.

02.3

The Hermle Share

Stock markets only come to life towards year's end

For the stock markets around the world, 2016 began in a muted way. Investors were especially keeping an eye on the Chinese economy, on growing geopolitical tensions and on uncertainty surrounding the monetary policy being pursued by the US Federal Reserve. The markets began to liven up from the second quarter onwards, until they were unsettled again by the unexpected outcome of the Brexit referendum. Then a degree of confidence returned for a few months following the publication of encouraging labor market data in the USA, a relatively robust Chinese economy contrary to predictions, and a recovery in raw material prices. Many indices picked up surprisingly well after the Presidential election in the USA. This included the DAX, which increased in value by 6.9 % over the whole year following a final sprint towards the end of 2016. The CDAX, reflecting the development of all German stocks in the Prime Standard and General Standard sectors, gained 6.5 %.

PRICE DEVELOPMENT OF THE HERMLE SHARE FROM JANUARY 2014 TO MARCH 2017



02.3

The Hermle Share

Hermle share significantly higher

The Maschinenfabrik Berthold Hermle AG preference share began the year 2016 modestly, moving sideways during the first quarter from the end-of-year price of € 214.10. It reached the low point for the year on February 8, 2016, with a price of € 198.00. The second quarter saw the share begin a sharp rise that continued until the fall, where it culminated in the year's peak price of € 306.15 on November 8, 2016. After this, the share lost ground until it reached the year's closing price of € 271.00. This represented an increase in value for Hermle's preference share of 26.6 % during the year under review.

Profit per share rises sharply

On the basis of the unusually good business development during 2016 – Group sales increased by 10.5 % to € 394,0 million and the net income from € 59.2 million to € 73.8 million – the key share figures improved significantly: The profit per preference share rose from € 11.88 to € 14.81, yielding a price-earnings ratio of 18.30 in relation to the 2016 year-end closing price. Cash flow per share increased to € 16.15, and shareholders' equity to € 45.99 per share.

Dividend to be increased to € 12.85

At the parent company Hermle AG, the net income grew from € 54.5 million to € 64.6 million. The balance sheet profit (net earnings) totaled € 64.1 million in 2016. The Board of Management and the Supervisory Board will recommend on July 5, 2017, that the basic dividend should remain unchanged at € 0.85 for each preference share and € 0.80 for each ordinary share, and that a bonus of € 12.00 (increased from € 10.00 the year before) be disbursed for each share. This means that the dividend per preference share would increase from € 10.85 to € 12.85.

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.

KEY HERMLE PREFERENCE SHARE DATA (IN €)

	2012	2013	2014	2015	2016
Result per preference share ¹	9.29	9.17	11.79	11.88	14.81
Cash flow ¹	10.71	10.30	12.85	13.08	16.15
Shareholders' equity ¹	35.30	37.03	40.55	41.96	45.99
High ²	93.50	168.00	188.45	224.00	306.15
Low ²	70.02	93.30	144.42	160.00	198.00
Closing price ²	91.50	150.80	161.53	214.10	271.00
Year-end profit ratio	9.85	16.44	13.72	18.02	18.30
Year-end cash flow price ratio	8.54	14.64	12.57	16.37	16.78
Dividend per preference share	0.85	0.85	0.85	0.85	0.85 ³
Bonus	7.20	7.20	10.00	10.00	12.00 ³
Price on Friday, March 31, 2017					296.00

¹ Share basis up to 2012: 4,971,847 shares (therefore diluted result)
Share basis from 2013: 5,000,000 shares

² Source: Stuttgart Stock Exchange

³ Subject to approval at the annual general meeting

Corporate governance and transparency

The 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. This aim is founded on our own corporate governance concept, which in turn is grounded in legal standards, the rules of procedure of the Management Board and Supervisory Board, as well as individual rules and regulations. The declaration pursuant to Section 161 on corporate governance of the German Stock Corporation Act is printed on pages 80 ff of this Business Report.

For Hermle, good corporate governance includes transparent and responsible communication.

Our shareholders, potential investors, the financial press and other financial market stakeholders are to be informed about the progress of our business and important events rapidly and on an equal footing. To this end, we make use particularly of the annual and half-yearly reports, intermediate communications, press releases and ad-hoc notices. These publications, as well as comprehensive background information about the company and its products, are available on our newly refurbished website www.hermle.de. On the occasion of the annual general meeting, we also provide our shareholders with an opportunity to get to know the company at first hand through factory visits.

02.4

The Investment Projects and Innovations

The Maschinenfabrik Berthold Hermle AG is firmly rooted in its home base in south-west Germany. We are investing heavily in the region - with the extension of the company headquarters location, with additional real estate and with state-of-the-art, digitally networked production plant. At the same time, we regularly develop trailblazing innovations for the machine tool industry at Gosheim, emphasizing our technological lead in 5-axis machining.

Extension of production facilities at the company headquarters

In response to the rising levels of business and the increasing size of machines, the facilities at our headquarters location in Gosheim are growing to match. We are extending and modernizing our capacity with a keen eye to future developments. This means major projects at regular intervals. In 2016, we started work on extensions for the metal-cutting manufacturing segment, which is one of our most important strategic production areas. This means not only extended facilities, but also the installation of a new, high-performance large machining center.

In addition to the more than 2,300 m² of new production space, a 700 m², cutting-edge technology center for energy-efficient air conditioning for the entire production hall is planned.

In order to save space and for reasons of sustainability, we are doing this by building over an existing complex. Specifically, we are raising the height of one of the oldest manufacturing halls from 5.0 m to 12.5 m. It proved possible to use the three-week vacation close-down in 2016 to erect the new building shell. The following installation work and construction of plant such as the air conditioning, compressed air and chip removal equipment, on the other hand, will be carried out in parallel with normal production, with completion by the 2107 vacation. Then we shall remove the roof and the other parts of the building that are serving to safeguard the normal operations in the meantime.



New location for future expansion

The options for further extension of the Gosheim facilities are limited by sheer lack of space and also the proximity of a residential area. Therefore in May 2016 we purchased a plot of land about 4 hectares in size in the neighboring district of Rottweil that will provide us with room to grow during the coming decade, while at the same time securing Hermle's future in Gosheim. The new location in Zimmern ob Rottweil has many advantages: It is close to headquarters, has easy access to the freeway and it extends our 'catchment area' for additional qualified employees. As the new location in Zimmern is in a newly developed, dedicated industrial and commercial area, we also have an excellent infrastructure and, in contrast to Gosheim, there are few restrictions in terms of planning permission.



Planning permission was granted in a short space of time, so construction could already start in September 2016 for a new production hall with over 3,000 m² of space and a height of 22 m, as well as an administrative building next door. The buildings are equipped with state-of-the-art heat pumps and air conditioning plant. To start with, we shall be manufacturing mineral-cast machine beds in Zimmern, in other words the foundations for our machining centers that we have so far always obtained from other suppliers. This will enable us to gather our own know-how in this important area, while improving our supply reliability through the combination of own production and third-party production. After the large mixing plant silos for the mineral casting had been installed, the building was completed in the first quarter of 2017. The work is running on schedule, so we will probably be able to start manufacturing as early as the second half of the year. In addition to this, we have plenty of space for other activities with new products and services.

02.4

The Investment Projects and Innovations

Industry 4.0 components for customers and our own production

Automated, digitally networked and to some extent self-controlling production steps have been part of Hermle's daily routine for many years now. Digital interfaces underpin our procedures from order processing and production planning to metal-cutting manufacturing to assembly. The accent here is on 'support', for the ultimate control and supervision devolves on the Hermle employees. Digitalization comes as an aid to them, for instance by providing clarity when it comes to decision-making.

We develop some of the digital components that we use in our own manufacturing, and provide them to our customers as well. The combination of Hermle machines and automation components makes for an intelligent manufacturing cell. When networked with a superordinated manufacturing system, this represents an important step towards the smart factory.

In 2016, we developed a number of innovations in this area: For instance, HACS Connect represents an extended version of the Hermle Automation Control System (HACS) for controlling and monitoring our automated machining centers: It has been combined with the Hermle 'Information Monitoring Software' (HIMS). HIMS provides the user with status information and current machine events on the medium of choice: PC, tablet or smartphone. In addition to this, we provide a new maintenance diagnosis system that can be used via HIMS. It allows the user to plan maintenance work across machines, with direct access to the control system and operating manual. There is also the so-called Remote Desktop Manager that allows for any PC user interface to be displayed on the machine's control screen.



Innovative automation and spindle technology

Machine technology remains at the focus of our innovation work. As part of the Open House in April 2017, we presented our new HS flex handling system to our customers: an economical, entry-level solution for automating our machining centers. The space-saving system with up to two individually configurable pallet storage units can be combined in many different ways to cope with a broad range of parts. HS flex does not need to be anchored to the ground, so it can be quickly and easily set up and put into operation. HS flex can be adapted to the Performance Line machines and four versions of the High Performance Line.

We already introduced a new generation of spindles for machining especially hard stainless and tooling steels to the market in 2016. Materials such as Inconel and titanium nitride – used mainly in the aerospace industry – can be machined as well. These heavy machining spindles have higher torques and cutting force, as well as larger spindle bearings. They have been developed for High Performance Line machines.

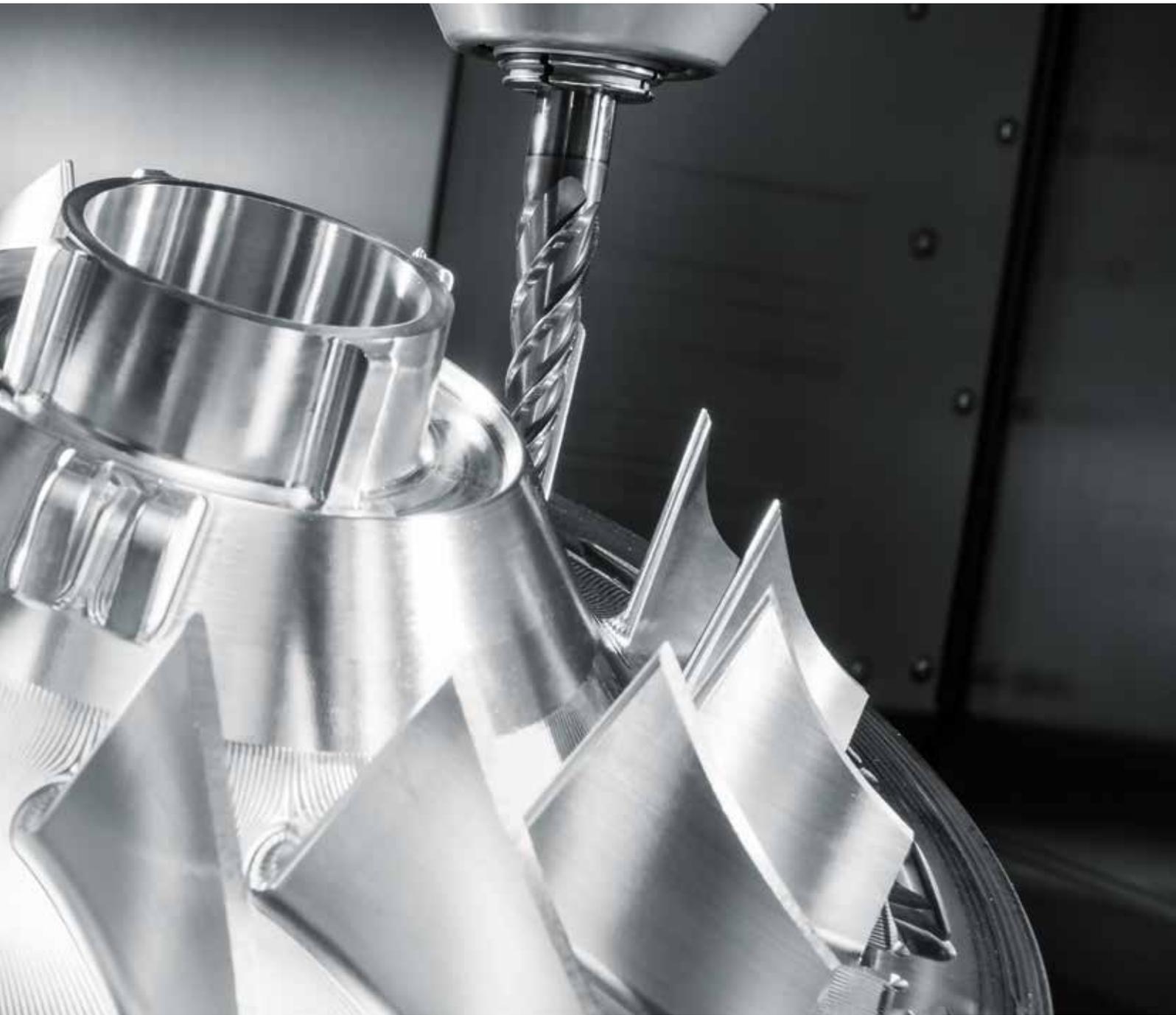


03

Consolidated Financial Statement



Automotive engineering. Fan propeller.



Automotive engineering. Aluminum fan propeller for a tractor engine.
After surface reconstruction, the new component is manufactured by means of complex 5-axis simultaneous machining in a single clamping operation.

03.1

Group Balance Sheet

ASSETS	Notes to the financial statements	31.12.2016 €k	Previous year €k
A. Long-term assets			
I. Intangible assets	(7)	1,462	1,187
II. Property, plant and equipment	(7)	56,949	47,938
III. Shares in companies valued using the at equity method	(7)	1,012	999
IV. Other financial assets	(7)	5	5
V. Other long-term assets	(8)	61	621
VI. Deferred tax assets	(25)	2,155	1,919
		61,644	52,669
B. Short-term assets			
I. Inventories	(9)	53,547	55,749
II. Accounts receivable from trading	(10)	58,640	49,915
III. Other short-term assets	(10)	4,130	2,932
IV. Securities and other assets	(11)	10,610	26,007
V. Cash and cash equivalent	(12)	120,992	101,074
		247,919	235,677
TOTAL ASSETS		309,563	288,346
LIABILITIES		31.12.2016 €k	Previous year €k
A. Equity			
I. Equity of shareholders of Hermle AG	(13)	229,924	209,784
II. Interests of other shareholders	(14)	16	12
		229,940	209,796
B. Non-current liabilities and provisions			
I. Other long-term assets	(16)	65	0
II. Long-term provisions	(15)	1,351	1,087
III. Deferred tax liabilities	(25)	140	272
		1,556	1,359
C. Current liabilities and provisions			
I. Current trade payables	(16)	8,466	8,671
II. Other short-term liabilities	(16)	29,317	32,008
III. Tax provisions	(15)	2,842	4,058
IV. Short-term provisions	(15)	37,442	32,454
		78,067	77,191
TOTAL LIABILITIES		309,563	288,346

03.2 Consolidated Income Statement

	Notes to the financial statements	2016 €k	Previous year €k
Sales	(17)	393,950	356,633
Change in stock of finished and unfinished products		-4	3,626
Other own work capitalized		248	2,224
Total turnover and operating revenue		394,194	362,483
Other operating income	(18)	9,432	10,850
Material costs	(19)	170,927	167,810
Personnel expenses	(20)	80,297	75,400
Depreciation on intangible assets, and plant and equipment	(21)	6,974	6,738
Other operating expenses	(22)	45,627	42,985
		303,825	292,933
Operating result		99,801	80,400
Result from companies valued using the at equity method	(23)	331	317
Other financial result	(24)	180	-99
Financial result		511	218
Earnings before taxes		100,312	80,618
Taxes on income	(25)	26,463	21,437
Net income		73,849	59,181
Profit shares of other shareholders		-4	-2
Profit share of Hermle AG shareholders		73,845	59,179
Result per share in €	(26)		
Per ordinary share		14.76	11.83
Per preference share including dividend preference		14.81	11.88

03.3

Group Overall Income Statement

	2016 €k	Previous year €k
Net income pursuant to income statement	73,849	59,181
Other total income		
Items that may subsequently be reclassified to the income statement		
Currency changes	472	1,542
Changes from derivative financial instruments	-173	398
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	46	-105
- Tax on changes from financial instruments available for sale	0	0
Total income tax on other overall income	46	-105
Other overall income after tax	345	1,835
Overall income	74,194	61,016
Shares of other shareholders in overall income	4	3
Shares of shareholders of Hermle AG in overall income	74,190	61,013

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
Status as per 31 Dec. 2014	12,000	3,000	3,286	1,749	100,521	81,892
Dividend for previous year according to shareholders' meeting resolution						-54,050
Net income 2015						59,179
Allocations to revenue reserves as per Art. 16(3) of articles of association					500	-500
Exchange rate changes						
Cash flow hedges						
Other changes						-10
Status as per 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
Annual surplus 2016						73,845
Allocation to revenue reserves as per Art. 16(3) of articles of association					1,000	-1,000
Exchange rate changes						
Cash flow hedges						
Other changes						
Status as per 31 Dec. 2016	12,000	3,000	3,286	1,749	102,021	105,306

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
184,162	826	-443	0	202,831	1	8	202,840
-54,050				-54,050			-54,050
59,179				59,179		2	59,181
	1,541			1,541		1	1,542
		293		293			293
-10				-10			-10
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

03.5

Group Cash Flow Statement

	2016 €k	Previous year €k
Net income	73,849	59,181
Depreciation on assets	6,974	6,738
Change in long-term reserves	264	-162
Profit shares in joint companies	-331	-317
Cash flow before change in working capital	80,756	65,440
Elimination of after tax result from investment disposals	-171	-946
Commitment of funds / release of funds		
Inventories	2,202	-5,316
Accounts receivable from trading	-8,725	16,774
Other short-term receivables	-1,198	632
Deferred tax assets and other non-current assets	324	366
Short-term trade accounts payable	-205	-355
Short-term provisions	3,772	-821
Other short-term liabilities	-2,691	581
Non-current financial liabilities	65	-17
Deferred tax liabilities	-132	-20
Inflow of funds from ongoing business activity	73,997	76,318
Disbursements for investments in property, plant and equipment	-15,545	-6,756
Proceeds from the disposal of property, plant and equipment	474	1,378
Disbursements for investments in intangible assets	-895	-371
Proceeds from the disposal of intangible assets	0	0
Dividends received from joint ventures	319	245
Disbursements for the purchase of third-party securities and other assets	-10,610	-26,007
Proceeds from the sale of outside marketable securities and other assets	26,007	12,142
Outflow of funds from investment activity	-250	-19,369
Funds raised / funds released from		
sale (+) / purchase (-) of treasury shares	0	0
disbursement of dividends	-54,050	-54,050
Outflow of funds from financing activity	-54,050	-54,050
Exchange rate-related value changes*	348	1,218
Change from direct charging without affecting the operating result*	-127	293
Other changes*	0	-10
Change in funds	19,918	4,400
Funds as per 01.01.	101,074	96,674
Financial funds as per 31 Dec.	120,992	101,074

* See equity statement and statement of asset additions and disposals

03.6

Segment Reporting

	Domestic companies	Operations abroad	Consolidation financial effects	Consolidated statement IFRS
	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
Various 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
	2015 €k	2015 €k	2015 €k	2015 €k
Sales with third parties	237,280	119,353		356,633
Operating result	74,033	6,778	-411	80,400
Share in profit for the period of companies valued at equity	317			317
Net income	55,249	4,990	-1,058	59,181
Long-term segment assets	47,999	4,670		52,669
Various Book value of the companies valued using the at equity method	999			999
Short-term segment assets	191,483	54,256	-10,062	235,677
Segment assets (Total assets)	239,482	58,926	-10,062	288,346
Segment debts including provisions	57,612	30,067	-9,129	78,550
Capital investments	6,431	706	-10	7,127
Depreciation	5,885	853		6,738
Employees annual average	859	114		973

See explanations in Notes to the financial statements (28)

03.7

Group Statement of Asset Additions and Disposals 2016

	Acquisition and manufacturing costs				
	Status as per 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. Fixed assets					
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 loans	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	
	Status as per 31 Dec. 2016 €k	Status as per 01.01.2016 €k	Additions €k	Retirements €k	Transfers to other accounts €k	Currency adjustments €k	Cumulated depreciation €k	Status as per 01.01.2016 €k	Status as per 31 Dec. 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

03.8

Group Statement of Asset Additions and Disposals 2015

	Acquisition and manufacturing costs				
	Status as per 01.01.2015 €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 to such rights and values	5,790	290	100	4	1
2. Capitalized development expenses	3,036	81			
	8,826	371	100	4	1
II. Fixed assets					
1. Land, leasehold rights and buildings including the buildings on non-owned land	52,529	326	541 ⁽²⁾		331
2. Technical equipment, plant and machinery	39,104	3,070	2,188	6	65
3. Other plant, operating and business equipment	24,179	2,942	1,795	-4	223
4. Advance payments on property, plant and equipment	13	418	6	-6	
	115,825	6,756	4,530	-4	619
III. Financial assets					
1. Shares in companies valued using the at-equity method	927	72 ⁽¹⁾			
2. Other loans	5				
	932	72			
Total I. to III.	125,583	7,199	4,630	0	620

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

⁽²⁾ The retirements relates to a retrospective price reduction for the production building capitalized in the previous year.

		Depreciation						Residual book value	
	Status as per 12.31.2015 €k	Status as per 01.01.2015 €k	Additions €k	Retirements €k	Transfers to other accounts €k	Currency adjustments €k	Cumulated depreciation €k	Status as per 01.01.2015 €k	Status as per 12.31.2015 €k
	5,985	4,972	318	100	4	2	5,196	818	789
	3,117	2,397	322				2,719	639	398
	9,102	7,369	640	100	4	2	7,915	1,457	1,187
	52,645	20,322	1,763			82	22,167	32,207	30,478
	40,057	30,773	1,701	1,902		56	30,628	8,331	9,429
	25,545	16,803	2,634	1,656	-4	156	17,933	7,376	7,612
	419							13	419
	118,666	67,898	6,098	3,558	-4	294	70,728	47,927	47,938
	999							927	999
	5							5	5
	1,004							932	1,004
	128,772	75,267	6,738	3,658	0	296	78,643	50,316	50,129

03.9

Group Notes to the 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 statement of Maschinenfabrik Berthold Hermle AG was prepared pursuant to International Financial Reporting Standards (IFRS), as applicable in the European Union (EU), and in compliance with the supplementary commercial requirements pursuant to Section 315a(1) HGB. In that respect, all applicable standards, concepts and interpretations that were mandatory on the balance sheet 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 balance sheet date Saturday, December 31, 2016.

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 Board of Management of Maschinenfabrik Berthold Hermle AG released the consolidated financial statements on Thursday, March 30, 2017 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 2016 business year. Their application is mandatory for business years that commence on Friday, January 1, 2016.

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

IAS 19:	Performance-oriented plans: Employee benefits (amendments)
IFRS 2010-2012:	IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38 (amendments)
IFRS 11:	Statement presentation of the acquisition of shares in joint activities (amendments)
IFRS 16, IAS 38:	Clarification of acceptable depreciation methods (amendments)
IFRS 16, IAS 41:	Agriculture: Bearer plants (amendments)
IFRS 2012-2014:	IFRS 5, IFRS 7, IAS 19 and IAS 34 (amendments)
IFRS 10, IFRS 12, IAS 28:	Investment companies: Applying the consolidation measures
IAS 1:	Disclosure Initiative

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

IFRS 9 'Financial instruments' is to be used in business years that start on or after January 1, 2018. It may be applied earlier, but this is not planned in the Hermle Group at present. 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. A preliminary assessment suggests that this will have no significant effect on the consolidated financial statement.

IFRS 15 'Revenue from contracts with customers' is to be used in business years that start on or after January 1, 2018. It may be applied earlier, but this is not planned in the Hermle Group at present. 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.

On conclusion of contract, it is to be determined whether the revenue resulting from the contract is to be recognized at a certain point in time or over a period of time. On the basis of certain criteria, it is to be clarified whether the control over the performance obligation is passed over a period of time. If this is not the case, then the revenue is to be recognized at that point in time when the control passes to the customer. Indicators for this are, for instance, the legal transfer of title, the transfer of significant risks and rewards and formal acceptance. Should, however control be passed over a period of time, the revenue may only be recognized over that period insofar as the progress of performance can be reliably determined using input or output oriented methods.

The Hermle Group satisfies performance by the sale of machine tools and the associated services. For contracts in which the sale of machine tools represents the sole performance obligation, the new regulations will probably have no significant effect on the consolidated financial statement. For contracts concerning the provision of services, a preliminary assessment suggests that such services are provided over a period of time, as the customer simultaneously receives and consumes all of the benefits provided by the performance. In the context of contracts with a combination of different performance types, the identification of the individual performance obligations, the transaction prices that apply in each case and the point in time of the revenue recognition may, in principle, lead to shifts in the revenues and consequently also in the respective, project-specific margin in subsequent periods. Nevertheless, a preliminary assessment suggests that this will have no significant effect on the consolidated financial statement.

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 16:	Leasing contracts
IFRS 10, IAS 28:	Sales or contributions of assets between an investor and its associate/joint venture
IAS 12:	Recognition of deferred tax assets for unrealized losses (amendments)
IAS 7:	Disclosure initiative (amendments)
IFRS 2:	Clarifications of classification and measurement of share based payment transactions
IAS 40:	Transfers of investment property (amendments)
IFRS 4:	Application of IFRS 9 financial instruments and IFRS 4 insurance contracts
IFRIC 22:	Foreign currency transactions and advance consideration
IFRS 2014-2016:	IFRS 1, IFRS 12 and IAS 28 (amendments)

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

03.9

Group Notes to the Statements

(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.

The group of consolidated companies is stated in the following table:

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
Segment foreign sales		
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 statement 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 12.31.2016	Reporting date rates 12.31.2015	Average rates 2016	Average rates 2015
USD	1.0541	1.0887	1.1032	1.1046
CHF	1.0739	1.0835	1.0909	1.0646

03.9

Group Notes to the Statements

(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 reliably 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 are 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 balance sheet 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 from 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.

Long-term 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 that are stated at fair value on the reporting date with an effect on the operating result.

Other long-term assets

The other long-term 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:

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. 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.

03.9

Group Notes to the Statements

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 held at the Hermle Group for commercial purposes currently only apply in individual cases, and are therefore not of great importance.

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 balance sheet 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 balance sheet 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 balance sheet 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.

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.

03.9

Group Notes to the Statements

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 178 (previous year €k 398). The research and development expenses recorded directly as expenses were €k 11,991 (previous year €k 11,815).

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:

	2016	2015
	€k	€k
Share in profits from continued activities	331	317
Share in profits from discontinued activities	0	0
Share in other profit	0	0
Share in total profit	331	317
Aggregated book value as per 31.12.	1,012	999

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

(8) Other long-term assets

The item includes profit participation from life insurance policies. Also, in the previous year unused corporate tax credits from taxed equity (EK40) as well as long-term derivative assets were included.

(9) **Inventories**

The inventories are classified as follows:

	12.31.2016 €k	12.31.2015 €k
Raw materials, supplies and consumables	22,888	25,111
Work in progress	16,926	16,684
Finished goods and merchandise	13,100	13,148
Advance payments on inventories	633	806
	53,547	55,749

The book value of the inventories stated at net sales prices was €k 9,438 (previous year €k 7,269). The increase in the value adjustment for inventories recorded with an effect on profits was €k 28 (previous year: €k 431). Advances paid are stated as net amounts without turnover tax.

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

	12.31.2016 €k	12.31.2015 €k
Accounts receivable from trading		
due from third parties	58,563	49,846
due from other Group companies	77	69
	58,640	49,915
Other short-term receivables		
Derivative financial instruments	13	90
Tax refund claims	1,819	561
Deferred charged and prepaid expenses	802	928
Remaining other assets	1,496	1,353
	4,130	2,932
Total	62,770	52,847

The accounts receivable from trading and other short-term receivables with a residual term of more than one year was €k 880 (previous year: €k 1,470). 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.

03.9

Group Notes to the Statements

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

	Book value Total €k	Thereof: neither impaired nor overdue €k	Thereof: not value adjusted and overdue in the following time bands			
			<3 Months €k	3-6 Months €k	6-12 Months €k	>12 Months €k
Trade receivables 12.31.2016	58,640	28,013	6,010	1	0	0
Trade receivables 12.31.2015	49,915	30,926	6,944	927	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:

	2016 €k	2015 €k
Impairment at the start of the business year	6,130	7,066
Amount stated in income statement in the period under review	66	-842
Writing off receivables	-179	-483
Currency conversion effects	47	389
Impairment at the end of the business year	6,064	6,130

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:

	2016 €k	2015 €k
Expenses for the complete charge off of receivables	225	537
Income from the receipt of charged off receivables	16	7

(11) Securities and other assets

In the year under review, debt securities amounting to €k 10,610 (previous year: €k 26,007) are stated in this item. In the previous year, fixed-term investments with a term of more than three months were also declared.

(12) Cash and cash equivalent

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

	12.31.2016 €k	12.31.2015 €k
Cash in banks	120,974	101,056
Cash on hand	18	18
	120,992	101,074

(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.

In compliance with Section 16(3) of the articles of association of Maschinenfabrik Berthold Hermle AG, €k 1,000 (previous year €k 500) were newly allocated from the business year to the revenue reserves.

The annual general meeting is recommended to pay out the amount of €k 64,050 from the 2016 balance sheet profit of Maschinenfabrik Berthold Hermle AG amounting to €k 64,064 through the payment of a dividend amounting to € 12.80 per ordinary share and € 12.85 per preference share, and to carry forward the remaining €k 14 to new account.

In the 2016 business year a dividend of € 10.80 per ordinary share and € 10.85 per preference share was paid in respect of the 2015 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 2016 business year expenses (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 410 (previous year: €k 196). In addition, an amount of €k 237 (previous year €k 594) was withdrawn from the equity and recorded as income (previous year: expenses) in the periodical 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.

03.9

Group Notes to the Statements

(15) Provisions

	Status 01.01.2016 €k	Consumption €k	Resolution €k	Allocation €k	Other changes €k	Status 12.31.2016 €k
Tax provisions	4,058	3,782	108	2,673	1	2,842
Personnel provisions	12,783	11,719	73	13,323	26	14,340
Other provisions						
in marketing and sales	19,718	11,838	2,450	17,915	60	23,405
For other areas	1,040	719	151	874	4	1,048
	20,758	12,557	2,601	18,789	64	24,453
	37,599	28,058	2,782	34,785	91	41,635
Various short-term provisions	36,512	27,964	2,766	34,430	72	40,284
Various long-term provisions	1,087	94	16	355	19	1,351

The provisions in the personnel area largely apply to holiday and flexi-time 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.

The other changes comprised currency and interest effects totaling €k +91 (previous year €k +519). The effects from discounting and from changes in the discounting interest rate amounting to €k 39 (previous year €k 59) were attributable to personnel provision to the amount of €k 19 (previous year €k 19) and to €k 20 (previous year €k 40) to other provisions.

(16) Liabilities

The liabilities relate in particular to:

	12.31.2016 €k	12.31.2015 €k
Other long-term liabilities		
Derivative financial instruments > 1 year	65	0
Short-term trade accounts payable		
to third parties	7,625	7,975
due to other Group companies in which interests are held	841	696
	8,466	8,671
Other short-term liabilities		
Received advance payments	15,678	19,478
Derivative financial instruments	632	635
Liabilities from taxes	7,197	6,256
Liabilities for social security	308	183
Other liabilities	4,423	4,400
Deferred charges	1,079	1,056
	29,317	32,008
Classification of liabilities according to residual terms		
to 1 year	37,783	40,679
1 to 5 years	65	0
more than 5 years	0	0
	37,848	40,679

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.

03.9

Group Notes to the Statements

EXPLANATIONS ON THE INCOME STATEMENT

(17) Sales

The sales proceeds are broken down by region as follows:

	2016 €k	2015 €k
Federal Republic of Germany	160,242	147,891
Other countries	233,708	208,742
	393,950	356,633

(18) Other operating income

The other operating income item applies to:

	2016 €k	2015 €k
Income from the liquidation of provisions	2,692	3,174
Income from the liquidation of value adjustments	3,775	4,500
Income from investment disposals	291	1,315
Remaining other operating income	2,674	1,861
	9,432	10,850

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:

	2016 €k	2015 €k
Expenses for raw materials and supplies and procured goods	157,126	155,209
Cost of purchased services	13,801	12,601
	170,927	167,810

(20) Personnel expenses

Personnel costs include:

	2016 €k	2015 €k
Wages and salaries	68,818	64,641
Social security, pension and other benefit costs	11,479	10,759
	80,297	75,400

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

Average numbers of employees:

	2016	2015
Production employees	321	303
White-collar workers	596	576
Trainees	92	94
	1,009	973

In line with the resolution adopted at the shareholders' meeting dated Wednesday, July 6, 2016, the emoluments of the Board of Management are not stated individually but rather for the entire Board of Management. The board members' emoluments totaled €k 2,624. Of that total, €k 691 was attributable to basic salaries including passenger car use and direct insurance policies. In addition, the item contained performance-related elements of €k 1,933. 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 0 (previous year €k 0) was applied in the business year.

03.9

Group Notes to the Statements

(22) Other operating expenses

	2016 €k	2015 €k
Creation of value adjustments for receivables	3,640	3,186
Currency losses	303	3,552
Remaining other operating expenses	41,684	36,247
	45,627	42,985

The other operating expenses largely apply to expenditure for marketing, service and administration, rent and leasing installations 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 2016 auditor's fees of €k 161 (previous year €k 150) were recorded as expenses. In the 2016 business year, €k 0 (previous year: €k 0) were charged for tax consultancy services and €k 5 (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 331 (previous year €k 317) 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:

	2016 €k	2015 €k
Other interest and similar income	331	283
Interest and similar expenses	-151	-382
	180	-99

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

The taxes on income apply to:

	2016 €k	2015 €k
Ongoing taxes	26,749	21,457
Deferred taxes	-286	-20
	26,463	21,437

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:

	2016 €k	2015 €k
Result before income tax	100,312	80,618
Arithmetical income tax in %	26.50 %	26.50 %
Calculated income tax	26,583	21,364
Tax-free income	0	0
Non-deductible expenses	+46	+19
Other non-recurrent taxes	-104	-81
Amendment of tax rates	+26	0
Differences from tax rates and currency conversion	-65	+69
Losses carried forward not taken into account	-23	+66
Total tax liability	26,463	21,437

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.

03.9

Group Notes to the Statements

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

	12.31.2016 €k	12.31.2015 €k
Deferred tax assets		
Tax losses carried forward	0	0
Consolidation	446	364
Fixed assets	147	163
Inventories and receivables	912	880
Provisions	465	344
Liabilities	0	0
Derivative financial instruments	185	168
Other	0	0
Total	2,155	1,919
Offset against deferred tax liabilities	0	0
Total	2,155	1,919
Various items charged to equity without affecting the operating result	100	84
Deferred tax liabilities		
Fixed assets	62	121
Inventories and receivables	49	76
Securities	0	0
Provisions	25	38
Derivative financial instruments	4	37
Other	0	0
Total	140	272
Offset against deferred tax assets	0	0
Total	140	272
Various items charged to equity without affecting the operating result	0	29

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

Tax losses capable of being carried forward of €k 684 (previous year €k 772) 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 taxed equity (EK40) were capitalized to the amount of €k 251 (previous year €k 494).

(26) Result for each share

	2016 €k	2015 €k
Net income:		
According to income statement	73,849	59,181
Minority interests in result	-4	-2
Result after minority interests	73,845	59,179
Expired dividend preferences	-50	-50
Result after minorities and preference dividends	73,795	59,129
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	14.76	11.83
For each preference share including dividend preference	14.81	11.88

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 272 (previous year €k 69) and cash flows from taxes of €k -30,369 (previous year €k -20,196).

03.9

Group Notes to the Statements

(28) Segment reporting

For table see page 49

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 Board of Management.

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) Contingency liabilities and other financial obligations

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

	12.31.2016	12.31.2015
	€k	€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	495	595
due up to 5 years	471	459
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:

	Amounts stated in the balance sheet pursuant to IAS 39				Fair Value 12.31.2016 €k
	Book value 31.12.2016 €k	Updated acquisition costs €k	Fair Value affecting profits €k	Fair Value neutral effect on profits €k	
Assets					
Long-term assets					
Other financial assets	5			5	5
Other non-current assets	61	61			61
Current assets					
Accounts receivable from trading	58,640	58,640			58,640
Other short-term 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 equivalent	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 liabilities valued at updated acquisition cost	12,955				
Financial liabilities affecting the operating result valued at fair value	96				

03.9

Group Notes to the Statements

	Book value 12.31.2015 €k	Updated acquisition costs €k	Fair value affecting profits €k	Fair value on profits €k	Fair value 12.31.2015 €k
Assets					
Long-term assets					
Other financial assets	5			5	5
Derivative assets	50			50	50
Other non-current assets	77	77			77
Current assets					
assets	49,915	49,915			49,915
Other short-term assets	1,543	1,543			1,543
Derivative assets	90		29	61	90
Securities and other assets	26,007	22,998	3,009		26,007
Cash and cash equivalent	101,074	101,074			101,074
Liabilities					
Non-current liabilities					
Financial liabilities	0				0
Derivative liabilities	0				0
Current liabilities					
Trade payables	8,671	8,671			8,671
Other liabilities	4,393	4,393			4,393
Derivative liabilities	635		320	315	635
Of which aggregated by valuation categories as per IAS 39					
Loans and receivables	175,492				
Financial assets available for sale	5				
Financial assets held for commercial purposes	3,038				
Financial liabilities valued at updated acquisition cost	13,064				
Financial liabilities affecting the operating result valued at fair value	273				

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

	from interest/ dividends €k	from to fair value €k	from follow-up currency conver- sion €k	valuations: value adjust- ment €k	from disposal €k	2016 €k	2015 €k
Loans and receivables	378		-1,492	135	-225	-1,204	-1,734
Financial assets available for sale	0					0	0
Financial assets held for commercial purposes		-32				-32	-9
Financial liabilities valued at updated acquisition cost	-55					-55	-382
Financial liabilities valued at fair value		-96				-96	-273
Total	323	-128	-1,492	135	-225	-1,387	-2,398

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 Saturday, December 31, 2016, the Hermle Group has an above-average equity ratio in the sum of 74.3 %. On the balance sheet date, the amount of liquid funds and securities was €k 131,602. 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.

03.9

Group Notes to the Statements

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 with residual terms of less than one year, largely 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 approx. € 0.7 million (previous year: € 0.6 million). On account of the ECB policy, the risk from worsening interest rates is no longer limited to values of 0 %. To date we have not been affected by negative interest, but in 2017 further interest reductions could be passed on to bank clients to 100 % (previous year 50 %). 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 € -0.5 million (previous year € -0.3 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 entire 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 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, could already be too late for individual countries. In other cases, 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 balance sheet 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 balance sheet 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 Saturday, December 31, 2016 and Thursday, December 31, 2015, 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 2016, an income for the 2016 business year of € 0.4 million (previous year: income of € 0.4 million) would arise; in the case of a corresponding increase in value, a loss of € 0.5 million (previous year: loss of € 0.5 million). In the case of depreciation of the key foreign currencies by 5 % in 2016, the Group capital as per December 31, 2016 would decrease by € 0.1 million (previous year: increase of € 0.7 million); in the case of a corresponding write-up of the foreign currencies, it would increase by € 0.2 million (previous year: Decrease of € 0.8 million).

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

	12.31.2016 €k	12.31.2015 €k
Forward currency sales:		
Nominal volume	18,386	28,960
Various residual term > 1 year	1,423	2,296
Positive market values	13	140
Various fair value hedges < 1 year	(1)	(0)
Various fair Value Hedges > 1 year	(0)	(0)
Various cash flow hedges < 1 year	(12)	(90)
Various cash flow hedges > 1 year	(0)	(50)
Negative market values	697	635
Various Fair value hedges < 1 year	(250)	(56)
of which Cash flow hedges < 1 year	(382)	(579)
Various Cash flow hedges < 1 year	(65)	(0)

The market value corresponds with the profits and losses in the case of a notional settlement of the derivatives on the balance sheet 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.

03.9

Group Notes to the Statements

(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 balance sheet date

No events of note occurred after the balance sheet date.

(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 Board of Management 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 were €k 308 (previous year €k 318), while the proportionate deliveries and services procured from companies consolidated using the at equity method were €k 9,228 (previous year €k 8,276). On the balance sheet date, the Group receivables due from companies consolidated using the at equity method were €k 77 (previous year €k 69), while the Group liabilities due to companies consolidated using the at equity method were €k 841 (previous year €k 696).

The deliveries and services performed and rendered by the Group for other closely affiliated companies were €k 192 (previous year €k 141), while the deliveries and services purchased by the Group from other closely affiliated companies were €k 2,416 (previous year €k 2,583). On the balance sheet date, the Group receivables due from other closely affiliated companies were €k 2 (previous year €k 22), while the Group liabilities due to other closely affiliated companies were €k 285 (previous year €k 272).

(34) Declaration pursuant to Section 161 AktG

The Board of Management 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 Board of Management and the Supervisory Board. In that respect, the mandatory requirements were complied with in full.

The Board of Management 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 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 Board of Management 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 five years

4.2.1.: Board of Management made up of several persons

This declaration is permanently available to the public on the Hermle website at

https://www.hermle.de/de/investor_relations/pflichtveroeffentlichungen/kodex_161_aktg.

03.9

Group Notes to the Statements

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

The following persons form the Board of Management

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

The following persons form the Supervisory Board:

Dietmar Hermle, Chairman of the Supervisory Board

Entrepreneur, Spokesperson of the Board of Management of Maschinenfabrik Berthold Hermle AG to 31 March 2014

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 Board of Management of Südwestbank AG, Stuttgart

Other memberships of supervisory boards and controlling bodies:

Deputy Chairman of the Supervisory Board of KIWI Financial Living AG, Heidelberg, from April 21, 2016

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

Adolf Weber*

Chairman of the Works Council

Joachim Weber*, until July 6, 2016

Application Engineer

Gerd Grewin*, from July 6, 2016

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, Thursday, March 30, 2017
Maschinenfabrik Berthold Hermle AG

Günther Beck

Franz-Xaver Bernhard

Alfons Betting

03.10

Auditor's Report

Auditor's Report

We have audited the consolidated financial statement prepared by Maschinenfabrik Berthold Hermle AG, Gosheim, – comprising the balance sheet, income statement and overall income statement, equity statement, cash flow statement, and Notes to the financial statements – as well as the Group management report for the business year from January 1, 2016 to December 31, 2016, which has been combined with the company's management report. The preparation of the consolidated financial statement and summarized management report pursuant to IFRS, as adopted by the EU, and the additional commercial law requirements of Section 315a(1) HGB (HGB), is the responsibility of the Board of Management of the company. Our responsibility is to express an opinion on the consolidated financial statement and the summarized management report based on our audit.

We conducted our audit of the consolidated financial statements pursuant to § 317 HGB and the German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position, results of operations and cash flows in the consolidated financial statement pursuant to the applicable financial reporting framework and in the summarized management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. Within the framework of this audit, the effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statement and the summarized management report are examined primarily on a spot check basis. The audit includes assessing the annual financial statements of those entities included in the consolidation, the determination of entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management as well as evaluating the overall presentation of the consolidated financial statement and the summarized management report.

We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statement of Maschinenfabrik Berthold Hermle AG, Gosheim, for the business year from January 1, 2016 to December 31, 2016 complies with IFRS, as adopted by the EU, and the additional requirements of the German Commercial Code (HGB) pursuant to Section 315a(1) HGB, and gives a true and fair view of the net assets, financial position, results of operations and cash flows of the Group in line with these requirements. The summarized management report is consistent with the consolidated financial statement, complies with statutory requirements and as a whole provides an accurate view of the Group's position and adequately presents the opportunities and risks of future development.

Stuttgart, dated Thursday, March 30, 2017

BANSBACH GMBH
Auditors and tax consultants

(Hauser)
Auditor

(Wiedmann)
Auditor

04

Additional Information



Model making. Washbasin.



Model making. A hand washbasin for prototyping in aluminum.
Highly precise 5-axis simultaneous machining for a perfect finish.

04.1 Balance Sheet

of Maschinenfabrik Berthold Hermle AG

ASSETS	12.31.2016 €k	Previous year €k
Fixed assets		
Intangible assets	1,213	731
Property, plant and equipment	53,155	44,321
Long-term financial assets	3,401	4,341
	57,769	49,393
Current assets		
Inventories	50,156	52,295
Trade and other receivables		
Receivables	45,454	40,469
Other assets	6,701	4,838
Marketable securities	6,305	2,998
Cash on hand and cash in banks	81,201	86,814
	189,817	187,414
Deferred charges and prepaid expenses	308	317
TOTAL ASSETS	247,894	237,124
LIABILITIES		
Shareholders' equity		
Subscribed capital	15,000	15,000
Capital reserve	2,874	2,874
Revenue reserves	103,517	102,517
Balance sheet profit	64,064	54,497
	185,455	174,888
Provisions	35,709	33,578
Liabilities		
Financial liabilities	0	0
Other liabilities	26,076	28,043
	26,076	28,043
Deferred charges and prepaid expenses	654	615
TOTAL LIABILITIES	247,894	237,124

04.2

Income Statement

of Maschinenfabrik Berthold Hermle AG

	2016 €k	Previous year €k
Sales	360,894	329,152
Change in stock of finished and unfinished products	230	3,479
Other own work capitalized	140	2,143
Total turnover and operating revenue	361,264	334,774
Other operating income	7,093	7,714
Material expenses	165,991	162,474
Personnel expenses	66,519	62,767
Depreciation	5,585	5,490
Other operating expenses	43,565	39,185
Operating result	86,697	72,572
Financial and operating result	801	1,052
Earnings before taxes	87,498	73,624
Taxes on income	22,708	19,034
Earnings after taxes	64,790	54,590
Other taxes	173	100
Net income	64,617	54,490
Profit carried forward	447	507
Allocation to revenue reserves	-1,000	-500
Balance sheet profit	64,064	54,497

04.3

Proposal for the Appropriation of Profits

In accordance with Art. 16, Para.3 of the articles of association of Maschinenfabrik Berthold Hermle AG, the Management Board and Supervisory Board have resolved to allocate € 1,000,000.00 from the 2016 retained profit to the revenue reserves.

The Management Board and Supervisory Board propose to appropriate the remaining balance sheet profit on the 2016 business year of € 64,064,009.99 as follows:

Distribution of a dividend of € 12.80 for each ordinary share (€ 0.80 + € 12.00 bonus)

Security identification number 605 280 / ISIN DE0006052806
for 4,000,000 ordinary shares for the 2016 business year:

€ 51,200,000.00

Distribution of a dividend of € 12.85 for each preference share (€ 0.85 + € 12.00 bonus)

Security identification number 605 283 / ISIN DE0006052830
for 1,000,000 preference shares for the 2016 business year:

€ 12,850,000.00

To be carried forward to new account:

€ 14,009.99

Net earnings

€ 64,064,009.99

In accordance with Art. 58 Para. 4 Section 2 of the AktG (German Stock Corporation Act) in the version effective from January 1, 2017, claims to a dividend become due on the third working day following the resolution of the annual general meeting, i.e. on July 10, 2017. Therefore the dividend shall be paid out on July 10, 2017.

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, Wednesday, April 26, 2017

Maschinenfabrik Berthold Hermle AG

Günther Beck

Franz-Xaver Bernhard

Alfons Betting

04.4

Hermle Worldwide



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



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



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



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



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



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



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



Hermle Belgium
Belgium
www.hermle-nederland.nl



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



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



Hermle Polska
Warsaw Branch, Poland
www.hermle.pl



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



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



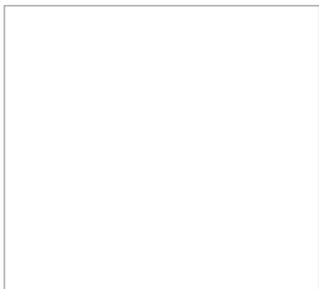
Hermle Vostok OOO
Moscow, Russian Federation
www.hermle-vostok.ru



Hermle Southeast Europe
Sofia, Bulgaria
www.hermle.de



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



Maschinenfabrik
Berthold Hermle AG
Industriestrasse 8-12
D-78559 Gosheim

Phone +49 (0)7426 95-0
Fax +49 (0)7426 95-1309

info@hermle.de
www.hermle.de

